

# China Economy

## PMI dropped to contraction calling for additional policy easing

China's manufacturing PMI came in below market expectation at 49.5 in Oct, after only one month of expansion in Sep. All of the 5 sub-indexes that made up the headline PMI worsened, in which new order, inventory and employment all remained in contraction territory. Manufacturing activities in large, medium and small enterprises all further dropped. Export order and import indexes further contracted, pointing to a still-weak external and domestic demand. Due to the pullback of energy and commodity prices, material purchase price index and ex-factory product index substantially dipped, dragging on the reflation trend in future. Employment in manufacturing and service remained tedious due to still-soft labour demand and industrial upgrading towards higher labour productivity. Service and construction PMI both deteriorated as real estate market continued to tumble. After two months of stabilization, China's economy softened again, calling for additional policy easing. We believe China will further loosen its fiscal policy and monetary policy while maintaining GDP growth target at 5% for 2024. Broad deficit ratio and credit growth may mildly rise in 2024. We maintain the GDP growth forecast for 2023 at 5.2% and the forecast for 2024 at 4.9%.

- **Manufacturing activity dropped to contraction after only one month of expansion.** China's PMI in manufacturing came in below expectation and contracted to 49.5% in Oct from 50.2% in Sep. Production index slowed down to 50.9% in Oct from 52.7% in Sep. New order and material purchase volume both ceased their two-month expansion and dropped to 49.5% and 49.8% from 50.5% and 50.7% in Sep, indicating a deterioration on the demand side. Breaking down by sector, new order indexes in equipment manufacturing and consumer goods reached above 50%, while textile, chemical products and steel products remained in the contractionary range. Both export and import indexes continued to worsen while both remained in contraction, indicating soft domestic and foreign demand in Oct. PMI of large, medium and small enterprises all worsened in Oct, while both small and medium enterprises remained in contraction.
- **Reflation trend softened after the pullback of energy and commodity prices.** Ex-factory price index railed back to contraction from 53.5% in Sep to 47.7% in Oct while manufacturing material purchase price worsened from 59.4% in Sep to 52.6% in Oct, indicating the deflation concerns are back on the table, after the easing of energy and commodity prices. Inventory for materials slightly worsened and finished products improved, as the destocking cycle continued with limited improvement. Construction price and service price index moderately dropped. Looking forward, China's CPI and PPI may gradually rebound in the next several quarters along with a mild recovery of aggregate demand.
- **Non-manufacturing sectors worsened as both construction and service were lower than expected.** Non-manufacturing PMI dropped to 50.6% from 51.7% in Sep. PMI in service fell from 50.9% in Sep to 50.1% in Oct. Breaking down by sector, output in railroad & air transportation, postal service and TV & broadcast noticeably expanded while capital market and real estate services fell below 50%. Business sentiment indexes in construction and services both drop around 0.5bps but still remained in highly expansion zone. Construction PMI dropped to 50.1% in Oct from 50.9%. The new order index continued to worsen to 49.2% from 50%.

