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HSBC China Manufacturing PMI™

Output rises only modestly in February, as new order growth slows. Price pressures remain substantial.

Key findings:

- PMI falls to seven-month low.
- New order growth eases to slowest since last August.
- Supplier delivery times lengthen at marked rate.

PMI survey data signalled that Chinese manufacturing operating conditions continued to improve in February, albeit at a markedly reduced rate. Output rose only modestly, as new business growth eased markedly and new export orders fell for the first time since last August. Meanwhile, companies continued to pass on strong cost inflation to clients through increased factory gate charges.

The headline seasonally adjusted HSBC Purchasing Managers' Index™ (PMI™) fell from 54.5 to a seven-month low of 51.7 in February. The latest reading was up slightly from the earlier flash estimate of 51.5, but still below the long-run trend of 52.3. The month-on-month drop in the index was one of the largest since the start of the series in April 2004.

Manufacturing production in China continued to increase during February, although the rate of expansion eased sharply to the slowest in the current seven-month period of growth. Moreover, the latest increase was only modest, and slower than the long-run series average. According to respondents, the weaker rise in output predominately reflected a slowdown in overall new business growth to a six-month low. Furthermore, intakes of new export orders fell marginally in February, thereby ending a five-month period of growth.

Although total new order growth eased sharply since January, backlogs of work in the Chinese manufacturing sector rose at a solid and accelerated rate in February. The latest increase was

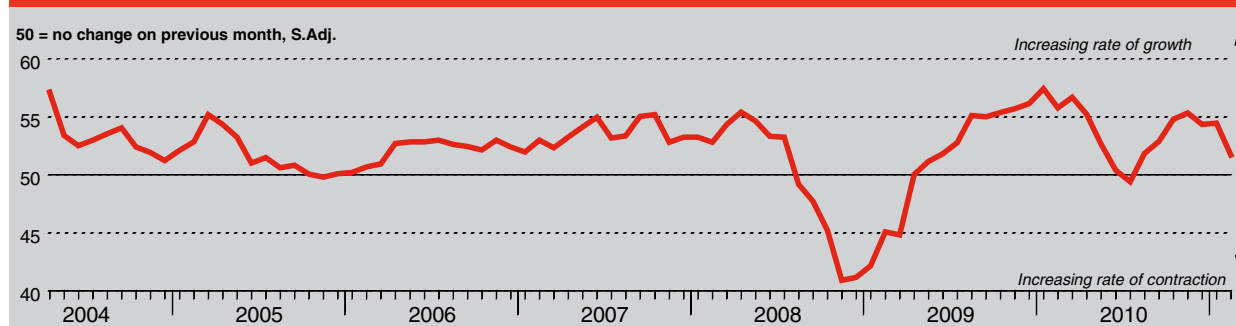
the eighth in successive months.

February data pointed to the first month-on-month decline in Chinese manufacturing employment since last October, although the pace of reduction was only marginal. Where a decline in staff numbers was signalled, respondents often linked job shedding to employee resignations.

Reduced output requirements prompted firms to scale back their purchasing in February, with growth easing substantially to its weakest in six months. As a result, stocks of purchases fell for a second successive month, with the rate of depletion quickening since January. Despite this, average vendor performance deteriorated at the joint-fastest rate in the current nineteen-month period of lengthening lead times. Panellists often linked longer delivery times to supply shortages at vendors.

Input cost inflation accelerated to a three-month high in February, with manufacturers attributing this to rising raw material and fuel costs. Prices paid for copper and steel were also reported as having risen from one month earlier. According to respondents, cost pressures emanated from domestic markets in the latest survey period. Firms continued to pass on higher costs to clients through increased output charges in February. The rate of factory gate charge inflation was substantial, and quickened to the fastest since November. The latest increase in charges was the seventh in as many months.

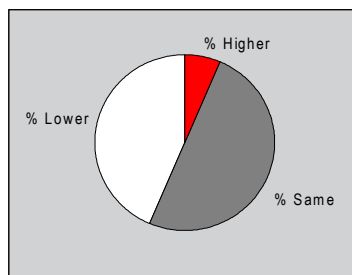
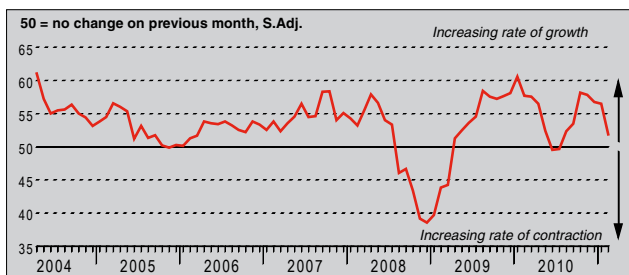
HSBC China Purchasing Managers' Index™ (PMI™)



