NAB Group Economics

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China's economy at a glance

November 2023

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Key points

Bond-fuelled lending to support near-term growth but challenges remain unaddressed

- There was little in this month's data to change our overall view of China's economy. Rapid expansion in government bond issuance in recent months should ensure that China meets (and likely exceeds) its growth target for the year, but not address fundamental constraints around household consumption and the real estate sector. Our forecasts for China's economic growth are unchanged – with 2023 growth at 5.2%, 2024 at 4.5% and 2025 and 4.8%.

- Growth in China's industrial production edged up in October, increasing by 4.6% yoy, compared with 4.5% yoy in both August and September. We continue to note that these rates of increase are relatively modest compared with pre-pandemic rates.

- China's real fixed asset investment grew more slowly in October – increasing by 1.8% yoy in October (down from 2.9% yoy previously). There remains a sizeable disparity between growth in nominal investment by state-owned enterprises (SOEs) and private sector firms. SOE investment rose by 3.1% yoy in October – its slowest rate of expansion since December 2021 – while private sector investment edged up by 0.1% yoy.

- China's trade surplus was somewhat narrower in October – totalling US$56.5 billion (down from US$77.8 billion in September) – with this outcome reflecting an easing in export values. Prices remain a key influence on both import and export values.

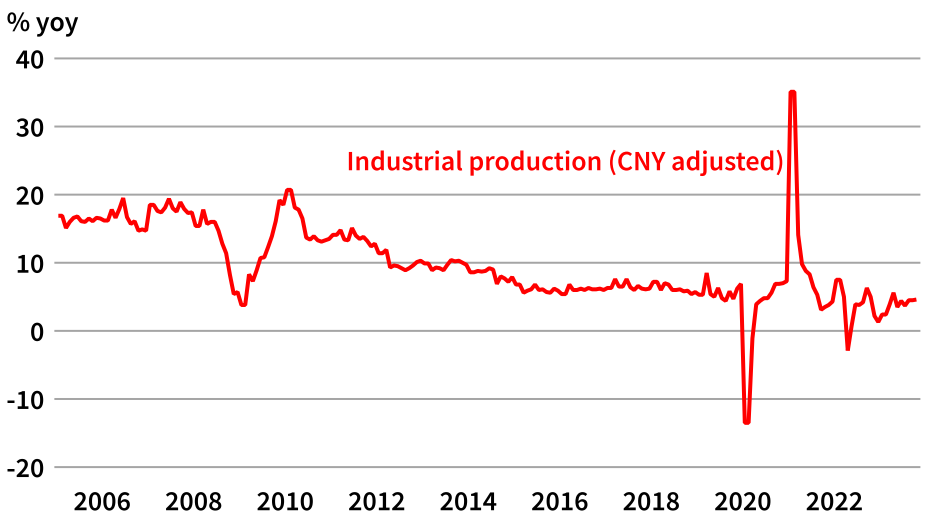
- Real retail sales grew by 7.8% yoy (also up from 5.5% yoy previously). The extreme volatility of sales data during the COVID-19 pandemic makes it difficult to interpret the direction of these trends; the pickup may reflect the impact of the Golden Week holidays at the start of the month – which were negatively impacted in 2022 by COVID-19 restrictions – resulting in a boost from base effects.

- The People's Bank of China (PBoC) left its medium term lending facility (MLF) rate unchanged in November. The MLF is the basis for bids from commercial banks used to determine the Loan Prime Rate (China's primary policy rate). That said, the PBoC provided additional funding to financial markets, over and above the MLF loans that were expiring this month to expand liquidity. At a high level, we don't view this as being particularly significant – there was no shortage of funds available for lending, rather demand for loans (particularly in the real estate sector and among private firms more generally) has been weak, and this move will do nothing to address this.

