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China Policy

China’s policy outlook after the tariff shock

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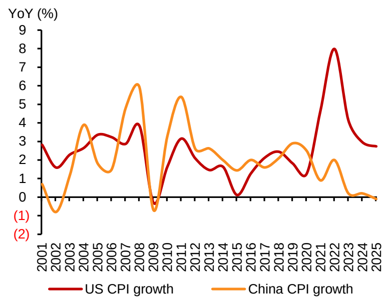
The Politburo held a meeting last Friday (25 Apr), calling for solid efforts to deal with the uncertainties caused by the US tariff shock. The meeting indicates that China will not succumb to US pressure as it prepares for a prolonged Sino-US conflict. Policymakers' planned measures for 2Q25 include a mild cut in RRR and LPRs, speeding up government bond issuance and fiscal spending, targeting employment support, especially in affected sectors, expanding the trade-in subsidy to include more durable goods, accelerating the AI+ initiative, opening up the service sector, strengthening trade ties with non-US economies, supporting companies to go global, stabilising the housing market and stimulating the capital market. The policy plan for 2Q25 seems conservative, as the policymakers need more time to observe and assess the dynamics of the Trump shock and its impact on China's economic growth. Policymakers may turn to aggressive fiscal stimulus to boost consumption in 2H25, as exports continue to slow while durable sales start to lose momentum. Keeping RMB and stock markets relatively stable might be a key target for China in struggling with the US.

- **Politburo meeting outlines policy plan for 2Q25**. Policymakers have stressed the need to coordinate domestic economic work with global economic wars, indicating that China will not bow to US pressure as it prepares for a prolonged Sino-US conflict in the future. The Politburo proposed seven aspects of policy in 2Q25 to counter the tariff shock. First, additional cuts in RRR and LPR. We expect the PBOC to cut RRR and LPRs slightly in 2Q25. For the full year, we expect RRR and LPRs to be cut by 50bps and 20bps, respectively. Second, government bond issuance and fiscal spending will be accelerated to provide more support to the real economy. Policymakers do not intend to increase the broad fiscal deficit this year, at least in 2Q25. They may turn to aggressive fiscal stimulus to boost consumption in 2H25 after goods exports continue to slow down while durable sales start to lose momentum. Third, raise incomes of middle and low-income groups by increasing the allocation of unemployment insurance refunds to firms affected by tariffs to stabilise employment, improving credit support for elderly care and other labour-intensive services, and expanding the coverage of "trade-in" subsidies for durable goods. Fourth, cultivate new pillar industries by introducing a "sci-tech board" in the bond market and speeding up the implementation of the AI+ initiative. Fifth, promote the construction of a unified national market, intensify pilot policies for opening up services, and support enterprises to go global. Sixth, strengthen the recovery of the housing market and reinvigorate the momentum of the stock market. Last but not least, strengthen trade relations with non-U.S. economies and collaborate to counteract unilateral bullying.
- **The tariff shock in 2025 is more severe than the US-China trade war in 2018.** According to our estimate, Trump's current tariffs would reduce the annualised GDP growth rates of the world, the US, China and Eurozone by 0.9ppts, 1.2ppts, 1ppt and 0.5ppts, respectively, while the 2018 Sino-US trade war is estimated to have reduced their GDP growth rates by 0.5ppts, 0.4ppts, 0.6ppts and 0.7ppts. However, the MSCI World equity index fell less in the 2025 tariff shock than in the 2018 Sino-US trade war, as other international currencies appreciated sharply after the former shock, while they depreciated after the latter shock. The short-term impact of the 2025 tariff shock should be much smaller than the 2022 recession panic, the 2020 pandemic and the 2008 financial crisis, as the latter three shocks were estimated to reduce global GDP growth by 1.9ppts, 5.5ppts and 5.0ppts,

