



# China Economy Update

## SUMMARY

- Latest monthly official data indicates the likely stable improvement in China’s economic activities since the last quarter continued;
- Exports and imports rebounded in January 2017, showing a recovery in demand at home and abroad. But caution required since trends in January and February can be distorted somewhat by the Lunar New Year holiday;
- Monetary policy points to risk prevention as economic activities continued to improve, but potential pressures on slowdown remained as traditional growth engines lose steam, possible inflation looms and the risk of capital outflow lingers in anticipation of another rate hike by the US Federal Reserve in June.

## China Economics Network

*For comments, suggestions, questions, please contact us:*

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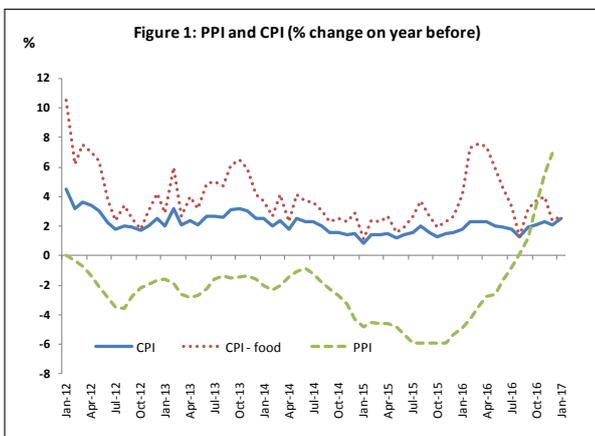
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## Rising demand contributed to the economy growing in January

1. Official data shows China’s economic activity continued to improve since the last quarter. Purchaser Price Index (PPI), a gauge measuring price change in industrial products, again rose 6.9 per cent year on year, compared with 5.5 per cent in December. A continuous increase in PPI since last year is helpful in improving producers’ profits and reducing financing costs.



2. Consumer Price Index (CPI), a gauge measuring price changes in consumption goods, also grew 2.5 per cent over the same period last year, a first reading over 2 per cent since February 2014. These two indexes refer to an obvious recovery in prices, indicating a gradual warming of the economy (Figure 1).

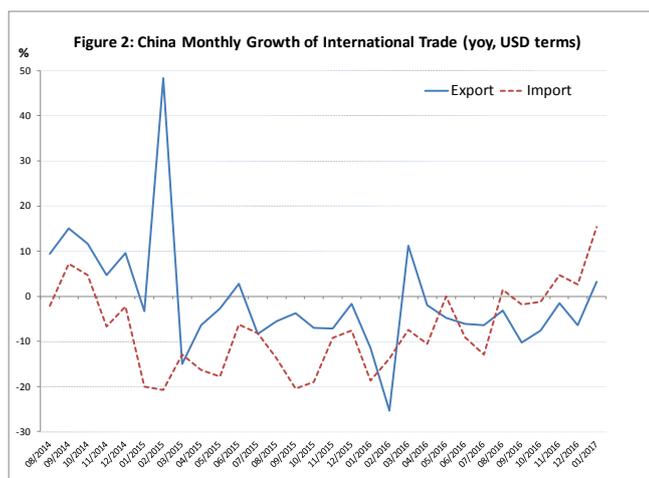
## Manufacturers’ confidence stayed on

3. China’s manufacturing sector grew steadily in January with the official PMI standing at 51.3 (non-official PMI at 51), marking the sixth straight month of expansion.
4. The official non-manufacturing PMI also rose from 54.5 in December to 54.6 in January (non-official at 53.1), well above the 50-point mark.

## Trade stats unexpectedly high on seasonal effects

5. China’s exports of goods, in USD terms, grew 7.9 per cent year on year, after a 6.2 per cent

decline last December. Imports rose 16.7 per cent compared to January 2016 (Figure 2).



- The surprisingly good performance in imports and exports in January is possibly an early sign of improved demand at home and overseas.
- Trends in January (and February) can be distorted by the Lunar New Year holidays, with business slowing down weeks ahead of time and many firms scaling back operations or closing. This year, the holiday straddled the last week of January and the first week of February.

### Housing price continued to cool down

- China's housing market continued to cool down in January, with 14 out of 15 cities (with Guangzhou the sole holdout) under the government's scrutiny reporting declining or unchanged prices, in the latest evidence that the government's heavy-handed curbs on the property market are having an effect.

### Total social financing rose to a record high

- Official data indicates China's total social financing (TSF), a broad measure of the volume of financing provided to the real economy including that offered by non-bank entities, surged to a record high of 3.74 trillion yuan (\$544.9 billion) in January from 1.63 trillion yuan in December 2016, compared to 3.48 trillion yuan in January 2016.
- Official data shows banks' new loan creation was modest but stable in January at 2.3 trillion yuan, 16% lower than a year previously. In

January, outstanding bank loans grew at the slowest rate since 2006, and total outstanding debt also slowed to the slowest pace in 11 months, indicating officials recognise the need to manage debt growth.

- A record high TSF indicates a more active real economy but also means a higher debt level, especially among the unregulated "shadow economy".
- Note that the rise in new bank lending is seasonal, as normally lending is front-loaded at the start of each year when banks are issued new loan quotas.

### While economy firms up, risks remain

- Accelerated industrial and consumer prices growth indicates nascent inflationary pressure, despite the good start to 2017. The PBoC highlighted rising inflation expectation over lingering uncertainties in a policy report issued on 17<sup>th</sup> February.
- Manufacturing activities picked up gradually, but property - a key driver of growth in 2016 - is losing steam. This is an intended effect, but managing the property market will be an important challenge in 2017.
- Official data shows China's foreign exchange reserves continued to fall by US\$12.3 billion to US\$2.998 trillion in January, compared to a decline of US\$41.1 billion in December and US\$69.1 billion in November. It may suggest the impact of the recent capital control policies has been effective but limited, although the State Administration of Foreign Exchanges commented that seasonal demand for foreign currency from domestic residents for overseas travel and consumption spending picked up around the Chinese New Year holiday in late January. The risk of capital outflow will persist not only because the US Federal Reserve is likely to continue to raise interest rates.