China Monetary Policy Report

Q3 2021

(November 19, 2021)

Monetary Policy Analysis Group of

the People's Bank of China

Executive Summary

Since the beginning of 2021, under the strong leadership of the CPC Central Committee with Comrade Xi Jinping at its core, the Chinese economy has remained on a trajectory of recovery and development. With major macro indicators staying within reasonable ranges, China’s economic growth has maintained good momentum and exhibited sustained resilience. GDP grew by 4.9 percent year on year in Q3 2021, averaging 4.9 percent during the past two years. The first three quarters witnessed stable employment, fast-growing import and export trade, as well as a 0.6 percent year-on-year rise in the CPI.

Following the guidance of Xi Jinping Thought on Socialism with Chinese Characteristics for a New Era, the People's Bank of China (PBC) resolutely implemented the decisions and arrangements of the CPC Central Committee and the State Council. Pursuing stability as its top priority, the PBC implemented a sound monetary policy, which was flexible, targeted, reasonable, and appropriate. With proper cross-cycle designs, the PBC improved its policies by making them more forward-looking and effective while keeping them stable. Meanwhile, the PBC managed market expectations scientifically, remained committed to serving the real economy, and managed financial risks effectively. These efforts have cultivated a favorable monetary and financial environment for achieving high-quality economic development.

First, liquidity was kept adequate at a reasonable level. On July 15, the PBC reduced the required reserve ratio (RRR) for financial institutions by 0.5 percentage points, which released about RMB1 trillion of long-term funds. Apart from that, a mix of monetary policy instruments, such as central bank lending and discounts, the Medium-term Lending Facility (MLF), and open market operations (OMOs), were used to satisfy the reasonable liquidity needs of financial institutions and to guide money market rates to move smoothly around the OMO rates. Reform was promoted for Standing Lending Facility (SLF) operations to improve the stability of liquidity in the banking system. **Second,** structural monetary policy tools were assigned a guiding role. Additional central bank lending in the amount of RMB300 billion was provided, aiming at giving more support to micro and small businesses (MSBs). In addition, the PBC prolonged the use of the two monetary policy tools providing direct support for the real economy, boosted coordinated regional development with multiple measures, and enhanced policy support for sci-tech innovations, MSBs, green development, and the manufacturing sector. **Third,** the benefits of the loan prime rate (LPR) reform were continuously unleashed. With the LPR continuing to serve as a signal for the loan market, actual loan rates remained stable with a slight decline. While the regulations over deposit rates were improved, the liability costs of banks dropped. All lenders were required to be explicit about their annualized interest rates. **Fourth,** focusing on the domestic situation, attention was paid to maintaining a balance between internal and external equilibria. The PBC deepened the market-oriented reform of the exchange rate to maintain the flexibility of the RMB exchange rate. Expectation management was strengthened to give play to the role of the exchange rate in adjusting the macro economy and as an auto stabilizer for the balance of payments. **Fifth,** upholding market principles and the rule of law, the PBC coordinated development and security, managed financial risks well, and firmly defended the bottom line that no systemic risk should occur.

Overall, China has managed well the intensity and pace of its sound monetary policies, while standing firm on a normal policy path. Plans were made in advance based on an overall judgment about the marginal changes in economic and financial development both at home and abroad as well as the likely policy shifts in the major economies. The real economy continued to receive solid support from the financial sector, and financial markets remained stable. At end-September, broad money (M2) and aggregate financing to the real economy (AFRE) recorded year-on-year growth of 8.3 percent and 10 percent, respectively. The credit structure continued to improve. At end-September, inclusive MSB loans and medium and long-term (MLT) loans to the manufacturing sector grew by 27.4 percent and 37.8 percent year on year, respectively. In September, the weighted average rate on corporate loans registered 4.59 percent, and that on inclusive MSB loans registered 4.89 percent, down 0.02 and 0.19 percentage points respectively from December 2020. Money market rates were stable. During the first nine months, the weighted average rate on 7-day repos between depository institutions in the interbank market (DR007) averaged 2.18 percent, only 2 basis points lower than the central bank's 7-day reverse repo rate. The RMB exchange rate moved in both directions and remained basically stable at an adaptive and equilibrium level. The central parity of the RMB against the US dollar was 6.4854 at end-September, an appreciation of 0.6 percent from end-2020. The annualized volatility rate of the RMB against the US dollar was 3.2 percent in the first three quarters.

China has a super-large economy with strong resilience, and the fundamentals for sound economic growth in the long run remain unchanged. In addition, it has large development potentials, vast room for policy adjustments, and active market entities.

However, it should also be noted that amid the changes unseen in a century, which have been compounded by the COVID-19 pandemic, the external environment is more complicated and serious, and domestic economic recovery and development are constrained by temporary, structural, and cyclical factors. In response, we should remain confident and focus on domestic issues. In the next stage, under the guidance of Xi Jinping Thought on Socialism with Chinese Characteristics for a New Era, the PBC will follow the guidelines of the Fifth and Sixth Plenary Sessions of the 19th CPC Central Committee as well as the Central Economic Work Conference, and implement the requirements set forth in the *Report on the Work of the Government.* In line with the decisions and arrangements of the CPC Central Committee and the State Council, the PBC will adhere to the general principle of seeking progress while ensuring stability. Applying the new development philosophy fully, faithfully, and comprehensively, it will deepen the supply-side structural reform, speed up the building of the new development paradigm, develop a modern central bank system, improve the modern monetary policy framework, and contribute to high-quality development. More efforts will be made to analyze and judge the marginal changes in domestic and global economic development so that macro policies for 2021 and 2022 will be well coordinated. Serving the real economy will be a higher priority. The PBC will maintain the stability of its monetary policy, stabilize market expectations, and keep the economic indicators within a reasonable range.

The sound monetary policy will remain flexible, targeted, reasonable, and appropriate. Focusing on domestic issues and pursuing stability as its top priority, the PBC will precisely manage the intensity and pace of its policies, and properly handle the relationship between economic development and risk prevention. With a proper cross-cycle policy design, the PBC will safeguard the stability of the national economy and strengthen the resilience of economic development. The mechanism for money supply management will be improved to keep liquidity adequate at a reasonable level. Aggregate credit will grow at a more stable pace so that the growth of M2 and the AFRE will be basically in line with that of nominal GDP and the macro leverage ratio will be basically stable. The PBC will closely follow and study price movements to stabilize social expectations and to keep prices generally stable. It will give play to structural monetary policy instruments and encourage commercial banks to make full use of the newly added RMB300 billion of central bank lending in support of MSBs. The two monetary policy tools providing direct support for the real economy will remain in place for a longer period. RMB200 billion of central bank lending will be used for coordinated regional development. The Carbon Emission Reduction Facility will be put into use and RMB200 billion of central bank lending targeted for clean and efficient coal use will be launched. Financial institutions will be guided to enhance their support for key areas and weak links, such as micro, small, and medium-sized enterprises (MSMEs) and green development. While enhancing the market-oriented interest rate formation and transmission mechanism, the PBC will continue to unleash the benefits of the LPR reform, improve deposit rate regulations, and guide the overall financing costs for MSBs to be stable with a slight decline. It will deepen the market-oriented exchange rate reform, enhance the RMB exchange rate flexibility, intensify expectation management, improve macro-prudential management for cross-border financing, and guide enterprises and financial institutions to remain risk-neutral, thereby keeping the RMB exchange rate basically stable at an adaptive and equilibrium level. The PBC will coordinate the prevention and resolution of major financial risks by firmly defending the bottom line, improving its holistic approach, and following market principles and the rule of law. While keeping the economy on a steady recovery trajectory, the PBC will endeavor to accomplish the major tasks set forth for economic development within the year.

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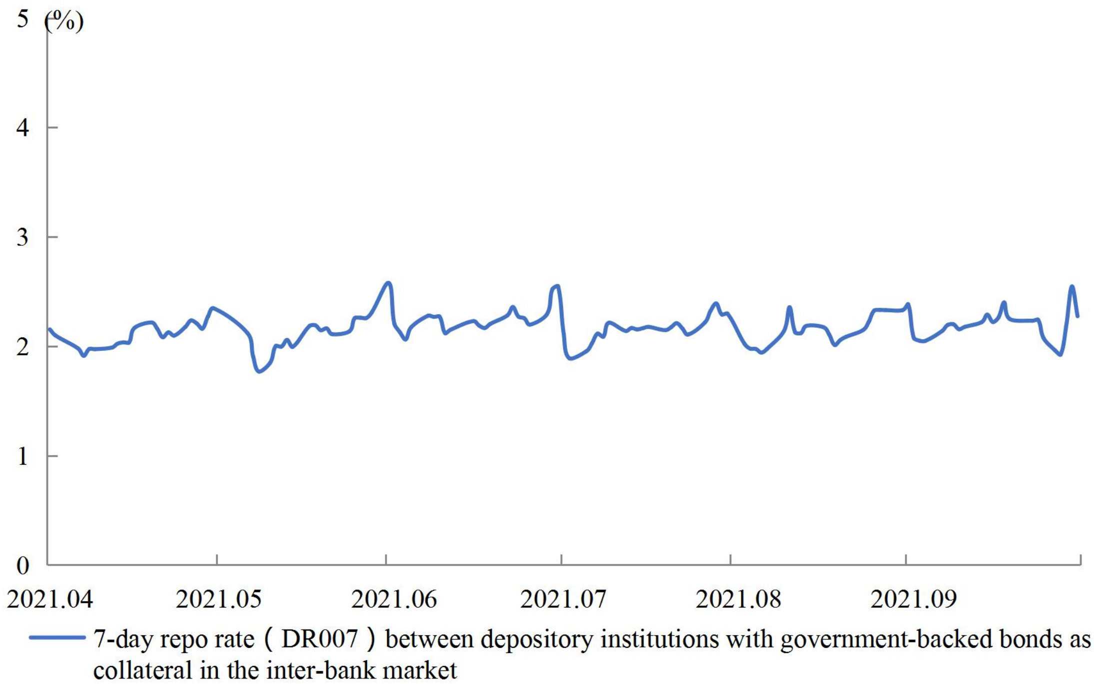
Since the beginning of 2021, under the guidance of Xi Jinping Thought on Socialism with Chinese Characteristics for a New Era, following the guidelines of the Fifth Plenary Session of the 19th CPC Central Committee and the Central Economic Work Conference, and implementing the requirements set forth in the *Report on the Work of the Government*, the People's Bank of China (PBC) pursued a sound monetary policy which was flexible, targeted, reasonable, and appropriate. Money, credit, and aggregate financing to the real economy (AFRE) gained reasonable growth. Overall financing costs remained stable, even with a slight decline. All this buttressed the real economy.

I. Liquidity in the banking system was adequate at a reasonable level

In Q3 2021, the PBC pursued stability as its top priority and made cross-cyclical policy designs based on scientific judgments about the marginal changes in macroeconomic conditions both at home and abroad. By using multiple policy tools, such as the required reserve ratio (RRR) cut, central bank lending and discounts, the Medium-term Lending Facility (MLF), and open market operations (OMOs) for liquidity provision, and by conducting these operations in a more forward-looking, flexible, and effective manner, the PBC maintained adequate liquidity in the banking system at a reasonable level. On July 15, the PBC reduced the RRR by 0.5 percentage points, which released long-term funds of about RMB1 trillion . The move optimized the term structure of funds held by financial institutions and provided more support to the real economy. Meanwhile, the PBC guided money market rates to move around the OMO rates by stabilizing market expectations in different ways. Interest rates displayed less volatility. At end-September, the excess reserve ratio of financial institutions registered 1.4 percent, up 0.2 percentage points from end-June.

Figure 1 Movement of Money Market Interest Rates



Source: www.chinamoney.com.cn.

Box 1 The Decline in the Excess Reserve Ratio: An Objective Perspective

Since the turn of the century, the payment and settlement system in China has been more efficient, the money market has witnessed rapid development, and financial institutions have been more competent in managing liquidity. These factors, combined with reforms such as the averaging approach to the required reserve assessment, have caused a gradual decline in the need of financial institutions for excess reserves once they ensure their liquidity is sound. The excess reserve ratio has shown an overall decline. At the beginning of this century, the ratio at the ends of quarters was generally above 4 percent. It dropped to 2.2 percent during the 2012–2016 period, and then to 1.9 percent in 2019.

During the past two years, especially since the beginning of 2021, the PBC has further lowered the interest rate on excess reserves and improved liquidity management and the framework for managing short-term interest rates, which reduced the financial institutions' need for excess reserves. Consequently, the excess reserve ratio decreased further. It recorded 1.5 percent, 1.2 percent, and 1.4 percent, respectively, at the ends of the first three quarters of this year. Meanwhile, money market rates have been more stable. The specific measures are as follows:

First, lowering the interest rate on excess reserves so that financial institutions voluntarily reduce their reserve levels. In April 2020, the PBC lowered the interest rate from 0.72 percent to 0.35 percent, which was the same as the benchmark rate on demand deposits. This eliminated the arbitrage space for financial institutions to absorb demand deposits and then to deposit them at the central bank. Holding excess reserves thus became less desirable.

Second, tracking market rates and accurately carrying out regular operations to present clearer policy goals. The PBC continuously released short-term policy rate signals through daily open market operations so as to timely iron out liquidity turbulence and guide money market rates to remain stable and to move around the open market rates. Meanwhile, by improving Standing Lending Facility (SLF) operations, the PBC strengthened the ceiling of the interest rate corridor, and fluctuations in the market rates were contained. In addition, the PBC devoted more efforts to policy publicity through various channels so that market entities can focus more on market rates and avoid over-interpretation of liquidity conditions and quantity changes in central bank operations.

Third, reducing fluctuations in money market rates to lower precautionary demand for liquidity. During the last two years, the deviation between money market and open market rates has been noticeably narrowed. In the first nine months of 2021, the weighted average rate on 7-day repos between depository institutions in the interbank market (DR007) averaged 2.18 percent, only 2 basis points away from the 7-day open market rate. This enhanced the credibility of the central bank's commitment to keep liquidity adequate at a reasonable level and to keep money market rates stable. It also reduced financial institutions' precautionary demand for liquidity.

Fourth, ensuring effective inter-temporal liquidity management through early arrangements and targeted operations. For example, before the 2021 Spring Festival, the PBC accurately projected the pre-holiday liquidity gap based on factors such as the pandemic and injected an appropriate amount of inter-temporal liquidity, mainly in the form of 7-day repos. The injection marked the lowest pre-holiday level in recent years. It both satisfied pre-holiday liquidity demand and avoided excessive post-holiday liquidity, and thus it reduced seasonal fluctuations in market rates. Meanwhile, the PBC released operation plans in announcements on open market operations, including changes in liquidity conditions, so as to guide financial institutions to make liquidity arrangements in advance.

To summarize, under a normal monetary policy, a decline in the excess reserve ratio in China is attributable to the development of the financial system as well as to the continuous improvement in the monetary policy management framework. From international experience, the aggregate liquidity level is not directly related to the stability of market rates. For example, before the 2008 global financial crisis when normal monetary policy was a common global practice, the total excess reserves of depository institutions in the US were only about two billion US dollars, but this did not affect the stable movement of US money market rates. Therefore, at present, it would be inappropriate to judge liquidity conditions purely on aggregate liquidity or on the excess reserve ratio. It would be even more inappropriate to interpret the decline in the excess reserve ratio as a liquidity squeeze. A rational approach to judge liquidity conditions is to focus on market rates.

II. Lending by financial institutions grew reasonably, with the lending rates at historical lows

Despite a high base in the previous year, financial institutions' credit grew reasonably in the first three quarters of 2021, recording a fairly larger year-on-year increase. Enterprises' normal financing needs were satisfied and support for the real economy remained solid. It should also be noted that, affected by the demand side, the upward momentum of credit growth has been slowing down since the second half of the year. The PBC strengthened guidance to promote overall stability of credit supply. At end-September, outstanding loans issued by financial institutions in domestic and foreign currencies grew 11.4 percent year on year to RMB195.6 trillion, increasing RMB17.2 trillion from the beginning of 2021 and RMB274.2 billion more than the increase during the corresponding period of 2020. Outstanding RMB-denominated loans grew 11.9 percent year on year to RMB189.5 trillion, up RMB16.7 trillion from the beginning of 2021 and an increase that was RMB462.4 billion larger than that during the corresponding period of 2020.

