DBS Flash

China: A mild recovery in sight

Economics/Growth/Monetary/Rates

DBS Group Research — January 20, 2020

Nathan Chow
Economist / Strategist

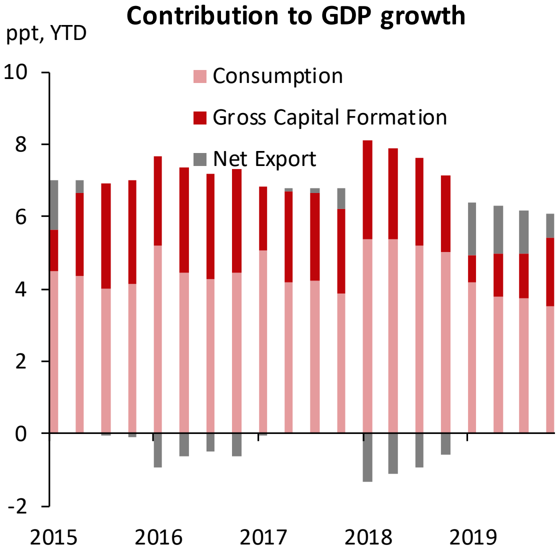
Samuel Tse
Economist

Please direct distribution queries to
Violet Lee +65 68785281 violetleeyh@dbs.com

- *Real GDP growth stabilized at 6.0% in 4Q19 from a further recovery in domestic activities in December.*
- *Full-year growth was 6.1% in 2019.*
- ***Implication to our forecast:** We expect another orderly growth slowdown to 5.8% in 2020.*
- ***Implication to our investor:** Liquidity injection should fuel upward pressure on asset prices.*

Real GDP growth stabilized at 6.0% in 4Q19 and brought full-year growth to 6.1% in 2019. The key driver was investment which contributed 1.9%pts to GDP in 4Q, up from 1.2%pts previously. For December, it went up to 5.4% YoY after having stayed at 5.2% for two months on liquidity injection.

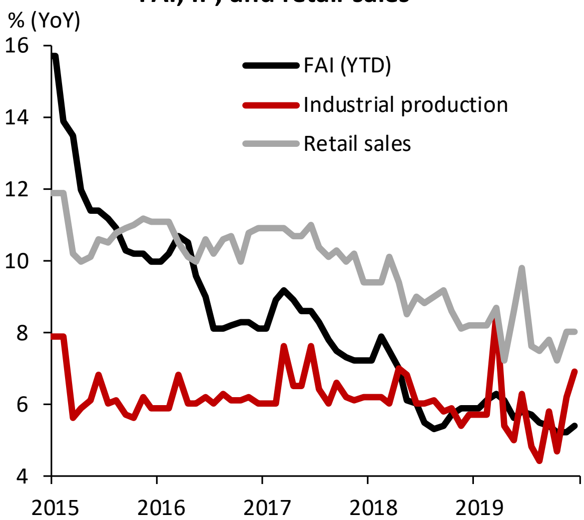
Contribution to GDP growth



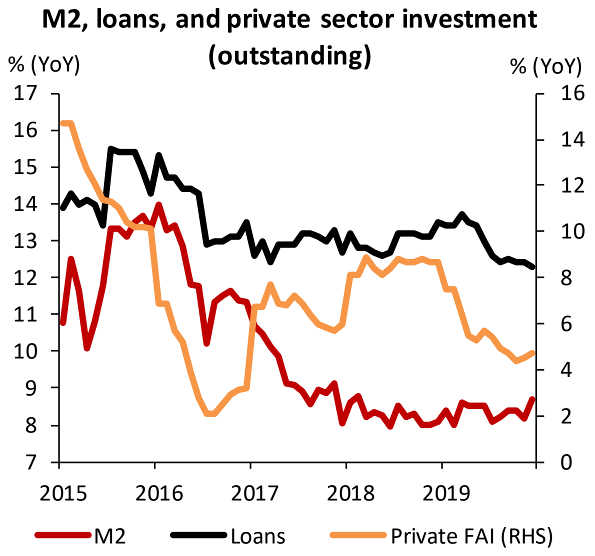
Source: CEIC, DBS

Thanks to monetary easing, private sector investment accelerated a second consecutive month to 4.7% in December from 4.4-4.5% in October-November. Growth in total social financing was steady at 10.7% YoY in December; slower growth in outstanding bank loans was offset by a smaller contraction in shadow financing. New yuan loans were also stable at 12.3%. The main drag from short-term corporate loans was balanced by the recovery in corporate bills long-term corporate loans.

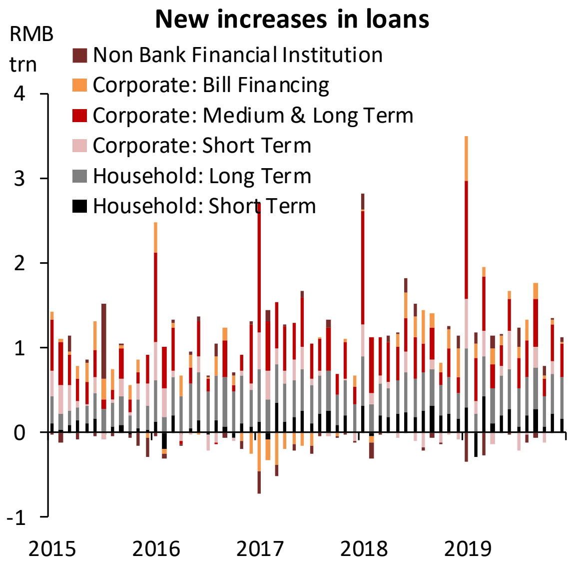
FAI, IP, and retail sales



Source: Bloomberg, DBS



Source: CEIC, DBS



Source: CEIC, DBS

Household loans continued to improve on robust mortgage demand. The uptick in money supply suggested an ongoing recovery in domestic demand. On the fiscal front, infrastructure spending will speed up in 2020 as reflected by increased local government bond issuances (up 4.8% in 2019). Special bond issuance had already begun in January. Accelerating commodities imports also pointed to more infrastructure investment ahead.

