CCXI
Macro-economy Research

Thematic Study

October 25, 2019

The Economy Recovers Marginally under Downward Pressure

- 2019 Q3 Macro-economic Review and Outlook

Overview

✧ **Economic performance: economic growth slowed from quarter to quarter, showing marked signs of marginal recovery under the stable growth policy**

Though China's economy faced a number of unfavorable factors in 2019 Q1-Q3, China managed to keep its economy within the government's target range for annual growth as the stable growth policy worked effectively. GDP grew by 6.2% in Q1-Q3 on average, and at 6.0% in Q3. In spite of the overall weakness of Q3 data, the economic data for September showed signs of marginal recovery of the macro-economy as the policy efforts were strengthened to ensure stable growth. However, it is noteworthy that, in spite of the current signs of marginal economic recovery, the overall weakness on both supply and demand sides did not improve fundamentally. The economy is still under downward pressure.

✧ **Internal and external environment: external uncertainties remain there, with the domestic policy to ensure stable growth expected to further strengthen**

- Global economy and trade continue to soften and the US-China trade frictions have eased with limited optimism. China's economy is still exposed to external uncertainties.
- The stable growth policy will continue to work under the pressure of economic downturn. The monetary policy still has room for further interest rate cuts and reserve requirement ratio (RRR) reduction. Financial supervision will remain focused on stable supervision.

✧ **The economy may improve temporarily in Q4, yet still under downward pressure**

- **The economic activity has signaled short-term weak pickup, suggesting a marginal recovery in Q4.** September data revealed some positive signals in the economy activity. They will likely bolster the Q4 economic performance to stage a better-than-expected marginal recovery in Q4.
- **Internal and external pressures still weigh on the Chinese economy.** The global economy continues to weaken, making foreign demand a weaker driver of economic growth. Real estate investment is likely to moderate in 2020 under housing curbs. Given the weak demand, enterprises' restocking gives a limited boost to the economy. Industrial and service sectors undergo a structural deterioration, showing escalating recessional structural changes and softening structural upgrades.

✧ **Summary:**

In spite of the subdued economic data in Q1-Q3, the macro-economic data in September showed some positive changes, including the mild marginal recovery spurred by the stable growth policy. Taking into account the low-base effect, Q4 is estimated to see stronger-than-expected economic growth and stage a temporary recovery on a weak footing. We maintain our forecast of 6.1% for annual economic growth. Meanwhile, the economy remains under a downward pressure. The weakening global economy may further drag on the Chinese economy. Though real estate is somewhat resilient under tight regulation, its support for investment and the larger economy will become weaker in 2020. Enterprises' restocking still has limited effect in driving the economy, which undergoes deceleration in structural upgrades and escalation in recessional structural changes. We should not be too optimistic about the economic performance in 2020, especially in 2020 H2.

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I. Economic Performance: economic growth slowed from quarter to quarter, showing marked signs of marginal recovery under the stable growth policy

Though China's economy faced a number of unfavorable factors in 2019 Q1-Q3, including structural adjustments and release of contradictions at home, as well the slowdown in global economy and trade, uncertainties in international trade environment and US-China trade frictions, China managed to keep its economy within the government's target range for annual growth as the stable growth policy worked effectively. GDP grew by 6.2% in Q1-Q3 on average, and at 6.0% in Q3. In spite of the overall weakness of Q3 data, the economic data for September showed signs of marginal recovery of the macro-economy as the policy efforts were strengthened to ensure stable growth. September saw stabilization in infrastructure investment alongside with the early signs of stabilizing industrial production and manufacturing. Aggregate financing to the real economy recovered with an improved credit structure, and economic leading indicators also showed better performance. The economy is expected to beat expectations slightly in Q4. However, it is noteworthy that, in spite of the current signs of marginal economic recovery, the overall weakness on both supply and demand sides did not improve fundamentally. The economy is still under downward pressure.

Table 1: China's Core Macroeconomic Indicators in 2018-2019

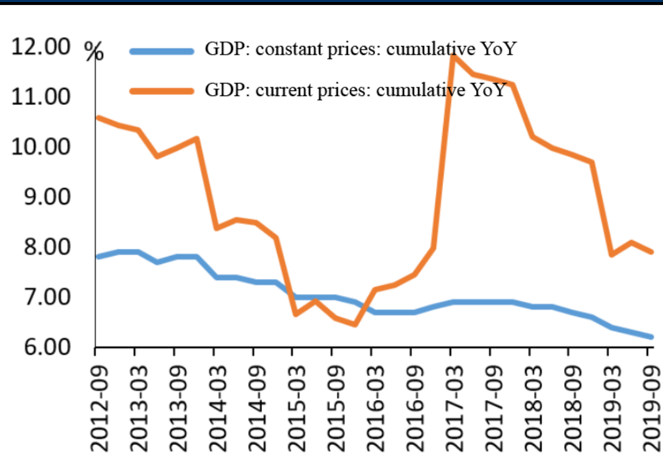
Core indicator	2018 (accumulative)				2019 (accumulative)			Change
	Q1	H1	Q1-Q3	Annual	Q1	H1	Q1-Q3	
GDP cumulative YoY (%)	6.8	6.8	6.7	6.6	6.4	6.3	6.2	↓
Industrial value added, YoY (%)	6.8	6.7	6.4	6.2	6.2	6.0	5.6	↓
Investment in fixed assets (%)	7.5	6.0	5.4	5.9	6.3	5.8	5.4	↔
Total retail sales of consumer goods (%)	9.8	9.4	9.3	9.0	8.3	8.4	8.2	↓
Exports, YoY (%)	13.73	12.52	12.22	9.88	1.40	0.10	-0.1	↓
Imports, YoY (%)	19.44	20.06	20.17	15.84	-4.80	-0.30	-5.0	↓
Trade surplus (USD100 million)	448.5	1,354.07	2,194.01	3,511.41	763.10	1,811.6	2,984.3	↑
M2, YoY (%)	8.2	8	8.3	8.1	8.6	8.5	8.4	↑
Aggregate financing to the real economy (RMB100 million)	58,535	100,691	154,027	192,584	81,800	132,300	184,900	↑
CPI (%)	2.1	2.0	2.1	2.1	1.8	2.2	3.0	↑
PPI (%)	3.7	3.9	4.0	3.5	0.2	0.3	-1.2	↓

(Note: ↓, ↑ and ↔ indicate that an indicator in 3Q 2019 recorded a decline, increase or flatness over the same period of 2018)

i. The economy further weakened under pressure and depended more on foreign demand

