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Turning frosty

China's growth cools as the US-China trade war heats up

降温

随着中美贸易战的持续升温，中国的经济增长放缓

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Introduction

1. **The macro perspective**

2. **Financial derisking**

3. **A long-term perspective**

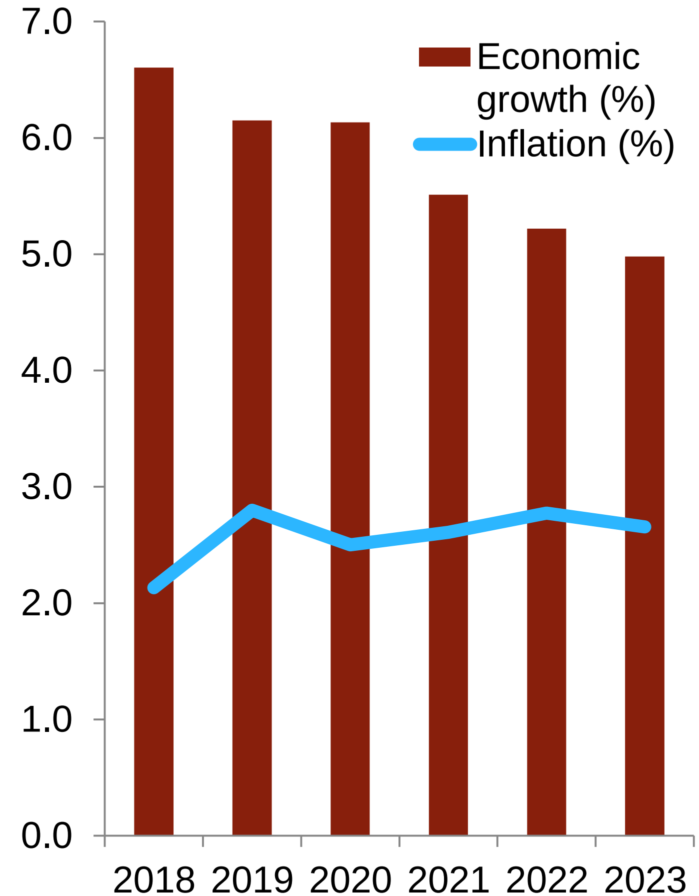
The macro perspective

Cooling growth, hardening politics

The economic challenges are mounting

- Financial “derisking” continues, despite trade war concerns
- Growing trend towards state control & SOE consolidation hurts productivity
- Centre-region fiscal rebalancing still needs to be tackled
- Demographic ageing is now weighing on GDP growth
- “Easy” gains from urbanisation are largely realised already

