



FOR PROFESSIONAL INVESTORS – 2 January 2024

Chi Flash

PBOC NEEDS TO EASE MORE AGGRESSIVELY AND FOR LONGER

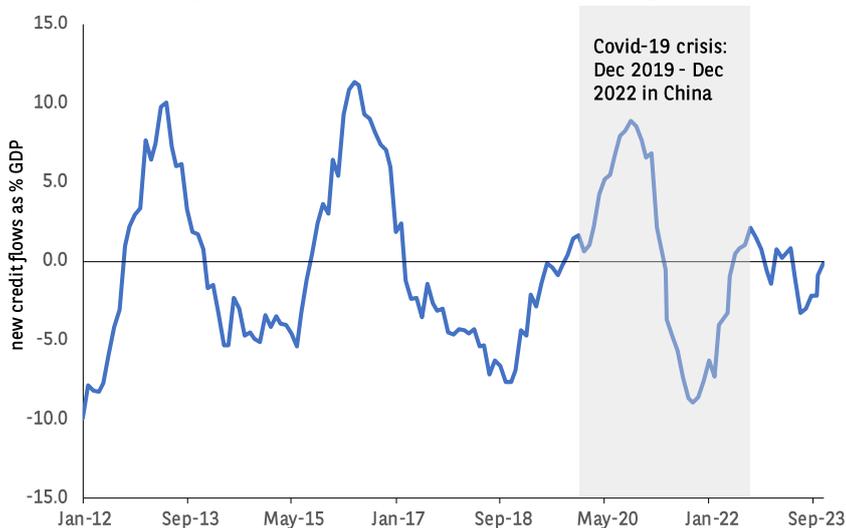
If you want a thing done well, do it yourself.

Napoleon Bonaparte

Recent [market research](#) found that China's monetary transmission mechanism has lost effectiveness since the pandemic. The absence of a sustained recovery in the credit impulse (i.e., new credit flows to the economy as a share of GDP), a leading economic indicator, despite rounds of monetary easing, underscores the severity of this problem (Exhibit 1).

Exhibit 1:

Monetary easing has not boosted China's credit impulse



sources: CEIC, UBS, BNP Paribas Asset Management 26 Dec 2023



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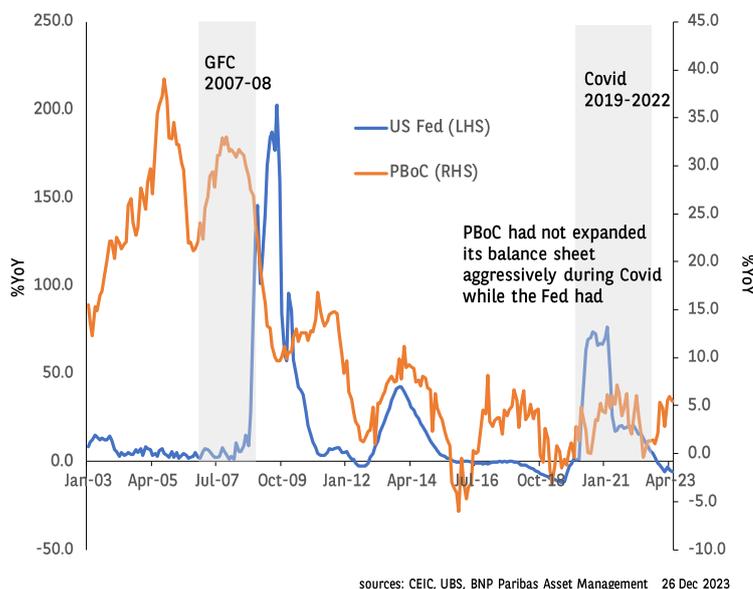
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Policy problems

Three years of Zero Covid Policy, some sector-level regulatory tightening (notably on the tech sector) between 2020 and 2022, and chronic weakness in the property sector since the pandemic have destroyed public confidence and blunted the policy easing effect on reviving growth momentum and 'animal spirit'. Hence, private consumption and investment spending have failed to respond to the easing measures.

