Autumn 2021

China Financial Index

January 10, 2022

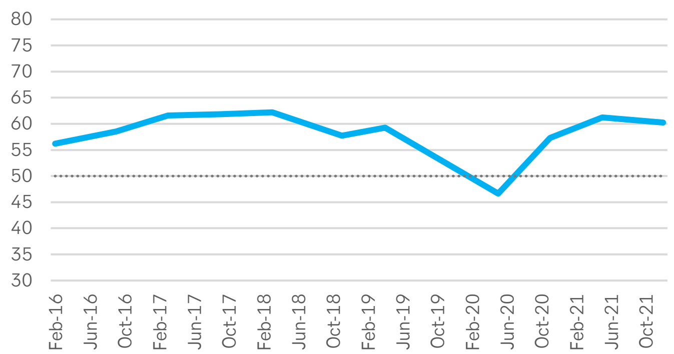
- The SEB China Financial Index for the autumn remained strong at **60.2,** slightly down from 61.3 in the previous survey conducted in May but still above the 57.3 posted one year ago
- While optimism regarding order intake over the next six months has declined, there is a clear intention to continue investments in China, primarily through the expansion of existing business
- Decoupling, regulations, and data/cyber security are among the topics that are concerning executives

Thilo L. Zimmermann
General Manager, Shanghai
+86 21 2052 1818
thilo.zimmermann@seb.se

Gaute Braastad Johansen
Client Executive, Shanghai
+86 21 2052 1871
gaute.johansen@seb.no

In this Autumn 2021 edition of the China Financial Index (CFI), the index value decreased to 60.2 based on the survey conducted between 6 December and 20 December. This underpins a continued optimistic outlook towards doing business in China, but there are changes to the composition of the index components which suggest an underlying shift in the outlook for the next six months.

Historical development of the CFI



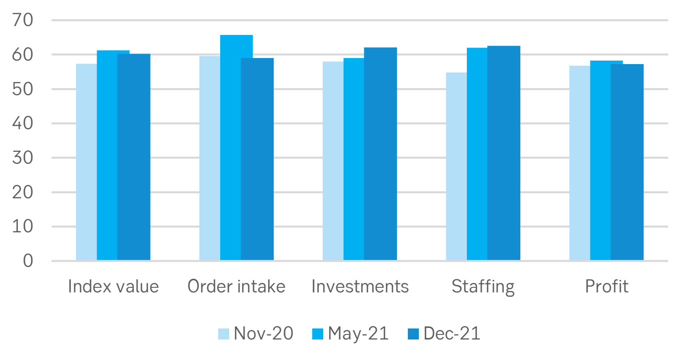
Source: SEB

As a result of the rather strict measures/zero-tolerance policy on COVID-19 implemented by the Chinese government, the economy has to a large extent been able to thrive through large parts of 2020 and 2021 contrary to most of the rest of the world. Corporates have so far reported a rather positive development and rebound in business in China. We will soon pass 24 months of the pandemic and are now starting to see vaccination rates that will support recovery in more parts of Asia. This could prove to be a threat to Chinese exports, but the emergence of omicron might challenge this scenario.

After a strong first half of 2021, Chinese Q3 GDP slowed more than SEB expected. The zero-tolerance policy towards COVID-19 has dulled private consumption, which is a key part of a sustainable recovery. Despite this, the uncertainty created by omicron will likely reinforce the authorities' decision to stick with the zero-tolerance policy. Infrastructure spending will likely have a bigger role in 2022 as Beijing tries to create a floor for the growth outlook. SEB's forecasts for Chinese GDP growth are 8.2% for 2021 and 5.2% for 2022.

If we look at the overall changes to the index components, the biggest drop is within "Order intake". This index component has dropped almost seven points in the latest survey. Although a large portion of the respondents are expecting +5 to +20 % sales growth over the next six months, there is a sharp increase in the number of companies expecting a +/- 5% development at the top line over this period, creating a downward pressure on the index. This shift is partly counterbalanced by an uptick in "Investments", which increases from 59 to 62.1. "Staffing" and "Profit" are nearly flat in the latest survey.

