China

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China's roadmap to 5% without heavy reliance on the property market

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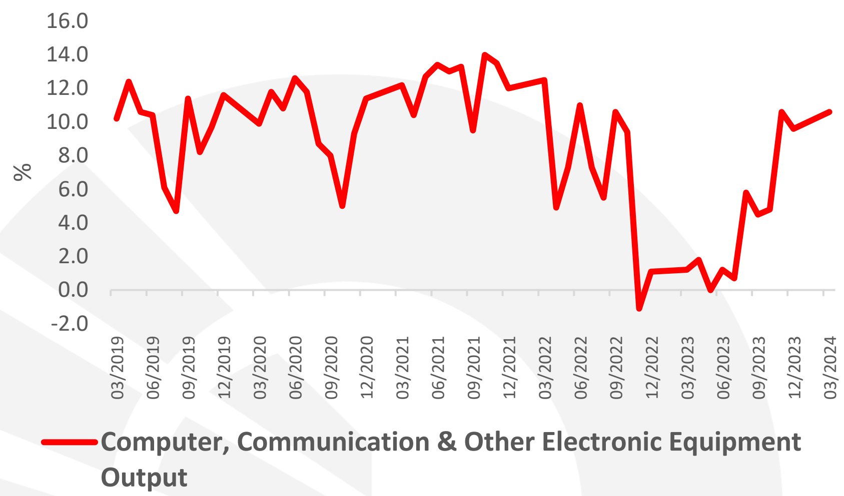
- This robust growth in the first quarter was underpinned by several key factors: resilient industrial activities, strong service consumption, and a rebound in external demand.
- It is possible for China to achieve its growth target without heavy reliance on the property market.
- Nevertheless, given the uncertainties surrounding both domestic and external demand, we believe that the stronger-than-expected first-quarter GDP data is unlikely to deter further monetary easing and demand-side measures.

The Chinese economy exceeded expectations, growing by 5.3% year-on-year in the first quarter, accompanied by a sequential quarter-on-quarter growth of 1.6% after seasonally adjusted. This robust expansion was underpinned by several key factors: resilient industrial activities, strong service consumption, and a rebound in external demand.

Industrial output surged by 6.1% year-on-year, marking an acceleration from the 4.6% growth seen in 2023. Notably, the growth rate surpassed that of the first quarter of 2023 by 3.1%, indicating a significant recovery from the Covid-related disruptions. The high-tech sectors also demonstrated notable strength, with a 7.5% year-on-year increase, highlighting the positive trajectory towards high-quality growth.

Chart1: Strong recovery of electronic equipment output



In the service sector, value added rose by 5% year-on-year, with contact-based services such as catering, transportation, and tourism experiencing robust growth. Retail sales of services expanded by 10% year-on-year, outpacing the growth in retail sales of consumer goods at 4.7%. The recent Qingming festival holiday travel saw per capita spending surpass pre-Covid levels for the first time, signaling a promising trend in consumer confidence. Additionally, nominal disposable income grew by 6.2% year-on-year, outpacing nominal GDP growth and further supporting consumer sentiment.

In terms of trade, total trade in RMB terms increased by 5% in the first quarter, aligning with the global trade recovery narrative for 2024. Notably, China's trade surplus in dollar terms reached $183.7 billion for the first quarter, a historic high for this period, indicating the resilience of external demand. While the breakdown of GDP based on the expenditure method was not provided, it was estimated during a press conference that domestic demand contributed approximately 85.5% to GDP growth, implying a positive contribution from external demand of around 14.5%, a significant improvement from the previous quarter.

Property: no light at the end of tunnel

China's property sales by value experienced a significant decline of 27.6% year-on-year in the first quarter, while fixed asset investment contracted by 9.5% year-on-year. Furthermore, recent high-frequency data indicates that there has been no indication of recovery in property transactions in major cities during the first half of April, suggesting that the property sector is likely to remain a weak point in the near term.

