NAB Group Economics

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China's economy at a glance

October 2022

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Key points

Growth rebounded in Q3, but base effects flattered the results

- China's latest national accounts data show its economy expanded by 3.9% yoy in Q3. By historical standards, this rate of growth is not particularly strong (particularly when compared with pre-pandemic rates) and this increase is somewhat inflated by base effects – given that Q3 2021 was negatively impacted by the Delta wave of COVID-19 and electricity shortages hitting a number of provinces.

- We have not fundamentally changed our views around China's economy this month. The slightly stronger than expected growth in Q3 bumps up our forecast for 2022 to 3.4% (from 3.3% previously). Our forecasts for 2023 and 2024 are unchanged at 5.0% and 4.5% respectively, and weaker demand from advanced economies will require growth to be driven by the domestic economy.

- China's industrial production growth accelerated in September – increasing by 6.3% yoy (from 4.2% yoy previously). The strength of this increase may be somewhat overstated – given that China's industrial sector was negatively impacted by energy shortages in September 2021.

- Growth in China's fixed asset investment edged higher in September – our estimates suggest that real investment rose by 4.6% yoy (from 3.1% yoy in August). State-owned enterprises recorded stronger growth than private firms, with manufacturing and infrastructure investment expanding rapidly, while real estate continued to contract.

- Real retail sales growth fell back into negative territory – contracting by 0.7% yoy (compared with a 2.2% yoy increase previously). The increase in real sales in August was in part related to the Delta wave of COVID-19 that led to weaker conditions in August 2021.

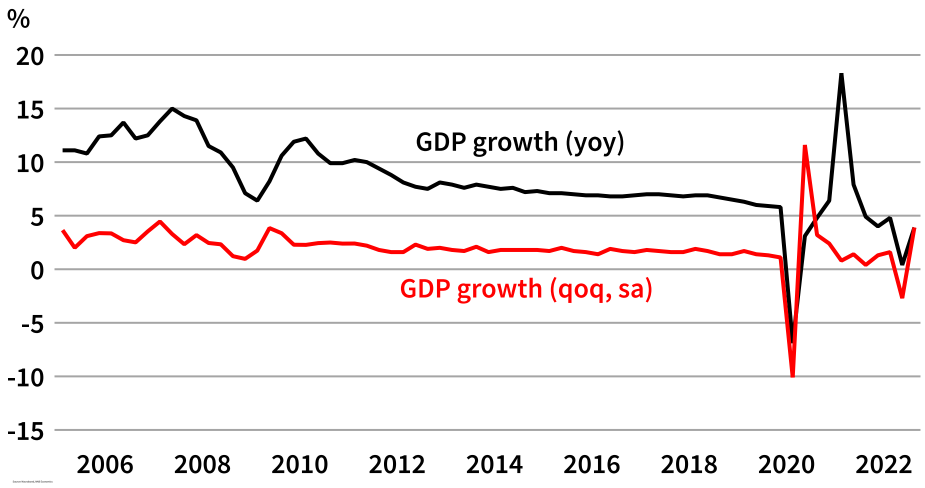
- In the first nine months of 2022, new credit issuance increased by 11.9% yoy to RMB 27.7 trillion. Bank loans continue to account for the largest share of total credit issuance and loans grew by 3.4% yoy. Non-bank lending rose by 30.5% yoy in the first nine months. The key driver over this period was government bond issuance – up by 33.8% yoy – however this rate of increase has slowed in recent months. In addition, shadow bank lending decreased by a smaller amount in this period.

- The PBoC maintained its Medium Term Lending Facility (MTF) rate unchanged in September. As we have noted in recent months, the effectiveness of monetary easing is questionable at present – with low interbank interest rates implying excess liquidity. Banks have a lot of funds available for lending, but there is little demand from the private sector – in part connected to the deterioration in the property sector, but also the weakness in household activity.

