Housing crisis continues to pull down the economy

- **After a strong start to 2024, the Chinese economy lost momentum again in recent months with the housing crisis and weak consumer spending still being at the center of the challenges.**
- **Looking ahead we expect more muddling through with new stimulus set to provide a lift to the rest of the year with the government committed to its' 5% growth target. Still, we revise down growth to 4.8% for 2024 (previous 5.2%). In 2025 we continue to project growth of 4.8%.**
- **Exports provided a tailwind in the first half of 2024 but export growth is expected to fade in the second half. We look for housing and consumption to stay weak over the forecast horizon as measures to turn the crisis remain too small.**
- **Chinese policy makers are set to increase stimulus measures in the coming quarters using both fiscal and monetary policy. However, a mini-bazooka is needed to drive a real recovery and we doubt this is coming.**
- **Taking a step back, China continues to muddle through a long and painful transition from an old to a new growth model with less focus on real estate and 'old' infrastructure and more emphasis on new technology, high-end manufacturing, green-tech, 'smart' infrastructure and private consumption.**
- **EU-China trade tensions have increased and we believe they are here to stay in the coming years. However, we don't look for a big trade war. If Donald Trump wins back the White House, we expect a new US-China trade war in 2025.**

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

	2023	Forecast 2024	2025
GDP Growth	5.2%	4.8% (5.2%)	4.8% (4.8%)
Inflation	0.2%	0.3% (0.7%)	1.5% (1.5%)
Unemployment	5.2%	5.2% (5.2%)	5.2% (5.2%)
Policy Rate*	2.50%	2.10% (2.30%)	1.80% (2.30%)

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

Down again

Following a strong first quarter, Chinese activity lost momentum again during early spring and into the summer. PMI for manufacturing as well as for the service sector fell back and the construction sector continued to struggle severely. On the demand side, exports performed well in the beginning of the year but is losing some momentum. Most importantly, though, the housing crisis continues to weigh over the economy with new home sales staying close to recent lows around 45% lower than pre-pandemic levels. House prices also keep declining at an annualized rate of close to 10%. With a lot of household wealth tied up in housing, household confidence has remained at a historical low. Consequently, household consumption growth remains weak with retail sales only growing 2½-3% on an annual basis. Large-scale green investments in solar, wind, batteries, EVs etc. is underpinning growth.

> The epicentre of China's current economic crisis is the housing market and until policy makers manage to stabilize housing, the economy will struggle

Allan von Mehren, Chief Analyst at Danske Bank

The logs are wet, more fuel is needed

The epicentre of China's economic crisis is the housing market and until policy makers manage to stabilize housing, the economy will struggle. More measures were launched in the first half of the year such as further reducing required down payments for house purchases and the government setting aside money for buying up empty homes, but there are still no signs it is having the desired impact. If you try to start a fire with logs that are wet, you need a lot of fuel and so far it is evident that China is not using enough of it. We believe China will launch yet another round of measures over the coming quarters to turn the crisis, which should be able to provide a small lift to growth again. But until we see more clear signs of a change in the willingness to take much stronger measures, we expect China to remain in a muddling through scenario with growth just below 5%, primarily driven by state support.

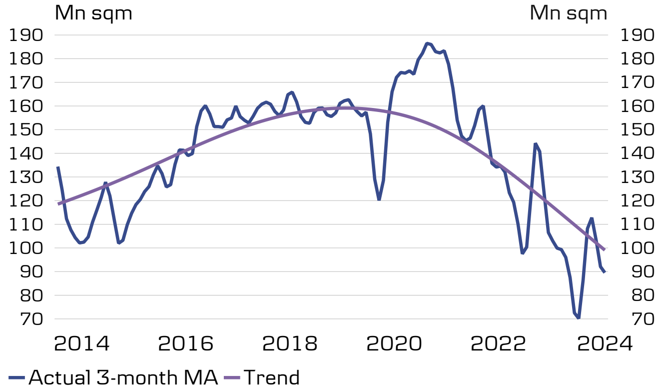
Third Plenum outlines strategy for next five years

In July, China held its' so-called Third Plenum which is held every five years and outlines reforms for the next five years. China vowed to increase the leverage of the market, opening up further, making a fiscal reform that moves more of the burden to the central government, and taking steps to underpin urbanization (and thus housing demand) by removing the so-called Hukou system which ties rights to social services (education, health care etc.) to people's place of household registration. A strong focus on technology, education and easing child care costs were also outlined, the latter to increase the birth rate. A retirement reform is also coming aimed at easing the decline in the labour force in the coming decades. While the plan contains many positive elements, the 'proof is in the pudding' and the results will depend on China's ability to follow through with implementation.

