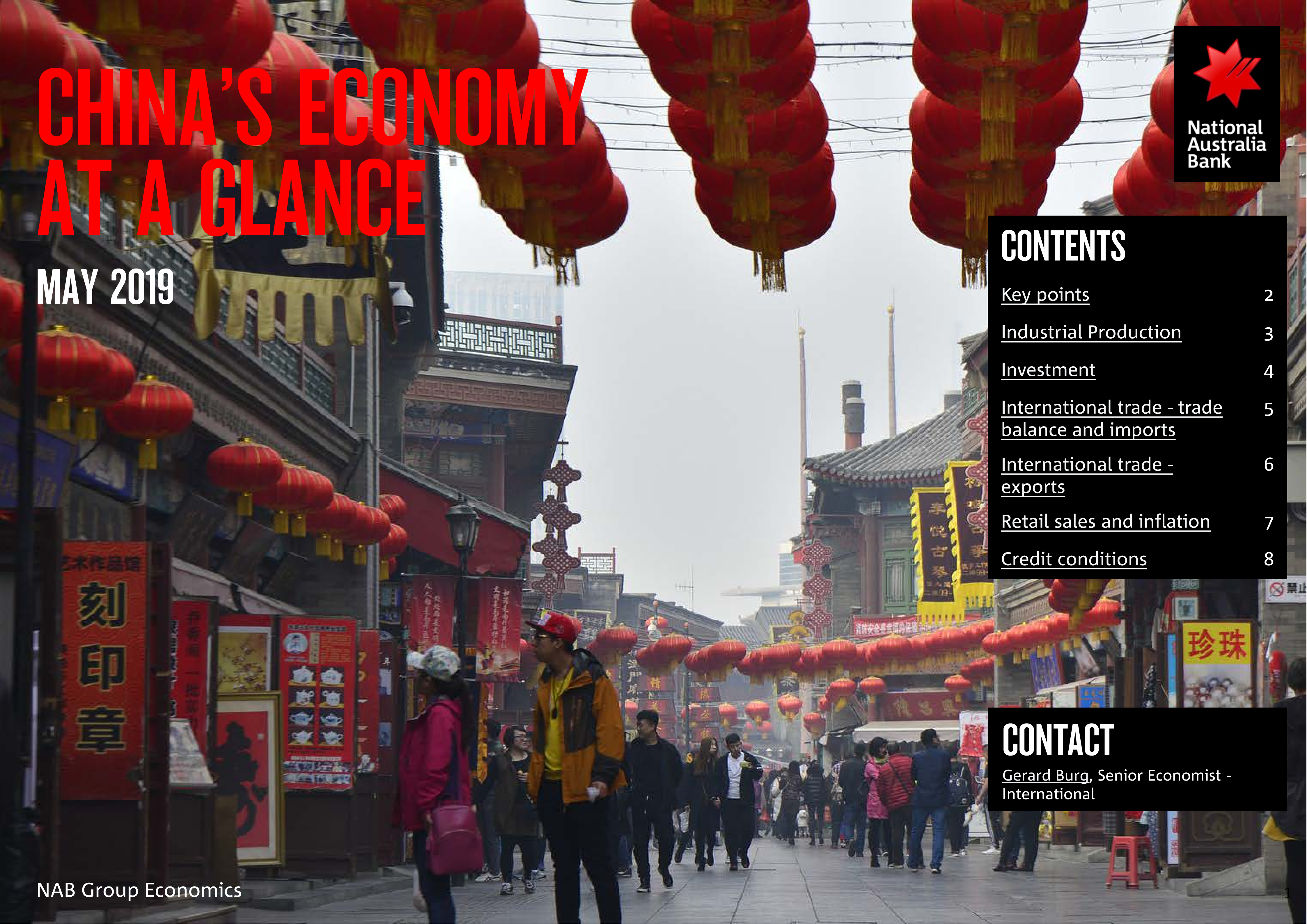

CHINA'S ECONOMY AT A GLANCE

MAY 2019

National Australia Bank

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CONTACT

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NAB Group Economics

KEY POINTS

Weaker economic trends even before trade tensions heat up again

- Most of China's economic indicators were a little weaker in April, and this was prior to the increase in trade tensions with the United States in early May. The increase in rates on the second phase of US tariffs (from 10% to 25% on around US$200 billion worth of goods) and likely public hearings on the third and final phase are a negative for the manufacturing sector and the broader economy as a whole. The trade relationship remains highly uncertain (given that an agreement could still be reached) as is the domestic policy response, meaning that our economic growth forecasts are unchanged for now – at 6.25% this year, 6.0% in 2020 before dipping below 6% in 2021.

