BNY
iFlow
MACRO MORNING BRIEFING

June 20, 2024

China Growth Sentiment Weakening

China's May data overall shows signs of slowing in investment, and in momentum of the wider recovery. Retail sales managed to stay resilient, but we would not construe that as 'strong'. Consumer spending arguably appears in a fragile state, with consumer goods retail trade growing at 3.6% y/y or 3.5% ytd y/y and auto sales languishing at 0.2% ytd y/y.

Activity and investment data is losing momentum after a strong Q1. Fixed-asset investment came in at 4.0% ytd y/y (April: 4.2%) and infrastructure investment at 5.7% ytd y/y (April: 6.0%). The top destinations of investment were railways, shipping, aerospace and other transport equipment, at 34.7% ytd y/y. We note that the main contributors were state-owned enterprises, at 7.4% ytd y/y. Private investment growth flattened out at 0.1% ytd y/y.

Industrial Production (IP) ticked down to 6.2% ytd y/y after a small rebound to 6.3% ytd y/y in April. The slowdown in IP was driven by electricity production, which eased to 4.3% y/y (April: 5.8%) or to 6.2% ytd y/y. Manufacturing softened to 6.0% y/y (April: 7.5%) or to 6.7% ytd y/y, but high-tech manufacturing remained strong at 10% y/y, 8.7% ytd y/y. By product type, production of integrated circuits and new energy automobiles continues to enjoy strong growth rates, at 33.6% y/y (33.9% ytd y/y) and 17.3% y/y (32.7% ytd y/y), respectively. Production of industrial robots grew 8.9% ytd y/y.

In the real estate sector, property investment contracted 10.1% y/y. Housing and real estate are still the main drags, with newly started residential construction at 217mn sqm (-25% ytd y/y), residential sales at 307mn sqm (-23.6% ytd y/y), and a further rise in residential housing inventories to 387mn sqm or +24.6% y/y.

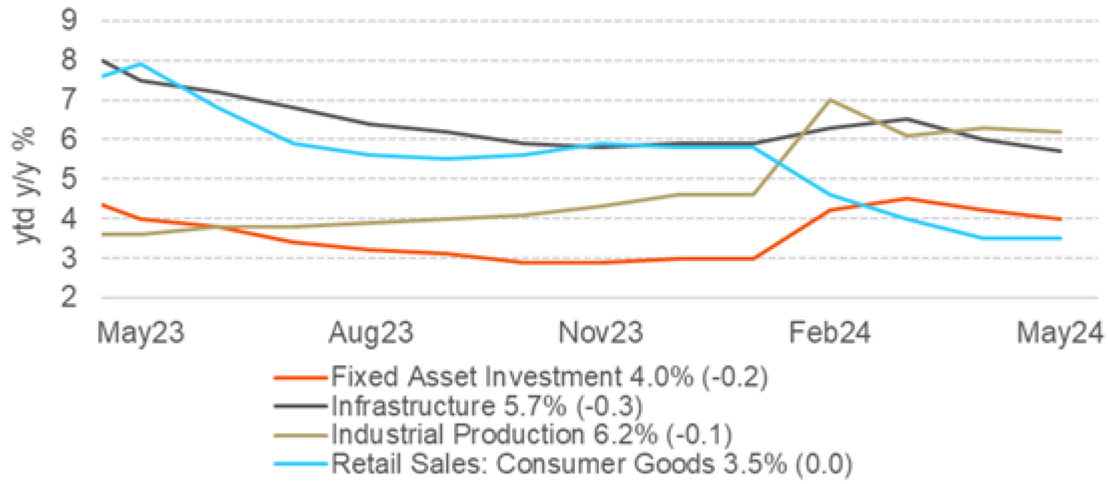
Sluggish activity and investment might also be related to the dysfunctional credit transmission mechanism, with excess liquidity used to repay debt rather than for investment purposes. The no-end-in-sight slide in credit data is an increasingly worrying sign to us.

