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China Economics Update: Strong 1Q GDP; Mar economic data showed gradual normalization

(中国 1 季度数据符合预期，复苏正在进行时)

Lulu Jiang
(852) 3911 8012
jianglulu@ccbintl.com

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

China's 1Q GDP came roughly in-line with expectation, growing 18.3% YoY. Mar data suggests that industrial production is still solid, led by momentum in high-tech sectors. Resilient exports and continued industrial upgrades are gradually feeding into manufacturing capex, though real estate investment remained the strongest among the major FAI categories compared to pre-pandemic level. Retail sales beat market expectation, as catering and online-sales rose sharply in Mar while auto sales remained strong.

The latest data suggests that growth recovery is on track. We maintain our yearly growth forecast at 8.5%. Industrial upgrades, consumption recovery and still-solid trade remain the main themes for 2021. Nonetheless, near-term risks including the supply constraint in chips as well as the new variant of COVID-19, the later could delay the recovery of major economies.

In our view, policy makers will tighten incrementally. Credit growth cooled in Mar while the central bank has remained accommodative in terms of the liquidity environment. We expect interest rates to edge up gradually amid more certainty on the growth recovery and rising inflation pressure.

中国第一季度 GDP 大致符合预期，同比增长 18.3%。3 月份的数据显示，在高科技领域的推动下，工业生产仍然保持稳健。出口的强劲和持续的工业升级正逐步推动制造业资本支出的回升，尽管相较疫情前的投资水平，房地产投资仍然最为强劲。零售好于市场预期，3 月餐饮和在线销售大幅增长，汽车销售强于疫情前年份。

最新经济活动数据表明增长正在步入正轨。我们维持 8.5%的年度增长预测。工业升级，消费复苏和稳健的贸易活动仍然是 2021 年的主题。短期风险包括芯片供应紧张以及病毒变种，后者可能会延迟主要经济体的复苏。

我们认为决策者将逐步收紧宏观政策。3 月信贷增长已经开始降温，而就流动性环境而言，央行仍在短期内保持宽松。我们预计随着复苏趋势进一步明确和通胀压力的上升，利率将会逐步抬升。

China's 1Q GDP rose 18.3%, largely in-line with market expectation

According to NBS, China's 4Q GDP grew 18.3% YoY, slightly lower than market expectation and higher than ours (CCBI: 17.8%, consensus: 18.5%). On a sequential basis, seasonally adjusted 4Q GDP rose 0.6%, easing from 2.6% in 4Q20. The average of 5 quarters of sequential growth was at 1.6%, similar to that of 2017 and 2018, suggesting that the pandemic has only had a temporary impact on China's growth trajectory, and that growth momentum has gradually normalized.

Detailed numbers show that secondary industries continued to grow faster than headline GDP, at 24.4% YoY, while tertiary industries delivered more contained growth than the headline at 15.6% YoY. This is consistent with the growth recovery that has been led by strong momentum in industrial activity while the service sector has recovered with some lag.

Mar economic indicators suggest that growth momentum has started to diverge: retail sales beat market expectations, while IP and FAI started to normalize

Industrial production (IP) held up at a solid pace, despite some sequential deceleration. On a sequential basis, IP eased slightly in Mar from the past three months, growing an average of 0.6% MoM seasonally-adjusted, or 7.4% annualized (vs. avg of 8.3% in Dec 2020 – Feb 2021), still solid compared to pre-pandemic levels (around 0.5 – 0.6% MoM growth). Among the three major industrial categories, IP for manufacturing was the strongest, rising 15.2% YoY, as it continued to outperform headline growth. IP for high-tech manufacturing eased from the past two months, but maintained a faster growth pace than the headline, rising 31.2% YoY in Jan - Mar (vs. 49.2% in Jan – Feb), indicating that continued industrial upgrades along with resilient tech exports remain key drivers of IP growth.

Retail sales were strong. Retail sales rose 34.2% YoY in the month of Mar (consensus: 28%). Catering rose meaningfully in Mar (Fig 1), outpacing already-strong growth in the beginning of the year (91.6% YoY in Mar vs. 68.9% YoY in Jan - Feb). Consumption recovery is more than the low base: compared to the pre-pandemic average during 1Q, most goods sales together with catering delivered positive growth. Sales in communication appliances, cosmetics, beverages and daily used goods all growing more than 20% (Fig 2). In contrast, housing related items as well as medicine were lower than pre-pandemic levels, possibly reflecting tighter housing measures and China's control over the pandemic. Overall, data is in-line with our view that consumption will be a main driver for this year's economic growth.

