

## China: PMI boosted by holiday spending, risks elevated

China's non-manufacturing PMI was supported by decent spending during the Golden Week holidays. The manufacturing PMI grew steadily even though this was a short month. The main risks to this rosy picture are in chip shortages, high commodity prices, Covid emerging in Guangdong (the factory province), and uncertainty around the direction of the yuan.



People watch the semiconductor products exhibited at the 2020 World Semiconductor Conference in Nanjing city, east China's Jiangsu province

Source: Shutterstock

### PMI grew on holiday spending spree

China's non-manufacturing PMI increased to 55.2 in May, from 54.9 in April.

Non-manufacturing PMI is the focus of all May PMI data as May is a big month of holiday spending due to the Golden Week holidays. Spending was CNY113 billion during the holidays, achieving nearly 80% of 2019's pre-pandemic level. There was an increase in tourist volume of 17%.

The manufacturing PMI was fairly stable at 51.0 in May, from 51.1 in April and a decent result when taking into account the short month for factory work. Overall, new orders and new export

orders fell, which likely reflects the impact of the holidays rather than anything more sinister. We believe that both sets of orders will pick up in June.

## **Demand should continue to pick up but there are so many risks ahead**

After the spending spree in May, we think that consumers will start saving for the long October holidays and their next spending spree. While there might still not be a revival of international travel by then, Chinese consumers can still spend in duty-free shops within China.

External demand will likely remain flat since, even with economic recovery in the US and parts of Europe as vaccine rollouts suppress the Covid pandemic, this is likely to be offset by increasing Covid cases in ASEAN (China's biggest trade partner).

China has also seen emerging Covid cases in Guangdong province, where most electronic factories are located. Together with semiconductor chip shortages and high commodity prices, there are challenges facing producers.

### **Yuan uncertainty also a headache**

Exporters are now at a crossroads in deciding whether to convert their dollar receipts to take profits on their appreciated yuan revenues, or to hold on for longer if the dollar is going to weaken further. But there are increasing warnings from the PBoC about yuan volatility that should not be ignored.

We expect that if the yuan continues to appreciate after recent rounds of talking down the appreciation by the PBoC, the PBoC may more forcefully manage the yuan's path. We have to remember that the yuan exchange rate mechanism is a managed-float mechanism. It is legitimate for the PBoC to choose to stabilise the exchange rate if it thinks this could reduce financial risks.

We keep our USDCNY forecast at 6.30 by the end of 2021.