

The Power of Transforming Public Expectations: The Chinese Experiences

by

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Working Paper No. 117

April 2025

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Acknowledgements

The Lau Chor Tak Institute of Global Economics and Finance is grateful to the following individuals and organizations for their generous donations and sponsorship (in alphabetical order):

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The Power of Transforming Public Expectations: The Chinese Experiences[§]

Lawrence J. Lau¹ and Mingchun Sun^{2 3}

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Abstract: Expectations of the future are important determinants of the behaviour of enterprises and households. Public expectations, positive or negative, if sufficiently concentrated and widely shared, can be self-fulfilling. They can, however, be transformed by the unexpected occurrence of sufficiently large and significant “surprises,” which can consist of unanticipated events or policy changes. A government with credibility is uniquely able to use the transformation of public expectations about the future of the economy as a possible macroeconomic policy instrument through its words and deeds. Four instances of successful transformation of public expectations from negative to positive by the Chinese government, in 1988, 1992, 1997-98 and 2008, respectively, are identified and examined. With the recent decline of public confidence in Mainland China and the intensification of the tariff war between China and the U.S., this may be the right time for some expectations-boosting moves from the Chinese government.

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³ The authors are most grateful to Prof. Yanyan Xiong of Zhejiang University for her invaluable advice and assistance on this study. They are also grateful to Prof. Joseph E. Stiglitz and Dr. Sujiang Zhang for their helpful comments. They remain solely responsible for any errors remaining herein.
The opinions expressed herein are those of the authors and do not necessarily reflect the views of the Institute.

Expectations of the future are important determinants of the behaviour of enterprises and households, affecting whether and how much they will invest and consume, respectively (Lucas, 1972; Barro, 1976). In particular, public expectations, positive or negative, if sufficiently concentrated⁴ and widely shared, can be self-fulfilling. If enterprises and households expect the economy to be good going forward and act accordingly, the economy will turn out to be good. Negative public expectations about the future, which are typically based on the actual existing economic conditions, can also be self-fulfilling. It is difficult for an economy with negative public expectations to prosper unless they are changed. Very often, what is needed to transform existing expectations is a “surprise,” a clear and unmistakable signal that transcends the then existing circumstances. For example, the breakout of peace, the proven discovery of vast oil or other mineral deposits, or the introduction of a new policy or set of policies can often transform public expectations from negative to positive and thus increase aggregate demand in a significant and sustainable manner (Barro, 1977; Cooper and Willis, 2010).⁵

The Formation and Transformation of Public Expectations

There are many ways in which public expectations about the future may be formed or transformed. Expectations may be based on past experience, such as the assumption of “tomorrow will be like today,” but they may not be based solely on past experience. As mentioned above, public expectations can be transformed by the unexpected occurrence of sufficiently large and significant “surprises”. The oil shocks of 1973 and 1980 were examples of such (negative) surprises. The collapse of Lehman Brothers in the U.S. in 2008 was another example of such a surprise. These surprises changed public expectations at the time and hence the subsequent economic trajectories.⁶ Public expectations of the future can also be transformed by some specific government pronouncement or action. A government, or sometimes a department such as the central bank or the planning commission, with credibility is uniquely able to use the transformation of public expectations about the future of the

⁴ Thus, not only the mean but also the dispersion of the distribution of the expectations of the public matter. Consider the following example: If half the population of a country expects a 3% economic growth and the other half expects a -3% growth, the expected rate of economic growth is 0%. However, it is likely that such an economy will behave quite differently from one in which the entire population expects 0% economic growth.

⁵ Of course, the “surprise” by itself may not be sufficient. The necessary accommodative and supportive measures must also be in place.

⁶ Robert Barro (1977) presented empirical evidence for the hypothesis that significant surprises (unanticipated money growth) can affect macroeconomic variables (unemployment) through their transforming effects on public expectations. Moreover, only genuine surprises can have such effects.

economy as a macroeconomic policy instrument through its words and deeds.⁷ It can perform the function of coordination of the expectations among the public (Guthrie and Wright, 2000; Pincheira, Calani and Landerretche, 2010; McKay, Nakamura and Steinsson, 2016; Bernanke, 2020; and Sun and Chen, 2025).

One well-known manifestation of self-fulfilling expectations is in the asset markets. If investors expect the price of an asset (for example, real estate or stock) to go up, and act accordingly by buying the asset, the price of the asset will indeed be driven up by the concerted buying because the increase in demand is not and cannot be immediately met by an increase in supply. Thus, the positive expectations of the investors (at least the initial ones) can be self-fulfilling. We have seen many such examples around the world, in which asset price bubbles are created. The Chinese stock price run-up and subsequent fall between November 2014 and July 2015 was such an example. However, self-fulfilling expectations are not limited to bullish ones. For example, if investors believe that the price of residential real estate is likely to be stable, and act accordingly, that is, they do not try to outbid one another in the market, since they know they can always buy a similar property at more or less the same price later, then the price of residential real estate will indeed be stable. This was what occurred in Singapore, where the government was believed by the public to adjust the rate of release of new lots for residential construction upwards and downwards in the same direction as the local market price of residential real estate. If investors believe that the price of residential real estate is likely to decline, as was the case in Mainland China after 2022 and in Hong Kong in 2024, and act accordingly, the price will decline, at least in the near term.

Another example of self-fulfilling expectations can be drawn from the experience of the Japanese economy. After the Japanese real estate price bubble burst in 1991, the expectations of the Japanese public, including both enterprises and households, about the Japanese economy were uniformly negative. Thus, enterprises refrained from making new investment and households cut back on consumption. As a result, Japanese aggregate demand fell and the Japanese economy hardly grew at all (Koo, 2009). The confirmation of the negative expectations through their realisation led to continuing negative expectations about the

⁷ We note that there is a distinction between transformation of public expectations and management of public expectations. Their objectives are quite different. Transformation requires a more comprehensive and holistic approach and is not limited to, for example, “forward guidance” on interest rates. Moreover, monetary policy alone may not be sufficient to transform negative public expectations as “one can pull on a string but not push on a string”.

subsequent period, with similarly negative results. Thus, negative expectations led to negative economic outcomes, which in turn led to still more negative expectations. Ultimately, because of this vicious circle, the Japanese economy remained stagnant for more than three decades.

However, one should not come to the simple conclusion that expectations are always self-fulfilling. In fact, there are expectations that are self-non-fulfilling. An example is the campus queen who winds up staying home alone on the night of the school prom because everyone who would have liked to take her to the prom thought that she must have a date already. Another example of self-non-fulfilling expectations is an election in which almost everyone expects one of the candidates to win, and hence few bother to go to the polls, and the favoured candidate winds up losing the election. Still another example is a concert by a famous singer, which everyone expects to be a sell-out. But if everyone expects it to be a sell-out, and hence does not bother to go to the concert, it may wind up with many empty seats.⁸

What is important about the distribution of expectations, in addition to its mean, is its degree of concentration—the more concentrated it is, the more likely the expectations will become self-fulfilling. However, as these expectations are fulfilled, they further reinforce, strengthen and concentrate the existing distribution of expectations, which then become even more self-fulfilling. Thus, once expectations become self-fulfilling and self-reinforcing, they are very difficult to change or dislodge. It will require a major correction, such as the bursting of the asset price bubble, or a major event, to change the entrenched public expectations. This is one reason the Japanese economy has remained sluggish for such a long time despite significant efforts on the part of its government and its central bank.

