

China Macro Outlook

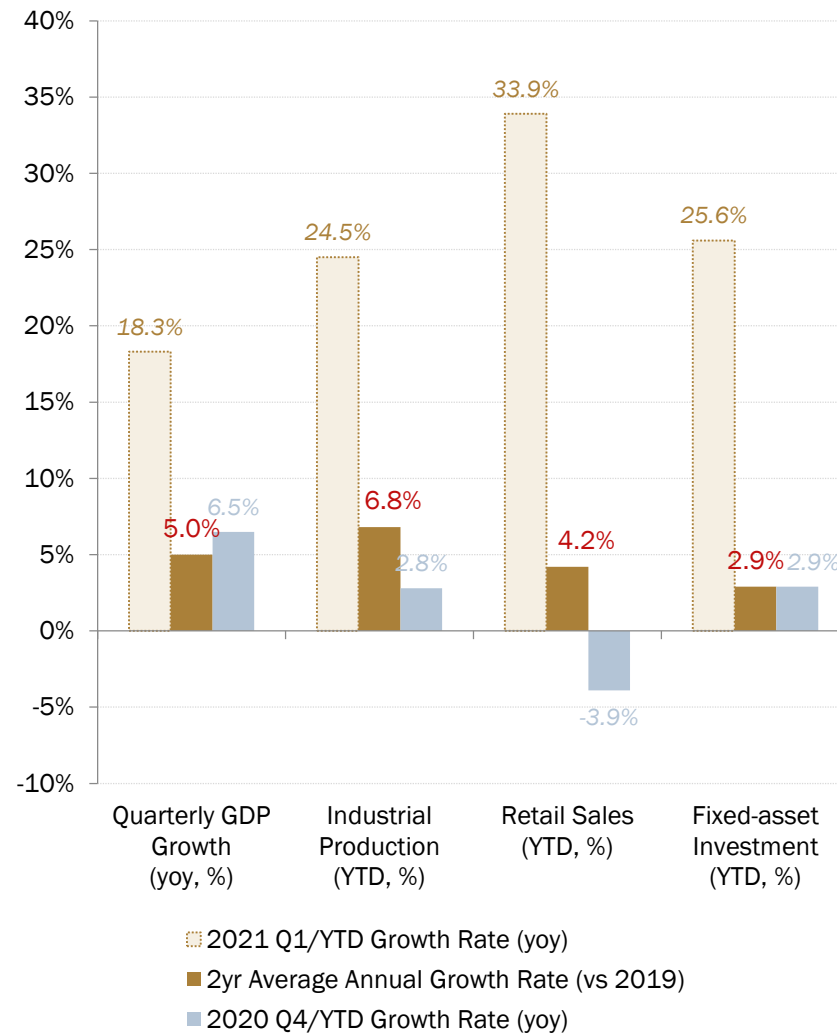
Recovery, Rebalancing and Risks

June 2021



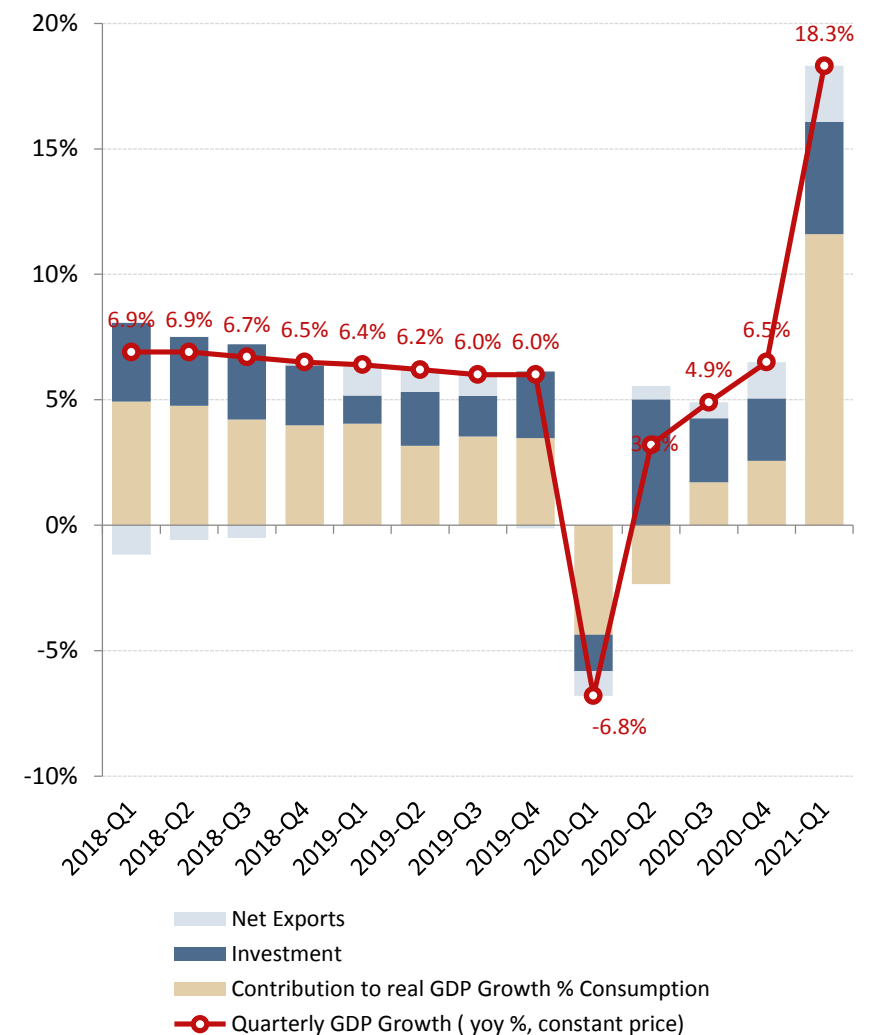
Post-pandemic recovery continued to gain firmer footing in Q1 2021

Double-digit growth illusion unmask broader recovery



Source: WIND, ICBC Standard

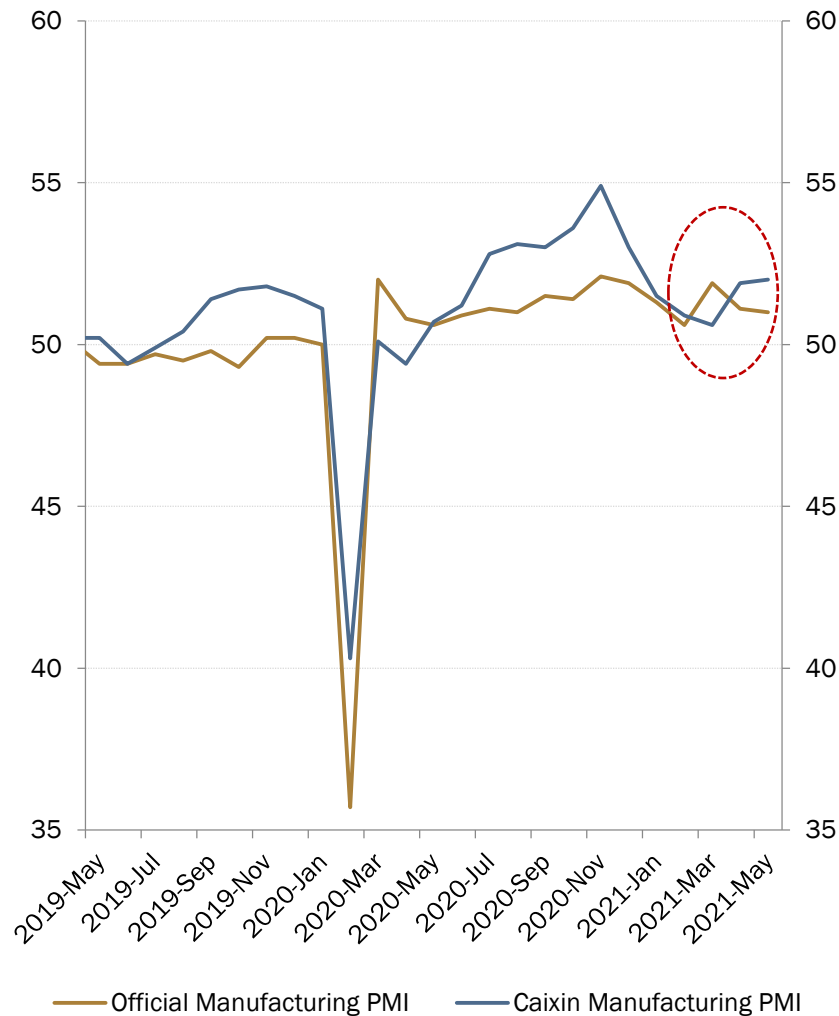
Growth is becoming more balanced and less reliant on public support



