

PMI Quarterly on China Manufacturing

PMI 1Q21

Robust growth in manufacturing production and economic activity

Policy Outlook

China to maintain necessary policy support for economy

2Q21 Forecasts

Real GDP growth to reach 8.0% yoy while PMI to fluctuate within 51.0 to 52.0

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PMI points to robust growth in manufacturing production and economic activity in 1Q21

Our observations

- Expansion of large enterprises accelerates while medium and small enterprises return to expansion.
- Manufacturing production expands at a relatively rapid pace as overall demand picks up fast.
- New export orders increase amid a sustained recovery in external demand.
- Prices of production inputs surge, adding cost pressures on Chinese manufacturers.
- Manufacturers raise ex-factory prices of their products amid increasing cost pressures and improving sales environment.
- Manufacturing employment increases alongside a strong recovery in the export sector and overall economy.

Policy outlook

- The Chinese government will maintain necessary policy support for the economy.
- The proactive fiscal policy will be implemented in a manner that is of higher quality, more effective and more sustainable. Meanwhile, the prudent monetary policy will be pursued in a more flexible, tailored and appropriate way, with steps to ensure 'reasonably sufficient' liquidity and a stable macro leverage ratio.
- These policies will help promote the continued recovery of the Chinese economy.

Our forecasts for 2Q21

- We project a further expansion of manufacturing production and economic activity in 2Q21.
- The headline PMI will stay above 50 and fluctuate within 51.0 to 52.0.
- Real GDP growth will reach 8.0% yoy.
- VAIO growth will top 8.5% yoy.
- Exports will jump by over 15.0% yoy.
- Year-on-year growth rates for both the purchaser price index and the PPI will rise further and reach their near-term peaks.

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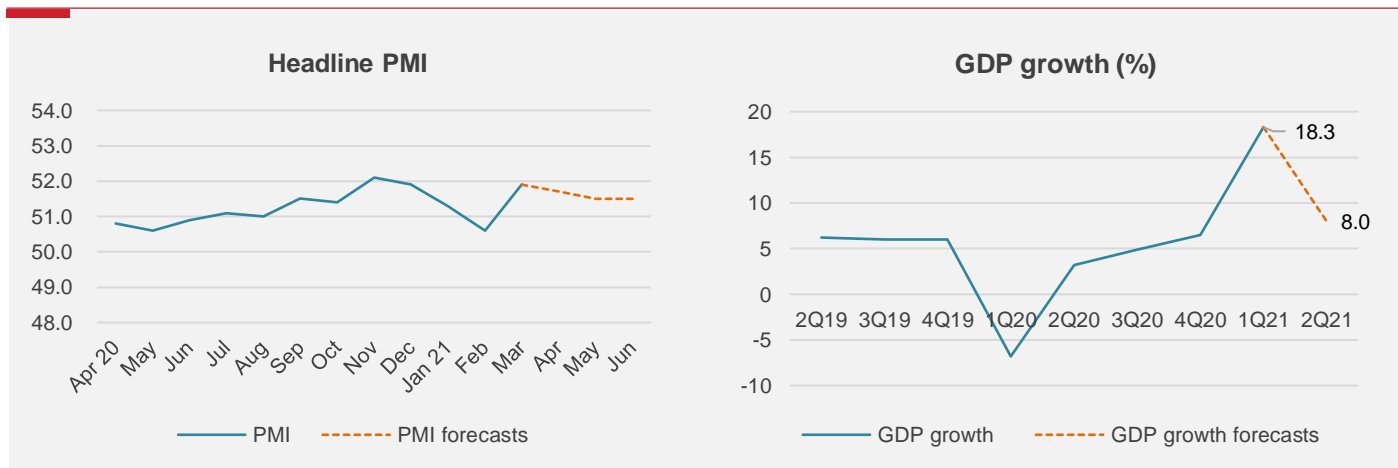
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1. PMI points to robust growth in manufacturing production and economic activity in 1Q21

China's manufacturing sector and economy in 1Q21

After dropping from 51.3 in January to 50.6 in February as the Chinese New Year holidays suppressed factory activity in the month, China's manufacturing PMI rose to 51.9 in March. Looking beyond the distortion caused by the Chinese New Year holidays, the PMI readings indicate a robust growth in the manufacturing sector in 1Q21. (See exhibit 1)

Production activities have expanded at a relatively fast pace lately, as the output index came in at 53.9 in March. The expansion was supported by a fast growth in overall new orders: The new orders index rose to 53.6 in March.

Prices of industrial products have increased: The ex-factory prices index rose from 57.2 in January to 59.8 in March. The jump in product prices was partly attributed to the surge in the prices of materials: The input prices index went up from 67.1 in January to 69.4 in March, well above the neutral level of 50.

Exhibit 2 shows the contributions of the sub-indices to the change in the headline PMI. The rise in the headline PMI in 1Q20 was due largely to the increase in the new orders index (which weighs 30% in the computation of the headline PMI). Among the 12 sub-indices (i.e. excluding the suppliers' delivery time index), the indices of output, new orders, purchases of inputs, input prices, ex-factory prices and business expectations have remained in the expansionary zone over the past three months. Meanwhile, the indices of backlogs of orders, stocks of finished goods and stocks of major inputs have stayed in the contractionary zone over the same period. (See exhibit 3)

Policy outlook and forecasts for 2Q21

Looking ahead, we expect the Chinese government to maintain necessary policy support for the economy. According to the *Government Work Report* published in March this year, the Chinese government has set the GDP growth target for 2021 at 'above 6%'. The Chinese government has pledged to avoid 'sharp turns in policy' and it will ensure the continuity, consistency, and sustainability of macro policies to keep major economic indicators within an appropriate range. The proactive fiscal policy will be implemented in a manner that is of higher quality, more effective and more sustainable. Tax cuts will be implemented. Meanwhile, the prudent monetary policy will be pursued in a more flexible, tailored and appropriate way, with steps to ensure 'reasonably sufficient' liquidity and a stable macro leverage ratio. We believe that these policies will help promote the continued recovery of the Chinese economy.

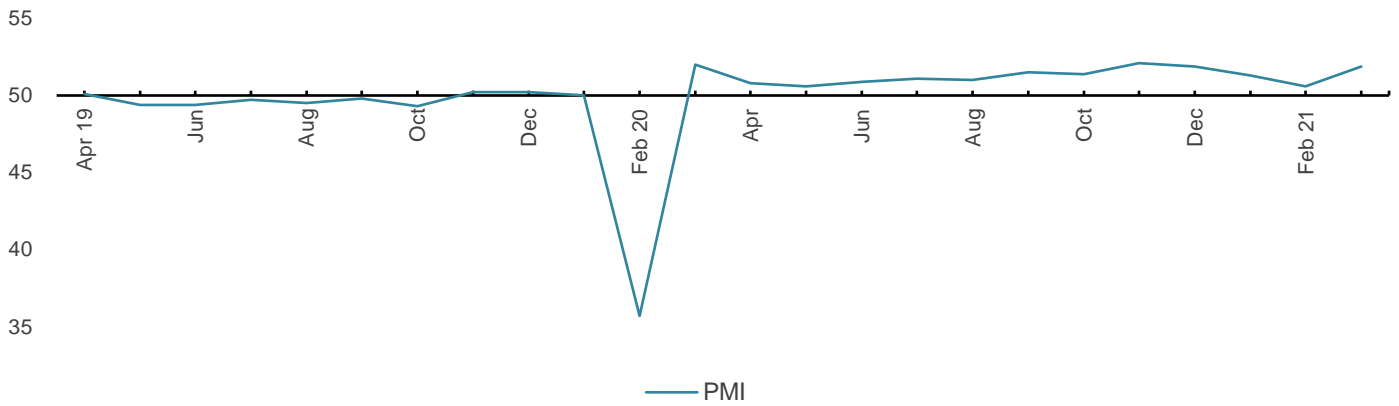
China's economic recovery is accelerating on the back of the easing COVID-19 pandemic and gradual reopening of advanced economies. Therefore, China's industrial production is set to expand further in the near term. Overall, we predict that the headline PMI will

We expect that a combination of improvement in external demand and a low comparison base last year will continue to boost VAI0 growth and GDP growth in 2Q21.

fluctuate within 51.0 to 52.0 in 2Q21. Meanwhile, the industrial production (VAIO) growth will top 8.5% yoy, due partly to a low comparison base in the same period last year.

