

# China Economy

## Tentative signs of stability with property as major drag

China's economy showed tentative signs of stabilisation in August as retail sales, industrial output and service activity rebounded noticeably and beat expectations. Other evidences included better-than-expected new loans, less YoY declines of exports & imports and easing deflationary pressure. However, real estate sector remained major drag on the economy as property sales and development investment further tumbled. The policymakers showed a more pro-growth stance from July with cuts in stock trading tax, LPR, down-payment ratios & interest rates for first-home and second-home mortgages, existing mortgage rates and RRR. But it needs more policy support and longer time to restore confidence and sustain growth momentum. The PBOC may continue to expand credit supply with additional cuts on deposit rates, LPRs & RRR while municipal governments will further loosen property policies in next several quarters. The central bank may use special lending facility to support policy banks to make special low cost loans to the inner-city renewal projects. Meanwhile, the MoF may raise broad fiscal deficit ratio for next year to support the growth. The latest policy easing cycle may become the strongest one since 2017. China's economy may gradually improve in next four quarters as the GDP growth is expected to reach 5.1% in 2023 and 4.8% in 2024.

- Property sector remained in deep contraction with mild improvement in second-hand housing market sentiment.** The gross floor area (GFA) sold and the GFA started for commodity buildings respectively dropped 7.1% and 24.4% YoY (all in YoY terms unless specified) in 8M23 after decreasing 6.5% and 24.5% in 7M23. Property development investment further declined 8.8% in 8M23 after dropping 8.5% in 7M23. 30 major cities continued to see declining recovery ratio of commercial housing unit sales compared to the same period in 2019. But the recovery ratio of second-hand housing unit sales in 11 major cities improved in August and the first half of September, probably thanks to the latest property policy and credit supply loosening. Breaking down the funding source for property development investment, deposit & advance payment and individual mortgage fund both further dropped 7.3% and 4.3% in 8M23 after falling 3.8% and 1% respectively in 7M23. Meanwhile, domestic loan fund further declined 12.8% in 8M23 after dropping 11.5% in 7M23. Potential housing supply has shrunk more significantly than housing demand as the rebalance has started in most cities with excess supply. The significant shrinkage of land-related fiscal system increased local government contingent debt risk and brought downside pressure on local government expenditures. Looking forward, housing sales may see tentative stabilization in September or October due as policymakers continue to loosen property policy and credit supply and service business recovery improves employment condition. However, the confidence of property developers may remain low as land sales and property development investment should recover even more slowly.
- Retail sales moderately recovered amid high energy price and robust summer demand.** Retail sales came in above the market expectation by rising 4.6% in August after climbing 2.5% in July. Its 2Y CAGR increased to 5% in August, up from 2.6% in July. Looking into the details, retail sales recovered almost across the board as catering service, petroleum product and auto continued to surge with their 2Y CAGRs respectively rose from 6.8%, 6.5% and 3.9% in July to 10.4%, 11.4% and 8.2% in August. Housing-related durables remained weak as construction & decoration materials and home

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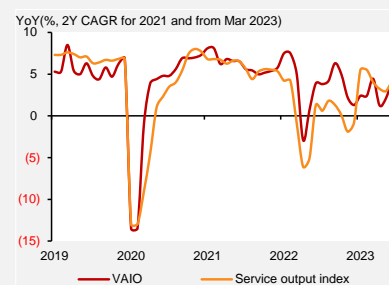
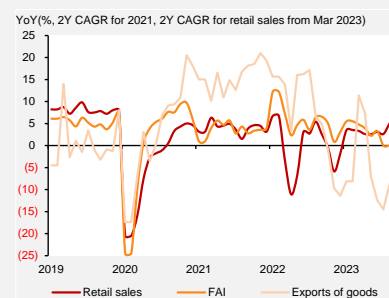
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appliance respectively dropped 11.4% and 2.9% with their 2Y CAGR at -10.3% and 0.2%. Furniture picked up 4.8% after rising 0.1%, but its 2Y CAGR remained negative at -1.9%. Staples moderately improved as the 2Y CAGRs of food, beverage and medicine respectively rose to 6.3%, 3.3% and 6.4% from 5.8%, 3% and 5.7% in July while alcohol & tobacco product dropped to 6.1% from 7.4% in July. Recovery of telecom equip eased as the 2Y CAGR edged down to 1.7% in August from 3.9% in July. Looking forward, retail sales may maintain mild to moderate recovery as employment and confidence slowly improve. We maintain our forecast for the retail sales growth in 2023 at 7.5%.

