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HSBC China Manufacturing PMI

Growth of the Chinese manufacturing sector continued to gain momentum during December.

Key findings:

- Manufacturing output rose sharply in December.
- Job creation remained solid.
- Both output and input price inflation accelerated.

At 56.1 in December, up from 55.7 a month previously, the headline HSBC China Manufacturing PMI™ pointed to a marked improvement of operating conditions in the Chinese manufacturing sector that was the second-fastest recorded by the series to date. For Q4 as a whole, the PMI averaged its highest reading in the survey history.

Behind December's PMI reading, the latest survey pointed to substantial increases in output and new business, while firms continued to add to their workforce numbers. Stocks of purchases rose for the second time in three months, while supplier delivery performance deteriorated at the most marked rate since August 2008.

Manufacturing production in China rose sharply in December, with the average rate of expansion for Q4 the fastest since Q2 2004. Where a rise in output was signalled, panellists widely attributed this to greater inflows of new work. There were also reports that growth was supported by new production lines coming on stream. Output levels have now risen for nine successive months.

Latest data pointed to the ninth consecutive monthly expansion of new order volumes received by Chinese manufacturers in December. The rate of increase in new work was considerable, accelerating to the fastest in four months. Those respondents that reported a rise in new business often linked this to buoyant demand from both domestic and external markets. Growth of

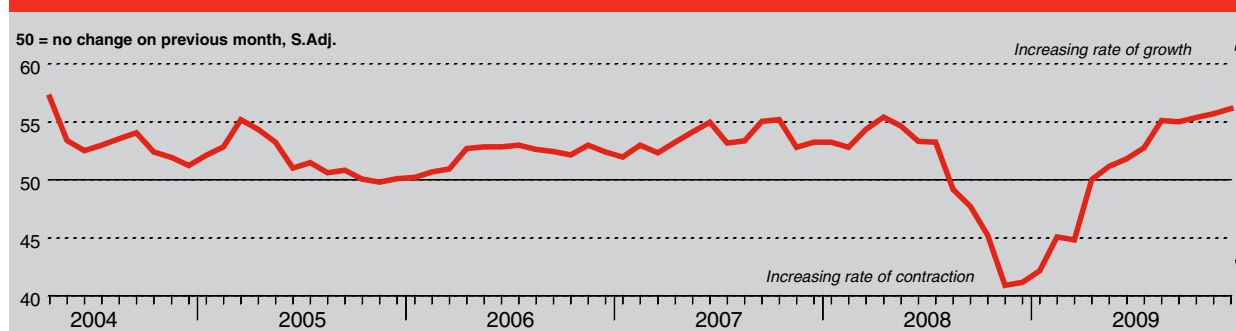
new export orders was the fastest since March 2005, and in marked contrast to the severe reductions seen in Q4 2008. Foreign order levels have risen throughout the second half of 2009.

Staffing levels in the Chinese manufacturing sector continued to rise in December. Despite easing for the second month running, the rate of job creation was the third-fastest since the start of the series in April 2004. Anecdotal evidence suggested that firms were encouraged to take on additional workers in line with increased production requirements.

December data signalled that prices charged by Chinese manufacturers were raised at a considerable rate that was the fastest since July 2008. Companies reported that a combination of buoyant market demand and rising raw material prices had generated inflationary pressure. Average input costs faced by Chinese manufacturers rose sharply in December. Where an increase in purchase costs was signalled, panellists frequently linked this to rising raw material prices, with steel mentioned in particular. Aluminium, coal, petroleum, textiles and zinc were also cited as having risen in price on the month.

In line with substantial growth of new business, buying activity in the Chinese manufacturing sector rose at the second-fastest rate in the survey history. Subsequently, supplier capacity was placed under additional pressure in December, with lead times lengthening for the fifth month in succession.

