# China Economic Briefing
by NAB Group Economics

22 October 2014

National Australia Bank

## China's growth rate slowed in Q3; unlikely enough to trigger further stimulus

China's latest economic data was a mixed bag – with many measures comparatively negative (against the trends of recent years) but stronger than somewhat pessimistic market expectations. While year-on-year GDP growth was at a five year low, the growth rate remaining above 7% will likely be enough to avoid further broad based stimulus – measures opposed by the People's Bank of China (PBoC).

As we have previously outlined, this result needs to be viewed in context. Last year's mini-stimulus program distorted activity in Q3 2013 (pushing growth higher), and as a result, sustaining the growth momentum from early 2014 was always unlikely this quarter.

Our forecasts remain unchanged, with economic growth at 7.3% in 2014, and slowing further to 7.0% in 2015.

### Gross Domestic Product

The latest national accounts data showed that China's economy grew by 7.3% yoy in the September quarter, the slowest rate of growth since March 2009 – the low point of the global financial crisis. That said, this result was slightly stronger than market expectations (at 7.2% yoy). In quarterly terms, growth remained reasonably strong at 1.9%.

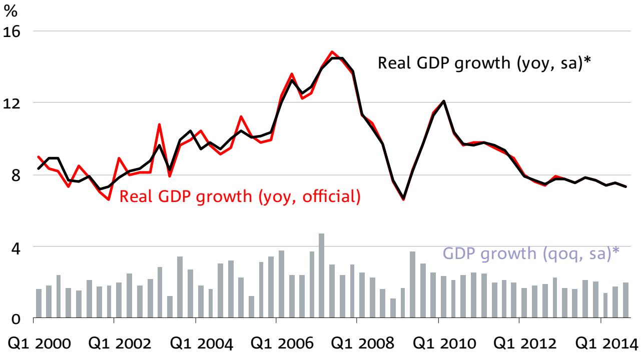
Soft industrial production data over the third quarter did not directly translate into a marked slowing in economic activity for the secondary industries. That said, the comparatively strong growth in China's service sector saw the tertiary industries account for a larger share of the economy in the third quarter – rising to 47% on a twelve month moving average basis. The share for secondary industries fell to 43% – highlighting the gradual transition that is continuing in China's economy.

There remains speculation around potential stimulus, however commentary from the PBoC continues to suggest opposition from some policy makers. Policy efforts to date have been quite narrow – in areas such as agriculture and social housing – attempting to avoid expansion in credit to over-leveraged sectors, such as residential property and heavy industry.

### Industrial Production and Investment

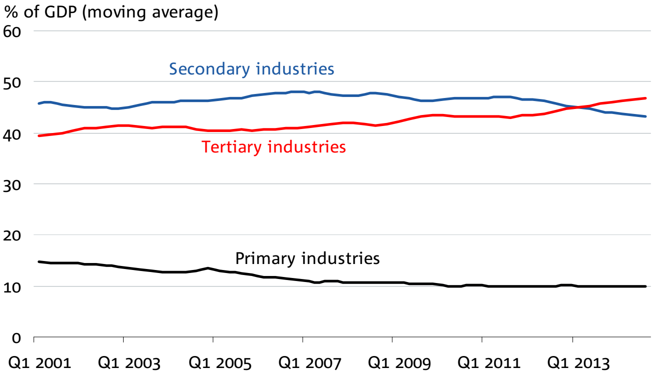
Following on from a very negative August, growth in industrial production marginally recovered in September – with output rising by 8.0% yoy (compared with 6.9% previously – the lowest level in over five years). This result was stronger than market expectations of around 7.5% yoy.

**China's real GDP in Q3 eased to the slowest rate of growth since March 2009**



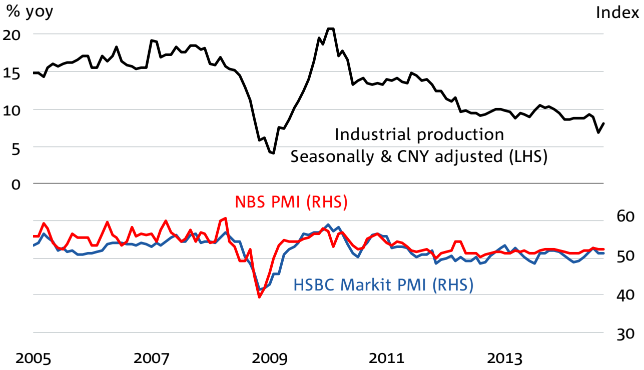

* Seasonally adjusted growth series are estimated by NAB.
Source: CEIC, NAB Economics

**Service sector share of China's economy continues to increase**




Sources: Datastream, NAB Economics

**Industrial production growth marginally recovered in September, from five year lows in August**




Source: CEIC, NAB Economics

The two major industrial surveys were stable in September. The official PMI (National Bureau of Statistics) was unchanged at 51.1 points, while the HSBC Markit PMI was also stable at 50.2 points. The former is considered a better indicator of larger state-owned enterprises, and the latter of the small-to-medium sector.

