# Deflation starts to grip the Chinese economy

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Most of the world is experiencing inflation at the highest rate in four decades. In China the opposite is the case, with the country entering a deflationary environment. However, this is not a sign of economic strength and stability but may portend a significant fall in economic growth.

After a brief increase following the lifting of all anti-COVID measures at the end of last year, the much-anticipated post-COVID "recovery" has failed to materialise.

Data released by the National Bureau of Statistics on Monday showed that the consumer price index was unchanged from a year ago—the lowest rate in more than two years. At the same time, factory gate prices continued to fall, an indication of lowered demand.

Producer prices for June were down by 5.4 percent from a year ago in the steepest decline since December 2015.

In its report on the data, the *Australian Financial Review* noted: "Producers have already spent months contending with lower commodity prices and weak demand at home and abroad. If consumers and businesses continue to hold back from spending or investment in the hopes of prices getting lower that could lead to a self-fulfilling price dropping spiral."

If present trends continue, and there is no sign of their abatement, this could call into question the government's target of 5 percent growth for the economy this year.

This has led to speculation that the People's Bank of China could further cut interest rates and ease monetary policy. However, any stimulus will be nothing like what was carried out in the past.

Bloomberg economist David Qu told the AFR: "Zero consumer price inflation and deeper falls in consumer prices in June suggest China's post-COVID rebound has lost more steam. Flagging momentum on the price front is a sign of weak demand that clouds the economic outlook. The need for more stimulus from the People's Bank of China is rising."

The last time China experienced a sustained period of deflation—there was a short period of price declines in early 2021—was in 2009 as a result of the global financial crisis that erupted in 2008.

The government introduced a major stimulus package, estimated to be around $500 billion, combined with an increase in credit to finance major infrastructure and investments. That is not going to be repeated because the earlier stimulus led to a large increase in debt, particularly by local government authorities.

The government and financial authorities are trying to cut back the expansion of debt, not least because of the problems in the real estate and property sector exemplified by the crisis at Evergrande in 2021 and other companies.

The ongoing economic war being conducted against China by the US, with its bans on the export of advanced chips needed for high-tech development and the push for US firms to get out of China—the drive for decoupling or "derisking"—is leading to a lack of investor confidence, further lowering the prospects for economic growth.

The Chinese government is making noises about the possibility of stimulus, but that is very much all they are at present.

China's Premier Li Qiang, as reported by the state-run news agency Xinhua last week, indicated the government was planning measures to deal with lower growth.

"Targeted and co-ordinated policy measures should be introduced and implemented in a timely manner to stabilise growth, ensure employment, and guard against risks," he said.

Li gave no details about what those measures might be. They could include some relaxation of monetary

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policy and reduction of business taxes, however such measures will only have an impact at the margin and will not lead to a new growth path for the Chinese economy.

Bruce Pang, chief economist at the real estate and investment management firm Jones Lang Lasalle, said it was "very unlikely" that the Chinese government would introduce major macroeconomy measures as it was emphasising high quality growth that is stable and would not lead to risks.

While the government is anxious to avoid financial risks, threats are increasing on the social and political fronts. The stability of the government rests on the belief that, even though it long ago abandoned any real commitment to socialism and genuine equality, its program of capitalist development will bring rising living standards, above all for young people.

It is here that the economic slowdown, which began before COVID struck, is having a significant impact as revealed in the rise in youth unemployment in the urban centres.

In May, some 20.8 percent of youth aged between 16 and 24 were unemployed, the highest rate since data started to be collected in 2018. Many of them have come onto the jobs market after completing university degrees costing 30,000 yuan a year—around a fifth of the average annual income for a family of three—to find there are only low paid jobs available.

According to a recent report in the *Financial Times* entitled "China's youth left behind as jobs crisis mounts," the government has responded with a campaign directed at graduates to "find a job first and then choose a career." President Xi Jinping has told young people to "ask for hardship" when seeking employment.

China's overall urban unemployment rate has remained stable at around 5.2 percent. However, the available jobs are low paid and not able to attract university graduates who anticipated greater remuneration after years of intense study at considerable expense for their families.

Youth have always played a powerful role in the struggles of the Chinese working class and there are predictions they could do so again.

A recent report from the China Macroeconomy Forum think-tank, cited in the FT article, indicated that youth unemployment was not a passing phenomenon.

"We estimate that the problem of youth unemployment may continue for 10 years in the future and continue to worsen in the future," it said.

"If handled improperly, it will lead to further social issues outside the economic field and even become the trigger for political issues."

That was the case in 1989. The repression of students at Tiananmen Square in June 1989 was only the most public expression of a wave of attacks on the working class.

After three years of debate and conflict within the ruling Communist Party, the turn was made to the full-scale development of capitalism. There was an acceleration of economic growth and a rise in living standards, leading to the claims by the regime that the "peaceful rise" of China within the framework of capitalism was possible.

Now China has run into two interconnected obstacles: the determination of the US to suppress its economic advance and the exhaustion of the methods used to promote growth in the past amid a deepening crisis of global capitalism.

The CCP regime used to maintain that at least 8 percent growth a year was necessary to maintain "social stability." Now the official growth target is well below that level and could fall even further as a well-educated cohort of millions of young people enter the working class and confront the contradictions of the capitalist economy and the actions of US imperialism.

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