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HSBC China Manufacturing PMI™

Manufacturing PMI™ signals seventh successive month of deteriorating operating conditions

Key findings:

- New order and output indices post sub-50 readings
- Employment down at fastest rate in 38 months
- · Input prices fall for first time since January

Maydatasignalled a furthermodest deterioration in manufacturing sector operating conditions, largely reflective of a seventh successive month-on-month decline in overall new business. Job shedding persisted as a result, with the latest reduction in staff numbers the sharpest in more than three years. A renewed fall in purchasing activity was signalled by May's survey, which in turn contributed to an improvement in vendor performance for the first time since July 2009. Meanwhile, average input costs fell at a solid rate, and selling prices decreased for the sixth time in the past seven months.

After adjusting for seasonal factors, the HSBC *Purchasing Managers' Index*TM (PMI^{TM}) – a composite indicator designed to give a single-figure snapshot of operating conditions in the manufacturing economy – registered 48.4 in May, down slightly from 49.3 in April, signalling a seventh successive month-onmonth worsening of Chinese manufacturing sector operating conditions. Despite accelerating since April, the rate of deterioration was only modest.

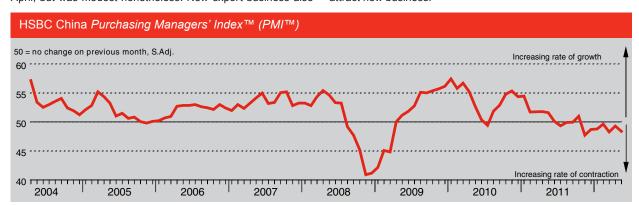
Manufacturing production decreased further in May, although the pace of decline was marginal. Moreover, the latest decrease in factory output was the weakest in the current three-month period of contraction. Where a decline in production was signalled, companies commented on falling new business.

The rate of decline in overall new orders accelerated since April, but was modest nonetheless. New export business also decreased, following a rise in the preceding month. Companies cited muted global demand conditions as the main reason behind the overall decrease in export sales.

Reduced intakes of new business contributed to another month of job shedding, with the rate of decline the sharpest in 38 months. Companies have now reduced their staff numbers in each of the past three months.

May data highlighted a renewed reduction in purchasing activity, albeit at a marginal rate. Holdings of pre-production goods decreased as a result, with the pace of stock depletion the fastest in three months. Meanwhile, muted demand for raw materials among goods producers meant that suppliers were able to shorten their lead times on average. Indeed, the overall improvement in vendor performance was the first in nearly three years.

Purchasing costs faced by manufacturing firms fell in May, ending a three-month period of marginal inflation. The pace of decline in input prices was solid, but slower than rates seen at the turn of the year. Companies reported lower prices paid for raw material and fuel. As a result of lower average costs, goods producers opted to reduce their factory gate charges on average. Output price discounting has now been recorded in six of the past seven months. Some respondents also mentioned lowering average tariffs in a bid to retain existing clients and attract new business.



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. 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.

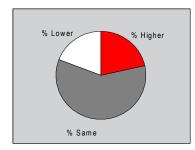




Output Index

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



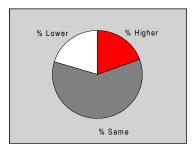


After adjusting for seasonal factors, the Output Index posted below the neutral level of 50.0 in May, signalling a third successive month-on-month decline in Chinese manufacturing production. The rate of contraction was only marginal, however, and the weakest in that period. Anecdotal evidence provided by survey respondents linked reduced factory output to falling new business. There were also reports of a general deterioration in economic conditions.

New Orders Index

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



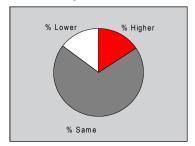


Demand for manufactured goods produced in China continued to deteriorate, with incoming new orders placed at companies falling for the seventh successive month in May. The pace of reduction in total new business accelerated from one month earlier, but was nevertheless only modest. Of the 20% of survey participants that reported a decrease in new order levels, many linked this to stagnant demand on both domestic and global markets.

New Export Orders Index

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



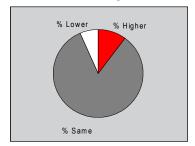


May data pointed to a renewed decline in the level of new export business placed at Chinese manufacturing firms. However, the latest seasonally adjusted New Export Orders Index was consistent with only a modest pace of reduction. Companies cited muted global demand conditions as the main reason behind the overall decrease in export sales. Indeed, panel responses indicated that demand weakness was broad-based across all of China's major trading partners.

