

# CHINA'S ECONOMY AT A GLANCE

JUNE 2019



National  
Australia  
Bank

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# KEY POINTS

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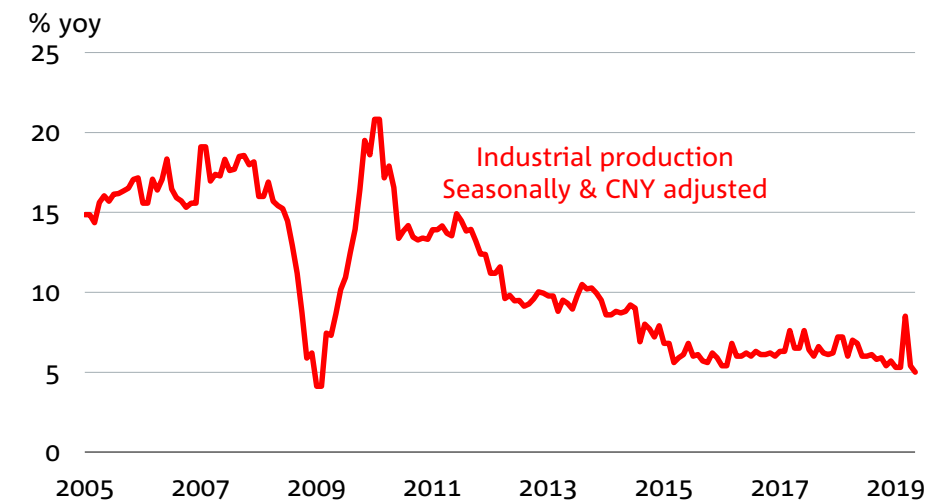
## Policy makers ready to stimulate as signs of weakness grow

- China's policy makers are likely to boost domestic support in the wake of the deteriorating trade relationship with the United States. The PBoC's Governor suggested a range of measures in early June, including cutting interest rates, lowering the required reserve ratio and other monetary policy tools along with increased fiscal policy support. This domestic policy response remains the key driver for us to maintain our growth forecasts at 6.25% this year, 6% in 2020 and 5.8% in 2021.
- Growth in industrial production slowed in May, down to 5.0% yoy (compared with 5.4% yoy in April). This was the slowest monthly increase since the January-February period of 2009 – the bottom of the Global Financial Crisis. There was some divergence in PMI trends in May, with the official NBS measure turning negative, while the private sector Caixin Markit survey was unchanged at neutral levels.
- Growth in real investment fell in May – down to 3.8% yoy (from 4.9% previously). The slowing trend has been driven by private sector firms, while investment in manufacturing and infrastructure were particularly weak.
- China's trade surplus widened again in May (compared with a relatively narrow surplus in April), as exports rose and imports fell month-on-month. The United States accounts for the majority of China's trade surplus. With tariffs implemented by both countries, both exports and imports have fallen, but this has not substantially reduced China's trade surplus with the US – which rose to a record US\$329.8 billion for the twelve months to May.
- Despite a modest upturn in May, real retail sales growth remained historically weak. In part this likely reflects the tightening in shadow banking which is constraining consumers – particularly in the auto sector. However, consumer confidence has remained high – picking up to 125.3 points (from 124.1 points in March), just below an all time high in February.
- New credit issuance has continued to grow strongly in May – reflecting the short term priority of policy makers to support growth overtaking the medium term deleveraging goals of the previous two years. In the first five months of the year, new credit issuance increased by over 27% yoy, to total RMB 10.9 trillion.
- The period of high volatility in short term interbank rates continued in May and early June. Since the start of May, the 7 day Shanghai Interbank Offered Rate (Shibor) has traded in a range of over 50 basis points – well above the typical range exhibited since November 2015 (when monetary policy switched to targeting this rate). Longer dated rates have fallen considerably since early 2018 – but have trended marginally higher since early April.

