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HSBC China Manufacturing PMI™

Growth of the Chinese manufacturing sector gathered momentum at the start of Q4.

Key findings:

- Strong domestic demand drives production higher.
- New export orders rose only modestly.
- Input price inflation the fastest in over two years.

Chinese manufacturing sector operating conditions continued to strengthen at the start of the final quarter, with the rate of improvement quickening to the fastest since April. The headline seasonally adjusted HSBC China Manufacturing Purchasing Managers' Index™ (PMI™) climbed from 52.9 to 54.8 in October, representing one of the largest month-on-month rises in the PMI since the start of the series in April 2004. Behind the latest reading, October's survey pointed to strong and accelerated increases in both output and new business. However, manufacturing employment fell for the first time since March 2009.

Manufacturing output growth surged in October. The latest increase, which extends the current period of expansion to three months, was the fastest since January. Where a rise in production was signalled, respondents commonly linked growth to higher intakes of new business.

Overall new business received by Chinese manufacturing firms rose sharply in October, with the pace of expansion reaching a six-month high. However, a faster uptick in total new work relative to new export orders, which increased only modestly, suggested that total new business growth was centred on the domestic market in October.

Backlogs of work rose for the fourth month running in October, although the rate of accumulation was only modest. Anecdotal evidence suggested that outstanding business growth reflected

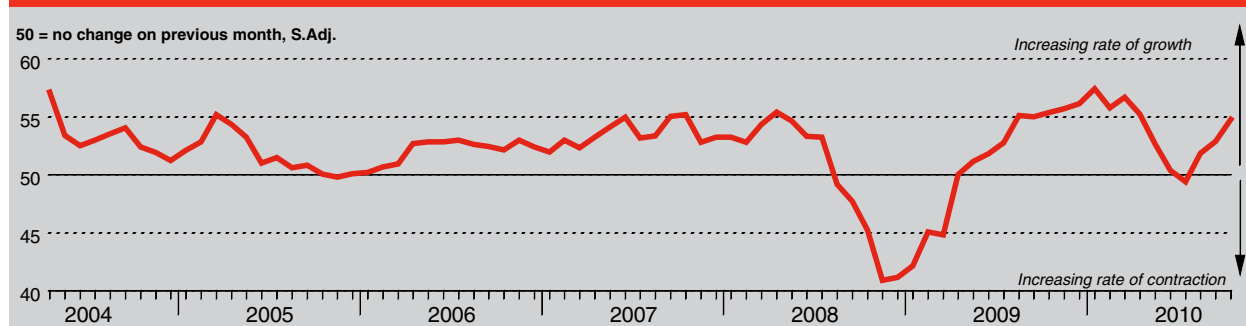
strong gains in new work.

Average input costs faced by Chinese manufacturing companies rose considerably in October, and at the fastest rate since July 2008. The PMI input prices measure has risen more than thirty-one points since July, highlighting the rapid extent which inflationary pressures have built within the sector. Prices paid for coal, cotton, grain and steel were all reported as having risen since September. Higher cost burdens were also reflective of attempts to meet government emission targets, state restrictions on electricity usage and, in some cases, the rising price of global commodity futures.

Output prices set by Chinese manufacturing firms rose further in October, with the rate of inflation hitting a twenty-seven month high. The latest increase was the third in as many months, and faster than the long-run trend. Factory gate price inflation predominantly reflected the need to protect operating margins in the face of rising input costs.

Purchasing activity rose markedly in October. As a result, the rate at which vendor performance deteriorated quickened to the joint fastest in the current fifteen-month period of lengthening lead times. Rapidly rising production needs, coupled with increased delivery delays, meant that manufacturing firms often had to utilise existing stocks of purchases to meet new business growth in the latest survey period.

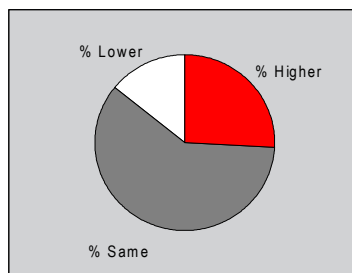
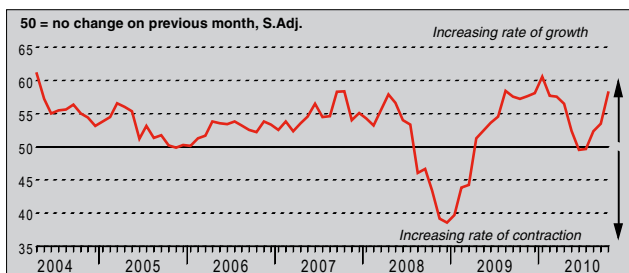
HSBC China Purchasing Managers' Index™ (PMI™)



