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China's Economy: Current Trends and Issues

The International Monetary Fund (IMF) assesses that the People's Republic of China's (PRC's or China's) real gross domestic product (GDP) grew by 5.2% in 2023 and projects 5.0% real GDP growth in 2024. This growth is unbalanced, with supply much higher than domestic demand. The World Bank says that soft domestic demand, weak domestic and foreign business confidence, "tepid" productivity growth, and systemic debt, among other issues, could constrain PRC future growth prospects. Some economists contend that the economic returns of China's growth model, which has emphasized government investment and exports, is diminishing. These elements still appear to feature in China's current economic policies, however.

The PRC government is seeking to reduce debt and boost growth and productivity by investing in innovation, education, digital infrastructure, advanced manufacturing, and emerging technologies. It is also pursuing state-led industrial policies to advance its economic and technology development goals. Such statist approaches can distort markets and incentivize production well above what China can absorb domestically. As products supported by PRC industrial policies come to market, China appears to be looking to foreign markets for growth. China's share of global manufacturing output was about 30% as of 2022, highlighting the potential influence of PRC production and export policies on U.S. and global markets. Some in Congress and the Biden Administration have expressed concerns that PRC industrial policies and related subsidies are fueling PRC export expansion in sectors such as electric vehicles (EVs), semiconductors, solar energy, and steel.

The Third Plenum

In July 2024, the Third Plenum of the Communist Party of China (CPC) Central Committee focused on economic policies through 2035 to advance "Chinese-style modernization," a term the CPC uses to refer to China's approach to economic development. The Plenum's decision affirmed 14th Five-Year Plan (FYP) (2021-2025) priorities (see **text box**). It featured plans to develop the digital economy and service sector; to deepen capital markets and securitize intellectual property; and to internationalize China's currency, the *renminbi* (RMB) and develop a digital RMB and PRC cross-border payment system. It mentioned plans for commodity trading platforms and global distribution centers; a pilot to extend rural land contracts by 30 years; household registration reforms to benefit rural migrants living in urban areas; and an expansion of how local government funds can be spent.

At a May 2024 business forum before the Plenum, China's leader Xi Jinping emphasized employment, income growth, housing, education, and healthcare issues. Xi also called for "resolutely dismantling institutional barriers hindering Chinese-style modernization." CPC policy debates include how to boost economic growth (particularly lagging consumer spending) and productivity; address inequalities; and reform national-local government tax-revenue sharing.

Efforts to Boost Growth

PRC leaders appear reluctant to adopt broad stimulus to boost domestic consumption as they try to reduce debt levels. They have pursued narrow stimulus measures and government-led fixed asset investment in manufacturing to boost growth. Such measures include value-added tax export rebates, tax incentives for technology and research, and expanded financing for programs that promote a "buy back" of old appliances and EVs for new purchases. Other PRC government actions to boost the economy include

- **March 2024:** The PRC government said it would issue up to $539 billion in local government special purpose bonds, typically used to fund infrastructure projects and pay off government debt.
- **May 2024:** The central bank announced $41.4 billion to convert unsold housing into subsidized housing. The Finance Ministry pledged to issue $138 billion in ultra-long-term special sovereign bonds through November 2024 to support 14th FYP (2021-2025) priorities.
- **July 2024:** The central bank cut its one-year medium-term lending rate by 20 basis points to 2.3%.
- **August 2024:** The State Council announced stimulus programs to boost domestic consumption in services.

The 14th Five-Year Plan (FYP) (2021-2025)

The 14th FYP prioritizes research, education, finance, and technology, and calls for $1.4 trillion in investment in digital infrastructure. It emphasizes self-reliance and indigenous innovation while sustaining access to U.S. and other foreign markets, technology, capital, and research to advance PRC goals. It prioritizes self-sufficiency in energy and agriculture (biotechnology, genetic resources, and seed technology), and calls for China to lead in setting global trade rules and technical standards. It promotes China's extraterritorial reach, and pursuit of global acceptance of PRC judicial rulings on intellectual property and technology pricing and PRC antitrust actions.

Manufacturing Investment and Excess Capacity

To boost growth, Xi has revived a "dual circulation" policy that PRC leaders last used in the 2009 financial crisis that seeks to expand production while promoting exports. In 2009, the PRC government used this approach to fund production in 13 manufacturing industries while global industry contracted, generating excess capacity that China then exported to other markets. Amid weak domestic demand, the PRC government's increased investment in manufacturing is fueling deflation, stressing corporate margins, and expanding production beyond what China can absorb. Fixed-asset investment in manufacturing grew by 9.6% in the first five months of 2024 over the same period in 2023 with investment growth in prioritized sectors: rail, shipping, and aerospace (35% increase); metal products (18% increase); and information technology (15%

increase). In May 2024, the PRC government announced a third investment phase of its semiconductor fund with $47.5 billion over five years.

PRC industrial policies and related subsidies are fueling PRC exports and could distort global markets in sectors such as semiconductors, EVs, solar energy, and steel. For example, China is projected to account for almost half of all new global capacity in mature semiconductors (e.g., 28 nanometer and above) coming online during 2024-2029. In EVs, PRC industrial policies in place since 2009 have incentivized the build out of production capacity well above what can be sold in China, motivating exports. Some reports say China could face a surplus of 20 million EVs by 2025; oversupply is driving down factory utilization rates, prices, and profits for EV firms in China.