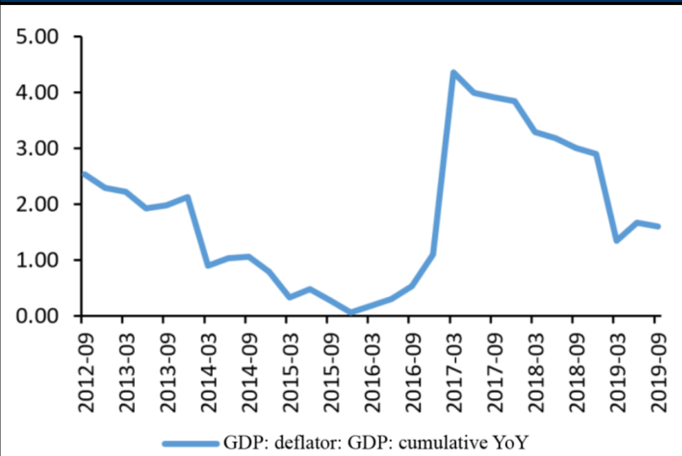
Real GDP grew 6.2% YoY in Q1-Q3, down 0.5 ppt YoY and 0.4 ppt from the end of last year. In terms of quarterly performance, Q1, Q2 and Q3 saw a YoY growth rate of 6.4%, 6.2% and 6% respectively. Both demand and supply remained weak and GDP continued to slow down under pressure. Alongside the pullback in GDP deflator, nominal GDP growth fell from 8.08% in H1 to 7.90%, down 2.01 ppts YoY. **By economic sectors,** the primary and secondary sectors showed weakening growth. The tertiary sector maintained stable growth and kept improving structurally. **By demand components,** net exports pulled back YoY and its cumulative GDP contribution rate fell by 1.1 ppts from H1, yet still the highest in the same period of recent years. This year, the economy's rising dependence on foreign demand deserves intense attention amid subdued domestic demand. The GDP contribution rate of consumption and investment rebounded by 0.4 ppt and 0.6 ppt from H1, but down 17.5 ppts and 12 ppts YoY, respectively.

Fig. 1: Cumulative YoY Changes in GDP at Current and Constant Prices



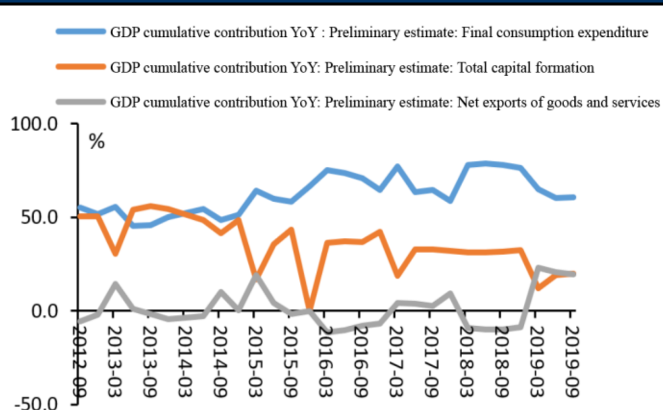
Source: CCXI Macro Interest Rates Database

Fig. 2: Trends in GDP Deflator



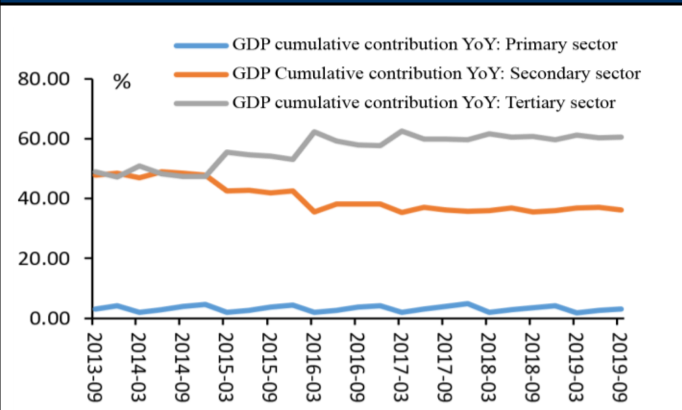
Source: CCXI Macro Interest Rates Database

Fig. 3: Trends in Contributions of Three Demands



Source: CCXI Macro Interest Rates Database

Fig. 4: Trends in Contributions of Three Sectors

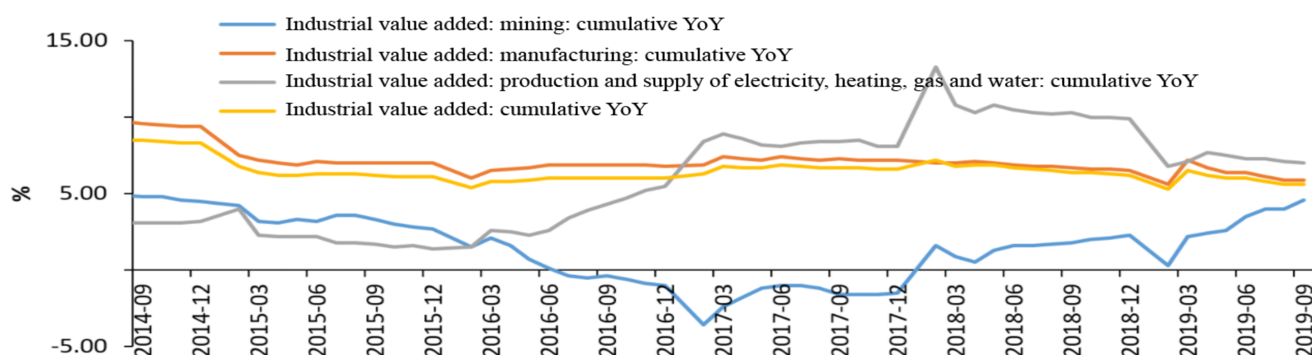


Source: CCXI Macro Interest Rates Database

ii. Industrial value added fell YoY but improved in September alone, likely to stabilize mildly in Q4

Industrial value added improved marginally with softness in end demand and uncertainty. In Q3, the value added of industrial enterprises above designated scale increased by 5.6% YoY, down 0.8 ppt YoY, with the cumulative YoY growth rate down 0.4 ppt from H1. Of the three categories, mining picked up from H1 and the same period of last year. Manufacturing and production and supply of electricity, heating, gas and water slowed down from H1 and the same period of last year. In September alone, however, industrial and manufacturing value added still picked up showing signs of temporary stabilization amid the production restrictions imposed on some enterprises before the National Day holiday. Given the current low level of finished goods inventory, the restocking demand of industrial enterprises may translate into mild recovery. But the industrial output cuts in the heating season imposed by environmental authorities may place a pressure on industrial and manufacturing production.

