China's economy at a glance

by NAB Group Economics

15 May 2016

National Australia Bank

Construction activity continued ramp up in April, but we are concerned about the sustainability of growth

- A rebound in real estate investment in early 2016 has supported a surge in construction activity. In the first four months of 2016, residential construction starts rose by 18% yoy – with an acceleration in growth across March and April – underpinning growth in China's industry sector – particularly demand for steel and cement.

- We have serious concerns around the sustainability of the current rebound in Chinese construction activity. The recovery in house prices is largely related to policy changes that have relaxed purchase requirements, looser credit and the poor performance of alternative investment options – to re-inflating the property bubble that had somewhat deflated across 2014 and 2015. In the absence of a broad based fundamental support for current real estate trends, any policy changes that prove adverse to construction could result in a sharp slowdown in industrial activity.

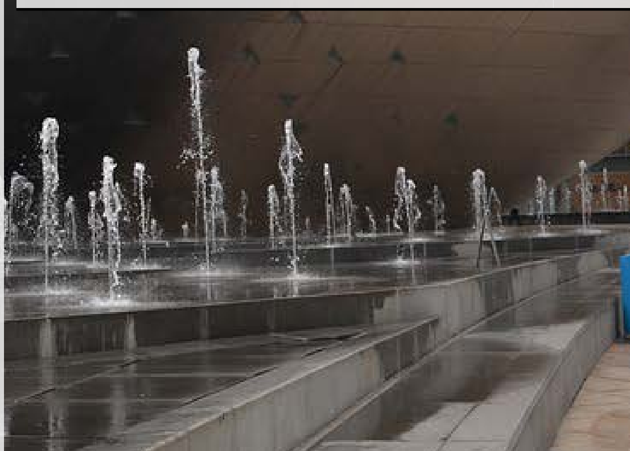
- China's industrial production growth was somewhat weaker in April – at 6.0% yoy (down from 6.8% in March) – below market expectations.

- Growth in China's fixed asset investment was slightly slower in April – at 10.1% yoy (from 11.1% in March). Although fixed asset investment has trended lower since late 2013, it has recovered modestly in recent months from lows recorded in September 2015. The recovery in real estate investment has been a major contributor to this trend.

- A month-on-month rise in exports and a fall in imports in April led to a widening in China's trade surplus, to US$45.6 billion (from US$29.9 billion in March).

- China's new credit expansion was relatively modest in April – compared with the surge in the first quarter – with new aggregate financing of RMB 751 billion – down around 29% yoy. That said over the first four months of the year, aggregate financing expanded by over 28% yoy to RMB 7.3 trillion – driven by large increases in January and March.

Contents



Contact

Gerard Burg gerard.burg@nab.com.au

Industrial production

- China's industrial production growth was somewhat weaker in April – at 6.0% yoy (down from 6.8% in March). This level was below market expectations – at 6.5% in the Bloomberg survey. That said, month-on-month growth remained around recent trend levels.

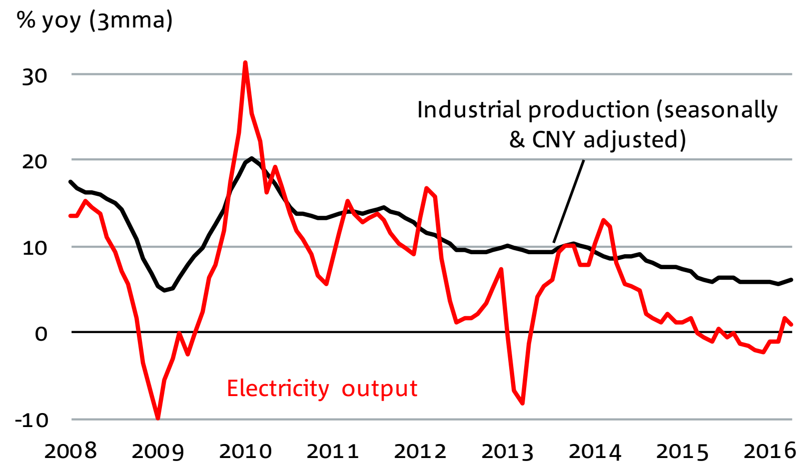
- Key heavy industrial sectors recorded weaker growth in April – with crude steel rising by just 0.5% yoy (down from 2.9% previously) and cement growing by 2.8% yoy (compared with 24% in March – albeit off a very weak base) – with both of these sectors linked to construction. Motor vehicle production rose by 4.3% yoy (down from 8.9%) and electricity output contracted – down by -1.7% yoy.

