

China growth to be around half Xi's target in 2022

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3 August 2022



The International Monetary Fund has issued a revised forecast of just 3.3% GDP growth for China this year, in a further signal that Beijing's ambitious 5.5% target is looking increasingly unattainable. The IMF's latest forecast in its [World Economic Outlook Update](#), revised down from 4.4%, is now below the current Reuters consensus expectations of economists, which stand at 4.0%. It came as little surprise to Fathom Consulting, however, which predicted Chinese growth of just 2.8% for 2022 in our Global Outlook forecast on 8 June - a figure we see no reason to revise. So what is the backdrop to the downbeat growth forecast and what will be the factors in play going forwards?

China's economy was hit hard by the COVID lockdowns. Fathom's China Momentum Indicator (CMI), an independent measure of Chinese economic activity that does not rely on official Chinese GDP data, showed that the economy contracted by 2.8% during Q2 when the most severe lockdowns occurred, and by 0.5% over the twelve months to April-June – the latter was the joint second weakest reading since the series began in 2003. Activity has gradually recovered from its trough in April, however, as key cities have reopened and the economy has benefited from stimulus. Fathom's CMI improved from -1.7% on a twelve-month basis in April to -1.1% in May and +1.1% in June. All the purchasing managers' surveys had moved into expansionary territory by June, although the NBS Manufacturing PMI contracted once more in July, highlighting the somewhat tentative nature of the recovery and the headwinds it faces. The surveyed unemployment rate has fallen back in recent months, but it remains quite elevated, particularly in the largest cities.

