Chinese slowdown opens door to stimulus

Chinese economic data

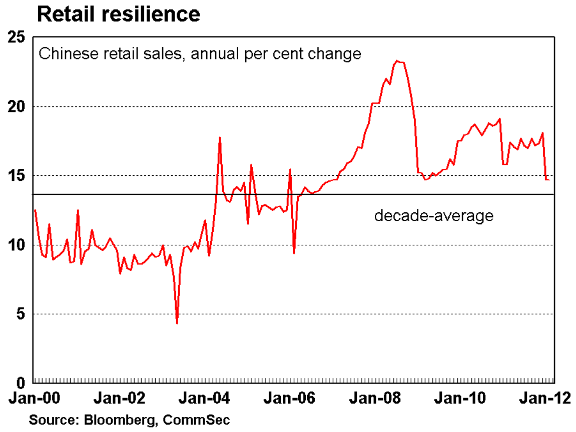
- **<u>Chinese economic data was generally weaker than expected</u>. Retail sales in January-February were up 14.7 per cent on a year ago (consensus 17.5 per cent); industrial production was up 11.4 per cent (consensus 12.3 per cent); but fixed asset investment In January and February was up by 21.5 per cent on year ago (consensus 20.0 per cent).**
- **<u>Scope to ease policy.</u> The slower pace of growth combined with other data showing that inflation is back in control gives the Chinese authorities scope to ease bank reserve requirements.**

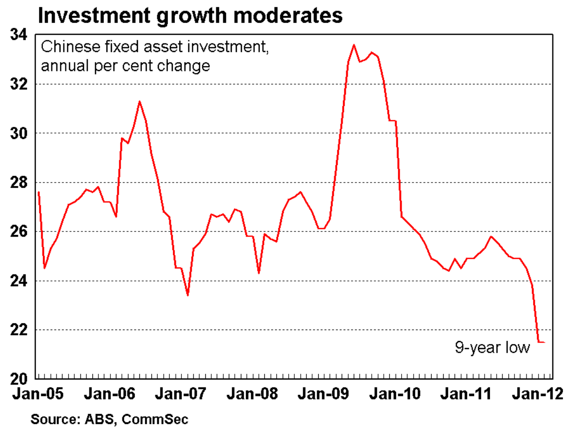
What does it all mean?

- Growth has slowed, but not stalled, and inflation has also eased. In short, Chinese authorities have successfully engineered a "soft landing" for their economy. There is now greater scope to ease monetary policy – largely a lowering of the required reserves that banks need to hold at the central bank.
- Chinese authorities are being careful not to crank up growth too quickly. But a staged lowering of reserve requirements would clearly be positive for Australian resources companies. Engineering a slowdown is a useful feat but the trick is not to let the downward momentum go too far.
- Other data out today showed that Chinese inflation has retraced to a near two-year low. Clearly the economy had to slow to a more sustainable pace and inflation had to come down, and the objectives have been achieved.
- The authorities must be careful to ease policy judiciously so that inflation stays low and economic growth lifts modestly to the required speed limit.
- The Aussie dollar held firm at US106.4 cents while the All Ordinaries lifted 38 points today. Clearly all the news has been good in the last 24 hours – favourable Chinese economic data and a successful Greek bond deal.

What do the figures show?

- **Industrial output** expanded at an 11.4 per cent annual pace in January-February, down from 12.8 per cent in December and below forecasts centred on a result near 12.3 per cent. Production is growing at the slowest pace in over 2½ years and is well off the highs of 20.7 per cent annual growth in January/February 2010.





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- China's **urban fixed asset investment**, such as spending on roads and power plants, grew at a 21.5 per cent in 2012 to date (January and February), modestly above forecasts (20.0 per cent) but down from 24.5 per cent in December. Investment growth is the slowest in over 9 years.
- **Retail sales** grew at a 14.7 per cent annual rate in February, down from 18.1 per cent in January and below forecasts, centred on 17.5 per cent annual growth. Most components slowed, especially home appliances, now 2.9 per cent down on a year ago. But telecom equipment is up 43.1 per cent on a year earlier.
- **Money supply (M2)** grew at a 13.0 per cent annual pace in February, up from 12.4 per cent in January and above market forecasts centred on growth of 12.8 per cent.
- **New yuan lending** was 710.7 billion yuan in February, below January's 738.1 billion and below forecasts of 750 billion yuan.
- **Outstanding loan growth** stood at a 15.2 per cent annualised rate in February, close to forecasts and up from 15 per cent in January.

What is the importance of the economic data?

- **China's National Bureau of Statistics** releases its monthly economic statistics around the middle of each month. Quarterly GDP data is released around the 16th of January, April, July and October. China is Australia's largest trading partner and changes in the Chinese economic have major implications for the Aussie economy.

What are the implications for interest rates and investors?

- China doesn't need to slow the economy further, rather it is more likely to stimulate activity. As such, for forward-looking investors, this is a positive situation.
- The Aussie dollar has potential to rise. However if the currency does lift and is not accompanied by higher commodity prices, then the Reserve Bank would view this negatively and lean in favour of further rate cuts.
- A stronger Aussie dollar would be negative for a raft of Australian industries including manufacturing, tourism and retailers.

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