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China Macro Roundup

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The Story So Far

The Chinese economy is recovering, but dreams of a V have quickly Vanished to be replaced by some form of an elongated U. Uncertainty has also risen given new government attention to choking off a potential second COVID-19 wave in and around the Northeastern province of Jilin. Even a short lockdown will delay industrial recovery in China's Rust Belt, but for now we wait for more evidence before making a call on the second wave. We stay with expectations for actual 2.5% real growth for China in 2020:

- *A China whose productive capacity will be more or less fully restored by 3Q20*
- *But whose ability to use its capacity will be curtailed by slower global and domestic demand*
- *The April retail sales figures showed us a consumer who is hardly on a tear of "revenge buying"*
- *One whose job prospects are considerably dimmer with wages frozen or even cut*
- *Making the climb back to last year's consumption levels looking more of a 3Q20 expectation*
- *We continue to think that even with stimulus on steroids in 2020 that China Inc. will only crank out 4ppt of domestic demand to add to real GDP*
- *While a gradual recovery in the rest of the world will see external demand subtract -1.5ppt off of GDP*
- *The sight of China resuming lockdown in May should give the rest of the world pause about July*

Retail Sales: -7.5%YoY < Consensus -6.0% but > Last -15.8%YoY

So much for revenge buying

Though April retail sales were weaker than our and consensus expectations, we remain heartened by what seems to be a realistic report. March-April figures should put paid to any expectations that expiring coupons or notions of "revenge spending" could quickly snap Chinese consumption back to where it once was.

Consumption that will only match (slow) growth

Our expectations for Chinese consumption at the GDP level in 2020 are slow but very basic: We look for Chinese consumption to match income this year, and since we expect 2.5% actual growth in China for all 2020 (who knows what it will ultimately report out as), that means consumption will also grow a real 2.5%. The drivers are prosaic: A loss of jobs and lower wages will restrain consumption this year.

Fear will be the main driver of the global consumer this year, with precautionary saving up

China's pattern matches up well with trends elsewhere in the world. It seems almost trivial to say this (but it's not): Regardless of policies or politics or even theme songs when unlocking, Fear will the main arbiter of consumption behavior this year, probably all over the world. Unless households come to believe face-to-face interaction is as safe as it once was before COVID-19 struck, there will always be reluctance that keeps the consumer back – sometimes way back. Even in countries that are famous for not having *any* precautionary saving to speak of – looking at you, USA – we suspect there will be a pickup in precautionary saving that will tamp down consumption growth for the first year or two out of COVID-19.

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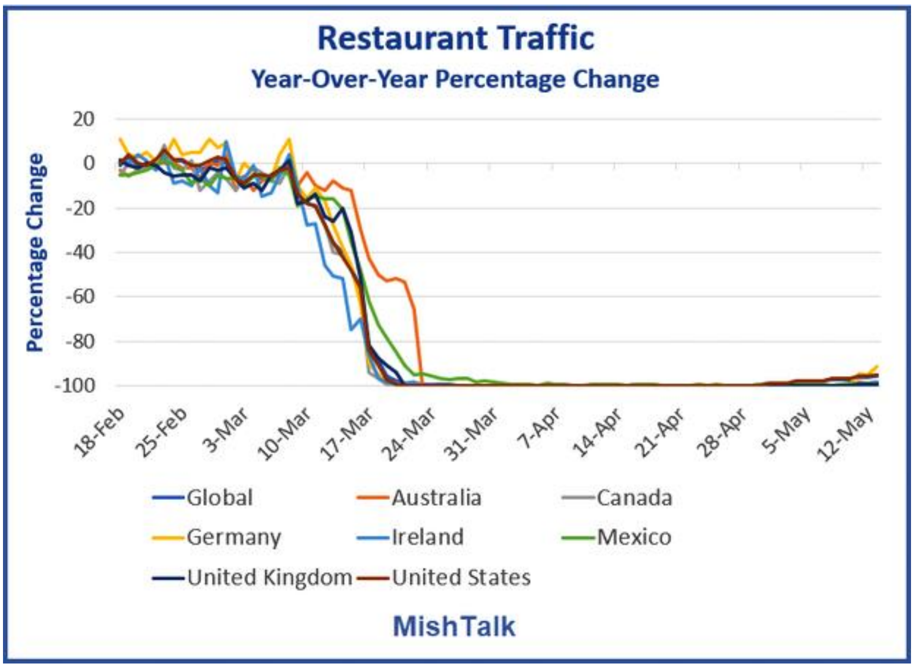
GLOBAL RESTAURANT TRAFFIC AT THE BEGINNING OF UNLOCKING



Source: https://www.thestreet.com/mishtalk/economics/when-will-restaurant-traffic-get-back-to-normal

But the South – and the Chinese consumer – shall rise again

We are, however, not so gloomy as to think Chinese retail sales will stay down in the doldrums. Remember, our expectation is for consumption to grow in line with real income at 2.5%, so we think tracking %YTD figures for retail sales is a worthwhile activity, with one of the major markers the point at which %YTD climbs back to zero (ie, when 2020 retail sales by value matches up with YTD figures from 2019).

Autos a good place to look for any pent-up demand

Auto sales are a natural place to go looking for catchup in China, since this sector had been notably weak for two years. Before COVID-19 struck, we thought Chinese consumers had already been revising down estimates of permanent income (due to structurally slowing growth), so that growth in China's car market to becoming the Godzilla of the world would be delayed by a few years. So if there was going to be catchup it might as well be here, if there is any pent-up demand at all. Automobile sales in April were flat YoY, similar to the April sales of SAIC, which grew 0.5%.

