China Economic Monitor

Issue: 2023 Q3

August 2023

kpmg.com/en

Key takeaways

- China’s GDP grew 5.5% year-over-year (yoy) in 2023 H1, posting a steady economic rebound. In Q2, the economy rose by 6.3%, up from 4.5% in Q1, largely thanks to a low base. On a quarter-on-quarter basis, China’s GDP plummeted to 0.8% in Q2 from 2.2% in Q1, showing a slowdown in the domestic economic recovery.
- With Covid-19 restrictions lifted, retail sales saw a solid recovery in H1 2023, and the contribution of consumption to economic growth continues to expand. Consumer sentiment improved modestly and the share of households indicating higher savings dropped slightly (but remains high).
- Manufacturing and infrastructure investments held up relatively well, growing 6.0% and 10.7% in H1 2023, respectively. However, momentum has weakened somewhat recently. Looking ahead, investment in high-end manufacturing and the upgrading of equipment will likely continue to see robust growth.
- The property market recovery has slowed down since April, the growth rate of key indicators such as new home sales and property investment still declined. With the support of financing policies, the liquidity pressure of real estate companies has improved, but the land transaction market is still in the doldrums.
- China's exports fell in H1 2023 due to the weak external demand, but still outperformed other major Asian export-oriented economies. . Despite slowing exports to advanced economies, China’s trade with emerging markets continued to rise. Meanwhile, the structure of China’s exports is also changing with a rising share of advanced manufacturing products. New energy vehicles (NEVs), solar panels, and lithium battery have become bright spots for China’s exports.
- Overall, China’s economy is recovering since the removal of pandemic-related restrictions, with demand gradually improving. However, the recovery is still at an early stage and varies by sector. Improving household and corporate confidence is still the key to unlock faster economic growth. The government has issued guidelines on boosting confidence in the private sector, and a new round of property easing measures to revive growth. KPMG has lowered China’s GDP growth forecast to 5.5% in 2023 and expect the economy to grow 5.2% in 2024.

China's Q2 economic recovery momentum has slowed down due to the subdued property activities and tepid investment in private sector

Growth rate of major economic indicators, %

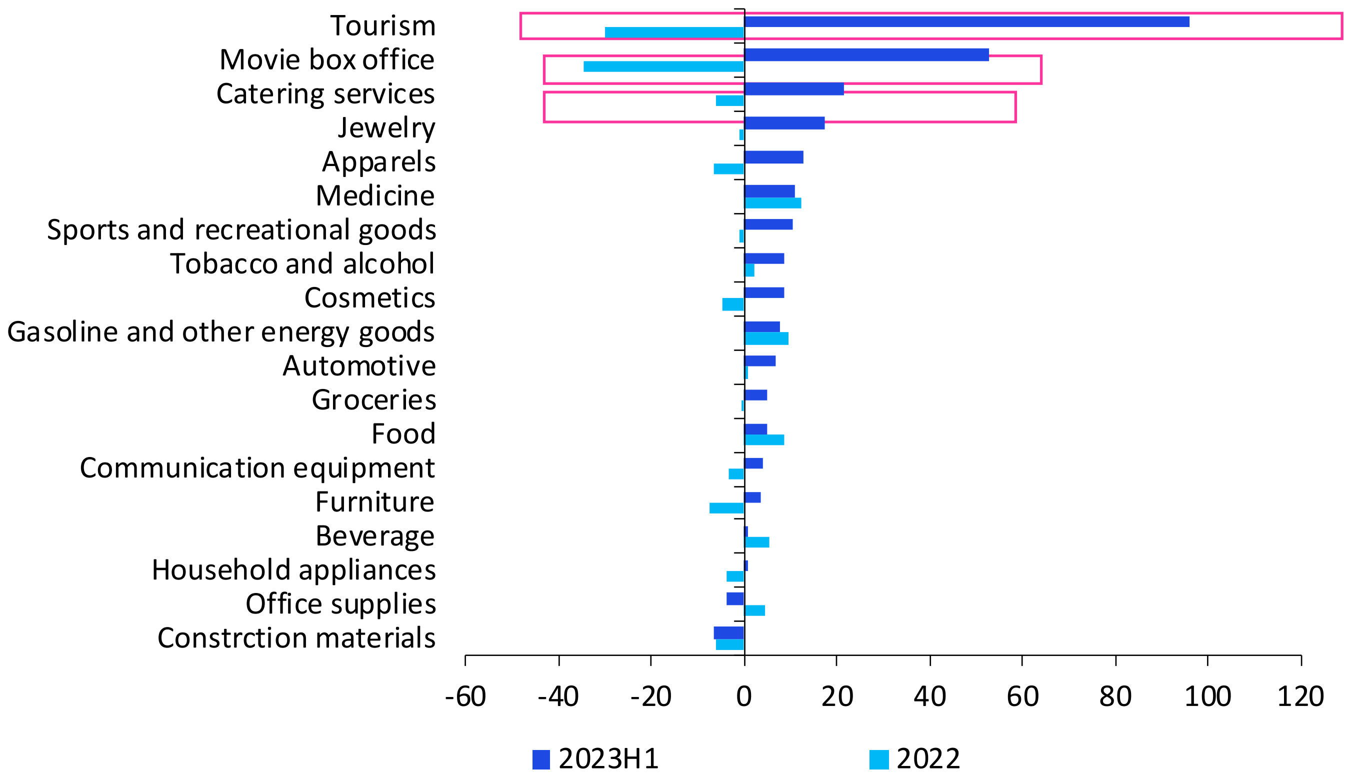
	2017-19 Average	2022Q2	2022Q3	2022Q4	2023Q1	2023Q2
GDP	6.6%	0.4%	3.9%	2.9%	4.5%	6.3%
Industrial Production	6.2%	0.6%	4.8%	2.8%	3.0%	4.5%
Retail Sales	9.0%	-4.6%	3.5%	-2.5%	5.8%	10.7%
Fixed Asset Investment	6.2%	4.2%	5.5%	2.9%	5.1%	2.8%
Exports	6.1%	12.9%	10.1%	-6.6%	0.5%	-4.7%
Imports	9.8%	1.7%	0.9%	-6.5%	-7.1%	-6.4%
Income per capita	6.5%	0.4%	3.6%	2.0%	3.8%	8.4%
Fiscal revenue	5.8%	-28.0%	2.2%	31.2%	0.5%	31.7%
Fiscal expenditure	8.2%	3.7%	6.7%	4.8%	6.8%	1.0%

Source: Wind, KPMG analysis
Note: growth of GDP, industrial production, and income per capita are in real terms, and others are in nominal terms.

- China's GDP grew 5.5% year-over-year (yoy) in 2023 H1, and 6.3% in Q2, up from 4.5% in Q1, largely thanks to a low base.
- The contribution of consumption to economic growth continues to expand. Retail sales growth picked up from 5.8% in Q1 to 10.7% in Q2. Exports growth declined by 4.7% in Q2 due to sluggish global economic growth, while exports of new energy products performed better than expected.
- Investments in infrastructure remained resilient with policy support, but property activities remained subdued, and weakened growth prospects in the private sector slowed down its investment. Fixed asset investment growth dropped to 2.8% in Q2 from 5.1% in Q1.

