December 19, 2019 | 4:39 PM EST

Is China turning a corner?

Overview

While Chinese consumer and manufacturing data appears to be on a short-term rebound, China is entering a period of structurally slower growth, with year-over-year GDP growth likely to slow below 6% by 2021.

We don't view this as purely negative, though. Somewhat slower growth will be the consequence of China's unwillingness to pursue further massive fiscal stimulus (i.e., direct government spending) programs. Capital flows should shift from negative margin state-owned enterprises (SOEs) to profitable private enterprises, with a materially positive effect on productivity, standard of living, business investment and financial markets.

A trade policy detente between the United States and China will stimulate production and consumption on both sides of the Pacific, a boon to transportation companies across modes. International freight forwarders could see near-term margin compression but top line growth if steamship lines are able to make their General Rate Increases stick.

Railroads and trucking carrier volumes will benefit from the removal of trade friction, especially if credit in China is diverted to productive private corporations — now the key driver of Chinese economic growth — rather than its lumbering, state-owned industrial conglomerates, banks and infrastructure holding companies.

China economic data

Retail Sales	+8% y/y
Automotive Sales	2,057,000
Industrial Production	+6.2% y/y
Manufacturing PMI	51.8

Chinese port volumes Oct. y/y change (YTD y/y change)

Shanghai	+2.8% (+4.9%)
Hong Kong	-4.1% (-6.2%)
Shenzhen	-3.1% (+0.9%)
Ningbo	+4.4% (+5.4%)
Guangzhou	+6.1% (+5.9%)

East Asia November GDP growth y/y change

China	+1.5%
Japan	+0.4%
South Korea	+0.4%
Taiwan	+0.6%
Singapore	+2.1%
Indonesia	+3.06%

JP Hampstead
Director, Passport Research
jphampstead@freightwaves.com
(865) 388-1708

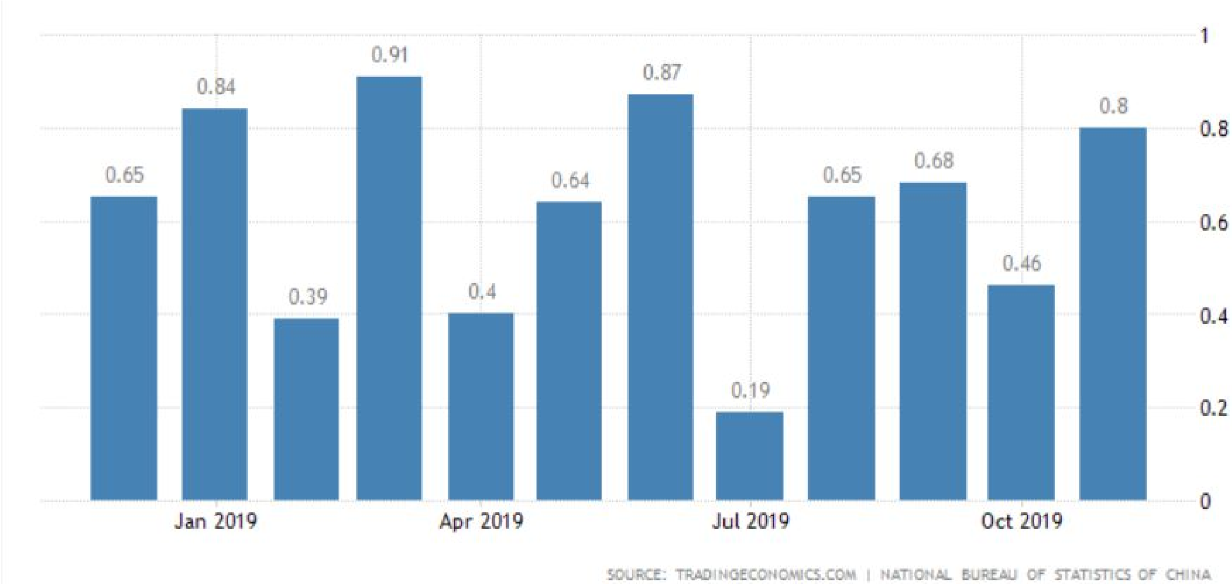
Hunter Carroll
Research Associate
hcarroll@freightwaves.com
(423) 650-5702

Tony Mulvey
Research Associate
tmulvey@freightwaves.com
(423) 637-1940

Domestic

Chinese retail sales rose 8% year-over-year in November, an encouraging sign for the domestic consumer economy going forward. This strong print came against a backdrop of uncertainty around trade and geopolitical unrest regarding Hong Kong and was the largest percentage increase since June of this year.

