CHINA'S ECONOMY AT A GLANCE

DECEMBER 2021

National Australia Bank

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KEY POINTS

November data show little underlying improvement from October's weakness

- Following on from weakness in October, there was little sign of improvement in underlying economic conditions in November – despite reports that electricity shortages have eased. Overall, growth in industrial production was only marginally stronger, investment trends remained extremely weak and retail sales data point to minimal consumption growth. Reflecting this, we have trimmed our economic growth forecast for 2021 to 8.0% (from 8.3% previously), while our forecast for 2022 is unchanged at 6.0% (albeit we expect marginally weaker conditions at the start of the year to be offset by stronger growth at the end).

- China's industrial production grew slightly more strongly in November – up by 3.8% yoy – from 3.5% yoy in October. By historical standards, this was a weak rate of growth, suggesting limited gains from the reported easing of electricity shortages. With weakening trends in the construction sector over recent months, heavy industry tied to construction declined – with output of cement and crude steel falling by 18.6% yoy and 22% yoy respectively.

- Although growth in producer prices was marginally softer in November (off multi-decade highs in October) – with these price pressures flowing through into the cost of investment goods. In real terms, we estimate that fixed asset investment fell by 11.7% yoy (from 12.5% yoy previously).

- China's trade surplus narrowed slightly in November – down from an all time high of US$84.5 billion in October to US$71.7 billion. While the value of both imports and exports rose month-on-month, imports rose more rapidly, pushing down the surplus. Prices continue to impact import and export values – reflecting a range of factors – including strong growth in commodity prices, ongoing disruptions related to COVID-19, shortages of key inputs and constraints in global shipping.

- Real retail sales increased by just 0.5% yoy (down from 1.9% yoy in October) – the weakest outcome since August 2020, and far below pre-COVID-19 levels.

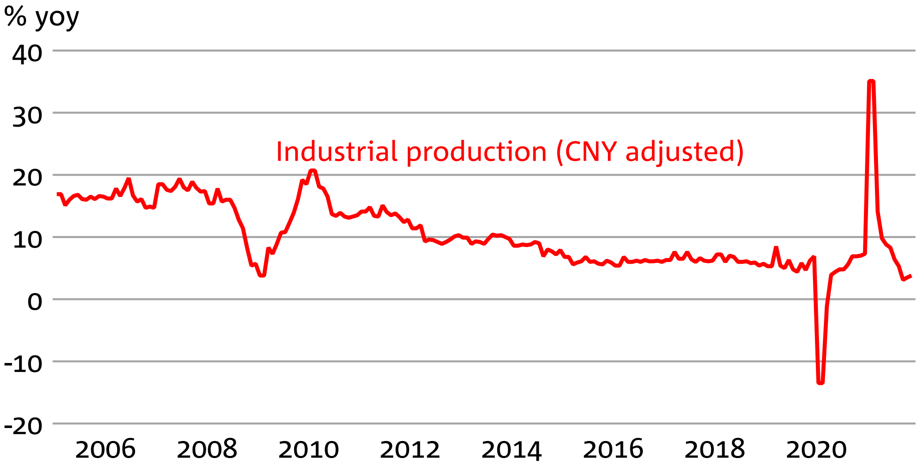
- In early December, the PBoC announced another 50 basis point cut to the Reserve Requirement Ratio – the second change in 2021. This will free up around RMB 1.2 trillion for banks to expand lending – albeit an unspecified amount will be used to repay maturing medium term lending facility loans from the central bank. The PBoC has provided guidance that it is seeking to boost lending to smaller firms.

- The PBoC has held the Loan Prime Rate (its main policy rate) stable at 3.85% since April 2020. Although Chinese authorities may seek some additional stimulus to stabilise the economy in 2022, the increasing likelihood of rate rises in advanced economies (most notably the United States) may constrain the PBoC's capacity to cut policy rates – particularly given the risk of capital outflow. This may mean a greater role for fiscal stimulus next year.

