

Longtime China Watchers Predict What's Next for Slowing Economy

Some of the most prominent voices on China share their outlooks.

[Enda Curran](#)

China's economy started the decade in a boom and will end it suffering the worst slowdown since the early 1990s.

What comes next? Bloomberg asked some of the world's most prominent China watchers, several of which distinguished themselves over the past 10 years with prescient forecasts or market-beating returns.



Predictions of even slower economic growth were near unanimous among the group, though most respondents also said policy makers have the tools to

avoid a crisis. Several investors flagged buying opportunities in Chinese stocks after valuations sank to record lows versus global peers.

Among the biggest long-term worries: demographics. Ed Yardeni, who coined the term “bond vigilantes” in the 1980s, had a similarly colorful take on China, calling it “the world’s largest nursing home.” His and other comments below have been lightly edited and condensed.

George Magnus, research associate at Oxford University’s China Centre and author of “Red Flags: Why Xi’s China is in Jeopardy”

In the spirit of self-criticism, I’d say my best call on the economy was an early spot of the huge demographic shift that kicked off in earnest in 2012, an abiding assertion that China’s elevated growth rates could not be sustained, and anticipation of a financial crisis that turned up in 2015-16. Worst call was thinking that crisis might turn into a ‘Minsky Moment’ for China, as per 2007-08, and failing to integrate properly the tools the state has to prevent catastrophic failure.

I expect China to flirt with officially recorded growth of around 6%, but the reality is that the tempo of growth is ratcheting down to somewhere between 3% and 4%. In 2020, perhaps 5.8% to 6%, officially, not least because the economic news has to remain upbeat ahead of the CCP centenary in 2021. The consequences of over-indebtedness, demographic change, inadequate wealth transfer and income redistribution policies, and stagnant total factor productivity growth associated with institutional flaws are the main drags on growth. The 2020s will be a challenging time for China.

Dong Baozhen, whose Chinese stock fund has returned about 520% over the past five years, a period when the Shanghai Composite Index was little changed

People have not made much money in the stock market the past decade. While China was seen to be the growth engine of the world during the financial crisis, markets elsewhere are at new highs, whereas we are still where we started. That could mean the gains have been postponed.

The probability of no increase in stock valuations in the next decade is a lot smaller than the index reaching 10,000, up from around 3,000 now. That could happen if the valuation of large caps doubles from their current PE to about 10. I like blue chips and financials that are severely undervalued. The sectors favored in the past two years, consumer staples and drugmakers, are way overvalued.

Jim O'Neill, the former Goldman Sachs Group Inc. chief economist who coined the term BRIC

The BRICs path assumed China would grow 5% a year in the decade 2020-29 and I have no reason for changing this. If it does, and so long as the renminbi doesn't decline a lot in value, then by the end of the decade, China will be very close to being as big in current dollar terms as the U.S.

As this decade nears its end, China has major problems positioning itself in the world. As evidenced by the Uighur situation, China's approach to life now gets much more global attention than when it was smaller. In the coming decade, China has to somehow develop a more subtle and sophisticated stance on many of these issues, and I am not sure Beijing fully realizes this yet.

Wang Qing, president and chief economist of Shanghai Chongyang Investment Management Co. The firm's flagship fund recorded a 385% return from its inception in 2008 through the end of November

The scale of the economy will surpass that of the U.S. for sure over the next decade, with annual growth likely slowing to an average 4%, which

would still be a healthy level given the size of it. What China is experiencing now is like what Japan and Korea had been through decades ago. If we take a 10- to 20-year view, events like trade war are just small disruptions along the course of economic development.

In the past decade it was properties and wealth management products with guaranteed returns that won favor with investors and enjoyed the fastest growth, while equities only accounted for a small portion of the pie. Now with the era of fastest property development growth behind us, and policy changes that shake up the WMP industry, returns on such investments will be much less attractive and risk-adjusted returns in equities will outweigh those on property investment.

Consumption remains a sector that offers abundant opportunities. The past decade has been a golden age of durables consumption (like home appliances and automobiles). In the coming decade it'll be services consumption that takes the center stage, with gems to be found in education, health care, leisure and travel as well as sports.

Charlene Chu, senior analyst at Autonomous Research

What I wasn't expecting to see was that the authorities would get religious on what I was talking about, which is that they had a shadow credit monster on their hands that had to be dealt with or it was going to have really serious longer term consequences. On the whole, they have done a very good job of really coming in and saying this has to stop, even in the middle of a trade war.

The problem is they still have a lot of bad debt that has been built up and that hasn't really been dealt with. We estimate more than 20% of total credit is bad credit. The real risk is that the pace of clean up is too slow, and that this dead weight strangles growth.

The question for China over the next ten years is are they going to be

forced to deal with these problems in a much more rapid and aggressive fashion or can they just continue to drag these out forever.

Edward Yardeni, president and chief investment strategist at Yardeni Research Inc.

Demography is starting to really weigh on China's growth. China is rapidly evolving into the world's largest nursing home.

They are going to have to provide a social safety net for these folks who are going to get older and need health care. If they don't do that, they are going to depress their consumers. When you want to be a superpower there are a lot of factors that matter, and demography is certainly one of them.

