

# THE WALL STREET JOURNAL.

This copy is for your personal, non-commercial use only. To order presentation-ready copies for distribution to your colleagues, clients or customers visit <http://www.djreprints.com>.

<https://www.wsj.com/articles/chinas-bright-economic-future-is-bound-up-in-the-past-1508416787>

## ASIAN BUSINESS NEWS

# China's Bright Economic Future Is Bound Up in the Past

For all the talk of a bigger role for markets, the role of China's state sector has grown under President Xi Jinping



A factory in Dalian in January; smokestack industries are carrying China's economy. PHOTO: QILAI SHEN/BLOOMBERG NEWS

By *Lingling Wei*

Oct. 19, 2017 8:39 a.m. ET

BEIJING—President Xi Jinping lauded China's transition to high-quality growth as he opened a major leadership meeting this week. For now, though, smokestack industries are carrying the economy.

It grew at a 6.8% pace in the third quarter, much above forecasts at the beginning of the year that warned of a slowdown.

Nothing less than a stellar report would be expected when Communist Party leaders are gathered in Beijing to anoint Mr. Xi for a second term. But the disconnect between the president's words and Thursday's data from the National Bureau of Statistics was striking, illustrating that for all the talk of a bigger role for markets, the state sector's role has grown under Mr. Xi.

While recovering global demand has lifted China's exports, a main reason for the strong numbers was that coal miners and metal makers cranked up production as prices rose—driven higher by government-mandated capacity cuts that had forced out many private companies.

Other old-economy players, such as real-estate developers, kept appetite for cement, steel and other construction materials strong, defying government efforts to cool the housing market.

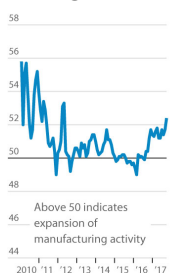
In fact, despite much-touted efforts to relieve long-term ills such as high debt, overbuilding and overproduction, many manufacturers say their overall capacity is rising, not falling, and Chinese banks are lending more, not less.

That and growing global demand give Beijing some economic breathing room—in the short term.

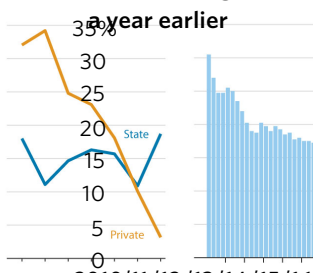
## Old-Economy Recipe

China's growth is once again dependent on heavy industry and the state sector.

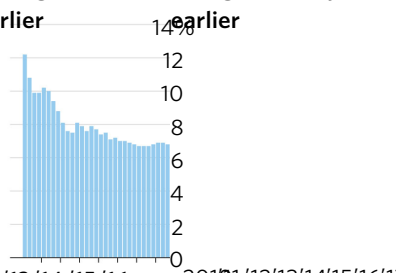
### Purchasing Managers' Index\*



### Investment in fixed assets, change from a year earlier



### Quarterly GDP, change from a year earlier



\*Largely tracks big industrial firms

Sources: Wind Info (PMI, investment); National Bureau of Statistics (GDP)

“Financial stresses that continue to build up in the background can be kept at bay for at least a little longer,” said Eswar Prasad, a China scholar at Cornell University

and the International Monetary Fund’s former top official in China.

In a survey by data provider China Beige Book, hundreds of coal, steel, aluminum and copper companies reported that the third quarter was the sixth in a row in which overall capacity rose.

Sunstone Development Co., which makes carbon blocks used in aluminum production and employs nearly 2,000 workers across China, has increased its capacity by a third as prices for its products have gone up significantly—partly because tougher environmental rules forced many smelters to shut down.

“Our products are in short supply,” said Lang Guanghui, Sunstone’s chairman.

Because tackling inefficiencies could slow growth in the short term, it collides with party pledges to improve life for ordinary Chinese and turn China into a rich country. Mr. Xi’s speech emphasized goals—such as a “moderately prosperous society” by 2020—that are likely to limit Beijing’s flexibility in managing the economy.

## China’s Congress: What to Watch



AGENCE FRANCE-PRESSE/GETTY IMAGES

“Keeping growth above the 6% floor will remain the top policy priority,” said Chi Lo, China economist at BNP Paribas Investment Partners.

But in the longer run, economists say, failure to trim bloat or allow more competition increases risks of a severe slowdown that could derail China’s ambition to join the rich world.

For now, Beijing’s tendency is toward larger state control

rather than market forces. In his speech Wednesday to open the party congress, Mr. Xi emphasized a “stronger, better and bigger” state sector in his plan to turn China into a strong global power.

Senior government officials attending the congress reaffirmed their mission to keep the economy on an even keel. The head of the agency overseeing major state companies told reporters it will try to introduce more market discipline, but continue to favor consolidation over bankruptcies.

“We hope to have more job transfers and fewer layoffs,” said Xiao Yaqing, chairman of the State-owned Assets Supervision and Administration Commission.



A construction site Shenzhen in September; real estate continues to be a major economic driver, even as the government tries to cool the housing market. PHOTO: QILAI SHEN/BLOOMBERG NEWS

At a group discussion Thursday morning on the sidelines of the congress, central-bank Gov. Zhou Xiaochuan warned about the risk of excessive optimism. Ever-rising corporate debt, he said, could lead to a “Minsky moment”—named for the late American economist Hyman Minsky—in which asset prices collapse suddenly after a long period of economic growth.

However, neither Mr. Zhou nor other top financial regulators at the discussion said much about measures to lower debt.

One sector regulators have repeatedly tried to rein in is real estate, which is playing an increasing role in growth. Property investment in the first nine months of 2017 was up 10.4% from a year earlier, and purchases of furniture and decorating materials were a major driver of consumer spending.

David Li, a manager at furniture maker Fudan-Nisi in the southern city of Foshan, said the strong property market has benefited his entire industry. But like many private businesses, he also complained of a profit squeeze from higher commodity prices.

“The price of the foam used in sofas has gone up three times in the past month,” Mr. Li said.

— *Lin Zhu contributed to this article.*

*Appeared in the October 20, 2017, print edition as ‘China Economy Backs Into Future.’*