China Flash

November activity indicators point to moderating, though still strong growth momentum

Today's release of November activity indicators shows that growth momentum remains robust, with signs of some moderation in Q4. Specifically, industrial production (10.0% y/y vs. consensus: 10.1%), urban fixed asset investment (19.9% y/y ytd vs. consensus: 20.0%), and retail sales (13.7% y/y vs. consensus: 13.2%) came in line with expectations, with retail sales surprising to the upside (Charts 1-4). The data follow the release of robust November PMI (51.4) and exports (12.7% y/y) announced in recent days, along with benign inflation (3.0% y/y). However, today's data reveal some softening of investment as "mini" stimulus measures wear off and as the government seeks to address financial fragilities and over-capacity in some industries. In particular, some components of manufacturing investment such as the metal refinery sectors and general equipment slowed down (Chart 5). Based on activity indicators for October and November, it appears that Q4 GDP growth will easily be in line with our 7.6-7.7% y/y forecast, and in line with our 7.7% full-year growth projection for 2013. Looking ahead, we expect growth momentum to continue to H1 2014 before slowing down in H2, resulting in 7.6% growth for 2014. On the policy front, the 2-day annual Central Economic Work meeting convened today, and is expected to announce next year's growth target shortly, most likely in the 7.0-7.5% range.

- **Manufacturing activity softened somewhat,** with industrial production easing from 10.3% last month to a still-robust 10.0% y/y in November (in seasonally adjusted terms, industrial production rose by 0.76% m/m from 0.85% in October). The slowdown is attributable to certain sectors such as electricity and metal refinery, which are sensitive to the winding down of government "mini" stimulus measures and efforts to address over-capacity.
- **Domestic demand tilted toward consumption growth in November,** as retail sales surged and investment slowed. The rise in retail sales growth (13.7% y/y from 13.3% in October) may partially reflect a one-day online sales promotion on November 11, but nevertheless hints at improving consumption trends. Meanwhile, after strengthening in recent months manufacturing investment slowed to an estimated 14.1% y/y from 23.7% in October. As a partial offset, investment in the real estate sector and public transportation are picking up, and improvements in external demand may give rise to additional investment.
- **Exports surged in November,** pointing to a further pickup in external demand. According to data released on December 8 and reported in yesterday's Asia Flash, the rise in exports (12.7% y/y vs consensus: 7.0%) was broad-based, with demand from the US (17.7% y/y) and EU (18.4%) rising sharply. A deceleration of import growth (5.3% y/y vs. consensus: 7.6%) resulted in an especially large trade surplus of USD 33.8 bn (consensus: 21.2 bn USD), the largest in almost five years.
- **Headline CPI inflation remains stable, and PPI deflation is moderating.** CPI inflation, announced yesterday, fell to 3.0% y/y (consensus: 3.1%) in November on falling food price inflation (Chart 6). With inflation within the authorities' 3.5% tolerance level, the likelihood of a sharp tightening of monetary policy is reduced, although there remain concerns about rising financial fragilities in the form of rapid shadow bank lending and accelerating home prices. Looking forward, we expect average inflation to trend up gradually, but remain tame, at an average of 3.3% in 2014 from 2.7% in 2013, on stronger demand and reforms to administered prices of utilities and natural resources. Meanwhile, PPI deflation eased further (-1.4% vs prior -1.5%), helping firms to recover their profit margins.

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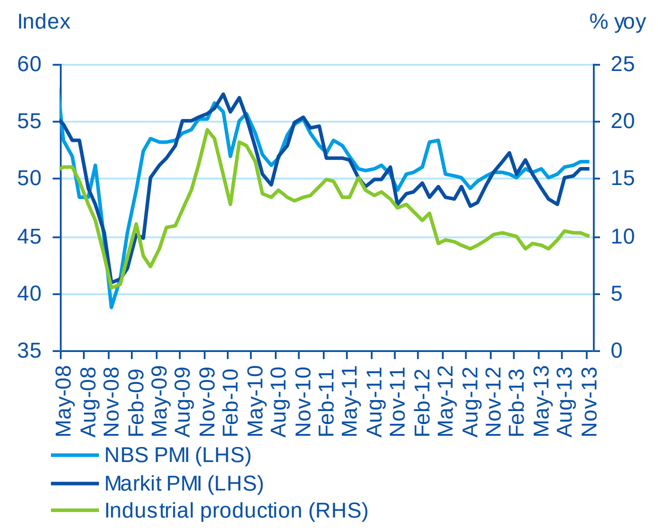
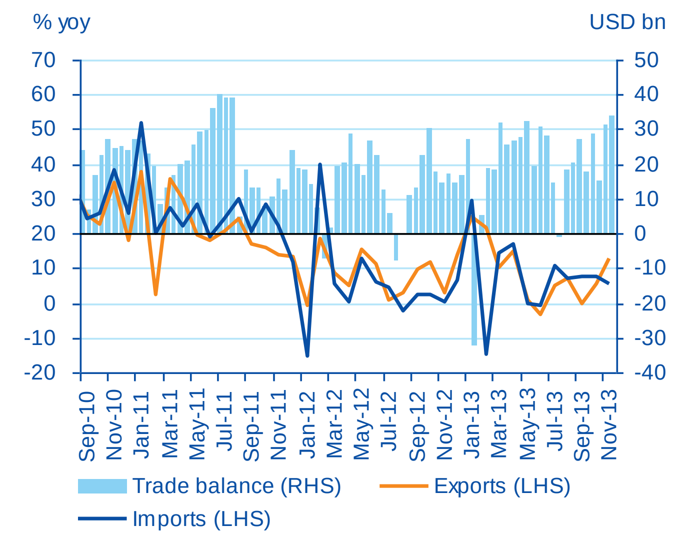
Chart 1
Industrial production is moderating slightly …



