

China PMI shows weaker economy in October. November will probably be worse.

China's PMI indices show that the economy was weak in October. Rising Covid cases, further contraction in construction and a possible contraction in export demand means this weakness will likely continue



We are worried that lockdowns in China will keep happening

Both manufacturing and non-manufacturing indices indicate a weaker Chinese economy in October

China's official manufacturing PMI recorded a contraction in activity (49.2) in October, down from the very modest expansion (50.1) indicated in September. The non-manufacturing PMI index also registered a contraction, falling to 48.7 in October, down from 50.6 in September a month ago.

For the manufacturing PMI, almost every sub-index fell from last month's reading. The exception to this was for raw material prices, which means even thinner profit margins for manufacturers. New orders were weaker, hinting at a further fall in activity levels in the coming months. New export orders remained in contraction, but slightly less so than last month. That makes it very hard to be optimistic about either manufacturing or exports for November and December.

In terms of the non-manufacturing PMI, the index was still dragged lower by real estate and construction. But adding to the gloom, the retail sector was also weaker, even though the first week of October was the Golden Week holidays. As a result, we believe that retail sales in October could be very soft.

All in all, October looks to have been a weak month for the economy, and November looks as if it will be no better than October. Compounding this is the fact that Covid cases are climbing again, and it is possible that we will see further small-scale lockdowns in China. We also expect a contraction in export demand in the coming months reflecting the weakening external environment.

Yuan to weaken further

We expect that the CNY will weaken further in the short term given the apparent weakness of the economy. Together with more Covid cases and expected lockdowns, it becomes even more difficult to be upbeat about the yuan.

But the central bank does not want the CNY to weaken too fast. With the recent increase in macro-prudential parameters for cross-border finance, we expect that demand for the yuan should increase when USDCNY gets close to 7.4. It is therefore possible that the yuan will remain range-bound between 7.2 and 7.4.