Source: Wind, CMBIGM

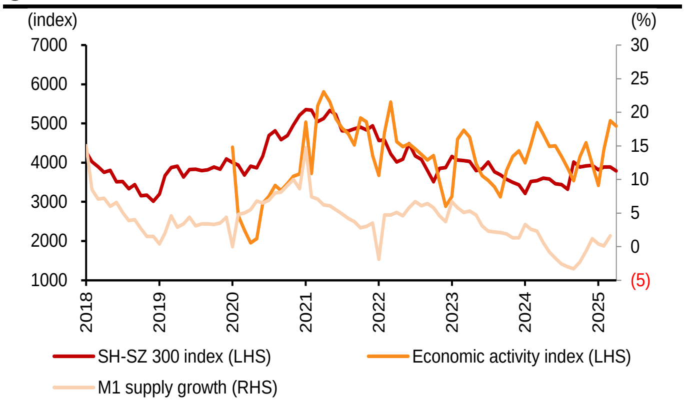


Source: Wind, CMBIGM

respectively. The MSCI World Index declined by 16.3% in 2025 tariff shock while dropping by 59.6%, 33.9% and 27.4% from the peak before the shock to the trough after the 2018 financial crisis, 2020 pandemic and 2022 recession panic. However, the 2025 tariff shock could have a long-lasting impact on the global economic landscape, trade flows and geopolitics in the future.

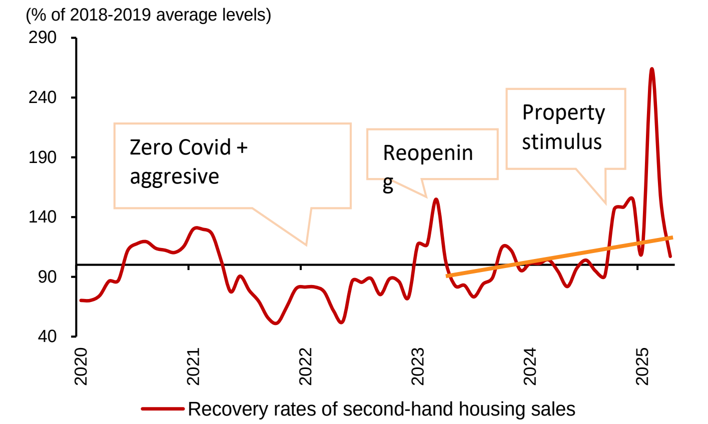
- **RMB and the stock markets could be important battlegrounds in the US-China confrontation.** The White House chose to use very high tariffs to pressure China with a view that the tariffs will crush China's economy and trigger a sharp fall in the RMB exchange rates and Chinese stocks, leading to a confidence crisis in the financial system, while a depreciation of RMB exchange rate will also help the cost of the tariffs to be borne more by Chinese exporters, reducing the inflationary pressure on the US. China has chosen to use very high retaliatory tariffs to prove to the US its determination to fight bravely, while it will endeavour to keep the RMB exchange rate and the stock market stable, support confidence in the financial markets, and increase the transmission of tariff costs to US inflation, thus letting the US back off.

