

China Economy in 3Q20

Service sector took longer to recover

China's 3Q GDP growth of 4.9% came in line with our expectation (5.0%). Growth during the first three quarters turned positive to 0.7% YoY from -1.6% in 1H20. Pace of recovery still varied across sectors and industries. While growth of the primary and secondary sector has almost rebounded to pre-pandemic levels, that of the service sector fell short and may take longer to get back normal. Nonetheless, sequential improvement was broadly observed in both supply and demand. Job market continued to tighten, with unemployment rate edging down and leading indicators trending up steadily.

- **Industrial output accelerated to expand 6.9% YoY in Sep**, boosted not only by sustained satisfactory performance of high-tech industries (+7.8%) but also by robust recovery of traditional industries. All of the 17 major manufacturing industries reported speedier growth or narrowing decline in 9M20 compared to 8M20. Fastest recovering industries include automobile, electrical machinery, general-purpose machinery, and computers, communication & electronic equipment.
- **Urban FAI advanced 0.8% YoY in 9M20**, the first positive growth since this year. **1) Manufacturing FAI** narrowed its decline to 6.5% in 9M20, with investments of pharmaceuticals and computers, communication & electronic equipment industries outpacing others at 21.2% and 11.7% YoY. **2) Infrastructure FAI** turned positive growth at 0.2% YoY in 9M20. However, monthly growth seemed to be cooling down partly due to last year's high base, increasing 3.2% YoY in Sep vs. 4.0% in Aug. Komtrax data also showed that hours of machine use inched down a bit in Sep. **3) Real estate investment speeded up to increase 5.6% YoY in 9M20**. Resilient growth was attributable to both construction spending and land acquisition expenditures.
- **Retail sales +3.3% in Sep, driven by booming demand before and during the Oct 1 holiday**. Catering sector warmed up, +1.9% for the above-designated-size sample, marking the first positive growth since COVID-19. For the full sample, catering also narrowed decline from 7% in Aug to 2.9% in Sep. Momentum of strong car sales lasted into Sep, +11.2% in retail value. Excluding car sales, retail sales growth was 2.4% YoY in Sep.
- **Risks. 1)** When winter approaches, infrastructure spending and construction activities may decelerate; **2)** Urban residents, who contribute to the majority of consumption spending, experienced 0.3% decline of real disposable income in 9M20, lagging GDP growth and income growth of rural residents. Such lacklustre income growth is likely to weigh on consumption recovery.

Data Summary

YoY growth (%)	May-20	Jun-20	1H20	Jul-20	Aug-20	Sep-20
Industrial value-added	4.4	4.8	-1.3	4.8	5.6	6.9
FAI, YTD	-6.3	-3.1	-3.1	-1.6	-0.3	0.8
- Manufacturing FAI	-14.8	-11.7	-11.7	-10.2	-8.1	-6.5
- Real estate FAI	-0.3	1.9	1.9	3.4	4.6	5.6
- Infrastructure FAI	-6.3	-2.7	-2.7	-1.0	-0.3	0.2
Retail sales value	-2.8	-1.8	-11.4	-1.1	0.5	3.3

Source: NBS, CMBIS

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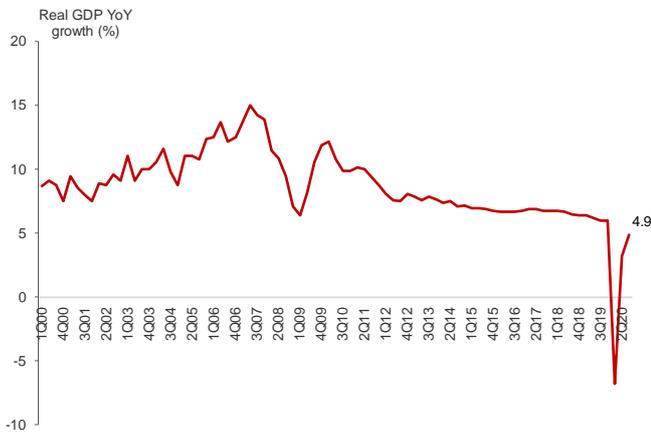
GDP and income growth

■ 3Q GDP growth in line; tertiary sector rebound may take longer

China recorded 4.9% GDP growth in 3Q20, which was 0.1ppt/0.3ppt lower than our/consensus forecast. Growth during the first three quarters turned positive to 0.7% YoY from -1.6% in 1H20, whereas growth by quarter was -6.8%/+3.2%/+4.9% in 1Q/2Q/3Q.

