

ZEW-PwC China Economic Barometer

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ZEW-PwC-China Economic Barometer

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Editorial

The ZEW-PwC China Economic Barometer presents the current situation and expected trends for the Chinese economy over the next 12 months. The barometer is based on a quarterly survey of managers from German companies in China. Along with the economic situation and trends, the German managers in China were asked to assess the performance of macroeconomic indicators, as well as company sales, investment across various sectors and the regulatory environment. The *ZEW-PwC China Economic Barometer* is compiled and published jointly by the Centre for European Economic Research (ZEW) and PwC.

- **Key message 1**

After the US election: Managers expect rise in trade with China.

- **Key message 2**

Outlook on economic growth modest.

- **Key message 3**

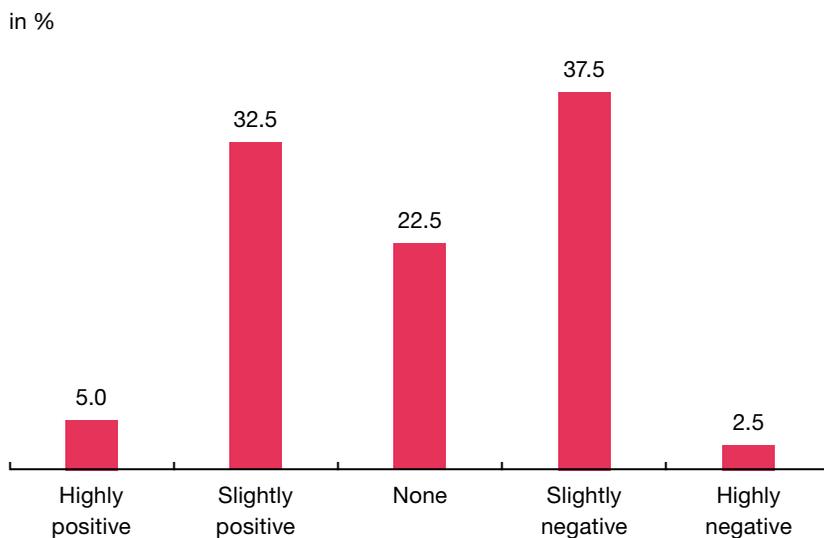
Private domestic demand continues to grow in importance.

After the US election: Managers expect rise in trade with China

Since Donald Trump was elected as President of the United States, there has been an increasing trend towards international protectionism and greater concentration on domestic markets. One example of this is the USA's withdrawal from the Trans-Pacific Partnership (TPP).

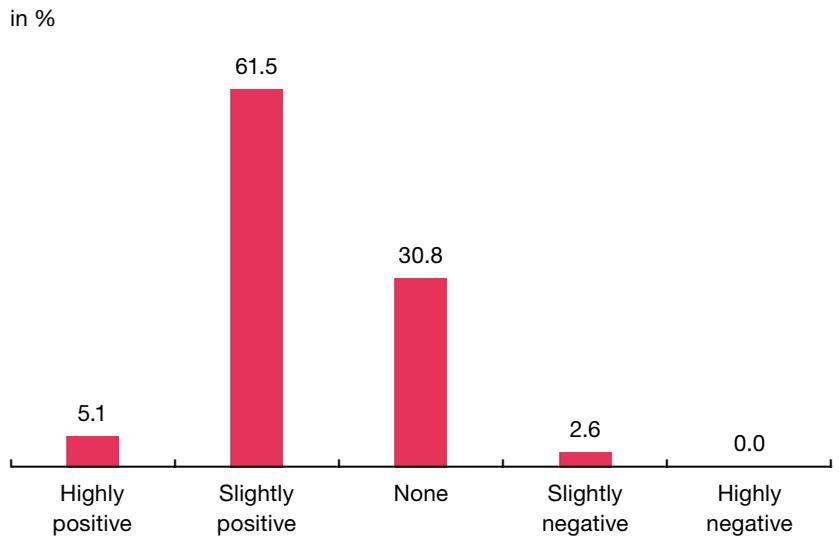
This issue's special focus examines these trends. In a first segment, we asked managers what impact such developments will have on the Chinese economy this year. As Figure 1 shows, the median response was clearly in the "no impact" category. A third of those surveyed (32.5%) leaned towards slightly positive and 37.5% towards slightly negative impacts but overall they almost balance each other out.

