FOREIGN EXPERIENCE

Activating Consumer Demand as a Key to Successful Development of the PRC Economy

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Abstract—In the 14th five-year plan of the PRC (2021–2025), consumer demand is considered as the basis for future economic development and GDP per capita growth. Stimulating consumption within the PRC is one of the tasks of the government for 2021. This article analyzes the factors affecting the expansion of consumer demand, and also analyzes the economic indicators associated with the selected issue. The article also draws conclusions about the impact of the United States-China trade war and the COVID-19 pandemic on changing consumption patterns in the PRC.

Keywords: economy, PRC, 14th five-year plan, consumer demand, COVID-19, consumption

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In 2020, the PRC completed the implementation of the 13th five-year plan (2016–2020), and at the beginning of 2021, the 14th five-year plan (2021–2025) was adopted. Both plans contain ambitious targets to bolster domestic demand in the country and replace a predominantly export-driven growth model with a predominantly domestic consumption-driven one. To this end, in May 2020, the president of the People's Republic of China Xi Jinping for the first time voiced the concept of the development of the Chinese economy as “double circulation” (双循环) [1], according to which China should rely on a sustainable cycle of domestic demand and innovation as the main engine of the economy, while maintaining foreign markets and investment as the second engine of growth. Xi stressed that in modern conditions “it is necessary to deepen structural reforms in the supply sector, to fully use the country's super-scale market advantages and the potential of domestic demand.”

The relevance of the topic of the article is due to the fact that in the case of the successful implementation of the plans of the Chinese leadership, the structure of the PRC's economy may radically change, and given its scale, it will have a serious impact on the world economy.

However, the problem of changing consumer demand in China, given the new factors (the US–China trade war, the coronavirus pandemic), has been little studied. The purpose of this article is to investigate the process of changing the influence of consumer demand on the economy of the PRC and identify the impact of the United States–China trade war and COVID-19 on this process.

The idea of using the world's largest domestic market as a driver of economic development did not belong to Xi Jinping. Back in 2008, the premier of the PRC State Council, Wen Jiabao, stated that “in order to achieve sustainable development, China needs to increase domestic consumption.” However, the efforts made by the government to stimulate demand have not been effective enough: the share of final consumption in China's GDP remains relatively low, only 1 pp higher in 2019 (55.65%) than in 2005 (54.3%) (Fig. 1).¹ For comparison: in the United States, this figure in 2019 was 81.8%, in India 72.3%, and in Russia 68.7%.

The level of income of the population of the PRC. The stagnation in spending by Chinese consumers has intensified since the onset of the coronavirus pandemic. The main reason for this phenomenon is the fall in incomes of the population. According to researchers from the University of British Columbia and Boston College, 47.5% of the Chinese population faced partial loss of income [2]. However, oddly enough, McKinsey & Company in its report on consumer demand in the PRC indicates that 54% of respondents are extremely optimistic about the recovery of the PRC economy after the pandemic (in the United States this figure was 22%, and in Japan –22%,

¹ The PRC CSO understands final consumption expenditures as the total expenses of residents of the country for the purchase of goods and services both in the domestic economic territory and abroad to meet the needs of material, cultural and spiritual life. Final consumption expenditures are subdivided into household consumption expenditures and government consumption expenditures.

Fig. 1. Final consumption expenditure in the PRC: —◆— final consumption costs; —▲— GDP growth.

According to the State Investigation Directorate of the People's Republic of China: <http://www.stats.gov.cn/tjsj/ndsj/>.

this means that the Japanese are extremely pessimistic about the possibility of a quick economic recovery), and 60% of respondents believe that it will take only 2–3 months to recover the affected industries [3].

At the same time, according to the official data of the National Bureau of Statistics of the PRC, in 2020, the average disposable income per capita in China reached 32 189 yuan, which is 4.7% more in nominal terms than in the previous year, and real growth was 2.1% after excluding price factors (Table 1).

The average disposable income of urban residents per capita was 43 834 yuan, an increase of 3.5% (1.2% after excluding price factors). Per capita income for rural residents was 17 131 yuan, an increase of 6.9% (3.8% after deducting price factors). This contradiction can be explained by the fact that in 2020 there was an increase in the propensity of the population to save, which for the Chinese economy is not a positive trend in the policy of stimulating demand.

