Mounting economic problems for Chinese government

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The National People's Congress (NPC) is always an important event in the Chinese political calendar, not because it involves genuine debate and discussion of policy, but because it is where the leadership of the government lays out its agenda for the year.

This year's congress, which begins on March 5, will be particularly significant because the Xi Jinping regime confronts a worsening economic situation with no sign of a turnaround in sight.

In broad terms, it comprises: the onset of deflation, a fall in the stock markets and worsening problems in the housing and real estate sector which contributes around 25 percent to the growth the economy.

On top of this there is the deepening economic offensive by the Biden administration, coupled with ever more overt military preparations and the recent threat by Donald Trump that he would impose a 60 percent tariff on all Chinese goods should he become president again, a very real possibility.

This time last year the government was banking that its lifting of zero-COVID public health measures would provide a "boost" to the economy even as it knew that millions would die. The deaths came—numbering up to 2 million—but except for a brief uptick in the early months of last year, the hoped-for economic revival did not.

The clearest expression of the economic downturn is the tightening grip of deflationary forces. Data published earlier this month showed that consumer prices had fallen at their fastest rate in 15 years in January, down by 0.8 percent year on year.

In was the fourth straight monthly fall and the largest decline since 2009 in the wake of the global financial crisis which led to the loss of 23 million jobs in China.

Numbers of economists have warned that a series of economic indicators are "flashing red" and that if deflation is prolonged it will undermine consumer and business confidence, creating a feedback loop in which falling expenditure creates further deflationary pressures.

Deflation of consumer prices started last July with prices either flat or lower in every month, with the exception of August, since then. The fall in producer prices, those charged at the factory gate, has been even more marked. They declined every month last year and were down by a further 2.5 percent in January.

At the NPC, incoming Chinese premier Li Qiang will deliver his first government work report, setting out the government's growth target, its deficit projections, and the overall direction for economic, social and foreign policies for 2024.

The growth projection will be carefully scrutinised amid conjecture that the government's figures are overstated. Last year's growth was 5.2 percent, slightly above the target of 5 percent—the lowest level in three decades. There is considerable doubt as to whether growth in 2024 will even be able to reach that level.

In the recent period, the government has rolled out some measures to boost the economy. But they have been described as piecemeal and far short of what is needed.

One of the main problems facing economic policymakers is the crisis in real estate and property development.

Since 2021, more than 50 Chinese property firms have defaulted on their debts, including two of the biggest, Evergrande and Country Garden. Evergrande was put into liquidation by the decision of a Hong Kong court at the end of last month and Country Garden, which had been touted as secure firm in contrast to Evergrande, defaulted last October.

According to a report in the *New York Times* (NYT), published at the end of last month, the downturn in property, “already the longest record, is not only dragging on—it is accelerating.”

China’s housing sales were down 6.5 percent for the year and in December plunged by 17.1 percent compared to the same month a year earlier.

In an indication of how precipitous the fall has been, Country Garden reported that presales of unfinished apartments fell for the ninth straight month in December and were down 69 percent from the year before.

Throughout the sector the completion of homes which have been paid for, either in full or in part, is a major problem as the companies building them run out of money.

The NYT article cited calculations by the Japanese financial firm Nomura which estimated there were 20 million presold units waiting to be finished that would require $450 billion in funding to be completed.

The government is trying to pressure financial institutions to come up with loans to property developers. Last month, Xiao Yuanqi, deputy director of the National Regulatory Administration, said they had an “inescapable responsibility to provide strong support” for the property sector. They should not cut off loans for projects in trouble but should find ways of supporting them.

But this injunction only points to the contradictions in government policy. The downturn in property and real estate, which has found its sharpest expression so far in the fate of Evergrande and the troubles at Country Garden, was set off in mid-2020 by the government decision to order the tightening of credit known as the “three red lines.”

This was prompted by fears that the growth of debt was unsustainable and would lead to a financial crisis if it continued and a decision that it was necessary to move away from the growth path based on real estate and infrastructure construction.

A note issued by Larry Hu, chief economist for the Macquarie finance group, cited in the NYT article, pointed to the vicious circle now at work. The debt problems of the property developers kept buyers away, fearing they will not get delivery of their home, while the fall off of new business only worsened the developers’ financial problems.

Echoing calls by others for the government to step in with a “big bazooka,” he said the main thing to watch was whether the government would intervene to stop the contagion by bailing out companies. Hu said the Chinese authorities should consider something like the Troubled Asset Relief Program (TARP) developed in the US in response to the financial crisis of 2008.

A further complication is the fall in the stock market which, despite some temporary boosts as a result of government interventions, is continuing. Last month, the day after premier Li Qiang called for “forceful” measures to halt the stock market slide, more than 40 percent of attendees at a Goldman Sachs conference in Hong Kong said in a survey that they considered China to be “uninvestible.”

The government is clearly concerned by the slide which has seen the benchmark MSCI down by more than 60 percent from its peak in early 2021. Earlier this month the chair of its securities regulator was removed. No official reason was given but it was clear he was axed because of the slump in the market.

And unless there are some major initiatives by the government, the slide in the economy and the stock market looks set to continue.