Macro Strategy

DBS Flash

China stimulus tracker: A one-year report card

Group Research

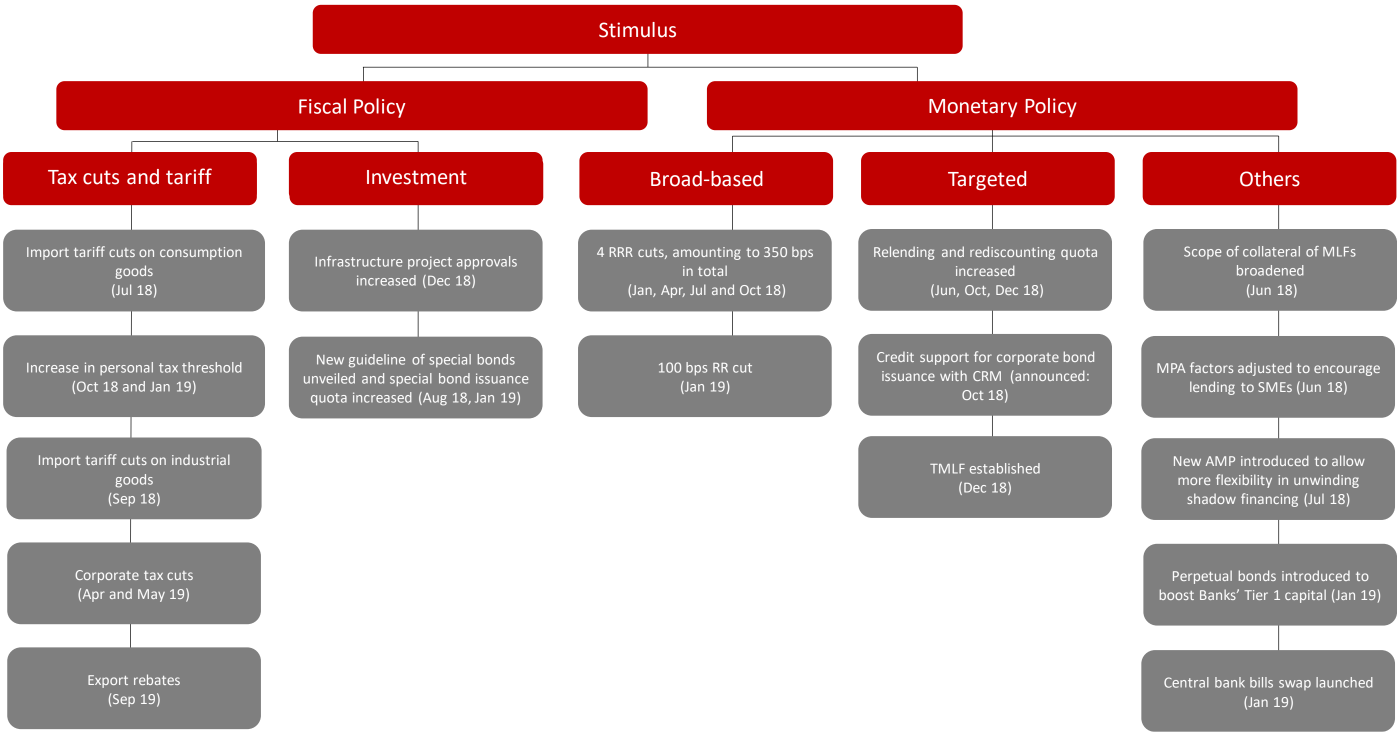
March 27, 2019

Nathan Chow
Strategist/Economist

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

- *Worries over China's economy have intensified since 2H18 due to faltering momentum of external trade and domestic demand.*
- *A moderate stimulus package and insistence on deleveraging indicate Beijing's increased tolerance for slower growth.*
- *Policy supports from reserve requirement ratio cuts to infrastructure binge are yielding positive results.*
- *Demand-side indicators – retail sales and investment – are showing signs of stabilization. But supply-side gauges such as production and employment remain subdued.*

Figure 1: Policy changes since 2018



Import tariff cuts on consumption goods

- Import tariffs on a range of consumer goods were slashed in July 2018, including tariff reductions on apparel (i.e. clothes, shoes, and hats), kitchenware, and fitness products from an average of 15.9% to 7.1%, and household appliances from an average of 20.5% to 8%.