Strong fixed asset investment (FAI) growth mostly reflected the low base. FAI rose 25.6% YoY in Jan – Mar, in line with market consensus of 26%. Based on our calculation, FAI rose by 12.3% in 1Q compared to the average 1Q levels in 2017 – 2019 (pre-pandemic years). Among which, real estate remained the fastest growing sector, up by 28.6%, while infrastructure investments, taking into consideration investments in electricity, gas & water production and supply, rose by 11.6% (infra FAI excl. E&G up 11.4%). Despite a strong rebound in manufacturing FAI on a YoY basis, the pickup when compared to pre-pandemic levels remained relatively low, at only 1.2%.

Real estate investments expected to cool on the back of tightening measures. 1Q sales data looked particularly strong (Fig 4), even compared to pre-pandemic years, rising 21.4%, consistent with rising property prices and private sector credit demand in recent months (Fig 5). Nonetheless, growth in started floor space was only 3.4% higher than in pre-pandemic periods, together with declining land sales in recent weeks (Fig 6), all indicating that property investments will cool down in the coming months.

Trade data released earlier this month remained strong. Total exports rose 30.6% YoY in Mar (consensus: 38%), and 1Q exports were more than one-third higher than the pre-pandemic 1Q level. Exports to the US in Mar remained the fastest growing among China's major trading partners (+53.3% YoY), while the major export commodities including home appliances, integrated circuits, data processing equipment and parts, as well as cars (including chassis) all expanded their share when compared to 2019. As such, China has maintained its strong trade performance, notwithstanding the stronger competition as global production recovers. Import growth of around 38.1% YoY was mostly driven by strong commodity prices that increased over 80% YoY in Mar. Import volume growth diverged: while imports for crude oil, iron ore and copper were strong, imports of coal and refined petroleum remained sluggish.

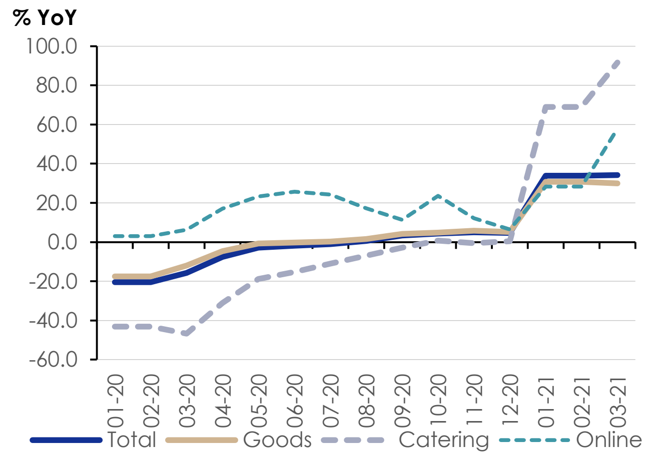
Our view:

March data confirms steady recovery consumption while manufacturing momentum remains solid. Strong industrial sector growth is, supported by solid external demand and industrial upgrades (Fig 6). Auto sales and off-line services have furthered their momentum, supporting a strong recovery in consumption. Infra spending has received support from increased fiscal support and new local government bond issuance after the national two sessions. The property sector has shown early signs of softening, though sales growth stayed strong during 1Q.

We maintain our forecast for full-year growth at 8.5% , supported by consumption, manufacturing upgrades, and continued global recovery. One key risk is the chip supply shortage that may put some constraints on the tech manufacturing sector. So far, there were few signs of meaningful impact on Chinese production, except for the auto sector: production declined 23% QoQ in the first quarter of this year after a strong 4Q. However, the impact is expected to be temporary, with much of the pressure brought by supply chain disruption to be alleviated in the second half.

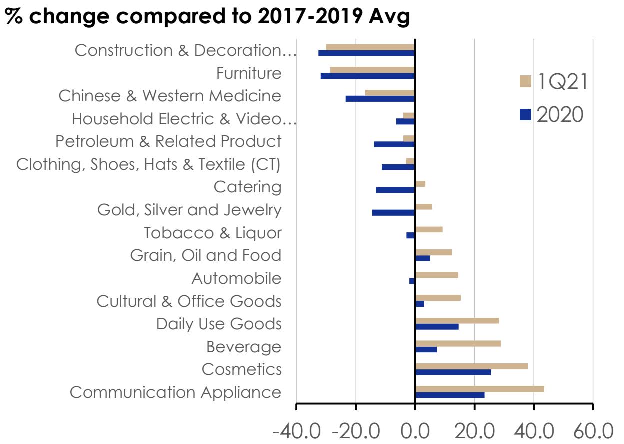
Incremental policy tightening expected. Today's data should provide some confidence to the government that a tighter stance is warranted, especially as the recovery in consumption should benefit the services sector and job growth. Monetary policy started to normalize in 2H last year, though overall the policy stance is more accommodative than pre-pandemic levels. The central bank has kept liquidity conditions balanced in recent months. For instance, the PBoC injected RMB150b through MLF on Apr 15th, just enough to match the matured amount. Policy controls on the property sector are likely to continue, given the still strong momentum in the property sector, and interbank rates will likely trend higher with the reflation trend.

