BBVA | Research

China Economic Outlook

4th QUARTER 2017 | ASIA UNIT

Index

Closing date: **13 October 2017**

1. The positive global environment is strengthening

The growth of the world economy stabilised by mid-year at around 1% QoQ, and the available indicators suggest so far that this trend will continue in the second half of the year. Global confidence indicators have continued to improve, both in advanced and emerging economies, and anticipate a more positive outlook than the activity indicators which slowed down at the beginning of the third quarter. Nonetheless, global trade growth remains solid and the recovery of the industrial sector continues apace, underpinning the upturn in investment, while private consumption remains resilient despite weaker tailwinds.

This positive dynamic reflects a stronger economic performance in all areas. In the advanced economies, US GDP rebounded in Q2 and dispelled doubts over the sustainability of modest growth in the coming quarters, while a greater strength from domestic factors was behind the positive surprise in Europe. In emerging economies, stable growth in China will continue to support the rest of Asia, which, coupled with favourable financial markets conditions, is also allowing growth in LatAm countries to gain traction. Finally, the recovery in Russia and Brazil means that these two are no longer dragging global growth.

In an environment where growth remains dynamic and with no downward surprises in inflation, central banks are pressing ahead with the gradual process of withdrawing monetary stimulus. Specifically, the US Federal Reserve (Fed) has announced the start of a reduction in its balance sheet from October onwards. We expect a 25 bp hike for official rates in December this year and then two further hikes up to 2% in 2018. The European Central Bank (ECB) will announce a scaling down of its asset purchase programme in October, which it would start to implement in January next year. Our scenario contemplates a gradual reduction in purchases until the programme ends in summer 2018. Rate hikes, however, will be delayed until mid-2019, largely due to the ECB's growing concern over euro appreciation and its potential impact on inflation.

All in all, we maintain our GDP growth forecast of 2.1% in 2017 and 2.2% in 2018. The solidity of global growth, dollar depreciation, expectations of sustainable oil prices and the mild improvement in construction should support an upturn in investment. On the contrary, the more gradual improvement in the labor market and higher inflation lead us to continue to forecast a slowing down in private consumption over the forecast horizon. Even so, more sluggish growth in prices in recent months and the absence of any clear signs of inflationary pressures mean that we expect the Fed to continue slowly with its normalisation process for monetary policy.

The risks for this scenario are still to the downside owing to the unknowns regarding the implementation of the economic policy measures announced, whereas the long period of cyclical expansion together with lax demand-side policies still work in favour of an accumulation of financial vulnerabilities that could trigger a recession in the medium term.

2. Policy-led growth moderation coupled with mitigated risks

After registering a stronger-than-expected growth in the first half of the year, the economy showed more signs of moderation in the third quarter due to a number of policy initiatives. These policy initiatives can be further classified to two set. The first set of policy measures focuses on risk management, including the authorities' prudent monetary policy, the stepped-up regulatory tightening on shadow banking activities as well as the overheating property market, and the stronger exchange rate boosted by the authorities' increasing invention. The second set of policy initiatives includes various forms of the supply-side reform. In particular, the authorities recently enhanced the enforcement of the existing environmental policies to exit obsolete and high-polluted capacity in certain industry on top of their efforts to use administrative orders to eliminate overcapacity.

Apart from reining in financial risks, the first set of policy initiatives also weighed on aggregate demand. Tightening credit condition, stemming from a combination of prudent monetary policy and tightening regulations, tends to dampen domestic investment while a strong currency has taken a toll on exports. Meanwhile, the measures of supply-side reform have led to a contraction of supply and boosted price indicators, to a greater extent for PPI. As such, growth has somewhat moderated of late amid the policy-led headwinds from both the supply and demand sides.

On a positive note, a number of long-standing financial risks have shown positive signs of stabilization or even marginal improvement thanks to the abovementioned policy measures. In particular, the authorities' efforts to curb shadow banking activities and housing bubbles have started to take effect. (Please refer to our report Taming China's shadow banking sector) The indebtedness of the corporate sector also halts its deteriorating trend not only for that the growth rate of nominal GDP have broadly surpassed the pace of aggregate credit expansion so far in this year but also for that the increased price levels resulted in a fast rebound in firms' profits. Moreover, capital outflows have significantly slowed thanks to both effective implementation of restrictive measures under the capital account and investors' alloyed concern over sharp currency depreciation.

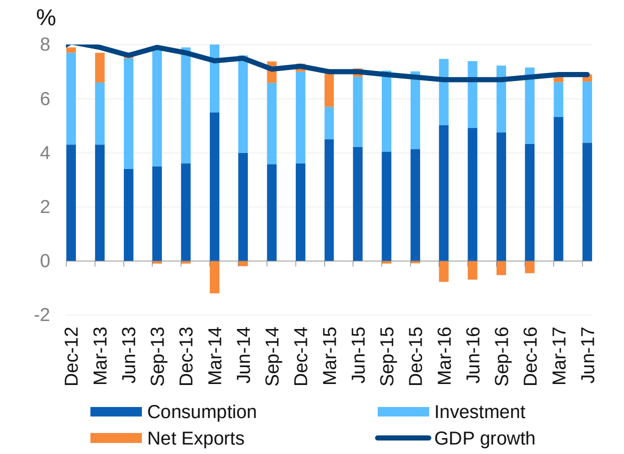
All in all, a policy-led moderation in growth has come hand-in-hand with alleviated financial risks. With a strong outturn in the first half of the year, it is no doubt that the authorities can meet this year's official growth target of around 6.5%. Looking ahead, the dynamic of China's economy in the coming months will highly depend on the authorities' attitudes towards the balance between pursuing growth and maintaining financial stability.