- Both of China's major industrial surveys were weaker in April – albeit remaining considerably stronger than trends over the past nine months. The official NBS PMI eased back marginally – to 50.1 points (from 50.2 points in March), while the Caixin Markit PMI fell to 49.4 points (from 49.7 points previously).

- We have serious concerns around the sustainability of the current rebound in Chinese construction activity – which is supporting demand for key industrial products. In the absence of a broad based fundamental support for current real estate trends, any policy changes that prove adverse to construction could result in a sharp slowdown in industrial activity.

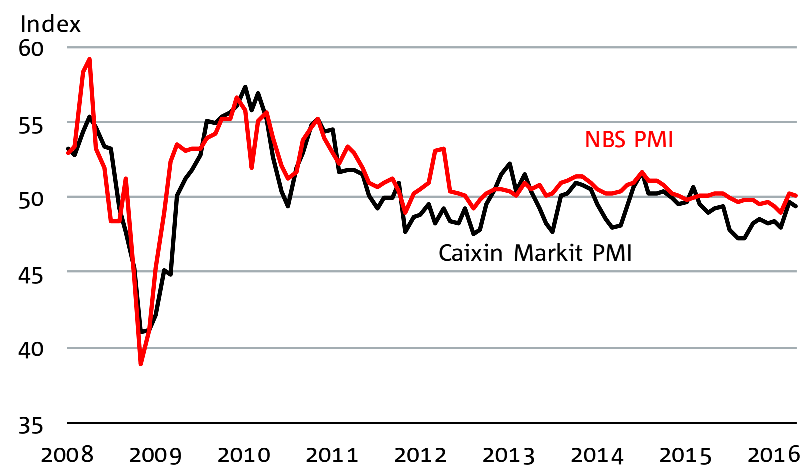
- As a result, we feel greater confidence around our above consensus forecast for economic growth in 2016 – at 6.7% – given that real estate activity should underpin growth in Q2. However we have greater concerns around China's medium term growth prospects.

Rebound in China's construction sector has stabilised IP growth – but concerns around its stability



Source: CEIC, NAB Economics

China's main PMI surveys eased back in April – but remained stronger than recent trend levels



Source: CEIC, NAB Economics

Investment

- Growth in China's fixed asset investment was slightly slower in April – at 10.1% yoy (from 11.1% in March) – a little below market expectations. Although fixed asset investment has trended lower since late 2013, it has recovered modestly in recent months from lows recorded in September 2015.

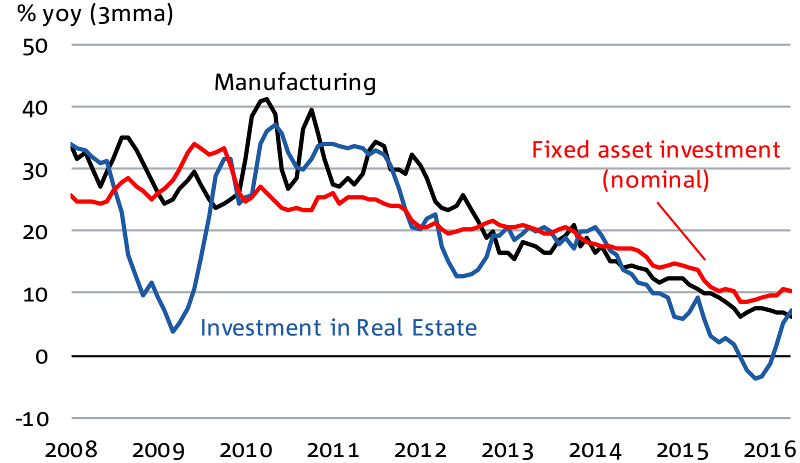
- A recovery in real estate investment has been a major contributor to this trend. Investment in real estate rose by 7.3% yoy (3mma) in April (up from 5.2% previously) – despite questions as to the sustainability of such investment. Manufacturing investment has also stabilised – at 6.2% yoy (3mma) in April (down from 6.9% in March). Together, these sectors accounted for 59% of total investment in Q1 2016.