Industrial production

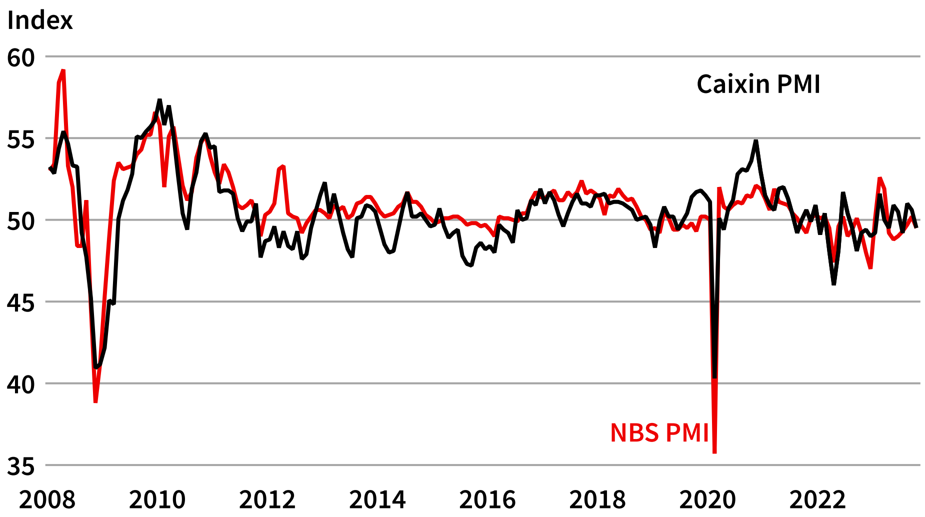
Industrial production growth

Output growth edged up but diverging subsector trends continued



Manufacturing PMI surveys

Both surveys converged at modestly negative levels in October



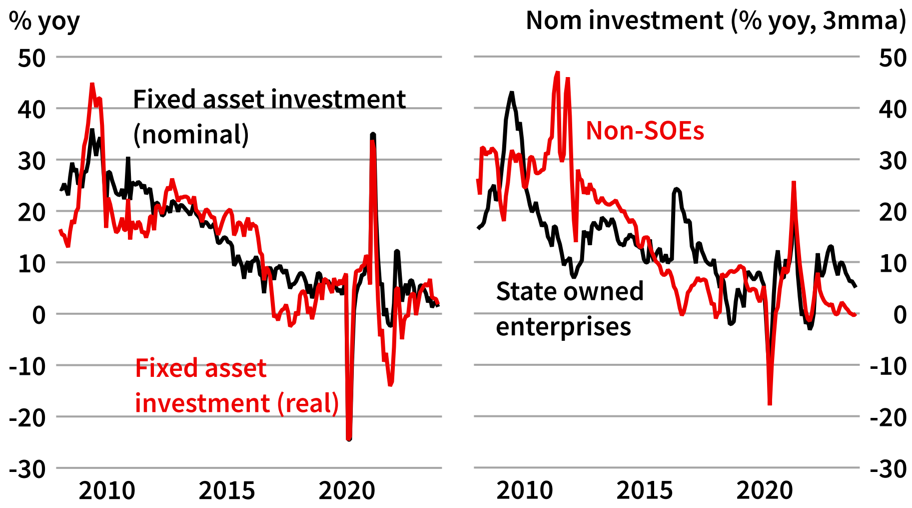
- Growth in China's industrial production edged up in October, increasing by 4.6% yoy, compared with 4.5% yoy in both August and September. We continue to note that these rates of increase are relatively modest compared with pre-pandemic rates.
- There remain diverging conditions in major industrial subsectors. The continued weakness in residential construction has been a negative for cement and crude steel – which contracted by 4.0% yoy and 1.8% yoy respectively. In contrast, the production of motor vehicles rose by 8.5% yoy and electronics by 4.8% yoy.
- China's major manufacturing surveys have exhibited differing trends at various times over the past year – in part reflecting a greater degree of volatility in the private sector Caixin PMI. That said, this trend was not evident in October, with both surveys converging at a mildly negative 49.5 points – from 50.6 points for the Caixin PMI and 50.2 points for the official NBS PMI.
- Both surveys showed a slowing trend for manufacturing production, while trends in domestic new orders differed – with expansion in the Caixin survey and contraction in the NBS measure. New export orders remained negative in both surveys, consistent with the weakening global environment.

