Mizuho China Weekly

Economics & Strategy | Asia ex-Japan

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China Weekly Outlook

Divergence Remains the Theme

Judging by the latest PMI releases, divergence remains the defining theme of China’s economy.

The official **Manufacturing PMI** eased to 50.0 in May, pointing to muted growth from April as weakness in new orders weighed on the sentiment. Beneath the headline, however, sector performance remained highly uneven.

By industry, high-tech and equipment manufacturing continued to outperform, with PMIs rising to 52.9 and 52.1, respectively, marking the strongest readings since 2024 and 2023. In contrast, consumer goods and basic raw materials lagged, with both sectors slipping back below the expansion threshold of 50.

Divergence was also evident across firm sizes. Large manufacturers remained resilient, with PMI readings holding above 51, while small and medium-sized ones fell back into contraction territory. This likely reflects SMEs’ greater exposure to rising input costs and margin compression.

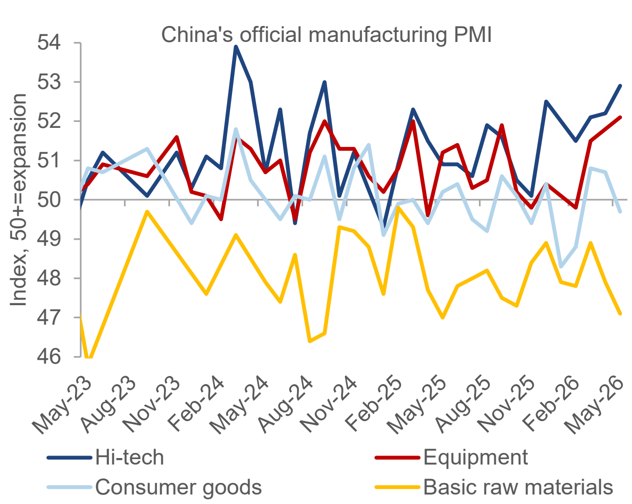
Meanwhile, **non-manufacturing** activity surprised to the upside, defying expectations of moderation as the PMI edged up to 50.1 in May. The services PMI climbed to a nine-month high of 50.3, supported by stronger sentiment in sectors such as rail transportation, telecom services, as well as insurance. Although the construction PMI came in at 48.8, it rebounded meaningfully from April’s trough, suggesting eased contraction.

Further Margin Compression

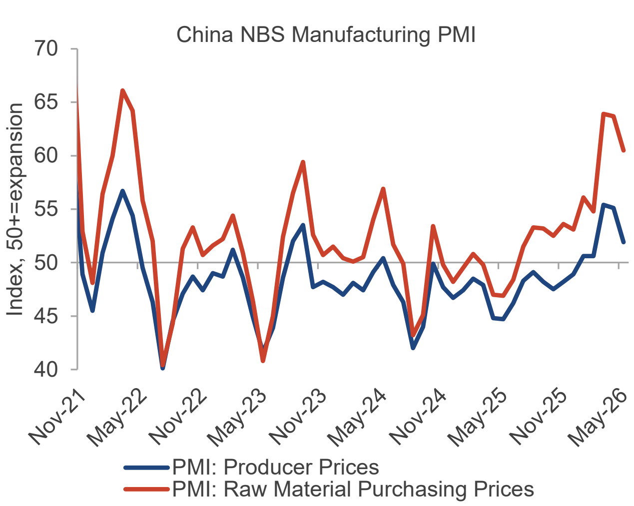
On **the inflation front**, PMI gauges for both raw material costs and producer prices moderated from recent highs, although remained in the expansion territory for a fifth consecutive month. Importantly, the gap between the two indices stayed near a four-year wide, underscoring manufacturers’ ongoing difficulty in passing higher input costs downstream amid persistent oil supply disruptions and still-weak domestic demand.

Against this backdrop, we expect the PBoC to maintain a wait-and-see stance for more significant easing measures for now, unless there are clearer signs of an escalation in Middle East tensions and fading prospects for a near-term US-Iran peace agreement.

< Uneven industrial performance in the manufacturing sector >



< Wider gap between raw material costs and producer prices >



Source: CEIC, Mizuho

CNH Outlook

Weekly Price Change#	Week Open	Week High	Week Low	Week Close	Weekly Change*
USD/CNH	6.7942	6.7948	6.7605	6.7635	-348
USD/CNY	6.7842	6.7884	6.7662	6.7663	-300
CNY PBoC Fixing	6.8318	6.8318	6.8176	6.8176	-197
Shanghai Composite Index	4126.34	4153.88	4055.83	4068.57	-44.33

#Last week, from Monday to Friday
*pips in USD/CNY,USD/CNH row

Weekly Price Change#	HK Close	Weekly Change		HK Close	Weekly Change
CNH Forward (1yr)	-1701	19	CNH HIBOR (3mth)	1.559	-0.019
CNH Currency Swap (3yr)	1.275	-0.025	CNH Implied yield (1Y)	1.249	-0.065

Recap

The offshore renminbi (CNH) strengthened against the US dollar throughout the week, ending just shy of the 6.76 level. The move was supported by hopes of a US-Iran peace agreement, which should help contain inflation expectations and UST rates. This came against the backdrop of a marginally softer US dollar, which declined by around 0.3%, as well as continued PBoC efforts to lean against one-way appreciation expectations in the renminbi.

In fact, both CNH and the onshore renminbi (CNY) have appreciated by more than 1.4% against the dollar since the US/Israel strikes, standing out as the only Asian currency that did not weaken in response to heightened geopolitical risks and oil supply shocks. Even the Hong Kong dollar weakened by 0.2% over the same period. This reinforces the view that the renminbi is increasingly being perceived as a relative safe-haven asset during periods of external uncertainty. Notably, the PBoC has been pushing back against excessive RMB strength since April, setting the daily fixing in May at around 0.6% weaker than levels implied by the CFETS model.

