



GDP Observatory

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China's Real GDP grew 6.1% yoy in Q1 2009 amidst a sharp global recession. The economy has bottomed and robust recovery can be expected in Q2.

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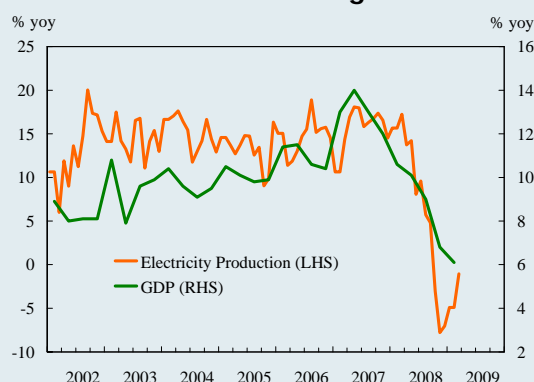
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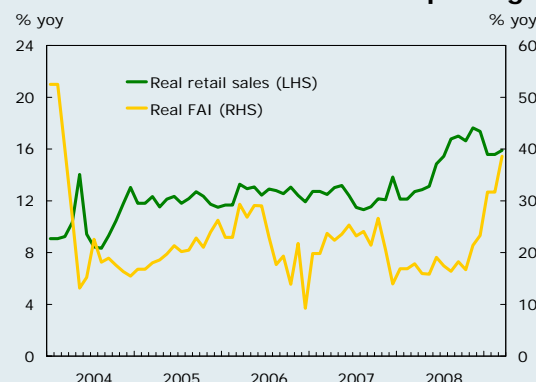
- China's real GDP grew by 6.1% in Q1 2009 amidst a sharp global recession. Although the Q1 growth has continued to weaken from 6.8% in Q4 2008, we think the economic slowdown has bottomed and strong recovery can be expected in Q2, as domestic policies are gaining more traction and the sharply deteriorating external environment has stabilized.
- The continued slide in Q1 growth was led by weak external demand, which in turn depressed economic activities and industrial profits. While the GDP by expenditure data are not available, the spokesperson of the National Bureau of Statistics commented that final consumption, investment and net exports contribute by 4.3, 2.0, and -0.2 percentage points, respectively, to the 6.1% GDP growth in Q1.

Chart 1: Real GDP growth



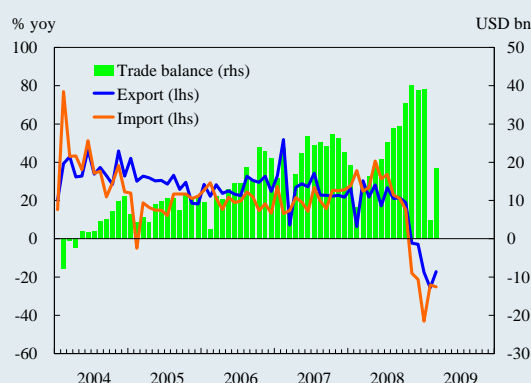
Sources: CEIC and BBVA estimates.

Chart 2: Domestic demand was picking up



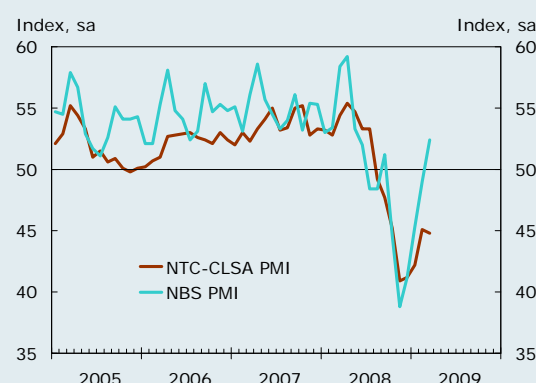
Sources: CEIC and BBVA estimates

Chart 3: External Trade



Sources: CEIC and BBVA estimates.

Chart 4: PMI



Sources: Datastream and BBVA estimates

- In addition to the Q1 GDP figure releases, there are several new data releases on March industrial production, retail sales, fixed asset investment (FAI), PPI, and CPI inflation. These data suggest that the economy has stabilized and steady rebound is on the way.
- Growth in industrial production picked up to 8.3% in March, from an averaged 3.8% in January-February, suggesting that the impact of the fiscal stimulus package and monetary policy ease has been working through the economy. We expect these policies are going to work in full tilt in the Q2. As a result, the rebound in Q2 could be stronger.
- Nominal retail sales slowed to 14.7% yoy in March from 15.7% in the first two months of 2009 on slowing household income growth, which moderated to 10.2% in Q1 2009 from 13.8% in Q4 2008. However, real retail sales remain robust, picking up slightly from 15.6% in January-February to 15.9% in March. Certain durable consumption goods and large ticket items such as passenger cars and electronics enjoyed robust increases, benefiting from the reduction of sales taxes on motor vehicles and the government subsidy policies to rural consumers.
- Thanks to the massive fiscal stimulus package, fixed asset investment pick up strongly by 30.3% in March, one of historical highs. This is about 3.8 percentage points higher than that in January-February. Meanwhile, growth in real FAI surged to 38.6% as more new projects benefiting from the fiscal stimulus have started in earnest.
- Given the considerable slack still remaining in the economy, CPI inflation continues to drop, falling by 1.2% yoy in March. However, the pace of CPI inflation appears to have slowed somewhat, compared with a decline of 1.6% in February. Falling food prices and high base effect contributed to the drop of CPI inflation. Meanwhile, producer price index fell by 4.6% in Q1, on sharp falls of raw material prices.
- We do not believe these price developments will necessarily lead to deflation in China, as M2 and credit growth have been growing at an unprecedentedly high and the economy is expected to expand strongly going forward. In fact, such price falls could have expansionary effect for both private consumption and production.
- Released earlier, China's exports continued to fall by 17.1% yoy in March, moderated from a sharp decline of 25.7% in February. However, imports dropped even more sharply by 25.1%. As a result, trade surplus continued to remain large at USD 18.6 billion.
- Looking forward, given the full implementation of the large fiscal stimulus package, we expect the Chinese economy to recover strongly in Q2. We therefore continue to maintain our call that China will be able to achieve its growth target of 8% this year because of the massive fiscal stimulus package, ample room for further monetary ease, and credible institutions.
- Although rumors have been circulating that China may apply additional stimulus package soon. Given our previous analysis on the impact of the fiscal package (China Watch, January 2009), we think the current package is adequate and no additional stimulus is needed at this juncture.
- Perhaps what China needs to do more now is to continue to engage in decisive reforms in the pension system, the education system, and the resident registration system. Indeed, the medical reform package just announced is one of such policy reform initiatives the market would like to see, as they are important measures in facilitating the Chinese economy to transform itself by relying more on domestic demand for growth.
- In addition, the authorities could do more to facilitate loans to small and medium enterprises (SMEs). Despite the rapid growth in credit in the first quarter, SMEs have yet to benefit from the relaxed monetary policy environment.