Commentary on the August 2022 CKGSB Business Conditions Index

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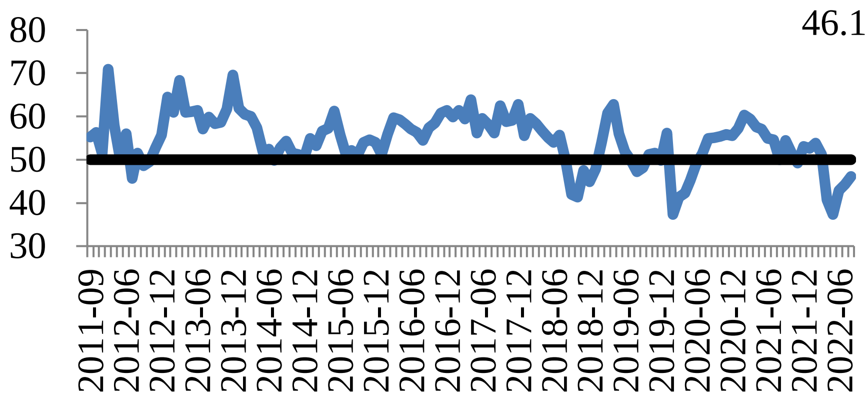
In August, the “CKGSB Business Conditions Index” (BCI) rose to 46.1 from 44.3, a small improvement on prospects in July, but still below 50.0. This reflects expectations of growth among business leaders but shows that China’s economy is still on an extremely weak footing.

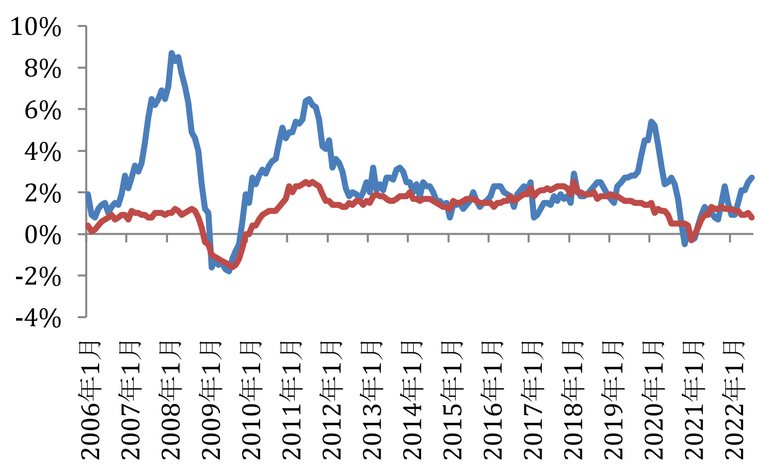
Figure 1 **Business Conditions Index (BCI)**



Source: CKGSB Case Center and Center for Economic Research

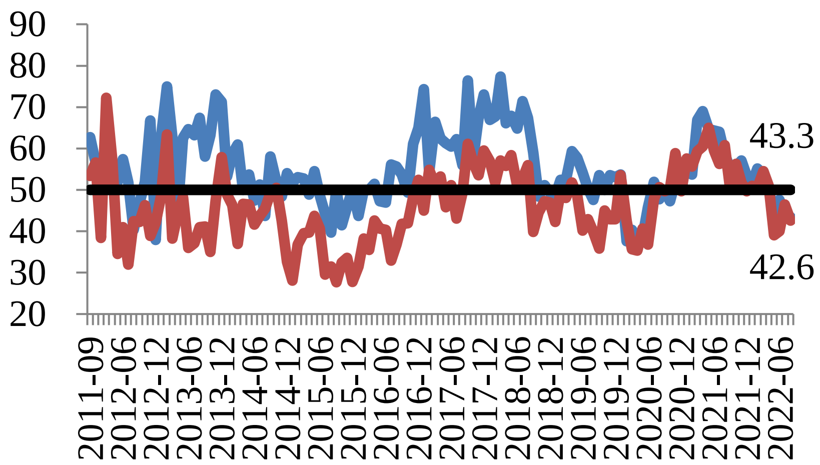
The following is a detailed commentary on the macroeconomic situation this August. On the positive side, both official data and our survey show that China’s risk of inflation is very low at present (Figure 2, Figure 3), giving the government room to stimulate the economy using a series of measures. In August, it is worth noting that crude oil prices worldwide have risen significantly (Figure 4). Despite the unfavorable context, they have fortunately remained relatively stable.

