

China Economic Report: 2023 NPC Review

Conservative and Realistic Government's Targets & Stronger Leadership of CPC Under Mounting Tension With US

Summary

- Government set conservative and realistic targets for 2023 at NPC (National People Congress).
- We judge that government should give priority to stable inflation than higher economic growth.
- Institutional reform of Communist Party of China (later, CPC or Party) aims to beef up leadership of CPC over financial and science technology under stricter sanctions by US.
- New Party institution reform is a double-edged sword; great success if assignment of right persons and adequate use of stronger power vs serious failure if not.
- Among institution reform of government, we positively evaluate a centralized control over banking institutions from a viewpoint of financial risk management
- Government personnel change was overall within expectation, because we acknowledged a hierarchy of CPC executive members at First Plenary Party Central Committee on 23 October 2022.
- We would like to highlight 1) stronger power of Xi Jinping and 2) importance of technocrats from the Party and government personnel.

1. Government's Targets

Conservative and realistic targets

Central government set its economic growth target at around 5% for 2023, lower than around 5.5% for 2022 and market consensus, although government has acknowledged current economic recovery.

Exhibit 1: Government's Target Figures at NPC

	2023	2022
real GDP growth	around 5%	around 5.5%
fiscal deficit of GDP	around 3%	around 2.8%
local gov special bonds	RMB3.8tri	RMB3.65tri
CPI inflation	around 3%	around 3%
new employed in urban	around 12mn	not less than 11mn
unemployment rate in urban	around 5.5%	not more than 5.5%

Source: NPC

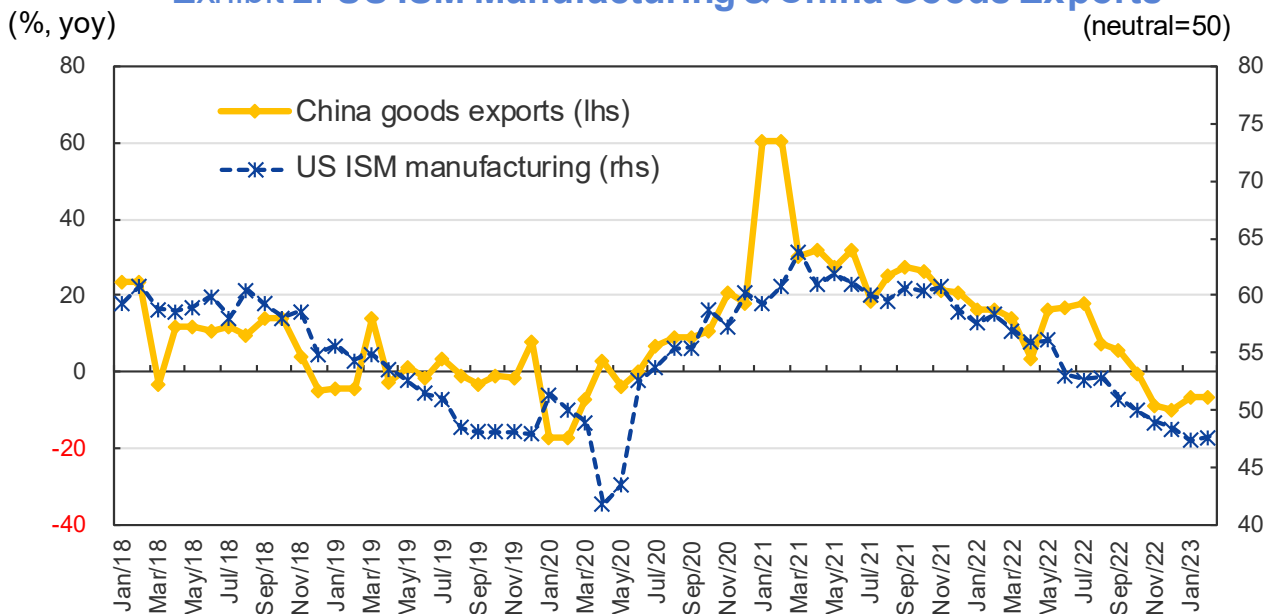
We would like to highlight three reasons for the conservative growth target.