Real GDP vs consumer price inflation

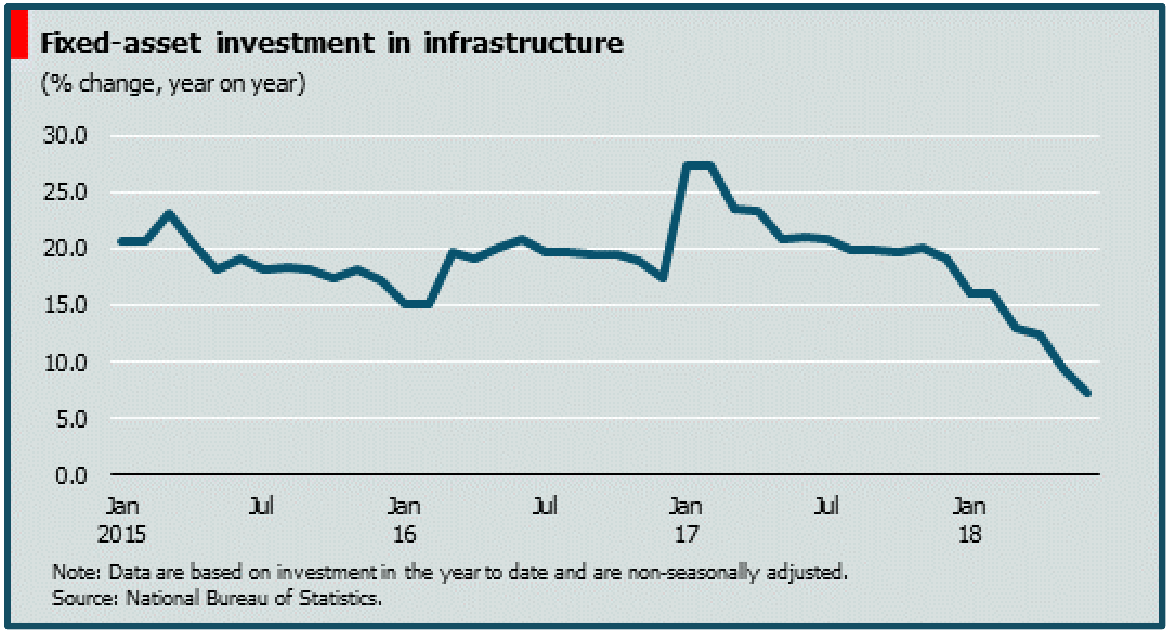


Source: The Economist Intelligence Unit.

Consumption – downgrading fears overplayed

- Retail sales growth has slowed
- Annual car sales set to fall in 2018; first time since 1990s
- Some “low-end” brands outperforming
- Concerns about “consumption downgrade”, but overplayed
- Incomes continue to climb ~8% p.a.
- We see real growth of 6.5% in household spending in 2019

Investment: slowing, slowing… contracting?

