CHINA'S ECONOMY AT A GLANCE

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CONTACT

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KEY POINTS

COVID-19 uncertainty continues to cloud China's economic outlook

- Overall, while China's partial economic data for May was somewhat improved when compared with April, they continue to point to the impact of COVID-19 restrictions that constrained activity, particularly on the demand side of the economy. While measures in many major centres (most notably Shanghai and Beijing) were eased substantially at the start of June, there are concerns at the time of writing that some restrictions may be re-imposed following another increase in COVID-19 case numbers. This serves to highlight the ongoing uncertainty around China's economic outlook, given the continuation of zero-COVID public health policies. For now our forecasts remain unchanged, with China's economy to grow by 4.2% in 2022, 5.6% in 2023 and 4.9% in 2024, however we continue to note downside risks related to any further COVID-19 outbreaks.

- China's industrial production grew marginally in May – up by 0.7% yoy – compared with the 2.9% yoy fall recorded in April, while real fixed asset investment growth returned to zero, compared with a 3.5% yoy contraction previously.

- China's trade surplus climbed significantly in May, increasing to US$78.8 billion (from US$51.1 billion in April) – the fourth highest monthly total on record. While the value of imports remained relatively stable in May, there was a sharp increase in export values.

- China's retail sales remained weak in May, with consumer demand continuing to be impacted by various COVID-19 lockdowns and the uncertainty related to China's public health policies. Real retail sales contracted by 9.7% yoy (compared with a 14.0% fall in April).

- In the first five months of 2022, new credit issuance increased by 11.8% yoy to RMB 15.8 trillion. Although bank lending accounts for the largest share of new issuance, it contracted by 1.8% yoy over this period. In contrast, non-bank lending rose by almost 56% yoy over the first five months, with government bond issuance the key driver.

- There is already limited scope for the People's Bank of China to cut its benchmark policy rate, and further tightening in policy by advanced economies will add additional pressure. Since the start of April, the yield on 10 year US Treasuries has exceeded 10 year Chinese government bonds, and the gap has continued to widen. Monetary policy imbalance between China and other major central banks risks capital outflows that could destabilise China's financial sector as well as placing further pressure on the exchange rate.

INDUSTRIAL PRODUCTION

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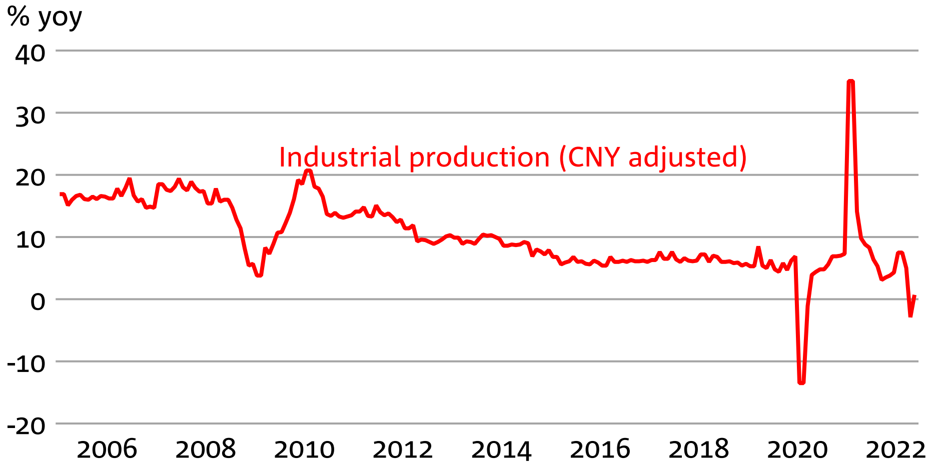
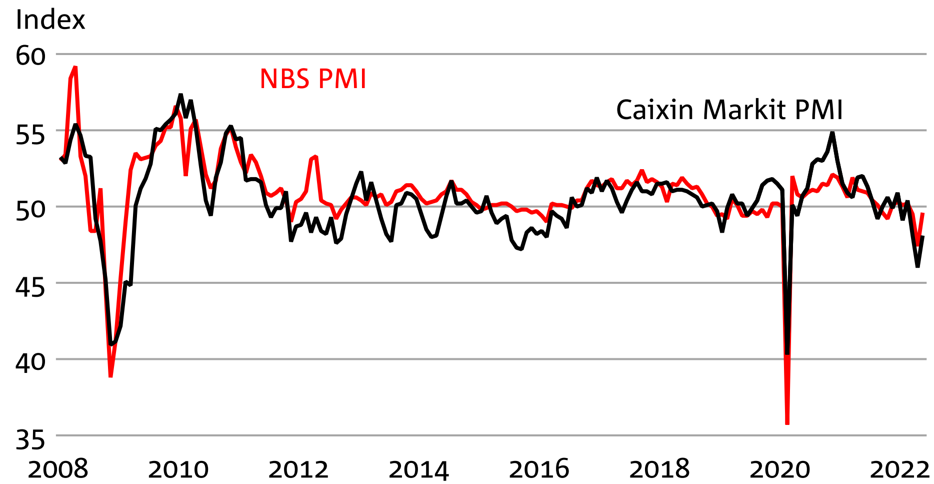
Modest recovery in IP with COVID-19 restrictions still impacting



