CHINA'S ECONOMY AT A GLANCE

OCTOBER 2020

National Australia Bank

CONTENTS

CONTACT

Gerard Burg, Senior Economist - International

NAB Group Economics

KEY POINTS

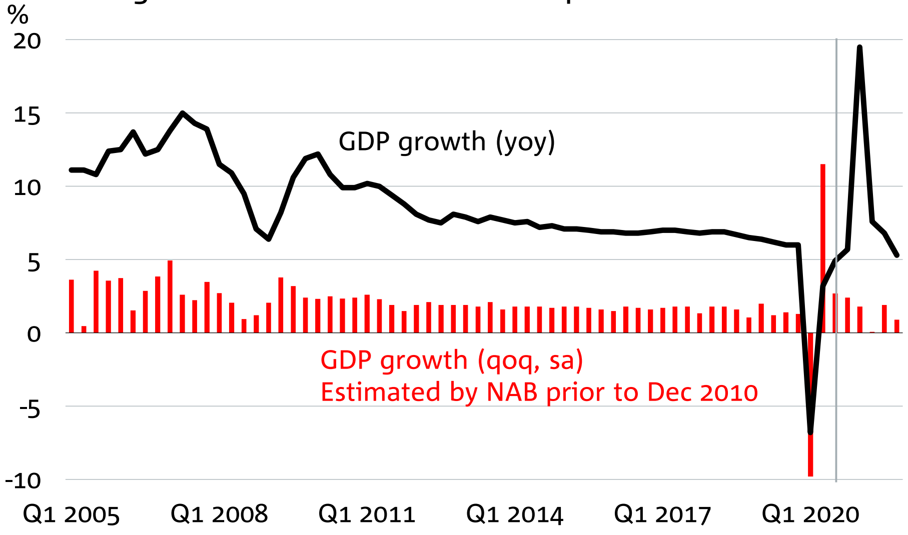
China's recovery remains industrial led, but consumers are finally emerging

- China's economy expanded by 4.9% yoy in Q3, up from a 3.2% yoy increase in Q2. This was somewhat weaker than expected – with the mean of forecasts reported by Bloomberg at 5.5% yoy. China's secondary sector –comprising manufacturing and construction – remained the key driver of growth in Q3, increasing by 6.0% yoy.
- We continue to anticipate a gradual recovery in China's growth. We have revised our forecast for 2020 to 1.8% (from 1.5% previously) and our forecast for 2021 remains unchanged (at 9.5%). Key questions remain however, including the ability of consumers to replace industry as the key engine for growth in the near term, as well as international relations – with China not yet meeting targets under the Phase One trade deal with the United States.
- China's industrial production growth has continued to accelerate, increasing by 6.9% yoy in September (from 5.6% yoy in August). The two major Manufacturing PMI surveys show a considerable improvement in new export orders.
- Real fixed asset investment was unchanged in September at 9.4% yoy – the strongest rate of increase since August 2016. There are signs that private sector investment is starting to recover.
- Real retail sales increased by 2.5% yoy in September (from -1.1% yoy previously). This was the first positive reading in 2020, but remains well below pre-COVID-19 levels.
- China's trade surplus was narrower in September, reflecting a surge in imports during the month. The surplus totalled US$37.0 billion, down from US$58.9 billion in August. China's trade surplus with the US has widened in recent months, climbing to US$292.7 billion for the twelve months to September (compared with the post-trade war low of US$273.8 billion in March). Although demand was weak earlier in the year (due to COVID-19 restrictions), China's imports from the US are way below the levels agreed to in the Phase One trade deal.
- China's new credit issuance was slightly more modest in September, but remained strong – totalling RMB 3.5 trillion (compared with RMB 3.6 trillion in August). Compared with the previous month, bank lending accelerated, while there was a slowdown in non-bank issuance.
- The People's Bank of China (PBoC) has maintained stable monetary policy since the previous cut to its policy rate in April. Compared with other major economies, the PBoC has considerable policy room, but has flagged its intention to maintain "normal" policy for as long as possible – highlighting its concern around longer term risks, such as debt expansion and asset bubbles.

