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Domestic Trade

Retail sales of consumer goods gain 10.4% yoy in January to April.

Purchaser price index drops in April.

NPC sets the 2015 growth target at 7%.

Confidence among secondary industry entrepreneurs improves.

PMI stays in the expansionary zone in March and April.

Foreign Trade

Both exports and imports post negative year-on-year growth in April.

Foreign exchange reserves fall for the third consecutive quarter.

Total value of deals signed at the 117th Canton Fair drops 3.8% from the previous session.

Import tariffs on some consumer products reduced by more than half.

Global merchandise trade posts low single-digit growth in 2014.

China issues an action plan for the 'One Belt One Road' Initiative.

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Executive Summary

Domestic Trade

Retail sales of consumer goods reached 9,310.2 billion yuan over the period January to April 2015, up nominally by 10.4% yoy. By product category, sales of 'telecommunications equipment' achieved the fastest growth (37.2% yoy), boosted by the strong demand for smartphones.

Purchaser price index dropped by 1.3%, 1.0%, 0.3% and 0.2% in January, February, March and April respectively, indicating that the domestic prices of production inputs have fallen at a slower pace lately.

Macroeconomic targets set for 2015. During the third session of the 12th National People's Congress, the government set a lower real GDP growth target of 7% for 2015. This shows that the Chinese leaders are willing to tolerate a moderation in economic growth, as long as employment and social stability are not undermined.

Confidence among entrepreneurs in the secondary industry has improved. The Entrepreneur Confidence Index for the industry picked up to a three-quarter high of 120.6 in 1Q15.

PMI stayed in the expansionary zone in March and April, suggesting growth stabilization of the Chinese economy.

Foreign Trade

Both exports and imports posted negative yoy growth in April. Exports fell by 6.4% yoy in April, while imports recorded a sharper drop of 16.2% yoy in the same month, posting negative yoy growth for the sixth month in a row.

Exports to the US, the EU and ASEAN gained 11.3% yoy, 2.5% yoy and 20.6% yoy respectively in 1Q15. In contrast, exports to Japan registered negative growth of minus 11.8% yoy over the same period, indicating the weak demand for Chinese products from Japan.

Foreign exchange reserves fell for the third consecutive quarter. China's foreign exchange reserves decreased by US$ 113.0 billion in 1Q15, amounting to US$ 3.73 trillion as at the end of 1Q15.

Total value of deals signed at the 117th Canton Fair fell 3.8% from the previous session. The number of buyers from Europe dropped sharply by 17.9%, while the number of buyers from Asia, the Americas, Oceania and Africa rose by 2.8%, 6.0%, 8.5% and 2.9%, respectively, from the previous session.

Global merchandise trade posted low single-digit growth in 2014, according to the WTO. China has continued to be the world's largest merchandise exporter, followed by the US and Germany.

State Council announced to reduce the import tariffs on various types of consumer products, effective from 1 June. For example, the tax rates for imports of suits and fur clothes will be reduced to 7-10% from 14-23%, while those for short boots and sports shoes will be adjusted downward from 22-24% to 12%.

China issued an action plan for the 'One Belt One Road' Initiative on 28 March. According to the Initiative, China is going to negotiate with countries and regions along the Belt and Road to establish more free trade areas, lower non-tariff barriers and jointly improve the transparency of technical trade measures. China will also cooperate with those countries to improve road, port and aviation infrastructure. We believe that these actions will greatly liberalize and facilitate trade, which will in turn benefit Chinese exporters and importers.

A Recent developments

1 China's economic growth moderates to the lowest level in six years

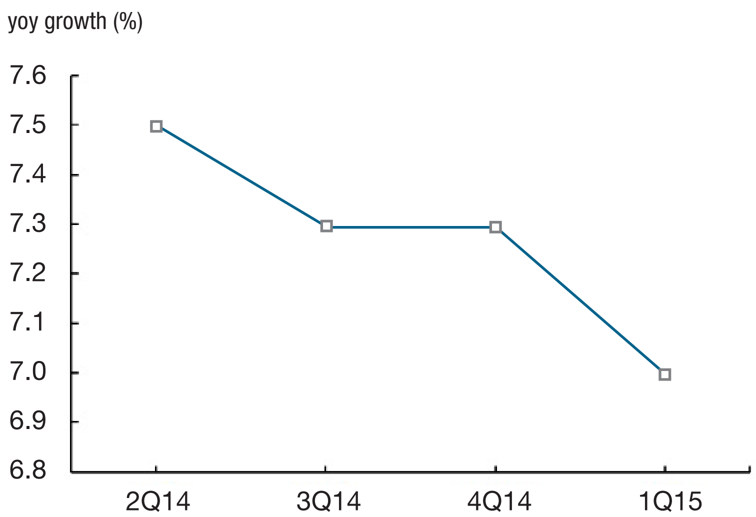
According to the National Bureau of Statistics, China's real GDP growth moderated from 7.3% year-on-year (yoy) in 4Q14 to 7.0% yoy in 1Q15, the lowest level since 2Q09 (see exhibit 1). On a quarter-on-quarter (qoq) basis, the growth of seasonally-adjusted real GDP fell from 1.5% in 4Q14 to 1.3% in 1Q15, indicating growth deceleration in the Chinese economy. Overall, in 1Q15, China's nominal GDP amounted to 14.1 trillion yuan.

The tertiary sector has continued to grow faster than the secondary sector. The value-added of the tertiary industry, which contributed 51.6% of China's nominal GDP in 1Q15, gained 7.9% yoy in real terms in 1Q15. In comparison, the value-added of the secondary industry, which contributed 42.9% of the country's nominal GDP, increased 6.4% yoy in real terms over the same period.

In our view, the latest set of GDP data indicates that the growth momentum of the economy has continued to weaken. In recent months, the government has introduced more pro-growth policies. For example, the mortgage polices were further loosened on 30 March. Then, on 8 April, the State Council announced to reduce the power tariffs for commercial and industrial users and to launch a six-month campaign to abolish various types of administrative fees charged to enterprises. Afterwards, on 11 May, China's central bank cut the benchmark interest rates, in a bid to further lower the financing cost. Besides, the government has accelerated the construction of water conservancy infrastructure recently.

Looking ahead, through better coordinated use of monetary policy, fiscal policy and other policy tools, we expect the government to step up efforts to support growth. On the monetary front, we expect to see further interest rate cuts and required reserve ratio (RRR) cuts this year. On the fiscal front, the government has announced to continue to carry out structural tax cuts; and we also expect the government to launch infrastructure projects related to the One Belt One Road Initiative in near future. With the pro-growth policies starting to take effect, we forecast a slight rebound in growth to around 7.1-7.2% yoy in 2Q15 from 7.0% yoy in 1Q15.

Exhibit 1 China's real GDP growth, 2Q14 to 1Q15



FY14	7.4%
2Q14	7.5%
3Q14	7.3%
4Q14	7.3%
1Q15	7.0%

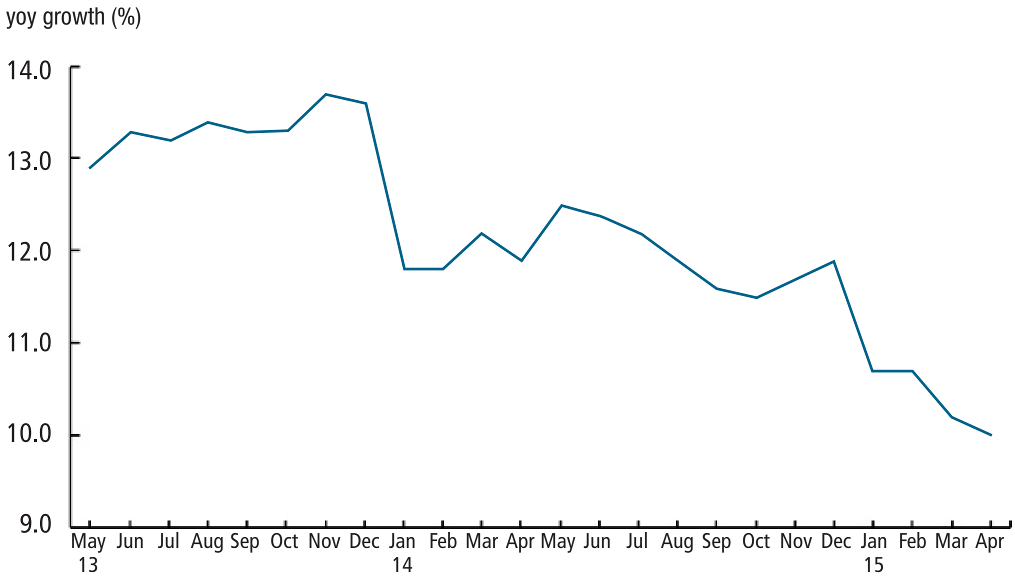
Source: National Bureau of Statistics, PRC

2 Growth of retail sales slows

According to the National Bureau of Statistics, the growth of China's total retail sales slowed from a four-month high of 11.9% yoy in December to 10.7% yoy in January to February 2015, and further to 10.2% yoy in March and 10.0% yoy in April. On a month-on-month (mom) basis, the growth of seasonally-adjusted retail sales fell from 0.99% in February to 0.64% in March, and then remained low at 0.74% in April. These figures confirm that the consumption demand in China has remained sluggish.

Overall, over the period January to April 2015, the total retail sales of consumer goods reached 9,310.2 billion yuan. The nominal growth rate was 10.4% yoy over the period January to April 2015, compared to the 12.0% yoy growth seen in FY14 (see exhibits 2 and 3).

Exhibit 2 China's total retail sales, year-on-year nominal growth, May 2013 to April 2015



FY14	12.0
May 14	12.5
Jun	12.4
Jul	12.2
Aug	11.9
Sep	11.6
Oct	11.5
Nov	11.7
Dec	11.9
Jan-Feb 15	10.7
Mar	10.2
Apr	10.0

Source: National Bureau of Statistics, PRC

Exhibit 3 China's total retail sales, month-on-month nominal growth, November 2014 to April 2015

mom growth (%), seasonally adjusted

	Nov 14	Dec	Jan 15	Feb	Mar	Apr
Total retail sales	0.81	0.90	0.51	0.99	0.64	0.74

Source: National Bureau of Statistics, PRC

Rural retail sales have been growing faster than urban retail sales. Over the period January to April, rural retail sales expanded by 11.5% yoy to 1,304.6 billion yuan, while urban retail sales rose by 10.2% yoy to 8,005.6 billion yuan.

The pace of retail sales growth diverged for different modes of sales: The nominal growth for catering services sales improved from 9.7% yoy in FY14 to 11.4% yoy over the period January to April 2015. On the contrary, the nominal growth for sales of goods decelerated to 10.3% yoy over the period January to April 2015 from 12.2% yoy in FY14.

Retail sales of goods by enterprises above a designated size[1] rose 7.5% yoy to reach 4,045.7 billion yuan over the period January to April 2015. By product category, sales of 'telecommunications equipment' achieved the fastest growth (37.2% yoy), boosted by the strong demand for smartphones. In contrast, sales for 'petroleum and related products' dropped by 7.3% yoy, partly attributed to the fall in fuel prices. The growth in sales for 'clothing, shoes, hats and textiles' came in at 10.6% yoy over the same period, down slightly from the 10.9% yoy growth seen in FY14. Exhibit 5 demonstrates the growth of China's retail sales by product among enterprises above a designated size.

Exhibit 4 China's total retail sales, 2014 to April 2015

Nominal growth, yoy (%)	FY14	1Q15	Apr
Total retail sales	12.0	10.6	10.0
Goods	12.2	10.5	9.8
Sales by enterprises above a designated size	9.8	7.8	6.7
Catering services	9.7	11.3	11.7

Source: National Bureau of Statistics, PRC

3 Chinese consumers are optimistic

The consumer confidence index[2] dropped slightly from 105.8 in December from 105.7 in January, before jumping to 109.8 in February, the highest level since August 2008. The index remained high at 107.1 in March, indicating that Chinese consumers are still optimistic (see exhibit 6).