More signs of growth moderation emerged after a strong Q2 growth

The Q2 GDP outturn (6.9% y/y) extended its good performance of Q1. Sequentially, GDP expanded by 1.7% q/q, compared to a mere 1.3% q/q in the first quarter. By category, the contribution of investment to the total GDP growth picked up in Q2 due to both seasonal factors and improved investors' confidence. The net exports continued to make a small but positive contribution to the total GDP growth thanks to the improving external environment. (Figure 2.1)

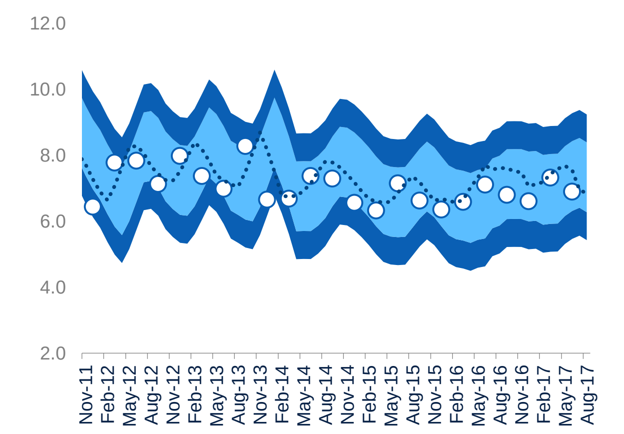
Despite the economy's stronger-than-expected performance in 1H, a batch of activity and credit indicators released recently indicate that growth is losing its momentum of late. In particular, our MICA model yields a monthly GDP estimate 6.84% in August (6.90% in July), down from readings in the second quarter. (Figure 2.2) We expect that Q3 GDP will further decelerate to 6.6% in the third quarter. That being said, the growth is subject to a number of policy headwinds from both supply and demand sides.

Figure 2.1 Growth momentum in 1H is strong



Source: BBVA Research and CEIC

Figure 2.2 BBVA MICA model for GDP forecasting



Source: BBVA Research and CEIC

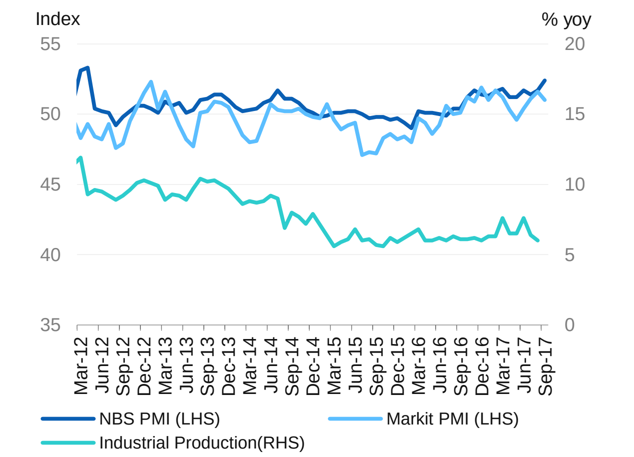
On the supply side, the growth of industrial production significantly decelerated to 6.0% y/y in August from 6.4% y/y previously (consensus: 6.6% y/y). Meanwhile, the different indicators of producers' sentiment sent mixed signals. China's official manufacturing PMI has been trending up through the third quarter and climbed to 52.4 in September from 51.7 in August, well above market expectations (Consensus: 51.6) and registering the highest since April 2012. However, the Caixin China Manufacturing PMI, which includes a survey sample tilting toward SMEs and exporters, declined to 51.0 in September (versus consensus 51.5) from 51.6 in the previous month. (Figure 2.3)

The divergence between the official PMI and Caixin PMI as well as the anemic growth in industrial production confirmed our assessment that some growth headwinds such as the RMB appreciation and the enforcement of environmental policy tend to have a greater adverse impact on SMEs and exporters rather than larger enterprises. Overall, the supply-side reform and the enforcement of environmental policy have led to production disruption.

Both supply and demand sides subject to headwinds.

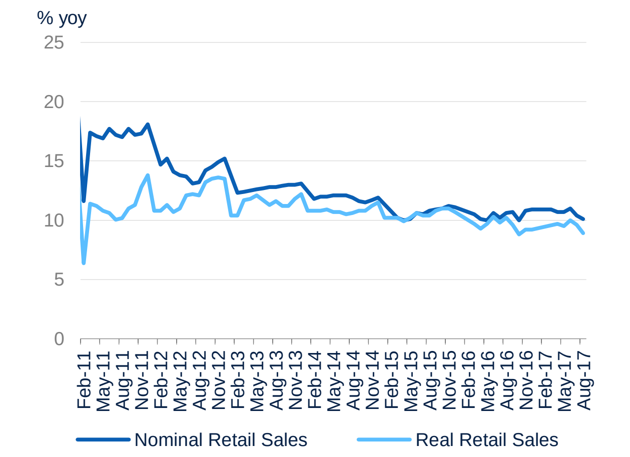
The demand side is also subject to downward pressure. Retail sales growth slowed down to 10.1% y/y in August from 10.4% y/y in July (consensus: 10.5% y/y). (Figure 2.4) The slowdown is led by auto sales, which grew by 6.0% y/y in August compared to a 6.4% y/y growth in July, mainly due to the expiration of fiscal subsidy for passenger car purchase. The silver lining is the rapid growth of online sales, surging 34.3% y/y in the first eight months of the year from 33.7% in the first seven months.