Of course, expectations can only be fulfilled if the expected outcomes are also feasible economically and technologically. The price of an asset cannot continue to go up forever if all the potential buyers are already in the market, so that at some point, without the inflow of new buying power, the price will begin to fall, despite the bullish expectations. This is what happened during the “tulip mania” in the Netherlands from 1634 to 1637⁹ and in the “dot-com”

⁸ However, with widespread adoption of social media and internet platforms (online ticketing, instant messaging, etc.) over the past decades, the last two examples are less likely to occur today.

⁹ This may be regarded as the very first asset price bubble in the world on record. Note that it lasted for three years. A speculative bubble can last for a while.

internet stock price bubble in the U.S. around 2000. So, ultimately, the rosy expectations may fail to be fulfilled. And this will lead to a collective revision of the expectations.

The Chinese Experiences

We identify and examine four instances of successful transformation of public expectations by the Chinese government during the past four decades. In China, public expectations are formed not only from directly experienced past market outcomes but also from the pronouncements and actions of the government. The government, because of the many potential instruments at its disposal, has the ability to transform negative expectations credibly through its words and deeds.

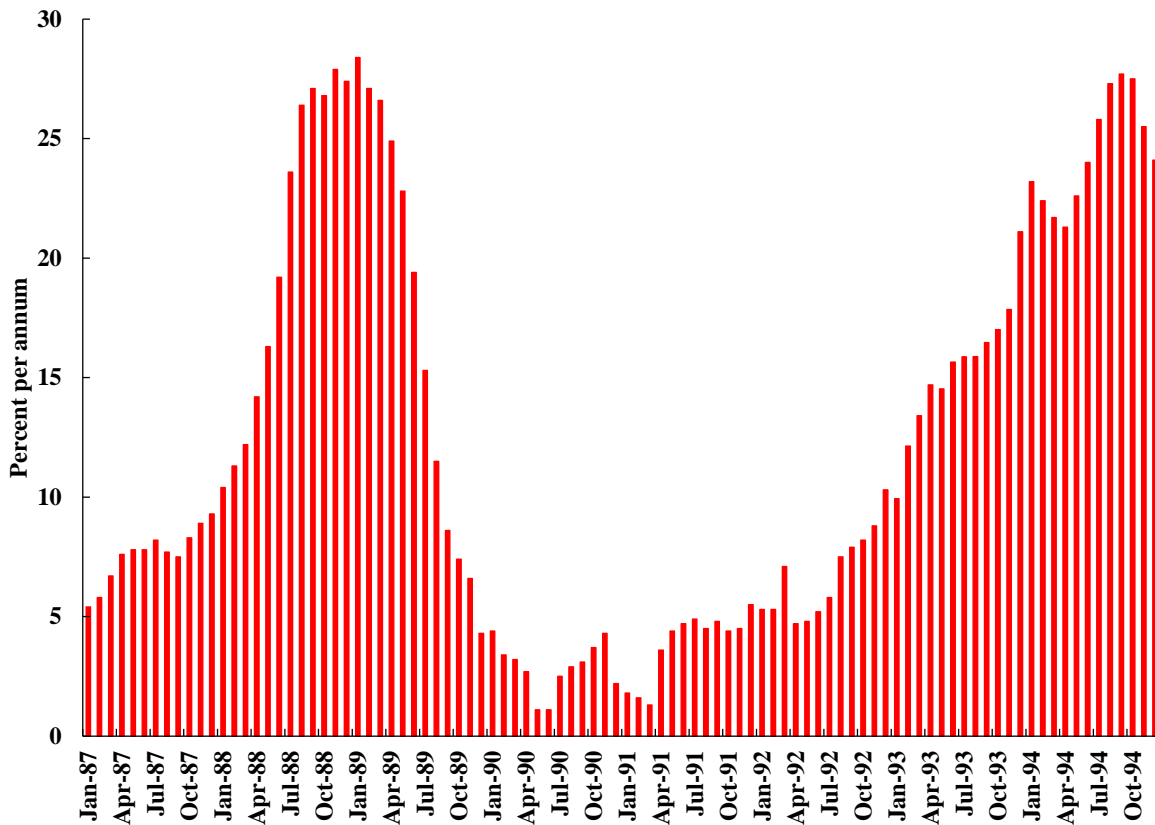
The first example is the control of a surge in consumer price inflation in August 1988. At the time, the rate of inflation was rising rapidly because of the introduction of free markets in the urban areas under the Chinese economic reform. The monthly year-on-year consumer price index rose from approximately 10.4% per annum annualised in January 1988 to 26.4% in August, the very first time for such high rates of inflation in China since the early 1950s. The public inflationary expectations were so high that there was panic buying and hoarding of goods everywhere. In response, the Chinese government introduced inflation-indexing of both the principal and the interest of bank savings deposits of over-three-year duration on 10 September and suspended further marketisation, which were sufficient to turn around the inflationary expectations of the public, restore confidence in the currency, and stop the panic buying and hoarding.^{10 11} The consumer price index stopped accelerating and only increased 0.7% to 27.1% that month. The Chinese government further imposed price controls on 24 October.¹² Finally, the rate of inflation began to decline rapidly in February 1989 (see Chart 1).

¹⁰ Inflation-indexing of bank savings deposits was also used in the early 1950s and was effective in bringing down the hyper-inflation at the time.

¹¹ Zhonggong Zhongyang Dangshi he Wenxian Yanjiuyuan (2025), Volume 3, Part 1, p. 435.

¹² Ibid.

Chart 1: Monthly Percentage Change in the Consumer Price Index, All Items, Year-on-Year



Source: International Financial Statistics.

