

## China: GDP rebounds solidly but risks remain

The Chinese economy avoided recession in 2020 and continued to grow strongly in 4Q20. This upbeat growth trend should continue in 2021. Control of people-flows has started, so the risk of a widespread outbreak of Covid should be small. But the risk of a technology war between China and some economies remains if the US does not remove some measures



### China grew solidly

China's economy grew 2.3% in 2020, and 6.5%YoY in 4Q20. Fixed asset investment increased 2.9%, industrial production grew 2.8% but retail sales shrank 3.9% in 2020. The contraction in retail sales occurred mostly in 1H20, recovering quickly in 2H20 as consumers started cross-province travels from May. We believe that the economic recovery will continue for China.

When China can achieve a complete recovery is still an open question, even though GDP growth was positive for the year. Some GDP growth came from fiscal and monetary stimulus and without those stimuli, the economy would not have recovered at such a pace since external demand has been very weak.

## Not a full recovery yet even with big growth numbers in 1Q21

It is too early to conclude that this is a full recovery. External demand has not yet fully recovered. This is a big hurdle for a full recovery of China's industrial production, especially for smaller manufacturers. The pandemic has resulted in a pause in international travel. And with rapid increases in Covid cases in the US and Europe, industries related to exports will continue to be in a difficult situation.

Due to the negative base effects in 1Q20, we expect GDP growth to reach 12.0%YoY for 1Q21. Covid cases have returned (around 100 cases for Mainland China per day). But so far, domestic travel across only a few cities has been reduced. There is no full-scale lockdown in most locations in the country.

Even if people do not go back to their home towns during the Chinese New Year, the impact on consumption should be relatively small. In fact, people staying at their work locations will continue to consume during the Chinese New Year.

## Active fiscal stimulus but not monetary policy

We expect that fiscal stimulus will continue to help companies experiencing difficulties until steady external demand returns, which in turn will help avoid increases in unemployment.

Some of the fiscal stimuli will be allocated to strategic sectors, for example, technology R&D to fulfill self-sufficiency targets and green energy for achieving environmental sustainability targets.

Given this growth picture, we expect monetary policy will stay put, i.e. no change in 7D reverse repo, 1Y medium lending facility rate, 1Y and 5Y loan prime rate, and reserve requirement ratio.

## Political risks to continue in 2021

We expect the newly elected US government will continue most of the current policies on China, at least for the first quarter. That means tariffs and technology measures on China will still be in place.

The most positive development we can envisage is that tariffs could be reduced gradually over 2021 with no additional pressure on the technology side. It is difficult to conceive of a dramatic improvement in the US attitude towards China's technological advancement as that would require a change in the belief of the US general public that China uses US technology for China's own military, even if that may not actually be the case.

## Forecasts

From the above projection, we expect China's GDP will grow by 7% in 2021 given the low base in 1H20, and the expectation that vaccines could slow down the spread of Covid and therefore provide some chance of faster recovery in external demand, helping manufacturing and exports.

Exchange rate liberalisation will continue to be the main theme for USDCNY's movements. We expect USDCNY to reach 6.20 by the end of 2021.