- The rebound in real estate investment has supported a surge in construction activity. In the first four months of 2016, residential construction starts rose by 18% yoy – with an acceleration in growth across March and April – underpinning growth in China's industry sector – particularly demand for steel and cement.

- Although average property prices have risen in recent months, the strong increases remain a phenomenon of China's largest tier 1 cities. Tier 1 prices rose by 22% yoy in April, while prices in tier 2 and tier 3 (and below) cities rose by just 2.6% yoy and 3.6% yoy respectively.

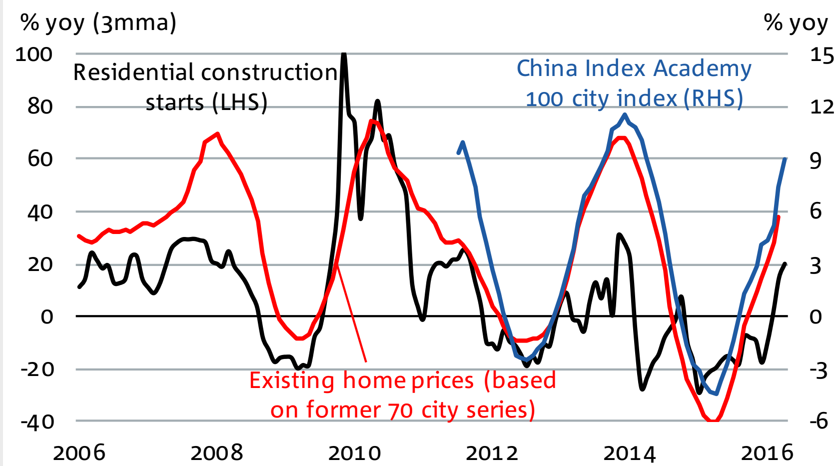
- It is likely that there is under supply in tier 1 cities – however these cities are home to just 5.1% of China's population. Elsewhere little appears to have changed at a fundamental level – with anecdotal evidence of excess supply in many locations. The recovery in house prices is largely related to policy changes that have relaxed purchase requirements, looser credit and the poor performance of alternative investment options (following the share market correction and crackdowns on shadow banking). These factors may be starting to re-inflate the property bubble that had somewhat deflated across 2014 and 2015.

Real estate investment has trended up from cyclical lows in late 2015 – underpinning recovery in total investment



Source: CEIC, NAB Economics

Construction activity has surged, while house prices have risen sharply – but largely in the tier 1 cities

