Green shoots in domestic economy amid new trade war

- **We see signs of green shoots in China's housing market and a potential lift in private sector animal spirits following tech breakthroughs and encouraging policy signals.**
- **We look for continued stimulus to give counterweight to the expected US-China trade war this year.**
- **We still look for a weaker CNY against the USD, which will dampen some of the impact from higher tariffs.**
- **Growth is set to remain fragile, though, as it will take time to repair household confidence following years of first covid lockdowns and subsequently a continued housing crisis.**
- **We keep our forecasts unchanged from December looking for GDP to grow 4.7% in 2025 and 4.8% in 2026.**
- **The US-China rivalry is set to intensify with Trump's foreign policy taking stronger aim at China. He is unlikely to cross China's red line on Taiwan, though.**
- **Trump's America First policy may pave the way for a reset of EU-China relations. However, we expect trade tensions to remain due to China's rise as a competitor in many sectors, heavy use of industrial policy and overcapacity issues.**

5 March 2025
Important disclosures and certifications are contained from page 3 of this report.

	2024	Forecast 2025	2026
GDP Growth	5.0%	4.7% (4.7%)	4.8% (4.8%)
Inflation	0.2%	1.0% (1.5%)	1.5% (1.5%)
Unemployment	5.1%	5.1% (5.2%)	5.1% (5.2%)
Policy Rate*	2.00%	1.50% (1.50%)	1.50% (1.50%)

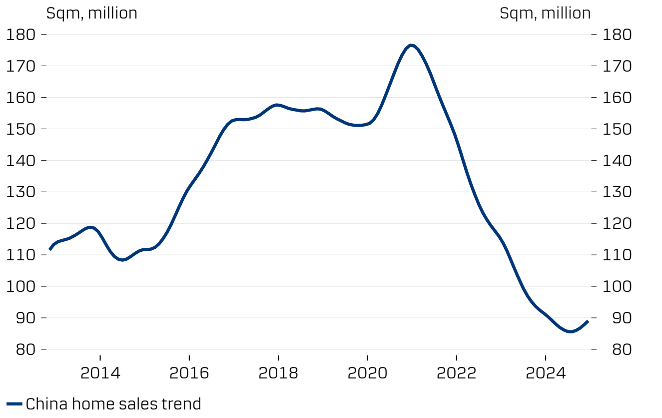
Paranthesis are the old projections (From December 2024)
**End of period (1-year Medium Lending Facility)*
Source: Danske Bank, Macrobond Financial

Signs of bottoming in the housing market
China's housing crisis has been a massive drag on the economy for the past three years. Home sales have been cut in half since the peak in late 2020 and home prices have declined for more than 2½ years leading to big declines in households wealth. The erosion of wealth has led to a sharp rise in the savings by households and kept consumption growth at low levels. This has in turn hurt employment and undermined consumption further. China has thus been caught in a negative spiral. However, it finally looks like the wide range of policy measures to turn the housing market is having an effect. We now see the first signs that home sales and prices are moving higher in the biggest cities. As we see the housing crisis as the epicentre of China's growth challenges, this is an important development.

In the middle of a painful transition
China is in a painful transition from an old growth model where housing construction, 'old' infrastructure and low-level exports

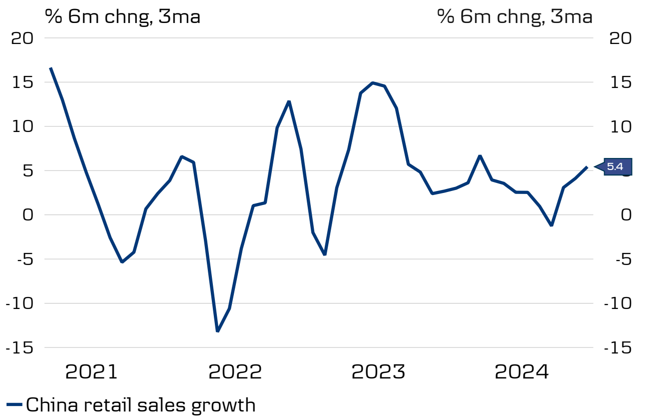
> *We now see the first signs that home sales and prices are moving higher in the biggest cities.*
>
> *Allan von Mehren, Chief Analyst*

Chinese housing market show signs of bottoming



Remark: Trend- and seasonally adjusted
Source: China National Bureau of Statistics (NBS)

China needs to lift consumption growth further



Macrobond Financial, NBS, Danske Bank

Chinese tech rally to spur more animal spirits in private sector?

Remark: Seasonally adjusted
Source: China National Bureau of Statistics (NBS)

were key growth drivers to a new growth model where China aims for private consumption and high-tech investments to be the key engines. And where the manufacturing sector upgrades and exports higher quality goods. Infrastructure investments will be centered on 'smart infrastructure' such as EV charging stations, data centers, ultra-high voltage transmission lines etc. which can support China's future technological development. While China is already making strides in the tech field, the economy suffers from the vacuum from weaning off housing led growth which in turn obstructs getting the consumer engine started. Apart from creating overcapacity, insufficient consumer demand result in deflationary pressures and tensions with trading partners. China's current growth is mainly coming from the green-tech sector and infrastructure investments, which are dominated by China's own firms.

Reviving consumption growth priority number one
For these reasons, China's policy makers in December put boosting consumption growth to the very top of their 9-point priority list for the coming year. A trade-in-scheme subsidizing consumption is being scaled up, public worker wages have seen a new lift and social transfers are increased. Still, the most important factor to improve consumption is a stabilization of the housing market but as mentioned there are a bit more positive signs in this field as well. We thus expect consumption growth to see a gradual move higher but we are unlikely to see a big boom of any kind as it will take time to repair the very weak consumer confidence. We expect growth this year to decline from 5.0% to 4.7% and see a broadly similar rate in 2026 at 4.8%, unchanged from our previous forecast.

AI breakthrough and policy signals to improve animal spirits
In January, China's AI start-up DeepSeek surprised by launching a model that on many parameters performs at par with the best US models, which triggered renewed optimism in Chinese tech and fueled a strong rally in tech stocks. Sentiment saw a further boost when President Xi Jinping hosted a private sector symposium stressing the leadership's support of the private sector. This could be the beginning of more animal spirits returning to China's entrepreneurs after several years of low confidence from a tech crackdown and weak macroeconomic performance.

Trade war looming
A new headwind is looming on the horizon, though, from a new trade war with the US. We expect Trump to continue to increase tariffs on China during the year in response to a trade report coming in April that will likely conclude China is cheating on trade and never lived up to the phase one deal. A deal will likely eventually be struck but as with the first trade war, we expect it to take many rounds of negotiations to get there. We expect US tariffs will gradually increase to around 40% on average on Chinese goods. A weaker CNY will partly compensate for the increase. In December we already shaved off ½ percentage points of our forecast in anticipation of the trade war. Trump's disruption of the global order and new tensions with EU could pave the way for a reset of EU-China relations. At least recent comments from EU and China points and opening for new engagement.

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Where no other source is mentioned statistical sources are: Danske Bank, Macrobond, EC, IMF and other national statistical institutes as well as proprietary calculations.

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