Foreign & Commonwealth Office

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FCO COUNTRY UPDATES FOR BUSINESS

China Economic Focus: November 2013

British Embassy Beijing

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Overview

- China's economy grew by 7.8 percent (year-on-year) in the third quarter of 2013, up from 7.5 percent in the previous quarter. The latest monthly data show that the mild economic rebound in the Chinese economy continues.

- Forward looking indicators (such as the purchasing managers index) are also robust, suggesting momentum will be maintained until at least the end of the year, with most analysts forecasting overall growth of around 7.6 percent for 2013, slightly higher than the official target of 7.5 percent.

- Growth in 2014 is expected to be slightly stronger, though it is likely that the official target will be lowered to 7 percent, as the government seeks to emphasise the quality rather than the pace of growth.

- The major economic event in November was the Communist Party's Third Plenum, which exceeded expectations in terms of the reformist ambition demonstrated by the new leadership. The resulting 'Decisions Document', published on 15 November, touches upon all elements of economic reform, including references to:
  - the 'decisive role' that markets will play in future resource allocation, including capital, energy and water. Many argue that such factor price liberalisation will of itself go a long way in correcting China's macroeconomic imbalances;
  - significant reform to fiscal relations between the central government and the provinces, including through increasing transparency; moving some spending responsibilities (back) to the centre; and continuing to roll-out important tax reforms. These measures would address widespread concerns about the sustainability of local government finances; and
  - accelerating reform of the household registration system (the 'hukou') in small and medium cities, thereby widening access to social services. This will be expensive for the government, but would have profound (positive) implications for the economy and society.

- The 'Decisions Document' does not contain a detailed timetable for implementation. However, it does emphasise the need to make substantial progress in all areas by 2020. And the formation of a new 'Central Leading Group on Deepening Reform', to be Chaired by President Xi, bodes well for cutting through bureaucratic impediments to change.

- We will be looking to December's Central Economic Work Conference for an indication about the short-term reform priorities.

- Further examples of our recent reporting can be found at: http://www.ukti.gov.uk/export/countries/asiapacific/fareast/china/fcoupdates.html. Please get in touch if you have any questions or comments.

The 3rd Plenum sends positive singal for China's economy

1. China's economy has stabilised. The economy grew by 7.8 percent in 2013 Q3 (on a year earlier), compared with 7.5 percent in 2013 Q2. Most analysts are now expecting an overall growth of around 7.6 percent in 2013, slightly above the authorities' target of 7.5 percent. **See Figure 1**.

Figure 1: External growth forecasts for 2013

Institute	Forecasts
World Bank	7.5 percent
IMF	7.6 percent
HSBC	7.7 percent
Standard Chartered	7.5 percent
Citibank	7.6 percent
UBS	7.6 percent
Goldman Sachs	7.6 percent
JP Morgan	7.6 percent
CICC	7.6 percent
'Official Target'	7.5 percent

2. The Chinese Communist Party (CCP) held its 3rd Plenum of its 18th Party Congress on 9-12 November. After a vague Communiqué published on 12 November which disappointed the market, a full version of the CCP's Decision on major reform issues reset the confidence 3 days later. The full report is substantive and covers comprehensive and detailed reform themes. The key reforms regarding economic development include:
   - To well manage the relationship between the government and the market, and to ensure market's "decisive" role in resources allocation;
   - To increase the dividends paid by State-owned Enterprises to 30 percent by 2020 (the current level is 5-15 percent);
   - To improve fiscal allocation redistribution, matching responsibilities with budget;
   - To establish a unified market of construction land (land used to build homes on), and to set up intermediaries for rural construction land translations; and
   - To expand financial liberalisation and open-up, to encourage two-way capital flows, to speed up capital account liberalisation and to set up deposit insurance mechanism.

3. This is arguably the biggest reform package of market economic reforms since 1992. It shows senior leaders determination to deepen reforms. Now the key lies with implementation. A new 'Central Leading Group on Deepening Reform' will be set up to design, coordinate the reforms. More detailed measures are expected to follow in the coming Central Economic Work Conference, which usually takes place in the first week of Decembers.