Outlook

Looking ahead, headlines around US-Iran developments are likely to remain a key driver of market sentiment in the coming weeks. However, as markets have increasingly priced in a peace deal, the renminbi may become more vulnerable to widening US-China rate differentials.

While a US rate hike does not appear to be an immediate risk, Chinese government bond yields have continued to move lower across the curve amid signs of softer domestic activity (Fig. 19 & 20). Against this backdrop, **we expect USD/CNH to remain largely range-bound between 6.75 and 6.80 this week**.

Further out, we expect underlying demand for renminbi-denominated assets to continue improving over the medium term. Key supportive factors include elevated policy uncertainty from the White House and US Fed. At the same time, the PBoC's continued efforts to smooth excessive FX volatility suggest that the current appreciation cycle may proceed at a measured pace, but with greater durability. **We therefore maintain our view of modest RMB appreciation and continue to forecast USD/CNH at 6.65 by year-end**, implying full-year gains of nearly 5%.

<FX Charts on Page 8>

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Activity monitor (1/2)

Fig 1 Thermal coal: upbeat sentiment amid oil supply disruptions

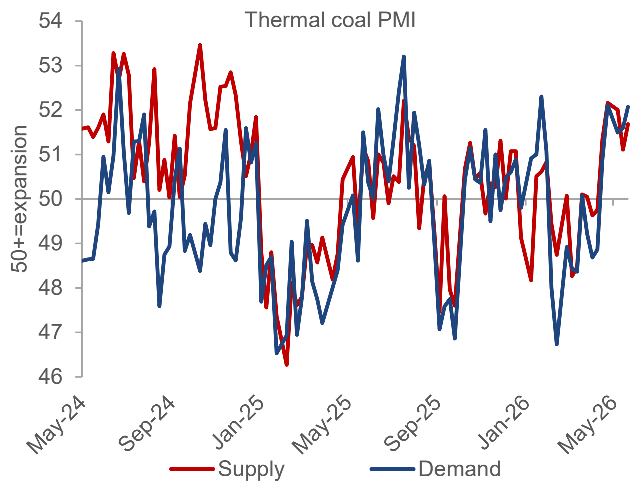
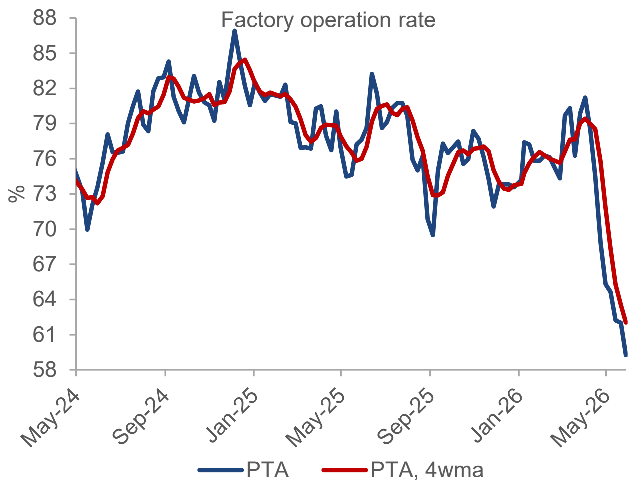


Fig 2 PTA production dropped to its lowest level since 2015



Source: Wind, Mizuho

Fig 3 Steel production: the YoY decline has turned muted in May

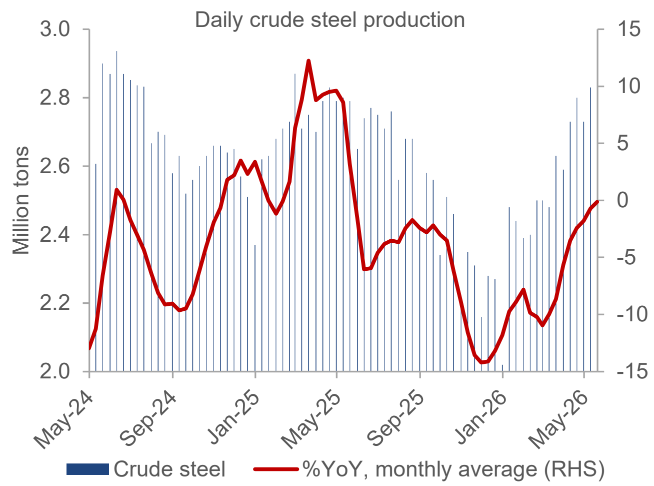
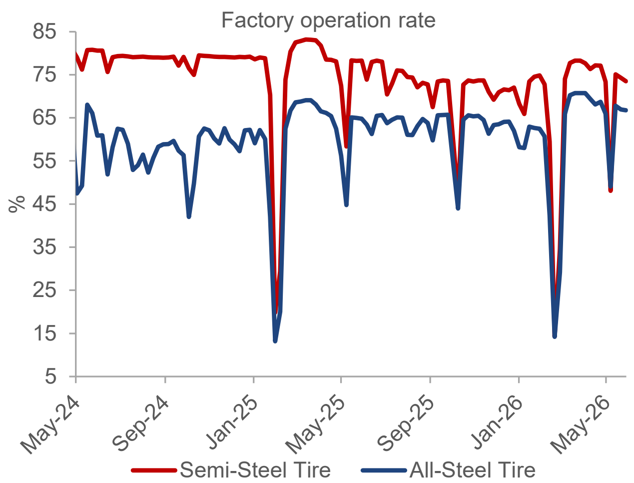