Source: Macrobond, NAB Economics

MANUFACTURING PMIS STRONGER IN MAY

But both surveys remained in negative territory



Source: Macrobond, NAB Economics

- China's industrial production grew marginally in May – up by 0.7% yoy – compared with the 2.9% yoy fall recorded in April. Reports suggest that there was some easing in COVID-19 restrictions in various parts of the country, however measures remained in place in both Shanghai and Beijing (to differing degrees) until the start of June – which likely continued to constrain manufacturing activity.

- Output in a number of major industrial sectors remained weak in May. Construction related heavy industry continued to decline, with production of cement and crude steel falling by 17.0% yoy and 3.5% yoy respectively. Similarly, motor vehicle manufacturing also declined, down by 4.8% yoy in May (albeit this followed a 44% yoy fall in April, meaning there was a sizeable pickup month-on-month). In contrast, production of electronics rose by 7.3% yoy.

- Having plunged in April, both of China's major manufacturing surveys improved in May – albeit remaining in negative territory, with activity continuing to be impacted by various public health measures to control COVID-19 outbreaks.

- The official NBS PMI rose to 49.6 points in May (from 47.4 points previously). In contrast, the private sector Caixin Markit PMI moved up to 48.1 points (compared with 46.0 points in April). It is likely that the relaxation of restrictions in Shanghai and Beijing at the start of June will support stronger readings for the month – albeit there are concerns at the time of writing that fresh outbreaks in both cities could see restrictions reimposed.

- Both surveys pointed to less negative outcomes for production and overall new orders, however new export orders remained comparatively weaker. Similarly, the disruptions coming from COVID-19 restrictions was evident in supplier delivery times remaining very weak – with respondents in the Caixin survey noting substantial issues in transport and logistics.

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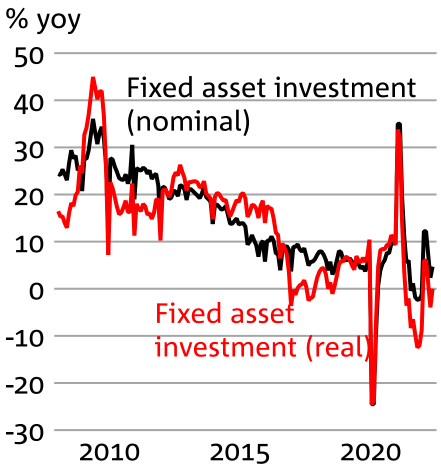
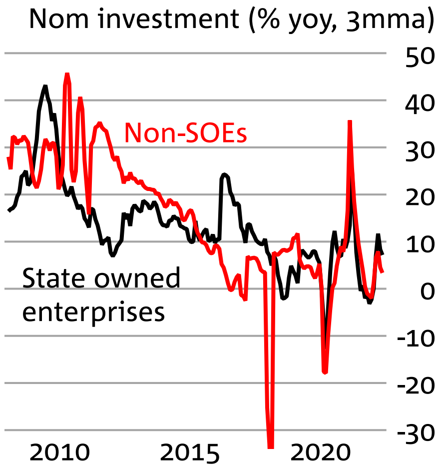
INVESTMENT