Service consumption is seeing a faster recovery

Growth of retail sales by category, yoy, %

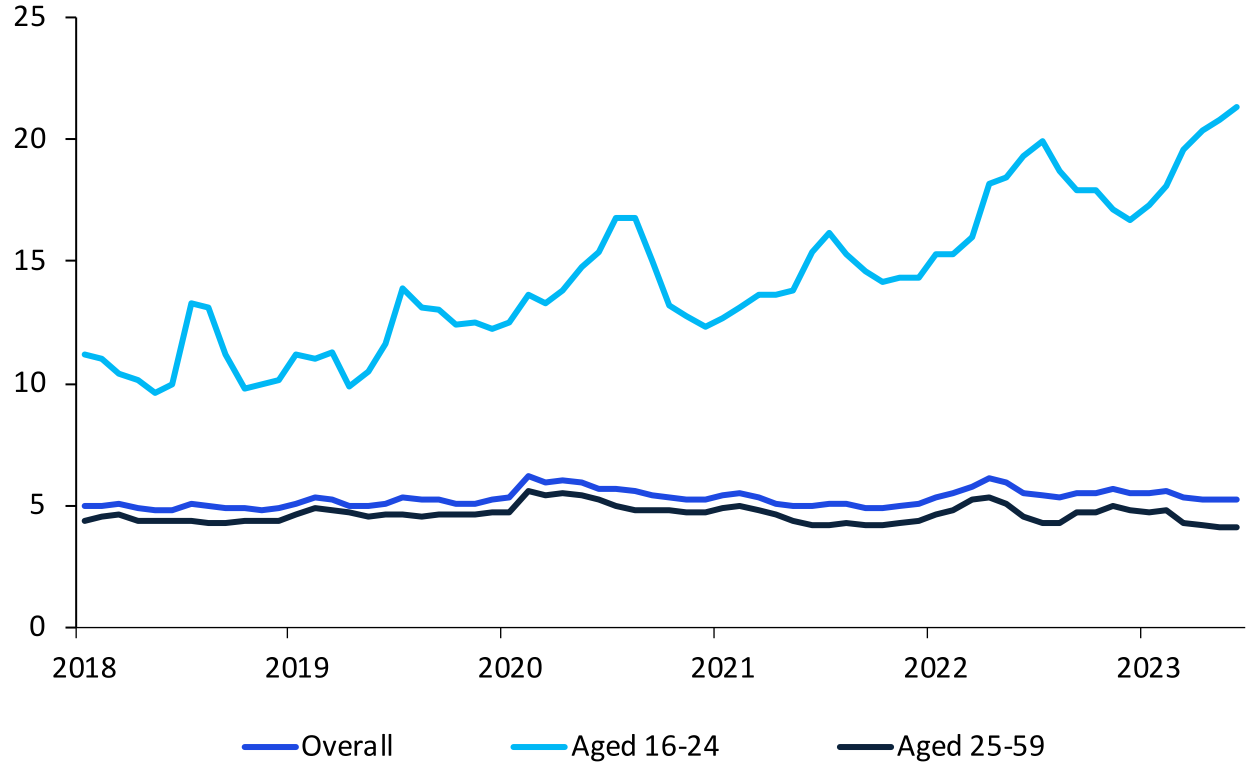


Source: Wind, KPMG analysis.
Goods sales data are for above-size retail enterprises.

- With COVID-related travel restrictions lifted, retail sales saw a significant recovery in H1 2023, especially in the services sector.
- Contact-related consumption including dining, entertainment and travel grew rapidly in H1 2023, with revenues from tourism, movie box offices and catering increasing by 95.9%, 52.9% and 21.4% respectively.
- In terms of sales growth of goods, jewellery, apparel and medicine showed a faster growth compared to last year. But real estate-related retail sales remained generally soft, and construction materials continued to slide. Auto retail sales growth picked up with policy support.

China youth unemployment hits high

Urban surveyed unemployment rate, %

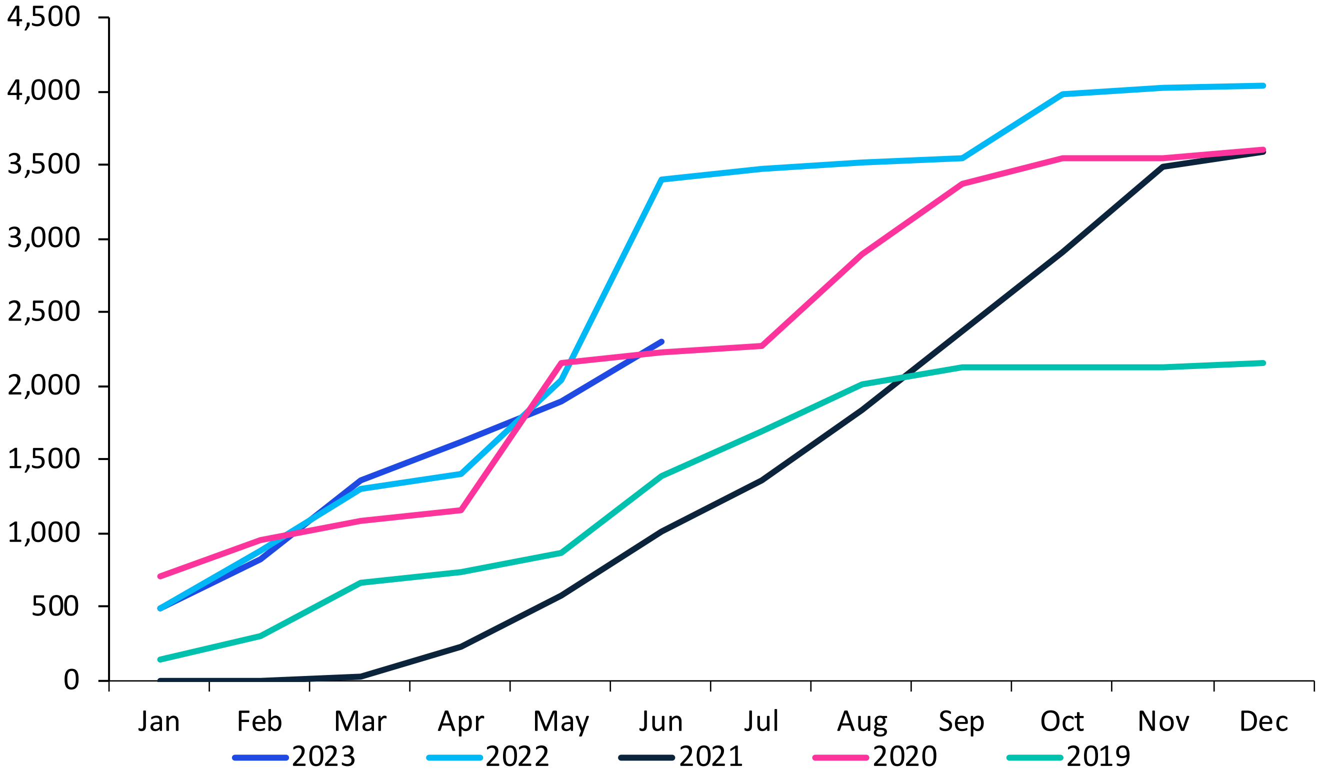


Source: Wind, KPMG analysis

- The overall urban surveyed unemployment rate remained unchanged at 5.2% in June. The unemployment rate of people aged 25 to 59 is also at a relatively low level.
- However, rising youth unemployment adds to concerns, The unemployment rate for the 16-24 age group hit a new high of 21.3% in June, up from 20.8% in May.
- The elevated youth unemployment rate highlights the need for more policy support to create new job opportunities.

