CAPITAL ECONOMICS 凯投宏观

CHINA ECONOMICS UPDATE

Rare drop in household wealth will cap recovery

- **Bank deposit held by Chinese households have soared over the past year. But that mostly reflects a shift out of riskier assets rather than a surge in savings. In fact, our calculations show that household wealth declined in 2022 for the first time in at least two decades. This suggest that once the initial reopening rebound has happened, we shouldn't expect a further surge in consumer spending.**
- Chinese households have been quick to shake off the shackles of the zero-COVID policy. High-frequency data show that, by mid-January, they were back on the streets and public transport networks in full force. Less certain, however, is how quickly they will reopen their wallets. Private consumption is almost 40% of GDP and was the most depressed type of expenditure last year. The extent of its recovery will therefore be key in determining the strength of China's reopening rebound.
- In many advanced economies, private consumption rose above its pre-pandemic trend once virus disruptions faded. This can be pinned on "revenge spending" as households dipped into the excess savings that they had built up early in the pandemic thanks to large fiscal transfers and restrictions on spending.
- Those hoping for something similar in China may end up disappointed. Admittedly, **household bank deposits have surged recently** – by the end of 2022, they were 32% above their pre-pandemic trend. (See Chart 1.) **But this isn't the bullish signal that some have suggested**.
- For years, Chinese households have poured money into wealth management products (WMPs) and other asset management products (AMPs) sold by the banks, treating them as high-yielding quasi-deposits. On paper, customers shoulder the risks associated with these products. But for a long time, banks always stepped in to prevent customers from suffering losses, creating the impression that the products were risk-free. These implicit bank guarantees have been scaled back in recent years amid a regulatory overhaul, with 1st January 2022 marking the deadline for full compliance. A sell-off in the bond market, where the bulk of AMP funds are allocated, also added to the exodus from these products late last year.
- Taken together, the recent net increase in household holdings of bank deposits and AMPs does not appear especially strong. (See Chart 2.) In other words, **most of the acceleration in deposit growth reflects the reallocation of savings away from AMPs rather than the build-up of new savings**.
- That's not to say that the pandemic didn't alter the savings behaviour of Chinese households. They did increase their savings rate in response to the initial outbreak and the subsequent waves of disruption from the Omicron variant. However, **the increase in the savings rate was smaller than the rise in deposits alone implied and also more modest than that seen in most developed economies**. (See Chart 3.)

Chart 1: Household Deposits

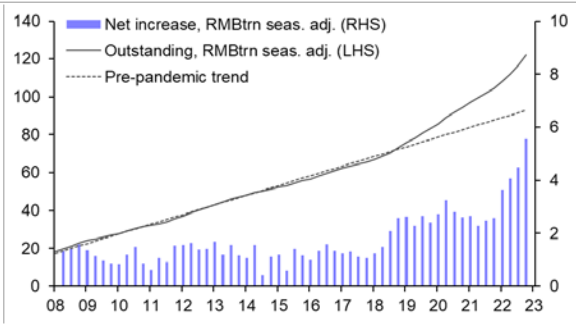
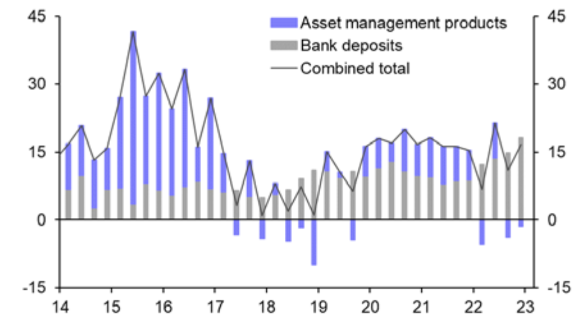


Chart 2: Net Increase in Household Assets (% of GDP)