# INDUSTRIAL PRODUCTION

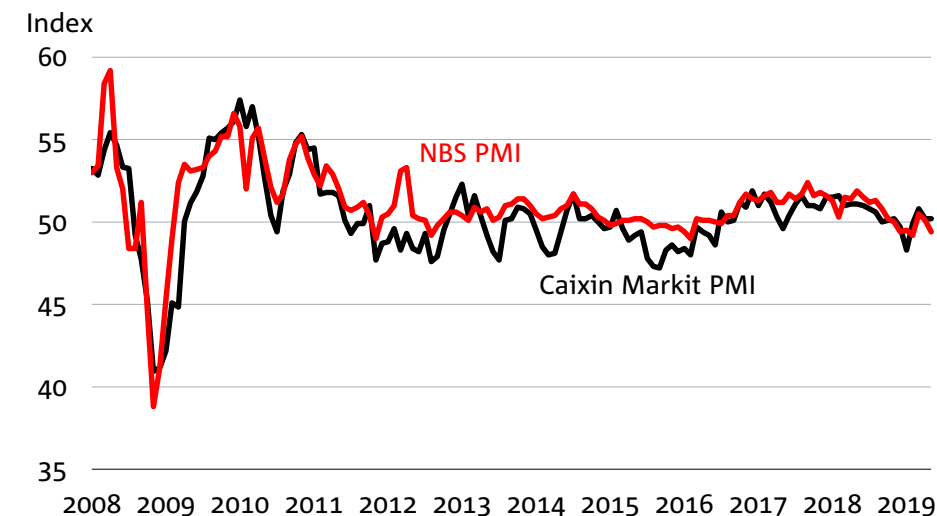
## INDUSTRIAL PRODUCTION

Growth slowed to post-GFC low



## PMI SURVEYS SOMEWHAT MIXED

Official survey weaker on negative export orders

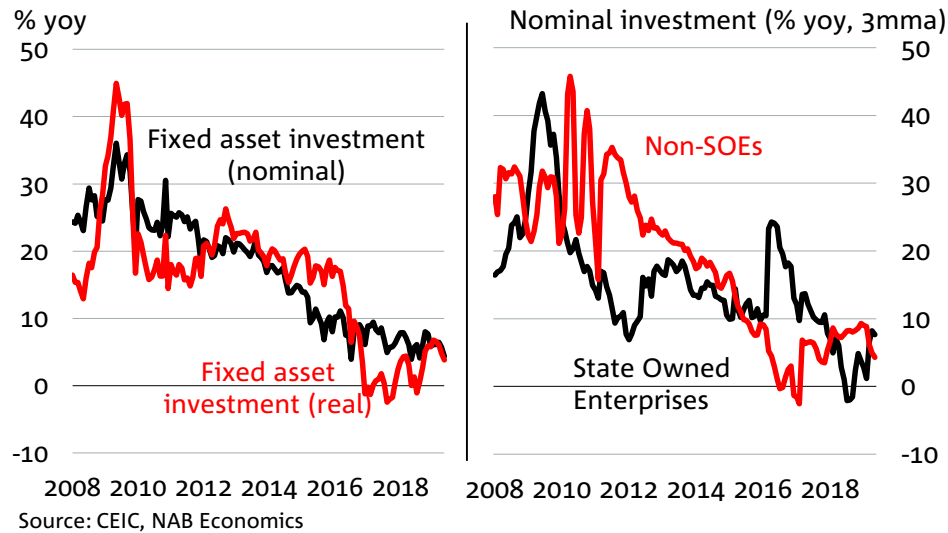


- Growth in industrial production slowed in May, down to 5.0% yoy (compared with 5.4% yoy in April). This was the slowest monthly increase since the January-February period of 2009 – the bottom of the Global Financial Crisis – when industrial production rose by 3.8% yoy.
- There were highly divergent trends in different industry segments. Crude steel production has continued to increase strongly – increasing by 10.0% yoy to 89 million tonnes (a new monthly record). Cement output – another construction linked heavy industry – rose by 7.2% yoy. Production of consumer electronics increased by 10.6% yoy.
- In contrast, motor vehicle manufacturing continues to suffer – with output falling by over 21% yoy – with tighter credit availability (primarily from the shadow banking sector) impacting auto sales. Electricity output rose by just 0.2% yoy.
- Both of China’s main manufacturing PMI surveys remained relatively weak, however there was some divergence in the underlying trends for May. The NBS PMI survey – which typically has a larger sample of big state owned enterprises – turned negative, down to 49.4 points (from 50.1 points previously). In contrast, the private sector Caixin Markit PMI (which has a larger share of SME firms) was unchanged at 50.2 points.
- Export demand readings were noticeably divergent between the two surveys – with new export orders in the NBS survey remaining deeply negative, while the measure in the Caixin Markit survey was positive in May – at its equal strongest level since March 2018. This was somewhat surprising, given that the increase in US tariffs was announced on 5 May – leaving little time for consumers to bring purchases forward.