Fig 4 Steel tire production stayed relatively supported



Source: Wind, Mizuho

Fig 5 CCFI: prices for outward shipments continued to climb

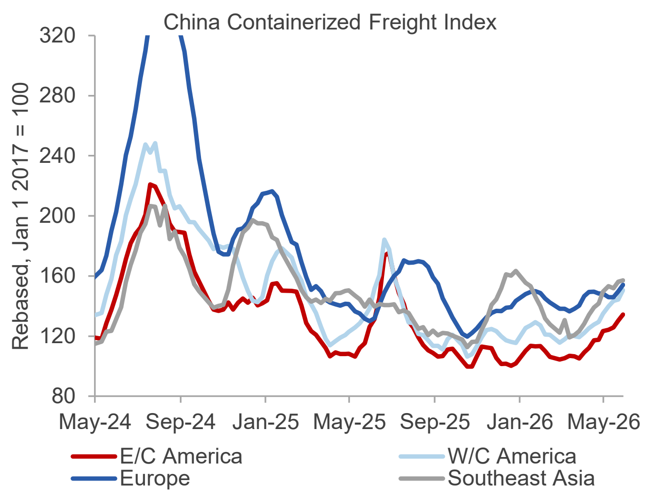
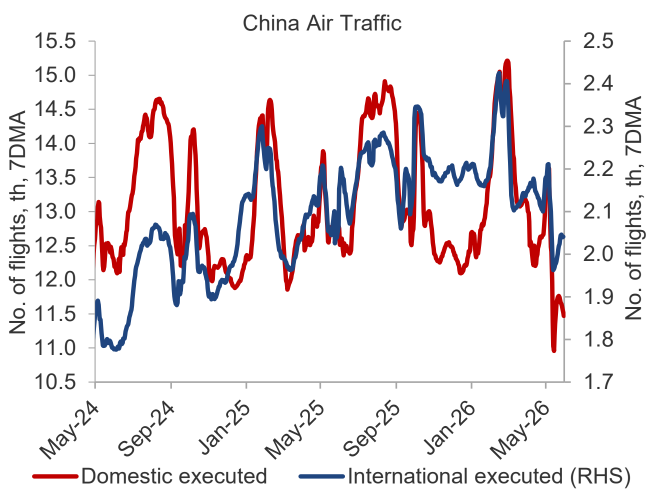


Fig 6 Air traffic: domestic travel dropped notably amid higher fuel prices



Source: Wind, Mizuho

Activity monitor (2/2)

Fig 7 Road construction activity dipped on supply disruptions

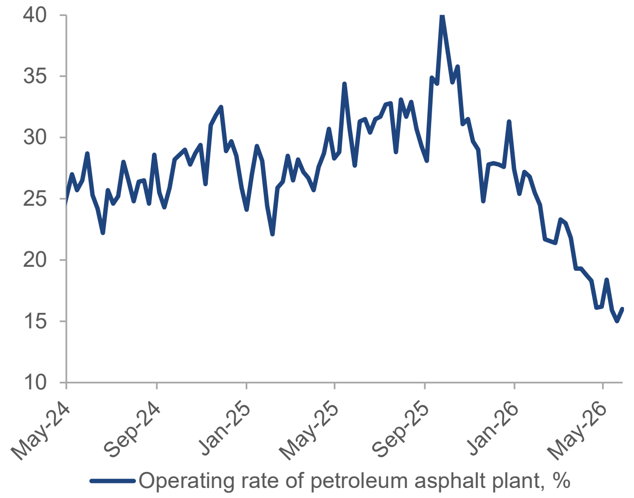


Fig 8 Construction material prices: rebar prices softened recently

Source: Wind, Mizuho

Fig 9 Land sales saw persistent YoY declines

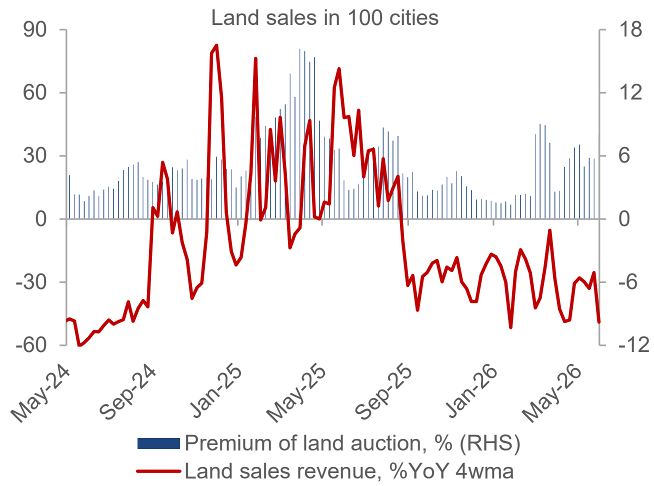
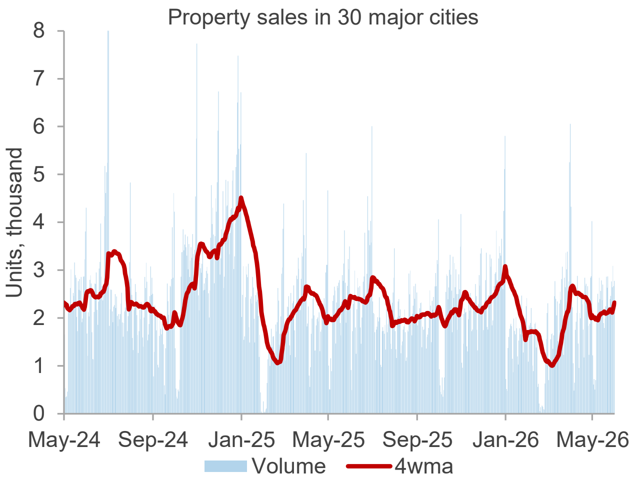


