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WORLD | CHINA

China Goes All In on Green Industry to Jolt Ailing Economy

Capital is pouring into factories that make items such as electric vehicles, batteries and renewable-energy gear as Beijing looks for new sources of growth

By Jason Douglas Follow

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Many of China's export partners in the West are looking to diversify supply chains. PHOTO: QILAI SHEN/BLOOMBERG NEWS

China is doubling down on manufacturing to reboot its economy after a turbulent year, a strategy that risks igniting new tensions over trade as countries step up support for prized industries and global growth teeters.

The push for new growth drivers comes as figures showed the world's second-largest economy expanded in 2023 at its weakest rate in decades, aside from the three years when China was closed to the outside world during the Covid-19 pandemic. A drawn-out property crunch means Beijing can no longer rely on debt-fueled real-estate investment to power the economy, and officials have shown little appetite to shift activity decisively toward consumer spending.

The result: Capital is pouring into factories as Beijing tries to nudge China's supertanker economy onto what it hopes will be a healthier trajectory.

Central to that ambition is a plan to dominate global markets in emerging industries, such as electric vehicles, batteries and renewable-energy gear. Chinese companies such as automotive giant BYD, battery maker CATL and solar manufacturer Longi Green Energy Technology are already among the world's most prominent players in those markets.

The hope is that growth in what Chinese officials refer to as the "New Three" industries and other favored sectors will help China's economy banish the specters of deflation and Japan-style stagnation as a real-estate crunch weighs heavily on construction, investment and consumer confidence.

Longer-term, Beijing wants these and other high-tech manufacturing industries to be in the vanguard of its push to eventually unseat the U.S. as the world's largest economy, while also helping it grow richer and weather the pressure of an aging and shrinking population.

Economists, though, see two big hurdles ahead.

One is that real estate has grown to be such a huge chunk of China's economy that it can't easily be replaced. That implies the hoped-for rebalancing will be accompanied by a spell of much weaker growth in China than households, businesses and investors have come to expect.

The second is that many countries, especially big markets such as the U.S. and Europe, are signaling they aren't that eager to buy the fruits of China's industrial renewal—and in some cases are already raising barriers to Chinese products.

The risk is a new round of tit-for-tat protectionism that could put lasting pressure on the global economy.

"If China builds up all this capacity and cannot absorb this capacity domestically, it will be looking for export markets around the world," said Eswar Prasad, professor of trade policy at Cornell University and former head of the International Monetary Fund's China division. "China is feared as a country that could dominate global markets and wipe out domestic producers."

China is hoping to build up its manufacturing capacity. PHOTO: CFOTO/ZUMA PRESS

European Commission President Ursula von der Leyen, speaking Tuesday at the World Economic Forum in Davos, Switzerland, said China was one of the continent's most important trading partners, but added: "We need to derisk in some areas." She said recent export restrictions China placed on critical minerals didn't help build trust, and Europe was working to diversify its supply chains.

Manufacturing investment in China was a bright spot last year in an otherwise sluggish year for growth. China's economy grew 5.2% in 2023, according to official data released Wednesday, a modest expansion just above Beijing's target for the year but less than the speedier growth rates that were commonplace in the recent past.

But investment in high-tech manufacturing rose 9.9% in 2023 from the previous year, Wednesday's data showed, powered by spending in electronics, aviation and communications.

Unlike Japan, South Korea and Taiwan, which mostly ceded low-end manufacturing to cheaper locations as they became adept at high-tech manufacturing, China is aiming to consolidate its position as the world's factory floor by making not only high-end goods such as aircraft and semiconductors, but also the stuff that it has excelled in for decades, like toys and furniture. In 2022, China accounted for 31% of global manufacturing, according to United Nations data, compared with 16% for the U.S.

One standout success for China in 2023 was its fast-growing auto sector. Aided by surging sales of mostly gas-powered vehicles to Russia, China is estimated to have overtaken Japan as the world's largest car exporter last year. Chinese firms such as BYD and XPeng have set their sights on the growing EV market, causing consternation in Europe especially, where the European Union has opened an antisubsidy probe into cheap Chinese EVs.

Yet this manufacturing prowess and China's pole position in hot industries such as electric cars and solar panels can obscure the economy's reliance on real estate and construction as the drivers of growth.

Estimates by Kenneth Rogoff of Harvard University and Yuanchen Yang of the International Monetary Fund suggest that real-estate construction, investment and associated activities accounted for as much as 25% of China's annual gross domestic product before the pandemic, compared with between 10% to 15% for most other economies. Add in infrastructure spending and that share reaches 30%.

Rory Green, chief China economist at GlobalData TS Lombard in London, said a generous amalgamation of Beijing's favored manufacturing sectors would add

up to perhaps 10% of the country's GDP.

And construction is still fueling Chinese growth, even as the country's residential property woes mean the number of unfinished apartment blocks has mushroomed. Infrastructure investment rose 6.5% in 2023 from a year earlier as the government bankrolled transport and power projects, data show.

"The Chinese economy is still extremely dependent on construction activity," said Julian Evans-Pritchard, head of China economics at Capital Economics in Singapore. "The reason the economy is still growing at 5% is not because EV exports are booming. That's just too small."

Economists at Goldman Sachs concur, calculating that investment in New Three industries in the years ahead won't be enough to offset the drag from China's wider challenges. In a recent report, they estimated that the continuing property slump and declining production of traditional autos would shave 0.5 percentage point off annual growth in the years through 2027—even after accounting for lavish investment in EVs, batteries and renewables. The net impact on jobs would also be negative, they found, since construction tends to be more job-heavy than modern manufacturing. The investment bank anticipates annual growth in China will slow to around 4.5% this year and 3.7% in 2027.

China is estimated to have become the world's largest car exporter last year. PHOTO: CHEN WEI/ASSOCIATED PRESS

China's aggressive charge into high-end manufacturing comes as the U.S. and other rich nations abandon years of laissez-faire globalization and increasingly

look to nurture and protect strategic industries while reducing their perceived overreliance on China. The U.S. is dangling billions of dollars in subsidies for renewable-energy projects and semiconductor manufacturing, though some project and hiring delays have underlined what for some analysts are longstanding weaknesses in U.S. manufacturing after decades of offshoring.

Green, of TS Lombard, said Beijing's new growth model presents the West with "a unique mercantilist challenge," pairing the technological prowess of an advanced economy with the income level of a developing one. As it pursues its new growth strategy, China will likely import less as it learns to make more things itself, while exporting more high-end products to global markets, he said.

The likely result will be a wave of new tariffs and other trade frictions, which imply higher prices for consumers and weaker global growth as barriers to trade and investment rise, many economists say.

It also means Western companies are set to face fiercer competition from Chinese firms in developing countries. While some countries, such as India, are themselves considering tighter restrictions on certain Chinese products to protect fledgling industries, others are likely to embrace them as affordable alternatives to Western high-tech goods.

"China is just going to swamp those markets and dominate everywhere else," said Green.

—Kim Mackrael contributed to this article.

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