NAB Group Economics

China's economy at a glance

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Author: Gerard Burg, Senior Economist - International

Key points

China's growth beat expectations in Q1, but big question marks around its sustainability

- According to China's latest national accounts data, its economy expanded by 5.3% yoy in Q1 2024 (compared with a 5.2% yoy increase in Q4 2023) – stronger than markets had anticipated. Disaggregated data showed some diverging trends – growth was driven by the manufacturing and construction sectors (despite the downturn in building construction) – while services growth eased. Combined with weak retail and lending data, these point to ongoing weakness in domestic demand, with the manufacturing sector increasingly reliant on exports – leading to growing trade tensions. As a result of the questionable sustainability of this growth, our forecasts are unchanged – we expect China to miss its growth target this year, expanding by 4.5% in 2024 and 4.8% in 2025.

- China's industrial production growth slowed in March – increasing by 4.5% yoy (down from an average increase of 7.0% yoy in January and February). It is worth noting that the January-February increase was likely inflated by base effects, due to China's economy adjusting to the end of zero-COVID policies in late 2022.

- Real fixed asset investment growth picked up in March – increasing by 6.0% yoy (compared with an average increase of 5.4% yoy in January and February). The wide disparity in investment trends by individual sectors has continued – with real estate investment continuing to plunge, while manufacturing investment has accelerated.

- China's trade surplus was narrower in March than the average across January and February, as an uptick in imports outpaced the increase in exports. The surplus totalled US$58.6 billion (down from an average of US$62.6 billion across the first two months). It is worth noting that by historical standards, this surplus remains comparatively high. Data on export prices and volumes is lagged by a month. On average, export volumes rose by around 20% yoy across January and February, while export prices fell by over 8% yoy.

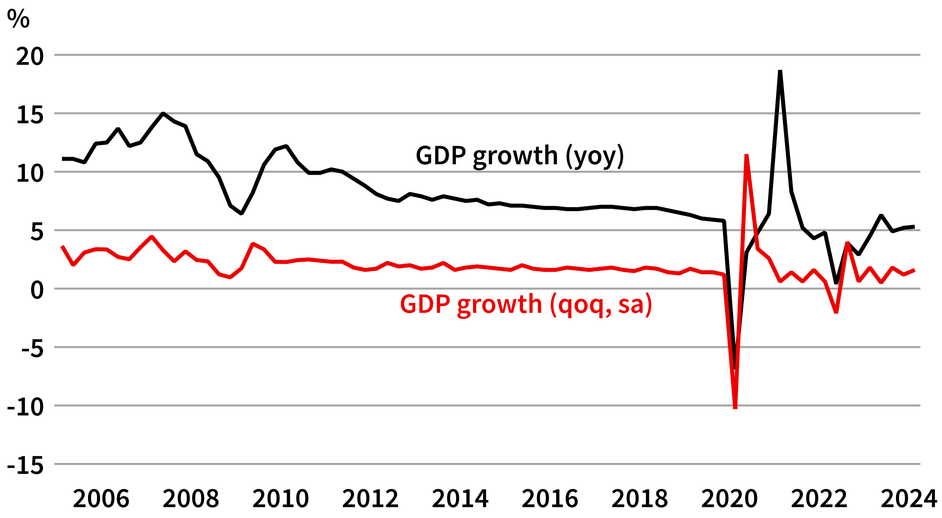
- Real growth in retail sales was relatively subdued in March, increasing by 3.0% yoy (compared with an average increase of 5.6% yoy in January and February). This indicator does not point to any notable improvement in domestic demand.

- The People's Bank of China (PBoC) has kept its policy rate unchanged since mid-2023. In an environment of such weak loan demand, it is unclear that any rate cuts, or cuts to banks reserve requirement ratios, would have a meaningful stimulatory effect.

