

China Macro Flash

May Data Preview: Real Activity May Have Improved Moderately

- **Abundant credit appears to have sustained growth momentum** – Official PMI improved by 0.2ppt to 50.8 in May, a strong reading considering that the index dropped by 2.7ppts on average in May during 2005-12. Non-manufacturing PMI declined by 0.2ppt to 54.3, and remained in the 54-56 range most of the time in the past year. Overall economic growth may have remained steady thanks to accommodative monetary and credit policies. We maintain our GDP growth forecast of 7.8%YoY for 2Q, and see a low probability of an interest rate cut in the near term.
- **CPI inflation likely edged up to 2.6%YoY, and PPI deflation intensified slightly** – Vegetable prices fell sharply during the month. We estimate that overall price level may have declined by 0.1%MoM. However, the base effect contributed 0.3ppt to the YoY inflation. As a result, YoY CPI inflation may have risen from 2.4% in Apr to 2.6% in May. The base effect would contribute 0.5ppt to the YoY inflation in Jun, likely to bring inflation to close to 3%. Interim data on producer good prices and PMI input price index suggest PPI may have dropped by 0.3%MoM, and YoY deflation likely intensified from -2.6% in Apr to -2.7% in May.
- **Real activity may have improved moderately** – The PMI production index rose 0.7ppt to 53.3, indicating acceleration of industrial production. Interim data also show an increase in daily electricity production in May. We estimate that IP growth may have picked up from 9.3%YoY in Apr to 9.7% in May. Supported by abundant credit, the growth momentum for investment in infrastructure and property may have continued into May, and FAI growth may have increased slightly to 20.7%. Retail sales may have been bolstered by increased home sales and purchases ahead of the expiry of government subsidies on energy saving electronic goods. The nominal retail sales likely accelerated from 12.8% in Apr to 13.0%YoY in May.
- **Trade growth may have decelerated** – As the government started to take measures to address export over-invoicing and FX borrowing for faked imports, trade data in May are likely to reflect the reality better. The PMI new export order index stayed below 50 while the import index rose above 50, reflecting relatively strong investment momentum. We estimate that export and import growth decelerated to 8.9% and 12.1%YoY in May, with a trade surplus of \$15.1bn.
- **M2 growth likely fell to 15.4%, and new RMB lending increased to 808bn** – While benign inflation, weak recovery and policy easing in other countries make it possible for China to maintain accommodative monetary and credit policies for longer, we expect the PBOC to gradually bring money growth to a level closer to the annual target of 13%. During the month, liquidity injections through open market operations and FX purchases may have been mostly offset by an increase in government deposits, causing a slowdown of money growth. We expect credit extension to be broadly in line with an implicit annual loan quota of Rmb9.0tn.

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Real Activity May Have Improved Moderately

Figure 1. Economic Data Release for May 2013

	Date	For	Citi Fcst	Mkt Fcst	Prev
Trade Balance (\$bn)	8-Jun	May	15.1	18.65	18.16
Exports (YoY%)			8.9	7.0	14.7
Imports (YoY%)			12.1	5.9	16.8
CPI (% YoY)	9-Jun	May	2.6	2.5	2.4
PPI (% YoY)			-2.7	-2.5	-2.6
IP (% YoY)			9.7	9.2	9.3
Retail Sales (% YoY)			13.0	12.9	12.8
FAI - urban (% YoY ytd)			20.7	20.5	20.6
M0 Supply (%YoY)	10~15-Jun	May	11.3	-	10.8
M1 Supply (%YoY)			12.1	11.9	11.9
M2 Supply (%YoY)			15.4	15.9	16.1
New Yuan Loans (RMB bn)			808.0	850.0	792.9

Source: Bloomberg and Citi Research

Jun 9,

CPI

Headline: 2.6%YoY

Food: 4.0%YoY

Nonfood: 1.9%YoY

CPI inflation likely edged up to 2.6%YoY, due to base effects – Based on data made available during the month as well as the seasonal pattern of price fluctuations, we estimate that the overall price level may have declined by 0.1%MoM. However, the base effect contributed 0.3ppt to the YoY inflation. As a result, YoY CPI inflation may have risen from 2.4% in Apr to 2.6% in May.

