CHINA'S ECONOMY AT A GLANCE

MARCH 2021

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CONTACT

Gerard Burg, Senior Economist - International

NAB Group Economics

KEY POINTS

Don’t be fooled by surging annual growth rates – momentum is set to slow across 2021

- Interpreting Chinese data will become more challenging for the next few months – due to the extreme base effects related to restrictions imposed to control the spread of COVID-19 in early 2020. Few official Chinese data series are seasonally adjusted, meaning that comparing year-on-year trends is the typical approach. Year-on-year growth rates of many indicators will be extremely large for the next few months, until the sharp falls following last year’s lockdown drop out of the calculations. An example of how this can distort the underlying picture is the over 60% yoy increase in the value of China’s exports across January and February, even as business surveys indicate a weakening in new export orders.

- Growth in China’s industrial production surged by 35.1% yoy across January and February, a record high, however month-on-month data show weaker growth than during the period from April to October 2020, as China’s manufacturers were recovering from COVID-19 shutdowns. These data also highlight how much China relied on the industrial sector for its recovery – industrial production was around 17% higher than January-February 2019, whereas retail sales were just 6.4% stronger.

- China’s fixed asset investment grew strongly in the first two months of 2021, rising by 35% yoy. Growth in private sector investment outpaced that of state-owned enterprises in early 2021. SOEs provided the majority of investment growth in the early stages of China’s recovery from COVID-19, with private investment overtaking the state sector in Q4 2020.

- In the first two months of 2021, China’s trade surplus averaged US$51.6 billion, compared with a record high of US$78.2 billion in December 2020 and an average US$3.7 billion trade deficit across January and February 2020. There remains limited clarity around the Biden Administration’s approach towards the US-China trade relationship, albeit it is unlikely to return to the openness of the Obama Administration. China’s trade surplus with the US has steadily increased from early 2020 lows – totalling a new record high of US$349.2 billion in the twelve months to February 2021. This could further escalate tensions between the two countries.

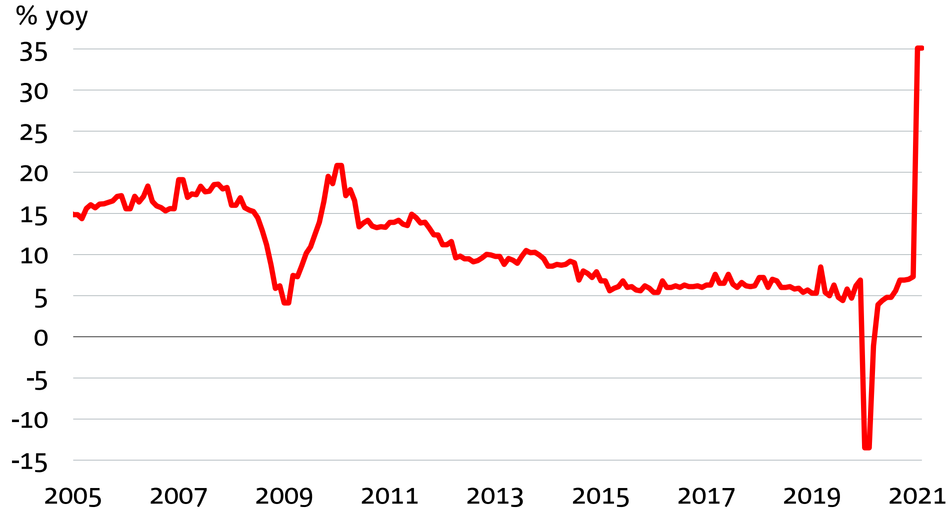
- In the first two months of 2021, China’s new credit issuance totalled RMB 6.9 trillion, an increase of 16.1% yoy. The bulk of this increase occurred in February – reflecting the sharp decline in new credit in February 2020 due to the impact of COVID-19 restrictions. Bank lending grew comparatively rapidly over the first two months, while non-bank lending declined overall.

