

Research

China outlook: recovery set to lose steam in 2017

Growth:

- **Chinese growth indicators continue to support the case for a moderate recovery** this year. PMIs have trended higher and industrial production and profits have rebounded too. Indicators for electricity production and steel production confirm this.
- The recovery is being driven by (a) fiscal stimulus via infrastructure investments, (b) a recovery in the construction sector due to strong home sales and reduction in home inventories and (c) a moderate export recovery supported by a 10% weakening of the CNY.
- **Looking ahead, we expect to see some moderation in the recovery** going into 2017 as the stimulus effects fade slightly, and the biggest boost to construction should fade as home sales growth has come down in response to regional tightening measures. We expect average GDP growth to be 6.6% in 2017 (consensus: 6.3%).

Policy:

- **We expect monetary policy to be on hold for the rest of this year but expect to see a resumption of easing in Q2 17** as the cycle loses some steam. However, fiscal policy is the preferred tool for now as the government is concerned over rising leverage in the financial system and regional housing bubbles. The government has already indicated a further fiscal easing in H2 but not how much. **We believe the fiscal growth impact will on average be slightly smaller in 2017 versus 2016.**

Markets:

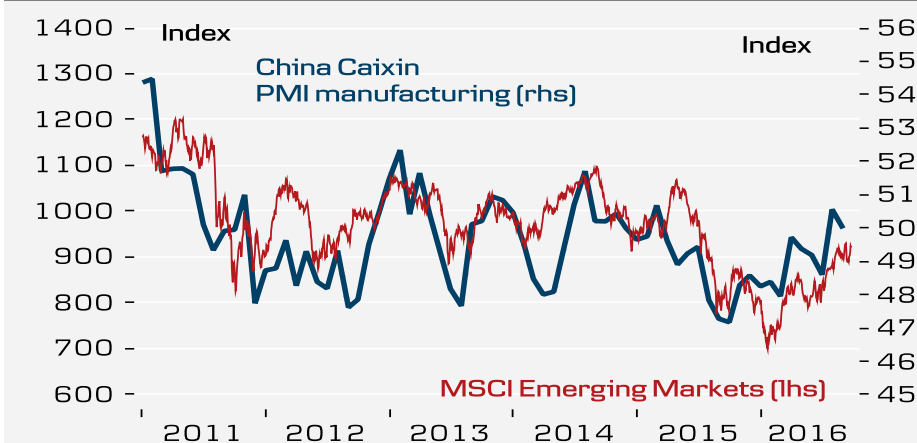
- **We look for a continuation of the weakening trend of the CNY**, not least versus the EUR where we expect a 10% depreciation +12M. For 2016, we believe there is more upside as momentum is positive and the business cycle still supports profits. However, stock markets will be more challenged in 2017 as growth momentum fades a bit again.

China home sales set to ease further – set to dampen construction again in 2017



Source: Macrobond Financial

Chinese recovery this year but set to lose some steam in 2017



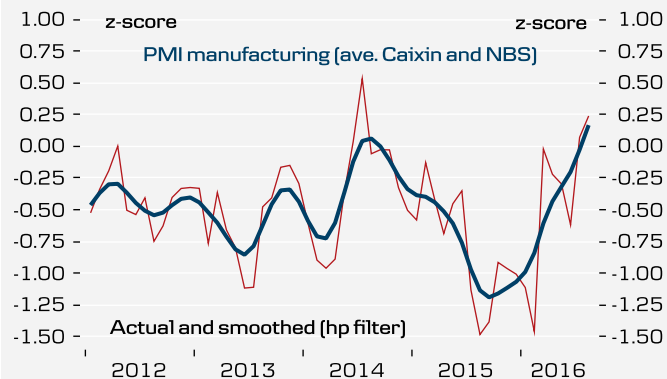
Source: Macrobond Financial, Bloomberg, Danske Bank Markets (basket own calculation)

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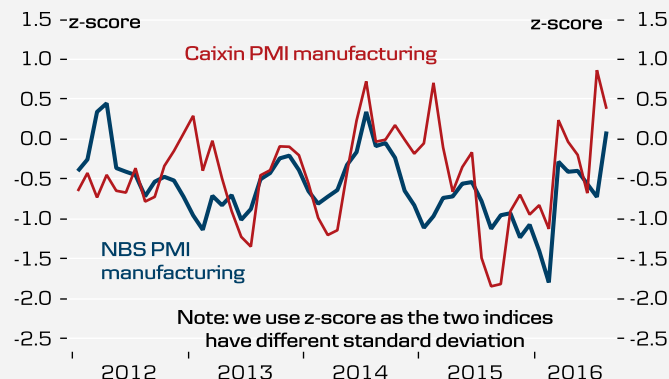
China activity indicators

