Following an uptick in 2023, economic growth will likely moderate in 2024 and 2025 with persistent deflationary pressures a continuing concern until there is a substantial revival in domestic and global demand. Growth this year and next will be driven by continued fiscal support, but could accelerate if the property sector correction is largely addressed. There is a pressing need to address the property sector and local government finance issues.

**Economic Performance**

**Economic growth rebounded to 5.2% in 2023 from 3.0% in 2022 on a robust expansion in services and consumption after COVID-19 restrictions were lifted in late 2022 (Figure 2.11.1).** However, the rebound was bumpy. GDP growth fell from 6.3% in the second quarter (Q2) to 4.9% in Q3 with the property market weakening more than expected. GDP growth recovered to 5.2% in Q4 after a series of stimulus packages were introduced in the second half (H2) of the year, financed by additional sovereign bond issuance, the further easing of monetary policy, and policies supporting the property market.

**On the demand side, consumption, especially services expenditure, drove the post-pandemic recovery.** Household consumption recovered as disposable household income per capita grew by 6.1% in real terms (Figure 2.11.2). Consumption’s contribution to growth increased sharply from 1.2 percentage points in 2022 to 4.3 points in 2023. Spending on services such as dining rebounded after COVID-19 mobility-related restrictions were lifted in late 2022. However, spending on consumer goods did not grow as much as services, suggesting that household confidence has yet to recover fully.

**Investment grew by 3.0% in 2023 as solid growth in manufacturing and infrastructure investment offset the decline in property investment.** Investment contributed 1.5 percentage points to growth in 2023 (similar to the 1.4 points in 2022) as policy measures boosting high technology manufacturing, public infrastructure projects, and disaster rebuilding offset the property market downturn. Manufacturing investment, especially in high-tech industries, grew by 6.5% in 2023, supported by rising bank credit. Infrastructure investment also grew by a robust 5.9%, but real estate investment contracted by 9.6% (Figure 2.11.3). New construction remained subdued in most cities as homebuyer confidence has yet to recover and property developers continue to struggle with debt servicing and a large backlog of unfinished projects.

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Consumption and investment drove the economic recovery in 2023 while income grew steadily. Net exports weighed down growth amid slowing global demand (Figure 2.11.4). Net exports finished the year subtracting 0.6 percentage points from growth, compared to a positive 0.4 points contribution in 2022 after a good start early in the year and some tailwinds from electric vehicle and technology product exports.

On the supply side, the tertiary sector rebounded in 2023. It grew by 5.8% and contributed 3.1 percentage points to GDP growth, up from 1.7 points in 2022 (Figure 2.11.5). Accommodation and catering, information and technology services, and transportation led the recovery, but real estate services contracted. Secondary industry grew by 4.7% in 2023 and contributed 1.8 points to growth. High-tech manufacturing expanded rapidly, with the production of solar cells, new energy devices, and power-generating units growing in the double digits. The contribution of primary industry to growth remained unchanged at 0.3 points.

The labor market improved in 2023. The surveyed urban unemployment rate decreased from 5.5% in January to 5.1% in December 2023 and new urban jobs increased from 12.1 million in 2022 to 12.4 million in 2023. However, imbalances remained as young workers still faced multiple challenges such as limited job creation in private business and skill mismatching. The youth unemployment rate (ages 16–24) peaked at 21.3% in June 2023. Excluding university students, the rate was 14.9% in December. Migrant workers benefitted from the economic recovery, especially in the low-paid services. The unemployment rate for migrant workers from rural areas working in urban areas dropped to a historical low of 4.3% in December 2023.

Inflation remained subdued in 2023, dragged down by food deflation and softer energy prices. Consumer price inflation averaged 0.2% in 2023, down from 2.0% in 2022, driven by food deflation and lower energy prices (Figure 2.11.6). Food prices declined by 0.3% with pork prices falling 11.3%. Non-food inflation dropped to 0.4%, reflecting weak demand and softer global energy prices. Core inflation (excluding energy and food prices) was 0.7%. The producer price index declined by 3.0% in 2023 after increasing by 4.2% in 2022, as commodity and raw material prices decreased and domestic and external demand remained weak. Prices for newly constructed homes in the top 70 cities
declined by an average 0.9%, with prices in tier 3 cities declining the most and those in top tier 1 cities rising (Figure 2.11.7).

