

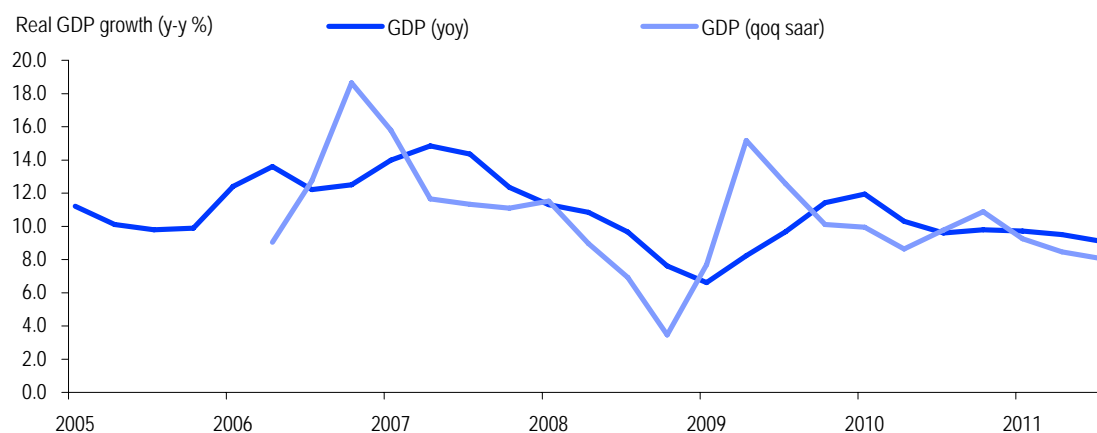
# Asia Economics

## China's economy is cooling

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**China's GDP grew 9.1% YoY in the third quarter, down from 9.5% YoY in the second quarter.** According to China's National Bureau of Statistics (NBS), this implies QoQ growth of 9.5% at an annualised rate, about the same as in Q2. However, according to our estimates, QoQ (SAAR) growth eased to around 8% in the third quarter of 2011. The YoY pace was in line with our expectations (and slightly lower than Bloomberg consensus forecasts). However, our QoQ (SAAR) estimates suggest a sharper slowdown than we anticipated, in part because of revisions to data for the first half.

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Source: CEIC, MF Global estimates

**The slowdown in the third quarter was due largely to weaker exports, while domestic demand held up well, until recently.** On our preliminary estimates, the contribution of net exports to YoY GDP growth eased from 1.3 percentage points in the second quarter to 0.8 percentage point in the third quarter, while domestic demand growth actually picked up, YoY.

**Industrial growth has held up surprisingly well, so far.** The deceleration in GDP was less pronounced in the industrial sector (GDP growth eased from 10.9% YoY in the second quarter to 10.5% YoY in the third quarter) than in the services sector (GDP growth decelerated from 9.3% YoY to 8.5% YoY). According to the monthly data, value-added growth in industry held up, with activity in heavy industry gaining speed in September.

**However, investment slowed in September.** Fixed-asset investment grew 24.9% in January-September in nominal terms, after 25.5% in the first half, implying a slight slowdown in the third quarter. However, after remaining robust in July and August, FAI growth slowed significantly in September. According to NBS estimates, overall FAI declined in September, month-on-month. In particular, housing construction activity is starting to show the impact of measures to contain property price increases and weak housing sales. FAI growth in real estate declined from 22% in August to 16.5% in September, in real terms, while the expansion of floor space started and under construction also declined in September.

**Consumption has remained steady.** Retail sales growth remained steady at 11% in real terms in September, with rural consumption benefiting from strong, broad-based income growth in the countryside.

**Looking ahead, the economy is likely to slow further.** The strong showing in industrial production in September is surprising and may not be sustainable given signs that investment is starting to slow. Exports are also likely to weaken in the months ahead. We believe QoQ GDP growth may fall under 8% in the fourth quarter. That would still mean 9% growth for 2011 as a whole, but would set the stage for around 8% GDP growth in 2012, in line with our below-consensus forecast.

**There are no signs of a hard landing in China but, over time, the case for some adjustments to the macro-policy stance is strengthening.** With worries about global growth intensifying and widespread media coverage about the financial hardships facing SMEs, there have been calls for a looser policy stance. The cooling of the economy and likely decline in inflation (see our China Macro Economics note on 13 October), combined with better-contained housing prices, should, over time, create space for a shift in focus to support growth. Since the slowdown in China's economy has so far been moderate – while the moderation of inflation is likely to be gradual and subject to upward risk – it is unlikely that the government will make a bold adjustment to its policy stance. However, in the meantime, the authorities may effectuate some selective easing of some elements of macro policy. The likelihood for that has increased with the particularly low money growth in September, which may have partly been the result of monetary conditions being tighter than the authorities had planned.

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