China: Worst-ever profit data for factories

Industrial profits fell sharply in China's state-owned and privately-owned enterprises in January and February. What can we expect for March and April?

-38.3%

The worst industrial profits on record

YoY YTD in February

Profits of factories plunged in the first two months

Industrial profits fell 38.3% year-on-year, year-to-date in February from -3.30% YoY YTD in December. This is the worst data on record.

The plunge spanned state-owned (-32.9%YoYYTD) and privately-owned (-36.6% YoY YTD) manufacturers. But manufacturers in Mainland China who are funded by Hong Kong, Macau and Taiwan suffered the most serious falls in profits, at 53.6% YoY YTD.

Credit should deteriorate as account receivables lengthen

There is a risk that the profit squeeze leads to a credit event, especially among smaller manufacturers, as the number of days of account receivables has increased to 71.3 days from December's 53.7 days. Again, Hong Kong, Macau and Taiwan-funded factories are at a higher risk. The number of days of account receivables they faced is 89.4.

When account receivables lengthen, the risk of a cash flow problem is higher. The risk of being unable to pay an invoice then goes up, which can turn a liquidity risk into a credit risk.

Some manufacturers are also suppliers. If their upstream manufacturers cannot pay them back in time, they will have difficulty paying their downstream suppliers. The chain effect has been seen in previous difficult times. This is no different.

71.3

Account receivable days

Chinese manufacturers

So far no sign of stress in the market

The good news is that the market in Mainland China so far has not seen any sign of a liquidity crunch or credit crunch. Interbank interest rates have been low, and we have not seen any spikes- that is there is no stress in the market in general. 7D to 3M interest rates have been below 2%, while the People's Bank of China 7D policy rate is currently at 2.4%.

But small manufacturers' problems may not be reflected in the interbank market as they have difficulty borrowing from banks.

According to the PBoC website, the central bank's re-lending programme to support the resumption of SME operations has released CNY130 billion, which is only a fraction of the CNY500 billion re-lending programme.

It is expected that some SMEs may close their businesses, which will affect the stability of the job market, and therefore will slow down the recovery of domestic consumption. This will put further pressure on SMEs.

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