Increase in personal tax threshold

- The threshold for collecting income taxes increased to RMB5,000 per month from RMB3,500 in October 2018.
- Effective January 2019, taxpayers can deduct expenses such as those relating to children's education, interest on home mortgages, housing rent and treatment for serious diseases.

***Impact:** Retail sales, which weakened sharply over Mar-Nov 2018, have started stabilizing. It rose 8.2% YoY in Jan-Feb spearheaded by online sales and catering sector. It grew 7.1% in real terms, up from 6.6% in December. Yet consumer confidence remained fragile due to job insecurity. Official unemployment rate was up from 4.9% in December to 5.3% last month, the highest in nearly two years.*

Import tariff cuts on industrial goods

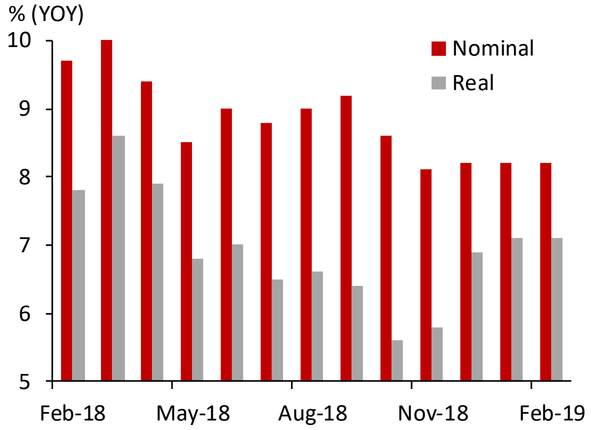
- Import tariffs on a range of industrial goods were slashed in September 2018. Tariff for electronic equipment was reduced from 12.2% to 8.8%; textiles and building materials from 11.5% to 8.4%.

Corporate tax cuts

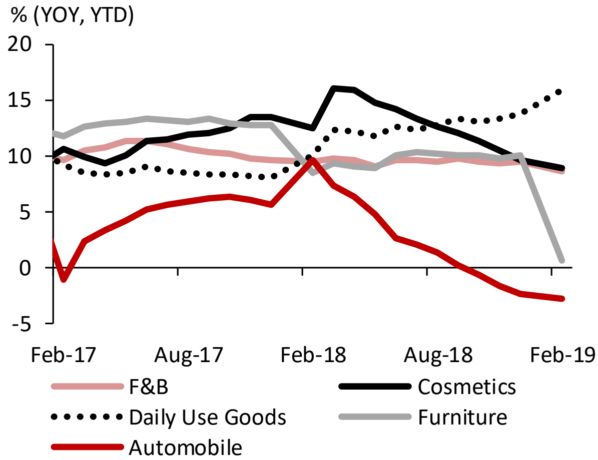
- The value-added tax (VAT) rate for manufacturers will be cut from 16% to 13%, and the VAT rate for the transport and construction sectors from 10% to 9%, effective April 1.
- The business sector's social security contributions will lower to 16% from 20%, effective May 1.

***Impact:** Improvement in industrial activities and profits were not clearly visible so far. Factory production grew at a nine-year low of 5.3% in Jan-Feb. Industrial profits fell 1.9% in December (-1.8% in November). For FY18, profits were up 10.3%, down sharply from FY17's 21%. While tax cuts are encouraging, the impact will take time to materialize owing to the deteriorating investment appetite. Factory deflation and faltering global demand will continue to damp optimism in the near term.*

