CHINA'S ECONOMY AT A GLANCE

DECEMBER 2018

National Australia Bank

CONTENTS

CONTACT

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KEY POINTS

Weaker indicators point to slowing economic growth in Q4

- There was a broadly negative trend in China's data in November. Industrial production was at a post-GFC low, trade activity slowed noticeably and the retail sector remains subdued. Combined, these indicators point to slowing economic growth in Q4 – albeit within the bounds of our forecasts. Our forecasts remain unchanged, with China's economy growing by 6.6% in 2018, down to 6.25% in 2019 and 6.0% in 2020.

- China's industrial production growth slowed considerably in November – increasing by 5.4% yoy (compared with 5.9% in October). This was well below market expectations, and was the same growth recorded in the January-February period in 2016, which was the weakest rate recorded since the GFC. China's main manufacturing surveys highlight broadly neutral conditions in the industry at present, with export orders particularly weak.

- China's nominal fixed asset investment grew a little more slowly in November. However, the sharp downturn in producer prices – which flow through into investment goods – meant that real investment growth increased, up by 5.6% yoy, from 5.3% in October.

- There was a marked slowdown in the growth rates of China's exports and imports in November, which may reflect the deterioration in the global trading environment (following the dispute between the US and China). Some of the slowdown in exports may also reflect timing impacts of US tariffs – with purchases brought forward ahead of the second round of measures in late September subduing more recent demand. The outlook from here is highly uncertain.

- In real terms, China's retail sales growth edged marginally higher in November – to 5.8% yoy (from 5.6% in October), a historically weak result. As highlighted in our detailed article last month, this measure includes public and private business spending, meaning that the slowdown could be linked to trends other than household consumption. This may explain why consumer confidence has remained firm. The measure was stronger in October – at 119.1 points (compared with 118.5 points previously). While off the peaks of early 2018, confidence has remained well above the levels seen over the previous decade.

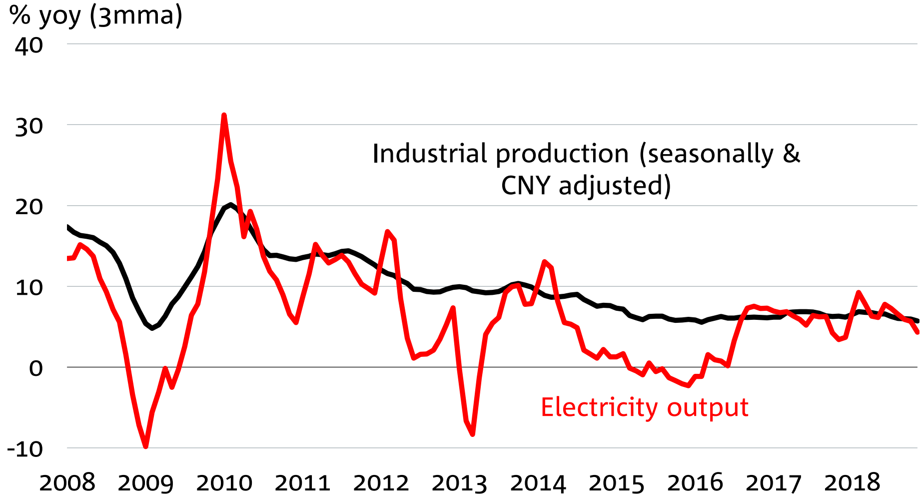
- New credit issuance remained weak in November, with lending falling by around 20% yoy. The continued declines in new issuance suggests that Chinese authorities are yet to introduce widespread stimulus in response to US tariffs, implying that the need to address corporate debt concerns remain a priority.

- Following the considerable volatility exhibited across the third quarter, the 7 day Shanghai Interbank Offered Rate (Shibor) has become far more stable recently – since the start of November, it has traded in a band of less than 10 basis points around the 2.6% mark. This represents an easing of around 25 basis points from the early 2017 to mid 2018 period. This appears to be the target rate for the Shibor in the short term, however the general tightening trend in monetary policy globally may present some upside risk going forward.

