




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# CHINA: SCARRING AND STIMULUS

Rory Green

May 2023

# SUMMARY

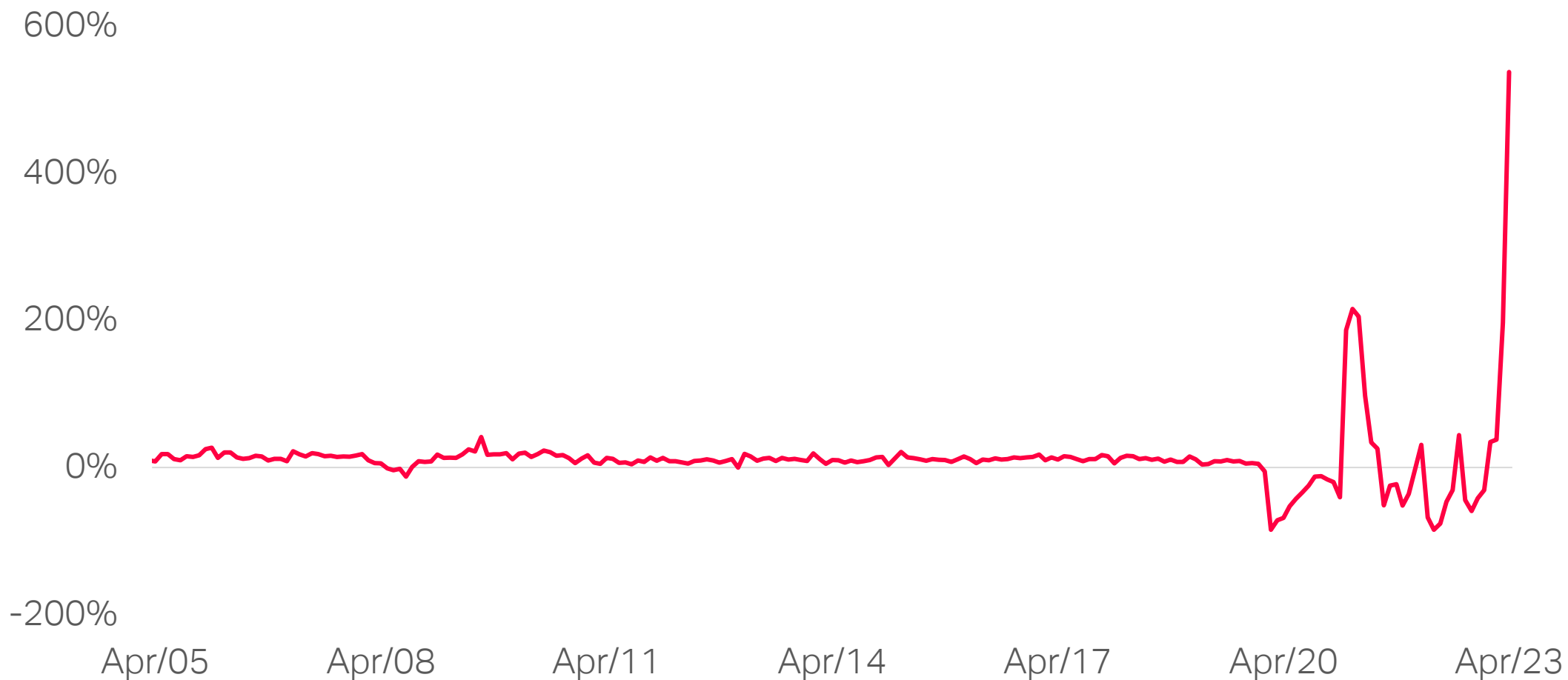
- **Lopsided recovery losing momentum.** Reopening sets up strong H1. H2 slowdown. Full year 5.7% yoy
- **Service spending soaring.** But investment and manufacturing weak and will remain so
- **China is heavily scarred.** 1) Covid 2) Property crash 3) “Common Prosperity” shift – leave a long hangover
- **Property green shoots on unstable ground.** Sales sluggish, and investment negative through 2023
- **Fiscal stimulus to the fore.** Bond issuance points to mid-year infrastructure bounce
- **Money trap.** PBoC will stay loose but “balance sheet recession” lowers efficacy of policy transmission
- **Q3/23 graduate woes likely to trigger extra round of stimulus around mid-year**
- **Global demand and inflation spillovers mild.** Service spending does not drive commodity imports
  
- **Beyond 2023 China is entering a structural slowdown.** The “3D’s” debt (property), decoupling, and demographics will push potential growth rates to 4% before dropping to 2-3% yoy in 10 years’ time
- **Beijing is betting on advanced tech and consumption to power growth**

## Market implications

- **Our favoured transition trades are:** long A Share consumer equities and USDCNY, we are neutral rates
- **Beyond the cycle,** we are negative RMB + traditional commodities but bullish CGBs and policy equities

# SERVICES SURGING

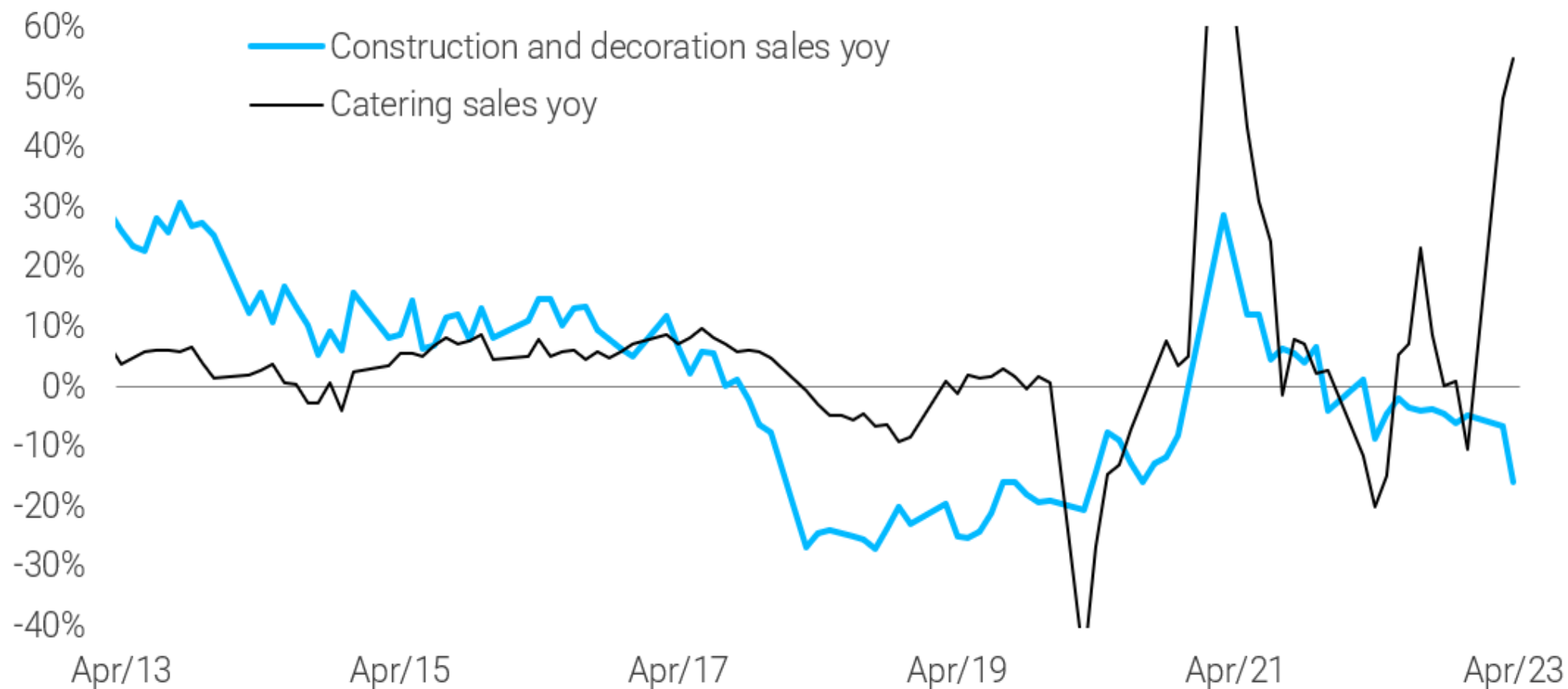
## Airline passengers yoy



Sources: CEIC, TS Lombard.

# LOPSIDED RECOVERY

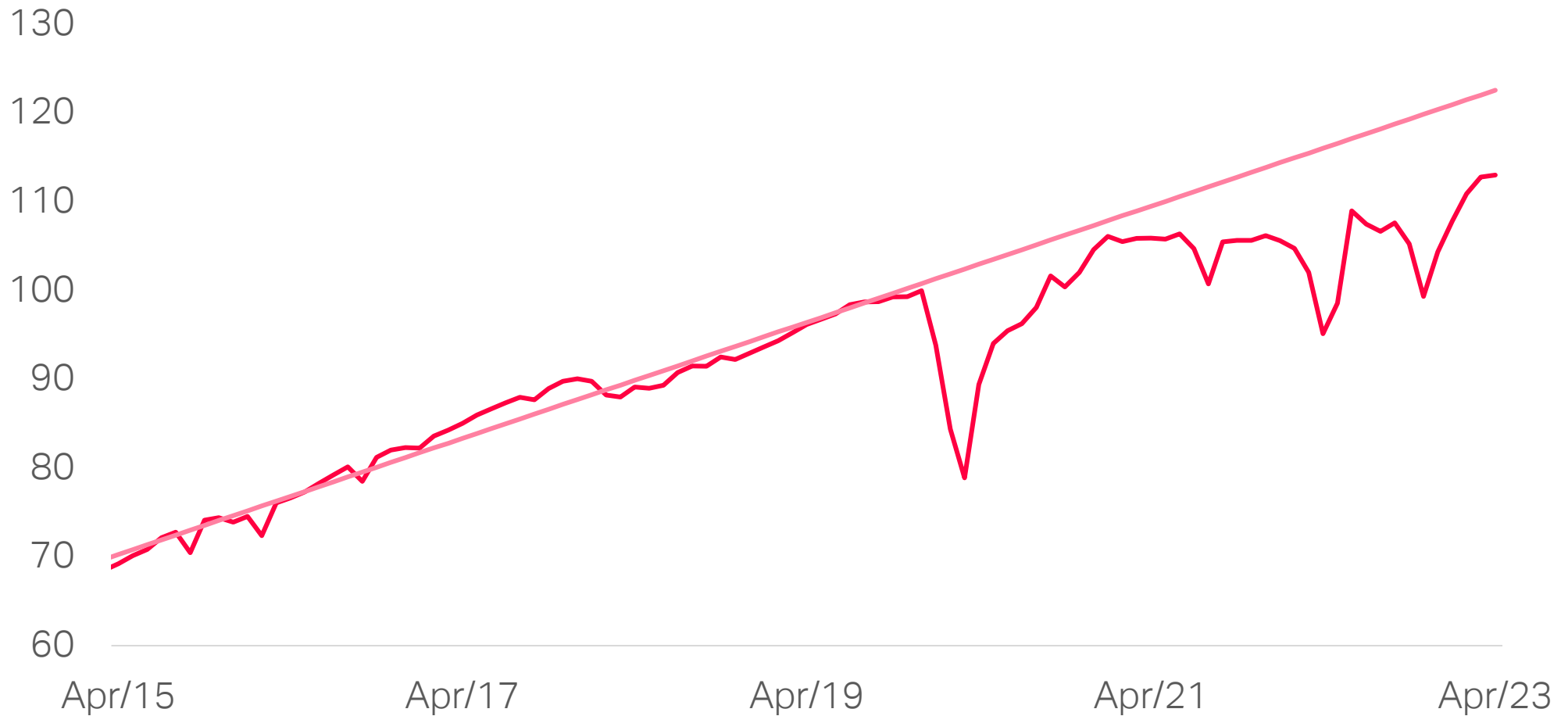
## Spending on services leads lopsided growth



Sources: NBS, TS Lombard.

