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China Economics Update: China economic data held up, defying the expectation of a slowdown
(中国经济数据表现强劲，减少市场对复苏乏力的担忧)

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中国 6 月经济数据表现强劲，零售和生产均超出预期。高科技带动了工业生产活动。房地产投资有所降温，而持续的产业升级进一步推动制造业资本支出。虽然二季度 GDP 同比增幅略低于市场预期，但环比增速加快，服务业增速回升预示经济进一步正常化。

下半年经济预计受到消费修复、制造业升级和全球持续复苏的支持。我们维持全年增长 8.5% 的预测。风险一是芯片供应短缺，可能制约贸易和制造业增长，二是 Delta 变种病毒超预期传播，带来全球经济重回风险。目前看这些风险因素范围有限。

六月数据有助减少市场对中国经济复苏乏力的担忧。就此而看，近期的降准将更可能是技术性驱动，降低银行融资成本，而非全面的货币宽松转向。未来央行流动性管理细节或会提供更加明确的政策方向。

June data was strong, with retail sales and production both beating expectations. Industrial production was led by momentum in high-tech. Real estate investment has shown signs of cooling, while continued industrial upgrades are feeding into manufacturing capex. Although 2Q GDP was slightly below market consensus, it gained sequentially, and the pickup in services growth points to further normalization of the economy.

We maintain our forecast for full-year growth of 8.5%, supported by consumption, manufacturing upgrades, and the continuing global recovery. One key risk is the chip supply shortage that may put constraints on the tech manufacturing sector; another is the spread of the Delta virus.

Today's data should instill greater confidence that China's economy is on a steady recovery path and that the recent RRR cut was driven primarily by technical factors. We maintain the view that the latest RRR cut represents another step in the broader structural adjustment designed to lower bank funding costs, rather than a case of broad-based monetary easing. The future direction of central bank liquidity management should give more clarity on the policy direction.

China's 2Q21 GDP rose 7.9%, slightly below market expectation

According to NBS, China's 2Q GDP grew 7.9% YoY, slightly lower than the market expectation and higher than ours (CCBI: 8.1%, cons: 8.0%). On a sequential basis, seasonally adjusted 2Q GDP rose 1.3%, up from 0.4% in 1Q.

Detailed figures show that tertiary industries delivered faster growth than the headline at 8.3% YoY, while secondary and primary industries grew 7.5% YoY and 7.6% YoY, respectively, a pattern that underpinned the economic transition that was interrupted by the pandemic. One interpretation could be that the growth recovery that had once been led by strong industrial activity is now being led by the services. Among the service sectors, transportation, storage & post, and IT services increased notably in 1H, by 21% and 20.3%, respectively, compared with 11.8% growth for the overall service sector.

June economic indicators suggest that growth momentum remained strong: IP, retail sales, and trade all beat market expectations, while FAI was in line with consensus

Industrial production (IP) held up at a solid pace as sequential growth edged up. IP rose by 8.3% YoY in June, beating the market expectation (cons: 7.9%). On a sequential basis, IP ticked up in June from the past two months, to 0.6% MoM seasonally-adjusted, or 6.9% annualized (vs. an average of 6.5% for the past two months), similar to pre-pandemic levels of around 0.5-0.6% MoM growth. Produciton showed broad-based strength as IP growth for most sectors, including materials, equipment, and high-tech, either held up or improved, having benefiting from solid trade and domestic demand. High-tech manufacturing growth was particularly strong, rising 18% YoY in June (vs. an average of 15.1% YoY in Apr-May), suggesting continued industrial upgrades along with resilient tech exports are still driving IP growth. Auto production, by contrast, contracted from a year ago, possibly reflecting supply bottlenecks caused by the global chip shortage.

Retail sales were stronger than expected. Retail sales rose 12.1% YoY in the month of June (cons: 10.8%). Catering eased from previous months as the high base effect gradually faded, though it remained the fastest growing retail category (Fig 1). Improvement in online sales was also notable, having risen 11.7% YoY compared with an average of 7.3% YoY in previous two months. Meanwhile, the consumption recovery has played a bigger part than the low base: most consumer goods categories and catering outperformed in 1H21 compared with same period in 2019, with medicine and petro the sole exceptions (Fig 2). Overall, retail data came in much better than the market has initially expected, despite the pandemic situation in Guangdong province, supporting our view that consumption will remain a driver of economic growth this year.

Divergent fixed-asset investment (FAI) growth. FAI rose 12.6% YoY in 1H21, in line with market consensus. Based on our calculations, FAI rose by 6.0% YoY in June, or 11.7% if compared with the same month in 2019 (pre-pandemic). Notable changes in specific FAI categories included:

- June manufacturing FAI growth, which accelerated (16.4% YoY in June vs. 13.5% YoY in May), and
- Traditional infrastructure investment, which continued to slow although the pace relented somewhat (-1.5% YoY in June vs. -2.5% YoY in May).

