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China Economics Update: 1Q GDP beat expectations, lifting annual growth forecasts

中国经济评论: 经济增长良好开局，上调 2024 年 GDP 增长预测

Strong GDP in 1Q bodes well for growth. Downside surprise in industrial production in Mar could have occurred as the result of holiday distortions. We expect the industrial sectors to enjoy solid growth as manufacturing PMI improves. Despite a stubborn downturn in the property market, manufacturing and infrastructure investment accelerated in 1Q, fueled by a strong economic transition. Sequential improvement in retail sales suggests stabilizing consumption. Given the good start to the year and continued policy support, we raise our 2024 GDP growth forecast for China from 5.0% to 5.2%.

Macro policy support to continue. Apart from greater fiscal support, new policy initiatives such as large-scale equipment upgrades and consumer good trade-ins could add to investment and consumption demand. We continue to expect a 25bp cut to the Required Reserve Ratio (RRR). However, the strong US dollar may limit the room for interest rate cuts in the near-term.

Kevin Xie
(852) 3911 8241
kevinxie@ccbintl.com

Li Cui
(852) 3911 8274
cuili@ccbintl.com

Huiting Yan
(852) 3911 8012
yanhuiting@ccbintl.com

强劲的一季度 GDP 为年度稳健增长奠定基础。3 月份工业生产弱于预期的表现可能受假期影响。制造业 PMI 近期趋势改善，我们预计工业部门将稳步增长。尽管地产市场持续低迷，但在强劲的经济转型推动下，制造业和基础设施投资加速。零售环比改善表明消费企稳。鉴于良好开局和持续的政策支持，我们将 2024 年 GDP 增长预测从 5%上调至 5.2%。

预计宏观政策支持持续。除了加大财政支持外，设备升级和消费品以旧换新计划等新的政策举措有助增加投资和消费需求。我们仍预计存款准备金率将下调 25 个基点。不过，美元走强可能会限制近期降息空间。

Stronger-than-expected 1Q 2024 GDP bodes well for the rest of the year

GDP growth came in stronger than our and the Bloomberg expectation (actual: 1.6% QoQ versus consensus: 1.5% QoQ and our forecast: 1.3% QoQ). Furthermore, the National Bureau of Statistics (NBS) raised its 4Q 2023 growth estimate by 0.2ppt. As a result, annual GDP growth accelerated from 4.8% YoY to 5.3% YoY in 1Q 2024, despite a high base in 1Q 2023.

By industry, China's industrial sectors remain the growth engine of the economy, with year-on-year growth picking up to 6% YoY in 1Q 2024. By contrast, services growth slowed from 5.8% YoY to 5.0% YoY amid waning demand and base effects.

March data distorted by CNY holiday and base effects

IP growth slowed to 4.5% YoY in Mar, which was softer than the consensus expectation of a 6% YoY rise and our estimate of a 6.2% YoY rise. Seasonal adjusted sequential IP contracted by 0.1% MoM, after several months of strong expansion.

By industry, growth in mining output slowed to just 0.2% YoY, probably because the cold winter had affected mining activity. Manufacturing output expanded 5.1% YoY, slightly softer than the previous two months. Auto, chemicals, computers, and electronic equipment remain the leading output industries (Fig 1).

Retail sales growth picked up sequentially. Seasonally adjusted sequential growth rose to 0.3% MoM in Mar, the highest level since Oct 2023. In YoY terms, retail sales slowed from 5.5% YoY to 3.1% YoY in Mar (consensus: 4.8% YoY, our forecast: 4.0% YoY), driven by the high base in 2023. By contrast, online sales growth surged as consumers shifted to online spending hoping to take advantage of online sales promotions (Fig 2). Year-on-year growth in most consumer goods categories decelerated, affected by base effects. Catering spending slowed from 12.5% YoY to 6.9% YoY in Mar. Car sales contracted 2.9% YoY, the first contraction since Feb 2023.

