British Embassy
Beijing

China Economic Focus – December 2012

Overview

- Macroeconomic data released this month was generally positive, with robust growth shown in retail sales, industrial production and fixed asset investment. This all suggests that the economy continues to pick up speed and that Q4 growth will be faster than Q3's growth of 7.4 percent. Data for Q4 growth will be released in mid January.

- That said, export data was surprisingly weak, with Chinese exports to the EU, the US and Japan all contracting. This indicates continued weakness in external demand, which remains the main short-term risk to Chinese economy.

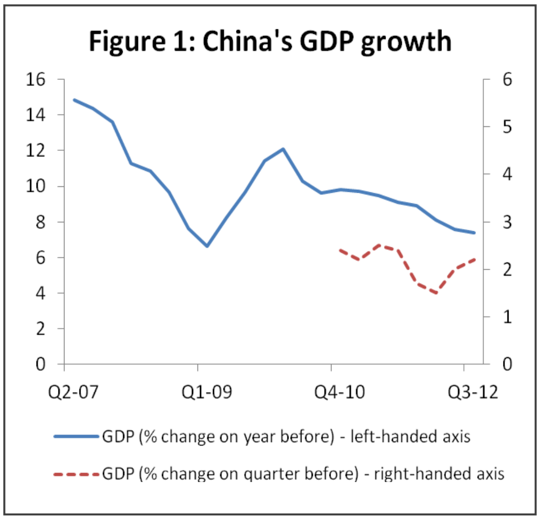
- Inflation rose a little in November but remains well below the authorities' 4 percent target, and it is forecast to remain low for the coming months. This means that there is space for further monetary easing, though with most economic indicators performing well the authorities are unlikely to take action soon.

- Overall growth in 2012 growth will fall between 7.5-8 percent. This would be the slowest rate of economic growth since 1999, but above the authorities' target of 7.5 percent. Most forecasters currently expect growth of a little over 8 percent in 2013.

- The central economic work conference (CEWC) will take place shortly. At this annual event the leadership set out the broad parameters of the next year's macroeconomic policy. It is expected that next year's monetary policy stance will remain 'prudent' and the fiscal policy 'proactive' and we will be looking for further indications about the new leadership's commitments to economic reform.

China's economy is recovering mildly

1. Growth in the Chinese economy is picking up, registering 2.2 percent quarterly growth in 2012 Q3 compared with compared with 2.0 percent in 2012 Q2 (and 1.5 percent in 2012 Q1). **See figure 1.** We expect this trend to continue when the data for 2012 Q4 is released in mid January.

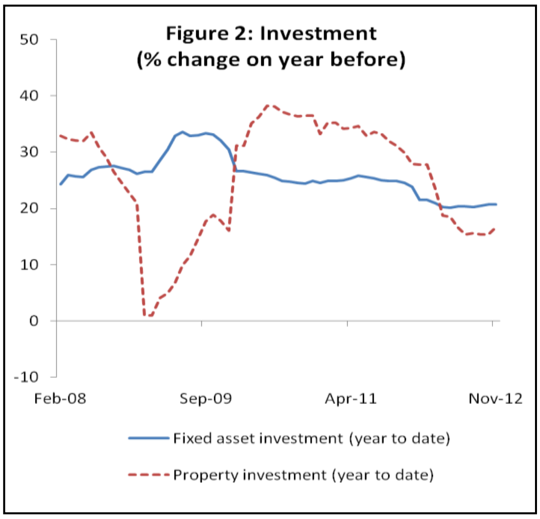


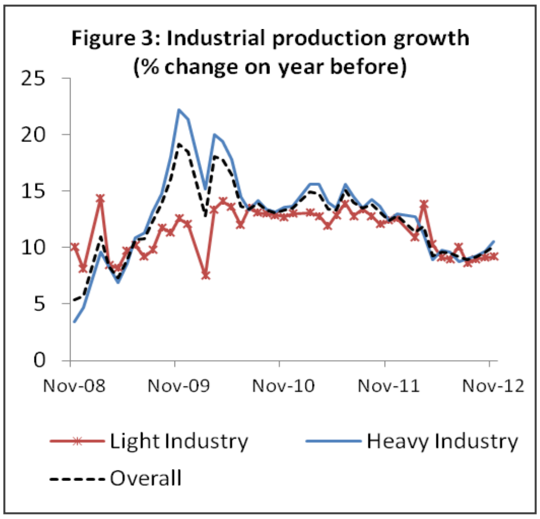
2. China Academy of Social Sciences, a leading think tank to the central government, predicts that the growth for 2013 will be 8.5 percent, supported by high levels of infrastructure investment. The IMF and World Bank currently forecast growth of 8.2 percent and 8.1 percent for 2013.