Gross domestic product

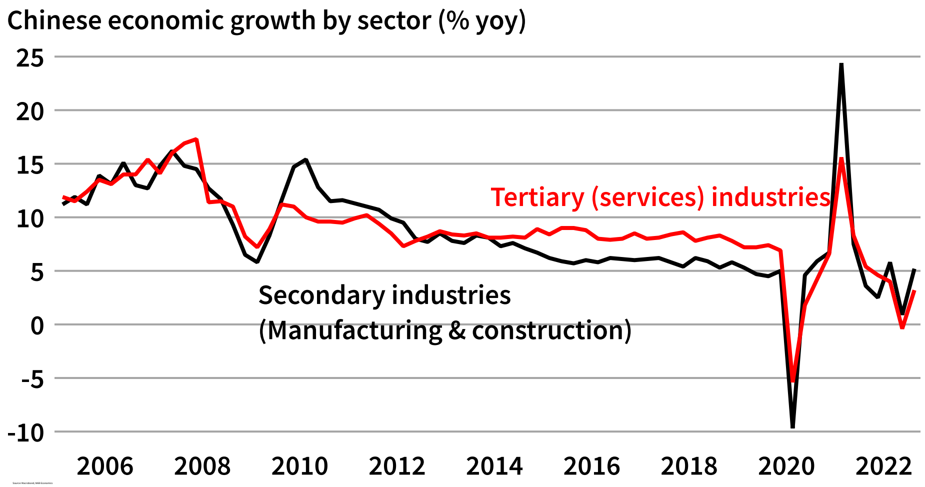
China's economic growth

China's growth rebounded but was boosted by base effects



Economic growth by industry

Services continue to lag on weak household demand



- China's latest national accounts data show its economy expanded by 3.9% yoy in Q3. By historical standards, this rate of growth is not particularly strong (particularly when compared with pre-pandemic rates) and this increase is somewhat inflated by base effects – given that Q3 2021 was negatively impacted by the Delta wave of COVID-19 and electricity shortages hitting a number of provinces.

- Similarly, the seasonally adjusted quarterly growth of 3.9% followed on from a steep contraction (revised lower to -2.7%) in the second quarter, which was driven by lockdowns and other COVID-19 restrictions in a range of locations, most notably Shanghai.

- By industry, growth was stronger in the industrial sector – which increased by 5.2% yoy, while the services sector increased by a more modest 3.2% yoy – continuing to highlight the relative weakness in China's household demand – which appears unlikely to improve while strict policy responses to COVID-19 outbreaks remain in place.

- We have not fundamentally changed our views around China's economy this month. The slightly stronger than expected growth in Q3 bumps up our forecast for 2022 to 3.4% (from 3.3% previously). Our forecasts for 2023 and 2024 are unchanged at 5.0% and 4.5% respectively, and weaker demand from advanced economies will require growth to be driven by the domestic economy.

