CHINA'S ECONOMY AT A GLANCE

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National Australia Bank

CONTENTS

CONTACT

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KEY POINTS

Growth slowing as base effects wash away; consumers continue to lag industry

- Slowing trends for most of the key indicators in May largely reflected the impact of diminishing base effects. As China's recovery from COVID-19 was well underway by May, year-on-year growth in May has slowed from the peaks seen at the start of the year. That said, China's economic growth remains imbalanced – with an over-reliance on the industrial sector and exports, while consumption remains relatively subdued. Overall our outlook for China remains unchanged, with growth at 9.5% in 2021, before slowing to 5.8% in 2022 and 5.6% in 2023.

- China's industrial production rose by 8.8% yoy in May, easing from the 9.8% yoy growth recorded in April. Base effects largely explain this slowing in growth – with the seasonally adjusted month-on-month growth unchanged in May.

- The slowing in fixed asset investment was larger than base effects alone – with real investment falling by 4.7% yoy (in part reflecting the surge in producer prices). The contraction in new credit issuance may be a driver, with nominal investment in infrastructure falling year-on-year in May.

- China's trade surplus was marginally wider in May – totalling US$45.5 billion (compared with US$42.9 billion in April). This increase was driven by a slight month-on-month decline in imports (from high levels), with the value of exports essentially unchanged. China's rolling twelve month surplus with the United States set a new record in May (the fourth straight month this has occurred) – rising to US$358.1 billion. Trade tensions between the two countries remain and a White House review of supply chain vulnerabilities (published on June 8) could reduce US demand for China's exports in key areas (such as semi-conductors, large capacity batteries, critical minerals and pharmaceuticals).

- The uptick in retail prices in May meant that real retail sales increased by 10.1% yoy (from 15.8% yoy previously). When compared with same month in 2019, real retail sales increased by 6.1% in May, compared with 5.4% in April. This increase remains well below the growth recorded in the industrial sector – highlighting the ongoing imbalance in China's economy.

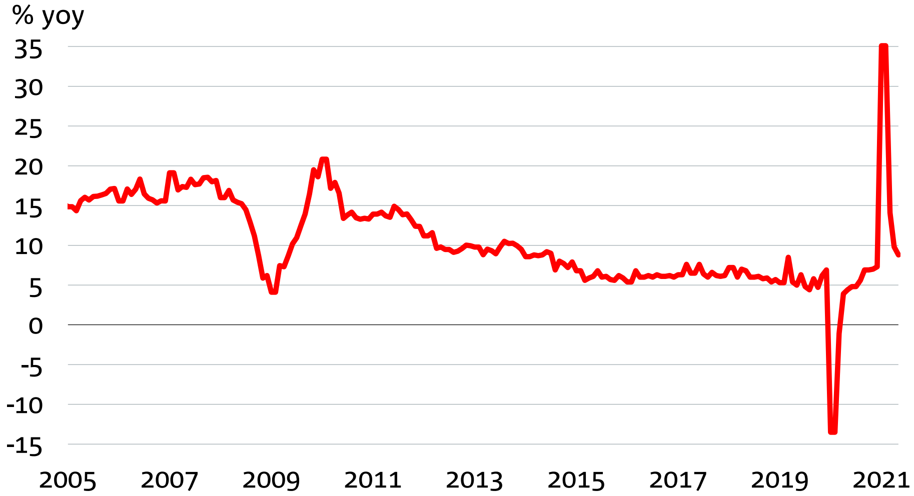
- In the first five months of 2021, China's new credit issuance totalled RMB 14.0 trillion, a decrease of 19.3% yoy. Bank lending remains the largest share of new credit issuance, increasing marginally (up 0.3% yoy) over this period to RMB 10.8 trillion. In contrast, non-bank lending plunged in the first five months of 2021 – down by 51% yoy to RMB 3.3 trillion.