4 Household income shows high single-digit growth in 1Q15

In 1Q15, the per capita disposable income of households in China amounted to 6,087 yuan, up by 9.4% yoy in nominal terms (or 8.1% yoy real).

Growth of rural household income has outpaced growth of urban household income. In 1Q15, the per capita disposable income of rural households increased nominally by 10.0% yoy (or 8.9% yoy real) to 3,279 yuan; while the per capita disposable income of urban households rose by 8.3% yoy in nominal terms (or 7.0% yoy real) to reach 8,572 yuan.

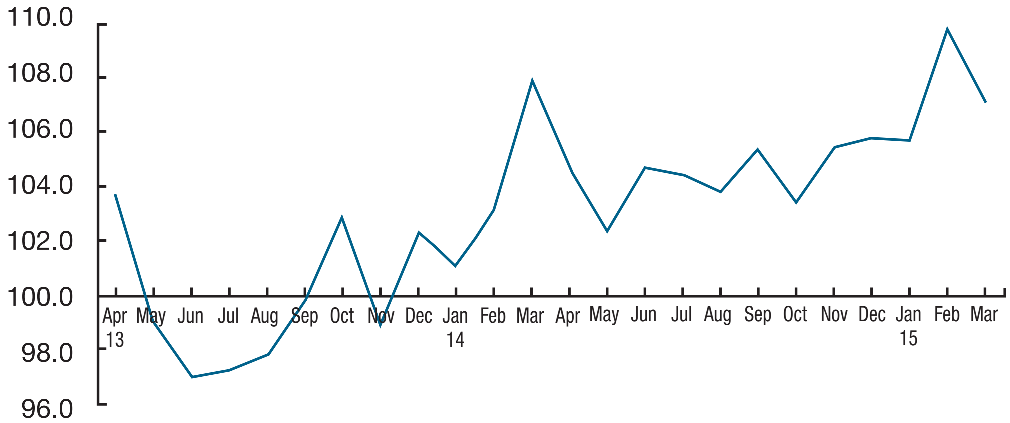
1 'Enterprises above a designated size' refers to enterprises with annual sales of 5 million yuan or more and with an employee strength of 60 or more.
2 A reading above 100 indicates that consumers tend to be optimistic; a reading below 100 indicates that consumers tend to be pessimistic.

Exhibit 5 China's retail sales by enterprises above a designated size, by product, 2014 to April 2015

Nominal growth, yoy (%)	FY14	1Q15	Apr
Grain, oil, food, beverages, tobacco and liquor	11.1	10.8	-
Clothing, shoes, hats and textiles	10.9	10.5	10.9
Cosmetics	10.0	10.1	9.3
Gold, silver and jewellery	0.0	3.6	10.3
Products for daily use	11.6	14.9	11.8
Sports and entertainment products	1.8	8.9	-
Home appliances and video equipment	9.1	13.7	9.5
Chinese and Western medicines	15.0	15.1	14.0
Stationery and office accessories	11.6	14.2	9.0
Furniture	13.9	15.4	16.4
Telecommunications equipment	32.7	38.0	34.9
Petroleum and related products	6.6	-7.2	-7.4
Automobiles	7.7	6.5	1.6
Building and decoration materials	13.9	15.8	18.7

Source: National Bureau of Statistics, PRC

Exhibit 6 China's consumer confidence index, April 2013 to March 2015



Apr 14	104.8
May	102.3
Jun	104.7
Jul	104.4
Aug	103.8
Sep	105.4
Oct	103.4
Nov	105.5
Dec	105.8
Jan 15	105.7
Feb	109.8
Mar	107.1

Source: National Bureau of Statistics, PRC

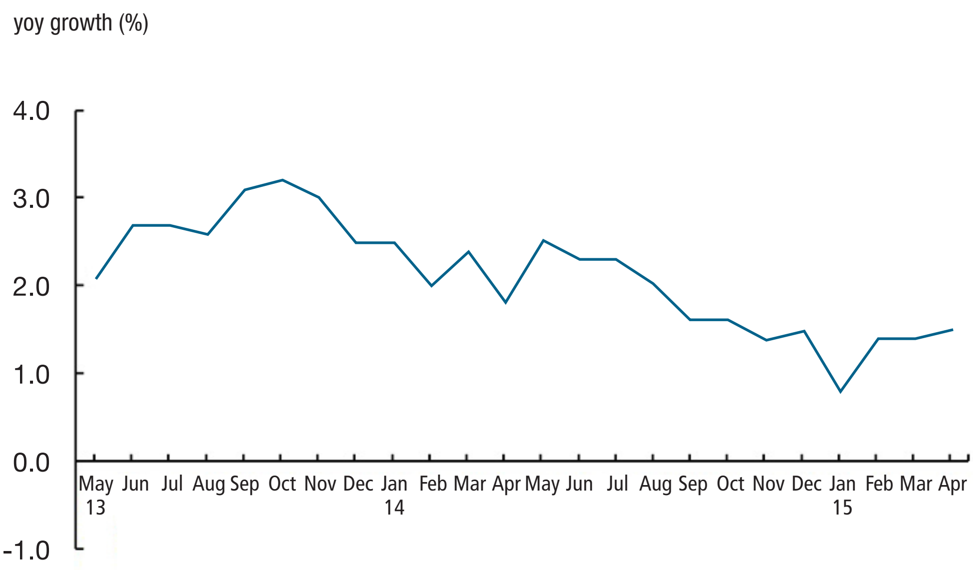
5 CPI growth edges up in April

The year-on-year (yoy) growth rate of China's consumer price index (CPI)[3] fell to 0.8% yoy in January, the lowest level in five years. Afterwards, due partly to the different timing of the Chinese New Year in 2014 and 2015, the CPI growth rebounded to 1.4% yoy in February. The CPI growth then stayed flat at 1.4% yoy in March, before edging up to 1.5% yoy in April.

Food prices have risen faster than non-food prices in recent months. The yoy growth of the food component in the CPI fluctuated between 1.1% and 2.9% during December to April. Meanwhile, the yoy growth of the non-food component in the CPI stayed within the range of 0.6% to 0.9% over the same period (see exhibits 7 and 8).

Looking ahead, we expect the CPI growth to stay low in the near term, due to the weak domestic demand.

Exhibit 7 China's CPI growth, May 2013 to April 2015



May 14	2.5%
Jun	2.3%
Jul	2.3%
Aug	2.0%
Sep	1.6%
Oct	1.6%
Nov	1.4%
Dec	1.5%
Jan 15	0.8%
Feb	1.4%
Mar	1.4%
Apr	1.5%

Source: National Bureau of Statistics, PRC

3 The CPI, compiled by the National Bureau of Statistics of China, measures the price of a basket of goods and services purchased by a typical household.

Exhibit 8 China's CPI growth by commodity, November 2014 to April 2015

yoy growth (%)	Nov 14	Dec	Jan 15	Feb	Mar	Apr
Food	2.3	2.9	1.1	2.4	2.3	2.7
Tobacco and liquor	-0.7	-0.7	-0.4	-0.6	-0.5	-0.5
Clothing	2.6	2.6	2.9	2.9	3.0	2.9
Household services, maintenance and renovation	1.2	1.1	0.9	1.5	1.2	1.1
Medical and healthcare and personal care	1.3	1.5	1.6	1.9	1.6	1.8
Transportation and communication	-0.8	-1.4	-2.2	-1.7	-1.5	-1.6
Recreational, educational products and services	1.0	0.9	0.3	1.8	1.6	1.6
Housing	1.4	1.0	0.8	0.6	0.6	0.6

Source: National Bureau of Statistics, PRC

The yoy growth rate for China's producer price index of industrial products (PPI)[4] fell to minus 4.8% in February, the lowest level since November 2009, and then edged up to minus 4.6% in March and in April (see exhibits 9 & 10).

On a mom basis, the PPI fell by 0.7%, 0.1% and 0.3% in February, March and April respectively, indicating that the ex-factory prices of industrial products have continued to drop.

Going forward, we expect China's PPI to stay low in the near term, given the serious problem of excessive production capacity in various sectors in China.

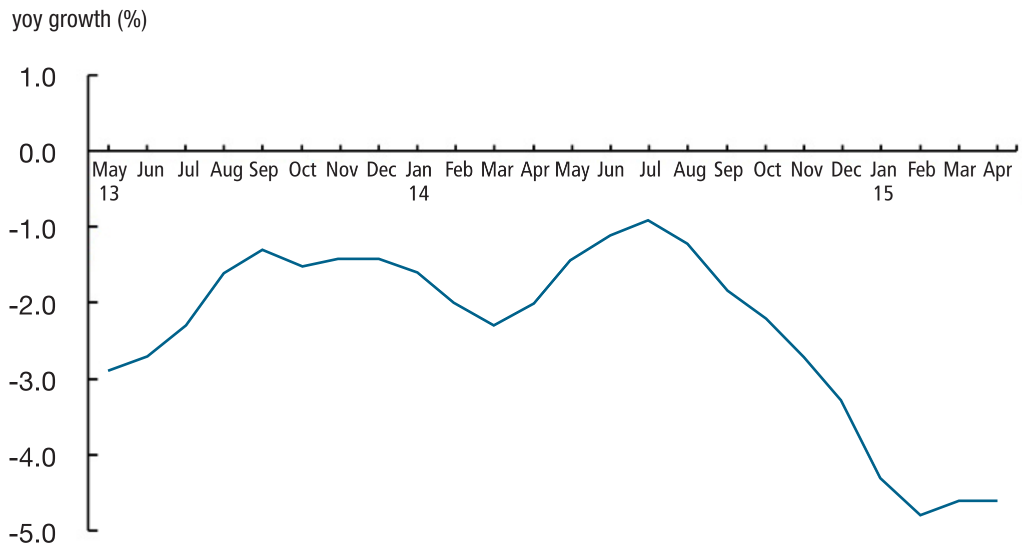
The yoy growth rate of the purchaser price index of industrial products dropped from minus 5.2% in January to minus 5.9% in February, but then rebounded to minus 5.7% in March and minus 5.5% yoy in April (see exhibits 11 & 12).

On a mom basis, the purchaser price index dropped by 1.3%, 1.0%, 0.3% and 0.2% in January, February, March and April respectively, indicating that the domestic prices of production inputs have dropped at a slower pace lately.

The input prices sub-index of China's manufacturing PMI, a leading indicator of upstream prices, came in at 47.8 in April, staying below the critical 50-mark for nine consecutive months. The latest index reading suggests that the domestic prices of production inputs are likely to drop further in the coming months.

4 The PPI, compiled by the National Bureau of Statistics of China, measures the prices of industrial products when they are sold for the first time after production.