Source: WIND, ICBC Standard

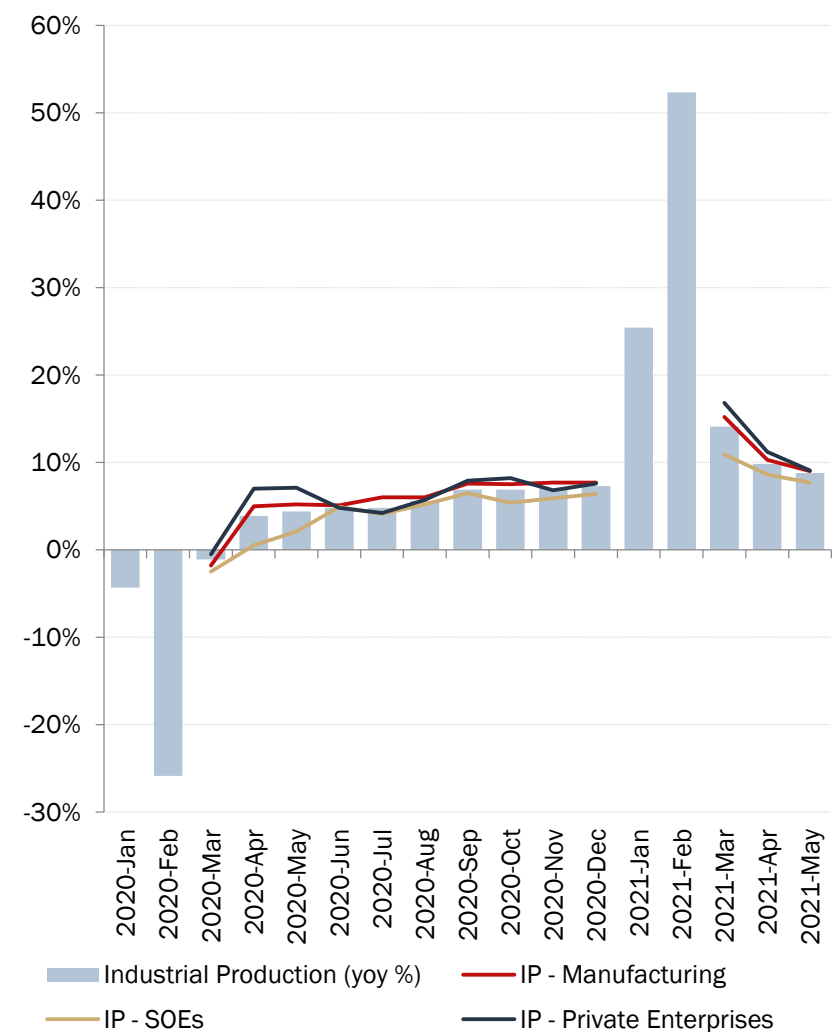
Supply-side recovery still holds up well, though with signs of plateauing

Manufacturing PMIs continue to moderate in Q2 2021



Source: WIND, ICBC Standard

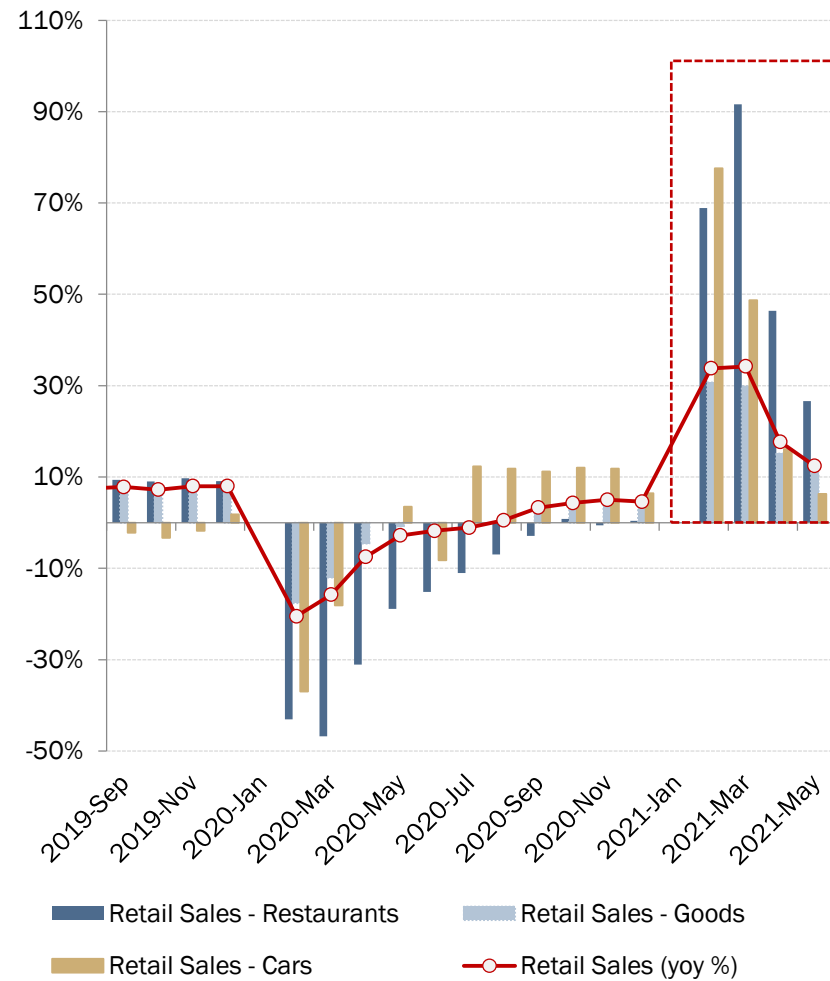
Manufacturing and private firms continue to outperform SOEs



Source: WIND, ICBC Standard

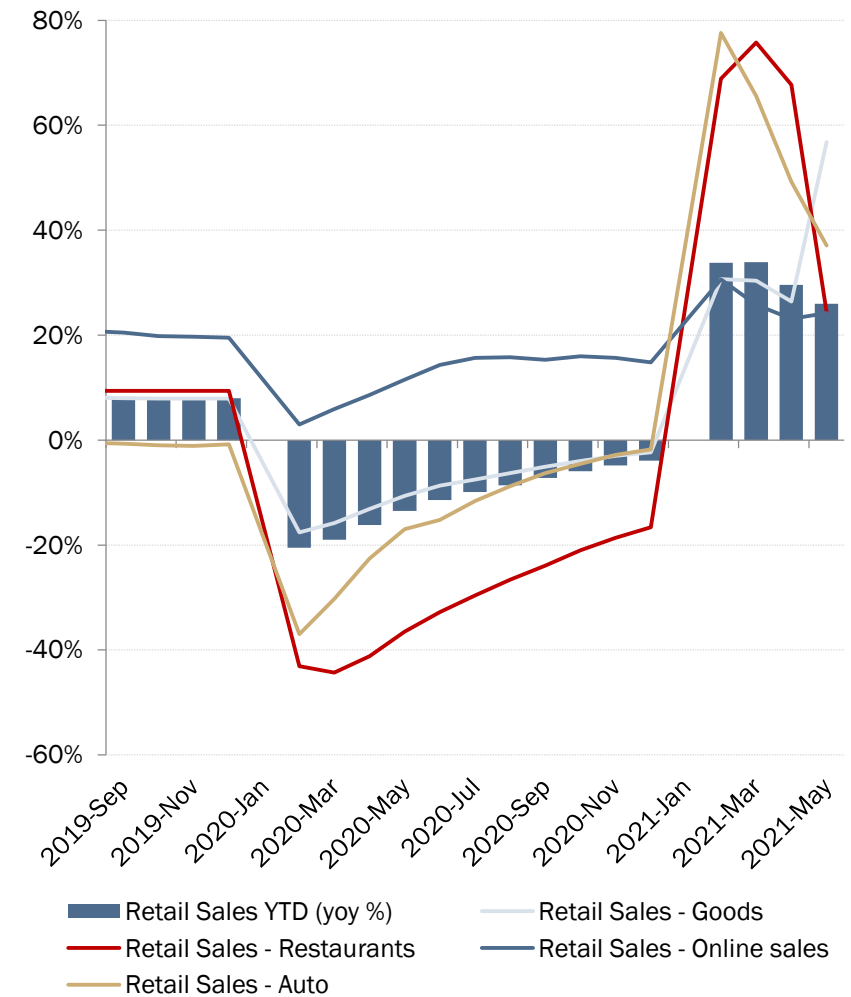
Positive signals of consumption catching up support growth to rebalance

Consumption momentum continued to improve on monthly basis in the first five-month of 2021, albeit the low base-effect distortion



Source: WIND, ICBC Standard

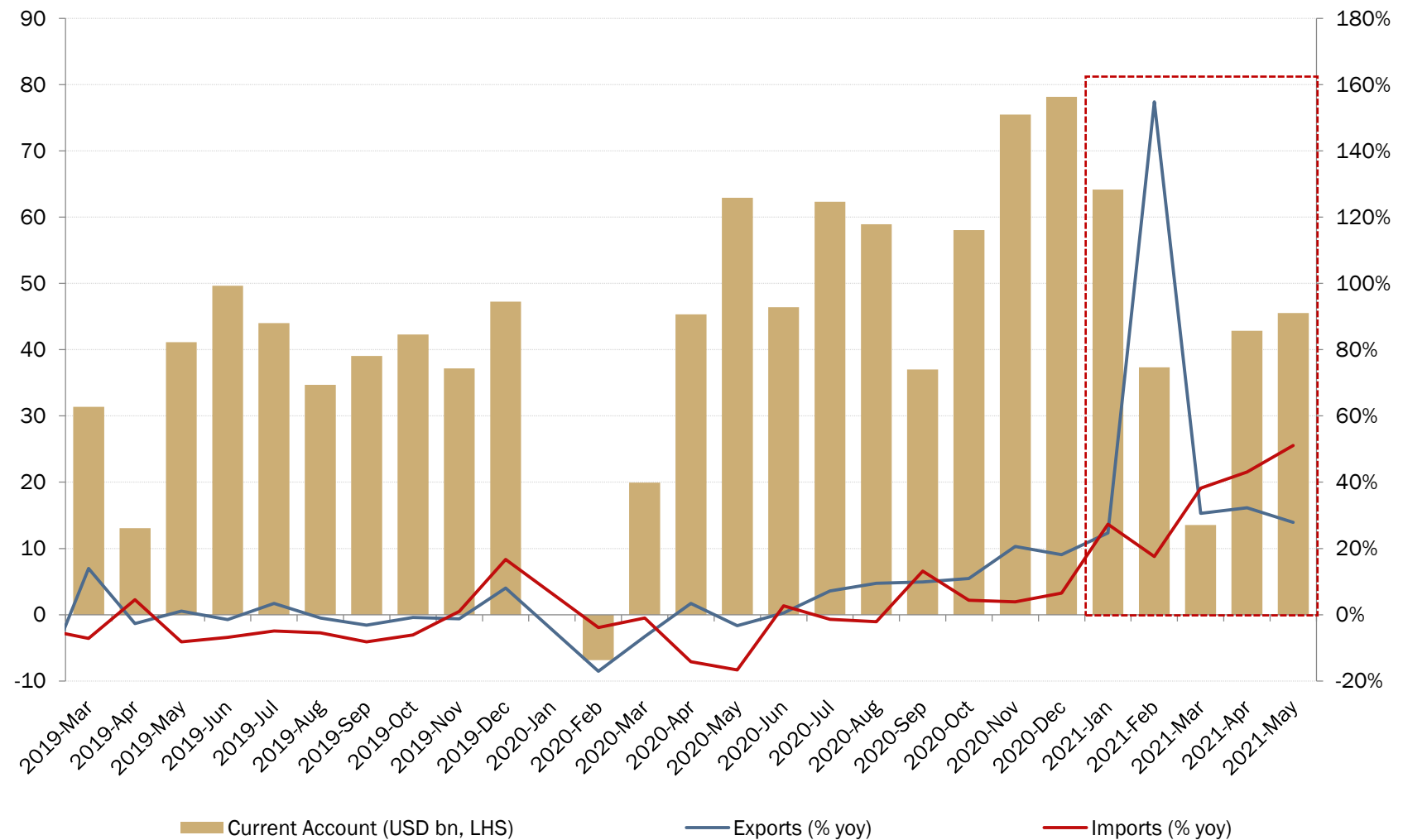
YTD data reflects a broad yet still vulnerable recovery across restaurant and auto sales, while e-commerce sales remain steady