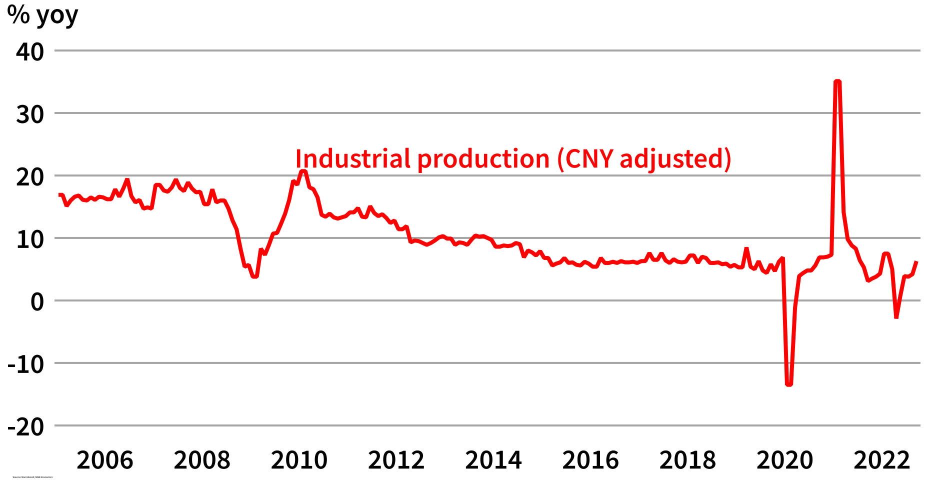
NAB China GDP forecasts

%	2021	2022	2023	2024
GDP	8.1	3.4	5.0	4.5

Industrial production

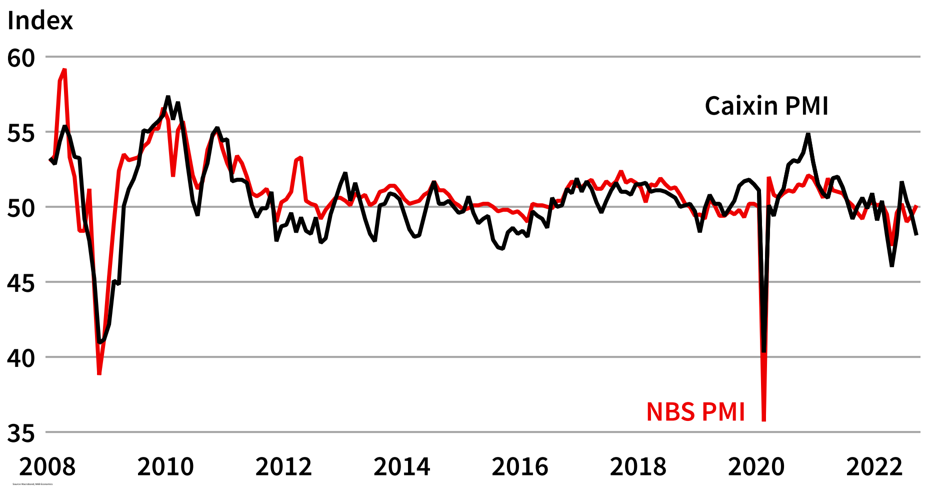
Industrial production

Growth accelerated in part on energy shortage base effects



Diverging trends in China's manufacturing PMIs

Private sector survey weaker, as official measure turns neutral

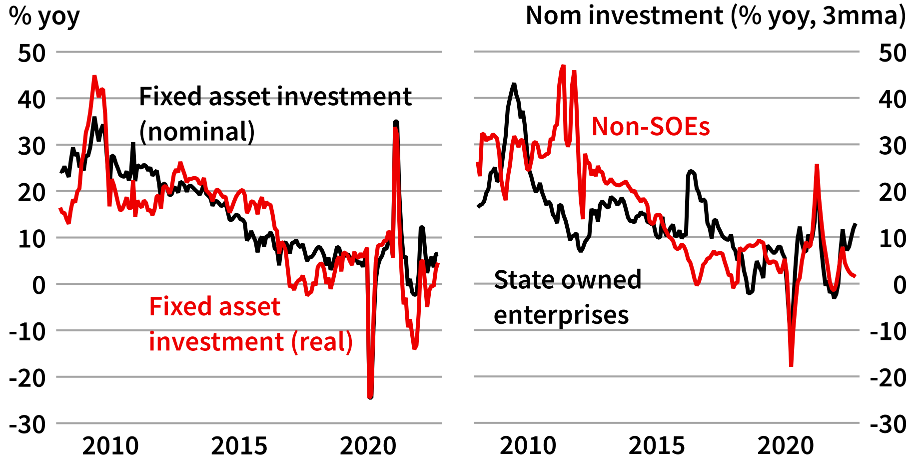


- China's industrial production growth accelerated in September – increasing by 6.3% yoy (from 4.2% yoy previously). The strength of this increase may be somewhat overstated – given that China's industrial sector was negatively impacted by energy shortages in September 2021.
- This meant that there were some sizeable increases in some of the sectors negatively impacted last year. Crude steel production rose by 17.6% yoy, while automobile output increased by 25.4% yoy, while electronics – which was less impacted last year – increased by 10.6% yoy.
- China's main manufacturing surveys showed diverging trends in September. The official NBS PMI returned to neutral levels – at 50.1 points (from 49.4 points in August). In contrast, the private sector Caixin PMI fell further – down to 48.1 points (from 49.5 points previously).
- A key difference between the two surveys was the production measure – which rebounded in the NBS survey but deteriorated in the Caixin one – potentially highlighting the differing composition of firms in each survey. Similarly, new orders were less negative in the official survey, but more negative in the private survey. Both surveys pointed to continued deterioration in new export orders – as tighter financial conditions in advanced economies has started to impact demand.