PMI was strong in August



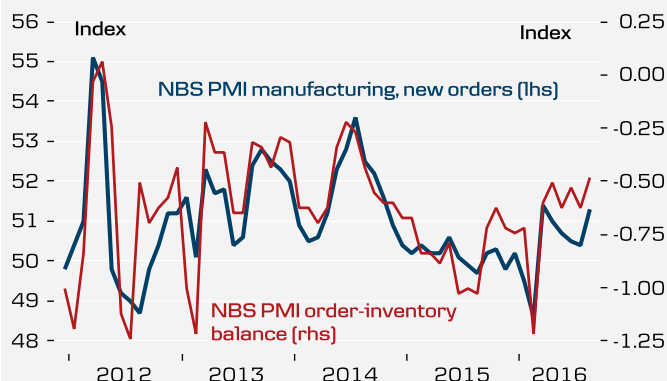
Source: Macrobond Financial

Both PMI manufacturing indices at solid levels



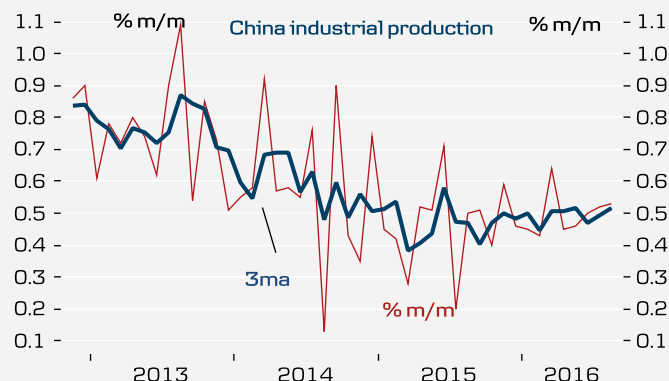
Source: Macrobond Financial

Order-inventory balance (NBS) is still robust



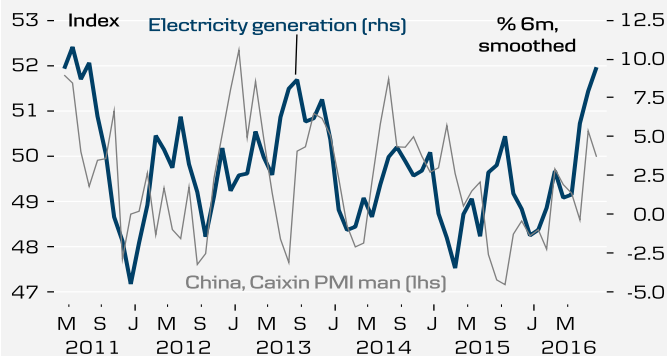
Source: Macrobond Financial

Industrial production momentum gradually higher



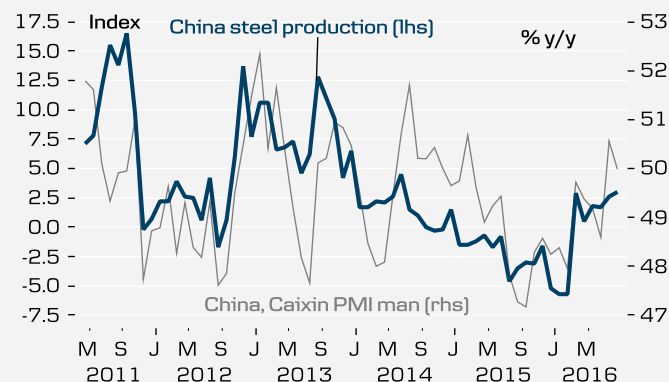
Source: Macrobond Financial

Electricity generation in line with higher activity



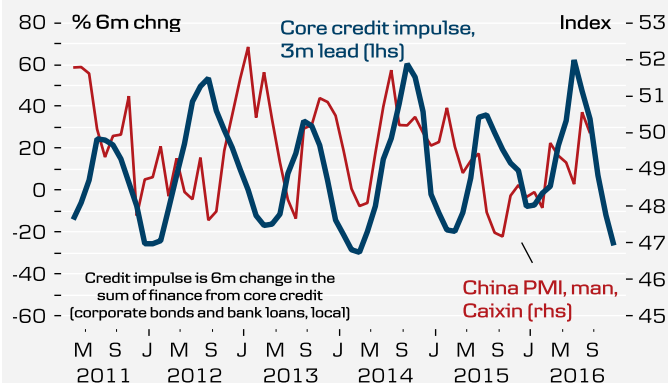
Source: Macrobond Financial

Steel production growth also higher



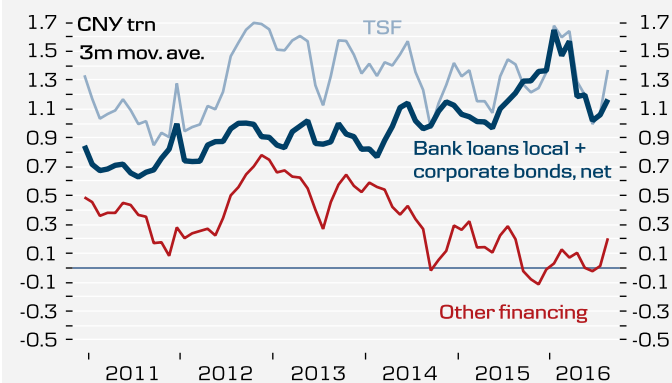
