CDI-NERI MACRO OUTLOOK

August 2016

Why the IMF Raised Its Growth Outlook

The IMF in June raised its 2016 growth outlook for China to 6.6%, a 0.1 pp uptick from its April projection, even though Brexit prompted the Fund to slice its global growth forecast for 2016 by 0.1 pp, to 3.1%.

The growth upgrade for China shows that the IMF is optimistic about the major reforms underway in China. The Fund's outlook is consistent with our forecast, as China still has plenty of room to lift its fixed asset investment and current structural reforms, including by deleveraging and cutting excessive capacity, which should generate sustainable growth. Other common media concerns, such as the increase in non-performing loans, the increase of government and household debt and yuan instability, are all mentioned. The Fund also notes that the Chinese government is fully aware of the problems, and is taking action to deal with them.

The bad news is that Chinese fixed asset investment was up just 3.9% y/y in real terms in July, down a significant 4.3 pps from Q2. We expect state investment to increase to counteract this declining trend, and to address the slowdown in private investment, since state investment complements private sector investment.

Industrial output was up 6% y/y, in a slight slowdown from Q2. Production and sales of automobile surged in Q2, by about 17%. Retail sales of consumer goods rose 10.2% y/y in nominal terms in July, flat on Q2. Exports fell -4.4% y/y, while imports fell -12.5% y/y, down 5.7 pps.

CPI rose 1.8% y/y, down for three consecutive months, and down 0.5 pps from April. Producer prices continue to recover. The ex-factory price index of industrial products fell -1.7% y/y, and PPI fell -2.6% y/y, down 0.9 and 0.8 pps from June.

Financial and monetary indicators showed divergent trends in July. M1 increased 25.4% y/y, up 0.8 pps from June, and up a significant 18.8 pps from July 2015. But other financial indicators failed to perform well. M2 rose 10.2% y/y, down 1.6 pps from June, and down 3.1 pps from 2015. Loans from financial institutions rose 12.9% y/y, down 1.4 pps from June, to their lowest level since 2006. The main reason behind this divergence is the inconsistency of monetary policy.