

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 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**

Negative trend shows slight improvement

- **Key message 2**

Unit labour costs boost inflation concerns

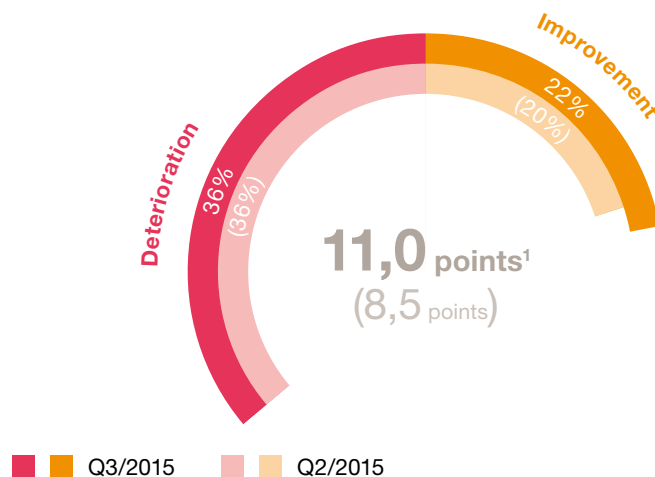
- **Key message 3**

German companies feel well positioned with respect to their Chinese competitors

Some grounds for optimism over current situation but overall trend still downward

For the third quarter of 2015, the rating of the current economic situation by German managers in China is up at 11 points. This is broadly the same as in the third quarter of 2014. The proportion of managers surveyed who think an economic upturn is likely in the next twelve months is around 22%, slightly up on the previous quarter, whilst the proportion who think it will deteriorate remains the same at 36%. The overall rating of economic performance thus remains negative at -8.5 points.

Fig. 1 Current assessment of the economic situation in China and probability of a change in direction over 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.

Source: ZEW and PwC.

Rising inflation and intensified efforts to stimulate growth

Some of the scores for macroeconomic variables for the next six months have changed considerably since the second quarter. The score for inflation rose to 22.4 points; almost 50% of those surveyed now expect consumer prices to increase in this period. One factor driving inflation would be a further increase in unit labour costs, which around 90% of those surveyed are convinced will happen.

On interest rates, the majority – around 60% – expect rates to continue to fall. Given the current low inflation and deteriorating economic prospects, they believe that the People's Bank of China seemingly has the scope – or will be forced – to reduce interest rates further. But 51.3% of those surveyed expect private investment to rise, and 63% even expect private consumption to increase. 67% of managers believe government expenditure will continue to rise.

On China's trade activities, ratings are considerably more negative than they were just last quarter, for both exports and imports. Around 54% of those surveyed expect imports to fall and only envision a slight increase in exports.

The same pattern applies to inward investment, which is expected to weaken considerably; at -28.2%, it is the lowest score since 2013.

Development of indicators concerning German companies in China

The appraisal of the activities of German companies in China is viewed in a similarly cautious manner to the economic situation in China. Those surveyed see no change in the workforce for the next six months and also expect trade activities to stagnate. On production, the ratings are a little more positive, with 39% of managers expecting it to continue to grow, compared with the 27% who are expecting the reverse. The most positive view remains that of sales by German companies in China, where around 48% expect them to continue to increase.

Foreign acquisitions and investment activity in China by sector

With respect to Chinese foreign investment, over 83% of those surveyed expect this to continue to increase in the next six months. Although Germany's attractiveness as an investment destination was down slightly on the second quarter, around 61% of those surveyed still think Chinese investments in Germany will increase.

In terms of investment in China, the managers surveyed are much more positive about the situation compared with the second quarter, although ratings vary considerably from industry to industry. The most positive changes since the last survey are seen in the machinery, chemicals, steel/metals and construction industries. In the last two, however, the balance is still in negative territory. A more marked fall in investment activity is expected in the energy and service industries.

The highest ratings continue to be reserved for the information and telecommunication technology industries. Here, 68% of those surveyed expect investment activity in China to rise.

Fig. 2 Expected investment activity in China in the next six months by industry

Industry	Trend	Balance
Information/Communications	↑	42.2
Services	↑	33.9
Banking/Insurance	↑	32.3
Consumer goods	↗	23.5
Machinery	↗	18.6
Electronics	↗	17.1
Retail	↗	16.7
Energy	↗	14.1
Automotive	↗	12.5
Chemicals	↗	11.7
Construction	↘	-28.8
Steel/Metals	↘	-30.0

Source: ZEW and PwC.

Trends in the regulatory environment

Depending on the category, 50% to 60% of those surveyed do not expect there to be any changes in the regulatory environment in the next six months. It is only in the “financing” and “business approval requirements” categories that the majority of those surveyed expect to see an improvement. A much larger number of senior executives now share the view that RMB exchange rate flexibilisation and the free convertibility of the Chinese currency are drawing closer.

