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A Critical Examination of the "China Collapse" Narrative

by

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ABSTRACT

Western media and academia have heralded the China collapse narrative. This paper provides a critical and balanced examination of the four challenges facing the Chinese economy—namely, deflation, debt, demographics, and de-coupling/de-risking. It argues that while deflationary pressure is present, consumer demand has been improving as the property market stabilized and policies to bolster domestic demand were and continue to be effective in reflating the economy. China's debt is predominantly internal and semi-public; the central government could leverage up to resolve the local government debt conundrum. A talent dividend and employment optimization could offset the dissipating population dividend; and finally, China's high-quality opening, its participation in the multilateral system and its meaningful engagement with the Global South help counteract the decoupling/de-risking strategies of the US. In sum, while challenges abound, China's sound economic foundations and sensible developmental and macroeconomic policies help to propel economic growth, structural transformation, and green transition.

KEYWORDS: China, Economic Recovery, Public Debt, Government Debt, Job guarantee, Financial Structure, Economic Collapse

JEL CODES: O20, O53, E12

INTRODUCTION

Western media and scholars have long sensationalized the tale of China's economic collapse. Lately, they claim that the four "Ds" (Odd Lots 2023)—Deflation, Debt, Demographics, and Decoupling/De-risking—are insurmountable forces that will end China's economic growth. These are no doubt critical challenges facing the Chinese economy, but should be understood in the context of China's structural transformation. Further, these challenges are not met with inaction. The Chinese government has proactively crafted policies to address these economic headwinds while accelerating the economic transformation. The history of China's economic development over the past four decades reveals that economic progress is rarely smooth; the path to national rejuvenation and economic modernization is always full of roadblocks, but challenges harbor opportunities. The current difficulties will catalyze structural reforms and policy activism in China. The Chinese economy will steadily advance through industrial renewal, structural optimization, and the formation and growth of the new quality productive forces. Below, we will further interpret and analyze the four challenges mentioned above, striving for a more balanced and rational understanding therein while proposing measures to turn them into new opportunities.

"DARE TO CONSUME, ABLE TO CONSUME, WILLING TO CONSUME"

Western observers of China often point out the lack of consumer demand and argue that weak consumer demand is caused by insufficient household income—a phenomenon known as "a wealthy nation, but poor people." They further conclude that weak consumer demand leads to overcapacity and deflation. However, based on data from the Organisation for Economic Co-operation and Development (OECD) (n.d.), Chinese household income accounts for nearly 60 percent of GDP, similar to countries like Canada, Japan, and Germany, and higher than South Korea and Sweden. Given the rapid growth of household income over the past 20 years, China's average annual growth rate of household final consumption reached 9.3 percent (Liang 2023), more than three times the world average, based on the World Bank data. At the same time, due to the rapid growth of investment in recent decades, final consumption's share in GDP remains relatively low at 56 percent (though one may quibble that the consumption statistics fail to capture some of the service consumption [Han 2023]), compared to 66 percent in India and 67 percent in Thailand. From this perspective, there is room for growth in consumption share. The question, then, is how does China stimulate consumption growth? Western scholars typically suggest cash handouts to consumers, but believe the Chinese government will refuse to do so as it prefers a centrally controlled production model over decentralized, consumption-driven growth. However, such a speculation is unfounded. President Xi Jinping has clearly stated that China needs to drive consumption growth by ensuring the public “dare to consume, can consume, and are willing to consume.” “Dare to consume” means that consumers have the confidence to spend; “can consume” means there must be stable income to support consumption; and “willing to consume” refers to having high-quality products and a favorable consumption environment that enables consumers to make consumption choices. While it is necessary to provide income assistance to poor households, teaching people to fish is better than giving them fish, as the old Chinese saying goes. A one-time cash handout will most likely be saved or used to pay down debt rather than for consumption; and continuous cash handouts amount to a basic income guarantee scheme, which would be inferior to a job guarantee program (Tcherneva 2020).