Source: WIND, ICBC Standard

Imports momentum began to pick up, while exports growth turned softer

Recovery in domestic demand and commodity prices will continue to support improvements in imports in the coming months, while exports may continue to expand sequentially given renewed lockdown pressure in other Asian economies but at a slower pace in H2

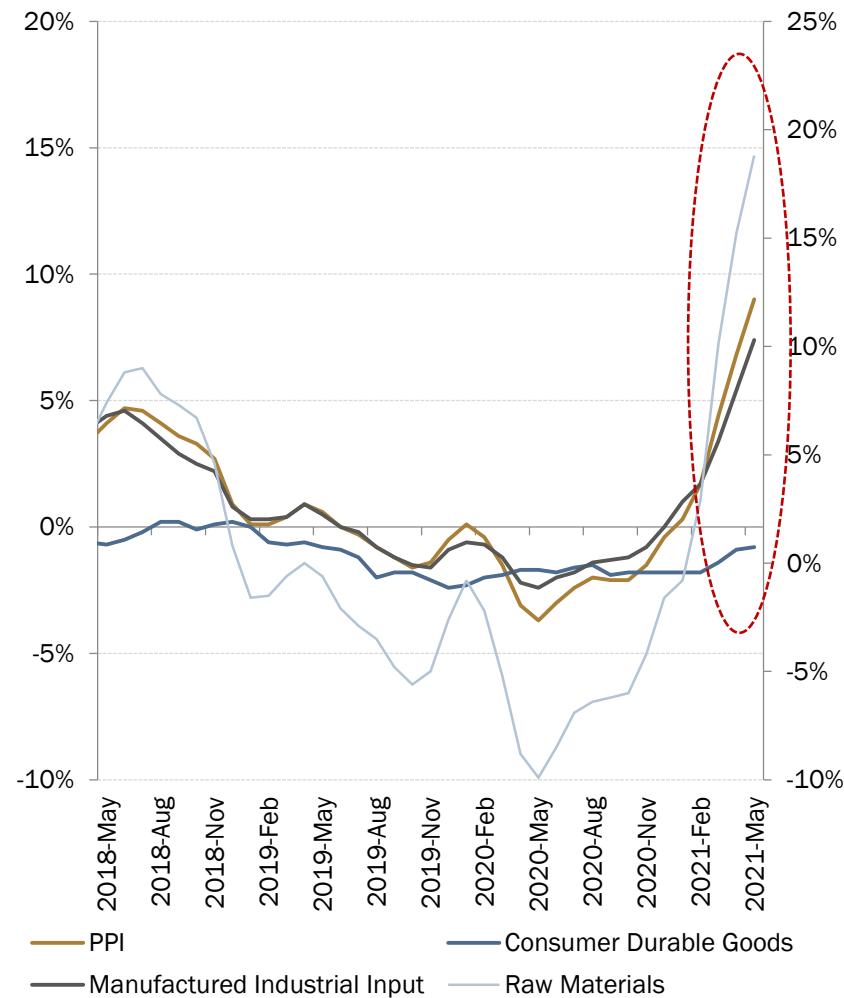


Source: WIND, ICBC Standard

Inflation divergence reflects limited pass-through to consumer prices so far

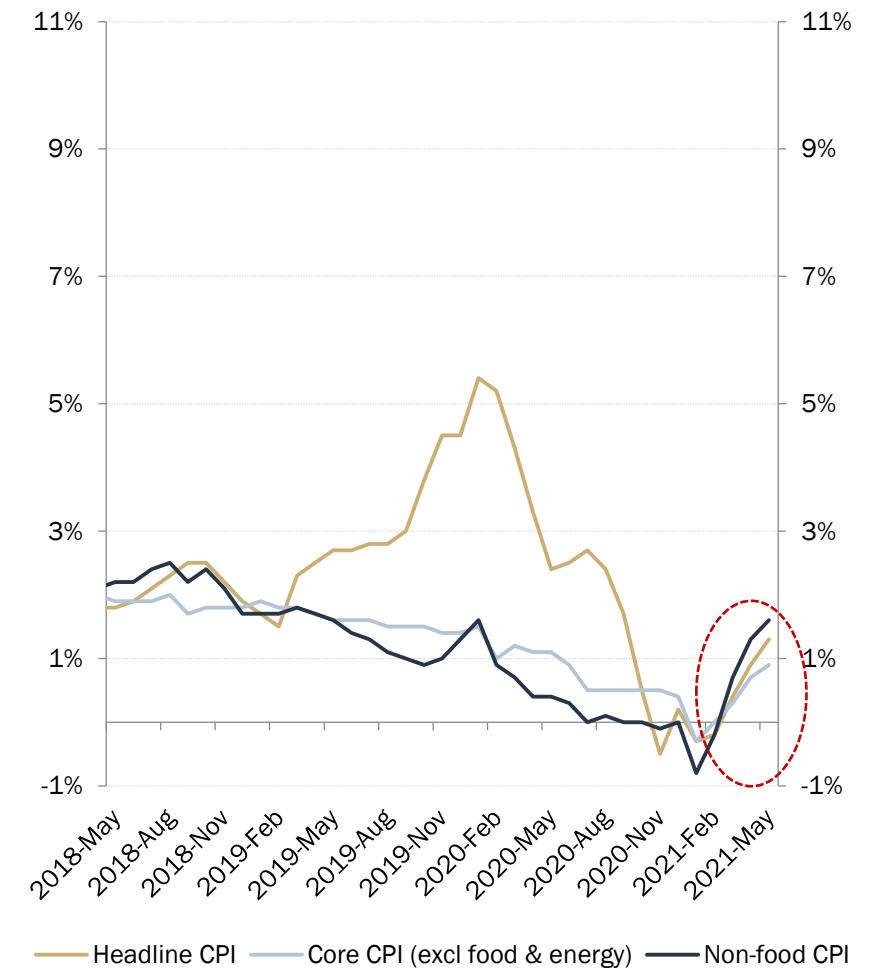
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Surge in global commodity prices and low-base effect have both contributed to sharp rise in headline PPI in April



Source: WIND, ICBC Standard

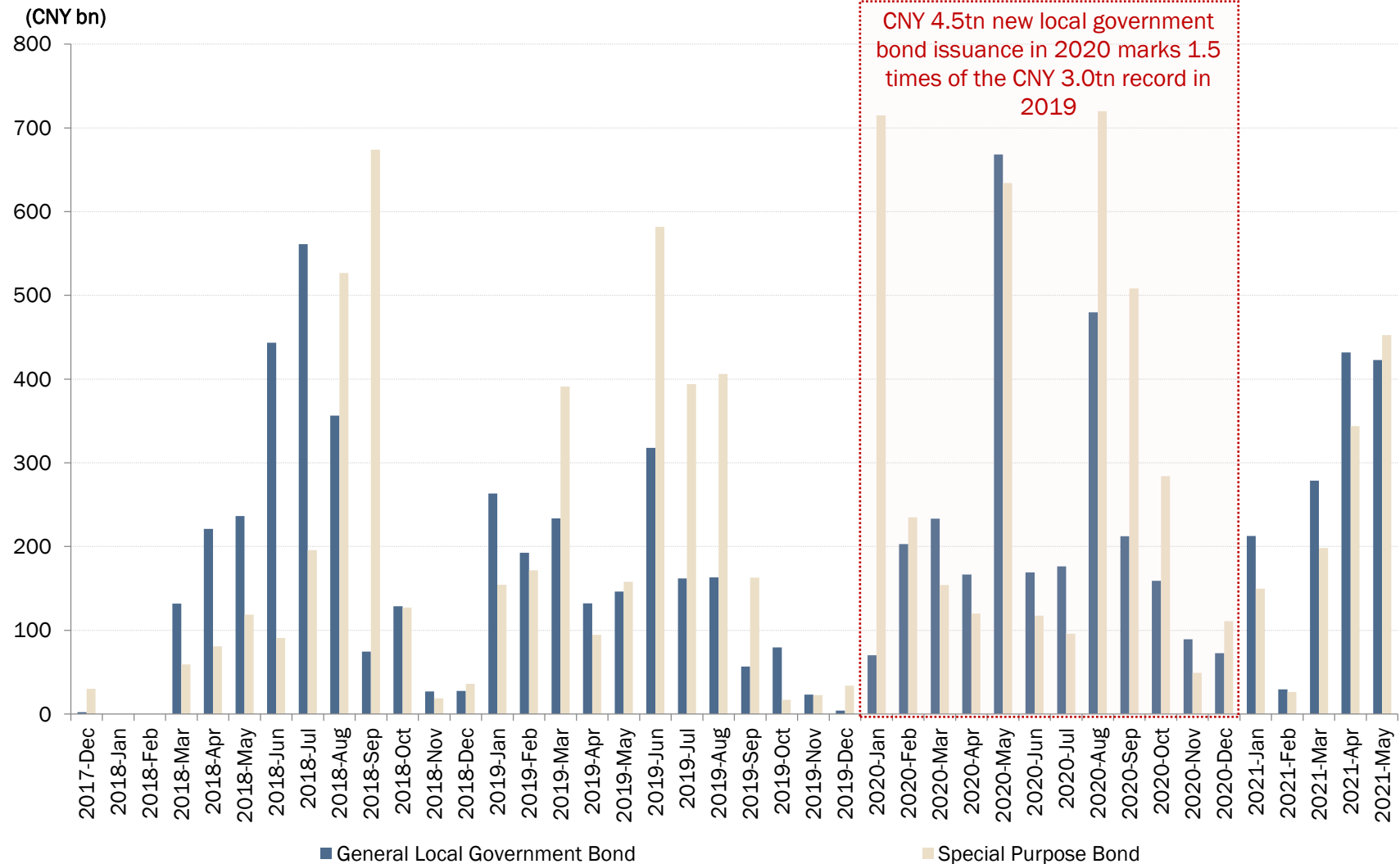
Core CPI remained below 1.0% in the first four months of 2021 and is likely to stay well below 2.0% in H2 2021



