NAB Group Economics

national australia bank

China's economy at a glance

April 2023

Author: Gerard Burg, Senior Economist - International

Key points

Services sector supports growth rebound in Q1, as base effects boost consumption

- According to China's national accounts data, its economy grew by 4.5% yoy in Q1. This was stronger than market expectations (at around 4.0%), reflecting the faster than anticipated transition period following the end of zero-COVID policies, as well as support from base effects (with the end of Q1 2022 marking the start of the COVID-19 wave that would heavily impact the following quarter). We have revised our forecast for China's growth in 2023 to 5.6% (5.4% previously), although the property sector and foreign trade could be headwinds. The outlook for 2024 and 2025 is unchanged.

- China's industrial production grew more strongly in March, up by 3.9% yoy (compared with 2.4% yoy in January-February). It is worth noting that this remains a relatively weak rate of growth when compared with the pre-pandemic trend.

- Growth in nominal fixed asset investment slowed in March. That said, the declines in producer prices – which flow through into the cost of investment goods – accelerated in March. As a result, our estimate of real investment rose to 5.2% yoy (from 4.4% yoy in January and February).

- China's trade surplus strengthened in March, totalling US$88.2 billion (compared with an average of US$58.4 billion across January and February). Both exports and imports were stronger in March, with the increase in the surplus driven by the more rapid upturn in exports. We expect tighter financial conditions in advanced economies, along with the shift in preferences towards services, to limit export growth going forward.

- In nominal terms, China's retail sales rose by 10.6% yoy in March (compared with 3.5% yoy in January and February). It is worth noting that this growth rate was boosted by base effects – with retail sales falling by almost 1.4% mom in March 2022 as the COVID-19 outbreak in Shanghai (that led to a long running hard lockdown) began to emerge.

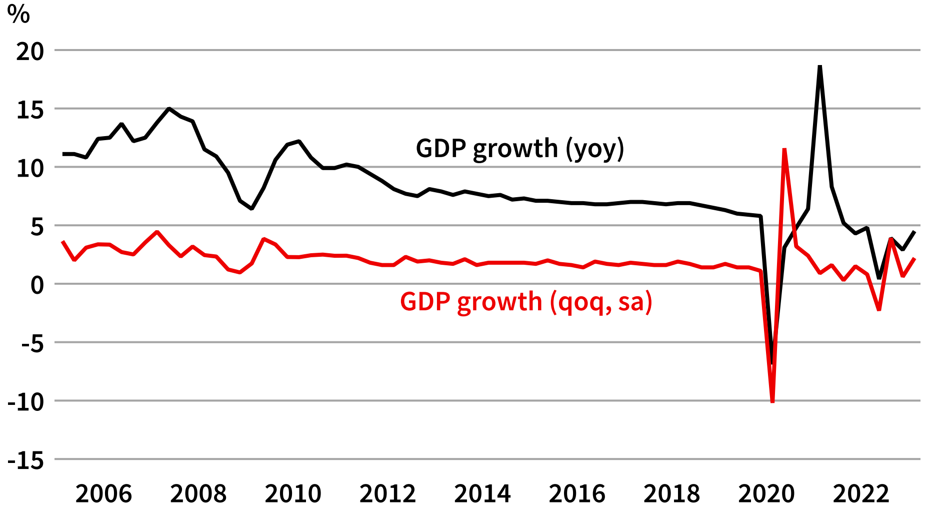
- New credit issuance has continued to expand strongly – up by 20.5% yoy in the first three months of 2023 to total RMB. Bank lending has been the key driver of credit issuance in early 2023 – increasing by 26.4% yoy to RMB 10.8 trillion. Growth in outstanding bank loans has been primarily driven by increased lending to households – reflecting a modest recovery in the property sector, but it remains to be seen how sustainable this upturn proves to be.

- China's monetary authorities have continued to ease policy from a quantity perspective – by cutting the Reserve Requirement Ratio (RRR) – rather than the price (with the Loan Prime Rate having remained unchanged since August 2022). This change may not have a significant impact on lending – given that banks were not facing a shortage of liquidity prior to the cut, and the Loan Prime Rate has been providing something of a floor to interbank rates. Some of the rationale may have been pre-emptive support for Chinese banks in the event that mid-March's banking sector fears in the United States and Europe became global.