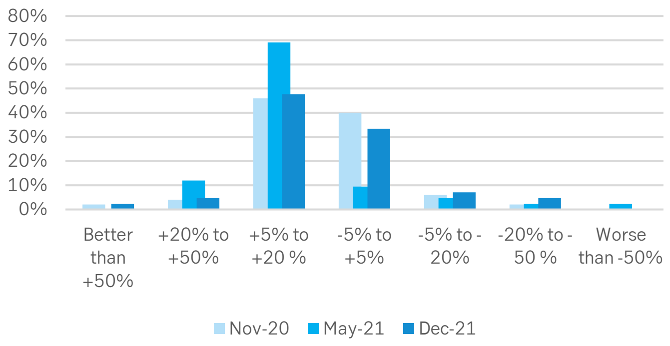
Index values



Source: SEB

Sales figures, year over year, remain broadly positive as 65% of respondents report sales growth above 5% compared to the second half of 2020. There is, however, an uptick in corporates finding themselves in the +/- 5% bracket and 14% report a sales decline of -5% to -20%. As economic growth has slowed recently, these developments are not a major surprise as many economists have reduced their growth forecasts, but there is also a slight shift in optimism regarding sales over the next six months as well. We note that congested shipping lines do have an impact on supply, even if there is existing demand in the domestic Chinese market. As a result, some respondents may have to lower their forecasts as well.

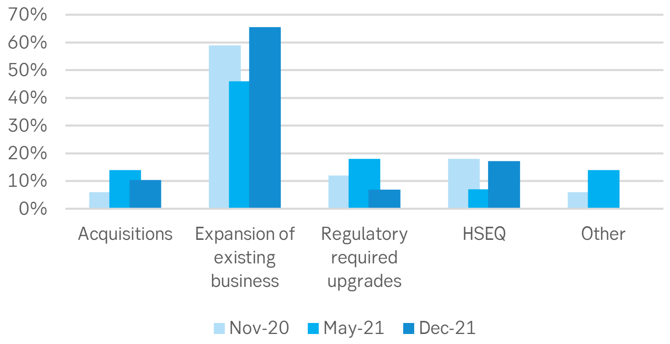
Expected order-intake over the next six months



Source: SEB

Investments continue to be on the agenda. Amongst all the index components, "Investments" is this survey's biggest climber (from 59 in May to 62.1). Forty-nine percent of respondents expect investments to remain unchanged, 42% report "modest investment plans" and 9% report major investment plans. Although small, there has been a slight uptick in companies expecting *Major investments* (up from 4% to 8%). The recovery of the *Investment index* has been lagging compared to the other sub-values, but it is now back to pre-COVID levels. We find this development confirm corporates commitment towards China.

Nature of investments

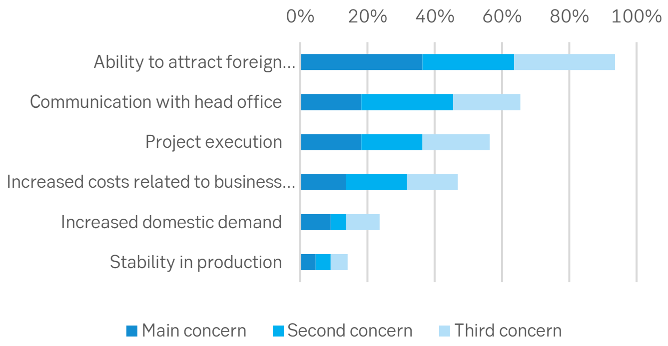


Source: SEB

Expansion still takes the number one spot when it comes to investments. Of the respondents, 76% reported that they planned either expansion of existing businesses or acquisitions, while there was a slight increase in HSEQ-related investments and the "other categories". On the people side, 63% of respondents plan to increase staffing over the next six months and the index component "Staffing" is marginally up from the survey in May this year (from 62.0 to 62.9).

A zero-tolerance policy on COVID-19 has been China's most important weapon in keeping the economy open. The policy has had strong support among the population, but it is clear that strict border controls and difficult entry requirements are having some impact on foreign businesses and expat population. In this survey, therefore, we introduced a question about the main impacts of this policy. The responses show clearly that the main impacts have been the ability to attract foreign talent, communication with the head office, and project execution.