Fathom China Momentum Indicator 3.0 and GDP

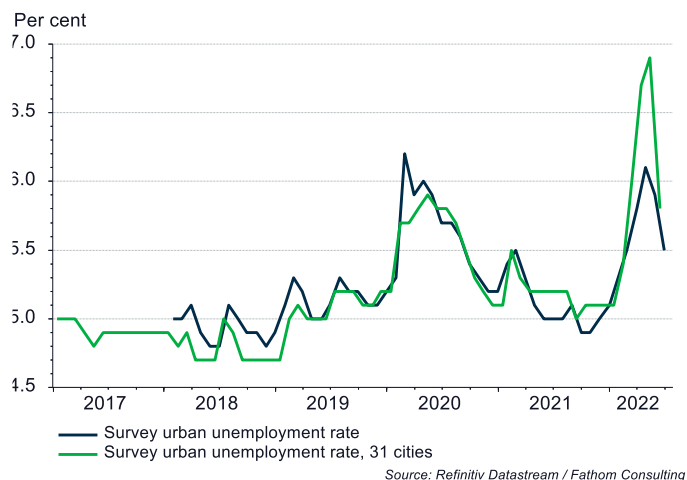
Four-quarter percentage changes



Source: Refinitiv Datastream / Fathom Consulting

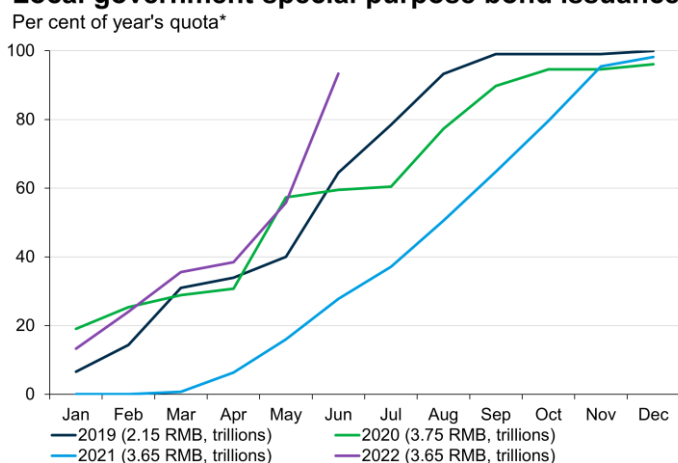


China unemployment rate



Beijing stepped up the policy stimulus to support the recovery in activity. A key focus has been fiscal easing, particularly tax and fee cuts for businesses, and increased infrastructure spending. By the end of June, local governments had issued over 90% of their annual quota of special bonds that are largely used to fund infrastructure spending (at comparable points in 2020 and 2021, around 60% and 25% respectively of similar-sized quotas had been issued); and spending of the proceeds should further boost activity over coming months. Media reports suggest that the authorities may even allow local governments to bring forward some of their special bond quota for 2023, which could further boost activity later in the year. There were also signs of policy easing coming through in the total social financing figures, with June's increase of 5.2 trillion RMB being easily the strongest on record for that month. Within that, there was a significant rise in bank lending, with some key lending categories showing signs of life: there were large increases in borrowing for long-term corporate loans and to a lesser extent mortgage loans.

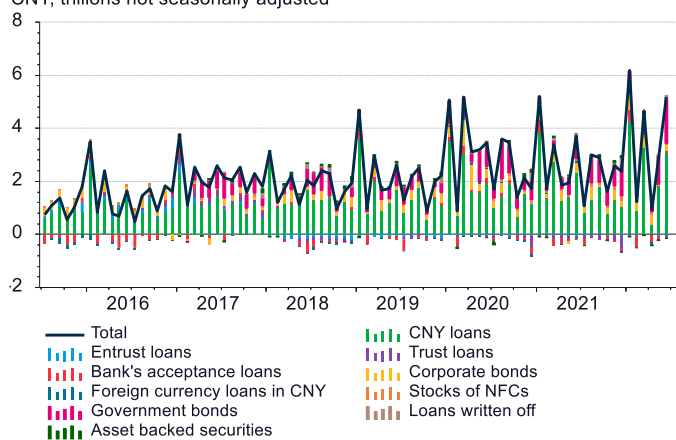
Local government special purpose bond issuance





China net new total social financing

CNY, trillions not seasonally adjusted



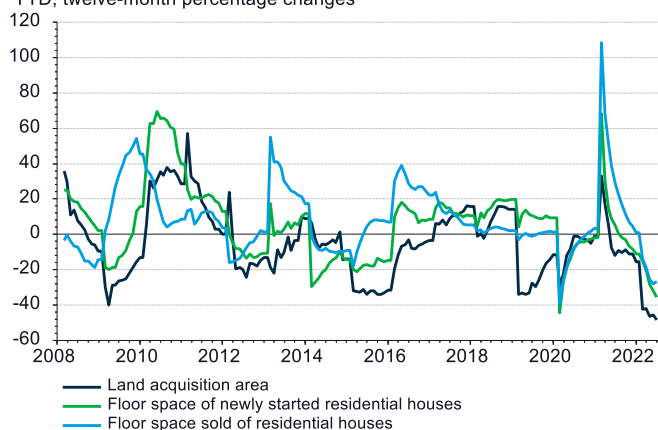
Source: Refinitiv Datastream / Fathom Consulting

Nevertheless, the economy continues to face several major headwinds through the remainder of the year: not least, from Beijing's insistence on sticking to its 'dynamic zero-COVID' policy. Despite some easing in enforcement measures, the policy is likely to continue to result in strong, unpredictable restrictions in activity as the more transmissible Omicron variant fuels recurrent outbreaks. President Xi is highly unlikely to move away from his signature policy before the National Party Congress, probably in October or November. In addition to the negative impact on growth from further lockdowns, the policy will continue to weigh on the confidence of private businesses and households.