Fig 10 New home sales: a lack of pickup at the national level



Source: Wind, Mizuho

Fig 11 Movie box office revenue slightly improved in May

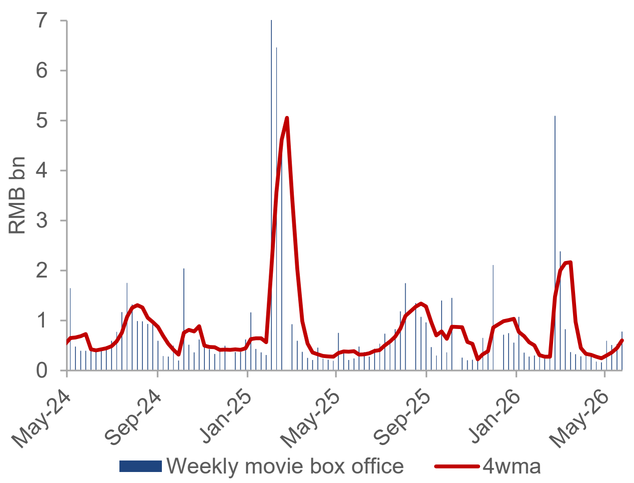
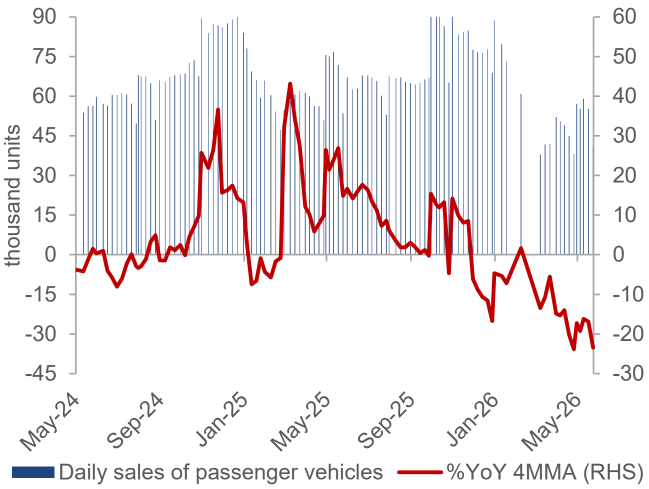


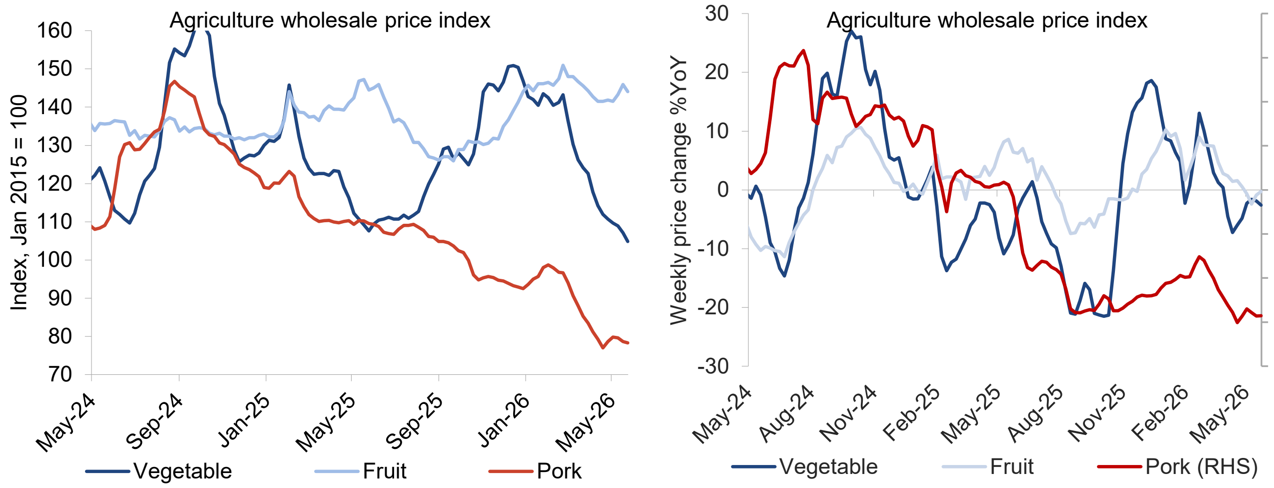
Fig 12 PV sales: April saw the fastest decline since 2023



