

## Macro Monthly Letter

AUGUST 2021

# China's moderate slowdown

**Cecilia Machado**  
Chief Economist

**Felipi Bruno**  
Economist

**Nicolau Curi**  
Economist

**Gabriel Maciel**  
Intern

**Joel Makangila**  
Intern

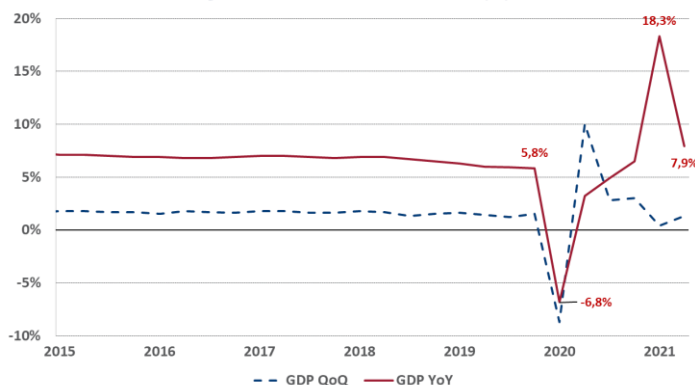
**Luisa Curcio**  
Intern

**Marco Abreu**  
Intern

Global growth forecasts for 2021 are being revised as economic activity resumes. The IMF continues to project 6% overall, but its forecasts for specific economies have recently changed, mainly to reflect the latest developments in the pandemic (vaccine supplies, the pace of vaccination, and novel variants such as Delta), as well as government support via fiscal and monetary policy. In its latest forecast, it revised down the growth outlook for the emerging economies. In the case of China, its forecast was lowered by 0.3 of a percentage point (from 8.4% to 8.1%) in line with first-half data showing economic activity decelerating moderately.

Compared with the first quarter, when year-over-year growth reached 18.3%, second-quarter growth of only 7.9% was eye-catching but widely expected because first-quarter growth mostly reflected the depressed base in first-quarter 2020, when the impacts of the pandemic were at their worst in China. Assuming Chinese growth returns to the pre-pandemic level or a little lower at 5%-5.5%, the coming quarters will see a further slowdown.

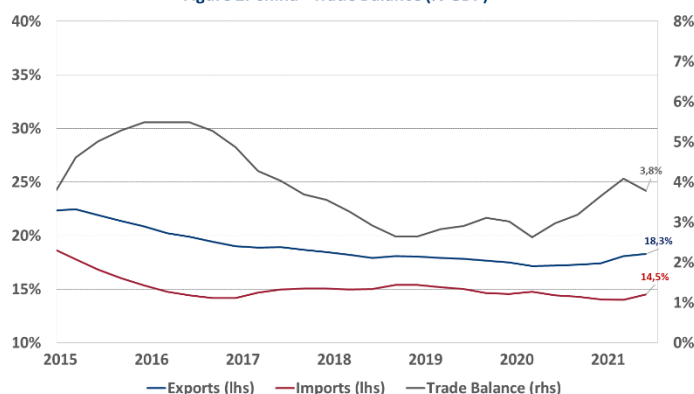
Figure 1: China - Real GDP Growth (%)



Source: CEIC

On the demand side, one of the main components of growth – exports – continued to perform well with no sign of decelerating. In June, exports significantly outperformed market expectations, with growth of 32.3% year-over-year. Imports also exceeded expectations, growing 36.7% year-over-year, and signaling a recovery by domestic demand. Both exports and imports continued to grow year-over-year, with the trade surplus falling very moderately.

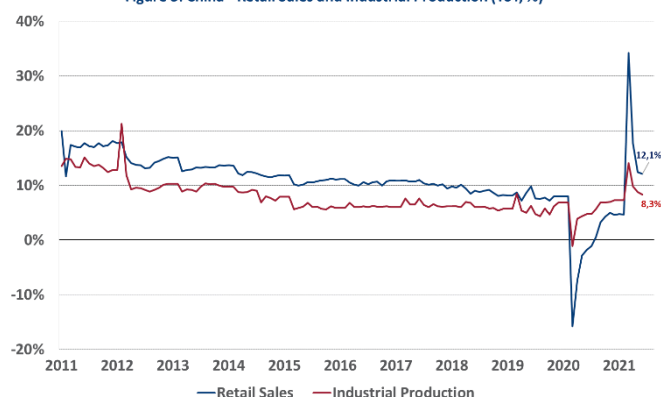
Figure 2: China - Trade Balance (% GDP)



Source: CEIC

A breakdown of the growth points to consumption as its main driver, as expected, given that consumption was most affected during the pandemic. Savings increased as a result of the lack in spending on recurrent items such as services. The recovery in household consumption was also evidenced by retail sales growth of 12.1% year-over-year in June. While this was 0.3% lower than in May, retail sales grew 4.9% once the base effect is accounted for (i.e., using a two-year average), which is 0.4% more than in May. Consumption accounted for about 75% of the second-quarter growth of 7.9%.

