China Economic Monitor

Issue: 2024 Q2

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Key takeaways

- China's GDP grew 5.3% year-on-year (YoY) in Q1 2024, up from 5.2% in Q4 2023 and higher than market expectations. Driven by the implementation of equipment renewal policies and the recovery of external demand, the rebound in industrial production, manufacturing investment and exports were the main contributors to the growth of China's economy.
- Consumption recovered with divergency. Service consumption continued to strengthen, with a growth rate of 10% in Q1 2024, while the growth of consumer goods consumption lagged behind its pre-pandemic level. It remains necessary to enhance residents' income growth and boost their confidence to spend.
- Manufacturing and infrastructure investments maintained their strong upward momentum, growing 9.9% and 8.8% in Q1 2024, respectively. Looking ahead, the push for equipment renewal is expected to sustain robust growth of manufacturing investment, and infrastructure investment will benefit from accelerated issuance of government bonds.
- The property market is still confronted with weak sales and sluggish investment, with real estate investment declining by -9.5% in Q1 2024. Looking forward, the property market is expected to pick up due to a low base last year and the easing of liquidity for property developers. However, the long-term improvement of the property market still requires sustained policy support on the demand side.
- The export growth rate in Q1 2023 returned to positive territory, mainly driven by the recovery of global manufacturing. China's trade with emerging markets has seen fast growth, reflecting strengthened regional collaborations. Meanwhile, the export commodity structure continues to optimize and upgrade, with exports expected to remain resilient in 2024.
- Looking ahead, the manufacturing PMI, a leading indicator of production, remained in the expansion zone, indicating a recovery in business prospects. However, challenges persisted in real estate and local government investments, which continue to hinder the recovery of economic growth. In addition, external demand is fraught with uncertainty. Against this backdrop, it is important to strengthen support on the demand side of the real estate sector, and expand fiscal expenditure.

Driven by rebounds in industrial production, manufacturing investment, and exports, GDP growth in Q1 2024 exceeded market expectations

Growth rate of major economic indicators, YoY, %

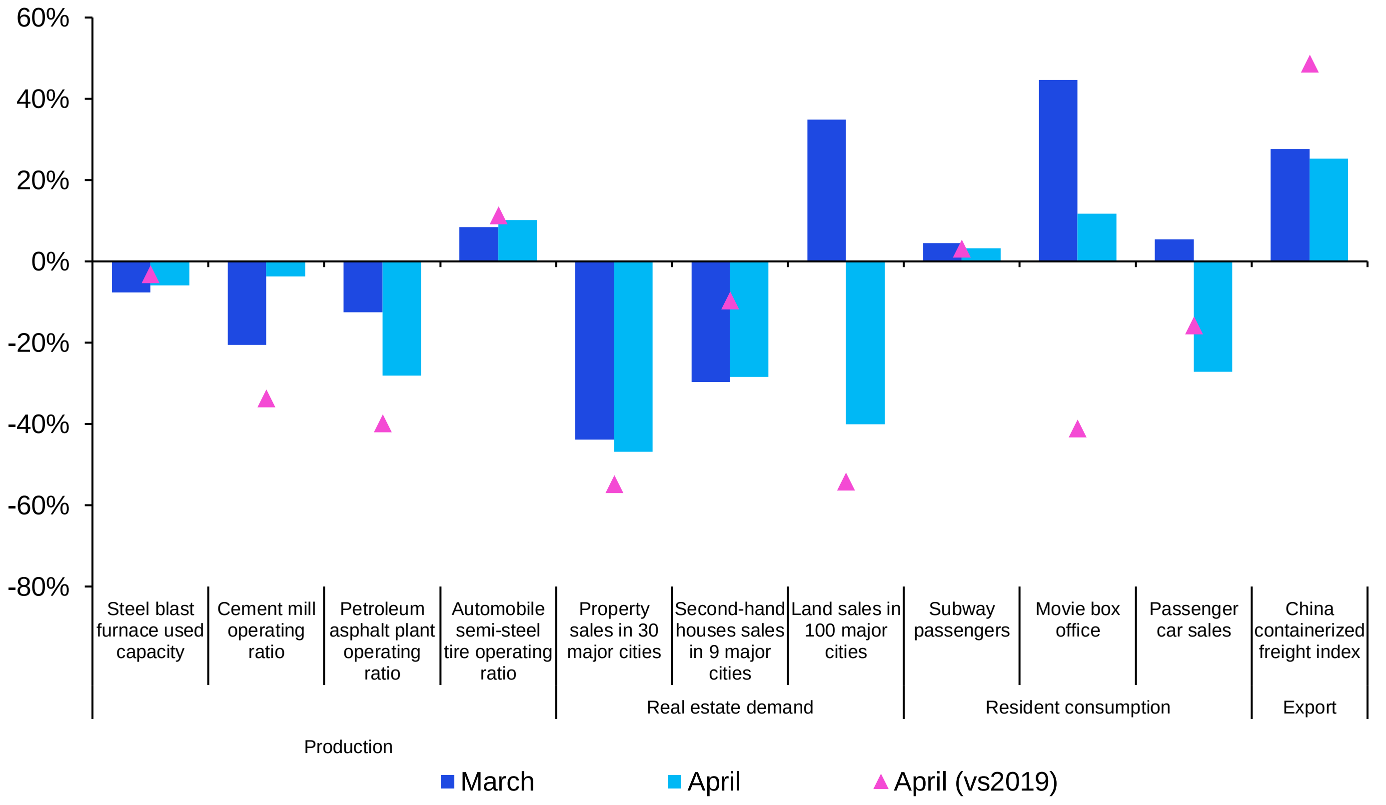
	2020-23 Average	2023Q1	2023Q2	2023Q3	2023Q4	2024Q1
GDP	4.7%	4.5%	6.3%	4.9%	5.2%	5.3%
Industrial Production	5.1%	3.0%	4.5%	4.2%	5.2%	6.1%
Retail Sales	3.7%	5.8%	10.7%	4.2%	8.3%	4.7%
Fixed Asset Investment	4.0%	5.1%	3.1%	1.9%	2.7%	4.5%
Exports	7.8%	-1.9%	-4.9%	-9.9%	-1.2%	1.5%
Imports	5.3%	-7.2%	-7.0%	-8.5%	0.8%	1.5%
Income per capita	4.8%	3.8%	8.3%	6.1%	6.7%	6.2%
Fiscal revenue	3.3%	0.5%	31.7%	-0.9%	-1.0%	-2.3%
Fiscal expenditure	3.6%	6.8%	1.0%	4.1%	9.2%	2.9%

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 5.3% YoY in Q1 2024, up from 5.2% in Q4 2023 and higher than market expectations.
- The growth was mainly driven by rebounds in industrial production, manufacturing investment, and exports, fuelled by the equipment renewal policies and a recovery in external demand.
- The growth rate of retail sales in Q1 2024 was 1.1 percentage points lower than Q1 2023, but showed a certain improvement of 1 percentage points compared to the two-year average for Q1 in 2022-23. Exports grew 1.5% YoY in Q1 2024, 3.4 percentage points higher than Q1 2023. Manufacturing and infrastructure investments supported a 4.5% growth rate in fixed assets investment during the same period.

