The US has come out of the pandemic in better shape than China with GDP above pre-pandemic forecasts, whereas China has struggled in the face of structural issues like the property slump. Slower growth means China’s economy is now unlikely to match the size of the US economy until the mid-2030s and living standards will remain well below those in the US.

What’s more, our cautious baseline may overstate the prospects for Chinese catch-up with the US. Our long-term growth forecasts now show China following a similar decelerating growth path to that seen in previous decades in South Korea and Taiwan, with GDP growth falling to around 2% by 2040. This has important consequences for China’s prospects of economic catch-up.

A decade or so ago, some forecasters thought China’s GDP would surpass that of the US by 2019, but our baseline forecasts now point to this happening only in 2036. And if China’s growth is 0.5% per year slower than in our baseline this date would be pushed back beyond 2040.

China’s GDP already looks larger than that of the US if purchasing power parity exchange rates are used. But PPP estimates are subject to large margins of error and have limited value in geopolitical terms. Even using PPP exchange rates, China’s living standards will remain well below US levels, with income per head just 40% of the US level in 2040 according to our baseline.

In addition, some estimates suggest that official Chinese data overstate its GDP by around 20%. If correct, this would mean catch-up prospects are even more distant – China’s GDP would be currently smaller than that of the US even using PPP exchange rates.

China’s growth over the next 20 years is also subject to notable downside risks. Our baseline forecast remains dependent on strong productivity growth to offset demographic drags, and this may disappoint. The US is also likely to benefit more from a potential AI-related productivity upturn, at least initially, with decoupling potentially delaying China’s gains in this area.

Chart 1: US GDP has matched pre-pandemic forecasts while China’s has lagged

<table>
<thead>
<tr>
<th>US and China: GDP</th>
<th>Indices, Q4 2019=100, different forecast bases</th>
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<tr>
<td><strong>US</strong></td>
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<td>US Dec 2023</td>
<td>China Dec 2023</td>
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<td>US Jan 2020</td>
<td>China Jan 2020</td>
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</table>

Source: Oxford Economics
Solid US growth since the pandemic contrasts with the stuttering performance of China

The US has come out of the coronavirus pandemic in better shape than China. Over the last year, US growth has surprised to the upside and the level of US GDP in Q3 2023 was slightly above our pre-pandemic forecast from January 2020. By contrast, our forecasts for China over the last year have been revised down – its GDP in the same quarter was 4% below our pre-pandemic forecasts (Chart 1).

While the US has benefitted from robust consumer spending, aided by fiscal expansion, China has struggled with the negative effects of its prolonged zero covid policies, regulatory uncertainty, and serious structural problems – including in the property sector. Low US unemployment has contrasted with record high youth unemployment in China. This divergence in performance has been reflected to some extent in foreign exchange markets, with the Chinese renminbi losing around 14% of its value against the dollar since Q4 2021.

Increasingly, commentators are talking of China having a broken growth model, which has significant consequences for long-term growth forecasts and geopolitical developments. Our baseline forecasts for long-term Chinese growth now show the country following a similar decelerating path to that taken by an earlier generation of fast-growing Asian economies such as South Korea and Taiwan. China’s growth has already slowed from a double-digit annual pace in 1995-2014 to around 5% per now, and we expect it to decline further to around 3.5% per year in 2030 and around 2% by 2040 (Chart 2).

Chart 2: A further growth slowdown to come in China

These forecasts are very different from some of the bullish projections for China’s long-term GDP that were common a decade or so ago. Our current baseline implies a real GDP level for China in 2035 that is around 30% lower than consensus forecasts of 2014 would have suggested. Even comparing with consensus forecasts from 2020, our baseline for Chinese GDP in 2035 is 12% lower (Chart 3).
Chinese catch-up prospects recede as the US outperforms

Chart 3: Chinese long-term growth downgrades since 2014 have been large

China: Real GDP long-term forecasts
Indices, 1999=100

1600
1400
1200
1000
800
600
400
200
0
Forecast
Dec-23
Consensus 2014
Consensus 2020

Source: Oxford Economics/Consensus Forecasts

China’s catch-up with the US now unlikely until the mid-2030s

These massive downward revisions in the outlook for long-term Chinese GDP have profound implications for the prospects of economic catch-up by China. In 2010, The Economist suggested China’s GDP would be larger than that of the US as early as 2019. In 2011, Goldman Sachs forecast 2026 as the ‘crossover’ year. In 2018, the OECD was still forecasting 2025 as the year when China’s GDP would outstrip the US’s, and as late as 2020 the EIU said 2029. But as of 2023, China’s nominal dollar GDP is only 70% of that in the US and our baseline forecasts see it surpassing the US’s only in 2036 (Chart 4).

Chart 4: China’s catch-up with the US keeps being pushed back

China: Nominal GDP as a share of US GDP

% of US GDP

Source: Oxford Economics/OECD/EIU/GS

Moreover, additional growth disappointment in China over the coming years could push this date considerably further into the future. If China’s GDP growth were 0.5% per year slower than in our baseline forecast, the crossover point with US GDP would be delayed beyond 2040. A better-than-expected US growth performance could have a similar result.