GROSS DOMESTIC PRODUCT

CHINA'S ECONOMY CONTINUING TO RECOVER IN Q3

However growth a little slower than expected

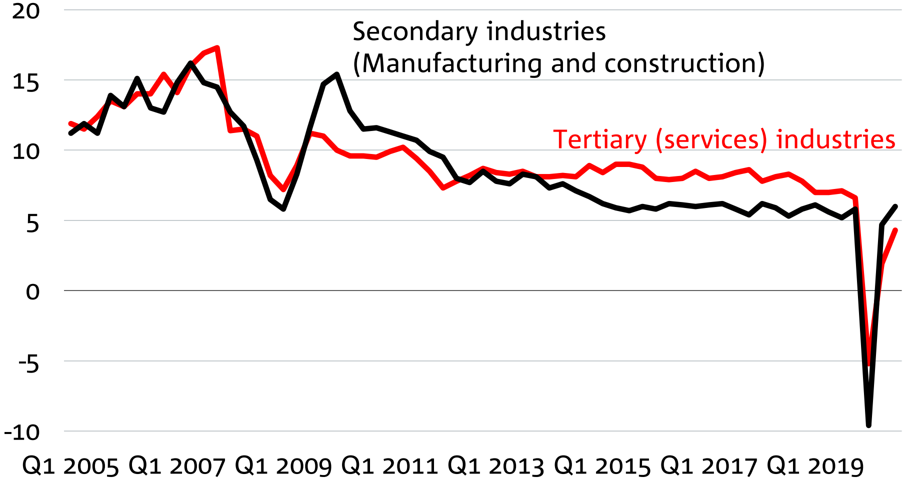


Source: CEIC, NAB Economics

ECONOMIC GROWTH BY INDUSTRY

Secondary sector still number one, but tertiary recovering

Chinese economic growth by sector (% yoy)



Source: CEIC, NAB Economics

- China's third quarter national accounts data showed its economy expanded by 4.9% yoy, up from a 3.2% yoy increase in Q2. This was somewhat weaker than expected – with the mean of forecasts reported by Bloomberg at 5.5% yoy.
- While growth has continued to recover, it remains worth highlighting that this increase was below the trends exhibited prior to COVID-19, at around 6.0% yoy.
- China's secondary sector – comprising manufacturing and construction – remained the key driver of growth in Q3, increasing by 6.0% yoy (from 4.7% yoy in Q2). However, there was a pickup in the tertiary (services) sector, which increased by 4.3% yoy, from just 1.9% yoy previously. The comparatively slower growth highlights the weakness in consumption, particularly early in the quarter.
- We continue to anticipate a gradual recovery in China's growth. We have revised our forecast for 2020 to 1.8% (from 1.5% previously) and our forecast for 2021 remains unchanged (at 9.5%). Key questions remain however, including the ability of consumers to replace industry as the key engine for growth in the near term, as well as international relations – with China not yet meeting targets under the Phase One trade deal.