Fig. 5: Trends in Industrial Value Added



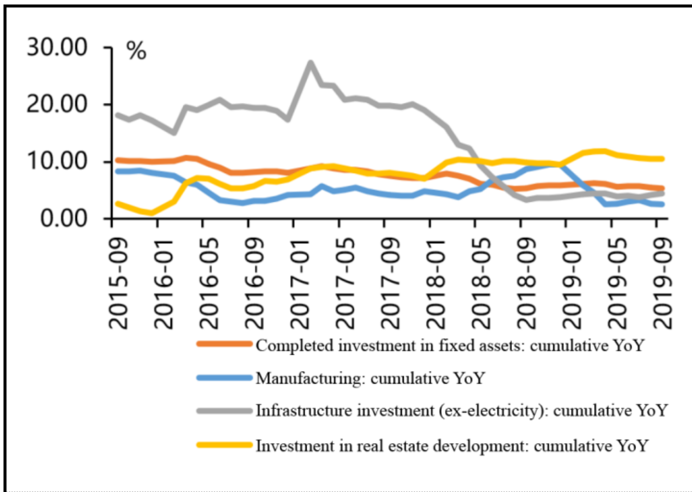
Source: CCXI Macro Interest Rates Database

iii. Infrastructure and real estate continued to bolster investment, which is very likely to remain low due to a number of factors

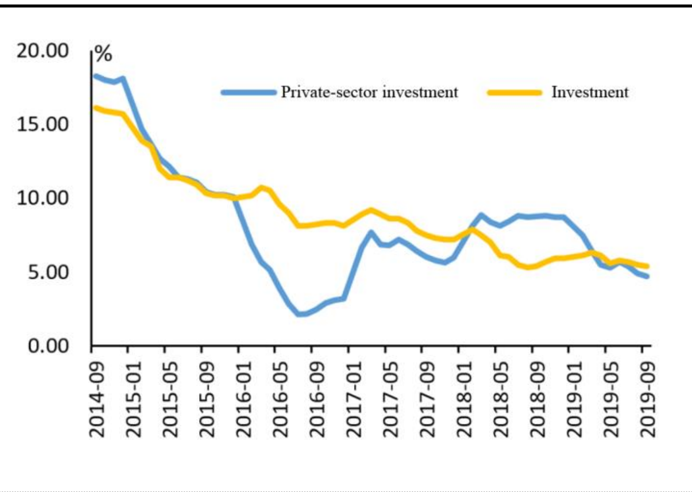
Infrastructure recovered on the stable growth policy, real estate investment remained resilient and investment was flat with one year ago. Investment increased by 5.4% YoY in Q1-Q3, 0.4 ppt slower than H1 but flat with the same period of last year. The continued recovery in infrastructure investment stimulated by the stable growth policy and the inertial fast growth in real estate investment bolstered fixed asset investment in H1. Investment in manufacturing remained sluggish. Investment in manufacturing increased accumulatively by 2.5% YoY, flat with April at the lowest level on record. This was a drag on fixed asset investment.

Infrastructure is expected to recover mildly, real estate investment will continue to edge down slightly and investment is likely to stay low. The State Council required at its early September executive meeting that all special bonds within the quota should be issued completely by the end of September and the proceeds should be allocated to the target projects by the end of October. In addition, some new quotas for special bonds were also issued at the meeting. Infrastructure investment is expected to further beef up fixed asset investment in Q4 and continue to recovery mildly. Though real estate investment remained resilient during Q1-Q3, and currently the housing sales, starts and construction all demonstrate certain resilience, real estate investment still face a downward whether pressure amid tight property curbs. In addition, whether organic investments including private-sector investment and manufacturing investment will improve or not remains uncertain amid the subdued demand. Overall, fixed asset investment is expected to stay low in the foreseeable future.

Fig. 6: Investment Slowed down, Real Estate Investment Remained High	Fig. 7: Trends in Private Investment in Fixed Assets



Source: CCXI Macro Interest Rates Database

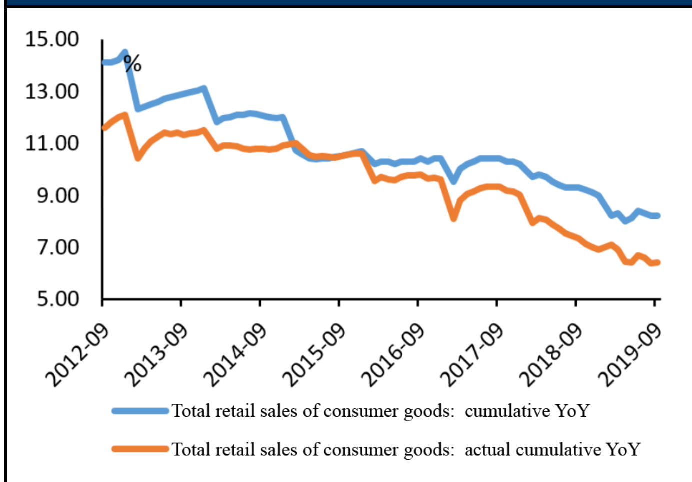


Source: CCXI Macro Interest Rates Database

iv. Total retail sales of consumer goods remained subdued, likely to recover modestly for a while as the automobile consumption becomes a smaller drag

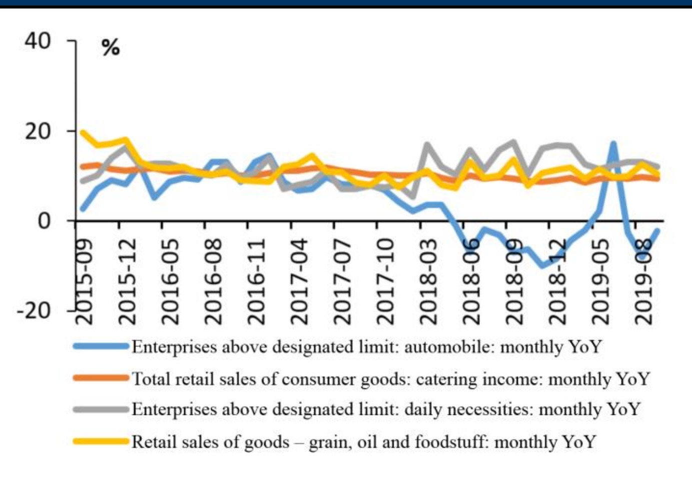
Sluggish automobile consumption dragged down total retail sales of consumer goods, coupled by moderating upgrades in rural consumption. In Q1-Q3, total retail sales of consumer goods increased by 8.2% YoY, down 1.1 ppts YoY, or down 0.2 ppt from H1, suggesting overall weakness in consumption. By region, in spite of faster growth in rural consumption than urban consumption due to low base and poverty alleviation efforts in rural areas, the growth in rural retail sales of consumer goods and the online retail sales decelerated faster than the overall average. The rural consumption upgrading was slowing down. The consumption stimulus policy is bottlenecked by the heavy debt burden in the housing sector. However, automobile consumption may become a smaller drag on total retail sales of consumer goods in Q4 as vehicle production and sales are recovering mildly now, which is expected to sustain mild growth in total retail sales of consumer goods for a while.

