

# China Economic Update August 2024

## More of the same: Third Plenum shows little appetite for needed reform in China

### NAB Group Economics



In mid-July, the 20th Central Committee of the Communist Party of China held its third plenary session (or Third Plenum) – a key policy meeting in each five year political cycle. Any hopes that China’s government may seek reforms to support the demand side of the economy were disappointed, with the announced proposals doubling down on supply side policies that risk further trade tensions with the United States and European Union.

### The 2013 reforms fell short of their ambition

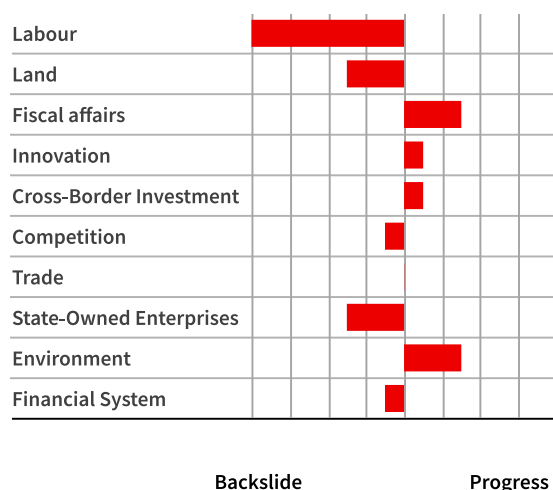
Over recent decades, the Third Plenum has become widely associated with economic policy and reform. This reputation was built on the Third Plenum of 1978, where Deng Xiaoping’s reforms commenced China’s opening up and modernisation period and, to a lesser extent, Jiang Zemin’s reforms in 1993 that culminated in China’s accession to the World Trade Organization in 2001. There were high expectations following the Third Plenum of 2013, when Xi Jinping announced a broad reform agenda to be implemented by 2020. These proposals came at a critical time, given a long identified need to transition China’s model of growth away from investment and towards consumption and given that China’s working age population had already peaked (meaning that demographics were set to become an increasing drag on the economy).

The subsequent record in implementing these policies was at best mixed. In its final assessment of the 2013 reforms against the 2020 target, the Asia Society and Rhodium Group divided the 2013 reforms into ten dimensions, finding that four categories (the environment, fiscal affairs, innovation and cross-border investment) had seen modest advancement, while the other six had either gone backwards or, at best, stalled.

### Third Plenum 2013 reforms

#### Limited progress on ambitious reform agenda

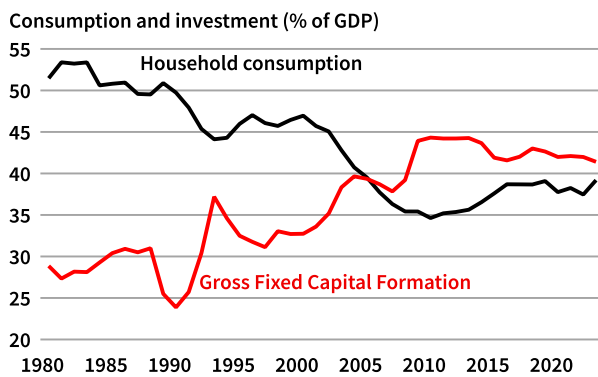
Asia Society & Rhodium assessment of 2013 reforms



Similarly, the Council on Geostrategy divided the 2013 reforms into four categories (which they noted had considerable overlap) – namely the relationship between the state and the market; state-owned enterprise reform; fiscal reform (particularly taxation and local versus central government budgets) and labour mobility. The organisation’s assessment was that China had failed to successfully implement the outlined reforms in these dimensions and that the unsustainable growth model remained largely unchanged – with China’s economy overly reliant on investment, with the consumption share too low.

## China's consumption

### Consumption share of economy remains low



It is important to note that these assessments are contrary to the Communist Party's own view. The opening of the main report from the 2024 Third Plenum (typically abbreviated to "the Decision") simply states that "we have accomplished the reform tasks set at the third plenary session of the 18th Central Committee".

### What is in this year's Decision?

A key emphasis of this year's Third Plenum was national security – both in terms of maintaining the Party's control over governing the country and directing development but also with respect to key inputs and resources – with President Xi noting that in many advanced manufacturing sectors, China remains reliant on technologies that are controlled by other countries. This has been particularly notable in recent times with the US attempting to restrict China's access to high end semi-conductor technology. Many observers have noted that President Xi views economic policy and national security as being entwined.

As a result, there was considerable focus on industrial policy – particularly in encouraging investment in high tech manufacturing commonly described as "new productive forces" to further strengthen China's supply side. These industries are not explicitly defined, but are understood to include sectors such as electric vehicles, batteries and renewable technologies such as solar panels and other green energy. It is worth highlighting that many of these industries have been targeted for tariff increases in the United States and European Union in recent months based on accusations of overcapacity, unfair subsidies and the need to protect domestic manufacturers. China's pledges to increase investment in these sectors – that are already producing well beyond what the domestic economy can consume – are only likely to intensify trade tensions with other major economies.

A range of other measures appear to echo the 2013 reform agenda. These include references to the market

playing the decisive role in resource allocation within China's economy and leveling the playing field for private firms competing with state-owned enterprises (SOEs). However, much like 2013, it also proposes to further invest in SOEs to ensure that they "get stronger, do better, and grow bigger, with their core functions and core competitiveness enhanced".

Broadly the focus of measures announced in the Third Plenum fall on the supply side of China's economy – despite the long identified need to evolve the country's growth model towards consumption. There may be some modest gains from further reforms to China's household registration (or hukou) system, that would provide migrant workers with access to social services in the cities of their residence. As migrant workers typically save a large proportion of their income, improved service provision may boost their consumption, but as comparatively lower income earners, gains to China's economy are likely to be marginal (particularly as many cities have already implemented similar measures).

### Conclusions

Chinese leaders have long identified the need to transition its economy towards consumption. In December 2004, then Premier Wen Jiabao announced a plan to facilitate this transition, however the household consumption share of GDP has fallen below the level recorded in 2004 – 40.7% – in every subsequent year.

China's household savings rate (in excess of 35% of disposable income in 2022) is way above advanced economy trends, however this in part reflects an inadequate social safety net – meaning that savings are in part self-insurance for periods of unemployment or retirement. Developing a stronger social security system would likely boost consumption, however Chinese authorities appear to have an ideological opposition to such a measure.

Ideology may also explain why the Third Plenum appears to double down on supply side policies. The Asia Society notes in its assessment of the Plenum and its accompanying documentation that President Xi firmly believes that this is the correct course, that poor progress on his agenda of "high quality development" announced in 2017 is due to poor implementation at the local level and that there is less need for internal debate within the party.

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