



Slower Growth and Continued Stability in China

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April 2, 2019

PIIE



GDP Growth: Closer to 6% than 6.5%

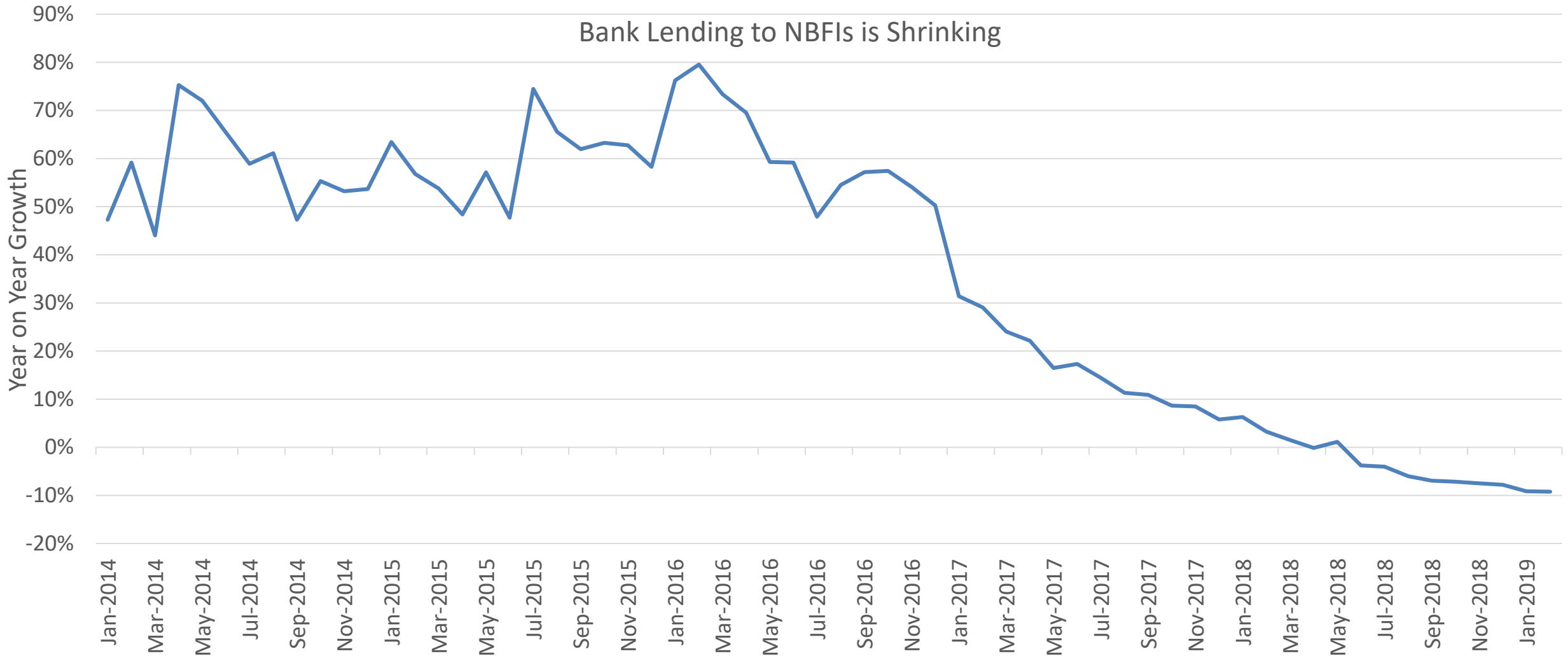
Success in restraining credit growth & shadow banking suggest continued financial stability