Arthur Kroeber, a founding partner and managing director at research firm Gavekal Dragonomics

One of the things that has been surprising, particularly since Xi Jinping took over, is the degree to which the state has held onto its huge position in the economy and in many cases reinforced it. The lack of progress away from a state driven economy to a more private-sector one has been disappointing but it has also been surprising that they have been able to maintain the pace of growth that they have, even with the state sector.

Ten years from now, I don't think we are going to be in a much different place as far as the internationalization of the Chinese currency. As long as they have this problem of high leverage and a somewhat fragile domestic financial system, they are going to have very little incentive to allow full fluidity of capital flows into and out of the country.

Michael Pettis, a finance professor at Peking University and former Bear Stearns Cos. banker

My best call was probably to insist, even in 2015-16 when the market strongly expected otherwise, that as quickly as debt was rising, China was unlikely to experience a financial crisis and a sharp depreciation of the currency. I think the market didn't understand that these are mainly balance sheet events, and as long as China's financial system was closed and its regulators powerful, Beijing could easily extend and restructure liabilities so as to prevent a crisis.

My worst call was to propose that Beijing would recognize the extent of investment misallocation and the inexorable rise in debt by 2015-16, and would begin to lower the GDP growth target rapidly after that. I did not recognize how politically difficult this would prove, and that it couldn't happen until Xi Jinping and the people around him had done a lot more to consolidate political power.

Every historical precedent -- and the logic of the growth dynamics -- suggests it will be another Japan. GDP growth rates will drop consistently every year until China is growing at below 3%, and the longer it takes to get there, the more debt it will have to work off and the greater the macroeconomic financial distress costs it will have to absorb.

Fraser Howie, author of “Red Capitalism: The Fragile Financial Foundation of China’s Extraordinary Rise”

I thought there would have been greater shocks because of the debt. Not necessarily crises, but I think China has spun out the debt problems far longer than anyone even on the bearish side would have given them credit for. It's only now in 2019 that we are starting to see a dramatic increase in defaults.

You are now starting this decade with almost the worst numbers and financials at every level, so why would we think this is going to turn around when our starting point is so much worse? The ability for China to stimulate their way out is clearly going to be much more limited. Last

decade was a decade of building problems and the coming decade is one of avoiding the consequences of those problems.

Eswar Prasad, who once led the International Monetary Fund's China team and is now at Cornell University

The government has succeeded in maneuvering the economy around the seemingly inevitable prospects, at various points, of a financial crisis, massive currency devaluation, housing market meltdown, and economic stagnation. None of these plausible doomsday scenarios has yet come to pass and it is not clear any of them will.

Over the next few years, China is likely to continue growing at a rate that will look low relative to its recent history but will still be remarkable for a \$13 trillion economy. Even a decent growth performance hinges, however, on the government's ability to reform the financial system so it allocates more resources to the parts of the economy that are more productive and can generate better employment growth.

Scott Kennedy, senior adviser and trustee chair in Chinese business and economics at the Center for Strategic & International Studies

China's economy has been more resilient than I expected it would have been without engaging in substantial liberalization. Although growth has slowed as a result of shoveling a growing proportion of resources to unproductive SOEs, authorities have managed to keep a lid on potential crises.

The growth outlook for 2020: 5.7% to 5.8%, just enough to reach their double centenary goals. In ten years: "Ja-pines" (a mix of Japan and the Philippines), highly successful in a few sectors, yet beset by problems of inequality, debt, and poor governance.

Diana Choyleva, chief economist at Enodo Economics in London

China is now facing the sternest test of its development model since the economy started opening up 40 years ago. It is already an economic super power, but the 180-degree shift in its political and economic orientation under Xi's leadership is undermining the key drivers of its economic success.

Our read is that the market has pushed their earlier China worries to the back of their mind. But those will resurface during 2020 as Beijing goes for a credit-fueled investment boost, raising investor debt concerns again after the likely initial positive response to more stimulus.

Hao Hong, the chief strategist at Bocom International in Hong Kong and one of the few forecasters to call the peak of China's equity boom in the middle of the decade

The consensus for 2020 is very optimistic. People are saying that we are bound for a 'strong nation bull.' Most are taking a cheery view on next years stock market but not so much for the economy, which is contradictory. We've only seen one instance where the local stock market and economy did not move in tandem -- in 2015. We see a bottom of 2,700 for the Shanghai Composite, and a peak that will probably not exceed 3,500. Next year might not be as easy to make money in the market.

The best trades will have to be bottom up, and you'll have to find the leading firms in each sector, or so called platform companies like Alibaba. These are likely to emerge as the winners. Obvious themes like tech, health care and consumer bother me because i don't think we can think in terms of entire sectors. It will be a more intricate case of finding the niche opportunities — real estate services is one of them. A lot of opportunities may be found in companies that are not public as well, especially those that do innovative drugs.

Andy Xie, an independent economist and former Asia-Pacific chief economist at Morgan Stanley

China uses official statistics as an expectations-management tool, gradually easing figures down so that confidence does not go bust. They won't lift expectations from here forward because they don't want hopes rising and then falling empty. The stats may say there is still stable growth, but in reality it's much more volatile. I think the official figures, say at the end of the decade, will be 4% or below.

I think leading companies in agriculture and education may be good areas to invest -- anything that China wants to buy will do well. And under this principle, things that China wants but cannot create on its own. But these must be really world-leading companies, like Cargill, General Mills and Disney.

— *With assistance by Amanda Wang*

Before it's here, it's on
the Bloomberg
Terminal.

[LEARN MORE](#)