BOC Research Institute

China's Economic and Financial Outlook

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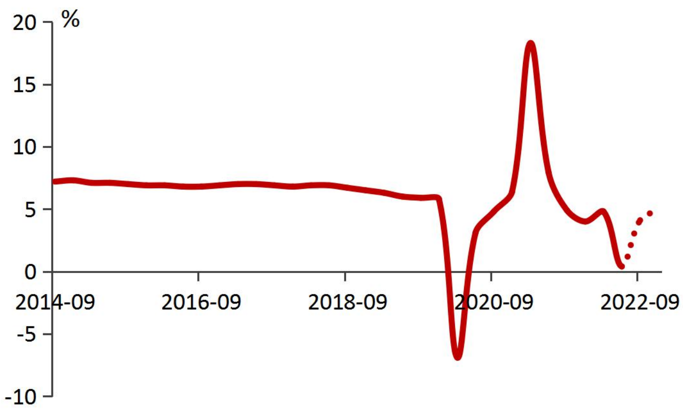
Highlights

- China's economy continued to recover in 2022Q3 as its COVID-19 policy improved continuously, the pro-growth policy worked persistently and the mild inflation gave elbow room for macro policy operations, coupled with strong exports. However, China's economy recovery missed expectations due to weaker domestic demand amid coronavirus resurgence, heatwaves and droughts and property market crunch. China's GDP is expected to have grown by around 3.8% in Q3, a rally of about 3.4 percentage points from Q2.

- Looking forward to Q4, China's exports may weaken and the fallout from COVID-19 will still persist in the country. The recovery of domestic demand depends on the sustained effect of the pro-growth policy and continued improvement in the COVID-19 policy. GDP growth is projected to be about 5% for Q4, and approximately 3.5% for the year.

- The pro-growth policy should focus on stabilizing domestic demand and expectations. It is necessary to balance stable growth and fiscal sustainability and keep boosting the utilization efficiency of funds. The monetary policy will keep the aggregate supply largely stable and strengthen the function of structural policy tools to help industries and businesses tide over difficulties. Investment will play a stronger role in supporting economy recovery and steps will be taken to boost consumers' expectations and willingness to spend. The real estate policy will be optimized on both supply and demand sides to help stabilize the housing market. A more stable, law-based and predictable development environment will be provided.

"Weak Recovery" of China's Economy in 2022Q3



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BOC Research Institute
China Economic and Financial Research Team

Team leader: Chen Weidong

Deputy leader: Zhou Jingtong

Team members: Li Peijia
Liang Jing
Zhao Tingchen
Fan Ruoying
Liang Si
Ye Yindan
Liu Chen
Wu Dan
Qiu Yilin
Liu Peizhong
Wang Jing

Contact: Fan Ruoying

Telephone: 010-66592780

Email: fanruoying@qq.com

Policies need to Balance Growth and Sustainability amid “Weak Economic Recovery”

-- China’s Economic and Financial Outlook (2022Q4)

China’s economy continued to recover in 2022Q3 as its COVID-19 policy improved continuously, the pro-growth policy worked persistently and the mild inflation gave elbow room for macro policy operations, coupled with strong exports. However, China’s recovery missed expectations due to weaker domestic demand amid coronavirus resurgence, heatwaves and droughts and property market crunch. China’s GDP is expected to have grown by around 3.8% in Q3, a rally of about 3.4 percentage points from Q2. Looking forward to Q4, China’s exports may weaken and the fallout from COVID-19 will still persist in the country. The recovery of domestic demand depends on the sustained effect of the pro-growth policy and continued improvement in the COVID-19 policy. GDP growth is projected to be about 5% for Q4, and approximately 3.5% for the year. Going forward, the pro-growth policy should focus on stabilizing domestic demand and expectations. It is necessary to balance stable growth and fiscal sustainability and keep boosting the utilization efficiency of funds. The monetary policy should keep the aggregate supply largely stable and structural policy tools should function more effectively to help industries and businesses tide over difficulties. Investment will play a stronger role as the last resort while steps will be taken to boost consumers’ expectations and willingness to spend. The real estate policy will be optimized on both supply and demand sides to help stabilize the housing market. A more stable, law-based and predictable development environment will be provided.