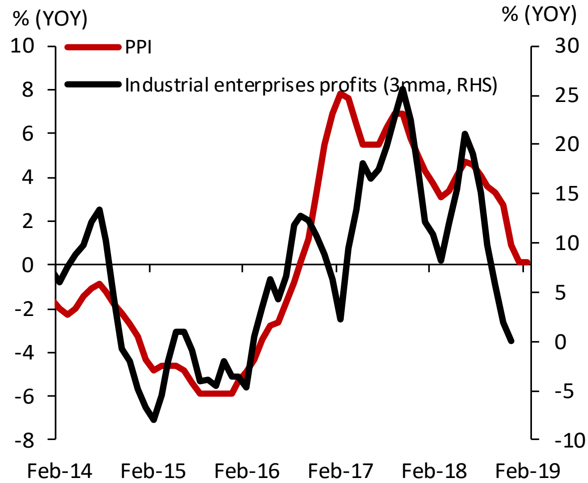
Nominal and real retail sales growth



Retail sales by category



PPI vs profits

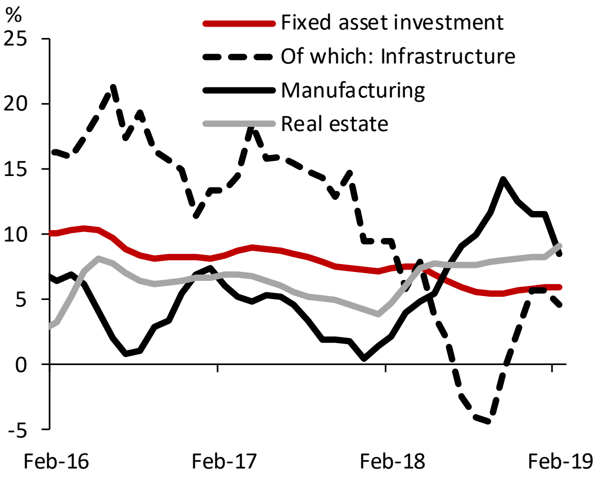


Infrastructure

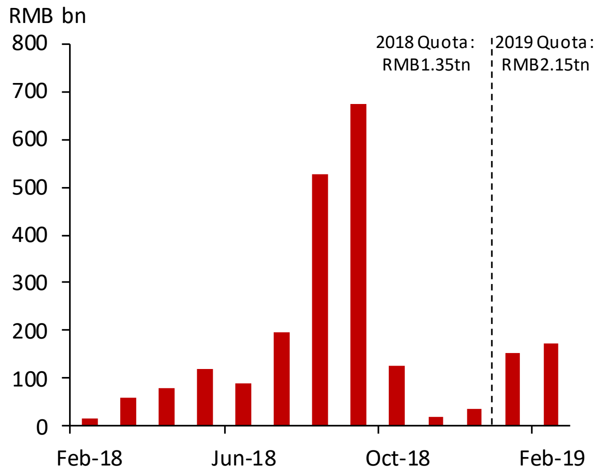
- Since the start of December, the National Development and Reform Commission (NDRC) has approved 16 projects, totaling RMB1.1tn in total.
- Policymaker plans to invest USD119bn to build 6,800-km railway in 2019, a 40% jump from the length of tracks laid last year. The intended railway lines will cover projects linking Beijing, Hebei, and other major locations across the country, as well as 14 remote and destitute areas, which accounts for two-third of China's railway infrastructure investment.

Impact: *Frontloading project approvals has already led to a recovery of infrastructure investment. After slowing to 3.3% in FY18, they recovered to 4.3% YTD. Spending on both roads and railways registered double-digit growth. Local governments plan to sell RMB2.15tn in special bonds this year, up from 2018's RMB1.35tn. Last year, more than 80% of infrastructure spending was funded by special bonds. A majority portion of bond proceeds will likely go into stimulus spending. We expect infrastructure investment to advance 10% in 2019.*

Fixed asset investment (YTD 3mma)