Gross domestic product

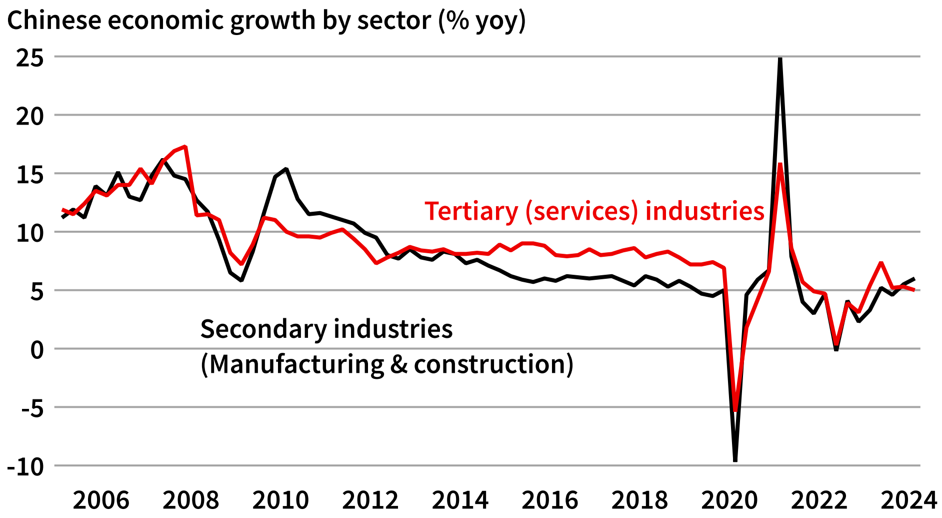
China's economic growth

China's growth beat market expectations in Q1



Economic growth by industry

YOY growth in the secondary sector accelerated



Sources: Macrobond, NAB Economics

- According to China's latest national accounts data, its economy expanded by 5.3% yoy in the first quarter of 2024 (compared with a 5.2% yoy increase in Q4 2023). In seasonally adjusted quarter-on-quarter terms, they reported a 1.6% increase. In both cases, these outcomes were stronger than markets had anticipated – the Reuters poll had year-on-year growth at 4.6%.

- Digging into growth by industry category shows some diverging trends. The key driver of the economy in Q1 2024 was the secondary sector – which grew by 6.0% yoy (up from 5.5% yoy in Q4). This sector comprises manufacturing and construction, and while disaggregated data is not yet available, both non-residential and residential construction have been contracting for some time, although fiscal spending likely boosted infrastructure construction. Industrial production grew strongly.

- In contrast, year-on-year growth in services slowed – down to 5.0% yoy (from 5.3% yoy in Q4). Combined with weak retail and lending data, these point to ongoing weakness in domestic demand, with the manufacturing sector increasingly reliant on exports – leading to growing trade tensions.

- Despite the stronger than expected growth in Q1, our forecast for the full year remains unchanged, and we anticipate weaker growth across the remainder of 2024. Chinese authorities are yet to implement any substantial policies to address weakness in domestic consumption, and the export led growth appears unsustainable. We expect growth to fall short of this year's target ("around 5%"), and remain below this level going forward.