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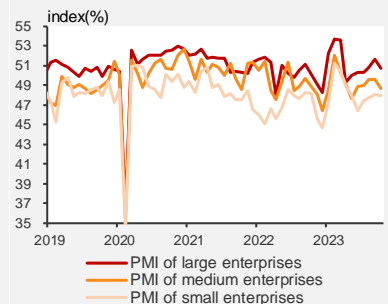
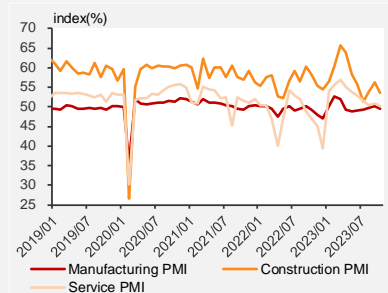
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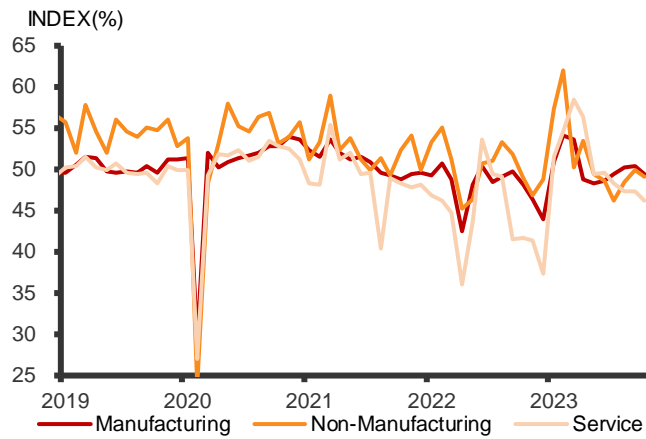
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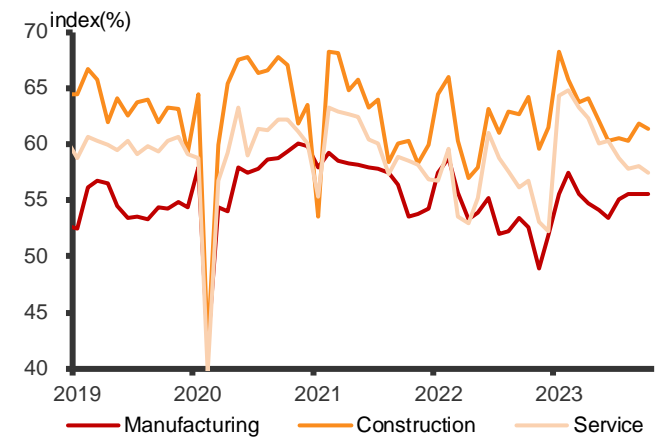
- **Employment still struggled as employment index further deteriorated.** Employment remained in deep contraction as employment indexes in manufacturing and service continued to drop to 48% and 46.5% in Sep from 48.1% and 46.9% in Sep while employment in construction marginally improved to 46.4% in Oct from 46.3%. The weak employment condition will restrain the recovery momentum of household consumption in China and be a major drag on the economic growth.
- **China may further loosen fiscal and monetary policies ahead.** The recent fiscal stimulus indicates Chinese policymakers' stronger commitment to restoring market confidence and shoring up the economy as the economy dipped again in Oct. Although GDP growth beat expectations in 3Q23, severe challenges are likely to persist into 2024, including property market stress, deflation pressure and global economic uncertainty. The Chinese policymakers may continue to launch supportive policies ahead to boost market confidence and economic growth momentum. 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. In addition, China will continue to improve ties with the US and other countries to lower geopolitical risks as we expect a Xi-Biden summit in November. We maintain the GDP forecast for 2023 at 5.2% and that for 2024 at 4.9%.