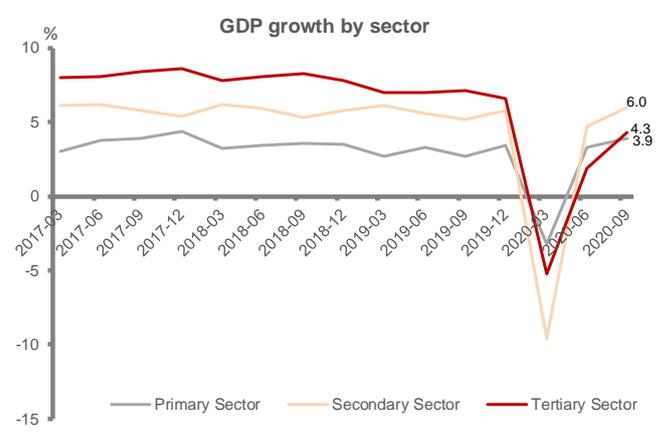
Primary/secondary/tertiary sector reported 3.9/4.3/6.0% YoY growth in 3Q20, respectively, representing sequential improvement from 2Q20. While the primary and secondary sectors have largely rebounded close to pre-pandemic levels, growth in tertiary sector, at 4.3% YoY in 3Q20, was short of pre-pandemic level by at least 2ppt. Despite this, evidence was solid regarding sequential improvement and positive outlook of the tertiary sector, judging from leading indicators. Among the industries, information transmission, software & IT services and the finance industry documented 15.9%/7.0% YoY growth in 9M20, speeding up 1.4/0.4ppt from 1H20.

Figure 1: GDP growth recorded 4.9% YoY in 3Q20



Source: NBS, Wind, CMBIS

Figure 2: GDP growth by sector

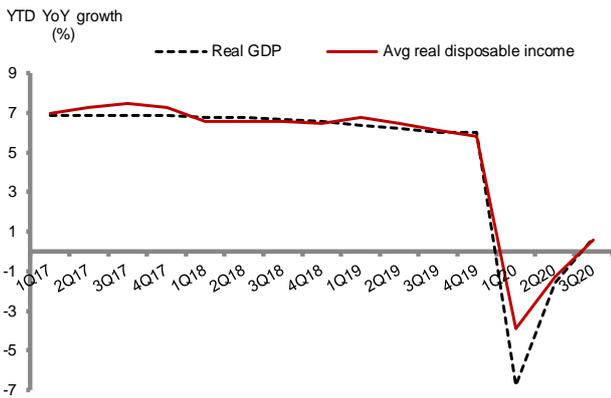


Source: NBS, Wind, CMBIS

■ Income growth reversed decline, but that of urban residents missed

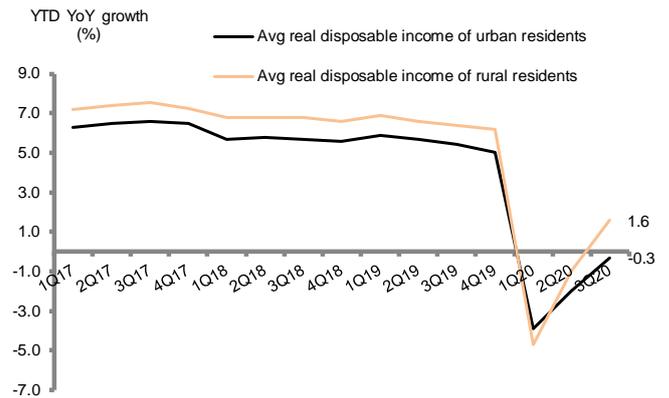
Real disposable income largely tracked the trend of GDP growth, increasing 0.6% YoY in the first three quarters, reversing its decline of 1.3% in 1H20. However, income growth of urban residents remained in negative spectrum, declining 0.3% YoY in 9M20 (rural residents +1.6%). Since urban residents contributed to the majority of consumption expenditure in China, lackluster income growth of the urban population would continue posing risks to consumption recovery.

