



Global Macro Research - Insight

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#China

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#Growth

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#Data indicators

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China sees strong GDP growth but March data are weak

Strong growth in Q1 combined with data revisions imply that the authorities' growth target of "around 5%" is now in sight. Policy makers may now temper the degree of additional support they provide, but the mixed data flow in March and still weak nominal environment imply further loosening remains on the cards.

Key Takeaways

- Despite mixed monthly data for March, Chinese Q1 GDP beat expectations, rising 5.3% year over year and 1.6% quarter over quarter (non-annualised).
- This was mainly due to the traditional engines of the country's growth – specifically trade and investment. But consumers also helped, with a reasonable showing across retail and services.
- The pace of expansion remains uncertain, as our China Activity Indicator (CAI) implies that activity eased off its blistering pace in March. Property indicators also continue to paint a downbeat picture.
- Even if there are reasons why some payback from Q1's strength could temper GDP growth through the remainder of 2024, statistical revisions make it easier for the authorities to hit their "around 5%" growth target.
- Policy also continues to gain traction, helped by a recovery in China's real equilibrium interest rate (r^*). Our China Financial Conditions Index (CFCI) has been revised higher and now looks more akin to the early stages of the 2016 loosening.
- We do not expect prolonged easing on the scale of 2016. The weak nominal environment and challenges in the real estate sector point to some additional policy easing, but the strong start to 2024 and the focus on national security suggest this could now be toned down.
- We have increased our 2024 growth forecast to 5.1%, implying the authorities' "around 5%" growth target will be met.

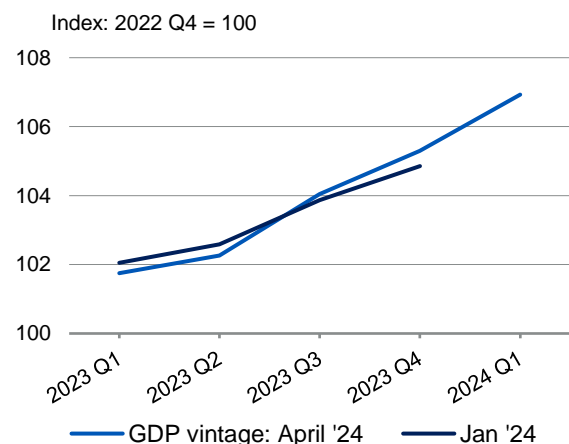
Strong growth in Q1 and data revisions all help

Chinese GDP beat expectations, rising 5.3% year over year and 1.6% quarter over quarter (non-annualised) in Q1.

The National Bureau of Statistics (NBS) once again revised the quarterly growth back data, implying a weaker exit from zero-Covid in H1 2023, but then a stronger pace of expansion through H2 and into Q1 2024.

One can certainly debate the plausibility of stronger growth in the latter stages of 2023 given the upward levels shift implied by the end of zero-Covid. Either way, this pivoting of the GDP profile makes it easier for the authorities to hit their "around 5%" growth target by improving the base effects in the annual growth calculation (see Figure 1).

Figure 1: GDP revisions (again) make it easier for the authorities to hit their growth target



Source: Haver, abrdrn (April 2024)



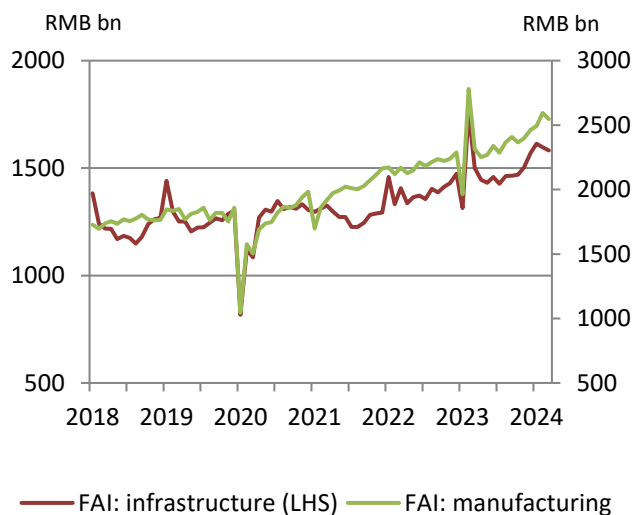
Traditional engines of growth were roaring in Q1...

Previously released strong export figures (+9% quarter over quarter) and a notable improvement in the NBS PMI implied that industry was likely to provide a solid contribution via secondary sector growth. But sectoral data seem to imply exceptional strength over the quarter beyond just trade and goods manufacturing.

Fixed asset investment (FAI) did surprise on the upside in March, coming in at 4.5% year to date year over year versus the 4% expected, seemingly helped by a strong showing from policy-driven infrastructure and manufacturing investment.

