

China Economy

PMI signalled mild improvement amid continuous policy easing

China's manufacturing PMI further improved in August, yet staying in contraction territory for five straight months. Production, new order and purchase volume all returned to expansion, indicating a moderate recovery on domestic demand side. However, export order and import indexes remained below 50% as global households shifted from goods consumption to service consumption with destocking cycle and deflation pressure in most manufacturing industries. Due to a pick-up in food and energy prices, material purchase price index and ex-factory product index substantially increased. We expect the PPI may continue to narrow its YoY declines in August. Employment in manufacturing remained tedious due to weak demand and industrial upgrading towards higher labor productivity. Service PMI remained in expansionary range yet softened in the hot summer. Travel, transport service, hotel, catering and recreational service performed better thanks to strong demand for those services during the summer holiday. Recently, China has signalled stronger policy loosening ahead. The country lowered its stock trade tax and eased property policies even in tier-one cities. We expect additional RRR cut and credit supply loosening in next few months. China's economy may gradually improve in next four quarters. We maintain our forecast on China's GDP growth at 5.1% in 2023 and 4.8% in 2024.

■ Manufacturing activity moderately improved yet remained in contraction.

China's PMI in manufacturing slightly improved in August to 49.7 from 49.3 in July, but remained in the contraction territory. Production index continued to expand from 50.2% in July to 51.9% in August. New order and material purchase volume returned to expansion for the first time since April, showing a moderate improvement on the demand side. Breaking down by sector, indexes in agricultural product processing, chemical materials & products and automobile reached above 53%, while textile remained in the contractionary range. Export and import indexes slightly improved but remained in contraction, indicating possible mild improvement of China's foreign trade activity in August.

■ Deflation pressure eased as material purchase price and ex-factory price sharply rebounded.

Material purchase price index and ex-factory price index respectively rebounded from 52.4% and 48.6% in July to 56.5% and 52% in August, indicating a significant alleviation of deflation in the industrial sector. Inventory for materials and finished products marginally improved but remained in contraction, as the destocking cycle continued with some improvement. Construction price remained in expansion and service price index moderately increased. We expect China's CPI and PPI to mildly rebound in next several quarters along with a gradual recovery of aggregate demand.

■ Service activity softened with better performance in some services related to summer holiday.

Non-manufacturing PMI dropped to 51% in August. PMI in service further declined from 51.5% in July to 50.5% in August. Breaking down by sector, output in transportation, lodging, catering, accommodation and recreation services noticeably expanded during the summer holiday. Business sentiment indexes in retail, postal service, telecom service, TV & broadcast, financial and insurance service remained above 60%. Construction PMI continued to recover to 52.8 in August from 51.2 in July.

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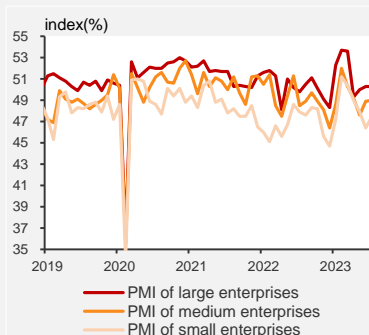
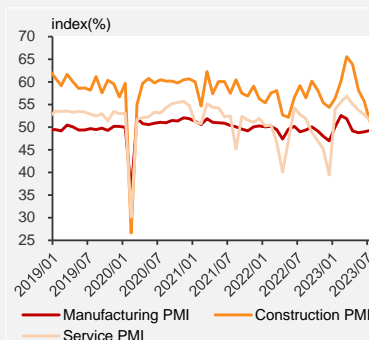
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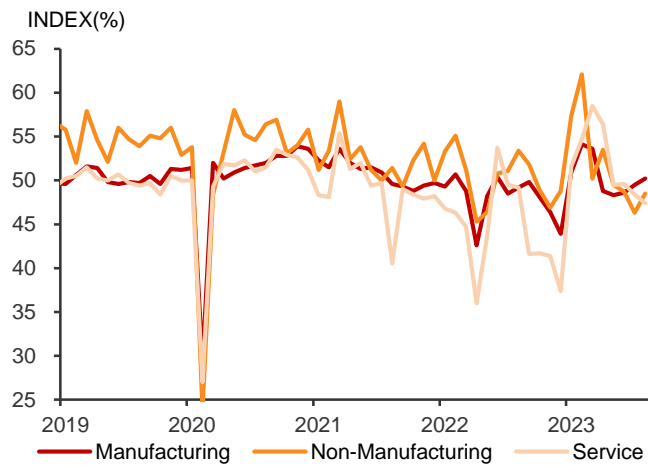
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However, new order index remained in contraction at 48.5 in August compared to 46.3 in July, indicating downside pressure on construction activity in future.

