China’s Rebalancing and External Sector Adjustment

Maurice Obstfeld
Economic Counsellor
China: Slowing down and rebalancing

Real GDP growth
(percent; year-on-year)

Consumption and investment shares
(percent of GDP)

Sources: Haver Analytics, and IMF, World Economic Outlook.
Service sector becoming more important

GDP by Production
(percent of GDP)

- Industry (including construction)
- Services

Employment by Sectors
(percent of total employment)

Primary
Industry
Services

Source: Haver Analytics.
Strong domestic demand has helped reduce external balance

China: Current account surplus
(percent of GDP; four quarter rolling sum)

Source: Haver Analytics.
Gradual shift toward greater currency flexibility

Value of foreign currencies against the yuan
(index; 2000 average=100)

Source: Haver Analytics.

Nominal effective exchange rate
U.S. dollar per Yuan

Appreciation of Yuan

Change to parity setting
Announcement of CFETS basket reference

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Recent changes in the currency regime

Exchange rate
(China renminbi per U.S. dollar)

De facto USD weight in
RMB basket vs. NEER 1/

Sources: Bloomberg, L.P.; Haver Analytics; IMF, Global Data Source; and IMF staff calculations.

1/ Shaded region corresponds to 95 percent confidence bands around basket-weight estimate.
Reserves have fallen since 2014

Foreign Exchange Accumulation and Intervention
(billions of U.S. dollars)

Sources: Bloomberg, L.P.; and CEIC.
Capital flows also play an important role.
Record capital outflows

Current and capital account
(percent of GDP, four quarter rolling sum)

Source: Haver Analytics.
Drivers (I): Carry trade inflows stop with depreciation expectations

RMB implied 1-year appreciation/depreciation (percent)

Sources: Bloomberg L.P.; and IMF staff calculations.
Drivers (II): Rising concern about the health of financial sector and slowdown in GDP growth

Corporate credit: High level relative to peers 1/
(selected economies; 2014)

Source: CEIC Data Company Ltd.; IMF, World Economic Outlook and IMF staff estimates

1/ Luxembourg and Hong Kong SAR not shown; these have corporate credit-to-GDP ratios and GDP per capita of (118.2, 413.6) and (40.1, 216.6), respectively.

2/ Calculated as total social financing minus equity, LGFV and household loans.

China: Real GDP Growth (percent, year-on-year)

Credit to non-financial corporates (percent of GDP)

GDP per capita (USD thousand)

Source: CEIC Data Company Ltd.; IMF, World Economic Outlook and IMF staff estimates

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Drivers (III): Continued anti-corruption campaign and changes in the enforcement of capital controls

Anti-corruption efforts: more court conclusions and less new investigations

(number in thousands (lhs) and in percent year-on-year growth (rhs))

Sources: Supreme People’s Procuratorate; IMF, Balance of Payments database; and IMF, *World Economic Outlook*.

Foreign direct investment

(percent of annual GDP)
Net inflow reversal and reserves still ample in China

Net capital inflows to EMs
(U.S. billions)

Chinese reserves well above relevant adequacy ratios
(U.S. billions)

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Sources: Haver Analytics, and IMF, World Economic Outlook.
Process not over – Rebalancing still under way
Excess saving

Investment and saving
(percent of GDP)

China is major outlier in saving and consumption
(percent of GDP, 155 countries)

Orange dots are East Asian economies

Sources: Haver Analytics; IMF, World Economic Outlook; and IMF staff estimates.
Higher saving, particularly at lower income deciles

Average household saving rates, per income deciles
(In percent)

Sources: Luxemburg Income Study (LIS), and Chinese Household Income Project (CHIP) for China.
Spillovers to EMDEs: Chinese foreign asset appetite, along with trade, resulting in large exposures to China

Chinese banks’ claims, 2016Q2 1/ 2/
(percentage of borrower country’s GDP)

Exports to China, 2015 1/
(percentage of exporter country’s GDP)

Sources: Bank for International Settlements; and IMF, Direction of Trade Statistics.
1/ The 3 countries with largest financial/trade exposures to China in each region are depicted in red.
2/ Estimates for 2016Q2 based on the differences between two vintages of BIS Locational Banking statistics for the same quarter (one vintage before and the other after China and Russia were included as BIS reporting countries in November 2016).
Chinese economy is heavily managed

China among most closed in OECD
(OECD's product market regulation (PMR) index)

Source: OECD.
Note: The PMR index assesses degree to which policies promote competition in the product market. Policies assessed include state control of business enterprises; legal and administrative barriers to entrepreneurship; and barriers to international trade and investment.
And has relatively few final consumption imports

China, OECD and EMDEs: Import Breakdowns, 2015
(percent of GDP)

Source: OECD STAN Bilateral Trade Database in goods.
Excessive saving is problematic for macroeconomic stability

- Allocating a higher share of income to consumption could both increase welfare and support growth in a less debt-intensive way
- Given home bias and capital account restrictions, high saving translates into excessive domestic investment which is unlikely to be absorbed efficiently
- The fall in inefficient investment, without an increase in consumption, would widen the current account surplus, worsening global imbalances and undermining the multilateral trade system

Better macro-policy mix should play a key role in the transition

- The current fiscal stance uses up limited fiscal space to support unsustainable growth
- A modest removal of monetary policy accommodation is justified by the growth and inflation outlook, and financial stability concerns
- Progress toward a more flexible exchange rate should continue