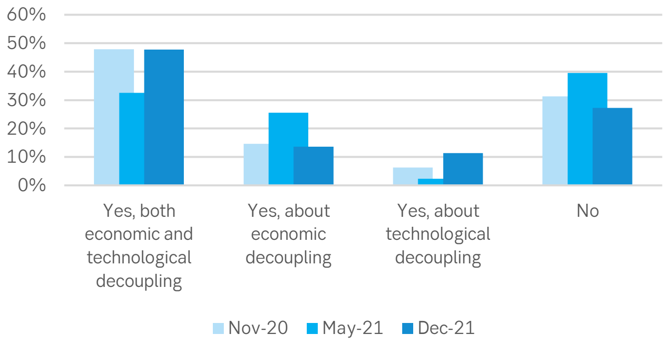
Main impact of the zero COVID-19 policy



Source: SEB

As China seems to be turning inward somewhat, there is a risk that this policy may further increase decoupling between China and the West, which may ultimately impact investments into China. There is a clear positive sentiment towards China among the survey respondents, but looking at some of the replies, there are clear concerns among executives which can be read negatively. Around 60% now report that they have experienced China becoming more regulated and are finding it more difficult to do business in the country. This is an increase of around 11 percentage points from the survey in May. In addition, we note a large drop in respondents saying that they are not worried about decoupling.

Are you worried about decoupling?

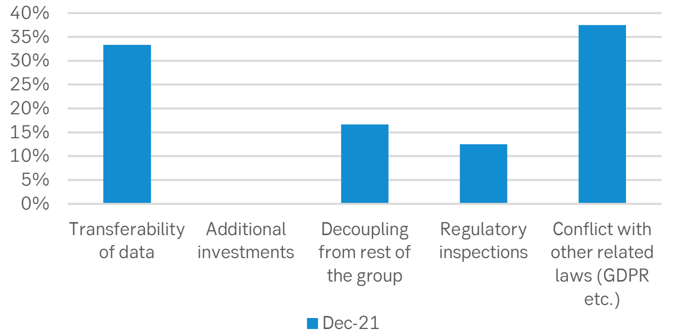


Source: SEB

Furthermore, it seems evident that respondents to a larger extent are worried about technological decoupling. In recent weeks, there have been events that have made it clear China is willing to decouple trading partners that do not share its views.

Another hot topic among the executives of foreign businesses is the new data and cyber security laws that aim at protecting both national and personal security with the ultimate effort to try to curb the power of big tech companies and regulate the digital sphere. This is in our view is not necessarily controversial in itself - but it is an area where China is lagging western economies in terms of implementation. What is challenging is the current ambiguity of these laws and more specifically their implementation. Several new laws have been passed, but as an example, the Data Security Law still lacks guidelines as to how to define and identify important data, how to handle cross-border transfer and which regulators will be in charge. For MNCs, this poses a lot of questions due to their IT infrastructures and commitments to foreign laws. We decided, therefore, to ask if corporates are worried about the state of data and cyber-security requirements in China. Fifty-one percent responded “Yes”, while 26% responded with “No” and the rest had no opinion. The concerns are mainly related to the transferability of data and conflicts with other related laws.

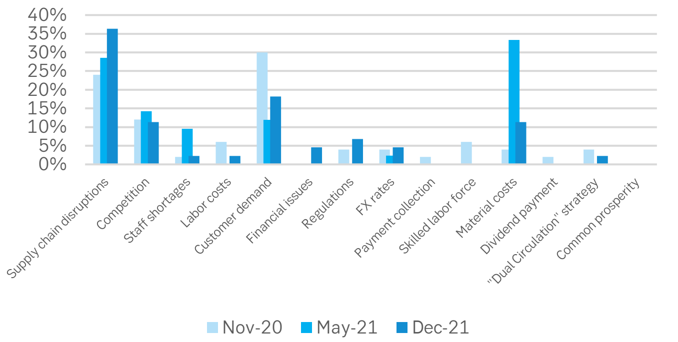
State of data and cyber-security requirements – Main concern



Source: SEB

Supply chain disruption is now the main concern among corporates over the next six months. In our previous survey, we saw *material costs* jump to a clear pole position following the surge in commodity prices. “Material costs” have now fallen back considerably to the third spot, which it shares with “Competition”. Supply chain disruption on the other hand has climbed for the third consecutive survey and is now the main concern among 36% of the respondents. The shift in consumer preference to physical goods as global travel remains largely restricted and reduced productive capacity have put tremendous pressure on supply chains.

