

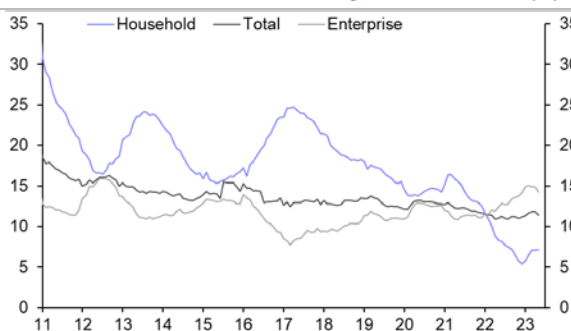
CHINA RAPID RESPONSE

Bank Lending & Broad Credit (May)

A worrying deceleration

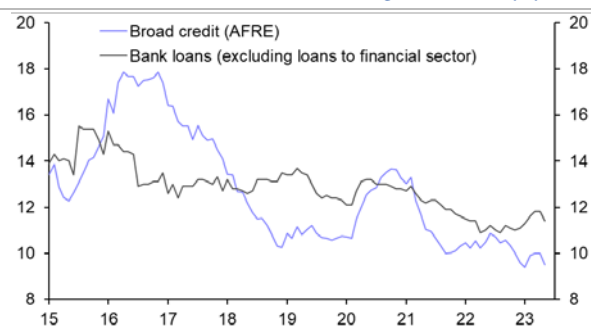
- **Broad credit growth slowed sharply in May and has now reversed almost all its reopening recovery. This poses a downside risk to growth and strengthens the case for additional policy support.**
- China's banks extended RMB1,360bn in new local currency loans in May on a net basis, lower than expected (the Bloomberg median was RMB1,550bn and our forecast was RMB1,800bn). Aggregate financing (AFRE), the PBOC's measure of broad credit, was also weak, rising by RMB1,560bn (Bloomberg RMB1,900bn, CE RMB2,800bn).
- The simplest way to cut through the seasonality of the net increase numbers is to look at what they imply for y/y growth in outstanding credit. Based on this, **bank loan growth dropped from 11.8% y/y to 11.4%, the lowest since January.** (See Chart 1.) This was mainly driven by a slower expansion in lending to corporates. Lending to households accelerated marginally, supported by the lagged impact of the earlier pick-up in home sales on mortgage disbursements.
- Non-bank lending also softened last month. Both corporate and government bond issuance slowed, with the latter dropping back as the boost from the front-loading of fiscal borrowing faded. All told, **broad credit growth cooled from 10.0% y/y to 9.5%, almost entirely reversing its reopening rebound.** (See Chart 2.)
- **This is concerning given that credit growth is one of the most reliable leading indicators of China's economic cycle.** Unless the slowdown in lending is arrested soon, it risks derailing the reopening recovery. The bits of the service sector driving the current rebound are not credit intensive, but the wider economy could still be dragged down by sectors that are.
- This risk helps explain why the PBOC **lowered** its 7-day reverse repo rate by 10bps earlier today, a move which is likely to be followed by wider monetary easing over the coming weeks, including cuts to the MLF rate and LPR, as well as a loosening of reserve requirements and bank loan quotas.
- We will wait until Thursday, when we get May's activity and spending data, before reassessing our forecasts. But **the lacklustre credit data suggest that our expectation for GDP growth of 6.5% this year could prove too optimistic, even amidst a step up in policy support.**

Chart 1: Growth of Outstanding Bank Loans (% y/y)



Sources: CEIC, Capital Economics

Chart 2: Growth of Outstanding Credit (% y/y)



Sources: CEIC, Capital Economics

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