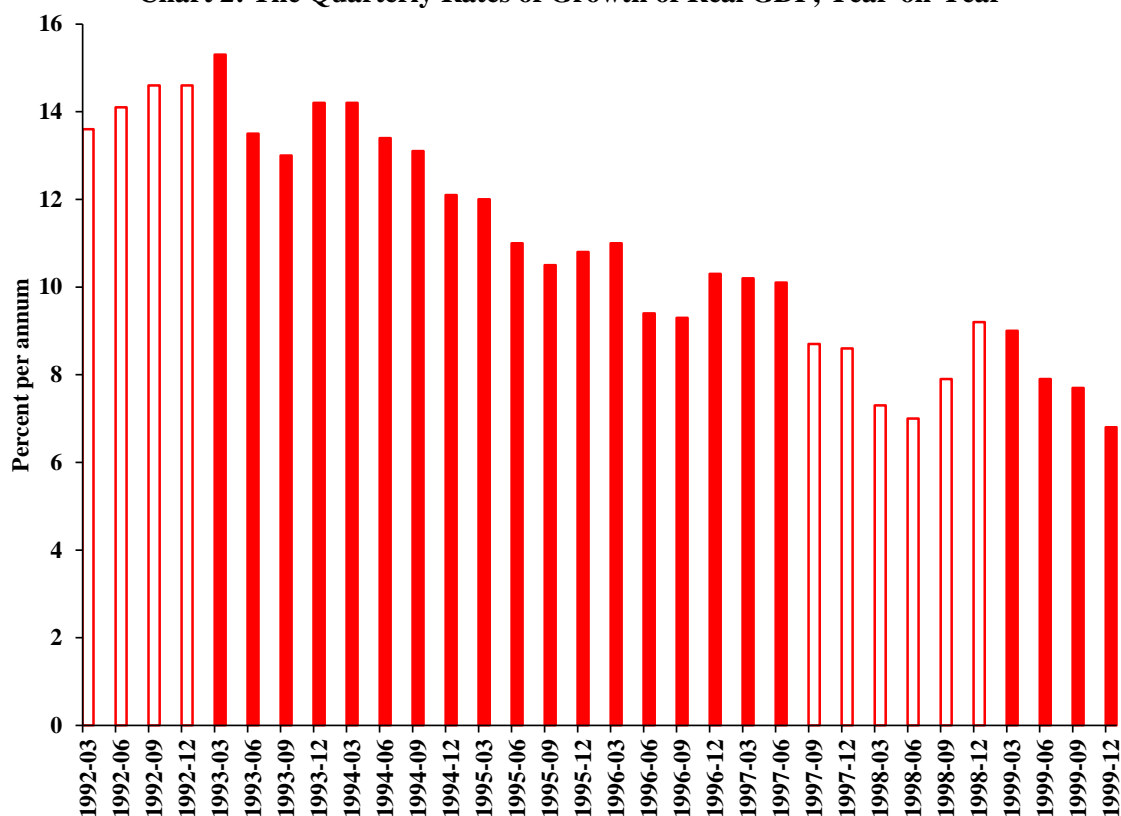
The second example is the southern tour of Mr. Deng Xiaoping, the then paramount leader of China, in January/February 1992. In 1989, in the aftermath of the 4th June incident, the Chinese economy became quite depressed, in part because of foreign sanctions, but mostly because of generally negative expectations about the future on the parts of enterprises and households. As a result, enterprises held back on their investments and households reduced their consumption. 1990 and 1991 were similarly slow years, despite an abundance of liquidity (see the discussion below). Then between 18 January and 21 February 1992, Mr. Deng undertook his famous southern tour, visiting Wuhan, Shenzhen, Guangzhou (Canton), Zhuhai and Shanghai. Everywhere he went, he emphasized the importance of economic development and urged the people to seize the moment and grasp the opportunities, putting aside the unproductive debate on capitalism versus socialism. His words changed public expectations in the entire country in the ensuing weeks and months. Enterprises, including private ones, began investing and households began consuming once again. Government officials at different levels changed their behaviour and became much more pro-growth. Banks were allocated more credit quotas, which was key to supporting the increases in fixed-asset investment in 1992-93 (see Chart 3). As a result, the rest of 1992, as well as 1993 and 1994,

were boom years for the Chinese economy, with double-digit rates of real economic growth (see Chart 2). Without Mr. Deng's southern tour, the stagnant negative expectations would probably have persisted and would not have been changed by the then existing economic data.

The available data on the rate of growth of quarterly Chinese real GDP are presented from 1992Q1 up to 1999Q4 in Chart 2.¹³ Chart 2 clearly shows the acceleration of the rate of growth of real GDP after 1992Q1. In Chart 3, the annual rates of growth of fixed-asset investment between 1982 and 2024 are presented. The "southern tour" effect is also clearly corroborated by the rates of growth of almost 50% and 70% in 1992 and 1993, respectively! This effect is further corroborated by the annualised monthly data on the rate of growth of Chinese value-added in industry between January 1990 and December 1994, presented in Chart 4. The positive impacts of the "southern tour" can be seen beginning in February 1992 (the dips in the monthly rates of growth in January 1993 and February 1994 were due to the Chinese New Year holidays). The "southern tour" effect is also reflected in Chart 1, in the renewed acceleration of the rate of inflation beginning in the second half of 1992 and through the second quarter of 1994.

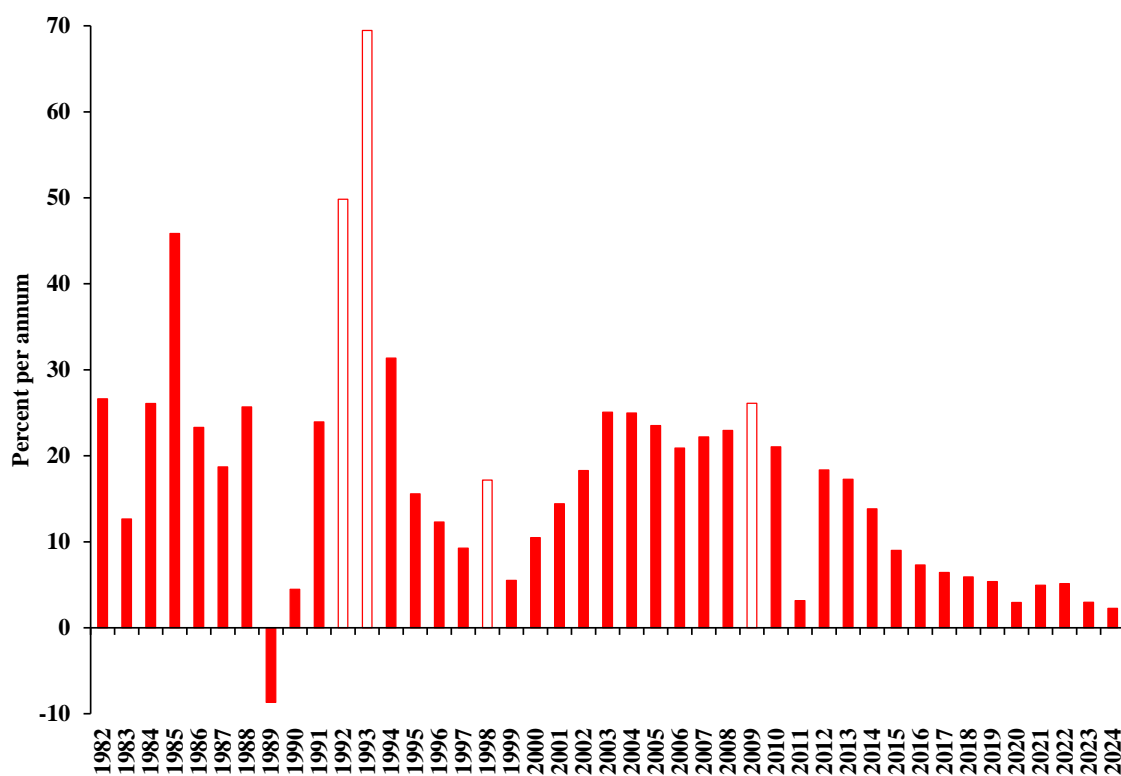
¹³ Unfortunately, published quarterly data on Chinese real GDP are not available before 1992. The annual rate of growth of Chinese real GDP in 1991 was 9.3%, which may be compared to the 13.6% of the annualised rate of growth of 1992Q1. The annualised quarterly rate of growth of Chinese real GDP remained above 9.3% until 1997Q3, when the East Asian currency crisis broke out.