Exhibit 9 China's PPI growth, May 2013 to April 2015



May 14	-1.4%
Jun	-1.1%
Jul	-0.9%
Aug	-1.2%
Sep	-1.8%
Oct	-2.2%
Nov	-2.7%
Dec	-3.3%
Jan 15	-4.3%
Feb	-4.8%
Mar	-4.6%
Apr	-4.6%

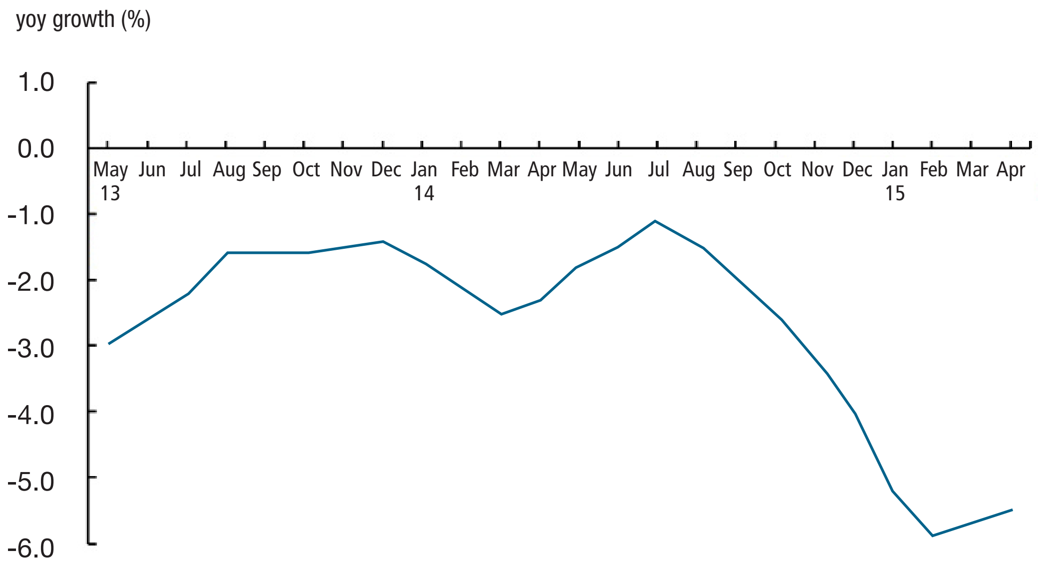
Source: National Bureau of Statistics, PRC

Exhibit 10 China's PPI growth by selected industry, November 2014 to April 2015

yoy growth (%)	Nov 14	Dec	Jan 15	Feb	Mar	Apr
Textile industry	-1.5	-1.7	-2.1	-2.4	-2.5	-2.4
Textile and clothing	0.1	0.2	0.7	0.6	0.9	0.6
Timber processing & wood, bamboo, cane, palm fiber and straw products	0.9	0.8	0.7	0.5	0.6	0.4

Source: National Bureau of Statistics, PRC

Exhibit 11 Growth of China's purchaser price index of industrial products, May 2013 to April 2015



May 14	-1.8%
Jun	-1.5%
Jul	-1.1%
Aug	-1.4%
Sep	-1.9%
Oct	-2.5%
Nov	-3.2%
Dec	-4.0%
Jan 15	-5.2%
Feb	-5.9%
Mar	-5.7%
Apr	-5.5%

Source: National Bureau of Statistics, PRC

Exhibit 12 China's purchaser price index of industrial products by selected commodity, November 2014 to April 2015

yoy growth (%)	Nov 14	Dec	Jan 15	Feb	Mar	Apr
Fuel & power	-5.2	-7.0	-9.9	-12.0	-11.5	-11.2
Non-ferrous metals	-2.5	-2.9	-4.8	-5.7	-4.6	-3.7
Raw materials for the chemical industry	-2.3	-3.7	-5.5	-6.3	-6.0	-5.4
Timber and paper pulp	-0.7	-0.8	-0.7	-0.8	-0.8	-0.8
Textile raw materials	-1.8	-2.1	-2.4	-2.5	-2.5	-2.4

Source: National Bureau of Statistics, PRC

6 Industrial production shows weak growth

China's value-added for industry (industrial production, IP) has posted weak growth in recent months. The IP growth fell all the way from 7.9% yoy in December to 5.6% yoy in March, and then remained low at 5.9% yoy in April (see exhibit 13)[5]. Overall, over the period January to April 2015, China's IP expanded by 6.2% yoy, slower than the 8.3% yoy growth recorded in 2014.

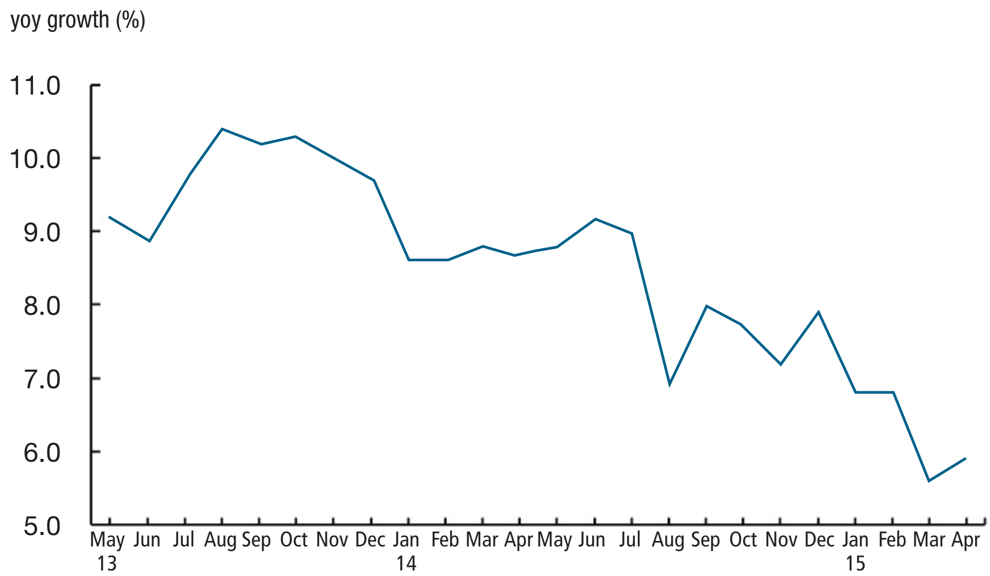
In the coming months, industrial activities will be supported by the positive impact of the accommodative monetary policy and the relaxation of mortgage policies, and the accelerating construction of infrastructure, especially water conservancy infrastructure. Negative factors, however, include the rising labour and environmental costs, intense competition in the international market, foreign protectionism, weaker luxury and housing-related spending, and the overcapacity problem. Overall, we expect the industrial production growth to accelerate to 7-8% yoy in 2Q15 from 6.4% yoy in 1Q15.

7 Industrial profits drop at a slower pace

The total profits earned by large and medium industrial enterprises above a designated size[6] have dropped at a slower pace recently. China's industrial profits fell by 8.0% yoy, 4.2% yoy and 0.4% yoy in December, January-February and March respectively. Overall, in 1Q15, China's industrial profits, which amounted to 1,254.3 billion yuan, posted negative growth of minus 2.7% yoy, compared to the positive growth of 3.3% yoy recorded for 2014 (see exhibit 14).

Profits of upstream industries such as 'coal mining and washing', 'extraction of petroleum and natural gas' and 'mining of ferrous metals' plunged by 61.9% yoy, 71.7% yoy and 49.3% yoy respectively in 1Q15. On the contrary, several high-tech industries such as 'railway, ships, aircrafts, aerospace and other transportation equipment' and 'communications, IT and electronic equipment and instruments' recorded relatively strong growth of 17.8% yoy and 22.9% yoy respectively over the same period. Meanwhile, profits of light industries such as 'garments and clothing accessories' and

Exhibit 13 China's industrial production growth, May 2013 to April 2015



May 14	8.8%
Jun	9.2%
Jul	9.0%
Aug	6.9%
Sep	8.0%
Oct	7.7%
Nov	7.2%
Dec	7.9%
Jan-Feb 15	6.8%
Mar	5.6%
Apr	5.9%

Source: National Bureau of Statistics, PRC

5 The National Bureau of Statistics has changed the method of compiling the value added for industry (industrial production, IP), effective January 2011. The statistical threshold for industrial enterprises has been raised to cover those with annual revenues of 20 million yuan or above, up from the previous threshold of 5 million yuan or above.

6 'Industrial enterprises above a designated size' refers to industrial enterprises with annual sales of 20 million yuan or more.

'furniture' posted double-digit growth of 13.2% yoy and 23.2% yoy respectively in 1Q15.

8 Growth of fixed asset investment decelerates

The growth of China's nominal fixed asset investment (FAI) (excluding rural households) decelerated to 12.0% yoy over the period January to April 2015 from 15.7% yoy in 2014.[7] Overall, over the period January to April 2015, China's nominal FAI (excluding rural households) amounted to 12.0 trillion yuan (see exhibit 15).

The growth of FAI (excluding rural households) for real estate development fell to 6.0% yoy over the period January to April 2015 from 10.5% yoy in 2014, amid the cooling property market in China. Meanwhile, the growth of FAI (excluding rural households) in the secondary industry decelerated to 9.8% yoy over the period January to April 2015, down from the 13.2% yoy growth recorded in 2014. In our view, a major reason for the fall in FAI growth is that the overcapacity problem in various industrial sectors has discouraged manufacturers from making investment.

The investment in several infrastructure-related sectors posted strong growth in the first four months of 2015. For example, the growth of FAI (excluding rural households) in the 'public facilities management' sector rose by 19.9% yoy, and the FAI (excluding rural households) in the 'road transportation' sector gained 21.6% yoy during the period.

Exhibit 14 China's industrial profits growth, September 2014 to March 2015

yoy growth (%)	Sep 14	Oct	Nov	Dec	Jan-Feb 15	Mar
Total profits made by industrial enterprises above a designated size	0.4	-2.1	-4.2	-8.0	-4.2	-0.4

Source: National Bureau of Statistics, PRC

Exhibit 15 China's FAI (excluding rural households) growth, November 2014 to April 2015

	Nov 14	Dec	Jan 15	Feb	Mar	Apr
FAI (excluding rural households) *(year-to-date, yoy growth %)*	15.8	15.7	-	13.9	13.5	12.0
FAI (excluding rural households) *(mom growth %, seasonally adjusted)*	1.03	1.04	0.97	0.92	1.00	0.89

Source: National Bureau of Statistics, PRC

7 The National Bureau of Statistics has expanded coverage of the monthly statistics for FAI from the urban areas to rural enterprises and institutions, effective from 2011. Thus: 'FAI (excluding rural households)', the new indicator, has been released by the bureau as from March 2011 to replace 'urban FAI', the previous indicator. Also, a new statistical criterion has been adopted. The statistical threshold for the size of investment projects has been adjusted upwards from 500,000 yuan to 5 million yuan.

B Highlights

1 State Council vows to improve consumption tax policy on consumer products

On 28 April, presiding at a State Council meeting, Premier Li Keqiang announced several measures to boost domestic consumption.[8] One major measure is to launch a pilot scheme to reduce import tariffs for some popular consumer products. (See *Part 2: Foreign Trade* for more details on the latest policy announced.) In the same announcement, the government also indicated that it would continue to improve its consumption tax policy on consumer products such as cosmetics and accessories. Although the details have not been released yet, it is widely expected that the government will reduce the consumption tax rates on these types of products in coming future.

Due in part to the high consumption tax, value-added tax and import tariffs, prices of some types of imported products are higher in the Chinese mainland than in the overseas markets. It is hoped that the reductions in import tariffs and consumption tax will give domestic retailers more room to reduce prices, thereby stimulating the sales, of the related products.

2 Retail prices for gasoline and diesel have bottomed out since early February

For the first time since July last year, the Chinese government raised the maximum retail prices (including taxes) of gasoline and diesel on 10 February. Afterwards, in response to the price movements of the global crude oil prices, the government further adjusted the maximum retail prices (including taxes) of gasoline and diesel on 28 February, 27 March, 11 April, 25 April and 12 May. Overall, the maximum retail prices (including taxes) for gasoline and diesel have been increased by 15.5-20.2% after these six adjustments.

The rise in fuel prices is set to raise transportation costs, which would in turn put upward pressure on consumer prices. According to the revised pricing mechanism for refined oil adopted since March 2013, fuel prices are adjusted every 10 working days, based on the changes in a basket of global crude oil prices. As the adjustment interval has been shortened to 10 working days from the previous 22 working days and the 4% price change threshold has been removed, we expect the Chinese government to adjust fuel prices more frequently under the new pricing mechanism.

3 Growth of RMB loans accelerates

Growth of broad money supply (M2) came in at 10.1% yoy as at the end of April, down from the growth of 12.2% yoy as at the end of December last year.