Source: WIND, ICBC Standard

Fiscal policy remains accommodative and above pre-pandemic level

Ultra-proactive fiscal policy in 2020 with over CNY 4.5tn of local government bonds new issuance dwarfed records in the past ten years

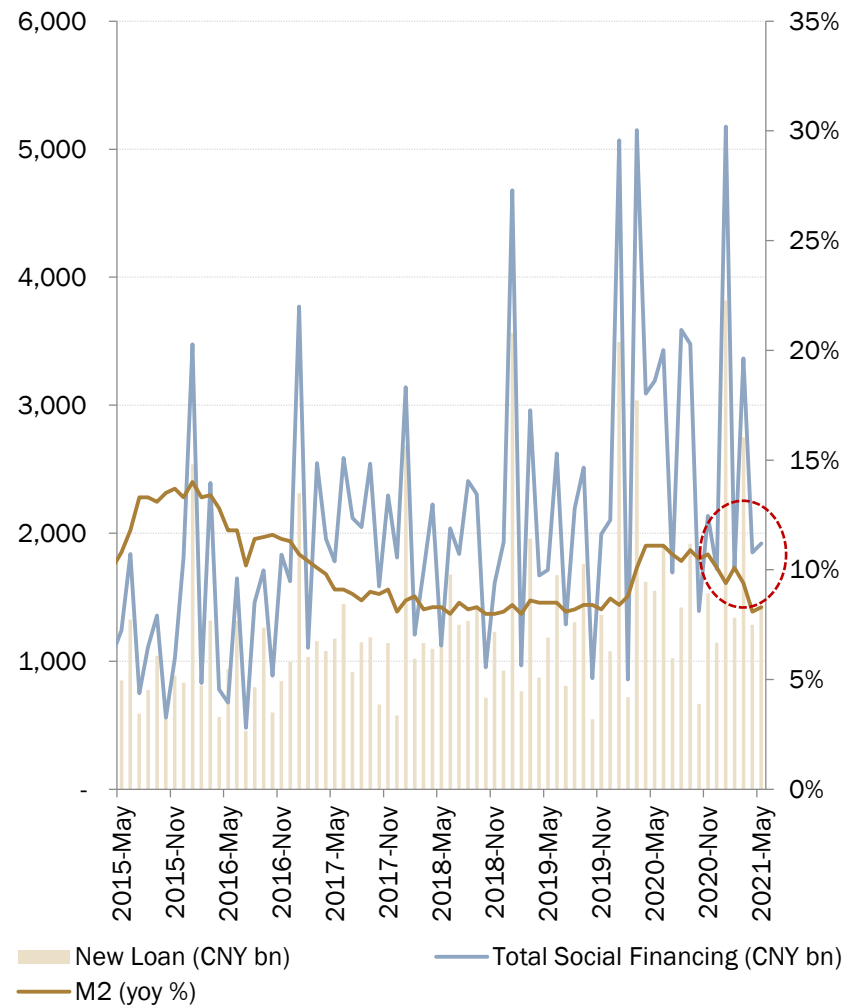


Source: WIND, ICBC Standard

Note: * NPC meeting in May has approved CNY 3.75tn worth of special purpose bond quota for 2020. By the end of H1 2020, more than CNY 2.37tn worth of special purpose bond have already been issued, accounting for nearly 65% of the annual quota.

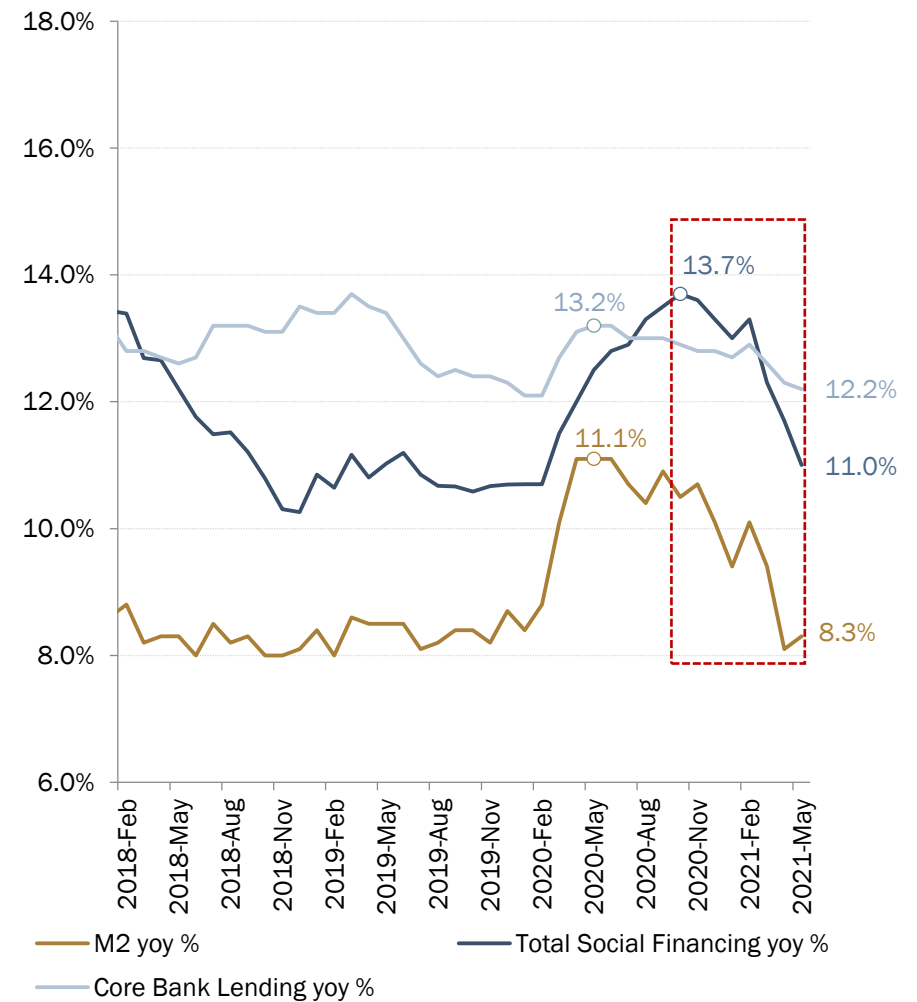
But the PBoC has already gradually tightened credit policy since Feb...

Growth of bank lending and total social financing began to ease since Feb 2021, reflecting tightening bias of credit provision



Source: WIND, ICBC Standard

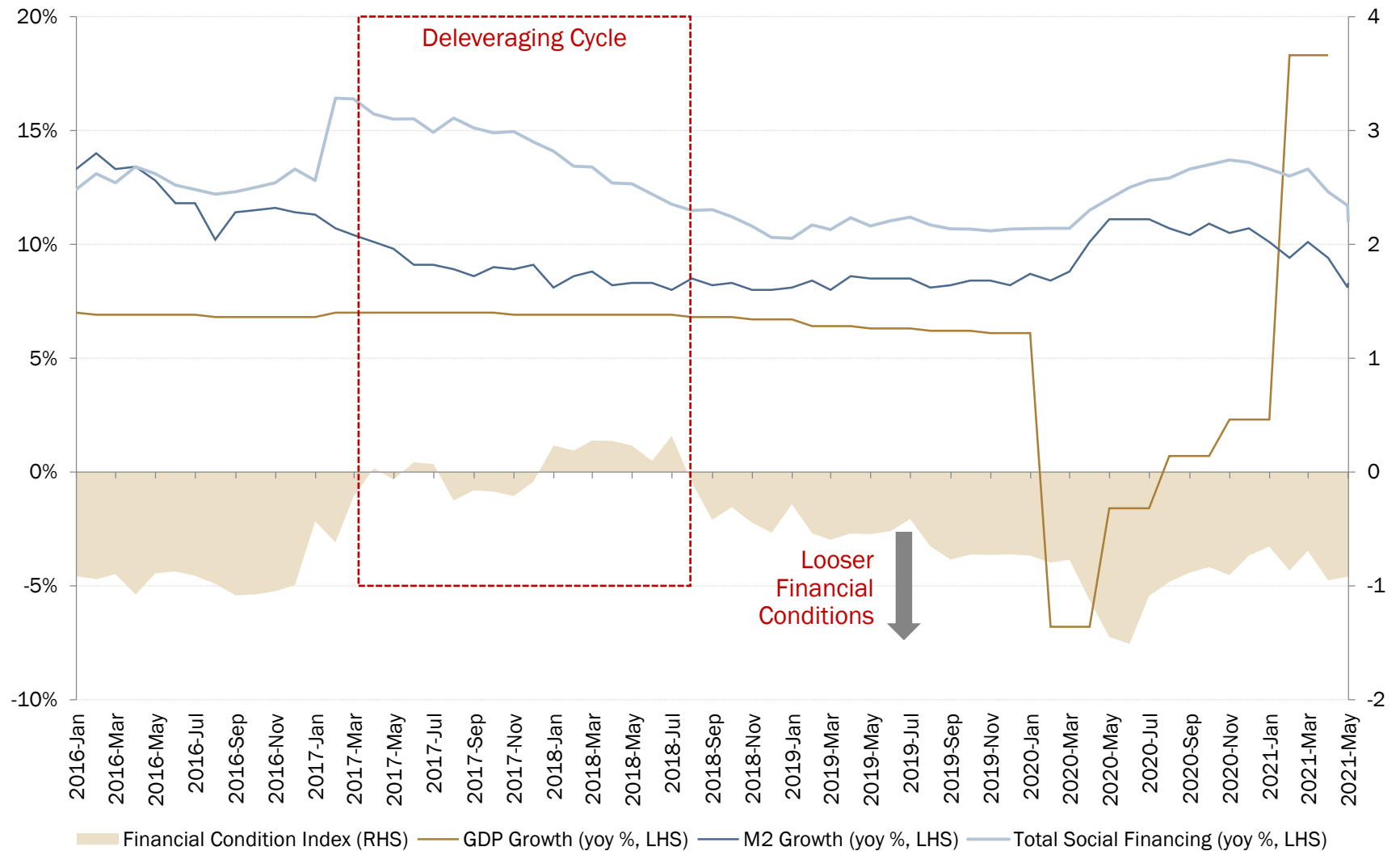
M2 growth has already returned to its pre-pandemic level, coupled with synchronised decline in bank lending and TSF growth