Challenge this year: restoring credit to private sector needed to sustain growth

Limited prospects for large scale monetary/credit stimulus

Expecting 2019 growth on lower end of government target

Success : slower credit growth and shift away from shadow banking

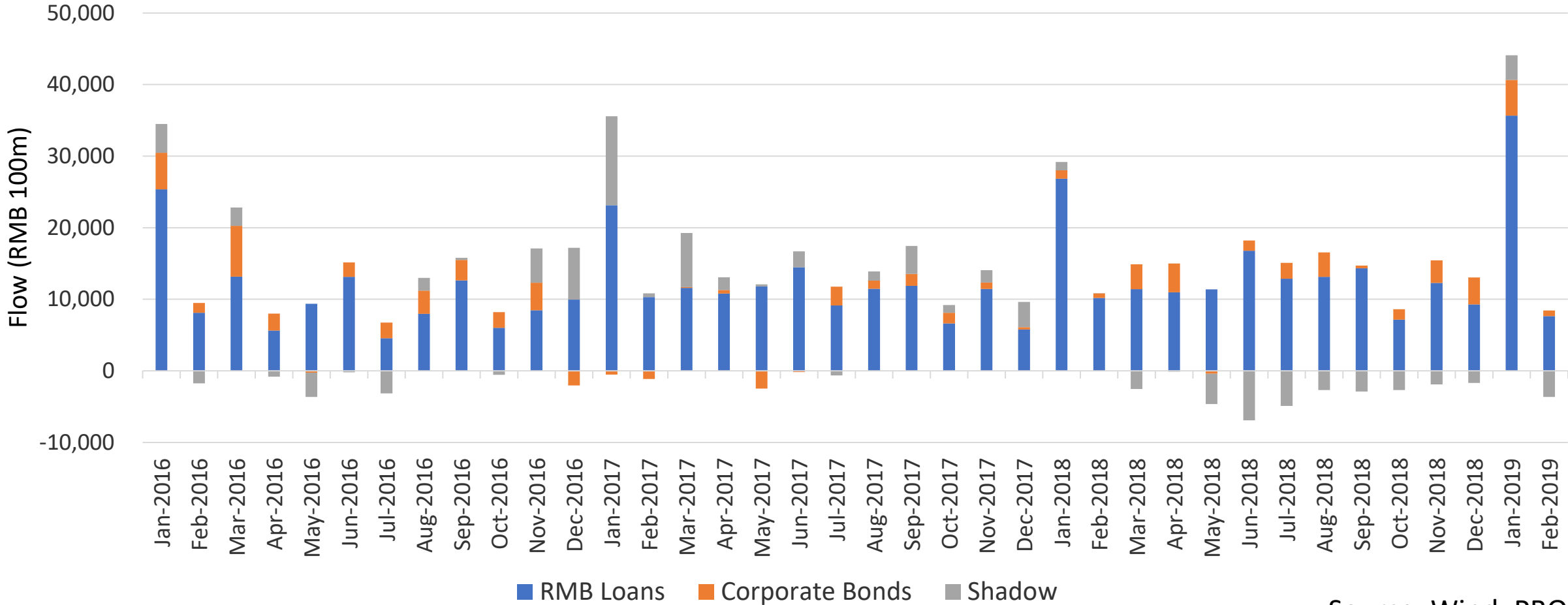


Source: Wind, PBOC

Success : slower credit growth and shift away from shadow banking



Shadow Banking is Shrinking



Source: Wind, PBOC

More Difficult: Credit to Private Sector and Small Companies



SOEs are growing on easy bank credit

- One of the “two unswervinglies” (bigger state companies) is more unswerving than supporting private business

Hard to end “one country, two financial systems”

- Shadow banking crackdown mostly hit small, private firms
- P2P collapse alone withdrew over 500 billion RMB in credit

Banks have not picked up slack: de-risk or lend to small firms?

- Private sector was only around 1/3 of bank loans in 2016
- Micro and small enterprise lending unlikely to hit 30% growth target
 - Big 5 state banks *reduced* by 320b RMB in 2018
 - Overall growth of 9% was *down* from 15% in 2017





Prospects for Stimulus

Rising tension in policy apparatus spilling into public view

- July 2018 PBOC/MOF spat over fiscal policy
- February 2019 Li Keqiang/PBOC disagree on Dec. credit growth and shadow banking resurgence

Credit Stimulus: fewer levers available

- Premier promises “no flood” of credit
- Issues with monetary policy transmission mechanism (e.g. not want flow to real estate or local governments)
- Adjusting credit composition rather than deleveraging
- Hard line on shadow banking may reverse somewhat in 2H 2019

Fiscal Stimulus likely to be limited in effects

- Gov deficit up to 4.3% of GDP
- Tax cuts, but stepped up enforcement by squeezed local governments will muddle effects



Outlook

2019-2020

- Trade resolution with US could boost sentiment and trade
- Expect some loosening on shadow banking
- Continued data-dependent balance of financial risk reduction with floor on growth

Medium-term: challenges point to continued slowdown

- Focus on employment reduces probability of hard SOE reforms that would boost productivity
- Need long-term solution to local government financing imbalance (property tax?)
- Technology competition with US not going away