**Monetary policy was accommodative amid multiple constraints.** The People’s Bank of China (PBOC), the central bank, trimmed the 1-year medium-term lending facility rate twice for a total of 25 basis points to 2.50% in 2023, even though concerns over bank profits, pressures from currency depreciation, and capital outflows had increased (Figure 2.11.8). As a result, the 1-year loan prime rate moderated from 3.65% at the end of 2022 to 3.45% at the end of 2023. The PBOC also reduced the required reserve ratio for commercial banks twice to free up additional funds for lending and lowered the 5-year loan prime rate used for mortgage pricing by 10 basis points to 4.20% to support the stressed real estate sector.

**Credit supply ticked up in 2023 on strong government bond issuance.** Total social financing—an aggregate that includes bank loans, shadow bank financing, government and corporate bonds, and equity financing—grew by 9.8% in 2023, up from 9.6% a year earlier (Figure 2.11.9). Government bonds outstanding increased by 15.9% at the end of 2023 as local government special bond issuance accelerated in H2 and loans outstanding increased by 10.7% by year-end. Banks reallocated credit from the property sector to manufacturing. Medium- and long-term loans to manufacturing grew by 31.9%, but those to the property sector declined by 1.0% at the end of 2023.
The current account surplus narrowed driven by a lower merchandise trade surplus and a wider services trade deficit. The surplus decreased from 2.2% of GDP in 2022 to 1.5% of GDP in 2023.
Imports also dropped by 4.0% on weak domestic demand and lower commodity prices. Thanks to the resumption of cross-border travel, the services trade deficit widened from 0.5% of GDP in 2022 to 1.3% of GDP in 2023, recovering to 87.8% of the 2019 pre-pandemic level.

**Foreign direct investment (FDI) inflows decreased in 2023 amid weaker confidence and geopolitical tensions.** Increased geopolitical tensions and economic slowdown concerns dampened foreign company confidence, while a wider positive interest rate spread between the US and the PRC made investment in the PRC less attractive. As a result, FDI inflows decreased by 81.7%, resulting in a net outflow equal to 0.9% of GDP, compared to a net inflow of 0.2% of GDP in 2022. Meanwhile, net portfolio investment outflows reached 0.8% of GDP in the first 3 quarters of 2023, lower than 2.0% of GDP during the same period in 2022 (Figure 2.11.12). Reserve assets increased by $143 billion and stood at $3.45 trillion at end-2023. The renminbi depreciated by 1.7% against the US dollar over the year (Figure 2.11.13). It depreciated by 1.3% in nominal effective terms (against a trade-weighted basket of currencies) and by 5.5% in real effective terms (taking inflation differentials into account).

**Figure 2.11.12 Balance of Payments**

FDI inflows decreased significantly in 2023 amid weaker confidence and increased geopolitical tensions.

![Balance of Payments Chart](chart.png)

FDI = foreign direct investment, Q = quarter.

Note: Only current account balance and net FDI data available are for Q4 2023.

Sources: CEIC Data Company, Asian Development Bank calculations.

**Economic Prospects**

**Economic growth is expected to moderate in 2024 and 2025.** GDP is forecast to grow by 4.8% in 2024 reflecting the ongoing property market adjustment and weak external demand. Growth will further moderate to 4.5% in 2025 (Table 2.11.1). Last year’s support for the housing market—including lower down payment rates and lower buying restrictions—along with accommodative monetary policy through lower reserve requirement ratios and policy rates, and fiscal stimulus to rebuild disaster-affected areas could have some near-term effects. Household consumption should help drive economic recovery in 2024 as the labor market and household income improve. Investment will be supported by strong public infrastructure growth boosted by fiscal expansion, while high-tech and other manufacturing investments should continue to grow solidly due to policy support. However, low consumer and investor sentiments in the property sector are expected to persist, tamping down consumer spending.

**Table 2.11.1 Selected Economic Indicators, %**

<table>
<thead>
<tr>
<th></th>
<th>2022</th>
<th>2023</th>
<th>2024</th>
<th>2025</th>
</tr>
</thead>
<tbody>
<tr>
<td>GDP growth</td>
<td>3.0</td>
<td>5.2</td>
<td>4.8</td>
<td>4.5</td>
</tr>
<tr>
<td>Inflation</td>
<td>2.0</td>
<td>0.2</td>
<td>1.1</td>
<td>1.5</td>
</tr>
</tbody>
</table>

GDP = gross domestic product.

Sources: CEIC Data Company; Asian Development Bank estimates.
and private investment. Real estate investment will also remain a drag due to sluggish housing demand, especially as the backlog of unfinished projects and concerns over debt repayment weaken developers’ investment appetite. Weak external demand, together with increased trade tensions will dampen demand for PRC exports with net exports continuing to drag down growth.

