

**CHINA'S POLITICAL ECONOMY
IN THE RUN-UP TO THE
THIRD PLENUM**

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Executive Summary

1. China's economic recovery has been less vigorous than expected.
2. Though the government's target for 2023 remains within reach, waning confidence is undermining household consumption and private investment, local government debt and lower land revenues is slowing government spending, and a cooling world economy is dragging down exports.
3. The disappointing recovery triggered a barrage of documents supporting the private sector, but the key question remains as to whether China's policymakers still believe in the decisive role of the market in the allocation of resources. Despite much support set out in policy documents, investors remain sceptical.
4. It is premature to talk of a balance sheet recession. The blows that the faltering property sector has inflicted on the economy are as of yet too small, and because prices are holding up, the impact is largely contained within the property sector.
5. In the short term the government will likely support the property sector to the extent that it stabilises at much lower levels of activity. Property developer debt to the financial sector and debts of local government financing vehicles would need to be addressed in the coming years, but China has the experience and tools to do so.
6. To keep medium-term growth at reasonable levels it is becoming increasingly urgent for the government to address structural challenges facing China's economy.
7. The forthcoming third plenum is an opportunity for the new economic team to propose a credible policy package that addresses short-term headwinds and structural issues in the labour market, fiscal system and financial sector.
8. These reforms must address the supply side as well as the demand side of the economy. Critical for demand side reforms is addressing the primary and secondary distribution of income.