

China: Retail sales strength enables PBoC pause

All three activity data releases were better than expectations, but the highlight for us was the strength of retail sales. This is even more notable during a period of strict people flow control during the Chinese New Year holidays. This better-than-expected news has enabled the PBoC to hold policy rates steady



China is still under a zero-Covid policy and consumption has been weak

Big surprise

Retail sales rose 6.7%YoY YTD in February, down from 12.5% in December. Industrial production increased 7.5%YoY YTD, down from 9.6% at the end of 2021, and fixed asset investment grew 12.2%YoY YTD, up from 4.9% at the end of last year.

Although fixed asset investment grew the fastest of these three measures of activity data, and beat 2021's growth number, this was not unexpected, because a portion of local government special bonds for infrastructure projects in 2022 was assigned before the end of 2021. Most of the growth came from investment in equipment, which highlights the importance of infrastructure projects.

Our highlight within this set of activity figures is the retail sales growth rate of 6.7%YoY YTD in

February. This was an excellent result given that strict people flow controls were imposed during the Chinese New Year to limit the spread of Covid during the Winter Olympics. Spending on gasoline increased, implying not only higher gasoline prices but also more people travelling by car, most likely on short trips for the holidays. This hints that the middle-income class has kept up its spending.

With only moderate growth in industrial production, faster growth in fixed-asset investment should help to fill in any gaps left by retail sales.

Good growth makes PBoC pause

Looking at all this activity data together, China's first two months of GDP should be better than previously expected. The GDP growth rate for the first two months of 2022 look as if it should be revised upward. This also makes it likely that the PBoC will hold the 1Y Medium Lending Facility rate steady at 2.85%.

But risks are piling up. Covid in Shenzhen has led to a lockdown of the city, probably for two weeks. This could affect port operations if Covid cases are found there. There is also some suspension of factory operations. But manufacturing output in Shenzhen is not the main activity of the city, which focuses more on technology services. Working from home should not affect productivity substantially.

The spread of Covid in the north of China could be more damaging, as this part of the country is more focused on heavy manufacturing.

We believe the PBoC will also monitor these risks to see if they need to provide extra help to SMEs, for example, through targeted RRR cuts.