- Authorities are attempting to unwind emergency support measures. At the Central Economic Work Conference in late 2020, the PBoC signalled it intends to slow credit creation in coming months, but it is not necessarily set to increase the policy rate. Tighter restrictions on property lending could form part of this strategy. This monetary tightening is set to be paired with a fiscal contraction as well. Due to the opaque nature of local government finances, it is difficult to be clear around the size of the contraction – but some early estimates put it in the range of 2-3% of GDP.

INDUSTRIAL PRODUCTION

INDUSTRIAL PRODUCTION SOARED IN EARLY 2021

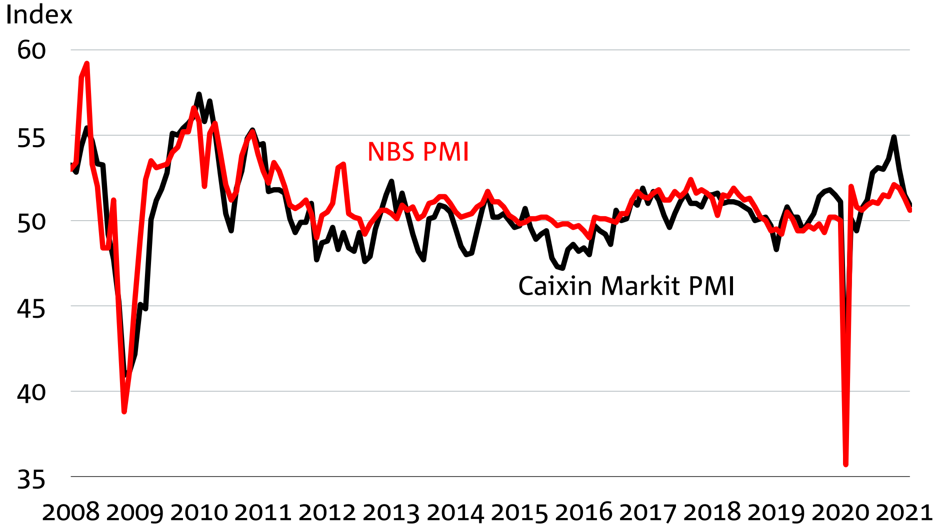
COVID-19 closures in early 2020 distort yoy growth