Fig. 1 What impact do you see the trend towards greater protectionism and concentration on national markets having on the Chinese economy this year?



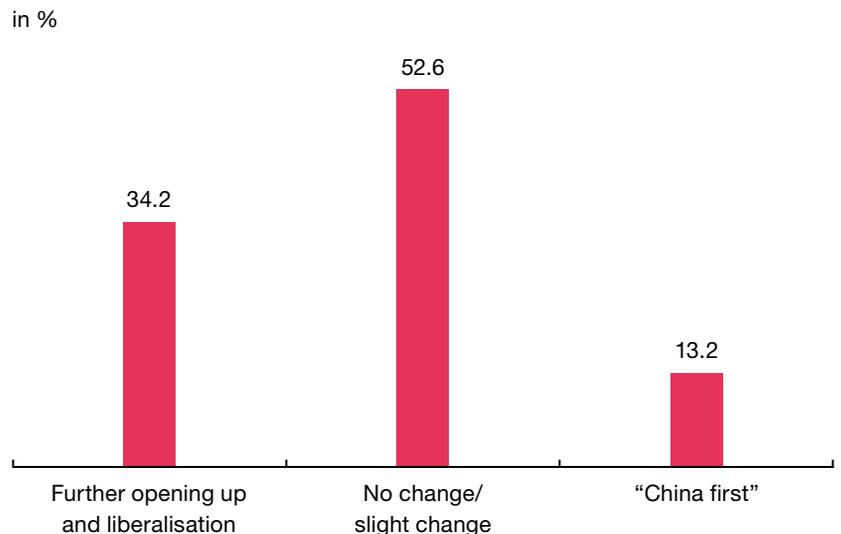
Managers' views were a little clearer on the second part of the question. This related to the expected effects of the new US trade policy on Chinese-German trade relations. A significant majority (66.6%) believed it would have positive effects on bilateral trade relations (Figure 2). Looming protectionism in the USA is viewed as an opportunity for China and Germany to work towards a rapprochement to offset any unfavourable impact on global trade coming out of the USA.

Fig. 2 What impact do you see the trend towards greater protectionism and concentration on national markets having on Chinese-German trade?



Xi Jinping, the President of the People's Republic of China, gave a speech at this year's World Economic Forum in Davos in which he supported free trade, globalisation and open markets. We asked the survey participants how significant they thought this speech was for Chinese economic policy over the next five years. The majority of managers (52.6%) thought the speech would not have a significant impact on China's economic policy in the medium term, but around a third thought it pointed to a further opening up and liberalisation of the Chinese markets. However only a few managers thought a response to the US policy in the form of "China first" was likely (Figure 3).

Fig. 3 How significant do you think the speech by the Chinese head of state, Xi Jinping, at the Davos World Economic Forum in January 2017 is for Chinese economic policy for the next five years?



The last part of the question related to the need for economic policy reform in China which is seen as necessary for a sustainable growth strategy. The managers surveyed could choose up to three out of eleven different options that they thought were particularly important in this respect. The measure mentioned most frequently, by 17%, was further privatisation of Chinese state-owned companies. This was followed by improvement in legal certainty for foreign companies (14%). Dismantling trade barriers in China was in third place (13.2%). It is also striking that strengthening environmental protection was also viewed by 11.8% of participants as a key trigger for a successful economic strategy. So the state of the environment is a not inconsiderable economic factor, at least as far as German managers are concerned.

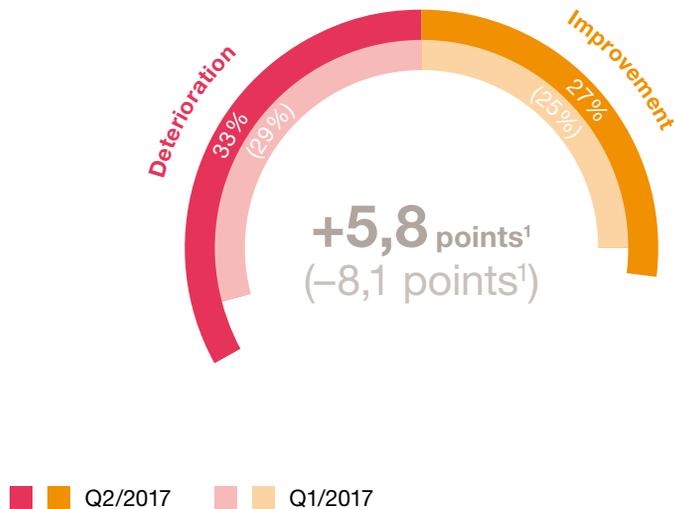
Outlook on economic growth modest

The results were mixed on China's economic prospects. On the one hand the German managers we surveyed scored China's macroeconomic situation far higher than in the previous quarter. The score is now 5.8 points compared with -8.1 in the previous survey.

