



Temporary slowdown in economic growth to be followed by a rebound in 3Q11

Highlights

- ❖ **Initial signs of economic growth slowing down.** The control of inflation will inevitably come at the toll of economic growth. Currently, China's efforts to rein in inflation have curbed aggregate demand and economic growth. In March, economic growth started easing, with the downward trend likely to continue until the latter part of 2Q11. Nonetheless, the recent decline in economic growth has been relatively modest and lasted for a relatively short period. We expect China's GDP to grow by 9.2% and 9.4% in 1Q11 and 2Q11 respectively, with the QoQ growth rate in 2Q11 slowing down modestly. Excluding the base effect, the economy has been slowing in 2Q11.
- ❖ **Easing aggregate demand.** While investment activities seem to be robust in January and February, advanced indicators including new project investments indicate that investment growth will ease to a certain extent in 2Q11, with a 1-2 ppt decline in growth. Factors including the European debt crisis, nuclear radiation in Japan and others are likely to have a negative impact on Chinese exports. Given a slowdown in car sales and the impact on sales of home appliances and furniture as a result of cooling measures targeting the real estate market, consumer spending will remain low. The decline in aggregate demand will become more significant in 2Q11.
- ❖ **Micro indicators indicating a slowing economic growth.** Micro indicators including air traffic volume, sales of heavy-duty trucks and traditional machinery and equipment have declined. Prices of raw materials including steel and building materials were relatively weak. Inventory indices of certain upstream sectors increased. These micro indicators demonstrate that economic growth has been slowing down, with industrial growth likely to slow down in the future.
- ❖ **Economic growth expected to rebound in 3Q11.** Policymakers will likely adjust their control efforts based on future changes in inflation levels. We expect inflationary pressure to significantly ease in 2H11. During this period, although the underlying tone of the policy is to remain the same, policy tightening will likely be adjusted in order to restore economic growth momentum. We believe that the intensity of monetary tightening will be eased in 2H11. Moreover, policymakers would step up efforts on fiscal expansion, as development of welfare housing continues and restrictive policies on consumption of certain product categories are adjusted. All these factors will lead to a rebound of economic growth in 3Q11. We expect economic growth to rebound to 9.5 to 10% in 2H11.

CITICS Securities Research

Jianfang Zhu
Tel.: 010-84588756
Email: zhujf@citics.com
Business practicing license no:
S1010510120003

Yifan Hu
Tel: 852-22379116
E-mail: yifanhu@citics.com.hk
Business practice certificate no:
S1010510120070

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	Overweight	Relative performance over MSCI-China Index 5% ~ 20%
	Hold	Relative performance over MSCI-China Index -10% ~ 5%
	Sell	Relative performance over MSCI-China Index > -10%
	NR	Not rated
Sector rating	Outperform	Relative performance over MSCI-China Index >10%
	Neutral	Relative performance over MSCI-China Index -10% ~10%
	Underperform	Relative performance over MSCI-China Index > -10%

地址:	香港中环 添美道 1 号 中信大厦 26 楼	ADDRESS:	26/F CITIC Tower 1 Tim Mei Avenue Central, Hong Kong
电话:	(852) 2237 6409	TEL:	(852) 2237 6409
传真:	(852) 2104 6580	FAX:	(852) 2104 6580
Email:	hkresearch@citics.com.hk	Email:	hkresearch@citics.com.hk
网址:	http://www.citics.com.hk	Web:	http://www.citics.com.hk