Production trends at the sub-sector level remain highly mixed. Output of electricity was stronger this month, at 4.1% yoy (compared with -2.2% in August), as was motor vehicle production (4.5% yoy in September compared with 3.1% previously). In contrast, construction related products were weaker. Cement output fell, down -2.2% yoy (from 3.0% in August) and crude steel output was unchanged (down from 1.0% in August).

China's fixed asset investment remained comparatively weak in September, with the rate of growth unchanged at 13.8% yoy (in seasonally adjusted terms). Key sub-sectors continue to weaken – most notably manufacturing and real estate.

The growth in real estate investment has continued to slow – driven in part by weak market conditions. Investment slowed to 10.1% yoy in September (from 11.4% in August) – the weakest growth rate since the global financial crisis. Similarly, manufacturing investment has continued to trend lower – with growth of 12.3% yoy in September (from 13.8% last month).

Concerns around the broader impact of a property slowdown – reflecting the importance of the sector to China's economic growth and local government revenues – have resulted in the loosening of a range of policies, with a goal of stabilising the sector. The total residential floor space sold in September fell by -12% yoy (compared with -13% last month). In contrast, the value of these sales fell by just -10% yoy – implying a slight increase in indicative prices in September.

### International trade

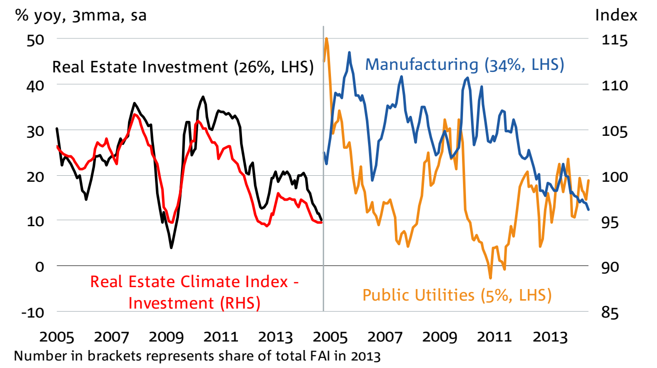
China's trade surplus pulled back in September, to US$30.9 billion (compared with a record US$49.3 billion in August). The narrowing of the balance was driven largely by a sharp rebound in imports.

US dollar denominated exports rose by 15.3% yoy in September (compared with 9.4% in August). The scale of the acceleration reflects some base effects – with a monthly fall in exports occurring in September 2013.

In terms of China's major export markets, there was a sharp increase exports to East Asia – with growth of 24% yoy (compared with just 3.5% in August) – driven entirely by a pick up in Hong Kong, which at almost US$38 billion exceeded exports to the United States and European Union. This raised some concerns around a return to the false invoicing distortions evident in 2013. US exports grew by 11% yoy (largely unchanged) while EU exports increased by 15% yoy (from 12% in August).

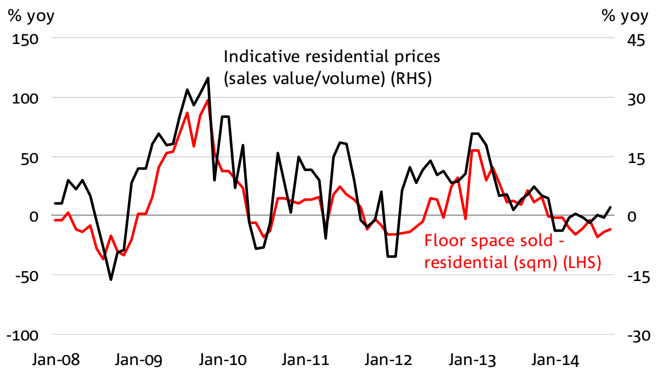
There was a rebound in High Tech exports – up by 5.8% yoy (compared with -1.2% previously) and Mechanical & Electrical goods, which grew by 8.1% yoy (from 4.7% in August).

