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SPECIAL ALERT

September 24, 2024

China's "Whatever It Takes" Moment?

In This Report

Yesterday, the Chinese central bank, together with financial regulators, announced a slew of stimulus measures, triggering a sharp rebound in Chinese stocks. This move aligns with our expectation that the PBoC will follow the Federal Reserve with more easing measures, as discussed in today's report.[1] What surprised us was how aggressive the PBoC's steps were to prop up the stock market.

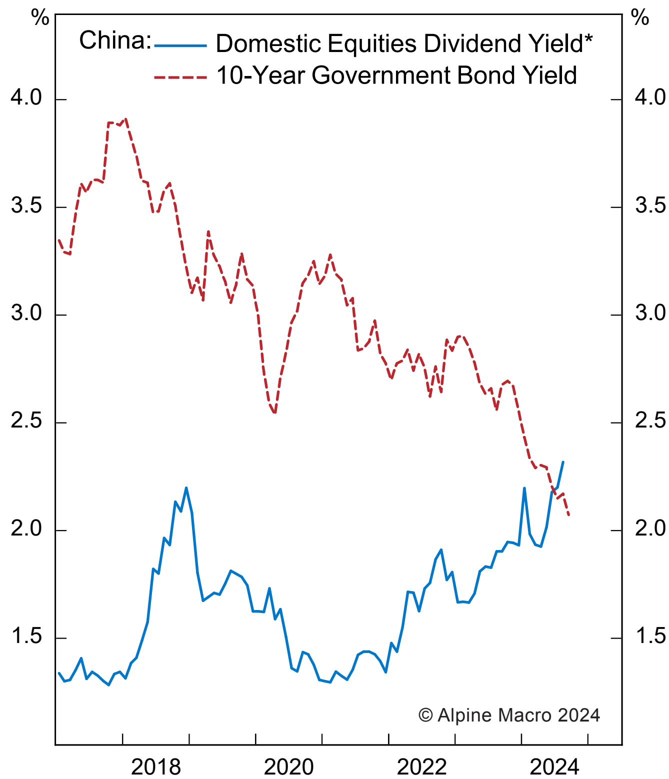
We have been holding Chinese stocks and over-weighting China in an EM equity portfolio. The latest policy moves suggest more gains ahead.

Beijing Is Blinking

What sets the latest reflation drive apart from the one earlier this year is a greater sense of urgency. After months of poor performance, any hope that the economy could recover on its own should have waned. Beijing is very concerned about growth and the risk of deflation, and must take on more heavy-lifting to boost the economy.

Meanwhile, the government sees the onset of the Fed easing cycle as an opportunity to reflate more aggressively without worrying about the exchange rate. The tone of central bank governor Pan Gongsheng is more determined and aggressive than before, and the measures are much broader, raising the possibility that Beijing may stimulate in a more persistent manner.

Chart 1 PBoC Aims For Higher Stock Prices



*Source: MSCI

1 Alpine Macro *EM & China Strategy* "Central Bank Decisions: The Fed, Brazil, And South Africa" (September 24, 2024).

Three Arrows

There are numerous news reports detailing Beijing's recent measures. Broadly, the PBoC package can be summarized as follows:

First, the PBoC announced additional policy rate cuts and a reduction in the reserve requirement ratio (RRR) to boost bank liquidity and increase loanable funds. RRR cuts are equivalent to QE with limitations and will release RMB 1 trillion in liquidity. However, these moves alone are insufficient to turn around the economy, as the contraction in loans stems from extremely weak demand rather than banks' unwillingness or inability to lend.

Second, on housing, it has long been our view that Beijing's easing measures in recent years have only made housing policy less restrictive, rather than outright stimulative. The latest changes are much more aggressive. Regulators no longer discriminate against investment demand for properties and are pushing commercial banks to lower interest rates on existing mortgage borrowers. The PBoC expects a 50 basis-point reduction on existing mortgage loan rates, an unprecedented move, with estimated interest expense savings of RMB 150 billion. The old mantra "housing is for living, not for speculating" is now obsolete.

