

CHINA RAPID RESPONSE

PMIs (Jun.)

Growth now below pre-pandemic levels

- *This report has been updated with additional analysis and charts since first publication.*
- **The PMI surveys suggest that China's reopening recovery continued to lose momentum in June. Downward pressure on manufacturing persisted. Waning fiscal support weighed on construction activity. And even service sector growth, a bright spot earlier this year, has now dropped below pre-pandemic levels. The economy should still make some headway during the rest of the year provided that greater policy support is forthcoming, but the gains are likely to be modest.**
- We learned on Friday that the official manufacturing PMI edged up from 48.8 in May to 49.0 in June (the Bloomberg consensus and our forecasts were 49.0). Monday's release, by contrast, showed that the Caixin manufacturing PMI fell from 50.9 to 50.5, above expectations (Bloomberg and CE: 50.0).
- **The average of the two edged down and is consistent with some deterioration in factory activity last month.** (See Chart 1.) Given differences in the composition of the firms surveyed, the decline in the Caixin index suggests tailwinds benefiting smaller firms and those located closer to the coasts are fading.
- 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, the output component fell. This appears to reflect increased downward pressure on foreign demand. The new orders component was broadly unchanged. Meanwhile, the export orders component declined further to a five-month low of just 48.2, and points to a renewed drop in exports. (See Chart 2.)
- The official non-manufacturing PMI, also released on Friday, dropped back from 54.5 to 53.2 (Bloomberg: 53.7, CE: 52.0). (See Chart 1 again.) This was largely due to a decline in the services index from 53.8 to 52.8, its lowest since reopening and slightly below pre-pandemic levels – the average in 2019 was 53.1. Wednesday's release of the Caixin services PMI showed a decline as well, from 57.1 to 53.9 (Bloomberg: 56.2, CE: 54.0). **Taken together, both surveys suggest that, after a short-lived reopening boost, the service sector appears to be settling into a new post-pandemic normal of slower growth.**
- Meanwhile, the official construction index fell from 58.2 to 55.7, a six-month low. (See Chart 1 again.) This suggests that the pick-up in infrastructure spending earlier in the year, which had helped to offset further weakness in real estate, continued to unwind in June as fiscal support was pared back.
- **All told, the average of the official and Caixin composite PMI fell in June. As a result, the labour market appears to be softening again.** The composite employment index weakened and hints at an uptick in the unemployment rate. (See Chart 3.)
- Thanks to its strength earlier in the quarter, the composite PMI is, on past form, still consistent with Q2 GDP growth of around 1.5% q/q. (See Chart 4.) But the hard data have been less resilient recently and suggest that growth will come in a bit lower – our forecast is 1.2% q/q.
- **Looking forward, policy support will be key to preventing a further deceleration in growth.** Aside from some token rate cuts, officials have so far been slow to announce meaningful stimulus. Thursday's State Council meeting reportedly discussed measures to boost consumption as well as spending on urban renovation projects. But **unless concrete support is rolled out soon, the recent downturn in demand risks becoming self-reinforcing.**



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

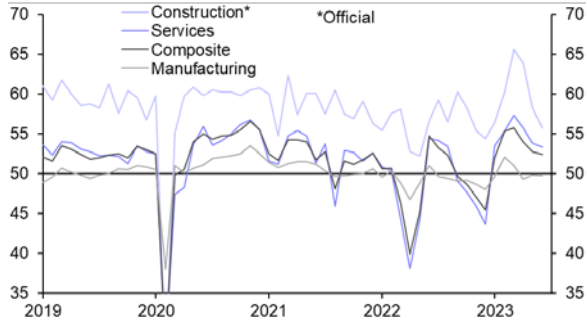


Chart 2: Exports & Official PMI – Export Orders

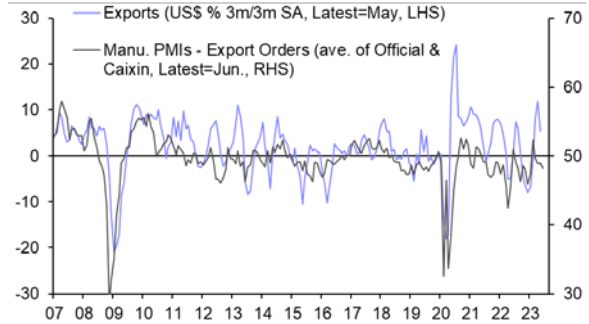


Chart 3: Unemployment Rate & Composite PMI

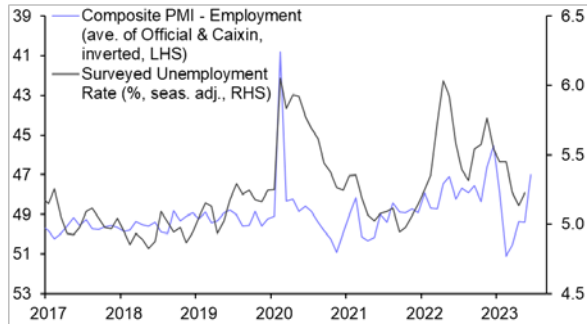
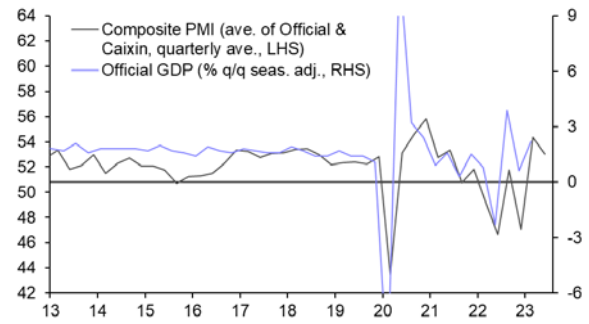


Chart 4: Official GDP & Composite PMI



Sources: CEIC, Capital Economics



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