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CHINA ACTIVITY MONITOR

Service sector activity picking up

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- **Construction slowed well before the rest of China's economy in 2008 and it has since led the recovery. But our China Activity Proxy (CAP) suggests that recovery is now entrenched across all sectors of the economy, including services.**
- We launched the CAP at the beginning of May to provide an alternative to China's widely-questioned official GDP figures. It is based on a set of relatively low profile indicators chosen to reflect activity across a wide section of the economy. (Full details are in our *Asian Economics Focus*, "Can China grow by 8% this year?", 6th May.) As the Chart below shows, the CAP has a similar profile to the official GDP growth numbers, but it diverges in periods when many observers have questioned the accuracy of the official data. For example, the CAP shows a deep slowdown in the late 1990s – when official figures suggested growth was steady despite a wave of closures in industry – and it suggests activity was faster than shown in the official figures before the policy tightening of 2004.
- More recently, the CAP supports the view that the economy slowed much more than was officially acknowledged in Q4 2008 and Q1 2009. But it has since pointed to a sharp rebound. Indeed, the CAP suggests the latest official GDP figures (which showed 8.9% growth in Q3) understate the extent of China's recovery.
- **The October data suggest that sources of Chinese growth are broadening**. In the initial months of the recovery, the pick-up in activity was led by stimulus-related construction. Of the five components that we use to construct the CAP, floor area under construction continues to grow fastest, both in absolute y/y terms and relative to the trend growth of the last five years. (See Charts on following page.) However, **for the first time since July 2007, each of the other four components in the CAP is now also growing faster than its average pace over the past five years**.
- The next strongest turnaround has been in domestic freight transport, which we take as a broad measure of activity across the economy. Growth of shipments through China's ports remains steady. The two remaining components, passenger transport and electricity output have recently accelerated sharply. The strength of electricity output is partly due to base effects, but not that of passenger transport, which did not tail off until early 2009. **This is an encouraging sign that consumer confidence and service sector spending is fairly strong**.
- Base effects will have a big positive impact on the y/y growth rate in the months ahead. Apart from passenger transport, each of our other measures weakened substantially in November 2008. **But this should not distract from the fact that m/m growth, as proxied by our seasonally-adjusted version of the CAP, also remains strong**.

CAPITAL ECONOMICS

China Activity Charts

Chart 1: China Activity Proxy (CAP) & GDP

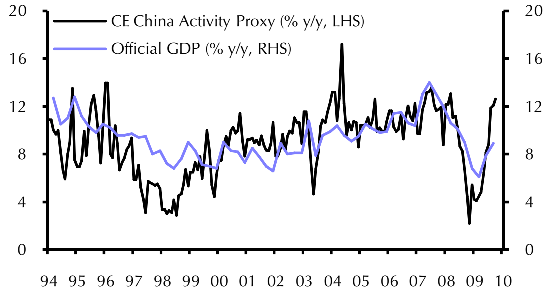


Chart 2: CAP & Industrial Output (seas. adj., vol., % 3m/3m)

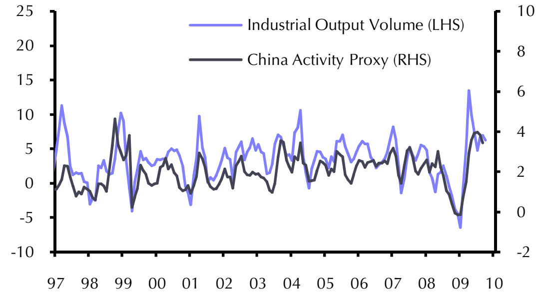


Chart 3: Floor Area Under Construction

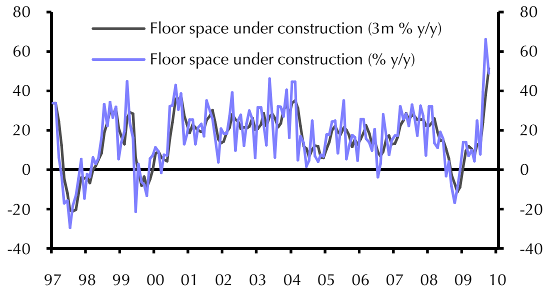


Chart 4: Domestic Freight

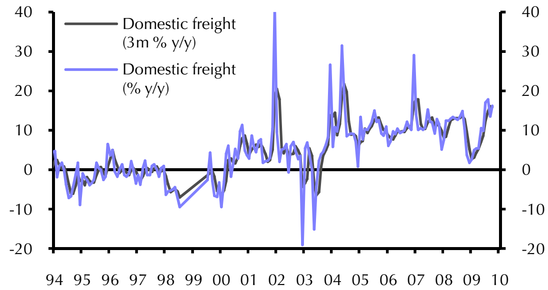


Chart 5: Seaport Freight

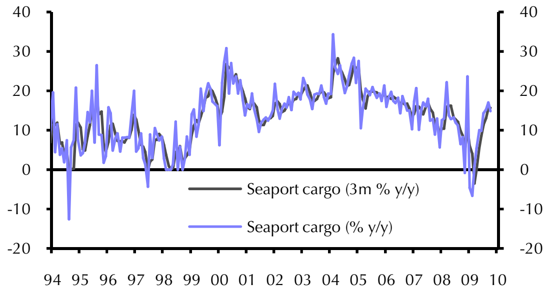


Chart 6: Passenger Transport

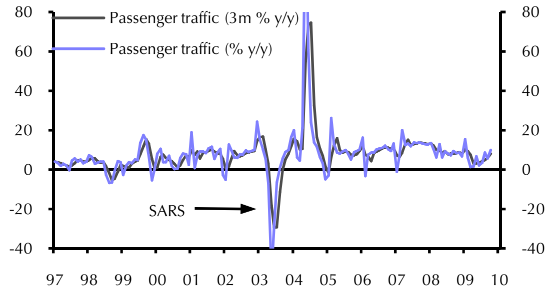


Chart 7: Electricity Output

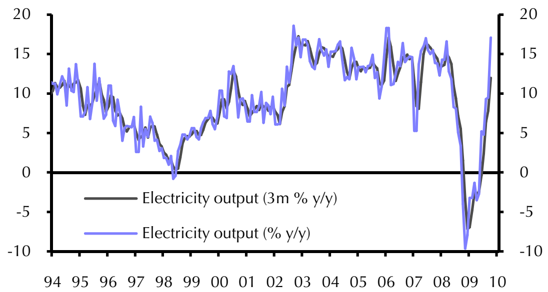
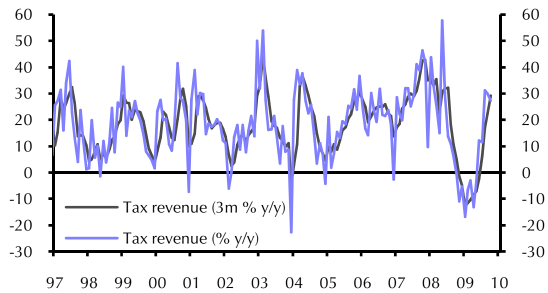


Chart 8: Tax Revenue (not a component of the CAP)



Sources – CEIC, Thomson Datastream, Capital Economics

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