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

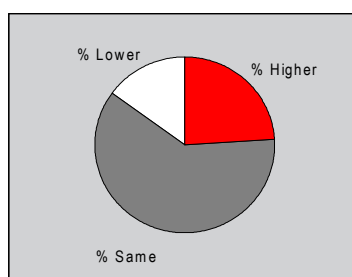
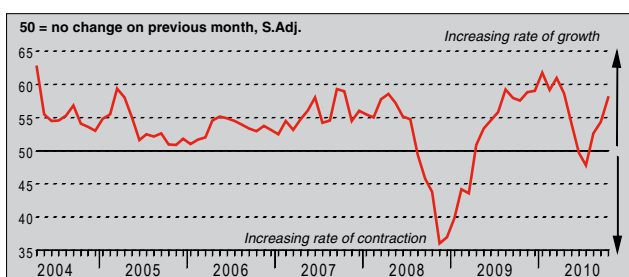
Q. Please compare your production/output this month with the situation one month ago.



Manufacturing production growth accelerated rapidly in October, with the month-on-month rise in the seasonally adjusted Output Index amongst the largest since the start of the series in April 2004. The rate of expansion was substantial, and the fastest since January. According to respondents, production growth predominantly reflected a strong rise in new order volumes. The latest increase in output was the third in as many months.

New Orders Index

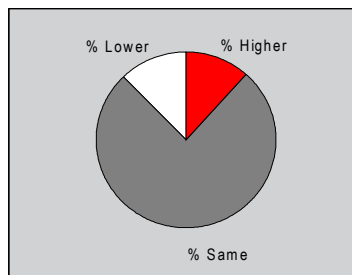
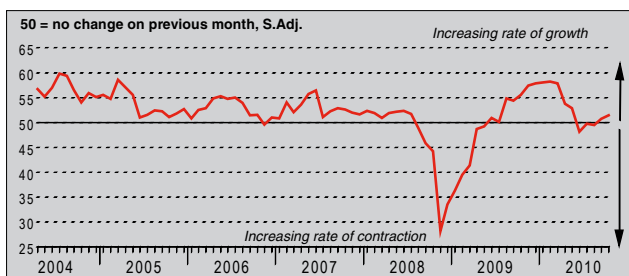
Q. Please compare the level of new orders received (China and export) this month with the situation one month ago.



New orders rose steeply in October, with the rate of expansion quickening to the fastest since April. The latest increase in orders stretches the current period of growth to three months. Where a rise in new work was signalled, respondents commonly attributed this to rising demand for manufactured products. However, data suggested that total new business growth was centred on the domestic market, as highlighted by a much faster rise in overall new business relative to new export orders.

New Export Orders Index

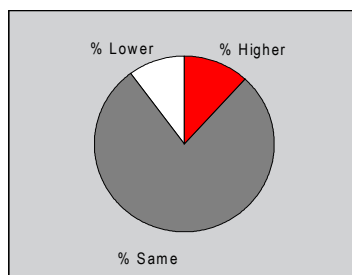
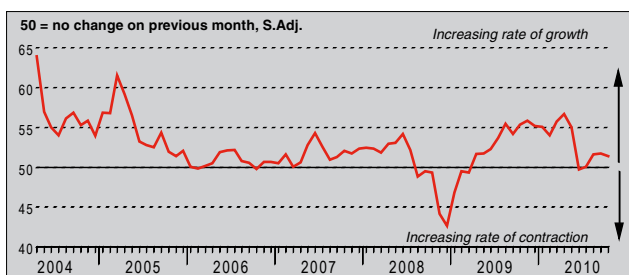
Q. Please compare the level of new export orders received this month with the situation of one month ago.



The seasonally adjusted New Export Orders Index remained above the neutral level of 50.0 for the second month running in October, pointing to a further rise in new export business. Nonetheless, the rate of expansion was only modest, and much slower than the overall rate of new business growth. The majority of panellists (around 76%) reported that foreign order levels remained unchanged since the preceding month. Panellists widely commented that demand from external sources remained lacklustre continuing amid global economic uncertainty.

Backlogs of Work Index

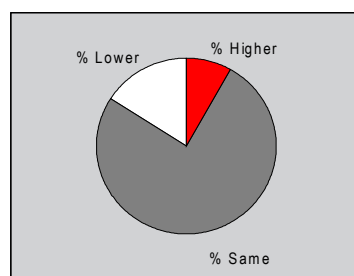
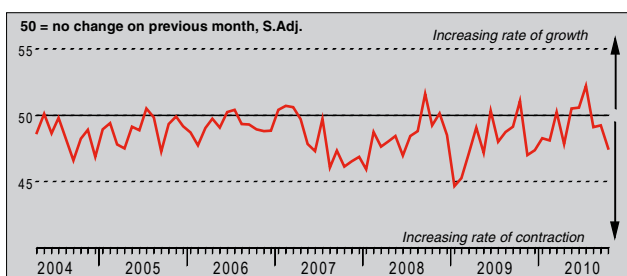
Q. Please compare the level of outstanding business in your company this month with the situation one month ago.