Sources: Macrobond, NAB Economics

Investment

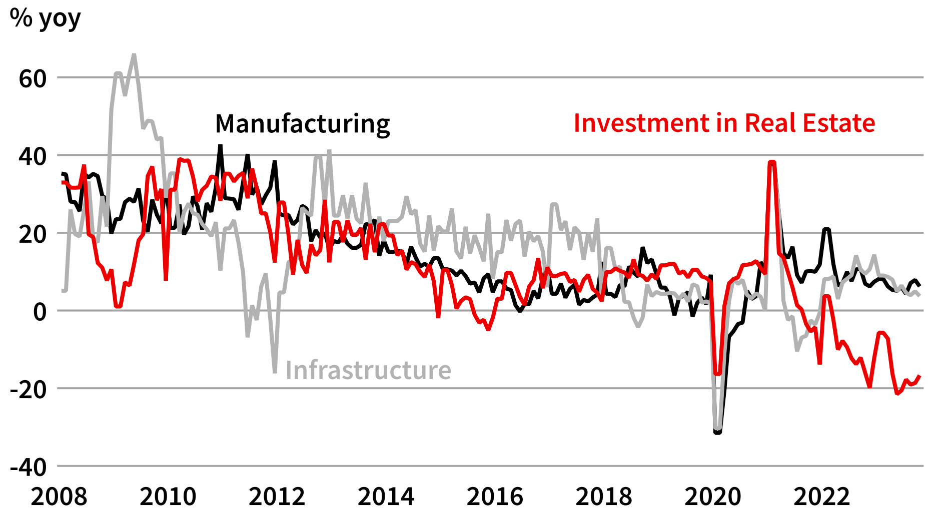
Fixed asset investment growth

Real investment growth slowed in October



Fixed asset investment by industry

Real estate remains the key drag on investment growth



Sources: Macrobond, NAB Economics

- China's nominal fixed asset investment grew more slowly in October – increasing by 1.3% yoy (down from 2.5% yoy in September). The cost of investment goods – which is influenced by factory gate prices – continues to contract in year-on-year terms, meaning that our estimate of real investment growth was 1.8% yoy in October (down from 2.9% yoy previously).

- There remains a sizeable disparity between growth in nominal investment by state-owned enterprises (SOEs) and private sector firms. SOE investment rose by 3.1% yoy in October – its slowest rate of expansion since December 2021 – while private sector investment edged up by 0.1% yoy.

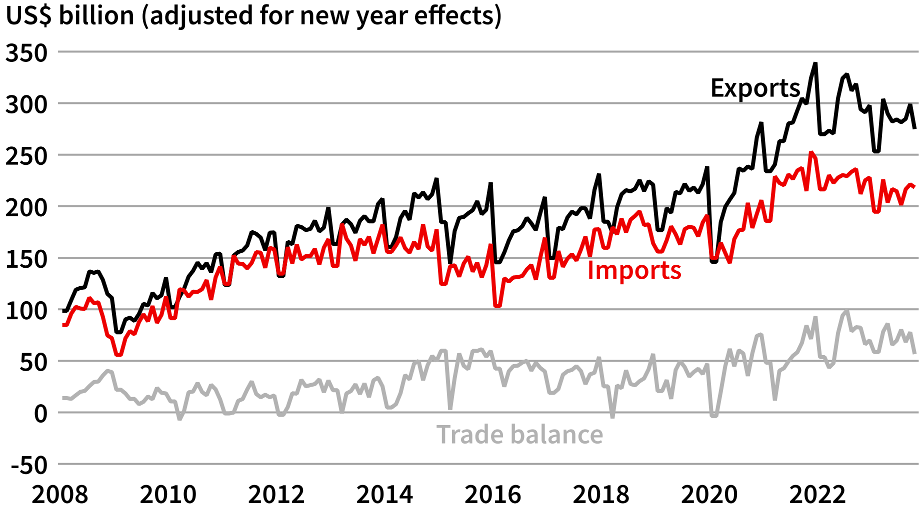
- Spokespeople from the NBS have previously attributed the difference between SOE and private investment to weakness in the real estate sector. Real estate investment fell by 16.7% yoy in October (compared with a 18.7% yoy fall in September). Activity in the real estate sector remains weak – new residential construction starts fell by 20.2% yoy while residential sales dropped by 21.0% yoy.

- In contrast, nominal investment in both manufacturing and infrastructure continue to grow – increasing by 6.2% yoy and 3.7% yoy respectively in October. The expansion of government bond issuance in recent months may support more rapid infrastructure growth in the near term.