### Ongoing weak investment driven by real estate and manufacturing



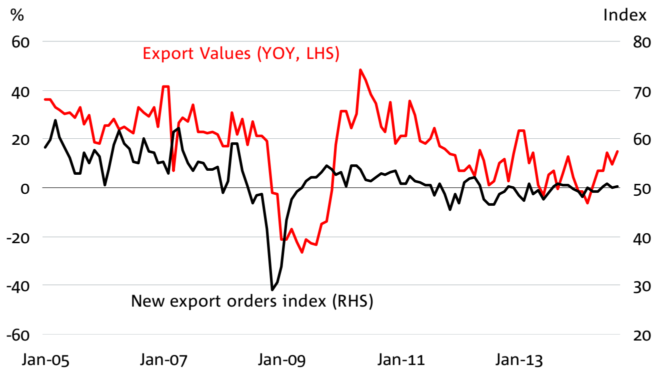

Number in brackets represents share of total FAI in 2013
Source: CEIC, NAB Economics

### Slight improvement in indicative residential property prices – but sales are still falling



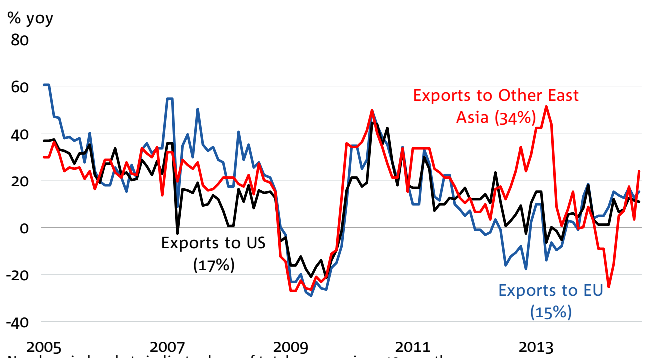

Sources: CEIC, Datastream, NAB Economics

### Recent export trends stronger post false invoice distortions




Source: CEIC, NAB Economics

### Hong Kong the key driver of export growth this month




Numbers in brackets indicate share of total over previous 12 months
Sources: CEIC, NAB Economics

Imports were stronger in September, following on from two surprisingly weak months. Imports rose by 7.1% yoy (compared with a -2.3% yoy fall in August).

Trends for commodity import volumes were mixed. Iron ore imports improved – with growth accelerating to 14% yoy (from 8.5% in August), while coal was less negative (albeit very weak), with imports down -18% yoy (from -27% last month). In contrast, copper imports fell by -15% yoy (from -13% in August), while crude oil slowed to 7.4% from 18% previously.

### Retail Sales and Inflation

Retail sales tracked lower in September, with nominal growth easing to 11.6% yoy (down from 11.9% in August) – the weakest rate of growth since February 2006. This trend was less negative in real terms – reflecting the low levels of inflation in recent times – with growth edging up to 10.8% yoy (from 10.6% last month).

Sales of food and drink products and household goods recorded slower growth, with the former surprisingly weak at 7.5% yoy (down from 12% last month). In contrast, jewellery sales were up over 11% yoy – having fallen sharply across the first half of 2014.

Inflation slowed in September, driven by softer growth in food prices. Consumer prices rose by 1.6% yoy (compared with 2.2% in August). Non-food prices eased to the lowest level since April 2010 at 1.3% yoy.

Food price inflation slowed to 2.3% yoy in September (compared with 3.0% previously). Previously strong growth in eggs and fresh fruit prices was pared back, while prices for fresh vegetables have continued to fall.

Producer prices fell once again – having fallen for thirty-one months in a row – down by -1.8% yoy in September. This deflation remains driven by heavy industry (down by -2.4% yoy), and trends are closely correlated to weaker global commodity prices.

### Credit conditions

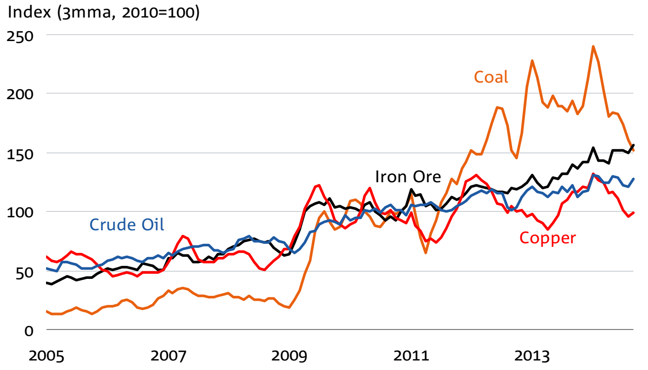
New credit – as measured by total social financing – edged higher in September to RMB 1050 billion. While this was the strongest level for new credit in the past three months, it was around 26% lower than September 2013.

Bank loans continued to contribute the largest share of new credit in September, at RMB 807 billion (for both domestic and foreign currency loans) – accounting for over three-quarters of the total.

Over the first nine months of 2014, new credit declined in year-on-year terms, down by -8.3% yoy. Bank loans have increased modestly – increasing by 3.4% yoy – while net corporate bond financing has grown strongly (at almost 19% yoy).