What is your main concern over the next six months?



Source: SEB

Our conclusions

The survey results do not unveil any big surprises. As the world continues to fight for recovery, corporates remain optimistic about doing business in China. As domestic growth has slowed somewhat, , it seems that our client base has adjusted its optimism accordingly but remains committed to operations in China. If anything, some of the questions that are outside the index components show a mixed picture, where there is a broader view that China is becoming more regulated and a more difficult place to do business, while at the same time the strict COVID-measures in China that have supported recovery are starting to show some impact on our clients’ businesses as well.

Information about the survey

SEB’s China Financial Index first launched in 2007 and is based on input, in this edition from CEOs, CFOs or Treasurers at 50 subsidiaries of major Swedish, Finnish, Norwegian, Danish, German, British and Swiss companies. Most of the surveyed companies have a global turnover above EUR 500m. The survey is web based and confidential and was carried out from 6 December to 20 December 2021.

China Financial Index – composition

SEB’s China Financial Index in the Autumn of 2021 displayed a value of 60.2, indicating a small drop in optimism in the business environment compared with the survey in May 2021. A value of 50 indicates a neutral view. The index is based on four components with the following ranking in the survey: Order Intake 59.0, Profit Expectations 57.3, Investment Plans 62.1 and Employment Plans 62.6.

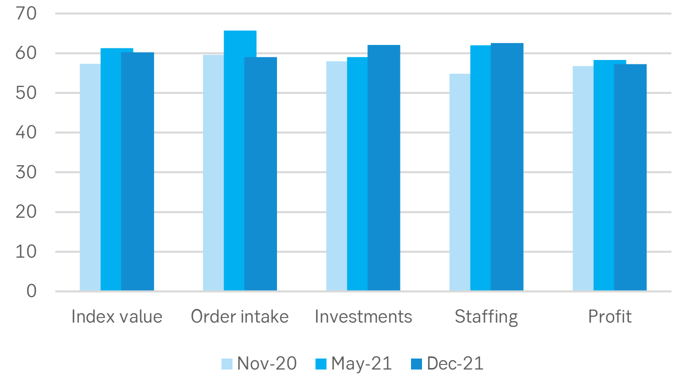
Forecasts – Real GDP, % y/y

	2020	2021	2022
China	2.3	**8.2**	**5.2**
India	-7.1	**7.9**	**7.3**
Indonesia	-2.0	**3.3**	**5.4**
Malaysia	-5.6	**3.2**	**5.7**
Philippines	-9.4	**5.0**	**6.3**
Singapore	-5.4	**6.9**	**4.3**
South Korea	-0.9	**4.0**	**2.8**
US	-3.5	**5.6**	**3.9**
Eurozone	-6.7	**4.6**	**4.3**
Japan	-4.9	**2.5**	**2.3**

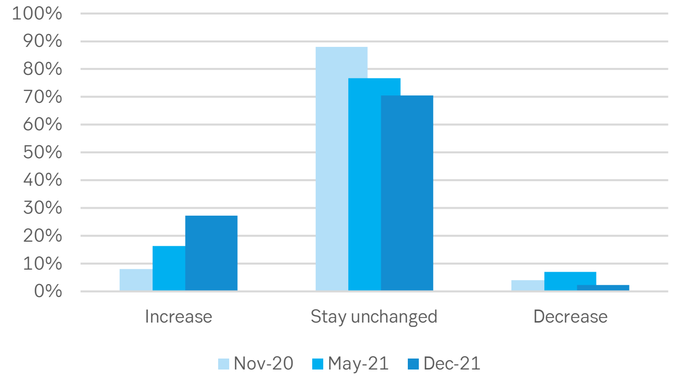
Source: Bloomberg, CEIC, SEB

Please note: The following graphs are all produced by SEB and represent all the questions in the latest China Financial Index as well as historical surveys (if applicable).

