

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**

Higher public spending to support economic growth

- **Key message 2**

Sharp increase forecast in company takeovers in China and abroad

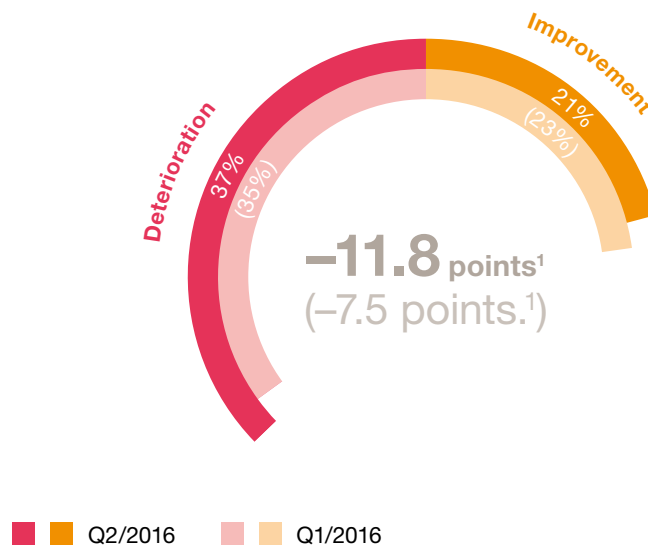
- **Key message 3**

New capital controls expected to have only minor impact

Economic expectations down again slightly

After sentiment picked up considerably in the previous quarter, ratings of the economic situation by German managers in China have fallen to -11.8 points for the second quarter of 2016. The aggregate score has been in negative territory for more than half a year, showing that the overall assessment of the economic situation is rather gloomy. The experts think there is only a 21% likelihood of an economic upturn over the next twelve months, whilst the likelihood of a continuing downturn has risen to 37%.

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

Higher public spending to support economic growth

There has been a striking shift in expectations on China's public debt. The score has gone up from 52.7 in the previous quarter to 75 points in the current quarter, a considerable increase. The managers surveyed also expect international debt to increase even further over the coming year (Q1 2016: 22.2 points; Q2 2016: 31.4 points). The forecast increase in debt is mainly due to an increase in public spending. This indicator has also increased sharply, from 48.7 (Q1 2016) to 60.5 points. Together with private consumption, which is expected to continue rising, public spending is currently the central factor driving growth.

Managers were particularly negative on prospects for Chinese exports, which they expect to continue to decline. This indicator has been in negative territory since Q2 2015 and is now at -25.0 points, an all-time low.

Development of indicators concerning German companies in China

Ratings for the categories "trade activities", "sales" and "workforce" of German companies in China show little or no change since the last quarter and are slightly up for the next six months. However, the forecast for "production activities" has declined, dropping from 16.1 points in Q1 2016 to 5.9 points in Q2 2016. Overall, the managers surveyed expect the activities of German companies in China to show moderate growth over the coming half year, particularly in relation to sales of products and services.

Foreign acquisitions and investment activity in China by sector

The ratings for mergers and acquisitions show a strong increase from already high expectations, regarding both domestic and foreign acquisitions by Chinese companies. The indicator for mergers and acquisitions in China has increased from 29.7 in Q2 2016 to 44.4 points. The indicator for foreign acquisitions was already 56.6 points in Q1 2016 and has again achieved a very high level of 71.6 points. Germany's importance as an investment destination for Chinese investors is expected to continue to grow.

The predictions for investment activity by sector show a continuing increase in expected spending in the consumer industry in particular. Ratings for the services, information and communications sectors, as well as the consumer sector, have again improved noticeably over the previous quarter. However, ratings for the banking and insurance sector have worsened. As in previous quarters, the construction and steel/metals sectors are scoring well behind the others.

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

Industry	Trend	Balance
Services	↑	56.9
Information/Communications	↑	50.0
Consumer goods	↑	35.7
Banking/Insurance	↗	17.2
Retail	↗	12.9
Electronics	↗	10.6
Energy	→	7.4
Machinery	→	-5.9
Automotive	→	-8.6
Chemicals	↘	-16.1
Construction	↓	-34.3
Steel/Metals	↓	-64.7

Sources: ZEW and PwC.

Trends in the regulatory environment

There were only slight changes in ratings for the regulatory environment for German companies in China. Ratings for conditions for business financing continue to be relatively positive. However, ratings for public tenders show a noticeably less favourable trend, declining from 0 to -7.1 points.