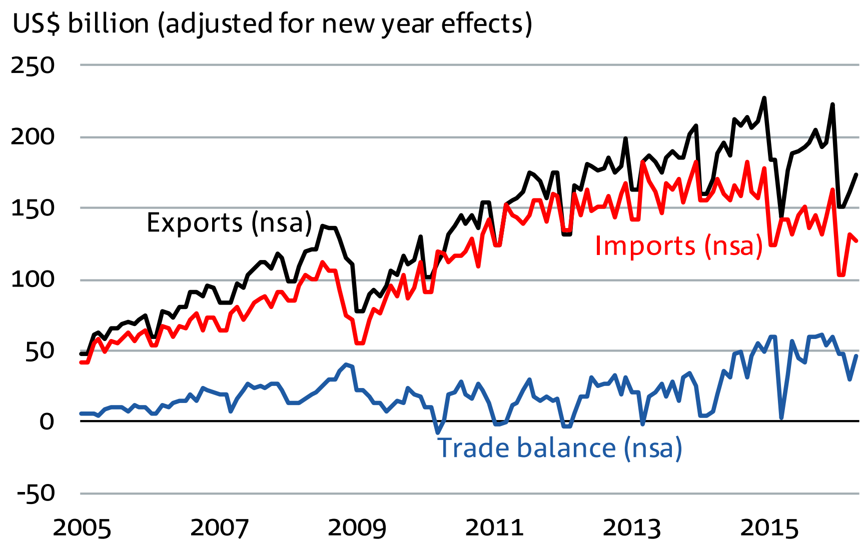


Source: CEIC, Datastream, NAB Economics

International trade – trade balance and imports

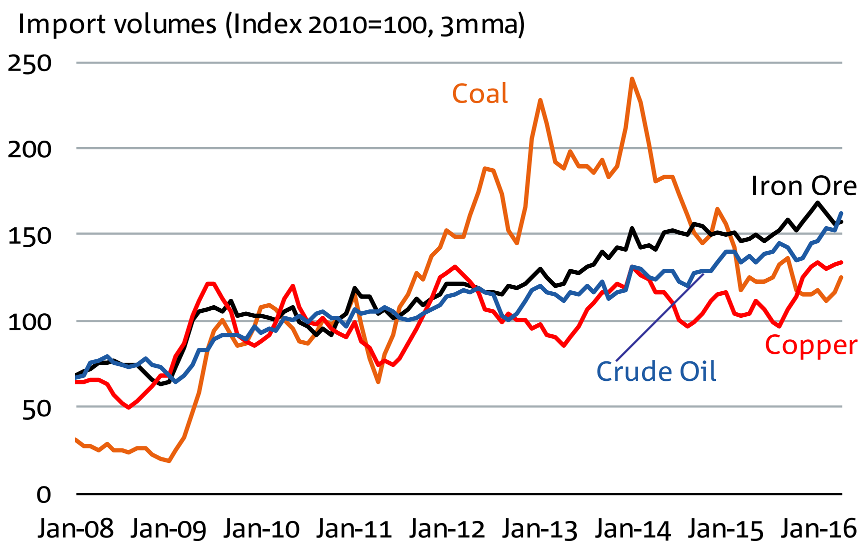
- A month-on-month rise in exports and a fall in imports in April led to a widening in China's trade surplus, to US$45.6 billion (from US$29.9 billion in March).
- China's imports pulled back to US$127.2 billion in April (from US$131.0 billion previously). In year-on-year terms, this was a decrease of 10.9%.
- As noted last month, there has been a considerable increase in reported imports from Hong Kong – rising by 203% yoy in April to US$2.1 billion. This may indicate disguised capital flows out of China through false invoicing.
- Commodity prices have fallen since 2011, and are a major influence on the lower value of China's imports. The RBA Index of Commodity Prices fell by around 7.7% yoy in April – however the index has trended up since hitting recent cyclical lows in January.
- Compared with a strong increase in commodity import volumes in March, increases were more subdued in April – with crude oil imports up 7.6% yoy (from 22% previously), copper and iron ore up 5.0% yoy and 4.6% yoy respectively while coal imports fell by 5.8% yoy.

