

China: Consumption is key

Economic recovery to continue: We expect China's recovery to continue in Q1. China was the only major economy to record growth this year (4.9% in Q3 and 0.7% between January and September), thanks, in our view, to the control of the Covid-19 pandemic and effective containment, which has allowed economic activity to return largely to normal. Industrial production momentum has accelerated since April, driven by strong export demand and investment in property and infrastructure.

Consumption is key to the next step for growth: We expect services to catch up; the real drag has been consumption, which has fallen behind because of constraints on consumer activity, behaviour and confidence. Consumption is key to determining the success of China's 'dual-circulation' growth strategy – a parallel emphasis on internal and international cycles of production, distribution and consumption – outlined in the 14th Five Year Plan, which aims to promote urbanisation, increase purchasing power, and to enhance consumption capability and propensity and raise public consumer spending.

Paced exit from stimulus: Policymakers appear satisfied with the growth recovery and have started to exit stimulus slowly. We expect the broad fiscal deficit ratio to reduce to 5.5% of GDP in 2021, compared with 8.5% in 2020. However, we think the government could change its spending structure to give more support to industrial innovation and upgrading, carbon emissions reduction and social security systems.

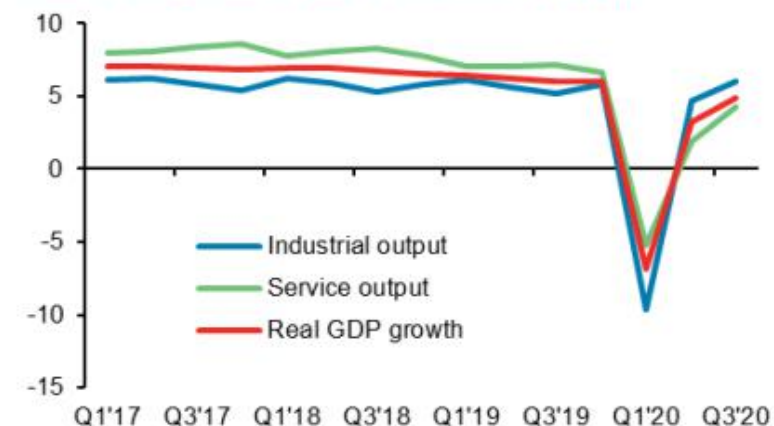
We expect monetary policy to become more of a balancing act between sufficient liquidity and financial risk control. Anti-internet-platform-monopoly measures, restrictions on peer-to-peer financing and the 'three red lines' on property developers' debt ratios will help to cap credit growth, in our view. While we think the odds of a hike in the official policy rate are low, a rise in the loan prime rate at some point in H2 2021 is likely.

Growing toward the new trend: Based on current growth momentum and the policy outlook, we forecast GDP to rise by 8.6% in 2021, with the economy still in the growth recovery stage. Indeed, productivity losses suffered under Covid-19 mean a full recovery to the growth trend or potential may not be realised before 2023. We project GDP to grow 5.3% in 2022.

Limited RMB strength: We expect RMB appreciation to continue through 2021 due to strong economic fundamentals, effective Covid-19 control, a weakening USD, interest rate spread widening, financial and capital market liberalisation, and changes in policy stance regarding RMB FX. However, as these effects fade, and given the uncertainty in China-US relations, we think this appreciation is likely to slow.

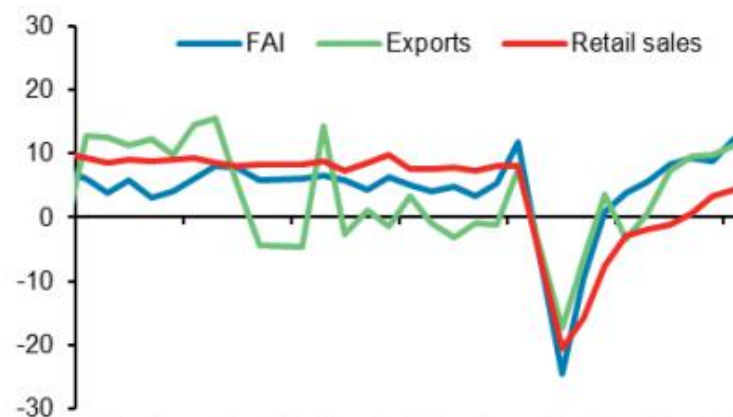
[Xingdong Chen](#), Head of GM Economic Research, China | [Jacqueline Rong](#), Economist, China | BNP Paribas (China) Limited

Industrial output leading the growth recovery (% y/y)



Sources: China NBS, BNP Paribas

Consumption to determine strength of growth (% y/y)



Sources: China NBS, China Customs, BNP Paribas