The third is on the stock market. The PBoC will establish a swap facility to give non-bank financial institutions access to RMB 500 billion in funding to invest in stocks. Additionally, the central bank has set up a RMB 300 billion special relending program, allowing listed companies and major shareholders to borrow from banks with collaterals such as government bonds for share buybacks and stake increases (Chart 1). PBoC Governor Pan Gongsheng hinted at the possibility of expanding these programs, signaling an open-ended commitment akin to a "whatever it takes" moment.

With these measures, authorities now seem to view rising stock prices as a key confidence indicator for the economy. This marks a sharp policy U-turn from Beijing's previous strategy of shifting focus from the "virtual" to the "real" economy. Under that strategy, sectors like internet, real estate, and capital markets were targeted in crackdowns, while banks were mandated to serve the "real" economy, particularly manufacturing. That era appears to be decisively over.

These measures can be viewed as the PBoC's "three arrows" targeting weak business and consumer confidence, inadequate demand, and rising deflation risk. Whether these measures will be enough to spur the economy remains to be seen.

Our Assessment

They were announced few days after this report was released

Although no new fiscal measures were announced in this stimulus package, it's important to note that the line between China's fiscal and monetary policies is often blurred. Many of the PBoC's actions, such as the swap facilities and plans to bolster capital for six major banks to ease net interest margin pressures, should be viewed as fiscal measures.

Overall, we have long argued that the central bank and government should aggressively expand their balance sheets to shore up demand (Chart 2). The latest measures are clearly a step in the right direction.

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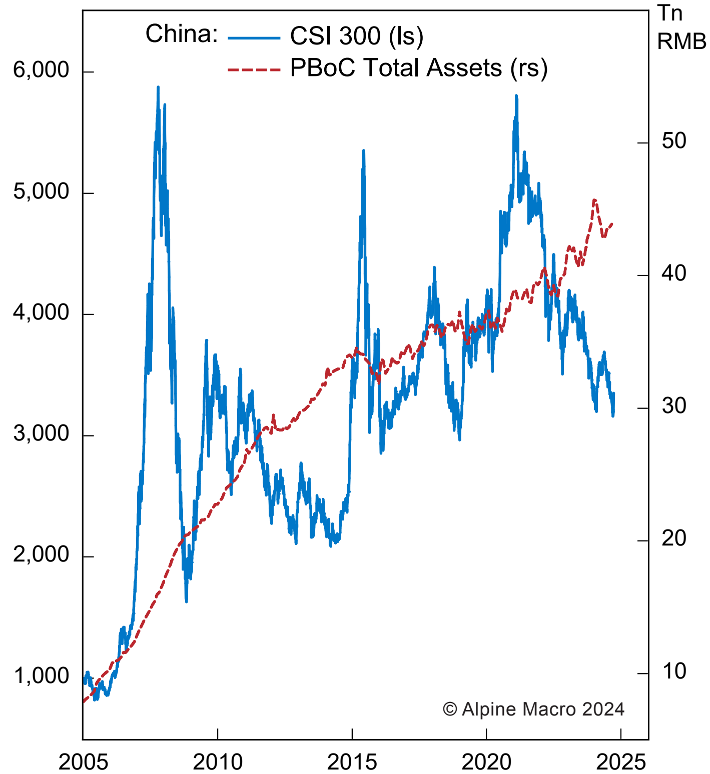
It is encouraging that Beijing seems to be waking up to mounting economic pressures and social tensions. We expect these measures to trigger a sizable rebound in Chinese stocks, and it is not too late to join the rally. However, for this rebound to evolve into a sustained bull market, Beijing must do more to fundamentally revitalize the economy, as discussed in our earlier report.[2]

Similar to Japan's "Abenomics," any plan to revitalize China's economy must include another set of "three arrows":

- Major stimulus measures to boost demand.
- Decisive debt-relief programs for local governments and a new incentive structure to mobilize technocrats toward a pro-growth agenda.
- A credible commitment to domestic private enterprises and foreign investors that China remains dedicated to liberal reforms.

Beijing's policy calendar suggests that significant moves may occur towards the end of the year, during the Politburo meeting and the Central Economic Work Conference. We will follow up on these issues in the coming weeks.

Chart 2 PBoC Expands Balance Sheet



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2 Alpine Macro *EM & China Strategy* "Is China In A Slow-Motion Implosion?" (August 27, 2024).

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