Figure 3: Real disposable income +0.6% in 9M20



Source: NBS, Wind, CMBIS

Figure 4: Disposable income, urban vs. rural



Source: NBS, Wind, CMBIS

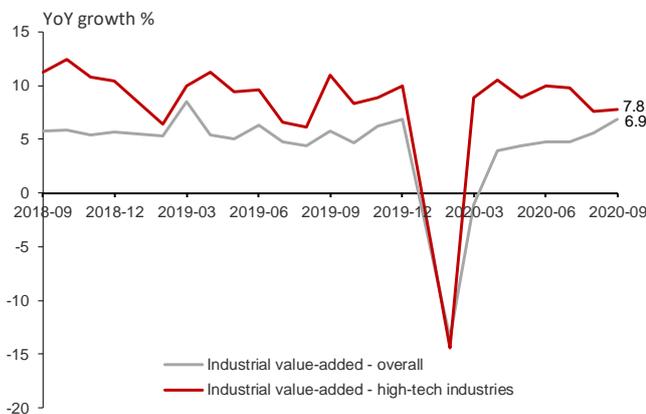
Industrial output growth accelerated

Growth of industrial value-added accelerated to 6.9% YoY in Sep, boosted not only by sustained satisfactory performance of high-tech industries (+7.8%) but also by robust recovery of traditional manufacturing industries.

Figure 7 plotted output growth of the 17 major industries in 8M20 vs. in 9M20. Encouragingly, all the 17 industries posted better output performance in 9M20, either accelerating YTD growth or narrowing YTD decline compared to 8M20. This is a result of resuming demand from both domestic and overseas markets.

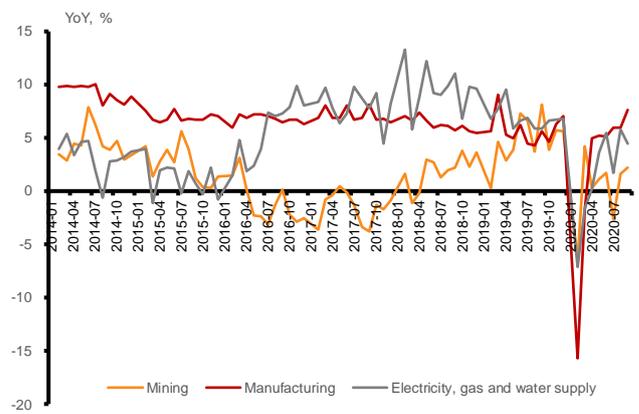
Industries worth noting are 1) automobile, of which output growth speeded up to +4.4% in 9M20 driven by domestic demand and recovery of global auto market (export of auto parts also increased strongly in Sep). Production of NEVs increased 51.1% YoY; 2) electrical machinery and general-purpose machinery, of which output advanced 5.6% and 2.6% YoY in 9M20; 3) computers, communication and electronic equipment, which maintained robust growth at 7.2% YoY in 9M20, contributed by work-at-home demand for digital appliances and an upward product cycle of consumer electronics.