I. 2022Q3 Economic Review and Q4 Outlook

I.1 Economic review in 2022Q3

First, the pro-growth policy and strong foreign demand were major drivers of economic recovery. The pro-growth policy kept strengthening. The State Council rolled out 19 follow-up policy measures at its executive meeting, as an extension of its earlier stimulus package to stabilize the economy. Increased fiscal support and the use of policy and development financial instruments will accelerate the growth of infrastructure investment. The policy to facilitate struggling companies has worked effectively to restart business activity and boost the resilience of manufacturing investment. **Exports maintained rapid growth.** First, overseas demand thrived as China’s major trade partners experienced rapid economic growth in 2022H1. Second, the earlier backlog of orders was a continued driver of growth; in particular, the “rush effect” in the Yangtze River Delta continued into July. Third, the global supply chains continued to recover from disruptions. Fourth, the price effect was a strong support.

Second, inflation was generally moderate and controlled. Since 2022 began, there has been a sharp contrast between China’s moderate inflation and scorching inflation in many other economies. On the one hand, China’s fiscal and monetary policies have been relatively restrained since the onset of COVID-19 to avoid a flood of stimulus, thus curbing the source of inflation. Also, the Chinese government took steps to ensure undisrupted supply at stable prices to tackle imported inflationary pressure from soaring commodity prices, stabilizing the key commodity markets such as energy and food in a timely manner. On the other hand, food has a larger weight than energy in China's CPI basket. As a result, the surging prices of energy and other commodities did not contribute as much to CPI increase as in the United States. The moderate and controlled price levels in China have left sufficient elbow room for macro-policies to cope with the downward economic pressure.

Third, subdued consumer demand was a key drag on economic recovery. In Q3, China's economy performed better on the supply side than on the demand side. Despite the heatwaves, droughts and power rationing in some parts of the country, their impact on industrial activity was generally under control. On the contrary, sluggish domestic demand came as the primary cause of weaker-than-expected economic recovery. The weak recovery of consumer demand was attributable mainly to the following factors: **First, COVID-19 resurgence led to slower growth of household income and closure of consumer venues. Thus the consumer market recovery was sluggish.** On the one hand, the trend of consumption downgrade has emerged. On the other hand, the recovery of service consumption was interrupted by coronavirus outbreaks many times. **Second, the real estate market continued to slump, and market expectations and confidence have not been effectively reversed.** Authorities and local governments have implemented a series of easing policies, such as lowering mortgage rates, lowering the eligibility criteria for homebuyers and relaxing purchase restrictions, but the housing market expectations have not improved significantly. In Q3, the incidents related to "incomplete buildings" went rampant across the country, undercutting the already-teetering confidence in property market. On the whole, the real estate market is still in the bottom.

Fourth, market players became less optimistic about their future development, showing some balance sheet contraction. In the household sector, first, income growth moderated amid growing uncertainty in employment and the broader economy. Flexible employees and self-employed individuals suffered a significant pandemic-induced decline in income. Employees in sectors hit hard by the virus also saw a marked contraction in wages. **Second, the COVID-19 resurgence led to sporadic lockdowns and shrinking activity, which dented consumer confidence.** The Consumer Confidence Index has receded sharply since March, staying below 90 for four consecutive months. The index was 87.9 in July, 31.9 points lower than the end of last year. In addition, the COVID-19 shocks and changing expectations have led to an increasing awareness of risk prevention and willingness to save in the household sector. **Third, the household-sector leverage slowed down.** On the one hand, household assets were at risk of contraction amid property market gloom, financial market turmoil and income slowdown. On the other hand, households became less willing to borrow more and some even "rushed to pay off home mortgages early".

In the business sector, first, industrial enterprises showed mixed growth in value added. Automobile makers saw both demand and supply booming, while manufacturers in food, beverages, textile, computer and pharmaceuticals industries were losing steam due to pent-up demand. **Second, micro, small and medium-sized businesses were significantly strained.** Given the weak demand in coronavirus resurgence, SMEs are less resilient to risks and more pessimistic about the future. **Third, enterprises were reluctant to seek financing.** The business-sector leverage rose to 141.8% in 2022Q2 from 134.9% in 2021, mainly due to strong policy support but slowing growth of value added. Businesses had limited willingness to take on financing, showing mild overall expansion in debts.

Contrary to the unwillingness to borrow more in the household and business sectors, the government sector increased its leverage ratio markedly as the fiscal policy support stepped up and special local government bonds were issued at a faster pace, further widening the gap between public revenue and expenditure.