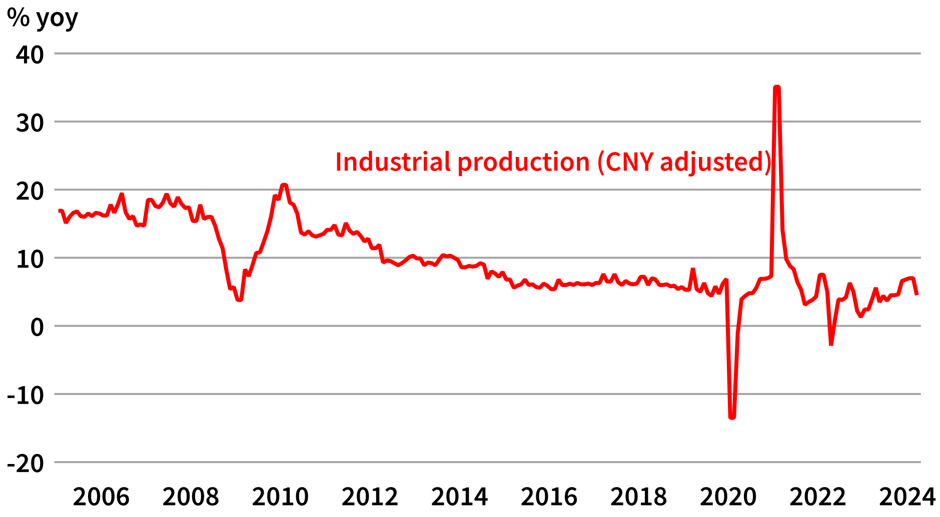
NAB China GDP forecasts

%	2023	2024	2025	2026
GDP	5.2	4.5	4.8	4.5

Industrial production

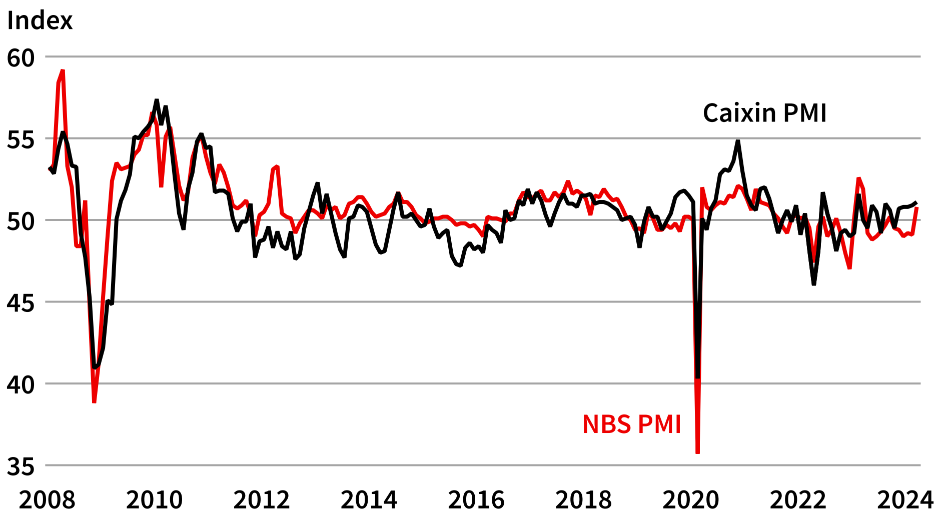
Industrial production growth

Industrial output slowed from inflated growth rates in Jan-Feb



Manufacturing PMI surveys

Surge in official measure narrows the gap between China's surveys



Sources: Macrobond, NAB Economics

- China's industrial production growth slowed in March – increasing by 4.5% yoy (down from an average increase of 7.0% yoy in January and February). It is worth noting that the January-February increase was likely inflated by base effects, due to China's economy adjusting to the end of zero-COVID policies in late 2022.

- There was considerably disparity in growth rates between major industrial subsectors. Output of electronics was considerably stronger – up by 10.6% yoy – while motor vehicle production also rose – increasing by 6.5% yoy. In contrast, production of construction-related materials was much weaker – with crude steel output falling by 7.8% yoy and cement production down 22.0% yoy.

- Following three months of wide disparity between China's two major manufacturing surveys, a sharp pickup in the NBS manufacturing survey saw these measures converge in March. The official NBS survey surged to 50.8 points (from 49.2 points in February). In contrast, the private sector Caixin manufacturing PMI edged up to 51.1 points (from 50.9 points previously).

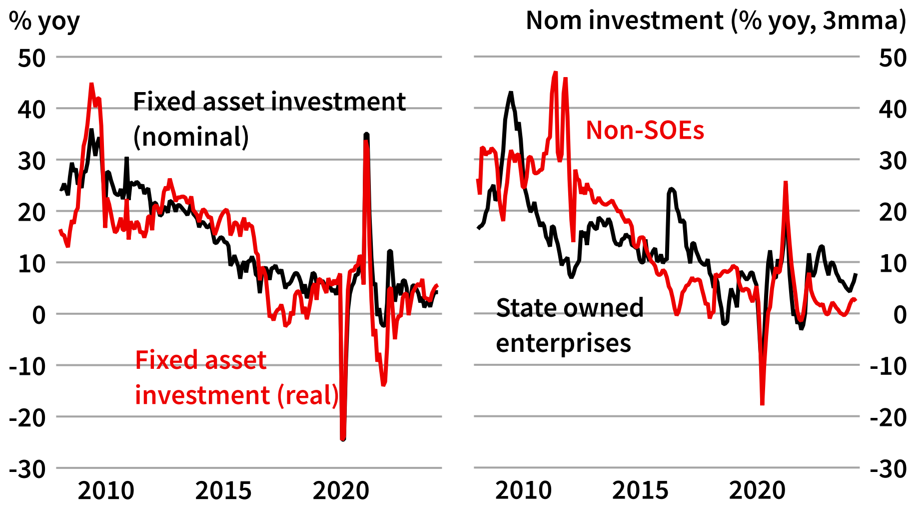
- Critical to the uptick in the NBS PMI was strengthening in both the production and new orders measures – both of which moved from negative to positive territory. These measures had been key contributors to the divergence between the NBS and Caixin PMIs (having already been positive in the latter survey).