**Figure 1: New Order Index**



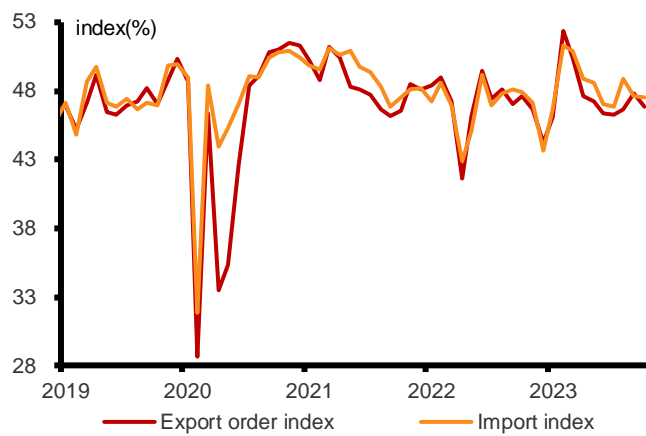
Source: WIND, CMBIGM

**Figure 2 : Business Sentiment Index**



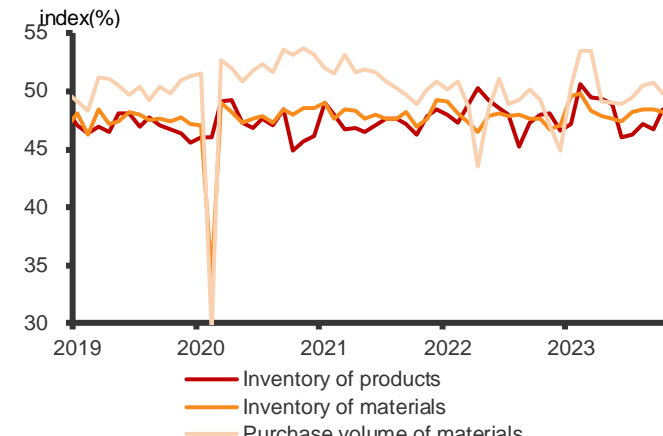
Source: WIND, CMBIGM

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



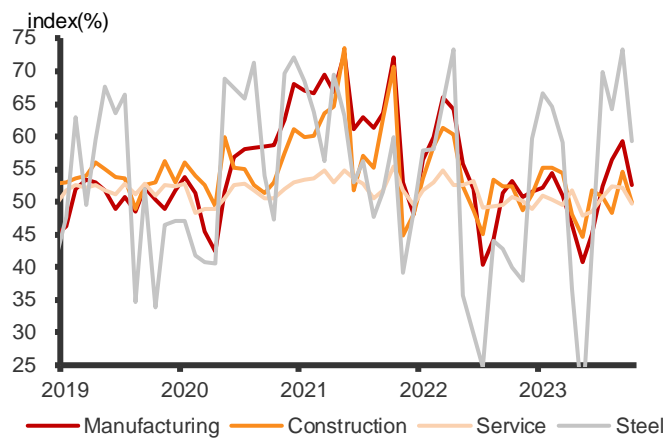
Source: WIND, CMBIGM

**Figure 4: Inventory Index**



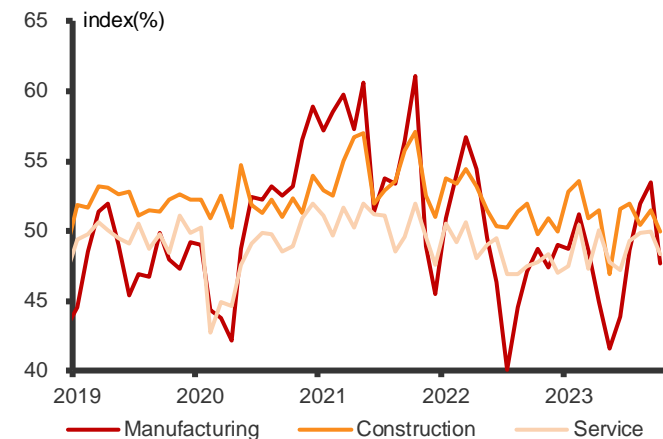
Source: WIND, CMBIGM

**Figure 5: Material Purchase Price Index**



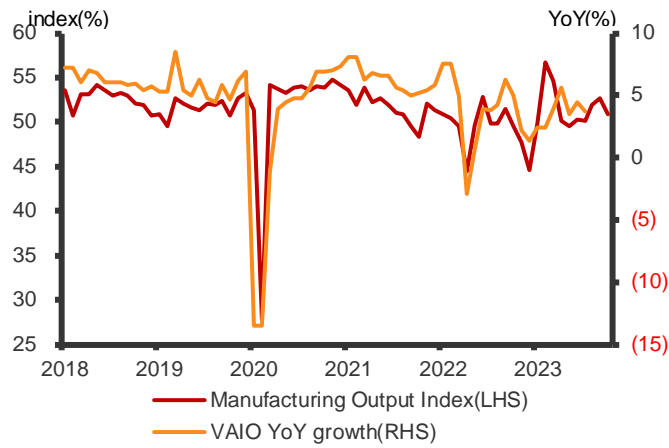
Source: WIND, CMBIGM

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



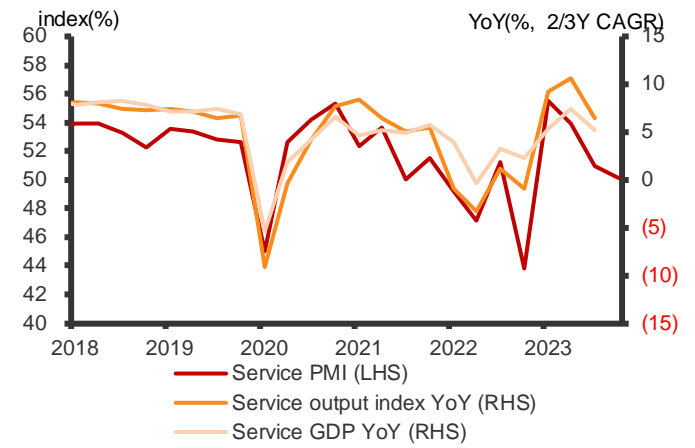
