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China Turns On the Charm, but Economist Stephen Roach Isn't Buying It

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The China Development Forum in Beijing in March drew CEOs of U.S. companies.
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Following his first visit to Beijing in 3½ years, Stephen Roach, the economist and former chairman of Morgan Stanley Asia, is sounding the alarm on what he considers a dangerous path for U.S.-China relations.

And after attending the China Development Forum, a confab in Beijing last month that drew global corporate chiefs, including Apple 's Tim Cook and Pfizer 's Albert Bourla, he's becoming more somber on China's economic prospects.

The message from China's leadership: China is back—the private sector is important and foreign multinationals are welcome. The tightly scripted message, Roach says, was aimed at reassuring investors and companies rattled by the crackdown on the technology and property sectors in the past couple of years, as well as China's stringent Covid policies and worsening U.S.-China relations.

"They were trying very hard to get this message across—conceivably trying too hard," Roach says, noting that there were fewer top U.S. executives at the forum than in the past.

Alibaba Group Holding 's (ticker: BABA) recent decision to split up, opening the door to public offerings for some of its businesses, and the reappearance of co-founder Jack Ma, who had faded from public view after falling afoul of China's regulators a couple of years ago, were intended to suggest the crackdown on the private sector is over.

But Roach, a senior fellow at the Paul Tsai China Center of the Yale Law School and author of *Accidental Conflict: America, China, and the Clash of False Narratives,* isn't convinced. He noted the clampdown on fan culture and certain online music and videos, as well as the still-hobbled private after-school tutoring industry, after Beijing upended their business models.

"They insist technology companies are welcome to re-engage, provided they do it in tight alignment of the standards and requirements of the Chinese Communist Party, so it isn't an open-ended restarting of a dynamic private sector by any stretch of the imagination," Roach says.

A restrained private sector doesn't bode well for economic growth, nor do the relatively subdued levels of consumer confidence. While Roach expects growth this year to improve as China's economy recovers from its zero-Covid policy, he sees increased uncertainty about what lies beyond the recovery-oriented growth—a view shared by others he met on his trip.

Part of the concern is the decline in China's working-age population and its baby bust. Despite incentives to get couples to have children, birthrates aren't rising. One reason: the dearth of safety nets available to the Chinese in terms of healthcare and retirement benefits as the population ages rapidly.

"That's a key reason why the income that is generated by the growing service sector and the rural-urban migration is being saved, not spent," Roach says.

With the population not growing as fast, the economy needs improved productivity. But here, too, China is challenged, especially as the economy is driven more by low-productivity state-owned enterprises under President Xi Jinping and high-productivity sectors like technology are hobbled by regulation, Roach says.

An aging population and a weak productivity outlook mean China is beginning to look like Japan, Roach says. That's a problem for China's leadership, whose power rests on sustaining economic growth to deliver on its political contract with the Chinese people.

It's also problematic for the outlook for the world economy, since China has contributed roughly a third of global growth. Slower Chinese growth fed into the

International Monetary Fund's latest global outlook for 3% annual growth in five years, the lowest level in decades.

Roach's other takeaway on China: There is a growing resignation that the U.S.-China relationship is beyond repair. "They have given up on hope of resolving the conflict and are prepared to move on," Roach says of the people he met.

Roach has encouraged Chinese and U.S. leaders and others on the need to get the relationship back on track and rebuild trust, including through bilateral areas where both countries could benefit from growth or even a U.S.-China Secretariat position that could create a pathway for engagement.

The political climate in both countries makes such an endeavor difficult, he says. "There's nobody in Washington right now who wants to speak in favor of re-engagement. It's a bad word," Roach says. "The conflict is now in a danger zone. As both sides harden their approach to conflict, the tensions to me feel like high-octane fuel that could easily be ignited by a spark. We are trading off national security for economic security."

It's a trade-off others are worried about as well. In a J.P. Morgan survey of investors at last week's IMF and World Bank annual spring meetings, geopolitical tensions ranked first on the list of concerns about China, followed by a further shift in the centralization of CCP authority under Xi.

Investors are still wrestling with what that means for their portfolios. For now, it's clear it could bring more volatility.

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