

China Update

GTSF Investments Committee | Feb 02, 2023



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2023 Policy Overview

As stated in China's 2023 Government Schedules, this year's economic policies focus on the following:

1. Supporting the expansion of domestic demand and optimizing the demand structure, aiming to hedge the downside risks of the global market (including possible US recession and geopolitical risk factors).
2. Guaranteeing financing accessibility of private businesses and small, medium, and micro-sized enterprises, aiming to improve market expectations.
3. Preventing and resolving systematic risks, including the real estate bubble and persisting influence of the pandemic, aiming to maintain local governments' fiscal stability and restore market expectations.
4. Maintaining the stability of the RMB exchange rate, aiming to hedge potential international risks and shift economic focus back to domestic demand and supply.

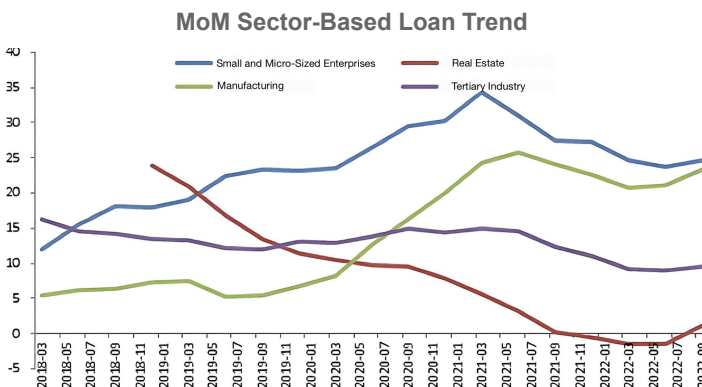
As a result, in 2023, though China's reopening may benefit the international supply chain, commodity trading, etc., China may focus on restoring the domestic market instead of global demand. Thus, it is worth not being overconfident about the restoration effect China's reopening can bring to the global economy.

Indicators	2023 China Major Economic Indicators Prediction							
	Historical		Expected		Projected			
	4Q22	Y22	1Q23	2Q23	3Q23	4Q23	Y23	
GDP YoY (%)	3.6	3.2	3.8	8.0	4.2	4.3	5.0	
Real GDP YoY (%)	5.0	5.9	5.8	9.0	5.9	6.4	6.8	
Value-Added YoY (%)	5.5	4.3	3.5	10.0	6.0	4.5	6.0	
Fixed Asset Investment YoY (%)	5.8	5.8	4.5	5.6	5.7	6.0	6.0	
Retail YoY (%)	3.0	1.4	5.0	15.0	5.0	4.0	7.0	
Import YoY (%)	2.0	9.5	(8.0)	(6.0)	(2.0)	1.0	(4.0)	
Export YoY (%)	(3.0)	2.2	(2.0)	0.0	8.0	5.0	3.0	
CPI YoY (%)	2.2	2.1	3.0	2.1	1.8	1.9	2.2	
PPI YoY (%)	(0.6)	4.4	(0.6)	(2.5)	0.0	0.7	(0.6)	
1-Year LPR (%)	3.7	3.7	3.6	3.5	3.5	3.5	3.5	
5-Year LPR (%)	4.3	4.3	4.2	4.1	4.1	4.1	4.1	

Economic Overview

According to the People's Bank of China, in January 2023, 718 billion new loans were issued, with a 135 billion YoY increase. The YoY growth rate of M2 increased by 0.8% to 12.6% compared to December 2022. Concerning loan types, corporate loans' total amount and industrial distribution were healthy, while residential loans still needed to be repaired. In terms of the loan period, medium- and long-term loans increased by 513 billion dollars, and short-term loans increased by 220 billion dollars, with monthly increments reaching a new historical high.

The high growth of medium- and long-term loans reflects the gradual successful implementation of economic recovery policies in the second half of 2022. The optimistic growth of short-term loans reflects the gradual improvement of production and operation in small and micro-sized enterprises. However, retail loans only increased by 37.7 billion dollars in January, lacking an 87.9 billion YoY increment, indicating that real estate sales are still in repair. Regarding the exchange rates, the RMB spot exchange rate appreciated by nearly 2.8% against the dollar in January, which peaked since January 2018.