China to speed up special bonds issuance to support infrastructure investment

Newly issued local government special bonds, RMB billion

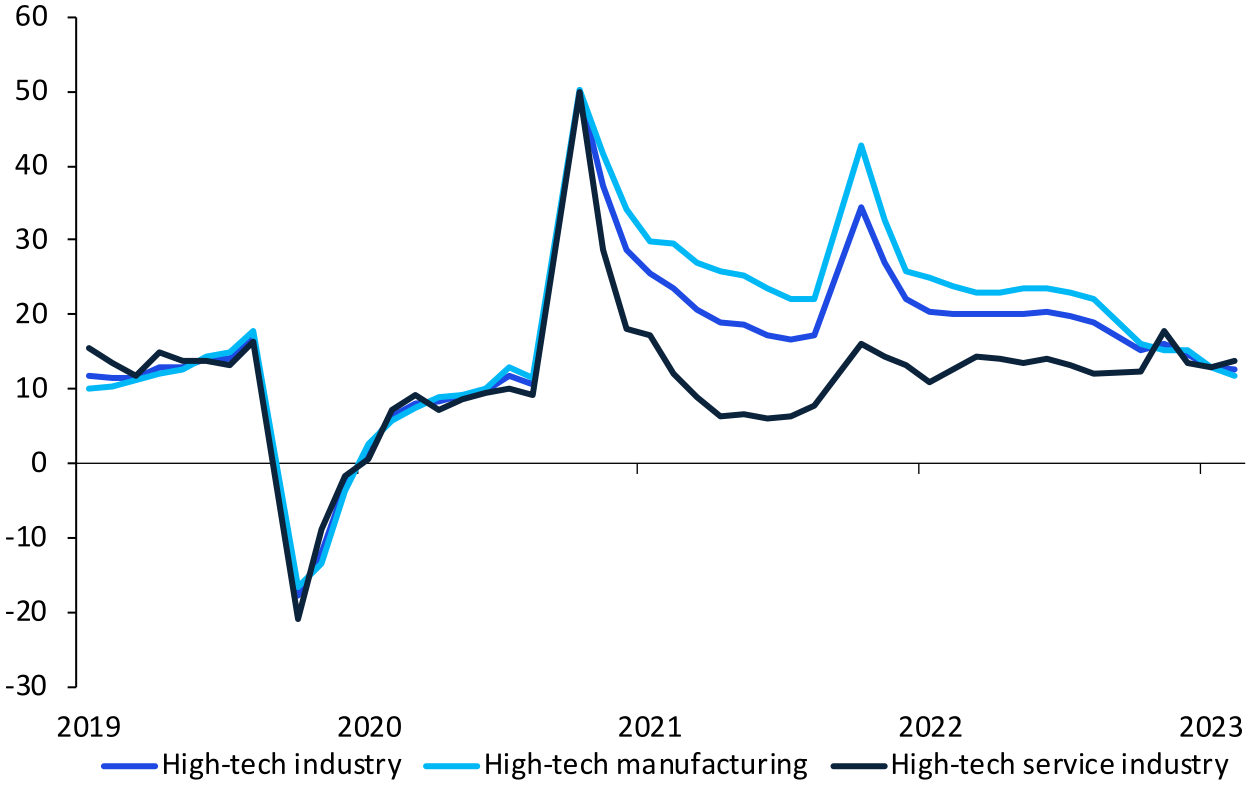


Source: Wind, KPMG analysis

- With the stable growth policies remaining in force, infrastructure investment registered a cumulative growth of 10.7% in H1 2023.
- Newly issued local government special bonds hit 2.3 RMB trillion, accounting for 60.5% of the annual quota (3.8 RMB trillion), a pace which is lower than the 84.3% seen in the same period last year.
- China's local government special bonds issuance will accelerate in the second half of this year. Infrastructure investment is thus expected to maintain a high degree of prosperity.

High-tech investment maintained robust increases

Investment in high-tech sectors, yoy, %

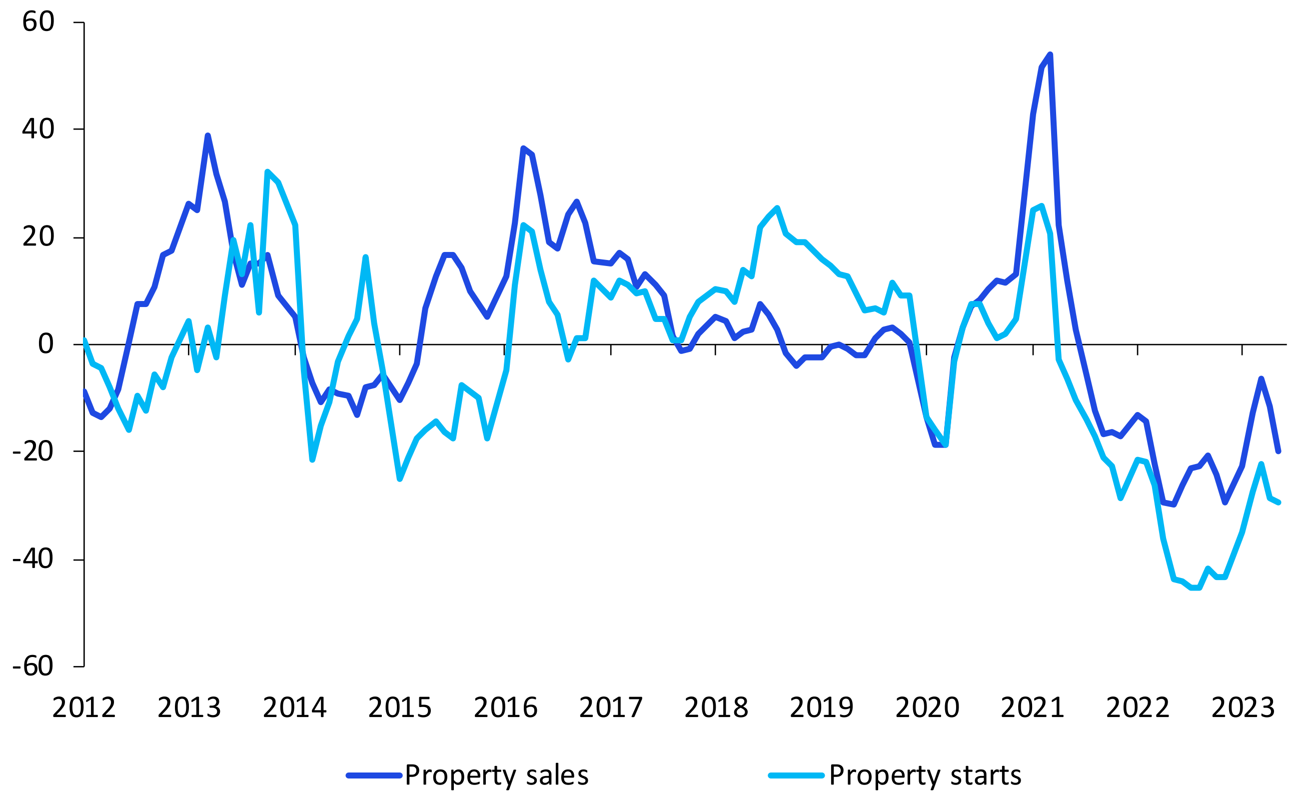


Source: Wind, KPMG analysis

- High-tech industry investment grew by 12.5% in H1 2023, 8.7 percentage points higher than overall investment.
- Investment in high-tech manufacturing and services grew by 11.8% and 13.9% respectively—8.0 and 10.1 percentage points higher than overall investment.
- However, compared to the high-tech service industry, China's high-tech manufacturing declined substantially compared with last year's annual growth rate of 22.2%.
- We expect that high-tech investment will maintain its strength and resilience through the support of financial credit policies.

The pace of recovery in the property sector is slowing down

Property starts and new home sales, yoy, three-month moving average, %



Source: Wind, KPMG analysis

- Driven by a concentrated release of pent-up demand, the property market appeared to be recovering in Q1. However, the pace of recovery slowed in Q2, with some property-related indicators showing a broad-based slowdown.
- Growth in new home sales dropped notably to -28.1% in June from -19.8% in May, with the decline widening for three consecutive months. Growth of property starts further contracted to 31.4%.
- The July Politburo meeting pointed out more support for the property sector in H2, which will be conducive to boost market confidence.