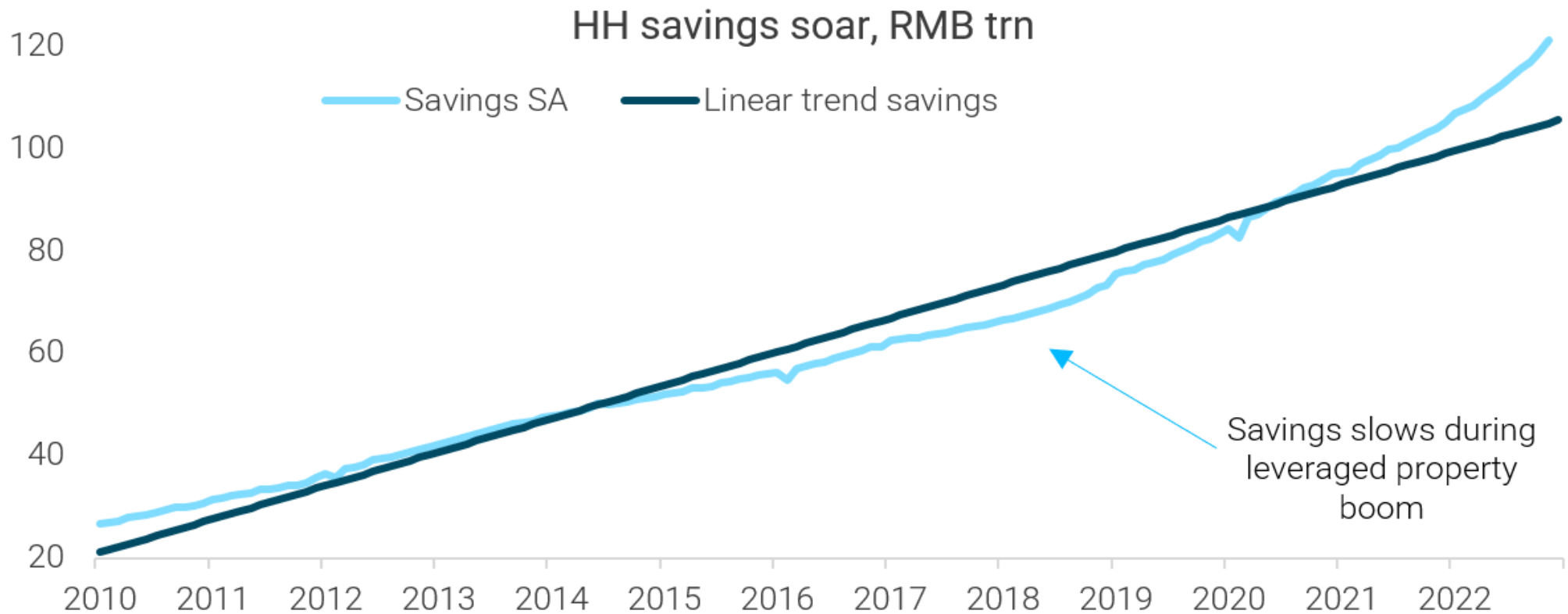
# CONSUMPTION IMPROVING STILL WEAK

Retail sales, 100 = Dec 2019



Sources: CEIC, TS Lombard.

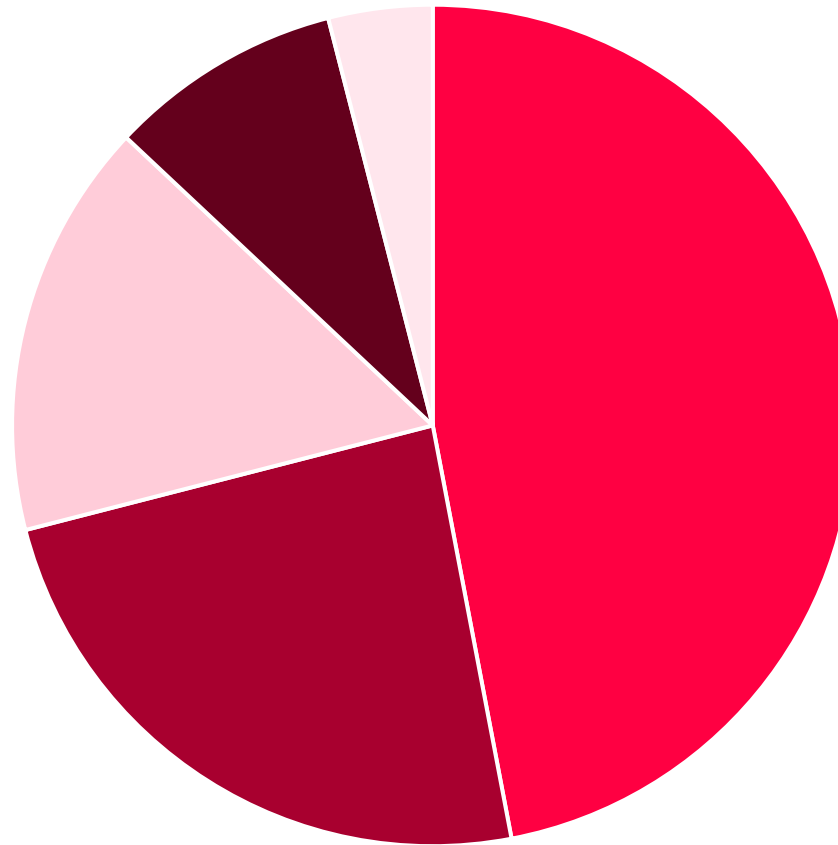
# SAVINGS HAVE RISEN 30%



Sources: NBS, CEIC, TS Lombard.

# BUT LARGELY FOR THE WEALTHY

## Excess savings by income bracket

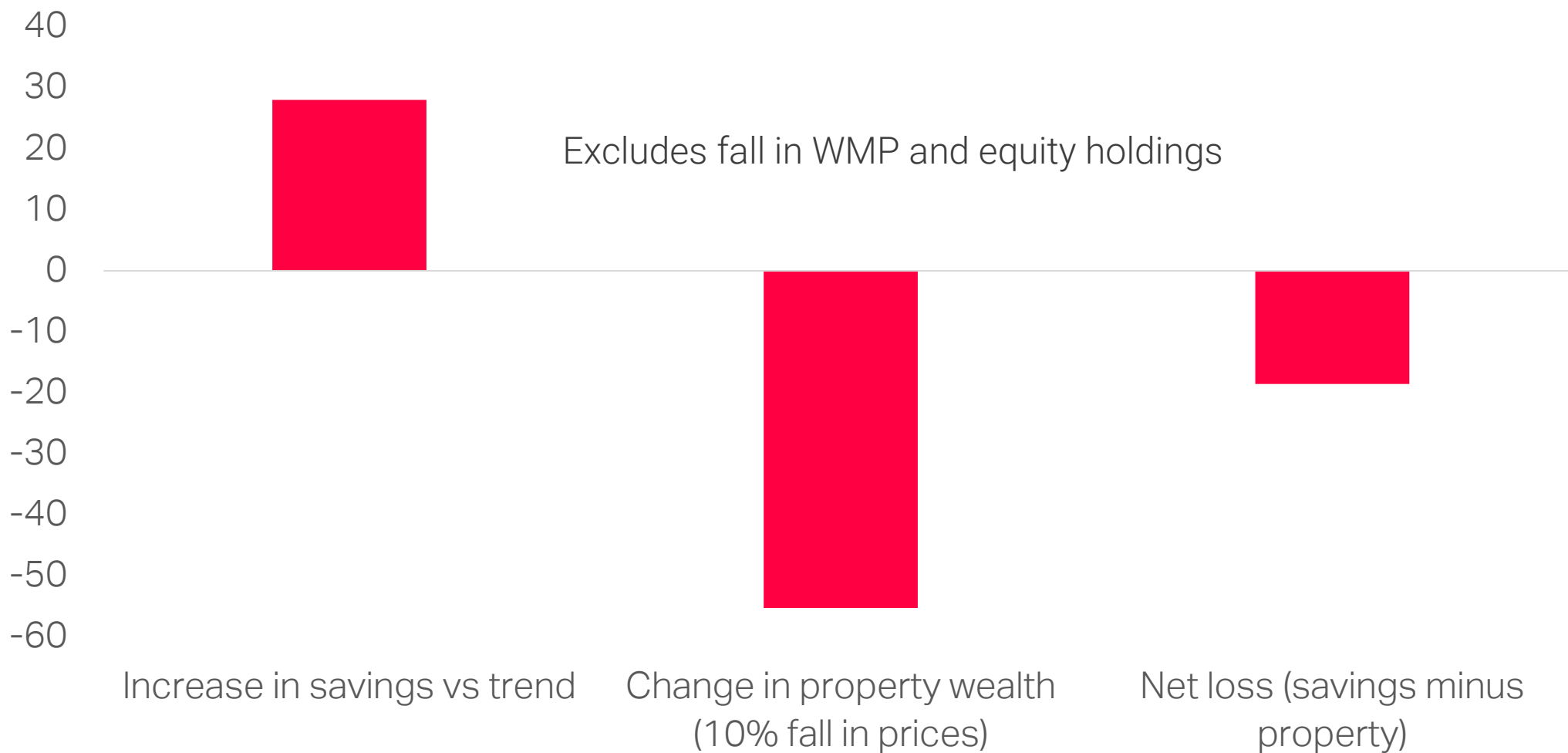


■ Top ■ Upper Middle ■ Middle ■ Lower Middle ■ Bottom

Sources: PBoC, BBG, TS Lombard.

# NOT A "US STYLE" REOPENING BOOM

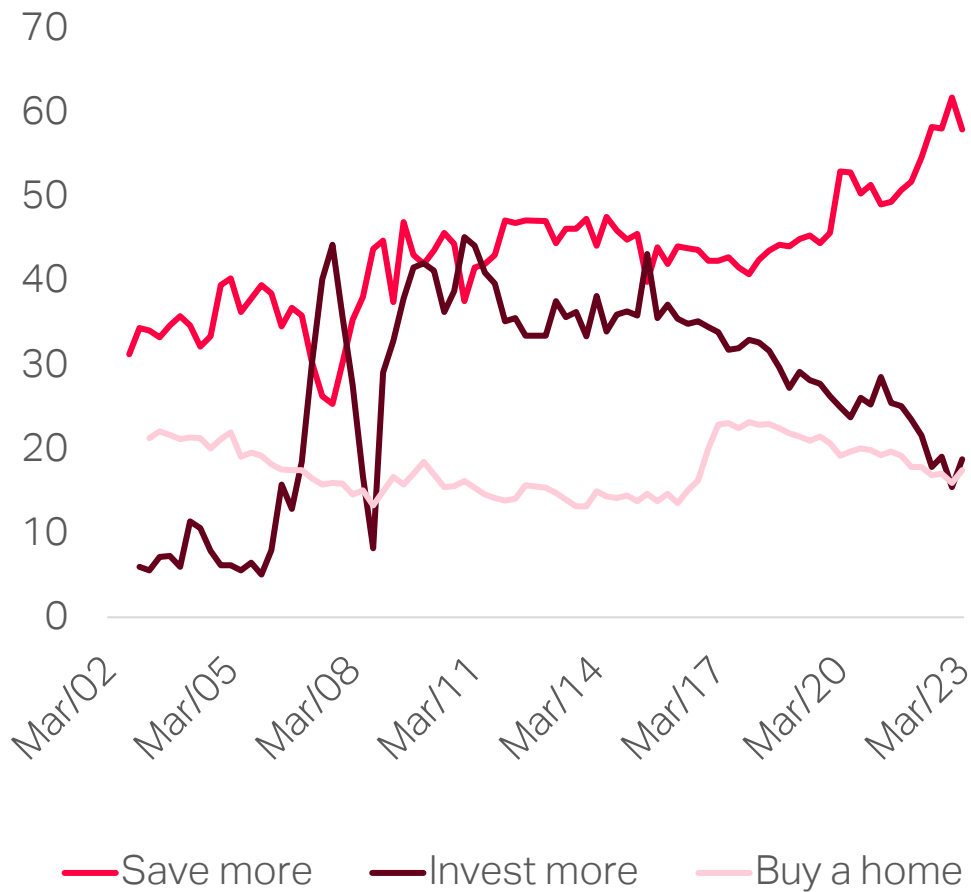
Chinese households have become poorer in last two years (RMB trn)



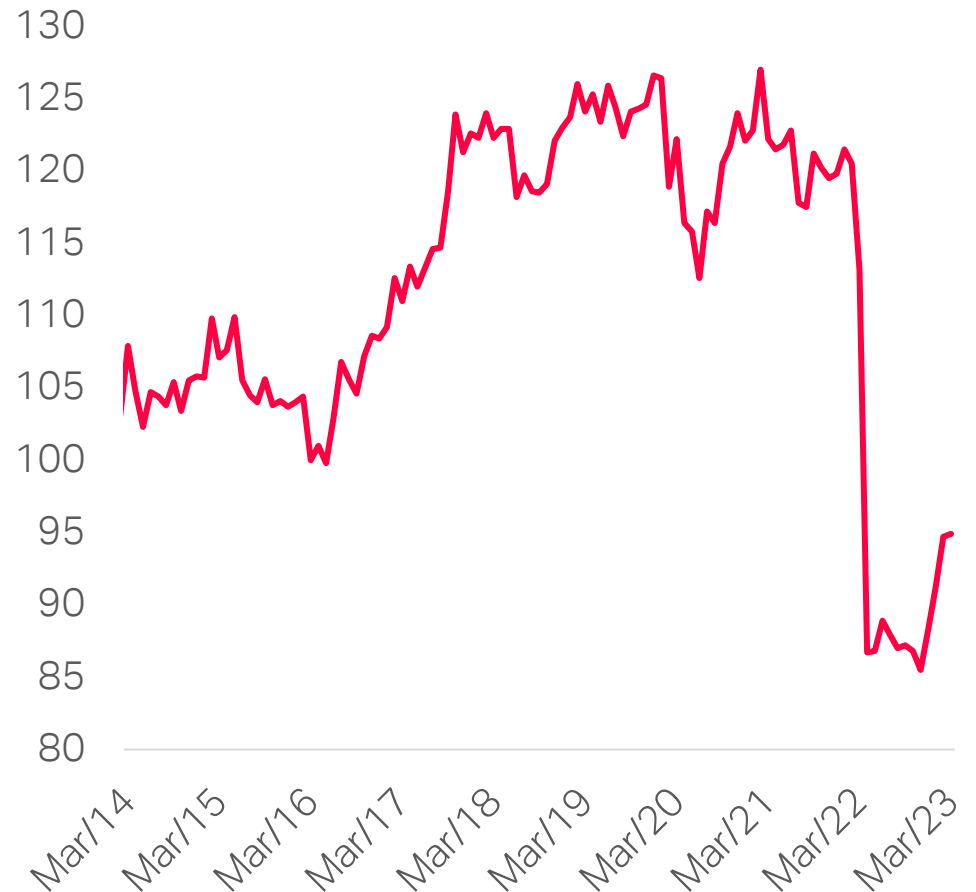
Sources: NBS, CEIC, TS Lombard.