However, the outlook for the next 12 months is slightly depressed. The score here fell 5.1 points to -3.5. There was no significant change in the combined ratings for expectations and situation assessment since the previous quarter, with prospects on trade with China still modest.

Some uncertainty was shown by the ratings on the likelihood of macroeconomic changes over the next 12 months. The likelihood of it both improving and deteriorating was up since the previous survey. However the overall view slightly favoured a continuing deterioration in the macroeconomic situation over an improvement.

Fig. 4 Current assessment of the economic situation in China and probability of a change in direction over the next 12 months



¹ Centre: Assessment of the current economic situation in China. Difference between positive and negative responses.
Ring: Probability of a deterioration/improvement in the economic situation over the next twelve months in percent. Difference from 100%: probability of "no change". Figures for previous quarter in brackets. Sources: ZEW and PwC.

Private domestic demand continues to grow in importance

There were marked differences since the last survey on estimates for inflation over the next six months and on interest rates. The overall score for the inflation question was up from 38.3 to 47.6 points and from 8.9 to 30.8 points on interest rates. 71.4% of managers surveyed now expect inflation to rise slightly and 12% even expect a larger increase. On interest rates, 56.4% expected these to rise over the next six months.

Ratings also changed markedly on macroeconomic drivers. The overall score for private consumption is now 41.5 points, up from 29.6 points, and the score for private investment rose from 10 points to 28.2 points. Ratings on public expenditure continued to be slightly higher, but the importance of private domestic demand is increasing noticeably. Managers' ratings for the importance of exports were down. The overall score here fell from 8.1 points to -11.6 points. Given the US government's statements on its country's pivot to increased protectionism, this is a clear change in expectations of Chinese export opportunities.

Development of indicators concerning German companies in China

Ratings for the activities of German companies in China were considerably better in the current survey. The overall scores for expectations in terms of production and workforce rose considerably. Just under 59% of the managers surveyed expected production to increase over the next six months and 49% expect the workforce to increase. Expected sales declined somewhat but around 64% of respondents were still predicting an increase.

Foreign acquisitions and investment activity in China by industry

In line with the decline in expectations on the overall economy, expectations also showed a downward trend within industries. Expectations fell sharply for the electronics and machinery industries. Both of these are highly committed to exports. However, scores for consumer industries (consumer goods, retail and services) improved, or at least remained stable compared with the previous quarter.

Expectations on corporate mergers in China fell from a balance of 51.9 points to 43.6 points. The overall ratings for Chinese foreign acquisitions fell by 5.4 to a new level of 37.5 points. But 67.5% of the managers surveyed still expect foreign acquisitions to rise. 68.3% continue to expect an increase in relation to Germany as an investment destination.

Tab. 1 Expected investment activity in China over the next six months by sector

| Industry | Trend | Balance |
|----------------------------|-------|---------|
| Services | ↑ | 51.3 |
| Information/Communications | ↑ | 45.0 |
| Consumer goods | ↑ | 34.5 |
| Automotive | ↗ | 20.0 |
| Retail | ↗ | 17.5 |
| Banking/Insurance | ↗ | 16.7 |
| Electronics | ↗ | 13.8 |
| Energy | → | 6.4 |
| Chemicals | → | 3.8 |
| Machinery | → | 0.0 |
| Construction | ↘ | -20.7 |
| Steel/Metals | ↓ | -48.8 |

Sources: ZEW und PwC.

Expectations remain dampened for regulatory environment

Ratings on the regulatory environment are almost entirely positive compared with the previous survey. There are particularly sharp changes on the “Taxation” and “Public tenders” items. Scores on taxation improved from -17.3 to 0 points and those for “Public tenders” were up from -19.3 at -8.6 points. Ratings now appear to have shifted from largely negative to more neutral territory.