Gross domestic product

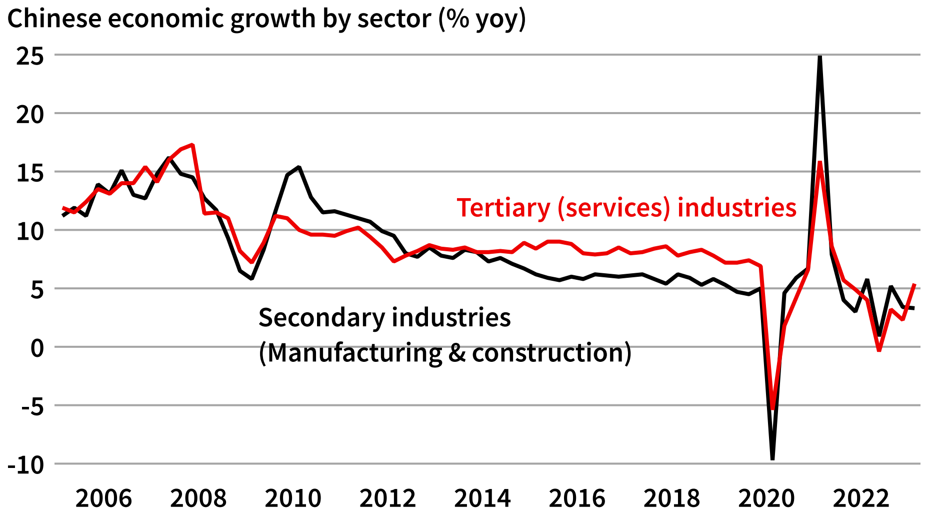
China's economic growth

Growth picks up on quick transition and base effects



Economic growth by industry

Services accelerated as the zero-COVID shackles were removed



Sources: Macrobond, NAB Economics

- According to China's national accounts data, its economy grew by 4.5% yoy in Q1. This was stronger than market expectations (at around 4.0%), reflecting the faster than anticipated transition period following the end of zero-COVID policies, as well as support from base effects (with the end of Q1 2022 marking the start of the COVID-19 wave that would heavily impact the following quarter).
- By industry, there was a strong rebound in China's service sector growth – up by 5.4% yoy (compared with 2.3% yoy in Q4 2022). This sector had the greatest potential for gain, as it was heavily impacted by zero-COVID policies. In contrast, the secondary sector (manufacturing and construction) grew marginally more slowly – up by 3.3% yoy (from 3.4% yoy in Q4 2022).
- There remains uncertainty around the outlook for China's growth across the rest of 2023 – particularly related to the strength of household consumption and the path of the property sector (which represents an outsized share of China's economy when compared with other major economies), which could remain a headwind, along with foreign trade. Growth in Q2 will be elevated by base effects (reflecting the impact of the severe lockdowns that affected activity during this period in 2022).
- Reflecting the stronger than anticipated start to the year, we have revised our forecast for China's growth in 2023 to 5.6% (5.4% previously). The outlook for 2024 and 2025 is unchanged.