- Similarly, new export orders also improved in both surveys – again recording positive readings. Recent months have seen an acceleration in China's export volumes, albeit this has come about by cuts in export prices. Given our forecasts for weaker global growth in 2024, we do not expect this trend to be sustainable.

Investment

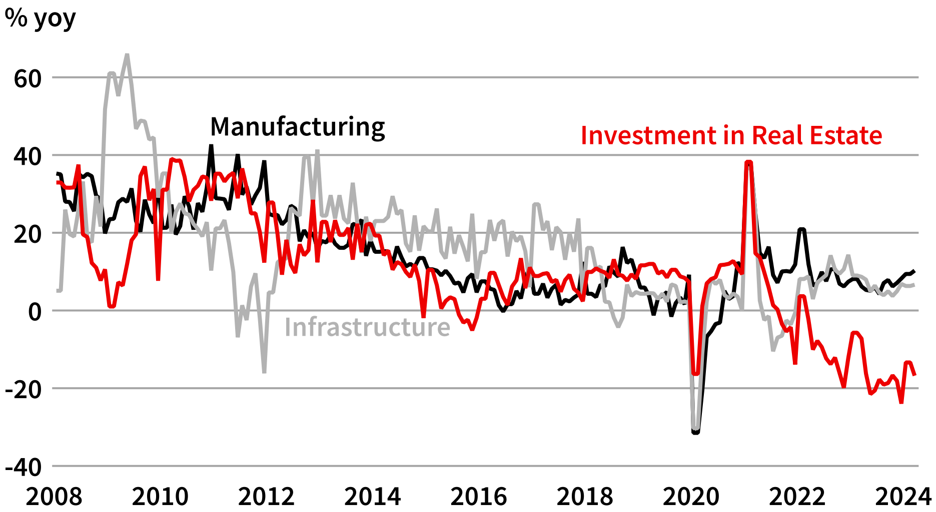
Fixed asset investment growth

SOEs continue to drive the growth in nominal investment



Fixed asset investment by industry

The slump in the real estate sector continues unabated



Sources: Macrobond, NAB Economics

- China's nominal fixed asset investment growth picked up in March – increasing by 4.7% yoy (compared with an average increase of 4.2% yoy in January and February). The continued decline in factory gate prices has lowered the cost of investment goods. This means a stronger real increase in investment – up by 6.0% yoy (compared with 5.4% yoy in January-February).

- Nominal investment continues to be driven by large state-owned enterprises (SOEs). In March, investment by SOEs rose by 8.2% yoy (up from an average of 7.3% yoy in the first two months). In contrast, private sector investment grew by 2.4% yoy (edging up from an average of 2.3% yoy in January-February). The National Bureau of Statistics has previously attributed the weakness in private investment in the downturn to the property sector.

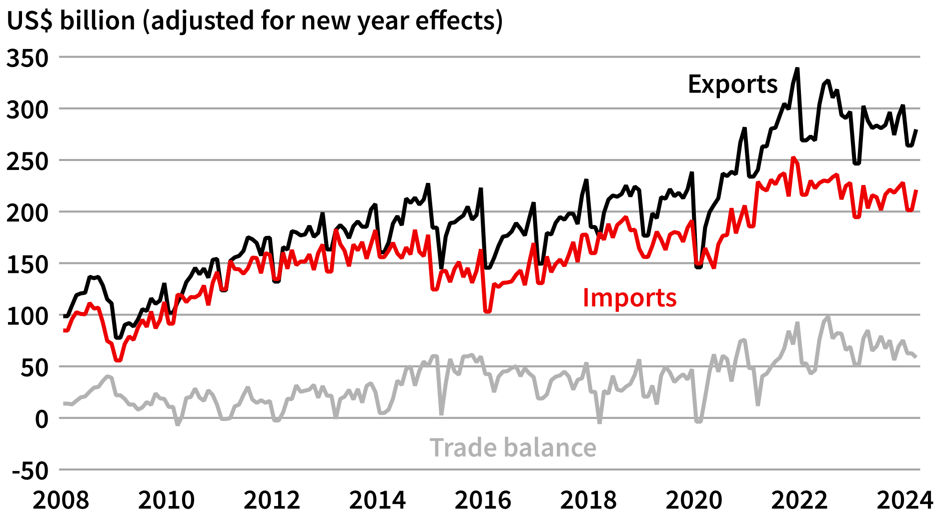
- The wide disparity in investment trends by individual sectors has continued. Investment in real estate has plunged since the implementation of the Three Red Lines policy, contracting by 16.8% yoy in March. Residential construction starts fell by 26.7% yoy in March, while sales fell by 27.1% yoy. There is no sign of a turn-around in this sector – indeed it may be a multi-year correction.

