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MONDAY VIEW

By Dr Gerard Lyons

Selling to China, the three key words for the UK

THIS week, Britain and China meet for their fourth annual Economic and Financial Dialogue.

Chancellor George Osborne will host one of China's vice-premiers, Wang Qishan, and his high-level delegation. This is the only dialogue of its type China has in Europe, and one has to wonder whether the UK makes the most of this.

Increasingly, what happens in China is of more importance to us.

Now the world's second largest economy, China is experiencing an industrial revolution every bit as important as the one the UK enjoyed more than two centuries ago.

I still do not think the UK fully appreciates the scale and pace of change on the ground across Asia and much of the emerging world.

China is at the forefront of that change. With so much that can be said about China let me highlight three key issues for the UK.

First, China's economy is still set to grow at a solid pace in the coming years. For much of the past year, China has been tightening policy to curb inflation. Now it appears to have peaked and instead the authorities are more worried about the impact on China of the recent global financial market turbulence.

Unlike here, where the policy cupboard is almost bare, China has plenty of room to boost its economy if needed.

In the coming months, they could start by relaxing controls on lending. Government spending can even be boosted, although that is not yet needed.

Second, despite its strong economic performance it would not be a surprise if, at some stage, China suffered a setback. After all, the business cycle exists in China, as it does everywhere else in the world.

As China's economy continues to grow it becomes harder to manage from the centre.

This has already triggered worries about the debt of local government investment vehicles and about high house prices.

I am often asked if China is a bubble economy. 'No' is the answer, but it is an economy prone to bubbles,

particularly in its property sector. This has led not just to higher interest rates but also to specific curbs aimed at cooling house prices.

These controls, called macro-prudential measures, are now being looked at by other countries, including the UK, to see if they can learn from them.

Third, it is vital to understand how China is changing the world. Over the last decade, the three most common global words were 'Made in China', as it became the centre for manufacturing.

This decade, the three most common words may well be 'Bought by China', as it swallows up resources around the world.

China's demand for commodities has been a key factor behind the high price of food, metals and oil.

Its relevance for the UK is that this is the explanation for why, unless sterling starts to become a stronger currency, we could face ever rising import prices.

Following his meeting with the Chancellor, the Chinese vice premier heads to Latin America. That region, like Africa, is vital for China's resource needs.

LOOKING further ahead, the three words likely to define the 2020's may well be 'Paid in Renminbi', as China's currency starts to assume a greater global role.

The renminbi is heavily controlled, but over the last year a significant development has been the growth of the offshore Chinese currency market, outside of China.

This is focused in Hong Kong but at some stage this market will grow in Europe.

London should aim to be Europe's offshore centre for trading the renminbi. This is one of many areas for the UK to explore when the September Dialogue takes place.

Another is for the UK and China to boost ties in trade and financial services.

The UK should not, however, underestimate the growing Chinese enthusiasm for Germany as Europe's leading economy.

Three key future words for the UK economy should be 'Selling to China.'

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