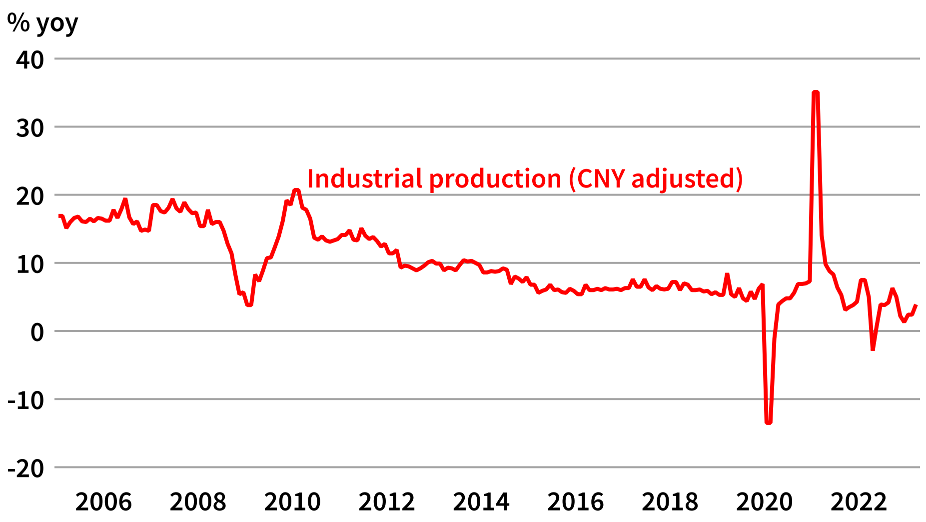
NAB China GDP forecasts

%	2022	2023	2024	2025
GDP	3.0	5.6	4.5	4.8

Industrial production

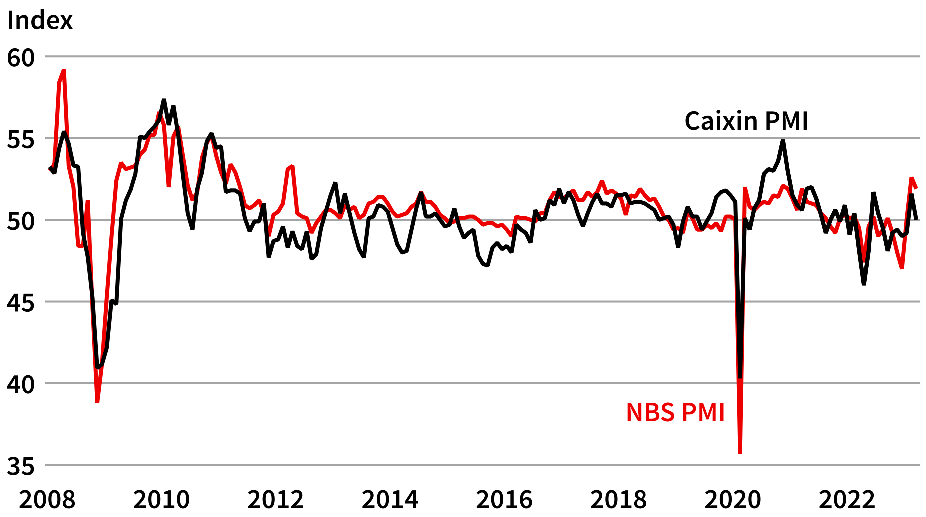
Industrial production

Output growth rose in March, but still relatively weak



Manufacturing PMI surveys

Softer readings in March, with private survey back to neutral



Sources: Macrobond, NAB Economics

- China's industrial production grew more strongly in March, up by 3.9% yoy (compared with 2.4% yoy in January-February). It is worth noting that this remains a relatively weak rate of growth when compared with the pre-pandemic trend.

- Output trends among major industrial categories remained quite mixed in March. Motor vehicle production rose strongly – up by 11.2% yoy – along with construction related heavy industries – with cement and crude steel increasing by 10.4% yoy and 6.9% yoy respectively. In contrast, production of consumer electronics products grew by just 1.2% yoy.

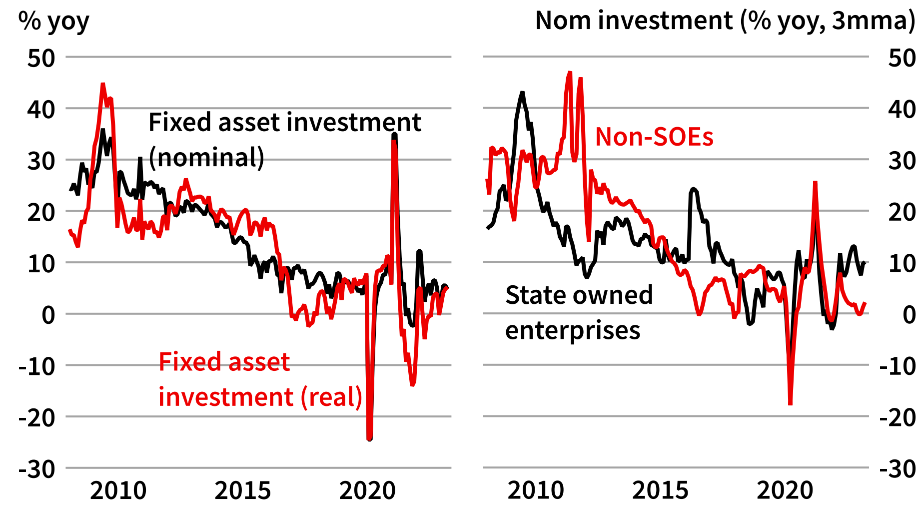
- China's main manufacturing surveys were softer in March – albeit the scale of the softening differed between the two. The Caixin PMI declined to a neutral 50.0 points (from 51.6 points previously) – which may suggest that the rebound from the end of zero-COVID has run its course for private sector firms. In contrast, the official NBS PMI was only marginally weaker – at 51.9 points (from 52.6 points in February).

- A key point of difference between the two surveys in March was new export orders. The official PMI measure remained positive – albeit less so than was the case in February – while this measure dipped back into negative territory in Caixin survey.

