Stimulus measures ease slowdown in Chinese growth

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The Chinese government reported Friday that the nation's economy grew by 6.7 percent in the first quarter of this year, the lowest quarterly result since the beginning of 2009. The figure was in line with the government's target of growth between 6.5 percent and 7 percent, but it was achieved only as a result of stimulus measures that boosted housing and infrastructure spending.

While the growth data eased immediate concerns of a rapid slowdown in the Chinese economy, there are warnings that the government's measures mean an increase in debt and an easing in the pace of so-called "financial reform" demanded by the West.

The increase in debt was reflected in figures showing that the total stock of financing in the economy, including the issuance of bonds by local government, increased by 15.8 percent in the year to March from the year ago, the fastest rate in two years.

The impact of stimulus measures was reflected in monthly production data, issued at the same time as the quarterly GDP numbers. They showed fixed asset investment growth of 10.7 percent in the year to March, ahead of expectations and the highest level since August last year. Industrial production rose by 6.8 percent, its fastest pace for nine months.

One of the key drivers of the increase in investment was a pick-up in the property market, especially in the large cities, where sales rose by 33 percent in the first three months, the biggest increase in two years.

Cornell economics professor Eswar Prasad, former China head at the IMF, said the new macroeconomy data "painted a picture of an economy that has lost some growth momentum but lives to fight another day." The data appeared to repudiate the "excessively pessimistic" view about China in financial markets earlier in the year, "although there is still plenty of ammunition for pessimists to maintain their negative outlook."

Other commentary on the growth figures focused on the impact of government measures. The managing director and vice-chairman for Asia Pacific at JPMorgan Chase, Jing Ulrich, told CNBC that the economy was recovering from the lows experienced last December and January. "That shows that the government measures, which they introduced in recent months, are beginning to have an effect," he said.

The "weak spot" was the decline in the total value of exports and imports, which are down by 5.9 percent in the first quarter compared to a year ago, reflecting weaker global growth, which is impacting Chinese trade.

The Asia economist at the Economist Intelligence Unit, Tom Rafferty, said the growth figures represented only a "temporary respite" for the economy. The data "ought not to distract from the fact that the structural issues facing China's economy remain unresolved," he said. "It has taken considerable monetary and fiscal loosening to stabilize growth at this level and this effort has distracted from the reform agenda that is fundamental to long-term economic stability."

Central to the "reform agenda" is the closure of unprofitable enterprises, with the loss of millions in jobs in basic industries, and the reduction of debt.

The International Monetary Fund's *Global Financial Stability Report*, issued earlier this week, warned that declining growth and profitability had led to a rise in the share of debt held by Chinese firms that do not earn enough to cover their interest payments. This category is now 14 percent of the total debt of Chinese companies—more than triple the level in 2010.

Chief China economist at JPMorgan in Hong Kong, Zhu Haibin, told the *Financial Times* that corporate

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debt was “alarmingly high.”

“If credit growth continues to be very strong, while at the same time we don’t see a concrete plan to deal with ‘zombie companies’ such as bankruptcies and writing off bad loans, then the situation may get worse,” he said.

There is also considerable scepticism about the accuracy of the figures, with some analysts claiming the real Chinese growth rate is closer to 4 percent. An index based on data on electricity usage, rail cargo volumes and bank lending showed a drop of 13 percent in the first quarter.

The president of China Beige Book International, which monitors Chinese growth data, Leland Miller, said the basic trends were lower investment and rising layoffs. The latest data indicated that the Chinese government had decided to slow down reform and restructuring. “It means that they’re taking more debt and they’re putting off their problems for longer,” he said.

While the speed of the slowdown has moderated, its continuation, as reflected in the decline in trade figures, will further impact the global economy as a whole and the Asian economies in particular.

Japan is being adversely affected. While the Chinese and global slowdown has cut Japan’s export markets, it has also had the effect of bringing down the value of the US dollar, with the Fed, citing international conditions, backing away somewhat from its program of interest rate hikes. As a result, the dollar has ceased its rise in international markets, leading to an increase in the value of the yen and making Japanese products less competitive.

This movement has dashed the hopes of the Bank of Japan and the Abe government that the central bank’s negative interest rate regime, introduced at the end of January, would see the value of the currency fall. Instead, it has moved sharply in the opposite direction.

The *Financial Times* reports that Japanese Finance Minister Taro Aso told US Treasury Secretary Jack Lew, during discussions at the IMF meeting in Washington, that he was “gravely concerned” by the surge in the value of the yen.

According to the report, Japanese officials were met by “firm warnings” not to devalue the currency, following commitments made at the G20 meeting earlier this year that governments would not target exchange rates, lest this set off a “currency war.”

That agreement is coming under increasing strain. Aso said his message to Lew was that “extreme and disorderly movements in foreign exchange markets have a negative effect on the economy, and I’m gravely concerned by recent one-sided moves.”

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