FIXED ASSET INVESTMENT

Real investment growth back to zero following April's fall

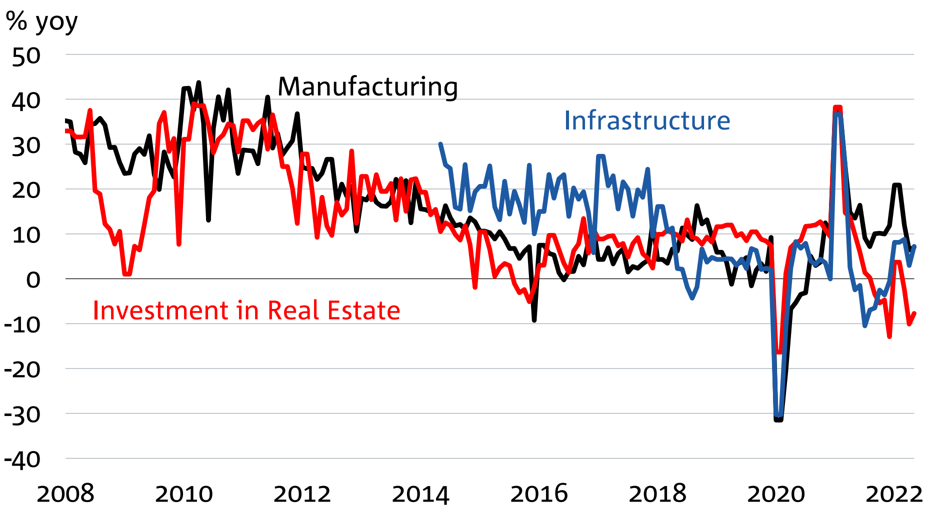




Source: Macrobond, NAB Economics

FIXED ASSET INVESTMENT BY INDUSTRY

Real estate investment continues to contract



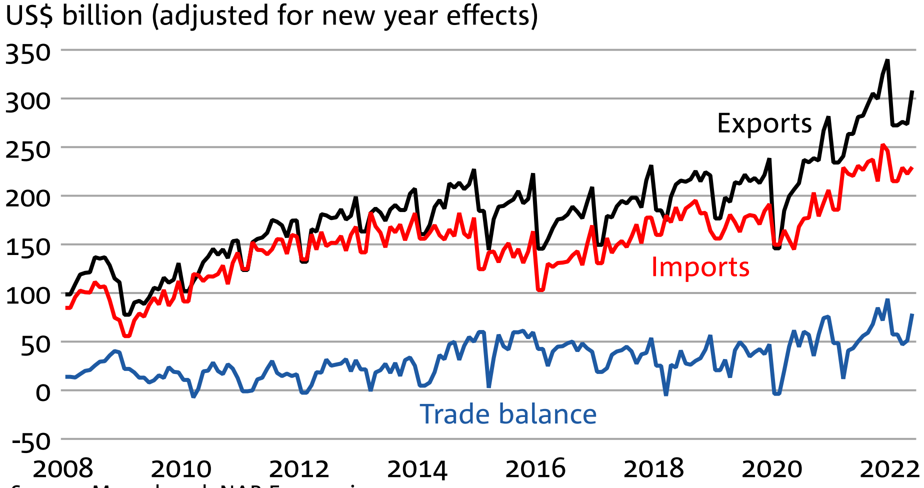
Source: Macrobond, NAB Economics

- There was a modest uptick in nominal fixed asset investment in May – increasing by 4.7% yoy (up from 2.3% yoy in April). Reflecting an easing in producer prices – which flows through into the cost of investment goods – our estimate of real investment growth returned to zero, compared with a 3.5% yoy contraction previously.
- Since the start of 2022, nominal investment by state-owned enterprises (SOEs) has outpaced that of private sector firms. SOE investment rose by 6.9% yoy in May (up from 4.6% yoy previously), while investment by private firms rose by 3.6% yoy (from 1.0% yoy in April).
