

China Economy

PMI contraction signals caution ahead

China's manufacturing PMI dropped 0.1 to 49.4% in Nov, falling short of market expectation again. New order, export order and existing order further contracted, signalling weak demand for goods both domestically and internationally. The hindrance from demand side on final products also transmitted to corporate procurement activities as both material purchase volume and import order edged down. Material purchase price index dipped again while ex-factory product index stayed in contraction, extending the deflation process. Employment minimally improved although remained in contraction. Service PMI noticeably dropped into contraction for the first time in 2023 as national holidays ended in Oct, while construction rebounded thanks to the fiscal expansion. China's economy has softened recently, calling for additional policies ahead. China may maintain its GDP growth target at 5% for 2024 with more expansionary fiscal policies and additional monetary policy easing. We maintain our forecast for GDP growth at 5.3% in 2023 and 4.8% in 2024.

- Manufacturing activities remained in contraction dragged by still-soft domestic and external demands.** China's manufacturing PMI came in below expectation and contracted to 49.4% in Nov from 49.5% in Oct. Production index inched down to 50.7% in Nov from 50.9% in Oct. New order, export order and existing orders all remained in contraction at 49.4%, 46.3% and 44.4%, respectively, from 49.5%, 46.8% and 44.2%, showing no signs of alleviation from the demand side, both domestically and externally. Material purchase volume and import order both edged down from 49.8% and 47.5% to 49.6% and 47.3%, indicating the weak demand is weighing on corporate procurement activities. Breaking down by sector, new order indexes in medicine, automobile and other transportation equipment reached above 53% while more than 60% of surveyed companies indicated insufficient market demand. The PMI of large and small enterprises worsened in Nov, while both small and medium enterprises remained in contraction.
- Deflation pressure increased after the pullback of energy and commodity prices.** Ex-factory price index stayed in contraction but slightly rebounded from 47.7% to 48.2%, while manufacturing material purchase price worsened from 52.6% to 50.7%. The deflation pressure increased in manufacturing goods with the retreat of energy and commodity prices. Inventory for materials and finished products worsened, as firms continued to destock proactively amid weak demand and confidence. Service price index moderately dropped, while construction price rebounded. Looking forward, China's CPI and PPI may gradually rebound in 2024 thanks to base effect, demand improvement and the end of de-stocking cycle.
- Service sector dropped into contraction for the first time in 2023, while construction mildly rebounded.** Non-manufacturing PMI dropped to 50.2% from 50.6%. PMI in service fell from 50.1% in Oct to 49.3%, the first contraction in 11 months as pent-up demand in the post-Covid era came to an end. Breaking down by sector, output in railroad & air transportation, catering and lodging, and sports & entertainment pulled back from high level as national holidays ended in October. Capital market and financial services, real estate services and TV & broadcast kept booming. Construction PMI bounced to 55% from 53.5% thanks to the fiscal and infrastructure stimulus, while the new order index continued to worsen to 48.6% from 49.2%. Business

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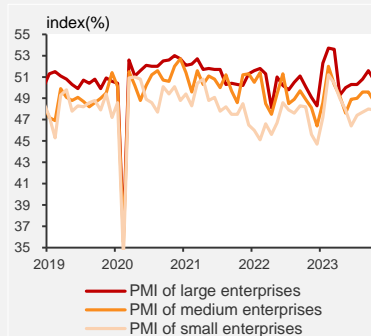
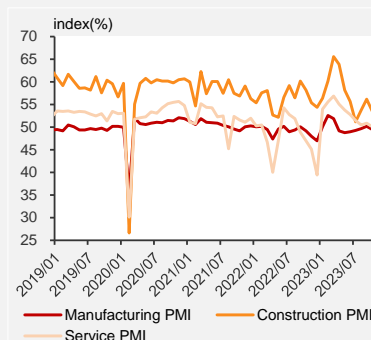
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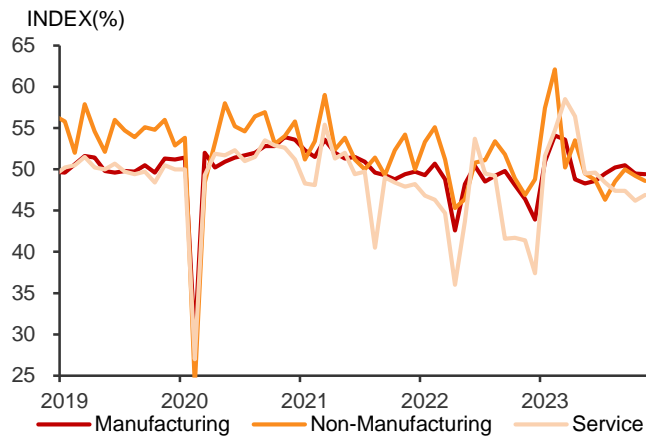
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sentiment indexes in construction and services both improved and remained in high expansion zones.