Another factor weighing heavily on economic performance is the state of the Chinese housing market, which remains firmly in the doldrums. The volume of housing starts and sales was around a third and a quarter lower respectively in the first half of 2022 compared with twelve months earlier. House prices at a national level have fallen modestly since last autumn, with the prices of new and second-hand homes falling by 0.5% and 2.1% on a twelve-month basis in June. The proportion of respondents expecting prices to rise over the coming quarter is close to its lowest on record, according to the Urban Depositors Survey. The highly-publicised mortgage boycott by individuals waiting to receive their unfinished properties risks further weakening sentiment towards the sector. Sharply falling revenues from land sales will also reduce the ability of local government to support growth (revenues from land sales are equal to around 80% of official local government revenues).

China real estate

YTD, twelve-month percentage changes

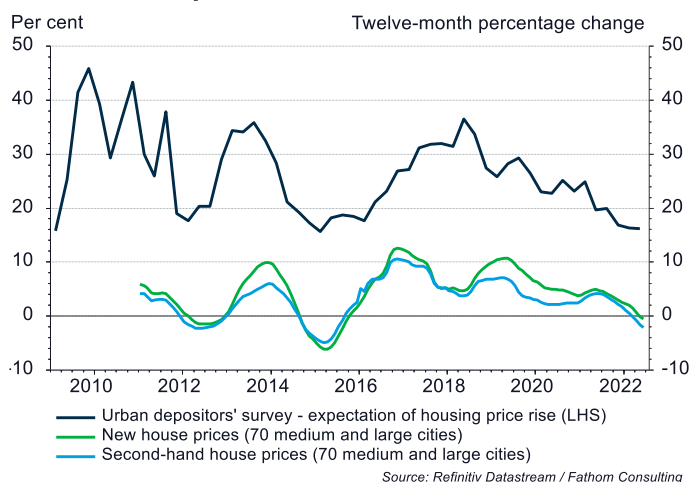


Source: Refinitiv Datastream / Fathom Consulting



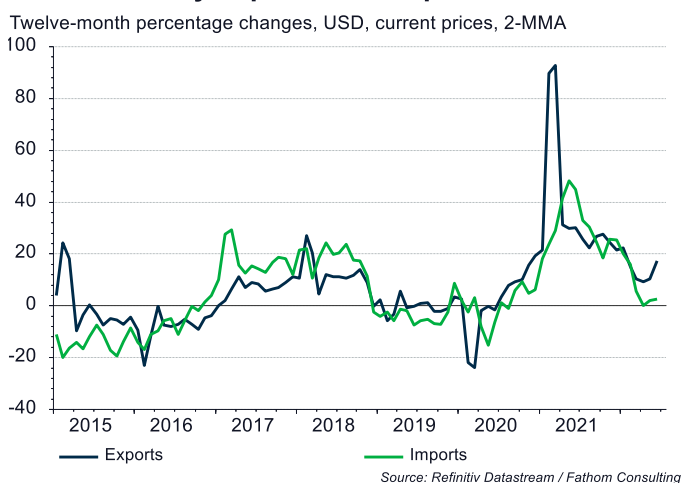


China house prices



Strong exports have been a bright spot for the Chinese economy; exports are currently growing at a much faster rate than imports, resulting in a record monthly trade surplus in June. That said, the external backdrop is likely to become much less favourable in the coming months, with the prospect of recession in key markets. Last week's GDP data suggest the US is already in technical recession, with a relatively modest contraction of economic activity in Q1 and Q2. The euro area is potentially facing a more severe economic downturn.

China monthly exports and imports



All in all, despite the gradual recovery in the Chinese economy in recent months, growth is likely to come in significantly below the government's target this year. The leadership appeared to acknowledge the inevitable in a statement from the Politburo after its meeting on 28 July, dropping the previous reference to meeting the economic targets in 2022, and suggesting merely that the best possible outcome for the economy should be striven for. Even before the major lockdowns in April and May, Fathom had thought the growth target was a stretch amid problems in the real estate sector, the zero-Covid strategy and Russia's invasion of Ukraine. This cannot be what President Xi was expecting or hoping for in such an important political year, although he still seems likely to secure an unprecedented third term as leader.



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