CCAS
Centre for China Analysis & Strategy
中国分析及策略中心

15 March 2020

THE COVID-19 EPIDEMIC AND CHINA'S ECONOMY

by JAYADEVA RANADE

1. The Coronavirus epidemic struck China when it was in the midst of serious economic problems and high unemployment and Chinese economists were already candidly warning of a 1 percent drop in growth this year. The attempted cover-up by Chinese authorities of the Coronavirus epidemic for nearly two months -- unimaginable in democracies -- exacerbated economic losses and disruption in addition to causing the loss of numerous lives and delaying an international medical response to the virus. Reports say at least two international pharmaceutical companies will start human trials of vaccines against Coronavirus by next month and could have the vaccines ready by early next year. Chinese economists had warned in January that if the epidemic was not contained by mid-February, China's growth rate could drop by two percent. The absence of transparency in efforts to, initially inform the people and later combat the Coronavirus, led subsequently to the imposition of unavoidable drastic measures and sharply accentuated the already high level of distrust between the people and China's communist regime.

2. The US-based Rhodium Group assessed (March 11) that while the pace of new Covid-2019 transmissions is coming down in China, the "pathway to economic recovery remains deeply uncertain". It asserted that China has endured a severe economic downturn in the first quarter of 2020. The Report pointed to the Transportation sector which registered 82% fewer trips in the 25 days following the Lunar New Year in 2020 relative to 2019, signalling that workers were not returning from the countryside. It recorded that: Coal consumption by China's six largest power plants fell over 40%;

property sales in major cities were near-zero in February; manufacturing and services recorded major contractions; and that the shutdown of China's economy is even visible from space with satellite readings showing almost non-existent nitrogen oxide and dioxide emissions from swaths of the industrial heartland.

3. Despite the economic losses and disruption caused by the Coronavirus epidemic, Chinese President Xi Jinping sought to keep the focus on China's economic targets and the 'Two Centenary' goals. In a teleconference directly with over 170,000 officials across the country on February 23 on 'Coordinating and Promoting New Crown Pneumonia Epidemic Prevention and Control and Economic and Social Development Work', Chinese President Xi Jinping focussed on reviving the economy. He said over 46% of China's counties and districts are classified as 'low risk' and should be getting back to normal soon. Those facing 'moderate risk' need to be more cautious – resuming work only gradually. Xi Jinping also assured that top leaders are ready to employ fiscal and monetary policies if needed and "Macro policies… should prevent the economy from slipping out of a reasonable range." He urged local governments to address supply chain congestion in and between provinces. Xi Jinping expressed concern about China's role in global trade saying: "[We] need to secure the smooth operation of foreign trade supply chains and stabilize [China's] share in the international market."

4. At the Politburo Standing Committee (PBSC) meeting on March 4 to "study the current epidemic prevention and control work and economic and social stability", Xi Jinping claimed there was overall improvement in the epidemic situation across China and resumption of economic activities had accelerated. He had earlier issued instructions to speed up resumption of work in factories etc. He reminded PBSC members of the "complexity" of the current epidemic prevention and control and the economic and social developments. He urged deepening international cooperation and giving full play to China's role as a "responsible great power." The meeting specifically stated that prevention and control efforts must persist in Wuhan, Hubei, and the Beijing region and emphasised the importance of enhancing scientific efforts to develop treatments and vaccines. It stressed the imperative to minimise economic losses and also that China must assist companies, stabilise employment, and facilitate the hiring of key groups such as college graduates and migrant workers. The adoption of various "point-to-point" transportation methods should continue to allow employees to return to work as

soon as possible. Additionally, China will push for the construction of major projects including 5G and increase investments in public health services and production of emergency supplies. The meeting urged stabilising foreign trade and investment and facilitating foreign-invested companies in China to resume work. In conclusion, the meeting emphasised the importance of grasping Spring agricultural production, stabilising prices of agricultural products, and increasing poverty alleviation efforts.

5. In step with Chinese President Xi Jinping's exhortation and despite the severe disruption caused by the Covid-19 epidemic, China has continued trying to further the objectives of the 'China Dream'. The Economics & Technology Research Institute (CNPC-ETRI) of the State-owned China National Petroleum Corporation (CNPC), for instance, disclosed they were exploring the possibility of a Beijing-led global health organization that would rival the World Health Organisation (WHO). Carice Witte, founder and Executive Director of the Israeli company SIGNAL, confirmed the idea and described it as "very interesting in the context of China's aim to reshape global governance, including setting up parallel institutions." Chinese Foreign Minister Wang Yi, while highlighting (March 2) the Chinese government's strengths in combatting the Coronavirus epidemic, referred to China's 'Two Centenary Goals' and vision of building "a community with a shared future for mankind"! On March 8, the Chinese government announced its decision to donate US$ 20 million to the World Health Organization (WHO) to support it in carrying out international cooperation in fighting the outbreak of novel coronavirus disease (COVID-19).
6. The impact of the Coronavirus epidemic on China has been severe. With over 80,000 persons infected by the Coronavirus; millions of persons under quarantine; schools, colleges, restaurants and public places closed resulting in laying-off millions of workers to join the millions of those already unemployed; stringent transport restrictions imposed throughout China; and 18 cities placed under strict isolation, the economic losses are enormous. Additionally, the Chinese government's delayed response to the epidemic and lack of transparency further raised the existing serious trust deficit between the authorities and the public of which there were frequent public demonstrations.