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

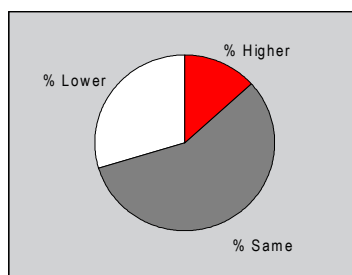
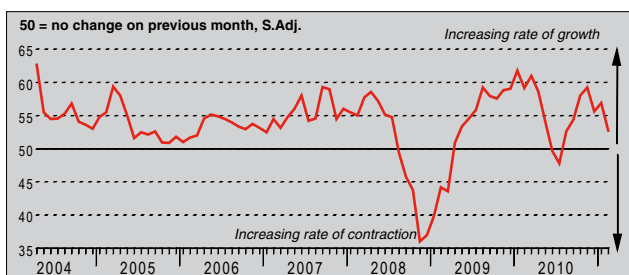
Q. Please compare your production/output this month with the situation one month ago.



According to the latest data, Chinese manufacturing production continued to rise in February. Nonetheless, the seasonally adjusted Output Index fell from 56.5 to a seven-month low of 51.9, signalling a sharp easing in the rate of expansion. The index was at a level indicative of only a modest increase in manufacturing output. Furthermore, overall growth was weaker than the long-run trend. The slower rise in production primarily reflected a weaker increase in total new business.

New Orders Index

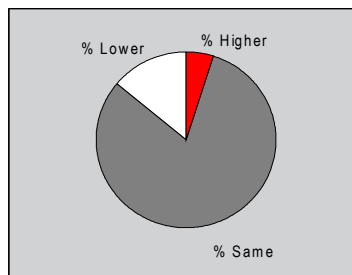
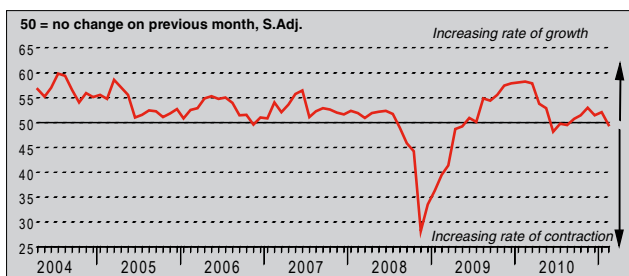
Q. Please compare the level of new orders received (China and export) this month with the situation one month ago.



The level of incoming new business received by Chinese manufacturing firms rose further in February. However, the rate of expansion was weak in the context of historical data after easing markedly since January. This was highlighted by the seasonally adjusted New Orders Index falling more than four points to a six-month low. Moreover, the index reading was below the long-run series average. New order levels have now risen continuously since last August.

New Export Orders Index

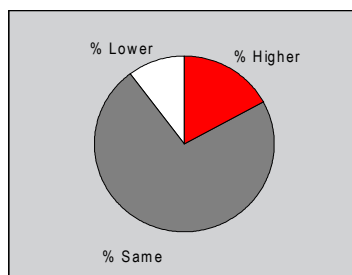
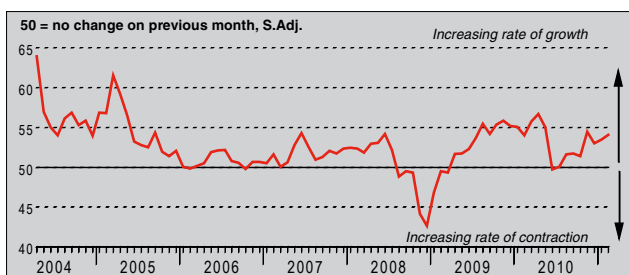
Q. Please compare the level of new export orders received this month with the situation of one month ago.



After adjusting for seasonal variation, the New Export Orders Index fell below the neutral 50.0 threshold in February, pointing to the first month-on-month reduction in new export business since August 2010. The latest reading was in stark contrast to that seen one year earlier, when the index hit a near-record high. Nonetheless, the rate of contraction was only marginal, with the vast majority of panellists (approximately 81%) reporting that new export orders were unchanged since the preceding month.

Backlogs of Work Index

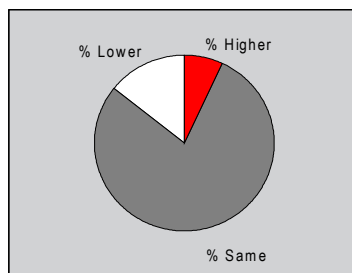
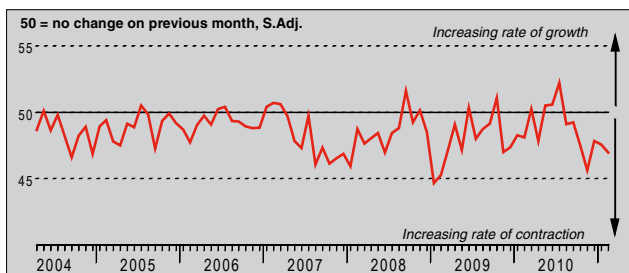
Q. Please compare the level of outstanding business in your company this month with the situation one month ago.



