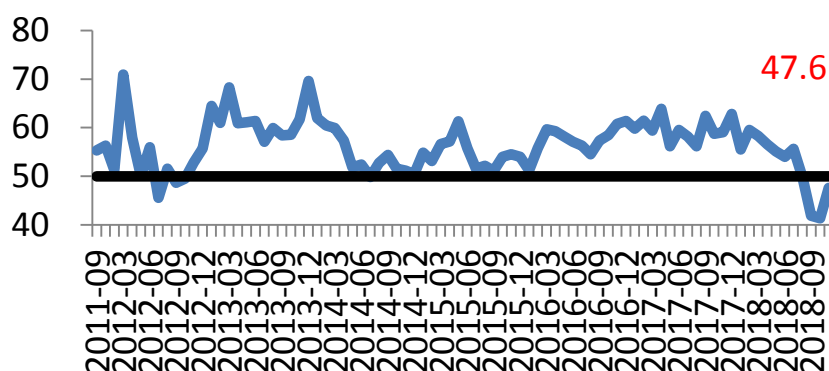


### Commentary on the November 2018 CKGSB BCI

Professor Li Wei

In November, the CKGSB Business Conditions Index (BCI) moved towards the confidence threshold, landing at 47.6. This is a marked improvement on last month's reading of 41.9 (Figure 1).

Figure 1 Business Conditions Index (BCI)



Source: CKGSB Case Center and Center for Economic Research

This month's BCI reading resembles a collective counterattack after a run on all economic indicators over the last few months. In November, apart from costs and recruitment, all the other operational indices rebounded. Even the financing environment index that had fallen again and again these past months rose from 25.0 to 31.5. For specifics, please see this month's BCI report.

Why has there been such a dramatic shift this month? The most important reason is a change in policy. Recently, the government made public a series of concrete, large-scale offers to support private enterprises, especially the hardest-hit, private SMEs.

The first thing to consider is the impact of a private business symposium held between President Xi Jinping and representatives from 54 large, medium and small private enterprises. They represented manufacturing, online companies and pharmaceuticals, but excluded real-estate developers. The symposium addressed market concerns.

In the President's speech, he affirmed the positive role of private enterprise in China's economy and stressed the need for "unwavering encouragement, support and guidance for the development of the private economy." He pronounced that private enterprises had "contributed more than 50% of tax revenue, 60% of GDP, 70% of innovations, 80% of urban employment, and 90% of enterprises." Xi expressed his disapproval of perspectives shared by netizens suggesting that private business was useless, should quit the market, or should be merged with state industry according to a "new public-private partnership theory."

In addition to giving a much needed confidence boost to private business, President Xi Jinping offered six specific proposals to support the development of private enterprises, including:

1. A reduction to corporate taxes and fees. Xi called for "increased tax reduction efforts, and substantial cuts to taxes included VAT."

2. Lifted financing constraints. Xi said bank performance appraisals should be linked to support the development of the private economy, and should not come down to a generalized reluctance to lend.” Xi also addressed “issues with some government departments and large enterprises that have taken advantage of their dominance to bully smaller firms and default on their loans, impacting on the availability of funds for private business.”

3. Create a level playing field.

4. Improve the way policies are implemented. Xi proposed that “capacity-reduction and deleveraging policies should apply to all types of enterprises equally. The government should not wear tinted-glasses when implementing such policies, or use prejudice when it comes to debt repayments.”

5. Build a new, more cordial relationship between government and business, and promote the healthy development of the non-public economy and the healthy growth of non-public entities. Xi said the government was determined “to support and guide state-owned enterprises and private enterprises, especially small and medium-sized enterprises, in overcoming difficulties, in innovation and development, and be strongly involved in supervision.” The government would continue to “strengthen public opinion guidance, publicize party policy, and guide the national policy discussion, so as to clarify misinformation as soon as it occurred.”

6. Protect business interests. Xi Jinping pointed out that “irregular practices have taken place in private business. From a developmental perspective, these should be dealt with according to the law and the principle of innocence until proven guilty. Entrepreneurs can take comfort in the government’s reiteration of the law. Xi repeatedly stressed the need to identify mishandled cases that infringed on business property rights. He mentioned several recent cases that were reversed in the People’s Court, meeting societal approval.”

Although Xi Jinping’s speech was less than 7000 words in length, it clearly and comprehensively expounded on the current attitude of the central government towards private business and the policies it was preparing to implement in support of their development. The speech was highly targeted, full of detail, and truly of comfort to struggling private businesses across China. Shortly afterwards, even more powerful policies were announced.

From November 5 to 7, the Supreme People’s Court stated that it would stop economic disputes being brought to court as crimes and prevent civil liability from being treated as criminal responsibility. The Supreme People’s Procuratorate stated that criminal cases transferred by the relevant departments involved corruption, and it was necessary to take compulsory measures in a prudent manner and fully consider the need to protect business development.