# "SCARRED" CONSUMERS

**PBoC consumer survey - % planning to ...**



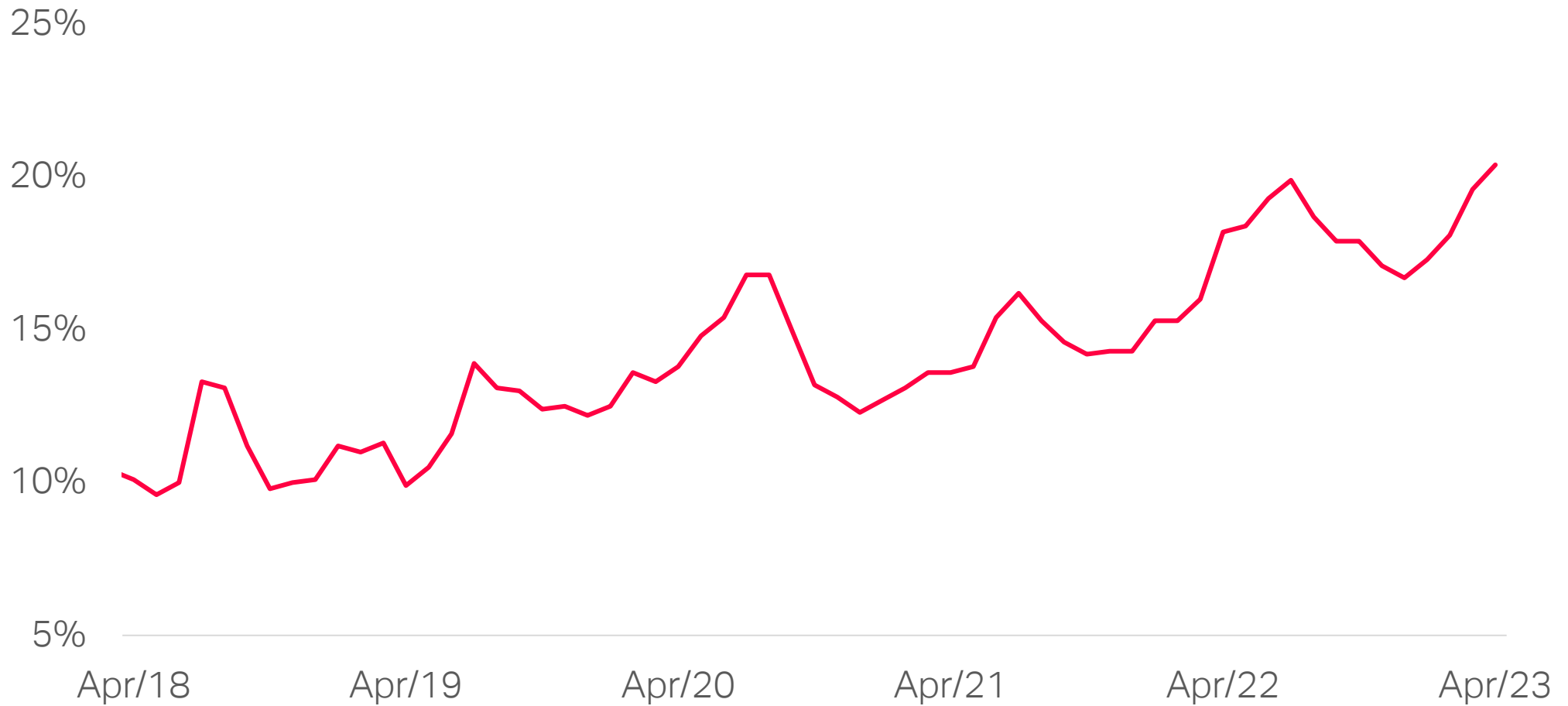
**Consumer confidence improving slowly**



Sources: NBS, PBoC, CEIC, TS Lombard.

# GAP BETWEEN RE-OPENING AND RE-HIRING

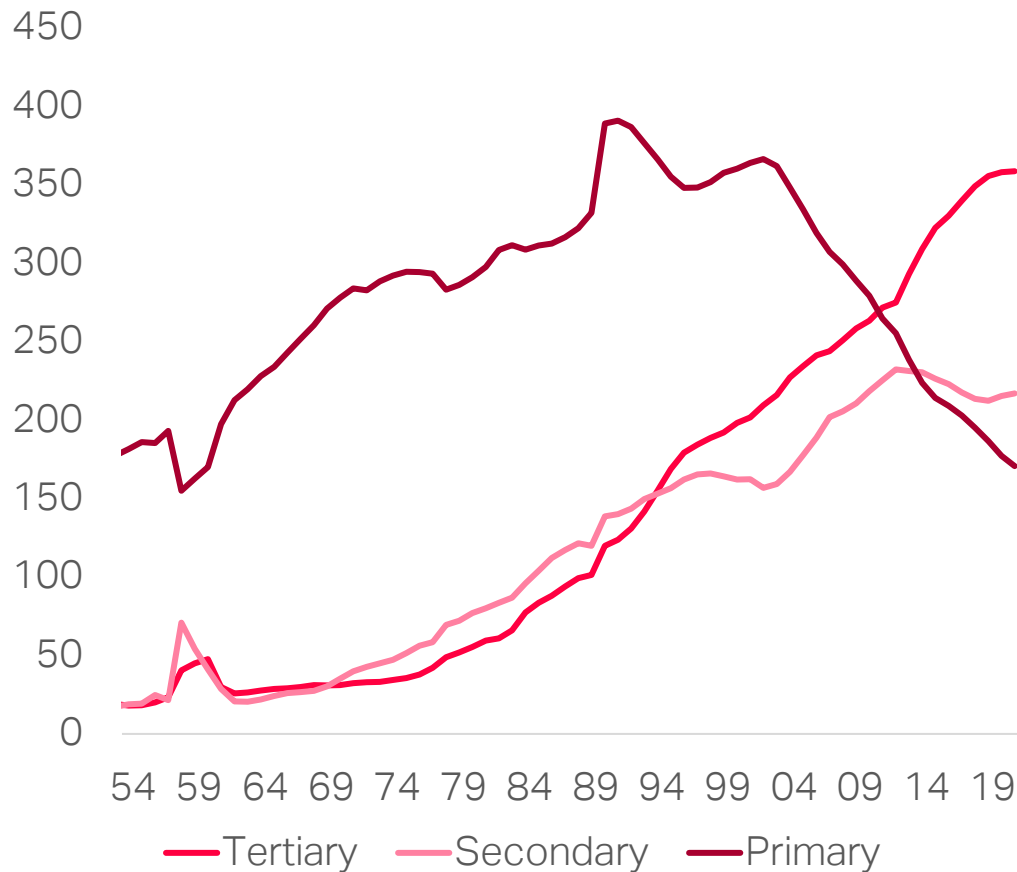
## Youth Unemployment



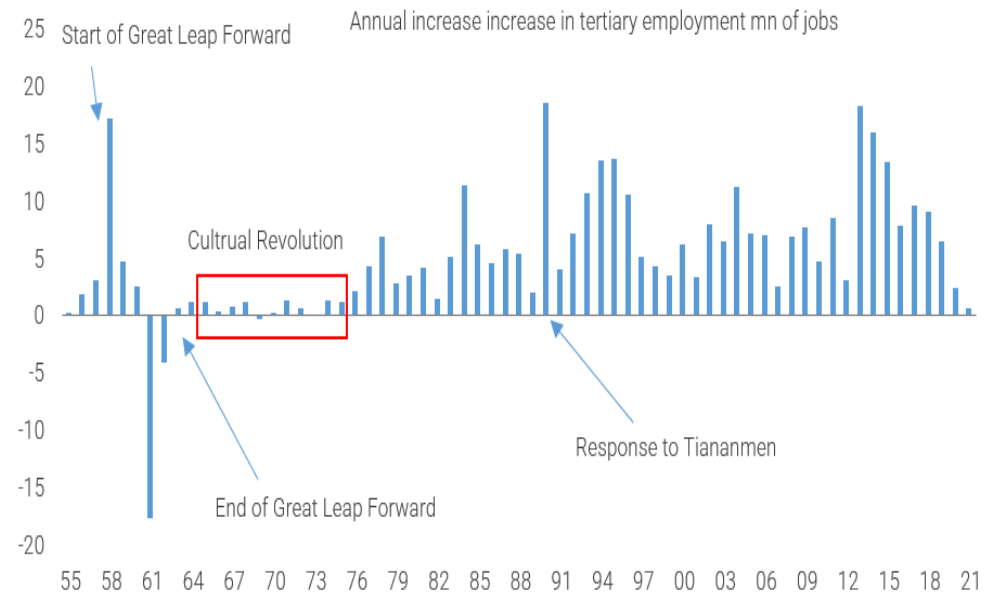
Sources: NBS, CEIC, TS Lombard.

# STRUCTURAL AND CYCLICAL HEADWINDS TO JOBS

## China employment mn



2021 had the smallest increase in tertiary sector employment since 1973



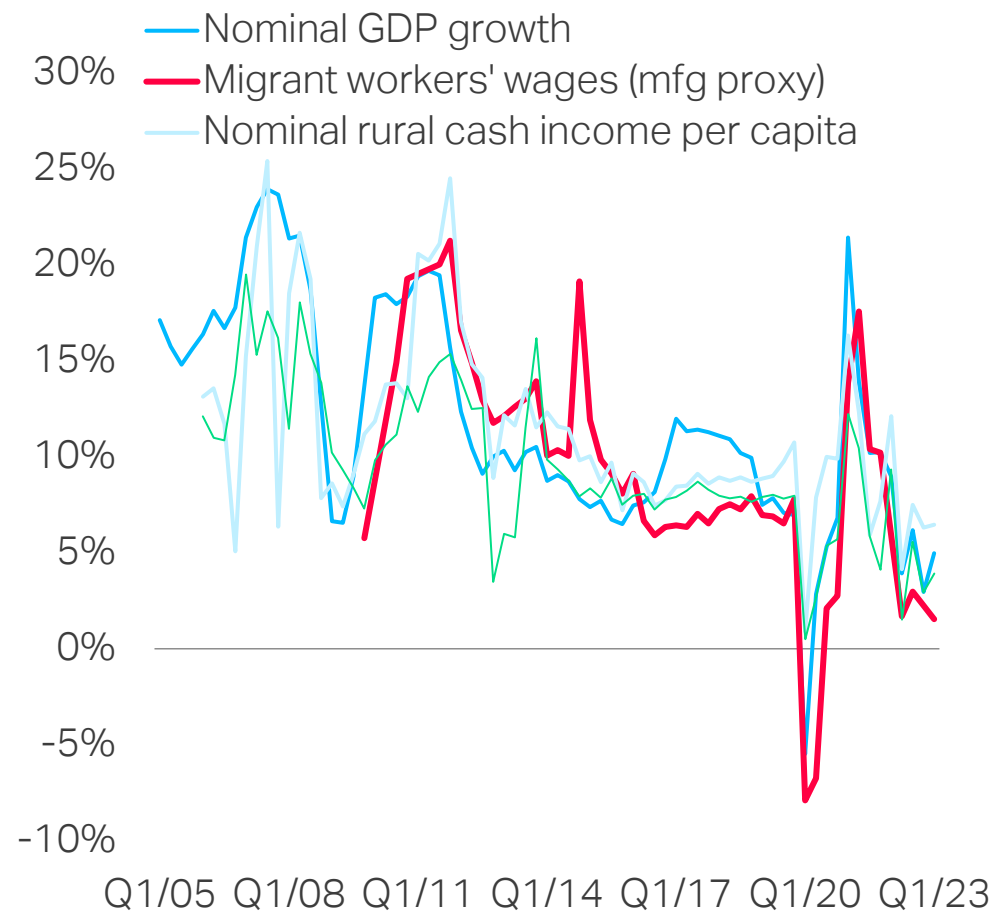
Sources: NBS, CEIC, TS Lombard.

