China Monetary Policy Report

Q2 2023

(August 17, 2023)

Monetary Policy Analysis Group of

the People's Bank of China

Executive Summary

Since the beginning of 2023, under the strong leadership of the CPC Central Committee with Comrade Xi Jinping at its core, the Chinese economy continued to recover with an upward trend. In H1, the GDP grew 5.5 percent year on year, laying a good foundation for reaching the socio-economic development goals for the entire year. The CPI rose 0.7 percent year on year, remaining generally stable. Following the guidance of Xi Jinping Thought on Socialism with Chinese Characteristics for a New Era, the People's Bank of China (PBOC) resolutely implemented the decisions and arrangements of the CPC Central Committee and the State Council. Pursuing the principle of seeking progress while taking stability as a top priority, it implemented a sound monetary policy in a targeted and effective manner and contributed to overall improvements in economic performance.

First, money and credit witnessed reasonable growth. The PBOC injected liquidity through multiple channels, including required reserve ratio (RRR) cuts, central bank lending and discounts, the medium-term lending facility (MLF) operations, and open market operations (OMOs), to keep liquidity adequate at a reasonable level. It encouraged financial institutions to consolidate their credit support for the real economy so as to enhance the stability and the sustainability of aggregate credit growth. **Second,** the financing costs for the real economy remained stable with a slight decline. With the policy rate playing a guiding role, the rates for the June and August OMO repo operations and the MLF dropped 20 and 25 basis points (bps), respectively. As the loan prime rate (LPR) reform continuously unleashed its potential, the financing costs for businesses and the borrowing costs for residents remained stable with a downward trend. The mechanism for market-oriented adjustments of deposit rates played an important role, and the mechanism for dynamic adjustments to first-home mortgage rates was still in effect. **Third,** the structural monetary policy toolkit continued to play its role. While making full use of the existing structural policy tools, the PBOC increased the quotas for central bank lending and discounts for rural development and micro and small businesses (MSBs) and prolonged the use of several temporary tools, such as inclusive MSB loan facilities. In addition, the terms were extended for some policies under the 16 financial measures to bolster the real estate market, and the special central bank lending for troubled property developers and the loan support scheme for rental housing were implemented. **Fourth,** the internal and external equilibria were maintained. The PBOC deepened the market-oriented reform of the exchange rate while upholding the decisive role of the market in the RMB exchange rate formation and giving play to the role of the exchange rate as an automatic stabilizer for the macro economy and the balance of payments. **Fifth,** risk prevention and resolution were enhanced. Following market principles and the rule of law for risk resolution, the PBOC established a working framework for bank risk monitoring, early warnings, and hard-constrained early corrections based on different levels and stages so as to firmly defend the bottom line whereby no systemic financial risks will occur.

Overall, the monetary policy this year has remained forward-looking, effective, and sustainable, with its pace and force being properly managed in line with the situation, thus creating a sound monetary and financial environment for the economic recovery. Money and credit witnessed reasonable growth. RMB loans saw a cumulative rise of RMB15.7 trillion in H1, RMB2.0 trillion more than their growth during the same period of the previous year. At end-June, RMB loans, broad money (M2), and outstanding aggregate financing to the real economy (AFRE) recorded year-on-year growth of 11.3 percent, 11.3 percent, and 9.0 percent, respectively. The credit structure continued to improve. At end-June, inclusive MSB loans and medium and long-term (MLT) loans to the manufacturing sector grew by 26.1 percent and 40.3 percent year on year, respectively. Loan rates declined notably. In June, the weighted average rate on new corporate loans and on personal housing loans registered 3.95 percent and 4.11 percent, respectively, down 0.21 percentage points and 0.51 percentage points year on year and representing a historical low. The RMB exchange rate moved in both directions. The exchange rate of the RMB against the U.S. dollar dropped beyond seven in May but then appreciated 1.3 percent in July. The market witnessed rational and orderly foreign exchange sales and purchases, and market expectations remained basically stable.

Currently, China's economy has returned to normal and is steadily functioning on a path of high-quality development. However, it should be noted that the global political and economic situations are complex and grim, the cumulative effects of the rapid rate hikes in the developed economies remain, and momentum for an economic recovery has waned, while domestically the economy is facing multiple challenges, including insufficient demand, hardships suffered by some businesses, and existing and potential risks in some key areas. Still, China's economy is blessed with huge development resilience and potential, as its sound fundamentals for long-term development remain unchanged and advantages and positive factors are on the rise. Therefore, we should maintain a strategic focus and enhance confidence in development. During the next stage, guided by Xi Jinping Thought on Socialism with Chinese Characteristics for a New Era, the PBOC will thoroughly implement the guidelines of the 20th CPC National Congress and the Central Economic Work Conference. Upholding the general principle of pursuing progress while ensuring stability, it will apply the new development philosophy fully, faithfully, and comprehensively, and it will play its part in accelerating the building of a new development paradigm. It will deepen the reform and opening-up, integrate implementation of the strategy to expand domestic demand with efforts to deepen the supply-side structural reform, and strengthen macro-policy adjustments. Also, by developing a modern central banking system and fully exploring the efficacy of monetary and credit policies, the PBOC will continue its efforts to achieve better economic performance, enhanced endogenous forces, and improved social expectations as well as resolution of existing and potential risks so as to help effectively upgrade and appropriately expand economic output.

The PBOC will pursue a sound monetary policy in a targeted and effective manner, and it will give better play to the role of monetary policy instruments in adjusting both the aggregate and the structure so as to provide solid support for recovery and development of the real economy. Using a mix of monetary policy instruments, it will keep liquidity adequate at a reasonable level, and it will ensure that the growth rates of M2 and the AFRE continue to be basically in line with nominal economic growth. It will continue to deepen the market-oriented interest rate reform, optimize the central bank policy rate system, unleash the potential of the LPR reform, and give play to the important role of the mechanism for market-oriented deposit rate adjustments so as to ensure that the financing costs for businesses and the borrowing costs for residents remain stable with a slight decline. The structural monetary policy instruments will be targeted, appropriate, and flexible. Those still in effect will be properly used, and those that support structural problem-intensive areas will be prolonged. Meanwhile, support will be continuously enhanced for MSBs, sci-tech innovation, and green development. Considering the great changes in supply and demand relations, the real estate policies will be adjusted and improved as appropriate to promote steady and sound development of the market. Maintaining the positive role of finance in promoting consumption, stabilizing investment, and expanding domestic demand, the PBOC will work to keep prices basically stable. Pursuing a managed floating exchange rate regime based on market supply and demand with reference to a basket of currencies, it will stabilize expectations with a mix of policies to keep the RMB exchange rate basically stable at an adaptive and equilibrium level and to firmly guard against risks arising from exchange rate overshooting. The PBOC will prevent and resolve financial risks in key areas, coordinate efforts to resolve local debt risks with financial support, and steadily promote risk alleviation for small and medium-sized financial institutions through reforms, thereby firmly defending the bottom line whereby no systemic financial risks will occur.

Contents

Boxes

Tables

Figures

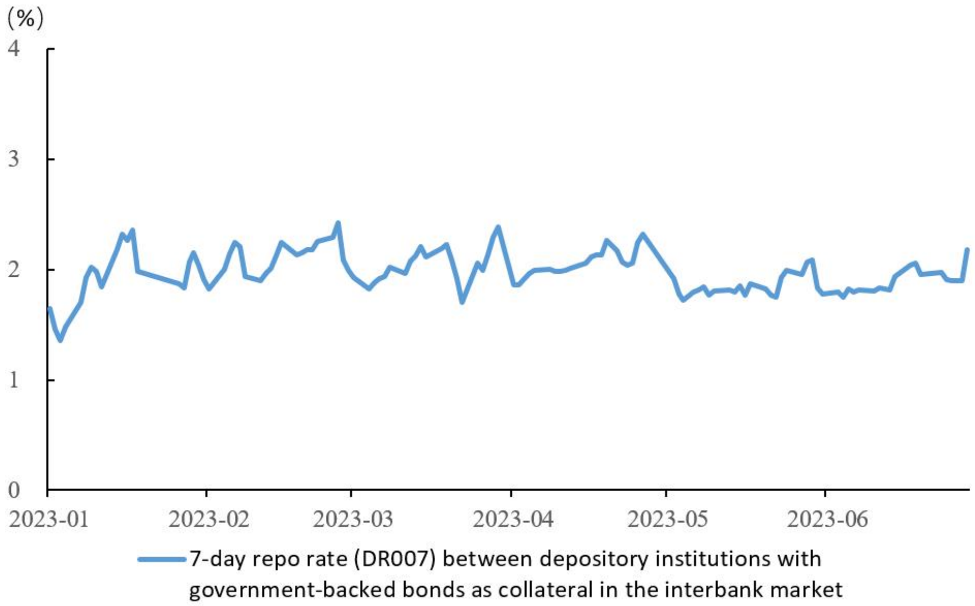
Part 1 Money and Credit Analysis

Since the beginning of 2023, the People's Bank of China has followed the guidance of Xi Jinping Thought on Socialism with Chinese Characteristics for a New Era and has fully implemented the guiding principles of the 20th National Congress of the Communist Party of China (CPC) as well as the Central Economic Work Conference and the requirements set forth in the *Report on the Work of the Government*. Taking stability as its top priority and pursuing progress while ensuring stability, it has implemented a sound monetary policy in a targeted and effective manner, increased the intensity of counter-cyclical adjustments, and scientifically managed market expectations to effectively serve the real economy. As a result, money, credit, and the AFRE are witnessing reasonable growth, overall financing costs are declining steadily, the credit structure is improving continuously, and the RMB exchange rate is remaining basically stable at a reasonable and equilibrium level, thereby strongly supporting the overall economic recovery and improvement.

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

In the first half of 2023, the PBOC employed a mix of instruments, such as the required reserve ratio (RRR) cut, central bank lending and discounts, the medium-term lending facility (MLF), and open market operations (OMOs), to inject liquidity into the economy in a targeted and effective manner and to keep liquidity adequate at a reasonable level in the banking system, thereby creating a favorable liquidity environment to promote financial support for the high-quality development of the real economy. In March, the PBOC cut the RRR by 0.25 percentage points across the board to release long-term liquidity and strengthen support for the real economy. In June and August, interest rates on open market reverse repo operations and the MLF rate decreased in succession, significantly boosting market confidence. Since the beginning of 2023, the money market interest rate has been steadily moving around the central bank's open market reverse repo operation rate, and the market interest rate at the end of H1 has also been relatively stable. At end-June, the excess reserve ratio for financial institutions registered 1.6 percent, up 0.1 percentage points year on year.

Figure 1 Movement of Money Market Interest Rates



Source: www.chinamoney.com.cn.

II. Lending by financial institutions grew rapidly, and lending rates remained at historic lows

Credit aggregates grew rapidly. In the first half of 2023, credit aggregates grew at a more stable pace and maintained year-on-year (YOY) growth on a high base, better meeting the effective loan demand of the real economy. At end-June, outstanding loans issued by financial institutions in domestic and foreign currencies grew 10.6 percent year on year to RMB235.7 trillion, increasing RMB15.7 trillion from the beginning of 2023 or a YOY acceleration of RMB1.8 trillion. Outstanding RMB loans grew 11.3 percent year on year to RMB230.6 trillion, up RMB15.7 trillion from the beginning of 2023 or a YOY acceleration of RMB2.0 trillion.

The credit structure has been improving. At end-June, medium and long-term (MLT) loans to enterprises and public entities grew by RMB9.7 trillion from the beginning of 2023, accounting for 75.8 percent of total corporate loans. The YOY growth rate of MLT loans to the manufacturing sector registered 40.3 percent, 29.0 percentage points higher than the YOY growth of total loans, which maintained their rapid growth since 2020. The YOY growth rate of MLT loans to the infrastructure sector was 15.8 percent, 4.5 percentage points higher than the YOY growth of total loans. The YOY growth rate of loans to "specialized, sophisticated, distinctive, and innovative" SMEs was 20.4 percent, 9.1 percentage points higher than the YOY growth of total loans. Outstanding inclusive loans to MSBs grew 26.1 percent year on year, 14.8 percentage points higher than the YOY growth of total loans. A total of 59.35 million MSBs were supported, a rise of 13.3 percent year on year.

Table 1 The Structure of RMB Loans in H1 2023

Unit: RMB100 million

	Outstanding amount at end-June	YOY growth (%)	Increase from the beginning of the year	YOY acceleration
RMB loans to:	2305767	11.3%	157324	20180
Households	785611	6.1%	27951	5723
Enterprises and public entities	1503308	14.0%	128150	14193
Non-banking financial institutions	5805	32.6%	-15	-120
Overseas	11043	37.8%	1239	383

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 from Financial Institutions in H1 2023

Unit: RMB100 million

	Increase from the beginning of the year	YOY acceleration
Chinese-funded large-sized banks [1]	85814	12215
Chinese-funded small and medium-sized banks [2]	71757	5513
Small-sized rural financial institutions [3]	20248	1864
Foreign-funded financial institutions	-166	-61

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 rate of loans remained at a historic low. The PBOC continuously deepened the market-oriented reform of interest rates, effectively tapping into the loan prime rate (LPR) reform and bringing into play the key role of the market-based adjustment mechanism for deposit interest rates so as to promote a steady decline in actual lending rates. In June, the one-year LPR and the over-five-year LPR stood at 3.55 percent and 4.20 percent, respectively, both of which were 0.1 percentage points lower compared with December 2022. In June, the weighted average interest rate on new loans recorded 4.19 percent, down 0.22 percentage points year on year. In particular, the weighted average interest rate on ordinary loans registered 4.48 percent, down 0.28 percentage points year on year, and the weighted average interest rate on corporate loans was 3.95 percent, down 0.21 percentage points year on year, both of which remained at historic lows. In June, the share of ordinary loans with rates above, at, and below the LPR registered 56.67 percent, 5.59 percent, and 37.74 percent, respectively.

Table 3 Weighted Average Interest Rates on New Loans Issued in June 2023

Unit: %

	June	Change from last December	YOY Change
Weighted average interest rate on new loans	4.19	0.05	-0.22
on ordinary loans	4.48	-0.09	-0.28
of which: on corporate loans	3.95	-0.02	-0.21
on bill financing	2.03	0.43	0.17
on mortgage loans	4.11	-0.15	-0.51

Source: The People's Bank of China.

Table 4 Shares of RMB Lending Rates at Different Levels from January to June 2023

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	37.38	6.28	56.34	16.65	19.06	10.22	5.70	4.72
February	37.60	6.02	56.38	16.32	16.84	10.28	6.54	6.40
March	36.96	6.88	56.16	17.10	17.57	10.57	6.18	4.74
April	36.62	6.20	57.18	15.54	17.18	11.14	7.08	6.24
May	36.28	5.52	58.20	13.98	16.79	11.71	7.98	7.74
June	37.74	5.59	56.67	17.79	17.31	10.81	6.09	4.68

Source: The People's Bank of China.

Interest rates on foreign-currency deposits and loans edged up. In June, the weighted average interest rates on demand large-value USD-denominated deposits and on large-value USD-denominated deposits with maturities within three months registered 1.65 percent and 4.46 percent, respectively, up 0.01 and 0.23 percentage points from March 2023, respectively. The weighted average interest rates on USD-denominated loans with maturities within three months and with maturities between three months (including three months) and six months registered 5.68 percent and 5.63 percent, up 0.43 and 0.30 percentage points from March 2023, respectively.

