NAB Group Economics

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China's economy at a glance
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Key points

China confirms an unchanged growth target for 2024 but headwinds will make it much harder to reach

- China's National People's Congress in March confirmed the widely expected unchanged growth target of "around 5%" for 2024. A lack of positive base effects this year, the likely ongoing softness in domestic demand (due in part to a lack of demand-side policy support), further falls in the property sector and limited growth potential via exports will make this a very challenging goal. Our forecasts are unchanged this month – we expect China to grow by 4.5% in 2024 and 4.8% in 2025.

- A range of indicators were stronger than market expectations in the first two months of 2024 – with industrial production, fixed asset investment and retail sales (albeit only marginally for the latter) stronger than the Reuters poll. That said, volatility in early 2023, the result of the Omicron wave of COVID-19 and the abandonment of zero-COVID policies in late 2022, mean that year-on-year growth rates do not necessarily provide the clearest signal.

- While nominal fixed asset investment rose by 4.2% yoy in January-February, the real estate sector remains a constraint on growth. Investment in real estate contracted by 13.4% yoy in January-February. Residential construction starts have continued to fall – down 24.2% yoy in February – with the total floor space (in square metres) at its lowest levels since late 2005.

- China's trade surplus narrowed somewhat across January-February, averaging US$62.6 billion (compared with US$75.3 billion in December 2023) – albeit this remains relatively high by historical standards. Exports slowed more rapidly than imports when compared with December, with these downturns being typical season patterns.

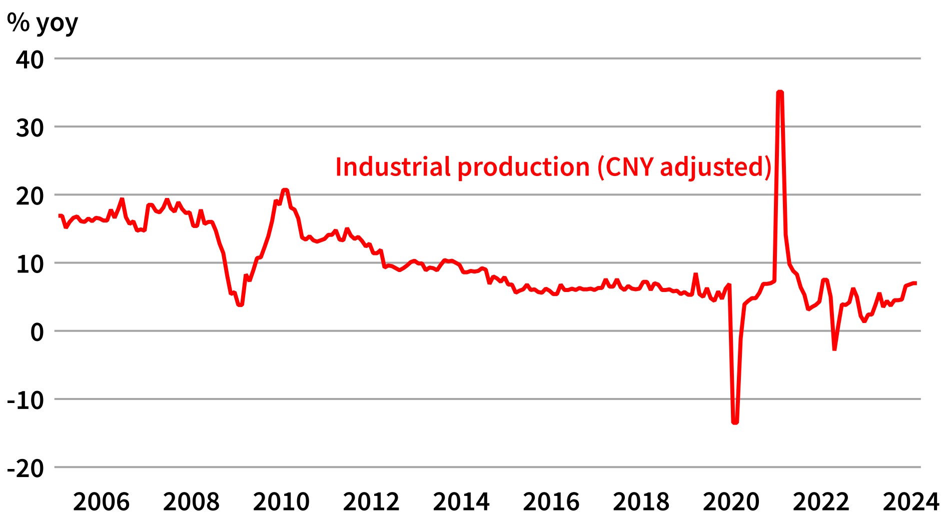
- There was some monetary policy easing in February, with the five-year Loan Prime Rate – a benchmark used to price mortgages – cut by 25 basis points to 3.95%. The one-year rate (used mainly for business lending) was left unchanged. Given the deep declines in property sector activity since the implementation of the Three Red Lines policy, a relatively modest cut to mortgage rates is unlikely to spur a recovery in the sector.

- Growth in outstanding bank lending has trended down since April 2023, indicative of weak loan demand, with financial markets having plenty of liquidity following cuts to the Reserve Requirement Ratio across 2023 and early 2024. This limited demand constrains the ability of monetary policy easing to boost economic activity.

