China’s stimulus package threatens more economic turmoil

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When the Chinese government's huge stimulus package was announced last November, it was hailed in international financial circles as an effective measure to counter the global economic slump. An article in *Newsweek* last month declared that China, which has previously been described as an immature market economy and "command capitalism," was seen in the West as "a bulwark of stability".

Morgan Stanley Asia chief Stephen Roach told the magazine: "What we're seeing is that the Chinese command-and-control system can actually work more effectively than other market-based systems in the time of economic stress." Andy Rothman of CLSA commented: "Government control of the most capital intensive sectors leaves me optimistic about China's prospect. The government can say to companies in these sectors, ‘Continue to spend, don't defer your investment plans'."

Far from being in control of the economy, Beijing has fully embraced the free-market agenda of capitalism over the past three decades. Its ability to implement a 4 trillion yuan ($US585 billion) stimulus package is a product of China’s booming economy which is contracting as global demand dries up. Economic growth has halved since 2007 and exports have plunged. Instead of reviving the Chinese economy, there are signs that the stimulus measures are threatening new economic and financial turmoil.

In contrast to the continuing global credit crunch, bank lending is surging in China, jumping 21 percent in January from a month earlier. Much of the credit, however, is for short-term bills, rather than long-term loans for business expansion, and is fuelling speculation on the stock market. The Shanghai share market jumped 30 percent in the first part of 2009, the largest rise internationally, before diving again in the last week or so.

State bank lending increased by about 1.6 trillion yuan ($234 billion) in January, or one third of the total of new loans throughout 2008. According to the financial magazine *Caijing*, 500-600 billion yuan went straight into the stock markets, as companies have no confidence in their future prospects. Steep falls in imports in recent months, especially of components and capital goods, confirm that businesses are cutting production and axing plans for expansion. As a result, the impact of the stimulus package on fixed asset investment, which accounts for 40 percent of GDP, will be more limited than predicted.

The Chinese government is providing only 30 percent of the stimulus package, leaving the rest mainly to the state banks. In the midst of the financial crisis in the US and Europe, some senior officials have bragged about China's sound banking model. In fact, the state banking system accumulated huge quantities of bad debt during the past three decades through propping up failed state enterprises and financing infrastructure projects.

In 1999-2000, Beijing transferred 1.4 trillion yuan ($205 billion) in bad loans to state-run asset management companies (AMCs), effectively making the government liable. Some analysts warn that these AMCs are now insolvent because they have sold their better assets and face difficulties paying the interest and principal on the bonds they issued. Given that the government has guaranteed these bonds, Fitch Rating recently raised its estimate of the outstanding public debt in China from 18 percent of the GDP to almost 22 percent.

Provincial governments have announced their own stimulus packages totalling around 10 trillion ($1.5

trillion). But these measures are only creating internal political tensions as provinces tie their spending to protectionist measures aimed against their rivals.

Reuters reported that Anhui province has declared that car companies have to use steel produced within the province. From March, construction and appliance companies must source steel from the province's Ma'anshan Steel. From April, all power plants must buy from the province's four big coal miners, under the slogan of "Anhui power uses Anhui coal".

In Changchun city, in the northeast of the country, home to the FAW Group's joint auto ventures with Volkswagen and Toyota, government officials have been ordered to buy FAW cars. Building projects and other firms must source up to 50 percent of their new equipment locally. Farmers buying locally-made tractors receive additional subsidies of 10 percent.

Early last year, amid a booming economy and surging demand for power, many provinces banned the "export" of locally-mined coal to neighbouring provinces. Now amid a rapidly shrinking economy, provincial governments are engaging in "beggar thy neighbour" policies that can only lead to conflicts.

The working class is being forced to bear the brunt of the downturn. More than 20 million migrant workers have lost their jobs this year, with more to come, but the stimulus package is biased toward capital-intensive industry and will create relatively few jobs directly. With businesses folding and owners absconding, Beijing has proposed a new law to deter businessmen who disappear without paying wages, but it is unlikely to be enforced.

In Guangdong, non-payment of wages is rampant. Police in the free trade zone of Shenzhen reported that by the end of last year, 370 firms failed to pay 102 million yuan in wages to 39,200 workers. This month, 2,000 workers from the Italian-run DeCoro furniture maker blocked traffic in Shenzhen in protest at the factory's shut down. The protest was only ended when the local labour bureau paid 10 million yuan in outstanding wages.

The attitude of authorities prosecuting businessmen is already apparent. The Hong Kong-based *China Labour Bulletin* reported that the Guangdong provincial government last month specifically instructed its prosecutors not to arrest factory owners and senior staff suspected of commercial crimes, such as corruption or embezzlement, to avoid adding to the mounting toll of failed business.

In the case of the DeCoro closure, local authorities footed the bill for unpaid wages. However, the Chinese regime cannot pay the growing army of millions of laid-off workers. Its budget is already in deficit, due to falling tax revenues. This year's budget will have the largest-ever deficit of 950 billion yuan ($139 billion), far higher than the 280 billion yuan initially proposed and 9 times higher than the deficit in 2007.

Beijing's financial difficulties are being compounded by demands from Washington, emphasised during US Secretary of State Hillary Clinton's recent visit, that China keep buying US bonds. China already has around $700 billion in US bonds and fears large losses if the US dollar depreciates. Expressing the frustrations in Beijing, China Banking Regulatory Commission head Luo Ping, during a recent visit to New York, declared: "Once you start issuing $1-2 trillion [of bonds]... we know the dollar is going to depreciate, so we hate you guys, but there is nothing much we can do." If China stopped buying bonds, the dollar would fall even faster, the yuan would rise and Chinese exports to the US would suffer a further downturn.

Far from representing a new brand of "command capitalism," the Chinese regime, like capitalist governments everywhere, is powerless before the global economic meltdown. Its stimulus package to prop up the Chinese economy is fuelling new financial turmoil, economic difficulties and political tension, while offering little relief for working people. All this is creating the conditions for an eruption of political and social unrest.