- In contrast, there remains strong growth in manufacturing investment – which rose by 10.3% yoy. Infrastructure also grew – albeit at a similar rate to the start of 2024 – up by 6.6% yoy, benefiting from government bond issuance in the second half of 2023.

International trade – trade balance and imports

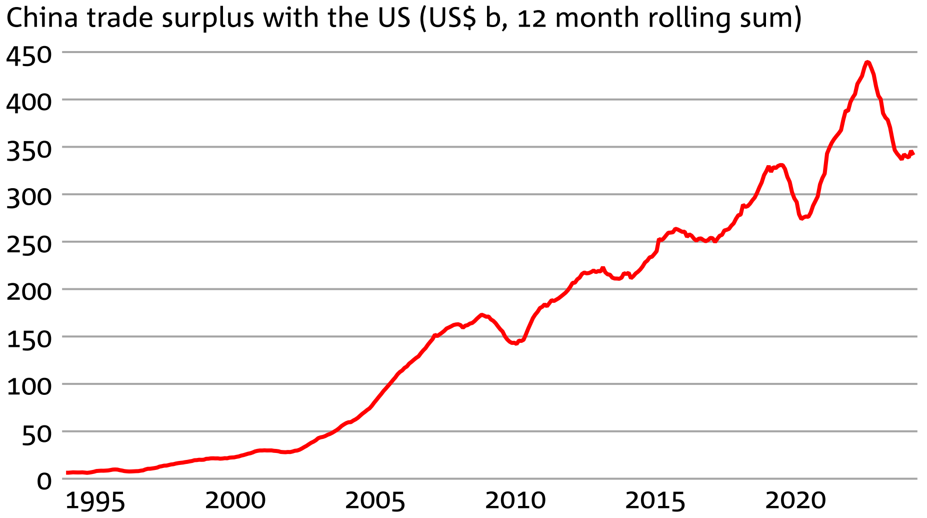
China's trade balance

Surplus slightly narrower in March but still comparatively high



China's trade surplus with the United States

While well off its peaks, China's rolling surplus has stabilised



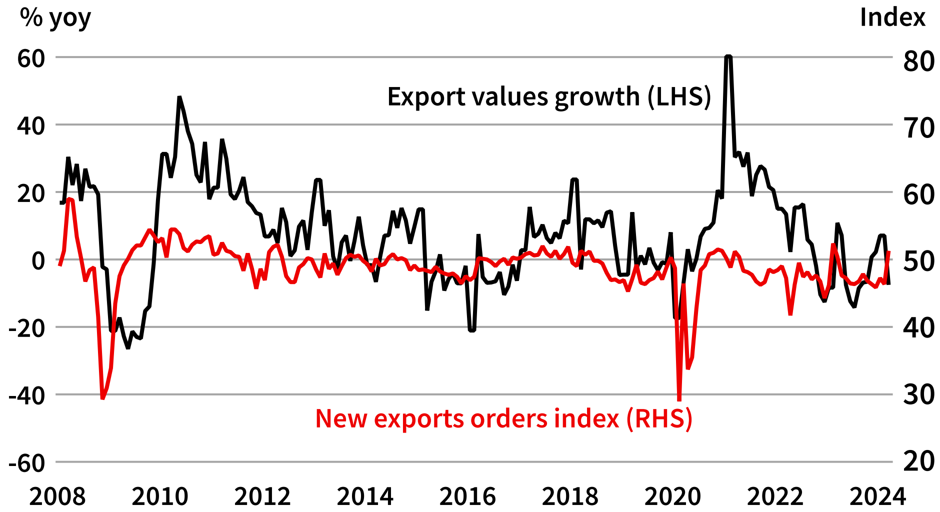
Sources: Macrobond, NAB Economics

- China's trade surplus was narrower in March than the average across January and February, as an uptick in imports outpaced the increase in exports. The surplus totalled US$58.6 billion (down from an average of US$62.6 billion across the first two months). It is worth noting that by historical standards, this surplus remains comparatively high.
- On a rolling twelve-month basis, China's trade surplus with the United States was marginally lower in March – at US$341 billion (compared with US$345.9 billion in February). While the trade surplus has retreated from an all-time high in July 2022 (of US$439.7 billion), it has essentially stabilised around the current level since August 2023. Trade tensions between China and the United States and European Union have risen in recent months, with the advanced economies accusing China of addressing its excess industrial capacity and weak domestic demand by dumping goods into global markets.
- China's imports totalled US$221.1 billion in March, up from an average of US$201.4 billion in January and February. Despite the monthly rise, imports fell in year-on-year terms – down by 1.9%.
- For much of 2023, China's import volumes grew strongly, benefiting from relatively strong declines in import prices. That said, in the past few months, the rate of decline of import prices has rapidly eroded. Much of the earlier declines were driven by energy prices – particularly oil related – though these prices have started to trend higher once again.