International trade – trade balance and imports

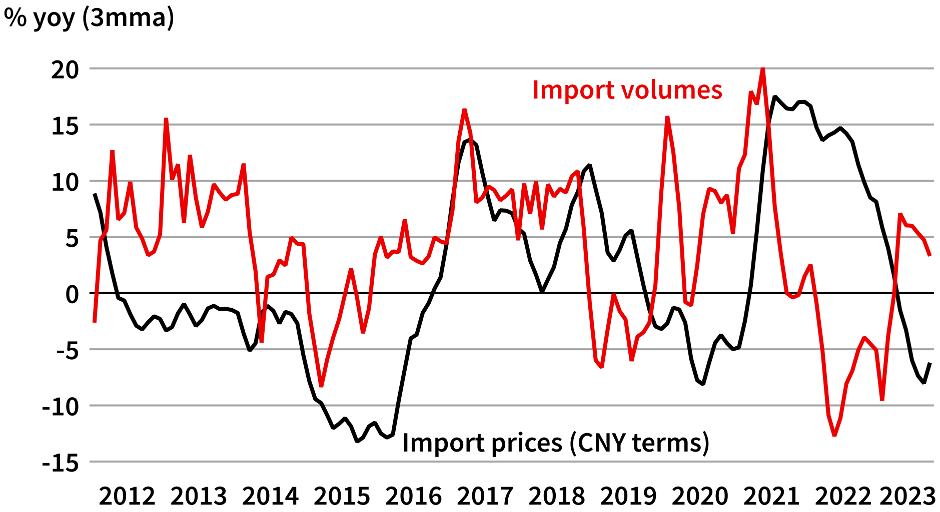
China's trade balance

Drop in export values drove trade surplus lower in October



Import volumes and prices

Falling import values in 2023 have been price driven



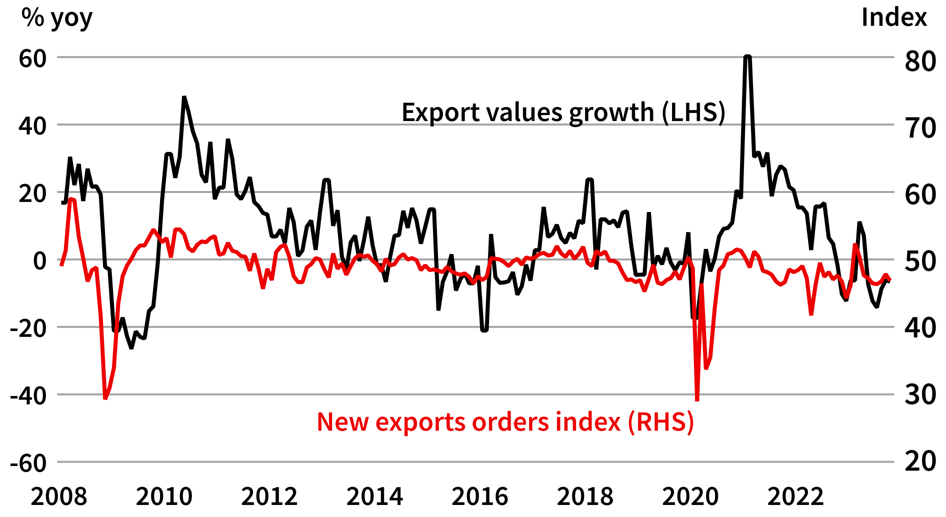
- China's trade surplus was somewhat narrower in October – totalling US$56.5 billion (down from US$77.8 billion in September) – with this outcome reflecting an easing in export values.
- China's rolling twelve month trade surplus with the United States edged lower in October – down to US$336.6 billion (from US$340.0 billion in the twelve months to September). While the rolling surplus has fallen from a peak of US$439.7 billion in July 2022, it remains marginally above the peaks prior to the US-China trade war (US$330.8 billion in June 2019).
- China's imports totalled US$218.3 billion in October, marginally down from the US$221.3 billion in September. This represented an increase of 3.0% yoy – the first year-on-year increase in import values since August 2022.
- The key driver of declining import values across much of 2023 has been falling prices, with import volumes rising in year-on-year terms since February 2023. Global commodity prices can be used as a proxy for China's import prices, and the RBA Index of Commodity Prices (when converted to RMB terms) fell by 13.7% yoy in October – which implies a sizeable increase in export volumes (in excess of 10% yoy). It is worth noting that October 2022 was impacted by a wave of COVID-19.
- Energy prices were a key driver of the declines in import prices evident across much of 2023, however this cycle may be close to its end – with global oil prices in mid-November around the same levels as a year ago and other energy commodities slightly lower. In October, the commodities that saw the largest price falls in year-on-year terms were fertilisers, paper pulp, LPG and other gases and grains.