First, government would not like to guide rapid economic growth pace, which should cause higher CPI inflation. In fact, central government set CPI inflation target at around 3% for 2023, the same as for 2022, in line with some conservative growth target. There are still many poor people in China. At least 80% of population have not reached income tax threshold RMB5,000 (around USD730) per month. In addition, at 2020 NPC, Premier Li Keqiang mentioned that average monthly salary stayed at around RMB1,000 for 600mn poor people in China. In other words, annual income was USD1,740, much lower than per capita of USD10,525 in 2020. We judge that government would like to protect purchasing power of many poor people, who cannot enjoy higher economic growth.

Second, export-oriented manufactures should face headwinds under correction in US manufacturing sector. We have observed downside trend of goods exports since 3Q22. Given our view of weak US manufacturing sector for the rest of 2023, we cannot bet on upside exports growth on yoy in 2023.

Third, US government and Congress should beef up sanctions over China. Both Democrat and Republican parties in US have acknowledged that they can obtain more supports from constituents in advance of Presidential election in 2024, if they show intent to attack China.

Exhibit 2: US ISM Manufacturing & China Goods Exports



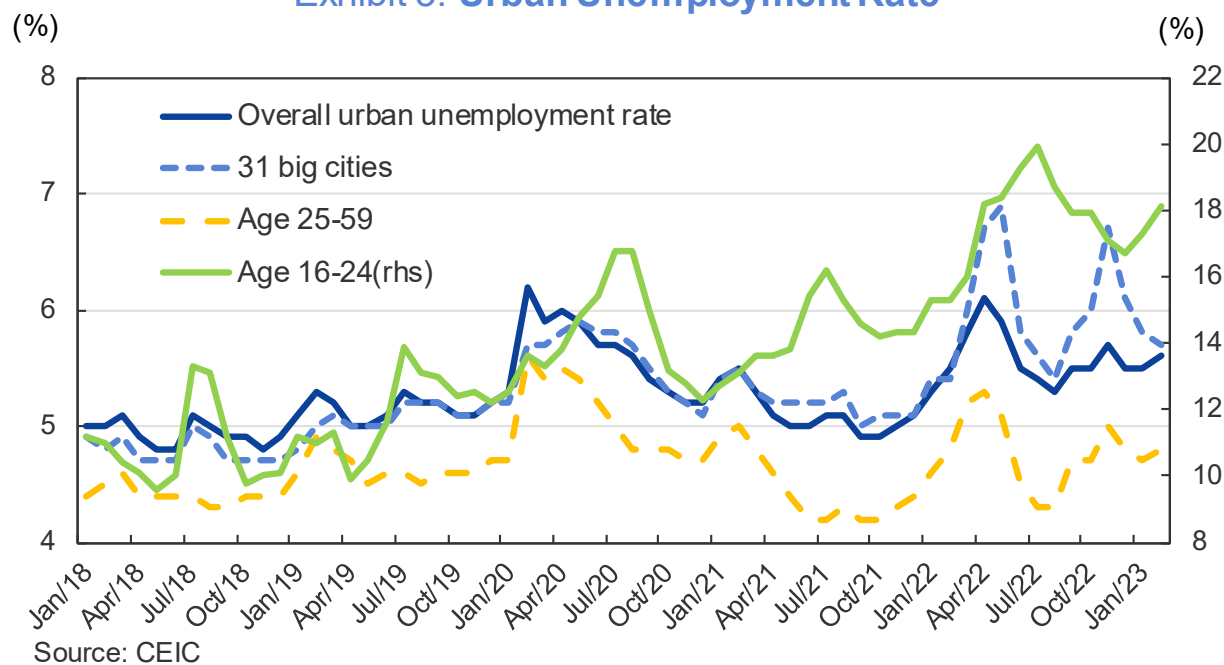
Source: CEIC

Note: Average growth for Jan-Feb in China exports to delete Chinese New Year Holidays seasonality

Given these three reasons, we would like to maintain our economic growth outlook at 5.3% for 2023.