- Despite the recent inflationary pressures – particularly for producer prices – the Governor of the People's Bank of China (PBoC) has argued recently that inflation is under control and that monetary policy stability was a priority. The PBoC has held its main policy rate – the Loan Prime Rate – at 3.85% since April 2020, and Governor Yi's comments are consistent with our view of stable rates for some time.

INDUSTRIAL PRODUCTION

INDUSTRIAL PRODUCTION

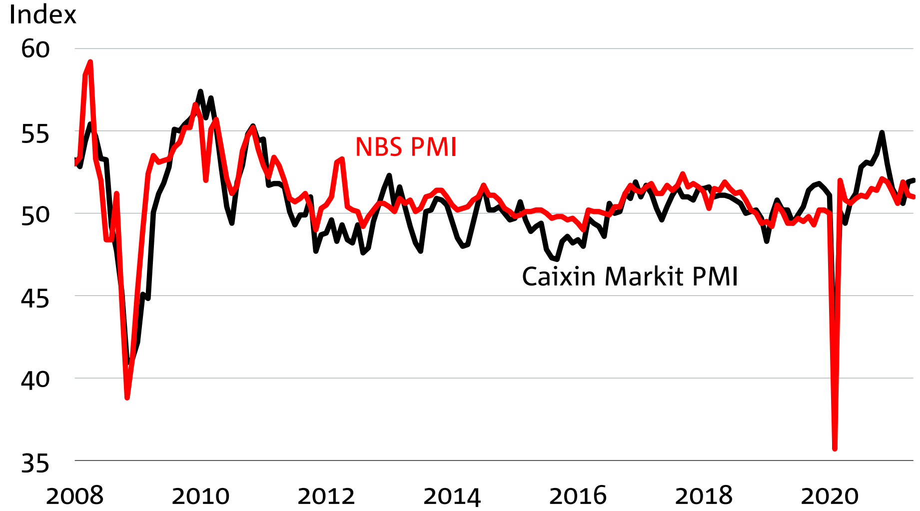
Diminishing base effects largely explain slowing growth



Source: CEIC, NAB Economics

MANUFACTURING SURVEYS REMAIN DIVERGENT

Differing views on export demand in the two surveys



Source: CEIC, NAB Economics

- China's industrial production rose by 8.8% yoy in May, easing from the 9.8% yoy growth recorded in April. Base effects continue to diminish – reflecting that China's economy was already well into its recovery from COVID-19 by May 2020 – with this factor reflecting much of the decline.

- On a seasonally adjusted basis, month-on-month growth in industrial production was unchanged in May – at 0.52%. While monthly growth has slowed consistently since late 2020, the relative stability in growth in recent months points to a sector that has essentially completed its recovery and is now in a more typical growth phase.

- Trends in China's major industrial sub-sectors differed considerably in May. Output of electronics rose strongly – up by 12.7% yoy – continuing to benefit from strong global demand, while steel production rose by 6.6% yoy to a new record high.

- In contrast, output of both cement and motor vehicles fell in May – down by 3.2% yoy and 4.0% yoy respectively.

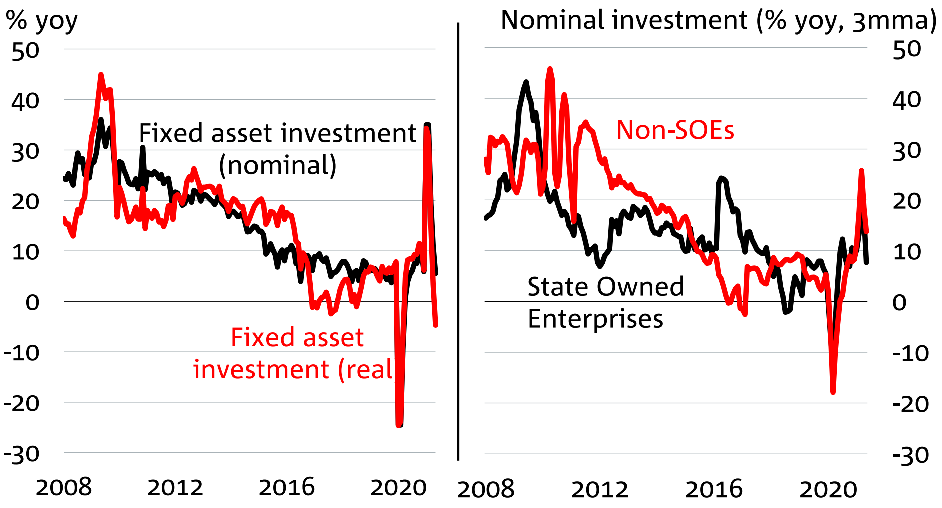
- China's major manufacturing surveys continued to diverge in May. The official NBS PMI eased marginally in May, down to 51.0 points (from 51.1 points previously). In contrast, the private sector Caixin Markit PMI edged higher, to 52.0 points (from 51.9 points in April).