October's data are broadly stable

4. Headline fixed asset investment (FAI) growth has stabilised. FAI increased by 20.1 percent in the first 10 months (on a year earlier), edging down marginally from 20.2 percent in the first 9 months. This was slightly below market expectations of 20.2 percent and a growth of 20.7 percent during the same period in 2012. On monthly basis (seasonally adjusted), FAI growth accelerated to 1.43 percent in October, compared with 1.34 percent in September. Manufacturing FAI grew by 23.5 percent in October, higher than September's 22.1 percent. Infrastructure FAI growth slowed to 16 percent in October, compared with 21.6 percent in September and 29.3 percent in August. **See Figure 2.**

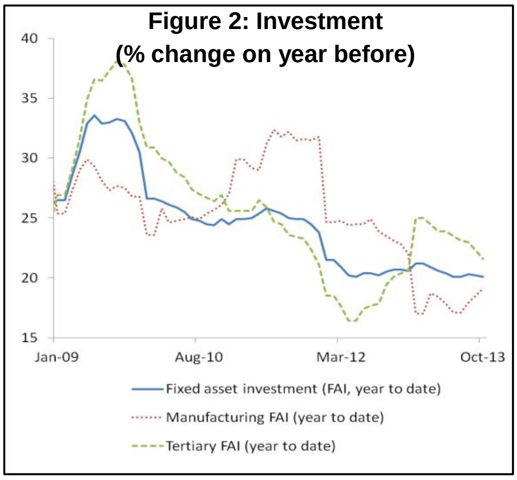


Figure 2: Investment (% change on year before)

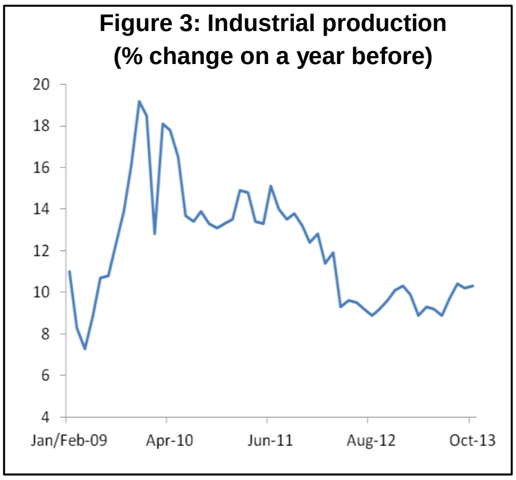


Figure 3: Industrial production (% change on a year before)

5. Industrial production (IP) growth edged up marginally to 10.3 percent in October (on a year earlier), compared with 10.2 percent in September and beating market expectations of 10.1 percent. In month-on-month terms (seasonally adjusted), the growth of IP accelerated to 0.86 percent in October, compared with 0.73 percent in September. Growth of production of electricity, cement and crude oil picked up in October, after an ease in September. Car production continued a quick increase. **See Figure 3.**

6. The purchasing manager's index (PMI), a forward-looking measure of business conditions, remains improving. The official Manufacturing PMI hit an 18-month high of 51.4 in October, up from 51.1 in September – the 13th consecutive month in the expansion zone (above 50). The separate HSBC Manufacturing PMI seen as a better measure of business conditions for small enterprises, accelerated to 50.9 in October, compared with 50.2 in September. Both of the official and HSBC services PMI continued to improve and perform stronger than the manufacturing indices. **See Figure 4 & 5.**

