

## Economics

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## China Macro Flash

## 2012 Budget Poses Downside Risks

- **2012 budget deficit lower than expectation** – The annual National People's Congress (NPC) meetings started today. The proposed budget presented by Premier Wen envisages fiscal deficit of Rmb800bn, or 1.5% of GDP, of which Rmb550bn is central government deficit, and Rmb250bn is local governments' deficit to be financed by debt issuance. The budget deficit was lower than the market (around 2% of GDP) and our (2.5% of GDP) expectations. The proposed budget is expected to be approved by the NPC with only marginal changes, based on past experience.
- **There is no major surprise otherwise** – The main targets and policy measures are in line with expectations (*What to Expect from the NPC Meeting?* Feb 27, 2012):
  - GDP growth target of 7.5% and inflation target of around 4%. The growth target was set below 8% for the first time in 8 years, in order to provide room for economic transformation. We are of the view that the government is trying to lower growth expectation, but is de facto targeting above 8% growth this year.
  - Nine million new jobs and registered unemployment rate below 4.6%. In addition, urban and rural household income growth is to be kept abreast of GDP growth.
  - Total trade (the sum of exports and imports) growth of about 10%. The growth target was modest relative to the actual growth in 2011 (22.5%), in recognition of the weak global recovery and debt crisis in Europe.
  - Broad money growth of 14%. This is supportive of the growth and inflation targets, implying prudent monetary policy but with an easing bias.
  - On property market policies, the report calls for strict implementation and gradual improvement of measures to contain speculation and investment demand. By expediting the construction of the housing information system and reforming the property tax, we think the government is laying the ground for the expansion of the property tax to replace home purchase restriction when house prices return to reasonable levels. We may see this happen by the middle of the year.
- **Inactive fiscal policy poses downside risks** – Our assessment is that the fiscal policy would not be proactive in 2012 since the budget deficit is only slightly higher than the actual outcome of 2011 (1.1% of GDP). Given the tendency of deficit undershooting, the actual fiscal stance is likely to be neutral. As private sector demand appears weak, reflected in the recent weak money/credit growth data, the downside risk to growth has increased. The budget constrains the fiscal room for maneuver, which opens the possibility of resorting to bank lending again (including through the urban development investment vehicles) in case the economy turns out to be weaker than the government expected.

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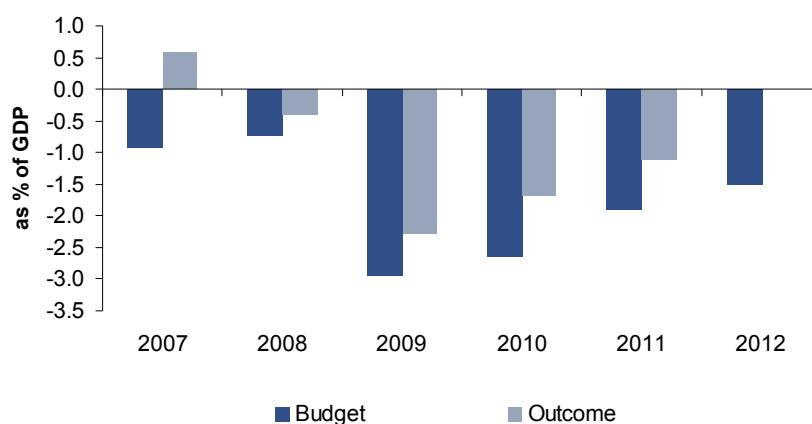
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## 2012 Budget Poses Downside Risks

Figure 1. Fiscal Balance



Source: MoF and Citi Investment Research and Analysis

Figure 2. Main Economic Target for 2012

|                                   |       |
|-----------------------------------|-------|
| GDP (YoY%)                        | 7.5%  |
| CPI (YoY%)                        | 4%    |
| Unemployment Rate: Urban (%)      | 4.6%  |
| Trade (Export+ Import) (YoY%)     | 10%   |
| Budget deficit                    | 800bn |
| New jobs creation                 | 9mn   |
| Social housing new starts (units) | 7mn   |
| Social housing completion (units) | 5mn   |

Source: Citi Investment Research and Analysis

## Appendix A-1

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