It is well known that Chinese households have a strong preference for saving. The household savings rate (the proportion of household savings to disposable income) in China is close to 35 percent, while in the United States, it is 15 percent, and in the European Union, 13 percent. Additionally, due to the COVID-19 pandemic, Chinese households have increased their saving propensities, evidenced by a whopping increase of $8.9 trillion worth of household bank deposits from January 2020 to November 2024 (using an exchange rate of $1=7.1 yuan) (People’s Bank of China 2024). A survey by the People’s Bank of China in the fourth quarter of 2022 showed that 61.8 percent of Chinese people wanted to "save more" (Caixin 2023). These savings helped Chinese households cope with the sudden outbreak of COVID-19 and the resulting economic shutdown. However, once the pandemic ended, people continued to save more—out of uncertainties and weak confidence—leading to weak consumption.

In the short term, boosting household consumption requires uplifting consumer confidence. The Chinese government has introduced some stimulus measures to promote consumption, such as distributing consumption vouchers, reducing consumption taxes and fees, and offering sales subsidies and trade-in programs to encourage purchases of major items like EVs and household appliances. Many local governments are also taking measures to stimulate rural consumption, digital consumption, and services consumption. Moreover, the government is supporting private enterprises through policy measures and encouraging the private sector to create more job opportunities. The introduction of the "31 measures" (China State Council 2023) to stimulate private enterprises in 2023 conveys a positive signal to the private sector and a renewed commitment to leveling the playing field for private enterprises (e.g., access to government procurement, national labs, and favorable financing). Private enterprises provide 80 percent of job opportunities, and as they gradually recover and expand, this will lead to increased employment and income opportunities, thereby boosting consumer income and confidence. Finally, a raft of stimulus policies passed since September 2024 includes a 24-point guideline China State Council 2024) on the employment-first strategy issued by the state council. Stimulus policies also include more income supplement to low-income households, as well as plans to increase pay to civil service workers and raise pension benefits.

Long-term consumption growth requires structural changes and sustained productivity and income growth. Structural changes include growth in the high tech and emerging industries, but also further development of the modern service industries. China has embarked on a high-quality development path based on technological innovation and productivity growth. The development of new energy, green technologies, and the digital economy has fostered the emergence of "new productive forces," gradually replacing the past growth engines, such as real estate investment. These emerging industries will generate high-skilled, high-wage jobs, leading to healthy income growth, which will further enhance consumption capacity. That said, with automation and robotization, the manufacturing share of employment has been declining, from 28 percent in 2012 to 22 percent in 2022 (China National Statistics Bureau 2024). Meanwhile, the employment share of the services sector has increased. The services industry includes a range of growth areas such as tourism, entertainment, education, childcare and elderly care, public health, IT services, leasing and business services, public management, and social security, etc. Some of the service jobs have grown substantially in the past 10 years. Currently, services account for about 50 percent of China's GDP, far below the 70 percent level in developed countries, and its productivity is only about 20 percent of that in the United States (Zhu, Zhang, and Peng 2019). In 2023, retail sales of services grew by 20 percent, but services sector investment only grew by 0.8 percent. In other words, there is enormous potential for investment in the service sector. Developing the service industry not only improves productivity and creates high-paying jobs, but also offers high-quality services to meet consumer demand.

Another structural change involves continued urbanization, facilitated by the household registration (hukou) system reform, which is important in promoting long-term consumption growth. Currently, 500 million Chinese people still live in rural areas, and the income gap between urban and rural areas is still as high as 2.5 to 1, with rural consumption levels remaining relatively low. In addition, migrant workers are paid 22 percent less (Cheng, Hu, and Li 2020) and save 8 percentage points (Tan et al. 2021) more out of their income compared to their urban counterparts. Policies to support rural revitalization and relax household registration restrictions (to promote migrant workers' income and consumption) are crucial to promote rural and urban consumption, narrow the urban–rural consumption gap, and achieve urban–rural consumption integration. In cities, improving migrant workers' access to education, healthcare, and other public services will also reduce their precautionary savings and allow them to spend more on discretionary items.