Table 5 Average Interest Rates on Large-value USD-denominated Deposits and

Loans from January to June 2023

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	1.25	3.99	4.62	5.34	5.46	4.96	4.91	5.12	5.10	5.53	5.99
February	1.42	4.18	5.10	5.51	5.50	5.44	5.08	5.23	5.39	5.46	5.58
March	1.64	4.23	5.02	5.53	5.67	5.54	5.25	5.33	5.11	5.34	5.86
April	1.76	4.50	5.29	5.49	4.91	5.72	5.39	5.47	5.49	5.64	5.62
May	1.78	4.63	4.65	5.68	5.63	5.64	5.55	5.46	5.52	5.39	5.98
June	1.65	4.46	5.29	5.63	5.47	5.75	5.68	5.63	5.46	5.41	5.71

Source: The People's Bank of China.

Box 1 A Proper Assessment of the Profits of China's Commercial Banks

In recent years, the profits of China's commercial banks have maintained growth. However, their net interest margins (NIMs) have continued to narrow, leading to a deceleration in profit growth. Commercial banks face capital constraints in issuing loans to the real economy and require a capital buffer against risks. Their capital adequacy ratios are subject to an explicit national regulatory standard. To maintain sound operations and to prevent risks, commercial banks should keep profits and NIMs at a proper level, which will be favorable for them to provide more sustainable support for the real economy.

Although the asset scale and total profits of China's commercial banks are growing gradually, their NIMs and returns on assets (ROA) are sinking. At end-Q1 2023, the total assets of China's commercial banks registered RMB337 trillion, growing at an average annual rate of 10.4 percent during the past five years. As the market-based reform of interest rates advances, competition in the credit market will escalate, leading to a decline in loan rates and the edging down of bank profitability. This was especially noteworthy after the outbreak of the COVID-19. In Q1 2023, net profits of commercial banks posted RMB667.9 billion, up 1.3 percent year on year, 6.1 percentage points lower than the YOY growth in Q1 2022. The NIM and ROA posted 1.74 percent and 0.81 percent, respectively, down 0.23 and 0.08 percentage points year on year, respectively. As the profitability of unit assets deteriorates, the growth of profits are mainly attributable to an expansion in the scale of assets. To put it in another way, a reduction in prices is made up for by an increase in the amount. Throughout the world, the NIMs of the banking sectors in the U.S., Japan, Germany, and other major advanced economies have generally decreased since 2010. In 2022, the NIM in the U.S. banking sector temporarily rebounded, mainly due to the aggressive interest rate hike by the U.S. Federal Reserve (Fed). According to statistics released by the Federal Deposit Insurance Corporation (FDIC), in Q1 2023 the NIM of commercial banks in the U.S. was 3.31 percent, almost twice that in China and up 0.77 percentage points year on year.

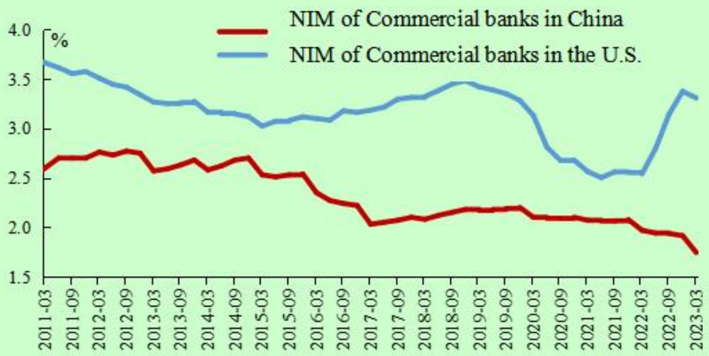


Figure: NIMs of Commercial Banks in China and the U.S.

The net profits of China's commercial banks are mainly used to replenish common equity tier 1 capital and to distribute dividends to shareholders, which will exert an influence on the real economy through the leverage of capital. In contrast with overseas counterparts, capital replenishments of domestic banks suffer from limited channels, multiple barriers, and slow progress, leading to a huge capital gap among them. For instance, the average P/B for A-share listed banks is 0.58, restricting their ability to replenish common equity tier 1 capital by issuing common equities or other external channels. Therefore, while expanding external channels, it is particularly important to retain the ability to replenish capital through internal channels. Maintaining an appropriate profit growth rate is an important internal channel for capital replenishment that can enhance the ability of banks to provide support for the real economy and prevent risks, thus boosting the confidence of domestic and overseas investors in China's macro economy. From 2018 to 2022, about two-thirds of the cumulative net profits of six major state-owned commercial banks was reserved to replenish their own common equity tier 1 capital, ensuring that their capital adequacy ratios would satisfy the international regulatory requirements. The profits used for capital replenishment influenced the real economy through credit issuance and other channels. The remainder were mainly used to distribute dividends to shareholders.

Currently, the Chinese economy faces various difficulties and challenges. Against this backdrop, we need to give further play to the role of banks in serving the real economy and to level the virtuous circulation between the financial sector and the economy. As the financial cycle is seldom in parallel with the economic cycle and exposure of the credit risks of banks takes time, we should prepare in terms of both financial resources and risk buffers. We should allow banks to maintain their sound operations through reasonable means, which, in the meanwhile, will enhance their capability to provide sustainable support for the development of the real economy. It is common for the profitability of commercial banks to fluctuate with the economic cycle. We should make a reasonable assessment of this and refrain from making any over-interpretations.

Deposits grew significantly. At end-June, outstanding deposits in domestic and foreign currencies at all financial institutions had increased 10.5 percent year on year to RMB284.7 trillion, up RMB20.2 trillion from the beginning of 2023 and an acceleration of RMB1.1 trillion year on year. Outstanding RMB deposits grew 11.0 percent year on year to RMB278.6 trillion, an increase of RMB20.1 trillion from the beginning of 2023 and an acceleration of RMB1.3 trillion year on year. Outstanding deposits in foreign currencies stood at USD837.4 billion, down USD16.6 billion from the beginning of 2023 and a deceleration of USD6.3 billion year on year.

Table 6 The Structure of RMB Deposits in H1 2023

Unit: RMB100 million

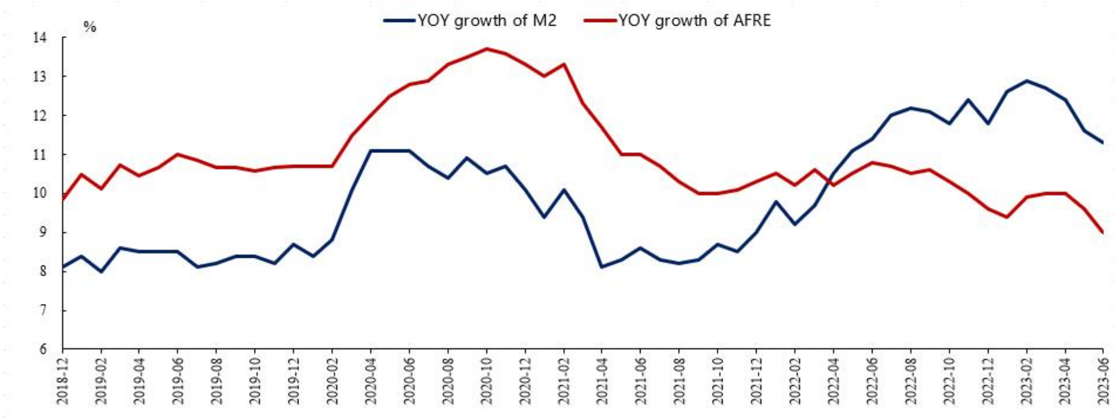
	Outstanding deposits at end-June	YOY growth (%)	Increase from the beginning of the year	YOY acceleration
RMB deposits:	2786205	11.0%	200997	12966
Households	1322387	17.2%	119147	15882
Non-financial enterprises	795170	6.2%	49649	-3218
Public entities	351238	7.0%	20813	3828
Fiscal entities	49888	-10.4%	-125	-5186
Non-banking financial institutions	249698	6.8%	10840	1328
Overseas	17823	13.7%	673	332

Source: The People’s Bank of China.

III. Money supply and the AFRE grew at a rapid pace

The monetary aggregate grew at a rapid pace. At end-June, outstanding broad money M2 registered RMB287.3 trillion, up 11.3 percent year on year; narrow money M1 and currency in circulation M0 registered RMB69.6 trillion and RMB10.5 trillion, respectively, up 3.1 percent and 9.8 percent year on year, respectively. The first half of 2023 witnessed a net cash injection of RMB78.9 billion, a decrease of RMB440.5 billion year on year.

Figure 2 The YOY Growth of Outstanding Broad Money (M2) and the AFRE



Source: The People's Bank of China.

According to preliminary statistics, the outstanding AFRE reached RMB365.5 trillion at end-June and its YOY growth registered 9.0 percent. In the first half of 2023, the AFRE increment totaled RMB21.5 trillion, RMB475.4 billion more than that in the first half of 2022. The AFRE was characterized by the following structural features: first, RMB loans witnessed rapid growth. In the first half of 2023, the increment in RMB loans issued by financial institutions to the real economy grew by RMB2.0 trillion year on year to RMB15.6 trillion, accounting for 72.4 percent of the AFRE increment during the same period. Second, in the first half of 2023, new government bonds decreased year on year, and the increment in net financing of government bonds was RMB1.27 trillion less than that in the previous year; the increment in direct corporate financing decreased significantly year on year, with the increment in corporate bonds and domestic equity financing by non-financial enterprises decreasing by RMB788.3 billion and RMB43.2 billion year on year, respectively. Third, there was a recovery in off-balance-sheet financing. In the first half of 2023, new entrusted loans, trust loans, and undiscounted bankers' acceptances grew by RMB79.7 billion, RMB398 billion, and RMB261.9 billion year on year, respectively. Fourth, asset-backed securities of depository institutions decreased by a larger margin year on year, while loans written off increased at a slower pace year on year.

Table 7 Aggregate Financing to the Real Economy in H1 2023

	End-June 2023		H1 2023	
	Stock (RMB trillion)	YOY growth (%)	Flow (RMB100 million)	YOY change (RMB100 million)
The AFRE	365.45	9.0	215488	4754
Of which: RMB loans	228.86	11.2	156047	19909
Foreign-currency loans	1.89	-18.9	-242	-700

	End-June 2023		H1 2023	
(RMB equivalent)				
Entrusted loans	11.32	4.1	743	797
Trust loans	3.77	-5.1	228	3980
Undiscounted bankers' acceptances	2.75	-2.8	852	2619
Corporate bonds	31.34	-0.4	11678	-7883
Government bonds	63.57	10.1	33783	-12749
Domestic equity financing by non-financial enterprises	11.1	11.4	4596	-432
Other financing	10.64	6.8	2306	-1692
Of which: Asset-backed securities of depository institutions	1.83	-12.3	-1512	-712
Loans written off	7.98	14.9	4655	-307

Notes: ① The AFRE (stock) refers to outstanding funds provided by the financial system to the real economy at the end of a period. The AFRE (flow) refers to the volume of funds provided by the financial system to the real economy within a certain period of time. ②Since January 2023, the PBOC has included three types of non-deposit financial institutions in the banking industry, namely consumer finance companies, wealth management companies, and financial asset investment companies within the scope of financial statistics. Therefore, adjustments will be made to the data on "RMB loans issued by the real economy" and "loans written off" in the scale of social financing. ③YOY statistics in the table are on a comparable basis.

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

Box 2 Financial Support for a Macroeconomic Recovery

Since the beginning of 2023, the PBOC has implemented a sound monetary policy in a targeted and effective manner and has strengthened counter-cyclical adjustments to bolster a sustained recovery and an overall rebounding of the economy. At end-June, M2, the AFRE, and RMB loans witnessed a YOY growth of 11.3 percent, 9.0 percent, and 11.3 percent, respectively. YOY growth of GDP came in at 4.5 percent in Q1 and rose to 6.3 percent in Q2.

The sustainability of financial support for the real economy has significantly improved. In H1, headline financial data were good, the credit structure continued to improve, the financing costs of the real economy were brought down steadily, and the transmission effect on the macro economy gradually became apparent. **In terms of aggregates, the PBOC has maintained an appropriate money supply.** It has managed the pace and intensity of policy operations in response to the changing markets, employed a mix of monetary policy instruments, kept liquidity adequate at a reasonable level, and maintained reasonable growth of credit and aggregate financing. In March, the PBOC cut the RRR by 0.25 percentage points, releasing long-term liquidity of over RMB500 billion. Presently, growth of M2, the AFRE, and loans have all maintained high levels at about 10 percent, higher than the nominal GDP growth rate of about 5 percent in H1 and creating a favorable monetary and financial environment for a sustained improvement in the economy. **In terms of prices, the PBOC has stimulated market demand in a steady and effective manner.** It has continuously brought into play the important roles of the LPR reform and the market-based adjustment mechanism for deposit rates, and it has steadily brought down both the funding costs of enterprises and the lending rates for residents, thus contributing to tapping into the potential of market demand. In June, the OMO rate and the MLF rate were guided to decline by 0.1 percentage points, and the weighted average interest rates on corporate loans, residential mortgages, and inclusive MSB loans registered 3.95 percent, 4.11 percent and 4.68 percent respectively, down 21, 51, and 51 bps from the corresponding period of the previous year, respectively, and all were at historic lows. The financial system has been cutting down on its profits in favor of the real economy. In August, the OMO rate and the MLF rate were guided to decline by another 0.1 percentage points and 0.15 percentage points respectively, and counter-cyclical adjustments were strengthened when appropriate to bolster a sustained economic recovery. **In terms of the structure, the PBOC has stepped up its efforts to promote a transformation of the economic growth mode.** It has continuously increased its support for small and micro private enterprises, technological innovation, and green development, and it has vigorously supported the cultivation of endogenous economic growth drivers. The PBOC has also increased the quota for central bank lending to support rural development and central bank discounts, it has extended the terms of inclusive MSB loan facilities as well as facilities to support the delivery of presold residential housing projects, and it has continued to implement both the carbon emissions reduction facility (CERF) and the special central bank lending for clean and efficient coal use. At end-June, outstanding MLT loans to the manufacturing sector, green loans, inclusive MSB loans, and loans to “specialized, sophisticated, distinctive and innovative” small and medium-sized enterprises (SMEs) grew by 40.3 percent, 38.4 percent, 26.1 percent, and 20.4 percent year on year, respectively, substantially higher than the growth rate of all loans. The growth rate of real estate development loans has rebounded, with a YOY growth rate of 5.3 percent at end-June, 1.6 percentage points higher than that at end-2022.

