March 2019

China Economy Update

China Economics Network

For comments, suggestions, questions, please contact us:

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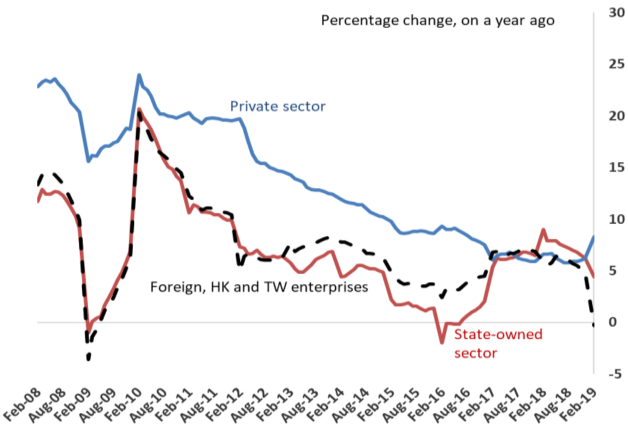
SUMMARY

- **Official data showed a further weakening in China's economy in the first two months of 2019.**
- **Investment growth ticked up slightly reflecting stable (government supported) infrastructure investment and a surge in property investment. But industrial production growth slowed further, retail sales remained weak, and exports and imports softened.**
- **The government reaffirmed its pro-growth policy stance at the March annual 'parliamentary' meetings following the weak data, highlighting the downward economic pressure from home and aboard, while continuing to raise concern about systemic financial stability risks.**

Industrial output continued to slow

1. Official data showed industrial value-added growth slowed further from 5.7 per cent year on year in December 2018 to 5.3 per cent in the first two months of 2019, a seventeen year low. In attempt to calm the market, the National Bureau of Statistics claimed underlying growth was actually 6.1 per cent once adjusting for Spring Festival holiday related factors, although there were no details on what the factors were.
2. The slowdown was mainly caused by weak mining and electricity output, up only 0.3 per cent and 2.9 per cent year on year in Jan-Feb, respectively. Manufacturing output grew 5.6 per cent, unchanged from Dec 2018.
3. Growth of industrial production by Chinese state-owned and private companies increased by 4.4 per cent and 8.3 per cent year-on-year in the first two months this year, respectively. But the growth of production by foreign invested companies (including HK, Macao and Taiwan) contracted 0.3 per cent, continuing the slowdown seen since June 2018. Policy uncertainty due to US-China trade disputes are likely to be weighing on production prospects of foreign invested companies (Figure 1).

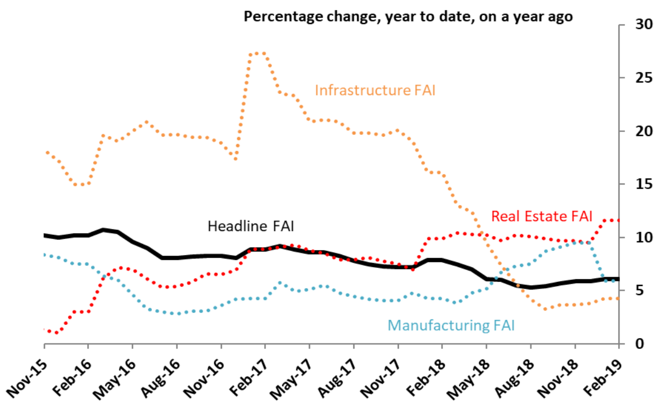
Figure 1: Industrial Production growth



Investment growth recovered marginally, but may not be sustained

4. Official data showed fixed-asset investment increased 6.1 per cent year-on-year in Jan-Feb, up from 5.9 per cent in 2018, driven by sustained growth in (government supported) infrastructure investment, and a surprise surge in property investment (Figure 2).

Figure 2: Fixed-asset investment growth (FAI)



5. Property investment growth accelerated to a five-year high of 11.6 per cent in Jan-Feb from 9.5 per cent in December 2018. But this may not be sustained. Growth of land purchases contracted 34.1 per cent year-on-year, and the growth of floor space sold declined to -3.6 per cent, the first negative growth since June 2015. The significant slowdown in housing market activity indicates a possible deterioration in property investment in the second quarter of this year, unless there is a nation-wide loosening in property polices.

6. Manufacturing investment growth slowed sharply to 5.9 per cent in Jan-Feb from 9.5 per cent in 2018, likely reflecting uncertainty arising from US-China trade tensions.

Retail sales remained subdued

7. Official data showed retail sales growth remained weak, up 8.2 per cent in Jan-Feb over the same period last year, but unchanged from December 2018. In addition to weak car sales, sales of mobile phones, other daily necessities, and housing related products (building materials, home appliances, and furniture) were also subdued, a worrying sign of broad-based weakness in domestic demand.

Export and import growth continued to fall

8. Official data showed China's export and import growth slowed further in Jan-Feb, down 4.6 per cent and 3.1 per cent year-on-year in US dollar terms, respectively.

9. The volatility in monthly exports - which declined 20.7 per cent year-on-year in February to a three year low, following a 9.1 per cent increase in January - was partly due to the Chinese New Year holiday. But shipments to the US (accounting for 16.8% of China's total goods exports) were notably weak, contracting by 28.6 per cent on a year ago.

Credit growth picked up, only modestly

10. Growth in the outstanding stock of Total Social Financing picked up to 10.4 per cent and 10.1 per cent year-on-year in Jan and Feb, respectively, from 9.8 per cent in Dec2018. This was driven by government and corporate bond issuance, suggesting the measures to support credit to the real economy and boost local government investment, announced since late 2018, may be starting to have an effect.

11. Shadow banking (i.e. off-balance sheet financing) continued to shrink, but at a slower pace. Total reduction in shadow banking sector in Jan-Feb was RMB21.7bn, compared to RMB209.2bn of monthly average in Q4 2018. Money supply (M2) grew 8 per cent year-on-year in Feb, down from 8.4 per cent a month earlier.

The government reaffirmed its pro-growth policy stance

12. The subdued data were announced a day before the government wrapped up China's parliamentary sessions where Premier Li highlighted concerns about growing downward economic pressure (reflecting weak internal and external demand and uncertainties from the trade dispute). He promised imminent fiscal stimulus measures of a 'greater intensity', while urging all to stay alert to financial risks.

13. Monetary policy is to remain 'prudent' with money supply and credit growth to be kept in line with nominal GDP growth. Policy makers are also focusing on 'Financial Supply-Side Structural Reform' (the latest buzzword), a campaign to improve the monetary policy transmission to the real economy, provide diversified financial products, and improve the allocation of financial resources.