The relationship between consumer demand and the economic development of the PRC. To study the current state of the problem of consumer demand in the PRC, it is necessary to consider the genesis of this issue. Since the beginning of Deng Xiaoping's policy of "reforms and opening," the PRC has followed the path of attracting foreign investment for the develop-

ment of its own economy. This strategy ensured high rates of GDP per capita growth. However, by 2008, the Chinese government realized that it was necessary to accentuate the development of domestic demand in order to continue the trend of rapid GDP growth.

First, China could no longer rely solely on exports and financial flows from outside, since the global economic environment became extremely unstable and volatile, which was demonstrated, for example, by the global financial crisis of 2008 (yes, the Chinese economy as a result of the state support program suffered little from it, however, exports decreased by more than 20%).

Secondly, state investments in fixed assets, primarily in the framework of the implementation of large infrastructure projects, have made a significant contribution to the economic growth of the PRC. At the same time, the effectiveness of these projects and, accordingly, their payback remain in question. For example, in China, hundreds of billions of dollars were invested in the construction of high-speed railways, although ticket prices were unaffordable for most Chinese, and many major cities did not have a metro.

Third, in China by 2005–2010, a significant difference in the economic development of cities and rural areas began to be observed, and the deepening economic imbalance between residents of cities and villages prevented an increase in the level of aggregate domestic demand in the country.

An important problem in the context of studying consumption in China is the high share of savings. Since the late 1970s, there has been a significant increase in this indicator. In the 1980s, following the introduction of the one-family-one-child policy and the decollectivization of agriculture in rural areas, the share of savings increased from 5% to 20% of disposable income. In the 1990s, after Deng Xiaoping's "southern trip" (邓小平南巡), during which the course to deepen the policy of "reform and opening

Table 1. Real disposable cash income per capita (yuan)

Year	National average	Urban area	Countryside
2015	21966.2	31 194.8	11 421.4
2016	23821.0	33 616.2	12 363.4
2017	25973.8	36 396.2	13 432.4
2018	28 228.0	39 250.8	14 617.0
2019	30 733.0	42 358.8	16 020.7
2020	32 189.0	43 834.0	17 131.0

Prepared according to the data of the State Statistical Office of the People's Republic of China: <http://www.stats.gov.cn/tjsj/ndsj/>.

Fig. 2. Household savings rate:

▨ China; ▤ European Union; ■ United States; ▩ Russian Federation.

According to the OECD: <https://data.oecd.org/hha/household-savings.htm>.

up” was confirmed, and the reform of state-owned enterprises, which was central to the political course, was accompanied by the transformation of the system of social guarantees and guarantees of providing jobs, there was a further increase in the share of savings to 25%.

After China joined the WTO in 2001, which led to an export boom, the share of savings increased to 30%. In 2018, this figure was 29.6% (Fig. 2).

Reforms that began in the late 1970s increased income uncertainty as many jobs were no longer paid from the state budget. Since the 1970s, there has been a trend towards shifting the burden of pension expenditures onto households; by retirement, it was necessary to generate additional savings in order to pay for services that were previously nearly free; in the early 2010s the financial market and banking system of the PRC were just beginning to reform, as a result it was difficult to obtain loans for housing, education, medical care and other large items of expenditure. For example, a mortgage required a minimum of 30% down payment, not taking into account the already high real estate prices in large cities [4].

Some researchers also point to a demographic reason (after the introduction of the one-family-one-child policy) for the growth of savings: on the one hand, fewer children require less parental spending (especially on education, which is actually paid in China), on the other hand, these are restrictions on the costs of the children themselves when they grow up, since they will actually have to support their elderly parents [5]. Even with the decline in GDP growth rates, the level of citizens’ savings continued to grow; the Chinese prefer to save in both good and bad economic conditions. In the analytical report of the Bank for International Settlements, according to data for 2010, two groups of reasons for the increase in the level of savings in Chinese society [6] are given: economic and demographic, as well as key institutional changes.

