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Flash Notes

China: 4Q11 Growth Tracking Above Expectations

China's 4Q11 GDP report this morning (17 Jan) showed continuation of deceleration in headline figure, but came in above expectations. **Headline came in at 8.9%y/y, from 9.1%y/y in 3Q11, above both consensus of 8.7% and our view of 8.5%. However, the pace in 4Q11 is the weakest in 2 ½ years, tracing back to near 2009** lows in the aftermath of the Global Financial Crisis. For the full year, China's economy expanded 9.2% in 2011, from a revised 10.4% in 2010. On a q/q basis, activities in 4Q11 slowed slightly to 2.0% pace seasonally adjusted, down from 2.3%q/q in 3Q11. At 8.2% annualized for 4Q11, it would be more reflective of actual momentum than the reported above-9% figure for the full year, meaning that growth pace is actually far slower than indicated by the y/y numbers.

The surprisingly strong 4Q11 headline was partly boosted by the above-consensus December industrial production, which expanded 12.8%y/y vs. 12.4% in Nov, as well as the weaker than expected imports in the month. Retail sales also turned out to be robust rising 18.1%y/y in Dec, breaking above the normal staid pace of 17% and the fastest in nearly a year. Other key data released earlier are consistent with activities moderating but far from a "crash landing" situation. In particular, M2 growth rebounded in Dec at 13.6%y/y, ending a five consecutive months of decline. New RMB loans also rose faster than expected in Dec, adding RMB640.5bn of new loans, vs. RMB562.2bn of new loans in Nov, as banks appeared to have loosened up after Premier Wen Jiabao made a visit to Wenzhou and other places to look into SMEs' credit woes. For the year, China's banking system added a total of RMB7.5tn new loans, lower than the nearly RMB8tn pace seen in 2010 and RMB9.6tn in 2009. Note that investment activities have slowed in 2011 as a natural outcome of tighter policy, with urban fixed asset investments (FAI) rising 23.8% for the year, from 24.5% in 2010 and the slowest annual pace since the 17.4% rate recorded at end-2002.

While 4Q11 turned out to be surprisingly strong, we nonetheless expect moderation momentum to continue in the first half of 2012, as both domestic and external headwinds gather. At the same time, PBoC is even more reluctant to ease aggressively with such positive headlines. **For now, we look for headline GDP growth figures dipping below 8% in 1Q12-2Q12, and then rebounding in the second half. A "soft landing" scenario is the more likely outcome** in the current period of property price declines, which means a relatively low probability for the "hard landing" case (approximated by headline quarterly growth figures in the 5% range). Both PMI series show that the extent of moderation is still manageable at this point, though outlook ahead is likely to be downward biased given the uncertainty in Eurozone sovereign debt front as well as domestic difficulties in property sector and various debt problems. Taking all these into account, we maintain our full year 2012 growth projection at 8%.

China: NBS PMI vs HSBC PMI

Source: CEIC, UOB Economic-Treasury Research Estimates

The surprise reserve requirement ratio (RRR) cut announced at end-Nov suggests PBoC is taking its first step towards policy easing. With difficulties faced by SMEs in getting bank credit and further weakness in property prices, **we look for PBoC to loosen its grip gradually, which could see the central bank lowering RRR four more times by the first half of this year. However, interest rate cuts will be less likely at this point as inflation is still a top policy priority** and there is also wariness of fanning property prices. As such, the central bank would probably take to the interest rate cut route only in a later stage as growth momentum slows or upon some critical event. In all, we look for 2 cuts of interest rates (25bps each) sometime in the next two quarters (current level: 6.56% for 1Y lending and 3.50% for 1Y deposit).

Recent trading shows that RMB currency is also exposed to the risk aversion trade in both onshore and offshore. While there has been a reversal since early 2012 in the offshore trading with CNH strengthening above CNY, the average gap of about 40pips so far has yet to revert to the average spread of 100pips during Jan-Sep 2011. In onshore trading, RMB remains on weak footing, having declined 0.3% against USD so far in 2012, with similar trend observed for the daily fixings. **This means that current market conditions appear to be still in risk aversion mode, and potentially negative for CNH. For 2012, we expect slower pace of appreciation for the RMB, in line with downbeat sentiment globally. We maintain our USD/RMB forecasts, with year-end projection at 6.15 vs. end-2011 close of 6.295**, with end-1Q12 projection at 6.27, vs. recent RMB trading of around 6.31 per USD.

China's Key Macro Data										
	2008	2009	2010	2011	3Q11			4Q11		
Real GDP Growth (% y/y)	9.6	9.2	10.4	9.2	9.1			8.9		
Real GDP Growth (% q/q SA)					2.3			2.0		
% y/y change	2008	2009	2010	2011	Jul-11	Aug-11	Sep-11	Oct-11	Nov-11	Dec-11
Industrial Output	12.9	11.0	15.7	13.9	14.0	13.5	13.8	13.2	12.4	12.8
CPI	5.9	-0.7	3.3	5.4	6.5	6.2	6.1	5.5	4.2	4.1
PPI	6.9	-5.4	5.5	6.1	7.5	7.3	6.5	5.0	2.7	1.7
Exports	17.3	-15.9	31.3	20.3	20.3	24.4	17.0	15.8	13.8	13.3
Imports	18.4	-11.3	38.9	24.9	23.0	30.4	21.1	29.1	22.6	12.1
Trade Balance (US$ bn)	297.3	198.2	184.5	$ 157.9	$ 31.5	$ 17.8	$ 14.5	$ 17.0	$ 14.5	$ 16.5
New Loans (RMB bn chg)	4,170.4	9,629.0	7,951.2	7,480.7	¥ 492.6	¥ 548.5	¥ 470.0	¥ 586.8	¥ 562.2	¥ 640.5
M2	17.8	27.7	19.7	13.6	14.7	13.6	13.0	12.9	12.7	13.6
Urban Fixed Asset Investment YTD	26.1	30.5	24.5	23.8	25.4	25.0	24.9	24.9	24.5	23.8
Retail Sales	21.6	15.5	18.4	17.1	17.2	17.0	17.7	17.2	17.3	18.1
Source: CEIC, National Bureau of Statistics; UOB Economics-Treasury Research estimates. All data for individual months except noted.										

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