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Written by Tian Yong Woon

More On China

In this week's newsletter, we return our focus to China, which has recently released its latest economic data and concluded its Third Plenum meeting. While acknowledging disappointing economic indicators, we also recognize China's shift away from pursuing growth for its own sake, moving instead toward prioritizing the quality of its growth. However, we highlight persistent weaknesses in China's property sector, amid continued declines in property prices despite support measures announced earlier this year. Turning to the Third Plenum meeting, which provided limited details and signaled no major policy changes, we emphasize China's renewed emphasis on “Chinese modernization” and "high-quality development". We discuss the country's ongoing challenges, particularly its growing trade surplus with the rest of the world, the resulting trade frictions, and accusations of overcapacity and dumping.

Broadly reviewing our findings, it is evident that China's strategic focus on shifting towards high-quality growth remains steadfast. However, the economy must contend with several challenges. These include uneven growth momentum, escalating debt levels, lingering weaknesses in consumer and business sentiment, potential trade-related actions by other economies, and a fragile property sector. Therefore, we might observe ongoing challenges for the Chinese economy in the near term before growth gains an even footing. It is perhaps in response to these challenges that the central bank decided earlier today to lower several policy rates by 10 basis points each. Namely, the 7-day reverse repo rate now stands at 1.7%, while the one-year loan prime rate (LPR) has been reduced to 3.35% and the five-year LPR to 3.85%.

China’s recent dataflow

The latest dataflow from China has been largely disappointing. GDP growth slowed to 4.7% y/y in Q2, marking the slowest pace of growth in five quarters (Chart 1). Monthly data releases revealed more specific setbacks: retail sales growth unexpectedly dropped to 2% y/y in June, and industrial production growth cooled to 5.3%. Looking more broadly, however, it can also be argued that China's slowing economic growth was inevitable, given its stage of development and the challenges it faces, such as an ageing population. This is notwithstanding significant leaps in productivity brought about by technological advances. Furthermore, China has been restructuring its economy, shifting its focus from pursuing high growth rates for their own sake to prioritizing the quality of growth. This includes assessing the sources and drivers of growth, a topic we will explore further below in an upcoming segment.

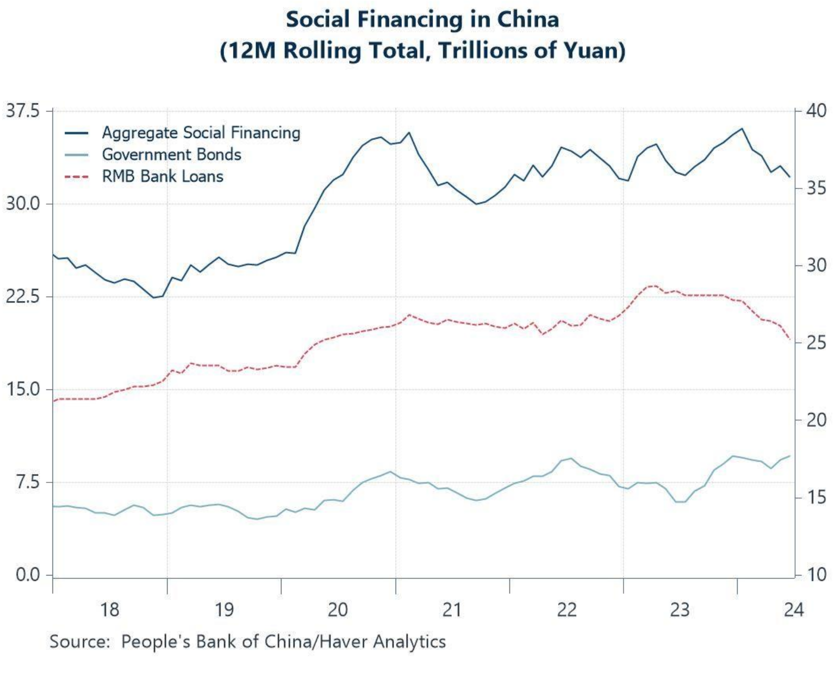
Chart 1: China GDP and monthly indicators