One objection to this pessimistic take on China’s catch-up potential is that if purchasing power parity exchange rates are used, China’s GDP is already larger than that of the US. This is true if we use the PPP estimates from the International Comparisons Program (ICP). But such comparisons are fraught with difficulties for several reasons:
PPP exchange rates are much harder to estimate than market exchange rates. Assembling PPP estimates is a very complex process, involving collecting the prices of a wide range of goods and services across very different economies. An obvious danger is that some prices collected are unrepresentative of average prices across an economy, biasing PPP estimates. Deaton and Heston in 2010 argued the practical difficulties involved “make comparison exceedingly hazardous”.

PPP estimates are subject to large margins of error. The International Comparison Program notes that there is a margin of error of 15% when using its data to compare economies of different sizes. PPP estimates have also been heavily revised in the past. The 2017 survey revised China’s PPPs for 2011 by 5%. Most remarkably, the 2003-2007 round revised down China’s PPP GDP by a massive 40%. There can also be large discrepancies between different estimates of PPP GDP, including due to methodological issues. A 2004 study found that using unit values from household surveys rather than price surveys produced quite different results for PPP estimates between Indonesia and India compared to World Bank estimates.

New figures for PPP comparisons are available only infrequently. Surveys occur several years apart and for years in between estimates must be made that can introduce inaccuracies. Using PPP estimates for any year other than the benchmark year when the detailed price data was collected is risky.

For geopolitical comparisons, PPP is less useful than market exchange rates. Simply put, you cannot buy things on the world market with PPP currency. An economy’s capacity for purchasing supplies and armaments or being an international borrower or lender is based on market exchange rates. Similarly, an economy’s importance to others as a trading partner is also based on market exchange rates.

All this means that while using current dollar GDP to compare the size of economies has its drawbacks (most notably possible distortions from fluctuating exchange rates), using PPP exchange rates is arguably even more problematic.

Where PPP is most useful is in comparing living standards across economies, as it can capture important differences in national price levels (in particular, that non-traded goods and services tend to be quite a lot cheaper in lower-income economies). But even on this dimension, China’s prospects for catch-up with the US are receding. In 2011, it looked like China might see GDP per head in PPP terms converge with that of the US relatively quickly. But the rate of catch-up has slowed notably since. Our baseline forecasts now see China’s PPP GDP per head at only 40% of that in the US even in 2040, versus around 30% now (Chart 5).

Chart 5: China’s living standards will remain well below those of the US even in 2040

It's also feasible that official measures of GDP in China are overstated. Chen et al. suggest that China's growth was overstated by 1.8ppt per year in 2010-2016 on the basis of alternative data from tax records, light intensity observed from satellites, and other trade and activity measures. As a result, China's GDP today might be as much as 18% lower than the official statistics claim, and only 58% of the US level rather
than 70%. Using these alternative estimates, even PPP GDP would be smaller than that of the US (Chart 6). Other studies also point in this direction such as Henderson et al, and, perhaps most notably, Wu whose alternative GDP estimates for 2012 were over 20% lower than the official data.

**Chart 6: China’s official GDP numbers may be overstated**

![Chart 6: China’s official GDP numbers may be overstated](source: Oxford Economics * Based on Chen, Chen, Song & Hsieh (2019))

### Several downside risks to China’s catch-up

As above, even a relatively modest disappointment in China’s growth over the next 15-20 years would risk pushing the date of China’s economic catch-up with the US back even further. In our view, the risks of such a disappointment are considerable, especially in light of China’s slower than expected progress in catch-up over recent years.

One obvious risk relates to the ongoing slump in the property sector. Some impact from this is factored into our baseline forecasts, but a longer and larger effect can’t be ruled out, especially if the authorities’ tolerance for short-term pain rises (leading to a sharper tightening in credit conditions) or households reduce their demand for property assets more than we currently expect on the back of more entrenched expectations of sharp price declines.

In addition, there are risks associated with the structure of long-term growth. From 2030 onwards, labour supply will become a negative factor for potential GDP, and growth will increasingly rely on relatively high rates of productivity increases to offset the demographic drag (Chart 7). As we have noted before, there are clear downside risks here – our forecast for total productivity growth for China to 2040 is high compared to other emerging economies with similar income levels over the same period.
Chinese catch-up prospects recede as the US outperforms

Chart 7: China’s long-term growth could disappoint

The impact of trade and technological decoupling is another risk area. We have estimated previously that technological decoupling could cut Chinese growth by 0.3ppts per year, with additional trade decoupling perhaps doubling this in a very negative scenario. We are optimistic about some fast-growing industries such as batteries, electric vehicles, and renewables, but these sectors are still relatively small compared to key traditional Chinese industries like property, infrastructure, and processing trade and so are unlikely to carry the whole economy.

Also in the tech sphere, the US as the global tech leader is more likely to reap the benefits of any productivity bonus from the adoption of AI, at least initially, with decoupling potentially delaying benefits for China. As a result of all these risks, it would not be surprising to us if a few years from now the forecast date for when China’s total GDP will outstrip that of the US is pushed back even further.

Appendix: China versus India

While China’s prospects for catch-up to the US are less marked than some claim, India is not an automatic alternative.

Although we have a positive view on India’s economy and it also has a huge population, the prospects of India overhauling China’s GDP in the next two decades and India thus providing an alternative market to China are slim. Despite rapid long-term growth of almost 6% per year in 2020-2030 and around 5% per year in the following decade, India is starting from a low base with its total dollar GDP at current exchange rates only 20% of China’s. This will rise to around 30% by 2040 (Chart 8).
Chinese catch-up prospects recede as the US outperforms

Chart 8: India set to remain a smaller market than China

China and India: GDP
US$ tr, nominal

Source: Oxford Economics