- China's industrial production increased by 5.4% yoy in April – down from an unusually strong 8.5% yoy in March (which was likely related to one-off factors). PMI surveys are near neutral levels, with export order indicators still weak prior to the latest trade tension escalation.

- Real fixed asset investment growth slowed to 4.9% yoy (from 6.1% in March). This slowdown has largely been driven by private sector firms, where growth has eased. In contrast, investment by state-owned enterprises has accelerated in recent months.

- A fall in exports (both month-on-month and year-on-year) and an increase in imports led to a narrowing in China's trade surplus in April. The surplus totalled US$13.8 billion, the weakest result since the surprise trade deficit recorded in March 2018. Tariff measures introduced by both countries has slowed growth in exports to the United States and imports from the United States.

- Growth in real retail sales slowed significantly in April – down to 5.1% yoy (from 6.7% previously). This was the weakest rate of growth since May 2003. Despite the weak rate of growth of real retail sales, China's consumer confidence has remained at high levels. In March, confidence dipped marginally to 124.1 points (off an all time high of 126 points in February).

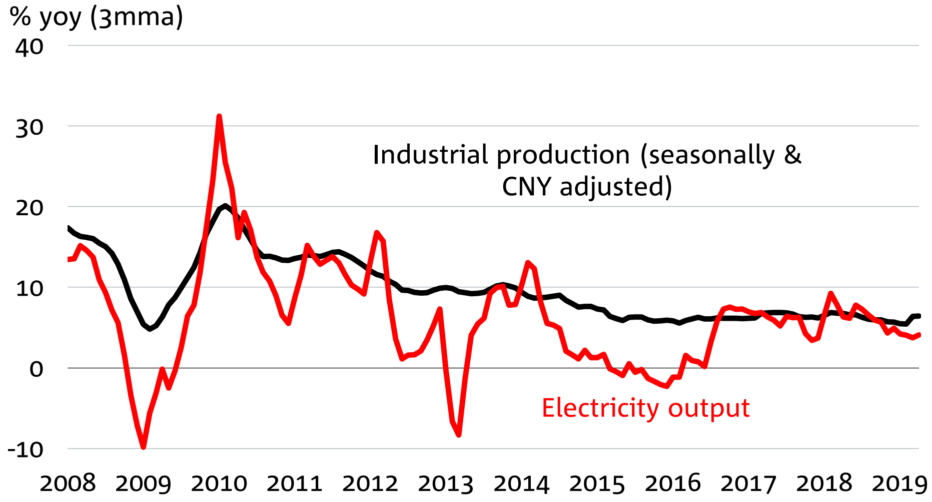
- China's new credit issuance has remained strong in the early months of 2019 – suggesting that authorities are seeking to support growth in the short term. Public statements from regulators suggest that deleveraging is now less of a priority (compared with comments from late last year that the program would continue), however it remains to be seen whether the program will resume once they are satisfied that growth has stabilised.

- The current period of volatility in short term interbank rates has continued. From the start of April through to mid-May, the 7 day Shanghai Interbank Offered Rate (Shibor) has traded in a 50 basis point trading range. Since the start of this year (as volatility in near term interbank rates has increased), there has been a notable decline in longer term rates. Compared to this time last year, there has been a decline of around 120 basis points for both 3 month and 12 month rates.

INDUSTRIAL PRODUCTION

INDUSTRIAL PRODUCTION

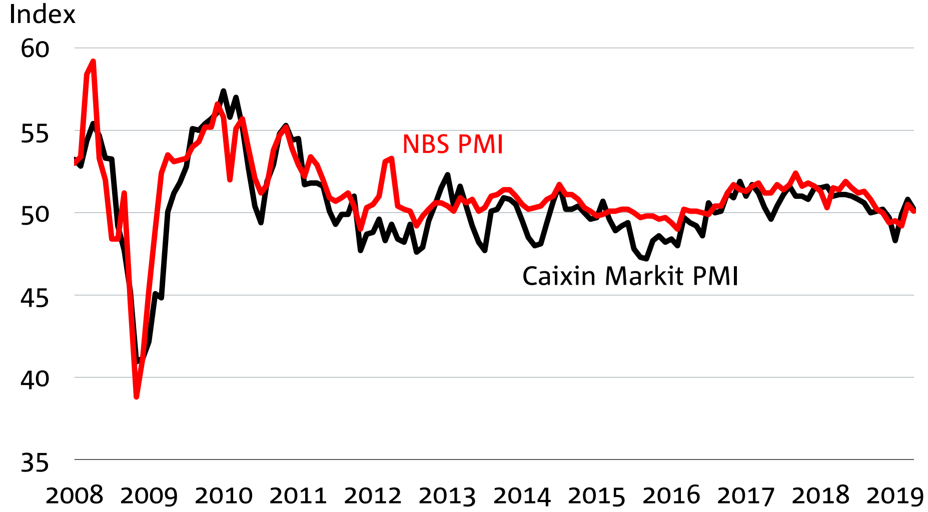
Growth slowed back to recent trends after one-off spike in March