Finally, as the Chinese economy develops, its social safety net needs to be strengthened. Indeed, the social security system has expanded continuously over the past decade. Latest figures show that social security and employment support expenditures grew by 175 percent and education expenditures grew by 87.5 percent during 2013–23 (Hart et al. n.d.). While the growth of spending in social safety net has been steady in the past decade, there is still room for further increase. Based on the OECD data, pension payments amounted to 7.7 percent of GDP on average, while in China, it was 5.4 percent as of 2023. The Ministry of Finance has pledged to continue increasing social spending and income transfers to support household income and consumption growth. Expanding the coverage of the social security system and public services will effectively reduce precautionary savings, boost consumer confidence, and provide more disposable income for consumers to make discretionary expenditures.

REDUCING PRIVATE DEBT LEVERAGE: THE NECESSARY AND POSITIVE ROLE OF PUBLIC DEBT

There is no doubt that, in recent years, both China and other countries around the world have seen their debt levels rise due to the impacts of the COVID-19 pandemic and the resulting economic slowdown. However, the so-called "debt crisis" in China stems from a misunderstanding of the difference between private sector debt and public sector debt. Although China's total debt-to-GDP ratio has reached 286 percent as of 2023, much of this is public debt held by central and local governments. The IMF estimates (IMF 2024) that the central government debt accounted for 24 percent of GDP, local government explicit debt accounted for 33 percent of GDP, household debt accounted for 61 percent of GDP, and non-financial corporate debt was 168 percent of GDP, which may appear dauting. However, much of the so-called non-financial corporate debt is actually debt from local government financing vehicles (LGFVs). The IMF estimates that the LGFVs debt has reached 60 trillion yuan, or about 48 percent of GDP in 2023. In other words, if we categorize debt correctly, local government debt should account for 81 percent of GDP, while non-financial corporate debt should be adjusted down to 120 percent of GDP. In short, much of China's debt is public or semi-public debt, while non-financial corporate debt is similar to the level of South Korea and Japan, and household debt is much lower than major economies like those of the US, the UK, Japan, and South Korea.

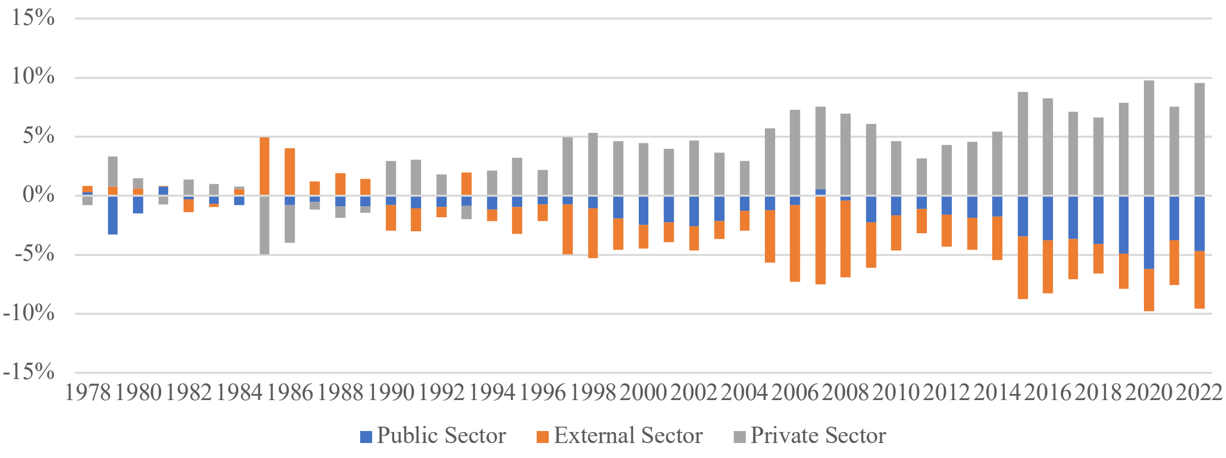
Traditional views hold that public debt is harmful and risky, because the government could "run out of money" or public debt implies deficit spending and excess demand-driven inflation. However, the reality is far from it. First, the vast majority of the public debt is denominated and repayable in yuan. The Chinese central government has the monopoly power of issuing its national currency and cannot "run out" of the yuan to repay its debt. Second, China's inflation rate in 2023 is merely 0.2 percent, and there is no inflationary pressure caused by government spending and public debt. Third, public debt plays a crucial role in maintaining economic stability and funding social welfare projects such as education, medical care, and social security. By financing public services and social programs, public debt can stimulate economic activity, improve productivity, create jobs and income, provide a social safety net, and enhance living standards. Fourth, much of the public spending and debt is used to fund public infrastructure such as high-speed rail, solar energy parks, grid modernization, and high-tech industrial zones, among others. These public infrastructure projects greatly enhance the connectivity of information and logistics, increase the production capacity of renewable energy, and promote the innovation and industrialization of advanced technologies. Although these infrastructures may not be profitable in the short term, they generate many positive externalities, improving the overall efficiency of the economy, and are indispensable for long-term economic development and transformation. Finally, as the IMF has pointed out, although China's public debt level is relatively high, the Chinese government also holds sizeable assets. As of 2019, the value of Chinese government assets reached $12.5 trillion (Lam and Moreno Badia 2023). The government's holdings in financial and non-financial public companies make up the largest share of its financial assets, valued at 68 percent of GDP, which is about three times the average of other countries. The IMF notes that the Chinese government has a healthy balance sheet and does not face a debt repayment risk. Therefore, the so-called debt crisis is alarmist and lacks factual support.