# SERVICE SPENDING TO RAISE JOBS + WAGES

## Covid-19 vulnerable jobs\* share of total China employment



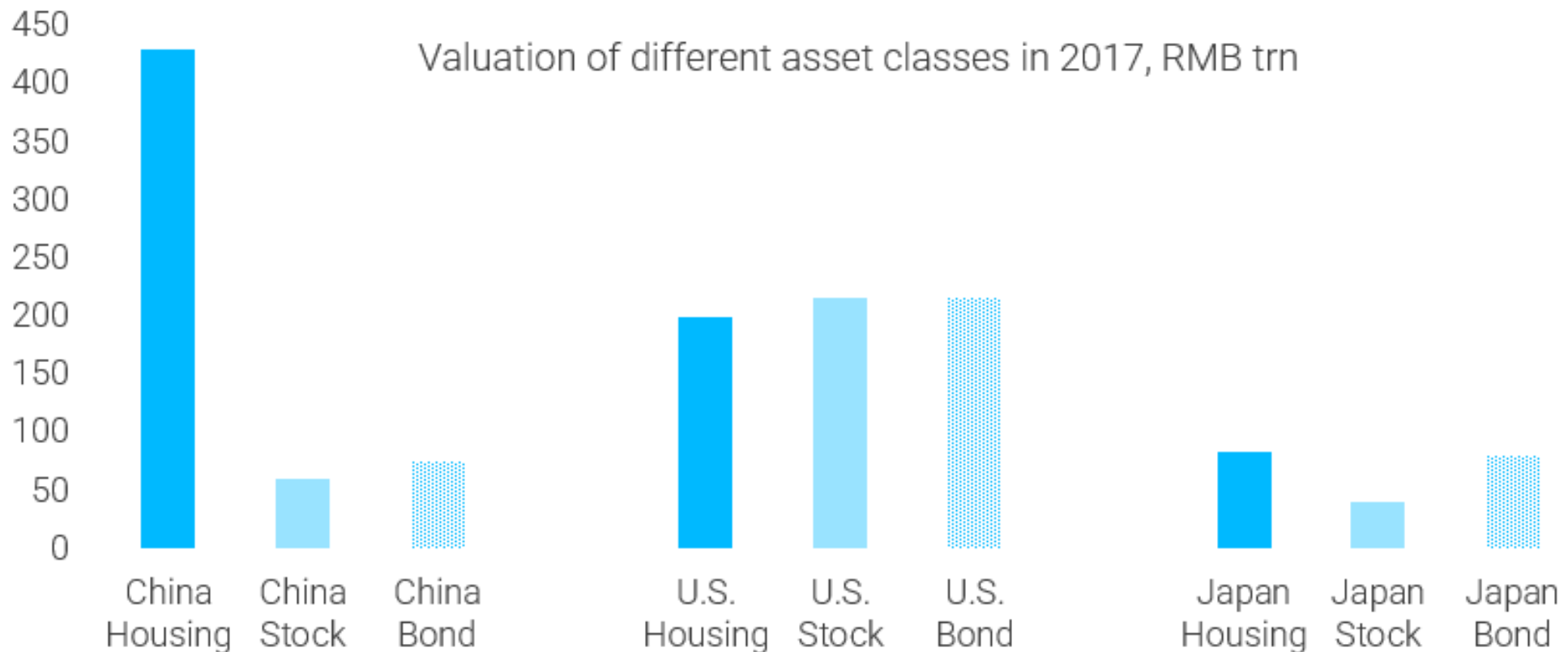
## Income growth, yoy



Sources: NBS, CEIC, TS Lombard.

# PROPERTY OUTLOOK IS KEY

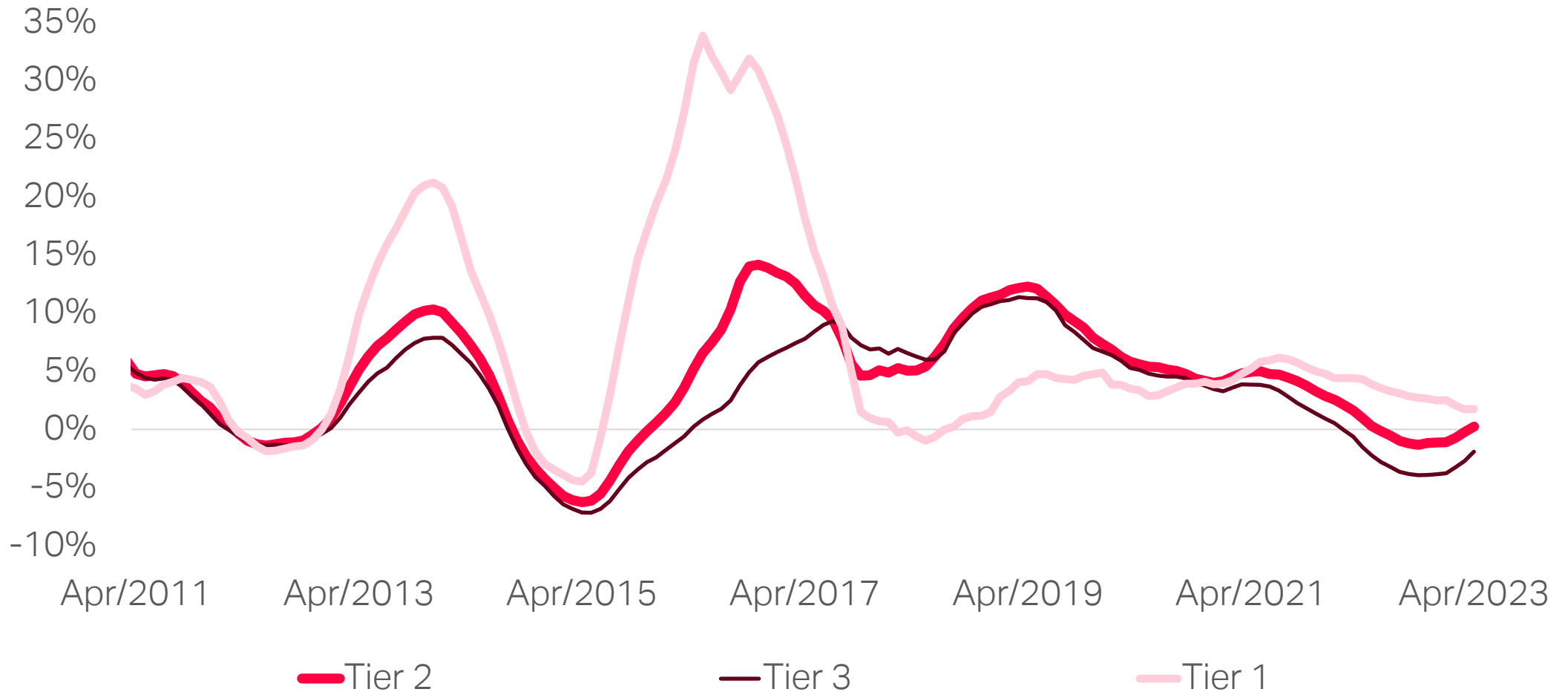
## The most important sector in the world



Source: 2018 China Urban Household Wealth Health Report

# WILL HOUSEHOLDS BUY THE DIP...?

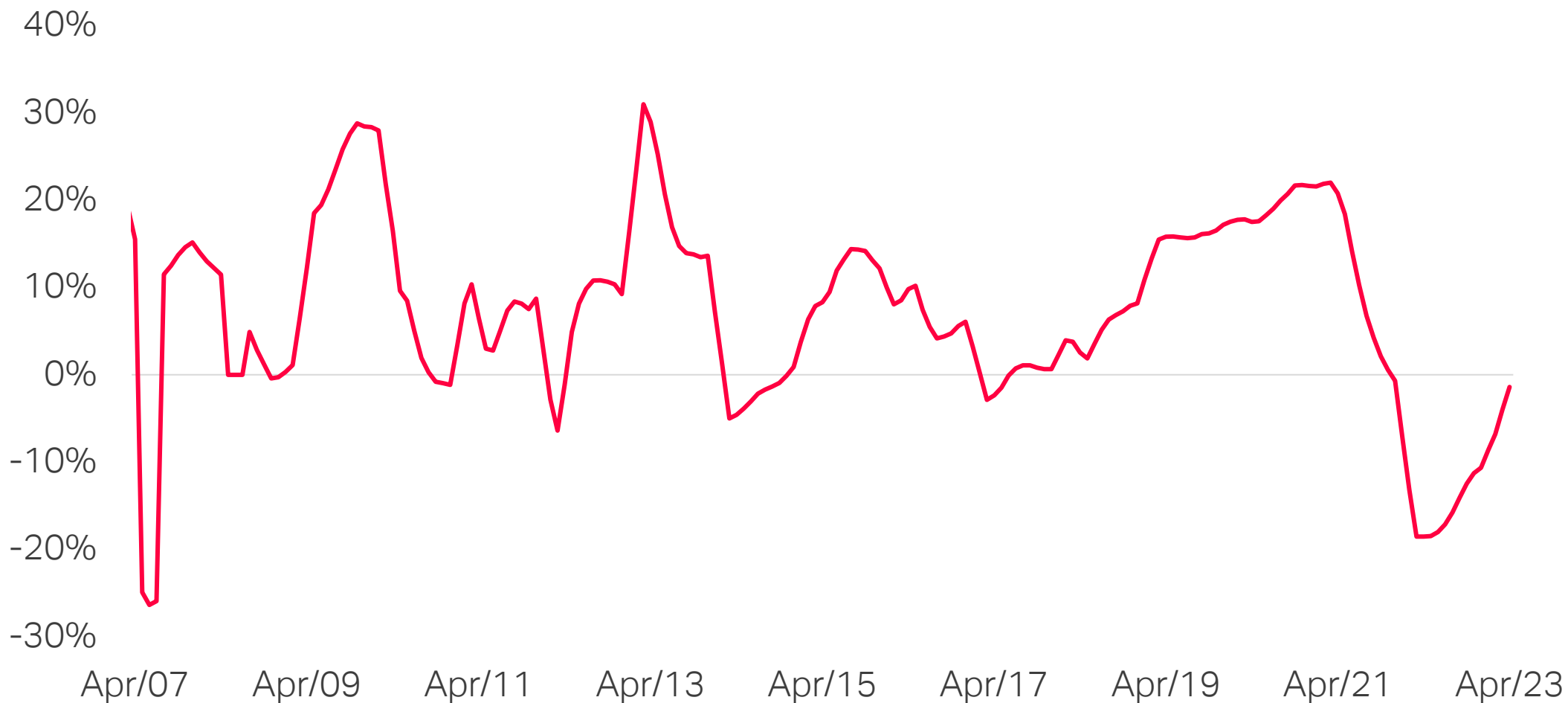
## China property prices yoy



Sources: NBS, CEIC, TS Lombard.

# ...ONLY IN TIER 1 + 2 CITIES

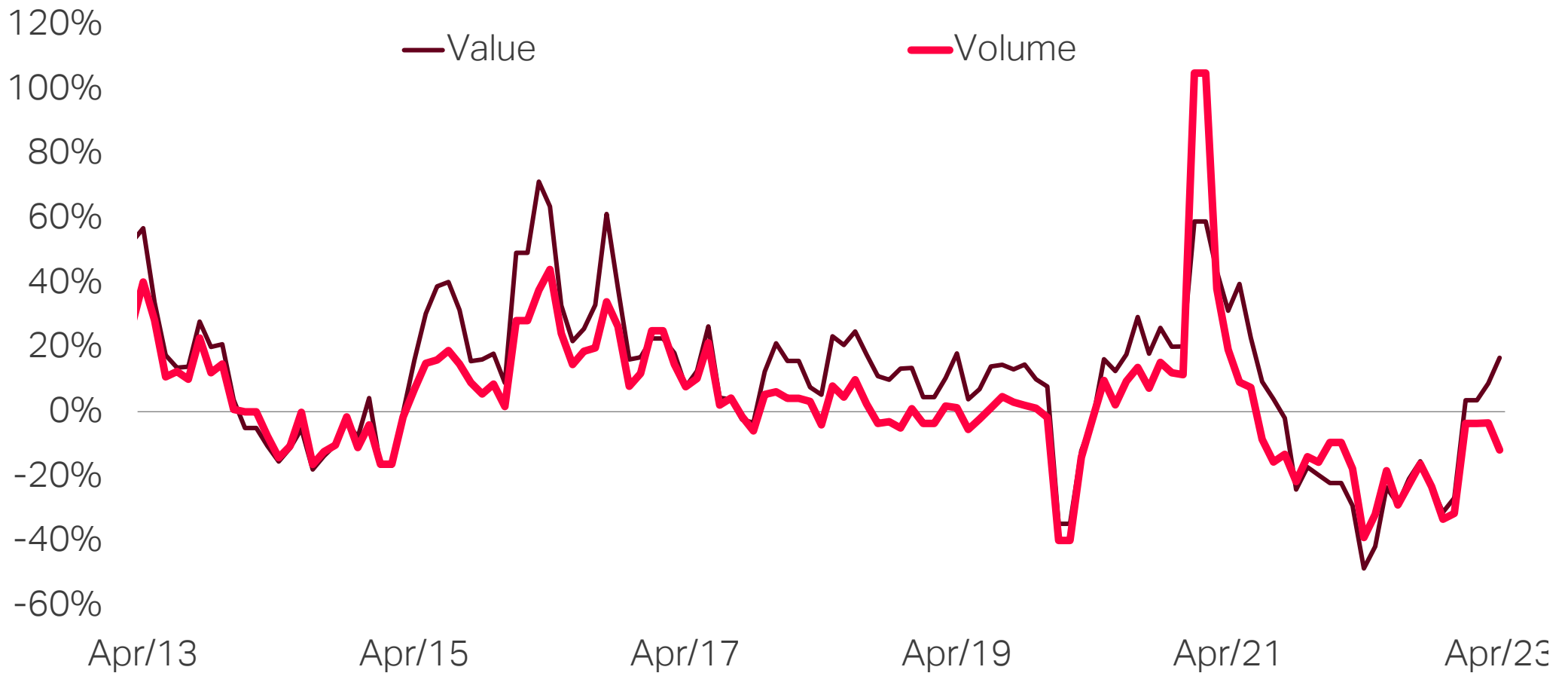
## Existing home sales price, yoy



Sources: NBS, CEIC, TS Lombard.