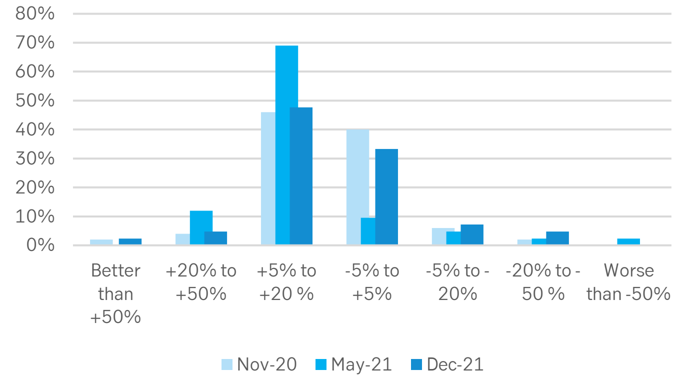
1 – Index values



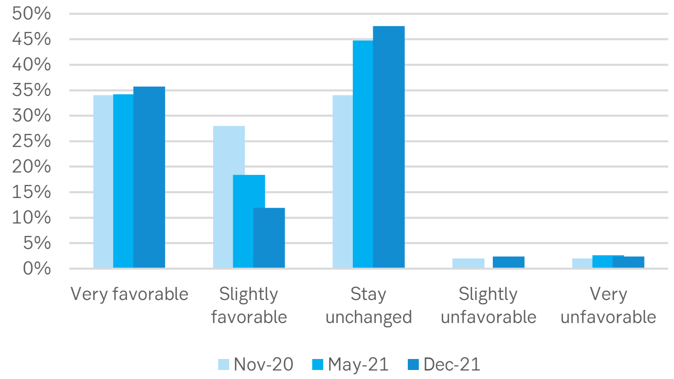
5 – Borrowing outlook



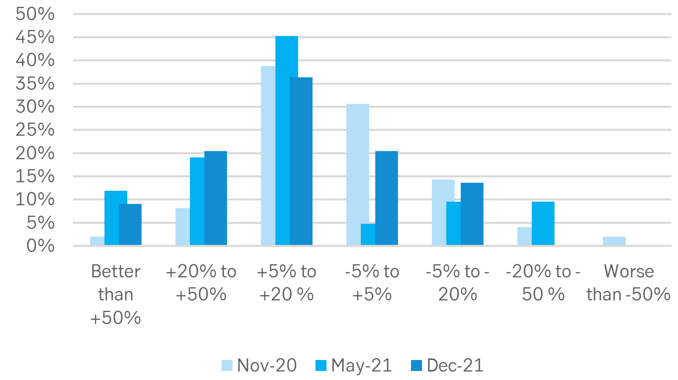
2 – Sales outlook (next six months)



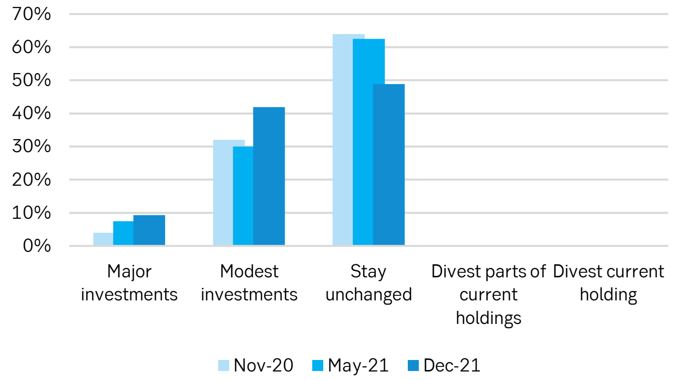
6 – Bank's lending attitude



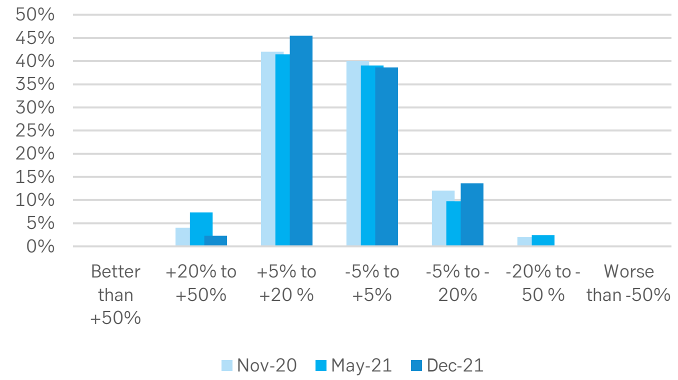
3 – Y/y sales development (H2/21 vs H2/20)