Investment

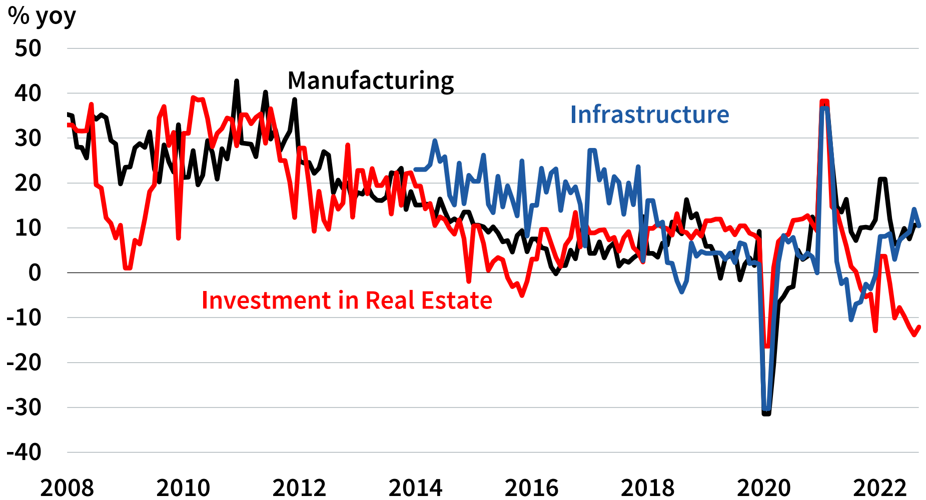
Fixed asset investment

SOEs continue to drive growth in investment



Fixed asset investment by industry

Real estate investment continues to contract



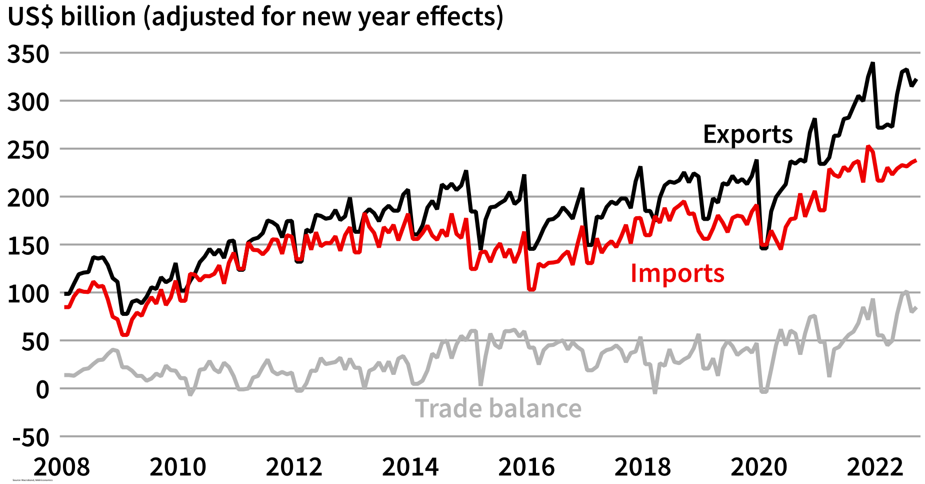
Source: Macrobond, NAB Economics

- Growth in China's fixed asset investment edged higher in September – increasing by 6.5% yoy (from 6.4% yoy previously). Producer prices flow through into the cost of investment goods, and the easing of producer prices imply stronger growth in real investment. Our estimates suggest that real investment rose by 4.6% yoy (from 3.1% yoy in August).
- State-owned enterprises (SOEs) have continued to lead the increase in nominal investment. In September, SOE investment increased by 13.6% yoy, while in contrast, investment by private sector firms rose by 2.2% yoy.
- There remains substantial divergence in investment trends by industry. There continues to be strong growth in investment in both manufacturing and infrastructure – up by 10.7% yoy and 10.5% yoy respectively in September. Chinese authorities have sought to ramp up infrastructure spending in recent months to provide economic stimulus.
- In contrast, investment in real estate continues to decline – down by 12.1% yoy. New residential construction starts have continued to fall – down by almost 44% yoy in September – as the steep correction in the sector continues.