■ **Base effect may have kept YoY food inflation at 4.0%** – Interim data from the Ministry of Commerce (mostly wholesale prices) showed that food prices dropped 1.1% during the month, with meat prices falling nearly 1%MoM and vegetable prices falling 11%MoM. The NBS interim data showed a decline of retail food prices of about 0.6%MoM. According to our estimate, food prices may have dropped by 0.9%MoM. However, the monthly price decline may have been fully offset by the base effect, and YoY food inflation may have remained flat at 4.0%.

■ **Non-food inflation may have risen to 1.9%YoY** – The fuel prices were cut on 25 Apr and raised on 10 May, and the net effect on monthly inflation should be minimal. Seasonally, non-food prices tend to increase in May, but the degree of increase is likely to be restrained by weak economic recovery and excessive capacity. We estimate that non-food prices rose 0.2%MoM and YoY inflation increased from 1.6% to 1.9%.

■ **YoY inflation may rise further in Jun due to base effect.** In Jun, prices tend to decline MoM according to the seasonal pattern, but the base effect would contribute 0.5ppt to the YoY inflation, likely to bring inflation to close to 3%.

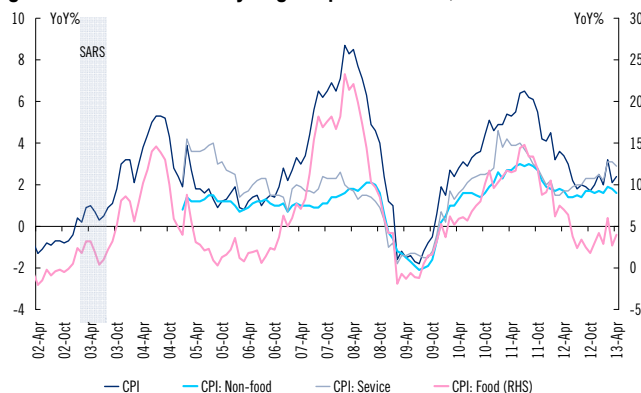
Jun 9,

PPI

Headline: -2.7%YoY

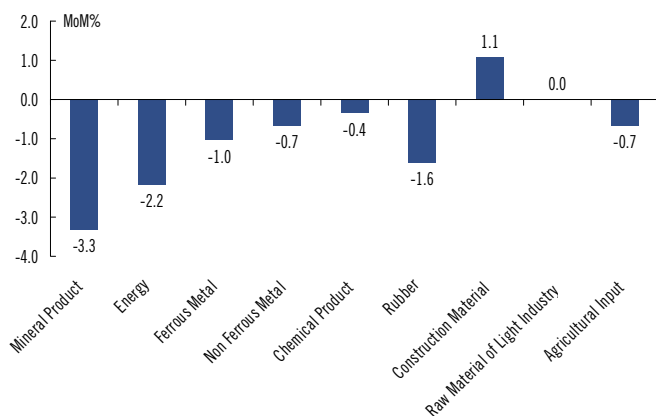
PPI deflation may have intensified slightly to -2.7%YoY – The international commodity prices as measured by the CRB index increased by 0.2% during the month. Interim data from the Ministry of Commerce showed that producer good prices for most raw materials declined during the month (3.3% for mineral products, 2.2% for energy and 1.6% for rubber). The PMI input price index increased by 5ppts to 45.1 in May, indicating continued price declines but at a slower pace. We estimate that overall PPI may have dropped by 0.3%MoM, and YoY deflation likely intensified from -2.6% to -2.7%.

