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## HSBC China Services PMI™

Chinese service sector activity rose solidly in June, but confidence in the one-year business outlook dipped to record low.

### Key findings:

- Business activity increased at below-par rate.
- Job creation quickened to the fastest in 2011 to date.
- Business confidence the lowest in the series history.

Chinese service providers signalled a further increase in business activity during June, as new order growth quickened to an eight-month high. Subsequently, the number of people employed within the service sector increased further during the latest survey period. This occurred despite a drop in business confidence to a series-record low. Meanwhile, average input prices rose sharply in June, but competitive pressures restricted the ability of firms to pass on the full extent of cost rises to clients, with data signalling only a modest rate of output charge inflation.

The headline seasonally adjusted Business Activity Index – which is based on a single question asking respondents to report on the actual change in business activity at their companies compared to one month ago – posted 54.1 in June, down slightly from 54.3 in the previous month. Although this signalled a solid increase in activity during the latest survey period, the index reading was down on the long-run series average of 57.2.

Activity growth was supported by a continued rise in new business during June. The rate of new order growth was solid, and the sharpest since last October, but yet again slower than the long-run trend. Companies that reported an increase in new order volumes mostly linked this to firmer underlying demand from clients. Some survey participants also mentioned the success of promotional activities.

Outstanding business fell for the fourteenth successive month during June. Although only modest, the rate of backlog depletion

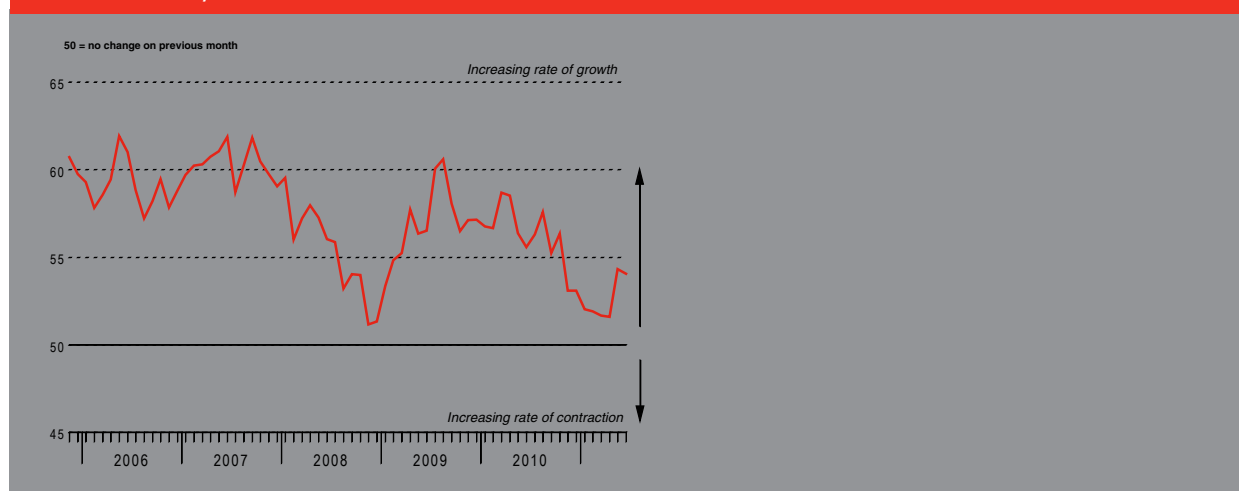
was the fastest since October 2010. According to survey respondents, falling work-in-hand in part reflected below-par new business growth. There were also reports of increased staff numbers.

Employment levels in the Chinese service sector rose again during June, extending the current period of growth to twenty-nine months. The rate of job creation was solid, and the fastest in 2011 to date. Anecdotal evidence suggested that employment growth reflected new order wins and, in some cases, business expansion plans.