Production activities outpaced demand growth

Economic activities growth rate in March and April, YoY, %

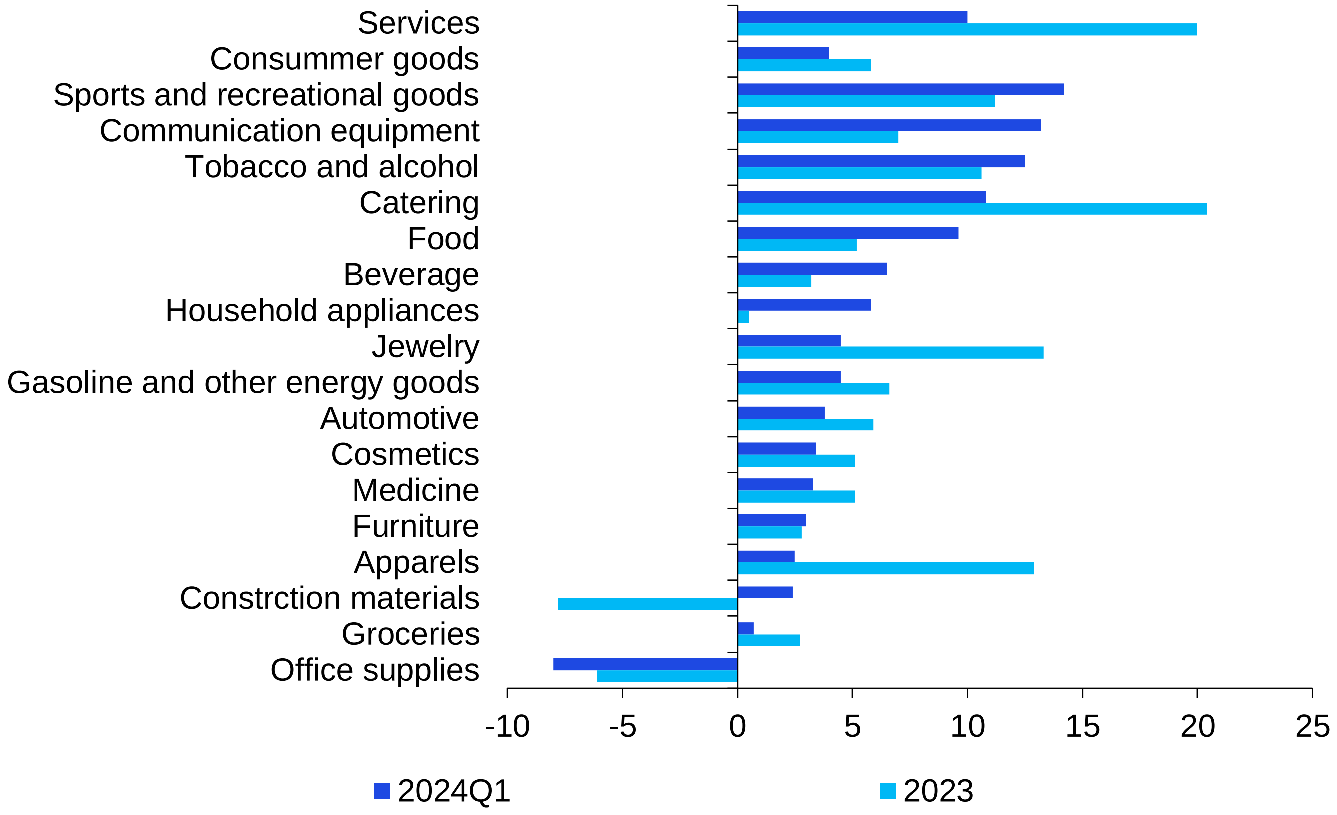


Source: Wind, KPMG analysis

- The manufacturing PMI in April reported a higher production index of 52.9, up from 52.2 in March 2024. However, the demand index saw a decline.
- In terms of the performance of high-frequency data, production of steel and cement recovered in April compared to March, while auto production remained robust. Meanwhile, on the demand side, indicators such as auto sales, infrastructure construction, and property transactions weakened compared to March.
- The divergency between production and demand highlights further supports on the demand side, particularly in fiscal and real estate areas.

Consumption continued to show a steady recovery

Growth of retail sales by category, YoY, %

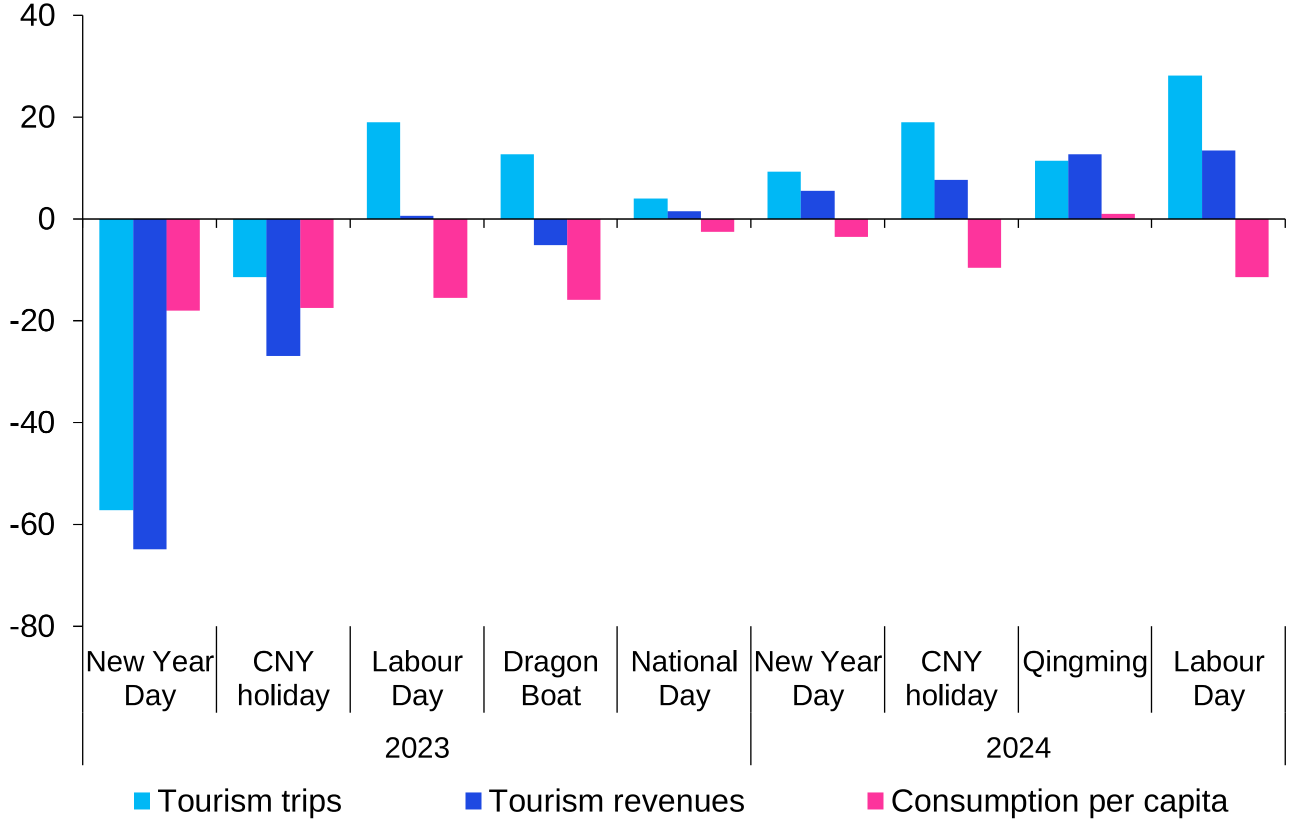


Source: Wind, KPMG analysis. Goods sales data are for above-size retail enterprises

- Consumption has continued a pattern of differentiated recovery since 2023, with services sales increasing by 10% YoY in Q1 2024, 6 percentage points higher than goods sales growth. Travel consumption also saw a boost in Q1 2024.
- Demand for higher quality goods is being released, partly due to the effective trade-in policy of consumer goods. Retail sales of household appliances, furniture, and construction materials also experienced positive growth rates.

Consumers are increasingly willing to spend, but their ability to do so is hindered

Changes in major holiday trips and tourism income compared to the same period in 2019, %

