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The Impact of World Economic Crisis on China Economy

Introduction

In 2008, a series of bank and insurance company failures triggered a financial crisis that effectively halted global credit markets and required unprecedented government intervention. Fannie Mae (FNM) and Freddie Mac (FRE) were both taken over by the government. Lehman Brothers declared bankruptcy on September 14th after failing to find a buyer. Bank of America agreed to purchase Merrill Lynch (MER), and American International Group (AIG)was saved by an $85 billion capital injection by the federal government. Shortly after, on September 25th, J P Morgan Chase (JPM) agreed to purchase the assets of Washington Mutual (WM) in what was the biggest bank failure in history. In fact, by September 17, 2008, more public corporations had filed for bankruptcy in the U.S. than in all of 2007. These failures caused a crisis of confidence that made banks reluctant to lend money amongst themselves, or for that matter, to anyone. Asian financial institutions had little exposure to the esoteric financial instruments that have sent the world markets into spiral. This is largely due to the fact that having experienced their own financial crisis ten years earlier, firms learned to take a more measured risk management approach, relying less on leverage and maintaining higher liquidity ratios. As a result, Asian firms (particular in Japan) have been well positioned to make strategic investments in the finance industry (with Mitsubishi UFJ buying a 21% stake in Morgan Stanley and Nomura Holdings Inc ADR (NMR) purchasing Lehman's Asia platform). Even so, Asian governments are aware that their countries are not immune to general market dynamics and witnessed their stock markets dip as banks, fearful of counterparty risk, constricted credit. Moving in lock step with Europe, the governments of Hong Kong, Malaysia, and Singapore then responded by guaranteeing all bank deposits in their respective countries to prevent runs on the banking system. The government of South Korea, Asia's fourth largest economy, unveiled a $130 billion bailout plan designed to help its banks pay international debts.

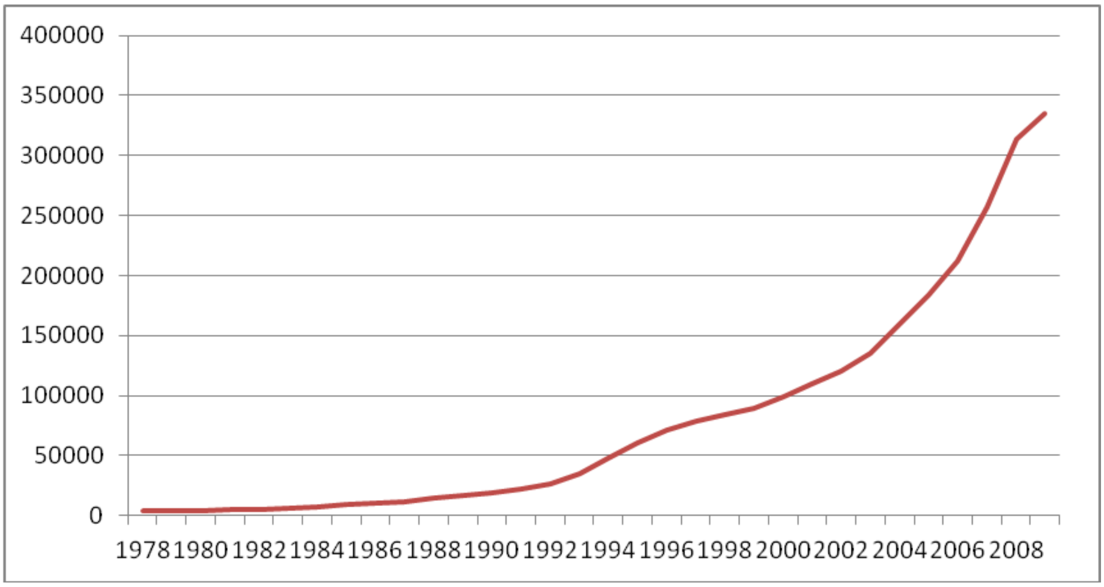
Such measures were considered necessary because the won has fallen to a 10 year low, placing strains on local institutions that borrow in dollars from international institutions. The world's attention has focused on the biggest country in the far east — China. Can China survive the current economic crisis? The answer is yes; china can not only survive, but thrive in the very challenging economic environment brought about by the collapsing US economy. And like most such challenges, there is, in fact a great opportunity for China in this mess. This paper analysis the impact of economic crisis on China and also further explicate the resolution against the economic crisis.

Statistics of the China's economy

China's economy during the past 30 years has changed from a centrally planned system that was largely closed to international trade to a more market-oriented economy that has a rapidly growing private sector and is a major player in the global economy. Reforms started in the late 1970s with the phasing out of collectivized agriculture, and expanded to include the gradual liberalization of prices, fiscal decentralization, increased autonomy for state enterprises, the foundation of a diversified banking system, the development of stock markets, the rapid growth of the non-state sector, and the opening to foreign trade and investment. Annual inflows of foreign direct investment rose to nearly $108 billion in 2008. Here are some set of statics that display the economic achievement over the past 30 years.

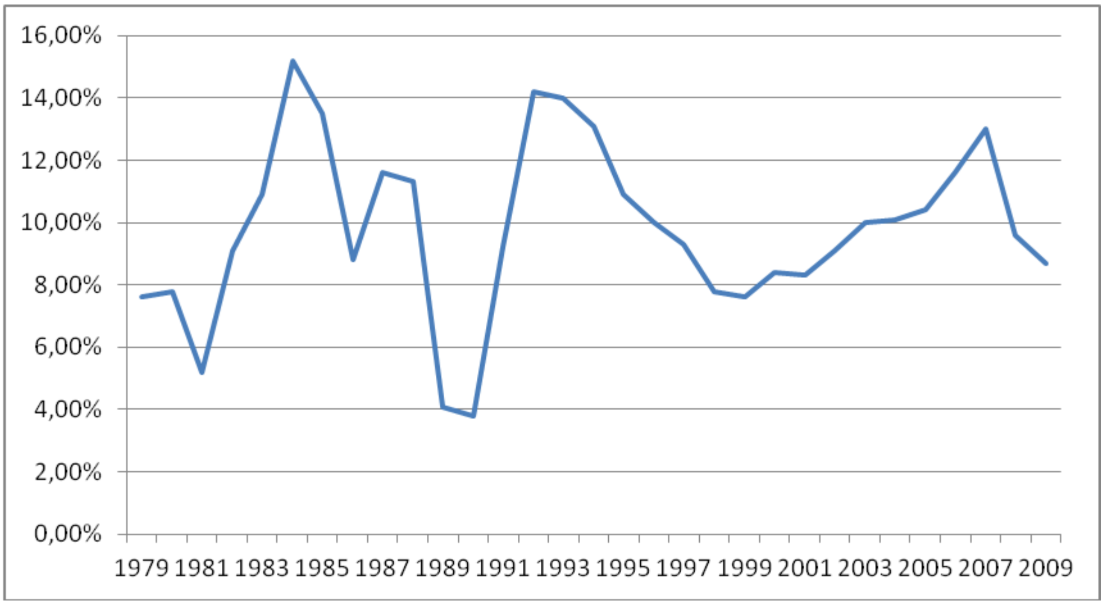
G.D.P. over the past 30 years (100 million yuan)

