

PMI Quarterly on China Manufacturing

PMI 2Q21

Steady growth in manufacturing production and economic activity

Policy Outlook

China to maintain necessary policy support for economy

3Q21 Forecasts

Real GDP growth to top 6.0% yoy while PMI to fluctuate around 51.0

Fung Business Intelligence

Helen Chin

Vice President
helenchin@fung1937.com

William Kong

Senior Research Manager
williamkong@fung1937.com

China Federation of Logistics & Purchasing

Chen ZhongTao

czt@clic.org.cn

PMI points to steady growth in manufacturing production and economic activity in 2Q21

Our observations

- The recovery of small enterprises continues to lag behind that of large and medium enterprises.
- Manufacturing production continues its stable expansion.
- Overall market demand improves despite a fall in new export orders.
- Manufacturers raise ex-factory prices of their products amid high cost pressures as prices of production inputs continue to rise.
- Manufacturing employment remains steady.

Policy outlook

- The Chinese government will maintain necessary policy support for the economy.
- The proactive fiscal policy will be implemented thoroughly to help optimize China’s economic structure. Meanwhile, the prudent monetary policy will be adopted to maintain reasonably sufficient liquidity, so as to provide stronger support for the real economy and key areas and weak links in the economy.

Our forecasts for 3Q21

- We project a further expansion of manufacturing production and economic activity in 3Q21.
- The headline PMI will stay above 50 and fluctuate around 51.0.
- Real GDP growth will top 6.0% yoy.
- VAIO growth will surpass 7.0% yoy.
- Exports will grow by 10% yoy.
- Year-on-year growth rates for both the purchaser price index and the PPI will moderate.

Helen Chin

Vice President

E: helenchin@fung1937.com

William Kong

Senior Research Manager

E: williamkong@fung1937.com

Fung Business Intelligence

1/F LiFung Tower

888 Cheung Sha Wan Road

Kowloon, Hong Kong

T: (852) 2300 2470

F: (852) 2635 1598

E: fbicgroup@fung1937.com

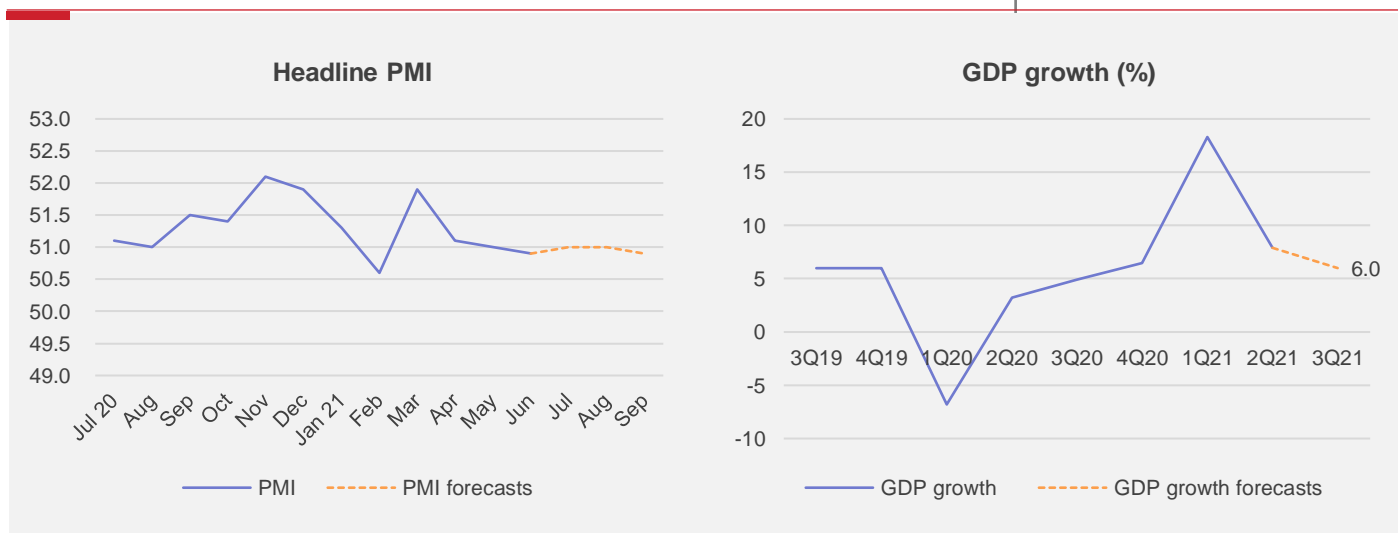
W: <http://www.fbicgroup.com>



Chen ZhongTao

czt@clic.org.cn

China Federation of Logistics & Purchasing



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1. PMI points to steady growth in manufacturing production and economic activity in 2Q21

China's manufacturing sector and economy in 2Q21

China's manufacturing PMI edged down from 51.1 in April to 51.0 in May and 50.9 in June. The headline PMI readings have hovered around 51.0 in recent months, indicating a steady growth in the manufacturing sector in 2Q21 (See exhibit 1)

Manufacturing output has continued its stable expansion in recent months, as shown by the strong output index throughout April to June. The expansion was supported by a steady growth in overall new orders: The new orders index stayed within the range of 51.3 to 52.0 throughout April to June, indicating a steady pick up in the overall market demand lately.

Prices of industrial products have continued to increase but at a slower pace lately: The ex-factory prices index fell from 60.6 in May to 51.4 in June. The recent slowdown in product price hikes was partly attributed to a smaller rise in the prices of materials lately: The input prices index went down from 72.8 in May to 61.2 in June.

Exhibit 2 shows the contributions of the sub-indices to the change in the headline PMI. The rise in the headline PMI in 2Q20 was due largely to the increase in the output index (which weighs 25% in the computation of the headline PMI) and the new orders index (which weighs 30%). 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, stocks of major inputs and employment have stayed in the contractionary zone over the same period. (See exhibit 3)

Policy outlook and forecasts for 3Q21

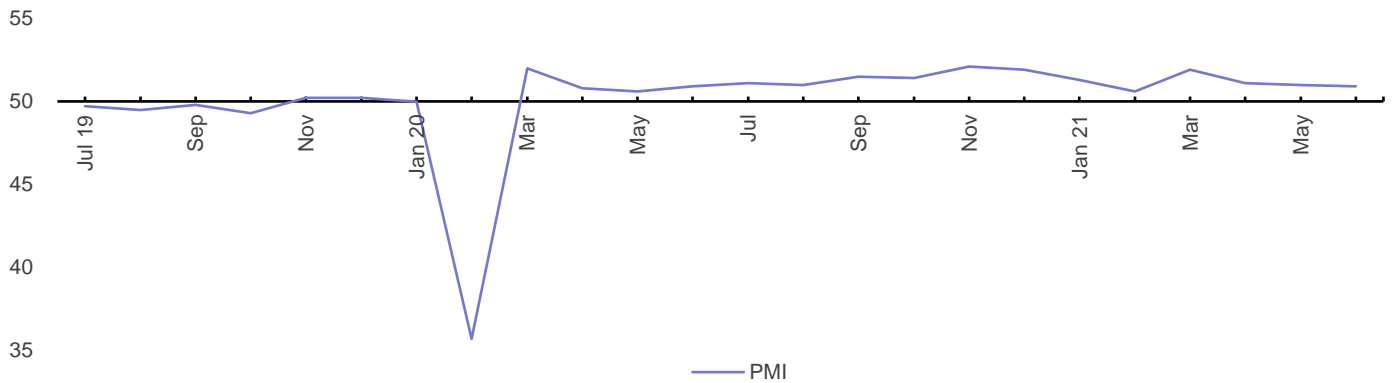
Looking ahead, we expect the Chinese government to maintain necessary policy support for the economy. A meeting of the Political Bureau of the Communist Party of China (CPC) Central Committee was held on 30 April. According to the meeting, China should implement macro policies with precision while maintaining their continuity, stability and sustainability and avoiding 'sharp turns in policy'. The proactive fiscal policy will be implemented thoroughly to help optimize China's economic structure. Meanwhile, the prudent monetary policy will be adopted to maintain reasonably sufficient liquidity, so as to provide stronger support for the real economy and key areas and weak links in the economy. For example, the People's Bank of China (PBoC) lowered the required reserve ratios (RRR) for all banks on 15 July. We believe that these policies will help promote the continued growth of the Chinese economy.