Fig. 8: Trends in Total Retail Sales of Consumer Goods



Source: CCXI Macro Interest Rates Database

Fig. 9: Trends in Major Consumer Goods



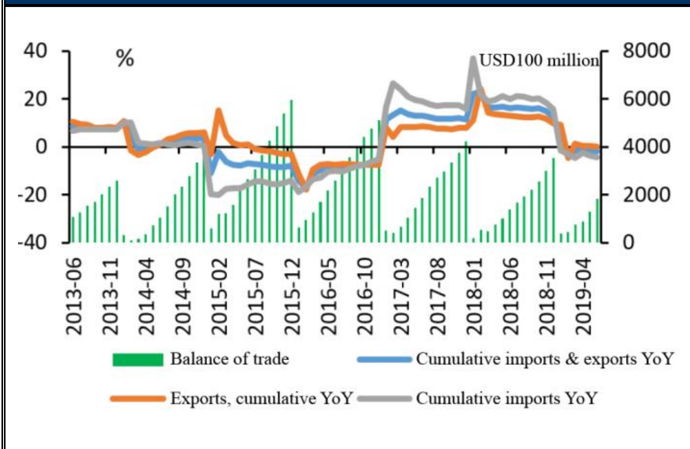
Source: CCXI Macro Interest Rates Database

v. Both imports and exports weakened but recessional surplus expanded, with imports expected to improve in the short term on eased trade conflicts

Imports and exports weakened on subdued demand with an expanding recessional surplus. Total imports and exports fell by 2.4% YoY in Q1-Q3. Specifically, exports fell by 0.1% YoY, down 12.1 ppts from the same period of last year. It is unlikely to be upbeat on exports amid subdued global demand at present. Imports slipped by 5.0% YoY, showing a continued drag on imports from insufficient demand alongside the RMB depreciation run starting in August. Trade surplus was USD298.4 billion, expanding significantly by 34.8% YoY and showing a marked characteristic of recessionary trade surplus.

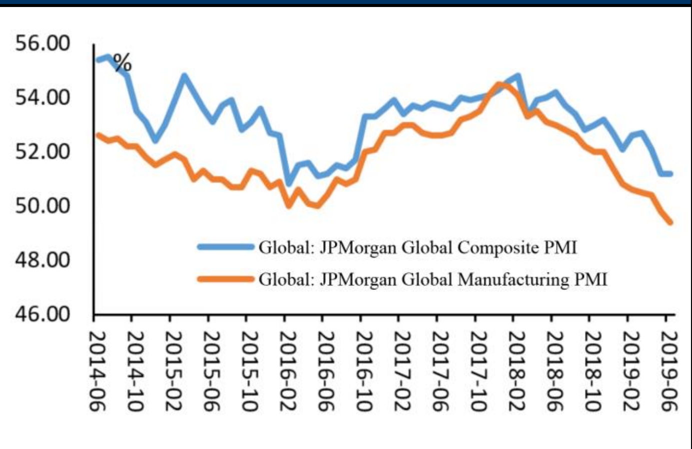
Exports are likely to improve in the short term on eased US-China trade frictions, with imports and exports still under pressure from subdued global economy. Looking ahead, the World Bank further lowered its growth forecasts for the world economy and expected it to stabilize in 2021, provided that no major economic conflicts occur in the global economy. In addition, the United States, Japan and Europe all have seen their PMI receding. The soft foreign demand cannot improve in the short term will still weigh on Chinese exports. However, upbeat news have come from the latest US-China trade talks. The two sides have reached a phase-one trade agreement. The eased US-China trade tensions will abate the pressure on exports to some degree. Overall, though the eased US-China trade tensions have softened the ongoing exports downturn, the global demand remains subdued. Exports are very unlikely to improve fundamentally against the backdrop that the World Bank has lowered its economic expectations for all major trade partners of China. In terms of imports, short-term imports may improve slightly on the stabilizing RMB exchange rate and the substantive consensus reached in the US-China trade talks on purchase of agricultural products and opening-up.

Fig. 10: Export Growth Retreated, Import Growth Further Weakened



Source: Compiled by CCXI

Fig. 11: JPMorgan Global Manufacturing PMI Continued to Fall



Source: Compiled by CCXI

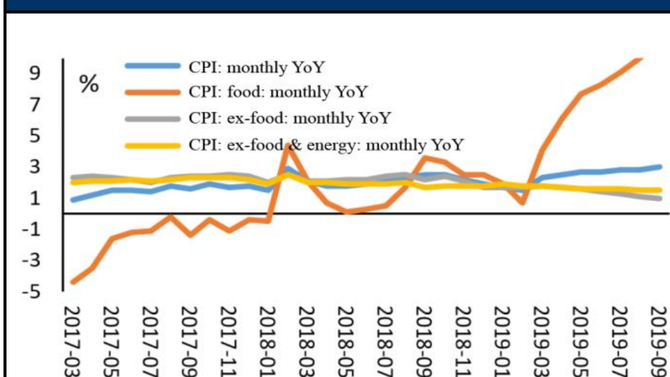
vi. CPI and PPI remained divergent, but either inflationary or deflationary pressure is under control

Pork price hikes pushed CPI up to a six-year high, but CPI was stable and PPI decline continued to gain pace. CPI rose by 3.0% in September YoY, up 0.2 ppt from the previous month. The swine fever has resulted in a very big shortage in pork supply that cannot be filled over a short period. The short-term expansion in imports and the release of pork from state reserves had limited effect in curbing pork prices, which rose steeply. Pork alone contributed 1.65 ppts or 55% of CPI. Ex-pork CPI was low. Non-food components of CPI showed six rises and one drop. YoY decline in PPI gained pace due to weak demand and subdued carryover effects. PPI fell by 1.2% in September YoY, up 0.4 ppt from the previous month. International oil prices fell rapidly following a pickup. Prices went down faster than a year ago in oil and

natural gas and ferrous metal industries. PPIRM decelerated faster YoY, and its spread with PPI stayed flat with one year ago.