International trade

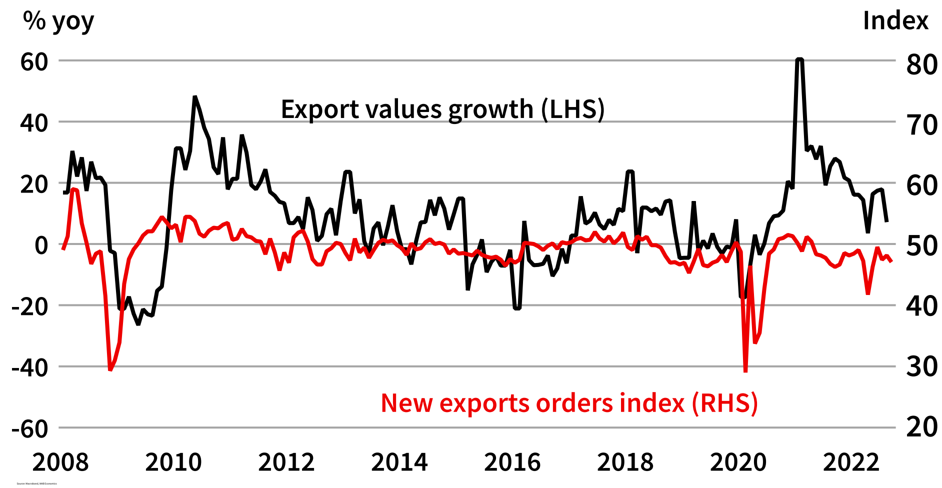
China's trade balance

Surplus stronger in September as exports rose faster



Export value and new export orders

Export growth slowed in recent months, and new orders are weak



- China's trade surplus was stronger in September, as exports rose more rapidly than imports month-on-month. Overall, the surplus totalled US$84.7 billion (compared with US$79.4 billion previously) – a level that is quite high by historical standards.

- China's imports totalled US$238.0 billion, up from US$235.5 billion in August. Imports have increased only marginally in year-on-year terms in recent months, rising by just 0.3% in September. Given rising import prices in recent months, this implies that import volumes have continued to contract.

- Export values rose in September to US$322.8 billion (from US$314.9 billion previously). In year-on-year terms, exports increased by 5.7% yoy. In a similar trend to imports, growth in export values has been largely driven by price effects – with export prices increasing at double digit rates between May and August.

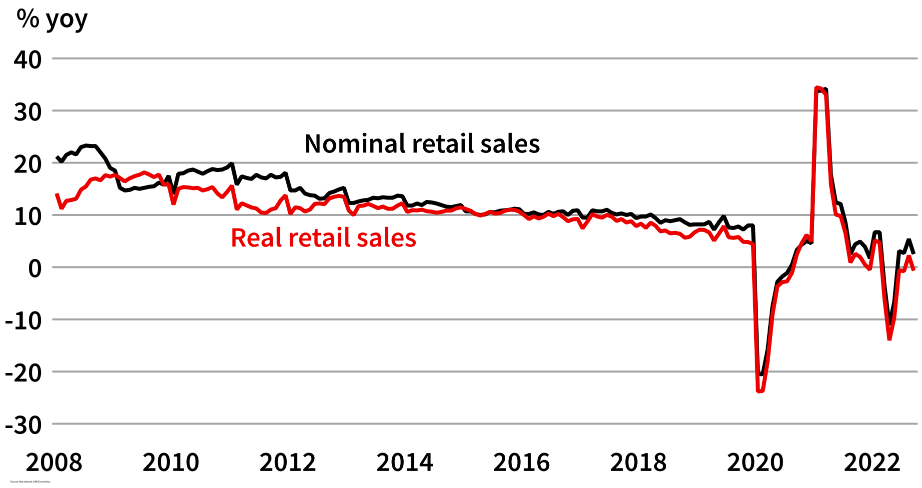
- The new export orders measure in the NBS manufacturing PMI survey has remained negative since May 2021 and dipped further in September – down to 47.0 points (from 48.1 points in August). Weaker growth in advanced economies in coming months is likely to negatively impact export growth going forward.