Industrial production

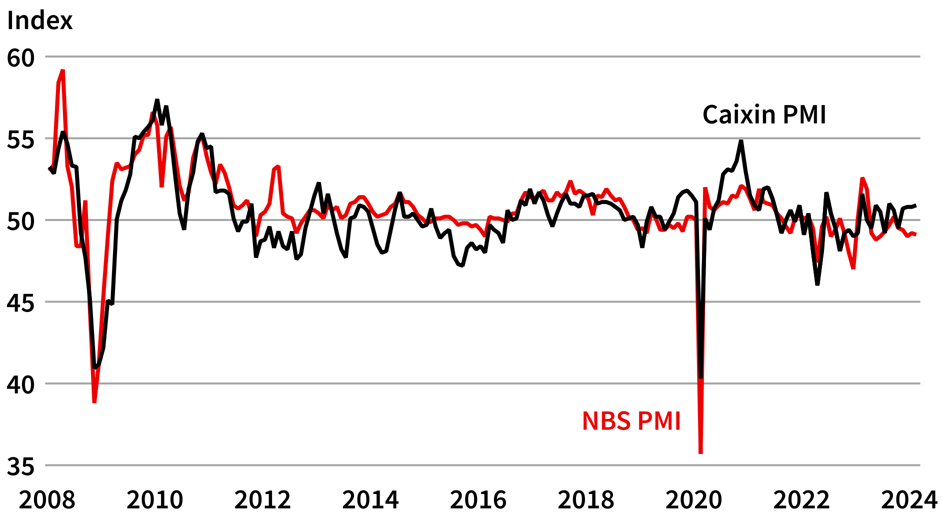
Industrial production growth

Output growth edged up in Jan-Feb, likely boosted by base effects



Manufacturing PMI surveys

Wide disparity between manufacturing surveys persist



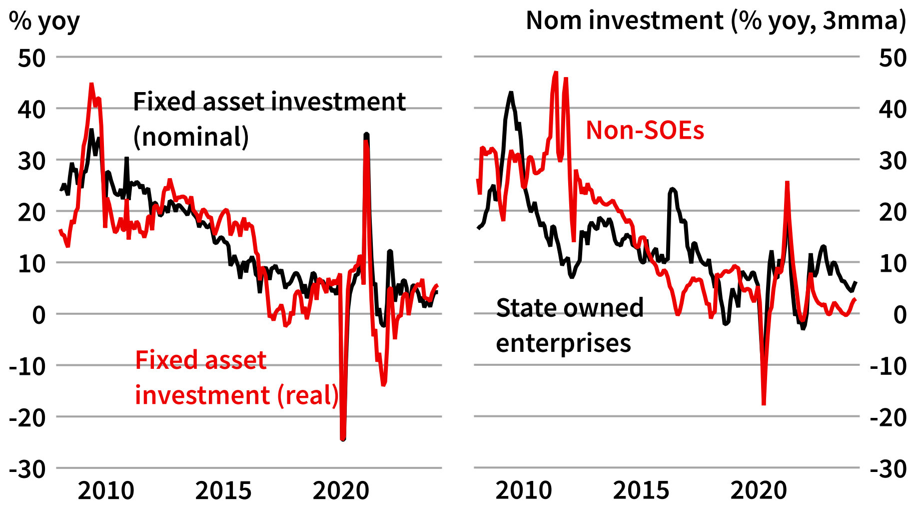
Sources: Macrobond, NAB Economics

- China's average industrial production growth accelerated slightly across January and February, increasing by 7.0% yoy (compared with 6.8% yoy in December). This was the fastest pace of increase since January-February 2022 (when output rose by 7.5% yoy). It is likely that the early 2024 increase was somewhat inflated by base effects – with China's economy adjusting to the reopening from COVID-19 restrictions in early 2023.
- There was considerable disparity in growth rates within major industrial subsectors. Electronics manufacturing surged – increasing by 14.6% yoy in the first two months, while motor vehicle production rose by 4.4% yoy. In contrast, crude steel output rose by just 1.6% yoy and cement production contracted by 1.6% yoy.
- Since November 2023, there has been a sizeable margin between China's two major manufacturing surveys, and this trend persisted in February. The private sector Caixin PMI has remained positive – at 50.9 points (up from 50.8 points in both January 2024 and December 2023). In contrast, the official NBS PMI has remained negative, at 49.1 points (from 49.2 points previously).
- In part, this may reflect the differing composition of firms in each survey – it is generally understood that the NBS survey has a larger share of large state-owned manufacturers (more focused on heavy industry), whereas the Caixin survey has more respondents from the private and SME sectors.
- Domestic demand remains a key factor explaining the divergence between these surveys. New orders in the NBS survey have been negative since October 2023. In contrast, this measure has been positive in the Caixin survey – with the difference even more stark for new export orders in the two surveys.