We expect that a combination of improvement in external demand and a low comparison base last year will continue to boost GDP growth in 3Q21.

China's economy, in particular the manufacturing sector, is continuing its recovery on the back of the easing COVID-19 global pandemic and reopening of advanced economies. China's industrial production is set to expand further in the near term. Overall, we predict that the headline PMI will fluctuate around 51.0 and the industrial production (VAIO) growth will top 7.0% yoy in 3Q21.

Exhibit 4 plots the quarterly real GDP growth rates versus the monthly PMIs since July 2016. We project that China's real GDP growth will top 6.0% yoy in 3Q21 due partly to a low comparison base in the same period last year.

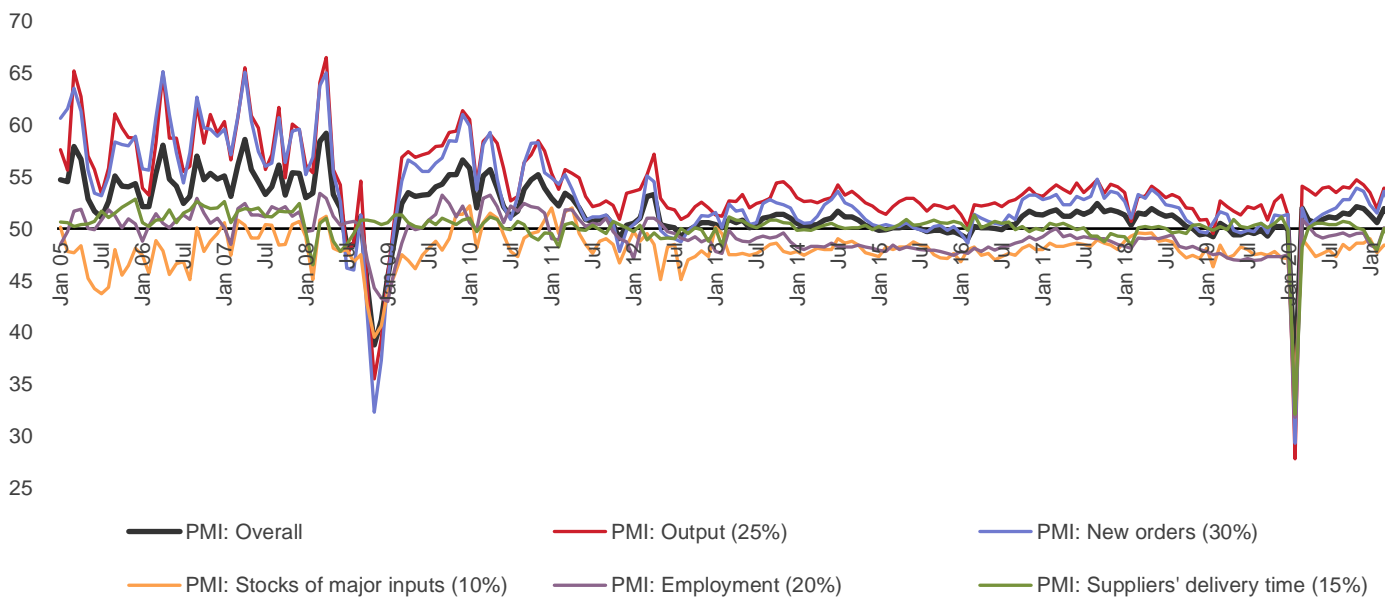
Exhibit 1: Headline PMI, July 2019 to June 2021



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

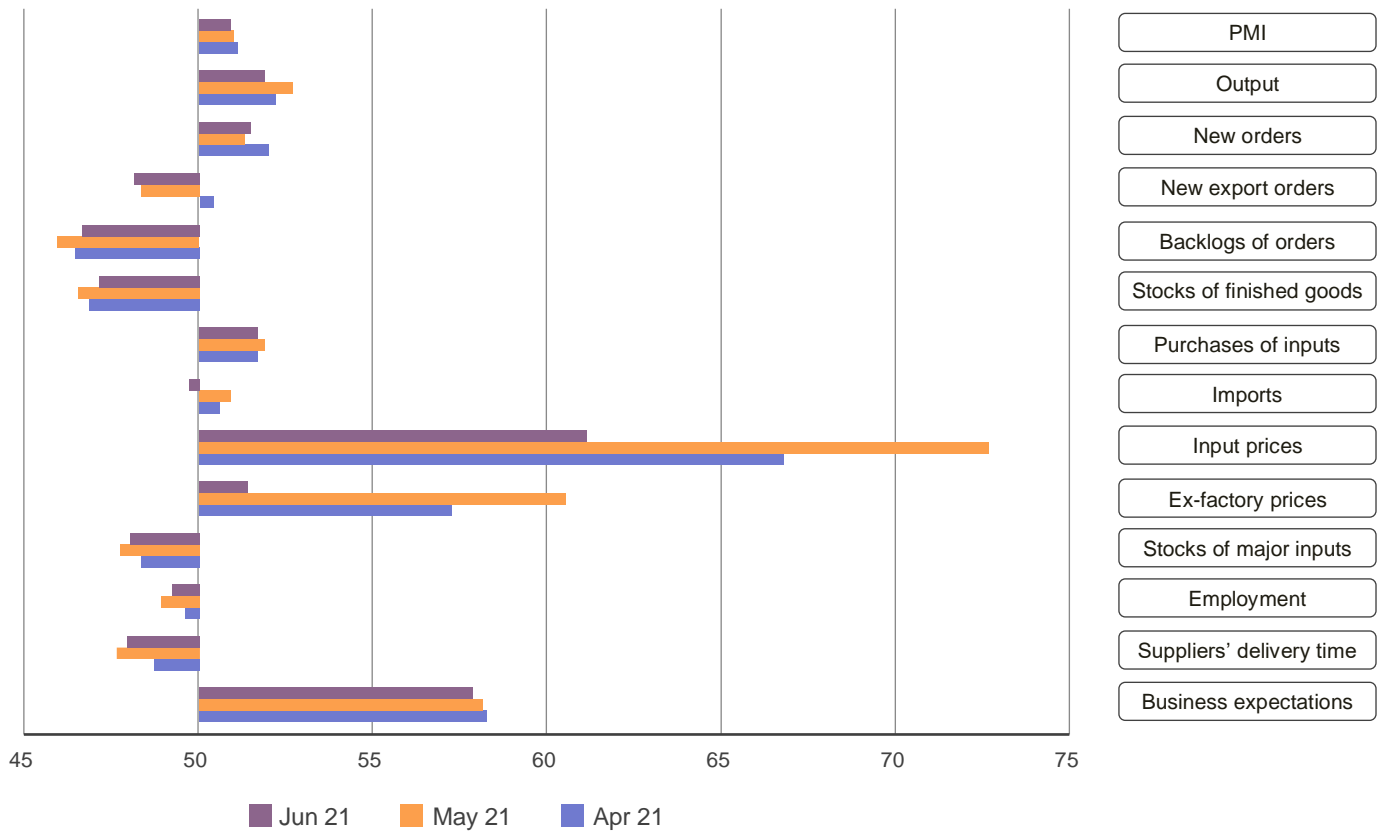
Exhibit 2: Headline PMI and sub-indices, January 2005 to June 2021

