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Creating Opportunities

China | Real estate stimulus and loosening “zero Covid” policy help to rebuild sentiments

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November 15, 2022

In 2022, the Chinese economy experienced a bumpy recovery since Shanghai lockdown was lifted, due to the two main downside risks: housing market crash and “zero Covid” policy. Amid economic slowdown, recently, the authorities promulgated policy stimulus on the housing market and at the same time loosened “zero-Covid” policy restrictions in a bid to tackle these two main risks of the economy.

In particular, the initiatives of the recent “16-point plan” by the PBoC and CBIRC to support real estate market soft-landing range from addressing the liquidity crisis faced by developers to an easing of a signature restriction on bank lending and to facilitating home-buyers financing needs etc., which indicates the authorities’ full efforts to bail out the tumbling real estate market. In addition, with the rest of the world moving to “co-existence” strategy for Covid-19 pandemic, Chinese authorities also started to ease the previously strict “zero Covid” measures, chief among them is to shorten the quarantine length for overseas travelers from “7+3” to “5+3”. Although it is still far from a complete lift of “zero Covid” strategy which we anticipate will be after March 2023, the recent beginning of the easing measures, together with President Xi’s high-profile foreign visit in G-20 in Bali of Indonesia, all signalled a gradual ease of “zero Covid” policy is on the way. In addition, the ongoing President Xi and Biden’s meeting during G20 in Bali also gave the market some positive signals on China-US relationship, as the two sides seek to avoid escalating competition into conflicts in the future and the US also re-claimed the “One China” principle on the Taiwan issue.

Based on these two important policy moves, we maintain our 2022 prediction at 3.6% (IMF: 3.3%, Bloomberg consensus: 3.4%) and anticipate growth will bounce back to 5.3% in Q4 amid the policy support. As the US and EU lowered their 2023 GDP forecasts to a large extent to indicate the recession fear, we accordingly lowered our 2023 GDP from 5.2% to 5% modestly, reflecting a decelerating external demand. However, due to the statistical base effect and the 20th National Congress’ growth target of 2020-2035 to “double GDP or GDP per capita” during this period which requires an annual growth of 4.5-4.7%, we do not lower our 2023 forecast to a further extent.

However, October activity indicators remained lackluster and worse-than-expected, due to the recent large number of Covid-19 affected cases in mainland China (more than 17,000 daily cases), indicating the economic recovery will be quite bumpy and the policy effort to try to solve the “dilemma” of balancing “zero Covid” and economic growth will be challenging going forward.

On the supply side, the year-on-year growth of industrial production in October significantly decelerated to 5% y/y from 6.3% y/y in the previous month, lower than the market consensus at 5.2% y/y, and its seasonal adjusted m/m growth also dipped from 0.84% m/m to 0.33% m/m. By categories, the highest growth component continued to be the electric vehicle production which maintained its momentum at 84.8% y/y, compared with110% y/y in the previous month (ytd y/y: 108.4%), supported by the authorities’ priority of green economy and new energy sector to

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fulfill the carbon neutrality target in 2030. However, due to the surging Covid-19 cases in the past month together with a tumbling external demand, many sectors recorded negative growth of production, such as unicircuit (-26.7% y/y), computer equipments (-16.6% y/y), hydraulic electricity generation (-17.7% y/y) etc. (Figure 1)

On the demand side, retail sales turned to negative growth due to the strengthening “zero Covid” policy in October amid surging confirmed cases, while real estate fixed-asset investment (FAI) further dipped.

