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-1.9%YoY December profits decline
but full-year +10.3% growth in China, if
you can believe it

But we have doubts; because for some
time now Chinese profit growth rates
don't match up with historical data

Eg, in the past six months it appears
reported growth rates are significantly
higher than what history suggests

Which can only be true if prior-year
data is revised *down* massively

USD/CNY – Revisionist Profits History

28 January 2019

Key Points:

- We use China's December industrial profits to illustrate discrepancies between current reported growth rates and inferred growth rates from past reports
- Eg, using original reports would transform December's -1.9%YoY growth rate to -19.5%!
- Such a discrepancy implies a revision (down) of around 20ppt or more (!) in the level of prior year data, making each new data point nearly useless in terms of information (because we suspect they will be massively revised later on)
- Unrevised profits numbers appear little correlated with economic activity
- Which makes us wonder whether profits contribute into GDP estimation or the other way round?

The Data

China reported December industrial profits data today. As releases go, it was hardly notable on its own: %YoY growth was reported at -1.9%, nearly the same as November's -1.8% reading. For all 2018, NBS claimed 10.3% profit growth for the year, which seemed suitable enough for a 6.6% annual 2018 growth rate reported earlier.

The Big Revision

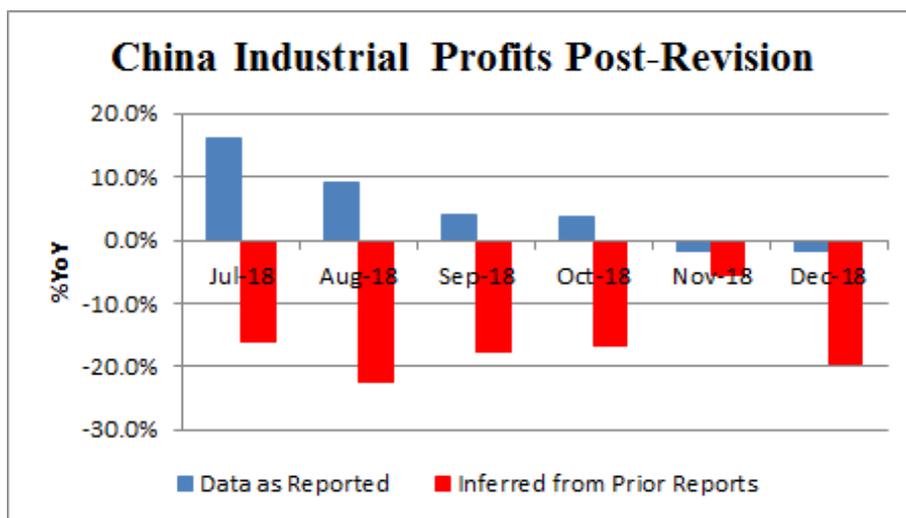
Bloomberg noted (as it has in recent months):

The official year-on-year growth rate for profits began diverging from the growth rate calculated from the nominal profit figures in 2017, and continued to be higher in December's release. That discrepancy has led some economists to question the veracity of the figures.

To explain this, the following chart shows reported headline profit growth in the NBS's monthly website reports over the second half of last year, and compare these growth rates with growth rates backed out of the originally reported *levels* data. Ie, each month NBS reports a year-to-date level of profits, total and broken down into sectors. The change in the YTD figures presumably is a good measure of monthly profits, particularly since we have never seen a transparent explanation of prior year revisions.

What we mean by our somewhat audacious title below is that the discrepancy between currently reported growth rates from what would be implied by previously reported numbers would involve revising *down* prior-year numbers by 20% or even more! It's not that profits numbers, which are volatile, are not routinely revised around the world. But any sampling framework that produces this sort of "measurement error" make the entire series possibly useless for analysts. Certainly we can say this for monthly numbers.

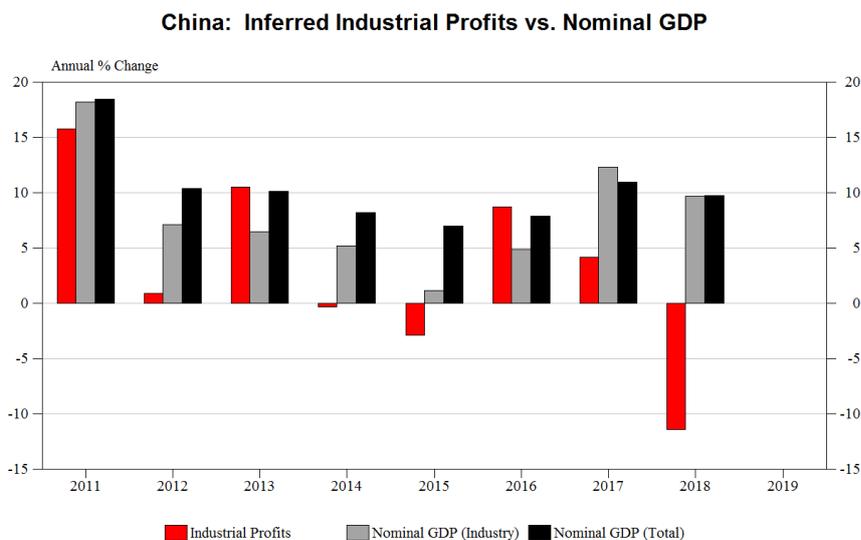
CHINESE PROFITS APPEAR HEAVILY MASSAGED



Source: Bloomberg, CEIC, MUFG Bank

It's Still the Economy, Stupid

CHINA: UNREVISED PROFITS GROWTH DO NOT MATCH GDP



Source: CEIC

Last Data 2018

Source: CEIC, MUFG Bank

Unrevised industrial profits data can then look wildly out of kilter with GDP

Of course, industrial profits figures are most important in markets as hints of economic activity. The problem with the size of revisions implied above is that when you aggregate the implications over a year, they muddy any correlation with GDP. The second chart above shows annual growth rate of industrial profit as originally reported by NBS (annual growth of the December YTD totals each year) and compare them with nominal growth rates of both industrial-sector GDP as well as overall GDP. The profits figures have *not* been revised as what NBS is reporting (you can see, eg, how a 10.3% annual growth rate for profits in 2018 look much less conspicuous against reported GDP growth). Eyeballing the above made us wonder whether it's profits that contribute to an estimate of GDP or the other way round?

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