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



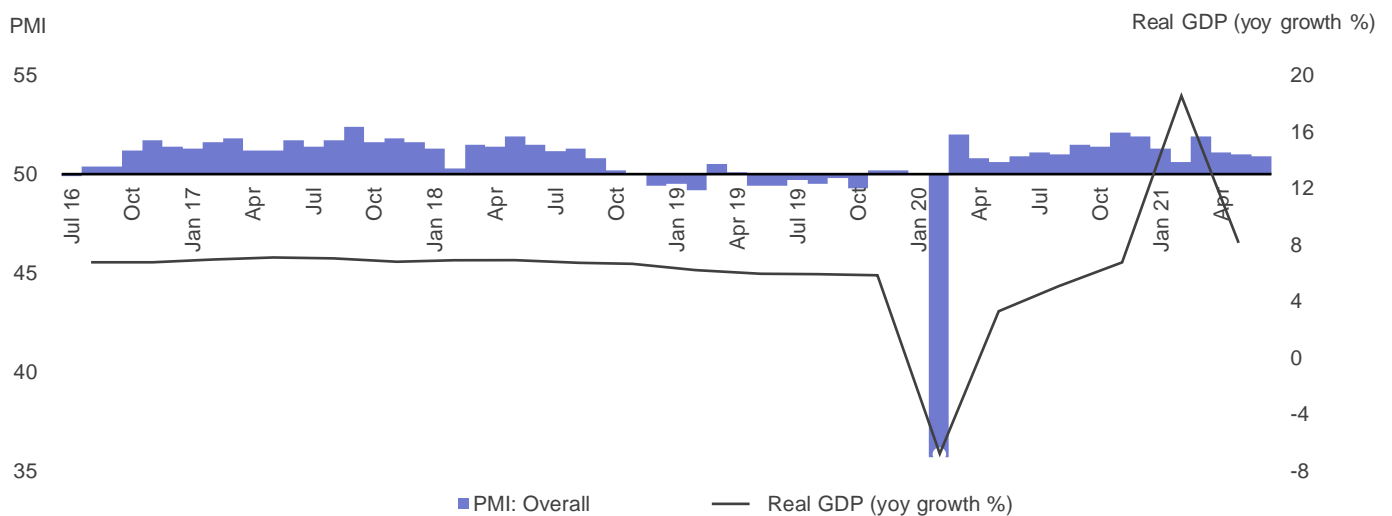
Source: China Federation of Logistics & Purchasing, China National Bureau of Statistics

Exhibit 3: Headline PMI and all sub-indices, April to June 2021



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

Exhibit 4: Headline PMI and real GDP growth, July 2016 to June 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

Large and medium enterprises continue to expand

The PMI of 'large enterprises' stayed high within a narrow range of 51.7 to 51.8 throughout April to June, showing a continued expansion of 'large enterprises'. After rising from 50.3 in April to 51.1 in May, the PMI of 'medium enterprises' retreated to 50.8 in June, indicating that the expansion of 'medium enterprises' has slowed lately.

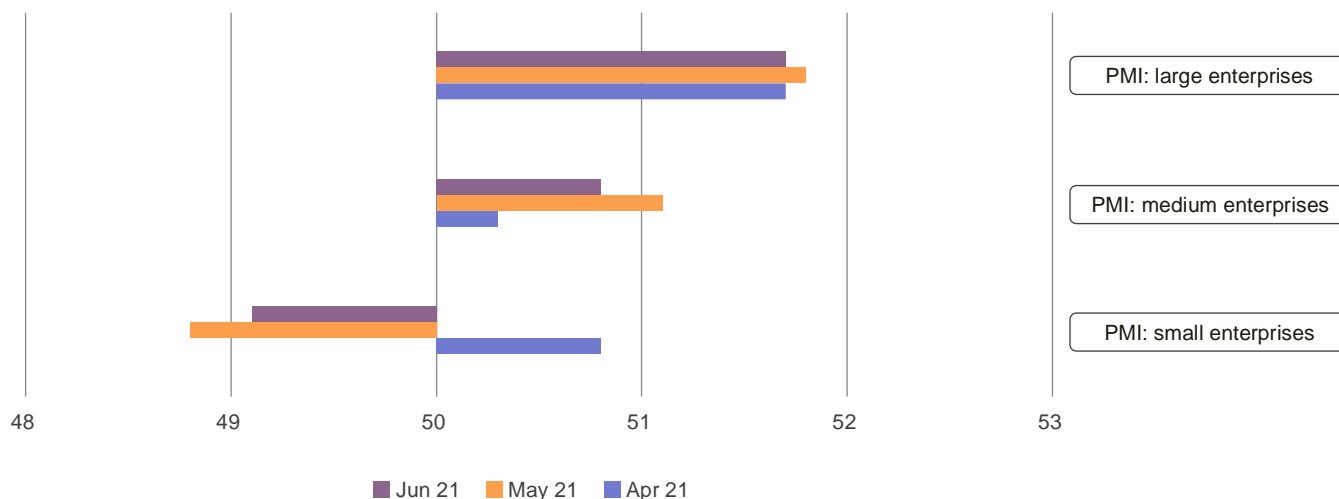
Small enterprises return to contraction

The PMI of 'small enterprises' dropped from 50.8 in April to 48.8 in May and then picked up to 49.1 in June. The index readings have stayed below the critical 50-mark since May, indicating that small enterprises have been facing difficulties in production and operations lately.

The recovery of small enterprises has lagged behind that of large and medium enterprises since June last year. (See exhibit 5)

The recovery of small enterprises has lagged behind that of large and medium enterprises since June last year.

Exhibit 5: PMIs of large enterprises, medium enterprises and small enterprises, April to June 2021



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

3. What the PMI tells us about manufacturing production

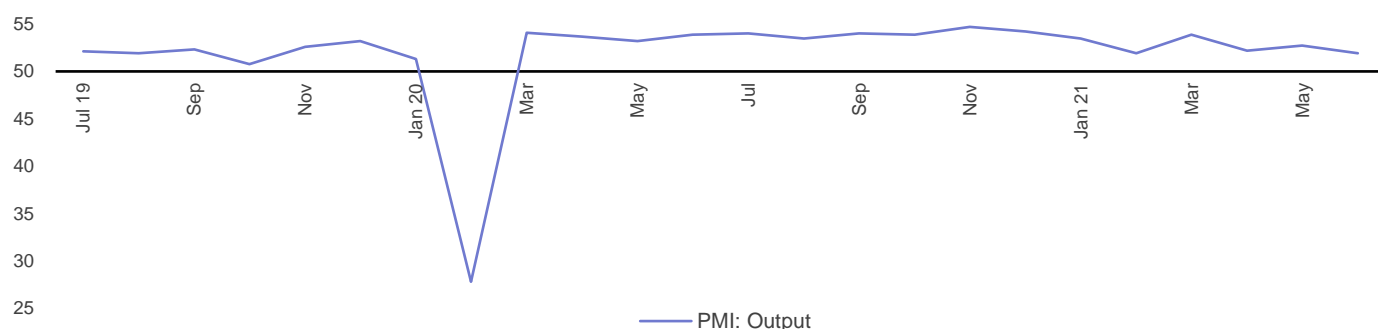
Manufacturing production continues its stable expansion

The output index rose from 52.2 in April to 52.7 in May, before dropping to 51.9 in June. The index readings have stayed high around 52.0, indicating a stable expansion in manufacturing output. (See exhibit 6)

