Are we overplaying the bad situation in China?

Nicholas Lardy, one of the foremost experts on the Chinese economy, certainly thinks so. Lardy thinks many analysts are looking at the wrong indicators in China and are misinterpreting the central bank's decision to introduce a more flexible exchange rate regime.

First, let's address the issue of overstating the GDP. Critics point to the country's weak industrial production, export and investment figures as proof that the country is fudging its number. Lardy, a senior fellow at the Peterson Institute of International Economics, points to a salient fact that many people choose to ignore: the biggest contributor to the country's GDP is now the services industry.

" … the skeptics have taken insufficient notice of China's progress in transitioning to its new model of economic growth, one less dependent on expanding industrial output, investment, and exports and more dependent on expanding private consumption expenditure", he says.

Between 2011 and 2014, the size of the service sector as a share of GDP rose by about 4 percentage points to 48 per cent and, at the same time, the share of the industrial sector dropped to 43 per cent of GDP. This is a marked change from a decade ago, when the industrial sector accounted for 47 per cent of the GDP while the service sector only accounted for 41 per cent of the economy.

Considering the size of China's economy -- it's a $US10 trillion behemoth -- the transition is even more impressive. Many services are booming in China, the e-commerce sector grew by 31.4 per cent in 2014. The entertainment sector has been growing at an average of 17 per cent a year between 2010 and 2015. In health care, McKinsey predicts the growth in spending will grow from $US357 billion in 2011 to about $US1 trillion in 2020.

If you pause for a moment and think about the growth momentum in these sectors, the grim situation in China looks a bit less frightening. The consumption trend is also backed by sustained wages growth. The country's disposable income has been growing at a double-digit rate for more than a decade and factories are now paying more than 100,000 yuan ($21,000) in annual wages to skilled workers.

Nicholas Lardy believes one of the reasons that sceptics are overlooking the positive story in China's development is there are no high frequency data to support the analysis above. "At best these data are quarterly, some are annual and some are released with a very long time lag. The rising demand for a real-time analysis of the Chinese economy and growth performance has led to overreliance on industrial and investment data, which has been published monthly," says the veteran China watcher.

This was a reasonable approach in the 2000s when industry was the main driver of China's growth, but not today when the sources of growth have evolved."

Though China's economic growth story is far from perfect or even healthy, it is wrong to focus exclusively on data from the industrial sector that is no longer the main driver of the country's GDP.

Commentators and analysts invented the 'Li Keqiang Index' as a way of gauging the true state of the Chinese economy, it's about the time we started to dig into Alibaba data, box office figures and sales of medicine in order to better understand the true dynamics of this rapidly changing economy.