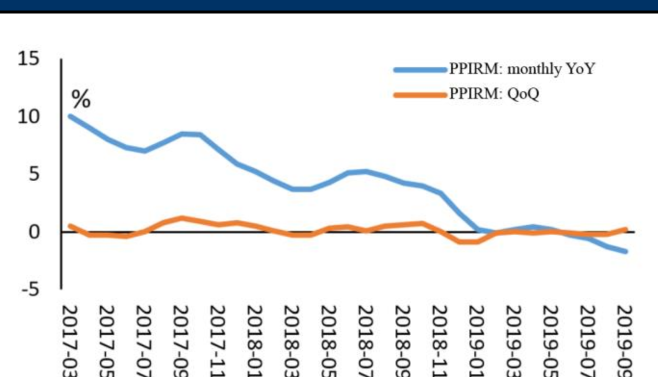
CPI may return to the “2” range, while PPI has limited room for further decline As for CPI, recent high-frequency data indicate continued hike in pork price. But the pork price inflation may soften due to rising supply of substitute meat and egg against the backdrop of earlier increase in pork supply from state reserves and receding demand for pork with soaring prices. In addition, the CPI carryover effect further subdued in October compared with September, and non-food CPI and service prices are unlikely to reverse the trend of weakening. Thus CPI may return to the “2” range. Continued inflation will be a low probability. As for PPI, PPI inflation continued to moderate as expected. New construction orders surged in September. Iranian oil tanker explosions on October 11 partially affected crude oil supply, expected to ripple over to international oil prices. Backed by these factors, PPI is unlikely to further drop in October. The deflationary pressure remains under control. Due attention should be paid to the impact on PPI from changes in real estate financing policy, whether the industrial output cuts in the heating season go beyond expectations and whether new special bond issues can be accelerated this year.

Fig. 12: CPI Remained High in September, with Food CPI Continuing to Rise



Source: Compiled by CCXI

Fig. 13: PPIRM Picked Up QoQ But Went Down YoY

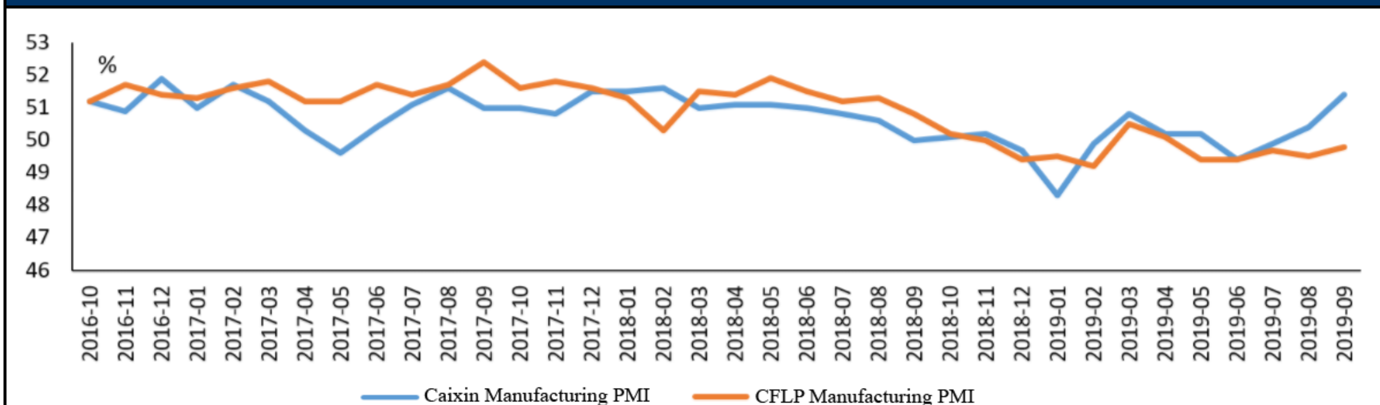


Source: Compiled by CCXI

vii. Supply and demand improved mildly, with manufacturing climate restored somewhat

Manufacturing PMI picked up mildly on improvements in both supply and demand. Manufacturing PMI was 49.8% in September, up 0.3 ppt from the previous month and still below the boom-or-bust line. But the overall climate improved as compared with August. The demand side improved modestly. The new exports order index picked up and domestic demand recovered modestly, thanks to the lessening reliance on exports to the United States and the delay of tariff increase announced by the United States in September. On the supply side, production expanded faster and product sales made a turn for the better amid the modest recovery in demand, showing continuous de-stocking. In addition, the production activity expectations index rose by 1.1 ppts to 53.3%, suggesting stronger optimism of enterprises. In addition, Caixin PMI recorded 51.4%, up 1 ppt from August, the highest since March 2018 following a three-month rally. It went divergent from the CFLP PMI, mainly due to stronger rise in the new orders and output components of Caixin PMI. The services and construction climates continued to be divided. Non-manufacturing PMI edged down slightly. Non-manufacturing PMI inched down by 0.1 ppt to 53.7% in September, yet still in an overall uptrend. The services business activity index rebounded by 0.5 ppt to 53.0% while the construction climate subdued, albeit still within a medium-to-high range.

