

FISCAL SUSTAINABILITY IN CHINA

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Executive Summary

1. Fiscal sustainability has become a concern of the Chinese government, with government expenditure and debt soaring to a record high in recent years. Between 2008 and 2013, average annual fiscal expenditure grew at 18.7%, while outstanding central government debt increased from RMB3.26 trillion in 2005 to RMB8.68 trillion in 2013.
2. However, the ratio of deficit and public debt to gross domestic product (GDP) remains relatively low, with outstanding central government debt to GDP ratio decreasing from 17.6% in 2005 and 15.3% in 2013. Annual deficit remains at a relatively low level of about 2% of GDP.
3. Estimation of debt-GDP ratio in China from different sources differed between 30% and 80% in 2012. Considering various international standards, the public finance condition in China is still robust.
4. Concerns about fiscal sustainability in the near future however remain. First, government social expenditure is expected to continue to outgrow the economy, as urbanisation accelerates and population ages.
5. Second, while overall government fiscal situation remains manageable, local government debt is huge and has increased rapidly. By June 2013, local government debt had hit over RMB10 trillion.
6. Third, some local governments have announced fiscal stimulus package which would further increase fiscal expenditure. Fourth, the growth rate of fiscal revenue may be slower after the recent round of tax reform.
7. In response, some policy initiatives have been proposed recently. One is the Central Budget Stabilisation Fund and the other is the local government bond which could become an important source of local financing.

8. Policy initiatives for the budget system were proposed to improve fiscal sustainability. Some local pilot programmes for state-owned assets have been initiated to improve local fiscal conditions. The mixed ownership (混合所有制) scheme has been suggested to widen financing sources.
9. Remaining issues to be addressed include reforming the intergovernmental fiscal system and budget system, improving the efficiency of fiscal expenditure and regulating privately financed public projects.