Realizing the need to expand domestic demand for the development of the economy and increase its resilience, the Chinese government has repeatedly stressed the importance of this task. For example, the 12th Five-Year Plan (2011–2015) set out the following goals: reduce social barriers that inhibit rural-to-urban travel, improve access to social and public services, and increase social insurance. Speaking at the opening of the 18th Congress of the Chinese Communist Party (CCP), Hu Jintao said that “China must firmly adhere to a strategic focus on stimulating domestic demand and unlocking the potential for individual consumption,” [7] and the Chinese economy must be more focused on demand. Also in 2012, Hu Jintao said that China is making efforts to create long-term economic tools to increase domestic demand [8]. In general, the measures taken by the government led to an increase in final consumption expenditures by 2015 by an insignificant five percentage points (Fig. 1).

The 13th Five-Year Plan also paid a lot of attention to consumption. The program stated that in order to meet and stimulate consumer demand, work should be done to improve the environment: improve it and offer innovative solutions. Interestingly, this five-year plan indicated a commitment to integrating online and offline consumption. The government also announced that it is actively working to encourage the population to buy domestic goods.

Consumer demand as a driver for the development of the modern economy of the PRC. The slowdown in China’s GDP growth and the trade war with the United States that began in 2018, according to researchers from McKinsey & Company, are not factors of a significant drop in demand in China [9]. To prove their position, the authors point out that despite the decline in the growth rate of retail sales in 2019, as well as the decline in the second half of 2018 in the consumer confidence index, at the beginning of 2019 this index reached a ten-year maximum (Fig. 3).

Fig. 3. Consumer Confidence Index in China: ---- growth rate of retail sales; — consumer confidence index (right scale). Prepared by the author based on the data of the State Investigative Committee of the People's Republic of China: <http://www.stats.gov.cn/tjsj/ndsjs/>.

At the end of 2019, analysts from the aforementioned company identified five trends in the development of consumer demand in China in 2020.

First trend—The engines of consumer demand growth in the near future will be the so-called young free spenders from the 2, 3, 4 line cities (large cities, including million-plus cities), since their consumption model is very different from the model of other Chinese. For example, on average, they work fewer hours per day than residents of metropolitan areas,² so they have more free time to shop. This group has money and confidence in the future, and in their opinion, expensive goods are better than cheap ones. At the same time, they are not particularly interested in saving money. This social group accounts for a quarter of the total population, but it accounts for almost 60% of the total increase in expenditures (in 2018 compared to 2017).

Second trend—The majority of Chinese consumers are becoming more discerning and cost effective: 60% of respondents said that they are not interested in reckless spending, even if they felt “richer” (in 2017 it was 52%). Analysts believe that the reason for this behavior lies in the slowdown in the growth of household income.

Third trend—An increase in spending on goods and services related to a healthy lifestyle.

Fourth trend—Increased travel expenses.

² Chinese city level system (Chinese: 中国城市等级制) Is a hierarchical classification of Chinese cities, usually cities with 1,2,3,4 lines are distinguished. There are no official lists of the distribution of cities, but this system is often mentioned in the media and statements by officials. Cities across lines reflect differences in consumer behavior, income levels, population, infrastructure, business opportunities, and other factors. The cities of the 1st line usually include Beijing, Shanghai, Guangzhou and Shenzhen.

Fifth trend—Increased attractiveness of high-quality Chinese brands. If earlier the Chinese preferred European goods to Chinese goods, believing that their quality is higher, then recently the trend has begun to change. Respondents stated that they clearly prefer Chinese brands over foreign ones in 13 out of 19 categories (toilet paper, household cleaning products, milk and fresh food, consumer electronics, beer and household appliances such as refrigerators).

Relationship between the development of the middle class and the development of the PRC's economy. An important factor influencing the expansion of consumer demand in China is the development of the middle class in the country. The size of the Chinese middle class has increased significantly compared to 2010 (Table 2).

However, it is important to note that the Chinese government measures poverty and middle class levels by Chinese standards, not global ones. According to the methodology of the State Statistical Office of the PRC (2019), the middle class includes citizens whose income ranges from 2000 to 5000 yuan per month. (approximately \$300–750), i.e., about 400 million people [10]. However, about 600 million people continue to live on 1000 yuan a month (about \$150). According to Xi Jinping, poverty in China has been overcome [11]. However, the problem now remains: how to “drag” the remaining 600 million Chinese, who, according to Li Keqiang, live on \$146, into the middle class.