In addition, we would like to highlight some softening stance for labor related target. In fact, government set surveyed unemployment rate in urban areas at around 5.5% for 2023, milder than not more than 5.5% for 2022. We can raise three factors as main background for the softening labor target. First is weak exports and second is sanctions by US. As the third factor, we can point out unemployment problem for young generation, which may turn more serious in 2023, because the number of university graduates is expected at 11.58mn in 2023, larger by 0.82mn than in 2022.

Exhibit 3: Urban Unemployment Rate



2. Policy Stance

Less aggressive fiscal policy stance

Central government set fiscal deficit target of GDP at around 3% for 2023, more expansionary compared with around 2.8% for 2022. Revenue outlook at 6.7% for 2023 in general account seems rational given some acceleration of nominal GDP growth rate. Expenditure outlook at 5.6% for 2023 against actual for 2022 was lower than 8.2% for 2022, although the outlook seems reasonable to stimulate the economy. In general accounts, government set fiscal deficit target at 4.5% of GDP for 2023, smaller than 4.7% for 2022. Government would like to depend less on special funds and contribution from government agencies. We can recall that PBOC contributed more than RMB1tri to finance the fiscal budget.

In addition, central government set limit for local government special bonds at RMB3.8tri for 2023, larger than RMB3.65tri for 2022. More accurately, central government allowed local government to issue special bonds under carry-over quotas of RMB500bn for 2022. In that sense, local government issued their special bonds at RMB4,038.4bn for 2022, within the amended budget of RMB4.15tri. Theoretically, given unused budget at RMB1,146.3bn for 2022 (difference between special bonds budget outstanding and actual outstanding at end of 2022), central government can hold some buffer in a case of serious economic crisis.

Central government set defense budget at RMB1,553.7bn, for 2023. We have observed upside trend of defense budget share out of total expenditure budget since 2019 reflecting mounting tension with US. Going forward, we judge that further increase in defense budget should cause a challenging factor for fiscal consolidation in medium and long term.

Ending universal accommodative monetary policy stance

In its 2023 plan for National Economy and Social Development, central government reiterated the same monetary policy stance as Central Economic Work Conference. Government would like to seek more precise and stronger measures under prudent policy stance. Given economic recovery scenario for 2023, we judge that universal accommodative monetary policy represented by rate cut should be over. In addition, in a case of further USD appreciation phase, it should be more difficult for government to take additional rate cut, because government is afraid of a vicious spiral between RMB depreciation and capital outflow. We do not deny potential cut in RRR (reserve requirement ratio) to ease upside pressure for interbank interest rates caused by large gap between supply and demand in interbank markets, because change in RRR shall not express policy stance for government.

