



Global Macro Research - Insight

21 May 2024

5:42 minute read

#China

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#Data indicators

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China: Policymakers step in to help the housing market

A surprise contraction in April's credit flow hurried along the start of the much-anticipated ultra-long government debt issuance, and the PBOC announced measures to support the property sector. New tariffs on exports to the US may have also been a factor, even if the expansion of the 'small yard, high fence' is modest.

Key Takeaways

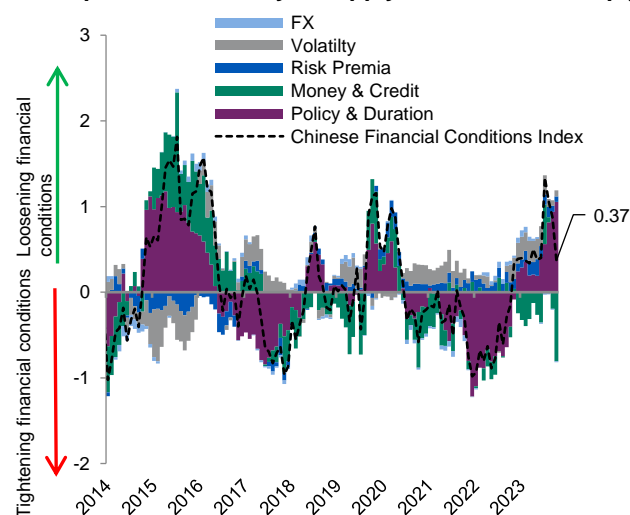
- China's worst credit print since 2005 helped to fire the starter pistol on the RMB 1 trillion ultra-long government debt issuance. This should help support credit and financial conditions going forward.
- The property sector remains a key headwind, with price falls accelerating on the month. Cuts to house purchase downpayments and a loosening of minimum mortgage rates are welcome, as is the news that local governments will buy excess inventory and turn it into affordable housing.
- That said, there is some risk that households continue to sit on the sidelines, waiting for prices to stop falling, while the poor health of some local governments' finances could lead to constraints on purchases in some cities.
- Despite the property drag, activity remains reasonable on net. Our China Activity Index (CAI) suggests Q2 started fairly strong, helped by an industrial rebound.
- New US tariffs on imports from China may have helped motivate additional easing, but they are small enough that China is unlikely to retaliate. Indeed, the EU investigation into the country's trade practices, and a second trade war under Trump are larger risks.
- Until either of these (or other) risks are crystalised, the pattern of incremental policy easing is set to remain the modus operandi.
- Indeed, a third month of above zero inflation – combined with the ongoing aversion to FX weakness – suggests the appetite for a more substantial easing remains slim.

A tougher backdrop across credit, housing and geopolitics motivated policymakers to ease in May

Chinese officials finally announced some measures to ease fiscal policy and support the property market. These include a reduction to downpayments for purchasing houses as well as cuts to minimum mortgage rates. The decision was likely driven by the unexpected contraction of credit, an acceleration in house price falls, and new tariffs on US imports of Chinese goods.

While the Chinese economy remains in reasonable shape, Total Social Financing (TSF) surprised by contracting RMB 0.2 trillion in April – well below the increase of RMB 0.9 trillion expected by consensus, and the worst print since October 2005.

Figure 1: Financial conditions became less supportive in April as money supply receded sharply



Source: Bloomberg, Haver, abrdrn (May 2024)



However, on a seasonally adjusted basis, flows were less catastrophic, remaining positive – ‘only’ their worst level since April 2016.

The drivers of the credit contraction were the negative net flows from government bond issuance and shadow lending, which together fell by RMB 0.5 trillion. A small net positive flow from corporate bond issuance failed to prove much of an offset.

This likely contributed to the significant fall in money supply through the period, dragging our China Financial Conditions Index (CFCI) sharply lower in April (see Figure 1).

M1 money supply surged before Lunar New Year, but this spike has since reversed, dragging the index 0.50 points lower, to 0.37. It is possible that this volatility in money will cause a rebound in the CFCI next month.

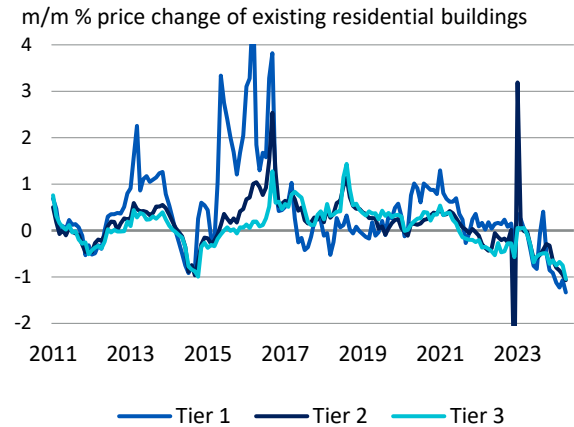
The sharp decline in money and credit may have spurred policymakers to commence issuance of the long-awaited ultra-long government bond programme, which began with little warning in mid-May. The RMB 1 trillion bond issuance will reportedly be comprised of 300 billion for the 20-year tenor, 600 billion for 30-year bonds and 100 billion for 50-year ones. At a minimum, it should give a boost to the government debt component of TSF over the next seven months, while also providing indirect support to the money supply.

