



# Research Institute

## China: Macro, Money & Policy

31 January 2023

6:37 minute read

#China

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#Monthly

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#Data indicators



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## Rebounding consumption to drive China's GDP growth to 5.5% in 2023

The country's rapid transition towards endemic living led to a substantial upward revision of our forecast.

### Key Takeaways

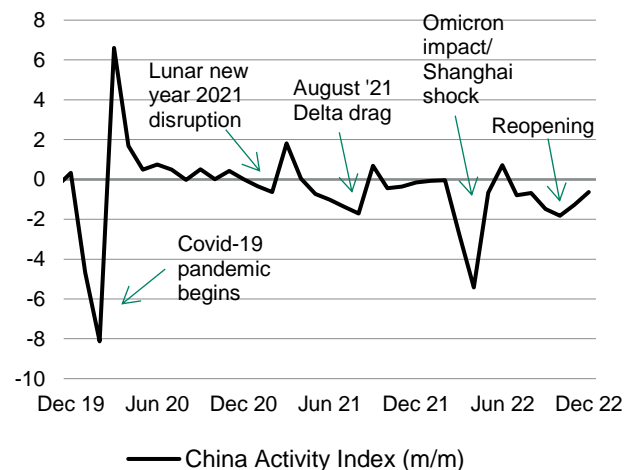
- Monthly data for December and high frequency data for January show that activity is picking up sharply.
- The rapid transition towards endemic living has led to a major upward revision to our growth forecast. We now expect GDP growth to reach 5.5% in 2023.
- The surge in Chinese bank deposits overstates the extent of “excess savings”, but one does not need to appeal to a deposits rundown to believe consumption can rebound. Returning to normal rates of consumption out of income should be enough for nominal consumption to rise by around 14% in 2023.
- If households tap the RMB 4.2tn buffer built up over the pandemic, annual consumption growth could reach 20%. But the potential for this to trigger stronger services inflation, or leak into foreign holidays could also temper the boost to real GDP.
- Policy rhetoric may have turned ‘pro-growth’, but it is unlikely that the authorities will really increase stimulus when the economy is rebounding.
- Our Chinese Financial Conditions Index has moved out of accommodative territory, while local governments are likely to dial back infrastructure spending to repair their fiscal positions.

### The China Activity Indicator backs up the picture of a fast transition towards endemic living

China's transition towards endemic living appears to be almost as fast as the abrupt policy pivot away from Zero Covid. Of course, with no official reporting on case numbers it is impossible to be sure how fast the virus has really been spreading. But the combination of government reports,

surveys and ‘anecdotal’ points to an exceptionally rapid wave, likely peaking towards the end of December.

**Figure 1: The China Activity Indicator (CAI) points to a reopening bounce beginning in December, but does not imply Q4 GDP avoided a contraction**



Source: abrdrn, Refinitiv, Haver. (January 2022)

In many ways the Covid wave has become a moot point; households and governments are behaving as if it is over, with households making use of their new-found freedoms and no sign of authorities reaching for restrictions. Additionally, there is little sign that the end of ‘Zero’ is causing major disruption to manufacturing, implying any impact on supply chains should also pass quickly.

Data to December typically came out better than expected, implying an earlier start to the recovery than we had thought.



Retail sales surprised by only registering a 1.8% y/y fall - well above consensus expectations of -9% y/y - while we estimate that volumes expanded 2.4% m/m.

We have now entered the seasonal data black hole, so will need to wait until mid-March before receiving any more hard monthly data to gauge the pace of activity.

**High frequency data confirms an ongoing bounce back through January, with scope for ongoing recovery**

The Ministry of Culture and Tourism reported that the number of domestic visitors over the Lunar New Year golden week (21<sup>st</sup> to 27<sup>th</sup> January) increased to almost 90% of pre-pandemic levels.

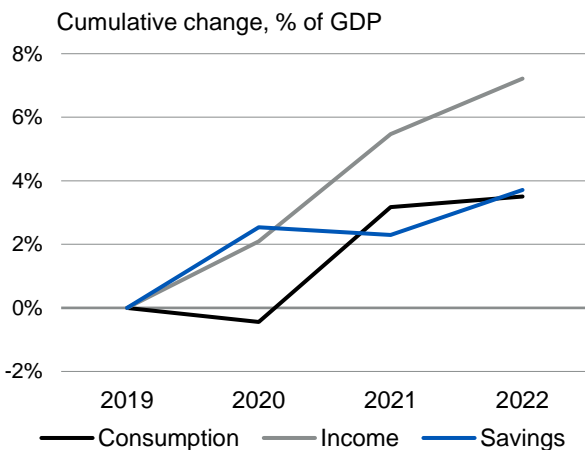
Official travel statistics imply a less forceful rebound - with the Ministry of Transport estimating total passenger numbers returned to 53% of 2019 levels - but this appears to miss a rise in private travel by car. The Baidu migration index actually points to stronger inter-city travel than 2019.

Some other metrics also outperformed pre-pandemic norms: Box Office revenue over the golden week was the second highest on record; while catering businesses also rebounded to slightly above 2019 levels, according to the China Cuisine Association.

**China's faster transition has led us to revise up our 2023 GDP growth forecast to 5.5%**

Previously we had expected that China's transition to endemic living would proceed more slowly and cautiously, with the authorities reaching for modest restrictions to alleviate pressure on healthcare and households mindful of the impact on the under-vaccinated elderly population.