Source: CEIC, NAB Economics

PMI SURVEYS BACK TO NEUTRAL LEVELS

Short rebound but stronger than early 2019



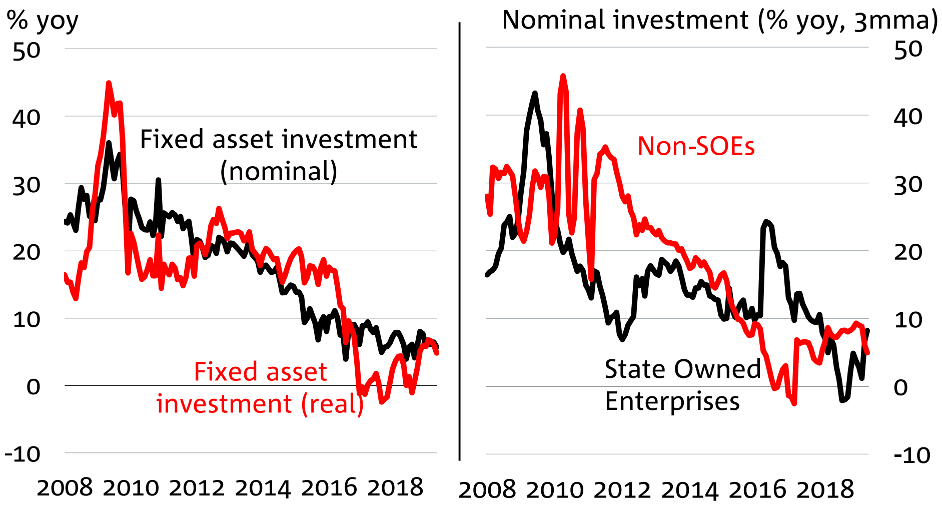
Source: CEIC, NAB Economics

- China's industrial production increased by 5.4% yoy in April – down from an unusually strong 8.5% yoy in March. It is worth noting that the strong increase recorded in March is not evident in the seasonally adjusted month-on-month series also produced by the National Bureau of Statistics, meaning that one off factors likely contributed to this strength.
- There were some highly divergent trends in output by industry. Crude steel production increased strongly – up by 12.7% yoy to a new monthly record of 85 million tonnes. Consumer electronics production also increased strongly, with output rising by 12.4% yoy.
- There were more modest increases in other parts of heavy industry. Cement output rose by 3.4% yoy, while electricity production increased by 3.8% yoy (down from 5.4% previously).
- Motor vehicle output fell by 15.8% yoy in April – with auto sales having fallen since the second half of 2018 due to tighter credit availability (particularly in the shadow banking sector).
- The rebound evident in the March manufacturing surveys partially reversed in April. The official NBS PMI survey was at 50.1 points (from 50.5 points previously) while the private sector Caixin Markit PMI eased to 50.2 points (from 50.8 points in March). It is worth noting that these essentially neutral readings are stronger than those recorded between December 2018 and February 2019.
- Export demand remains an issue for Chinese manufacturers. New export orders were negative in both surveys – albeit the least negative reading since August 2018 in the NBS survey, while the Caixin measure returned to negative territory (having turned positive in March).