Fig. 14: Divergent Trends in CFLP PMI and Caixin PMI



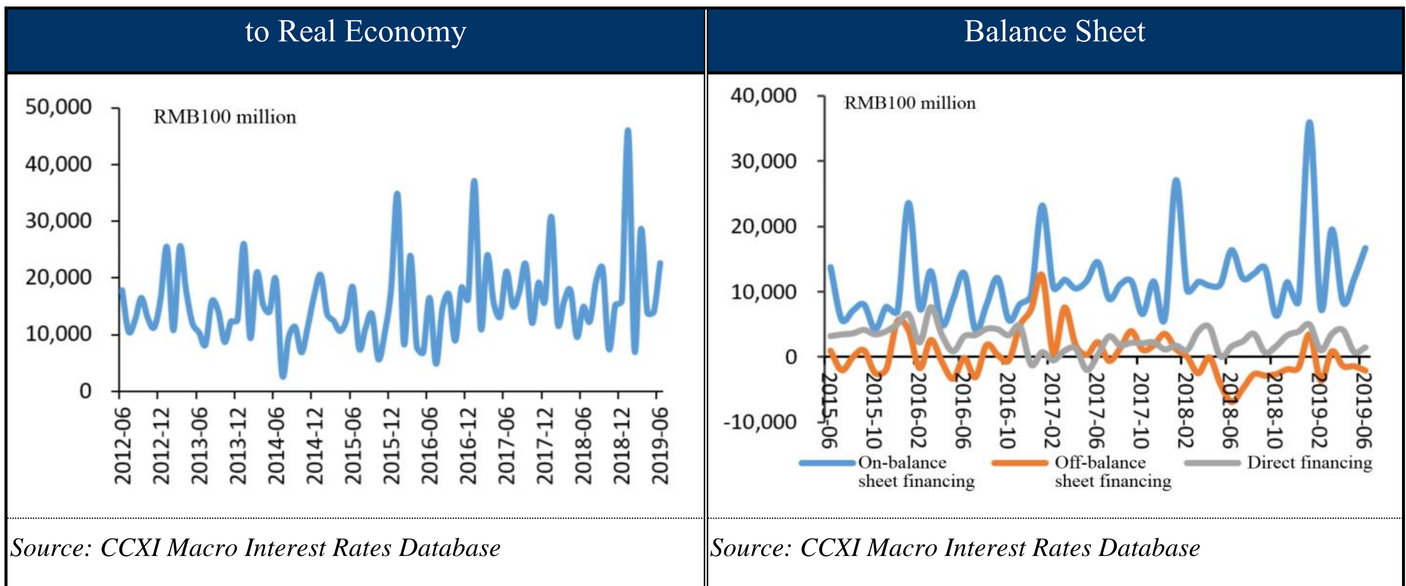
Source: Compiled by CCXI

viii. M2 and aggregate financing maintained overall stability with an improved credit structure

Aggregate financing rebounded and structurally improved in an easy credit climate. M2 increased by 8.4% YoY in Q1-Q3, up 0.1 ppt YoY or 0.3 ppt from the end of last year. New aggregate financing to the real economy stood at RMB18.49 trillion, an increase of RMB3.09 trillion over the same period of last year. On-balance-sheet financing increased by RMB13.82 trillion, a YoY increase of RMB1.21 trillion, showing continued strong growth. Under regulatory marginal adjustments, the drop in off-balance-sheet financing moderated. Off-balance-sheet financing decreased by RMB1,275.6 billion, down RMB1,027.9 billion YoY, showing an obviously slower contraction. With interest rates staying stable at lows, direct financing increased by RMB2,624.3 billion, RMB674.7 billion more than the increase recorded one year ago, indicating improved financing to the real economy. Net proceeds of local government special bonds stood at RMB2.17 trillion, up RMB470.4 billion YoY. In the context of a prudent monetary policy and financial supervision sticking to structured credit easing, aggregate financing to the real economy structurally improved in Q3 and medium- and long-term loans to businesses staged a marked rally, either YoY or QoQ. That means enterprises may be not over-pessimistic about futures and also indicates to some extent the resilience of China's economic growth.

Fig. 15: Monthly Trends in New Aggregate Financing	Fig. 16: Trends in Direct Financing on vs. off

to Real Economy	Balance Sheet



Source: CCXI Macro Interest Rates Database

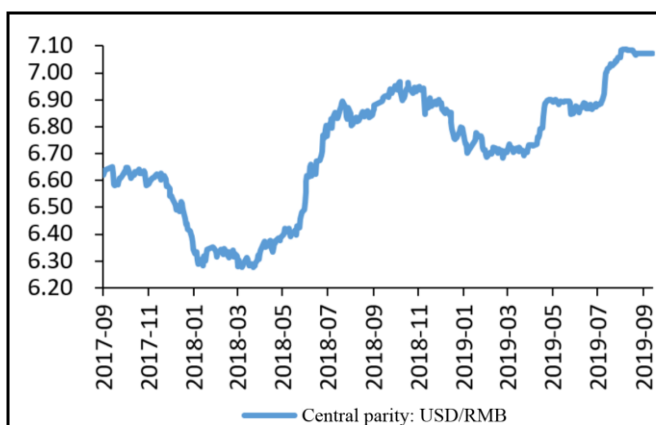
Source: CCXI Macro Interest Rates Database

The monetary policy is expected to remain in the current stance through the rest of the year. Interest rate and RRR cuts are not ruled out in the coming year as the downward economic pressure strengthens. The US Federal Reserve lowered interest rates by 25 bps in July and September, and announced to extend repurchase and expand balance sheet in September. Then other economies followed suit across the world. In the short run, the targeted RRR cut announced by PBOC in September will be put into action in October and November. As the economy improves marginally, the overall inflationary pressure is not heavy and the price trend has not yet become a constraint on the monetary policy in spite of the CPI hike fueled by pork price rise, China is unlikely to further ease its monetary policy by the end of the year. However, the downward economic pressure has not faded away and it is still possible to see PBOC further cut interest rates and RRR in the year ahead.

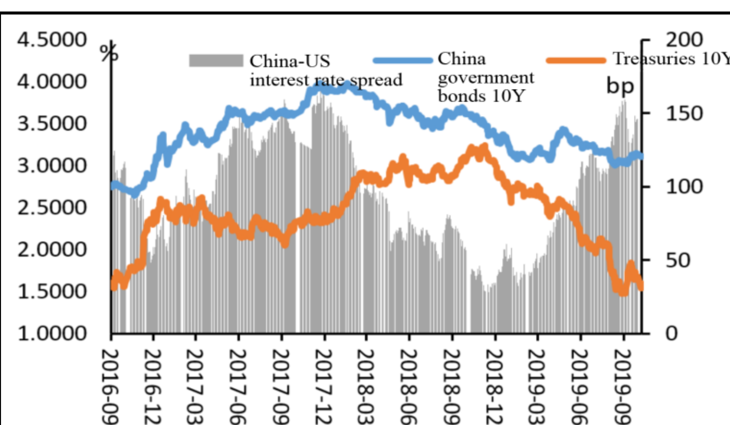
ix. RMB weakened below 7 to USD in Q3, but remained relatively stable on a firm footing

RMB tumbled in value against USD, yet expected to remain stable after the Fed's two interest rate cuts. RMB exchange rate swung widely in Q3. Offshore RMB depreciated below 7 to USD in early August, the first breach of the 7 mark since the "811" exchange rate reform in 2015. But the RMB depreciation, which was well expected, was thoroughly absorbed in market and then RMB exchange rate has regained stability. The Fed announced two rate cuts in Q3, followed by another round of balance sheet expansion kicked off in mid-October. In addition, the euro area lowered the overnight deposit rate to -0.5% and announced to resume quantitative easing. Many other economies also reduced their interest rates in succession. Currently China's monetary policy faces a fairly easy external environment and the China-US interest rate spread keeps widening, making Chinese assets more and more attractive to overseas investors and thus helping enhance the stability of RMB exchange rate.