Figure 5: Industrial value-added +6.9% YoY in Aug



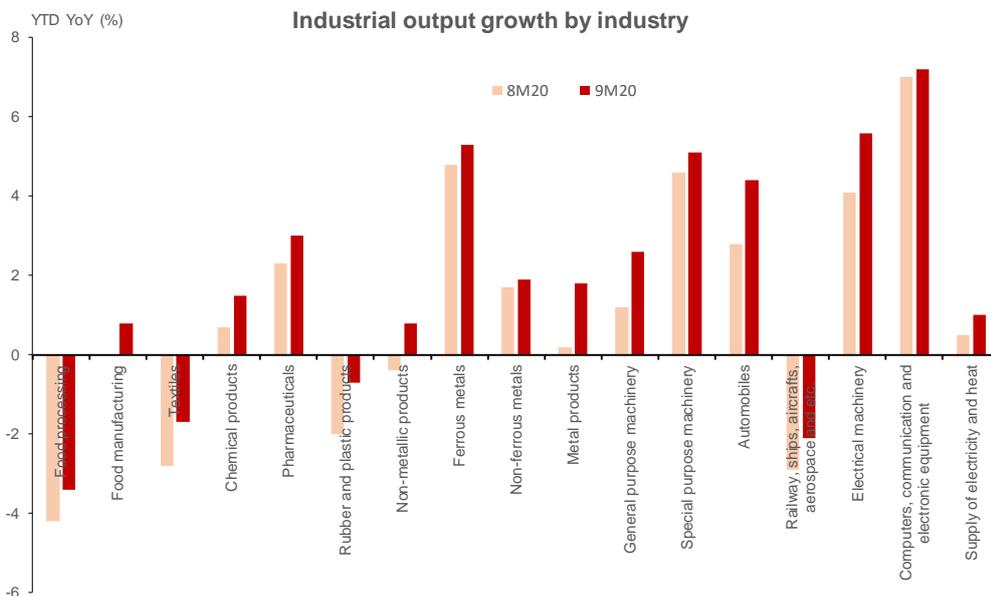
Source: NBS, Wind, CMBIS

Figure 6: Industrial value-added growth by sector



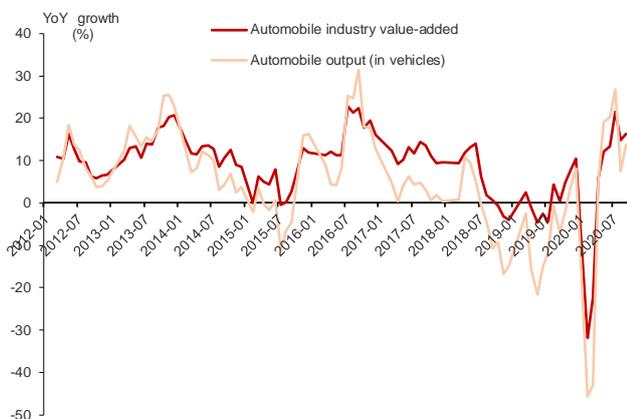
Source: NBS, Wind, CMBIS

Figure 7: Major industries recorded improving output growth in 9M20 vs. 8M20



Source: NBS, Wind, CMBIS

Figure 8: Strong momentum of automobile industry continued

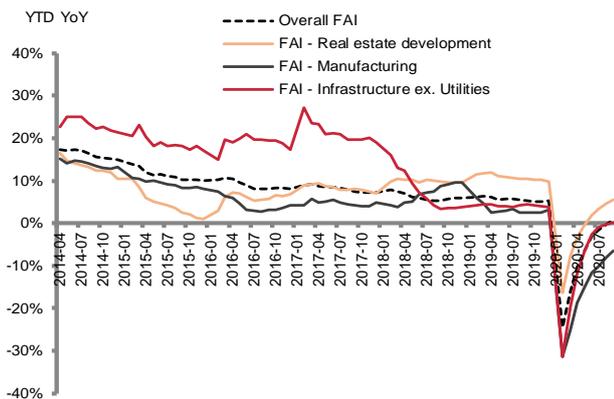


Source: NBS, Wind, CMBIS

FAI growth turned positive

Urban FAI advanced 0.8% YoY in 9M20, the first positive growth since this year. Manufacturing FAI declined 6.5%, infrastructure FAI increased 0.2% and real estate investment rose 5.6% in 9M20.

Figure 9: Urban FAI growth turned positive +0.8% in 9M20 vs. -0.3% in 8M20

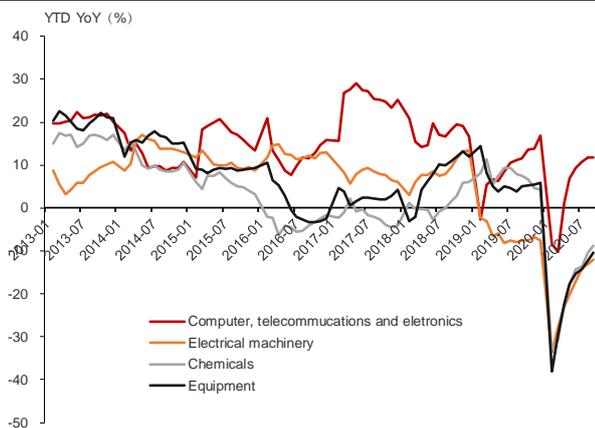


Source: NBS, Wind, CMBIS

Manufacturing FAI -6.5% in 9M20s

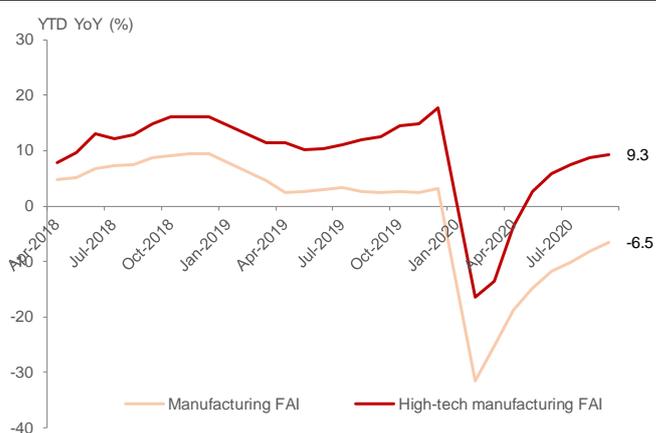
The majority of manufacturing industries still experienced decline in FAI in 9M20, although the declines have been narrowing month over month. Only a few particular industries expanded investments, including 1) pharmaceuticals (FAI +21.2%, much faster than pre-pandemic investment growth), and 2) computers, communication and electronic equipment (FAI +11.7%, close to pre-pandemic level).