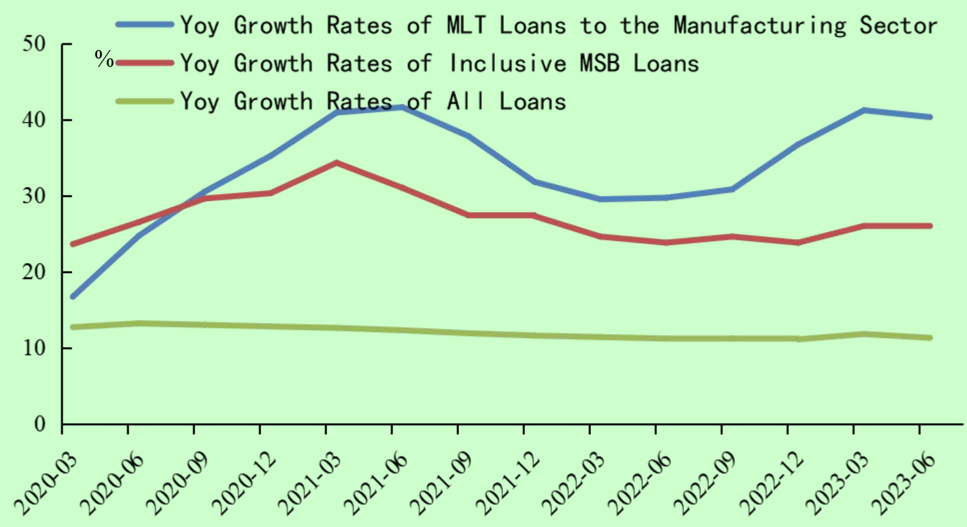


Figure: YOY Growth Rates of MLT Loans to the Manufacturing Sector, Inclusive MSB Loans and All Loans

The macro economy is expected to be on an upward trajectory, and economic figures will closely match the financial data in the future. As macroeconomic policies and financial policies are forward-looking and are usually introduced at an early stage, leading to a time lag between implementation of the policies and recovery of the real economy, financial data are currently temporarily ahead of the economic figures. The economic recovery is far from smooth. It will take time for consumption and the overall economy to recover in the post-pandemic era. From a global perspective, the growth rates of M2 were generally higher than the nominal GDP growth rates in both the U.S. and the EU when the COVID-19 containment measures were lifted in 2021. In China, the pandemic has been over for only about half a year. The willingness of consumers to spend money is declining as compared with the pre-pandemic levels and private investment is waiting for an additional impetus. Both of these factors are quite normal on the road towards a post-pandemic recovery. **Currently,** China's post-pandemic economic recovery is gradually moving on the right track. Economic circulation and the income of residents are both picking up, and the YOY growth rate of infrastructure investment continues to be higher than the YOY growth rate of all investments. In H1, the number of domestic tourists and the amount of revenue from tourism grew by over 60 percent and 90 percent year on year, respectively, and exports of independent brands owned by private enterprises achieved two-digit growth. China's GDP growth reached 5.5 percent in HI 2023 and the annual GDP growth target is expected to be attained. China's GDP growth maintains at a relatively high level among the major economies, and the gap between economic and financial growth will gradually be bridged. **From a long-term perspective,** the fundamentals sustaining China's long-term growth will remain unchanged. In the next 15 years, the middle-income group will grow to over 800 million, with a huge market potential. The driving force for sci-tech innovation is growing, green transition is steadily advancing, and the consumer market is gradually recovering and upgraded. The momentum for high-quality development is increasing. There is sufficient policy space to address any unexpected challenge or change. China has full confidence and patience to achieve steady and sustained development of its economy.

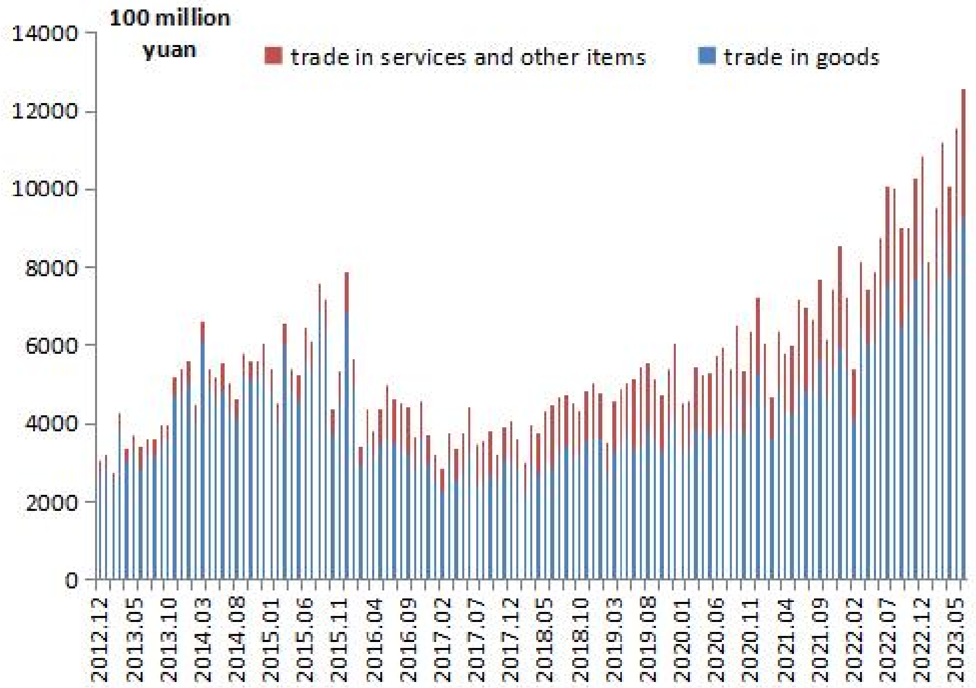
Going forward, the PBOC, in accordance with the arrangements made by the CPC Central Committee and the State Council, will continue to implement its sound monetary policy in a targeted and effective manner, manage the pace and intensity of policy operations based on market changes, and strive to maintain the momentum for an economic recovery. It will also strengthen counter-cyclical adjustments, build up its monetary policy toolbox, and make stepped-up efforts to expand domestic demand, boost market confidence, and prevent risks so as to effectively upgrade and appropriately expand economic output.

IV. The RMB exchange rate remained basically stable at an adaptive and equilibrium level

Since the beginning of 2023, cross-border capital flows have been stable and orderly, supply and demand in the foreign exchange market have basically been in equilibrium, and the RMB exchange rate is expected to be generally stable. Against the backdrop of a complex and volatile international situation, the major developed economies have continued to adjust their monetary policies, while the RMB exchange rate has fluctuated in both directions, playing its role as an auto stabilizer in macroeconomic management and the balance of payments and generally maintaining basic stability at a reasonable and equilibrium level. In the first half of 2023, based on market supply and demand, the RMB exchange rate depreciated against a basket of currencies. At end-June, the China Foreign Exchange Trade System (CFETS) and the RMB Exchange Rate Index based on the special drawing rights (SDRs) basket closed at 96.74 and 92.17, respectively, depreciating 2.0 percent and 4.1 percent, respectively, from end-2022. According to calculations by the Bank for International Settlements (BIS), from end-2022 to end-June 2023 the nominal effective exchange rate (NEER) and the real effective exchange rate (REER) of the RMB depreciated 2.5 percent and 5.7 percent, respectively. From 2005, when the reform of the RMB exchange-rate formation regime began, to end-June 2023, the NEER and REER of the RMB appreciated 40.6 percent and 37.2 percent, respectively. At end-June, the central parity of the RMB against the U.S. dollar was 7.2258, depreciating 3.6 percent from end-2022. At end-July, the central parity of the RMB against the U.S. dollar was 7.1305, appreciating 1.3 percent from end-June. In the first half of the year, the annualized volatility rate of the RMB against the U.S. dollar was 5.3 percent, up 0.1 percent year on year.

The internationalization of the RMB is steadily advancing, with increased use of the RMB in cross-border trade and investment. In the first half of the year, cross-border RMB settlements increased 20 percent year on year to RMB24.5 trillion, accounting for 57 percent of the total amount of domestic and foreign-currency settlements during the same period. Specifically, RMB receipts and payments posted RMB12.0 trillion and RMB12.4 trillion, respectively. Cross-border RMB settlements under the current account grew by 37 percent year on year to RMB6.3 trillion. In particular, RMB settlements under trade in goods registered RMB4.8 trillion, while RMB settlements under trade in services and under other items registered RMB1.5 trillion. Cross-border RMB settlements under the capital account registered RMB18.2 trillion, an increase of 15 percent year on year. In the first half of 2023, the proportion of cross-border RMB settlements under trade in goods and direct investments registered 23 percent and 70 percent of local and foreign currency cross-border settlements, respectively, with YOY growth of 6.7 and 6.6 percentage points, respectively, which is the highest level in recent years.

Figure 3 Monthly RMB Settlements under the Current Account



Source: The People's Bank of China.

The attractiveness of RMB assets is constantly increasing. As of end-June, the total balance of financial assets. such as domestic RMB stocks, bonds, loans, and deposits held by overseas entities, was about RMB10 trillion. The offshore RMB market was relatively active. From January to June, the issuance of offshore RMB bonds (excluding negotiable certificates of deposit) increased by 34 percent year on year, and by end-June the balance of RMB loans in Hong Kong had increased by 69 percent year on year.

Part 2 Monetary Policy Operations

In Q2 2023, the PBOC resolutely implemented the decisions and arrangements made by the CPC Central Committee and the State Council. Following the principle of seeking stability while making progress, the PBOC pursued a sound monetary policy in a targeted and effective manner. It strengthened counter-cyclical adjustments, kept liquidity adequate at a reasonable level, and enhanced the stability and sustainability of credit aggregate growth. The PBOC facilitated a steady decline in the costs of corporate financing and consumer credit, guided financial institutions to scale up financial support for weak links and key areas, such as financial inclusion, sci-tech innovation, and green development, and promoted a continuous recovery and overall rebounding of the national economy.

I. Conducting open market operations in a flexible manner

Conducting reverse repos in a flexible and targeted manner. In Q2, the PBOC closely followed the macroeconomic and financial developments and strengthened the assessment and monitoring of liquidity supply and demand in the banking system. It managed the intensity and pace of open market operations in a flexible manner so as to offset the influence of reserve deposits, tax payments, government bond issuances, regulatory assessments at quarter-ends and other factors in the supply and demand of liquidity in a timely manner, and it kept liquidity in the banking system adequate at a reasonable level. In late June, the PBOC timely increased reverse repos in response to the mounting demand for short-term funds among financial institutions and the emergence of liquidity pressures in some financial institutions. From June 25 to June 30, the PBOC conducted 7-day reverse repos in a total amount of RMB1.169 trillion, fully satisfying the demand of primary dealers and ensuring a sufficient supply of liquidity by end-H1 and the smooth operation of all market participants in the money market by quarter-end.

Guiding market rates to move down moderately. On June 13, the rate of open market 7-day reverse repos dropped by 10 basis points to 1.90 percent, reflecting market supply and demand of funds and sending a policy signal from the central bank of enhancing counter-cyclical adjustments and stabilizing market expectations, thereby boosting market confidence. From the reduction of the reverse repo rate to end-June, the weighted average rate of 7-day reverse repos for depository institutions in the interbank market (DR007) averaged 1.94 percent, moving around the rate of open market 7-day reverse repos without great volatility. On August 15, the rate of open market 7-day reverse repos decreased by another 10 basis points to 1.80 percent, further boosting market confidence.

In addition, in Q2 the PBOC continued to conduct central bank bill swap (CBS) operations on a monthly basis, which were conducive to improving liquidity in the secondary market of bank-issued perpetual bonds. Meanwhile, the PBOC continued to issue central bank bills in Hong Kong on a regular basis. At end-June, the balance of central bank bills in Hong Kong reached RMB80 billion, playing a positive role in promoting the sound development of the offshore RMB money market and the bond market.

II. Conducting MLF and SLF operations

Conducting MLF operations to fully meet market demand. From December 2022 to August 2023, the MLF was renewed for nine consecutive months, with the amount of newly-issued MLFs exceeding that of maturing MLFs on each occasion. The MLF rate moved down by 10 and 15 basis points in June and August, respectively, ensuring the supply of medium and long-term liquidity and giving effective play to the guiding role of interest rates. In H1, the PBOC conducted a total of RMB2.291 trillion of MLF operations, all of which were with a maturity of one year and with those in Q2 reaching RMB532 billion. The MLF rates in the first five months and in June were 2.75 percent and 2.65 percent, respectively. At end-June, outstanding MLFs registered RMB5.191 trillion, an increase of RMB641 billion from the beginning of 2023.

Conducting standing lending facility(SLF) operations. Locally-incorporated financial institutions were provided with a sufficient amount of short-term liquidity support as needed so as to stabilize market expectations, strengthen the stability of liquidity in the banking system, and prevent liquidity risks. In H1, the PBOC conducted a total of RMB11.98 billion in SLF operations, among which those in Q2 reached RMB4.31 billion. At end-June, outstanding SLF operations registered RMB3.48 billion. The SLF rate continued to serve as the ceiling of the interest rate corridor, thereby helping to maintain smooth operations in the money market. At end-June, the overnight, 7-day, and 1-month SLF rates stood at 2.75 percent, 2.90 percent, and 3.25 percent, respectively, all down 0.1 percentage points from end-Q1. In August, SLF rates of all maturities declined by another 0.1 percentage points.

III. Lowering the RRR for financial institutions

Lowering the RRR to inject long-term liquidity. On March 27, 2023, the PBOC reduced the RRR for financial institutions (excluding those that had already implemented an RRR of 5 percent) by 0.25 percentage points. It freed up over RMB500 billion in long-term funds and saved about RMB6 billion in the cost of funds in the banking sector. This marked the 15th RRR cut since 2018; the current weighted average RRR for financial institutions is 7.6 percent, with the lowest RRR in three brackets at 5 percent, which strongly supports the development of key areas, such as inclusive finance.

IV. Further improving the macro-prudential system and the management framework

Giving full play to the role of the macro-prudential assessment (MPA) in optimizing the credit structure and promoting the supply-side structural reform of the financial sector. In Q2, the PBOC further optimized the MPA framework and guided financial institutions to maintain appropriate credit aggregates at a steady pace and to step up support for inclusive MSB loans, especially unsecured inclusive MSB loans, for medium and long-term financing to the manufacturing sector.

Refining the regulatory framework for systemically important financial institutions. The PBOC strengthened the monitoring and analysis of systemically important banks (SIBs) and worked with related regulators to guide the SIBs to update and improve their recovery and resolution plans, making them more practical and effective. The PBOC urged the SIBs to fulfill the additional capital and leverage ratio requirements on time and to disclose the assessment indicators and the relevant supervisory indicators in accordance with requirements so as to promote their sound operations.

Adjusting the macro-prudential adjustment parameter for cross-border financing. On July 20, 2023, in order to further improve macro-prudential management of unified cross-border financing and to continue to expand the sources of cross-border funds for enterprises and financial institutions and to optimize their asset-liability structure, the PBOC and the State Administration of Foreign Exchange (SAFE) decided to raise the macro-prudential adjustment parameter for cross-border financing for enterprises and financial institutions from 1.25 to 1.5. This was the first time it was raised to 1.5 since the creation of this tool in 2016.

V. Giving full play to the role of monetary policies to optimize the structure

Actively using central bank lending in support of rural development and MSBs, central bank discounts, pledged supplementary lending (PSL), and other policy instruments. Central bank lending in support of rural development and MSBs was utilized to guide locally incorporated financial institutions to expand their credit supply for rural revitalization. Central bank lending for poverty alleviation was rolled over according to current regulations so as to consolidate the achievements in poverty alleviation. The PBOC promoted coordinated regional development by continuously guiding locally incorporated financial institutions in ten provinces to effectively use policy instruments, such as central bank lending, so as to expand the credit supply for weak links within the region. On June 30, the PBOC decided to increase central bank lending and discount quotas in support of rural development and MSBs by a total of RMB200 billion. The move is aimed at further ramping up financial support for agriculture, rural areas, farmers, MSBs, and private enterprises, providing liquidity in a targeted manner, reducing funding costs, helping expand employment, and boosting recovery of the endogenous drivers for economic growth. On August 16, the PBOC decided to increase the central bank lending quota in support of rural development and MSBs by RMB35 billion and to provide financial support for flood prevention and relief as well as post-disaster reconstruction in disaster-hit provinces (municipalities). At end-June, outstanding central bank lending in support of rural development, in support of MSBs, and for poverty alleviation posted RMB565.8 billion, RMB1.4231 trillion, and RMB138.2 billion, respectively. Outstanding central bank discounts registered RMB595 billion and the outstanding PSL posted RMB2.9896 trillion.