7. A number of China's factories, R&D centres and companies, many headquartered in Wuhan, were shut with efforts to reopen them beginning in late February with patchy

results. Navy Shipyards, aircraft factories and weapons production plants were closed. Regulations were issued to restrict the activities and training of China's People's Liberation Army (PLA). Recruitment to the PLA, which had been planned in two phases, was postponed. China's major internet companies, including Tencent, ByteDance, Baidu and Didi, deferred the date for their employees to return to offices.

8. After January though, the government made huge efforts, including severe isolation measures for entire cities and populations. It constructed three hospitals within weeks, using China's Air Force to transport medical equipment, supplies and personnel, and deploy military doctors and medical staff to Wuhan.

9. Restaurants, food stalls etc closed due to the coronavirus epidemic rendering millions of workers unemployed. A China Cuisine Association survey reported that around 95% of caterers experienced major losses over the Lunar New Year. The report said the impact of the coronavirus outbreak on China's restaurants, fast-food joints and snack stands will be several times greater than that caused by the SARS outbreak of 2003. Besides losses over the holiday, businesses are likely to face serious cash flow issues and difficulty obtaining financing in coming months. More than 300 Chinese companies including smartphone-maker Xiaomi and China's ride-hailing giant Didi Chuxing are seeking bank loans totalling at least US$ 8.2 billion to ease the impact of the coronavirus epidemic. China has decided to provide medium-term funding to banks and cut the interest rate it charges as officials seek to cushion the economy from the epidemic.

10. Well-known Chinese news site *Sina* reported on January 27, that China's Ministry of Human Resources and Social Security issued new regulations to relax certain labour laws for the period when the nation is combating the coronavirus. The new regulations prohibit laying off workers or stopping their pay if the workers are not able to work due to government bans. Companies have been instructed to provide a minimum living payment to those not able to work. For those involved in the rescue activities of the epidemic who temporarily lose income and are not able to pay off credit card debts or a mortgage, this will not be recognized as a breach of contract. Delayed payments should be allowed. The State Grid for electricity also announced that customers would be allowed to continue to use electricity even if their date for payment of dues is past.

The State Grid will also arrange for customers to do business remotely online without visiting local offices.

11. Soon after the Coronavirus struck and its magnitude was gauged, Chinese economists said in early January that China's services sector alone was suffering a loss of US$ 144 billion a week! Some of China's major internet companies, including Tencent, ByteDance, Baidu and Didi, deferred the date for their employees to return to offices. Apple iPhone maker Foxconn, which employs more than 400,000 on the Chinese mainland, delayed complete reopening until March. A broad survey of American companies in China released on February 18, showed that more than three-quarters have insufficient staff to run a full production line. Data released by Chinese software company Gaode on March 10, showed that while Wuhan's work resumption rate stands at just 12.54%, most companies planned to ramp up work to 80% by end March. Meanwhile, to encourage companies to resume work amid the coronavirus outbreak, China's Ministry of Transport said (February 15) that China's roads will be toll-free starting February 17. The policy will be in force until the epidemic is deemed to be over.

12. China's official 'The Paper' observed (March 5) that while businesses are re-opening, the "economy remains severely depressed". It cited Baidu's Big Data as showing that over 50% of offline [businesses] had resumed work nationally. It said "The percentage of offline [businesses] that have resumed work exceeds 63% in Xining, Dalian, and Changchun, which lead the country in this respect." Separately Xinhua reported that less than half of small and medium enterprises are back at work. It said "Around 45 percent of China's small and medium-sized enterprises (SMEs) had resumed work" by March 2, up from 32.8 percent as of February 26, according to the Ministry of Industry and Information Technology (MIIT). MySteel, a magazine reporting on the coal industry, said "The capacity utilization rate as of March 3 [of coal mines was] 83.4%, according to official data from China's National Energy Administration." In a rare and major step, China National Offshore Oil Corp., China's biggest LNG buyer, invoked force majeure and told some suppliers it won't take delivery of cargoes because of constraints caused by the coronavirus. French oil and gas giant Total SA have rejected the declaration. Soon thereafter the Chinese copper smelter Guangxi Nanguo also declared it would refuse to take delivery of raw

materials. China's biggest oil refiner, Sinopec Group, is similarly likely to ask Saudi Arabia to reduce crude supplies next month.