On the basis that there is no debt crisis, we should further recognize that central government debt is not only sustainable but also necessary. In order to effectively "de-leverage" the real estate sector and local governments, the central government must "increase leverage." The Chinese government is determined to adjust the real estate industry. Although real estate has been an important engine of economic growth for more than a decade, this engine is gradually losing momentum. On the one hand, speculation in the real estate sector has made housing increasingly unaffordable and has distorted the effective allocation of capital; on the other hand, with changes in population structure and total size, demand for housing will begin to stabilize. Excessive borrowing and expansion in the real estate sector will lead to resource losses and waste. Therefore, the "Three Red Lines" policy, implemented in 2020 to limit real estate leverage and restructure the industry, is highly necessary. However, since real estate investment accounts for over 20 percent of total fixed asset investment, a sharp decline in real estate investment may bring about financial risks and cause insufficient investment demand and deflationary pressure. In fact, the real estate adjustments in Japan in the late 1980s and in the US in the late 2000s resulted in disastrous economic consequences.

In contrast, despite the adjustment and downfall in the real estate sector, China’s real GDP grew at 5.3 percent in 2023 (partly due to the reopening from the COVID hiatus) and 5 percent in 2024. There are many reasons why the Chinese economy was more resilient and pressure-resistant. First, the central bank and state-owned commercial banks provided necessary liquidity to qualified real estate developers to complete unfinished real estate projects—the “white list” program set aside 2 trillion-yuan liquidity and was further expanded to 4 trillion at the end of 2024. This liquidity support has, on the one hand, helped alleviate financial risks, and on the other hand, ensured stability in the real estate market. Second, many cities have relaxed home-buying restrictions, and the government’s three major infrastructure projects, including affordable housing construction, urban village redevelopment, and "dual-use" public infrastructure development, have provided certain demand support for the real estate market, preventing excessive contraction. Third, investment in manufacturing and infrastructure has offset the contraction of investment in the real estate sector. In 2024, fixed-asset investment grew by 3.2 percent, despite a 10.6 percent contraction in real estate investment.