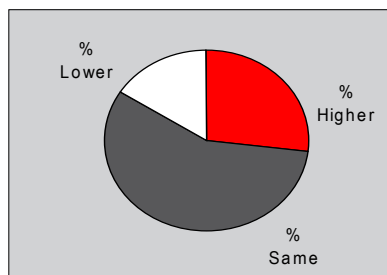
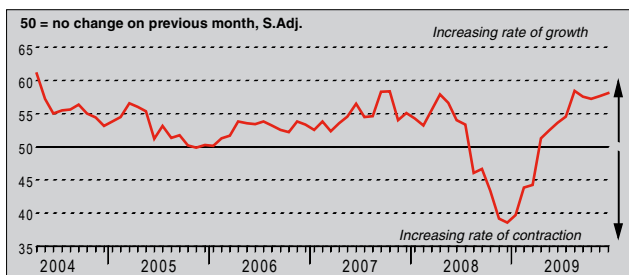
HSBC China Purchasing Managers' Index (PMI™)



The HSBC China Purchasing Managers' Index (PMI) is a composite indicator designed to provide an overall view of activity in the manufacturing sector and acts as a leading indicator for the whole economy. The indicator is derived from individual diffusion indices which measure changes in output, new orders, employment, suppliers' delivery times and stocks of goods purchased. A reading of the PMI below 50.0 indicates that the manufacturing economy is generally declining; above 50.0, that it is generally expanding. A reading of 50.0 signals no change. The greater the divergence from 50.0, the greater the rate of change signalled by the index.

Output Index

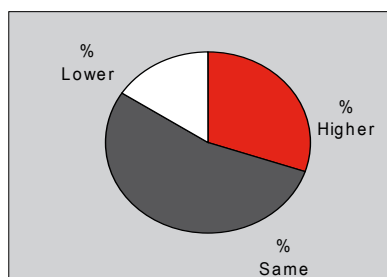
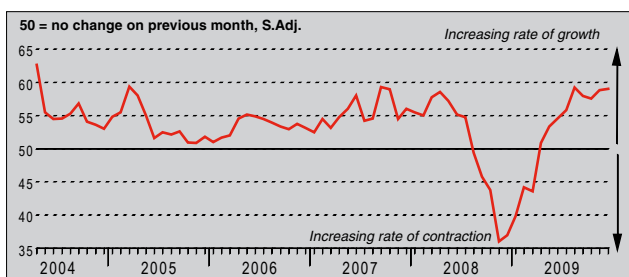
Q. Please compare your production/output this month with the situation one month ago.



Latest data signalled that Chinese manufacturing production continued to rise in December, increasing at a marked rate that was the fastest for four months. Furthermore, the average rate of expansion for Q4 was the most marked since Q2 2004. Where a rise in output was signalled, survey participants generally attributed this to substantial gains in new business and the start of new production lines. Output levels have now risen for nine successive months.

New Orders Index

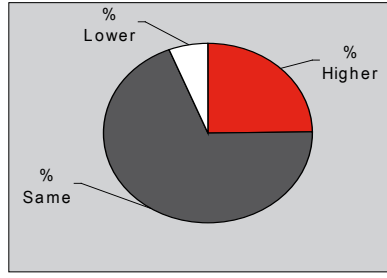
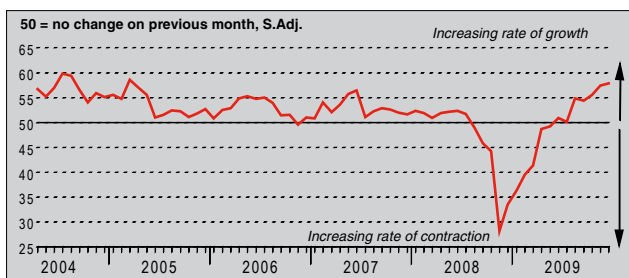
Q. Please compare the level of new orders received (China and export) this month with the situation one month ago.



New business growth was maintained for the ninth month running in December. The seasonally adjusted New Orders Index rose to a four-month high, pointing to a substantial expansion of new order volumes received by Chinese manufacturers. More than 30% of panellists reported an increase in new work from a month ago, with many linking this to buoyant market demand. Higher levels of promotional activity were also cited as having supported sales in the latest survey period.

