

# CHINA ECONOMIC UPDATE NOVEMBER 2018



Hands in pockets: Chinese consumers are confident but that doesn't show up in retail sales data

NAB Group Economics

China's retail sales data are closely watched, providing something of a pulse check on the transition from industrial-led growth towards consumer-led growth. Recent months have seen a significant softening trend in retail sales – to the weakest levels in over fifteen years – despite measures of consumer confidence remaining near record highs. While there are some limitations with the retail sales measure, these don't appear to explain this disconnect.

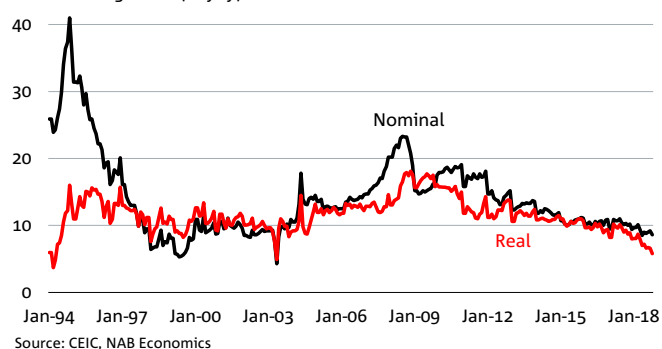
## WHAT IS THE DATA SHOWING?

Nominal retail sales grew by 8.6% yoy in October – marginally above the recent fifteen year low of 8.5% yoy in May 2018. Overall growth in retail sales has been generally trending downwards since peaking in mid-2008, dropping below double-digit rates in late 2017. When adjusted for retail price inflation, the slowdown in retail sales has been a little stronger – with growth at just 5.8% yoy in October, the weakest rate of growth since May 2003 and slower than the overall rate of growth of the economy in the third quarter.

## CHINA RETAIL SALES SLOWING

### Real sales weakest since May 2003

Retail sales growth (% yoy)



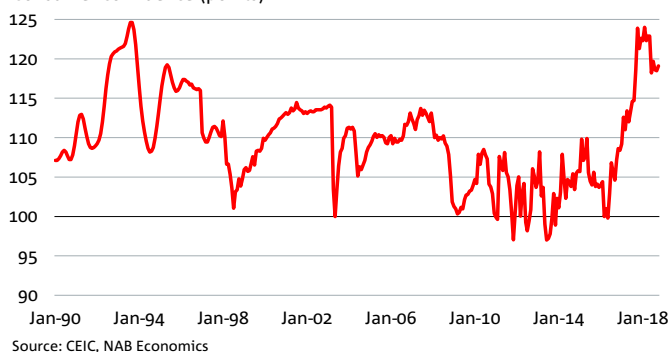
Among larger retailers – who account for a sub-set of the overall total – the slowdown in sales appears to be driven by weakness in the auto sector (which have fallen significantly year-on-year in recent months). However it is not clear that these declines are large enough to explain the slowdown across the broader retail space.

The weakness in retail sales data is in stark contrast to the strength in consumer confidence. The measure produced by the National Bureau of Statistics (NBS) started to strengthen from neutral levels in the early months of 2016, reaching its highest levels in almost a quarter of a century in February 2018 – at 124.0 points. While confidence has eased since this time, the level recorded in October – 119.1 points – remains historically high.

## CONSUMER CONFIDENCE REMAINS HIGH

### Current levels a little off 25 year high

Consumer confidence (points)



This positive consumer confidence measure is supported by private sector surveys. The Bankcard Consumer Confidence Index, produced by news agency Xinhua and financial services provider China UnionPay, peaked in July 2018 and has edged lower since, but remains above any reading between 2010 and 2017. Similarly, the quarterly Nielsen China Consumer Confidence Index was a little softer in Q2 2018, however the level recorded in Q1 2018 was its ten year high.

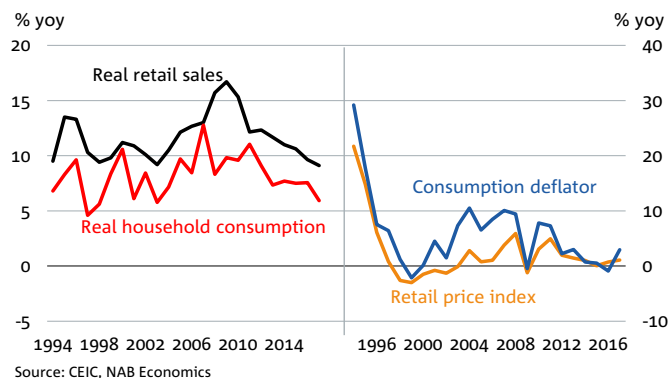
## WHAT ARE RETAIL SALES ACTUALLY MEASURING?