- **Service activity and industrial output both resurged.** Service output index and VAIO growth both came in above the market expectation. They respectively rose 6.8% and 4.5% in August after growing 5.7% and 3.7% in July, thanks to a recovering consumer demand and narrowing export decline. In terms of 2Y CAGRs, VAIO and service output index respectively increased to 4.3% and 4.3% from 3.1% and 3.7% in July. In service sector, lodging and dining, internet & IT service and transportation saw higher YoY growth and transportation, lodging and dining, and telecom service had good sentiment. In manufacturing sector, auto sector continued to be the highlight in the economy with elevated 11.7% YoY growth in 8M23 amid strong export and domestic performance. Output in chemical products, rubber & plastic product, ferrous & non-ferrous metal smelting & pressing, and electronic equipment saw robust growth while textile, nonmetal mineral products, medicine, metal product and general & special purpose equip remained weak as domestic and foreign demand remained weak. Looking forward, we may see a gradual recovery of service sector and VAIO as domestic consumer demand continues to improve and exports further narrow the declines.
- **FAI slightly rebounded although property investment remained sluggish.** FAI picked up 2% in August after rising 1.2% in July. Property sector remained sluggish as property development investment fell by 10.9% after declining 12.2% in July. The liquidity condition of most private developers remained restricted as some of them started to rollover the domestic debt and reorganized their foreign debt. With loosening property policies, we expect the property developers may have a short period of relief benefiting from a gradual recovery in housing market. The YoY growth of FAI in manufacturing rebounded to 7.1% growth from 4.3% in July. Looking forward, chemical product, auto and electrical material & equipment may maintain strong FAI growth as the energy transition and smart technology revolution boosts business capex in those sectors. However, most other manufacturing industries are likely to see a gradual slowdown of FAI due to continuous slowdown in demand growth as well as uncertainty in domestic policy and geopolitics. Infrastructure YoY growth mildly recovered at 6.2% growth in August from 5.3% as local government expanded the fiscal support amid an acceleration in local government bond issuance. The YoY growth of FAI in public utility, transportation, storage & post service, and railway transportation remained elevated while fixed investment in public facility management and health & social welfare remained weak. Looking forward, we expect infrastructure investment may continue to expand since the new trend in credit data showed government is picking up debt to offset the deficit of private credit demand. We maintain our forecast on the FAI growth in 2023 at 3.8%.
- **The current policy easing cycle may last longer than the previous ones as the policy effectiveness on economic growth declines.** The recent policy moves indicate an important change of policy stance in China as policymakers have made stronger commitment to restoring confidence and

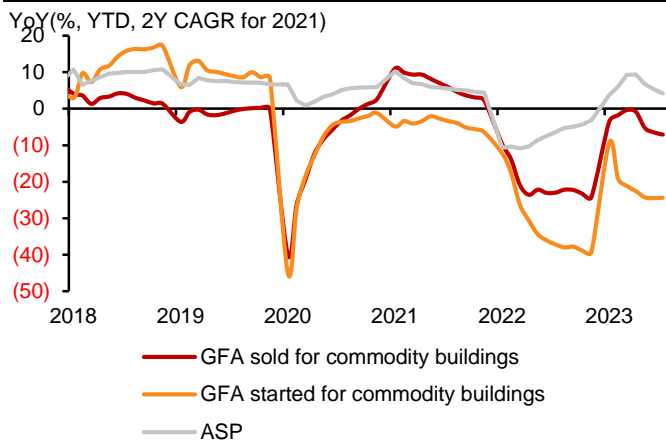
growth momentum. China launched two rounds of strong stimulus in the past two decades with one in 2008-2009 and the other in 2015-2016. After the stimulus, the economy experienced a recovery cycle for 1.5-2 years and then continued with the structural slowdown trend. The latest policy cycle is likely to become the strongest one since 2017. But the policy effectiveness on economic growth declines with more aging population, less labor supply, weaker market-oriented incentive and greater geopolitical uncertainty. That means the current policy easing cycle may last longer than the previous ones if the policymakers continue to seek growth at around 5% in next two years.