China's trade surplus widened in April, as exports increased month-on-month while imports eased



Sources: CEIC, NAB Economics

Import volumes for iron ore and crude oil have continued to climb, while coal has fallen away

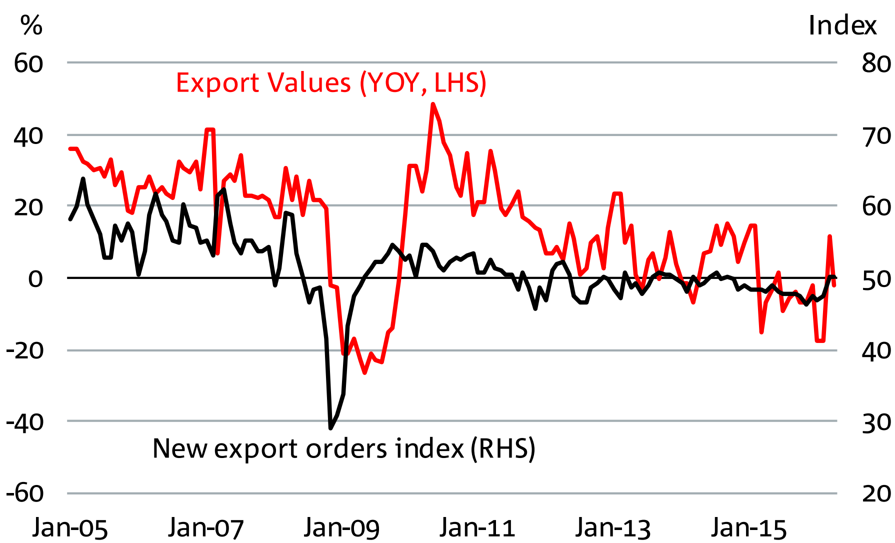


Sources: CEIC, NAB Economics

International trade – exports

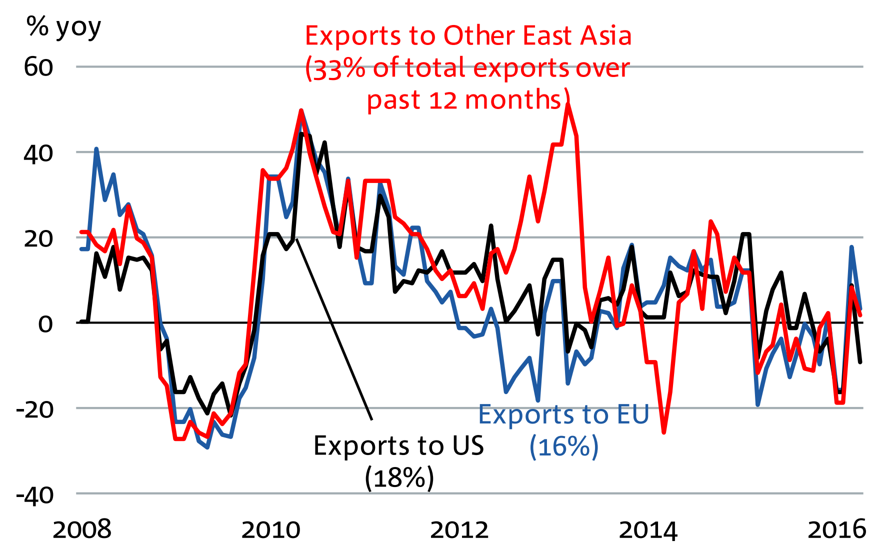
- China's exports totalled US$172.7 billion in April, up from US$160.8 billion previously. However, in year-on-year terms this was a decrease of 1.8%.
- China's exporters have been relatively more positive in recent months, compared with the trends across much of 2015. The new export orders component of the NBS PMI survey was at 50.1 points in April (marginally down from 50.2 points previously).
- While export growth to all major markets pulled back in April, this was most evident in the United States, where imports fell by 9.3% yoy (compared with a 9.0% increase in March).
- In contrast, growth was modest for deliveries to the European Union – 3.2% yoy (down from 17.9% previously) – and Asia, at 1.7% yoy (compared with 8.5% in March).
- As was the case in March, growth in exports to Asia was stronger than to non-Hong Kong markets – counter to the trend seen across much of 2015. Exports to Hong Kong fell by 0.4% yoy, while exports to other markets rose by 3.3% yoy – with the Philippines, Thailand and Singapore being the main drivers.