An analysis of managers’ ratings since our surveys began in the fourth quarter of 2013 shows that the forecasts on legal protection and intellectual property, which were originally very positive, have now given way to a much more sober view.

Evaluation of Chinese competitors

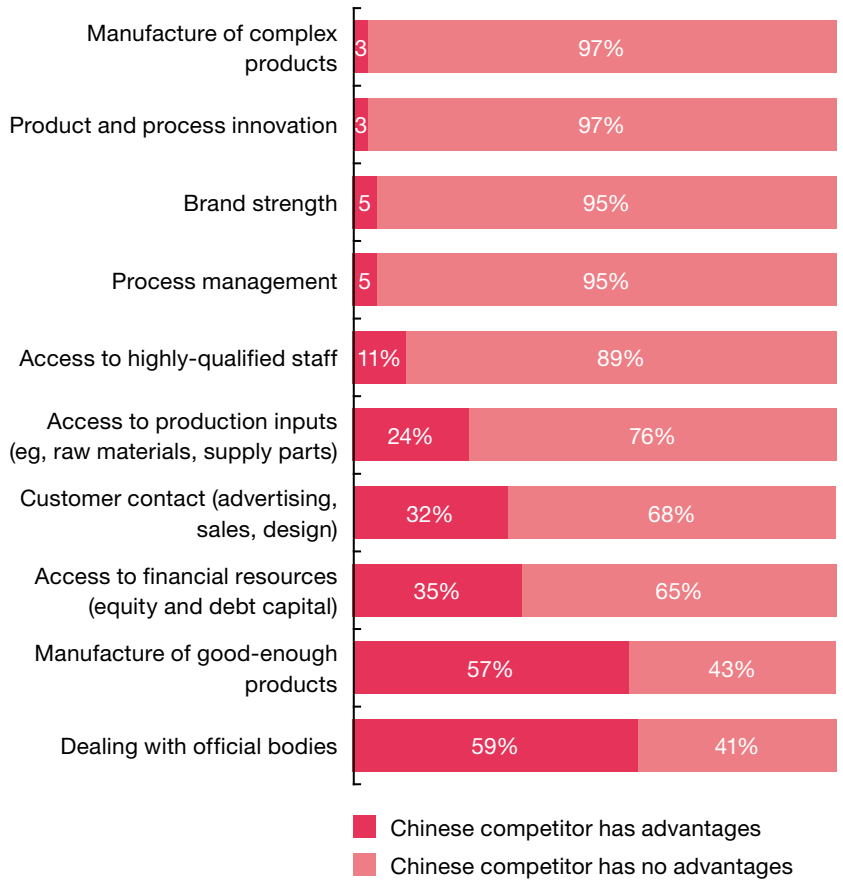
The majority of managers think their own company is slightly (46%) or considerably (27%) ahead of the Chinese competitors. Eleven percent of managers are even of the opinion that they are in the position of having no direct competitors. Just eight percent state that the Chinese competitors have a competitive advantage.

The German companies believe they have the advantage in almost all of the rating categories, but particularly with respect to the manufacture of complex products, process and product innovation, brand strength, process management and access to highly-qualified staff. However, they admit that where their direct Chinese competitors score higher is in relation to dealing with official bodies, manufacturing good-enough products and access to funding. Those surveyed believe that German companies in China are very well equipped to compete with their Chinese competitors.

Fig. 3 Rating of Chinese competitors by industry

In what areas have your Chinese competitors in China got a competitive advantage over your company?

Multiple answers possible



Eight percent state that the Chinese competitors have a competitive advantage.

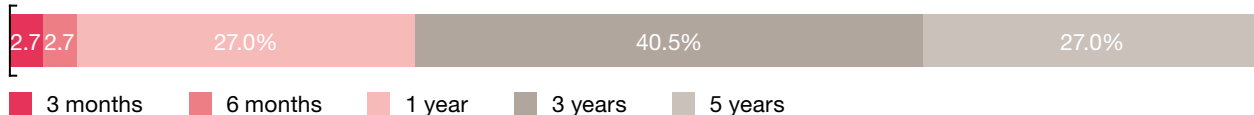
Fig. 4 ZEW-PwC China Economic Barometer Q3 2015: Detailed results of the standardised questions