Source: Macrobond Financial

Credit impulse quite weak after significant boost in Q1



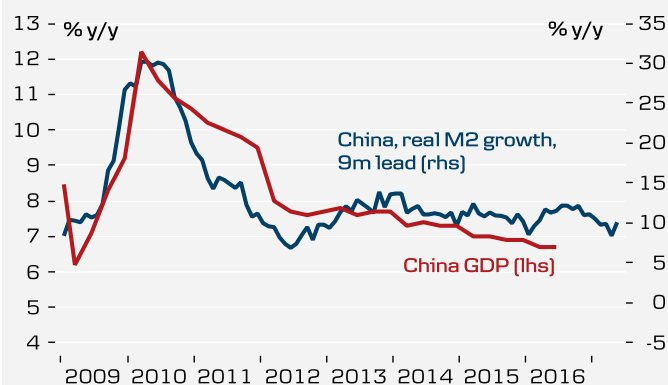
Source: Macrobond Financial

Total social financing – core credit off from the highs



Source: Macrobond Financial

Real M2 growth up in August but still points to softening



Source: Macrobond Financial

Real M1 growth paints a more upbeat picture



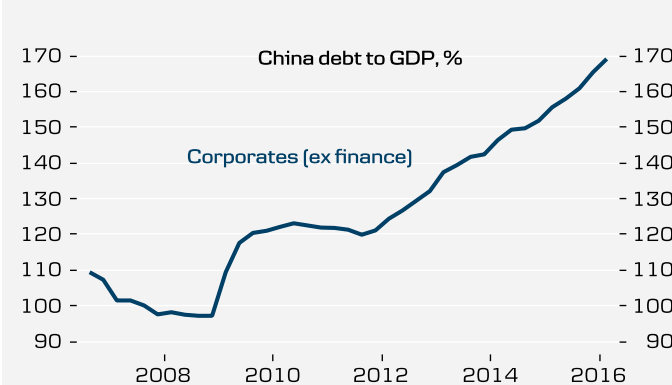
Source: Macrobond Financial

Investment growth continues to slow despite more planned projects



Source: Macrobond Financial

Rising need to start deleveraging in corporate sector – to become structural headwind for investment growth