Investment

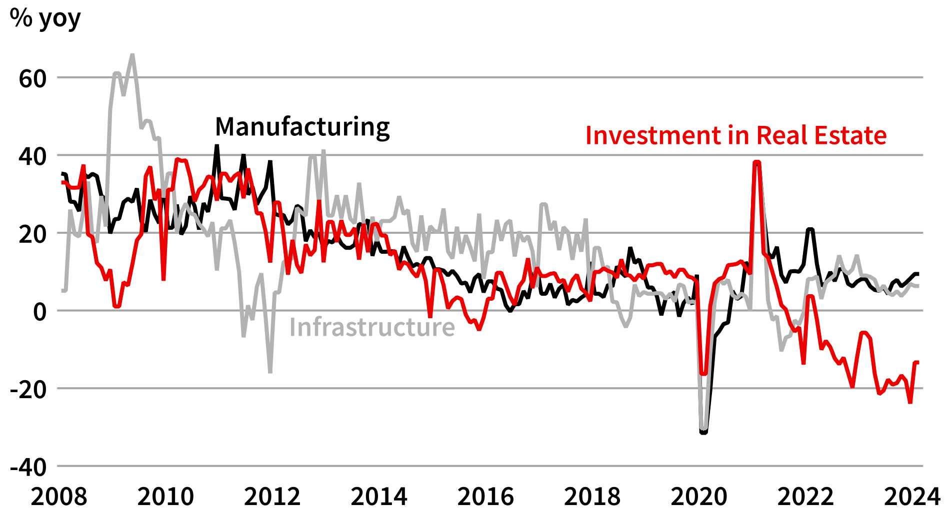
Fixed asset investment growth

Real investment growth continued to edge up from Q3 23 lows



Fixed asset investment by industry

Real estate continues to restrict total investment growth



Sources: Macrobond, NAB Economics

- In nominal terms, fixed asset investment growth accelerated slightly in January-February, increasing by 4.2% yoy (compared with 4.0% yoy in December). The price of investment goods has continued to fall (in line with declines in producer prices), boosting the real rate of growth to 5.5% yoy in January-February (compared with 4.8% yoy in December).

- Nominal investment remains driven by large state-owned enterprises (SOEs), which rose by 7.3% yoy in January-February (compared with 5.3% yoy in December). In contrast, private investment rose by 2.3% yoy (down from 3.3% yoy previously) – albeit this was stronger than the very weak trends across most of 2023. Some of the weakness in private investment may be attributable to the weakness in the property sector.

- There remains a wide disparity in investment trends by sector – where real estate investment continues to contract, having trended lower since late 2021. Investment in real estate contracted by 13.4% yoy in January-February.

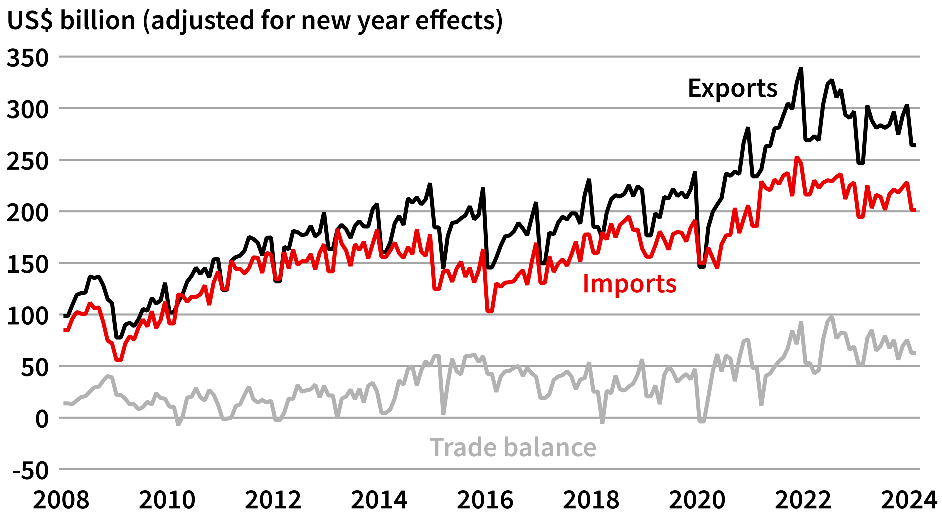
- Residential construction starts have continued to fall – down 24.2% yoy in February – with the total floor space (in square metres) at its lowest levels since late 2005. Similarly, residential sales fell further – down 27.3% yoy in February.

- In contrast, investment in both manufacturing and infrastructure continues to increase at a relatively strong pace – up by 9.3% yoy and 6.3% yoy respectively in January-February.