# INVESTMENT

## FIXED ASSET INVESTMENT

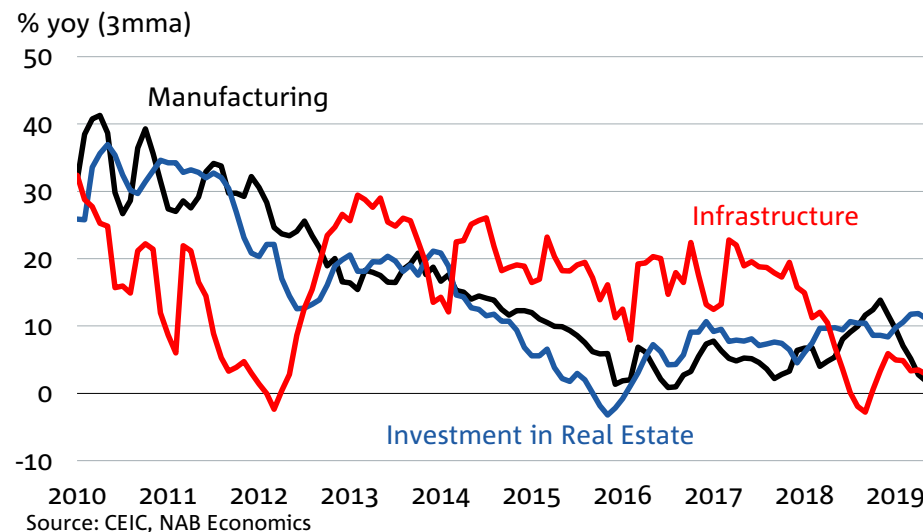
Real investment continues to slow, with private firms weaker



- Growth in China's fixed asset investment slowed considerably in May – down to 4.3% yoy (compared with 5.7% in April). Despite a moderation in producer prices – which flow through into the cost of investment goods – real investment also fell in May – down to 3.8% yoy (from 4.9% previously).
- The slowing trend for nominal investment in recent months has been driven by private sector firms. On a three month moving average basis, private sector investment slowed to 4.3% yoy in May (compared with 5.0% in April) – less than half the rate of growth at the start of the year. In contrast, investment by state-owned enterprises grew by 7.7% yoy (3mma), down from 8.2% yoy previously.
- There remains some divergent trends in investment by industry. Manufacturing investment has plunged in recent months – likely reflecting the deteriorating conditions in the sector, in part related to the US-China trade tensions – with investment growing by just 1.9% yoy (3mma). Similarly, infrastructure investment has been weak – increasing by 2.9% yoy (3mma).
- In contrast, investment in real estate has continued to grow strongly – a trend that has persisted since the start of 2018. In May, real estate investment increased by 11.2% yoy (3mma).
- There remains some uncertainty around the future direction of real estate investment, with residential property sales stalling since late last year. If property market conditions deteriorate, this could lead to a rapid slowdown in investment.