With the credit structure continuously being improved, key areas and weak links, such as the manufacturing sector as well as micro and small businesses (MSBs), received targeted support. At end-September, medium and long-term loans to enterprises and public entities grew by RMB8.3 trillion from the beginning of the year, a year-on-year acceleration of RMB1.1 trillion. Medium and long-term loans to the manufacturing sector increased by 37.8 percent. In particular, the high-tech manufacturing sector witnessed a year-on-year increase of 39.7 percent. Outstanding inclusive loans to MSBs grew by 27.4 percent year on year to RMB18.6 trillion, 15.5 percentage points higher than the growth of total loans during the same period. These loans supported 40.92 million MSBs, rising 30.8 percent year on year.

Table 1 The Structure of RMB Loans in the First Three Quarters of 2021

Unit: RMB100 million

	Outstanding amount at end-September	YOY growth (%)	Increase from the beginning of the year	YOY acceleration
RMB loans to:	1894591	11.9%	167178	4624
Households	695298	13.2%	63450	2210
Enterprises and public entities	1189163	11.3%	104815	-817
Non-banking financial institutions	3503	-31.4%	-1619	3101
Overseas	6628	14.7%	532	131

Note: Loans to enterprises and public entities refer to loans to non-financial enterprises, government departments, and organizations.

Source: The People’s Bank of China.

Table 2 New RMB Loans by Financial Institutions in the First Three Quarters of 2021

Unit: RMB100 million

	Increase from the beginning of the year	YOY acceleration

Chinese-funded large-sized banks [1]	76680	2336
Chinese-funded small and medium-sized banks[2]	88792	738
Small-sized rural financial institutions[3]	23816	983
Foreign-funded financial institutions	1455	911

Notes: 1. Chinese-funded large-sized banks refer to banks with assets (in both domestic and foreign currencies) of RMB2 trillion or more (according to the amount of total assets in both domestic and foreign currencies at end-2008). 2. Chinese-funded small and medium-sized banks refer to banks with total assets (both in domestic and foreign currencies) of less than RMB2 trillion (according to the amount of total assets in both domestic and foreign currencies at end-2008). 3. Small-sized rural financial institutions include rural commercial banks, rural cooperative banks, and rural credit cooperatives.

Source: The People's Bank of China.

The weighted average interest rates on loans were at historical lows. The PBC continued to deepen the market-based reform of interest rates, strengthen competition in MSB credit markets, guide actual lending rates to go down amidst stability, and encourage the financial sector to cut profits in favor of the real economy. In the meantime, the PBC optimized regulation over deposit rates and promoted a decline in the interest rates of long-term deposits. Thus, the term structure of deposits was optimized, and a pricing pattern with orderly tiers and differentiated competition was consolidated in deposit markets. In September, the one-year LPR and the over-five-year LPR stood at 3.85 percent and 4.65 percent, respectively, on par with those in December 2020. The weighted average lending rate recorded 5.00 percent in September. In particular, the weighted average interest rate on ordinary loans registered 5.30 percent, down 0.01 percentage points year on year. The weighted average corporate lending rate fell by 0.04 percentage points year on year to 4.59 percent, reaching historically low levels. This indicates that financial support for the real economy continues to yield positive results.

Table 3 Weighted Average Interest Rates on New Loans Issued in September 2021

Unit: %

	September	Change from last December	YOY change

Weighted average interest rate on new loans	5.00	-0.03	-0.12
On ordinary loans	5.30	0.00	-0.01
Of which: On corporate loans	4.59	-0.02	-0.04
On bill financing	2.65	-0.45	-0.58
On mortgage loans	5.54	0.20	0.18

Source: The People's Bank of China.

In September, the share of ordinary loans with rates above, at, and below the LPR registered 68.13 percent, 8.36 percent, and 23.52 percent, respectively.

Table 4 Shares of RMB Lending Rates at Different Levels, from January to September 2021

Unit: %

Month	LPR-bps	LPR	LPR+bps					
			Subtotal	(LPR, LPR+0.5%)	[LPR+0.5%, LPR+1.5%)	[LPR+1.5%, LPR+3%)	[LPR+3%, LPR+5%)	LPR+5% and above
January	23.93	7.51	68.56	15.45	24.38	13.24	8.09	7.39
February	26.24	7.02	66.74	14.26	23.59	12.28	8.25	8.36
March	22.03	8.42	69.54	14.98	24.79	13.56	8.76	7.45
April	21.08	7.46	71.46	14.45	23.88	14.78	9.69	8.68
May	22.89	7.38	69.73	14.27	23.60	14.00	9.04	8.82
June	24.25	8.07	67.67	15.46	23.79	13.36	8.10	6.97
July	22.37	7.15	70.48	14.20	24.18	13.76	9.25	9.10
August	22.48	7.42	70.10	14.20	23.25	13.91	9.37	9.37
September	23.52	8.36	68.13	14.94	23.42	13.24	8.59	7.93

Source: The People's Bank of China.

Interest rates on foreign-currency deposits and loans declined slightly. In September, the weighted average interest rates on demand and large-value USD-denominated deposits with maturities within 3 months registered 0.10 percent and 0.40 percent, down 0.06 and 0.19 percentage points from December 2020, respectively. The weighted average interest rates on USD-denominated loans with maturities within 3 months and with maturities between 3 months (including 3 months) and 6 months registered 1.11 percent and 1.05 percent, down 0.11 percentage points and 0.31 percentage poinst from December 2020, respectively.

Table 5 Average Interest Rates on Large-value USD-denominated Deposits and Loans from January to September 2021

Unit:%

Month	Large-value deposits						Loans				
	Demand deposits	Within 3 months	3–6 months (including 3 months)	6–12 months (including 6 months)	1 year	Over 1 year	Within 3 months	3–6 months (including 3 months)	6–12 months (including 6 months)	1 year	Over 1 year
January	0.14	0.65	0.88	0.92	1.10	1.17	1.25	1.12	1.06	1.04	1.94
February	0.14	0.61	0.72	0.90	1.05	1.04	1.23	1.17	1.05	1.16	2.37
March	0.14	0.55	0.77	0.91	1.09	0.99	1.23	1.09	1.01	0.90	2.14
April	0.12	0.51	0.77	0.81	0.99	1.07	1.32	1.15	1.16	1.03	1.93
May	0.11	0.46	0.69	0.73	0.92	0.84	1.31	1.11	0.86	0.90	2.20
June	0.10	0.43	0.62	0.77	0.91	0.90	1.15	0.99	0.90	0.78	2.22
July	0.11	0.43	0.65	0.70	0.93	0.59	1.14	1.03	0.93	0.86	1.93
August	0.09	0.41	0.64	0.69	0.99	0.88	1.25	1.05	0.94	0.90	2.24
September	0.10	0.40	0.55	0.71	0.85	0.80	1.11	1.05	1.10	0.93	2.16

Source: The People’s Bank of China.

Deposits grew steadily. At end-September, outstanding deposits in domestic and foreign currencies in all financial institutions increased 8.7 percent year on year to RMB235.6 trillion, up RMB17.2 trillion from the beginning of 2021 and a deceleration of RMB1.4 trillion. Outstanding RMB deposits grew 8.6 percent year on year to RMB229.2 trillion, an increase of RMB16.6 trillion from the beginning of the year and a deceleration of RMB1.5 trillion. Outstanding deposits in foreign currencies stood at USD992.7 billion, an increase of USD103.4 billion from the beginning of 2021 and an acceleration of USD12.5 billion.

Table 6 The Structure of RMB Deposits in the First Three Quarters of 2021

Unit: RMB100 million

	Deposits at end-September	YOY growth (%)	Increase from the beginning of the year	YOY acceleration
RMB deposits:	2291808	8.6%	166088	-15423
Households	1010914	10.8%	84904	-14601
Non-financial enterprises	679289	4.6%	20170	-34705
Public entities	315173	1.0%	15717	942
Fiscal entities	56884	20.7%	12112	5834
Non-banking financial institutions	215220	21.4%	31779	27014
Overseas	14329	13.4%	1404	92

Source: The People's Bank of China.

III. Broad money supply and aggregate financing to the real economy displayed appropriate growth

The stable increase in the financial sector provided strong support for the real economy. Outstanding M2 recorded RMB234.3 trillion at end-September, increasing 8.3 percent year on year. Outstanding M1 and M0 registered RMB62.5 trillion and RMB8.7 trillion, respectively, increasing 3.7 percent and 5.5 percent year on year. The first three quarters of 2021 witnessed a net cash injection of RMB255.2 billion, which is RMB262.9 billion less than that in the same period of the previous year.

According to preliminary statistics, the outstanding AFRE reached RMB308.05

trillion at end-September. Year-on-year growth registered 10 percent, decelerating 3.3 percentage points compared to the growth recorded at end-2020. The AFRE increment in the first three quarters of 2021 totaled RMB24.75 trillion, dropping RMB4.87 trillion year on year. In general, financial support for the real economy adapts to economic development, which shows the following characteristics: first, RMB-denominated loans maintained an appropriate increase. Second, trust loans and undiscounted bankers' acceptances recorded a significantly larger year-on-year drop. Third, financing through government and corporate bond issuances returned to normal and showed a year-on-year drop in growth, while domestic equity financing of non-financial companies exhibited a year-on-year increase. Fourth, financing of asset-backed securities of depository institutions showed a larger year-on-year increase.

Table 7 Aggregate Financing to the Real Economy in the First Three Quarters of 2021

	End-September 2021		First Three Quarters of 2021	
	Stock (RMB1 trillion)	YOY growth (%)	Flow (RMB100 million)	YOY change (RMB100 million)
AFRE	308.05	10.0	247481	-48677
Of which: RMB loans	188.42	12.0	168281	1400
Foreign-currency loans (RMB equivalent)	2.35	-0.2	2531	-521
Entrusted loans	10.93	-1.8	-1142	2048
Trust loans	5.14	-27.0	-12270	-8133
Undiscounted bankers' acceptances	3.28	-15.8	-2228	-7904
Corporate bonds	29.25	6.9	24310	-16616
Government bonds	50.46	13.5	44155	-23158
Domestic equity financing by non-financial	9.06	13.8	8142	2043

	End-September 2021		First Three Quarters of 2021	
enterprises				
Other financing	8.94	21.4	8693	1657
Of which: Asset-backed securities of depository institutions	2.05	25.8	1560	2092
Loans written off	5.95	23.2	6644	-1000

Notes: ①AFRE (stock) refers to outstanding financing provided by the financial system to the real economy at the end of a period. AFRE (flow) refers to the volume of financing provided by the financial system to the real economy within a certain period of time. ②Since December 2019, the PBC has further improved AFRE statistics by incorporating "central government bonds" and "local government general bonds" into the AFRE and combining them with the existing "local government special bonds" under the item of "government bonds." The value of this indicator is the face value of bonds under custody. Since September 2019, the PBC has further improved the "corporate bonds" statistics contained in the AFRE by incorporating "exchange-traded asset-backed corporate securities." To improve the AFRE statistical method, the PBC has incorporated "local government special bonds" into the AFRE since September 2018 and has incorporated "asset-backed securities by depository institutions" and "loans written off" into the AFRE statistics under the item of "other financing" since July 2018. ③Year-on-year statistics in the table are on a comparable basis.

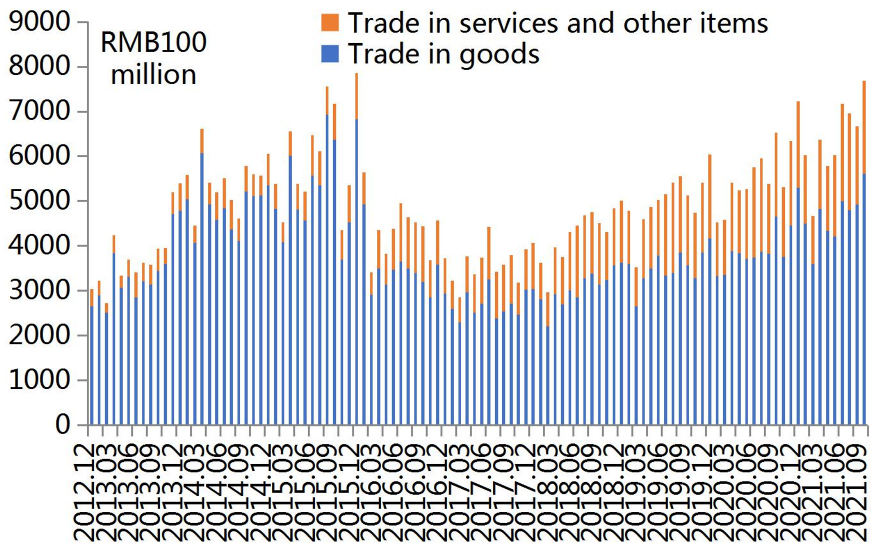
Sources: The People's Bank of China, China Banking and Insurance Regulatory Commission, China Securities Regulatory Commission, China Central Depository & Clearing Co., Ltd., National Association of Financial Market Institutional Investors, etc.

IV. The RMB exchange rate remained basically stable at an adaptive and equilibrium level and cross-border RMB business sustained growth

Since the beginning of 2021, cross-border capital flows and foreign-exchange supply and demand have been basically in equilibrium, and market expectations have been generally stable. Based on market supply and demand, the RMB exchange rate moved in both directions and remained basically stable at an adaptive and equilibrium level. During the first three quarters of 2021, the RMB appreciated slightly against a basket of currencies. At end-September, the China Foreign Exchange Trade System (CFETS) RMB exchange-rate index and the RMB exchange-rate index based on the special drawing rights (SDRs) basket closed at 99.64 and 97.61, respectively, up 5.1 percent and 3.6 percent from end-2020. According to calculations by the Bank for International Settlements (BIS), during the first three quarters of 2021, the nominal effective exchange rate (NEER) and the real effective exchange rate (REER) of the RMB appreciated 3.9 percent and 1.2 percent, respectively, and from the reform of the exchange rate formation mechanism that began in 2005 to end-September 2021, the appreciation of the NEER and REER of the RMB registered 43.1 percent and 53.2 percent, respectively. At end-September 2021, the central parity of the RMB against the US dollar was 6.4854, appreciating 0.6 percent from end-2020 and 27.6 percent on a cumulative basis since the reform of the exchange-rate formation mechanism that began in 2005. During the first three quarters of 2021, the annualized volatility rate of the RMB against the US dollar was 3.2 percent.

During the first three quarters of 2021, cross-border RMB settlements increased 32 percent year on year to RMB27.4 trillion, with RMB receipts and payments posting RMB13.9 trillion and RMB13.5 trillion, respectively. Cross-border RMB settlements under the current account grew by 18 percent year on year to RMB5.7 trillion, among which RMB settlements of trade in goods registered RMB4.2 trillion, whereas RMB settlements of trade in services and other items registered RMB1.5 trillion. Cross-border RMB settlements under the capital account registered RMB21.7 trillion, increasing 36 percent year on year.

Figure 2 Monthly RMB Payments and Receipts under the Current Account



Source: The People’s Bank of China.

Part 2. Monetary Policy Operations

In Q3 2021, the PBC resolutely implemented the decisions and arrangements made by the CPC Central Committee and the State Council, kept the sound monetary policy flexible and targeted and at a reasonable and appropriate level, and managed policy rhythm and intensity well. The PBC lowered the required reserve ratio (RRR) for financial institutions by 0.5 percentage points on July 15, conducted open market operations (OMOs) and the Medium-term Lending Facility (MLF) in a flexible manner, advanced market-based reforms of interest rates and exchange rates, continued to leverage the targeted guidance role of structural monetary policy instruments, and further intensified policy support for scientific and technological innovations, micro, small, and medium-sized enterprises (MSMEs), green development, and manufacturing, thus fostering a favorable monetary and financial environment for high-quality economic development.

