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HD **Why Chinese tiger may get second wind**

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Big Picture

Beijing still has the ability to stop the Chinese economy from braking too sharply by lifting government spending, says leading US economist Barry Eichengreen. In Australia as a guest speaker at a Centre for International Finance and Regulation (CIFR) conference on internationalising the yuan, Eichengreen says of China's growth outlook: "We're going to have to wait and see what kind of policy measures they take, if any.

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"I think they're more reluctant to ramp up infrastructure spending, they're more reluctant to increase the rate of growth of bank credit than they were four years ago. But I think they can still take some limited measures on spending, in particular. I'm still of the view that China is enough of a controlled economy that they can control the rate of deceleration as well."

All the same, Eichengreen (the Professor of Economics and Political Science at the University of California, Berkeley) told AFR Weekend that Chinese growth will not reach Beijing's 7.5 per cent forecast this year.

"They won't hit their 7.5 per cent growth rate although they can always announce a 7.5 per cent growth rate whatever the underlying reality," he said. "But if growth were to slow to 7 per cent or something like that – that would not be a disaster."

Eichengreen's comments come as investors are becoming increasingly worried that the Chinese tiger could be running out of puff. This week the state-owned Bank of China reported its second-weakest profit growth since its initial public offering in 2006.

Standard & Poor's also sounded an alarm bell, warning in its quarterly Asia credit report that Chinese policymakers may be forced to rein in massive lending by the so-called shadow banking sector.

Signs of growing strains in the country's financial system were on clear display as hundreds of depositors raced to withdraw their cash from a small rural bank in eastern China, forcing local officials to take emergency measures.Recent fall welcomed

Investors are worried that financial strains in China could undermine economic activity, and that Australian mining companies will feel the fall out in lower commodity prices.

Eichengreen says Chinese policymakers will welcome the recent fall in the Chinese currency. The People's Bank of China – which keeps a tight grip on the currency – has allowed the yuan to fall since February.

"I think the authorities' intent in pushing the currency down initially was to introduce some two-way risk into the market primarily and to tell carry traders that there were no one-way bets,"he said. "Since then, there's been more evidence of the economy slowing down, and if a weaker currency boosts Chinese exports that will be a welcome side effect of the initiatives."

Eichengreen said that "one of the mysteries of Abenomics" (the radical policy to reflate Japan's economy named after Japanese prime minister Shinzo Abe) was that Japanese exports had not risen despite the sharp decline in the value of the Japanese yen.

He said he was "a little bit worried" about the rise in the Japanese consumption tax which next month will rise from 5 per cent to 8 per cent, but said he supported the move because "it's an important statement about commitment to debt sustainability".

In addition, he said: "I think in principle they can offset the impact of the consumption tax hike – the Bank of Japan can do more." Last April the Japanese central bank unveiled plans to **purchase** 7.5 trillion yen ($79.6 **billion**) of **bonds** a month and to double the country's monetary base in two years.No disruption to markets

Eichengreen appeared optimistic that the US central bank could **wind** up its massive bond-buying program – known as quantitative easing or QE – without disrupting markets.

He said the Fed's plan was "to give markets plenty of time to prepare and signal a strategy to proceed with $US10 **billion** of tapering a month which is a very small number, no reason why that should roil anyone.

"It's really a drop in the bucket when you look at the size of US Treasury bond markets or the Fed's balance sheet." The US central bank "will be telegraphing as clearly as it can that interest rates will begin to rise, presumably some time in 2015, presumably in the second half of the year."

He added that "we know that markets get roiled when they're surprised and the whole strategy here is not to surprise. Markets were roiled in May and June of 2013, because they were surprised – the Fed is trying to avoid another episode like that one".

He said that "lots of stars are aligning" for the US economy.

"I see developments in the US as pretty positive because there won't be much additional fiscal drag this year, because consumer confidence is strong . . . because the housing market has had a bit of a lull in the bad weather but has been picking up otherwise, because capital spending has been weak, and if consumers are spending capital spending will have to catch up."

What's more, he said, "I think [new US central bank chair] Janet Yellen is committed to growth and lower unemployment so that makes me think that things look good in the US, and it's only bad news coming from **China** which you in Australia think about, or bad news coming from Russia . . . which could throw things off course.'

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