## FIXED ASSET INVESTMENT BY SECTOR

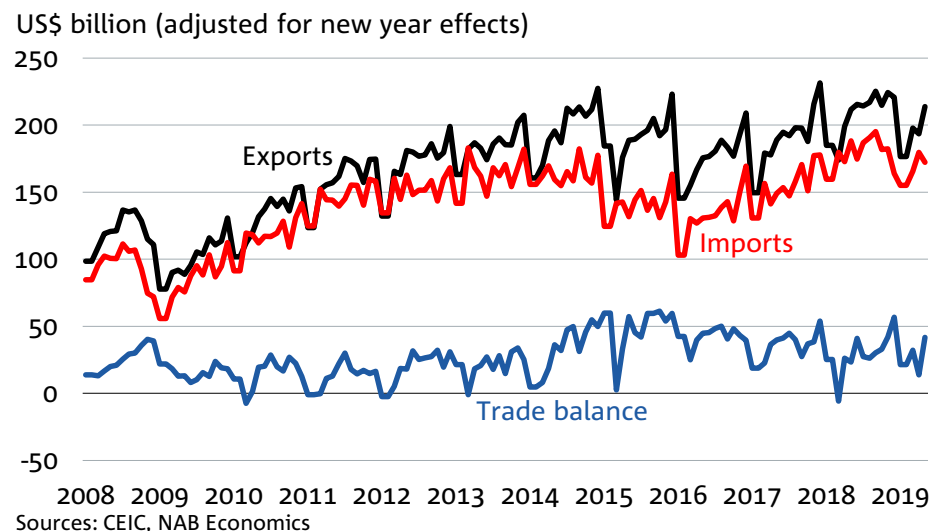
Manufacturing investment has plunged on weak conditions



# INTERNATIONAL TRADE – TRADE BALANCE AND IMPORTS

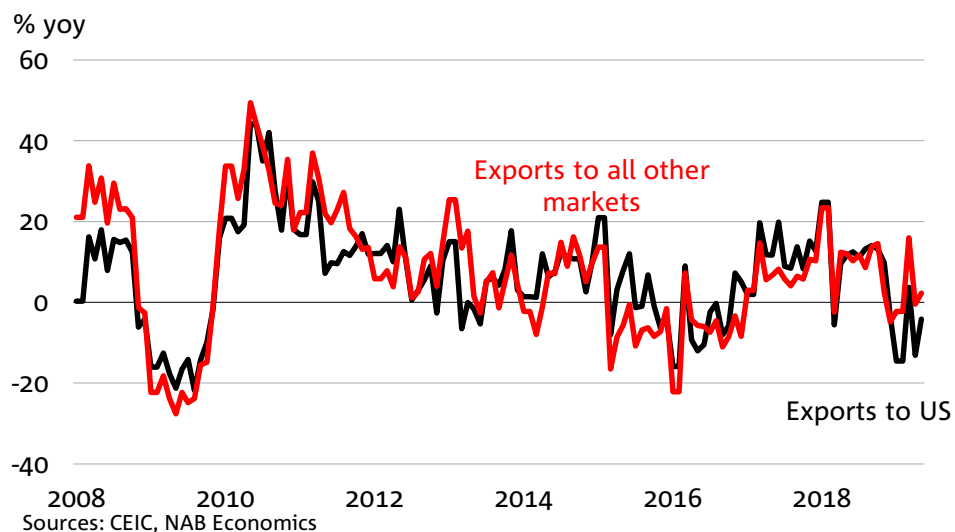
## TRADE SURPLUS WIDENS FROM NARROW RESULT IN APRIL