Source: WIND, ICBC Standard

...with continued warnings against risks of re-inflating asset bubbles

Overall financial conditions remain favourable but with tightening bias given repeated regulatory warning against speculative investments

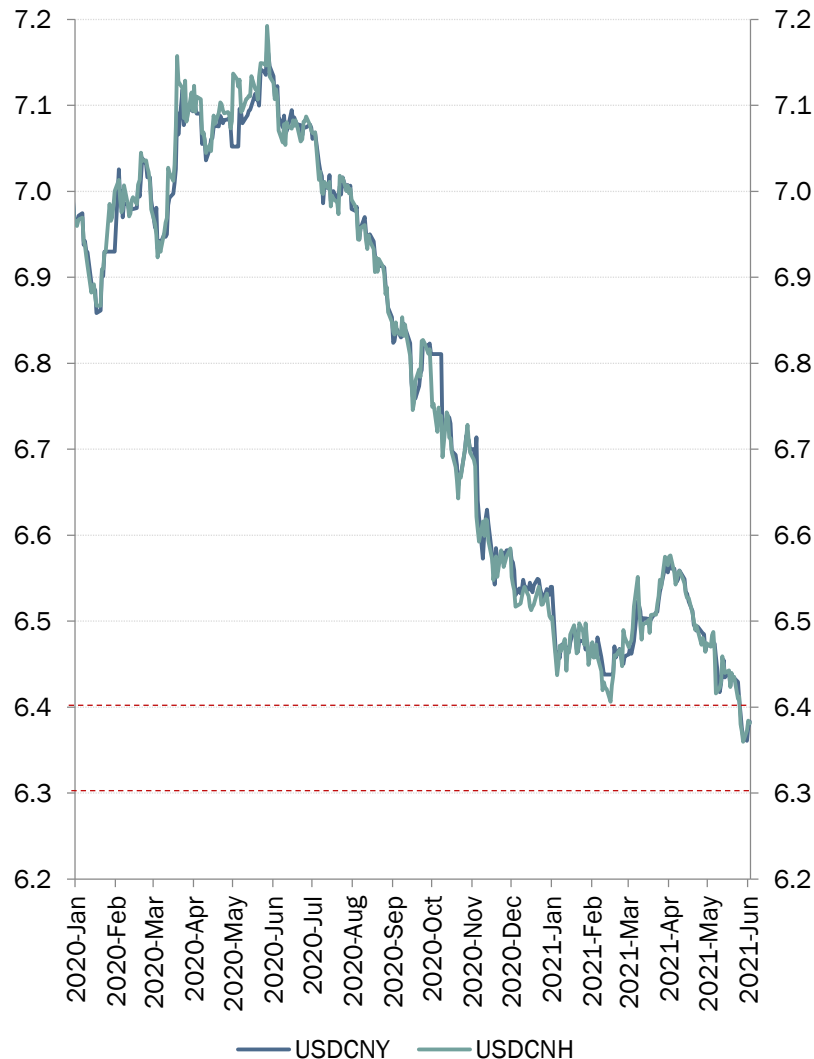


Source: WIND, ICBC Standard

Note: Negative reading of Caixin Financial Condition Index reflects loose financial condition, and positive reading means tighter financial condition in the onshore China market.

“Two-way fluctuation” remains PBoC’s key FX policy focus

Recent yuan rally may have limited strength to break record lows



Source: WIND, ICBC Standard

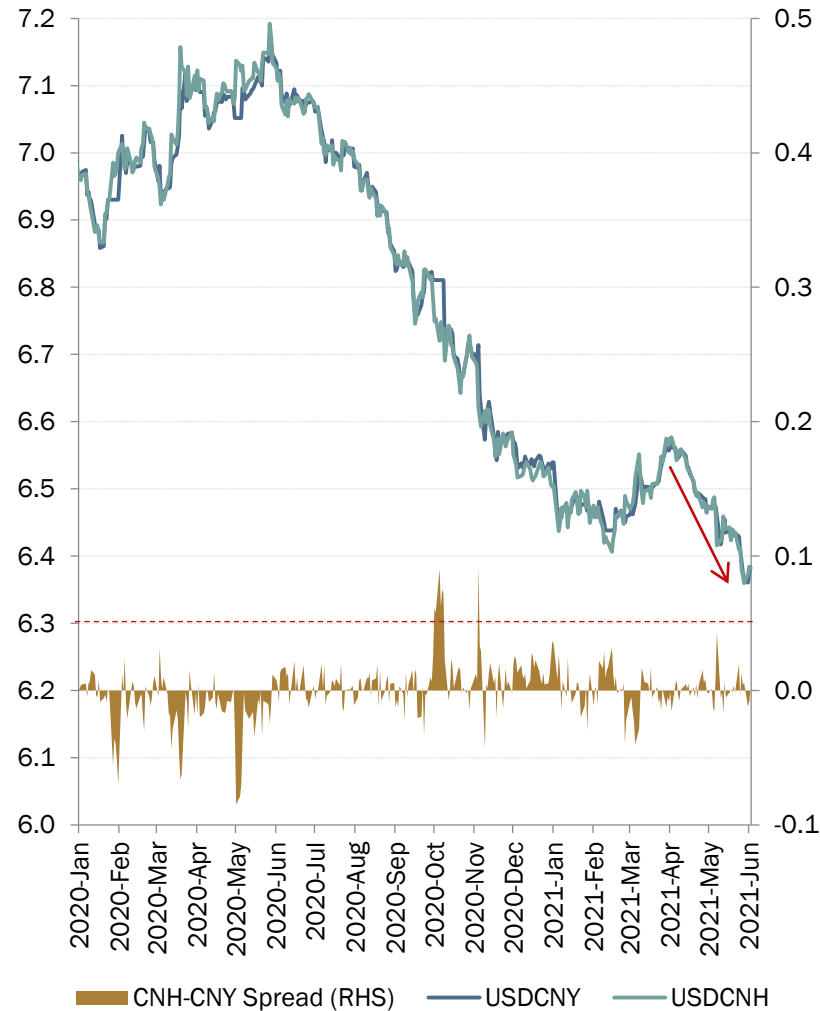
PBoC has frequently adopted macro-prudential tools to steer market expectation since Q4 2020

Date	PBoC Policy Measures/Events
Oct. 2020	Cut FX Risk Reserve Ratio.
Jan. 2021	Increase macro-prudential adjustment coefficient from 0.3 to 0.5 for firms lending to overseas borrowers.
Jan. 2021	Reduce macro-prudential adjustment coefficient from 1.25 to 1.00 for firms borrowing from overseas.
May 2021	Host PBoC FX Standing Committee meeting calling Chinese banks to stay neutral on FX trading.
May 2021	Raise the reserve requirement ratio for FX deposits from 5% to 7% with effective from 15 th June.
Jun. 2021	Grant fresh QDII quotas of c. USD 10bn to allow domestic institutional investors to undertake more outbound investment activities.
Jun. 2021	China Development Bank sells USD 2 billion of 1-year notes on the interbank market, the first onshore dollar bond issuance since 2015. Market sees the move as a signal for state FIs to help absorb onshore USD liquidity.

