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China's growth recovery

The novel coronavirus (COVID-19) is set to alter the pattern of economic growth over the coming two years, possibly for the better.

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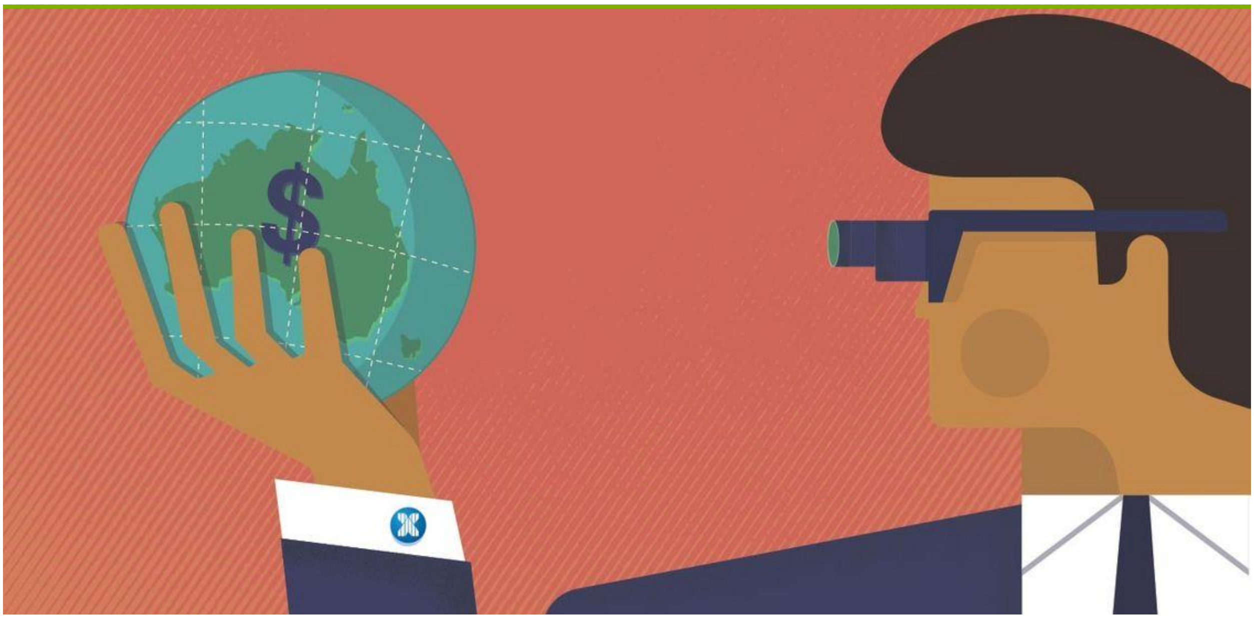

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The mining industry entered 2020 with a hint of optimism from forecasts that global growth could strengthen in the new year. The investment fortunes of the industry are heavily geared to the momentum of global growth. Metal intensive expansions of production capacity are most likely to occur in response to a surge in growth. This is when unforeseen metal shortages are most likely.

Amidst accelerating growth, investment strategists are more likely to revise up their growth forecasts contributing to more favourable investment sentiment and an improving flow of funds to the sector.

China's growth had been expected to slow slightly in 2020 irrespective of the COVID-19 outbreak, and possibly for several years after, driven by structural changes. Entering 2020, China's official quarterly growth rate was most likely around 1.4% after reported growth in the four quarters of 2019 fell within 1.4-1.6. A 2020 growth outcome around 5.8% was on the cards.

COVID-19 is having an immediate effect. Consumer spending has stalled as shops have put up the shutters in China, high spending tourists have been reluctant to travel, disrupted supply chains are threatening manufacturing output and leading to product shortages on shelves outside China as global business conferences to promote investment are being cancelled. From local market stallholders in Wuhan to high profile global companies like Apple, Disney and Starbucks, revenues are lower.

Now, something closer to 4% growth is looming for 2020 in China even if normal business conditions can be restored sufficiently quickly for output in the second quarter to match the level at the end of 2019.

Mining has been among the more vulnerable industries to the COVID-19 outbreak though, to date, the equity market response has been muted. The EMIX global mining index has fallen 6.3% over the four weeks since 20 January. The BHP and Rio Tinto dominated S&P/ASX 100 resources share price index has lost 7.9%. The stocks in the financially less robust ASX small resources share price index have lost just 4.8%.

> **COVID-19 could prove an opinion-shaping test for central government authority**

For the vast bulk of stocks in the sector, the COVID-19 outbreak has added another weight to all those already anchoring share prices near historically low levels.

With China's global economic links having been growing by the day, hardly any part of the world is sufficiently isolated to avoid an impact.

The most advanced economies are at least risk of an adverse economic impact because of their superior healthcare management systems, economic resources and political resilience.

The countries most at risk are those with inadequate health monitoring regimes or healthcare systems ill-equipped to cope with a virus outbreak. Pakistan, Myanmar, Bangladesh and Laos, in Asia, and Angola and South Africa are examples of where these risks might be greatest.

Countries vulnerable to external account shocks or already dealing with domestic political unrest, irrespective of economic links with China, are also at risk. Peru, Brazil, South Africa and Indonesia might be examples in this category. Their predicaments would be aggravated by fiscal constraints limiting the speed and efficiency of any response to a virus outbreak within their borders.

So far, financial markets appear to have shrugged off the consequences of COVID-19 hitting these more vulnerable economies. Markets appear content to assume that the worst will be over within two or three months.

Helping the ‘no worries' narrative is the uniquely authoritarian nature of the Chinese government response. It has been able to lock down metropolitan centres, intimidate large numbers of people into staying put and, possibly, conceal the full extent of the transmission and death toll.

At the same time, China's government is taking steps to meet the threat to its economic goals arising from the virus.

A week ago, the finance ministry reported having already allocated 71.85 billion yuan (US$10.3 billion) to prevent and control the epidemic. China's central bank is reported to have set aside 300 billion yuan to help fund companies supplying goods and services with a direct link to controlling the epidemic.

Local governments are being encouraged to waive taxes and pressure is being applied to financial institutions to lower interest rates for small and medium sized enterprises.

The central bank has indicated that it might cut other lending rates and reconsider rules to curtail financial risks due for implementation in 2020. Policymakers have continued to inject funds over the past few weeks to ensure ample systemic liquidity. China's finance ministry has announced early release of special purpose bond quotas designed to fund public infrastructure projects.

If the worst of the epidemic is near at hand enabling business to resume normal trading during April and May, economic growth could accelerate rapidly through the second half of 2020.

The strength of recovery will partly depend on how much household income has been lost permanently. Forced savings during the period of confinement will eventually be spent, even if not on what would have been bought if normal conditions had prevailed.

At the same time, the improved trade flows between the US and China written into the recently signed trade agreement between the two countries will be having a positive effect on growth in both countries.

Without having to make very heroic assumptions about the nature of the stimulus on offer, the Chinese government could report growth over the year of 7-8% for early 2021 and, with that momentum, something in excess of 7% for 2021 as a whole, even as the economy reverts to a more sustainable path in the aftermath of the COVID-19 epidemic.

Something even better might be achievable if the Chinese government takes more determined efforts to boost activity in the knowledge that COVID-19 could prove an opinion-shaping test for central government authority among a disillusioned and potentially fearful populace.

Although unsustainable, China's growth a year ahead could be outstripping expectations by enough to underpin a revival of sentiment about the global economy.

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