New orders growth fuels the growth in manufacturing production

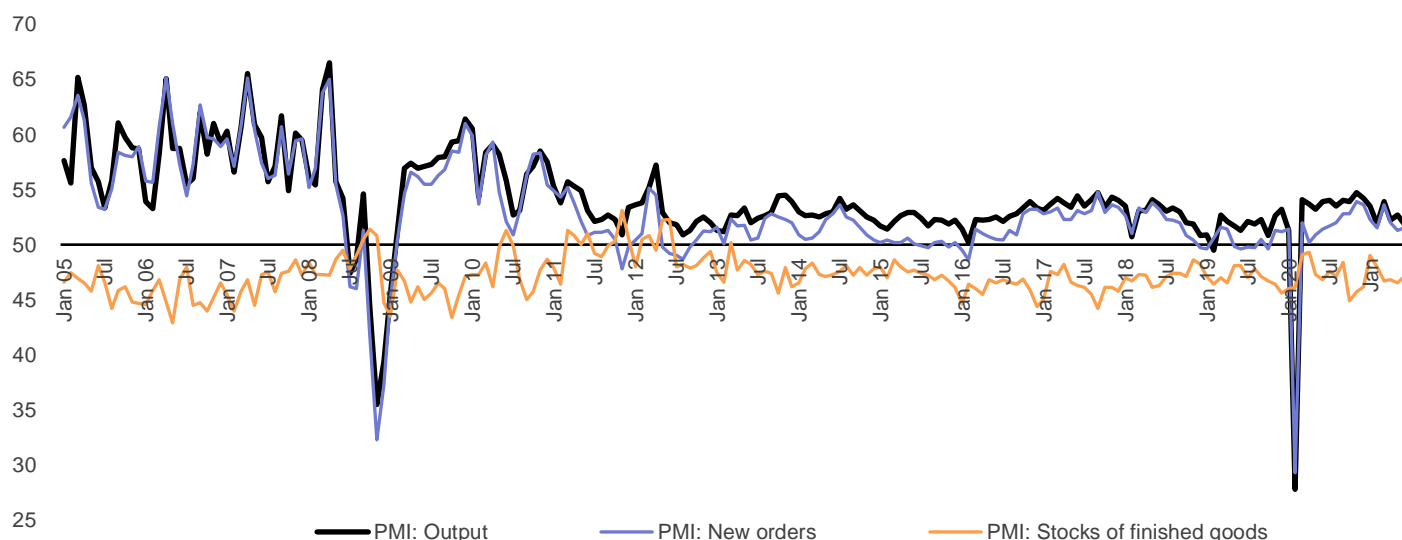
Exhibit 7 shows that the output growth in 2Q21 was mainly fuelled by new orders growth instead of restocking activities, as the stocks of finished goods index had stayed in the contractionary zone for 99 consecutive months as of June. However, output may grow strongly later when manufacturers finally run out of their inventory or regain confidence to restock.

Exhibit 6: Output index, July 2019 to June 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 June 2021



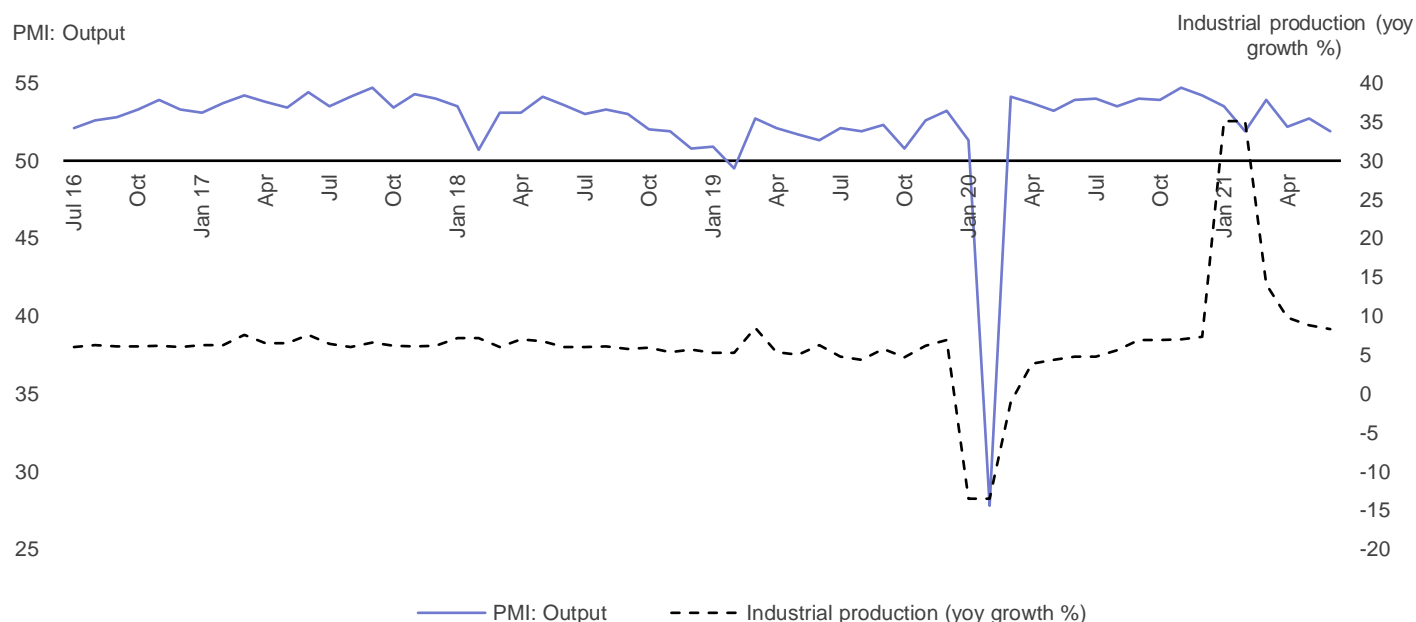
Source: China Federation of Logistics & Purchasing, China National Bureau of Statistics

Growth in manufacturing production to stay high in 3Q21

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 overall demand, China’s VAIO growth is expected to exceed 7.0% yoy in 3Q21. Still, challenges facing Chinese manufacturers include ongoing trade frictions between China and the US, intense competition in the international market, electricity shortage in some regions, and strong government’s determination to reduce industrial carbon emissions.

We expect that the VAIO growth will exceed 7.0% yoy in 3Q21, amid an improving overall demand.

Exhibit 8: Output index and industrial production growth, July 2016 to June 2021



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

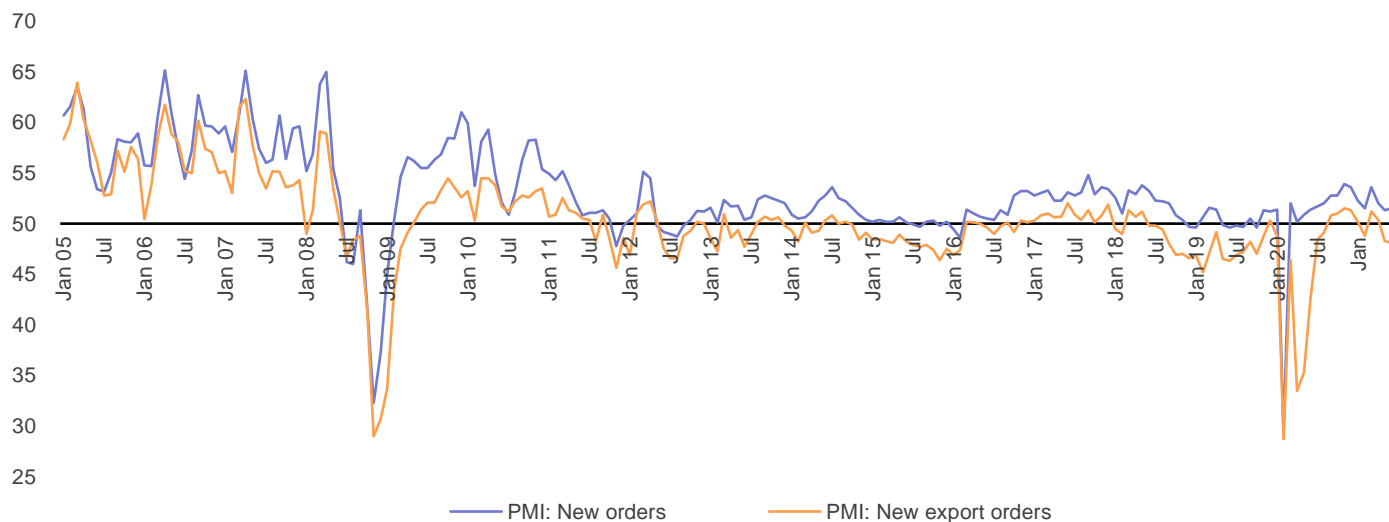
4. What the PMI tells us about the overall market demand

Overall market demand improves steadily

The new orders index stayed above 50 and fluctuated within a narrow range of 51.3 to 52.0 throughout April to June, indicating a steady pick up in the overall market demand lately.

