CHINA'S ECONOMY AT A GLANCE

AUGUST 2016

CONTENTS

CONTACT

Gerard Burg, Senior Economist – Asia
+613 8634 2788
+61 477 723 768

KEY POINTS

China's real estate rebound is fading; authorities will require a new engine for growth in H2 2016 and 2017

- A rebound in real estate investment, new construction activity and industrial demand for related products – such as steel and cement – helped to underpin economic growth in the first half of 2016. This rebound is fading, with investment and new construction starts slowing, along with weaker trends for housing sales (in both value and floor space terms). The latest data doesn't change our forecasts for economic growth – 6.6% in 2016 and 6.5% in 2017 (with risks weighted to the downside for the latter) – with this slowing trend in line with our expectations.

- While most indicators were relatively stable in July, there was a marked slowdown in China's fixed asset investment – with growth down to 3.9% yoy (from 7.4% in June) – compared with double digit growth across the first four months of the year. State-owned enterprises (SOEs) have been driving fixed asset investment in recent months – counter to attempts to reform the sector and address widespread industrial overcapacity. In July, fixed asset investment by SOEs rose by 14% yoy (down from 24% in June), while non-state firm investment contracted by 1.0% yoy.

- Growth in China's industrial production eased slightly in July – down to 6.0% yoy (compared with 6.2% in June). Construction related industries have shown some weakening trends – with crude steel output in July around 5% lower than May, and growth in cement production slowing. In contrast, growth in electricity output accelerated and automotive production rose by 25% yoy.

- China's trade surplus was a little wider in July, at US$52.3 billion (compared with US$47.9 billion previously), as exports rose month-on-month while imports tracked sideways. In year-on-year terms, both exports and imports contracted – a trend evident since early 2015 that largely reflects falling prices.

- Trends for China's retail sales were a little softer in July – with growth easing to 10.2% yoy (from 10.6% in June). Retail price inflation has softened in recent months – down to just 0.3% yoy in both May and June (compared with 0.9% in February) – however it was likely to be strong enough to push real retail sales growth back below 10% yoy in July (our estimate is 9.9%).

- Headline inflation eased marginally in July, with the Consumer Price Index growing by 1.8% yoy – the slowest rate since December 2015. This was despite widespread flooding in southern China that had been expected to impact on the prices of key food products (including pork).

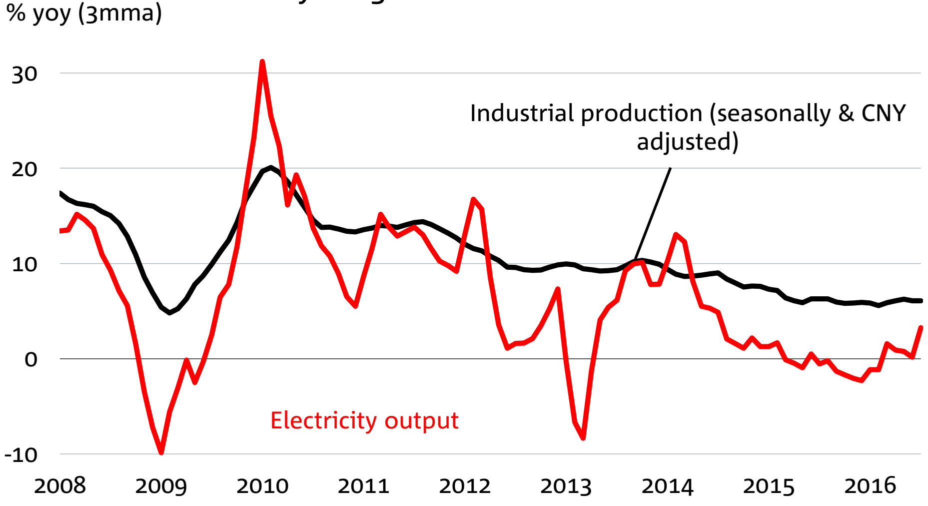
- Credit data was unavailable at the time of writing. As we noted last month, we expect the People's Bank of China to keep the benchmark one year lending rate unchanged for the remainder of 2016, although we see the potential for further cuts to the Required Reserve Ratio over this period.