- There were some notable differences driving these trends. While both domestic and export demand were strong in the Caixin Markit survey, new export orders deteriorated in the official NBS survey – turning negative for the first time since a brief dip in February and the end of sustained weakness in August 2020.

INVESTMENT

FIXED ASSET INVESTMENT

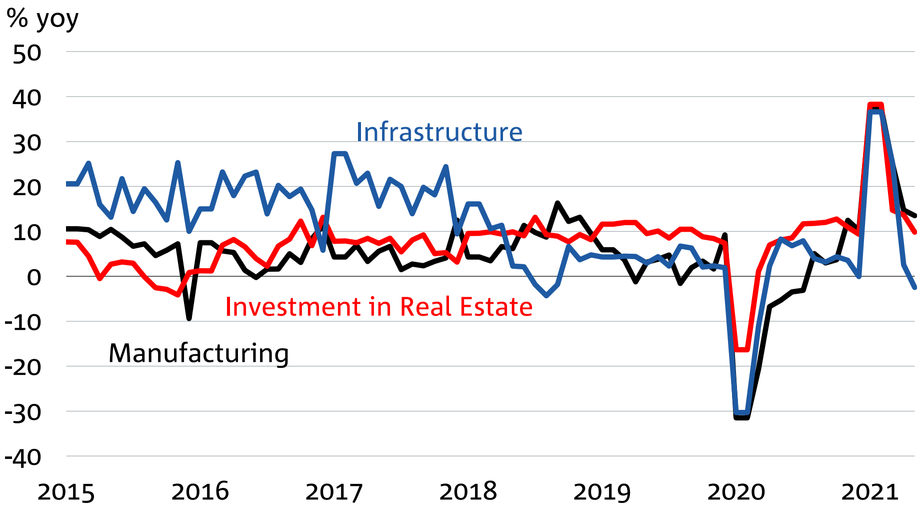
Soaring input costs drive decline in real investment in May



Source: CEIC, NAB Economics

FIXED ASSET INVESTMENT BY INDUSTRY

Nominal investment in infrastructure fell yoy in May



Source: CEIC, NAB Economics

- Growth in China's fixed asset investment slowed considerably in May – down to 5.5% yoy (from 10.9% yoy previously). Although diminishing base effects contributed to this slowdown – as with the case with other indicators – this downturn appears to be larger than base effects alone.

- Producer price inflation has accelerated sharply in recent months – with the increase in factory gate prices flowing through into the cost of investment. This means that in real terms, fixed asset fell in year-on-year terms – down by 4.7%.

- In part, this decline may reflect the impact of tighter access to funding – given that new credit issuance has declined by over 19% in the year to date, with the potential for differing impacts in different industries. For example, nominal investment in infrastructure declined 2.5% yoy in May.

- In contrast, investment in manufacturing rose by 13.5% yoy in May, while investment in real estate increased by 9.8% yoy.

- There was a marked slowdown in investment by state-owned enterprises in May – with nominal investment contracting by 3.3% yoy. In stark contrast, investment by private sector firms rose by 10.7% yoy. The differences between the two sectors may reflect differing base effects – with SOEs leading the early stage of the investment recovery in 2020.

