ABN·AMRO

Short Insight

Group Economics
Emerging Markets &
Commodity Research

01 April 2019

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China: Encouraging signs

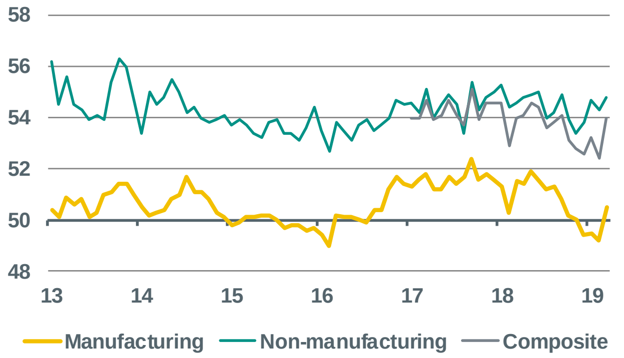
- **Clear improvement in China's official PMIs, …**
- **… as well as in Caixin's manufacturing PMI**
- **Export and import subindices suggest Chinese foreign trade is bottoming out**
- **Trade deal in sight, although strategic 'tech' competition will likely linger on**

1. Clear improvement in China's official PMIs, …

Over the past months, we have regularly pointed at several green shoots for the Chinese economy, such as the pick-up of state-led investment and overall credit growth following the policy shift from targeted tightening/ financial deleveraging to targeted, piecemeal fiscal and monetary easing. The Purchasing Managers' Indices published over the past few days provide further signs of stabilisation. The 'official' PMIs for March published last Sunday – which have a strong focus on the larger and state-owned companies – showed a clear uptick. The NBS manufacturing, services and composite PMIs all rose to the highest levels since September 2018. The manufacturing PMI jumped by 1.3 point to 50.5, outbeating expectations (consensus: 49.6) and coming in above the neutral 50 mark again for the first time since October 2018. The NBS Services PMI rose to 54.8 (February: 54.3, consensus forecast: 54.4) and the NBS Composite PMI gained 1.6 point, rising to 54.0. We note that the strong improvement in March likely partly reflects the resumption of activity after the long Lunar New Year holiday break in February.

Official PMIs show clear improvement in March

China, official PMIs (NBS), indices, 50 = neutral mark



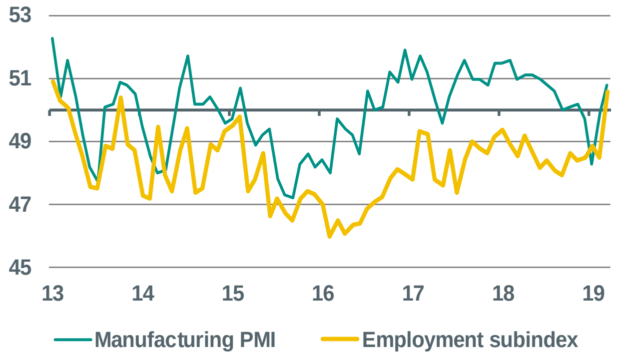
Source: Thomson Reuters Datastream

2. … as well as in Caixin's manufacturing PMI

Today, Caixin's manufacturing PMI for March was published; services/composite PMIs are due on Wednesday. Caixin's survey focuses more on smaller and export-oriented firms. Caixin's manufacturing PMI showed a further improvement of almost a full point, coming in at 50.8 (February: 49.9) and beating expectations as well (consensus: 50.0). This followed an already sharp uptick in February of 1.6 points, compared to the three-year trough (48.3) reached last January. The improvements in this index was quite broad-based. The new order component rose to a four month high, while the exports component returned to above the neutral 50 mark. Remarkably, the employment sub-index surged to a six-year high. This takes away some of the concerns about the Chinese labour market, after the unemployment rate in urban areas had reached a one-year high in February.