Figure 2 **Consumer Price Index**



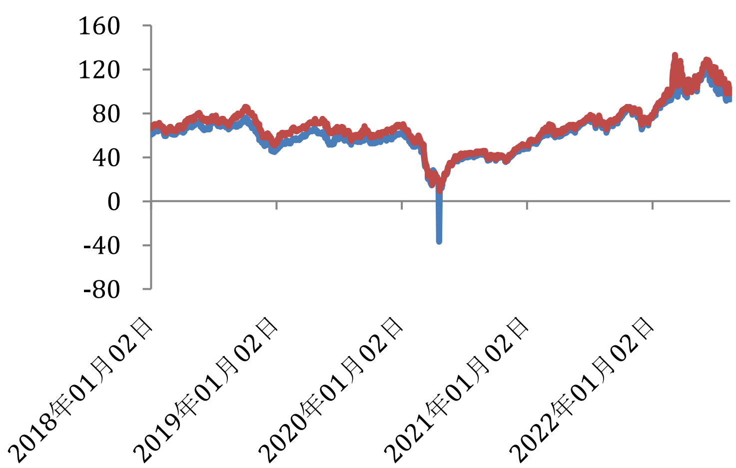
Blue: CPI, Red: Core CPI (excluding food)

Figure 3 **CKGSB BCI CPI**



Blue: BCI Consumer price index; Red: BCI Producer price index

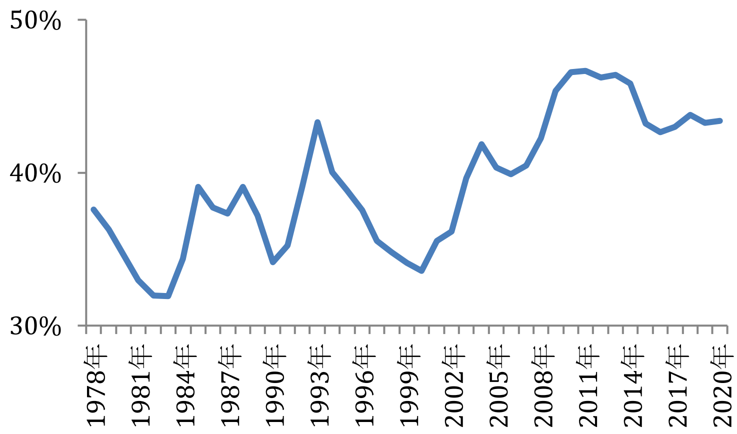
Figure 4 **Crude Oil Prices**



Blue: Crude Oil, West Texas Intermediate; Red: U.S. Brent (crude oil priced in USD per barrel)
Source: CEIC

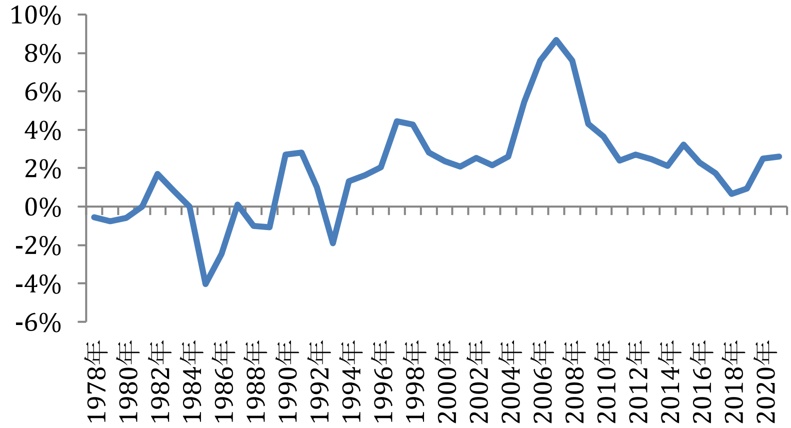
Second, long-standing structural problems in the Chinese economy may be worsening. It is an indisputable fact that China's economy has had serious structural problems for a long time. Of the large number, the most important is that economic growth relies too much on investment (Figure 5) and net exports (Figure 6), while household consumption has hovered at a low level for a long time (Figure 7).