International trade – exports

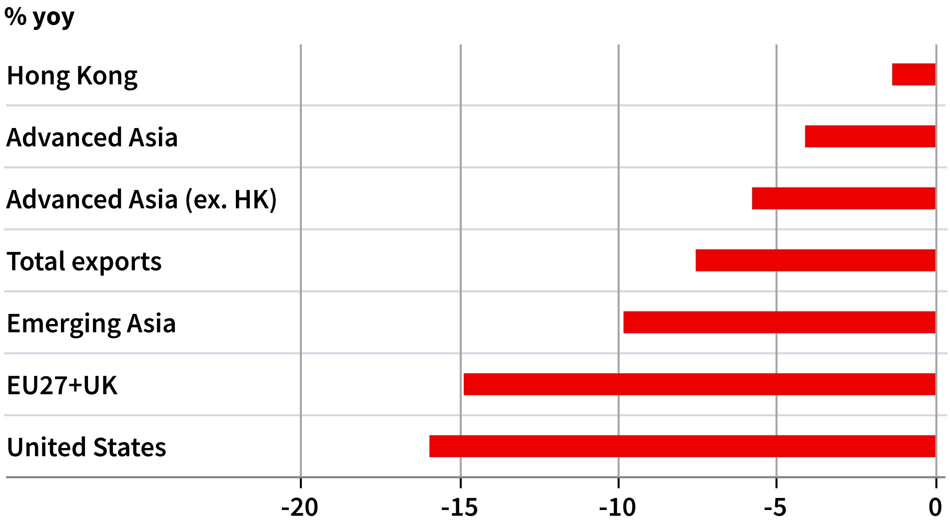
Export value and new export orders

Price falls driving values lower but orders higher



Exports to major trading partners

Export values fell for all major trading partners in March



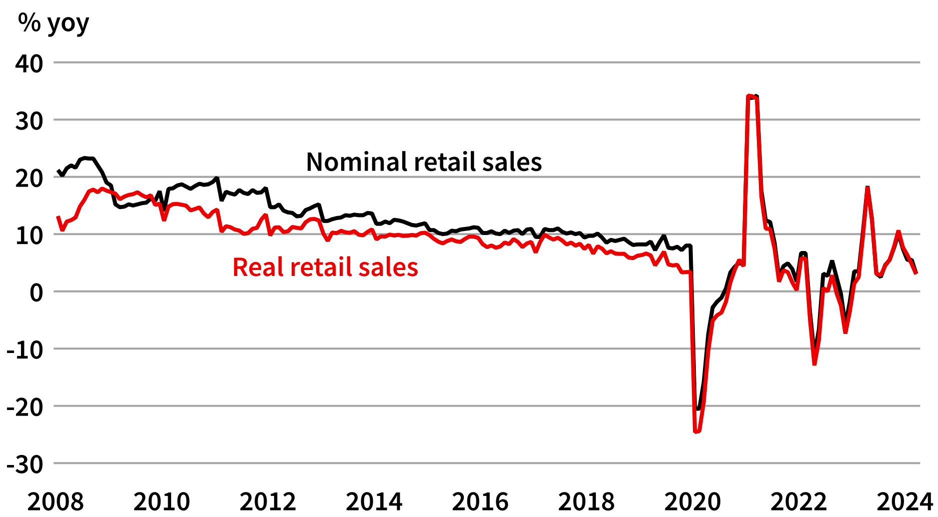
Sources: Macrobond, NAB Economics

- The value of China's exports totalled US$279.7 billion in March, up from an average of US$264.0 billion across January and February. However in year-on-year terms, export values fell by 7.5%. This reflects the sizeable falls in export prices over recent months, as Chinese producers have ramped up exports into a slowing global market.
- The new export orders measure in the NBS manufacturing PMI survey surged higher in March – up to 51.3 points – having been in negative territory between April 2023 and February 2024.
- Data on export prices and volumes is lagged by a month. On average, export volumes rose by around 20% yoy across January and February, while export prices fell by over 8% yoy.
- The value of exports fell across the board for China's major trading partners in March. The largest declines were recorded for the United States (where export values fell by 15.9% yoy) and the European Union-27 + the United Kingdom (down by 14.8% yoy). The declines were more modest in Asian markets, with exports to emerging Asia down by 9.8% yoy and advanced Asia falling by 4.1% yoy (albeit this increased to 5.8% when Hong Kong is excluded).
- Last year saw a massive ramp up in exports to Russia, however even the value of these exports fell substantially in March – falling by 15.7% yoy.

