China's Fiscal Stimulus Policies in Response to GFC and COVID Crisis

Jingxuan Wu
Beijing National Day School, Beijing 100000, China.

Abstract: This paper focuses on discussion of China's economic policy especially in response to Global Financial Crisis and COVID-19, with emphasis on infrastructure investment stimulus package policy as reference, analyzing the integration of economic theories with China's accurate stimulus package during this counter-cyclical period. This may offer reference for other economies that are facing similar challenges. In 2020, China implemented a significant infrastructure stimulus policy aiming to boost economic growth and creating jobs amid outbreak of COVID-19 pandemic. This policy involves a number of measures including increased government spending on infrastructure projects and encouraging private investment in areas such as renewable energy and digital technology. The paper analyzes pros and cons of this policy including long term and short team impact to economic development. When the market economy develops for a certain period, it will always meet with the "Minsky moment", prosperity and bubbles will interact. We need to realize that stimulus package was a short-term remedy, we need make a good diagnosis of what the real reason that cause problem so that we can take those into our future economic policy choices to better navigate us amid various economic cycles.

Keywords: China COVID Stimulus Policy; Economic Policy; Infrastructure Investment; Spill Over Effect

1. Introduction

After the 2008 subprime mortgage crisis, through the stimulus policies led by the United States, the European Union, and China's RMB4 trillion(US$564 billion) fiscal investment policy, with the help of globalization, the world economy has ushered in a relatively stable stage of low inflation, low interest and with high debt. Until the outbreak of the Covid epidemic, the world economy suddenly fell into a liquidity crisis[1]. Confidence of consumer groups was lost; the economy is landing in high inflation and with fear of stagflation. China, the world's second economy, has attracted attention from all aspects on how it maintains a sustainable economic growth in economic counter-cyclical period.

Under the market economy, Keynesian economics, Hyman Minsky's financial instability hypothesis and other economic theories give some answers to the stable growth of the economy and the response to the crisis. This paper focuses on discussion of China's fiscal policy especially in response to GFC in 2008-09 and Pandemic crisis in 2020-01, taking China's fiscal policy with emphasis on infrastructure investment as reference, analyzing the integration of economic theories that empowers sustainable economic growth. China's accurate stimulus package during this counter-cyclical period offers some useful reference for both advanced and emerging economies who are facing the ongoing challenges in economic development amid COVID situation.

Keynesianism (also known as Keynesian economics) advocates that the state adopts expansionary economic policies to promote economic growth by increasing demand. That is, expand government spending, implement deficit finance, stimulate the economy, and maintain prosperity.

After analysis of USA stimulus package during the two crisis, we found that Keynesianism has a profound influence on USA policy maker.[2]

Table 1 Debt Level 2008/09 v.s.2020/2021

2008/09	2020/2021
high debt	higher debt
low interest	Higher interest rate
low inflation	high inflation
11-year growth after	GDP contract Q1 2022

In the Table 1, we found that economics theories play important role in dealing with different cause of crisis in the USA, but the practical results are different. We also found that Heyman Minsky financial instability hypothesis need to pay more attention even in economy stable growth period. Hyman Minsky quote: “stability breeds instability” and “stability is destabilizing.” If an economy is stable, it is likely to become unstable in the immediate period or future. It is good to use compounding and superimposing economic theory. With the rise of inflation, especially with the beginning of the interest rate hike cycle in the United States, whether debt austerity causes stagflation is a matter of close concern.

2. Analysis the impact of China stimulus policy

China has also adopted economic theories such as Keynesian to deal with the two crisis. In response to the global financial crisis in 2008, Chinese government implemented RMB 4 trillion (US$575 billion) stimulus package. Most of this stimulus on various government-led projects, particularly hard infrastructure like high speed rail lines (HSR), train stations, metro systems, and airports. In the past decade, the vast expansion of HSR, for instance, now accounts for almost two thirds of the global total network, dramatically transformed day-to-day life in China for millions of citizens and businesses, and continue to provide long-term economic benefits[3].

In the meantime, China accumulated relatively high debt as well. In the face of the possible "Minsk moment" as rest of the world after pandemic meltdown, China did not mechanically copy Western economic theory but used compound financial instruments after Pandemic to come out of a way of responding to the crisis with Chinese characteristics. This makes China in a unique position from rest of the advanced countries—[4] relatively low inflation with stable currency, no skyrocket debts like USA, in which create a foundation for economy to have a long run (Figure 1).