13. Xinhua reported on February 13 that according to data for January released by the China Association of Automobile Manufacturers (CAAM), Chinese national automobile manufacturing volume declined 33.5 percent, month-over-month, and 24.6 percent, year-over-year. The sales volume declined 27 percent, month-over-month and 18 percent, year-over-year. Passenger car sales declined 27.1 percent month-over-month and 20.2 percent, year-over-year. New energy source automobile sales declined 54.4 percent year-over-year. According to CAAM officials, the coronavirus impact started later in January so February numbers are expected to be much worse, as they will start to show the impact on market activities, manufacturing capacity, export limitations, financial bottlenecks and tougher government regulations. They anticipate the Chinese automobile market may slump further.

14. The Coronavirus epidemic also has hidden costs. For example the Deputy Governor of the People's Bank of China (PBoC), Fan Yifei disclosed (February 15) that the Bank was 'sanitising' bank notes as well as blocking their movement between cities in regions most affected by the outbreak to limit transmission of the virus. Other banks could be expected to have done the same. There was indication too of capital flight. China's central bank in February announced increased punishment for financial institutions that fail to adequately guard against money laundering and imposed fines of more than 10 million yuan (US$ 1.4 million) for the first time. The China Minsheng Banking Corp. was fined 23.7 million yuan and China Everbright Bank Co. Ltd. 18.2 million yuan. They were penalized for failing to properly perform required customer identification checks, failing to keep customer data and transaction records and failing to report large or suspicious transactions. The PBoC fined the brokerage Huatai Securities Co. Ltd. 10.1 million yuan for similar violations.

15. The severe blow to the Chinese economy caused by the Coronavirus, however, has come atop an already deteriorating economy. Singapore's primary Chinese-language newspaper Lianhe Zaobao reported (December 31) that China saw its lowest level of overseas acquisitions in 2019, with a total value of US$ 41 billion, or half the 2018 volume. Acquisitions in the US declined by 80 percent in 2019. Analysts in the global

banking industry believe that the sharp decline in overseas acquisition is directly attributable to the US-China Trade War and significantly tightened government regulatory measures imposed in many countries against Chinese buyers. It observed that with the economic slow-down in China, the Chinese government began strictly controlling the volume of capital flowing out of China, making it especially difficult for Chinese investors to pay back the debts acquired overseas. It is expected that more domestic investments will be seen in China than overseas.

16. Reuters reported (January 22) that about two-thirds of China's provinces, regions and municipalities had cut their 2020 growth targets from last year, despite easing trade tensions with the US. It added: "Of China's provincial-level regions, 22 including Beijing, Guangdong, Zhejiang, Henan, Hainan, and Fujian, set lower growth targets this year compared to last, a similar number to last year. Beijing, Shanghai, and the southern export hub of Guangdong all dropped their targets from 6-6.5% growth to "around 6%" in 2020, in line with the expected change to the national target ... At least 11 provincial-level regions missed their 2019 GDP targets, according to preliminary statistics released by local governments. Targets for 2020 ranged from around 5% growth - for the north-eastern province of Heilongjiang and the northern city of Tianjin - to around 9% growth for the Tibet Autonomous Region."

17. There have been other earlier warnings of the downturn in China's economy. In mid-December 2018, Renmin University Prof. Xiang Songzuo highlighted serious doubts about the economy at a public function, which was promptly censored on the Chinese internet. He questioned China's real rate of growth -- declaring that a "research group of an important institution" released an internal report stating China's GDP growth this year was about 1.67 percent -- the poor state of private businesses in China, and a lack of confidence. Within days, 59-year old Chen Hongtian, Chairman of the Cheung Kei Group and member of the Chinese People's Political Consultative Conference (CPPCC), warned nearly 150 tycoons based mainly in Shenzhen and Hong Kong, that China's private business entrepreneurs should prepare for a "winter colder and longer than expected". The group included Tencent Chairman Pony Ma, the Chairman of carmaker BYD, Wang Chuanfu, and the Chairman of courier service SF Express, Wang Wei. Meanwhile, State owned Enterprises (SoEs) expanded to enter virtually every sector of economy activity.

18. More recently on November 27, Gao Shanwen, a well-known economist in China, in a speech at an internal annual strategy meeting predicted that China's economic slowdown will last several years and that the average annual economic growth between 2020 and 2030 will stay below five percent. Gao Shanwen was even concerned about whether GDP (gross domestic product) would grow above four percent. He identified two contributing factors: first, the impact of the trade war; and second, the stagnation of China's economic reform as seen in the "advancement of the state enterprises and the retreat of the private sector." Gao Shanwen said that the government has used strong counter-cyclical measures to prevent the economic downturn, but these have barely supported the growth rate at about six percent. The stimulus policies are less and less effective and, with a weak domestic market, the economy of 2020 doesn't look good. Gao Shanwen's speech was widely circulated on the Internet, but deleted within a day.