New housing policies are welcome, but may not be enough to be a floor under prices and activity

Alongside the start of ultra-long debt issuance, the People’s Bank of China (PBOC) announced that minimum downpayments for house purchases will be lowered by 5 percentage points – to 15% for first time buyers and to 25% for second home purchases – while provinces will also be free to determine minimum mortgage rates, rather than these being centrally decided.

And according to state-run Xinhua News, local governments are being directed to acquire empty properties for affordable housing, which should help ease pressure on developer financing while also reducing the supply-demand imbalance.

Figure 2: Property activity might be closer to a trough, but prices are now falling faster than in 2014



Source: Haver, abrdrn (May 2024)

Policymakers are at least reacting, but it remains unclear how much further the price and activity adjustment will go.

Local governments’ finances remain strained as a result of zero-Covid expenditures and reduced land sales, implying that they may be constrained in their ability to scoop up developers’ excess inventory.

There is also some risk that households continue to sit on the sidelines, waiting for a turnaround in house prices, which have actually been falling at a faster pace (see Figure 2).

The beleaguered property sector has almost certainly held back consumers by reducing the value of China’s most important store of wealth.

Retail sales and services have at least made a steady, albeit unspectacular, rise since 2023’s summer lull, and this continues to support our China Activity Index (see Figure 3).

Figure 3: Our China Activity Index ticked higher in April, helped by an industrial rebound



Source: Haver, abrdrn (May 2024)

But there is little sign of excess savings accrued over the pandemic being spent that could really fire up the engine of consumption.



Indeed, retail sales fell short of consensus expectations in April, and we estimate that both these and the services output index fell by around 0.8% month over month.

In contrast, industry outperformed: headline industrial production (IP) was strong in April, rising 6.7% year over year – up from 4.5% year over year and 1.2ppts more than consensus. And the National Bureau of Statistics estimate that IP expanded by 12.3% month over month annualised, though this partly reflects a recovery from the sequential contraction they now pencil in for March.

The ‘small yard, high fence’ just got a bit bigger

The desire to loosen policy also got a helping hand from the Biden administration.

US President Joe Biden announced tariff increases ranging from 25% to 100% on a number of Chinese goods, primarily aimed at electric vehicles, batteries and semiconductors.

The administration said the tariffs were designed to help increase US competitiveness in green technology manufacturing, protect sectors vital for national security and guard against unfair Chinese trade practices.

Around \$18bn of Chinese goods exports across 11 categories will be affected by the increases, but the vast majority of this is accounted for by just lithium-ion batteries and battery parts, which both see tariffs rise from 7.5% to 25%. Other goods, the imports of which are almost negligible, will often face higher tariff rates – an attempt to guard against future surges in the imports of these Chinese products, especially electric vehicles (EVs).

Figure 4: Biden announced US tariffs on ~\$18bn worth of Chinese imports, primarily hitting batteries

Product	New tariff	Starting
Steel and aluminium	25%	2024
Electric vehicles	100%	2024
Lithium-ion batteries (EVs)	25%	2024
Solar cells	50%	2024
Ship-to-shore cranes	25%	2024
Medical products	25%-50%	2024-2026
Semiconductors	50%	2025
Batteries (non-EVs)	25%	2026
Natural graphite	25%	2026
Permanent magnets	25%	2026

Source: abrdn, [The Whitehouse](#) (May 2024)

From an economic point of view, the outcome of the ongoing EU investigation into Chinese trade practises, in particular around EVs, is likely to be much more significant for China.

As such, we expect that China will not retaliate against these latest US actions, in part because they are relatively modest, but also because it would risk pouring fuel on Trump’s rhetorical fire.

Policy set to remain incremental... for now.

Financial conditions may have become less supportive and the spectre of another trade war may still loom large, but the decent start to activity in Q2, combined with the latest policy measures, implies that the policy floodgates will remain shut unless a larger shock emerges.

Indeed, while fears of ‘Japanification’ will still take time to recede, a third month in a row of above-zero CPI inflation suggests the nominal environment is getting slowly better.

This is likely to add to the PBOC’s aversion to “excessive moves” in the currency, even as the trade-weighted basket continues to rise and the export deflator turns around.

Overall, we think the economy is still likely to ‘meet’ (+/- 0.2ppt) the ~5% growth target for 2024. The bigger question that remains is: what will happen in 2025 and beyond?

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AA-270524-178633-54

