Comments to C.H. Kwan's paper

The Business Cycle in China since the Lehman Crisis

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The argument

- China’s real interest rate is inversely correlated with the inflation rate
- This shows that the interest rate policy has not played its expected role as an instrument to stabilise China’s economy

Background

- Two policy objectives for China's policy makers:
  - economic growth (and employment)
  - inflation
- These influence key prices (policy interest rate, the exchange rate and stock prices)

What the paper shows

- The inflation rate tends to follow the growth rate with an average time lag of three quarters
- The business cycle has four phases (instead of two)
- The Chinese policy makers failed to stabilise the economy at the time of the Lehman crisis because they used the wrong measures

Or, should the argument be reversed?

- The Chinese authorities implemented inappropriate measures at the time of the Lehman crisis
- As a result the business cycle presented four phases because GDP growth and inflation moved in divergent directions (because of time-lagged inflation)
- Therefore it has become more difficult for the Chinese authorities to manage and stabilise the economy

Is there a lesson from China's policy-makers?

- Need to calibrate economic policies especially in view of the long-term structural changes:

  shifting the model of economic growth

  demographics

  less pressures on the labour market (unemployment)

- Also, understanding inflation in China is complicated (the shift to the market economy is still work in progress)

Definitions (for better understanding)

- Recession or stagnation? Recession ‘Chinese style’?
- Output gap: better than average growth rate?
- Figure 6
- Is it a managed floating exchange rate regime?
- GDP gap or output gap?
- Robust enough results by using the GDP growth rate instead of the potential GDP growth rate?

Thank you

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