Exhibit 4 plots the quarterly real GDP growth rates versus the monthly PMIs since April 2016. We project that China's real GDP growth will reach 8.0% yoy in 2Q21 due partly to a low comparison base in the same period last year.

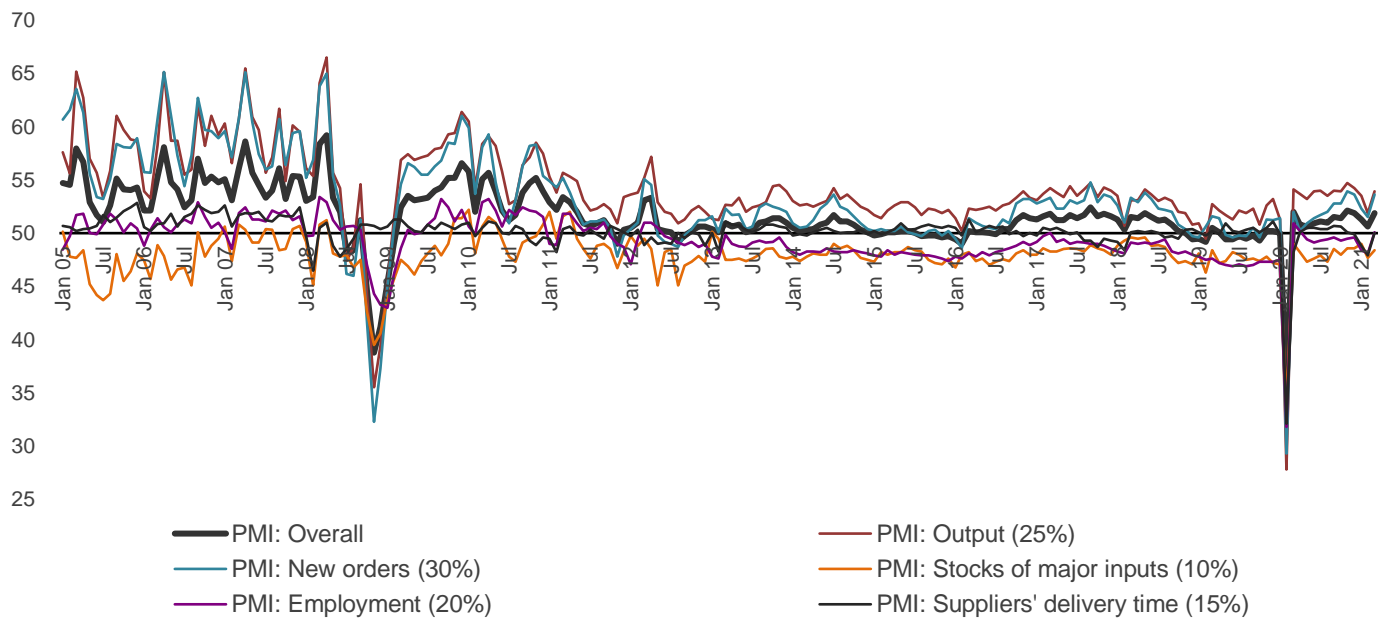
Exhibit 1: Headline PMI, April 2019 to March 2021



Source: China Federation of Logistics & Purchasing, China National Bureau of Statistics

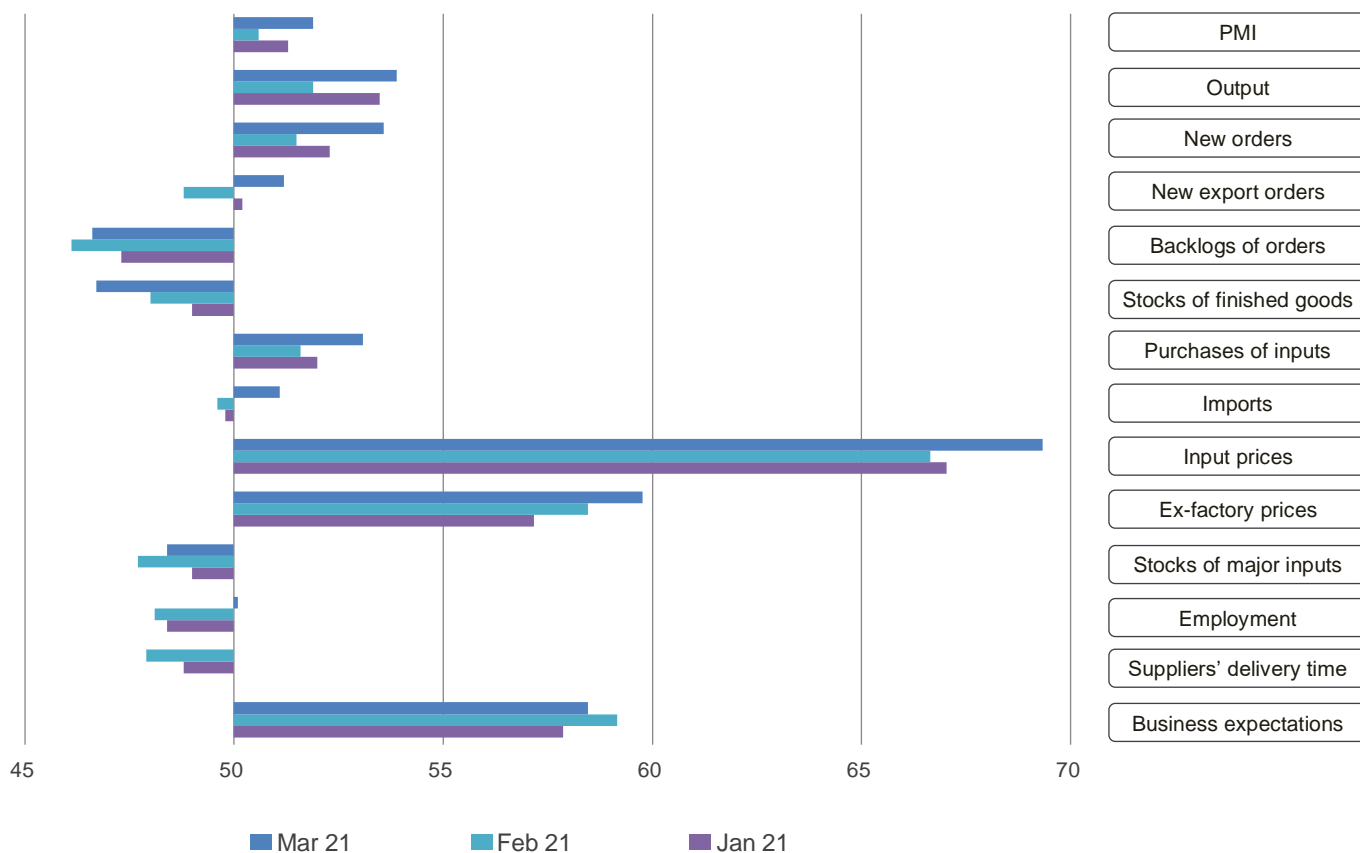
Exhibit 2: Headline PMI and sub-indices, January 2005 to March 2021

$PMI = Output \times 25\% + New\ Orders \times 30\% + Stocks\ of\ Major\ Inputs \times 10\% + Employment \times 20\% + (100 - Suppliers'\ Delivery\ Time) \times 15\%$