Figure 10: FAI by manufacturing industries



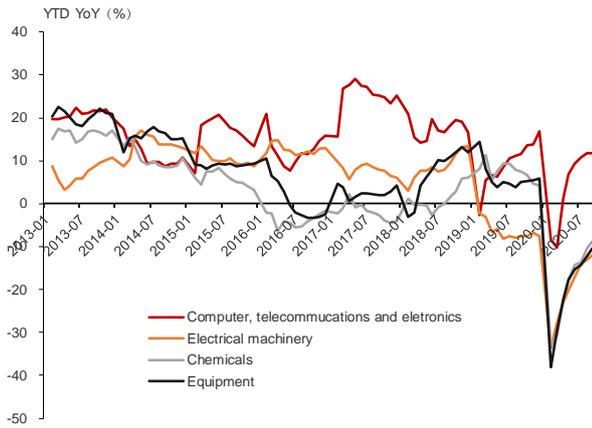
Source: NBS, Wind, CMBIS

Figure 11: High-tech manufacturing FAI +9.3% in 9M20



Source: NBS, Wind, CMBIS

Figure 12: FAI of key manufacturing industries

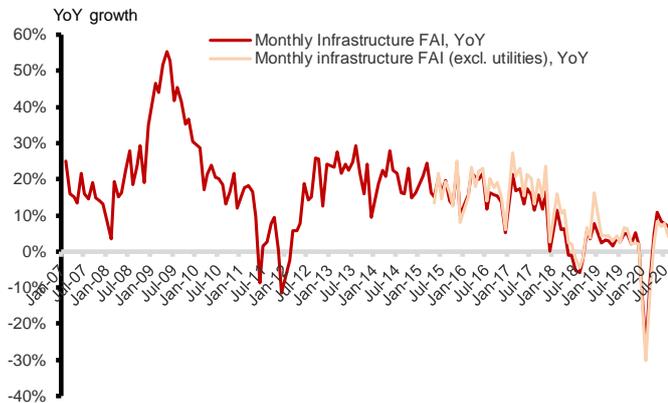


Source: NBS, Wind, CMBIS

■ **Infrastructure FAI +0.2% in 9M20, vs. -0.3% in 8M20**

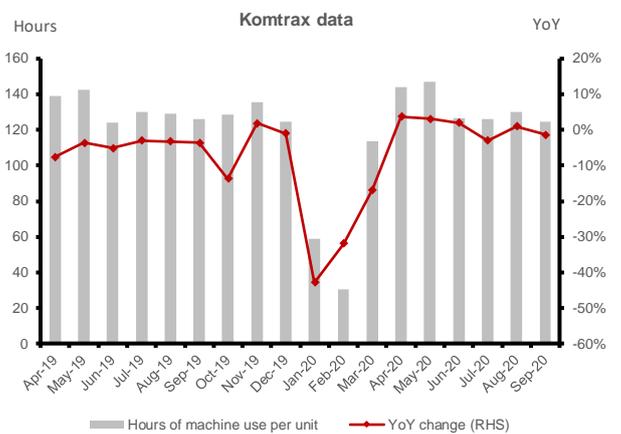
Although YTD change turned positive, monthly growth seems to be cooling down since 3Q partly due to last year’s high base. Based on our calculation, monthly infrastructure FAI decelerated to 3.2% YoY in Sep, from 4.0% in Aug. Komtrax data suggested that hours of machine use per unit decreased 1.3% YoY and 4.3% MoM in Sep. When winter approaches, we think infrastructure spending and construction activities may face deceleration risks under freezing conditions.