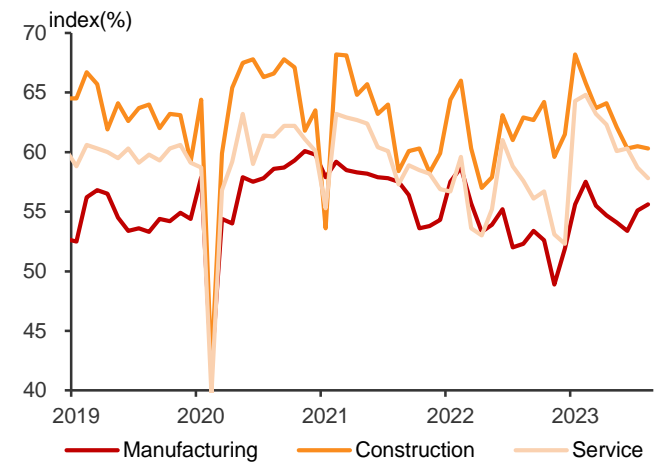
- **Employment still struggled as employment index further deteriorated.** Employment indexes in manufacturing and construction further dipped to 48 and 44.7 in August from 48.1 and 45.2. Employment in service remained in contraction at 47.2. The unemployment concern became increasingly alarming especially after the NBS absurdly ceased the publication of youth and fresh graduates' unemployment data. The weak employment condition will definitely restrain the recovery momentum of household consumption in China.
- **Stronger loosening policies are expected to carry out as China's economy may gradually improve ahead.** Policymakers have adopted a broad spectrum of supportive policies including loosening property policies, expanding credit supply, cutting deposit rates and existing mortgage rates, relieving local government debt risk and activating capital market. Looking ahead, China may further cut RRR, loosen property policy and expand credit supply. The policymakers may restructure local government contingent debt and take measures to boost investor and business confidence. China's economy is expected to gradually improve in next four quarters. We maintain our forecast on the GDP growth at 5.1% for 2023 and 4.8% for 2024.