On November 6, Yi Gang, Governor of the People’s Bank of China, said that the bank would adopt policies to permit more liquidity to flow to private enterprises and areas in which it was most needed. First, it would direct increased credit towards private enterprises, especially small and micro enterprises. Second, it would support bond issuance for private enterprises. Third, it would set up an investigation into how best to establish equity financing tools for private firms.

On November 7, Guo Shuqing, chairman of the China Insurance Regulatory Commission and chief banking regulator, said in an exclusive interview with *Financial Times* that according to the contribution of private enterprises to the national economy, initial targets would be set: For large-scale banks, lending to private companies should not be less than 1/3 of all new corporate loans, and for small and medium-size banks, no less than 2/3. After three years, the proportion of lending to private enterprise should account for no less than 50% of new corporate loans. This has been called the “125” ratio.

According to incomplete statistics, loans to private enterprises account for 25% of the current banking loan balance, despite the private economy having contributed more than 60% to the national economy.

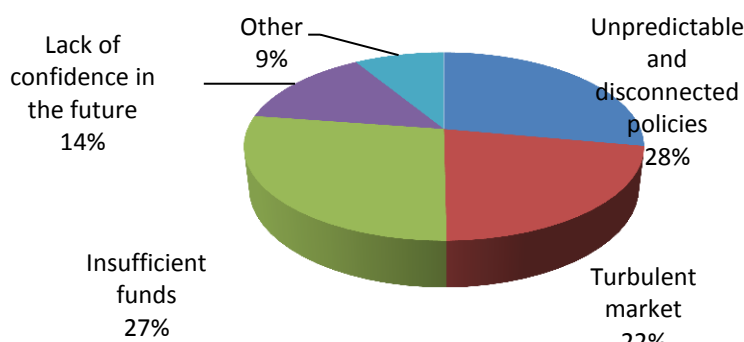
These are just some of the many measures announced in recent days, the details of which we will not discuss further here. What should be noted is that within the existing institutional framework, the decision-making level is indeed making a real effort to help private enterprises develop its way out of various bottlenecks. So what are the effects of these policies? This month we added a temporary survey to explore this. The questionnaire consisted of four questions (two multiple-choice, and two open-ended).

The first multiple-choice question was: “Central government official have just spent considerable time motivating private enterprises. Has your confidence in future business conditions changed in any way?” Our data point of 66.9 is high, showing that most sample firms have seen their confidence levels increase recently. It indicates that central government encouragement to private enterprises has had a positive impact.

The second multiple-choice question was, “Recently, central government has introduced a series of policies to ease private businesses’ financing woes. How have these solutions been felt in your company?” Our data point is 52.2, much higher than the corporate financing index of 31.5 (the corporate financing environment index measures year-on-year). This means that central government policies to lighten private companies’ financing pressures have had a positive effect.

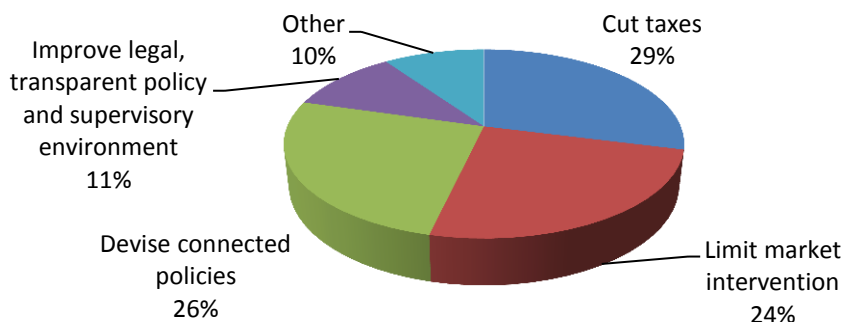
As for the final two open-ended questions, we classified answers in the following pie charts:

Figure 2 Business worries



Source: CKGSB Case Center and Center for Economic Research

Figure 3 What the government should do



Source: CKGSB Case Center and Center for Economic Research

The above two charts show us the way forward. What private businesses appear to need most is not “remedial” action such as credit easing or a new round of subsidies. They need a fair and equitable marketplace in which the government acts as a small but strong force, imposing taxes lightly but fairly, and without extreme shifts in direction. What the Chinese economy needs most is not the flourishing of certain high-tech sectors, but institutional support for the entire array of industry. In such an environment, fair competition will bring out the most efficient, and the entire economy will be nourished. Upgrading will follow, and the current extensive growth model will give way to a more intensive one. This is the way forward for the Chinese economy, and will act as a sustainable driving force to improve everyone’s standard of living.

This is the author’s commentary on the CKGSB BCI report for November 2018. Do not hesitate to contact the BCI team by email as shown in the accompanying BCI data report.

CKGSB Professor Li Wei  
November 27, 2018