Low base effect and economic recovery contribute to government revenue growth

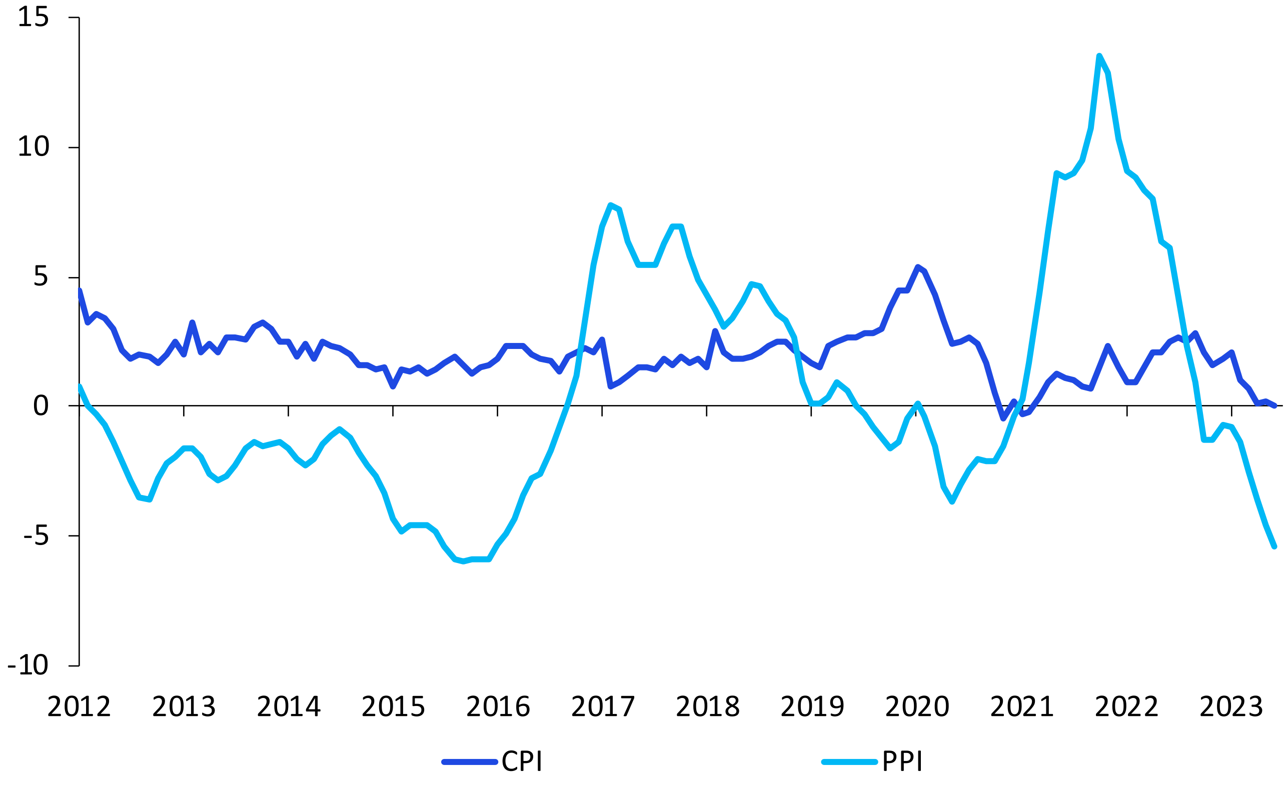
General government revenue and expenditure, yoy, %

Source: Wind, KPMG analysis

- Total government revenue increased by 7.1% in H1 2023, exceeding this year's budget target of 4.9%. Such fiscal revenue growth not only benefits from the country's economic recovery, but was also influenced by the base effect of the large-scale VAT deferral and refund since last April, resulting in a significant increase in tax refunds.
- Total government expenditure fell by 3.6% in H1, continuing the declining trend seen since mid-2022. Fiscal expenditure growth is now slower than the budget target, with China expected to ramp up fiscal stimulus to support the slowing economy in H2.

Weak demand is curbing inflation

China consumer price index (CPI) and producer price index (PPI), yoy, %

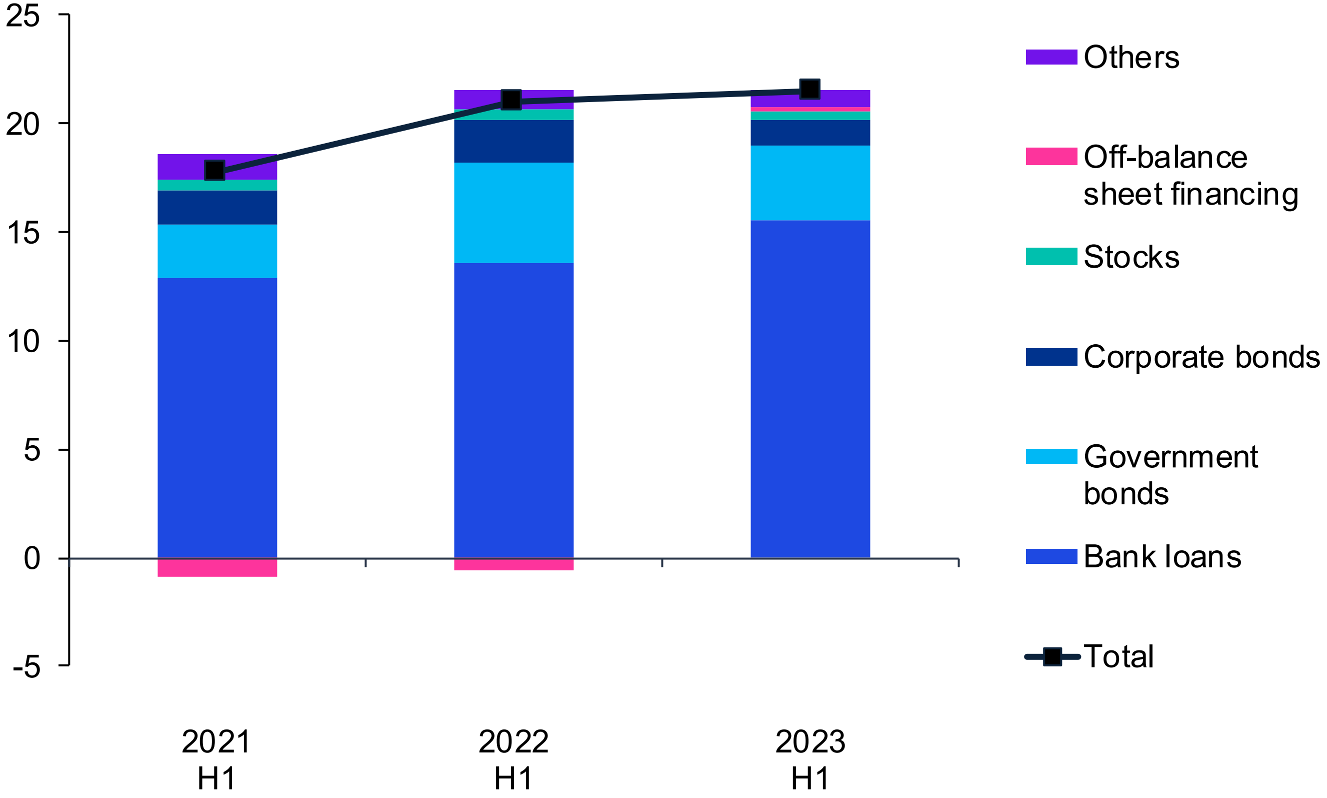


Source: Wind, KPMG analysis

- China's CPI in June fell from 0.2% in May to 0%, mainly driven by pork and energy prices. However, Core CPI, excluding food and energy, also fell 0.2 percentage points to 0.4%, indicating sluggish demand.
- Due to the continued decline in commodity prices and a higher base, China's PPI continued to fall by 5.4% in June, which remained in negative territory for nine consecutive months.
- Looking ahead, we expect China's CPI will rebound slowly as economic activities recover and policy stimulus continues, while the year-on-year decline in PPI will gradually converge as the high base effect subsides.