Chart 2: The Quarterly Rates of Growth of Real GDP, Year-on-Year



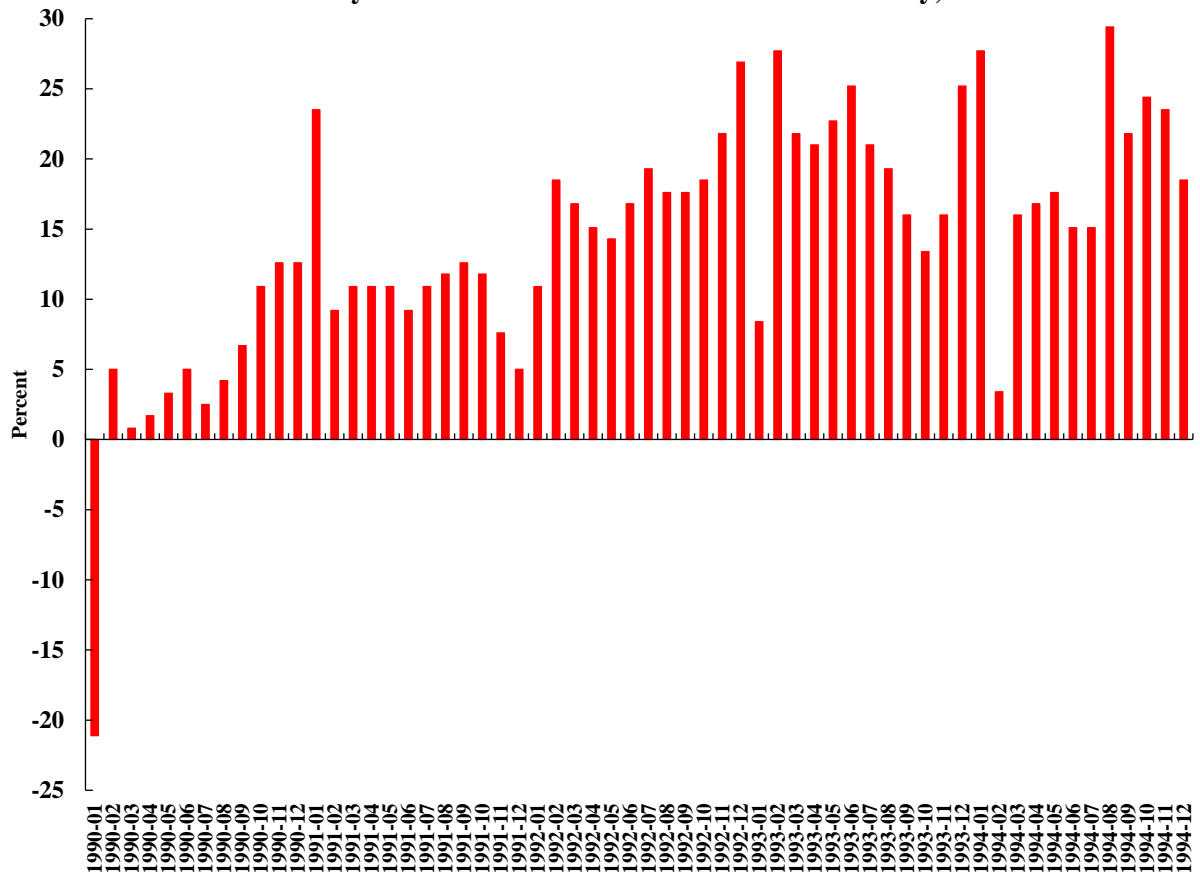
Source: National Bureau of Statistics of China.

Chart 3: The Annual Rates of Growth of Fixed-Asset Investment



Source: National Bureau of Statistics of China.

Chart 4: The Monthly Rates of Growth of Value-Added in Industry, Year-on-Year

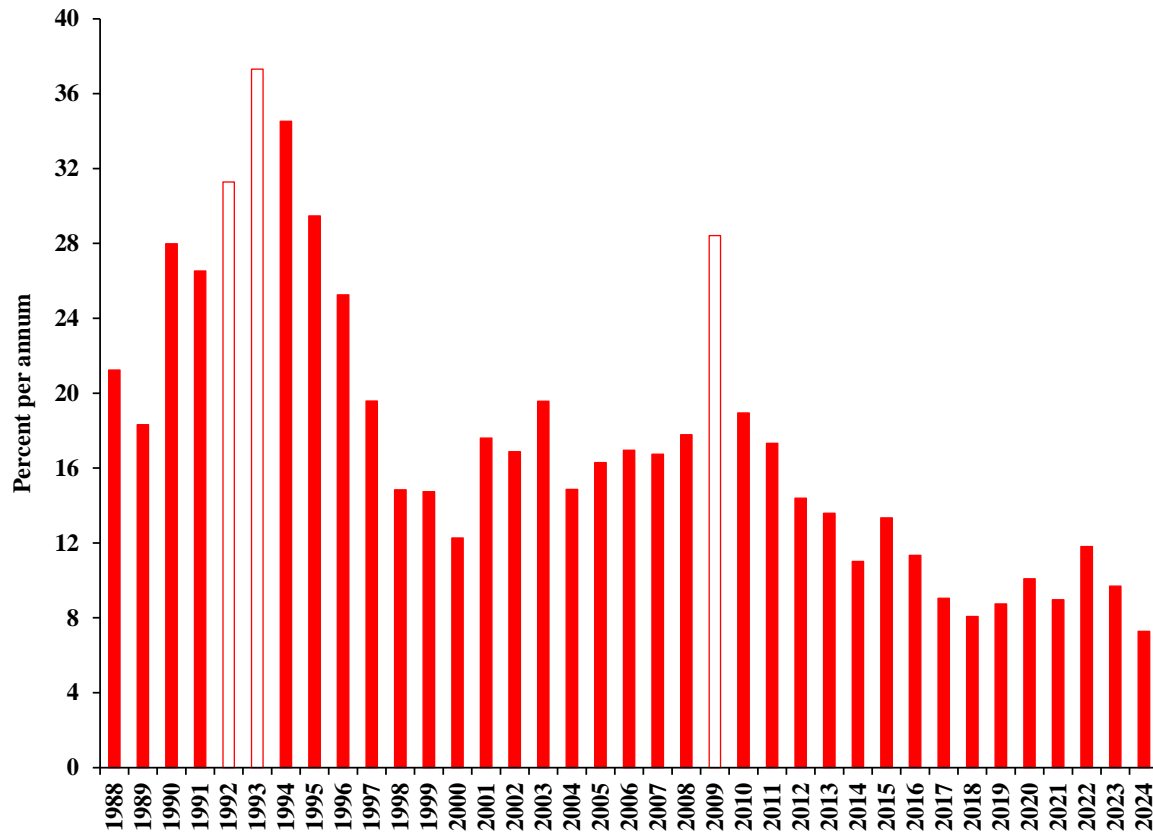


Source: National Bureau of Statistics of China; Wind Data Service (WDS) Database
(<https://www.wind.com.cn/portal/en/WDS/database.html>).

It is also of interest to examine the degree of adequacy of the Chinese money supply around the time of the southern tour. In Chart 5, the annual rates of growth of the Chinese money supply, M2,¹⁴ between 1988 and 2024 are presented. Chart 5 shows that even though liquidity was already ample in 1990 and 1991, with rates of growth of M2 of 28.0% and 25.5%, respectively, the economy did not respond until Mr. Deng spoke in early 1992. It took the southern tour for the Chinese economy to start growing rapidly again.

¹⁴ M2 is defined as total money supply and includes cash on hand, all bank deposits, and other short-term monetary instruments.

