



THE WEEKLY **ASIA** ECONOMIC MONITOR

FEBRUARY 4, 2019
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China's Caixin manufacturing PMI plunged unexpectedly in January, to its lowest level in three years.

The index is unlikely to fall much further, although it should remain subdued into Q3.

The unemployment rate in Japan fell again in December, but the story isn't all rosy.

Unboxing—and Making Sense—of the Collapse in China's Caixin PMI

The Caixin manufacturing PMI for January was grim, indicating that China's start to the year wasn't as benign as the official surveys suggested. The index dropped off a cliff, plunging to 48.3 from 49.7 in December and hitting its lowest point since early 2016. The drop was led by falls in the output and new orders sub-indices, jarring with their broadly stable counterparts in the official manufacturing gauge.

Crucially, the weakness in new orders was mostly in domestic demand. The extent of the slump in local demand was significant, as total new orders contracted despite the simultaneous surge in overseas sales to their strongest level since March.

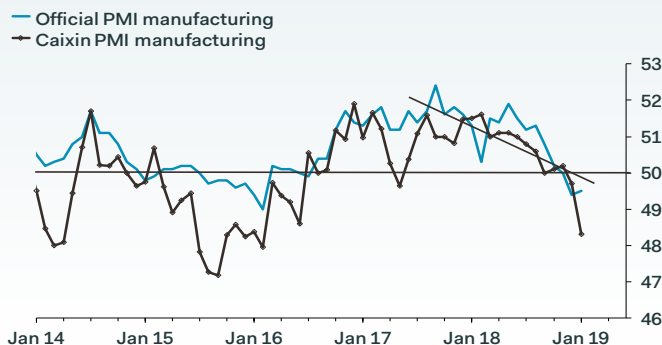
We aren't reading too much into the jump in new export orders just yet, though, not least because

it clashes with the still-abysmal official measure. That sub-index improved marginally in January, but remains consistent with falling exports. *Moreover, the little hard data, so far, on trade activity in Asia in January have been poor.*

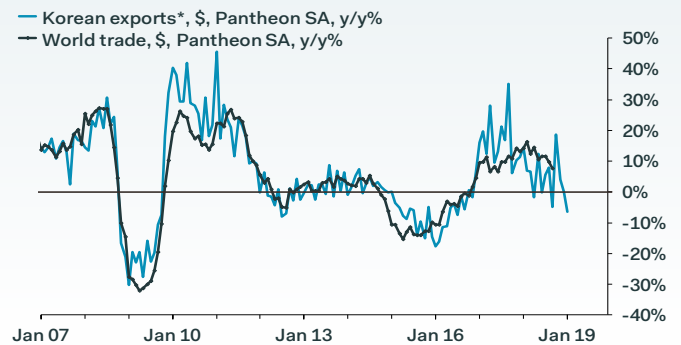
Korean exports, which are reported early and provide a good barometer for global trade, contracted by 5.8% year-over-year in January, marking a deterioration in growth from -1.3% in December. Trends at the margin are even more shocking. Exports collapsed at an annualised rate of -18.9% in the three months to January, compared with the previous three months, seasonally adjusted, down from their -9.5% plunge in the three months to December.

The relative weakness of the Caixin PMI compared with its official counterpart likely reflects, in part, the big differences between their target samples. The Caixin survey purports to gauge the health of small- and medium-sized private firms, while the official one focuses on large state-owned enterprises. Naturally, it's much easier for the authorities to force SOEs into action with the press of a button. **The private sector's ostensibly weaker performance adds weight to our assumption that the transmission mechanism of the authorities' SME-focussed stimulus won't be as smooth.**

THE PRIVATE SECTOR IN CHINA SCREAMS "OUCH"

