



# Economic Observatory

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## A re-cap of latest policy measures to combat economic slowdown in China

### 1. State Council announced ten point plans to guide policies for Q4

China's State Council meeting on Oct 18 announced ten point plans to guide economic policies for Q4. The meeting aimed at implementing a series of flexible and prudent macro-economic policies to offset the on-going negative impact from the global financial crisis. A series of fiscal, monetary and foreign trade policies is expected to be issued to ensure a stable and reasonably fast economic growth. Key messages from the 10-point plan are as follows:

- Agriculture to remain a priority and the government to increase the minimum grain purchase price up to 15% in 2009 as well as increase other subsidies to the rural sector.
- Encouraging financial institutions to increase lending to small and medium-sized enterprises, to expand SMEs' direct financing channels, and to provide fiscal incentives to their technology upgrading.
- Raising export tax rebates for labor-intensive industries including clothing, textiles and mechanical and electrical products to maintain stable export growth.
- The government to speed up re-construction in the earthquake area and increase fixed-asset investment, focusing on agricultural, water, energy, transportation and urban infrastructure projects, and to keep a reasonable level of fixed-asset investment, and etc.

The ten-point plan was the policy guidance only for the near future, and more detailed policies are expected to follow suit.

Immediately following the State Council's decisions, export tax rebates and support measures for the property sector have been issued, both effective from 1 November.

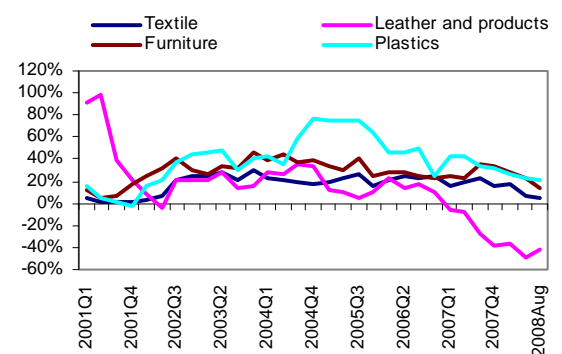
### 2. China would raise the export tax rebates effective on 1 Nov.

Ministry of Finance and State Administration of Taxation announced to raise export tax rebates effective from 1 Nov. The rebates of this time cover 25.8% of China's exports. In particular, export goods in labor-intensive industries and high value-added sectors will benefit from the rise of export tax rebates.

The export tax rebates for certain textiles and apparel will increase from 13% to 14%, rebates for certain toy products will rise from 11% to 14%; rebates for certain plastics products will rise from 5% to 9%; and rebates for certain furniture, drug ingredients, and wire and cable products and other machinery will also rise by different levels, etc.

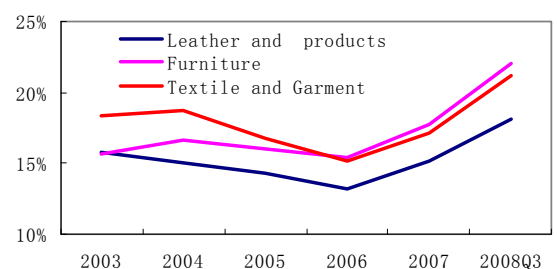
The move came as China's economic growth in the last quarter fell to 9% around a five-year low. It is expected the worsening financial crisis in developed countries will continue to weigh on China's exports, which has seen a gradual slowdown to 23.1%, 3.1 percentage points lower than that in

Chart1: Quarterly Export Growth YoY



Source: CEIC and BBVA estimates

Chart 2: The proportion of the loss-making enterprises in their industries



Source: CEIC and BBVA estimates

2007. As shown in Chart 1, export growth in these sectors has underperformed in recent years. Indeed, the proportion of loss-making enterprises in these sectors has increased on rising labor costs, the renminbi appreciation, and high commodities costs.

The increase in export tax rebates will boost those SMEs with an export orientation, thus potentially alleviate the problem of unemployment in the coastal regions.

How large is the fiscal impact on the central government?

Assuming the export growth rate in 2009 to be maintained at that in January-August in 2008, we estimate the rebates will have little impact on the fiscal conditions of the central government based on a back-of-envelope calculation. As shown in Table 1, it appears that these increases in export tax rebates will only increase tax burden of the government by USD3.85 billion or CNY25.7 billion. Compared with the fiscal revenue of CNY 5.1 trillion in 2007, these increases only reduce fiscal revenue by 0.5%.

Table 1: Estimates of tax rebates in 2009, USD million

	Tax rebate rate	Tax rebate rate hike	2007 Export	2008Jan-Aug Export	2008Jan-Aug yoy %	2008F Export	2009F Export	2009F Rebate
Textile and garment	14%	1%	198,608	139,874	9%	216,483	235,966	2,360
Furniture	11-13%	2%	26,949	20,483	21%	32,608	39,456	789
Plastic	9%	4%	10,758	8,631	24%	13,286	16,408	656
Leather and leather products	11%	6%	2,307	985	-41%	1,361	803	48
<b>Total</b>								<b>3,853</b>

Note: the number of exports in 2007 and 2008 Jan-Aug are summed by SITC categories, while the numbers in 2008F and 2009F are forecasts with same growth rate as 2008 Jan-Aug.

Source: CEIC and BBVA estimates

### 3. Tightening measures on the property market have started to ease

Ministry of Finance and State Administration of Taxation lowered the property deed tax to 1 percent from 1.5 percent for the first-time home buyer with a floor space of no more than 90 sqm. Meanwhile, the 0.05 percent stamp duty tax and land value-added tax for first-time home purchases was also waived.

