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Markit Economic Research
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China manufacturing

Robust start to third quarter as flash PMI hits one-and-a-half year high

- **Flash manufacturing PMI™ highest since start of 2013**
- **Output and new order growth accelerates**
- **Pace of job shedding eases**
- **Survey points to ongoing improvement in domestic demand plus signs of export pick up**

Growth of China's manufacturing economy accelerated to the fastest for a year and a half in July, according to the first PMI-based snapshot of business conditions. An upturn in export growth signalled by the survey also suggests that global economic growth is reviving as we move into the second half of 2014, providing a welcome accompaniment to signs of an ongoing improvement in domestic demand within China.

The manufacturing PMI rose from 50.7 in June to 52.0 in July, its highest since January 2013, according to the flash reading produced by Markit for HSBC. July was the second successive month in which an improvement in business conditions has been signalled, following five months of decline.

The flash estimate is based on approximately 85% of usual monthly replies and acts as a reliable guide to the final data, which will be next published on 1 August.

Faster economic growth

The improvement will fuel hopes that the government is on course to meet its 7.5% growth target for 2014. At 49.4, the average PMI reading for the second quarter was up from 48.7 in the first quarter, an improvement that was later confirmed by official data showing growth of gross domestic product accelerating from an annual rate of 7.4% in the first three months of the year to 7.5% in the second quarter. The latest reading of 52.0 therefore points to a further acceleration of growth at the start of the third quarter.

The upturn in the headline PMI was driven by faster rates of increase for both output and new orders, as well as a reduction in the rate of job losses compared to prior months.

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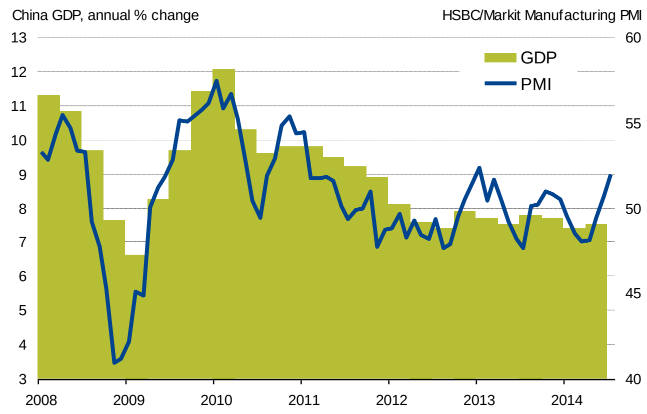
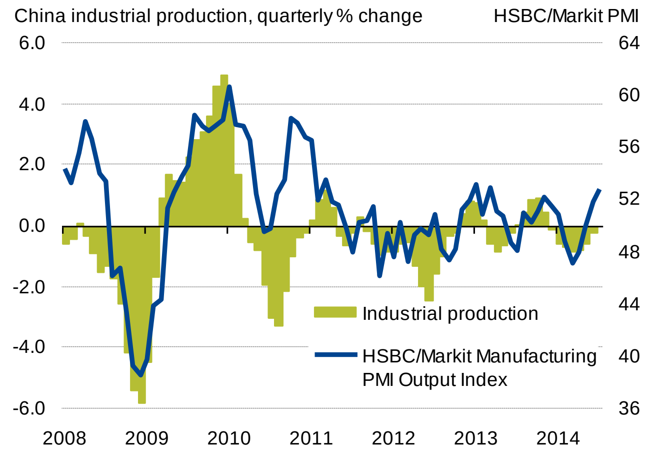
Economic growth and the manufacturing PMI



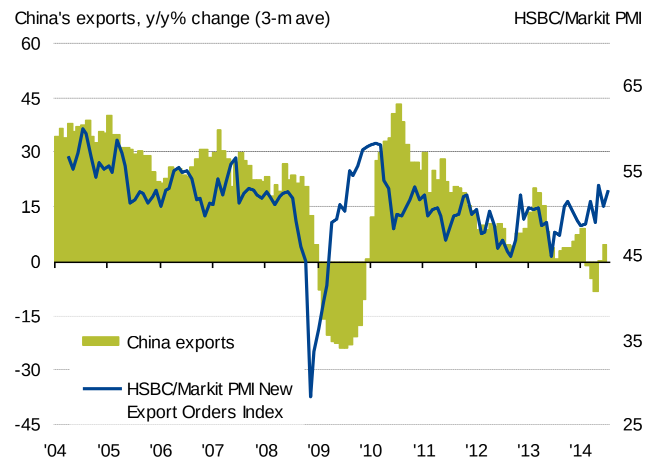
Sources: Markit, Ecowin.