INDUSTRIAL PRODUCTION

INDUSTRIAL PRODUCTION

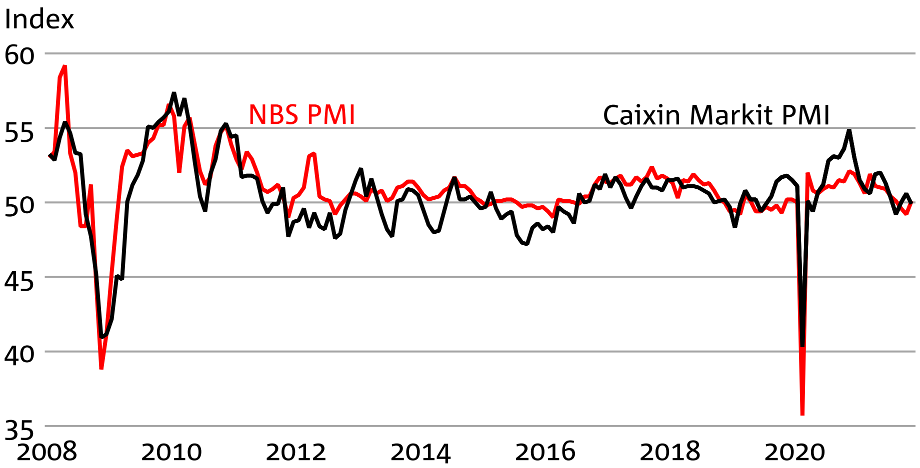
Marginal acceleration in growth as electricity shortages eased



Source: Macrobond, NAB Economics

MANUFACTURING PMIS CONVERGED IN NOVEMBER

Both surveys near neutral levels



Source: Macrobond, NAB Economics

- China's industrial production grew slightly more strongly in November – up by 3.8% yoy – from 3.5% yoy in October. By historical standards, this was a weak rate of growth, suggesting limited gains from the reported easing of electricity shortages.
- Output trends remained highly mixed in November. With weakening trends in the construction sector over recent months, heavy industry tied to construction declined – with output of cement and crude steel falling by 18.6% yoy and 22% yoy respectively.
- Motor vehicle production has been weak across much of 2021 – in part related to semi-conductor shortages – with output down by 7.1% yoy in November. In contrast, output within the electronics sector rose by 13.5% yoy.
- Recent months have seen diverging trends in China's two major manufacturing surveys – as different parts of industry experienced differing trends – with traditional heavy industry particularly impacted by slowing construction activity and shortages of electricity, of which the latter appears resolved for now (at least until demand rises further with anticipated cold weather).
- The official NBS PMI survey was surprisingly stronger in November – up to a relatively neutral 50.1 points, from 49.2 points in October – well above market expectations. It is generally understood that this survey typically has a larger share of heavy industry, and the increased electricity availability in November (compared with recent months) may explain this rebound.
- In contrast, the private sector Caixin Markit PMI weakened – having been comparatively stronger over the past two months – down to 49.9 points (from 50.6 points previously).
- Despite the overall neutral outcomes in both surveys, demand conditions appear somewhat negative – with new orders measures below 50 points in both surveys in November.

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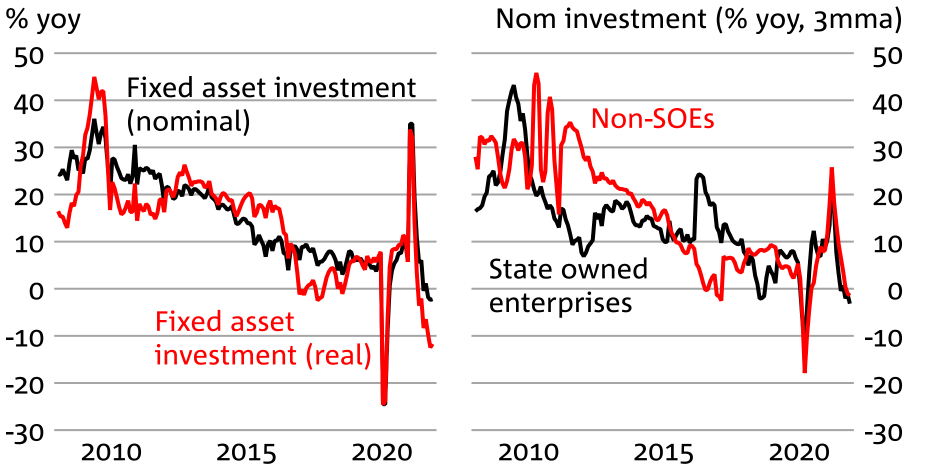
INVESTMENT

