Political Transition Will Override China's Policy Targets

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On 5 March, Chinese Premier Li Keqiang presented the government's work reports for 2017 at the annual meeting of China's National People's Congress (NPC), the country's rubber stamp legislature. This year, the government's message was crystal clear: Economic growth is set to slow, the credit binge is well and truly over, and 'blue skies' will be restored. Or was it?

Leeway on economic growth

At first glance, the report is all about slower economic growth and tighter fiscal policies. But on closer scrutiny, it also leaves enough room for the government to step in and support growth, should the economy falter.

Much attention has been paid to the GDP growth target, which was set at 'around 6.5%', compared to 'between 6.5-7%' in 2016. But on closer scrutiny, the work report gives the government enough leeway to support economic growth should it need to do so. For instance, after setting the GDP growth target, Premier Li Keqiang also stated that higher growth should be sought. And while the fiscal deficit-to-GDP ratio is set to remain at 3%, according to the government, in absolute terms it will still widen slightly, to RMB2.38 trillion ($340 billion), compared to the targeted RMB2.18 trillion in 2016, and may well be even higher given that in 2016 the actual deficit-to-GDP ratio reached 3.8%.

Clearly, the Communist Party congress in the autumn, where President Xi Jinping will have the opportunity to consolidate his influence by appointing allies to the Politburo, remains the most important event this year, and the government wants to ensure everything is running smoothly as it approaches. Even though Beijing wants to signal that it is acutely aware of the systemic risks and will act to tackle them, the priority remains preventing the economy from decelerating too quickly.

Clean air at the mercy of politics

The government's work report also highlighted the need to tackle pollution and promote energy efficiency, with Premier Li pledging to 'make our skies blue again'. But despite talking tough about pollution, restrictions on coal output could end up being lighter than in 2016.

Beijing plans to cut coal capacity by 150 million tonnes this year, with the National Development and Reform Commission (NDRC) further pledging to shut down or stop construction of 50 gigawatts of coal-fired power plants as well as to reduce energy consumption per unit of GDP by 3.4%. Yet these goals are much less ambitious than last year, when China shuttered 290 million tonnes of outdated coal capacity. Of course, the large shutdowns of 2016, which led to a 9% year-on-year decline in production, also brought about a 66% surge in coal prices, which in turn led the government to ease mining restrictions. This year, even though air quality is a top concern, the priority for Beijing will be first and foremost to keep coal prices stable, a fact that the NDRC has also tacitly acknowledged.

To be sure, if the economy chugs along smoothly enough, and the political jockeying for top spots does not lead to friction, the government will look to address the deteriorating air quality. New regulations could be introduced later in the year to further cut coal production and use. Already the Ministry of Environmental Protection has reportedly circulated a draft regulation that would ban coal trucking at the port of Tianjin, China's second-largest coal trading hub. By September, ports in Hebei province would not be allowed to use trucks to carry coal from railways to ships.

But needless to say, the draft plan may still be watered down after consultation with various ministries and industrial groups. And for all of the government's pledges at the NPC, only one thing really matters this year, and that's the political transition.

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