



Australia's exposure to a Chinese economic hard landing: New findings

Last year the Australia-China Relations Institute (ACRI) reported on modelling by Deloitte that found an economic hard landing in China would send the Australian economy into recession.¹ New research points to a more sanguine outcome.

Inoue, et al. (2018) modelled the impact of a one percentage point drop in Chinese GDP growth.²

1. Australia's GDP growth rate falls by 0.06 percentage points in the short run, moderating to 0.045 percentage points in the medium and long term. Australia's trend rate of GDP growth is around 3 percent, suggesting that even if the Chinese shock were larger, the impact would be material but manageable.

2. The impact on Australia would be of a similar order of magnitude to other high income countries in the region, such as the US, EU, Japan and Korea.

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Karam and Muir (2018) modelled the impact of a four percent reduction of Chinese GDP in the short run and a 10 percent reduction in the long run.³

3. Australia's GDP fell by 0.4 percent in the short run. Similar to Inoue, et al (2018) this is material but does not make a recession inevitable.

4. In the medium term Australia's flexible exchange rate would mitigate the negative short run impact. In the medium and long term, Australia's GDP would rise by 0.4 percent, boosted by exports stemming from a lower exchange rate.

5. Australia's consumption would be two percent lower in the short and long run as the cost of imported goods increase, meaning Australians may feel worse off even if output and jobs remain relatively stable.

Groenewold (2018) modelled the impact of a permanent fall in China's growth from 10 percent to seven percent.

6. Australia's growth would fall by about 0.2 percentage points in the short run and 0.5 percentage points in the long run.⁴ Once again, this suggests the impact would be material but manageable.

1 James Laurenceson, 'Australia's exposure to a Chinese economic hard landing', Australia-China Relations Institute fact sheet, August 30 2017 <<http://www.australiachinarelations.org/content/australias-exposure-chinese-economic-hard-landing>>.

2 Inoue, T., Kaya, D., Ohshige, H. 2018. 'Estimating the Impact of Slower People's Republic of China Growth on the Asia and the Pacific region: a Global Vector Autoregression Model Approach', in J.Lin, P. Morgan, G. Wan (eds), *Slowdown in the People's Republic of China: Structural Factors and Implications for Asia*, Asia Development Bank, Manila, 357-373.

3 Karam, P., Muir, D. 'Australia's Linkages with China: Prospects and ramifications of China's economic transition', IMF Working Paper WP/18/119. May 2018 <<https://www.imf.org/en/Publications/WP/Issues/2018/05/22/Australia-s-Linkages-with-China-Prospects-and-Ramifications-of-China-s-Economic-Transition-45846>>.

4 Groenewald, N. 'China's "New Normal": how will China's growth slowdown affect Australia's growth?' *Australian Economic Papers*, 2018 <<https://doi.org/10.1111/1467-8454.12121>>.

A Chinese economic hard landing is not a consensus forecast but is plausible.

7. The Australian Treasury expects China to average GDP growth of 6.25 percent during 2018-2020. This compares with 4.25 percent for Australia's trading partners as a whole.⁵

8. The World Bank sees China growing at an average annual rate of 6.3 percent out to 2020, against an advanced economy average of 2.0 percent.⁶

9. The International Monetary Fund expects Chinese growth to average 6.5 percent in 2018-19, compared with 2.1 percent for advanced economies, and Chinese growth being maintained at 5.5 percent in 2023.⁷

5 Australian Treasury, 'Statement 2: Economic outlook', May 8 2018 <https://www.budget.gov.au/2018-19/content/bp1/download/bp1_bs2.pdf>.

6 World Bank, 'Global economic prospects: turning of the tide?', June 2018, <<http://www.worldbank.org/en/publication/global-economic-prospects>>.

7 International Monetary Fund, 'World economic outlook: Cyclical upswing, structural change', April 2018 <<http://www.imf.org/en/Publications/WEO/Issues/2018/03/20/world-economic-outlook-april-2018>>.