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China Flash

Another month of weak domestic demand

Key takeaways: With the risk of sounding like a broken record, China's data batch for July highlighted the two-speed economy as consumer and investment demand disappointed again, while exports released last week shows continued strong export growth. Today's report underlines the need for more policy support in the second half, already hinted at by the Politburo in late July.

Details:

- **Retail sales growth dropped from 1.0% y/y to 0.6% y/y (consensus 1.5% y/y).** Consumer goods demand continues to suffer from low household confidence due the ongoing housing crisis and weak employment demand. Lower trade-in subsidies this year have also hit car sales and durable goods demand.

- **The housing crisis continues but with a few (small) rays of light.** New home prices showed further declines with another drop of 0.18% m/m in July after -0.15% m/m. However, adjusting for seasonality new home prices look a bit better as they show prices are falling at a slower speed (chart 6). Existing home prices declined 0.31% m/m on a seasonally adjusted basis.

  In the past months, I pointed to tentative rays of light from a stabilisation in home sales, albeit at a low level. This continued to be the picture in July (chart 2). Construction starts are still trending lower, though, and has reached very low levels suggesting that new construction is running below home sales, which in turn helps to reduce housing inventories. Lower inventory levels are needed to eventually see a stabilisation in home prices. Maybe a story for 2027?

- **Fixed asset investments disappointed again this month** with a drop from -18% y/y year-to-date to -19.2% y/y year-to-date (consensus -18.9% y/y year-to-date). Outside high-tech investments, companies are holding back building new capacity as overcapacity is prevalent in many areas. A drop close to 20% in property investments also weigh on the total.

- **The unemployment rate increased from 5.0% to 5.2%** but has moved broadly sideways for a couple of years between 5 and 5.4%. As highlighted before, it is a poor labour market indicator, though, and surveys of labour demand from both PMI data and CKGSB (chart 11) points to a weak labour market.

The data shows that China is still caught in a negative spiral in the domestic economy where lower home prices erode household wealth and keep household confidence low. Weak consumer spending hurts employment growth – which in turn hurts incomes and thus spending. **Until we see a stabilisation and moderate improvement in housing, I find it unlikely to see a turn in consumer spending**. **However, once this happens a more virtuous cycle could be triggered** where consumers dare to lower their high savings rate, which in turn would create more employment and underpin consumption further. This will take time, though. My **best guess is we the first steps in such a recovery during 2027 but it may take even longer**. China is still in a painful transition de-toxing from old growth drivers (especially housing) while creating new drivers centred around technology and – eventually – consumption.

Chart 1: Consumer goods demand a key weak spot in Chinese economy

Source: Macrobond, NBS, Danske Bank

Chart 2: Housing crisis continues but signs of stabilisation in home sales

Source: Macrobond, NBS, Danske Bank

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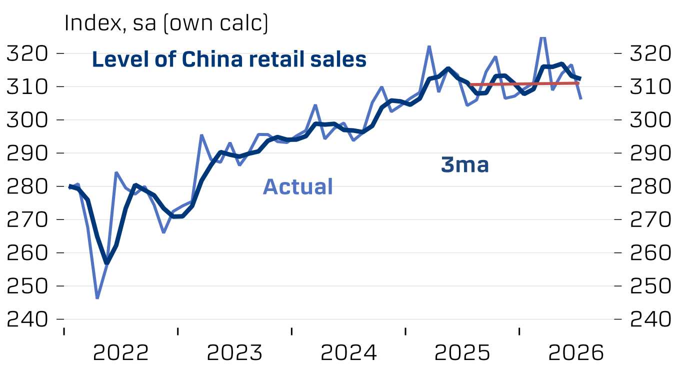
Chart 3: Level of retail sales show sideways spending



Source: Macrobond, NBS, Danske Bank

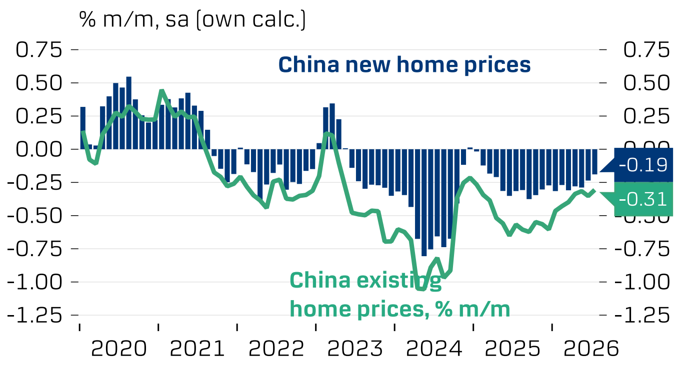
Chart 4: Retail sales even weaker than PMI employment points to

