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# 1Q2022 Outlook: Strong but Short Stimulus Expected to Stabilize Growth

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## 1Q2022 Key Takeaways:

- Beijing's "Zero-Covid" containment strategy will remain in place, but its economic impact will be more modest than meets the eye;
- The Chinese government is expected to offset weak growth with strong but short-lived stimulus that will likely peak by the end of 1Q2022;
- The dissipation of supply-side constraints such as energy shortages will mean fewer downside risks to growth;
- As such, Beijing is aiming for a year of steady but not-so-stellar growth of around 5% in a year where stability is paramount.

China's 2021 headline growth of 8.1% belies a very weak fourth quarter of just 4% growth. This has led to expectations of more significant easing in 1Q2022, only to have Beijing's response to the Omicron wave throw yet another wrench into the growth picture.

We expect Beijing to stimulate the economy through 1Q2022 before tapering off in the second quarter, while not deviating from the "Zero-Covid" containment strategy. The impact of such a strategy on the economy will certainly be felt in the first quarter, but quarterly growth should nonetheless exceed 5%.

That's because Covid lockdowns' impact will be more modest than meets the eye. These lockdowns occurred with frequency in 2H2021, but were far less responsible for slowing growth than the confluence of drags on the economy, including tight monetary policy, the energy crunch, and property sector volatility.

We expect many of those drags to dissipate in 2022. Therefore, after weathering the headwind from Omicron in the first quarter, growth for the year will likely settle around 5% as a result of the low base effect.

## Zero-Covid Stays, Impact Modest

At this point, China stands alone as the only major economy opting to contain, rather than coexist, with Covid-19. This strategy, involving periodic lockdowns, quarantine, and massive testing, is expected to remain in effect through 1Q2022, based on three main reasons:

1. “Zero-Covid” and “life first” have become an important plank of President Xi Jinping’s political platform heading into the 2022 transition, with little room to budge on this stance.
2. The economic impact of the containment strategy is more modest in reality, which means the tradeoff costs are not yet obvious.
3. Shifting away from lockdowns may impose more economic costs than maintaining the containment strategy.

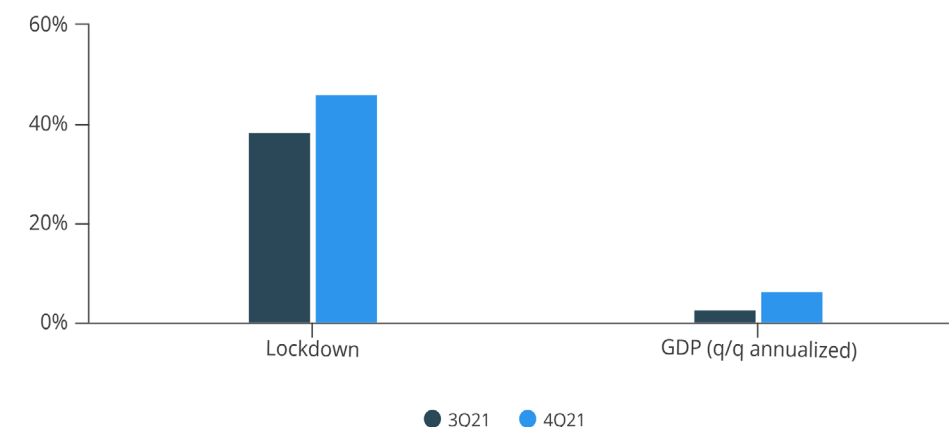
Beijing’s main calculation in holding the line on Zero-Covid is the tradeoff between political benefits and economic costs. At this point, Beijing continues to judge the former to outweigh the latter, particularly since Xi’s administration has capitalized on battling Covid as a demonstration of the validity and credibility of China’s political system.

This political calculation will endure so long as the economic impact from Covid remains manageable. So far, that appears to be the case. In fact, despite the headline risk of lockdowns once again disrupting consumption and ensnaring supply chains, we believe the actual impact will be more modest.

In retrospect, what transpired in 2H2021 can demonstrate why the current bout of lockdowns will not see economic costs as significant as some assume.

Take growth for example. 4Q2021 saw much faster growth than in 3Q2021, even though the fourth quarter had more Covid lockdowns (see Figure 1). It would appear that alleviating the energy crunch at the end of 2021 had a much bigger impact on growth. Moreover, the effect of lockdowns in 2H2021 didn’t show up in supply chains. In fact, China’s ports had a banner year in 2021, [handling a record volume](#) of goods and containers even during months most disrupted by Covid.