INDUSTRIAL PRODUCTION

INDUSTRIAL PRODUCTION

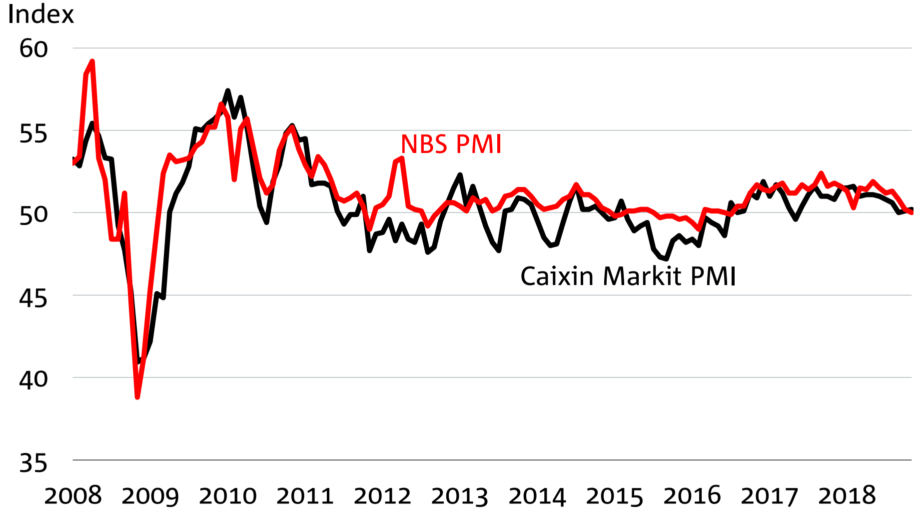
Growth at post GFC lows, with very mixed trends by sub-sector



Source: CEIC, NAB Economics

PMI SURVEYS AT NEUTRAL LEVELS IN NOVEMBER

Export order measures remain firmly negative



Source: CEIC, NAB Economics

- China's industrial production growth slowed considerably in November – increasing by 5.4% yoy (compared with 5.9% in October). This was well below market expectations, and was the same growth recorded in the January-February period in 2016, which was the weakest rate recorded since the GFC.
- Trends in the manufacturing sector remain highly divergent. Crude steel output fell month-on-month – as winter capacity closures start to impact output – but increased around 10.2% yoy. In contrast, cement production rose by just 1.6% yoy.
- Production of consumer electronics (such as mobile phones and computers) grew a little more modestly – up by 12.3% yoy (compared with 14.6% yoy previously). Electricity output rose by 3.6% yoy (down from 4.8% yoy in October). Production of motor vehicles has continued to fall, down 16.7% yoy.
- China's main manufacturing surveys highlight broadly neutral conditions in the industry at present. The official NBS PMI survey fell to 50.0 points in November (from 50.2 points previously). In contrast, the Caixin Markit PMI was marginally stronger – up to 50.2 points (from 50.1 points in October) – but still a barely positive result.
- Both surveys have exhibited a deterioration in new export orders over recent months – the clearest impact of the US-China trade tensions in any of China's data. The NBS survey measure marginally improved in November – albeit remaining firmly in negative territory – while the Caixin Markit measure has been below the 50 point mark for eight months in a row.

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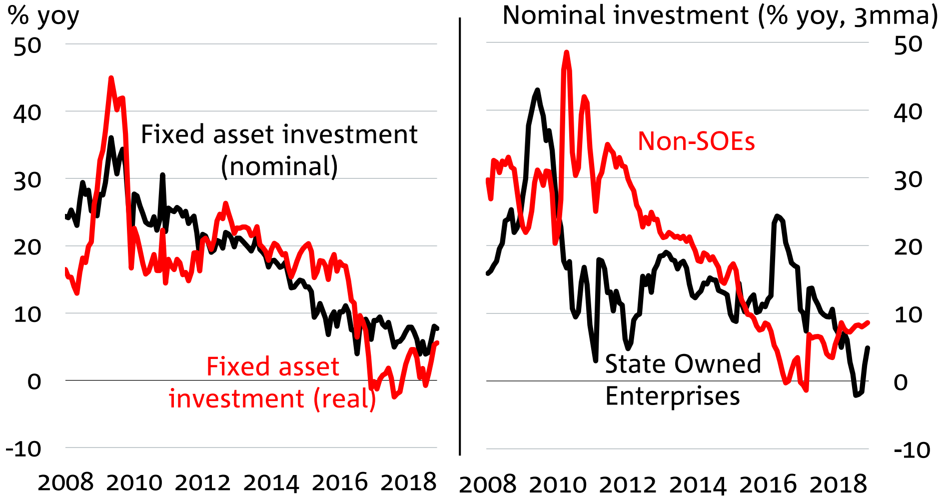
INVESTMENT