Meanwhile, the new export orders declined from 50.4 in April to 48.3 in May and further to a one-year low of 48.1 in June, indicating a fall in new export orders lately. (See exhibit 9)

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



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

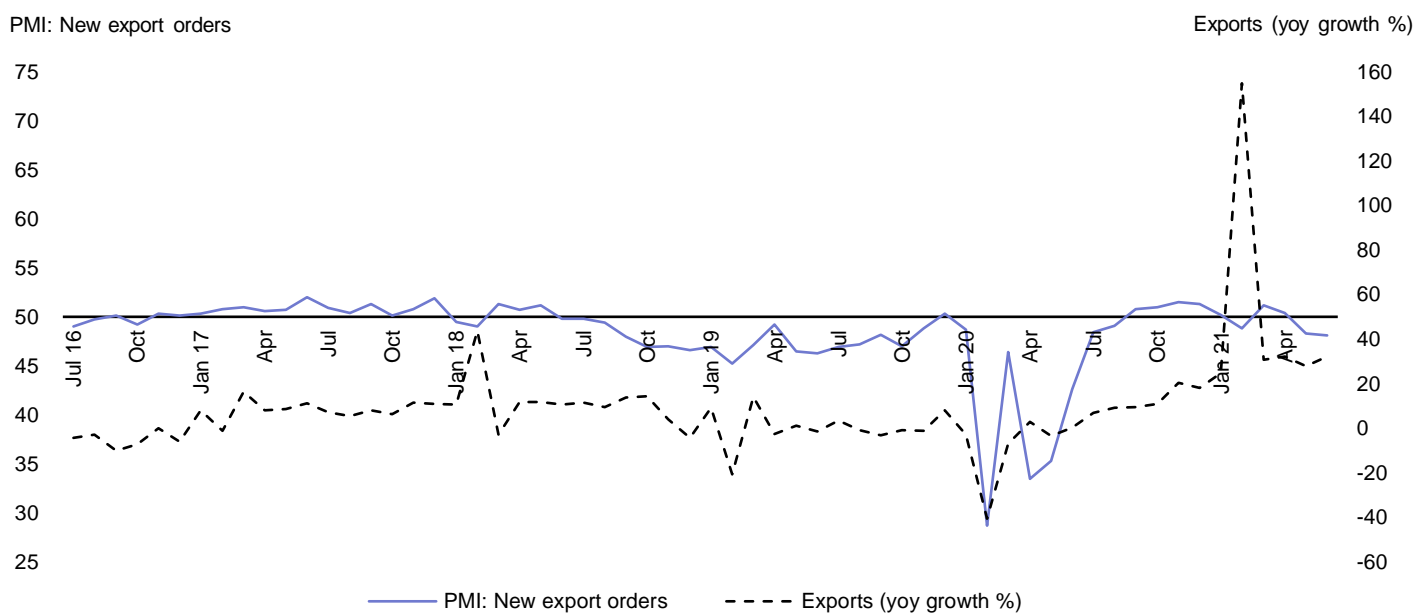
Sustained recovery in external demand bodes well for exports in 3Q21

Exhibit 10 plots the new export orders index against the year-on-year growth rates 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 2Q21, suggesting a sustained recovery in external demand for China’s exports. All in all, we forecast that China’s exports will grow by 10.0% in 3Q21.

With a continued improvement in external demand, we forecast that China’s exports will grow by 10.0% yoy in 3Q21.

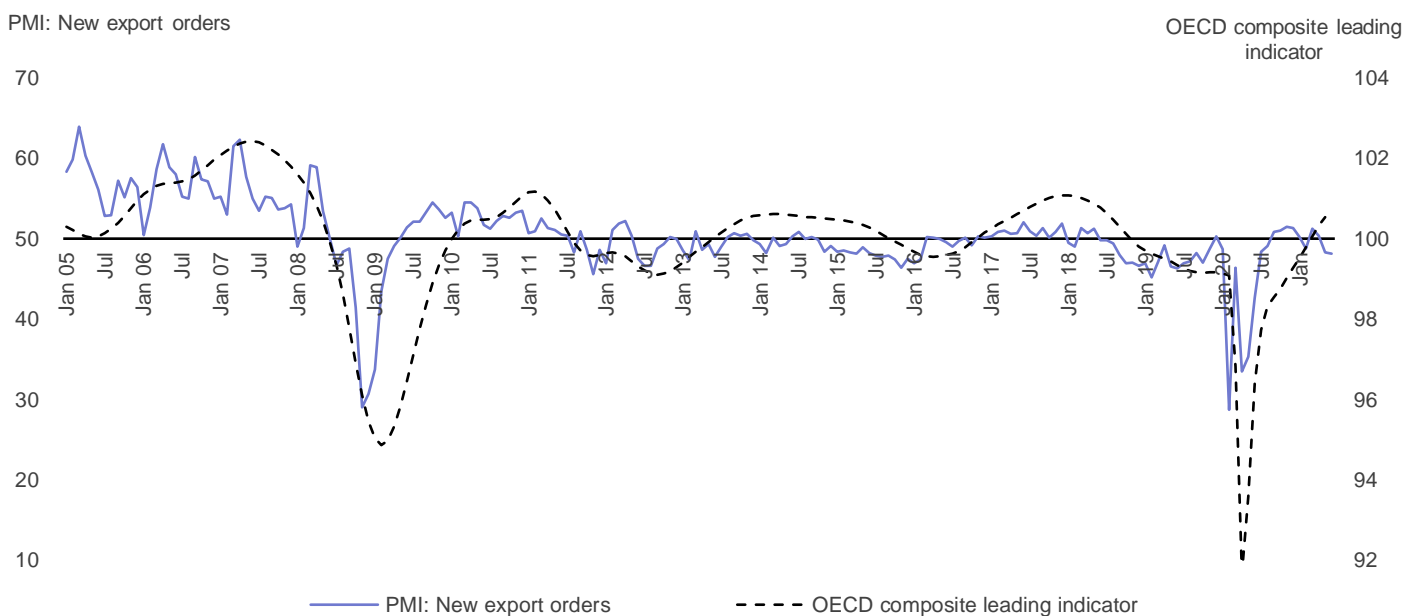
¹ The OECD composite leading indicator, compiled by the Organization for Economic Cooperation and Development, is designed to provide early signals of turning points (peaks and troughs) between expansions and slowdowns of economic activity, and covers Australia, Austria, Belgium, Canada, Czech Republic, 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, July 2016 to June 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 June 2021



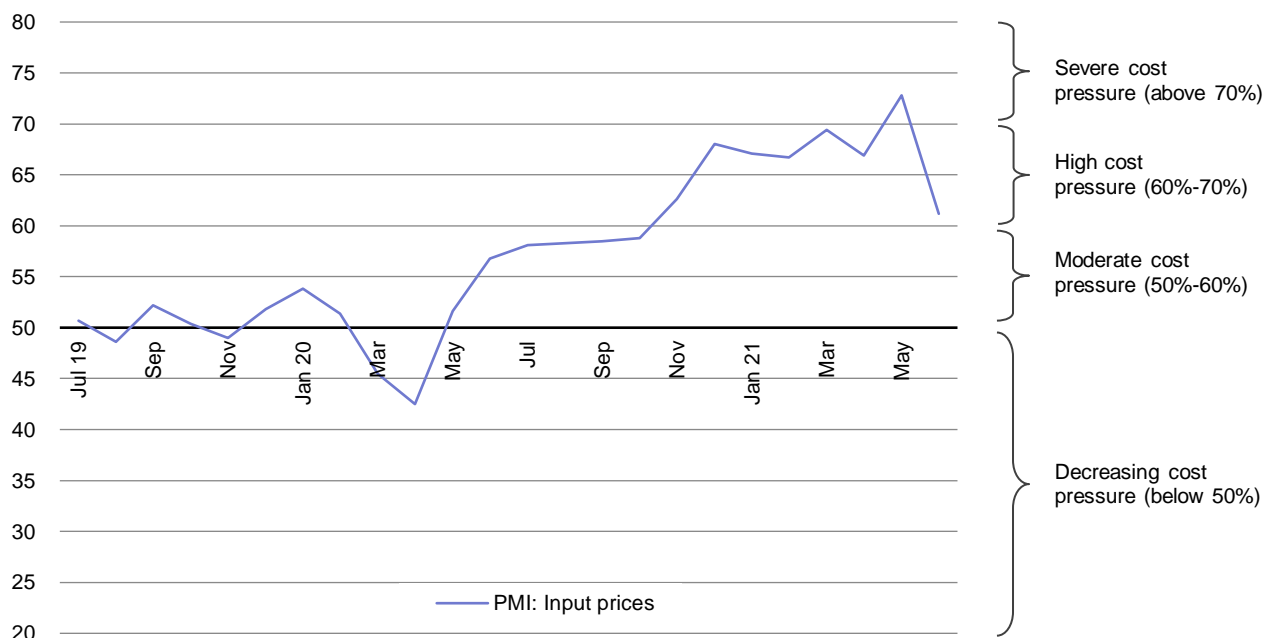
Source: China Federation of Logistics & Purchasing, China National Bureau of Statistics, Organization for Economic Cooperation and Development