Special bond issuance

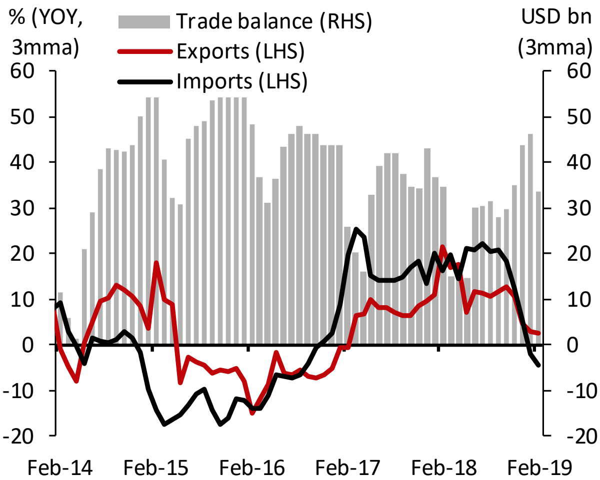


Export rebates

- Export tax rebates on 397 items have been raised in September to a range of products, including steel products, chemicals, lithium batteries, LEDs, multi-component semiconductors, machinery products, and books and newspapers. The 15-percent bracket and part of the 13-percent bracket have been lifted to 16%. The 9 percent notch has been adjusted to 10% or 13%, and the 5 percent tier to 6 or 10%.
- The government has also streamlined procedures for the rebate system to support foreign trade. Other measures include cutting customs clearance red tape, reducing the cost of customs procedures, and expanding export credit insurance.

Impact: *Even discounting the lunar new year effect, exports still fell almost 5% in Jan-Feb. While a likely resolution to the China-US trade war may lift sentiment, leading indicators for major trading partners (i.e. PMIs for the euro area and Japan) point to further export weakness ahead. The strengthening yuan also compromises the competitiveness of exporters.*

Merchandise trade

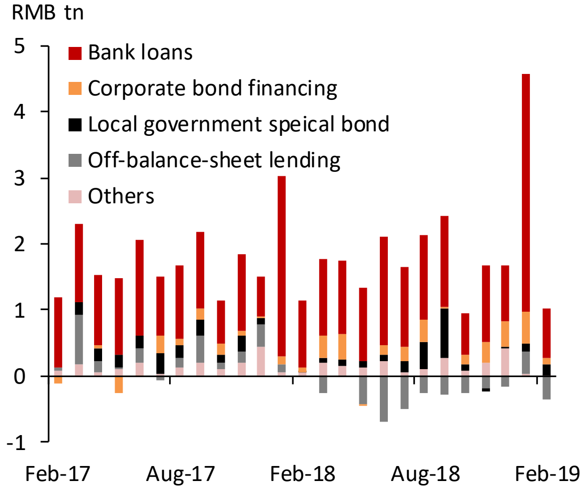


Monetary loosening

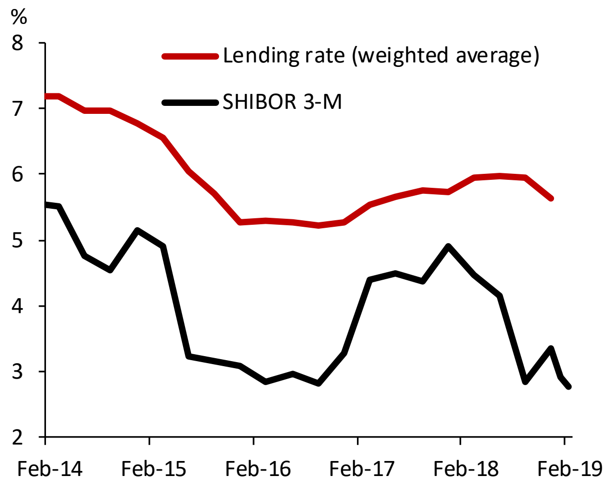
- The PBoC has cut the RRR by 350bps since of 2018, releasing an estimated RMB4.8tn into the system.
- MPA factors were adjusted to encourage lending to SMEs in June 2018.
- The authority increased the relending and rediscounting quota by RMB150bn for small and micro companies and private enterprises in October 2018.
- Targeted medium-term lending facility was introduced in December 2018 to encourage loans to small and private business.
- Perpetual bonds and central bank bills swap were introduced in January 2019 to boost banks' tier 1 capital.