Source: Macrobond, NBS, Danske Bank

Chart 5: Construction starts at very low levels

Source: Macrobond, NBS, Danske Bank

Chart 6: New home price declines easing when adjusted for seasonality

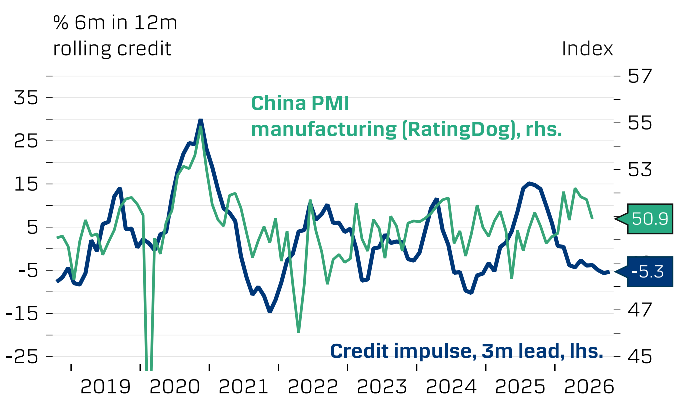


Source: Macrobond, NBS, Danske Bank

Chart 7: Industrial production growth moving in 4-6% range

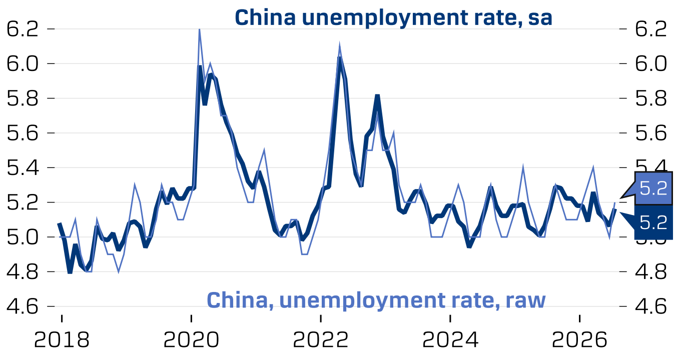
Source: Macrobond, NBS, Danske Bank

Chart 8: Weak credit impulse



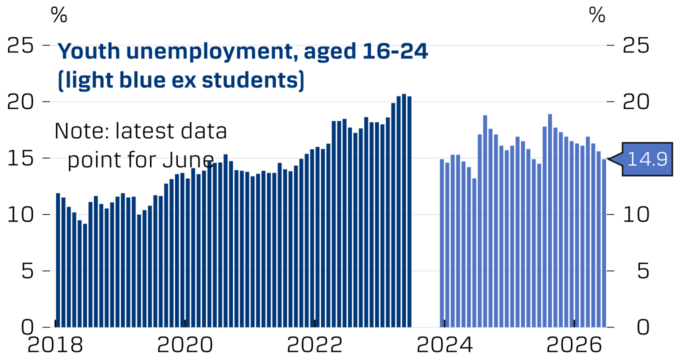
Source: Macrobond, S&P, Danske Bank

Chart 9: Official unemployment rate up in July



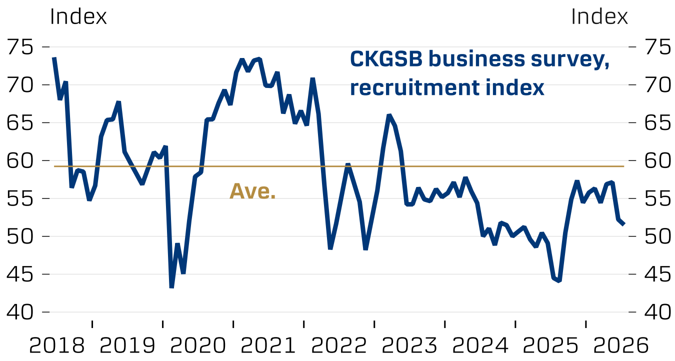
Source: Macrobond, NBS, Danske Bank

Chart 10: Youth unemployment lower lately, may rise in July/August as new graduates enter labour market



Source: Macrobond, NBS, Danske Bank

Chart 11: CKGSB shows weak labour demand



Source: Macrobond, CKGSB, Danske Bank

Chart 12: Exports (released last week) still strong

Source: Macrobond, GAC, Danske Bank

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