Trade Tensions

PRC leaders appear concerned about foreign governments' efforts to counter China's industrial policies and export-oriented growth strategy. Official readouts of a May 2024 meeting of senior CPC leaders noted "significantly rising external uncertainties." At a World Economic Forum meeting in June 2024, Premier Li Qiang encouraged countries to "reject bloc confrontation and decoupling, keep industrial and supply chains stable and smooth, and advance trade and investment liberalization and facilitation" to promote global growth. Foreign government efforts to counter PRC exports include:

- In April 2024, the U.S. Trade Representative extended most tariffs on PRC goods that it has imposed since 2018 under Section 301 of the Trade Act of 1974 and increased tariffs on some PRC goods in response to China "flooding global markets with artificially low-priced exports," including on EVs, EV batteries, semiconductors, medical products, ship to shore cranes, solar cells, and steel and aluminum items.
- The European Union (EU) has launched investigations against PRC trade and investment practices in anti-subsidy (EVs), anti-dumping (steel), and procurement (medical devices) areas. In June 2024 the EU announced 21-38% provisional tariffs on imports of EVs from China on top of its general 10% tariff on auto imports.
- In July 2024, the Indonesian and Canadian governments said they were considering tariffs on some PRC imports.

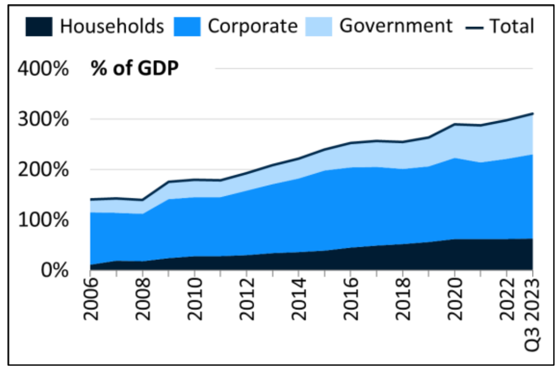
Foreign Business Confidence

Two years of "zero covid" restrictions, economic softening in China, and PRC political controls and economic coercion, appear to have fueled a sense of risk among some foreign firms of doing business in China. In February 2024, the American Chamber of Commerce said 57% of its firms lack confidence in China's business environment. In 2024, the PRC government has sought to boost market confidence by featuring high profile visits from global business leaders.

Currency

The RMB faces downward pressure from low domestic and international confidence in China's market, a strong U.S. dollar, and a widening gap between U.S. and PRC interest rates. The PRC central bank sets a narrow band within which the RMB can trade through daily guidance to PRC banks. Since August 2023, the central bank has set the RMB's daily rate well above the market rate to stabilize the currency. Some U.S. analysts assess that the PRC is seeking to manage depreciation and slowly devalue the RMB in a controlled manner. PRC state banks have supported the government's efforts to stem the RMB's rapid depreciation by selling U.S. dollars. In September 2023, the central bank decreased the amount of foreign currency deposits it requires PRC banks to hold. China remains on the Treasury Department watch list for currency practices, including its failure to publish exchange rate intervention data.

Figure 1. China's Non-Financial Debt as Share of GDP



Source: CRS with data from the Bank for International Settlements.

Notes: Government debt only available in nominal value. Comparable U.S. total non-financial debt as of Q3 2023 was 253% of GDP.

China's Systemic Debt

China's total non-financial debt—household, corporate, and government—reached 311% of GDP in the third quarter of 2023 (**Figure 1**), with most debt held by private firms and provincial and local governments. Local governments and firms have relied on bank loans and bond issuances to spur economic activity via fixed-asset investment as consumer spending has lagged. A 2016 government campaign sought to rein in banking, local government, and corporate debt. In 2018, Xi pledged to tackle financial risk as one of "three tough battles." The government relaxed the campaign during the pandemic and required local governments to fund pandemic mitigation and stimulus programs, which increased their debt burden. China has faced defaults by major property developers tied to local governments. Income from property sales is a main source of local government revenue and property prices are a key factor in firms' valuations and household net worth. This dynamic constrains PRC policy options to advance Xi's stated commitments to reduce debt and his "common prosperity" policy that seeks to address economic inequality.

Issues for Congress

Congress has debated the role of U.S. tariffs to address PRC industrial policies and their effects on trade. Some Members have expressed support for U.S. tariffs while others have said they harm the U.S. economy. Congress has responded to PRC industrial policies by passing legislation to develop U.S. semiconductor, solar, and EV industries (P.L. 117-167 and P.L. 117-169). Among its options, Congress may consider whether or not to:

- Encourage USTR to initiate a "phase two" Section 301 investigation to address PRC industrial subsidies;
- Explore joint trade actions with the EU and other top trading partners vis-à-vis China; and
- Address PRC overseas investments that may distort markets. PRC firms supported by PRC industrial policies are investing in the U.S. and third markets.

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