Commentary on the July 2020 CKGSB Business Conditions Index

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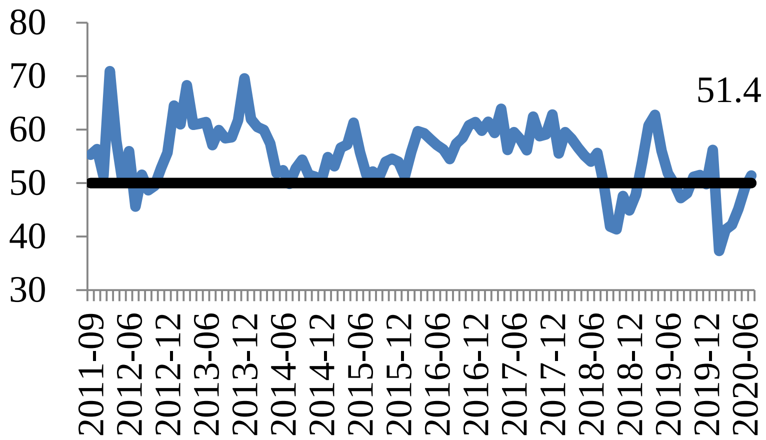
In July 2020, the CKGSB Business Conditions Index (BCI) crossed the confidence line from 49.1 to 51.4 (Figure 1). Government policies are clearly having a positive impact on business, especially private companies that comprise most of our sample. From this, we suggest that there is now a high chance that China's economic performance this year will end positively.

Figure 1 **Business Conditions Index (BCI)**

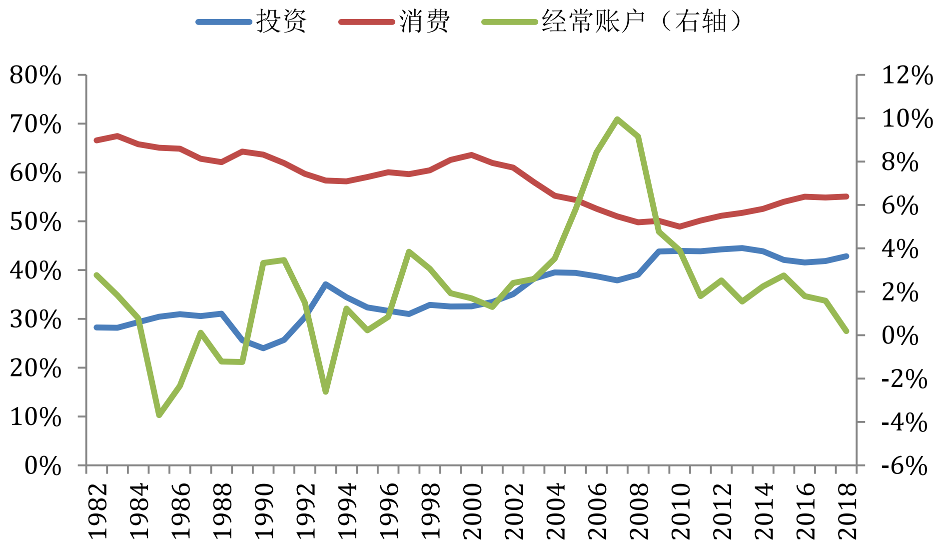


Source: CKGSB Case Center and Center for Economic Research

There are not many changes to the data this month, only minimal improvements. With an emphasis on the impact of decision-making on macroeconomics, 'internal circulation' has become a hot topic, despite not being clearly defined by anyone. In terms of semantics, internal circulation and domestic demand have a certain degree of overlap, referring to the operations-side of the domestic economy.

As a large country, it is essential that the Chinese economy is mainly fueled by domestic demand, rather than external demand. In around 2007, China's current account debt to GDP ratio was as high as 10%, provoking fear in the eyes of China's trading partners that China was "stealing" their domestic demand. Now the situation has completely flipped with the country's current account debt to GDP ratio having dropped to near zero (data for 2018, Figure 2). China can now mostly sustain its economy on domestic demand alone.

Figure 2 **China's Budget as a Percentage of GDP**



Source: World Bank
(blue = investment; red = consumption; green = current account)

In the process of becoming a country that relies mainly on domestic demand, China has had to follow a path to endogenous growth. The key has been improving the business environment so that industry and commerce can operate better. The World Bank officially released its "Doing business 2020" report on October 24, 2019.