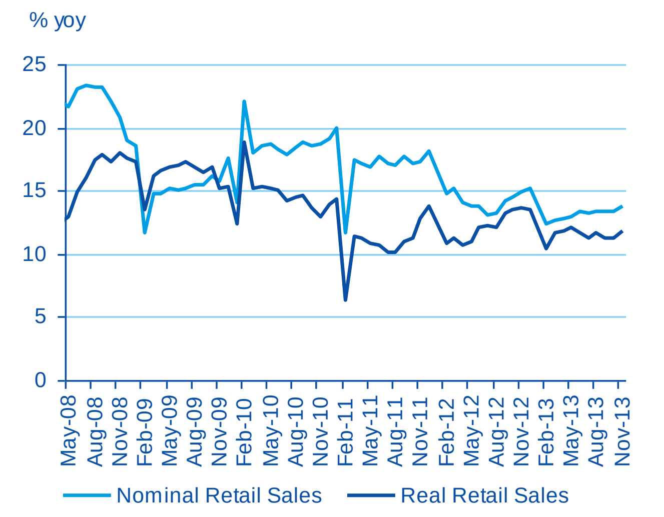
Source: CEIC and BBVA Research

Chart 2
…while exports pick up on improving external demand



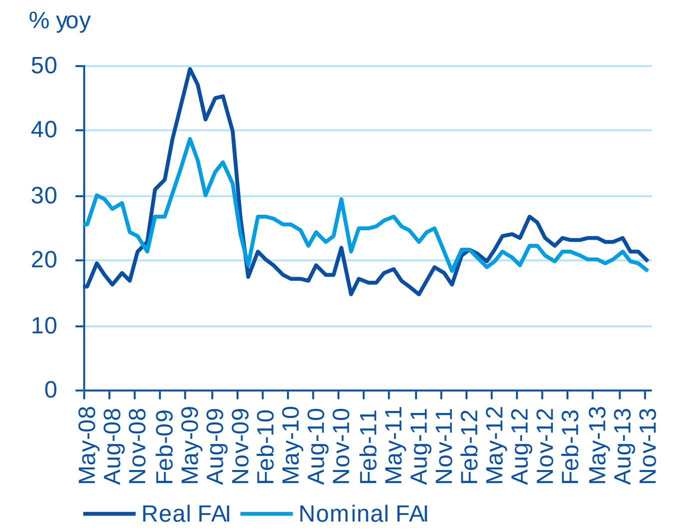
Source: CEIC and BBVA Research

Chart 3
Retail sales are showing strength …



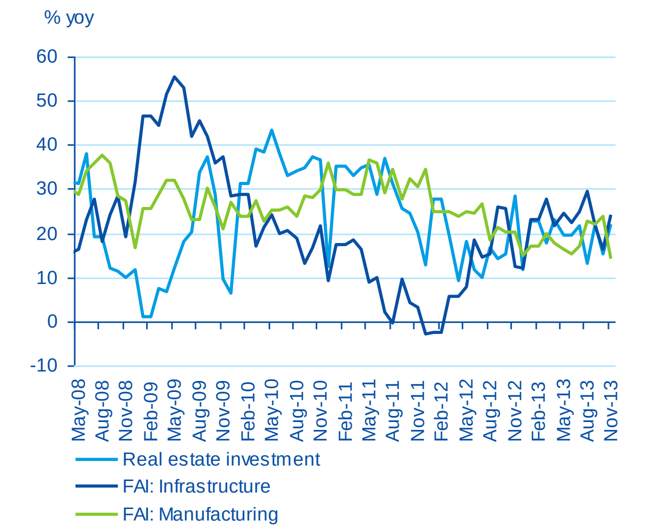
Source: Wind and BBVA Research

Chart 4
… as investment trends are moderating



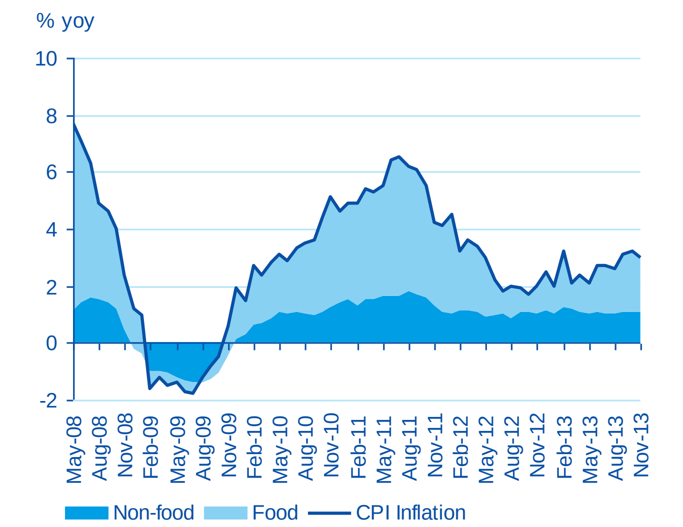
Source: CEIC and BBVA Research

Chart 5
Infrastructure and property investment is strengthening



Source: CEIC and BBVA Research

Chart 6
Inflation remains subdued



Source: CEIC and BBVA Research