National Australia Bank

INDUSTRIAL PRODUCTION

INDUSTRIAL PRODUCTION REMAINING STABLE

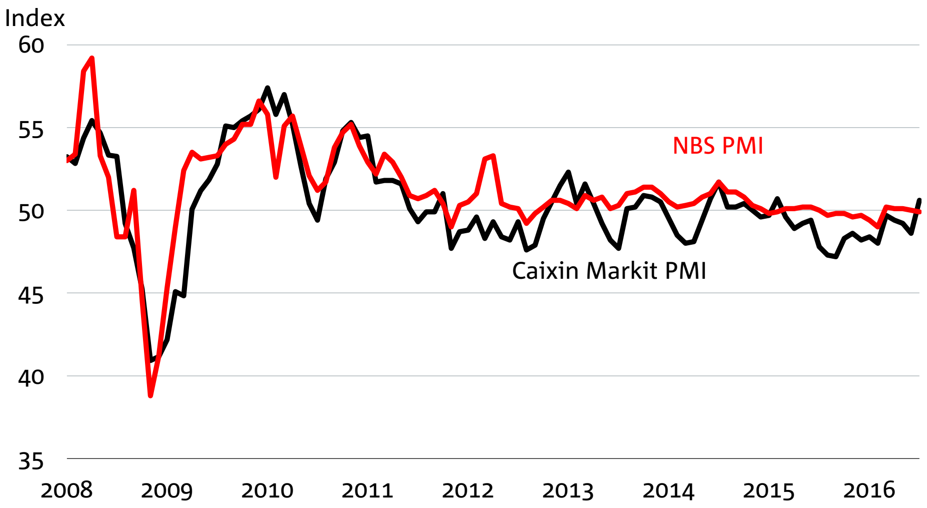
Autos and electricity surges as construction industries soften



Source: CEIC, NAB Economics

MIXED RESULTS FROM THE PMI SURVEYS

Caixin Markit measure turns positive for the first time since Feb '15



Source: CEIC, NAB Economics

- Growth in China's industrial production eased slightly in July – down to 6.0% yoy (compared with 6.2% in June). This was also slightly below market expectations – with the Bloomberg survey anticipating no change in the rate of growth.
- Construction related industries have shown weakening trends – with crude steel output in July around 5% lower than May (despite recording year on year growth of 2.6%). Similarly, the growth in cement slowed to 0.9% yoy (from 2.6% previously). In contrast, growth in electricity output accelerated – up to 7.2% yoy (from 2.1% in June) and automotive production rose by 25% yoy (from 8.1% last month).
- Trends in China's two main industrial surveys were quite mixed in July. The official NBS PMI edged marginally lower – to 49.9 points (from 50.0 points in June). In contrast, there was a strong improvement in the Caixin Markit PMI – which rose to 50.6 points (from 48.6 points previously). This was the first positive reading for the Caixin Markit measure since February 2015.