Fig. 17: Trends in RMB Exchange Rate	Fig. 18: China-US Interest Rate Spread Continued to Widen



Source: CCXI Macro Interest Rates Database



Source: CCXI Macro Interest Rates Database

II. Internal and External Environment: external uncertainties remain there, with the domestic policy to ensure stable growth expected to further strengthen

Global economy and trade continue to soften and the US-China trade frictions have eased with limited optimism. China's economy is still exposed to external uncertainties. In the current stage, the World Bank further lowered its global growth forecasts for both 2019 and 2020 in early October. IMF also cut its global growth forecasts for 2019 and slashed its expectations for growth in global trade. Bilateral trade conflicts occurred frequently: US-Europe, US-Japan and Japan-South Korea bilateral trade ran into some frictions. Many economies further cut interest rates amid the weakening global economy as a whole: The Fed announced to cut interest rate again in September, less than two months after cutting rates for the first time, and resumed balance sheet expansion in mid-October. In addition, the euro area lowered the overnight deposit rate to -0.5% and announced to resume quantitative easing. Many other economies also reduced their interest rates in succession. Net exports play an increasingly vital role in economic growth amid China's economic downturn. The weakening major economies and sluggish global demand can hardly give an effective boost to the Chinese economy in the future. Despite the upbeat news on the US-China trade talks that the two sides reached a phase-one trade agreement in mid-October, the US-China trade frictions will be a long-lasting issue due to the United States' fickle attitude in trade and its strategic deterrence against China. Looking into the future, though the bettered US-China relationship will improve China's external environment in the short term, the gloomy global economy and the hardening US trade policy will cast uncertainties on the Chinese economy in the long run.

The stable growth policy will continue to work under the pressure of economic downturn. This year, China's macro-economic policy has been sticking to the guiding principle of ensuring stable growth amid the weakening global economy and mounting downward pressure on domestic economy. The overall policy focuses on deepening the reform and opening-up. The proactive fiscal policy strengthens mainly through tax and fee cuts and special bond issues. The monetary policy remains prudent with a focus on structural easing. Financial supervision remains stable. Regulatory policy effort is principally the refining of existing regulations. Given the economic slowdown in Q3, the State Council has reiterated the six-pronged policies to boost stability and the pivotal role of stable growth at its recent executive meetings. Future policies are expected to be more proactive and coordinated to ensure the annual growth target is met.

The fiscal policy will remain proactive and special bond issues will continue to strengthen to bolster stable growth. The fiscal policy has become more proactive and effective this year to date, as evidenced by the following figures: The government expenditure was front-loaded, growing by 9.4% YoY as of September, registering a deficit exceeding the budget published at the beginning of the year. Government special bonds continued to gain pace and accomplished the annual plan for local government bond issues in September. Tax and fee cuts exceeded RMB1.5 trillion in the first eight months, expected to break the mark of RMB2 trillion

annually. Looking into the future, the fiscal policy will be more proactive given the subdued economic growth in Q3. Recently the State Council called for further tax and fee reductions at its recent executive meeting. The *Plan for Advancing the Plan for Revenue Reallocation between Central and Local Governments after Massive Tax and Fee Cuts* set forth a plan to maintain the equal share of VAT revenue between central and local governments, adjust the VAT refund sharing mechanism and shift consumption tax collection to later stages and steadily allocate it to local governments. It is estimated that, if all the consumption tax revenue in 2018 is allocated to local governments, the local governments' share of revenues would rise from 54.4% to 59.2%. The three measures have eased local governments' revenue and expenditure pressure somewhat through reforming the administrative power and financial power of central and local governments. They help promote the fiscal equity between local authorities and ensure infrastructure investment and more aggressive tax and fee cuts. The accelerated issuance of government special bonds will boost the aggregate financing and infrastructure investment in Q4, unleashing the vital role of these bonds in stabilizing growth. We expect special bond issues to further expand next year under a mounting downward pressure on the economy.

The monetary policy remains prudent, leaving room for further cuts in interest rates and RRR. Globally, after the Fed cut interest rates twice in H2, central banks in other major countries followed suit, ushering in a global rate-cutting cycle. China's monetary policy adhered to "self-centeredness". The lending rates represented by LPR edged down slightly. After rounds of broad and targeted RRR cuts, the RRR has been lowered to 13.0% for large financial institutions and 11.0% for small and medium-sized financial institutions, still a relatively high level worldwide. The favorable external environment lends flexibility to the monetary policy. Domestically, the core CPI remains stable despite a short-lived break of 3%. Moreover, the PPI staying in a negative range in H2 poses a certain deflationary pressure. Thus the inflation level has not mounted to a constraint on the monetary policy. On the other hand, the proactive policy cannot work effectively without a relatively easy monetary environment. The downward economic pressure creates demand and room for further RRR cuts and policy interest rate reduction. Next year, in particular in its second half, the monetary policy will have room for RRR and rate cuts. Taking into account the necessity of meeting financing demand of the real economy, easing the financing difficulties of private enterprises and regulating the property market under the guiding principle that "houses are for living in, not for speculation", however, the monetary policy will remain focused on structural adjustments.

