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CHINA: TOWARDS WHAT POST-COVID-19 GROWTH MODEL?

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Abstract: This article investigates the effects of the Covid-19 pandemic on the worldwide economy, the implemented stimulus measures, and the impact of the trade conflict and the "decoupling" plan on China's economy. Given the new situation, the Chinese government is pondering the introduction of economic stimulus policies as part of a revised growth model centred around domestic demand and the ability to produce through industrial policies and technological advancements for which they no longer rely on foreign sources.

Keywords: Pandemic, China, economic growth, trade war.

Introduction

The Covid-19 pandemic has been both a shock and a catalyst, marking a turning point or a point of no return in international economic (and political) relations, especially between China, the US, and the EU. It has resulted in increased decoupling, control of investments, technology transfers, and the initiation of relocation policies towards advanced economies. It prompts inquiries about the strategies for reviving the global economy, its various components, and the future of China's growth model, which is currently facing pressure from both the US-led decoupling effort and President Xi Jinping's proposed double circuit.

China is seeking to maintain and solidify the benefits its economy has gained from globalization by building upon its specialized advantages over the past four decades while still preserving its "socialism with Chinese characteristics" model, which has recently undergone significant changes in governance (Fan et al., 2019; Iza & Tellaeche, 2021). However, it may prove challenging or even impossible to obtain the necessary resources in several industries, particularly in high-tech sectors. The question remains, can China continue to sustain the growth model that has led to its success up to this point (Song & Appiah-Otoo, 2022; Zhenhua et al., 2018; Li et al., 2021)?

The traditional stimulus policies China has relied on (such as large-scale public investment in infrastructure) are reaching their limits (Sun et al., 2017, Chen et al., 2021; Kim et al., 2021). Substantial reforms to the growth model and its governance are necessary to complement the economic policies the Chinese government has begun to implement.

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Many Western and Asian companies (such as those from Japan and South Korea) will still operate in China to serve the sizeable domestic market across various industries, including automotive, telecommunications, and suppliers of components from Europe, the US, Japan, and South Korea.

The yield on 10-year bonds issued by the Chinese government currently stands at 2.7%, compared to 0.8% on equivalent investments in the US. The cracks in globalization existed before the pandemic outbreak (Zhang, 2021; Bi & Xin, 2021; Wang & Zhang, 2021) and have become increasingly apparent over the past decade, especially with the rise of the Chinese economy.

The Chinese government has faced numerous criticisms (Furuoka, 2018) from the US and Europe regarding its approach to multilateralism and practices that go against fair competition, such as subsidies for state-owned companies, forced technology transfers, and intellectual property theft. Despite the significant trade and market access imbalances, Europe has until now been lenient towards China but is now beginning to voice its concerns (Zhang et al. 2021).

Results

The recent slowdown in globalization due to the trade war and decoupling between China and the US has resulted in a new trend of de-globalization that prioritizes the protection of strategic industries and their relocation to nearby or home countries. However, relocating activities is not easy as many countries have already acquired specialization in the host countries of Western foreign direct investment. Cost-effectiveness remains the critical factor for companies to decide where to relocate, and robotization of work could lead to a sharp decline in manufacturing costs, as seen in the repatriation of activities from labour-intensive countries to the US.

The relocation of activities to the South has been a significant development tool for the receiving countries. Still, it has also resulted in interdependence and new forms of dependence, as seen with the localization of pharmaceutical production. Despite their competitive advantage in volume, production cost, transportation, and economies of scale, the international value chains built in recent years are fragile, as seen during times of crisis. In the short term, foreign firms, especially American and European, will continue to be attracted to the Chinese market. Still, China will likely feel the most severe impact of decoupling by limiting or blocking access to sophisticated components for high and medium-technology products. The Silk Roads project, with proper funding, is helping to maintain China's advantage in logistics and boost its trade with the rest of the world.

The potential breakout of a "cold war" between China and OECD countries, leading to a decoupling, would significantly impact both economies. China would face a decline in FDI and exports to the OECD, leading to a loss of 8% of its GDP. On the other hand, OECD countries would also see a decrease in their exports to China and face losses from the cessation of production by their branches in China. To mitigate these impacts, economists suggest the development of a peaceful economic coexistence where trade benefits are still reaped. Still, each entity can maintain its own distinct economic system.

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However, there are many uncertainties surrounding the duration of the recession and the speed of recovery, as highlighted by the recent IMF Economic Outlook.

Table 1. IMF growth projections, real GDP, annual % change

	2021	2022	2023
World Output	**6.0**	**3.2**	**2.7**
Advanced economies	**5.2**	**2.4**	**1.1**
United States	5.7	1.6	1.0
Euro area	5.2	3.1	0.5
Germany	*2.6*	*1.5*	*-0.3*
France	*6.8*	*2.5*	*0.7*
Italy	*6.7*	*3.2*	*-0.2*
Spain	*5.1*	*4.3*	*1.2*
Japan	1.7	1.7	1.6
United Kingdom	7.4	3.6	0.3
Canada	4.5	3.3	1.5
Other advanced economies	5.3	2.8	2.3
Emerging market and developing economies	**6.6**	**3.7**	**3.7**
Emerging and developing Asia	7.2	4.4	4.9
China	*8.1*	*3.2*	*4.4*
India	*8.7*	*6.8*	*6.1*
ASEAN-5	*3.4*	*5.3*	*4.9*
Emerging and developing Europe	6.8	0.0	0.6
Russia	*4.7*	*-3.4*	*-2.3*
Latin America and the Caribbean	6.9	3.5	1.7
Middle East and Central Asia	4.5	5.0	3.6
Sub-Saharan Africa	4.7	3.6	3.7
Emerging market and middle-income economies	6.8	3.6	3.6
Low-income developing countries	4.1	4.8	4.9

Source: IMF (2022).

The post-Covid-19 economic policies in China differ from those implemented in 2008-2009 as the current economic environment is more uncertain, and the Chinese economy faces structural problems that require far-reaching reforms.

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China is pursuing a strategy of endogenous growth based on domestic demand and proactive industrial policies in key sectors, such as technology, to reduce its gap with advanced market economies. The US decoupling strategy aims to reduce China's dependence and prevent it from acquiring advanced technologies. Still, China has responded with the idea of a "dual circuit" strategy, maintaining and strengthening its economic links with the outside world while pursuing its own needs and objectives. Implementing these strategies will take time and bring challenges, such as supporting the consumption and income of the Chinese population, achieving technological independence, and maintaining and strengthening economic links with the rest of the world.

Conclusion

The impact of the COVID-19 pandemic on global economic growth, the pace of recovery, and the economic and social costs are still uncertain. The latest WTO forecasts are more pessimistic and predict a shorter but regionally differentiated recession. Decoupling between the US and China is being initiated by the US. Still, it is difficult to imagine a total decoupling as there are strong dependencies, particularly in the US economy, on Chinese imports. If decoupling is implemented, it will be felt more severely in China and could halt the rise of firms that have been able to move upmarket and escape the middle-income trap. Maintaining international value chains will become more complicated, more expensive, and riskier. Promoting domestic demand in China will also confront major political and social issues.

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