



## China's Economy Shadows the Obama-Xi Summit

*Nicholas R. Lardy discusses China's economic difficulties and other issues likely to come up when Presidents Obama and Xi Jinping meet.*

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Steve Weisman: President Xi Jinping of China arrives on September 24th for an important Summit Meeting with President Obama. Some of the issues they will be discussing are political, some economic.

This is Steve Weisman of the Peterson Institute for International Economics with Nick Lardy of the Institute to talk about the economic aspects of the visit.

Nick, thanks for joining us. What are the major economic issues likely to come up?

Nicholas Lardy: Well, I think there are a range of issues. They might be able to announce some progress or semi-conclusion of a bilateral investment treaty that they had two rounds of negotiations recently. They made some progress although the details aren't really available yet.

I would not be surprised if President Obama raises with President Xi the whole question about what's the trajectory of Chinese economic growth. The whole question of how reliable are the data, how timely are they, how accurate, and there's been a lot of global reaction based on the assumption that the economy is slowing down quite a bit. And, I think, he might ask for more clarity on that as well as the broader issue of how are they doing on the reform agenda that they laid out a couple of years ago at the so-called 3rd Plenum. How strong are they going to be on the reform of state-owned enterprises and a range of other issues.

And, I think, he will raise some of the issues that are of specific concern to some sectors in the US economy particularly technology firms. China has adopted a number of policies recently that would appear to disadvantage American firms in the Chinese marketplace and I would expect that that would also be a subject for discussion.

Steve Weisman: That's not a small agenda. Let's talk first about the Chinese economy. The markets and policymakers are worried that the Chinese economy is really going down, is swooning. What's your latest analysis?

Nicholas Lardy: Well, I think the problem is we don't get enough high frequency data for the most important part of the Chinese economy, which is the service sector, which now accounts for half of the total economy. And the Chinese give us very frequent data on the industrial sector and industrial output has been declining but it's been declining since 2010 almost continuously. So the real question is whether or not the service sector is growing fast enough to partially offset that and given the lack of high frequency comprehensive data on the service sector, it's very hard to make a judgment on that.

Steve Weisman: Now, American concerns about Chinese manipulation of its currency have been on the agenda for years and years and there are some people in Congress that are still worried about that although the administration has not so much raised that recently, how is that going to factor into the discussions?

Nicholas Lardy: I think it would be, at most, a very secondary subject that might be alluded to or discussed in passing. China has basically done what we've been asking them to do for years so there might be an opportunity for President Obama to give a recognition that they're moving in the right direction in terms of adopting policies that will, over time, lead to a more market determined exchange rate.

Steve Weisman: Let me come back to the Bilateral Investment Treaty or BIT. Tell us what is it and why is it so important?

Nicholas Lardy: Well, this would be a treaty that would be approved by the Senate eventually that would open up large parts of China that have currently, up till now, been off-limits or subject to immense restrictions in terms of investment by foreign firms.

This is particularly in financial services. They opened up quite a bit in 2001 when they came into the WTO but the world has moved down a great deal in terms of financial services since then. And there are a lot of restrictions on ownership whether it's in securities, insurances, asset management. The US and other foreign firms can't operate their own businesses there, they have to partner up with Chinese institutions. Telecommunication is another area that's quite closed.

The most important parts of the economy that would be opened up on a very liberal investment treaty would be in the services sector so financial services, telecommunication services, value added telecommunication services would be opened up to foreign investors.

Steve Weisman: The Chinese, of course, are concerned fairly or not that in their view the US is not open to Chinese investment as much as they would like. Has there been progress on that aspect of the discussions?

Nicholas Lardy: It's hard to tell, but I think the opportunity for progress is pretty limited because we have a very open investment environment, very few restrictions. There are some restrictions on airlines and a few other things like that but they're quite small compared to the restrictions that exist in China.

And what the Chinese really object to the most is this Committee on Foreign Investment in the United States, which has to examine many investment transactions particularly if a State company is involved from the Chinese side. And that's a fairly opaque process that the Chinese still don't really understand very well and that there have been a few well-publicized examples where deals have not been approved and the Chinese in practice would like to see some revisions in that process.

It is very unlikely that that can be accomplished because that whole process was set-up by the Congress and I don't think they're in the mood to make adjustments to deal with Chinese sensitivities.

Steve Weisman: Let me ask a final question about the atmospherics. With all of the publicity over the last six months over the Chinese Stock Market problems and other aspects of the economy, other signals that some parts of it are slowing down as you mentioned earlier. There's a lot of talk that somehow President Xi has lost the spring in his step and that he comes to this visit not as confident about China's economic power as he might have been last year, what would be your assessment of that sort of talk?

Nicholas Lardy: I think that's probably a correct assessment. I think now that some time has gone by even within China they recognized that their attempt to slow down the correction in the Stock Market was probably a mistake. It might have been handled differently. They're changing their exchange rate policy in August. It might have been more fully better communicated, created a great deal of uncertainty.

I think there is this impression that for decades China has had brilliant economic decision making that has led to a record pace of economic growth. And in the last six months or so, they haven't been quite as perfect as they were in the past. So, I think, it is a different environment and people are kind of re-examining how strong is the economic decision making. Are they going to be able to carry on the growth trajectory that they've had—not the double digit but will they be able to sustain what they call the “New Normal” which is a growth of 6% or 7%. A lot of critics are saying they're headed for 2% or 3%.

Steve Weisman: Well, this is a speculative final, final question. So forgive me, but how much do those economic factors filter in to the political discussions, which are also very sensitive?

Nicholas Lardy: I think inevitably they're interrelated but even though China is growing slower than it was a few years ago, it's still, probably, the fastest growing economy in the world. They are growing at least twice as fast as the United States.

So, their economic footprint is still expanding in the global context, maybe not quite as fast as in the past. So I don't think the wind has really been completely taken out of their sails.

Steve Weisman: Okay. Nick, thanks a lot.

Nicholas Lardy: Thank you.