Figure 2. CPI inflation likely edged up to 2.6%YoY, due to base effect



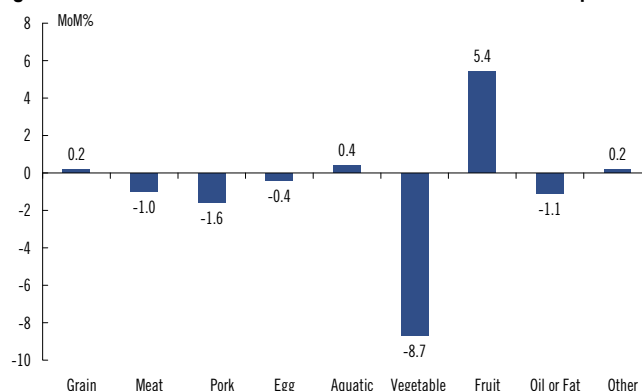
Source: NBS and Citi Research

Figure 4. MOC data indicate continued producer price deflation



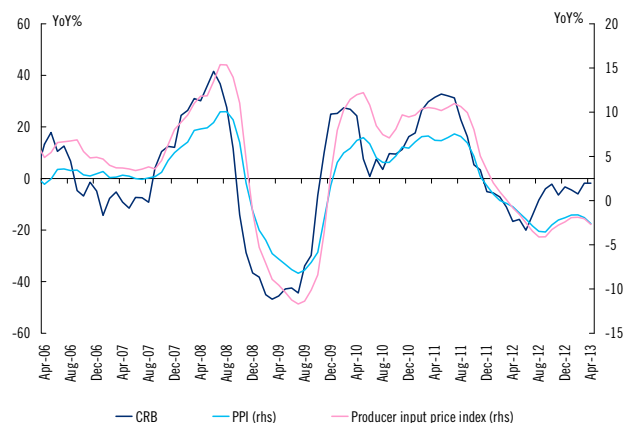
Source: MOC, CEIC and Citi Research

Figure 3. The NBS interim data showed a decline of retail food prices



Source: NBS, Bloomberg and Citi Research

Figure 5. PPI deflation may have intensified slightly to -2.7%YoY



Source: NBS, CEIC and Citi Research

Jun 9,
Industrial Value Added
Headline: 9.7%YoY

Industrial production (IP) growth may have picked up to 9.7%YoY – The official manufacturing PMI improved from 50.6 in Apr to 50.8 in May, and production index rose 0.7ppt to 53.3, indicating acceleration of industrial production. This is a quite strong reading given that PMI consistently dropped in the month of May during 2005-12. However, HSBC manufacturing PMI declined from 50.4 in Apr to 49.2 in May. The divergence of the two sentiment measures can be attributed partially to the decline of PMI for smaller enterprises. Meanwhile, the interim data from the State Electricity Regulatory Commission (SERC) show an increase in daily electricity production in May. We estimate that IP growth may have picked up from 9.3%YoY in Apr to 9.7% in May.

Jun 9,
Urban FAI, YTD
Headline: 20.7%YoY

Fixed-asset investment (FAI) growth may have increased slightly to 20.7% – Year-to-date FAI grew by 20.6%YoY in Apr, bolstered by investment in infrastructure (21.5% YoY) and property development (21.1% YoY). The growth momentum for investment in infrastructure and property may have continued into May, in light of significantly higher land sales reported in some large cities, turnovers in the property market, local government investment zeal, as well as abundant credit supply in the first four months. Taking these factors into consideration, nominal investment growth may have accelerated despite continued input price deflation.