China is in a painful structural transition to reduce reliance on housing as a demand driver and policy makers aim for an economy where growth drivers are instead high-tech investments, upgrade of manufacturing, green investments and private consumption. The transition is difficult and is set to weigh on growth in the next couple of years with household confidence staying low due to the weak housing market. In the long term, China could come out stronger but the path is set to be long and bumpy. The long term growth potential also faces headwinds from a falling working age population, Western tech sanctions and lower foreign investments. But we still see China's trend growth in the coming 3-4 years around 4½% on average. More reforms, a low GDP per capita (less than 20% of US level), as well as a strong focus on education, innovation, and tech, should underpin this potential.EU-China trade tensions set to continue, Trump win could trigger new trade war

Home sales still at very low levels

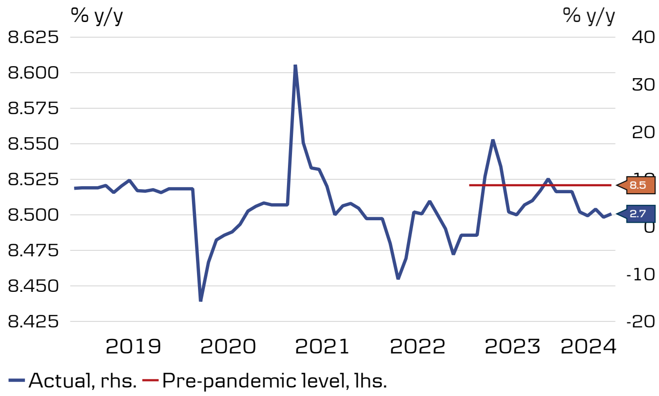
China home sales



Remark: Trend- and seasonally adjusted
Source: Statistics Sweden

Lacklustre private consumption

Retail sales



Remark: Seasonally adjusted
Source: Creditsafe, Swedish Agency for Growth Policy Analysis

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Trade tensions between EU and China have carried on over the summer with the EU implementing higher tariffs on Chinese goods and China being in the process of several anti-dumping investigations of certain EU products, such as pork and brandy. We believe tensions will continue in the years to come but doubt it will evolve into a real trade war. It is a risk, though. In US-China relations, a trade war is likely if Donald Trump wins the US election in November. Geopolitical tensions around Taiwan and the South China Sea are also set to be with us for the foreseeable future.

Allan von Mehren
China
alvo@danskebank.com

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Global Danske Research

Global Head of Research
Heidi Schauman
heidi.schauman@danskebank.com

Macro

Head of
Las Olsen
Denmark
laso@danskebank.com

Allan von Mehren
China macro and CNY
alvo@danskebank.com

Antti Ilvonen
US macro, AUD and NZD
ilvo@danskebank.com

Bjørn Tangaa Sillemann
Denmark, Japan
bjsi@danskebank.com

Frank Jullum
Norway
fju@danskebank.com

Louise Aggerstrøm Hansen
Denmark
louhan@danskebank.com

Minna Kuusisto
Emerging Markets
mkuus@danskebank.com

Pasi Kuoppamäki
Finland
paku@danskebank.com

Rune Thyge Johansen
Euro Area
rujo@danskebank.com

Sweden

Head of
Filip Andersson
Fixed income strategy
fian@danskebank.com

Michael Grahn
Sweden
mika@danskebank.com

Therese Persson
Sweden macro
THP@danskebank.com

Jesper Fjärstedt
SEK, PLN, HUF and CZK
jesppe@danskebank.com

Stefan Mellin
SEK strategy
mell@danskebank.com

Joel Rossier
Fixed income strategy
joero@danskebank.com

Fixed Income Research

Head of
Jan Weber Østergaard
DKK and EUR fixed income
jast@danskebank.com

Frederik Romedahl Poulsen
Global rates
frpo@danskebank.com

Jens Peter Sørensen
Nordic and EUR fixed income
jenssr@danskebank.com

Jonas Hensch
DKK fixed income
jhens@danskebank.com

Piet P.H. Christiansen
ECB and EUR fixed income
phai@danskebank.com

FX and Corporate Research

Head of
Kristoffer Kjær Lomholt
NOK
klom@danskebank.com

Mohamad Al-Saraf
EUR, USD, JPY, and Institutional FX
moals@danskebank.com

Jens Nærvig Pedersen
DKK, commodities, USD liquidity, Institutional FX
jenpe@danskebank.com

Kirstine Grønborg Kundby-Nielsen
GBP, CHF and Corporate FX
kigrn@danskebank.com

Credit Research

Head of
Jakob Magnussen
Utilities
jakja@danskebank.com

Benedicte Tolaas
Norwegian HY
beto@danskebank.com

Brian Børsting
Industrials
brbr@danskebank.com

Christian Svanfeldt
Real Estate and Industrials
chrsv@danskebank.com

Lina Berg
Industrials
linab@danskebank.com

Linnea Sehlberg
Industrials
sehl@danskebank.com

Louis Landeman
Sustainability/ESG
llan@danskebank.com

Mads Rosendal
TMT and Industrials
madros@danskebank.com

Mark Thybo Naur
Financials and Strategy
mnau@danskebank.com

Marko Radman
Norwegian HY
mradm@danskebank.com

Olli Eloranta
Industrials and Real Estate
oelo@danskebank.com

Rasmus Justesen
Credit Portfolios
rjus@danskebank.com

Sverre Holbek
Financials
holb@danskebank.com

Marcus Gustavsson
Real Estate
marcg@danskebank.com

Mille Opdahl Müller
Industrials
mifj@danskebank.com