Investment

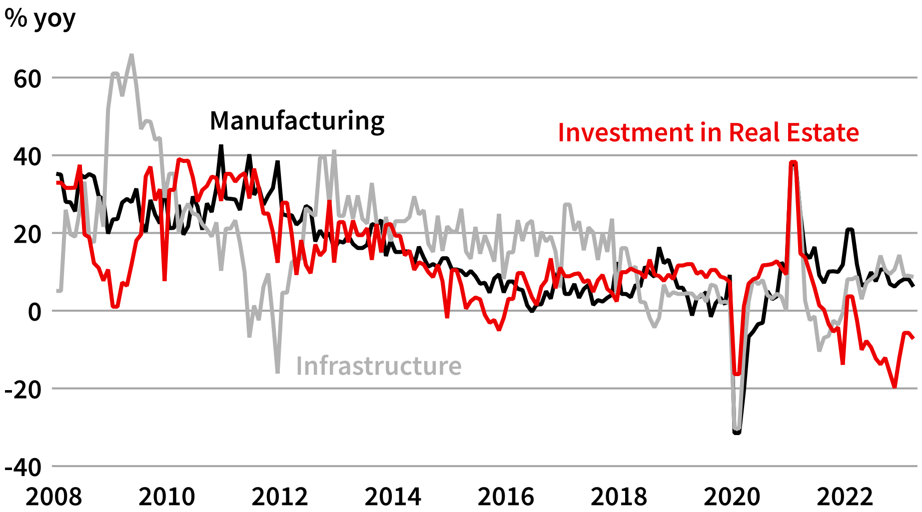
Fixed asset investment growth

State-owned firms continue to drive investment growth



Fixed asset investment by industry

Real estate investment remains weak



Sources: Macrobond, NAB Economics

- In nominal terms, China's fixed asset investment increased by 4.8% yoy in March (down from an average of 5.5% yoy in the first two months of 2023). That said, the declines in producer prices – which flow through into the cost of investment goods – accelerated in March. As a result, our estimate of real investment rose to 5.2% yoy (from 4.4% yoy in January and February).

- Investment growth continues to be driven by state-owned enterprises – with private sector investment growth relatively weak since the early months of 2022. Nominal SOE investment rose by 9.6% yoy in March (down from 10.5% yoy in January-February), while private investment grew by just 1.8% yoy (from 2.6% yoy previously).

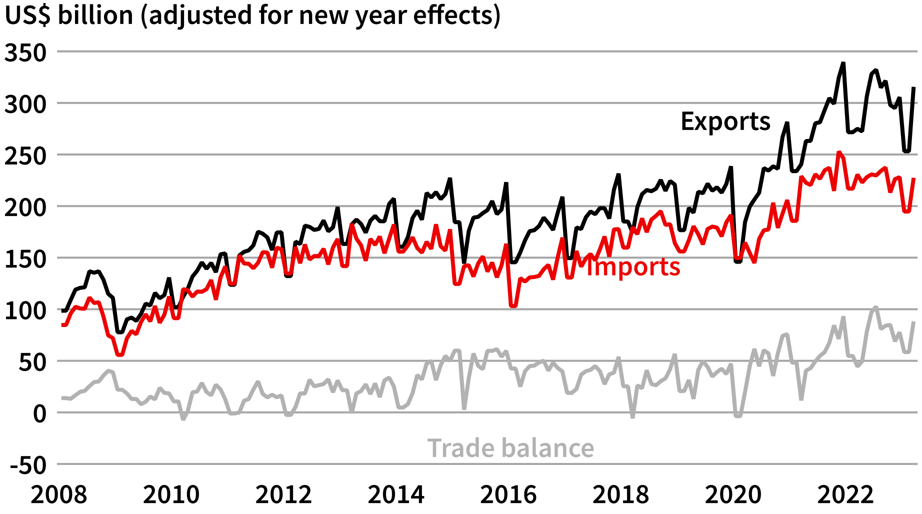
- Investment trends by major industries continue to diverge. Investment in both infrastructure and manufacturing have increased strongly in recent months – up 8.7% yoy and 6.2% yoy respectively in March.

- In contrast, investment in real estate has remained weak – reflecting the impact of the Three Red Lines policy, the collapse of major property developer Evergrande (along with some smaller peers) and last year's mortgage strike. Investment in the sector fell by 7.2% yoy in March. There are signs emerging of a turn-around in the property sector – with residential sales (by floor area) increasing by 1.4% yoy in March (the first increase since mid-2021), however construction starts continue to contract.