Source: Wind, Mizuho

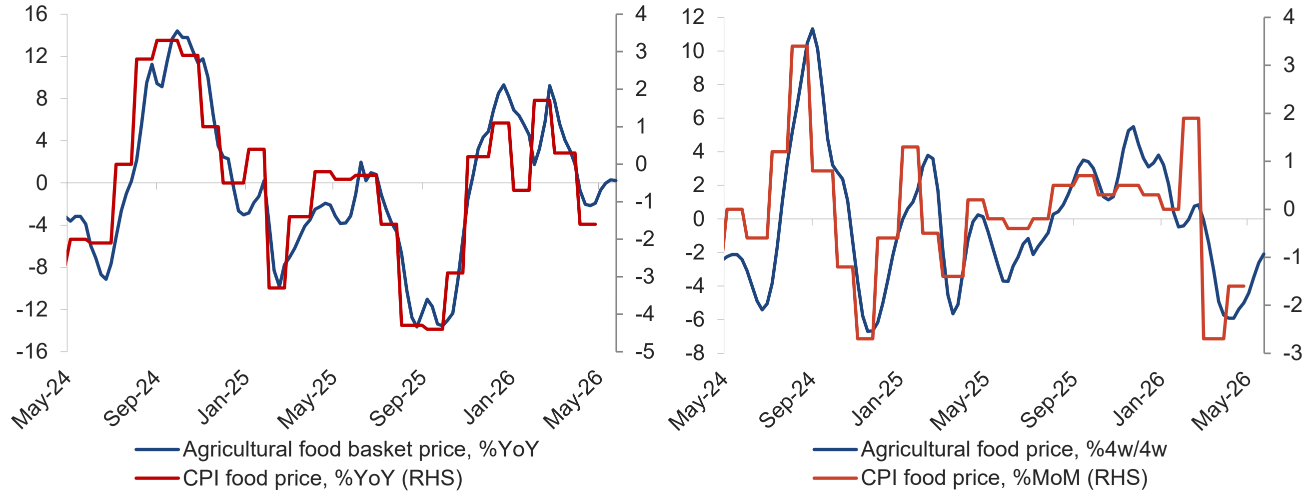
Price monitor

Fig 13 Major food items: pork prices stay around their lowest level in ten years



Source: Wind, Mizuho

Fig 14 Wholesale food prices decreased at a slower pace in May



Source: CEIC, Mizuho

Fig 15 Non-ferrous metal prices remain relatively elevated

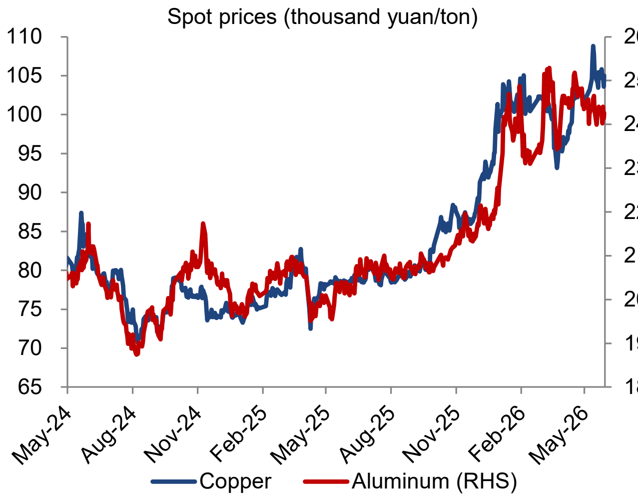
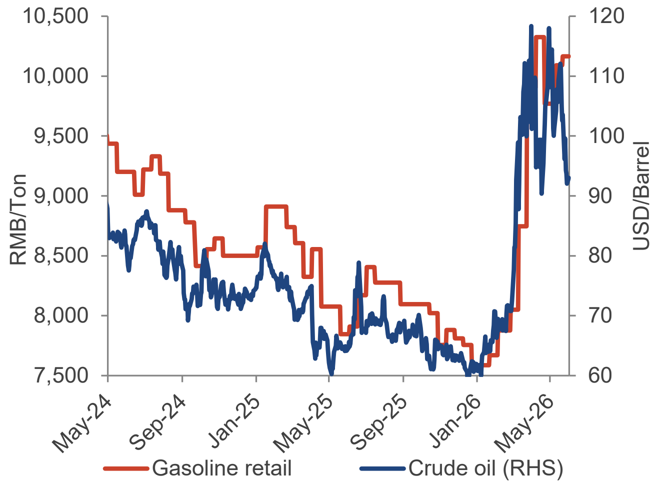


Fig 16 Oil prices: crude oil prices softened on prospects of a peace deal



Source: CEIC, Wind, Mizuho

Liquidity monitor

Fig 17 OMOs: net injection of RMB605b during 25 - 29 May

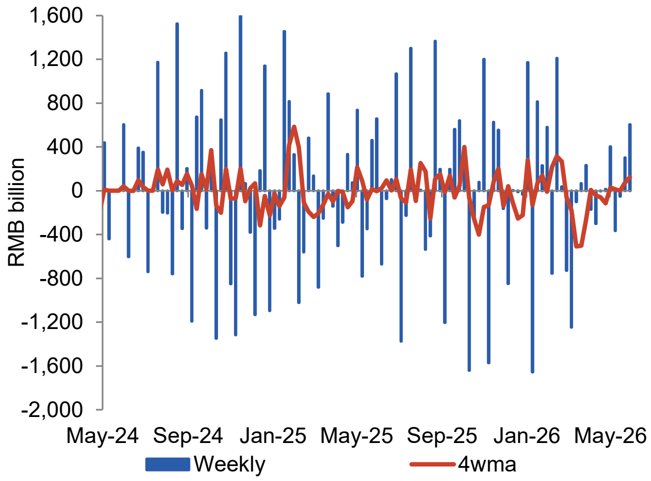
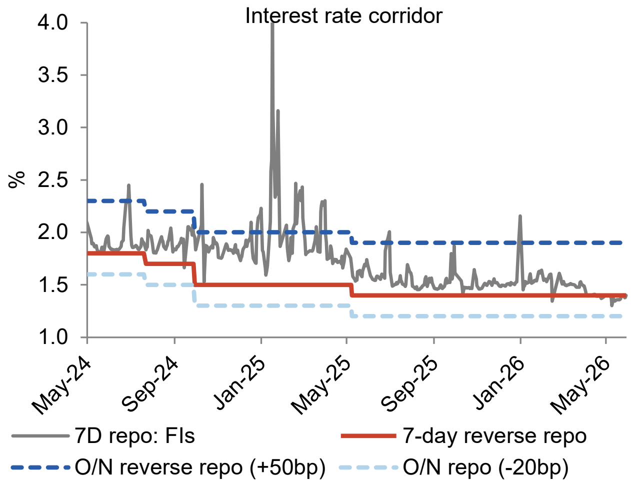