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

Rising upstream prices exerts high cost pressures on manufacturers

The input prices index went up from 66.9 in April to 72.8 in May, and then fell to 61.2 in June. Despite the recent drop, the latest index reading was still well above the critical 50-mark, indicating a decelerating yet continued increase in the prices of production inputs lately, which would continue to exert high cost pressures on manufacturers. (Exhibit 12)

Exhibit 12: Input prices index, July 2019 to June 2021

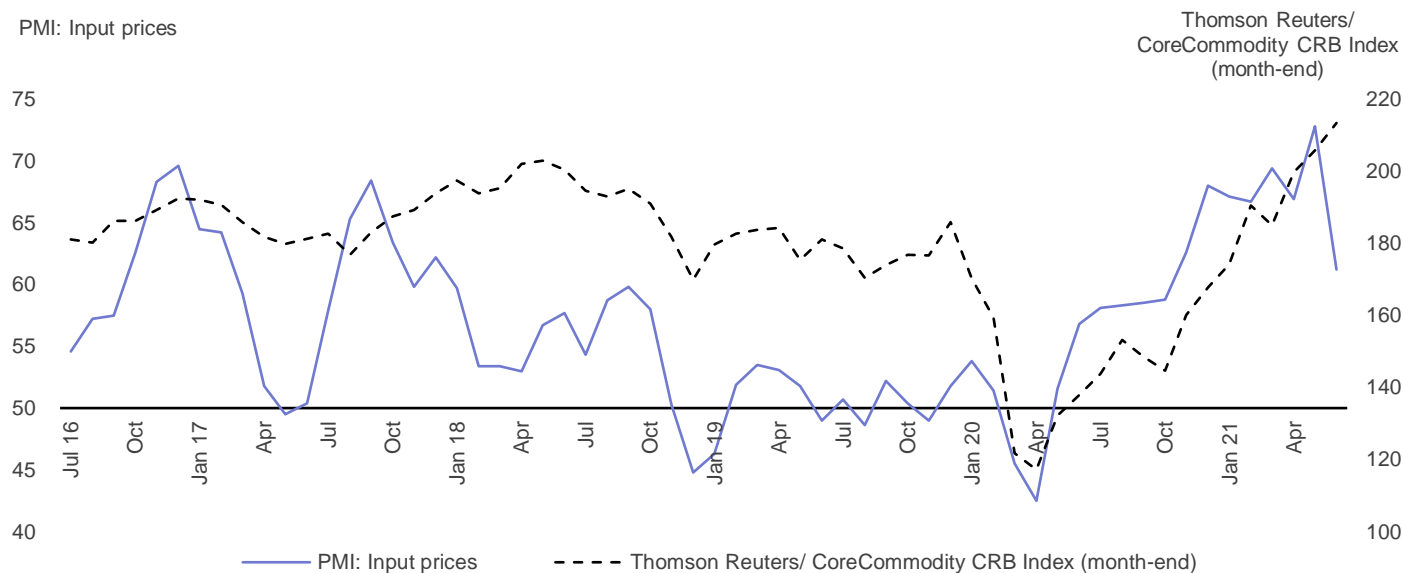


Source: China Federation of Logistics & Purchasing, China National Bureau of Statistics

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, July 2016 to June 2021

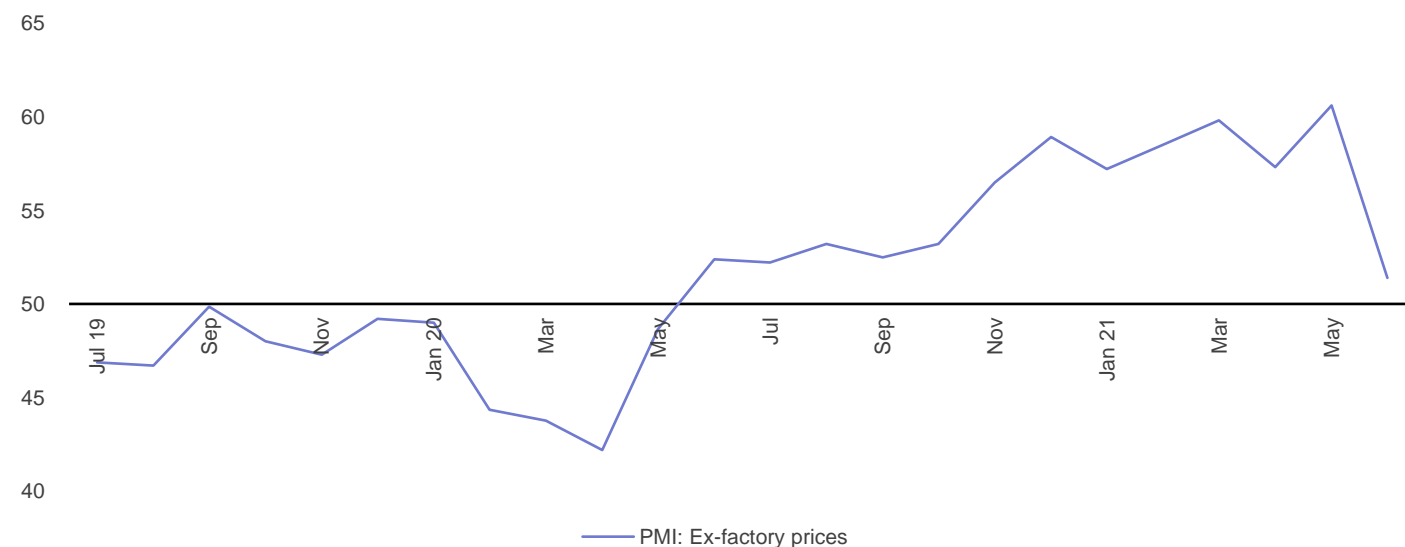


Source: China Federation of Logistics & Purchasing, China National Bureau of Statistics, Thomson Reuters

Manufacturers raise ex-factory prices of their products

After rising from 57.3 in April to 60.6 in May, the ex-factory prices index declined to 51.4 in June. The index readings indicate that Chinese manufacturers have continued to raise the ex-factory prices of their finished products lately amid high cost pressures, though the price increase has not been as steep as in the previous months.³ (Exhibit 14)