Meanwhile, the growth of outstanding RMB loans accelerated to 14.1% yoy as at the end of April, compared to 13.6% yoy at the end of December 2014. The amount of new RMB loans reached 4.38 trillion yuan in January to April 2015, much higher than the same period of the previous year (i.e. 3.78 trillion yuan) (see exhibit 16). We believe that the strong lending figure in the first four months of 2015 was highly associated with the actions taken by the People's Bank of China (PBOC), China's central bank, to inject liquidity and to lower interest rates in the past few months.

The PBOC has continued to take moves to ease the credit conditions in China recently. For example, on 20 April, the central bank lowered the reserve requirement ratios (RRRs) for all depository financial institutions by 1 ppt, marking its second RRRs cut this year. Soon afterwards, on 11 May, the central bank reduced the benchmark interest rates, for the second time this year.

The latest set of economic data indicates that the growth momentum of the economy has remained weak. Looking ahead, the government is likely to step up efforts to support growth, and we expect to see further interest rate cuts and RRR cuts in coming months.

4 'Total social financing' falls

'Total social financing' (covering sources of financing such as RMB loans, foreign currency loans, trust loans, entrusted loans, bank acceptance bills, corporate bonds, equity issuance and other instruments) amounted to 5.65 trillion yuan in January to April 2015, down by 1.50 trillion yuan compared to January to April 2014 (see exhibit 17). The drop in 'total social financing' was due largely to the reduction in new foreign currency loans, new entrusted loans, new trust loans, bank acceptance bills and corporate bond financing.

In January to April 2015, the share of new RMB loans in 'total social financing' was 78.0%, much higher than 59.4% in 2014, indicating that RMB loans have become a more important source of financing recently.

Exhibit 16 Broad money supply (M2) and RMB loans, May 2014 to April 2015

As of	Broad money supply (M2) Amount (trillion yuan)	Broad money supply (M2) yoy growth	Total outstanding RMB loans Amount (trillion yuan)	Total outstanding RMB loans yoy growth
End-May 14	118.2	13.4%	76.6	13.9%
End-Jun	121.0	14.7%	77.6	14.0%
End-Jul	119.4	13.5%	78.0	13.4%
End-Aug	119.8	12.8%	78.7	13.3%
End-Sep	120.2	12.9%	79.6	13.2%
End-Oct	119.9	12.6%	80.1	13.2%
End-Nov	120.9	12.3%	81.0	13.4%
End-Dec	122.8	12.2%	81.7	13.6%
End-Jan 15	124.3	10.8%	83.7	13.9%
End-Feb	125.7	12.5%	84.7	14.3%
End-Mar	127.5	11.6%	85.9	14.0%
End-Apr	128.1	10.1%	86.6	14.1%

	New RMB loans (trillion yuan)
FY14	9.78
1Q15	3.68
May 14	0.87
Jun	1.08
Jul	0.39
Aug	0.70
Sep	0.86
Oct	0.55
Nov	0.85
Dec	0.70
Jan 15	1.47
Feb	1.02
Mar	1.18
Apr	0.71

Source: People's Bank of China

Exhibit 17 Total social financing, 2014 to January-April 2015

	FY14 Amount (billion yuan)	FY14 Share (%)	Jan-Apr 15 Amount (billion yuan)	Jan-Apr 15 Share (%)
Total social financing	16,457.0	100.0	5,652.1	100.0
RMB loans	9,781.6	59.4	4,411.0	78.0
Foreign currency loans	355.4	2.2	-20.4	-0.4
Trust loans	517.4	3.1	-3.3	-0.1
Entrusted loans	2,507.0	15.2	358.6	6.3
Bank acceptance bills	-128.5	-0.8	53.0	0.9
Corporate bonds	2,425.3	14.7	468.8	8.3
Equity issuance	435.0	2.6	240.5	4.3

Source: People's Bank of China

8 http://www.gov.cn/guowuyuan/2015-04/28/content_2854625.htm

Snapshot: Key takeaways from the Government Work Report (presented by Premier Li Keqiang to the National People's Congress)

The third session of the 12th National People's Congress (NPC) was held from 5 to 15 March in Beijing. At the meeting, Premier Li Keqiang presented the *Government Work Report* on behalf of the State Council, setting the policy focus for 2015.[9] The report, together with other important documents such as the *Report on National Economic & Social Development* and the *Central & Local Budgets*, was discussed and approved.

The key takeaways from the *Government Work Report* are:

1. The Chinese policymakers embrace a 'new normal'.[10]

(i) A moderation in GDP growth rate will be tolerated (real GDP growth target set at 7% for 2015, vs. 7.5% target and 7.4% actual for 2014), as long as employment and social stability are not undermined. (Unemployment rate target set at 4.5% for 2015 vs. 4.6% for 2014. Job creation target set at 10 million for 2015, the same target as for 2014.) We notice that the robust service sector has so far been absorbing job losses in the manufacturing sector, and therefore the job pressure is much less than what the economic figures are indicating.

(ii) Economic policies (fiscal and monetary policies) will only be slightly more accommodative this year, just to 'stabilize' the economy (not to reaccelerate growth). Thus, we do not expect any large-scale fiscal stimulus this year.

(iii) Besides, it should be noted that China is in an economic transition away from manufacturing-based growth and is in the middle of an anti-corruption campaign. Both are positive to long-term sustainable growth, although they might affect short-term growth.

2. Premier Li also spent a lot of time talking about reforms. He stressed the need for de-regulation and easing restrictions in order to regain market dynamism and investment confidence in the private sector.

Structural reform bright spots:
(a) Government administrations
(b) Investment and financing mechanisms
(c) Factor pricing mechanism
(d) Fiscal and taxation systems
(e) Financial system
(f) State-owned enterprises and state capital

3. Another important theme: An all-rounded opening up

(i) To promote the 'Silk Road Economic Belt and 21st Century Maritime Silk Road' Initiative.

(ii) The 'Go Global' strategy: Especially to encourage Chinese firms to actively participate in overseas infrastructure investment, and to cooperate with their foreign counterparts in building up production capacity.

(iii) To transform and upgrade foreign trade.

(iv) To adopt a more effective approach to making use of foreign capital.

4. Regarding the domestic consumption:

(i) To create a better environment for consumption: More measures to support domestic consumption, through enhancing household disposable income and improving the social welfare system, are announced.

(ii) Target for growth of retail sales is set at 13% for 2015. We think it is achievable. In particular, online retail sales are set to continue the remarkable growth this year. We also expect to see more rational, 'healthier' consumption, especially under the anti-corruption campaign, which curbs bad practices, extravagance, and spending on luxury items.

9 http://english.gov.cn/archive/publications/2015/03/05/content_281475066179954.htm

10 According to a series of articles on the 'new normal' published on the People's Daily, the newspaper of the Chinese Communist Party, in early August last year, the 'new normal' can be interpreted as: (a) Shifting from 'high' growth to 'medium-high' (but sound) growth; (b) Tertiary sector to become the leading sector of the economy; (c) Consumption to take over the driver's seat of growth; (d) Narrowing urban-rural/regional disparity; (e) Entrepreneurship and innovations as new generators of growth.

C Outlook

1 Macroeconomic targets set for 2015

The third session of the 12th National People's Congress (NPC) was concluded in mid-March 2015, and the major macroeconomic targets for the year were announced (see exhibit 18).

The government set a lower real GDP growth target of around 7% for 2015, compared to the growth target of 7.5% for 2014. In our view, this shows that the Chinese leaders are willing to tolerate a moderation in economic growth, as long as employment and social stability are not undermined. The unemployment rate target was set at 4.5% for 2015 (vs. 4.6% for 2014), while the urban job creation target was set at 10 million for 2015, the same target as for 2014.

2 Entrepreneurs confidence rises to a three-quarter high

China's Entrepreneur Confidence Index (ECI) for the secondary industry picked up from 115.1 in 4Q14 to a three-quarter high of 120.6 in 1Q15, indicating that Chinese entrepreneurs in the industry have become more optimistic (see exhibit 19).[11]

The 'manufacturing', 'mining' and 'electricity, gas & water' sectors all recorded higher index readings in 1Q15, compared to 4Q14. Among these sectors, the 'manufacturing' sector posted the biggest gain in ECI – the ECI for the sector rose by 5.7 pts from the previous quarter to 122.6 in 1Q15. Meanwhile, despite registering quarterly gain in 1Q15, the index reading for the 'mining' sector was still well below the critical 100-mark, indicating that entrepreneurs in this sector have remained pessimistic (see exhibit 20).

Exhibit 18 Macroeconomic targets set for 2015

1. Real GDP growth of about 7% *(vs. 7.4% actual in 2014)*.
2. CPI growth of about 3% *(vs. 2.0% actual in 2014)*.
3. Fixed asset investment to grow by 15% *(vs. 15.3% actual in 2014)*.
4. Retail sales of consumer goods to increase by 13% *(vs. 12.0% actual in 2014)*.
5. Total exports and imports to rise by about 6% *(vs. 3.4% actual in 2014)*.
6. Over ten million new jobs for urban residents *(vs.13.22 million actual in 2014)*.
7. Urbanisation rate to reach 55.77% *(vs. 54.77% actual as of end-2014)*.
8. M2 money growth of about 12% *(vs. 12.2% actual as of end-2014)*.

Source: The Government Work Report delivered by Premier Li Keqiang on 5 March 2015; the Report on National Economic & Social Development

11 China's Entrepreneur Confidence Index (ECI) ranges from 0 to 200. A reading above 100 indicates that entrepreneurs tend to be optimistic; a reading below 100 indicates that they tend to be pessimistic.

Exhibit 19 China's Entrepreneur Confidence Index (Secondary Industry), 2Q13 to 1Q15

	2Q13	3Q13	4Q13	1Q14	2Q14	3Q14	4Q14	1Q15
Entrepreneur Confidence Index (Secondary Industry)	119.4	122.7	121.0	124.3	121.4	119.0	115.1	120.6

Source: National Bureau of Statistics, PRC

Exhibit 20 Entrepreneur Confidence Index by sector, 4Q14 and 1Q15

	4Q14	1Q15	Compared with the previous quarter
Secondary industry	115.1	120.6	Higher
Mining	75.3	78.8	Higher
Manufacturing	116.9	122.6	Higher
Electricity, gas & water	130.0	131.6	Higher

Source: National Bureau of Statistics, PRC

3 April PMI suggests growth stabilization of the Chinese economy

China's manufacturing Purchasing Managers' Index (PMI) rose slightly from 49.9 in February to 50.1 in March. The index then stayed at 50.1 in April, suggesting growth stabilization of the Chinese economy (see exhibit 21).

Output growth has reaccelerated. After falling all the way from 53.6 in September to 51.4 in February, the output index rebounded to 52.1 in March and 52.6 in April.

However, both domestic demand and export demand have remained sluggish in recent months. The new orders index stayed low at 50.4, 50.2 and 50.2 in February, March and April respectively.[12] Meanwhile, the new export orders index fell from 48.5 in February to 48.3 in March and 48.1 in April, the lowest level since July 2013.

The purchases of inputs index improved from the recent low of 49.4 in February to 49.7 in March, and further to 50.1 in April. The index reading in April was above the critical 50-mark, showing signs of recovery in purchasing activities.

The stocks of finished goods index went up from 47.0 in February to 48.6 in March, the highest level since June 2013. However, the index dropped to 48.0 in April, suggesting that the destocking activities have quickened again. The stocks of major inputs index fluctuated within the range of 47.3 to 48.2 throughout November to April, staying below the critical-50 mark. Manufacturers have continued to reduce their inventory of major inputs.

The input prices index rose all the way from 41.9 in January to 47.8 in April, indicating that the domestic prices of major inputs have been falling at a slower pace. After surging from 54.0 in February to 61.3 in March, the business expectations index remained high at 59.5 in April. The figures show that Chinese manufacturers are optimistic about the near-term outlook for their respective industries.