Apart from those aforementioned economic growth indicators, additional data revealed a further decline in house prices across China in June, underscoring persistent weakness in the property sector and despite government support measures. According to our GDP-weighted index of property prices (Chart 2), new home prices dropped 4.2% y/y, while existing home prices saw a steeper decline of 8.4%. To recap, recent efforts by the authorities include easier mortgage regulations and 300 billion yuan ($41.3 billion) of funding to help state-owned enterprises absorb surplus housing inventory. However, despite these policy interventions, many analysts remain cautious about calling a bottom in China's property sector, primarily due to persistent oversupply that continues to weigh on real estate prices.

Chart 2: Property prices in China

Tying into the ongoing weakness in China's property market is subdued sentiment in the country's credit environment. As depicted in Chart 3, social financing in China, measured by the 12-month rolling total flows, has been declining, primarily driven by reductions in yuan-denominated bank loans. Furthermore, government bond issuance, although rising, has provided only a partial offset. Delving deeper into the factors behind the decline in yuan-denominated bank loans, we observe two trends. Loans to nonfinancial firms, government agencies, and organizations have been decreasing since early 2023. However, it was only this year that loans to households started to decline on a 12-month rolling basis. Despite China's authorities maintaining accommodative monetary conditions to facilitate lending, the trends mentioned above underscore the persistent weakness in credit demand in the economy.

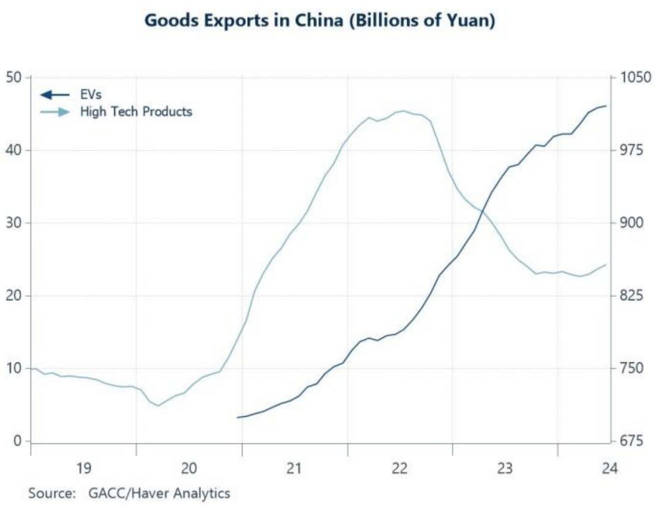
Chart 3: Social financing in China



China's Third Plenum meeting

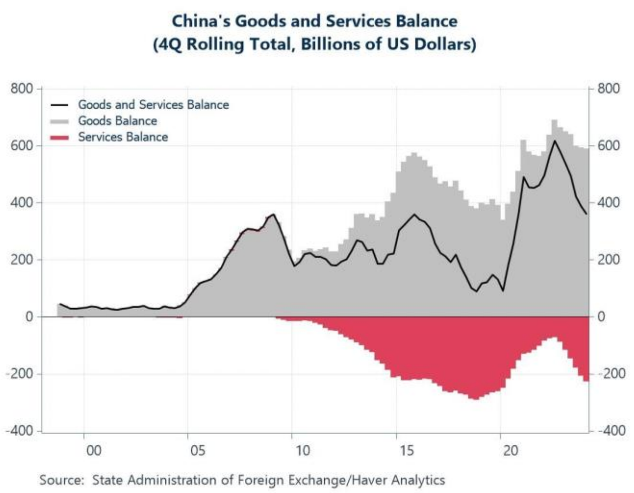
Next, we'll touch on key insights emerging from last week's closely watched Third Plenum meeting. While light on policy specifics, the post-meeting communique indicated no significant shifts in China's policy trajectory. However, there were repeated references to "Chinese modernization" and "high-quality development," underscoring China's ongoing commitment to these areas. These priorities have long been central to China's economic strategy, though assessing overall progress remains challenging. For instance, while China has seen a steady increase in its exports of electric vehicles in recent years, shipments of what it classifies as "high-tech" products have encountered difficulties, as shown in Chart 4. That being said, China's challenges with its exports of certain goods are also intertwined with geopolitical factors. These factors encompass concerns regarding overcapacity within China and allegations of dumping by other economies, which we will delve into further in a later section.