I.2 Economic Forecast for 2022Q4

1. Consumption will recover mildly under lingering fallout from COVID-19.

In Q4, consumption is likely to remain in a recovery backed by policy support. First, the COVID-19 prevention and control measures will likely be further optimized to set the stage for service consumption and offline consumption to recover. In particular, the consumer spending in tourism, cultural and entertainment services has been dented significantly by coronavirus in 2022. The suppressed demand for tourism and entertainment is expected to be released by the end of the year. Second, automobile consumption is likely to remain a major driver of consumption recovery. Sales of new energy vehicles will maintain fast growth. Third, the prior-year base is low. However, there will also be some unfavorable factors for recovery of consumption in Q4. The winter will come with a higher risk of COVID-19 resurgence, which may disrupt the recovery of consumption. It will take some time for the improved employment and income to boost expectations and then spark a rebound in consumption. On the whole, consumption is expected to increase by around 5.5% in Q4 and about 2.2% for the year.

2. Investment growth will recover slowly, still driven principally by infrastructure investment.

In Q4, investment will remain divided and recover slowly. Investment in infrastructure will partially offset the pressure from weakened investment in manufacturing and subdued investment in real estate. **First, infrastructure investment is expected to remain in the fast lane.** From the perspective of funding, infrastructure projects receive stronger support from fiscal and financial policies, including the policy and development financial instruments and unused quota of special local government bonds. From the perspective of projects, there is a sufficient reserves for infrastructure projects. **Second, the investment in manufacturing may slow down.** Weak domestic demand and pent-up foreign demand will suppress manufacturers' willingness to invest. The slowing growth of corporate earnings will undermine manufacturers' ability to invest. These factors, coupled with the heavy pressure of de-stocking, will move the manufacturing investment cycle into the downturn phase. **Third, real estate investment is unlikely to improve significantly.** Property market sales are still cooling. As developers are still cash-strapped and reluctant to acquire land, real estate investment will remain in the downturn through Q4. Overall investment is expected to grow by around 5.2% in Q4 and 6% for the year. Investment in real estate will drop by about 5% in Q4 and approximately 7.2% in annual terms.

3. Exports are unlikely to remain on fast track due to softening foreign demand and receding commodity prices.

With developed economies' growth slowing down, commodity prices falling back and recovery of orders losing steam, it is unlikely to sustain fast growth of exports into the future. **First,** as foreign demand may further soften amid a rising risk of global stagflation, China's exports momentum will weaken. **Second, the retreat in commodity prices will dent the nominal growth rate of exports.** Alongside the non-energy commodity price index pulled back from its April peak and the persistent rate hikes in major economies to tame inflation,the decline in commodity prices will gradually pass on to exports and weaken the price support for export growth. **Third, the backlog effect of orders is fading.** The new export orders index began to move lower after reaching 49.5 in June, and hit 48.1 in August, staying below the boom-or-bust line. Overall, export growth is expected to slow to about 5% in Q4, with a projected annual growth of about 11.1%.

4. The pro-growth policy stokes steady growth of industrial activity, while the pandemic and real estate crunch dents the recovery of services.

Looking forward to Q4, the industrial production will keep rebounding on the supply side. **First, adverse effects of coronavirus outbreaks and heatwaves are fading. Second, the pro-industry economic policy is persistently implemented.** Recently, a number of provinces and cities have clearly defined the development tasks for consolidating industrial-sector growth by the end of the year. The "specialization, refinement, differentiation and innovation" enterprises will further unleash their strengths in shoring up "weaker links" of the industry and supply chains. **Third, the prior-year base is low.** The growth of industrial value added value averaged 3.9% in 2021Q4, down 1 percentage point from a quarter ago. However, the continued property gloom and weaker export demand will weigh on the growth of industrial production. Overall, the industrial value added is expected to grow by around 5.8% in Q4 and about 4.3% for the year.

Services still have significant upside potential. The weaker consumption expectations have not yet taken hold as a drag on services. With the improvement of the pandemic situation in China in the future, there is still room for improvement and optimization. However, the service-sector recovery will be dampened by COVID-19. From the perspective of market expectations, the confidence of service market players is repeatedly disturbed by the pandemic. Overall, the service value added is projected to grow by about 4% in Q4, and approximately 2.7% for the year.