Supportive policies are essential to bring the economy back on solid footing. To revive growth momentum, effective measures to resolve property sector problems and strengthen private investment and household consumption should be enhanced in the policy pipeline this year. More targeted fiscal and monetary policies supplementing those announced and implemented in 2023, as well as the effective use of ultra-long special treasury bonds announced in March 2024, are necessary to address the challenges of persistently tepid external demand, high local government debt, deflationary pressure, geopolitical risks, and new sources of productivity gains amid demographic changes and an aging population.

Policy support to selected industries will drive the supply side despite excess capacity in certain sectors. Growth in services will moderate in 2024 as the post-COVID recovery boost fades. However, credit support, tax breaks, and grants for technology sectors, including semiconductors, high-tech equipment, and artificial intelligence, along with demand for low-carbon technologies, including electric vehicles, batteries, and renewables, will likely continue in 2024. Construction will be supported by infrastructure investment and public projects. Excess capacity concerns increased as the industrial capacity utilization rate dropped from 75.6% in 2022 to 75.1% in 2023. Inventory drawdowns as consumption rises and a pickup in new orders should lessen excess capacity in some manufacturing industries, such as automobile, pharmaceutical, electric machinery, and equipment, where capacity utilization rates dropped in recent years.

The labor market should improve but youth unemployment challenges will likely remain. The labor market should improve in line with a pickup in household consumption and a step up in policy, especially fiscal support. Jobs created in construction and services will continue to benefit low and medium-skilled labor, especially migrant workers. However, youth unemployment will likely remain as the government expects a record high of 11.8 million new college and university graduates in 2024.

Inflation is forecast to rise to 1.1% in 2024 and 1.5% in 2025 as the economy continues to recover. The lingering effects of overcapacity in some manufacturing companies should tamp down price increases this year, and continued weakness in domestic and external demand will likely put downward pressure on producer prices and core inflation. However, with pork prices bottoming out and energy prices increasing, overall price movements should steer away from outright deflation. Inflation should increase further in 2025 assuming domestic demand, especially in the property sector, continues to recover.

Monetary policy will remain accommodative. In early January 2024, the PBOC announced a further reduction in the bank reserve requirement ratio (RRR) by 50 basis points that took effect on 5 February, doubling the size of typical RRR cuts, and signaled increased efforts to shore up credit supply. The central bank also injected CNY350 billion into policy banks via the Pledged Supplementary Lending facility likely to provide low-cost funding to social housing and infrastructure. To support the property market, the PBOC lowered the 5-year loan prime rate—mortgage reference rate—by 25 basis points to 3.95% in February 2024.

Fiscal policy will support growth. The higher new local government special bond issues quota (CNY 3.9 trillion in 2024) and CNY1 trillion ultra-long special government bond issuance announced in March 2024 should support economic growth. Fiscal policy measures are expected to be targeted and focused on strategic industries, affordable rental housing projects, urban renovation, and rebuilding disaster-affected areas. In addition, the central government is expected to take a bigger role in fiscal spending to help ease the financing burden of local governments. While the economy is expected to continue expanding in 2025, the fiscal spending will likely moderate after years of high fiscal deficit and rising local government debt, which have increased from 21.6% of GDP in pre-pandemic 2019 to 32.3% in 2023. COVID-related expenditure and reduced land sales have increased the financial strain faced by local governments and made it difficult for them to service their debt.
The current account surplus is projected to decrease slightly due to tepid external demand and resumption of outbound travel. The expected easing of growth in advanced economies and ongoing global trade slowdown will dampen demand for PRC exports. While exports from new industries such as electric vehicles, batteries, and renewables are bright spots, they will face headwinds from growing trade tensions with their Europe and US counterparts. Meanwhile, the services trade deficit will likely increase as outbound travel, which has yet to return to pre-pandemic levels, can be expected to pick up. FDI will likely continue its downward trend, but should remain strong in high-tech sectors. Outward direct investment could pick up in new sectors as offshoring to improve efficiency and gain higher market share gradually occurs. Capital outflow pressure is expected to ease as US interest rates trend downward.

Risks to the outlook are balanced. Downside risks include further deterioration in the property market, undermining financial stability, and threatening the growth outlook. Longer-than-expected financial market turbulence can dampen consumer sentiment as happened following the recent stock market slump. External risks include increased trade tensions with the US and EU further weakening PRC’s exports, escalated geopolitical tensions that could disrupt supply chains, renewed energy challenges triggered by geopolitical conflict, and fragmentation of the global economy. Full and effective implementation of government fiscal and monetary measures as announced along with additional policy support could raise private sector confidence faster-than-expected, resulting in higher growth and inflation than forecast.