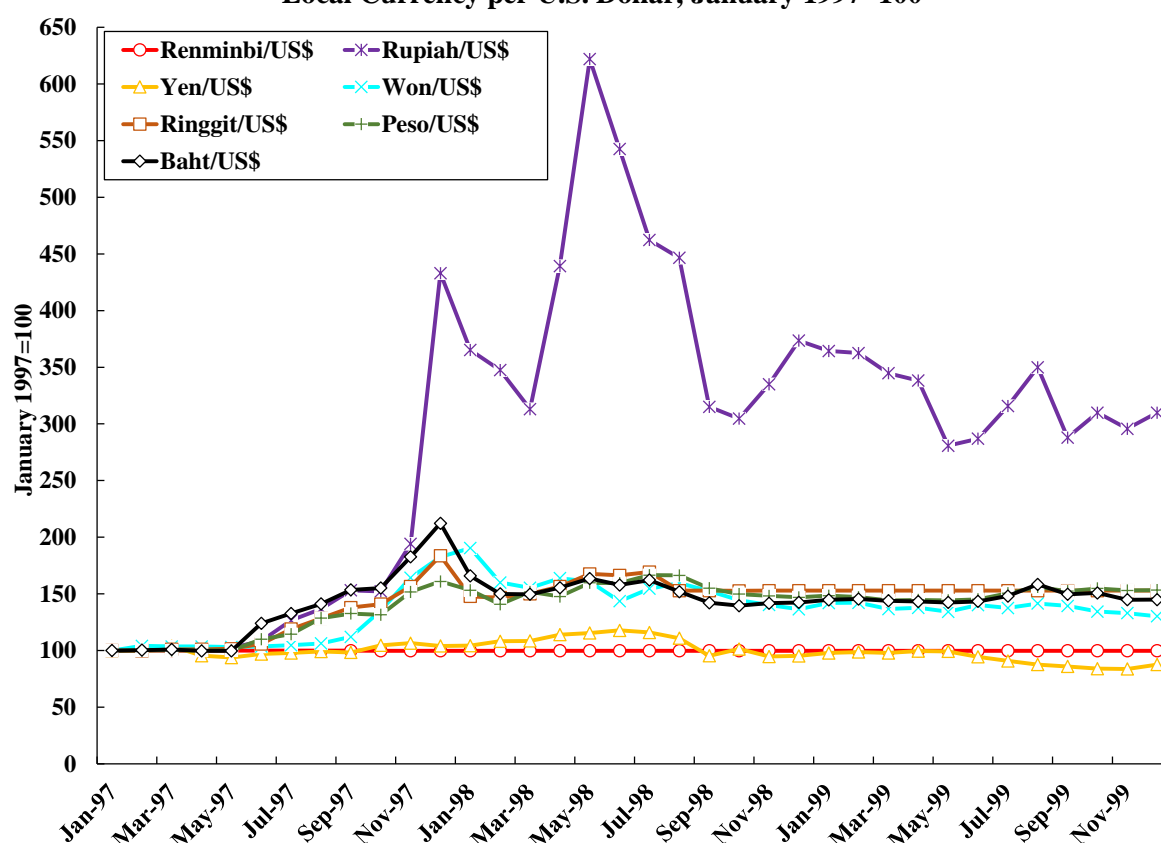
Chart 5: The Annual Rates of Growth of the Money Supply (M2)



Source: The People's Bank of China.

The third example is the Chinese response to the East Asian currency crisis of 1997-1998. The indexes of the exchange rates of selected East Asian currencies—Chinese Yuan, Indonesian Rupiah, Japanese Yen, South Korean Won, Malaysian Ringgit, Filipino Peso and Thai Baht—vis-à-vis the U.S. Dollar, with January 1997=100, are presented in Chart 6 below. The Renminbi/US\$ exchange rate is represented by the red line, which was essentially unchanged during this period. In July 1997, the crisis broke out, first in Thailand, followed by South Korea, until it eventually engulfed almost all of the East Asian economies. All of the East Asian currencies, with the exception of the Hong Kong Dollar, which was (and still is) pegged to the U.S. Dollar, and the Japanese Yen, devalued significantly, by 50% or much more.

Chart 6: The Indexes of the Exchange Rates of the Renminbi and Other East Asian Currencies, Local Currency per U.S. Dollar, January 1997=100



Source: International Financial Statistics.

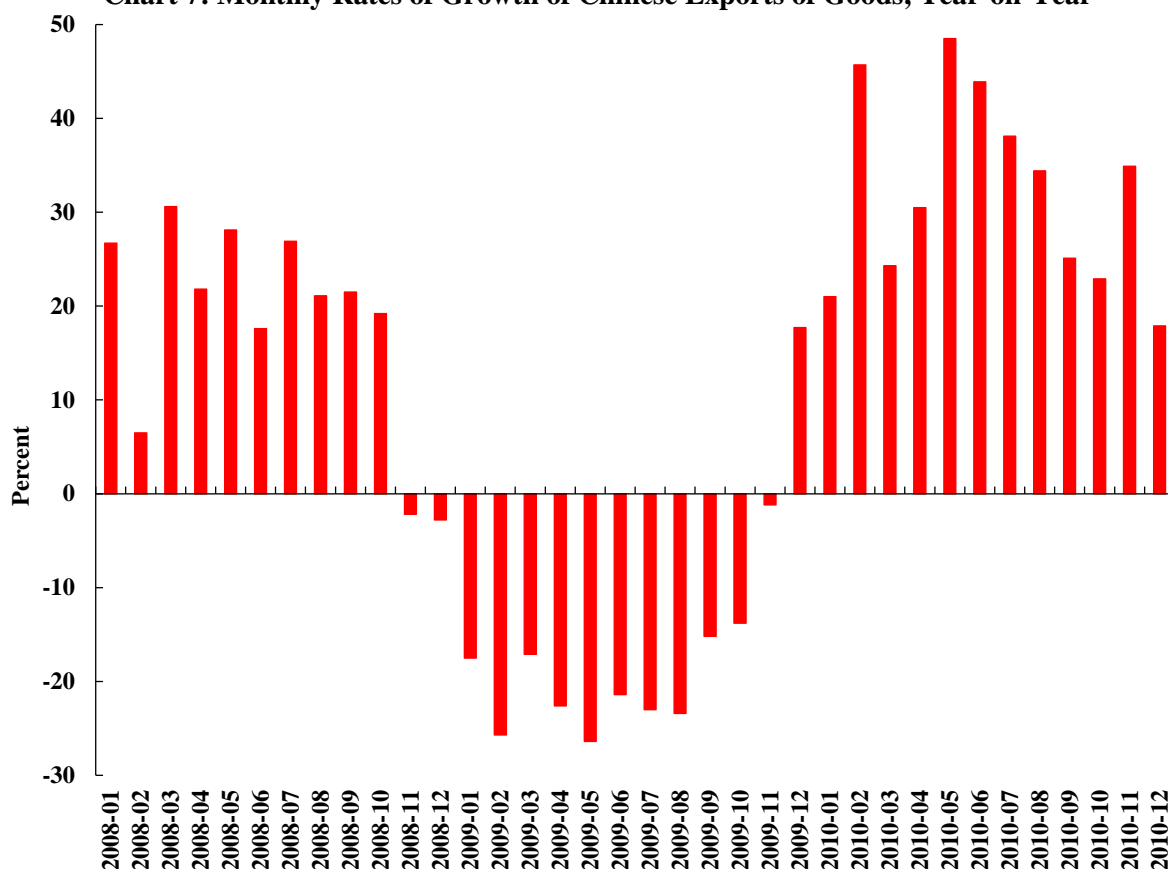
Amidst the chaos of the East Asian currency crisis, Chinese Premier Zhu Rongji decided to hold the Renminbi/US\$ exchange rate steady and made an explicit commitment of not devaluing the Renminbi vis-à-vis the U.S. Dollar in order to anchor public expectations. The Chinese central bank tightened measures to control short-term capital outflows as well as intervened directly in the onshore foreign exchange market. As a result, the Renminbi/US\$ exchange rate remained stable throughout this period, thus maintaining the confidence of the Chinese enterprises and households, transforming their expectations from negative to positive, and keeping the Chinese economy on a steady course. In so doing, China also helped to create favourable conditions for the eventual stabilisation of the exchange rates of the other East Asian currencies and the recovery of the other East Asian economies (Lau, 1997 and 1998). Had China also devalued at that time, it would have led to another cycle of competitive devaluations among the East Asian economies, with unimaginably negative economic, political, and social consequences.

