China: Surprisingly restrained loan growth

Credit growth has been much lower than expected even though companies have continued to suffer damage from the Covid-19 outbreak. What's going on?

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Loan growth was very slow

Using data from aggregate finance, yuan loans drawn in China rose just CNY 720.2 billion in February, smaller than the CNY 764.1 billion seen in the same month last year. Even combining the first two months, loan growth was just CNY 4.21 trillion, CNY 118.3 billion lower than the same period of 2019. This looks strange as China needs more credit to buffer the economy amid the Covid-19 outbreak.

While aggregate finance growth was a mere CNY 855.4 billion in February, it does look bigger when we combine the first two months, coming in at CNY 5.92 trillion.

The main difference between growth in loans and aggregate finance is the high growth of government bond issuance (including sovereign, quasi-sovereign, local governments, and local government special bonds), which seemed to be front-loaded in January. Government bond issuance grew by CNY 943.7 billion, an increase of CNY 339.1 billion from the same period a year ago.

Fiscal stimulus more crucial to recovery than bank loans

The data tells us that the government believes the damage brought about by Covid-19 is better addressed by government finance, which means fiscal stimulus and tax and fee cuts. We expect fiscal stimulus to be around 4% of nominal GDP while tax and fees cuts should be around 2% to 2.5% of nominal GDP in 2020.

The role of bank loans to alleviate the damage from the coronavirus might be moderate. This is understandable as the government has been worried that banks may lend to borrowers who might seek to take advantage of volatile markets by leveraging low-interest borrowings and investments, potentially boosting speculative assets.

This also highlights that the government does not want low-cost lending to enter the property sector, be it property development or property investments.

The risk lies in stock collateral

Though the government can restrict bank lending, the growth of stock collateral continued to increase in January-February by CNY 105.8 billion, compared to an increase of CNY 40.8 billion year-on-year in 2019.

This shows that stockholders may either be leveraging existing stock to increase investments in asset markets, or they need cash for their companies' operating cash flows.

The number looks small but the stock market has been volatile due to flowing news of Covid-19. And this stock collateral could be problematic if stock prices fall.

Fiscal stimulus will support economic recovery

From this loan data, we see that fiscal stimulus and tax and fee cuts are considered to be the main channels of support to the economy.

Chairman Xi has already pushed to speed up 5G infrastructure in February. We believe that this is one of the sectors that is going to boost GDP growth in 2020.

Other sectors that have mentioned by the government include electric car charging stations, high-voltage electricity infrastructure, refining transportation networks, which include highways, railways and metro lines, and big-data centres.

With this fiscal stimuli and tax and fee cuts, in total around 6% to 6.5% of nominal GDP in 2020, we maintain our GDP forecast for 1Q20 at 4.4% and for 2020 at 5.2%.