China’s Infrastructure Spending in the Wake of COVID-19

Green growth pressures spell opportunity for strategic investors

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Executive Summary

We anticipate China’s current post-COVID-19 growth spurt to continue into 2021. Beyond that, we see a cooling down in trend growth consistent with the pre-pandemic structural slowdown.¹ China’s infrastructure spending is an important factor in this economic recovery period. Like a growing number of countries before it, China’s government recently pledged to achieve carbon neutrality by 2060. At the same time, governments around the world have pledged trillions of dollars in stimulus programs to counteract the economic fallout from the COVID-19 crisis. Achieving these carbon reduction targets requires that a significant part of this stimulus spending be directed towards so-called green investment. In this report we analyze what share of China’s infrastructure spending has been allocated to green projects so far, and what can be expected going forward.

Insights for What’s Ahead

Initially, China’s economic recovery will not be from “green” infrastructure; but, over time, we expect to see an acceleration of investment into green projects. Comparing the size of local government special-purpose bonds (SPBs) issued in the first half of 2019 and 2020, the share of green projects increased from 5.4 percent to 20 percent. However, when taking public housing redevelopment out of the equation (which can no longer be financed through SPBs in 2020), the share of green SPB investment has remained constant pre- and post-COVID: 22 percent in 1H 2019 versus 21 percent in 1H 2020. China has neither backtracked on green investments nor has it moved forward noticeably. This suggests that growth pressures are significant and that efforts, so far, are centering around mitigating the economic impact from COVID-19, and that this includes supporting legacy, environmentally intensive sectors. Having said that, we believe that the government will stand by, and likely strengthen, its commitment to environmental protection and pollution control. Companies will need to monitor near-term regulatory developments very closely to anticipate changes in domestic energy and environmental priorities.

Longer-term, China’s pledge to achieve carbon neutrality by 2060 will create major opportunities for companies who contribute positively to China’s carbon reduction target. On September 22, the Chinese government announced that its economy would be carbon neutral by 2060. The systemic change required to do this will have a profound impact on companies’ in the local operating environment and a positive impact for those companies contributing to the achievement of this promise. Once economic planning and target setting pivots towards carbon neutrality, there is going to be significant upside opportunity for investments focused in areas like renewable power generation and energy storage capacity, energy efficiency in transport, buildings, and industrial systems, and electrification in industry, transport, and end-use, including smart, digital, and flexible electricity networks.

In the meantime, China’s trend towards stricter pollution control and prevention is unlikely to falter. Companies, especially those in emissions-intensive industries, should proactively prepare for tightening oversight of emissions. COVID-19 has clearly influenced domestic energy and environmental policies in the near-term. But we expect this to be temporary. The 14th Five-Year Plan (FYP), due to be released next March, will almost certainly lay out some important emissions-related markers. Areas to watch include the possibility of more aggressive non-fossil fuel energy share and carbon emissions targets, a fully operating national carbon market, and possibly peak carbon targets for specific sectors and localities. Business should also expect the release of more detailed plans and quantitative targets that support the government’s long-range objectives through 2035. These policy developments will have direct business implications regarding companies’ emissions monitoring and disclosure requirements, supervision, auditing, and overall enforcement of emissions standards. Companies should expect this stepped-up supervision to involve China’s Corporate Social Credit System.2

Looking further ahead, China’s carbon neutrality pledge presents a strategic opportunity for companies to steward green growth as a core value proposition element. Given the attention China’s carbon neutrality pledge has received both domestically and internationally, China’s government bureaucracy will foreseeably place high importance on achieving progress-to-plan on emissions reduction. To accelerate implementation, the government is certain to lean on large businesses to serve as role models and drive change. Now is the time for companies to strengthen their sustainability agenda in China and develop or update their business and government relations strategies to emphasize their support for net-zero achievement. For companies leading on decarbonization, significant benefits should be achievable across market access, government relations, customer relations, and employer brand dimensions.

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