Exhibit 14: Ex-factory prices index, July 2019 to June 2021



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

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

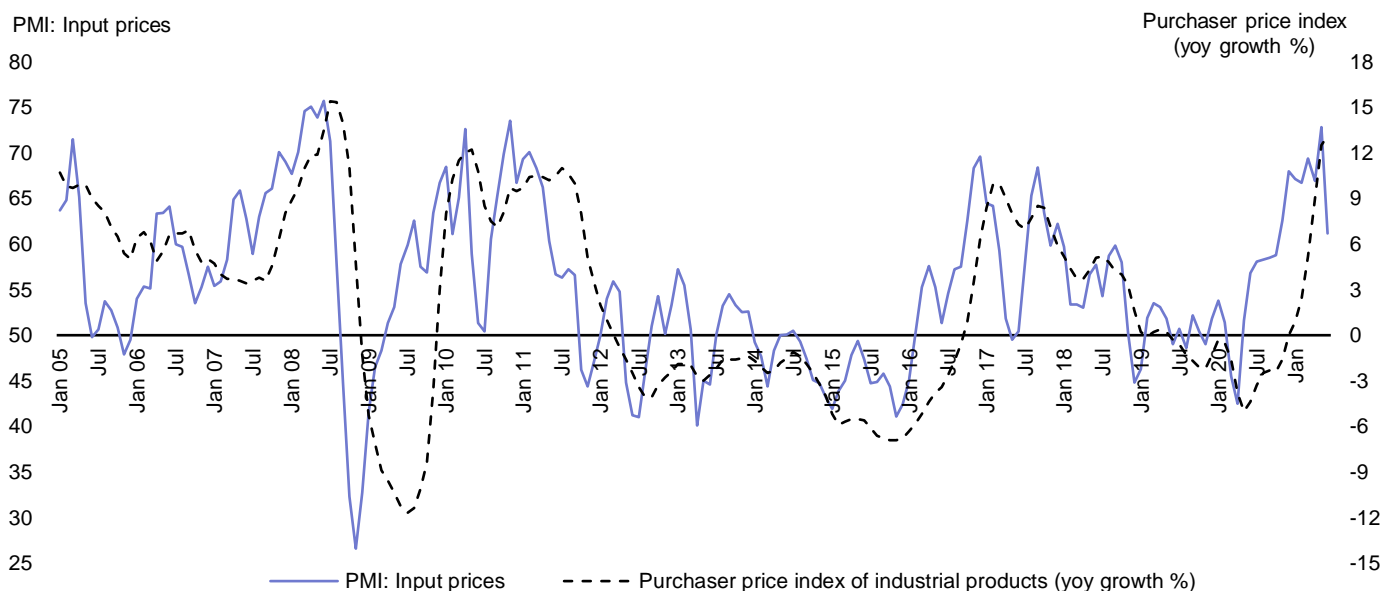
Growth in purchaser price index and PPI to moderate in 3Q21

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 moderate in 3Q21, due partly to a high base for comparison in the same period last year.

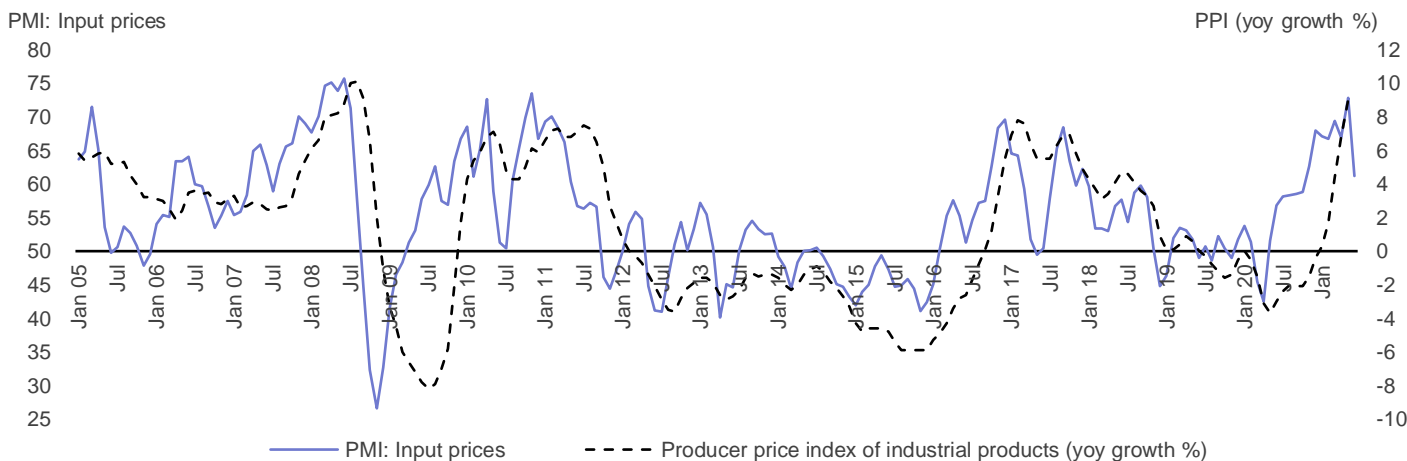
We expect that the year-on-year growth rates for both the purchaser price index and the PPI will moderate in 3Q21.

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



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

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



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

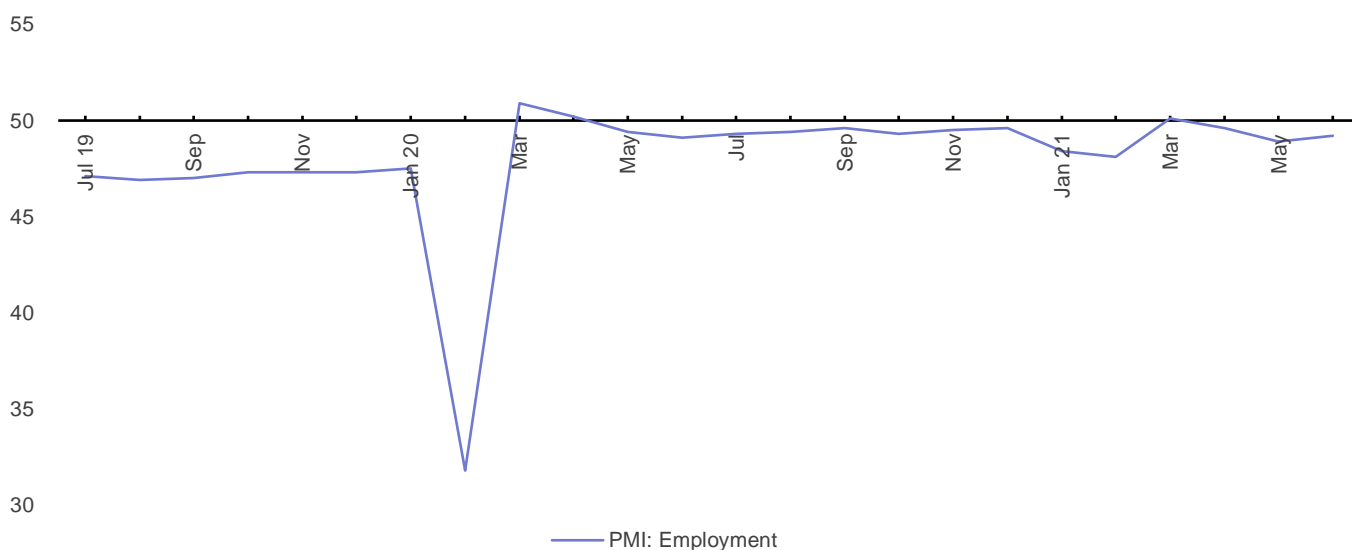
⁴ The producer price index of industrial goods (PPI), compiled by China National Bureau of Statistics, measures the prices of industrial products when they are sold for the first time after production.

