



PANTHEONTM
MACROECONOMICS

INDEPENDENT • INCISIVE • ILLUMINATING

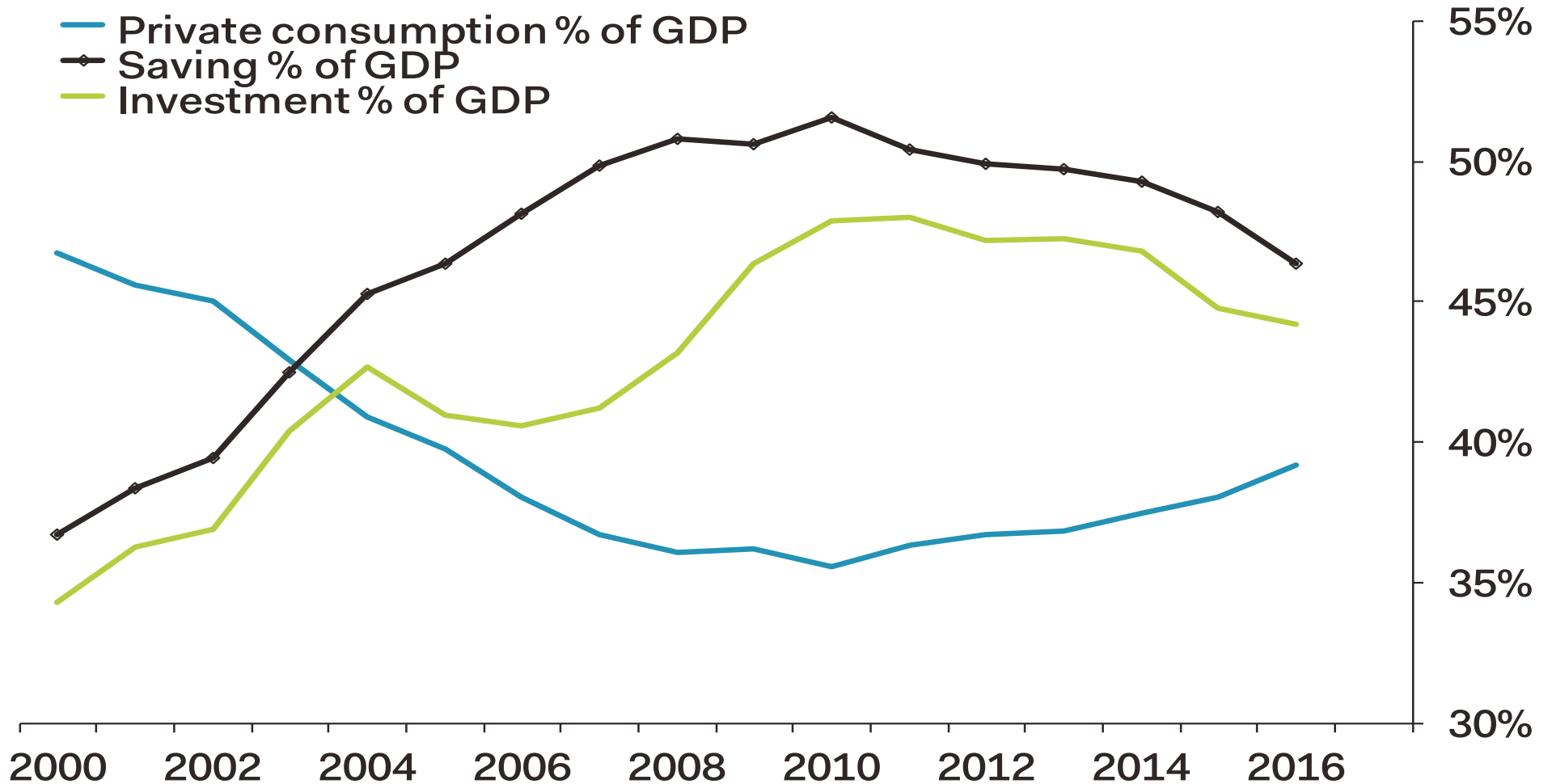
THE BIG PICTURE ON SINO-U.S. TRADE WARS... ...THE IMMEDIATE THREAT AND THE MEDIUM-TERM RISKS

ASIA WEBINAR CHARTBOOK, OCTOBER 2018

DATA AS AT OCTOBER 3 | FREYA BEAMISH, CHIEF ASIA ECONOMIST
WWW.PANTHEONMACRO.COM | +44 191 249 9209



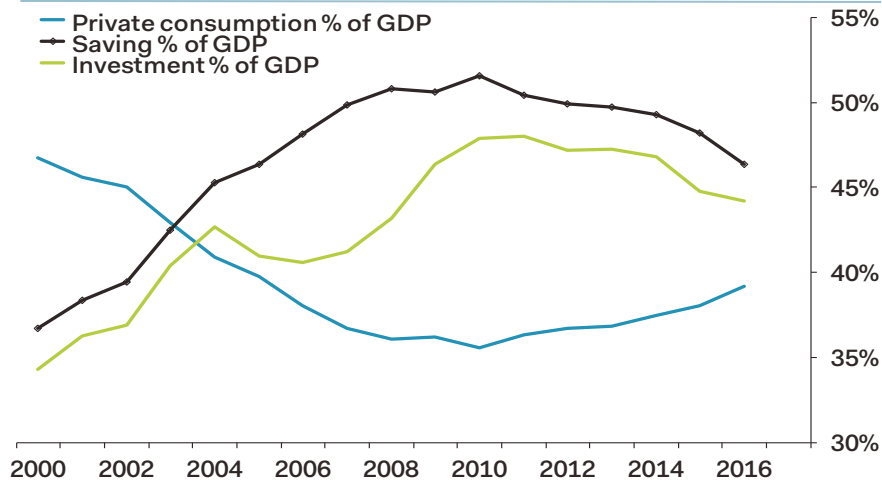
1. EXCESS SAVING HAS DIMINISHED IN CHINA IN RECENT YEARS, BUT REMAINS SUBSTANTIAL