The GDP of China in 2009 reached 493 billion US dollars



Source: www.stats.gov.cn

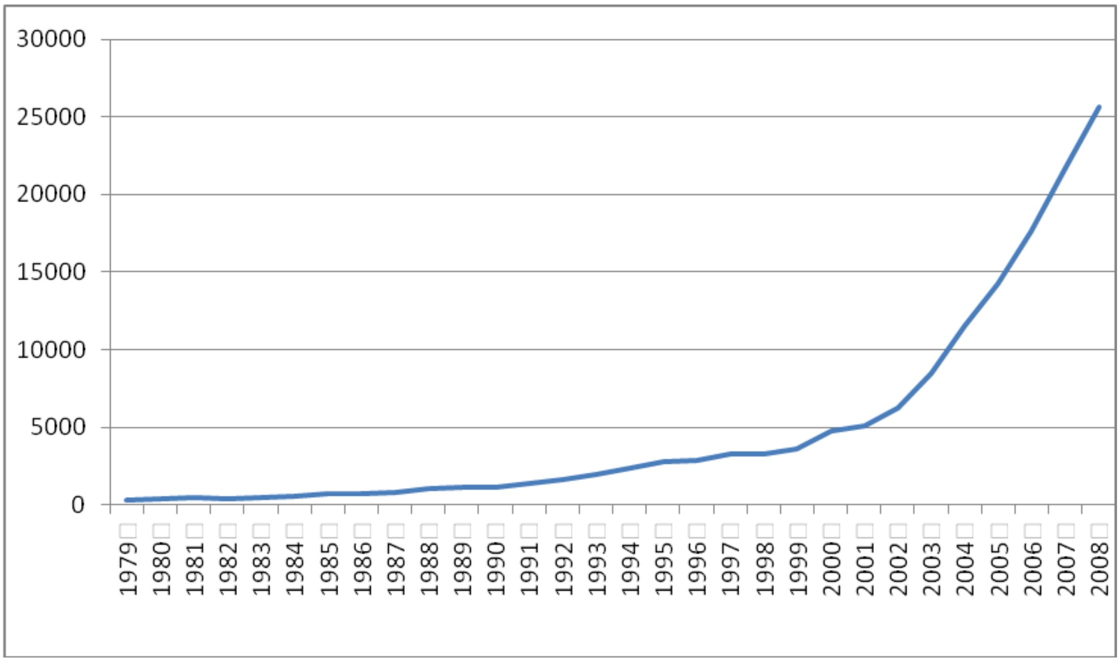
The growth rate of GDP over the past 30 years



Source: www.stats.gov.cn

Import and Export value from 1979 to 2008

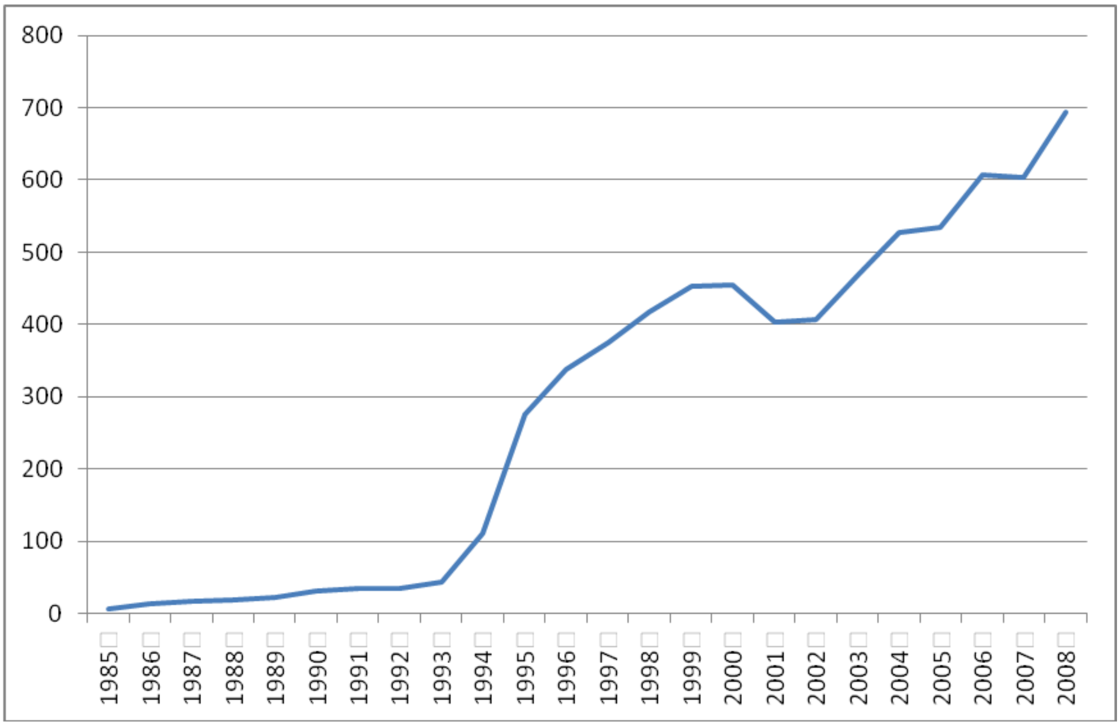
2009 Total value is 2207 billion US dollars decreased by 13.9%



Source: www.stats.gov.cn

Foreign direct investment from 1979 to 2008

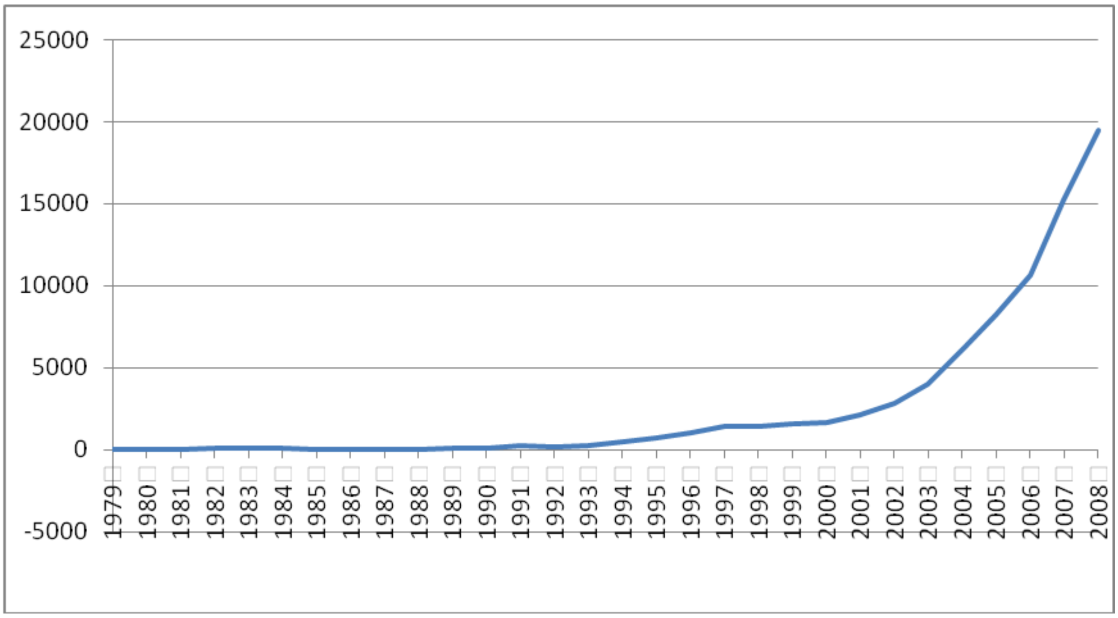
2009 Total value of foreign direct investment is 90 billion US dollars