FIXED ASSET INVESTMENT

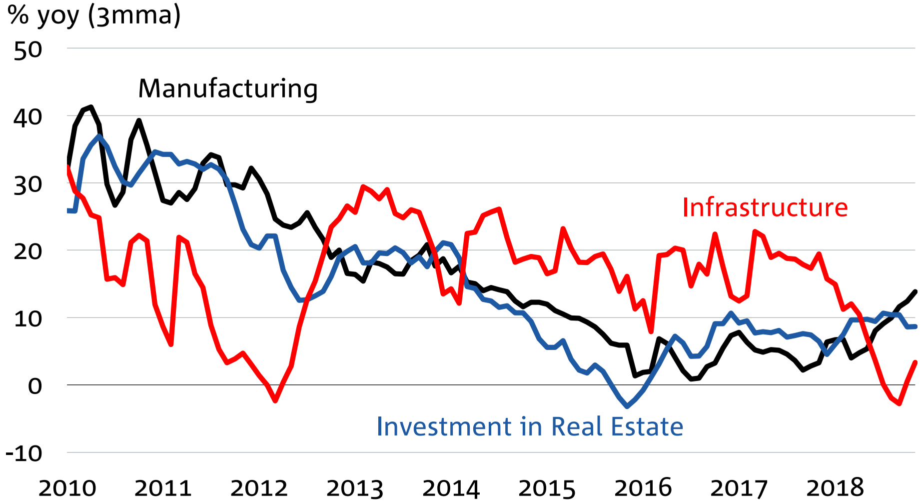
Real investment edges higher; private investment growing stronger



Source: CEIC, NAB Economics

FIXED ASSET INVESTMENT BY SECTOR

Infrastructure investment starting to recover



Source: CEIC, NAB Economics

- China's fixed asset investment grew a little more slowly in November – increasing by 7.7% yoy (down from 8.0% previously). Despite this weaker growth, it remained stronger than the rates recorded between March and September. However, the sharp downturn in producer prices – which flow through into investment goods – meant that real investment growth increased, up by 5.6% yoy, from 5.3% in October.

- Private sector firms have accounted for the bulk of nominal investment growth this year – with investment by state-owned enterprises (SOEs) falling year-on-year during the third quarter. That said, investment by SOEs has accelerated in the past two months – resulting in an increase in November of 4.9% yoy (on a three month moving average basis). In contrast, investment by private firms has grown at a relatively stable rate, up by 8.6% yoy (3mma) in November, from 8.3% yoy previously.