FIXED ASSET INVESTMENT

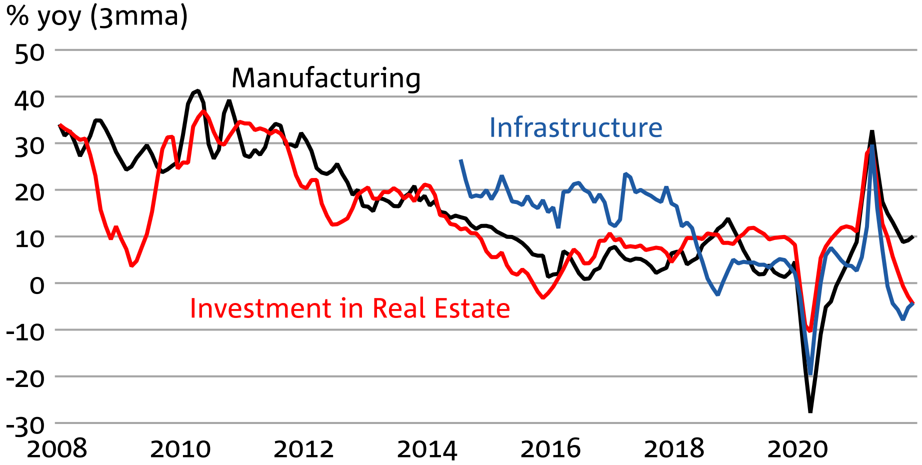
Weaker SOE investment leads the overall declines in November



Source: Macrobond, NAB Economics

FIXED ASSET INVESTMENT BY INDUSTRY

Real estate investment continued to contract



Source: Macrobond, NAB Economics

- Nominal fixed asset investment contracted in November – the third straight monthly decline – down by 2.2% yoy (compared with a 2.4% yoy fall previously). Growth in producer prices was marginally softer in November (off multi-decade highs in October) – with these price pressures flowing through into the cost of investment goods. In real terms, we estimate that investment fell by 11.7% yoy (from 12.5% yoy previously).

- Nominal investment by state-owned enterprises (SOEs) contracted more sharply than private sector firms in November. SOE investment fell by 6.1% yoy, compared with a 0.1% yoy increase in investment by private firms.

- Investment trends remain divergent across different industry categories. Manufacturing investment has remained comparatively strong – increasing by around 10.0% yoy (on a three month moving average basis) in November. In contrast, infrastructure investment has continued to contract – down by 4.3% yoy (3mma). Local governments are responsible for the bulk of infrastructure funding, and total government bond issuance has contracted in 2021.

- Investment in real estate – previously a key driver of China's economic activity – has continued to contract, down by 4.5% yoy (3mma). Major property developer Evergrande had managed to avoid a technical default for several months, but finally succumbed in early December. The fallout of the restructuring process could further disrupt the sector in coming months – which would negatively impact demand for steel, and by extension, demand for Australian iron ore.

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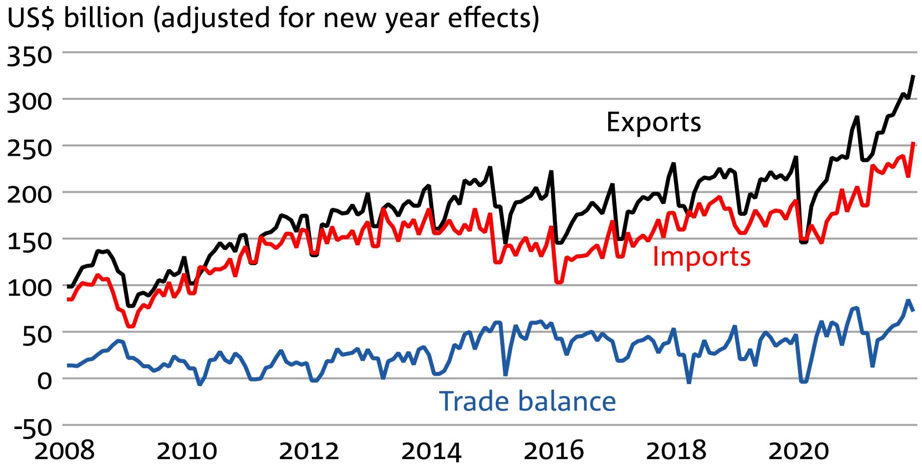
INTERNATIONAL TRADE – TRADE BALANCE AND IMPORTS

