Economics

DBS Flash

China: Stimulus is working; more coming

Group Research

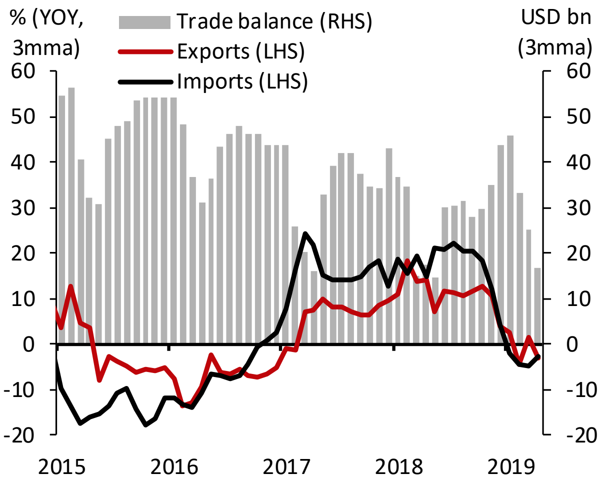
May 10, 2019

Samuel Tse
Economist

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

- *Exports dropped 2.7% YoY from 13.8% in March while imports bounced back by 4.0% from -7.6%*
- *The consumer price inflation accelerated to 2.5% in April from 2.3% in March*
- *Outstanding aggregate financing growth inched down from 10.7% to 10.4%*
- *Downward pressure on local interest rate will soon resume*

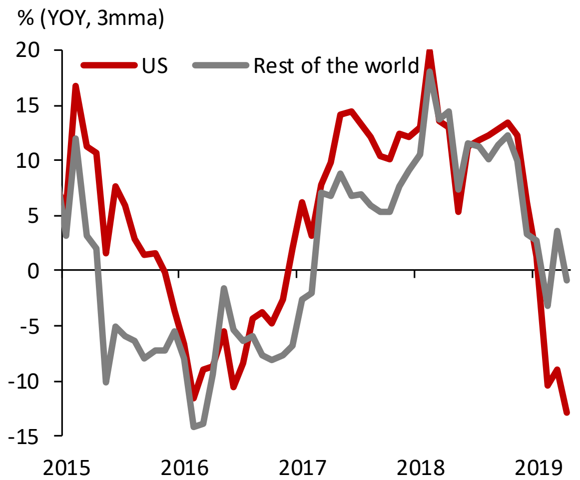
Chart 1: Merchandise trade



Source: CEIC, DBS Group Research

China's export performance (-2.7% YoY) turned sluggish in April (Chart 1). The weak early indicator, April's NBS Manufacturing new export orders PMI (stayed in the contraction zone for 11 straight months), pointed to a lacklustre trade environment (Chart 2). Amid the weakening global demand, export growth to the EU dropped to 6.5% from 23.7% alongside the continued downtrend of its PMI of (edged down to 51.5 from 51.6). Outward shipment to Japan also fell by 16.3%, the biggest drop since Feb16 (its PMI stayed at 50.4, the lowest reading since Sep16).

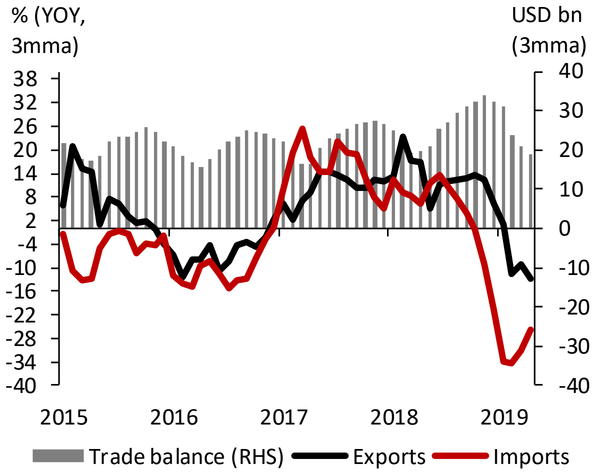
Chart 2: Exports to US and rest of the world