- **Employment minimally improved but remained weak.** Employment indexes in manufacturing, service and construction recovered to 48.1%, 46.7% and 48.2% from 48%, 46.5% and 46.4% in Oct, but remained in contraction. The weak employment condition will restrain the recovery momentum of household consumption and become a major drag on the economic growth.
- **China's economy dipped again calling for additional policy support ahead.** The PMI in November signaled China's economy may have weakened again recently. The policymakers may maintain the GDP growth target at 5% for 2024. However, it is more difficult to achieve the 5% growth next year as the lower base effect should decline. China may adopt more expansionary fiscal policies and further loosen monetary policy & property policy to boost the growth. Broad fiscal deficit ratio may reach 8% of GDP in 2024. The PBOC may launch additional cuts in RRR, deposit rates and LPRs in the next several quarters. Municipal governments may further loosen property policy to stabilize the property sector. We maintain the GDP forecast for 2023 at 5.3% and that for 2024 at 4.8%.

Figure 1: New Order Index



Source: WIND, CMBIGM

Figure 2 : Business Sentiment Index



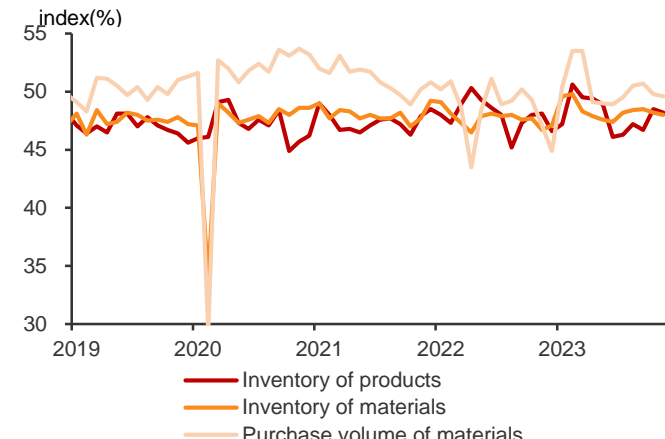
Source: WIND, CMBIGM

Figure 3: Export Order Index and Import Index



Source: WIND, CMBIGM

Figure 4: Inventory Index



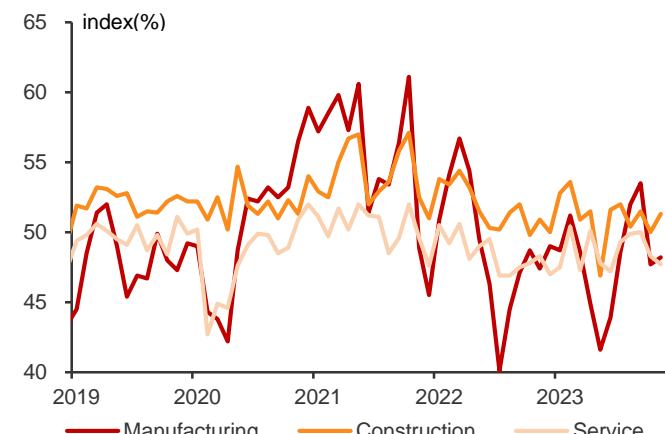
Source: WIND, CMBIGM

Figure 5: Material Purchase Price Index



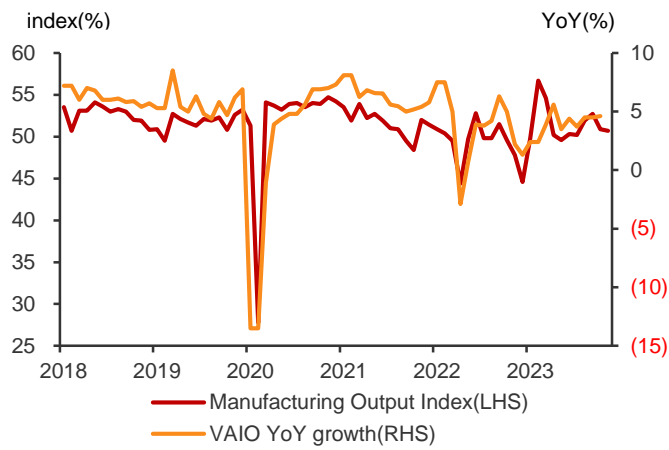
Source: WIND, CMBIGM

Figure 6: Ex-factory Price Index



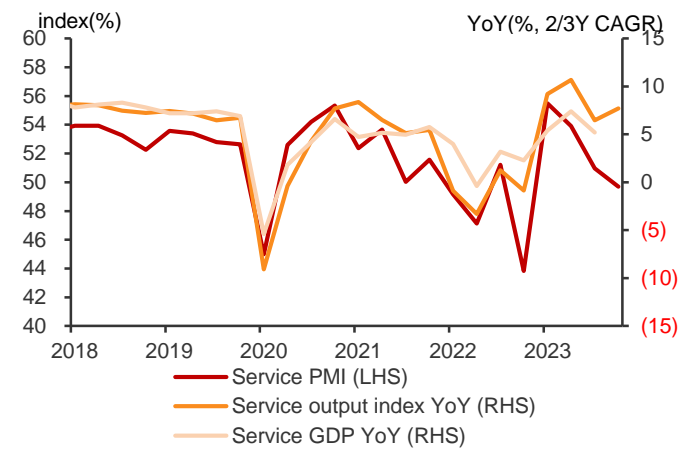
Source: WIND, CMBIGM

Figure 7: Manufacturing Output Index



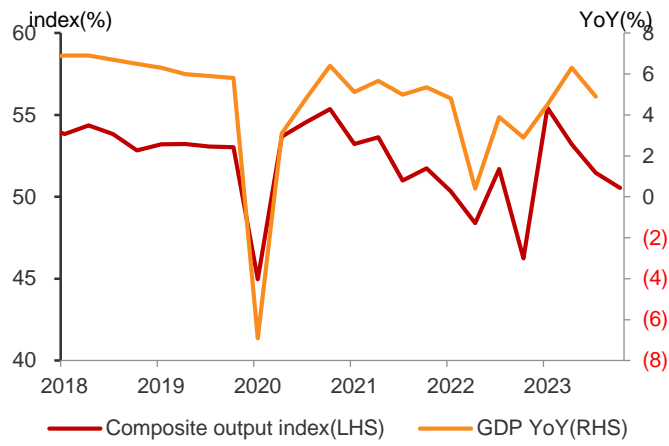
Source: WIND, CMBIGM

Figure 8: Service PMI & Output Index



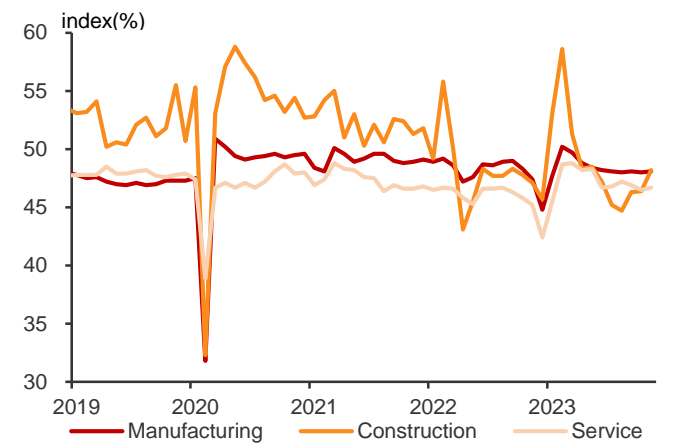
Source: WIND, CMBIGM

Figure 9: Composite Output Index



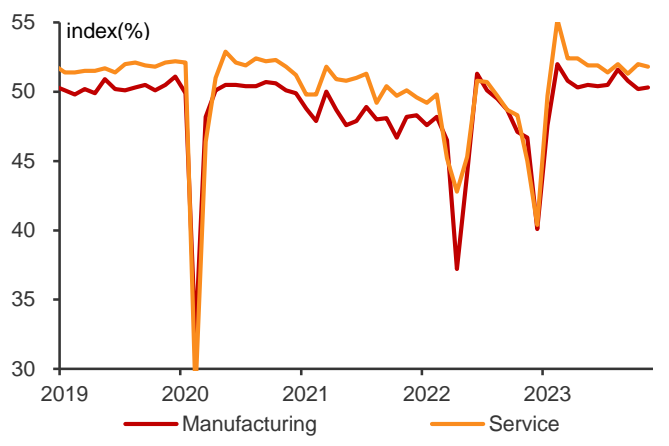
Source: WIND, CMBIGM

Figure 10: Employment Index



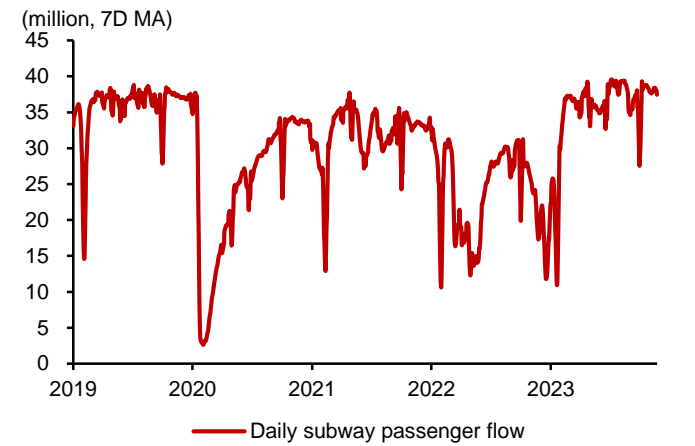
Source: WIND, CMBIGM

Figure 11: Supply Delivery Index



Source: WIND, CMBIGM

Figure 12: Subway passenger flow in tier-1 cities



Source: WIND, CMBIGM

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