

# China's Economy Gains Speed, but Challenges Loom

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By Annie Whitehurst

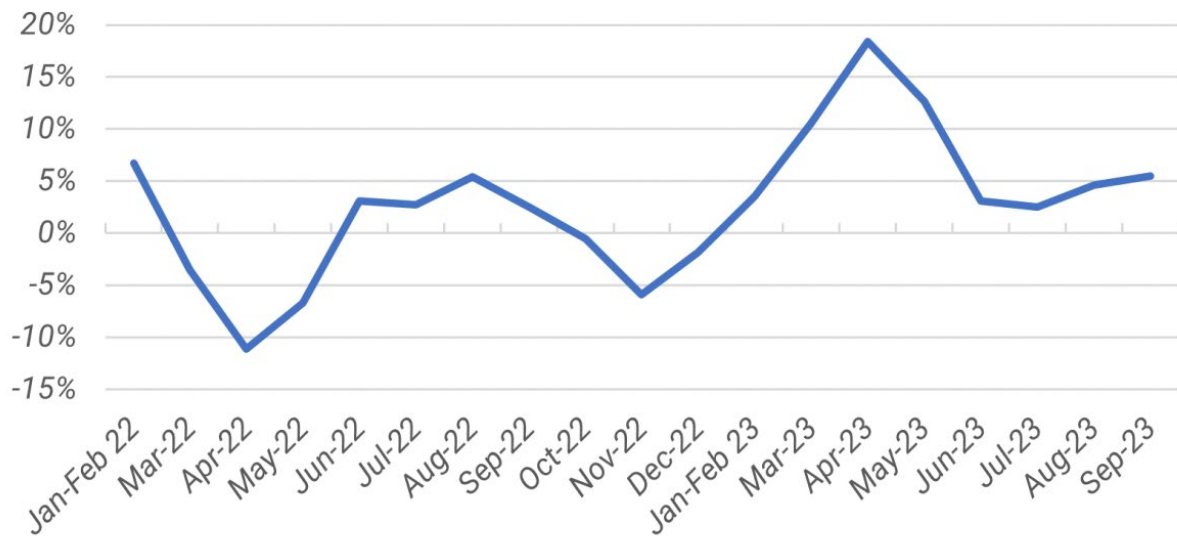
- *China's third quarter economic performance put the economy on track to reach its 5 percent annual growth target, but systemic economic problems complicate longer term growth prospects.*
- *Retail sales and industrial output both boosted growth in the third quarter, though concerns over deflation persist, which could further stymie demand and industrial profits.*
- *Next week the government is expected to hold the twice-a-decade National Financial Work Conference, where more details could emerge on China's plans to address the property sector and local government debt challenges.*

China's third quarter economic data [exceeded](#) expectations, growing 4.9 percent year-on-year. According to China's National Bureau of Statistics, this growth puts China on track to reach its 5 percent annual economic growth target, provided fourth quarter growth [reaches](#) at least 4.4 percent. Although parts of the economy showed signs of a recovery, systemic problems persist, which could complicate long term growth prospects.

## Mixed signs of quality growth

While the first quarter [showed](#) emerging signs of a post-COVID recovery of consumer spending, second quarter retail data [remained](#) tepid. Third quarter data paints a somewhat improved picture. In September, total retail sales of consumer goods increased by 5.5 percent year-on-year, marking an increase of 0.9 percent from August.