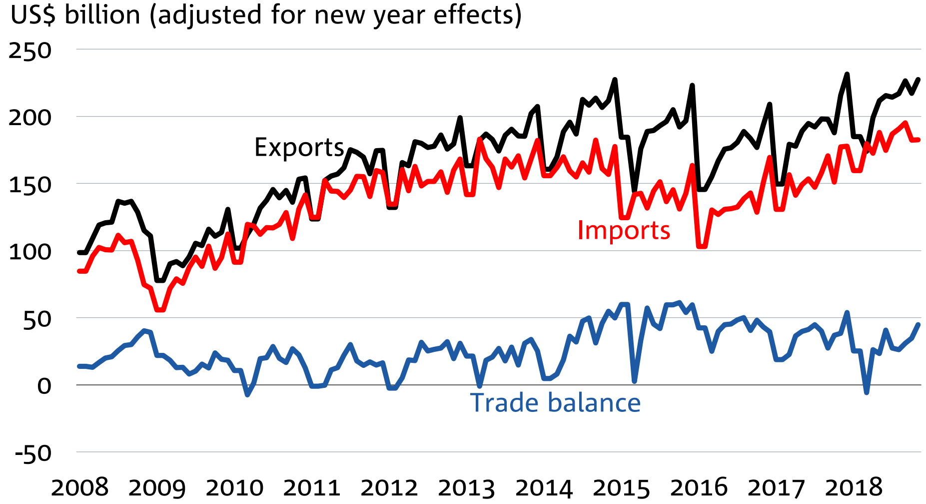
- Trends in investment by industry remain highly mixed. Infrastructure investment – which had been particularly strong between late 2012 and late 2017 – slowed significantly across much of 2018, turning negative in August and September. This was likely linked to the deleveraging campaign impacting the funding capacity of local governments. In recent months, growth has returned, albeit modestly – at 3.3% yoy (3mma) in November.

- In contrast, investment in manufacturing has continued to accelerate – up by 13.9% yoy (3mma) in November (from 12.4% yoy previously). Growth in real estate investment has remained relatively stable recently, increasing by 8.6% yoy (3mma), unchanged from October.

INTERNATIONAL TRADE – TRADE BALANCE AND IMPORTS

TRADE SURPLUS WIDER IN NOVEMBER

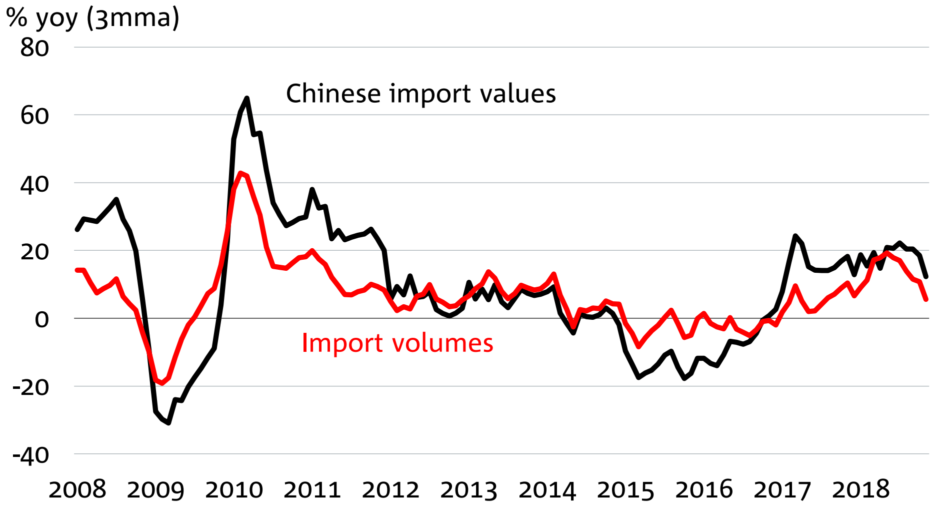
Exports and imports grew more slowly this month



Sources: CEIC, NAB Economics

IMPORT GROWTH SLOWED SHARPLY IN NOVEMBER

Falling import volumes the key driver



Source: CEIC, NAB Economics

- There was a marked slowdown in the growth rates of China's exports and imports in November, which may reflect the deterioration in the global trading environment (following the dispute between the US and China), however the outlook from here is highly uncertain . Given a larger slow down in imports, China's trade surplus widened in November, to US$44.7 billion.

- As we have previously noted, the bulk of this trade surplus is with the United States. Imports from the US fell sharply in year-on-year terms, down 25% to US$10.7 billion. Combined with an increase in China's exports to the US, the trade surplus totalled US$35.6 billion. In addition to China's retaliatory tariffs, currency movements may explain some of the reduced demand for US goods. In November, the Yuan was around 4.8% weaker in year-on-year terms – increasing the cost of US goods for Chinese consumers.