Figure 2.3 Decoupling between PMIs and industrial production



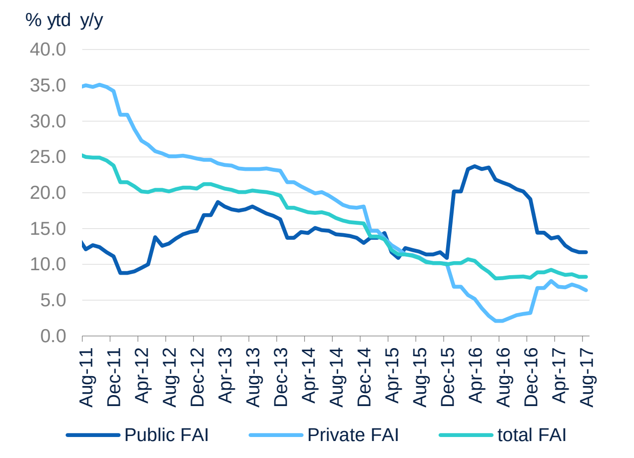
Source: BBVA Research and CEIC

Figure 2.4 Both real and nominal retail sales declined



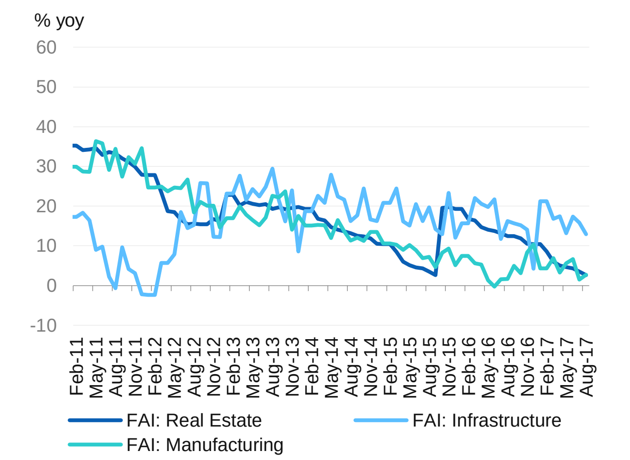
Source: BBVA Research and CEIC

Figure 2.5 Private and Public investment display the trend of converging



Source: BBVA Research and CEIC

Figure 2.6 Infrastructure investment has softened



Source: BBVA Research and CEIC

Demand-side weakness is also reflected on urban fixed asset investment, which dipped to 7.8% ytd y/y in August (consensus 8.2% ytd y/y) from the previous month reading of 8.3% ytd y/y. Accordingly, the growth of private investment declined to 6.4% ytd y/y in August from 6.9% ytd y/y previously. (Figure 2.5) Moreover, the slowdown in investment is broad based across the infrastructure, real estate and manufacturing sectors. (Figure 2.6) Apart from the financial tightening stemming from prudent monetary policy and the clampdown on shadow banking activities, investors could intentionally hold their investment projects in the run up of the Party's National Congress which is to be held in mid-October.

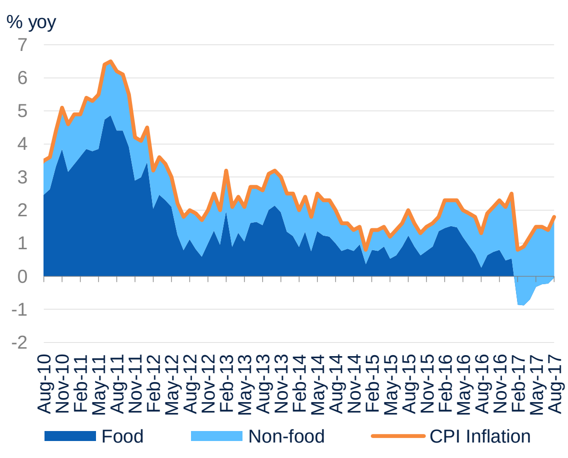
Price indicators affected by supply-side shocks

The policy-led disruptions of supply side have bolstered up both CPI and PPI and widened their gap again. Headline CPI inflation picked up to 1.8% in August, above market consensus of 1.6% and up from July's reading of 1.4%.The uptick in CPI inflation was driven by food prices as their negative contribution to year-on-year price increase significantly narrowed in August.(Figure 2.7)

On the other hand, PPI started to pick up to 6.3% y/y from 5.5% y/y in July due to the shortfall of certain products caused by supply-side disruptions. The rising PPI has lent a great support to bolster firms' profits and nominal GDP to alleviate the debt overhang of the corporate sector. (Figure 2.8) However, we reckon these one-off shocks of the supply side cannot be sustainable. That being said, CPI and PPI are likely to converge gradually in the coming months.

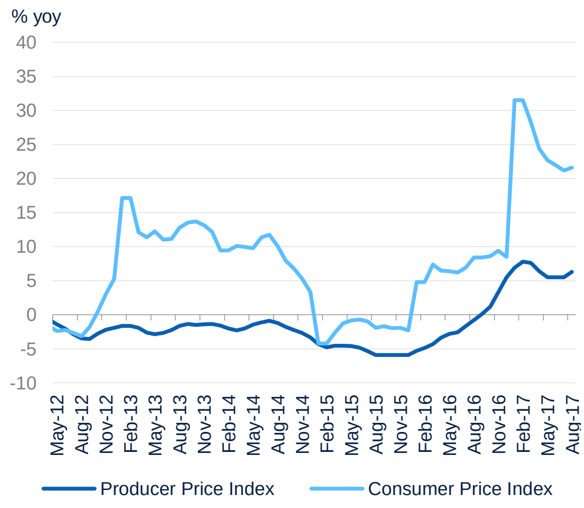
Convergence of CPI and PPI looks set to be delayed again

Figure 2.7 CPI picked up marginally in August



Source: BBVA Research and CEIC

Figure 2.8 Rising PPI boosted profit growth



Source: BBVA Research and CEIC

The unexpected RMB appreciation has taken a toll on exports

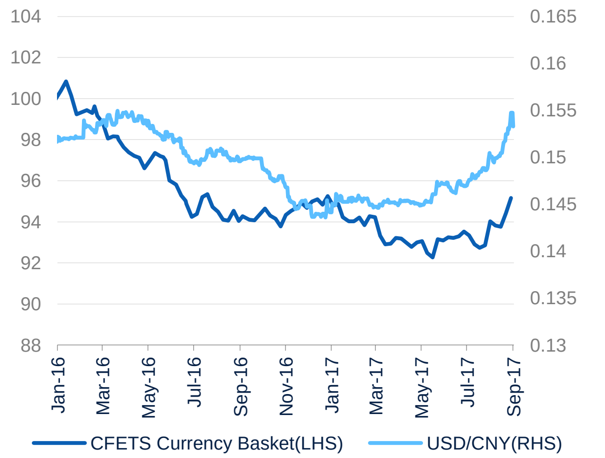
The RMB exchange rate experienced a sharp appreciation between July and mid-September on the backdrop of a sluggish USD. Accumulatively, the RMB has appreciated by 2.3% against the USD since the beginning of the second quarter. It is noted that the RMB appreciation during this period is not only against the USD but also against the CFETS currency basket. (Figure 2.9) Despite the persist weakness of the USD, the strong rebound of the RMB also benefits from the ever-increasing restrictions under the capital account as well as the adjustment of the RMB fixing price against the USD. Moreover, the appreciation of the RMB also has its self-fulfilling nature as exporters flocked to exchange their foreign currency revenues for the RMB after seeing a streak of currency strength.

The RMB appreciation pushed up the imports while weighed on exports

However, the unexpected strength of the RMB has taken a toll on its external sector. In September, the growth of exports (in USD terms) increased to 8.1% y/y (versus consensus: 10.0% y/y) from the previous reading of 5.5% while imports registered a year-on-year growth of 18.7% (versus consensus: 14.7% y/y ; July: 13.3% y/y). As a result, the balance of trade narrowed to USD 28.5 billion in September from USD 41.99 billion in August. (Figure 2.10)

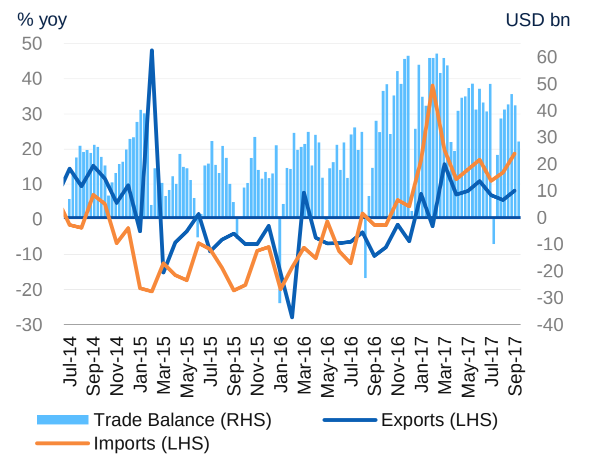
The authorities are wary of the adverse impact of sharp currency appreciation on its exports and have recently attempted to halt its uptrend. In particular, the authorities repealed the 20% reserve requirement for buying FX forwards so as to reduce the costs of shorting the RMB exchange rate.