- **External**

2. WHAT TO DO WITH EXCESS SAVINGS?

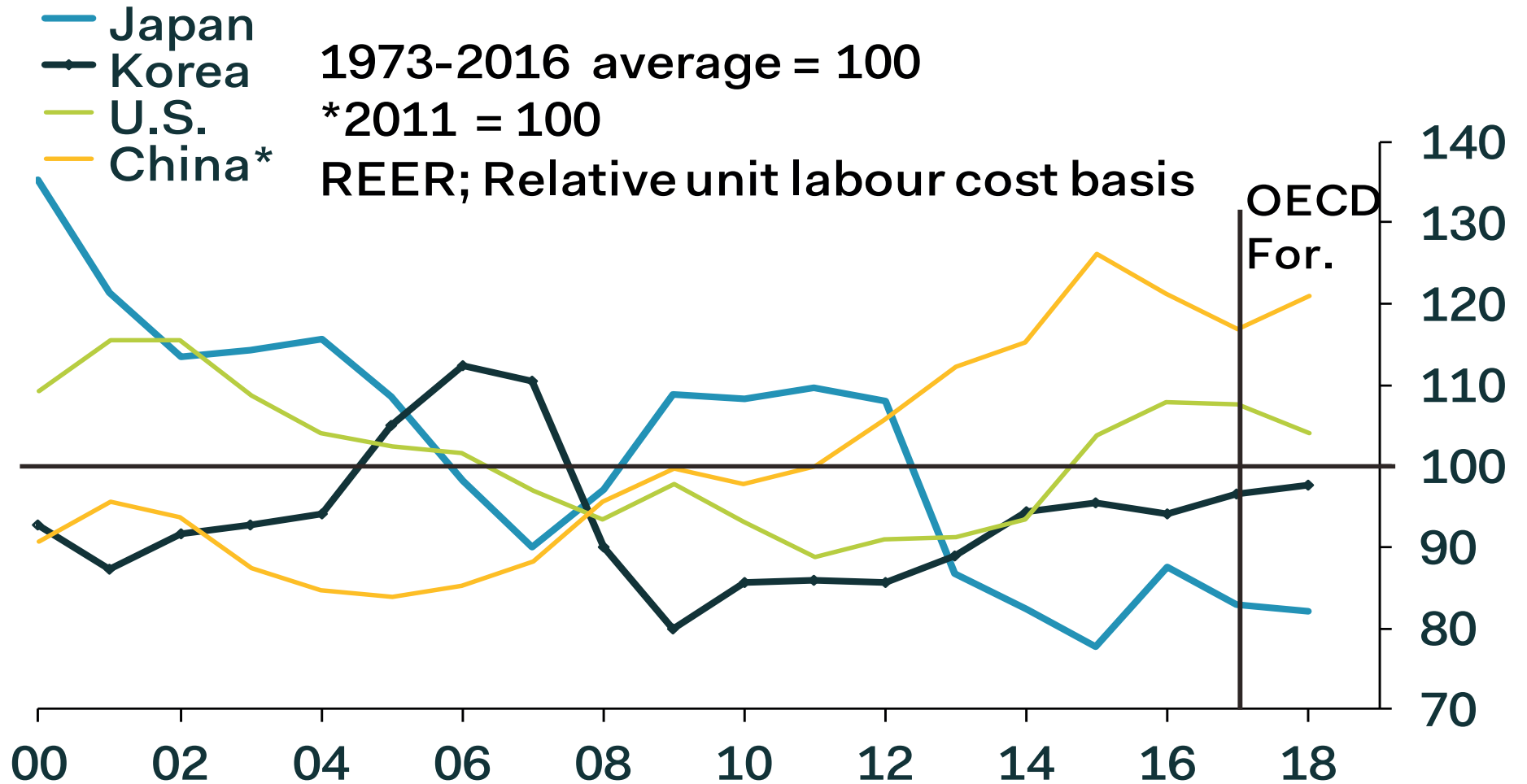


- **Internal**

- **Businesses**
- **Households**
- **Government**

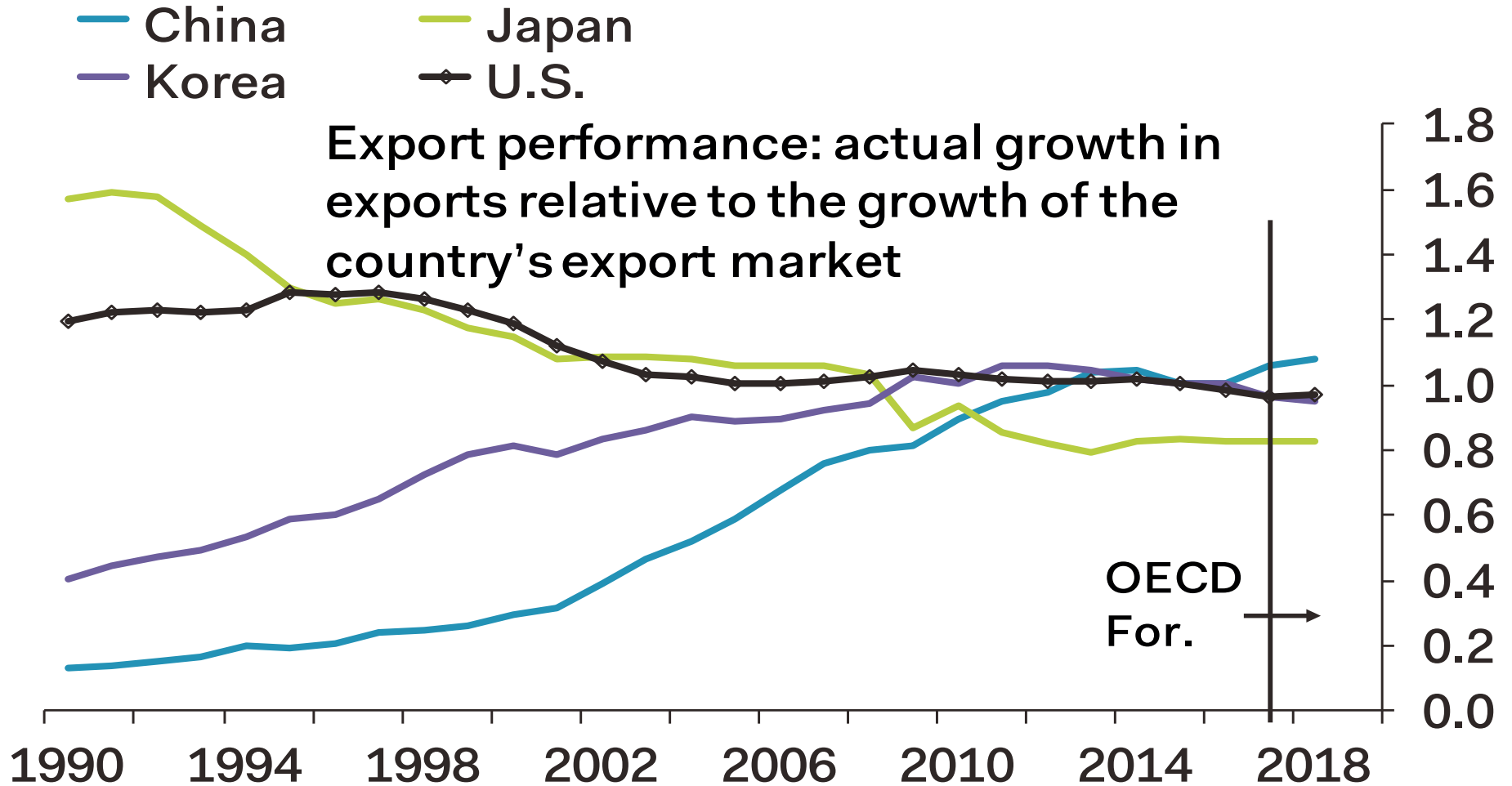


3. RMB OVERVALUATION HAS FORCED THE BURDEN OF EXCESS SAVING BACK ONTO CHINA



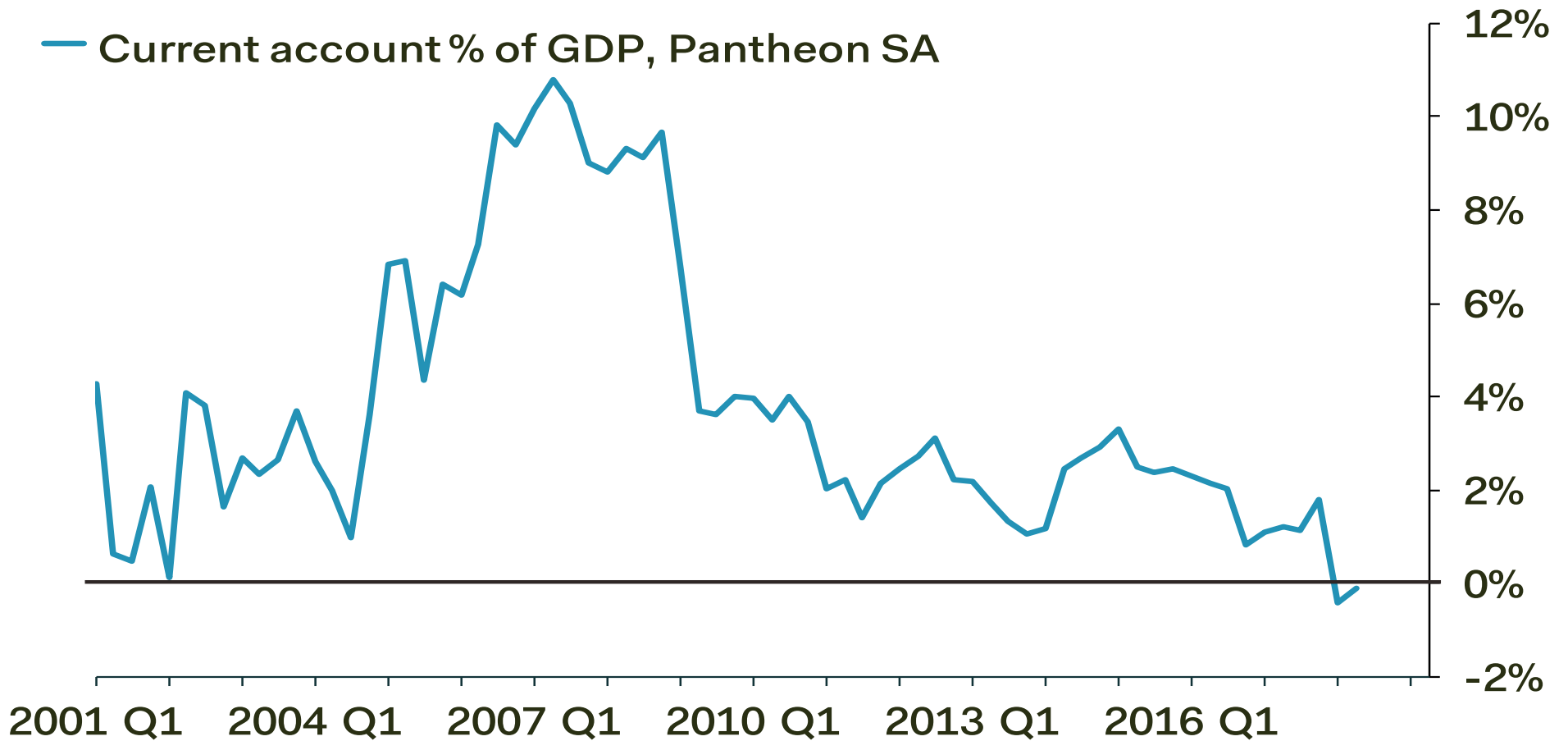


4. CHINA HAS BEEN LESS ABLE TO EXPORT ITS SURPLUSES





5. THE CURRENT ACCOUNT SURPLUS IS GONE, BUT THAT DOESN'T MEAN EXCESS SAVINGS ARE

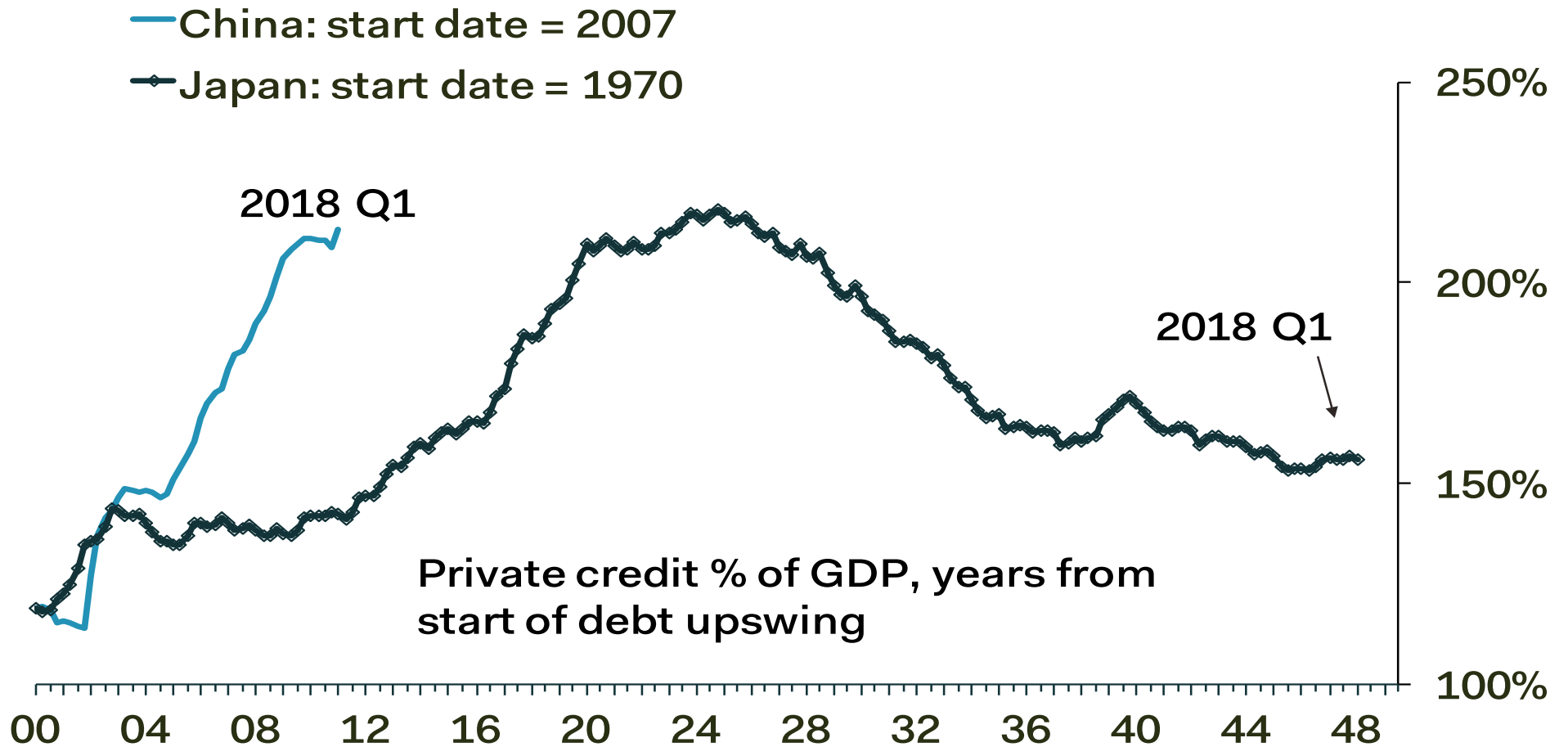




- **Bearing the burden of excess savings internally**
 - **Internal deficits**
 - **Disinflation/deflation**
 - **GDP growth slowdown**

