

Nomura Research Examines Impact of China Slowdown on Global Growth

Asian economies would be hardest hit by China slowdown, Nomura Research shows

Hong Kong, July 24, 2013 — In its latest anchor report, Nomura considers a downside risk scenario where China's GDP growth falls below the bank's baseline forecast of 6.9% in 2014 and examines the potential global economic impact.

According to the findings, if China's GDP growth falls by one percentage point, global growth outside China would decrease by 0.3 of a percentage point. A summary scorecard of indicators is used to gauge the relative exposures to China of 26 countries through the export, commodity prices and financial markets channels.

"We believe that the likelihood of China experiencing this risk scenario is a non-trivial 10-20%," said Rob Subbaraman, Nomura's Chief Economist and Head of Global Markets Research, Asia ex-Japan. "We have considered a range of stresses which the economy faces from many dimensions, including financial leverage, pollution and social tensions."

The hardest hit economies would be in Asia, with growth falling by 1 percentage point (pp) or more in Hong Kong, Singapore and Taiwan. The impact is also large on commodity-producing countries, such as Australia, Malaysia and those in Latin America. Despite being located much further away from China, the impact on GDP in Latin America (-0.5pp) is as large as that on Asia.

In the Euro area, the overall impact is -0.3pp, with Finland, Austria, Belgium, Germany and the Netherlands among the most exposed. The United States is among the least exposed.

"Slowing growth and falling inflation is paving the way for 13 of the 19 central banks to cut interest rates in 2014, the exceptions being those that have no scope, either due to the monetary policy framework or because policy rates are already at rock bottom, namely Japan, Hong Kong, Singapore, Canada, the US and the UK," added Mr. Subbaraman.

Equities as the growth sensitive asset class would likely suffer more than other assets. These risks appear more fully priced already into China H-share stocks themselves than in much of the rest of the global equity space.

“We find that stocks in the mining and energy-intensive UK, Latin America and EEMEA exhibit the MSCI World’s highest -- and in this scenario, adverse -- correlations with China H-shares,” said Michael Kurtz, Nomura’s Global Head of Equity Strategy and Chief Asia ex-Japan Strategist. “It is Japan, however, that offers the world’s lowest equity correlation vs. H-shares by far, along with key fundamental firebreaks that make it an attractive ‘defensive’ equity market in a China slowdown scenario,” added Mr. Kurtz.

For global FX, a sharp slowdown in China’s economy would have both direct and indirect negative impacts on commodity producers and countries with relatively large China trade links.

China would likely hold the USD/CNY fix stable. “The AUD, CAD, BRL and KRW would suffer among the most, while MXN and PHP should be relative outperformers” said Craig Chan, Nomura’s Head of Asia FX Strategy.

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