Tab. 2 ZEW-PwC-China Economic Barometer: Results March 2017

| Current overall macroeconomic situation | | | | | | |
|--|-----------|-------------------|-----------|-------------------|----------|---------|
| | very good | good | normal | bad | very bad | balance |
| China | 2.3 | 27.9 | 51.2 | 16.3 | 2.3 | 5.8 |
| Eurozone | 0.0 | 19.0 | 52.4 | 23.8 | 4.8 | -7.1 |
| USA | 5.0 | 40.0 | 35.0 | 15.0 | 5.0 | 12.5 |
| Economic expectations (12 months) | | | | | | |
| | improve | slightly improve | no change | slightly worsen | worsen | balance |
| China | 0.0 | 34.9 | 32.6 | 23.3 | 9.3 | -3.5 |
| Eurozone | 0.0 | 21.4 | 50.0 | 21.4 | 7.1 | -7.1 |
| USA | 2.4 | 29.3 | 31.7 | 22.0 | 14.6 | -8.5 |
| Probability of the development of the overall macroeconomic situation in China over the next 12 months | | | | | | |
| | | | | | | |
| ■ improve ■ not change ■ worsen | | | | | | |
| Macroeconomic indicators for China (6 months) | | | | | | |
| | increase | slightly increase | no change | slightly decrease | decrease | balance |
| Inflation | 11.9 | 71.4 | 16.7 | 0.0 | 0.0 | 47.6 |
| Interest rates | 12.8 | 43.6 | 35.9 | 7.7 | 0.0 | 30.8 |
| Public debt | 40.5 | 42.9 | 16.7 | 0.0 | 0.0 | 61.9 |
| International debt | 26.3 | 34.2 | 31.6 | 7.9 | 0.0 | 39.5 |
| China's FDI inflow | 0.0 | 29.3 | 17.1 | 41.5 | 12.2 | -18.3 |
| China's FDI outflow | 25.0 | 32.5 | 15.0 | 22.5 | 5.0 | 25.0 |
| China's import activity | 4.7 | 23.3 | 37.2 | 25.6 | 9.3 | -5.8 |
| China's export activity | 7.0 | 16.3 | 27.9 | 44.2 | 4.7 | -11.6 |
| Chinese imports from Germany | 2.4 | 31.0 | 45.2 | 19.0 | 2.4 | 6.0 |
| Chinese exports to Germany | 4.7 | 25.6 | 51.2 | 16.3 | 2.3 | 7.0 |

| Investment activities in China (6 months) | increase | slightly increase | no change | slightly decrease | decrease | balance |
|--|----------|-------------------|-----------|-------------------|----------|---------|
| Banking and Insurance | 11.1 | 25.0 | 50.0 | 13.9 | 0.0 | 16.7 |
| Automotive | 12.5 | 42.5 | 20.0 | 22.5 | 2.5 | 20.0 |
| Chemicals | 7.7 | 25.6 | 38.5 | 23.1 | 5.1 | 3.8 |
| Steel/Metals | 0.0 | 12.2 | 17.1 | 31.7 | 39.0 | -48.8 |
| Electronics | 10.0 | 37.5 | 25.0 | 25.0 | 2.5 | 13.8 |
| Machinery | 2.5 | 35.0 | 30.0 | 25.0 | 7.5 | 0.0 |
| Consumer goods | 11.9 | 50.0 | 33.3 | 4.8 | 0.0 | 34.5 |
| Information and telecommunication technology | 17.5 | 57.5 | 22.5 | 2.5 | 0.0 | 45.0 |
| Construction | 4.9 | 14.6 | 36.6 | 22.0 | 22.0 | -20.7 |
| Retail | 5.0 | 42.5 | 37.5 | 12.5 | 2.5 | 17.5 |
| Energy | 5.1 | 25.6 | 51.3 | 12.8 | 5.1 | 6.4 |
| Services | 22.5 | 57.5 | 20.0 | 0.0 | 0.0 | 51.3 |
| Indicators of German companies in China (6 months) | increase | slightly increase | no change | slightly decrease | decrease | balance |
| Trade activities | 8.1 | 54.1 | 27.0 | 10.8 | 0.0 | 29.7 |
| Production | 8.8 | 50.0 | 23.5 | 14.7 | 2.9 | 23.5 |
| Sales | 15.4 | 48.7 | 23.1 | 10.3 | 2.6 | 32.1 |
| Workforce | 2.6 | 46.2 | 33.3 | 17.9 | 0.0 | 16.7 |
| Mergers & Acquisitions activities within China (6 months) | increase | slightly increase | no change | slightly decrease | decrease | balance |
| | 10.3 | 71.8 | 12.8 | 5.1 | 0.0 | 43.6 |
| Chinese M&A activities abroad (6 months) | increase | slightly increase | no change | slightly decrease | decrease | balance |
| | 37.5 | 30.0 | 7.5 | 20.0 | 5.0 | 37.5 |
| Germany's importance as an investment destination (6 months) | increase | slightly increase | no change | slightly decrease | decrease | balance |
| | 19.5 | 48.8 | 24.4 | 7.3 | 0.0 | 40.2 |