- When compared with the level of investment in May 2019, investment by private firms increased by 10.6% in May 2021, compared with a 7.7% increase from SOEs.

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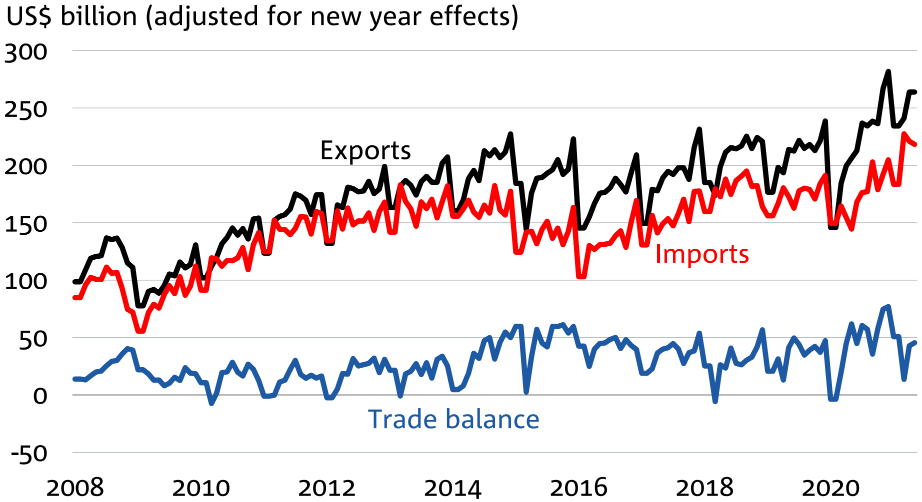
INTERNATIONAL TRADE – TRADE BALANCE AND IMPORTS

CHINA'S TRADE BALANCE

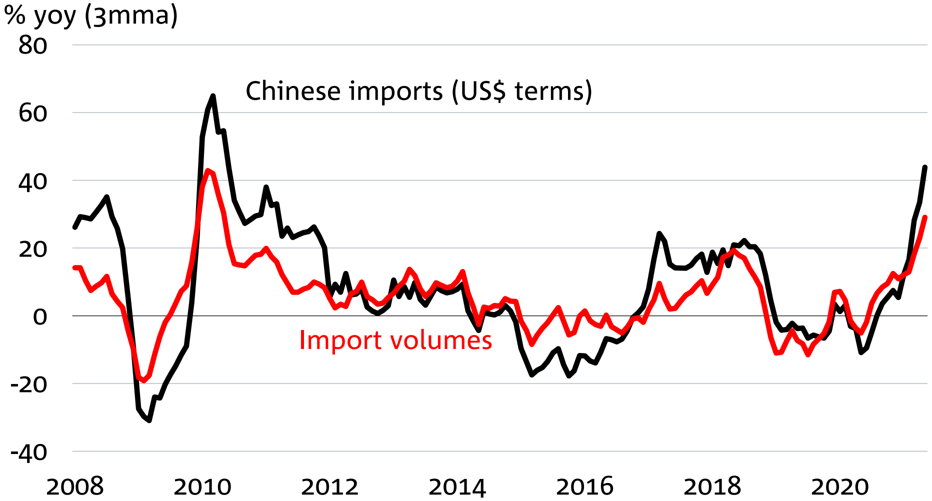
Trade surplus widened in May, as imports eased from high levels



Sources: CEIC, NAB Economics

CHINA'S IMPORT VALUES AND VOLUMES

Strong yoy increase in both prices and volumes in May



Source: CEIC, NAB Economics

- China's trade surplus was marginally wider in May – totalling US$45.5 billion (compared with US$42.9 billion in April). This increase was driven by a slight month-on-month decline in imports (from high levels), with the value of exports essentially unchanged.

- China's rolling twelve month surplus with the United States set a new record high in May (the fourth straight month this has occurred) – rising to US$358.1 billion. Trade tensions between the two countries remain and a White House review of supply chain vulnerabilities (published on June 8) could reduce US demand for China's exports in key areas (such as semi-conductors, large capacity batteries, critical minerals and pharmaceuticals).