3. The Central Economic Work Conference (CEWC) will take place shortly. At this annual event the leadership set out the broad parameters of the next year's macroeconomic policy. It is expected that next year's monetary policy stance will remain 'prudent' and the fiscal policy 'proactive' and we will be looking for further indications about the new leadership's commitments to economic reform.

Key economic indicators broadly positive for November

4. Headline fixed asset investment (FAI) growth remained unchanged at 20.7 percent in the first 11 months (on a year before). Property investment, which accounts for around 20 percent of FAI, grew by 16.7 percent in November (year to date), picking up from 15.4 percent in October, thanks to the continuous rebound of property sales and more new home starts being built (**see Figure 2**). Infrastructure investment growth slowed to 12.4 percent, down from 25 percent growth in October.



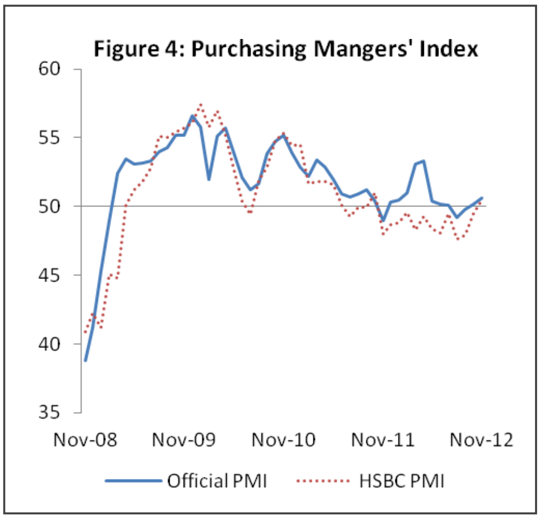


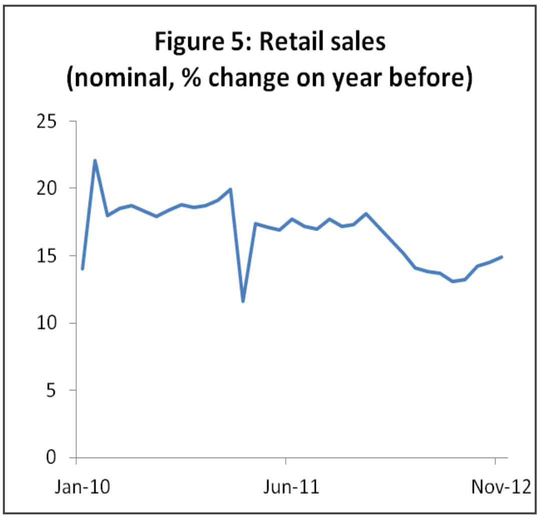
5. Growth of industrial production (IP) beat market expectations and accelerated to an 8-month

high at 10.1 percent in November, compared with 9.6 percent in October. This was the 4th consecutive month of acceleration (**see Figure 3**). Growth of electricity, steel, and crude oil production reached the highest levels in the year. Cement production saw a slight deceleration.

6. The improvement of IP was supported by the latest official purchasing managers' index (PMI). The PMI picked up to 50.6 in November, from 50.2 in October (a reading above 50 suggesting manufacturing sector expansion). PMI for big manufactory companies were much stronger than that for small and medium ones (official PMI for SMEs were still at the contraction zone). The separate HSBC PMI reached a 13-month high of 50.5 in November (**see Figure 4**).

7. Consistent with improved IP and PMI figures, corporate profitability growth was picked up – an increase of 20.5 percent in October (the latest figure), compared with 7.8 percent in September and contraction from May to August.