| Domestic demand in China (6 months) | increase | slightly increase | no change | slightly decrease | decrease | balance |
|--|----------|-------------------|-----------|-------------------|----------|---------|
| Average wages | 29.3 | 68.3 | 2.4 | 0.0 | 0.0 | 63.4 |
| Unit labour costs | 28.2 | 53.8 | 15.4 | 2.6 | 0.0 | 53.8 |
| Private capital investments | 20.5 | 30.8 | 38.5 | 5.1 | 5.1 | 28.2 |
| Private consumption | 24.0 | 41.5 | 26.8 | 7.3 | 0.0 | 41.5 |
| Private savings rate | 0.0 | 20.5 | 51.3 | 20.5 | 7.7 | -7.7 |
| Public spending | 29.3 | 48.8 | 22.0 | 0.0 | 0.0 | 53.7 |
| Regulatory environment (6 months) | improve | slightly improve | no change | slightly worsen | worsen | balance |
| Financing | 2.6 | 23.7 | 50.0 | 15.8 | 7.9 | -1.3 |
| Business approval requirements | 5.3 | 31.6 | 39.5 | 18.4 | 5.3 | 6.6 |
| Public tenders | 0.0 | 17.1 | 54.3 | 22.9 | 5.7 | -8.6 |
| Taxation | 5.3 | 18.4 | 55.3 | 13.2 | 7.9 | 0.0 |
| Legal protection | 2.6 | 21.1 | 57.9 | 7.9 | 10.5 | -1.3 |
| Intellectual Property | 0.0 | 28.9 | 55.3 | 5.3 | 10.5 | 1.3 |

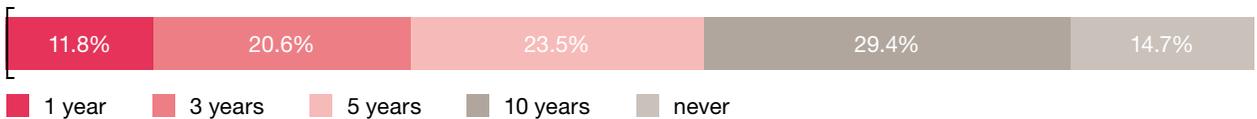
The RMB exchange rate will noticeably become more flexible within ...



Full convertibility of the RMB



Relaxation/deregulation of the sector-related Catalogue of Industries for Guiding Foreign Direct Investment



Introduction of an "International Board" at the Shanghai Stock Exchange



Note: The survey for the *ZEW-PwC-China Economic Barometer* was conducted during the period between February 3rd and 20th 2017. 44 managers of German companies located in China participated in the survey. Numbers displayed are percentages of the corresponding answer categories. Balances refer to the weighted distributions from positive and negative assessments. Assessments are weighted with +1, +0.5, 0, -0.5, -1 and move within the interval (-100, +100).

Register now!

Are you a decision-maker with expert knowledge of China? Would you like to take part in the *ZEW-PwC China Economic Barometer*, which assesses the mood of German companies with regards to China's economy every three months? Then register now for the survey at the following link: survey.zew.de/wiba. Participating is easy – you can comfortably answer the questions online with your PC or tablet.

Your benefit

You will receive the outcome of the survey before it is published, providing you with a valuable information head-start. The ZEW will of course treat your data anonymously.

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The Centre for European Economic Research (ZEW), Mannheim

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