

# China Macro Outlook

Returning to potential growth

October 2020



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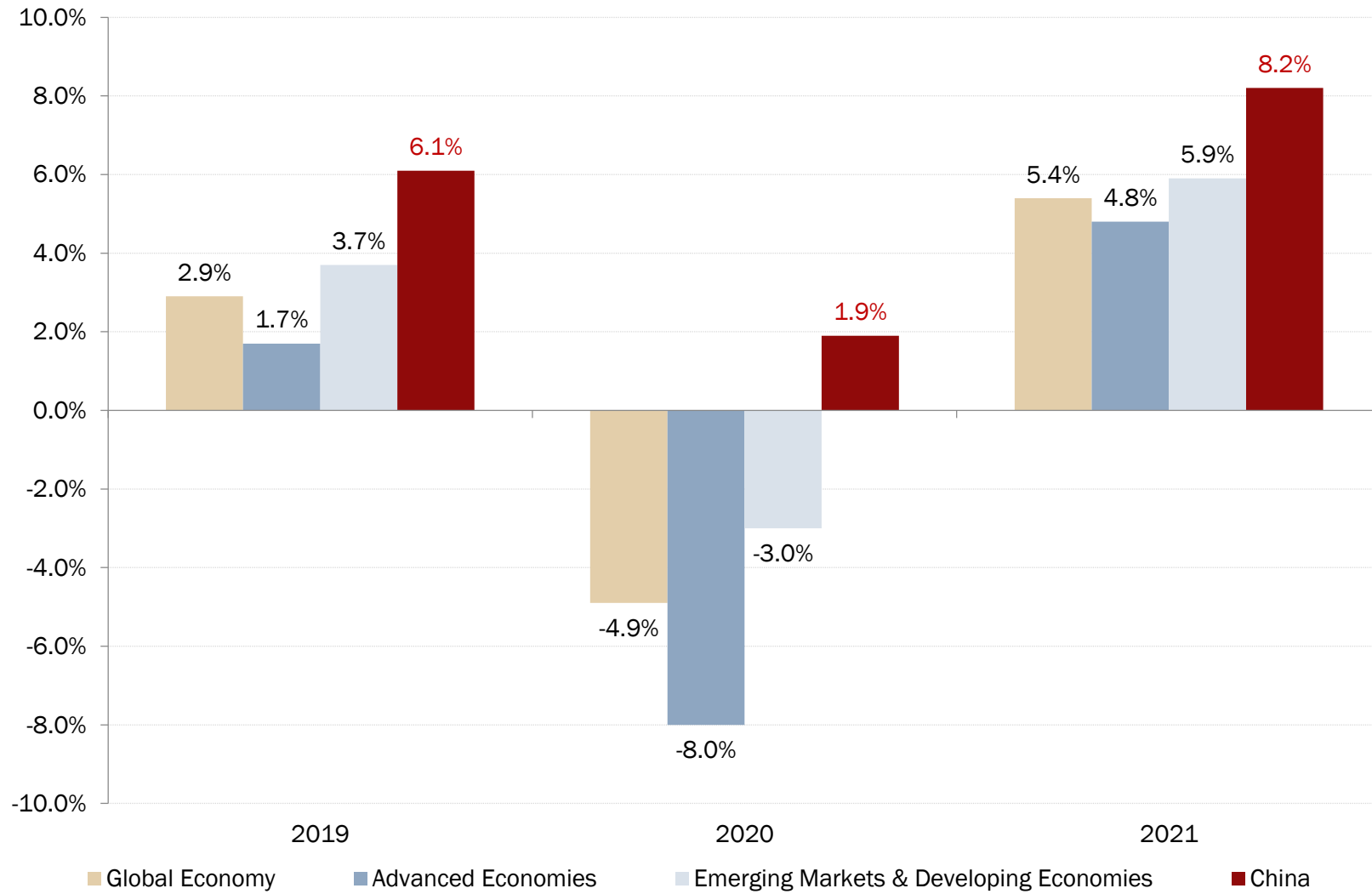
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## Recovery well on track to record a positive GDP print by year-end

- The latest September(Q3) economic data adds further evidence to the notion that China is outgrowing the pandemic shock and is well positioned to further improve on the 0.7% YTD growth underpinned by successful containment of the pandemic.
- 4.9% growth in Q3 points to a strong and robust improvement over Q2 (3.2%) with a more balanced recovery in consumption activities as well as industrial production in August and September.
- Upshot in retail sales and investments, coupled with sustained growth momentum in industrial production, all confirmed that the recovery has gained solid footing and is becoming more entrenched in late-Q3.
- The Chinese yuan (CNY) has been a key beneficiary of broad-based macro improvements. USDCNH rallied to record levels in October aided by refreshed dollar weakness ahead of the US elections.
- That said, domestic consumption is far from its pre-pandemic levels and is unlikely to fully resume positive growth before year-end. Further investment recovery could also be limited since strong YTD growth momentum in both property investment and local government bond issuances is likely to tail-off in Q4.
- Meanwhile, PBoC and regulators remain committed to curtailing speculative investments to avoid further asset price inflation. That said, the central bank has kept credit conditions highly accommodative, while balancing inter-bank liquidity via OMO and keeping rates easing tools suspended since May.
- All in all, the latest set of data is a reminder that policy support may likely remain in place to ensure sustained recovery for the time being. More policy clarity is expected post the Fifth Plenary meeting and the US elections.
- Heading into Q4, the upturn in China's recovery is on course to continue in the rest of 2020 with a positive outlook of achieving the c.2.0% real implied growth objective by year-end.

# Bleak growth projection reveals worst hit to global economy since WWII

IMF World Economic Outlook Growth Projections (Oct. 2020)



Source: IMF, ICBC Standard

## China is on course to outperform amidst sluggish global recovery

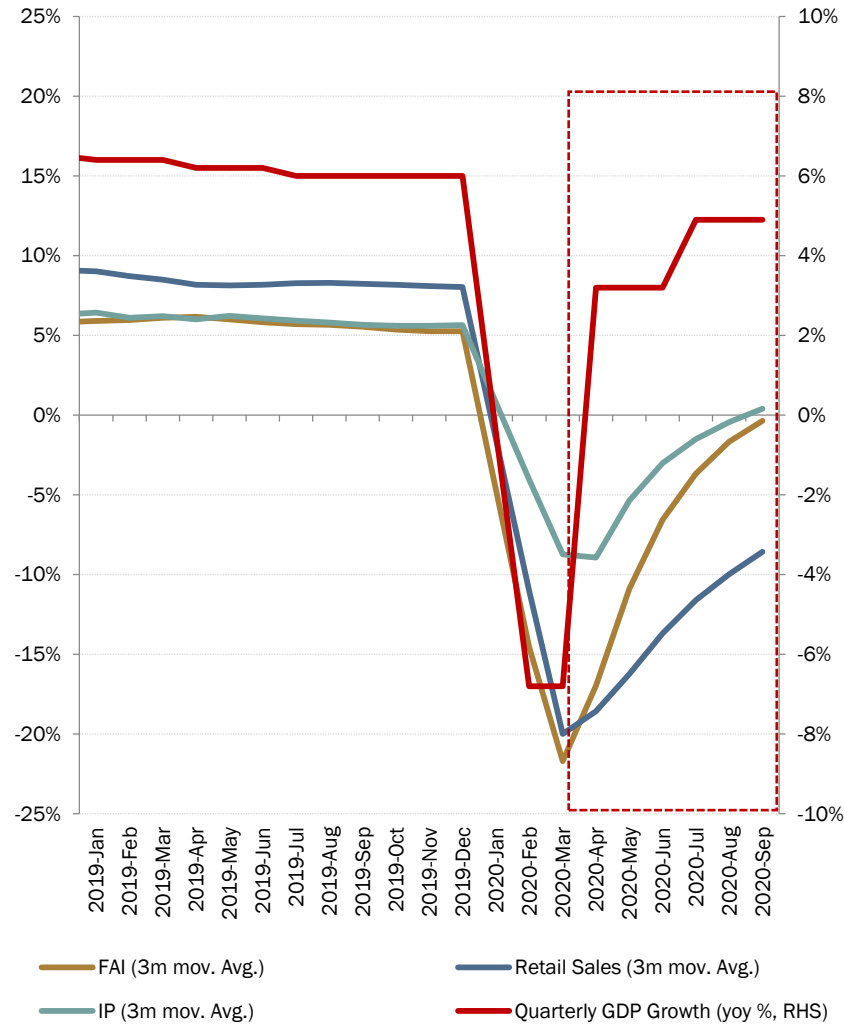
### Growth outlook of key economies

	2019	2020	2021
<b>Advanced Economies</b>	<b>1.7</b>	<b>-5.8</b>	<b>3.9</b>
US	2.2	-4.3	3.1
Euro Area	1.3	-8.3	5.2
Germany	0.6	-6.0	4.2
France	1.5	-9.8	6.0
Italy	0.3	-10.6	5.2
Spain	2.0	-12.8	7.2
UK	1.5	-9.8	5.9
Japan	0.7	-5.8	2.3
Canada	1.7	-7.1	5.2
<b>Emerging Markets and Developing Economies</b>	<b>3.7</b>	<b>-3.3</b>	<b>6.0</b>
<b>China</b>	<b>6.1</b>	<b>1.9</b>	<b>8.2</b>
India	4.2	-10.3	8.8
Russia	1.3	-4.1	2.8
Brazil	1.1	-8.1	2.8
South Africa	0.2	-8.0	3.0
Nigeria	2.2	-4.3	1.7
Saudi Arabia	0.3	-5.4	3.1

Source: IMF (WEO October 2020), ICBC Standard

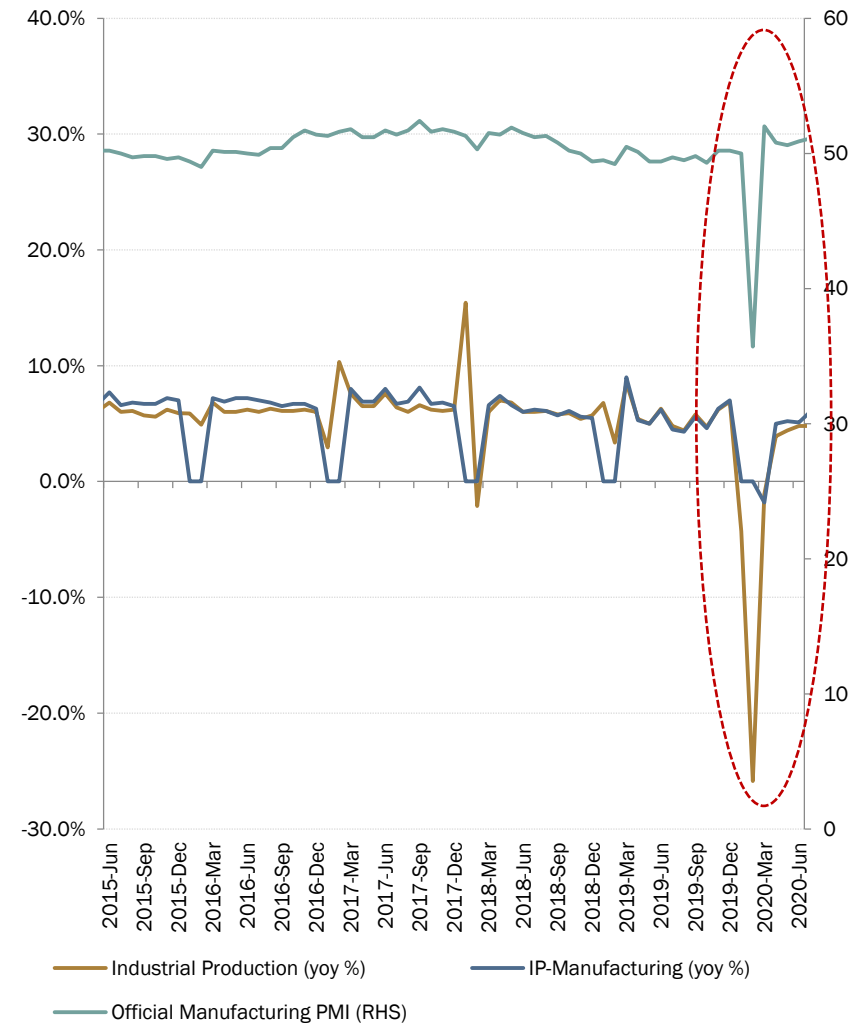
# Broad-based Q3 improvements bode well to reach c 2.0% annual growth

