China Economic Monitor

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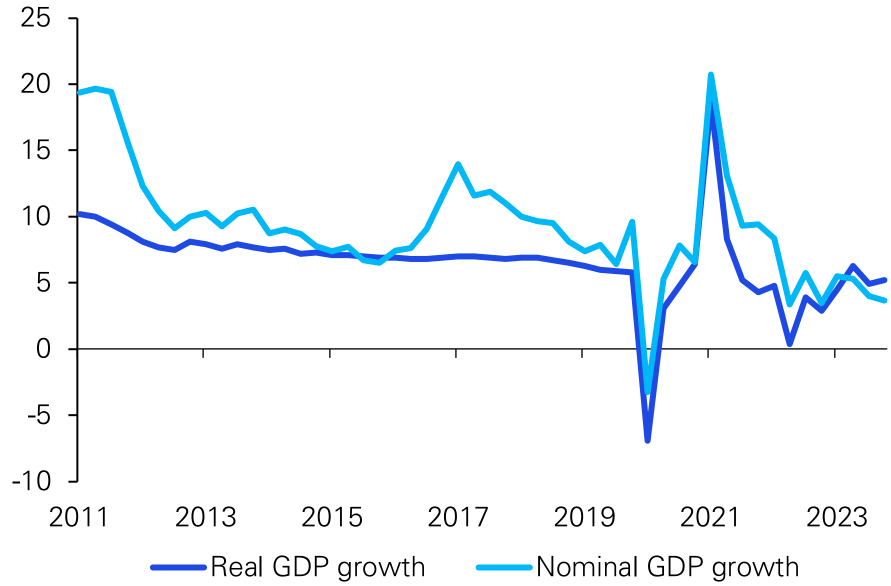
In 2023, China’s economy expanded by 5.2%, successfully meeting the annual growth target of “about 5%”. This growth included a year-on-year increase of 5.2% in the fourth quarter. Additionally, GDP rose by 1% on a quarter-by-quarter basis in the fourth quarter. The steady recovery of industrial production, significant improvement of the service sectors, and continuous optimization of the export structure supported the steady recovery of China's economy in 2023, with the economic growth rate surpassing the target put forward at the two sessions last year. Consequently, the size of China's economy has reached a new milestone with annual GDP reaching RMB 126 trillion.

Looking forward to 2024, the employment landscape is expected to gradually improve, increasing consumer income and leading to growth in consumption. In terms of investment, infrastructure is anticipated to play a supporting role in the economy and maintain steady growth. The manufacturing industry is projected to see growth, bolstered by policy support. The further easing of real estate policies is expected to gradually release housing demand. This change is likely to improve the financing conditions for real estate enterprises, helping to stabilize the real estate market, and lessen the drag on the economy.

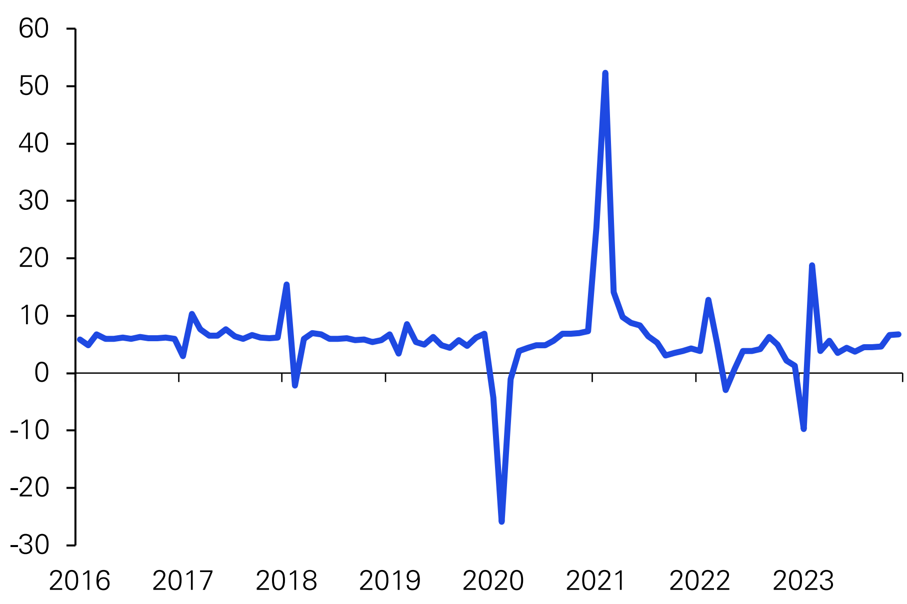
Internationally, the fall in the inflation rate has led the Federal Reserve to suspend the pace of interest rate hikes, easing the pressure on the RMB exchange rate and capital markets, which is conducive to the stability of China's financial market. However, the global environment is still complex and severe. Confidence remains low, domestic demand needs to be further released, and the economy is facing several difficulties and challenges that hinder its recovery. Despite these obstacles, we expect that China's economy will continue its recovery and grow by 4.8% for the full year.