Current overall macroeconomic situation						
	very good	good	normal	bad	very bad	balance
China	4.9	29.3	48.8	17.1	0.0	11.0
Eurozone	2.6	7.9	42.1	47.4	0.0	-17.1
USA	5.4	37.8	35.1	18.9	2.7	12.2
Economic expectations (12 months)						
	improve	slightly improve	not change	slightly worsen	worsen	balance
China	4.9	19.5	34.1	36.6	4.9	-8.5
Eurozone	2.5	25.0	42.5	27.5	2.5	-1.3
USA	5.1	20.5	53.8	17.9	2.6	3.8
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	not change	slightly decrease	decrease	balance
Inflation	10.5	39.5	34.2	15.8	0.0	22.4
Interest rates	0.0	13.2	26.3	47.4	13.2	-30.3
Public debt	25.6	46.2	28.2	0.0	0.0	48.7
International debt	2.7	40.5	48.6	8.1	0.0	18.9
China's FDI inflow	7.7	12.8	12.8	48.7	17.9	-28.2
China's FDI outflow	26.3	50.0	15.8	5.3	2.6	46.1
Chinas import activity	5.1	38.5	25.6	25.6	5.1	6.4
Chinas export activity	5.3	23.7	15.8	36.8	18.4	-19.7
Chinese imports from Germany	2.6	34.2	39.5	21.1	2.6	6.6
Chinese exports to Germany	2.6	20.5	35.9	35.9	5.1	-10.3

Investment activities in China (6 months)	increase	slightly increase	not change	slightly decrease	decrease	balance
Banking and Insurance	19.4	38.7	29.0	12.9	0.0	32.3
Automotive	8.3	41.7	19.4	27.8	2.8	12.5
Chemicals	10.0	30.0	36.7	20.0	3.3	11.7
Steel/Metals	3.3	20.0	20.0	26.7	30.0	-30.0
Electronics	8.6	40.0	34.3	11.4	5.7	17.1
Machinery	17.1	25.7	37.1	17.1	2.9	18.6
Consumer goods	11.8	38.2	35.3	14.7	0.0	23.5
Information and telecommunication technology	18.8	50.0	28.1	3.1	0.0	42.2
Construction	6.1	18.2	18.2	27.3	30.3	-28.8
Retail	6.1	36.4	42.4	15.2	0.0	16.7
Energy	3.1	40.6	40.6	12.5	3.1	14.1
Services	16.1	41.9	35.5	6.5	0.0	33.9
Indicators of German companies in China (6 months)	increase	slightly increase	not change	slightly decrease	decrease	balance
Trade activities	14.7	14.7	41.2	26.5	2.9	5.9
Production	12.1	27.3	33.3	24.2	3.0	10.6
Sales	17.1	31.4	20.0	28.6	2.9	15.7
Workforce	8.3	22.2	33.3	30.6	5.6	-1.4
Mergers & Acquisitions activities within China (6 months)	increase	slightly increase	not change	slightly decrease	decrease	balance
	16.7	63.9	16.7	0.0	2.8	45.8
Chinese M&A activities abroad (6 months)	increase	slightly increase	not change	slightly decrease	decrease	balance
	33.3	50.0	16.7	0.0	0.0	58.3
Germany's importance as an investment destination (6 months)	increase	slightly increase	not change	slightly decrease	decrease	balance
	30.6	30.6	27.8	8.3	2.8	38.9

Domestic demand in China (6 months)	increase	slightly increase	not change	slightly decrease	decrease	balance
Average wages	34.2	55.3	10.5	0.0	0.0	61.8
Unit labour costs	34.2	55.3	10.5	0.0	0.0	61.8
Private capital investments	10.8	40.5	37.8	8.1	2.7	24.3
Private consumption	13.0	50.0	26.3	10.5	0.0	32.9
Private savings rate	5.4	18.9	45.9	27.0	2.7	-1.4
Public spending	19.4	47.2	19.4	13.9	0.0	36.1
Regulatory environment (6 months)	improve	slightly improve	not change	slightly worsen	worsen	balance
Financing	2.8	47.2	38.9	8.3	2.8	19.4
Business approval requirements	2.8	36.1	44.4	16.7	0.0	12.5
Public tenders	5.9	8.8	58.8	26.5	0.0	-2.9
Taxation	0.0	27.0	51.4	16.2	5.4	0.0
Legal protection	0.0	19.4	61.1	19.4	0.0	0.0
Intellectual Property	2.8	27.8	58.3	8.3	2.8	9.7

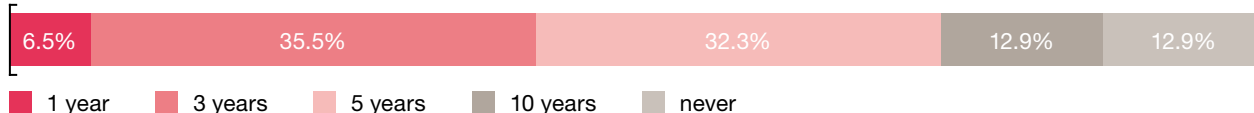
The RMB exchange rate will noticeably become more flexible within ...



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 June survey for the ZEW-PwC-China Economic Barometer was conducted during the period 06/01 – 06/22/2015. 42 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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