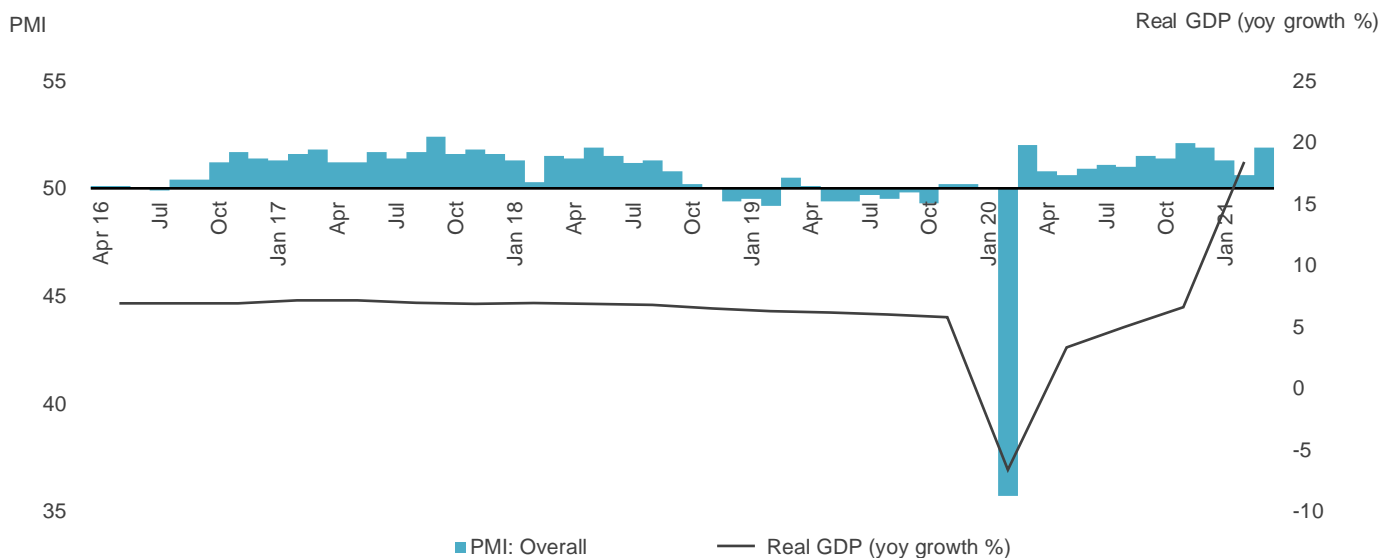
Source: China Federation of Logistics & Purchasing, China National Bureau of Statistics

Exhibit 3: Headline PMI and all sub-indices, January to March 2021



Source: China Federation of Logistics & Purchasing, China National Bureau of Statistics

Exhibit 4: Headline PMI and real GDP growth, April 2016 to March 2021



Source: China Federation of Logistics & Purchasing, China National Bureau of Statistics

2. What the PMI tells us about the performance of enterprises of different sizes

Expansion of large enterprises accelerates

The PMI of 'large enterprises' rose from 52.1 in January to 52.2 in February and 52.7 in March, showing an accelerated expansion of 'large enterprises'.

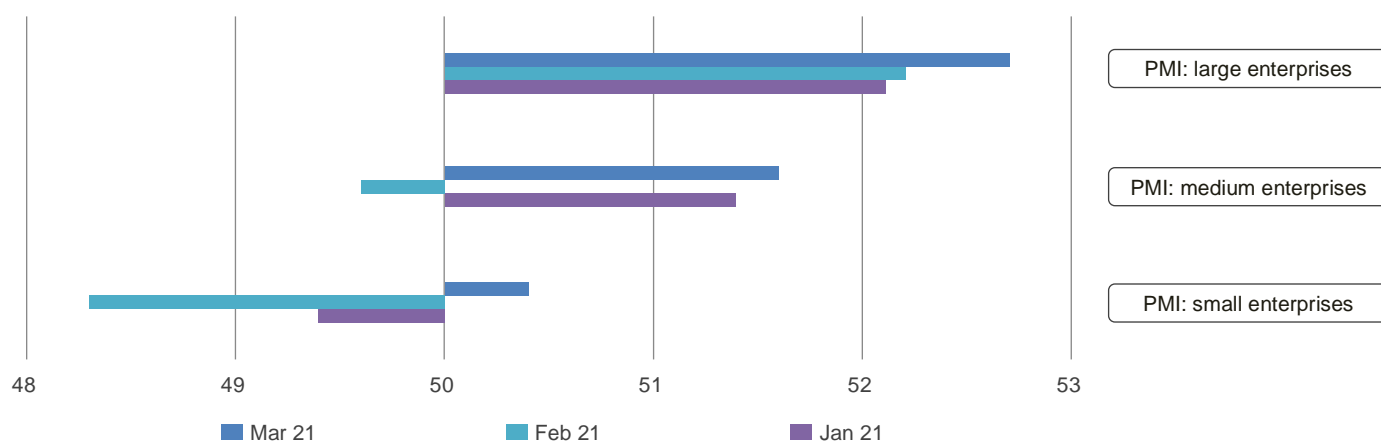
Medium and small enterprises return to expansion in March

The PMI of 'medium enterprises' dropped from 51.4 in January to 49.6 in February and then picked up to 51.6 in March, indicating that 'medium enterprises' have resumed its expansion lately. Meanwhile, after falling from 49.4 in January to 48.3 in February, the PMI of 'small enterprises' went up to 50.4 in March, returning to the expansionary zone for the first time since November last year.

Although it remains to be seen whether small businesses could sustain their growth momentum in the coming months, the marked improvement in March is a positive sign of recovery. (See exhibit 5)

Although it remains to be seen whether small businesses could sustain their growth momentum in the coming months, the marked improvement in March is a positive sign of recovery.

Exhibit 5: PMIs of large enterprises, medium enterprises and small enterprises, January to March 2021



Source: China Federation of Logistics & Purchasing, China National Bureau of Statistics

3. What the PMI tells us about manufacturing production

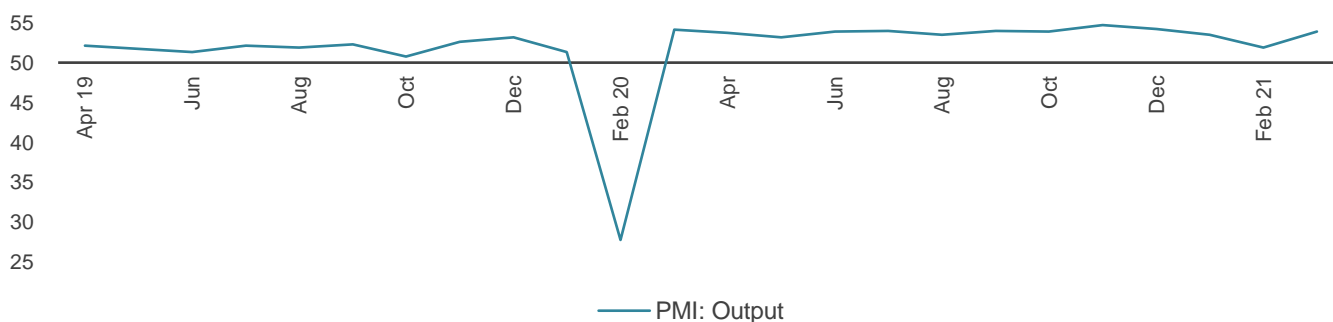
Manufacturing production expands at a relatively rapid pace

After dropping from 53.3 in January to 51.9 in February, the output index rose to 53.9 in March, indicating that production activities have expanded at a relatively fast pace lately as the overall demand has improved. (See exhibit 6)