- China's imports eased month-on-month in May to US$218.4 billion, compared with US$221.1 billion previously. That said, in year-on-year terms, imports rose by 51.1% (compared with a 43.1% yoy increase in April). This increase reflects both price and volume effects – with volume growth reflecting the impact of widespread COVID-19 lockdowns in May 2020 that limited the capacity of many countries to supply China with inputs.

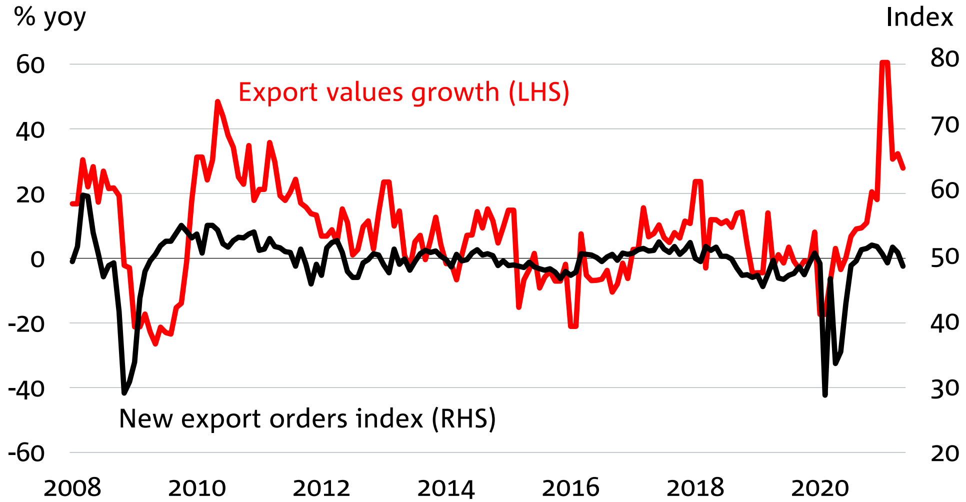
- Global commodity prices rose strongly in May, with the RBA Index of Commodity Prices increasing by 47.5% yoy. Price increases have been particularly noticeable in metals markets, with iron ore and copper rising to record highs – given supply constraints and strong demand. Our estimate of import volumes uses commodity prices as a proxy for China's import prices. This suggests that import volumes rose by 33.4% yoy in May, up from 28.1% yoy in April.

- That strong growth was not evident in the imports of major commodities that we track. Iron ore and refined copper imports rose modestly – up by 3.2% yoy and 2.2% yoy respectively. In contrast, coal imports fell by 4.6% yoy and crude oil imports fell by 14.6% yoy. Digging further into China's import data, there were large scale increases in imports of natural gas and higher value machinery and equipment (including motor vehicles and aircraft).

INTERNATIONAL TRADE – EXPORTS

EXPORT VALUE AND NEW EXPORT ORDERS

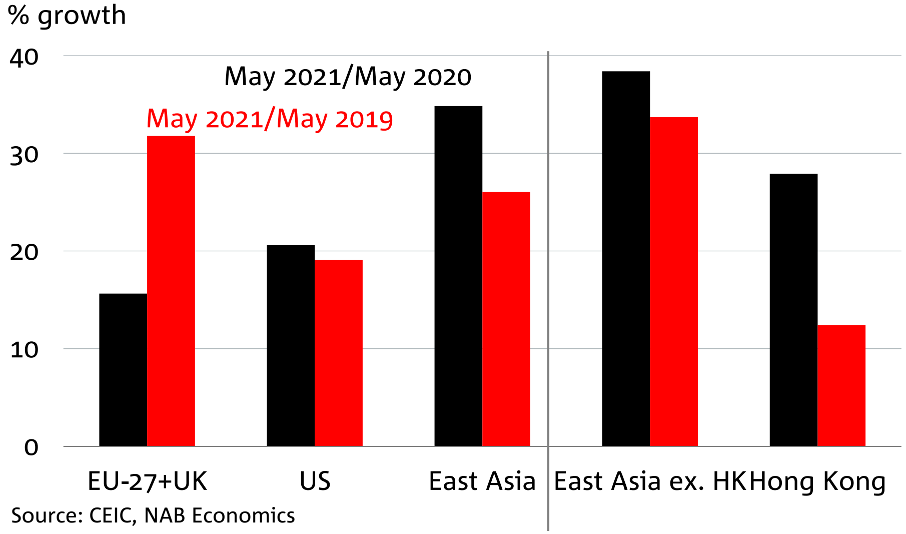
Export growth remains high, but surveyed new orders weaker