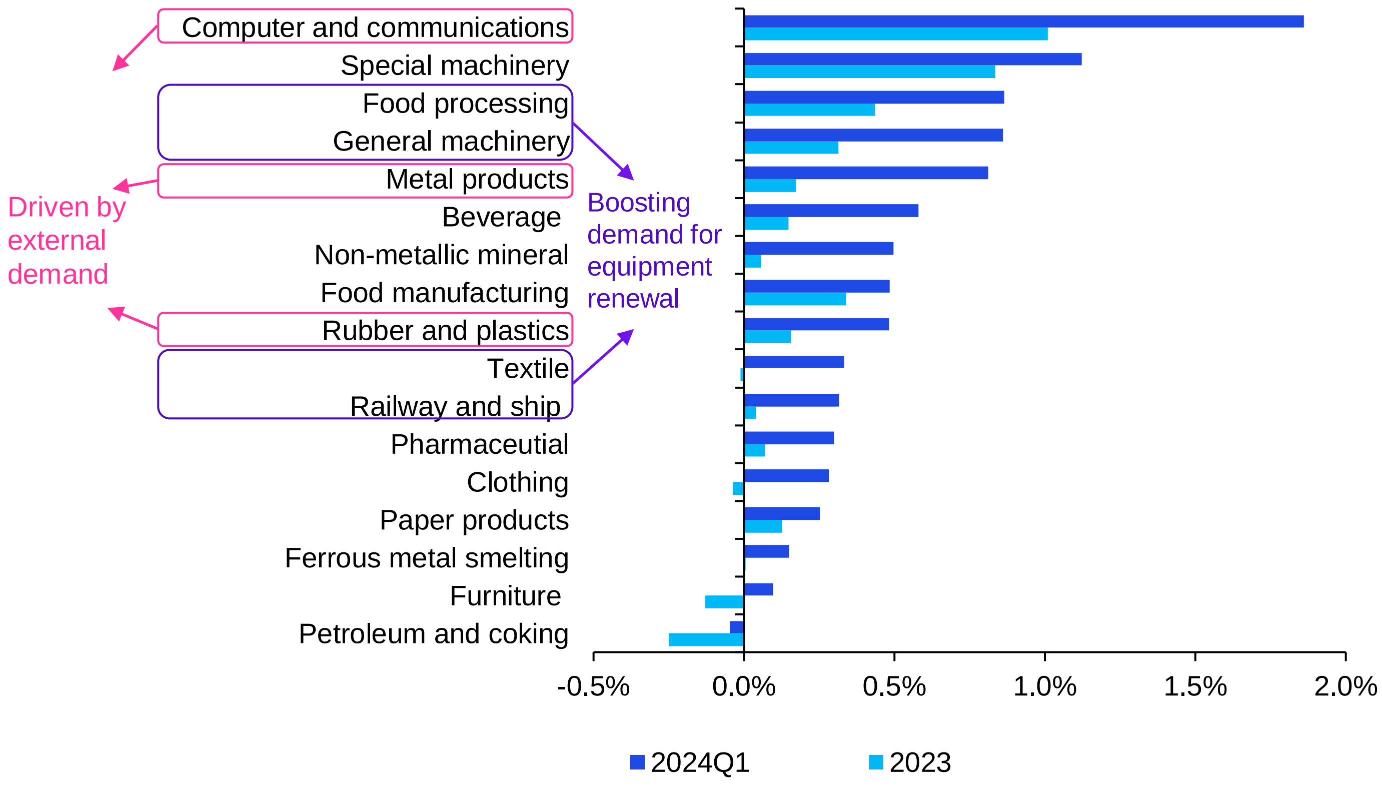


Source: Wind, KPMG analysis

- During the Labour Day holiday, domestic tourism trips and total tourism revenues increased by 7.6% and 12.7% YoY, with a comparable increase of 28.2% and 13.5% compared to the same period in 2019, respectively.
- Inbound and outbound tourism is recovering rapidly, thanks to the resumption of flights, easier border entry processes, and increasing visa-free travel.
- However, per capita spending on tourism declined during the Labour Day holiday, indicating that there is still room to improve spending capacity of residents.

Exports and equipment renewal drove improved manufacturing investment

Contributions to manufacturing investment growth by sector in Q1 2024 and 2023, %



Source: Wind, KPMG analysis

- The growth rate of manufacturing investment reached 9.9% in Q1 2024, an increase of 2.7 percentage points compared to Q4 2023, and 4.4 percentage points higher than the overall growth rate of fixed asset investment, exceeding market expectations.
- This high growth rate was attributed to the recovery of exports and the accelerated implementation of equipment renewal policies.

The carryover of trillions in central government bonds has bolstered infrastructure investment

Contributions to infrastructure investment growth by sector in Q1 2024, %

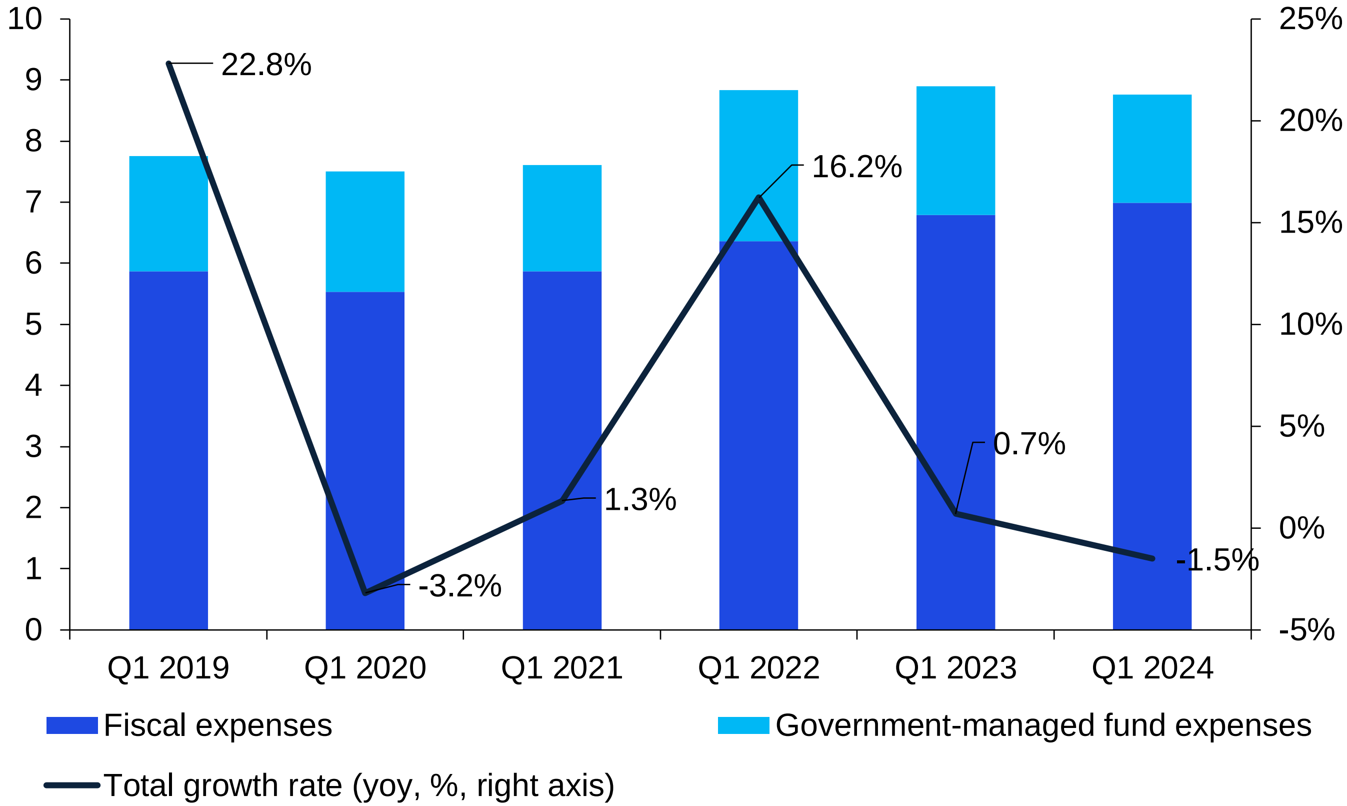
Infrastructure Industry	The share of projects led by the central government	Contributions
Infrastructure	**8%**	***8.8%***
Electricity, heat, gas, and water production and supply	**23%**	***5.8%***
Electricity and heat production and supply	29%	***5.1%***
Gas production and supply	9%	***0.1%***
Water production and supply	1%	***0.4%***
Transportation, warehousing, and postal	**10%**	***2.8%***
Railway transportation industry	50%	***0.7%***
Road transportation industry	2%	***0.9%***
Waterway transportation industry	9%	***0.1%***
Air transportation	1%	***0.3%***
Pipeline transportation	9%	***-0.1%***
Warehousing	2%	***0.4%***
Water conservancy, environmental and public facility management	**2%**	***0.1%***
Water conservancy	2%	***0.9%***
Ecological protection and environmental management	1%	***-0.1%***
Public facility management	2%	***-0.8%***

- Infrastructure investment grew by 8.8% YoY in Q1 2024, an increase of 1.5 percentage points compared to Q4 2023.The growth rate had remained robust with support from the carryover of trillions in central government bonds issued at the end of 2023.
- There was a significant divergence in the performance of central and local infrastructure projects. Projects led by the central government (particularly in electricity and railways) contributed 67% to the growth rate of infrastructure investment. However, due to the limited budget of local governments, municipal projects decreased by 2.4% YoY, dragging the growth rate of infrastructure investment by 0.8 percentage points.

