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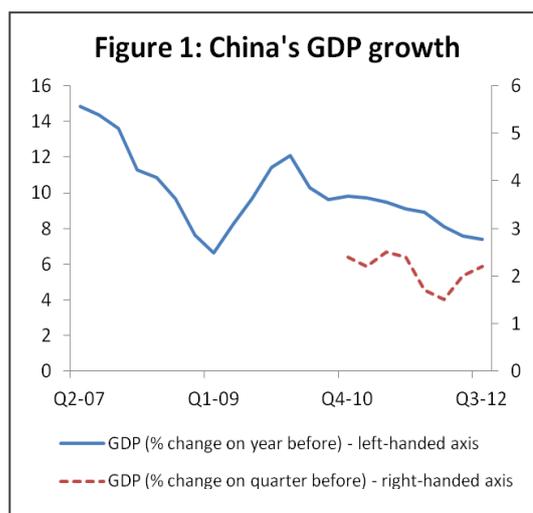
China Economic Focus – November 2012

Overview

- Data published over the past month shows that key economic indicators have stabilised, having experienced around 6 months' of falling growth earlier this year. Growth in investment, industrial production, retail sales and exports all rose slightly but a sharp economic rebound is unlikely. Overall growth this year is expected to be between 7.5 – 8 percent.
- Inflation fell slightly this month to 1.7 percent, its lowest level since February 2010. Inflation is likely to rise gradually in the coming months, but it not expected to reach the government's 4 percent target anytime soon. Further monetary easing is unlikely, given the recent pick-up in activity.
- This month saw the start of the 18th Party Congress. In his opening speech, President Hu Jintao introduced the target of doubling both GDP and incomes between 2010-2020, which implies average GDP growth of around 7 percent between 2012 and 2020. Hu also emphasised the need for further structural economic reform, in particular around the role of the government in the economy.
- In subsequent sessions of the Party Congress:
 - PBOC (the central bank) Governor Zhou Xiaoquan stated that the current monetary policy would be maintained until the end of the year;
 - CSRC (the securities' regulator) Chairman Guo Shuqing indicated that quotas for RQFII (the mechanism through which funds are channelled from Hong Kong to the Mainland) would be significantly expanded in the near future;
 - the Minister for Commerce, Chen Deming, said that the difficult global trading environment would make it very difficult to reach the 2012 target for increasing overall trade by 10 percent; and
 - the Minister for Housing, Jiang Xinwei, said that the government would continue to 'work hard' at controlling property prices.

Growth has stopped declining and 7-8 percent annual growth expected in coming years

1. Headline year-on-year growth was 7.4 percent last quarter, the lowest since the height of the global financial crisis. However, quarter-on-quarter growth, a better way of looking at recent economic performance, rose to 2.2 percent, compared with 2.0 percent in 2012 Q2 (and 1.5 percent in 2012 Q1). See figure 1.



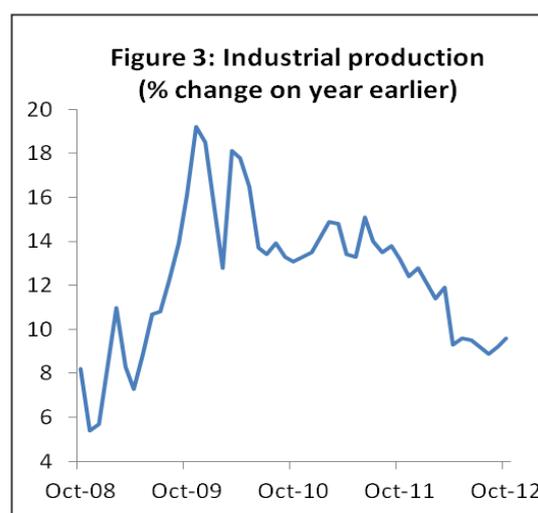
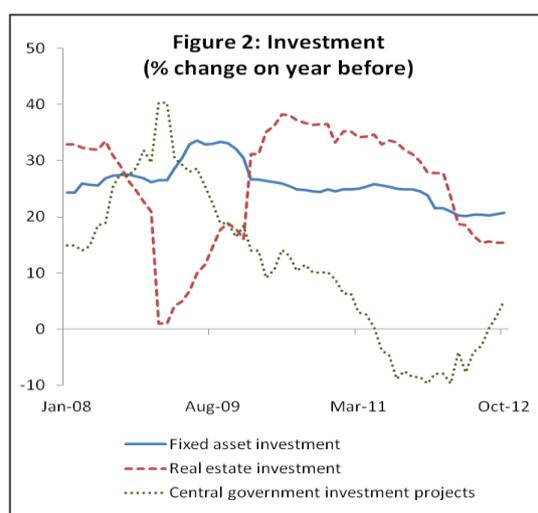
2. President Hu Jintao announced at the start of the 18th Party Congress a target to double 2010 real GDP by 2020. This implies annual growth of around 7 percent per year between 2012-2020. President Hu also discussed the need for

continued economic reform, “the underlying issue we face is how to strike a balance between the role of the government and that of the market, and we should follow more closely the rules of the market and better play the role of the government.”