Source: CEIC, NAB Economics

MANUFACTURING SURVEYS WEAKER IN FEBRUARY

Weaker results in output and export orders drag measures lower



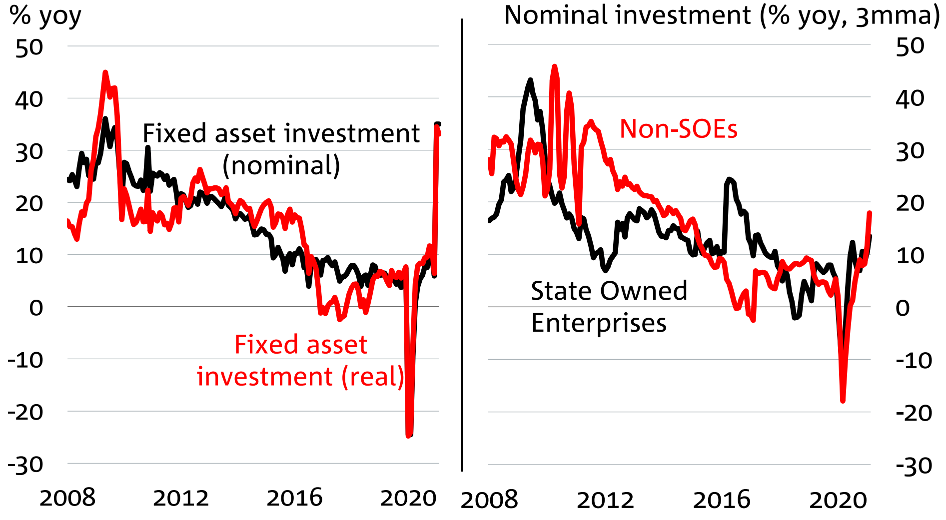
Source: CEIC, NAB Economics

- Growth in China's industrial production surged by 35.1% yoy across January and February – the largest rate of growth on record (stretching back to January 1995) – with the sheer scale of this increase reflecting the impact of industrial closures in February 2020 to control the spread of COVID-19.
- The seasonally adjusted month-on-month industrial production data showed an increase of 0.69%, marginally stronger than growth between November 2020 and January 2021, but weaker than that seen from April to October 2020 – when manufacturing was recovering from the shutdowns.
- There were some stark differences in the growth rates by major sub-sector. Booming global demand for electronics saw computer production increase by 112% yoy and mobile phones by 49.2% yoy. Similarly, motor vehicle production rose by almost 90% yoy.
- Output of construction related materials was more mixed. While cement output rose by 61% yoy, crude steel production increased by just 12.9% yoy. The increase in electricity output was also comparatively modest – up by 19.5% yoy.
- China's major manufacturing surveys have continued to trend down in recent months, albeit they remained in positive territory. The Caixin Markit PMI survey was at 50.9 points in February (from 51.5 points previously), while the official NBS PMI survey was weaker, at 50.6 points (from 51.3 points in January).
- Both surveys noted weaker output growth in February, while new export orders were negative for the second straight month in the Caixin survey and for the first time since August 2020 for the NBS survey.

INVESTMENT

FIXED ASSET INVESTMENT

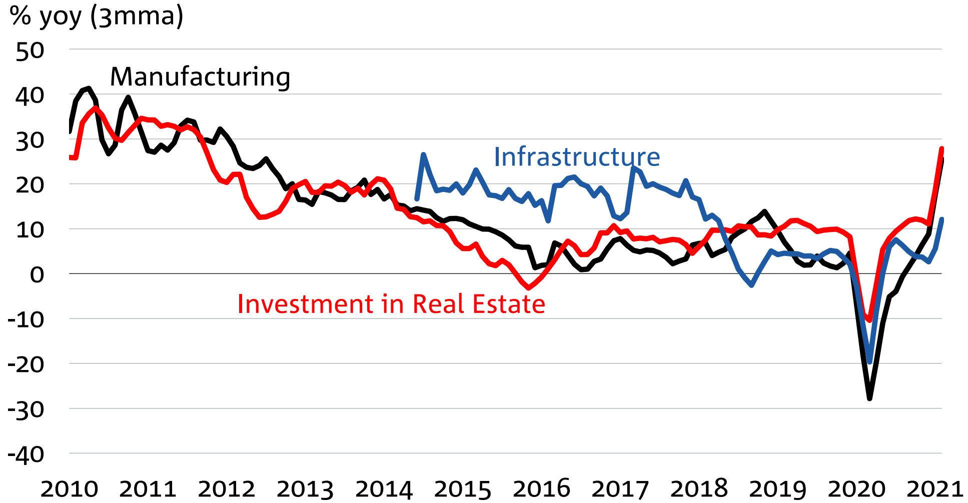
Investment surges following early 2020 weakness



