China's modest recovery

Tommy Xie Dongming
Economist
+65 6530 7256
xied@ocbc.com

- **Auto sector led the recovery**
- **Infrastructure investment is doing the heavy lifting reversing the decline trend of overall fixed asset investment for the first time in 2022. d**
- **Manufacturing activity remains resilient.**
- **Property sector will remain the weakest link for a while.**
- **Weak sentiment in the household sector remains the key challenge.**

China's key August economic indicators beat market expectation. Industrial production and retail sales growth accelerated to 4.2% yoy and 5.4% yoy respectively in August from 3.8% yoy and 2.7% yoy in July. In addition, fixed asset investment rebounded to 5.8% yoy in the first eight months from 5.7% yoy in the first seven months, reversing the decline trend for the first time this year (Chart 1).

Auto sector led the growth

Auto sector continued to recover from the disruption in the second quarter during the Shanghai lockdown. In addition, China has also stepped up its stimulus to boost both auto output and demand. On 18 August, China's State Council announced to extend the vehicle purchase tax exemption for new energy vehicles by another year to the end of 2023.

Retail sales of auto rose by 15.9% yoy in August while auto production in August jumped by 39% yoy. Excluding auto sales, China's August retail sales would only grow by 4.3% yoy instead of 5.4% headline growth (Chart 2).

Chart 1: Fixed asset investment rebounded for the first time in 2022.

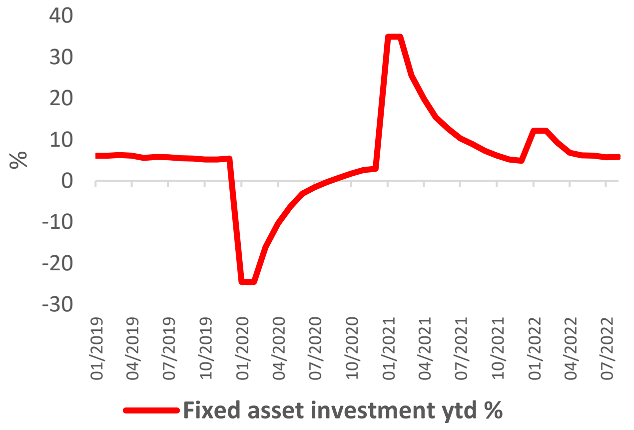
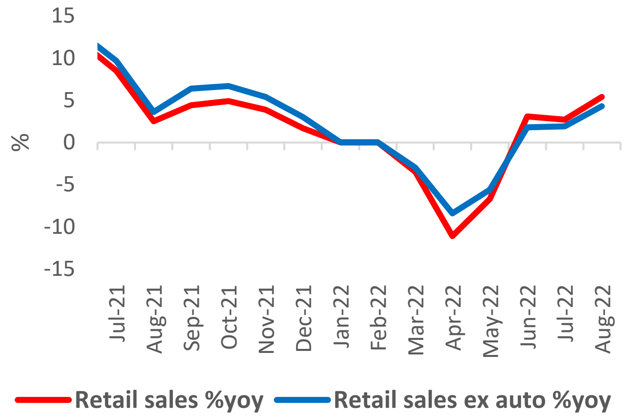


Chart 2: Retail sales ex auto would only grow 4.3% yoy vs. 5.4% headline growth

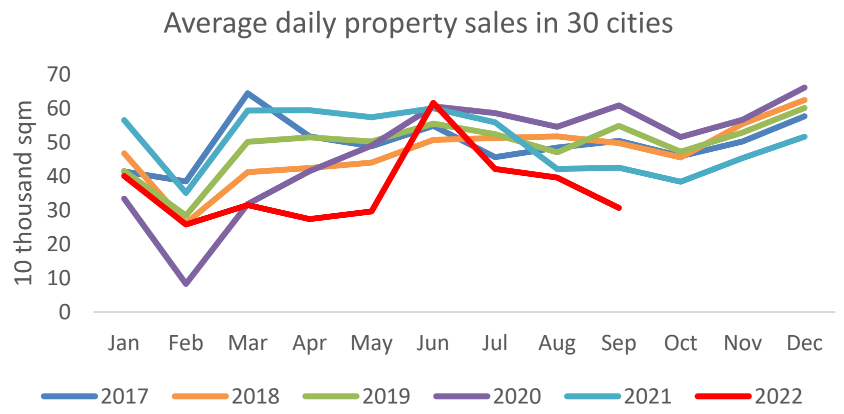


Source: Wind, CEIC, OCBC Bank

Property market remains the weakest link
China's property investment contracted further by 7.4% yoy in the first eight month from 6.4% yoy contraction in the first seven months. Property market has been the key drag on the growth this year and there is no sign of imminent recovery.