The seasonally adjusted Backlogs of Work Index remained above the neutral level of 50.0 in February, pointing to a further rise in outstanding business at Chinese manufacturing firms. The rate of backlog accumulation was solid, and quickened to the fastest in three months. Around 17% of the survey panel reported a rise in unfinished work since January, which they generally attributed to growing capacity pressures. The latest increase extends the current period of expansion to eight months.

Stocks of Finished Goods Index

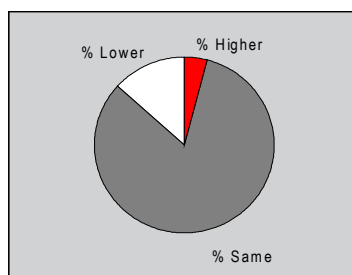
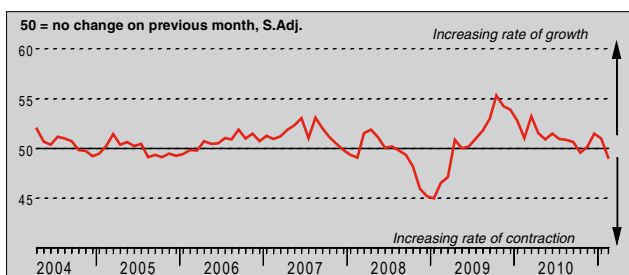
Q. Please compare your stocks of finished goods (in units) this month with the situation one month ago.



February data pointed to another reduction in post-production inventories, with the seasonally adjusted Stocks of Finished Goods Index recording a level indicative of a moderate rate of stock depletion. Approximately 14% of panellists reported a decline in finished goods holdings from one month earlier, around double the proportion that signalled an increase. Anecdotal evidence suggested that some manufacturers opted to meet greater inflows of new business through stock depletion.

Employment Index

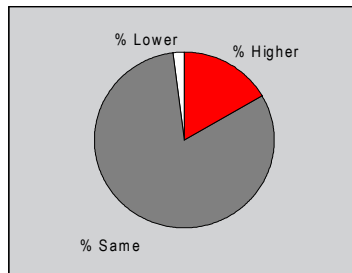
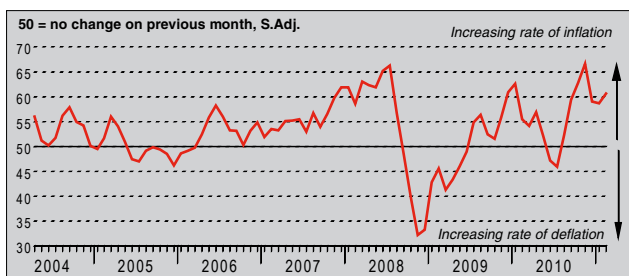
Q. Please compare the level of employment at your unit with the situation one month ago.



Employee numbers in the Chinese manufacturing sector fell in February, thereby ending a three-month period of growth. However, the pace at which firms reduced their payrolls was only slight, with the vast majority of panellists (almost 83%) reporting no change in employment levels from a month ago. Where a decline in staff numbers was signalled, respondents often linked this to employee resignations. Panel members that reported hiring additional staff attributed job creation to higher output requirements.

Output Prices Index

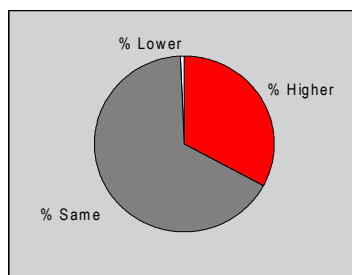
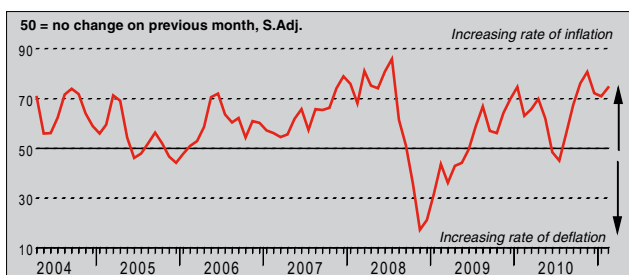
Q. Please compare the average price that you charge per unit of output (volume weighted) this month with the situation one month ago.



Factory gate prices set by Chinese manufacturing firms rose sharply in February, with almost 17% of panellists reporting an increase since the preceding month. This compared to only 2% that indicated a reduction. As a result, the rate of output charge inflation quickened to a three-month high, and was much stronger than the long-run series average. Anecdotal evidence suggested that inflation reflected the passing on of higher input costs to clients. Charges at the factory gate have now risen continuously since August 2010.