I. Conducting open market operations in a flexible manner

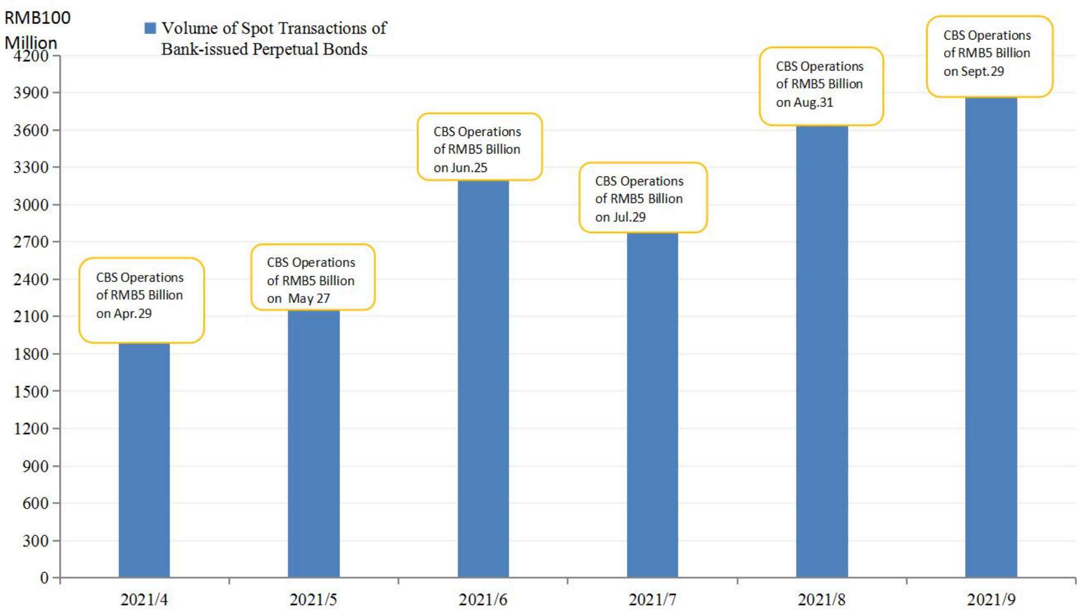
Conducting open market operations in a flexible manner. In Q3 2021, on the basis of a scientific assessment of the current situation, the PBC strengthened market monitoring. With the provision of medium and long-term liquidity via RRR cuts, the MLF, and other monetary policy instruments as the basis, the PBC factored in the required reserve payments, tax payments, the issuance of government bonds, and other elements that affected liquidity, conducted successive open market operations daily, and precisely managed the intensity of operations to maintain liquidity in the banking system at a proper and adequate level. In mid- to late September, the PBC timely conducted 14-day reverse repos to release cross-quarter liquidity in advance, and financial institutions felt reassured about end-of-season asset and liability management. Meanwhile, the PBC conducted 7-day reverse repos and scaled up the operations appropriately to offset the impact of the peak period for paying taxes, the intensive issuance of local government bonds, and other factors, thus effectively maintaining money market stability at the end of the quarter.

Guiding market rates to move around central bank policy rates in a stable manner

In Q3 2021, both the rates paid on the MLF and the open-market reverse repos remained unchanged. Meanwhile, since the beginning of 2021, the PBC has sent successive short-term policy rate signals through open market operations and has guided money market rates to move around the OMO rates on 7-day reverse repos. As a result, short-term policy rates have played a strengthened role as the pivotal guiding rates, and the deviation of the weighted average rate on 7-day repos between depository institutions in the interbank market (DR007) from the OMO rates narrowed sharply. During the first nine months of 2021, the DR007 averaged 2.18 percent, a deviation of 2 basis points from the central bank's 7-day reverse repos rate. Liquidity expectations of financial institutions became more stable, management of monetary policy expectations scored more notable effects, and demand for precautionary liquidity decreased significantly.

Continuously conducting central bank bill swap (CBS) operations. In Q3 2021, the PBC conducted CBS operations three times, with the total amount registering RMB15 billion. The maturity of each operation was three months, at a fixed rate of 0.10 percent. Since the beginning of 2021, the PBC has conducted CBS operations regularly on a monthly basis, and these operations have played a positive role in boosting liquidity in the secondary market of bank-issued perpetual bonds and in supporting the issuance of perpetual bonds to replenish capital and the steady growth of aggregate credits by banks, especially by small and medium-sized banks.

Figure 3 Volume of Spot Transactions of Bank-issued Perpetual Bonds



Issuing central bank bills in Hong Kong on a regular basis. In Q3 2021, the PBC issued three batches of RMB-denominated central bank bills in Hong Kong, totaling RMB30 billion. Specifically, the 3-month, 6-month, and 1-year bills registered RMB10 billion, RMB5 billion, and RMB15 billion, respectively. During the first three quarters of 2021, the issuance of nine batches of RMB-denominated central bank bills totaled RMB90 billion, which enriched the RMB investment products and the RMB liquidity management tools in the Hong Kong market and played an active role in propelling both domestic and overseas market entities to issue RMB-denominated bonds, to conduct RMB business in the offshore market, and in promotinge the sound development of the offshore RMB market. During the first nine months of 2021, offshore RMB bond issuances, excluding RMB-denominated central bank bills issued in Hong Kong, registered roughly RMB140 billion, a year-on-year increase of 40 percent. The RMB offshore market remained buoyant and maintained this upward trend.

II. Timely conducting Medium-term Lending Facility and Standing Lending Facility operations

Conducting MLF operations in a timely manner. To ensure an appropriate supply of medium and long-term liquidity and to give play to the signaling and guiding functions of the medium-term policy rates, the PBC conducted a total of RMB2.55 trillion of MLF operations during the first nine months of 2021, all with a maturity of one year and an interest rate of 2.95 percent. The MLF operations conducted in Q3 totaled RMB1.3 trillion. At end-September, the outstanding MLF registered RMB5.0 trillion, RMB150 billion less than that at the beginning of 2021.

Advancing the reforms of SLF operations. Advancing the reforms of the electronic operations of the SLF to orderly achieve an entire electronic process and to enhance operational efficiency. The demand for short-term liquidity by locally incorporated financial institutions was met in the full amount to stabilize market expectations, to bolster up the stability of liquidity in the banking system, and to prevent liquidity risks. During the first nine months of 2021, the PBC conducted RMB61.81 billion worth of SLF operations, of which operations in Q3 registered RMB2.75 billion and the balance of such operations at end-September posted RMB1.43 billion. The SLF rate played its role as the ceiling of the interest rate corridor, and it promoted the smooth operation of the money market. At end-September, the overnight, 7-day, and 1-month SLF rates stood at 3.05 percent, 3.20 percent, and 3.55 percent, respectively, on par with the rates at the end of the previous quarter.

III. Lowering the required reserve ratio for financial institutions

The required reserve ratio for financial institutions was lowered by 0.5 percentage points in an attempt to support the real economy and ensure that the costs of overall financing drop steadily. The PBC decided to reduce the required reserve ratio by 0.5 percentage points, effective on July 15 (not applicable to financial institutions that had already implemented an required reserve ratio of 5 percent), releasing about RMB1 trillion of long-term funds. After this round of RRR cuts, the weighted average required reserve ratio for financial institutions stood at 8.9 percent. This RRR reduction is a conventional operation following the normalization of monetary policies, aimed at improving the funding structure of financial institutions and enhancing their capability to allocate funds. First, by keeping adequate liquidity at a reasonable level, the PBC created a favorable monetary and financial environment for high-quality development and supply-side structural reform. Second, by optimizing the financing structure of financial institutions, the PBC effectively expanded the sources of long-term stable funding for financial institutions to support the real economy and guided these institutions to actively use the funds released from the RRR reduction to boost support for MSBs. Third, the RRR reduction lowered the funding costs of financial institutions by approximately RMB13 billion per year, which further reduced overall social financing costs through the transmission of financial institutions.

IV. Further improving the macro-prudential management framework

The regulatory framework for systemically important financial institutions was improved. On October 15, the PBC and CBIRC promulgated the *Additional Regulatory Rules for Systemically Important Banks (SIBs) (Trial)* (Order No.5 [2021] of the PBC and CBIRC) in an attempt to provide guidance and standards for implementing regulation over the SIBs. The contents are as follows. First, the *rules* specify the requirements for additional regulatory indicators, such as additional capital and an additional leverage ratio. Second, the requirements for recovery and resolution plans (RRP) are clarified. The SIBs shall formulate a proposal for group-level RRP and submit it for review to the crisis management group, which is led by the PBC, in line with the regulations. Third, prudential supervision requirements are specified, such as information reporting and disclosure, aggregated risk data, and risk reports, as well as corporate governance. Based on monitoring and analysis as well as the results of pressure tests, the PBC and CBIRC may issue risk warnings to SIBs as appropriate and urge relevant institutions to reduce systemic financial risks. On the same day, the PBC and CBIRC published a list of domestic

SIBs, of which 19 banks were identified as domestic SIBs on the basis of a data assessment in 2020, including six state-owned commercial banks, nine joint-stock commercial banks, and four city commercial banks. The SIBs are categorized into five groups according to their systemic importance in ascending sequence. Group One consists of eight banks, namely Ping An Bank, China Everbright Bank, Huaxia Bank, China Guangfa Bank, Bank of Ningbo, Bank of Shanghai, Bank of Jiangsu. and Bank of Beijing. Group Two consists of four banks, including SPD Bank, China Citic Bank, China Minsheng Bank, Postal Savings Bank of China. Group Three consists of three banks, namely Bank of Communications, China Merchants Bank, and Industrial Bank. Group Four consists of four banks, including Industrial and Commercial Bank of China, Bank of China, China Construction Bank, and Agricultural Bank of China. For the time being, no bank is categorized in Group Five.

V. Actively leveraging the role of structural monetary policy instruments

Actively using central bank lending to support rural development, central bank lending for MSBs, central bank discounts, and other tools to guide financial institutions to enhance support for key areas and weak links in the national economy, such as MSBs, private firms, agriculture, rural areas, and rural people, as well as poverty alleviation, and for coordinated regional development. The role of central bank lending was further brought into play to provide targeted liquidity and to serve as a positive incentive so as to support and consolidate the effective connections between the achievements in poverty eradication and rural revitalization. Central bank lending to support rural development and central bank lending for MSBs were used to guide locally incorporated financial institutions to expand credit supply for rural revitalization. Central bank lending for poverty alleviation was rolled over according to the current regulations so as to underpin and consolidate the achievements of poverty eradication. Coordinated regional development was promoted, with enhanced support for the real economy. In ten provinces, locally incorporated financial institutions were guided to leverage well the quota of RMB200 billion of central bank lending and to step up support for the economic weak links, such as local agro-related businesses, MSBs, and private firms. In order to implement the decisions and arrangements of the State Council on enhancing help and assistance to market entities, especially MSMEs, to weather difficulties, the PBC added a new quota of RMB300 billion of central bank lending for MSBs in order to back locally incorporated financial institutions to issue loans at lower financing costs to MSBs and self-employed businesses which were hit hard by mounting commodity prices and the pandemic. As of end-September, outstanding central bank lending to support rural development stood at RMB474.7 billion. Outstanding central bank lending for MSBs and for poverty alleviation posted RMB993.7 billion and RMB190.4 billion, respectively. Outstanding central bank discounts registered RMB584.2 billion. During the first nine months, the PBC made net withdrawals of PSLs in the amount of RMB350.6 billion from development and policy banks, with net withdrawals in Q3 totaling RMB208.2 billion and the outstanding PSLs registering RMB2.8844 trillion at end-September.

Steadily advancing two monetary policy instruments that directly support the real economy with highlighted characteristics of directness and precision to bolster the development of MSMEs. From the introduction of the policy in June 2020 to end-September 2021, operations of the instrument supporting deferred repayments on inclusive MSB loans were conducted on a monthly basis. The instrument provided a total of RMB17.8 billion of incentive funds for locally incorporated banks, which supported an extension of RMB1.7833 trillion in principal repayments on inclusive MSB loans so as to ease the phased pressures on MSBs to repay the principal and interest. The support plan for inclusive unsecured MSB loans operated on a quarterly basis. Cumulative preferential funding of RMB274.4 billion was used to provide support for the issuance of RMB765.1 billion of unsecured loans to MSBs, thereby effectively alleviating their difficulties in accessing financing. From the beginning of 2020 to September 2021, banking institutions nationwide deferred RMB13.5 trillion of principal and interest repayments and issued a cumulative RMB8.6 trillion of inclusive unsecured MSB loans.

Implementing the important decisions and deployment of the CPC Central Committee and the State Council on carbon peaking and carbon neutrality, and launching the carbon emission reduction facility (CERF). As a structural monetary policy instrument, the CERF aims to support the development of clean energy, energy conservation, environmental protection, carbon reduction technology, and other relevant key areas in a steady and direct manner and to mobilize more social capital to promote a carbon reduction. Under a direct mechanism of “central bank lending follows corporate loans,” the PBC provides funds in the amount of 60 percent of the principal at a rate of 1.75 percent for qualified carbon emission reduction loans to relevant enterprises in key areas for carbon emission reduction. Under this facility, the PBC guides financial institutions to issue carbon reduction loans on an equal basis and at rates close to the loan prime rate (LPR) of the same maturity, under the preconditions that the institutions make independent decisions and bear the risks by themselves. The CERF complements efforts to beef up the overall capacity for energy supply by using incremental funds to support the investment and development of clean energy and other key areas. On the basis of the CERF, an additional RMB200 billion of special central bank lending was introduced to support the clean and efficient use of coal so as to achieve policy scale and promote green and low-carbon development.

VI. Bringing into play the role of credit policy to guide structural reform

Financial support to keep businesses and employment stable was stepped up. The Project of Enhancing the Capacity to Provide Financial Services for MSMEs was further advanced in a bid to promote MSB financing, featuring “increased volume, expanded coverage, and lowered prices”. At end-September 2021, outstanding inclusive loans to MSBs grew by 27.4 percent year on year to RMB18.6 trillion. These loans supported 40.92 million MSBs, an increase of 30.8 percent year on year. By focusing on key support groups and key businesses, the PBC made innovations in many types of activities connecting government agencies, banks, and businesses to enable more effective and better-targeted connections for financing. From the beginning of 2020 to end-September 2021, a nationwide enterprise list was developed, comprising 456,000 firms in pandemic-hit industries and core businesses in the supply chain, under which financial institutions extended loans to 193,000 enterprises cumulatively, totaling RMB7.5 trillion.

Support was provided by the financial sector to consolidate and expand the achievements of poverty eradication, and rural revitalization was promoted in a comprehensive manner. On August 23, the PBC took the lead in holding a tele-conference on Financial Support for Consolidating and Expanding Achievements in the Critical Battle against Poverty and Comprehensively Promoting Rural Revitalization, which urged and guided financial institutions to strictly follow the requirements of the “Four Withouts,” i.e., lifting areas out of poverty without loading off responsibilities, without abolishing policies, without ceasing support, and without removing supervision, so as to continuously support development of the regions and population that had been lifted out of poverty. Meanwhile, the PBC ensured financial services to key areas that safeguard an efficient supply of grain and vital agricultural products as well as to key entities such as new types of agribusinesses. At end-September 2021, outstanding agro-related loans increased 10.1 percent year on year to RMB42.64 trillion.

VII. Further deepening the market-based interest rate reform

The benefits of the LPR reform were continuously unleashed. First, financial institutions were encouraged to take full advantage of the LPR in pricing so as to enhance competition in the MSB loan market and promote the steady drop of actual loan rates on the basis of their significant decrease in 2020. **Second**, the PBC implemented measures to optimize regulation over deposit rates, maintained fair competition in the deposit market, and modified the mechanism for a self-regulatory ceiling of deposit rates by adding basis points to the benchmark interest rates so as to guide medium-to-long-term deposit rates to move down, improve the maturity structure of deposits, reduce bank liability costs, and encourage the financial sector to make interest concessions to the real economy. **Third**, lenders of all sorts were continuously promoted to explicitly post the annualized interest rates of their loan products so as to protect the legitimate rights and interests of financial consumers. In addition, the PBC continued to advance the onshore shift in international benchmark interest rates. It guided the National Association of Financial Market Institutional Investors (NAFMII), in collaboration with the International Swaps and Derivatives Association (ISDA), to study and release the standard document for the backup mechanism of the Interbank Offered Rate (IBOR) in the NAFMII master agreement. Beginning from July 30, 2021, market participants may sign multilateral agreements and file with the NAFMII. The standard document took effect on October 29, 2021.

Box 2 Significant Achievements in the Optimization of the Self-regulatory Ceiling of Deposit Interest Rates

On June 21, 2021, the PBC guided the Self-regulatory Mechanism for Market Rate Pricing (hereinafter referred to as the Mechanism) to shift from multiplying the benchmark deposit rates by a designated multiplier to adding basis points to the benchmark interest rates, while setting the ceiling for deposit interest rates. Since its implementation, remarkable achievements have been made in optimizing the self-regulatory ceiling of deposit interest rates, with competition in the deposit market more orderly, long-term deposit interest rates obviously declining, and the maturity structure of time deposits becoming fairly optimized. The distribution of deposits among banks remains basically stable, conducive to stabilizing the liability costs of banks.