International trade – trade balance and imports

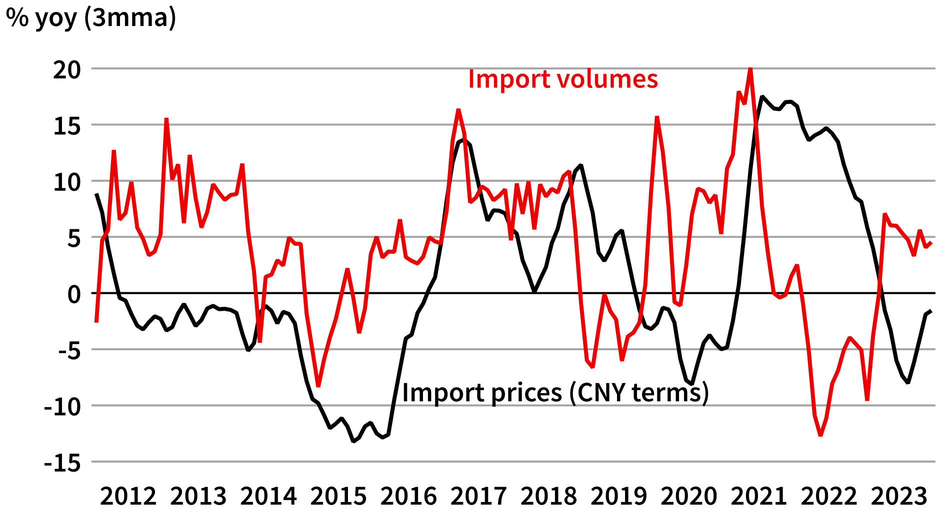
China's trade balance

Surplus narrows as exports ease more than imports in early 2024



Import volumes and prices

Falling prices the key driver of softer import values in 2023



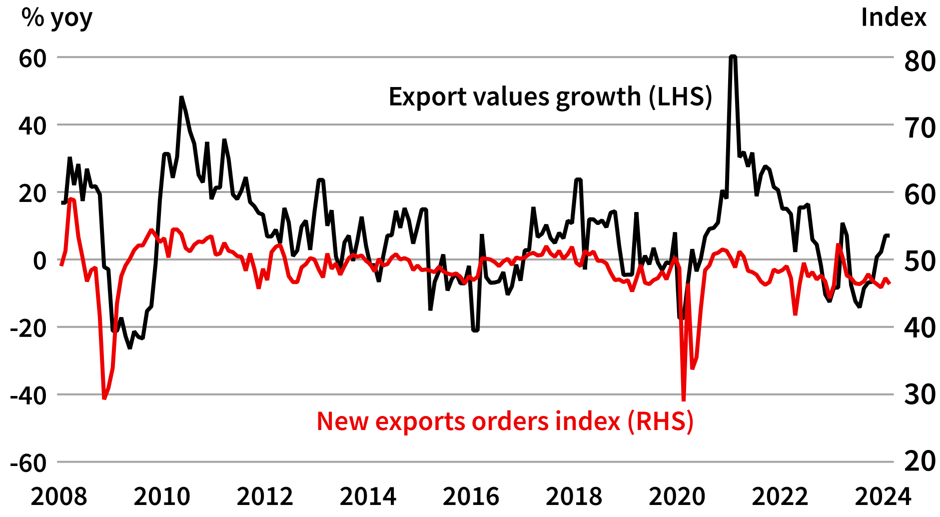
Sources: Macrobond, NAB Economics

- China's trade surplus narrowed somewhat across January-February, averaging US$62.6 billion (compared with US$75.3 billion in December 2023) – albeit this remains relatively high by historical standards. Exports slowed more rapidly than imports when compared with December, with these downturns being typical season patterns.
- On a rolling twelve-month basis, China's trade surplus to the United States edged up in February, totalling US$345.9 billion in February, up from US$339.9 billion in December 2023. The trade surplus has contracted from its all-time peak in July 2022 (at US$439.7 billion) however it remains marginally above the levels recorded around the start of the US-China trade war.
- China's imports averaged US$201.4 billion in January and February, down from US$228.3 billion in December 2023. In year-on-year terms, this represented an increase of 3.5%.
- Notwithstanding the increase in early 2024, the value of China's imports has generally trended lower year-on-year over the past eighteen months. Declines in import prices have explained much of the trend over this period, with import volumes increasing by 3.6% yoy in December 2023 (the most recent data available). In part this reflects declines in global commodity prices – the RBA Index of Commodity Prices fell by 7.7% yoy in February, having fallen in year-on-year terms each month for the past year.
- That said, a closer look at major commodity imports shows some divergent trends. In RMB terms, there remain relatively steep year-on-year price declines for some key energy commodities (particularly coal and LPG & other gases – which includes LNG), while there was less price effect for crude oil and refined petroleum products. In contrast, prices rose sharply for iron ore and fertilisers.