19. On December 8, Sina.com published economic data posted on the Internet by an unnamed author which explained that China's economy is at its most difficult time. It was widely disseminated across the internet in China. The main points are: (i) the number of people using Baidu to search for jobs in 2019 jumped to 28.54 million from the under 7.5 million people job seekers in 2018; (ii) all four Chinese companies ranked in the top ten companies with the highest profits in the world are banks, suggesting that China's banking sector is squeezing profits out of other industries. China's banking sector claims 40 percent net income return; (iii) China's state-owned enterprises (SoEs) are growing and the private companies and foreign companies are shrinking; (iv) People are short of money. The fund industry (both mutual funds and hedge funds) raised 500 billion yuan (US $72 billion) in the third quarter of 2017 alone. However, for the whole year of 2019, it only raised 180 billion yuan; (v) 1,884 movie or TV related companies closed in 2019; (vi) New car sales dropped 2.76 percent in 2018 compared to 2017. From January to October 2019, the number of new cars manufactured and sold dropped 10.4 percent and 9.7 percent respectively, compared to a year ago; (vii) China is departing from real (manufacturing) businesses. Among the total assets of companies in China, the financial and real estate industries claim 47.9 percent of the assets, whereas the manufacturing sector only accounts for 11.7 percent; (viii) In the first six months of 2019, all provinces in China, except Shanghai, ran into a fiscal deficit.

20. The Coronavirus had an important political impact too. The attempts by the government to cover up news of the epidemic, delayed response and lack of transparency in the initial weeks generated very angry public reaction. It provoked seldom seen public criticism of Chinese President Xi Jinping and the Chinese Communist Party (CCP). Xi Jinping's till now unexplained absence between January 29 and February 10, from public view and the official media and state-owned National TV at a time when China faced a national medical crisis, drew added critical comment. Reputed Chinese intellectuals and scholars at certain personal risk posted criticisms of Xi Jinping and the CCP on their public social media accounts. Well known Chinese Professor Xu Zhangrun of Beijing's Tsinghua University, on February 5, posted a scathing criticism of Xi Jinping and the Chinese authorities captioned 'Angry People No Longer Fear', that went viral on China's social media. He was arrested shortly thereafter. There were similar displays of anger by other Chinese intellectuals and even one Supreme Court Judge!

21. Videos surfaced of Wuhan residents shouting "fake, fake" and "this is not real" during an inspection by Politburo member Sun Chunlan. A call by Wuhan Party Secretary Wang Zhonglin, a close associate of Xi Jinping, to "carry out gratitude education among the citizens of the whole city, so that they thank the General Secretary [Xi Jinping], thank the Chinese Communist Party, heed the Party, walk with the Party, and create strong positive energy" evoked sharp rebuke and widespread anger. Chu Zhaoxin, a local journalist posted (March 7) an article on his public WeChat account entitled "Have a Bit of Conscience: It's Not Time to Ask the People of Wuhan for their Thanks", adding that Wang Zhonglin's timing was "insensitive". He said "If this is Wang Zhonglin's idea, I think he needs to educate himself. You are a public servant, and your job is to serve the people. Now the people you serve are broken, the dead are still cold, and the tears of the living have not yet dried. The sick have not yet recovered, and much of their dissatisfaction is completely reasonable. Rather than blaming the people in Wuhan you serve for not being grateful, you should reflect and be ashamed because you and your team are not working properly." Predictably, the post was removed late by March 7 night. The South China Morning Post reported (February 18) that He Weifang, Professor of Law at Peking University, in a 2-page handwritten article shared with friends on WeChat on February 17, calling for press freedoms. Xu Zhiyong, a former law lecturer and founder of the social campaign New Citizens Movement, was

arrested on February 15 for his article of February 3, where he urged Xi Jinping to step down for his “inability to handle major crises”.

22. With their image substantively dented, if not damaged, Chinese President Xi Jinping and the CCP have a long and arduous road ahead to revive economic growth and create jobs. A top priority will be to rebuild and restore public trust which is crucial to the CCP’s legitimacy as the sole ruling party. For Xi Jinping it is imperative he demonstrates that the ‘China Dream’ and China’s goal of becoming “a major world power with pioneering global influence” remain intact. China will need to try and re-establish international supply chains, but more important will be whether global markets will be willing and in a position to procure and absorb Chinese products as they themselves struggle to recover from the after effects of the Coronavirus epidemic.

(The author is former Additional Secretary, Cabinet Secretariat, Government of India and is presently President of the Centre for China Analysis and Strategy.)