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China – 2020 growth forecast cut further on Covid-19

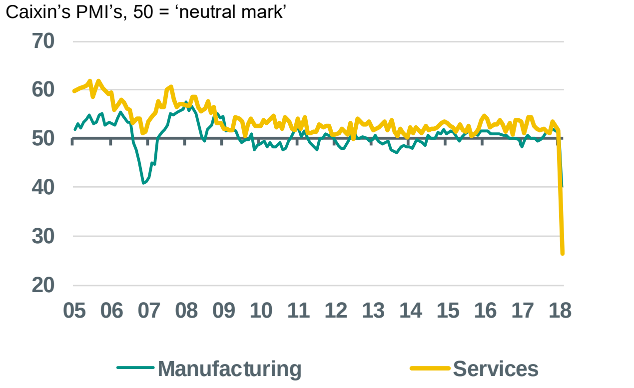
Arjen van Dijkhuizen
Senior Economist
Tel: +31 20 628 8052
arjen.van.dijkhuizen@nl.abnamro.com

- **PMIs illustrate severity of disturbances caused by Covid-19 crisis**
- **Rebound car sector hit by extended post-LNY lockdowns**
- **Continued frontloading of monetary and fiscal stimulus**
- **Adjusting our growth forecasts a bit further down**

1. PMIs illustrate severity of disturbances caused by Covid-19 crisis

Over the past days, the first monthly data for February were published that showed the impact of the corona crisis on activity. This reflects the draconian measures taken to stem the spread of the virus, such as extended post-Lunar New Year lockdowns and stringent mobility restrictions. All PMIs published by NBS and Caixin reached record lows. The services PMIs were hit most, illustrating that some parts of China's services sector (e.g. transportation, entertainment) form the epicentre of the shock. Caixin's services PMI published today fell by 25 points, to 26.5. The official PMI showed a similar unprecedented decline, from 54.1 in January to 29.6 in February. The manufacturing PMIs also showed sharp declines, but not as extreme as their equivalents for the services sector. The official manufacturing PMI dropped by 15 points, to 35.7. Caixin's manufacturing PMI fell by almost 11 points, to 40.3. The PMIs came in much weaker than consensus expectations. However, the sharp drop in these indicators reflects the fact that production capacity and supply chains have been severely distorted last month. We expect China's PMIs to improve sharply again in the coming months, as production capacity will be restored.

China's PMIs fall to record lows due to corona crisis

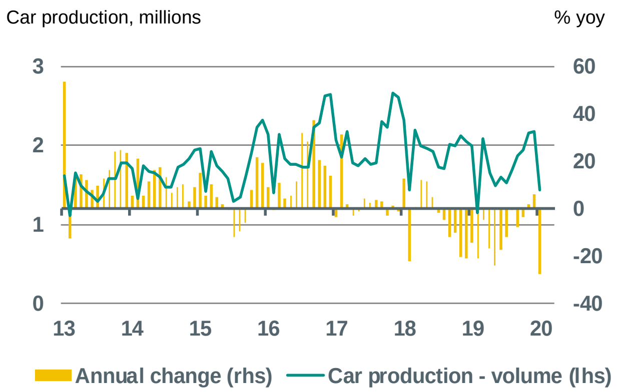


Source: Thomson Reuters Datastream

2. Rebound car sector hit by extended post-LNY lockdowns

The corona crisis is also preventing a rebound in the car sector, which has been one of the drags to Chinese growth last year (next to previous financial deleveraging and the US-China conflict). Annual growth of car production and sales was sharply negative in late 2018 and 1H19. This not only reflected weak domestic demand, but also problems with implementing new emission standards or the fading out of tax stimuli. However, in late 2019 a recovery started, with annual growth of car production even turning positive. The sharp drop in production and sales in January can be partly attributed to the Chinese New Year holiday break. However, the extended post LNY-lockdowns and other draconian measures taken will hit production and sales even more. Hubei province (where the virus originated, the number of infections and the death toll are the highest and the safety measures the most severe) accounted for 10% of Chinese car production in 2018. It will take quite some time before these car production facilities can operate normally again.

