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2Q 2023 China Economy Update: The Locomotive is Powering Through Amid Global Headwinds

Executive Summary

Recently, National Bureau of Statistics of China released a slew of the country's economic data for 2Q 2023 that failed to live up to heightened expectations. Specifically, the country's GDP, a comprehensive measure of its economic activity, grew only 0.8% Q/Q in the quarter, as compared to 2.2% quarterly increase in 1Q 2023. The slowdown has sparked growing pessimism across the board, as many analysts are speculating the data indicates that China's remarkable economic growth achieved in past decades is coming to an end and the robust recovery seen in 1Q 2023 after the removal of COVID-19 induced restrictions is fading. Some economists believe that latest economic dataset raises the risk of China missing its modest 5% GDP growth target for 2023. As a result, various institutions have provided dull forecast of China's 2023 GDP growth rate of below 5%, potentially leading to a sub-5% GDP growth for three consecutive years through 2024 after a 3% expansion in 2022.

However, we believe the negative view on China is politicized and biased, and the economic outlook of China could be more positive, with the Chinese economy acting again as the world economy "locomotive" after COVID-19 induced disruptions. The World Bank projects that the pace of China's GDP growth to rise to 5.6% in 2023, led by a rebound in consumer demand. Meanwhile, capital spending in infrastructure and manufacturing is expected to remain resilient. At the same time, the International Monetary Fund ("IMF") forecasts China's economy to grow at a similar rate of 5.2% in 2023. In the medium-term, growth is expected to return to a path of structural deceleration for which Chinese policymakers have long prepared. Taking a closer look at the statistics, the quarterly numbers may not necessarily reveal the full picture in part due to ignoring the impact from seasonality. Examining 1H 2023 data, China's economy looks much healthier than that depicted by some economists, with GDP and imports (by volume) growing 5.5% and 1.0% respectively relative to 1H 2022.

Besides manufacturing and services, the sluggish property market, which normally accounts for more than one quarter of China's GDP, has been a drag on the country's economy. Declining sales owing primarily to weak consumer confidence rather than affordability and to some extent government's preemptive measures to prevent the formation of asset bubbles have caused some over-leveraged property developers in financial distress. The bleak outlook of the property market has aroused fear of a repeat of the U.S. subprime mortgage crisis in 2008, resulting in the collapse of home prices and turmoil of the financial system. Nonetheless, we believe the Chinese real estate market is fundamentally stable and healthy, without reckless mortgage lending and widespread spillover effect as we seen in the U.S. that led to a global GDP contraction of 1.3% in 2009.

China's economy is currently facing challenges attributable primarily to tepid demand both at home and abroad, but it is unlikely to follow the Japan's footsteps and undergo years of lackluster growth after the "Lost Decade"[1] because of the following four reasons:

[1] A period of economic stagnation when big banks overleveraged with speculative investments failed and borrowers became insolvent in Japan caused by the asset price bubble's burst in late 1991 after the central bank hiked interest rate to 6% in 1990 to curb speculation

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