

CHINA: THE ECONOMY HAS YET TO ABSORB THE END OF THE ZERO-COVID POLICY BEFORE GRADUALLY RECOVERING



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Event

Early December, Beijing made a sudden reversal of its nearly three-year long zero-Covid policy when it decided to end the strict containment rules, de facto paving the way to a 'living with Covid' approach. As a result, containment-related disruptions have been replaced by the impact of China's largest Covid wave on economic activity. The inevitable temporary health crisis, fuelled by a rapid economic reopening and happening during the winter, is expected to hit the country's economy in the first quarter of 2023 before easing and leading to a gradual strengthening of its momentum. Beijing endorsed the policy shift towards an economic focus at its Central Economic Work Conference mid-December. It confirmed proactive fiscal and monetary support to domestic demand and a stabilisation of the real estate market.

Impact

The sharp relaxation of zero-Covid rules marks the end of a socially and economically unsustainable policy. The negative economic impact was becoming increasingly difficult to bear. This being said, the timing of the decision can probably largely be explained by the rare landmark protests that occurred simultaneously in many large cities last November. The official message is now basically to downplay Covid-19-related risks, to request people to take care of themselves – while urging them to go to work in case of mild symptoms – and to call on tens of millions of elderly people to get vaccinated. Since the end of December, official reporting of contaminations has stopped, thereby making it more difficult to trace the evolution of the pandemic in China. However, the latest visible impact on overcrowded hospitals – amid estimated millions of new daily contaminations – and economic activity (which saw manufacturing production contract in December) leaves no doubt about the ongoing severe Covid wave spreading across large cities. Weak factory activity due to medical reasons, hindrances to mobility and corporate activity highlight the shock from this unprecedented Covid wave.

In the first quarter of 2023, GDP growth is projected to suffer before picking up gradually. Indeed, the expected easing of the Covid wave within one or two months, expanded fiscal stimuli and the central bank's rescue package to the property sector are likely to support the recovery. Moreover, further upside risks come from the services sector, which is likely to be boosted, notably by the removal of travel restrictions (including reopened borders, which put an end to international isolation), an improved business confidence for 2023 and higher private consumption, depending on the evolution of the health situation. Still, it is cautious to say that one cannot expect impressive performances this year, as the ailing property sector will not support growth as it did in the past and given weaker external demand from the sharply slowing US and EU markets. In a statement released at the end of November and thus before the changed Covid policy, the IMF expected China's GDP growth to rise to 4.4% this year (from +3.2% in 2022).

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