CHINA ECONOMICS WEEKLY

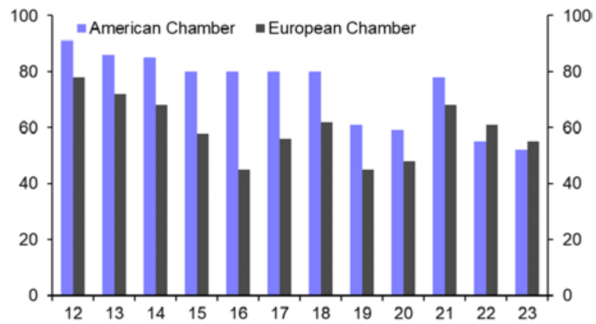
Foreigners staying away, consumers perking up

Efforts to boost foreign investment are failing

In March, the government launched a year-long "Invest in China" campaign to shore up sagging foreign investment. As part of these efforts, it set out 24 measures in August to improve the business environment for foreign firms. And this week, the financial regulators met some of those firms in a bid to reassure them about the direction of policy. There are also reports that caps on foreign ownership in onshore-listed firms will be eased.

These efforts have so far fallen flat. FDI continued to slide in Q2, by the most on record. In a survey released this week by the American Chamber of Commerce in Shanghai, which it conducted at the end of Q2, the proportion of companies expressing optimism on China's business outlook hit a record low of 52%. That's even worse than the 55% share on a similar survey published by the European Chamber of Commerce in June. In both cases, firms were more pessimistic than in 2022, with the move away from zero-COVID failing to provide the hoped-for boost to confidence. (See Chart 1.)

Chart 1: % of Companies Feeling Optimistic about China's Business Outlook



Sources: American Chamber, European Chamber, Capital Economics

Meanwhile, foreign investors have continued to pull their money from onshore capital markets this year, with no signs yet of any reversal.

The Chamber of Commerce surveys suggest that the main concerns among foreign firms are geopolitical tensions and the slowing economy. Growth fears may ease a bit in the near-term if we are right that a cyclical pick-up is now getting underway. But concerns about the medium-term outlook are likely to remain, and geopolitical tensions are here to stay.

China is not particularly dependent on foreign capital. But foreign investment has historically played an outsized role in supporting growth through the diffusion of foreign technology and management practices. That process has now ground to a halt, to China's detriment.

Green shoots in the consumption data

The strong pick-up in retail sales last month caught most analysts by surprise. The NBS doesn't provide a detailed breakdown of the headline data, but does produce one for large retailers, which are responsible for around a third of overall retail sales.

The data suggest that a jump in fuel and gold prices played an important role last month. After stripping out these components, growth held steady. But at 0.8% m/m, it is still relatively strong compared to pre-pandemic growth rates. (See Table 1.) One recent prop has been measures introduced in July to boost auto sales, the most notable being an increase in annual car registration quotas in major cities.

Table 1: Retail Sales (% m/m, seas. adj.)

	2019 ave.	Jul. 23	Aug. 23
Overall retail sales	+0.6	+0.2	+0.5
Large retailers	+0.4	+0.5	+1.2
Excl. fuel & gold/jewellery	+0.4	+0.8	+0.8
Automobiles	+0.4	-1.5	+2.0

Sources: CEIC, Capital Economics

Admittedly, the breakdown suggests that wider spending has yet to accelerate. But we think it may do so before long. The labour market is tightening again thanks to policy support and the IPSOS consumer sentiment index ticked up this month after trending down since May.

The week ahead

We think the PMIs will show steady manufacturing activity and a pick-up in service sector momentum.

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Data Previews

Fri. 30th Sep. / Sat. 1st Oct. – Manufacturing PMIs (Sep.)

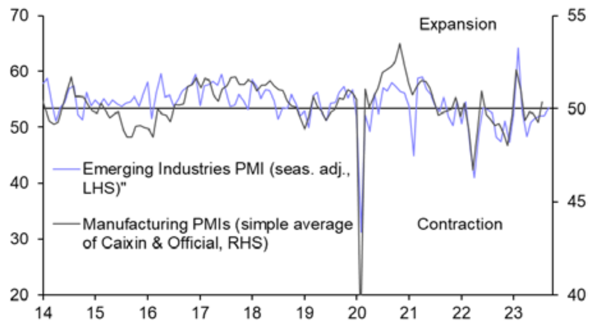
Forecasts	Time (China)	Previous	Consensus	Capital Economics
"Official" PMI (1st Oct.)	09.30	49.7	50.2	50.0
Caixin/S&P Global PMI (30th Sep.)	09.45	51.0	51.1	51.0

Factory activity stabilising

After falling into contractionary territory for four months, the average of the official and Caixin manufacturing PMIs jumped in August, returning above 50. We think the surveys will hold on to these gains and be little changed in September.

Admittedly, the flash PMIs for China's major trading partners were weak this month, hinting at a continued drag from cooling external demand. But domestic demand is likely to have held up better, supported by the recent step up in infrastructure spending. Encouragingly, the timely Emerging Industries PMI – which covers high-tech parts of industry – continued to improve in September. (See Chart 2.)

Chart 2: Manufacturing & Emerging Industry PMIs



Sources: CEIC, S&P Global, Capital Economics

Fri. 30th Sep. / Sat. 1st Oct. – Non-manufacturing PMIs (Sep.)