5. Inflationary pressure is generally moderate and controlled, and "the negative spread" between PPI and CPI is likely to widen.

Inflation in China will be generally moderate and tamed in Q4, but the structural characteristics of price movements are worth noting. **First, CPI and PPI inflation will diverge.** A further rebound in pork prices will put a floor under food prices. But considering the relatively mild pig cycle and ebbing carryover effect, the CPI inflation is expected not to go significantly hotter in Q4. With mounting downside risk to global economy and ongoing monetary tightening in major economies, commodity prices are losing further momentum. PPI growth is expected to further soften or even move into the negative territory. The divergence between CPI and PPI inflation will widen "the negative spread" in between. **Second, core CPI and CPI will diverge.** The CPI inflation is going hotter mainly due to food prices, and will remain so for a certain period to come. Given the fragile footing of economic recovery and still-weak domestic demand, however, the core CPI excluding food and energy will stay low. CPI and PPI are expected to increase by 2.8% and -2% in Q4, and by 2.2% and 4% in annual terms, respectively.

II. 2022Q3 Financial Review and Q4 Outlook

II.1 Economic review in 2022Q3

Financial policies gave equal weight to volume and price in Q3 in an all-out effort to stabilize the macro-economy. At the aggregate level, the Executive Meeting of the State Council launched two rounds of policy and development financial instruments to support major projects, and introduced special relending and interest subsidies to support the upgrading of equipment in selected areas, so as to continuously boost market demand. At the price level, PBOC announced to lower the one-year MLF and the one-year and five-year LPRs to further bring down lending rates and corporate financing costs. These policies have achieved certain results. The money supply and aggregate financing to the real economy began to pick up and various interest rates declined markedly. In particular, lending rates have fallen to all-time lows. However, China's financial markets became more volatile due to COVID-19 resurgence, hot global inflation, USD liquidity reversal and extensive slump in non-USD currencies. With the stock market shaky and tumbling and the USD/RMB exchange rate exceeding "7", property developers were still at a high debt risk.

1.The growth of money supply and aggregate financing picked up slightly, with stronger funding demand from the real economy.

From January to August, new aggregate financing to the real economy totaled RMB24.19 trillion, an increase of RMB2.33 trillion year-on-year (Figure 15). **RMB loans and government bonds were the main contributors to year-on-year increase in aggregate finance.** New RMB loans increased by RMB261.1 billion year-on-year, which was related to the stronger corporate willingness to take on financing as the pandemic eased in Q3. In particular, new medium- and long-term corporate loans rose by RMB213.8 billion in August, the second biggest monthly gain in 2022 to date (next only to the June level). **Equity financing growth accelerated modestly year-on-year.** The new domestic equity financing of non-financial enterprises totaled RMB737 billion, an increase of RMB34.7 billion year-on-year, which was attributable to the accelerated listing of many new economic entities thanks to streamlined IPO procedures. **The contraction in off-balance-sheet financing eased.** Off-balance-sheet financing (trust loans, entrusted loans and undiscounted bank acceptances) decreased by RMB385.7 billion, compared with a decline of RMB1.35 trillion recorded for the same period of last year.

The credit structure continued to improve to increase support for key fields and weaker links. First, the balance of inclusive loans to micro and small businesses, industrial loans and lending to other key sectors kept growing fast. At the end of 2022Q2, the balance of inclusive loans to micro and small businesses, green loans and industrial loans grew by 23.8%, 40.4% and 29.2%, respectively. Among them, outstanding inclusive loans to micro and small businesses kept growing at a pace of more than 20% for nearly 40 consecutive months. **Second, real estate loans recorded the lowest growth on record.** The growth of outstanding real estate loans at the end of Q2 further decelerated to 4.2%, a fresh record low, down 5.3 percentage points year-on-year.

2. Liquidity continued to be loose, with market interest rates generally moving lower.

PBOC cut interest rates again while the market rates remained low in Q3. Key policy rates including one-year MLF and seven-day reverse repo rate were lowered in August. Major interest rates generally declined under the combined effect of policy rate reduction and sluggish demand for corporate and personal financing.By the end of August, the weighted monthly average rate of pledge-style repos and the weighted monthly average rate of inter-bank lending were 1.24% and 1.23%, down 33 bps from the end of Q2, respectively. Financial institutions' weighted average RMB lending rate fell to 4.41% in 2022Q2, down 24 bps from Q1 to a record low. It is worth noting that China's money market may show a phenomenon of liquidity "sedimentation". First, the money market rates are persistently lower than short-term policy rates. Second, the weighted average lending rate of financial institutions fell faster than LPR. Third, the bills financing rate has dropped sharply.