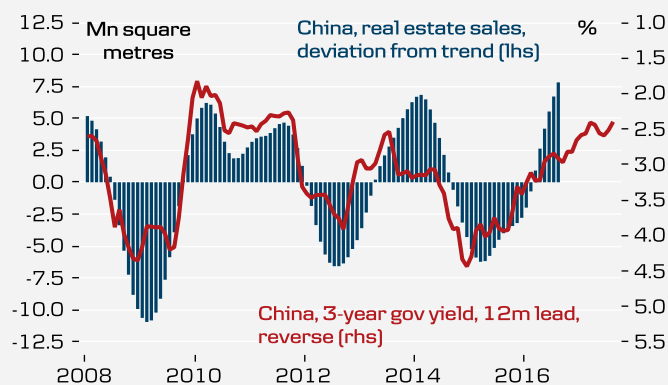
Source: Macrobond Financial

Home sales trend still strong - likely to ease in H2



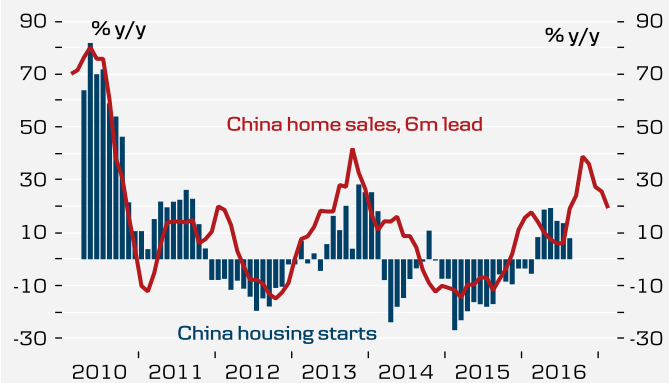
Source: Macrobond Financial

Lower yields and requirement for down payment lift sales



Source: Macrobond Financial

Housing starts lag home sales - should see more pick-up



Source: Macrobond Financial

Housing inventories have come down a lot giving a lift to prices



Source: Macrobond Financial

Our forecast for construction underpins commodity prices



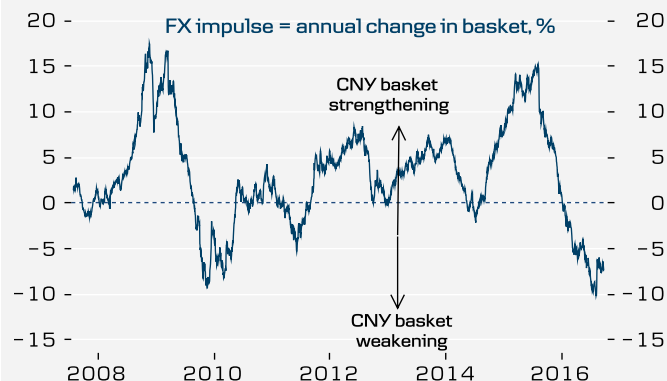
Source: Macrobond Financial

Chinese exports getting moderate lift from stronger US



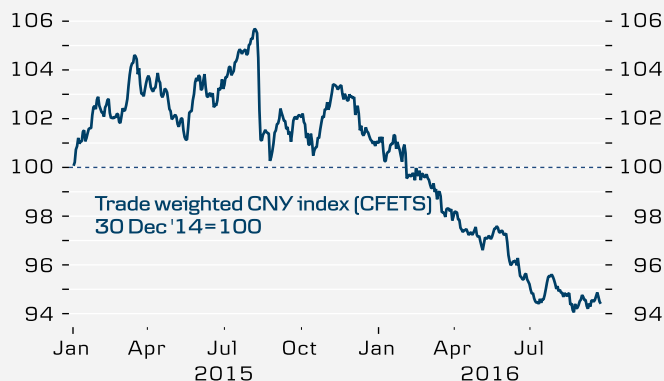
Source: Macrobond Financial

Strong tailwind to exports from weaker CNY



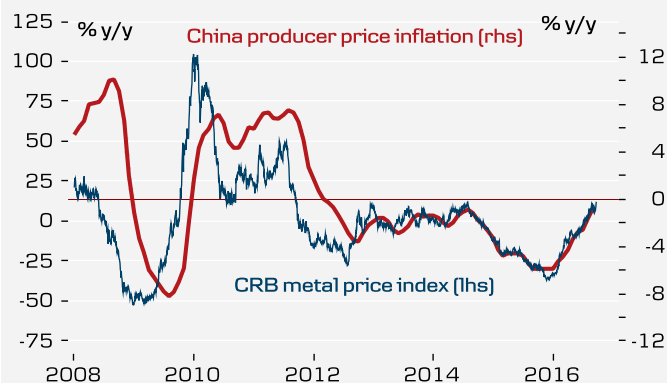
Source: Macrobond Financial, Danske Bank calculations

Continued weakening of CNY vs the basket over past year



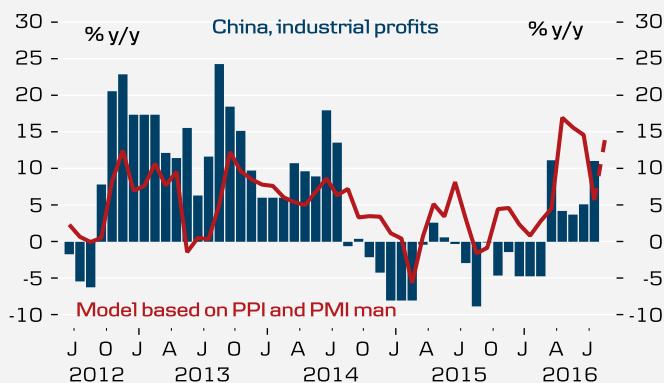
Source: Macrobond Financial, Danske Bank calculations