Exports a little stronger, while imports fell



## CHINA'S IMPORTS FROM THE US

China's retaliatory tariffs have lowered demand for US goods

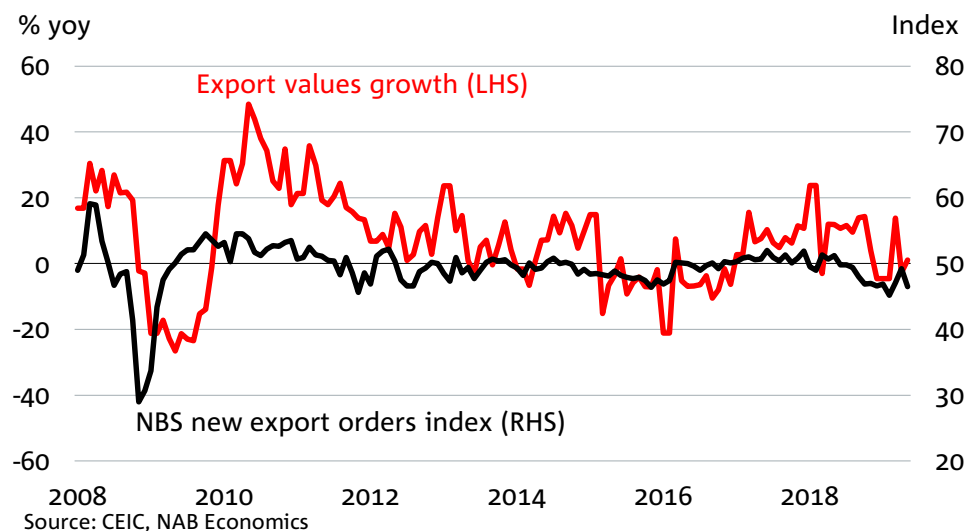


- China's trade surplus widened again in May (compared with a relatively narrow surplus in April), as exports rose and imports fell month-on-month. The surplus totalled US\$41.7 billion, up from US\$13.8 billion in April.
- The United States accounts for the majority of China's trade surplus. With tariffs implemented by both countries, both exports and imports have fallen, but this has not substantially reduced China's trade surplus with the US – which rose to a record US\$329.8 billion for the twelve months to May.
- China's total imports fell by around 8.5% yoy in May to US\$172.2 billion (compared with US\$179.7 billion in April). There remains a sizeable difference between trends in import from the United States (where China has imposed tariffs in retaliation to US trade barriers) and from other markets – with US imports falling by almost 27% yoy in May, compared with a 2.3% yoy increase for non-US imports. This came ahead of the additional trade barriers that effectively commence in June – meaning that imports from the US are likely to fall further in coming months.
- The fall in the total value of imports in May appears to be driven by weaker import volumes. Our estimate of import prices is based on global commodity price trends – with the RBA Index of Commodity Prices up by around 9.2% yoy in May (albeit with considerable divergence between individual commodities). On a three month moving average basis, we estimate that China's import volumes fell by 6.9% yoy in May – compared with double digit growth in volumes between February and September 2018.
- There remains some divergence in import trends by major commodity. Imports of coal have increased strongly – up by 6.9% yoy (3mma), while crude oil imports also rose by 4.8% yoy (3mma). In contrast, imports of iron ore and copper both fell – down by 4.5% yoy (3mma) and 14.7% yoy (3mma) – with the former possibly related to supply constraints in Brazil and Australia.

# INTERNATIONAL TRADE – EXPORTS

## CHINA'S EXPORTS MODESTLY HIGHER IN MAY

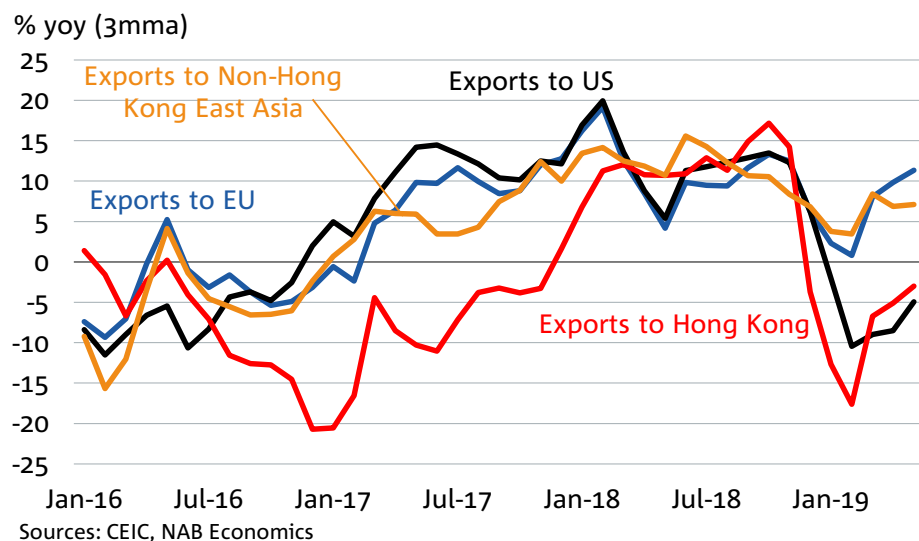
Export orders fall in May – ahead of the US tariff increase