Figure 2.9 Imports growth has outperformed exports since 2H 2016



Source: BBVA Research and CEIC

Figure 2.10 The comparative weakness in processing trades reflects the loss of low-labor -cost



Source: BBVA Research and CEIC

Risks to BOP eased

Foreign reserves continued to grow in the third quarter and reach USD 3.11 trillion at end-September, up from USD 3.02 trillion in July. (Figure 2.11) Barring the favourable valuation effects of non-USD foreign reserves over the past several months (which we estimated to account for one third of China's total foreign reserves), the narrowed capital outflows also contributed to the growth of foreign reserves. In particular, we estimate that capital outflows amounted to USD 16.1 billion in August, significantly down from USD 33.4 billion in the previous month. (Figure 2.12)

The increase in foreign reserves and moderating of capital outflow could continue in the following months.

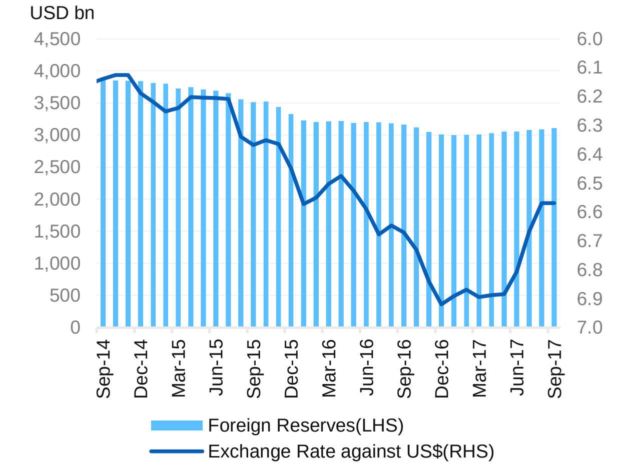
The slower capital outflows mirrored the success of the authorities' policies of "promoting inflow and tightening outflow". On top of a series of opening measures to domestic financial markets such as the Bond Connect programme, the authorities have beefed up their efforts to clamp down illegal capital flows. Moreover, the authorities announced new guidelines for regulating outward FDI. In particular, new guidelines classified all outward FDI into three categories of Banned, Restricted and Encouraged as below:

- Banned: Core military technology, gambling, sex industry, investments contrary to national security

- Restricted: Property, hotels, film, entertainment, sports, obsolete equipment, investments that contravene environmental standards
- Encouraged: Investments that further Belt and Road framework, enhance China's technical standards, research and development, oil and mining exploration, agriculture and fishing

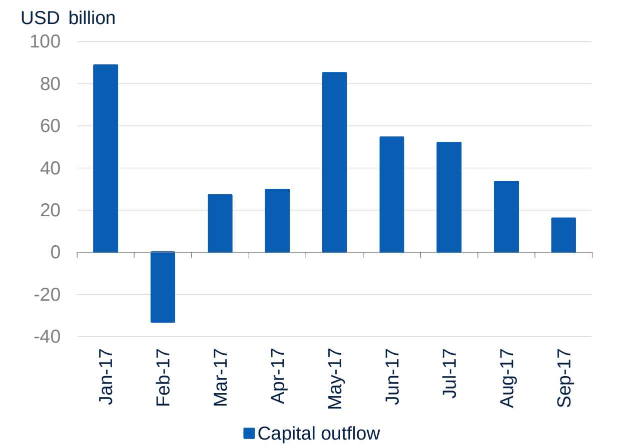
As such, we expected that these measures under the capital account as well as stabilized foreign reserves will continue to mitigate risks to China's Balance of Payment (BOP) and help to avert a vicious spiral of currency depreciation and capital flight.

Figure 2.11 Foreign reserves recorded several months of growth



Source: BBVA Research and CEIC

Figure 2.12 Estimates of Capital outflows



Source: BBVA Research and CEIC

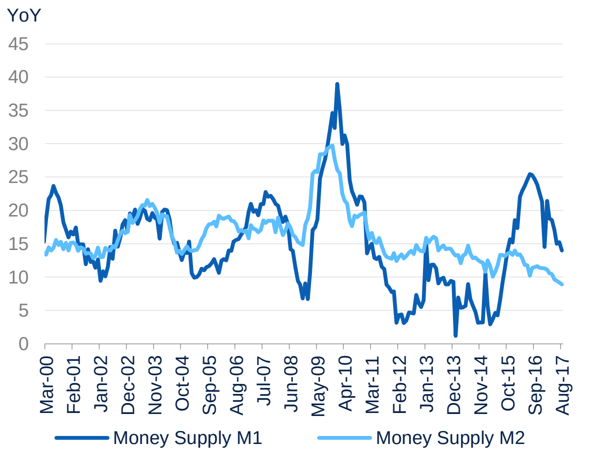
Monetary prudence and tightening regulations helped to contain credit boom

The authorities fine-tuned their monetary policy stance at end-2016 from "accommodative" to "prudent". In practice, the PBoC even guided market interest rates to a higher level so as to curb shadow banking activities and contain credit boom. These measures have taken effect as M2 growth dipped to its historical low of 8.9% y/y in August, compared with the previous month's reading at 9.2% YoY (consensus: 9.1% YoY). (Figure 2.13)

The monetary prudence and macro-prudential measures have led to slowdown in M2.

