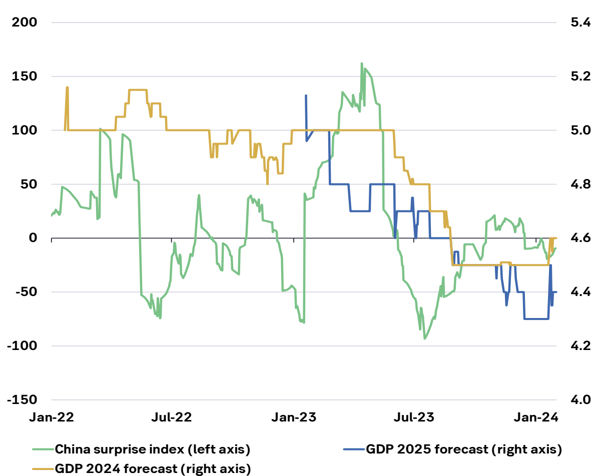
Theme: China
A focus on “modern industrial systems”

Building “modern industrial systems” is now a top priority for policymakers in Beijing, and they have increased their policy focus on ensuring reasonable economic growth in 2024. China faces an economic landscape that is affected by everything from challenges in the real estate sector to the surprising renaissance of the automotive industry.

Beijing has increased its policy focus on ensuring reasonable economic growth in 2024

Favourable base effects pushed 2023 growth above the official target of “about 5 per cent”. With fading base effects, Chinese officials need to ramp up fiscal support in order to reach reasonable growth this year. We expect GDP to rise by 4.6 per cent, even as the real estate sector contracts for another year. But the renaissance of the automotive sector, along with the growth of other priority sectors, should still provide some positive surprises to growth. Despite some stabilisation in activity in the certain sectors, analysts remain wary about bumping up forecasts for this year. Beijing will not release official economic targets until March.

2024 GDP forecasts have not yet improved



Source: Bloomberg, SEB

The policy pendulum is swinging in favour of growth

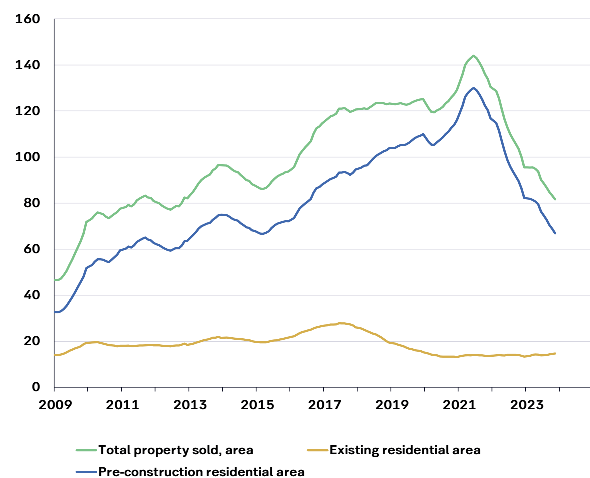
In mid-December 2023 the Central Economic Work Conference (CEWC) – the yearly meeting that sets the country’s economic agenda for the following year – even indicated that non-economic policies will be incorporated into the assessment of macro policy consistency. Simply put, officials across the various centres of power will be held accountable to ensure that overall policies will not have a negative impact on growth.

Beijing is now ready to shoulder some of the fiscal responsibility

For a long time, local governments have been tasked to deliver on growth-boosting projects. Yet with subdued revenues and the pressure to re-absorb off balance sheet debt issued by local government financing vehicles (LGFVs), local authorities have had little room to pursue public sector investments. As a result, growth in infrastructure spending was weak at less than 6 per cent. In October 2023, the central government issued a supplementary budget of around 0.8 per cent of GDP. The proceeds of the additional funding were allocated to local governments, keeping the momentum of activity up through Q1 2024.

The release of economic targets in March will include bond quotas for both central and local governments. Because the central government partially front-loaded its deficit spending in 2023, there is only room for Beijing to announce a small bump in the planned deficit for 2024. Meanwhile, if China were to target GDP growth above 4.8 per cent, then the bond quotas for the local governments would need to be increased substantially. In any case, fiscal policy will keep bond supply elevated through the year. To limit volatility in onshore interest rates, we expect the central bank to raise liquidity injections and maintain an easing bias.

Property sales have fallen to 2013 levels



Source: Bloomberg, SEB

The real estate sector will continue to contract in 2024

Since real estate sales started to decline in late 2021, more than 50 per cent of listed developers have either defaulted or restructured their public bonds. Those refinancing challenges of the developers were exacerbated by a loss of confidence from homebuyers. At the peak of the real estate cycle, more than 90 per cent of all transactions in China were pre-construction sales. By the time the property is completed, homebuyers would have already paid more than 50 per cent of the value of their property. Meanwhile, pre-construction revenues make up a large percentage of funding for the developers. Despite numerous policy adjustments designed to boost demand for new homes, households remain wary of the remaining real estate developers. As a result, pre-construction sales have now collapsed to levels last seen in 2013. As long as households doubt the ability of developers to complete outstanding projects, pre-construction sales will probably continue to decline. With tight funding capabilities, developers will have a limited project pipeline, possibly through 2025. Overall, this will remain a dampener on construction activity.

