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For Client Use

Macro Insight

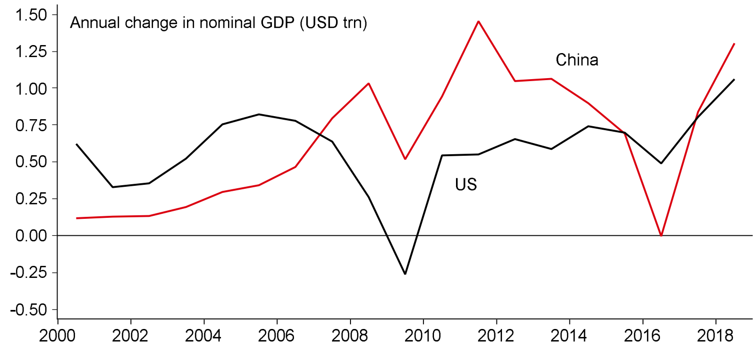
China's economy: taking the lead

China's economy is already larger than the US and adds more to global GDP

Measured in US dollars (USD), China's GDP accounted for around 15% of global GDP in 2018, notably lower than the US share of almost 25%. However, because China has a much lower general price level than the US, its "real" value is understated while the US's is overstated. Adjusting for this effect shows that China accounted for 19% of global GDP in 2018 versus 15% for the US.

Moreover, while China's pace of growth has, on average, slowed in recent years, it is still well above that of the US. This means that even when measured in "nominal" USD terms (i.e. not adjusted for price-level differences), China has typically contributed more than the US to the annual increase in global GDP since the global financial crisis (Figure 1).

Figure 1: China's GDP is rising more quickly than the US's in dollar terms



Source: Macrobond, OECD, HSBC Global Asset Management, data as of 20 November 2019.
Past performance is not a reliable indicator of future performance.

But it's not just China's scale that matters for the global economy and markets

It is not just the scale of the Chinese economy that matters when assessing how it influences the global economy and markets. Two further factors need to be considered.

1. China likely to be more cyclical than official data suggest

China's published real GDP data suggest that growth has exhibited significant stability around a gradually declining trend since 2012. This stability in real GDP is at odds with other Chinese data – such as energy use, nominal GDP and some surveys – as well as the cycles we see in other economies.

For example, since 2012, official Chinese GDP has deviated from its trend by less than 0.5ppt in any given year, contrasting with US growth which has deviated by 1ppt or more on a number of occasions (Figure 2). It is therefore possible that China's economic cycle is more pronounced than often assumed and its contribution to global growth more variable.

Our views

We see the outlook for Chinese and global growth as consistent with a "pro-risk, but conservative" investment strategy

Energy use, nominal GDP and surveys suggest China's economy is more cyclical than believed

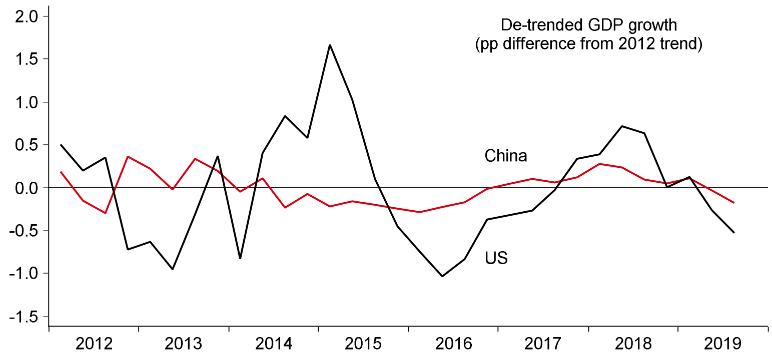
2. The economy has become more domestically driven

The structure of the Chinese economy is also changing. China's growth was export-driven from the mid-1990s until the financial crisis. In recent years this has changed as the share of exports to GDP has fallen from over 30% a decade ago to around 20% in 2018, while the trade surplus has fallen below 1% of GDP - its lowest since 1993.

Furthermore, since 2012, we have seen China's import growth leading its export growth (Figure 3), suggesting China's domestic demand has a large impact on the global cycle by stimulating activity and demand in other regions.

Whichever way one looks at it, China is now very much a second engine of global growth; it leads the global economy, not lags it.

Figure 2: Is China's cycle under-recorded?



Source: Macrobond, HSBC Global Asset Management, data as of 20 November 2019.
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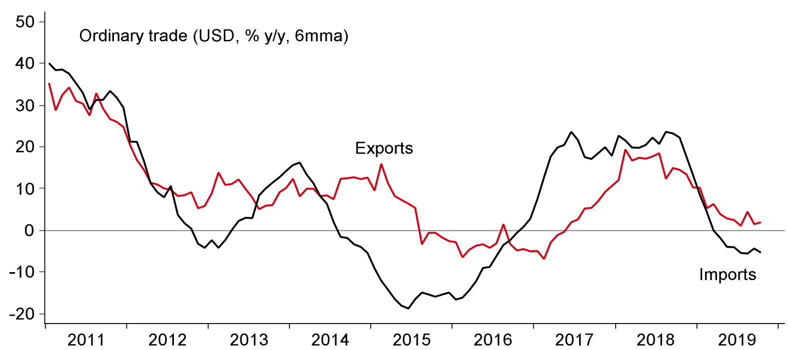
And China has shifted to an economy driven by domestic demand

Understanding the recent cycle

The above analysis is important in understanding the recent Chinese and global cycles. Because the slowdown seen in China since early 2018 coincided with an increase in trade tensions with the US, it is tempting to infer this is the main cause of the weakening. However, China's trade data show that in the upswing from late 2016 to 2018, import growth picked up well in advance of its exports and in the subsequent downswing import growth slowed much more abruptly than export growth (Figure 3). This suggests domestic factors have been more important in driving China's recent cycle.

Figure 3: China's imports have led its exports in recent years



Source: Macrobond, HSBC Global Asset Management, data as of 20 November 2019.
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Ultimately, the strong pick-up in imports (and implicitly domestic demand) from late 2016 through 2017 appears to reflect the lagged impact of a loosening in credit conditions.

China's import cycle leads activity in the rest of the world and is influenced by policy

Likewise, the sharp slowdown in domestic demand that began in the second half of 2018 followed a clampdown on credit during 2017, particularly in the shadow banking sector.

Importantly, with the Chinese authorities easing policy over the past year, credit dynamics improved markedly in the first half of 2019. While imports are still falling in year-on-year terms, this reflects a sharp adjustment at the end of 2018; imports have been trending up from early this year, consistent with more stable domestic conditions. Credit growth needs to be watched closely however, as there are signs that it has lost some momentum in recent months.

Market considerations

China plays a central role in the global economic cycle. After slowing notably in 2018 we have seen greater stability in China's growth this year and we expect this trend to be maintained. However, if economic data were to soften, the authorities are likely to ease policy further to sustain growth, thereby limiting the chances of a renewed slowdown. Supported by our valuation estimates, we see the outlook for Chinese and global growth as consistent with a "pro-risk" investment strategy in our multi-asset portfolios, although elevated political uncertainty justifies a degree of caution.

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