CHINA'S ECONOMY 2009 IN REVIEW: REBOUND FIRST AND REBALANCE LATER

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Executive Summary

1. The Chinese economy by the end of 2009 has clearly rebounded, with around 8.5% growth for the whole year. China's growth has also spurred regional and global economic recovery.

2. Looking back, Premier Wen Jiabao called 2009 a "scary year" (惊心动魄), as China's economic growth in Q1 plunged to 6.1%, the lowest quarterly growth for more than a decade.

3. As China's economy is quite dependent on exports, the US credit crunch quickly reverberated in China's export industries, causing widespread factory closures and industrial layoffs.

4. The Chinese government took alarm and immediately put up a huge stimulus package of 4 trillion yuan (US$586 billion). Together with massive bank loans (9 trillion yuan), the pro-active stimulus polices quickly produced results, and the economy bottomed out in Q2.

5. China's growth pattern in 2009 has not changed much, except for the external demand (net exports), which registered a negative 30.6% growth due to the slump in global demand. Thus, growth in 2009 was primarily fuelled by the expansion of domestic demand, particularly investment (up 32.1%).

6. The decline in foreign trade growth has not altered China's global trade patterns but has lifted China to become the world's largest trading nation. Regionally, the recession has strengthened China's trade relations with its Asian neigbhours, particularly ASEAN. The China-ASEAN FTA will be operational in 2010.

7. Overall, the government's basic strategy is to restore economic growth first and then tackle the long-term structural problems. Accordingly, the

government has achieved preciously little in terms of rebalancing and restructuring the economy.

8. Rebalancing is a long-term goal. But China also has its own political and economic imperatives for sticking to the existing development strategies. It is essentially difficult to restructure the existing growth pattern, which has evolved from its own economic and institutional characteristics.

9. Chinese top leaders hope to boost domestic demand for "improving the people's livelihood". But the economy is institutionally biased towards savings, investment and exports, leaving little room for expanding domestic consumption.

10. For similar reasons, Premier Wen would not bow to international pressure and revalue the RMB (*Renminbi*), even though this will help China and the world to reduce macroecoomic imbalances. China apparently takes the view that global macroeconomic rebalancing is a collective effort, and China should not do this alone.

11. Still, China should be aware of the costs and risks of continuing with its old economic growth patterns. It also needs to address many short-term problems from industrial over-capacity to over-lending by banks.

12. China has recently revised its 2008 GDP upwards to US$4.6 trillion, or US$5 trillion for 2009. This means that China is about to replace Japan as the world's second largest economy any time in 2010.

13. The global economy in 2010 is still under a lot of uncertainty. Specifically for China, its major challenges are to sustain and manage its economic rebound, and to enhance the "quality" of economic recovery.