International trade – trade balance and imports

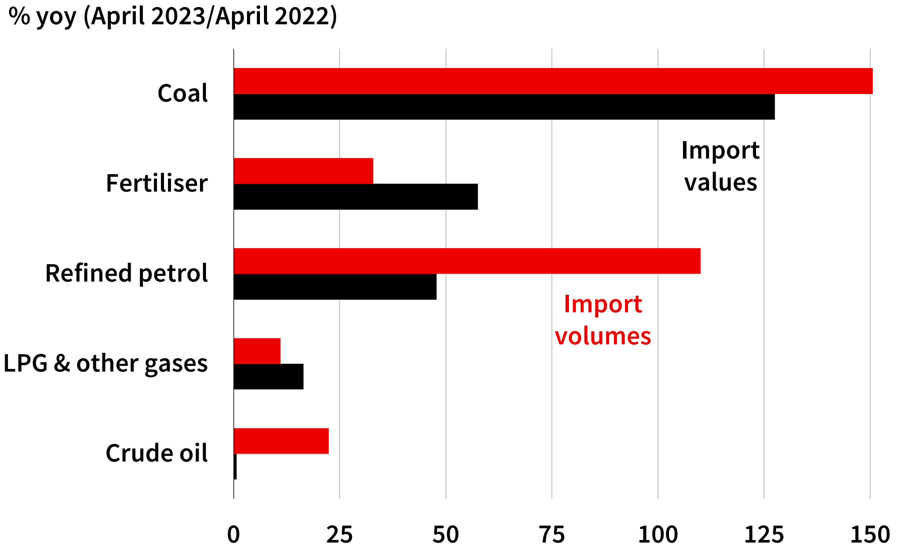
China's trade balance

Surplus rises on surprise surge in exports



Energy related import volumes and prices

Falling prices lowered most energy import values (versus volumes)



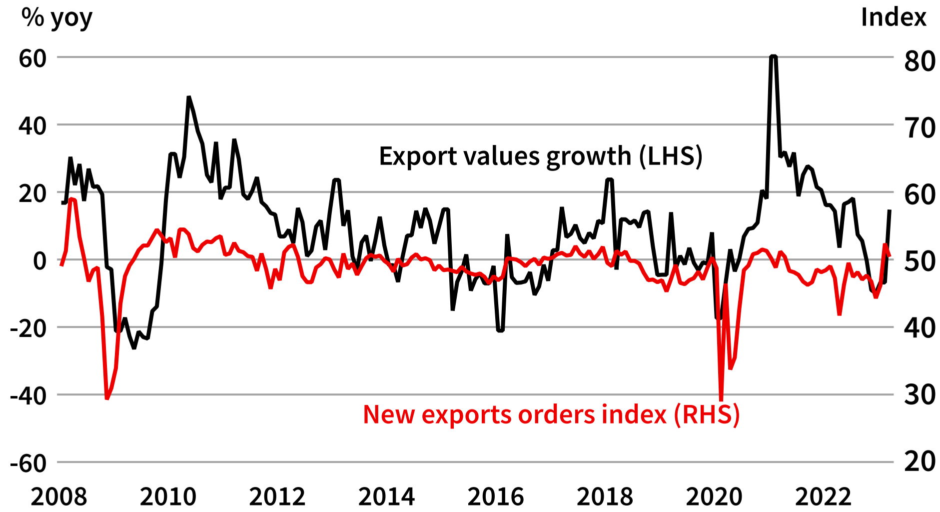
Sources: Macrobond, NAB Economics

- China's trade surplus strengthened in March, totalling US$88.2 billion (compared with an average of US$58.4 billion across January and February). Both exports and imports were stronger in March, with the increase in the surplus driven by the more rapid upturn in exports.
- China's rolling twelve month trade surplus with the United States has continued to decline, reflecting the impact of tighter monetary policy and a rebalancing in US consumption towards services (and away from goods). In March, the rolling surplus totalled US$380.9 billion, well below the peak of US$439.7 billion in July 2022, but still above the pre-trade war levels.
- China's imports totalled US$227.4 billion in March (up from an average of US$194.7 billion in the first two months of 2023). Although this represented a sizeable increase month-on-month, China's imports fell by 1.4% yoy.
- In a large part, the relative weakness in imports reflects price effects. US dollar denominated import prices increased strongly from early 2021 through mid-2022, before falling from November 2022 onwards. In contrast, import volumes fell year-on-year across most of 2022, but rose sharply in February 2023 (albeit January and February data can be distorted by the differing timing of Chinese New Year). Given a strong year-on-year fall in US dollar commodity prices (as measured by the RBA Index of Commodity Prices) in March, import volumes likely rose again last month.
- Lower energy prices were a key driver of this trend – reflecting the surge in prices in March 2022 (following Russia's invasion of Ukraine) and subsequent easing from mid-year. Import volumes for coal, refined petroleum products and crude oil rose more strongly than import values due to lower prices for these commodities. The most notable exception was fertilisers – which are typically energy intensive in production and where global trade has been significantly disrupted by the European conflict.