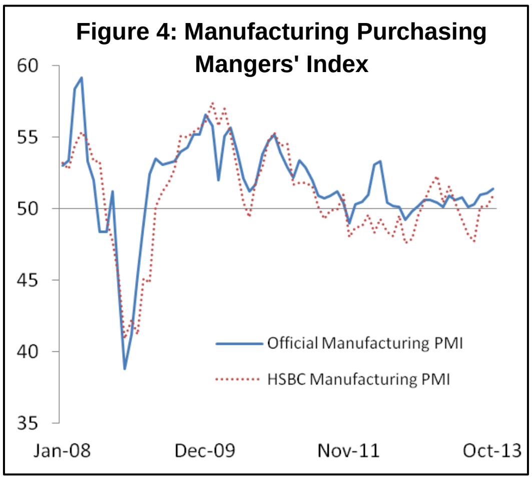


Figure 4: Manufacturing Purchasing Mangers' Index

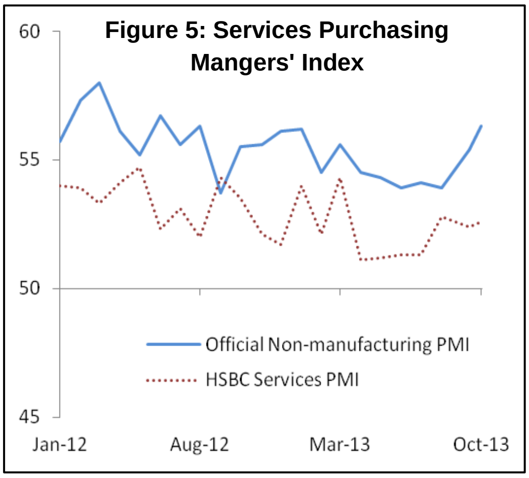
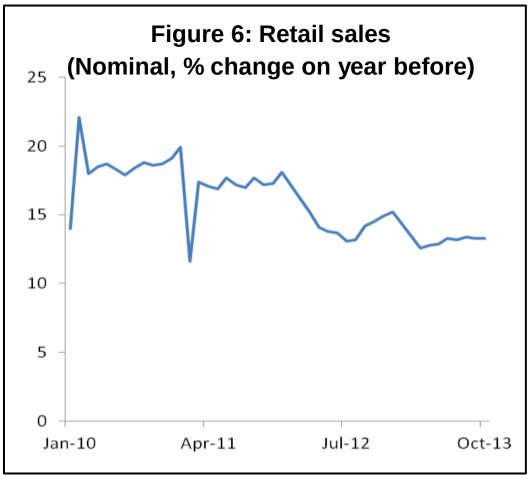
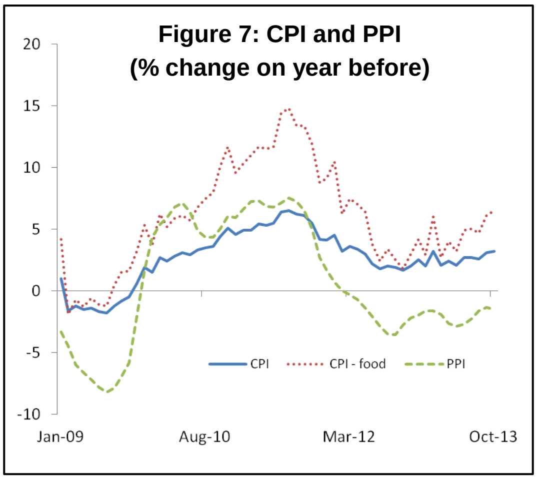


Figure 5: Services Purchasing Mangers' Index

7. Retail sales growth remained unchanged at 13.3 percent in October (on a year earlier), from September. On monthly basis (seasonally adjusted), retail sales increased by 1.19 percent in October, down slightly from September's 1.26 percent. Growth of sales of medicine, telecoms equipment, oil products and automobile improved; whereas that of food and beverage, textile, gold/jewellery and home appliance eased. Sales of catering sector, which is likely influenced by the government's austerity campaign, contracted by 0.6 percent in October, up from -1.3 percent in September. **See Figure 6.**





Inflation picked up, but remains not a concern

8. The consumer prices index (CPI) stood at an 8-month high of 3.2 percent in October (on a year earlier), slightly higher than September's 3.1 percent. Food prices remained as the main contributor – it increased by 6.5 percent in October (compared with 6.1 percent in September), contributing 2.11 percentage points to headline CPI. Vegetable prices, in particular, grew by 31.5 percent in the past month, contributing 0.81 percentage points to headline CPI. Most analysts believe that inflationary pressure remains low and CPI is unlikely to exceed the official target (cap) at 3.5 percent. **See Figure 7.**

9. The contraction of producer prices index (PPI), a measure of upstream inflation pressure, deepened to -1.5 percent in October (on a year earlier), compared with -1.3 percent in September.