Confidence among China's exporters has improved with the upturn of industrial activity



Source: CEIC, NAB Economics

A decline in shipments to the United States was a major contributor to the softer export trend

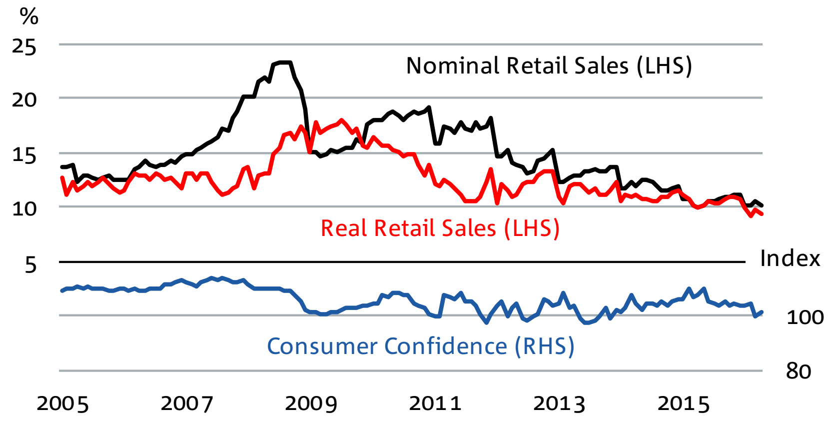


Sources: CEIC, NAB Economics

Retail sales and inflation

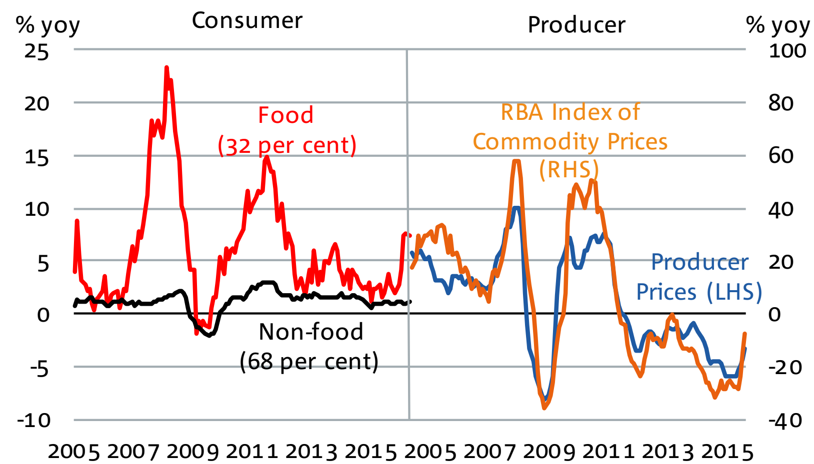
- Growth in retail sales was marginally slower in April – at 10.1% yoy (down from 10.5% in March) – below market expectations (10.6% yoy in the Bloomberg survey).
- The recent strengthening in inflation trends has pushed real retail sales below 10% yoy – estimated at 9.3% yoy in April (retail price index data was not available at the time of writing) – compared with 9.7% yoy previously.
- Consumer confidence has pulled back over the past two months – to 101 points in April, close to the neutral 100 point level.
- Headline inflation has remained stable again in April – with the Consumer Price Index rising by 2.3% yoy – the same rate of growth for the past three months. This rate of growth has been the strongest since mid-2014, easing some of the deflationary concerns in China's economy.
- Food prices continued to be the main contributor – rising by 7.4% yoy. Pork prices – up over 33% yoy – and fresh vegetables (up 23% yoy) were major drivers of food price growth, while prices for eggs and fresh fruit fell. Non-food prices were relatively stable – rising by 1.1% yoy (compared with 1.0% in March).
- Producer prices have fallen for fifty months in a row – however the rate of decline has slowed to 3.4% yoy (from 4.3% in March). In line with the modest upward trend in commodity prices since January 2016, month-on-month producer prices have risen – up 0.7% from March.