**Figure 1: China Economic Indicators**

	YoY (%)										2Y CAGR (%)					
	2019	2020	2021	2022	1Q23	1H23	Jul	Aug	Sep(F)	Oct(F)	1Q23	1H23	Jul	Aug	Sep(F)	Oct(F)
GDP	6.0	2.3	8.4	3.0	4.5	5.5			4.4		4.6	4.0			4.1	
VAIO	5.7	2.8	9.6	3.6	3.0	3.8	3.7	4.5	2.0	3.9	4.7	3.6	3.7	4.3	4.1	4.4
-Mining	5.0	0.5	5.3	0.6	3.2	1.7	1.3	2.3	1.0	3.0	6.9	5.5	4.6	3.8	4.1	3.5
-Manufacturing	6.0	3.4	9.8	(2.0)	2.9	4.2	3.9	5.4	2.2	4.0	4.5	3.5	3.3	4.2	4.3	4.6
-Public utility	7.0	2.0	11.4	(2.2)	3.3	4.1	4.1	0.2	8.5	7.0	4.7	4.0	6.8	6.7	5.7	5.5
Delivery value for exports	1.3	(0.3)	17.7	5.5	(5.3)	(4.8)	(6.4)	(4.5)	(4.0)	(2.0)	4.1	2.7	1.4	0.4	0.4	0.2
Service output index	6.9	0.0	13.1	(0.1)	6.7	8.7	5.7	6.8	7.5	9.0	4.6	4.1	3.1	4.3	4.4	4.5
Retail sales	8.0	(3.9)	12.5	(0.2)	5.8	8.2	2.5	4.6	7.2	10.5	4.5	3.7	2.6	5.0	4.8	4.9
Exports of goods	0.5	3.6	29.9	7.0	(1.5)	(3.2)	(14.5)	(8.8)	(7.0)	(2.0)	6.5	4.8	0.1	(1.4)	(1.2)	(1.5)
Imports of goods	(2.7)	(0.6)	30.1	1.1	(6.9)	(6.7)	(12.4)	(7.3)	(5.0)	(2.5)	1.5	(0.8)	(5.8)	(3.9)	(2.6)	(1.8)
Urban FAI (YTD)	5.4	2.9	4.9	5.1	5.1	3.8	3.4	3.2	3.0	2.8	7.2	4.9	4.5	4.5	4.4	4.3
-Property development	9.9	7.0	4.4	(10.0)	(5.8)	(7.9)	(8.5)	(8.8)	(9.0)	(8.0)	(2.6)	(6.7)	(7.5)	(8.1)	(8.5)	(8.4)
-Manufacturing	3.1	(2.2)	13.5	9.1	7.0	6.0	5.7	5.9	5.7	5.9	11.2	8.2	7.8	7.9	7.9	7.8
-Infrastructure	3.3	3.4	0.2	11.5	10.8	10.2	9.4	9.0	8.8	8.2	10.6	9.7	9.5	9.7	10.0	9.8
GFA sold for commodity building (YTD)	20.9	(20.8)	0.0	0.0	(1.8)	(5.3)	(6.5)	(7.1)	(7.8)	(7.0)	(8.0)	(14.2)	(15.2)	(15.4)	(15.3)	(15.0)
GFA started for commodity building (YTD)	0.0	0.0	0.0	0.0	(19.2)	(24.3)	(24.5)	(24.4)	(25.0)	(22.0)	(18.4)	(29.5)	(30.5)	(31.1)	(31.8)	(30.3)

