

Greater Bay Area Insight

Consumption recovery in sight

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Economics - China

- ◆ Mainland China's reopening has led to favourable developments in retail activity at the start of 2023
- ◆ Policy remains accommodative; the property sector's stabilisation can lift consumption and lead to a virtuous cycle
- ◆ We expect new consumption trends to emerge in Guangzhou, led by online services

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Retail activities in the GBA region showing signs of recovery

Guangdong's retail sales growth increased by 1.8% y-o-y in January-February 2023, up 2.8ppt from December 2022. Service consumption, represented by the spending on catering, rebounded from a deep contraction at the end of 2022. The reopening of mainland China also led to a steady rise in intra-city and cross-boundary travel flows, pointing to potential improvements in retail activities.

In Hong Kong, a revival in discretionary spending, combined with strong holiday demand, led to the fastest rise in retail spending since April 2022, climbing 7% y-o-y in January. With a further pick-up in mainland Chinese visitors to the city as transport capacity is restored, consumption demand should grow further in the coming months.

Reasons to be constructive about regional consumption

Aside from mainland China's reopening, the Guangdong city government has pledged to focus on expanding domestic demand this year by supporting home upgrading and promoting sales in key consumption categories, including new energy vehicles and catering. Meanwhile, the PBoC's monetary stance, which has already provided fuel for reviving domestic demand, is expected to remain accommodative. Recent developments in the property sector, if sustained, can feed into consumption, potentially leading to a virtuous cycle. The Guangdong government aims to achieve a 6% growth target for retail sales in 2023.

Consumption upgrading and regional integration can foster new trends

In mainland China, Guangdong province accounts for 23% of the country's online goods sales and 17% of online service sales, far exceeding peers of a similar economic scale. In our view, Guangdong has the necessary expertise and the right demographic wealth profile to expand online services. Meanwhile, Guangzhou has been chosen by the central government to be an "international consumption centre", which should allow the city to leverage its large and wealthy population to cultivate new consumption trends. Regional integration is also expected to help convert inbound traveller spending into effective consumption power.

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Consumer activities are gradually recovering

GBA's consumption recovery led by the service sector

In 2022, Guangdong's total value of retail sales reached RMB4.5 trillion (accounting for 10.2% of mainland China's aggregate), up only 1.6% y-o-y, rather muted compared to peer provinces (Chart 1). Entering 2023, mainland China's data suggest that consumer activities are gradually recovering, and Guangdong is following a similar trend. In January-February, the province's retail sales increased by 1.8% y-o-y, up 2.8ppt from December 2022.

A key reason why Guangdong's economy underperformed the national average last year was mainly due to the service sector, which was heavily constrained by the pandemic and related control measures. The situation has changed considerably since the reopening of the country. In January-February 2023, spending on catering services increased by 18.8% y-o-y, compared to a deep contraction in December 2022 (Chart 2). Guangdong's regional traffic flows also surged, as did cross-boundary travel flows (refer to Chart 1-5 in section 2).

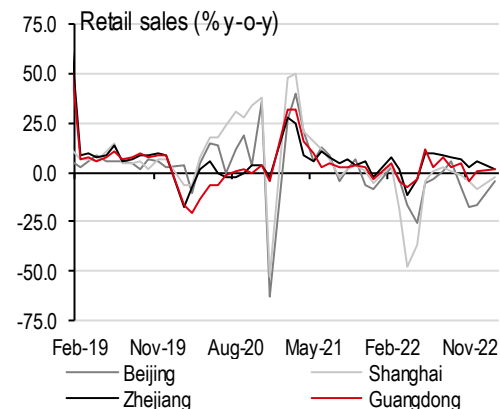
Take Hong Kong for example: the number of mainland Chinese visitors to Hong Kong reached 1.11m in February after the full resumption of customs clearance, nearly quadrupling from January. Still, this accounts for only about 45% of the pre-pandemic level (in the most recent week ending 26 March), leaving plenty of room for Hong Kong's local retail and service businesses to grow.

Hong Kong's local consumption recovery should continue to strengthen

In the near term, the revival of Hong Kong consumption demand is being driven by local demand, with 7% y-o-y retail sales growth in January underpinned by increased purchases of discretionary goods like clothing and jewellery, which can be attributed to more services consumption as people go out more. Hong Kong's local consumption recovery should continue to strengthen on the back of another round of consumption vouchers (first batch in mid-April). With the removal of quotas and PCR testing requirements since the beginning of February as well as the restoration of transportation links (long-distance high-speed rail services will fully resume starting on 1 April), the pickup in mainland Chinese visitors to Hong Kong should continue to fuel the consumption of goods and services. We expect full-year mainland Chinese visitors to reach about two-thirds of pre-pandemic levels this year.