Source: CEIC, DBS Group Research

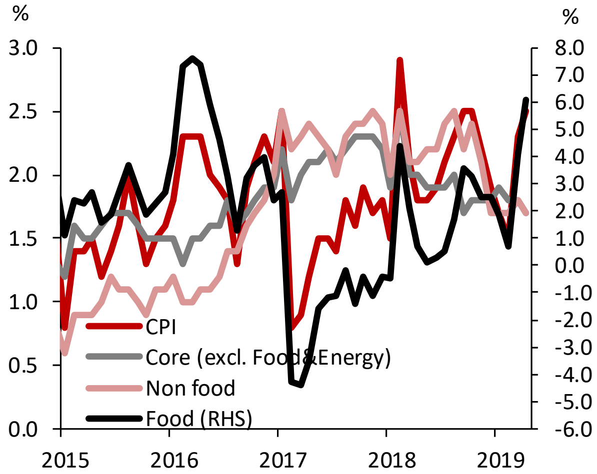
The outlook of the external environment is cloudy due to lingering trade tension with the US. US President Trump has threatened that tariffs on USD200bn of imports from China will rise from 10% to 25% on Friday. The Chinese delegation will be visiting the US despite the looming threat. Potential higher tariff for the rest of the Chinese imported goods (mainly consumer goods) is also on the cards. Export to the US in April dropped 13.1%, compared to the 3.7% advance in March. Yet, the trade balance increased from USD20.5bn from USD21.0bn due to slumping import (-25.7%) from the US (Chart 3).

Chart 3: Trade balance vis-à-vis the US



Source: CEIC, DBS Group Research

Chart 4: CPI by category

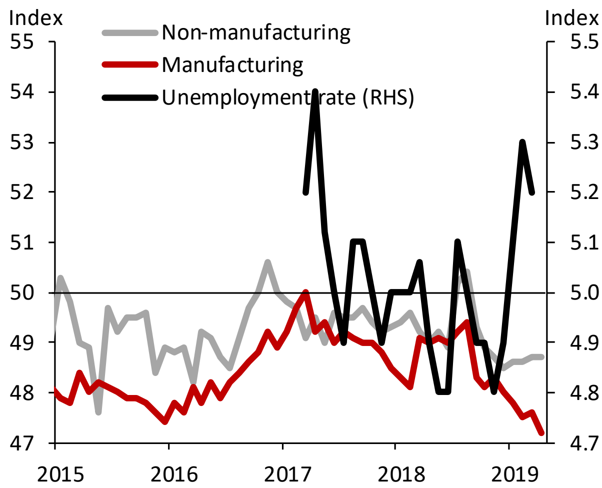


Source: CEIC, DBS Group Research

Imports growth was 4.0% in April on the back of gradually improving domestic demand. Headline NBS Manufacturing PMI was above 50 for the second time since Nov18, with the import component improved from 48.7 to 49.7. In fact, the industrial production and fixed asset investment surge to 8.5% and 6.3% in March from 5.3% and 6.1% registered in Jan-Feb respectively due to large-scale stimulus policy. These increased the demand for commodities such as oil, copper and coal. The respective import volumes increased by 10.8%, 6.6% and 13.5%. The rise in commodity price fuelled upward pressure to headline import figure. For instance, iron ore price jumped over 30% from its year-low. WTI crude oil prices rebounded 45% in the past 4 months to USD62/barrel. Import of these products in value terms is even higher than that in volume terms (oil: 4.3% ppt higher; iron ore: 25.7ppt). Meanwhile, the China-US trade deal also boosted soybeans import. The inward shipment soared by 10.4% in volume terms/2.9% in value terms due to the decrease of value-added tax for the product effective in April. This is the first YoY increase since Nov18.

The CPI was up 2.5% YoY in April from 2.3% in March (Chart 4). Food inflation was 6.1%, with pork prices jumping by 14.4% YoY in April after recording 25 consecutive declines till March. This was the strongest increase since Jun16 and was largely due to the swine fever outbreak. Reportedly, China's pork production fell 5% in 1Q19 and is expected to see a bigger drop in the quarters ahead. The pig stock also saw a 18.8% drop in March according to the Ministry of Agriculture and Rural Affairs. Pork prices are likely to stay elevated.