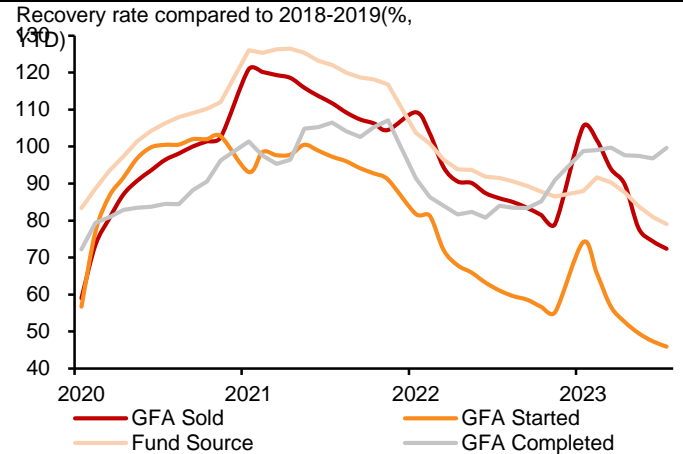
Source: Wind, CMBIGM estimates

**Figure 2: Property Market Indicators**



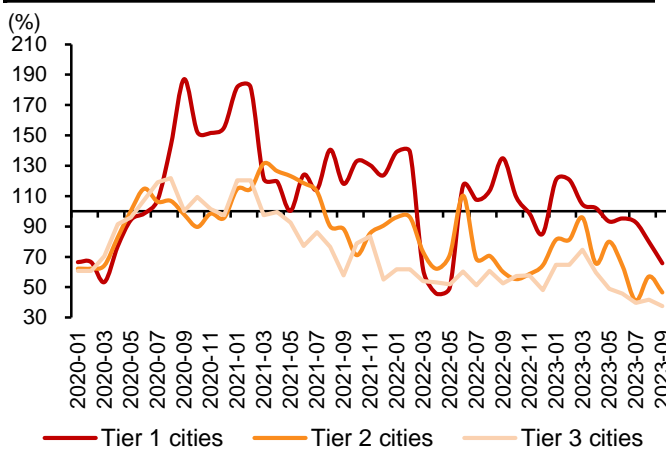
Source: WIND, CMBIGM

**Figure 3: Recovery Rates Compared to 2019**



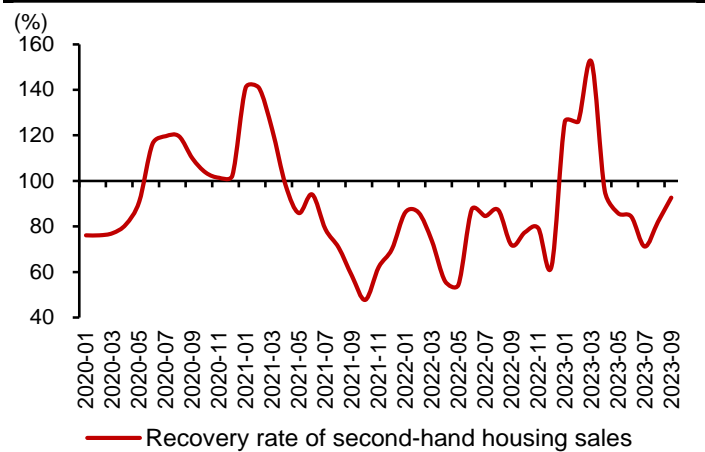
Source: WIND, CMBIGM

**Figure 4: Housing Sales Recovery Rates to 2019 in 30 Cities**



Source: WIND, CMBIGM

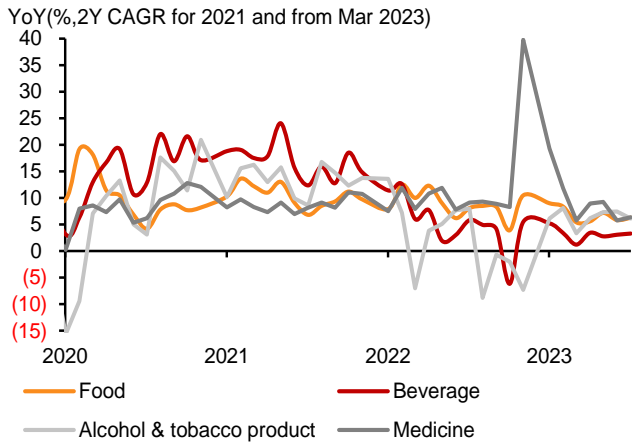
**Figure 5: Recovery rate of second-hand housing sales compared to 2019 in 11 selective cities**



Source: WIND, CMBIGM

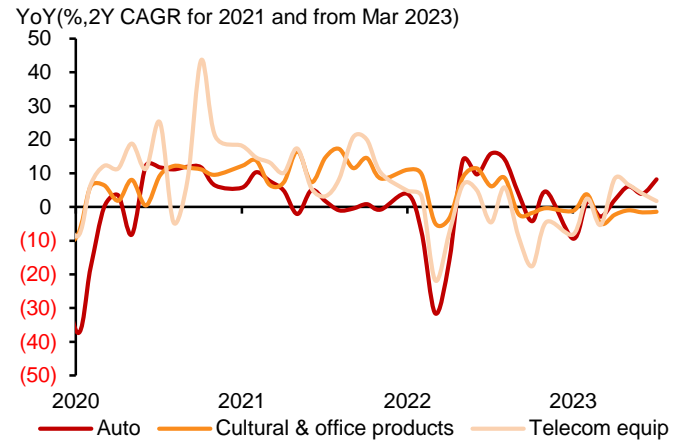
11 cities include Beijing, Shenzhen, Hangzhou, Nanjing, Chengdu, Qingdao, Suzhou, Xiamen, Wuxi, Dongguan and Foshan

