

## China's true economic growth rate

The Chinese government should come clean about its economic record.

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With news that China's exports fell for the seventh consecutive month in January, fears are mounting about China's economy. China's purchasing managers' index also indicates contraction. Related indices that don't usually make the headlines are doing even worse.

All eight business indexes published by China's National Bureau of Statistics point towards recession. The open orders index, which tracks purchasing orders actually awaiting fulfilment, has been in negative territory for more than a year. The orders just aren't coming in.

Tellingly, Taiwan's exports to China have fallen by double digits over the past year. Taiwan exports advanced components such as semiconductors that are used in China's manufacturing industries, which just aren't buying these days. South Korean companies are suffering even more. Korean exports to China are down more than 20 percent.

The Chinese government insists that economic growth continues to hum along at an annual rate of more than 6 percent. Is this figure credible? With manufacturing falling, exports falling, imports falling, and consumer confidence at record low levels, can it really be that China has one of the world's fastest-growing economies?

Chinese Premier Li Keqiang admits that China faces "great challenges and uncertainties" but claims that "China's economic fundamentals are stable". Such assurances increasingly ring hollow. The hard facts point in a different direction. The only thing keeping the Chinese economy afloat is government spending on a massive scale.

### Proactive fiscal policy

The Chinese government has a special name for deficit spending: "Proactive fiscal policy". Proactive fiscal policy means pumping money into the economy to prevent a recession. The rest of the world calls this Keynesian economics. Keynesian economics went out of fashion in the West after the 1970s, but it is alive and well in China today.

No country in the midst of a sustained period of rapid economic growth in excess of 6 percent per year pumps huge amounts of money into the economy in a desperate attempt to boost activity.

In 2015 China's national government spending rose at a wildly unsustainable pace of 15.8 percent. Local government spending may have risen even faster; nobody knows the true figures. At the same time taxes are being cut. And the State Council expects these "proactive fiscal policies" to be "continued and strengthened" in 2016.

And China is doing much more than building bridges and cutting taxes - the orthodox Keynesian approaches to propping up a faltering economy. In a country where all commercial banks are state-owned, the government has the capacity to pump money into the economy through the banking system too.

No one was surprised to learn that bank lending expanded at record levels in January. The surprise was that new bank lending quadrupled between December and January, adding an extra \$400bn to the economy. Adding in other government-sponsored lending programmes boosts this figure even higher.

This is not a bad thing. In fact, it is exactly what many Western economists would prescribe for an economy teetering on the brink of a recession. But China claims not to be teetering on the brink of recession. If the Chinese economy really is growing at an annual rate of more than 6 percent, Keynesian economic policies make no sense.

Success in admitting failure

Credit expansion and deficit spending are emergency measures. No country in the midst of a sustained period of rapid economic growth in excess of 6 percent per year pumps huge amounts of money into the economy in a desperate attempt to boost activity. China's breakneck spending programme is a policy without a plan.

Keynesian economics fell out of favour in the West when governments resorted to deficit spending as a way to maintain growth at artificially high levels. During an economic slowdown, deficit spending soaks up excess capacity to prevent a recession from turning into a depression. But in a growing economy, deficit spending just drives up prices, causing inflation.

If China's economy were really growing at more than 6 percent per year, expansive bank lending and rising fiscal deficits would quickly translate into higher prices. But there are no signs of this occurring. In 2015 China's inflation rate was less than 1.5 percent. It has been on a continuous downward trajectory ever since 2011.

Instead, it seems as if China is using Keynesian economic tools in an entirely appropriate way: to prop up a failing economy. The only missing element in this equation is an open admission by the Chinese government that its economy really is failing. But if the economy is succeeding, China's current economic policies make no sense.

It is a cliché of China commentary to claim that the Communist Party of China (CPC) relies on economic growth to legitimate its continued rule. Many analysts inside and outside China believe that a political revolution will break out the first time China suffers a real economic recession. This is ridiculous.

The CPC seems to be doing a relatively good job fighting off a serious economic downturn by using every tool in its arsenal. That is the right thing to do. The only wrong thing is to lie about it.

The CPC will get more credit from international analysts - and from its own people - if it is honest about the challenges China is facing and what it is doing to meet them. China can survive a recession. With good policy, it might even prevent one.