Impact of the US–China Economic War and the COVID-19 pandemic on the development of the Chinese economy. In 2018, the president of the United States, Donald Trump, introduced the first duties on Chinese goods, followed by several “reciprocal exchanges” of duties by the United States and China. Based on bilateral trade volume in 2019, United States and retaliation

tory Chinese tariffs currently affect imports and exports of goods by more than \$460 billion. In January 2020, the first phase of the United States–China trade deal was signed and entered into force in February 2020. China has committed to 2020–2021 a total increase in purchases of American goods by about \$200 billion in relation to the level of 2017 in exchange for Washington’s refusal to carry out the latest round of tariff increases and a halving (to 7.5%) of the tariff on Chinese imports in the amount of \$112 billion [12].

By the end of 2020, the PRC fulfilled its obligations by 58% (about \$100 billion against the plan of \$173.1 billion). The question of the influence of American duties on the economic development of the PRC is extremely controversial. However, in the fourth quarter of 2020, the growth rate of the PRC’s GDP amounted to 6.5%, which indicates that the Chinese government has found alternative ways to increase the country’s GDP. According to the author, this is precisely the domestic demand, which is confirmed by some other experts [13].

The election of Joe Biden as United States president did not influence the “anti-Chinese” policy. United States Secretary of State Blinken in January 2021, during a meeting in the Senate, said that cooperation with China will proceed from a “position of strength.” Interestingly, under the Biden administration, there is a tendency not only towards economic confrontation with China, but also towards an ideological one: the secretary of state made it clear that Washington would try to destroy ideas about the attractiveness of the Chinese path of development and Chinese soft power as an alternative to the values of the Western world, led by the United States [14].

If the United States–China trade war could be predicted (Donald Trump talked about the need to “solve” the Chinese issue even during the election race), then COVID-19 has become a real challenge to the Chinese economy: both the economic situation and the type of consumption have changed. The pandemic has accelerated the long-standing trend of the digitalization of the Chinese economy and online consumption. For example, the share of e-commerce in retail sales in 2020 in China was 24.9% (in the US this figure is 14%, the Russian Federation about 10%, and Germany 19.9%) (Fig. 4). China leads in the field of not only Internet sales, but also mobile payments; according to 2019 data, in China, 35% of payments are made using mobile devices.

Experts from the eMarketer company cite much larger numbers: they believe that in 2020 the share of e-commerce in the PRC was 44.8%. They forecast that in 2021, more than 52% of the country’s retail sales will come from e-commerce, which means that for the first time in the world, most of the country’s retail sales will come from the Internet.

During the pandemic, according to research by the Kantar Group, the largest cost savings to Chinese

Table 2. Annual disposable income of households, RMB/mln people

Income, thousand yuan	2010, mln people	2018, mln people
Less than 49	79	72
49–79	134	89
79–138	403	257
138–197	34	311
197–297	10	63
297–390	3	10
More than 390	6	16

Prepared by the author according to the data of the State Investigative Committee of the PRC <http://www.stats.gov.cn/tjsj/nds/>.

consumers fell on three areas: eating out, entertainment and travel. However, the pace of cost recovery in these areas is also significant [15]. Some seemingly far from the pandemic industries have also suffered damage. For example, due to a decrease in the number of outdoor activities, 57% of consumers surveyed have canceled or reduced spending on alcohol. The same happened with cosmetics (a 56% cut in spending) and clothing (a 67% cut in spending).

At the same time, the pandemic increased spending in areas such as food and beverages (40% of respondents said they started spending more), house cleaning (48%), health insurance and life insurance (38%), the largest increase was noted in Hubei province, the center of which is the infamous Wuhan). At the same time, the pandemic forced people to try something new, as 84% of respondents tried at least one new service for the first time: the highest rates are for online medical consultations (34%) and online education (33%), followed by software for work from home (29%); and digital entertainment subscriptions (26%).