Source: WIND, CMBIGM

**Figure 7: Manufacturing Output Index**



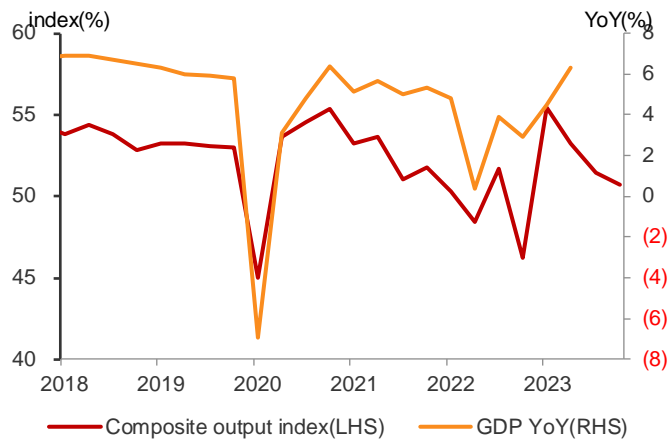
Source: WIND, CMBIGM

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



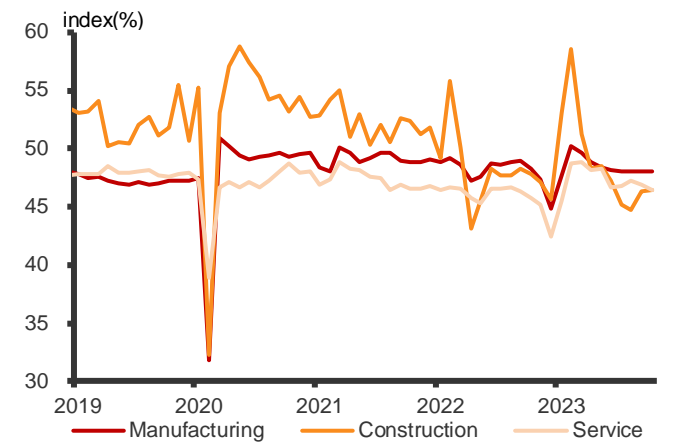
Source: WIND, CMBIGM

**Figure 9: Composite Output Index**



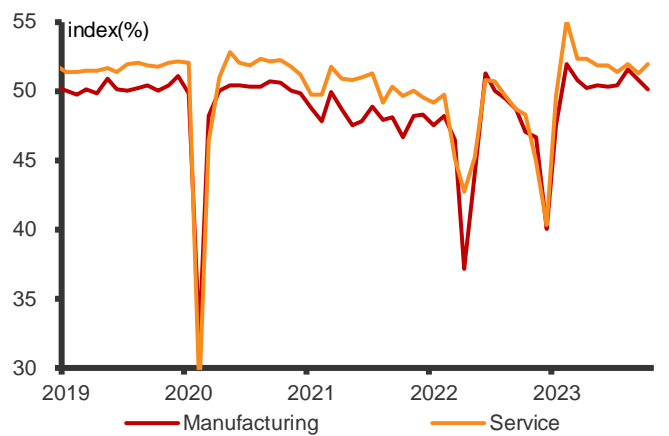
Source: WIND, CMBIGM

**Figure 10: Employment Index**



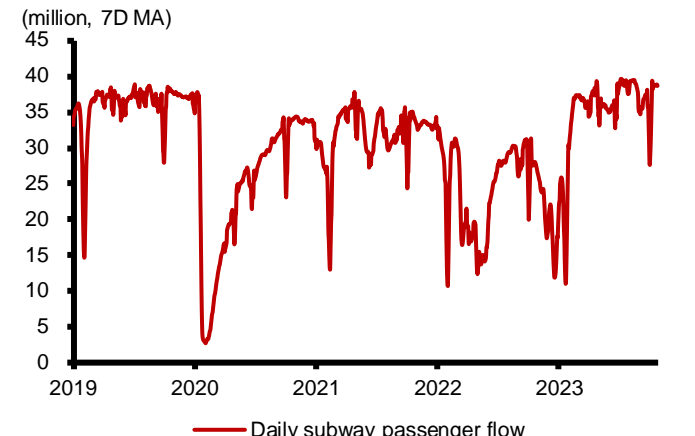
Source: WIND, CMBIGM

**Figure 11: Supply Delivery Index**



Source: WIND, CMBIGM

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



Source: WIND, CMBIGM

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