Outstanding business in the Chinese manufacturing sector rose in October, with the seasonally adjusted Backlogs of Work Index posting above the neutral 50.0 threshold for the fourth month in a row. Approximately 12% of panellists reported an increase in unfinished business since the preceding month, which the majority attributed to greater inflows of new business. Nonetheless, the rate of accumulation was only modest, and the least marked in three months.

Stocks of Finished Goods Index

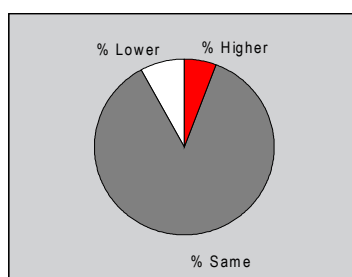
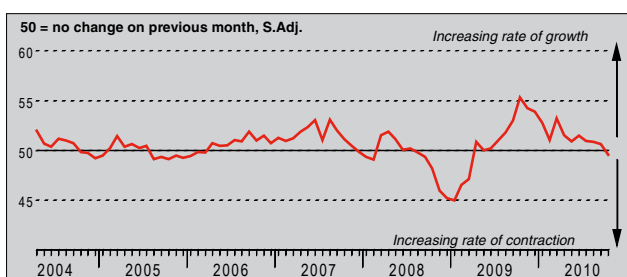
Q. Please compare your stocks of finished goods (in units) this month with the situation one month ago.



Stocks of finished goods continued to fall in October, extending the current period of contraction to three months. The rate at which post-production inventories were depleted was moderate, and accelerated to the sharpest in 2010-to-date. Exactly 16% of the survey panel reported a drop in stock levels since September, around double the proportion that indicated an increase. Anecdotal evidence suggested that some manufacturers opted to meet greater inflows of new business through stock depletion.

Employment Index

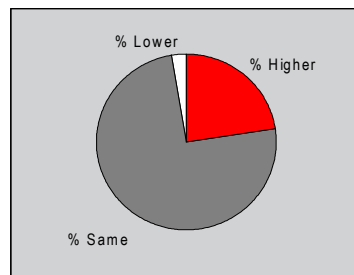
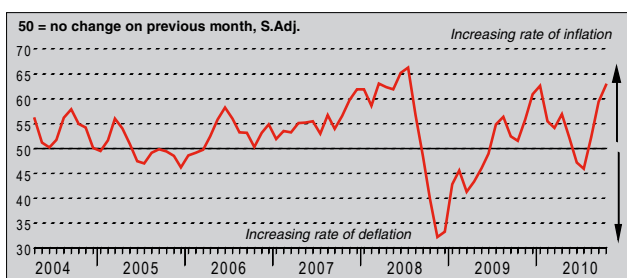
Q. Please compare the level of employment at your unit with the situation one month ago.



October data signalled that manufacturing employment in China fell for the first time since March 2009. Anecdotal evidence provided by the survey panel suggested that reduced staffing levels reflected a combination of employee resignations and retirements. However, the rate at which employee numbers were reduced was only slight. Where a rise in employment was signalled, panellists often linked growth to new product developments and, in some cases, company expansion plans.

Output Prices Index

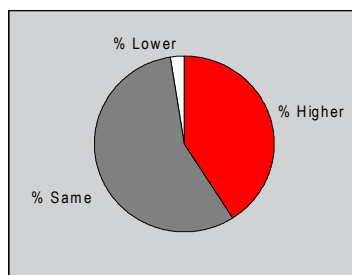
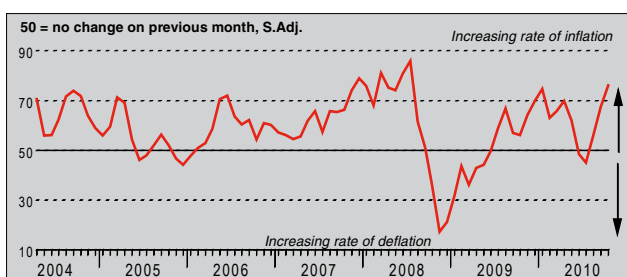
Q. Please compare the average price that you charge per unit of output (volume weighted) this month with the situation one month ago.



Prices charged by Chinese manufacturers for their finished goods increased for the third consecutive month in October. The rate of factory gate inflation was substantial, with the seasonally adjusted Output Prices Index climbing to its highest level since July 2008. Higher charges were widely attributed to the need to rebuild operating margins in the face of sharply rising input costs. Almost 23% of panellists signalled an increase in their selling prices, compared with only 3% that indicated a decline.