- China's exports increased modestly in May – rising by 1.1% yoy to US\$213.8 billion (compared with US\$193.5 billion in April). It is unlikely that this increase represents purchases being brought forward ahead of the latest increase in US tariffs – due to the short window between the announcement and imposition of these measures.
- According to the NBS PMI survey, the new export orders measure remained firmly negative – at 46.5 points – consistent with the deteriorating global trading environment.
- China's exports to the United States have continued to fall – reflecting the impact of existing tariffs on the demand for Chinese goods. In May, exports to the US fell by 4.2% yoy. It is worth noting that this decline was ahead of the latest increase in US tariffs – meaning that exports are likely to fall further in coming months.
- In contrast, exports to the European Union increased by 6.1% yoy in May, while exports to non-Hong Kong East Asia rose by 3.8% yoy. The latter was largely driven by a sizeable increase in exports to Vietnam, while in contrast exports to Indonesia and Singapore fell.
- Exports to Hong Kong fell by 3.1% yoy in May. Unlike earlier periods, where trade data with Hong Kong was distorted by unauthorised capital flows disguised as trade activity, there does not appear to be a clear sign of this occurring in recent months. Hong Kong customs data shows a substantial drop off in imports since late last year – reflecting the deteriorating trade environment.

## EXPORTS TO MAJOR TRADING PARTNERS

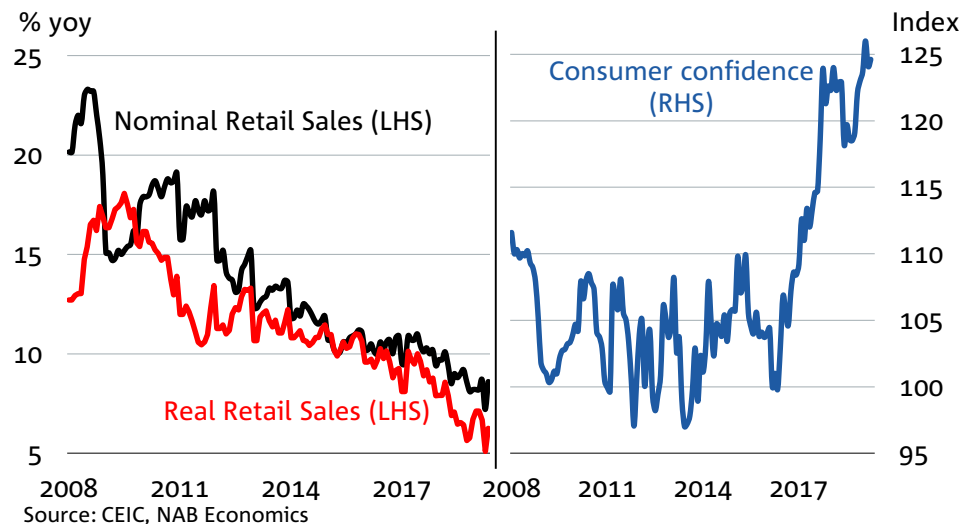
Stark differences between Europe/East Asia and the US