Figure 3: China - Retail Sales and Industrial Production (YoY, %)

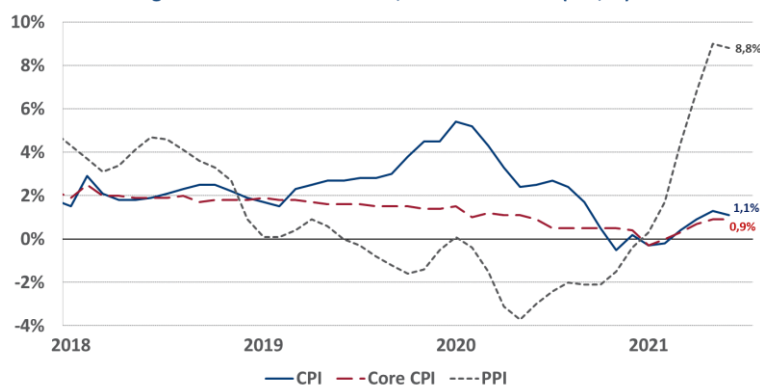


Source: CEIC

There are, however, more pessimistic views regarding China's economic deceleration. Some analysts are wondering whether the pace of growth – and even other indicators of activity, such as retail sales – will return to pre-pandemic levels, given the policy of very low tolerance of outbreaks involving novel variants, especially mobility restrictions. More importantly, recent data suggests mobility patterns may have changed in a more structural manner, with less propensity for travel or consumption away from home. If so, the transition to a more consumer-driven economy may slow down.

With regard to monetary policy, the PBOC (China's central bank) recently lowered the reserve requirement ratio (RRR) by 50 basis points to 8.9%, fueling liquidity in the economy. The cut in the RRR is a strong sign that the PBOC may have embarked on a fresh easing cycle, in contrast with the rest of the world, where monetary authorities are considering rate hikes in response to the high inflation that is accompanying the economic reopening. China's inflation is below its target, with well-anchored inflation expectations and the CPI on 1.1% year-over-year. As for the other monetary policy instruments, it is too soon to know whether there will be changes. Fiscal, monetary and credit policies could become more stimulatory in response to additional deceleration.

**Figure 4: China - Inflation CPI, CPI Core and PPI (YoY, %)**



Source: CEIC

In Brazil, alongside concerns over the risk of deceleration in China, there are own fiscal risks, in light of several important reforms proposed by the government that would increase public spending. They include the second stage of the tax reform and the reformulation of the Bolsa Família cash transfer program, entailing an increase in payouts and coverage. Adding uncertainty to the outlook, expenditure is expected to rise by some R\$ 89 billions in 2022 owing to the court-ordered payment of federal debts (*precatórios*). In the context of high inflation, we have revised up our forecast for the Selic rate to 7.5% in 2021 and in 2022.

ECONOMIC FORECASTS	2016	2017	2018	2019	2020	2021F	2022F
GDP Growth (%)	-3,3%	1,3%	1,3%	1,1%	-4,1%	5,3%	2,2%
Inflation (%)	6,3%	2,9%	3,7%	4,3%	4,5%	7,1%	3,6%
Unemployment Rate, SA (eoy, %)	12,6%	12,4%	12,2%	11,7%	13,9%	13,0%	13,0%
Policy Rate (eoy, %)	13,8%	7,0%	6,5%	4,5%	2,0%	7,5%	7,5%
<b>External Accounts</b>							
Trade Balance (US\$ bn)	48	67	53	48	51	69	46
Current Account Balance (US\$ bn)	-23	-10	-42	-51	-13	-2	-15
Current Account Balance (% of GDP)	-1,3%	-0,7%	-2,2%	-2,8%	-0,9%	-0,1%	-0,9%
<b>Fiscal Policy</b>							
Fiscal Primary Balance (% of GDP)	-2,5%	-1,7%	-1,7%	-1,2%	-10,0%	-2,0%	-1,1%
Government Gross Debt (% of GDP)	69,4%	73,7%	75,3%	74,3%	88,8%	82,3%	82,9%

This report was prepared by Banco BOCOM BBM and is distributed free of charge with the sole purpose of providing information to the market. Any forecasts, estimates, and certain information contained herein may be based upon proprietary research and should not be interpreted as investment advice or recommendation. Although the information contained herein was prepared with utmost care and diligence, in order to reflect the data at the time in which they were collected, Banco BOCOM BBM cannot guarantee the accuracy thereof. Banco BOCOM BBM cannot be held responsible for any loss directly or indirectly derived from the use of this information or its contents, and the readers should make their own investment decisions. This report cannot be reproduced, distributed or published by the recipient or used for any purpose whatsoever without the prior written consent of Banco BOCOM BBM.