4 Non-manufacturing sector expands at a slower pace

China's Business Activity Index, which is quoted as the Non-manufacturing Purchasing Managers' Index (NMI), fell from 53.9 in February to 53.7 in March, and further to a 15-month low of 53.4 in April. The latest index reading suggests that the non-manufacturing sector has expanded at a slower pace (see exhibit 22).

The new orders index dropped from 51.2 in February to 50.3 in March. In April, the index went down to 49.1, dipping into the contractionary zone for the first time since October last year. The latest index reading indicates that the growth of new orders has turned negative.

Meanwhile, the price charged index was below the critical 50-mark in March and April, showing that enterprises have been lowering their services charges. Nevertheless, the input prices index rose above 50 in April, indicating greater cost pressure on enterprises.

Despite facing difficult situations, purchasing managers in the non-manufacturing sector remain optimistic about the near-term outlook for their respective sub-sectors: The business expectation index rose slightly from 58.7 in February to 58.8 in March, and further reached 60.0 in April, well above the neutral level of 50.

12 The 'new orders index' covers both domestic and export orders. That is to say, the manufacturers are not asked to differentiate between domestic and export orders when filling in questionnaires.

Exhibit 21 China's manufacturing PMI at a glance, April 2015

Index	Seasonally Adjusted Index	Index Compared with the Previous Month	Direction
PMI	50.1	Unchanged	Expanding
Output	52.6	Higher	Expanding
New orders	50.2	Unchanged	Expanding
New export orders	48.1	Lower	Contracting
Backlogs of orders	43.8	Lower	Contracting
Stocks of finished goods	48.0	Lower	Contracting
Purchases of inputs	50.1	Higher	Expanding
Imports	47.8	Lower	Contracting
Input prices	47.8	Higher	Falling
Stocks of major inputs	48.2	Higher	Contracting
Employment	48.0	Lower	Contracting
Suppliers' delivery time	50.4	Higher	Quickening
Business expectations	59.5	Lower	Optimistic

Source: China Federation of Logistics & Purchasing; National Bureau of Statistics, PRC

Exhibit 22 China's non-manufacturing purchasing managers' index (NMI) at a glance, April 2015

Index	Seasonally Adjusted Index	Index Compared with the Previous Month	Direction
Business activity	53.4	Lower	Expanding
New orders	49.1	Lower	Contracting
Input prices	50.8	Higher	Rising
Prices charged	48.9	Higher	Falling
Business expectations	60.0	Higher	Optimistic

Source: China Federation of Logistics & Purchasing; National Bureau of Statistics, PRC

A Recent developments

1 Both exports and imports post year-on-year drop in April

China's export growth decelerated from 8.5% yoy in 4Q14 to 4.7% yoy in 1Q15, indicating a weakening in demand for Chinese products (see exhibits 23, 24 and 25). Overall, in 1Q15, China's exports amounted to US$ 513.9 billion.

The drop in import demand has deteriorated. Compared to 4Q14, China's imports posted a sharper fall in 1Q15. After dropping by 1.6% yoy in 4Q14, China's imports contracted by 17.6% yoy in 1Q15. Overall, in 1Q15, China's imports totalled US$ 390.2 billion.

In April, China's exports fell by 6.4% yoy. China's imports recorded a sharp drop of 16.2% yoy in April, posting negative yoy growth for the sixth month in a row.

In 1Q15, China's exports to the US, the EU and ASEAN gained 11.3% yoy, 2.5% yoy and 20.6% yoy respectively. In contrast, China's exports to Japan registered negative growth of minus 11.8% yoy over the same period, showing that the demand for Chinese products from Japan has been sluggish.

China's trade surplus decreased by US$ 25.8 billion from the previous quarter to US$ 123.7 billion in 1Q15, still at a high level.

Exhibit 23 China's quarterly foreign trade data, 2Q14 to 1Q15

USD billion (yoy growth)

	Exports		Imports		Trade Balance
FY14	2,342.7	(6.1%)	1,960.3	(0.4%)	382.5
2Q14	570.8	(4.9%)	484.9	(1.4%)	85.9
3Q14	635.1	(13.0%)	506.9	(1.2%)	128.2
4Q14	646.1	(8.5%)	496.6	(-1.6%)	149.5
1Q15	513.9	(4.7%)	390.2	(-17.6%)	123.7

Source: China Customs

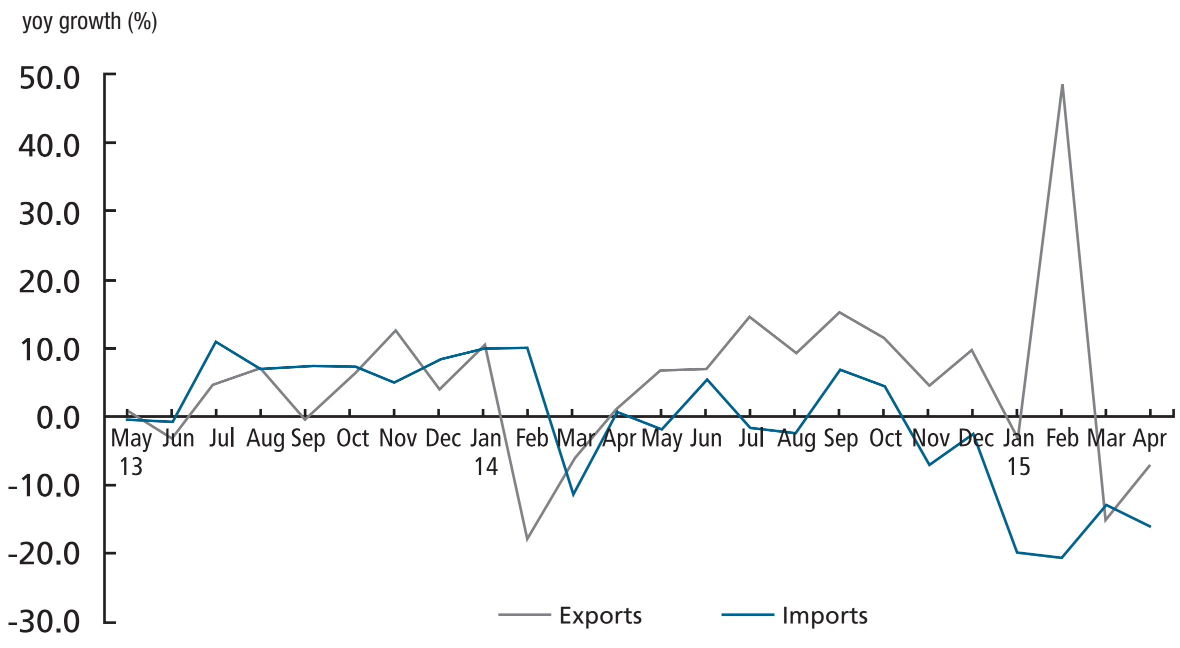
Exhibit 24 China's monthly foreign trade data, May 2014 to April 2015

USD billion (yoy growth)

	Exports		Imports		Trade Balance
May 14	195.5	(7.0%)	159.6	(-1.6%)	35.9
June	186.8	(7.2%)	155.2	(5.5%)	31.6
July	212.9	(14.5%)	165.6	(-1.5%)	47.3
August	208.5	(9.4%)	158.6	(-2.4%)	49.8
September	213.7	(15.3%)	182.7	(7.0%)	31.0
October	206.9	(11.6%)	161.5	(4.6%)	45.4
November	211.7	(4.7%)	157.2	(-6.7%)	54.5
December	227.5	(9.7%)	177.9	(-2.4%)	49.6
January 15	200.3	(-3.3%)	140.2	(-19.9%)	60.0
February	169.2	(48.3%)	108.6	(-20.5%)	60.6
March	144.6	(-15.0%)	141.5	(-12.7%)	3.1
April	176.3	(-6.4%)	142.2	(-16.2%)	34.1

Source: China Customs

Exhibit 25 Growth rates of exports and imports, May 2013 to April 2015



Source: China Customs

Exhibit 26 Exports by category, 2014 and 1Q15

yoy growth (%) of export value, calculated in USD	2014	1Q15
Textile materials and products	4.9	4.2
Garments and clothing accessories	5.2	2.0
Footwear	10.8	5.3
Toys	14.2	14.5
Coal	-34.5	-57.4
Crude oil	-66.3	288.4
Refined oil	5.2	-34.9
Steel	33.1	15.8
Mechanical and electrical products	3.7	6.1

Source: China Customs

Exhibit 27 Imports by category, 2014 and 1Q15

yoy growth (%) of import value, calculated in USD	2014	1Q15
Cereal and cereal flour	21.9	25.5
Soybean	6.0	-17.3
Iron ore	-11.8	-43.8
Crude oil	3.9	-43.0
Refined oil	-26.8	-43.4
Steel	5.0	-12.7
Textile yarns, fabric and textile products	-6.0	-6.2
Vehicles and related parts	24.4	-21.7

Source: China Customs

2 Share of processing trade in China's total trade falls in 1Q15

The growth of processing trade[13] exports dropped from 6.4% yoy in 4Q14 to minus 6.1% yoy in 1Q15 (see exhibit 28). In contrast, the growth of general trade[14] exports accelerated from 10.6% yoy in 4Q14 to 11.9% yoy in 1Q15.

Growth of both general trade imports and processing trade imports decelerated in 1Q15, compared to 4Q14. The general trade import growth dropped from minus 7.2% yoy in 4Q14 to minus 21.8% yoy in 1Q15, while the growth of processing trade imports fell from 11.1% yoy in 4Q14 to minus 8.4% yoy in 1Q15. The latter figure suggests that the processing trade exports are likely to continue to show negative growth in the near future, as processing trade imports may serve as a leading indicator of processing trade export performance.

The share of processing trade in China's total trade fell to 31.4% in 1Q15, compared to 34.8% in 4Q14. Processing trade continues to play a key role in China's overall foreign trade picture, especially as it recorded a large surplus – US$ 79.8 billion – in 1Q15. In comparison, general trade recorded a smaller surplus of US$ 55.1 billion over the same quarter.

13 'Processing trade' refers to the business of importing all or part of the raw and auxiliary materials, parts and components, accessories and packaging materials from abroad, and re-exporting the finished products after processing or assembly by enterprises within the Chinese Mainland.

14 'General trade' refers to China's import or export of goods by enterprises holding import-export rights. According to China's National Bureau of Statistics, the scope of general trade covers: Imports and exports using loans or aids; the import of materials by foreign invested enterprises (FIEs) for processing of goods for sale in the domestic market; the export of goods purchased by FIEs or manufactured by processing domestically-produced materials; the import of food and beverages by restaurants and hotels; the supply of domestically-produced fuels, materials, parts and components to foreign vessels or aircraft; the import of goods as payment in kind, in lieu of wages in labour service cooperation projects with foreign countries; and the export of equipment and materials by enterprises in China for their investment abroad.

Exhibit 28 China foreign trade (general and processing trades), 2014 to 1Q15

Item	yoy growth (%)			Share (%)		
	FY14	4Q14	1Q15	FY14	4Q14	1Q15
Exports	6.1	8.5	4.7	100.0	100.0	100.0
Of which:						
General Trade	10.7	10.6	11.9	51.4	50.2	54.0
Processing Trade	2.7	6.4	-6.1	37.7	38.8	35.4
Imports	0.4	-1.6	-17.6	100.0	100.0	100.0
Of which:						
General Trade	0.0	-7.2	-21.8	56.6	53.8	57.0
Processing Trade	5.5	11.1	-8.4	26.8	29.7	26.2
Total of Imports and Exports	3.4	3.9	-6.3	100.0	100.0	100.0
Of which:						
General Trade	5.3	1.8	-6.1	53.8	51.8	55.3
Processing Trade	3.8	8.1	-7.0	32.7	34.8	31.4

Source: China Customs

3 China's export growth to the US accelerates in 1Q15

As in the previous year, the EU was China's largest trading partner in 1Q15. Comprising 14.7% of China's total foreign trade, Sino-EU trade amounted to US$ 133.0 billion in 1Q15. The growth of Sino-EU trade dropped to minus 2.7% yoy in 1Q15 from 9.9% yoy in 2014. The growth of China's exports to the EU fell to 2.5% yoy in 1Q15 from 9.4% yoy in 2014, while the growth of China's imports from the EU dropped to minus 10.0% yoy in 1Q15 from 10.7% yoy in 2014.