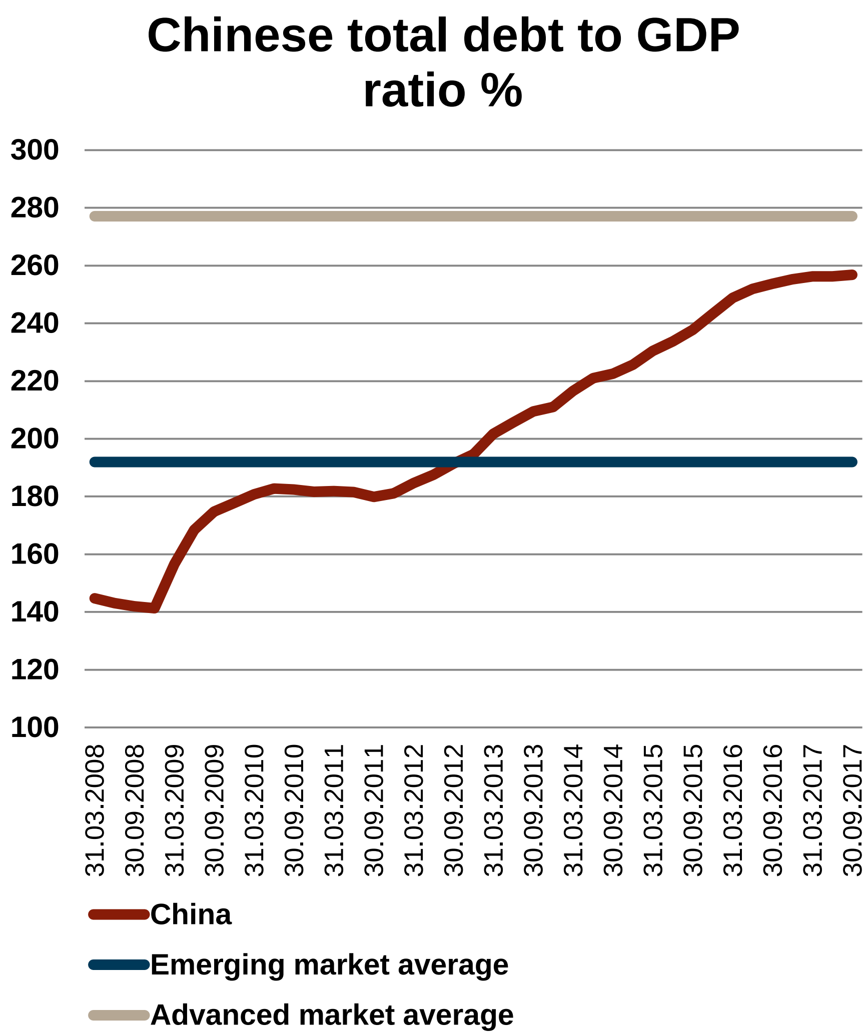


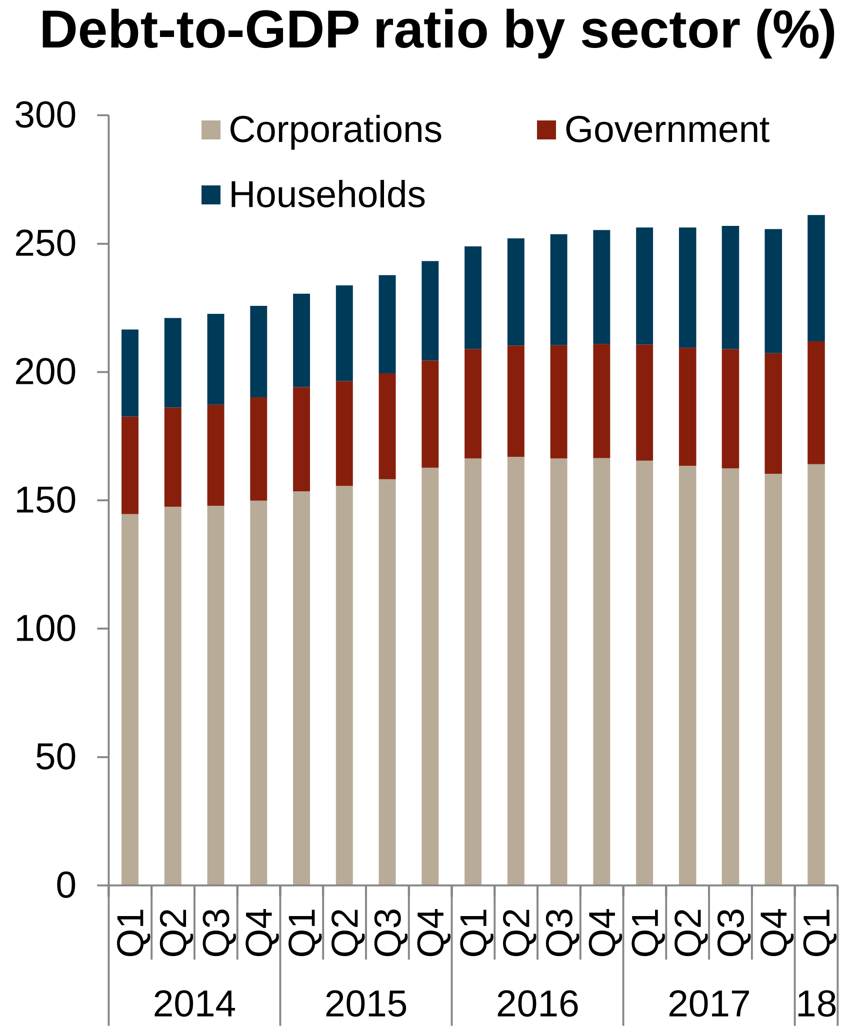
- Financing infrastructure increasingly challenging
- Government has loosened restrictions on local government infrastructure plans & stepping up bond issuance, but no return to 2016
- Property investment unlikely to surge again - but some exceptions

