

# China Economy

## Weak PMIs confirm downside pressure for growth

China's manufacturing activity further contracted, while service activity continued to expand yet with noticeable softness. New orders slid deeper into the contraction territory, pointing to further economic slowdown in near term. Deflation pressure increased as manufacturing ex-factory price extended declines and service price softened. Employment condition remained tough as private businesses were still cautious to expand capex. The weak data is negative for Chinese stocks, renminbi exchange rates and commodities which are sensitive to China factor. Looking forward, as the economy continues to weaken, the PBOC may mildly cut LPRs to boost demand in around July. The central bank may also encourage banks to expand credit supply especially to hard technologies and manufacturing sector. However, the possibility of fiscal stimulus on consumption is very low as the policymakers like to control resource to accomplish great tasks rather than letting the market decide resource allocation. The continuous recovery of service sector should provide some support to private SMEs and employment condition, paving the way for better recovery in 2H23. We maintain our forecast on China's GDP growth for 2023 at 5.7%. The 2Y CAGR of GDP is expected to slow from 4.6% in 1Q23 to 4% in 2Q23 before rebounding to 4.3% in 2H23.

- Manufacturing activity further contracted as demand continued to weaken.** China's PMI in manufacturing dropped to 48.8% in May from 49.2% in April, sliding deeper into the contraction territory. Demand in manufacturing softened as new order index dropped from 48.8% in April to 48.3% in May. Meanwhile, export order index and import index declined from 47.6% and 48.9% in April to 47.2% and 48.6% in May. By sector, food, alcoholic beverage & tea, medicine, special equipment, railway & other transport equipment and electrical equipment remained in the expansionary range, while chemical materials & products, non-metal mineral products and ferrous metals were very weak.
- Service activity continued to expand, but the growth slowed.** PMI in construction and service declined from 63.9% and 55.1% in April to 58.2% and 53.8% in May. Construction and service sectors continued to expand, but their growth slowed. New order indexes in construction and service sectors both declined to 49.5% in May from 53.5% and 56.4% respectively in April, pointing to a contraction of demand. By sector, the indexes in railway/ship/air transportation, telecom service, TV & broadcast, internet software and IT service remained above 60%, while those in capital market service, real estate and other business activity fell below 50%.
- Deflation pressure increased as ex-factory price further declined.** Ex-factory price index in manufacturing tumbled from 44.9% in April to 41.6% in May as the producer price index (PPI) may have extended YoY declines in May. The product inventory index and material inventory index in manufacturing respectively declined from 47.9% and 49.1% in April to 47.6% and 49.0% in May as businesses tried to keep their inventory low with bearish expectations about the demand prospect. Service price index also dropped from 50.1% in April to 47.8% in May as demand further weakened. Looking forward, we expect CPI to remain low and PPI to further decline in 2Q23 before gradual rebound in 2H23-2024.

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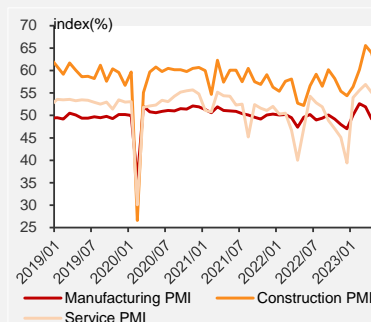
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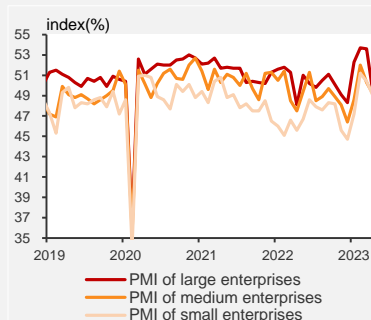
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Source: NBS, CMBIGM