New orders growth fuels the growth in manufacturing production

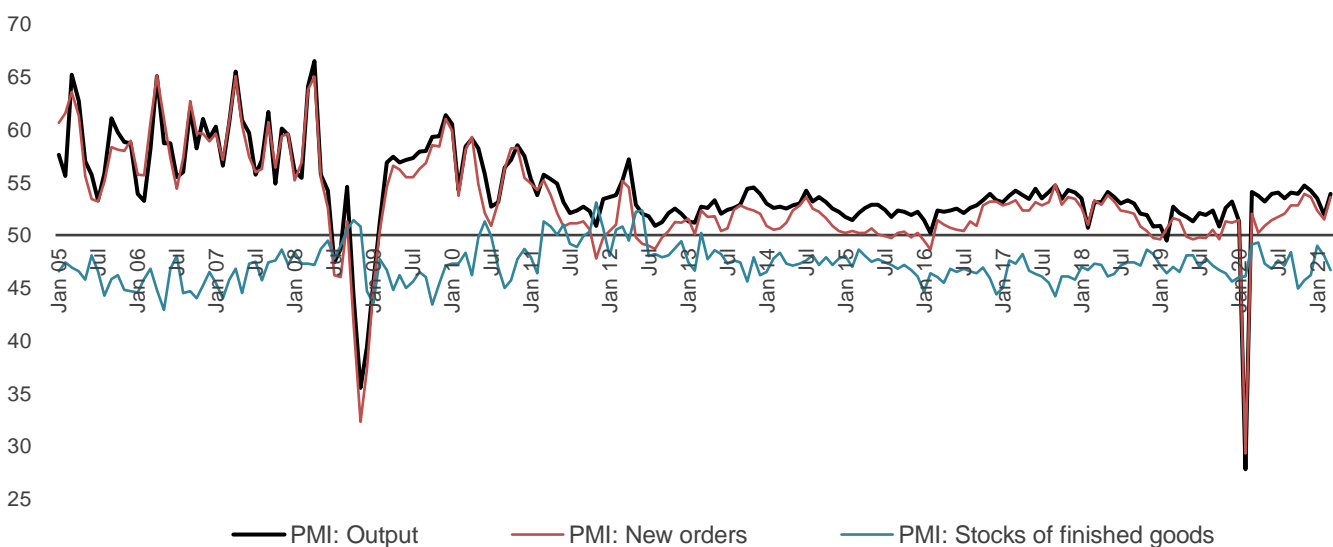
Exhibit 7 shows that the output growth in 1Q21 was mainly fuelled by new orders growth instead of restocking activities, as the stocks of finished goods index had stayed in the contractionary zone for 96 consecutive months as of March. However, output may grow strongly later when manufacturers finally run out of their inventory or regain confidence to restock.

Exhibit 6: Output index, April 2019 to March 2021



Source: China Federation of Logistics & Purchasing, China National Bureau of Statistics

Exhibit 7: Output, new orders and stocks of finished goods, January 2005 to March 2021



Source: China Federation of Logistics & Purchasing, China National Bureau of Statistics

Growth in manufacturing production to stay high in 2Q21

Exhibit 8 demonstrates the correlation (with some lags) between the output index and the year-on-year growth of value-added of industrial output (VAIO). Given an improving domestic and external demand and a low comparison base in the same period last year, China’s VAIO growth is expected to top 8.5% yoy in 2Q21. Still, challenges facing Chinese manufacturers include a fragile external demand caused by the COVID-19 pandemic, ongoing trade frictions between China and the US, intense competition in the international market, and strong government’s determination to reduce industrial carbon emissions.

We expect that the VAIO growth will top 8.5% yoy in 2Q21, amid an improving domestic and external demand and a low comparison base in the same period last year.

Exhibit 8: Output index and industrial production growth, April 2016 to March 2021



Source: China Federation of Logistics & Purchasing, China National Bureau of Statistics

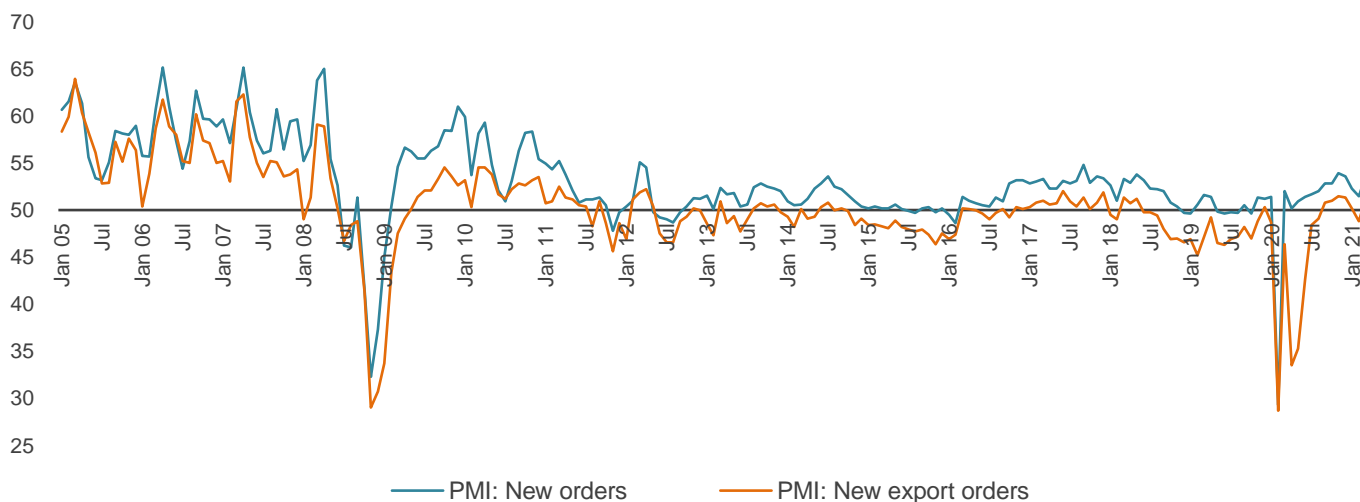
4. What the PMI tells us about the overall market demand

Overall market demand picks up fast

The new orders index fell from 52.3 in January to 51.5 in February and then rose to 53.6 in March. The relatively fast growth of new orders in March indicates a fast pick up in the overall market demand lately.

Meanwhile, the new export orders also picked up from 48.8 in February to 51.2 in March, indicating that new export orders have increased lately. (See exhibit 9)

Exhibit 9: New orders index and new export orders index, January 2005 to March 2021



Source: China Federation of Logistics & Purchasing, China National Bureau of Statistics

Sustained recovery in external demand bodes well for exports in 2Q21

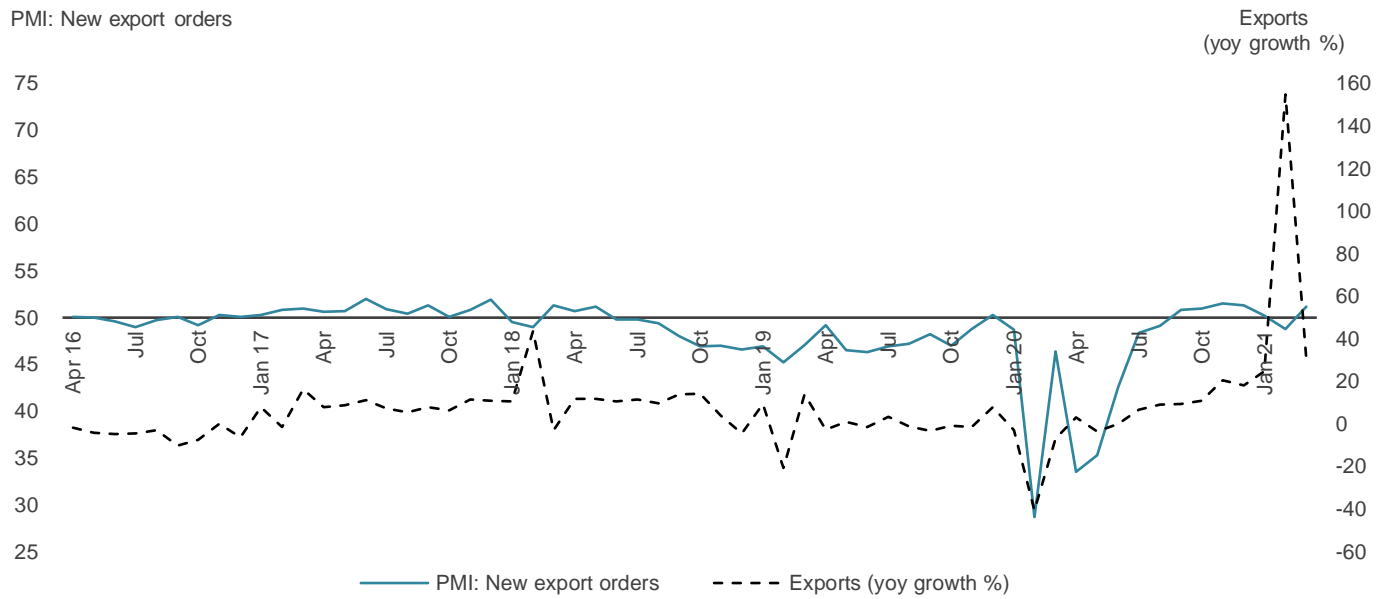
Exhibit 10 plots the new export orders index against the year-on-year growth rates of China’s exports. As the new export orders index has risen above the critical 50-mark lately, we are optimistic about the near-term prospects of China’s exports.