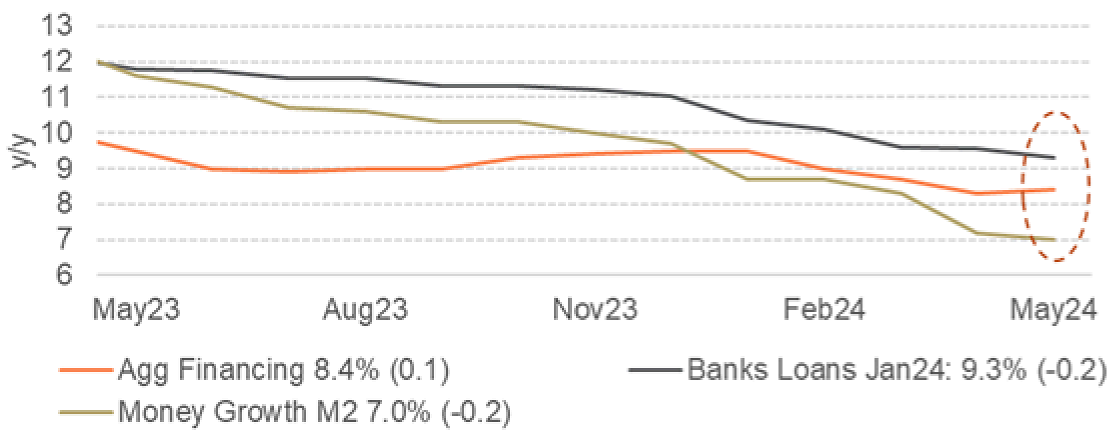
The uptick in aggregate financing in May, +0.1 to 8.4% y/y, offers little comfort for stabilisation, as the bulk of the credit growth was due to government bond issuance. Indeed, loans by financial institutions and RMB-loans within aggregate financing both slowed to new lows, 9.3% y/y (April: 9.6%) and 8.9% y/y (April: 9.1%), respectively. This suggests more effort and policy stimulus are needed to ensure normalisation of the corporate credit market.

Our overall takeaway from the macro releases: sentiment is weakening. This dovetails with manufacturing PMI unexpectedly falling into the contraction zone recently. What's more, slow retail sales growth doesn’t lend much support to the prospect of China putting the disinflation threat behind. May headline CPI was steady at 0.3% y/y, but core inflation drifted marginally lower, to 0.6% y/y. Indeed, this is echoed by China's National Bureau of Statistics, which in a press release added and emphasized that “...effective demands remain insufficient at home...” on top of the "complex and severe" external environment.

More easing could be expected in the near term, as indicated by PBoC Governor Pan at the Lujiazui Forum in Shanghai this week. He committed to strengthening counter- and cross-cyclical policies and signaled adding China government bond trading to the PBoC's toolkit.

Exhibit #1: China Recovery Momentum Slowed





Source: BNY, Bloomberg L.P.