Source: www.stats.gov.cn

Foreign exchange reserve from 1979 to 2008

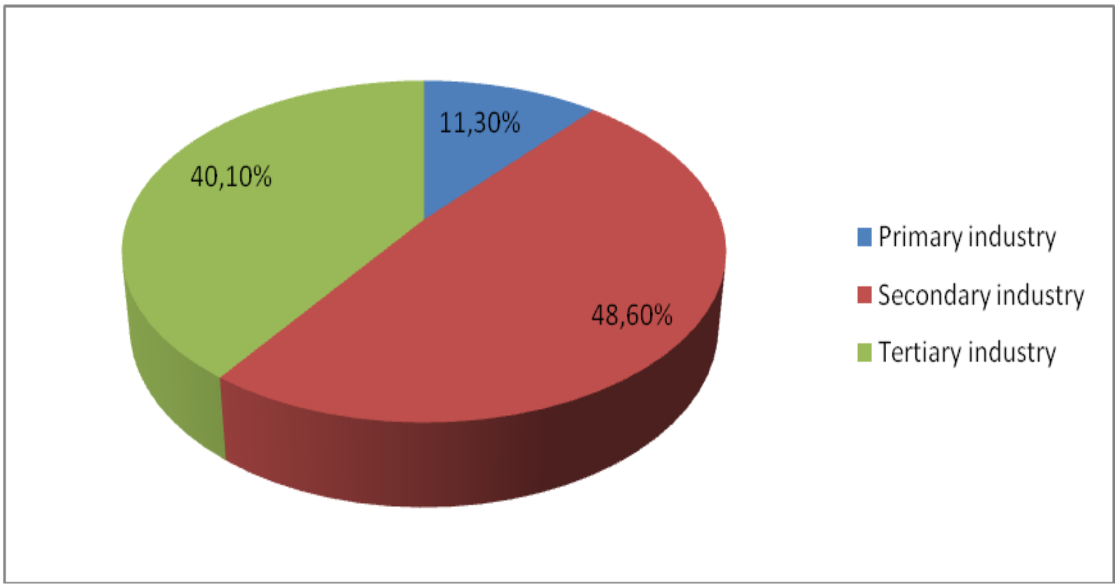
Total value of Foreign exchange reserve in 2009 is 2400 billion US dollars



Source: www.stats.gov.cn

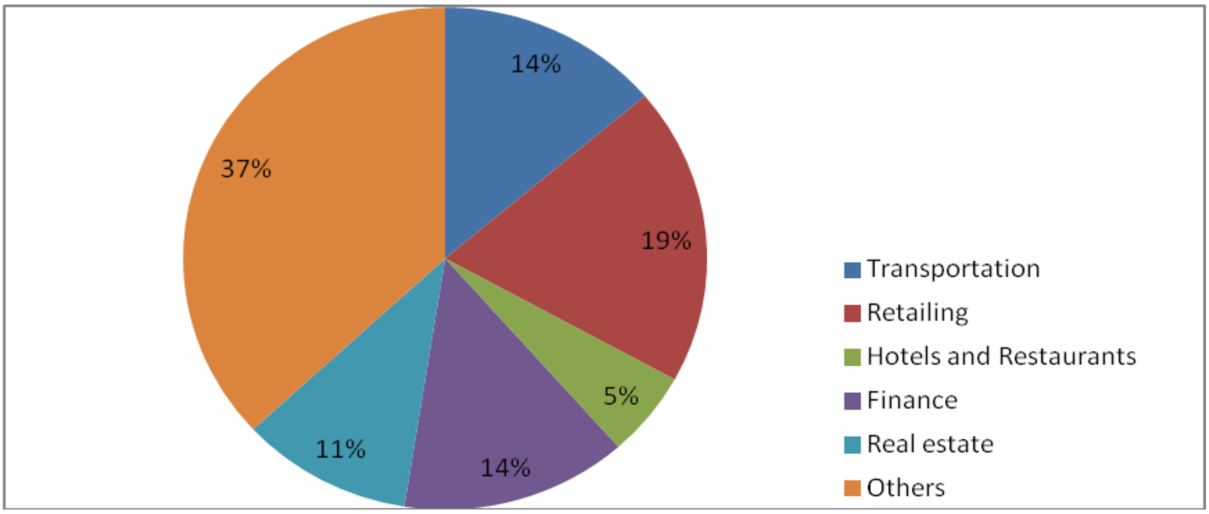
From the statistic listed above, we can see that china has under through rapid growth period over the past 30 years. Although it's GDP per capita still rank 104th in the world, it's GDP and foreign trade value has reached top 3 places in the world. Especially China now is the No.1 foreign exchange reserve country and this April China has surpass Germany, become the No.1 country in exportation. But when we look at the GDP according to value added by industries in 2009, it indicates that the secondary industries still occupied too much proportion, basically if China wants to keep 8% of growth rate, the country needs to restructure its GDP. Tertiary industry still needs developed. The pie chart below show the GDP according to value added by industries.

GDP according to value added by industries



Source: www.stats.gov.cn

Tertiary industry distribution in 2009



Source: www.stats.gov.cn

The impacts on foreign trade

The economic situation during the year 2008 indicates the fact that the global economic situation will not be revival instantly. China was facing an even greater challenge at that time, especially in the foreign trade section. The direct impact on the foreign are basically divided in to three aspects.

1. The slowdown of the global economy has decreased china's external demand.

Due to the subprime mortgage crisis, the global economy has slow down the economic growth; a turbulent period of the financial market cannot be avoided. The rise of oil and grain price further increased the pressure of global inflation. There is no doubt that the global economy is going through a relatively cold period. It is estimated that every 1% drop of growth rate in U. S. will lead to 4.75% drop in the china's exportation value; 1% drop of growth rate in EU, will lead to 1.5% drop of electronic production and 0.5% drop of textile production in the total value of exportation. For the first eight month, our exportation growth rate to U.S. and EU are 26.3% and 10.6% respectively. On year-on-year basis dropped by 5% and 6.1% separately. Owing to the drop of growth rate in the major export partner, our exportation has decreased on year-on-year basis. From January to August our exportation value reached 937.6 billion dollars, which decreased 5.3% compare to last year.

