17 July 2023

Global Markets Research

Research Alert

China: 2Q GDP disappointed with a 6.3% y/y growth

Economic growth decelerated sharply on a q/q basis

External demand remained weak; domestic demand remained fragile

PBoC maintained 1Y MLF rate at 2.65%; monetary policies to stay supportive

Summary

China's 2Q GDP growth came below expectations to expand by 6.3% y/y in 1Q (2Q: +4.5% y/y). This marks the second quarter where growth has accelerated, but this is partially skewed by the low base effect due to the COVID-19 lockdown in Shanghai during spring 2022. On a q/q basis, growth was noticeable slower, decelerating to +0.8% q/q (1Q: +2.2% q/q), while YTD growth of 5.5% for 1H suggests that the government's target of 5.0% for the whole of 2023 is within reach at this juncture.

Mixed details signalled uneven recovery

National Bureau of Statistics, in explaining the disappointing 2Q GDP, said that China is facing a complex geopolitical and economic international environment and added that the domestic economic recovery and development foundations is still not solid yet.

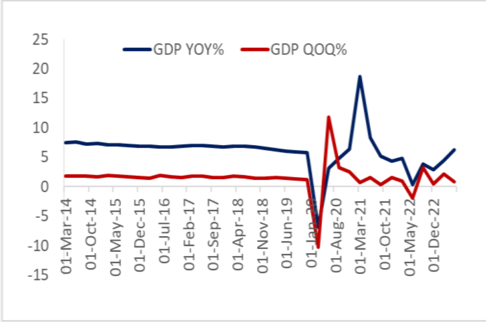
Recent exports data suggests further double-digit contractions in external demand, and this has weighed down on IPI's number released this morning. No doubt, IPI surprised on the upside at 4.4% y/y (May: +3.5% y/y), partially supported by a positive turnaround in the mining sector, and quicker growth in manufacturing output (+4.8% vs +4.1% y/y). By industry, output was supported by crude-oil processing, coal and non-energy vehicles, which more than offset the contractions in electronics and electrical products.

In terms of domestic demand, retail sales softened more than expected to 3.1% y/y in June (May: +12.7% y/y), largely supported by reopening factor as reflected in double digit growth in restaurant/catering. Sales of consumer goods, on the other hand, decelerated sharply to 1.7% y/y (May: +10.5% y/y), pointing to signs of softening consumer spending. This is despite steady jobless rate of 5.2%. Fixed asset investment, meanwhile, expanded better than forecast by 3.8% y/y YTD. Within fixed asset investment, investment into real estate fell 7.9% y/y, but was cushioned by steady increase in manufacturing investment (+6.0% y/y).

Monetary policy to stay accommodative with more measures expected to be rolled out for property, exports and EVs

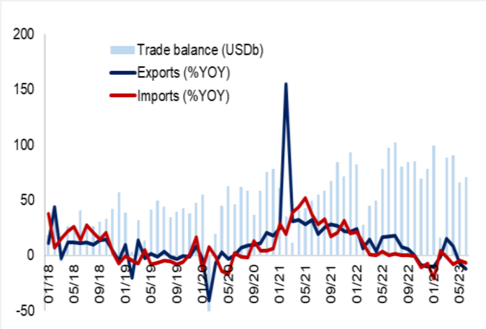
As per expectations, the People's Bank of China also kept its 1Y medium-term lending facility rate steady at 2.65% after shaving 10bps in the month of June. The pause could be attributable to the much stronger than expected credit expansion recorded in June. There is no change in our view that the monetary policy will stay accommodative, but we believe that any cuts in 2023 will be largely capped between 20-35bps (PBoC cut rates by 20bps in 2022 and 35bps for the period 4Q19-2020). Instead, we expect PBoC to maintain its targeted sector approach, be it in the form of extension of property support measures, which may include lower reserve requirement ratio (RRR), easier property controls and funding support for local developers, as well as tax breaks for exports and electric car purchases. Fiscal policy is expected to stay relatively supportive to fund infrastructure investment, but this could be capped on the back of high government debt concerns.

Figure 1: GDP growth slowed q/q



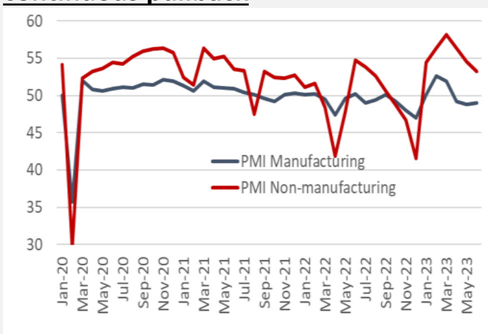
Source: Bloomberg

Figure 2: Weaker external demand will continue to dampen growth outlook



Source: Bloomberg

Figure 3: Manufacturing remained contractionary while services saw continuous pullback



Source: Bloomberg

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