In addition to keeping the Renminbi/US\$ exchange rate stable, the Chinese government also adopted a few measures to help lower the costs of Chinese exporters, including the full rebate of value-added taxes paid on goods exported,¹⁵ and increased new fixed-asset investment (see Chart 3). It set a target of a real rate of growth of 8% for 1998 and actually managed to achieve 7.8%.

The fourth and final example is the Chinese response to the Global Financial Crisis of 2008, triggered by the collapse of Lehman Brothers in the U.S. on 15 September 2008. In the immediate aftermath, all bank credit dried up in the U.S. as well as most of the other developed economies. Overnight, importers in the U.S. and other developed economies could no longer place their import orders to China and other trading partner countries because their banks were not in a position to issue acceptable letters of credit. As a result, export orders received by Chinese enterprises declined by approximately 50% (see the subsequent collapse in Chinese exports, with significant negative rates of growth for every month between November 2008 and November 2009 in Chart 7). There was real panic in the air. Fortunately, barely six weeks after 15 September, in November 2008, Chinese Premier Wen Jiabao announced the launch of the 4-trillion-Yuan economic stimulus programme, which once again managed to boost the confidence of Chinese enterprises and households in the economy and turn around their negative expectations.

¹⁵ Full rebate of value-added taxes paid on exports is actually a standard international practice.

Chart 7: Monthly Rates of Growth of Chinese Exports of Goods, Year-on-Year

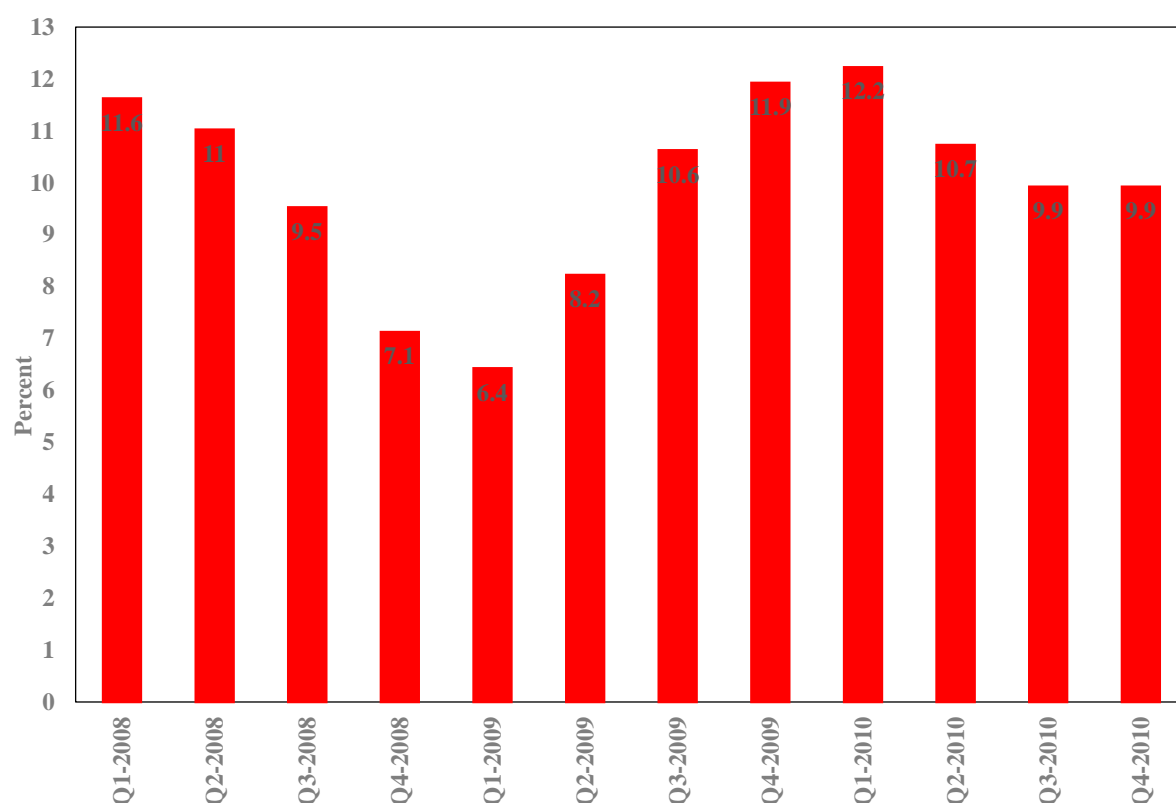


Source: National Bureau of Statistics of China.

Following the announcement of the 4-trillion-Yuan economic stimulus programme, the National Development and Reform Commission (NDRC) immediately accelerated its approval process for new fixed-asset investment. The People's Bank of China (China's central bank) also eased monetary policy and credit control significantly, resulting in surges in the money supply (M2) and loan growth in 2009 (see Chart 5), which facilitated the expansion of the aggregate demand caused by the stimulus programme (Sun, 2009; Cong, Gao, Ponticelli and Yang, 2019).

It is also possible to see the direct impact of the 4-trillion-Yuan stimulus programme on Chinese real GDP. In Chart 8, the annualised quarterly rates of growth of Chinese real GDP, year-on-year, between 2008 and 2010, are presented. The positive effect of the stimulus programme in reviving Chinese economic growth is clearly evident—the rate of growth declined from 11.6% in 2008Q1 to 6.4% in 2009Q1 as a result of the Global Financial Crisis. Then it began to accelerate again in response to the stimulus, reaching 12.2% in 2010Q1 and remained almost double-digit for the rest of 2010.

Chart 8: Quarterly Rates of Growth of Chinese Real GDP, percent per annum, Year-on-Year



Source: National Bureau of Statistics of China.

These Chinese experiences, with the possible exception of the one in 1988, share a few common characteristics. First, domestically, there was insufficient aggregate demand, even with apparently ample liquidity, which resulted from low public confidence and negative expectations about the future of the economy. Even a very low or negative real interest rate failed to encourage investment or consumption. Second, externally, China was faced with various constraints on the growth of her exports—ranging from weak demands, sanctions, or high tariff rates of trading partner countries such as the U.S. and those in Western Europe—and a devaluation of the Renminbi would not have improved the situation. In addition, foreign direct investment (FDI) had, for different reasons, also been significantly reduced or even completely halted in all these cases. This left increasing domestic aggregate demand as the only viable option for the Chinese economy to resume its growth. China had to rely mostly on itself to make the economy grow again.