Input Prices Index

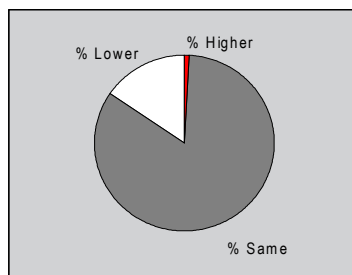
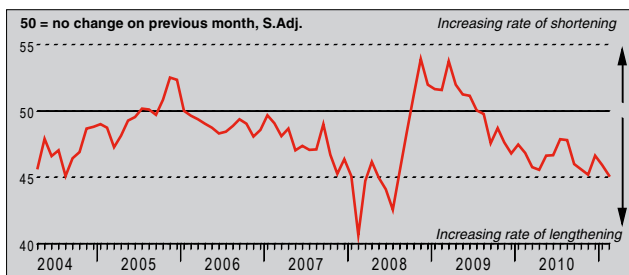
Q. Please compare the average price of your purchases (volume weighted) this month with the situation one month ago.



Average input costs faced by Chinese manufacturing firms increased for a seventh successive month in February. After adjusting for seasonal factors, the Input Prices Index rose to a three-month high, a level indicative of a substantial rate of purchase price inflation. According to respondents, cost inflation reflected higher raw material and energy costs. Prices paid for copper and steel were reported as having risen since January. There was evidence that cost pressures emanated from domestic markets in the latest survey period.

Suppliers' Delivery Times Index

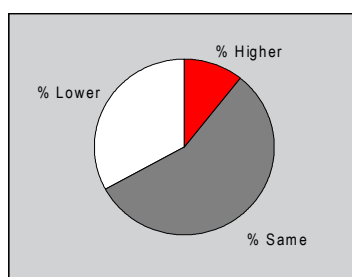
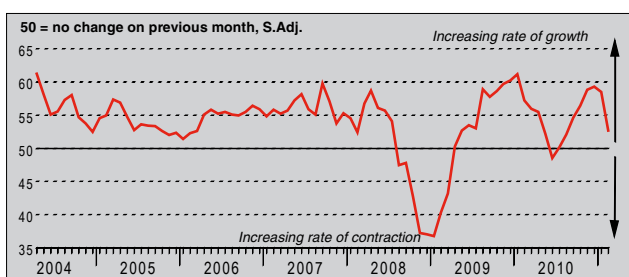
Q. Please compare your suppliers' delivery times (volume weighted) this month with the situation one month ago.



The seasonally adjusted Suppliers' Delivery Times Index posted its joint-lowest reading for over two-and-a-half years in February, signalling a marked deterioration in average vendor performance. Slower lead times have now been signalled for nineteen successive months. Longer delivery times were recorded by almost 16% of the survey panel, with the majority attributing this to supply shortages at vendors. There were also reports of transportation difficulties.

Quantity of Purchases Index

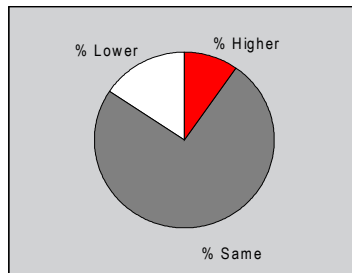
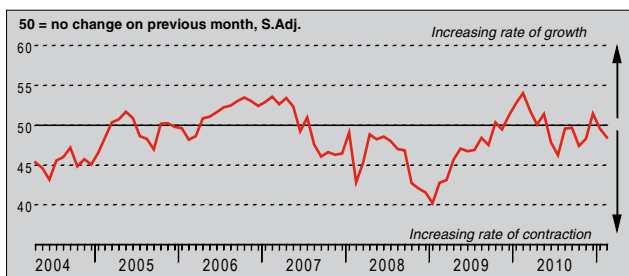
Q. Please compare the quantity of items purchased (in units) this month with the situation one month ago.



Buying activity in the Chinese manufacturing sector continued to rise in February, with the seasonally adjusted Quantity of Purchases Index posting above the neutral 50.0 threshold for the eighth month in a row. However, the rate of expansion eased sharply since January, with the index falling almost six points from one month earlier. Anecdotal evidence suggested that the moderation reflected a marked slowdown in new business growth.

Stocks of Purchases Index

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



Stocks of semi-manufactured goods and raw materials in the Chinese manufacturing sector decreased for a second successive month during February. However, the rate at which stocks were depleted was only modest, and accelerated from one month earlier. Almost 16% of panellists reported a reduction in inventories since January, compared to around 10% that signalled an increase. Respondents signalled that the latest drop in pre-production inventories reflected relatively subdued purchasing growth.

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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