Continuously utilizing instruments in support of inclusive MSB loans. At end-June, through these instruments, the PBOC provided incentive funding in the amount of RMB49.8 billion, an increase of RMB22.3 billion from the beginning of 2023. It supported an increase of RMB2.7 trillion in inclusive MSB loans issued by locally incorporated financial institutions, up RMB1.1 trillion from the beginning of 2023. In order to continuously support the development of MSBs, the instruments in support of inclusive MSB loans has been extended until end-2024. The PBOC has decided to incentivize financial institutions at 1 percent of the incremental balance of their inclusive MSB loans, down from 2 percent.

Implementing the carbon emission reduction facility (CERF) in tandem with the targeted central bank lending facility for clean and efficient use of coal. At end-June, the outstanding amount through these two PBOC instruments registered RMB453 billion and RMB245.9 billion, respectively, an increase of RMB143.3 billion and RMB164.8 billion, respectively, from the beginning of 2023. In order to sustain financial support for green development and a stable energy supply, the CERF has been extended until end-2024 and the targeted central bank lending facility for clean and efficient use of coal has been extended until end-2023.

Targeted central bank lending facilities for inclusive elderly care continue to play a guiding role. At end-June, outstanding central bank lending for inclusive elderly care posted RMB1.3 billion, an increase of RMB600 million from the beginning of 2023. Central bank lending for sci-tech innovation, targeted central bank lending for equipment upgrading and renovation, and targeted central bank lending for transport and logistics all expired and the PBOC exited from these facilities, but outstanding funds that were issued are still available.

The outstanding amount posted RMB320 billion, RMB169.4 billion, and RMB43.4 billion, respectively, an increase of RMB120 billion, RMB88.5 billion, and RMB19.2 billion from the beginning of 2023.

Leveraging policy tools to promote the steady and sound development of the real estate market. The PBOC implemented the loan support scheme to ensure deliveries of presold housing projects. Its balance at end-June was RMB500 million. For continuous policy support, the scheme will be extended until end-May 2024. The PBOC launched targeted central bank lending to help ease real estate developers' difficulties and the support scheme for rental housing loans, thereby supporting national financial asset management corporations to acquire existing housing projects of distressed real estate developers and encouraging financial institutions to issue long-term loans for rental housing purchases by specialized rental housing operators in pilot cities.

Box 3 Continuous Support from Structural Monetary Policies in Key Areas and Weak Links

In recent years, the PBOC has resolutely implemented the decisions and arrangements of the CPC Central Committee and the State Council and it has continuously adjusted and improved its system of structural monetary policy instruments with a focus on providing support for key areas and weak links in the national economy and serving high-quality development. The central bank mainly considers two factors when deciding on the creation, extension, or exit of structural monetary policies: **First, prominent structural problems in economic performance.** For instance, to ease the difficulties often faced by micro and small enterprises in accessing affordable financing, the PBOC has created various structural instruments, including long-term structural instruments, such as central bank lending and discounts. and temporary structural instruments, such as inclusive MSB lending facilities. **Second, financial institutions enhancing their willingness and capabilities to serve specific areas.** In areas such as supporting green and low carbon development and sci-tech innovation, financial institutions still face a relatively high "green premium" and a "risk premium." The PBOC has created instruments, including the CERF and central banking lending for sci-tech innovation to give full play to the leveraging and guidance roles. In light of the evolving nature of these two factors, structural instruments may change with economic development and policy guidance, and hence most of the instruments are temporary. Since the beginning of 2023, a proper balance between "entry" and "exit" has been maintained in structural monetary-policy instruments, which has played a positive role in encouraging and guiding financial institutions to optimize the allocation of credit resources and in promoting high-quality economic development.

"Entry" is mainly reflected in serving high-quality development. The aggregate amount of structural instruments remained at an appropriate level. As of end-June 2023, outstanding structural monetary-policy instruments registered RMB6.9 trillion, accounting for about 16 percent of the PBOC's total assets, a ratio basically on par with similar financial systems, such as those in the euro area, the UK, and Japan. Structural instruments prioritized areas that most needed bank funding support in the following respects: **First, providing continuous support for inclusive finance.** Small and micro enterprises mirror the economic vitality, which requires continued and consolidated support for inclusive finance, such as MSBs. Since the beginning of 2023, the PBOC has provided an additional RMB235 billion through central bank lending and discounts in support of rural development and small businesses. It has extended implementation of the inclusive MSB lending facility until end-2024, and it has adjusted the ratio of incentive funds as appropriate. **Second, providing continued support for areas such as green and low carbon development and sci-tech innovation.** Green development and sci-tech innovation, which call for more effective and stronger funding support, are priorities to advance the momentum for economic growth . Since the beginning of 2023, the PBOC has extended both the CERF and the targeted central bank lending for clean and effective coal use. For broader policy benefits, it also expanded coverage of the CERF by including some foreign-funded banks and locally incorporated banks. Meanwhile, in accordance with the action plan to support financing for sci-tech enterprises, it gave play to the incentive role of central bank lending and other policy instruments to channel continued support from financial institutions to such enterprises. **Third, supporting the smooth functioning of the real estate market.** The implementation of targeted policies has met the reasonable funding needs of the real estate market, thus contributing to the stability of consumption, investment, and the macro economy. The loan support scheme to ensure deliveries of presold housing projects has been extended until end-May 2024 so as to encourage and guide financial institutions to provide financial support for eligible projects. A scheme to provide support for rental housing has been steadily implemented in pilot cities by supporting diversified and full-cycle financial services of financial institutions for the housing rental market.

"Exit" in a smooth and orderly manner. The PBOC will evaluate the structural instruments when they expire. An orderly exit will take place as scheduled when some instruments attain their expected goals. For instance, the central bank lending facilities, with their respective quotas of RMB300 billion and RMB500 billion, were created at the beginning of 2020 to support the COVID-19 response and to ensure supply as well as the recovery of production, and the exit came as scheduled at end-June 2020. When some policy instruments expire, an appropriate roll-over of existing funds will help achieve a gradual and progressive exit. For some facilities that were introduced in 2022, such as central bank lending for sci-tech innovation, targeted central bank lending for equipment upgrading, and targeted central banking for transportation and logistics, to achieve potentially the best "progressive" exit effects, the roll-overs of existing funds will be up to three to five years when the PBOC exits from those instruments that will be expiring consecutively this year. The PBOC will continue to implement policy instruments in areas that call for necessary or continued support, including inclusive finance and green and low carbon development.

In the next step, the PBOC will fully leverage the dual functions of monetary policies in terms of aggregate amount and structure. Structural instruments will further focus on key areas, be reasonable and appropriate, and achieve a proper balance between entry and exit. The PBOC will continue to adjust and refine the monetary-policy instruments in light of economic and financial developments, guide financial institutions to beef up support for key areas and weak links, and, when necessary, create new instruments in accordance with the decisions and arrangements of the CPC Central Committee and the State Council to better serve the high-quality development of the economy.

VI. Enhancing the efficiency and role of credit policy in structural guidance

Constantly improving the quality and effectiveness of financial services for MSBs. The PBOC actively promoted the project to enhance financial services for micro, small, and medium enterprises (MSMEs), accelerated the establishment of the long-term mechanism for boosting the confidence, willingness, capacity, and professionalism of financial institutions to issue loans, improved the assessment scheme for credit policy in terms of supporting MSBs, and continuously enhanced the willingness, capability, and sustainability of financial institutions to serve the MSBs. The PBOC timely promoted the expansion of coverage and the increase in volume of bond financing supporting tools for private enterprises, namely, “the second arrow.” Since the expansion of coverage in November 2022, support has been provided for a total of RMB284 billion bonds issued by private enterprises. The PBOC also increased the credit sources of banks to support small enterprises, supporting commercial banks to issue a total of RMB124 billion special financial bonds for SMEs in H1 2023. All these moves were aimed at promoting an increase in the aggregate, expanding the coverage, and reducing the cost of MSB financing. At end-June, outstanding inclusive MSB loans and the number of inclusive MSBs that were granted loans registered a YOY increase of 26.1 percent and 13.3 percent, respectively, and the interest rate on newly issued inclusive MSB loans in June posted 4.40 percent.

Constantly improving financial services for rural revitalization. Together with the National Administration of Financial Regulation, the China Securities Regulatory Commission, the Ministry of Finance, and the Ministry of Agriculture and Rural

Affairs, the PBOC issued the *Guiding Opinions on Providing Financial Support for Advancing Rural Revitalization Across the Board and Stepping Up Efforts to Build Up China's Strength in Agriculture*. It guided financial institutions to optimize resource allocations by continuously increasing the supply of financial resources for major areas, such as stable production and secure supplies of grain, key agricultural products, sci-tech equipment innovation, and green development in agriculture, and the high-quality development of rural industries. It assessed the financial institutions in terms of their providing financial services for rural revitalization and it enhanced the application of the assessment results so as to further enhance the quality and efficiency of financial services for rural revitalization. At end-June, outstanding agro-related loans registered a YOY increase of 16 percent, reaching RMB54.6 trillion.

Continuously providing financial services for the manufacturing sector and sci-tech innovation. Jointly with the administrative agencies of the relevant industries, the PBOC engaged in match-making between financial institutions and key investment projects and enterprises in the manufacturing sector and sci-tech innovation. It drafted the *Action Plan for Enhancing Financial Support for Sci-tech Enterprises,* improving the policy framework for serving sci-tech enterprises and providing incentives to guide financial institutions to increase credit support for the manufacturing sector and for sci-tech innovation. As of end-June, outstanding medium and long-term loans to the manufacturing sector grew by 40.3 percent year on year to RMB11.6 trillion, while medium and long-term loans to the high-tech manufacturing sector and loans to sci-tech small and medium enterprises reached RMB2.5 trillion and RMB2.4 trillion, with a YOY growth of 41.5 and 25.1 percent, respectively. The PBOC actively gave play to the financing function of the interbank bond market, innovatively launched financing instruments for sci-tech innovation, such as financial bonds for innovation and entrepreneurship and sci-tech innovation bills, and encouraged good use of "the second arrow," namely, guarantee and credit enhancement instruments, supporting the bond financing of eligible sci-tech enterprises and leading enterprises in the manufacturing sector. As of end-June, outstanding bills for sci-tech innovation issued by sci-tech enterprises reached RMB226.4 billion, outstanding bonds issued by sci-tech corporations stood at RMB225.8 billion, and outstanding bonds issued in the interbank market by enterprises in strategic emerging industries amounted to approximately RMB660 billion.

VII. Improving the formation and transmission mechanism of the market-based interest rate

Continuously unleashing the benefits of the LPR reform and giving play to the role of the market-based adjustment mechanism in deposit interest rates.

The benefits of the LPR reform have been continuously unleashed, the rates for OMOs and the MLF have been guided to decline by 0.1 percentage points, the one-year and over-five-year LPR issued in June were guided to decline 0.1 percentage points, promoting a decline in actual loan rates. In June 2023, the weighted average interest rate of corporate loans stood at 3.95 percent, declining 0.21 percentage points year on year and remaining at a historical low. In August, the rates of OMOs and the MLF rate declined by another 0.1 and 0.15 percentage points, respectively, continuously giving play to the guidance role of policy rates. The effect of the market-based adjustment mechanism on deposit interest rates came further into play. In June, the major banks voluntarily lowered the quoted deposit rates of some maturities and simultaneously lowered the authorized ceiling of internal rates. This was the second time that commercial banks had voluntarily adjusted the posted deposit rates in accordance with their operational needs and market supply and demand since September 2022, thereby further enhancing the market-based deposit rates and the transmission efficiency of interest rates.

Continuing to implement the dynamic adjustment mechanism for first-home mortgage interest rates. By the end of June 2023, 100 cities had reduced or removed the interest rate floor on first-home loans, among all 343 cities (municipal or above). In particular, 87 cities lowered the interest rate floor for first-home loans 10 to 40 basis points lower than the national floor, and 13 cities removed the floor for first-home loans. The adjustment and improvement in the interest rate policy for first-home loans have brought down mortgage rates. Nationally, the weighted average interest rate for newly issued personal mortgage loans in June registered 4.11 percent, down 0.51 percentage points year on year.

VIII. Deepening the market-based reform of the RMB exchange rate

The PBOC 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. Ensuring that the market plays a decisive role in determining the exchange rate, the PBOC gave play to the role of the exchange rate as an auto stabilizer for macroeconomic management and for the balance of payments. With comprehensive measures, the PBOC strengthened expectation guidance and kept the RMB exchange rate basically stable at an adaptive and equilibrium level. In H1, the highest and lowest RMB central parities against the U.S. dollar were 6.7130 and 7.2258, respectively. During the 118 trading days, the RMB appreciated on 53 days and depreciated on 65 days. The biggest intraday appreciation and depreciation were 1.0 percent (654 bps) and 0.9 percent (630 bps), respectively. The RMB witnessed both an appreciation and a depreciation against major international currencies, with two-way fluctuations. As of end-June, the central parity of the RMB against the Japanese yen had appreciated 4.5 percent from end-2022, while the central parity of the RMB against the U.S. dollar, the euro, and the pound sterling had depreciated 3.6 percent, 5.8 percent, and 8.2 percent, respectively, during the same period. From 2005 when the reform of the RMB exchange-rate formation regime began to end-June 2023, the RMB appreciated by a cumulative 14.5 percent, 27.1 percent, and 45.8 percent, respectively, against the U.S. dollar, the euro, and the Japanese yen. Direct RMB trading was rather buoyant in the interbank foreign exchange market with stable liquidity, the exchange costs for microeconomic entities such as enterprises were reduced, and bilateral trade and investment were promoted.

Box 4 The RMB Exchange Rate Remains Basically Stable at an Adaptive and Equilibrium Level

In the first four months of 2023, the RMB exchange rate remained basically stable against the U.S. dollar, with an cumulative appreciation of 0.6 percent for the central parity. Since the beginning of May, domestic and overseas factors have been intertwining with one another, thereby heightening the depreciation pressures on the RMB exchange rate. **First,** expectations about Fed rate hikes have been reversed. Despite weakened expectations of further Fed rate hikes at the beginning of 2023, such expectations have started to rise again, supporting an appreciation of the U.S. dollar. **Second,** political factors, such as the U.S. government debt ceiling and geopolitical risks, have been driving up risk-aversion sentiments in global markets and pushing up the U.S. dollar exchange rate. **Third,** domestic seasonal foreign exchange purchasing demands have widened the foreign exchange supply-demand gap. From June to August, companies listed on the Hong Kong Stock Exchange (HKEX) should pay dividends to their shareholders, and most of such dividend payout funding must be fulfilled through foreign exchange purchases. After the COVID-19 pandemic, foreign exchange purchasing demands for cross-border travel and overseas studies also increased significantly. On May 17, the offshore and onshore RMB exchange rates (CNH and CNY) against the U.S. dollar consecutively moved beyond 7.