Source: Wind, KPMG analysis
Note: The share of projects led by the central government is calculated based on “Statistical Yearbook of the Chinese Investment Field (2021)”.

Total government expenditure dropped in Q1 2024 due to weak revenue

Government expenses, RMB trillion

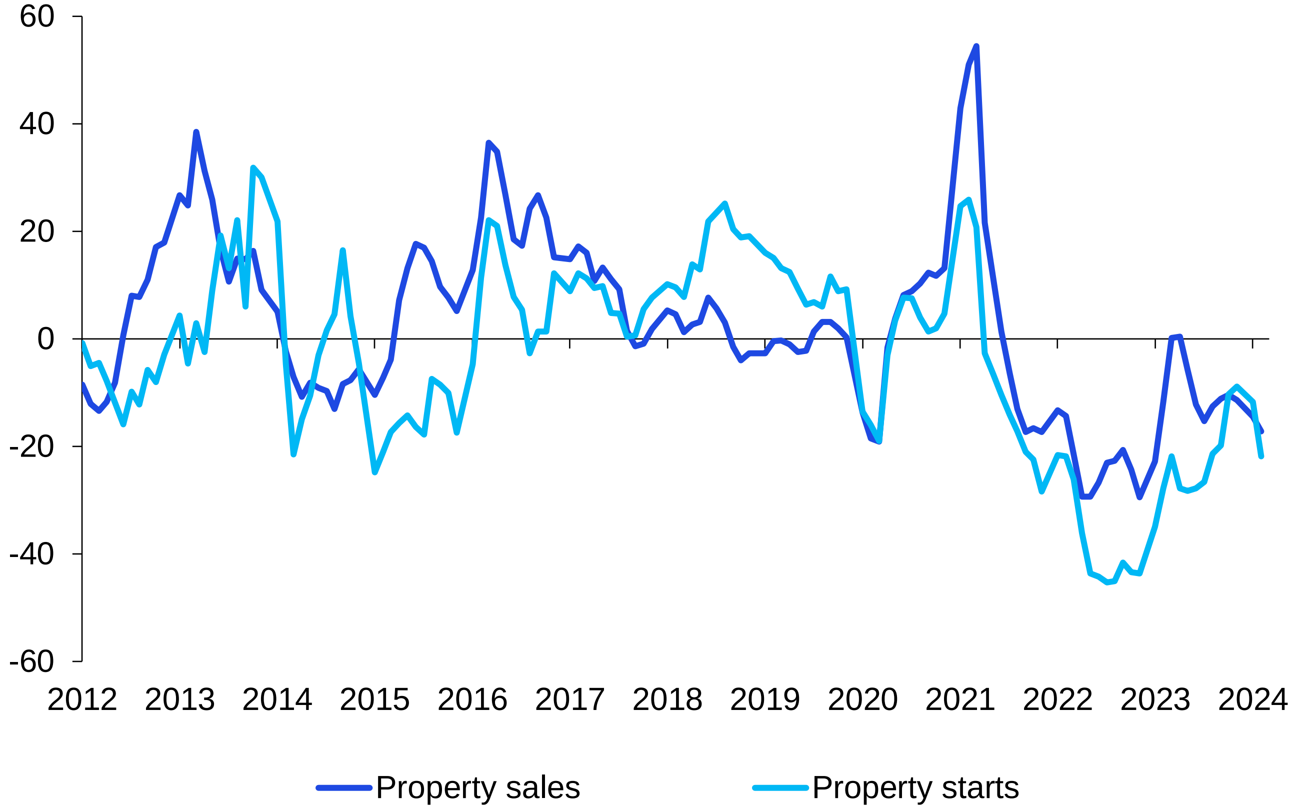


Source: Wind, KPMG analysis

- The growth rate of total fiscal expenditure was -1.5% YoY in Q1 2024, undershooting the budgeted growth rate of 7.9% set at the beginning of the year.
- This slowdown was mainly due to underperforming fiscal revenues, including tax revenue, land transfer income, and government bond issuance.
- Looking forward, the pace of government bond issuance is expected to accelerate to support infrastructure investment in Q2.

Property market activities continued to weaken

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

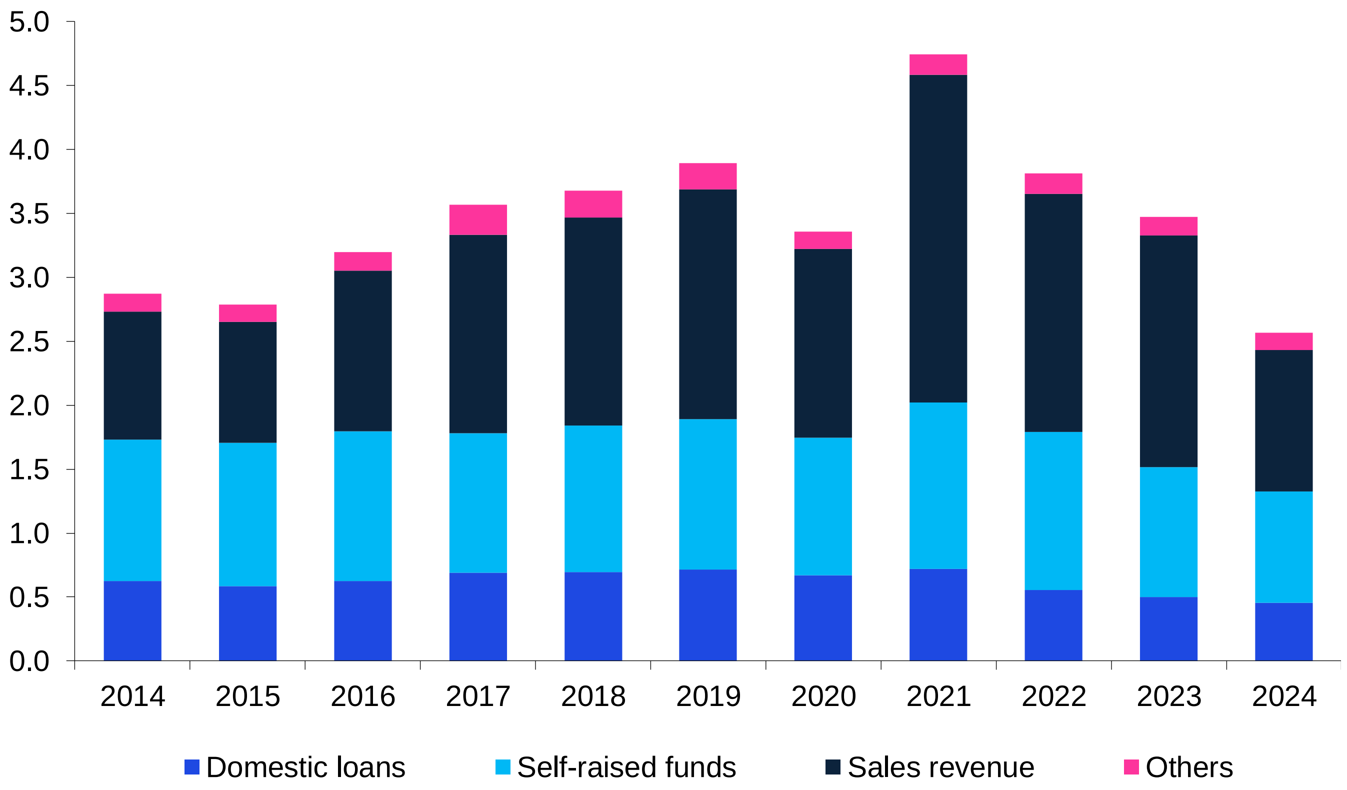


Source: Wind, KPMG analysis

- The YoY decline in property starts widened by 7.4 percentage points compared to the end of 2023, reaching -27.8% in Q1 2024. The effect of the "three major projects" on real estate investment remains to be seen.
- Property developers have adopted a "lower price for higher volume" strategy, yet, property sales remained sluggish. Property sales totalled 2.3 trillion square meters in Q1 2024, marking a YoY decrease from -8.5% in 2023 to -19.4%. Property prices in 70 large cities also decelerated in Q1.
- The recovery of property sales still requires more robust policy efforts on the demand side.