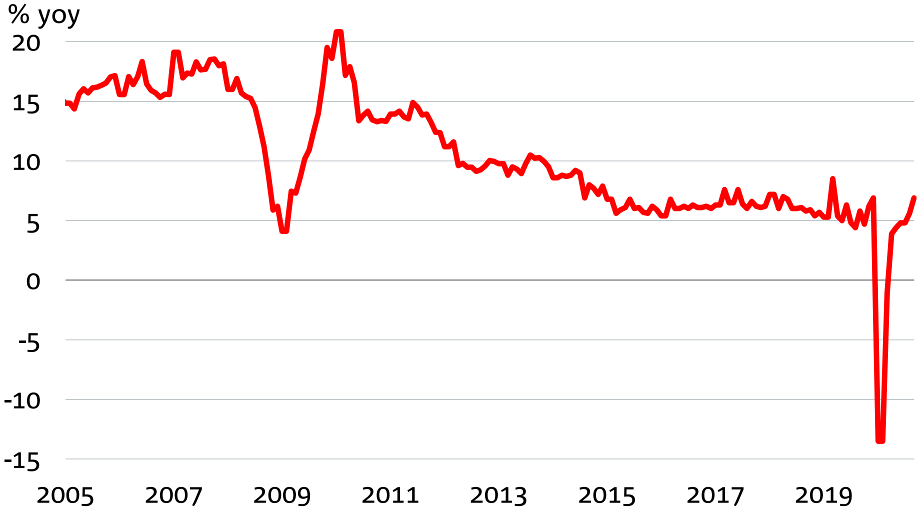
NAB CHINA GDP FORECASTS

%	2019	2020	2021
GDP	6.1	1.8	9.5

INDUSTRIAL PRODUCTION

INDUSTRIAL PRODUCTION

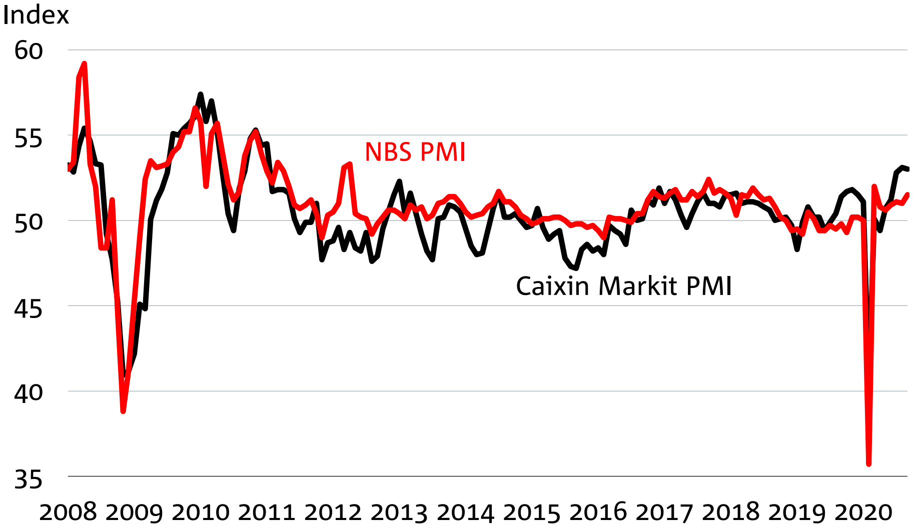
Industrial sector the key engine for China's recovery



Source: CEIC, NAB Economics

MANUFACTURING PMIS IN POSITIVE TERRITORY

Global economic recovery supporting stronger export demand



Source: CEIC, NAB Economics

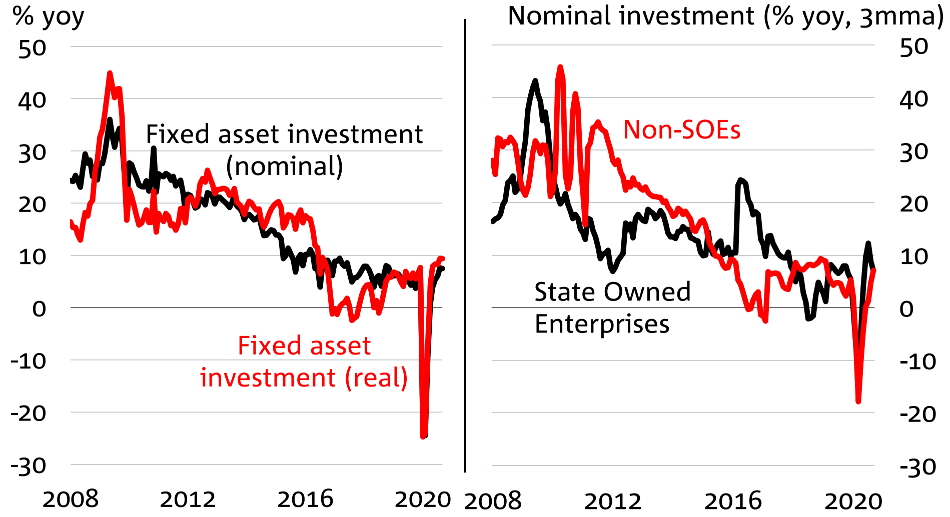
- China's industrial production growth has continued to accelerate, increasing by 6.9% yoy in September (from 5.6% yoy in August). The industrial sector has continued to provide the key impetus for China's overall growth in the post-COVID-19 period.
- Reflecting the demand from the construction sector, growth in heavy industrial products such as crude steel and cement remained strong – increasing by 10.9% yoy and 6.4% yoy respectively (albeit steel output eased away from its record high last month).
- Production of motor vehicles also increased strongly (particularly for new energy vehicles) – up by 13.8% yoy – while electronics rose by 8.0% yoy. Electricity production rose by 5.3% yoy.
- The gap between the headline levels of China's two major manufacturing surveys remained sizeable in September, albeit a little narrower than in August. The private sector Caixin Markit PMI – which has a larger representation of China's SME manufacturers – edged down to 53.0 points (from 53.1 points previously). In contrast, the official NBS PMI (which has a larger share of the big state-owned firms) rose to 51.5 points (from 51.0 point in August).
- The broadly improving trend in the global economy is evident in the export demand measures in these surveys. New export orders in the NBS PMI survey rose to 50.8 points – the strongest reading since May 2018. This measure was considerably stronger in the Caixin Markit survey, recording its highest reading since August 2017.