The PBOC and the SAFE have paid great attention to foreign exchange development, and they have mitigated the depreciation pressures on the RMB exchange rate in a proactive yet prudent manner through measures such as strengthening expectation management, regulating supply and demand in the foreign exchange market, and raising the unified macro-prudential adjustment parameter for cross-border financing. **Overall, the current RMB exchange rate does not deviate from the fundamentals, and the foreign exchange market is operating in a generally orderly manner.** In June, the surplus between the purchase and sale of foreign exchange in the banking sector amounted to USD8.2 billion, significantly higher than the monthly average in the previous months of this year. In H1 2023, the foreign exchange purchase ratio, which measures the willingness for foreign exchange purchases, registered 67.5 percent, 0.5 percentage points higher than that in H1 2022, thus indicating rational trading behavior in the foreign exchange market. In July, the RMB strengthened against the U.S. dollar, with the closing rate on July 31 reaching 7.1465, an appreciation of 1.6 percent from the end of June. Since the beginning of August, as the USD index has gone up and the RMB has depreciated against the U.S. dollar. However, the CFETS RMB exchange rate index, which measures the RMB exchange rate against a basket of currencies, has strengthened, with a price of 97.47 on August 11 or an increase of nearly 2 percent from its recent trough.

The RMB exchange rate reflects price relations between the RMB and other currencies, which are subject to a wide range of domestic and overseas factors. The short-term exchange rate is full of uncertainties and difficult to predict, whereas the long-term exchange rate is determined intrinsically by the fundamentals of the Chinese economy. Currently, from the perspective of both overseas and domestic factors, the RMB exchange rate will not move in the single direction of depreciation; rather, it will float in both directions. In terms of overseas factors, the rate hike cycle by the U.S. Fed is coming to an end, thus limiting momentum for a significant rise in the U.S. dollar. From a domestic perspective, the fundamentals for sound Chinese economic growth over the long run remain unchanged. As smooth flows in the economy have been promoted, the continuous overall improvement in China's economic performance will support the RMB exchange rate. In China, the current account surplus maintains at a moderate level of roughly 2 percent of GDP and cross-border capital flows remain balanced autonomously. China's foreign exchange reserves balance remains steadily above USD3 trillion and witnessed a month-on-month increase at the end of July, remaining in first place in the world.

During the past few years, the RMB exchange rate moved beyond 7 against the U.S. dollar on three occasions and later it strengthened to under 7. In the process of dealing with multiple rounds of external shocks, **the PBOC and the SAFE have accumulated rich experience and have developed an ample reserve of policy tools, hence they have the confidence, conditions, and capabilities to maintain steady operations in the foreign exchange market.** Going forward, the PBOC and the SAFE will resolutely implement the decisions and arrangements made by the CPC Central Committee and the State Council. With the aim of keeping the RMB exchange rate basically stable at an adaptive and equilibrium level, the PBOC and the SAFE will leverage the advantages of a managed floating exchange rate regime based on market supply and demand with reference to a basket of currencies. They will also pursue a holistic approach in terms of policy implementation and they will stabilize expectations, making best use of various regulatory tools to regulate supply and demand in foreign exchange markets and correcting pro-cyclical single-direction market behavior so as to strongly forestall risks of exchange rate overshooting.

IX. Forestalling and defusing financial risks

Strengthening the monitoring and assessment of systemic risks. The PBOC has continued to strengthen its monitoring and assessment of systemic financial risks, and it has improved its framework for monitoring and assessment of financial stability. It has also organized banking financial institutions to conduct stress tests and has provided them with timely risk warnings, thus guiding financial institutions to operate in a sound manner. The PBOC has conducted a Central Bank Rating on over 4,000 banking financial institutions on a regular basis and it has established a differentiated management framework according to the rating results. For institutions rated Grades 1-7, the PBOC has established an index system that includes expansionary risks, inter-bank risks, liquidity risks, and credit risks, and it has organized early warnings with the aim of preventing these institutions from deteriorating into high-risk institutions. Meanwhile, the PBOC has also continued to conduct risk monitoring in the securities sector, the insurance sector, and financial markets through the use of financial market stress indexes to monitor risks in the equity, bond, money, and foreign exchange markets.

Continuously advancing the forestalling and defusing of financial risks. The PBOC remains committed to addressing risks in a market- and law-based manner and it has properly resolved some prominent financial risks. For high-risk institutions rated Grades 8-10 in the Central Bank Rating, the PBOC has distinguished previously identified institutions from newly identified institutions in the process of addressing related risks. The PBOC has proactively taken effective measures to reduce the number of previously identified high-risk institutions. As for newly identified institutions, the PBOC has established pilot programs to implement early corrections with hard constraints and to defuse risks within a time limit of one year. These measures have already had preliminary effects.

X. Improving the capability to serve cross-border trade, investment, and financing

Promoting the coverage and quality of facilitation policies for quality enterprises. The SAFE has put more effort into publicizing facilitation policies for quality enterprises and it has supported more banks and enterprises with good credit, excellent capabilities, as well as real demand to receive the benefits of the facilitation policies. These actions have continuously expanded the coverage of the facilitation policies for small- and medium-sized quality enterprises. In the first half of 2023, facilitation-related transactions amounted to USD460 billion.

Deepening international monetary and financial cooperation. As of end-June 2023, under the bilateral currency swap agreements between the PBOC and the overseas monetary authorities, the overseas monetary authorities had utilized a total of RMB115.08 billion and the PBOC had utilized foreign currencies equivalent to USD423 million. These operations have played an active role in promoting bilateral trade and investment.

Table 8 Trading Volume of the RMB Against Other Currencies in the Interbank Foreign Exchange Spot Market in H1 2023

RMB100 million

Currency	USD	EUR	JPY	HKD	GBP	AUD	NZD
Trading volume	329787.43	3945.74	2562.26	897.28	116.72	258.45	54.14
Currency	SGD	CHF	CAD	MYR	RUB	ZAR	KRW
Trading volume	61.01	37.91	199.99	5.94	29.78	1.05	23.13
Currency	AED	SAR	HUF	PLN	DKK	SEK	NOK
Trading volume	0.30	12.77	1.00	0.55	2.01	21.99	0.56
Currency	TRY	MXN	THB	KHR	KZT	MNT	IDR
Trading volume	1.00	8.09	20.65	0	0.05	0	11.88

Source: China Foreign Exchange Trade System.

Part 3 Financial Market Conditions

In H1 2023, the performance of the financial market was generally stable. Money market interest rates went down, with increasingly active market transactions. The interest rates of treasury bond and financial bond issuances decreased, with an increase in the volume of issuances and transaction. The stock market index picked up, with turnover and the amount of funds raised decreasing year on year.

I. Financial market overview

1. Money market interest rates went down with increasingly active market transactions

In June 2023, the monthly weighted average interest rate for interbank lending was 1.57 percent, and the monthly weighted average interest rate for pledged repos posted 1.67 percent, 13 basis points and 18 basis points lower than those in March 2023, respectively. The monthly weighted average interest rate for government-backed bond pledged repos among depository institutions posted 1.47 percent, 20 basis points lower than the monthly weighted average interest rate for pledged repos. At end-June, the overnight and 7-day Shibor posted 1.48 percent and 2.06 percent, respectively, down 47 basis points and 16 basis points from end-December 2022, respectively.

The level of market transaction activity increased. In H1 2023, the cumulative volume of bond repos trading on the interbank market registered RMB796.4 trillion, representing an average daily turnover of RMB6.5 trillion and an increase of 25.4 percent year on year. The YOY growth rate was 4.8 percentage points higher than that in Q1 2023. The cumulative volume of trading for interbank lending registered RMB74.1 trillion, representing an average daily turnover of RMB602.4 billion and an increase of 9.2 percent year on year. In terms of the maturity structure, overnight repos accounted for 86.8 percent of the total turnover in bond repos, up 1.2 percentage points year on year, and overnight lending constituted 90.3 percent of the total turnover in interbank lending, up 2.0 percentage points year on year. In H1 2023, the volume of bond repos trading on the exchange markets increased 16.8 percent year on year to RMB225.2 trillion.

Table 9 Fund Flows Among Financial Institutions in H1 2023

Unit: RMB100 million

	Repos		Interbank lending	
	H1 2023	H1 2022	H1 2023	H1 2022
Chinese-funded large banks①	-3,447,118	-2,010,169	-261,347	-197,651
Chinese-funded medium-sized banks②	-613,901	-819,288	-46,373	-78,357
Chinese-funded small-sized banks③	261,586	1,363	53,756	38,862
Securities institutions④	1,033,712	811,036	213,447	185,566
Insurance institutions⑤	103,462	94,317	571	604
Foreign-funded banks	30,671	39,356	-8,916	-6,167
Other financial institutions and vehicles⑥	2,631,587	1,883,386	48,863	57,141

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. ② Chinese-funded medium-sized banks refer to policy banks, China Merchants Bank, and eight other joint-equity commercial banks, Bank of Beijing, Bank of Shanghai, and Bank of Jiangsu. ③Chinese-funded small-sized banks refer to the 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. ④ Securities institutions include securities firms, fund management companies, and futures companies. ⑤Insurance institutions include insurance firms and corporate annuities. ⑥ Other 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 Deposits (CDs) and negotiable CD businesses operated orderly. In H1 2023, about 14,000 interbank CDs were issued on the interbank market, raising RMB12.8 trillion. The total volume of trading on the secondary market registered RMB130.1 trillion. At end-June, outstanding interbank CDs reached RMB14.4 trillion. The weighted average interest rate of 3-month interbank CDs was 2.39 percent, 4 basis points higher than that of the 3-month Shibor. In H1, about 38,000 negotiable CDs were issued by financial institutions, raising RMB8.6 trillion and increasing by RMB1.1 trillion year on year.

Interest rate swap transactions remained stable. In H1 2023, the RMB interest rate swap market witnessed 167,000 transactions, increasing 37.1 percent year on year, with the volume of the notional principal totaling RMB15.1 trillion, an increase of 78.9 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 RMB10.4 trillion, accounting for 69.0 percent of the principal of all maturities. The 7-day fixing repo rate (FR) and the Shibor served as the main reference rates for the floating leg of the RMB interest rate swaps, accounting for 90.4 percent and 8.3 percent, respectively, of the total notional principal of the interest rate swaps. In H1, interest rate swaps anchored to the loan prime rate (LPR) witnessed 778 transactions, with RMB133.41 billion of the notional principal.

Table 10 Interest Rate Swap Transactions in H1 2023

	Transactions	Notional principal (RMB100 million)
H1 2023	167,162	151,031.9
H1 2022	105,227	84,433.6

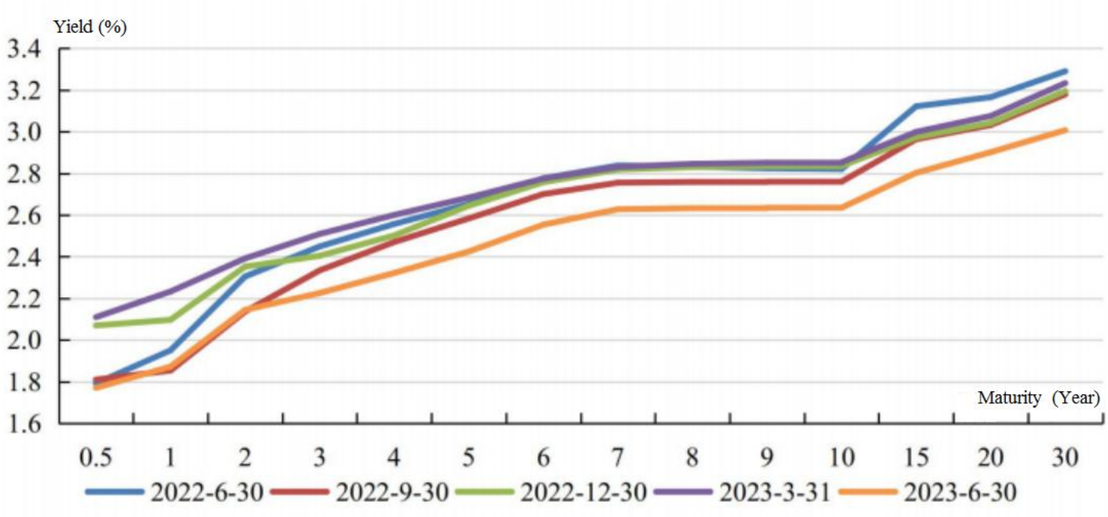
Source: China Foreign Exchange Trade System.

The interest rate options business developed at a steady pace. In H1 2023, a total of 697 interest rate options transactions were concluded, totaling RMB111.60 billion. Specifically, 6 were interest rate swap transactions, amounting to RMB2.0 billion of the notional principal, and 691 were interest rate cap/floor transactions, amounting to RMB109.60 billion of the notional principal.

2. The coupon rates of bonds went down, while bond issuances and trading increased

The coupon rates of government securities and financial bonds fell. In June 2023, the yield on 10-year government securities issued by the Ministry of Finance was 2.65 percent, 18 basis points lower than the rate in March. The coupon rate of 10-year financial bonds issued by the China Development Bank (CDB) was 2.75 percent, 24 basis points lower than the rate in March. The average rate of 1-year short-term financing bills (bond rating A-1) issued by AAA-rated enterprises was 3.47 percent, 18 basis points lower than the rate in March.

Figure 4 Yield Curves of Government Securities in the Interbank Market



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

On the whole, the yield on government securities edged downward in H1 with slightly expanded term spreads. At end-June 2023, yields on 1-year, 3-year, 5-year, 7-year, and 10-year government securities decreased by 22 basis points, 18 basis points, 22 basis points, 19 basis points, and 20 basis points, to 1.87 percent, 2.23 percent, 2.42 percent, 2.63 percent, and 2.64 percent from end-2022, respectively. The term spread between 1-year and 10-year government securities was 76 basis points, increasing 2 basis points from end-2022.

Bond issuances increased year on year. The cumulative value of bonds issued in H1 grew by 9 percent year on year to RMB34.3 trillion, RMB2.8 trillion more than that in the same period of last year mainly due to the large increase in government securities and interbank certificates of deposits. At end-June, outstanding bonds held in custody amounted to RMB150.3 trillion, representing an increase of 6.1 percent year on year. Since the expansion of the "second arrow" in November 2022, a supporting instrument to stabilize and promote bond financing by private enterprises, bond issuances by private enterprises has reached a cumulative RMB28.4 billion.

The trading volume of spot bonds grew. In H1, the value of cash bonds traded on the bond market posted RMB163.0 trillion, registering an increase of 13.1 percent year on year. Specifically, the value of cash bonds traded on the interbank market was

RMB143.7 trillion, representing an increase of 15.6 percent year on year. The value of cash bond transactions on the stock exchanges totaled RMB19.2 trillion, a decrease of 2.5 percent year on year.

Table 11 Bond Issuances in H1 2023

Unit: RMB100 million

Type of bond	Issuance	YOY change
Government securities	44,846	10,471
Local government bonds	42,033	-10,469
Central bank bills	0	0
Financial bonds①	184,218	26,709
Of which: Financial bonds issued by the CDB and policy financial bonds	35,619	7,157
Interbank certificates of deposits	128,107	19,449
Corporate credit bonds②	71,471	1,317
Of which: Debt-financing instruments of non-financial enterprises	45,448	-2,995
Enterprise bonds	2,347	-830
Corporate bonds	18,057	4,569
Bonds issued by international institutions	709	198
Total	343,278	28,227

Notes: ① Including 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. ②Including 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(CSRC), and China Central Depository & Clearing Co., Ltd. Updated with the latest data from the providers.

3. The bill acceptance business fell back, and bill financing business was generally stable with a slight shrinkage

The bill acceptance business declined. In H1 2023, commercial drafts issued by enterprises totaled RMB12.4 trillion, falling 11.7 percent year on year. At end-June, outstanding commercial drafts stood at RMB16.3 trillion, decreasing by 2.2 percent year on year. Outstanding commercial draft acceptances decreased. At end-June, outstanding commercial draft acceptances dropped by RMB403.3 billion from the end of March. Of the outstanding bankers' acceptances, 67.7 percent were issued by micro, small, and medium-sized enterprises (MSMEs). Supply chain bill business has been implemented. In H1, discount financing by enterprises amounted to RMB12.8 billion, effectively playing the role of bill business in serving the real economy.