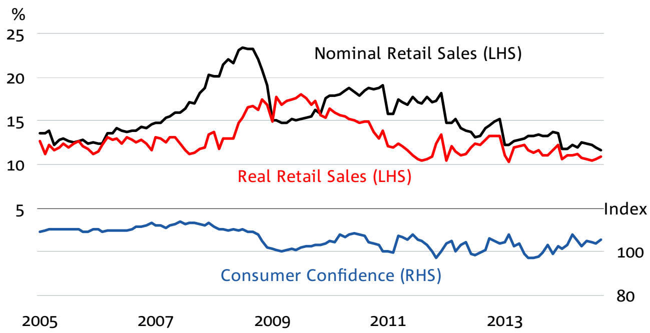
Attempts to address concerns around the growth of shadow banking appear to have impacted on non-bank lending, with other financing contracting by -37% yoy over the first nine months of the year. This was led by trust and entrusted loans (two key components of China's shadow banking sector), where new credit has fallen by -37% yoy.

### Mixed trends in commodity import volumes – with coal and copper particularly weak



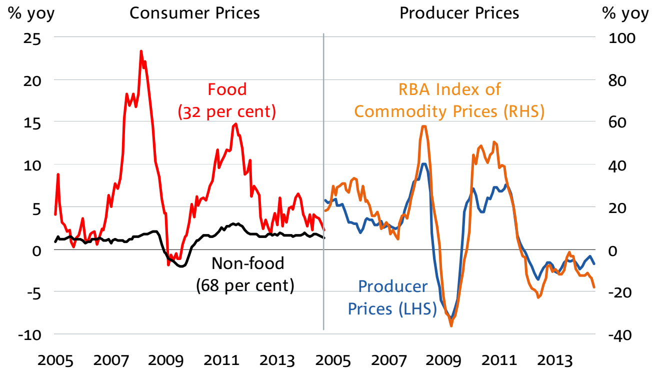

Sources: CEIC, NAB Economics

### Real retail sales growth edges higher, even as nominal sales growth falls to eight year low in September



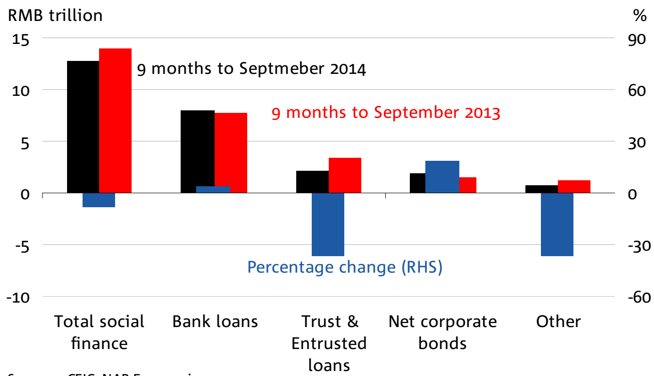

* No observation is shown for January due to the effect of Chinese New Year; Feburary shows the average of January and February compared to December.
Source: CEIC, NAB Economics

### Inflation trends softer on weaker food price growth




Sources: CEIC, RBA, NAB Economics

### Credit remains weaker year-on-year, with trust & entrusted loans pulling back

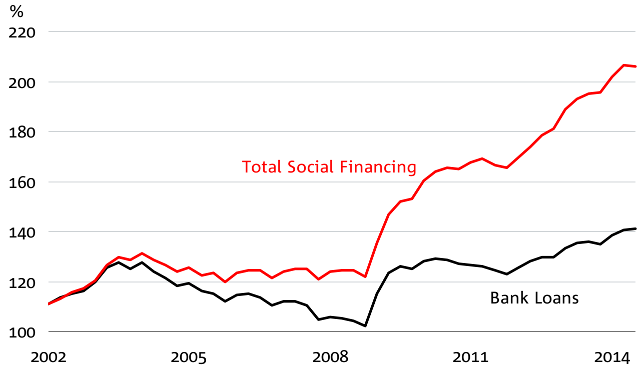



Sources: CEIC, NAB Economics

The overall stock of China's debt has increased in recent years, particularly since the 2009 stimulus program implemented to recover from the GFC. The stock of bank loans was around 141% of GDP in the September quarter, while total social finance was 206% of GDP – the latter stabilising following a climb from 165% of GDP at the end of 2011.

While the People's Bank of China has cut the interest rate on 14-day repurchase agreements and is injecting additional liquidity into the country's banking system – around RMB 200 billion to smaller national and regional lenders (following on from around RMB 500 billion to large banks last month) – the bank is keen to control credit growth, particularly in over-leveraged sectors such as residential property and heavy industry.

**China's debt to GDP ratio (excluding government bonds) has stabilised in recent quarters**




Sources: CEIC, NAB Economics

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