Caixin's manufacturing PMI improves further in March

China, Caixin manufacturing PMI, index, 50 = neutral mark

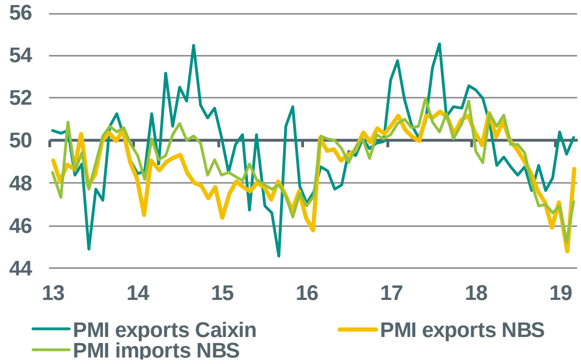


Source: Thomson Reuters Datastream

3. Export, import subindices suggest Chinese trade is bottoming out
China's export and import growth has remained solid in the first ten months of 2018 despite the trade conflict, but weakened materially over the past months driven by exports. Payback from previous frontloading plays a role here as well, and so does the drop in commodity prices. That said, we think export and import growth is bottoming out, although we expect annual growth to remain below the strong levels seen in 2017 and 2018. The PMI export and import subindices also suggest that the worst may be behind us in this respect. While the export and import components of China's official PMIs are still below 50, we saw a sharp improvement in March. The export subindex rose by almost two points to 47.1, while the PMI import index jumped by almost four points to 48.7. Meanwhile, the export subindex of Caixin's manufacturing PMI has also improved over the past few months, and came in above the neutral 50 mark again in March (50.2). In our view, the improvement in the export and import components of the various PMIs partly reflect an improvement of perceptions about the potential outcomes of the ongoing negotiations between the US and China (see below).

Exports/imports solid in October, despite trade conflict

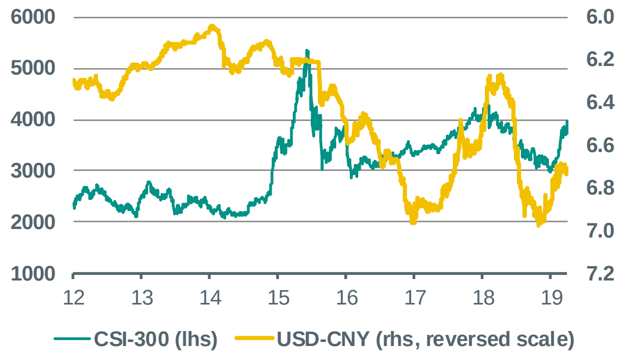
PMI export/import subindices, 50 = neutral mark



Source: Thomson Reuters Datastream

4. Trade deal in sight, although tech competition will likely linger on
Meanwhile, we have become a bit more optimistic about the prospects of a short-term US-China trade deal, following a truce between presidents Trump and Xi agreed last December. High-level negotiations between the US and China have resumed last week, although another meeting between the two presidents has not been scheduled yet. What would be crucial for in our view is a kind of a short-term arrangement that would make a further rise of import tariffs unlikely. Such a deal would take away a key headwind for the Chinese and global economy and will be preferable for the macro outlook and financial markets. After underperforming last year, China's stock markets have already reacted positively to improved prospects for a trade deal following the Trump-Xi deal, while the Chinese yuan has also appreciated a bit versus USD since late 2018. That said, strategic competition between the US and China will probably linger on for years, while the Huawei case shows that the trade war has shifted to a tech war. Hawks in the US administration will likely continue to push of restrictions on strategic exports to China and on FDI from China. The EU has also sharpened its stance versus China recently (also see my colleague Sandra Phlippen's comments in her recent *Macro Weekly*).

Sentiment on China's financial markets has improved



Source: Bloomberg

Key forecasts for the economy of China

	2016	2017	2018e	2019e	2020e
GDP (% yoy)	6.7	6.8	6.6	6.3	6.0
CPI inflation (% yoy)	2.1	1.5	1.9	2.5	2.5
Budget balance (% GDP)	-3.8	-3.8	-4.0	-4.5	-4.5
Government debt (% GDP)	16	17	19	22	25
Current account (% GDP)	1.8	1.4	0.3	0.0	0.0
Gross fixed investment (% GDP)	42.7	42.9	43.9	43.1	42.1
Gross national savings (% GDP)	45.9	46.0	44.6	43.5	42.4
USD/CNY (eop)	7.0	6.5	6.9	6.6	6.6
EUR/CNY (eop)	7.3	7.8	7.8	7.7	8.3

Economic growth, budget balance, current account balance for 2019 and 2020 are rounded figures
Source: EIU, ABN AMRO Group Economics