- China's imports were largely unchanged month-on-month in November, totalling US$182.7 billion, compared with US$182.3 billion previously. This was a modest increase of 3.0% yoy – well below the average increase of around 20% yoy in the first ten months of 2018.

- Our estimate of import volumes declined sharply in November – suggesting that the slowing growth was driven more by volumes than price trends. On a three month moving average basis, volumes rose by 5.6% yoy – compared with a double digit trend across the bulk of 2018.

- The import trends for key commodities were generally negative – with the exception of crude oil, where volumes increased by 15.7% yoy to 42.9 million tonnes (a new monthly record level). In contrast, iron ore imports fell 8.8% yoy (as a restocking phase came to an end ahead of winter steel capacity closures), coal imports declined by 13.1% yoy and copper imports fell 3.0% yoy.

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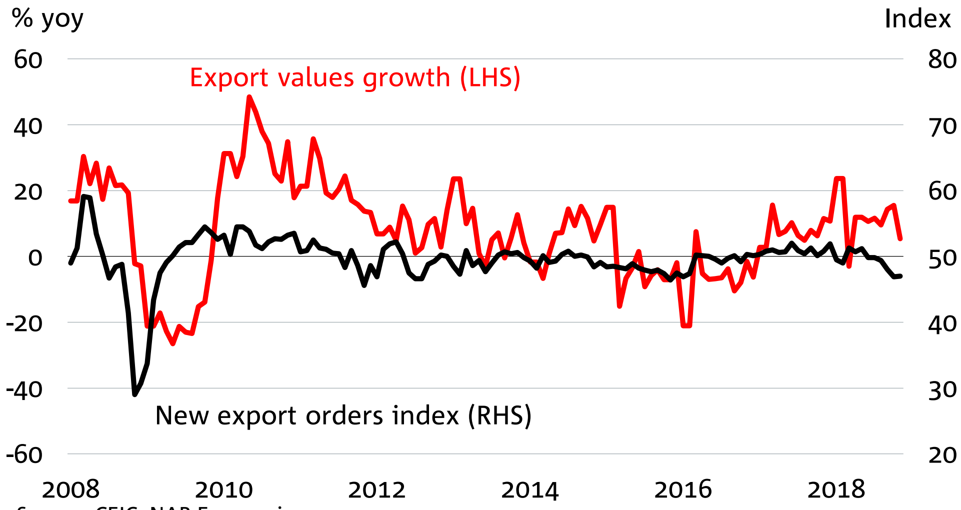
INTERNATIONAL TRADE – EXPORTS

CHINA'S EXPORT VALUES AND NEW ORDERS

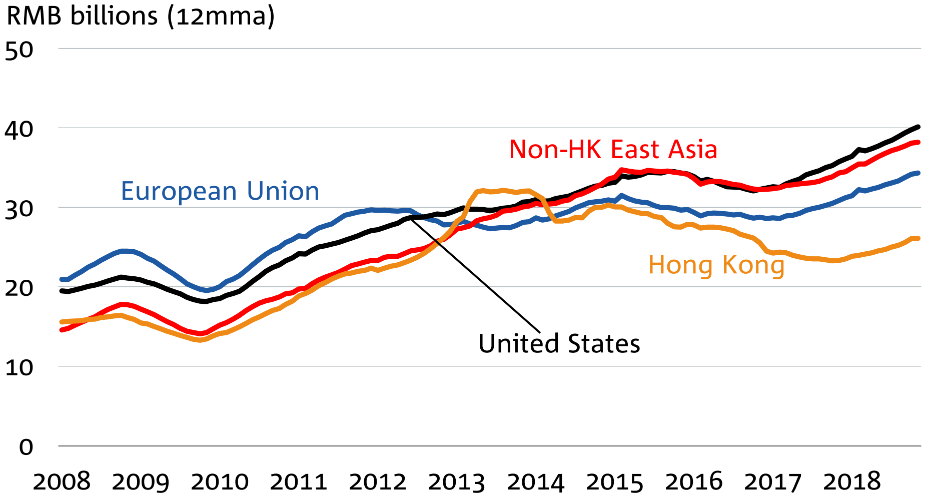
PMI export orders in firmly negative territory