In all of these examples, the Chinese government was able to turn around the very negative prevailing public expectations about the future of the Chinese economy by concrete and decisive actions at critical junctures, such as increasing fixed-asset investment and credit

availability, and thus enhancing the confidence of both enterprises and households and reducing greatly the uncertainty. These transformed expectations in turn led to investment booms that began in 1992, 1998 and 2009, respectively, and resulted in robust economic growth in the subsequent years.

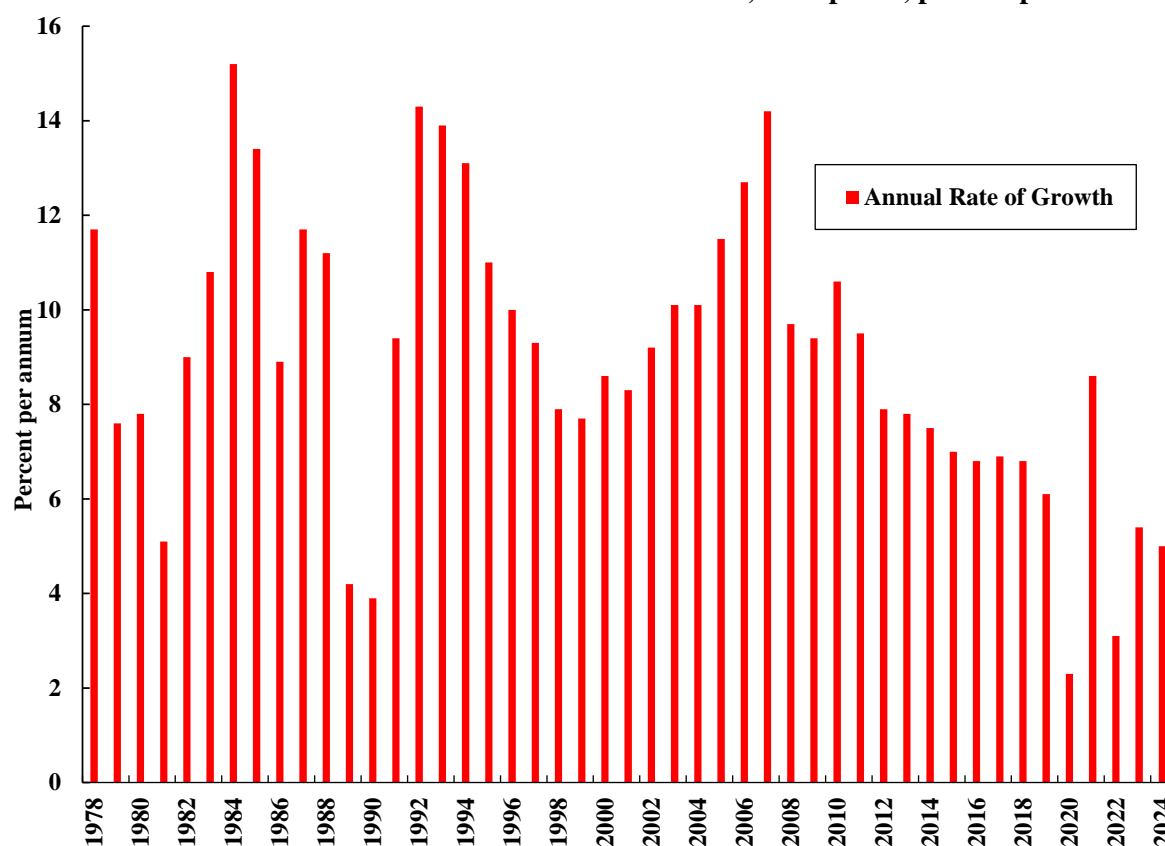
Implications for the Present

Since the mid-2010s, the Chinese economy has been in the process of transitioning to a “new normal”—a lower quantity but a higher quality of growth,¹⁶ more environmentally friendly, less export-dependent, more service-sector focused, less-tangible-inputs- and more-innovation-driven. The rate of growth of the Chinese economy has slowed down gradually from almost double-digit rates to a recent 5.0% in 2024 (see Chart 9). The announced target rate of growth for 2025 is around 5%. The slowdown is due, in part, to the quality-quantity trade-off, and, in part, to cyclical factors as well as multiple structural challenges (Lardy 2019; Fang, 2023; Wang, 2023),¹⁷ in addition to the COVID-19 epidemic of 2020-2022 (Lau and Xiong, 2021 and 2024) and all the uncertainty created by the ongoing China-U.S. strategic competition (Lau, 2019) in trade, technology and investment. It has led to a downward shift of public expectations about the future of the Chinese economy, contributing to insufficient domestic aggregate demand, even with apparently ample liquidity. Externally, China is faced with various constraints on the growth of her exports—ranging from weak demands, sanctions, or high tariff rates of trading partner countries such as the U.S. and those in Western Europe, which is not a problem that can be solved through a devaluation of the Renminbi. In addition, foreign direct investment (FDI) has also been declining. In other words, the Chinese economy is now faced with similar challenges as it was before.

¹⁶ There is indeed a trade-off between quantity and quality since many desirable public goods, such as blue skies, green hills and clear water, and extension of life expectancy, have real costs but no positive market prices.

¹⁷ Including the decline of the real estate sector and the lack of a sustainable tax base for the local governments.

Chart 9: Annual Rates of Growth of Chinese Real GDP, 2024 prices, percent per annum



Source: National Bureau of Statistics of China.

However, it is also important to realise that exports, which were the most important driver of Chinese economic growth in the two decades between 1990 and 2010, today play only a relatively subsidiary role (Lau, 2018a and 2018b; Wang, 2023; Lau, 2024 and 2025), just as they have been doing in the United States and Japan.¹⁸ This is due to the growth of Chinese real GDP per capita and its domestic market. In the meantime, China has become a surplus economy—there exists ample excess production capacity in China at the present time. This means that the domestic demands for consumption and investment together can determine the ultimate level of real GDP, unconstrained by supply. If there is demand, there will be supply. Moreover, the underutilisation of the existing production capacity is, for the aggregate economy as a whole, a waste of valuable resources.

The recent highly uncertain and unpredictable geopolitical situation, especially the “tariff war” being launched by U.S. President Donald Trump, has further negatively impacted