China's economy expanded by 4.9% yoy in Q3 vs. 3.2% in Q2



Source: WIND, ICBC Standard

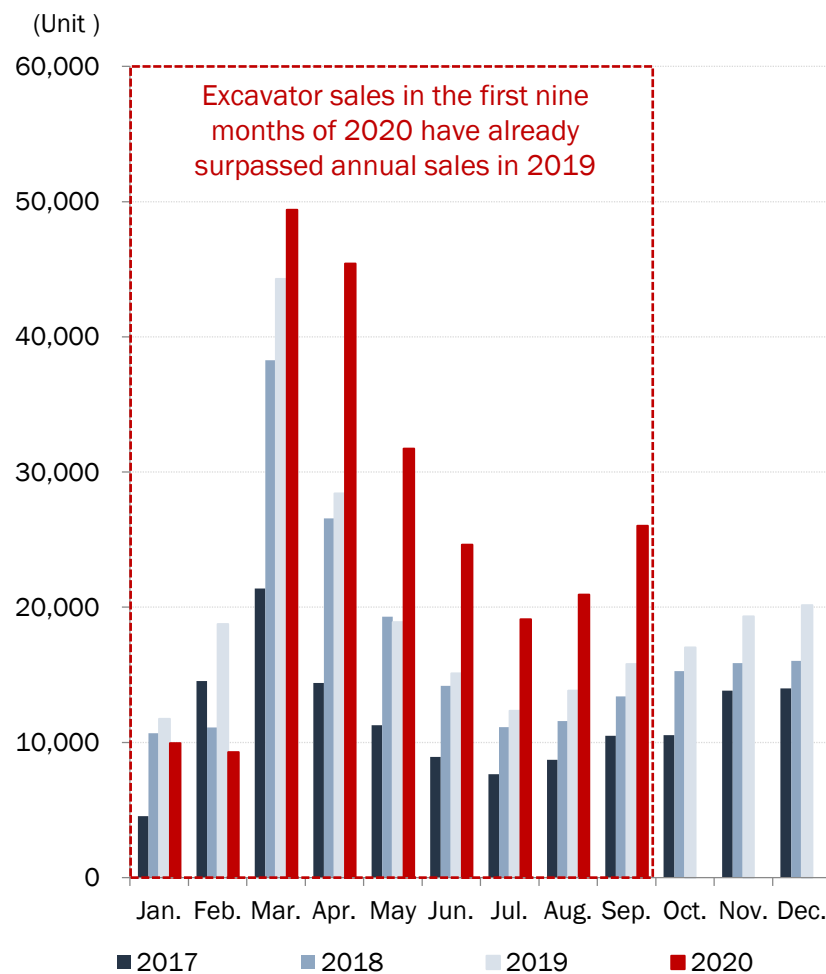
September IP growth accelerated to 6.9% yoy in sync with PMI



Source: WIND, ICBC Standard

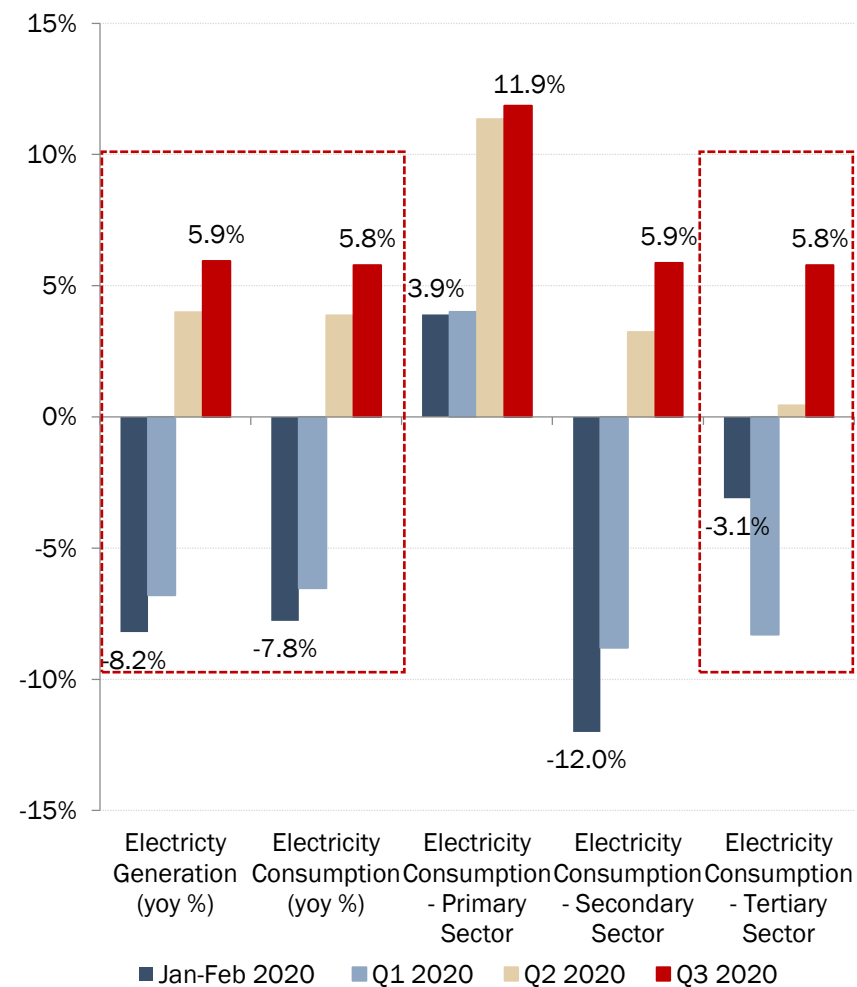
## High-frequency data confirms sustained supply-side recovery in Q3

**Continued growth in excavator sales in Q3 points to extended support from infrastructure projects in the months ahead**



Source: WIND, ICBC Standard

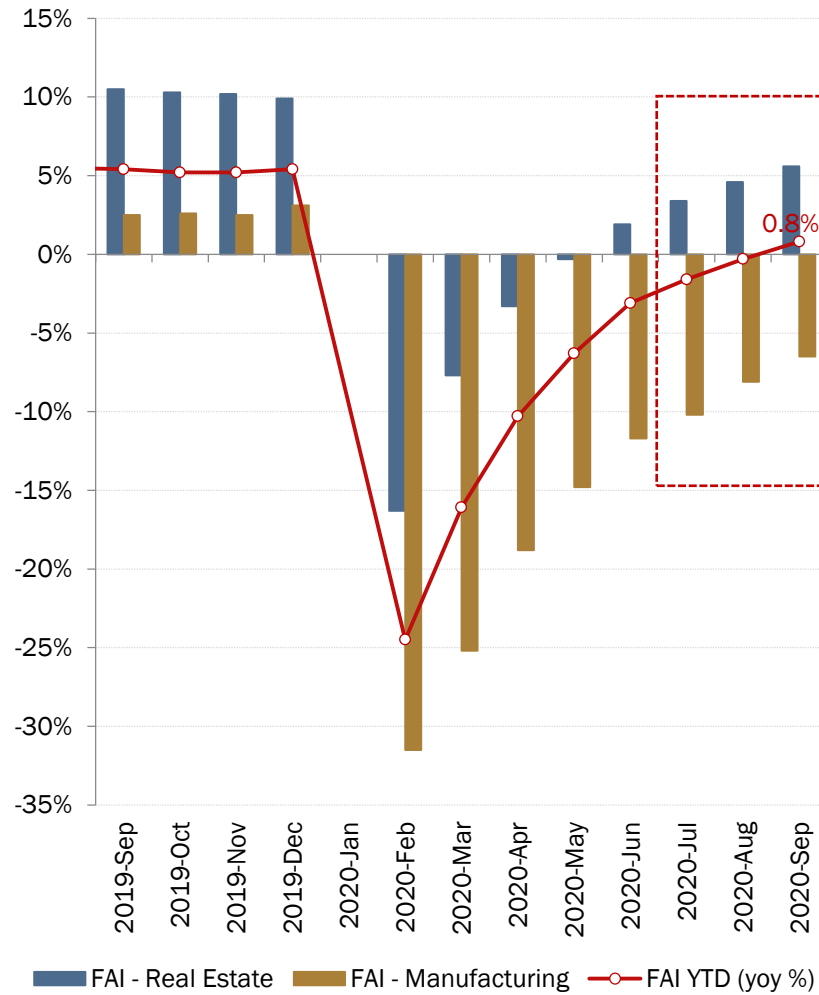
**Q3 electricity consumption further confirms a broad-based improvements especially in the services sector**