Overview of the import and export value in 2009 billion $

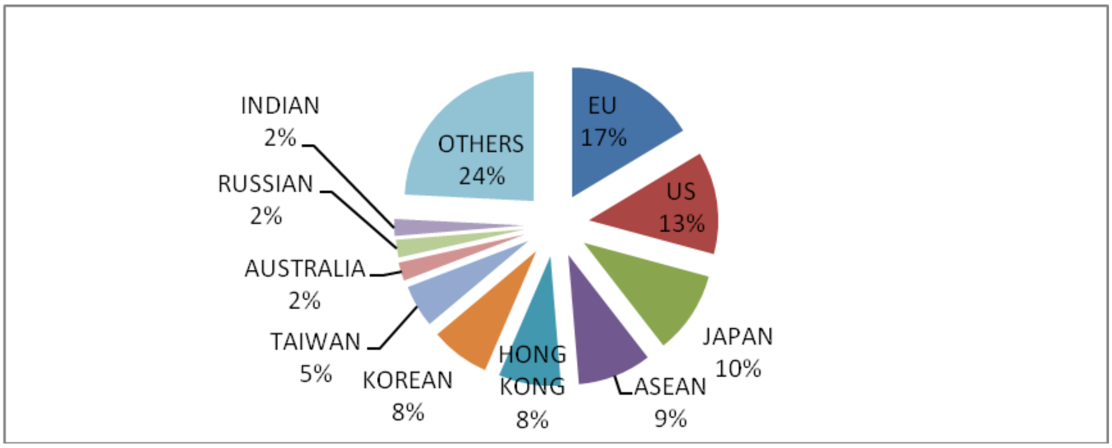
total value	Growth rate	import	growth rate	export	growth rate	trade surplus	growth rate
2207	-13.90%	1005	-11.20%	1201	-16%	196	-34.2%

Unit: 10000 US dollars						
Country（region）	total value	export value	import value	growth rate on year-on-year basis		
				total	export	import
Total	2,561,632,045	1,428,545,709	1,133,086,336	17.8	17.2	18.5
EU	54,294,143	36,627,939	17,604,090	21.2	21.7	20.2
EU （ 27 countries）	42,557,769	29,287,820	13,269,950	19.5	19.5	19.6
EU （ 15 countries）	38,731,804	26,068,485	12,663,320	18.3	17.8	19.5
C.I.S.	9,841,428	6,421,822	3,357,491	29.5	34.4	21.1
Russian	5,683,054	3,300,543	2,382,511	18.0	15.9	21.0
U.S.	33,373,763	25,229,734	8,144,029	10.5	8.4	17.4
Japan	26,678,510	11,613,414	15,065,095	13.0	13.8	12.5
EU 27 countries）	42,557,769	29,287,820	13,269,950	19.5	19.5	19.6
EU （ 15 countries）	38,731,804	26,068,485	12,663,320	18.3	17.8	19.5
Germany	11,500,901	5,917,408	5,583,493	22.2	21.5	23.0
Netherlands	5,121,109	4,591,040	530,069	10.5	10.8	7.6
UK	4,562,363	3,606,866	955,497	15.7	13.9	22.9
France	3,894,363	2,330,394	1,563,970	15.7	14.6	17.2
Italy	3,825,570	2,660,848	1,164,723	21.9	25.7	14.1
Spain	2,616,552	2,074,160	542,392	24.8	25.5	22.4
Belgium	2,019,652	1,485,841	533,810	14.4	17.2	7.3
Finland	1,086,129	733,149	352,980	4.9	11.7	-7.0
Sweden	1,015,441	511,491	503,950	16.8	12.4	21.7
Denmark	816,570	556,918	259,652	27.3	21.3	42.4
Ireland	707,046	432,341	274,706	11.1	-2.6	42.7
Austria	488,471	177,147	311,324	22.0	14.1	27.0
Greek	423,645	405,016	18,629	23.7	24.5	9.3
Luxemburg	384,856	355,457	29,399	67.0	73.1	16.8
Portugal	269,137	230,411	38,726	21.7	26.2	0.7
Newly joined EU countries	3,825,965	3,019,335	606,630	32.8	34.9	22.5
Poland	1,042,931	903,675	139,256	36.1	37.9	25.2
Hungary	747,669	409,454	138,215	20.1	21.5	14.2
Czech Republic	650,576	550,274	100,302	31.0	33.1	20.7
Romania	321,193	285,127	36,066	35.8	36.8	28.1
Slovakia	294,946	196,621	98,325	33.7	33.7	33.7
Marta	151,517	106,527	44,990	115.4	225.3	19.7
Bulgaria	132,810	111,132	21,678	36.8	36.8	37.2
Cyprus	113,411	112,353	1,059	60.7	61.0	32.0
Lithuania	108,720	105,806	2,914	32.3	31.9	440.0
Slovenia	108,273	95,117	13,156	34.8	37.3	19.0
Latvia	86,452	84,651	1,801	22.4	23.7	-16.2
Estonia	67,468	58,599	8,869	0.0	0.2	-1.3

Source: www.stats.gov.cn

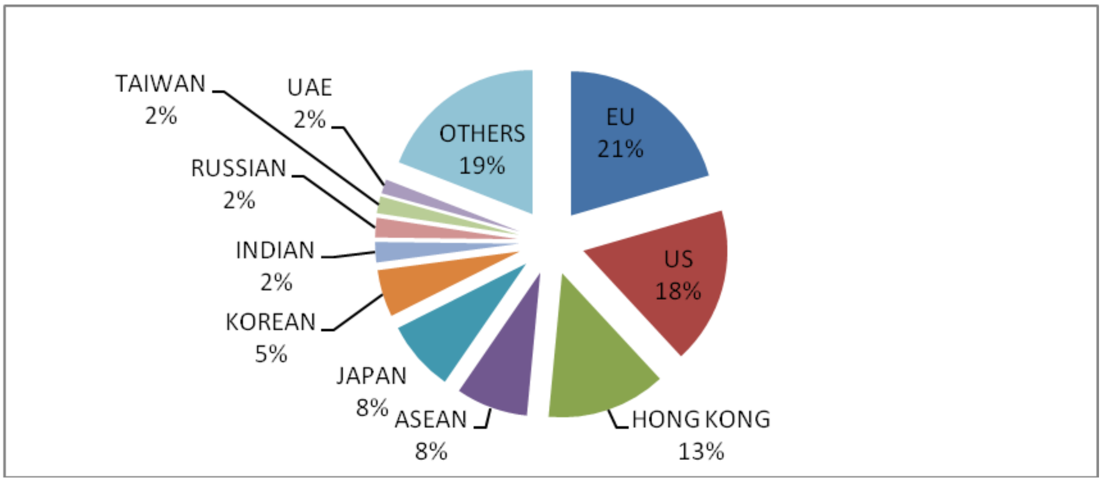
The above data show the detail information of foreign trade between China and European Union Countries, as we can see that China has a strong connection with EU especially EU 15 countries, and there is also a rapid growth in the newly joined EU countries. In the chart listed Poland rank the 1st place and has a growth rate of 36%, indicates that the east EU market is playing very import roles in foreign trade between China. And the pie chart below shows the proportion of the trading partners with China.

TOP TEN FOREIGN TRADE PARTNERS



Source: www.stats.gov.cn

TOP TEN MARKET FOR EXPORTATION



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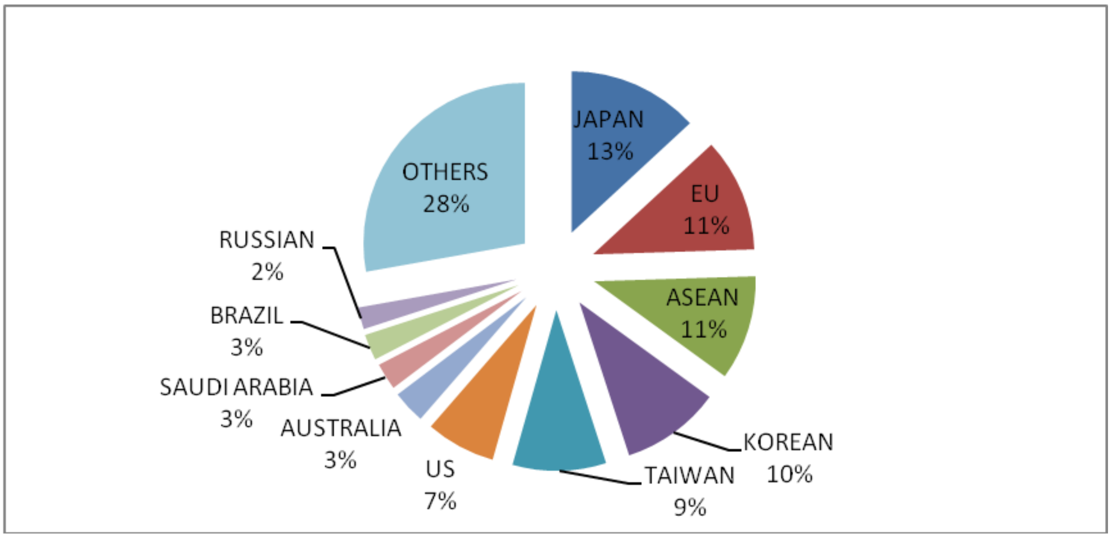
TOP TEN MARKET FOR IMPORATION



