

PRESS RELEASE

China reopening has a positive but gradual impact on consumption

Bucharest, January 17, 2023 – China’s reopening process has come faster and earlier than expected. After announcing a gradual easing of its zero-Covid policy in November, the National Health Commission finally decided to downgrade the Covid-19 risk level in late December.

The economic, social and fiscal costs of the zero-Covid policy led to enormous uncertainty over the economy, weighing heavily on consumption and investment. At the same time, the rate of infection linked to the lifting of restrictions has put huge pressure on economic activity. The current wave of infections is expected to peak in mid-January, while a second wave – driven by the spread to rural areas – is estimated to reach its peak in early March. Given this context, Coface is forecasting a gradual normalisation of economic activity in March with a firm recovery starting in Q2 2023.

Increasingly unsustainable zero-Covid policy

The Covid-control measures introduced in China have hurt domestic demand with a negative impact on household spending. Compulsory testing and lockdown fears have severely suppressed consumption. Retail sales were flat in the first 11 months of 2022, and labour market prospects weakened with the unemployment rate hitting 5.7% in November.

Manufacturing production and logistics were also disrupted by the Covid-control measures, with industrial output growth slowing markedly to 2.2% in November and supplier delivery times lengthening sharply.

China has also been faced with a weakening external outlook. Exports were one of the key drivers for the country’s growth during the pandemic and in 2022, but external demand is now expected to be much weaker in 2023 with the slowdown in global growth. Goods exports in November fell by 8.7% year-on-year.

A case could have been made for maintaining the zero-Covid policy due to the October 2022 congress held by the Chinese Communist Party. But the strict control measures, lockdowns and mass testing requirements have ended up fuelling public tensions, which contributed to demonstrations in several cities towards the end of 2022.

Reopening clouded in uncertainty

China’s reopening is expected to be positive for the consumption outlook, but its impact will be gradual and possibly limited.

The rapid spread of infections and herd immunity should contribute to economic normalisation in Q2 2023. Although the infection rate is sending down the available labour supply – thereby affecting production and logistics activity – we should see a normalisation in this area.

Nevertheless, **although we expect a recovery in consumption in 2023, it will be gradual.** We have observed that disposable income is slow to recover, household savings remain high (40.3% of GDP in Q3 2022), and net wealth is falling. Moreover, the unemployment rate – which is still high – will continue to weigh heavily on consumption. The level of household debt should also be factored in: it has doubled compared to a decade ago (62% of GDP in 2022 compared to 30% in 2012), constraining the scope for leveraged consumption.

It is still possible, however, that consumption will benefit from a fiscal stimulus. Policymakers have stressed “stability” this year and pledged to prioritise domestic consumption and raise personal income. Consumer stimulus measures, such as consumption vouchers, could give a stronger boost to household spending.

Last but not least, investment is likely to continue to be a drag on growth this year, especially in real estate. Although the housing sector is expected to stabilise gradually given increasing policy support, infrastructure investment growth may be softer. Given the weakening global outlook, export-oriented companies are unlikely to invest in facilities.

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