For a long period of time, the deposit market in China has faced fierce competition. In particular, several banks have attracted deposits at high interest rates due to their high-risk operations and blind pursuance of scale expansions. As a result, normally operating banks had to follow the pricing, landing them in a “prisoner’s dilemma,” which led to the issue of “pricing by bad banks”. This has hampered the transmission of market-based interest rates to the deposit interest rates and to some extent it has affected the promotion of the market-oriented reform of deposit interest rates through the LPR reform. In 2013, the Mechanism was established under the guidance of the PBC, aimed at self-regulation on interest-rate pricing by financial institutions. After relaxing control on deposit interest rates in 2015, the Mechanism has set the ceiling for deposit interest rates through self-regulatory negotiations, placed constraints on the attraction of deposits at high interest rates by several banks, and restrained irrational competition in the deposit market, effectively safeguarding orderly competition in the deposit market. However, as in the past a leverage effect occurred, with the self-regulatory ceiling determined by adjusting the benchmark deposit rates by a designated multiplier, the medium and long-term deposit interest rates were relatively high. Several banks could absorb deposits at high interest rates through the so-called "innovative" products, such as time deposit products withdrawn in advance with the interest calculated with reference to the interest rate of time deposits with a corresponding maturity, which has weakened the self-regulatory effect of the deposit interest rates.

After the optimization of the self-regulatory ceiling for deposit interest rates, the self-regulatory ceilings for demand deposits and short and medium-term time deposits with a maturity of one year or less have remained basically stable, and that of long-term time deposits with a maturity of two years or longer has been slightly reduced. This has not only guaranteed room for the independent pricing of banks but also has effectively put constraints on the irrational competition of some banks. Since its implementation, the optimized self-regulatory ceiling for deposit interest rates has produced remarkable results. **First**, deposit interest rates have witnessed notable changes, with the short- and medium-term deposit interest rates basically stable and the long-term rates obviously declining, leading to more orderly competition in the deposit market. In September, the weighted average interest rate for new time deposits stood at 2.21 percent, decreasing 0.17 percentage points year on year and 0.28 percentage points from May before the optimization. In particular, the two-year, three-year, and five-year time deposit interest rates fell by 0.25 percentage points, 0.43 percentage points, and 0.45 percentage points from May, respectively. **Second**, the maturity structure of time deposits has been optimized, with the proportion of actual long-term deposits against all time deposits somewhat reduced. In September, new time deposits stood at RMB5.6 trillion. In particular, long-term time deposits with a maturity of two years or longer accounted for 26.4 percent, decreasing 5.9 percentage points year on year and 10.6 percentage points from May. **Third,** the distribution of deposits among banks has remained basically stable. In September, actual time deposits in nationwide banks totaled RMB3.7 trillion. They accounted for 66 percent of total deposits, up 0.7 percentage points year on year and up 3.2 percentage points from May. In particular, interest rates on long-term time deposits with a maturity of two years or longer witnessed a notable decline, of which nationwide banks in September held RMB784.2 billion. They accounted for 53.3 percent of the total, down 1.4 percentage points year on year and down 0.9 percentage points from May.

Table of Changes in Deposit Interest Rates Before and After Optimization of the

Self-regulatory Ceiling

deposit maturity			demand deposits	three months	half a year	one year	two years	three years	five years
benchmark deposit interest rates			0.35	1.10	1.30	1.50	2.10	2.75	—
self-regulatory ceiling of deposit interest rates	pre-optimization (floating multiplier)	state-owned banks （1.4 times）	0.49	1.54	1.82	2.10	2.94	3.85	—
		other banks (1.5 times)	0.53	1.65	1.95	2.25	3.15	4.13	—
	post-optimization (determined by adding basis points)	state-owned banks (plus 50 basis points)	0.45	1.60	1.80	2.00	2.60	3.25	—
		other banks (plus 75 basis points)	0.55	1.85	2.05	2.25	2.85	3.50	—
weighted average deposit interest rates (September versus May in 2021)			0.00	0.01	0.00	-0.04	-0.25	-0.43	-0.45

Going forward, the PBC will continue to deepen the market-oriented reform of interest rates, continuously unleash the potential of the LPR reform, smooth the transmission channel for loan interest rates, optimize the allocation structure of financial resources, and consolidate previous achievements in reducing loan interest rates. Meanwhile, the PBC will optimize regulation over deposit interest rates, keep the liability costs of financial institutions basically stable, and urge financial institutions to transfer the policy benefits to the real economy so as to secure the general stability of loan interest rates with a decline.

VIII. Improving the market-based RMB exchange-rate formation mechanism

The PBC continued to advance the market-based reform of the RMB exchange rate and to improve the managed floating exchange rate regime based on market supply and demand with reference to a basket of currencies. It maintained the flexibility of the RMB exchange rate and gave play to the role of the exchange rate as an automatic stabilizer in adjusting the macro economy and the balance of payments. The PBC attached importance to guiding expectations and kept the RMB exchange rate basically stable at an adaptive and equilibrium level. In Q3 2021, the highest and lowest RMB central parities against the USD were 6.4330 and 6.4984, respectively. During the 64 trading days, the RMB appreciated on 31 days and depreciated on 33 days. The biggest intraday appreciation and depreciation were 0.5 percent (340 bps) and 0.3 percent (215 bps), respectively. The RMB exchange rate appreciated against the other major international currencies. At end-September, the central parities of the RMB against the dollar, the euro, the pound, and the Japanese yen appreciated 0.6 percent, 6.6 percent, 2.1 percent, and 9.2 percent, respectively, from end-2020. Since the reform of the RMB exchange-rate formation mechanism that commenced in 2005 to end-September 2021, the RMB had appreciated by a cumulative total of 27.6 percent, 33.1 percent, and 26.1 percent, respectively, against the dollar, the euro, and the Japanese yen. A work conference on the foreign exchange market self-regulatory framework was held, requiring that financial institutions actively provide services for MSMEs to hedge against exchange-rate risks and to help them reduce related costs. In October 2021, the China Foreign Exchange Trade System started to reduce by 50 percent the service fees related to MSMEs' derivatives trading on the interbank market so as to reduce the hedging costs of MSMEs and to support the development of the real economy. Meanwhile, direct RMB trading was buoyant in the interbank foreign exchange market with stable liquidity, which helped lower the exchange costs of micro economic entities and facilitated bilateral trade and investment.

Table 8 Trading Volume of the RMB against Other Currencies in the Interbank Foreign Exchange Spot Market in Q3 2021

Unit: RMB100 million

Currency	USD	EUR	JPY	HKD	GBP	AUD	NZD
Trading volume	158866.06	4547.95	458.54	484.47	188.37	110.50	36.39
Currency	SGD	CHF	CAD	MYR	RUB	ZAR	KRW
Trading volume	93.83	26.99	68.53	1.29	14.26	0.33	18.24
Currency	AED	SAR	HUF	PLN	DKK	SEK	NOK
Trading volume	0.02	0.54	0.20	1.47	2.12	7.07	3.04
Currency	TRY	MXN	THB	KHR	KZT	MNT	IDR

Trading volume	0.08	0.19	87.58	0	0	0	2.61

Source: China Foreign Exchange Trade System.

As of end-September, under the bilateral currency swap agreements between the PBC and the foreign monetary authorities, the foreign monetary authorities utilized a total of RMB61.531 billion and the PBC utilized foreign currencies equivalent to USD473 million. These operations played an active role in promoting bilateral trade and investment.

IX. Forestalling and defusing financial risks and deepening the reform of financial institutions

Financial risks were forestalled and defused. The *China Financial Stability Report* (2021) was issued, which introduced overall performance of the economy and finance at home and abroad. It continuously improved the risk monitoring of the banking, securities, and insurance sectors and the financial market, conducted a comprehensive assessment of the stability of the financial industry, summarized recent developments in China's construction of a systemic financial risk prevention and control framework, and enhanced communications with the general public, market entities, and international society in terms of financial stability. The central bank rating of financial institutions in Q2 was completed, with over 4000 banking financial institutions being rated throughout the nation. As the actual risk situation was ascertained, high-risk institutions were identified precisely. The PBC conducted stress tests on over 4000 banking financial institutions, timely imposing risk alerts and guiding financial institutions to operate in a sound manner. Risk resolution, reform, and restructuring of small and medium-sized financial institutions were promoted orderly and periodic progress was made in the risk disposal of key high-risk conglomerates.

Reform of development and policy financial institutions was continuously deepened. The PBC continued to implement reform plans for development and policy financial institutions to redefine their responsibilities and business scope, apply classified accounting, improve corporate governance, strengthen restraint mechanisms, and prevent financial risks. The PBC guided development and policy financial institutions to fulfill their responsibilities, focus on their main business, and give full play to their role in supporting economic restructuring and high-quality development on the basis of strengthening risk prevention and control.

X. Deepening reform of foreign exchange arrangements

Pilot programs were promoted in terms of expanding the coverage and improving the quality of trade facilitation. Pilot conditions for trade facilitation were verified in a high-standard manner. Coverage of the program was expanded in a steady and orderly manner and the pilot program was further optimized, promoting internal compliance and targeted facilitation of market entities. As of end-September 2021, the pilot program had been expanded to incorporate 26 areas, 123 banks, and 1192 enterprises.

Tax filing of outbound payments under trade in services was optimized. In July 2021, the SAFE and the State Taxation Administration jointly released the *Supplementary Notice on Tax Filing of Outbound Payments under Trade in Services* (STA SAFE Notice [2021]19) and relevant policy interpretations. It expanded the scope of businesses exempt from filing taxes and facilitated "filing only when making the first foreign exchange payment under each contract", which has further enhanced the facilitation of outward payments in foreign exchange under trade in services for domestic institutions and individuals.

The healthy development of new forms of trade was promoted. The SAFE continued to give play to the advantage of banks in cross-border settlements and to provide support for more banks to handle cross-border e-commerce businesses based on electronic transaction information, in a bid to promote the healthy and orderly development of cross-border e-commerce. As of end-September, 12 banks were eligible to handle foreign exchange businesses with respect to new forms of trade based on electronic transaction information, involving more than 8000 merchants.

The regular issuance of qualified domestic institutional investors (QDII) quota was continuously promoted. In August 2021, the SAFE issued QDII quota totaling USD2.5 billion to three institutions, better satisfying the reasonable demand of domestic market entities for cross-border asset allocations so as to further promote the two-way opening-up of the financial market.

Part 3. Financial Market Conditions

In Q3 2021, the financial market operated in a generally sound and stable manner. Money market interest rates remained stable with active market transactions. The bond market featured increased bond issuances, declined bond coupon rates, and decreased cash bond transactions. The stock market index fluctuated downwards and turnover witnessed relatively rapid increases.

I. Financial market overview

1. Money market interest rates remained stable, and the growth of market transactions was active.

Money market interest rates were generally stable. In September, the monthly weighted average interest rate of pledged repos posted 2.19 percent, 2 basis points higher than that in June. The monthly weighted average interest rate of government-backed bond repos among depository institutions posted 2.06 percent, 13 basis points lower than the monthly weighted average interest rate of pledged repos in the interbank market. In September, the monthly weighted average interest rate for interbank lending posted 2.16 percent. At end-September, the overnight and 7-day Shibor posted 2.22 percent and 2.27 percent, respectively.

Market transactions were active. In Q1–Q3 2021, the volume of bond repos trading on the interbank market reached RMB751.8 trillion, representing an average daily turnover of RMB4 trillion, up 2.5 percent year on year. The volume of cumulative trading of interbank lending registered RMB88 trillion, with an average daily turnover of RMB467.9 billion and a year-on-year decrease of 24.4 percent. In terms of the maturity structure, overnight repos accounted for 83.9 percent of the total turnover in bond repos, decreasing 0.9 percentage points year on year, and overnight lending made up 89.2 percent of interbank lending, down 1.3 percentage points year on year. The volume of bond repos traded on the exchange markets increased 21.6 percent year on year to RMB251.6 trillion.

Table 9 Fund Flows Among Financial Institutions in Q1–Q3 2021

Unit: RMB100 million

	Repos		Interbank lending	
	Q1-Q3 2021	Q1-Q3 2020	Q1-Q3 2021	Q1-Q3 2020
Chinese-funded large banks①	-1,576,735	-2,088,769	-217,149	-319,064
Chinese-funded medium-sized banks②	-1,179,586	-654,137	-66,807	-45,958
Chinese-funded small-sized banks③	97,677	-1,119	78,991	94,169
Securities institutions④	990,838	820,183	158,666	205,936
Insurance institutions⑤	96,662	90,597	295	650
Foreign-funded banks	55,426	58,785	-19,375	-18,575
Other financial institutions and vehicles⑥	1,515,718	1,774,460	65,380	82,841

Notes：①Chinese-funded large banks include the Industrial and Commercial Bank of China, Agricultural Bank of China, Bank of China, China Construction Bank, China Development Bank,

Bank of Communications, and Postal Savings Bank of China. ②Chinese-funded medium-sized banks refer to policy banks, China Merchants Bank, and the eight other joint-equity commercial banks, Bank of Beijing, Bank of Shanghai, and Bank of Jiangsu. ③Chinese-funded small-sized banks refer to Hengfeng Bank, China Zheshang Bank, China Bohai Bank, other city commercial banks, rural commercial banks, rural cooperative banks, private banks, and village and township banks. ④Securities institutions include securities firms, fund management companies, and futures companies. ⑤Insurance institutions include insurance firms and corporate annuities. ⑥Other financial institutions and vehicles include urban credit cooperatives, rural credit cooperatives, finance companies, trust and investment companies, financial leasing companies, asset management companies, social security funds, mutual funds, wealth management products, trust plans, and other investment vehicles. Some of these financial institutions and vehicles do not participate in the interbank lending market. ⑦A negative sign indicates net lending and a positive sign indicates net borrowing.
Source: China Foreign Exchange Trade System.

Interbank Certificates of Deposit (CD) and negotiable CD businesses witnessed orderly development. In Q3 2021, 7,115 interbank CDs were issued on the interbank market, raising RMB5 trillion. The volume of trading on the secondary market totaled RMB37.2 trillion. At end-September, outstanding interbank CDs reached RMB12.7 trillion. In Q3 2021, the average weighted interest rate of 3-month interbank CDs was 2.44 percent, 5 basis points higher than that of the 3-month Shibor. A total of 10,681 negotiable CDs was issued by financial institutions in Q3 2021, raising RMB2.4 trillion, with an increase of RMB408.6 billion year on year.

The turnover of interest rate swaps operated stably. In Q3 2021, the RMB interest rate swap market witnessed 62,800 transactions, decreasing 13.1 percent year on year, with the volume of the notional principal totaling RMB5.4 trillion, an increase of 16.5 percent year on year. In terms of the maturity structure, contracts with maturities of up to one year traded most briskly and the volume of the notional principal posted RMB3.9 trillion, accounting for 72.6 percent of the principal of all maturities. The 7-day fixing repo rate and the Shibor served as the main reference rates for the floating leg of the RMB interest rate swaps, accounting for 86.3 percent and 12.8 percent, respectively, of the total notional principal of the interest rate swaps. In Q3 2021, interest rate swaps anchored to the loan prime rate (LPR) witnessed 195 transactions, with RMB30.02 billion of the notional principal.

Table 10 Interest Rate Swap Transactions in Q3 2021

	Transactions	Notional principal (RMB100 million)
Q3 2021	62,757	54,349.6
Q3 2020	72,310	46,568.5

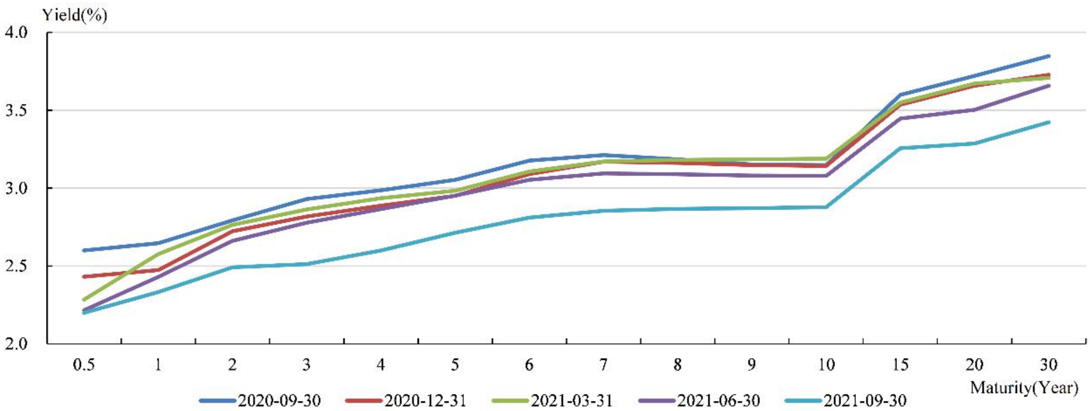
Source: China Foreign Exchange Trade System.

The LPR interest rate option business developed steadily. The LPR interest rate option business made its debut on the interbank market in March 2020, and fixing repo rate (FDR) options were newly added to the interbank market on March 29, 2021. In Q3 2021, a total of 81 interest rate option transactions were concluded, totaling RMB22.119 billion. Specifically, one was an interest rate swap transaction, amounting to RMB10 million of the notional principal, and 80 were interest rate cap/floor transactions, amounting to RMB22.109 billion of the notional principal.