It is clear, from both the real economy and the balance-sheet perspectives, that government spending and government debt are necessary and effective tools to address the real estate sector adjustment. As discussed above, to offset the contraction in real estate investment, public investment in both the industrial sector and in infrastructure is necessary. From a balance-sheet angle, public deficit allows for the private sector to run a surplus. As shown in Figure 1, the economy can be divided into three sectors: the external trade sector, the private sector (households and non-public enterprises), and the public sector. The diagram shows that the balance of accounts is mirrored. In other words, if the government sector’s accounts are in deficit (spending more on the private sector than taxes collected), and if the trade account with other countries shows a deficit (China has a trade surplus), then the private sector’s accounts will show a surplus. Analyzing the macro balance sheet demonstrates the positive impact of fiscal deficits on the private sector’s de-leveraging and accumulation of surpluses.

Figure 1: China Sectoral Balance, Percent of GDP, 1978–2022



Source: China National Statistical Bureau (various years)

But local government debt is problematic, especially debt incurred by LGFVs. Local governments are responsible for 85 percent of fiscal expenditures, and in the past, land leasing income accounted for about 30 percent of government revenue. Due to the restructuring of the real estate market, local governments' fiscal spending and debt-servicing capabilities have been significantly constrained. If local government debt is not properly addressed, it could trigger losses for financial institutions, as well as negatively affect local economies. Therefore, the central government needs to adopt counter-cyclical expansion to offset and resolve local government debt and fiscal problems. In November 2024, the Standing Committee of the National People's Congress approved a 6 trillion-yuan additional local government bond issuance quota over the next three years to swap out LGFV debt, and another special bond issuance of 4 trillion yuan over the next five year to repay local government debt. These debt swap measures would help local governments better manage their debt, save on an interest rate payment of over 600 billion yuan, and therefore, spend more on public services and development projects, make wage payments to their employees, and repay arrears owed to private suppliers and contractors. All these benefits would help support local economic growth. That said, more forceful measures to reduce local government's debt burden. Having the central government take over part of local debt and increase fiscal transfer payments is the safest and most effective way to resolve local debt burden and fiscal issues. As a sovereign issuer of currency, the central government's debt capacity is far greater than that of local governments, and its bond interest rates, i.e., its borrowing costs are much lower than those of local governments. From this perspective, the central government's issuance of 1 trillion yuan in special bonds at the end of 2023, with funds transferred to local governments for disaster prevention and other infrastructure projects, is a reassuring move. But more is needed and it is expected that more measures to address local government debt and fiscal reforms will be announced at the National People's Congress in March 2025.

FROM THE LABOR DIVIDEND TO THE TALENT DIVIDEND

Many commentators have raised alarm about China's population shrinkage and aging. They argue that China's past growth was driven by abundant and cheap labor, and that, with the decline in the population dividend, China's growth will stagnate. However, this view contains at least four key errors.

Firstly, current research does not establish a direct and inevitable correlation between aging populations and slower economic growth. Economist Lin Yifu's research (Lin 2024) shows that, among 26 countries facing "aging before becoming wealthy" (where more than 14 percent of the population is over 65 and per capita GDP is less than half of that of the US), per capita and overall economic growth rates actually increased in the ten years after aging began, rather than declining. In China's case, although its labor force peaked at 800 million in 2015 (Statista 2024), China's growth continued at nearly 7 percent annually before the COVID-19 pandemic in 2019.

Secondly, China still has ample room to improve labor allocation. Official statistics show that 24 percent of China's workforce remains in agriculture, whereas the share of agricultural employment in developed countries such as the US (1.7 percent), France (2.5 percent), and Japan (3.2 percent) is much lower. This indicates that China is still in a stage of development and transformation, and a large portion of the workforce can move from agriculture to industry and services, thereby improving the effective allocation of labor.

Thirdly, although the total labor force is shrinking, the quality of China's labor force has significantly improved. Young workers entering the labor market now have an average of 7.8 more years of education than the retiring generation.

Lastly, China has accelerated industrial automation in recent years. In 2021, China installed 268,000 industrial robots (International Federation of Robotics 2022), more than the total in all other regions combined (249,000), representing a 51 percent year-on-year increase. As industrial automation continues to develop and labor efficiency improves, it will help mitigate labor shortages.