Fixed asset investment (FAI) growth picked up to 4.7% YoY in Mar according to our estimate (Fig 3). This was the fifth consecutive month of acceleration. Accelerating manufacturing and infrastructure investment remain the key growth drivers of China's economy, offsetting weakness in real estate investment. By category:

- **Broad infrastructure investment growth accelerated** by almost 2ppt to 11.7% YoY in Mar. Investment growth in traditional infrastructure investment such as railways, highways, and industrial parks, remained solid at 6.6% YoY, a testament to government efforts to bolster growth. Investment growth to decarbonize China's power sector jumped to 31.5% YoY in Mar, proving once again that green investment is of paramount importance to the government.
- **Manufacturing investment growth accelerated** to 10.3% YoY. Broad-based growth picked up across China's manufacturing industries, suggesting industrial upgrades are the dominant theme not only in prioritized areas, such as transportation, electrical machinery & equipment, and nonferrous metals, but also in traditional sectors such as food processing and general equipment.
- **Contraction in real estate investment widened** by 1ppt to 10.0% YoY in Mar by our estimate**.** The outlook for real estate investment remains soft given persistent concerns over funding stress at property developers. Year-on-year contraction in funding widened to 29% YoY amid broad-based weakness.

Volume-based property indicators make for a weak outlook. The contraction in property starts in Mar eased slightly, but was still wide at 25.6% YoY. Property under construction and property completions contracted 19.1% YoY and 25.1% YoY in Mar, 8ppt and 1ppt wider than they were in Jan-Feb. Property sales contracted 23.7% YoY, which was marginally better than the previous period and consistent with gradual improvement revealed in the high frequency data (Fig 4).

The average price of new properties in the 70 largest Chinese cities fell 0.34% MoM in Mar, marking eight months of consecutive decline. Downward price pressure was heavier in lower-tier cities.

Inflation fell sharply in Mar, driven by waning seasonal demand, as we expected. Consumer inflation slowed notably to 0.1% YoY in Mar, after a 0.7% rise in Feb, lower than the market expectation of 0.4%. Sequentially, inflation fell 1% MoM in Mar, following a 1% MoM rise in Feb. Seasonal holiday demand faded, with food inflation and transportation and communication inflation down 2.7% YoY and 1.3% YoY, respectively. Outside food, travel, and fuel prices, overall inflation remains soft. Low core inflation reminds us that domestic consumption demand is still soft.

PPI registered a 2.8% YoY decline in Mar. Sequentially, PPI inflation fell for the fifth consecutive month, this time by 0.1% MoM. Despite rising global commodity prices, declining mining and quarrying costs weighed on Chinese PPI in Mar.

Total social financing (TSF) rose 8.7% YoY in Mar, the slowest pace on record. We attribute the slowdown in growth to slower bank loan expansion and government bond issuance. By contrast, shadow credit and corporate bond issuance rebounded slightly. Both medium- to long-term (ML) corporate and household borrowing slowed on a year-on-year basis, partly because of a high base. Sequential growth in both measures rebounded slightly.

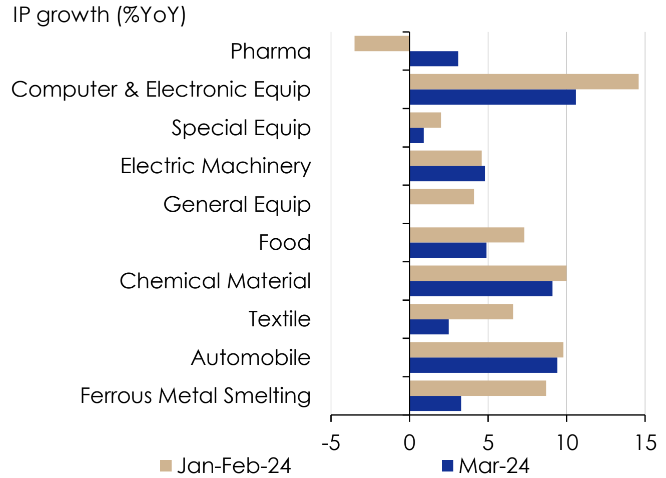
Our view:

While much of the monthly data for 1Q was distorted by the CNY holiday effect, average growth momentum suggests a solid start to the year, consistent with our expectation of an economic recovery (*Big Picture: 2024 macro outlook – more recovery ahead*). Solid growth momentum will likely persist in the near-term, in our view. Both the Caixin and official manufacturing PMIs have exhibited similar improving trends, suggesting that the slower sequential IP growth in Mar could be a one-off after several months of expansion. Accelerating fixed investment highlights the strong economic transition, driven by industrial upgrades, the green transition, and technological innovation, all compensating for the prolonged property downturn. Furthermore, the official new export order sub-PMI has improved, suggesting rising external demand. Sequential improvement in retail sales suggests stabilizing consumption. Given these tailwinds, we raise our 2024 growth forecast from 5.0% to 5.2%.