- Trends in exports to major trading partners were highly mixed in September. The strongest growth was recorded in exports to East Asia – rising by 10.8% yoy - with an even stronger increase in this region when Hong Kong is excluded. In contrast, exports to the European Union-27 + the United Kingdom rose by just 3.0% yoy, while exports to the United States contracted by 11.6% yoy.

Retail sales and inflation

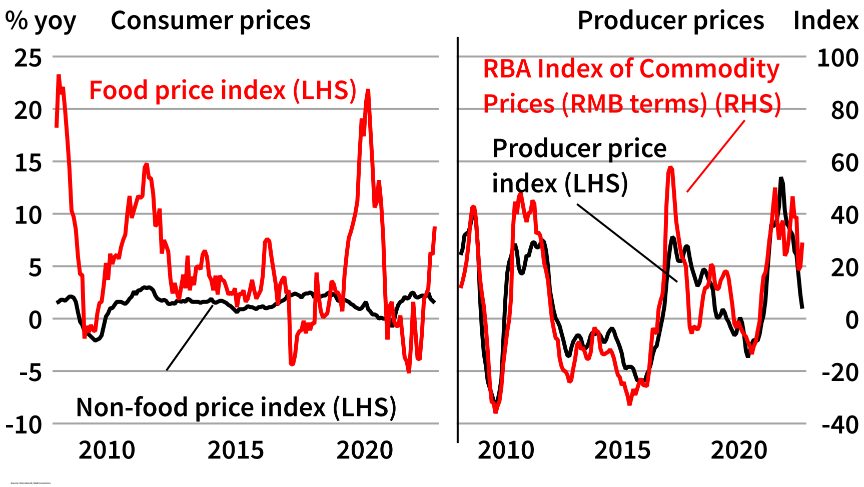
Retail sales growth

Real sales returned to negative territory in September



Consumer and producer prices

Pork now driving food price inflation (reversing recent trends)

