Commentary on the October 2020 CKGSB Business Conditions Index

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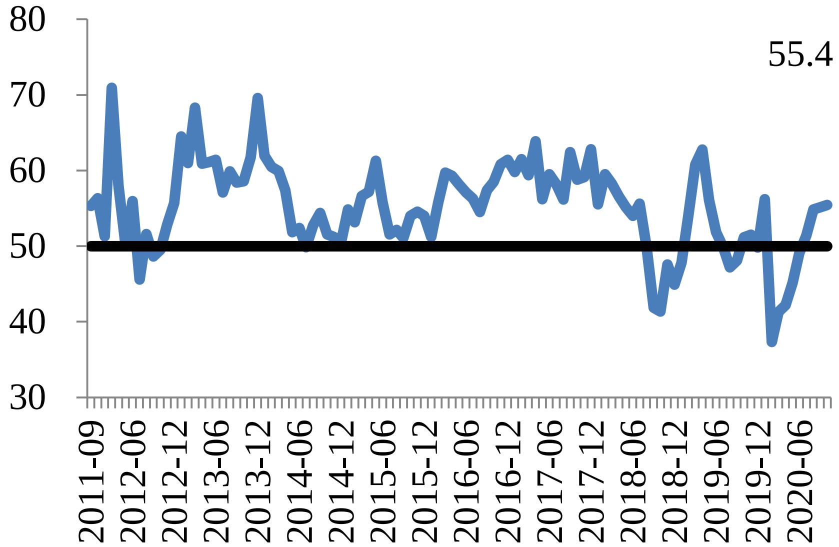
The CKGSB Business Conditions Index (BCI) welcomed a slight rise from 55.2 to 55.4 in October 2020 (Figure 1). It is important to note that with confidence above 50.0, it appears as though economic relief policies implemented by the government are having a marked impact on private business. If nothing changes, there is now a fairly high probability that China’s economy will finish this tumultuous year on a positive note.

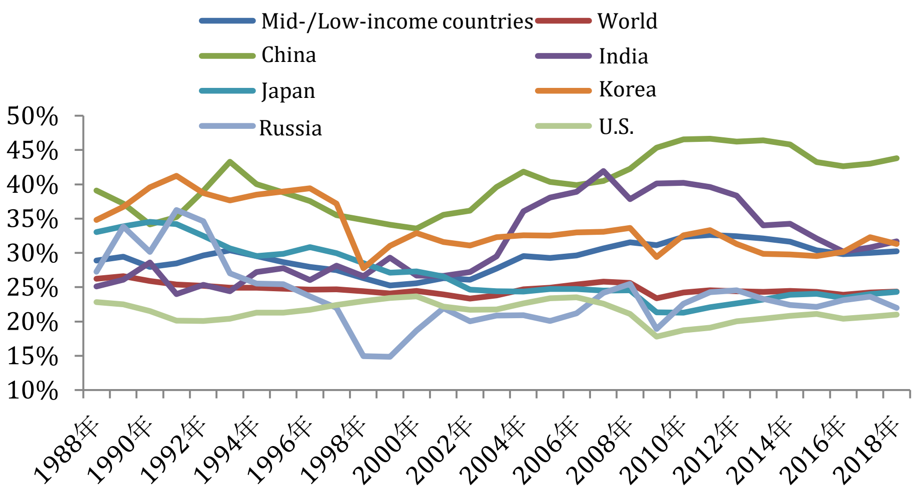
Figure 1 **Business Conditions Index (BCI)**



Source: CKGSB Case Center and Center for Economic Research

This month’s BCI data has not changed by much, but does look brighter. First of all, investment conditions have improved from 62.9 to 65.0. Those who have tracked the BCI for a while will know that investment is a large part of China’s economy, to the point at which you could say investment is the main driver of national growth.