# TIER 1 SALES RISE BUT TOTAL VOLUME KEY FOR GDP

## Property sales growth yoy

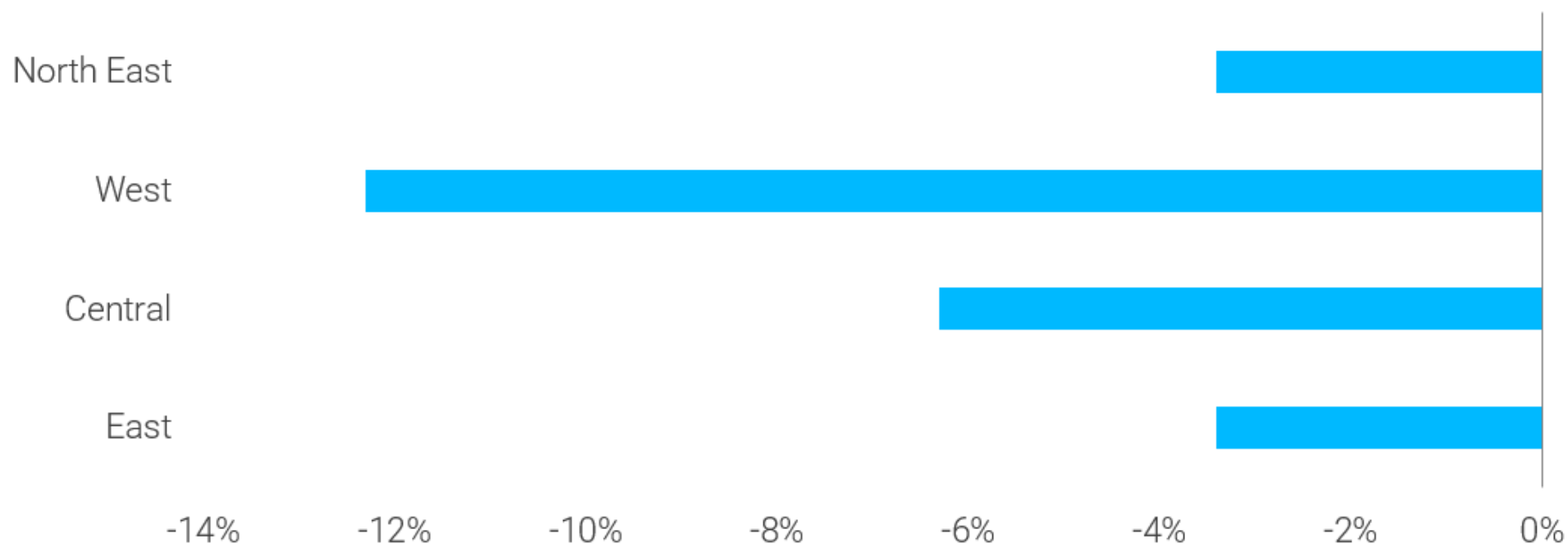


Sources: NBS, CEIC, TS Lombard.

# TIER 3 AND BELOW (70% OF MARKET) LAGGING

## Uneven property rebound

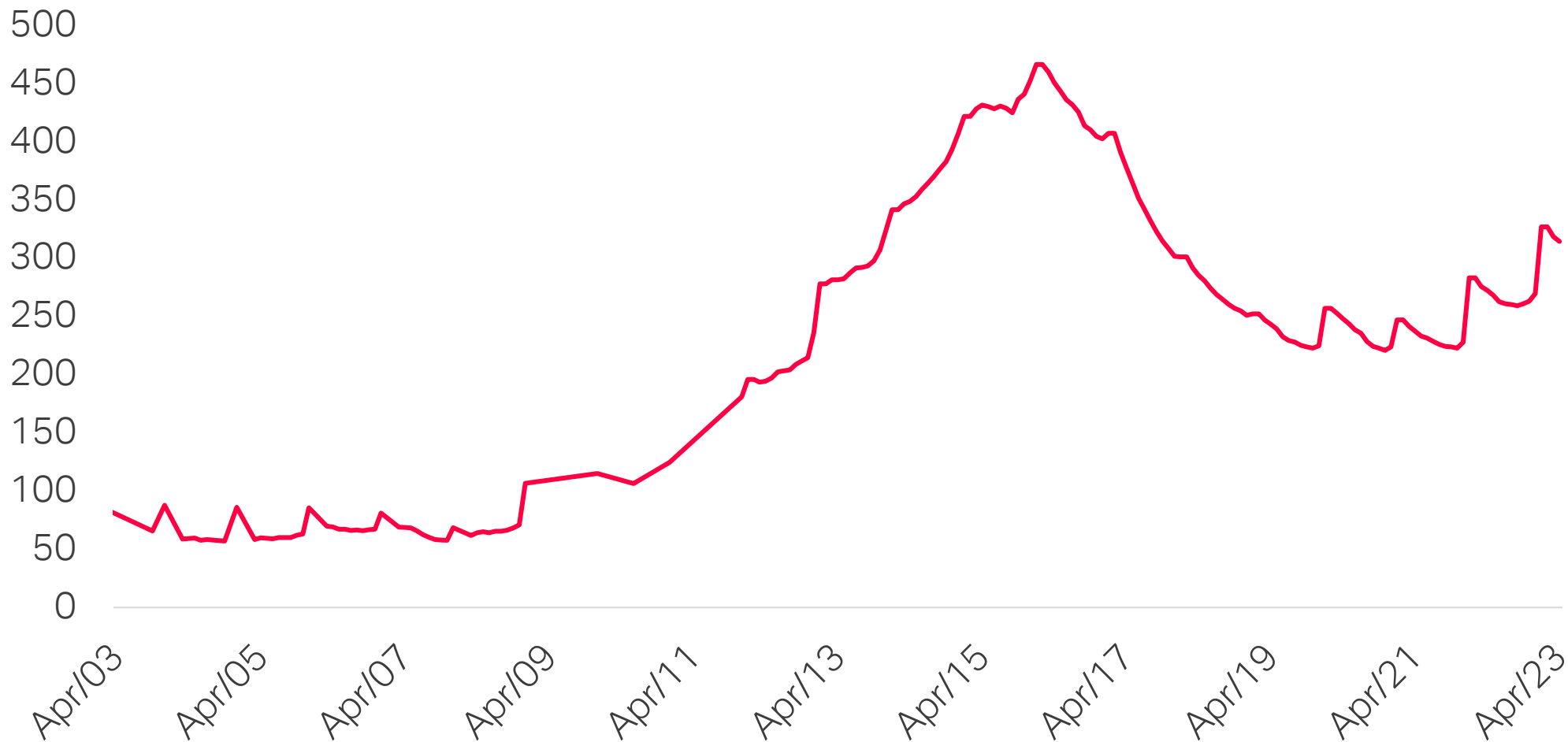
### Jan-Mar real estate investment by region yoy



Sources: NBS, TS Lombard.

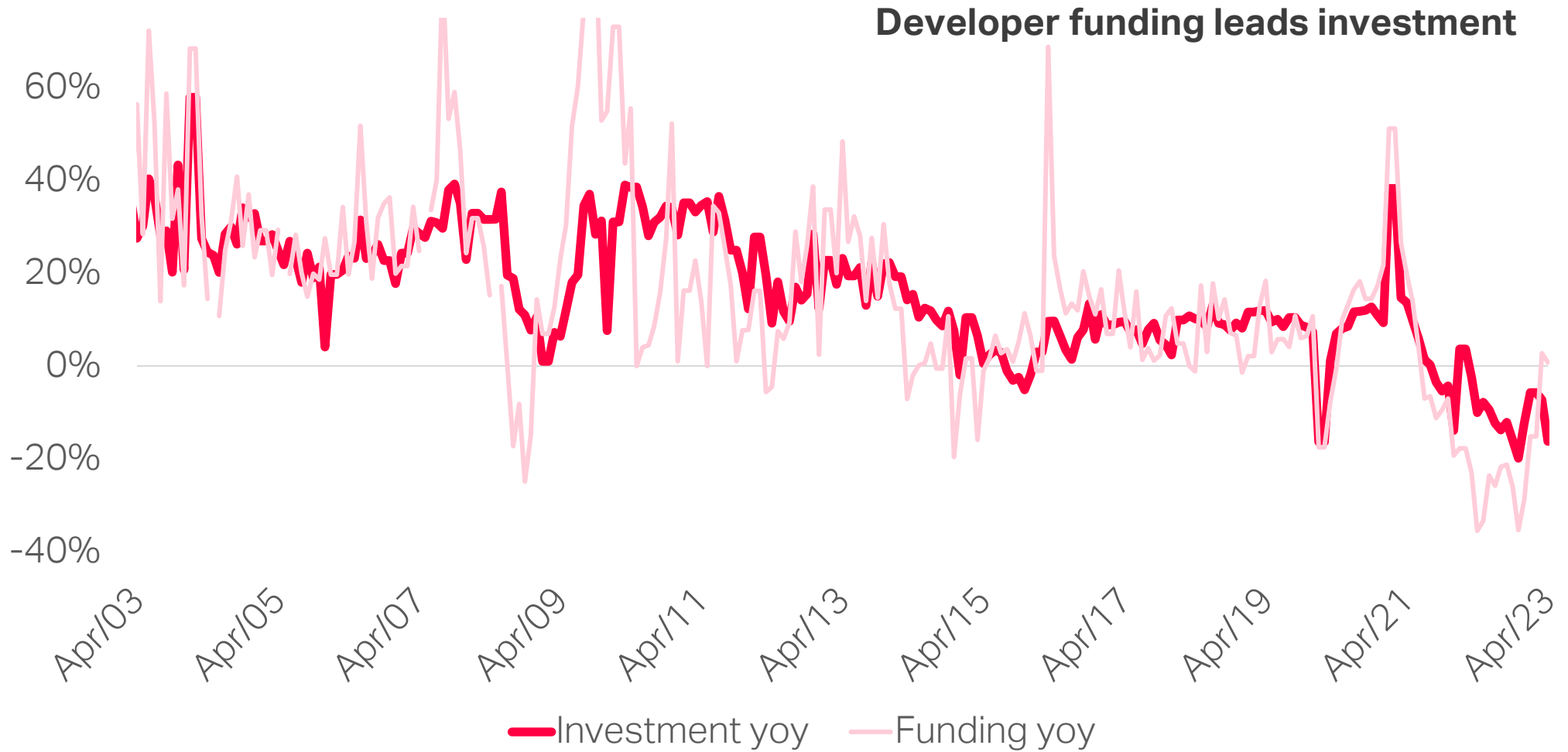
# INVENTORY LEVELS ARE HIGH

Floor space waiting for sale, sq m mn



Sources: NBS, CEIC, TS Lombard.

# FUNDING SLUMP MEANS NO INVESTMENT GROWTH



Sources: NBS, CEIC, TS Lombard.