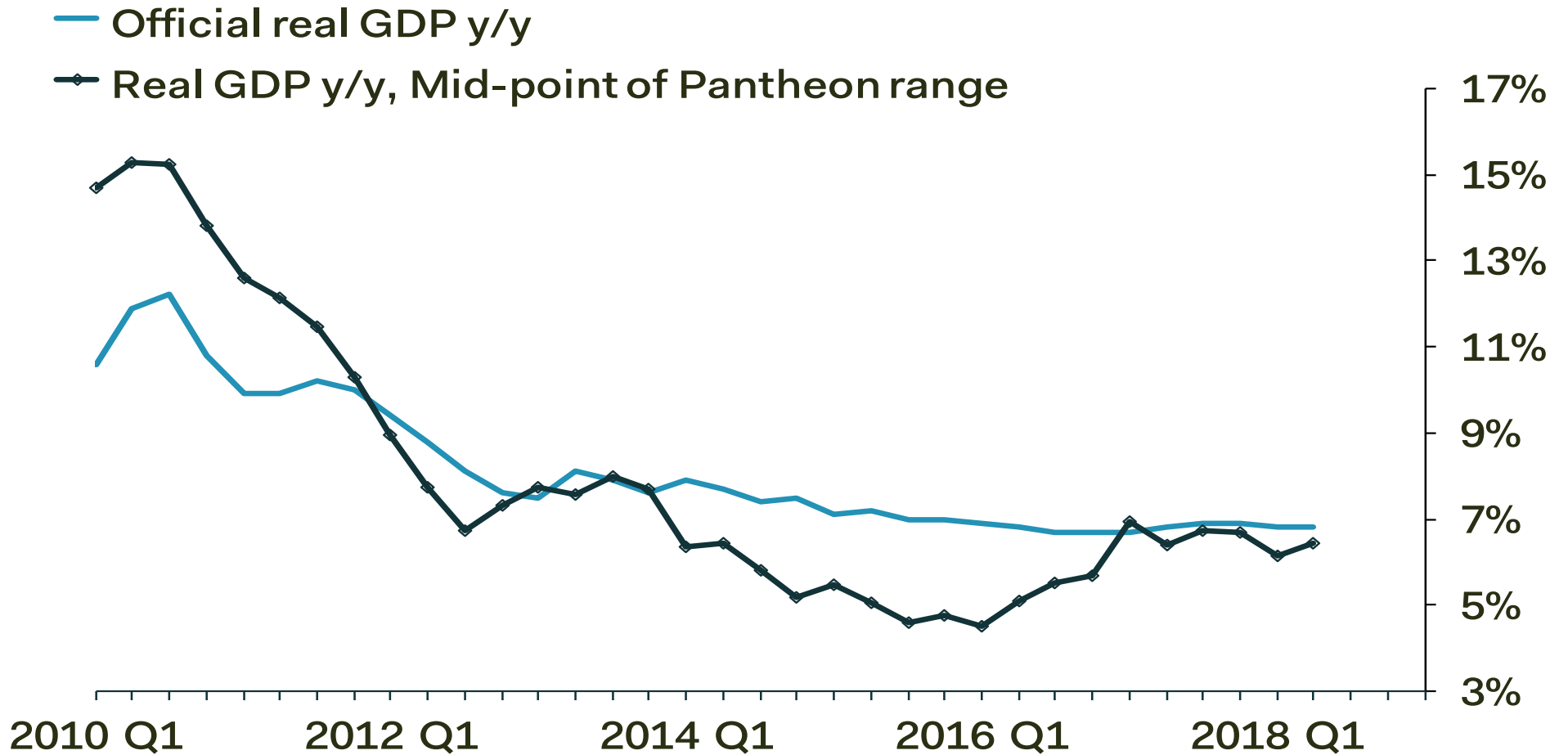


6. CONDITIONS IN 2017 MADE IT EASY FOR CHINA TO DELEVERAGE



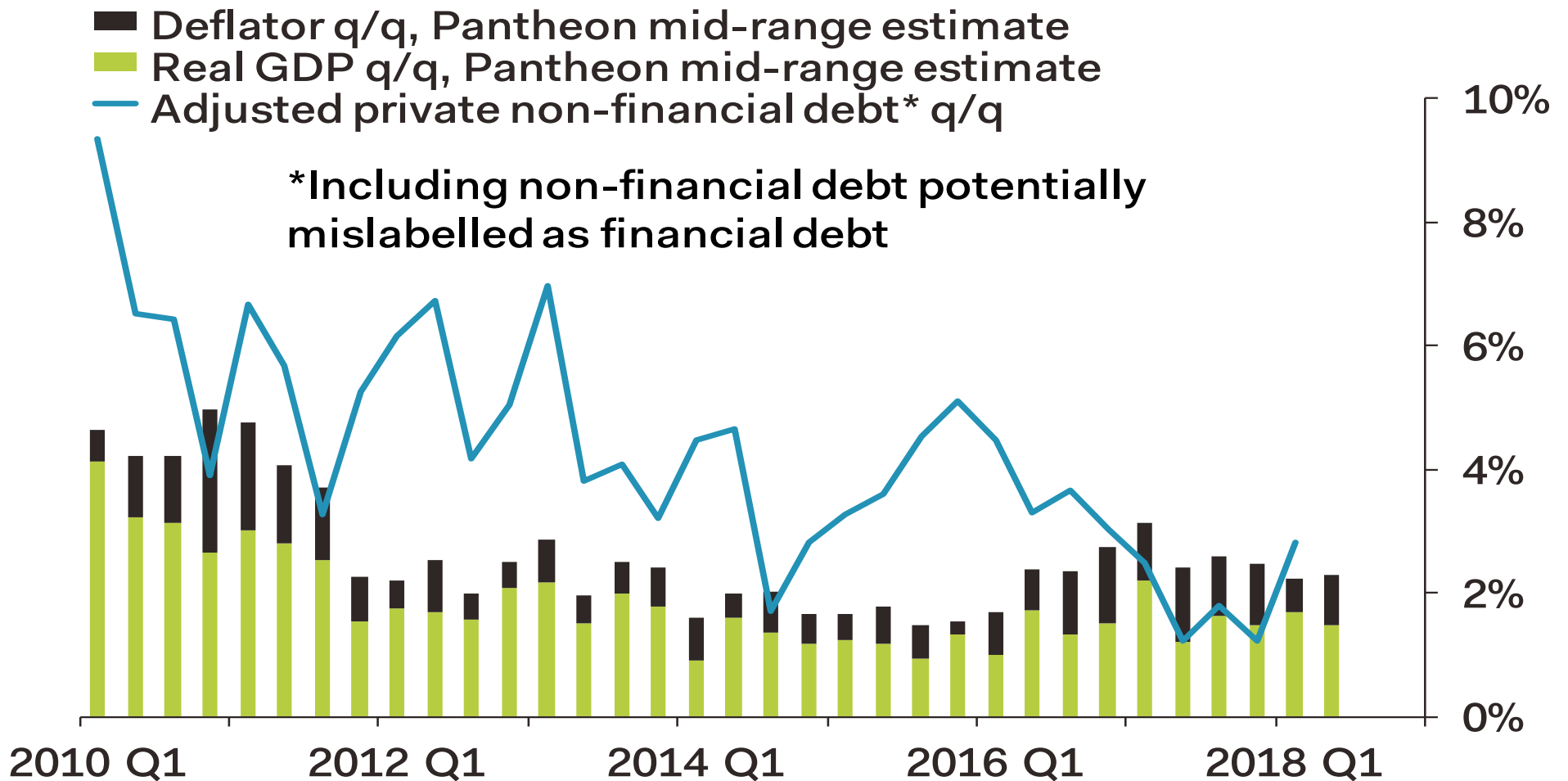


7. THE OFFICIAL NUMBERS DON'T SHOW IT; BUT 2017 WAS BENIGN FOR DELEVERAGING

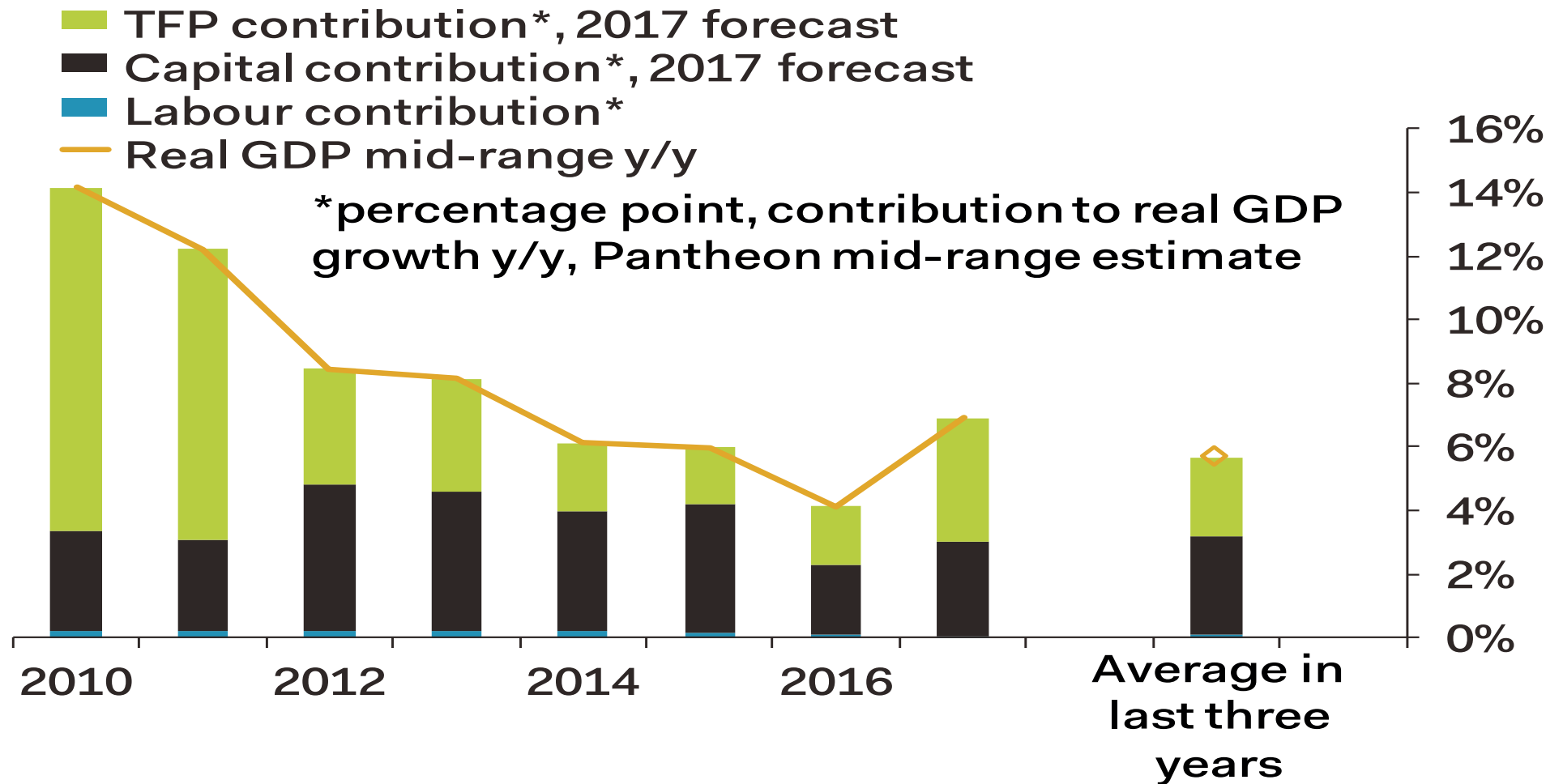




8. REFLATION HELPED CORPORATIONS BEAR THE BURDEN



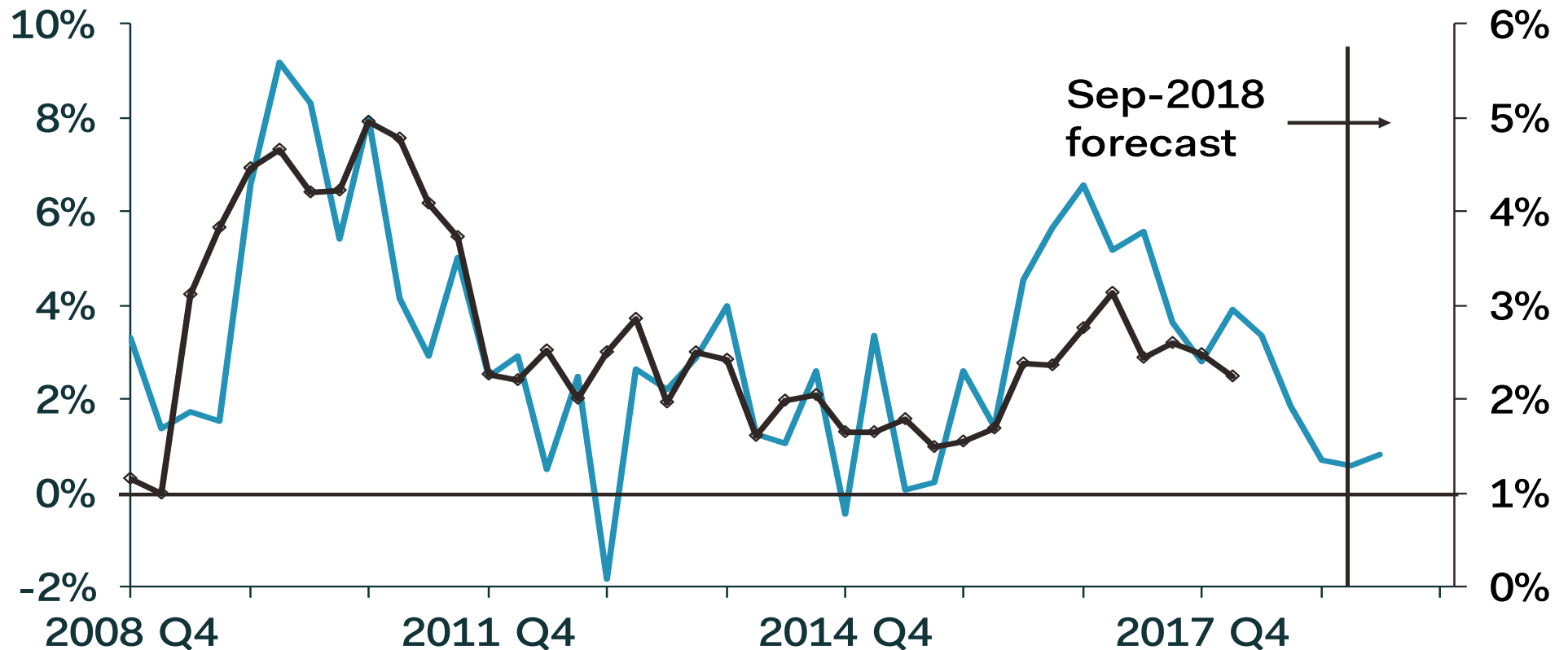
9. THE 2017 PRODUCTIVITY REBOUND LIKELY WAS CYCLICAL



