

China: A strong signal on 2023 reopening

Bottom line:

After the Politburo Standing Committee meeting yesterday (Nov 10), the government released “20 measures” to improve its Covid control methods. This is essentially a change in Covid control guidelines, similar to the one in late June where quarantine periods were shortened and definitions of risk-districts were standardized. We still see downside risks to near-term growth as a number of major cities are reporting sharply rising Covid cases, the zero-Covid policy will stay in place during the winter, and the changes to the quarantine period from “7+3” to “5+3” are marginal in terms of economic impact. However, the signal that the top leadership is preparing for an exit from three years of zero-Covid policy at some point next year - in our view, most likely soon after the “Two Sessions” are held in March - seems clear and important.

Main points:

1. What happened? On Nov 10, the Politburo Standing Committee held a meeting chaired by President Xi discussing China’s Covid situation. Although still emphasizing the need to continue implementing the “dynamic zero-Covid” policy, especially during the winter flu season, this meeting placed less emphasis on “calculating the political cost” and more emphasis on optimizing Covid control measures to reduce the negative impact on the economy. In addition, it was the Politburo Standing Committee’s first time to mention focusing on improving the effectiveness of Covid vaccines and increasing vaccination of the vulnerable population. On the following day (Nov 11), the government released the details of “20 measures” aimed at implementing the zero-Covid policy in a more “scientific and targeted” manner (Exhibit 1). Key changes include:

- *On individual quarantine:* The quarantine requirement for close contacts and inbound travelers will be shortened from “7-day centralized quarantine + 3-day home health-monitoring” to “5-day centralized quarantine + 3-day home quarantine”. Although the National Health Commission (NHC) maintains its requirement to identify close contacts in a timely and accurate manner, close contacts of close contacts will no longer need to be identified. The requirement for domestic travelers from high-risk districts has been changed to “7-day home quarantine” from “7-day centralized quarantine” previously.
- *On regional Covid risk management:* The classification of Covid risk districts has been simplified to a two-tier regime with “high” and “low” from the three-tier one (“high”, “medium” and “low”), to minimize the amount of the population

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under restrictions. High-risk districts will be downgraded to low-risk districts if no new cases for five consecutive days, vs at least ten days.¹

- *On inbound international travel:* The government will end the “circuit breaker” mechanism for airline flights. This mechanism used to require airline companies to temporarily ban specific routes into China for one-to-two weeks, depending on how many Covid cases were identified among passengers of the specific flights. Only one Covid test will be required (vs two previously) within 48 hours before boarding. PCR tests with CT value at below 35 will be adopted, vs 35-40 previously.²
- *On medical preparations:* The guidance emphasized scaling up storage of Covid treatment drugs, including traditional Chinese medicine. To expand hospital capacity, the government would not only prepare more ICU beds but also train doctors and nurses for Covid treatment. Moreover, the government will set up a differentiated treatment guidance depending on the severity of Covid symptoms to avoid overcrowding medical facilities and to protect the vulnerable sections of the population, such as the elderly. Importantly, the guidance stated the intention to substantially increase the elderly vaccination rate and to further develop and approve Covid vaccines.

Taken together, the “20 measures” introduced today suggest that the government would like to (1) reduce the negative impact of China’s zero-Covid policy on mobility and economic activity domestically; (2) facilitate more engagement with the rest of the world and inbound FDI by cutting restrictions on inbound travel; and (3) make necessary medical preparations for an eventual and orderly exit from the zero-Covid policy.

Exhibit 1: Key differences between the 9th edition of Covid control guidelines and the “20 measures”

Key dimension for comparison	9th version (Jun 2022)	20 measures (Nov 2022)
Quarantine time for close-contact of Covid cases or inbound travelers	Centralized quarantine for 7 days + home health-monitoring for 3 days	Centralized quarantine for 5 days + home quarantine for 3 days
The classification of risk districts	Applying the high/mid/low-risk district classification nationwide	Applying the high/low-risk district classification nationwide
Criteria for the risk-level downgrading	No local case over consecutive 7 days for downgrading from high- to mid-risk districts, and no local cases over consecutive 3 days for downgrading from mid- to low-risk districts	No local case over consecutive 5 days for downgrading from high- to low-risk districts
Guidelines for international flights	International flight “circuit breaker” mechanism remains in place*	Removing the “circuit breaker” mechanism for international flights
Treatments for close contacts of close contacts	Home quarantine for 7 days	Close contacts of close contacts will no longer be identified and traced

*This mechanism requires airline companies to temporarily ban specific routes into China for one-to-two weeks, depending on how many Covid cases were identified among passengers of the specific flights.