Bank loans are still the main contributor to total social financing

Growth of total social financing by sector, RMB trillion

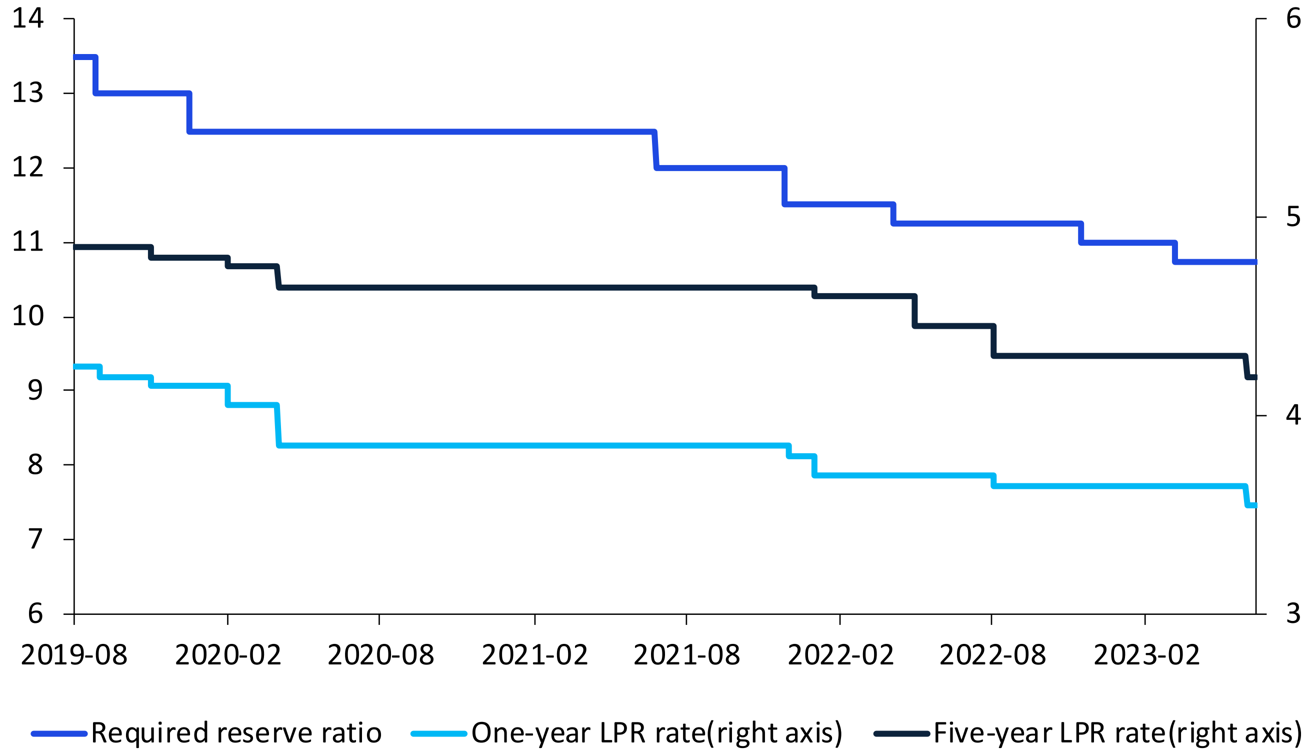


Source: Wind, KPMG analysis

- About RMB 15.6 trillion in new bank loans originated in H1 2023, up RMB 2.0 billion from H1 2022, a share of 72.4% for new total social financing. New bank loans in Q2 2023 totaled 4.9 trillion, down 6 trillion from Q1 2023.
- With the slow issuance of special bonds in H1, government bonds issuance fell by 1.3 trillion from H1 2022. Chinese local governments will speed up special bonds issuance in H2.
- Corporate bonds issued in H1 2023 totaled 1.2 trillion, a share of 5.4% of total social financing, down RMB 78.83 billion from the same period last year.

China's central bank is stepping up monetary support to boost economic growth

Required reserve ratio (RRR) and loan prime rate (LPR), %

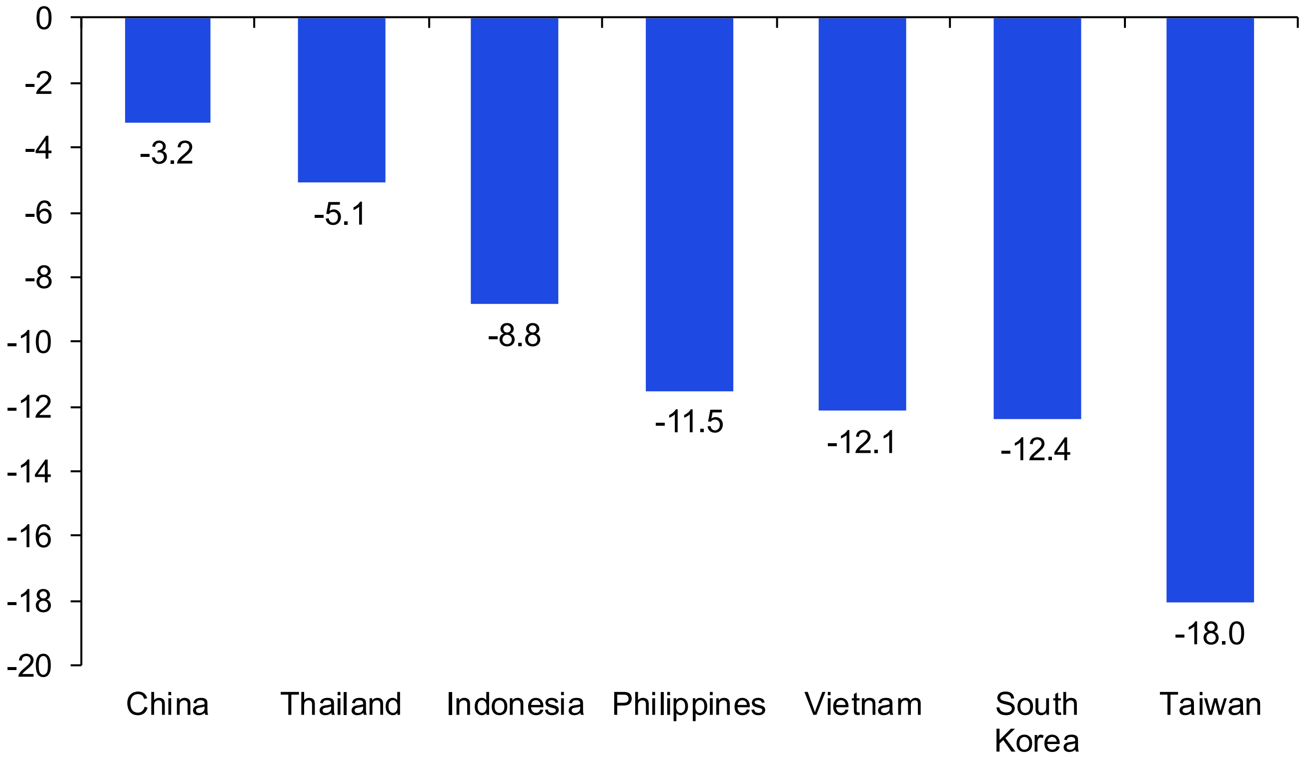


Source: Wind, KPMG analysis

- In early June, major Chinese banks lowered deposit rates by 5 to 25 bps. On June 13, the PBoC lowered the reverse repo (OMO) and the 1-year medium-term lending facility (MLF) by 10 bps respectively, and then lowered the 1-year and 5-year LPRs by 10 bps respectively to further reduce the cost of residential loans and corporate financing.
- The central bank has also increased its direct credit support to SMEs, green investment, tech and elderly care via channels such as special relending facilities.