- There remains some notable divergence in investment trends by major sector. There was a slight pickup in manufacturing investment in May – up by 7.1% yoy (from 6.4% yoy in April), while infrastructure investment accelerated more rapidly – up by 7.2% yoy (from 3.0% yoy previously).
- In contrast, nominal real estate investment contracted by 7.7% yoy in May (albeit this was compared with a 10.1% yoy fall in April). Despite commentary in recent months from Chinese authorities around stabilising the real estate sector, residential property sales and new construction starts continue to contract sharply – down by 37% yoy and 41% yoy respectively (as measured in square metres).

INTERNATIONAL TRADE – TRADE BALANCE AND IMPORTS

CHINA'S TRADE BALANCE

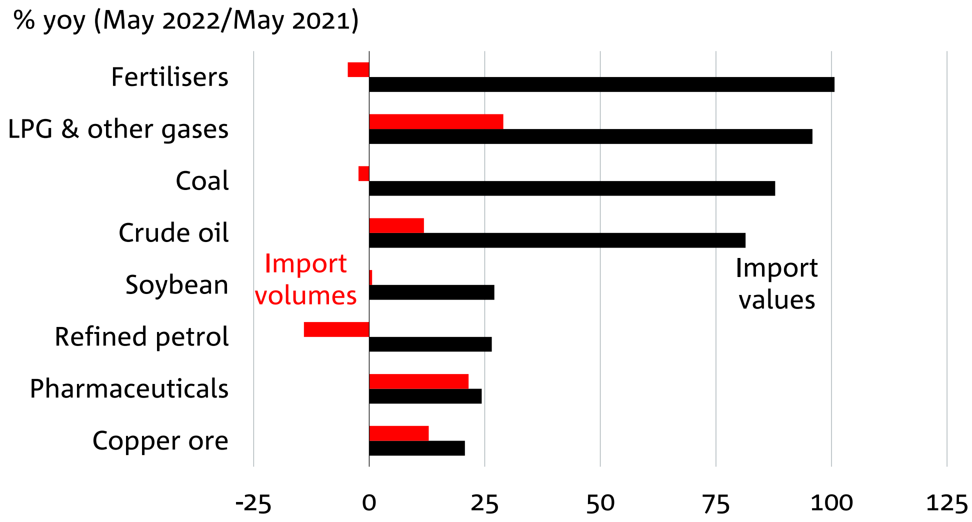
Exports increased markedly to increase China's trade surplus