**Figure 6: Retail Sales of Staples**



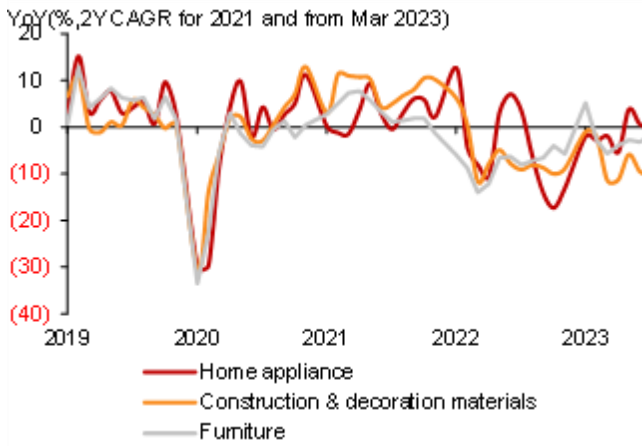
Source: WIND, CMBIGM

**Figure 7: Retail Sales of Auto & Electronics**



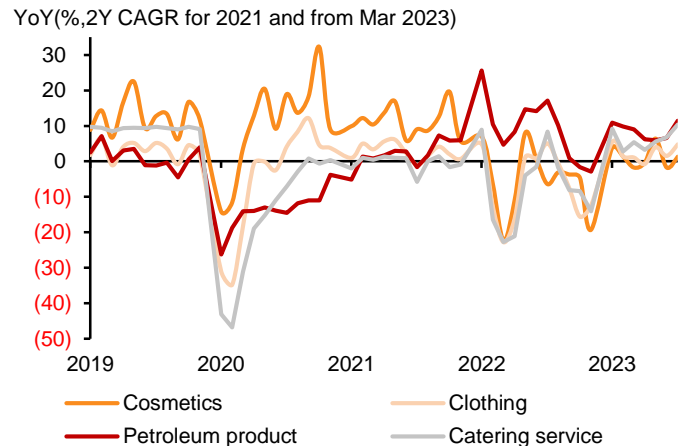
Source: WIND, CMBIGM

**Figure 8: Home Appliance & Furniture Retail Sales**



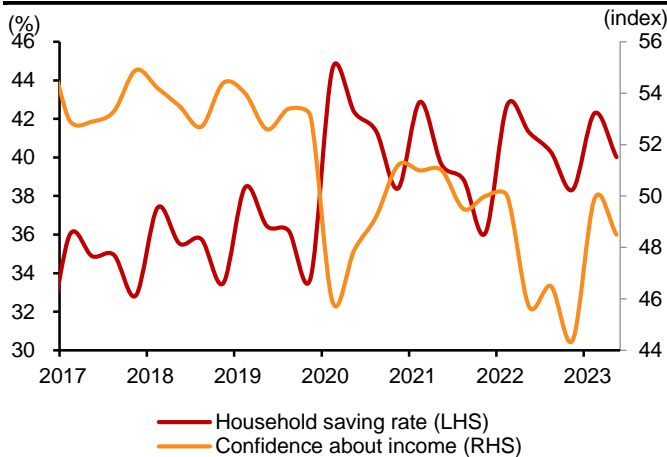
Source: WIND, CMBIGM

**Figure 9: Retail Sales Related to Outgoing Activities**



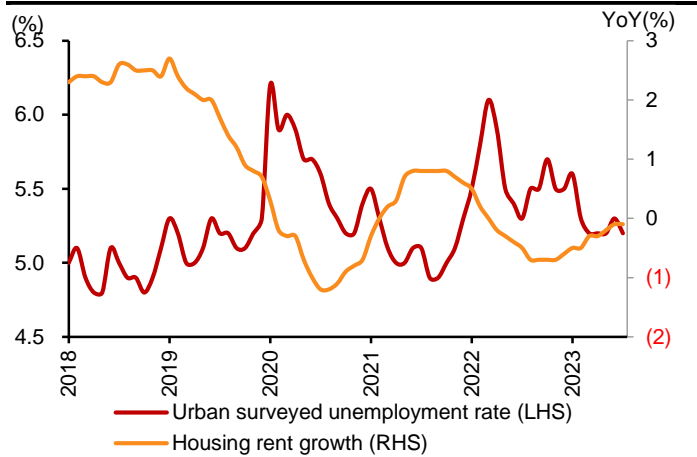
Source: WIND, CMBIGM

**Figure 10: Consumer Confidence**



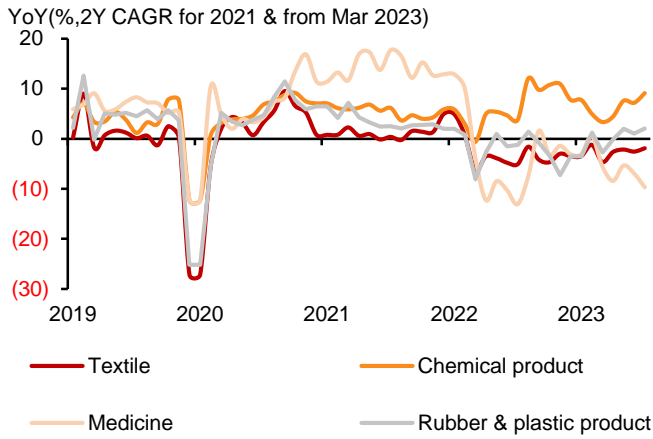
Source: WIND, CMBIGM

**Figure 11: Urban Unemployment Rate & Housing Rent**



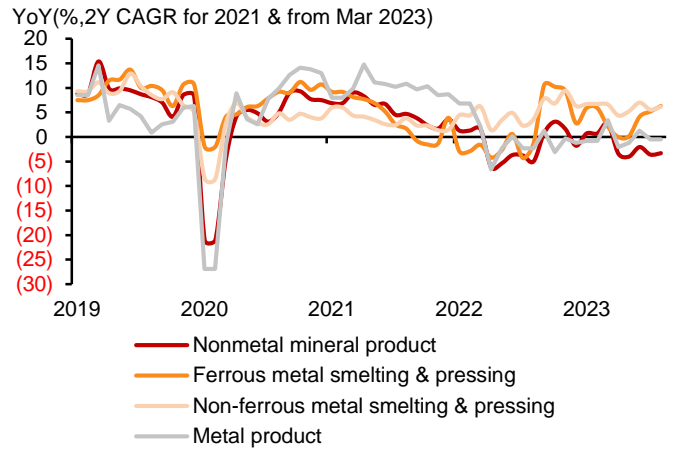