Source: WIND, ICBC Standard

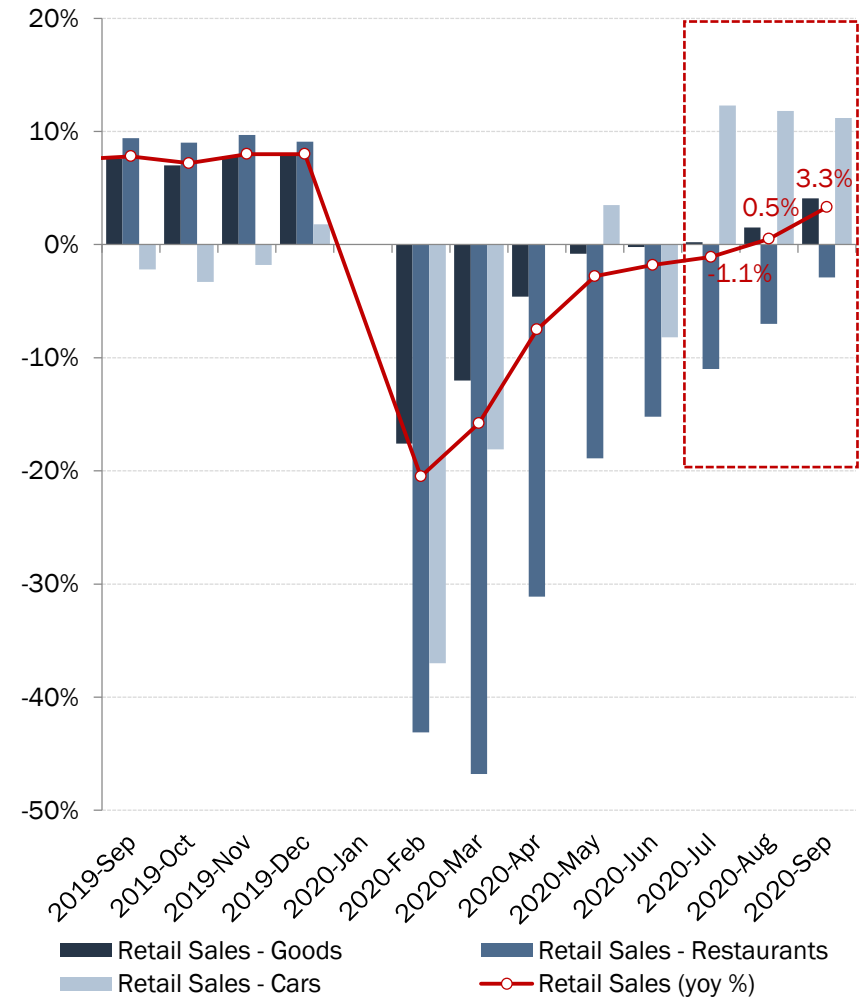
## Lagging-consumption and investment both picked up in late-Q3

YTD FAI finally resumed positive growth but future recovery could be limited in Q4 given policy shift to dial-down property investment



Source: WIND, ICBC Standard

Monthly growth momentum in retail sales began to gather pace in late-Q3 led by pick-up in consumer goods and auto sales

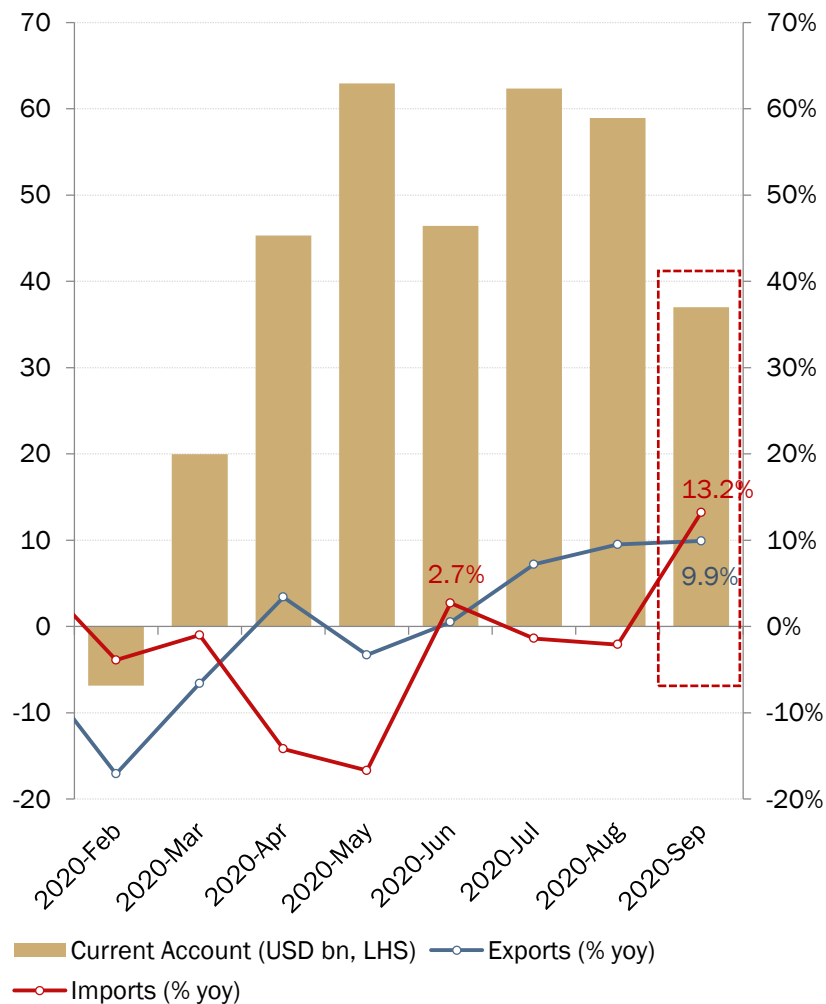


Source: WIND, ICBC Standard



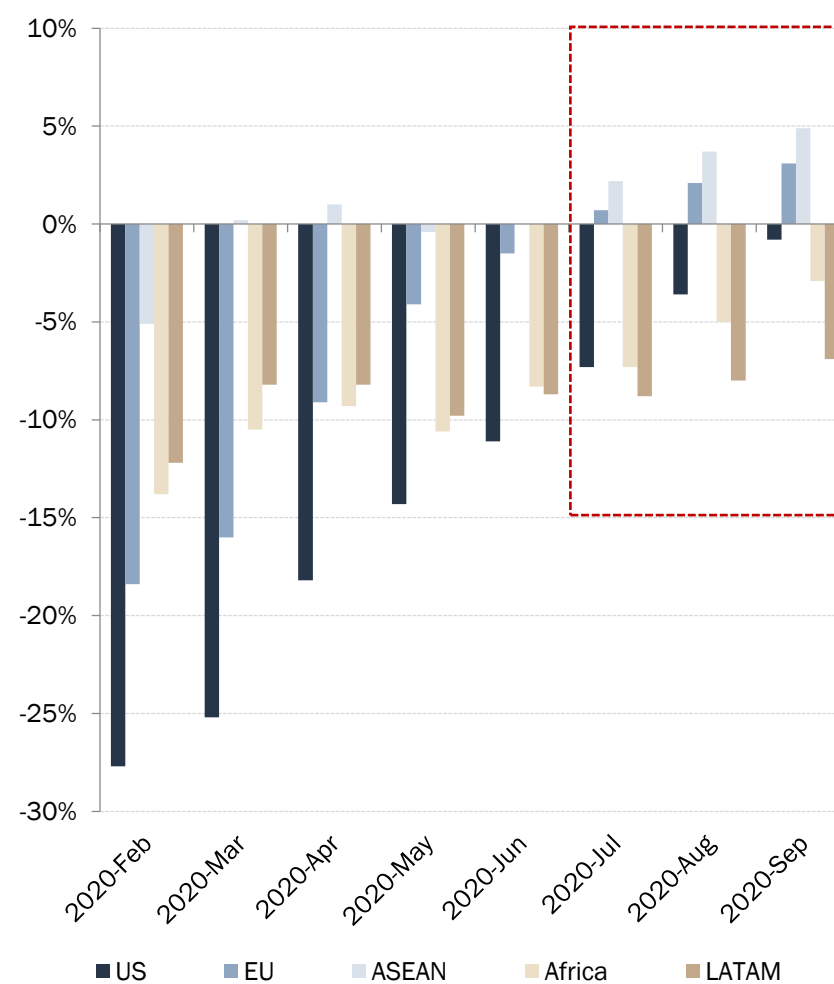
## Imports shows strong pick-up and exports remains resilient

September surge in imports growth reflected evident improvements in domestic demand, while exports sustained recovery in Q3



Source: WIND, ICBC Standard

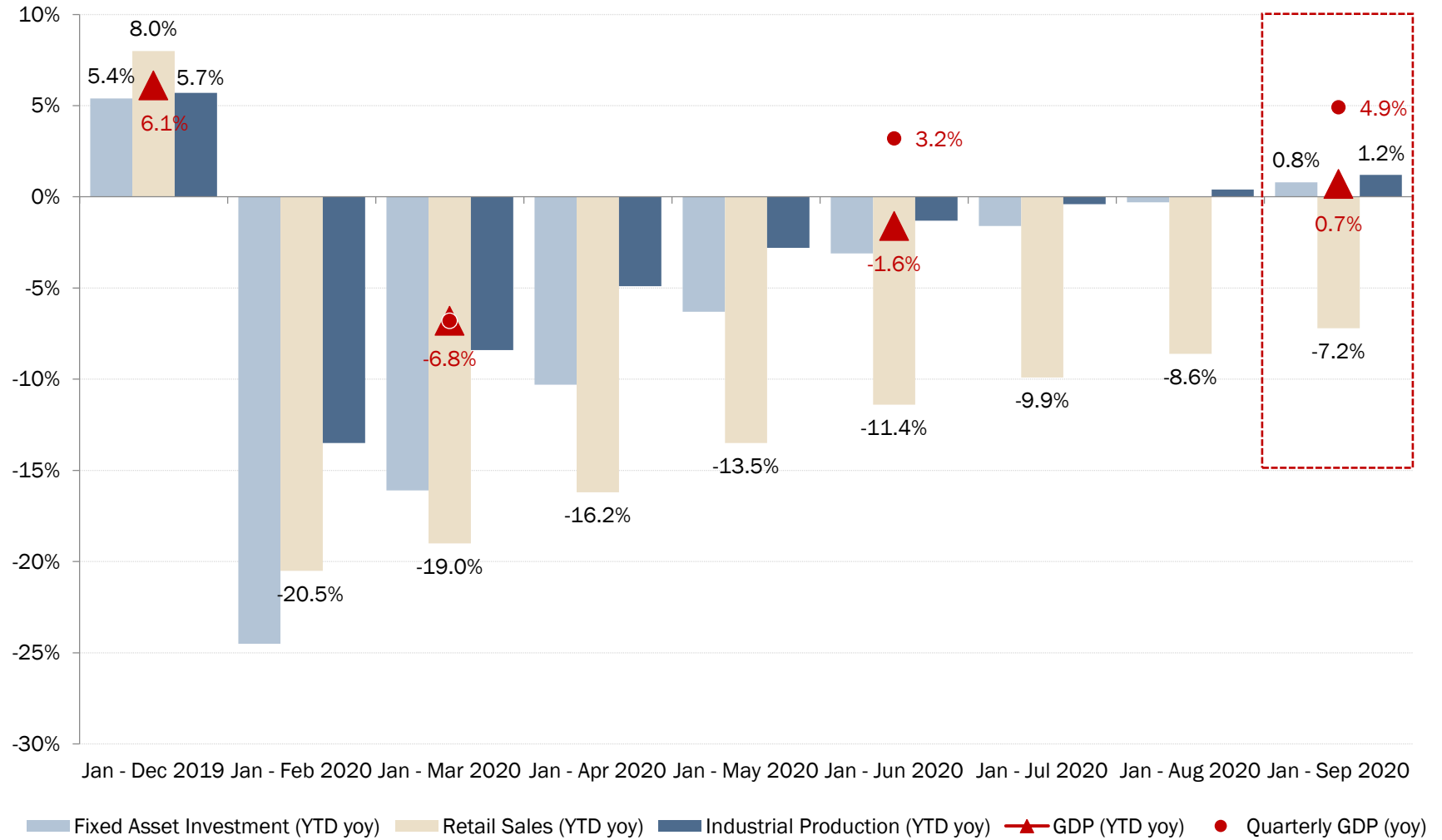
External demand from ASEAN and EU has gradually recovered with regional YTD exports both resuming expansion in Q3



