QUARTERLY DATA RELEASE

China's growth stays strong in March – but will it last?

China's National Bureau of Statistics (NBS) released quarterly data for several key economic indicators including GDP growth and fixed asset investment, providing the first comprehensive account of the country's standing this year. The picture the report paints is a largely resilient economy in the face of building threats both internal and external, though with slowdowns anticipated later in the year.

Real GDP in Q1 2018 grew 6.8% year-on-year (y/y), in line with *Bloomberg'*s market consensus. This matches the growth rate of Q4 2017 and falls just shy of 2017 as a whole, which recorded annual growth of 6.9%, though interestingly exceeds the Chinese government's target for the year of 6.5%. As analysts at **ANZ research** point out, this initial strong performance may provide a cushion for a likely softening of growth in the second half of the year as financial reform policies take effect.

The data also suggested that **consumer confidence** remains robust. **Retail sales** in March grew 10.1% y/y, from 9.4% in January and February combined, beating the market forecast of 9.7%.

Some analysts are more sceptical of the underlying strength of China's growth. Julian Evans-Pritchard of **Capital Economics**, says "of course, the official growth figures need to be taken with a grain of salt as they have been implausibly stable in recent years." By the economic research company's own metric of China's economic activity – the China Activity Proxy (CAP) – Capital believe that **growth most likely slowed** to as low as 4.8% y/y last quarter.

Other aspects of the report were notably weaker, underperforming relative to market expectations. **Industrial output**, for example, slowed to 6.0% y/y from 6.2% in January-February, compared with the market consensus of 6.3%. As expected given recent fiscal tightening, **fixed asset investment** growth also decelerated to 7.5% y/y for the quarter lead by cooling manufacturing and infrastructure investment, after seeing a strong February reading of 7.9%.

Nomura sees these weaker-than-expected figures as signs of **potential weakness** for the rest of the year as deleveraging continues to weigh down on investment, alongside "structural reforms which bring short-term pain, and rising trade protectionism."

The NBS also released the first monthly **urban unemployment rates**, based on government surveys. For January, February and March unemployment stood at 5.0%, 5.0% and 5.1% respectively, in accordance with targets of less than 5.5%.

The rest of the data reflects the ongoing **transition in China's economy towards services**. The **tertiary sector**'s contribution to GDP growth continued **to increase** in Q1 2018, making up 56.6% from 56.3% the same time last year. Furthermore, whilst fixed asset investment slowed down for the economy as a whole, it actually **accelerated** in the tertiary sector, growing by 10% y/y in the quarter from 9.5% in 2017.

BANKING & FINANCE

People's Bank cuts banks' RRR and deposit rates to bolster growth

The People's Bank of China announced a **1% cut in commercial banks' required reserve ratio** (RRR), with the aim of providing a capital boost to what might be a year of **slowing** economic growth. The cut, **effective April 25th**, will allow banks to issue more loans by reducing the minimum amount of liquidity they need to hold in reserve. this will inject up to **$200 billion** into the economy at a time when concerns about China's growth prospects are beginning to take form. Many analysts view the move as reinforcement for growth in light of economic **headwinds coming in H2**.

The PBOC also **relaxed the upper limit to interest rates** for some commercial bank deposits but will not follow through on suggestions made previously that it will lift the cap on all deposit types. Instead, commercial banks will have greater freedom to adjust their certificate of deposit (CD) – financial products available to private and institutional investors that offer higher return rates than the normal high-street savings account – interest rates depending on their size and assets. For China's largest banks, such as **China Construction Bank or Industrial and Commercial Bank of China**, CD interest rates can be raised **as high as 50%** above the central bank's benchmark, up from 40% under the previous system. For smaller banks the ceiling now stands at 55%, up from 45%. Officially, the PBOC had already removed the deposit interest rate ceiling back in October of 2015, however influence from government watchdogs and the **market interest rate pricing self-regulating mechanism** had imposed implicit limits.

GLOBAL POLICY

World Bank to tighten lending to China under new US deal

Changes made by the World Bank to its **lending model** will see China eligible for **fewer** loans as the US pushes for more money to be allocated to poorer countries. The White House reached a deal with the World Bank last week in which the US will contribute a **further $13 billion** to the bank's two principal bodies – **the International Bank for Reconstruction and Development** (IBRD) and the **International Finance Corporation** – on the condition that poorer nations see a larger share of annual loans issued. Countries such as China will be moved into a bracket with **higher interest rates** for wealthier states. China was the largest recipient of IRBD loans in 2017, borrowing **$2.4 billion**, or 11% of the bank's total. As a result of the changes China's voting share at the World Bank is expected to **increase** from 4.45% to 5.7%. The US, however, still holds a decisive voice with 16% of votes.

US-China trade war threatens global confidence and growth, says Lagarde

IMF chief **Christine Lagarde** weighed in on the ongoing US-China trade dispute, warning of the secondary impacts of protectionist measures on global **confidence and investment**. Although the direct impact may appear manageable in the short term, the real threat lies in the "**erosion of confidence**" that stunts global investment and growth. Speaking in Washington ahead of the **IMF and World Bank spring meetings**, Lagarde said: "When investors do not know under what terms they will be trading, when they don't know how to organize their supply chain, they are reluctant to invest." She added: "investment and trade are two key engines that are finally picking up. We don't want to damage that."