Figure 1: Equity index, economic activity and M1 growth



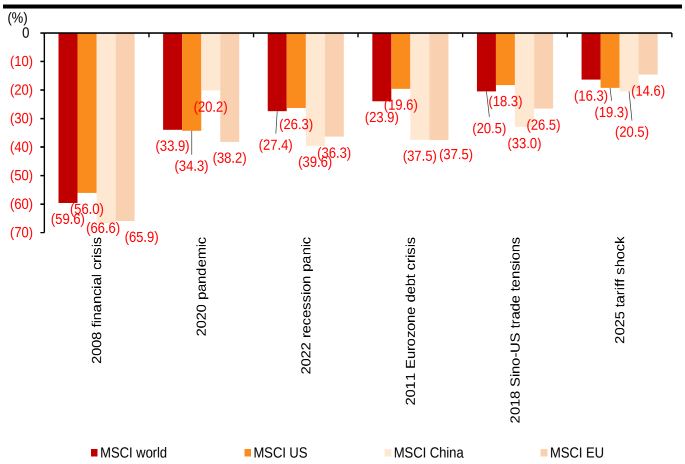
Source: Wind, CMBIGM

Figure 2: Recovery rates of second-hand housing sales



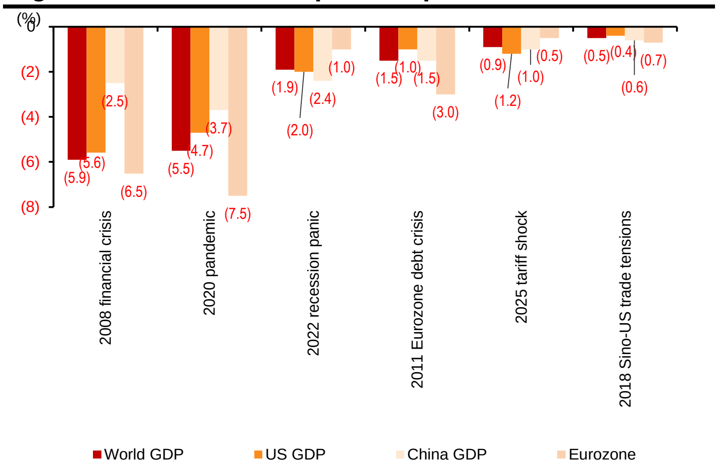
Source: Wind, CMBIGM

Figure 3: Global stock performance in previous shocks



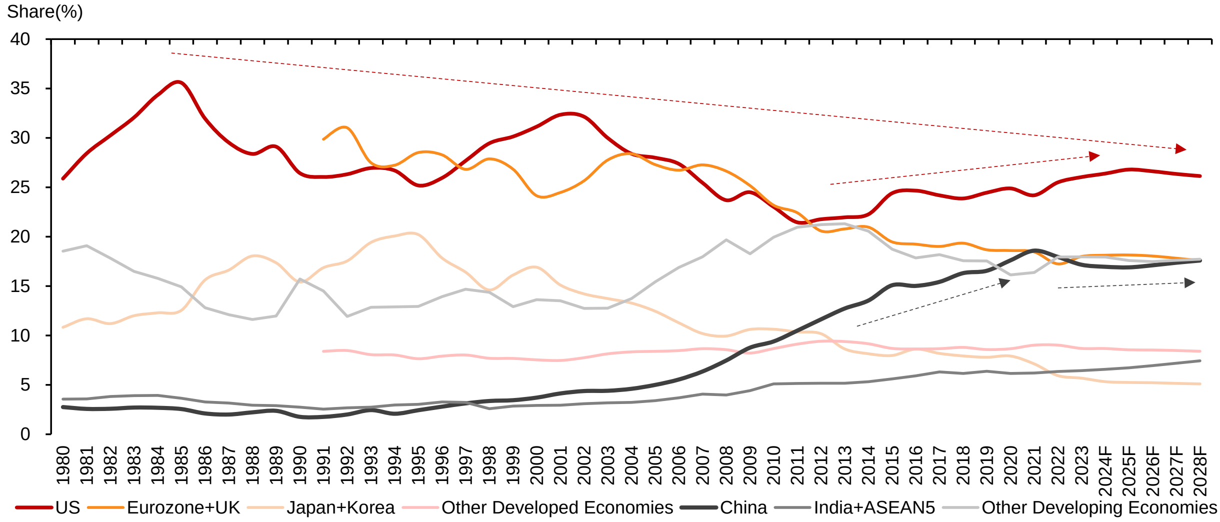
Source: Wind, CMBIGM

Figure 4: Global GDP impacts in previous shocks