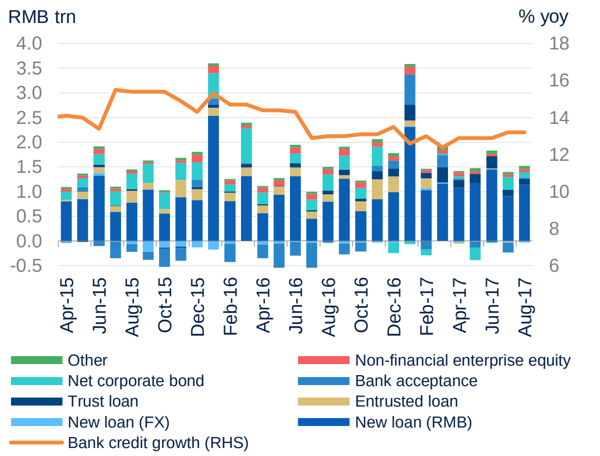
Meanwhile, the growth of new loans and total social financing are steady as funding demand remains firm. In particular, total social financing increased to RMB 1,479 billion (prior: RMB 1,220.0 billion; consensus: RMB 1,280.0 billion) in August. (Figure 2.14) Importantly, new loans now accounts for a larger share of total social financing than before, implying that banks have moved a considerable size of their off-balance-sheet business back to their books as guided by the authorities. Such a trend will help to contain the risks associated with shadow banking activities and fast credit growth.

Figure 2.13 M2 growth dipped significantly in August



Source: BBVA Research and CEIC

Figure 2.14 Shadow banking activities start to shrink



Source: BBVA Research and CEIC

Housing markets continue to cool down

The tightening measures on the property market have effectively moderated price increases and frozen the trading volume in Tier 1 cities (Figure 2.15). As more local authorities started to deploy tightening measures in cities other than tier 1, housing bubbles now seem to ease further. (Figure 2.16) On top of impose home purchase restrictions; the authorities also use financial tools to contain housing bubbles. For example, in several cities with rapid growth of property prices, the authorities increased the interest rate of mortgage loans. Moreover, the authorities particularly forbid home buyers from borrowing short-term loans to pay for their down payment, in a bid to keep household leverage at a manageable level.

Figure 2.15 The volume of housing transactions decline significantly

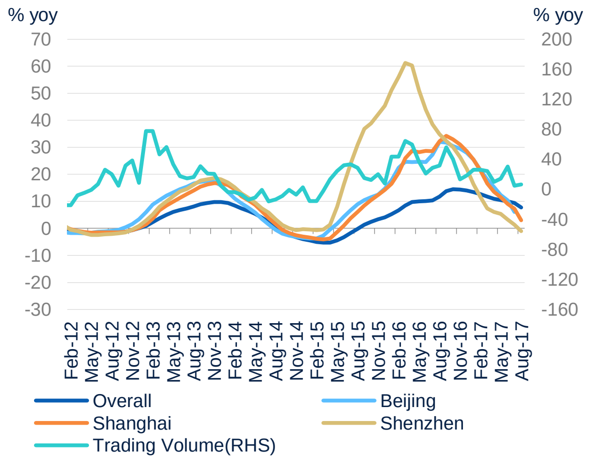
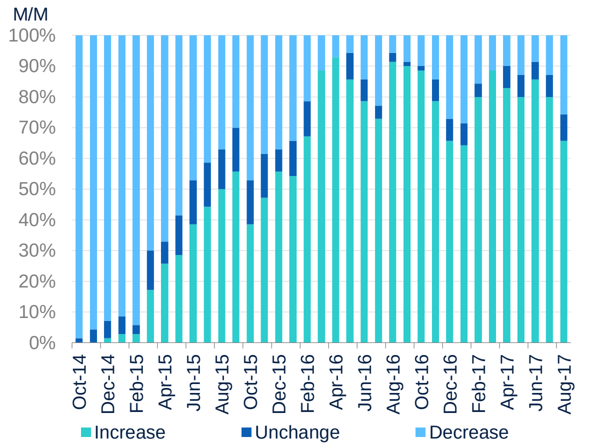


Figure 2.16 Mega-cities report remarkable price decline due to tighter regulations



Source: BBVA Research and CEIC

Source: BBVA Research and BIS

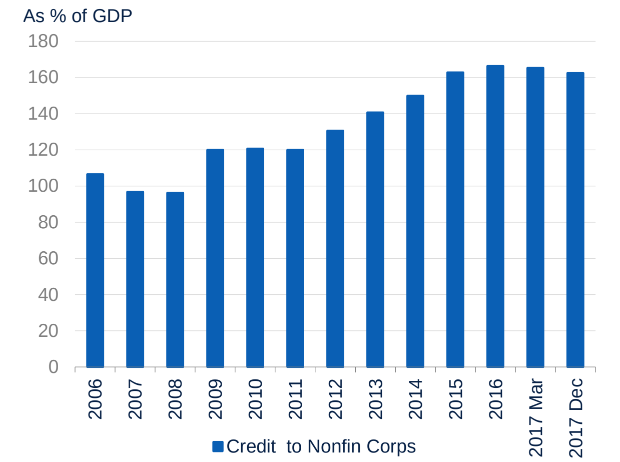
Corporate deleveraging has born some early fruits

Many investors' prime concern of China's economy is the sustainability of China's corporate debt, which increased from 130.6% of GDP in 2012 to 166.2% of GDP in 2016. (Such a fast rise in credit generally leads to a financial crisis in other countries, which makes investors increasingly worried about China's outlook. (Figure 2.17)

Debt level in China is still sustainable.

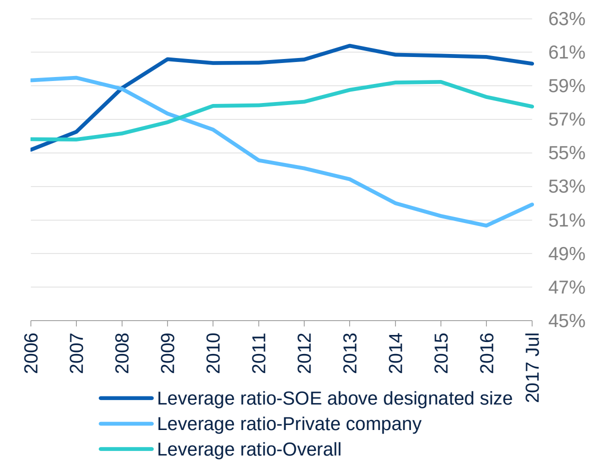
Fortunately, the authorities have already realized the seriousness of this debt problem and set out to tackle it. The BIS has reported a slight decline of China's corporate debt to its GDP in the first quarter of 2017. We also find some evidence that both SOEs and non-SOEs have made some encouraging progress in lowering their leverage ratio (refer to our previously circulated note Early fruits of corporate deleveraging add to growth resilience (Figure 2.18) We estimate that the corporate debt level will continue its gradual correction in the remainder of the year and decline towards 162.5% of GDP by end-2017. (Figure 2.17)

