

CHINA DATA RESPONSE

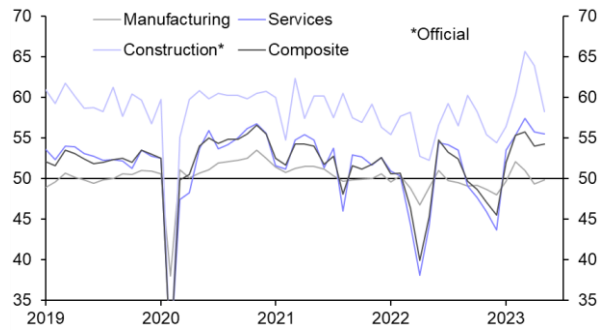
PMIs (May)

Recovery still making headway

- *This report has been updated with additional analysis and charts since first publication.*
- **The PMI surveys suggest that China's economic recovery was still ongoing in May. Waning fiscal support weighed on construction activity. But manufacturing output ticked up and the service sector is still seeing decent gains, suggesting that Q2 GDP growth may not be as bad as many fear.**
- The official manufacturing PMI declined from 49.2 in April to 48.8 in May (the Bloomberg consensus was 49.5, our forecast was 49.0). In contrast, the Caixin manufacturing PMI rose from 49.5 to 50.9, above expectations (the Bloomberg consensus was 49.5 and our forecast was 49.0).
- **The average of the two picked up and is consistent with easing downward pressure in factory activity last month.** (See Chart 1.) Given differences in the composition of the firms surveyed, the decline in the official index suggests that larger firms and those located inland are facing the greatest headwinds.
- We think it makes sense to average across both PMIs to gauge conditions in industry and get a sense of what they mean for the hard data. On this basis, after pointing to stagnation in April, the output component rose and points to a modest expansion last month. But both the new orders and new export orders components are still consistent with weak demand – the new orders index is at 50.0 while new exports orders remains below 50.
- **Still soft demand is resulting in greater slack in supply chains** – supplier delivery times shortened more rapidly while backlog of orders reduced further. The output price component dropped back again, and points to a roughly 1% m/m decline in producer prices in May, which would be the largest in nine months.
- The official non-manufacturing PMI dropped back from 56.4 to 54.5 (Bloomberg: 55.0, CE: 56.0). The services index declined from 55.1 to 53.8. In contrast, the Caixin services PMI rose from 56.4 to 57.1 (Bloomberg: 55.2, CE: 56.0). **The average of the two edged down slightly but is still consistent with a rapid expansion in services activity last month.** (See Chart 1 again.)
- Meanwhile, the official construction index fell from 63.9 to 58.2, a four-month low. This suggests that the prop to infrastructure spending from the front-loading of fiscal support this year is now starting to fade.
- All told, the average of the official and Caixin composite PMI edged up (see Chart 1 again) and is consistent with slightly faster gains in economic output last month.
- Furthermore, there is still some scope for improvements in consumer activity over the coming months as the labour market continues to tighten and wage growth picks up – the employment components of the PMIs edged down in May but they remained above their five-year average for services, the sector responsible for the bulk of urban job creation.
- **Currently, the composite PMI points to official GDP growth of around 2.5% q/q this quarter (assuming no change in June).** (See Chart 2.) **That's higher than the 1.8% q/q we have pencilled in for Q2, and leaves us comfortable with our above-consensus GDP forecast of 6.5% for this year.**

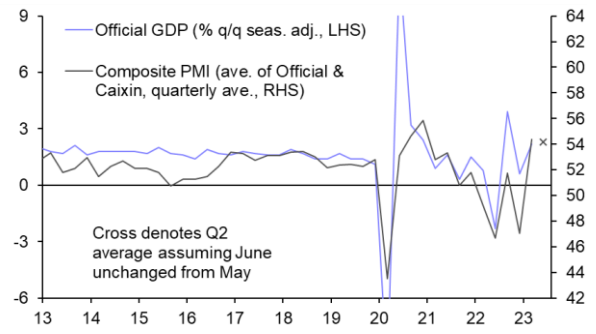


Chart 1: PMIs (Average of Official and Caixin PMIs)



Sources: CEIC, Capital Economics

Chart 2: Official GDP & Composite PMI



Sources: CEIC, WIND, Capital Economics



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