Source: WIND, CMBIGM

**Figure 12: VAIO in Textile & Chemical Products**



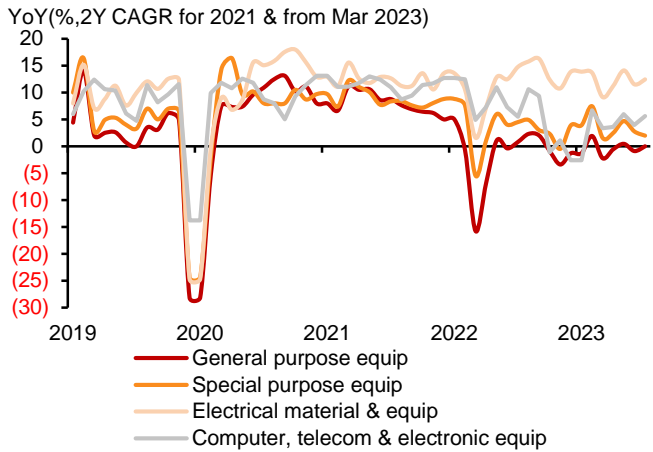
Source: WIND, CMBIGM

**Figure 13: VAIO in Mineral & Metal Products**



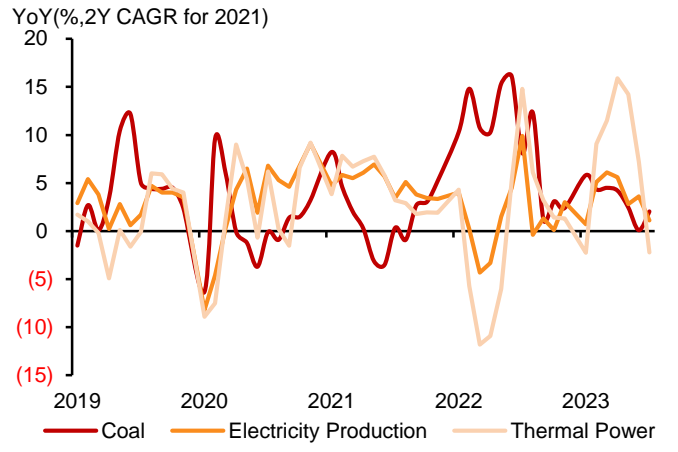
Source: WIND, CMBIGM

**Figure 14: VAIO in Equipment**



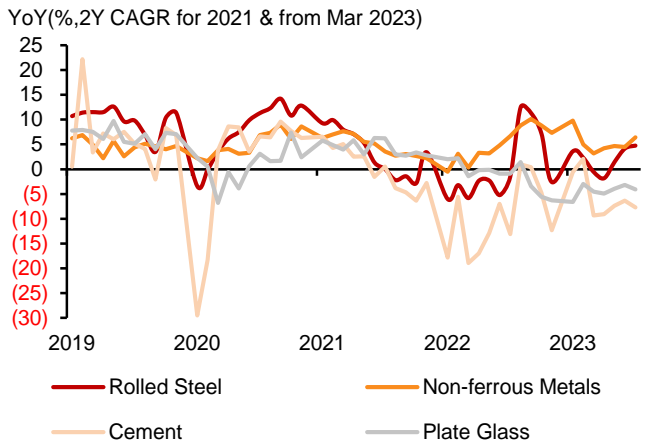
Source: WIND, CMBIGM

**Figure 15: Output in Energy and Electricity**



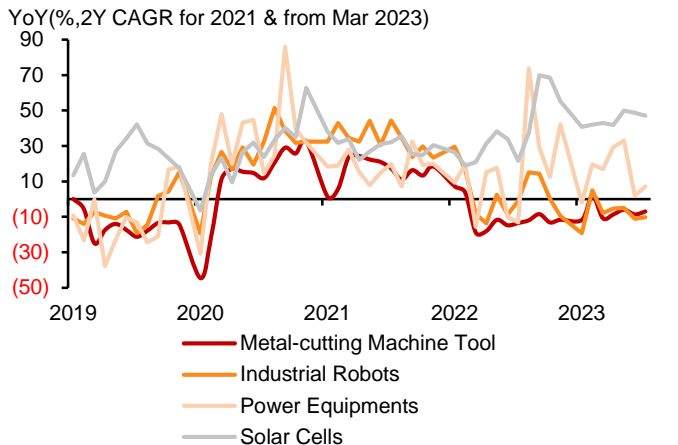
Source: WIND, CMBIGM

**Figure 16: Output in Steel & Construction Material**



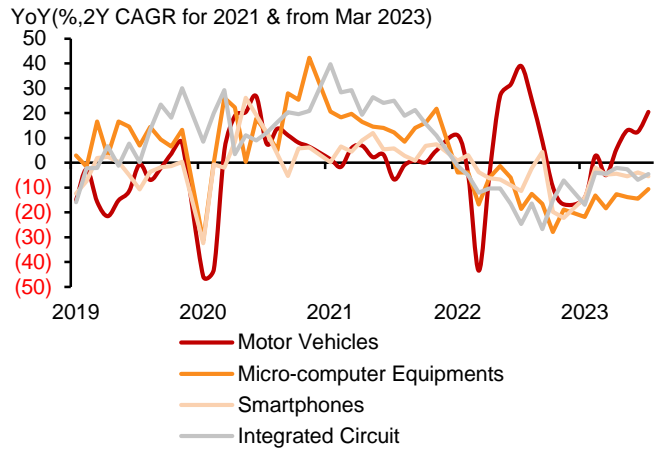