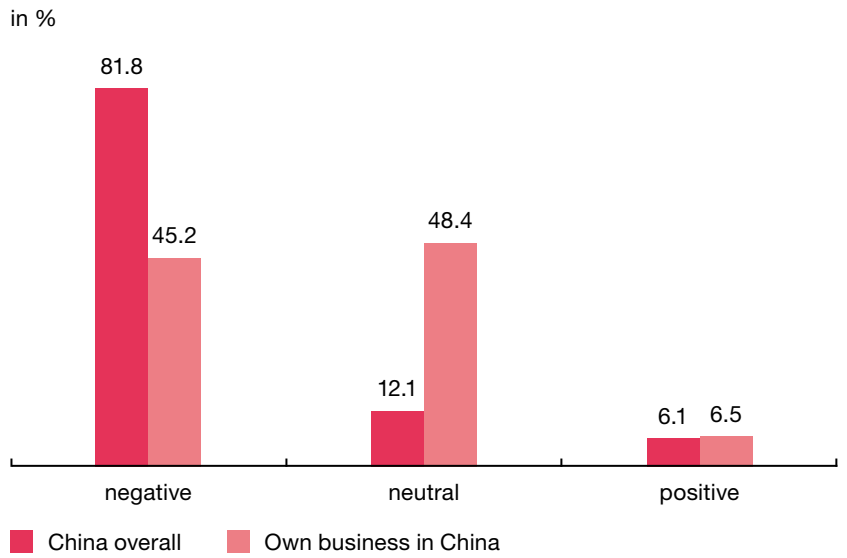
Results of the special question: What impact will the new, stricter capital controls have?

The Chinese Central Bank imposed new restrictions on so-called “cross-border cash pooling” at the end of January 2016. Negative cross-border cash pool balances are no longer permitted until further notice. China’s State Administration of Foreign Exchange (SAFE) has also restricted cross-border cash withdrawals by UnionPay bank card holders since October 2015.

The impact of these restrictions varies widely. The new restrictions have affected just 26% of respondents severely, with 43% slightly affected and 31% practically unaffected.

81% of the managers surveyed expect the potential consequences of these restrictions for China overall to be negative, although 72% of these expect that the impact will only be minor. Regarding the consequences for their company’s own business in China, 45% expect it to suffer, although responses overwhelmingly suggest that the negative impact will be negligible.

Fig. 2 Impact of the new capital controls



Tab. 2 ZEW-PwC China Economic Barometer: Results March 2016

Current overall macroeconomic situation						
	very good	good	normal	bad	very bad	balance
China	2.6	13.2	44.7	36.8	2.6	-11.8
Eurozone	2.9	11.4	68.6	17.1	0.0	0.0
USA	0.0	52.9	47.1	0.0	0.0	26.5
Economic expectations (12 months)						
	improve	slightly improve	no change	slightly worsen	worsen	balance
China	0.0	21.6	35.1	29.7	13.5	-17.6
Eurozone	0.0	11.1	44.4	41.7	2.8	-18.1
USA	2.8	22.2	66.7	8.3	0.0	9.7

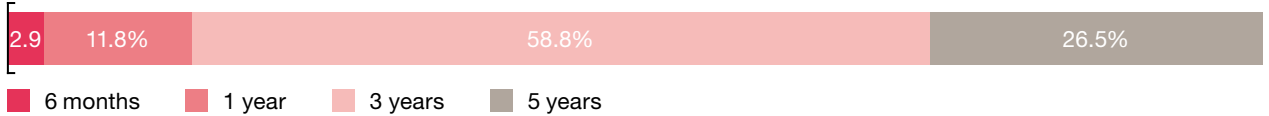
Probability of the development of the overall macroeconomic situation in China over the next 12 months


Macroeconomic indicators for China (6 months)						
	increase	slightly increase	no change	slightly decrease	decrease	balance
Inflation	17.6	47.1	23.5	11.8	0.0	35.3
Interest rates	0.0	8.8	29.4	52.9	8.8	-30.9
Public debt	55.6	38.9	5.6	0.0	0.0	75.0
International debt	17.1	40.0	31.4	11.4	0.0	31.4
China's FDI inflow	2.9	17.1	20.0	37.1	22.9	-30.0
China's FDI outflow	35.3	44.1	14.7	5.9	0.0	54.4
China's import activity	0.0	25.7	37.1	22.9	14.3	-12.9
China's export activity	2.8	19.4	25.0	30.6	22.2	-25.0
Chinese imports from Germany	2.9	25.7	31.4	31.4	8.6	-8.6
Chinese exports to Germany	8.8	17.6	38.2	26.5	8.8	-4.4