The high frequency daily property transaction volume showed that average daily property sales in the first half of September in 30 major cities fell by 27.7% yoy despite easing measures (Chart 3).

Chart 3: No golden September this year in property market.



Source: Wind, CEIC, OCBC Bank

The only bright spot is that source of funds for developers improved slightly with the decline narrowed slightly to 25% yoy in the first eight months from 25.4% yoy in the first seven months (Chart 4).

Nevertheless, the appetite for land acquisition remains weak. The collapse of land purchase by area widened to 49.7% yoy from 48.1% yoy (Chart 5). This signals weak property investment ahead.

Chart 4: Developer's source of funds improved

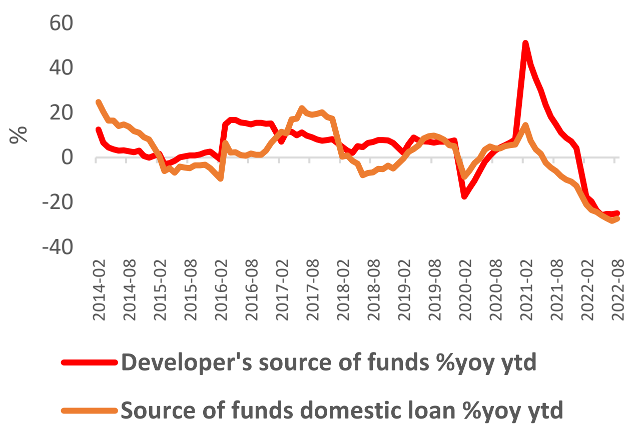
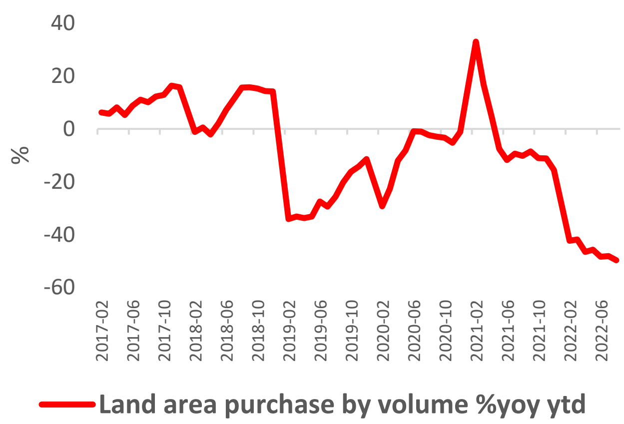


Chart 5: But demand for land remained weak



Source: Wind, CEIC, OCBC Bank

Infrastructure investment to play a bigger role
Against the backdrop of sharp deceleration of property investment, infrastructure investment growth accelerated to 8.3% yoy in the first eight months from 7.4% yoy in the first seven months on the back of policy and funding supports (Chart 6). We expect China's infrastructure investment to accelerate further to 10% in the coming months, which will offset the loss from the property investment.

Manufacturing investment remains resilient
Other than that, manufacturing sector remains resilient on the back of supply chain upgrade and more funding supports despite rising uncertainty from the external demand. Manufacturing investment accelerated to 10% yoy in the first eight months from 9.9% yoy in the first seven months.

Investment in high tech sectors rose by 20.2%. Of which, investment in high tech manufacturing increase by 23% yoy.

Chart 6: Stronger infrastructure investment and resilient manufacturing investment