National Australia Bank

INVESTMENT

FIXED ASSET INVESTMENT

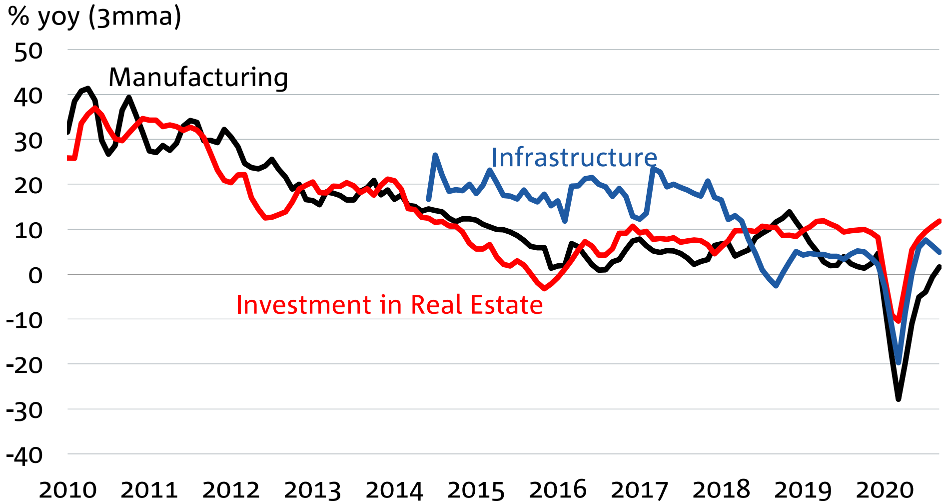
Private sector investment is showing signs of recovery



Source: CEIC, NAB Economics

FIXED ASSET INVESTMENT BY SECTOR

Real estate investment remains strong



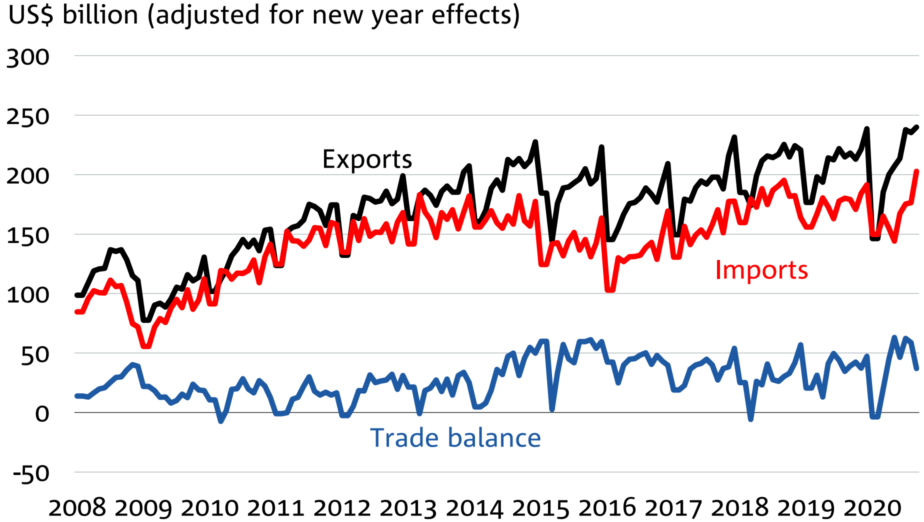
Source: CEIC, NAB Economics

- Nominal growth in fixed asset investment dipped marginally in September – to 7.5% yoy (from 7.6% yoy in August). With only a modest change in producer price inflation – which flows through into the cost of investment goods – we estimate that growth in real investment was unchanged in September at 9.4% yoy – the strongest rate of increase since August 2016.
- State-owned enterprises (SOEs) led the recovery in nominal fixed asset investment, from its COVID-19 trough, however in recent months this rate of growth has slowed considerably – to around 7.0% yoy (on a three month moving average basis) in September. In contrast, private sector investment has increased to 7.1% yoy (3mma), from 4.8% yoy (3mma) in August).
- By industry, there remain some divergent investment trends. On a three month moving average basis, investment in real estate has remained strong – increasing by 11.8% yoy (3mma) – reflecting the surge in construction activity. In contrast, there was a dip in infrastructure investment which rose by 4.9% yoy (3mma), compared with 6.3% yoy (3mma) in August.
- Investment in manufacturing has finally turned positive, increasing by 1.6% yoy (3mma), the first increase in 2020.

