

China manufacturing

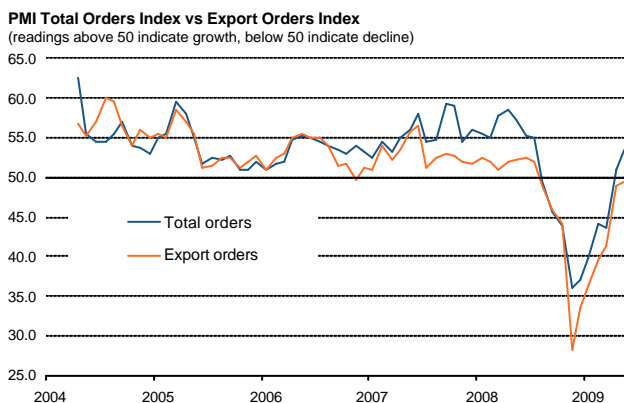
China's manufacturing sector expands amid evidence of 'decoupling'

- **PMI data suggest domestic demand is a key driver of recovery in China.**
- **Similar trends evident in India and Brazil.**

The CLSA China manufacturing PMI, compiled by Markit, signalled an expansion of the country's manufacturing sector for the second month running in May. The improvement was underpinned by a solid rise in new orders, which was achieved despite a further drop in new exports. This suggests that growth was powered mainly by domestic demand, and provides evidence to suggest an element of 'decoupling' between China and the West.

PMI data on Chinese manufacturing suggest that total new orders have generally been more buoyant than export orders since mid-2006, whereas prior to then domestic and export orders had moved in tandem. In the recent downturn, exports suffered to a greater extent than domestic sales and continue to lag total new orders (see chart 1).

Chart 1: China total orders v export orders

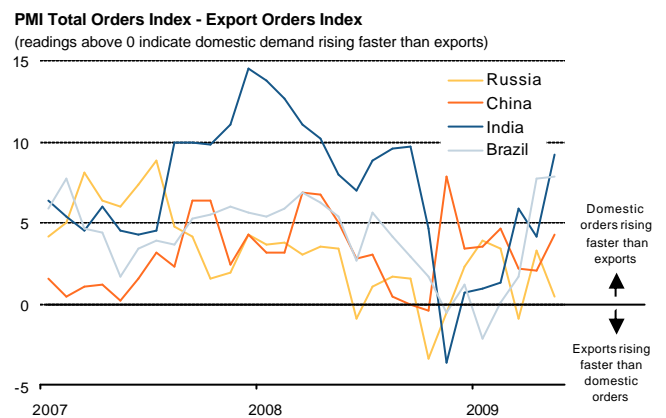


Domestic demand remains key driver across BRIC region

Latest PMI data point to similar trends in the other BRIC economies (see chart 2). In India and Brazil, the outperformance of total orders relative to exports has

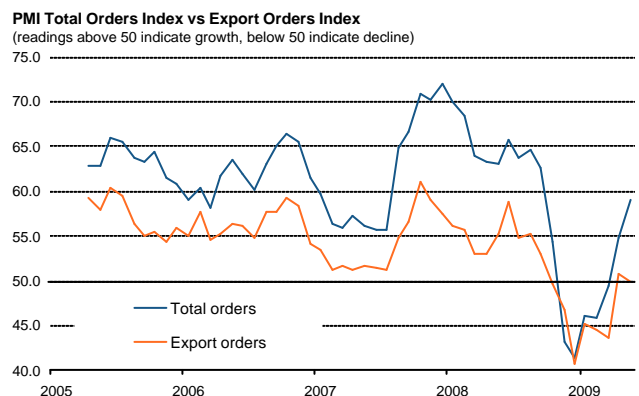
been even more pronounced than in China, although the differential in Russia has narrowed.

Chart 2: BRIC economies total orders less export orders



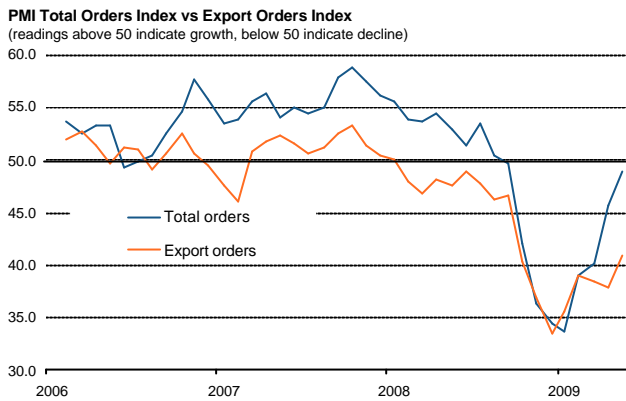
In India (a much less export-oriented economy than China) a gap between the PMI series tracking total orders and exports has been apparent throughout almost the entire four-year survey history (see chart 3). While this is perhaps unsurprising, the extent of the difference underscores the role played by domestic demand in powering the Indian economy's expansion.

Chart 3: India total orders v export orders



A similar picture is evident in Brazil, where the recent rebound in total new orders has yet to be matched by the export component (see chart 4).

Chart 4: Brazil total orders v export orders

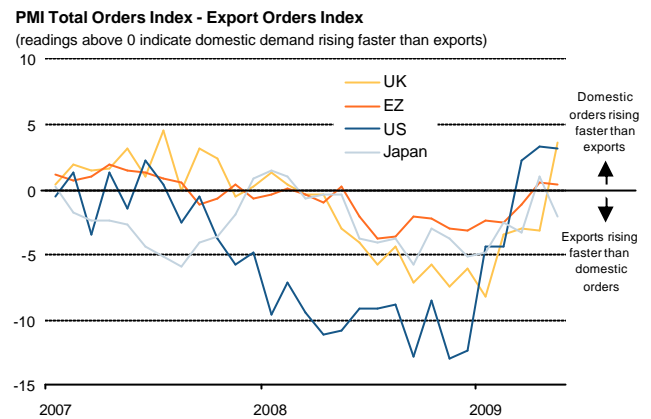


The ability of these large, emerging economies to recover in advance of a sustained rebound in external demand highlights the resilience of underlying growth momentum in their domestic sectors, and that they too have achieved a degree of decoupling.

The decoupling argument still needs to be treated with caution, however, as manufacturing PMI data for the developed economies (chart 5) also imply a strengthening of domestic demand relative to exports in the US and UK (and to a lesser extent in the Eurozone)

in recent months. But the divergence is far less than that observed in India and Brazil. In Japan, on the other hand, the case is perhaps more clear cut, with total new orders deteriorating at a faster pace than the export component, suggesting muted domestic demand.

Chart 5: Developed economies total orders less export orders



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