Producer prices getting a lift from higher commodity prices



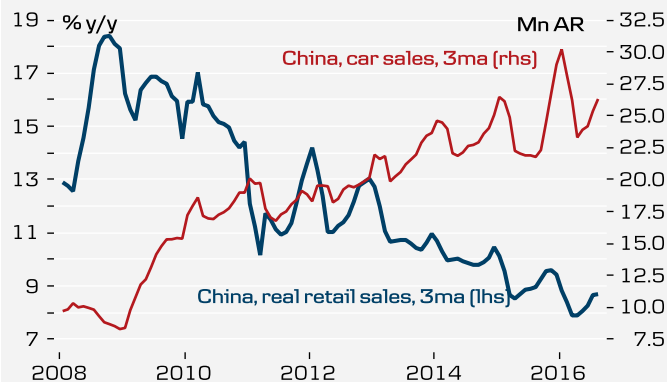
Source: Macrobond Financial

Industrial profits model



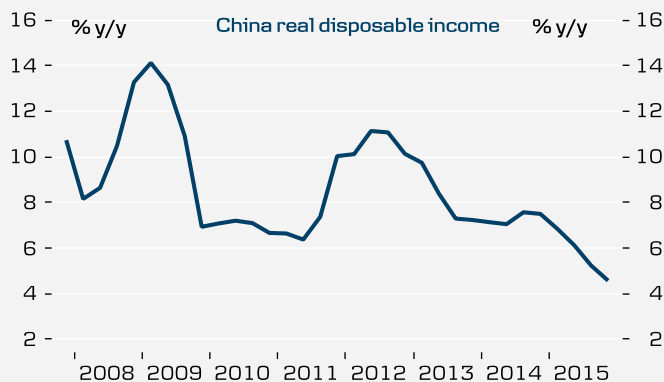
Source: Macrobond Financial

Chinese consumption growth slowing...



Source: Macrobond Financial

... as real household income growth is slowing



Source: Macrobond Financial

Financial conditions easing as bond yields are falling...



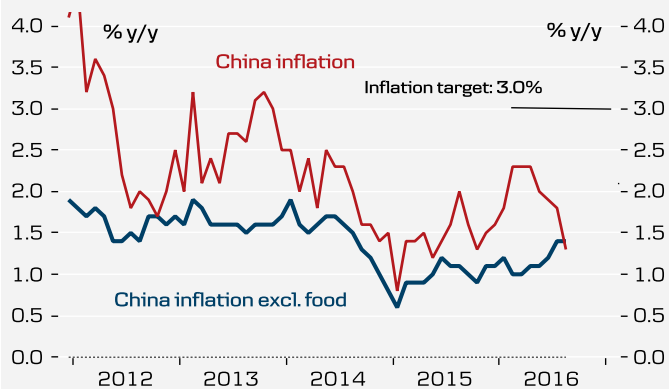
Source: Macrobond Financial, Bloomberg

... and stock markets higher



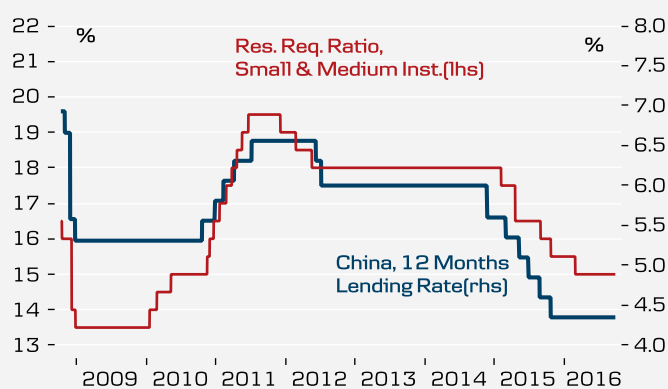
Source: Macrobond Financial, Bloomberg

No inflation pressure



Source: Macrobond Financial

Monetary policy on hold for now



Source: Macrobond Financial

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Expected updates

None.

Date of first publication

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