Figure 2.17 China's debt level slightly declined in Q1



Source: BBVA Research and BIS

Figure 2.18 Diverging leverage ration between SOE sand non-SOEs



Source: BBVA Research and NBS

3. Awaiting the important policy meeting amid growth slowdown

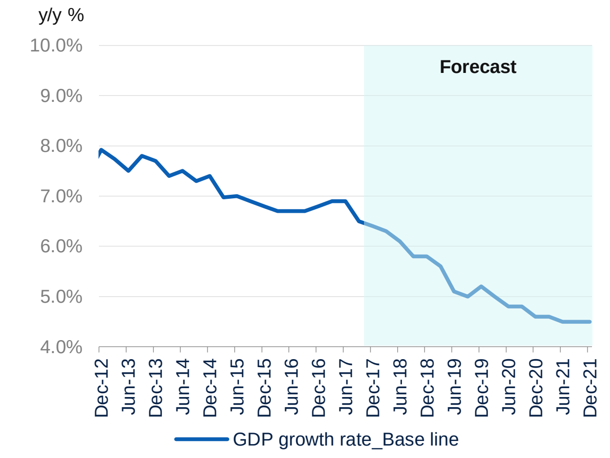
Upward revision of short-run GDP while long-run slowdown is set to continue

China's growth has exhibited some new developments into the third quarter. On one hand, more signs of moderation emerged in the third quarter due to a number of policy-related headwinds include monetary prudence, regulatory efforts to curb shadow banking activities and overheating property market and even recent currency appreciation. On the other hand, these policy initiatives have helped to mitigate several tail risks to the economy and financial stability, increasing the likelihood of a soft-landing scenario for the world's second largest economy.

Accordingly, we raise our 2017 growth forecast to 6.7% from 6.5% previously (official target: 6.5%; Bloomberg consensus: 6.7%), reflecting the strong 1H growth and mitigated risks. Nevertheless, we anticipate that the authorities broadly maintain the policy mix in the next couple of years over the concern of financial stability. We therefore keep our growth projection of 2018 unchanged at 6.0%. The growth will be mainly driven by domestic consumption.

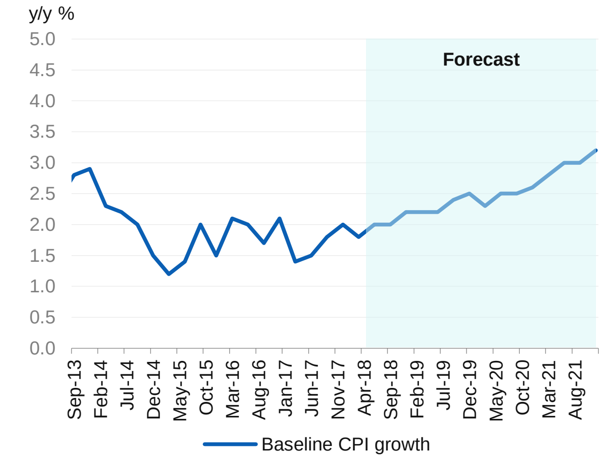
Regarding inflation, we remain our 2017 monthly average projection of CPI at 1.7% at the end of 2017 (Figure 3.2) due to lower-than-expected food prices in the first half of the year. Looking ahead, the CPI and PPI will gradually converge over time. CPI is expected to trend up gradually after the food-prices rebound from the current low level. Meanwhile, the PPI will gradually slow its pace. That being said, supply-side shocks caused by overcapacity elimination are likely to have diminishing marginal impact on price levels as investors gradually factor it into their expectations.

Figure 3.1 We have raised our 2017 GDP forecast to 6.7% from 6.5% previously



Source: BBVA Research and CEIC

Figure 3.2 We keep our CPI forecast at 1.7% for 2017



Source: BBVA Research and CEIC

Currency depreciation will continue with a measured pace

The strong performance of the RMB has made us revise our projections of the exchange rate, mainly in the pace but not in the direction. We anticipate that the exchange rate will soften towards 6.75 by the end of 2017 and continue its mild deprecation next year (6.90 by end-2018). Such a trajectory means a relatively stable value against the CFETS currency basket, which has become the important anchor of the RMB. (Table 3.1)

We believe that a "clean float" remains the authorities' ultimate goal of exchange rate reform. The floating of the RMB might take place in the second half of 2019, which could make the exchange rate overshoot to 7.4 during a short period but ultimately go back to its long-term equilibrium level of around 7.

Table 3.1 Baseline Scenario

Baseline Scenario

	2016	2017 (F)	2018 (F)	2019 (F)	2020 (F)	2021 (F)
GDP (%, YoY)	6.7	6.7	6.0	5.2	4.8	4.5
Inflation (average, %)	2	1.7	2	2.3	2.5	3
Fiscal balance (% of GDP)	-3	-3.5	-3.5	-4	-4	-4
Current account (% of GDP)	2.5	2.3	2.4	2.5	2.5	2.5
Policy rate (%)	**4.35**	**4.35**	**4.1**	**3.6**	**3.6**	**3.6**
Exchange rate (CNY/USD)	**6.95**	**6.75**	**6.9**	**7.4**	**6.9**	**6.8**

What's in the 19th Party's National Congress

On October 18th the Chinese Communist Party (CCP) will hold its 19th National Congress. By then 2,300 delegates of the CCP, on behalf of 87.8 million CCP members, will convene at Beijing for around a week to form the Party's ruling organizations over the next five years, including the Central Committee, the Politburo and the Standing Committee of the Politburo. In addition to reshuffling the ruling organizations, the Party's Congress is bound to announce a new set of important policy guidelines and certain targets of social and economic development for the next five years.

Setting long-term growth targets is always at the top of the agenda for the Party's Congress. At the 17th Party's Congress held in 2007, the Party set up two long-term goals of (i) building a Moderately Prosperous Society by 2020 and (ii) quadrupling 2000 GDP level by 2020. Five years later, the 18th Party's Congress reiterated the goal of building a Moderately Prosperous Society while amended the other growth target to double 2010 GDP level by 2020.

The first goal set at the 18th Party's Congress seems achievable. However, the second long-term goal looks more challenging. Doubling the GDP size between 2010 and 2020 implies an average aggregate GDP growth rate of 6.4% during the period of 2017-2020, which is almost 1% higher than the implied growth rate of the first growth target. Given that China's economy is still on its trajectory of slowdown and subject to enormous financial vulnerabilities from severe corporate indebtedness to rampant shadow banking activities, maintaining an average growth rate of 6.4% between 2017 and 2020 could be difficult if not impossible.