New Export Orders Index

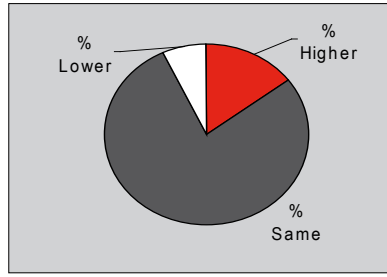
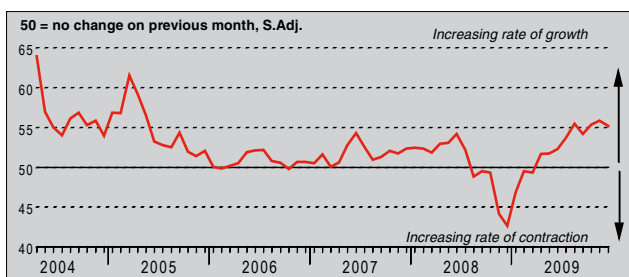
Q. Please compare the level of new export orders received this month with the situation of one month ago.



Levels of incoming new business received by Chinese manufacturers from foreign clients continued to rise in December, with almost one-quarter of respondents reporting an increase from the month before. Data signalled that the pace of expansion accelerated for the third successive month to the fastest since March 2005. Those panellists that reported a rise in export sales generally attributed growth to firmer demand from external sources, while some firms also mentioned competitive pricing.

Backlogs of Work Index

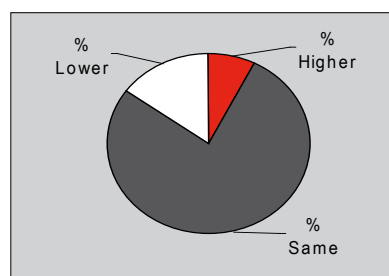
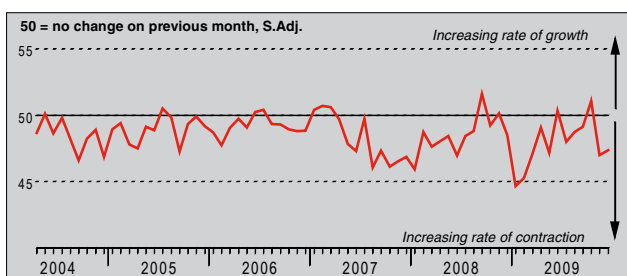
Q. Please compare the level of outstanding business in your company this month with the situation one month ago.



Volumes of unfinished business in the Chinese manufacturing sector increased for the ninth successive month in December. Backlogs of work rose at a rate that, although the slowest in three months, remained solid. Exactly 15% of survey participants reported an expansion of work-in-hand from a month earlier, versus 7% that signalled a decline. Anecdotal evidence suggested that outstanding business growth largely reflected greater inflows of new work.

Stocks of Finished Goods Index

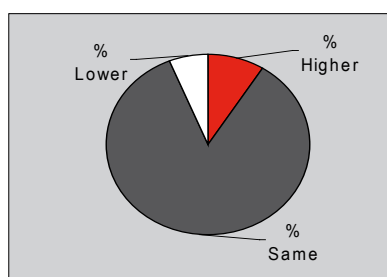
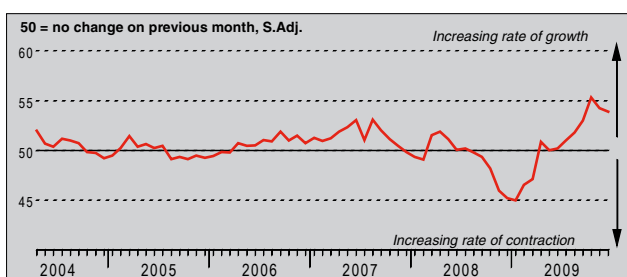
Q. Please compare your stocks of finished goods (in units) this month with the situation one month ago.



Stocks of finished goods in the Chinese manufacturing sector fell for the second successive month in December. Data indicated that inventory levels were reduced at a moderate rate that was slightly slower than in the previous month. Just over 15% of panellists reported a decrease in finished goods holdings since November, more than double the proportion that noted a rise. Evidence provided by the survey panel suggested that increased sales had led manufacturers to utilise existing stock.