The outlook for priority sectors remains optimistic

Beijing has elevated industrial policy to its top priority for this year. This is in contrast to 2023, when its priority was to ensure the recovery of domestic consumption. "Building modern industrial systems" is now top of mind for policymakers. The development of high-tech manufacturing has been a sectoral priority for years. It is not a surprise that even with weak infrastructure spending, investments in priority manufacturing sectors rose at a double-digit pace in 2023. At the heart of China's industrial policy is boosting capabilities in the automotive sector, battery manufacturing, the green energy transition and the health sector. In light of the ageing population, Beijing has been raising investments in goods and services that will benefit the senior population. Building on these capabilities will likely continue in 2024.

The renaissance of the automotive sector goes beyond electric vehicles

The electrification of the domestic auto market has come in faster than even the government's target. By end-2023, new electric vehicles (NEVs) made up more than 32 per cent of new car sales. The uptake in tier-one cities may have already reached more than half of sales. With continued investment in charging infrastructure throughout the country, sales of NEVs will likely continue to surge. As a result, a Chinese EV manufacturer is now the top-selling car brand in China, a designation long-held by a German brand. The industrial policy that has long focused on building NEV capabilities has widened the gap between Chinese NEV technology and traditional European brands. The taste of Chinese consumers has also shifted in favour of smart vehicles.

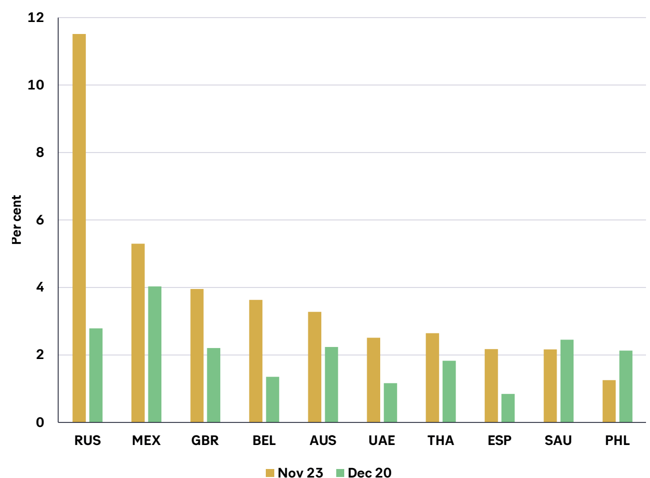
Meanwhile, sales of internal combustion engine (ICE) vehicles have also turned positive

After years of contracting volumes, ICE car sales grew almost 9 per cent in 2023, pushing up overall sales for the year. Yet, even with strong sales volumes, overcapacity in the domestic market has intensified pressure to cut prices. With more than 100 car brands in China, this aggressive price war has squeezed corporate margins throughout the automotive sector supply chain. Already, more than half of car brands are not profitable. It is expected that most home-grown brands will not survive as industrial subsidies fade.

The export market provides another tailwind to the auto sector

Auto exports rose around 30 per cent in 2023. Since the war in Ukraine began, Russia has emerged as the top market for Chinese-made vehicles. While it is likely that most exports to Europe are electric vehicles, the diversified export market suggests that there is also demand for Chinese petrol-powered cars. Although it is still uncertain whether the European Union will impose trade restrictions on Chinese-made EVs, there are other markets where automakers can still expand their presence, like ASEAN, Latin America, the Middle East and Africa.

China is exporting cars to a diversified basket of economies



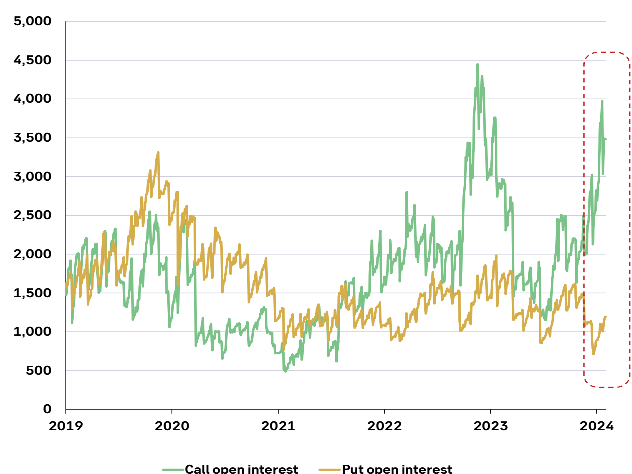
Source: CEIC, SEB

Despite persistently weak sentiment, the stock market must prepare for upside growth surprises

After three years of disappointing equity market performance, the market is cautious about yet another sombre year. Large-cap ETFs have already lost around 10 per cent in the first weeks of 2024. Yet option traders are ramping up positions that will take advantage of a possible turnaround in Chinese equities.

Read more about our thoughts on China and its stock market in the global equities section, starting on page 10.

Option traders are preparing for upside gains in stocks



Source: Bloomberg, SEB