Fig 1: Service sector recovered with improving consumer confidence, online and caterings are particularly strong



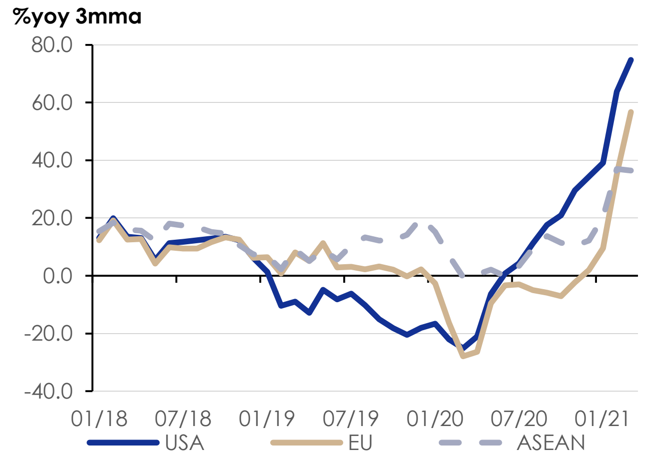
Source: NBS, CCBIS

Fig 2: Compared to pre-pandemic years, sales remained strong for consumer discretionary, while housing related items retreated



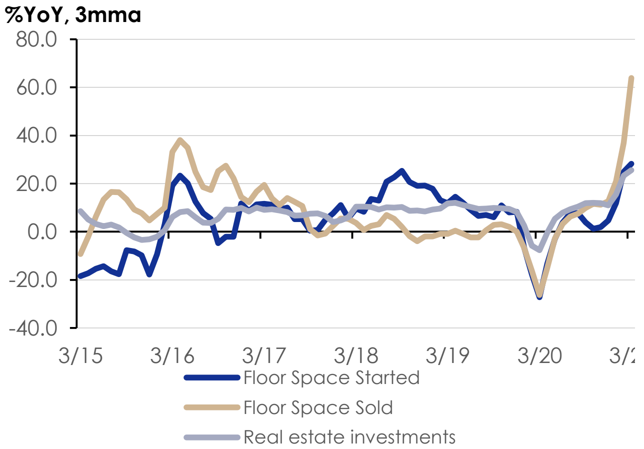
Source: NBS, CCBIS

Fig 3: Exports to the US remained the strongest



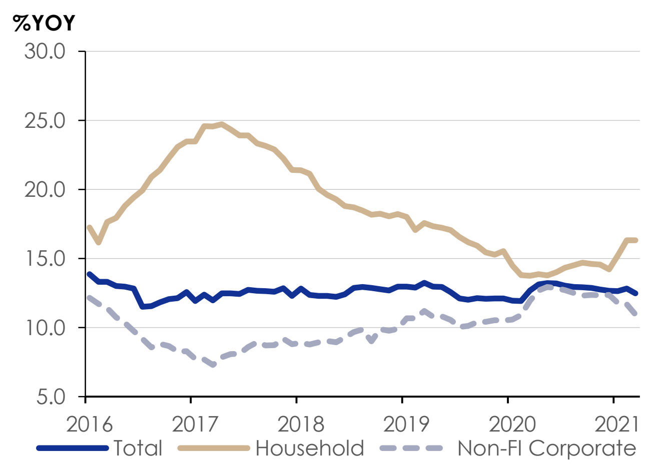
Source: NBS, CCBIS

Fig 4: Property sales were particularly strong in Mar



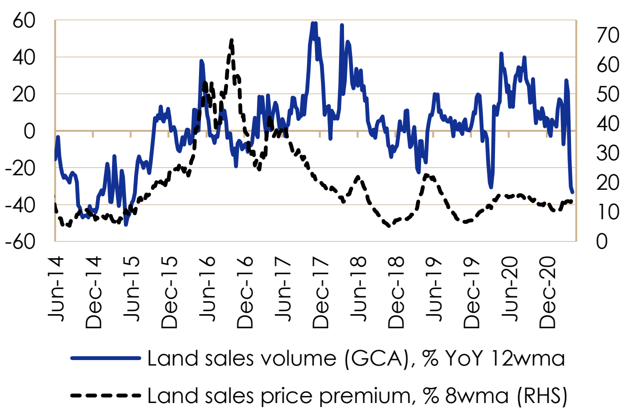
Source: CEIC, CCBIS

Fig 5: Medium to long-term loan growth of the private sector was strong in the beginning of the year



Source: CEIC, CCBIS

Fig 6: Land transaction has declined sharply three weeks since Mar 26, suggesting moderating property investments going ahead



Source: Wind, CEIC, CCBIS

Rating definitions:

Outperform (O) – expected return > 10% over the next twelve months
Neutral (N) – expected return between -10% and 10% over the next twelve months
Underperform (U) – expected return < -10% over the next twelve months

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