Source: CEIC, NAB Economics

EXPORTS TO MAJOR TRADING PARTNERS

Stronger growth in Europe and non-HK Asia in the past two years



Source: CEIC, NAB Economics

- In month-on-month terms, China's exports were essentially unchanged in May – remaining at US$263.9 billion. In year-on-year terms, this represented an increase of 27.9%. China's exports were negatively impacted in May 2020 by COVID-19 shutdowns in some of its major trading partners.
- The new export orders measure in the NBS PMI survey deteriorated in May – turning negative at 48.3 points (compared with a fairly neutral 50.4 points in April). This was the weakest reading for this measure since June 2020 (as China's exports were starting to recover).
- There remains some divergence in export growth to China's major trading partners. There was strong growth in exports to East Asia in May – increasing by 34.8% yoy – compared with an increase of 20.6% yoy for the United States and 15.6% yoy for the European Union 27 plus the United Kingdom.
- While it appears that export growth to Europe has lagged other markets, this is due to base effects. Exports to Europe rose by almost 14% yoy in May 2020, compared with year-on-year declines in the other regions. Compared with May 2019, exports to the EU-27+UK have increased more rapidly than those to East Asia.
- That said, exports to Hong Kong fell sharply in May 2020 and recovered less rapidly in May 2021. There is also considerable inconsistency re-emerging between the trade data produced by China and Hong Kong Customs. Excluding Hong Kong, exports to East Asia rose by 38.4% yoy – led by Vietnam, Malaysia and South Korea.

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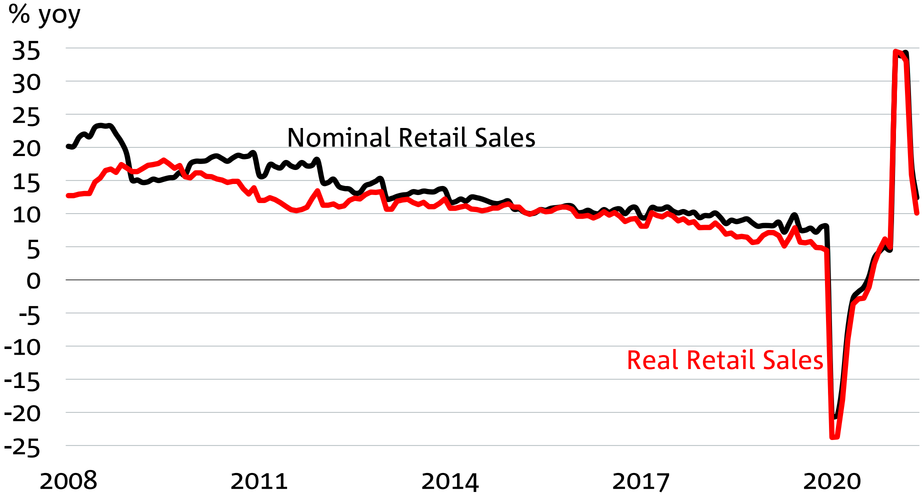
RETAIL SALES AND INFLATION