2. Coupon rates of bonds declined, while bond issuances expanded

Coupon rates of bonds declined. In September, the yield on 10-year government securities issued by the Ministry of Finance was 2.85 percent, 25 basis points lower than that in June. The coupon rate of 10-year financial bonds issued by the China Development Bank (CDB) was 3.13 percent, 34 basis points lower than the rate in June. The average rate of 1-year short-term financing bills (bond rating A-1) issued by AAA-rated enterprises was 3.86 percent, 8 basis points lower than the rate in June.

Figure 4 Yield Curves of Government Securities on the Interbank Market



Source: China Central Depository & Clearing Co., Ltd.

On the whole, government securities yields went down, with the term spreads narrowing. At end-September, yields on 1-year and 10-year government securities decreased by 10 basis points and 20 basis points to 2.33 percent and 2.88 percent from end-June, respectively; the term spread between 1-year and 10-year government securities was 54 basis points, down 10 basis points from end-June. Credit spreads expanded at end-September, with yield spreads on 3-year AAA and AA-rated short-to-medium-term bills and CDB bonds widening by 2 basis points and 12 basis points to 42 basis points and 113 basis points from end-June, respectively.

Bond issuances saw year-on-year growth. In the first three quarters, the cumulative value of bond issuances increased by 6.2 percent, or RMB2.6 trillion, year on year to RMB45.1 trillion, most of which were interbank CDs. At end-September, outstanding bonds held in custody amounted to RMB128.1 trillion, representing an increase of 12.6 percent year on year.

The volume of spot bond transactions on the interbank market decreased, while that on the stock exchange continued to grow. In the first three quarters, the value of cash bonds trading on the bond market posted RMB175.2 trillion, registering a decrease of 14.7 percent year on year. Specifically, the value of cash bonds trading on the interbank market was RMB155 trillion, representing a decrease of 19.3 percent year on year. The value of cash bond transactions on the stock exchanges totaled RMB20.2 trillion, an increase of 50.3 percent year on year.

Table 11 Bond Issuances in Q1–Q3 2021

Unit: RMB100 million

Type of bond	Issuance	YOY change
Government securities	46,640	-1,229
Local government bonds	56,155	-634
Central bank bills	0	0
Financial bonds①	238,223	26,115
Of which: Financial bonds issued by the CDB and policy financial bonds	44,861	1,078
Interbank certificates of deposit	158,923	26,257
Corporate credit bonds②	109,016	1,877
Of which: Debt-financing instruments of non-financial enterprises	71,875	776
Enterprise bonds	4,430	279
Corporate bonds	24,124	831
Bonds issued by international institutions	710	205
Total	450,744	26,334

Notes: ①Including financial bonds issued by the CDB, policy financial bonds, bonds issued by commercial banks (including ordinary bonds, subordinated bonds, and hybrid bonds), bonds issued by securities firms, and interbank certificates of deposit. ② Including debt-financing instruments issued by non-financial enterprises, enterprise bonds, corporate bonds, convertible bonds, bonds with detachable warrants, privately offered SME bonds, and asset-backed securities on the Shanghai Stock Exchange and the Shenzhen Stock Exchange issued by non-financial enterprises.

Sources: The People's Bank of China, China Securities Regulatory Commission, and China Central Depository & Clearing Co., Ltd.

3. Bill financing saw steady growth, and interest rates in the bill market were

basically stable

The bill acceptance business recorded stable growth. In the first three quarters, commercial drafts issued by enterprises totaled RMB18.0 trillion, rising 8.8 percent year on year. At end-September, outstanding commercial drafts stood at RMB14.6 trillion, increasing by 4.9 percent year on year. At end-September, outstanding commercial draft acceptances witnessed stable growth, increasing by RMB500.0 billion from the beginning of this year and RMB249.6 billion from end-June, respectively. Of the outstanding bankers' acceptances, 67.5 percent was issued by micro, small, and medium-sized enterprises (MSMEs).

Bill financing witnessed steady growth, with generally stable interest rates. In the first three quarters, total discounts by financial institutions amounted to RMB34.9 trillion, growing 14.1 percent year on year. At end-September, the balance of bill financing was RMB9.2 trillion, up 13.9 percent year on year. The balance accounted for 4.8 percent of total outstanding loans, up 0.1 percentage points year on year. In the first three quarters, the interest rates for bill financing first increased and then decreased, but they remained generally stable.

4. Stock indices experienced a choppy fall, with turnover and the amount of funds raised increasing year on year

The stock indices experienced a choppy fall. At end-September, the Shanghai Stock Exchange Composite Index closed at 3,568 points, decreasing by 0.6 percent from end-June. The Shenzhen Stock Exchange Component Index closed at 14,309 points, decreasing by 5.6 percent from end-June. Turnover on the stock markets maintained fast growth. In the first three quarters, the combined turnover on the Shanghai Stock Exchange and the Shenzhen Stock Exchange reached RMB190.9 trillion, and the average daily turnover was RMB1048.7 billion, representing an increase of 21.1 percent year on year. The amount of funds raised on the stock markets increased year on year. In the first three quarters, a cumulative RMB1 trillion was raised, increasing by 25.2 percent year on year.

5. Premium income decreased year on year and the growth of assets in the insurance sector slowed down

In the first three quarters of 2021, total premium income in the insurance sector amounted to RMB3.7 trillion, down 1.3 percent year on year, a deceleration of 7.4 percentage points from the previous year. Claim and benefit payments totaled RMB1.2 trillion, representing a year-on-year increase of 16 percent. Specifically, total property insurance claims and benefit payments increased by 10.5 percent year on year, and total life insurance claims and benefit payments went up by 21.3 percent year on year.

Table 12 Asset Allocations in the Insurance Sector at End-September 2021

Unit: RMB100 million, %

	Balance		As a share of total assets	
	End- September 2021	End-September 2020	End-September 2021	End-September 2020
Total assets	243,196	224,386	100.0	100.0
Of which: Bank deposits	26,095	25,796	10.7	11.5
Investments	198,331	181,266	81.6	80.8

Source: China Banking and Insurance Regulatory Commission.

The growth of assets in the insurance sector slowed down. At end-September 2021, total assets in the insurance sector increased 8.4 percent year on year to RMB24.3 trillion, a deceleration of 4.9 percentage points from end-2020. Specifically, bank deposits increased by 1.2 percent, while investment-linked assets increased by 9.4 percent year on year.

6. Turnovers of spot and swap foreign exchange transactions witnessed rapid growth

In the first three quarters of 2021, the cumulative turnover of spot RMB/foreign exchange transactions registered USD7.5 trillion, an increase of 32.1 percent year on year. The cumulative turnover of swap RMB/foreign exchange transactions totaled USD14.6 trillion, an increase of 21.1 percent year on year. Specifically, cumulative overnight RMB/USD swap transactions posted USD9.7 trillion, accounting for 66.7 percent of the total swap turnover. The turnover of RMB/foreign exchange forward transactions totaled USD83.5 billion, rising 10.8 percent year on year. The turnover of foreign currency pair transactions totaled USD1 trillion, increasing by 102.9 percent year on year. In particular, the EUR/USD pair registered the largest trading volume, accounting for 59.1 percent of the total market share.

7. The volume of gold trading declined and prices went down

At end-September 2021, international gold prices closed at USD1,742.8 per ounce, representing a loss of 1.2 percent from end-June. The Au99.99 on the Shanghai Gold Exchange closed at RMB362.14 per gram, decreasing by 1.0 percent from end-June. In the third quarter of 2021, the volume of gold traded on the Shanghai Gold Exchange was 7,850.67 tons, representing a decrease of 49.9 percent year on year. Turnover posted RMB2.94 trillion, a decrease of 54.8 percent year on year.

II. Development of institutional arrangements in the financial markets

1. Institutional arrangements in the bond market

The development of the credit rating industry in the bond market was further standardized. In August 2021, the PBC, together with the National Development and Reform Commission (NDRC), Ministry of Finance (MOF), China Banking and Insurance Regulatory Commission (CBIRC), and China Securities Regulatory Commission (CSRC) released the *Notice on Promoting the Sound Development of the Credit Rating Industry in the Bond Market* (Yinfa No.206 [2021]). The quality of credit rating was improved, with clearer distinctions among the different rates. With the release of the Notice, credit rating can play a better role in risk disclosures and risk pricing so as to create a fair and equitable market environment and to serve the sound development of the bond market.

A multi-layered bond market system was formed and improved. In August 2021, the PBC, NDRC, MOF, CBIRC, CSRC, and the State Administration of Foreign Exchange (SAFE) jointly released the *Guiding Opinions on Advancing the Reform, Opening-Up, and High-Quality Development of the Corporate Credit Bond Market* (Yinfa No.217 [2021]). The Guiding Opinions aimed to improve the legal system for the bond market and to build a multi-tiered bond market system featuring robust regulation, orderly competition, transparency, and openness.

The high-level two-way opening-up of China's bond market pressed ahead in a steady manner. On September 15, 2021, the PBC and the Hong Kong Monetary Authority (HKMA) jointly announced the launch of Southbound Trading under the mutual bond market access and connection scheme between the Mainland and Hong Kong (hereinafter referred to as the "Southbound Bond Connect"). On the same day, the PBC released the *Notice of the PBC on Launching Southbound Trading under Mutual Bond Market Access between the Mainland and Hong Kong*. The Southbound Bond Connect is an important step taken by the central government to support the economic development of Hong Kong and to promote cooperation between the Mainland and Hong Kong. First, the launch of the Southbound Bond Connect served as an institutional arrangement that enhanced the two-way opening-up of China's bond market and further expanded domestic investors' asset allocation opportunities in international financial markets. Second, it helped cement the status of Hong Kong as a gateway and hub linking the Mainland and international markets, integrate it into the big picture of national development, and safeguard its prosperity and stability in the long run.

2. Institutional arrangements in the capital market and the securities and futures sector

The registration-based reform of the IPO system forged ahead steadily to cover all stock markets. In July 2021, the CSRC issued the *Guiding Opinions on Urging Securities Companies to Engage in Investment Banking with a Commitment to Compliance and Duties under the Registration System.* The Guiding Opinions strengthened regulation of investment banking businesses, such as sponsorship, underwriting, and financial consulting, to urge securities companies to earnestly perform their duties and better serve as "gatekeepers." In September, the CSRC released the revised *Special Provisions on the Issuance and Underwriting of Initial Public Offerings on the Growth Enterprise Market*. The Special Provisions improved the issuance and underwriting rules of registration-based IPOs, which enabled a better equilibrium in the buyer-seller game, as well as enhanced the decisive role of the market in resource allocation. In September, the CSRC released the *Regulations on the Guidance of Initial Public Offerings and Listings*, which further regulated guidance-related work and leveraged the advantages of the CSRC's agencies as local supervisors. With intermediaries shouldering due responsibilities, the quality of listed companies will be improved at the source.

The legal system for the capital market was improved. In July 2021, the CSRC released the *Measures on Administrative Penalties for Illegal Acts in Securities and Futures*, which regulated the administrative penalty- related work of the CSRC and its agencies so as to maintain market order and protect the legitimate rights and interests of market entities.

3. Institutional arrangements in the insurance market

The reinsurance business was further regulated. In July 2021, the CBIRC released the newly revised *Regulations on the Reinsurance Business* for the purposes of further regulating the reinsurance business, forestalling and defusing risks, and promoting the high-quality development of the reinsurance market. The revisions covered such aspects as ensuring the management of the top-level reinsurance strategy, improving the safety of the reinsurance business, strengthening regulation over the management of reinsurance contracts, enhancing the management of direct insurers' retrocession business and supervision over reinsurance brokers, and supporting the development of the direct insurance market.

The clauses to regulate the insurance and the premium rates of property and casualty insurance companies were improved. In August 2021, the CBIRC released the newly revised *Measures on Insurance Clauses and Premium Rates of Property and Casualty Insurance Companies*. The revised Measures further improved the institution and mechanism for the regulation of property and casualty insurance companies' products. Adjustments were made with respect to the regulator of insurance clauses and premium rates as well as the management of approvals and filings. The revised

Measures also improved the principles for clause development and premium rate determination, specified responsibility in reviewing the development of the clauses and the determination of the premium rate, and strengthened supervision and regulation of insurance clauses and premium rates.

Market entry for branches of insurance companies was improved. In September 2021, the CBIRC released the *Rules on Market Entry of Branches of Insurance Companies*, which standardized the procedures for insurance companies to set up, alter, and change premises, and remove branches, with an emphasis on improving the provisions concerning the alteration and change of premises and the removal of the branches, as well as the prerequisites for the establishment of branches. The Rules also further clarified the procedures and materials required for administrative approvals, providing standards and facilitation for the application and approval processes.

Part 4. Macroeconomic Overview

I. Global economic and financial developments

In Q3, amid the marginal slowdown in the global economic recovery coupled with the intensified frictions in supply chains, some issues stood out, such as a surge in commodity prices (especially energy products), a tight market for raw materials, a shortage in the labor force for certain industries, and a widened economic gap between different sectors. Looking forward, chances are that the resurgence of the COVID-19 pandemic will haunt the world by fits and starts. The global economy will remain in a complex and serious situation, with hindered overseas production and consumption and prolonged inflation possibly caused by the supply-chain bottleneck and energy shortages. In the meantime, the major developed economies have already started to adjust their monetary policies. High attention needs to be paid to the possible shocks to financial markets and the spillover effects on the emerging economies triggered by these adjustments.

1. Economic performance and financial markets in the major economies

The momentum for a global economic recovery weakened. In Q3, the annualized quarterly rate of GDP in the US posted 2.0 percent, showing a remarkable drop from 6.7 percent in Q2. In particular, the growth rate of personal consumption expenditures plummeted from 12.0 percent in Q2 to 1.6 percent in Q3. The University of Michigan's Index for Consumer Sentiment dropped to about 70, significantly lower than the 85.5 in June. In the euro area, though GDP registered an increase of 2.2 percent in Q3, signs of a slowdown in consumption growth had already emerged. In

Germany, retail sales fell 3.9 percent in August from the previous month and edged up 1.3 percent in September. In the UK, the retail sales index decreased 0.2 percent month on month in September, shrinking for five consecutive months.

The economic divergence was exacerbated by the resurgence of the pandemic. Owing to high COVID-19 vaccination rates, the major advanced economies were able to adopt a strategy characterized by loosened control and booster shots, and hence they reeled only from controllable blows. However, due to limited coverage of the vaccinations, the emerging economies suffered much more, with lockdowns imposed, production hindered, and recovery subdued. The PMI of several emerging economies in Asia fell below 50 into the contraction zone. In September, the manufacturing PMI of Vietnam, Malaysia, and Thailand stood at 40.2, 48.1, and 48.9, respectively.

Supply side bottlenecks became salient, featuring stubbornly high commodity prices. First, supply and demand imbalances were aggravated amid the resurgence of the pandemic and the underproduction of some of the emerging economies that served as crucial processors and manufacturers in the global industrial chain. Second, the transportation sector was constrained by inadequate freight capacity, filled-up storage, a shortage in the labor force, and other drawbacks. Therefore, international freight costs were on a constant and considerable rise. At end-September, the Baltic Dry Index shot up by 199.5 percent year on year. Third, energy prices moved up rapidly. In October, the price of Brent Crude Oil Futures rose above USD80 a barrel, reaching a peak since October 2018. The price of natural gas futures on the New York Mercantile Exchange jumped up to above USD6.4 per million British thermal units, a record high since April 2010. Energy is an essential upstream product whose price movements have a profound transmission effect on industrial and agricultural products. In September, the CPI in the US, the HICP in the euro area, the IPCA in Brazil, and the CPI in Russia rose 5.4 percent, 3.4 percent, 10.3 percent, and 7.4 percent from September 2020, respectively.

Recovery in the labor market was slow. The unemployment rate in the euro area stood at 7.4 percent in September. The US unemployment rate dropped to 4.8 percent in September, yet nonfarm payroll employment increased by only 194,000 during the same period, falling far short of market expectations of 500,000. Meanwhile, the number of job openings in the US was 10.44 million in September, indicating a tough situation both in employment and in recruitment.

Volatility intensified in the international financial market. The market’s concern about the economic outlook gradually unfolded in asset pricing. After reaching historical highs in August, the US and European stock markets entered a phase of correction in September, as evidenced by the Dow Jones Industrial Average Index and the EURO

STOXX 50 Index dropping 4.3 percent and 3.5 percent, respectively. At end-September, the 10-year US Treasury yield went up to 1.52 percent and the US Dollar Index increased by 2.1 percent compared with end-June, which reflected not only market expectations regarding the Federal Reserve's monetary policy adjustments but also the rise of risk-averse sentiments among investors.