# BEIJING'S UNAMBITIOUS GROWTH GOALS

Targets		2023	2022
Economy	GDP	about 5%	about 5.5%
	CPI	about 3%	about 3%
Fiscal	Deficit	3%	2.8%
	LG special purpose bonds	RMB 3.8trn	RMB 4.15 trn (including 2021 unused quota)
	Tax and fee cuts	Continuation and optimization	Tax refund and reduction RMB 2.5 trn
Monetary	M2, TSF	Basically inline with nominal growth	Basically inline with nominal growth
Employment	New urban jobs	about 12mn	above 11mn
	Urban unemployment rate	about 5.5%	below 5.5%
Decarbonisation	Carbon intensity of GDP	Lower the carbon intensity of GDP	Within 14th Five Year Plan targets

# MONETARY POLICY IS LOOSE BUT INEFFECTIVE

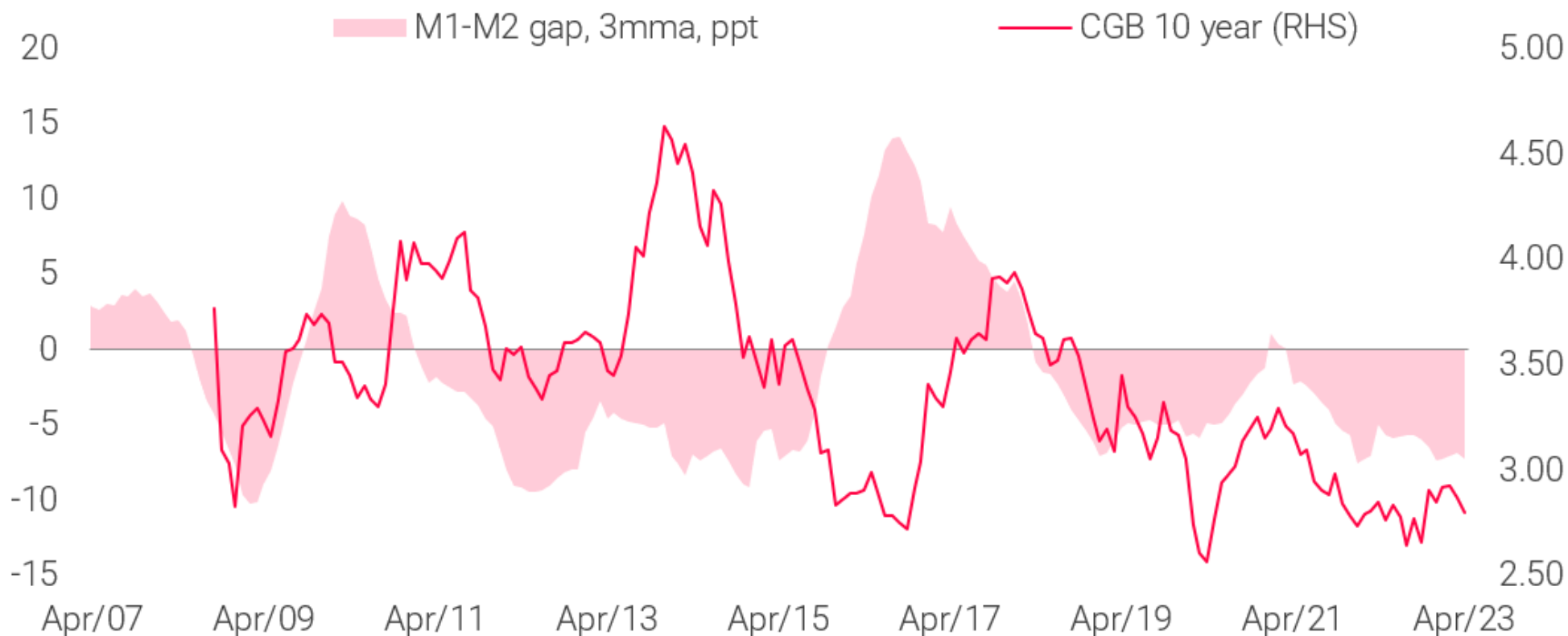
## Where is the money?



Sources: PBoC, CEIC, TS Lombard.

# M2 FAILS TO SPARK PRICES/PRODUCTION/ASSETS

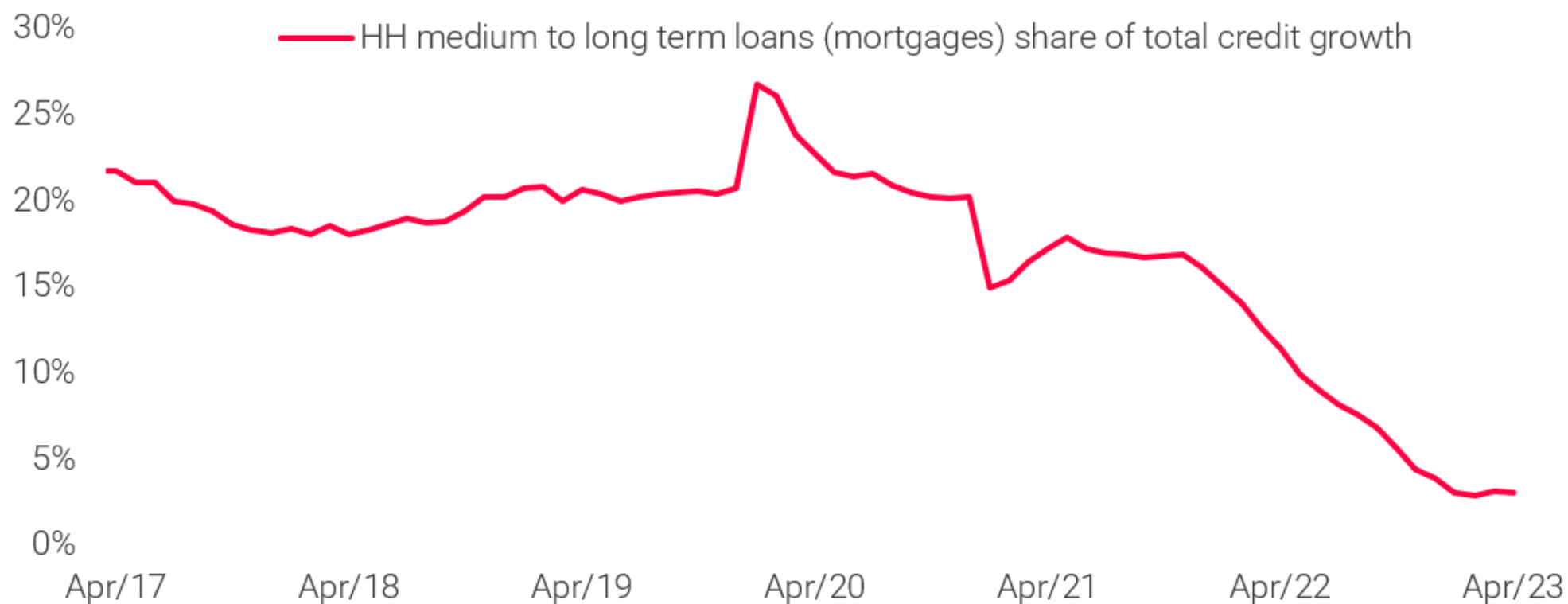
## M1-M2 gap is wide



Sources: TS Lombard, PBoC

# ANAEMIC PRIVATE SECTOR CREDIT DEMAND

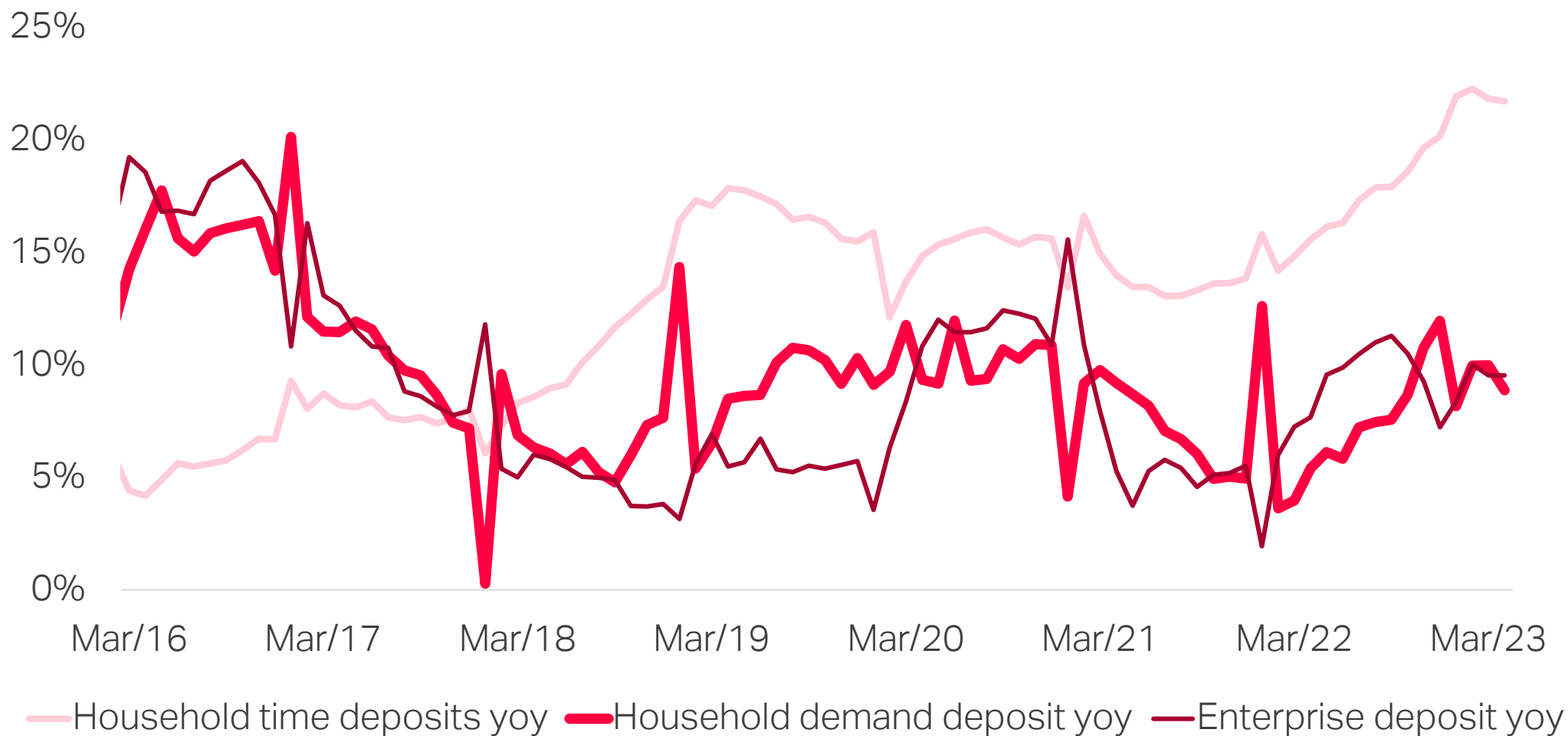
## Balance sheet recession



Sources: TS Lombard, PBoC.

# MONEY TRAP

## Rise in time deposits decrease flow of HH funds to real economy



Sources: PBoC, CEIC, TS Lombard.