Retail sales and inflation

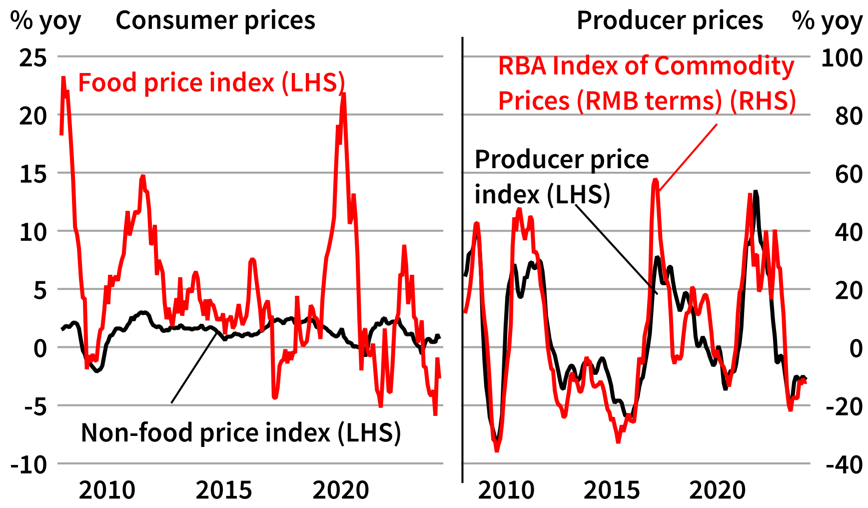
Retail sales growth

Real sales relatively subdued in March



Consumer and producer prices

Weak consumer price growth as factory gate prices fall again



- Nominal growth in retail sales was relatively subdued in March, increasing by 3.1% yoy (compared with an average increase of 5.5% yoy in January and February). Our estimate of real retail sales growth – using the consumer price index as the deflator – was 3.0% yoy in March, down from 5.6% yoy in the first two months. This indicator does not point to any notable improvement in domestic demand.

- China's consumer prices edged marginally higher in March – up by 0.1% yoy (compared with an average fall of 0.1% yoy in the first two months of 2024).

- Food prices have continued to fall, having been in negative territory since mid-2023. Food prices contracted by 2.7% yoy (compared with an average of 3.6% yoy across January-February). Pork prices were a major driver of lower food prices in 2023 – falling by double digit rates across the second half – although they eased by just 2.4% yoy in March. However, downward pressure on food prices has also come from lower prices for eggs, fresh fruits and fresh vegetables.

- Growth in non-food prices was marginally stronger – up by 0.7% yoy (from an average of 0.6% yoy in January & February). A major contributor to this uptick has been vehicle fuel prices, which have rising in line with trends in global oil markets.

