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China Macro – The Makeup Washes Off

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Key Points:

- We stick with “stabilization in 1H19, recovery in 2H19”
- But chest-thumpers on both sides of the Pacific may be underestimating the real effects of Trump’s latest escalation
- April headline retail sales grew at its slowest rate since May 2003
- Retail sales still look on track for 7.5-8.0% for all 2019
- Autos remain stuck in first gear; 2H19 recovery is more in doubt
- Official hint at stimulus; of course equities rallied

The Story So Far

We stick with our “stabilization only in 1H19 and not 1Q19” thesis, with possible recovery in 2H19; the latter on watch for quality and vitality of recovery. While we don't think the US-China Trade War to date was the main driver behind China's slowdown (we focus primarily on domestic debt and demand), our initial impressions of chest thumping from both sides after Trump's Trade War escalation suggest **officials on both sides may be underplaying the eventual real side impact of Trump's escalation.**

Retail Sales

At first blush, our main impression after China's April real side indicator release was, boy, there sure could have been quite an effort to window dress March and get that 6.4%YoY 1Q19 GDP growth rate over the line and jotted down in history! We had said China's economy as a runner would get **tired** again, but even we probably didn't expect so soon.

At 8.0%YTD for April < last 8.3%, retail sales remains in the tight neighborhood of the 8.2%YTD growth reported for Jan+Feb, where we had suggested it might stay all year. Eyeball econometrics had suggested to us that overall retail sales in 2019 could report out at between 7.5-8.0% nominal.

While the eating out theme remains firm this year – 8.5%YoY < last 9.5% - the housing-related items we highlighted last month seemed to have largely deflated. Furniture 4.2% < last 12.8%; yes there was a high growth rate a year ago, in April 2018, but March 2018 growth was also strong. Construction materials -0.3% << last 10.8%. This despite reports of what might be considered frothy conditions in some residential markets, where home prices rose more than 20%YoY in 1Q19 and land sale premiums are up by more than 30%. On residential housing we note April property investment ticked up one tick (just the way authorities prefer) from last 11.8%YTD to 11.9% now.

Autos remained stalled in first gear with sales at -2.1%YoY > last -4.4%; even petrol sales slowed to 0.1% << 7.1% (though here the # of working days should matter). Industry data was far worse, with sales falling -14.6% in April. (Even for the largest auto market in the world, since the industry is the industry we wonder how we get such a large discrepancy between industry data and NBS data?) OEMs we spoke to a couple of months back were counting on the base effect to drop out in 1H19 and to

Recovery in 2H19 but with Trade War downside

Quite a bit of mascara may have been applied to March data

Retail sales still in the 7.5-8.0% range for all 2019

Despite frothier real estate, housing-related retail sales slowed

Autos stuck in first gear, more doubts

start seeing +ve growth #s in the second half; **more recent data is sowing doubts about that.**

Industrial Production

Autos also affected production, while foreign enterprises whacked

More properly, VAI (value added in industry): 5.4%YoY < consensus 6.5% << last 8.5%; 6.2%YTD < last 6.5%. (We had been wondering what that 8.5% was all about.) By industry, there were a whole host of somewhat puzzling slowdowns like machinery 7.1%YoY < last 15.2% as an example. There was a notable difference between the pace of growth of domestic enterprises and foreign-invested (including Hong Kong and Taiwan) enterprises, the latter growing only 2.5% possibly reflecting a bigger hit from the Trade War. Given weaker sales, vehicle production fell by nearly -16% in April with sedans down -18.8%, worst reading since September 2015.

The weightless economy

NBS noted in its press release that in its Index of Services Production, information transmission, software and IT had grown 25%YoY in April. This is in real terms. Some activity in this sector has been dubbed the weightless economy in recent years, meaning the basic product is data which has no weight. We have to wonder about the economic meaning behind this measure; whether 10Gb of data means 10X more output (or welfare, if you follow the utilitarian roots of economics) than 1Gb of data?

Policy Response

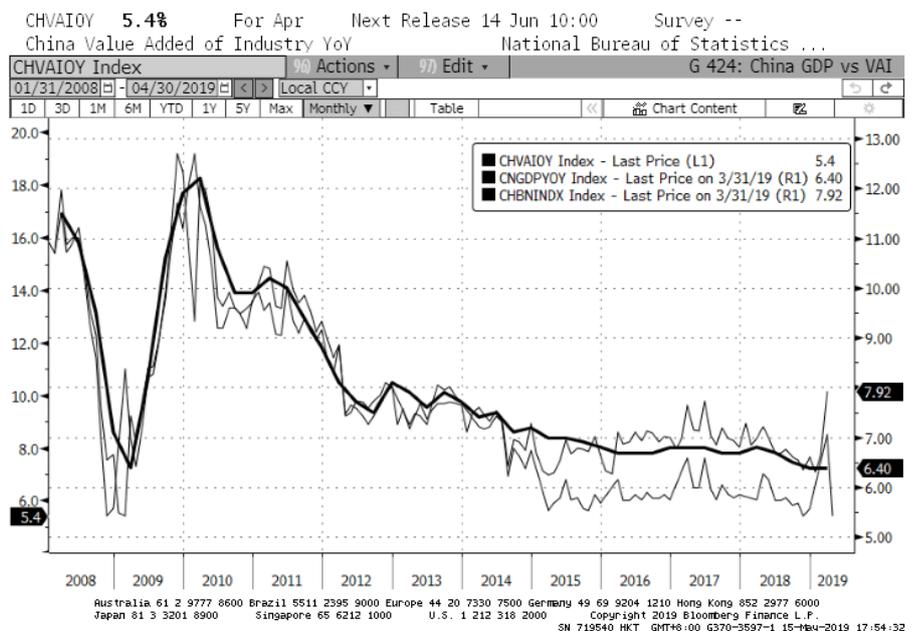
Hope in stimulus springs eternal

An NBS spokeswoman at the presser hinted there was relatively big room for policies to support growth. As we'd commented last month, we didn't think authorities had enough confidence to take their feet off the accelerator. Onshore equities, predictably, rallied on this hint.

One Chart

We reproduce a chart which we have shared with clients in the past few months.

CHINA'S RECOVERY: DEPENDENT ON CONSUMPTION AND SERVICES



Source: Bloomberg, MUFG Bank

But consumption is slowing

The thick black line in the chart is headline GDP growth on a quarterly %YoY basis; the other two lines are monthly %YoY growth rates of VAI (lower line towards the

right) and Bloomberg's China GDP Tracker (top line towards the right). Now that 8.5% blip from March is out of the way, the gap between headline GDP and VAI since mid-2014 has been cited by officials to claim China's growth is now much more dependent on consumption and services. Flipping that around, that means whether China gets close to its official 6-6.5% growth target this year seems largely dependent on consumption/services, but in the April data just reported, it seems the latter largely slowed.

For another view ...

The official view

For the officially translated NBS commentary, follow this [link](#). We reproduce the first paragraph:

In April, under the guidance of Xi Jinping Thought on Socialism with Chinese Characteristics for a New Era, all regions and departments implemented the decisions and arrangements made by the CPC Central Committee and the State Council, stuck to the general working guideline of making progress while maintaining stability, insisted on promoting high-quality development of the economy, focused on the supply-side structural reform, took coordinated steps to stabilize growth, stimulate reform, adjust structure, benefit people's livelihood and fend off risk, intensified efforts in policy implementation to maintain stability in areas like employment, financial sector, foreign trade, foreign investment, domestic investment, and market expectation. The economy performed within the reasonable range, and sustained the momentum of progress in overall stability.

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