3. The RMB exchange rate went lower in choppy trading as the Fed hiked rates in row.

In Q3, the RMB exchange rate was generally volatile and trended downward. The main contributors to RMB depreciation were as follows: **First, DXY kept rising.** The Fed sharply raised the federal funds rate by 75 bps on September 22, pushing DXY beyond 113, a 20-year high. As a result, the RMB fell in value against USD in choppy trading. Most non-US currencies depreciated simultaneously, at a sharper pace than RMB. **Second, the gap between China and the US interests continued to widen.** The widening gap between China and US interest rates has added to the pressure of capital outflows, weighing on the RMB exchange rate. **Third, the balance of foreign exchange settlement/sales contracted seasonally.** A small deficit in foreign exchange settlement/sales occurred under capital and financial accounts in July due to cyclical factors such as seasonal dividend payout. A deficit of USD53 million and USD628 million was recorded for direct investment and securities investment, respectively.

4. Total issue size of bonds was stable, while CDB yield fell in choppy trading.

The yield on the 10-year CDB fluctuated downward in Q3 due to weaker-than-expected economic fundamentals and rate cuts by PBOC. The 10-year CGB yield closed at 2.68% on September 23, 2022, down 14 bps from the end of June. Overall, the bond market mainly showed the following characteristics in Q3: **First, the total bond issuance was stable in size, with continued structural divergence.** As of September 23, 2022, a total of RMB45.82 trillion bonds were issued, representing a year-on-year increase of RMB1.51 trillion. Driven by the front-loaded fiscal policy, local government bond issuance was significantly front-loaded as the fiscal policy became more forward-looking. Local government bond issues surged year-on-year in Q1 and Q2, but slowed down markedly since Q3 began. **Second, term spread shrank amid swings, while credit spread narrowed slightly.** As of September 23, the CGB term spread (between 10-year and 1-year CGB yields) stood at 0.85%, up 32 bps from the beginning of the year, or down 2 bps from the end of Q2. Credit spread shrank due to less credit bond issuance and ample liquidity. **Third, innovative bonds continued to expand.** As the green transition continued to advance, green bonds (including carbon-neutral bonds, blue bonds and transition bonds) issued in 2022 to date totaled RMB433.068 billion, representing a year-on-year increase of 111.87%. **Fourth, the credit risk of bonds continued to recede.** As of September 23, 2022, accumulative defaults on credit bonds amounted to RMB63,409 million, representing a year-on-year decrease of 42.74%. Specifically, debt defaults in the real estate industry totaled RMB31.11 billion, with little change year-on-year, but debt rollovers reached RMB106.231 billion, up RMB75.731 billion year-on-year.

5. A-shares moved lower in choppy trading amid weak market sentiment.

A-shares have entered a correction since Q3, showing a volatile downtrend amid teetering market confidence and a push-and-pull of market dynamics. SSE Composite Index closed at 3,088.37 on September 23, 2022, down 15.15% from 3,639.78 recorded at the end of 2021, or down 9.13% from the end of Q2 (3,398.62). Negative factors were as follows: **First, the domestic economic recovery missed expectations, affecting market confidence.** Economic activity has not yet returned to normal amid COVID-19 resurgence and pent-up consumer demand, resulting in a sluggish recovery of market confidence. **Second, adverse events fueled market panic.** For example, the US politicians' unannounced visit to Taiwan Province in early August triggered market turbulence, sending A-shares down more than 2% on the same day. The United States put 159 US-listed Chinese firms on the "pre-delisting" watch list. The slump in China concept stocks also weighed on A-shares. **Third, the profitability of listed companies weakened.** According to interim reports of listed companies, the listed firms in most sectors reported a year-on-year decline in ROE, led by real estate, consumer staples and industries with a decrease of 2.18%, 1.37% and 0.87%, respectively. **But there were also many positive factors for A-shares,** including that China and the United States signed an audit oversight agreement, signaling a key step in the cooperation between the two countries that helps bolster market expectations. The State Council launched 19 follow-up policy measures at its executive meeting to support relevant fields and stabilize the economy, covering housing credit and platform economy. PBOC's stronger-than-expected rate cuts in August also further boosted market confidence.