Policy Challenge—How Stimulating is Government Spending?

How effective has large fiscal spending been in stimulating growth remains a largely open question. During the 2008–2009 global financial crisis, the government rolled out a fiscal stimulus package equivalent to nearly a fifth of GDP. To boost the property sector in 2015, it subsidized interest rates on loans by policy banks. As the pandemic struck in 2020, it guided the policy bank financing for infrastructure projects and issued special sovereign bonds. These packages substantially raised fiscal deficits. Understanding the extent to which these large stimulus packages have been effective in achieving their objectives has become increasingly relevant as the economy continues to face many headwinds, including the property sector downturn, local government debt, deflationary pressures, uncertainty in global markets, lukewarm confidence among the private sector and households, overcapacity in some sectors, and aging population and productivity issues. It is thus important to assess the lessons learned from past government stimulus spending to inform the design and implementation of future policies.

Concerns over public debt levels imply that the scope for additional borrowing is narrowing and new loans should be more productive. According to official statistics (IMF 2024), at the end of 2023 central government debt was estimated to equal 23.8% of GDP, with local government debt the equivalent of 32.3%. It is estimated that off-balance sheet liabilities from local government financing vehicles (LGFVs)—set up to finance public infrastructure projects—could be as large as 48.1% of GDP. Together, the augmented debt of central and local governments grew from 80.8% of GDP in 2018 to 116.2% in 2023. Since the property market downturn started in 2021, local governments have also faced hard budget constraints as their own-source revenues declined with the sale of land-use rights to property developers. At the same time, local governments shared the significant burden of pandemic-related health and medical expenditure. With local government debt still large and their ability to raise revenue limited, the central government will likely assume some local government responsibilities, which in turn will require additional fiscal packages that will affect debt sustainability. Therefore, it is essential to ensure that these fiscal injections are designed and implemented so they are effective in meeting their objectives.

Measured by the usual fiscal multiplier yardstick, several studies on the impact of local authority expenditures indicate that these fiscal impulses have been reasonably effective. The studies used provincial data to show that the fiscal multiplier was positive, as an increase in government spending did indeed lead to positive output growth. The analyses yielded a range of local fiscal multipliers from 0.6 (Guo et al. 2016) to 1.0 (Chen et al. 2021),
indicating that a 1% increase in government spending leads to an increase in output between 0.6%–1.0%. The results varied across localities, however, with spending by localities receiving larger transfers from the central government not necessarily yielding larger multipliers. A more recent study of local fiscal multipliers in the PRC yielded a multiplier of 0.7 (Dong et al. forthcoming). However, this study also showed that if fiscal spending does not lead to a deterioration of the fiscal balance, the multiplier is 2.9, and 0.2 if the financing is by increasing fiscal deficits. Thus, to raise the effectiveness of government spending, local governments should reduce the deficit by raising revenues. These findings point to the dependence of local government on land and other property sales, which is their main source of revenue, and the detrimental effect of local government borrowing on the efficacy of fiscal policy as measured by local fiscal multipliers.

**The results of the fiscal multiplier studies also varied by targeted economic sector.** Government spending on investment had a multiplier of 0.6, but investment in technology yielded a fiscal multiplier of 8.6, much higher than the infrastructure spending multipliers of 0.4 and 0.1 for construction and real estate-related industries. These results and the correction in the housing market that has led to fragility of LGFVs and debt-ridden local governments indicate that growth fuelled by fiscal resources directed toward infrastructure investment and the property sector is unsustainable.

**The more effective the fiscal policy supporting consumption, the higher and more sustainable the quality of long-term development.** Economic growth must also rely on domestic demand to maintain its momentum amid uncertainty in the global environment. As income levels increase in the PRC, consumption of goods and services will likely play an increasing role in driving GDP growth and the long-term sustainability of economic development. However, the fiscal multiplier on private consumption is shown to be small, but at the same time, raising the effectiveness of government support for consumption is becoming more urgent given ongoing demographic changes, including declining fertility, an aging population, and urban-rural migration. Thus, several policy measures and reforms are needed. In the near term, the property sector problems should be addressed as private consumption depends on household wealth, which is stored in the housing market. In addition, policies targeted at strengthening social safety nets, particularly pension insurance, unemployment insurance, and medical insurance—along with improving the effectiveness of government spending in these areas—will increase household consumption, thereby raising the fiscal multiplier of government consumption incentives.