Financial de-risking

Not done yet

Efforts to rein in leverage lose traction



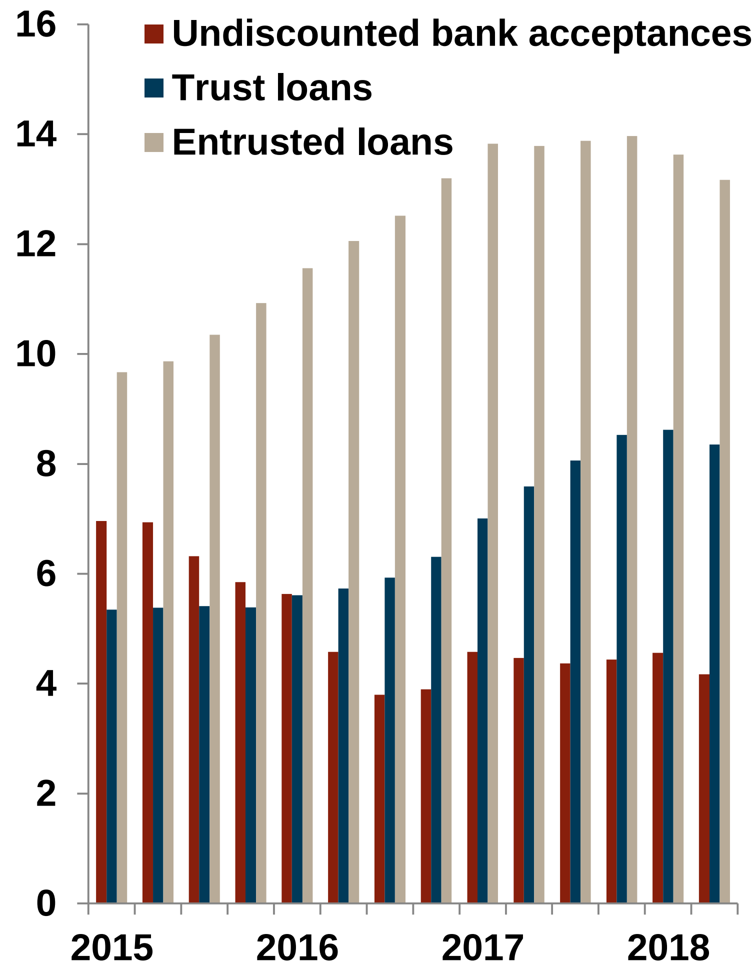


Source: BIS.

Central bank moves to squeeze out some risk

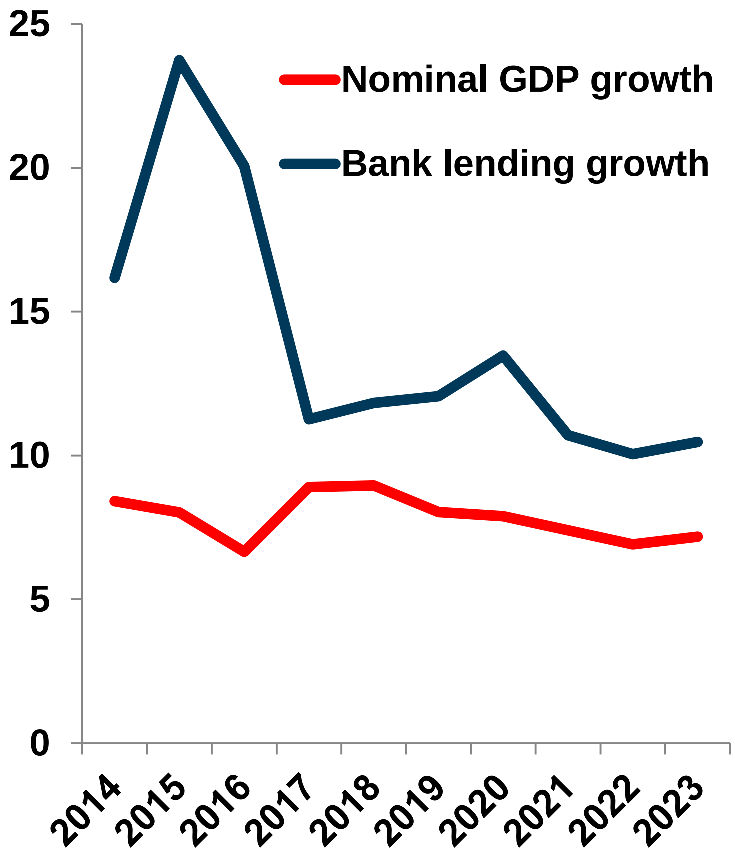
- PBC approach has been to allow innovation, for 1-3 yrs then tighten
- Served well in boosting fintech & developing competition for big SOCBs
- But risk has grown in less regulated parts of the financial sector
- Key areas of concern include: BADs; trust products; P2P lending
- Biggest risks are around exposure to property prices & local govt projects
- Fear of social instability => Implicit state guarantee

Stock of financing (Rmb trn, eop)



We see some progress, but not a lot

Lending will continue to outpace GDP



- Government has limited tolerance for slower GDP growth
- Expect progress on:
  - Increasing FDI in finance via liberalisation
  - Eroding implicit guarantees
  - Slowing loan growth
- Expect less headway on:
  - Reducing overall leverage
  - Tackling exposure to property & LGFVs
  - Transparency
  - Resolution of bad debt