Sources: Macrobond, NAB Economics

International trade – exports

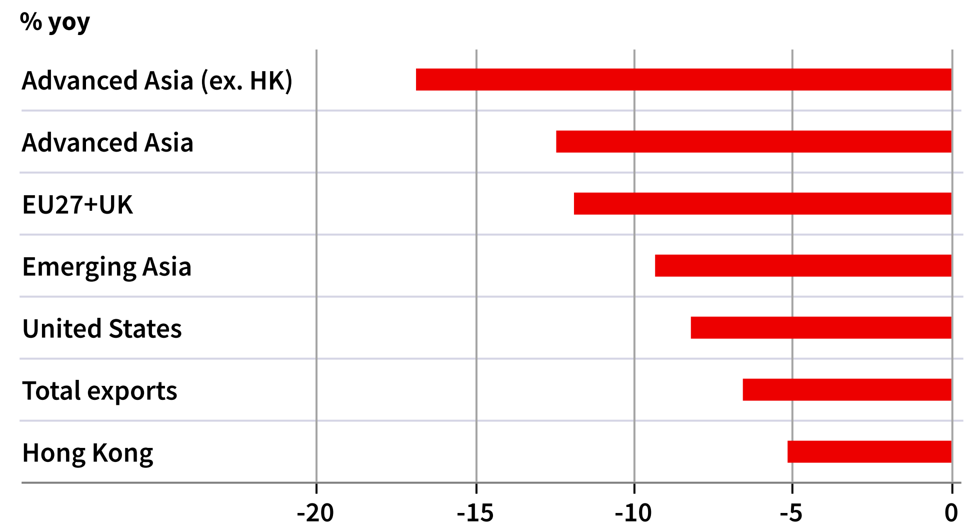
Export value and new export orders

Values continue to fall; new export orders still weak



Exports to major trading partners

Advanced Asia and European markets saw the largest falls



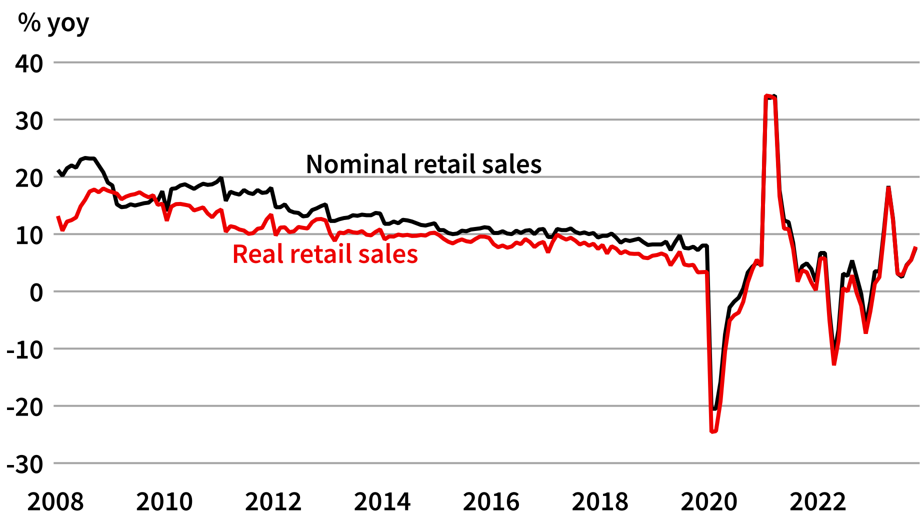
Sources: Macrobond, NAB Economics

- The value of China's exports fell in October – down to US$274.8 billion (from US$299.1 billion previously). In year-on-year terms, this represented a decline of 6.5%.
- The new export orders measure in the NBS PMI survey remained in negative territory – dipping to 46.8 points in October (compared with 47.8 points previously). Despite this trend, recent months have shown that export volumes have risen in year-on-year terms, with steep falls in export prices driving the declines in overall values.
- Continuing the trend that has become increasingly evident across 2023, exports to China's major trading partners grew more slowly than the overall total – declining by 10.7% yoy in October. This reflects an increasing shift in trade towards other markets – most notably Russia, where exports rose by 17.2% yoy.
- The steepest declines in exports were to advanced Asian economies (down by 12.4% yoy) and the European Union-27 + the United Kingdom (which fell by 11.9% yoy). If Hong Kong – which has had considerable distortions in historical trade data due to capital flows being disguised as trade activity – is excluded, advanced Asian exports fell by 16.8% yoy.
- Exports fell a little more modestly for Emerging Asia and the United States – down by 9.3% yoy and 8.2% yoy respectively.