Figure 1: New Order Index



Source: WIND, CMBIGM

Figure 2: Business Sentiment Index



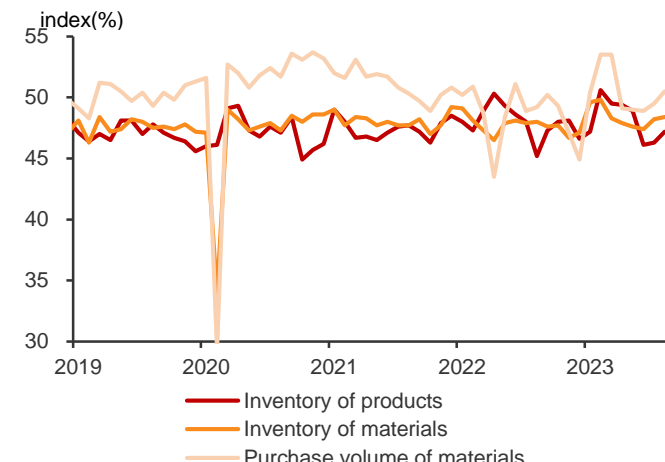
Source: WIND, CMBIGM

Figure 3: Export Order Index and Import Index



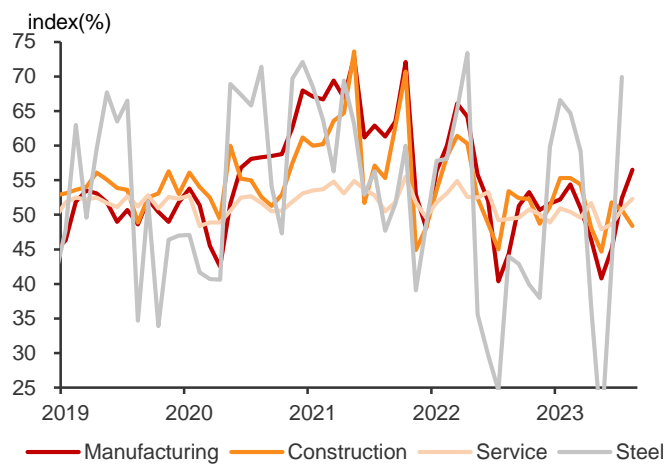
Source: WIND, CMBIGM

Figure 4: Inventory Index



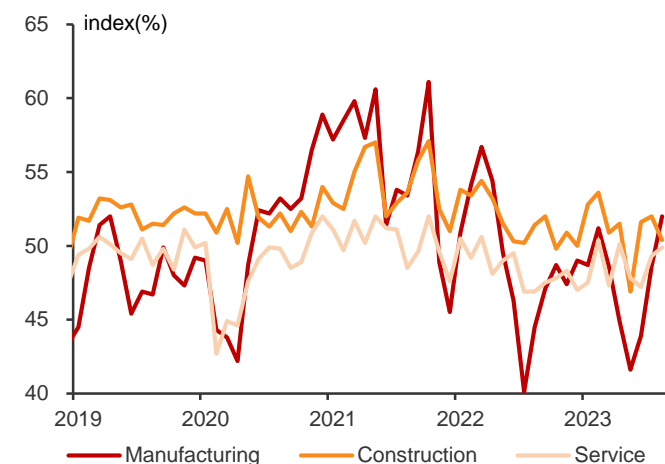
Source: WIND, CMBIGM

Figure 5: Material Purchase Price Index



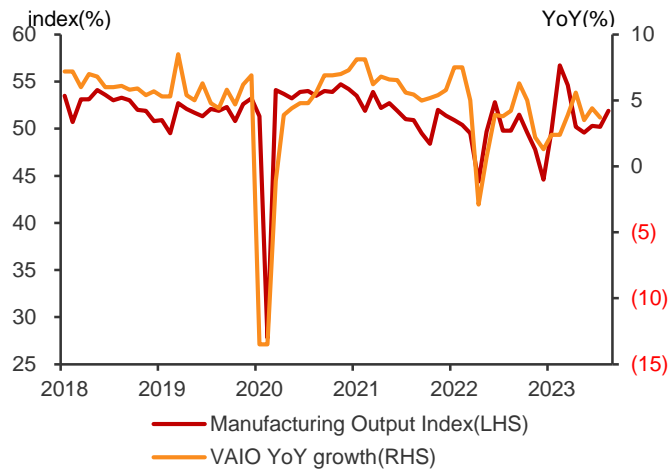
Source: WIND, CMBIGM

Figure 6: Ex-factory Price Index



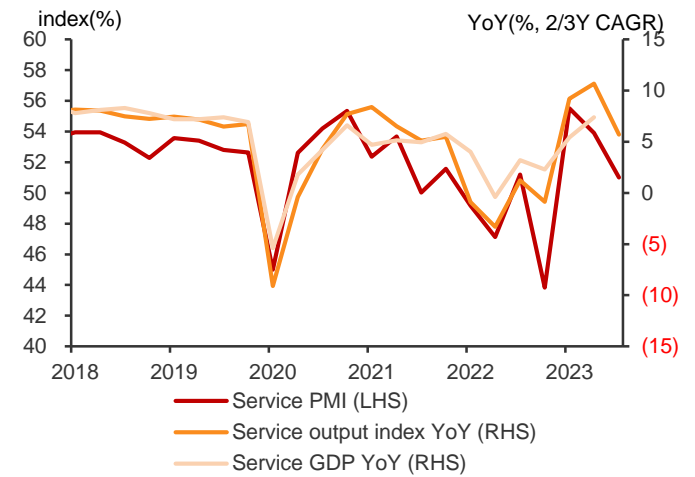
Source: WIND, CMBIGM