Exhibit 4: China Fiscal Budget at NPC

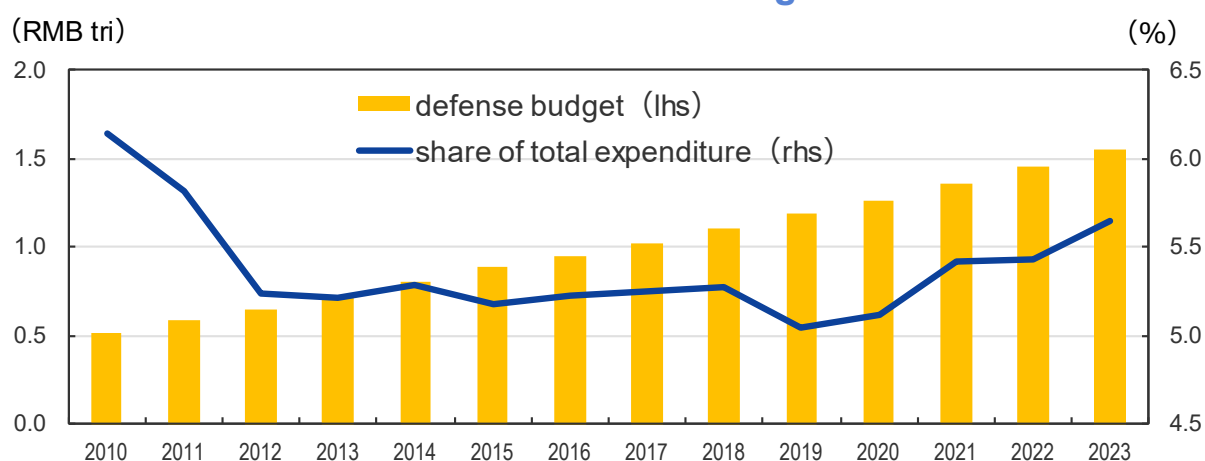
	2022		2023	
	A	B	vs A	vs B
	budget	actual	budget	
total revenue	23,343	22,824	23,633	23,633
(%, yoy)	8.9	6.5	1.2	3.5
revenue (general account)	21,014	20,370	21,730	21,730
(%, yoy)	3.8	0.6	3.4	6.7
from government funds etc	2,329	2,454	1,903	1,903
total expenditure	26,713	26,194	27,513	27,513
(%, yoy)	6.9	4.8	3.0	5.0
expenditure (general account)	26,663	26,061	27,513	27,513
(%, yoy)	8.2	5.8	3.2	5.6
from government funds etc	50	134	0	0
fiscal balance	-3,370	-3,370	-3,880	-3,880
(% of GDP)	-2.8	-2.8	-3.0	-3.0
fiscal balance(general accounts)	-5,649	-5,691	-5,783	-5,783
(% of GDP)	-4.7	-4.7	-4.5	-4.5

Source: NPC

Note: Both growth figures for 2022 against actual figures for 2021

In addition, we can highlight upside performance of defense budget. The share of defense budget of total expenditure budget has shown an increasing trend since 2019 reflecting mounting tension between Sino-US governments. It should be difficult for China government to shift to fiscal consolidation.

Exhibit 5: Defense Budget



Source: NPC and CEIC

3. Institution Reform

Stronger leadership of Party over Finance and Science Technology under stricter sanctions by US

Central Committee of CPC held the second plenary session on 26-28 February, before NPC. At the session, Central Committee approved a “plan for the reform of CPC and government institutions” to beef up leadership of Party.

CPC revealed total contents about the institutional reform on 16 March, after closing of NPC on 13 March. We should give more attention to Party institutional reform than government institutional reform, because CPC leads everything in China.

Party Reform

We have acknowledged Party’s strong intent to strengthen its direct leadership on financial sector and science technology sector to protect China economy and society from stricter sanctions by US. In addition, Party has shown greater interest in security issues of HK & Macau. New Party institutional reform is a double-edged sword; great success or serious failure.

Exhibit 6: Party Institutional Reform

Major areas:	Strengthen party's direct lead on important social areas
Central Financial Commission	Administer all the top decisions, coordination, execution and supervision of financial stability and development
Central Financial Work Committee	Guide and advise party construction in the financial system. As an agency dispatched by party, it works together with central financial commission to ensure party’s lead on financial work.
Central Science and Technology Committee	Administer revised Ministry of Science and Technology; promote civil-military fusion
Central Social Work Department	Guide collection of suggestions and feedback from people; enhance unified and direct party lead on national industry associations; guide party construction work of non-SOE enterprises and new organizations
Central Hong Kong and Macau Work Office	Replace previous state council HK & Macau affair office; ensure implementation of 'One country Two systems'.

Source: NPC and Xinhua News

Financial sector and tech sector are especially of Party’s interest – the former linked to potential financial systematic risk inclusive of potential sanction to restrict USD settlement; the latter linked to concern over healthy development of high-tech sectors caused by stricter sanctions over semiconductor related issue by US.