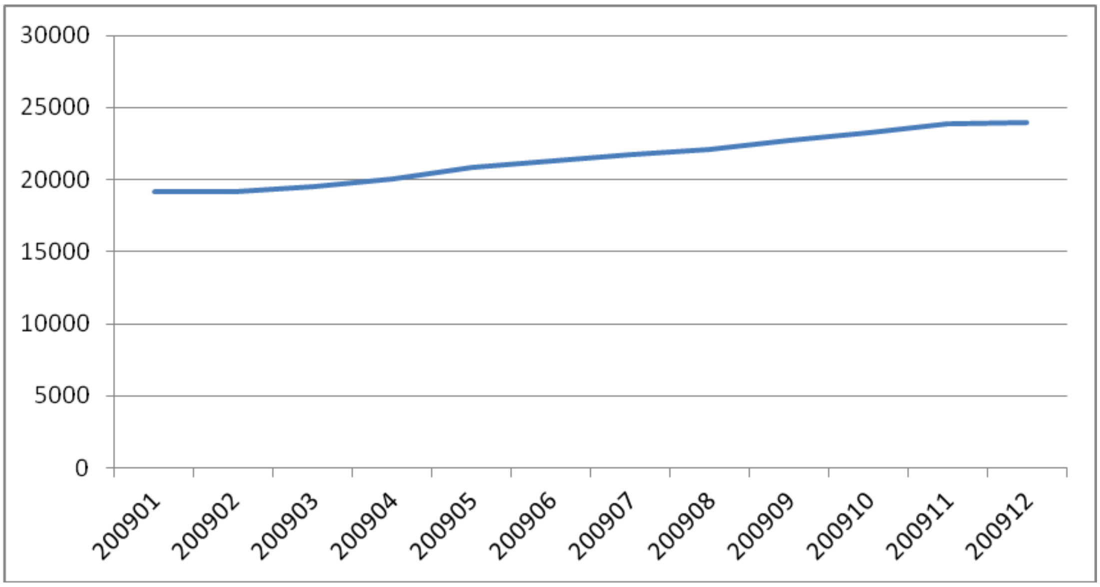
Source: www.stats.gov.cn

We can conclude from the data above that EU and U.S has quiet important position in China's foreign trade, due to the Chinese cheaper labor market and well-constructed local facilities such as highway and tariff-free zone. So there would be no doubt that the subprime crisis deeply decreased the import and export value since China is well connected with the global market.

2. The subprime crisis leads to the appreciation of RMB.

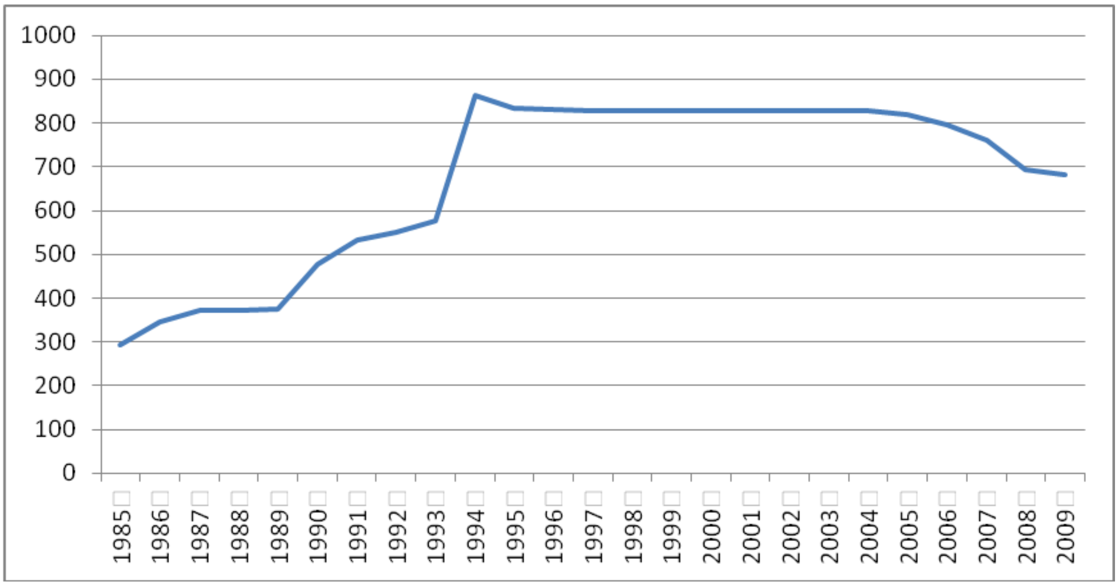
In order to take proper resolution against the crisis, the American Federal Reserve committee has reduced the interest to provide capital movement for the bank which triggered the depreciation of the US dollars and further leads to the appreciation of RMB. Since 1992, the exchange of US dollars has increased by 21%, nevertheless from in 2008, January to August the exchange rate has increased by 6.88%. There are majorly two negative aspects toward the appreciation of our currency: On the one hand, price superiority of the export products will be weakened and due to the unpredicted global market, enterprise are not willing to take massive orders from other country; on the other hand, reducing the cost of the imported goods are quiet helpful for importation. From January to August 2008, the import value has increased by 48.5%, increased by 23.3% on year-on-year basis.