INVESTMENT

FIXED ASSET INVESTMENT

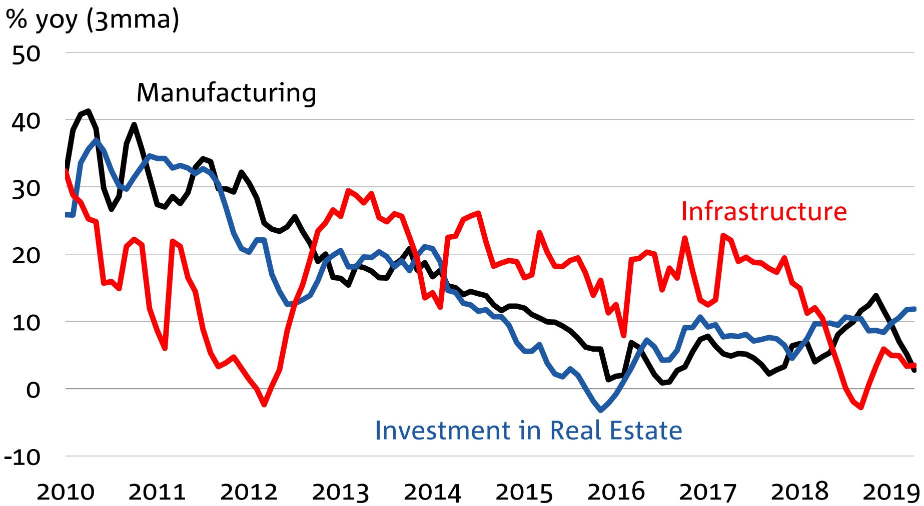
Real investment dips in April, led by private firms



Source: CEIC, NAB Economics

FIXED ASSET INVESTMENT BY SECTOR

Manufacturing and infrastructure slowing; real estate still strong



Source: CEIC, NAB Economics

- Investment in fixed assets grew at a slower pace in April – increasing by 5.7% yoy (compared with 6.5% in March). Increased producer and corporate goods prices (which flow through into the cost of investment goods) further pushed down the growth in real investment – to 4.9% yoy (from 6.1% in March).

- The slowing growth in nominal investment has largely been driven by private sector firms. On a three month moving average basis, investment by private firms increased by 5.0% yoy, from 6.1% previously. In contrast, investment by state-owned enterprises (SOEs) has accelerated – rising by 8.2% yoy (3mma), compared with 6.7% in March.

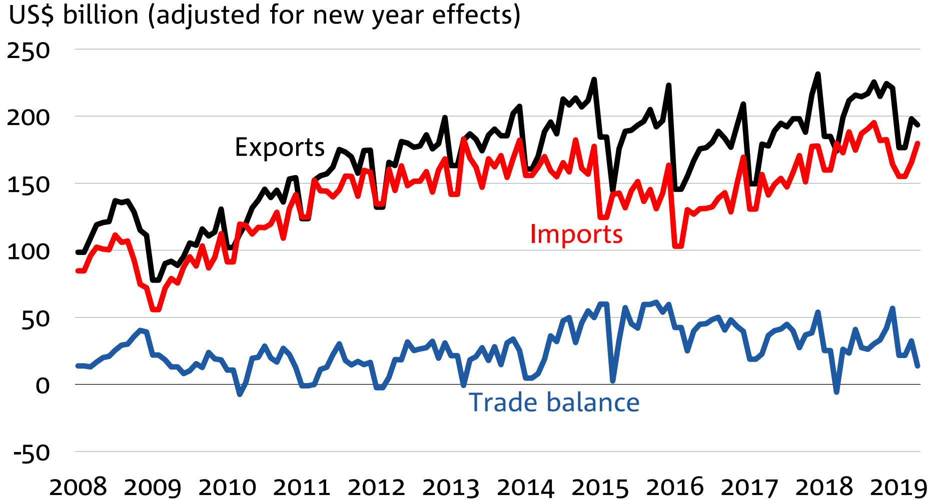
- Investment trends by major industry remain highly divergent. There has been a sharp slowdown in growth for both infrastructure investment and manufacturing investment (down to 3.5% yoy (3mma) and 2.8% yoy (3mma) respectively). Weakness in manufacturing conditions (particularly in export markets) may have contributed to this trend.

- In contrast, investment in real estate has remained strong – increasing by 11.9% yoy (3mma) in April, and having recorded double digit growth rates for the past three months. There remains a notable disconnect in residential property markets at present, with new construction starts increasing by 15.8% yoy (3mma) in April, compared with sales growth of just 1.2% yoy (3mma). This could lead to a rapid slowdown in property investment if market conditions deteriorate.