Fig 18 7D repo for FIs stayed close to the target level



Source: CEIC, Wind, Mizuho

Fig 19 Short-end CGB yields moved lower across maturities

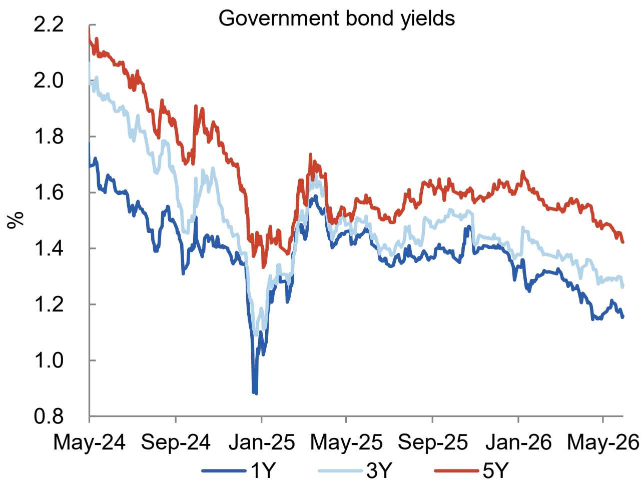
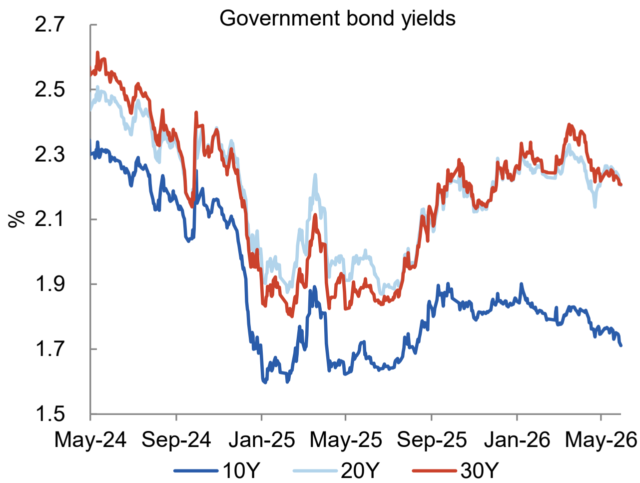
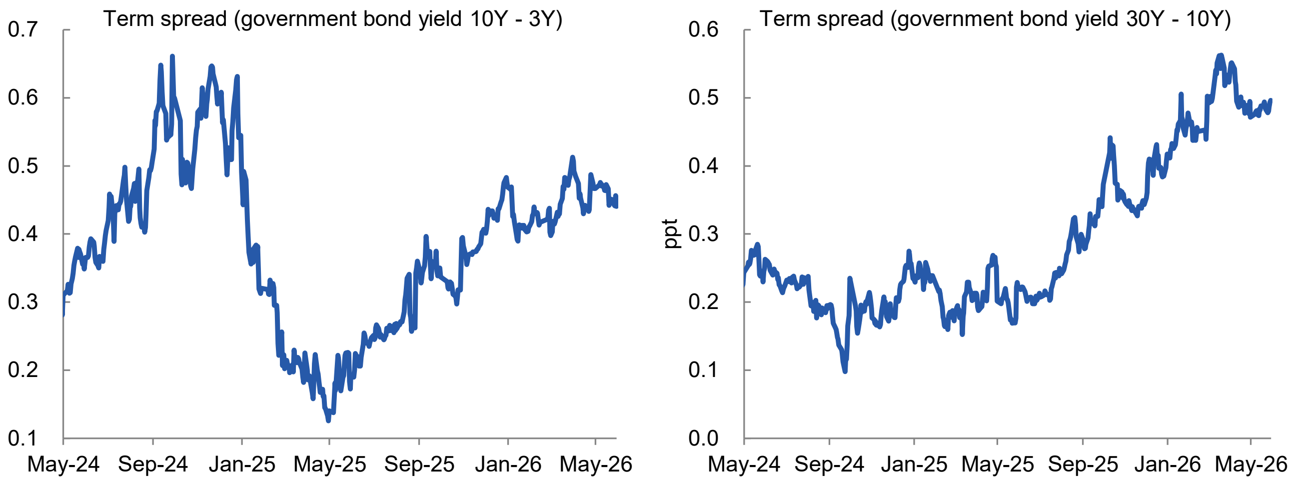


Fig 20 Long-end CGB yields also edged lower last week



Source: CEIC, Mizuho

Fig 21 CGB term spreads: tightened across the yield curve in recent weeks



Source: CEIC, Mizuho

Credit monitor

Fig 22 Onshore IG credit yields fell across maturities

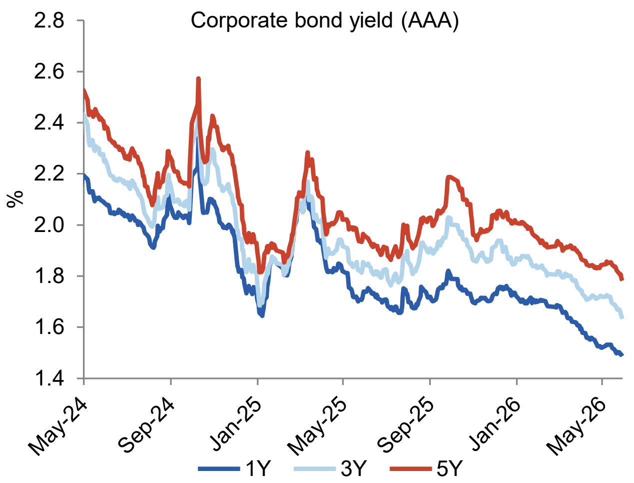
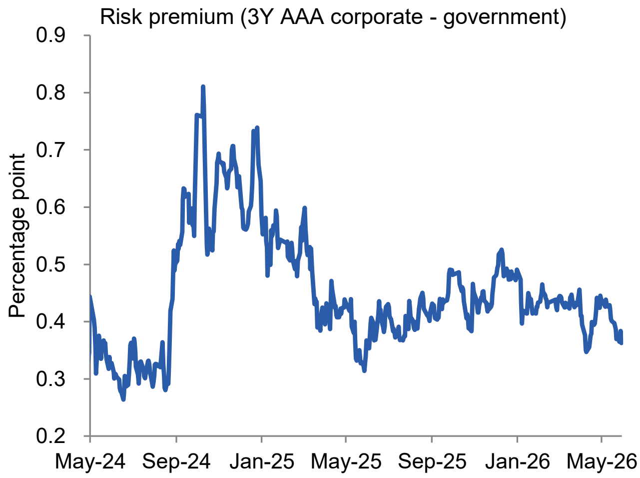