In particular, retail sales dipped from previous 2.5% y/y in September to -0.5% y/y, significantly lower than the market consensus at 1% y/y. By component, restaurant sales dipped significantly from -1.7% y/y in September to -8.1% y/y, given that “zero Covid” restrictive social distancing measures in pandemic affected areas persist. Other sectors of retail sales also dropped, including wines and smoke (-0.7% y/y), clothing (-7.5% y/y) domestic appliance (-14.1%) and cosmetic (-3.7% y/y) etc., amid a lower income expectation and higher surveyed unemployment rate, particularly in 16-24 age group’s unemployment rate staying above 20%. In sum, we maintain our view that the Chinese government’s persistence of “zero tolerance” strategy on Covid-19 pandemic with limited easing at the current stage will continue to constrain China’s consumption recovery in the rest of the year. (see our recent Economic Watch: China | Will the country abandon the “zero tolerance” strategy on Covid19?) (Figure 4)

On the other hand, fixed-asset investment (FAI) marginally moderated from 5.9% ytd y/y to 5.8% ytd y/y in October, lower than the market consensus of 5.9% ytd y/y, while its month-on-month growth also edged down to 0.12% m/m from 0.48% m/m in the previous month. By components, manufacturing FAI marginally declined to 9.7% ytd y/y from 10.1% ytd y/y previously, which surpassed the infrastructure FAI at 8.7% ytd y/y (prior: 8.6% ytd y/y) and real estate FAI at -8.8% (prior: -7.5% ytd y/y) to lead the investment growth recovery. It also indicates that infrastructure FAI achieved significant improvement due to the expansionary fiscal measures particularly the use-up of local government bond issuance quota in 1H 2022 (see our recent Economic Watch: China | Will infrastructure investment become a key growth stabilizer in 2022?). However, real estate crash remains to be the largest headwind to drag China’s economy and at the same time to threaten regional financial stability due to the mortgage boycotts and small banks’ bankruptcy.

There are quite a number of reasons to explain real estate investment maintaining in the negative territory for more than half a year. Chinese authorities cracked down on the housing market in 2021, taking use of the precious time-window to press ahead “common prosperity” and regulatory reforms. In addition, lower income expectation and high unemployment rate particularly in the age 16-24 group (20%) significantly deteriorate house purchase demand. Although the authorities eased housing policy from both demand and supply side recently, as the principle of “housing is to live not to speculate” remains, a soft-landing will take some time. As long as the housing price increase expectation (which lasted for the past 20 years) is broken, it is difficult to rebuild market sentiments, no matter how low the interest rate is. That means, the real estate sector needs more time to achieve a soft-landing going forward. (See our recent China Economic Watch: China | Real estate sector needs a soft-landing) (Figure 2 and 3) However, we anticipate the recently promulgated “16-point plan” by PBoC and CBIRC to support housing sector soft-landing will largely alter the market sentiments on real estate going forward.

In sum, worse-than-expected October economic indicators again suggest a bumpy recovery path of the Chinese economy amid the “zero Covid” policy and real estate crash. However, we anticipate the recently promulgated “16-point plan” to support the housing market and the easing of “zero Covid” restrictions could help to alter market sentiments and rebuild the confidence. Going forward, it remains challenging that the authorities have to strike a balance between the continuation albeit gradual easing of “zero Covid” policy and a decent growth figure and at the same time to secure a housing sector soft-landing.