II.2 Financial Forecast for 2022Q4

Looking forward to Q4, the financial market will likely remain steady. From the perspective of economic fundamentals, such factors as mitigated impact of COVID-19, economic recovery and confidence restoration will help stabilize financial markets. From the policy point of view, PBOC is expected to flexibly use open market operations and various lending facilities to ensure reasonably sufficient liquidity and keep liquidity steady and slightly easy. On the whole, new credit supply is expected to further ratchet up in Q4, corporate financing costs will continue to drop, capital markets will remain volatile, and the RMB is unlikely to stage a continuous depreciation.

However, the pandemic may continue to disrupt the expectations of economic entities, which in turn will dent the stability of financial markets.

1.The financing environment will remain stable and slightly easy to help stabilize the real economy.

First, money supply and aggregate financing will likely maintain their double-digit growth. Driven by restored corporate confidence in economic prospects, the funding demand is set to recover steadily and drive aggregate financing up. **Second, the credit structure will continue to improve.** Financial institutions will still focus their support on key sectors and weaker links of the economy, including micro and small businesses covered by inclusive finance, green businesses and technological innovation. Credit growth in supported fields is expected to remain above 20%. **Third, the growth of real estate loans firmed up.** As many cities in China have adopted measures such as relaxing purchase restrictions and lowering the down payment requirement to support first-time buyers and upgraders, coupled with expedited credit underwriting and issuance from banks, 2022Q4 will likely see a recovery in the financing demand related to real estate and a gradual stabilization in credit growth.

2. With abundant money supply and pent-up demand, the financing cost of the real economy will remain low.

Given the ongoing economic recovery on a fragile footing, the monetary policy is expected to remain easy in Q4 and keep financing costs low across the real economy。 **First, policy rates will likely remain stable.** Against the backdrop of China-US monetary policy divergence and continued aggressive rate hikes by central banks including the Fed, further rate cuts will intensify the pressure of RMB depreciation and capital outflow. PBOC is unlikely to further cut interest rates in Q4. **Second, money market rates will find a solid floor.** In view of the current liquidity "sedimentation", PBOC is stepping up its efforts to drain liquidity from the open market, which will push money market rates higher. **Third, lending rates will stay low.** The corporate financing demand will remain weak, which means lending rates are more likely to fall than rise. According to PBOC survey, the loan demand index for Q2 was 56.6%, a sharp drop of 15.7 percentage points compared to Q1, especially for smaller businesses. As shown by forward-looking indicators of loan demand such as profitability and operational robustness of industrial enterprises[1], the real economy will unlikely see a fundamental recovery of financing demand in the foreseeable future.

3. The RMB exchange rate has limited downside in the short term, and will remain resilient over the medium and long terms.

The RMB exchange rate will remain under pressure in Q4, yet with limited downside. The **RMB exchange rate will face the following short-term pressures: First,** the Fed keeps raising the federal funds rate. Curbing inflation is still the Fed's top priority (the US CPI was still as high as 8.3% month-on-month in August). Rate hikes are expected to continue into November. A strong US dollar will add to the depreciation pressure on the RMB. **Second,** the weaker foreign demand will slow down China's exports, and the shrinking trade surplus will weigh on the RMB exchange rate. **However, the RMB value still has its strong support: First,** market expectations are generally stable. The ratio of foreign exchange settlements[2] reached 71% in August, a relatively high level in recent years. The ratio of foreign exchange sales[3] was 67%, fitting with the monthly

[1] In the first seven months of 2022, the profit of industrial enterprises decreased by 1.1% year-on-year, putting an end to the streak of positive growth that started in October 2020. The loss of loss-making enterprises was 48.5%, up 3.6 percentage points from the end of June.

[2] Ratio of foreign exchange settlements: The foreign exchanges sold by customers to banks as a percentage of customer's foreign exchange earnings, used to measure the willingness to settle foreign exchange.

[3] Ratio of foreign exchange sales: The foreign exchanges purchased by customers from banks as a percentage of customer's foreign

average in 2022 to date. They show overall stability of the market participants' willingness to settle and sell foreign exchanges. **Second,** China has a stable and abundant stock of foreign exchange reserves. At the end of August, China had USD3,054.9 billion in its official foreign exchange reserve and financial institutions recorded USD953.7 billion in balance of foreign exchange deposits, both staying high and serving as "ballasts" to tackle excessive volatility in the RMB exchange rate.