Foreign exchange reserve during the financial crisis



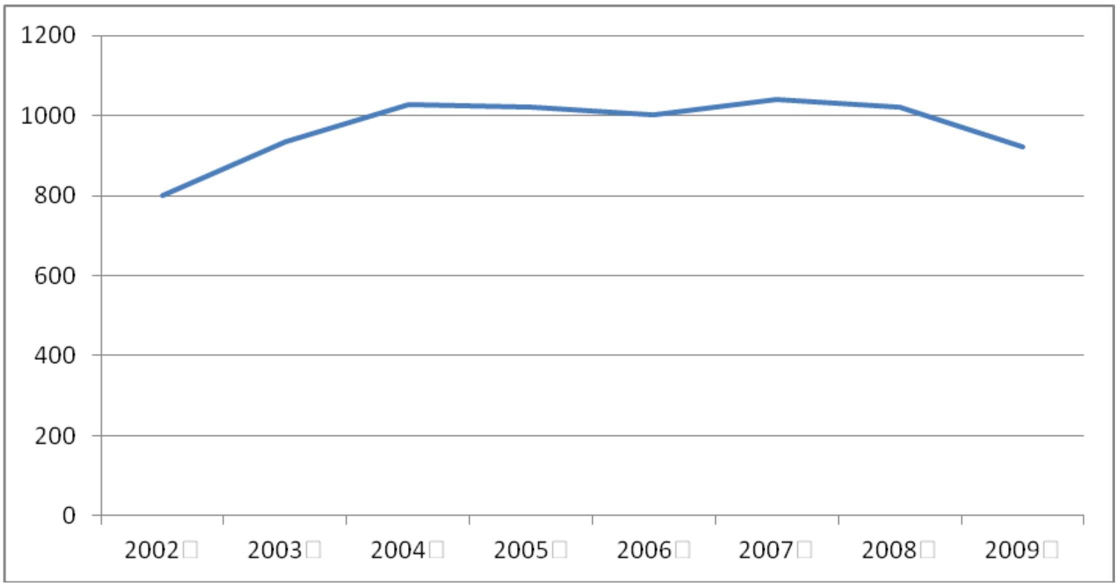
http://www.pbc.gov.cn

RMB exchange rate with US dollars



Source: www.stats.gov.cn

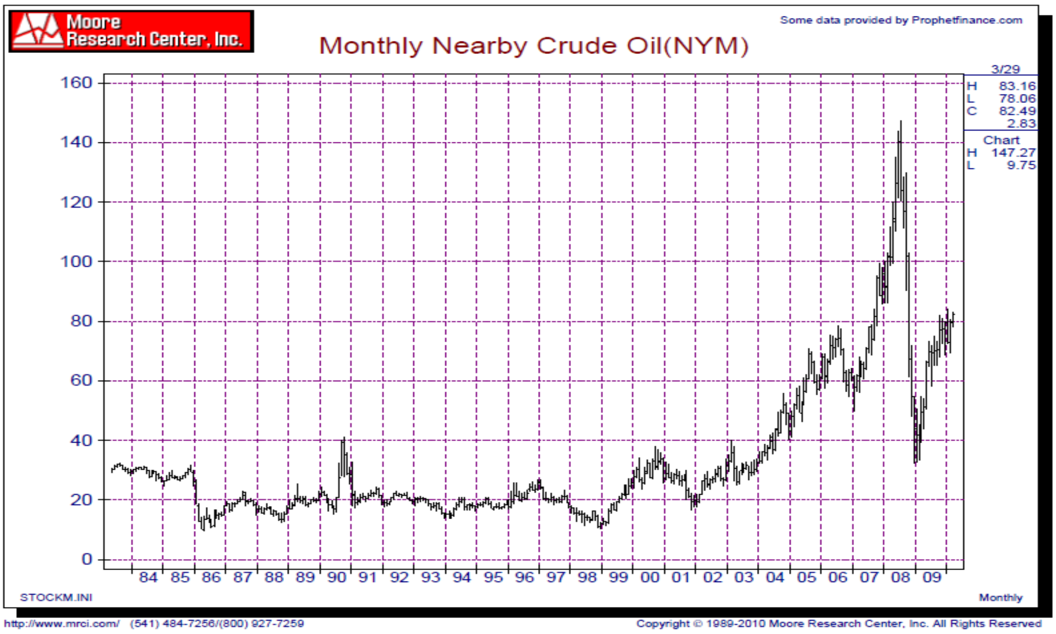
RMB exchange rate with EURO

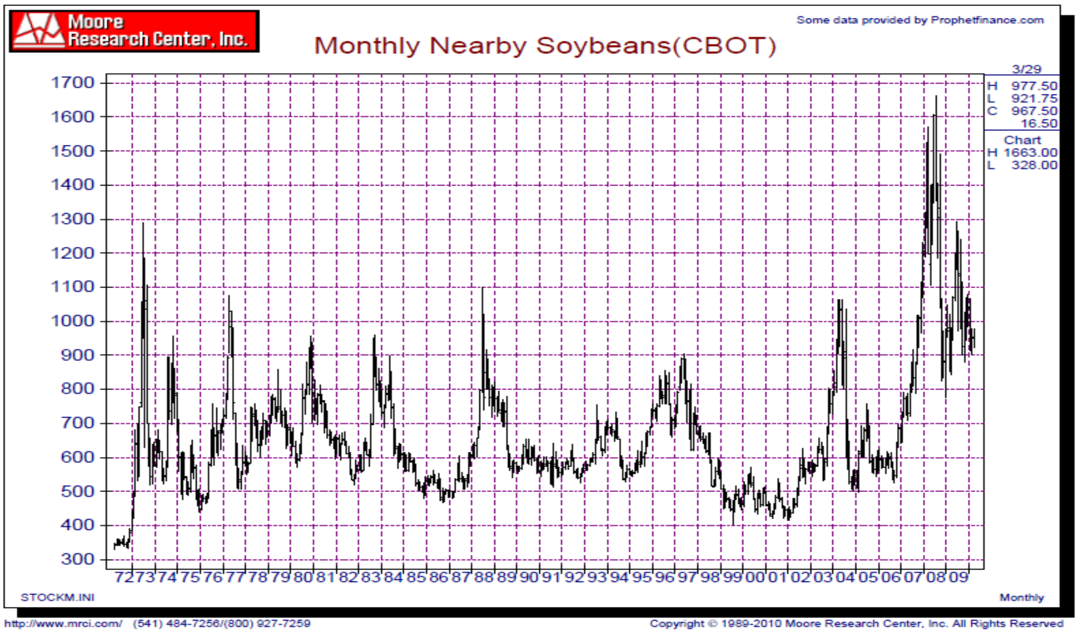


Source: www.stats.gov.cn

3. The cost of the primary products rises due to the subprime crisis and further result to the rise of the cost of foreign trade.

Since 2002, along with the excess of global liquidity and the depreciating of US dollars, the price of the primary products in the global market has raisin over the past years. For one thing, the financial crisis prevent the international fluid capital to find opportunity to invest in the financial market, for the purpose of avoiding high risks and profits, they turned themselves in to the commodity futures, huge amount of capital streamed into the market and causing the price of oil and grain keeping rising and later result the global inflation. And due to the current fact, that china has a great dependence over the exportation of primary products. Negative effects are quiet obvious, for one thing, the cost of imported good has risen, the first 8 month our primary products importation has increased by 71.2%, 47.5% higher than the record last year. And the price of imported good also increased vastly. Let us take at look at the chart below, both chart shows the price of crude oil and soybeans we can see that the price has been risen up since 2007 and reached to the top in 2008.





Iron sand	77.90%
Oil	91.70%
Coal	64.90%
Soy bean	79.20%

Also the price of iron sand and coal has increased by 77.9% and 64.9%. For another reason, export enterprises have harder situation to survive during this period of time. They are facing the challenge of less profit margin due to the cost of raw materials keep rising. It is estimated that nearly more than 2000 small trading company was being closed during the financial crisis.