Source: Government websites, data compiled by Goldman Sachs Global Investment Research

2. Limited implications for near-term activity

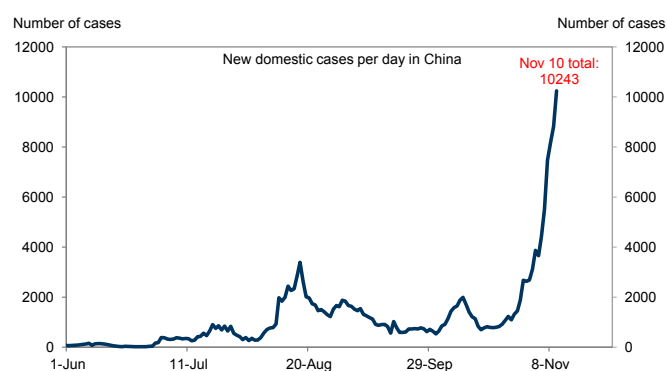
China’s Covid situation has become more concerning in recent weeks. Daily new cases

¹ In the past, high-risk districts were downgraded to medium-risk districts if no new cases for seven consecutive days, and medium-risk districts were downgraded to low-risk districts if no new cases for three consecutive days.

² The higher the cycle threshold value (CT value), the more sensitive the PCR test is and the more likely the test result would be positive.

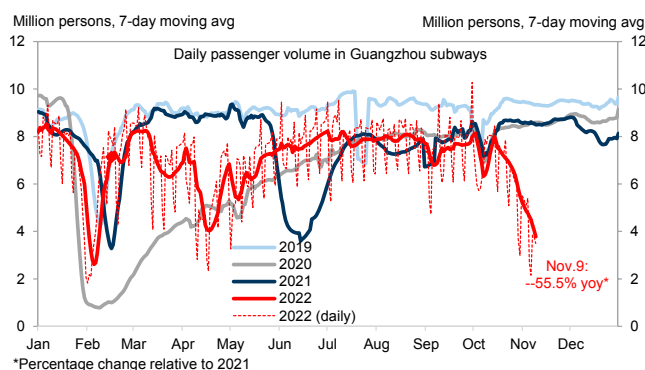
rose to around 10k on Nov 10, with Guangzhou and Chongqing recently imposing district-based lockdowns ([Exhibit 2](#) and [Exhibit 3](#)). The GDP share of cities with high/mid-risk districts remained elevated at 46% currently, and our effective lockdown index (ELI) is hovering above 30 in recent weeks (at a scale of 1-100, with 100 referring to the strictest). Note Guangzhou accounted for 2.5% of national GDP, and is a production base for auto, electronics and petrochemicals. Guangzhou port is also one of the major ports in China. If we include other Covid-hit cities such as Chongqing (2.5% of national GDP), Zhengzhou (1.2%) and Fuzhou (1.0%), the economic impact of ongoing Covid restrictions could be larger, imposing downside risk to near-term growth outlook.

Exhibit 2: Covid cases rose sharply in recent days



Source: NHC, CEIC

Exhibit 3: Subway ridership in Guangzhou fell in recent days due to local lockdown



Source: Wind, Goldman Sachs Global Investment Research

Despite the fine-tuning in Covid control measures today, policymakers reiterated their stance to “firmly stick to the dynamic zero-Covid policy”, and acknowledged the risk that “Covid resurgence could escalate further”, especially in the middle of the winter flu season and when the Lunar New Year travel season begins in two months. As [discussed](#) previously, we expect the central government would need local officials to stay vigilant on Covid control until the country has done all the required medical preparations (e.g., vaccinating its elderly population, stockpiling Covid pills, and expanding medical facilities) as well as communication preparations (e.g., alleviating fears of Covid infections among the population). Although we see the rationale in lifting restrictions such as requiring residents to do multiple PCR tests within a day, the impact of such changes on domestic economic activity is likely to be limited as long as the zero-Covid policy remains.