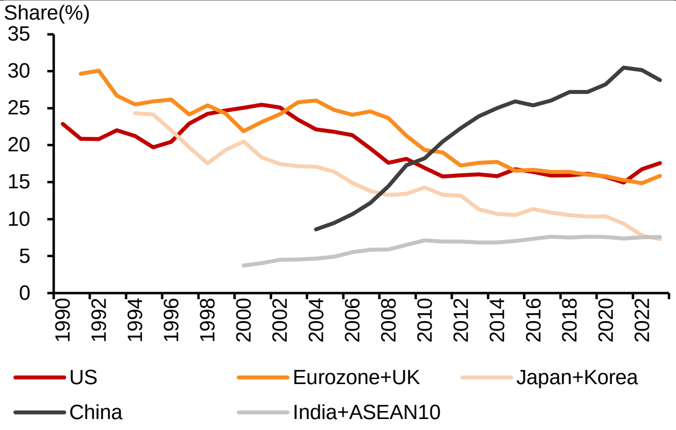
Source: Wind, CMBIGM

Figure 5: Share of major economics in global GDP



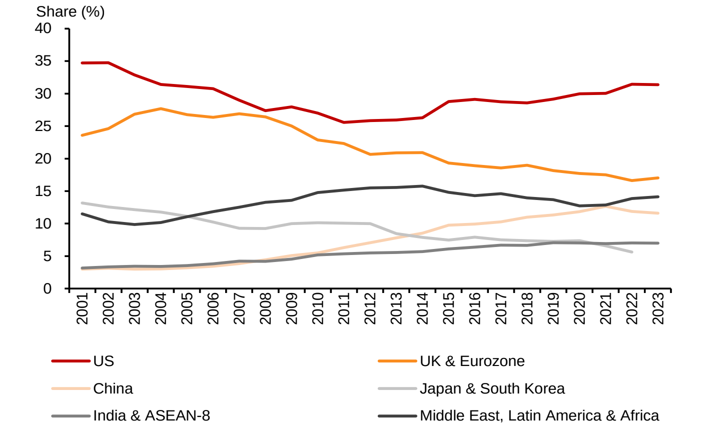
Source: Wind, CMBIGM estimates

Figure 6: Shares of major economies in global manufacturing GDP



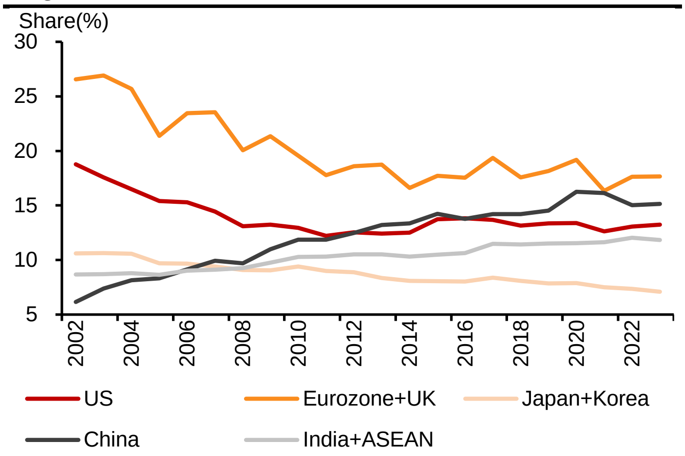
Source: Wind, CMBIGM

Figure 7: Shares of major economies in global household consumption



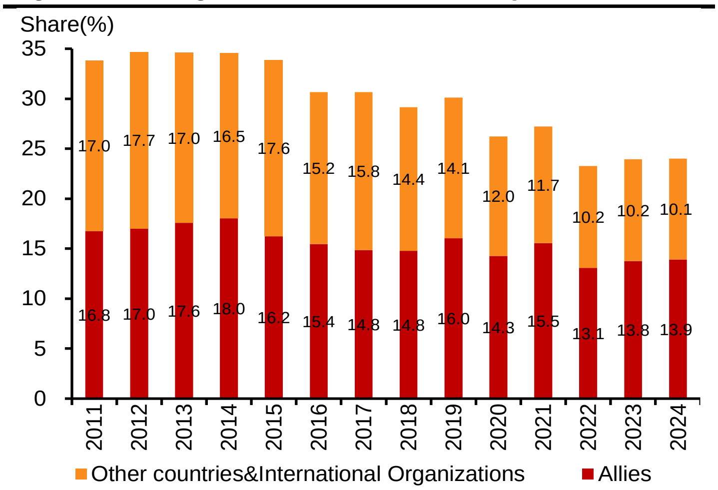