The impact on financial market

1. The direct impact from the subprime financial crisis has relatively small influence.

There were only 3 major banks that brought the subprime related financial product which are: Bank of China, Industrial and Commercial Bank of China, and China Construction Bank. According to data published by the official authority, till December 31, 2007 the value of their mortgage related to subprime crisis are 4.9, 1.26 and 1.06 billion dollars accordingly. Compare to their total assets such debt are not quiet critical.

	mortgage value	rating	percentage of total assets	percentage of total stock capital
ICBC	1.226 billion dollars	AA-	0.1%	2.68%
BC	4.9 billion dollars	AAA	0.6%	14.36
CCB	1.06 billion dollars	AA	0.117%	3.2%

Take Bank of China as an example, the total mortgage that bank holds converted to RMB is 36.5 billion yuan, but according to the financial statistics in 2007, their profits after taxes could reach 56.02 billion yuan. Even they will lose the total assets of their mortgage; they would not have a big loss by the end of the year. Consider ICBC and CCB hold quiet small amount of mortgage, they wouldn't even lost more than 8% of their profits after taxes. To sum up, take into account the fact the local banks have limited capacity of holding foreign debt, not mention using the leverage effect, the losses are generally speaking under controlled and will not cause further financial problems.

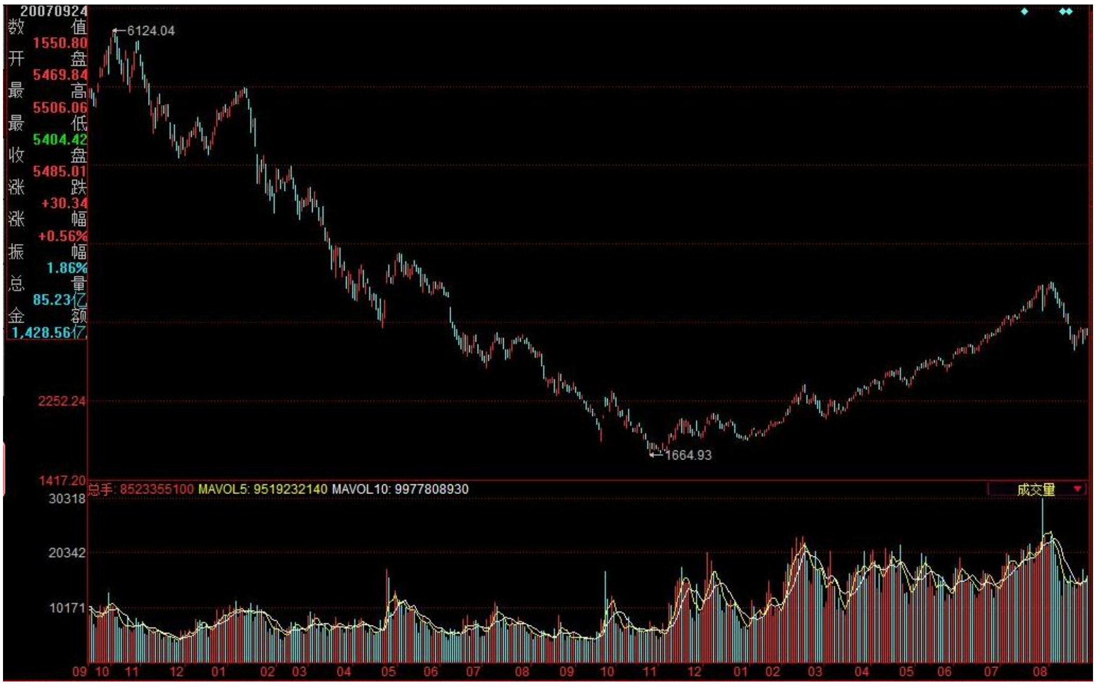
2. The financial crisis deeply dropped the local investor's confidence toward the future market.

When numerous global financial institutions were dragged by the subprime crisis, global investors' confidence on the financial market will not remain the same, this will further lead to a huge damage to the financial environment. Due to the fact that some of our local banks hold oversea business, such drop of investor's confidence will surely affect the local market. It is estimated that the longer the financial crisis lasts the great damage the Chinese financial environment will suffer. Although the local financial institution has less influence from the mortgage losses, according to a recent financial data on the Chinese stock market, financial section, which is one of the most valuable sections, for a time lead the market index goes down directly. Such phenomena indicate that the local investors do not have sufficient confidence toward the future situation. 3 major banks stock index dropped over 40%, especially in the H-share which dropped 45%. Here are the list of the stock performance during the financial crisis.

	BEFORE FINANCIAL CRISIS	DURING THE FINANCIAL CRISIS	DROP RANGE
ICBC A-Shares	9 YUAN	5.3 YUAN	-41.11%
ICBC H-Shares	7.49 HK DOLLARS	4 HK DOLLARS	-46.60%
BC A-Shares	7.58 YUAN	4.78 YUAN	-36.94%
BC H-Shares	5.27 HK DOLLARS	2.91 HK DOLLARS	-44.78%
CCB A-Shares	11.58 YUAN	6.82 YUAN	-41.10%
CCB H-Shares	8.97 HK DOLLARS	4.36 HK DOLLARS	-51.39%

日线 工商银行
9.00
3.13
总手: 1597320 MAVOL5: 2935629 MAVOL10: 3618711
成交量
07 08 09 10 11 12 01 02 03 04 05 06 07 08 09 10 11 12 01 02 03 04 05 06 07 08 09 10 11 12 01 02 03 04

日线 中国银行
7.58
2.82
总手: 1410953 MAVOL5: 1324929 MAVOL10: 1285014
成交量
08 09 10 11 12 01 02 03 04 05 06 07 08 09 10 11 12 01 02 03 04 05 06 07 08



As we can easily see that since the financial crisis starts the SSE index went down rapidly to 1664 point touch the bottom, reached the lowest point in recent years. And gradually went up after then. For detail global information of financial crisis on the stock market see schedule 1

Resolutions against the economy crisis

The 2008 - 2009 Chinese economic stimulus plan is a RMB¥ 4 trillion (US$ 586 billion) stimulus package announced by the central government of the People's Republic of China on 9 November 2008 in its biggest move to stop the global financial crisis from hitting the world's third largest economy. On June 2009, the World Bank raised its growth forecast in China for 2009 from 6.5% to 7.2% amid signs that the economy is doing better than expected, which has been helped by the stimulus package. But it says the country's exports are still down, as the rest of the world struggles with the global recession. It was previously predicted in March 2009 that the Chinese economy would grow by 6.5% in 2009, several percentage points down on 2008's growth.

Announcement

A statement on the government's website said the State Council had approved a plan to invest 4 trillion yuan in infrastructure and social welfare by the end of 2010. This stimulus, equivalent to US$586 billion, represented a pledge comparable to that subsequently announced by the US, but which came from an economy only one third the size. The stimulus package will be invested in key areas such as housing, rural infrastructure, transportation, health and education, environment, industry, disaster rebuilding, income-building, tax cuts, and finance. China's export driven economy is starting to feel the impact of the economic slowdown in the United States and Europe, and the government has already cut key interest rates three times in less than two months in a bid to spur economic expansion. The stimulus package was welcomed by world leaders and analysts as larger than expected and a sign that by boosting its own economy, China is helping to stabilize the world economy.

Here are the 10 major plans:

1. Housing: Building more affordable and low-rent housing and speeding the clearing of slums. A pilot program to rebuild rural housing will expand. Nomads will be encouraged to settle down.

2. Rural infrastructure: Speeding up rural infrastructure construction. Roads and power grids in the countryside will be improved, and efforts will be stepped up to spread the use of methane and to ensure drinking water safety. This part of the plan also involves expediting the North-South water diversion project. Risky reservoirs will be reinforced. Water conservation in large-scale irrigation areas will be strengthened. Poverty relief efforts will be increased.

