

*Market Monitor – Mainland China*
**Cautious Balance of Economic Growth and Monetary Tightening**

**Pandemic weighs on economic performance in the first quarter**

China's economy grew at a record-breaking 18.3% in Q1 of this year, in a bounce-back from the low base of 2020. Filtering out the base effect, the economy was up 5.0% YoY on average from Q1 2019, which is below the 6.5% growth seen in Q4 2020. On a QoQ basis, the economy grew at 0.6% in Q1 2021, sharply down from a revised 3.2% in Q4 2020. The services sector has borne the brunt of the resurgence of new Covid-19 infections in January and February. This shows that economic recovery has been broadly stable, but is nevertheless susceptible to pandemic-related volatility and the withdrawal of government policy support.

Average yearly growth	Compared to 2020		Compared to 2019	
	1-2/2021	3/2021	1-2/2021	3/2021
Retail Sales	33.8%	34.2%	3.2%	6.5%
Cumulative Investment	35.0%	25.6%	1.7%	2.9%
Industrial Production	35.1%	14.1%	8.1%	6.6%
Exports	60.6%	30.6%	15.2%	10.3%
Imports	22.4%	38.1%	8.3%	16.7%

Sources: National Bureau of Statistics of China, General Administration of Customs of China

**Domestic demand rises in March**

Economic momentum continued to pick up in March, with domestic demand showing a notable recovery. Retail sales grew faster, with a two-year average growth of 6.5% in

❖ **March data shows China's economic momentum continuing to pick up. The government is expected to balance economic growth and stimulus withdrawal cautiously.**

❖ **With the continued surge in home prices, the government will roll out further restrictions in hotspot cities.**

❖ **China's financial markets are supported by strong economic data, but growth is limited by market concern over monetary tightening and US-China tensions.**

## Economic Research

May 2021

March. Although growth has yet to reach the pre-pandemic level of around 8.0%, March's figure is significantly up from the 3.2% growth in the first two months of this year. Movement of people has started to normalise now that the pandemic has subsided, and consumer sentiment is rebounding. Private consumption was boosted by a stable growth of disposable income and a lower survey-based unemployment rate of 5.3%.

Meanwhile, fixed-asset investment growth accelerated to a two-year average growth of 2.9% in Q1 2021, up from 1.7% in the first two months of the year. The major driver is infrastructure investment, including transport and transport equipment. In addition, private investment growth has risen from 0.2% to 1.1%. Business sentiment rebounded as the economic outlook brightened. Firms are opting for longer-term investment, with a faster increase in medium and long-term corporate loans. This also helped the new renminbi bank loans beat market expectation to reach CNY 2.73 trillion in March.

### Illegal real estate financing triggers regulatory concern

A surge in short-term household loans is causing some concern. Households are now finding it harder to obtain mortgages from banks under the central bank's new limitations on loans to the real estate sector. Some may resort to applying for short-term loans to purchase homes. The People's Bank of China (PBOC) and the China Banking and Insurance Regulatory Commission (CBIRC) are therefore requiring banks to investigate operating loan applications more thoroughly. Banks are also required to check for any funds flowing into the real estate sector illegally by end-May 2021.

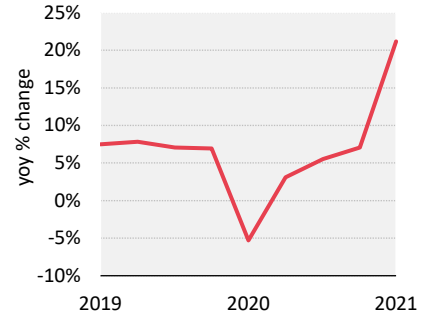
With property market sentiment remaining elevated, home prices continued to grow by 0.5% in March from the previous month, following a 0.6% growth in February. The government has rolled out at least 150 rounds of housing market restrictions since the start of the year, while urging at least 13 cities to stabilise their housing markets. More restrictions and regulations on fund usage are expected. The increase in mortgage rates in various hotspot cities is also expected to help to cool the housing market. Home prices are thus expected to see growth decelerate in the coming months.

### Supply side remains robust

The supply side remained the major driver for economic growth. Industrial production decelerated to a two-year average growth of 6.8% in March, down from 8.1% previously, mainly due to the low base effect from 2020 beginning to fade out. Nevertheless, this growth has still surpassed the pre-pandemic growth of 5.7%. The pickup in domestic demand and robust global demand is supporting industrial production. The official manufacturing purchasing managers' index (PMI) stayed in expansionary territory at 51.1 in April, as did the Caixin manufacturing PMI at 51.9.

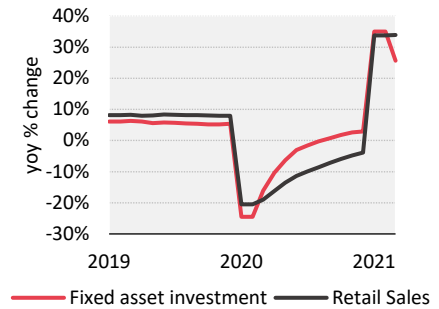
Exports continued to surge at a two-year average growth of 10.3% in March, underpinned by a revival of global demand. Stimulus programmes and gradual global recovery boosted China's exports. At the same time, import growth accelerated from 8.3% to 16.7%. This reflected optimism about domestic and external demand on the part of Chinese firms, which are importing increased amounts of manufacturing material for further production.