Figure 1 GDP growth, % , YoY



In terms of output, industrial production increased by 4.6% year-on-year in 2023, 0.6 percentage points higher than in the first three quarters. Specifically, in December, it increased 6.8% year on year, 0.2 percentage points higher than in November. Policies aimed at stabilizing growth continued to be effective, new growth engines emerged, and innovation steadily increased. These factors promoted the stable recovery of the industrial economy, supported the recovery of industrial production, and continued to optimize the industrial structure. Looking ahead, after three consecutive months of decline, the manufacturing PMI rebounded for the first time in January 2024, to 49.2%, 0.2 percentage points higher than in December 2023.

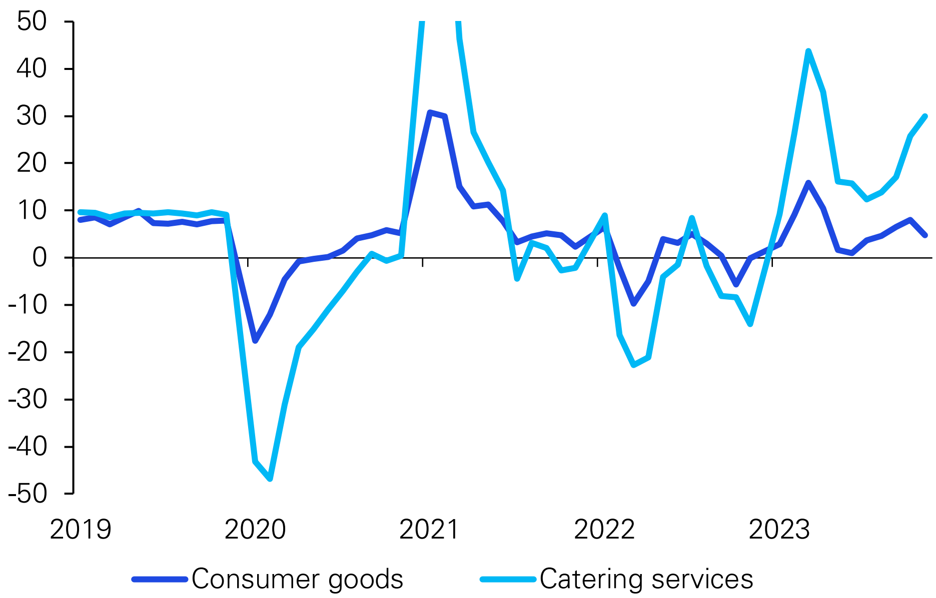
Figure 2 Growth of industrial production, YoY,%



Source: Wind, KPMG analysis

On the demand side, in 2023 total retail sales reached RMB 47.1 trillion, an increase of 7.2% over the previous year, 7.4 percentage points higher than that of 2022, setting a new record for total consumption. The contribution of final consumption expenditure to economic growth reached 82.5%, underscoring its role as the main driver of economic growth. From a consumption standpoint, service consumption picked up quickly in 2023. As residents continue to pursue a better quality of life, it is expected that the proportion of service consumption will continue to rise. In addition, in 2023, national online retail sales reached RMB 15.4 trillion, marking an increase of 11% over the previous year, and accounting for 27.6% of social retail sales – a record high. During the Spring Festival in 2024, travel and consumption during the national holidays saw a significantly increase compared with the same period last year. With policies actively promoting stable expectations for growth and employment, residents' incomes and market expectations are anticipated to gradually improve to help the consumer market further recover.

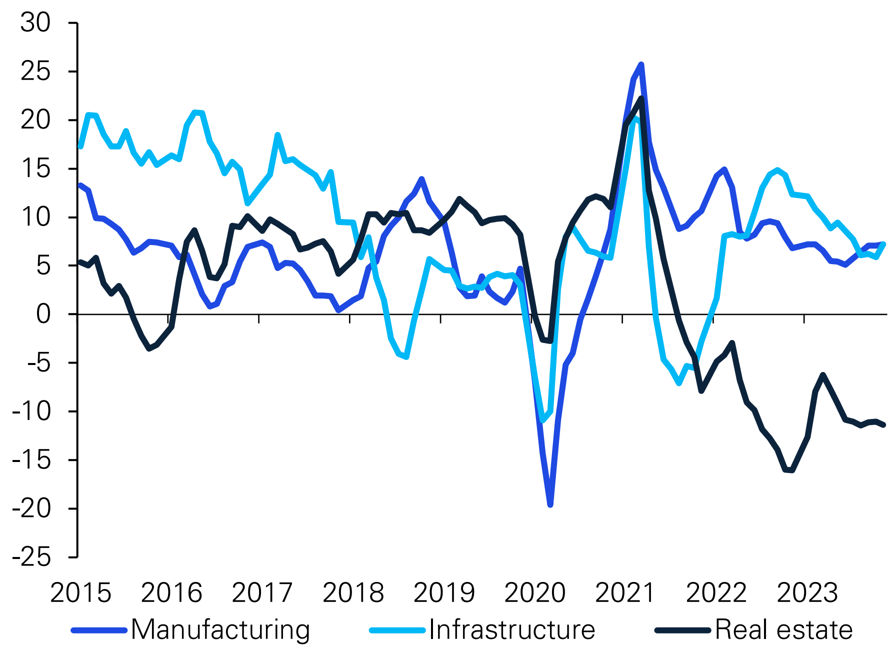
Figure 3 Retail sales and catering revenue, %, YoY