Bill financing was generally stable, with a slight decline. In H1, total discounts by financial institutions amounted to RMB25.6 trillion, falling 11.3 percent year on year. At end-June, the balance of bill financing was RMB11.9 trillion, down 0.4 percent year on year. The balance accounted for 5.2 percent of the total outstanding loans, down 0.6 percentage points year on year. In Q2, the interest rates for bill financing went down.

4. The stock indices grew, with turnover and the amount of funds raised on the stock markets decreasing year on year

The stock indices witnessed a choppy rise. At the beginning of 2023, with the smooth transition of pandemic containment and the recovery of the economy, the stock market rebounded quickly, with both the Shanghai Stock Exchange Composite Index and the Shenzhen Stock Exchange Component Index. After March, the overall trend became volatile. At end-June, the Shanghai Stock Exchange Composite Index closed at 3,202 points, increasing by 3.7 percent from end-2022. The Shenzhen Stock Exchange Component Index closed at 11,027 points, increasing by 0.1 percent from end-2022. The turnover and the amount of funds raised on the stock markets declined year on year. In H1, the combined turnover on the Shanghai Stock Exchange and the Shenzhen Stock Exchange reached RMB111.5 trillion, and the average daily turnover was RMB944.6 billion, representing a decrease of 3.4 percent year on year. In H1, cumulative funds in the amount of RMB512 billion were raised, decreasing by 9.8 percent year on year.

5. Premium income increased year on year and the growth of assets accelerated

In H1 2023, total premium income in the insurance sector amounted to RMB3.2 trillion, up 12.5 percent year on year, an acceleration of 8 percentage points compared to that recorded in 2022. Claim and benefit payments totaled RMB915.1 billion, representing a year-on-year increase of 17.8 percent. Specifically, total property insurance claims and benefit payments increased by 17.1 percent year on year and total life insurance claims and benefit payments increased by 18.3 percent year on year.

Table 12 Asset Allocations in the Insurance Sector at End-June 2023

Units: RMB100 million, %

	Balance		As a share of total assets	
	End-June 2023	End-June 2022	End-June 2023	End-June 2022
Total assets	291,998	266,385	100.0	100.0
of which: Bank deposits	28,967	28,603	9.9	10.7
Investments	239,255	215,992	81.9	81.1

Source: National Administration of Financial Regulation.

The growth of assets in the insurance sector accelerated. At end-June 2023, total assets in the insurance sector increased 9.6 percent year on year to RMB29.2 trillion, an acceleration of 0.5 percentage points from end-2022. Specifically, bank deposits increased by 1.3 percent, while investment-linked assets increased by 10.8 percent year on year.

6. The turnover of spot foreign exchange transactions increased while that of forward transactions declined year on year

In H1 2023, the cumulative turnover of spot RMB/foreign exchange transactions registered USD4.9 trillion, an increase of 27.5 percent year on year. The cumulative turnover of swap RMB/foreign exchange transactions totaled USD9.8 trillion, a decrease of 0.5 percent year on year. Specifically, cumulative overnight RMB/USD swap transactions posted USD6.4 trillion, accounting for 65.6 percent of the total swap turnover. The turnover of RMB/foreign exchange forward transactions totaled USD48.4 billion, decreasing 28.3 percent year on year. The turnover of foreign currency pair transactions totaled USD823.3 billion, increasing by 19.1 percent year on year. In particular, the EUR/USD pair registered the largest trading volume, accounting for 39.4 percent of the total market share.

7. The volume of gold trading expanded year on year, while gold prices went up

At end-June 2023, international gold prices closed at USD1,912.3 per ounce, representing an increase of 5.5 percent from end-2022. The Au99.99 on the Shanghai Gold Exchange closed at RMB448.5 per gram, increasing by 9.3 percent from end-2022. In Q2 2023, the volume of gold traded on the Shanghai Gold Exchange was 10,000 tons, an increase of 0.5 percent year on year. The turnover posted RMB4.4 trillion, up 12.6 percent year on year.

II. The development of institutional arrangements in financial markets

1. Institutional arrangements in the bond market

The business of bond valuation in the interbank bond market was regulated. In June 2023, the PBOC released the *Measures for the Administration of Bond Valuation Business in the Interbank Bond Market (Exposure Draft)* for public comments. The Measures specifies requirements for valuation institutions, with respect to their internal governance, information disclosures and conflict of interest, as well as the general principles and methodologies for valuations. It aimed to make bond valuation more neutral, impartial, professional and transparent, to enhance the effectiveness of market pricing and market functions, and to prevent market risks.

The opening-up of the bond market at a high level will be steadily promoted. Under the guidance of PBOC, relevant financial infrastructure institutions implemented a package of measures to facilitate investment. First, foreign-funded institutions in China were included in the market makers for the Northbound Bond Connect. With the strong advantages of foreign market makers in regional overseas client resources and in cross-border service capabilities, the capability of serving overseas investors were improved. Second, the function of trading a basket of bond portfolio became available. It better met the needs of index investors, reduced the cost of inquiry when multiple bonds were transferred, and improved trading efficiency. Third, the reporting procedure for settlement failures in the Northbound Bond Connect was improved. After upgrading the infrastructure system, we enabled online one-stop reporting, thus greatly improving the convenience of investments. Fourth, connectivity and cooperation were enhanced between the interest rate swap markets of the mainland and Hong Kong. With connected infrastructures, overseas investors can enjoy a greater convenience in interest rate risk management.

2. Reform and institutional arrangements in the securities market

The legal system for the capital market was improved. In April 2023, the CSRC released the *Work Plan for Promoting the High-quality Development of Bonds of Scientific and Technological Innovation Companies*, covering such aspects as upgrading financing services, enhancing fund supply for sci-tech innovation, improving the liquidity of sci-tech innovation bonds, and optimizing the evaluation and assessment mechanism. The Work Plan aimed to establish a full-life-cycle bond financing support system for sci-tech innovation enterprises, improve the quality and efficiency of serving sci-tech innovation enterprises at a faster pace, and promote a virtuous cycle of science and technology, industry, and finance. On June 16, the State Council, at its 8th Executive Meeting, deliberated and passed the *Regulation on the Supervision and Administration of Private Investment Funds (Draft)*, which was officially released by the CSRC on July 9 and came into force on September 1. The Regulation clarified regulatory requirements for key entities, standardize the requirements for fund raising and filing, regulate investment business activities and market-based exit mechanisms, enrich the means of supervision during and after the event, bring all types of private equity funds under the rule of law and standardization, and further give play to the role of private equity investment funds in serving the real economy and promoting sci-tech innovation.

The two-way opening-up of the capital market was boosted. On May 16, the CSRC released the *Guidelines for the Application of Regulatory Rules – Overseas Offerings and Listings No. 6: Guidelines for the Overseas Offering of Global Depository Receipts by Domestic Listed Companies*. The Guidelines regulate the behavior of domestic listed companies issuing depository receipts that can be converted into domestic underlying shares and support domestic listed companies to make good use of two markets and two resources to meet their needs to develop overseas businesses.

3. Institutional arrangements in the insurance market

The actuarial system for agricultural insurance was improved. In April 2023, the former China Insurance and Banking Commission (CBIRC) released the *Actuarial Provisions for Agricultural Insurance (Trial)*. The Provisions clarify the actuarial rules for agricultural insurance, covering the rate structure, rate backdating, and assessment of the premium deficiency reserve. By specifying the use of benchmark pure risk loss rates, additional rates, and a rate adjustment coefficient, the Provisions enable management of the floating prices centering on risks for agricultural insurance. The floating range of the rate adjustment coefficient of financial subsidy products is limited to [0.75,1.25], and that of other products is limited to [0.5,1.5], so as to facilitate the stable and sustainable development of agricultural insurance. At the same time, the Provisions also clarifies the responsibilities of the chief actuary of the insurance company and the corresponding regulatory measures.

Part 4 Macroeconomic Overview

I. Global economic and financial developments

Recovery continued in the major economies, and inflation fell further in Europe and the U.S.. The labor market cooled marginally, but remains tight. It will take some time before inflation falls back to pre-pandemic levels. The advanced economies may be close to the end of this tightening cycle, and the global financial markets strengthened. However, the potential risks of rising uncertainties in monetary policy, persistently tighter global financial conditions, and escalating geopolitical tensions still merit attention.

1. Economic performance and financial markets in the major economies

Economic recovery continued. In the second quarter (Q2), real gross domestic product (GDP) increased at an annual rate of 2.4 percent in the U.S., slightly higher than the 2 percent in the first quarter (Q1), but still lower than the 2.6 percent in the fourth quarter (Q4) of last year. In June, the manufacturing Purchasing Managers' Index (PMI) was 46, staying below 50 for eight straight months. The GDP in the euro area grew by 0.6 percent year on year in Q2, slower than the 1.1 percent growth in Q1 and the 1.7 percent growth in Q4 of last year. The manufacturing PMI posted 43.4 in June, a reading that has been under 50 for 12 months in a row. In Japan, the GDP gained 2.0 percent year on year in Q2, the same as that in Q1, and the total output still has not returned to pre-pandemic levels.

Inflation has come down further in the U.S. and Europe. In June, the U.S. Consumer Price Index (CPI) was up by 3.0 percent year on year, falling for 12 months in a row, and the core CPI has eased from 5.6 percent in March to 4.8 percent. The

Harmonized Index of Consumer Prices (HICP) in the euro area rose by 5.5 percent over the prior year, far below the 6.9 percent in March, but the core HICP rebounded slightly compared with the increase in May and reached 5.5 percent. The CPI in the UK was up by 7.9 percent in June, a sharp decline from the over 10 percent increase in Q1, but remained at historic highs.

The labor market remained tight. From April to June, the U.S. jobless rate stayed between the record lows of 3.4 percent and 3.7 percent, indicating that the labor market is still hot. In June, nonfarm payrolls increased by 185 thousand, below the May's gain of 281 thousand. Job vacancies dropped from 10.32 million in April to 9.58 million, slightly below market expectation. The labor force participation rate has stayed at 62.6 percent for four consecutive months, still lower than the pre-pandemic average. The year-on-year growth of hourly wage for nonfarm workers moderated, hovering around 4.4 percent.

Global financial markets strengthened. The U.S. and European equity markets witnessed higher volatility after the collapse of some banks in March, and strengthened as market sentiments improved. In the first half of this year, the S&P 500 and EURO STOXX 50 increased by 15.9 percent and 16.0 percent, respectively, while the Nikkei 225 surged by 27.2 percent, making a new record high since 1990. The entrenched core inflation has cooled market expectations for a near-term pivot to easing in the major economies, and the bond yields went up. As of end-June, the yield on 10-year and 2-year U.S. Treasuries was 3.81 percent and 4.87 percent, respectively, up by 33 basis points (bps) and 81 bps compared with end-March. The U.S. dollar index fluctuated slightly above 100, rising by 0.8 percent from the end of March. The euro and British pound strengthened, appreciating by 0.7 percent and 3.0 percent against the U.S. dollar in Q2.

Table 13 Macroeconomic and Financial Indicators in the Major Advanced Economies

Economy	Indicator	Q2 2022			Q3 2022			Q4 2022			Q1 2023			Q2 2023		
		Apr.	May	Jun.	Jul.	Aug.	Sept.	Oct.	Nov.	Dec.	Jan.	Feb.	Mar.	Apr.	May	Jun.
United States	Real GDP Growth (annualized quarterly rate, %)	-0.6			3.2			2.6			2.0			2.4		
	Unemployment Rate (%)	3.6	3.6	3.6	3.5	3.7	3.5	3.7	3.6	3.5	3.4	3.6	3.5	3.4	3.7	3.6
	CPI (year-on-year, %)	8.3	8.6	9.1	8.5	8.3	8.2	7.7	7.1	6.5	6.4	6.0	5.0	4.9	4.0	3.0
	DJ Industrial Average (end of the period)	32977	32990	30775	32845	31510	28726	32733	34590	33147	34086	32657	33274	34098	32908	34408
Euro Area	Real GDP Growth (year-on-year, %)	4.2			2.4			1.7			1.1			0.6		
	Unemployment Rate (%)	6.7	6.7	6.7	6.7	6.7	6.7	6.7	6.7	6.7	6.7	6.6	6.5	6.4	6.4	6.4
	HICP (year-on-year, %)	7.4	8.1	8.6	8.9	9.1	9.9	10.6	10.1	9.2	8.6	8.5	6.9	7.0	6.1	5.5
	EURO STOXX 50 (end of the period)	3803	3789	3455	3683	3517	3318	3618	3936	3794	4165	4246	4376	4359	4218	4399
United Kingdom	Real GDP Growth (year-on year, %)	3.8			2.0			0.6			0.2			…		
	Unemployment Rate (%)	3.8	3.8	3.6	3.5	3.6	3.7	3.7	3.7	3.7	3.7	3.8	3.9	3.8	4.0	…
	CPI (year-on-year, %)	9.0	9.1	9.4	10.1	9.9	10.1	11.1	10.7	10.5	10.1	10.4	10.1	8.7	8.7	7.9
	FTSE 100 (end of the period)	7545	7608	7169	7423	7284	6894	7095	7573	7452	7772	7876	7632	7871	7446	7532
Japan	Real GDP Growth (annualized quarterly rate, %)	5.1			-1.2			0.2			3.7			6.0		
	Unemployment Rate (%)	2.5	2.6	2.6	2.6	2.5	2.6	2.6	2.5	2.5	2.4	2.6	2.8	2.6	2.6	2.5
	CPI (year-on-year, %)	2.5	2.5	2.4	2.6	3.0	3.0	3.7	3.8	4.0	4.3	3.3	3.2	3.5	3.2	3.3
	Nikkei 225 (end of the period)	26848	27280	26393	27802	28092	25937	27587	27969	26095	27327	27446	28041	28856	30888	33189

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

2. Monetary policies of the major economies

The central banks in the major advanced economies continued with monetary tightening, but at a slower pace. The Federal Reserve (Fed) raised rates in May by

25 bps, paused in June, and hiked again by 25 bps in July. The federal funds rate is now at a target range of 5.25-5.5 percent. Fed Chair Jerome Powell said the Fed would take a data-dependent approach in determining the extent to which additional policy firming may be appropriate. In the meantime, the Fed continued to shrink its balance sheet as planned. The European Central Bank (ECB) increased interest rates in May, June, and July each by 25 bps, bringing the interest rate on its main refinancing operations, marginal lending facility, and deposit facility to 4.25 percent, 4.5 percent, and 3.75 percent, respectively. The ECB started to shrink its balance sheet from early March by a monthly average amount of EUR15 billion until the end of June. In July, it ended the reinvestment of the principal payments from maturing securities under the Asset Purchase Program (APP). The Bank of England raised rates by 25 bps, 50 bps, and 25 bps in May, June, and August, respectively. Now, the Bank Rate is 5.25 percent. The Bank of Japan (BOJ) kept its short-term policy rate unchanged at -0.1 percent, and continued to allow 10-year Japanese government bond yields to fluctuate in the range of around plus and minus 0.5 percentage points from its 0 percent target level. In July, the BOJ decided to conduct yield curve control with greater flexibility, regarding the upper and lower bounds of the range as references, not as rigid limits, in its market operations, and will offer to purchase 10-year Japanese government bonds at 1.0 percent every business day through fixed-rate purchase operations. The Reserve Bank of Australia paused rate hikes in April, and raised rates in May and June by 50 bps cumulatively. The Bank of Canada raised rates by 25 bps in June after a pause in March and April. The Bank of Korea kept rates unchanged in Q2.

