

—The macroeconomy—

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Summary

December's economic indicators generally accelerated on the previous month. A glance at the GDP data for 2019 shows imports slumping more than exports, with growth supported by the positive contribution of external demand. The improvement in December's indicators and the phase one trade agreement between the US and China are both positive factors, but the spread of the pneumonia due to the new outbreak of the coronavirus could act to drag the economy down. The 2020 work conferences of the People's Bank of China (PBC) and the China Banking and Insurance Regulatory Commission (CBIRC) both revealed a strong awareness of the need to 'prevent and defuse major financial risks' as part of the 'Three Tough Battles' strategy for 2018–20.

1. December's economic indicators accelerated on the previous month

- **The government hit its GDP target for 2019**
- **Production and investment accelerated**
- **Automobile sales “will remain firm around 25 million vehicles in 2020 too” (Ministry of Industry and Information Technology)**
- **New homes prices grew at a slower pace in all tiers of city**
- **Exports and imports both rallied on a y-o-y basis**
- **At +3.0%, CPI growth stood within the government's target range; PPI growth contracted at a slower pace**
- **Net new bank loans rose at a slower pace; total social financing expanded**

2. The policy response: Attention will focus strongly on 'preventing and defusing financial risks' in 2020, the decisive year of the 'Three Tough Battles'

- **Recent signs of improvement and headwinds**
- **Financial administration is focused strongly on 'preventing and defusing financial risks'**

1. December's economic indicators accelerated on the previous month

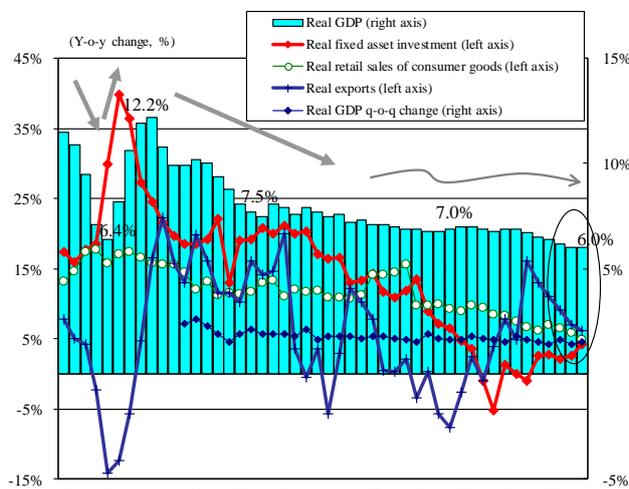
▪ The government hit its GDP target for 2019

On January 17, the National Bureau of Statistics (NBS) announced¹ that China's real GDP growth rate for 2019 stood at +6.1%, down on the +6.7% recorded in 2018,² while the figure for October–December hit +6.0% on the same period last year (from here on, all figures refer to a 'same-period previous-year comparison' unless otherwise specified), thus remaining within the government's target for 2019 of +6.0–6.5%. Growth was up +1.5% on the previous quarter (Fig. 1).

The 4Q figure of +6.0% represented the lowest quarterly pace of growth since 1992, following on from a similar result the previous quarter. In a press conference, NBS director Ning Jizhe said China's per capita GDP had reached RMB 70,892 (\$10,000), its population had topped 1.4 billion, and its economy now accounted for over 16% of global GDP. He added that China remained an engine driving the global economy.

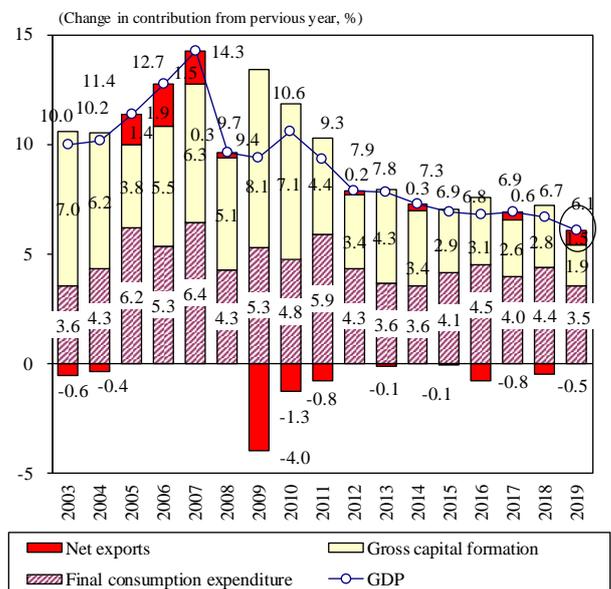
A glance at contribution levels by demand item over 2019 shows the contribution of final consumption expenditure hitting +3.5%, down on 2018's figure of +4.4%, while the contribution of gross capital formation fell from +2.8%Pt in 2018 to hit +1.9%Pt. However, the contribution of net exports expanded from -0.5Pt to +0.7%Pt. The details show the contribution of domestic demand hitting +5.4%Pt in 2019, down on 2018's figure of +7.2%Pt, though growth was bolstered after the contribution of external demand returned to positive territories, up from -0.5%Pt in 2018 to hit +1.2%Pt (Fig. 2).

Fig. 1: GDP and major economic indicators (quarterly)



Note: The real RMB value of exports is indexed using the producer price index (PPI); the real value of fixed asset investments is indexed using the price index of investment in fixed assets; and the real value of retail sales of

Fig. 2: Breakdown of GDP by demand item



Source: National Bureau of Statistics of China, CEIC

¹ China Net, January 17, 2020, “国新办举行 2019 年国民经济运行情况发布会 (The State Council Information Office Convenes a Meeting to Discuss National Economic Performance in 2019)”

http://www.china.com.cn/zhibo/content_75618333.htm#fullText

² NBS, January 20, 2020, “Preliminary Accounting Results of GDP for the Third Quarter of 2019”

The GDP growth rate from around 2014 onwards was also revised, with the result for 2018 upgraded 0.1%Pt from +6.6%.

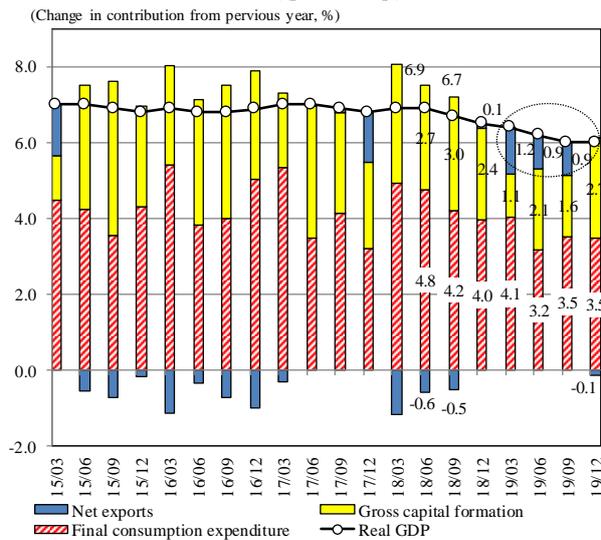
http://www.stats.gov.cn/english/PressRelease/202001/t20200120_1724023.html

consumer goods is indexed using the retail price index (RPI).