4. The bond issuance is unlikely to expand significantly, and bond yields will remain low.

The bond market is expected to show the following characteristics in Q4: **First, the bond issuance size will remain stable with continued structural divergence.** In particular, the annual quota for special local government bond issues has been basically completed. The issuance of local government bonds is expected to further decline in Q4. Given the limited improvement in financing demand of the real economy, the issuance of bonds by either listed or unlisted companies can hardly expand markedly. Under great pressure to replenish capital, however, commercial banks are expected to maintain a high level of subordinated bond issues. **Second, bond yields will remain low.** From the perspective of economic fundamentals, bond yields lack the upward momentum as the real economy stands to remain in a weak recovery due to COVID-19 resurgence. **Third, the debt defaults of property developers deserve close attention.** Credit risk in the bond market has been effectively controlled as liquidity remains reasonably sufficient and the diversified default handling mechanism gradually improves. But the real estate industry still poses prominent risks. Debt rollover will give property developers a respite in debt service, but we suggest keeping an eye on the recovery of their profitability and solvency.

5. The stock market will remain volatile as market expectations are impacted by various factors.

Looking forward to Q4, there are still multiple disturbing factors in the market. Overall, A-shares will remain in choppy trading. The negative factors were as follows: **First,** the uncertainty in pandemic developments will still drag down recovery of the real economy. The fragile footing of economic recovery will impair investors' confidence and risk appetite, thus putting the stock market under greater downward pressure. **Second,** external factors will continue to send shock waves to A shares. The wild swing of commodity prices and rate hikes in major economies are likely to trigger overreaction among investors and exacerbate the A-share volatility. However, there are still some positive factors for A-shares: **First,** a stable and slightly easy monetary policy will keep liquidity reasonably sufficient and bolster the strength of A-shares. **Second,** from the perspective of valuation, A-shares are at an all-time low level of valuations, generally below that in overseas markets. For example, as of September 23, 2022, the CSI 300 Index had a P/B ratio of 1.29, compared with the S&P 500 P/B ratio of 3.72. In particular, there are still opportunities in booming industries such as new energy vehicles, techs and new materials.

exchange expenditure, used to measure the willingness to sell foreign exchange.

Table 1: China's Main Economic & Financial Indicators and Forecasts in 2022Q4 and 2022 (%)

Indicator	2019 (R)	2020 (R)	2021 (R)	2022 (F)				
				Q1 (R)	Q2 (R)	Q3 (E)	Q4 (F)	Full year (F)
GDP	6.0	2.2	8.1	4.8	0.4	**3.8**	**5.0**	**3.5**
Industrial value added of enterprises above designated size	5.7	2.8	9.6	6.5	0.6	**4.3**	**5.8**	**4.3**
Value added of the services sector	7.2	1.9	8.2	4.0	-0.4	**3.0**	**4.0**	**2.7**
Fixed asset investments (cumulative)	5.4	2.9	4.9	9.3	6.1	**5.9**	**6.0**	**6.0**
Investment in real estate development (cumulative)	9.9	7.0	4.4	0.7	-5.4	**-7.9**	**-7.2**	**-7.2**
Total retail sales of consumer goods	8.0	-3.9	12.5	3.3	-4.9	**4.0**	**5.5**	**2.2**
Exports (denominated in RMB)	5.0	4.0	21.2	13.2	12.7	**14.9**	**5.0**	**11.1**
Imports (denominated in RMB)	1.7	-0.2	21.5	8.3	1.9	**6.3**	**4.0**	**5.0**
Consumer Price index (CPI)	2.9	2.5	0.9	1.1	2.2	**2.8**	**2.8**	**2.2**
Producer price index (PPI)	-0.3	-1.8	8.1	8.7	6.8	**2.4**	**-2.0**	**4.0**
Broad money supply (M2, ending balance)	8.7	10.1	9.0	9.7	11.4	**12.0**	**12.0**	**12.0**
Aggregate financing to the real economy (stock, ending balance)	10.7	13.3	10.3	10.5	10.8	**10.8**	**10.5**	**10.5**
1-year MLF	3.25	2.95	2.95	2.85	2.85	**2.75**	**2.75**	**2.75**
1-year LPR	4.15	3.85	3.80	3.70	3.70	**3.65**	**3.65**	**3.65**
RMB/USD spot exchange rate	6.97	6.54	6.37	6.35	6.66	**7.05**	**6.90**	**6.90**

Source: BOC Research Institute

III. Macro Policy Suggestions

III.1 Balance stable growth with fiscal sustainability, continue improving the efficiency of fund utilization.