Source: WIND, ICBC Standard

## Consumption remains a laggard in the "V-shaped recovery"

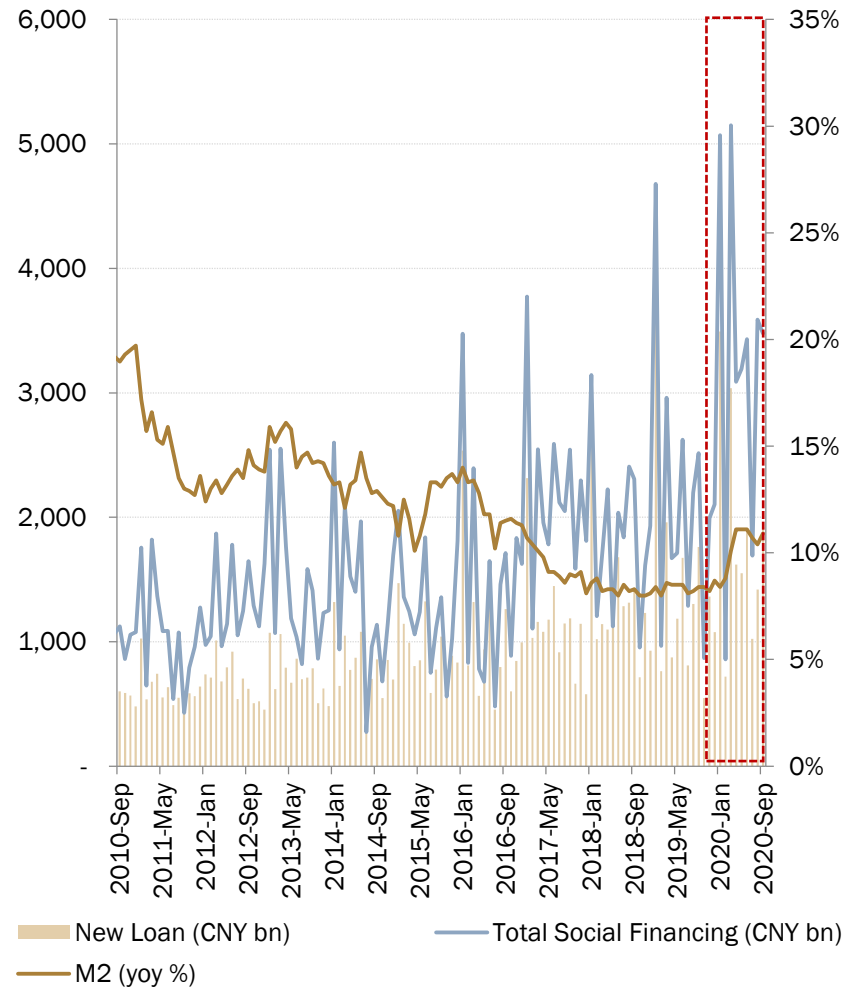
YTD retail sales is yet to catch up with supply-side improvements and faces challenges to reverse the declining trend before year-end



Source: WIND, ICBC Standard

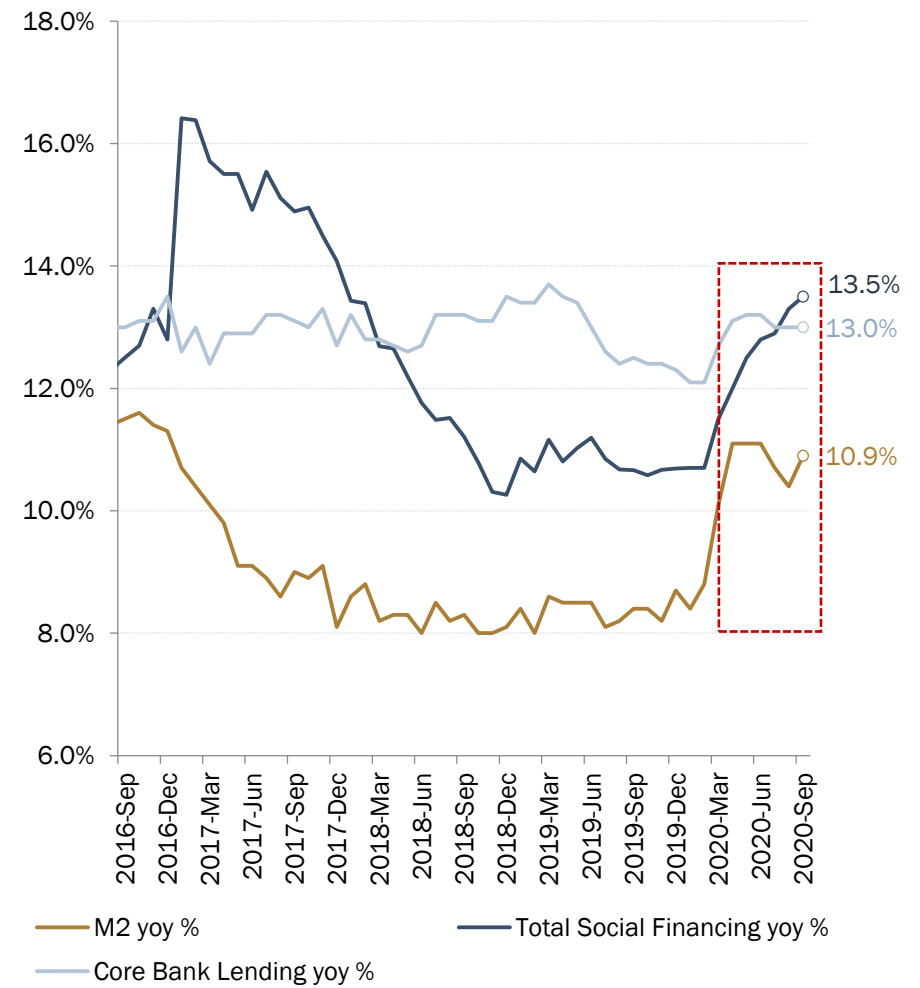
## Beijing has kept credit policy highly accommodative since Feb. 2020

The pace of credit expansion in H1-2020 is rather significant compared to the past decade of deleveraging attempts



Source: WIND, ICBC Standard

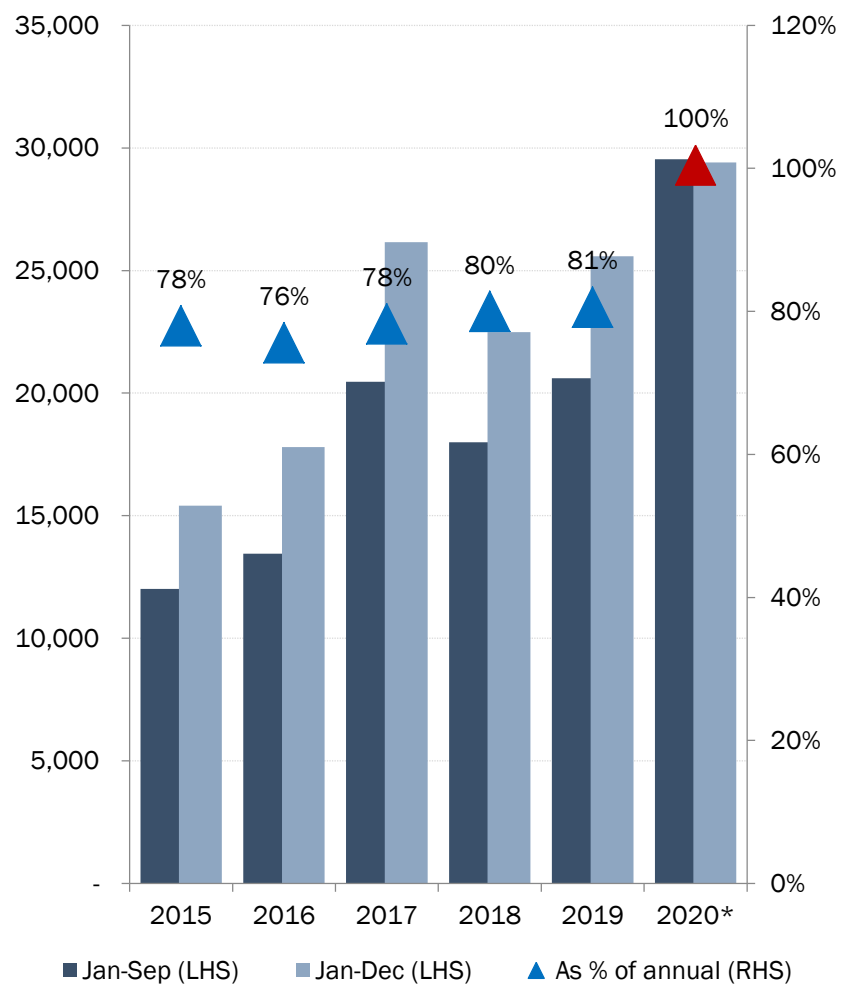
Growth in broad social credit has returned to a double-digit pace since March and is likely to sustain in Q4



Source: WIND, ICBC Standard

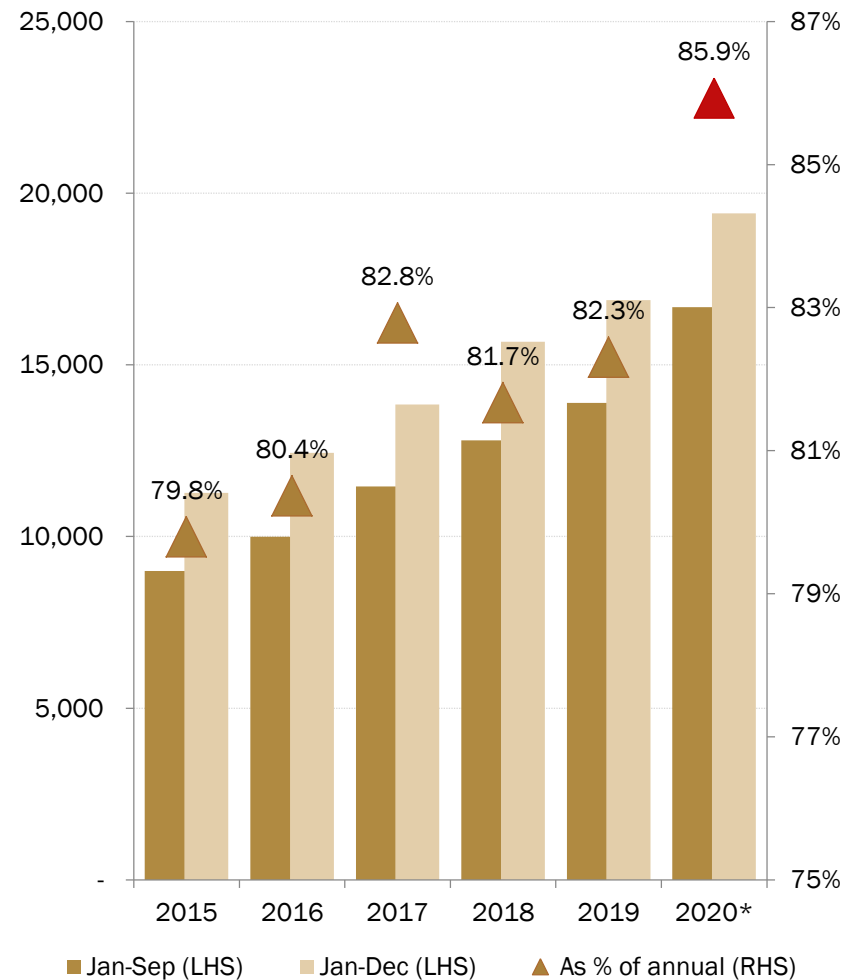
## Broad social credit and new bank lending both rose rapidly in Jan - Sep

**YTD total social financing already exceeded the annual volume in 2019, hence pointing to a minimum 15% annual growth in 2020**



Source: WIND, ICBC Standard  
 \*Note: Assume total social financing to increase by 15% from 2019, exceeding CNY 29.4tn by 2020 year-end.