Real estate investment continued to ease (6.0% YoY in June vs. 9.8% YoY in May). **Other property indicators continue to cool as expected.** In YoY terms, property starts and sales data both eased from earlier highs (Fig 4). The slowdown in new starts and the decline in sales in recent months suggest that though private sector housing demand was resilient, property investment is likely to cool over the coming months owing to policy restrictions.

Trade data released earlier this week beat market expectations. Total exports rose 32.2% YoY in June. Among China's major trading partners, export demand remained strong for ASEAN countries, while export growth to the US and EU both eased from recent peaks (Fig 5). In June, import growth of 36.7% YoY was in large part due to the price increase. Import volume growth in June declined in YoY terms across most categories, except for coal, which rose 12.3% YoY, and copper, which rose 4.8% YoY.

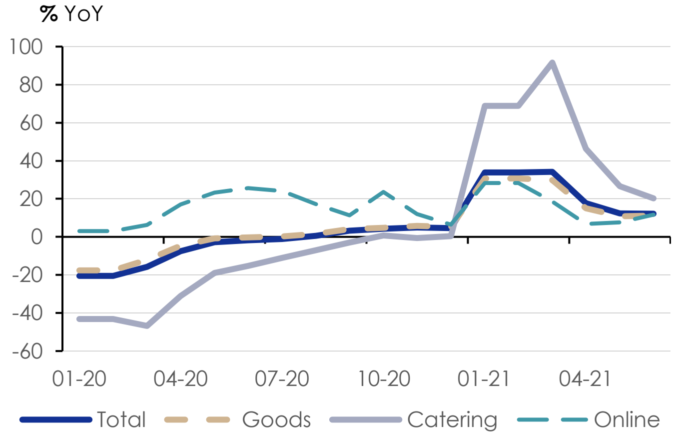
Our view:

June data confirms that the steady economic recovery continues, alleviating concerns over downside risks. Strong industrial sector growth has been supported by solid external demand and industrial upgrades (Fig 6). Despite the temporary lockdown of Guangdong province, retail sales continued to recover, with online sales outperforming. Due to the still strong export sector and industrial upgrade requirements, investment in manufacturing FAI growth continued to accelerate as infrastructure spending received support from improved fiscal conditions and gradually increasing local government bond issuance. The property sector has shown further signs of softening, though sales growth was strong.

We maintain our forecast for full-year growth of 8.5%, supported by consumption, manufacturing upgrades, and the continuing global recovery. One key risk is the chip supply shortage that threatens to place constraints on the tech manufacturing sector. Another concern is a widespread outbreak of the Delta virus. So far, there have been few signs that these factors have had a meaningful impact on China's export sector. We see strength in external demand extending into 2H21F. From the recent trend, it appears that production has normalized in terms of speed of growth. Continued industrial upgrades as suggested by the strong trend in high-tech manufacturing is expected to provide support for Chinese IP in the coming months.

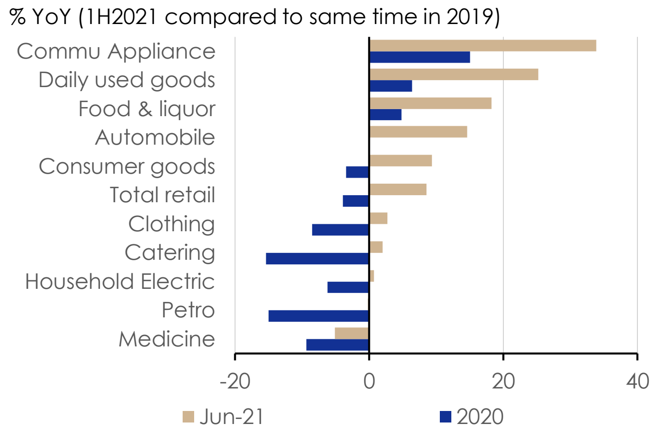
Dovish policy signal appeared to be more technically driven. Today's data should instill more confidence that China's economy is on steady recovery path. Strong credit data for June indicates solid private demand and continued PPI price pressure. Together, these developments suggest limited scope or need for sustained easing. The dovish signal given by the recent PBOC RRR cut now appears to have been primarily driven by liquidity demand amid large MLF maturing in 2H21. Nonetheless, the central government has turned cautious on word of the spreading Covid Delta variant. We maintain our view that the latest RRR cut represents another step in a broader structural adjustment designed to lower bank funding costs, rather than a case of broad-based monetary easing. The future direction of central bank liquidity management should offer more policy clarity.