TRADE

Beijing appeases US on cars, but hits sorghum imports

China has listed a string of **concessions to the US** with regards to opening up its domestic car industry, only to apply hefty new **tariffs on US sorghum imports**. Beijing said that it plans to make foreign investment into the Chinese auto market much easier, with a lifting of all **current foreign ownership caps** on electric vehicles, shipping and aircraft makers by the close of this year. This will be **extended to commercial vehicles by 2020**. Under the existing model, foreign companies must enter into **50-50 joint ventures** with a Chinese partner firm if they desire to manufacture cars within China. In the same day, the Chinese government placed **178% levies** on one of the US' largest exports to China, sorghum, which was a $1 billion market last year.

China seeks out EU support against US protectionism (Reuters)

In what appears a concerted effort to gather international support against the prospect of U.S. protectionism, China has been meeting with trade representatives from Europe to make its case amid global trade concerns, sources told *Reuters*. Officials from **France, Germany, the UK, Spain, Italy, and the EU** met with **China's International Trade Representative Fu Ziying** for what the sources say were "**non-confrontational**" discussions, although there may have been some "**subliminal threats**" for companies from countries that chose to side too closely with the US. This may be a sign of China's true **unease** about the possibility of a trade war with Washington. The EU's delegate to the talks said that the meeting "**smacks of desperation** because China also knows that the European Union is not going to confront its biggest ally," adding that "China has been very effective at making the most of the free-trading rule book. I don't think anyone in the West is going to leave it to China to set new ones.

China plans to set up free trade zone on Hainan

China has announced plans to establish a **free trade zone** on the tropical island province of Hainan by **2020** and will encourage multinational businesses to set up their headquarters there. The announcement, published jointly by the Communist Party and State Council, comes days after President Xi Jinping's speech at the Boao Forum, a high-profile economic summit held at a resort in Hainan, in which he said China would grant firms **greater economic freedom** on the island. The government will set up an **investment fund** to support the development of a **free trade port** in Hainan by **2025**. As *Xinhua* points out, a free trade port is "the world's most open form of economic zone." The model has been used in other regional hubs including Hong Kong and Singapore. Hainan is famous across China for its sandy beaches and its economy is currently heavily reliant on tourism.

TECHNOLOGY

Western markets deal heavy blows to China's ZTE corp.

The US and UK have both taken action to **limit the influence** of major Chinese telecommunications equipment firm ZTE Corp., on the grounds of national-security concerns. The US Commerce Department has invoked a 7**-year export ban** on ZTE due to the Chinese company's alleged violation of a deal made last year following allegations of trade relationships with **North Korea and Iran**, where ZTE also agreed to pay a **$1.19 billion fine**. For ZTE, currently the **world's fourth largest telecommunications equipment manufacturer**, the ban will prevent sourcing of US components which it heavily relies on to make phones and other products. In a separate move, **UK cybersecurity regulators** issued a warning to UK telecoms companies, urging them to **cease business** with ZTE and use of its products.

China remains sceptical of Qualcomm-NXP deal

A somewhat **negative** statement from China's antitrust regulator cast doubt on the viability of **Qualcomm's $44 billion buyout of NXP Semiconductors**, following the US firm's second refiling of their application. Qualcomm **withdrew** its previous application only four days before the Ministry of Commerce had to make a decision on the deal. The refile will give regulators up to **another 6 months to review the application**. Approval from the Chinese government is the last obstacle required for the deal to go ahead. A spokesman for the Chinese Commerce Ministry, Gao Feng, said that a review of the application found "**related issues that are hard to resolve, making it difficult to eliminate the negative impact**", adding that it had considered possible solutions proposed by Qualcomm to the issue of market competition. There was no mention, however, that the deal will not be approved eventually.

ENERGY

Chinese iron-ore futures soon to be open to foreign traders

Foreign investors will be allowed to buy **Chinese iron-ore futures** from **May 4th**, which if successful could provide a new local **benchmark** for the commodity. Guidelines set out by the **Dalian Commodity Exchange**, the only Chinese exchange selling iron ore futures, say foreign investors will be able to trade only through a **futures-company member**, although this could be on behalf of an overseas broker. Last year **$2.72 trillion worth of futures contracts** were traded on the Dalian exchange.

Brazil's Petrobras approaches landmark deal with China's CNPC over oil refinery (Reuters)

Petrobras is in the final stages of negotiations with China National Petroleum Corp. on a deal that would **swap Chinese investment in a Brazilian oil refinery for crude oil imports**, sources told *Reuters.* This would be China's **first** oil refinery operation in either South or North America. From the deal, China is expected to receive stakes in oil fields in Brazil's south-eastern Campos basin, as well as access to the new Comperj refinery. One of the sources with knowledge of the matter told *Reuters*: "We are going to have a deal, but it is complex. We should have an integrated solution." China has been fostering **a growing interest** in Brazil's natural resources in recent years, which has made its energy sector much more open to foreign investors. In 2016, for instance, **Comperj signed a $10 billion deal with China Development Bank**, offering oil in exchange for Chinese investment.