10. THOSE BENIGN CONDITIONS FROM 2016H2-TO-2017Q3 ARE NOW DISSOLVING; BIZ AS USUAL?

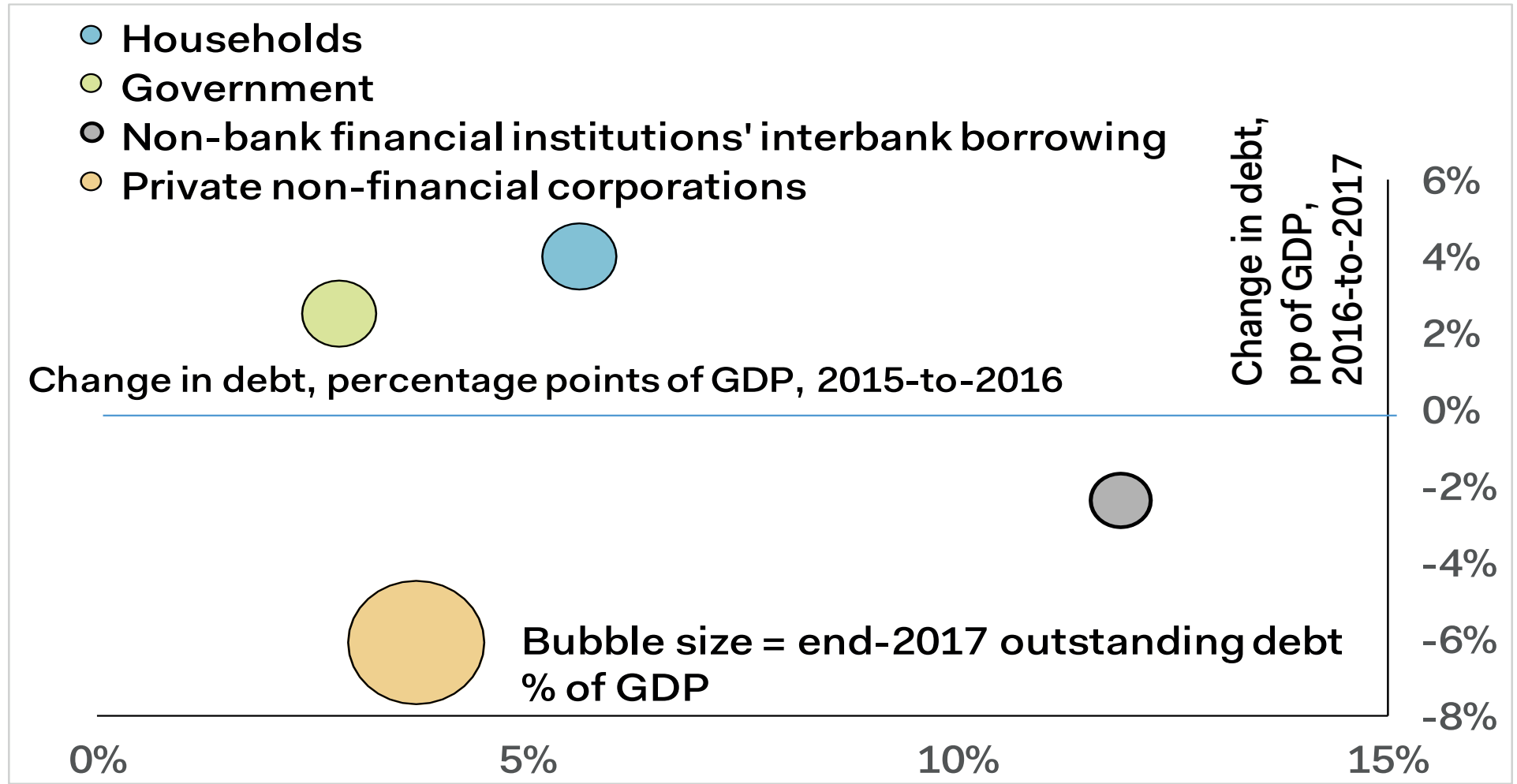
— M1, SA, q/q, advanced by 3 quarters (Left)

— Nominal GDP q/q, 2017 data subject to revisions, Pantheon SA (Right)





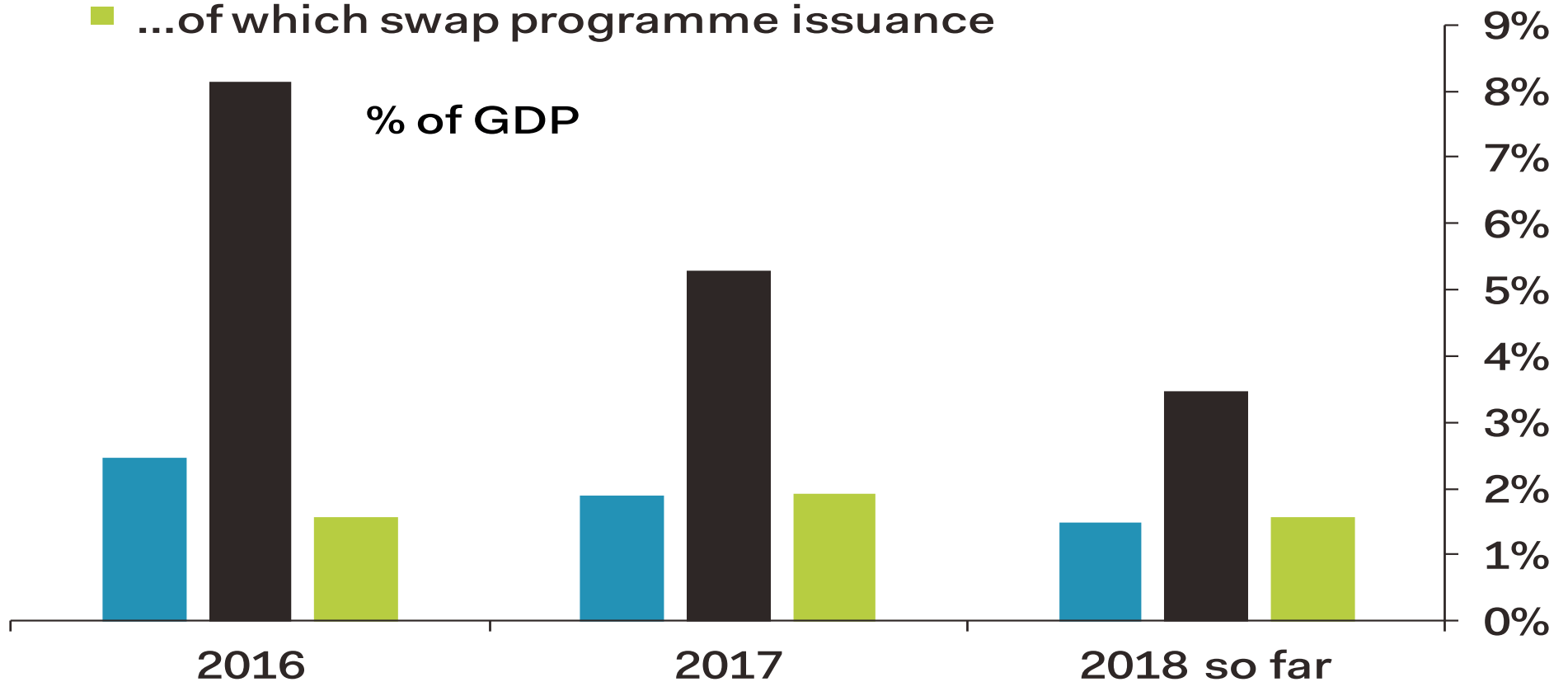
11. HAVE CORPORATIONS HIT A WALL? DEBT HAS NEW DRIVERS, BUT OFFICIALS DON'T LIKE IT





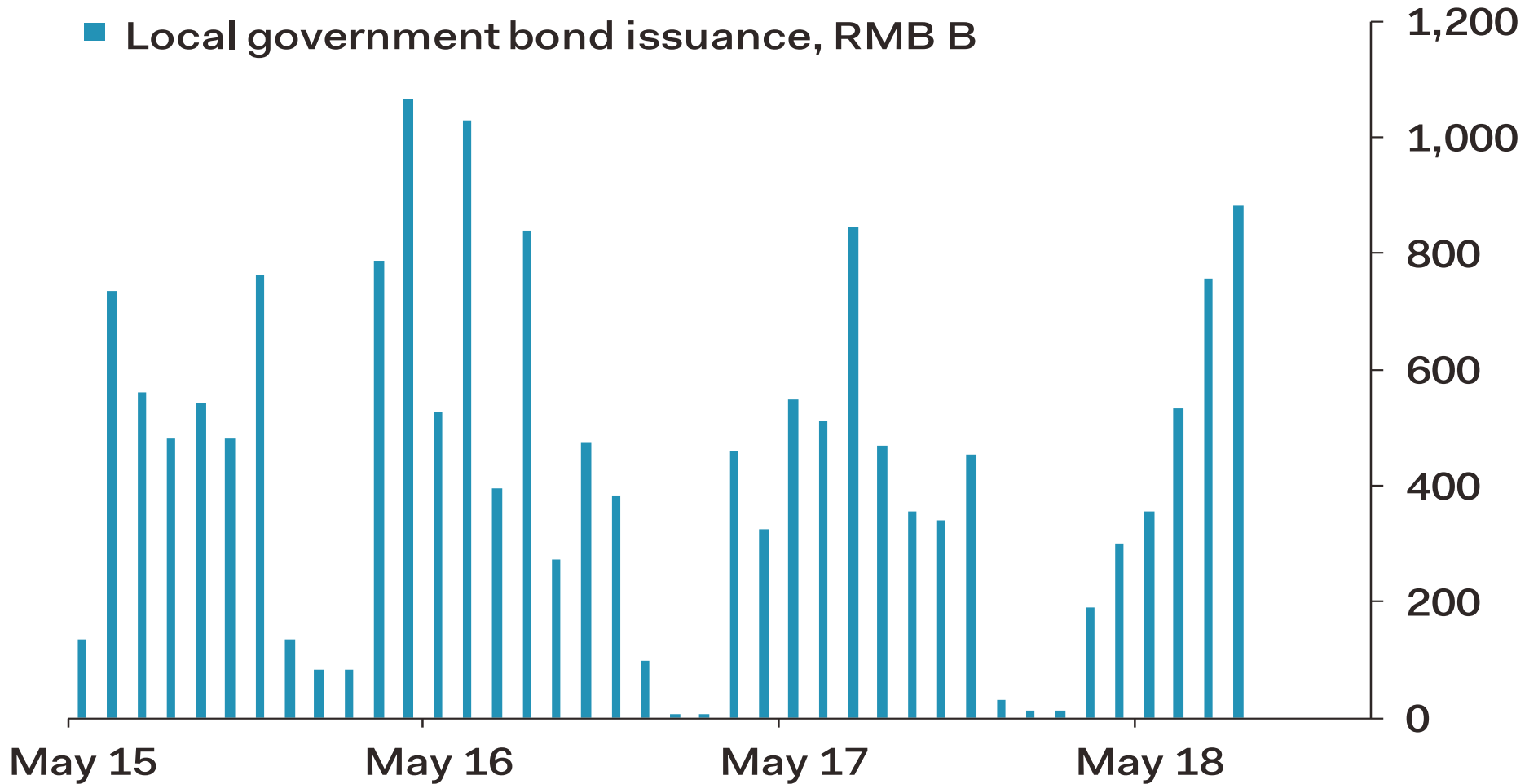
12. LOCAL GOVERNMENT DEBT ISSUANCE STALLED; THE PROVINCIAL DEER IN HEADLIGHTS EFFECT

- Issuance of LGFV bonds
- Total local government debt issuance
- ...of which swap programme issuance