Jun 9,
Retail Sales
Headline: 13.0%YoY

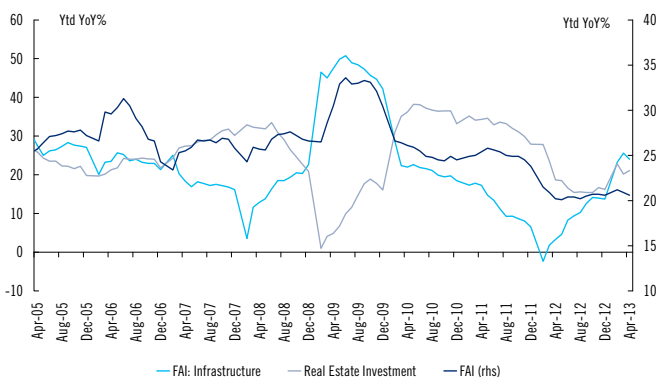
Retail sales growth may have risen moderately to 13.0%YoY – Nominal retail sales growth accelerated from 12.6% in Mar to 12.8%YoY in Apr. Catering sales growth fell further from 8.7%YoY in Mar to 7.9%YoY in Apr and the impact of the government campaign to cut lavish official spending is expected to continue, weighing on retail sales. However, retail sales may have been bolstered by increased home sales (demand for building materials and furniture), the fading effect of bird flu on poultry consumption and increased sales ahead of the expiry of government subsidies on energy saving electronic goods at end-May. We estimate that the nominal retail sales accelerated to 13.0%YoY in May, also benefiting from higher CPI inflation.

Figure 6. IP growth may have picked up to 9.7%YoY



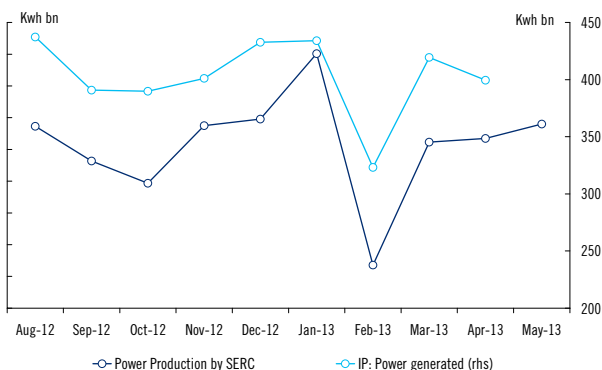
Source: CEIC and Citi Research

Figure 8. The growth momentum for investment in infrastructure and property may have continued into May



Source: CEIC and Citi Research

Figure 7. SERC data show a rise in daily electricity production in May



Source: WIND, CEIC and Citi Research

Figure 9. Retail sales may have been bolstered by increased home sales



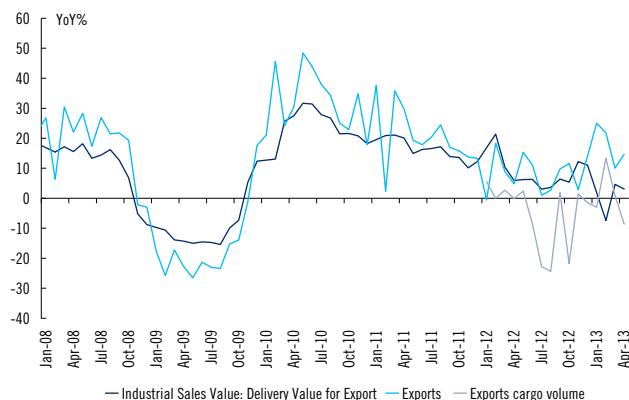
Source: CEIC and Citi Research

Jun 8,
Trade
Balance: \$15.1bn
Exports: 8.9%YoY
Imports: 12.1%YoY

Trade growth may have decelerated as government started to address hot money inflows – Exports and imports grew by 14.7% and 16.8%YoY in Apr. Both may have been inflated, and there is anecdotal evidence that trade channel—such as export over-invoicing and FX borrowing for faked imports—has been used to bring in FX in anticipation of currency appreciation. Data on port throughput, export delivery value of industrial good and import from trading partners suggest single-digit export growth. As government started to take measures to address these issues, trade data in May are likely to reflect the reality better. The official PMI new export order index improved but stayed below 50 in May (49.4), while the import index rose above 50 (50.3), reflecting relatively strong investment momentum. We

estimate that exports and imports growth decelerated to 8.9% and 12.1%YoY in May, with a trade surplus of \$15.1bn.