Beijing's two-year long 'incremental easing' approach has not helped turnaround the situation, as it is insufficient especially when the monetary transmission is impaired. Throughout the pandemic, the PBoC had not expanded its balance sheet aggressively to pump-prime the economy while its developed market counterparts engaged in quantitative easing through massive central bank balance sheet expansion (Exhibit 2).

Exhibit 2:
Central bank balance sheet growth



China also refrained from making any fiscal transfer to the Chinese consumer during the pandemic while governments in the developed markets made massive fiscal transfers to support consumption. The difference in this fiscal policy approach also explains China's lack of consumption recovery post-Covid-19 and robust consumption growth in the developed markets.

Implications

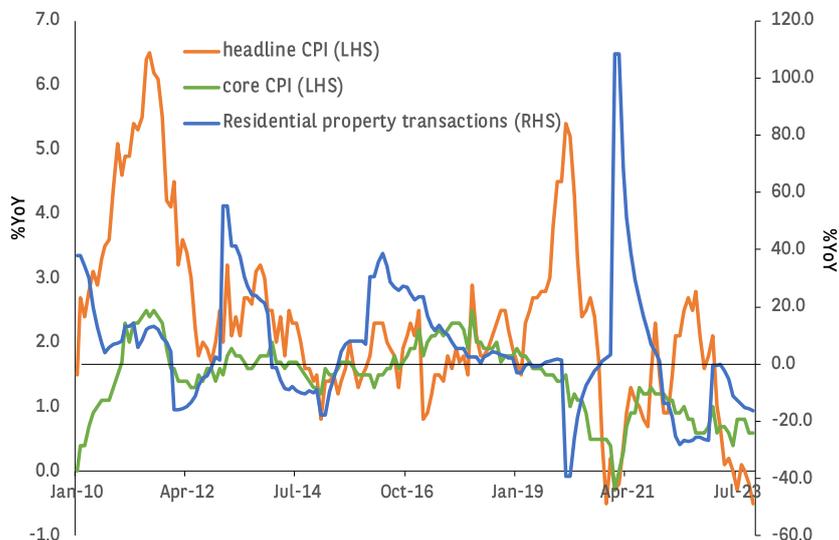
Granted, Beijing wants to quit the old debt-fuelled supply-expansion growth mode. So, it is willing to tolerate slower growth by focusing on structural reforms and debt reduction. However, this deflationary policy mode runs the risk of mis-calculating the economy's resilience to negative shocks and deprives it of recovery momentum! The loss of monetary transmission efficacy argues that the PBoC would have to pursue more aggressive easing and sustain it for a longer period than in the previous cycles to achieve the same growth impact.

Realising that the property market woes are spreading the risk of deflation (Exhibit 3), Beijing has ramped up policy easing to stabilise the property sector, notably by accelerating urban village renovation and social housing construction and increasing financing for viable non-state-owned developers. The PBoC has also announced a plan to inject more than RMB1 trillion to fund property and infrastructure investment in major cities and has drawn up a 'whitelist' of 50 developers for credit support.

The risk, however, is the timing of implementation. Many of these measures are yet to be carried out at the time of writing.

Exhibit 3

China's property transaction contracting, CPI flirting with deflation



sources: CEIC, UBS, BNP Paribas Asset Management 26 Dec 2023

Market outlook

The cyclical outlook for Chinese assets in 2024 hinges upon Beijing's policy reaction to the feeble economic growth momentum. As I argued earlier, an ['economic pain point'](#) might have been reached and prompted Beijing into more assertive easing than it had done over the past two years. The loss of monetary transmission effectiveness reinforces such argument.

If Beijing can sustain its assertive easing in the coming months to repair confidence and convince the markets that China's outlook is improving, there is a fair chance of a sustained rebound in Chinese economic growth and stock market in 2024. If not, we could see Chinese growth stuck in low gears, causing weakness in China's asset prices.

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