Total social financing decelerates due to seasonality

10. Total social financing (TSF), a measure of all forms of new credit, totalled RMB 856.4 billion (£85.6 billion) in October, much lower than September's RMB 1.4 trillion (£140 billion) and reached a 3-month low. All of the sub items of TSF fell over the past month. This was mainly seasonal. **See Figure 8.**

11. New bank lending eased to RMB 506 billion (£50.6 billion) in October, down from RMB 787 billion in September. This was also seasonal, since loan demand usually weakens towards year end. Both of mid to long term loans and short term loans fell from September to October.

12. Money supply (M2) grew by 14.3 percent in October (on a year earlier), up marginally from 14.2 percent in September. In the first 10 months of 2013, M2 kept exceeding the official annual target of 13 percent. The authorities will continue to keep their monetary policies accommodative. In their Q3's report, the PBoC's (Central Bank) Monetary Policy Committee reiterated to implement stable policies, neither loosening nor tightening, with fine-tuning "when appropriate".

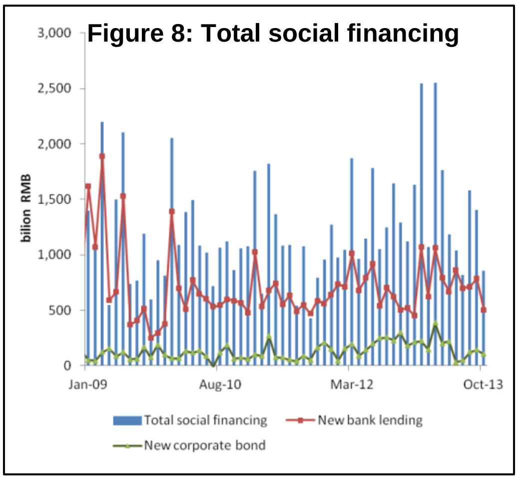


Figure 8: Total social financing

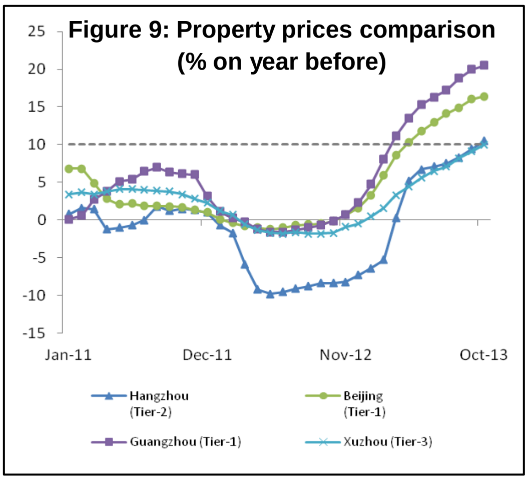


Figure 9: Property prices comparison (% on year before)

Property prices continue to increase

13. Property prices continued quick increases. The official data show that 65 out of 70 cities surveyed saw higher property prices in October (on a month earlier), the same as in September. Property prices growth in all Tier 1 cities (Beijing, Shanghai, Guangzhou and Shenzhen) exceeded 15 percent in October (on a year earlier) – prices in Guangzhou and Shenzhen, in particular, grew by 20.5 and 20.2 percent respectively. **See Figure 9.**