Source: CEIC, NAB Economics

FIXED ASSET INVESTMENT BY SECTOR

Tighter funding likely to see infrastructure investment underperform



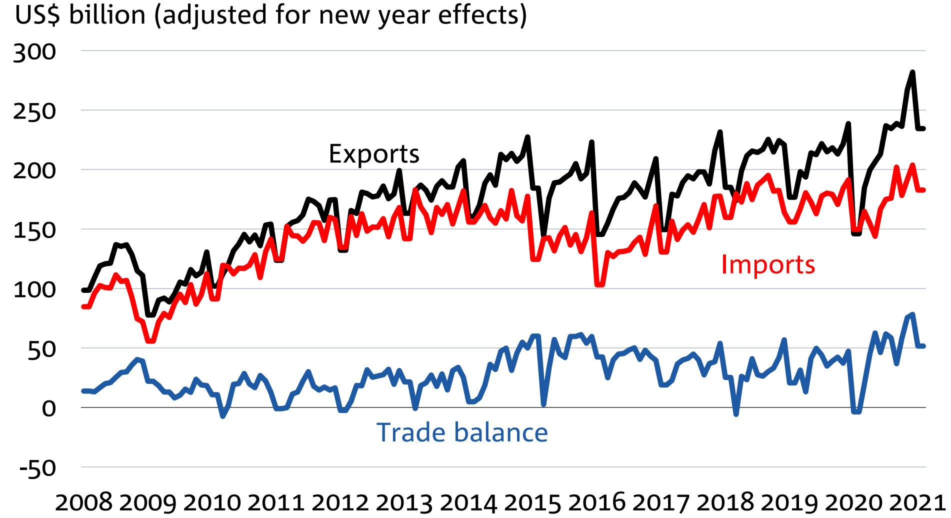
Source: CEIC, NAB Economics

- China's fixed asset investment grew strongly in the first two months of 2021, rising by 35% yoy. As with a range of other indicators, this surge in growth was the result of base effects – with investment plunging in February 2020 due to COVID-19 restrictions.
- There was a slight increase in producer prices in the first two months – which is closely tied to the cost of investment goods – meaning that in real terms, investment grew marginally more weakly, at around 33.8% yoy over this period.
- Growth in private sector investment outpaced that of state-owned enterprises in early 2021 – increasing by 36.2% yoy (compared with 32.9% yoy for SOEs). SOEs provided the majority of investment growth in the early stages of China's recovery from COVID-19, with private investment overtaking the state sector in Q4 2020.
- There was also some divergence between major industries. Investment in both manufacturing and real estate increased strongly in the first two months of 2021 – up by almost 26% yoy and 28% yoy respectively. In contrast, infrastructure investment rose by nearly 37% yoy – however this strength is unlikely to last.
- Infrastructure investment was weak in the latter months of 2020 and China's central government has cut the local government special bond quota – a primary source of funding for infrastructure development – for this year by just over 2.5%.

INTERNATIONAL TRADE – TRADE BALANCE AND IMPORTS

CHINA'S TRADE BALANCE

Trade surplus remained historically high in early 2021



Sources: CEIC, NAB Economics

CHINA'S TRADE SURPLUS WITH THE UNITED STATES

Rolling surplus in February exceeds pre-trade war peak

Sources: CEIC, NAB Economics

- In the first two months of 2021, China's trade surplus averaged US$51.6 billion, compared with a record high of US$78.2 billion in December 2020 and an average US$3.7 billion trade deficit across January and February 2020. Exports plunged in February 2020 as the COVID-19 pandemic impacted Chinese manufacturing production.

- There remains limited clarity around the Biden Administration's approach towards the US-China trade relationship, albeit it is unlikely to return to the openness of the Obama Administration. China's trade surplus with the US has steadily increased from early 2020 lows – totalling a new record high of US$349.2 billion in the twelve months to February 2021. This could further escalate tensions between the two countries.

- Over the first two months of 2021, China's imports rose by 22.2% yoy, to average US$182.8 billion a month. While this was lower than the record high US$203.8 billion level recorded in December 2020, it was close to the average level recorded across the second half of the year.