Industrial production



Sources: Markit, NBS (via Ecowin).

Exports



Sources: Markit, NBS (via Ecowin).

Industrial production set to rise in third quarter

The flash PMI data showed manufacturing output rising at the fastest rate since March of last year, indicating that industrial production should return to growth in the third quarter after declining in the first two quarters of the year.

While the recent upturn in the PMI Output Index correctly anticipated the easing in the quarterly rate of decline of industrial production from 0.8% to 0.2% between the first and second quarters, historical comparisons suggest the July PMI Output Index reading is roughly indicative of industrial production rising at a quarterly rate of 1.0% at the start of the third quarter.

Economy buoyed by rising exports and improved domestic demand

Behind the rise in production during July was a second successive monthly improvement in firms' order books. The latest expansion of new business was the strongest since January of last year, buoyed in turn by the second-largest monthly increase in new export orders since November 2010, the expansion of which fell just shy of the recent peak seen in May. Export orders have now risen for three straight months, pointing to strengthening demand in key trade markets and boding well for global economic growth.

However, with overall order books still rising at a faster pace than export orders in July, the survey also suggests that stimulus measures implemented by the Chinese authorities are lifting domestic demand and helping to revive growth.

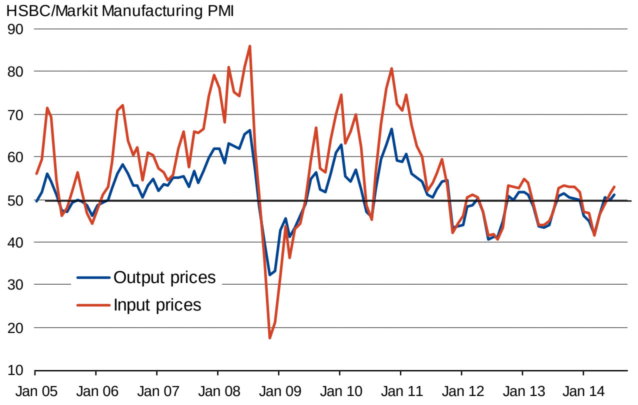
There were several signs that production will continue to rise in August. First, the amount of inputs bought by firms for use in production showed the steepest rise for one and a half years as firms rebuilt stock levels. Stocks of inputs showed the largest rise since March 2010 as a result. Second, backlogs of work also rose, albeit only modestly, for a second successive month, suggesting firms will continue to boost production to help clear outstanding business.

Employment, in contrast, continued to fall as firms sought to cut costs and boost productivity. However, the July survey pointed to the smallest drop in employment for nine months, raising the possibility that staffing numbers could stabilise or even start to rise again in August if sales continue to improve.

Finally, price trends picked up slightly during the month. Manufacturers' input prices showed the biggest monthly rise since November, and selling prices were raised to the greatest extent since September.

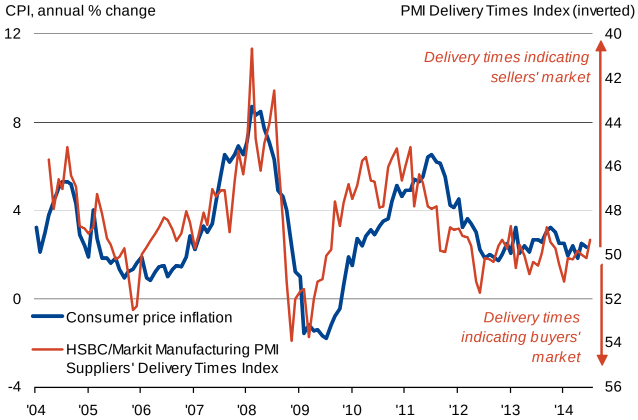
Although on the rise, the lack of bottlenecks in the manufacturing supply chain (as signalled by only a very modest increase in supplier delivery times) points to a general lack of inflationary pressures.

Input and output prices



Source: Markit.

Suppliers' delivery times and inflation



Sources: Markit, HSBC, NBS (via Ecowin).

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