China: Soft-Landing of a Cat?

1. IP, and even a wider gauge of activity that includes freight, credit as well as power and auto and production square with weaker GDP (% YoY, Quarterly)

2. Sharp plunge in real estate investments was a key driver of China’s growth headwinds; the surprise is that growth did not fall more.

3. Whereas Services is now picking up the slack in manufacturing industries hit by overcapacity issues (%-points; YoY)

4. China property sales picking up will help revive investments back-stopping wider growth and stabilizing commodities

“Well! I’ve often seen a cat without a grin,’ thought Alice ‘but a grin without a cat! It’s the most curious thing I ever saw in my life – Lewis Carroll, Alice in Wonderland
• **Q3 GDP data were grim** on the account of deceleration to 6.9% from 7.0% in Q2. And that it dragged year-to-date growth below “official” 7% target added insult to injury.

• **But** everything, including data pessimism, is relative. And given **expectations of sharper drop to 6.8% (and fearing worse), gentle easing to 6.9% was welcome relief instead.**

• So much so, that there is even a sense of **bottoming in China’s growth beginning to percolate** (albeit very slowly). That is **worthy of a (relieved) grin** perhaps.

• “Alice” got it right in that a **grin (China bottoming) is a curious notion in the absence of a cat (discernible pick-up in industrial or investment activity).**

• To be sure, **industrial activity indicators were almost ubiquitously pointing to much more bearish outcome for growth** (Chart 1); even if we used wider indicators that included autos, electricity, freight and credit (Chart 2).

• And arguably, the curious “grin without a cat” is most acute in **unrelentingly steep slump in real estate fixed asset investments**, confounding relatively steady growth (Chart 3).

• A likely reason is that **China’s economy is now a lot more service-centric** than it was in the past, and so **the correlation with “hard” industrial activity is less pronounced.**

• Especially as **industrial overcapacity comes home to roost, industrial activity tends to overstate weakness** (just as strength used to be overstated in the past).

• Whereas, services now account for a larger share of China’s economy that has gradually diversified and restructured, mitigating industrial weakness (Chart 4).

• Crucially, **if nascent recovery in property market transactions is sustained uninterrupted** (Chart 5), conviction about China’s bottoming will grow.

• In particular, if followed by **substantial lift in real estate investments** (albeit with a lag) given that **China’s economy is still predominantly investment-driven.**

• What’s more, **property transactions will provide wider boost to ancillary activity and services**, providing follow-through and broader economic momentum.

• **Upshot:** The “grin” may not be illusory if nascent inflections in China begin to harden, and the cat’s outline becomes more apparent.
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