

China: PMI shows recovery at a slower speed

Recovery in both manufacturing and service sectors continued in China in April. We expect that an export demand recovery will help factory orders and that the May holiday will help the services sector. Both point to a rosy picture. But there are still risks from the technology war and too rapid reform



Manufacturing PMI points to slightly slower growth

China's manufacturing PMI was 51.1 in April, down from 51.9 in the prior month, but still indicates that the sector is growing.

Some production activity will have been affected by chip shortages, e.g. production of home appliances, automobiles, laptops and smartphones. As the chips shortage is expected to last for a few more quarters, there could be continuous rises in the price of semiconductors, which could push up the prices of electronic goods.

New export orders fell to 50.4 in April from 51.2 a month ago, this may reflect a delayed response to the Covid recovery in the US and in Europe. We should see some improvements in export orders as Covid continues to subside in these major export markets.

Services PMI still at high level albeit growing slower, and should go up in May

The service-sector PMI slowed to 54.9 due to a slowdown in real estate activity following tighter controls on home buying in some locations in China. But this could reverse in May as the long holiday is expected to result in more inbound tourism, and boost catering and retail sales.

On real estate activity, the central government would like to shrink the debt level of real estate developers. Big developers have consequently divested assets and repaid some debts. This approach may not apply to smaller developers. The government will allow more homes sales, but with the objective that this does not fuel home price gains. This will mean that property developers with weak cash flow will still be able to raise cash from home sales to repay past debts. So there is a lot of micro-management of housing policies at the city level.

The risk is that if deleveraging is pursued too rapidly, it could trigger a series of defaults. But as I mentioned, these policies are micromanaged, and they can be loosened if there are growing signs of default.

Risk and opportunity

Our GDP 2021 forecast is 8.6%, which looks like very strong growth. But don't forget that the base was low at 2.3% in 2020.

The main risk remains the technology war, which will make it difficult for China to pursue its ambition to expand the economy with the help of advanced technology. This risk is also an opportunity for China to develop its own technology and rely less on other economies. Technology investment will boom in China from now on. This will support future manufacturing and service PMIs.