IMF warning: European “storm” would halve Chinese growth

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The International Monetary Fund (IMF) has warned that a major recession in Europe could drag down China’s growth rate by as much as 4 percentage points, halving the projected 8.2 percent figure for this year. The prediction has underscored the acute vulnerability of the Chinese economy to the turmoil gripping European and global capitalism.

“A storm emanating from Europe would hit China hard,” the IMF office in Beijing stated in its “China Economic Outlook,” published on Monday. For years, the Chinese government has regarded an 8 percent growth rate as the minimal level needed to contain unemployment and prevent widespread social unrest. A fall to 4 percent or lower would be catastrophic for Beijing.

The IMF report provided some idea of the economic chain reaction that would follow in China: “Europe and United States account for nearly half of China’s total exports. Lower global demand would, therefore, feed back negatively to corporate and financial sector balance sheets, hampering the performance of firms in the tradable sector (where excess capacity is already prevalent), increasing NPLs [non-performance loans], and potentially prompting banks to deleverage. This would further reduce investment, employment and growth and could trigger a decline in China’s property market.”

In the aftermath of the global financial meltdown in late 2008, more than 20 million of China’s workers lost their jobs, mainly in export industries, threatening to spark a social explosion. The deepening crisis in Europe could set off even greater shocks.

Although the IMF emphasised that the 4 percentage-point decline would occur only “in the absence of a domestic policy response,” the Chinese regime is in no position to react as it did to the last shock in 2008. Beijing had to unleash a huge stimulus package and a flood of credit that, according to the IMF, boosted growth by at least 6 percentage points. Even so, China’s growth rate still slid by nearly 5 percentage points, from almost 11 percent to 6 percent in early 2009.

The latest IMF warning again highlights the basic character of Chinese capitalism: that of providing the global transnational corporations with a cheap labour platform, with narrow profit margins. It is also highly dependent on the major developed economies for markets, investment and technology. Its vast factories are part of the global supply chain for the transnationals.

Throughout Asia as well, many economies have become dependent on China as their largest export market of intermediate goods which are then used to manufacture products for re-export. Reflecting fears of the potential fallout for these countries, Singapore’s Prime Minister Lee Hsien Loong warned last weekend that China was heading for a “rough landing.”

China’s exposure to a European “storm” was further underlined by Chinese Premier Wen Jiabao’s talks with visiting German Chancellor Angela Merkel last week. Wen promised to “be more deeply involved” in resolving the European debt crisis by tapping into its $3.18 trillion foreign currency reserves.

Wen argued that it was in China’s “national interests" to do so, but no concrete measures were announced. Speaking in Guangdong, the country's export hub, Wen stated: "On the one hand, our largest export market is Europe. On the other hand, Europe is our biggest source for importing technology."

Beijing is currently struggling to deal with the consequences from slowing property prices. According to data gathered by Reuters on Wednesday, major Chinese steel companies have accumulated at least $400 billion in debts, and they could face repayment difficulties because of slowing construction and manufacturing activities.

China's stimulus package in 2008-09 only compounded the economy's contradictions. Much of the cheap credit went into property speculation, essentially because of the lack of profitable returns available from investing in production. As a result local government and industry groups have enormous debts and are highly vulnerable to any collapse of property prices.

Of the 10.7 trillion yuan ($1.69 trillion) in loans that local governments had incurred by the end of 2010, it is estimated that some 20-30 percent could become bad debts due to poor investment returns in infrastructure and property projects.

Moreover, Beijing's previous stimulus package has exacerbated a looming crisis of overproduction by spurring fixed asset investment, largely in industrial projects and infrastructure. Last year, China invested 40 percent more fixed capital than the US, but its consumer spending was only one-fifth of America's.

The IMF called for a shift from dependence on investment to personal consumption, which would supposedly "re-balance" the Chinese economy. But that would necessarily involve lifting real wages for the working class. It would also require providing an effective social safety net to replace the basic services—everything from housing to healthcare—that were eliminated along with many state enterprises in the 1990s during the process of restoring capitalism.

The IMF noted that urban household saving rates had increased from 19 percent of disposable income in the mid-1990s to 30 percent in 2009. Yet much of this relates to necessary saving for emergencies, such as a huge medical bill. In turn, these savings provide capital for the banks to supply cheap credit to industrialists, all in order to exploit the army of cheap labour.

There is acute concern in the ruling class internationally about the prospect of explosive class struggles in China. An article in the London-based *Financial Times* last Sunday warned that the Chinese police force was "ill-equipped to combat unrest." It noted that police numbers had increased from 863,000 in 2003 to some two million in 2010, but remained "low" on a per capita basis compared to the world average.

"Despite a steep ramp-up in spending on internal security, riot control forces remain stretched thin, and structural problems continued to plague the security apparatus," the article noted. In other words, Beijing must urgently expand its already massive apparatus of repression to prepare for a feared eruption of the Chinese working class.