For financial industry, Party will establish both Central Financial Commission and Central Financial Work Committee to strengthen and consolidate party’s leadership on financial work and financial system administration. For tech sector, Party will establish Central Science and Technology Committee to strengthen party’s unified and direct leadership on technology work as well as to coordinate the integration of civil-military technology development.

We will introduce two other new Party institutions below;

Party will set up Central Social Work Department to administer directly social issues in nationwide. Under the 30th article of the Party Constitution, any institution that holds three or more Party members is required to set Party organization in its institution. New Department will beef up control by Central Committee over revised Party organization in many kinds of institutions such as private companies, research institutions, schools and so on.

We have acknowledged Party's strong intent to strengthen its direct leadership on financial sector and science technology sector to protect China economy and society from stricter sanctions by US. In addition, Party has shown greater interest in security issues of HK & Macau. New Party institutional reform is a double-edged sword; great success or serious failure.

Party will set up Central Hong Kong and Macau Work Office, which replaces the current government office. We judge that main background for stronger leadership over Hong Kong and Macau should be to keep national security in these two areas, especially in Hong Kong. We can recall the 2019 violent demo in Hong Kong, which caused National Security Law in Hong Kong to fight against any force of anti-“CPC unique one country two systems”. Given the supreme position of CPC over three powers in mainland, next focusing point should be any potential extrajudicial action in Hong Kong by CPC. Washington D.C. is more likely target Hong Kong under direct control by CPC when they shall take more sanctions over “China’.

We strongly believe that stronger leadership of Party should be a double-edged sword. If Party assigns right persons as executive staff for these new institutions and use the stronger leadership adequately, Party can succeed in efficient control of several fields. However, if not, wrong decisions backed by stronger power should cause a serious mistake in the corresponding fields.

We can add a fact that Party shall not establish “Central Internal Affairs Work Commission”, which had been expected to serve as direct control over national security issue according to Ming Pao news¹, one of Hong Kong media, on 23 February 2023. Following this article of Ming Pao news, many media reported negative news flow by highlighting potential role of the Commission as KGB under former Soviet era. This time, official document released on 16 Mar did not refer to “Central Internal Affairs Work Commission” or national security issue.

Government Reform

The major two areas for reform are Finance and Science Technology in line with Party institutional reform.

Exhibit 7: Government Institutional Reform

Major areas:	Overall positive - consolidate resource and prevent spillover of financial risks across sectors
Re-establish Ministry of Science and Technology	Develop technology and promote technology independence
Establish National financial regulatory administration	The entity will consolidate financial holding regulatory and financial consumer protection function of PBOC and investor protection function of CSRC into the same body and ensure adequate risk management across sectors.
Deepen local financial regulatory system reform	Local financial regulatory affairs will be mainly managed by central agencies.
Establish national data agency	Promote data-related infrastructures construction and to coordinate the integration, sharing, development and utilization of data resources

Source: NPC and Xinhua News

¹ [機構改革動作大 - 明報加西版\(溫哥華\) - Ming Pao Canada Vancouver Chinese Newspaper](#)

Exhibit 7: Government Institutional Reform (continued)

Others:	Regular institutional reform with streamlining government entity and enhancing efficiency
	Generally positive but little impact on investment
CSRC – promoted to be institutions directly under State Council	Strengthen capital market supervision responsibilities
PBOC branches reform	Streamline local sales department, consolidate entities and rebalance geographical coverage
Improve the state-owned financial capital management system	Strip off market operation institutions managed by central financial management department. Consolidate management of state-owned financial assets
Strengthen the unified and standardized management of staff in financial management departments	Apply national civil servant salary standards for financial management departments
Optimize the responsibilities of the Ministry of Agriculture and Rural Affairs	Support rural construction and development, implement assistance policies to rural areas, and make rational use of fiscal resources
Improve the employment system for the elderlies	To deal with aging society
Improve intellectual property management system	Protect fair competition and encourage innovation
National public complaints and proposals administration- promoted to be institutions directly under State Council	Promote information transparency
Reducing the staffing of central government agencies (civil servant directly under central government)	Reduce 5% cross all sectors