Fig 23 IG corporate risk premium gapped tighter



Source: Wind, Mizuho

Fig 24 Onshore HY credit yields continued to edge lower

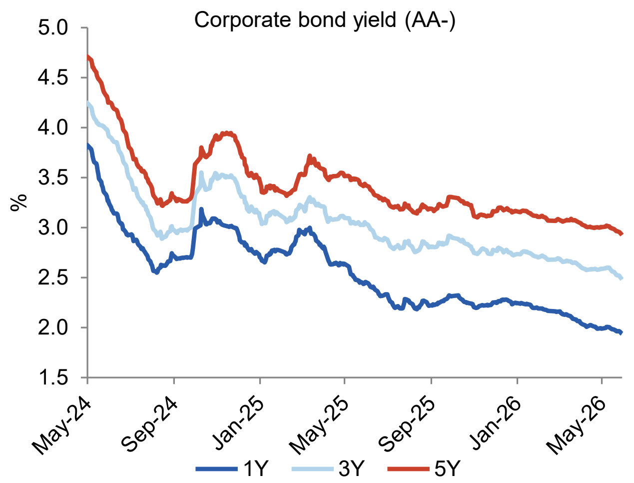
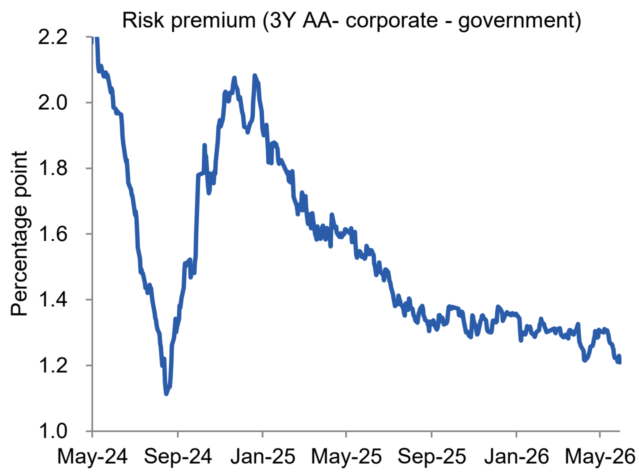
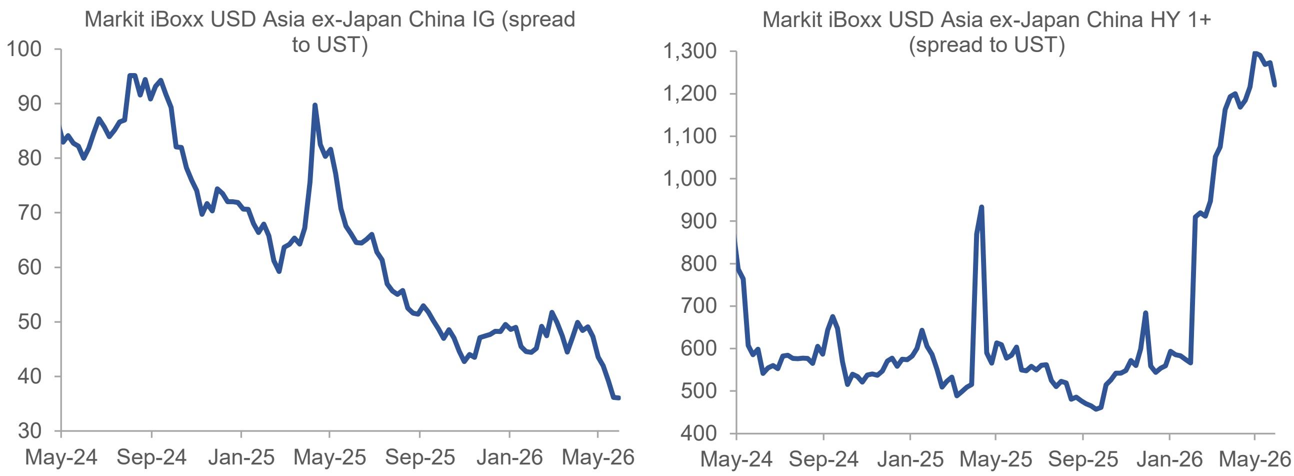


Fig 25 HY corporate risk premium tightened further



Source: Wind, Mizuho

Fig 26 China USD credit spreads squeezed mostly tighter last week helped by ongoing hopes for a US/Iran peace deal