Source: WIND, CMBIGM

**Figure 17: Output in Capital Goods**



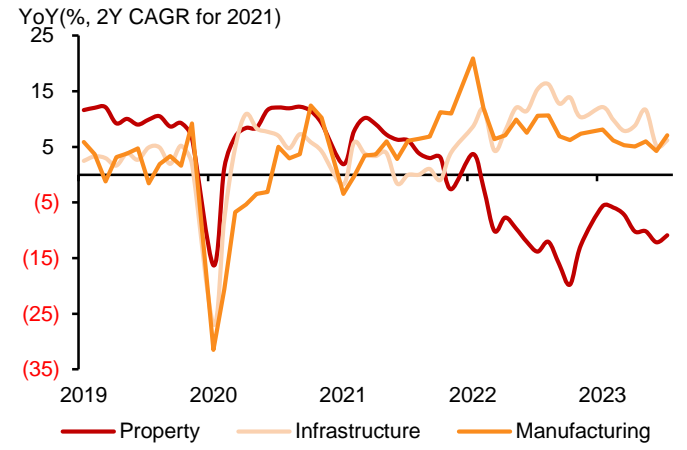
Source: WIND, CMBIGM

**Figure 18: Output in Auto, Computer & Smartphone**



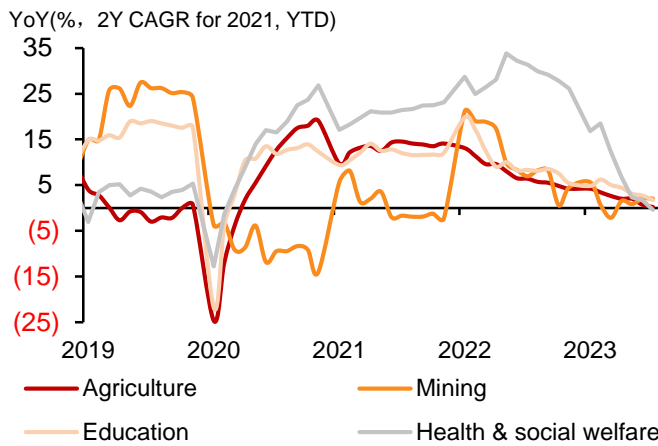
Source: WIND, CMBIGM

**Figure 19: FAI by Sector**



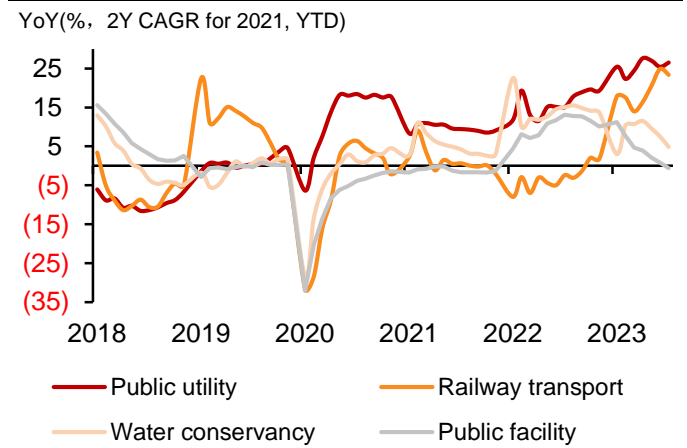
Source: WIND, CMBIGM

**Figure 20: FAI in Agriculture, Mining & Public Service**



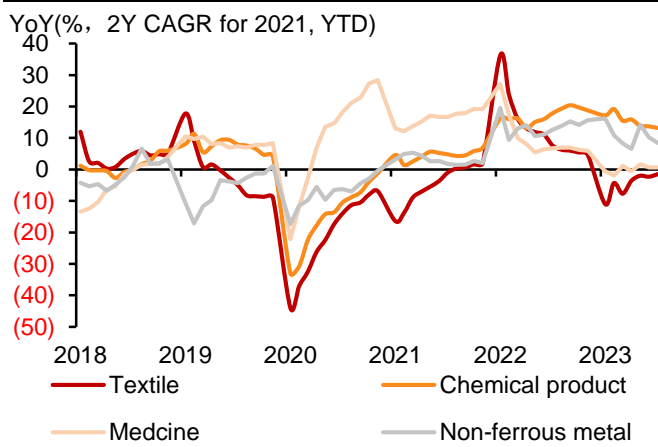
Source: WIND, CMBIGM

**Figure 21: FAI in Infrastructure Sectors**



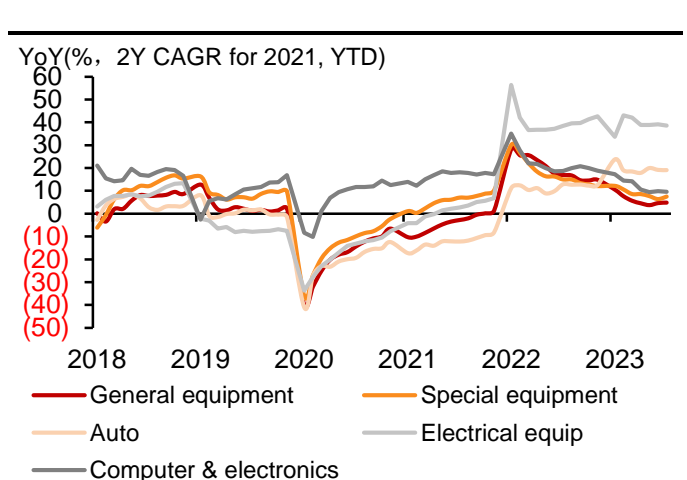
Source: WIND, CMBIGM