INTERNATIONAL TRADE – TRADE BALANCE AND IMPORTS

CHINA'S TRADE BALANCE

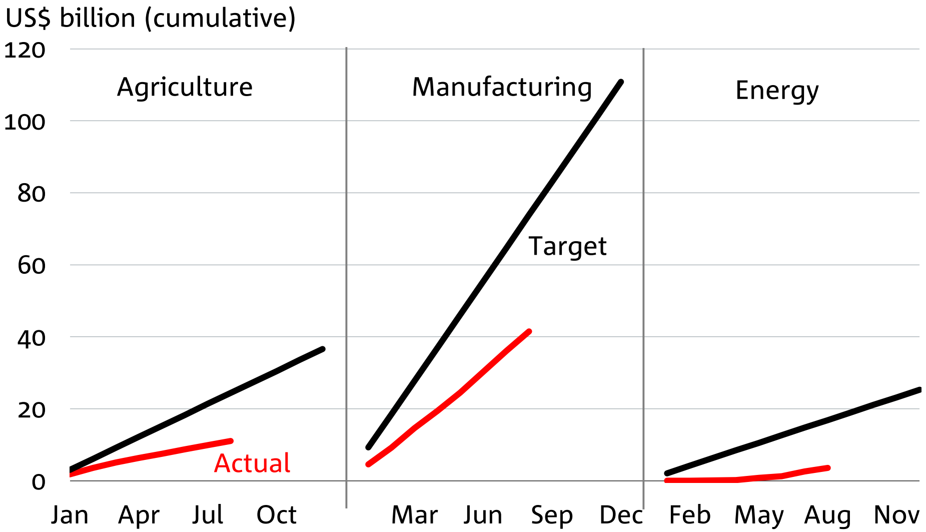
Surplus narrowed in September as imports surged to record levels



Sources: CEIC, NAB Economics

CHINA'S PROGRESS ON PHASE ONE TARGETS

China's imports of US products way below agreed levels



Sources: PIIE, NAB Economics

- China's trade surplus was narrower in September, reflecting a surge in imports during the month (compared with a smaller month-on-month increase in exports). The surplus totalled US$37.0 billion, down from US$58.9 billion in August.

- Trade tensions with the United States remain. China's trade surplus with the US has widened in recent months, climbing to US$292.7 billion for the twelve months to September (compared with the post-trade war low of US$273.8 billion in March). Although demand was weak earlier in the year (due to COVID-19 restrictions), China's imports from the US are way below the levels agreed to in the Phase One trade deal.

- China's imports totalled US$202.8 billion in September – up from US$176.3 billion in August – a new record high (exceeding the total recorded in September 2018. In year-on-year terms, imports rose by 13.2%.

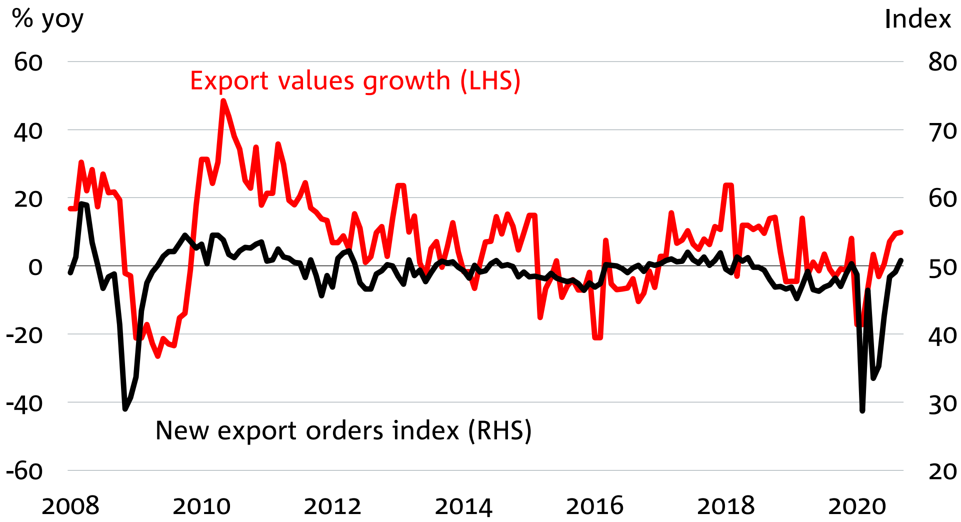
- The surge in imports does not appear to be driven by prices – with US dollar denominated commodity prices (as measured by the RBA Index of Commodity Prices) falling by 2.8% yoy. Our proxy for Chinese import prices is based on this commodity price series, and suggests that import volumes rose by around 14% yoy in September – albeit it is worth noting that growth was comparatively weaker in July and August. On a three month moving average basis, volumes rose by around 6.0% yoy.

- There was a wide variation in import trends by key commodity. The volume of refined copper imports rose by 62% yoy – reflecting both the strength of domestic demand and the shortage of copper concentrate due to COVID-19 constraints in key exporters – while crude oil imports rose by 18% yoy. Iron ore imports rose by 9.2% yoy – supported by ongoing strength in steel output – but coal imports fell by 38% yoy. Reports suggest the Chinese authorities have ordered steel mills and electricity generators to not purchase Australian coal, although this alone does not explain the decline, with a drop in Indonesian imports as well.