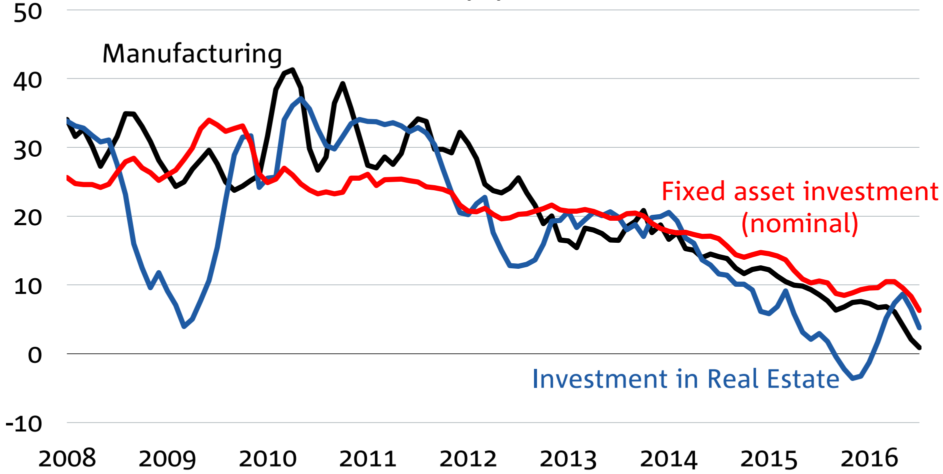
National Australia Bank

INVESTMENT

INVESTMENT TRENDS BY INDUSTRY

Real estate and manufacturing drag investment lower

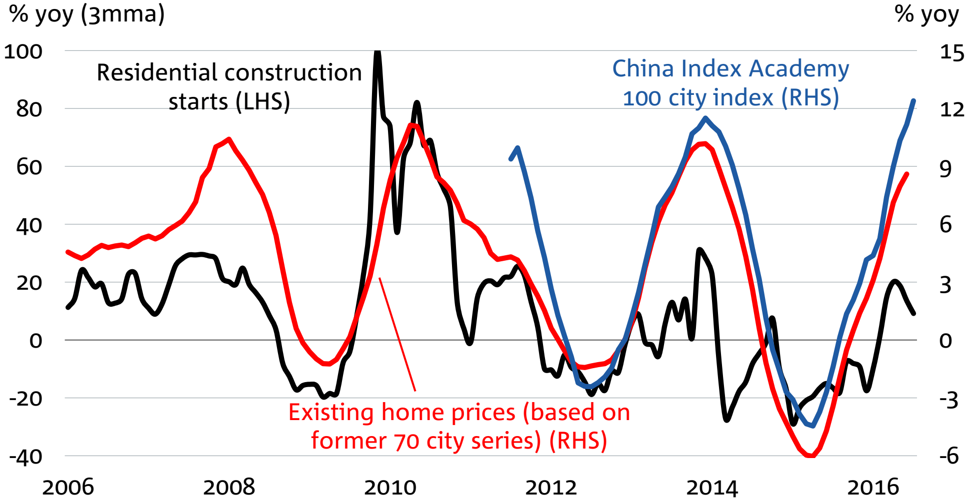
Growth in fixed asset investment (% yoy, 3mma)



Source: CEIC, NAB Economics

PROPERTY PRICES AND CONSTRUCTION STARTS

Construction starting to falter as real estate investment slows



Source: CEIC, Datastream, NAB Economics

- There was a marked slowdown in China's fixed asset investment in July – with growth down to 3.9% yoy (from 7.4% in June) – compared with double digit growth across the first four months of the year.

- State-owned enterprises (SOEs) have been driving fixed asset investment in recent months – counter to attempts to reform the sector and address widespread industrial overcapacity. In July, fixed asset investment by SOEs rose by 14% yoy (down from 24% in June), while non-state firm investment contracted by 1.0% yoy.

- Two key sectors for investment – manufacturing and real estate – have seen deteriorating trends more recently. On a three month moving average basis, manufacturing investment slowed to 0.9% yoy in July (from 2.1% in June), while investment in real estate slowed to 3.8% yoy (from 6.6% previously).

- The slowdown in real estate investment has been felt in the construction sector. Residential construction starts have slowed – down from 18.7% yoy growth in May to 9.2% yoy in July. This trend is consistent with our views that the rebound in construction activity across the first half of 2016 was unsustainable and suggests that the real estate growth is losing momentum.

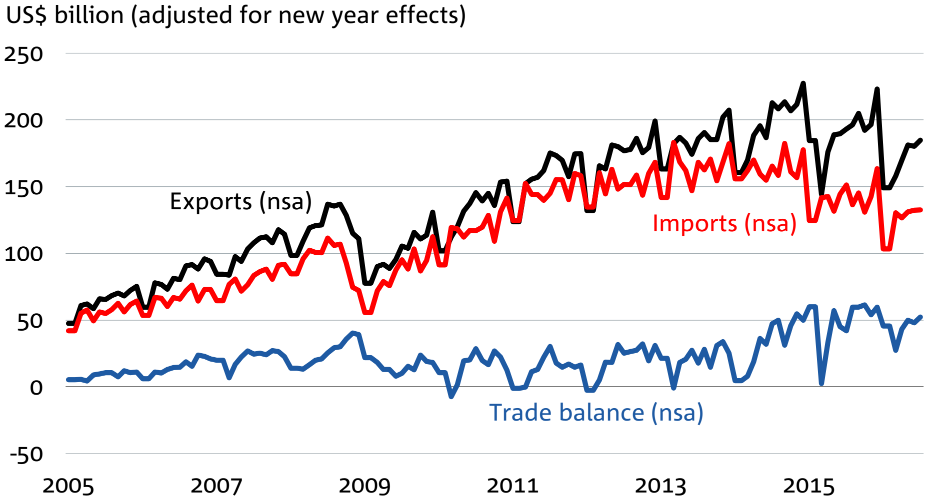
- That said, property price growth is continuing, with second tier city prices accelerating (1.5% mom in July) even as tier 1 city price growth appears to be slowing (1.8% mom in July, compared with 2.2% in May). Despite this upward trend, both the total value of housing sales and total floor space sold is slowing – albeit from comparatively high levels in recent months.