From exhibit 11 we can see that the new export orders index has been strongly correlated to the external economies, especially the developed economies. The OECD composite leading indicator¹ continued to pick up in 1Q21, suggesting a sustained recovery in external demand for China’s exports. Combined with a low comparison base in the same period last year, we forecast that China’s exports will jump by over 15.0% yoy in 2Q21.

With a continued improvement in external demand, we are optimistic about the near-term prospects of China’s exports. We forecast that China’s exports will jump by over 15.0% yoy in 2Q21.

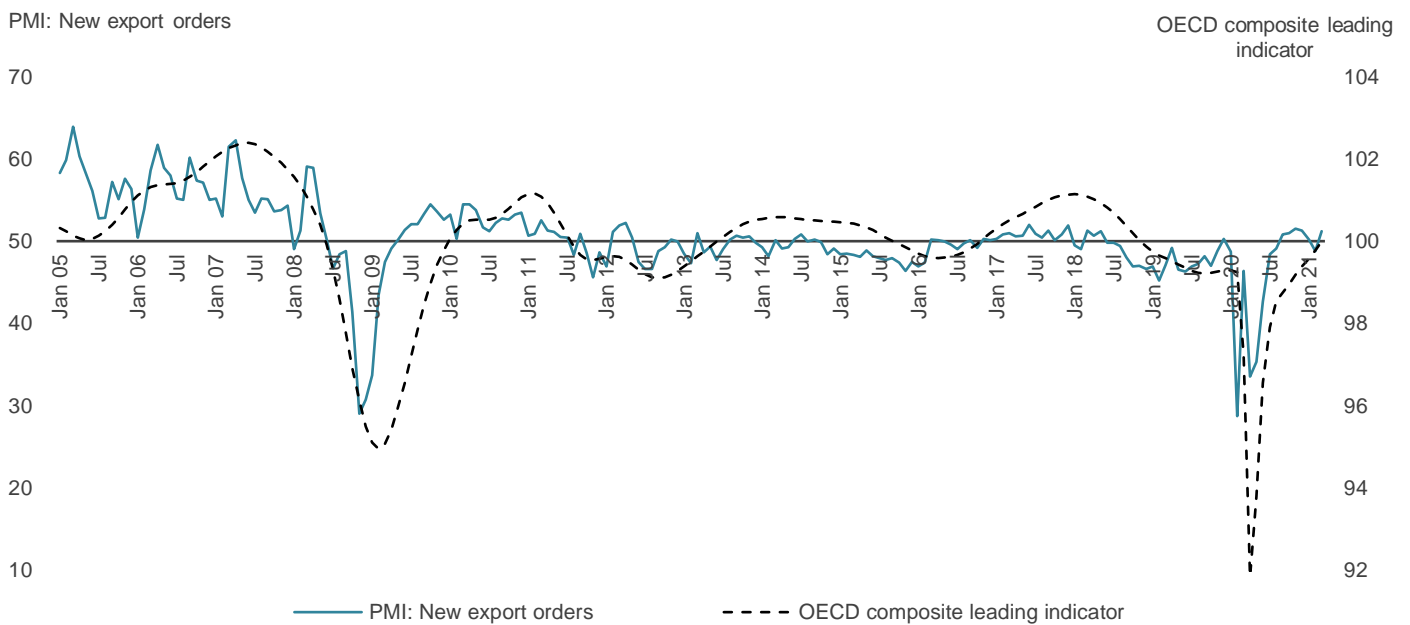
¹ The OECD composite leading indicator, compiled by the Organization for Economic Cooperation and Development, is designed to provide early signals of turning points (peaks and troughs) between expansions and slowdowns of economic activity, and covers Australia, Austria, Belgium, Canada, Czech Republic, Denmark, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Japan, Korea, Luxembourg, Mexico, Netherlands, New Zealand, Norway, Poland, Portugal, Slovak Republic, Spain, Sweden, Switzerland, Turkey, United Kingdom and United States.

Exhibit 10: New export orders index and export growth, April 2016 to March 2021



Source: China Federation of Logistics & Purchasing, China National Bureau of Statistics, China Customs

Exhibit 11: New export orders index and OECD composite leading indicator, January 2005 to March 2021



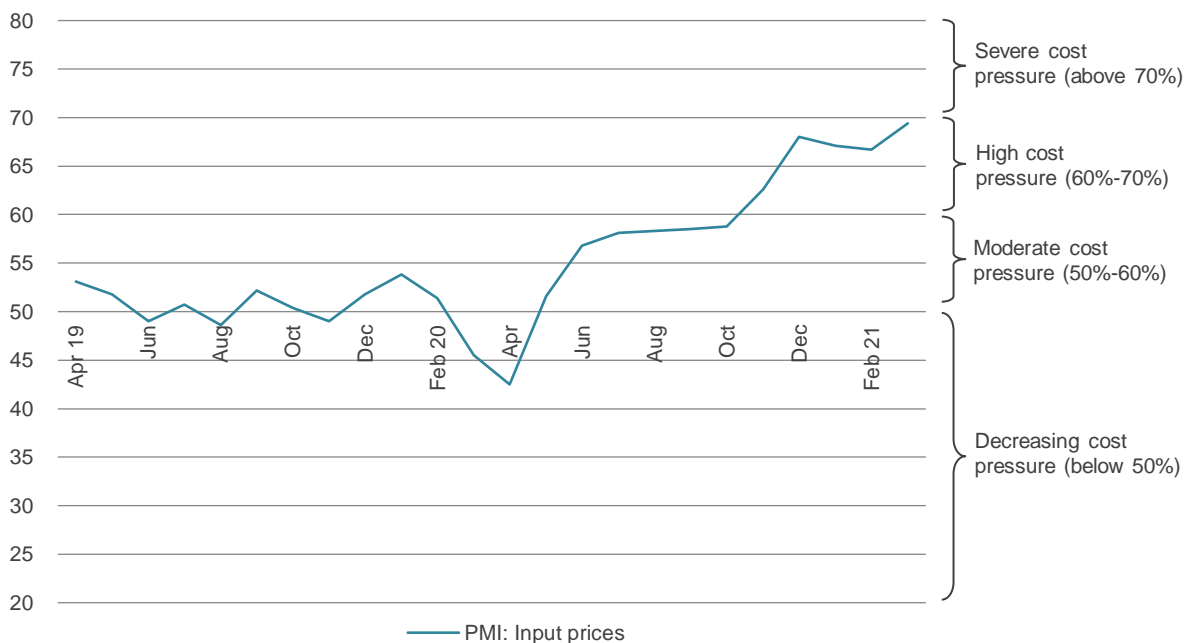
Source: China Federation of Logistics & Purchasing, China National Bureau of Statistics, Organization for Economic Cooperation and Development