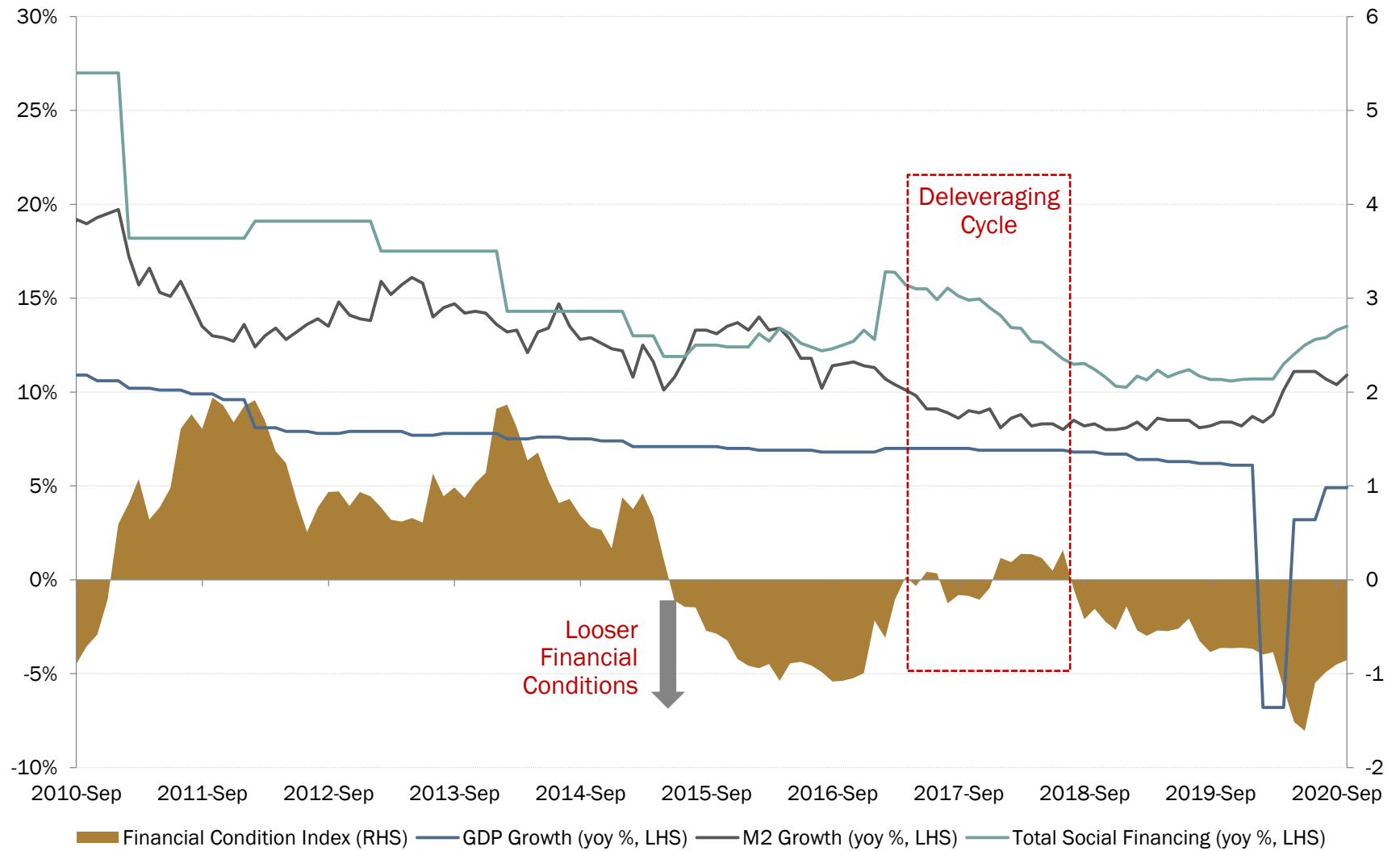
**New loans also reached record high at nearly 86% of annual new bank lending by the end of September 2020**



Source: WIND, ICBC Standard  
 \*Note: Assume new loans in 2020 to expand by 15% from 2019, reaching CNY 19.4tn by 2020 year-end.

## But accommodative liquidity conditions risk re-inflating asset bubbles

Financial conditions marginally tightened since June as regulatory tone has shifted towards curtailing speculative investments

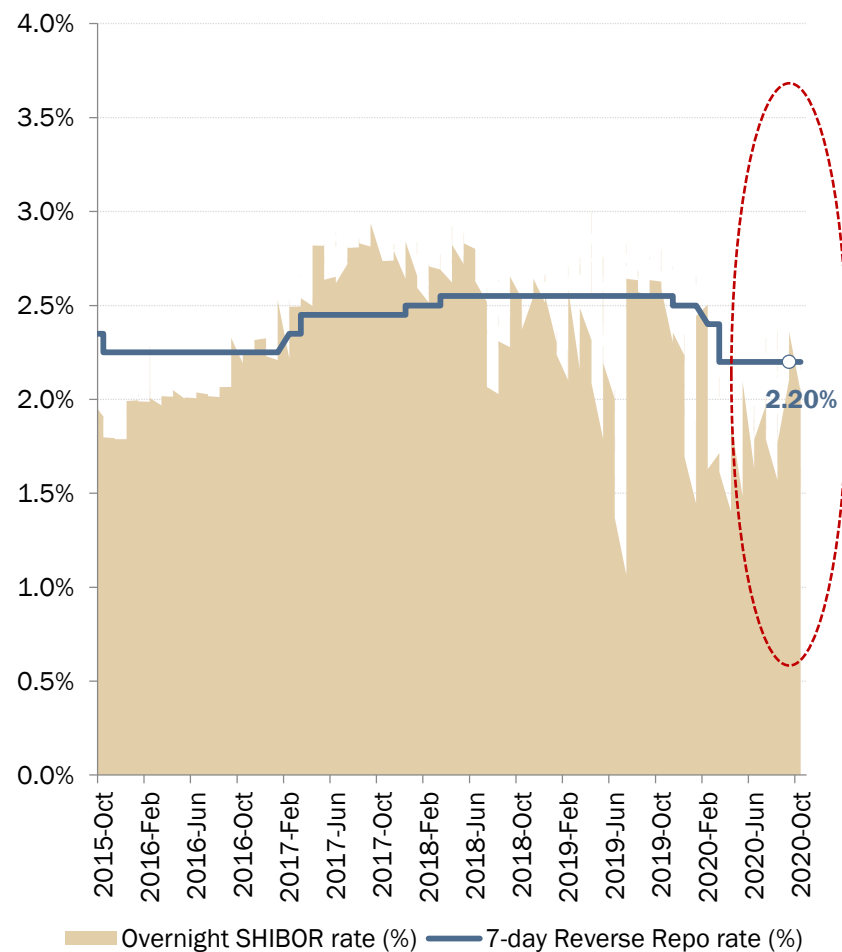


Source: WIND, ICBC Standard

Note: Negative reading of Caixin Financial Condition Index reflects loose financial condition, and positive reading means tighter financial condition in the onshore China market.

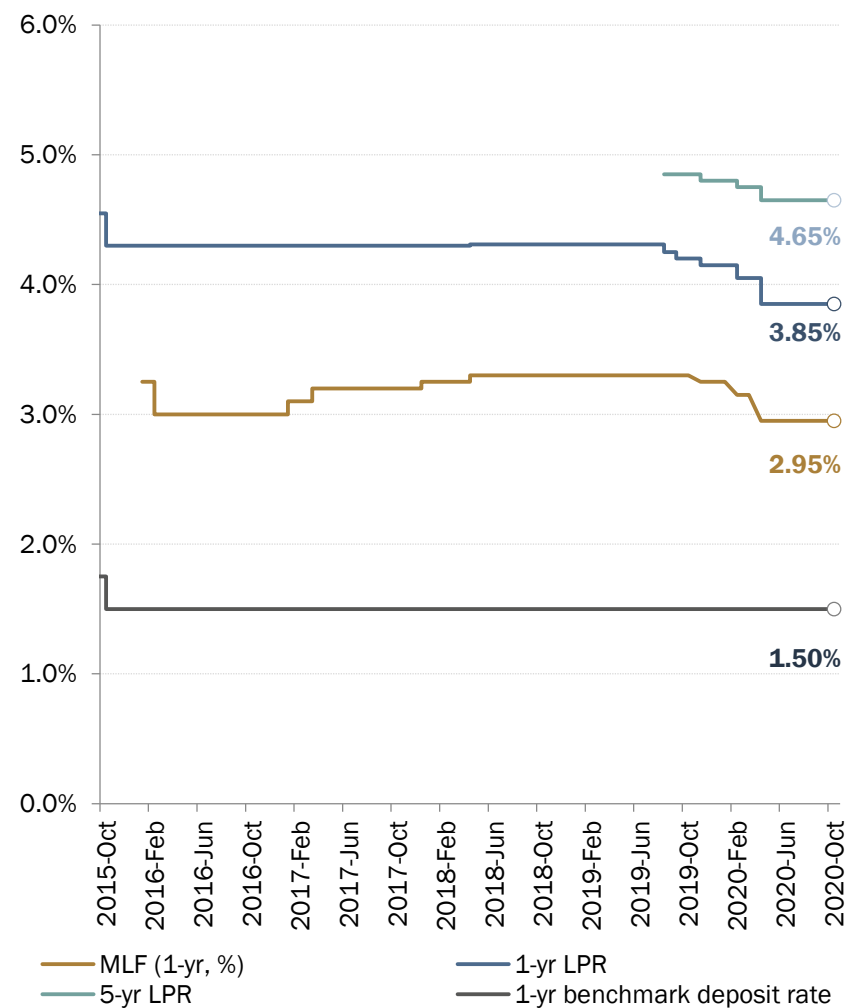
## PBoC remains vigilant against risks of asset price inflation