Source: CFETS, ICBC Standard

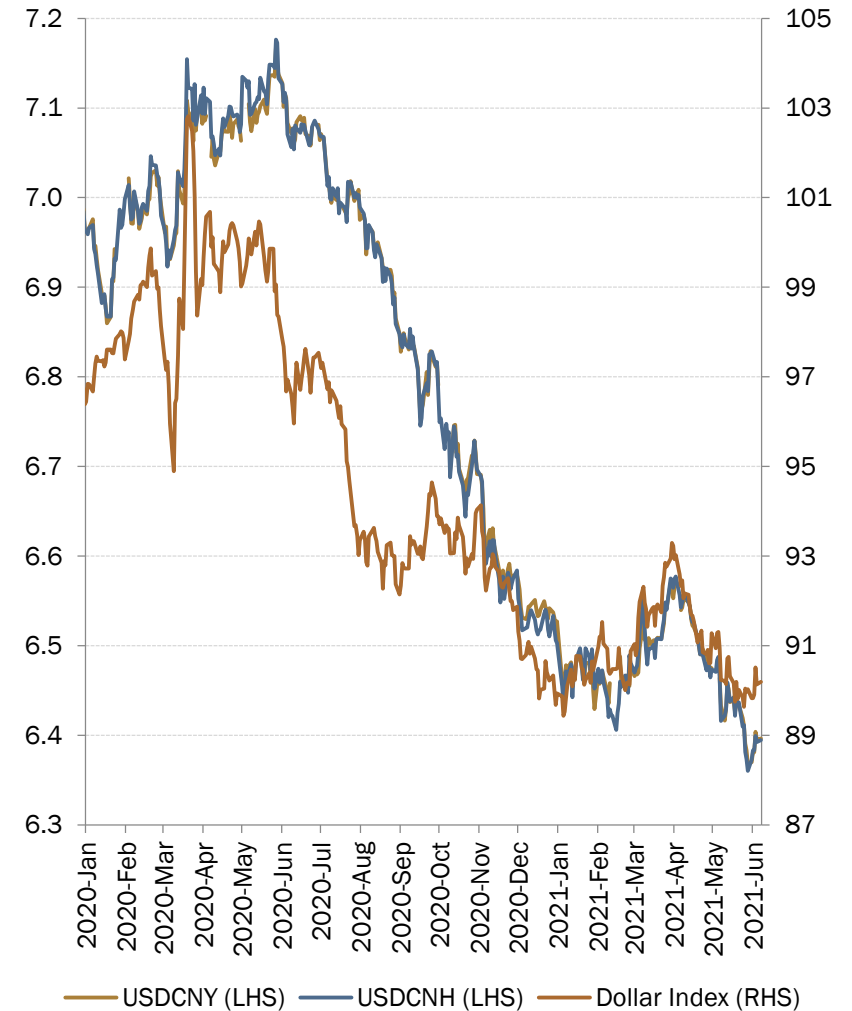
Persistent USD weakness and macro-recovery continue to support CNY

Yuan has appreciated by more than 3% since its peak in April 2021



Source: WIND, ICBC Standard

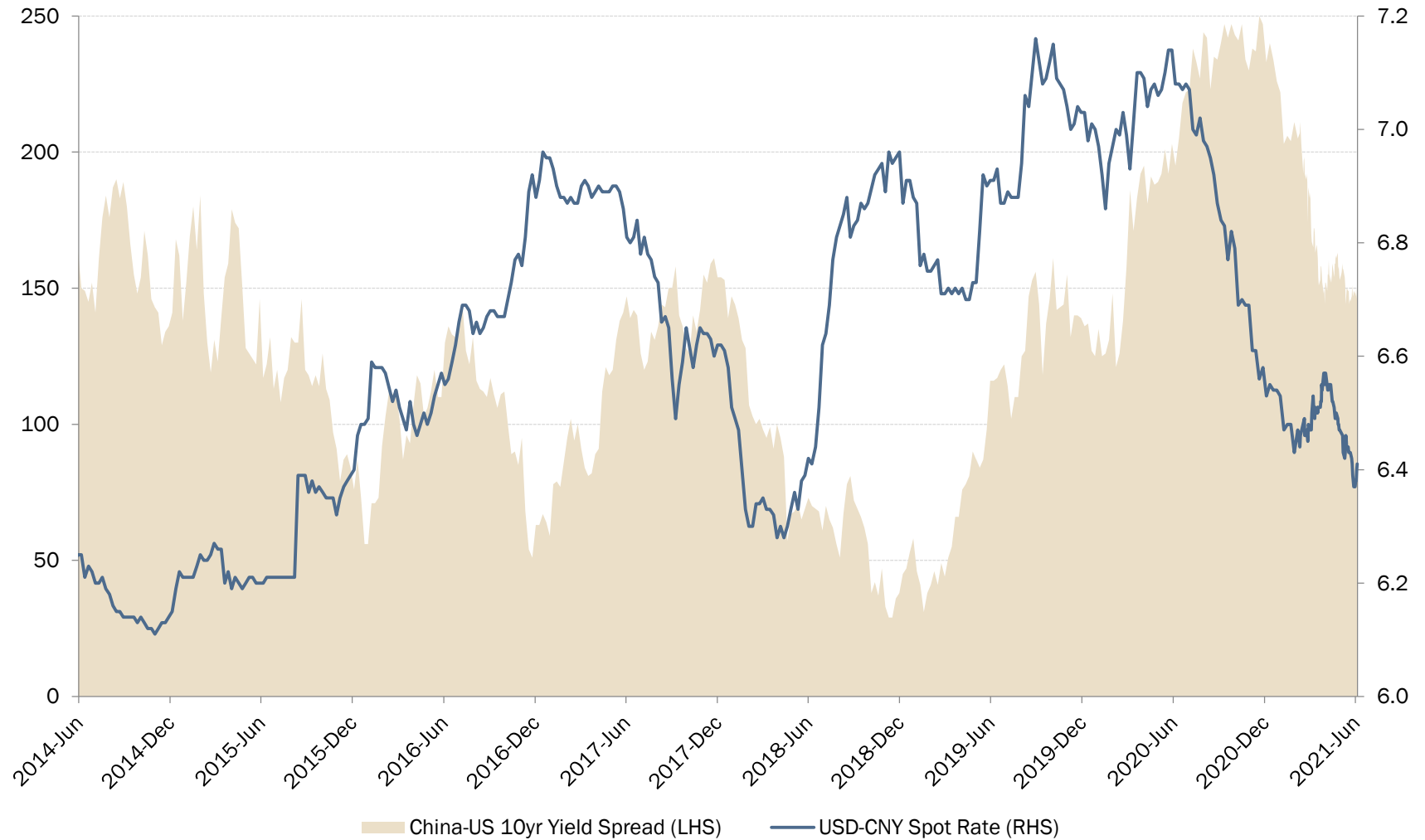
Persistent dollar weakness supported yuan rally since April 2021



Source: Bloomberg, ICBC Standard

Rate differentials between China and US continued to narrow in H1 2021

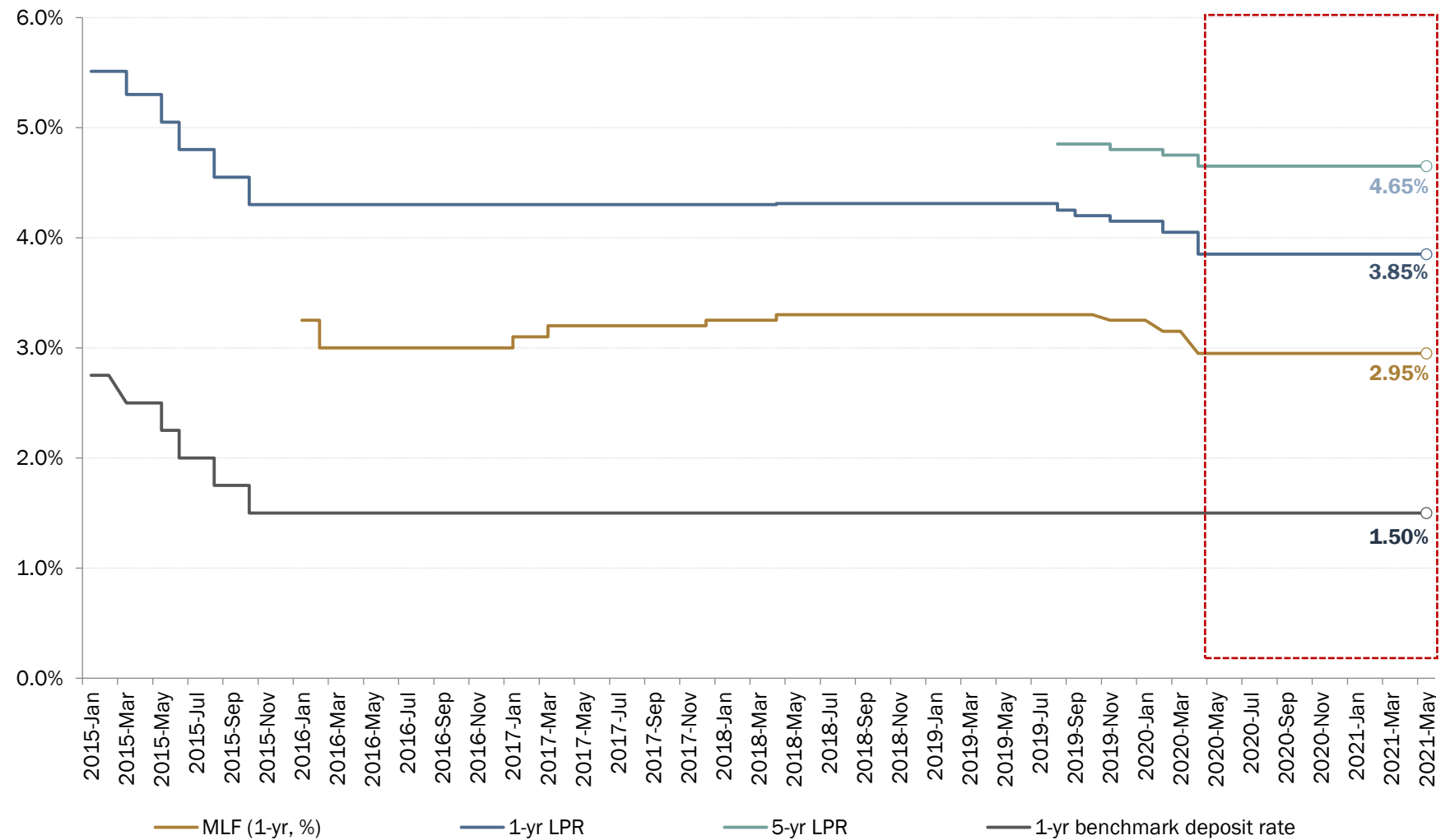
Yield spread between China-US 10yr government bond has narrowed to 150bps in June 2021 from c. 250bps in November 2020