China's RMB 4 Trillion stimulus plan in 2008	billion(USD)
Transport and power infrastructure (railroads, roads, airports, electricity grids)	219.0
Post-earthquake reconstruction	146.0
Rural village infrastructure	54.0
Environmental investment	30.7
Affordable housing	58.4
Technological innovation and structural adjustment	54.0
Health and education	21.9

China's Covid-19 stimulus plan RMB 31.6 Trillion		
ITEM	2019 billion(USD)	2020 billion(USD)
Central government budget deficit	2.8%	3.5%
Pandemic bonds	--	142.9
Construction project investment fund	88.2	85.7
Railway construction fund	117.6	128.6
Quota for 'Special bonds' issue by local governments	316.2	535.7
Bank lending, status for the first six months	1426.5	172.9

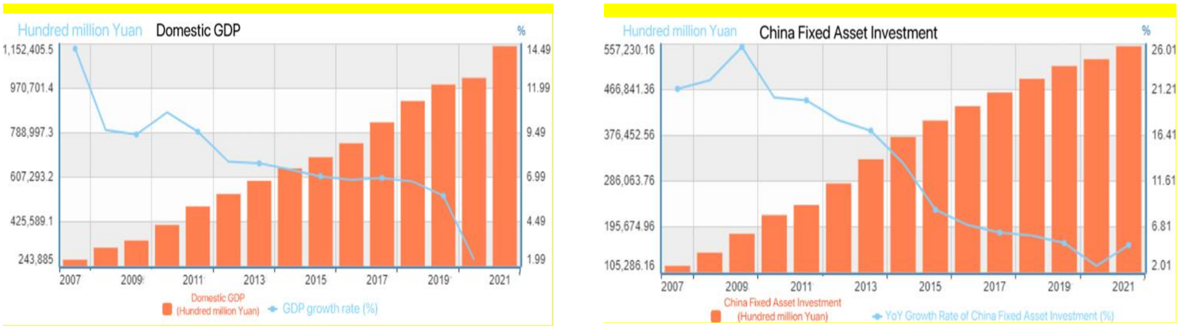
Figure 1 China’s stimulus plan in 2008 and 2020 (Data: Xinhua Net- China Fiscal Policy 2021)

In 2020, China again implemented significant infrastructure stimulus policy which aimed at improving economic growth, securing jobs amid COVID pandemic. This set up policies include increased government spending with focus on infrastructure projects like railways, highways, 5G networks together with measurement on encouraging private investment in areas such as renewable energy and digital technology. This resulted in China’s strong economy rebound in 2H 2020 into 2021 since the policy successfully promote confidence in the economy including new jobs, increased consumer spending. However there is argument about the long-term sustainability of China’s growth model which was partially caused by the surging of debt level, environment impact on certain over spending industries [5]. Some analysis of this policy is provide as following:

Firstly, in the early stage of the epidemic, one trillion special treasury bond was issued, taking advantage of China's unique industrial chain, focusing on epidemic-related PPE, not only meet domestic demand but also Increase Exports. With strong PPE related medical industry huge contribution, China achieves GDP from contraction to expansion before The Rest of The World's Economies.

Secondly, amid the slowdown of economy under COVID-19, China’s plans to bolster growth as COVID outbreaks and lockdowns activity is seen $5.3 trillion pumped into its economy in 2020. China again largely refrained from providing direct financial support for its citizens (comparing to the practice in U.S.), rather focusing its relief exclusively on private businesses and government investment. The $500 billion stimulus package in China revealed in May 2020 was overwhelmingly focused on infrastructure spending to create more jobs and brings in liveliness of economy[6].

Thirdly, China has launched economic policies to deal with COVID-19 on the economy amounting to $2.3 trillion or 16.1% of GDP by the end of May 2021. Supporting policies to SME to secure employment and obtaining credit; Fiscal support including tax cuts and social security contribution exemption, support for infrastructure investment, industry-specific programs, and consumers subsidies. CNY1 trillion in special COVID-19 bonds were issued to strengthen local government finances. The consistently executed infrastructure investment stimulus over the years together with other fiscal policies successfully helped China economy stepping out two times of V shape economy cycle (2008-09/2020-21 inclusive), avoiding economy recession and empower the economy with strength for further development.