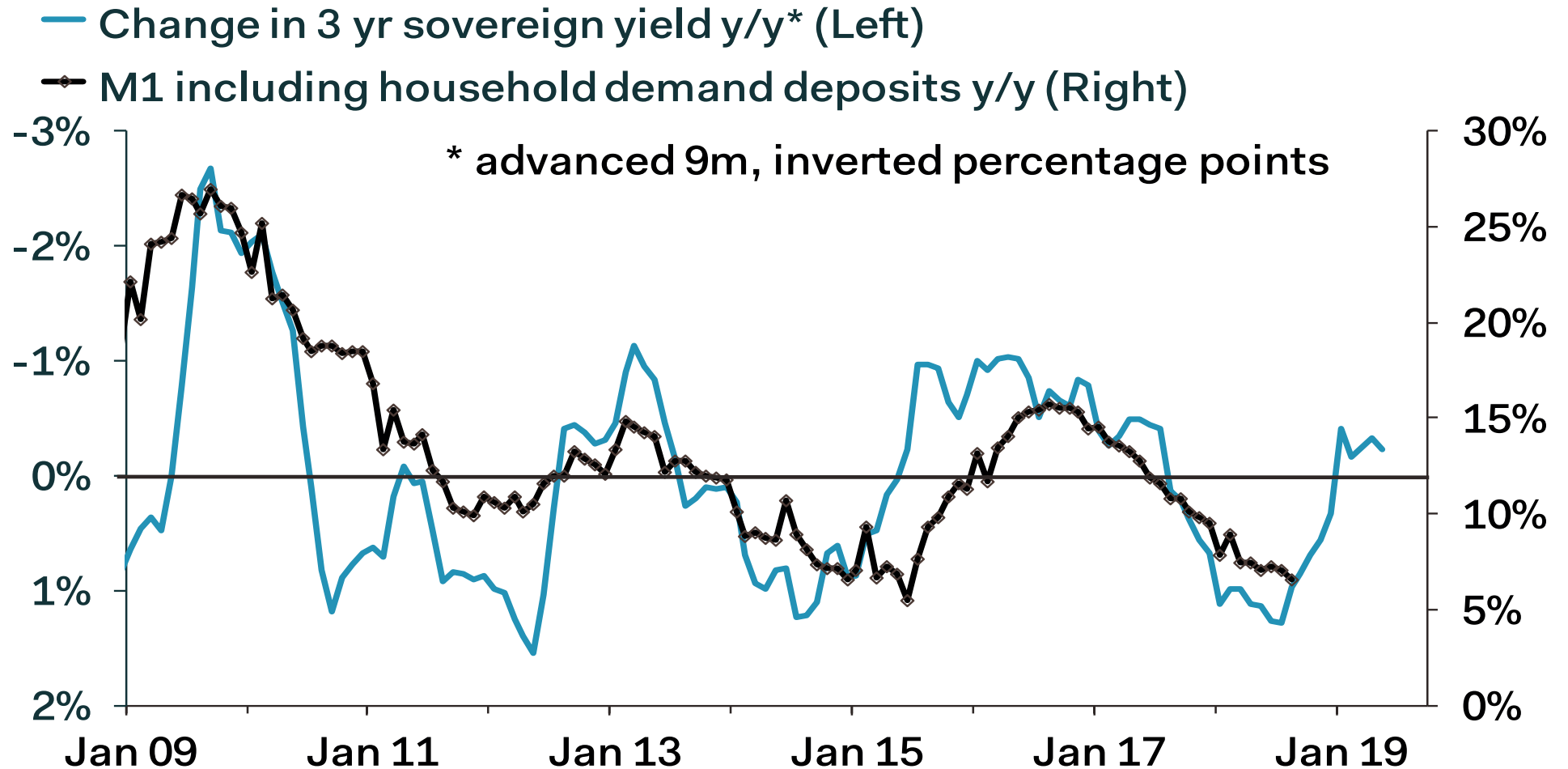


13. LOCAL OFFICIALS HAVE NOW HEADED THE CALL TO BORROW AND INVEST IN INFRASTRUCTURE



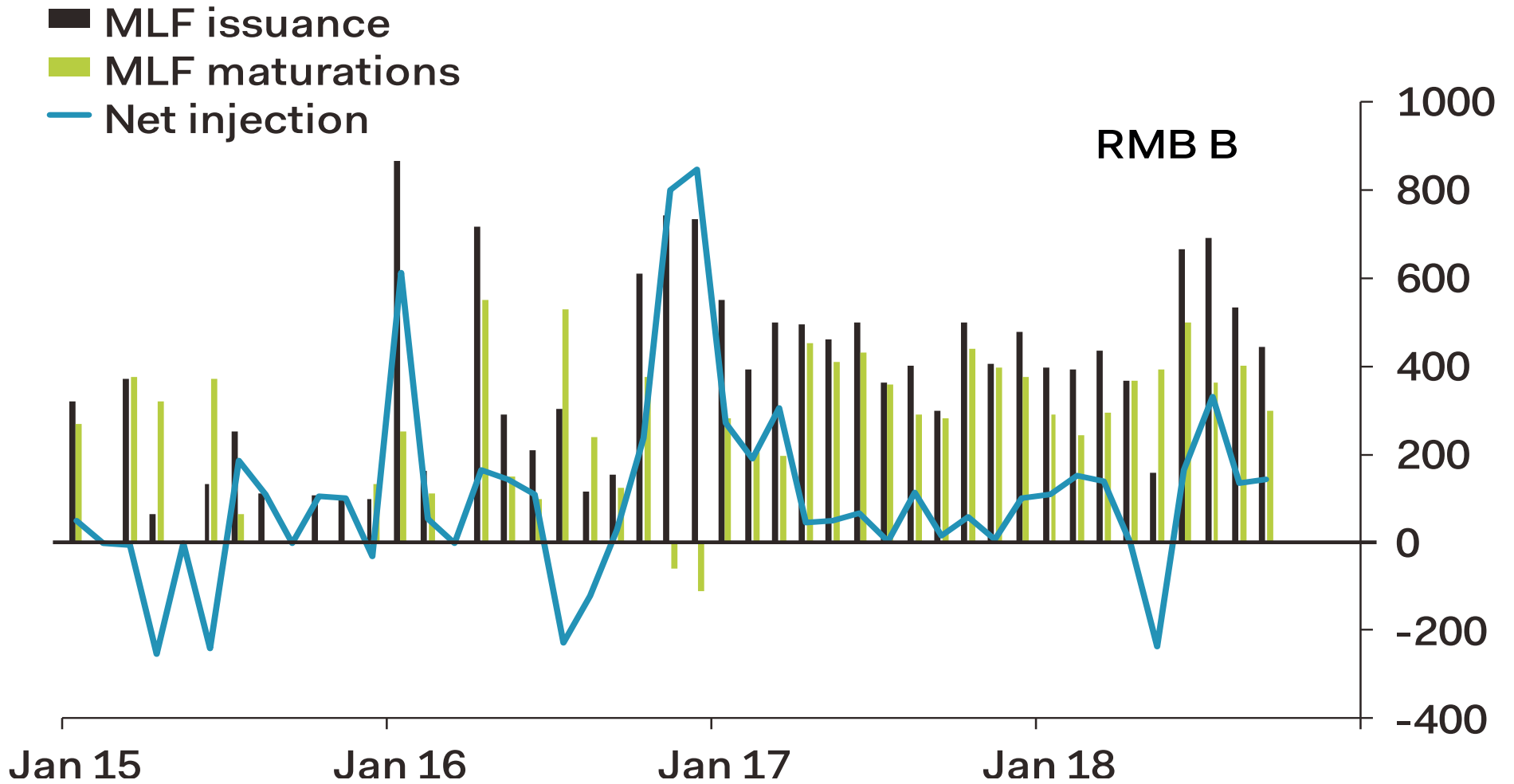


14. THE MONETARY STANCE BEGAN LOOSENING IN Q2





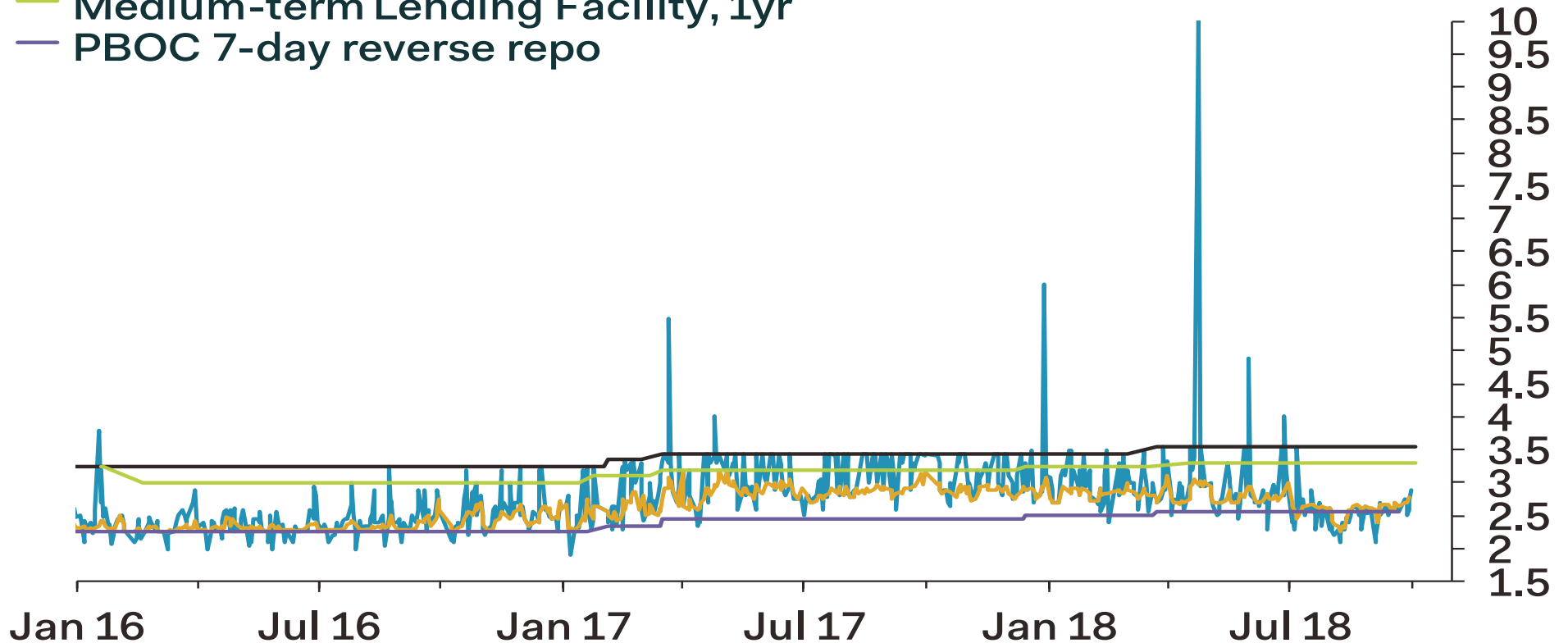
15. PBOC LIQUIDITY INJECTIONS ARE SUPPORTING PROVINCIAL ISSUANCE





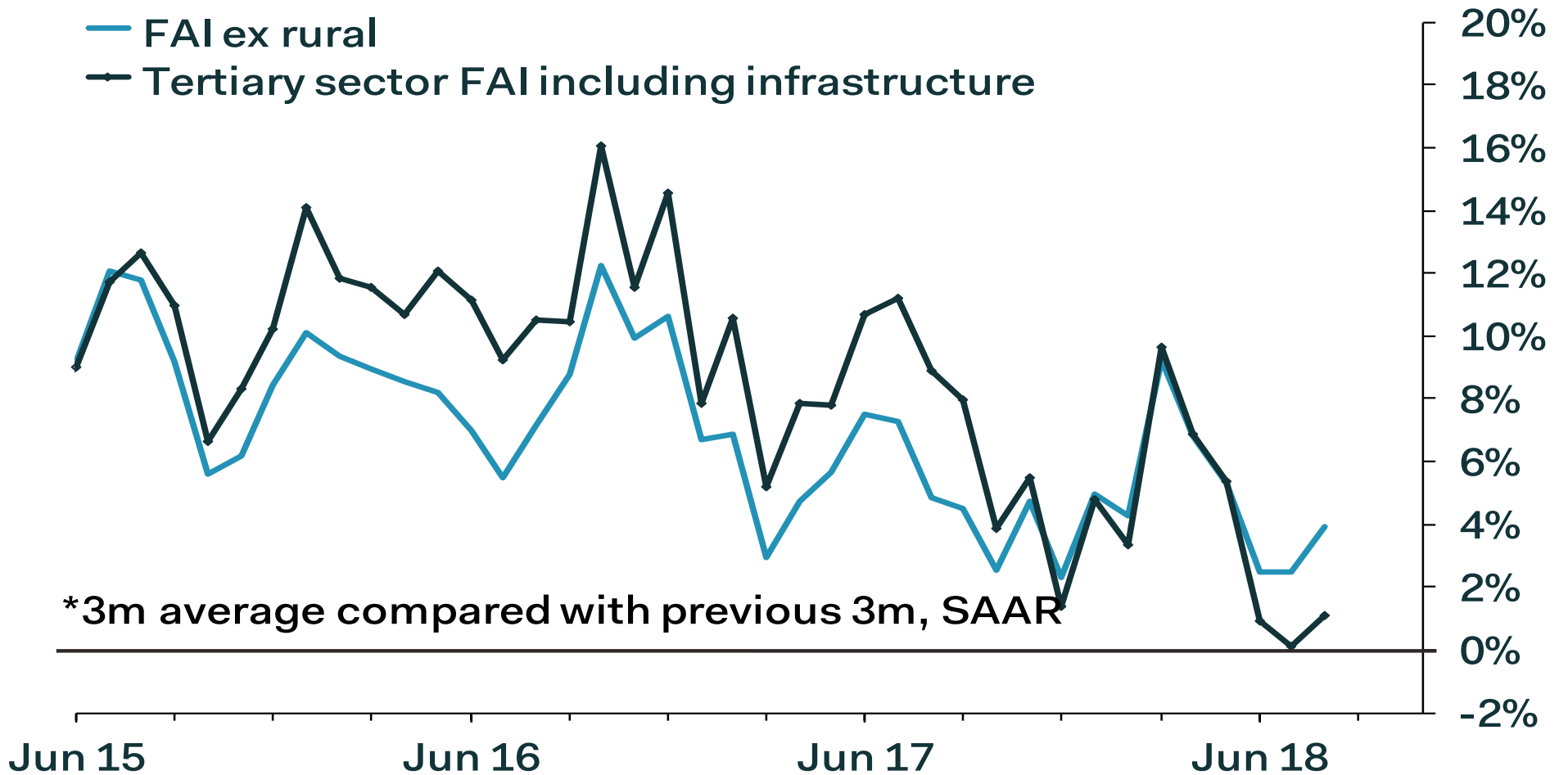
16. INTERBANK RATES HAVE SNAKED ALONG THE BOTTOM OF THE CORRIDOR, EVEN BELOW

- 7-day repo rate, %
- Standing Lending Facility, 1m
- CFETS China Interbank repo, volume-weighted average, 7d
- Medium-term Lending Facility, 1yr
- PBOC 7-day reverse repo