The US was China's second largest trading partner in 1Q15, accounting for 14.0% of China's total foreign trade. The growth of Sino-US trade was 3.0% yoy in 1Q15, slower than the 6.6% yoy growth seen in 2014. The growth of China's imports from the US declined to minus 12.9% yoy in 1Q15 from 4.2% yoy in 2014. In contrast, the growth of China's exports to the US improved to 11.3% yoy in 1Q15, as compared to a growth of 7.5% yoy in 2014.

The Association of South East Asian Nations (ASEAN) was China's third largest trading partner in 1Q15. China's trade with ASEAN gained 4.3% yoy to reach US$ 109.6 billion in 1Q15, accounting for 12.1% of China's total foreign trade. China's export growth to ASEAN accelerated rapidly to 20.6% yoy in 1Q15 from 11.5% yoy in 2014. In the meantime, the growth of China's imports from ASEAN decelerated to minus 14.5% yoy in 1Q15 from 4.4% yoy in 2014.

Sino-Japan trade contracted by 11.4% yoy to US$ 66.1 billion in 1Q15. China's exports to Japan fell by 11.8% yoy, while China's imports from Japan were down by 11.0% yoy over the period (see exhibits 29 and 30).

4 Growth of China's exports to India and Brazil accelerates in 1Q15

China's export growth to India jumped to 23.0% yoy in 1Q15 from 12.0% yoy in 2014, while China's export growth to Brazil improved to 0.4% yoy in 1Q15 from minus 2.8% yoy in 2014. Nevertheless, the growth rate for exports to Russia plunged to minus 34.5% yoy in 1Q15 from 8.2% yoy in 2014, attributable to the deteriorating economic situations in the country. Together, these three BRIC members accounted for 5.6% of China's total exports in 1Q15, down from 6.1% in 2014 (see exhibits 29 and 30).

China's imports from Russia, India and Brazil posted sharp drop in 1Q15. China's imports from India and Brazil registered negative growth of minus 29.2% yoy and minus 37.5% yoy respectively in 1Q15, compared to minus 3.5% yoy and minus 4.8% yoy respectively in 2014. Meanwhile, China's imports from Russia registered negative growth of minus 32.6% yoy in 1Q15, after gaining 4.9% yoy in 2014. On aggregate, these three BRIC members accounted for 4.4% of China's total imports in 1Q15, down from 5.6% in 2014.

Exhibit 29 China's trading partners, 1Q15

Country/ Region	Trade value (USD billion)	Share of total trade (%)	Export value (USD billion)	Import value (USD billion)	yoy growth (%) Total trade	Exports	Imports
EU	133.0	14.7	82.5	50.5	-2.7	2.5	-10.0
US	126.2	14.0	89.7	36.5	3.0	11.3	-12.9
ASEAN	109.6	12.1	67.8	41.8	4.3	20.6	-14.5
Japan	66.1	7.3	32.9	33.2	-11.4	-11.8	-11.0
Brazil	14.4	1.6	8.1	6.3	-20.7	0.4	-37.5
Russia	14.4	1.6	7.1	7.3	-33.6	-34.5	-32.6
India	16.9	1.9	13.4	3.5	6.7	23.0	-29.2

Source: China Customs

Exhibit 30 China's trading partners, comparing growth rates for 2014 and 1Q15

yoy growth (%)

Country/Region	Total Trade		Exports		Imports	
	2014	1Q15	2014	1Q15	2014	1Q15
EU	9.9	-2.7	9.4	2.5	10.7	-10.0
US	6.6	3.0	7.5	11.3	4.2	-12.9
ASEAN	8.3	4.3	11.5	20.6	4.4	-14.5
Japan	0.0	-11.4	-0.5	-11.8	0.4	-11.0
Brazil	-4.0	-20.7	-2.8	0.4	-4.8	-37.5
Russia	6.8	-33.6	8.2	-34.5	4.9	-32.6
India	7.9	6.7	12.0	23.0	-3.5	-29.2

Source: China Customs

5 The top seven provinces/ municipalities in terms of foreign trade value account for a smaller share of China's total foreign trade in 1Q15

China's top seven provinces and municipalities in terms of foreign trade value – Guangdong, Jiangsu, Shanghai, Beijing, Zhejiang, Shandong and Fujian – jointly accounted for 76.8% of China's total foreign trade in 1Q15, down from 77.4% in 2014 (see exhibit 31).

It is noteworthy that exports from some provinces/ municipalities in China's central and western regions have recorded robust growth. For example, exports from Chongqing, Henan and Hubei gained 38.2% yoy, 21.6% yoy and 22.9% yoy respectively in 1Q15. We believe that the strong export growth from these provinces was closely associated with the relocation of factories from the eastern provinces.

6 China's FDI maintains positive year-on-year growth

China's foreign direct investment (FDI) maintained positive growth in the past few months, with the growth rate registering 29.4% yoy, 0.7% yoy and 1.6% yoy in January, February and March respectively. Overall, in 1Q15, China's FDI amounted to US$ 34.9 billion, up by 10.7% yoy (see exhibit 32).

Among the sectors, FDI in the service sector rose by 24.1% yoy to US$ 21.6 billion in 1Q15. The share of the service sector in China's total FDI reached 61.9% in 1Q15, up from 55.4% in 2014. In contrast, FDI in the manufacturing sector fell by 3.6% yoy over the same period, suggesting that foreign enterprises are less optimistic about prospects in this sector.

FDI in the eastern region increased by 18.8% yoy in 1Q15. In comparison, FDI in the central and the western regions dropped by 26.0% yoy and 15.2% yoy respectively over the same period.

The top ten countries/ regions in terms of FDI value jointly accounted for 95.4% of China's total FDI in 1Q15. Among these countries/ regions, FDI from the EU gained robustly by 30.5% yoy in 1Q15. Meanwhile, FDI from the US, Japan and ASEAN dropped by 40.4% yoy, 12.3% yoy and 31.2% yoy respectively over the same period.

Exhibit 31 The top seven provinces and municipalities in terms of foreign trade value, 1Q15

Provinces/ Municipalities	Foreign trade value (USD billion)	Share of total trade (%)
Guangdong	215.6	23.8
Jiangsu	123.8	13.7
Shanghai	106.2	11.7
Beijing	78.2	8.6
Zhejiang	77.9	8.6
Shandong	53.9	6.0
Fujian	39.2	4.3

Source: China Customs

Exhibit 32 China's FDI, April 2014 to March 2015

	Amount (USD billion)	yoy growth
FY14	119.6	1.7%
1Q15	34.9	10.7%
April 14	8.7	3.4%
May	8.6	-6.7%
June	14.4	0.2%
July	7.8	-17.0%
August	7.2	-14.0%
September	9.0	2.0%
October	8.5	1.3%
November	10.4	22.2%
December	13.3	10.3%
January 15	13.9	29.4%
February	8.6	0.7%
March	12.4	1.6%

Source: Ministry of Commerce, PRC

7 China's foreign exchange reserves fall for the third consecutive quarter

China's foreign exchange reserves fell by US$ 113.0 billion in 1Q15, amounting to US$ 3.73 trillion as at the end of 1Q15 (see exhibit 33). It was the third consecutive quarter that China had seen a drop in foreign exchange reserves, which was attributable to capital outflows and the drop in value of Euro-denominated assets held by the Chinese government due largely to the appreciation of the US dollar against the Euro.

Looking ahead, we expect China's foreign exchange reserves to drop further in 2Q15. The US Federal Reserve is widely expected to raise the interest rates later this year, which may lead to further hot money outflows from China and a further appreciation of the US dollar against the Euro.[15]

Exhibit 33 Foreign exchange reserves by quarter, 2Q14 to 1Q15

USD billion	Accumulation	End of the quarter
FY14	21.7	
2Q14	45.1	3,993.2
3Q14	-105.5	3,887.7
4Q14	-44.7	3,843.0
1Q15	-113.0	3,730.0

Source: State Administration of Foreign Exchange, PRC

15 The nominal Euro-US dollar exchange rate was 1.0731 on 31 March 2015, compared to 1.2098 on 31 December 2014.

B Highlights

1 China reduces import tariffs to boost domestic consumption demand

On 25 May, the State Council announced to reduce the tax rates for imports of various types of consumer products by more than half, on average, effective from 1 June 2015.[16]

For example, the tax rates for imports of suits and fur clothes will be reduced to 7-10% from 14-23%, while those for short boots and sports shoes will be adjusted downward from 22-24% to 12%. Meanwhile, the tax rate for imports of diapers will be cut from 7.5% to 2%, and the tax rate for imports of skincare products will be reduced to 2% from 5%.

Due partly to the high import tariffs, prices of some types of imported products are higher in the Chinese mainland than in the overseas markets. According to analysts quoted by the Reuters news agency, prices of some luxury goods sold in the Chinese mainland are around 20% higher than those sold in Europe.[17] Therefore, many Chinese consumers choose to shop overseas or to purchase through 'daigou' agencies.[18]

Increasing domestic consumption is regarded as an important way to promote stable economic growth and structural adjustment, the major economic goals of the Chinese government. It is hoped that the reductions in import tariffs will steer a change in shopping behaviour of Chinese consumers, which will in turn boost imports and domestic consumption.

2 Chinese yuan appreciates against the US dollar

The Chinese yuan has appreciated against the US dollar recently. After trending downward throughout mid-December to mid-March, the daily fixing rate (also known as the central parity rate) of the Chinese yuan went up from 6.1615 on 15 March to 6.1123 on 13 May (see exhibit 34).[19] Besides, the USD-CNY spot exchange rate appreciated from the recent low of 6.2743 on 3 March to 6.1961 on 19 March, and has fluctuated within a narrow range since then (as of 13 May). The spot exchange rate closed at 6.2044 on 13 May.

The daily fixing rate of the Chinese yuan against the Euro reached 6.4852 on 16 March, the highest level since China's central bank launched the exchange rate reform in July 2005, and then showed fluctuation till mid-April. Afterwards, the daily fixing rate of the Chinese yuan against the Euro depreciated to 6.9426 on 7 May, before rising slightly to 6.8768 on 13 May (see exhibit 35).

According to the Bank for International Settlements, the real effective exchange rate (REER) of the yuan has continued to be strong in the recent months.[20] The REER of the yuan reached 131.65 in March, the highest level since the record began in January 1994, and then stayed high at 130.44 in April. Overall, the Chinese yuan appreciated by 3.2% in real terms against its trading partners in the first four months of 2015 (see exhibit 36).

Looking ahead, we do not expect the exchange rate of the Chinese yuan against the US dollar to appreciate much in the near term, amidst the interest-rate cuts and the growth moderation of the Chinese economy. Nevertheless, we still maintain that the yuan will appreciate, albeit at a slow and gradual pace, against the US dollar in the medium to long term.