Forecasts	Time (China)	Previous	Consensus	Capital Economics
"Official" PMI (1st Oct.)	09.30	51.0	50.5	51.5
Caixin/S&P Global PMI (30th Sep.)	09.45	51.8	52.0	52.0

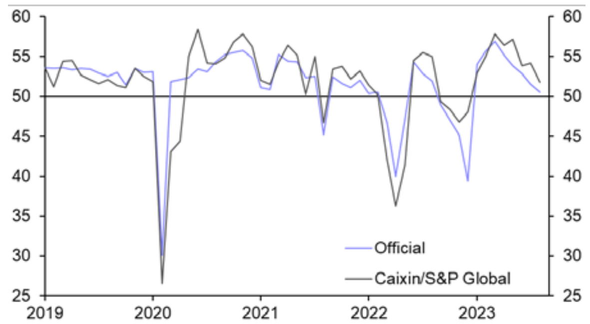
Services slowdown may be bottoming out

In contrast to the manufacturing surveys, the services PMIs fell again in August. (See Chart 3.) We think that might mark the trough this cycle, with the PMIs likely to show a pick-up in services activity in September.

Retail sales exceeded expectations in August, and growth in the services production index also improved, perhaps indicative of a turning point. The unemployment rate also declined, which should help to support wage growth. Consumer caution seems to be easing too, with the IPSOS consumer sentiment index ticking up in September.

Construction activity, which is part of the official non-manufacturing PMI, may have picked up too. Admittedly, new housing starts almost certainly fell again amid declining home sales. But bond issuance by local government rose on the back of directives to fully utilise annual quotas for special bonds by the end of this month. As such, infrastructure construction probably picked up this month.

Chart 3: Services PMIs



Sources: CEIC, S&P Global, Capital Economics

Economic Diary & Forecasts

Upcoming Events and Data Releases

Date	Country	Release/Indicator/Event	Time (China)	Previous*	Median*	CE Forecasts*
September						
Tue 26th	**HK**	Exports (Aug., HKD)	(16.30)	(-9.1%)	-	(-4.5%)
	HK	Imports (Aug., HKD)	(16.30)	(-7.9%)	-	(-0.5%)
	HK	Trade Balance (Aug., HKD)	(16.30)	-30.0bn	-	-27.5bn
Wed 27th	**Chn**	Profits of Large Industrial Firms (Aug.)	(09.30)	(-6.7%)	-	-
Thu 28th	**Chn**	Current Account Balance – Final (Q2, USD)	-	+65.3bn	-	-
Fri 29th	**Chn**	Mid-Autumn Festival (National Holiday)	-	-	-	-
	Chn	Caixin Manufacturing PMI (Sep.)	(09.45)	51.0	51.1	51.0
	Chn	Caixin Services PMI (Sep.)	(09.45)	51.8	52.0	52.0
	HK	Retail Sales (Aug.)	(16.30)	(+16.5%)	-	(+17.5%)
Also expected during this period:						
TBC	**Chn**	Trade – Detailed Breakdown (Aug.)	-	-	-	-
TBC	**Chn**	CBRC Data on Assets and Liabilities of Financial Institutions (Aug.)	-	-	-	-

Selected future data releases and events:

September

Sat 30th	**Chn**	"Official" PMIs (Sep.)
	HK	The Day Following Mid-Autumn Festival (National Holiday)
October		
1st – 6th	**Chn**	National Day Golden Week (National Holiday)
Mon. 2nd	**HK**	National Day of the People's Republic of China (National Holiday)

Main Economic & Market Forecasts

%q/q annualised (%y/y), unless stated	Latest	Q3 2023	Q4 2023	Q1 2024	Q2 2024	2022	2023f	2024f	2025f
Official GDP	+0.8(+6.3)*	(4.3)	(5)	(4)	(4.4)	(3.0)	(5.0)	(4.5)	(4.0)
GDP (CE CAP-derived estimates)	+2.5(+11.3)*	(4.7)	(7.7)	(5.2)	(3.4)	(-3.5)	(6.5)	(4.0)	(2.5)
Consumer Prices	(+0.1)**	(0.2)	(0.2)	(1.1)	(1.2)	(2.0)	(0.5)	(1.0)	(1.0)
Producer Prices	(-3.0)**	(-2.5)	(-2.2)	(-1.6)	(-0.3)	(4.0)	(-2.5)	(-0.5)	(-1.0)
Broad Credit (AFRE)	(+9.0)**	(9.2)	(10.3)	(9.4)	(10.0)	(9.6)	(10.3)	(9.7)	(8.4)
Exports (US$)	(-8.8)**	(-15.5)	(-8.5)	(-15.0)	(-15.5)	(7.0)	(-8.5)	(-10.0)	(2.0)
Imports (US$)	(-7.3)**	(-7.5)	(-7.0)	(11.0)	(3.5)	(1.0)	(-7.0)	(4.0)	(2.0)
RMB/$†	7.31	7.25	7.30	7.20	7.10	6.95	7.30	6.90	6.70
7-day PBOC reverse repo† %	1.80	1.80	1.60	1.60	1.60	2.00	1.60	1.60	1.60
1-year Loan Prime Rate† (LPR) %	3.45	3.45	3.25	3.25	3.25	3.65	3.25	3.25	3.25
1-year MLF Rate† %	2.50	2.50	2.30	2.30	2.30	2.75	2.30	2.30	2.30
10-year Government Bond Yield† %	2.68	2.60	2.40	2.50	2.60	2.85	2.40	2.60	2.60
RRR (major banks)† %	10.50	10.50	10.25	10.25	10.25	11.00	10.25	10.25	10.25
CSI 300 Index†	3,672	3,750	3,800	3,900	4,000	3,872	3,800	4,200	4,900
Hong Kong GDP	(+1.5)*	(7.0)	(10.5)	(7.0)	(10.5)	(-3.5)	(5.5)	(9.0)	(6.0)
Hang Seng Index†	17,655	17,800	18,250	18,400	19,363	19,781	18,400	22,250	25,500

Sources: Bloomberg, Refinitiv, CEIC, Capital Economics *Q2; **Aug.; † End of period

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