Fig 1: Service sector recovered with improving consumer confidence; online sales growth accelerated



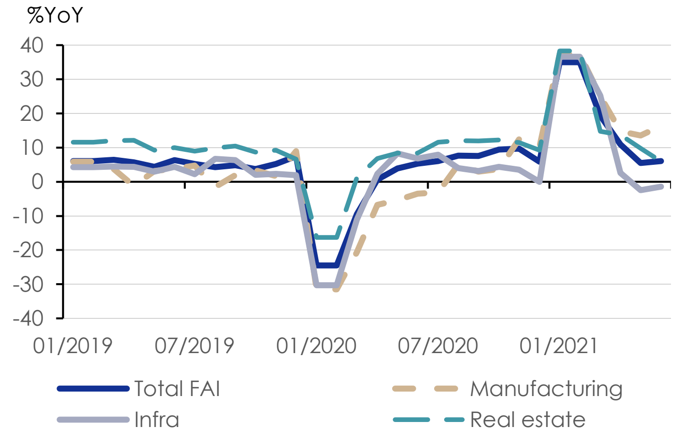
Source: NBS, CCBIS

Fig 2: Compared with 1H19, sales improved for most categories, pointing to continued normalization



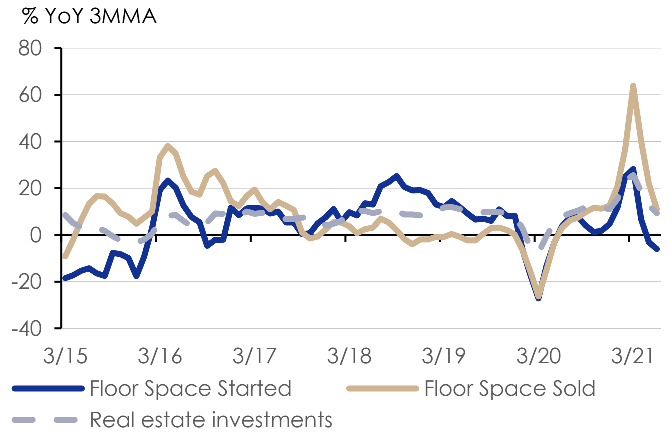
Source: NBS, CCBIS

Fig 3: Manufacturing capex led the pickup in FAI



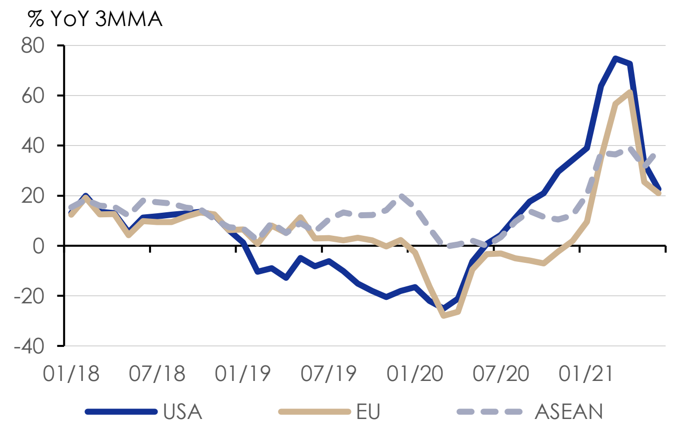
Source: NBS, CCBIS

Fig 4: Property indisctors eased from earlier highs



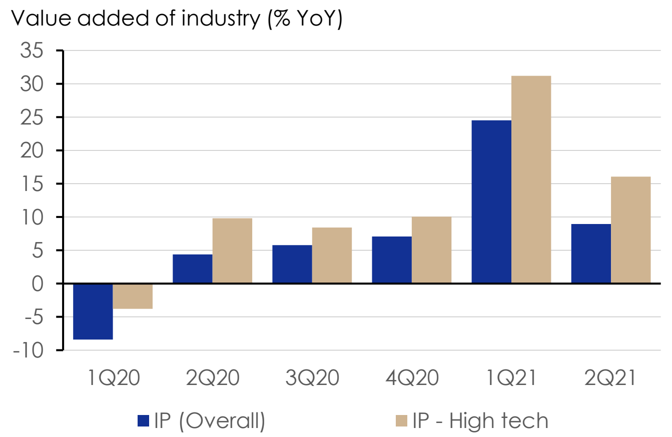
Source: CEIC, CCBIS

Fig 5: Export growth to US and EU moderated, while demand from ASEAN countries held up



Source: CEIC, CCBIS

Fig 6: Continued industrial upgrades are expected to support IP growth in coming months



Source: Wind, CEIC, CCBIS

Analyst certification:

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