Source: NPC, Xinhua News and Sumitomo Mitsui DS Asset Management

For financial sector, we positively evaluate a centralized administration over financial risk. In details, government will set up national financial regulatory administration for general financial industry regulation, other than securities industry regulation (which shall be in charge by CSRC). We think the creation of the entity will help to consolidate financial regulatory, which shall benefit financial risk mitigation and help to prevent financial system risk. In addition, government will deepen local financial regulatory reform. Clear division of responsibilities helps to resolve local financial affairs and minimize duty overlap as well as conflicts of interests. However, we shall warn of potential hurdles in executional level—central government agencies may lack of local experience to handle unique and/or specific issues in some local areas. The actual effectiveness of this reform should depend on cooperation of local governments with central government.

For tech sector, re-establishing Ministry of Science and Technology and creating national data agency have revealed that China has realized the potential serious impact of high-tech sanction by US. It is in line with Xi's vow during different meetings on promoting technology independence and better utilizing data resources on innovation and technology advancement. However, we think so far the actual impact on sector development should not be overestimated.

4. Personnel Change

Overall in line with Party First Plenum; Preference of Technocrats

When constitution amendment bill was passed in 2018, we had expected Xi to extend his term to the third one (previous Max. 2 terms). And at the First Plenary Party Central Committee held on 23 October 2022, we observed the candidates for Premier and several other important positions in line with positions in the Party. In that sense, personnel change at NPC generally showed no big surprise to us. The new incumbent team has proved strong political power held by Xi.

Exhibit 8: Major Personnel Announced at NPC

Chinese Name	Mandarin Pronunciation	Age	Government Position	CPC Position
习近平	XI Jinping	69	President	Secretary General
韩正	HAN Zheng	68	Vice President	N.A.
赵乐际	ZHAO Leji	66	Chairman of Standing Committee of NPC	Standing member of Politburo
王沪宁	WANG Huning	67	Chairman of Chinese People's Political Consultative Conference	Standing member of Politburo
李希	LI Xi	66	Secretary of Central Commission for Discipline Inspection	Secretary of Central Commission for Discipline Inspection; Standing member of Politburo
李强	LI Qiang	63	Premier	Standing member of Politburo
丁薛祥	DING Xuexiang	60	Vice Premier	Standing member of Politburo
何立峰	HE Lifeng	68	Vice Premier	Member of Politburo
张国清	ZHANG Guoqing	58	Vice Premier	Member of Politburo
刘国中	LIU Guozhong	60	Vice Premier	Member of Politburo
李尚福	LI Shangfu	65	State Councilor, Minister of National Defense	Member of Central Committee; Central Military Committee member
王小洪	WANG Xiaohong	65	State Councilor, Minister of Public Security	Member of Central Committee
吴政隆	WU Zhenglong	58	State Councilor, Secretary-General of State Council	Member of Central Committee
谌贻琴	SHEN Yiqin	63	State Councilor	Member of Central Committee
秦刚	QIN Gang	57	State Councilor, Minister of Foreign Affairs	Member of Central Committee
易刚	YI Gang	65	PBoC Governor	N.A.
郑栅洁	ZHENG Shanjie	61	Chief of NDRC	Member of Central Committee
刘昆	LIU Kun	66	Head of Ministry of Finance	N.A.

Source: NPC

Note: 1. Ages as of 20 Mar 2023

2. Only ten members circled by gothic line can attend State Council Standing Committee.

Xi Jin Ping has been appointed as President for the third term, the first third time in the modern China history. We can bet on the fourth term of Xi as President, because government appointed Han Zheng, who has not been Party Central Committee member, as Vice President. This personnel of Vice President suggests that Han is unlikely to promote to President at NPC in Mar 2028. In fact, at NPC in March 2018, Wang Qishan was appointed as Vice President and retired at NPC in March 2023.