3. A strong signal of a potential reopening next year

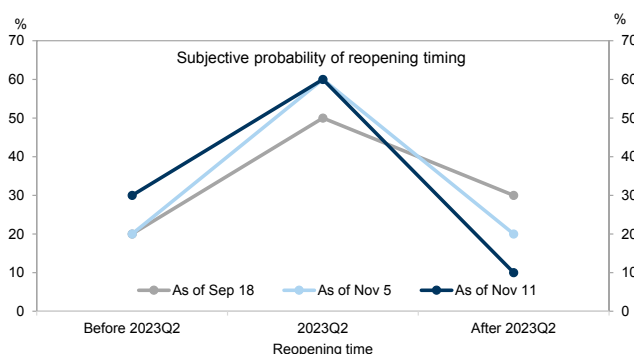
While the effective relaxation of the Covid control policy stance after today’s announcement seems marginal, we see this fine-tuning of the policy as a strong signaling effect. It suggests policymakers are now focused on optimizing Covid control policies and have started the preparation work for more relaxation of Covid control policies in the future and eventual reopening. Specifically, it is worth highlighting that measures on expanding medical capacity, promoting medical campaigns, and enhancing supply chain security may have followed Hong Kong’s experience in Covid controls. Indeed, Vice-Minister of the National Health Commission (NHC), Cao Xuetao, [endorsed](#)

Hong Kong's experience of Covid control this morning (Nov 11).

We continue to expect policymakers to gradually start reopening in 2023Q2, after the Chinese New year and Two Sessions next year, with a subjective probability of 60%. Today's announcement of a marginal relaxation of Covid control policies has lowered the risk of delayed reopening (till after 2023Q2) in our view ([Exhibit 4](#)). We therefore adjust our subjective probability assessment of reopening before 2023Q2 to 30% (vs 20% previously), and lower the probability of reopening after 2023Q2 to 10% (from 20% previously).

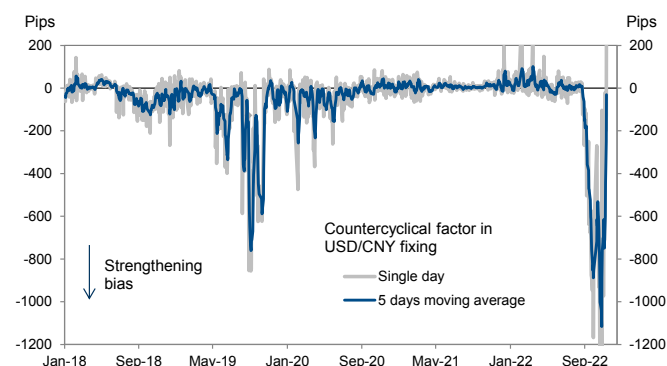
Markets demonstrated "risk-on" sentiment in response to today's announcement. CNH appreciated by around 1000pips against USD from 7.19 to 7.09 (as of this writing), CGB sold off (especially at the front end), and the equity market rallied. We see downside risk (risk of a stronger currency) to our 3-month forecast of USDCNY at 7.40. After the softer-than-expected US inflation print on Nov 10, the broad USD weakened and CNH appreciated. This morning, the PBOC posted the first positive countercyclical factor (CCF) in the CNY fixing (likely signaling their intention of a weaker currency) since late August this year, which in our view suggests that the PBOC probably wants to avoid a too-strong currency amid slowing export growth.³ Separately, President Xi will meet with US President Biden at the G20 summit in Bali on Nov 14. It will be the first in-person meeting since Biden became president, following their phone call in July this year. According to the White House, they will discuss "*efforts to maintain and deepen lines of communication*" between the two countries.

Exhibit 4: We continue to expect 2023Q2 reopening



Source: Goldman Sachs Global Investment Research

Exhibit 5: PBOC fixed CNY on the weaker side for the first time since late August



Source: Bloomberg, Goldman Sachs Global Investment Research

³ We caution that CCF on a single day might contain some noises and we will closely monitor CCF in the next few days for clearer signals by the PBOC.

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Reg AC

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