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ECONOMICS: ASIAN PERSPECTIVES

CHINA: JOBS IN FOCUS AS ECONOMY SLOWS

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Despite a marked slowdown in China's industrial output and fixed-asset investment—previously the main drivers of growth—there is no sign of panic among policymakers, and the stock market is rallying. Some observers worry about an eventual doomsday, but we believe that the economy and social stability will be underpinned by a sturdy jobs market, provided that the services sector continues to expand.

New Normal

Recent data suggest that the Chinese economy is now solidly entrenched in the new normal slower-growth era. Key growth engines such as industrial production and fixed-asset investment have slowed to decade-low paces, while retail sales and housing investment have decelerated to their lowest growth levels since the global financial crisis.

Only a few years ago, a slowdown of such a magnitude would have been unthinkable and would have been deemed a hard landing. Somehow, Chinese policymakers have managed market expectations quite deftly. In fact, the Chinese equity market has been rallying sharply since mid-2014. The People's Bank of China (PBC) is in no panic with its monetary easing, and the government is not giving up on its structural reform agenda either, despite the headwinds that the reform process has caused for the current growth cycle.

Jobs Matter

Panic will set in only if the job market starts to creak, in our view. Social instability fueled by a disgruntled, jobless population would be a major threat to China's one-party rule. So far, however, employment looks fairly stable, based on published official data and anecdotal evidence. At least, no abrupt, mass layoffs like the ones seen in the aftermath of the 2008–2009 global financial crisis have been observed.

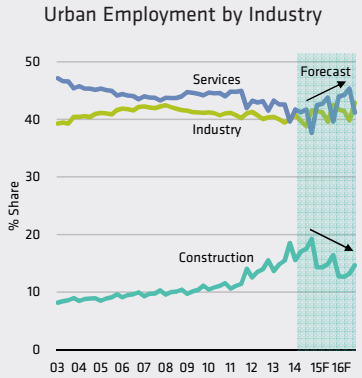
Efforts by state-owned enterprises to maintain head counts by reducing work hours and paying just basic wages may have played a role in keeping things calm. But we think that has not been a dominant phenomenon.

Services Will Be Crucial

Economic rebalancing toward services—a central tenet of China's ongoing economic reform—has been key to minimizing the risk of an employment crisis as job growth in this labor-intensive sector has helped to absorb losses in other industries. This will be even more crucial in the future, especially as more construction jobs are lost as the housing sector undergoes a more prolonged consolidation. Further pressure may come from manufacturing, as Chinese factories move up the value chain, swapping manual labor with robots.

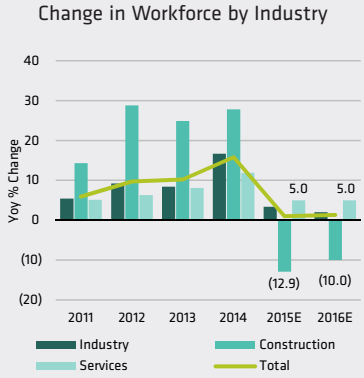
According to official data, China's urban areas created 3.24 million new jobs in the

Display 1
Services Key to Offsetting Construction Job Losses



As of May 20, 2015
Source: CEIC Data and AB

Display 2
Services to Take Up Employment Slack



As of May 2015
Source: CEIC Data and AB

first quarter of 2015, down 200,000 jobs from 3.44 million a year ago. Now, we have to note that this data series is very volatile and—importantly—new jobs are still being created. But a more structural, and potentially explosive, problem is the job mismatch for the young well-educated workers. A recent survey showed that 58% of college graduates (totaling 7.5 million this year) were finding it hard to get a job.

The solution, both for the near term and the long run, will have to be a continued expansion of the services sector. The experience in the more developed economies, such as Japan, South Korea and Taiwan, suggests that as a nation moves up the income ladder the services industry expands to replace agriculture, manufacturing and construction as the main driver of economic growth and employment. In each country, the net outcome of this transformation has been the creation of enough new jobs to achieve full or near-full employment during the development process.

Scenario Analysis

Thanks to rapid industrialization and urbanization, the industrial and construction sectors in China have a higher share of total employment (38% and 18%, respectively) relative to other countries in similar stages of economic development. So there is concern that a prolonged downturn in the housing market, resulting in job losses in that sector, will make it impossible for China to keep the jobless rate stable, particularly given the backdrop of the new normal growth environment.

A simple scenario analysis shows, however, that this worry is overdone—so long as jobs in the services sector, which currently accounts for 41% of total employment, continue to grow steadily. In our analysis, a a modest 5% annual growth in services jobs should be able to absorb the slack resulting from job cuts in other sectors—even if the reductions in construction reached some 10%–13% annually (compared with 25%–30% annual growth over the past three years) and jobs in industrial are stagnant (*Displays 1 and 2, previous page*). ■