International trade – exports

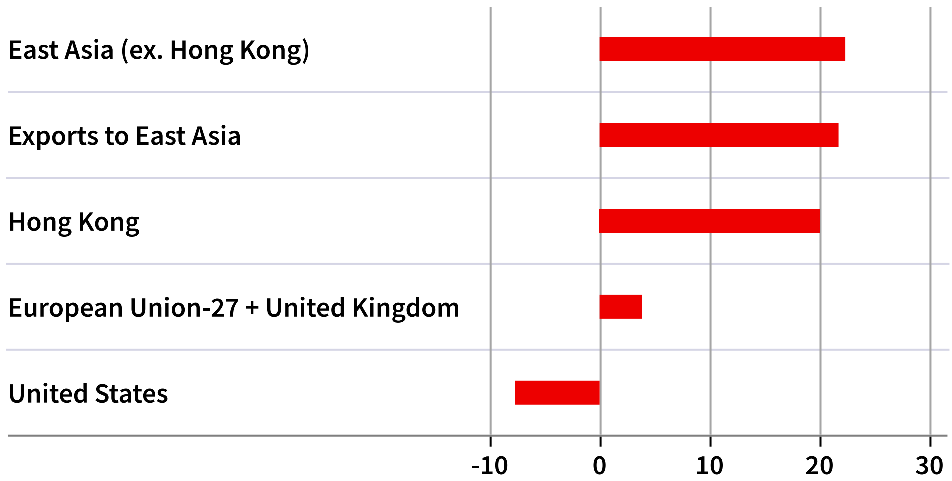
Export value and new export orders

Surprise rebound in exports in March not expected to continue



Exports to major trading partners

Growth led by exports to East Asia



Sources: Macrobond, NAB Economics

- China's exports totalled US$315.6 billion in March, up from an average of US$253.2 billion in the first two months. In year-on-year terms, this represented an increase of 14.8% – albeit this may reflect base effects, given the disruptions to activity (particularly transport and logistics) due to the COVID-19 wave that commenced in March 2022.

- That said, the strong month-on-month rebound was somewhat surprising, given the weakening prospects in global demand. Despite this, the new export orders measure in the NBS PMI remained in positive territory for the second straight month – at 50.4 points (from 52.4 points in February). We expect tighter financial conditions in advanced economies, along with the shift in preferences towards services, to limit export growth going forward.

- Exports to major trading partners were highly divergent in March. Following steep falls in January and February, exports to the United States declined once again – down by 7.7% yoy – while exports to the European Union-27 and the United Kingdom rose moderately – up by 3.7% yoy.

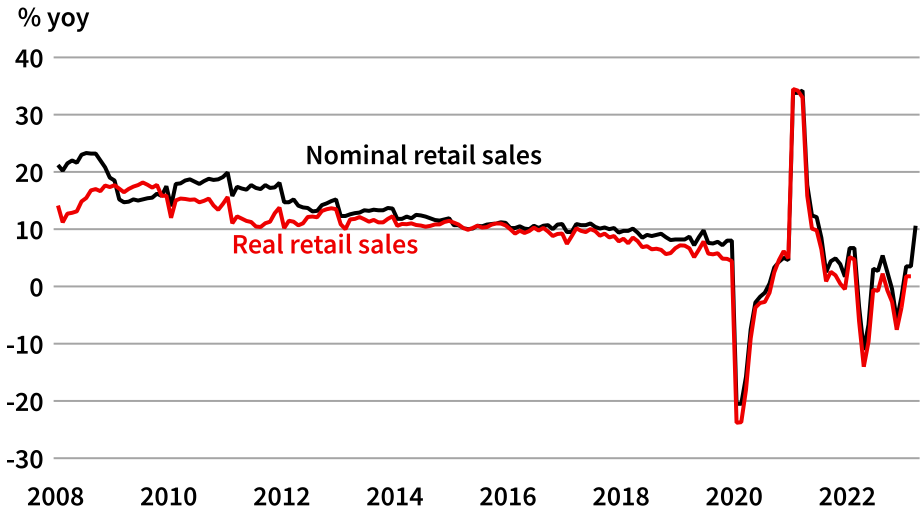
- In contrast, exports to East Asia surged in March – up by 21.7% yoy. Hong Kong recorded its first increase in exports since January-February 2022 – increasing by 20.0% yoy, while non-Hong Kong East Asia rose by 22.3% yoy – led by Vietnam, Singapore and Malaysia.

- In addition, there was a surge in exports to the Russian Federation – up by 136% yoy.

