

## Economic Analysis

## Keep calm: August blip doesn't mean an imminent hard-landing

Le Xia and Jinyue Dong

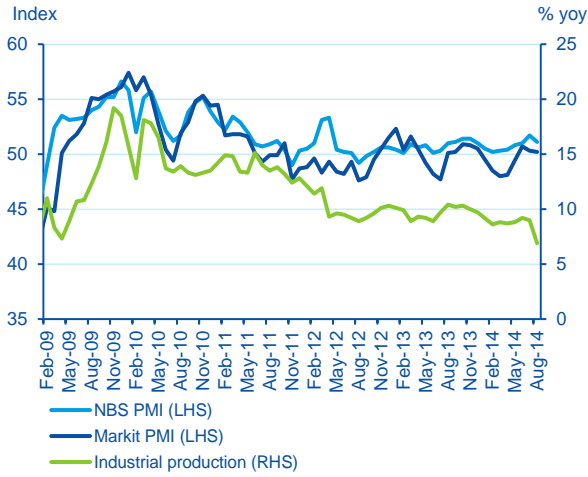
China's government announced a batch of important activity indicators over the weekend, among which, industrial production, retail sales and fixed asset investment, were all below market expectations as well as their growth rates in the previous month. In particular, industrial production fell sharply to 6.9% y/y in August (consensus: 8.8% y/y) from July's 9.0% y/y and registered the lowest reading since December 2009, which has greatly fuelled investors' worries about a growth hard-landing.

Although the slowdown in growth momentum is evident, we believe that the situation might not be as bad as the headline figures showed. A confluence of base effect and certain one-off factors have negatively distorted August outturn of industrial production (see below). Furthermore, credit growth in August, released on last Friday, recovered part of lost ground and gave investors a sigh of relief. With ample options of policy stimulus at their disposal, the authorities can still sustain this year's annual GDP growth above 7.0%. We expect more targeted loosening measures to be deployed in the rest of the year. The probability of the PBoC's adopting universal RRR cuts is increasing too. Overall, we maintain our annual GDP forecast at 7.2% for this year, implying a 7.0% y/y growth for the second half of the year.

Nevertheless, the disappointing August indicators did sound the alarm for the authorities. To a large extent, they show that the stimulus packages tend to become less effective and short-lived after they were frequently used over the past several years to lift growth. That said, the authorities need to accelerate the structural reforms promised in their agenda of the Third Plenum last November, so as to put growth on a sustainable trajectory and to reduce its reliance on short-term policy stimulus.

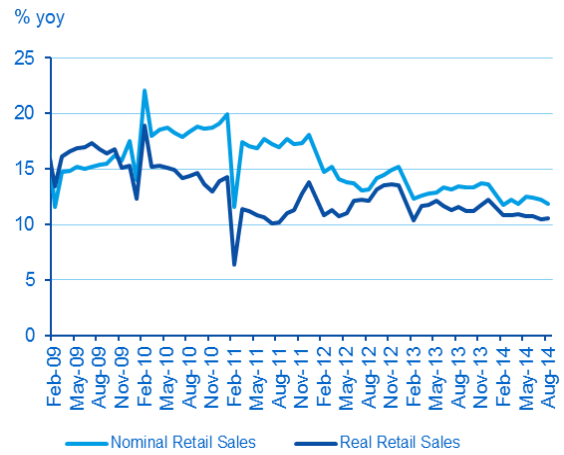
- **Economic activities fell sharply in August due to sluggish domestic demand.** Industrial production slowed to 6.9% y/y in August from 9.0% y/y in the previous month (Figure 1), significantly below expectations (Consensus: 8.8% y/y). Although the print was partially affected by an unfavorable base effect (Industrial production achieved its within-the-year peak in August 2013) as well as the anti-monopoly investigations against foreign automakers, the significant slowdown in growth momentum is still the primary culprit. In particular, the persistently subdued housing market has exerted negative spillover effects on production activities in related industries such as construction materials, furniture and home appliance. On the other hand, the deceleration of retail sales and the total fixed asset investment growth appeared to be mild: retail sales softened to 11.9% y/y in August (Figure 2), compared with 12.2% y/y in July, while the total fixed asset investment fell to 16.5% y/y YTD in August from 17.0% y/y YTD in July. (Figure 3)
- **Credit growth improved in August, staving off a fear of credit crunch.** The total social financing, a broad gauge of credit including bank loans, bond issuance and shadow banking activities, surged to RMB 957.4 billion from RMB 273.1 billion in July; while new bank loans increased to RMB 702.5 billion from RMB 385.2 billion in July (Figure 4). Accordingly, M2 growth dropped to 12.8% y/y from 13.5% y/y in July. As we explained in our previous flash, July credit data was seriously distorted by banks' "mid-year window dressing" so that investors shouldn't read too much into it. In August, credit growth seemed to be back on track and was likely to lend support to growth stabilization in the coming months.