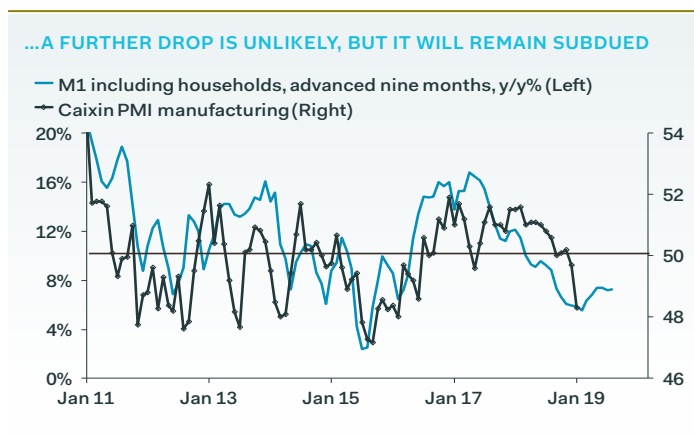
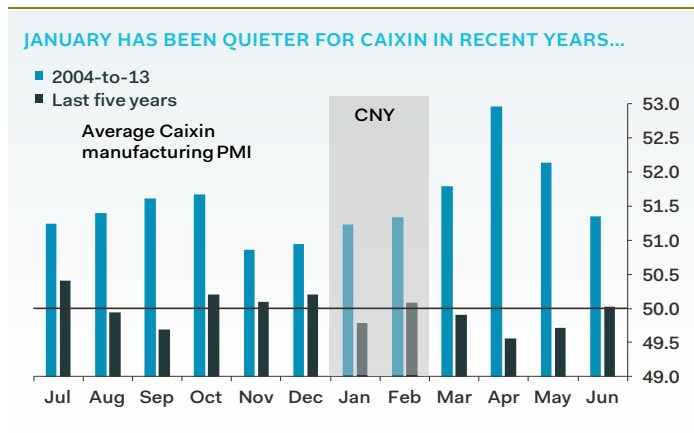


KOREAN EXPORTS POINT THE WAY SOUTH



Seasonal trends in the Caixin PMI recently haven't been as pronounced as in the past, as our first chart below crudely shows. *But Januaries have tended to be quieter in recent years; previously, the index tended to rise in the early part of the year.* Last month's fall could be reflecting the weakness of some of the forward-looking indicators ahead of the Chinese New Year break this month. The long holiday, which can sometimes start in late January, will fall fully within February this year, meaning far fewer working days, on average. **As always, we take Q1 Chinese data with a pinch of salt, given the holiday noise.**

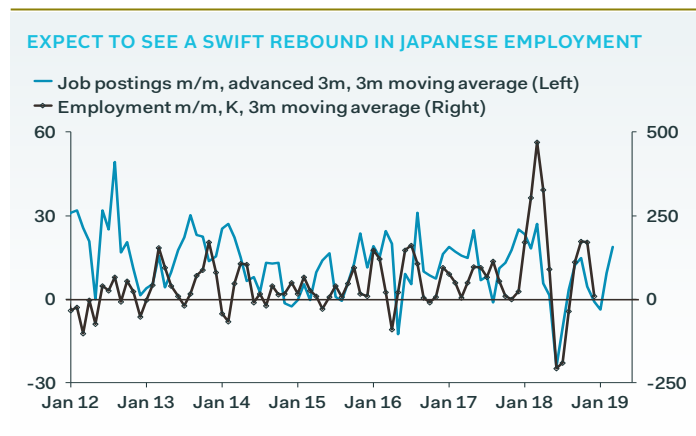
M1 growth gives a decent three-quarter lead on the Caixin index. And so the January in the index plunge, while affected by noise, doesn't look out of kilter with the sharp slowdown in M1 growth in the first half of last year. More recent trends in M1 growth, including household deposits, suggest that the PMI is unlikely to fall much further from here. But the index looks set to stay subdued and deep in contraction into Q3.



Don't focus on the dip in Japanese unemployment

Japan's jobless rate ticked down, surprisingly, to 2.4% in December, from 2.5% in November. We aren't particularly impressed with the improvement, however, as the number of unemployed workers was due a correction after two months of sharp increases. And the unemployment rate barely rounds down to 2.4%, even with this sharp monthly fall in absolute numbers. Indeed, the size of the labour force dropped markedly month-on-month in December, while the participation rate ticked down.

The number of workers employed tanked by 450K, after rising by 250K in November, as predicted by previous trends in job postings; see our chart below. Encouragingly, though, the notable surge in postings in the last two months of 2018 augurs well for labour market activity in the current quarter. The only reason the jobs-to-applicants ratio held steady in December was because of another hefty increase in the number of applicants. Admittedly, hiring activity looks set to soften in Q2, based on the weak signals from January's flash manufacturing PMI survey, though it still is too early to tell. *Overall, while Japan's labour market remains historically tight, it is clear from the past six months worth of data that a further tightening is highly unlikely.*



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THIS WEEK IN BRIEF

Data and events covered in the Asian Data Wrap.