6. What the PMI tells us about manufacturing employment

Stabilization of employment index indicates steady employment situation in manufacturing sector

The employment index registered 49.6 in April, 48.9 in May, and 49.2 in June respectively. The index has stabilized around 49.0, indicating the steady employment situation in the manufacturing sector in the past few months. (Exhibit 17)

Exhibit 17: Employment index, July 2019 to June 2021

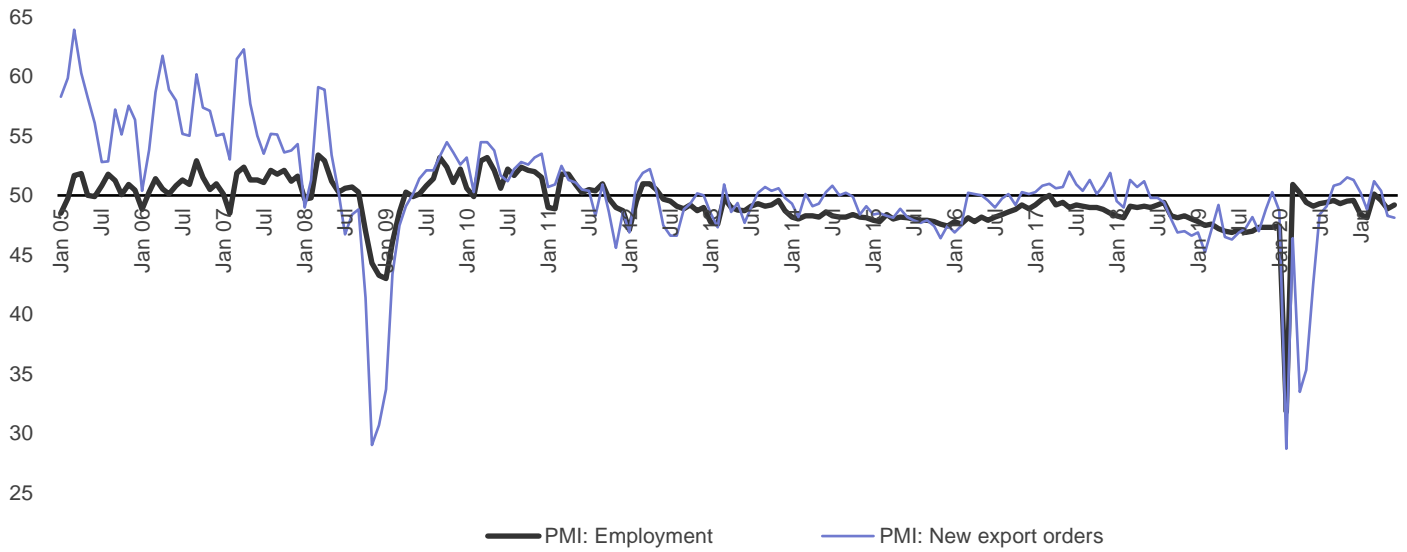


Source: China Federation of Logistics & Purchasing, China National Bureau of Statistics

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 continued growth in the export sector and the overall economy, we expect that the employment situation in the manufacturing sector will remain steady in 3Q21.

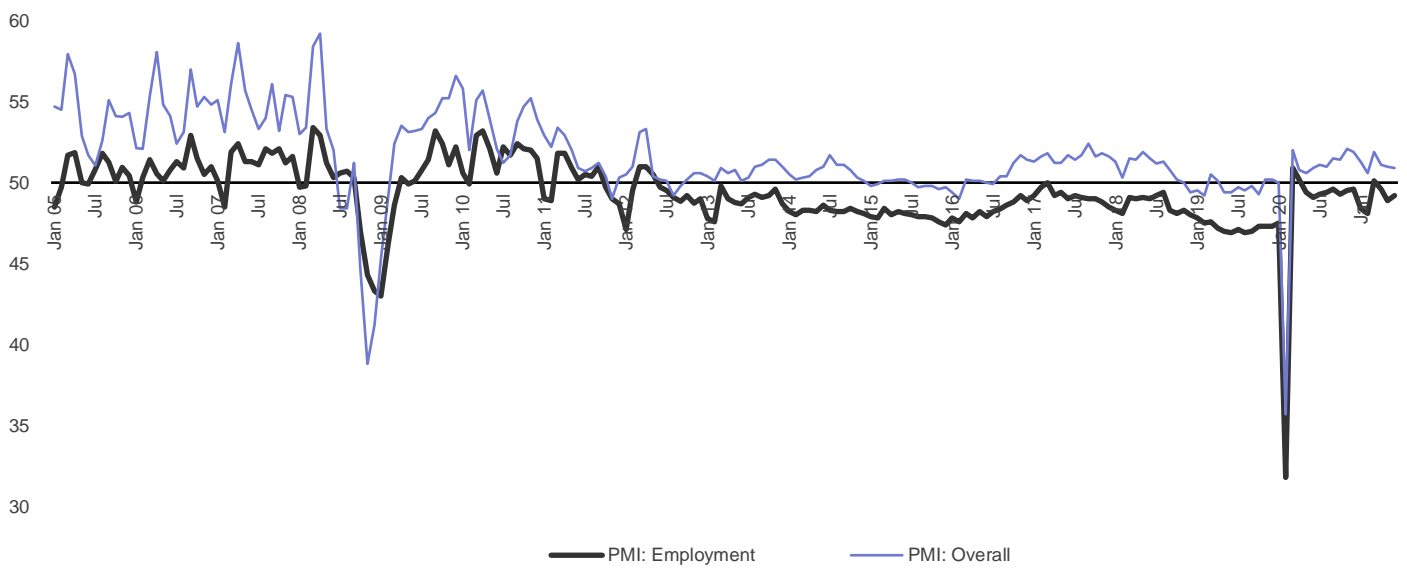
Given a continued growth in the export sector and the manufacturing industry, we expect the employment situation in the manufacturing sector to remain steady in 3Q21.

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



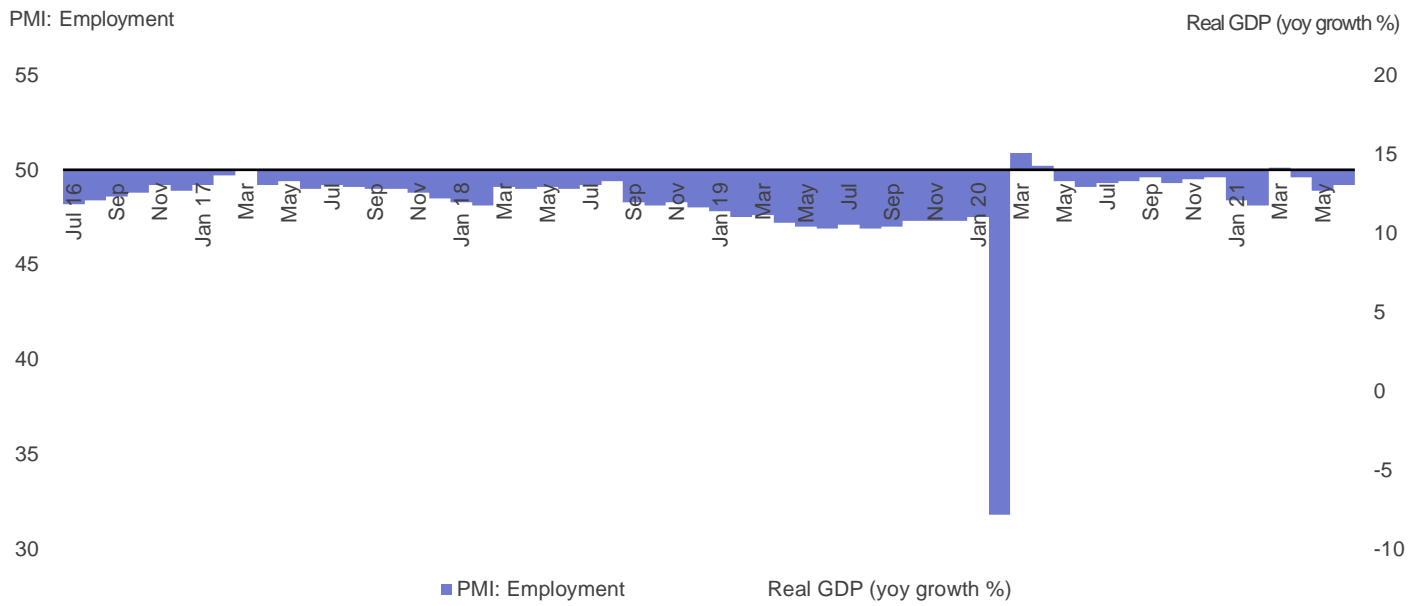
Source: China Federation of Logistics & Purchasing, China National Bureau of Statistics

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



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

Exhibit 20: Employment index and real GDP growth, July 2016 to June 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 26,000 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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