Retail sales and inflation

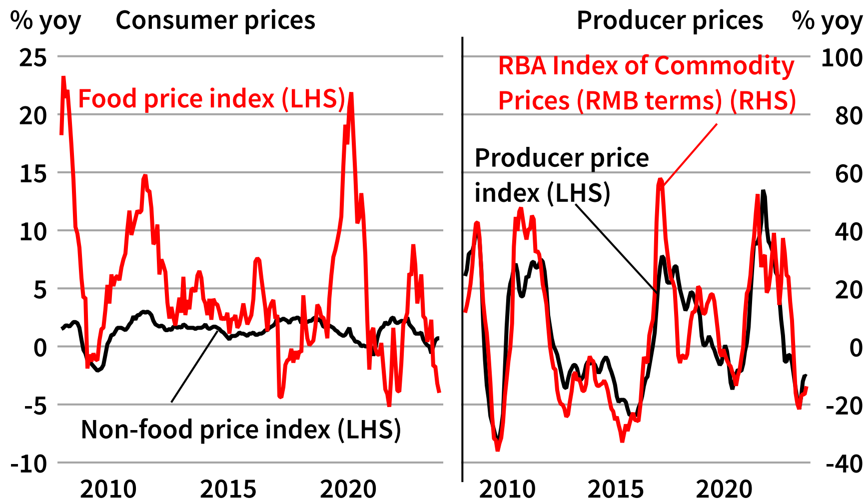
Retail sales growth

Sales growth picked up in October but may reflect base effects



Consumer and producer prices

Pork drives consumer prices back to deflationary territory



Sources: Macrobond, NAB Economics

- Growth in nominal retail sales accelerated in October – increasing by 7.6% yoy (compared with 5.5% yoy in September. When deflated by consumer prices, real retail sales grew by 7.8% yoy (also up from 5.5% yoy previously).

- We have noted in recent months that the extreme volatility of sales data during the COVID-19 pandemic makes it difficult to interpret the direction of these trends. Real retail sales in October were around 12.7% above the same month in 2019, compared with 10.8% increase in September and 7.3% increase in August. The pickup may reflect the impact of the Golden Week holidays at the start of the month – which were negatively impacted in 2022 by COVID-19 restrictions – resulting in a boost from base effects.

- Consumer prices returned to deflationary territory in October, with the headline consumer price index contracting by 0.2% yoy. Once again, food prices were the main driver of this trend, declining by 4.0% yoy (from -3.2% yoy in September). Pork has had a major influence on overall food prices in recent years, and this remains the case with pork prices plunging by 30.1% yoy in October. Prices for fresh vegetables were also lower – down by 3.8% yoy – while fresh fruit was up by 2.2% yoy.

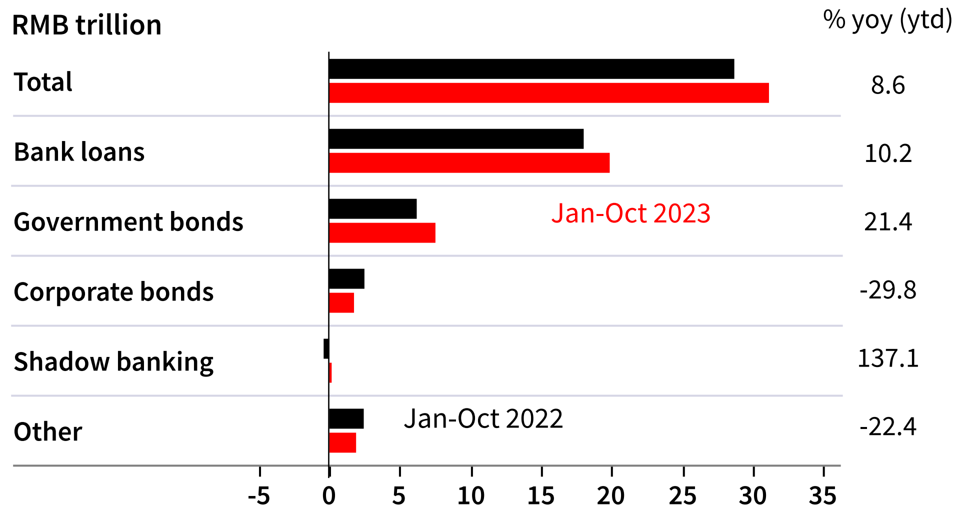
- In contrast, non-food prices rose by 0.7% yoy – with the rate of increase unchanged from September. Vehicle fuel prices had kept non-food inflation subdued since early 2023, however the recent uptick in global oil prices saw these prices rise by 1.8% yoy in October, compared with a 1.1% yoy fall previously.