Liquidity pressure for property developers persist

Funding sources of real estate developers in the first quarter each year, RMB trillion

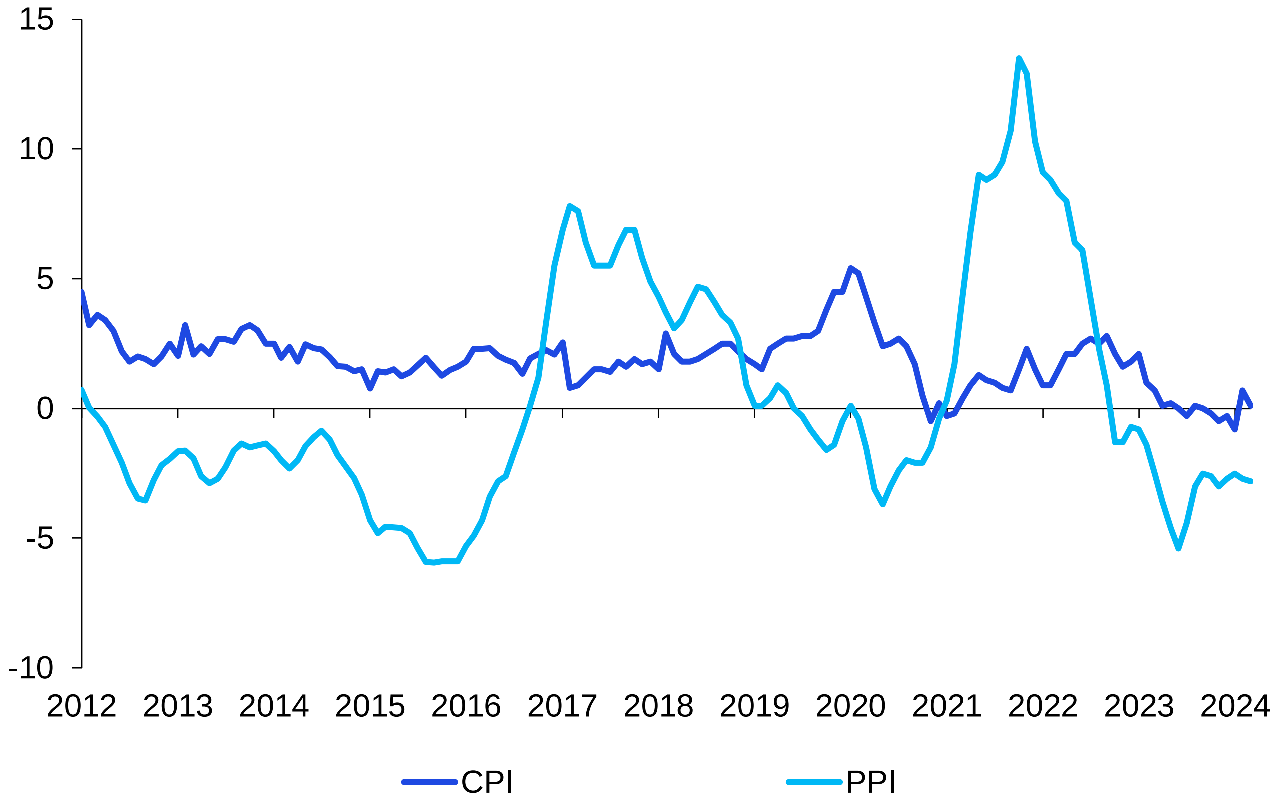


Source: Wind, KPMG analysis

- Funds available to property developers decreased by 26% year-on-year in Q1 2024, with the decline expanding by 13 percentage points compared to 2023. Liquidity pressure for property developers remained tight.
- Sales refunds continued to decline significantly as demand weakened, dragging down the YoY growth of total funds by 20 percentage points.
- By contrast, funding from bank loans has stabilized, with a decline in Q1 of -9.1%, 0.8 percentage points higher than that of last year.

Inflation remained subdued in line with weak demand

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

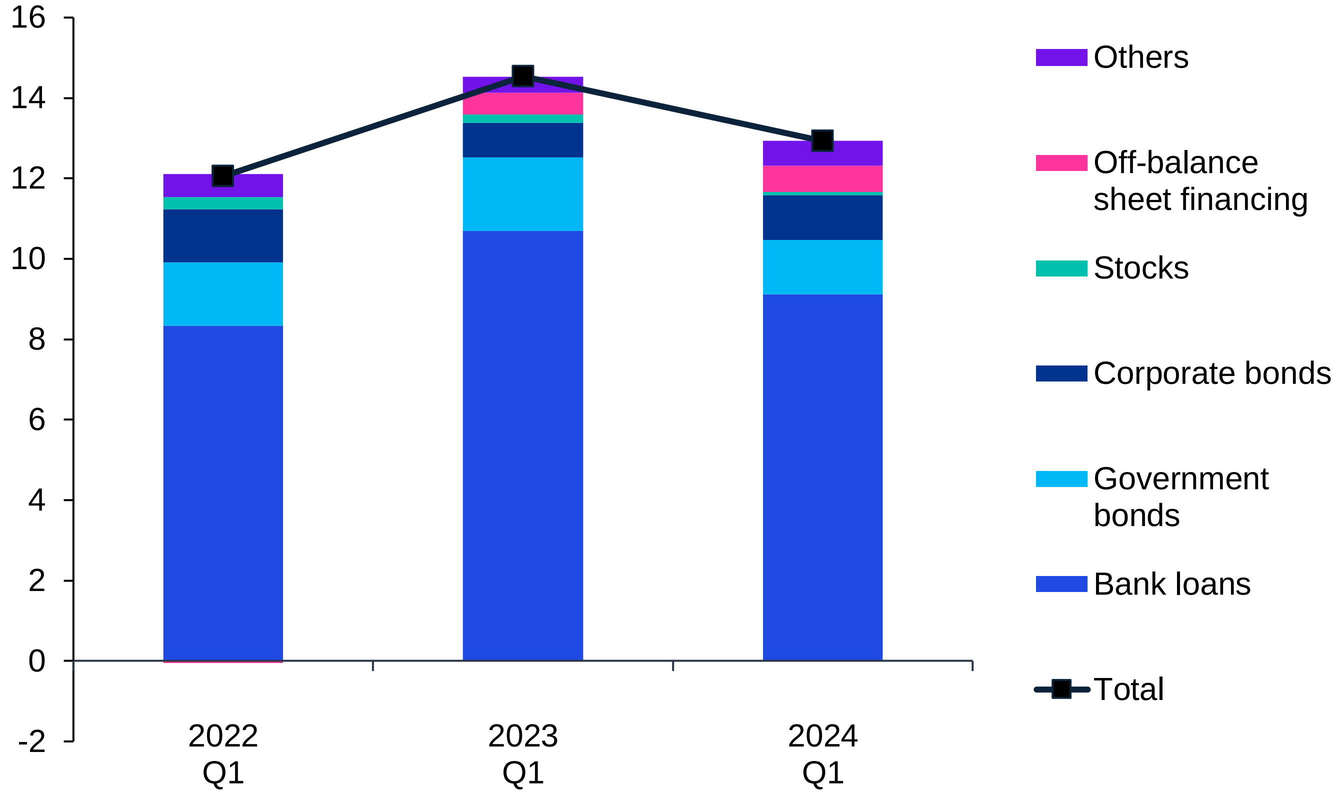


Source: Wind, KPMG analysis

- CPI inflation fell to 0.1% in March 2024, mainly affected by the significant decline in prices of food and travel-related services as demand dropped post Spring Festival.
- The robust growth in manufacturing investment boosted oil and non-ferrous prices. However, due to weak demand, PPI declined to -2.8% in March 2024, 0.1 percentage point lower than that of December 2023.
- Looking ahead, driven by policy efforts and a lower base of last year, a gradual upturn is expected in both the CPI and PPI.