INTERNATIONAL TRADE – TRADE BALANCE AND IMPORTS

TRADE SURPLUS NARROWS IN APRIL

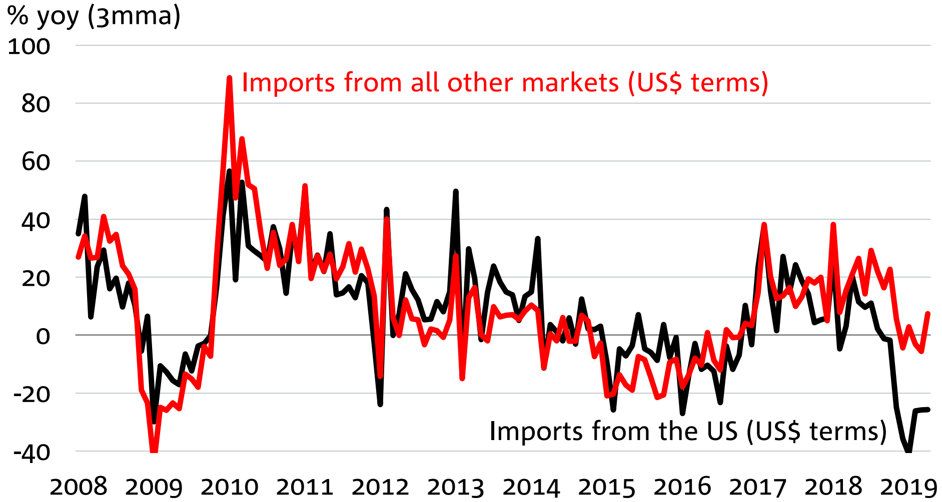
Weaker exports & a pickup in imports behind this weak outcome



Sources: CEIC, NAB Economics

CHINA'S IMPORTS FROM THE US

Tariff measures have reduced trade activity



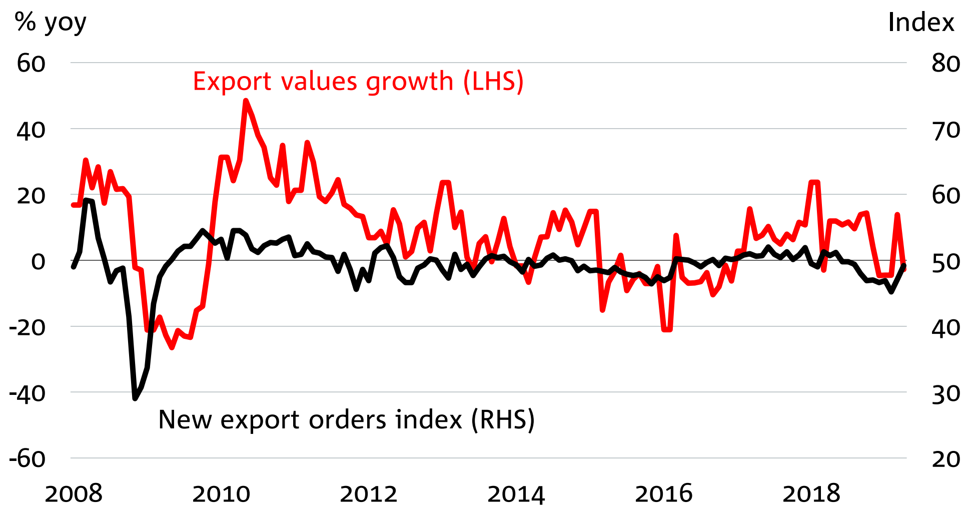
Source: CEIC, NAB Economics

- A fall in exports (both month-on-month and year-on-year) and an increase in imports led to a narrowing in China's trade surplus in April. The surplus totalled US$13.8 billion, the weakest result since the surprise trade deficit recorded in March 2018.
- The United States has long accounted for the bulk of China's trade surplus, although the rolling twelve month value declined marginally in April – totalling US$327.5 billion (from US$328.7 billion in March). The trade relationship between the two countries has deteriorated rapidly in the past few weeks (compared with previous expectations of an imminent agreement) – with the US increasing the rate on the second phase of tariffs in May and exploring an additional third and final phase.
- China's imports rose by 4.0% yoy in April to total US$179.7 billion (compared with US$165.5 billion in March). There is a noticeable difference between import trends for the United States and all other markets – with imports from the US falling by 26% yoy – reflecting the impact of existing trade measures, ahead of the subsequent escalation in tensions in May.
- After around five months of falling import volumes, volumes appeared to rise in April – based on the historically close relationship between China's import prices and global commodity prices. The RBA Index of Commodity Prices rose by 9.4% yoy in April, which flows through into an estimated increase in China's import volumes of 1.1% yoy. This is compared with an average 10% yoy fall in volumes between November 2018 and March 2019.
- That said, there were some significant differences in terms of import volumes by major commodity. Imports of coal and crude oil rose strongly – up by 13.5% yoy and 10.8% yoy respectively (the latter just below the record volume in December 2018). In contrast, imports of iron ore and copper both fell in year-on-year terms, down 2.6% yoy and 8.4% yoy respectively.