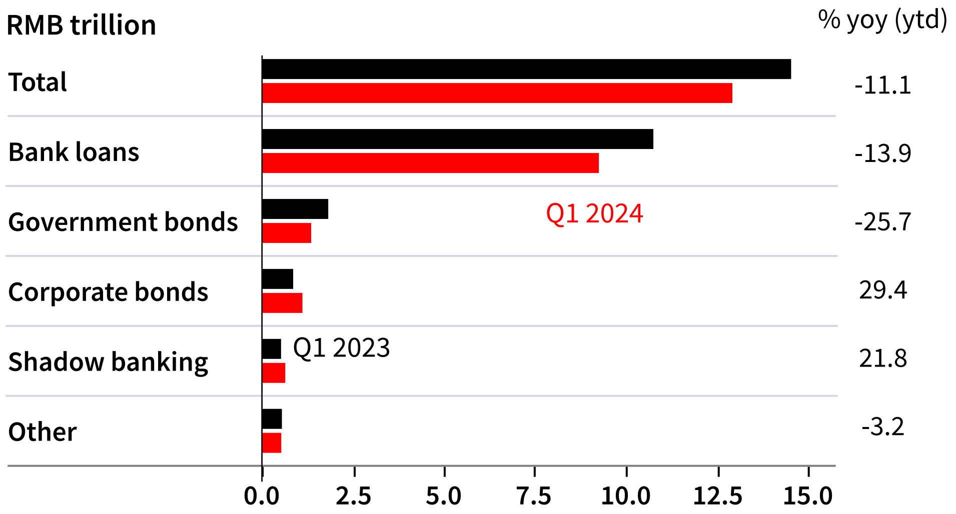
- China's producer prices fell once again in March – down by 2.8% yoy (compared with an average decline of 2.7% yoy in January and February). As measured by the RBA Index of Commodity Prices (converted into RMB terms), global commodity prices fell by 11.8% yoy in March – albeit there has been substantial divergence between individual markets – with steel inputs substantially lower, while base metals and oil have moved higher.

Sources: Macrobond, NAB Economics

Credit conditions

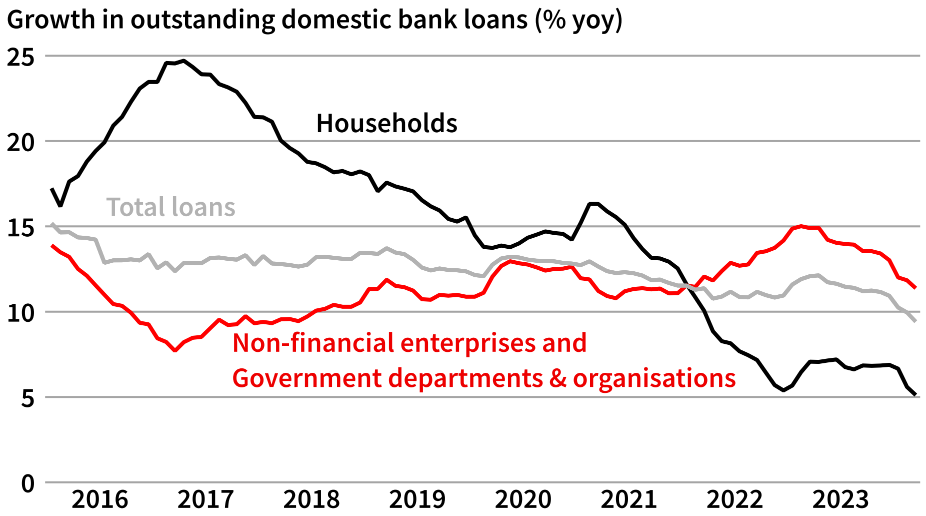
New credit issuance

Banks drove the drop in lending in Q1 2024



Bank lending

Slowing growth points to ongoing weakness in loan demand



- New credit issuance contracted in the first quarter of 2024, down by 11.1% yoy to RMB 12.9 trillion. While bank lending remains the dominant source of new credit (at almost 72% of the total), bank loans contracted slightly more rapidly – down by 13.9% yoy to RMB 9.3 billion. In contrast, the decline in non-bank lending was more modest – down by 3.1% yoy.

- There remains a wide divergence between different categories of non-bank credit. Government bonds were a key driver of growth in 2023, but they fell by 25.7% yoy in Q1. In contrast, corporate bond issuance was weak last year, but expanded by 29.4% in the first three months.

- At a fundamental level, the weakness in bank lending – despite authorities' efforts to encourage banks to lend – points to ongoing soft loan demand. Growth in outstanding loans to households fell its lowest on record (stretching back to the start of 2008), while growth in total lending slowed to its weakest rates since July 2005.

- The People's Bank of China (PBoC) has kept its policy rate unchanged since mid-2023. In an environment of such weak loan demand, it is unclear that any rate cuts, or cuts to banks reserve requirement ratios, would have a meaningful stimulatory effect.

Sources: Macrobond, NAB Economics

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

Lea Jurkovic
Economist – Agribusiness
+(61 0) 452 090 770

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

Thao Nguyen
Economist – Data & Analytics
+(61 0) 451 203 008

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

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

Global Markets Research

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