Figure 5 **Investment as a portion of GDP in China**



Line: Investment/GDP

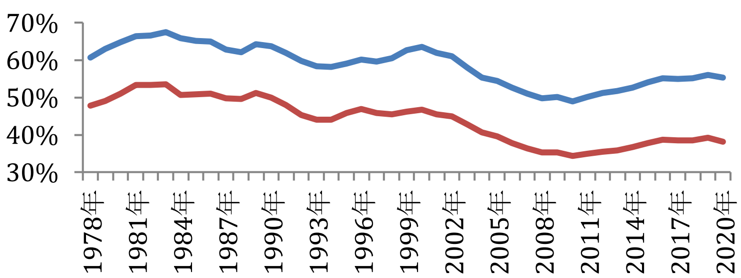
Figure 6 **Net exports as a portion of GDP**



Line: net exports/GDP

Source: CEIC

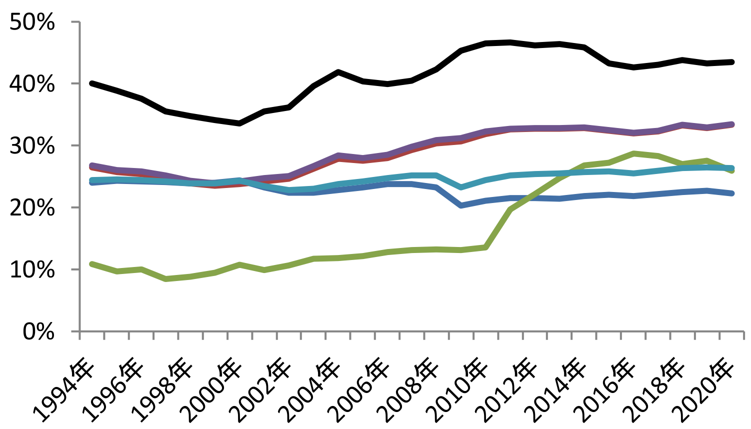
Figure 7 **China's consumption expenditure as a portion of GDP**



Blue: Total consumption expenditure/GDP; Red: household consumption expenditure /GDP

According to CEIC data, China's proportion of investment in GDP has grown substantially since 2000, reaching a high of 47% at its peak. In 2020, this indicator was at 43%. In contrast, the ratio of household consumption expenditure to GDP has fallen sharply since 2000. The indicator was only 34% at its lowest, and was still only 38% in 2020. Net exports as a share of GDP fell sharply to close to 9% of GDP, but rose again after 2018. Conclusions are only formed from comparisons when analyzing this kind of data. China is too dependent on investment and net exports because, unlike other countries, China has a unique economic structure. Let us take the example of investment to illustrate the problem. It is clear to see that in the ratio of investment to GDP (Figure 8), China leads the field.

Figure 8 **National average incomes compared**

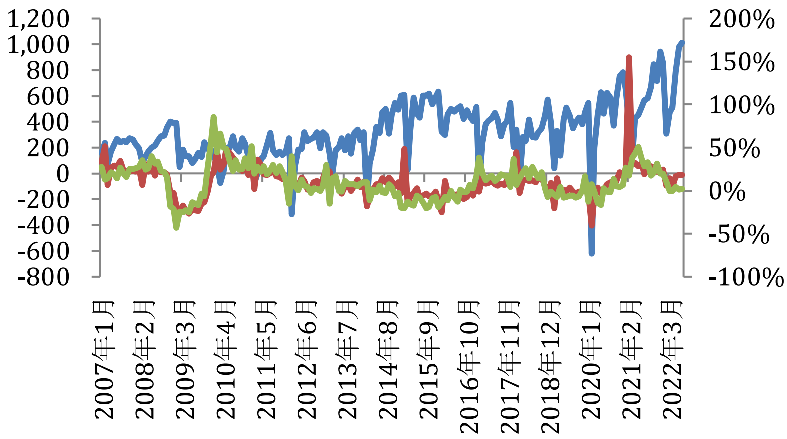


Blue: High income countries; Red: medium to low income countries; Green: Low income countries; Purple: Medium income countries; Light blue: World average; Black: China

Source: World Bank

China's structural issues might be worsening too. In Figure 9, we can see that China's trade surplus is far higher than it was two years ago. In July 2022, this measure exceeded USD $100 billion for the first time. Net exports are a GDP growth driver, so how should we view the situation? Net exports are equal to exports minus imports. Since the beginning of 2021, year-on-year growth rates of both exports and imports have fallen, but the decline in the year-on-year growth rate of imports is higher than that of exports. As a result, this has led to a substantial increase in the trade surplus. Imports are often related to domestic demand. Based on this, we can tell that domestic demand in China has weakened.