Chinese car production down again

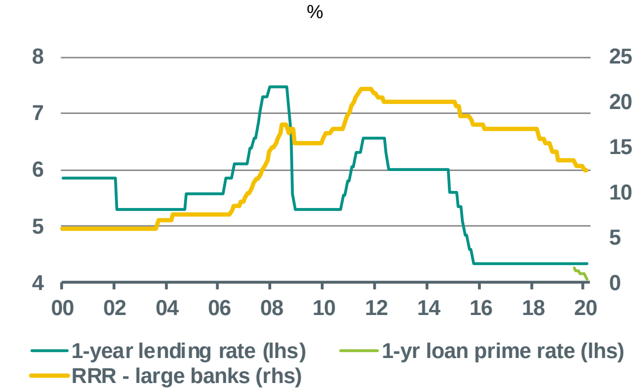


Source: Thomson Reuters Datastream

3. Continued frontloading of monetary and fiscal stimulus

To offset the fall-out from the corona crisis related disturbances, Beijing continues with piecemeal monetary and fiscal easing, while also providing targeted support to certain sectors and companies. Over the past weeks, the PBoC has continued with mini cuts of several policy interest rates. The central bank also announced to lower bank RRRs further: after reducing them by 400 bp in 2018-19 and 50 bp (to 12.5%) in January 2020, we expect another 150 bp in RRR cuts in the course of this year. On the fiscal front, the authorities had already frontloaded and raised quota for local government bond issuance. In January, that triggered a sharp rise of new lending. The government also announced special tax breaks as well as targeted state support for sectors most hit by the corona crisis, such as the airline industry. Meanwhile, macroprudential regulation is being relaxed, as the PBoC and the CBIRC have for instance allowed banks to delay the recognisition of bad loans extended to SMEs suffering from the corona crisis. We expect the Chinese authorities to continue with these policies to cushion the blow from the headwinds created by the corona crisis.

PBoC to frontload further monetary easing



Source: Thomson Reuters Datastream

4. Adjusting our growth forecasts a bit further down

Earlier this week, we have adjusted our global growth forecasts downwards again, as we have seen a further escalation in the spreading of the Covid-19 virus beyond China (see here for more background). We have cut our annual growth forecasts for the key economies a bit further down to reflect this, by another 0.2-0.3 ppts. For China, we still assume that the disruptions from the corona crisis will prove temporary, and that economic activity will normalise in the course of March. We now foresee negative qoq growth in Q1, still followed by a clear pick-up in quarterly growth in subsequent quarters. That pick-up is partly helped by the frontloading of stimulus, targeted support for certain sectors and companies and a relaxation of macroprudential policies, as mentioned above. All in all, we have revised our annual growth forecast for 2020 a bit further down, to 5.3% (from 5.5%; and down from 5.8% pre-corona crisis). Reflecting spillover effects from a stronger second half of the year, we have revised our 2021 growth forecast a bit higher, to 6.0% (from 5.8%; and up from 5.6% pre-corona crisis).

Chinese stock market quickly recovers from corona dip

CSI 300 Index

Source: Bloomberg

Key forecasts for the economy of China

	2017	2018	2019e	2020e	2021e
GDP (% yoy)	6.8	6.7	6.1	5.3	6.0
CPI inflation (% yoy)	1.5	1.9	2.9	3.5	2.5
Budget balance (% GDP)	-3.8	-4.2	-4.5	-4.5	-4.5
Government debt (% GDP)	17	15	18	22	24
Current account (% GDP)	1.6	0.4	1.0	0.5	0.5
Gross fixed investment (% GDP)	42.9	43.1	42.1	41.6	40.5
Gross national savings (% GDP)	46.3	45.2	45.1	43.6	41.9
USD/CNY (eop)	6.5	6.9	7.0	7.0	7.1
EUR/CNY (eop)	7.8	7.8	7.8	8.1	8.5

Economic growth, budget balance, current account balance for 2019, 2020 and 2021 are rounded figures

Source: EIU, ABN AMRO Group Economics

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