17. INFRASTRUCTURE GROWTH IS PICKING UP AT THE MARGIN, FROM HISTORICALLY LOW RATES





- **Is there a new outlet for China's excess savings?**

- **Internal: Made in China 2025**

- **External: Belt and Road Initiative**

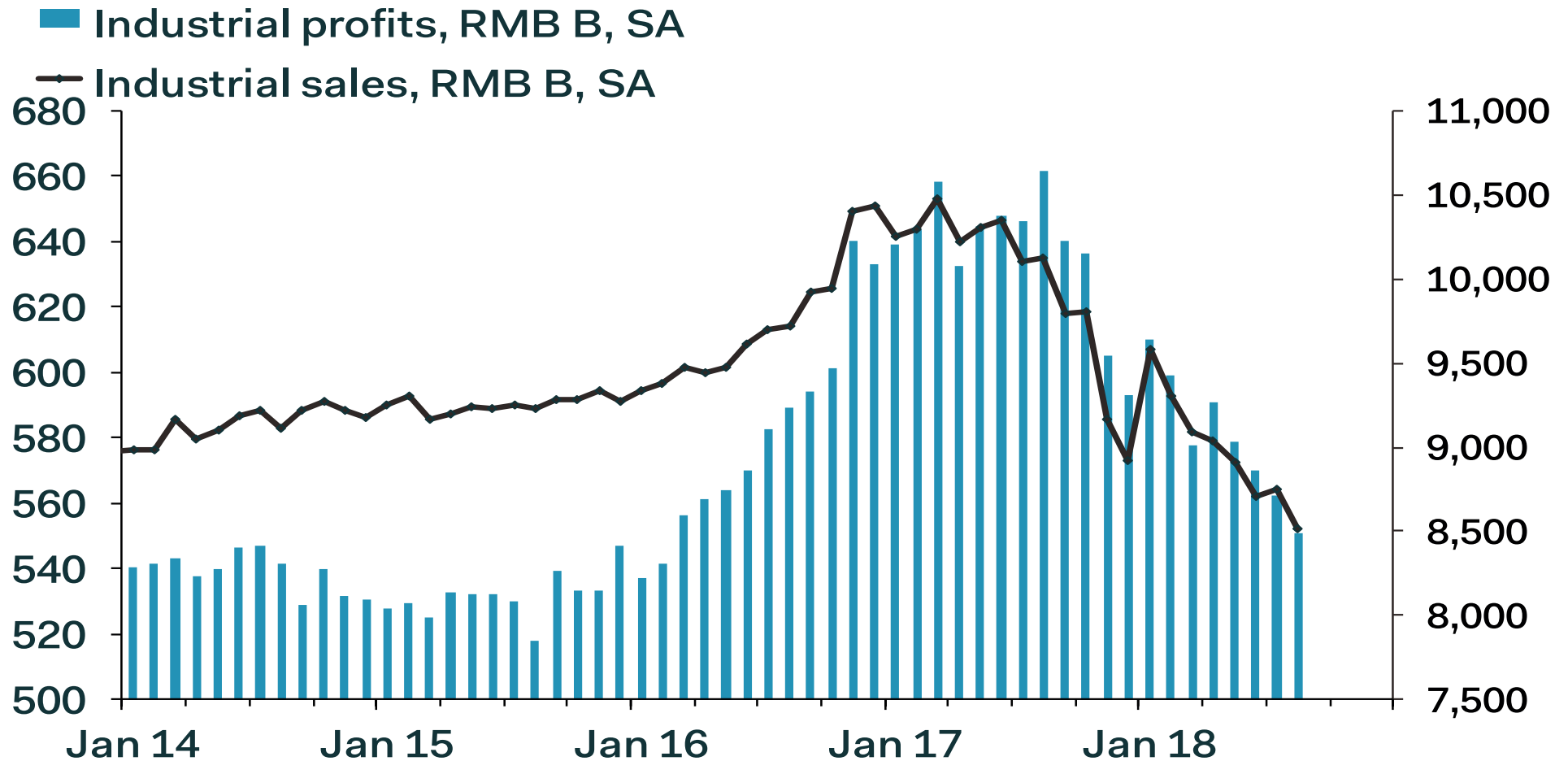
- ***Containment?***

- ***Debt***

- ***Pollution***



18. BUT THE PRIVATE SECTOR IS STRUGGLING, AS MEASURES TO RE-DIRECT RESOURCES FAIL



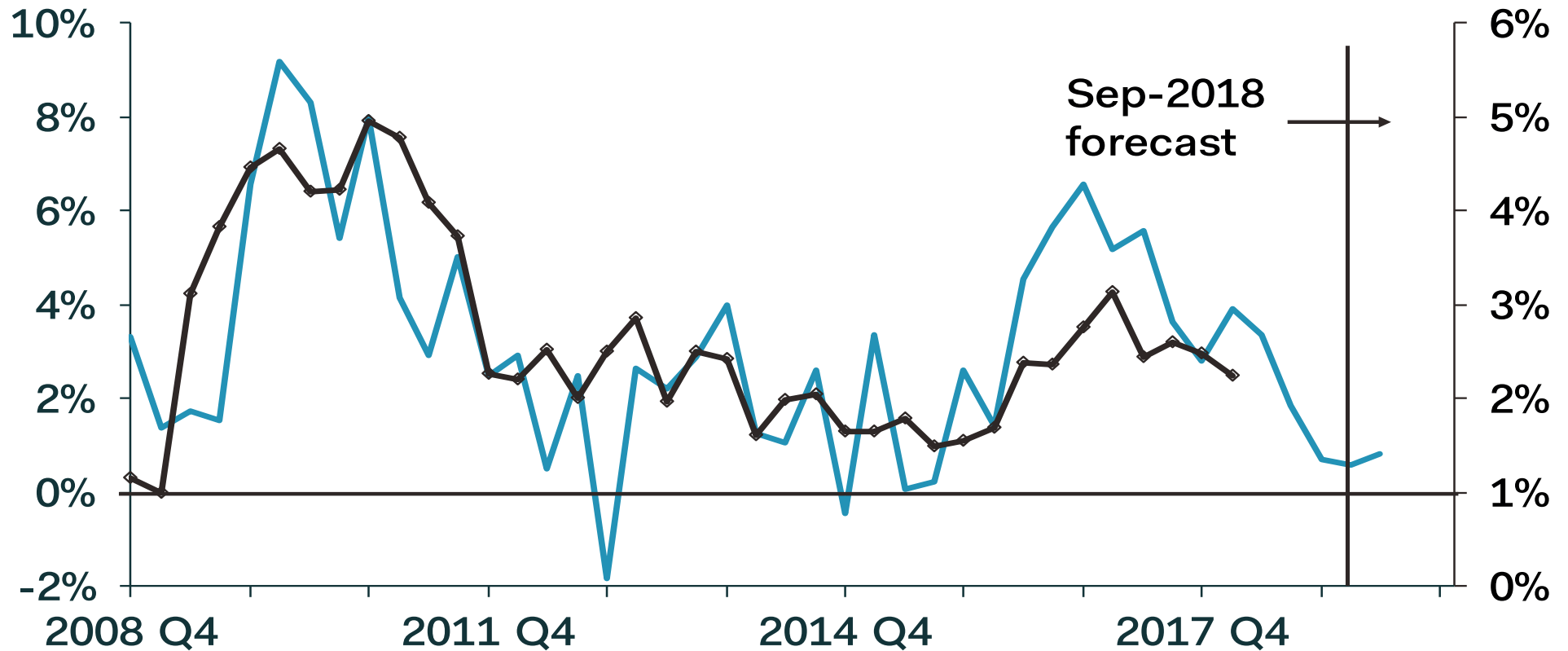
- **Near-term downside risks?**



19. IN SHORT, GDP GROWTH WILL TAKE TIME TO RESPOND

— M1, SA, q/q, advanced by 3 quarters (Left)

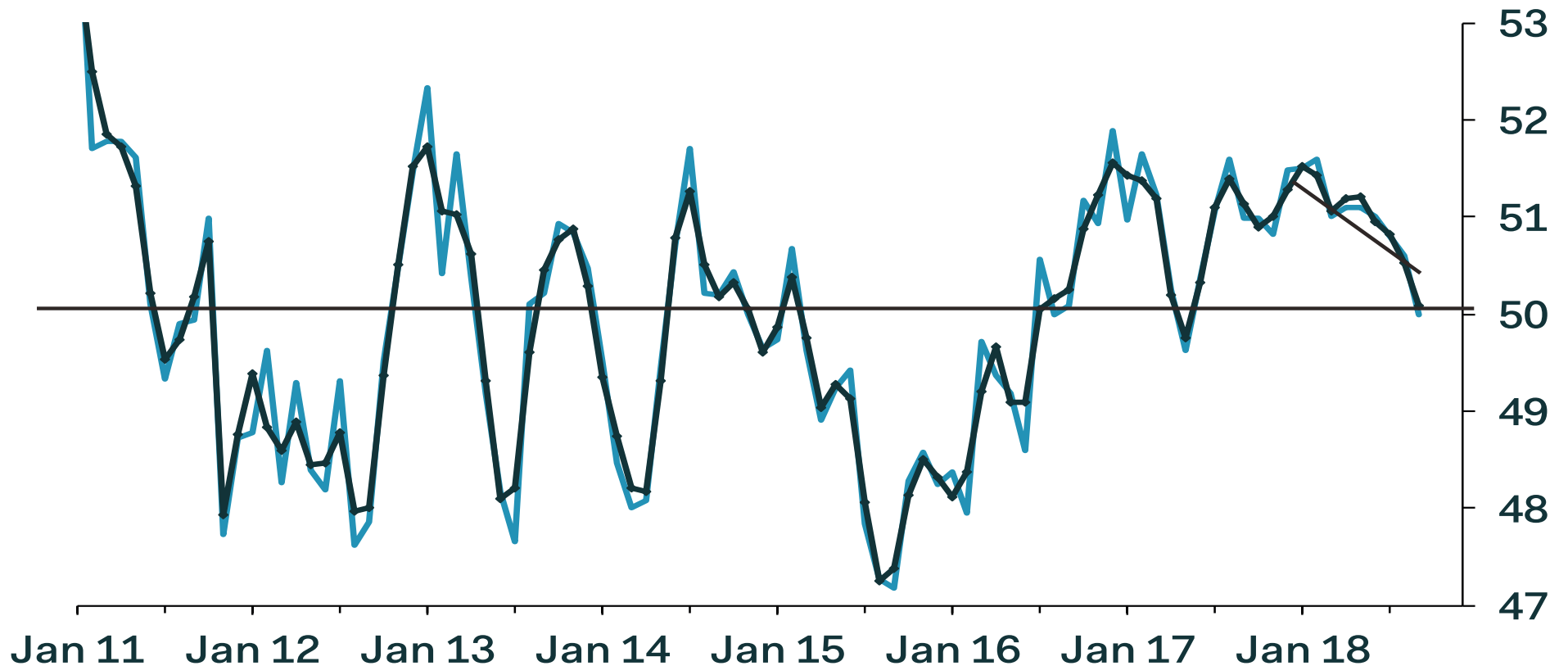
— Nominal GDP q/q, 2017 data subject to revisions, Pantheon SA (Right)