Figure 13: Monthly infrastructure FAI growth slowed down in Sep partly due to last year’s high base



Source: NBS, Wind, CMBIS estimates

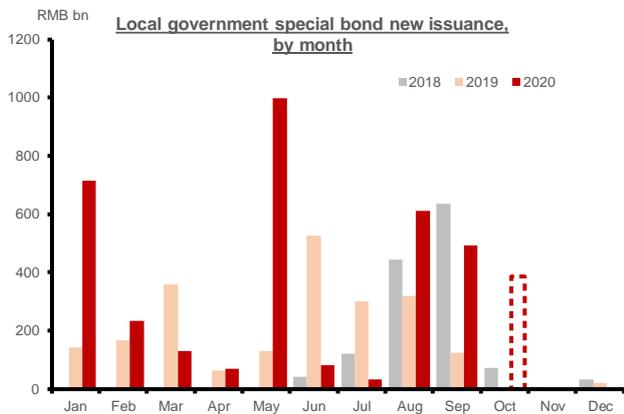
Figure 14: Komtrax data – hours of machine use per unit decreased 1.3% YoY and 4.3% MoM in Sep



Source: Komtrax data, CMBIS

As an important source of infrastructure funding, RMB 3.37tn local government special bond had been issued as of 30 Sep, representing 89.7% of the annual target at RMB 3.75tn. The rest RMB 385bn are scheduled for issuance in Oct.

Figure 15: RMB 3.37tn local government special bond had been issued as of 30 Sep 2020

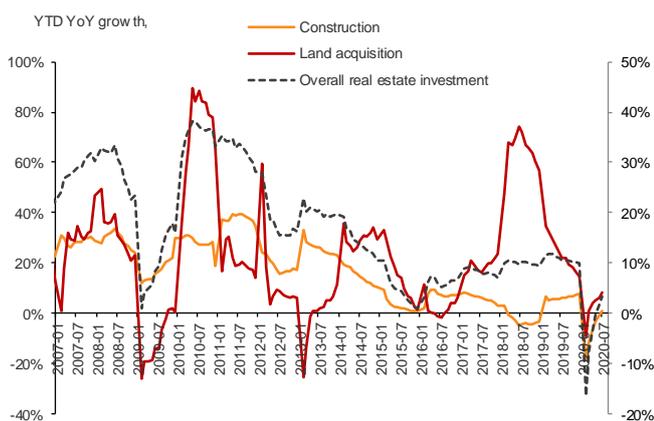


Source: Ministry of Finance, Wind, CMBIS estimates

■ Real estate investment +5.6% in 9M20

Real estate investment speeded up to increase 5.6% YoY in 9M20, 1ppt faster than in 8M20. Resilient growth was attributable to both construction spending and land acquisition expenditures. Although developers are faced with stringent financing restrictions to maintain healthy balance sheet and certain markets have tightened home purchase criteria, real estate investment tends to be a lagged variable of all the above changes and won't turn weak immediately. Construction of previous projects and steady land acquisition expenditures will continue to firm up real estate investment in 4Q.

Figure 16: Real estate investment driven by both construction and land acquisition expenditures



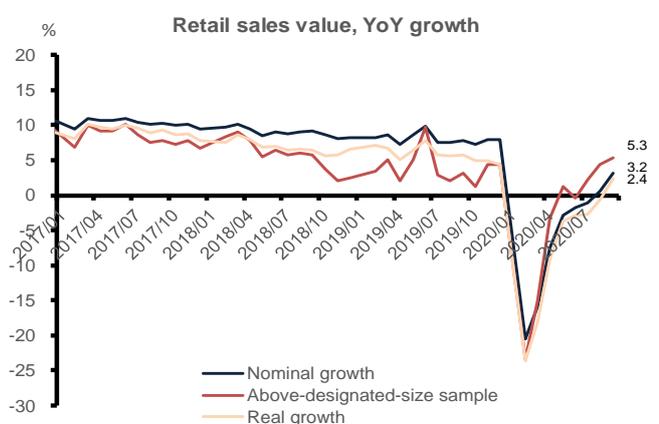
Source: NBS, Wind, CMBIS estimates

Retail sales +3.3% YoY in Sep

Booming demand before and during the Oct 1 holiday lifted consumption recovery in Sep. Retail sales increased 3.3% YoY, advancing 2.8ppt from that in Aug. Momentum of strong car sales sustained in Sep, +11.2% in retail value. Excluding car sales, growth was 2.4% YoY in Sep.

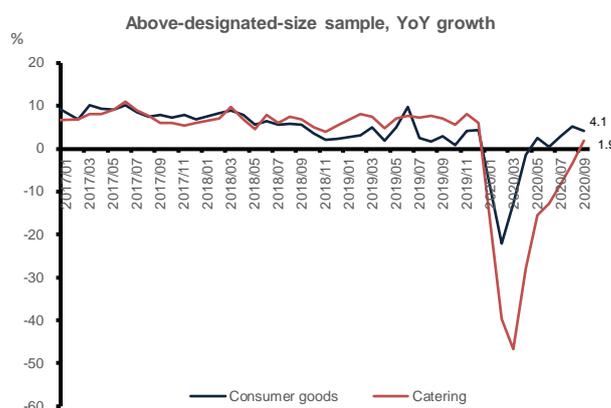
Catering sector warmed up, +1.9% for the above-designated-size sample, marking the first positive growth since COVID-19. For the full sample, catering also narrowed decline from 7% in Aug to 2.9% in Sep.