INTERNATIONAL TRADE – EXPORTS

CHINA'S EXPORT VALUES AND NEW ORDERS

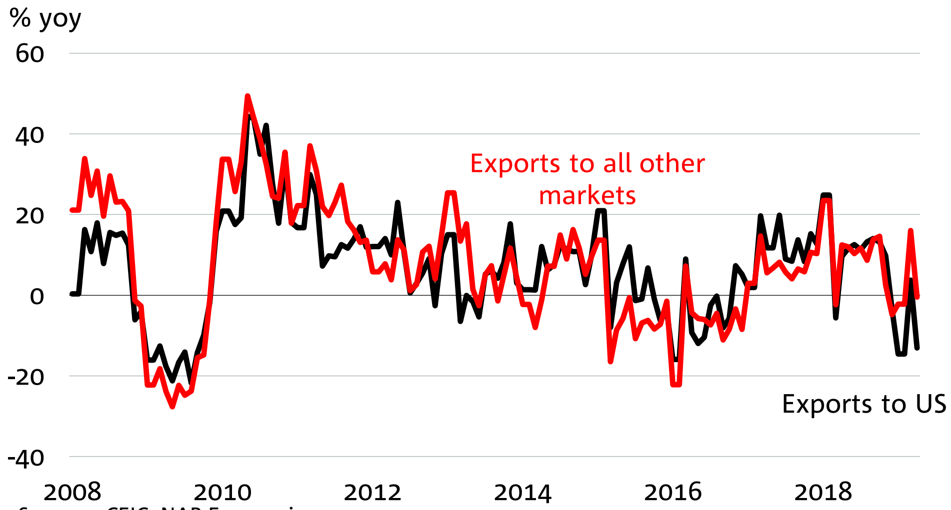
Exports fall in April; new orders ahead of latest tariff measures



Source: CEIC, NAB Economics

EXPORTS TO MAJOR TRADING PARTNERS

Impact of US-China trade tensions evident



Sources: CEIC, NAB Economics

- The total value of China's exports fell marginally in April – to US$193.5 billion (compared with US$197.9 billion previously). This represented a decrease of 2.7% yoy.
- The new export orders measure in the NBS PMI survey remained negative in April – at 49.2 points – however this was the least negative reading since August 2018. That said, this survey was conducted prior to the escalation in US-China trade tensions, and it is likely to worsen in coming months.
- Growth in exports to the United States has lagged other major markets since December 2018 and this remained the case in April. Exports to the US fell by 13.1% yoy – reflecting the impact of existing trade measures (prior to the recently announced increase, which is unlikely to be evident in the data until June at the earliest).
- In contrast, exports to the European Union increased by around 6.5% yoy, while exports to East Asia fell by 2.4% yoy. A fall in exports to Hong Kong was the main driver of this trend – down by 5.0% yoy – which may reflect historical distortions in the trade data.
- Exports to non-Hong Kong East Asia fell by 0.8% yoy. The value of exports to South Korea and Indonesia both fell significantly in April, partially offset by an increase in exports to Vietnam.

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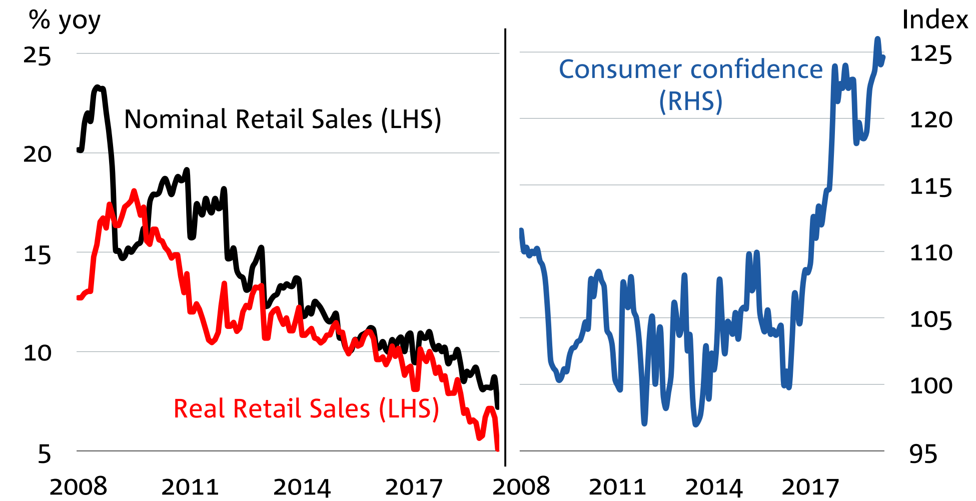
RETAIL SALES AND INFLATION