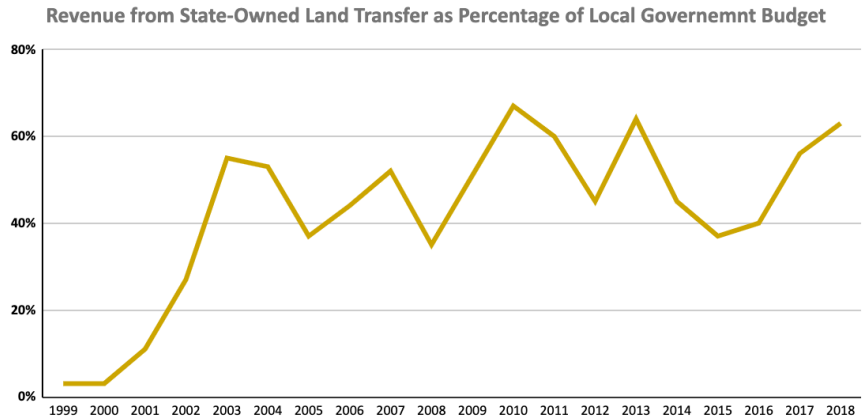
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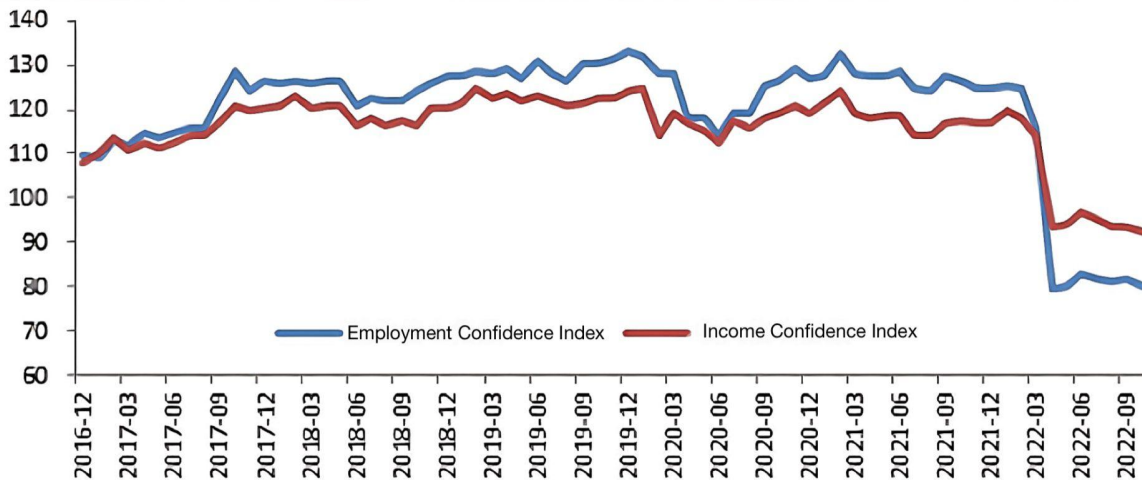
Resolving Systematic Risk: Tracing Back to Evergrande Liquidity Crisis

Evergrande liquidity crisis, the start of China's real estate crisis, is essentially a disguised budget constraint formed by mutual collateral guarantees among members within the pyramid holding structure of most large financial institutions (FIs). Before the financial crisis in 2008, most Chinese FI asset allocations focused on the manufacturing sector. However, due to the 4 trillion pumped into the Chinese market after 2008 and the Land Finance fiscal policy approach, FIs have shifted their focus to real estate lending. After more than a decade of real estate credit policy backup from local governments, FIs are now used to the risk control approach based on collateral value. Many small and medium-sized FIs are losing their ability to accurately assess the risk of other real economy customers, resulting in the homogenized real-estate-centered holding structure and mutual collateral guarantees. The number of large-cap FIs involved in Evergrande's debts is as high as 128, which shows the convergence of allocation in the industry.

The governance failure manifested by excessively associated credit and other irregular capital appropriation has become an essential source of financial risks in recent years. Over the past year and a half, the Chinese government has attempted to quell a systematic financial crisis resulting from the Evergrande liquidity crisis and a plunge in market expectations brought about by the apparent real estate bubble. Given that the market expectations of the Chinese economy and the healthiness of local government's revenue are closely tied to real estate, one of the most critical guidelines mentioned in the 2023 forecast is to ensure that real estate properties are delivered as promised. Under this policy guidance, China's real estate industry may recover slowly in 2023.



Market Expectations Dropped Drastically in 2022



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