On top of the above four points, the Chinese government has also taken active policies to counter the aging population challenge. For example, they have recently raised the retirement ages, gradually in the next 15 years, from the current 60 to 63 for male workers, and from 50–55 to 55–58 for female workers. In addition, the government has gradually relaxed child birth restrictions and provided incentives and programs to encourage more child birth.

An important but often overlooked issue is that population aging also affects the demand side of the economy. China now has nearly 300 million people aged 60 or older, and by 2035, the elderly population will reach 400 million, accounting for 30 percent of the total population. As the proportion of elderly people increases, consumption levels and structures may undergo profound changes. According to a 2016 survey by the Chinese Academy of Social Sciences in six cities, the average consumption capacity of people aged 60–65 is about two-thirds of the peak consumption level of the 20–25 age group. Therefore, stimulating consumption and investment demand related to aging is crucial. For example, health and wellness products and services, elderly travel and recreational services, technologies and smart products for the elderly, pension financial products and services—these are all areas with enormous growth potential. The size of the "silver economy" is estimated to reach 7 trillion yuan ($972 billion), accounting for 6 percent of the country's GDP (*Xinhua News* 2024). By 2035, the value of the silver economy will rise to about 30 trillion yuan, accounting for 10 percent of GDP. Further, as mentioned above—with automation and robotization—even though the number of workers is decreasing, the quality of skills and labor productivity are increasing. Additionally, wages will rise, leading to greater purchasing power and improved living standards. Overall, from the demand-side perspective, population aging is both a challenge and a significant opportunity for China's economy.

HIGH-LEVEL OPENNESS

Western observers of China argue that the rapid growth of China over the past few decades benefited from an open and inclusive international environment. They assert that with US approval, China joined the World Trade Organization (WTO), thus beginning an era of export-led growth. However, those days are now gone. In today's world, geopolitical tensions and regional conflicts are disrupting global trade and supply chains. Countries are increasingly adopting protectionist policies. As the IMF points out, nearly 3,000 protectionist measures were enacted in 2023, three times the number enacted in 2019. Global trade in 2023 is estimated to have fallen by 5 percent, and excluding conduit economies, foreign direct investment (FDI) globally is estimated to have decreased by 18 percent in 2023 (UNCATD 2023). Against this backdrop, the US has also adopted a so-called "de-risking" strategy with China, which has received some support from its European and Japanese allies. Compared to 2022, China's exports to the US fell by 13 percent and its FDI inflows decreased by 8 percent in 2023.

However, it is important to note that China has never been a passive recipient of the international order. China has played an active role in reshaping the global order in a multipolar and inclusive direction. At the same time, China continues to strengthen its comparative advantages, maintaining a strong competitive position in global trade and investment.

Firstly, China has strategically diversified its trade partners. Although the Western share of China's exports has declined, the share of trade with Belt and Road Initiative (BRI) countries has grown from 39.2 percent in 2013 to 45.5 percent in 2022. ASEAN has become China's largest trading partner, accounting for 15.4 percent of total trade in 2022. In 2023, China's exports to BRI countries exceeded those to the US, the EU, and Japan combined. China is firmly advancing the BRI and enhancing trade cooperation and trade facilitation with ASEAN countries, BRICS countries, and the Global South in general.

Secondly, as a responsible major power, China is striving to stabilize relations with the West. Open and constructive meetings between President Xi and President Biden during the 2023 G20 summit and during the APEC Summit in November 2024 helped maintain high-level communications and dialogues so as to stabilize bilateral relations and reduce the chance of geopolitical miscalculations.

Thirdly, China continues to develop and strengthen its manufacturing capabilities. China accounts for 30 percent of global manufacturing capacity and holds a dominant position in the global supply chain of many industrial products, such as electric vehicles, lithium-ion batteries, and solar panels—referred to as the “new three” in exports. Notably, China has replaced Japan as the world’s largest car exporter, with 4.91 million cars exported in 2023. These technology-intensive and high-value-added exports have replaced the “old three” of clothing, home appliances, and furniture. China's export product structure continues to optimize and upgrade, reflecting the new trend of high-quality economic development in China. "Made in China" is actively contributing to the global green and low-carbon transformation, while also reflecting China’s strong competitiveness in the global trade system.