Industrial production rose by 6.9% YoY in December, up from 6.2% in November. Manufacturing industries growth picked up to 7.0% from 6.3% on the suspension of additional tariffs. Among all, auto production growth surged to 8.1% from 3.7%. **China and the US signed a Phase One trade deal on January 15.** While positive for market sentiment, the deal would only provide temporary relief to softening industrial activities.

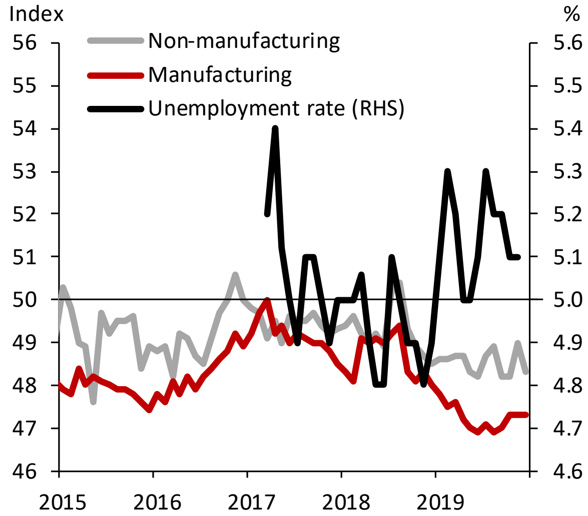
The outlook remains cautious. US has maintained tariffs on USD370bn worth Chinese exports. More importantly, China's hefty commitment to purchase an additional USD200bn worth of US goods and services by end-2021 will be a drag on its current account surplus. The threat of sanctions on tech remains. Core disputes such as intellectual property protection, state subsidies and greater financial market openness are unresolved and left to Phase 2 negotiations.

Retail sales growth was resilient at 8%. Auto sales rebounded to 1.8% after 5 straight months of YoY drop. Demand for luxury products such as gold, silver and jewellery also saw notable improvement. However, the **consumption outlook remains clouded by the weak labour market.** Hiring sentiment remained tepid on cloudy factory production outlook. Employment PMIs persistently stayed in contraction zone and jobless rate in urban areas stayed above 5% for 12 months in a row.

Elevated housing costs should also reduce available income for consumption. Property prices have risen for the 56th straight month in December.

As a result, more easing is needed to stabilize growth. Domestically, the private sector continued to suffer from high entry barriers and financing difficulties. Mild core inflationary pressures will provide PBoC more room to maneuver. Beijing's tolerance for leverage will be higher in 2020 to fulfil policy and growth targets (see "China: More PBOC cash injection ahead", January 16).

Employment PMIs and unemployment rate



Source: CEIC, DBS

In retrospect, PBoC's monetary policy in 2019 was less proactive compared to global peers. The yield differential between Chinese and US 10Y sovereign bonds has widened by 60 bps in 2019 and was last at 127 bps, above the 80-100bps gap preferred by Governor Yi Gang. Over the course of 2020, we are looking for a 40bps cut in 1Y Loan Prime Rate and more reductions in the banks' require reserve ratio to achieve an orderly growth slowdown to 5.8% this year while supporting asset prices.

Group Research

Economics & Macro Strategy

Taimur Baig, Ph.D.
Chief Economist - G3 & Asia
+65 6878-9548 taimurbaig@dbs.com

Chang Wei Liang
Strategist
+65 6878-2072 weiliangchang@dbs.com

Ma Tieying, CFA
Economist - Japan, South Korea, & Taiwan
+65 6878-2408 matieying@dbs.com

Nathan Chow
Strategist - China & Hong Kong
+852 3668-5693 nathanchow@dbs.com

Radhika Rao
Economist – Eurozone, India, & Thailand
+65 6878-5282 radhikarao@dbs.com

Masyita Crystallin, Ph.D.
Economist – Indonesia & Philippines
+62 21-2988-4003 masyita@dbs.com

Irvin Seah
Economist - Singapore, Malaysia, & Vietnam
+65 6878-6727 irvinseah@dbs.com

Eugene Leow
Rates Strategist - G3 & Asia
+65 6878-2842 eugeneleow@dbs.com

Samuel Tse
Economist - China & Hong Kong
+852 3668-5694 samueltse@dbs.com

Chris Leung
Economist - China & Hong Kong
+852 3668-5694 chrisleung@dbs.com

Duncan Tan
FX and Rates Strategist - Asean
+65 6878-2140 duncantan@dbs.com

Philip Wee
FX Strategist - G3 & Asia
+65 6878-4033 philipwee@dbs.com

Sources: Data for all charts and tables are from CEIC, Bloomberg and DBS Group Research (forecasts and transformations).