3. Transportation: Accelerating the expansion of the transport network. That includes more dedicated passenger rail links and coal routes. Trunk railways will be extended and more airports will be built in western areas. Urban power grids will be upgraded.

4. Health and education: Beefing up the health and medical service by improving the grass roots medical system. Accelerating the development of the cultural and education sectors and junior high school construction in rural western and central areas. More special education and cultural facilities.

5. Environment: Improving environmental protection by enhancing the construction of sewage and rubbish treatment facilities and preventing water pollution in key areas.

Accelerating green belt and natural forest planting programs. Increasing support for energy conservation and pollution-control projects.

6. Industry: Enhancing innovation and industrial restructuring and supporting the development of the high-tech and service industries.

7. Disaster rebuilding: Speeding reconstruction in the areas hit by the May 12 earthquake.

8. Incomes: Raising average incomes in rural and urban areas. Raising next year's minimum grain purchase and farm subsidies. Increasing subsidies for low-income urban residents. Increasing pension funds for enterprise employees and allowances for those receiving special services.

9. Taxes: Extending reforms in value-added tax rules to all industries, which could cut the tax corporate burden by 120 billion yuan (about 17.6 billion U.S. dollars). Technological upgrading will be encouraged.

10. Finance: Enhancing financial support to maintain economic growth. Removing loan quotas on commercial lenders. Appropriately increasing bank credit for priority projects, rural areas, smaller enterprises, technical innovation and industrial rationalization through mergers and acquisitions.

Source: Xinhua News Agency

To ensure sustainable development, the Chinese government also allocated some 210 billion yuan, or 5.3% of the stimulus package for promoting energy saving and gas emission cuts, and environmental engineering projects. Last but not least, 150 billion yuan was allocated for educational, cultural and family planning purposes. One year later, these programs seem to have been even more successful than expected.

Conclusion

China has generally implemented reforms in a gradualist or piecemeal fashion. In recent years, China has re-invigorated its support for leading state - owned enterprises in sectors it considers important to "economic security", explicitly looking to foster globally competitive national champions. After keeping its currency tightly linked to the US dollar for years, China in July 2005 revalued its currency by 2.1% against the US dollar and moved to an exchange rate system that references a basket of currencies. Cumulative appreciation of the renminbi against the US dollar since the end of the dollar peg was more than 20% by late 2008, but the exchange rate has remained virtually pegged since the onset of the global financial crisis. The restructuring of the economy and resulting efficiency gains have contributed to a more than tenfold increase in GDP since 1978. Measured on a purchasing power parity (PPP) basis that adjusts for price differences, China in 2009 stood as the second-largest economy in the world after the US, although in per capita terms the country is still lower middle-income. The Chinese government still faces numerous economic development challenges, including:

(a) Reducing its high domestic savings rate and correspondingly low domestic demand through increased corporate transfers and a strengthened social safety net

(b) Sustaining adequate job growth for tens of millions of migrants and new entrants to the work force

(c) Reducing corruption and other economic crimes

(d) Containing environmental damage and social strife related to the economy's rapid transformation

Economic development has been more rapid in coastal provinces than in the interior, and approximately 200 million rural laborers and their dependents have relocated to urban areas to find work. One demographic consequence of the "one child" policy is that China is now one of the most rapidly aging countries in the world. Deterioration in the environment - notably air pollution, soil erosion, and the steady fall of the water table, especially in the north - is another long-term problem. China continues to lose arable land because of erosion and economic development. In 2006, China announced that by 2010 it would decrease energy intensity 20% from 2005 levels. In 2009, China announced that by 2020 it would reduce carbon intensity 40% from 2005 levels. The Chinese government seeks to add energy production capacity from sources other than coal and oil, and is focusing on nuclear and other alternative energy development. In 2009, the global economic downturn reduced foreign demand for Chinese exports for the first time in many years. The government vowed to continue reforming the economy and emphasized the need to increase domestic consumption in order to make China less dependent on foreign exports for GDP growth in the future. Turmoil in international markets has "shattered" the sentiment of Chinese investors; detailed plans on expansion of domestic demand over the next two years should be formulated as soon as possible. The stability of agriculture is essential against a backdrop of an international financial crisis, governor urging greater efforts to increase production and raise farmers' incomes.

The financial crisis rings the alarm for the China's economy, more industry restructure needs to be done and we have to take patient attitude towards regaining the investor's confidence in the domestic market and also in the global financial market.

The Impact of World Economic Crisis on China Economy

Abstract

For centuries China stood as a leading civilization, outpacing the rest of the world in the arts and sciences, but in the 19th and early 20th centuries, the country was beset by civil unrest, major famines, military defeats, and foreign occupation. After World War II, the Communists under MAO Zedong established an autocratic socialist system that, while ensuring China's sovereignty, imposed strict controls over everyday life and cost the lives of tens of millions of people. After 1978, MAO's successor DENG Xiaoping and other leaders focused on market-oriented economic development and by 2000 output had quadrupled. For much of the population, living standards have improved dramatically and the room for personal choice has expanded, yet political controls remain tight. In the past 10 years china's economy has becoming the world's attention, rapid growth of G.D.P. brought millions of business opportunity to this mysterious Far East country. In 2009 china has passed a number of economic milestones. It is now the world's largest exporter, surpassing Germany. It is the world's largest market for vehicles, surpassing America. China's foreign reserve which is now the world's largest, are now over $2,000bn. The biggest landmark of them all – the moment when China becomes the world's largest economy – is getting closer. But in 2008 the economic crisis was wide spread all over the world, and china was greatly hit by the crisis, this thesis analysis the impact of the financial crisis on china's economy and the government's resolution against the economic crisis.

	Asian Financial Crisis			Internet Bubble Economy			Sub-prime crisis		
TIME	1997.2.5	1998.9.1	Change net %	2000.3.10	2002.10.9	Change net %	highest in last 52 weeks	lowest in last 52 weeks	Change net %
NASDAQ	1347.69	1575.09	16.87%	5048.62	1114.11	-77.93%	2861.51	2155.42	-24.68
Heng Sheng Index	13520.26	7062.47	-47.76%	17831.86	8977.35	-49.66	31958.41	19270.72	-39.70%
KLCI Kuala Lumpur Composite Indes	1271.57	262.7	-79.34%	948.09	641.53	-32.33%	1516.22	1173.22	-22.62
D-Jones Industrial average	7037.83	7827.43	11.22%	9928.82	7682.27	-26.61%	14279.96	11508.74	-19.40%
Nikkei 225 Index	19070.07	14369.63	-24.65%	19750.4	8539.34	-56.76%	15885.5	10770.6	-32.30%
BSE SENSEX	3356.83	2862.55	-14.72%	5301.78	2956.89	-44.23%	20873.33	14809.49	-29.05%
SSE Shanghai Stock Exchange	1017.96	1143.13	12.30%	1705.05	1535.37	-9.95%	6124.04	3516.33	-42.58%
S&P500	812.1	994.24	22.43%	1395.07	776.76	-44.32%	1576.09	1256.98	-20.25%
TWSE Taipei Weighted Index	7887.36	6335.09	-19.68%	9429.6	3947.61	-58.14%	9809.88	7408.4	-24.48%
FTSE 100	4344.7	5169.1	18.97%	6568.7	3742.4	-43.03%	6730.7	5414.4	-19.56%

P.S 52 weeks represent the date before 2008.03.20 (Schedule 1)