Source: National Bureau of Statistics of China, CEIC

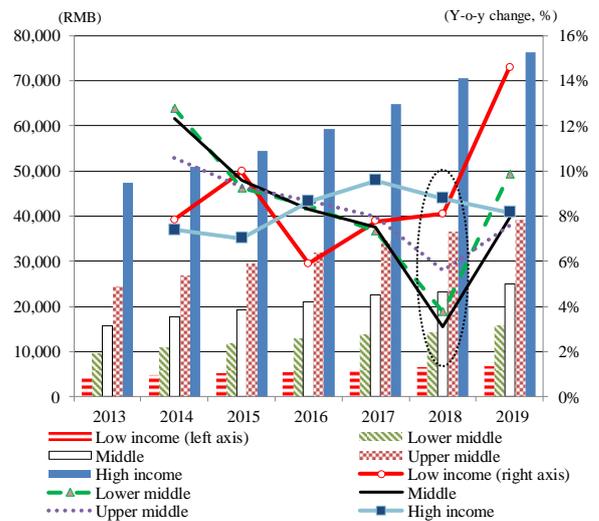
External demand had continued to make a positive contribution up until the third quarter, but it dipped slightly into negative territories in the fourth quarter, though the contribution of gross capital formation expanded on a quarterly basis, with growth pulled along by fixed asset investment (Fig. 3). A breakdown by sector shows primary industry growing by +3.1% over 2019, down on the +3.5% figure recorded in 2018, with growth in the secondary sector also slowing from +5.8% to +5.7% and growth in the tertiary industry slowing from +8.0% to +6.9%.

Fig. 3: Breakdown of GDP by demand item (quarterly)



Source: National Bureau of Statistics of China, CEIC

Fig. 4: Urban disposable income



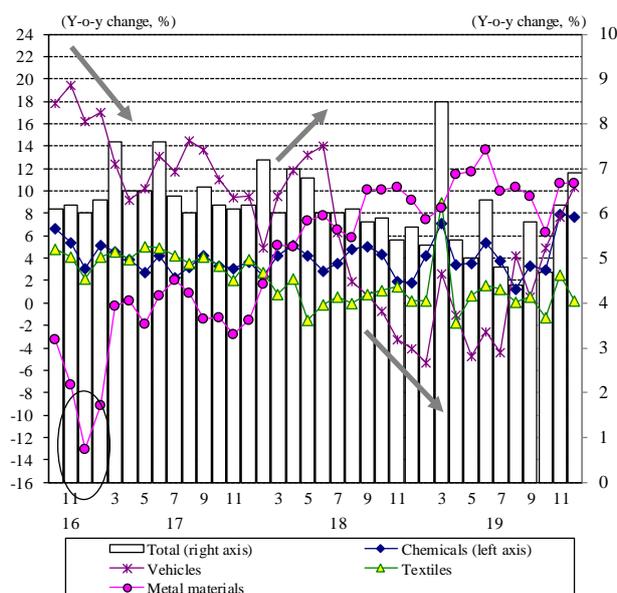
Source: National Bureau of Statistics of China, CEIC

• Production and investment accelerated

December’s economic indicators generally accelerated on the previous month. At +6.9%, value-added industrial production in December was up on November’s +6.2% (the m-o-m figure was +0.6%) (Fig. 5). Automobile, steel and chemicals production all grew at a faster clip. At +5.7%, growth in 2019 was down on 2018’s figure of +6.2%.

At +5.4%, nominal fixed asset investment in January–December was up on January–November’s +5.2%. At +10.0%, the standalone monthly figure was also up on November’s +5.2% (the m-o-m figure was +0.4%). At +3.8%, investment in infrastructure construction in January–December was down on January–November’s +4.0% figure, while real estate investment also slowed from +9.4% to +9.1%. However, manufacturing investment grew slightly from +2.5% to +3.1% (Fig. 6). Though real estate investment in 2019 was up on 2018’s figure of +8.3%, manufacturing investment was down on 2018’s +9.5%, while investment in infrastructure construction was unchanged at +3.8%.

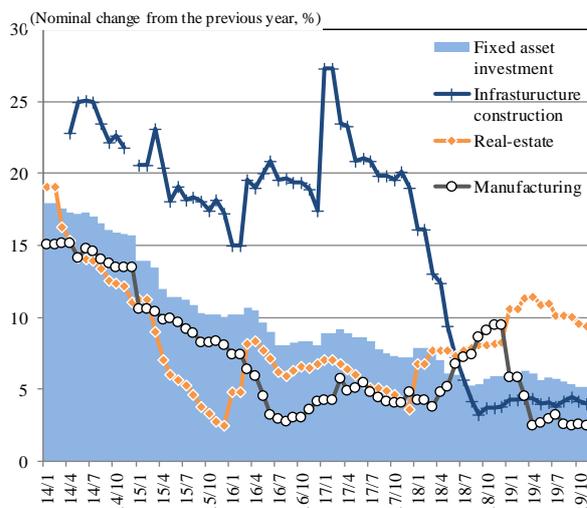
Fig. 5: Value-added industrial production



Note: The value-added industrial production amount. The figure for January shows the aggregate year-on-year change for the period January–February.

Source: CEIC

Fig. 6: Fixed asset investment



Note: The figures show a same-period previous-year comparison of the cumulative results for periods lasting from the beginning of the target year until the month in question.

Source: National Bureau of Statistics of China, CEIC

Nominal retail sales of consumer goods grew by +8.0% in December, unchanged on November (the m-o-m figure was +0.5%) (Fig. 7). Internet retail sales of goods and services hit RMB 10,632.4 billion over January–December (goods: RMB 8,523.9 billion; services: RMB 2,108.5 billion), with net shopping growing by +16.5% to account for 20.7% of total retail sales of consumer goods during this period (RMB 41,164.9 billion, +8.0%).³

Sales of new vehicles hit 2.6583 million in December (-0.1%). This represented an improvement on November’s figure 2.3096 million (-3.6%), with sales also contracting on a slower y-o-y basis (Fig. 8). Sales had trended upward until 2017 (28.941 million and +3.6%), but in 2018 they hit 28.0398 million (-3.1%) to record the first y-o-y decline since 1990, with the pace of contraction then hitting -8.2% (25.7545 million) over 2019. The slowdown was probably because the tax break on purchases of small passenger vehicles (instituted in October 2015) was abolished at the end of 2017,⁴ with consumer sentiments also hit by uncertainty about US/China trade frictions and so on.

Though sales of automobiles (new vehicles) and homes have been hit by moves on the policy front, income growth has recovered on the income tax cuts instituted in 2019 (Fig. 4), with demand for high-quality consumption moving firmly overall on China’s expanding middle class and a stable jobs environment.

³ NBS, January 19, 2020, “Total Retail Sales of Consumer Goods Went up by 8.0 percent in 2019”

http://www.stats.gov.cn/english/PressRelease/202001/t20200119_1723651.html

⁴ On December 15, 2016, the Ministry of Finance and the State Administration of Taxation announced that the tax cut on purchases of new vehicles with low emissions would be extended one year to the end of 2017. However, the tax rate will rise from 5% to 7.5%, so the size of the cut (compared to the normal tax rate of 10%) will be halved in 2017 (2.5%). Ministry of Finance: “关于减征 1.6 升及以下排量乘用车车辆购置税的通知 (Circular on the Lowering of the Purchase Tax on Passenger Vehicles with Emissions of 1,600cc or Less)”

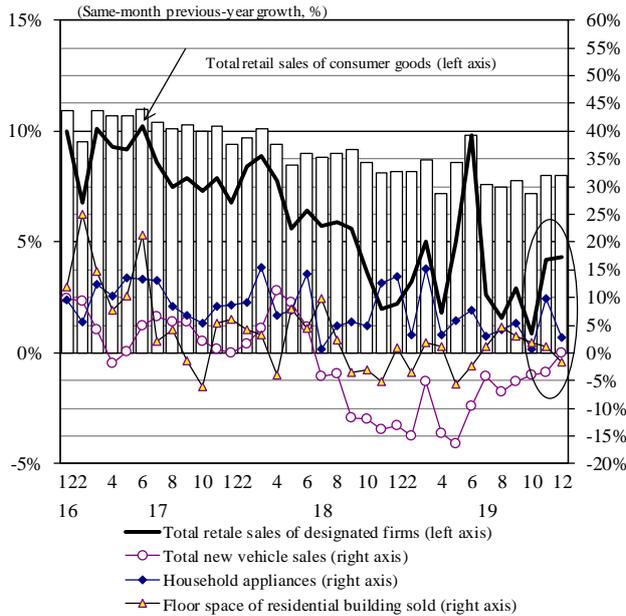
http://szs.mof.gov.cn/zhengwuxinxi/zhengcefabu/201612/t20161215_2483048.html

On September 29, 2015, the State Administration of Taxation issued Notice No. 104 [2015]. This announced that the purchase tax on passenger vehicles with emissions of 1,600cc or less would be lowered from 10% to 5% from October 1, 2015 to the end of 2016.