20. IN THE MEANTIME, ACTIVITY IS SET TO WEAKEN

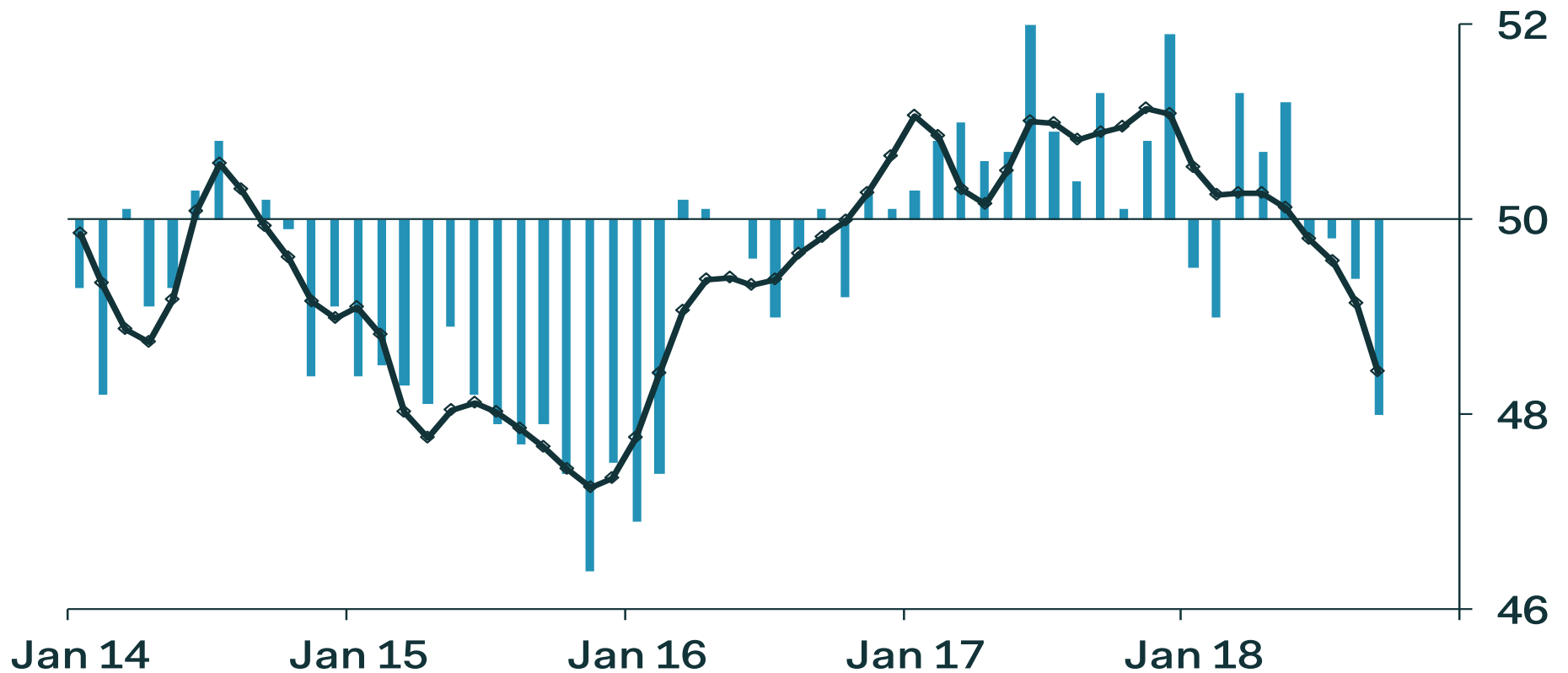
- Caixin PMI manufacturing, actual
- Caixin PMI manufacturing, short-term adjusted trend





21. AND TARIFFS ARE TAKING A TOLL, YET TO BE REFLECTED IN THE HARD TRADE DATA

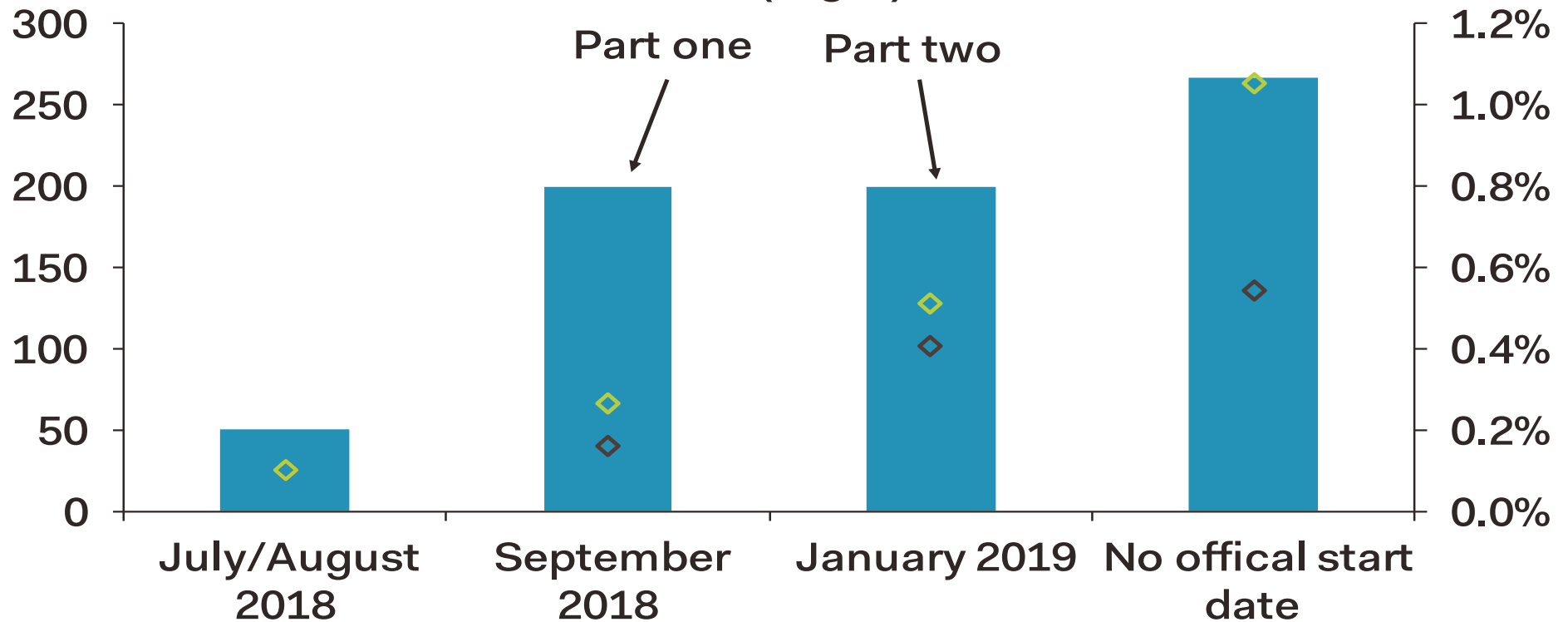
- New export orders, actual
- ◆ New export orders, Pantheon sa trend





22. THE TARIFF HIT TO GDP SO FAR IS MODEST

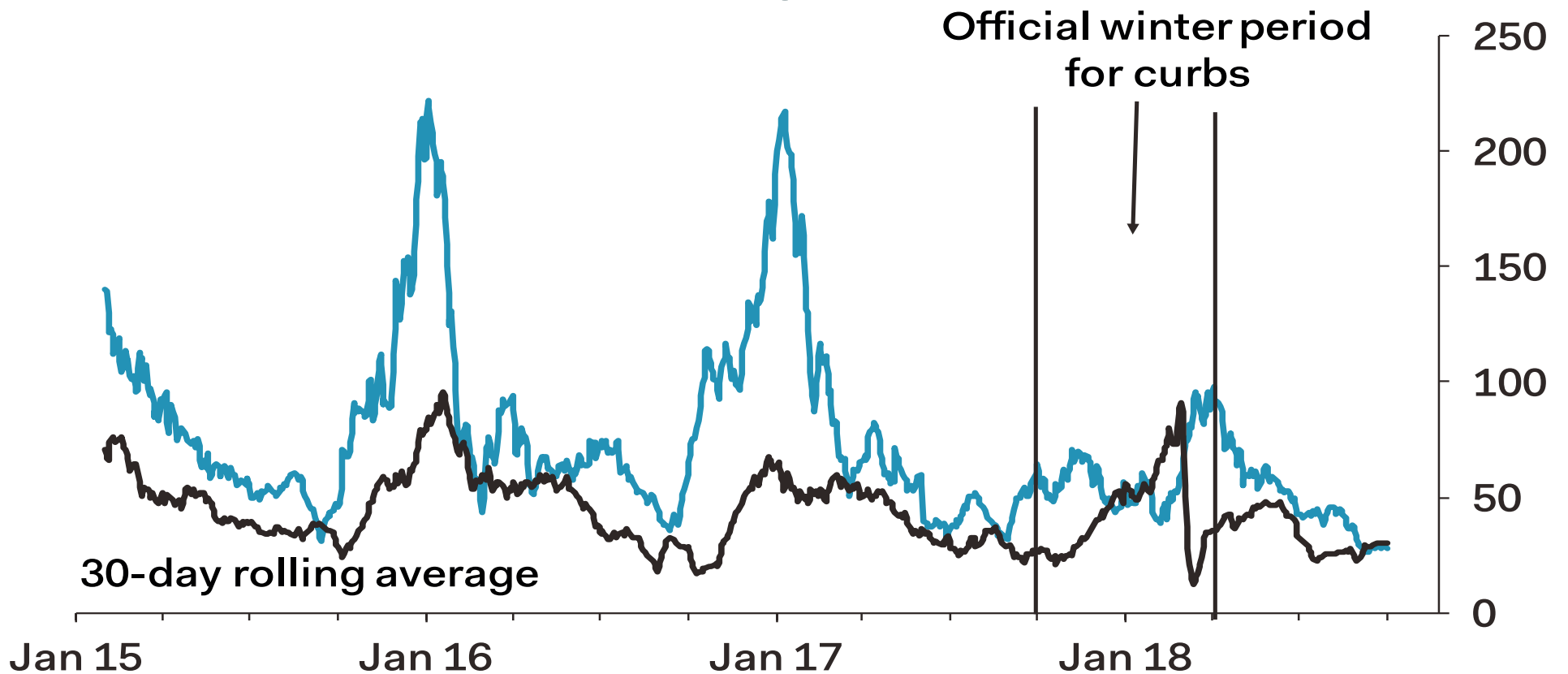
- Imports affected, USD B (Left)
- ◇ Tariffs as % of Chinese GDP (Right)
- ◇ Cumulative tariffs as a % of GDP (Right)