7-day OMO rate unchanged since NPC meeting while overnight borrowing rate retreated to 2.20%+ level



Source: WIND, ICBC Standard

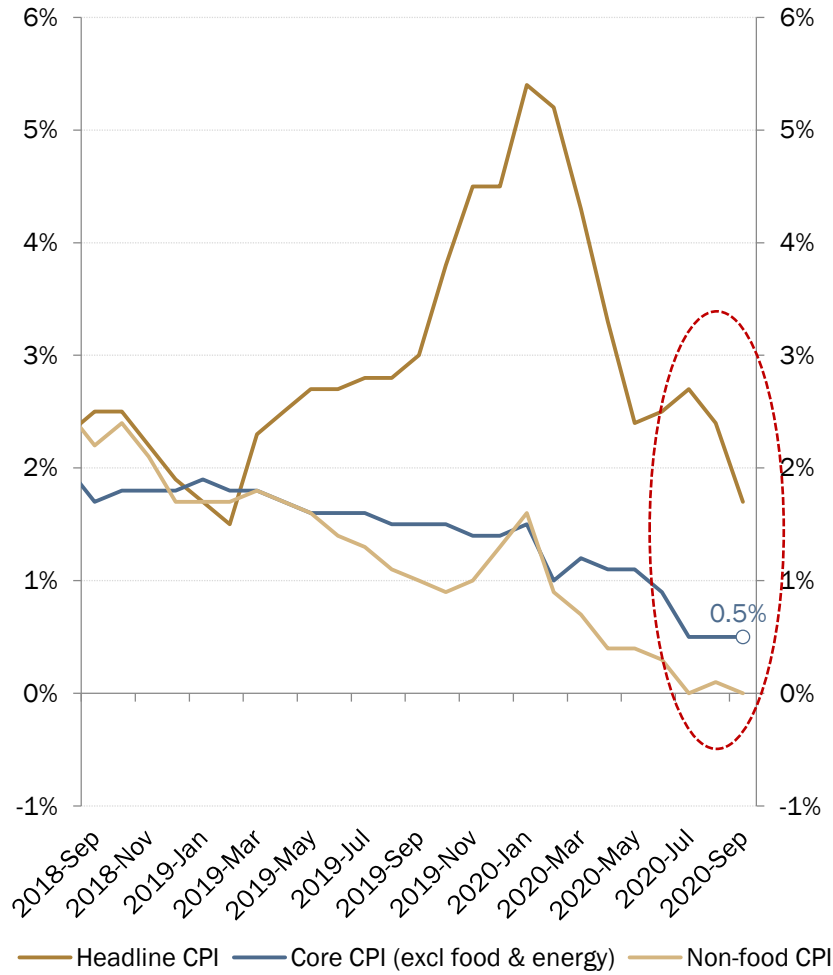
PBoC has kept interbank rates unchanged since May



Source: WIND, ICBC Standard

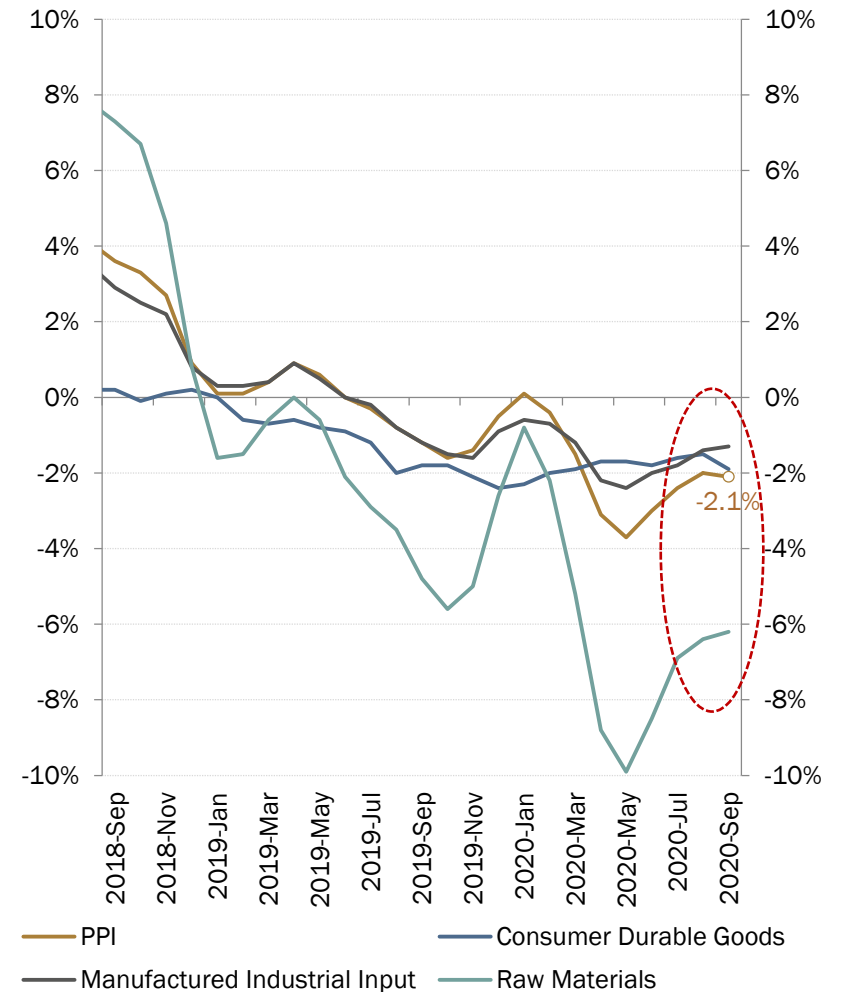
# Inflation is yet to improve on recent recovery in consumption activities

**Core CPI remain well below 1% in Q3, while headline CPI dropped elevated pork price**



Source: WIND, ICBC Standard

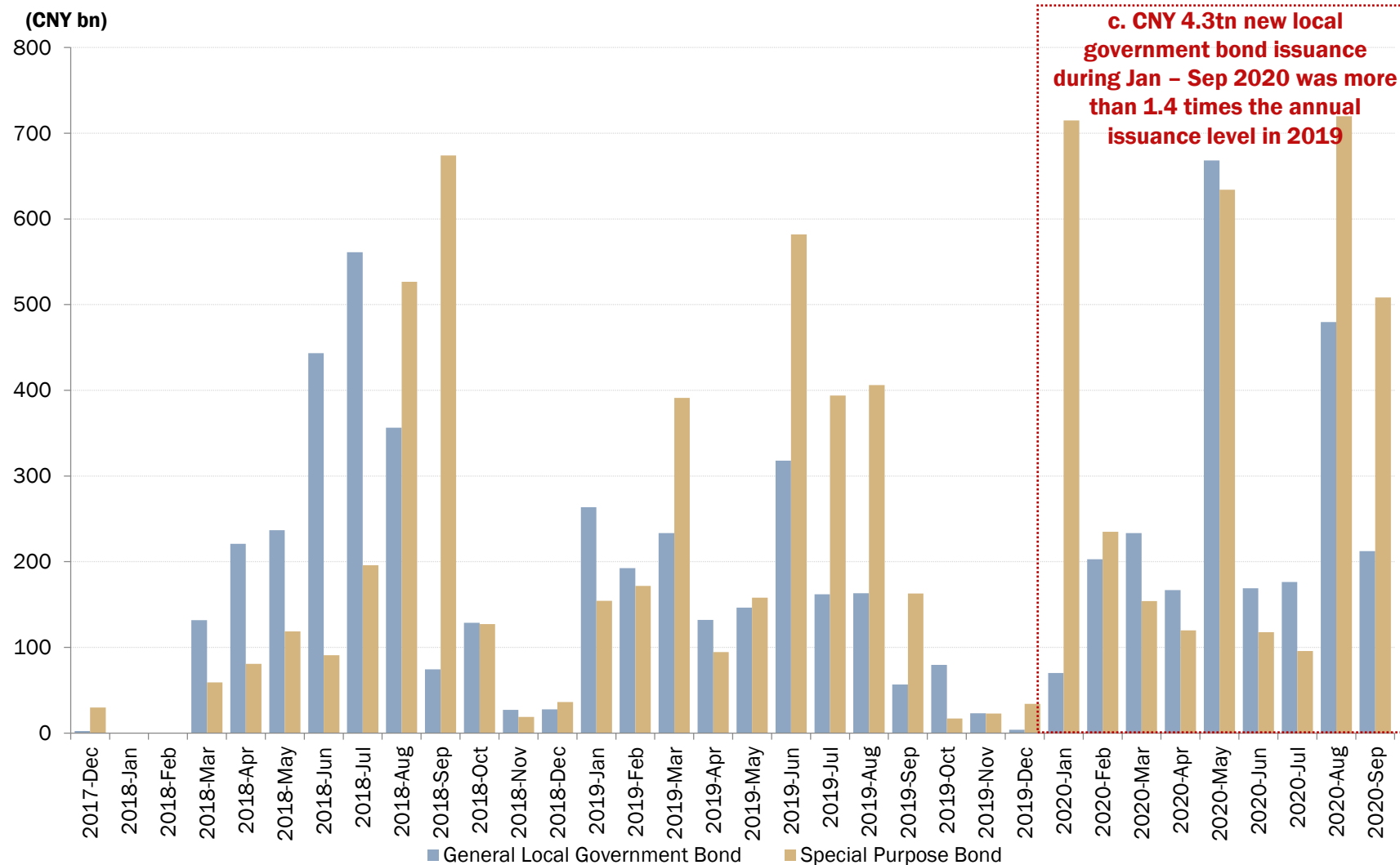
**Factory deflationary pressure continued to ease in Q3**



Source: WIND, ICBC Standard

## Ultra-proactive fiscal policy will support growth into Q4-2020

CNY 3.0tn local government bonds new issuance record in 2019 dwarfed by over CNY.4.3tn bond issuance in the first nine months of 2020