(a) (b)

Figure 2 (a) China GDP 2009/2021 after stimulus; (b) China Fixed Asset investment. (Source: China National Bureau of Statistics)

China' infrastructure investment stimulus has remained an important tool to stimulate the economy (2008-2009, 2020-now). It is a short-term cost but creating long-term gain (Figure 2) [7].

Analysis of this economic policy impact in the short run:

- **Increased construction activities:** the policy led to increased spending on infrastructure projects which boost the liveliness of construction spending around the country. This in terms improves employment rate with spurred job creations.
- **Avoid recession:** the significant public sector investment in infrastructure has partially offset the pressure resulted from economy slowdown. The stimulus package contributed to improved GDP growth in 2020, giving China as one of few major economies to experience positive growth amid pandemic years [8].
- **Helping employment:** infrastructure investment brings up new employment opportunities. Employment in the new high-tech infrastructure increases innovation capacity, which has partially mitigated overall unemployment pressure because of the reduced investment from private sector and export related service sector.
- **Spillover effect:** short-term impact of infrastructure stimulus has positive contribution on the total economic demand not only creating additional demand in China but has also brought up increasing demand from other countries via export, particularly those countries in Asia and Africa that have close ties with China including Indonesia (high speed railway between Jakarta and Bandung and developing the Jakarta-Bandung New Economy Zone).

Analysis of this economic policy impact in the long run:

- **A Great Leap Forward:** It is reviewed by the World Economic Forum the Global Competitiveness Index shows that China's overall infrastructure has improved significantly in the past 10years from ranking of 66 of 152 countries to 36 in 2019, this reflects China's increased investment in infrastructure to prop up demand [9]. Basic infrastructure development helps China to remove long outstanding bottom neck on economy development including lack of advanced transportation related infrastructure upgrade, which is set to lift productivity and to build pillar of future growth.
- **Improving productivity:** the investment has increased regional spillover effect for higher productivity, which include time and cost saving for business and individual travelers, increased scope of market access, all of which helps to boost economic return in the long run[10].
- **Benefit for the local economy development:** infrastructure investment especially HSR has significantly upgraded local

economic development, this brings in long term benefit especially given the economic development gap between eastern and western regions, inner land and coastal cities in China, these investments has narrowed down the imbalanced development for China, achieving great improvement of life quality to the population.

China’s massive fiscal stimulus played an important role in the overall recovery of the global economy. The well-chosen infrastructure investments not only could finance themselves in the long run through stable economic rate of return, but also helped improve business climate and crowded in the private investment as well as boosting employment in the related industry sector, therefore enhanced productivity growth[11].

3. Conclusion

China’s massive economic stimulus plays an important role in the recovery of the global economy. The well-chosen infrastructure investments not only financed themselves in the long run through a good economic rate of return, but also helped improve business climate and crowded in the private investment as well as boosting employment in the related industry sector, therefore enhanced productivity growth.

The implementation of stimulus policy has demonstrated the extent to which Chinese government continues to rely on administrative instruments to manage the macro economy along with monetary policy. The experience has shown the advantages including quick results. It’s also important to closely observe the trend of debt increase (170% Total Debt/GDP in 2008 to 272% Total Debt/GDP in 2021-data from China National Statistics Bureau), adjusting local government funding tools, improving the efficiency and effectiveness of public expenditures and public investment, in order to build a sustainable growth economy into future.

To sum up, we will encounter various economic crisis in the future. When the market economy develops for a certain period, it will always meet with the "Minsky moment", prosperity and bubbles will interact. We need to realize that stimulus package was a short-term remedy, we need make a good diagnosis of what the real reason that cause problem. As for USA and western country’s economists suggested to borrow more and spend more, that was not the method to save economy from going to recession. As for most Asian economies, macro-policies were introduced and enforced directly targeting market entities, which are the backbone for economy to recover and demonstrated effectiveness. It is necessary for policy makers to flexibly use financial instruments to empower short-term and long-term sustainable growth. China’s accurate stimulus plan under this economic counter-cyclical period can be valuable references for countries that are still fighting the economic shock from the pandemic.

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