Key economic indicators have stabilised

3. Headline fixed asset investment (FAI) growth remains stable at between 20-21 percent in 2012. Property investment, which accounts for around 20 percent of FAI, grew by 15.4 percent, around half the rate of growth seen a year ago. Government investment accelerated between September to October (See Figure 2).

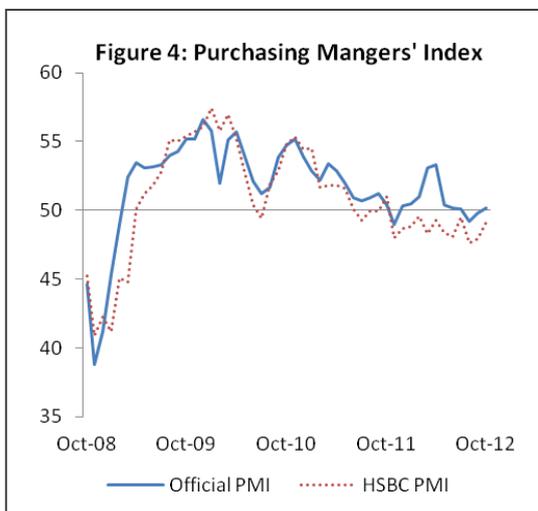
4. Industrial production (IP) grew by 9.6 percent in October (on a year before), slightly higher than over the past 4 months (See Figure 3). The production of electricity and steel picked-up from September to October, while the production of cement, oil, and cars grew at a slower rate.



5. The official purchasing managers’ index (PMI) was 50.2 in October, having fallen below 50 in each of the last two months. The HSBC PMI, which focuses on smaller firms, rose to 49.1 (See

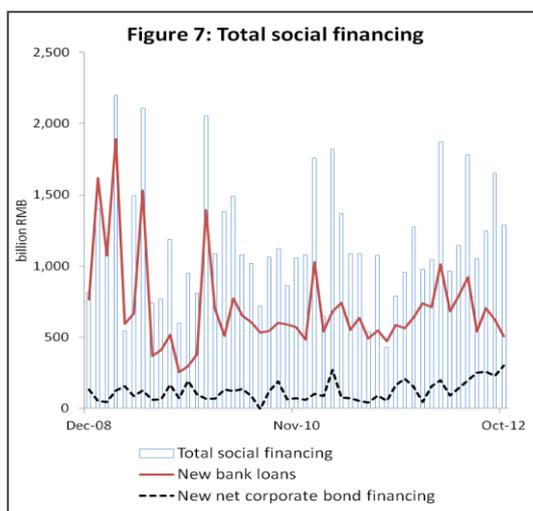
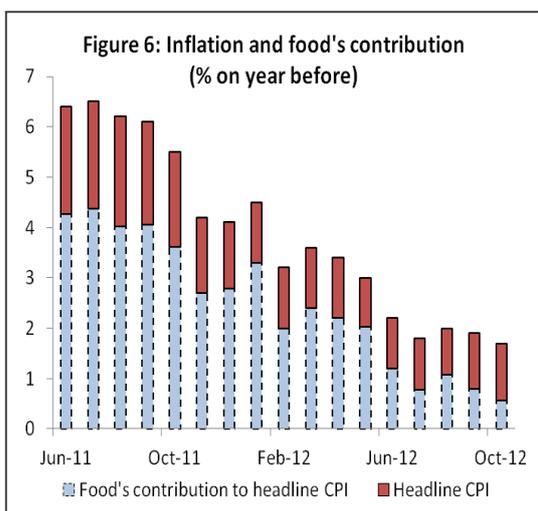
Figure 4). Consistent with better IP and PMI figures, corporate profitability rose by 7.8 percent in September (the latest data), having contracted in each of the past four months.

- Retail sales grew by 14.5 percent in October and they are now at the highest level for 7 months (See Figure 5). Sales of food and beverage, cosmetics, daily necessities, and automobile accelerated.



Inflation falls but it is expected to rise gradually in the coming months

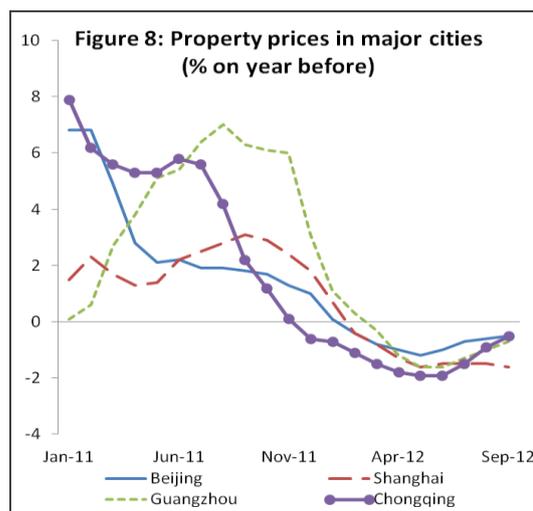
- Headline CPI eased to 1.7 percent in October, with food price inflation slowing to a 3-year low of 1.8 percent (see figure 6). Most analysts expect CPI would remain a low level at 2 – 3 percent for the next six months. Despite low inflation, further easing before the end of the year is unlikely. On 8 November PBoC Governor Zhou Xiaochuan said that the government would continue the current monetary policy till next year.
- Total social financing, a measure of all forms of new credit, reached RMB 1.29 trillion (£129 billion) in September, down from the previous month. Bank lending was significantly lower than expectations and corporate bond issuance continues to rise quickly (see figure 7).
- Money supply (M2) grew by 14.1 percent in October, compared with 14.8 percent in September (both on a year earlier).



