

China announces package for debt-ridden local governments

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The Chinese government has announced a \$1.4 trillion plan to assist local government authorities to more slowly pay off their massive debts. Its hope is this might free up money for spending and provide a boost to the Chinese economy as it confronts the lowest growth rates in more than three decades.

The decision, which came at the end of a four-day meeting of the Standing Committee of the National People's Congress on Friday, consisted of two parts. Local governments were allocated additional government borrowing of about \$838 over three years with a further \$539 billion over five years.

The plan was not so much a bailout for local governments as a debt swap. It will enable them to bring so-called “hidden debt,” which is not officially recorded as it is carried out off balance sheet by entities known as local government financing vehicles [LGFVs], onto their books.

The money raised by LGFVs has been used to finance investment in infrastructure and real estate, paid off with money raised from land sales.

This mechanism has been responsible for much of the growth in the Chinese economy over the past decade and a half, with real estate, construction and related industries, often financed by local governments, estimated to have accounted for around 25 percent of GDP.

But the real estate sector faces a crisis, which began around 2021 and has seen major companies, such as Evergrande, collapse, as well as a host of smaller ones, leading to a fall in land sales. This has hit local government revenue to such an extent that some have fallen behind in paying the wages of their employees.

Announcing the new measures, finance minister Lan Fo'an said the plan would replace \$1.4 trillion of “hidden debt,” which he put at \$2 trillion at the end of

2023.

Calculations by private economists, however, say it is much higher—somewhere between \$7 trillion and \$11 trillion. The International Monetary Fund has estimated it to be \$8 trillion.

Whatever the exact number, it has been increasing rapidly. According to analysis by Victor Shih, a specialist in Chinese finance and politics at the University of the California, cited by the *New York Times*, the debt level of most local governments has doubled between 2018 and 2023.

He said the measures would save local governments only about \$84 billion over the next five years and was an “accounting exercise” which did “nothing for a real economy.”

His overall assessment was that while a large sum of money was involved “it is still basically kicking the can down the road.”

Wang Tan, chief China economist at the Swiss bank UBS, also cited in the *Times* report, held a similar view. She said that while the measures helped reduce debt service payments over the next few years, they did “not solve the local government debt issue.”

Economists at the ANZ bank also pointed out that the measures did not actually pay down the debt but simply pushed their maturity dates into the future and that the economic impact of what amounted to a debt swap would be indirect and almost imperceptible.

Presenting the plan, Lan said money saved by governments on interest over the next five years (around 600 billion yuan) would free up resources to boost investment and consumption.

He said the package was a “major policy decision taking into consideration international and domestic development environments.”

The most significant factor in the “international

environment” is the election of Trump to the US presidency which took place as the Standing Committee was meeting.

Apart from continuing and deepening the high-tech bans on China which he initiated in his first term, and which were significantly intensified under Biden, Trump has said he will impose a 60 percent tariff on all goods coming from China—a major increase from the present levies which average around 12.5 percent.

According to a *Wall Street Journal* report, economists at UBS estimate that a tariff of 60 percent could reduce the Chinese growth rate by as much as 2.5 percentage points in the 12 months after they come into force.

This is in conditions where the growth rate fell in the September quarter to below an annual rate of 5 percent, which is the official government target for 2024.

The Standing Committee meeting was keenly anticipated to see if there were any measures aimed at boosting the domestic economy. It is characterised by low consumption spending, lower investment, except in high-tech areas which are supported by the government, and continued deflation such that many industrial enterprises are struggling to make a profit, or are even experiencing losses.

Measures undertaken in September and October that loosened financial conditions did provide a 20 percent boost to the stock market, which has been in significant decline, but were not aimed at the real economy.

And Friday’s package was not either.

However, given the threat to growth posed by the Trump administration, the Xi Jinping government may be forced to take some action because its greatest fear is that a further major slowdown in growth will lead to “social instability,” that is, an eruption of class struggle.

In his press briefing, Lan said there would be a “more forceful” fiscal policy next year. He said the government was “studying” additional measures to recapitalise major banks, buy unfinished property developments and lift consumption.

“We are planning the next phase of fiscal policy and are intensifying countercyclical adjustments,” he said.

The next major meeting of the Chinese leadership is set to take place in December when the 24-member Politburo will discuss the economy. According to some estimates, additional spending of 12 to 13 trillion yuan (around \$1.8 trillion) is needed just to counter the effect

of US tariff hikes.

Whether a decision is made there will depend on how far advanced US plans are for the tariffs to which Trump committed himself at various times in his election campaign.

Pointing to the absence of any stimulus measures in Friday’s package, the WSJ noted that this absence pointed to “Beijing’s desire to hold some dry powder in reserve should trade tensions with the US intensify.”

Considering the central role played by tariffs in Trump’s election campaign, where they were held out as the solution to nearly all the economic, and even social, problems confronting the US, such an intensification is likely to come sooner rather than later.



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