

ZEW-PwC China Economic Barometer

Fourth quarter 2015

ZEW

Zentrum für Europäische
Wirtschaftsforschung GmbH
Centre for European
Economic Research



ZEW-PwC China Economic Barometer

Published by PricewaterhouseCoopers Aktiengesellschaft Wirtschaftsprüfungsgesellschaft (PwC) and the Centre for European Economic Research (ZEW).

October 2015, 16 pages, 2 figures, 2 tables

All rights reserved. This material may not be reproduced in any form, copied onto microfilm or saved and edited in any digital medium without the explicit permission of the publishers.

This report was compiled with the utmost care and based upon information from sources the publishers consider reliable, but for which they do not assume liability regarding accuracy, completeness and correctness. The expressed assessments reflect the opinions of the publishers at the time of the compilation of this report and can change without prior notification. Historical developments are no indicator for future results.

PricewaterhouseCoopers AG Wirtschaftsprüfungsgesellschaft and the Centre for European Economic Research (ZEW GmbH) assume no liability for direct or indirect damages that may arise from inaccuracies, incompleteness or mistakes in this report.

© October 2015 PricewaterhouseCoopers Aktiengesellschaft Wirtschaftsprüfungsgesellschaft and Zentrum für Europäische Wirtschaftsforschung GmbH (ZEW) Mannheim. All rights reserved.

In this document, "PwC" refers to PricewaterhouseCoopers Aktiengesellschaft Wirtschaftsprüfungsgesellschaft, which is a member firm of PricewaterhouseCoopers International Limited (PwCIL). Each member firm of PwCIL is a separate and independent legal entity.

Editorial

The *ZEW-PwC China Economic Barometer* presents the current situation and expected trends for the Chinese economy over the next twelve 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**

Rising concern over China's economic growth

- **Key message 2**

Higher public spending and lower interest rates to stimulate economic growth

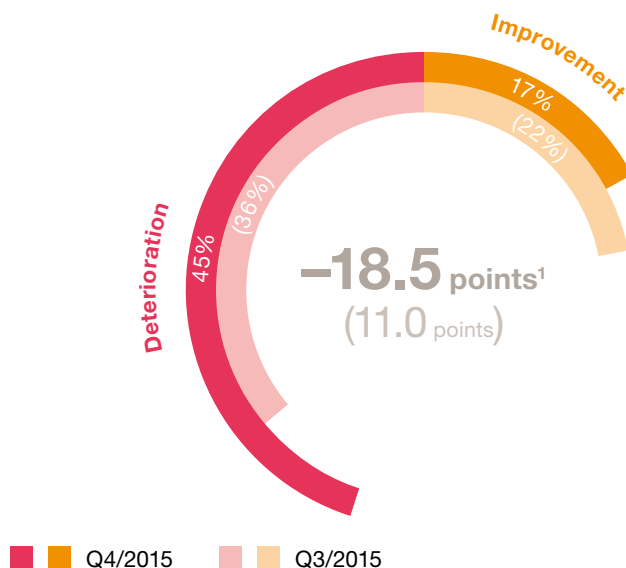
- **Key message 3**

Great uncertainty about the further development of the German automotive and automotive supply industry in China

Shifting sentiment

For the fourth quarter of 2015, the rating of the current economic situation by German managers in China has shifted considerably into negative territory with a balance of -18.5. Forty-five percent of managers surveyed estimate the probability of further economic downturn in the coming twelve months to be significantly higher than in the previous quarter.

Fig. 1 China Economic Barometer: How likely do you think the following developments in the overall economic situation in China are to take place in the next twelve months?



Remaining proportion (out of 100%): "no change" in economic situation.
Figures for previous quarter in brackets.

¹ Balance = Difference between positive and negative responses regarding the current economic situation in China in percentage points.

Increasing public spending and decreasing interest rates to stimulate economic growth

The altogether more depressed sentiment is also apparent from individual macroeconomic indicators. The majority of those surveyed now expect negative growth contributions in both private consumption and private investment. Ratings with respect to China's import demand have also fallen considerably, which is consistent with expected lower macroeconomic growth. The difference between positive and negative ratings regarding China's import activities in the coming six months has fallen from 6.4 points in the previous quarter to -29.3 points. The balance in terms of imports from Germany has also reduced from 6.6 to -16.3. Half of German managers surveyed expect demand for German goods and services to fall in the coming half year.

In light of these forecasts there are now hardly any fears of inflation. At the same time a rise in wages and also in labour unit costs is expected again by a majority, if not necessarily as strongly as in the previous quarter. Labour costs rising more steeply than retail prices tends to result in declining margins for companies.