Source: Wind, KPMG analysis

In terms of investment, total fixed asset investment in 2023 grew 3% year on year, with the growth rate falling 2.1 percentage points compared with the same period last year. Notably, in Q4 fixed asset investment increased by 2.7% year-on-year, 0.9 percentage points higher than in the third quarter. Investment in 2023 was supported mainly by manufacturing and infrastructure, which saw increases of 6.5% and 8.2% respectively. In contrast, real estate investment faced challenges, declining by 9.6%, and thus became the main drag on the overall growth of fixed asset investment. The year-on-year growth rate of private fixed asset investment in 2023 was lower than that of all fixed asset investment, with a year-on-year decrease of 0.4%, about 1.3 percentage points lower than that of 2022. Looking ahead, with the ongoing implementation and refinement of supportive policies and measures, it is expected that private investment will gradually recover in 2024.

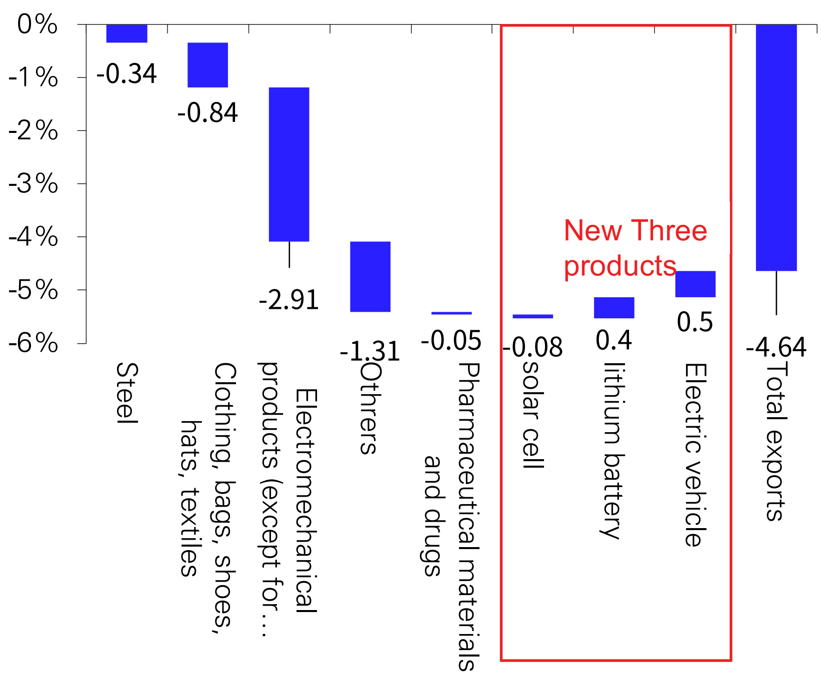
Figure 4 Fixed assets investment by sector, yoy, 3-month moving average ,%



Source: Wind, KPMG analysis

In 2023, China's exports amounted to USD 3.38 trillion, down 4.6% year on year. This decline was primarily driven by weak external demand. However, the export situation showed signs of improvement in the fourth quarter, thanks to a low base effect and the onset of the traditional peak consumption season overseas. In this period, the export situation improved since the fourth quarter, with the year-on-year rate improving to -1%, 9 percentage points higher than the third quarter. During the year, China continued its transition from traditional manufacturing to high-technology manufacturing, leading to a continuous optimisation of the export commodity structure. Notably, in 2023 the total export "three new products" made in China – electric manned vehicles, lithium-ion batteries and solar batteries – exceeding RMB 1 trillion for the first time, an increase of 29.9% over the previous year. On the other hand, the "Belt and Road Initiative" and RCEP have been conducive to the development of regional trade, with trade between China and emerging market economies showing promising growth momentum. With the anticipated improvement in the global economy and the continuous optimization of China's export commodity structure, it is expected that exports will maintain resilience in 2024.