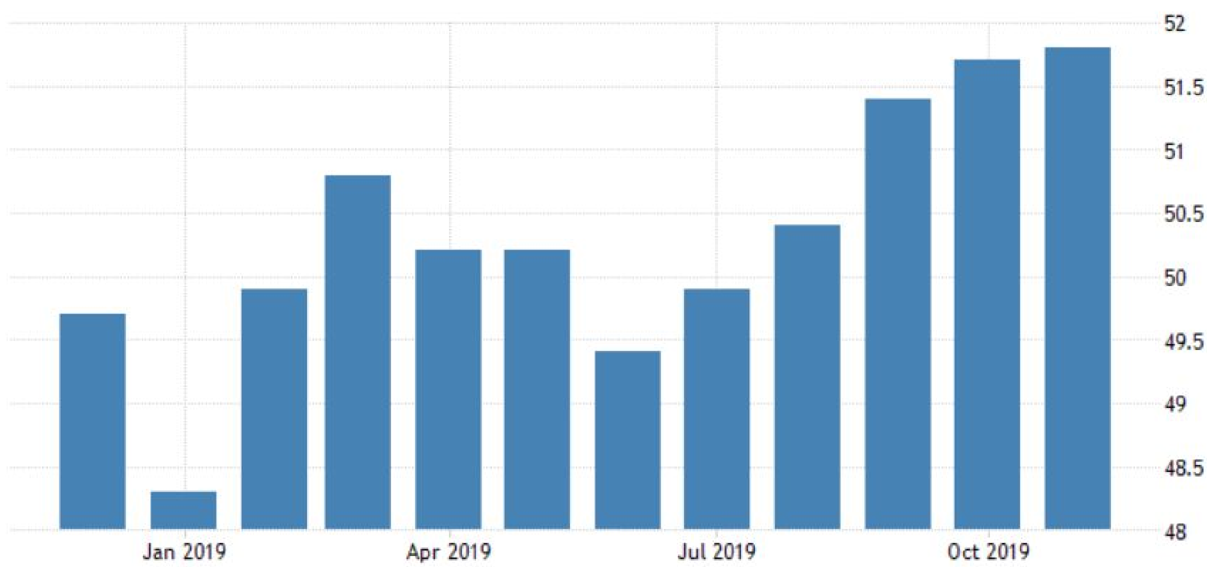
Faster retail sales growth is encouraging not only for Chinese companies but also American and other international companies. After the Phase 1 trade deal, the Trump administration said it expected a further opening of the Chinese economy, which along with an increase in retail sales, represents an opening for American foreign investment.



Car sales continue to be a drag on Chinese consumer spending numbers. Car sales have now decreased for 17 straight months and plunged lower from their highs at the end of 2017. One possible reason is a supply glut in the car market; another is increased regulation regarding greenhouse gas emission standards. Perhaps the most important factor is that in 2018 and 2019, Chinese consumers ramped up their household savings rates in anticipation of a protracted downturn.

Slumping car sales in China over the past 17 months coincided with broader weakness in auto sales across the globe. Fitch Ratings expects global auto sales to slide by 3.1 million in 2019.