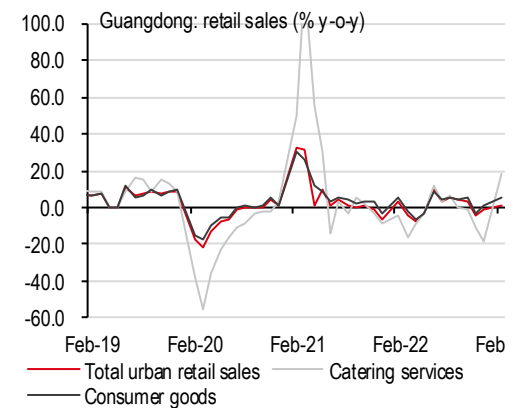
Despite notable improvements, national data suggest it will still take some time for private enterprises and households to regain confidence. The improvements in the labour market and consumer sentiment up until February were limited, and more policy support is needed to sustain the recovery trend, in our view.

Chart 1: Guangdong's retail sales growth was relatively muted compared to peers



Source: Wind, HSBC

Chart 2: Catering services demonstrated a notable bounce after the reopening



Source: Wind, HSBC

Reasons to be constructive about the consumption recovery in the GBA

During the local “Two Sessions”, Guangdong’s government presented a 6% growth target for retail sales of consumer goods in 2023, lower than the 8% target in 2022. Similar to the central government, we believe this is a relatively conservative target that is achievable. The government said it will focus on expanding domestic demand, supporting home upgrading and promoting the consumption of new energy vehicles and green smart home appliances. It will also promote service consumption, including catering, cultural tourism, elderly care and childcare. Automobile and catering services together account for more than 40% of Guangdong’s retail space, which explains why the government will put more emphasis on supporting these sectors.

A key supporting factor is the accommodative policy environment

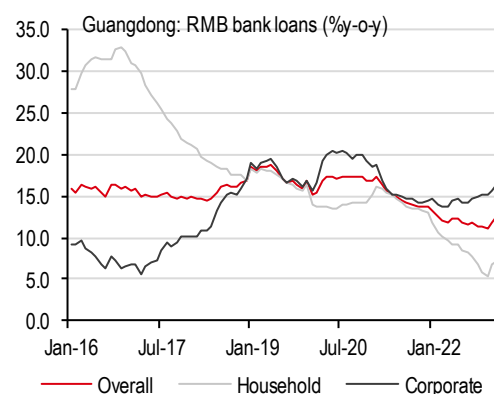
In terms of this year’s consumption outlook, a key supporting factor is the accommodative policy environment. The PBoC has kept pushing for lower financing costs to support domestic demand, especially for mortgages, and we believe there could be more space for monetary easing in 2Q23.

In Guangzhou, first-home mortgage loan rates have reached 4.3%, a four-year low (STCN, 24 March). For Zhuhai, first-home mortgage rates have come down to 3.7%, the lowest in the country (Shanghai Securities Journal, 1 February). Cities like Foshan and Dongguan also lifted housing purchase restrictions in December 2022. Amid these relaxation measures, medium- and long-term household borrowing started to turn at the beginning of the year (Chart 3), so have other property market indicators (Charts 6-9 in section 2). These developments may point to the further stabilisation of the local property market, which is expected to support consumer expenditure through the wealth effect (Chart 4).

In 2022, auto sales in Guangdong reached RMB569bn (accounting for 12.7% of Guangdong’s total retail sales), an increase of 4.9% y-o-y. This sector played a key role in driving positive retail sales growth last year, suggesting that relevant consumption-promoting policies were effective. However, with the expiration of the national subsidies for new energy vehicles by end-2022 (Xinhua, 21 February), local governments and car producers both had to step up.

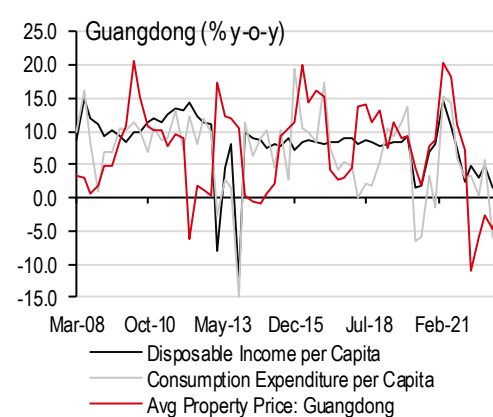
Aside from price cuts initiated by the auto manufacturers, the Guangdong government announced it will continue to exempt vehicle purchase taxes in 2023, and a number of cities also announced subsidies for car replacements and added EV purchasing quotas for residents (21jingji, 24 February). Overall, our auto sector analyst believes that it may take some time for the auto consumption recovery to resume as consumers may wait for more price cuts to materialize (Yuqian Ding, *China EV Tracker*, 20 February).