Chart 5: Employment PMI

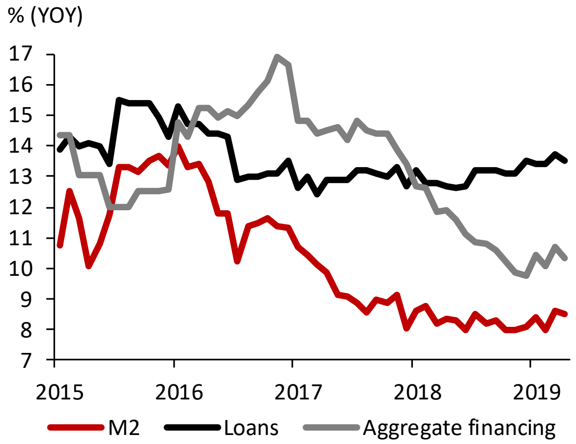


Note: Surveyed Unemployment rate in Urban Areas is only available since Jan17.

Source: CEIC, DBS Group Research

Non-food inflation also edged down to 1.7% YoY in April from 1.8% in March. Among all, the increase in prices of traffic and communication ease to -0.5% despite higher energy prices. Rent and healthcare & medical service also saw modest easing from 2.4% to 2.2% and 2.7% to 2.6% respectively. **Core inflation (excluding energy and food prices) edged down from 1.8% to 1.7%.** Consumption sentiment was dampened by weaker expectation of future income growth alongside a weakening labour market. The employment PMI for manufacturing sector went down to its 8 year-low of 47.2, while that of the non-manufacturing counterpart stayed in contraction zone for the 8th consecutive month (Chart 5). Unemployment rate also stayed above 5.0% for over 7 months. This will exert downward pressure on wage. According to the PBoC's Urban Depositor Survey, inflation expectation was the third lowest since 2010. Only 26.8% of the respondents expected prices to surge. **As such, we maintain our inflation forecast of 2.3% for 2019 (2018: 2.1%).**

Chart 6: M2, loans, and aggregarate financing (outstanding)

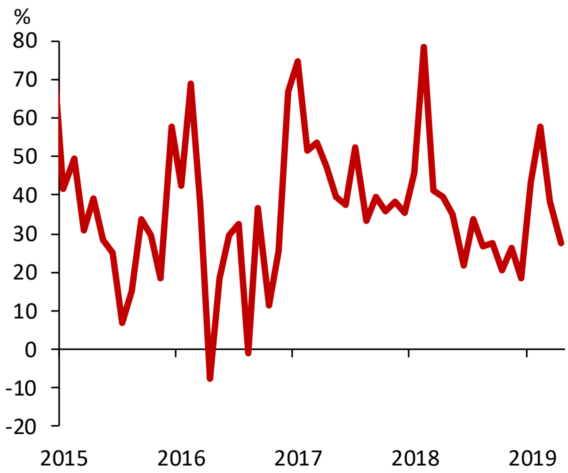


Source: CEIC, DBS Group Research

Monetary condition tightened somewhat last month. M2 growth inched down from 8.6% to 8.5% in April. Outstanding aggregate financing growth also eased back from 10.7% to 10.4%. Bank loan also drop from 13.7% to 13.5% (Chart 6). The corporate loan as percentage of total loan shrank, thereby suggesting a weak borrowing demand (Chart 7). Premature policy normalization could risk choking off growth momentum (see: "Economy still fragile despite stabilization policies", April 30). The escalated trade tension with US also warrants accommodative stance on monetary policy to stay.

Earlier this week, the PboC cut reserve requirement ratio (RRR) releasing RMB 280bn for small to medium size banks. Banks with assets lower than RMB 10bn will be subject to RRR of 8%. About 1,000 small banks will benefit. The latest cut will put downward pressure on the 7-day repo rate, and subsequently drive down average lending rates. Looking ahead, a broad-based easing is likely given persistent trade tensions (see: "RRR cut signals PBoC still supportive", May 06).

Chart 7: Corp. long term loan/total loan



Source: CEIC, DBS Group Research

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

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).