<http://www.chinatax.gov.cn/n810341/n810755/c1827947/content.html>

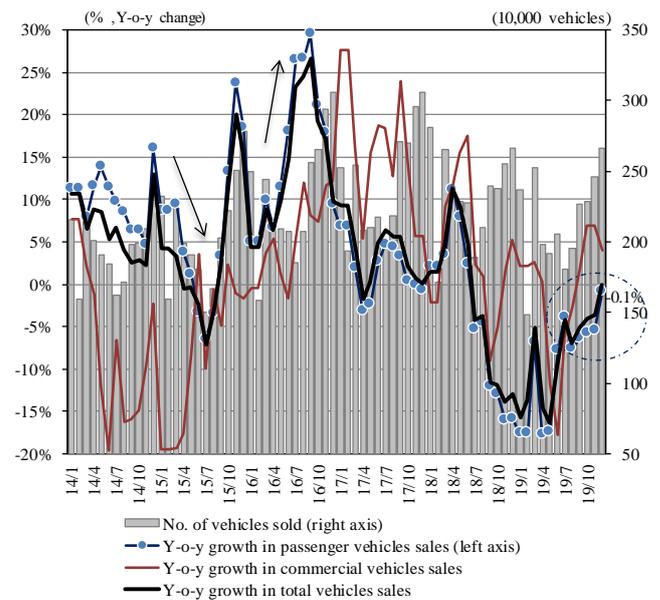
At 3.62%, the registered urban unemployment rate in 2019 improved on 2017's 3.90% and 2018's 3.80%.⁵ Furthermore, though the jobs-to-applicants ratio dipped in June and September 2019, it had rallied to 1.27 by the end of the year, thus matching the figure from the end of 2018, which itself had marked the strong result since records began (Fig. 20). The shrinking working age population explains why the employment situation remains stable amid slowing GDP growth.⁶ Given this demographic situation, if anyone does lose their job, they will probably be able to find a new one, with conditions changing compared to the time of the 2008 financial crisis.

Fig. 7: Retail sales of consumer goods; retail sales by item; floor space of residential building sold



Note: Designated firms: firms with an annual turnover of RMB 5 million or over; the household appliance data also refers to sales by these designated firms; February = the cumulative results for January–February.
Source: CEIC

Fig. 8: Number of vehicles sold (by passenger vehicles and commercial vehicles)



Note: The figure for January and February shows cumulative y-o-y growth for the period January–February.
Source: China Association of Automobile Manufacturers, CEIC

▪ Automobile sales “will remain firm around 25 million vehicles in 2020 too” (Ministry of Industry and Information Technology)

Though new car sales figures and data from the second-hand car market (traded vehicles)⁷ show demand for automobiles falling from 1.3% in 2018 to -4.5% in 2019 (the second-hand car data is extrapolated from the figure for January–October), the decline is not quite significant. Furthermore, the buoyancy of the market for second-hand cars would provide a boost to high-end vehicles from Japan, Europe and the US, which can fetch good prices even

⁵ The surveyed unemployment rate more closely reflects the real situation. This indicator hit 5.2% at the end of 2019. This marked a deterioration on the 4.9% recorded at the end of 2018, but it remained within the government's target of 5.5%.

⁶ The working age population hit 897.29 million at the end of 2018, down for the seventh straight year since 2012 (with the working-age population falling by a total of 43.15 million during this period). 13.52 million new jobs were created in 2019, thus hitting the annual target of 11 million.

⁷ 13.82 million second-hand vehicles were traded in 2018, a figure equivalent to 49.8% of new vehicle sales over the same period (28 million). The figure for January–October 2019 stood at 11.85 million. When this result is extrapolated for the whole of 2019, it gives a figure equivalent to 55.3% of new vehicle sales over 2019 (25.75 million).

Source: The China Automobile Dealers Association (http://www.cada.cn/Data/info_86_6836.html), etc.

when sold second hand.

In a press conference of January 20,⁸ MiaoWei, head of the Ministry of Industry and Information Technology, said the automobile industry had slowed in 2018 after previously growing for 28 years, with the market and the industrial structure entering a period of adjustment. However, he also said the contraction in automobile sales volumes would gradually ease and market sentiments would recover from the latter half of 2019 on corporate adjustments and the enactment of policies to promote consumption. He forecast sales of around 25 million in 2020, with sales moving flatly or just dipping slightly. He added that the execution of 2017's *Medium and Long-term Car Industry Development Plan* and the swift promulgation of the *New Energy Vehicle Industry Development Plan (2021-2035)* would promote high-quality growth in the new energy vehicle market.

▪ New homes prices grew at a slower pace in all tiers of city

At -0.1% (1,715.58 million m²), the floor space of residential buildings sold contracted in 2019 after previously recording positive growth of +7.7% in 2017 and +1.3% in 2018. Housing sales bottomed out and began recovering in April 2015 following measures by the authorities to prop up the real-estate market. The People's Bank of China (PBC) lowered deposit and lending rates six times from November 2014, for instance, while the (lowest) down payment rate for second homebuyers was cut from 60% to 40% (March 30, 2015) and the down payment rate for first-time homebuyers was also lowered to 25% (September 30, 2015). Thereafter, buying restrictions pioneering in Shanghai and Shenzhen⁹ in March 2016 subsequently spread to other cities with surging house prices,¹⁰ with the restrictions being tightened further.¹¹

In December, 68 of the 70 cities surveyed saw the price of new homes rising on the previous year, unchanged on November. Growth slowed when it came to first-tier cities (from +4.9% in November to +3.8%), second-tier cities (from +7.9% to +7.3%) and third-tier cities (from +7.0% to +6.7%) (Fig. 9).¹²

On a monthly basis, 50 of the 70 cities surveyed saw the price of new homes rising, up from 44 in November.

⁸ China Net, January 20, 2020, “新闻办就 2019 年工业通信业发展情况举行新闻发布会 (The State Council Information Office Holds a Press Conference About Industrial and Information Technology Development in 2019)”

http://www.gov.cn/xinwen/2020-01/20/content_5470965.htm

⁹ On March 25, 2016, the down payment rate for second homebuyers was lifted from 40% to 50–70% in Shanghai. Shenzhen has lifted the down payment rate for second homebuyers from 30% to 40%. Both moves represent a tightening of restrictions on purchases by non-resident buyers.

¹⁰ Similar tightening measures have also spread to cities with conspicuous house price inflation, with Xiamen, Nanjing and Hefei introducing similar regulations from the end of April to mid-July 2016, for example. Reference: Economic Information Daily, July 14, 2016, “房地产现严重分化 因城施策将是下半年楼市政策主线 (China's acute property price bifurcation problem: Main real-estate measures in 2H influenced by the regional policies)”, etc.

http://www.china.com.cn/shehui/2016-07/14/content_38877726.htm

People's Daily on October 11, 2016 entitled “限购、限贷，近期已有 20 城市推出新举措 楼市调控 因城施策 (Restrictions on housing purchases and loans recently introduced in 20 cities: Restrictions geared to meet the circumstances of each city).” Restrictions on housing purchases were introduced in 20 cities at the time the article was written.