Source: IHS Markit, Mizuho

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FX monitor

Fig 27 RMB fixing rate: the PBoC leans against yuan strength

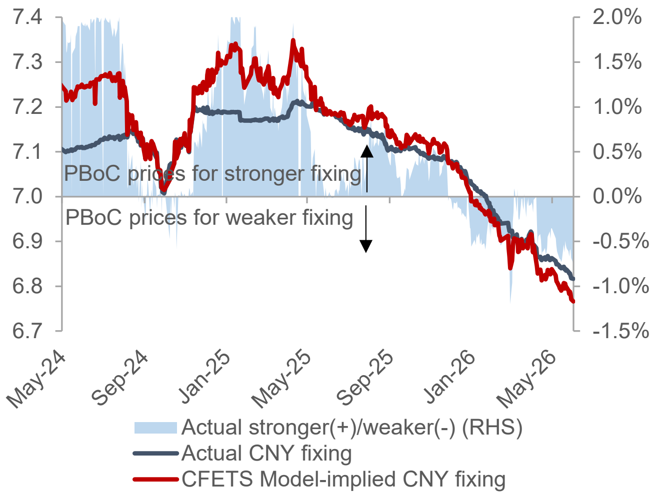
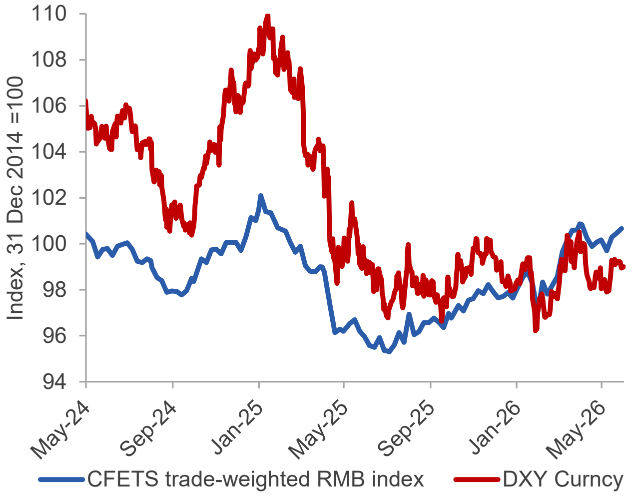
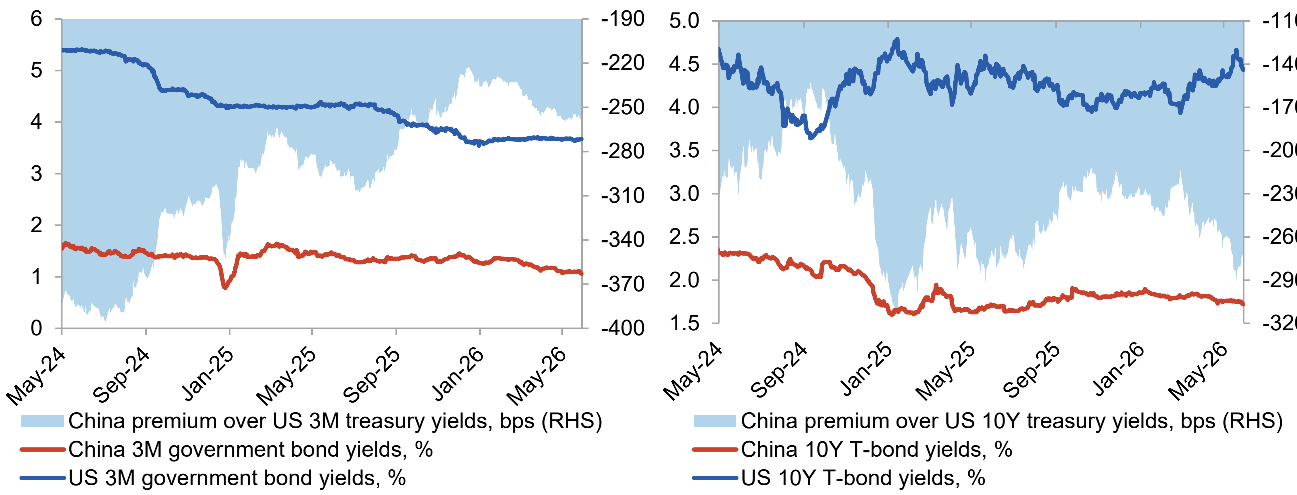


Fig 28 RMB trade-weighted index remains relatively supported



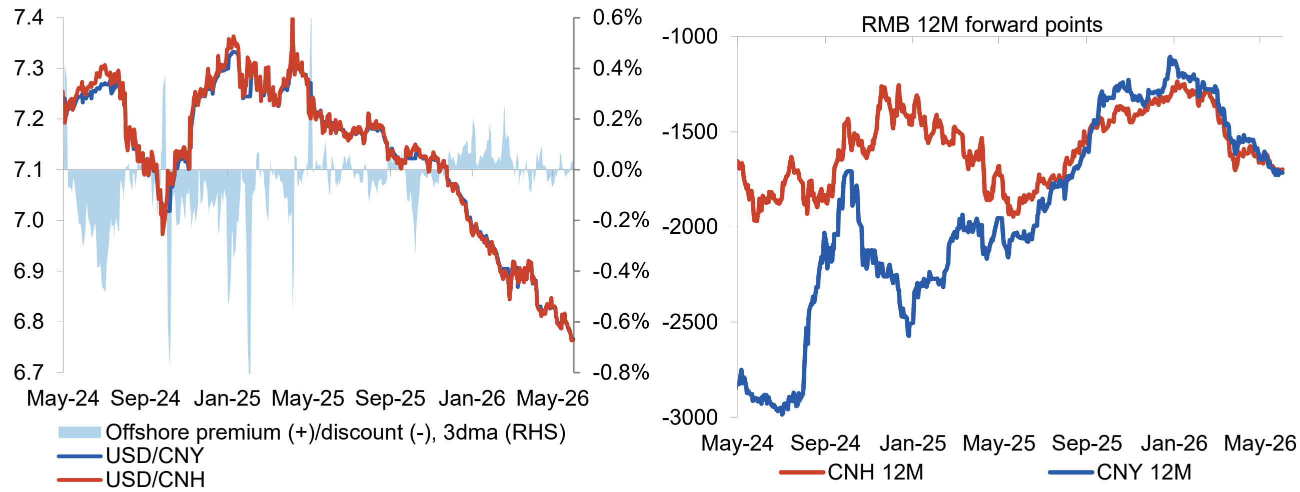
Source: CEIC, Bloomberg, Mizuho

Fig 29 China-US interest rate spreads have moved wider, especially at the back end



Source: CEIC, Bloomberg, Mizuho

Fig 30 Offshore RMB (CNH) is trading almost on par to the CNY amid broadening cross-border flows



Source: Bloomberg, Mizuho

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