REAL RETAIL SALES HISTORICALLY WEAK

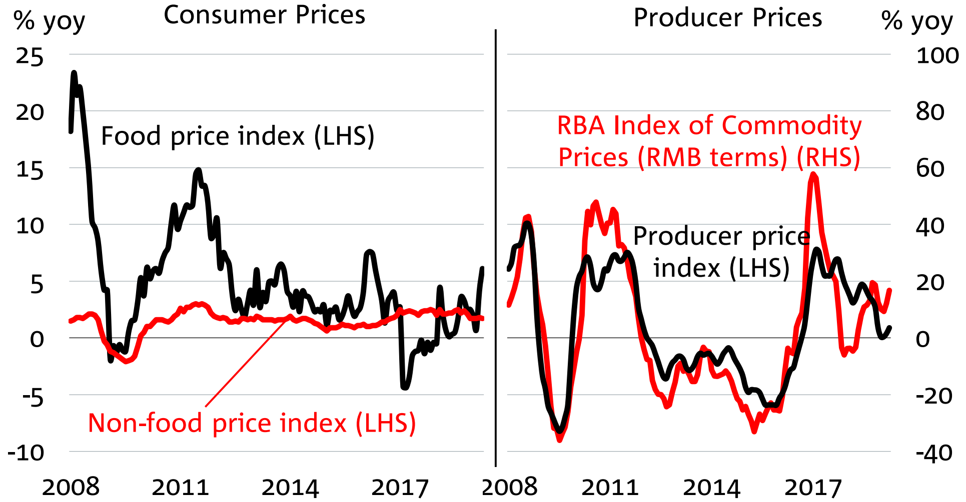
Consumer confidence remains near record highs



Source: CEIC, NAB Economics

CONSUMER AND PRODUCER PRICES

Pork pushes CPI high; disconnect between costs and factory prices



Source: CEIC, RBA, NAB Economics

- Growth in nominal retail sales slowed in April – down to 7.2% yoy (from 8.7% yoy in March). This slowing trend coincided with a slight increase in retail price inflation – up to 2.0% yoy from 1.9% in March. This meant that growth in real retail sales slowed significantly – down to 5.1% yoy (from 6.7% previously). This was the weakest rate of growth since May 2003.
- Despite the weak rate of growth of real retail sales, China's consumer confidence has remained at high levels. In March, confidence dipped marginally to 124.1 points (off an all time high of 126 points in February).
- Headline inflation accelerated for the second straight month in April, with the Consumers Prices Index increasing by 2.5% yoy (from 2.3% in March).
- Growth in food prices was the primary driver of this increase – with food prices rising by 6.1% yoy in April. Strong increases in pork prices have been a major factor – increasing by 14.4% yoy (from 5.1% previously) – as supply has been curtailed by the African Swine Flu outbreak. In addition, fresh vegetable and fresh fruit prices have also risen – up by 17.4% yoy and 11.9% yoy respectively.
- In contrast, non-food prices grew more slowly in April – increasing by 1.7% yoy (compared with 1.8% previously). Vehicle fuel prices were barely changed in April – increasing by 0.2% yoy (down from 3.3% in March).
- Producer price growth was stronger in April – albeit still quite modest at 0.9% yoy (compared with 0.4% in March. The disconnect between commodity price trends and producer prices has persisted – which may indicate the weakness in both domestic and export demand has limited the capacity of producers to pass through higher costs.