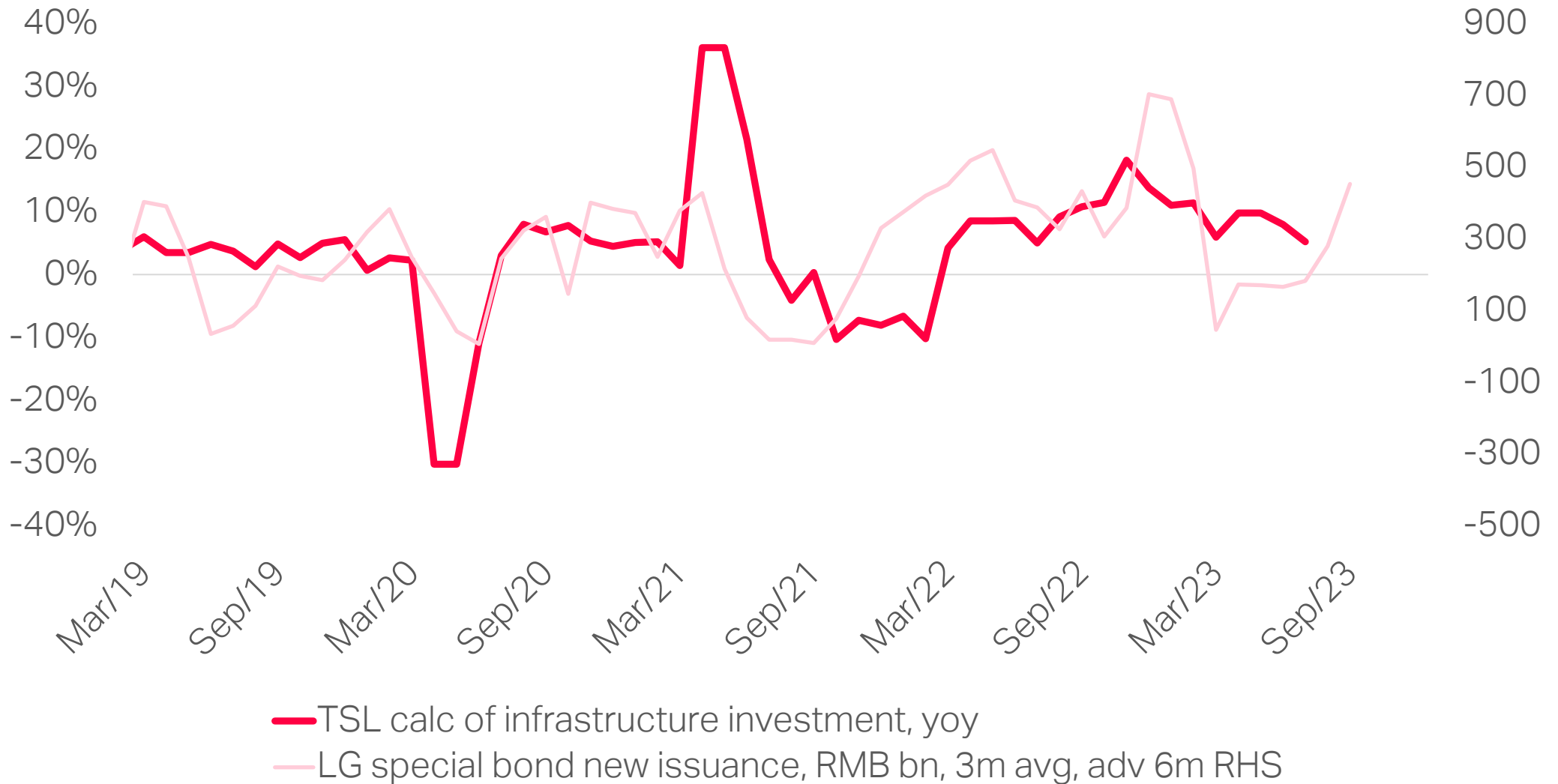
# MONEY CIRCULATION COLLAPSES

## Velocity of money still slowing



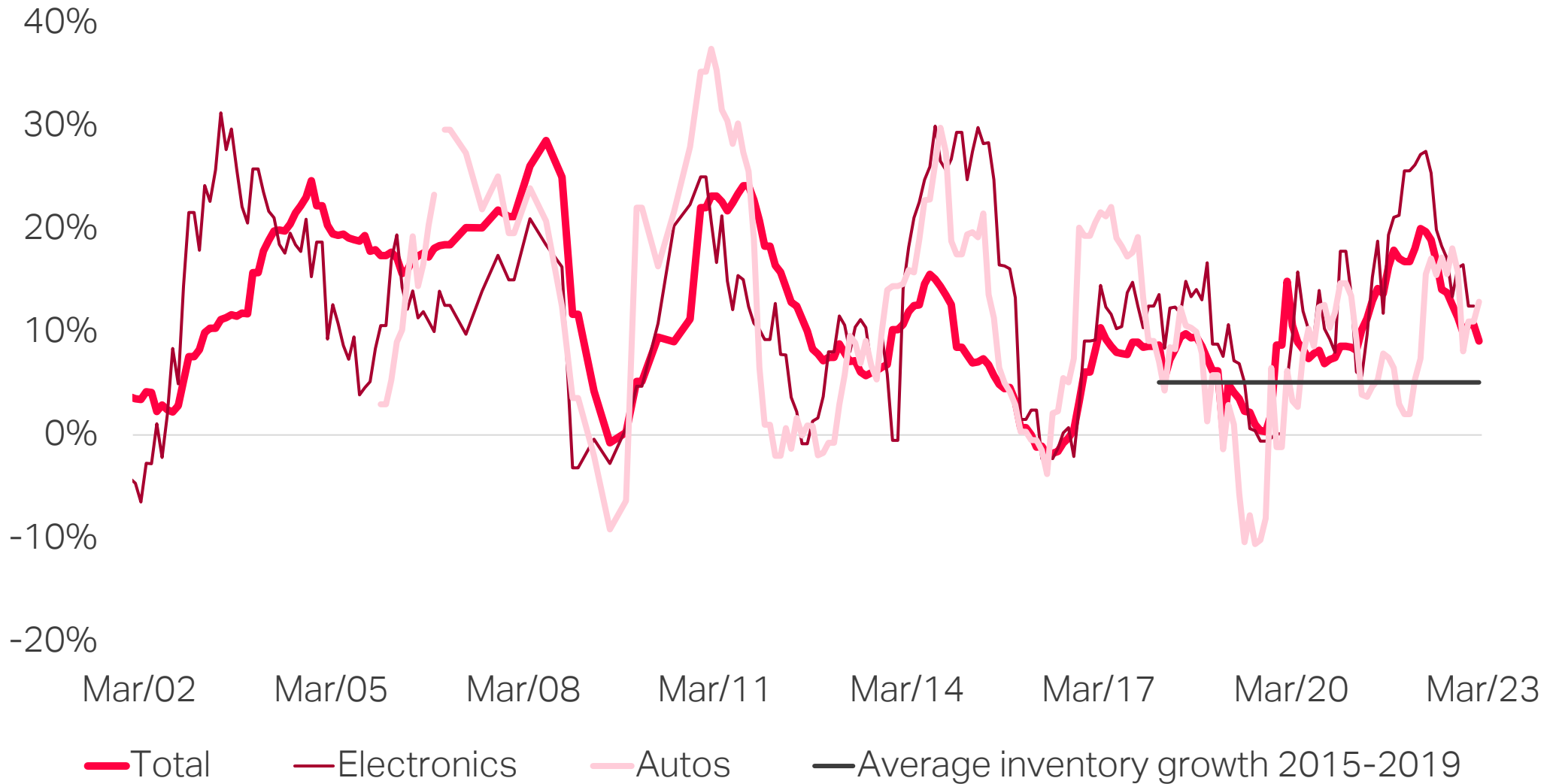
Sources: TS Lombard, PBoC.

# INFRASTRUCTURE IS KEY FISCAL LEVER



Sources: Local Government, CEIC, TS Lombard.

# INVENTORIES STILL GROWING TOO FAST



Sources: NBS, CEIC, TS Lombard.

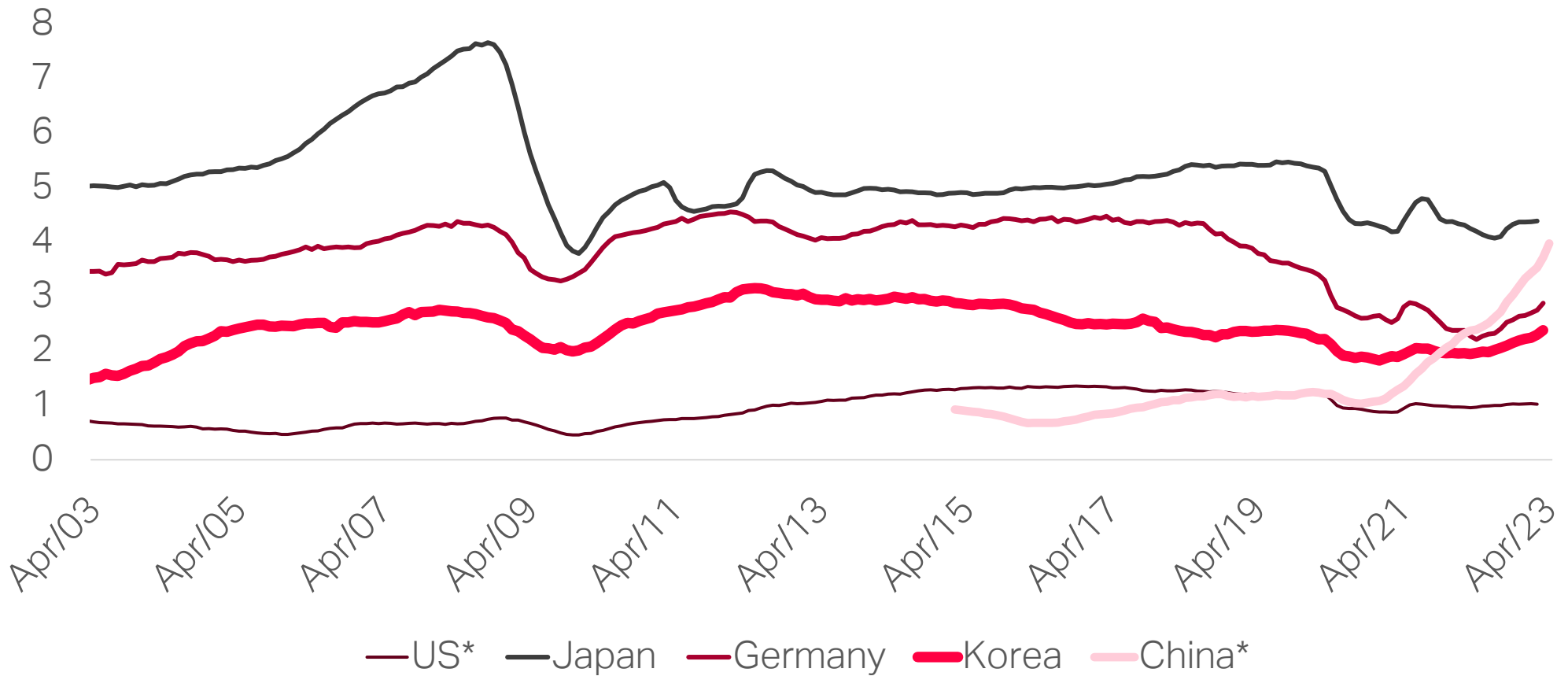
# METAL DEMAND DRIVERS WEAKENING



Sources: NBS, CEIC, TS Lombard.

# EXPORTS WEAK WITH POCKETS OF STRENGTH

Car exports by volume (12m sum, mn)

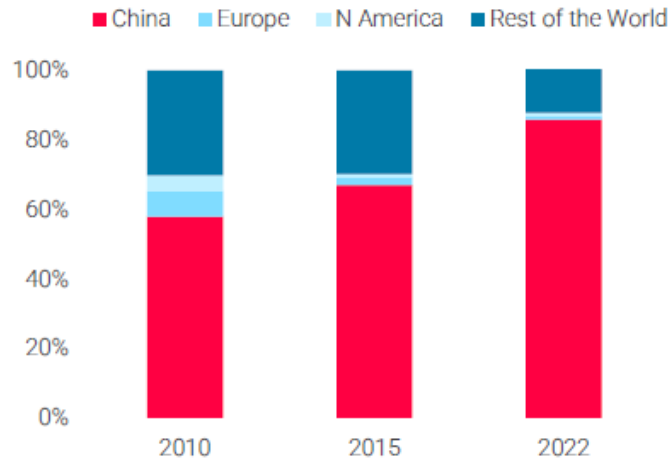


Sources: NBS, CEIC, TS Lombard.