Backlogs of Work Index

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



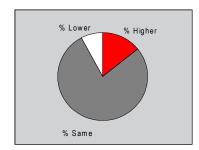


Despite a further decrease in new order inflows, backlogs of work in the China's goods producing sector increased further during May. The latest increase in outstanding business was the third in as many months. However, the rate of backlog accumulation was only modest, with the vast majority of panellists (around 83%) recording no change in volumes of work-in-hand (but not yet completed) since the preceding month.

Stocks of Finished Goods Index

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



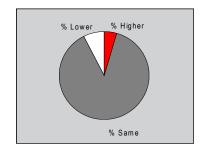


Holdings of post-production goods in the Chinese manufacturing sector increased in May, ending a two-month period of contraction. Despite posting the second-highest reading in almost two years, the seasonally adjusted Stocks of Finished Goods Index pointed to only a marginal rate of inventory accumulation. Higher stock levels largely reflected weaker-than-expected sales, according to respondents to the latest survey.

Employment Index

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

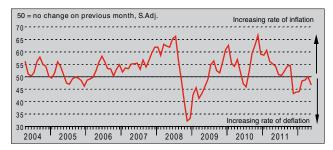


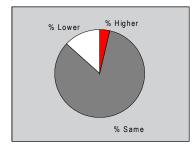


After accounting for seasonal trends, the Employment Index signalled another month of job shedding in China's manufacturing sector. May's index reading pointed to a moderate rate of decline in headcounts that was the fastest in 38 months. Almost 8% of panellists signalled a reduction in workforce numbers since April, compared to 5% that noted a rise. Where a reduction in staffing levels was signalled, companies often linked this to reduced intakes of new business.

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.





Output prices set by Chinese manufacturing firms decreased in May, following no change in April. Around 13% of panellists signalled a reduction in selling prices since the preceding month, compared to just 4% that noted a rise. The rate of output charge discounting was solid, and the sharpest in four months. Where a reduction in factory gate charges was recorded, survey respondents often linked this to the passing on of lower input costs to clients. There were also reports of competitive pressures.

Input Prices Index

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



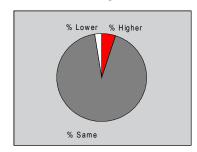


Average input costs faced by Chinese manufacturing firms fell for the first time in four months during May. Almost 14% of companies signalled a decline in average costs since April, compared to 7% that noted a rise. The pace of decrease in input prices was solid, but slower than rates observed around the turn of the year. Companies reported that lower prices paid for raw materials had contributed to the overall reduction in average costs.

Suppliers' Delivery Times Index

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



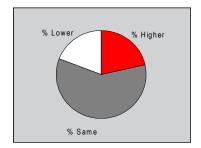


May data indicated that the average time taken by suppliers to deliver inputs to Chinese manufacturing firms shortened for the first time in nearly three years. The rate of improvement in vendor performance was only modest, however, with the majority of panellists (almost 93%) reporting no change since the preceding month. Anecdotal evidence provided by survey respondents suggested that shorter lead times reflected sufficient availability of inputs at vendors.

Quantity of Purchases Index

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

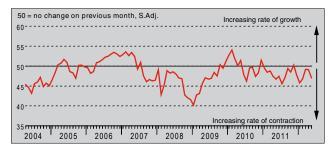


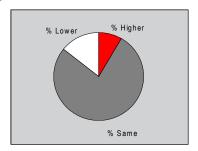


The latest survey findings showed a renewed reduction in the amount of inputs purchased by manufacturing firms in May. Of those companies that noted a decline in input buying since April (around 19%), a number commented on lower output requirements. The latest seasonally adjusted Quantity of Purchases Index reading was nonetheless consistent with only a marginal rate of reduction. The index has now posted below the neutral 50.0 threshold, signalling contraction, in six of the past seven months.

Stocks of Purchases Index

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





Manufacturers in China reported a sixth successive month-on-month decrease in stocks of purchases at their plants. Around 14% of survey participants mentioned a reduction in inventory holdings since the preceding month, compared to 8% that noted an increase. The rate of stock depletion was solid, and the sharpest in three months. Where a decline in pre-production inventories was recorded, panellists commonly linked this to reduced purchasing activity.

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 industry contribution to Chinese GDP. 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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