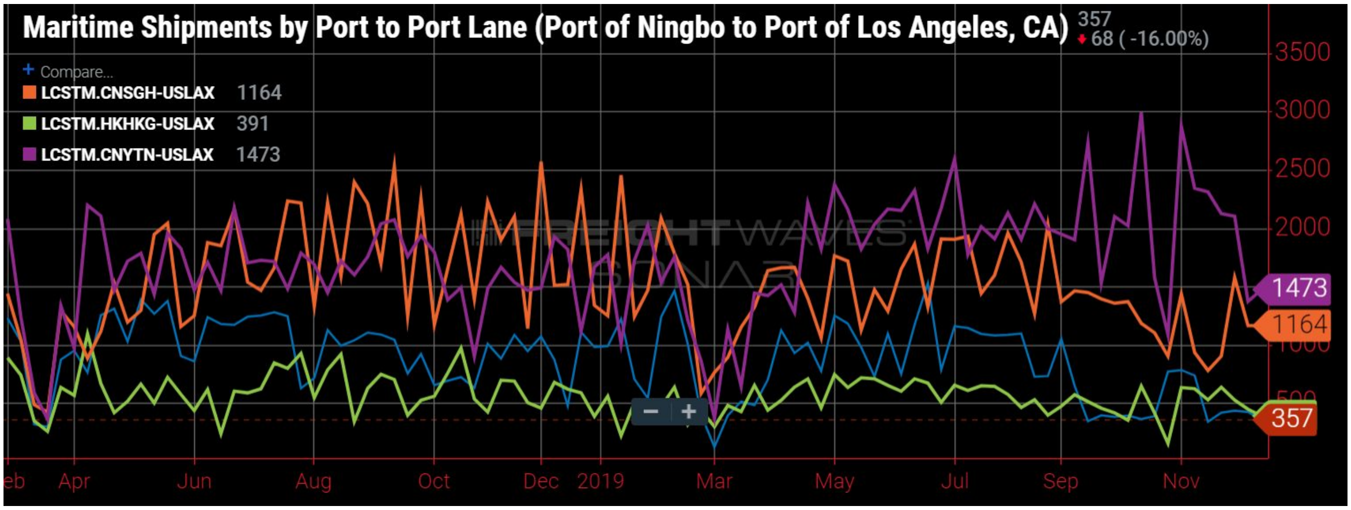
Adding to the solid industrial production print in November, manufacturing PMI also came in strong at 51.8, a three-year high. Manufacturing PMI has been trending up since June of this year. This coincides with an increase in the United States PMI since August, an encouraging sign for one of the world's most important bilateral trade relationships.



(Source: Trading Economics. China's manufacturing PMI)

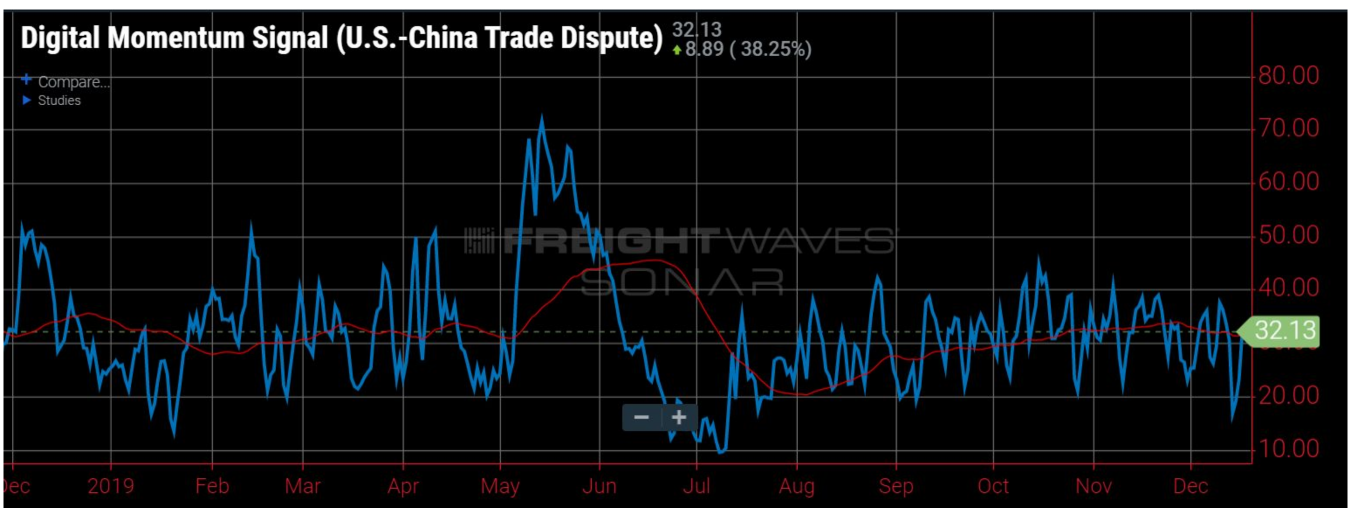
One negative development over the past couple of months has been increasing inflation, partially related to China's devaluation of the yuan in response to U.S. tariffs. This could be a concern going forward for Chinese consumers as they will be more crunched for cash and in turn possibly reduce discretionary spending. Part of the increase in consumer price inflation (4.5% in November) has been due to the shortage in pork, China's primary source of protein, from the African swine fever epidemic.