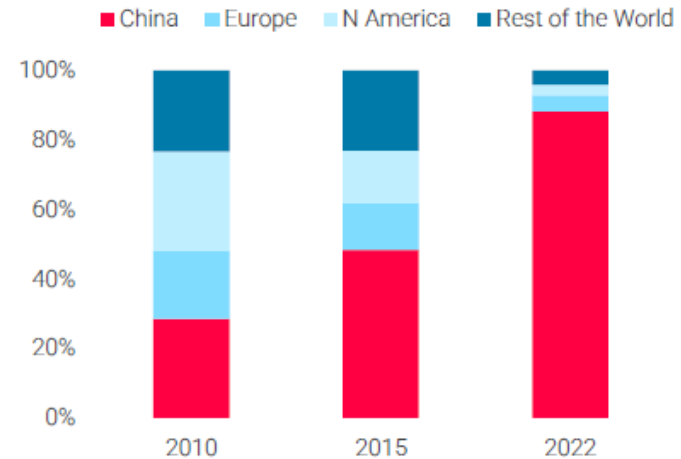
# CHINA CLEAN TEACH IS WORLD LEADING

## Global solar panel manufacturing capacity

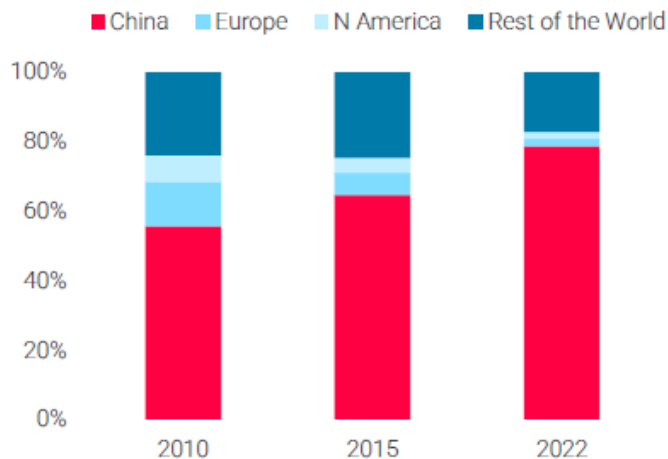
### PV cells



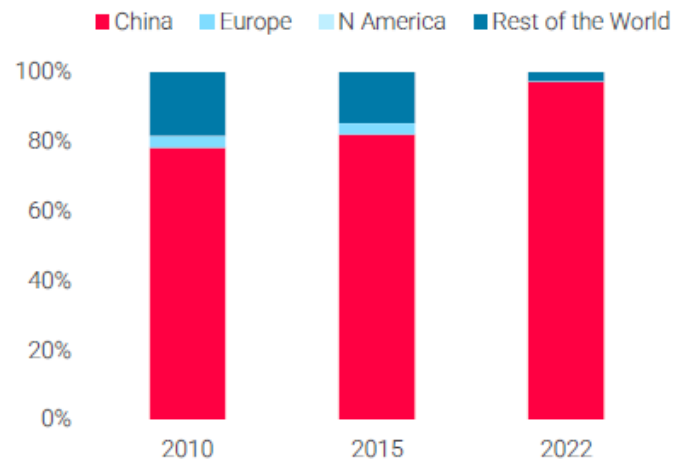
### Polysilicon



### PV modules



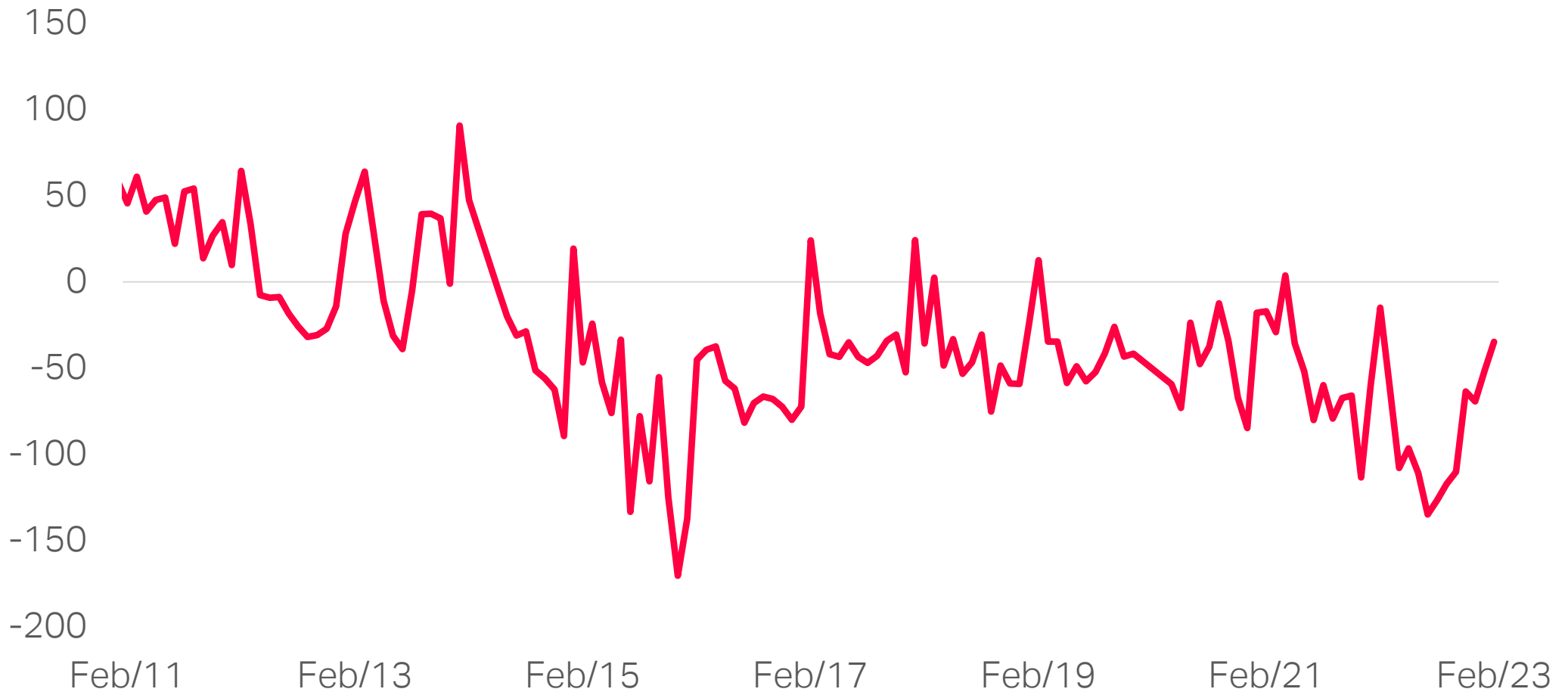
### Silicon wafers



Sources: IEA, CEIC, TS Lombard.

# HOUSEHOLD FLIGHT => RMB WEAKNESS

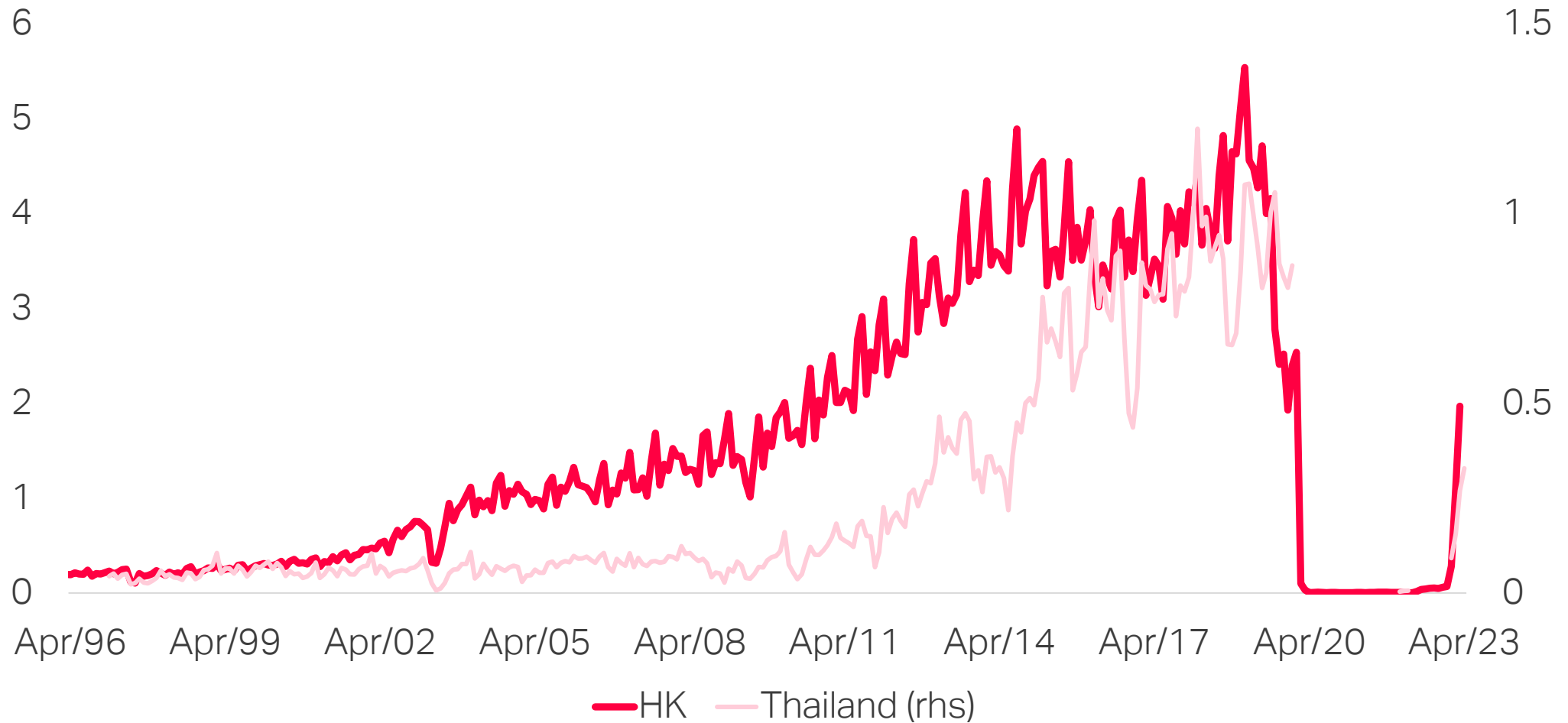
China capital outflow USD bn



Sources: BBG, CEIC, TS Lombard.

# SERVICE OUTFLOWS TO COME

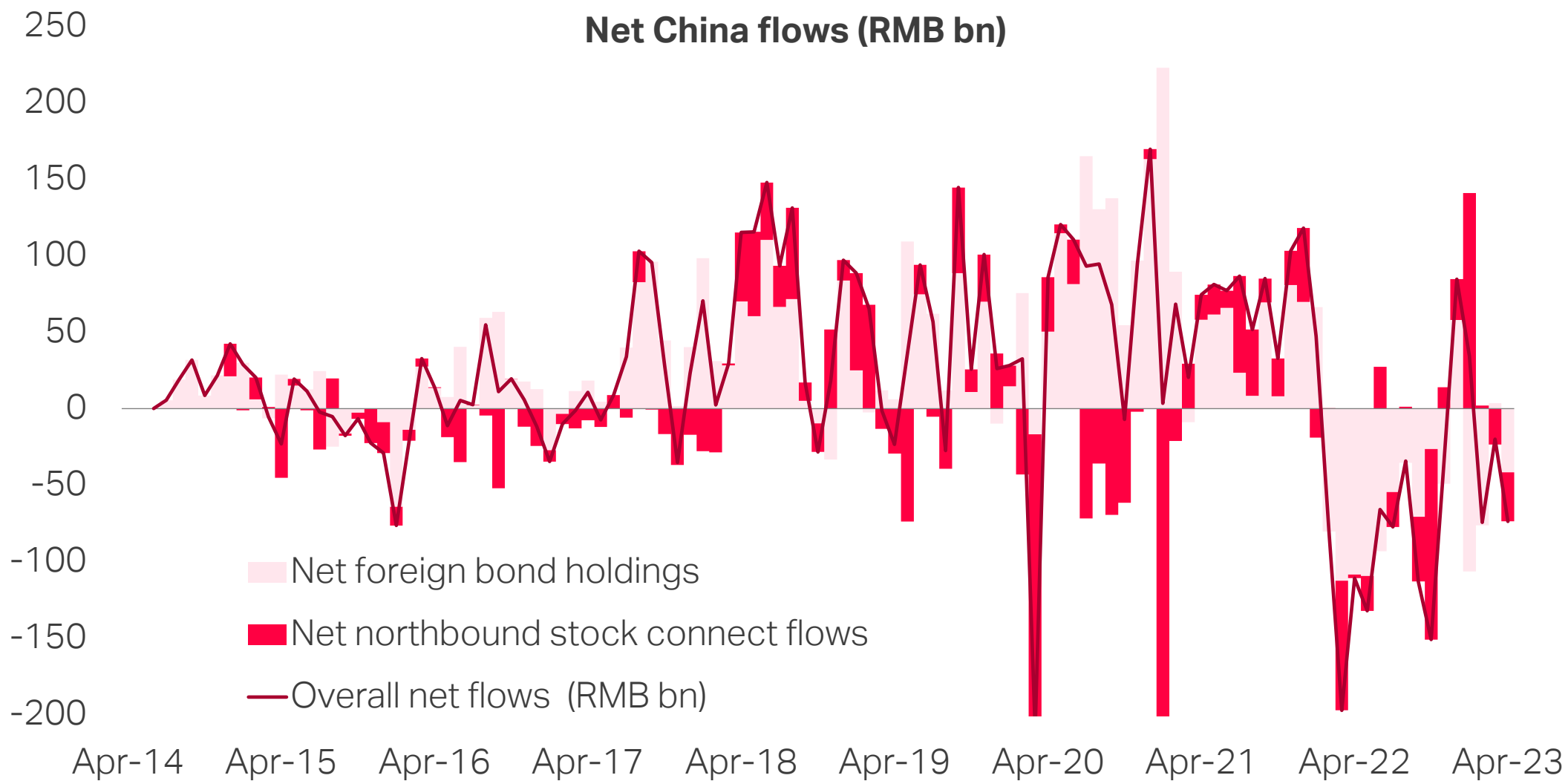
Chinese visitors, mn



Sources: CEIC, TS Lombard.

# SKITTISH FOREIGNERS

## Net China flows (RMB bn)



Sources: Stock Connect, CEIC, TS Lombard.

# CONCLUSION

- **Lopsided recovery losing momentum.** Reopening sets up strong H1. H2 slowdown. Full year 5.7% yoy
- **Service spending soaring.** But investment and manufacturing weak and will remain so
- **China is heavily scarred.** 1) Covid 2) Property crash 3) “Common Prosperity” shift – leave a long hangover
- **Property green shoots on unstable ground.** Sales sluggish, and investment negative through 2023
- **Q3/23 graduate woes likely to trigger extra round of stimulus in H2**
- **Global demand and inflation spillovers mild.** Service spending does not drive commodity imports

## Market implications

Long A Share consumer equities – Service sector spending is still strong

Neutral China index – H2 slowdown limits upside for MSCI China

Long USDCNY – Growth and rate differentials combine with service outflows to pressure RMB

Neutral rates – Slowdown and PBoC easing are priced in

Short industrial commodities – Investment drivers (particularly property) will remain on the back foot

## Research Packages

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### Global Macro

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Daily Note

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Macro Picture

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The View

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Global Macro Monthly

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Global Financial Trends

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Global Political Drivers

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US Watch

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Europe Watch

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UK Outlook

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### Global Strategy

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Asset Allocation

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Macro Strategy

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Strategy Chartbook

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### Global EM

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EM Strategy Monthly

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EM Watch

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The GRID

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China Watch

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Brazil

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India

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Russia

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LatAm

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EMEA

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S.E. Asia

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## Specialist

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Asia Property

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**United Kingdom & Europe**  
Standard House, 1  
12-13 Essex Street,  
London WC2R 3AA  
Tel: +44 (0) 207 246 7800  
london@tslombard.com

**North America**  
183 Madison Avenue  
Suite 419  
New York 10016  
Tel: +1 646 398 5903  
newyork@tslombard.com

**Asia Pacific**  
Unit 4, 16/F, Bonham Trade  
Centre, Bonham Strand  
Sheung Wan, Hong Kong  
Tel: +852 2521 0748  
hongkong@tslombard.com