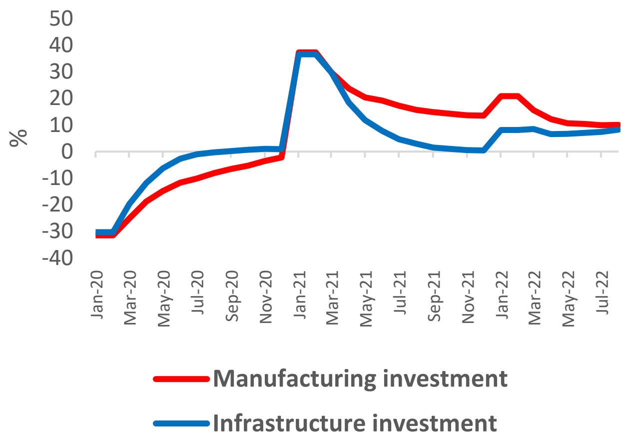
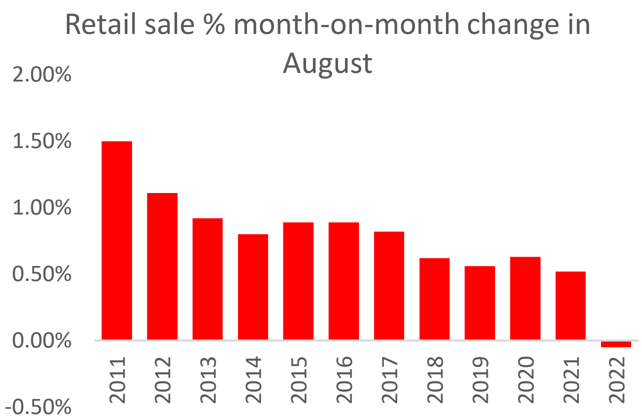


Chart 7: Retail sales fell month-on-month in August for the first time despite strong headline reading



Source: Wind, CEIC, OCBC Bank

Weak sentiment remains the key challenge
Other than auto sales, the rebound of catering and restaurant sales to 8.4% yoy in August after falling for five consecutive months was encouraging. This was probably due to revenge demand after some big cities emerged from the lockdown. Nevertheless, given the recent outbreak in megacities such as Chengdu and Shenzhen, the catering sales is likely to slow down.

Despite stronger than expected year-on-year growth, retail sales fell by 0.05% month-on-month seasonally adjusted (Chart 7). This was the first mom decline in August since China started to publish the mom reading in 2011. This shows a slow recovery of consumption due to fragile household sentiment.

The latest August credit data reinforced the concern about weak sentiment in the household sector. Medium to long term loan to household sector only increased by CNY265.8 billion, CNY160 billion below that in August 2021. Household deposit increased by CNY828.6 billion, way above average CNY330 billion increase in August in the past four years. The deteriorating household sentiment remains the key challenge for the Chinese economy.

Chart 8: Medium to long term loan to household sector remained weak

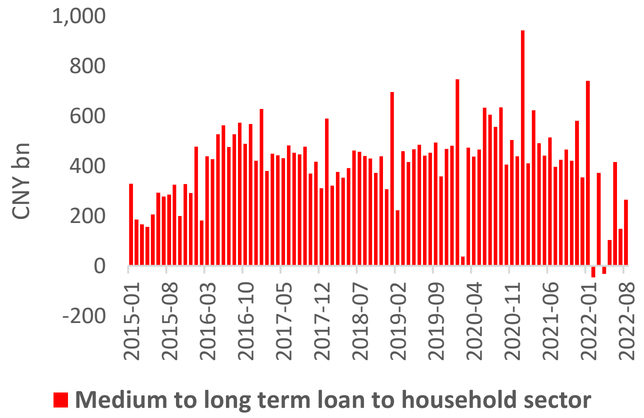
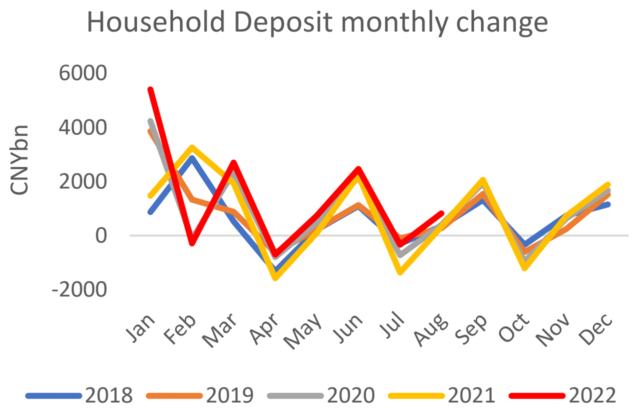


Chart 9: Household deposits increased sharply due to higher propensity to saving.



Source: Wind, CEIC, OCBC Bank

With China's dynamic zero Covid strategy in place, the weak sentiment in household sector is likely to slow down China's recovery pace. We think China's growth is unlikely to return to above 4% in the third quarter.

Co.Reg.no.:193200032W