The expectation that the Chinese government will try to adopt a more expansionary economic policy is even more apparent than in the previous quarter. Over 70% of managers predict short-term interest rates will continue falling and over 90% expect public debt to rise. In the fourth quarter "public spending" is the only category of domestic demand in China expected to rise. Evidently therefore managers do not envisage the expected fall in interest rates will be able to stimulate private demand with immediate effect.

Development of indicators concerning German companies in China

Ratings for the categories “trade activities”, “production” and “sales” of German companies in China have worsened considerably since the previous quarter. Positive and negative expectations in these categories nevertheless still balance each other out. The managers surveyed fundamentally expect development for German companies to be more positive than for the Chinese economy as a whole. However, a higher proportion of those surveyed anticipate decline (approx. 40%) as opposed to growth (approx. 30%) in the development of the “workforce” category.

Foreign acquisitions and investment activity in China by sector

Given the less favourable macroeconomic expectations in the domestic market, foreign investments continue to remain attractive for Chinese companies. Almost 80% of managers surveyed anticipate further investment in the course of the coming six months. Two thirds of those surveyed expect Germany’s importance as an investment destination to grow. By contrast ratings for mergers and acquisitions activities within China are weaker than in the previous quarter, but again in this category a majority (60%) expects continued growth.

In the predictions for investment activity in China by sector, however, the weakness of the overall economy stands out significantly. In nearly all sectors – particularly in the steel/metals, construction, automotive, chemicals and machinery sectors – ratings worsened very distinctly and the majority of managers expect a decrease in investment activity in the coming half year.

Interestingly, ratings for the services, information and telecommunication technology sectors, as well as for the energy and banking sectors, improved slightly compared to the previous quarter. Even in times of economic weakness the managers surveyed evidently recognise further potential for development with regard to investment activity in these sectors.

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

Industry	Trend	Balance
Services	↑	39.3
Information/Communications	↑	34.6
Energy	↗	15.4
Banking/Insurance	↗	12.8
Consumer goods	→	9.5
Retail	→	-5.0
Electronics	→	-9.8
Machinery	↘	-25.0
Chemicals	↘	-25.7
Automotive	↓	-37.5
Construction	↓	-56.3
Steel/Metals	↓	-59.0

Source: ZEW and PwC.

Trends in the regulatory environment

In some categories, such as e.g. “legal protection” and “taxation”, a slight deterioration is expected in the next half year. The German managers surveyed do not anticipate the weak economy will lead to an improvement of the regulatory environment. A large number of those surveyed (43%) still expect the situation regarding conditions for business financing to improve in the medium term.

Results of the special question

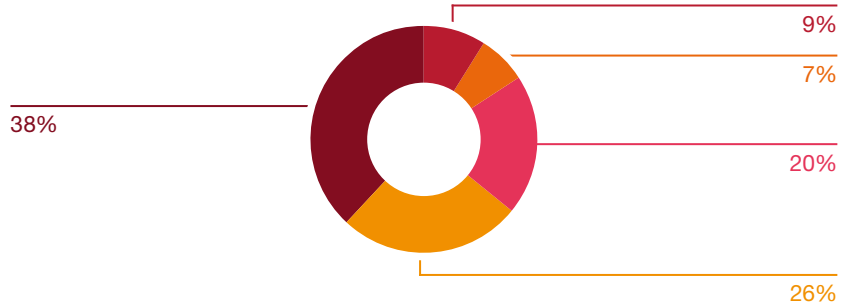
What consequences will the decline of the Chinese automotive sector have for the German automotive and automotive supply industry?

In comparison to the development of the Chinese automotive industry, which currently finds itself in decline, the outlook on the development of sales of German car manufacturers is mixed. This indicates a high level of uncertainty of opinion regarding prospects for further development. Overall 36% of managers surveyed expect the relative market share of German car manufacturers to increase; 20% are of the opinion that sales of German car makers will indeed fall, but not as sharply as the overall economy. Seven percent believe sales will remain constant and 9% even expect sales to rise. By contrast 38% expect the market share to decrease and 26% of those surveyed expect no change.

Expectations for the German supply industry are more restrained: 38% of those surveyed expect no significant change in the market share of German suppliers; just as many managers foresee a decrease and only 24% predict an increase.

A clear trend among market share predictions is therefore indiscernible. The phenomenon of China’s economic weakness is too recent and the assessment of the future development of German manufacturers and suppliers in the automotive industry is too uncertain.

Fig. 2 How will the economic weakness of the Chinese automotive sector influence sales of German car manufacturers in China?