Chart 4: Goods exports in China



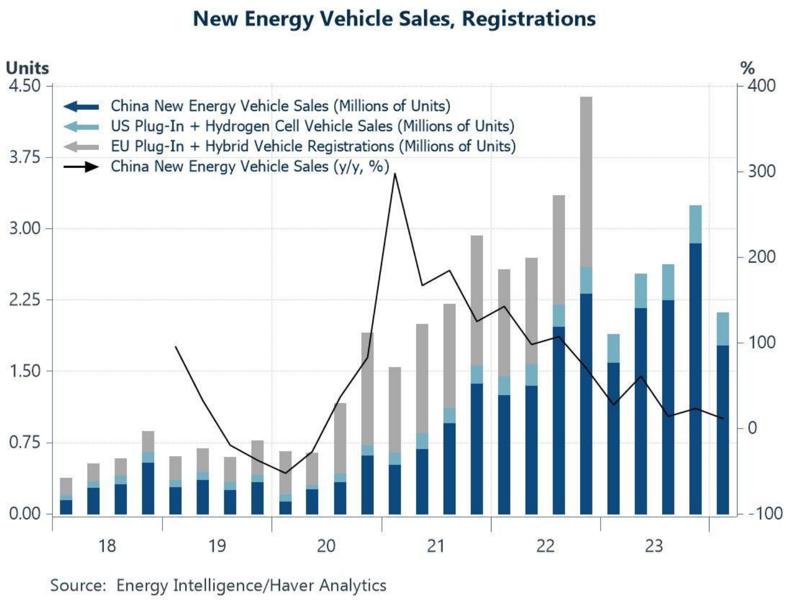
Looking broadly, as depicted in Chart 5, China's goods and services balance with the rest of the world, measured on a rolling 4Q basis, surged following the onset of the pandemic. This increase was driven by a combination of an improved goods surplus and a reduced services deficit. However, this balance peaked in Q3 2022 before receding, primarily due to the resumption of international travel impacting the services balance. While a robust goods surplus benefits the Chinese economy by boosting export revenues and, consequently, GDP growth, officials from several economies, including the US, have voiced concerns about these trends. One major accusation relates to that of "dumping," where China allegedly exports artificially low-priced products to these economies, undercutting local producers. Of particular concern is the potential erosion of domestic production capabilities in critical industries like electric vehicles (EVs) and solar panels.

Chart 5: China's goods and services balance



With that said, proponents of free market economics could argue that paying lower prices for goods benefits consumers overall. If a producer has a comparative advantage and can manufacture goods at lower costs, it theoretically enhances efficiency and consumer welfare. Moreover, in today's globalized economy, it is uncommon for domestic supply to perfectly match domestic demand due to varying advantages and disadvantages across economies. The imperfect match can arise from demographics, geography, and resource endowments, among other factors. Therefore, some degree of oversupply within economies is inevitable, with excess production often exported to meet demand elsewhere. However, underlying trade tensions often stem from concerns over economies' competitive advantages. These may arise along the dimensions of capabilities, market share, and expertise in future-oriented technologies – such as EVs (Chart 6) – which are critical for national security.

Chart 6: EV sales and registrations



About the author

Haver Analytics is pleased to bring Tian Yong Woon's commentaries on the state of the global economy to its clients.