Source: WIND, ICBC Standard

PBoC remains committed to hold benchmark policy rates

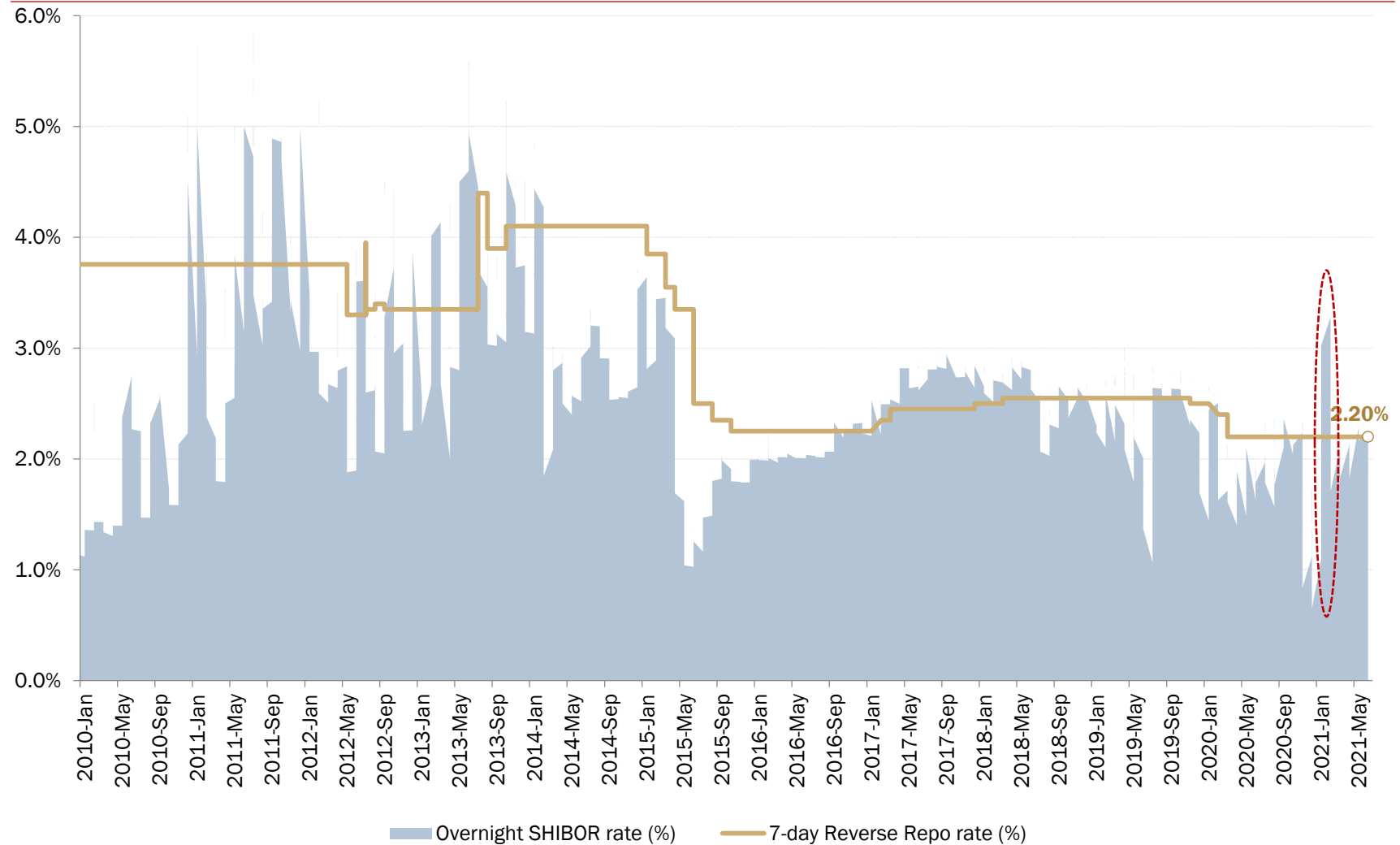
Longer-term benchmark rates remain unchanged since last May and are likely to remain at the same level in H2 2021



Source: WIND, ICBC Standard

Front-end interbank rates closely follow the 7-day OMO rates at c. 2.20%

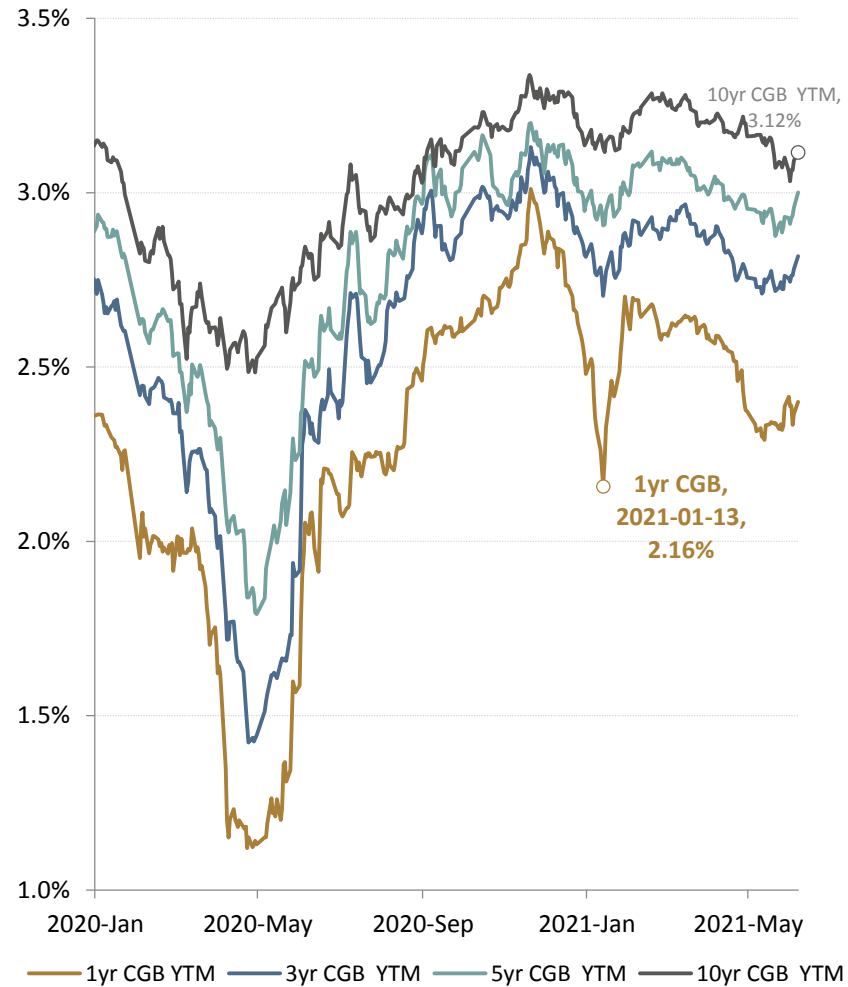
Overnight and 7-day rates went through volatile movements in Jan, but the PBoC remained determined to hold 7-day OMO rates unchanged



Source: WIND, ICBC Standard

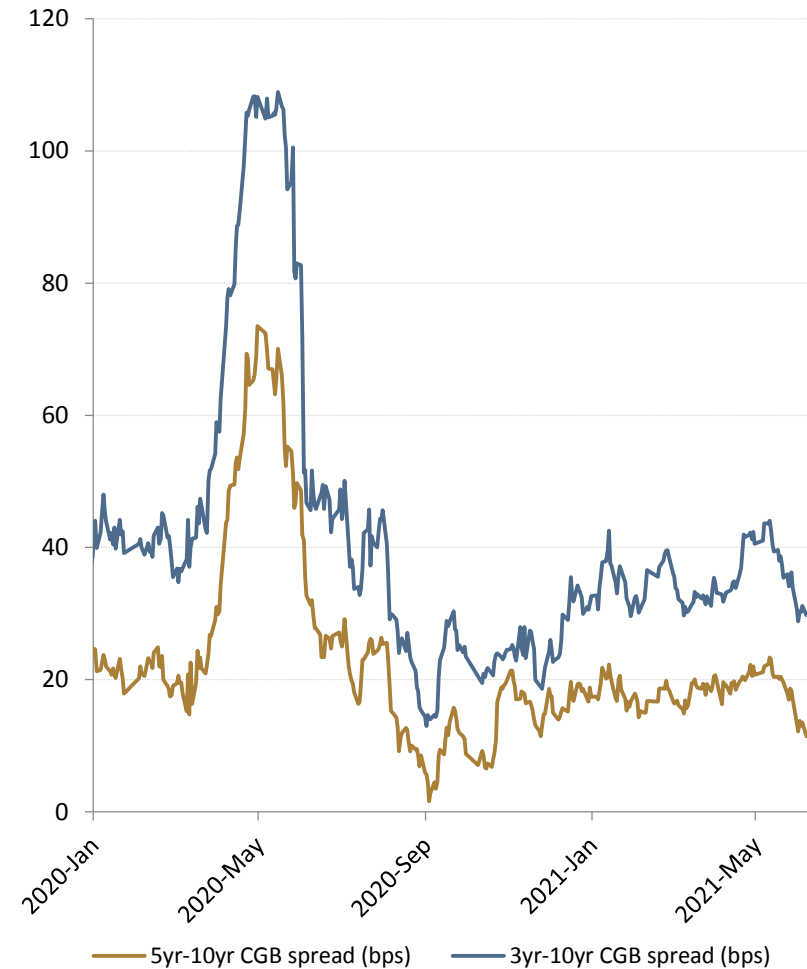
CGB yields are likely to remain range-bound in H2 2021

Yield of 1yr CGB notably bounced back in Jan 2021 due to front-end liquidity squeeze in the interbank system



Source: WIND, ICBC Standard

Yet CGB yields are likely to remain range bound in the near term as markets await further policy clarities on inflation outlook