International trade – exports

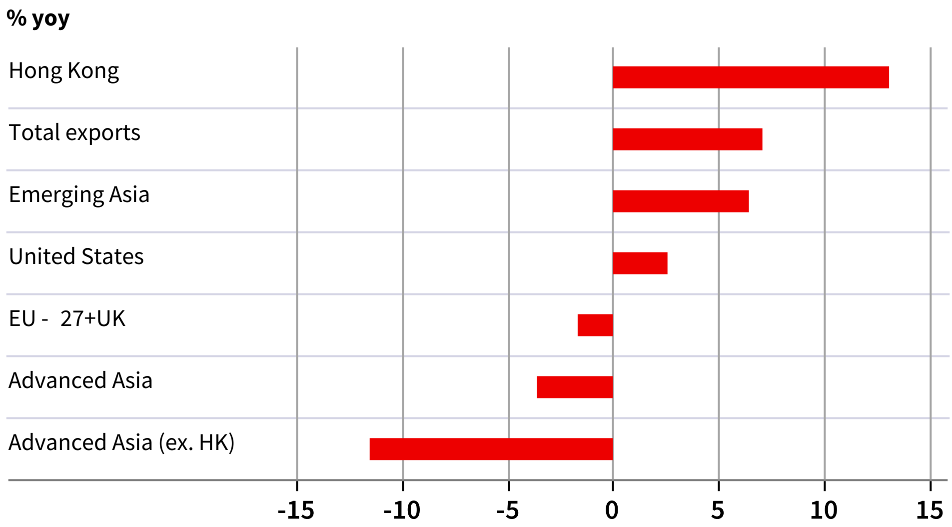
Export value and new export orders

Exports yoy in Jan-Feb, but new orders remain negative



Exports to major trading partners

Highly divergent export trends to major partners in early 2024



Sources: Macrobond, NAB Economics

- China's exports averaged US$264.0 billion in January and February (down from US$303.6 billion in December). That said, in year-on-year terms, export values rose by 7.1% - the largest increase since a brief spike in March 2023. Despite this uptick, the new export orders measure in the NBS PMI survey has remained firmly in negative territory – at 46.3 points (from 47.2 points in January).

- Export values contracted for much of 2023 and this was largely driven by falling export prices – driven in part by steep declines in factory gate prices. In contrast, export volumes rose strongly through to the end of 2023 – increasing by around 13.3% yoy in December.

- Trends in exports to China's major trading partners were divergent in the first two months of 2024, with exports to this group increasing by just 0.4% yoy (well below the overall increase in exports). This reflects rapid expansion elsewhere – most notably to the Russian Federation (with exports up by 11.8% yoy) and other former Soviet Union states.

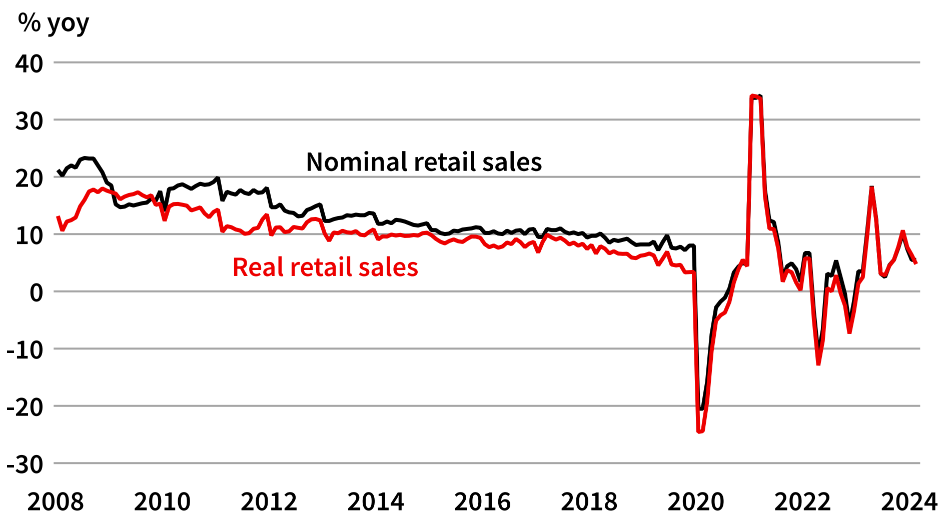
- Exports to the United States rose modestly – up by 2.6% yoy in January-February, while exports to emerging Asian markets rose by 6.4% yoy (with the latter primarily driven by a 17.4% yoy increase in exports to Vietnam).