The rate of input cost inflation was steep, and accelerated to the fastest since last November. The latest increase extends the current period of inflation to twenty months. Higher salary costs were cited by panellists as the main driver of inflation. A number of respondents also mentioned increased raw material prices. Despite this, output charges rose only modestly in June, as competitive pressures restricted the ability of firms to raise their average tariffs.

Firms commented that they remain optimistic regarding future activity levels in June. Expectations of further new business wins, new product launches and confidence in the economic outlook were all cited as factors supporting sentiment. However, the degree of optimism was the lowest since data were first compiled in November 2005. Firms operating in the Renting & Business Activities sector reported that policies aimed at cooling the property sector had dampened confidence in June.

### Business Activity Index

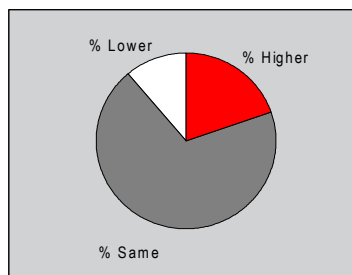
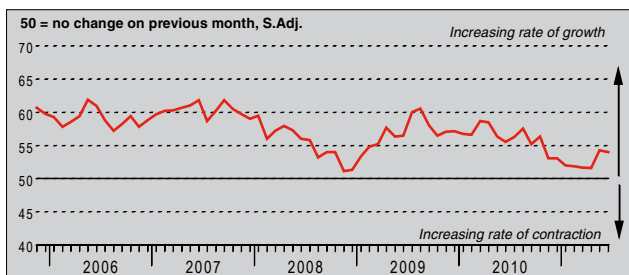


The survey uses a methodology identical to the HSBC China Manufacturing PMI™. The survey uses a panel of regularly participating companies to monitor trends in business conditions in the private sector services economy. The panel has been carefully selected to accurately replicate the true structure of the Chinese services economy.

Questionnaires are dispatched at mid-month, requesting comparisons of the current situation with that of one month previously. *Purchasing Managers' Index™* and *PMI™* are trade marks of Markit Economics Limited, HSBC use the above marks under licence. Markit and the Markit logo are registered trade marks of Markit Group Limited.

### Business Activity Index

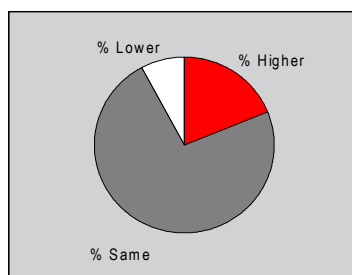
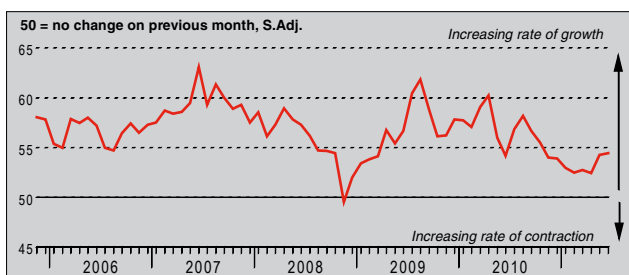
Q. Please compare the level of business activity (i.e. gross income, chargeable hours worked, etc) in your company this month with the situation one month ago.



Chinese service providers reported a further increase in business activity during June. Where a rise in services output was recorded, panellists generally attributed this to new business wins. Although at a level indicative of a solid pace of expansion, the seasonally adjusted Business Activity Index was below the long-run series average. Companies operating in the Renting & Business Activities sector mentioned that state-led policies aimed at cooling the property sector had restricted the overall pace of activity growth in the latest survey period.