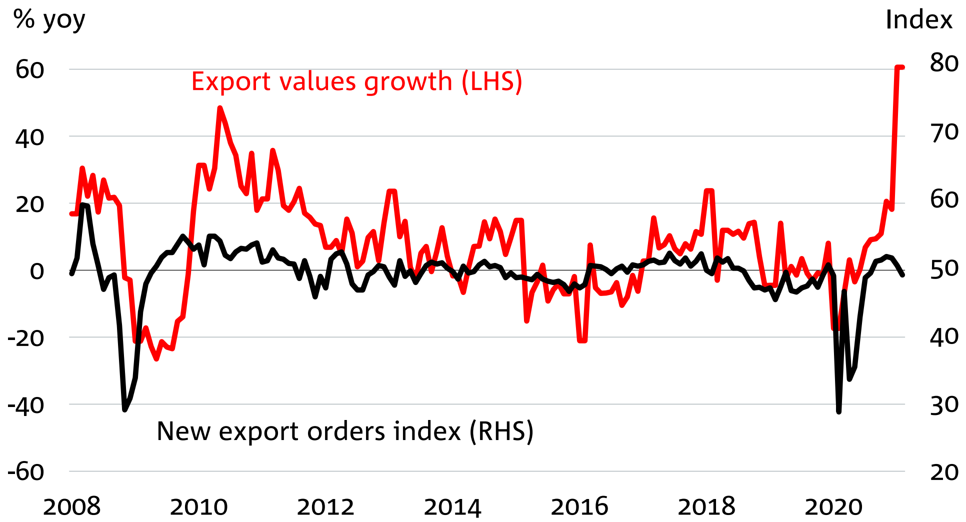
- It is worth noting that there has been a considerable increase in commodity prices in recent months – largely reflecting the improving global economic environment, particularly as COVID-19 vaccines rollout. In US dollar terms, the RBA Index of Commodity Prices rose by almost 28% yoy across January and February. Our estimate of China's import volumes rose by 12.8% yoy over this period.

- There was a modest increase in the import volumes for most major commodities in the first two months of 2021. Imports of refined copper rose by 4.7% yoy, while crude oil imports increased by 4.1% yoy. Iron ore imports rose more gradually – up by 2.7% yoy. The key exception was coal – with imports falling 39.5% yoy over January and February. This followed a seasonally unusual surge in coal imports in December, which may have resulted in major coal consumers being well stocked in the new year. China is continuing to seek coal volumes from non-Australian sources, leading to a realignment of coal trade in Asia.

INTERNATIONAL TRADE – EXPORTS

EXPORT GROWTH SURGES DUE TO COVID-19 BASE EFFECTS

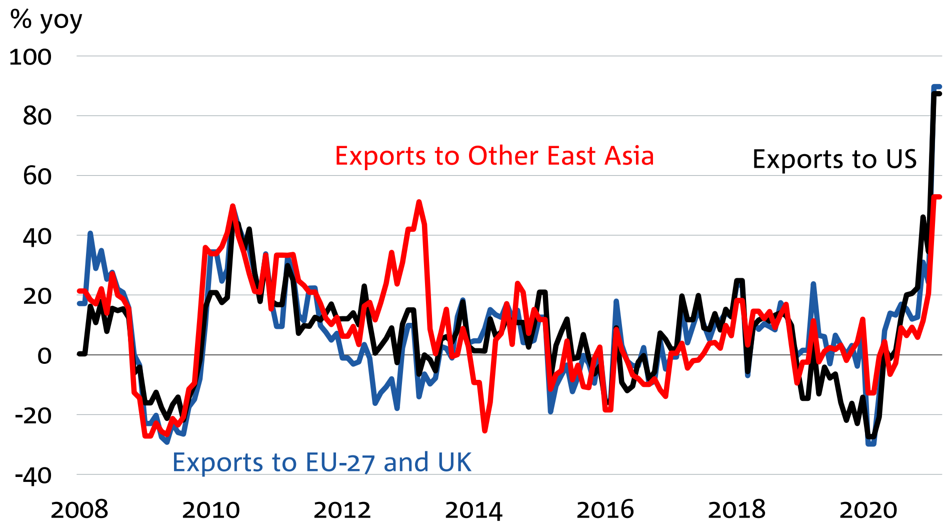
New export order measure turned negative



Source: CEIC, NAB Economics

EXPORTS TO MAJOR TRADING PARTNERS

Asian growth smaller due to smaller base effects



Sources: CEIC, NAB Economics

- China's exports surged across January and February 2021 – increasing by 60.6% yoy over the period to average US$234.4 billion a month – however the scale of this growth largely reflected the impact of factory shutdowns in 2020 due to China's COVID-19 response.

