

## China: GDP Growth Holds Steady In 2013

- China 4Q growth rate came in better than expected at 7.7%, the same pace as for full year of 2013 and 2012.
- We look for China to grow at an even pace for 2014, with the central bank holding its interest rate policy steady while letting market playing a greater role.
- Looking ahead, this year is likely to see far more policy risks than we have seen before, as China carries out its market reform plans laid out at the 18th Third Plenum in November last year.

### Data Largely Within Expectations

China released its 4Q13 and 2013 full year GDP report and the remainder of December monthly data including industrial production, retail sales, and fixed asset investment, this morning (Mon 20 January).

**4Q GDP growth came in marginally higher than expected at 7.7%/y, vs. expectation of 7.6%**, slowing down from 7.8% pace in 3Q13. For the full year, China's economy expanded 7.7% in 2013, the same rate as in 2012, but below that of the 9.3% pace seen in 2011. The slowing momentum is also reflected in the seasonally adjusted figure, which slowed to 1.8%q/q from 2.2%q/q in 3Q13, but consistent with the trend seen in the first half of 2013.

Other data released this morning included the industrial production and retail sales data, as well as fixed asset investment, all of which largely came in within expectations. Particularly for industrial production at 9.7%/y in Dec vs. 10.0% in Nov and retail sales at 13.6%/y in Dec vs. 13.7% in Nov, which matched exactly consensus forecasts. Unsurprisingly, fixed asset investments continued to trend lower to 19.6%/y increase in 2013, down from 20.6% gain in 2012 and 23.8% in 2011, as the country grappled with excess capacity and tight liquidity conditions.

Data released earlier already painted a softening in growth momentum, including the various PMI measures, external trade report, and loans data.

### More Policy Risks Ahead

While the data indicate softer momentum ahead, we see China entering into a moderate growth period compared to the previous two economic cycles, with an average growth rate of just 7.5% over the 2013-2015 period, 3 percentage points below the annual average of 10.5% between 2003 to 2012. Domestically, a period of "quality instead of quantity" rationalizing is in place to boost productivity of existing capacity and investments, which is likely to curb the appetite for capital expenditure. Externally, the ongoing recovery of the US economy is encouraging though the other leg of global economy, i.e. Eurozone, remains tentative.

**For 2014, we maintain our growth forecast for China at 7.7% target, assuming activities pick up in the second half of 2014 and key reform measures are implemented in the first half of the year.** Downside risks are still present especially as the government moves towards liberalizing key markets such as for commodities, interest rates, exchange rate, among others, which could result in disruption and rationalizations within those industries, thereby dampening activities.

The next key event to watch is the National People's Congress sessions in March, which are likely to see the government's economic reform plans to be endorsed and also for the government to pursue its economic agenda of having greater role for the market in determining key prices such as interest rates, exchange rates, key factors prices, regulating of shadow banking sector, and restructuring of local government debt, among other things. This means that 2014 will be a year dominated by policy risks which could put downward pressures on economic growth.

Meanwhile, we expect the PBoC to keep its key policy rates on hold, letting instead market forces to take a more prominent role in establishing market interest rates just as more regulations are put in place to rein the "shadow banking" sector and restructure the local government debt. As such, we look for benchmark interest rates and banks' reserve requirement ratio to stay unchanged, with 1Y deposit rate at 3%, 1Y lending rate at 6%, and RRR at 20% (RRR has been unchanged since May 2012).

In terms of currency, our base case for a steady appreciation of the RMB remains valid for 2014 as China continues to push forward its plans for currency internationalization and less intervention from the PBoC, which is consistent with its target of a market-determined exchange rate system.

As a next step, we anticipate the long-overdue widening of the RMB trading bands to take place in 2014, from 1% band around the midpoint currently, to 2% or 3% band. However, with the RMB now considered by PBoC to be near its equilibrium level against the USD, the currency is likely to stay muted even with such announcement. As such, we hold to our view that the RMB to stay on its moderate appreciation path into 2014 with a 1-3% annual appreciation pace. We are keeping to our forecasts for the USD/RMB of 5.90 at end-2014 (current: 6.05), and we anticipate the 6.00/USD barrier to be breached before mid-2014.

China's Key Macro Data												
	2011	2012	2013	2Q13			3Q13			4Q13		
Real GDP Growth %y/y	9.3	7.7	7.7	7.5			7.8			7.7		
Real GDP Growth %q/q SA				1.8			2.2			1.8		
%y/y change	2011	2012	2013	Apr-13	May-13	Jun-13	Jul-13	Aug-13	Sep-13	Oct-13	Nov-13	Dec-13
Industrial Output	13.7	10.8	9.7	9.3	9.2	8.9	9.7	10.4	10.2	10.3	10.0	9.7
NBS PMI	50.3	50.6	51.0	50.6	50.8	50.1	50.3	51.0	51.1	51.4	51.4	51.0
HSBC PMI	48.7	51.5	50.5	50.4	49.2	48.2	47.7	50.1	50.2	50.9	50.8	50.5
CPI	5.4	2.7	2.6	2.4	2.1	2.7	2.7	2.6	3.1	3.2	3.0	2.5
PPI	6.1	-1.7	-1.9	-2.6	-2.9	-2.7	-2.3	-1.6	-1.3	-1.5	-1.4	-1.4
Exports	20.3	7.9	7.9	14.6	0.9	-3.3	5.1	7.1	-0.4	5.6	12.7	4.3
Imports	24.9	4.4	7.3	16.6	-0.1	-0.9	10.8	7.1	7.4	7.5	5.4	8.7
Trade Balance (US\$ bn)	157.9	232.8	261.4	18.2	204.0	27.1	178.0	28.5	15.2	31.1	33.8	25.6
New Loans (RMB bn chg)	7,471.5	8,203.8	8,891.9	792.3	669.4	862.8	699.7	712.8	787.0	506.1	624.6	482.5
Total Social Financing (RMB bn chg)	12,828.6	15,760.5	17,290.0	1,762.9	1,187.1	1,037.5	819.1	1,584.0	1,411.3	864.0	1,226.9	1,232.2
M2	13.6	13.8	13.6	16.1	15.8	14.0	14.5	14.7	14.2	14.3	14.2	13.6
Urban Fixed Asset Investment YTD	23.8	20.6	19.6	20.6	20.4	20.1	20.1	20.3	20.2	20.1	19.9	19.6
Retail Sales	17.2	14.4	13.1	12.8	12.9	13.3	13.2	13.4	13.3	13.3	13.7	13.6

Source: CEIC, Bloomberg, National Bureau of Statistics; UOB Economics-Treasury Research estimates. All data for individual months except noted

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