Amidst COVID-19, what's next for China’s private sector?
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As a result of the coronavirus outbreak in many countries, China’s economic growth has been seriously hit, particularly after the countrywide lockdown that took place at the end of January and during February. The unprecedented damage caused by the pandemic has presented the global and Chinese economy with several challenges. So, how is China’s private sector weathering this storm, particularly since the majority of these companies are small and medium-sized enterprises? What challenges does the private sector face? Are there any opportunities in the post-pandemic period?

The private sector plays a critical role in China’s economy contributing to more than 60% of GDP

Mr. Lifeng He, head of the National Development and Reform Commission (NDRC) used five digits “56789” to describe the importance of China’s private sector during the “Two Sessions” in the spring of 2019. So what do these numbers mean?

- 5: More than 50% of China’s tax revenue comes from the private sector.
- 6: More than 60% of China’s GDP is produced by the private sector.
- 7: More than 70% of China’s technological innovations are generated by the private sector.
- 8: More than 80% of China’s urban employment is created by the private sector.
- 9: More than 90% of China’s enterprises are private.

Additionally, private investment has continued to be the most significant part of total fixed asset investment over the past ten years. Investment, together with consumption and exports have been the three most important pillars of China’s economic development over the past few decades.

More specifically, in 2019, private investment accounted for 56.4% of total fixed asset investment, increasing by only 5% year-on-year. Comparatively in the years prior, private investment accounted for much more of total fixed asset investment than in 2019. For example, private investment accounted for 62% of total investment in 2018 and 64% in 2015 and 2014. Private investment growth remained at 9% in 2018, 10% and 18% in 2015 and 2014 respectively, and nearly 25% in 2012.

The reasons why the speed of growth and proportion of private investment to total fixed asset investment have declined in the last few years are complicated. One reason is a gradual slowdown in China’s total GDP growth. Another might be the sluggish speed of reform. Experts have argued that the aggressive expansion of state owned investment in the last few years has squeezed out private investment in some sectors.
Furthermore, private companies became China’s largest contributor to international trade in 2019. Last year marked the first time that exports and imports generated by private enterprises accounted for more than 40% of China’s total trade. This is a very good example of how Chinese private companies have achieved global competitiveness. Comparatively, in the past, exports and imports from foreign-owned enterprises often accounted for the major proportion of China’s total trade.

Last year, trade from private enterprises went up by 11.4% and accounted 42.7% of total trade, though total imports and exports increased by only 3.4% year-on-year. On the other hand, trade from foreign-owned enterprises and state-owned enterprises accounted for 39.9% and 16.9% respectively.

The private sector provides more than 80% of China’s urban jobs

Together with self-employed businesses, more than 80% of China’s urban employment is created by the private sector. According to the China Statistical Yearbook published by the National Bureau of Statistics, there were nearly 900 million people of working-age population (aged 16 to 59 years) in China by the end of 2018, out of which roughly 770 million were employed.

By the size of business, micro, small and medium-sized enterprises (MSMEs) provided 233 million jobs which accounted for 79.4% of total employees of corporate legal entities. In addition, 84% of total MSMEs are privately owned. This proportion of employment does not include self-employed businesses, large-sized private enterprises and other types of jobs.

Comparatively, only 15.7% of total employees of corporate legal entities worked for state-owned enterprises.

Out of the 21.79 million corporate legal entities in China in 2018, 84% were private. Indeed, the number of privately owned MSMEs recorded was 15.27 million, which accounted for around 84% of total MSMEs (which in turn was 18.07 million). The number of private MSMEs has increased by 9.54 million or 166.9% since 2013, thanks to the improvement in the business environment in recent years.

The National Bureau of Statistics has not released private sector employment statistics according to specific segments. However, out of all the employment categories, the top three industries by number of jobs in 2018 were manufacturing, construction, and wholesale and retail.
There were 149 million people working in self-employed businesses in 2018. Many self-employed business jobs are created in urban areas, while some are included in rural employment. The top three sectors for self-employed businesses according to the number of jobs were wholesale and retail (64 million jobs and 43.2% of the total), hotels and catering services (22 million and 15.0% of the total), and industry including manufacturing (16 million jobs and 11.0% of the total).

In addition to comprising 80% of total corporate employment, the total assets from MSMEs reached 402 trillion yuan by the end of 2018, and accounted for 77.1% all corporate assets. Business revenues from MSMEs in 2018 totaled 188 trillion yuan and accounted for 68.2% of all corporate revenues.