Property sector restrictions remain in place but prices are basically stable

10. Official figures show that 31 of 70 cities surveyed saw property prices increase (in month-on-month terms) in September, compared with 36 in August and 50 in July (see figure 8).

11. On 12 November, Jiang Xinwei, Minister of Housing and Urban-Rural Development, said that the government would continue to ‘work hard’ at controlling property prices. He also announced that 6 million social houses would be launched in 2013 (compared with 7 million units of social housing launched so far in 2012).



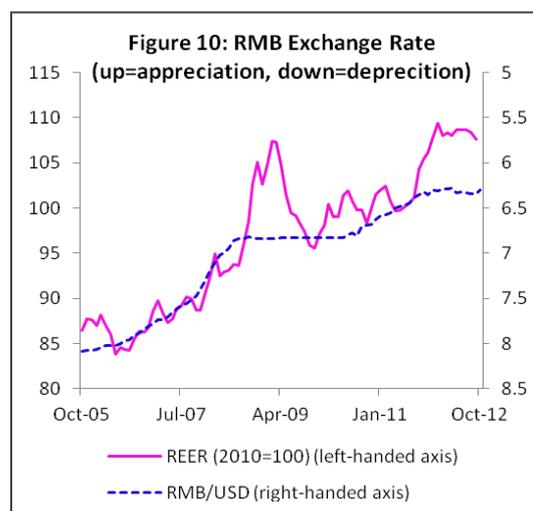
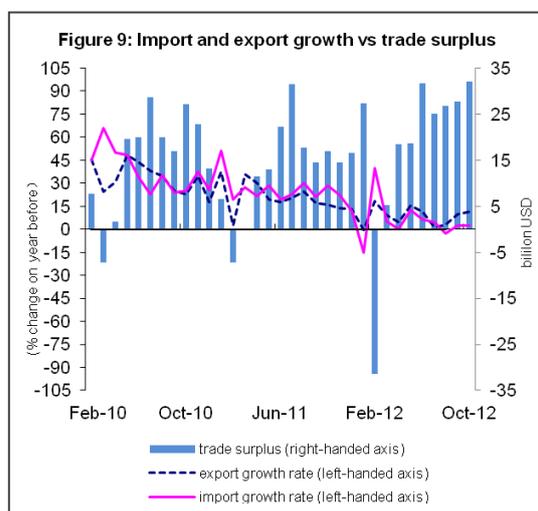
Exports and the trade surplus rise

12. Exports grew by 11.6 percent in October (on a year earlier). The increase, which was above market expectations, was mainly attributable to strong demand from emerging economies and resilient demand from the US. Exports to the EU over the first 10 months of 2012 have fallen 8.1 percent compared with the previous year.

13. Growth of imports in October remained at the same level (2.4 percent) as in September, below market expectations. Slow import growth is attributed to companies destocking and, as a result, stronger imports are expected in the coming months. Imports from Japan fell by 10.2 percent in October, the third consecutive month of contraction.

14. On 9 November Chen Deming, Minister of Commerce, said that the global trade outlook was unfavourable due to ongoing problems in the world economy, and that this would make it very difficult for China to achieve its 2012 target of increasing total trade by 10 percent.

15. The balance of exports and imports registered a trade surplus of \$32 billion in October, the highest trade surplus recorded since January 2009 (see figure 9).



RMB remains essentially at equilibrium

16. The RMB appreciated by around 0.5 percent in the past month, and has appreciated by roughly 8.5 percent against the dollar since the currency was de-pegged in June 2010. The RMB's real-effective exchange rate (REER – trade-weighted and inflation adjusted) has appreciated by 5.6 percent since June 2010 (**see figure 10**).
17. RMB deposits in Hong Kong, an offshore market for the Chinese currency, decreased to RMB 545.7 billion (£54.6 billion) in September, down 1.2 percent from August. Total RMB deposits have fallen by 13 percent since the peak in November 2011. RMB cross-border trade settlement totalled RMB 239.3 billion (£23.9 billion) in September, down 5.9 percent on a monthly basis.
18. Guo Shuqing, Chairman of the CSRC (the securities regulator) announced on 10 November that the authorities are likely to expand RQFII (RMB-denominated qualified foreign institutional investor) quota by RMB 200 billion (£20 billion) to RMB 270 billion (£27 billion). The expansion is expected to expand the channels through which offshore RMB can flow back onshore. The RQFII Scheme is only applied to Hong Kong.

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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