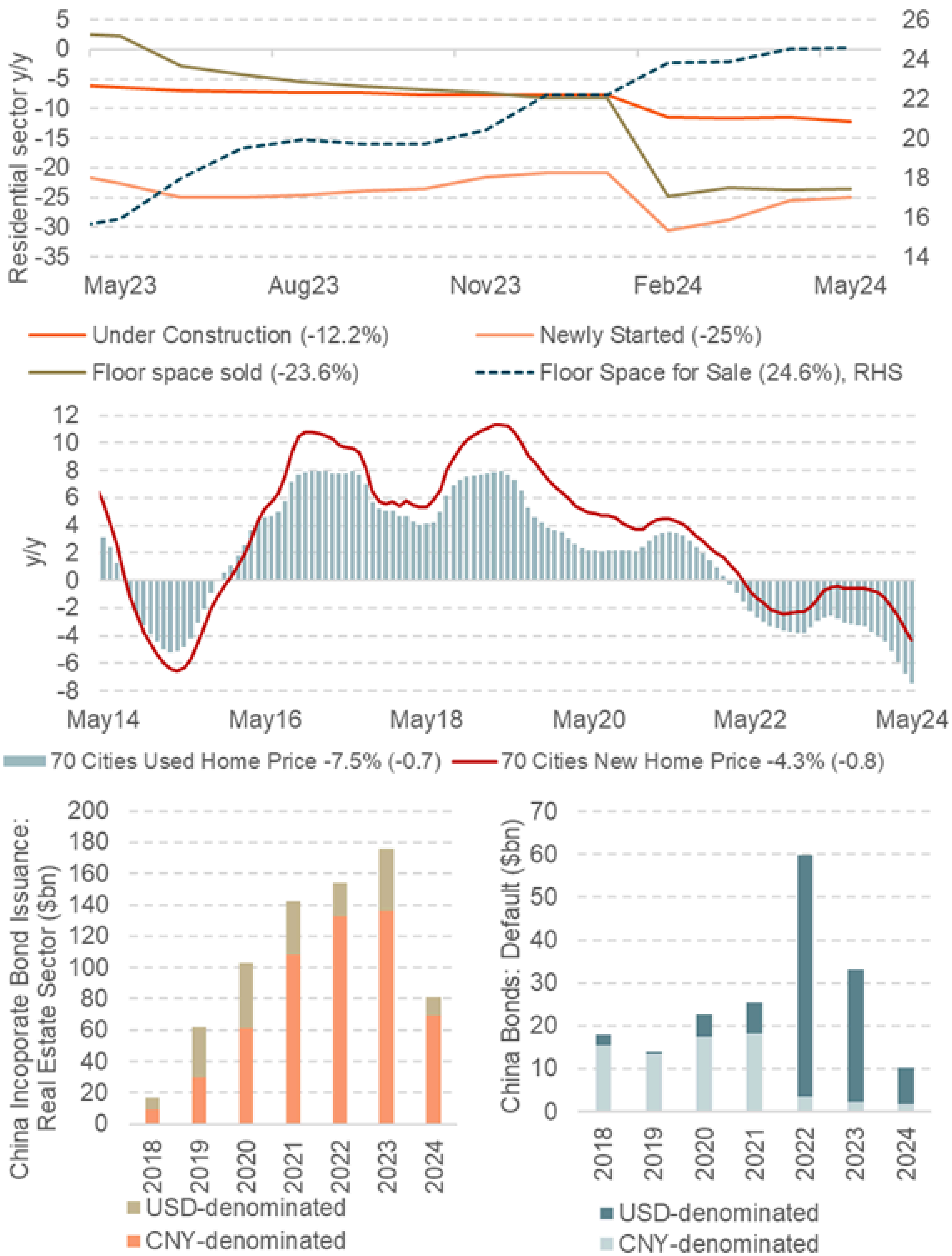
The drag in the housing sector is one of the top concerns in China. The accelerating drop in house prices has caught much market attention in the context of the multiple measures, such as cutting minimum mortgage rates, enabling state-owned enterprises to buy unsold flats, and an additional CNY 300bn funding via PSL, announced in May.

May house prices statistics look ugly. Used home prices m/m were down in all 70 cities – and for the fifth consecutive month on a y/y basis. The drop in the average for 70 cities' new and used residential house prices accelerated to -0.71% m/m and -1.0% m/m, respectively, or -4.3% y/y and -7.5% y/y, respectively.

That said, we think it's too early to write off the impact from policy measures; more time is needed to allow those to filter through. There had been anecdotal evidence of stabilisation in sentiment and a pick-up in transactions across various cities in China (see here).

Demand for homes is intertwined with the recovery of real estate developers. Instances of default in China corporate bonds have calmed down somewhat, at $10.6bn so far this year compared with $60.6bn in 2022 and $33.6 in 2023. Normalisation of corporate funding markets plays a vital role in addressing the near-term refinancing needs in the sector.