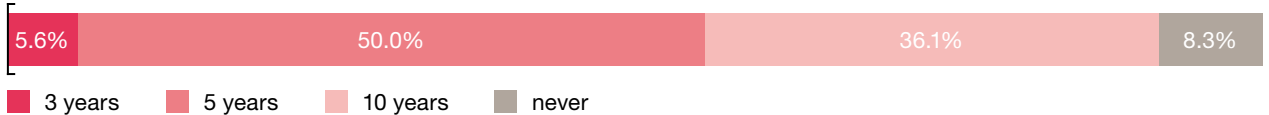
Investment activities in China (6 months)	increase	slightly increase	no change	slightly decrease	decrease	balance
Banking and Insurance	10.3	34.5	37.9	13.8	3.4	17.2
Automotive	8.6	20.0	25.7	37.1	8.6	-8.6
Chemicals	3.2	12.9	45.2	25.8	12.9	-16.1
Steel/Metals	0.0	5.9	14.7	23.5	55.9	-64.7
Electronics	0.0	45.5	36.4	12.1	6.1	10.6
Machinery	8.8	32.4	23.5	8.8	26.5	-5.9
Consumer goods	14.3	51.4	28.6	2.9	2.9	35.7
Information and telecommunication technology	26.5	50.0	20.6	2.9	0.0	50.0
Construction	2.9	14.3	20.0	37.1	25.7	-34.3
Retail	8.6	28.6	45.7	14.3	2.9	12.9
Energy	11.8	23.5	41.2	14.7	8.8	7.4
Services	30.6	52.8	16.7	0.0	0.0	56.9
Indicators of German companies in China (6 months)	increase	slightly increase	no change	slightly decrease	decrease	balance
Trade activities	11.1	33.3	36.1	11.1	8.3	13.9
Production	8.8	20.6	50.0	14.7	5.9	5.9
Sales	11.1	44.4	30.6	11.1	2.8	25.0
Workforce	8.1	29.7	35.1	21.6	5.4	6.8
Mergers & Acquisitions activities within China (6 months)	increase	slightly increase	no change	slightly decrease	decrease	balance
	25.0	50.0	19.4	0.0	5.6	44.4
Chinese M&A activities abroad (6 months)	increase	slightly increase	no change	slightly decrease	decrease	balance
	48.6	45.9	5.4	0.0	0.0	71.6
Germany's importance as an investment destination (6 months)	increase	slightly increase	no change	slightly decrease	decrease	balance
	40.5	35.1	21.6	2.7	0.0	56.8

Domestic demand in China (6 months)	increase	slightly increase	no change	slightly decrease	decrease	balance
Average wages	31.6	55.3	10.5	2.6	0.0	57.9
Unit labour costs	28.9	50.0	13.2	7.9	0.0	50.0
Private capital investments	2.7	35.1	37.8	18.9	5.4	5.4
Private consumption	8.0	48.6	35.1	8.1	0.0	28.4
Private savings rate	2.7	24.3	45.9	27.0	0.0	1.4
Public spending	39.5	50.0	5.3	2.6	2.6	60.5
Regulatory environment (6 months)	improve	slightly improve	no change	slightly worsen	worsen	balance
Financing	6.1	42.4	39.4	12.1	0.0	21.2
Business approval requirements	2.8	27.8	55.6	8.3	5.6	6.9
Public tenders	0.0	14.3	62.9	17.1	5.7	-7.1
Taxation	5.7	17.1	48.6	20.0	8.6	-4.3
Legal protection	0.0	25.0	58.3	8.3	8.3	0.0
Intellectual Property	0.0	33.3	58.3	2.8	5.6	9.7

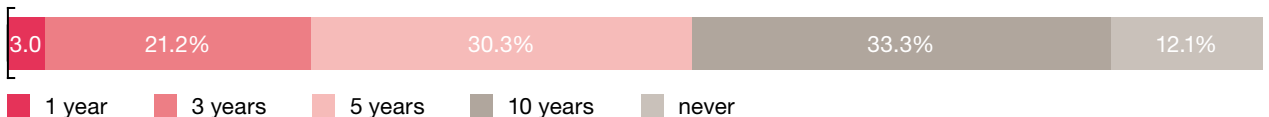
The RMB exchange rate will noticeably become more flexible within...



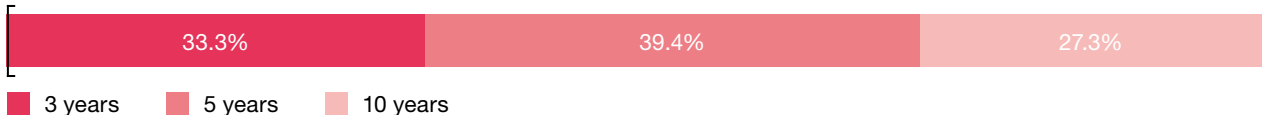
Full convertibility of the RMB



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



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



Comment: The March survey for the *ZEW-PwC China Economic Barometer* was conducted from 09. March to 04. April 2016. 38 senior executives from German companies in China took part. The numbers displayed are the percentages for each response category. Balances are based on the weighted distribution of positive and negative assessments. They range within the interval (-100, +100). The numbers are rounded to a single decimal place.

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.

Contacts



PwC

Thomas Heck

Partner, Assurance, Leader at China
Business Group

Tel: +86 21 2323-2266

thomas.l.heck@cn.pwc.com

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ZEW

Dr Michael Schröder

Project Leader and Senior Researcher,
International Finance and Financial
Management

Tel: +49 621 1235-368

schroeder@zew.de

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