Table 13 Macroeconomic and Financial Indicators in the Major Advanced Economies

Economy	Indicator	Q3 2020			Q4 2020			Q1 2021			Q2 2021			Q3 2021		
		Jul.	Aug.	Sept.	Oct.	Nov.	Dec.	Jan.	Feb.	Mar.	Apr.	May	Jun.	Jul.	Aug.	Sept.
United States	Real GDP Growth (annualized quarterly rate, %)	33.8			4.5			6.3			6.7			2.0		
	Unemployment Rate (%)	10.2	8.4	7.8	6.9	6.7	6.7	6.3	6.2	6.0	6.1	5.8	5.9	5.4	5.2	4.8
	CPI (year-on-year, %)	1.0	1.3	1.4	1.2	1.2	1.4	1.4	1.7	2.6	4.2	5.0	5.4	5.4	5.3	5.4
	DJ Industrial Average (end of the period)	26428	28430	27782	26502	29639	30606	29983	30932	32982	33875	34529	34503	34935	35361	33844
Euro Area	Real GDP Growth (year-on-year, %)	-4.0			-4.4			-1.2			14.2			3.7		
	Unemployment Rate (%)	8.4	8.6	8.6	8.4	8.1	8.1	8.2	8.1	8.1	8.1	8.0	7.8	7.6	7.5	7.4
	HICP (year-on-year, %)	0.4	-0.2	-0.3	-0.3	-0.3	-0.3	0.9	0.9	1.3	1.6	2.0	1.9	2.2	3.0	3.4
	EURO STOXX 50 (end of the period)	3174	3273	3194	2958	3493	3572	3481	3636	3919	3975	4039	4064	4089	4196	4048
United Kingdom	Real GDP Growth (year-on year, %)	-8.1			-7.1			-5.8			23.6			6.6		
	Unemployment Rate (%)	4.3	4.5	4.8	5.0	5.1	5.2	5.1	5.0	4.9	4.8	4.8	4.7	4.6	4.5	…
	CPI (year-on-year, %)	1.0	0.2	0.5	0.7	0.3	0.6	0.7	0.4	0.7	1.5	2.1	2.5	2.0	3.2	3.1
	FTSE 100 (end of the period)	5898	5964	5866	5577	6266	6461	6407	6483	6714	6970	7023	7037	7032	7120	7086
Japan	Real GDP Growth (annualized quarterly rate, %)	23.2			11.9			-4.2			1.9			-3.0		
	Unemployment Rate (%)	2.9	3.0	3.0	3.1	3.0	3.0	2.9	2.9	2.6	2.8	3.0	2.9	2.8	2.8	2.8
	CPI (year-on-year, %)	0.3	0.2	0.0	-0.4	-0.9	-1.2	-0.7	-0.5	-0.4	-1.1	-0.8	-0.5	-0.3	-0.4	0.2
	NIKKEI 225 (end of the period)	21710	23140	23185	22977	26434	27444	27663	28966	29179	28813	28860	28792	27284	28090	29453

Sources: Statistical Bureaus and Central Banks of the Relevant Economies.

2. Monetary policies of the major economies

The major advanced economies began to adjust their monetary policies. The Federal Reserve, at the Federal Open Market Committee (FOMC) meeting on November 3, decided to taper asset purchases to the tune of $15 billion per month (consisting of USD10 billion for Treasury securities and USD5 billion for agency mortgage-backed securities) in November and December, with similar reductions in the pace of asset purchases or possible adjustments to the pace likely next year when necessary. After the monetary policy meeting on September 9, the European Central Bank announced that favorable financing conditions could be maintained in Q4, with a moderately lower pace of net asset purchases under the Pandemic Emergency Purchase Programme (PEPP) than in the previous two quarters, releasing a signal of tapering. The Reserve Bank of New Zealand halted its bond purchasing programme. The central banks of Canada and Australia tapered. Norges Bank raised the policy rate from zero to 0.25 percent on September 23. The central banks of South Korea and New Zealand lifted interest rates by 25 basis points to 0.75 percent and 0.5 percent, respectively, on August 26 and October 6.

Several emerging economies continued to raise interest rates. To cope with domestic inflation pressures and to mitigate risks triggered by capital outflows and a currency depreciation, some emerging economies carried on with their interest rate hikes. In October, the central banks of Russia and Brazil both delivered their sixth interest rate hikes this year, adding up to an increase of 325 basis points and 575 basis points, respectively, since the beginning of 2021.

Box 3 Monetary Policy Adjustments in the Developed Economies and the Responses of the PBC

The major developed economies have recently started to adjust their monetary policies. Since June 2021, a signal of tightening monetary policy sent out by the US Federal Reserve has gradually become clear, while the European Central Bank has provided a briefing that it will slow down the pace of asset purchases. In June, the Federal Reserve started to consider gradually withdrawing from the ultra-loose monetary policies that were implemented in response to the COVID-19 pandemic. In July, the Federal Reserve had an in-depth discussion and made preparations for tapering asset purchases, and most members of the FOMC thought that it was appropriate to start reducing asset purchases within this year. According to the dot-matrix plot released after the September FOMC meeting, half of the FOMC members predicted that policy rates would be raised for the first time in 2022. The November FOMC meeting decided to start tapering asset purchases, beginning that month, and the market expected that asset purchases would probably come to an end in mid-2022. According to the performance of the Fed funds futures market, two interest rate hikes are expected in 2022. In September, the European Central Bank announced its plan to slow down the pace of asset purchases under the PEPP starting from Q4, 2021.

This round of Quantitative Easing (QE) programs adopted by the developed economies exceeded the previous round, with a faster pace and greater intensity. After the adjustments, both the US dollar index and the US bond yields were pushed upward, which will probably have an impact on the emerging economies. The first round of QE programs adopted by the Federal Reserve in 2008 had lasted for six years, when the scale of the Fed's balance sheet ballooned from less than USD1 trillion to USD4.5 trillion in 2014. In March 2020, in response to the global outbreak of the COVID-19 pandemic, the Federal Reserve launched another round of QE, with its balance sheet surging over USD4 trillion within one year, from the pre-pandemic USD4.3 trillion to USD8.6 trillion at end-October 2021. If the quantitative easing ends in mid-2022, as expected by the market, this round of QE will have lasted for over two years, notably shorter than the previous round. In 2013, the signal of policy tightening released by the Federal Reserve triggered capital outflows from the emerging economies and large fluctuations in the financial markets. This round of monetary policy adjustments by the Federal Reserve will probably support an appreciation of the US dollar, drive up the yields of US bonds, and attract international capital to flow back to the US. The central banks of the developed economies have attached greater importance to market communications and expectation guidance in this round of QE, hoping to alleviate the spillover effect on the financial markets and other economies. However, as the emerging economies have lower vaccination rates than the developed economies, and hence limited resistance to the pandemic, their economic recovery faces greater impacts and uncertainties. Some emerging economies with poor economic fundamentals will probably be facing greater impacts, mainly reflected in the correlation effect among capital outflows, exchange-rate depreciation, and financial market volatility.

At present, as the internal and external environments facing China are significantly different from those during the last round of global QE programs, the policy adjustments of the developed economies are expected to have a limited impact on China. First, China's macro economy currently is larger in size and more resilient. In recent years, China has continuously promoted the supply-side structural reform and it has witnessed improvements in the quality of its economic development. Since the outbreak of the COVID-19 pandemic in 2020, China has taken the lead in resuming work and production as well as in realizing positive economic growth, achieving a sustained and stable economic recovery, stabilizing the job market, and maintaining good momentum in import and export trade. **Second,** China has adhered to implementing a normal monetary policy. After three months of fighting the battle against the pandemic, significant strategic results were achieved in the aftermath of the outbreak of the pandemic in 2020. In Q4 economic growth will recover to around its potential output and the intensity of monetary policy will gradually return to normal since May 2020. **Third,** progress has been made in China's market-oriented reform of the exchange rate, with enhanced resilience to external shocks. In recent years, the reform of the RMB exchange-rate formation mechanism has been continuously promoted and the market has played a decisive role in the formation of the exchange rate. The RMB exchange rate has exhibited two-way fluctuations, both upwards and downwards, and exchange-rate flexibility has been enhanced. The RMB exchange rate has played a role in adjusting the macro economy and as an auto stabilizer for the balance of payments. **Fourth,** China's financial system is more independent and stable, and RMB assets are more attractive. With the launch of a mix of policy measures promoting an opening-up of the financial market, a diversified two-way opening-up of channels in the financial market has been continuously improved. The "Southbound Bond Connect" and the "Cross-border Wealth Management Connect" were launched in succession, facilitating the orderly flow of cross-border funds. Both the domestic and the overseas capital markets have displayed an obvious characteristic of two-way capital flows. In recent years, more overseas institutional investors, such as the central banks, have taken an initiative to invest in Chinese government bonds and policy financial bonds, contributing to an increasingly optimized foreign debt structure.

China's monetary policy, with its improved cross-cyclical design, can effectively respond to external shocks resulting from policy adjustments in the developed economies. First, the RMB exchange rate is kept basically stable at an adaptive and equilibrium level. In June 2021, the PBC raised the reserve ratio for foreign currency deposits by 2 percentage points and enhanced management of the foreign exchange liquidity of financial institutions. In the meantime, the PBC strengthened expectation management, timely and proactively voiced its policy stance in response to market concerns, and safeguarded the smooth operation of the foreign exchange market. **Second,** the PBC has further improved macro prudential management of full-caliber cross-border financing and has boosted the effectiveness and expanded the coverage of its management. The PBC cut the macro-prudential parameters for the cross-border financing of financial institutions and enterprises from 1.25 to 1 in December 2020 and January 2021, respectively. Through strengthened macro prudential management of cross-border financing, the PBC has helped to alleviate the pressures on enterprises to repay their foreign debt caused by the monetary policy adjustments of the developed economies. **Third,** market liquidity is kept adequate at a reasonable level. The cut in required reserve ratio (RRR) in July has freed up long-term funds of approximately RMB1 trillion, which contributes to optimizing the capital structures of financial institutions and supporting the development of the real economy. **Fourth,** the orderly conversion of the financial market benchmark from the LIBOR was promoted in the domestic market. Financial institutions were guided to prepare themselves in advance for the conversion and to guard against the risks arising from the combined impact of the shift in the financial market benchmark caused by the exit from the LIBOR and the monetary policy adjustments of the developed economies. All of the above-mentioned measures will help insulate against and mitigate risks, enhancing the resilience of China's financial system to respond to external shocks.

Going forward, comprehensive policy measures will be continuously implemented to respond to the monetary policy adjustments of the developed economies in an active and prudent manner. First, taking stability as its top priority, the PBC will focus on the domestic situation, enhance the autonomy of macro policies, and manage the intensity and pace of its policies based on the domestic economic situation and price movements. Second, the PBC will deepen the market-oriented exchange-rate reform, enhance RMB exchange-rate flexibility, strengthen expectation management, intensify macro-prudential management of cross-border financing, and guide enterprises and financial institutions to maintain a "risk neutral" awareness, thereby keeping the RMB exchange rate basically stable at an adaptive and equilibrium level. Third, the PBC will continue to promote the two-way opening-up of the financial market so as to increase the attraction of domestic RMB assets.

3. Issues that merit attention

The COVID-19 pandemic remains an important uncertainty affecting the global economic recovery. The virus variants are still evolving and the possibility of a resurgence of the pandemic persists. Against this backdrop, it is difficult for global economic activities to return to normal within a short period of time, growth momentum is going down, gaps among different industries, enterprises, and income groups are widening, and future development is facing still greater uncertainties. In the *World Economic Outlook* released by the IMF in October, growth of the global economy and the advanced economies were projected to stand at 5.9 percent and 5.2 percent in 2021, respectively, which are 0.1 percentage points and 0.4 percentage points down from the projection in July.

The impact of supply-chain disruptions and energy shortages cannot be ignored. The pandemic has triggered labor shortages in many places across the globe, and recruitment for some particular positions is becoming more difficult. Moreover, goods are stockpiling in a number of major global ports and frictions in the supply chain are increasing notably. Meanwhile, the global green transition is speeding up, while traditional energy producers are facing insufficient capital expenditures and shrinking inventories, which, coupled with the regional climate change and the geopolitical tensions, has pushed up the price of energy that was already at a high level. This is likely to prolong inflation overseas. In addition, supply constraints, energy shortages, and price hikes of raw materials will have broad implications for residents' consumption and enterprises' production and investment, which will probably dampen the outlook for a global economic recovery.

As the macro policies of the developed economies are witnessing diminished marginal intensity, attention should be paid to the accompanying prospects for economic and financial risks. The Federal Reserve announced that it will start tapering asset purchases from November and gradually withdraw from quantitative easing. As the previous fiscal stimulus plans of the US and the other developed economies are coming due, the intensity of their fiscal policies is going to decline. At the same time, stock markets and real estate prices in the major economies are still at historic highs. In August, the S&P Case-Shiller home price index in 20 medium and large-sized US cities rose by 20 percent year on year. In the future, the monetary policy adjustments of the developed economies, if larger than expected, may trigger asset price fluctuations, which may have a spillover effect on the emerging economies through channels such as interest rates, exchange rates, and cross-border capital flows.

II. Macroeconomic developments in China

In the first three quarters of 2021, pandemic containment and economic and social development in all regions and departments across the country were coordinated in a scientific way, with an emphasis on cross-cyclical adjustments of macro policies. China's economy sustained a steady recovery, employment was generally stable, residents' income continued to increase, and the economic structure was upgraded and optimized. According to preliminary statistics, GDP in the first three quarters stood at RMB82.3131 trillion, growing by 9.8 percent year on year on a comparable basis, and the average growth rate of GDP during the past two years was 5.2 percent, a deceleration of 0.1 percentage point from H1. GDP in Q3 grew by 4.9 percent year on year, and the average growth rate of GDP during the past two years was 4.9 percent.

1. Consumption maintained growth, investments rebounded steadily, and imports and exports recorded rapid growth.

The increase in residents' income kept pace with economic growth, and the per capita income gap between urban and rural residents narrowed. In the first three quarters, the country's per capita disposable income reached RMB26265, increasing by 10.4 percent year on year in nominal terms, or 9.7 percent in real terms, with the average growth rate during the past two years at 5.1 percent. The structure of income distribution continuously improved, and the per capita income gap between urban and rural residents narrowed. According to the Urban Depositors' Survey conducted by the PBC in Q3, 24.1 percent of residents were inclined to "consume more," down 1.0 percentage point from Q2 and up 0.6 percentage points year on year, respectively. In the first three quarters, total retail sales of consumer goods grew by 16.4 percent year on year, and the average growth rate during the past two years was 3.9 percent. In particular, growth in September increased by 4.4 percent, an acceleration of 1.9 percentage points from August, and the average growth rate during the past two years was 3.8 percent, an acceleration of 2.3 percentage points month on month.

Investments rebounded steadily and the structure continued to improve. In the first three quarters, total fixed-asset investments throughout China (excluding those by rural households) increased by 7.3 percent year on year, and the average growth rate during the past two years registered at 3.8 percent. In terms of sectors, investments in infrastructure increased by 1.5 percent in the first three quarters, with the average growth rate during the past two years registering at 0.4 percent. Year-on-year growth of investments in the manufacturing sector was 14.8 percent, 7.5 percentage points higher than that of total investments, and the average growth rate was 3.3 percent during the past two years. Investments in real estate development increased by 8.8 percent, and the average growth rate during the past two years registered at 7.2 percent. Investments in the high-tech industry grew by 18.7 percent year on year, and the average growth rate during the past two years registered at 13.8 percent. Investments in health and education grew by 31.4 percent and 10.4 percent year on year, respectively.

Imports and exports grew rapidly. In the first three quarters, imports and exports of goods grew by 22.7 percent year on year. Specifically, exports grew by 22.7 percent year on year and imports grew by 22.6 percent year on year, with the trade surplus in goods posting RMB2.7691 trillion. The trade structure continued to improve, with the share of imports and exports under general trade increasing by 1.4 percentage points year on year. Exports of machinery and electronics increased by 23 percent year on year, 0.3 percentage points higher than the growth of total exports, accounting for 58.8 percent of total exports. Imports from and exports to the countries along the Belt and Road and RCEP (the Regional Comprehensive Economic Partnership) trading partners grew by 23.4 percent and 19.3 percent, respectively. Our trading partners are becoming more diversified.