China's exports outperformed other major export-oriented economies in H1

Export growth of export-oriented economies (countries and jurisdictions) in Asia, yoy, %

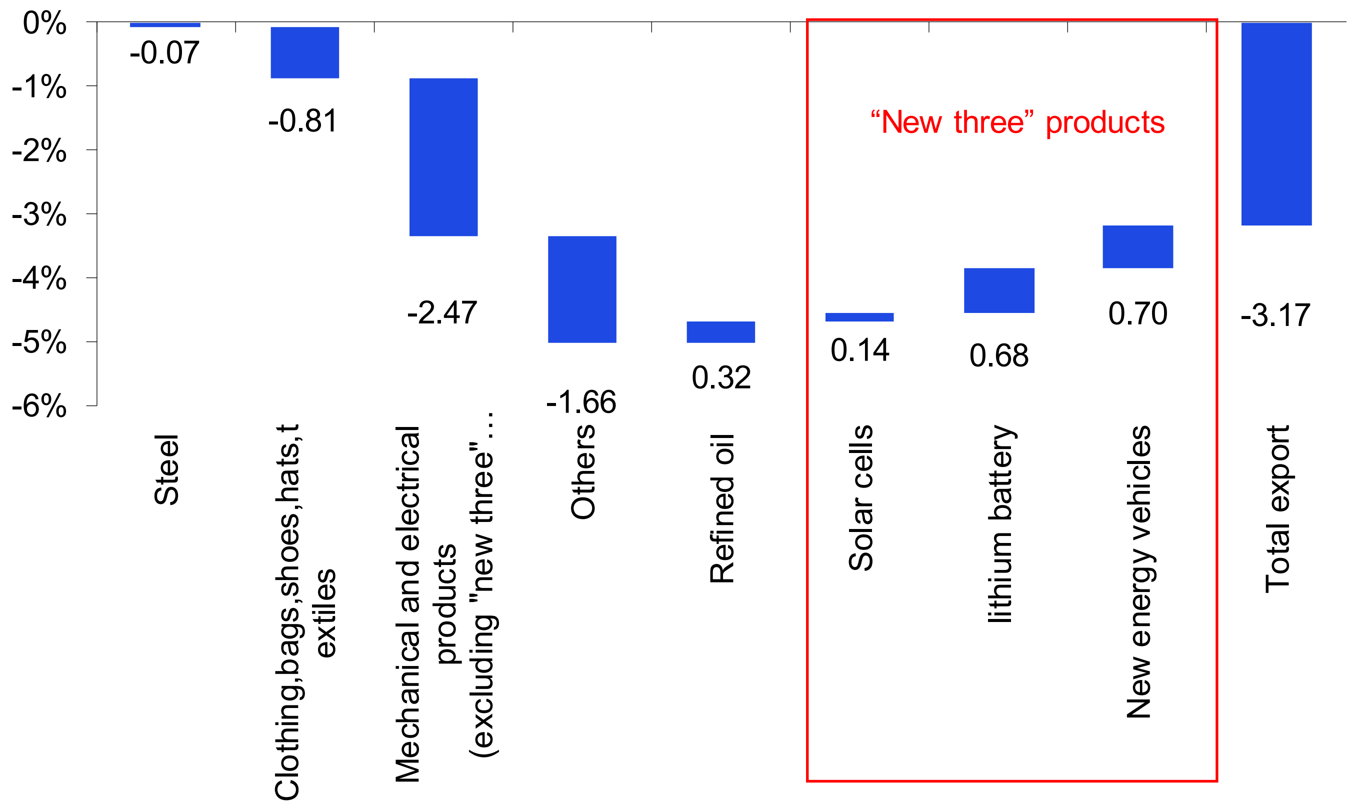


- China's exports performed better than expected in H1 2023, with robust growth in March and April. However, with a weakening external demand in May and June, coupled with a high base effect, export growth in H1 2023 fell back to -3.2%
- Despite overall slowing exports, China's exports still outperformed other major export-oriented countries and jurisdictions as Taiwan, South Korea and Vietnam declined by 18.0%, 12.4% and 12.1% respectively.

Source: Wind, KPMG analysis
Note: Thailand and the Philippines have accumulated year-on-year data from January to May 2023, while other economies have accumulated year-on-year data from January to June 2023.