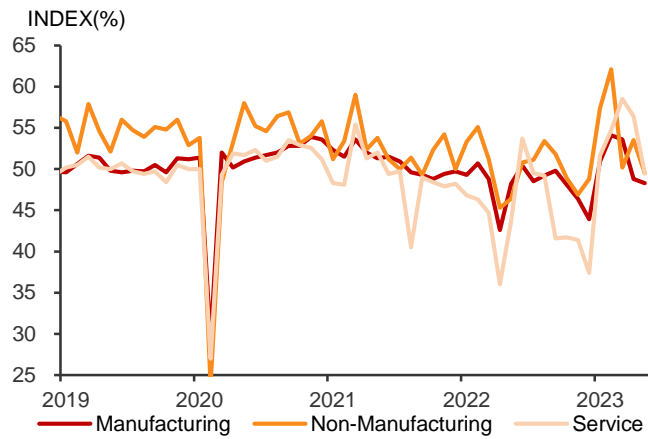


Source: NBS, CMBIGM

■ **Youth unemployment remains a top concern for China's policymakers.**

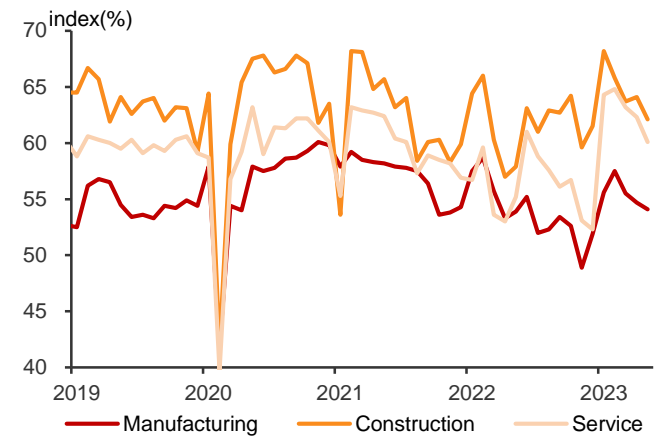
Employment index in manufacturing fell from 48.8% in April to 48.4% in May. Unemployment rate among youth and fresh graduates hit record high in April as job opportunities remained insufficient. Unemployment among those aged 16-24 increased from 19.6% in March to 20.4% in April, pointing to bleak prospects in China's job market amid weak economy as more students are graduating in recent months. The weak employment condition was mainly due to low confidence in private business community as private enterprises accounted for over 80% in total urban employment in China. The employment condition will determine the pace of China's consumption recovery by affecting consumer income and confidence. China has to boost confidence in private business to improve the employment condition and consumption recovery.