FAI data are typically volatile but, with this in mind, we estimate that both infrastructure and manufacturing investment expanded by around 5.5% quarter over quarter (non-annualised). Considering a longer-term perspective, both sectors have been helping to offset the real estate drag since 2021. The recent acceleration could potentially reflect robust credit flows, which have averaged almost RMB 3 trillion per month for the past 12 months.

Figure 2: Policy has been leaning on manufacturing and infrastructure investment



Source: Haver, abrdrn (April 2024)

... while household consumption also helped

Retail sales and services were also decent supports to growth over Q1, even if the headline growth rate for retail sales values for March was 3.1% year over year – 1.7ppts lower than consensus.

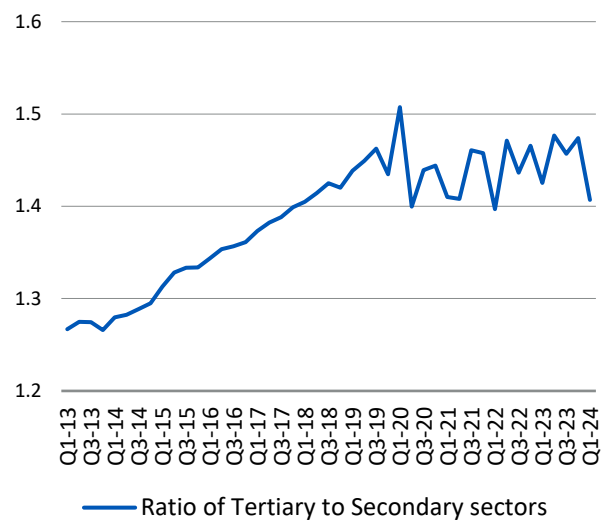
We estimate that retail sales volumes expanded by 2.8% quarter over quarter, similar to the implied quarterly growth rate obtained from seasonally adjusting the services production index.

For now, it appears that a renewed fall in the saving rate, which is now within 1ppt of its pre-pandemic rate, is helping to support consumption.

China's apparent excess savings may however never be tapped. The People's Bank of China (PBOC)'s Q4 urban resident survey implies still very depressed employment and income confidence, while the proportion of those who want to increase savings remains close to a record high and the amount of people expecting house prices will rise is still at a record low. Indeed, this could imply that the savings rate has been pushed permanently higher by the pandemic shock and the de-risking of the property sector.

Taking a step back, it is also notable that there has been a breakdown in the rebalancing between industry and services (see Figure 3). Alongside weakened consumption dynamics, this could imply a longer-lasting structural impediment, which may weigh on growth prospects.

Figure 3: Rebalancing is MIA



Source: Haver, abrdrn (April 2024)

Strong GDP and downside surprises for a few March releases is a puzzle throwing shade on the outlook

While implied quarterly growth rates generally back up the strong activity picture implied by the GDP release, March data often fell short of consensus expectations.

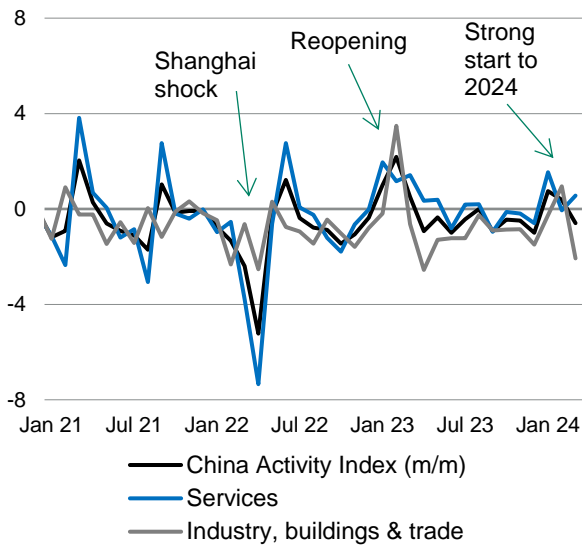
The March print for industrial production (IP) came in 1.5ppts below expectations, at 4.5% year over year, and the NBS estimates that the sector contracted by 0.1% month over month. Similarly, retail sales were 1.7ppts beneath consensus (3.1%).

And there is little to cheer about in the property sector: new starts, volumes and values of sales all edged down on the month; while house prices continue to fall. The only small silver lining is that the pace of price declines has moderated slightly for existing residential buildings and Tier-1 cities.

Our China Activity Indicator (CAI) picks up a notable moderation in sequential momentum towards the end of the quarter, casting some doubt on the pace of expansion going forward (see Figure 4).



Figure 4: Our monthly China Activity Indicator (CAI) has eased off its previously strong pace



Source: Haver, abrdrn (April 2024)

A weak nominal environment and ongoing property challenges should facilitate further easing

Even if official data show a strong real business environment, questions remain about the nominal backdrop.