Sources: CEIC, Capital Economics

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- What's more, the broader economic backdrop has been very different in China. In most developed economies, generous fiscal transfers limited the hit to disposable incomes from the pandemic (and more than offset it in the US). In contrast, Chinese households received little in the way of fiscal transfers during the pandemic. Some cities handed out consumption vouchers, but these programs were insignificant in macro terms. Coupled with the longer-lasting disruption to economic activity from repeated lockdowns, **household income growth was blown off course in China to a much larger degree than elsewhere**. (See Chart 4.)
- **As a result, although China's household savings rate has been higher than normal, the amount of money being saved each quarter has actually been below its pre-pandemic trend for much of the past few years**. (See Chart 5.) That's in stark contrast to most developed economies, where the opposite was true ahead of reopening.
- Another important difference is that the 2020/21 rally in global asset prices meant that households in advanced economies were benefiting from positive wealth effects as virus restrictions were dismantled. But in China's case, **the housing downturn and stock market slump of the past couple of years has resulted in negative wealth effects**.
- With all of this in mind, we think the single best measure to gauge the financial position of Chinese consumers is the level of household net wealth. It captures both changes in the flow of savings and fluctuations in asset values. China's Academy of Social Sciences, a government think-tank, publishes estimates on the stock of different types of household assets and liabilities. Their estimates only run to the end of 2019. But using more timely data from a variety of sources, we have extended their estimates to the end of last year.
- **Our calculations suggest that net household wealth fell outright last year for the first time in at least two decades**. (See Chart 6.) This is more than just a reversal of the unusually rapid increase in wealth at the start of the pandemic. It leaves households considerably worse off than if net wealth had risen at its pre-pandemic pace across the past three years.
- Last year's wealth destruction is likely to damage the confidence of Chinese households, many of whom had become accustomed to uninterrupted gains in economic prosperity. **As such, we expect consumers to remain cautious for a while, focusing on rebuilding wealth rather than running down accumulated savings**.
- With virus restrictions lifted and the outlook improving, consumption will nonetheless pick up in the near-term. We expect a jump in real consumer spending of around 10% this year, given its weak starting point. But once the initial reopening boost has happened, the recovery will lose momentum quickly.

Chart 3: Household Savings Rate – Deviation from Pre-Pandemic Level (%-pts)

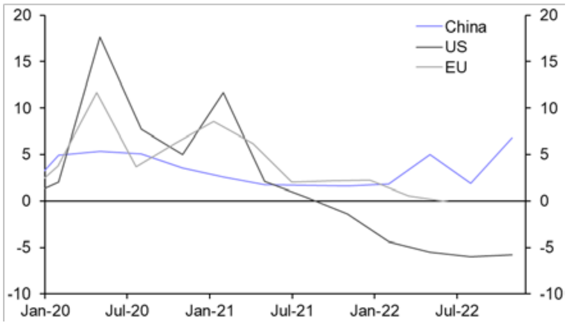
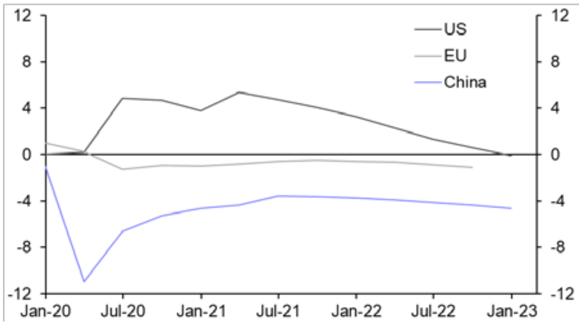


Chart 4: Household Disposable Income – Cumulative Deviation from Pre-Pandemic Trend (%)



Sources: CEIC, Capital Economics

Chart 5: Household Savings (RMB trn, seas. adj.)

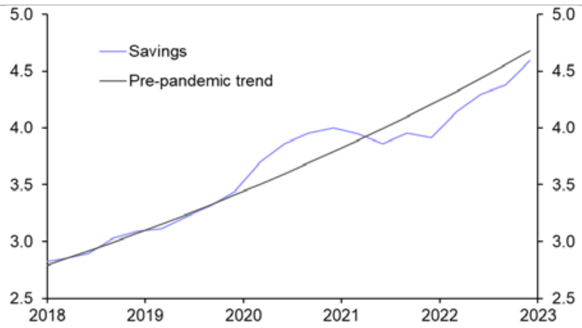
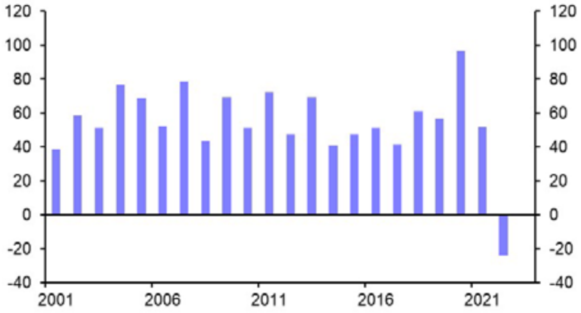


Chart 6: Change in Household Net Wealth (% of GDP)



Sources: CEIC, Capital Economics