5. What the PMI tells us about upstream and midstream prices

Surge in upstream prices exerts high cost pressures on manufacturers

The input prices index went up from 67.1 in January to 69.4 in March. The index readings continued its uptrend and were well above the critical 50-mark, indicating an accelerated increase in the prices of production inputs recently, which would raise the cost pressures on Chinese manufacturers. (Exhibit 12)

Exhibit 12: Input prices index, April 2019 to March 2021

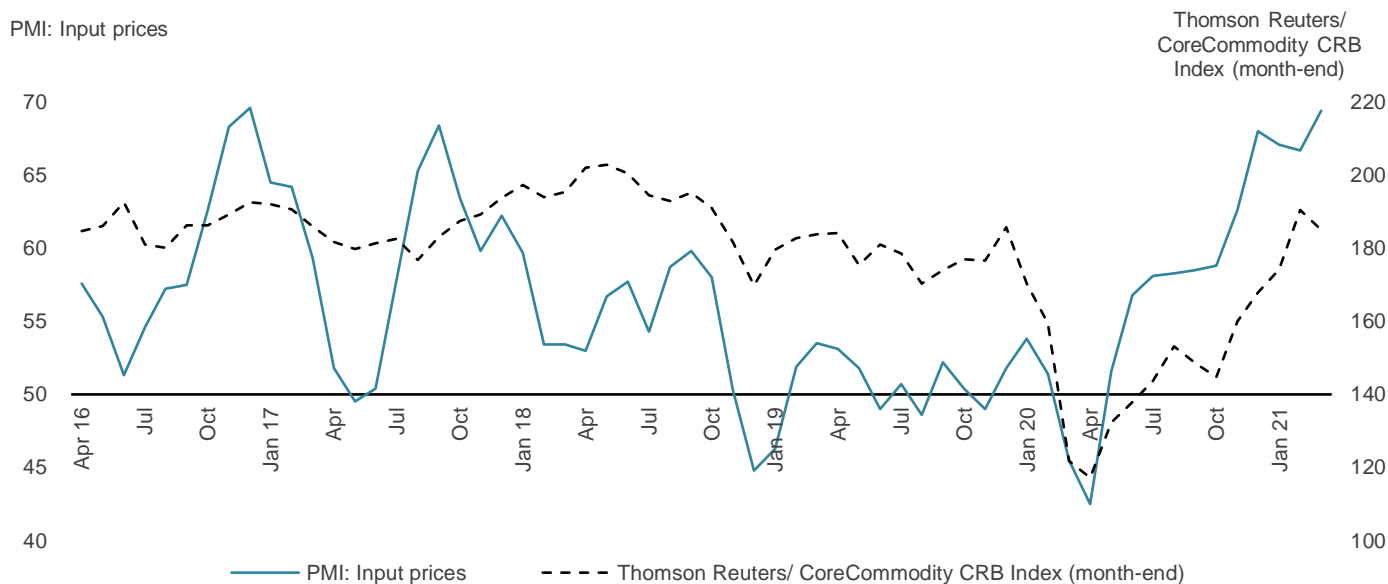


Source: China Federation of Logistics & Purchasing, China National Bureau of Statistics

To see the extent to which input costs of Chinese manufacturers are affected by global commodity prices, exhibit 13 puts together the input prices index and the Thomson Reuters/ CoreCommodity CRB index.²

² The Thomson Reuters/ CoreCommodity CRB Index, which comprises 19 commodities such as crude oil, aluminum, corn, cotton, gold, natural gas, soybeans, etc, has served as one of the most recognized measures of global commodity prices.

Exhibit 13: Input prices index and Thomson Reuters/ CoreCommodity CRB Index, April 2016 to March 2021



Source: China Federation of Logistics & Purchasing, China National Bureau of Statistics, Thomson Reuters

Manufacturers raise ex-factory prices of their products

The ex-factory prices index rose from 57.2 in January to 58.5 in February and further to 59.8 in March, indicating that Chinese manufacturers have continued to raise the ex-factory prices of their finished products lately amid rising cost pressures and improving sales environment.³ (Exhibit 14)

Exhibit 14: Ex-factory prices index, April 2019 to March 2021



Source: China Federation of Logistics & Purchasing, China National Bureau of Statistics

³ The ex-factory prices index has been released since January 2017.

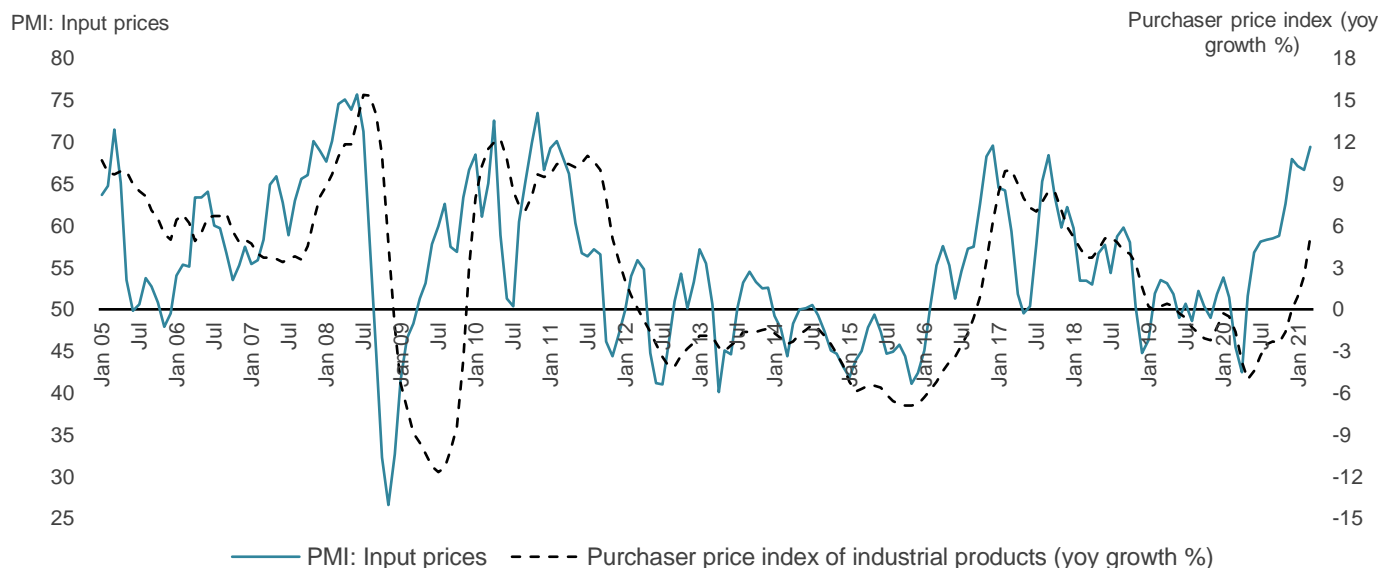
Purchaser price index and PPI to pick up further

Exhibit 15 shows that the input prices index is useful as a leading indicator of upstream prices. To show the association between the input prices index and ‘midstream’ prices, we plot the input prices index against the year-on-year growth of the producer price index (PPI)⁴ in exhibit 16.

Going forward, we expect that the year-on-year growth rates for both the purchaser price index and the PPI will rise further and reach their near-term peaks in 2Q21.