Retail sales and inflation

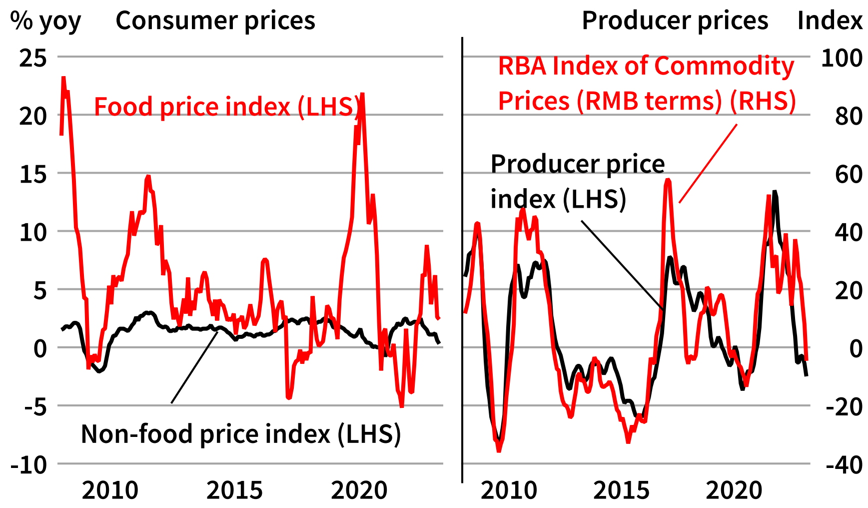
Retail sales growth

Base effects support strong rebound in March



Consumer and producer prices

Slower price growth in March; producer prices contract



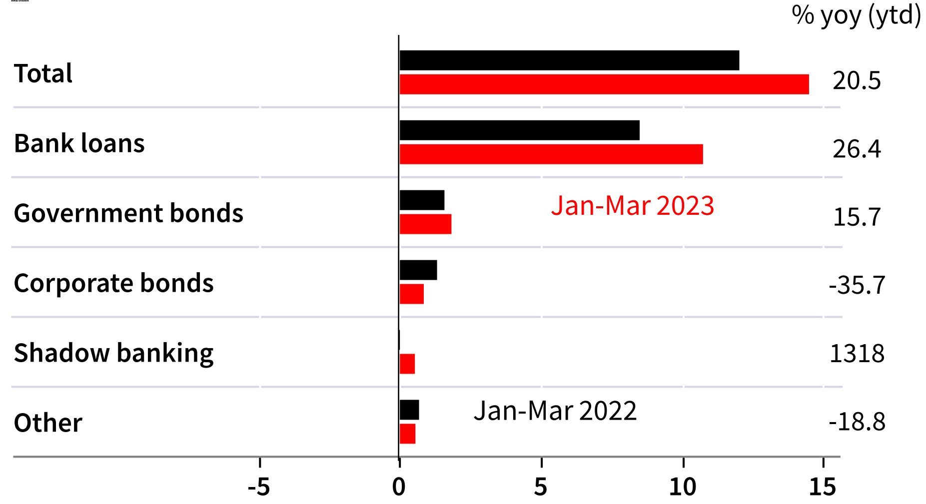
Sources: Macrobond, NAB Economics

- In nominal terms, China's retail sales rose by 10.6% yoy in March (compared with 3.5% yoy in January and February). It is worth noting that this growth rate was boosted by base effects – with retail sales falling by almost 1.4% mom in March 2022 as the COVID-19 outbreak in Shanghai (that led to a long running hard lockdown) began to emerge.
- Chinese authorities have not released retail price index data so far in 2023, however relative weak growth in consumer prices implies that real retail sales in March would have been at their strongest rate since mid-2021.
- Consumer price growth slowed considerably in March – down to 0.7% yoy, from an average of 1.5% yoy across January and February. This remains consistent with a modest rebound in consumer spending following China's reopening.
- Growth in food prices continued to slow in March – rising by 2.4% yoy (compared with a 4.4% yoy increase across the first two months of 2023). This slower trend came despite an uptick in pork prices – which have been a major influence on the overall food price index in recent years – up by 9.6% yoy (from 7.9% in January-February). In contrast, there was a sharp fall in prices of fresh vegetables and modest easing in seafood prices.
- Non-food prices have continued to grow more slowly – rising by just 0.3% yoy (compared with a 0.9% yoy increase in January-February). Vehicle fuel prices fell by 6.4% yoy in March, compared with a 2.9% yoy increase over the first two months – reflecting broader trends in global energy markets.
- Producer prices contracted more rapidly in March – down by 2.5% yoy (compared with a 1.1% yoy fall in January-February). In part this reflected weaker commodity prices – with the RBA Index of Commodity Prices (converted into RMB terms) falling by 4.6% yoy in March, compared with strong increases across the second half of 2022.