### New Business Index

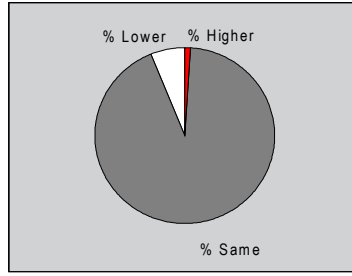
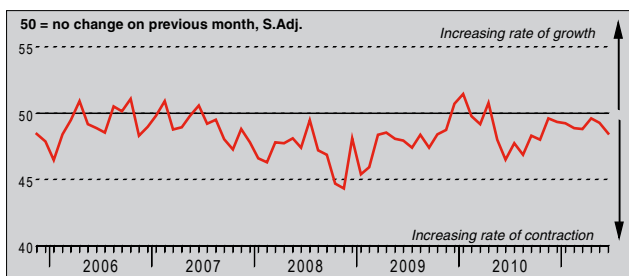
Q. Please compare the level of new orders/business placed at your company (whether already fulfilled or not) this month with the situation one month ago.



The seasonally adjusted New Business Index signalled a solid increase in new orders received by Chinese service providers during June. Despite quickening to the fastest in eight months, the rate of new business growth was slower than the long-run trend. Companies that reported an increase in new order volumes mostly linked this to firmer underlying demand from clients. Some survey participants also mentioned the success of promotional activities.

### Outstanding Business Index

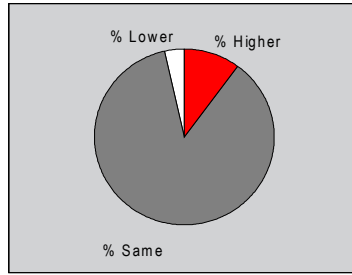
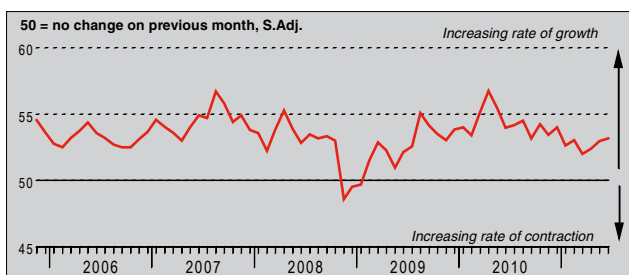
Q. Compare the level of outstanding business (i.e. work in hand but not yet completed) in your company this month with the situation one month ago.



After adjusting for seasonal variation, the Outstanding Business Index pointed to a further fall in backlogs of work held by Chinese service providers during June, extending the current period of expansion to fourteen months. Although only modest, the rate of backlog depletion quickened to the fastest since October 2010. Anecdotal evidence provided by survey respondents suggested that falling work-in-hand was primarily the result of below-par new business growth. There were also reports of higher employment helping to clear backlogs.

### Employment Index

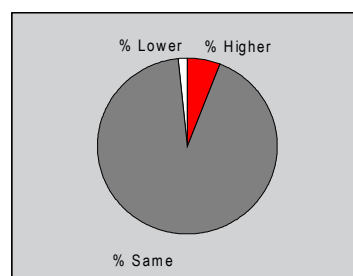
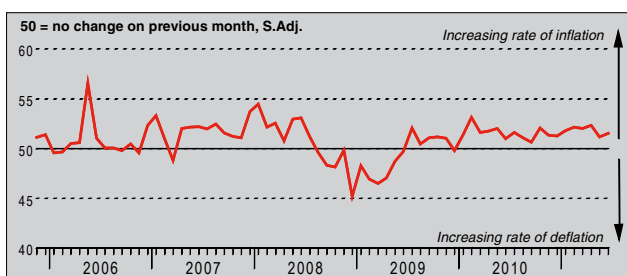
Q. Compare the number of people employed this month with the situation a month ago (treat two part as one full-time and ignore temporary labour).



Workforce numbers across the service economy increased for the twenty-ninth consecutive month in June, with around 10% of companies reporting a rise from one month ago. This compared to almost 4% that indicated a decline. The resulting pace of job creation was solid, and the sharpest in 2011 so far. A number of service providers linked the rise in employment levels to greater inflows of new business. Some panellists also mentioned business expansion plans.