INTERNATIONAL TRADE – EXPORTS

EXPORTS ROSE TO RECORD LEVELS IN SEPTEMBER

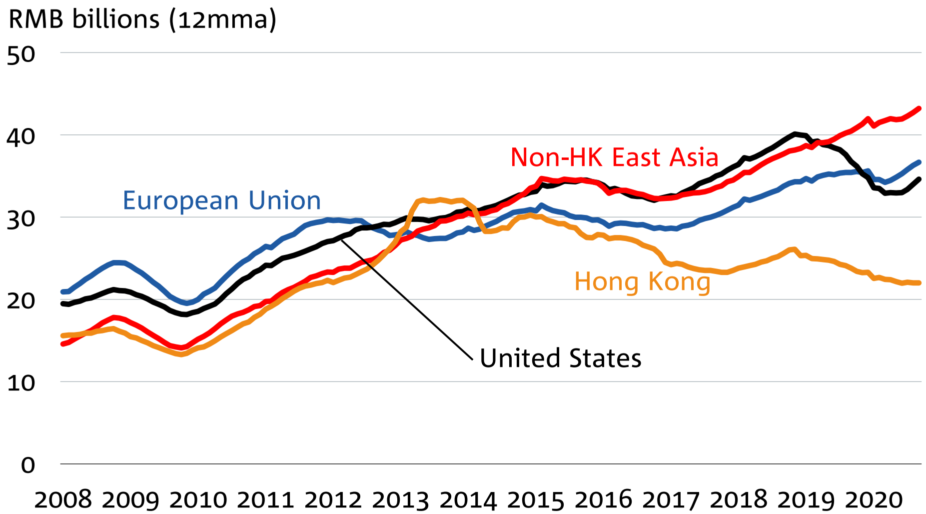
New export orders turn positive



Source: CEIC, NAB Economics

EXPORTS TO MAJOR TRADING PARTNERS

Strong growth in to all markets bar Hong Kong in September



Sources: CEIC, NAB Economics

- China's export values totalled US$239.8 billion in September, compared with US$235.3 billion in August. As was the case with imports, this represented a record high (in nominal terms), exceeding the previous peak recorded in December 2019. Global demand for medical supplies remains a key contributor to the growth in China's exports.

- Both of the major manufacturing surveys showed a pickup in new export orders – with the measure in the NBS PMI survey turning positive – at 50.8 points – the strongest reading since May 2018.

- There was a strong increase in exports to the United States – up by 20.5% yoy – while exports to the European Union and the United Kingdom rose by 11.9% yoy.

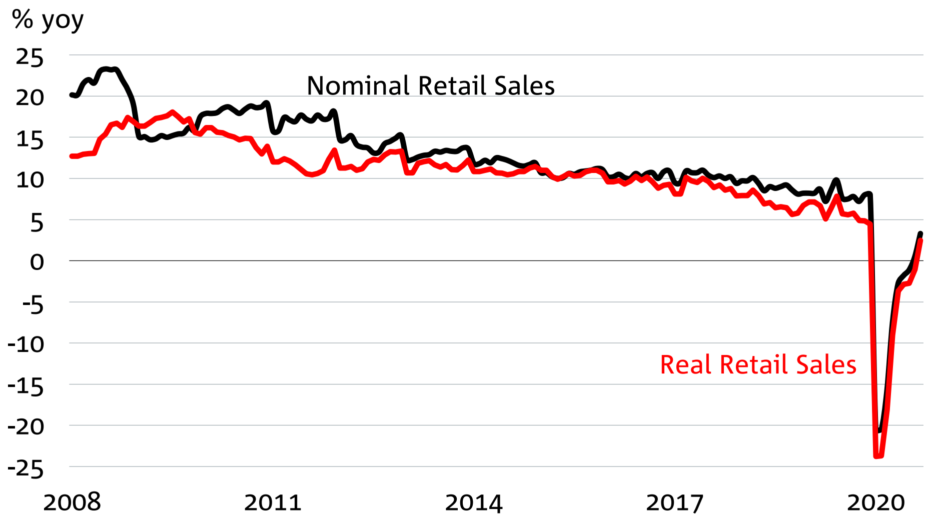
- Exports to East Asian markets rose a little more modestly – increasing by 9.2% yoy. That said, a key driver of this relative softness was Hong Kong, where exports were unchanged year-on-year (according to China Customs data). Historically there have been considerable distortions in trade data between China and Hong Kong – due in a large part to efforts to circumvent Chinese capital controls.