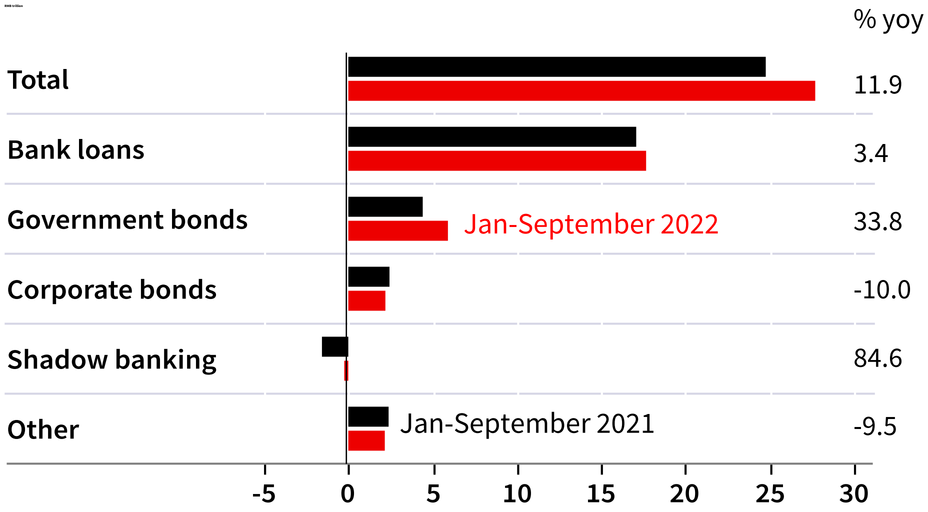


- Nominal retail sales growth eased in September, increasing by 2.5% yoy (compared with 5.4% yoy in August). Growth in retail prices was marginally stronger in September (compared with August), meaning that this drove real retail sales back into negative territory – contracting by 0.7% yoy (compared with a 2.2% yoy increase previously). The increase in real sales in August was in part related to the Delta wave of COVID-19 that led to weaker conditions in August 2021.
- Overall, China's consumer prices rose more rapidly in September – with the headline consumer price index increasing by 2.8% yoy (compared with 2.5% yoy in August). Despite this upturn, China's inflation remains weak when compared with global trends – in part reflecting soft domestic demand.
- Food prices continued to accelerate in September, increasing by 8.8% yoy (compared with 6.1% yoy previously). The reversal of earlier pork price deflation has been a key driver of the recent increase in food prices – with pork rising by 36.0% yoy in September. In addition, fresh fruit and fresh vegetable prices have also risen considerably – up by 17.8% yoy and 12.1% yoy.
- In contrast, non-food prices increased by 1.5% yoy (compared with 1.7% yoy in August). Vehicle fuel prices have continued to increase strongly in September – up by 19.0% yoy (compared with 19.9% yoy previously).
- Growth in producer prices continued to slow in September – rising by just 0.9% yoy (from 2.3% yoy previously). This deterioration came despite a recent upturn in commodity prices – with the RBA Index of Commodity Prices (converted to RMB terms) rising by 29% yoy in September. This may suggest that Chinese manufacturers are facing margin squeeze – unable to fully pass through cost increases due to weak demand in domestic and foreign markets.

Credit conditions

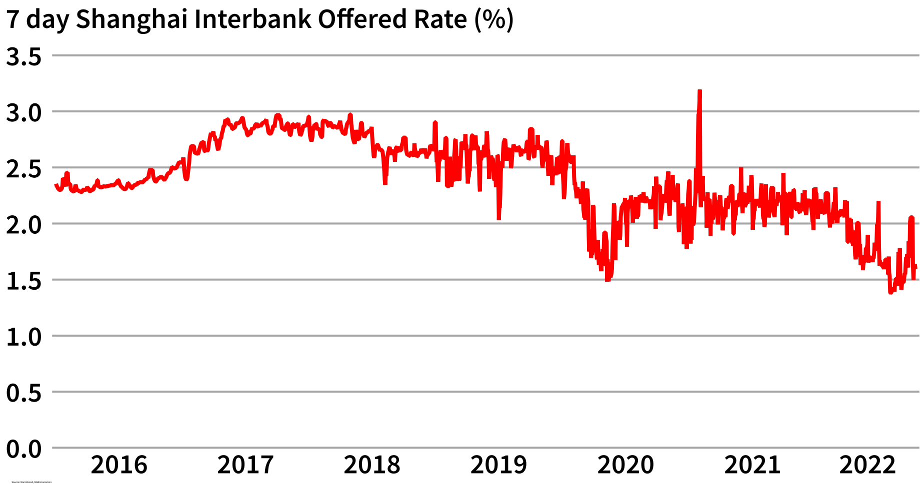
New credit issuance

Bank lending surge in September drove ytd growth higher



Interbank interest rates

Low rates point to excess liquidity in interbank markets



- Headline credit data in September appeared surprisingly strong – with a rebound in total issuance, led by a surge in bank lending. Various reports suggest that this primarily reflected loans from policy banks – backed directly by the People's Bank of China (PBoC) – to local government financing vehicles LGFVs). We detailed concerns around LGFVs in this month's China Economic Update.

- In the first nine months of 2022, new credit issuance increased by 11.9% yoy to RMB 27.7 trillion. Bank loans continue to account for the largest share of total credit issuance – around 64% of the total over this period – and loans grew by 3.4% yoy. This funding source had contracted year-on-year in the first eight months, but the surge in September was more than enough to reverse this trend.

- Non-bank lending rose by 30.5% yoy in the first nine months. The key driver over this period was government bond issuance – up by 33.8% yoy – however this rate of increase has slowed in recent months. In addition, shadow bank lending decreased by a smaller amount in this period.

- The PBoC maintained its Medium Term Lending Facility (MTF) rate unchanged in September. As we have noted in recent months, the effectiveness of monetary easing is questionable at present – with low interbank interest rates implying excess liquidity. Banks have a lot of funds available for lending, but there is little demand from the private sector – in part connected to the deterioration in the property sector, but also the weakness in household activity.

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