China Faces Pressure To Reverse Economic Slump

Elaine Kurtenbach, Joe McDonald, AP Business Writers

BEIJING (AP) — Gao Runping, who makes mechanical components for the oil industry, founded his business in the central city of Taiyuan with equipment bought from failing companies after the 2008 global crisis.

Now, with China's economy cooling abruptly again, Gao sees another wave of bankruptcies about to hit his industry.

"I can see about one-fifth to one-third of the factories are about to close, and owners are preparing to sell off their equipment," said Gao, general manager of Taiyuan Fanhe Engineering Co.

China's economic growth has decelerated from overheated to slower than Beijing wanted in just half a year as export demand and consumer spending at home weaken, raising the threat of job losses and possible unrest.

Chinese leaders are gradually reversing course after spending the past two years trying to cool growth and inflation. They are easing lending curbs and are expected to take other steps to shore up growth that fell to a nearly three-year low of 8.1 percent in the first quarter and is slowing further.

But they are moving cautiously after the stimulus that helped China avoid the 2008 crisis fueled inflation and a wasteful building boom.

"Everybody realized the stimulus was excessive," said UBS economist Tao Wang. "This time, I think the government will be more cautious and more prudent."

The slowdown adds to challenges for the Communist Party ahead of a once-a-decade handover of power to younger leaders this year. It follows a scandal over disgraced politician Bo Xilai and the embarrassment of a U.S.-Chinese high-level dialogue overshadowed by a standoff over a blind legal activist, Chen Guangcheng.

On Saturday, regulators reduced minimum reserves banks are required to hold in a move that frees up money for lending. Analysts said, though, that was in line with earlier plans and was unlikely to dramatically expand borrowing due to weak demand for credit.

That came after factory output in April plunged to its lowest level since the 2008 crisis and consumer spending, home sales and bank lending were unexpectedly weak, jarring hopes for a "soft landing" with growth rebounding as early as midyear.

Power consumption, an indicator of overall economic activity, rose just 3.7 percent in April over a year ago, compared with 7 percent in March, the National Energy Administration reported Tuesday.

The first quarter "was pretty anemic, and I think that is likely to get worse," said Eric Fishwick, head of economic research for Hong Kong-based investment bank CLSA.

The figures have prompted some analysts to trim their growth outlook for this year, though to still-robust levels of 8 to 9 percent. The World Bank and International Monetary Fund are forecasting growth this year at 8.2 percent.

Adding to the gloom, sales of home appliances during the weeklong May Day holiday were down 30 to 40 percent from a year earlier, according to the newspaper China Business Journal.

Planners face a conflict between immediate growth needs and Beijing's long-term effort to reduce heavy reliance on exports and investment and create a more self-sustaining, consumer-based Chinese economy.

A quick way to pump money into the economy is through more spending on building highways and other public works. But authorities are reluctant to do that again after the 2008 stimulus left local governments that splurged on new roads, buildings and other projects with heavy debts to state banks that some may be unable to repay.

The flood of money also set off stock market and real estate speculation, forcing up politically sensitive housing costs. Inflation spiked to a 37-month high of 6.5 percent last July, with food prices surging 14.8 percent, before subsiding to 3.4 percent in April, below the government's 4 percent target for the year.

Instead, authorities are likely to take carefully controlled steps to spend a small amount more on infrastructure, encourage more building of low-cost housing and nudge up bank lending, said Wang of UBS.

The government began easing controls late last year after global demand for Chinese goods weakened. Beijing promised more lending to small and private companies and eased a moratorium on loans to developers of lower-priced housing.

"So far, either these measures have not come out as quickly or have not had as much effect" as Beijing wanted, Wang said. "So I think the government, along the lines of modest easing, will do a little bit more."

Real estate poses another dilemma. The industry traditionally has been China's biggest growth driver, fueling spending on construction and home furnishings. But high housing costs divert money away from consumer spending that Chinese leaders are trying to encourage and are politically dangerous for the ruling Communist Party by eroding economic gains that underpin its claim to power.

Premier Wen Jiabao affirmed Beijing's resolve to keep most controls on real estate in place, saying in March that while prices had eased slightly from their mid-2011 highs, they were still far above "reasonable levels."

"The authorities have just not found a new industry is big enough to replace the vigor that the real estate industry had for boosting the economy," said Song Huiyong, director of research for Shanghai Centaline Property, a real estate broker.

"The authorities just want to stall for time," Song said.

Other policies used in 2008, such as subsidies for appliance purchases by rural families, have run out of steam and left producers with excess manufacturing capacity.

Beijing might be reacting too slowly, said Dariusz Kowalczyk, senior economist for Credit Agricole CIB in Hong Kong, in a report this week.

Policymakers "are increasingly looking behind the curve," Kowalczyk said. "Insistence that a growth slowdown is the price to pay for structural reforms makes sense in the long run, but — if taken too far — it threatens the medium-term growth targets."

China's struggling entrepreneurs are likely to be of little help in boosting demand as they put off investment amid plunging revenues.

Entrepreneurs that survived the 2008 crisis, which forced thousands of export-dependent factories to close, began to feel a new chill last autumn as global demand sagged. The slump has spread inland as domestic demand also weakens.

"We are getting fewer business inquiries. Market demand is weaker and we have less room for profit," said Gao, the manufacturer of oil equipment in Taiyuan.

Orders by foreign buyers at the spring session of the Canton Trade Fair, the country's biggest annual export sales event, were down 4.8 percent from a year earlier, the government newspaper China Daily reported.

In Wenzhou, a southeastern hub for private business, entrepreneurs cannot get credit from state banks, said Zhou Dewen, head of a small business association. That is despite a pledge by Beijing to increase private sector lending there after a wave of defaults last year by borrowers who were forced to turn to underground lenders.

"Businesspeople should brace themselves for hard times," Zhou said. "I don't think the situation will improve this year, but let's see how it will go next year."

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