CHINA'S TRADE BALANCE

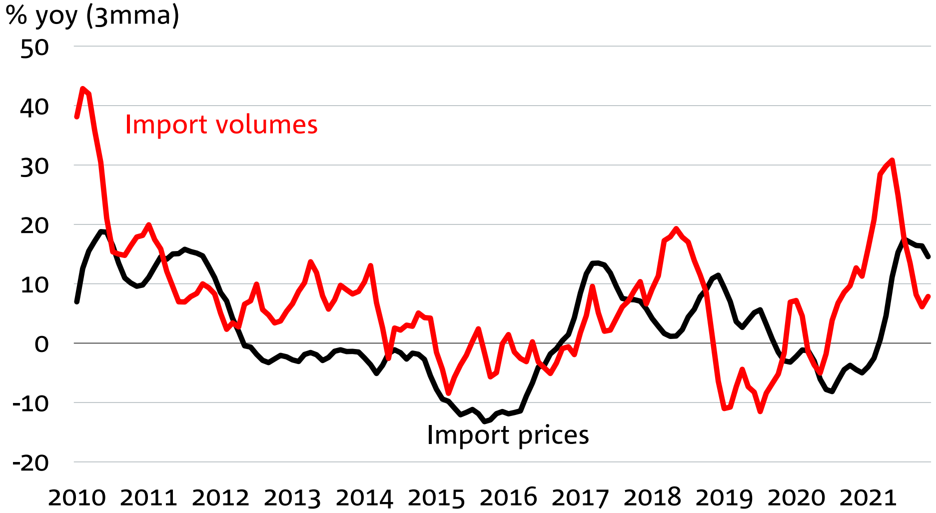
Surplus slightly narrower on strong import growth



Source: Macrobond, NAB Economics

IMPORT VOLUMES AND VALUES

Strong price growth a key contributor to rising import values



Source: CEIC, Macrobond, NAB Economics

- China's trade surplus narrowed slightly in November – down from an all time high of US$84.5 billion in October to US$71.7 billion. While the value of both imports and exports rose month-on-month, imports rose more rapidly, pushing down the surplus.

- The value of China's imports rose to US$253.8 billion in November, up from US$215.7 billion in October. In year-on-year terms, this represented an increase of 31.7%.

- Increasing import prices have contributed significantly to this trend. This reflects a range of factors – including strong growth in commodity prices (despite peaking in July and subsequently declining), ongoing disruptions related to COVID-19, shortages of key inputs (most notably semi-conductors) and constraints in global shipping.

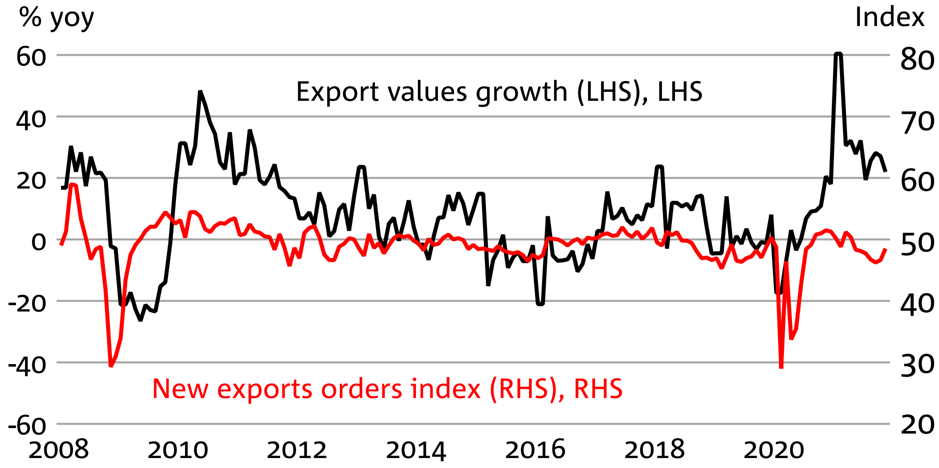
- The RBA Index of Commodity Prices rose by 34.5% yoy in November, down from 42.6% yoy in October. Our estimate of China's import volumes uses this price index as a proxy for import prices, and this suggests that there was a steep increase in import volumes in November – following weak growth in September and October. On a three month moving average basis, China's import volumes rose by 7.8% yoy in November, from 6.1% yoy previously. That said, it is worth noting that our proxy underestimated import prices in recent months – meaning that the growth in volumes may be overstated.