Source: CEIC, NAB Economics

EXPORTS TO MAJOR TRADING PARTNERS

Exports to US continue to grow, despite tariff measures



Sources: CEIC, NAB Economics

- Growth in China's exports slowed considerably in November – increasing by 5.4% yoy to US$227.4 billion (compared with US$217.1 billion in October – a typically weaker month due to the Golden Week holidays). New export orders in the NBS PMI survey were marginally improved in November, although still firmly negative at 47.0 points (from 46.9 points in October).

- Some of the slowing export growth may reflect timing impacts of US tariffs – with purchases brought forward ahead of the second round of measures in late September subduing more recent demand. It is possible that a another wave of forward purchases could occur, should the proposed increase in tariffs from 10% to 25% occur at the end of the 90 day "ceasefire" period.

- There was some divergence in terms of exports to major markets – with the strongest growth recorded in the United States (despite tariff measures). Exports to the US increased by 9.8% yoy – albeit this was down from 13.2% yoy in October.

- In contrast, exports to the European Union grew by 6.0% yoy in November, while exports to East Asian markets rose by just 3.1% yoy. There was minimal difference between growth in exports to Hong Kong (2.7% yoy) and Other East Asia (3.5% yoy) – with the largest increases in Indonesia and Taiwan, while exports to Korea fell year-on-year.

- In recent months there has been a growing discrepancy between export data reported by Hong Kong and China. In the first ten months of 2018, China's reported exports to Hong Kong exceeded Hong Kong's imports from China by over US$18 billion (equivalent to around 7% of China's exports to Hong Kong). During the same period in 2017, the difference was just US$7.3 billion. An increase in this discrepancy can indicate an increase in unauthorised capital flows (which are hidden as trade flows).

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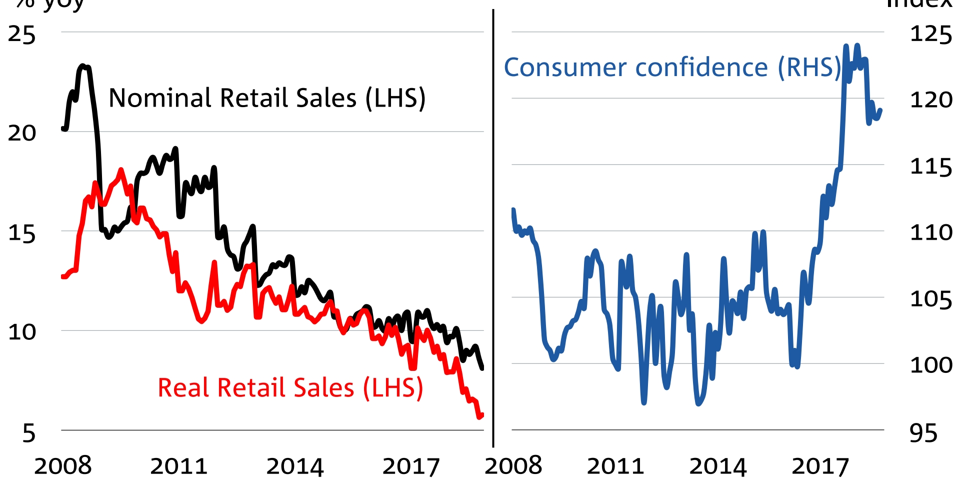
RETAIL SALES AND INFLATION