- In contrast, exports to the European Union-27 + the United Kingdom fell by 1.7% yoy, while exports to advanced Asian economies fell by 3.6% yoy (or 11.5% yoy when exports to Hong Kong are excluded).

Retail sales and inflation

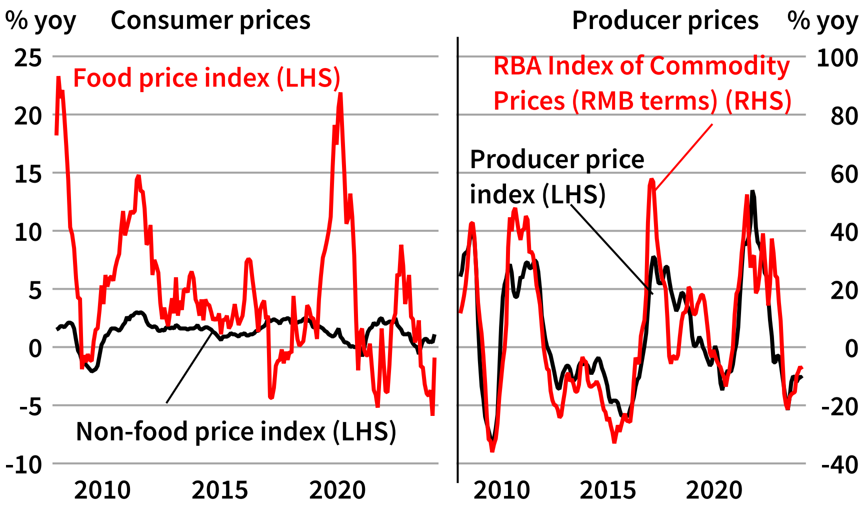
Retail sales growth

Weaker base effects explain some of the slowing in sales growth



Consumer and producer prices

Deflationary pressures weaker in Jan-Feb than mid-2023



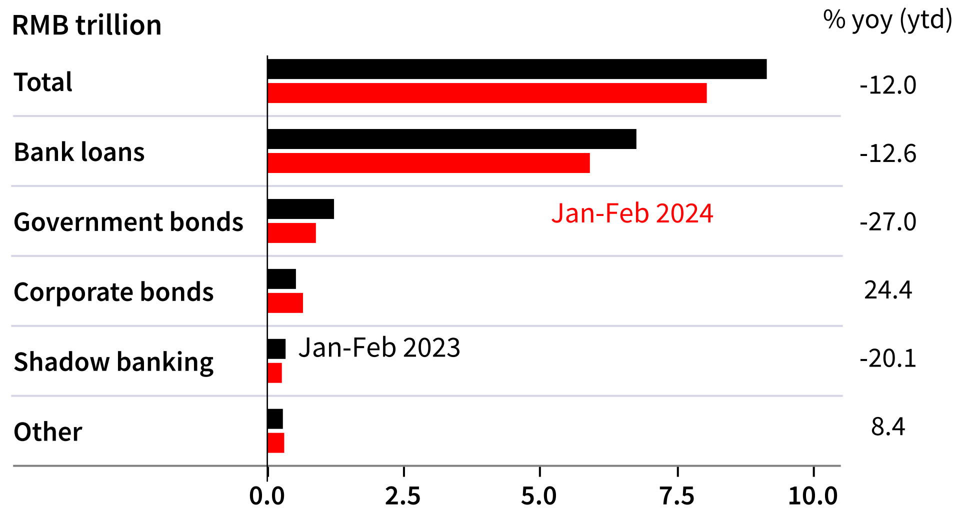
Sources: Macrobond, NAB Economics

- Nominal growth in retail sales continued to slow at the start of 2024, increasing by 5.5% yoy in January-February, compared with 7.4% yoy in December and 10.1% yoy in November. That said, these earlier months were much more heavily impacted by COVID-19 restrictions. Deflating these measures using consumer prices, real sales slowed from 7.7% yoy in December to 5.6% yoy in January-February.
- Although China publishes monthly inflation data for January and February, the timing of Chinese new year makes these data highly volatile. Smoothing across the two months, consumer prices were marginally lower year-on-year – down by 0.1% (compared with -0.3% yoy in December).
- Food prices have been the main deflationary driver since mid-2023, falling by an average of 3.6% yoy across January and February (compared with a 3.7% yoy decline in December 2023). Pork prices have been a major driver of the food deflation, however prices of fresh fruits also fell considerably in January and February.
- In contrast, non-food prices rose by 0.6% yoy across January and February, compared with 0.5% yoy in December. Non-food price growth has accelerated somewhat since mid-2023, as the downward pressure of falling global oil prices – which flowed through to lower vehicle fuel prices – gradually eroded.