National Australia Bank

INTERNATIONAL TRADE – TRADE BALANCE AND IMPORTS

CHINA'S TRADE SURPLUS WIDENED IN JULY

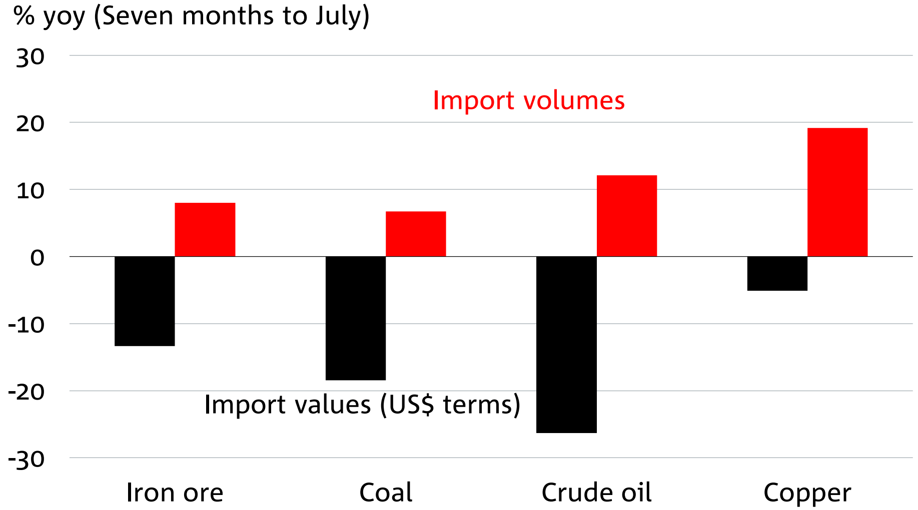
Driven by stronger exports and flat imports in monthly terms



Sources: CEIC, NAB Economics

IMPORT VOLUMES AND VALUES

Differing trends for key commodities highlights price effects



Source: CEIC, NAB Economics

- China's trade surplus was a little wider in July, at US$52.3 billion (compared with US$47.9 billion previously), as exports rose month-on-month while imports tracked sideways. In year-on-year terms, both exports and imports contracted – a trend evident since early 2015 that largely reflects falling prices.

- Import values fell by around 12.5% yoy in July, to total US$132.4 billion – a level that was largely unchanged from June. The growth rate was considerably weaker than market expectations – which were at around -7.0% yoy in the Bloomberg survey.

- Although weaker prices – particularly for commodities – explains much of the decline in import values in recent years, this appeared to be less of a contributor in July. The RBA Index of Commodity Prices fell by just 2.4% yoy in July – a considerably smaller decline than China's import values – likely indicating a drop off in volumes. It remains to be seen whether this was a one-off, or an indicator of upcoming industrial sector weakness.

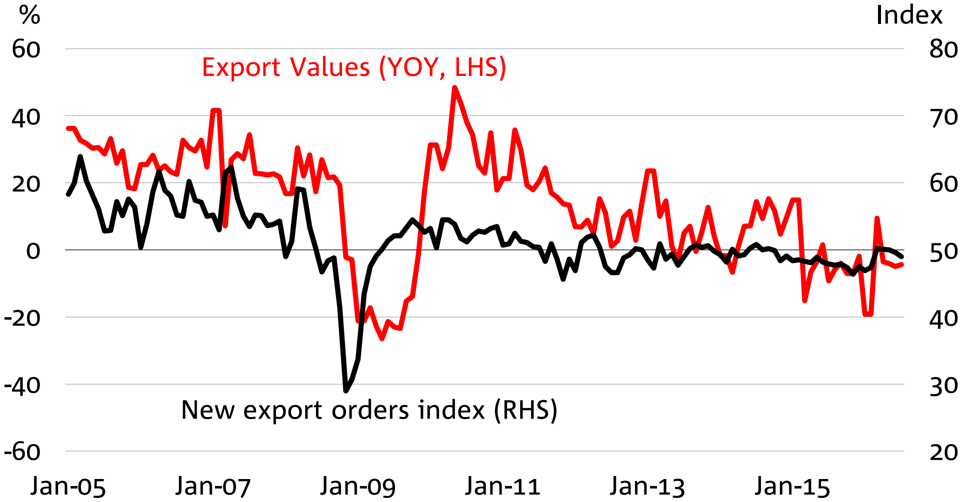
- The import volumes for key resource commodities generally rose in July – albeit less significantly than has been the case in recent months. Copper recorded the largest increase – at 3.4% yoy (down from 20% in June), while iron ore and crude oil rose by 2.7% yoy and 1.2% yoy respectively. Coal imports were around 0.2% lower in year-on-year terms, having risen by 31% yoy in June.