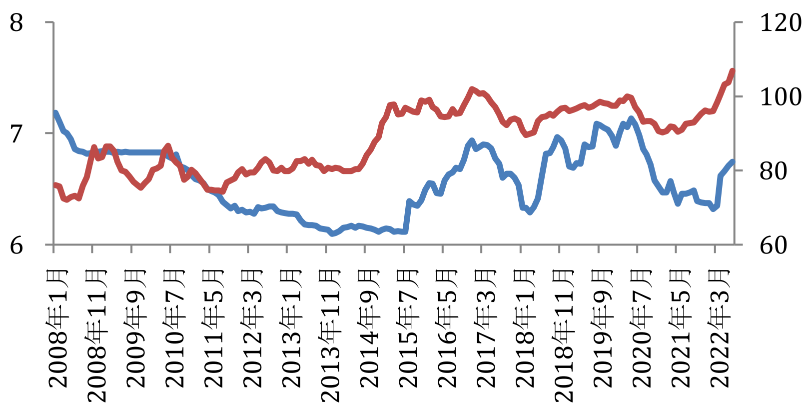
Figure 9



Blue: Trade surplus (USD 100m – left axis); Red: Export growth (y-o-y); Green: Import growth (y-o-y) Source: CEIC

And as the US Federal Reserve raised interest rates and the US dollar has gained strength, the RMB has fallen (Figure 10), which is good for exports and bad for imports. This also bolsters the trade surplus.

Figure 10 **USD to Dollar Exchange and US Dollar Index**

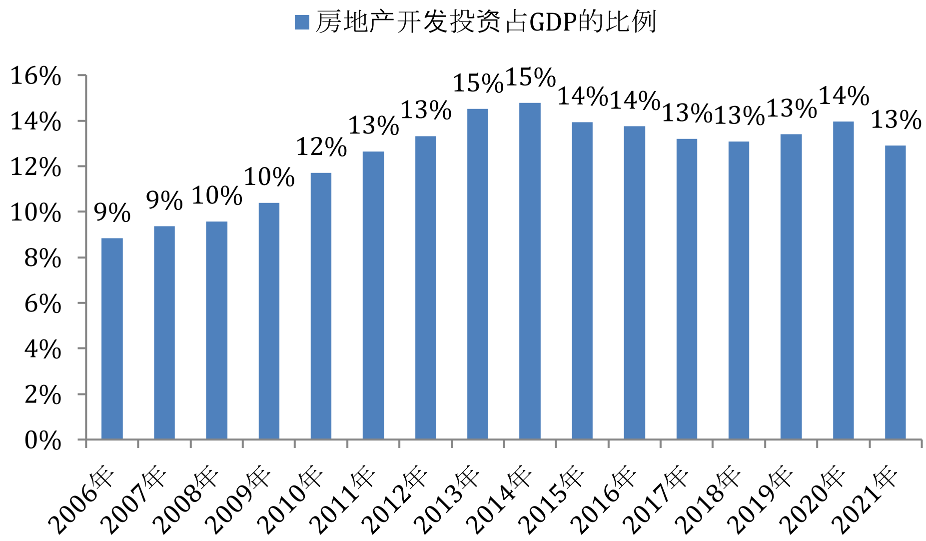


Red:; Green:;

Note: * The U.S. dollar index is a measure of the overall exchange rate of the U.S. dollar. The higher the value, the stronger the exchange rate. ** The U.S. dollar index had a March 1973 value of 100.

As everyone in the country knows, real estate is one of the most important industries in China (perhaps the only one), and the ratio of real estate development investment to GDP has been above 10% for a long time (Figure 11). According to a World Bank report this year, considering upstream and downstream industries, the output value of real estate and its associated industries accounts as much as 30% of China's GDP.