<http://www.fangchan.com/news/6/2016-10-11/6191397283909931925.html>

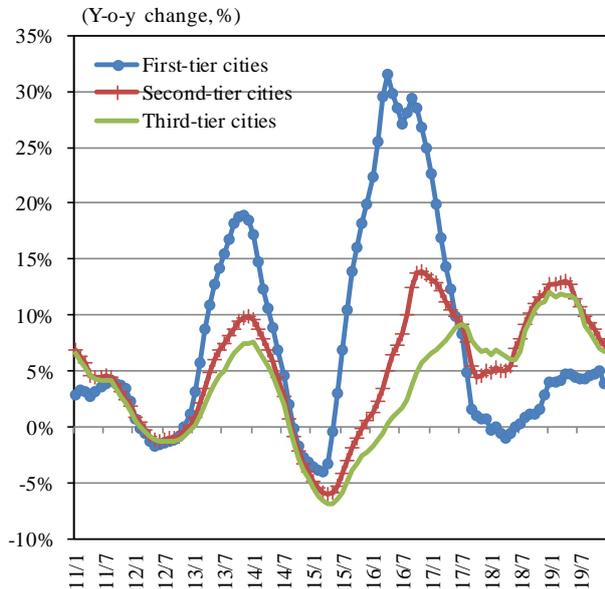
¹¹ The 21st Century Business Herald, March 20, 2017, “北京最严楼市调控” 认房又认贷” 下半年全国楼市降温可期 (Checks on housing and loan records: Beijing's strictest real estate controls set to chill housing markets nationwide in 2H).” Beijing has introduced ‘the toughest controls in history.’ It lifted the down payment rate for second home purchases to at least 60 percent on March 17, for instance, with the rate lifted to at least 80% for buyers who will not be living at the property. Furthermore, the city has also suspended issuances of mortgage loans for individuals with maturities of 25 years or more, while homes bought by companies cannot be resold for at least three years.

http://epaper.21jingji.com/html/2017-03/20/content_58356.htm

¹² Of the 70 cities surveyed, the following three cities saw the fastest home price growth: Hohhot +15.9%, Dali +15.4%, +Xian +14.2% (December).

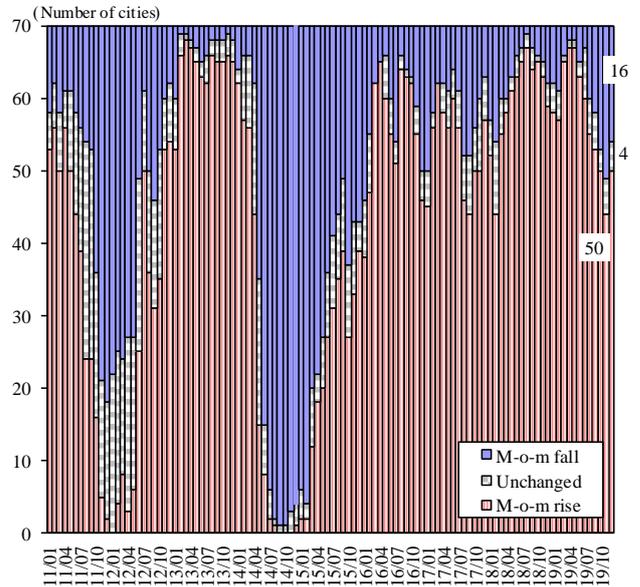
Four cities saw prices moving flatly on the previous month (down from five in November), while 16 cities saw prices falling on the previous month (down from 21 in November) (Fig. 10).¹³

Fig. 9: New-homes prices (Y-o-y)



Note: First-tier cities: Beijing, Shanghai, Guangzhou and Shenzhen
 Second-tier cities: Capitals other than first-tier cities (municipality), capitals of autonomous regions, Dalian, Qingdao, Ningbo, and Xiamen.
 Third-tier cities: Cities other than first-tier and second-tier cities (35 of the 70 cities surveyed)
 Source: CEIC

Fig. 10: Number of cities recording m-o-m changes in sales prices of residential buildings



Source: National Bureau of Statistics of China, CEIC

▪ **Exports and imports both rallied on a y-o-y basis**

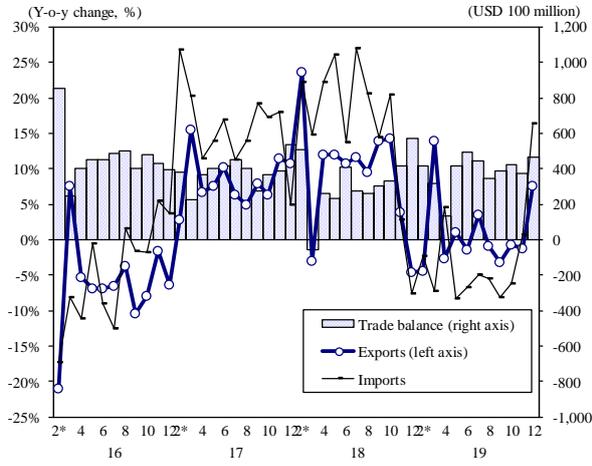
Exports rose by +7.6% (\$237.65 billion) and imports by +16.3% (\$190.86 billion) in December, with exports and imports both bouncing back after previously contracting on a y-o-y basis. The trade balance stood at \$46.79 billion (Fig. 11). The figures for 2019 show exports up by +0.5% (\$2,498.4 billion) and imports down by -2.8% (\$2,076.9 billion), with China’s trade surplus up a substantial +20.1% on 2018 to hit \$421.51 billion.

When it came to the trade situation in 2019, the Ministry of Commerce stated that “(1) imports and exports with the countries along the Belt and Road routes have increased by 10.8%, and their proportion has increased by 2 percentage points to 29.4%; (2) exports in the central and western regions accounted for 18.3%...the exports of processing trade of the central and western regions accounted for nearly 23%... positive progress was achieved in undertaking the transfer of processing trade industry [from the coastal region]; (3) the product structure has been continuously upgraded...the export of mechanical and electrical products accounted for 58.4% and the exports of integrated circuits and automobile vehicles have increased by 25.3% and 8.2% respectively; (4) imports and exports of foreign-invested enterprises accounted for 39.9% and continued to play a key role...the imports and exports of

¹³ NBS, January 16, 2020, “Sales Prices of Residential Buildings in 70 Medium and Large-sized Cities in December 2019” http://www.stats.gov.cn/english/PressRelease/202001/t20200116_1723191.html
 From January 2018, the data no longer includes the sales price of affordable housing.

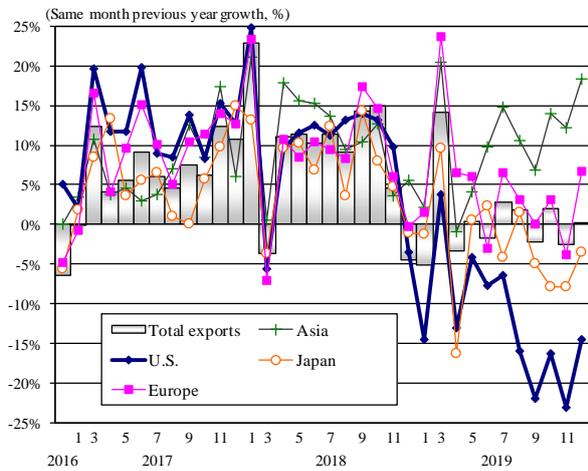
private enterprises accounted for 43.3% of imports and exports and became the new main force for foreign trade development.”¹⁴ Exports to the US continued to fall sharply, though imports from the US returned to positive territories for the first time since August 2018 (Figs. 13 and 14).