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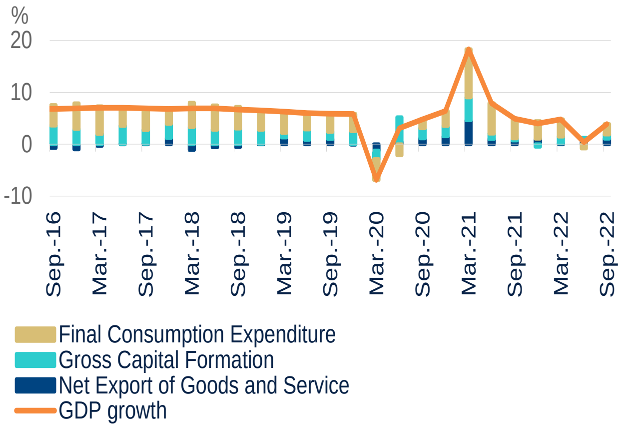
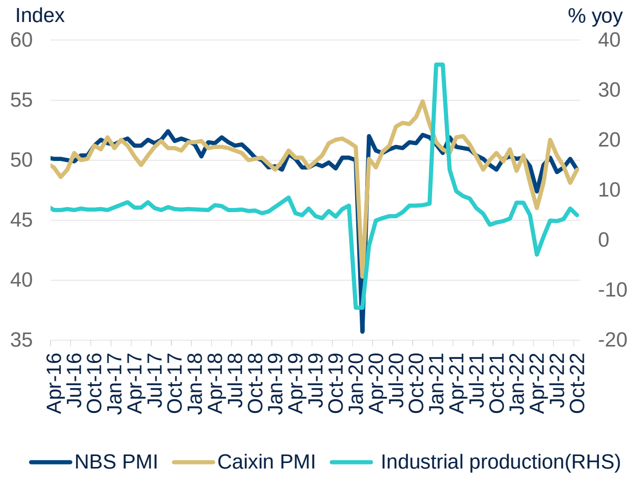
Figure 1. **WE MAINTAIN OUR 2022 GDP FORECAST AT 4.5% DUE TO THE RECENT POLICY STIMULUS**



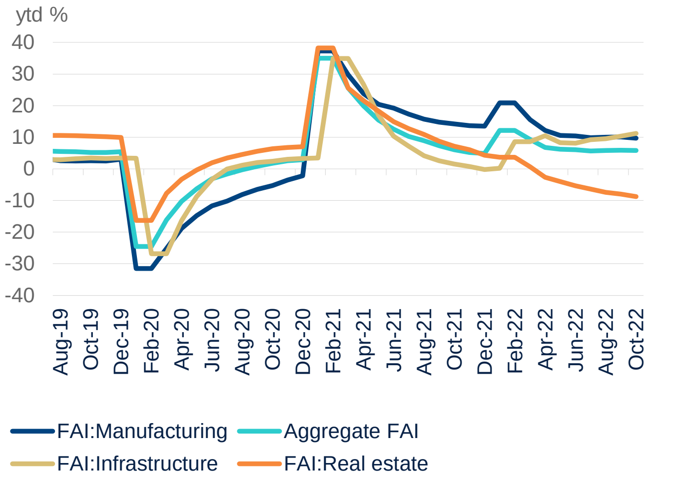
Source: CEIC and BBVA Research

Figure 2. **NBS AND CAIXIN PMI DIVERGED IN OCT., IP DECELEATED TO 5% FROM 6.3%**



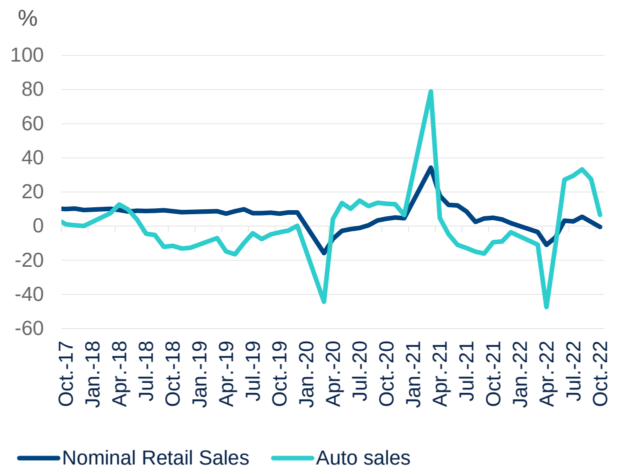
Source: CEIC and BBVA Research

Figure 3 INFRASTRUCTURE FAI PICKED UP TO 8.7% AMID EXPANSIONARY FISCAL MEASURES; HOUSING FAI DIPPED TO -8.8% YTD Y/Y



Source: CEIC and BBVA Research

Figure 4 RETAIL SALES TURNED TO NEGATIVE AT -0.5% Y/Y DUE TO RECENTLY SURGING COVID CASES



Source: CEIC and BBVA Research

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