However, according to the World Trade Organization (WTO), although MSMEs engage the majority of the workforce in most countries, their contribution to national GDP is often lower. In general, it is about 35% in developing countries and approximately 50% in developed countries. Although China is still a developing country, the contribution of MSMEs to GDP is much higher. It would be around 60% based upon the above facts and analysis. This demonstrates the significance of MSMEs, and the private sector overall, for China’s economic development.
China can speed up financial reform to improve financing for the private sector

By the end of 2018, the private sector had significantly penetrated most segments of the economy except for a few essential industries. According to the China Statistical Yearbook published by the National Bureau of Statistics, the industries, including those in the Industrial Classification for National Economic Activities, with greater than 50% employment in the private sector were determined. These included the following:

- Wholesale and retail (69%)
- Industry including manufacturing (52%)
- Renting and leasing activities and business services (64%)
- Construction (56%)
- Scientific research and technical services (60%; note that this is not an industry included in the Industrial Classification for National Economic Activities)
- Information transmission, software and IT services (50%)
- Community services, repairs and other services (77%)
- Hospitality (including hotels and catering services) (57%)

Moreover, 38% of the employment in the transportation, storage, and postal industry is in the private sector, aside from rail transport which is nearly 100% state owned and civic aviation which is also dominated by SOEs. Amongst all the industries in the Industrial Classification for National Economic Activities, the China Statistical Yearbook did not release data on private employment for the financial services and real estate industries. Since many of China’s leading property developers are private companies, real estate is considered a comparatively competitive market with both SOE and private sector players. At the same time, SOEs often enjoy easier access to cheap financing as well as better government relationships as compared to private developers.
Figure 19: Number of employees in transportation, storage and postal sector in 2018

Unit: Million

- Road transport
- Intermodality and forwarding agency
- Loading, unloading and storage
- Post
- Water transport
- Air transport
- Rail transport
- Pipeline transport

Source: The Fourth National Economic Census Bulletin

Figure 20: Number of registered business entities in transportation, storage and postal sector in 2018

Unit: Million

- Private enterprises
- Limited liability corporations
- Shareholding corporations
- State-owned enterprises
- Collective-owned enterprises
- Other enterprises
- Enterprises invested by HK, Macao and Taiwan
- Foreign-invested enterprises
- Joint-equity and JV enterprises

Source: The Fourth National Economic Census Bulletin
Financial services accounted for more than one-third of all corporate assets or 35% of the total in 2018. However, in terms of total employment, financial services ranked seventh out of 18 industries, generating 18.32 million jobs.

According to Mr. Shuqing Guo, chairman of the China Banking and Insurance Regulatory Commission (CBIRC), as at the end of 2018, although the private sector contributed more than 60% of China’s GDP, private enterprises only accounted for 25% of China’s total bank lending. Additionally, at that time, around 70% of total aggregate financing to the real economy was in the form of bank loans.

If China aims to maintain sustainable growth in the long term, China must alter the disparity and inequality in financing between private and state-owned enterprises.

Therefore, the reform and opening up of financial services sector is expected to speed up in 2020, further accelerated by the downward economic pressure triggered by COVID-19. China has scheduled timelines to open up foreign investment in banking, insurance, securities, fund management and other financial services within the year. As a result, the private sector should also be able to tap into these segments soon.
What are other challenges and opportunities for the private sector amidst COVID-19?

Fortunately during this COVID-19 outbreak, the Chinese government at both the central and local levels have realised that the private sector, particularly MSMEs, are the most vulnerable group. Therefore, many countermeasures have been implemented to help MSMEs, particularly by reducing taxes, fees and financing costs, as well as waiving rents if the landlords are government entities and SOEs. Banks are also encouraged to provide liquidity and cheaper loans to MSMEs.

Many small and medium private companies involved in international trade might struggle to survive during this period, since the cash flow cycle is much longer and orders are not being fulfilled. According to the IMF, global economic growth will drop to -3% in 2020. For China, this means both exports and imports will face challenges in terms of their growth potential, due to shrinking demand.

Furthermore, private companies in the hospitality sector (including hotels and catering services) have also been hurt badly, particularly over the lockdown period from the end of January and during February. Educational institutions and cinemas have also been shut down since the outbreak began, and both segments have probably faced the longest closure period as compared to other industry sectors.
How to better support these types of private enterprises, particularly MSMEs during tough times, is a complex decision that involves many stakeholders including different government departments.

Therefore, perhaps it is time to set up a ministerial-level organisation within the Chinese government to support and promote MSMEs, given their significant contribution to the national economy. The State-owned Assets Supervision and Administration Commission of the State Council (SASAC) is a ministerial-level organisation that was established in 2003. Accounting for the national employment created by MSMEs as well as their contribution to GDP, today’s MSMEs are far more important than the large SOEs supervised and managed by the SASAC. Setting up a ministerial-level organisation would definitely boost the development of MSMEs, as well as the national economy, by consolidating and coordinating resources.

Moreover, unleashing private investment in sectors dominated or controlled by SOEs (including financial services, energy, petroleum and petrochemicals, telecoms, railways, civic aviation, etc.) is a much more effective way to stimulate investment, as well as to improve competition and boost economic efficiency. During the economic downturn, these types of reforms are more likely to be implemented in order to stabilise growth.

Lastly, most of China’s private companies are small and vulnerable, except for a few that have emerged to become Fortune 500 companies, or have grown to rank within the top 500 private companies in China. Remaining in business during tough times, like the pandemic we are experiencing now, is a matter of life or death for some MSMEs.

At the same time, compared to policy countermeasures adopted by the US and EU, the Chinese government still has sufficient fiscal and monetary policy tools and financial resources to boost GDP growth up from the negative figure posted in the first quarter of this year. Once China’s economy returns to its steady growth trend, the private sector, particularly MSMEs, will gradually recover from the disruption caused by COVID-19.

Thus, it is very necessary that China gives priority to six areas of job security, basic living needs, operations of market entities, food and energy security, stable industrial and supply chains in 2020.
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