Fig. 11: Imports/exports; trade balance



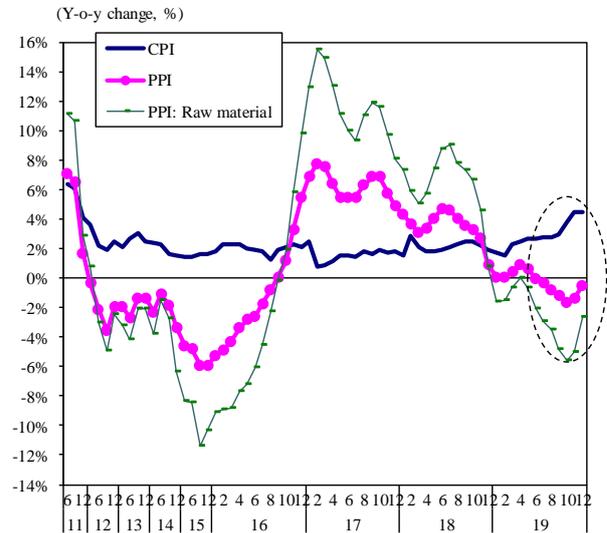
* The figures show the trade balance and a same-period previous-year comparison of the cumulative results for January–February.
Source: China Customs Statistics

Fig. 13: Exports by major region



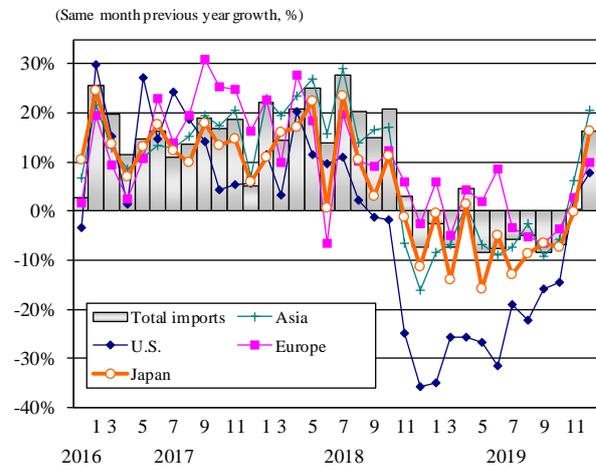
Note: The figure for January shows a same-period previous-year comparison of the cumulative results for January–February.
Source: China Customs Statistics, CEIC

Fig. 12: CPI, PPI



Note: The data from June 2011 to 2015 only shows the quarterly (March, June, September and December) figures.
Source: National Bureau of Statistics of China, CEIC

Fig. 14: Imports by major region



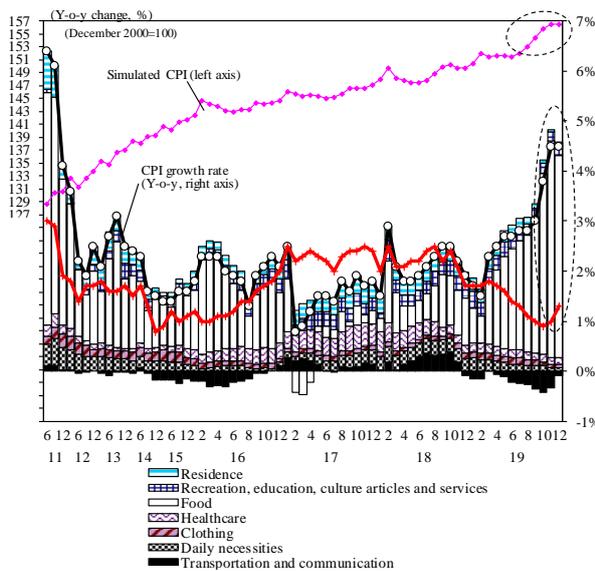
Note: The figure for January shows a same-period previous-year comparison of the cumulative results for January–February.
Source: China Customs Statistics, CEIC

¹⁴ Ministry of Commerce, January 16, 2020, “MOFCOM Department of Foreign Trade Comments on China’s Foreign Trade in 2019” <http://english.mofcom.gov.cn/article/newsrelease/policyreleasing/202001/20200102932176.shtml>

At +3.0%, CPI growth stood within the government’s target range; PPI growth contracted at a slower pace

In December, CPI (Consumer Price Index) growth hit +4.5%, unchanged on November. On a monthly basis, CPI growth stood at 0.0% in December, essentially unchanged on November (+0.4%). At +2.9%, the figure for 2019 fell below the government’s target of +3.0% (Fig. 12). A breakdown of the CPI data shows food price inflation slowing to +17.4% (November: +19.1%). At -8.0%, the price of fruit contracted at a faster pace compared to November (-6.8%), though vegetable prices rose at a faster clip at +10.8% (November: +3.9%). However, pork price inflation slowed to +97.0%, down from +110.2% in November (Figs. 15 and 16). Non-food prices grew by +1.3% in December, up slightly on November’s figure of +1.0%.

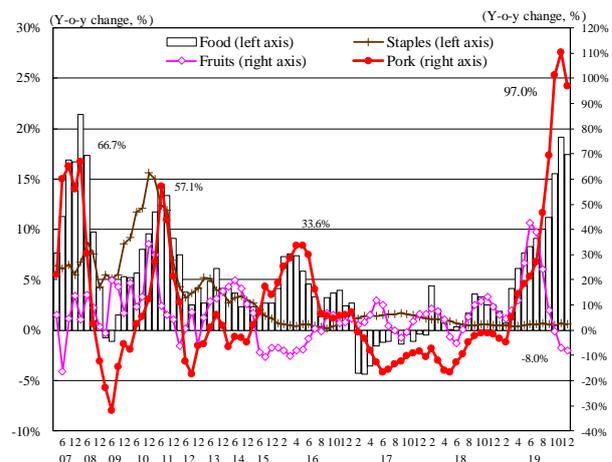
Fig. 15: CPI; Growth contribution by item



Note: The contribution rate by item is calculated by Mizuho Bank (China) based on the y-o-y growth rate and consumption expenditure statistics for each item. The simulated CPI data is calculated by Mizuho Bank (China) based on the m-o-m growth rate for each month, with December 2000 as the base month. The data from June 2011 to 2015 only shows the quarterly (March, June, September and December) figures.

Source: National Bureau of Statistics of China, CEIC

Fig. 16: Food prices



Note: The data up until 2015 only shows the quarterly (March, June, September and December) figures.

Source: National Bureau of Statistics of China, CEIC

The impact of the pork cycle¹⁵ waned after a peak in May 2016, though it bounced back after bottoming out in June 2017. Pork prices fell further into negative territories again from March 2018, though the pace of this contraction slowed from May 2018 and prices grew again from December 2018, with the trend shifting slightly during the ongoing phase of price declines. During this time, pork production recorded two consecutive years of negative growth in 2015 and 2016. It then picked up by +0.5% in 2017 to hit 54.52 million tons. It dropped back by -0.9% in 2018 to hit 54.04 million tons before falling sharply by -21.3% in 2019 to hit 42.55 million tons. This represented the first double-digit decline since 1996 (-13.4%).

At -0.5%, PPI (Producer Price Index) growth contracted at a slower pace in December (November: -1.4%).

¹⁵ This is a cycle whereby: farmers respond to lower pork prices by raising fewer pigs→supply falls and prices rise→farmers increase output→supply increases and prices stabilize→farmers raise fewer pigs.

