



# China's Economy Faces Renewed Pressures

Property sector weakness weighing on confidence.

August 2023

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## KEY INSIGHTS

- China's economy is slowing faster than expected, and further weakness is possible amid a flurry of negative developments in the property and trust sectors.
  - We expect further monetary policy easing measures from China's central bank to support the economy.
  - Fiscal support measures have been incremental so far, and if this trend continues, we believe it will take time to revive the confidence of consumers and businesses.
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China's economy is slowing—and at a faster pace than anticipated. A flurry of negative developments recently in the property and trust sectors could result in further weakness in the world's second-largest economy. Downside risks are growing, threatening to create negative feedback loops amid weak confidence and challenges in the manufacturing sector and labor markets.

In an effort to support the economy, the People's Bank of China has cut key policy rates, and we expect more monetary policy easing to come in the weeks and months ahead. But with credit demand low, it's uncertain how effective easing measures will be.

On the fiscal front, the response from authorities has been incremental so far, and if this approach continues, it's going to take time to revive the confidence of consumers and businesses. With the goal of putting the economy on a sustainable long-term path,

the government appears, to date, reluctant to do a “big bang” type stimulus like it has done in the past, namely in 2015/2016. But if the challenges continue to deepen, the resolve of the Chinese authorities on this front will likely be tested.

Even if we see a number of defaults among China's private sector property developers in 2023, the risks of a systemic financial crisis in China appear low. Following the government's financial deleveraging campaign that began in 2017, Chinese banks have been quietly strengthening their balance sheets.

At the same time, China's riskier “shadow” banking system, of which trusts are a part, is smaller in terms of relative importance today than it was five years ago. There has been a wave of regulations to contain the industry and develop more formalized channels of financing. As such, the key risks in the financials sector remain more at the periphery of the financial system and potentially resolvable through timely regulatory interventions.

Against this backdrop, we believe that it's important to continue monitoring developments in the property sector and possible spillovers to other sectors, which could lead to a broader loss of confidence in the financials sector among consumers and businesses.

So far, the emerging market economies are showing resilience in the face of China slowing, which is encouraging. Going forward, it will be important to watch the performance of commodity exporters and Asian manufacturers, as these are typically most exposed to China's economy. Commodity demand

has continued to be supported globally even as China slows amid a structural shift toward green energy and infrastructure buildouts.

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