Newly added total social financing reached the second-highest level in history

Growth of total social financing by sector, RMB trillion

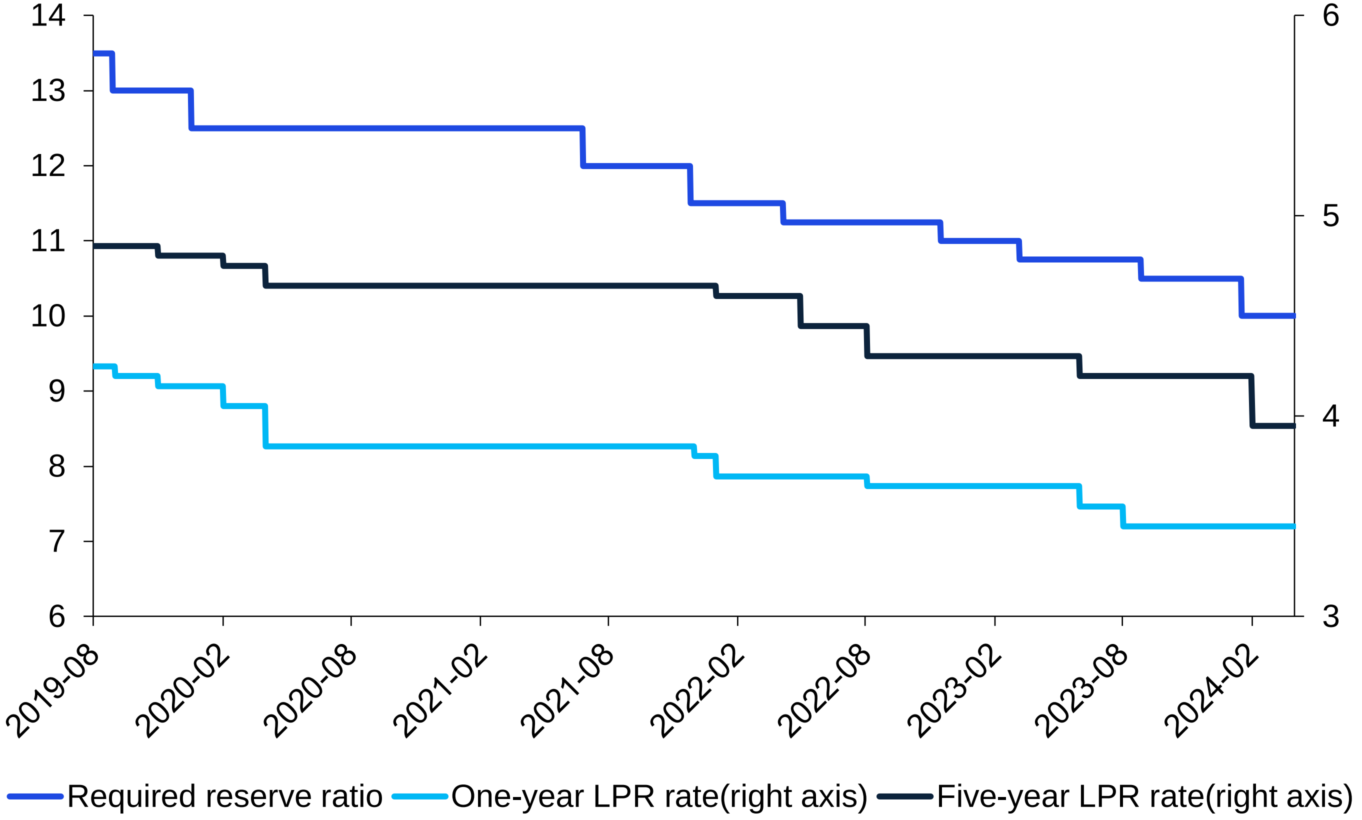


Source: Wind, KPMG analysis

- About RMB 9.1 trillion in new bank loans were issued in Q1 2024, a decrease of 1.6 RMB trillion compared to Q1 2023, due to last year’s high base.
- Net financing of government bonds fell to RMB 1.36 trillion in Q1 2024, a YoY decrease of RMB 470 billion, due to the slow issuance of local government special bonds.
- As the central bank lowered the reserve requirement ratio to release liquidity, and market interest rates were at a low level, the issuance of corporate bonds rebounded to RMB 1.12 trillion in Q1 2024, up RMB 270 billion from Q1 2023.

Prudent monetary policy was implemented in a targeted way

Reserve Requirement Ratio (RRR) and Loan Prime Rate (LPR), %

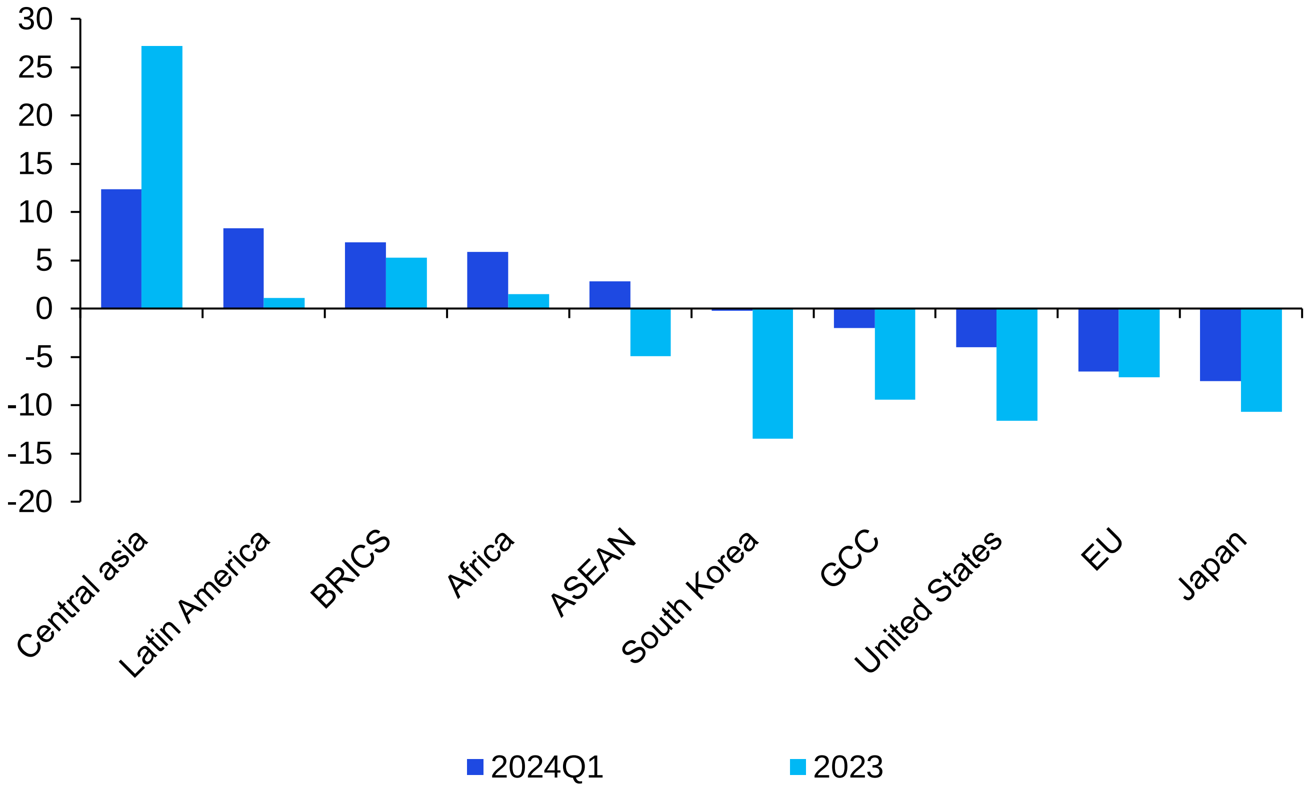


Source: Wind, KPMG analysis

- The reserve requirement ratio was lowered by 50 basis points, releasing more than RMB 1 trillion in liquidity.
- An unexpected cut of 25 basis points in the five-year loan prime rate has driven a steady decline in financing costs, creating a favourable financing environment for businesses.
- Reserve requirement ratio and policy rates are expected to cut with the easing financial conditions globally. Meanwhile, financial support is intensifying in key sectors such as private small and micro enterprises, technological innovation, digital economy, green development, inclusive finance, and infrastructure construction.