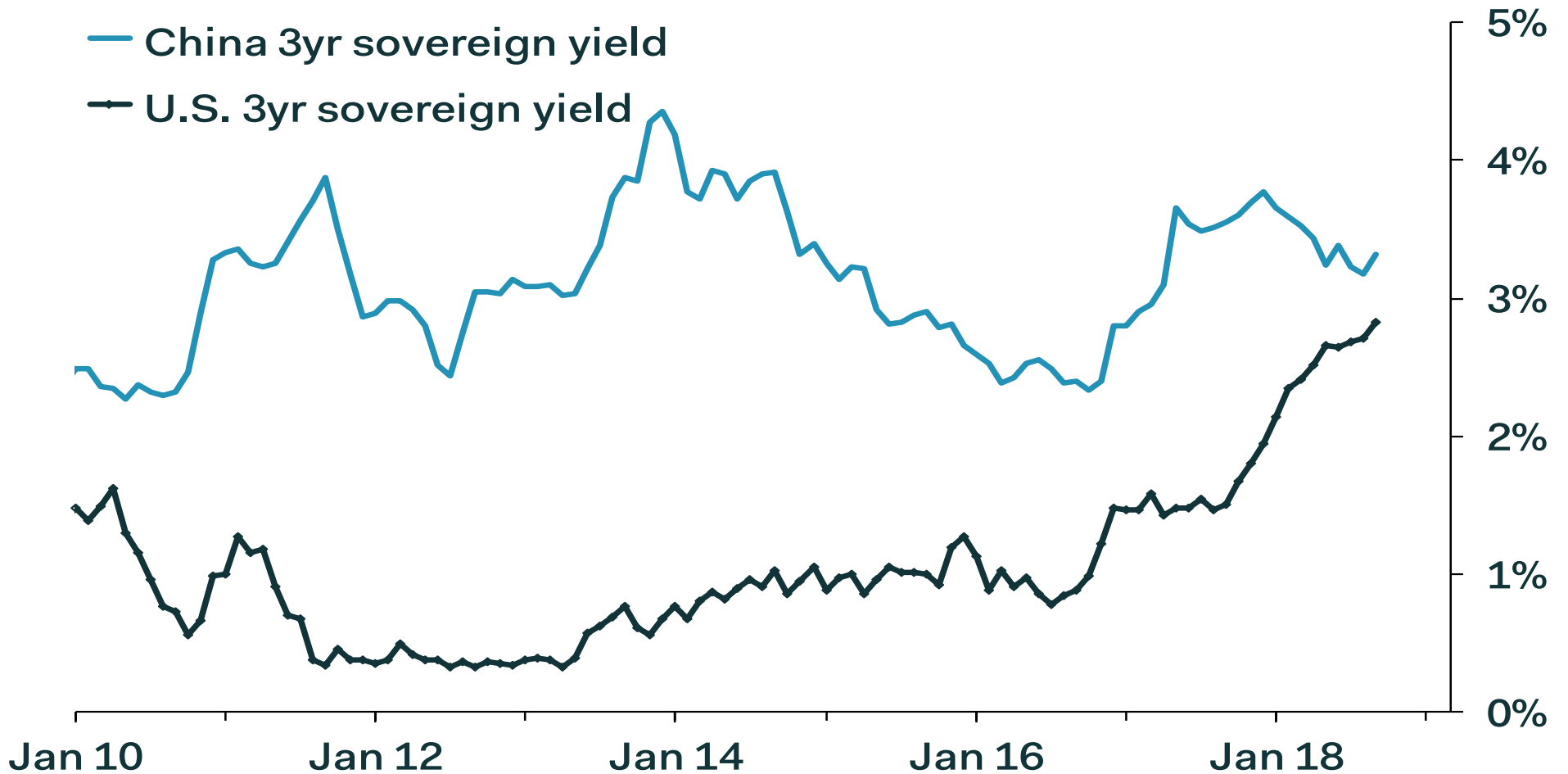
23. AND THE AUTHORITIES HAVE SET A STRONG PRECEDENT FOR KEEPING POLLUTION IN CHECK

- PM 2.5 concentrations, Beijing
- PM 2.5 concentrations, Shanghai



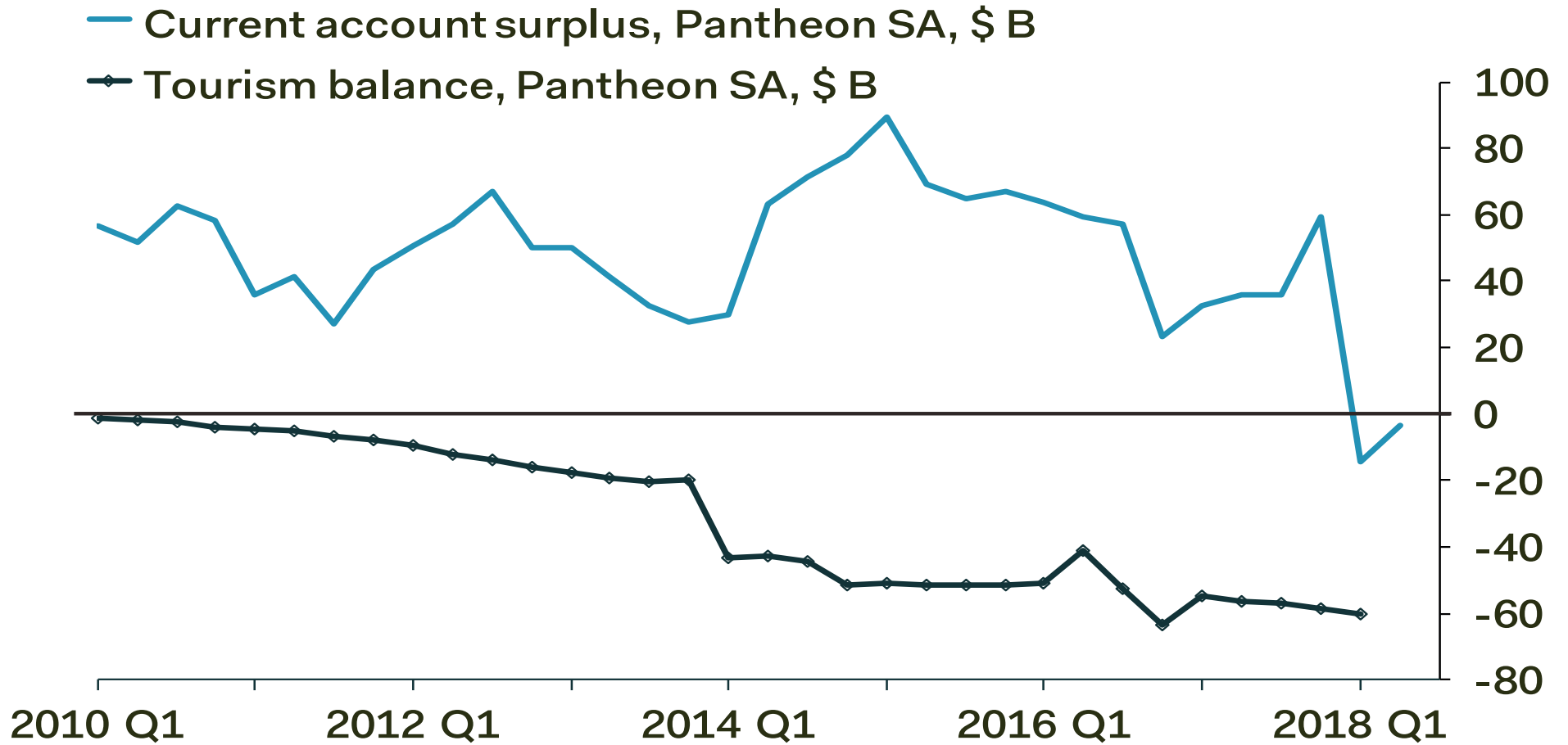


24. WHAT'S THE DOWNSIDE RISK?





25. A WIDENING TOURISM DEFICIT HAS BEEN A MAJOR DRAG IN RECENT YEARS





PANTHEON[™]
MACROECONOMICS

INDEPENDENT • INCISIVE • ILLUMINATING

- **Longer-term downside AND upside risk?**



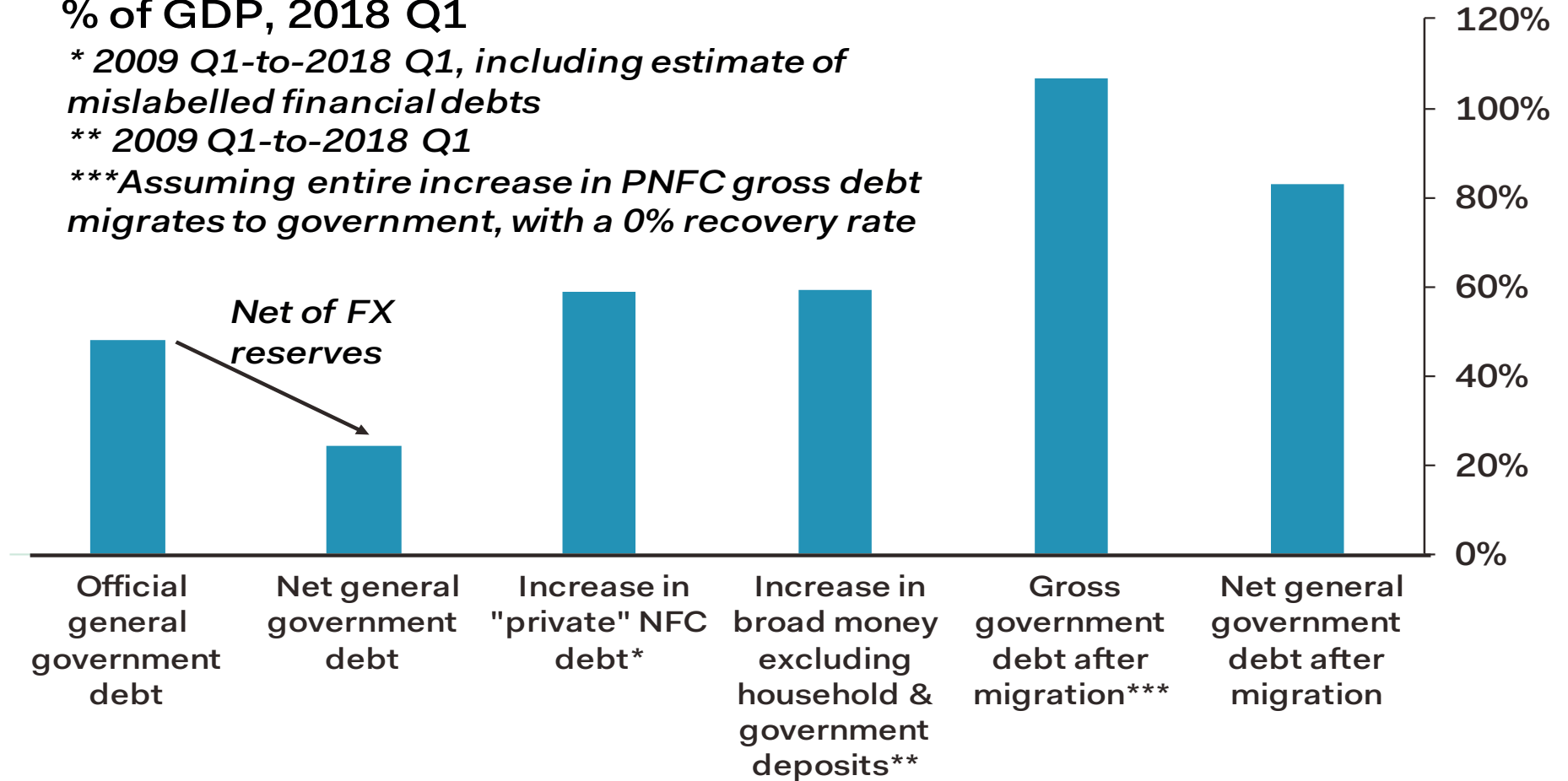
26. WHAT IF THINGS GET SO BAD THAT THEY GET GOOD?

% of GDP, 2018 Q1

** 2009 Q1-to-2018 Q1, including estimate of mislabelled financial debts*

*** 2009 Q1-to-2018 Q1*

****Assuming entire increase in PNFC gross debt migrates to government, with a 0% recovery rate*





Summary

- * **The last few years, since before Mr. Trump took office, were relatively benign for U.S.-Sino relations; China wasn't able to export its savings, so distortions were built domestically, not abroad.**
- * **But internal imbalances are becoming stretched, and the ongoing Fed hiking cycle is likely to uncover that, especially when external GDP growth starts to slow.**
- * **Conditions are turning against Chinese deleveraging.**
- * **Leading indicators, combined with the tariff threat and environmental curbs suggest activity still has further to slow, but GDP growth should pick up in the first half next year.**
- * **If the authorities overstimulate in the meantime, the consequences will be more severe than previously, resulting in a further RMB depreciation.**
- * **So far they are avoiding the temptation, and anyway face environmental constraints**
- * **The authorities still have space to clear up bad debts. The long-term upside risk is that China is pushed into cleaning up at this stage in the game, when a Japanning path can still be avoided.**