Source: Bloomberg, ICBC Standard

Appendix I: Employment and environment as key policy focus in 2021

Key economic targets in the Government Work Report: 2021 vs 2020

		2021	2020 "Endeavour to achieve the 13 th FYP target"		
		GWR Targets	Actual Data	GWR Targets	Actual vs Targets
GDP	GDP Target (%)	> 6.0%	2.00% - 4.00% implied growth rate		
	Actual GDP (CNY bn)	107,694.52	101,598.60	--	--
	GDP growth rate (yoy %)	6.0%	2.30%	2.0% - 4.0%	On target
Fiscal	Official Fiscal Deficit (CNY bn)	3,446	3,760	3,760	On target
	Official Fiscal Deficit Ratio (% GDP)	3.2%	3.6%	> 3.6%	On target
	Special Bond Quota (CNY bn)	3,650	3,750	3,750	Broadly on target
	Special Bond Quota (% GDP)	c.3.4%	3.75%	3.75%	
	Special Sovereign Bond (CNY bn)	0	1,000	1,000	On target
	Broad Fiscal Deficit Ratio (% GDP)	c. 6.5% - 7.0%	8.3%	> 8.5%	On target
	Railway Infra-Investment (CNY bn)	--	1000	900	
	Road and Water Transport Infra-Investment (CNY bn)	--		NA	
	Tax Cuts (CNY bn)	Increase VAT free allowance by CNY 50,000 per annum for SMEs	2,600	2,500	On target
	Household Disposable Income Growth (yoy %)	"Same as nominal GDP growth rate" (> 6.0%)	2.10%	"Same as nominal GDP growth rate"	Below target
Social	Urban New Job Creation (mn)	11.00	11.86	9.00	On target
	Unemployment Rate (%)	c. 5.50%	5.20%	6.00%	On target
	Poverty Reduction (mn)	Set up local social welfare enhancement system for low income countries and regions before 2025	5.51 Eliminated extreme poverty	10 estimated ("Eliminate extreme poverty")	On target
	Climate Change Action	3% reduction in energy intensity (Cut energy & carbon intensity by 13.5% and 18.0% respectively before 2025)			New target
	CPI (%)	3.0%	2.5%	3.50%	On target
Monetary	New Loan Growth for SMEs (%)	> 30%	54.8%	> 40%	On target
	Banking Sector CSR Profit Return (CNY tn)	--	1.5	NA	Exceeded the target
	M2 (yoy %)	"Same as nominal GDP growth rate"	10.1%	"Markedly higher than 2019"	On target
	Total Social Financing (yoy %)		13.3%		

Source: WIND, ICBC Standard

Appendix II: Key economic targets in the past Government Work Reports (2018 – 2020)

		2020		2019	2018
GDP	GDP Target (%)	“Endeavour to achieve the 13 th FYP target”		6.0% - 6.5%	6.50%
	Actual GDP (CNY bn)	--		99,086.50	91,928.11
	Previous GDP growth rate (yoy %)	6.10%		6.70%	6.90%
Fiscal	Official Fiscal Deficit (CNY bn)	3,760	↑	2,760	2,380
	Official Fiscal Deficit Ratio (% GDP)	> 3.6%	↑	2.8%	2.6%
	Special Bond Quota (CNY bn)	3,750	↑	2,150	1,350
	Special Bond Quota (% GDP)	3.75%	↑	2.18%	1.47%
	Special Sovereign Bond (CNY bn)	1,000	↑	NA	NA
	Broad Fiscal Deficit Ratio (% GDP)	> 8.5%	↑	5.0%	4.1%
	Railway Infra-Investment (CNY bn)	900	↑	800	732
	Road and Water Transport Infra-Investment (CNY bn)	NA	-	1,800	1,800
	Tax Cuts (CNY bn)	2,500	↑	2,000	1,100
Social	Household Disposable Income Growth (yoy %)	"Same as nominal GDP growth rate"	=	"Same as nominal GDP growth rate"	6.5%
	Urban New Job Creation (mn)	9.0	↓	11.0	11.0
	Unemployment Rate (%)	6.0%	↑	5.5%	5.5%
	Poverty Reduction (mn)	10 estimated ("Eliminate extreme poverty")	=	10	10
Monetary	CPI (%)	3.5%	↑	3.0%	3.0%
	New Loan Growth for SMEs (%)	> 40%	↑	30%	--
	M2 (yoy %)	“Markedly higher than 2019”		"Same as nominal GDP growth rate"	"Reasonable growth"
	Total Social Financing (yoy %)		↑		

Source: WIND, ICBC Standard

Appendix III: “Six guarantees” as Beijing’s Covid-relief policy priorities in H2 2020

Timeline	Policy Measures since end-March (see <i>Appendix for previous measures</i>)	Fiscal Policy	Monetary Policy
Mar.27 (Politburo meeting)	A key Politburo meeting marked Beijing proposal to increase its fiscal deficit to 3.5% as a share of GDP (from a de-facto 3% ceiling) , issue special sovereign debt and allow local governments to sell more infrastructure bonds as part of a package to stabilise the economy. The ramped-up spending on infrastructure investment could be backed by as much as CNY 2.5-2.8 trillion worth of local government special bonds . Beijing is also likely to have to lower its economic growth target for 2020 , down from the original target of around 6% agreed in December 2019.	Y	
Mar.30	The PBOC reduces the interest rate on 7-day reverse repurchase agreements to 2.2% from 2.4% while injecting CNY 50 billion into the banking system. The rate cut was the largest of its sort since 2015.		Y
Mar. 31	The State Council called for lower reserve-requirement ratios for smaller banks, more infrastructure bond issuances by local governments, and other steps including tax exemptions on new-energy vehicle purchases. A State Council meeting pledged another 1 trillion CNY of funding through the central bank’s relending and rediscounting program , a cheaper credit line for small commercial lenders.	Y	Y
Apr. 3 (Politburo meeting)	Politburo leaders in a statement pledged a raft of measures to strengthen the role of the market in land use, capital markets and labour mobility to build a more efficient economy. The Politburo also called for improvements to the country’s stock market infrastructure, faster development of the bond market and actively expanding financial-sector opening., and interest rates reform.	Y	
	PBoC announced cut of targeted Reserve Ratio Requirement (RRR) for smaller banks by 1.0 percentage points in two phases. The targeted RRR cut will release around CNY 400 billion into the banking system.		Y
Apr. 17 (Politburo meeting)	The Politburo for the first time put forward the goal of “six guarantees (六保)” , which includes ensuring residents’ employment, a basic livelihood and market participation, food and energy security, supply chain stability, and grassroots operations. ‘Full-employment and undisrupted functioning of social fabrics’ as well as ‘people’s livelihoods’ have been identified as top priority by the government.	Y	
Apr. 17-20	PBoC cut MLF rate by 20bps to 2.95% from 3.15%, the lowest since 2017, and injected CNY 100bn via 7-day repo. The one-year LPR was subsequently lowered to 3.85% from 4.05%, and the five-year tenor dropped by 10bps to 4.65% down from 4.75%.		Y
Apr. 20	MoF approved another CNY 1tn quota for special purpose bonds to be placed by end-May. NDRC outlined the five-year “New Infrastructure investment plan” worth CNY 10tn from 2020. 24 provinces have submitted CNY 8tn worth of infrastructure investment projects for 2020 so far (see next slide).	Y	
Apr. 21	State Council lowered the bad-loan coverage ratio for medium-small sized banks by 20 bps in phases, to unleash additional credit to support small and micro-sized businesses.		Y

Source: WIND, ICBC Standard

Appendix IV: China's COVID-emergency relief policy package in Q1 2020

Timeline	Policy Measures	Fiscal Policy	Monetary Policy
Feb. 1	Import tariffs exemption for medical materials used in epidemic control until March 31.	Y	
	PBoC strengthened countercyclical adjustments of monetary policy through open market operations. Together with other financial regulators, the PBoC rolled out 30 policy measures to support enterprises.		Y
Feb. 3-4	PBoC added a net CNY 150bn liquidity to the interbank market. The total injection announced was CNY 1.6tn, the largest single-day addition of its kind since 2004.		Y
Feb. 5	State Council announced support for debt financing and insurance for virus-impacted firms, and allowed local government to sell another CNY 848bn of bonds before March.	Y	
Feb. 6	PBoC issued credit support for enterprises heavily affected by the epidemic (small and micro companies and key manufacturing sectors) to borrow at record-low rate of 1.6% through state-owned commercial banks. PBoC also provided CNY 300bn for large banks and selected local banks in Hubei and other severely-hit provinces.		Y
Feb. 9	State Council announced total spending worth CNY 80.55bn as emergency funds to mitigate against COVID-19 related shocks to the economy.	Y	
Feb. 15	Various tax relief measures worth CNY 1tn (or about 1% of GDP), including reductions in employers' required social insurance payments, lower electricity fees and VAT waivers.	Y	
Feb. 17-20	PBoC lowered MLF rate by 10bps to 3.15% from 3.25%, the lowest since 2017, and injected CNY 100bn via 7-day repo. PBoC lowered the benchmark borrowing costs for new corporate and household loans. The one-year LPR was lowered to 4.05% from 4.15%, and the five-year tenor was lowered to 4.75% down from 4.8%.		Y
Mar. 4	7 provinces announced investment projects worth CNY 25tn with CNY 3.5tn to be fully allocated within 2020	Y	
Mar. 12-13	PBoC allows a higher cap of 1.25 on foreign debt, a move aimed at helping smaller and private companies raise more funds overseas. PBoC also cut Reserve Requirement Ratio (RRR) by 0.5 - 1.0 percentage points for banks, freeing up an additional CNY 550bn liquidity to the interbank market to help virus-impacted companies. The RRR for large banks is currently 12.5%. Qualified joint-stock commercial banks would enjoy an additional cut of 100 bps.		Y

Source: WIND, ICBC Standard

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