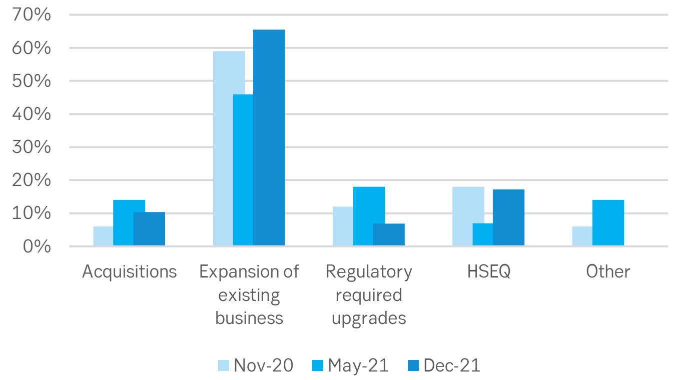
7 – Investment plans



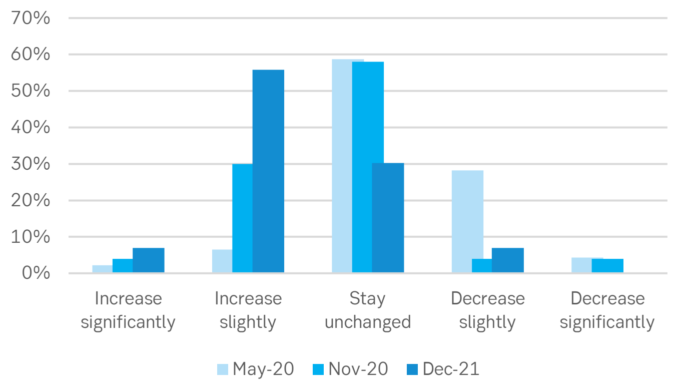
4 – Profit outlook (next six months)