- Import trends for key commodities remain highly mixed. There was strong growth in imports of LPG and other gases (up by 16.9% yoy) and coal (up by over 200% yoy – in part reflecting base effects due to historically weak import volumes in November 2020) as Chinese authorities sought to address earlier electricity shortages, while refined petroleum products increased by 26.5% yoy. In contrast, imports of crude oil fell 7.9% yoy and refined copper decreased by 9.1% yoy, while iron ore imports rose by 6.9% yoy (following two months of double digit falls).

INTERNATIONAL TRADE – EXPORTS

EXPORT VALUE AND NEW EXPORT ORDERS

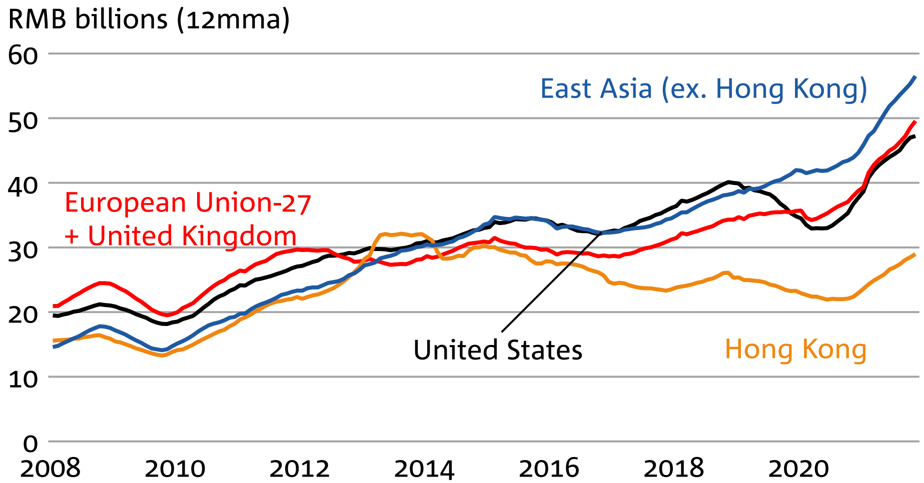
Strong export growth remains at odds with new export orders



Source: Macrobond, NAB Economics

EXPORTS TO MAJOR TRADING PARTNERS

Strong growth in exports to Europe and East Asia in November



Source: Macrobond, NAB Economics

- The value of China's exports rose considerably month-on-month in November – up to US$325.5 billion (from US$300.2 billion in October) – a new record high. In year-on-year terms, export values rose by 22.0%.
- There remains a notable disconnect between the relative strength in China's exports and survey measures of new export orders. This measure in the NBS manufacturing PMI survey remained negative in November – at 48.5 points – albeit this measure has improved since its recent low in September.
- In a similar trend to that seen in imports, export prices have also increased relatively strongly in recent months – contributing to the overall growth in export values. In October, export prices rose by around 8.1% yoy (down from 10.6% yoy in September – well below the increase in producer prices.
- There were highly divergent trends in exports to major trading partners in November. Exports to the European Union-27 + the United Kingdom rose by 28.2% yoy, while exports to East Asia rose by 24.0% yoy. Excluding Hong Kong, this increase was driven by increased shipments to South Korea, Malaysia, Indonesia and Thailand.
- In stark contrast, exports to the United States rose by just 5.2% yoy. The comparatively modest increase in exports to the United States meant that China's twelve month rolling surplus with the US declined slightly in November – down to US$387.8 billion (from a record US$388.3 billion in the twelve months to October).

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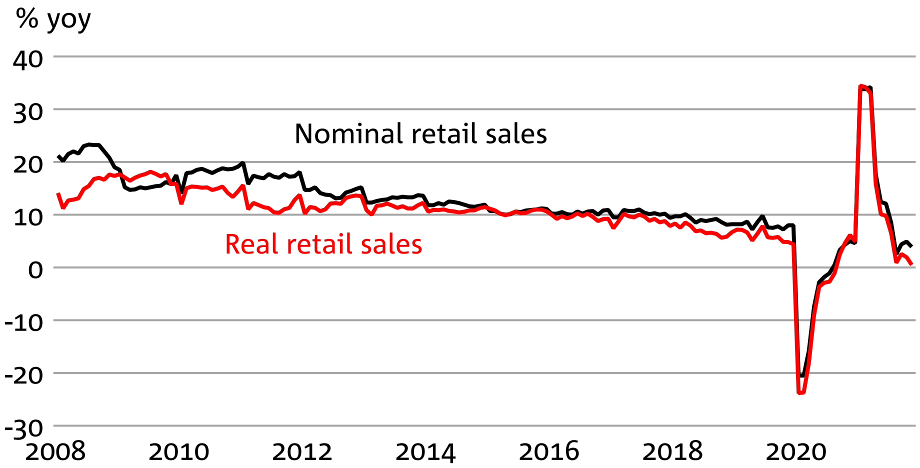
RETAIL SALES AND INFLATION