SALES GROWTH SLOWS AS BASE EFFECTS DIMINISH

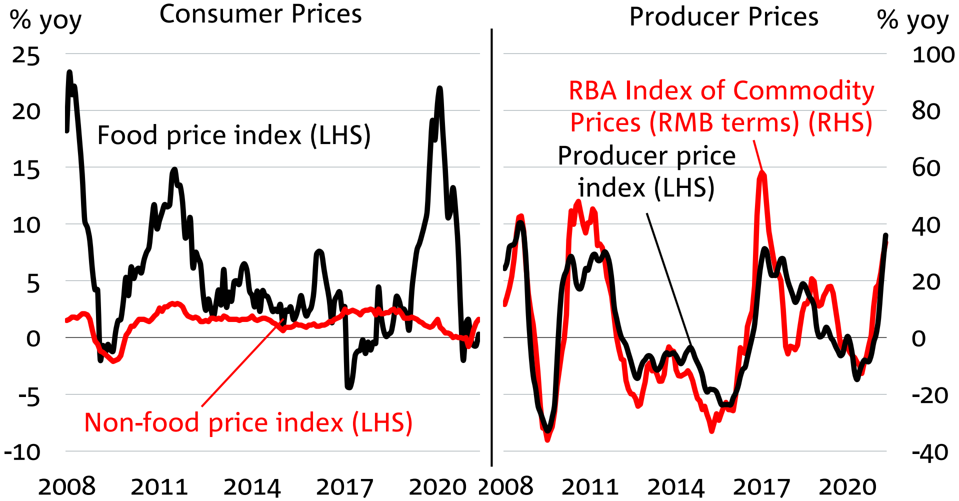
However sales growth lags industrial sector growth



Source: CEIC, NAB Economics

CONSUMER AND PRODUCER PRICES

Rising commodity prices adding inflationary pressure



Source: CEIC, RBA, NAB Economics

- Nominal growth in China's retail sales slowed again in May – with sales increasing by 12.4% yoy (compared with 17.7% yoy in April). Diminishing base effects are a major contributor for the slow down in growth – given that China's recovery from COVID-19 was well underway in May 2020.
- The uptick in retail prices in May meant that real retail sales increased by 10.1% yoy (from 15.8% yoy previously). When compared with same month in 2019, real retail sales increased by 6.1% in May, compared with 5.4% in April. This increase remains well below the growth recorded in the industrial sector – highlighting the ongoing imbalance in China's economy.
- China's headline consumer prices accelerated in May, with the consumer price index increasing by 1.3% yoy (compared with 0.9% yoy in April). There was a considerable turnaround in food prices, combined with the continuing uptrend in non-food prices.
- Food prices rose by 0.3% yoy in May, compared with a 0.7% yoy fall recorded in both March and April. While prices for meat continued to fall – led by pork – there was a sizeable acceleration in price growth for fresh vegetables, eggs and fish. There remains a risk that pork prices could climb once again, with a new strain of African Swine Fever spreading in the north eastern provinces.
- Non-food prices rose by 1.6% yoy in May – up from 1.3% yoy in April. Rising fuel prices remain a major contributor to this trend – with vehicle fuel prices up by 21.3% yoy, reflecting the increase in global oil prices.
- Producer prices rose strongly again in May – increasing by 9.0% yoy (from 6.8% yoy in April). Global commodity prices have risen strongly in recent months, with the RBA Index of Commodity prices (converted to RMB terms) increasing by 33.5% yoy in May – supported by record high prices for iron ore and copper.