Funding should be early planned in line with the latest economic developments to support recovery of the real economy. While seeking new sources of revenue, expenditure should be reduced. Funding support should be well targeted to avoid indiscriminate stimulus. Extra attention should be paid to the sustainability of fiscal resources to prevent a "fiscal cliff" next year.

Improve the management and utilization of non-tax revenue. The fees, charges and fines levied by governments at all levels, associations, chambers of commerce should be fully reviewed to speed up the removal and adjustment of unreasonable fees and fines beyond the statutory authority. A disciplinary system for illegal charges and fines should be created and implemented. The risk of local government debts in key regions should be closely monitored.

III.2 The monetary policy should strengthen the important function of structural instruments to help industries and enterprises to tide over difficulties.

While maintaining a favorable financing environment, the monetary policy should strengthen the use of structural monetary policy instruments to increase support for industries and enterprises hit hard by COVID-19. In particular, given the widening divergence between China's and foreign monetary policies in Q4, a good balance should be struck between stable domestic growth and stable RMB exchange rate. China should step up support for distressed industries and enterprises. In the future, we should give bigger play to structural monetary policy instruments. A combination of special relending, rediscounting and other tools should be used to help cash-strapped industries and businesses, so as to prevent the risk of disrupted cash flows and ensure continuity of industry and supply chains.

III.3 Attach greater importance to investment in supporting economy recovery, enhancing consumers' expectations and willingness to spend.

Infrastructure investment should continue supporting the economy recovery. Sources of funding for infrastructure investment should be early planned. The pipeline of high-quality projects should be created at a faster pace. Funding should be injected into projects, making it more efficient and bolstering stable growth of infrastructure investment. Policy support should be effectively provided for the purchase and renovation of equipment in a bid to fuel growth in manufacturing investment.

The effort to stabilize consumption should focus on ensuring stable employment and expectations. The part-time job market should be well regulated. Efforts should be stepped up to provide employment as a form of relief. Transitional jobs and vocational skills training should be provided for the unemployed and fresh graduates. It is necessary to take raising the threshold for levying individual income tax into consideration. Restrictive restrictions on consumer purchases should be reviewed and lifted as soon as possible.

III.4 Optimize the real estate policies on both supply and demand sides to help stabilize the housing market.

The demand-side restrictions should be relaxed on a city-specific basis to further lower the eligibility criteria for homebuyers. The pressure on first-time homebuyers should be eased by reducing the down payment ratio and allowing broader and more efficient use of housing provident funds. The gap in down payment ratios and mortgage rates between first-time homebuyers and home upgraders should be appropriately narrowed to unleash the demand for home upgrades.

On the supply side, we will do our best to “ensure the delivery of housing and the people’s livelihood”. Stronger credit support should be provided for property developers, including allowing rollover of bank loans for eligible developers. The risk management mechanism should be improved to deal with problem developers in a category-specific manner.

III.5 Make stronger efforts to protect market entities, provide a more stable, law-based and predictable development environment.

The rescue and relief policies should be persistent till lifting market players out of hardships. Special relief funds should be provided. The liquidity strain of micro, small and medium-sized businesses should be eased by increasing the quota for inclusive loans to micro and small businesses and extending the delay in social security contributions.

The government should strengthen communication with market players before the introduction of major policies, establish and improve an enterprise-related policy-making mechanism where business owners take part, set a reasonable transition period for market participants and create a stable, transparent and predictable development environment.

The business environment should be continuously improved to boost the confidence of market participants. The institutionalized transaction costs should be reduced to unleash the vitality of market players. Digital transition should be sped up to empower micro, small and medium-sized enterprises with digital technology. Diverse multi-governance should be leveraged to ensure fair competition among market players.

中國銀行
BANK OF CHINA

BOC Research Institute
1 Fuxingmen Nei Street, Beijing, 100818 China
Postal Code: 100818
Telephone: +86-10-66592780
Fax: +86-10-66594040