January-February Data Indicates a Dramatic Plunge of China's Economy

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Erupting across the country between late January and early March, the COVID-19 pandemic caused substantial disruptions to China's economy for the first quarter, and could significantly slow down the GDP growth over the year of 2020. China released its Jan-Feb data in mid-March, and the gloomy numbers indicate a great sag in China's economic activity during the coronavirus outbreak. Almost all indicators, from the consumer spending to factory output, fell more than expected earlier in February as the outbreak escalated. This prompted some forecasters to downgrade their predictions of China's GDP growth for the first quarter, which will very likely be negative, as well as the annual growth rate, which could possibly fall below 2%.

Many of the economic numbers announced by Chinese officials two weeks ago fell to its lowest level since the 1970s. Industrial output decreased by 13.5% from a year ago, as factory activities largely halted in February due to holiday extensions, travel bans and quarantines. The manufacturing sector, including automotive, textile, plastics, and electrical equipment, suffered a sharp drop of 15.7% in output. Production declines were seen on a massive number of products except for health and protective products such as masks and ethyl alcohol. Foreign-invested and domestic private enterprises took a harder hit than state-owned and joint-equity enterprises.

The home quarantine policy during the virus outbreak dampened demand for goods and services consumption in China and slashed retail sales by 20.5%. Restaurants were hit the hardest, with sales contracting by 43.1% during January and February. General merchandise sales also declined by 17.6%. Shored up somewhat by demand from a quarantined population, online sales fell only 3%. Household staples, such as cereals and vegetable oil, foods and beverage, and medical supplies, saw an uptick than last year.

Fixed-asset investment, a primary driver of China's GDP growth, tumbled 24.5% year-on-year to US$470 billion. All three sectors, primary, secondary, and service, reportedly shrank in January and February. Investment in infrastructure, manufacturing, and real estate also decreased by 30.3%, 31.5%, and 16.3%, respectively. Private enterprises and state-owned enterprises both cut investment in the first two months of 2020 and investment from the private sector showed a deeper dip. Nevertheless, the investment contraction in the high-tech and health sectors were reportedly lower than the average decline.

China's trade volume decreased by 9.6% during January and February, of which exports dropped by 15.9%, and imports dropped by 2.4%, resulting in a trade deficit of US$6 billion. However, general trade[1]

[1] General trade is a term compared to processing trade, where a country takes orders and import raw materials or parts from its trading partner, and re-export products after processing or assembling the raw materials and parts. Processing trade is often a utilization of a country's abundant production factors (For instance, cheap labor as in the Chinese context). A decrease in the ratio of processing trade and an increase in the general trade imply that China's trade is becoming more capital- or technology-intensive, indicating a higher position in the global value chains.

accounts for 60.6% of total trade value, with a year-on-year growth rate of 0.3%, indicating an optimizing trade structure. Meanwhile, China's trade with countries along the "One Belt and One Road" (B&R) is still expanding with an increase of 2% in imports and 1.8% in exports in January and February.

China's Foreign Direct Investment (FDI) reached US$12.4 billion in January, with a year-on-year increase of 4%. However, FDI decreased to US$6.6 billion in February, with a significant year-on-year drop of 25.6%. Combining January and February, China's FDI decreased year-on-year by 8.6%. High-tech industries however saw an increase in FDI. Compared to traditional manufacturing and services industries which require presence in the workplace, high-tech industries are more suitable for working from home, hence, less affected by the quarantine policy. Meanwhile, China's non-financial Outbound Foreign Direct Investment (OFDI) was US$8.1 billion in January, with a year-on-year decrease of 7.7%. For January and February together, China's non-financial OFDI amount to 107.86 billion yuan, with a year-on-year increase of 1.8%. Investment in countries along the B&R experienced a significant increase, with the increase rate of 18.3%.

China's unemployment rates in January and February are 5.3% and 6.2%, which increased by 0.1% and 0.9%, respectively. Due to factory shut downs China's job market experienced a tremendous shock in February. The service industries, including wholesale and retail, accommodation and catering, the transportation and post, and culture, sports and recreation, suffered the most. However, the unemployment rate of the population between age 25 to 49 is 5.6%, 0.6 percent lower than the aggregate number. Meanwhile, the unemployment rate of those between 20 to 24 with a college education is 0.4% lower than the national average in January. According to China's Ministry of Industry and Information Technology, as of March 7th, 78 million rural migrants have returned to work, accounting for 60% of total rural migrant worker population. Therefore, a reasonable recovery of employment in March may be expected.

China's Consumer Price Index (CPI) increased year-on-year by 5.4% and 5.2% respectively in January and February, compared to 4.5% in December 2019. Chinese officials said that a considerable spike in pork prices is largely to blame for the rise in consumer price (61.5% of the total CPI growth), which has shown a declining trend recently. Given the recent recovery in production and supply, a sharp increase in the CPI is less likely to been seen in the following months.

China's Industrial Producer Price Index (PPI) increased year-on-year by 0.1% in January and decreased year-on-year by 0.4% in February, which is mainly led by a sharp fall in the energy industry where the prices of related products decreased by 11% in February. However, due to the increasing demand for medical protective supplies, the price of domestically produced medical and pharmaceutical products increased by 0.3%. China's Manufacturing Purchasing Managers' Index (PMI) is 35.7%[2]. In February, a decrease of 14.3% from January, indicating a significant contraction of the manufacturing activities in China during the coronavirus crisis. The service PMI decreased by 13% for January and February, except for the financial services and high-tech services sectors, which saw a slight rise in activity. The aggregate PMI for February was 28.9%, 24.1% lower than January, suggesting that China's merchandise and services production in February is slowing. Yet the March Manufacturing PMI, which was just released, is 52%, implying a strong factory activity level in March.

[2] Industry is experiencing an expansion or increase when its purchasing manager index exceeds 50%, while on the other hand, the industry is experiencing a contraction or decrease when its purchasing manager index is less than 50%. The same criterion applies to other indexes.

The January and February official data released by Chinese authorities confirms a substantial contraction in China's economy in the first two months, as a result of the disruptive COVID-19. Given the number is much worse than expected, major institutions have slashed their forecasts of China's first-quarter and annual growth. Chinese officials and economists, however, are relatively optimistic about the economic recovery in the coming months and argued that the impact of coronavirus on China's economy is merely short-term. China is reportedly in the process of attempting to implement an ambitious "V-shaped recovery" plan by easing monetary policy and expanding fiscal stimulus to help workers to return to work and businesses resume their operations. The data showing a growing number of factories resuming production and the newly released encouraging manufacturing PMI appear to point to a positive outlook for the manufacturing sector in the recovery trajectory for the coming months.

Nevertheless, there are several uncertainties that may hold back China's recovery. The primary one is the domestic demand, which is hammered during the coronavirus outbreak and how quickly it may rebound still remains to be seen. The other major variable is the disrupted global supply and demand chains by the coronavirus pandemic which will undoubtedly be a drag on China's economic recovery. Instead of a V-shaped bounce-back that occurred after SARS between 2002 and 2003, China's recovery this time may turn out to be U-shaped and take considerably longer to execute.