MARGINAL UPTURN IN REAL SALES IN NOVEMBER

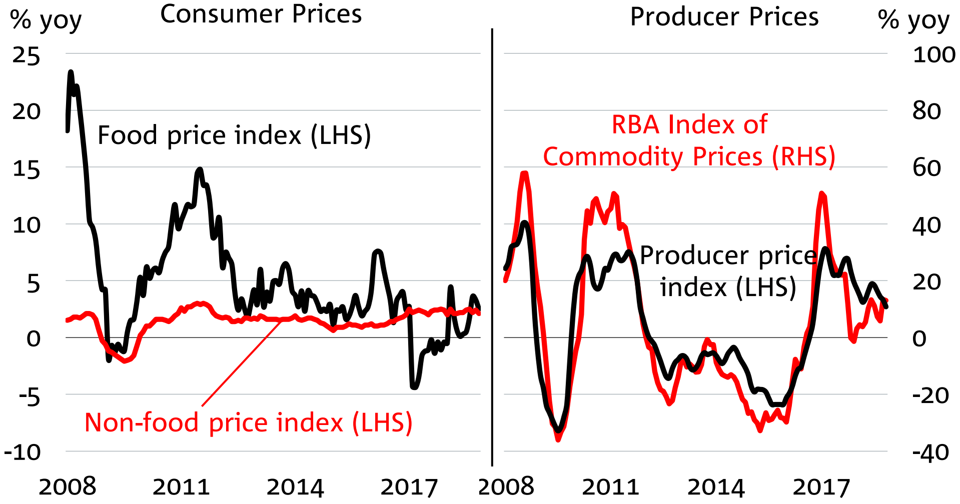
Weakness in retail sales contrasts with strong confidence



Source: CEIC, NAB Economics

CONSUMER AND PRODUCER PRICES

CPI weaker; PPI down with closer relationship to commodities



Source: CEIC, RBA, NAB Economics

- In nominal terms, there was a further slowdown in China's retail sales growth in November – with sales increasing by 8.1% yoy (compared with 8.6% yoy previously). Retail price inflation was somewhat softer in November, meaning that real retail sales growth edged marginally higher – to 5.8% yoy (from 5.6% in October). As highlighted in our detailed article last month, this measure includes public and private business spending, meaning that the slowdown could be linked to trends other than household consumption.

- This may explain why consumer confidence has remained firm. The measure was stronger in October – at 119.1 points (compared with 118.5 points previously). While off the peaks of early 2018, confidence has remained well above the levels seen over the previous decade.

- China's headline inflation was a little weaker in November, with the Consumer Price Index increasing by 2.2% yoy (compared with 2.5% in October).

- Food prices increased more modestly in November, up by 2.5% yoy (compared with 3.3% previously). A sharp decline in fresh vegetable inflation – down from 10.1% yoy to 1.5% yoy – was a major driver.

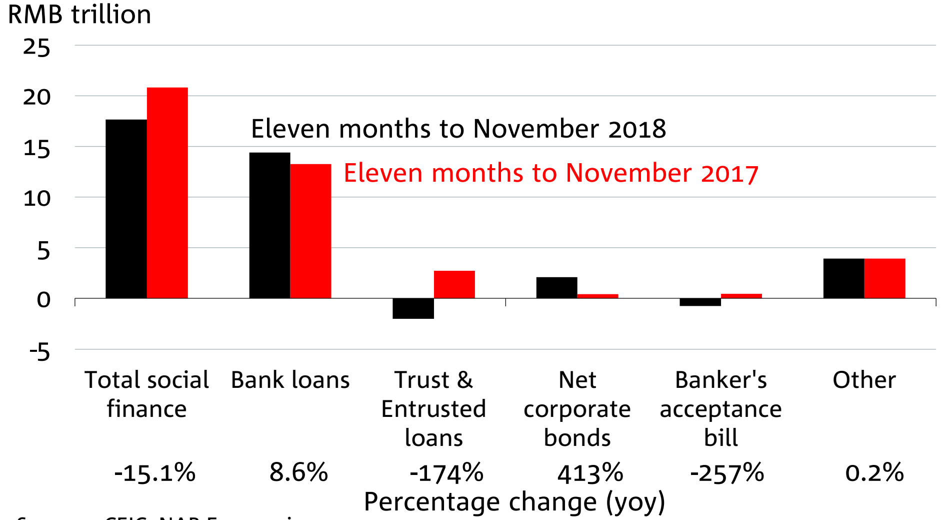
- There was also a slowdown in non-food price growth in November – with an increase of 2.1% yoy, compared with 2.4% previously. Vehicle fuel prices rose less significantly than previously, increasing by 12.6% yoy (versus 22.0% yoy in October). In contrast, healthcare inflation was stable – at 2.6% yoy, while residence expenses edged down – to 2.4% yoy compared with 2.5% previously.