Figure 2 **Proportion of Capital to GDP**



Source: CKGSB Case Center and Center for Economic Research

First, total capital is the sum of total fixed asset investment and inventory adjustments. It is an authoritative figure used to express national investment levels. Whether compared with developed countries, developing countries, or the global average, Figure 2 shows that China invests far more. So when China's investment rate falls, GDP growth will be severely affected. As private companies are now willing to invest, it demonstrates that they have confidence in the future of China's economy. When this happens, the economy will keep afloat.

Second, recruitment prospects also rose this month. Recruitment and investment figures are interconnected. When a company starts to expand, it increases investment first, and then uses some of this investment to build its workforce. Official data also indirectly demonstrates this point. According to urban unemployment figures from the National Bureau of Statistics, unemployment rates of 5.7% in July and 5.6% in August fell to 5.4% in September. Although it may relate to graduation season, if there were no expansion how could the many new graduates be absorbed into the system?

Third, corporate financing conditions have deteriorated. This may seem like a bad thing, but actually off the back of the virus, it is remarkable that the China's economy has pulled through and rebounded with decent momentum. The recovery may even have been a little too fast. All this is related to the government's loose monetary policy and policy of supporting private enterprises. A loose monetary policy saved the economy, but its side effects cannot be underestimated. A prolonged loose monetary policy will make everyone from decision-makers to regular people addicted, which will make it hard to end.

There is a slight contraction in the financing index, which is probably related to a stabilization of monetary policy at decision-making level. This also leaves room for the implementation of a future monetary policy, so the author believes that tightening the current monetary policy is an appropriate move.

In addition to some highlights, there are also some concerns expressed in the data, of which there are three main aspects. First, inventory prospects are not looking as good this month, as companies have more goods on their books. The author speculates that weak sales are to blame, leading to a build-up of stock. If this situation is temporary, there is no problem, as strong demand will draw down inventory and lead to a need for increased input again. But if this situation persists for a long time, it means that the expected demand growth ratio has not been fully fulfilled. After another year and a half, the accumulation of excess inventory may once again become an indicator of structural imbalance in China's economy.

Second, the consumer goods price index has been below 50 for most of this year, and while it rebounded during the return to work phase once the epidemic was controlled, it has since sunk back below 50. The downturn in consumer goods prices echoes swelling inventories and reflect the current situation in which consumer demand needs to improve in order to stabilize economic recovery. So are we still facing a greater risk of deflation? The author believes that after a sharp rebound in prices in the past two months, the risk of deflation has been fully resolved, and there is a high probability that macroeconomic policy will become stable by the end of this year or early 2021.

Third, at the cost end, confidence is rising to close to 80 this month. Combined with earlier sluggish inventory expectations, we can see that the structural imbalance of the Chinese economy has not been fundamentally resolved. "Cutting costs", a key part of the goal of "cutting overcapacity, destocking, deleveraging, reducing corporate costs and shoring up weak spots" is still far off.

Since China has successfully contained the pandemic and most countries are still struggling with its effects, export orders have been returning to China, and even new orders have come in. China's import and export situation has been pretty good. However, we need to be careful that as the pandemic worsens over the winter, overseas economies will be worse off, and this will impact on external demand.

At the same time, the epidemic may increase global supply chain costs and decrease reliability. As an important part of the global supply chain, China will not be left untouched. Given these conditions, we need to prepare for danger in times of peace.

As the first country to suffer from the coronavirus, China had the heaviest epidemic to begin with. However, the imposition of effective measures meant that China has controlled it better and the economy has rebounded quickly. But now it is almost winter, and winter is a period in which respiratory diseases thrive. We need to remain vigilant to the virus's return. As China has kept the pressure on the virus all year, we need to watch for epidemic fatigue as well. Imported cases are a major threat at this point in time. In short, fighting the epidemic is a protracted battle, and makes solving economic problems harder to focus on. However, a multi-objective and balanced operation is the task of modern governments. I believe that the Chinese government will take up the challenge.

This is a commentary on the CKGSB BCI report for October 2020 to which you are welcome to refer for detailed statistics. Do not hesitate to contact the BCI team by email as shown in the accompanying BCI data report.

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