- Price effects are clearly evident in these key commodities, with considerable volume growth over the first seven months of 2016, in stark contrast to the decline in values.

INTERNATIONAL TRADE – EXPORTS

CHINA'S EXPORTS MODESTLY WEAKER YEAR-ON-YEAR

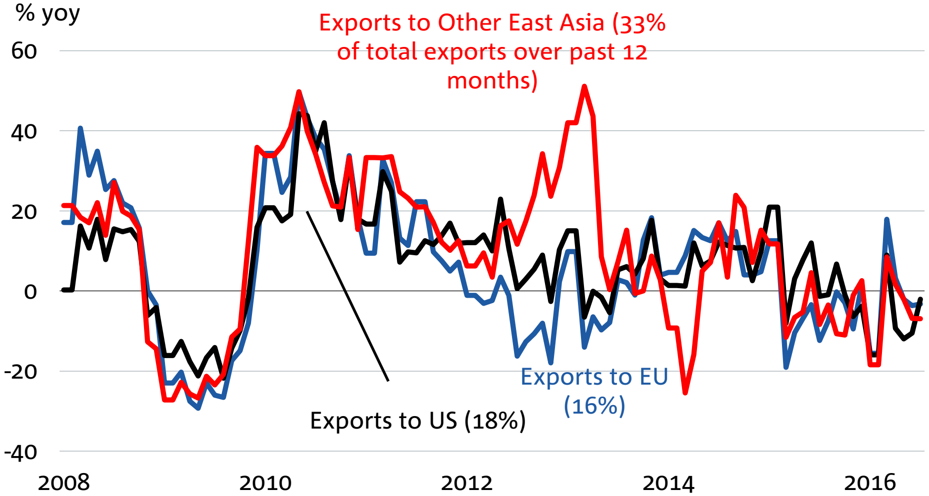
Surveyed new orders have declined in recent months



Source: CEIC, NAB Economics

EXPORTS TO MAJOR TRADE PARTNERS

East Asia led the declines in July, with US less negative



Sources: CEIC, NAB Economics

- The total value of China's exports rose month-on-month in July, up to US$184.7 billion (compared with US$180.2 billion previously). That said, this level still represented a decline of 4.4% yoy, broadly similar to market expectations of -3.5% yoy.

- The optimism of China's exporters has weakened marginally in recent months. The new export orders measure in the NBS PMI survey has eased to 49.0 points (from 49.6 points in June) – pushing further into negative territory. That said, these levels remain generally stronger than those recorded across the bulk of 2015.

- Export values fell for all of China's major trading partners – with the largest decline being to other Asian economies – down 6.9% yoy (compared with -6.8% in June). In contrast, exports to the European Union fell by 3.2% yoy and the United States by 2.0% yoy.