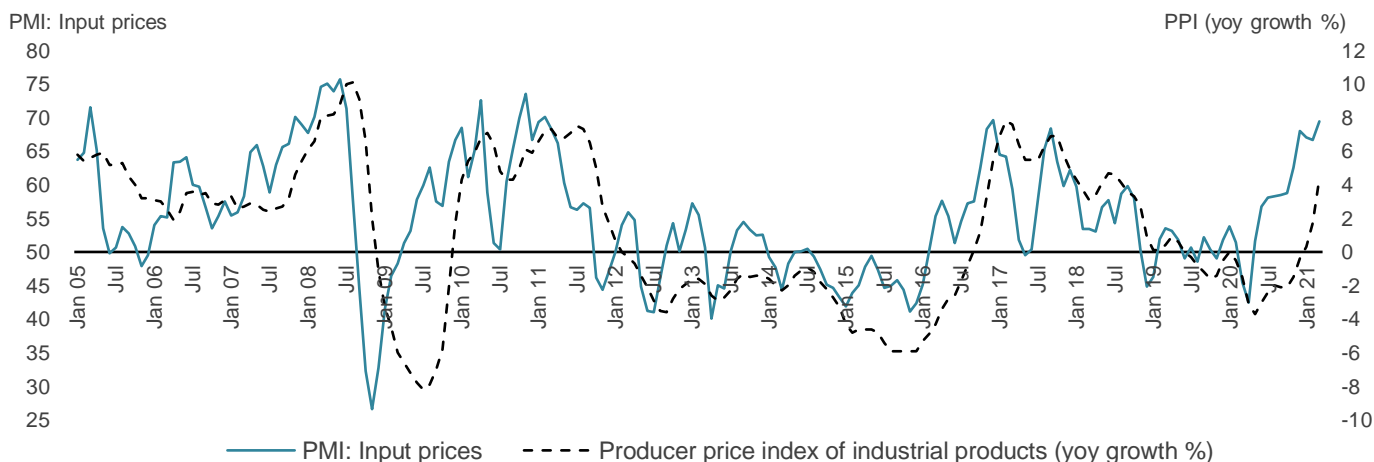
We expect that the year-on-year growth rates for both the purchaser price index and the PPI will rise further and reach their near-term peaks in 2Q21.

Exhibit 15: Input prices index and purchaser price index of industrial products, January 2005 to March 2021



Source: China Federation of Logistics & Purchasing, China National Bureau of Statistics

Exhibit 16: Input prices index and producer price index, January 2005 to March 2021



Source: China Federation of Logistics & Purchasing, China National Bureau of Statistics

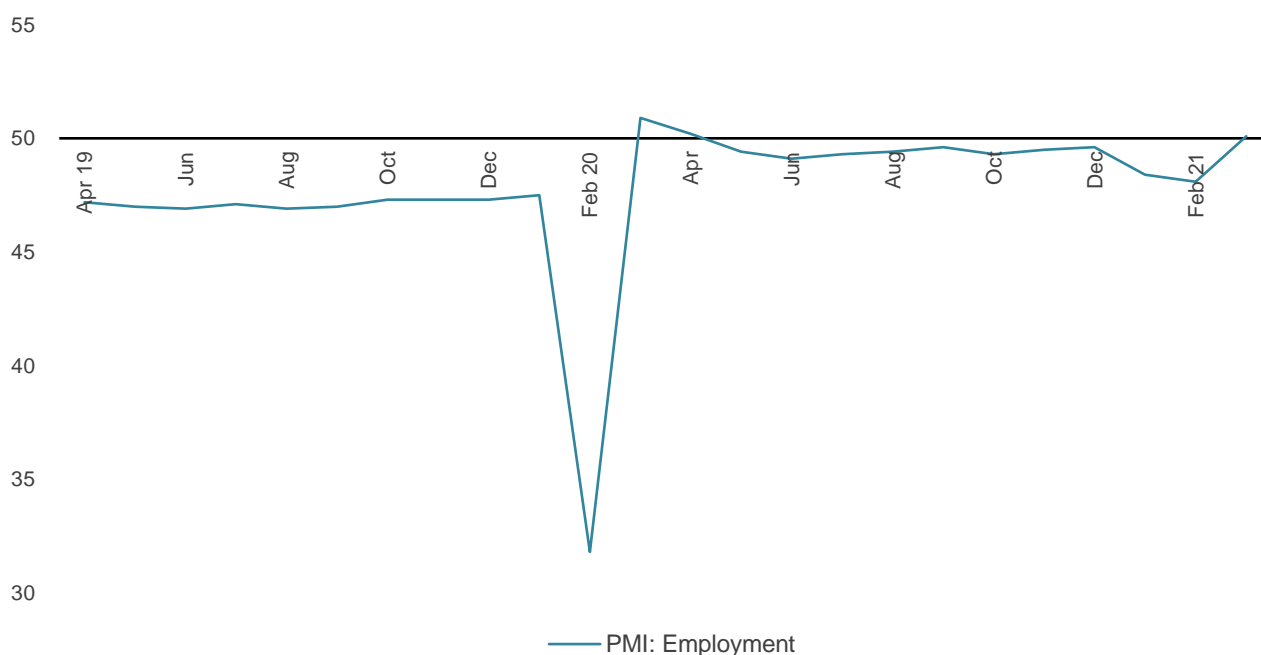
⁴ The producer price index of industrial goods (PPI), compiled by China National Bureau of Statistics, measures the prices of industrial products when they are sold for the first time after production.

6. What the PMI tells us about manufacturing employment

Recent pick up in employment index indicates improvement in manufacturing employment

The employment index increased from 48.1 in February to 50.1 in March, returning to the expansionary zone. The latest index reading indicates that the employment situation in the manufacturing sector has improved lately. (Exhibit 17)

Exhibit 17: Employment index, April 2019 to March 2021



Source: China Federation of Logistics & Purchasing, China National Bureau of Statistics

Exhibit 18 proves that the employment in China’s manufacturing sector has relied heavily on the export sector. Exhibit 19 and 20 give our readers some ideas about the extent to which the employment situation improves or deteriorates with the manufacturing sector and the overall economy. Given a strong recovery in the export sector and the overall economy, we expect that the employment situation in the manufacturing sector will remain robust in 2Q21.

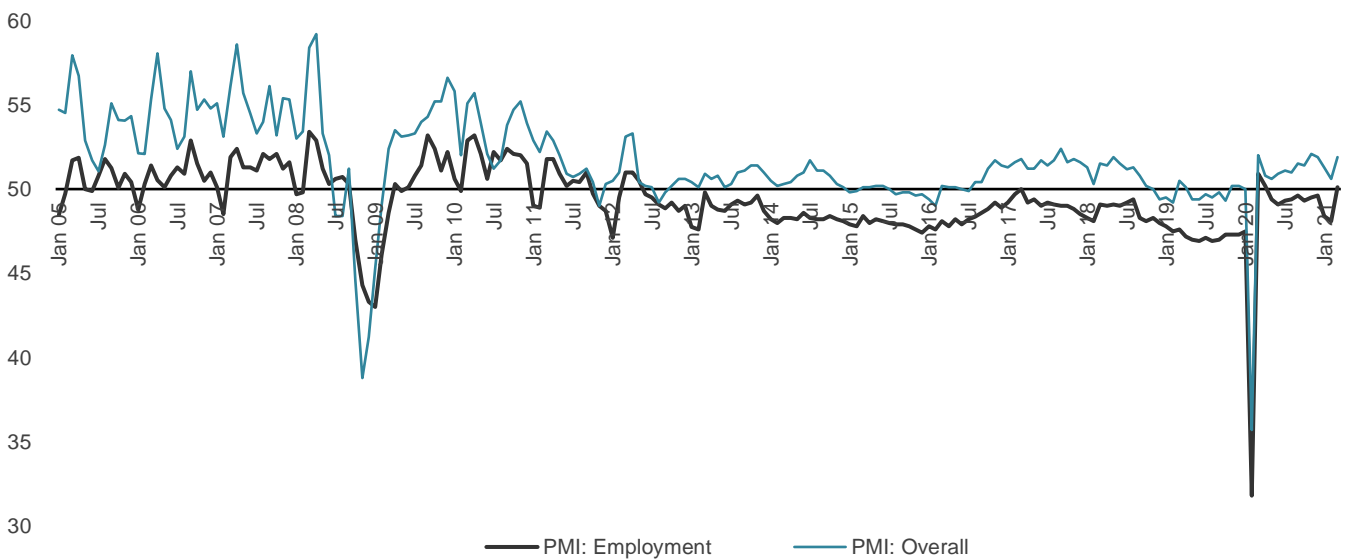
Given a strong recovery in the export sector and the overall economy, we expect the employment situation in the manufacturing sector to remain robust in 2Q21.