Figure 17: Retail sales value +3.2% in Sep



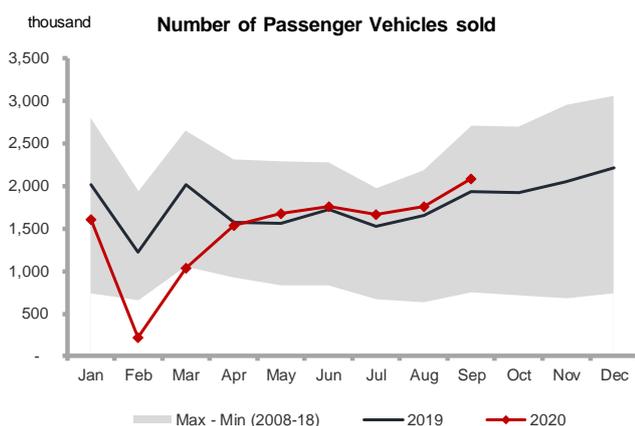
Source: NBS, Wind, CMBIS

Figure 18: Catering growth turned positive for the above-designated-size sample



Source: NBS, Wind, CMBIS

Figure 19: Sustained momentum of car sales



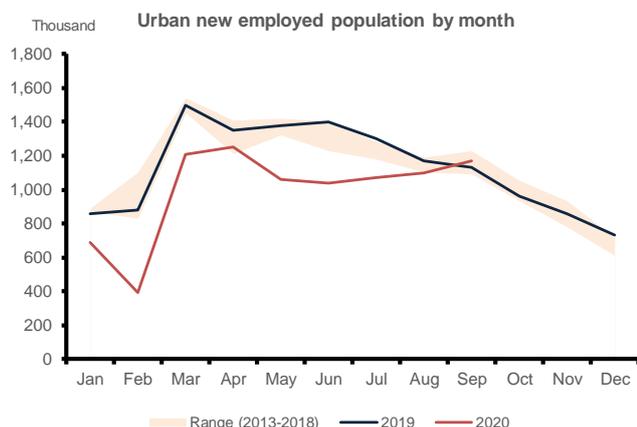
Source: Wind, CMBIS

Brighter employment situations

Employment situations are improving sequentially with the rebound of domestic economy and recovering export activities. In Sep, 1.17 million people were added to urban employed population, making total to 8.98 million in 9M20. Surveyed urban unemployment rate further inched down to 5.4% in Sep.

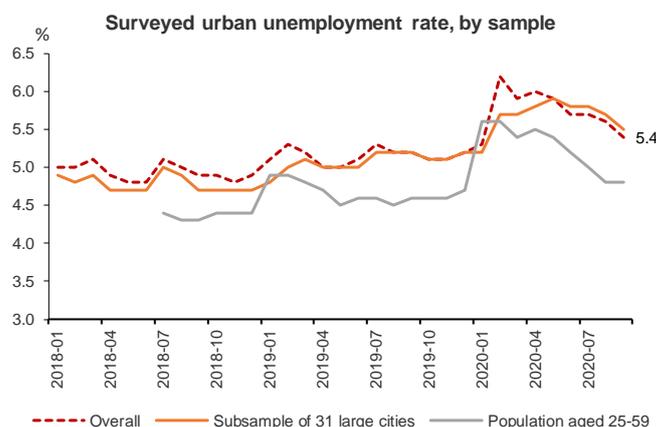
Firming trend also observed from employers' perspective. Unlike the official unemployment monitors, PMI employment subindex and the CKGSB Business Conditions Index (BCI) are leading indicators to depict job market from the angle of employers. Figure 22 shows that non-manufacturing employment PMI has been edging up notably since 3Q and especially in Sep (reaching 49.1% vs. 48.3% in Aug). The CKGSB BCI (Figure 23) also informed that small- to medium- business owners have been turning more positive towards recruitment situations.