**Figure 22: FAI in Chemical Product & Non-ferrous Metal**



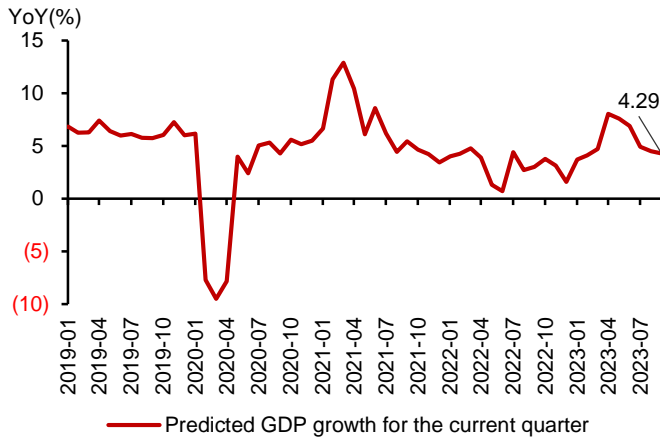
Source: WIND, CMBIGM

**Figure 23: FAI in Equipment**



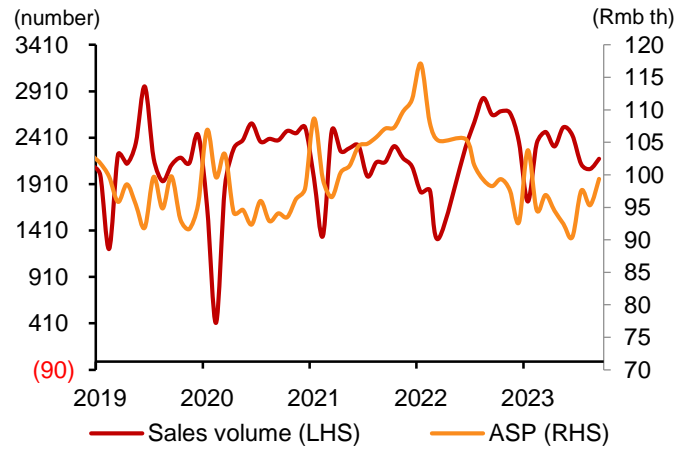
Source: WIND, CMBIGM

**Figure 24: Predicted GDP for Current Quarter**



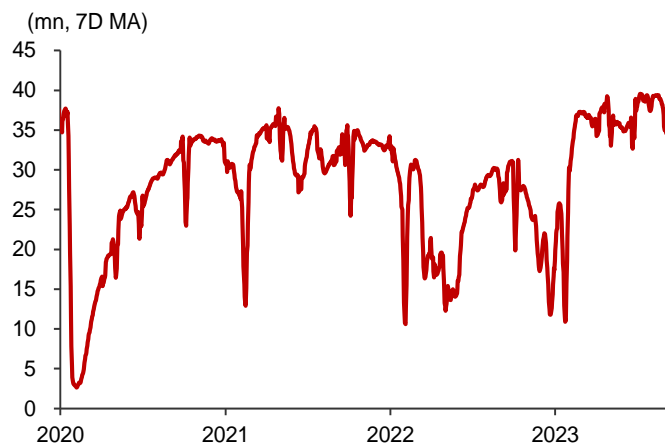
Source: WIND, CMBIGM

**Figure 25: Yicai Economic Activity Index**



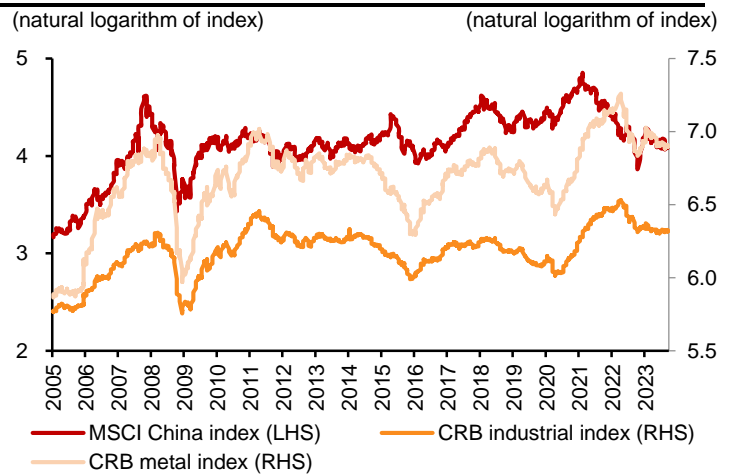
Source: WIND, CMBIGM

**Figure 26: Subway Passenger Flow in Tier-1 Cities**



Source: WIND, CMBIGM

**Figure 27: MSCI China and Industrial& Metal Index**



Source: WIND, CMBIGM



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