Exhibit 18: Employment and new export orders, January 2005 to March 2021



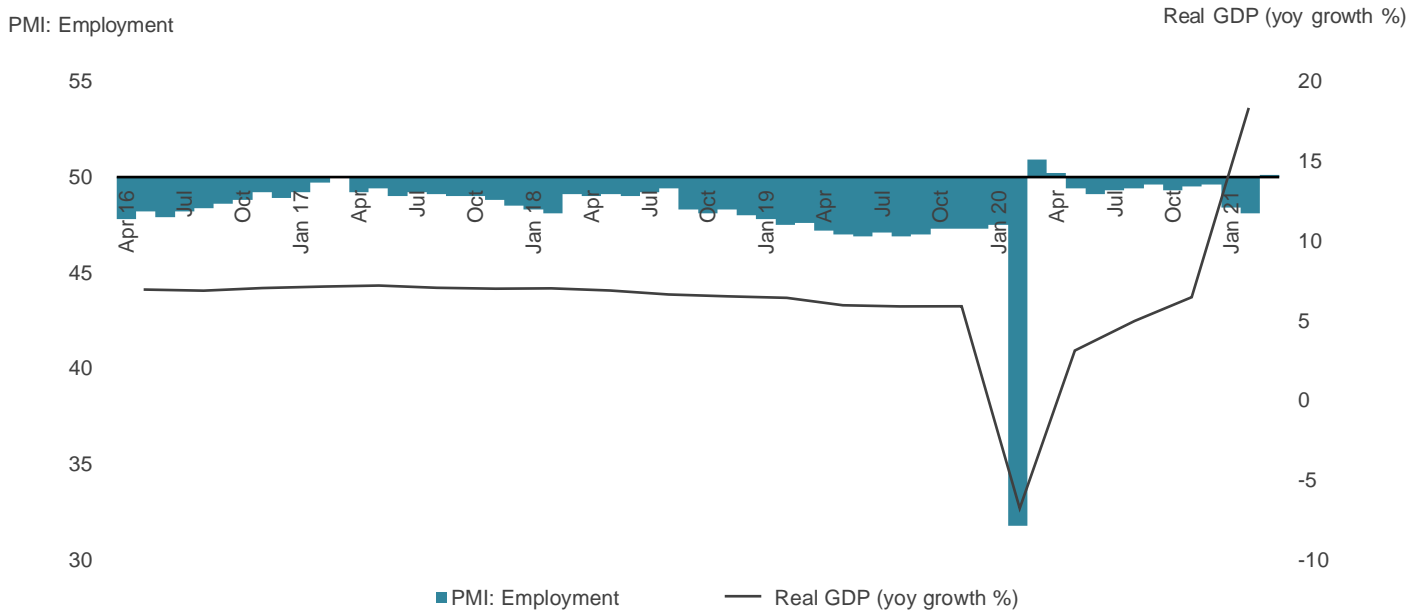
Source: China Federation of Logistics & Purchasing, China National Bureau of Statistics

Exhibit 19: Employment index and headline PMI, January 2005 to March 2021



Source: China Federation of Logistics & Purchasing, China National Bureau of Statistics

Exhibit 20: Employment index and real GDP growth, April 2016 to March 2021



Source: China Federation of Logistics & Purchasing, China National Bureau of Statistics

About China Manufacturing PMI:

China Manufacturing Purchasing Managers' Index (PMI) provides an early indication each month of economic activities in the Chinese manufacturing sector. It is jointly published by China Federation of Logistics & Purchasing (CFLP) and the National Bureau of Statistics (NBS). Fung Business Intelligence is responsible for drafting and disseminating the English PMI report.

Every month questionnaires are sent to 3,000 manufacturing enterprises all over China. The data presented herein is compiled from the enterprises' responses about their purchasing activities and supply situations. CFLP makes no representation regarding the data collection procedures, nor does it disclose any data of individual enterprises. The PMI should be compared to other economic data sources when used in decision-making.

3,000 manufacturing enterprises in 31 industries from Eastern, Northeastern, Central and Western China are surveyed. The sampling of the enterprises involves the use of Probability Proportional to Size Sampling (PPS), which means the selection of enterprises surveyed is largely based on each industry's contribution to GDP, and the representation of each geographical region.

There are 13 sub-indicators in the survey: Output, New Orders, New Export Orders, Backlogs of Orders, Stocks of Finished Goods, Purchases of Inputs, Imports, Input Prices, Stocks of Major Inputs, Ex-factory Prices, Employment, Suppliers' Delivery Time and Business Expectations. An index reading above 50 indicates an overall positive change in a sub-indicator; below 50, an overall negative change.

The PMI is a composite index based on the seasonally adjusted indices for five of the sub-indicators with varying weights: New Orders—30%; Output—25%; Employment—20%; Suppliers' Delivery Time—15%; and Stocks of Major Inputs—10%. A PMI reading above 50 indicates an overall expansion in the manufacturing sector; below 50, an overall contraction.

Currently there are more than twenty countries and regions conducting the PMI survey and compilation, based on an internationally standardized methodology.

About the Organisations:

China Federation of Logistics & Purchasing

China Federation of Logistics & Purchasing (CFLP) is the logistics and purchasing industry association approved by the State Council. CFLP's mission is to push forward the development of the logistics industry and the procurement businesses of both government and enterprises, as well as the circulation of factors of production in China. The government authorizes the CFLP to produce industry statistics and set industry standards. CFLP is also China's representative in the Asian-Pacific Logistics Federation (APLF) and the International Federation of Purchasing and Supply Management (IFPSM).

Fung Business Intelligence

Fung Business Intelligence collects, analyses and interprets global market data on sourcing, supply chains, distribution, retail and technology.

Headquartered in Hong Kong, it leverages unique relationships and information networks to monitor, research and report on these global issues with a particular focus on business trends and developments in China. Fung Business Intelligence makes its data, impartial analysis and specialist knowledge available to businesses, scholars and governments through regular research reports and business publications.

As the knowledge bank and think tank for the Fung Group, a Hong Kong-based multinational corporation, Fung Business Intelligence also provides expertise, advice and consulting services to the Group and its business partners on issues related to doing business in China, ranging from market entry and company structure, to tax, licensing and other regulatory matters.

Fung Business Intelligence was established in the year 2000.

Fung Group

Fung Holdings (1937) Limited, a privately-held business entity headquartered in Hong Kong, is the major shareholder of the Fung Group of companies, whose core businesses operate across the entire global supply chain for consumer goods including trading, logistics, distribution and retail. The Fung Group comprises over 30,000 people working in more than 40 economies worldwide. We have a rich history and heritage in export trading and global supply chain management that dates back to 1906 and traces the story of how Hong Kong and the Pearl River Delta emerged as one of the world's foremost manufacturing and trading regions. We are focused on both creating the Supply Chain of the Future to help brands and retailers navigate the digital economy as well as creating new opportunities, product categories and market expansion for brands on a global scale.

Listed entities of the Group include Global Brands Group Holding Limited (SEHK: 00787) and Convenience Retail Asia Limited (SEHK: 00831). Privately-held entities include Li & Fung Limited, LH Pegasus, Branded Lifestyle Holdings Limited, Fung Kids (Holdings) Limited, Toys "R" Us (Asia) and Suhyang Networks.

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