HE215/HE2015 – Macroeconomic Issues and Policies in Contemporary China

Course Description and Scope

This course is designed as an up-to-date course which will equip our students with the appropriate analytical framework and updated knowledge on the Chinese economy. The course will cover China’s latest macroeconomic issues which include:

- The exchange rate system reform since 2005;
- The banking reform in 2005-06, and its lessons to other emerging economies;
- Trade, foreign investment, balance of payment and foreign reserve management policies since 2006;
- China’s stock market since 2005: the building up of bubble in 2006-07, the gradual squeezing of bubble in 2008, the consolidation period in 2009-13, the rebound in 2014, and the risk of another bubble in 2015-16;
- China’s property inflation: microeconomic pains, macroeconomic risk, its solution and the effectiveness of the curbing measures;
- China’s macroeconomy since 2008: Impacts of the global financial tsunami, the ultra expansionary fiscal and monetary policies in 2008-10, impacts of the European Debit Crisis, macroeconomic challenges in 2011-14 and macroeconomic outlook in 2015-16;
- The latest property bubble in Asia, the risk of another Asian financial crisis and its potential impacts on China

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| 1       | **Macroeconomic Conditions and Debates before the Reform**
          | Macroeconomic conditions before the reform
          | Debates before the reform: China’s economic characteristics and the risk of various reform proposals | Yip, Ch 1 |
| 2       | **Transitional and Medium-term Designs of the Reform**
          | The proposed transitional reform:
          | • Gradual appreciation, no major or medium jump in exchange rate, and no widening of band;
          | • A basket of currencies with special care to the renminbi-US dollar rate at the early stage; and
          | • A narrow exchange rate band at the early stage
          | The proposed medium-term arrangement:
          | • The debating process before the medium-term recommendation;
<pre><code>      | • The medium-term recommendation | Yip, Ch 2 |
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<td>3</td>
<td><strong>Supplementary Measures that could help the Reform and Increase China’s Immunity and Resilience against Future Crises</strong>&lt;br&gt;Prolonged asset inflation and then economic crisis: a potential threat to China’s economic development&lt;br&gt;Supplementary measures:&lt;br&gt;• Banking reform;&lt;br&gt;• Control of asset inflation;&lt;br&gt;• Variable wage component;&lt;br&gt;• Capital control</td>
<td>Yip, Ch 3</td>
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<td>4</td>
<td><strong>The Transitional Reform in 2005 and the Market Response</strong>&lt;br&gt;The reform announced in July 2005&lt;br&gt;Market response during the first year of the reform&lt;br&gt;Important characteristics that contribute to the success in the first year&lt;br&gt;Subsequent mistakes committed by China’s central bank</td>
<td>Yip, Ch 4</td>
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<td><strong>Further Proposals on the Supplementary Measures</strong>&lt;br&gt;The potential disaster of developing a renminbi forward or futures market at that time&lt;br&gt;Further proposals to increase China’s immunity and resilience against future crises&lt;br&gt;Further proposals on the banking reform</td>
<td>Yip, Ch 5</td>
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<td><strong>The Second Stage Transitional Reform and Potential Choices for the Long Term System</strong>&lt;br&gt;Proposed design on the second stage transitional reform&lt;br&gt;Actual implementation of the second stage transitional reform&lt;br&gt;The medium-term exchange rate arrangement&lt;br&gt;Potential choices on the long term exchange rate system</td>
<td>Yip, Ch 6</td>
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<td>Chapter</td>
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| 7       | China’s Foreign Reserves, Trade Surplus, Outward Investments and Overseas Assets | Foreign reserves and holdings of foreign assets: some misconceptions and its policy implications  
Increase domestic demand to attain trade balance: a misleading proposal  
Trade balance not a good choice for China in the near future: dynamic optimum vs static optimum  
Reducing China’s dependence on exports: another misleading proposal | Yip, Ch 7        |
| Recess  |                                                                      |                                                                                                                                                                                                           |                 |
| 8       | China’s Stock Market Bubble and Lessons from the Bubble Squeezing Strategy | Excessive asset inflation: the more likely cause of a failed reform  
The formation of a stock market bubble in 2006-07  
The economic and political risks of a bursting of asset bubble: China’s last chance to gradually squeeze the bubble?  
The gradual bubble squeezing strategy  
The correction in 2008: from bubble squeezing to avoidance of over-correction  
Lessons from China’s experiences of bubble formation and bubble squeezing | Yip, Ch 8        |
| 9-10    | China’s Property Inflation: Microeconomic Pains, Macroeconomic Risk and Its Solution | Movements of property price in recent years  
Microeconomic reasons: why it could be disastrous to let free market force to guide China’s property market under the imperfect settings  
Macroeconomic costs and systemic risk  
Lessons from Hong Kong  
The policy solution  
Curbing measures since April 2010 | Yip, Ch 9-10      |
| 11      | Fiscal and Monetary Policies During the Global Financial Tsunami      | Sign of global economic slowdown in 2007H2  
Potential consequences of the anticipated plunge in US property price  
The debate with the central bank in 2008Q2-Q3  
The ultra expansionary fiscal policies  
The interest rate policy  
The substantial quantity easing in credit and money supply | Yip, Ch 11       |
Conclusions and Outlooks
US’s QE1 helped avoided a Great Depression, but raised the risk of subsequent global asset inflation and exchange rate cycle.
The global stock market during and after the financial tsunami.
US’s QE2 and its impacts.
US’s QE3 and its impacts.
The European Debt Crisis.
The latest property bubble in Asia, the risk of another Asian financial crisis and its potential impacts on China.

Textbook

Method of Instruction
Lectures : 2 hours per week
Seminars : 1 hour per week

Lectures commence in Week 1 and end in Week 13
Seminars commence in Week 2 and end in Week 14

Course Assessment
Project : 30%
Final examination : 70%
100%

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