

China Flash

May PMI surprises to the downside, still showing expansion

The official NBS Purchasing Managers Index (PMI) for May, released today, surprised to the downside at 50.4% (BBVA: 51.5%; Consensus: 52.0%), down from 53.3% in April, but remained above the +50 expansion/contraction threshold (Chart 1). Similarly, private-sector (Markit) PMI also weakened from the previous month, confirming a moderating trend of the underlying growth momentum. These outturns suggest that, despite a recent reserve requirement ratio cut (of 50bps) and an increase in growth-supportive fiscal policies since mid-May, domestic demand remains weak, while at the same time external demand also remains sluggish. That said, the benefits from the previously mentioned policy support should start to have a gradual effect on growth in the coming months, and we would not rule out further policy easing; in particular, we expect another 100-150bp in cuts in the RRR in the coming quarters, and up to two interest rate cuts. Hence, growth momentum may be close to bottoming out, although there is now downside risk to our full-year GDP growth projection of 8.3%, given the weak external environment.

- **The decline in the official PMI was driven by both domestic and external demand** (Chart 2). On the supply side, the production subcomponent (with a weight of 25%) declined to 52.9% from 57.2% in April. The employment subcomponent (with a weight of 20%) also weakened (albeit only slightly) from 51.0% to 50.5%. On the demand side, the overall new order subcomponent (with a weight of 30%) moderated significantly, from 54.5% in April to 49.8% in May, the first contraction in five months. The weaker new order figure was partly driven by weakening external demand, as the new export order subcomponent eased to 50.4% from 52.2% in the previous month.
- **Private sector PMI also suggests weakening growth momentum.** Consistent with the outturn of the official PMI, the private-sector (Markit) PMI, also released on June 1, moderated to 48.4% from 49.3% in the previous month, and has now shown a contraction for seven consecutive months. The Markit index is based on a sample of smaller, more export-oriented companies.
- **A number of important economic indicators will be released in the coming days (June 9-13)**, including inflation, industrial production, retail sales, fixed asset investment, trade, and credit aggregates in May. We will be watching these indicators closely for signs of growth momentum in major areas of the economy.

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Chart 1
PMI moderated in May

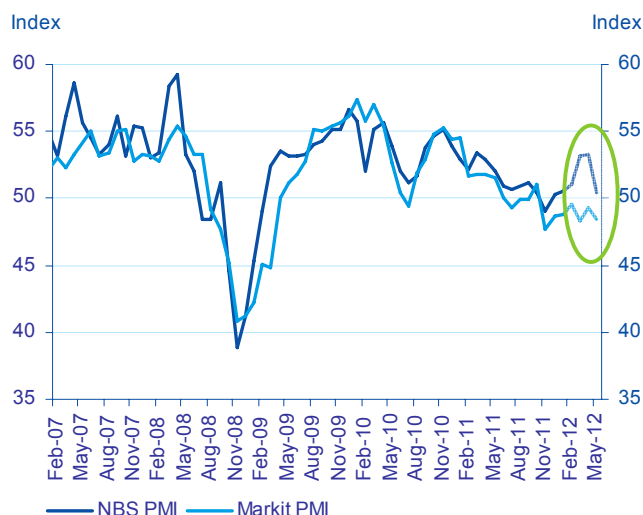
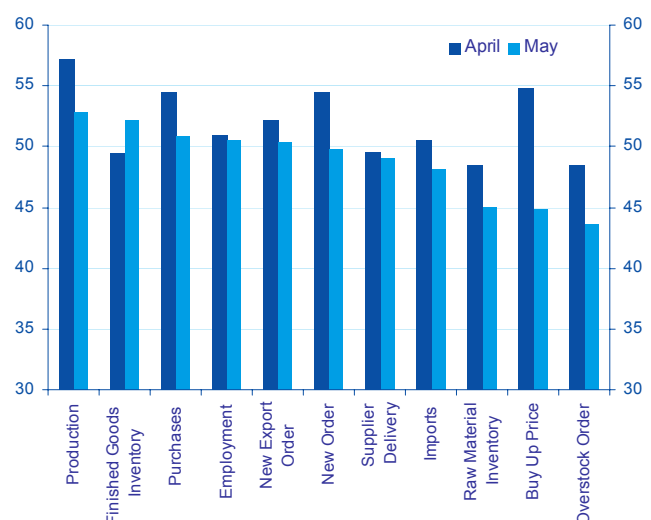


Chart 2
The moderation in May official PMI was broad-based





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