Monetary policies in emerging economies diverged. Some emerging economies continued to raise rates. In Q2, the central banks in Argentina, Turkey, South Africa, and Malaysia hiked rates by 1900 bps, 650 bps, 50 bps, and 25 bps, respectively, whereas those in India, Russia, Brazil, Mexico, and Indonesia stood pat on rates.

3. Issues and trends that merit attention

It takes more time for inflation to return to pre-pandemic levels. Inflationary pressures in the U.S. and Europe have eased, but prices fall relatively slowly. In June, the U.S. CPI fell to 3 percent mainly due to high base effects. The core inflation in the euro area proved quite sticky, as the core HICP hovered around 5.3-5.7 percent in the first six months of this year. The labor markets in the U.S. and Europe remain tight, and the unemployment rates are at record lows, which has supported rapid wage growth. Going forward, the journey to bring down inflation is likely to be tortuous.

Financial stability risks have increased. This year, the banking crisis in the U.S. and Europe, coupled with the risk of the U.S. government defaulting on its debt, has shocked global financial markets. The collapse of three U.S. regional banks and the crisis of the Credit Suisse have highlighted the challenges of tighter monetary and financial conditions. Despite timely and strong responses from the U.S. and European regulators to the banking crisis, and temporary solutions to the U.S. government debt ceiling, uncertainties and risk aversion remain in global financial markets. The revaluation of financial assets is still going on. The risk of tighter liquidity globally may have further spillovers to emerging market economies.

Economic outlook and monetary policy have become more uncertain. Some new complexities have emerged in the economic performance of the major economies since the beginning of this tightening cycle. Inflation falls slowly, while the labor market remains tight. Central banks would be happy to see economic and labor market resilience, but whether inflation will fall steadily is yet to be seen. A number of central banks, such as the Fed, the Bank of Canada, and the Reserve Bank of Australia all resumed rate hikes after a pause.

II. Macroeconomic developments in China

In H1, faced with the complex and severe international environment and the arduous tasks of domestic reform, development, and stability, all regions and departments earnestly implemented the strategic arrangements of the CPC Central Committee and the State Council and made coordinated efforts to put forth macro policies, placing an emphasis on stabilizing growth, employment, and prices. The national economy witnessed a continuous recovery and steadily turned toward high-quality development. Industrial upgrading underwent long-term accumulation, food and energy security were guaranteed effectively, and overall social stability remained. According to preliminary statistics, GDP in H1 grew by 5.5 percent year on year to RMB59.3034 trillion on a comparable basis. Specifically, GDP in Q2 grew by 6.3 percent year on year, an acceleration of 1.8 percentage points from Q1, thus laying a solid foundation for achieving the annual growth target.

1. Consumption recovered steadily, investments grew stably, and imports and exports maintained their growth

Residents' income grew steadily and consumption potential was gradually released. In H1, China's per capita disposable income reached RMB19672, increasing by 6.5 percent year on year in nominal terms, or 5.8 percent in real terms, an acceleration of 1.4 percentage points and 2.0 percentage points from Q1, respectively. The structure of income distribution continuously improved. The nominal and real growth rates of rural residents' income were 2.4 percentage points and 2.5 percentage points, respectively, which were higher than those of urban residents. In H1, total retail sales of consumer goods grew by 8.2 percent year on year, an acceleration of 2.4 percentage points from Q1. Consumption of basic living items saw stable growth, with retail sales of enterprises (units) above the designated size in terms of textile products, such as clothing, shoes, and hats, increasing by 12.8 percent and those in terms of grain, oil, and food increasing by 4.8 percent year on year. Sales of upgraded products increased fairly rapidly, with retail sales of gold/silver/jewelry, sports/entertainment products and cosmetics by enterprises (units) above the designated size increasing by 17.5 percent, 10.5 percent, and 8.6 percent, respectively. The recovery of service consumption accelerated, with domestic tourism revenue increasing by 95.9 percent year on year in H1. Institutions predicted that the heat of the summer tourism market this year would be higher than that over the same period for the past five years. According to the Urban Depositors' Survey conducted by the PBOC in Q2, 24.5 percent of residents were inclined to "consume more," up 1.2 percentage points from Q1.

Investments grew continuously and investments in the high-tech industry expanded rapidly. In H1, total fixed-asset investments throughout China (excluding those by rural households) increased by 3.8 percent year on year to RMB24.3113 trillion. In terms of sectors, investments in the manufacturing sector increased by 6.0 percent, 2.2 percentage points higher than the growth of total investments. Investments in infrastructure increased by 7.2 percent, 3.4 percentage points higher than the growth of total investments. Investments in real estate development decreased by 7.9 percent year on year. Investments in the high-tech industry grew by 12.5 percent year on year. Specifically, investments in the high-tech manufacturing industry and high-tech services industry grew by 11.8 percent and 13.9 percent, respectively. In the high-tech manufacturing industry, investments in the medical equipment/instrument manufacturing industry, and electronic and communication equipment manufacturing industry, increased by 16.8 percent and 14.2 percent, respectively, year on year. In the high-tech services industry, investments in professional technical service industry and science and technology achievements transformation service industry increased by 51.6 percent and 46.3 percent, year on year, respectively.

Imports and exports maintained growth, with the trade structure continuously improved. In H1, imports and exports of goods grew by 2.1 percent year on year to RMB20.1016 trillion. Specifically, exports grew by 3.7 percent year on year and imports fell by 0.1 percent year on year, with the trade surplus in goods posting RMB2.8159 trillion. The trade structure continued to improve. The share of imports and exports under general trade increased by 4.0 percent and accounted for 65.5 percent of total imports and exports, increasing by 1.2 percentage points year on year. Imports and exports of private enterprises increased by 8.9 percent, accounting for 52.7 percent of total imports and exports, increasing by 3.3 percentage points year on year. China's imports and exports with its trading partners continued to rise, with imports and exports to countries along the Belt and Road growing by 9.8 percent year on year.

Foreign direct investment (FDI) was basically stable and the quality of investments continued to improve. In H1, actually utilized FDI decreased by 2.7 percent year on year to RMB703.65 billion. The quality of investments continued to improve. Actually utilized FDI in the high-tech industries grew by 7.9 percent year on year, and that in the high-tech manufacturing industry increased by 28.8 percent year on year. The policies of an economy with a new height of openness has a significant driving effect, with 21 pilot free trade zones absorbing foreign investment increasing by 8.2 percent year on year to RMB129.66 billion.

2. Agricultural production was generally stable, industrial production recovered steadily, and the service industry grew rapidly

In H1, the value-added of the primary industry totaled RMB3.0416 trillion, up 3.7 percent year on year. The value-added of the secondary industry totaled RMB23.0682 trillion, up 4.3 percent year on year. The value-added of the tertiary industry totaled RMB33.1937 trillion, up 6.4 percent year on year.

Agricultural production was stable, and animal husbandry grew steadily. The output of summer grain saw another bumper harvest, with output achieving a second historic high. In H1, the output of pork, beef, lamb, and poultry grew by 3.6 percent year on year, and the output of pork specifically grew by 3.2 percent year on year. At end-June, the number of hogs in stock and the number of hogs for slaughter increased by 1.1 percent and 2.6 percent year on year, respectively.

Industrial production recovered steadily and the equipment manufacturing industry grew rapidly. In H1, the value-added of Industrial Enterprises Above a Designated Size (IEDS) increased by 3.8 percent year on year, an acceleration of 0.8 percentage points from Q1. Specifically, the value-added of the mining sector and of the manufacturing sector increased by 1.7 percent and 4.2 percent year on year, respectively. The electricity, heat, gas, and water production and supply sector increased by 4.1 percent year on year. In terms of enterprise types, the value-added of state-owned holding enterprises increased by 4.4 percent year on year and that of corporate enterprises increased by 4.4 percent year on year. In terms of products, the output of solar cells and new energy vehicles grew by 54.5 percent and 35.0 percent year on year, respectively. In June, the total profits of the IEDS decreased by 8.3 percent year on year, a deceleration of 10.9 percentage points from March.

The service industry grew rapidly, with significant improvements in the contact service industry. In H1, the value-added of the service industry grew by 6.4 percent year on year, an acceleration of 1.0 percentage point from Q1. Specifically, the value-added of accommodations and catering, electronic information transmission/software/information technology services, and the leasing/business services sectors grew by 15.5 percent, 12.9 percent, and 10.1 percent year on year, respectively. In June, the Index of Service Production (ISP) increased by 6.8 percent year on year, and the cumulative growth in H1 accelerated by 2 percentage points from Q1. Specifically, the ISP of accommodations and catering, electronic information transmission/software/information technology services, and the leasing/business services in June increased by 20.0 percent, 15.4 percent, and 9.3 percent year on year, respectively. The Business Activities Index for the services industry reached 52.8 percent in June. The revenue of enterprises above a designated size in the service industry increased by 8.5 percent from January to May, accelerating for three consecutive months.

3. Consumer prices remained at a low level, but the core CPI increased year on year.

Consumer prices remained at a low level. In H1, the CPI increased by 0.7 percent year on year, a deceleration of 0.6 percentage points from Q1. The CPI in April, May, and June increased by 0.1 percent, 0.2 percent, and 0.0 percent, respectively. Specifically, sufficient supply and weak demand led to a decline in prices of many fresh food products, and the price of pork stayed on a downward trend even as the decrease expanded. Compounded by the base effect, the year-on-year growth in food prices decreased by 1.2 percentage points from Q1. Service prices continued their recovery growth, but there was an expanded decrease in prices of industrial consumer goods such as fuel, transportation and communication equipment, and household appliances. The year-on-year growth in non-food prices decreased by 0.4 percentage points year on year. The year-on-year growth in core CPI (food and energy excluded) posted 0.7 percent, remaining within positive territory.

The year-on-year growth of producer prices continued to decelerate. Affected by the decline in energy prices, such as oil and coal, the high base effect, and weak demand in the real estate industry, the prices of products in downstream related industries continued to decrease. In H1, the Producer Price Index (PPI) decreased by 3.1 percent year on year, a deceleration of 1.5 percentage points from Q1. The decrease of PPI in April, May and June was 3.6 percent, 4.6 percent and 5.4 percent, respectively. In July, the PPI rebounded, with the year-on-year decrease narrowing by 4.4 percent. In H1, the Purchasing Price Index for Industrial Products (PPIRM) decreased 3.0 percent year on year, a deceleration of 2.2 percentage points from Q1. The Corporate Goods Price Index (CGPI) monitored by the PBOC decreased by 2.2 percent year on year, a deceleration of 1.6 percentage points from Q1 and 8.0 percentage points from H1 of 2022.

4. Fiscal revenue rose steadily and expenditures grew slightly.

In H1, revenue in the national general public budget posted RMB11.9 trillion, increasing 13.3 percent year on year. Specifically, central and local fiscal revenue increased by 13.1 percent and 13.5 percent, respectively. National tax revenue amounted to RMB9.9661 trillion, increasing 16.5 percent year on year. Specifically, the domestic value-added tax increased by 96.0 percent year on year. The consumption tax, the corporate income tax, and the personal income tax decreased by 13.4 percent, 5.4 percent, and 0.6 percent year on year, respectively. Non-tax revenue posted RMB1.9542 trillion, decreasing by 0.6 percent year on year.

In H1, expenditures in the national general public budget posted RMB13.4 trillion, increasing by 3.9 percent year on year. Specifically, expenditures in the central level general public budget and the local level general public budget increased by 6.6 percent and 3.5 percent year on year, respectively. In terms of the expenditure structure, expenditures related to housing, social security and employment, and health grew rapidly, witnessing a year-on-year increase of 8.5 percent, 7.9 percent, and 6.9 percent, respectively.

5. The employment situation remained generally stable

The surveyed urban unemployment rate continued to decline. In H1, 6.78 million people were newly employed in urban areas, and the surveyed urban unemployment rate averaged 5.3 percent, 0.2 percentage points lower than that in Q1. In June, the surveyed urban unemployment rate posted 5.2 percent, on par with the previous month. Specifically, the surveyed unemployment rate for the population between the ages of 25 and 59 posted 4.1 percent, 1.1 percentage points lower than the national surveyed urban unemployment rate. Due to the regular impact of the summer graduation season, the unemployment rate for the population between the ages of 16 and 24 posted 21.3 percent in June, increasing by 0.5 percentage point from last month, lower than the average over the same period in the past five years.

6. The balance of payments and the external debt

According to preliminary statistics, China's current account surplus registered USD146.8 billion in H1, accounting for 1.7 percent of the Gross Domestic Product (GDP) and remaining within a reasonable range. Specifically, according to the balance of payments statistics, trade in goods recorded a surplus of USD293.3 billion, ranking as the second highest over the same period of the previous years. Trade in services recorded a deficit of USD102.1 billion, gradually returning to normal. Cross-border capital flow under the capital and financial account generally remained stable. Specifically, the net outflow of overseas equity investment posted USD55.9 billion and net inflow of foreign equity investment in China posted USD32.3 billion. Foreign capital inflow into the domestic share market increased significantly, and the bond market resumed its trend of net inflow. By end-June 2023, foreign reserves stood at USD3.193 trillion, an increase of USD65.3 billion compared with those at end-2022. This was mainly due to the influence of factors such as currency conversions and changes in asset prices. Regarding the external debt, at end-March the balance of full-caliber foreign debt (denominated in both domestic and foreign currencies) posted USD2.4909 trillion. Specifically, the short-term external debt balance posted USD1.3997 trillion, accounting for 56 percent of the total external debt balance.

7. Analysis by sector

7.1 The real estate sector

In June, among 70 medium and large-sized cities nationwide, newly built and second-hand residential housing prices decreased by 0.4 percent and 2.8 percent year on year, down 1 percentage point and 0.1 percentage points from March, respectively. In H1, the total floor area of sold commercial housing decreased by 5.3 percent year on year. Housing sales increased by 1.1 percent year on year. Investments in real estate development decreased by 7.9 percent year on year. Specifically, investments in residential housing development decreased by 7.3 percent year on year.

Table 14 Floor Area of Newly Started, Under Construction, and Completed Real Estate Projects in H1 2023

	Floor area (100 million square meters)	YOY change (%)	Growth change from the previous quarter (percentage points)
Floor area of newly started real -estate projects	5.0	-24.3	-5.1
Floor area of real estate projects under construction	79.2	-6.6	-1.4
Floor area of completed real estate projects	3.4	19	4.3

Source: National Bureau of Statistics of China.

At end-June, outstanding real estate loans by major financial institutions (including foreign-funded financial institutions) grew by 0.5 percent year on year to RMB53.4 trillion. Specifically, outstanding individual housing loans fell by 0.7 percent year on year to RMB38.6 trillion. Outstanding housing development loans grew by 3.9 percent year on year to RMB9.8 trillion.

7.2 The new energy vehicle sector

Developing new energy vehicles (NEVs) is the path to building China into a world leader in the automobile industry and also a strategic measure for addressing climate change and promoting green development. In recent years, catalyzed by policies, technological progress and market demand, the NEV sector has made great achievements. **First, production and sales saw rapid growth.** According to the statistics of China Association of Automobile Manufacturers, production and sales of NEVs from January to June 2023 reached 3.788 million and 3.747 million, a year-on-year increase of 42.4 percent and 44.1 percent, respectively.