Figure 10. Export delivery value of industrial good and cargo volume suggest single-digit export growth



Source: WIND, CEIC and Citi Research

Figure 11. Imports may continue to outpace exports



Source: CFLP, NBS and Citi Research

Jun 10-15

Money

M0: 11.3%YoY

M1: 12.1%YoY

M2: 15.4%YoY

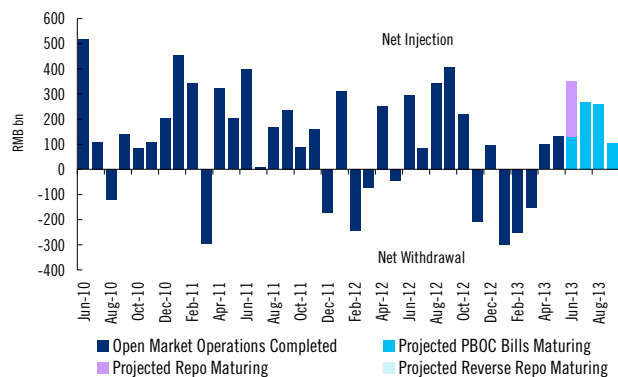
New RMB Loans: 808.0bn

Broad money (M2) growth may have fallen to 15.4% – M2 grew by 16.1% in Apr, way above the annual target of 13%. While benign inflation, weak recovery and policy easing in other countries make it possible for China to maintain accommodative monetary and credit policies for longer, we expect PBOC to gradually bring money growth to a level closer to the annual target. The following factors affected M2 growth in May:

- Government deposits at the PBOC may have increased by Rmb200-300bn, mainly due to payment of tax. This is equivalent to liquidity withdrawal.
- Trade account may have run a surplus in May (about \$15bn by our estimate), and net FDI inflows and other capital inflows may have continued. We assume that PBOC intervened by purchasing FX from the market to slow down the appreciation of RMB, injecting liquidity.
- PBOC injected Rmb130bn into the banking system through open-market operations.
- Taking these factors into consideration, M2 growth may have fallen to 15.4%YoY in May. M1 growth may have improved further to 12.1%YoY, reflecting increased economic activity. M0 growth may have also picked up to 11.3%YoY.

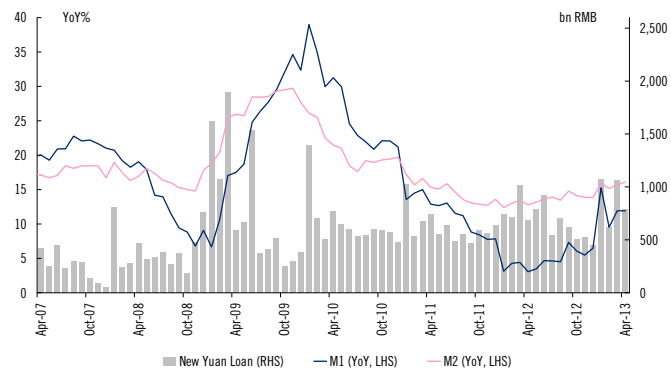
New RMB lending may have increased to Rmb808bn – New RMB lending in the first four months is broadly in line with an implicit annual loan quota of Rmb9.0tn. It is reported that the biggest four banks lend out about Rmb300bn on a net basis during the month. Based on the share of these banks in total lending, as well as the share of 2Q lending in annual lending, we estimate that new RMB lending may have increased from Rmb793bn in Apr to Rmb808bn in May.

Figure 12. PBOC injected liquidity through OMOs in May



Source: PBOC and Citi Research

Figure 13. Accommodative monetary and credit policies may be maintained for longer



Source: PBOC and Citi Research

Appendix A-1

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