# RETAIL SALES AND INFLATION

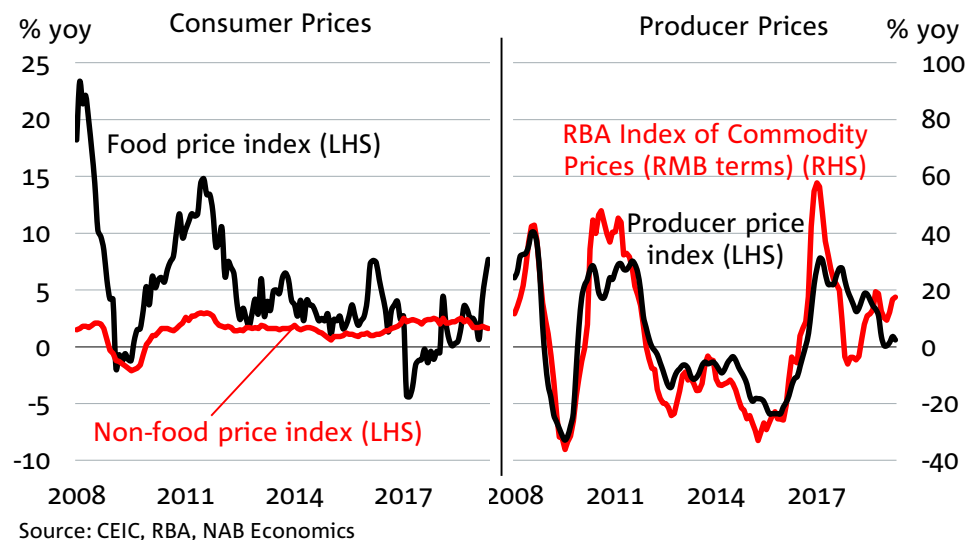
## REAL RETAIL SALES EDGE AWAY FROM LONG RUN LOW

Consumer confidence remains near record highs



## CONSUMER AND PRODUCER PRICES

Pork continues to elevate CPI; producer prices subdued

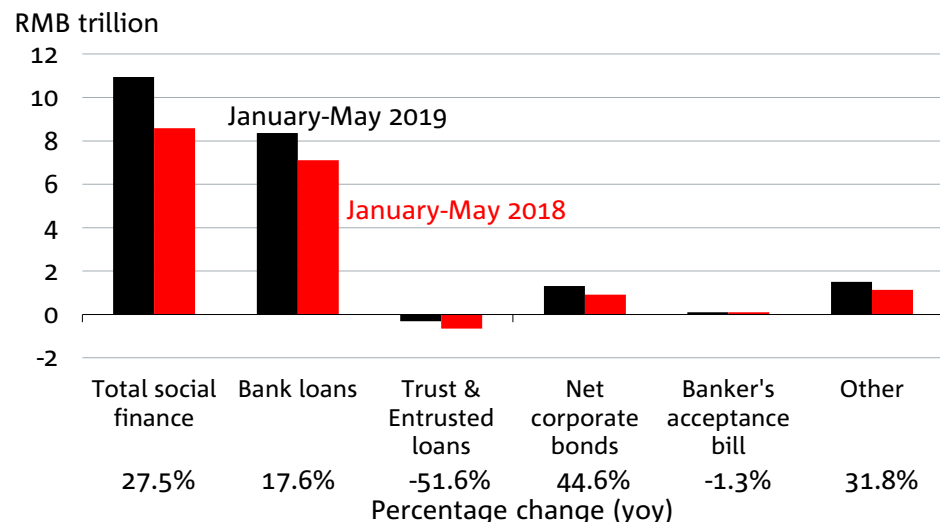


- There was a rebound in nominal retail sales growth in May – with an increase of 8.6% yoy (compared with 7.2% in April and 8.7% in March). With only a modest increase in retail price inflation, our estimate of real retail sales picked up to 6.3% yoy (from an almost 16 year low of 5.1% in April).
- Despite this modest upturn, real retail sales growth has remained historically weak. In part this likely reflects the tightening in shadow banking constraining consumers – particularly in the auto sector. However, consumer confidence has remained high – picking up to 125.3 points (from 124.1 points in March), just below an all time high in February.
- Headline inflation continued to accelerate in May – with the Consumer Price Index rising by 2.7% yoy (compared with 2.5% in April). This was the third month in a row that the growth rate increased.
- This acceleration was driven by a strong increase in food prices – which rose by 7.7% yoy (up from 6.1% yoy in April). Pork prices remain a critical factor – with supplies constrained by the African Swine Flu outbreak – with prices up by 18.2% yoy in May. Prices for fresh fruit and vegetables also increased strongly.
- In contrast, non-food price growth eased slightly in May – increasing by 1.6% yoy (down from 1.7% previously). Weaker global oil price trends translated into falling vehicle fuel prices – down by 1.4% yoy in May.
- Growth in producer prices was more subdued in May – with prices increasing by just 0.6% yoy. There remains a noticeable disconnect between current producer price growth and commodity price trends – which may indicate that producers are unable to pass rising costs to consumers – given weak domestic and export demand.