**Figure 2: A normalisation of the savings/consumption rate should drive a large consumption rebound, even without tapping 'excess savings'**



Source: aRI, Haver (January 2022)

The latest data imply a much faster, more 'V'-shaped, path for Chinese activity driven primarily by a rebound in consumption and services activity, which more than offsets drags from net trade, the real estate sector and fiscal retrenchment.

The large stockpile of bank deposits grossly overstates the extent of "excess savings" that households are likely to tap. But households have saved around RMB 4.2tn (3.7% of GDP) of their disposable income (see Figure 2).

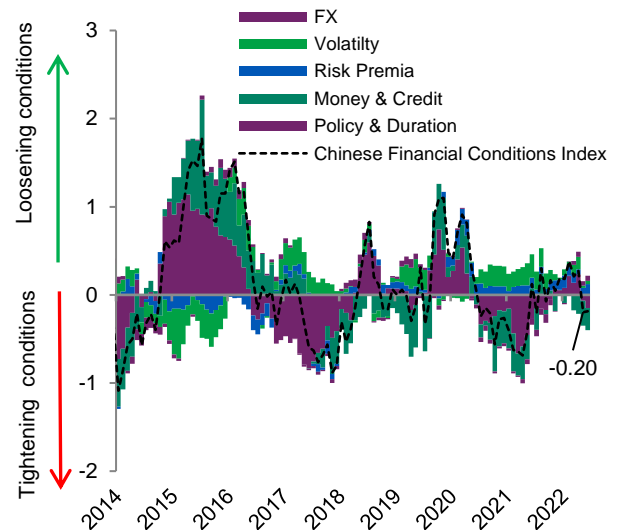
Moreover, one does not need to appeal to this as a major driver: simply returning the saving rate (and correspondingly the consumption rate) to prior norms, should be enough for nominal consumption to rise by around 14% in 2023.

Households tapping savings could push nominal consumption growth to 20%, although the skewed distribution of savings towards higher earners tempers this upside, as does the potential for stronger services inflation to curtail real consumption by more than we expect.

**Consumption should be strong enough to offset fading policy support and a tougher external environment**

Policy rhetoric may have turned 'pro-growth', but it is unlikely that the authorities will really increase stimulus when the economy is rebounding.

**Figure 3: Financial conditions are no longer accommodative**



Source: aRI, Bloomberg, Refinitiv, Haver (January 2022)

Indeed, our Chinese Financial Conditions Index (CFCI), remained tight in December (see Figure 3), reflecting the rebound-induced impact of higher yields and also the credit impulse pushing further into negative territory.



Of course, as we have noted before, the true shift in financial conditions needs to be considered relative to real equilibrium interest rates ( $r^*$ ), and many of our key variables are taken as spreads to  $r^*$  in the modelling. It is possible that rising yields actually capture a sudden rise in  $r^*$ , which should imply that financial conditions have not in fact tightened by as much as the CFCI implies. It is too early though to know whether our estimates of  $r^*$  will indeed rise.

Other strands of policy do not seem particularly supportive. Recent announcements of further support for the real estate sector seem consistent with our prior assumption that new starts would recover over the course of H1 2023. And local authorities are still likely to dial back infrastructure spending to repair their fiscal holes, netting off some of the private sector recovery in construction.

The end of 'Zero Covid' will at least provide some reprieve for local government finances - Guangdong province alone spent over RMB 70bn (\$10bn) controlling Covid, for example – but the end of testing and containment will also detract slightly from GDP as health spending drops.

Judging the overall fiscal stance in China remains a fraught affair, but averaging through estimates from Goldman Sachs and JPMorgan suggest that the augmented fiscal deficit could tighten by 2pp in 2023.

Finally, the net trade drag will intensify as China rebounds. Initially this should help support domestic manufacturing as demand for consumption goods rises, but it will be tough to escape the downturn in global goods demand. Moreover, the return of international travel – which was close to non-existent over the past 3 years – is another route for excess savings to flow.

#### Our latest China forecasts:

- **Activity:** Official Q4 GDP defied consensus expectations of a 1.1% q/q contraction to post zero growth. Reflecting the weaker steer from the the distribution of indicators and the CAI we did not upgrade the aRI GDP estimate on a one-for-one basis. We do however expect both our aRI measure of GDP and the official NBS series to rebound notably, with the latter more likely to break 6% than the former. Risks from a sub-par real estate recovery and a larger withdrawal of policy support remain.
- **Inflation:** Unlike the rest of the world, inflation has not been a problem for China to date. Re-opening is likely to drive services (and core) inflation notably higher, but China will benefit from the ongoing recovery in global value chains and the relative weakness within DMs. We condition on a US recession that leads to a marked fall in oil prices in H2 2023.
- **Monetary policy:** The People's Bank of China (PBOC) is highly unlikely to ease further as the economy rebounds. The US recession is however likely to cause an abrupt change of tack, leading to resumption of policy easing across a range of instruments which drives financial conditions back into accommodative territory.

	2021	2022	2023	2024
aRI GDP (%)	7.8%	2.0%	5.5%	4.8%
Official GDP (%)	8.9%	3.1%	5.9%	5.0%
CPI (%)	1.0%	2.0%	2.0%	2.0%
Policy Rate* (%)	2.2%	2.0%	1.8%	1.7%

\*7 day reverse repo. Broader policy stance captured by CFCI.

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GB-060223-187468-9