- Despite the decline of the Chinese automotive sector sales of German car manufacturers will increase.
- Despite the decline of the Chinese automotive sector sales of German car manufacturers will remain virtually constant.
- Sales will fall, but the proportion of sales of German car manufacturers will fall less sharply than the overall Chinese economy (increasing market share).
- Sales will fall and the proportion of sales of German car manufacturers will fall just as sharply as the overall Chinese economy (constant market share).
- Sales will fall, but the proportion of sales of German car manufacturers will fall more sharply than the overall Chinese economy (decreasing market share).

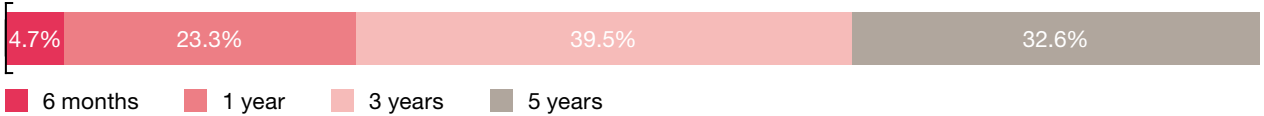
Tab. 2 ZEW-PwC China Economic Barometer Q4 2015: Detailed results of the standardised questions

Current overall macroeconomic situation						
	very good	good	normal	bad	very bad	balance
China	0.0	8.7	45.7	45.7	0.0	-18.5
Eurozone	2.2	13.0	63.0	21.7	0.0	-2.2
USA	4.7	65.1	25.6	2.3	2.3	33.7
Economic expectations (12 months)						
	improve	slightly improve	no change	slightly worsen	worsen	balance
China	0.0	14.9	21.3	46.8	17.0	-33.0
Eurozone	4.4	11.1	48.9	28.9	6.7	-11.1
USA	0.0	26.2	59.5	14.3	0.0	6.0
Probability of the development of the overall macroeconomic situation in China over the next 12 months						
	17.1%	38.0%		44.9%		
	improve	not change		worsen		
Macroeconomic indicators for China (6 months)						
	increase	slightly increase	no change	slightly decrease	decrease	balance
Inflation	6.5	39.1	34.8	17.4	2.2	15.2
Interest rates	0.0	6.5	21.7	58.7	13.0	-39.1
Public debt	37.8	53.3	8.9	0.0	0.0	64.4
International debt	14.0	41.9	37.2	4.7	2.3	30.2
China's FDI inflow	0.0	13.3	20.0	42.2	24.4	-38.9
China's FDI outflow	13.6	50.0	36.4	0.0	0.0	38.6
China's import activity	2.2	15.2	21.7	43.5	17.4	-29.3
China's export activity	0.0	22.2	28.9	31.1	17.8	-22.2
Chinese imports from Germany	2.2	19.6	28.3	43.5	6.5	-16.3
Chinese exports to Germany	0.0	19.6	41.3	34.8	4.3	-12.0

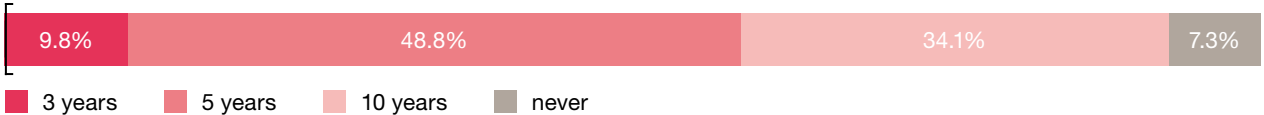
Investment activities in China (6 months)	increase	slightly increase	no change	slightly decrease	decrease	balance
Banking and Insurance	7.0	32.6	41.9	16.3	2.3	12.8
Automotive	0.0	15.9	15.9	45.5	22.7	-37.5
Chemicals	5.7	11.4	28.6	34.3	20.0	-25.7
Steel/Metals	0.0	7.7	12.8	33.3	46.2	-59.0
Electronics	4.9	24.4	26.8	34.1	9.8	-9.8
Machinery	2.4	16.7	21.4	47.6	11.9	-25.0
Consumer goods	7.1	28.6	40.5	23.8	0.0	9.5
Information and telecommunication technology	17.9	43.6	28.2	10.3	0.0	34.6
Construction	0.0	5.0	17.5	37.5	40.0	-56.3
Retail	0.0	25.0	42.5	30.0	2.5	-5.0
Energy	7.7	38.5	33.3	17.9	2.6	15.4
Services	19.0	47.6	26.2	7.1	0.0	39.3
Indicators of German companies in China (6 months)	increase	slightly increase	no change	slightly decrease	decrease	balance
Trade activities	2.5	32.5	40.0	15.0	10.0	1.3
Production	7.7	20.5	38.5	23.1	10.3	-3.8
Sales	7.0	27.9	27.9	30.2	7.0	-1.2
Workforce	2.2	26.7	28.9	35.6	6.7	-8.9
Mergers & Acquisitions activities within China (6 months)	increase	slightly increase	no change	slightly decrease	decrease	balance
	16.7	42.9	26.2	7.1	7.1	27.4
Chinese M&A activities abroad (6 months)	increase	slightly increase	no change	slightly decrease	decrease	balance
	28.9	48.9	13.3	8.9	0.0	48.9
Germany's importance as an investment destination (6 months)	increase	slightly increase	no change	slightly decrease	decrease	balance
	13.3	53.3	24.4	6.7	2.2	34.4