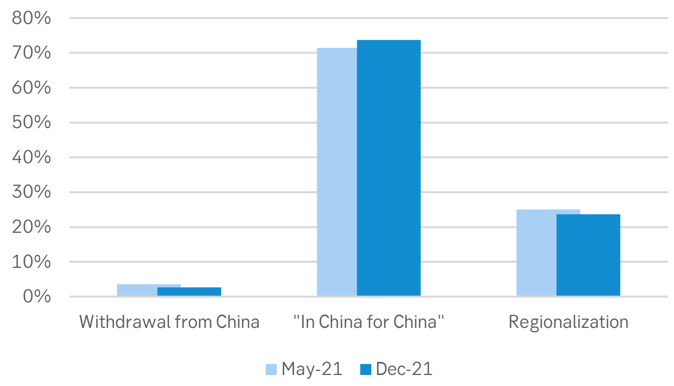
8 – Type of investment



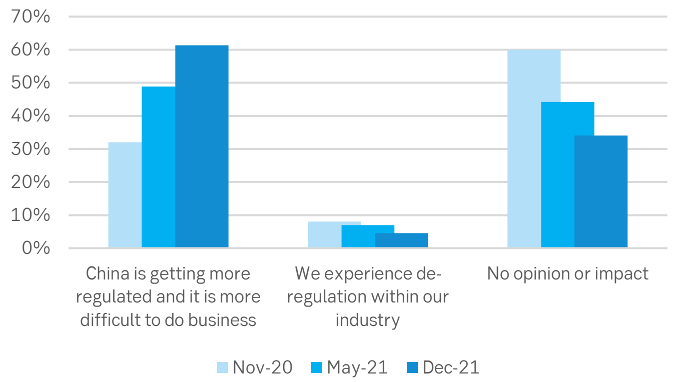
9 – Staffing development



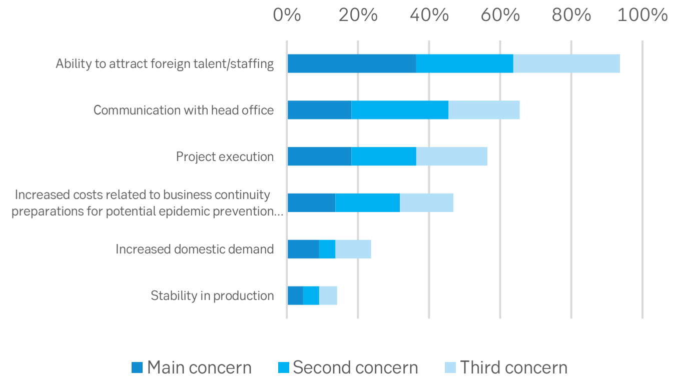
13 – Potential decoupling strategy



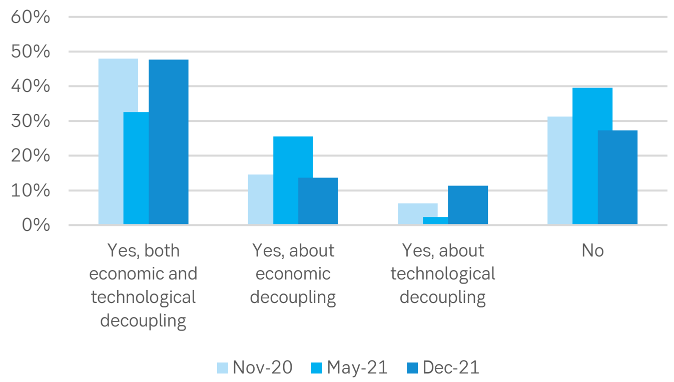
10 – Regulatory development in China



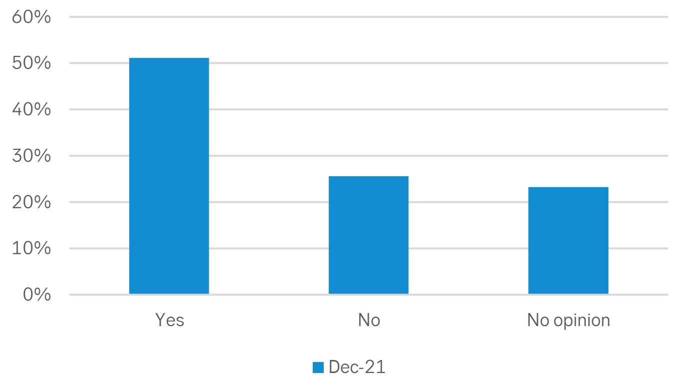
14 – Impact of zero-tolerance policy on COVID



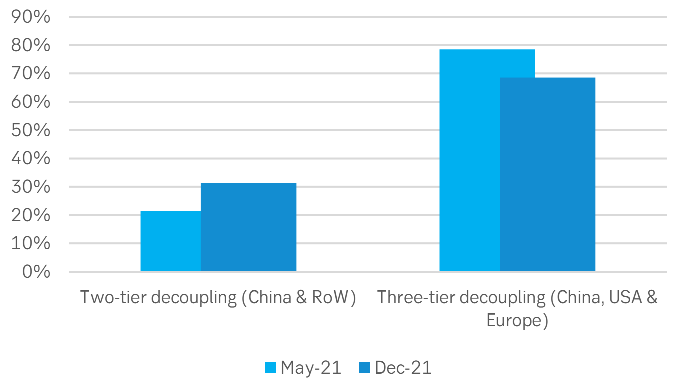
11 – Worried about decoupling?



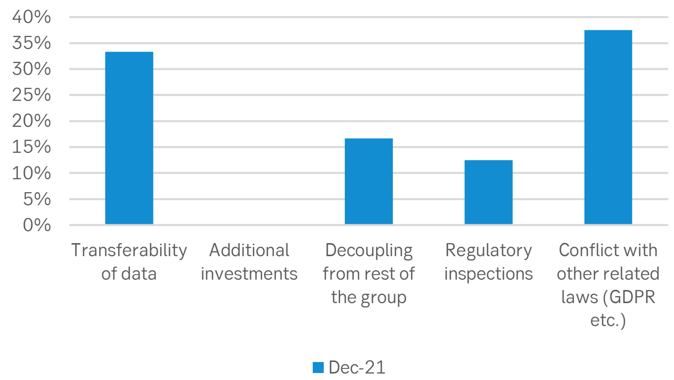
15 – Worried about data/cyber security?



12 – Type of decoupling



16 – Main concern regarding data/cyber security



17 – Main concern over the next six months