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# China Flash

## October PMI offers more signs of a modest upturn in growth

China's official PMI for October came out in line with expectations at 50.2%, rising back to above the 50 expansion threshold for the first time since July, and providing further comfort that growth is now picking up after bottoming out in Q3 (Chart 1). The increase was modest, but broad-based, showing a pickup in production and new orders, which may indicate that the inventory destocking cycle is winding down. As such, the PMI outturn suggests that the pickup in September activity indicators (for details, see *China Flash*) is in line with our expectation of a modest increase in GDP growth momentum in Q4 (to around 7.6% y/y), which would bring full-year growth to 7.6% in 2012 and 7.9% in 2013. The private-sector Markit/HSBC PMI, also released today, also showed a rise, to 49.5% from 47.9% in September (the index remains below 50, as it covers a set of smaller and more export-oriented companies). Given weak external conditions, low inflation, and downside risks to the outlook, we still expect further policy easing after the leadership transition is settled later this month.

- **The official PMI for October shows broad-based increases in production and demand (Chart 2).** On the supply side, the production subcomponent (with a weight of 25%) strengthened to 52.1% from 51.3% in September. The employment subcomponent (with a weight of 20%) also edged up, to 49.2% in October from 48.9% in the previous month. On the demand side, the overall new order subcomponent (with a weight of 30%) increased to 50.4% from 49.8% in September, and the new export order subcomponent also increased, to 49.3% from 48.8%.
- **We will be watching for October activity indicators (November 9-15),** for further signs of the strength of the rebound. We expect inflation to remain broadly flat at 2.0% in October, and to rise to only 2.6% by end-year. Other indicators such as industrial production, retail sales, and fixed asset investment should also show a further pickup from September.
- **More policy easing can be expected.** Given downside risks to the outlook and limited inflationary pressures, we still see room for a possible interest rate cut (increasingly an out-of-consensus call), as well as 1-2 more cuts in the RRR in the coming months. The strength of incoming activity indicators, external demand, and domestic liquidity will be key factors for the authorities in determining their monetary stance. Further fiscal support could also be forthcoming, especially once the leadership transition is complete in March (the 18th National Communist Party meeting is scheduled to begin on November 8, during which the Politburo members and Standing Committee will be selected, paving the way for the new the new President and Premier to be installed in March).

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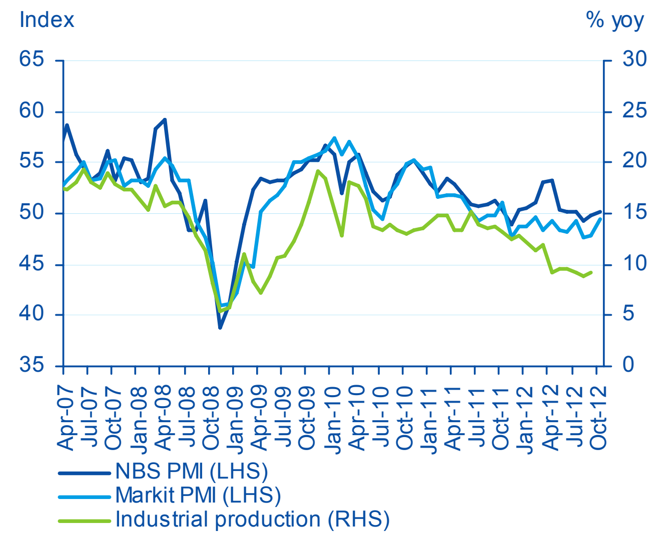
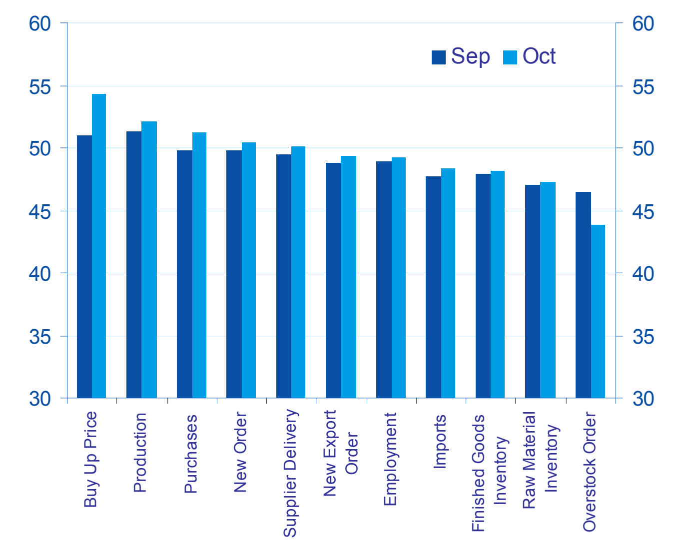
Chart 1
**Official PMI rises back to the expansion zone…**




Source: CEIC and BBVA Research

Chart 2
**… as production and new orders improve**




Source: CEIC and BBVA Research

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