Tian Yong joined Haver Analytics as an Economist in 2023. Previously, Tian Yong worked as an Economist with Deutsche Bank, covering Emerging Asian economies while also writing on thematic issues within the broader Asia region. Prior to his work with Deutsche Bank, he worked as an Economic Analyst with the International Monetary Fund, where he contributed to Article IV consultations with Singapore and Malaysia, and to the regular surveillance of financial stability issues in the Asia Pacific region. Tian Yong holds a Master of Science in Quantitative Finance from the Singapore Management University, and a Bachelor of Science in Banking and Finance from the University of London.

Data featured in this commentary:

Chart 1: China GDP and monthly indicators
Series 1: yryr%(N924TRS@EMERGEPR)
N924TRS@EMERGEPR [China: Retail Sales (NSA, 100 Mil.Yuan)]
Series 2: N924GDXY@EMERGEPR
N924GDXY@EMERGEPR [China: Real Industrial Value Added (NSA, Y/Y %Chg)]
Series 3: N924NGPY@EMERGEPR
N924NGPY@EMERGEPR [China: Real GDP: Year-to-Year Percent Change (%)]

Chart 2: Property prices in China
Series 1: yryr%(N924HWM@EMERGEPR)
N924HWM@EMERGEPR [China: 70 Cities: Price of New Commercial Residential Buildings (NSA, 2020=100)]
Series 2: yryr%(N924HK@EMERGEPR)
N924HK@EMERGEPR [China: 70 Cities: Price Index of Existing Residential Buildings (NSA, 2020=100)]

Chart 3: Social financing in China
Series 1: movt(N924FCTM@EMERGEPR,12)
N924FCTM@EMERGEPR [China: Aggregate Social Financing Flows to the Real Economy (NSA, 100 Mil.Yuan)]
Series 2: movt(N924FCTG@EMERGEPR,12)
N924FCTG@EMERGEPR [China: Social Financing Flows: Government Bonds (NSA, 100 Mil.Yuan)]
Series 3: movt(N924FCTB@EMERGEPR,12)
N924FCTB@EMERGEPR [China: Social Financing Flows: RMB Bank Loans (NSA, 100 Mil.Yuan)]

Chart 4: Goods exports in China
Series 1: movt(N924IE8F@EMERGEPR,12)
N924IE8F@EMERGEPR [China: Exports: Electric Cars (NSA, Mil.USD)]
Series 2: movt(N924IEQ9@EMERGEPR,12)
N924IEQ9@EMERGEPR [China: Exports: High Tech Products (NSA, Bil.USD)]

Chart 5: China's goods and services balance
Series 1: movt(N924ACGS@EMERGEPR,4)
N924ACGS@EMERGEPR [China: BOP: Current Account: Goods and Services (Mil.US$)]
Series 2: movt(N924ACG@EMERGEPR,4)
N924ACG@EMERGEPR [China: BOP: Trade in Goods: Balance (NSA, Mil.US$)]
Series 3: movt(N924ACS@EMERGEPR,4)
N924ACS@EMERGEPR [China: BOP: Trade in Services: Balance (NSA, Mil.US$)]

Chart 6: EV sales and registrations
Series 1: CNBMAM@NED
CNBMAM@NED [China: New Energy Vehicle Sales (Units)]
Series 2: (USBTAM@NED + USBPAM@NED)
USBTAM@NED [United States: Hydrogen Fuel Cell Electric Vehicles: Sales (Units)][AGG=SUM, Default]
USBPAM@NED [United States: Plug-in Electric Vehicles: Sales (Units)][AGG=SUM, Default]

Series 3: (E1BPAQ@NED + E1BPAQ@NED)
E1BPAQ@NED [European Union: Plug-in Electric Vehicles: Registrations (Number)]
E1BPAQ@NED [European Union: Plug-in Electric Vehicles: Registrations (Number)]
Series 4: yryr%(CNBMAM@NED)
CNBMAM@NED [China: New Energy Vehicle Sales (Units)]

For more info on our data offerings please contact our team on sales@haver.com.