16 http://gss.mof.gov.cn/zhengwuxinxi/zhengcefabu/201505/t20150525_1240116.html

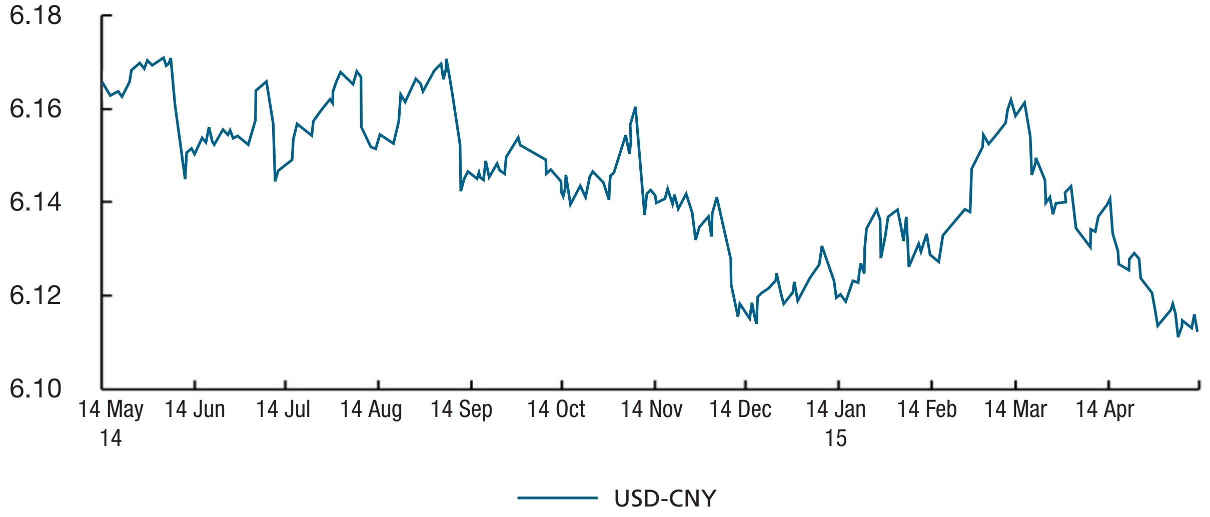
17 http://www.reuters.com/article/2015/05/25/china-imports-consumers-idUSL3N0YG1D020150525

18 'Daigou' agencies purchase overseas products on behalf of consumers, provide assistance to consumers especially on payment and delivery.

19 The daily fixing rate (also known as the central parity rate) of the Chinese yuan against the US dollar is released by the China Foreign Exchange Trade System (CFETS), a sub-institution of the People's Bank of China, at 9:15 am on each working day.

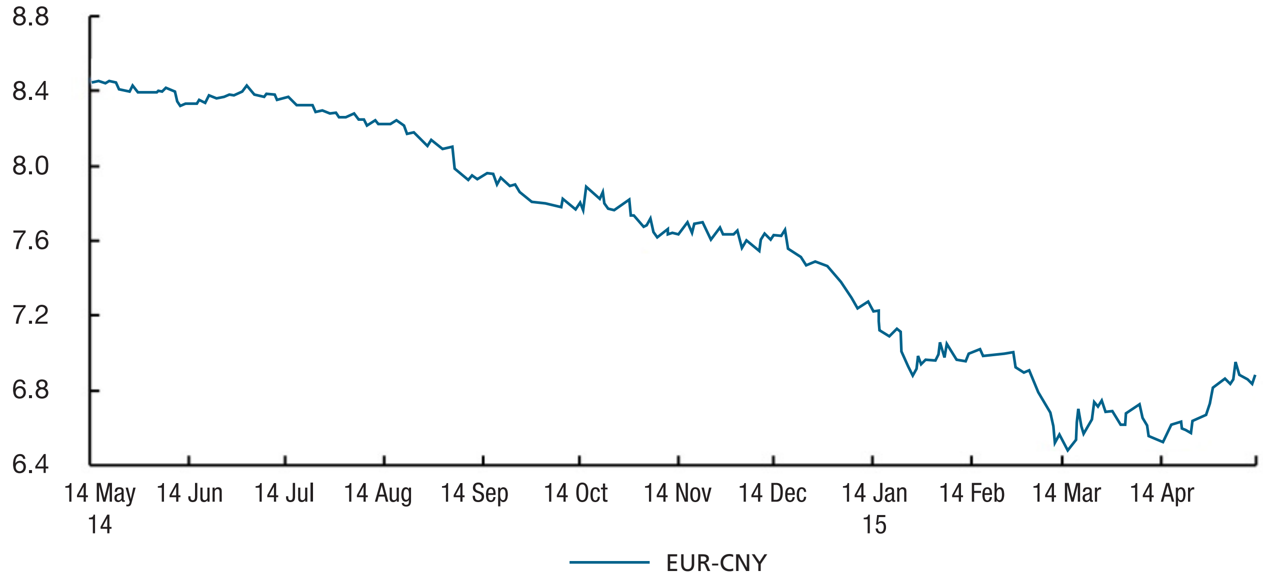
20 The Bank for International Settlements (BIS) calculates effective exchange rate (EER) indices for a total of 61 economies (including individual Eurozone countries and, separately, the Eurozone as an entity). Nominal EERs are calculated as geometric weighted averages of bilateral exchange rates. Real EERs are the same weighted averages of bilateral exchange rates adjusted by relative consumer prices. The weighting pattern is time-varying, and the most recent weights are based on trade in 2008-10.

Exhibit 34 USD-CNY daily fixing rate, May 2014 to May 2015



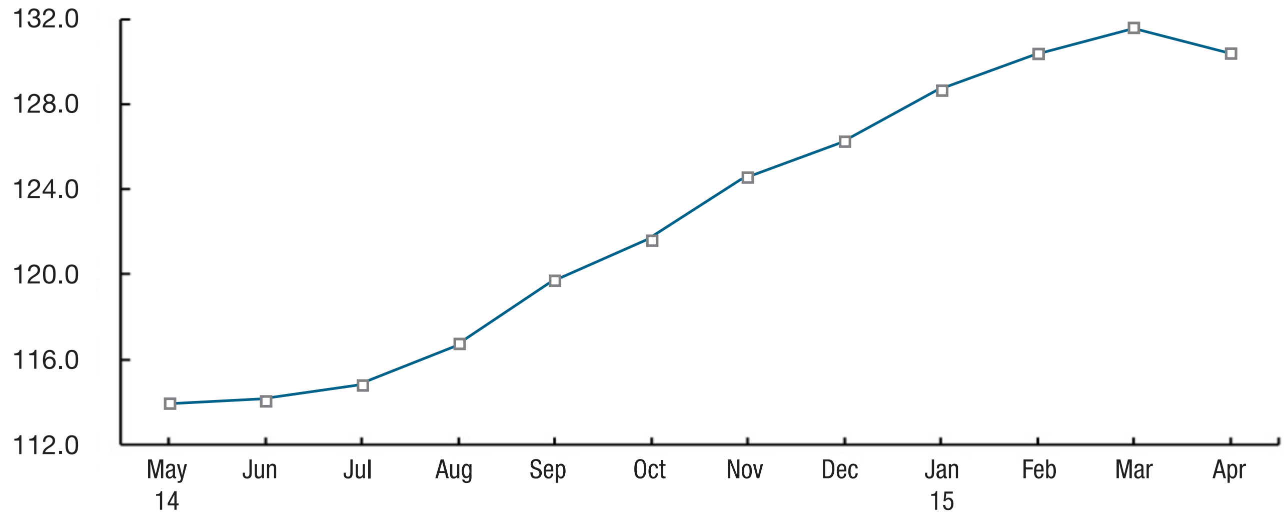
Source: State Administration of Foreign Exchange

Exhibit 35 EUR-CNY daily fixing rate, May 2014 to May 2015



Source: State Administration of Foreign Exchange

Exhibit 36 Real effective exchange rate of the Chinese yuan, May 2014 to April 2015



Source: Bank for International Settlements

3 Global merchandise trade posts low single-digit growth in 2014

In mid-April, the World Trade Organization (WTO) released the world trade statistics for 2014 with its forecasts.[21] According to the world body, the global merchandise trade volume grew only by 2.8% yoy in 2014, due mainly to the sluggish growth in the world economy.

In 2014, the global merchandise exports in US dollar terms gained by a mere 0.7% yoy to US$18.95 trillion. China has continued to be the world's largest merchandise exporter, followed by the US and Germany. Among the top 30 merchandise exporters in US dollar terms, Czech Republic posted the strongest growth in merchandise exports (i.e. 7% yoy) in 2014. The merchandise exports of China, Poland and Mexico also rose at a relatively rapid pace in 2014, by 6% yoy, 6% yoy and 5% yoy respectively.

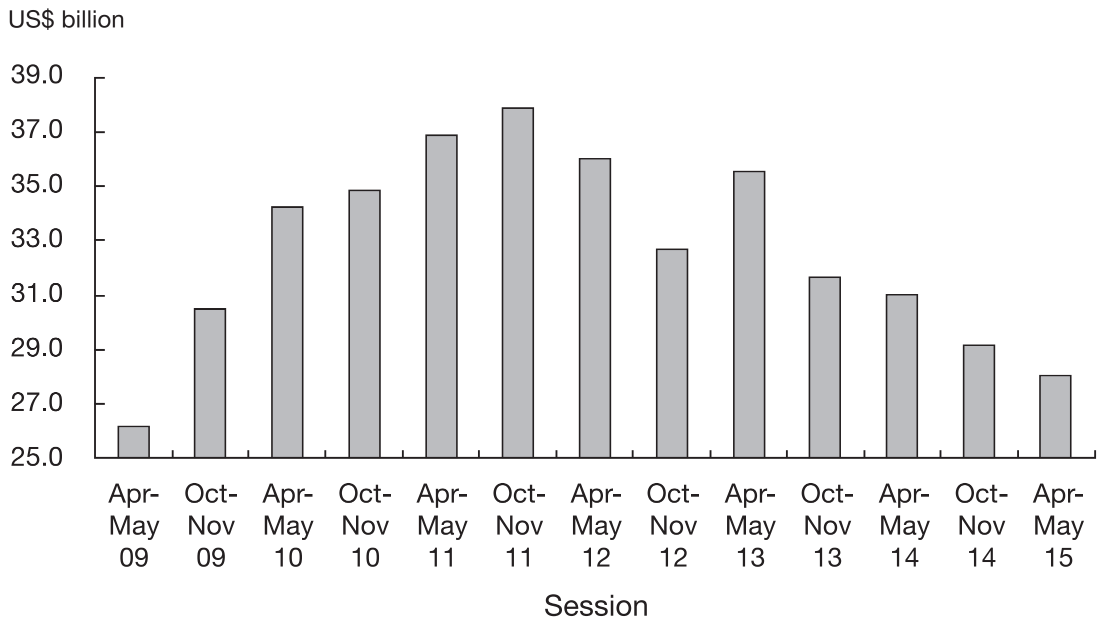
4 Total value of deals signed at the Canton Fair falls by 3.8%

The total value of deals signed at the 117th China Import and Export Fair (more widely known as the Canton Fair),[22] held in April and May 2015, fell by 3.8% to US$ 28.1 billion, compared with the previous session (see exhibit 37). The Canton Fair is widely regarded as the barometer of China's trade activity. The total value of deals signed at the fair has dropped for the fourth session in a row, suggesting that export orders have been weakening and China's exporters have been facing tough situations.

The total number of buyers visiting the fair totaled 184,801 in this session, down by 0.7% from the previous session. Particularly noteworthy is that the number of buyers from Europe fell sharply by 17.9% from the previous session. We believe that the depreciation of the Euro against the Chinese yuan greatly reduced the incentive for European buyers to visit the fair, as prices of Chinese products have become higher in Euro terms. Meanwhile, the number of buyers from Asia, the Americas, Oceania and Africa rose by 2.8%, 6.0%, 8.5% and 2.9% respectively from the previous session.

21 https://www.wto.org/english/news_e/pres15_e/pr739_e.htm
22 The China Import and Export Fair is China's largest and oldest trade exhibition.