Credit conditions

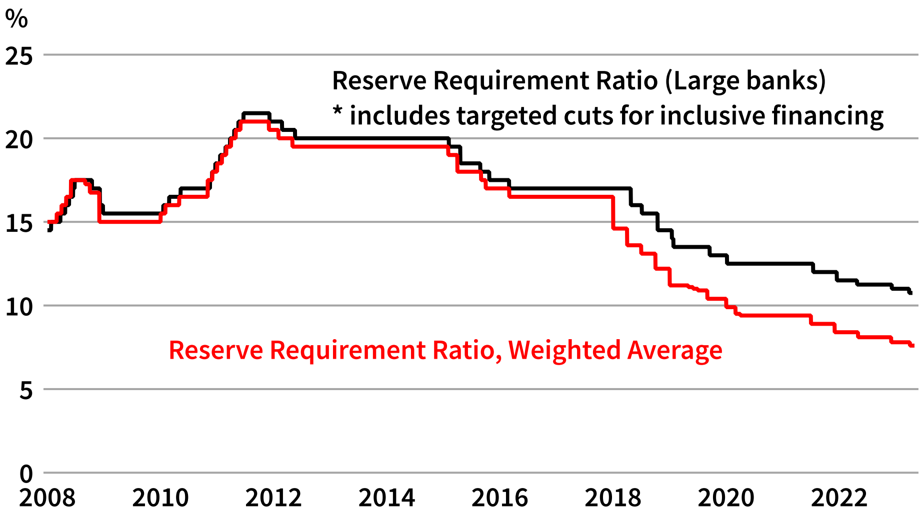
New credit issuance

Bank lending led the growth in credit in Q1



Reserve Requirement Ratio

China's latest easing may not significantly boost lending



Sources: Macrobond, NAB Economics

- New credit issuance has continued to expand strongly – up by 20.5% yoy in the first three months of 2023 to total RMB. Bank lending has been the key driver of credit issuance in early 2023 – increasing by 26.4% yoy to RMB 10.8 trillion. Growth in outstanding bank loans has been primarily driven by increased lending to households – reflecting a modest recovery in the property sector, but it remains to be seen how sustainable this upturn proves to be.

- In contrast, growth in non-bank lending was comparatively slow over this period, up just 6.3% yoy. Corporate bond issuance was considerably weaker in year-on-year terms, although this was more than offset by growth in government bond issuance and (perhaps surprisingly after several years of declines) shadow banking.

- China's monetary authorities have continued to ease policy from a quantity perspective – by cutting the Reserve Requirement Ratio (RRR) – rather than the price (with the Loan Prime Rate having remained unchanged since August 2022).

- In mid-March, the People's Bank of China (PBoC) announced a 25 basis point cut to the RRR, excluding banks whose ratio was already at 5% (such as smaller institutions and rural banks). According to the PBoC, the weighted average RRR fell from 7.8% to 7.6% following the move.

- This change may not have a significant impact on lending – given that banks were not facing a shortage of liquidity prior to the cut, and the Loan Prime Rate has been providing something of a floor to interbank rates. Some of the rationale may have been pre-emptive support for Chinese banks in the event that mid-March's banking sector fears in the United States and Europe became global.

Group Economics

Alan Oster
Group Chief Economist
+(61 0) 414 444 652

Jacqui Brand
Personal Assistant
+(61 0) 477 716 540

Dean Pearson
Head of Behavioural & Industry Economics
+(61 0) 457 517 342

Australian Economics and Commodities

Gareth Spence
Senior Economist – Australia
+(61 0) 436 606 175

Brody Viney
Senior Economist
+(61 0) 452 673 400

Phin Ziebell
Economist – Agribusiness
+(61 0) 475 940 662

Behavioural & Industry Economics

Robert De Iure
Senior Economist – Behavioural & Industry Economics
+(61 0) 477 723 769

Brien McDonald
Senior Economist – Behavioural & Industry Economics
+(61 0) 455 052 520

Steven Wu
Economist – Behavioural & Industry Economics
+(61 0) 472 808 952

International Economics

Tony Kelly
Senior Economist
+61 (0) 477 746 237

Gerard Burg
Senior Economist – International
+(61 0) 477 723 768

Global Markets Research

Ivan Colhoun
Chief Economist
Corporate & Institutional Banking
+(61 2) 9293 7168

Skye Masters
Head of Markets Strategy
Markets, Corporate & Institutional Banking
+(61 2) 9295 1196