## Year-on-Year Growth Rate of Retail Sales of Consumer Goods

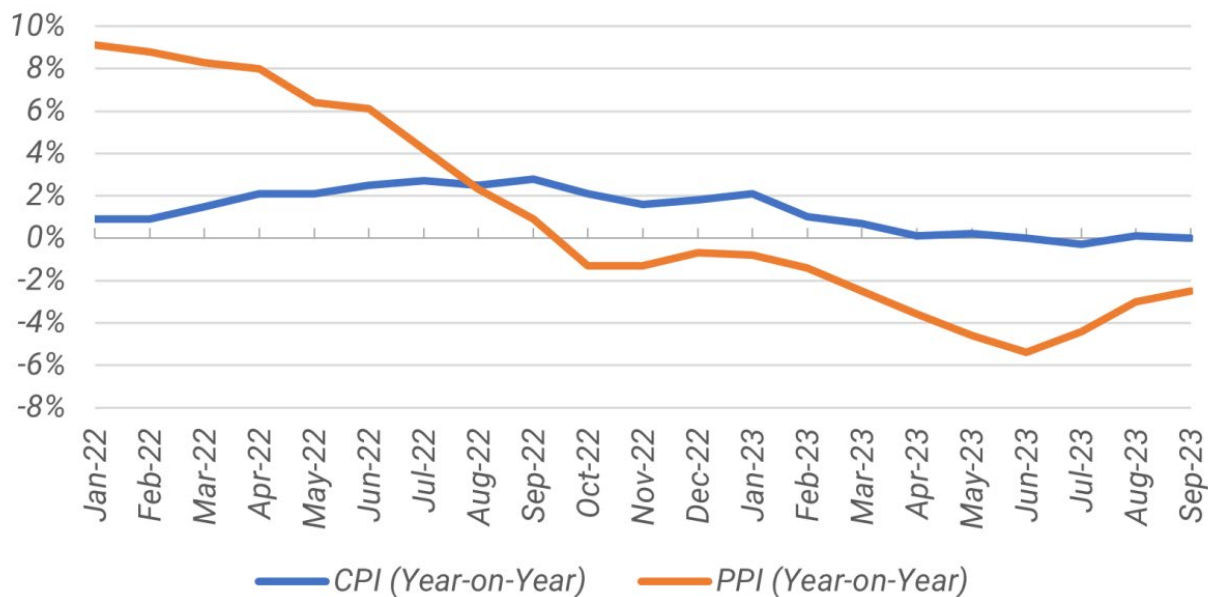


While China has not introduced a large-scale consumer stimulus package, the [National Development and Reform Commission](#) and the [Ministry of Commerce](#) issued piecemeal measures to boost consumption in the late summer, which appear to have helped stimulate demand. Some economists have long [argued](#) that Beijing must recalibrate its economy toward consumption and away from unproductive investment in infrastructure and real estate.

In September, value-added industrial output, which [measures](#) the output of businesses with revenues of at least RMB 20 million per year, grew 4.5 percent year-on-year. This [remained](#) unchanged from August, potentially indicating stabilization. *Caixin* noted that manufacturing and state-owned enterprises [were](#) key drivers of this growth. As a further sign of stabilization, in September, China's manufacturing purchasing managers' index (PMI) [was](#) 50.2, reaching expansion territory for the first time since March.

Despite moderate retail and industrial output performances, concerns over deflation remain, with the consumer price index (CPI) remaining unchanged and the producer price index (PPI) [falling](#) 2.5 percent year-on-year in September. If deflation takes hold, demand and industrial profits would likely be dampened, further eroding China's economic outlook, particularly if additional stimulus is not issued.

## CPI and PPI



### Continued challenges remain in the property sector

Meanwhile, in the first nine months of the year, fixed asset investment increased 3.1 percent year-on-year. Investment in high tech industries appears to be a key driver of this growth, with manufacturing of aviation-related equipment and medical equipment growing 20.7 percent and 17 percent, respectively. Investment in high technology remains a key priority of the government, particularly amid rising strategic technology competition between the United States and China.

However, compared to the first six months of the year, fixed asset investment [declined](#) slightly from 3.8 percent year-on-year. The decline is largely driven by the continued downturn in China's property sector, with investment in real estate development decreasing by 9.1 percent year-on-year for the first nine months of the year. China's new home prices also [continued](#) to decline in September, further stoking concerns for the sector, which [accounts](#) for up to 30 percent of the country's GDP by some estimates. As investment and home prices continue to fall, local governments [face](#) decreased revenue from land sales.

### More details on China's plans to address debt could emerge next week

The property sector faces a host of challenges ahead, with Country Garden reportedly entering into [default](#) on dollar bonds this week after failing to make payments. The government so far has not indicated an inclination to bail out developers. In August and September, China [issued](#) a round of targeted measures to stabilize the property sector, though they appear to have had a limited effect in addressing the systemic debt issues plaguing developers and local governments.

At the July Politburo meeting, officials [pledged](#) to resolve the debt risks of local governments, but a plan has yet to be issued. Last week, *Reuters* [reported](#) that state-owned banks have apparently been told to restructure local government debt, though specific details remain unclear. More details [could](#) emerge at the twice-a-decade National Financial Work Conference, which is reportedly expected to be held next week. China's property sector and local government debt challenges are expected to be at the top of the agenda.

### **Slower growth likely ahead in 2024**

In addition to managing the property sector downturn, local government debt, and the transition to a consumption driven economy, China also faces the issue of youth unemployment. China [stopped](#) publishing data on youth unemployment in the summer after reaching a high of 21.3 percent in June. Amid these headwinds, the IMF [reduced](#) China's 2023 economic growth from 5.2 to 5 percent and further downgraded China's 2024 forecast from 4.5 to 4.2 percent.

China's leaders are expected to set the economic agenda for 2024 at the annual Central Economic Work Conference in December. Boosting domestic demand, encouraging technological self-sufficiency, and addressing local government and property sector debt will likely be key policy focuses of the conference. There are very few signs that China's leaders will issue a large-scale consumer stimulus. China has instead [opted](#) for a piecemeal approach to boost consumer demand and support private sector growth, along with [turning](#) to the familiar playbook of increasing infrastructure spending to propel growth.

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