**Figure 1. Growth Accelerated in 4Q2021 Despite More Lockdowns**

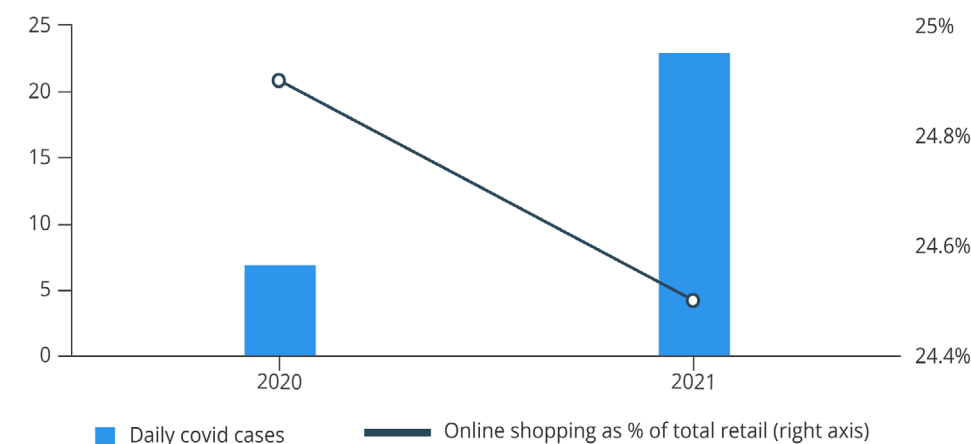


*Note:* Lockdowns are proxied by percent of air travel below 2019 levels.

*Source:* Wind and MacroPolo.

On the consumption front, Covid lockdowns appeared to have been a negligible factor affecting household consumption in 2021. Some of this can be seen in consumption patterns. For instance, Chinese consumers did not shift to e-commerce despite more draconian Covid lockdowns in 2021, suggesting other reasons are behind stubbornly weak consumption (see Figure 2).

**Figure 2. Share of Online Shopping in Retail Spending Actually Declined in 2021**



*Source:* Wind and MacroPolo.

Finally, if lowering case count follows the typical cycle of roughly four weeks, then the current containment strategy can handle the Omicron outbreak in a comparable timeframe. Tianjin and Henan, for example, have [already demonstrated success](#) in bringing case counts down to the single digits.

Given that imposing lockdowns won't impose dramatic costs to the economy, abandoning the strategy may actually have the opposite effect. Because vaccines are apparently less effective in China, lifting lockdowns will likely increase Covid risks, real and perceived. That elevated risk perception will likely spook consumers and affect consumption, just as the Omicron wave has put a dent in consumption in South Korea and the United States.

Declining consumer confidence, then, could further depress already weak consumption and end up more costly than the economic hit from maintaining containment.

### Stimulus Peaks in 1Q2022

Dealing with Omicron may not be how Beijing wanted to kick off the Winter Olympics, but there are reasons to be cautiously optimistic. Stronger monetary and fiscal easing and the dissipation of previous headwinds will support growth in the first quarter, with Beijing likely setting a 2022 target of around 5% at the National People's Congress in March.

Beijing has sufficient policy room and tools to offset the modest growth impact from Covid lockdowns, particularly since the main supply-side constraints in 2021—such as energy and chip shortages, as well as commodity inflation—are unlikely to be repeated this year. When it comes to the wobbly property sector, it is also showing signs of stabilization (a forthcoming research note will assess why the property sector's impact on growth may be overstated by at least 20%).

It behooves Beijing to stimulate early and strongly, because it usually takes two quarters for stimulus to work its way through the economy and reach maximum impact just before the 20th Party Congress in the fall. This will also help to shore up weakening market expectations, a risk that Liu Guoqiang, the central bank's vice governor, [recently noted publicly](#).

But don't expect stimulus to last beyond the first quarter. As Beijing increasingly prioritizes long-term growth, it has adopted a "just enough" philosophy on stimulus. That is, stimulus is now reined in quickly, sometimes even before the economy has fully recovered.

What happened in 2019 is a good reference for [what will likely transpire](#) in the first quarter. Beijing tapered stimulus in the first quarter, only to see the economy weaken again as the

US-China trade war escalated in May. But the Chinese government resisted more stimulus, holding out for more than three months before offering more supportive policies.

So too will broad-based stimulus peak by the end of 1Q2022, though other forms of policy support such as relief measures for struggling small and medium businesses will be extended. Beijing will also introduce more relief to address college student unemployment, a growing labor market problem.

### Mamahuhu: Steady But Not Stellar Growth

An investment-led stimulus, coupled with the disappearance of previous bottlenecks such as energy shortages, should put first quarter growth above 5%. But growth isn't likely to outperform expectations as stimulus will peter out quickly. The main reason Beijing believes it can probably grow 5% for the year is because of the low-base effect from 2021.

As such, while we expect somewhat improved growth, the Chinese economy will continue to perform below its potential in 1Q2022 and likely for the whole year. However, policy uncertainties that spooked global investors in 2021, such as the tech crackdown and the Evergrande crisis, are likely to recede in 2022. To the extent there are policy surprises, they will likely be of modest impact that affect a narrow set of companies.

In the spirit of the Year of the Tiger, 2022 is gearing up to be one of *mamahuhu* (马马虎虎) growth. That is, way fewer downside risks but also little upside surprise. In this year of stability, the most consequential factor for the economy will be the outcome of the 20th Party Congress in the fall. We will be [closely monitoring](#) Chinese politics this year and how it might affect economic outcomes.