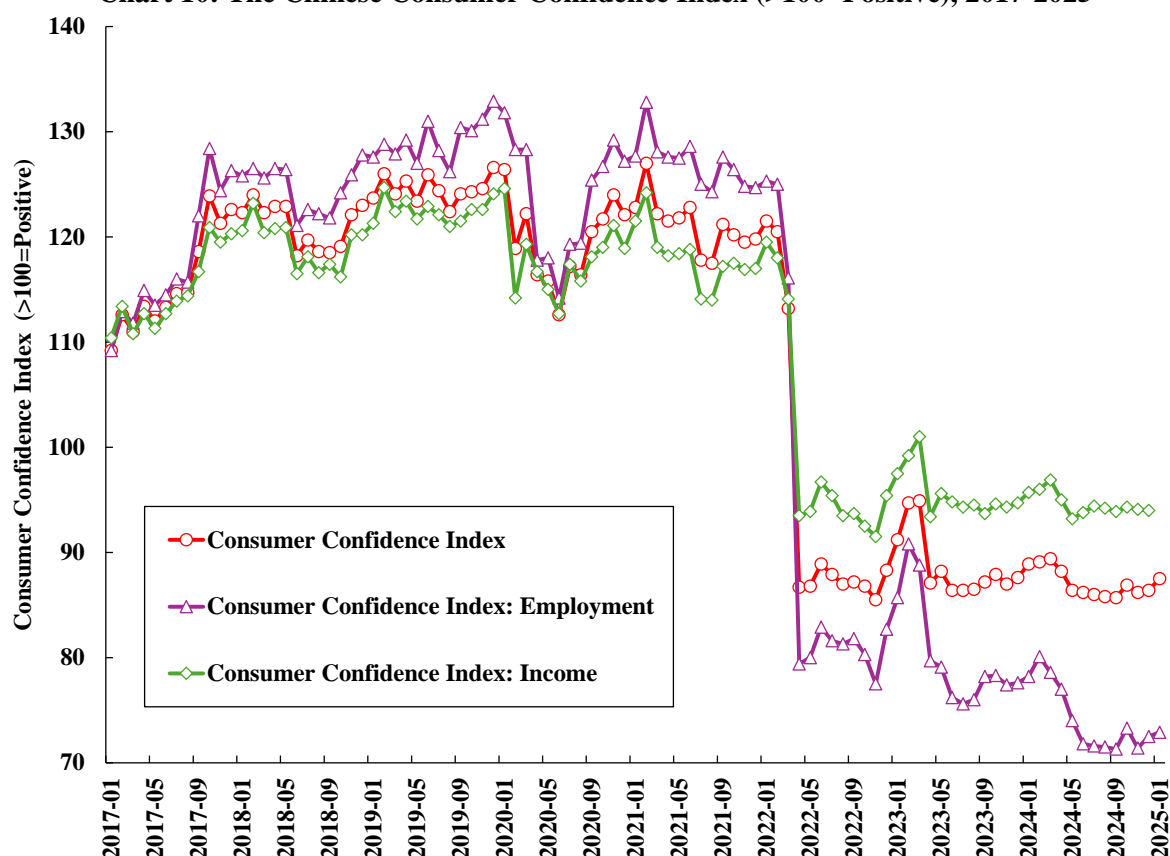
¹⁸ Chinese exports of goods and services accounted for approximately 20% of Chinese GDP, and had become quite diversified by destination over the years, with exports to the U.S. accounting for approximately 15% of total Chinese exports. Chinese net exports to the U.S. accounted for only 1.67% of Chinese GDP in 2023.

the Chinese economy both materially and psychologically. One prediction is that it would lower the rate of growth of Chinese real GDP in 2025 by 1.2%.¹⁹ It also implies that China must rely solely on its own domestic demand and not on foreign trade or foreign direct investment. In order for the Chinese economy to maintain a robust rate of growth, the Chinese government must ensure that there is sufficient domestic aggregate demand for consumption as well as investment. China must undertake additional economic stimulus measures to offset the negative impacts of the “tariff war”.

Domestic household consumption depends on household income and wealth as well as the level of confidence, which in turn depends on the household expectations of the future income and employment status. At present, although the official surveyed urban unemployment rate is only about 5%, workers are extremely unsure of the security and stability of their employment, resulting in a lack of confidence in their income prospects, which negatively affects their willingness to spend. This is clearly evident in the Consumer Confidence Index published by the National Bureau of Statistics, which plummeted in early 2022 because of the COVID-19 epidemic and has yet to recover, even though it seems to have stabilized somewhat (see Chart 10).

¹⁹ See Lau, 2025.

Chart 10: The Chinese Consumer Confidence Index (>100=Positive), 2017-2025



Source: National Bureau of Statistics of China.

Moreover, one cannot depend solely on household consumption to increase aggregate domestic demand because household income accounts for only about half of Chinese GDP.²⁰ One must therefore also increase domestic investment, both public and private, and in particular fixed-asset investment, as well as public goods consumption, just like what China did before. Thus, a transformation of public expectations is essential.

What are some potential sources of significant increases of domestic aggregate demand? On increasing domestic investment, infrastructural investments of various kinds are always possibilities, in not only communication, transportation and power sectors, but also public health (e.g., hospitals), elderly care, and environmental preservation, protection, and restoration. Another possibility is to extend China's current 9-year mandatory education, which was adopted in 1986, to 12 years.²¹ It will create the demand for a significant increase of new senior high schools in the whole country, greatly increasing the demands of teachers

²⁰ The Chinese Government has recently announced measures of stabilizing the residential housing and stock markets so as to increase household consumption through the household wealth effect.

²¹ In China, mandatory education means that it is provided free to the public by the state.

and administrators, as well as building materials such as cement, glass and steel, and construction services, and relieving the financial burden of lower-income families for putting their children through senior high school.^{22 23} It will also help to solve the current problems of high unemployment, especially youth unemployment,²⁴ and insufficient aggregate demand. It will also delay the entry of new workers into the labour force in the future by between three and seven years, as graduates of senior high schools are likely to go on to study in tertiary educational institutions.²⁵ Moreover, in view of the rapid development of artificial intelligence, it is imperative for the Chinese labour force to become better educated so that they remain productive in the future.

One important question is how 12-year mandatory education can be financed. As the provincial and local governments do not currently have the financial resources, it should be financed by the Chinese central government through the issuance of perpetual bonds. 12-year mandatory education should be considered a long-term national investment in human capital, and its costs can and should be shared by the current and all future generations through their successive payments of the interest on the perpetual bonds.²⁶

On increasing domestic household consumption, one would have to rely on the effects of increases of disposable income, wealth and liquidity (credit). Temporary suspension of the social security contributions (the five risks and one fund)²⁷ can help in the near term, so does reducing the degree of progressivity of the taxation of individual labour income.²⁸ However, the central government can also commit to an accelerated schedule of future salary adjustments for civil servants, which will raise their household wealth (human capital) and hence their household consumption immediately, but does not cost the government anything until a few

²² At present, only 60% of the graduates of junior high schools enroll in senior high schools, so there will have to be a significant increase in the number of senior high schools to meet the expanded demand. However, some of the existing vocational and professional high schools may be converted into formal senior high schools.

²³ Making senior high school mandatory and hence free to the public also has the additional benefit of reducing the financial burden of families with children, and perhaps encouraging them to have more than one child.

²⁴ For example, the unemployment rate for the cohort of ages 16 to 24 rose to 16.9% in February 2025.

²⁵ The extension of national mandatory education from 9 to 12 years will have a similar impact on increasing employment of graduates of tertiary institutions in the near term and national human capital in the long term as the expansion of the university freshman admission quota in 1998 under the then Premier Zhu Rongji.

²⁶ If the financial condition of the Chinese central government permits, it can also retire some or all of the perpetual bonds by buying them back on the open market from time to time.

²⁷ “wuxian yijin”.

²⁸ In the long term, it is necessary to raise the share of labour in GDP. This can be accomplished in various ways, including of course a rise in the level of salaries and wages. However, the right time to do so is when the economy is more prosperous. Equalising the taxation on capital and labour incomes can also be helpful.

years later. In the meantime, the government can benefit from the increased revenue resulting from the increased consumption. This will also induce the private sector to raise wages and salaries as well. It is probably a more reliable and sustainable way of increasing household wealth than trying to drive up the stock market.

Perhaps this is the time for the Chinese government to take more decisive and visible actions to increase domestic aggregate demand for consumption and investment, sending a clear signal to the public which reduces uncertainty, shores up confidence, and transforms the expectations of the Chinese people about the future. It should not hesitate to use its unique power, which has proven effective on quite a few previous occasions, to turn around the currently negative expectations to get the economy moving again.

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