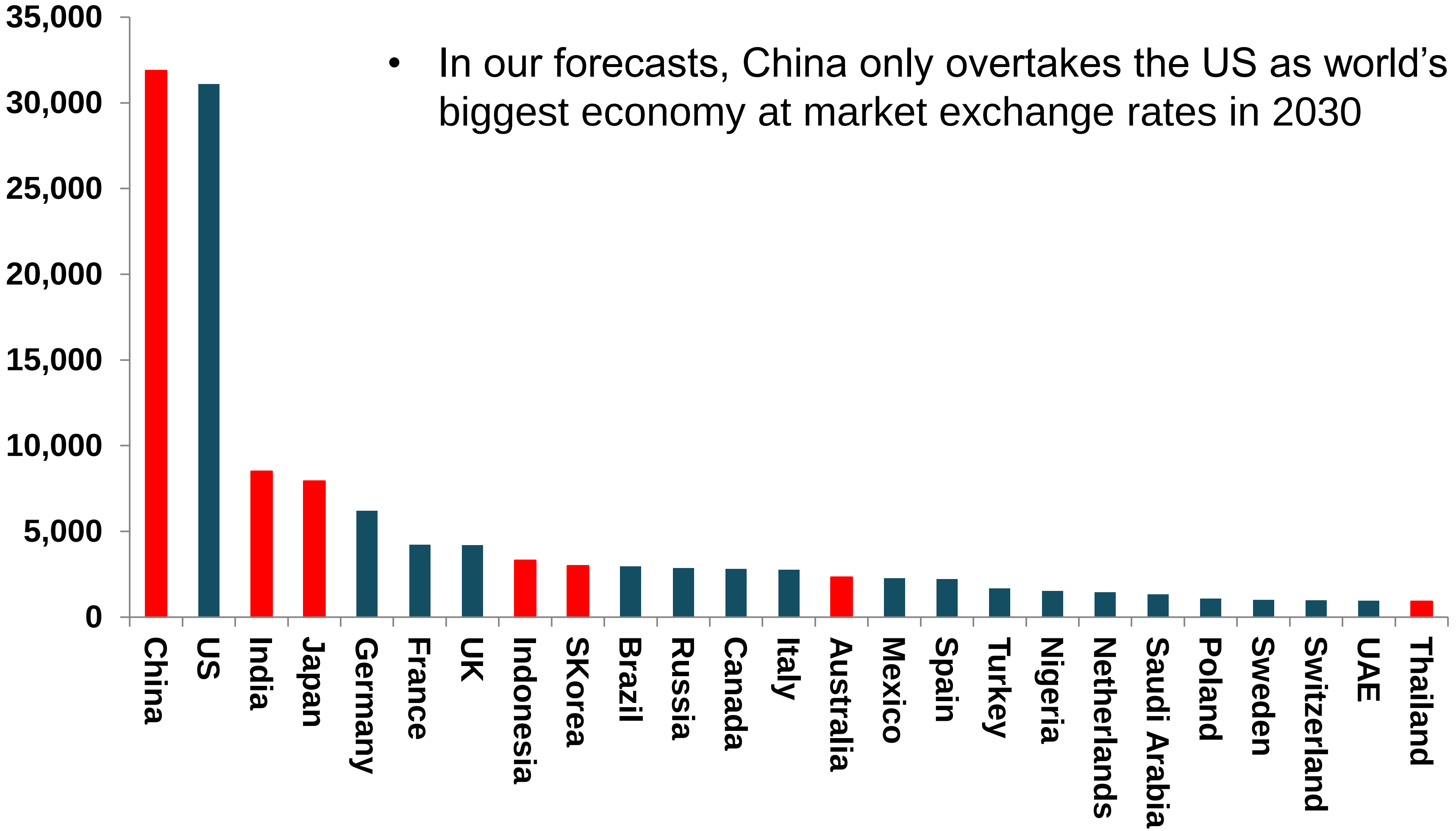
China vs US: Thucydides trap fears crystalize

- We see trade war being sustained until 2020 at least – probably longer
- US administration contains very hardliners & moderates. Trump a hardliner on trade
- Chinese leadership facing internal pressures too
- Trade tensions will seep into security clashes & broader strategic challenge
- Risk of new Cold War is high

A long-term perspective

Outlook still positive, but risks are rising

World's 25 largest economies in 2030



- In our forecasts, China only overtakes the US as world's biggest economy at market exchange rates in 2030

Nominal GDP, US$ trn. Source: The Economist Intelligence Unit.