- Chinese exporters have benefited from very high demand for medical supplies and personal protective equipment from the global healthcare sector, while electronics and furniture demand has strengthened during to the increased trend of working from home. As vaccine rollouts ramp up, demand in these sectors may gradually start to slacken. This may be reflected in the new export orders measure in the manufacturing PMI surveys – with both major surveys negative in February.

- There was extremely strong growth in exports across China's major trading partners. Exports to the European Union and United Kingdom rose by almost 90% yoy in the first two months of the year, while exports to the United States rose by over 87% yoy. In contrast, exports to East Asia rose by a smaller amount – up by almost 53% yoy – however exports to this region fell less dramatically in early 2020 – resulting in a smaller base effect.

- Within East Asia, exports grew slightly more rapidly to Hong Kong (up by almost 57% yoy) than the rest of the region (51% yoy), where Vietnam was the biggest contributor to growth.

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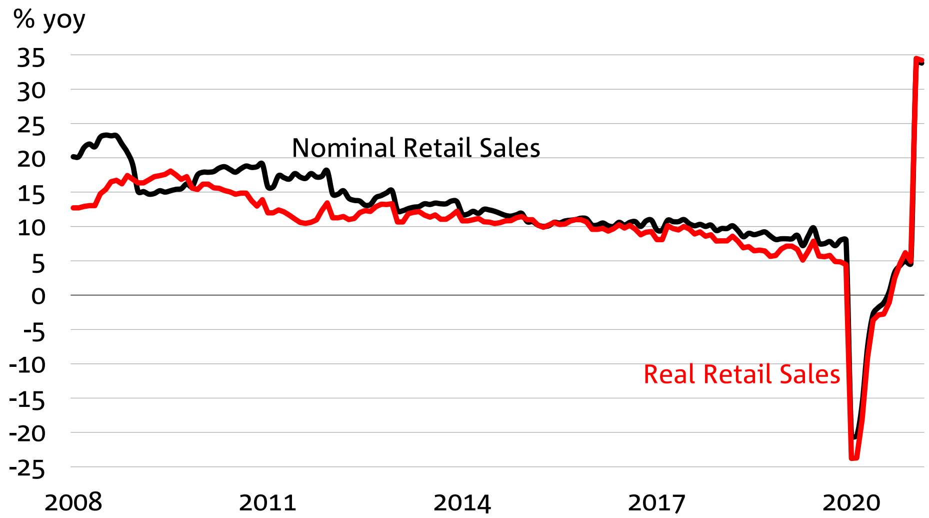
RETAIL SALES AND INFLATION