Source: WIND, ICBC Standard

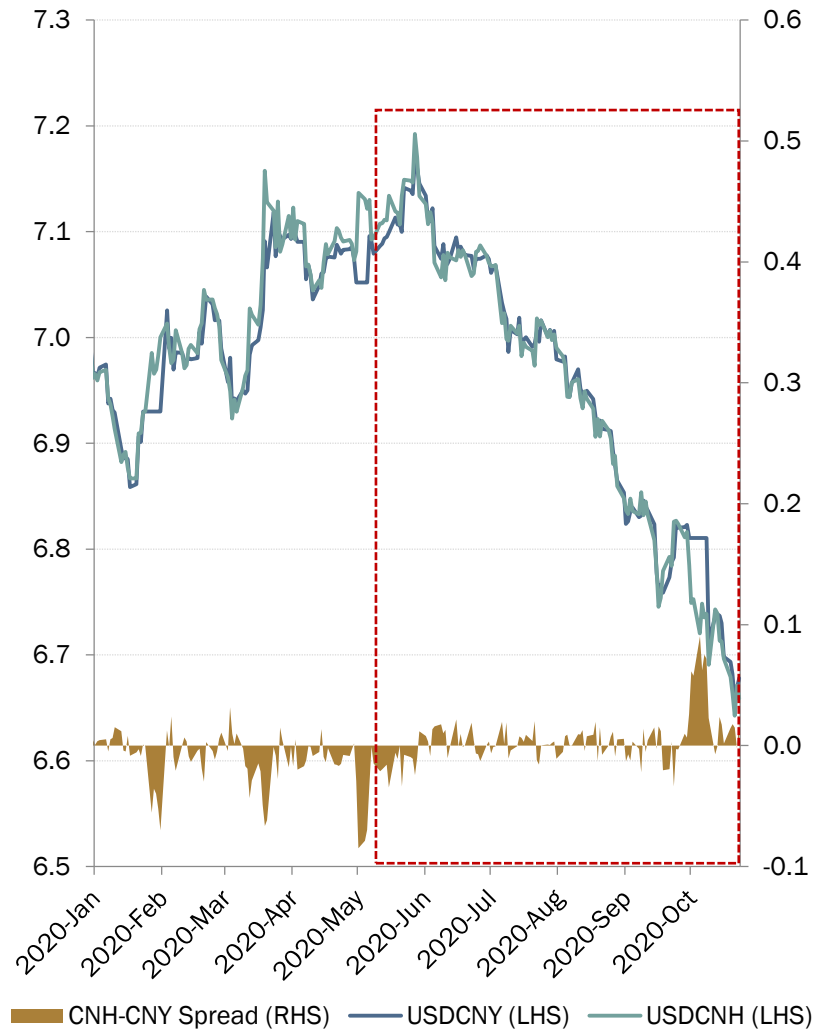
Note: \* NPC meeting in May has approved CNY 3.75tn worth of special purpose bond quota for 2020. By the end of H1 2020, more than CNY 2.37tn worth of special purpose bond have already been issued, accounting for nearly 65% of the annual quota.



# Dollar weakness and macro-recovery continue to fuel yuan rally

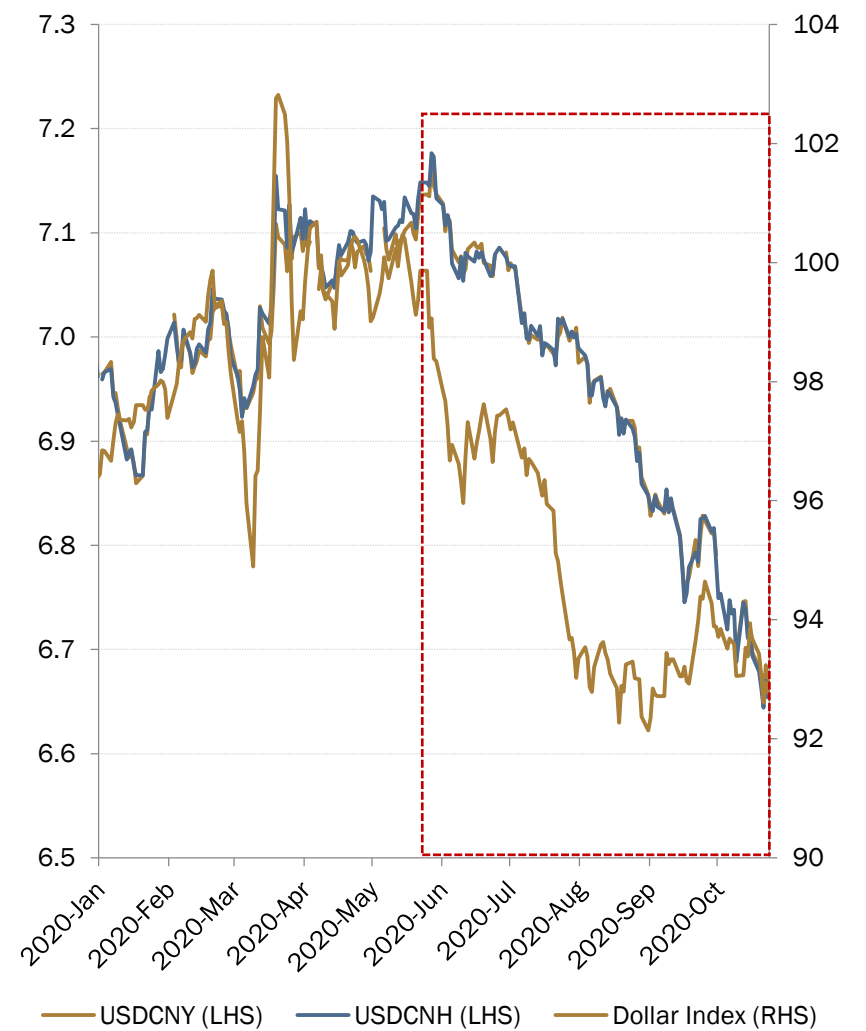
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Macro fundamentals support USD-CNY to hit new lows below 6.70



Source: WIND, ICBC Standard

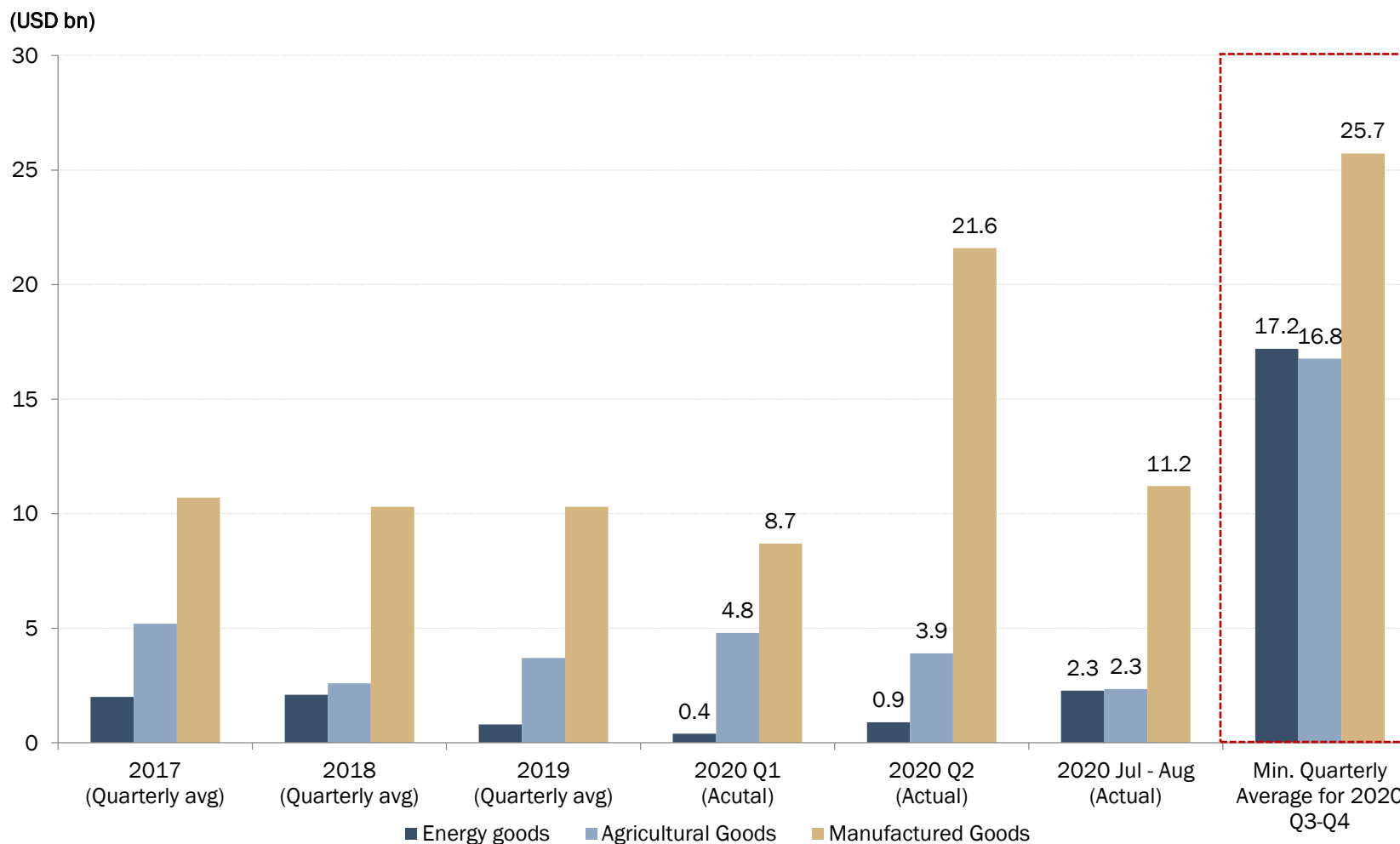
Pre-election dollar weakness supported CNY appreciation vs. USD