“New Three” products are emerging as new drivers for China's exports

Contribution to 2023H1 export growth by category, percentage points

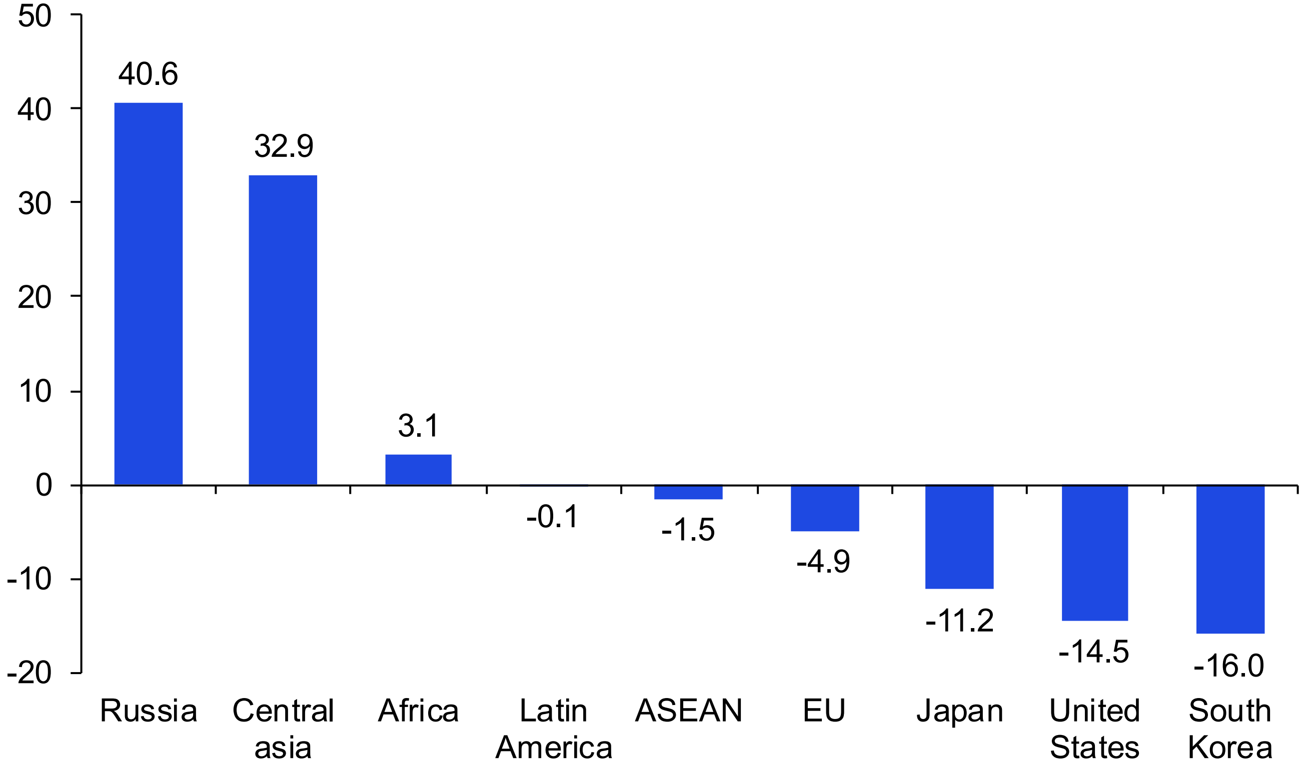


Source: The General Administration of Customs, KPMG analysis

- The share of advanced manufacturing in China’s exports continued to grow rapidly.
- The exports of “new three” products, including solar cells, new energy vehicles (NEVs) and lithium batteries, grew 50.1% in total in H1 2023, pulling up the overall export growth rate by 1.5 percentage points and becoming the main driver of China’s exports.
- Accommodative policies for green transition, particularly for new energy vehicles, are being actively implemented globally. We expect that the “New Three” products will remain bright spots in 2023.

Growth in trade with Russia and Central Asia-5 became the fastest

China’s trade with major economies in 2023H1, yoy, %

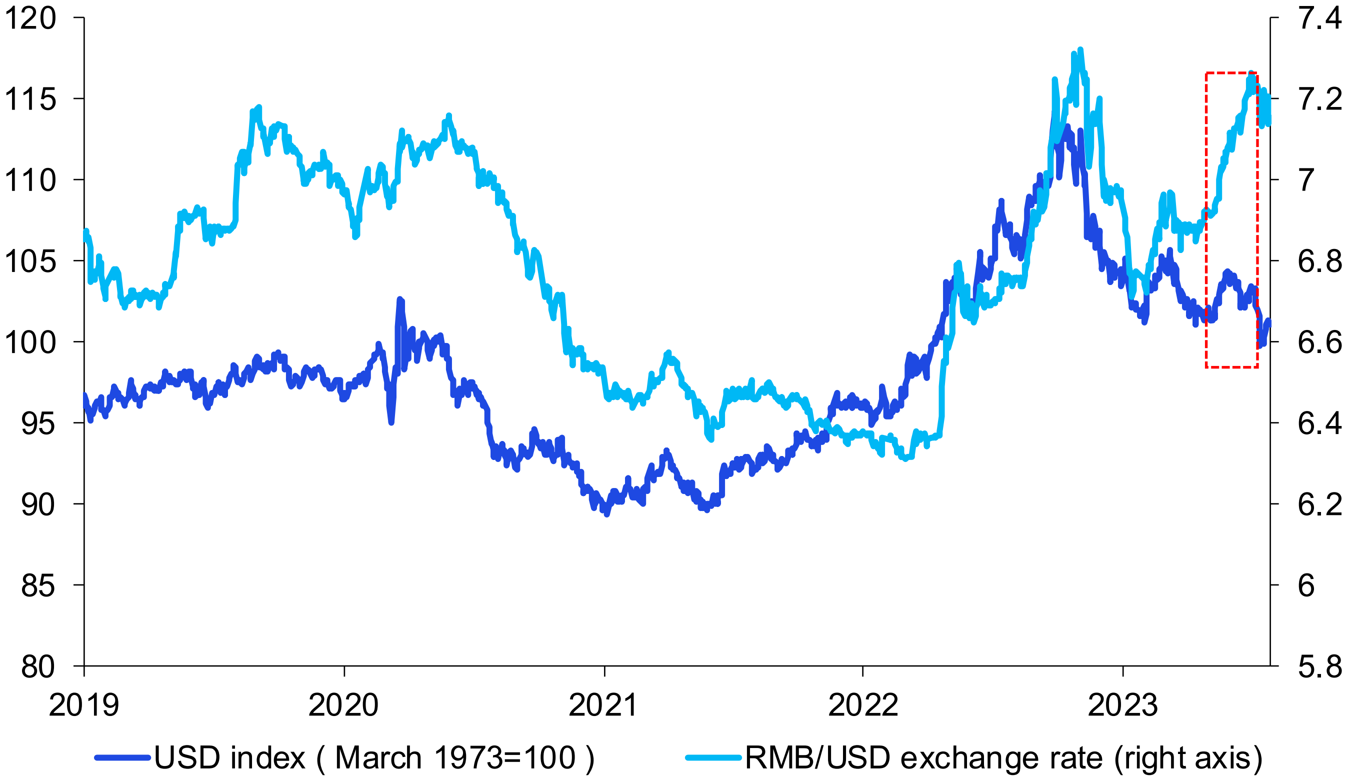


Source: Wind, KPMG analysis

- Despite slowing exports to advanced economies, China’s trade with Russia and most emerging markets continued to rise in H1 2023.
- The growth in trade with Russia and the Central asia countries became the fastest among all countries. Trade with Russia in H1 2023 went up 40.6% from H1 2022, and its share of total trade volume went up 130 bps to 3.9%.
- China has further diversified its trading partners to develop comprehensive trade channels and resist external market risks. We expect exports to remain resilient this year.