Source: Macrobond, NAB Economics

IMPORT VALUES AND VOLUMES

Energy prices have had a major impact on import values



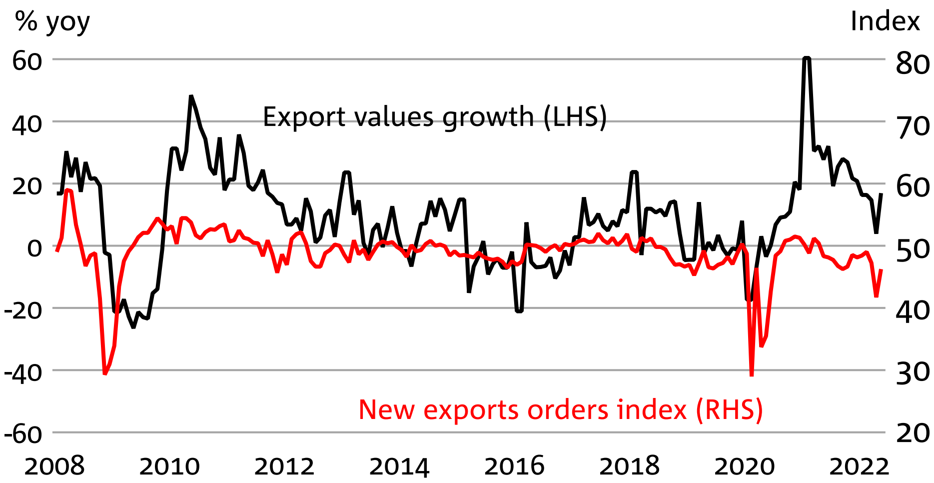
Source: Datastream, NAB Economics

- China's trade surplus climbed significantly in May, increasing to US$78.8 billion (from US$51.1 billion in April) – the fourth highest monthly total on record. While the value of imports remained relatively stable in May, there was a sharp increase in export values.
- China's imports totalled US$229.5 billion in May (up from US$222.5 billion in April, but little changed from March). In year-on-year terms, this represented an increase of 4.1% yoy.
- Prices have been the key driver of growth in imports in recent times – with price growth exceeding volume growth from the second half of 2021 onwards. China's trade data showed that import volumes fell by 16.3% yoy in April (following on from a 13.1% yoy fall in March), with COVID-19 disruptions explaining some of the decline. Our estimate of volumes for May – which uses global commodity prices as a proxy for import prices – suggests a more modest year-on-year decline (around 4%) but a sizeable increase month-on-month from April.
- These price effects are particularly evident when we break down imports by major products. The increase in energy prices (when compared with May 2021) is clear with the surge in import values for fertilisers (which are commonly produced from natural gas), LPG & other gases, coal and crude oil, while the volumes of these products have increased more modestly (or, in the case of fertilisers and coal, contracted year-on-year).

INTERNATIONAL TRADE – EXPORTS

EXPORT VALUE AND NEW EXPORT ORDERS

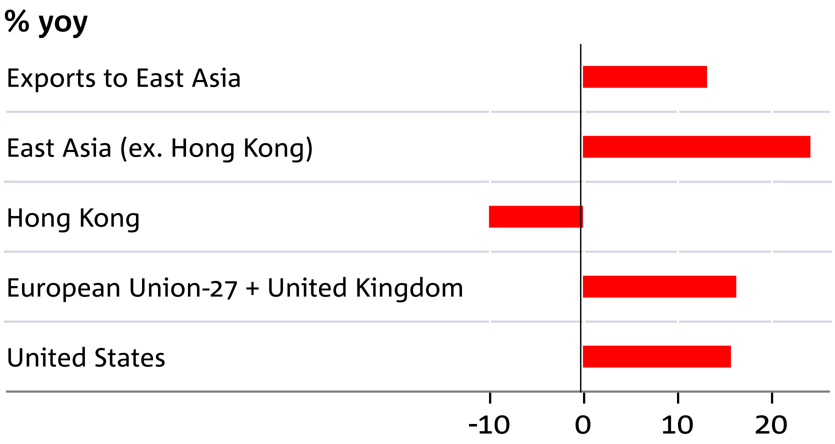
Export growth picked up in May, following April's weakness



Source: Macrobond, NAB Economics

EXPORTS TO MAJOR TRADING PARTNERS

Major markets recorded broadly similar growth in May



Source: Macrobond, NAB Economics

- China's exports surged in May, rising to US$308.2 billion (from US$273.6 billion in April). There was a notable pickup in year-on-year growth – up by 16.9% yoy (compared with 3.9% yoy in April). Some of this increase may have reflected some easing in the COVID-19 restrictions. Reports suggest that the transport and logistics sector was more heavily impacted than manufacturing, resulting in an increase in inventories in April waiting for export.

- This suggests that the rebound in exports is unlikely to be sustained going forward. The new export orders measure in the NBS PMI survey was less negative than in April – moving up to 46.2 points (from 41.6 points previously) – but still points to potentially weaker export growth in coming months.

- At a high level, there was relatively similar growth in exports to major trading partners in May. Exports to the European Union-27 + the United Kingdom rose by 16.3% yoy while exports to the United States increased by 15.7% yoy. Exports to East Asia rose slightly more modestly – up by 13.2% yoy, however this included a steep fall in exports to Hong Kong.