- Producer prices have been falling since October 2022, with prices down by 2.6% yoy in October (from 2.5% yoy in September). Producer prices have long had a close relationship to global commodity prices – with the RBA Index of Commodity Prices (when converted into RMB terms) falling by 13.7% yoy in October – however this weakness may also reflect softness in both domestic and export demand.

Credit conditions

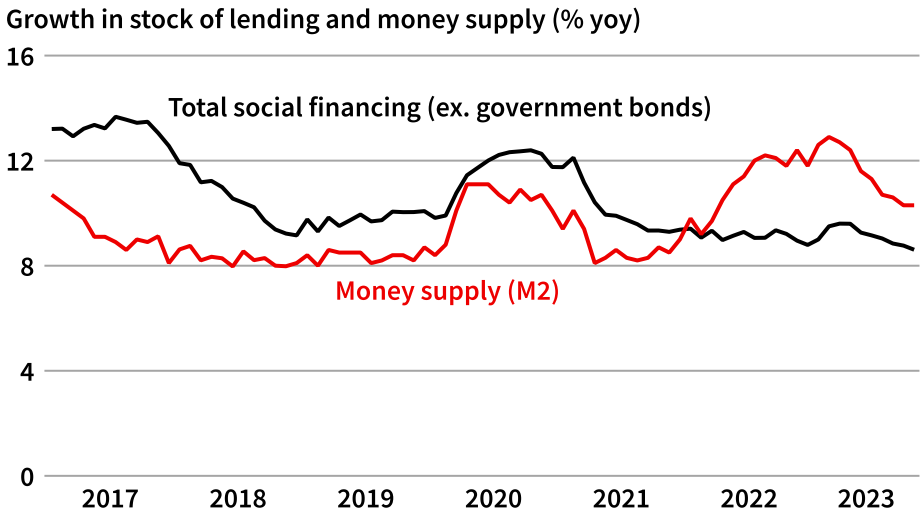
New credit issuance

Government bonds return non-bank lending to growth



Monetary policy

Additional liquidity unlikely to boost loan demand



Sources: Macrobond, NAB Economics

- October saw a continuation of the recent acceleration in new credit issuance. In the first ten months of 2023, new issuance increased by 8.6% yoy, compared with a 1.3% yoy increase in the first seven months – meaning that in the past three months, new credit issuance rose by 31.4% yoy. The key driver of the increase over this period has been government bonds – surging by 228% yoy between August and October. In contrast, bank lending rose by just 4.3% yoy over this period.

- In the first ten months of 2023, bank lending accounted for the largest share of total lending – around 64% – with bank loans increasing by 10.2% yoy to total RMB 19.9 trillion. However, the growth in bank lending has slowed substantially from its peak in April.

- Having contracted earlier in the year, non-bank lending rose by 5.7% yoy in the first ten months, driven by the rapid acceleration in government bond issuance in recent months. In contrast, corporate bond issuance has shrunk – down by 29.8% yoy.

- The People's Bank of China (PBoC) left its medium term lending facility (MLF) rate unchanged in November. The MLF is the basis for bids from commercial banks used to determine the Loan Prime Rate (China's primary policy rate). That said, the PBoC provided additional funding to financial markets, over and above the MLF loans that were expiring this month to expand liquidity. At a high level, we don't view this as being particularly significant – there was no shortage of funds available for lending, rather demand for loans (particularly in the real estate sector and among private firms more generally) has been weak, and this move will do nothing to address this.

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