China's Economic Outlook 2022Q3

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Highlights

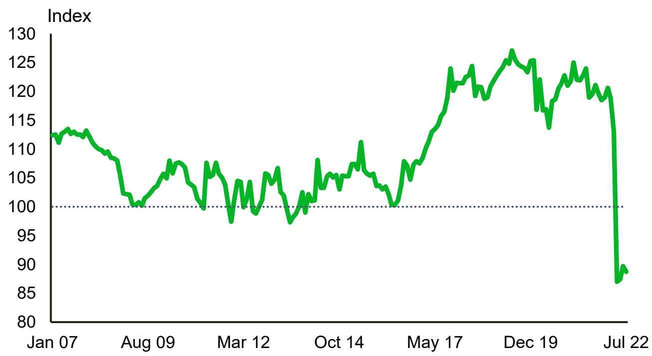
- China's economic problems look set to persist through 2022, and into 2023, as measures taken by authorities to offset the economic malaise will likely prove insufficient to kick-start the economy.
- Amid the pullback by domestic consumers, and the slowdown in the real estate sector, softening global goods demand will weigh on the recovery.
- We now project China's GDP to expand by 2.6% in 2022 (well short of the 5.5% target set in the spring) and by 4.2% in 2023, although uncertainty remains high as a policy shift could materially improve the outlook.

China's economic problems look set to persist through 2022, and into 2023, as measures taken by authorities to offset the economic malaise will likely prove insufficient to kick-start the economy. In our recent quarterly forecast, we now project China's GDP to expand by 2.6% in 2022 (well short of the 5.5% target set in the spring) and by 4.2% in 2023. To be sure, there is ample uncertainty surrounding the outlook. For instance, a more robust than expected policy response to address the underlying issues facing the economy could initiate a course correction to revive growth.

That said, it continues to appear unlikely that authorities will meaningfully alter policy to improve the near-term outlook. Eradication of COVID-19 remains the official strategy and requires severe responses. The strict lockdowns and economic after-effects have severely degraded consumer sentiment – pushing it to historic lows (Chart 1). Even as the severity of restrictions in response to COVID-19 outbreaks appear to be more muted going forward, as long as COVID-19 elimination remains the goal, there is limited scope for consumer sentiment to recover. Moreover, domestic and international travel continue to be stuck in the doldrums as intercity and international mobility (Chart 2) remain key points for controlling viral spread.

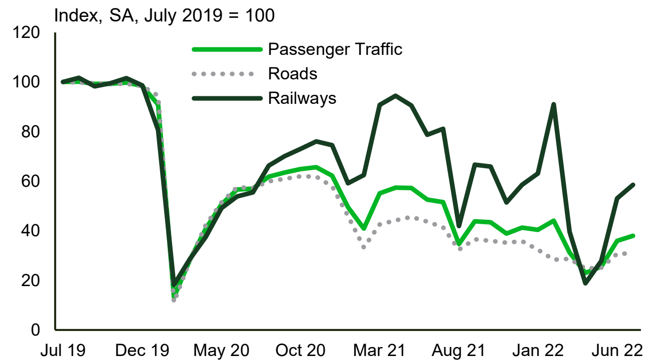
Reduced mobility and lower consumer confidence are supported by the second quarter consumer survey results from by the People's Bank of China (PBOC) showing higher savings expectations going forward (Chart 3). Under current conditions, we expect consumption expenditures to grow 0.2% in 2022, before rebounding moderately by 6.4% in 2023. The expansion in 2023 is notably slower than the 8.8% average growth rate between 2014 and 2018.

Chart 1: Consumer Confidence Tumbles to Historic Lows



Note: Readings above 100 indicate optimism.
Source: CNBS, TD Economics.

Chart 2: Passenger Traffic Has Yet to Return to Pre-pandemic Levels



Note: Index is based on the number of passengers.
Source: CNBS, TD Economics.

Chart 3: Urban Residents Are Looking to Save More

*Share of survey respondents reporting desire to increase savings.
Source: PBoC, TD Economics. Last observation: 2022 Q2.