- Producer price deflation has eased somewhat in recent months. Producer prices fell by an average of 2.7% yoy across January and February – essentially unchanged from December 2023, but considerable weaker than mid-2023. In a large part, this reflects the slowing falls in global commodity prices – with the RBA Index of Commodity Prices down by 7.7% yoy (in RMB terms) in February, compared with a 21% fall in June 2023). However, weaker export demand in advanced economies has also limited the capacity of producers to maintain export prices in recent months.

Credit conditions

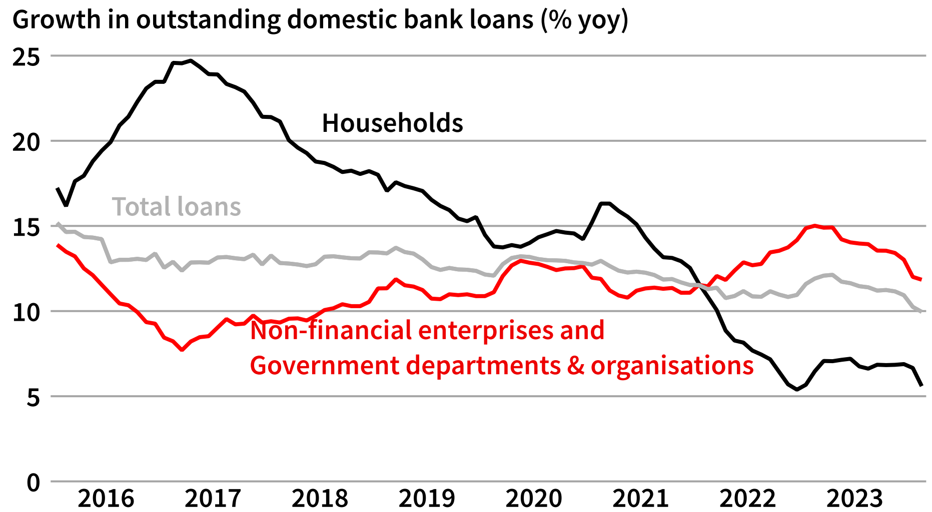
New credit issuance

Lending contracted in the first two months of 2024



Bank lending

Shrinking growth in outstanding loans points to weak loan demand



Sources: Macrobond, NAB Economics

- China's new credit issuance contracted in the first two months of 2024 – down by 12.0% yoy to RMB 8.1 trillion. Bank lending accounted for just under three-quarters of the total over this period, but shrank by 12.6% yoy to RMB 5.9 trillion. In contrast, non-bank lending fell marginally more modestly, down by 10.3% yoy.
- Within the non-bank sector, there were wide variations in lending growth over the first two months. Government bonds, which had been a major source of credit growth in 2023 (particularly in the second half), contracted by 27.0% yoy. In contrast, corporate bonds shrunk last year, but were up 24.4% in January-February.
- There was some monetary policy easing in February, with the five-year Loan Prime Rate – a benchmark used to price mortgages – cut by 25 basis points to 3.95%. The one-year rate (used mainly for business lending) was left unchanged. Given the deep declines in property sector activity since the implementation of the Three Red Lines policy, a relatively modest cut to mortgage rates is unlikely to spur a recovery in the sector.
- Growth in outstanding bank lending has trended down since April 2023, indicative of weak loan demand, with financial markets having plenty of liquidity following cuts to the Reserve Requirement Ratio across 2023 and early 2024. This limited demand constrains the ability of monetary policy easing to boost economic activity.

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