Exhibit 37 Total value of deals signed at the China Import and Export Fair, 2009-2015



Source: Official website of the China Import and Export Fair

5 China issues an action plan for the 'One Belt One Road' Initiative

On 28 March 2015, the National Development and Reform Commission, in conjunction with the Ministry of Foreign Affairs and the Ministry of Commerce, issued an action plan for the 'Silk Road Economic Belt and 21st Century Maritime Silk Road' (Belt and Road) Initiative.[23]

Titled the 'Vision and Actions on Jointly Building Silk Road Economic Belt and 21st Century Maritime Silk Road', the official document lays out the basic goals of the Belt and Road Initiative: 'It is aimed at promoting orderly and free flows of economic factors, highly efficient allocation of resources and deep integration of markets; encouraging economic policy coordination and broader and more in-depth regional cooperation among the countries along the Belt and Road; and jointly creating an open, inclusive and balanced regional economic cooperation architecture that benefits all.'

On the same day that the official action plan of the Initiative was announced, China's President Xi also revealed in his speech that around 60 countries along the routes have shown interest in taking part in the development of the Belt and Road.[24]

According to the Initiative, China is going to negotiate with countries and regions along the Belt and Road to establish more free trade areas, lower non-tariff barriers and jointly improve the transparency of technical trade measures. Besides, to ease transport bottlenecks, China will cooperate with those countries to improve road, port and aviation infrastructure. We believe that these actions will greatly liberalize and facilitate trade, which will in turn benefit Chinese exporters and importers.

23 http://en.ndrc.gov.cn/newsrelease/201503/t20150330_669367.html

24 Based on the five routes of the Belt and Road specified by the action plan, the *Fung Business Intelligence Centre* has identified 58 countries that are most likely to be taking part in the Initiative. See *The Silk Road Economic Belt and the 21st Century Maritime Silk Road* published by our centre.

25 IMF, *World Economic Outlook*, April 2015

C Outlook

1 US economic growth moderates

The economic growth in the US has moderated. After advancing by an annual rate of 2.2% in 4Q14, the real GDP grew at a slower pace, by an annual rate of 0.2%, in 1Q15 (see exhibit 38). Also noteworthy is the deceleration in the annual real growth rate of personal consumption expenditures, which moderated from 4.4% in 4Q14 to 1.9% in 1Q15.

On the production side, industrial production fell by 0.6% mom in March, posting negative growth in three of the last four months (see exhibit 39). According to the Institute for Supply Management, the manufacturing Purchasing Managers' Index (PMI) dropped all the way from 57.9 in October to 51.5 in March and April, indicating growth deceleration of the manufacturing sector. Nevertheless, new orders for manufactured durable goods rose strongly by 4.4% mom in March on a seasonally adjusted basis, posting positive monthly growth in two of the past three months.

The non-manufacturing sector has expanded at a stable pace in recent months. The non-manufacturing index (NMI), compiled by the Institute for Supply Management, registered 56.5, 56.7, 56.9 and 56.5 in December, January, February and March respectively.

After falling by 0.9% mom, 0.8% mom and 0.5% mom in December, January and February respectively, the US retail sales rebounded by 0.9% mom in March, showing signs of improvement in consumer demand. Meanwhile, the Reuters/University of Michigan Index of consumer sentiment remained high at 95.9 in April, indicating that US consumers are quite optimistic (see exhibit 40).

The pace of job creation has slowed recently. The non-farm payroll employment increased by 126,000 in March, after gaining 264,000 in February. In the meantime, the US unemployment rate dropped from 5.7% in January to 5.5% in February, the lowest level since June 2008, and then stayed at 5.5% in March (see exhibit 41).

Looking ahead, the US economic growth is expected to pick up in coming quarters of the year. Positive factors include the improving labour market and the lower crude prices, which gives consumers more room to spend. Negative factors, however, include the recent appreciation of the US dollar and the projected gradual increase in interest rates. According to the latest projection by the International Monetary Fund (IMF), the US real GDP growth will be 3.1% in 2015 and 2016, compared to 2.4% in 2014.[25]

Exhibit 38 US national accounts, 2013 to 1Q15

Annual growth (%)	2013	2014	2Q14	3Q14	4Q14	1Q15
Real GDP	2.2	2.4	4.6	5.0	2.2	0.2

Source: US Department of Commerce

Exhibit 39 US industrial production growth, October 2014 to March 2015

mom growth (%), seasonally adjusted	Oct 14	Nov	Dec	Jan 15	Feb	Mar
Industrial production	0.0	1.1	-0.1	-0.4	0.1	-0.6

Source: US Federal Reserve

Exhibit 40 US consumer market, November 2014 to April 2015

	Nov 14	Dec	Jan 15	Feb	Mar	Apr
Retail and food services sales *(mom growth %, seasonally adjusted)*	0.5	-0.9	-0.8	-0.5	0.9	-
Reuters/University of Michigan index of consumer sentiment	88.8	93.6	98.1	95.4	93.0	95.9
CPI *(yoy growth %)*	1.3	0.8	-0.1	0.0	-0.1	-

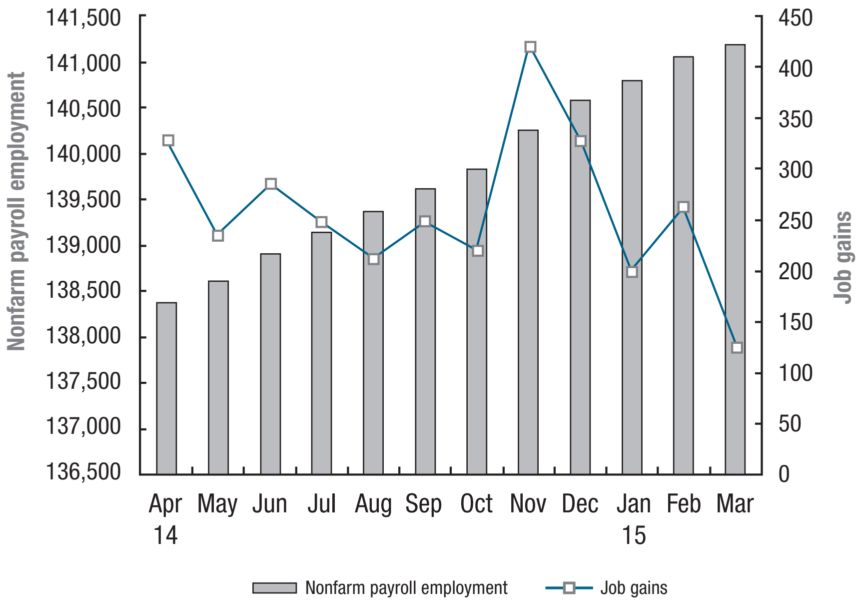
Source: US Department of Commerce, Reuters/University of Michigan Surveys of Consumers, US Department of Labor

Exhibit 41 US employment

	Unemployment rate (%)
2013	7.4
2014	6.2
Apr 14	6.2
May	6.3
Jun	6.1
Jul	6.2
Aug	6.1
Sep	5.9
Oct	5.7
Nov	5.8
Dec	5.6
Jan 15	5.7
Feb	5.5
Mar	5.5

Yearly figures: Annual average
Monthly figures: Seasonally adjusted

Nonfarm payroll employment, April 2014 to March 2015
In thousands, seasonally adjusted



Source: US Department of Labor

2 Eurozone economy continues to improve

The Eurozone economy has continued to improve.[26] According to the global survey firm Markit Economics, the Eurozone manufacturing PMI improved from 51.0 in February to a ten-month high of 52.2 in March, and then registered 52.0 in April. The recent index readings suggest that the manufacturing sector has expanded at a relatively fast pace.

The growth of the Eurozone services sector has also accelerated. The Eurozone services PMI went up all the way from 51.1 in November to 54.2 in March, the highest level since August last year.

26 Lithuania has become the 19th member of the Eurozone as from 1 January 2015. Other member countries include Austria, Belgium, Cyprus, Estonia, Finland, France, Germany, Greece, Ireland, Italy, Latvia, Luxembourg, Malta, the Netherlands, Portugal, Slovakia, Slovenia and Spain.

However, growth of retail trade volume in the Eurozone has decelerated in recent months, indicating a moderation in consumption demand. On a seasonally adjusted basis, the mom growth of the retail trade volume dropped all the way from 0.7% in November to minus 0.8% in March (see exhibit 43). Besides, the labour market conditions in the region have remained poor, which may discourage consumers to spend. The unemployment rate stayed high at 11.3% in January, February and March (see exhibit 44).

The Eurozone's economic sentiment indicator (ESI) rose all the way from 100.8 in November to 103.9 in March, indicating a continuous improvement in economic sentiment. The ESI remained high at 103.7 in April (see exhibit 45).

Going forward, the Eurozone economic growth is set to improve further in the near term, due to favourable factors such as lower oil prices, low interest rates and the depreciation of the Euro. According to the projections by the IMF, the Eurozone's real GDP growth will rise from 0.9% in 2014 to 1.5% in 2015 and 1.6% in 2016.[27]

Exhibit 42 Eurozone's real GDP growth, 2013 to 4Q14

	2013	2014	1Q14	2Q14	3Q14	4Q14
Real GDP *(qoq growth %)*			0.3	0.1	0.2	0.3
Real GDP *(yoy growth %)*	-0.5	0.9	1.1	0.8	0.8	0.9

*** The figures in 2013 and 2014 do not reflect Lithuania's membership of the Eurozone, which began on 1 January 2015.**

Source: Eurostat

Exhibit 43 Eurozone consumer market, October 2014 to March 2015

	Oct 14	Nov	Dec	Jan 15	Feb	Mar
Volume of retail trade *(mom growth %, seasonally adjusted)*	0.5	0.7	0.5	0.4	0.1	-0.8
Annual inflation (%)	0.4	0.3	-0.2	-0.6	-0.3	-0.1

*** The figures in 2014 do not reflect Lithuania's membership of the Eurozone, which began on 1 January 2015.**

Source: Eurostat

Exhibit 44 Eurozone labour market, October 2014 to March 2015

seasonally adjusted	Oct 14	Nov	Dec	Jan 15	Feb	Mar
Unemployment rate (%)	11.5	11.5	11.4	11.3	11.3	11.3

*** The figures reflect Lithuania's membership of the Eurozone, which began on 1 January 2015.**

Source: Eurostat

Exhibit 45 Eurozone economic sentiment indicator, November 2014 to April 2015

seasonally adjusted	Nov 14	Dec	Jan 15	Feb	Mar	Apr
Economic sentiment indicator	100.8	100.9	101.5	102.3	103.9	103.7

* Lithuania, which has become the 19th member of the Eurozone as from 1 January 2015, was included in calculation of this set of figures.

Source: Eurostat

3 China's exports are expected to post low single-digit growth in 2Q15

In its *World Economic Outlook* released on 14 April, the IMF predicts that the real GDP growth of the advanced economies will go up from 1.8% in 2014 to 2.4% in 2015. In contrast, the real GDP growth of the emerging markets and the developing economies is projected to decelerate from 4.6% in 2014 to 4.3% in 2015 (see exhibit 46).

Despite the improvement in economic situations in the advanced economies, we expect only low single-digit growth for China's exports in 2Q15, and Chinese manufacturers will continue to face intense competition from manufacturers in other Asian countries, including Vietnam, India and Bangladesh, to name just a few.

Exhibit 46 Latest GDP growth forecasts by the International Monetary Fund

yoy growth (%)	2014	2015 (Forecasts)	2016 (Forecasts)
World economy	3.4	3.5	3.8
Advanced economies	1.8	2.4	2.4
US	2.4	3.1	3.1
Eurozone	0.9	1.5	1.6
Japan	-0.1	1.0	1.2
Emerging markets and developing economies	4.6	4.3	4.7
China	7.4	6.8	6.3
India [28]	7.2	7.5	7.5
ASEAN-5 [29]	4.6	5.2	5.3
Brazil	0.1	-1.0	1.0
Russia	0.6	-3.8	-1.1

Source: International Monetary Fund, World Economic Outlook, April 2015

27 IMF, *World Economic Outlook*, April 2015

28 Data and forecasts are presented on a fiscal year basis. India's fiscal year runs from 1 April to 31 March.

29 Indonesia, Malaysia, the Philippines, Thailand and Vietnam.

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