Impact: *Liquidity conditions eased somewhat on entering 2019. Aggregate financing increased by 10.2% in Jan – Feb combined, 0.4ppt higher than that in December. More appreciable increases were found in bank loans. In February, share of long-term corporate loans to total loans increased to 58% from 43% in January. Meanwhile, the average lending rates have fallen too. But risk appetite has remained weak in the financial sector, where liquidity could not be transmitted to SMEs. Resolving this is a daunting challenge.*

Total social financing (new increase)



RRR and interest rates



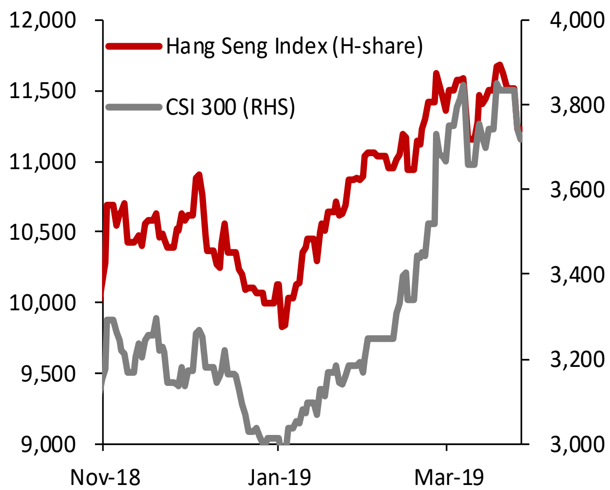
Equity market support

- In October 2018, the banking and insurance regulator issued rules clearing insurance companies to invest in stocks through specialized products. The move was intended to provide long-term, stable funding support for high-quality listed companies. It also mitigates liquidity risks related to shares pledged as collateral for loans.

- In January 2019, the Shanghai and Shenzhen stock exchanges have loosened the rules on repurchasing pledged stocks. Shareholders can since extend the repurchase period to more than three years. To compare, they were previously required to buy back the shares they had pledged as collateral for loans within three years.

Impact: *Equity markets are marching upwards due to easing SINO-US trade tensions and loosening regulation. Hang Seng Index (H-share) and CSI 300 index have soared 10.9% and 24.3% since January respectively in spite of weakening economic fundamentals.*

Chinese stock performance

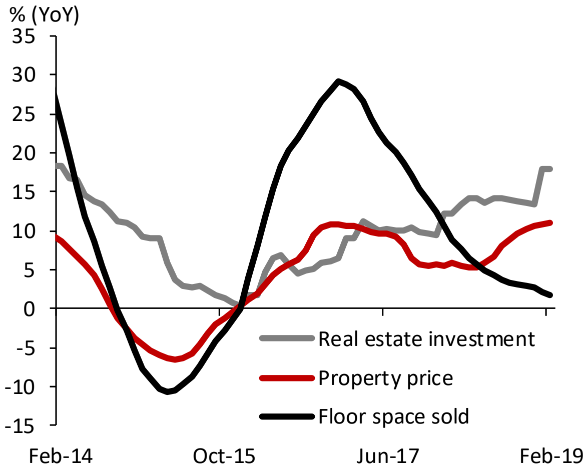


Property easing

- Since 4Q18, more than 10 Chinese cities have loosened property curbs marginally through various means, such as revising down mortgage rates and lowering the threshold for obtaining residency permits – a prerequisite for buying homes. Below are some of the recent loosening measures in individual cities:
  - For example, Heze, a prefecture-level city in Shandong province, has cancelled the three-year reselling ban imposed in 2017 and given the green light for developers to use more of the capital from pre-completion sales.
  - Guangzhou residents who had paid towards a housing provident fund policy could withdraw money for buying homes for living in nearby cities such as Foshan and Dongguan.

Impact: *January-February property investment rose 11.6% YoY, up from FY18's 9.5%. The rebound is not easy to sustain because of persistent weakening of home sales and land purchases. Recent pullback in housing starts mirrors the ongoing cautiousness of developers.*

Residential housing growth



Group Research

Economics & Strategy

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

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

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

Joanne Goh
Regional equity strategist
+65 6878-5233 joannegohsc@dbs.com

Neel Gopalakrishnan
Credit strategist
+65 6878-2072 neelg@dbs.com

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

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

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

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

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

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

Samuel Tse
Economist - China & Hong Kong
+852 3668 5695 samueltse@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).