Pro-growth policies should sustain the current momentum, in our view. Fiscal policies are likely to be more supportive than they were last year (details here). New policy initiatives such as large-scale equipment upgrades and consumer goods trade-ins could add to investment and consumption demand.

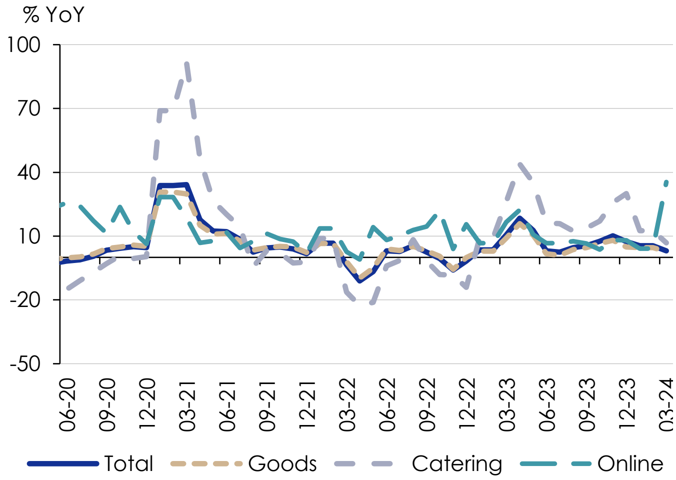
The recent PBoC communication re-iterated the imperative of maintaining sufficient liquidity. At the monthly medium-term lending (MLF) facility rollover, the PBoC reduced its net liquidity injection by RMB70b, while maintaining the 1-year MLF rate at 2.5%. Such a small reduction likely represents an adjustment to overall liquidity, rather than a shift in the PBoC's policy stance. We continue to expect a 25bp cut to the RRR though the strong US dollar may limit the room for interest rate cuts in the near-term.

Fig 1: Output in auto, computers & electronics, and chemicals remains strong



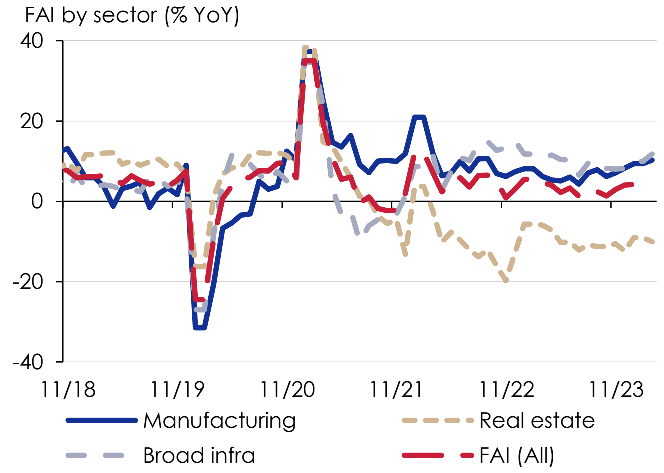
Source: NBS, CCBIS

Fig 2: Online spending growth surged in Mar



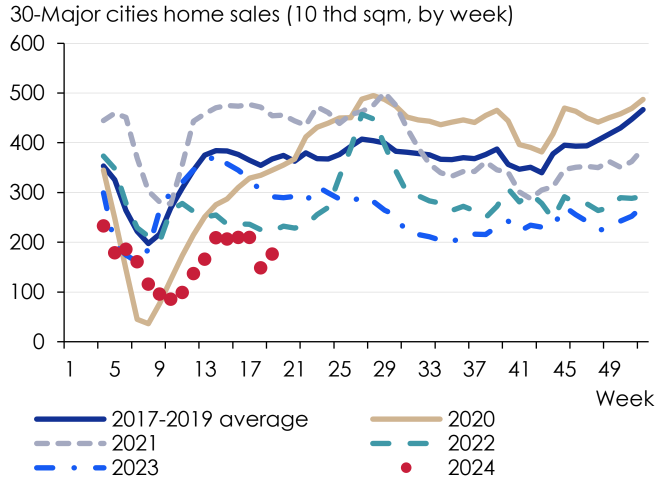
Source: NBS,CEIC, CCBIS

Fig 3: Manufacturing and infrastructure investment picked up, offsetting falling property investment



Source: NBS, CCBIS

Fig 4: Property sales sequentially improved, but remained soft



Source: NBS,Wind, CCBIS

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CCB International Securities Limited
12/F, CCB Tower, 3 Connaught Road, Central, Hong Kong
Tel: (852) 3911 8000 / Fax: (852) 2537 0097s