CHINA'S NEW MEASURES TO STIMULATE GROWTH

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Executive Summary

1. A sagging economy has eclipsed inflation as Beijing's biggest near-term concern. China' GDP growth eased to 7.6% in the second quarter of 2012 from a year earlier, its slowest pace in three years, while inflation mildly rose by 2% in the year to August. The data released recently show no sign that the economy will turn around in the near future.

2. Since November 2011, the central bank has reduced banks' reserved requirement ratio three times to 20% to stimulate growth. It has also cut interest rates twice this year, lowering the benchmark lending rates to 6% and deposit rates to 3%. While further monetary loosening is widely expected, the effectiveness of monetary easing may be limited.

3. Fiscal policies have also been adjusted to promote investment and accelerate tax reforms. During the first half of 2012, fixed asset investment grew by over 20% in nominal term. Business tax to value-added tax reform and structural tax reforms are emphasised to encourage the growth of the tertiary sector and small and micro-businesses.

4. The re-emphasis on growth has given various local governments the impetus to start new investment projects. However, it is unlikely that there will be another round of big stimulus plan given the concern over rising local government debts and potential risks to the banking sector.

5. Instead, the central government seems to favour more cautious and targeted measures. In addition to adjusting monetary and fiscal policies, the government started to push through crucial financial reforms by speeding up interest rates liberalisation and widening the yuan's floating ranges.

6. To ensure sustainable development, the central government has also passed new regulations to enhance the role of the non-state sector in investment and

to encourage household consumption. New measures have been announced to boost China’s trade, after recent data show renewed weaknesses.

7. There have been rising concerns over the deceleration of China’s economy and effectiveness of the government’s measures to boost the economy. While the growth of the first half year was within the government’s expectation, Beijing is still facing challenges to meet this year’s growth target of 7.5% given domestic slumps and external headwinds.