Source: Wind, CMBIGM

Figure 8: Shares of major economies in global trade of goods



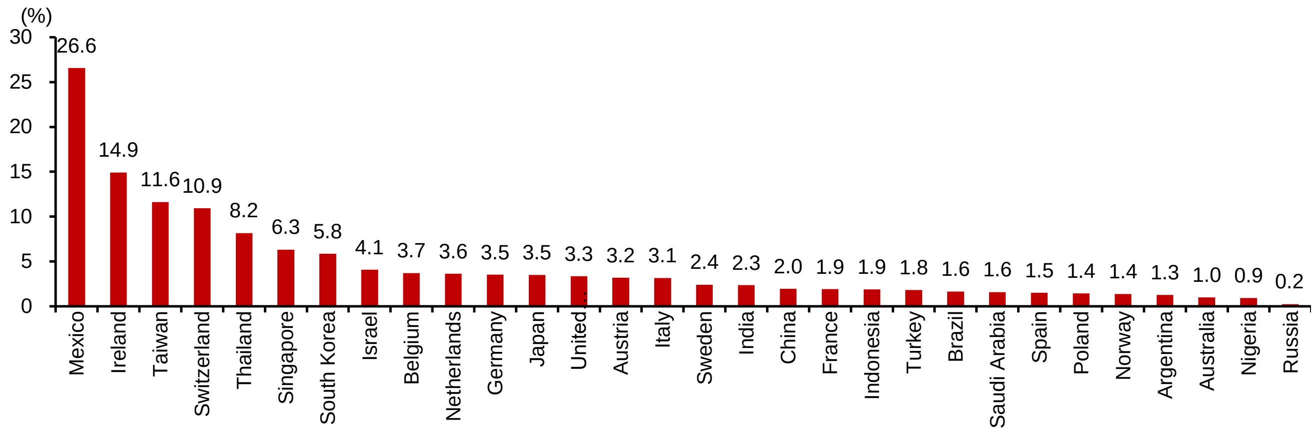
Source: Wind, CMBIGM

Figure 9: Foreign holders of US Treasury



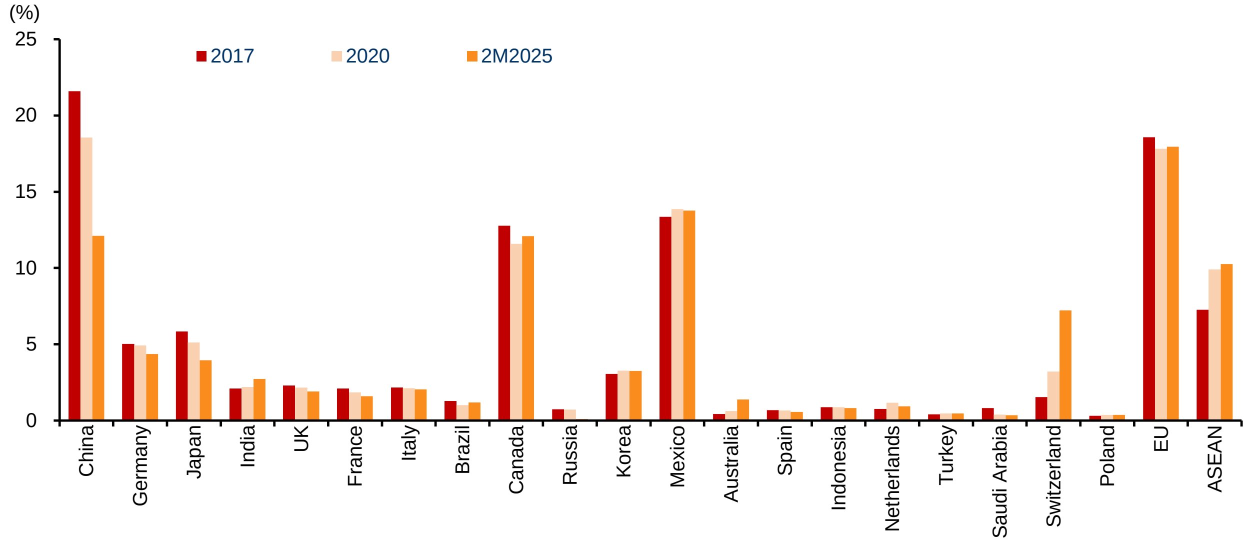
Source: Wind, CMBIGM

Figure 10: Exports of goods to US as % of GDP in 2023



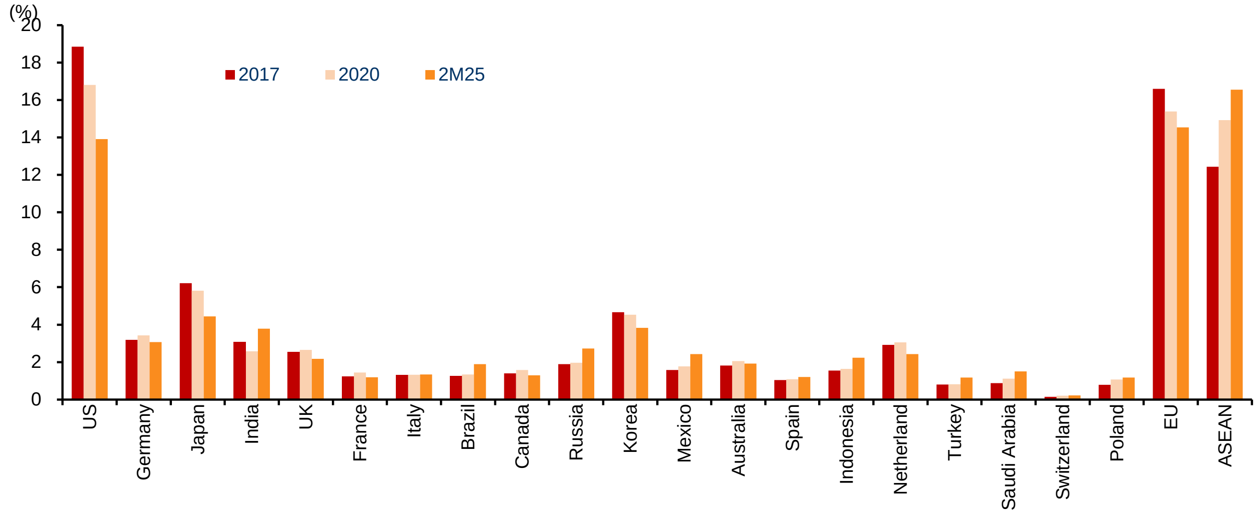
Source: Wind, CMBIGM estimates

Figure 11: Shares of US goods imports by major economies