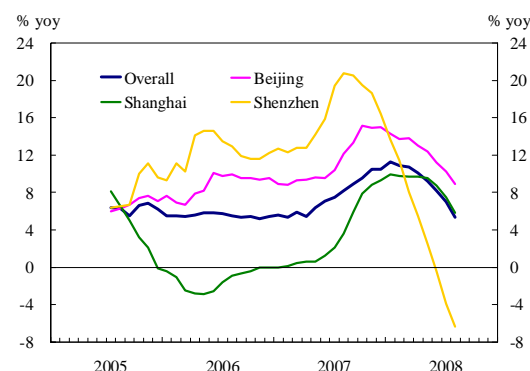
In addition, the People's Bank of China will reduce the down payment requirement to 20 percent from 30 percent for those first-time home purchasers. Banks will also charge only 70 percent of benchmark lending rates for such mortgages. The lending rates drawing from the housing provident fund will also be lowered by 27 basis points. Both policies would take effect from 1 Nov.

The move marks an initial unwinding of property tightening measures that the government put in place over the last few years to contain the rapidly rising prices. The real estate market transactions have weakened substantially since early this year; Growth in property prices fallen and transactions declined across the country (Charts 3 & 4).

Meanwhile, the central government also encouraged local governments to roll out their own policies to stimulate housing markets. Shanghai, Hangzhou and Nanjing, have already enacted such measures, including offering cash subsidies for home buyers and lowering taxes and fees for developers.

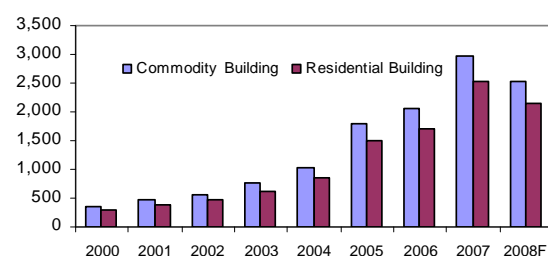
According to the State Council guidance, China needed to build more affordable housing for low-income people. It was well expected that several government agencies will collaborate to reach this goal. It is expected that these policies will not only stimulate the economy but also help solve the affordability problems for the low income people.

Chart 3: Housing prices



Source: CEIC

Chart 4: Commodity Building and Residential Building Sold, RMB billion



Source: CEIC and BBVA estimates

## Policy Impact

These policies are aimed to encourage home buyers to get into the housing market at a time when the real estate prices are expected to fall on slowing economic outlook and therefore slow-rising household income. Its effectiveness remains to be seen.

In addition, building more affordable housing at a time of falling property prices will put further pressure on the prices of the mid-end and high-end housing market, thus potentially running the risk of pushing the overall housing prices to fall further in China.

**Appendix Table: Important Policies and Guidelines in Real Estate Market (1998 to 2008)**

Date	Policies and Guidelines	Policy Impact On	
		Demand	Supply
1998	Central government abolished the state-allocated housing policy	+	+
	Mortgage lending started.	+	
1999	PBOC extended the maximum mortgage term to 30 years, increased maximum mortgage financing from 70% to 80%	+	
2001	Ministry of Construction issued regulations on sale of commodity housing		
2002	MOLR promulgated the rules regarding the grant of state-owned land use rights by way of Tender, Auction and Listing-For-Sale		—
2003	The State Council issued a notice for sustained and healthy development of the real-estate market		
	PBOC Circular 121 promulgated rules on more stringent administration of real-estate financing to reduce the credit and systemic risks associated with such financing		—
2004	The State Council issued a notice on adjusting the portion of capital fund for fixed assets investments in certain industries, and required capital financed by developers up from 20% to 35% of the total project.		—
	The Ministry of Construction amended the administrative measures on the Presale of commodity housing in Cities		—
	CBRC issued the Guideline for commercial banks on risks of real estate Loans to strengthen the risk control over real estate lending		—
2005	Following State Council eight directives, seven ministries jointly, MOC, NDRC, MOF, MOLR, PBOC, SAT and CBRC, instituted additional measures to discourage speculation in real properties, such as raising the minimum down payment for uncompleted projects from 20% to 30%; land use rights must only be made through auction or listing on land exchanges; increasing land supply for constructing ordinary and low-end housing; imposing a business tax of 5% on the proceeds from sales within two years of purchase and prohibiting resale of unfinished properties	—	
2006	Following State Council six directives, nine ministries jointly implemented additional land supply, bank financing and other measures to curb fast increases in property prices, to encourage the development of middle- to low-end housing and promote healthy development of the PRC property industry	mixed	Positive to low-end housing; Negative to high-end
	Regulation 171 jointly issued by MOFCOM, NDRC, MOC and PBOC regulated foreign investment in real estate. Foreign individuals can only buy property for self use if they work or study in China for at least one year; foreign institutions intending to invest in property not for self use must have registered capital at least 50% of the total investment if the investment is larger than US\$10mn	—	

2007	Land appreciation tax will be settled on real estate development enterprises		+
	The PBOC and CBRC raised the minimum down payment from 30% to 40% and increased interest rates for such mortgages by 10% for families who already own property.	—	
	In the second half, the PBOC decided to control overall loan growth, reducing bank financing for property developers.		—
	Government planned to increase the supply of affordable economic housing for low-income buyers		Positive for low-end housing
2008	State Council issued policy on idle land: government can recover the land if land approved for development remains unused for more than two years. If the land remains idle for more than one year and less than two years, land developers should pay a 20% non-usage fee.		+
	Ministry of Finance and State Administration of Taxation reduce the property deed tax to 1 percent from 1.5 percent for the first home with a floor space of no more than 90 sq m, and also lift the 0.05 percent stamp tax and land value-added tax. For those buying their first home, the down payment requirement will be lowered to 20 percent from 30 percent by PBOC, and banks are allowed to charge 70 percent of benchmark lending rates for such mortgages. The lending rates for housing provident loans are lowered by 27 basis points.	+	