**Figure 1**  
**Industry production fell sharply due to sluggish domestic demand**



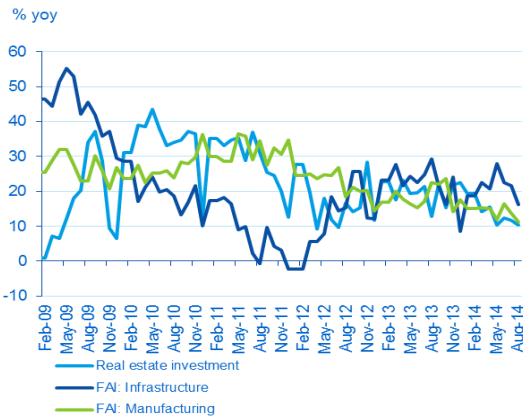
Source: CEIC and BBVA Research

**Figure 2**  
**Retail sales moderated in August**



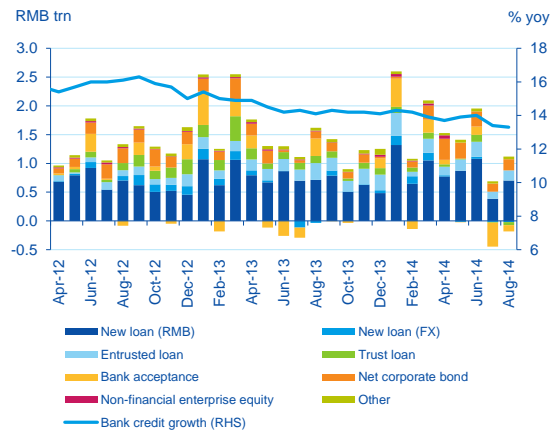
Source: CEIC and BBVA Research

**Figure 3**  
**Weakening fixed asset investment was led by the continuous deceleration of the property market**



Source: CEIC and BBVA Research

**Figure 4**  
**Both bank loans and total social financing bounced back from the last month**



Source: CEIC and BBVA Research

**DISCLAIMER**

This document has been prepared by BBVA Research Department, it is provided for information purposes only and expresses data, opinions or estimations regarding the date of issue of the report, prepared by BBVA or obtained from or based on sources we consider to be reliable, and have not been independently verified by BBVA. Therefore, BBVA offers no warranty, either express or implicit, regarding its accuracy, integrity or correctness.

Estimations this document may contain have been undertaken according to generally accepted methodologies and should be considered as forecasts or projections. Results obtained in the past, either positive or negative, are no guarantee of future performance.

This document and its contents are subject to changes without prior notice depending on variables such as the economic context or market fluctuations. BBVA is not responsible for updating these contents or for giving notice of such changes.

BBVA accepts no liability for any loss, direct or indirect, that may result from the use of this document or its contents.

This document and its contents do not constitute an offer, invitation or solicitation to purchase, divest or enter into any interest in financial assets or instruments. Neither shall this document nor its contents form the basis of any contract, commitment or decision of any kind.

In regard to investment in financial assets related to economic variables this document may cover, readers should be aware that under no circumstances should they base their investment decisions in the information contained in this document. Those persons or entities offering investment products to these potential investors are legally required to provide the information needed for them to take an appropriate investment decision.

The content of this document is protected by intellectual property laws. It is forbidden its reproduction, transformation, distribution, public communication, making available, extraction, reuse, forwarding or use of any nature by any means or process, except in cases where it is legally permitted or expressly authorized by BBVA.