The decline in FDI inflows is caused by a combination of factors. US industrial subsidies and the “de-risking” strategy may have persuaded some US investors to bring their investments back to the US. The rise in US interest rates and higher financial asset returns may have encouraged some foreign investors to withdraw investments from China through arbitrage. Higher interest rates could also increase the financing costs for these foreign investors. Lastly, the enhanced competitiveness of Chinese domestic companies may have forced market-oriented investors to reconsider their investment strategies in China.

Despite the decline in FDI in the short term, we still have ample reason to believe that market-seeking and efficiency-driven investors will continue to find China highly attractive. China’s economy remains a global highlight, with its safe and reliable environment, high-quality infrastructure, skilled labor force, complete supply chains, and industrial clusters, as well as continuous market openness and supportive policies (e.g., the newly passed "21 Commitments" to open more markets for foreign investors), and an ever-growing middle class—these are advantages that other countries cannot easily replicate. This is why, even with the "China + 1" investment strategy, businesses continue to heavily invest in China. While China's share in the global FDI may decrease, the value of FDI in China will continue to rise. In other words, foreign investors can expand the "cake" rather than cut it into smaller pieces. This also explains why, despite Western media's exaggerated claims of the "collapse" of China's FDI, business surveys show that most foreign investors choose to continue expanding their investments in China.

A special report by the South China American Chamber of Commerce on February 27, 2024, showed that 62 percent of 183 surveyed companies chose not to shift their investments out of China, and most that did move investments out only withdrew less than 30 percent of their projects. Notably, 66 percent of US-owned enterprises chose to deepen their commitment to the Chinese market, and 86 percent of the companies surveyed stated that they would not withdraw from China due to US–China trade tensions. On the other hand, although the surveyed companies were optimistic about China's economy and market, their reinvestment budgets for profits in China were somewhat reduced. This is understandable against the backdrop of China's economic transformation and the complex international situation.

It is important to note that China is no longer the "poor and backward" country that needs to heavily rely on foreign capital to fill foreign exchange gaps. Instead of focusing on the quantity of foreign investment, it is more important to emphasize the quality of foreign investment. What China needs are high-tech industries, advanced organizational and management skills, and reliable partners. In this regard, China is still performing well in attracting foreign investment. In 2023, China's high-tech industries attracted 423.34 billion yuan in investment, accounting for 37.3 percent of the total FDI, which is a 1.2 percentage point increase compared to 2022 (Ren and Xu 2024). Major high-tech companies, such as Airbus from Europe and BASF from Germany, are significantly increasing their investment in China. This not only demonstrates China's attractiveness in high-tech manufacturing but also shows that China continues to learn from foreign companies and benefit from technology spillovers.

Finally, despite Biden's tech containment, China's technological development forges ahead. In a recent Bloomberg study[1], the authors conclude that Made in China 2025 has largely accomplished its original goals. Out of the 13 advanced technologies, China leads in five (high speed rail, electric vehicles and lithium batteries, solar panels, unmanned ariel vehicles, and graphene), is catching up in seven (LNG carriers, semiconductors, AI, robots, machine tools, large tractors, and drugs), and lags in one (commercial aviation). ASPI, an Australian think tank, also notes that China leads in 57 out of 64 critical technologies (Leung, Robin, and Cave 2024). Some have argue that the tech containment strategy indeed catalyzes China's whole-nation-system (Ju G uo Ti Zhi, 举国体制), which mobilizes billions of dollar worth of public investment in high-tech and galvanizes scientists and entrepreneurs to develop indigenous tech capabilities. The recent launch of the Deep Seek-V3, an open-source AI large language model (LLM), which achieves similar levels of performances as the Chat GPT 4.0 with just a fraction of the costs, is yet another testament to China's capabilities in technological innovations despite (or perhaps thanks to) US tech sanctions.

