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Markit Economic Research
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China

PMI signals export-led stabilisation of manufacturing economy

- **Manufacturing PMI™ hits five-month high**
- **New export orders show largest rise since late-2010, but domestic demand remains weak**
- **Employment continues to fall**
- **Output charges rise for first time since November, albeit marginally**

Business conditions in China's manufacturing economy deteriorated for a fifth successive month in May, according to the flash PMI produced by Markit for HSBC. However, the rate of deterioration was only marginal and the weakest recorded so far this year.

At 49.7 in May, the PMI rose from 48.1 in April to reach a five-month high. The upturn pushes the average reading for the second quarter up to 48.9 compared to a first quarter average of 48.7, providing the first hint that GDP growth could accelerate from the recent low of 7.4% seen in the opening quarter of the year.

Export-driven upturn

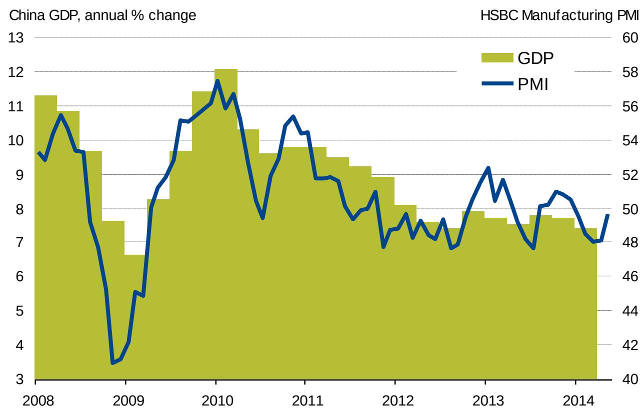
The survey pointed to the first increases, albeit only marginal, in output and new orders since January, with the increase in new orders driven by the largest rise in new export sales since November 2010. The outperformance of exports relative to total order books points to ongoing weakness of domestic demand in China. PMI data have indicated substantially better export performance than official trade data in recent months, reflecting an ongoing economic recovery in key markets such as the US, the Eurozone, the UK and Japan.

Restocking

The increase in sales took companies by surprise, on average, causing inventories of finished goods to register the largest decline since last July. The resulting orders-to-inventory ratio, which acts as a useful guide to future production trends, rose to a five-month high as a result.

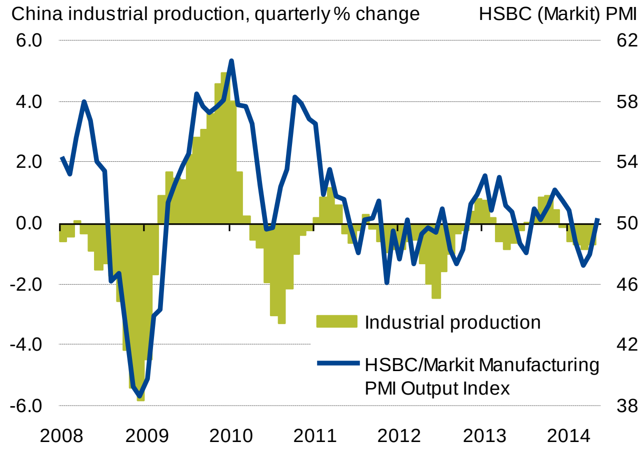
An upturn in production in June was also hinted at by companies increasing their purchases of raw materials

Economic growth and the manufacturing PMI



Sources: Markit, Ecowin.

Industrial production



Sources: Markit, NBS (via Ecowin).

Order books

Source: Markit.

Sources: Markit, NBS (via Ecowin).

for the first time in four months, boosting their inventory holdings of inputs for the first time since January.

Focus on cost-cutting

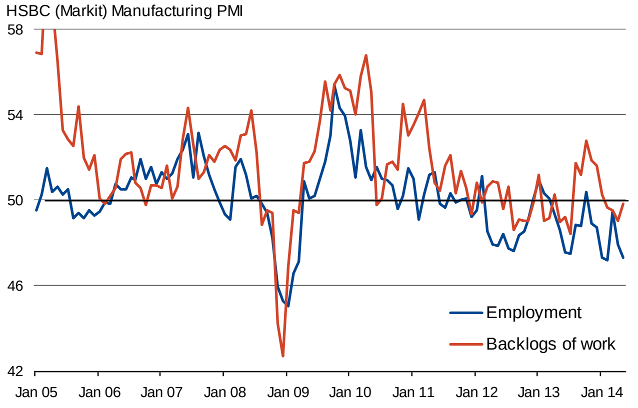
Less encouraging in relation to the outlook was the ongoing drop in manufacturing headcounts, which fell at the steepest rate since February as many firms remained focused on raising productivity and keeping costs low. The drop in employment was one of the largest seen since the height of the global financial crisis in 2008-9.

Prices stabilise

Prices meanwhile showed signs of stabilising. Having fallen significantly in prior months, average input prices fell only marginally in May; the weakest decline since costs began falling at the start of the year. Average selling prices rose marginally for the first time since last November.

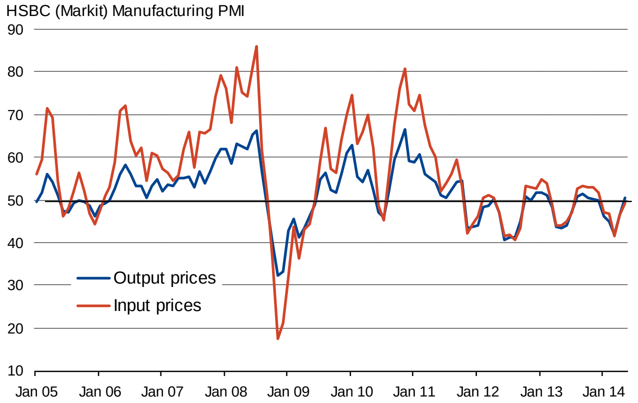
The absence of either significant deflationary or inflationary pressures was corroborated by the suppliers' delivery times index. This measure of supply chain capacity constraints continued to run at a neutral level, consistent with neither a buyers' nor a sellers' market and signalling consumer price inflation in the region of 2%.

Operating capacity



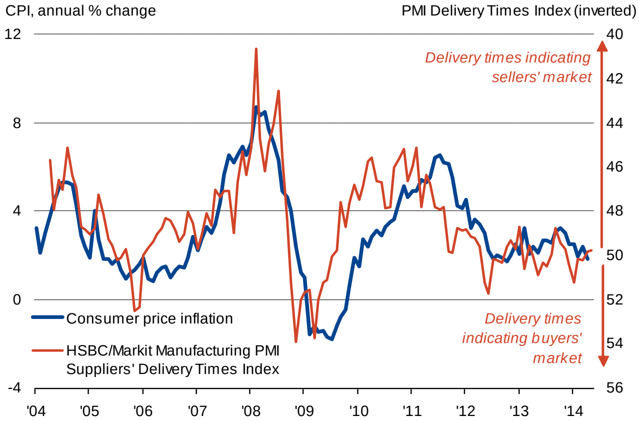
Source: Markit.

Input and output prices



Source: Markit.

Suppliers' delivery times and inflation



Sources: Markit, NBS (via Ecowin).

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