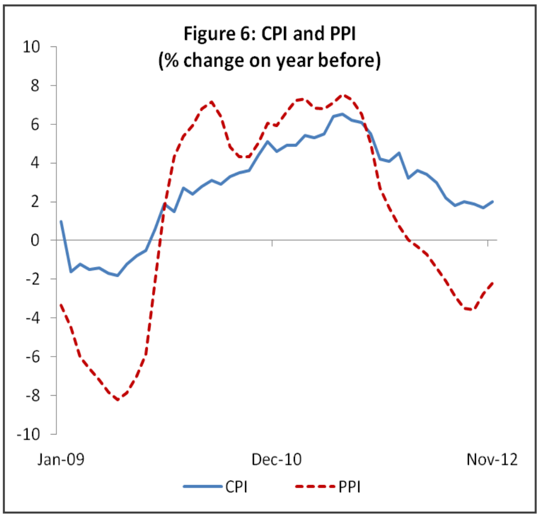


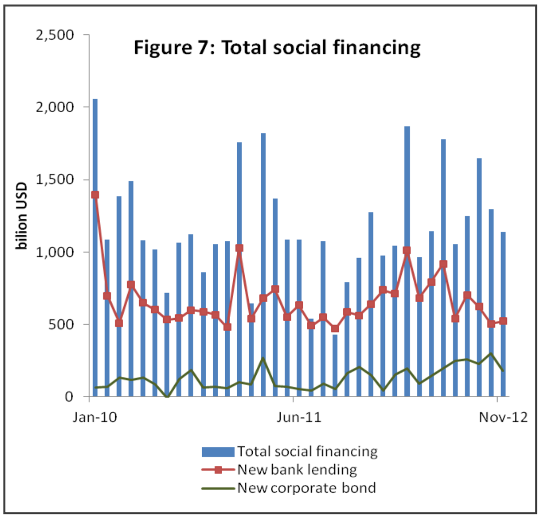
8. Retail sales grew by 14.9 percent in November, the highest level since March 2012 (**see Figure 5**). This suggests resilient consumer sentiment. Sales of garment, cosmetics, jewellery, home appliances, and medicine accelerated.

Inflation remains comfortable

9. Headline consumer prices index (CPI) increased by 2 percent in November, slightly higher than October's 1.7 percent (**see Figure 6**). It was mainly driven by food prices (fresh vegetable price in particular). Non-food prices inflation slowed marginally to 1.6 percent in November, down 0.1 percentage points from October. With food prices are expected to continue rising, most analysts believe that inflation will rebound in 2013, but remain under the official target of 4 percent.

10. Producer price index (PPI), a measure of upstream inflation pressures, continued to fall in November by 2.2 percent. The contraction has narrowed in the past 3 months.





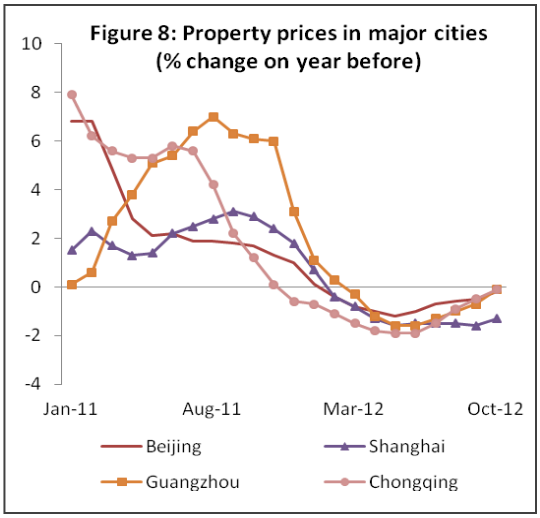
11. Total social financing, a measure of all forms of new credit, totalled RMB 1.14 trillion (£114 billion) in November, down from RMB 1.29 trillion (£129 billion) in the previous month. November's new banking lending was RMB 523 billion (£52.3 billion), lower than market expectations but higher than October's figure. Corporate bond issuance slowed, due to the tightening of credit standards by regulators (**see Figure 7**).

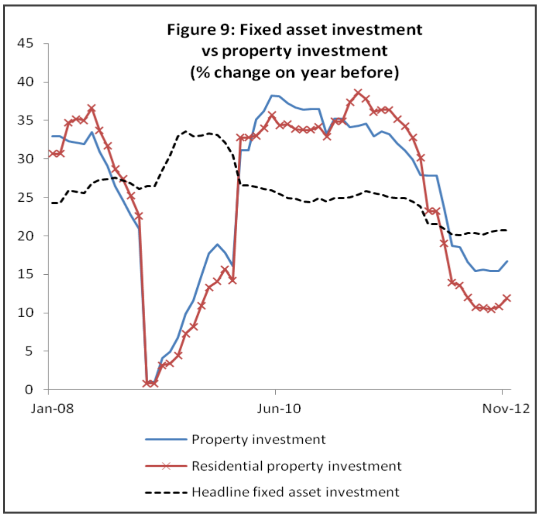
12. Money supply (M2) grew by 13.9 percent in November, nearly flat with October's figure. It is in line with the PBoC's (central bank) annual target of 14 percent.

Improvements in residential property

13. Official figures show that 35 of 70 cities surveyed saw property prices increase (in month-on-month terms) in October, compared with 31 in September (**see Figure 8**).

14. Investment in residential property increased by 11.9 percent in November (year to date), slightly higher than the past 4 months (**see Figure 9**). Home sales growth accelerated to 9.1 percent in November (year to date), registering the highest level in the year (although still much lower than November 2011).