RETAIL SALES GROWTH

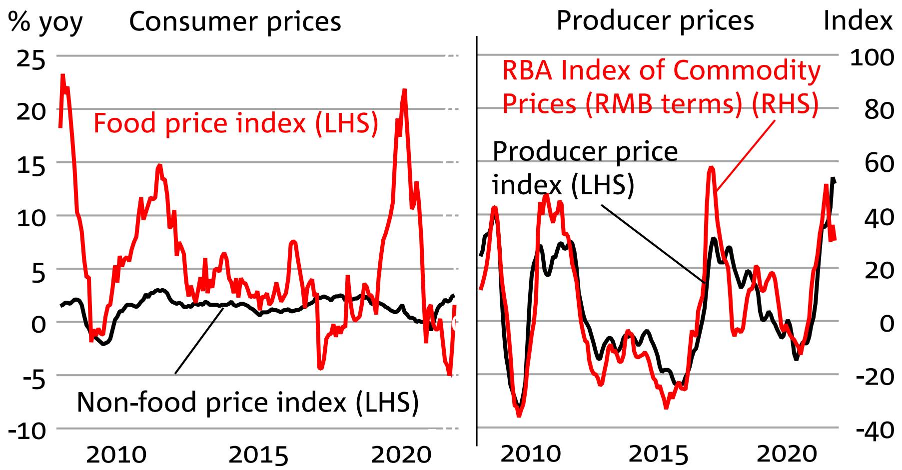
Real growth fell to its weakest rate since August 2020