Input Prices Index

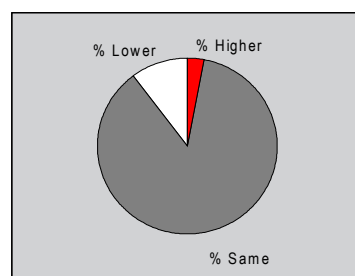
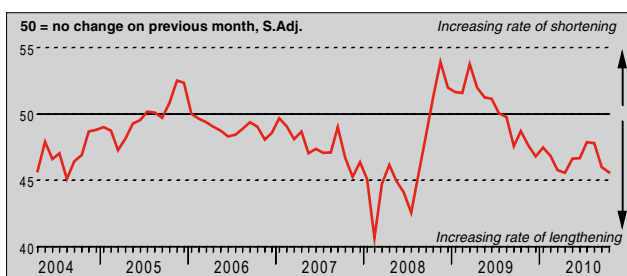
Q. Please compare the average price of your purchases (volume weighted) this month with the situation one month ago.



The rate of input cost inflation in the Chinese manufacturing sector accelerated sharply in October, with the seasonally adjusted Input Prices Index rising to its highest level since July 2008. Since July's recent low, the index has climbed over thirty-one points, highlighting the rapid acceleration of input price inflation. Prices paid for coal, cotton, grain and steel were all reported as having risen since September. Government restrictions on electricity usage, the need to meet emissions targets and, in some cases, the price of commodities futures were all cited as having led costs higher.

Suppliers' Delivery Times Index

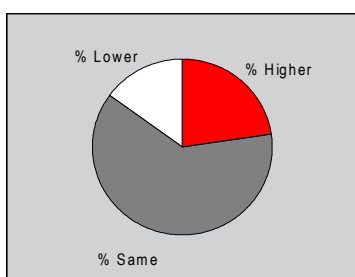
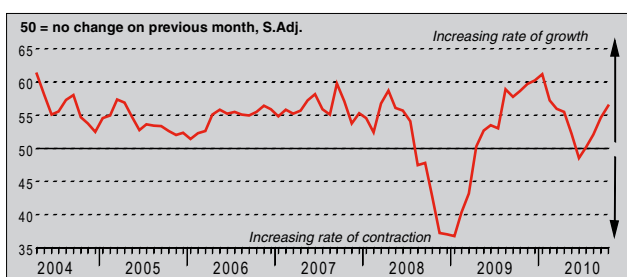
Q. Please compare your suppliers' delivery times (volume weighted) this month with the situation one month ago.



The average time taken by suppliers to deliver inputs to Chinese manufacturers lengthened in October, with around 10% of panellists reporting slower lead times since the preceding month. The rate of deterioration in vendor performance was marked, and the joint fastest in the current fifteen-month period of lengthening delivery times. Companies commented that delays in the delivery of inputs primarily reflected supply shortages at vendors. Transportation difficulties and government restrictions on electricity usage were also mentioned by a number of respondents.

Quantity of Purchases Index

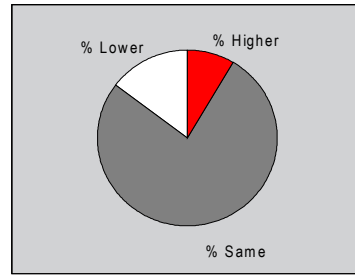
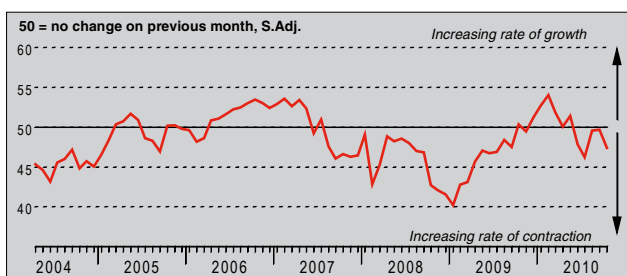
Q. Please compare the quantity of items purchased (in units) this month with the situation one month ago.



The seasonally adjusted Quantity of Purchases Index remained above the neutral 50.0 threshold in October, and was at a level indicative of a marked rise in purchasing among Chinese manufacturing firms. Those respondents that reported an increase in buying activity commonly linked growth to strong new business gains and a corresponding rise in production requirements. The latest increase in purchasing was the fourth in as many months, and the fastest since February.

Stocks of Purchases Index

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



Data signalled that inventories of semi-manufactured goods and raw materials declined for the fifth successive month in October. The rate of contraction was moderate, and accelerated to the sharpest in three months. Almost 15% of panellists reported a fall in stock levels since September, compared to around 9% that indicated a rise. Respondents signalled that the latest drop in pre-production inventories reflected rapidly rising production needs.

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: 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.

Markit do not revise underlying survey data after first publication, but seasonal adjustment factors may be revised from time to time as appropriate which will affect the seasonally adjusted data series.

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