Foreign direct investments (FDI) continued to gather in the high-tech industries. In the first three quarters, actually utilized FDI increased by 19.6 percent year on year to RMB859.51 billion (equivalent to USD129.26 billion), growing by 25.2 percent year on year (excluding investments in banking, securities, and the insurance industry). In terms of sectors, FDI continued to gather in the high-tech industries. In the first three quarters, actually utilized FDI in the service industry totaled RMB685.32 billion, up 22.5 percent year on year. Actually utilized FDI in the high-tech industry grew by 29.1 percent year on year, among which actually utilized FDI in the high-tech services industry grew by 33.4 percent year on year and actually utilized FDI in the high-tech manufacturing industry grew by 15.2 percent year on year.

2. Agricultural production saw another bumper harvest, industrial production grew steadily, and the service industry recovered continuously

In the first three quarters, the value-added of the primary, secondary, and tertiary industries grew by 7.4 percent, 10.6 percent, and 9.5 percent year on year, respectively. The average growth rates of the primary, secondary, and tertiary industries were 4.8 percent, 5.7 percent, and 4.9 percent, respectively, during the past two years.

Agricultural production was favorable, and China saw rapid growth in animal husbandry. In the first three quarters, the value-added of agriculture (farming) grew by 3.4 percent year on year, and the average growth rate was 3.6 percent during the past two years. The output of summer grains increased by 2.2 percent year on year. The output of pork, beef, lamb, and poultry grew by 22.4 percent year on year. Release of the production capacity of hogs accelerated, and at end-Q3 hogs in stock increased by 18.2 percent year on year.

Industrial production continued to grow, and the industrial structure was continuously optimized. In the first three quarters, the value-added of Industrial Enterprises Above a Designated Size (IEDS) increased by 11.8 percent year on year and the average growth rate during the last two years registered 6.4 percent. Specifically, the value-added of the mining sector increased by 4.7 percent year on year. The manufacturing sector increased by 12.5 percent year on year. The electricity, heat, gas and water production, and supply sectors increased by 12.0 percent year on year. The industrial structure was continuously optimized. The value-added of the high-tech manufacturing sector increased by 20.1 percent year on year, with the average growth rate posting 12.8 percent during the past two years. New energy cars, industrial robots, and integrated circuits grew by 172.5 percent, 57.8 percent, 43.1 percent year on year, respectively.

Growth in the services industry recovered steadily, and market expectations improved. In the first three quarters, the tertiary industry continued to grow. Specifically, the value-added of Electronic Information Transmission/Software/Information Technology Services, and Transportation/Storage/Post Services grew by 19.3 percent and 15.3 percent year on year, respectively. In September, the Index of Service Production (ISP) increased by 5.2 percent year on year, and the average growth rate registered 5.3 percent during the past two years. The Business Activities Expectation Index for the service industry reached 58.9 percent, 1.6 percentage points higher than that in August.

3. Consumer prices increased moderately, and producer prices rose greatly

Consumer prices increased moderately. In the first three quarters, the CPI increased by 0.6 percent year on year, an acceleration of 0.1 percentage points from H1. The core CPI (food and energy excluded) increased by 0.7 percent year on year, and the CPI in July, August, and September increased by 1.0 percent, 0.8 percent, and 0.7 percent year on year, respectively. As the supply of hogs continued to increase, pork prices declined and food prices dropped by 1.6 percent year on year in the first three quarters. The growth of non-food prices rebounded, increasing by 1.1 percent year on year in the first three quarters. The average month-on-month growth rate of the CPI from July to September was 0.1 percent, a deceleration of 0.3 percentage points from the same period of 2020. The average month-on-month growth rate of the core CPI (food and energy excluded) was 0.2 percent, an acceleration of 0.1 percentage points from the same period of 2020. The average month-on-month growth rate of food, tobacco, and alcohol was zero, a deceleration of 1.1 percentage points from the same period of 2020. Specifically, pork prices in September declined by 5.1 percent month on month. The average month-on-month growth rate of accommodations was 0.2 percent, an acceleration of 0.2 percentage points from the same period of 2020; specifically, the prices of water, electricity, and gas in September increased by 0.9 percent month on month. The average month-on-month growth rate of transportation and communications was 0.2 percent, on par with that in the same period of 2020; specifically, the price of transportation in September grew by 0.5 percent month on month.

Producer prices rose greatly. In the first three quarters, the Producer Price Index (PPI) increased by 6.7 percent year on year, an acceleration of 1.6 percentage points from H1. The growth rate of the PPI in July, August, and September registered 9.0 percent, 9.5 percent, and 10.7 percent, respectively. The Purchasing Price Index for Industrial Products (PPIRM) increased by 9.3 percent year on year, accelerating by 2.2 percentage points from H1. In the first three quarters, the Corporate Goods Price Index (CGPI) monitored by the PBC increased by 6.4 percent year on year, accelerating by 0.7 percentage points from H1.

4. Fiscal revenue experienced rapid growth

In the first three quarters, revenue in the national general public budget increased by

16.3 percent year on year to RMB16.40197 trillion, an acceleration of 22.7 percentage points from the same period of 2020. Specifically, central and local fiscal revenue grew by 17.1 percent and 15.6 percent year on year, respectively. Tax revenue amounted to RMB14.07022 trillion, up 18.4 percent year on year. Specifically, the domestic value-added tax, domestic consumption tax, business income tax, and personal income tax increased by 17.4 percent, 12.3 percent, 18.8 percent, and 21.6 percent year on year, respectively. Non-tax revenue reached RMB2.33175 trillion, up 5.4 percent year on year.

In the first three quarters, expenditures in the national general budget saw an increase of 2.3 percent year on year to RMB17.92927 trillion, an acceleration of 4.3 percentage points from the same period of 2020. Specifically, expenditures for medical treatment, health care, and social security grew steadily and expenditures for health care increased by 2.3 percent year on year.

5. The employment situation remained generally stable

The employment situation remained generally stable, and the surveyed urban unemployment rate was stable with a slight decline. In the first three quarters, 10.45 million people were newly employed, accounting for 95.0 percent of the annual employment goal. In September, the surveyed urban unemployment rate was 4.9 percent, down 0.2 percentage points from August and down 0.5 percentage point year on year. The surveyed urban unemployment rate in 31 major cities was 5.0 percent, down 0.3 percentage points from August. The average weekly working hours of employees in enterprises was 47.8 hours, increasing by 0.3 hours month on month.

6. The balance of payments and the external debt

A basic equilibrium was maintained in the balance of payments. According to preliminary statistics, in the first three quarters China's current account surplus registered USD202.8 billion. Specifically, trade in goods recorded a surplus of USD379.6 billion, whereas trade in services recorded a deficit of USD82.1 billion. The capital and financial account deficit was USD136.2 billion. Specifically, direct investments recorded a surplus of USD163.6 billion. By the end of September 2021, foreign exchange reserves posted USD3.2006 trillion, down USD13.4 billion from end-June. The decrease in the book value of reserves was mainly due to factors including the exchange rate and fluctuations in asset prices. By the end of June, the balance in the all-system foreign debt (denominated in both domestic and foreign currencies) posted USD2.6798 trillion. In particular, the short-term external debt balance was USD1.5079 trillion, accounting for 56 percent of the total external debt balance.

Box 4 Understanding the sources and utilization of the funds reflected in the BOP in a comprehensive and precise manner

The balance of payments (BOP) refers to all economic transactions between residents and non-residents. It is a comprehensive record of all transactions, including trade in goods and services, primary income, secondary income, direct investments, portfolio investments, other investments, and reserve assets, etc. It is also an overall reflection of the sources and the utilization of the relevant funds. To analyze China's external economic situation, it is rather important to have a comprehensive picture of the changes in the transaction items rather than only focusing on imports and exports and investments in equity and debt securities.

In terms of the sources of funds, China's current account surplus and net inflows of foreign investment built a foundation for China's external assets and outward investments. In the first half of 2021, the current account surplus and the net inflows of foreign investments amounted to USD565.6 billion, of which the current account recorded a surplus of USD122.7 billion, accounting for 22 percent, and foreign investments witnessed net inflows of USD442.8 billion, accounting for 78 percent. Under the current account, the BOP in the first half registered a surplus of USD238.2 billion under trade in goods, mainly arising from the relatively fast growth of exports and reflecting the resilience of China's external trade amid the impact of the COVID-19 pandemic; a deficit of USD50.5 billion under trade in services, representing a significant narrowing of the deficit in travel caused by the restrained cross-border flows of people; and a deficit of USD71.6 billion under investment income, indicating that China's industrial production continued its recovery and profits maintained a good momentum of growth, therefore laying a foundation for the growing gains in foreign investment. Among the net inflows of foreign investment, direct investments totaled USD177.0 billion, reflecting the sustained attraction of China's growth prospects for overseas medium and long-term capital; portfolio investments reached USD118.4 billion due to the increased holding of domestic portfolios by overseas investors; loans and deposits and other investments recorded USD151.5 billion, mainly due to the deposits of overseas banks and enterprises in domestic banks.

In terms of the utilization of funds, external assets of the private sector grew markedly, and official reserve assets recorded a modest increase. In the first half of 2021, the net outflow of China's foreign investments were USD499.0 billion, of which, the net outflow of private sector investments were USD414.0 billion, accounting for 83 percent, while the official reserve asset transactions increased USD85.0 billion, accounting for 17 percent. The change in reserve transactions differed from that in outstanding reserves as the latter could also be affected by non-transaction factors, such as the exchange rate and asset prices. Among the outward investments of the private sector, direct investments were USD55.7 billion, indicating that the outward direct investments of enterprises remained rational and were increasing in a stable manner; portfolio investments reached USD98.6 billion, of which USD60.0 billion was overseas investments, especially in the HK SAR market, by domestic residents through channels including the HK Stock Connect and the Mutual Recognition of Funds, indicating release of demand for a diversified portfolio; while external loans and deposits and other investments recorded USD265.3 billion. This was mainly due to the increase in the use of deposits and loans abroad by domestic entities because of liquidity management needs and the increase in overseas receivables of domestic institutions.

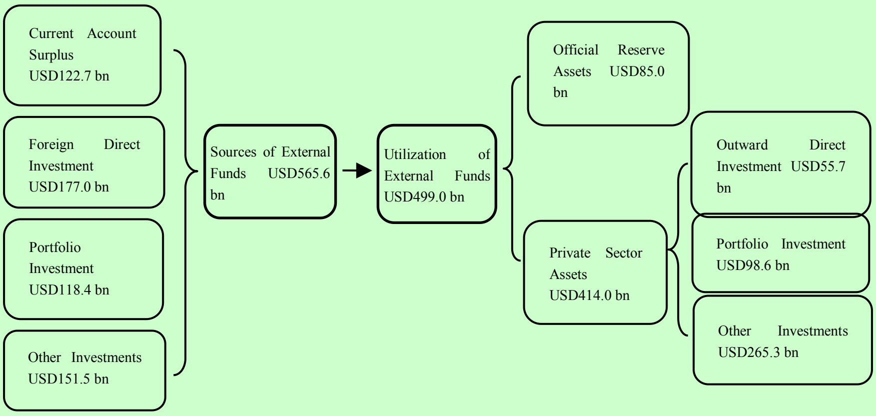


Figure: Sources and Utilization of Funds Reflected in the BOP (as of the first half of 2021)

Note: The difference between sources and utilization of funds is net errors and omissions. The BOP is based on double entry accounting, and each transaction item may not reach a balance due to the sources and the time of the statistics, thus resulting in statistics residuals, namely errors and omissions. In the first half of 2021, net errors and omissions totaled USD-66.6 billion, representing a ratio of -2.5 percent to the aggregate of imports and exports of goods, which was a relatively low level in recent years and within international recognition of a reasonable range.

In general, China’s BOP has taken on new characteristics in recent years, and an analysis calls for a fresh perspective and logic. First, the autonomous equilibrium pattern is becoming more solid, replacing the previous one characterized by high BOP surplus and fast reserves growth. Preliminary data show that, in the first three quarters of 2021, despite an increase in China’s current account surplus, the surplus was 1.6 percent of GDP and it remained within a reasonable and equilibrium range; cross-border investments in both directions remained buoyant under the capital account, reflecting a general equilibrium in capital inflows and outflows; outstanding foreign exchange reserves remained basically stable under the combined influence of the exchange rate, asset prices, returns on investment, etc. An autonomous BOP equilibrium fully indicated that the exchange rate was playing an effective role in regulating the macro-economy and serving as an automatic stabilizer for the BOP.

Second, the holding entities of external assets diversified steadily, and the reserve assets no longer accounted for about half of the total. In recent years, the ratio of reserve assets in China's external assets saw a reasonable decrease, falling to lower than 50 percent since 2016, and it was 37 percent at end-June 2021. The proportion of external assets held by the private sector to banks and enterprises increased accordingly, and they become the main entities utilizing external assets. At end-June, assets in the form of direct investments, portfolio investments, and other investments accounted for 27 percent, 11 percent, and 24 percent of China's external assets, respectively, which was conducive to optimizing the structure of external investments and returns as well as to upgrading the matching of the external assets and liabilities of the private sector.

In the future, China will accelerate construction of a new development paradigm, with domestic circulation as the mainstay and domestic and international circulation reinforcing each other, promote the coordinated development of both domestic and external demand, exports and imports, and foreign and outbound investments, and foster a basic equilibrium of the BOP. The sources and utilization of BOP related funds will continuously realize an autonomous equilibrium, and the structure of external assets and liabilities will be further optimized.

7. Analysis by sector

7.1 The real estate sector

In Q3 2021, the real estate market in China remained generally stable. In September, among 70 medium and large-sized cities nationwide, newly built residential housing prices increased by 3.3 percent year on year, decelerating by 1 percentage point from that at end-June, and second-hand residential housing prices increased by 2.4 percent year on year, decelerating by 1.1 percentage points from that at end-June. In the first three quarters, total floor area of sold units increased by 11.3 percent year on year, registering average growth of 4.6 percent during the past two years. Housing sales increased by 16.6 percent year on year, registering average growth of 10 percent during the past two years. Investments in real estate development grew by 8.8 percent year on year, registering average growth of 7.2 percent during the past two years and decelerating by 1 percentage point from that in H1. Specifically, investments in residential housing development rose by 10.9 percent year on year, accounting for 75.4 percent of total investments in real estate development.

Table 14 Floor Area of Real Estate Projects that Were Newly Started, Under Construction, and Completed in the First Three Quarters of 2021

	Floor area (100 million square meters)	YOY growth (%)	YOY acceleration (percentage points)
Floor area of newly started real estate projects	15.3	-4.5	-8.3
Floor area of real estate projects under construction	92.8	7.9	-2.3
Floor area of completed real estate projects	5.1	23.4	-2.3

Source: China National Bureau of Statistics.

On the whole, growth of real estate loans remained stable. At end-September, outstanding real estate loans by major financial institutions (including foreign-funded financial institutions) grew by 7.6 percent year on year to RMB51.4 trillion, a deceleration of 1.9 percentage points from that at end-June. Specifically, outstanding individual housing loans grew by 11.3 percent year on year to RMB37.4 trillion, a deceleration of 1.7 percentage points from that at end-June. Outstanding housing development loans grew by 0.1 percent year on year to RMB9.3 trillion, a deceleration of 3.3 percentage points from that at end-June.

7.2 Transformation and development of the iron and steel industry toward achieving a carbon emissions peak before 2030 and carbon neutrality before 2060 （“30•60” goal）

The iron and steel industry emits around 15 percent[1] of China’s gross carbon emissions. As the largest carbon-emitting industry in the manufacturing sector, it plays an important role in promoting China’s low carbon transformation toward achieving the “30·60” goal. During the 13th Five-Year Plan period from 2016 to 2020, the iron and steel industry made great efforts to promote supply-side structural reforms, continuously reducing excess capacity and encouraging innovation and green development. Since the beginning of 2021, driven by the sustained economic recovery and strong market demand, the operating income and profits of the iron and steel industry have been growing significantly. According to statistics of the China Iron and Steel Association, the operating income of large and medium-sized iron and steel enterprises from January to September increased by 42.5 percent year on year, and

[1] Source: China Iron and Steel Association.

their profits during the same period increased by 1.23 times year on year. Meanwhile, the iron and steel industry has steadily advanced the low-carbon transformation. By the end of July, a total of 237 iron and steel enterprises nationwide, with around 650 million tons of crude steel production capacity, had completed or were undergoing an ultra-low emission transformation, accounting for about 61 percent of China's crude steel production capacity. From January to September, sulfur dioxide, soot, and dust emissions of large and medium-sized iron and steel enterprises fell by 18.7 percent, 19.2 percent, and 7.5 percent year on year, respectively.