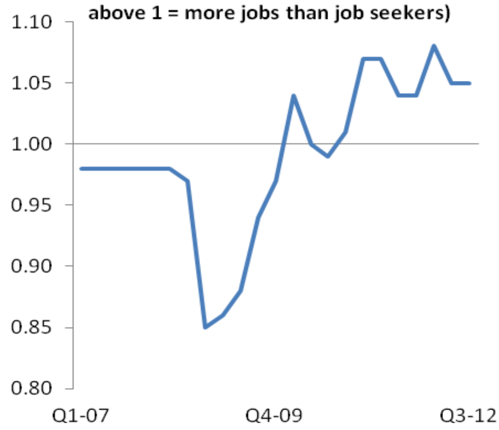
Labour market remains tight so far

15. This month a survey published by a Chinese university suggested that the urban unemployment ratio reached 8.05 percent earlier this year, up from an estimated 7.5 percent last year and much higher than the official unemployment rate of 4.1 percent.

16. The official unemployment data is not considered reliable, as it only measures a small percentage of the workforce. However, it is likely that the labour market remains more tight than is suggested by the survey, as many of those registered in the survey as unemployed had been former SOE employees, laid-off during the period of SOE restructuring in the 1990s, and as such are probably not actively looking for work.

17. The most robust data on the state of the labour market is the ratio of jobs to job-seekers, which remains above 1 (**see Figure 10**).

Figure 10: Urban labour market (below 1 = more job seekers than jobs; above 1 = more jobs than job seekers)



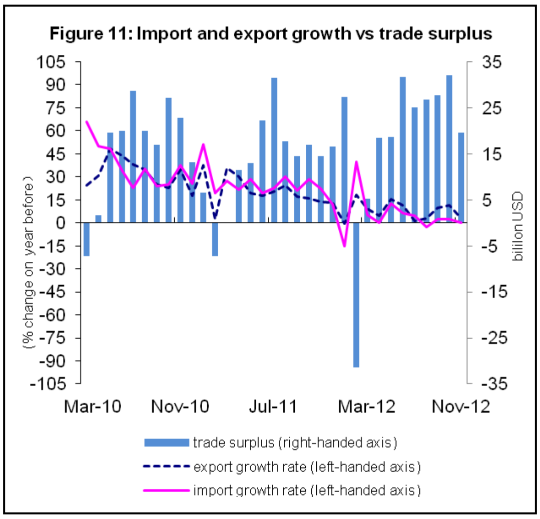
Weak external demand

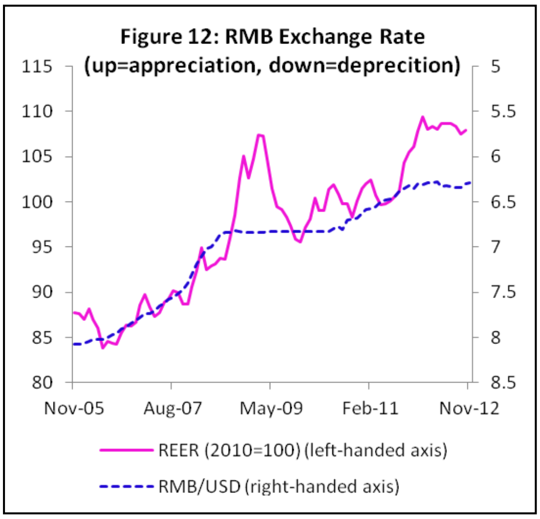
18. Both exports and imports were worse than expected in November. Exports growth slowed to 2.9 percent in November (on a year earlier), compared with 11.6 percent in October and 9.9 percent in September. November's slower rate of growth is likely to be more representative of underlying conditions as the figures for both September and October figures will have been distorted by Christmas orders.

19. China's exports to the major economies (the EU, the US and Japan) all contracted in November, with shipments to the US declining for the first time in 21 months. Growth of China's exports to ASEAN countries slowed significantly. November's imports experienced zero growth from October.

20. On 20 November, a spokesman of the Ministry of Commerce emphasised it would be "very difficult" to achieve an annual trade growth of 10 percent. The Ministry plans to discuss further measures to stabilise exports and imports in their forthcoming yearly National Commerce Conference.

21. The balance of exports and imports registered a trade surplus of $19.6 billion in November, down from October's $32 billion (**see figure 11**).





RMB remains flat

22. The RMB exchange rate remained roughly unchanged in the past month. The currency has appreciated (against the US dollar) by 8.6 percent since it was de-pegged in June 2010. The RMB's real effective exchange rate (REER – trade-weighted and inflation adjusted) has appreciated by 5.9 percent since June 2010 (**see Figure 12**).

23. RMB deposits in Hong Kong, an offshore market for the Chinese currency, totalled RMB 554.8 billion (£55.5 billion) in October, up 1.7 percent from September. Total RMB deposits have fallen by 13 percent since the peak in November 2011. RMB cross-border trade settlement totalled RMB 195.4 billion (£19.5 billion) in October, compared with RMB 239.3 billion (£23.9 billion) in September.

We encourage readers to get in contact for further information on any points covered in this note, or to suggest ways of improving the note for next month. Our details are:

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