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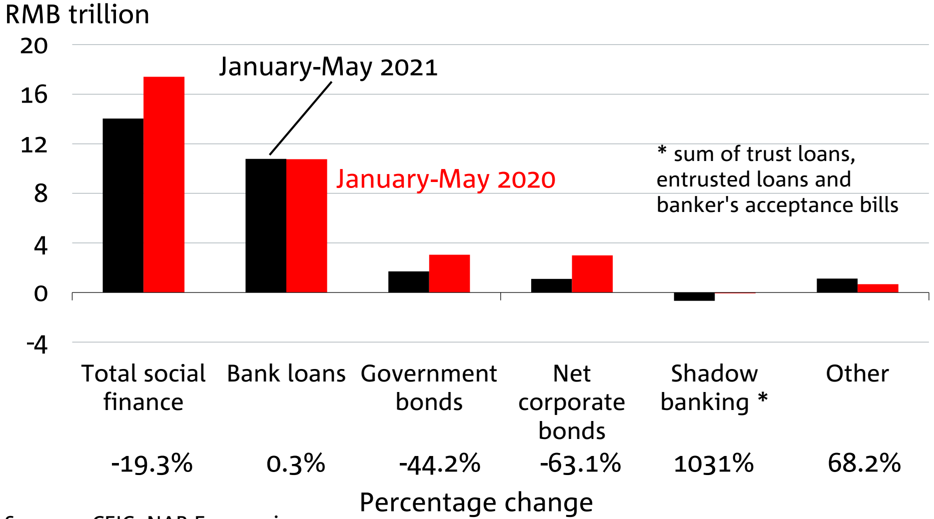
CREDIT CONDITIONS

NEW CREDIT ISSUANCE

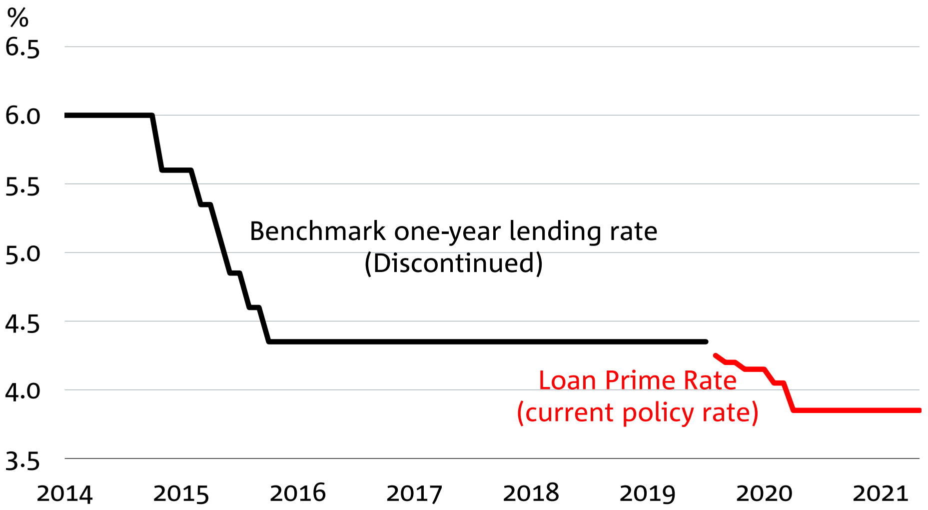
Weaker new issuance driven by declining bonds



Sources: CEIC, NAB Economics

MONETARY POLICY

PBoC signal rates to remain stable for some time



Source: CEIC, NAB Economics

- China's new credit issuance declined sharply year-on-year again in May – down by almost 40% yoy. That said, credit issuance in the second quarter of 2020 was incredibly strong, as government bond issuance soared to support China's recovery from the impact of COVID-19.

- In the first five months of 2021, China's new credit issuance totalled RMB 14.0 trillion, a decrease of 19.3% yoy. Bank lending remains the largest share of new credit issuance, increasing marginally (up 0.3% yoy) over this period to RMB 10.8 trillion.

- In contrast, non-bank lending plunged in the first five months of 2021 – down by 51% yoy to RMB 3.3 trillion. It is interesting to note that this level is also weaker than the first five months of 2019. Over this period, corporate bond issuance fell by 63% yoy and government bond issuance decreased by 44% yoy.

- Despite the recent inflationary pressures – particularly for producer prices – the Governor of the People's Bank of China (PBoC) has argued recently that inflation is under control and that monetary policy stability was a priority. The PBoC has held its main policy rate – the Loan Prime Rate – at 3.85% since April 2020, and Governor Yi's comments are consistent with our view of stable rates for some time.

- That said, the PBoC is continuing to unwind emergency stimulus introduced last year. It has signalled its intention to be more targeted in its measures going forward – aiming to support those sectors most negatively impacted by the pandemic.

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