Trade



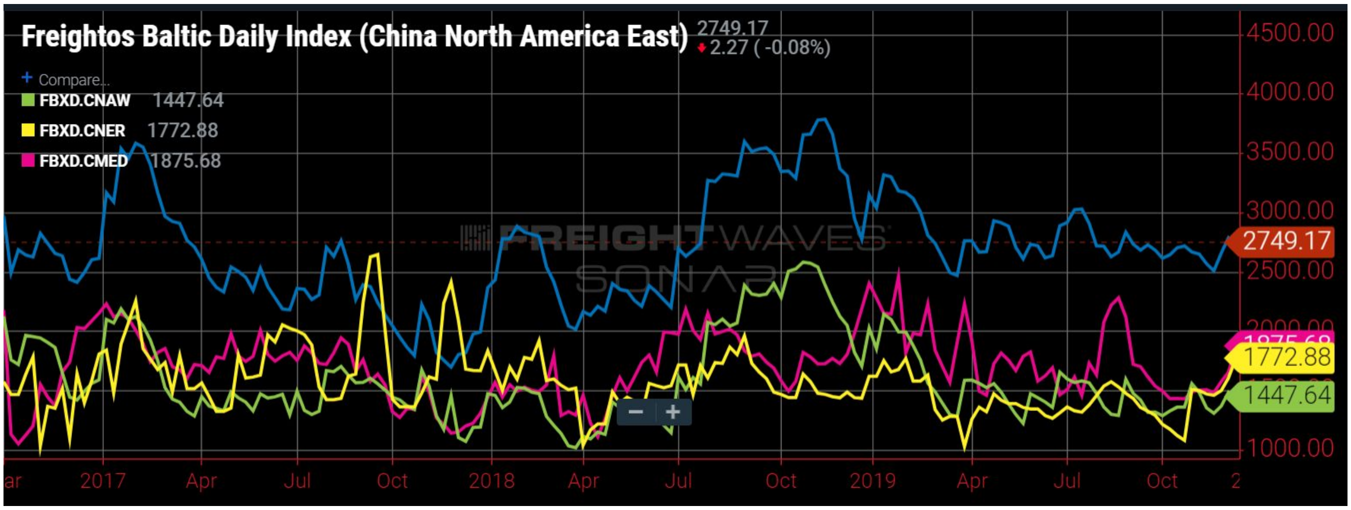
(Chart: Freightwave SONAR, seven-day moving average of import from port to port)

The trade war with the United States has impacted China since the beginning of 2018. Container volumes are rebounding following the tariffs implemented in December 2018. There was a pull-through of volume to avoid the tariffs, but inevitably trade had to continue for China and the United States. The Port of Yantian saw a surge in volumes from March through November, rising almost 680% from the bottom to its peak. The surge in volumes was partially from the threat of more tariffs on Dec. 15, 2019, that ultimately didn't materialize.



(Chart: Freightwave SONAR, SIGNAL.USCHINATRADE with 50-day moving average)

U.S. and China trade talks have dominated media coverage for the past two years. Digital Momentum Signals, displayed in the chart above, track the level of online interest in specific topics. We attribute the spike in May to President Donald Trump's raising of tariffs on China from 10% to 25%, but interest, which we read as concern, fell sharply after the Phase 1 deal seemed more likely.



(Chart: Freightwave SONAR, Container rates from China to various countries)

Container shipping rates have moderated from the highs of last year after the tariffs were implemented. Box prices bumped up recently in all of the major lanes out of China. The China - Europe and China - Mediterranean lanes' price increases mounted as demand for shipments increased. The U.S. tariffs on China required the Chinese to find new lanes, and Europe has been the new customer. With Chinese New Year on Jan. 25, the earliest it has been in three years, the rate increases to the U.S. are related to increased demand before the holiday.

Analysis

The temporary easing of trade tensions between the United States and China has already been stimulative of international trade, to the point that container volumes are approaching pre-tariff levels — though we note that near-term these may be impacted by CNY preparation.

Growing container volumes between China and Europe, both the Mediterranean ports and Rotterdam, reflect the new markets Chinese producers have found after being shut out of the transpacific. That shift in international trade could result in a rebalancing of ocean freight supply and demand and cause temporary steps up in transpacific rates.

Over the next few years, we still expect American firms to diversify their production and sourcing away from China to other emerging Asian markets, though a full resolution of the trade war could slow that process.

Ultimately, China's structurally slower growth signals the country's development into a mature, consumption-driven economy: one full of aspirational consumers who still love American culture and brands.