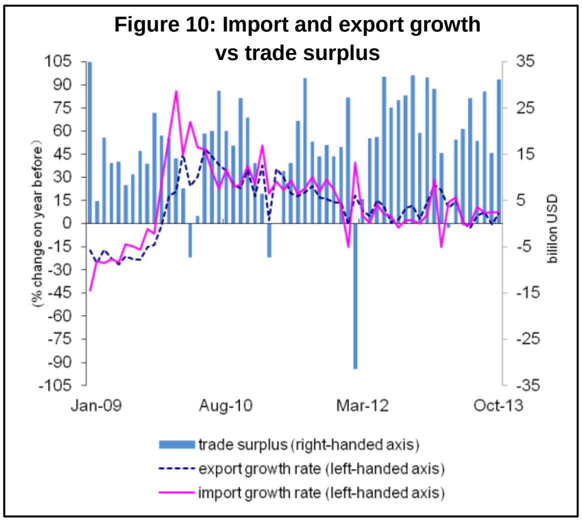
14. Property investment grew by 19.2 percent in the first 10 months (on a year earlier), lower than 19.7 percent in the first 9 months but higher than 15.4 percent in the first 10 months of 2012. Residential property, which accounts for 68.7 percent of property investment, grew by 18.9 percent in the first 10 months, compared with 19.5 percent in the first 9 months.

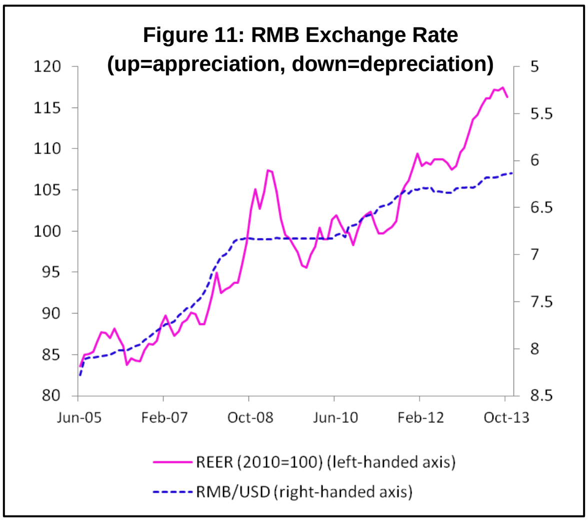
Exports rebound, imports remain resilient

15. China's export growth in October exceeded market expectations. Exports grew by 5.6 percent in October (on a year earlier), up from -1.3 percent in September. Exports to G3 markets (US, EU and Japan) led the rebound. Shipment to the US increased by 8.1 percent in October (4.2 percent in September), that to the EU surged by 12.7 percent (-1 percent in September) and that to Japan grew by 5.6 percent (1.3 percent in September). Exports to Hong Kong contracted in the past 2 months.

16. Imports growth remained resilient. October's imports grew by 7.6 percent in October (on a year earlier), picking up slightly from 7.4 percent in September. Imports of iron ore, steel and copper saw acceleration in volume terms.

17. The balance of exports and imports registered a trade surplus of USD 31.1 billion in October, doubling the amount in September. **See Figure 10.**





RMB:US$ exchange rate stays nearly flat

18. The RMB:US$ exchange rate (as of 21 November) has been nearly flat over the past month, and has appreciated by 2.5 percent since the beginning of 2013, compared with a 0.24 percent appreciation in 2012 as a whole. According to the Bank of International Settlement, the RMB's real effective exchange rate (REER) depreciated marginally by 1 percent from September to October. The RMB's REER has appreciated by 5.5 percent in the first 10 months, compared with 2.1 percent in 2012 as a whole. **See Figure 11.**

19. On 19 November, PBoC Governor Zhou Xiaochuan announced that China's Central Bank would "basically stop guidance on exchange rates on daily basis", and would allow the RMB to float freely (in April 2012, the PBoC widened RMB's daily trading band from 0.5 percent to 1 percent, against dollar). But Zhou did not give a clear timetable.

20. RMB deposits in Hong Kong, an offshore market for the Chinese currency, totalled RMB 730 billion (£73 billion) in September (latest figure), compared with RMB 709.5 billion (£70.9 billion) in August. RMB cross-border trade settlement reached RMB 331.7 billion (£33.2 billion) in September, increasing 9 percent compared with August.

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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