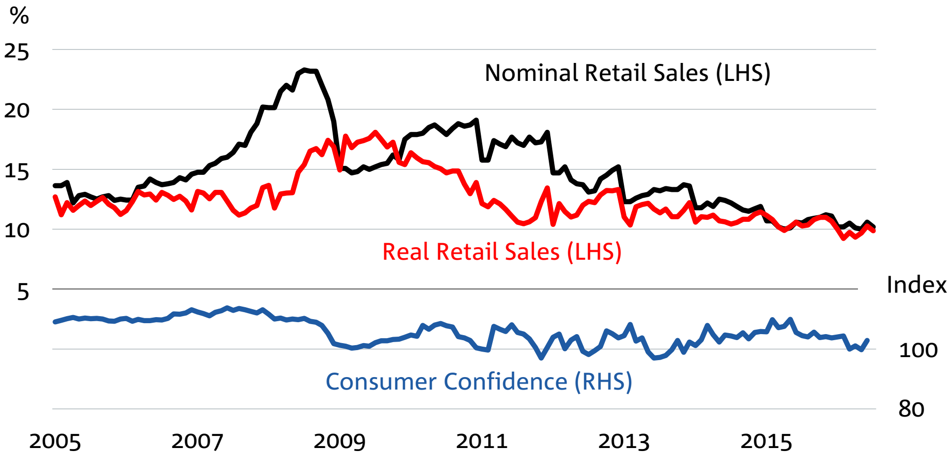
- East Asia is the largest market for China's exports – accounting for a third of the total). Exports to Hong Kong fell more rapidly than other Asian markets – down by 9.3% yoy. In contrast, other East Asia saw exports decline by 5.1% yoy – with steep declines in exports to Singapore and Taiwan.

National Australia Bank

RETAIL SALES AND INFLATION

RETAIL SALES GROWTH A LITTLE SOFTER IN JULY

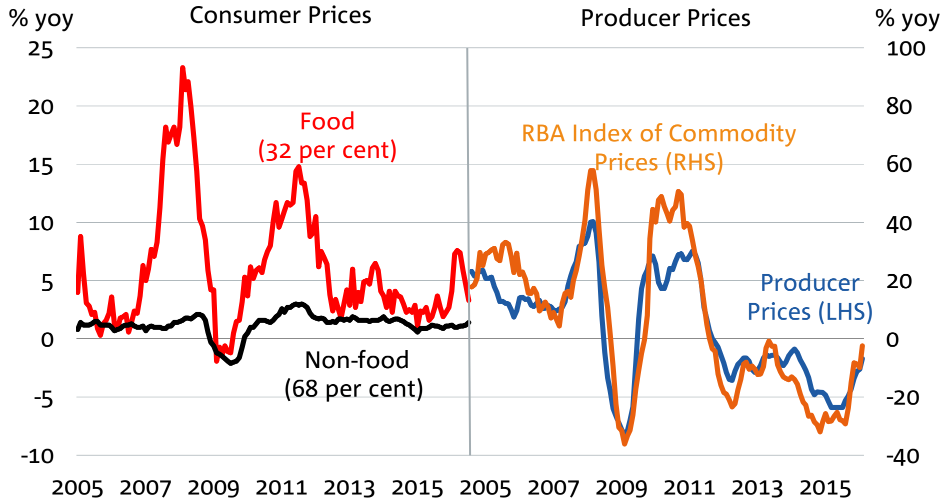
Inflation still relatively weak, but real sales dips below 10%



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

CONSUMER AND PRODUCER PRICES

Food prices softer despite flooding; producer prices up monthly



Sources: CEIC, RBA, NAB Economics

- Trends for China's retail sales were a little softer in July – with growth easing to 10.2% yoy (from 10.6% in June) – lower than market expectations. Retail price inflation has softened in recent months – down to just 0.3% yoy in both May and June (compared with 0.9% in February) – however it was likely to be strong enough to push real retail sales growth back below 10% yoy in July (our estimate is 9.9%).
- From a slight negative reading in May, consumer confidence improved in June – pushing up to 102.9 points. This measure has been trending broadly lower since May 2015.
- Headline inflation eased marginally in July, with the Consumer Price Index growing by 1.8% yoy (down from 1.9% yoy) – the slowest rate since December 2015.
- Food prices recorded slower growth in July – at 3.3% yoy (compared with 4.6% in June) – despite widespread flooding in southern China that had been expected to impact a range of key food products. Pork prices rose by 16% yoy – the lowest increase recorded this year. The floods may impact inflation trends in coming months.
- Non-food price inflation was somewhat stronger – rising by 1.4% yoy – the largest increase since August 2014. Fuel price deflation has softened in recent months – down 6.3% yoy in July (compared with 8.1% in June and 11.5% in May) – influencing the broader non-food price trend.
- Producer prices fell for the fifty-third straight month in July, however the rate of decline has continued to slow in recent months – in line with commodity price trends. The Producer Price Index fell by 1.7% yoy in July (compared with 2.6% previously). Producer prices have increased in monthly terms – with the index in July around 1.4% higher than in January.

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 Australian 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

National Australia Bank