We will introduce our evaluation for several important government personnel below;

First, we admit Premier Li Qiang as the representative of New Zhijiang Army² and his promotion has connections with this experience—he was Xi’s previous subordinate in Zhejiang Province. However, we can bet on his potential skill to develop private economy and entrepreneurship, because he spent most of his career in Zhejiang Province, the cradle of China’s private economy. During his past career, he led many projects to promote regional economic synergy, develop internet-based SMEs, and optimize local advantages to develop its economy. We see him as a pro-growth and pragmatic person.

Second, for vice Premiers, 1) Ding Xuexiang would be the first premier. He is well-known as a director of CPC general office and secretary since he is a good ‘yes man’. However, we would like to highlight his technocrat career. He spent his time as a technocrat at Shanghai Research of Material from 1982 to 1999. We expect Ding to support Li Qiang as first Vice Premier from a viewpoint of science technology issues based on his technocrat career. Our interpretation should be consistent with Party’s great interest in science technology. 2) He Lifeng would be a successor to Liu He, who had taken care of economic and financial-related work. He is a representative of New Zhijiang Army because he has obtained trust from Xi Jinping after his co-work with Xi in Xiamen City of Fujian Province from 1987 to 1989. He has little related experience for financial industry. He is more familiar with industrial world. He has been in NDRC since 2014 and is well-known to be companying with Xi in many important events. 3) Zhang Guoqing (previous CPC Secretary of Liaoning Province) and Liu Guozhong (previous CPC Secretary of Shaanxi Province) had been focused as candidates for Vice Premier by market participants, because both had stayed in northern part of China for most of their career with little experience on southeast area economic development mode. Zhang was in military business for 28+ years before he started political life in 2016. Liu majored in artillery system fuse design and manufacturing at undergraduate and graduate level. Liu stayed in Heilongjiang local government in 20+ years before he really entered core political system. We can summarize the two Vice Premier common career as a technocrat. We expect both Vice Premier to support Li Qiang in science technology as well as Ding.

Third, in terms of State Councilors, we would like to highlight the appointments of Li Shangfu and Qin Gang. 1) Li Shangfu has been appointed as a state councilor (ranked No. 1 along with his appointment as Minister of National Defense. He held rich experience and knowledge in military (served as commanders of PLA departments) and equipment-related field. He has spent 31 years in Satellite Launch Center. He has been sanctioned by US. since 2018 due to potential involvement in the weapon trade with Russian dealer. This is the first time China appoints someone on U.S. sanction list to be State councilor. 2) Qin Gang has been appointed as a state councilor along with his first-time appointment as foreign minister, which never happened before. Leveraging his experience as previous US ambassador, with good reputation and deep involvement, we judge China has taken Sino-US relationship as one of the key assignments for new incumbents. Premier holds State Council Standing Committee every week. Under Li Qiang administration, only ten members, Premier, four Vice Premiers, five State Council members (one of them serves as Secretary-General) can attend the Standing Committee. Many other ministers can attend plenary State Council Committee, which is held twice a year.

² New Zhijiang Army is a group of those who worked with Xi Jinping during his political promotion. The group name comes from Zhejiang Province with strong economic power, when Xi served as Party Secretary from 2002 to 2007.

Fourth, Governor of PBOC and MOF have been remained the same. We do not positively evaluate their same positions. Neither of them are included in party central committee, which means they are not taken as core leaders in China's political system. For PBOC, the discretionary right is getting smaller reflecting Party and government institutional reform. As for many financial-related decisions, PBOC should consult with State Council first before they disclose the measures to the public. In that sense, whoever assumes PBOC Governor does not matter. Under stronger leadership by Party, whoever assumes Finance Minister does not matter.

Fifth, we can bet on multi-task ability for new head of NDRC-Zheng Shanjie, who was CPC Secretary of Anhui Province previously. As for his experience, he had been relocated to new position, which required a key person for some specific issues. Most of the roles he undertook were pretty short—some were only several months. He had spent his time in Fujian Province for most of his career and then relocated to Zhejiang Province for 3+ years and then to Anhui Province for 1+ years.

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