Other retail sale breakdowns with interpretation:

BREAKDOWNS OF CHINA'S APRIL 2020 RETAIL SALES

Category	March %YoY	April %YoY	Interpretation
Restaurant/Catering	-46.8%	-31.1%	Still wary of gathering (see Chart above)
Food	+19.2%	+18.2%	Eating at home
Clothing	-34.8%	-18.5%	Foot traffic not all back even with e-commerce offset
Jewelry	-30.1%	-12.1%	Maybe less likely to buy online
Household Electronics	-29.7%	-8.5%	See Clothing
Petrol	-18.8%	-14.1%	Getting out less

Source: MUFG GMR, Bloomberg

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But probably July or later to match 2019

YTD, retail sales grew -16.2%. At this pace, it's looking as if the full convalescence of Chinese consumption (by which we mean getting YTD levels to = levels of a year ago) might not take place till 3Q20 (ie, not till July or later).

Value-Added in Industry (Industrial Production): +3.9%YoY > Consensus +1.5% > Last -1.1%

China worked off unfulfilled orders but now it's May

We expected the consensus beat because April USD exports also beat (+3.5%YoY > Consensus -11.0%). The export beat was likely linked to China working off of orders that were impossible to fulfill during the January-February lockdown, so there is an implicit silver lining that earlier orders had at least not been cancelled outright. But with global demand anemic, this is the month (May) we need to track more closely to see whether orders are evaporating as elsewhere in the neighborhood (eg, Taiwan and Korea). In other countries we would be watching inventories to see if there are signs of involuntary accumulation, but Chinese inventory data is next to worthless.

Autos and telecoms/computers are the outperformers

There do seem two rays of light in further VAI breakdowns. Automakers appear back on track, +5.8%YoY in April compared with -22.4% in March (when some platforms were sputtering upon restarting). Key question here is whether there will be demand for the cars that are made (see above)? The other ray of light came in telecoms/computers, whose March-April growth momentum matched what was observed in 4Q19. We had earlier noted Shenzhen traffic congestion patterns were the fastest to get back to normal across the major cities.

Fixed Asset Investment: -10.3%YTD ~ Consensus -10.0% and < Last -16.1%

Still difficult to stoke up infrastructure, but wait! CNY4trn of bonds on the way

Here there continues this theme that it's been difficult the past couple of years to get infrastructure spending going from the central government alone (FAI in China is perennially 95%+ a local government story). Don't worry: CNY4trn (hello, 2009!) of "special" local government bonds are on the way to the rescue. We're tempted to call them "very special."

The Unemployment Problem

Politically we didn't think the unemployment rate can rise > 6.2%

It was a bit of a surprise to us the surveyed unemployment rate crept back up by a tick, from 5.9% to 6.0%. We previously wrote we didn't think the record high 6.2% unemployment of February would be allowed to cross higher, so for March the rate dutifully marched down to 5.9%.

But it's still sticky high

But the persistence of a high unemployment rate (by the standards of China) points to possibly serious underlying unemployment problems that we also highlighted in our April monthly.

SCMP has a multi-part survey of Chinese unemployment that's worth reading

Hong Kong's *South China Morning Post* put out a 6-part series on the unemployment problems of China after COVID-19, noting:

Already in 1Q20 the implied drop in urban employment was about 26mn jobs.

Officially we lost 26mn jobs in 1Q20 but what about …

But SCMP further emphasized that China's surveyed unemployment figures - which are supposed to follow ILO standards and were meant to be an improvement over the older #s that were based on urban unemployment registrations - are missing out on two big groups.

Migrant workers?

One are 174mn migrant workers. In 1Q20, the lockdown and partial unlocking meant only 123mn had managed to make it back to jobs by end-quarter to resume work.

Where COVID-19 afflicted service jobs account for the majority

Moreover, NBS surveys for several years had shown that service jobs (eg, delivery drivers) now constitute more migrant work than traditional manufacturing jobs. And as we have learned, COVID-19 has consistently been a bigger hit to the service sector than to manufacturing.

The other missing big group of workers are:

And the self-employed?

China's 149 million self-employed workers – ranging from owners of family-run fruit and vegetable shops to neighbourhood hardware stores – have watched their income tumble on average 7.3 per cent in the first quarter, and a steeper 12.6 per cent in urban areas, the statistics agency said.

Whose business income have cratered

Here 1Q20 #s showed a particularly precipitous fall in the business income part of urban disposable income. That's likely tied to the self-employed and to reported sluggishness in the SME sector.

So overall: About 18.3 per cent of the workforce had been furloughed, taken a pay cut or unpaid leave in the first quarter, according to the NBS. [Tying into earlier anecdotal reports we posted of wage cuts or even the employed not receiving any pay = unpaid leave.]

Fewer jobs, lower pay = slower consumption

Bottom Line, as we said, is prosaic but also straightforward: Fewer jobs, lower pay = slower consumption.

Market Implications: Reluctance < 7

We might feel a bit antsy if USD/CNY fell below 7 again

The Macro Roundup this time leaves an impression of a recovering economy but one still a ways from digging itself out of a big hole. One market implication to us, logically, would be authorities who, having sent RMB > 7 last year, will be reluctant to see it < 7 anytime soon.

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