Figure 5 Contribution of major commodities to total exports, percentage points

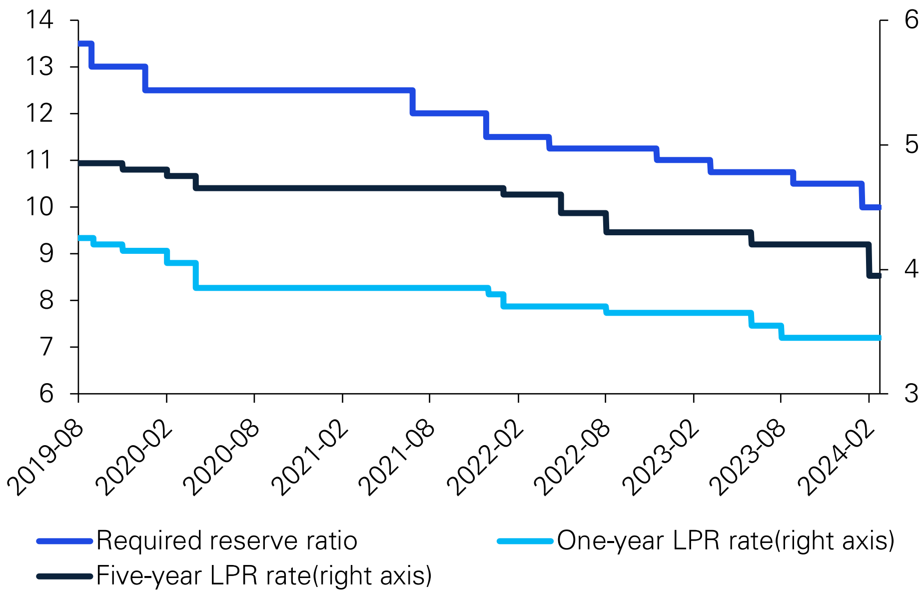


Source: General Administration of Customs, KPMG analysis

China’s fiscal revenue reached RMB 21.7 trillion in 2023, up 6.4% year on year, and 5.8 percentage points higher than that of the previous year. However, when excluding the impact of tax rebates, general government revenue fell 4.9% year on year, indicating that growth momentum of actual fiscal revenue needs further improvement. Government expenditure continued to increase in 2023, with total fiscal expenditure reaching RMB 27.5 trillion, up 5.4% year on year. Social security and employment, education, science and technology, agriculture, forestry, water, urban and rural communities, and other key areas of expenditure were prioritised, ensuring that spending in these areas was well protected. Affected by the continuous decline in the real estate market and the sharp drop in land sales, the government-managed fund revenues were lower than expected and declined by 9.2% in 2023. Expenditure of the government-management fund fell 8.4% year on year. This is expected to impact future financial flexibility and public investment capacity.

Throughout 2023, monetary policy continued to support steady growth and strengthen support for key sectors and weaker areas of the economy. The year saw the Central Bank implementing cuts to the deposit reserve ratio of financial institutions by 0.25 percentage points in both March and September, effectively releasing over RMB 1 trillion. Furthering these efforts, on February 5, 2024, an additional cut of 0.5 percentage points was made, unlocking more than RMB 1 trillion in medium-and long-term liquidity. This series of adjustments not only expanded the credit capacities of banks and reduced the cost of loans but also ensured ample liquidity, contributing to increased social trust and confidence. In structural terms, the Central Financial Working Conference held in November 2023 highlighted "five major areas: science and technology finance, green finance, inclusive finance, pension finance, and digital finance" to optimise the structural impact of monetary policy. Following this, the Pledged Supplementary Lending (PSL) mechanism started to provide funds to policy banks from December 2023. By the end of January 2024, a total of RMB 500 billion in loans targeted at supporting the construction of "three major projects", formed precise and effective investment, helping to stabilize economic growth. The central bank has also been actively using tools such as refinancing and rediscounting to expand the credit supply, particularly in areas such as scientific and technological innovation, inclusive elderly care, and transportation logistics, maintaining a focus on key areas.

Figure 6 Required reserve ratio (RRR) and loan prime rate (LPR), %



Source: Wind, KPMG analysis

The Central Economic Work Conference has reiterated that monetary policy should remain flexible, appropriate, precise and effective, ensuring that liquidity levels are both reasonable and sufficient. It also remains a priority to align the scale of social financing and money supply with anticipated economic growth and targeted inflation. Looking ahead, there is potential for further adjustments in both quantitative measures and pricing mechanisms in monetary policy, indicating that further reductions in the reserve ratio and interest rates are still possible. In terms of structural adjustments, the government will continue to implement a series of targeted monetary policies in a reasonable and appropriate manner, and increase support for scientific and technological innovation, green transformation, inclusive small and micro businesses, and the digital economy.

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