RETAIL SALES SURGE ON BASE EFFECTS

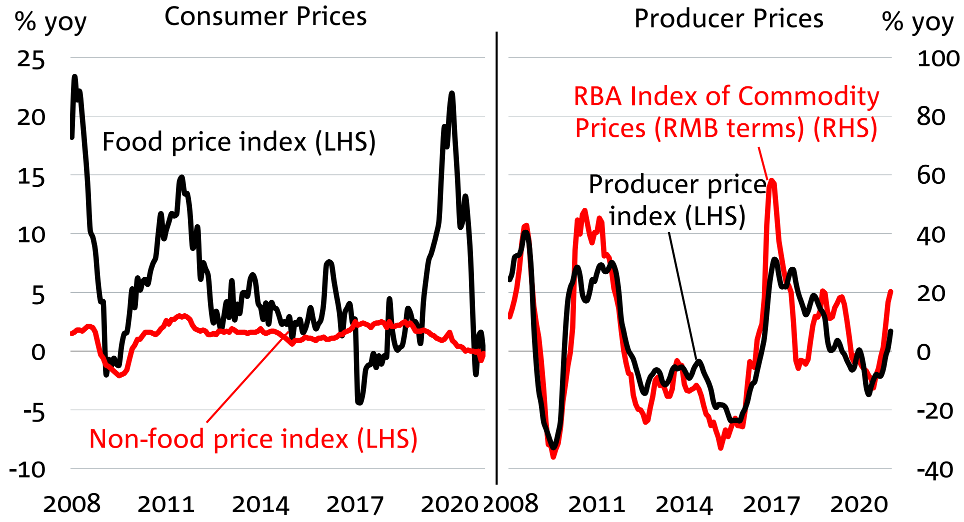
Real sales bolstered by slight retail price deflation



Source: CEIC, NAB Economics

CONSUMER AND PRODUCER PRICES

Consumer prices weak; PPI up on stronger commodities



Source: CEIC, RBA, NAB Economics

- Nominal retail sales rebounded in the first two months of 2021 – increasing by 33.8% yoy, with sales having fallen by 20.5% yoy in the same period in 2020. When combined, retail sales in January and February were around 6.4% stronger than the same period in 2019.
- Retail prices fell marginally over this period, meaning that real retail sales increased by around 34.3% yoy in the first two months.
- China's consumer prices fell across January and February – down by 0.3% yoy and 0.2% yoy respectively, compared with a marginal 0.2% yoy increase in December.
- Food price trends were mixed over this period, rising by 1.6% yoy in January, before falling by 0.2% yoy in February. Pork prices – which had a major upward influence on food price inflation across much of 2019 and 2020 – fell by 14.9% yoy in February (following a more modest decline in January).
- In contrast, non-food prices fell more strongly in January – down by 0.8% yoy – before easing more modestly in February – declining by 0.2% yoy. This was consistent with trends in vehicle fuel prices, down by 13.4% yoy in January and 5.2% yoy in February – with the potential for increases in coming months as global oil markets continue to recover.
- Producer prices rose comparatively strongly in February – up by 1.7% yoy, the largest increase since November 2018. There was a clear distinction between producer goods (or intermediate products), where prices rose by 2.3% yoy, and consumer goods – where prices continued to fall modestly. In part this reflects the increase in commodity prices – with the RBA Index of Commodity Prices, converted in RMB terms, increasing by around 20% yoy in February.

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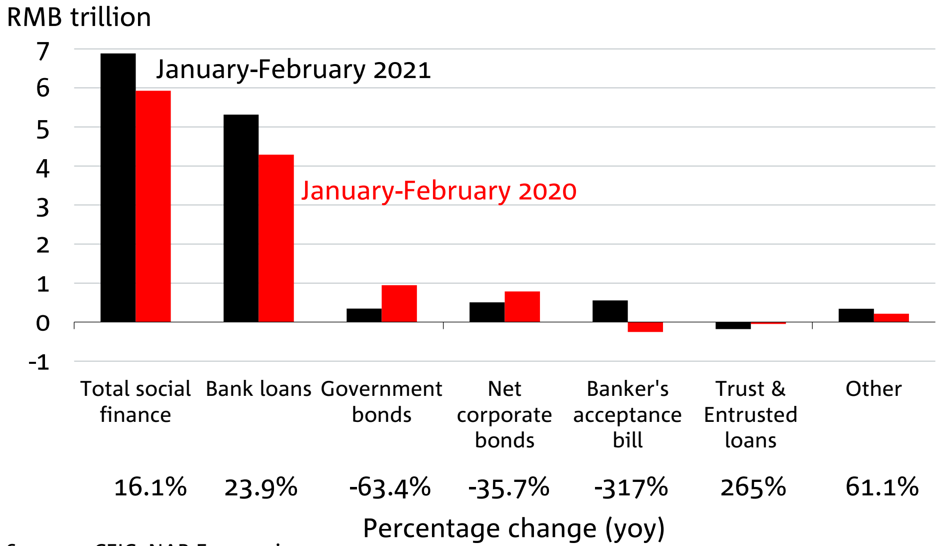
CREDIT CONDITIONS