Domestic demand in China (6 months)	increase	slightly increase	no change	slightly decrease	decrease	balance
Average wages	22.2	53.3	20.0	4.4	0.0	46.7
Unit labour costs	20.5	45.5	25.0	9.1	0.0	38.6
Private capital investments	4.5	11.4	34.1	38.6	11.4	-20.5
Private consumption	5.0	27.3	25.0	40.9	2.3	-4.5
Private savings rate	4.5	29.5	36.4	25.0	4.5	2.3
Public spending	40.9	45.5	6.8	4.5	2.3	59.1
Regulatory environment (6 months)	improve	slightly improve	no change	slightly worsen	worsen	balance
Financing	0.0	42.9	33.3	21.4	2.4	8.3
Business approval requirements	4.7	30.2	37.2	23.3	4.7	3.5
Public tenders	0.0	15.0	55.0	20.0	10.0	-12.5
Taxation	0.0	20.9	44.2	25.6	9.3	-11.6
Legal protection	0.0	16.3	62.8	18.6	2.3	-3.5
Intellectual Property	2.4	16.7	61.9	16.7	2.4	0.0

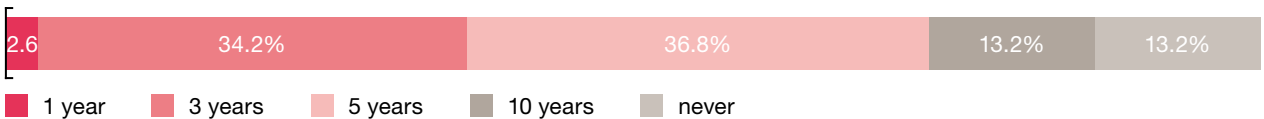
The RMB exchange rate will noticeably become more flexible within...



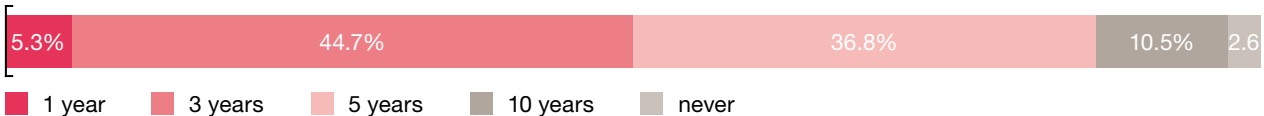
Full convertibility of the RMB



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 September survey for the *ZEW-PwC China Economic Barometer* was conducted during the period 09/14–09/28/2015. 47 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 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.

Contacts



PwC

Thomas Heck

Partner, Assurance, Leader at China
Business Group

Tel: +86 21 2323-2266

thomas.l.heck@cn.pwc.com

About us

Our clients face diverse challenges, strive to put new ideas into practice and seek expert advice. They turn to us for comprehensive support and practical solutions that deliver maximum value. Whether for a global player, a family business or a public institution, we leverage all of our assets: experience, industry knowledge, high standards of quality, commitment to innovation and the resources of our expert network in 157 countries. Building a trusting and cooperative relationship with our clients is particularly important to us – the better we know and understand our clients' needs, the more effectively we can support them.

PwC. 9,800 dedicated people at 29 locations. €1.65 billion in turnover. The leading auditing and consulting firm in Germany.



ZEW

Prof Dr Michael Schröder

Project Leader and Senior Researcher,
International Finance and Financial
Management

Tel: +49 621 1235-368

schroeder@zew.de

The Centre for European Economic Research (ZEW), Mannheim

ZEW works in the field of applied empirical economic research. It has gained a strong national and international reputation through its work on internationally comparative research in a European context, in particular, as well as the development of important scientific data bases, e.g. the Mannheim Innovation Panel (MIP) and the ZEW Start-up Panel. ZEW's key objectives are to conduct excellent economic research, provide science-based economic policy advice and transfer knowledge. ZEW was founded in 1991 and employs a staff of approximately 190, two thirds of whom are researchers.