According to the NBS, a y-o-y comparison for December shows: prices rising at a faster pace when it came to the extraction of ferrous metals (+8.8%) and the manufacture and processing of non-ferrous metals (+1.1%); prices contracting at a slower pace when it came to the manufacture of chemical raw materials and chemical products (-5.4%), the processing of petroleum, coking and other fuels (-1.8%) and the manufacture and processing of ferrous metals (-0.7%); prices shifting from negative to positive growth when it came to the extraction of petroleum and natural gas (+5.8%); and prices falling at a faster pace when it came to the mining and washing of coal (-3.6%).¹⁶

▪ **Net new bank loans rose at a slower pace; total social financing expanded**

According to the PBC, M2 money supply growth hit +8.7% in December, up slightly on November's figure of +8.2%. New bank loans increased by a net RMB 1,140.0 billion, down on November's figure of RMB 1,390.0 billion (Fig.17).

Total social financing, which includes funds procured from non-bank sources, increased by a net RMB 2,103.0 billion in December, up on November's figure of RMB 1,993.7 billion. A glance at the details reveals that: RMB loans, corporate bonds and non-financial-institution equity issuances all grew at a slower pace; banker's acceptances, government bonds,¹⁷ deposit-taking financial institution ABS and loan repayments grew at a faster pace; foreign currency loans fell at a slower pace; and entrusted loans and trust loans fell at a faster pace (Fig. 18).

Foreign exchange reserves stood at \$3107.92 billion at the end of 2019, up \$12.33 billion on the end of November and \$35.21 billion on the end of 2018. State Administration of Foreign Exchange (SAFE) press spokesperson Wang Chunying said the US dollar and major-country bond prices had fallen on the global trade situation, the foreign exchange policies of major central banks, and the results of the UK general election, for example. She added that factors like exchange rates and asset price changes had comprehensively worked to push foreign exchange reserves slightly higher (Fig. 19).¹⁸

¹⁶ NBS, January 9, 2020, “国家统计局高级统计师沈赟解读 2019 年 12 月份 CPI 和 PPI 数据 (NBS Senior Statistician, Shen Yun Deciphers the December 2019 CPI and PPI Data)”

http://www.stats.gov.cn/tjsj/sjjd/202001/t20200109_1721987.html

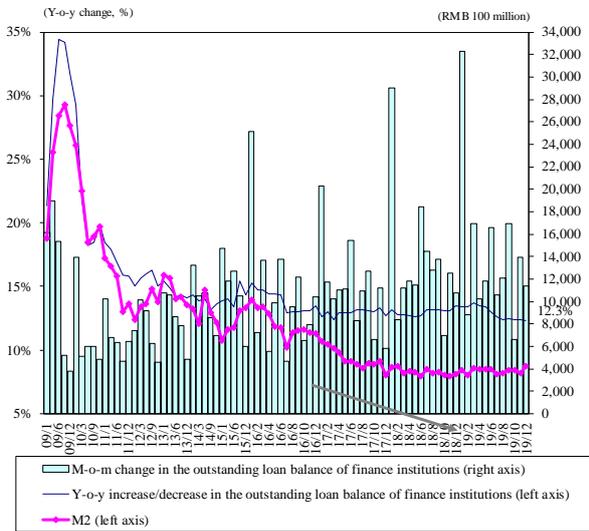
¹⁷ Since December 2019, sovereign bonds and ordinary bonds by local governments have been bundled together as ‘government bonds’ under the ‘local government revenue bonds’ heading. PBC, January 17, 2020, “2019 年金融统计数据新闻发布会文字实录”

<http://www.pbc.gov.cn/goutongjiaoliu/113456/113469/3961307/index.html>

¹⁸ The State Administration of Foreign Exchange, January 7, 2020 “国家外汇管理局新闻发言人、总经济师王春英就 2019 年 12 月份外汇储备规模变动情况答记者问 (Press Spokesperson and Chief Economist Wang Chunying answers journalist questions about foreign exchange reserve movements in December 2019.)”

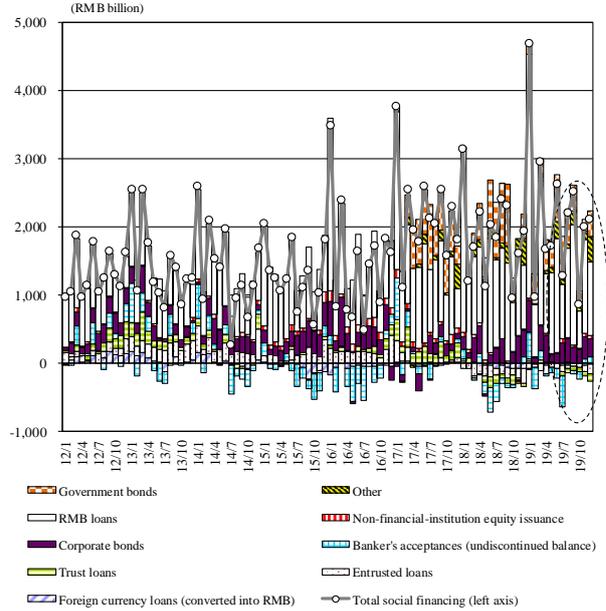
<http://www.safe.gov.cn/safe/2020/0107/15075.html>

Fig. 17: Financial institution lending; the money supply



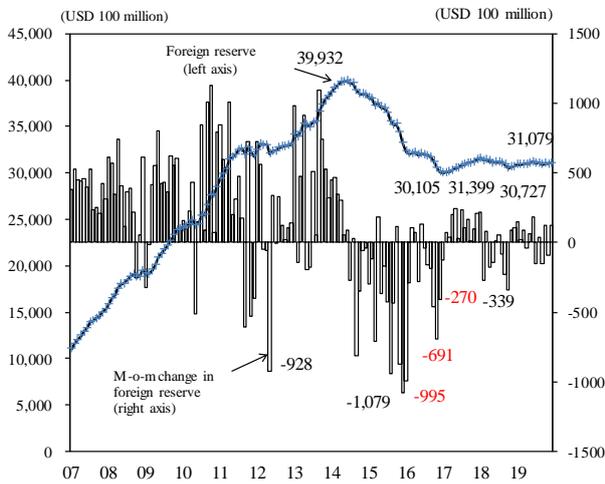
Note: The graph shows January and end-of-quarter figures up until 2015. The figure in the graph shows the y-o-y change in the outstanding loan balance for the most recent month.
Source: PBC, CEIC

Fig. 18: Total social financing (net increase and decrease)



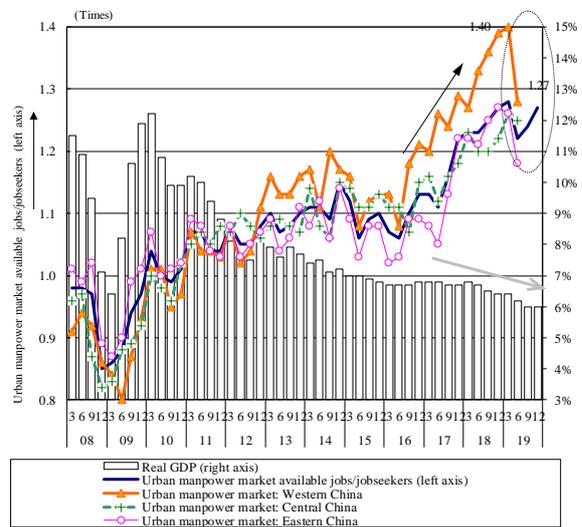
Source: PBC, CEIC

Fig. 19: Foreign exchange reserves



Note: The foreign reserve data shows the June 2014 at peak, end of 2016, 2017 and 2018, and the latest monthly figure.
Source: PBC, CEIC

Fig. 20: The jobs-to-applicants ratio



Source: Ministry of Human Resources and Social Security, National Bureau of Statistics of China, CEIC

2. The policy response: Attention will focus strongly on ‘preventing and defusing financial risks’ in 2020, the decisive year of the ‘Three Tough Battles’

▪ Recent signs of improvement and headwinds

During a press conference, Meng Wei, spokesperson for the National Development and Reform Commission (NDRC), was asked whether the improved indicators in December would fizzle out in the short term or whether they would lead to development over 2020. In response, Ms. Meng listed several positive trends, such as accelerated industrial production and total imports/exports, improved Purchasing Managers Index (PMI) data, and the flat m-o-m movements of the CPI and PPI. She added that the economy was progressing stably, with a series of policies starting to bear fruit, though she cautioned that the situation still needed monitoring.¹⁹ The y-o-y rally seen in the trade data for December 2019 was due in large part a reaction to the previous slump that had occurred following a surge in exports to the US in December 2018, so it remains to be seen whether this uptick will continue going forward. On the other hand, processing machinery orders and capital investment have bounced back on increased demand for semiconductors and so on.²⁰ Another optimistic factor for the economy in 2020 could be the boost that the phase one trade agreement between the US and China²¹ gives to investment and consumer sentiments.