**Figure 1: New Order Index**



Source: WIND, CMBIGM

**Figure 2: Business Sentiment Index**



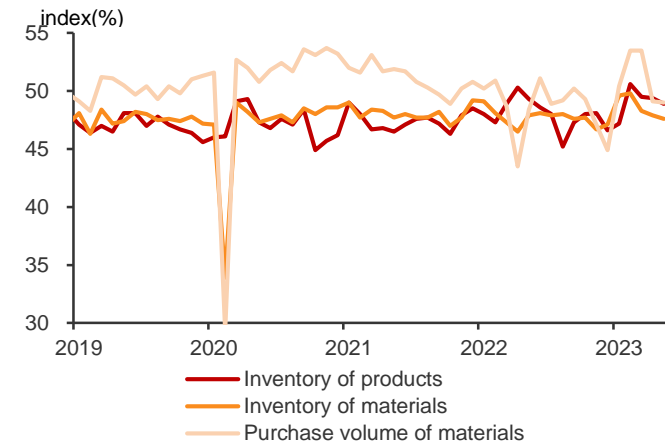
Source: WIND, CMBIGM

**Figure 3: Export Order Index and Import Index**



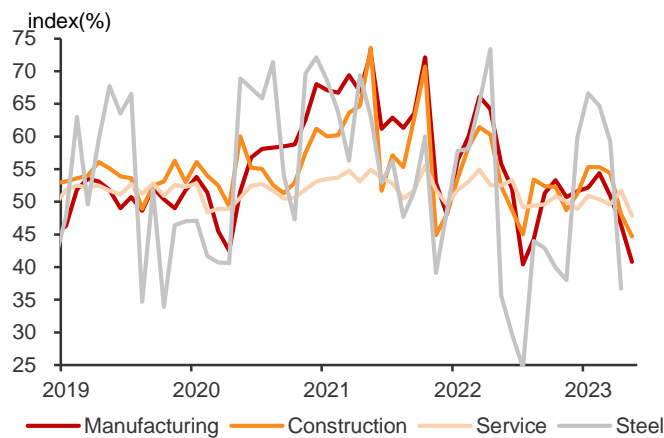
Source: WIND, CMBIGM

**Figure 4: Inventory Index**



Source: WIND, CMBIGM

**Figure 5: Material Purchase Price Index**



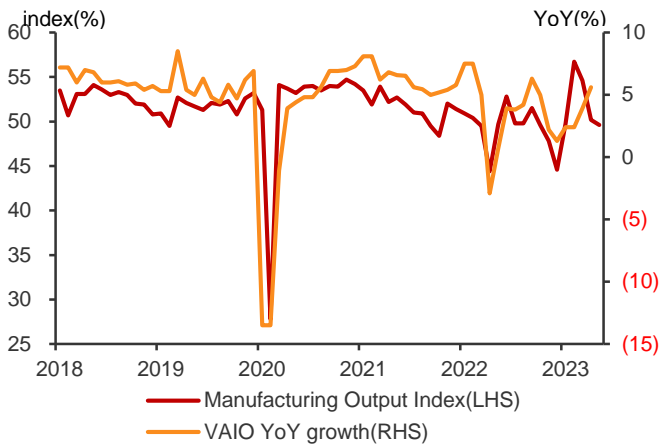
Source: WIND, CMBIGM

**Figure 6: Ex-factory Price Index**



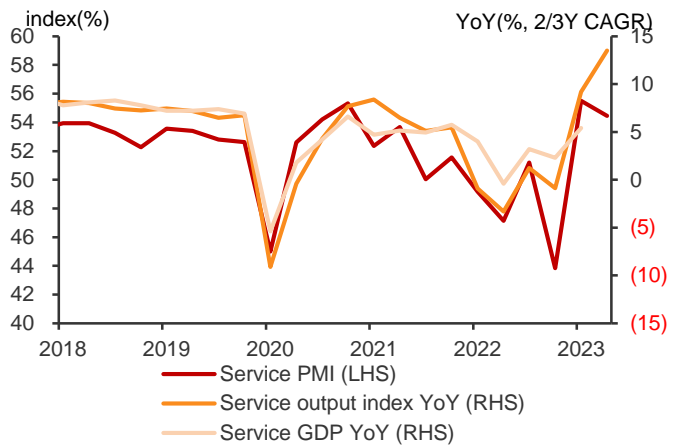
Source: WIND, CMBIGM

**Figure 7: Manufacturing Output Index**



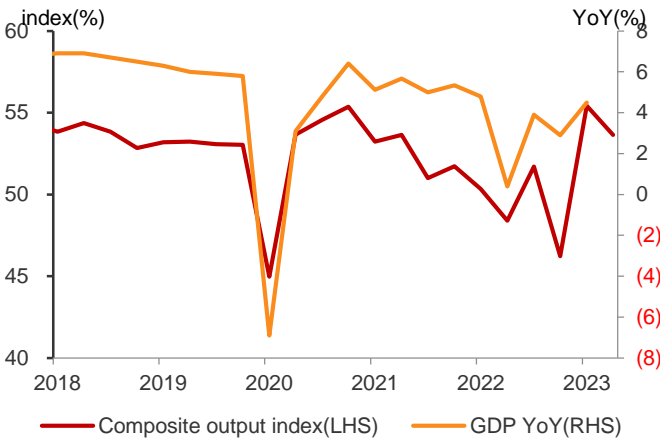
Source: WIND, CMBIGM

**Figure 8: Service PMI & Output Index**



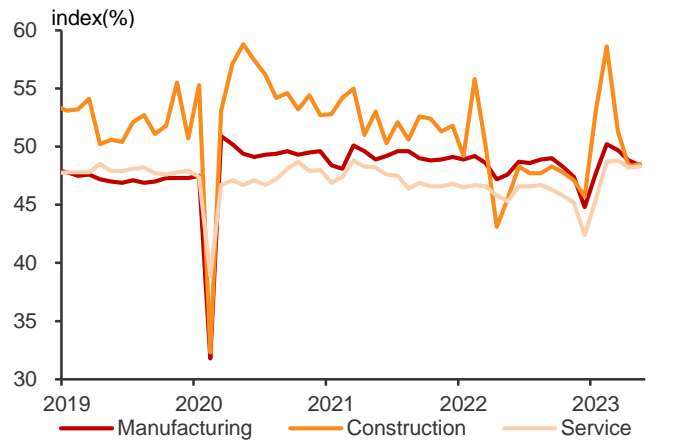
Source: WIND, CMBIGM

**Figure 9: Composite Output Index**



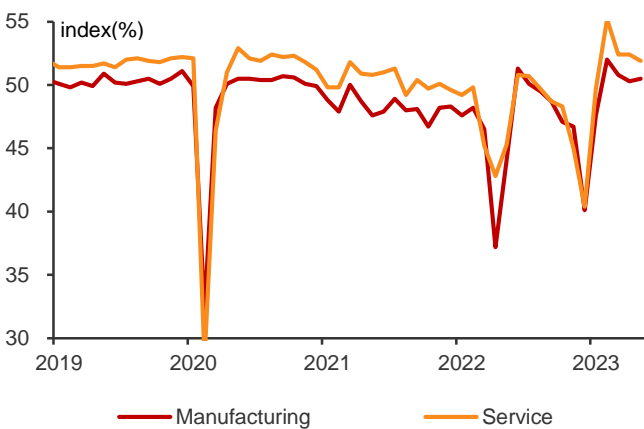
Source: WIND, CMBIGM

**Figure 10: Employment Index**



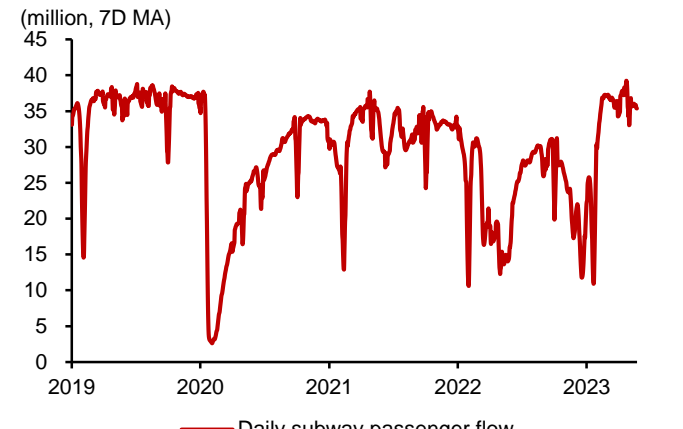
Source: WIND, CMBIGM

**Figure 11: Supply Delivery Index**



Source: WIND, CMBIGM

**Figure 12: Subway Passenger Flow in Tier-1 Cities**



Source: WIND, CMBIGM

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