- Producer prices rose by 2.7% yoy in November (down from 3.3% previously), the lowest increase recorded since October 2016. The relationship between producer prices and global commodity prices has become closer in recent months – following a sustained break from mid-2017 to mid-2018.

CREDIT CONDITIONS

NEW CREDIT ISSUANCE

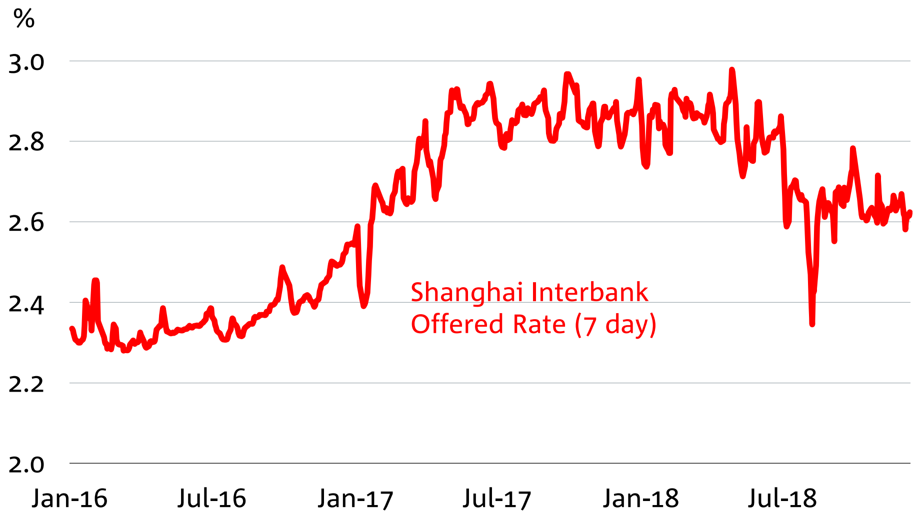
Non-bank lending has continued to contract sharply



Sources: CEIC, NAB Economics

SHIBOR HAS STABILISED FOLLOWING RECENT VOLATILITY

Greater stability across November and early December



Source: CEIC, NAB Economics

- New credit issuance remained weak in November, with lending falling by around 20% yoy. The continued declines in new issuance suggests that Chinese authorities are yet to introduce widespread stimulus in response to US tariffs, implying that the need to address corporate debt concerns remain a priority.

- In the first eleven months of 2018, new credit issuance totalled RMB 17.7 trillion, a 15% yoy decline. Bank lending has continued to increase – up by 8.6% yoy to RMB 14.4 billion, around 82% of the total. The decline in new issuance has been driven by the crackdown on the shadow banking sector – with tighter regulation over the financial sector constraining growth.

- Overall, non-bank lending fell by 57% yoy to RMB 3.3 trillion in the first eleven months. Major parts of the shadow banking sector (such as trust & entrusted loans and banker's acceptance bills) have contracted on a net basis. In contrast, there has been strong growth in corporate bond issuance – up by over 400% yoy – albeit this was an increase from a very small amount in 2017.

- Following the considerable volatility exhibited across the third quarter, the 7 day Shanghai Interbank Offered Rate (Shibor) has become far more stable recently – since the start of November, it has traded in a band of less than 10 basis points around the 2.6% mark. This represents an easing of around 25 basis points from the early 2017 to mid-2018 period.

- This appears to be the target rate for the Shibor in the short term, however the general tightening trend in monetary policy globally may present some upside risk going forward. Looser policy rates increase the risk of capital flight (which could threaten the stability of financial markets) and increase growth in debt – undermining what has been achieved in the deleveraging program.

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