Employment Index

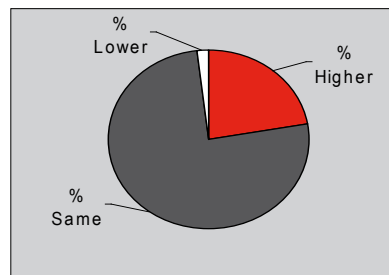
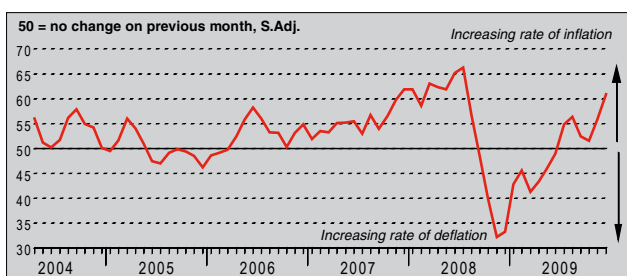
Q. Please compare the level of employment at your unit with the situation one month ago.



The seasonally adjusted Employment Index remained above the neutral level of 50.0 in December, pointing to a further expansion of Chinese manufacturing employment. Despite easing for the second month in a row, the rate of job creation remained solid, and comfortably above the historical average for the series. Where panellists reported a rise in staffing levels, this was often linked to greater production requirements and the need to expand capacity.

Output Prices Index

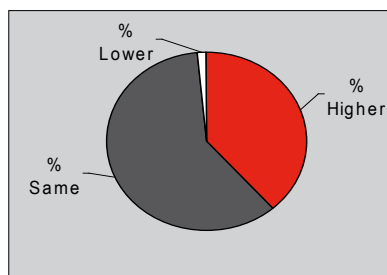
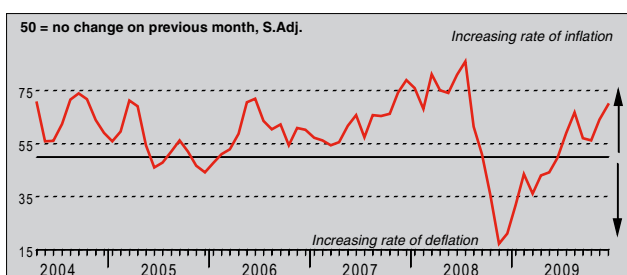
Q. Please compare the average price that you charge per unit of output (volume weighted) this month with the situation one month ago.



December marked the sixth successive month in which prices charged by Chinese manufacturers increased, with more than 22% of companies reporting a rise since November. This was up from almost 17% in November. After adjusting for seasonal variation, the Output Prices Index rose for the second month in a row, pointing to a sharp increase in output prices that was the most marked since July 2008. Manufacturers reported that a combination of strong market demand and rising prices for raw materials had generated inflationary pressures in December.

Input Prices Index

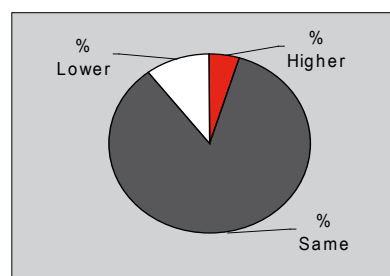
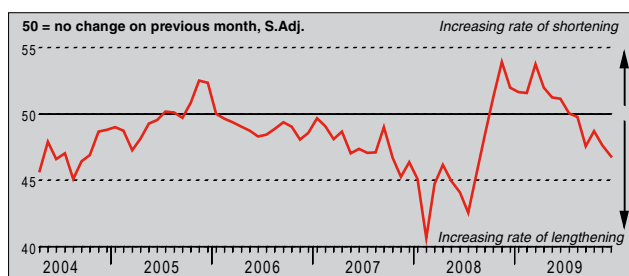
Q. Please compare the average price of your purchases (volume weighted) this month with the situation one month ago.



Average input costs faced by Chinese manufacturers rose for the sixth month running in December. The seasonally adjusted Input Prices Index rose markedly from the previous month, reaching a seventeen-month high and pointing to a considerable rate of input price inflation. Almost 39% of firms reported an increase in purchase costs since November, against only 2% that indicated a decline. Aluminium, coal, petroleum, steel, textiles and zinc were all reported to have risen in price from a month ago.