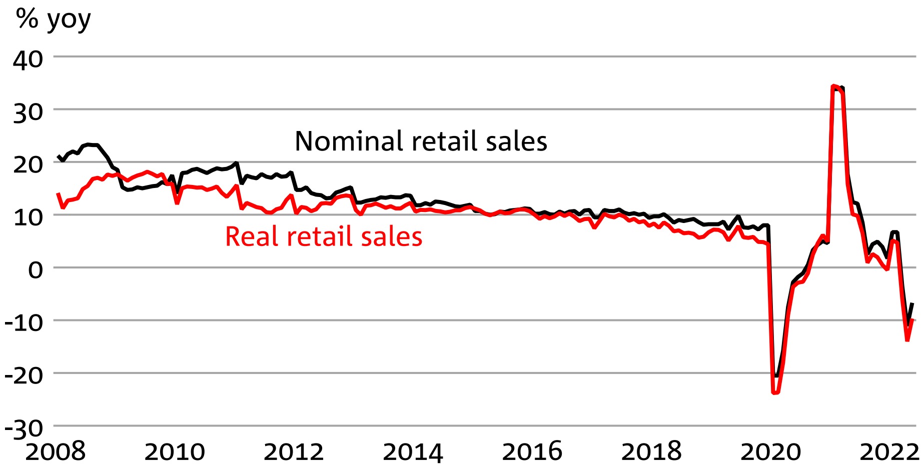
- Exports to Hong Kong fell by 10% yoy in May. We have frequently noted distortions in trade data reported by Hong Kong and China Customs – which in part reflects capital flows disguised as trade activity. There was a wide gap between these two measures in both April and May 2020, suggesting that the sizeable fall in China's exports to Hong Kong may not be entirely accurate.

- Excluding Hong Kong, exports to East Asia rose by 24.2% yoy, with strong increases in exports to South Korea, Vietnam, Singapore and Malaysia.

RETAIL SALES AND INFLATION

RETAIL SALES GROWTH

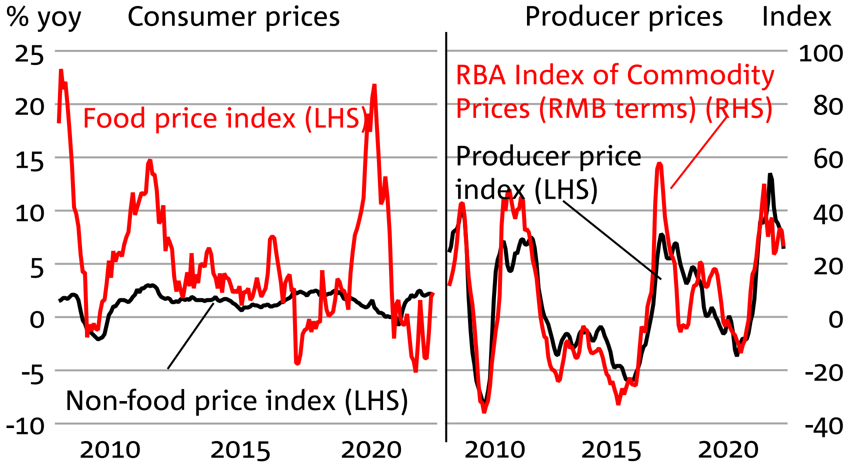
COVID-19 measures continue to impact consumer demand