Figure 7: Manufacturing Output Index



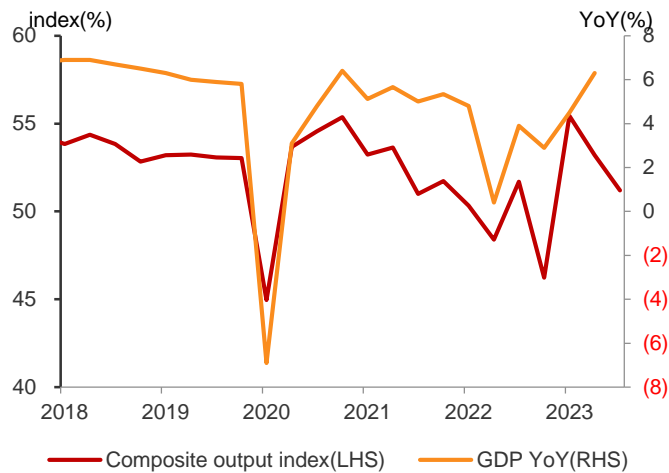
Source: WIND, CMBIGM

Figure 8: Service PMI & Output Index



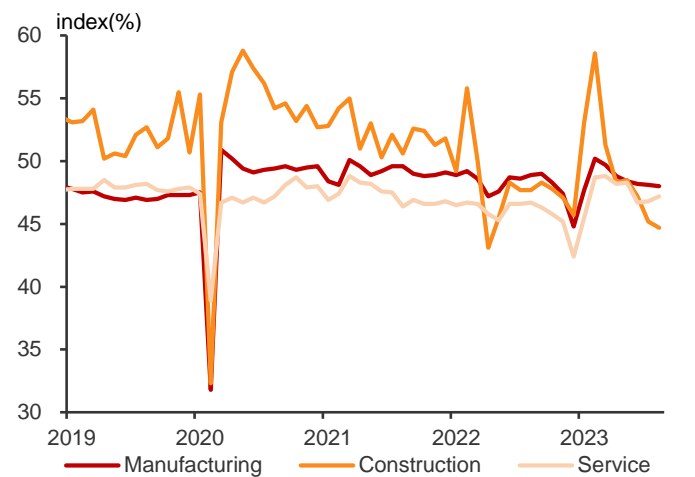
Source: WIND, CMBIGM

Figure 9: Composite Output Index



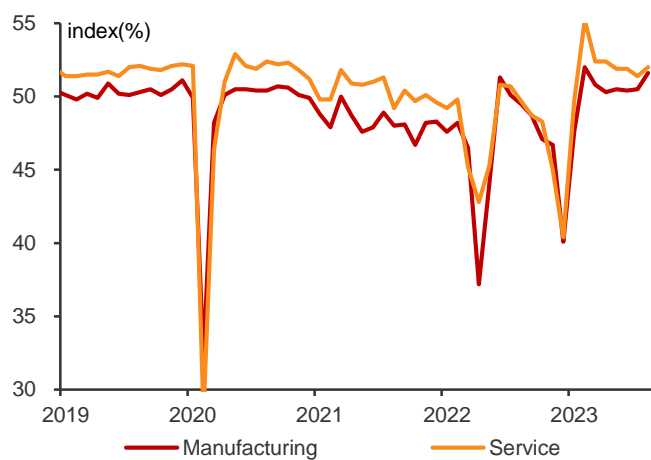
Source: WIND, CMBIGM

Figure 10: Employment Index



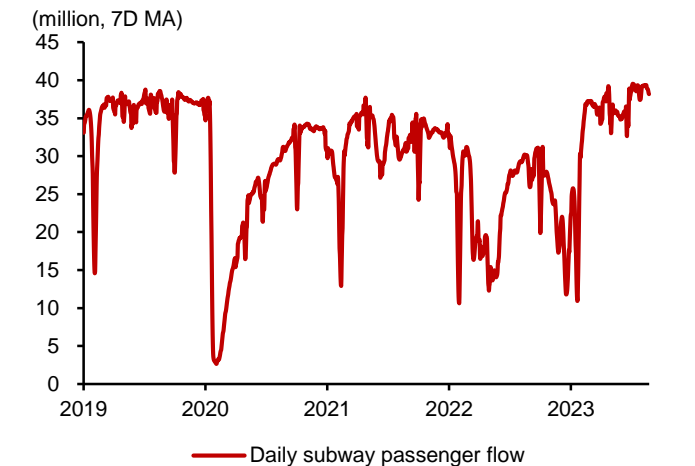
Source: WIND, CMBIGM

Figure 11: Supply Delivery Index



Source: WIND, CMBIGM

Figure 12: Subway Passenger Flow in Tier-1 Cities



Source: WIND, CMBIGM

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