# CREDIT CONDITIONS

## NEW CREDIT ISSUANCE

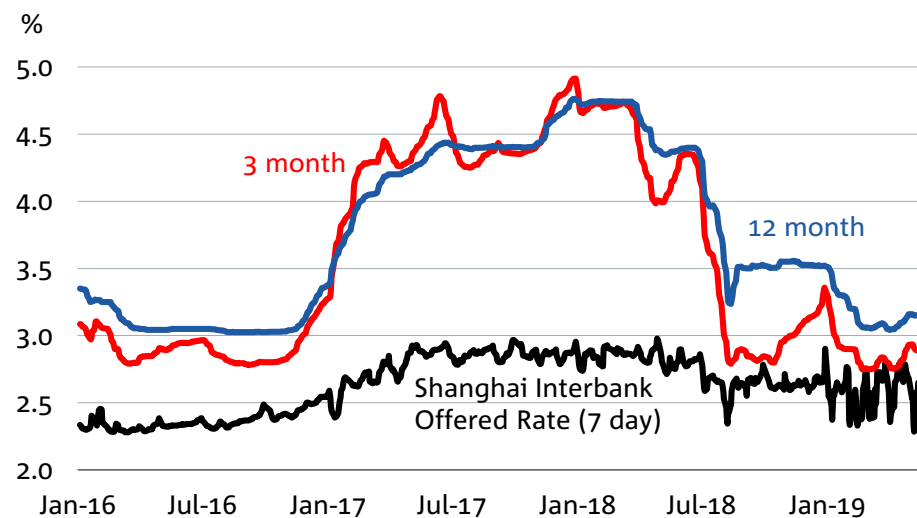
Strong growth in 2019 as short term priorities come to the fore



Sources: CEIC, NAB Economics

## SHORT TERM INTERBANK RATES

Volatility in 7 day Shibor has continued



- New credit issuance continued to grow strongly in May – reflecting the short term priority of policy makers to support growth overtaking the medium term deleveraging goals of the previous two years. In the first five months of the year, new credit issuance increased by over 27% yoy, to total RMB 10.9 trillion.
- Bank lending has increased slightly more modestly, rising by almost 18% yoy to RMB 8.3 trillion. Although bank lending's share of new issuance has fallen this year – as corporate bonds have grown more rapidly – it remains higher than the pre-deleveraging period, with bank funds no longer flowing through shadow banking products to the same extent.
- Non-bank lending increased more strongly – led by corporate bond issuance (up almost 45% yoy) and local government special bonds (up over 220% yoy). In contrast, key segments of the shadow banking sector (such as trust and entrusted loans and banker's acceptance bills) continue to decline.
- The period of high volatility in short term interbank rates continued in May and early June. Since the start of May, the 7 day Shanghai Interbank Offered Rate (Shibor) has traded in a range of over 50 basis points – well above the typical range exhibited since November 2015 (when monetary policy switched to targeting short term rates). Longer dated rates have fallen considerably since early 2018 – but have trended marginally higher since early April.
- In early June, Governor Yi of the People's Bank of China noted that there was “tremendous room” for policy adjustments should the US-China trade dispute worsen. This included cutting interest rates, lowering the required reserve ratio and other monetary policy tools. He also identified increased fiscal policy to boost growth.
- This domestic policy response is the key reason that we have not lowered our growth forecasts, despite the impact of the US-China trade tensions.



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