The market share of domestic NEVs recorded 28.3 percent. In 2022, China's NEV sales accounted for 65 percent of global sales, ranking the top in the world for eight consecutive years. **Second, exports maintained a strong growth momentum.** NEV exports grew by 1.6 times to 534,000, making China the world's largest car exporter in H1 2023, ahead of Japan. The share of domestic NEVs continued expanding in the international market, and Europe has become China's largest trading partner in NEV exports. **Third, the technique advanced rapidly.** The energy efficiency of pure electric passenger vehicles has been upgraded. The power of batteries is improving and the average driving range is expanding. According to statistics of the Ministry of Industry and Information Technology, the average driving range of China's domestic pure electric passenger vehicles in 2022 rose to 424 kilometers, up 9.0 percent year on year.

The fast-developing NEV sector is facing challenges. **First, innovation capabilities for core technologies is insufficient.** We still need to make breakthroughs in key technologies such as batteries, motors, and electronic controls, and the quality and safety of our products are yet to be further improved, which, to a certain extent, impairs the competitiveness of our NEVs. **Second, the industrial ecology is inadequate.** Domestic NEV manufacturers still fall behind world leaders in terms of quality management. The integrated development of automobile and auto part enterprises needs to be promoted whereby synergy among power battery and its upstream and downstream enterprises should be built up. Lack of high-quality capacity is prominent. **Third, infrastructure construction lags behind.** The car-to-charging pile ratio is approximately 2.5:1 in China. The gross charging facilities is insufficient to meet the growing needs. Meanwhile, charging piles are lacking in some places but are left idle in others. It is inconvenient for consumers to access, use, and pay for charging.

Second, we will encourage cross-sector synergy among enterprises in the fields of NEVs, energy, transportation and information communication, bring into full play the role of industry-leading enterprises, and upgrade industrial chain modernization. Third, we will promote the construction of battery charging and swapping network, expedite the construction of battery charging and swapping infrastructure, and improve the services of battery charging infrastructure.

Part 5. Monetary Policy Outlook

I. Outlook for the Chinese economy

The national economy is expected to improve continuously. Currently, more bright spots are emerging in China's economic development. Corporate production sentiment is improving and in June and July consecutively the manufacturing

Purchasing Managers' Index (PMI) rebounded. Due to effective policy support, market demand is recovering, with summer travel growth surging as shown by the number of hotel and flight reservations. There are well-grounded reasons for the continuous recovery of the Chinese economy in the second half of the year. First, the economy is cycling increasingly smoothly. With the rebound in income growth and the improvement in the consumer environment, rising consumption will turn into more income for both businesses and individuals, further enhancing the consumption potential and producing positive feedback to help expand domestic demand. Second, the new drivers for growth are gaining steam. Investments in sectors such as new energy and high-tech services saw double-digit growth in the January–June period, while production and sales in these sectors are expected to maintain rapid growth. Third, the policy effects will continue to materialize. Fund injections that have been made via policy-backed and development-oriented financial instruments will continue to be a driving force for delivering concrete progress, while infrastructure investment consistently underpins economic growth. Moreover, with the fast growth in money and credit, China has an appropriate monetary and financial environment. Overall, the Chinese economy is expected to continue getting back on track for normal operations and the major indicators will stay within an appropriate range.

Currently, the external environment is severe and complicated, while domestic economic operations are facing new difficulties and challenges. From an international perspective, geopolitical tensions remain high, mounting risks of de-globalization are weighing on the world economy, and the cumulative effect of this round of interest rate hikes by the advanced economies will continue to play out to influence the global economic and financial situations. From a domestic perspective, income expectations are still unstable, the recovery of consumption will take time, and private capital lacks confidence in investments. Furthermore, some enterprises are having a hard time, there are production lines moving out in some industries, and local governments are under greater pressure to achieve a fiscal balance. **Nevertheless, it should be noted that the Chinese economy has strong resilience and a huge potential for development. The fundamentals for China's sound economic growth over the long run remain unchanged.** Economic recovery calls for patience and confidence as it is a process of wave-like development and zigzag progress. We should continue to deepen reform and opening-up across the board and focus on expanding domestic demand, boosting confidence, and preventing risks so that China's economic performance will achieve sustained improvement.

Prices are expected to bounce up. In the first half of the year, price rises in China slowed down amid fluctuations. While the CPI came in flat in June compared with the same period of the last year, the July CPI saw –0.3 percent growth year on year, a temporary phenomenon mainly caused by the base effect as well as the time lag in the recovery of demand. Currently, there is no deflation in China as the macro economy is witnessing a steady recovery and broad money supply is maintaining rapid growth, a situation notably different from typical historic cases of deflation. Furthermore, there will not be any deflationary risks in the second half of the year. Contributing factors are increasing further to bring about improvements in supply and demand, income growth continues to recover, people's willingness to consume is on the rise, and both the consumption of big-ticket items and that of services are picking up. Overall, there is a high possibility that the pace of price rises has hit a yearly low. With pork prices recently beginning to rebound, travel prices climbing much higher, and China's refined oil prices seeing their fourth consecutive upward adjustment, the CPI is expected to start a gradual rebound in August and exhibit a U-shaped trend for the year. Having shown an improvement on a year-on-year basis in July, the Producer Price Index (PPI) will likely decline at a slower pace in the future. From a medium- to long-term perspective, supply and demand in the Chinese economy will be generally balanced, China will continue to pursue a sound monetary policy and inflation expectations will remain stable. Therefore, there is no basis for long-term deflation or inflation in China.

II. Outlook for monetary policy in the next stage

Guided by Xi Jinping Thought on Socialism with Chinese Characteristics for a New Era, the PBOC will thoroughly implement the guidelines of the 20th CPC National Congress and the Central Economic Work Conference. Upholding the general principle of pursuing progress while ensuring stability, it will apply the new development philosophy fully, faithfully, and comprehensively, and it will play its part in accelerating the building of a new development paradigm. It will deepen the reform and opening-up, integrate implementation of the strategy to expand domestic demand with efforts to deepen the supply-side structural reform, and strengthen macro-policy adjustments. Also, by developing a modern central banking system and fully exploring the efficacy of monetary and credit policies, the PBOC will continue its efforts to achieve better economic performance, enhanced endogenous forces, and improved social expectations as well as resolution of existing and potential risks so as to help effectively upgrade and appropriately expand economic output.

The PBOC will pursue a sound monetary policy in a targeted and effective manner, and it will give better play to the role of monetary policy instruments in adjusting both the aggregate and the structure so as to provide solid support for recovery and development of the real economy. Using a mix of monetary policy instruments, it will keep liquidity adequate at a reasonable level, and it will ensure that the growth rates of M2 and the AFRE continue to be basically in line with nominal economic growth. It will continue to deepen the market-oriented interest rate reform, optimize the central bank policy rate system, unleash the potential of the LPR reform, and give play to the important role of the mechanism for market-oriented deposit rate adjustments so as to ensure that the financing costs for businesses and the borrowing costs for residents remain stable with a slight decline. The structural monetary policy instruments will be targeted, appropriate, and flexible. Support will be continuously enhanced for MSBs, sci-tech innovation, and green development. Considering the great changes in supply and demand relations, the real estate policies will be adjusted and improved as appropriate to promote steady and sound development of the market. Maintaining the positive role of finance in promoting consumption, stabilizing investment, and expanding domestic demand, the PBOC will work to keep prices basically stable. Pursuing a managed floating exchange rate regime based on market supply and demand with reference to a basket of currencies, it will stabilize expectations with a mix of policies to keep the RMB exchange rate basically stable at an adaptive and equilibrium level and to firmly guard against risks arising from exchange rate overshooting. The PBOC will prevent and resolve financial risks in key areas, coordinate efforts to resolve local debt risks with financial support, and steadily promote risk alleviation for small and medium-sized financial institutions through reforms, thereby firmly defending the bottom line whereby no systemic financial risks will occur.

First, the PBOC will maintain appropriate aggregates and a steady pace in the supply of money and credit. By using a mix of monetary policy tools, the PBOC will keep liquidity adequate at a reasonable level. It will support efforts by financial institutions to meet the effective financing needs of the real economy based on market principles and the rule of law. Meanwhile, it will make the growth of credit aggregates more stable and sustainable to ensure that the growth rates of money supply and aggregate financing to the real economy (AFRE) continue to be basically in line with nominal economic growth. Moreover, it will put emphasis on raising the quality and efficiency of the monetary and credit support provided to boost recovery of the real economy. Watching closely on the monetary policy shifts of the major central banks, the PBOC will strengthen monitoring and analysis of liquidity conditions and financial market movements. By doing so, it will conduct open market operations in a flexible manner to keep liquidity in the banking system stable and to maintain the stable movement of money market rates.

Second, the PBOC will use structural monetary policy tools in a targeted, appropriate, and flexible manner. It will keep central bank lending and discount policies stable to continue providing inclusive and sustainable funding support for agro-related businesses, MSBs, and private enterprises. It will effectively implement the inclusive MSB lending facility and keep up financial support for MSBs to bolster the efforts aimed at stabilizing businesses and securing employment. It will continue to implement the carbon emission reduction facility and the special central bank lending facility for clean and efficient use of coal. These facilities encourage eligible financial institutions to provide funding at preferential interest rates for key projects that significantly reduce carbon emissions and for clean and efficient use of coal and coal-fired power, thereby supporting a green and low-carbon economic transition premised on the security of energy supplies. Additionally, the PBOC will put into practice the action plan for supporting the financing of sci-tech enterprises. It will consolidate the guiding role of the central bank lending policy for sci-tech innovation to further improve the willingness and capacity of financial institutions to provide services for sci-tech enterprises. Furthermore, it will continue to implement the special central bank lending facility for inclusive elderly care services to support ramping up such services. For those fields where structural problems are still prominent, the expiration dates of the policy tools may be extended while new tools may be launched if necessary.

Third, the PBOC will build the systems and mechanisms needed to provide effective financial support for the real economy. By making solid efforts to assess the effectiveness of implementation of MSB credit policies, the PBOC will guide financial institutions to optimize resource allocations as well as internal policy arrangements and to step up the use of sci-tech approaches. These measures are aimed at accelerating the establishment of long-term mechanisms for boosting their confidence, willingness, capacity, and professionalism to provide financial services for MSBs, increasing the availability of financing to MSBs, and making the process more convenient. Moreover, the PBOC will guide financial institutions to accelerate implementation of the *Guiding Opinions on Providing Financial Support for Advancing Rural Revitalization Across the Board and Stepping Up Efforts to Build Up China's Strength in Agriculture*. They will be encouraged to launch innovative financial products and services and further enhance their capacity to provide financial services to better meet the diverse financing needs of agro-related sectors, thereby playing their part in advancing rural revitalization across the board and stepping up efforts to build up China's strength in agriculture. With effective implementation of the “16 financial measures,” the PBOC will keep real estate financing stable and in order while increasing financial support for rental housing, the rebuilding of run-down urban areas, and the construction of government-subsidized housing. The expiration date of the loan support scheme for timely deliveries of pre-sold housing projects has been extended to end-May 2024. Meanwhile, work is steadily underway to implement the loan support scheme for rental housing in pilot cities. The PBOC will adopt city-specific measures and make effective use of policy tools to meet the rigid demand for housing and the needs to improve living conditions. It will take concrete steps to ensure timely deliveries of pre-sold housing projects, to secure the people’s livelihood, and to maintain stability, with a view to promoting the stable and sound development of the real estate market.

Fourth, the PBOC will deepen the market-oriented interest rate and exchange rate reforms, and it will focus on domestic conditions while balancing internal

and external equilibria. Continuing to advance the market-oriented interest rate reform, the PBOC will optimize the central bank policy rate system and improve the market-oriented interest rate formation and transmission mechanism. At the same time, it will continuously tap into the loan prime rate (LPR) reform, bring into play the important role of the mechanism for market-oriented deposit rate adjustments, and adopt multiple measures to stabilize and bring down the overall financing costs for businesses and the costs of credit for individuals. Taking steady steps to deepen the market-oriented exchange rate reform, the PBOC will improve the managed floating exchange rate regime that is based on market supply and demand with reference to a basket of currencies. Letting the market play a decisive role in the formation of exchange rates, it will give play to the role of the exchange rate as an automatic stabilizer for the macro economy and the balance of payments. Furthermore, it will strengthen expectation management, uphold bottom-line thinking, duly conduct monitoring and analysis of cross-border capital flows, and stress risk prevention. The PBOC will rectify pro-cyclical, one-sided conduct in the market when necessary and firmly prevent the risks of exchange rate overshooting so as to keep the RMB exchange rate basically stable at an adaptive and equilibrium level. In addition, it 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 of exchange rate risk hedging for micro, small, and medium-sized enterprises with authentic needs based on a risk-neutral concept, thereby maintaining the stable and sound development of the foreign exchange market.

Fifth, the PBOC will make continued efforts to deepen the financial reforms. It will improve the legal system for the bond market and consolidate the legal basis for corporate credit bonds. Meanwhile, it will push ahead with the measures to expand the coverage and scale of the support instrument for bond financing of private enterprises (the so-called "second arrow") in order to intensify the support of the bond market for the real economy. By further regulating bond underwriting and improving bond market-making, the PBOC will enhance the synergy between the primary and secondary markets as well as the effectiveness of bond pricing and its function as a transmission channel. Additionally, it will speed up development of the over-the-counter bond business and guide the market to be properly tiered so that the interbank bond market will operate more efficiently and its infrastructures will offer diversified services. Adhering to market principles and the rule of law, the PBOC will continue to adopt a zero-tolerance approach and step up efforts to crack down on illegal and irregular conduct in the bond market. At the same time, it will remain firmly committed to advancing the opening-up of the bond market. Moreover, the PBOC will advance RMB internationalization in an orderly manner. It will further expand use of the RMB in cross-border trade and investment, deepen international monetary and financial cooperation, and promote development of offshore RMB markets. It will steadily move ahead with the convertibility of the RMB under the capital account and the institutional opening-up of financial markets.

Sixth, the PBOC will work relentlessly to forestall and defuse risks. Further steps will be taken to improve the macro-prudential policy framework as well as the capacity for systemic risk monitoring, assessment, and early warning. It will also enrich the macro-prudential policy tools and steadily expand the coverage of the macro-prudential policy. The PBOC will improve regulation of systemically important financial institutions. It will urge systemically important banks to meet the additional regulatory requirements as scheduled and to enhance the sustainability of their support for the real economy. Additionally, it will push for introduction of measures for the assessment of systemically important insurance companies and work on the drafting of additional regulatory requirements for them. It will also pick up pace in pushing China's global systemically important banks to establish and improve their total loss-absorbing capacity so as to effectively enhance their risk prevention ability. While keeping a close watch on risks in key fields, the PBOC will coordinate the efforts to provide financial support for the mitigation of local debt risks, and it will steadily advance reform of the high-risk small and medium-sized financial institutions to defuse their risks. Continuing to follow the principles of "maintaining overall stability, taking a coordinated approach, adopting differentiated measures, and defusing bombs with precision," it will safeguard security in the pursuit of development and ensure that all concerned parties fulfill their respective responsibilities for the resolution of financial risks. It will reduce existing risks and strictly guard against emerging risks. To reinforce the system that safeguards financial stability, the PBOC will improve legislation on financial stability and the regulations of the Financial Stability Fund. It will continue to improve the framework for the monitoring and assessment of financial stability and to optimize the frameworks for central bank rating, monitoring and early warning, and stress testing. All these efforts are aimed at effectively preventing the buildup and spread of financial risks.