According to the NBS, the retail sales measure covers purchases by both households and the public sector, across a selection of goods and services – including retail sales by both wholesalers and retailers, catering services, publishing, postal and telecommunications services, as well as “other” services. The NBS provides no breakdown between public and private retail purchases.

The inclusion of the public sector means that the retail sales measure is broader than household consumption of goods, while the exclusion of a range of other goods and services (with Bloomberg noting that it excludes online sales, travel, education and healthcare) means it is narrower than total consumption. The annual increase in real household consumption – a component of China’s GDP by expenditure – has been consistently weaker than the growth in real retail sales. It is worth noting that price effects may contribute to this divergence, with the consumer deflator and retail prices differing (likely due to the wider coverage of goods and services in household consumption).

## RETAIL SALES VERSUS CONSUMPTION

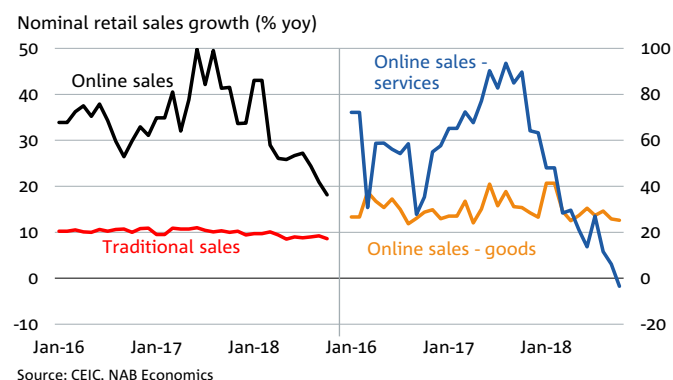
### Differing price trends one factor



The exclusion of online retailing from the broader retail sales data is potentially problematic as an indicator of household trends – given the rapid growth in this industry over the past few years. Online sales of goods and services have grown strongly (albeit from a small base) – increasing by almost 40% in 2017. The rate of growth has slowed this year (down to 18.2% yoy in October) led by the services component but remains much stronger than traditional retail sector. In the first ten months of the year, online retail sales were almost 23% of the traditional total – highlighting how rapidly Chinese consumers have embraced this medium.

## CHINESE ONLINE RETAIL

### Sales outpace traditional retail



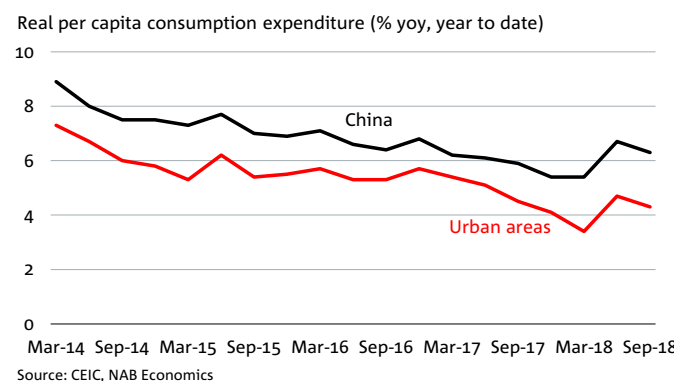
## WHAT IS DRIVING THE DOWNTURN IN SALES?

The lack of a breakdown between public and household consumption means that we don’t have a clear picture as to what exactly is driving the slowdown in retail sales. It is possible, for example, that the tighter financial conditions (created by the deleveraging program evident in the first half of the year) may have impacted public sector purchases of goods and services, but the impact on the aggregate sales is unclear. Similarly, household purchases may have been impacted by restrictions around non-bank finance.

Alternative indicators also appear to show a slowing in household consumption in recent years. According to the NBS Household Survey, growth in real per capita consumption has trended lower since the start of 2014 – increasing by 6.3% yoy in the first three quarters of 2018 (compared with almost 9% in Q1 2014). It is worth noting that growth in 2018 has been stronger than 2017, but growth is starting to slow again. The slowdown has been more stark in urban than rural areas – with an increase of just 4.3% yoy in urban expenditure over this period.

## CHINESE ONLINE RETAIL

### Sales outpace traditional retail



The survey provides a breakdown of expenditure by category on a nominal basis and highlights the outsized growth in spending on healthcare and residence costs – reflecting the surge in property prices in recent years (particularly in China’s largest cities). These expenses limit discretionary spending elsewhere – which has likely contributed to the slowdown recorded in retail sales. Chinese authorities introduced income tax cuts at the start of October, with further measures to commence in January, however it remains to be seen whether this will directly boost consumption – given the increase in household debt in recent years, along with high rates of saving.

## CONCLUSIONS

The lack of disaggregation in retail sales data – particularly between public and household purchases and the exclusion of some key service sectors – means that the measure does not provide a sufficient clarity around trends in private consumption. That said, the underlying trends in retail sales at least point towards the direction of consumption, providing a more timely indicator than either the annual expenditure measure in GDP or quarterly survey results.

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