Source: Macrobond, NAB Economics

CONSUMER AND PRODUCER PRICES

CPI growth remains modest by international standards



Source: Macrobond, NAB Economics

- China's retail sales remained weak in May, with consumer demand continuing to be impacted by various COVID-19 lockdowns and the uncertainty related to China's public health policies. Nominal retail sales fell by 6.7% yoy (compared with an 11.1% yoy fall in April and a 3.5% fall in March).
- Retail price inflation was marginally softer in May. This meant that real retail sales contracted by 9.7% yoy (compared with a 14.0% fall in April).
- Growth in China's consumer prices remained stable in May – increasing by 2.1% yoy. When compared with inflation trends globally, China's growth in prices has been quite modest, albeit this may in part reflect weakness on the demand side of the economy.
- Food prices increased by 2.3% yoy in May (up from 1.9% yoy in April and 1.5% yoy in March). The downward pressure on aggregate food prices from falling pork prices is starting to erode – reflecting the recovery in domestic supply following the African Swine Fever outbreak that started in 2018. Pork prices fell by 21.1% yoy in May (compared with 33.3% yoy in April) and these falls will continue to decrease in coming months.
- In contrast, non-food price growth was marginally weaker in May – increasing by 2.1% yoy (compared with 2.2% yoy in both March and April). Vehicle fuel prices remain a key driver on non-food price growth – increasing by 27.1% yoy in May (down from 28.4% yoy previously).
- Producer prices rose by 6.4% yoy in May (down from 8.0% yoy in April) – the lowest rate of increase since March 2021. Commodity prices have continued to rise, albeit at a marginally slower rate – with the RBA Index of Commodity Prices rising by 26.5% yoy (in RMB terms), down from 32.4% yoy in April.

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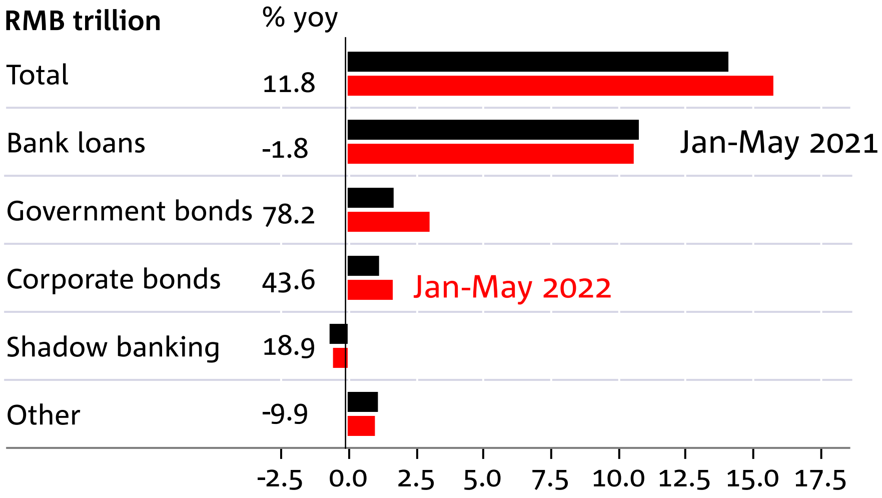
CREDIT CONDITIONS

NEW CREDIT ISSUANCE

Government bonds driving credit growth in 2022



Source: Macrobond, NAB Economics

GOVERNMENT BOND YIELDS

US returns have far exceeded China's since early April

Source: Macrobond, NAB Economics

- There was a sizeable rebound in new credit issuance in May – following the lockdown related weakness of April. Total issuance was RMB 2.8 trillion, led by a surge in bank loans and strong government bond issuance. In contrast, net corporate bond issuance contracted slightly in the month.
- In the first five months of 2022, new credit issuance increased by 11.8% yoy to RMB 15.8 trillion. Although bank lending accounts for the largest share of new issuance, it contracted by 1.8% yoy over this period, to total RMB 10.6 trillion. This decrease occurred entirely in April, with some observers attributing the drop to COVID-19 restrictions.
- Non-bank lending rose by almost 56% yoy over the first five months of 2022. The key driver of this increase has been government bond issuance, which increased by over 78% yoy over this period. Corporate bond issuance also rose strongly, up by almost 44% yoy, while shadow banking components continued to contract.
- The People's Bank of China (PBoC) cut the interest rate on the five year Loan Prime Rate in May by 15 basis points to 4.45%, while leaving the benchmark one year rate unchanged. The former is more related to property lending – with the PBoC seeking to stabilise this sector after steep declines in the year to date. The one year rate is more closely tied to business lending.
- There is already limited scope for the PBoC to cut its benchmark policy rate, and further tightening in policy by advanced economies will add additional pressure. Since the start of April, the yield on 10 year US Treasuries has exceeded 10 year Chinese government bonds, and the gap has continued to widen. Monetary policy imbalance between China and other major central banks risks capital outflows that could destabilise China's financial sector as well as placing further pressure on the exchange rate.

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