The RMB exchange rate against the USD is expected to remain relatively stable

USD index and RMB/USD exchange rate

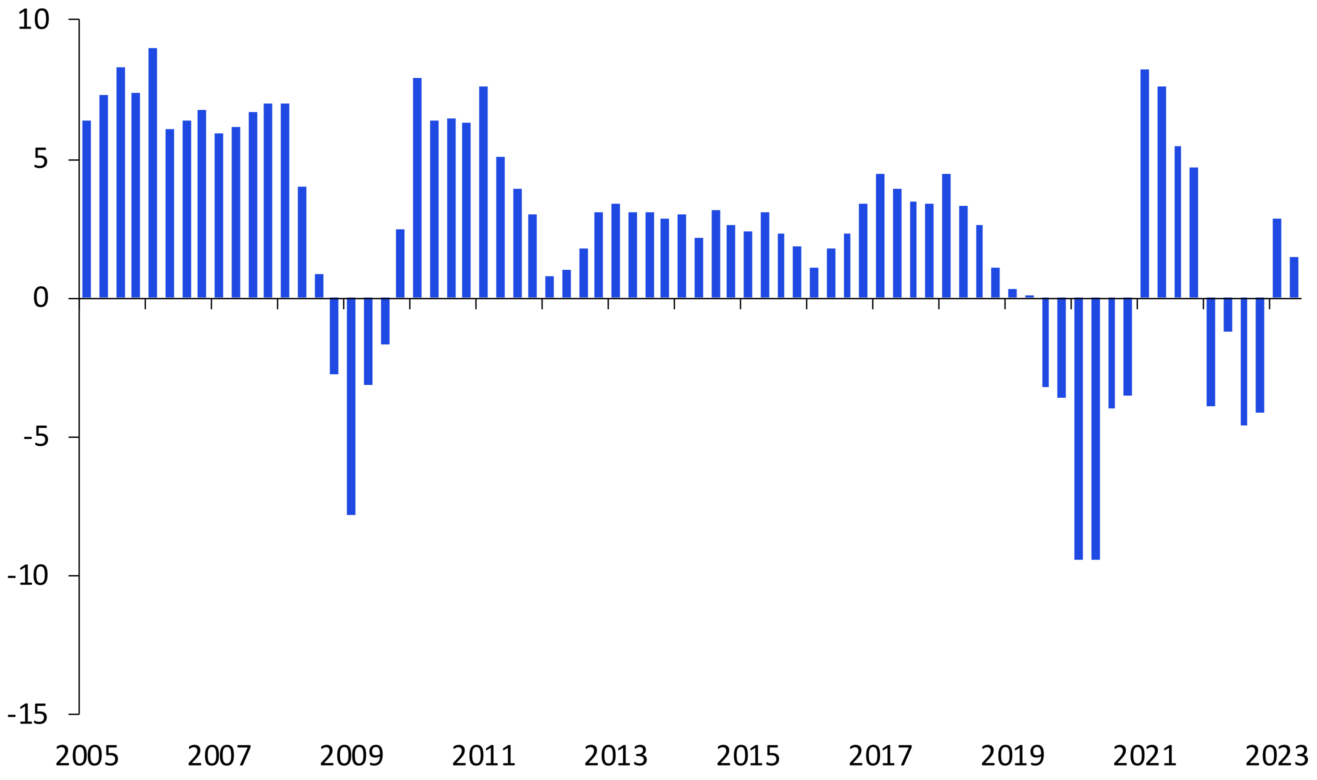


Source: Wind, KPMG analysis

- Amid a China-US monetary policy divergence and slowing momentum of China's economic recovery, the RMB has depreciated by more than 5% against the dollar since mid-April.
- The current round of RMB depreciation is mainly due to the weakening of domestic economic fundamentals. Since April, the CFETS RMB exchange rate index also fell by about 4.0%.
- Further stimulus measures may be announced soon, which should be sufficient to revive market expectations and bring the Chinese economy back on a faster recovery track, supporting the RMB to remain stable in H2 2023.

Hong Kong (SAR)'s economy continues to recover

Hong Kong's real GDP growth rate, yoy, %

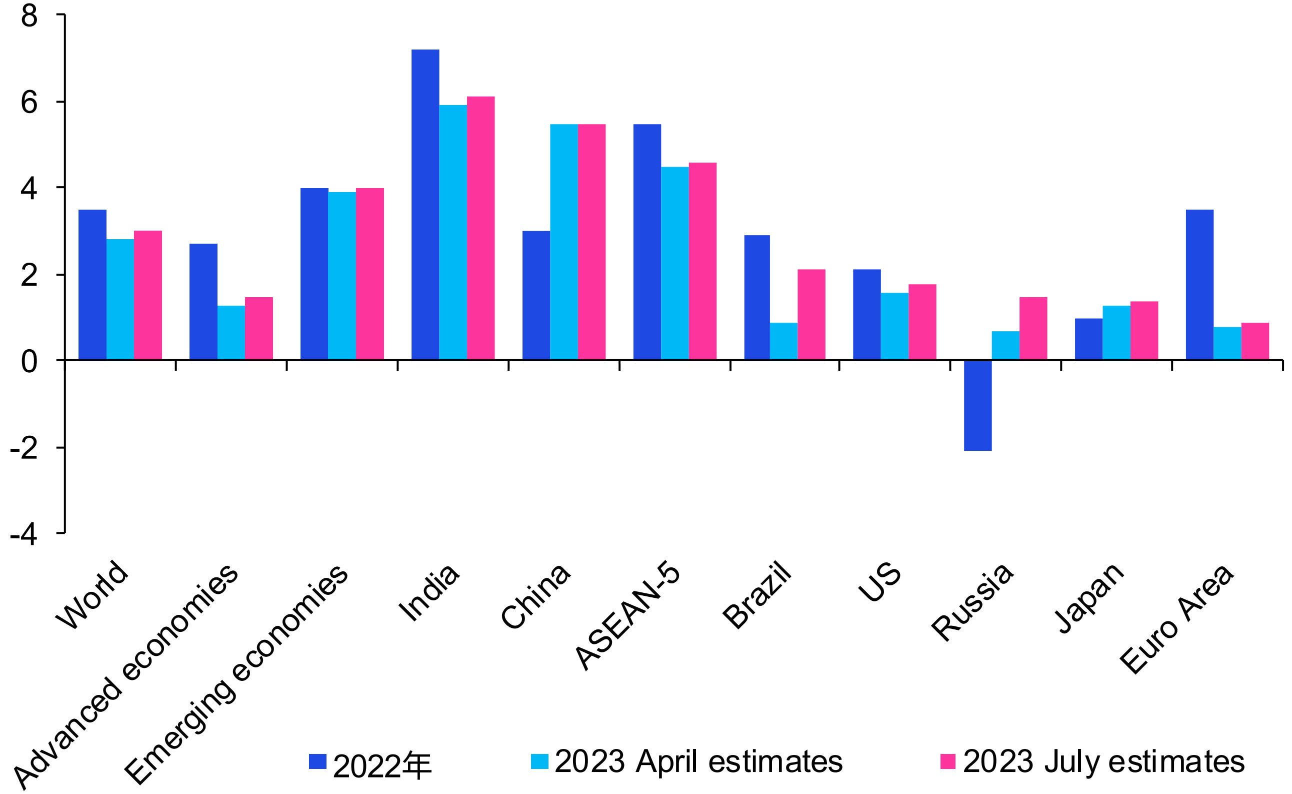


Source: Wind, KPMG analysis

- Hong Kong (SAR)'s economy grew by 1.5% in Q2 2023. Driven by a strong recovery in inbound tourism and private consumption, the Hong Kong economy continued to recover, though momentum softened on the back of the strong rebound seen in Q1.
- Exports declined further in June 2023 amid the weak external environment. The labour market continued to improve alongside the continued revival of domestic activities and inbound tourism.
- Looking ahead, inbound tourism and private consumption will remain the major drivers of Hong Kong's economic growth this year. Yet, exports of goods will continue to face intense pressure, as slower global economic growth weighs on external demand.

Despite recent positive growth surprises, global economic outlook remains challenging

Real GDP growth forecast for 2023, %



- The IMF raised its 2023 global growth forecast by 0.2 percentage points to 3.0% in its July report, up from 2.8% in its April assessment, but warned that persistent challenges were dampening the economic outlook.
- For advanced economies, the slowdown in growth projected for 2023 remains significant, from 2.7% in 2022 to 1.5% in 2023. The US forecast has been revised upward by 0.2 percentage points in July, on account of resilient consumption growth in Q1. The Euro area forecast is broadly unchanged.
- Growth of emerging economies is projected to be broadly stable at 4.0% in 2023. The 2023 forecasts for Brazil and Russia have been revised up sharply from April.

Source: IMF, KPMG analysis.
Note:China data is based on KPMG's projections. ASEAN-5 includes Indonesia, Malaysia, Philippines, Thailand, Vietnam.

Contact us

Michael Jiang
Head of Clients and Markets
KPMG China
+86 (10) 85087077
michael.jiang@kpmg.com

Norbert Meyring
Head of Multinational Clients
KPMG China
+86 (21) 22122707
norbert.meyring@kpmg.com

Miguel Montoya
Partner
KPMG China
+86 (10) 85084470
miguel.montoya@kpmg.com

Mark Harrison
Partner
KPMG China
+86 (21) 22123620
mark.harrison@kpmg.com

Shigeru Inanaga
Partner
KPMG China
+86 (755) 25473387
shigeru.inanaga@kpmg.com

Anson Bailey
Partner
KPMG China
+852 29788969
anson.bailey@kpmg.com

Kevin Kang
Chief Economist
KPMG China
+86 (10) 85087198
k.kang@kpmg.com

Research Team: Yanan Zheng; Feiyang Lin, Chengzhe Zhou(trainee)
Design: Zheng Zhu

kpmg.com/cn/socialmedia

For a list of KPMG China offices, please scan the QR code or visit our website:
https://home.kpmg.com/cn/en/home/about/offices.html