Monday, February 4

• **Japan: Monetary Base (1) 08:50 JST**

Monetary base growth likely slowed further, to **4.4%** y/y in January, from 4.8% in December. The BoJ's JGB holdings rose slightly last month, after it reduced them in December, amid the sharp drop in yields. We see only a small window, in Q2, for the BoJ to consider July-like policy tweaks. **Consensus: 4.6%**.

Tuesday, February 5

• **Japan: PMI Services (1) 09:30 JST**

The PMI probably rebounded marginally in January, to **51.3**, after falling sharply to 51.0 in December. The January survey will give the first real read on the service sector, as the indices in Q4 were distorted by catch-up activity. **Consensus: N/A.**

Wednesday, February 6

• **No major data released.**

Thursday, February 7

• **No major data released.**

Friday, February 8

• **Japan: Current Account Balance (12) 08:50 JST**

The unadjusted surplus likely continued to fall in December, to **¥602B**, from ¥757B in November. The trade balance likely returned to the black, on a balance of payments basis, but it will be offset by a seasonal drop in the primary surplus. **Consensus: ¥459B.**

• **Japan: Labour Cash Earnings (12) 09:00 JST**

Regular wage growth probably inched down to **1.5%** y/y in December, from 1.7% in November. Workers should have received generous end-year bonuses. But the y/y lift from this won't be as strong as the mid-year bonus bump, which benefited from a very favourable base. **Consensus: 1.7%.**

February 10-to-15

• **China: M2 (1)**

M2 growth probably edged down to **7.9%** y/y in January, from 8.1% in December, due in part to more adverse base effects. Growth should start to pick-up from February, though, as the PBoC's easing measures feed further through. An outright rate cut this year remains on the cards. **Consensus: 8.2%.**

CHINA ECONOMIC FORECASTS

GDP	q/q			y/y	
	Official	PM est.		Official	PM est.
Q3 2017	1.8%	1.9%	2015	6.8%	5.4%
Q4 2017	1.6%	1.6%	2016	6.8%	7.9%
Q1 2018	1.4%	1.6%	2017	6.8%	7.4%
Q2 2018	1.8%	2.0%	2018	6.4%	5.6%
Q3 2018	1.6%	0.9%	2019	6.1%	4.1%
Q4 2018	1.4%	0.9%			

	CPI, y/y		PPI, y/y
	Headline	Core	Headline
Dec-18	1.9%	1.8%	0.9%
Mar-18	2.1%	1.5%	0.8%
Jun-18	2.7%	1.5%	0.9%
Sep-19	1.7%	1.4%	0.7%

JAPAN ECONOMIC FORECASTS

GDP	q/q	CPI	Headline	Core*
Q1 2018	-0.3%	Dec-18	0.3%	0.1%
Q2 2018	0.8%	Mar-18	0.0%	0.2%
Q3 2018	-0.6%	Jun-18	0.1%	0.2%
Q4 2018	0.6%	Sep-19	0.0%	0.3%

*Excluding food and energy

KOREA ECONOMIC FORECASTS

GDP	q/q	CPI	Headline	Core
Q1 2018	1.0%	Sep-18	2.1%	1.4%
Q2 2018	0.6%	Dec-18	1.3%	1.3%
Q3 2018	0.6%	Mar-18	1.5%	1.4%
Q4 2018	1.0%	Jun-19	1.4%	1.4%

ASIAN YIELDS

		Dec	Mar	Jun	Sep
10-year, %	China	3.31	3.30	3.36	3.40
	Japan	0.03	0.10	0.20	0.20
	Korea	1.94	2.04	2.14	2.24

ASIAN MONETARY POLICY FORECASTS

China Two more RRR cuts this year, and 10bp cut to the 7-day reverse repo rate, and corridor in Q1.

Japan Further dilution of the 2% inflation target; further "tweaks" to allow rates to drift above the current 10-year target ceiling of 0.2%; balance rate lifted to 0.0%, from -0.1% in Q2 still on the table

Korea 7-day repo rate on hold at 1.75% through 2019.