An important indicator of domestic demand in China is the Chinese New Year and the so-called fes-

Fig. 4. Percentage of online sales of total retail sales:

--- China; —▲— Germany; — Russian Federation; —◆— United States.

Prepared by the author based on data from the Statista portal: <https://www.statista.com/>.

tive “golden week.” According to the Ministry of Commerce of the People’s Republic of China, the largest retail stores and restaurants recorded revenue of 821 billion yuan (127.12 billion dollars) in the golden week, up 28.7% over the same period in 2020 and 4.9% higher than in 2019 [16]. Online food delivery sales are up 135% year-on-year, jewelry and apparel stores tracked by the Department of Commerce reported 160.8% and 107.1% spikes in golden week sales, and fitness equipment on Chinese e-commerce platforms also increased by 49% compared to 2020.

Chinese government plans to strengthen domestic demand. Consumption was given serious attention in the report on the government’s work plans for 2021, in the 14th five-year plan and the program of long-term development goals of the country until 2035. In the 14th chapter of the Plan (“Accelerating the creation of a full-fledged system of domestic demand”), the goal is to increase the level domestic consumption (green, healthy and safe) combined with an increase in the standard of living of the population. Another goal is the development of new types of consumption (informational, digital and green), as well as encouraging the development of new models and formats of consumption (production of unique goods to order, customization, the use of intelligent systems and the consumption of “fashionable” goods).

The development of service consumption and the acceleration of the integration of online and offline sales channels, including the active promotion of e-commerce in rural areas, are highlighted as separate goals. To achieve these goals, the Chinese government sets goals to increase the income of residents and reduce the economic burden. It is important that the government sets the task of expanding the middle class and freeing up the potential for consumption (what Chairman Hu once spoke about) [17].

In January 2021, the Ministry of Commerce announced that consumption remains a pillar of the stable development of the Chinese economy, accounting for 54.3% of its GDP. In 2020, China became the world’s largest online shopping market for the eighth consecutive year, with online sales growing 14.8% year over year. To further increase consumption, the Ministry will implement a number of measures, including accelerating online and offline integration, expanding rural consumption, and promoting store construction and renovation [18]. However, it is important to note that in January 2021, producer prices in China rose for the first time in a year, while core consumer prices fell for the first time in more than a decade, indicating an unbalanced economic recovery.

According to the latest report from the financial conglomerate Morgan Stanley, in the next decade, private consumption in China will more than double to \$12.7 trillion dollars by 2030, which will make it the locomotive of global consumption. The report notes that the key shift in China’s consumption patterns in

the next 10 years will be the consumption of services, which will exceed the consumption of goods, and by 2030 the share of services will reach 52%. According to Morgan Stanley’s calculations, Chinese consumer demand will shift from the current needs of young consumers for home and pension services, as people aged 35 to 44 and over 55 are expected to dominate the consumer mix [19].

In general, the Chinese market has a specific feature: Chinese consumers prefer local goods and brands to foreign ones (there are many reasons for this behavior, including the fact that the Chinese often mistake foreign brands for local ones [20].) As of 2017, the overwhelming majority of consumers preferred “foreign” brands in only three categories: wine, baby milk powder and cosmetics. McKinsey & Company believes that local Chinese brands are superior to foreign brands on three criteria: price, quality, and after-sales service. This feature has helped the Chinese government to successfully intensify domestic consumption of local goods and services.

Conclusions. The emphasis of the Chinese government in the 14th five-year plan on further expansion of domestic demand clearly shows that there will be no economic growth without domestic demand (the target for 2021 is GDP growth of more than 6%). The trade war and the COVID-19 pandemic have finally convinced the Chinese government that it is necessary to look for opportunities to increase GDP domestically, not abroad. However, while demand in cities is steadily increasing, China still has serious work to do to stimulate demand in rural areas.

Fulfillment of the tasks set by the Chinese government within the framework of the 14th five-year plan may lead to a significant change in the model of the PRC’s economy, and further to a change in the world economic system. If China can cope with the task of reorienting the Chinese economy to primarily consumption, then the consequences of a reduction in exports from China could be extremely serious. However, it is important to note that the PRC’s plans are extremely ambitious, and the possibility of their implementation is a debatable issue.

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