With Donald Trump returning to the White House in 2025, an intensified trade war is looming on the horizon. However, China is prepared to cope with Trump 2.0 (Liang 2024). On the one hand, China is likely to retaliate proportionately, should the 60 percent across-the-board tariff be imposed; on the other hand, China will defend itself from "a point of strength." This means China will continue to roll out stimulus policies to stabilize short-term growth while undertaking structural reforms to bolster domestic demand and upgrade supply capabilities. The Central Economic Work Conference (CEWC) held in December 2024 announced nine major economic priorities and tasks for 2025 (China Briefing 2024). First and foremost, it calls for boosting domestic demand—promoting consumption demand and improving investment efficiency. Second, it emphasizes the promotion of technological innovations and development of new quality productive forces. Other tasks include economic system reform, high-level opening up, financial risk prevention and diffusion, rural revitalization, regional coordination and unified national market building, decarbonization and green development, and improvement of living standards for the people. These policy focuses reflect a profound understanding of the Chinese

[1] https://www.bloomberg.com/graphics/2024-us-china-containment/

economic reality—both in terms of the challenges and potentials—and rightly address the challenges.

To support the economy, the CEWC specifically highlights the deployment of “unconventional countercyclical policies,” including “more proactive fiscal” and “moderately loose monetary policy.” This signals that the monetary authority will continue to cut required reserve ratios and policy rates to reduce the cost of credit, and perhaps set up special facilities to support the stock and housing markets. On the fiscal front, the CEWC signals an expansion in fiscal spending and issuance of special-purpose bonds. While the specific scale and terms of the special-purpose bond issuance are still unknown, some sources have suggested 3 trillion yuan worth of issuance to finance three undertakings. First is the so-called “two major, two new” initiatives to bolster domestic demand (two majors refer to strategic investment projects, such as the construction of railways, airports, and farmland; and the two new refer to the trade-in programs for consumer appliances and durable goods, as well as subsidies for large-scale equipment upgrades for businesses). Second is the support for advanced manufacturing, technological innovations, and emerging industries. The third undertaking is to recapitalize major banks. It seems what is missing in the list is the funds need to resolve or improve local government indebtedness.

Externally, China will continue to strike for a “stable, healthy and sustainable” relationship with the US, but it will also engage more actively with the Global South as well as the non-US Western economies that have an interest in maintaining a multilateral system. While China has front-loaded some retaliatory measures, such as restricting the exports of Gallium, Germanium, and other critical minerals to the US to deter further aggression from the Trump administration, it must and will strike a fine balance between engaging with the US and retaliating against the US. Retaliations come at a cost, and can weaken China’s own engagement with the global economy. Rather than impose retaliatory tariffs, export banks, and restrict US firms’ Chinese subsidiaries, depreciating its own currency, it is better for China to bolster domestic demand, expand overseas markets outside of the US, invest abroad for fortify global supply chains, and cooperate with the Global South countries and US allies. Trump’s trade war 2.0 would be a major challenge for China, but it again would provide opportunities for China to both strengthen its economy and engage more meaningfully with the rest of the world as the US retreats from it (Liang 2024).

CONCLUSION

Over the past 40 years, Western media, academia, and political circles have relentlessly promoted the theory of China's economic collapse. However, the rise and development of China's economy have fully demonstrated its resilience, vitality, and potential. Currently, facing the challenges of domestic economic transformation and a complex international situation, the Chinese government will have no choice but to continue to deepen reforms, lead all market entities in expanding new spaces for economic development, cultivate and grow new productive forces, adhere to high-level openness, and promote win-win cooperation. Achieving modernization with Chinese characteristics and national rejuvenation is the will of the people, and "the people hope, and the government acts." It has been a time-honored tradition that the Chinese people, when united in purpose, can overcome difficulties together and continue to make China's economy stronger and more prosperous.

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