Chart 3: Guangdong’s bank loan growth has started to rise



Source: Wind, HSBC

Chart 4: Property prices still in decline in February but the gap is quickly closing



Source: Wind, HSBC

The pandemic contributed to strong online sales**New consumption trends in the region**

In January-February 2023, Guangdong's online retail sales of above-designated size enterprises increased 14% y-o-y, contributing 1.4ppt to headline growth. This was against a backdrop of an already strong 13.4% y-o-y growth for full-year 2022, 11.8ppt higher than headline retail sales growth. The pandemic partly contributed to the strong online sales up until early 2023. Though offline sales are expected to take back some share after the reopening, it is conceivable that the rapid development of e-commerce and logistics industries are fostering new consumption trends.

Indeed, 23% of mainland China's online goods sales and 17% of the online service sales take place in Guangdong, far exceeding other provinces of similar economic scale (Chart 5). Online consumption in Guangdong has expanded at an annual pace of 32% between 2017 and 2021, 10ppt higher than the national average, covering services, such as medical care, remote office, and education. Going forward, consumption that features green themes, artificial intelligence and health may well become the new drivers for service consumption. Take healthcare services for example – all the primary hospitals in Guangdong have set up internet hospitals. In the second half of December 2022, the online platforms served 62,400 people per day, equivalent to volumes at six medium and large hospitals, alleviating pressure on hospital outpatient services (21jingji, 4 January).

The concept of “international consumption cities” has been promoted since 2021

Meanwhile, the central government has been promoting the concept of “international consumption cities” since 2021. Guangdong's capital city Guangzhou, along with Beijing, Shanghai, Tianjin and Chongqing, are taking the lead. It is easy to understand the logic behind the choices: these five cities have large population bases and are considered the core cities in their respective regions. Most importantly, these cities are well connected with the external market through foreign trade and passenger traffic. Guangzhou has the biggest population among cities in Guangdong province and is designated as one of the four major hub cities of the GBA area. In 2022, Guangzhou joined with Shanghai, Beijing and Chongqing, to become the fourth mainland city to record total retail sales over RMB1 trillion.

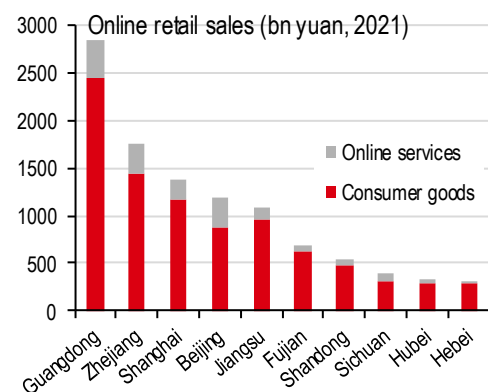
In March 2023, Guangzhou announced an “Urban Development Plan for Building an International Consumption Centre (2022-2025)”. The blueprint laid out several major targets for the coming years (Table 1), and the key tasks for the government are promoting consumption upgrading, building better business districts, and supporting the expansion of duty-free shops. Aside from the economic scale, several key elements are at play to support Guangzhou's ambitions. First, the city's annual per capita GDP reached more than RMB150,000 (about USD23,000) or 1.8x the national average as of 2021. It is one of the highest among domestic peers, allowing the city to pursue consumption upgrading and spend more on services. Second, Guangzhou has long been the country's southern commercial and manufacturing hub; given its new position as GBA's trade and transportation centre, there is great potential to unleash regional consumption power through integration.

From the regional perspective, further integration of GBA cities may help create synergies through cross-boundary consumption activities. For one, Guangdong is already ranked first among 31 provinces in terms of the number of inbound overnight tourists and group outbound tourists, accounting for 25.7% and 16.8% of mainland China's tourism flows, respectively. With mainland China's full reopening, the province can make full use of its regional transportation network and convert international passenger flows to effective consumption power.

In the blueprint, the Guangzhou government proposed expanding duty-free consumption, playing to its strength of having one of the mainland's busiest airports and railway stations. Meanwhile, the city aims to launch major sports events, including a pilot horse racing programme in cooperation with the Hong Kong Jockey Club (Southcn.com, 8 March). The latest relaxation of financial policies will also allow Hong Kong and Macau residents to get easier

access to mainland bank accounts and, therefore, mobile payment applications. Both are essential tools for people to travel and live in mainland China nowadays.

Chart 5: Guangdong ranks top in the mainland in online retail sales scale



Source: Ministry of Commerce, Wind HSBC

Chart 6: Guangzhou's key targets for building international consumption centre

	2021	2025e
Inbound Tourist Reception (10 thd person-times)	165	200
Number of Fortune 500 companies	300	335
Number of duty-free shops and departure tax refund shops	76	300
Total mileage of subway operation (km)	590	900
Number of online ride-hailing service cars (10 thd)	12	21

Source: Guangzhou City Government, HSBC

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