Suppliers' Delivery Times Index

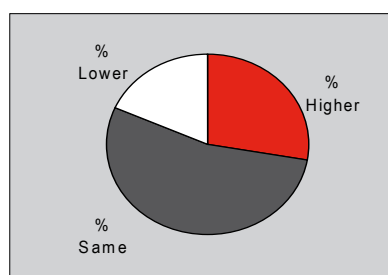
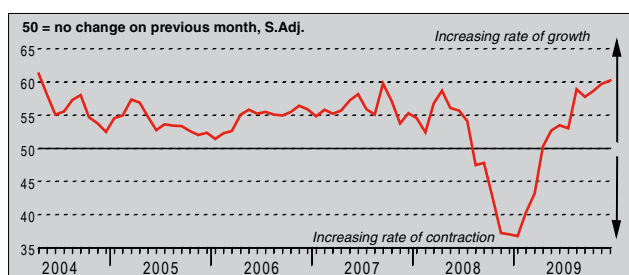
Q. Please compare your suppliers' delivery times (volume weighted) this month with the situation one month ago.



December data signalled that the average time taken by suppliers to deliver inputs to Chinese manufacturers lengthened for the fifth month in a row, mainly reflecting supply shortages at vendors. There were also reports that transportation problems and poor weather conditions had restricted the ability of some suppliers to meet delivery schedules. The extent to which average vendor performance deteriorated was the most marked since August 2008.

Quantity of Purchases Index

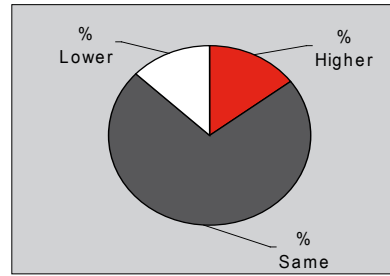
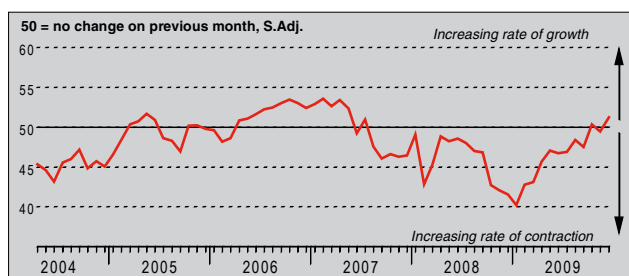
Q. Please compare the quantity of items purchased (in units) this month with the situation one month ago.



Buying activity amongst Chinese manufacturers rose again in December, extending the current period of expansion to nine months. Purchasing growth was the second-fastest recorded by the series to date, marking a distinct turnaround from the severe reductions seen at the start of 2009. Respondents widely commented that higher new order levels and subsequent rises in production requirements had supported growth of input buying.

Stocks of Purchases Index

Q. Please compare your stocks of purchases (in units) with the situation one month ago.



December data signalled that inventories of raw materials and semi-manufactured goods at Chinese manufacturers rose for the second time in three months. Although only modest, the rate at which stock levels were raised was the most pronounced since May 2007. Almost 15% of companies reported an increase in pre-production inventories since November, against 13% that recorded a decline. Anecdotal evidence suggested that the build-up of stock mainly reflected increased purchasing.

Notes on the Data and Method of Presentation

The Purchasing Managers' Index is based on data compiled from monthly replies to questionnaires sent to purchasing executives in over 430 manufacturing companies. The panel is stratified geographically and by Standard Industrial Classification (SIC) group, based on regional and industry contribution to Chinese Industrial Production. Survey responses reflect the change, if any, in the current month compared to the previous month based on data collected mid-month. For each of the indicators the 'Report' shows the percentage reporting each response, the net difference between the number of higher/better responses and lower/worse responses, and the 'diffusion' index. This index is the sum of the positive responses plus a half of those responding 'the same'.

The Purchasing Managers' Index (PMI) is a composite index based on five of the individual indexes with the following weights derived from the Chartered Institute of Purchasing & Supply's survey of the UK economy: New Orders - 0.3, Output - 0.25, Employment - 0.2, Suppliers' Delivery Times - 0.15, Stock of Items Purchased - 0.1, with the Delivery Times index inverted so that it moves in a comparable direction.

Diffusion indexes have the properties of leading indicators and are convenient summary measures showing the prevailing direction of change. An index reading above 50 indicates an overall increase in that variable, below 50 an overall decrease.

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