Strengthening in inflation has pushed real retail sales down under 10% yoy – but is still holding up



* Adjusted for Chinese New Year effects
Source: CEIC, NAB Economics

Consumer price growth has remained stable – fuelled by pork and vegetables – while producer price declines ease

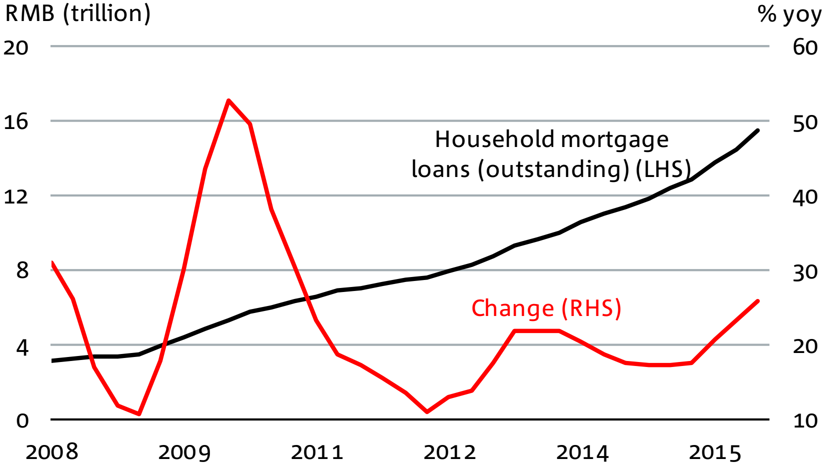


Sources: CEIC, RBA, NAB Economics

Credit conditions

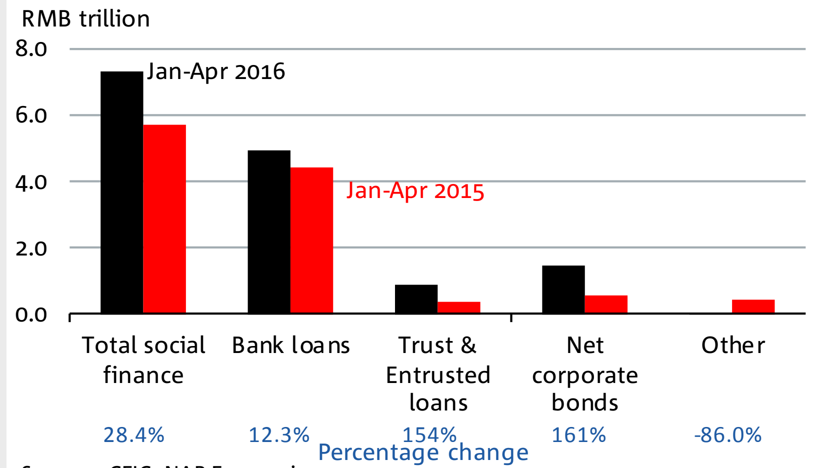
- Outstanding mortgage loans grew strongly in Q1 – rising by almost 26% yoy to RMB 15.5 trillion. The strong expansion helped to fuel growth in residential construction activity and Q1 GDP.
- China's new credit expansion was relatively modest in April – compared with the surge in the first quarter – with new aggregate financing of RMB 751 billion – down around 29% yoy.
- That said over the first four months of the year, aggregate financing expanded by over 28% yoy to RMB 7.3 trillion – driven by large increases in January and March.
- The majority of new aggregate financing has been traditional bank loans – totalling RMB 4.9 trillion in the first four months – an increase of 12% yoy. Loans in foreign currencies have continued to contract in early 2016 – contributing to the outflow of capital in recent times.
- Corporate bond financing has surged across the first four months of 2016 (albeit slower in April than in Q1) – totalling RMB 1.4 trillion – an increase of 161% yoy.
- Two key components of the shadow banking sector – trust and entrusted loans – have grown strongly in early 2016 – albeit off a low base, having contracted in 2015 on tightening regulation. In the first four months of the year, these loans rose by a combined 154% yoy.
- Monetary policy has remained on hold in recent months – with the benchmark one year lending rate at 4.35%. We continue to anticipate two cuts to rates in 2016 – however the stronger inflation trends in early 2016 may encourage the People's Bank of China to hold rates steady.