However, a new headwind for the economy is the coronavirus outbreak that has spread out from Wuhan in Hubei Province. As of the morning of January 22, 440 people had been infected, with nine dying of pneumonia.²² If the virus mutates or spreads further from here on, this could limit economic activity and the movement of people, thus becoming a negative factor for the economy.

▪ Financial administration is focused strongly on ‘preventing and defusing financial risks’

A study of China’s policy measures for 2020 based on meetings held by the PBC and the China Banking and Insurance Regulatory Commission (CBIRC) reveals a strong awareness of the need to ‘prevent and defuse major financial risks’ as part of the ‘Three Tough Battles’ strategy for 2018–20, based on measures adopted by the Central Economic Working Conference in December 2019.²³

¹⁹ The National Development and Reform Commission, January 19, 2020, “国家发展改革委举行1月份新闻发布会介绍宏观经济运行情况并回应热点问题 (The National Development and Reform Commission Held a Press Conference in January to Discuss the Macroeconomic Management Situation and Answer Some Key Questions)”

http://www.gov.cn/xinwen/2020-01/19/content_5470858.htm

²⁰ According to an article in the January 9 electronic edition of the Nihon Keizai Shimbun entitled “Yaskawa Electric Corporation: Chinese Orders Apparently Bottomed Out Over September–November,” there are signs of increased capital investment activity in China in certain sectors, such as semiconductor memory for data centers, with orders for servomotors (the driving parts of processing machinery) for smartphones and base transceiver stations also growing ahead of the fully-fledged roll-out of 5G.

<https://www.nikkei.com/article/DGXMZO54225670Z00C20A1EA1000/>

²¹ A ‘phase one’ agreement was reached on December 13, 2019 and signed on January 15, 2020. This commits China to purchasing more US exports (by +\$200 billion over 2020–1 compared to 2017) and it also contains moves to tackle structural problems related to intellectual property and technology transfers, for instance. In a separate announcement, the US said it would half the tariff hike introduced in September 2019 (from 15% to 7.5% on around \$110 billion of goods) on February 14 (12:01am US Eastern Standard Time). Ministry of Commerce, January 16, 2020, “Announcement on Releasing the Phase One China-US Economic and Trade Agreement”

<http://english.mofcom.gov.cn/article/newsrelease/significantnews/202001/20200102930958.shtml>

²² China Net, January 23, 2020, “Government brief on coronavirus outbreak: source confirmed, no super-spreaders”

http://english.www.gov.cn/news/videos/202001/23/content_WS5e2959c9c6d019625c603dba.html

²³ For reference, see this writer’s article in “みずほ中国ビジネス・エクスプレス経済編 No. 96 (Mizuho China Business Express Economic Journal No.96).” The other two ‘tough battles’ are (1) eradicating poverty, and (2) tackling pollution.

https://www.mizuho-bank.co.jp/corporate/world/info/cndb/economics/express_economy/pdf/R422-0096-XF-0105.pdf

A PBC Work Conference held over January 2–3 outlined seven major tasks for 2020 (Fig. 21).²⁴ First up, the conference boldly announced it would “resolutely win the critical battle of preventing and defusing major financial risks,” thus indicating it viewed 2020 as a crucial year for achieving this goal. Specifically, the conference announced it would ‘forge ahead with the risk resolution of key financial institutions’ and take ‘special rectification actions against Internet financial risks.’ It also added that ‘the role of deposit insurance institutions will be further strengthened in risk resolutions,’ thus suggesting that deposit insurance will be applied at times. The conference also stated that ‘the local coordination mechanism for the Office of Financial Stability and Development Committee will be set up in an accelerated manner.’²⁵ As for financial reform and opening-up, the conference said it would continue 2019’s work of developing the bond market, adding that it would steadily pursue research into a digital fiat currency as part of fintech research and development.

A document released on January 11 after the 2020 National Banking and Insurance Industry Supervision and Management Conference²⁶ also emphasized the need to ‘resolutely win the critical battle of preventing and defusing financial risks.’ The document also announced several measures to prevent and defuse risk, such as: dismantling and preventing the resurgence of the high-risk shadow banking business; supervising, liquidating, restructuring and recovering capital from financial groups that infringe laws and regulations; prioritizing the extirpation of Internet lending risk; and establishing and strengthening standards for Internet insurance.

It also talked about boosting the positive impact of finance on the real economy and guiding funds to priority areas and weak sectors. Numerical targets included lowering financing costs for inclusive small and micro businesses by 0.5%Pt, for example, and boosting lending by the big five banks to inclusive small and micro businesses by at least 20% (Fig. 22).

²⁴ PBC, January 5, 2020, “PBC Holds 2020 Work Conference in Beijing”

<http://www.pbc.gov.cn/en/3688110/3688172/3956977/index.html>

²⁵ According to PBC, January 17, 2020, “Local Coordination Mechanism to be Established under the FSDC Office to Strengthen Financial Cooperation between Central and Local Government Institutions,” a local coordination mechanism to be established in provincial branches of PBC. Its members include major chiefs from the dispatched provincial institutions of China Banking and Insurance Regulatory Commission, China Securities Regulatory Commission and the State Foreign Exchange Administration, major chiefs of provincial financial regulatory authorities and chiefs of provincial development and reform authorities as well as fiscal authorities. The mechanism will be consulted by the office of Financial Stability and Development Committee under the State Council.

<http://www.pbc.gov.cn/en/3688110/3688172/3960539/index.html>

²⁶ China Banking and Insurance Regulatory Commission, January 11, 2020, “中国银保监会召开 2020 年银行业和保险业监督管理工作会议 (China Banking and Insurance Regulatory Commission Convenes the 2020 National Banking and Insurance Industry Supervision and Management Conference)” <http://www.cbirc.gov.cn/cn/view/pages/ItemDetail.html?docId=s884698&itemId=915>

Fig. 21: The PBC's major tasks for 2020 (2020 PBC Work Conference)