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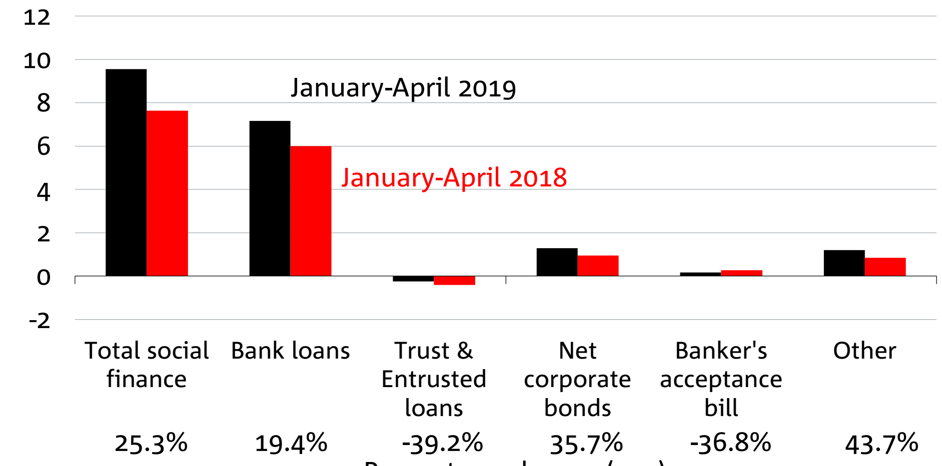
CREDIT CONDITIONS

NEW CREDIT ISSUANCE REMAINS STRONG

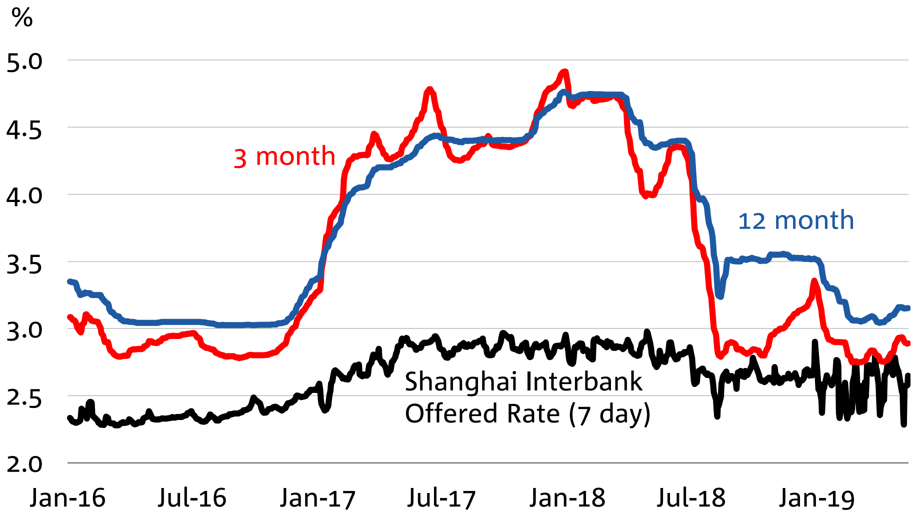
However issuance fell yoy in April



Sources: CEIC, NAB Economics

SHORT TERM INTERBANK VOLATILITY HAS CONTINUED

Longer term rates well below year ago levels



Source: CEIC, NAB Economics

- China's new credit issuance has remained strong in the early months of 2019 – suggesting that authorities are seeking to support growth in the short term. Public statements from regulators suggest that deleveraging is now less of a priority (compared with comments from late last year that the program would continue), however it remains to be seen whether the program will resume once they are satisfied that growth has stabilised.
- Between January and April, new credit totalled RMB 9.5 trillion, an increase of 25% yoy – that said, new issuance was weaker in the month of April, at RMB 1.4 trillion (compared with RMB 1.8 trillion in April 2018).
- Bank lending increased by over 19% yoy over this period – to RMB 7.2 trillion. Bank lending has increased its share of credit issuance in the past few years, as tighter regulation of shadow banking forced banks to direct funding back through traditional channels.
- Non-bank lending expanded more rapidly in the first four months – increasing by almost 47% yoy to RMB 2.4 trillion. The largest share of this issuance came from corporate bonds – which rose by 36% yoy – followed by local government special bond financing (up by 348% yoy from a very low base in early 2018).
- The current period of volatility in short term interbank rates has continued. From the start of April through to mid-May, the 7 day Shanghai Interbank Offered Rate (Shibor) has traded in a 50 basis point trading range – well above the trend since November 2015 (when the PBoC changed its monetary policy approach). Reduced Open Market Operations in recent months may explain the volatility in the Shibor, but so far we have no clear indication as to why the PBoC has pulled back from the market.
- Since the start of this year (as volatility in near term interbank rates has increased), there has been a notable decline in longer term rates. Compared to this time last year, there has been a decline of around 120 basis points for both 3 month and 12 month rates.

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