### Mainland China GDP Growth



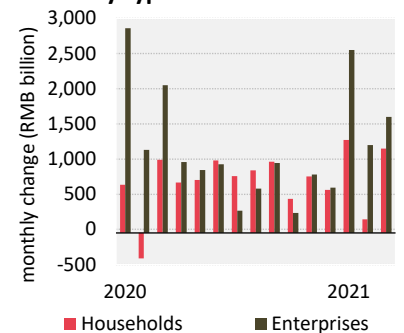
Source: National Bureau of Statistics of China, data as of 28/4/2021

### Cumulative fixed asset investment and retail sales



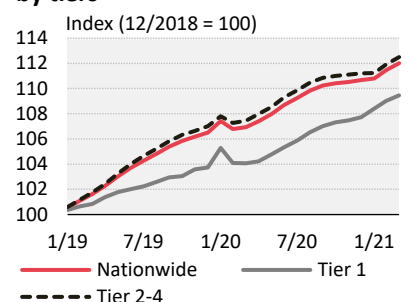
Source: National Bureau of Statistics of China, data as of 28/4/2021

### Loans by types of borrowers



Source: People's Bank of China, data as of 28/4/2021

### New commercial home prices index by tiers



Sources: National Bureau of Statistics of China, BEA Economic Research Department, data as of 28/4/2021

## Economic Research

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### Economic outlook stays positive, as the central bank balances monetary tightening and the need for economic growth

Looking ahead, China is on track for a robust economic recovery. Private consumption will be lifted by improvements in the labour market and the normalisation of social activity. In fact, over the Ching Ming Festival holiday, the number of domestic trips reached 94.5% of the pre-pandemic level. At the same time, public investment is expected to be supported by the infrastructure-related policies under the 14th Five-Year Plan. The Ministry of Finance approved the quota of local government special bonds in advance in early March, allowing local governments to start investing in various infrastructure earlier. In addition, exports are expected to stay robust, thanks to the global economic recovery.

As the economy showed strong growth in Q1, the PBOC is likely to gradually withdraw its monetary stimulus to control financial risks and deleverage. However, the pace is expected to be moderate in view of the recent bond defaults, such as China Fortune Land Development. According to Bloomberg, the defaulted amount of onshore and offshore bonds issued by Chinese firms reached USD 15.1 billion in Q1, the highest level since Bloomberg started tracking data. The PBOC also expressed concern over the risk of default by highly leveraged small and medium-sized developers. Moreover, some industries and private firms still require monetary support. The PBOC is expected to cautiously balance the withdrawal of monetary stimulus and economic development.

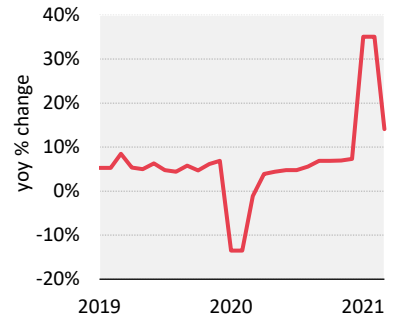
### Robust economic data spurs the market, but concern remains over monetary tightening and US-China tensions

In the stock market, A-shares have risen slightly by 0.1% in April. Several factors weighed on the stock market, including the US government's blacklisting of seven Chinese super-computer firms, the proposal by a US Senate committee for a "Strategic Competition Act of 2021" to counteract China, and market concern over monetary tightening. However, the stable 1-year loan prime rate of 3.85% gave investors some confidence.

In the foreign exchange market, the CNY appreciated by 1.2% against the US dollar in April, while the CNH rose by 1.4%. The US dollar weakened, with a 2.1% drop in the US dollar index as the Federal Reserve repeated that it would maintain loose monetary policy and as US government bond yields ebbed. Although the weak US dollar and China's strong economic data supported the renminbi, its appreciation was limited by US-China tensions.

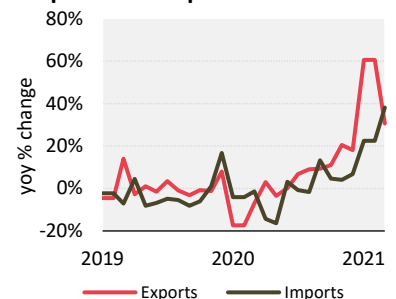
Looking ahead, China's resilient economic fundamentals will provide support to the financial markets. However, signs of the PBOC's tightening of monetary policy may trigger further market concern. The US-China dispute is expected to linger and will dampen investor confidence. In addition, the trend of the US dollar will dictate that of the renminbi. With a brighter economic outlook for the US and a resurgence of new infections in countries such as India and Japan, investor demand for the US dollar may increase, which would weigh on the renminbi's performance.

#### Industrial Production



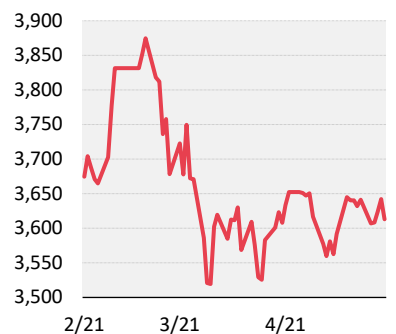
Source: National Bureau of Statistics of China, data as of 28/4/2021

#### Imports and Exports



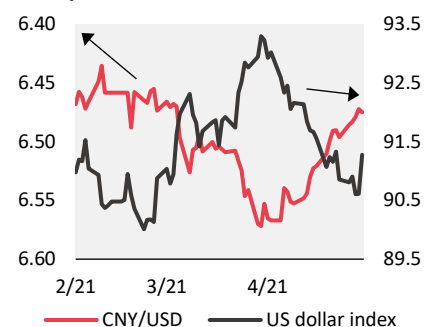
Note: Figures for January and February are the average growth of the two months.  
Source: General Administration of Customs, data as of 28/4/2021

#### A Share Index



Source: Bloomberg, data as of 30/4/2021

#### RMB/USD vs USD Index



Source: People's Bank of China, Bloomberg, data as of 30/4/2021

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