The central question arises: Can the Chinese economy achieve its growth target without heavy reliance on the property market? The latest first-quarter data suggests that this is indeed feasible, driven by improving external demand and enhanced demand-side support measures.

Filling the gap

The Chinese government is choosing to push for equipment upgrade and trade-ins of consumer goods given the softening property market. By stimulating consumption in bulk items like home appliances and automobiles, this initiative enhances the likelihood of China reaching its growth target without relying heavily on the property market.

The equipment upgrade and trade-in of consumer goods are not a panacea for solving China's structural problems. However, they serve as short-term solutions that can buy China more time to rebalance its economy. Historical evidence supports the effectiveness of these measures, as seen in the previous round of trade-in programs for household appliances.

For instance, the pilot project that began in June 2009 and expanded nationwide in April 2011 resulted in a direct consumption surge of 342 billion yuan, thanks to a cumulative subsidy of 30 billion yuan allocated by the central government based on the data from Commerce Ministry. This demonstrates an encouraging multiplier effect. Based on that multiply effect, it shows that for every 100 billion yuan subsidy, China's consumption of home appliances may expand by 800-900 billion yuan. This accounts for more than 1.5% of total retail sales and may help offset the decline in property-related transactions.

Mixed demand picture

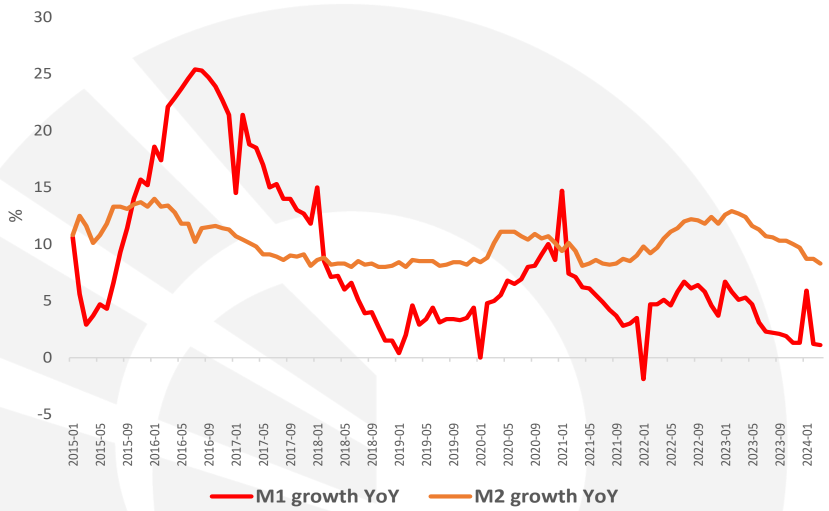
Despite some initial indications of recovery, recent inflation and credit data continue to reflect an uncertain outlook for domestic demand. China's GDP deflator, estimated to be around -1.07% in the first quarter, has remained negative for the fourth consecutive quarter.

Chart2: GDP deflator has remained negative for the fourth straight quarter

On credit data, China's new Yuan loans increased by 3.09 trillion yuan in March, indicating a reduction of 800 billion compared to March 2023. Notably, medium to long-term loans to both corporate and household sectors experienced declines compared to the same period in previous year, reflecting ongoing weakness in the real estate market and cautious sentiment in the corporate sector.

Further signaling caution, China's M1 growth decelerated to 1.1% in March from 1.2% in February, indicating that corporates remained hesitant to increase investments in the near term.

Chart3: M1 growth decelerated further



This persistent deflationary trend, decelerating M1 growth and falling loan demand suggest ongoing challenges in stimulating domestic demand and points to the need for continued policy support to bolster economic activity.

In summary, we maintain our outlook that China can attain its growth target for this year without overly depending on a recovery in the property market. Our forecast of 5% growth for the year remains unchanged. Nevertheless, given the uncertainties surrounding both domestic and external demand, we believe that the stronger-than-expected first-quarter GDP data is unlikely to deter further monetary easing and demand-side measures.

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