Housing credit grew strongly in Q1 – fuelling growth in residential construction and GDP



Sources: CEIC, NAB Economics

New credit growth was relatively modest in April – however it has surged 28% in the first four months



Sources: CEIC, NAB Economics

Group Economics
Alan Oster
Group Chief Economist
+61 3 8634 2927

Jacqui Brand
Personal Assistant
+61 3 8634 2181

Australian Economics and Commodities
Riki Polygenis
Head of Australia Economics
+(61 3) 8697 9534

James Glenn
Senior Economist – Australia
+(61 4)55 052 519

Vyanne Lai
Economist – Australia
+(61 3) 8634 0198

Amy Li
Economist – Australia
+(61 3) 8634 1563

Phin Ziebell
Economist – Agribusiness
+(61 4) 75 940 662

Behavioural & Industry Economics
Dean Pearson
Head of Behavioural & Industry Economics
+(61 3) 8634 2331

Robert De Iure
Senior Economist – Behavioural & Industry Economics
+(61 3) 8634 4611

Brien McDonald
Senior Economist – Behavioural & Industry Economics
+(61 3) 8634 3837

Steven Wu
Economist – Behavioural & Industry Economics
+(613) 9208 2929

International Economics
Tom Taylor
Head of Economics, International
+61 3 8634 1883

Tony Kelly
Senior Economist – International
+(61 3) 9208 5049

Gerard Burg
Senior Economist – Asia
+(61 3) 8634 2788

John Sharma
Economist – Sovereign Risk
+(61 3) 8634 4514

Global Markets Research
Peter Jolly
Global Head of Research
+61 2 9237 1406

Australia
Economics
Ivan Colhoun
Chief Economist, Markets
+61 2 9237 1836

David de Garis
Senior Economist
+61 3 8641 3045

Tapas Strickland
Economist
+61 2 9237 1980

FX Strategy
Ray Attrill
Global Co-Head of FX Strategy
+61 2 9237 1848

Rodrigo Catril
Currency Strategist
+61 2 9293 7109

Interest Rate Strategy
Skye Masters
Head of Interest Rate Strategy
+61 2 9295 1196

Alex Stanley
Senior Interest Rate Strategist
+61 2 9237 8154

Credit Research
Michael Bush
Head of Credit Research
+61 3 8641 0575

Simon Fletcher
Senior Credit Analyst – FI
+61 29237 1076

Andrew Jones
Credit Analyst
+61 3 8641 0978

Distribution
Barbara Leong
Research Production Manager
+61 2 9237 8151

New Zealand
Stephen Toplis
Head of Research, NZ
+64 4 474 6905

Craig Ebert
Senior Economist
+64 4 474 6799

Doug Steel
Markets Economist
+64 4 474 6923

Kymberly Martin
Senior Market Strategist
+64 4 924 7654

Jason Wong
Currency Strategist
+64 4 924 7652

Yvonne Liew
Publications & Web Administrator
+64 4 474 9771

Asia
Christy Tan
Head of Markets Strategy/Research, Asia,
+ 852 2822 5350

Julian Wee
Senior Markets Strategist, Asia
+65 6632 8055

UK/Europe
Nick Parsons
Head of Research, UK/Europe, and Global Co-Head of FX Strategy
+ 44207710 2993

Gavin Friend
Senior Markets Strategist
+44 207 710 2155

Derek Allassani
Research Production Manager
+44 207 710 1532