During the 14th Five-Year Plan period from 2021 to 2025, the iron and steel industry will still face many challenges. First, the prices of raw materials and fuel continue to be high. The sharp rise since 2020 in the prices of steelmaking materials, such as coking coal, coke, and scrap steel, have pushed up enterprises' production costs, posing challenges to the security of the supply chain for the iron and steel industry. Second, pressure to release production capacity has risen. Under the policy stimulus to maintain steady growth and investment, enthusiasm for investing in iron and steel is high throughout the country. Some provinces and cities have further expanded their iron and steel production capacity by means of relocating urban steel plants and by capacity replacement, leading to a risk of overcapacity. In addition, the costs of the low-carbon transformation are high. The iron and steel industry will soon be included in the national carbon emissions trading market in which carbon emissions will be limited by quotas, putting forward higher requirements for the low-carbon transformation of enterprises. An ultra-low emission transformation requires large investments in the raw material structure, manufacturing techniques, technology and equipment, green products, and connections between the upstream and downstream industries, presenting challenges to the production and operation of iron and steel enterprises.

In the next step, China should accelerate the transformation, upgrading, and high-quality development of the iron and steel industry. First, China is heavily dependent on iron ore imports. It is necessary to establish a diversified, multi-channel, multi-method, stable, and reliable resource guarantee system to enhance the level of the iron and steel industry chain and its anti-risk capacity. Second, China should steadily promote a layout optimization and structural adjustment in the iron and steel industry to ensure the phase-out of the reduced capacity, and at the same time strengthen guidance of expectations to avoid drastic fluctuations in the market. Third, China should give full play to the role of the capital market in technological transformation, energy conservation and environmental protection, intelligent manufacturing, mergers and acquisitions of iron and steel enterprises, and increase direct financing support to promote the green transformation and low-carbon development of iron and steel enterprises.

Part 5. Monetary Policy Outlook

I. Outlook for the Chinese economy

The Chinese economy is highly resilient and enormous in size, and the fundamentals for long-term steady growth remain unchanged. The economy is strongly characterized by a large growth potential and policy space, and the market entities exhibit ample vitality. This year, the government properly and with coordination promoted pandemic containment and economic and social development. The economy maintained its sound performance, with the main macro indicators generally falling within a reasonable range. GDP in the first three quarters grew 9.8 percent year on year, averaging 5.2 percent during the past two years.

The Chinese economy in Q3 2021 continued to recover with pronounced growth resilience. GDP grew 4.9 percent year on year, averaging 4.9 percent during the past two years. The third quarter witnessed fairly good agricultural production. Meanwhile, industrial production continued to grow, with a rapid improvement in profits. The economic structure was optimized, manufacturing value added and final consumption contributed a higher proportion to economic growth, and energy consumption per unit of GDP decreased. Exports maintained fast growth, and the trade structure continued to improve. Employment was stable overall, and public welfare protection was effective, providing the grounds for achieving the economic and social development goals set for the whole year. The sound monetary policy maintained its continuity, stability, and sustainability to help properly manage market expectations, serve the real economy, and effectively prevent financial risks. The macro leverage ratio remained basically stable. The RMB exchange rate is expected to be stable, and it has been moving in both directions with enhanced flexibility, playing the role of an auto stabilizer for the macro economy and the balance of payments.

However, under the mixed impact of the pandemic and the profound global changes unseen in a century, the external environment is becoming more serious and complex, and the domestic economic recovery is challenged by stage-specific, structural, and cyclical factors. This increases the difficulties in maintaining stable economic performance. It is still uncertain how the global pandemic will unfold as numerous countries have reported variant-infected cases of vaccinated populations. The momentum for a global economic recovery is slowing. The IMF and the OECD both lowered their global growth projections by 0.1 percentage points to 5.9 percent and 5.7 percent, respectively. Inflation is rising in the major developed economies. The US Federal Reserve has begun the tapering process, causing higher fluctuations in global capital flows and exchange rates and increasing price adjustment risks in financial markets. The domestic economy faces challenges such as local COVID-19 breakouts and high commodity price levels. Meanwhile, risks related to the real estate market are currently under control, and the sound overall development of the real estate market remains unchanged. In general, it is necessary to remain confident while being aware of the difficulties. The People's Bank of China (PBC) will focus on fulfilling its responsibilities by properly handling the relationships between reforms and macro management, short-term and long-term considerations, as well as internal and external equilibria to achieve high-quality development.

Inflation pressures are generally controllable. Supply and demand in the consumer market was basically stable in Q3 2021. The continuous drop in pork prices brought down CPI growth to below 1 percent. The CPI in October increased 1.5 percent year on year, and the CPI in Q4 is expected to experience a moderate increase and move within a reasonable range. Meanwhile, due to rising commodity prices, price increases for certain products in high energy-consuming industries, and the low base effect, PPI growth continued to accelerate and is likely to remain high in the short run. Looking forward, there is still uncertainty about the global pandemic. However, the Chinese economy has a strong capacity for self-sufficiency as China is a major global producer. China is in a good position to cope with the rising global commodity prices and the inflation overseas. Overall, domestic supply and demand are basically stable, and the PBC conducts normal monetary policy, which helps price movements to remain stable in the medium and long term.

II. Outlook for monetary policy in the next stage

In the next stage, continuing to follow the guidance of Xi Jinping Thought on Socialism with Chinese Characteristics for a New Era, the PBC will implement the guidelines of the Fifth and Sixth Plenary Sessions of the 19th CPC Central Committee and the Central Economic Work Conference and will put into practice the requirements set forth in the *Report on the Work of the Government*. In line with the decisions and arrangements of the CPC Central Committee and the State Council, it will adhere to the general principle of pursuing progress while ensuring stability, apply the new development philosophy fully, faithfully, and comprehensively, deepen the supply-side structural reform, accelerate the building of a new development paradigm, build a modern central banking system, improve the modern monetary policy framework, and promote high-quality development. The PBC will reinforce its studies and analysis of marginal changes in the economic situations at home and abroad and work to align this year’s and next year’s macro policies in a coordinated way. Always placing higher priority on serving the real economy, this year the PBC will maintain the stability of monetary policy, stabilize market expectations, and strive to fulfil the main targets and tasks for economic development.

The sound monetary policy will be flexible, targeted, reasonable, and appropriate, focusing on domestic conditions and giving top priority to stability. The PBC will properly manage policy pace and intensity, strike a balance between economic development and risk prevention, and effectively carry out cross-cycle policy adjustments in order to keep the economy generally stable and to strengthen the resilience of economic development. It will improve the mechanism for money supply management, keep liquidity adequate at a reasonable level, and make the growth of credit aggregates more stable so that the growth rates of money supply and aggregate financing to the real economy (AFRE) are basically in line with nominal economic growth and the macro leverage ratio will remain basically stable. Closely following and studying price movements, the PBC will stabilize social expectations and make efforts to keep prices generally stable. To bring into play the role of structural monetary policy tools, it will make effective use of the newly added RMB300 billion of central bank lending quotas dedicated to supporting micro and small businesses (MSBs) to help increase loans to them and to self-employed traders; it will implement the decision on extending the expiration dates of the two monetary policy tools providing direct support for the real economy; it will properly use the RMB200 billion of the central bank lending quota to support coordinated development across regions; it will put into operation the carbon emissions reduction facility and introduce targeted central bank lending in the amount of RMB200 billion to support the clean and efficient use of coal; and it will guide financial institutions to intensify support for micro, small and medium-sized enterprises (MSMEs), green development, and other key fields as well as weak links. Moreover, the PBC will enhance the market-oriented interest rate formation and transmission mechanism by further tapping into the loan prime rate (LPR) reform, optimizing regulation over deposit rates, and stabilizing and reducing overall financing costs for MSBs. It will deepen the market-oriented exchange rate reform, enhance the RMB exchange rate flexibility, strengthen expectation management, improve macro-prudential management of cross-border financing, and guide enterprises and financial institutions to always be risk-neutral, thereby keeping the RMB exchange rate basically stable at an adaptive and equilibrium level. The PBC will uphold bottom-line thinking, enhance systemic awareness, and make coordinated efforts to forestall and defuse major financial risks based on market principles and the rule of law.

First, the PBC will maintain reasonable growth in money and credit as well as in

the AFRE. It will reinforce monitoring and analysis of both the internal and the external market environment as well as various uncertainties and will conduct in-depth studies of liquidity supply and demand in the market so as to make cross-cycle liquidity adjustments. A mix of monetary policy tools, such as the Medium-term Lending Facility, open market operations, central bank lending, and central bank discounts, will be used to further improve the foresightedness, flexibility, and effectiveness of monetary policy operations, to keep liquidity adequate at a reasonable level, and to guide market rates to move around policy rates. The PBC will improve the mechanism for money supply management by bringing into shape the long-term mechanisms for liquidity, capital, and interest rate constraints, with which the central bank adjusts the money creation of commercial banks. Moreover, it will make the growth of credit aggregates more stable so that the growth rates of money supply and the AFRE will be basically in line with nominal economic growth. It will improve the mechanism for sustainable capital replenishment by replenishing capital for commercial banks through multiple channels and stepping up support for small and medium-sized banks in their issuance of perpetual bonds and other capital replenishment instruments, thereby improving the capacity of banks to serve the real economy and to forestall and defuse financial risks.

Second, the PBC will move ahead with policy implementation to bring into play the guiding role of structural monetary policy tools. It will keep central bank lending and discount policies stable to carry on inclusive and sustained funding support for agro-related businesses, MSBs, and private enterprises. Meanwhile, continued efforts will be made to implement the decision on extending the expiration dates of the two monetary policy tools providing direct support for the real economy. The PBC will keep up the intensity of financial support for MSBs so that they can play a bigger role in stabilizing businesses and safeguarding employment. Effective steps will be taken to put into operation the carbon emissions reduction facility, which will guide financial institutions to lend at preferential interest rates to key projects that will significantly reduce carbon emissions. It is expected that the exemplary policy effect will encourage social investments in green low-carbon fields and help reach the aims of peaking carbon emissions and achieving carbon neutrality. Furthermore, the PBC will leverage targeted central bank lending to support and improve the clean and efficient use of coal and to safeguard China's energy security.

Third, the PBC will build the systems and mechanisms needed to provide effective financial support for the real economy. It will ramp up efforts to implement the policy supporting the issuance of unsecured inclusive MSB loans and will vigorously promote the pay-as-you-go lending model. It will push for capacity building to improve the financial services for MSMEs so that a long-term mechanism will be formed whereby banks will have the confidence, willingness, ability, and professionalism to provide loans. At the same time, the PBC will implement policy measures on financial support for consolidating the achievements in poverty eradication and for advancing rural revitalization in all respects. It will enhance performance assessments and incentives to step up support for new types of agribusinesses, development of the seed industry and other key fields, as well as key regions, such as counties most in need of assistance for rural revitalization. Moreover, the PBC will support relevant agencies and carry out work on peaking carbon emissions and achieving carbon neutrality in a coordinated and orderly way. In compliance with laws and regulations and provided that risks are controllable, financial institutions will be encouraged to meet the reasonable financing needs of coal-fired power plants to support power supply in extraordinary times. With the introduction of innovative products, such as sustainability-linked bonds and carbon neutrality bonds, the financial sector will play its part in supporting a secure energy supply and promoting a green and low-carbon transition. Firmly adhering to the principle that housing is for living in, not for speculation, and that the real estate market shall not be used to provide a short-term stimulus to the economy, the PBC will remain committed to stabilizing land prices, housing prices, and expectations. It will also maintain the continuity, consistency, and stability of real estate finance policies, implement rules for prudential management of real estate finance, and increase financial support for the rental of housing. The PBC will work with relevant agencies and local governments to maintain the stable and healthy development of the real estate market and protect the legitimate rights and interests of consumers in the market.

Fourth, the PBC will deepen the market-oriented interest rate and exchange rate reforms to smooth the channels of monetary policy transmission. It will enhance the market-oriented interest rate formation and transmission mechanism by improving the central bank policy rate system and guiding market rates to move around the policy rates. The PBC will continue to unleash the potential of the LPR reform and give full play to its role in optimizing resource allocations. It will push financial institutions by market means to allocate more financial resources to MSBs so that competition will rise in the MSB loan market and the comprehensive financing costs for MSBs will stabilize and fall. Meanwhile, the PBC will push for the implementation of measures on optimizing regulation over deposit rates so as to keep bank liability costs basically stable, and it will continue guiding the financial sector to give up part of its profits to benefit the real economy. Taking steady steps to deepen the market-oriented exchange rate reform, the PBC will improve the managed floating exchange rate regime based on market supply and demand with reference to a basket of currencies, enhance the RMB exchange rate flexibility, and bring into play the role of the exchange rate in macroeconomic management and as an automatic stabilizer for the balance of payments. Furthermore, it will strengthen expectations management and keep the RMB exchange rate basically stable at an adaptive and equilibrium level. The PBC will continue to develop the foreign exchange market. Guiding both enterprises and financial institutions to be risk-neutral, it will offer guidance to financial institutions on providing services for the exchange rate risk hedging of the MSMEs with authentic needs based on the risk-neutral concept, on reducing the costs of exchange rate risk hedging of the MSMEs, and on strengthening risk management of their foreign exchange businesses, thereby maintaining the stable and sound development of the foreign exchange market. The PBC will continue to advance RMB internationalization stably and prudently by deepening international monetary cooperation and developing offshore RMB markets. In addition, it will launch a pilot program for the high-quality opening-up of cross-border trade and investment, further facilitating use of the RMB in cross-border trade and investment, and steadily move ahead with the convertibility of the RMB under the capital account.

Fifth, the PBC will always place equal emphasis on preventing risks and promoting development, and it will continue to advance the high-quality development of the bond market. It will take further steps to improve the legal system for the bond market, to tighten requirements for information disclosures, and to strengthen regulation over intermediary institutions. The PBC will work to improve the efficiency and interconnectivity of the multi-tiered market system and cultivate diversified and qualified investors. Efforts will be intensified to support major national strategies as well as key industries and regions and to improve the effectiveness and efficiency of the bond market in serving the real economy. The PBC will take steady steps to promote the higher-quality opening-up of the bond market while acting in a timely way to forestall and defuse bond market risks. Based on market principles and the rule of law, the PBC will see that all concerned parties fulfil their responsibilities. It will continue to put into practice the newly formed mechanisms for bond default resolution, improve the mechanism for unified law enforcement, and crack down on illegal and irregular conduct in the bond market.

Sixth, the PBC will work toward establishing a modern financial enterprise system with Chinese characteristics and will make continued efforts to improve the corporate governance of financial enterprises. Focusing on strengthening corporate governance, it will deepen the reform of large commercial banks and establish a modern financial enterprise system with Chinese characteristics. Large banks will be guided to shift the focus of their services to the primary level, while small and medium-sized banks will be guided to focus on their main duties and businesses. With these efforts, the financial market is expected to become more vigorous and resilient and a modern financial system will be formed, which is highly adaptable, competitive, and inclusive. The reform of development financial institutions and policy financial institutions will continue. They will be required to fulfil their responsibilities while institution-specific measures will be taken to advance the reform of existing businesses step by step and to carry out category-based management of businesses and separate accounting. Work also needs to be done to gradually improve transparency, to strengthen capital constraints as well as risk management, and to enhance incentives. In this way, development financial institutions and policy financial institutions will better play their roles in serving the real economy and supporting national strategies.

Seventh, the PBC will uphold bottom-line thinking, enhance systemic awareness, and make coordinated efforts to forestall and defuse major financial risks based on market principles and the rule of law. It will consolidate the foundation of financial stability while promoting high-quality economic development to defuse financial risks. The PBC will make every effort to defuse existing risks, to contain any possible resurgence of risks, and to guard against financial risks arising from risk resolution in other fields. It will further give play to the role of deposit insurance as a platform for market-oriented resolution and it will explore a number of market-oriented and law-based approaches to support small and medium-sized banks in defusing risks and replenishing capital. The mechanism for financial risk accountability will be improved so that those responsible for the outbreak of major financial risks will be strictly held to account. To that end, measures will be put in place to ensure that both CPC local committees and local governments play their part in preventing financial risks and that all concerned parties fulfil their respective responsibilities. The PBC will smooth the operation of relevant mechanisms and clarify the roles and duties of relevant parties so that they will not only do their part but also work together to effectively prevent moral hazards. More emphasis will be placed on the supervision of systemically important banks. The PBC will push these banks to meet additional regulatory requirements as scheduled, to come up with proposals for a recovery plan and a resolution plan, and to implement prudential regulatory requirements, such as for information reporting. Furthermore, it will issue risk warnings in a timely way. The PBC will properly handle the relationship between stabilizing growth and preventing risks and will firmly defend the bottom line that no systemic risk should occur.