China's trade with emerging markets has seen fast growth while trade with advanced economies has recovered slightly

Growth of trade volume between China and major trading partners in Q1 2024 and 2023, YoY, %

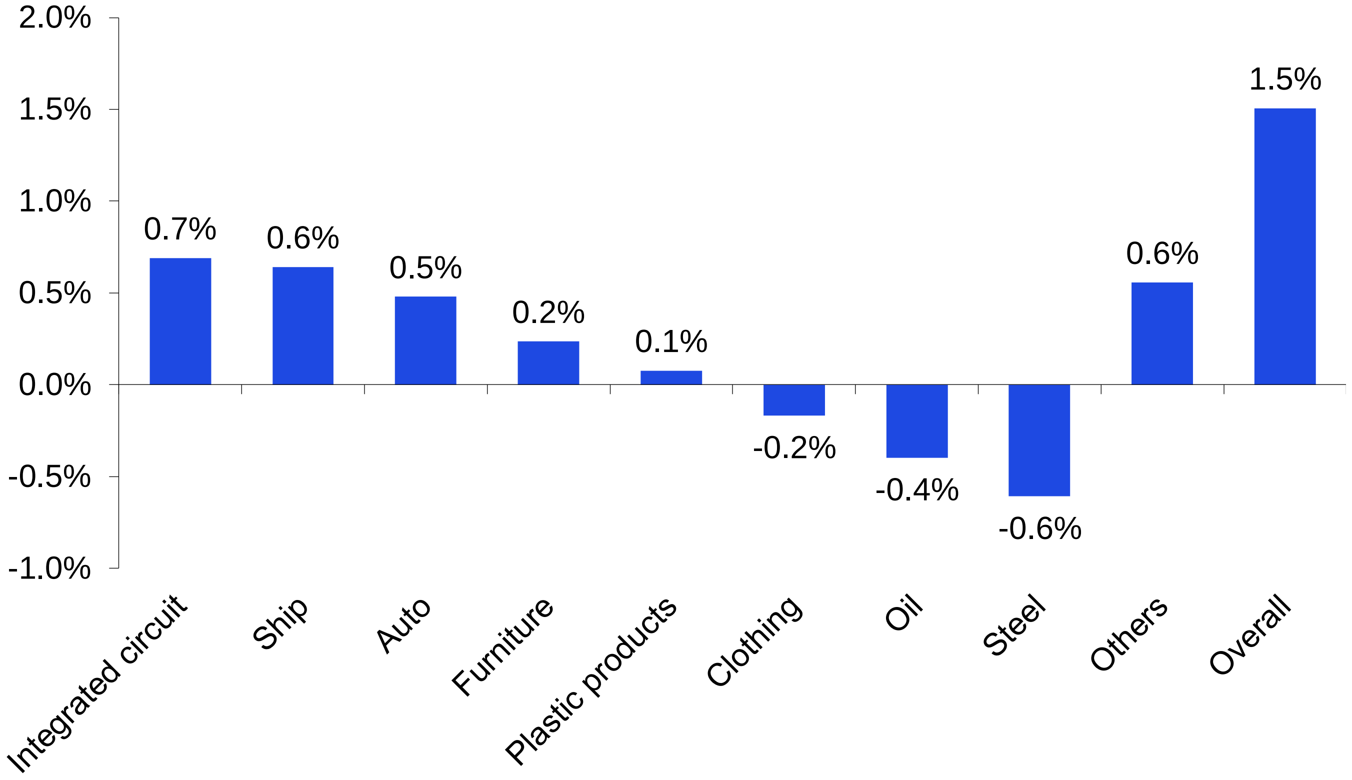


- China's exports rebounded in Q1 2024, with a YoY increase of 1.5%, a significant improvement from -4.7% in 2023.
- China's trade growth rate with "Belt and Road" economies and the BRICS outpaced the overall growth rate of China's trade in Q1 2024.
- ASEAN remains China's largest trading partner, with trade value totalling USD 224.6 billion, a YoY increase of 2.8%.
- China's trade with advanced markets has slightly recovered. Bilateral trade growth between China and the United States improved by 9.1 percentage points compared to the same period last year.

Source: Wind, KPMG analysis
Note: BRICS countries include Russia, Brazil, India, South Africa, Egypt, Iran, Saudi Arabia, United Arab Emirates, and Ethiopia.

Enhancements in the export commodity structure

Contributions to export growth by category in Q1 2024, %

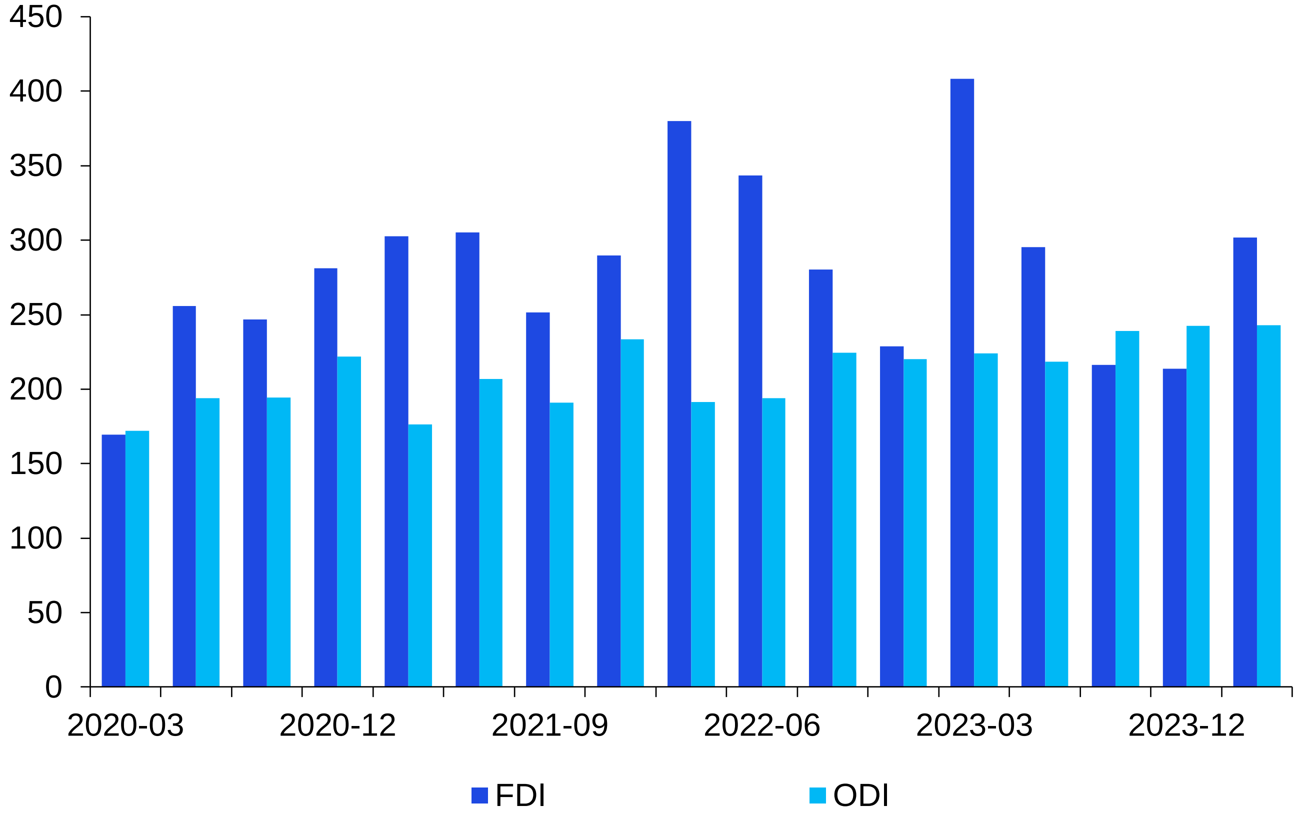


Source: The General Administration of Customs, KPMG analysis

- Mechanical and electrical products accounting for 59.2% in Q1 2024, contributed to the overall export growth rate by 1.1 percentage points.
- The “new trio” (electric vehicles, lithium-ion batteries, and photovoltaic products) remain an important driving force for the development of foreign trade.
- It is worth noting that the export of electric vehicles exceeded $10 billion in Q1 2024, a YoY increase of 18.6%, reaching a record high for the period.
- As production in information technology is gradually recovering, exports of integrated circuits increased by 19.7% YoY in Q1 2024, marking the first positive growth since Q4 2022.