<p>(1) The PBC will keep the sound (neutral) monetary policy flexible and appropriate. Countercyclical adjustments will be strengthened to keep liquidity reasonably adequate and align the growth of money, credit, and AFRE (aggregate financing to the real economy) with economic development.</p> <ul style="list-style-type: none"> Continued efforts will be made to deepen interest rate liberalization. More work needs to be done to promote the replenishment of bank capital via multiple channels such as the issuance of perpetual bonds. With the market playing a decisive role in the exchange rate formation, the PBC will keep the RMB exchange rate basically stable at a reasonable equilibrium level.
<p>(2) The PBC will resolutely win the critical battle of preventing and defusing major financial risks.</p> <ul style="list-style-type: none"> The PBC will clearly define and strengthen the responsibilities of all relevant parties, and ensure that financial institutions take primary responsibilities, local governments assume responsibility for local risk resolution and first responsibility for safeguarding stability, financial regulatory authorities assume regulatory responsibility, and the PBC fulfills its responsibility as the lender of last resort to resolutely prevent moral hazards. The PBC will establish and improve recovery and resolution mechanisms, loss sharing mechanisms, and incentive and restraint mechanisms for sound financial institutions. The PBC will forge ahead with the risk resolution of key financial institutions in accordance with laws and regulations. Special rectification actions will be carried out on a continuous basis and in a bid to basically defuse existing Internet financial risks and to establish an effective long-standing regulatory mechanism. The PBC will also step up efforts to establish a long-standing regulatory mechanism for real estate finance. The role of deposit insurance institutions will be further strengthened in risk resolutions. The local coordination mechanism for the Office of Financial Stability and Development Committee will be set up in an accelerated manner.
<p>(3) Priority will be given to addressing the difficulties in financing and high cost of financing for MSEs, enhancing financial support for supply-side structural reform</p> <ul style="list-style-type: none"> Efforts will be made to improve the assessment and incentive mechanism for MSE loans and foster a favorable policy environment where financial institutions can lend with confidence, willingness and capacity. The PBC will make effective use of policy tools, including targeted RRR reduction, central bank lending and discount, macroprudential assessment (MPA) and credit information management to pragmatically facilitate and improve MSE financing. Credit support will be enhanced for key sectors and weak links. The PBC will focus on extremely poor areas and establish sound mechanisms of poverty reduction by means of financial support for industrial development, contributing to winning the critical battle of targeted poverty alleviation.
<p>(4) The macroprudential management framework will be improved in an accelerated manner.</p> <ul style="list-style-type: none"> The PBC will formulate policy guidelines for macroprudential management. The PBC will set up the macroprudential pressure test system. The PBC will accelerate the establishment of an integrated macroprudential management mechanism for cross-border capital flow in both RMB and foreign currencies. The PBC will gradually expand the coverage of macroprudential policies. The PBC will promote the introduction of regulatory and administrative measures for financial holding companies.
<p>(5) Financial reform and opening-up will be further deepened.</p> <ul style="list-style-type: none"> The PBC will advance the reform of financial markets and financial institutions. The PBC will actively develop the bond market and continuously promote infrastructure connectivity in the bond market. The PBC will strengthen coordinated regulation and development planning of financial infrastructure. Efforts will be made to deepen the reform of small and medium-sized banks and rural credit cooperatives and to further enhance the governance structure of policy banks. The PBC will advance RMB internationalization in an active and prudent manner. The PBC will push forward the reform of the foreign exchange administration system, and support pilot reform programs of foreign exchange administration, especially in the pilot free trade zones (FTZs) and the free trade ports. The two-in-one administrative framework of cross-border capital flow, namely macroprudential management plus micro regulation, will be improved.
<p>(6) Fintech research, development and application will be enhanced</p> <ul style="list-style-type: none"> The PBC will implement the Fintech development plan and establish a sound basic rule system for Fintech regulation. Steady steps will be taken to advance the research and development of DCEP (Digital Currency Electronic Payment). The PBC will expand the application of the global LEI (Legal Entity Identifier) system in China.
<p>(7) Financial services and management will be comprehensively improved (details omitted here).</p>

Source: PBC, January 5, 2020, "PBC Holds 2020 Work Conference in Beijing"

<http://www.pbc.gov.cn/en/3688110/3688172/3956977/index.html>

Fig. 22: The CBIRC’s major tasks for 2020 (2020 National Banking and Insurance Industry Supervision and Management Conference)

<ul style="list-style-type: none"> ● The CBIRC will resolutely win the critical battle of preventing and defusing financial risks. <ul style="list-style-type: none"> ▪ The CBIRC will dismantle and prevent the resurgence of the high-risk shadow banking business. ▪ The CBIRC will ensure that ‘housing is used for living in, not for speculation’ and it will strictly prevent inflows of funds into real-estate markets by strengthening regulations governing credit concentration levels and so on. ▪ The CBIRC will supervise, liquidate, restructure and recover capital from financial groups that infringe laws and regulations. ▪ The CBIRC will prioritize the extirpation of Internet lending risk and will establish and strengthen standards for Internet insurance. ▪ The CBIRC will assist the reform and restructuring of regional state-owned enterprises while also promoting economic structural adjustment and striving to eliminate hidden debt risk. ▪ The CBIRC will effectively prevent and eliminate the risk of external shocks, carry out stress tests for banking and insurance institutions, improve response measures, and stabilize market sentiments.
<ul style="list-style-type: none"> ● The positive impact of finance on the real economy will be enhanced and funds will be guided to priority areas and weak sectors. <ul style="list-style-type: none"> ▪ The CBIRC will announce measures for the supervision and evaluation of commercial bank financial services for small and micro enterprises. Financing costs for inclusive* small and micro businesses will be lowered by 0.5%Pt and lending by the big five banks to inclusive small and micro businesses will be boosted by at least 20%. ▪ Financial services for private-sector manufacturers will be strengthened. The CBIRC will provide specific support to cutting-edge manufacturing and industry groups, and it will focus on eliminating the liquidity problems of promising enterprises. ▪ The CBIRC will enhance financial support for social services and pork production. ▪ The CBIRC will assist in the battles of poverty alleviation and pollution control. ▪ The CBIRC will substantially develop green finance, sell financial products that support environmental protection, and expand the coverage and penetration rate of environmental pollution liability insurance.
<ul style="list-style-type: none"> ● Financial supply-side structural reforms will be comprehensively deepened and the level of external opening will be raised. <ul style="list-style-type: none"> ▪ Bank wealth management and trust business will be steadily upgraded, the third pillar of the pension system will be established and upgraded, and financial product structures and institutional systems will be improved. The CBIRC will create the foundations for the sustainable, healthy development of capital markets. ▪ Banking and insurance institution reforms will be deepened with a focus on reforming small- and medium-sized banks and rural credit cooperatives. ▪ The CBIRC will place the commercial vehicle insurance market on a sound footing while establishing a re-insurance market and expanding trials of disaster insurance. ▪ The level of external opening will be expanded further and the implementation of existing policies accelerated. ▪ Capital structures will be significantly improved. The CBIRC will promote capital participation in Chinese banks and insurance companies by domestic and external institutions with a history of cutting-edge management and good results in their main businesses. ▪ The CBIRC will improve corporate governance. The guidance of the Party will be fused organically with corporate governance to produce modern corporate systems with Chinese characteristics that obey G20 regulations. ▪ The CBIRC will comprehensively strengthen the qualitative supervision and management of assets and liabilities. Classification rules will be segmented and industry classification accuracy improved based on the current five classifications. ▪ The CBIRC will swiftly establish qualitative debt regulatory and administrative measures and it will increase the stability and integrity of banks and insurance companies, particularly small- and medium-sized financial institutions. ▪ The CBIRC will examine ways to improve banking and insurance recovery/resolution mechanisms and it will work with other departments to research ways to confirm lists of domestic systemically-important financial institutions. ▪ The CBIRC will identify institutions that do not classify as systemically-important institutions and it will apply separate regulations to these institutions. ▪ The CBIRC will improve mechanisms for orderly resolutions, resolution responsibility confirmation, and loss sharing; it will also form sound, orderly financial management systems.

Note: Inclusive financing: Financial structures that provide effective and comprehensive services to all layers of society

Source: China Banking and Insurance Regulatory Commission, January 11, 2020, “中国银保监会召开 2020 分年银行业和保险业监督管理工作会议”

<http://www.cbirc.gov.cn/cn/view/pages/ItemDetail.html?docId=884698&itemId=915>

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