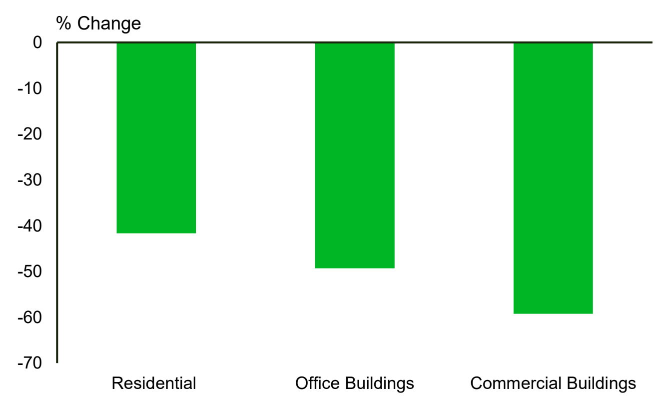
Downbeat consumer expectations will also weigh on the real estate sector. Real estate sales are down 23% on average so far in 2022 (on a year-on-year basis) and with demand withering, prices are falling. New home prices in 70 cities fell for the 12th consecutive month in August, now 2.1% below year-ago levels[1]. With new purchases pulling back, and access to capital drying up due regulatory changes, newly started residential construction (measured in square feet) is down 38% year-on-year (y/y) on a year-to-date basis — and just over 40% relative to 2019 (Chart 4).

The steep decline in real estate activity has forced government action. Credit is being extended to firms to ensure the completion of residential projects already underway[2] (200 billion yuan or 0.2% of 2021 nominal GDP), while local government financing vehicles are buying up land[3] – helping to preserve a key source of revenues to local governments. These interventions will help rebuild some confidence in the market but are unlikely to reverse the near-term trend in the real estate sector. Moreover, the recent cuts in the key five-year loan prime rate by the PBOC are unlikely to stimulate demand while lockdowns and sentiment weigh on activity. Investment in private dwellings is expected to contract 4.2% in 2022 and another 2.1% in 2023. Under the current circumstances, and downbeat consumer confidence, the real recovery in the residential sector is unlikely to start until late 2023 and early 2024.

Amid the pullback by domestic consumers and the slowdown in the real estate sector, softening global goods demand will weigh on the recovery. Our most recent forecast has U.S. demand for goods contracting 0.6% in 2023, with a corresponding 2.2% decline in imports. Moreover, the staggering scale of the energy shock in Europe will continue to erode disposable incomes, limiting discretionary expenditures. Given the gloomy backdrop, global trade will slow well into next year. Providing a small offset is the ongoing depreciation of the renminbi, down roughly 9% against the U.S. dollar since February, which will help support competitiveness for Chinese firms. However, as China is a key supplier of consumption goods for both the US and euro area, exports will contract marginally in 2023, well below the 3.1% growth rate averaged in the five years prior to the pandemic.

Including the stimulus in the housing sector, authorities recently announced 19 measures intended to help support the economy this year[4]. Key among them is an effort to kick-start growth through infrastructure investment and allowing local governments to raise funds via unused borrowing

Chart 4: Newly Started Construction Relative to 2019



Note: Construction is measured in square meters.
Source: CNBS, TD Economics.

quotas by the end of October. The total stimulus package will amount to 1 trillion yuan (146 billion USD, or 0.9% of 2021 nominal GDP). However, the stimulus measures announced so far will likely have a limited impact this year if consumer confidence remains subdued and restrictions on economic activity due to COVID-19 flareups continue. The root issues facing the economy are the weakness in the real estate sector, malaise amongst consumers, and a weak export outlook. A revival in infrastructure spending will struggle to outweigh these drivers.

Bottom Line:

Given the headwinds from COVID-19 control policies, limited political appetite for large monetary and fiscal stimulus, and depressed consumer demand we anticipate growth in 2022 to register a mere 2.6%, less than half the government's 5.5% target laid out late in 2021. Moreover, absent a change in policy, growth in 2023 will lie below trend as the weak handoff from the latter half of 2022 and policy uncertainty weigh on the outlook. Our view is thus that China's 2023 growth will register approximately 4%.

Importantly, this extended period of softness in China won't be lost on a global economy that is already facing the impact of recessions or stagnant performances in major advanced economies. In our updated global outlook, we have downgraded world growth to only 2.8% this year and 2.2% in 2023. One implication will be continued weakness in commodity prices, with WTI projected hang around $80 in early 2024.

Endnotes

1. Bloomberg News, (September 15, 2022), "China's Home Price Slump Reaches a Year as Crisis Drags On", https://www.bloomberg.com/news/articles/2022-09-16/china-s-home-prices-fall-for-one-year-straight-as-crisis-deepens
2. Bloomberg News, (August 22, 2022), "China Plans $29 Billion in Special Loans to Troubled Developers", https://www.bloomberg.com/news/articles/2022-08-22/china-plans-29-billion-in-special-loans-to-troubled-developers
3. Financial Times, (September 15, 2022), "China's Local Government Financing Vehicles Go on Land Buying Spree", https://www.ft.com/content/b6ef0852-6d51-44eb-9c7c-128f9c47c75a
4. Bloomberg News, (August 24, 2022), "These Are China's 19 New Measures to Bolster Economic Growth", https://www.bloomberg.com/news/articles/2022-08-25/these-are-china-s-19-new-measures-to-bolster-economic-growth