Economic Analysis

China | August PMIs surprise the market to the upside

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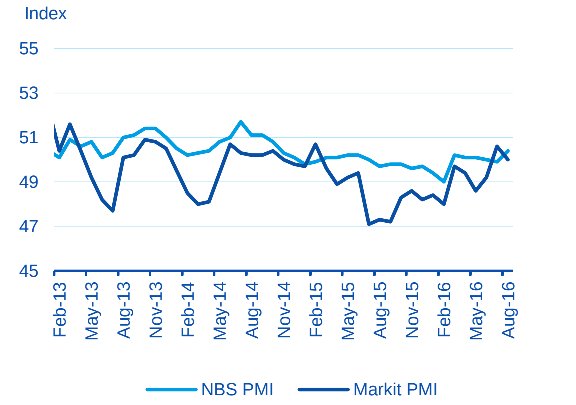
China's official manufacturing PMI unexpectedly rebounded above the watershed level in August. Its reading of 50.4 is also way above market expectations (Consensus: 49.8) and the July outturn of 49.9. Meanwhile, the Caixin manufacturing PMI, which tracks a survey sample with a larger proportion of small-and-medium enterprises (SMEs) than the official PMI, moderated to 50 in August from 50.6 in the previous month (consensus: 50.1) (Figure 1). Put together, although the official and Caixin PMIs have painted a mixed picture, manufacturing activities indeed gained traction in August, alloying investors' concerns over the risk of an imminent hard landing. However, optimists should take a grain of salt when interpreting these headline figures. The official service sector PMI slowed down to 53.5 in August from 53.9 in July. As China's economic rebalancing continued, the service sector now contributed to a larger share (50.5% as of 2015) to the country's total GDP than the manufacturing sector. Moreover, some anecdotal evidences show that the pickup in manufacturing activities is caused by the currently overheating property market. As the authorities set out to tighten the policy for the housing market again, the rebound can be proved to be short-lived. On balance, we maintain our growth forecast at 6.4% for 2016 (the official target is 6.5%) and 5.8% for 2017, which means no imminent hard landing in the second largest economy of the world.

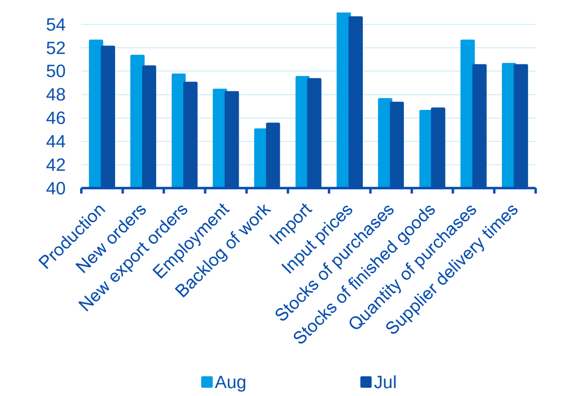
- **The pickup of the official manufacturing PMI is broad based by categories:** The improvement in the production index and new order index are pronounced in August. In particular, the former increased to 52.6 from its July reading of 52.1 while the latter rose to 51.3 from 50.4 in July. Export order index also picked up significantly to 49.7 from 49 in the previous month although the below-50 outturn still points to headwinds from the external environment. The employment and raw material stock indexes remain subdued while the index of delivery time is flat from its July outturn.
- **Looking ahead, more easing measures will be implemented in the rest of this year:** Due to the domestic growth headwinds and the weak recovery of external demand, policy stance needs to continue to be pro-growth, in order to offset the undergoing deleveraging and to avoid hard-landing. In this respect, we project another two RRR cuts with 50 bps each time and one asymmetric interest rate cut in the rest of 2016. The authorities will also implement more fiscal expansionary measures to boost public spending and infrastructure investment.

Figure 1
NBS PMI and Caixin PMI display a mixed picture



Source: CEIC and BBVA Research

Figure 2
Subcomponents of the NBS PMI



Source: NBS and BBVA Research

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