The GDP deflator fell by 1% in both year-over-year and quarter-over-quarter terms, implying that fears of ‘Japanification’ will be slow to recede.

This should at least keep policy makers on an easing footing. Stronger growth, an easier route to hit their growth target and ongoing de-risking policy priorities might have led to a more marked withdrawal of support if the economy was showing signs of building inflationary pressure. In practice, the supply-side biased policy response seems likely to keep a lid on prices, perhaps too effectively.

Financial conditions now appear looser than previously estimated, helped by GDP revisions and r^*

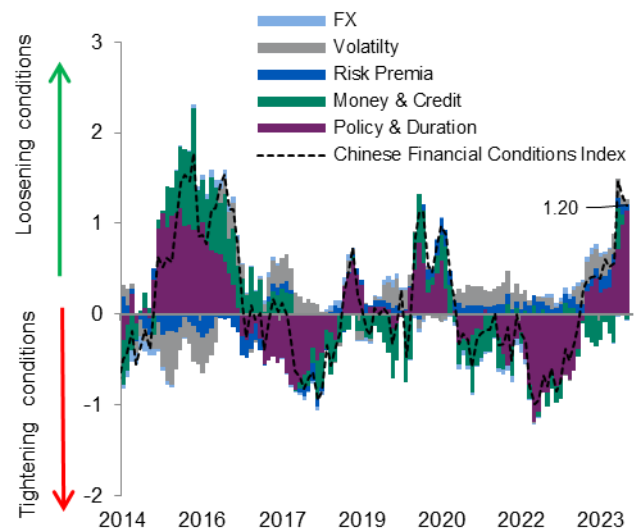
On the month, our China Financial Conditions Index (CFCI) declined by 0.08 points, to 1.20. M1 money supply surged before Lunar New Year. This spike then reversed, weighing on the index – and could push the index further down over the next few months.

But the real news is that the CFCI has been revised higher, moving it more sharply into accommodative territory since the turn of the year. Indeed, the loosening of the CFCI now appears more akin to the loosening in 2016 (see Figure 5).

The upward revision reflects two drivers. First, the Q1 GDP surprise has pushed up on our estimate of the real equilibrium interest rate (r^*), which is now back to its pre-pandemic level, having been severely depressed by real estate de-risking and lockdowns in 2022. This has meant

that policy easing has been gaining more traction than previously thought, pushing up on Policy & Duration factors.

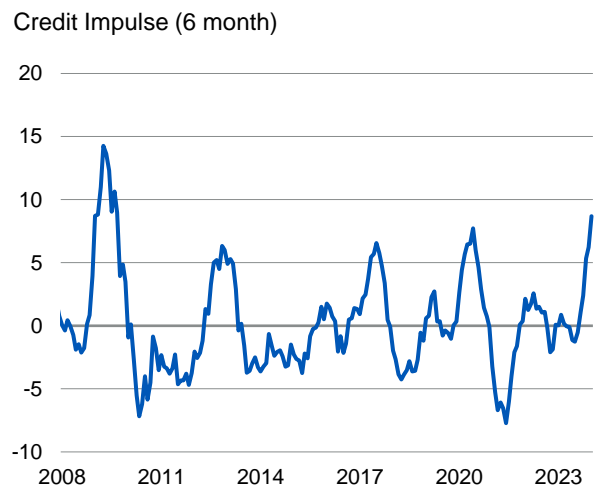
Figure 5: Financial conditions have surged since the start of 2024



Source: Bloomberg, Haver, abrdrn (April 2024)

Secondly, while there may be some legitimate questions about the reprofiling of GDP, this has combined with the ongoing strength of credit flows to push the credit impulse up sharply – now at its highest level since 2009 (see Figure 6).

Figure 6: The credit impulse has turned sharply up



Source: Haver, abrdrn (April 2024)



Strong start to the year, data revisions and looser financial conditions push up our GDP forecast

Putting it all together, the government's growth target of "around 5%" should now be much easier to achieve.

The credit impulse and financial conditions imply a chance that growth remains robust throughout 2024, which could even push growth above the authorities' target.

But we think the economy is more likely to 'meet' (+/- 0.2ppt) the target rather than 'exceed' it.

March data already signal a slowdown in sequential momentum. Some payback from exceptional net exports could weigh on Q2 growth. We remain cautious on household consumption and the drag from property, and we doubt that financial conditions will remain loose enough for long enough to ultimately resemble the conditions of 2016.

The weak nominal backdrop and ongoing challenges within property should keep policy easing at the margin, but policy priorities have fundamentally changed since 2016, with the authorities mindful of losing hard-fought progress on de-risking and increasingly focused on national security and resilience.

Moreover, some firepower will likely be withheld for the event of a ramp-up in US trade tensions, which would be more likely were Donald Trump to win the US presidential election in November.

Our new forecast for 2024 is 5.1 % (+0.5pts).

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