- Exports to non-Hong Kong East Asia rose by 14.9% yoy. This increase was driven by a surge in exports to Vietnam and a strong increase in deliveries to South Korea. In contrast, exports to Indonesia fell year-on-year.

RETAIL SALES AND INFLATION

RETAIL SALES STILL BELOW PRE-COVID-19 TRENDS

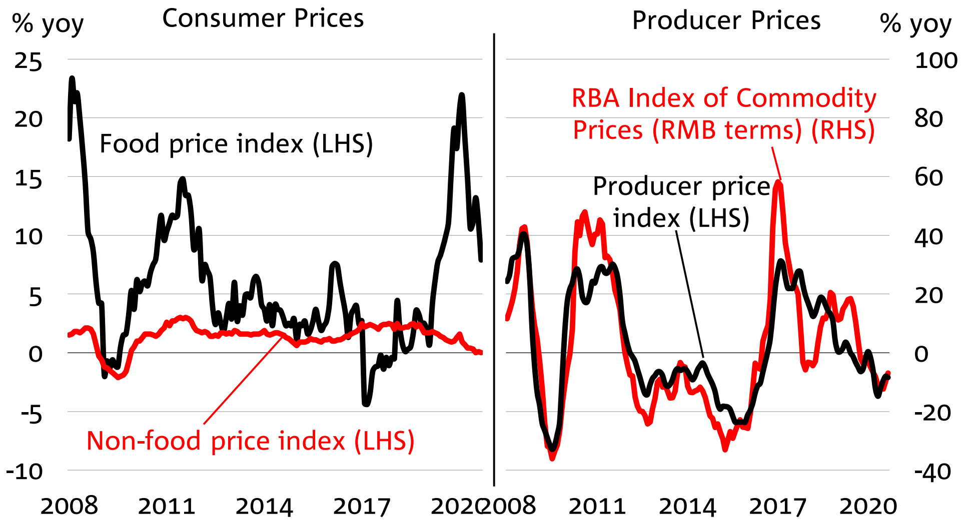
Real sales growth positive for the first time in 2020



Source: CEIC, NAB Economics

CONSUMER AND PRODUCER PRICES

Weakness in non-food and producer prices persists



Source: CEIC, RBA, NAB Economics

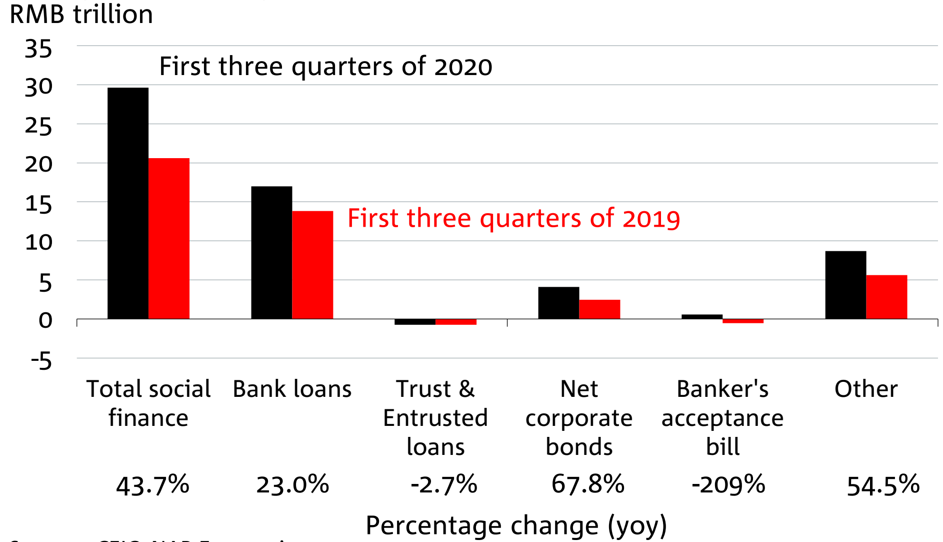
- The gradual recovery in China's retail sales continued in September, with nominal sales increasing by 3.3% yoy (compared with 0.5% in August) – although this remains well below the pre-COVID-19 trend.
- Retail price inflation was a little softer during the month, meaning that real retail sales increased by 2.5% yoy (from -1.1% yoy previously). This was the first positive reading in 2020.
- Consumer price growth continued to slow in September, with the Consumer Price Index increasing by 1.7% yoy (compared with 2.4% yoy in August and 2.7% yoy in July). Food prices have been the main driver of consumer prices across the past two years.
- Food price rose by 7.9% yoy in September (down from 11.2% yoy previously) – the weakest rate of increase since May 2019. Pork has been the key driver – with supply of the meat impacted by the African Swine Fever outbreak. Pork prices rose by 25.5% yoy in September, compared with 53% in August. Reports suggest that Chinese authorities may have exhausted or nearly exhausted strategic frozen pork stockpiles in recent months, meaning that pork inflation could accelerate again in coming months.
- Non-food price growth has been extremely weak in recent months – highlighting the ongoing softness in domestic consumption. Non-food prices were unchanged in year-on-year terms in September, compared with a 0.1% yoy increase in August. A 14.7% yoy fall in vehicle fuel prices contributed to this trend.
- Producer prices have continued to fall in year-on-year terms, down by 2.1% yoy in September, compared with 2.0% in August. In part this reflects falling commodity prices – with the RBA Index of Commodity Prices (converted into RMB terms) falling by 6.9% yoy, albeit this was a more modest decline than was recorded in August. It may also reflect the relative weakness in Chinese domestic consumption.