## Prices Charged Index

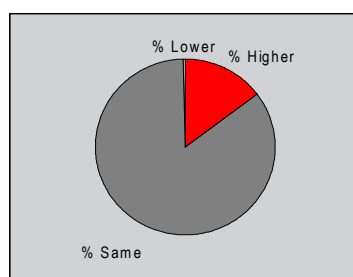
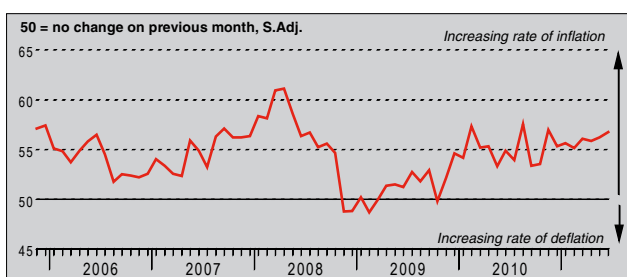
Q. Compare the average prices charged by your company (e.g. prices charged per item or unit of time) this month with the situation one month ago.



June data pointed to an increase in output prices set by Chinese service providers for the eighteenth consecutive month. However, the seasonally adjusted Prices Charged Index was at a level indicative of only a modest rate of inflation. Where an increase in tariffs was recorded (almost 6% of firms), this was attributed to the need to offset higher input prices. Those panellists that reported a decline in average tariffs (around 2%) generally cited competitive pressures.

## Input Prices Index

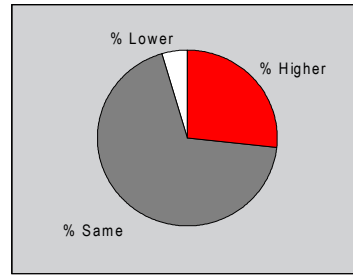
Q. Please compare the average prices paid by your company for all purchases, wages and salaries, etc. this month with the situation one month ago.



Average input costs faced by Chinese service providers continued to increase during June, with the seasonally adjusted Input Prices Index posting above the neutral 50.0 threshold for the twentieth month in succession. The pace of inflation was steep, and accelerated to the fastest since November 2010. Of the 15% of survey respondents that reported an increase in input prices from one month ago, the vast majority commented on higher salary costs. There were also some reports that higher raw material prices had pushed up overall input costs.

## Business Expectations Index

Q. In twelve months' time, do you expect overall activity at your business unit to be higher, the same or lower than now?



Service providers were optimistic about the twelve-month outlook for activity at their units. Panellists linked positive sentiment to expectations that new order growth will gather momentum in the year ahead. New product developments and buoyant economic prospects were also mentioned by respondents. Nonetheless, the degree of optimism was the lowest since data were first compiled in November 2005. Firms operating in the Renting & Business Activities sector cited policies aimed at cooling the property sector as having dampened business confidence in June.

## Notes on the Data and Method of Presentation

The China Services *PMI*<sup>TM</sup> covers transport & communication, financial intermediation, business services, personal services, computing & IT and hotels & restaurants.

Each response received is weighted each month according to the size of the company to which the questionnaire refers and the contribution to total service sector output accounted for by the sub-sector to which that company belongs. This therefore ensures that replies from larger companies have a greater impact on the final index numbers than replies from small companies.

The results are presented by question asked, showing the percentage of respondents reporting an improvement, deterioration or no change on the previous month. From these percentages an index is derived such that a level of 50.0 signals no change on the previous month. Above 50.0 signals an increase (or improvement), below 50.0 a decrease (or deterioration). The greater the divergence from 50.0, the greater the rate of change signalled.

The indexes are calculated by assigning weights to the percentages: the percentage of respondents reporting an "improvement/increase" are given a weight of 1.0, the percentage reporting "no change" are given a weight of 0.5 and the percentage reporting a "deterioration/decrease" are given a weight of 0.0. Thus, if 100% of the survey panel report an "increase", the index would read 100. If 100% reported "no change" the index would read 50 (100 x 0.5), and so on. 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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