China's overall business environment scored 77.9 points (China is at 77.9% of the global benchmark), an increase of 4.26 points over the previous year. At 31st in the world, China had improved its ranking by 15 places in a year.

The World Bank reported that due to the active reform agenda, China ranked among the top ten economies globally with the biggest improvements in business environment for the second year in a row.

Rui Ze, Director of the World Bank's China Bureau, said "China has made great efforts to improve its local business environment for small and medium-sized enterprises, keep up a good pace of reform, and make progress in a number of business environment indicators, especially in terms of handling construction permits."

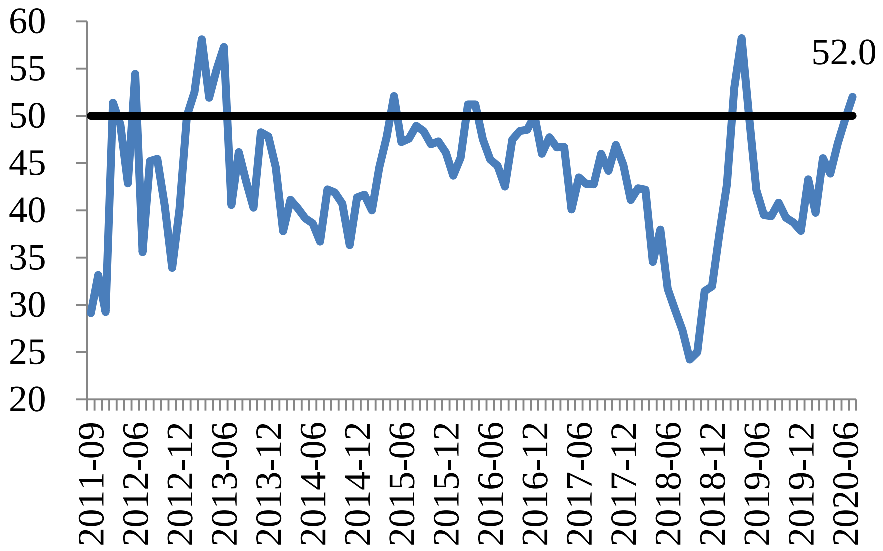
Of the ten World Bank indicators, eight have risen in China, one more than last year. Among them, building permits has improved from 88th to 33th, protecting small and medium investors has improved from 36th to 28th, bankruptcy handling has improved 10 places to 51th, and the ranking of cross-border trade has improved nine places to 56th. Taxation has improved nine places to

105th, electricity has stepped up two places to 12th, contract execution has moved up a place to 5th, and the start-up environment has moved up a place to 27th.

Despite all this, WTO reminds China it lags behind in tax payments (105th), access to credit (80th) and cross-border trade (56th). China's export border compliance takes 21 hours and costs an average of US$256, which is longer and more expensive than the OECD high-income economy average. It takes an average of 138 hours per year for Chinese companies to comply with fiscal and taxation regulations, compared with 64 hours in Singapore.

Our survey shows similar results. For example, China's financing environment index is generally sluggish, which is in line with the World Bank's report on how hard it is for Chinese companies to obtain credit (Figure 3).

Figure 3 **Corporate financial conditions**



Source: CKGSB Case Center and Center for Economic Research

While the World Bank report may have shortcomings of one kind or another, it does give us a horizontal and vertical benchmark by which to compare China's reform trajectory. We can see that great achievements have been made in some areas, while others still fall short. To a certain extent, competition in industry and commerce is all about the business environment. In today's world, capital and industry flow globally, and will go where conditions suit them. There is no question of patriotism, when environment is compared. Not only is this the case for international capital, but it also holds true for domestic capital. Cross-border and cross-provincial flows all compare business environments. For localities to develop their economy, they must attract investment. This investment is equally important whether it comes from abroad or outside the province. Therefore, the key is to improve the business environment, increase economic efficiency, and attract more investment to one's locality.

This is a commentary on the CKGSB BCI report for July 2020. Do not hesitate to contact the BCI team by email as shown in the accompanying BCI data report.

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30 July 2020