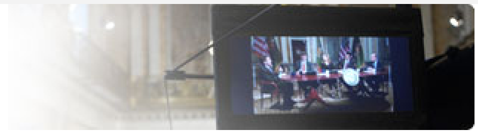
U.S. DEPARTMENT OF THE TREASURY

Press Center



Sheets Op-ed: The Importance of China's Transition to Smarter Growth

2/22/2016

WASHINGTON – In an op-ed published on Medium, Treasury Under Secretary for International Affairs Nathan Sheets underscored the importance of China's transition to a consumption-led economy, noting that if China implements the reforms that it has committed to, it has the necessary tools to support domestic demand and succeed in this economic transition.

Read the piece here.

The text of the piece follows:

The Importance of China's Transition to Smarter Growth
By Nathan Sheets

Later this week, China will host finance ministers and central bank governors from the G-20 nations for the first time since 2005. In the intervening decade, its economy has continued its remarkable rise, with its GDP last year climbing well above $10 trillion—nearly five times what it was when finance ministers from the world's largest economies last gathered as a group in Beijing.

China has become a key driver in commodity markets, a critical link in global supply chains, and increasingly a source of final demand for the exports of other countries' goods and services.

Yet even as its growth remains brisk—the International Monetary Fund expects China's GDP to rise 6.3 percent this year—recent financial market volatility around the world has put a spotlight on China's slowdown and the need for China to accelerate the pace of its transition to a more consumption-led economy.

We have long known that China's move from an economy dependent on manufacturing and investment toward one more reliant on services and household consumption would not be easy. But the transition is necessary for the economy to rebalance toward more sustainable engines of demand.

We continue to believe that if China implements the market-based economic reforms it has committed to, it has the necessary tools to support domestic demand and succeed in this economic transition. It is important for the Chinese to follow through on those commitments and to clearly communicate their actions as they do so.

The challenges to reform and sustaining domestic demand are real. China's service sector remains underdeveloped relative to other economies and China's households have unusually low incomes and consumption rates. Fiscal stimulus in China should boost household income and accelerate the necessary transition toward household consumption. This could include temporary cuts in payroll taxes and the value added tax, as well as taxes on some common household items such as soap and cosmetics.

Separately, the Chinese leadership has committed to not using the exchange rate to boost exports. The Chinese central bank has indicated that it is transitioning to a market-determined exchange rate, and that Chinese economic fundamentals support a basically stable renminbi. Clear communication to the market is critical during this transition—a transition that Treasury Secretary Lew and I, along with other U.S. officials, continue to press China to carry out in an orderly and transparent manner.

China's economic rebalancing will also require reallocating productive resources in the Chinese economy away from heavy industry. Consistent with its commitment, China must implement reforms of inefficient state-owned enterprises and reduce industrial overcapacity, including in its steel, aluminum, and coal sectors. Opening up its economy, including the services sector, will send a strong signal to markets that China is committed to reform and encourage greater foreign direct investment that can help support China's transition process. It must also strengthen the social safety net, implement land reform, and promote a more market-based financial system. And China must make these adjustments against the backdrop of high levels of debt.

Important progress has been made. For the past three years, China's services sector has grown faster than the industrial sector. Investment in services and more consumption-led sectors has remained strong, even as overall investment has slowed. And the number of new businesses registered in 2015—many in the service sector—totaled 4.4 million, a 22 percent annual increase.

Household and government consumption, meanwhile, accounted for two-thirds of last year's GDP growth. In 2015, 13 million jobs were created in urban areas, far exceeding the government target, while retail sales grew more than 10 percent. And auto sales have been robust, with China recently becoming the world's largest auto market.

A Chinese economy more reliant on services and household consumption would not only be more balanced internally. It would be more balanced externally so as to be less dependent on exports. This transformation would allow China to solidify its status as a driver of global demand and offers the best formula for China to achieve an orderly transition and put its economy on a more sustainable footing for healthy growth in the future. We want to see China make this transition, because we recognize that China's success ultimately benefits our own.

Nathan Sheets is Under Secretary for International Affairs at the Department of Treasury.

###