Foreign investment rebounded and outbound investment continued to rise

China's foreign direct investment (FDI) and outbound direct investment (ODI), RMB billion

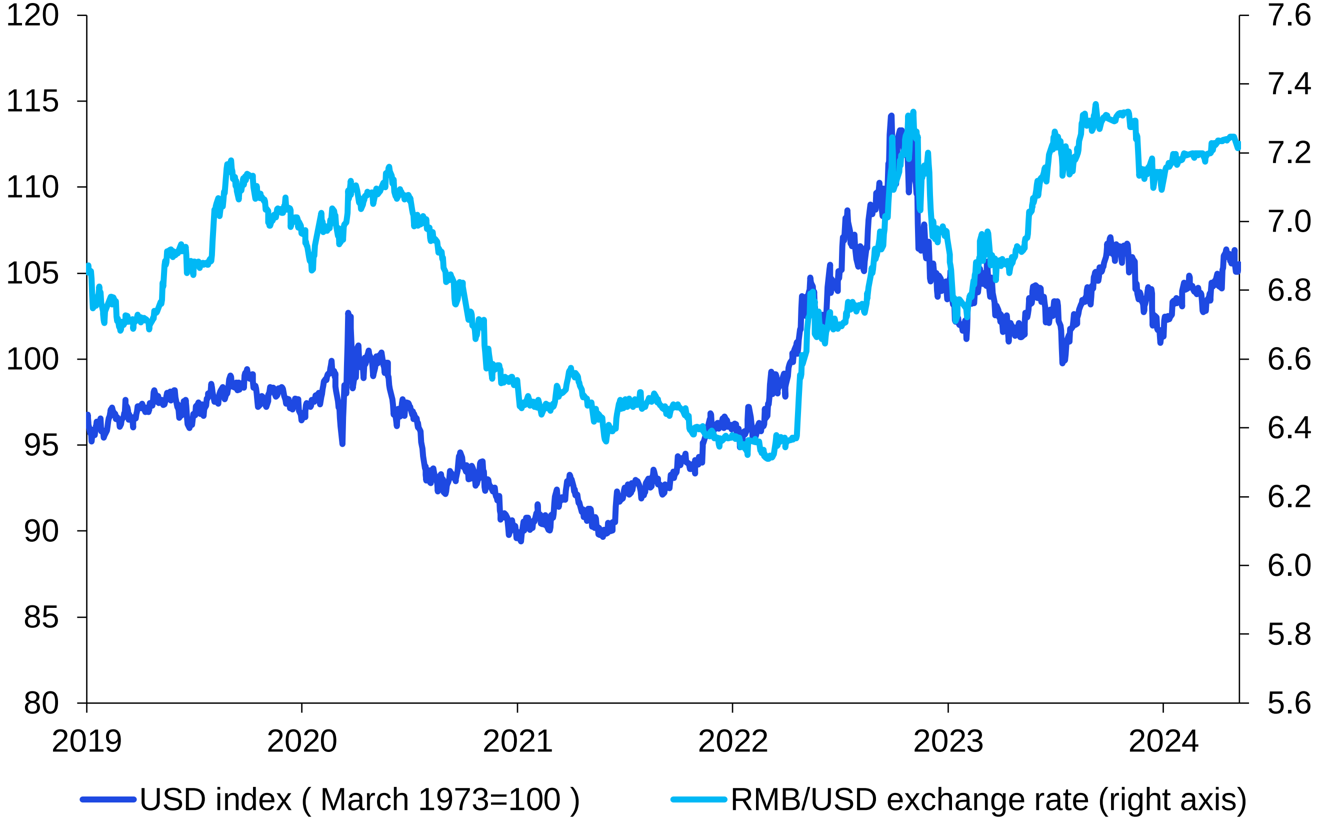


Source: Wind, KPMG analysis

- FDI reached RMB 301.7 billion in Q1 2024, a YoY decrease of 26.1%, but an increase of 41.7% over Q4 2023.
- Investments from Germany and ASEAN to China increased by 48% and 5.8%, respectively. FDI in high-tech manufacturing accounted for 12.5% of the total investments, up 2.2 percentage points from Q1 2023. FDI in the service sector also increased.
- ODI reached RMB 242.9 billion in Q1 2024, a year-on-year increase of 12.5%. Outbound investments in ASEAN and the EU increased significantly by 36.7% and 34.5%, respectively. ODI in "Belt and Road" countries accounted for 22.4% of the total.

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

USD index and RMB/USD exchange rate

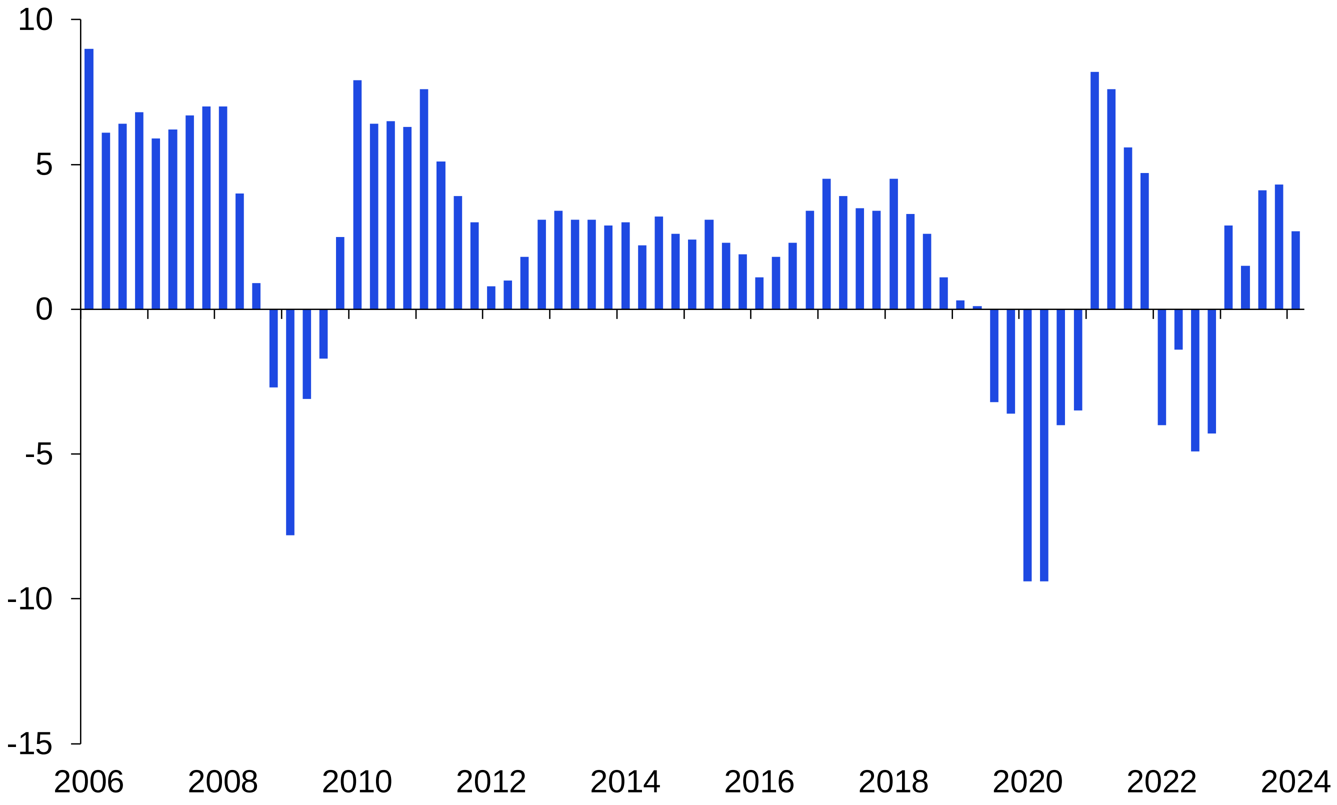


Source: Wind, KPMG analysis

- Thanks to the continuous recovery of China's economy, the RMB exchange rate against a basket of currencies (CFETS) rose to 99.78 at the end of March 2024, an increase of 2.4% compared to the end of 2023.
- Due to resilient inflation, market expectations for Fed rate cuts have fluctuated. The USD index recently reached a 6-month peak of over 106, leading to a slight decline in the RMB/USD exchange.
- As major advanced economies begin to cut policy rates, and China's exports recover, the RMB exchange rate is expected to remain stable in coming months.

Hong Kong's economy is showing stable development

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



Source: Wind, KPMG analysis

- Hong Kong (SAR)'s GDP showed a moderate growth of 2.7% in Q1 2024. Tourists visiting have gradually increased since re-opening, indicating an ongoing recovery of the tourism sector.
- Exports rebounded in March 2024 after a slight decline in February. The labour market reported a low unemployment rate of 3.0% in Q1 2024, thanks to stable economic development.
- Looking ahead, Hong Kong's economy is poised to improve as advanced economies cut interest rates. Tourism will further recover with improvements to related services. Private consumption and total investment will also strengthen with facilitating support from the government.

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