Exhibit #2: China Real Estate Sector Shows Little Sign Of Recovery



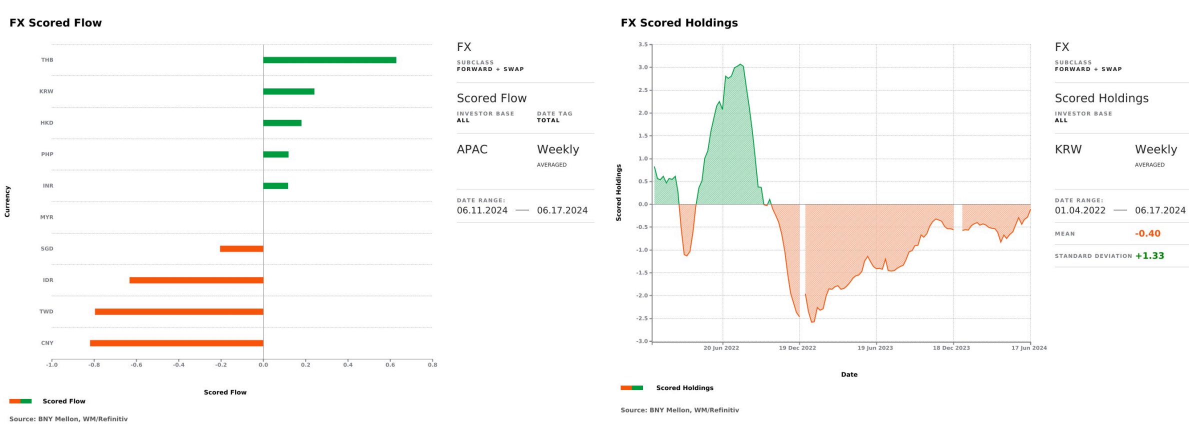
Source: BNY, Bloomberg L.P.

Weakening market sentiment around European politics and weak China data combined to prompt broad-based unwinding of risk exposures last week. iFlow data shows outflows from currencies across regions globally, as well as selling of equities and sovereign bonds.

APAC currency flows were dominated by outflows from CNY, TWD and IDR: all had weekly average scored flows to the left of -0.6. On the other side of the ledger, THB enjoyed weekly inflows after a month of selling and KRW buying continued for a ninth week. KRW scored holdings have narrowed substantially, from -0.9 in early April to near neutral this week. CNY scored holdings, by contrast, drifted lower to the most underheld of the year. IDR, being overheld and unprofitable, appears susceptible to a further positioning unwind, in our view.

In term of asset flows, sentiment towards China remains weak: accelerated selling in equities and acute selling pressure in corporate bonds. China sovereign bond outflows eased, however. A notable observation elsewhere is more buying of South Korea equities: 1.75 weekly average scored flows, the most within the iFlow universe. Among APAC sovereign bonds, India's were the only one with inflows; index inclusion starts at end-June.

Exhibit #3: CNY, TWD, IDR Outflows; KRW Scored Holdings Near Neutral



Source: BNY, Bloomberg L.P.

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Please direct questions or comments to: iFlow@BNYMellon.com

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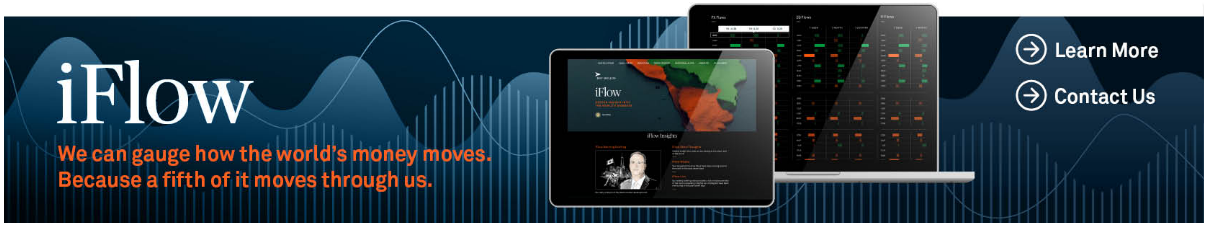

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