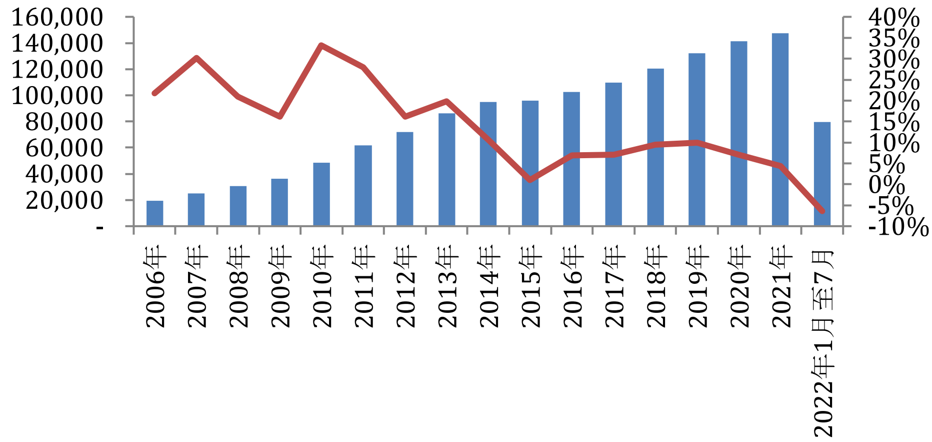
Figure 11 **Real estate developments as a portion of GDP**



Source: CEIC

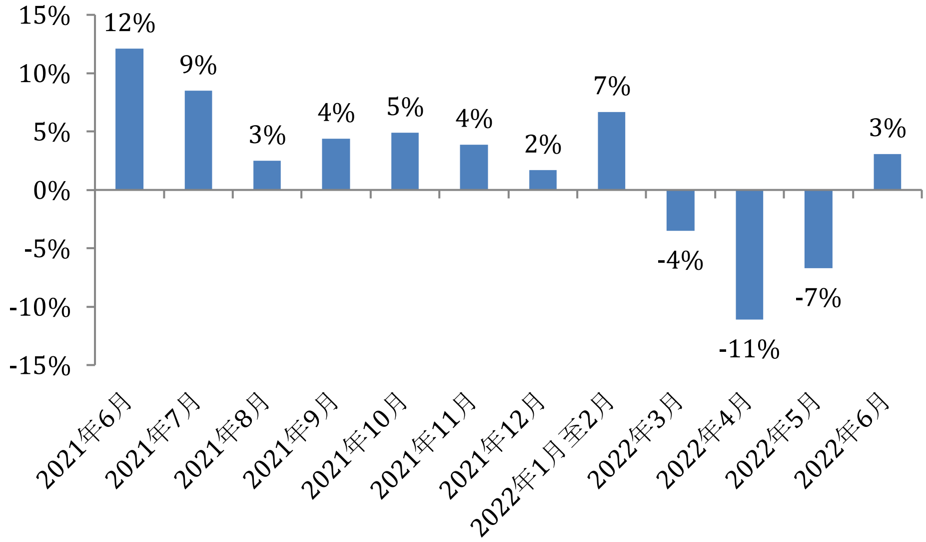
Over the past few years, although home prices have fluctuated, the general direction has been up, and sometimes steeply, which has given people a strong expectation that real estate may never fall. You can never lose if you buy a house, people said. However, controls in the past few years have made life for real estate developers harder and harder. Last year, leading real estate group Evergrande had its financing lines severed, abruptly ending work at building sites across the country. According to media reports, over 500 of Evergrande's 800-plus projects across China were suspended. Evergrande was not the only one. Its competitor Sunac also suffered from insufficient funds. The wake-up call alerted people to the fact that real estate investment had plummeted (Figure 12). In turn, the sense people have that house prices will only rise and never fall have been shattered.

Figure 12 **Real estate investment plummets**



The slump in real estate has caused a slump in investment, which has had a significant negative impact on China's economy. In terms of consumption, the economy is also suffering (Figure 13). According to data from the National Bureau of Statistics, in the first half of 2022, the total retail sales of consumer goods was 21,043.2 billion yuan, a year-on-year decrease of 0.7%.

Figure 13 Retail sales of consumer goods



Bars: total retail sales of consumer goods
Source: Chinese National Statistics

To sum up, China's economy has indeed entered a difficult period. In order to stimulate economic growth, local governments have begun to relax the rules of buying property again. This is simply a case of taking real estate as a means of regulating economic development. This way, residents' expectations for real estate will always fluctuate greatly, which is not conducive to the long-term development of the economy. Therefore, we should focus on the long-term and implement reform measures to promote the healthy development of the sector, and escape from the quagmire.

This is a commentary on the CKGSB BCI report for August 2022 to which you are welcome to refer for detailed statistics. Do not hesitate to contact the BCI team by email for the accompanying BCI data report.

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