More interesting is the new long-term growth target to be set at this Congress, in particular the one beyond 2020. The authorities must have learned a lot of lessons from the past experience with respect to how pursuing a too high growth rate could lead to serious distortions in the economy and build up the debt level of local governments and the corporate sector.

We are waiting to see how the authorities will balance different considerations in setting new long-term growth target at the incoming Congress. It might be good news if the authorities are willing to announce lower but attainable long-term growth targets or show more flexibility to them (for example, announce a range instead of a point target) at the Congress.

The Reform Agenda

In the third session of the 18th Party's Congress held in 2013, the authorities have come up with an excellent blueprint for reform comprehensively covering many aspects of social and economic development. This ambitious reform plan once boosted investors' confidence in China's economy greatly. However, investors' confidence faded in the following years when they found that many important reforms haven't been put into practice or if any, seriously lagged behind schedule. One remarkable example in this respect is the SOEs reform. Although the authorities quickly designated a number of SOEs to pilot different types of reforms in 2014, not much material progress has been made to date. Even worse is the deterioration in the debt level of SOEs over the past several years.

Meanwhile, some reform measures were deployed swiftly but have unintended effects. For example, the 2013 reform agenda devoted long lines to financial liberalization. Unfortunately, various liberalizing measures were implemented in an uncoordinated way and, as a result, increased the volatility of the financial market. Indeed, we have observed several rounds of market turmoil during the period of 2015-2016, including two stock market crashes in June-July 2015 and January 2016, the RMB devaluation in August 2015, and the bond market crunch in April 2016 etc.

To prevent these market turbulences from escalating to full-fledged systemic debacles, the authorities had to roll back some liberalizing measures. Now the authorities' inventions to the FX market become more frequent and the restrictions under capital account become tighter. All these run counter to the pledges the authorities made in their 2013 reform plan and have caused enormous confusion in the market. The Party's Congress provides a good opportunity for the authorities to review and revise its reform agenda and, more importantly, clearly communicate their ideas to the market. It remains to be seen what changes the authorities will bring to their original agenda and how they will adjust their implementation strategies according to implementation progress. It will be good news if the authorities reiterate their resolution to press ahead with SOE reforms and deploy new strategies to overcome the resistance of interest group. Meanwhile, the market will welcome the authorities' commitment to financial liberalization and their simultaneous efforts to build regulatory capacity to withstand associated risks.

4. Risks to the downside

Although the shift of the monetary stance and newly deployed regulatory efforts have somewhat slowed the momentum of shadow banking, the gigantic “stock” of these frailties still poses a material threat to the country’s financial stability. Domestically, risks from financial vulnerability still persist, mainly including debt overhang in the corporate sector and rampant shadow banking activities. On the other hand, the on-going deleveraging in the real economy and financial sector, with its original intention of mitigating the above risks, might drag on growth as well. Altogether, the authorities need to find a balance and choose an appropriate pace between pushing forward the deleveraging progress and maintaining a sustainable growth momentum.

Regarding the corporate debt problem, although the monetary prudence and supply-side reforms have helped to stabilize firms’ leverage, it is still not the time for investors to cheer for it. First, complacency could sow the seeds of failure. Some early success could make the authorities slow their pace and even avoid painful but necessary reforms. As such, the process of deleveraging and reforming SOEs could be adversely postponed. Second, if non-SOEs don’t have confidence in long-term growth prospect, the deleveraging process among non-SOEs could prompt them to increase their cash hoarding while avoid making new investments. As such, the economy could fall in a trap of “balance sheet recession”, in which even firms with good profitability decline to expand their production capacity while use their proceeds to pay off their debt. Collectively, such behaviours could lead to diminished investment demand and years of economic sluggishness as we seen in the past two decades in Japan.

Meanwhile, external risks still abound. Rising geopolitical tensions in the Korean Peninsula have escalated and could have a noticeable effect on trade and investment flows in the East Asian region. In addition to undermining investor sentiment, in particular China’s Northeast region which is adjacent to the North Korea and has been under several years of economic downturn, the standoff could give rise to further military buildups that could divert fiscal spending from more productive investments.

The still buoyant external demand is also subject to headwinds from rising populism and protectionism globally. The latest example is that the Office of the U.S. Trade Representative (USTR) formally initiated a Section 301 investigation into China’s intellectual property practices in August. If the investigation is warranted and finds that China’s trade policies have harmed U.S. interests, President Donald Trump can apply punitive measures on China’s exports, as a consequence, could derail the country’s growth recovery.

IMPORTANT DISCLOSURES

The BBVA Group companies that have participated in preparing or contributed information, opinions, estimates, forecasts or recommendations to this report are identified by the location(s) of the author(s) listed on the first page as follows: 1) Madrid, London or Europe = Banco Bilbao Vizcaya Argentaria, S.A., including its E.U. branches (hereinafter called 'BBVA'); 2) Mexico City = BBVA Bancomer, S.A. Institución de Banca Múltiple, Grupo Financiero BBVA Bancomer (hereinafter called 'BBVA Bancomer'); 3) New York = BBVA Securities, Inc. (hereinafter called "BBVA Securities"); 4.) New York Branch = BBVA, New York branch; 5.) Lima = BBVA Continental; 6.) Bogota = BBVA Colombia S.A.; 7.) Santiago = BBVA Chile S.A.; 8.) Hong Kong = BBVA, Hong Kong branch, 9.) Istanbul = Garanti Securities.

For recipients in the European Union, this document is distributed by BBVA, a bank supervised by Banco de España and by Spain's Stock Exchange Commission (CNMV), and registered with Banco de España with number 0182.

For recipients in Hong Kong, this document is distributed by BBVA, which Hong Kong branch is supervised by the Hong Kong Monetary Authority.

For recipients in Mexico, this document is distributed by BBVA Bancomer, a bank supervised by the Comisión Nacional Bancaria y de Valores (Mexico's SEC).

For recipients in Peru, this document is distributed by BBVA Continental, a bank supervised by the Superintendencia de Banca, Seguros y Administradoras Privadas de Fondos de Pensiones.

For recipients in Singapore, this document is distributed by BBVA, which Singapore branch is supervised by the Monetary Authority of Singapore.