NEW CREDIT ISSUANCE

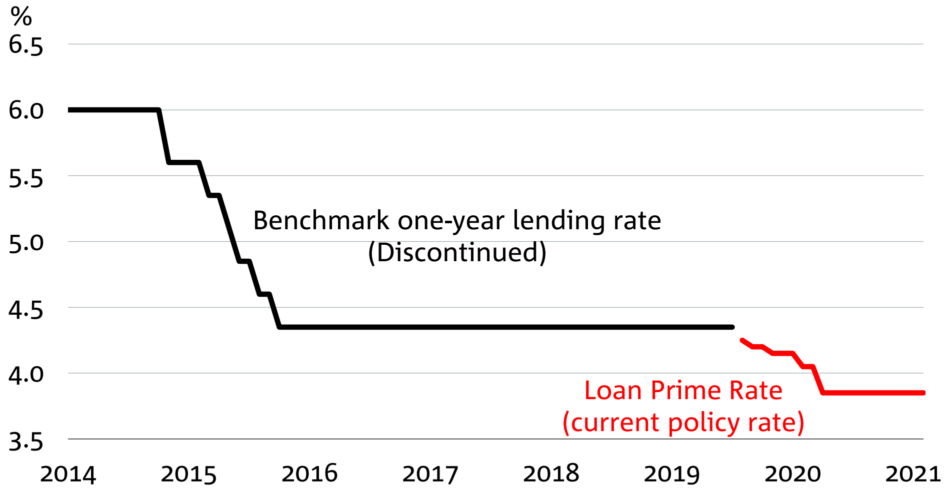
Bank lending the main source of growth in early 2021



Sources: CEIC, NAB Economics

MONETARY POLICY

PBoC may keep rates low as it restricts credit growth



Source: CEIC, NAB Economics

- In the first two months of 2021, China's new credit issuance totalled RMB 6.9 trillion, an increase of 16.1% yoy. The bulk of this increase occurred in February – reflecting the sharp decline in new credit in February 2020 due to the impact of COVID-19 restrictions.
- Bank lending grew comparatively rapidly over the first two months – increasing by 23.9% yoy to RMB 5.3 trillion.
- In contrast, non-bank lending declined overall, down by 4.2% yoy to RMB 1.6 trillion. Trends were highly mixed among the sub-sectors, with declines in corporate and government bond issuance (2020's main contributors to non-bank lending growth) of 36% yoy and 63% yoy respectively. There was a sizeable increase in banker's acceptance bills – a component of the shadow banking sector.
- The People's Bank of China (PBoC) has held its policy rates stable since April 2020, having cut rates much more modestly than other global central banks. That said, across last year it added liquidity to financial markets and supported lower than pre-COVID-19 interbank rates (with the exception of a short term spike in late January).
- Authorities are attempting to unwind emergency support measures. At the Central Economic Work Conference in late 2020, the PBoC signalled it intends to slow credit creation in coming months, but it is not necessarily set to increase the policy rate. Tighter restrictions on property lending could form part of this strategy.
- This monetary tightening is set to be paired with a fiscal contraction as well. Due to the opaque nature of local government finances (the level of government that accounts for the majority of fiscal spending) it is difficult to be clear around the size of the contraction – but some early estimates put it in the range of 2-3% of GDP.

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

Australian Economics and Commodities
Gareth Spence
Senior Economist – Australia
+(61 4) 36 606 175

Kaixin Owyong
Senior Economist
+(61 0) 436 679 908

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