Source: Macrobond, NAB Economics

CONSUMER AND PRODUCER PRICES

CPI accelerating; producer price growth off 16 year high



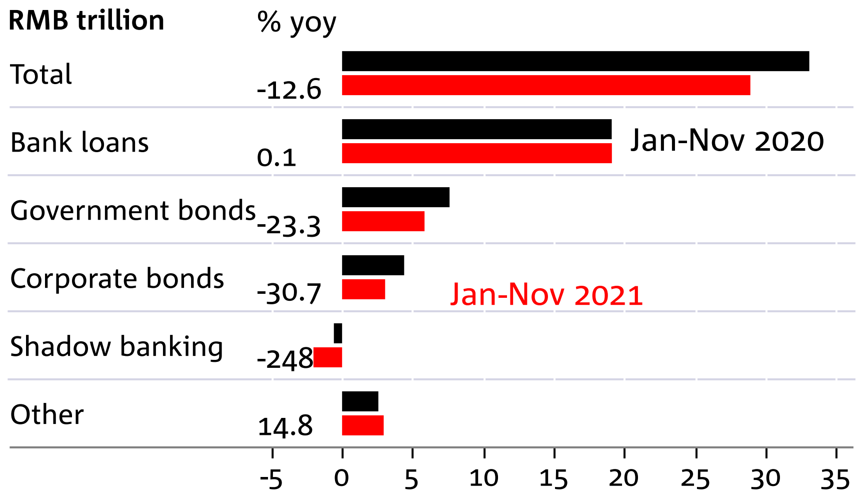
Source: Macrobond, NAB Economics

- In nominal terms, China's retail sales growth slowed in November – down to 3.9% yoy (from 4.9% yoy previously). In addition, there was another uptick in retail price inflation, meaning that in real terms, retail sales increased by just 0.5% yoy (down from 1.9% yoy in October) – the weakest outcome since August 2020, and far below pre-COVID-19 levels.
- China's consumer prices rose by 2.3% yoy in November (up from 1.5% yoy previously) – the strongest rate of increase since August 2020, as food price growth rebounded.
- The food price index increased by 1.6% yoy (compared with a 2.4% yoy decrease in October). Falling pork prices have been a major influence on overall consumer prices in recent times – with prices down by 32.7% yoy in November (compared with a 44.0% yoy fall in October). In contrast, fresh vegetable prices rose by 30.6% yoy – reflecting the impact of flooding and other recent extreme weather events on supply.
- Non-food prices accelerated slightly in November – increasing by 2.5% yoy (up from 2.4% yoy in October). Vehicle fuel prices have been a major influence on non-food prices in recent months – increasing by 35.7% yoy in November.
- Growth in producer prices dipped slightly in November – down to 12.9% yoy, from 13.5% yoy in October (which had been the largest increase since mid-1995). Recent months have seen producers impacted by a broad range of factors – including electricity shortages, COVID-19 outbreaks and countermeasures as well as surging commodity prices. The RBA Index of Commodity Prices – converted into RMB terms – rose by 30.2% yoy in November, down from around 36.1% yoy in October and in excess of 50% in July.

CREDIT CONDITIONS

NEW CREDIT ISSUANCE

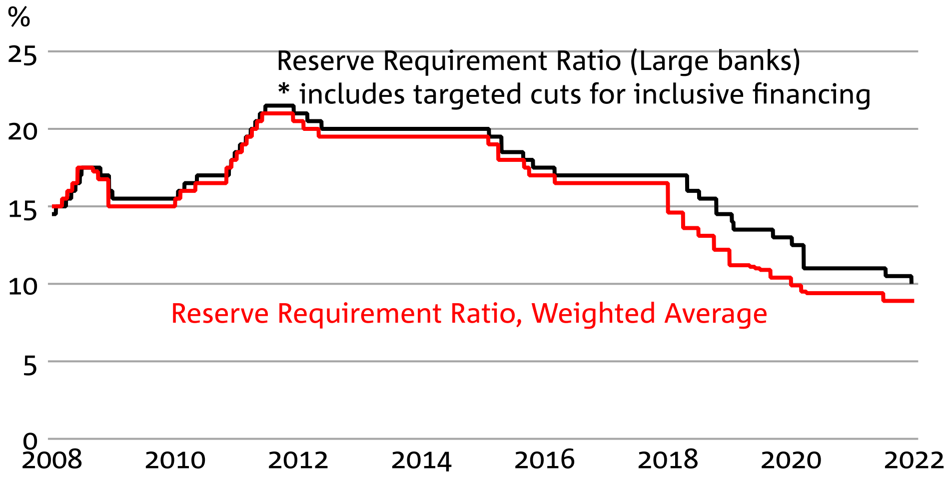
Weaker lending from bonds and shadow banking



Source: Macrobond, NAB Economics

RESERVE REQUIREMENT RATIO

Further cut in mid-December to boost liquidity



Source: Macrobond, NAB Economics

- There was a rebound in China's new credit issuance in November – totalling RMB 2.6 trillion, up from RMB 1.6 trillion previously. In part this reflected seasonal trends, with the start of October impacted by the Golden Week holiday period. However, total issuance expanded by 22.2% yoy – the largest increase recorded in 2021 (when smoothing the January-February period to account for Chinese new year).

- In the first eleven months of 2021, new credit issuance totalled RMB 29.0 trillion – a decrease of 12.6% yoy. Over this period, bank lending was virtually unchanged – rising by less than 0.1% yoy to RMB 19.1 trillion.

- More starkly, non-bank lending plummeted during the first eleven months of the year – down by 29.9% yoy to RMB 9.8 trillion. Over this period, the total value of government and corporate bond issuance declined by 23.3% and 30.7% respectively, while there was also a contraction in the stock of shadow banking lending tracked by the People's Bank of China (PBoC).

- In early December, the PBoC announced another 50 basis point cut to the Reserve Requirement Ratio – the second change in 2021. This will free up around RMB 1.2 trillion for banks to expand lending – albeit an unspecified amount will be used to repay maturing medium term lending facility loans from the central bank. The PBoC has provided guidance that it is seeking to boost lending to smaller firms.

- The PBoC has held the Loan Prime Rate (its main policy rate) stable at 3.85% since April 2020. Although Chinese authorities may seek some additional stimulus to stabilise the economy in 2022, the increasing likelihood of rate rises in advanced economies (most notably the United States) may constrain the PBoC's capacity to cut policy rates – particularly given the risk of capital outflow. This may mean a greater role for fiscal stimulus next year.

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