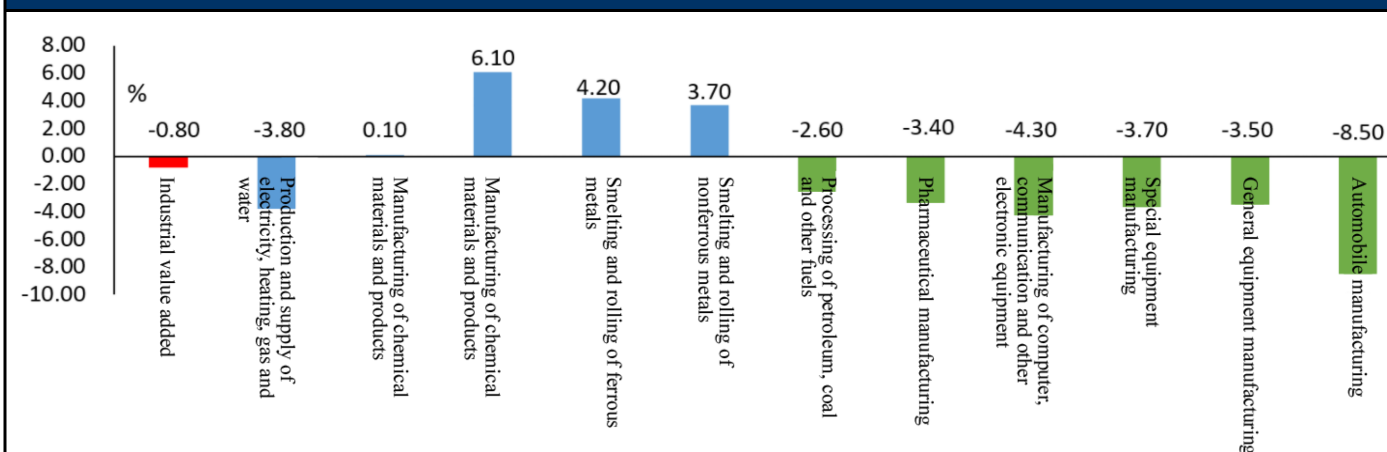
III. Economic Outlook: The economy is likely to recover marginally in Q4, yet still under downward pressure

The economic activity has signaled short-term weak pickup, suggesting a marginal recovery in Q4. Despite the continued GDP slowdown in Q1-Q3, September data revealed some positive signals in the economy activity. They will likely bolster the Q4 economic performance to stage a better-than-expected marginal recovery in Q4. First, the policy allowing local governments to issue special bonds to raise capital has led to a one-year high in the cumulative YoY growth of infrastructure investment. The accelerated issuance of the special bond quota for 2020 will boost the infrastructure investment in Q4. Second, housing starts slowed down mildly and the construction progress was basically stable. Q4 is likely to see a modest pullback in real estate investment, there being no ground for a sharp decline. Third, the current inventory of unsold vehicles is at a low since 2012, and car production has shown signs of marginal recovery recently. Automobile consumption may weigh less on total retail sales of consumer goods in Q4. In addition, the improvements in car production will turn into improvements in relevant industry chains. Fourth, the credit and aggregate financing has picked up with lending structurally improved, indicating to certain extent that the external financing pressure on enterprises has eased in the short term to encourage expansion of investment in the business sector. Fifth, in spite of contraction in both imports and exports, a short-term recovery is expected due to the easing US-China trade tensions and low-base effect. Overall, the economy is likely to gain momentum of marginal recovery in Q4.

Internal and external pressures still weigh on the Chinese economy. First, the global economy continues to weaken. Major economies are seeing their actual economic growth softening and international organizations

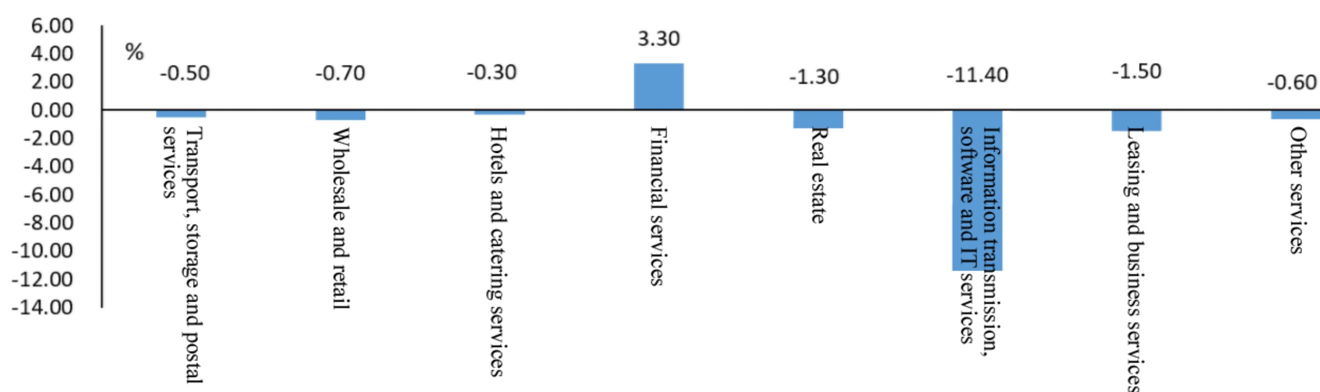
have lowered their forecasts for global growth. The US-China trade conflicts with twists and turns will continue into the future over the long term. The frequent geographical conflicts add to external uncertainties for China's economy. Foreign demand will become a weaker driver of Chinese economic growth. Second, the real estate under tight regulation will provide weaker backing for economic growth in 2020. Third, though the current industrial inventories remain low and industrial enterprises' restocking demand may give some impetus to economic growth, their restocking will have limited effect in driving the economy given the weak demand. Fourth, industrial and service sectors undergo a structural deterioration, showing escalating recessional structural changes and softening structural upgrades. Of the six energy-intensive industries, six saw an increase and two witnessed a decline in the cumulative YoY growth rate of industrial value added. High and new technology industries showed general deceleration in cumulative YoY growth in industrial value added. While the services sector slowed down in general, financial services have gained pace, indicating a possible escalation in the "shift from real to virtual economy". Overall, the downward pressure on the economy is likely to further mount in 2020 H2 as the momentum of short-term economic recovery moderates.

Fig. 19: YoY Changes in Cumulative Industrial Value Added



Source: Compiled by CCXI

Fig. 20: Cumulative YoY Growth in Service GDP (at Constant Prices)



Source: Compiled by CCXI

Summary:

In spite of the subdued economic data in Q1-Q3, the macro-economic data in September showed some positive changes, including the mild marginal recovery spurred by the stable growth policy. Taking into account the low-base effect, Q4 is estimated to see stronger-than-expected economic growth and stage a temporary recovery on a weak footing. We maintain our forecast of 6.1% for annual economic growth. Meanwhile, the economy remains under a downward pressure. The weakening global economy may further drag on the Chinese economy. Though real estate is somewhat resilient under tight regulation, its support for investment and the larger economy will become weaker in 2020. Enterprises' restocking still has limited effect in driving the economy, which undergoes deceleration in structural upgrades and escalation in recessional structural changes. We should be too optimistic about the economic performance in 2020, especially in 2020 H2.

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