National Australia Bank

CREDIT CONDITIONS

NEW CREDIT ISSUANCE

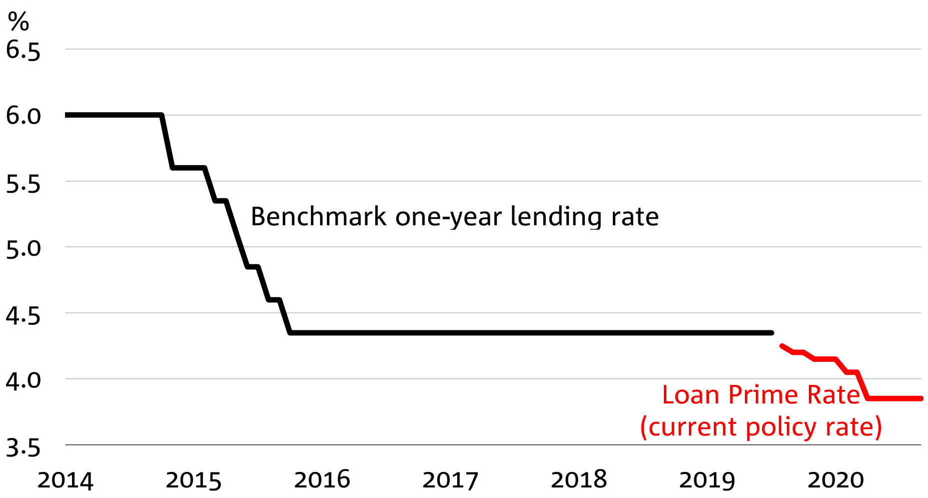
Strong growth in government and corporate bond issuance



Sources: CEIC, NAB Economics

MONETARY POLICY

PBoC has room to move, but seeks to control longer term risks



Source: CEIC, NAB Economics

- China's new credit issuance was slightly more modest in September, but remained strong – totalling RMB 3.5 trillion (compared with RMB 3.6 trillion in August). Compared with the previous month, bank lending accelerated, while there was a slowdown in non-bank issuance.
- Over the first three quarters of 2020, new credit issuance increased by 44% yoy to RMB 29.6 trillion. Bank loans accounted for the largest share of this total, however loans have grown comparatively slowly – up by around 23% yoy over this period to RMB 17.0 trillion.
- Growth in issuance has been even stronger in the non-bank sector – which rose by 86% yoy in the first three quarters to RMB 12.6 trillion. Unlike earlier periods of stimulus in China's recent history, this growth was not driven by shadow banking products (such as trust and entrusted loans and banker's acceptance bills) which have remained weak, but rather by government bonds (which rose by 69% yoy) and net corporate bond issuance (up by 68% yoy).
- The People's Bank of China (PBoC) has maintained stable monetary policy since the previous cut to its policy rate in April. Compared with other major economies, the PBoC has considerable policy room, but has flagged its intention to maintain "normal" policy for as long as possible – highlighting its concern around longer term risks, such as debt expansion and asset bubbles.

National Australia Bank

Group Economics

Alan Oster
Group Chief Economist
+61 3 8634 2927

Jacqui Brand
Personal Assistant
+61 3 8634 2181

Dean Pearson
Head of Behavioural & Industry Economics
+(61 3) 8634 2331

John Sharma
Economist
+(61 3) 8634 4514

Australian Economics and Commodities

Gareth Spence
Senior Economist – Australia
+(61 4) 36 606 175

Phin Ziebell
Economist – Agribusiness
+(61 4) 75 940 662

Behavioural & Industry Economics

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

Tony Kelly
Senior Economist
+(61 4) 77 746 237

Gerard Burg
Senior Economist – International
+(61 4) 77 723 768

Global Markets Research

Ivan Colhoun
Global Head of Research
+61 2 9237 1836