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HSBC China Services PMI™

Chinese service sector activity rises at sharpest rate in 19 months

Key findings:

- · Marked expansion of service sector output recorded
- Jobs growth unchanged at modest rate
- · Business optimism remains strong

Chinese service providers reported the strongest month-on-month expansion of business activity in 19 months, largely reflective of greater new business wins. Looking ahead, companies continued to express a strong level of confidence regarding the one-year business outlook, albeit to a weaker degree than the long-run trend. On the employment front, service providers added to their staff numbers in May, with jobs growth unchanged at a modest rate. Meanwhile, output charges were reduced for a second successive month, in spite of a marked increase in average costs.

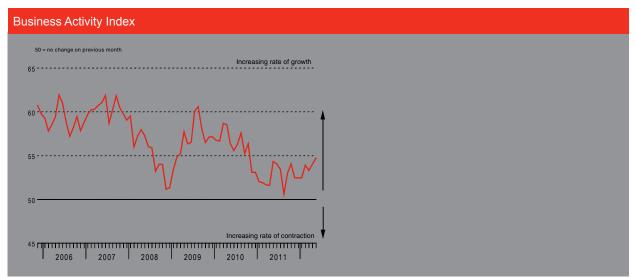
After adjusting for seasonal factors, the Business Activity Index rose from 54.1 to a 19-month high of 54.7 in May, signalling a marked expansion of Chinese service sector activity. New business wins were often cited by panellists as the main factor behind the latest increase. Indeed, the pace of new order growth was marked, and the fastest since October 2010. Companies commented on new product developments and better market demand. A number of survey participants also mentioned the success of promotional activities.

Despite the increase in new orders, backlogs of work in the Chinese service sector continued to fall during May. The latest decrease in volumes of work-in-hand (but not yet completed) was the fourth in as many months. However, the rate of backlog depletion remained marginal overall.

Companies reported another month of employment growth in May, although the rate of job creation was only modest. Moreover, the latest increase in staff numbers was weaker than the long-run trend average for the survey. Where a rise in employment was recorded, panellists attributed this to greater inflows of new work and business expansion plans.

May data signalled a marked rise in average costs faced by Chinese service providers, extending the current period of inflation to 31 months. Anecdotal evidence provided by survey respondents suggested that input price inflation largely reflected higher labour-related costs. Despite of the rise in input costs, companies reduced their average tariffs during the month. The latest decrease in selling prices was the second in as many months. However, the rate of output charge discounting remained only marginal. Where a reduction in average tariffs was reported, survey participants attributed this to competitive pressures and the need to retain existing clients.

Service providers were again optimistic regarding the one-year business outlook in May. The degree of confidence was strong, with the index measuring business expectations only slightly lower than April's one year-high. Companies linked positive sentiment to expectations of new business wins and better economic conditions. Companies also expect business expansion plans to supported growth in the coming year.



The survey uses a methodology identical to the HSBC China Manufacturing PMI^{TM} . 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. $Purchasing Managers' Index^{TM}$ 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.

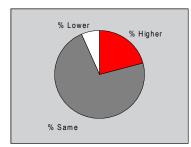




Business Activity Index

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.



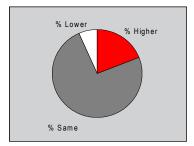


Chinese service providers recorded another increase in business activity during May, with approximately 21% of survey participants signalling a rise from one month earlier. This compared to 7% that registered a decrease. The rate of expansion in services output was marked, and the sharpest in 19 months. However, the latest seasonally adjusted Business Activity Index reading was below the long-run trend for the series (56.7). Anecdotal evidence provided by survey respondents suggested that activity growth reflected greater inflows of new business.

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.



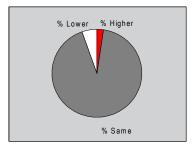


The volume of incoming new business placed at Chinese service providers increased again in May, extending the current period of expansion to 42 months. The seasonally adjusted New Business Index was at a level indicative of a marked pace of new order growth. Moreover, the latest index reading was the highest since October 2010. Service providers commented on new product developments, firmer client demand and 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.



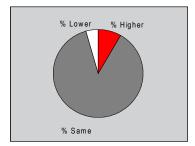


In line with the trend observed since February, the volume of work-in-hand (but not yet completed) in the Chinese service sector decreased during May. This occurred despite a marked increase in new order intakes. The latest seasonally adjusted Outstanding Business Index reading was nonetheless consistent with only a marginal rate of decline in unfinished work. The vast majority of panellists (around 92%) reported no difference in backlogs of work compared to one month earlier.

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).



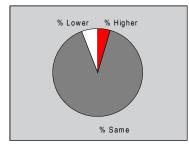


After adjusting for seasonal factors, the Employment Index posted above the neutral 50.0 threshold in May, signalling a fortieth successive month of jobs growth in the sector. The rate at which companies added to their staff numbers was only modest, however, and weaker than the long-run series average. Of those survey participants that mentioned a rise in headcounts (around 8%), many attributed growth to new business wins. Some companies also cited 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



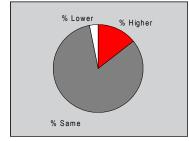


By posting a sub-50 reading, the seasonally adjusted Prices Charged Index signalled a continued decline in output prices set by Chinese service providers. May's index reading was the lowest in five months, but consistent with only a marginal rate of output charge discounting. Service providers that mentioned a decrease in average tariffs often linked this to competitive pressures and the need to retain existing clients. A number of firms in the Financial Intermediation sector also commented on state regulation.

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.

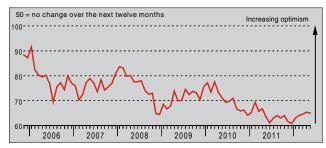




After adjusting for seasonal factors, the Input Prices Index pointed to another month of input cost inflation in the Chinese service sector. Despite dipping from April's 20-month high, the latest index reading nonetheless signalled a marked increase in average costs. Around 14% of survey participants reported a rise in input prices from one month earlier, compared to just 3% that noted a decline. Higher labour-related costs were cited by panellists as the main driver of inflation in the latest survey period.

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?





Chinese service providers expressed optimism regarding the near-term business outlook, with almost one-third of survey respondents expecting activity levels to be higher in 12 months' time. Despite remaining below the long-run trend for the series, the Business Expectations Index signalled a strong degree of optimism. Anecdotal evidence suggested that business confidence reflected expectations of new business wins and better economic conditions.

Notes on the Data and Method of Presentation

The China Services PMITM 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 an '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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