For recipients in the USA, research on products other than swaps, or equity securities and equity derivatives prepared by BBVA, is distributed by BBVA Securities, a subsidiary of BBVA registered with and supervised by the U.S. Securities and Exchange Commission and a member of the Financial Industry Regulatory Authority ("FINRA") and the Securities Investor Protection Corporation. U.S. persons wishing to execute any transactions should do so only by contacting a representative of BBVA Securities in the U.S. Unless local regulations provide otherwise, non-U.S. persons should contact and execute transactions through a BBVA branch or affiliate in their home jurisdiction.

Research on swaps is distributed by BBVA, a swaps dealer registered with and supervised by the Commodity Futures Trading Commission ("CFTC"). U.S. persons wishing to execute any transactions should do so only by contacting a representative of BBVA. Unless local regulations provide otherwise, non-U.S. persons should contact and execute transactions through a BBVA branch or affiliate in their home jurisdiction.

Research prepared by BBVA on equity securities and equity derivatives is distributed by BBVA to "major U.S. institutional investors" based on an exemption from registration provided by Rule 15a-6 of the U.S. Securities Exchange Act of 1934, as amended (the "Exchange Act"). BBVA is not a registered broker-dealer in the United States and is not subject to U.S. rules on preparing research or independence of research analysts.

BBVA and BBVA Group companies or affiliates (art. 42 of the Royal Decree of 22 August 1885 Code of Commerce), are subject to the BBVA Group Policy on Conduct for Security Market Operations which establishes common standards for activity in these entities' markets, but also specifically for analysis and analysts. This BBVA policy is available for reference on the following website: www.bbva.com.

Analysts residing outside the U.S. who have contributed to this report may not be registered with or qualified as research analysts by FINRA or the New York Stock Exchange and may not be considered "associated persons" of BBVA Securities (as such term is construed by the rules of FINRA). As such, they may not be subject to FINRA Rule 2241 or 2242 restrictions on communications with subject companies, public appearances and trading of securities held in research analysts' accounts.

BBVA is subject to Internal Standards of Conduct on the Security Markets, which detail the standards of the above-mentioned overall policy for the EU. Among other regulations, they include rules to prevent and avoid conflicts of interests with the ratings given, including information barriers. These Internal Standards of Conduct on the Security Markets are available for reference in the 'Corporate Governance' section of the following website: www.bbva.com.

BBVA Bancomer is subject to a Code of Conduct and to Internal Standards of Conduct for Security Market Operations, which details the standards of the above-mentioned overall policy for Mexico. Among other regulations, it includes rules to prevent and avoid conflicts of interests with the ratings given, including information barriers. This Code and the Internal Standards are available for reference in the 'Grupo BBVA Bancomer' subsection of the 'Conócenos' menu of the following website: www.bancomer.com.

BBVA Continental is subject to a Code of Conduct and to a Code of Ethics for Security Market Operations, which details the standards of the above-mentioned overall policy for Peru. Among other regulations, it includes rules to prevent and avoid conflicts of interests with the ratings given, including information barriers. Both Codes are available for reference in the 'Nuestro Banco' menu of the following website: https://www.bbvacontinental.pe/meta/conoce-bbva/.

BBVA Securities is subject to a Capital Markets Code of Conduct, which details the standards of the above-mentioned overall policy for USA. Among other regulations, it includes rules to prevent and avoid conflicts of interests with the ratings given, including information barriers.

Exclusively for Recipients Resident in Mexico

BBVA Bancomer acts as a market maker/specialist in: MexDer Future Contracts (US dollar [DEUA], 28-day TIIEs [TE28], TIIE Swaps, 91-day CETES [CE91]), Bonos M, Bonos M3, Bonos M10, BMV Price and Quotations Index (IPC), Options Contracts (IPC, shares in América Móvil, Cemex, CPO, Femsa UBD, Gcarso A1, Telmex L) and Udibonos.

BBVA Bancomer, and, as applicable, its affiliates within BBVA Bancomer Financial Group, may hold from time to time investments in the securities or derivative financial instruments with underlying securities covered in this report, which represent 10% or more of its securities or investment portfolio, or 10% or more of the issue or underlying of the securities covered.

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.

BBVA | Research

This report has been produced by the China Unit

Chief Economist for USA
Le Xia
Xia.le@bbva.com.hk

Betty Huang
betty.huang@bbva.com.hk

Jinyue Dong
jinyue.dong@bbva.com.hk

Sumedh Deorukhkar
sumedh.deorukhkar@bbva.com

BBVA Research

Group Chief Economist
Jorge Sicilia Serrano

Macroeconomic Analysis
Rafael Doménech
r.domenech@bbva.com

Global Macroeconomic Scenarios
Miguel Jiménez
mjimenezg@bbva.com

Global Financial Markets
Sonsoles Castillo
s.castillo@bbva.com

Global Modelling & Long Term Analysis
Julián Cubero
juan.cubero@bbva.com

Innovation & Processes
Oscar de las Peñas
oscar.delaspenas@bbva.com

Financial Systems & Regulation
Santiago Fernández de Lis
sfernandezdelis@bbva.com

Countries Coordination
Olga Cerqueira
olga.gouveia@bbva.com

Digital Regulation
Álvaro Martín
alvaro.martin@bbva.com

Regulation
María Abascal
maria.abascal@bbva.com

Financial Systems
Ana Rubio
arubiog@bbva.com

Financial Inclusion
David Tuesta
david.tuesta@bbva.com

Spain & Portugal
Miguel Cardoso
miguel.cardoso@bbva.com

United States of America
Nathaniel Karp
Nathaniel.Karp@bbva.com

Mexico
Carlos Serrano
carlos.serranoh@bbva.com

Turkey, China & Geopolitics
Álvaro Ortiz
alvaro.ortiz@bbva.com

Turkey
Álvaro Ortiz
alvaro.ortiz@bbva.com

China
Le Xia
le.xia@bbva.com

South America
Juan Manuel Ruiz
juan.ruiz@bbva.com

Argentina
Gloria Sorensen
gsorensen@bbva.com

Chile
Jorge Selaive
jselaive@bbva.com

Colombia
Juana Téllez
juana.tellez@bbva.com

Peru
Hugo Perea
hperea@bbva.com

Venezuela
Julio Pineda
juliocesar.pineda@bbva.com

FOR ANY QUERIES< PLEASE APPLY TO: BBVA Research: Calle Azul, 4. Edificio de la Vela - 4ª y 5ª plantas. 28050 Madrid, Spain. Tel.+34 91 374 60 00 and +34 91 537 70 00 / Fax+34 91 374 30 25 - bbvaresearch@bbva.com www.bbvaresearch.com