Source: Bloomberg, ICBC Standard

## Phase-One deal saw further progress but significant challenges remain

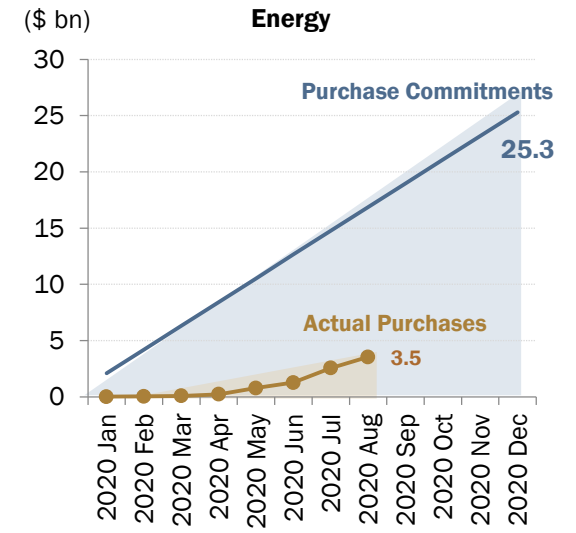
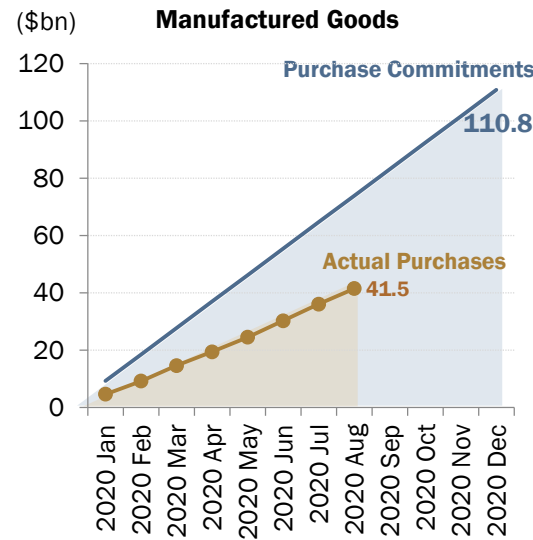
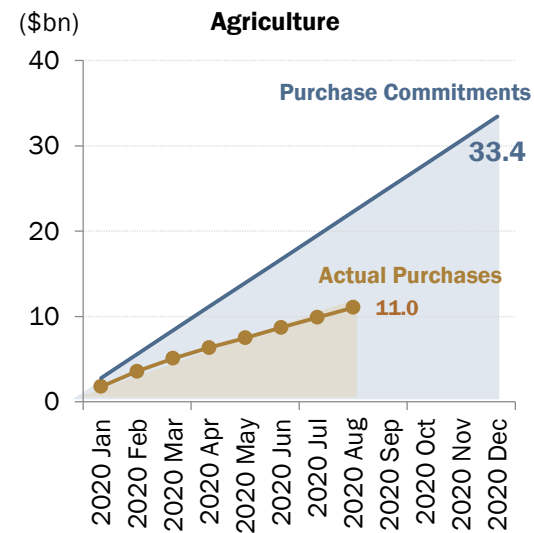
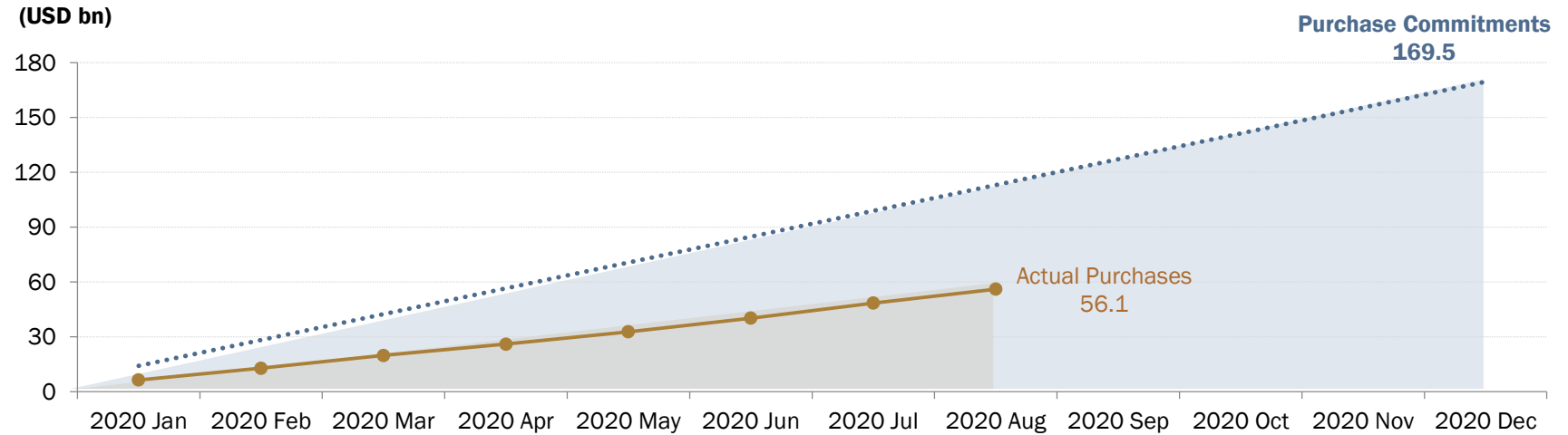
China has accelerated manufactured goods purchasing from the US since May, but the Phase-One deal commitments on agricultural and energy goods remain challenging to achieve before year-end.



Source: WIND, ICBC Standard

# Q4 new purchases would be essential to full completion of the deal

Through the first nine months of 2020, China's overall purchases from US were only at 33% of the US exports YTD targets.



Source: PIIE, ICBC Standard

## Appendix I: Key economic targets enlisted in the Government Work Report (2018 – 2020)

		2020	2019	2018
<b>GDP</b>	GDP Target (%)	<b>“Endeavour to achieve the 13<sup>th</sup> FYP target”</b>		6.0% - 6.5%
	Actual GDP (CNY bn)	–		99,086.50
	<i>Previous GDP growth rate (yoy %)</i>	6.10%		6.90%
<b>Fiscal</b>	Official Fiscal Deficit (CNY bn)	<b>3,760</b>	↑	2,760
	Official Fiscal Deficit Ratio (% GDP)	<b>&gt; 3.6%</b>	↑	2.8%
	Special Bond Quota (CNY bn)	<b>3,750</b>	↑	2,150
	Special Bond Quota (% GDP)	<b>3.75%</b>	↑	2.18%
	Special Sovereign Bond (CNY bn)	<b>1,000</b>	↑	NA
	Broad Fiscal Deficit Ratio (% GDP)	<b>&gt; 8.5%</b>	↑	5.0%
	Railway Infra-Investment (CNY bn)	<b>900</b>	↑	800
	Road and Water Transport Infra-Investment (CNY bn)	NA	-	1,800
	Tax Cuts (CNY bn)	<b>2,500</b>	↑	2,000
<b>Social</b>	Household Disposable Income Growth (yoy %)	"Same as nominal GDP growth rate"	=	"Same as nominal GDP growth rate"
	Urban New Job Creation (mn)	<b>9.0</b>	↓	11.0
	Unemployment Rate (%)	<b>6.0%</b>	↑	5.5%
	Poverty Reduction (mn)	10 estimated ("Eliminate extreme poverty")	=	10
<b>Monetary</b>	CPI (%)	<b>3.5%</b>	↑	3.0%
	New Loan Growth for SMEs (%)	<b>&gt; 40%</b>	↑	30%
	M2 (yoy %)	<b>“Markedly higher than 2019”</b>	↑	"Same as nominal GDP growth rate"
	Total Social Financing (yoy %)			"Reasonable growth"

Source: WIND, ICBC Standard

## Appendix II: April 17 Politburo meeting first laid out policy focus on “six guarantees”

Timeline	Policy Measures since end-March (see Appendix for previous measures)	Fiscal Policy	Monetary Policy
Mar.27 (Politburo meeting)	A key Politburo meeting marked <b>Beijing proposal to increase its fiscal deficit to 3.5% as a share of GDP (from a de-facto 3% ceiling)</b> , issue special sovereign debt and allow local governments to sell more infrastructure bonds as part of a package to stabilise the economy. The ramped-up spending on infrastructure investment could be backed by as much as <b>CNY 2.5-2.8 trillion worth of local government special bonds</b> . Beijing is also likely to have to <b>lower its economic growth target for 2020</b> , down from the original target of around 6% agreed in December 2019.	Y	
Mar.30	The PBOC reduces the interest rate on 7-day reverse repurchase agreements to 2.2% from 2.4% while injecting CNY 50 billion into the banking system. The rate cut was the largest of its sort since 2015.		Y
Mar. 31	The State Council called for lower reserve-requirement ratios for smaller banks, more infrastructure bond issuances by local governments, and other steps including tax exemptions on new-energy vehicle purchases. A State Council meeting pledged <b>another 1 trillion CNY of funding through the central bank’s relending and rediscounting program</b> , a cheaper credit line for small commercial lenders.	Y	Y
Apr. 3 (Politburo meeting)	Politburo leaders in a statement pledged a raft of measures to <b>strengthen the role of the market in land use, capital markets and labour mobility</b> to build a more efficient economy. The Politburo also called for improvements to the country’s stock market infrastructure, faster development of the bond market and actively expanding financial-sector opening., and interest rates reform.	Y	
	<b>PBoC announced cut of targeted Reserve Ratio Requirement (RRR)</b> for smaller banks by 1.0 percentage points in two phases. The targeted RRR cut will release around CNY 400 billion into the banking system.		Y
Apr. 17 (Politburo meeting)	The Politburo <b>for the first time put forward the goal of "six guarantees (六保)"</b> , which includes ensuring residents’ employment, a basic livelihood and market participation, food and energy security, supply chain stability, and grassroots operations. ‘Full-employment and undisrupted functioning of social fabrics’ as well as ‘people’s livelihoods’ have been identified as top priority by the government.	Y	
Apr. 17-20	<b>PBoC cut MLF rate by 20bps</b> to 2.95% from 3.15%, the lowest since 2017, and injected CNY 100bn via 7-day repo. The one-year LPR was subsequently lowered to 3.85% from 4.05%, and the five-year tenor dropped by 10bps to 4.65% down from 4.75%.		Y
Apr. 20	MoF approved another <b>CNY 1tn quota for special purpose bonds</b> to be placed by end-May. <b>NDRC outlined the five-year “New Infrastructure investment plan” worth CNY 10tn from 2020. 24 provinces have submitted CNY 8tn worth of infrastructure investment projects for 2020 so far</b> (see next slide).	Y	
Apr. 21	State Council lowered the bad-loan coverage ratio for medium-small sized banks by 20 bps in phases, to unleash additional credit to support small and micro-sized businesses.		Y

Source: WIND, ICBC Standard

## Appendix III: China's COVID-19 emergency relief policy package (Feb-Mar)

Timeline	Policy Measures	Fiscal Policy	Monetary Policy
Feb. 1	Import tariffs exemption for medical materials used in epidemic control until March 31.	Y	
	PBoC strengthened countercyclical adjustments of monetary policy through open market operations. Together with other financial regulators, the PBoC rolled out 30 policy measures to support enterprises.		Y
Feb. 3-4	PBoC added a net CNY 150bn liquidity to the interbank market. The total injection announced was CNY 1.6tn, the largest single-day addition of its kind since 2004.		Y
Feb. 5	State Council announced support for debt financing and insurance for virus-impacted firms, and <b>allowed local government to sell another CNY 848bn of bonds before March.</b>	Y	
Feb. 6	PBoC issued credit support for <b>enterprises heavily affected by the epidemic</b> (small and micro companies and key manufacturing sectors) <b>to borrow at record-low rate of 1.6%</b> through state-owned commercial banks. PBoC also provided CNY 300bn for large banks and selected local banks in Hubei and other severely-hit provinces.		Y
<b>Feb. 9</b>	State Council announced <b>total spending worth CNY 80.55bn as emergency funds</b> to mitigate against COVID-19 related shocks to the economy.	Y	
Feb. 15	<b>Various tax relief measures worth CNY 1tn (or about 1% of GDP),</b> including reductions in employers' required social insurance payments, lower electricity fees and VAT waivers.	Y	
Feb. 17-20	PBoC lowered MLF rate by 10bps to 3.15% from 3.25%, the lowest since 2017, and injected CNY 100bn via 7-day repo. PBoC lowered the benchmark borrowing costs for new corporate and household loans. The one-year LPR was lowered to 4.05% from 4.15%, and the five-year tenor was lowered to 4.75% down from 4.8%.		Y
Mar. 4	7 provinces announced <b>investment projects</b> worth CNY 25tn with <b>CNY 3.5tn to be fully allocated within 2020</b>	Y	
Mar. 12-13	PBoC allows a higher cap of 1.25 on foreign debt, a move aimed at helping smaller and private companies raise more funds overseas. PBoC also cut Reserve Requirement Ratio (RRR) by 0.5 - 1.0 percentage points for banks, freeing up an additional CNY 550bn liquidity to the interbank market to help virus-impacted companies. The RRR for large banks is currently 12.5%. Qualified joint-stock commercial banks would enjoy an additional cut of 100 bps.		Y

Source: WIND, ICBC Standard

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