Figure 20: In 9M20, 8.98 million people were added to the new employed population, reaching 99.8% of annual target



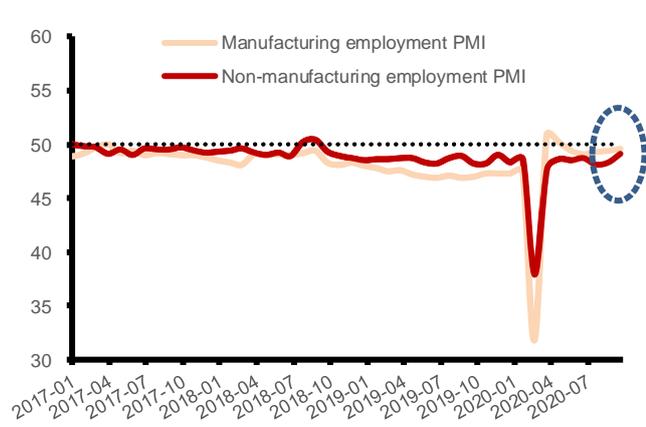
Source: NBS, CMBIS

Figure 21: Surveyed urban unemployment rate further inched down to 5.4% in Sep from 5.6% in Aug



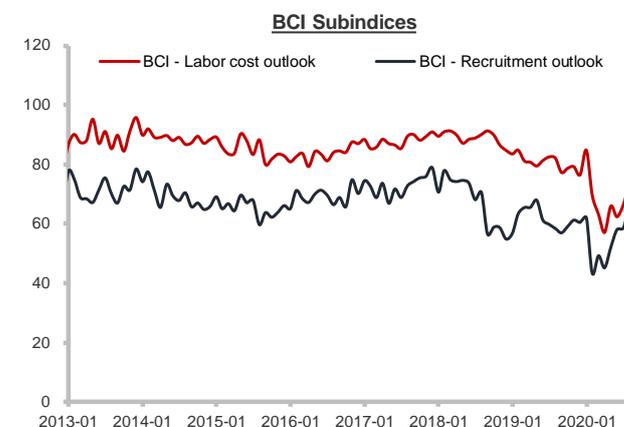
Source: NBS, Wind, CMBIS

Figure 22: Service sector employment witnessed notable progress since 3Q



Source: NBS, Wind, CMBIS

Figure 23: The BCI recruitment outlook has been turning positive



Source: CKGSB, Wind, CMBIS

Forecast of major economic indicators

Figure 24: Forecast of major economic indicators

	2017A	2018A	2019A	2020E
Real GDP (yoy growth, %)	6.9	6.6	6.1	2.4
CPI (YoY growth, %)	1.6	2.1	2.9	2.9
PPI (YoY growth, %)	6.3	3.5	-0.3	-2.0
Value-added industrial output (YoY growth, %)	6.6	6.4	5.7	1.8
Fixed asset investment (YoY growth, %)	7.2	5.9	5.4	2.5
Infrastructure	19.0	3.8	3.8	2.0
Manufacturing	4.8	9.5	3.1	-6.0
Real estate development	7.0	9.5	9.9	5.5
Retail sales (nominal, YoY growth, %)	10.2	9.0	8.0	-3.0
Export (in USD, YoY Growth, %)	7.9	9.9	0.5	-1.0
Import (in USD, YoY Growth, %)	15.9	15.8	-2.8	-5.0
M2 (YoY growth, %)	8.2	8.4	8.7	10.8
Total social financing (TSF) balance (%)	13.4	9.8	10.7	13.0
RMB loans outstanding (%)	12.7	13.5	12.5	12.7
1-year LPR (%)	n/a	n/a	4.15	3.85
5-year LPR (%)	n/a	n/a	4.80	4.65
1-year MLF operating rate (%)	3.25	3.30	3.25	2.95
7-day reverse repo rate (%)	2.50	2.55	2.50	2.20
10-year Government bond yield (%)	3.0-4.0	3.1-4.0	3.0-3.4	3.0-3.2
USD/CNY (range)	6.46-6.96	6.26-6.97	6.68-7.18	6.70-7.10
USD/CNY (end of period)	6.51	6.88	6.96	6.80

Source: NBS, PBoC, China Customs, Wind, Bloomberg, CMBIS estimates

Figure 25: Forecast of GDP growth under base and bull case

Real GDP growth	1Q20A	2Q20A	1H20A	3Q20A	4Q20E	2020E
Base case	-6.8%	3.2%	-1.6%	4.9%	6.0%	2.2%
Bull case					7.0%	2.5%

Source: NBS, CMBIS estimates

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