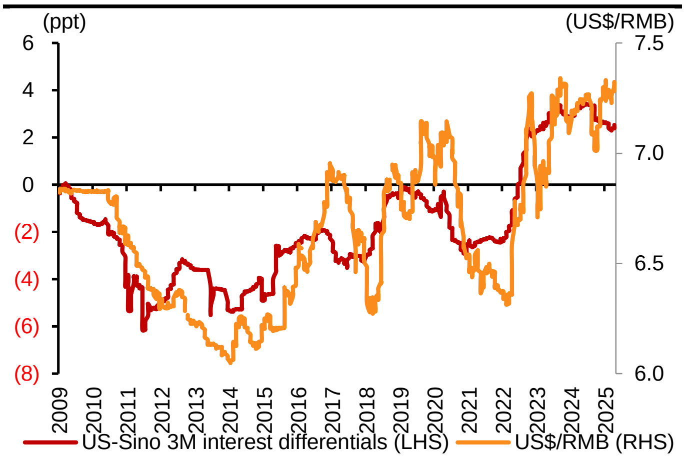
Source: Wind, CMBIGM

Figure 12: Shares of US goods imports by major economies



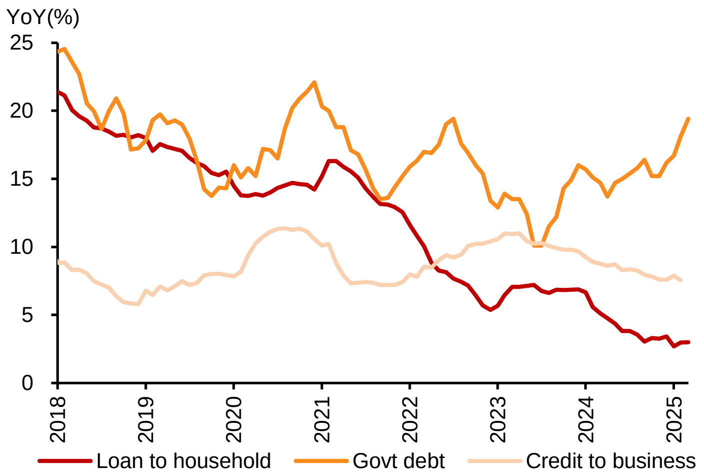
Source: Wind, CMBIGM

Figure 13: US-CN 3M yield spread & USD/RMB spot rate



Source: Wind, CMBIGM

Figure 14: Loans to real economy sectors in China



Source: Wind, CMBIGM

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