

# Daiwa's View

## Will Chinese manufacturing sector recover?

- Initial signs of recovery observed

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Daiwa Securities Co. Ltd.

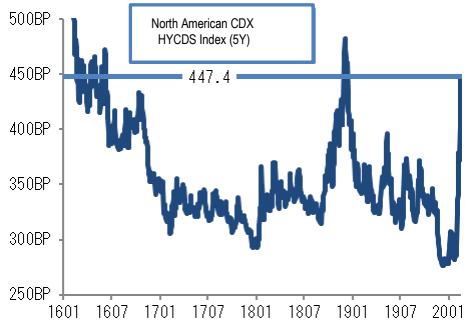
### Initial signs of recovery observed

### Will Chinese manufacturing sector recover?

As the market appears to have judged the strong US jobs report as a rearview mirror, extreme risk-off sentiment continued late last weekend. A concern is the sharp deterioration in credit indices as follows—the North American High Yield CDS Index to 447bp (+42bp) and the European iTraxx XOVER Index to 380bp (+61bp), the worst level since 2016. What is worse is the start of the spread of credit deterioration to “financials.” The iTraxx Europe Senior Financials Index widened by 13bp to 92bp. A credit crisis causes a chain reaction of “corporate bankruptcies (crisis) → job cuts (wage cuts) → weaker consumption → economic recession.” As the US and Europe are on the verge of a recession, the surge in capital flight to US Treasuries makes sense.

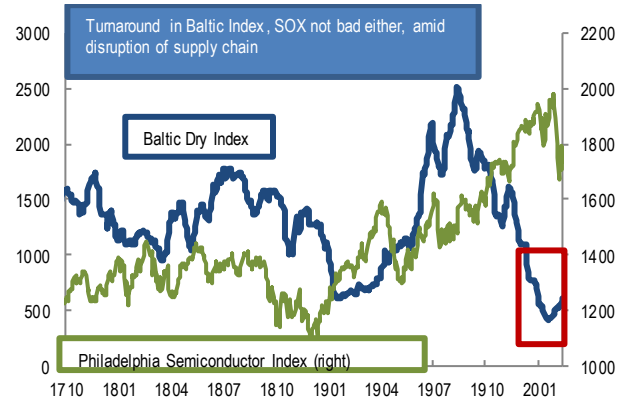
On the other hand, there are also positive media reports. Conceivably, what should be checked now may be this kind of information (as negative information overflowing in town, we do not need to repeat them). On 6 March, Jiji Press reported the announcement by Toyota Motor that “its Changchun plant for completed cars in Jilin Province of China will resume regular operations from 9 March.” The car maker appears to have judged that “employees’ safety and parts procurement should be secured.” The Baltic Dry Index turned around (Chart 2)—this would be unjustified if the Chinese manufacturing sector remains disrupted. During last week’s business trip to Osaka Prefecture, I interviewed the president of a small/midsize company (boasting world’s leading share for raw materials essential for plant operations in China). He said that he was surprised by export agencies’ request for the maximum possible deliveries. It has been said that the Chinese supply chain is disrupted due to the COVID-19 outbreak. However, there is a possibility that on-site operations are improving in the Chinese manufacturing sector in line with receding spread of the virus. We do not know yet whether operations will return to normal. However, if normal operations resume in April, the related data would be available in May and beyond. This is a bit of a long way off. Regarding the supply chain issue, however, we should keep in mind a surprise scenario that the PMI may sharply rebound beyond 60 from the current 30 level.

**Chart 1: North American High Yield CDS Index**



Source: Bloomberg; compiled by Daiwa Securities.

**Chart 2: Baltic Dry Index and SOX Index**



Source: Bloomberg; compiled by Daiwa Securities.

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The name and registration number of the Registered Credit Rating Agency in the group: Moody's Japan K.K. (FSA commissioner (Rating) No.2)

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- 2) Daiwa Real Estate Asset Management is a subsidiary of Daiwa Securities Group Inc. and serves as the asset management company for the following J-REITs: Daiwa Office Investment Corporation (8976), Nippon Healthcare Investment Corporation (3308), Japan Rental Housing Investments (8986).
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- 4) On 30 May 2019, Daiwa Securities Group Inc. formalized an equity/business alliance with Samty, and as of 14 June 2019 it owned 16.95% of shares outstanding in Samty along with convertible bonds with a par value of ¥10bn. Conversion of all of said convertible bonds into common shares would bring the stake of Daiwa Securities Group Inc. in Samty to 27.28%.
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- For derivative and margin transactions etc., our company may require collateral or margin requirements in accordance with an agreement made beforehand with you. Ordinarily in such cases, the amount of the transaction will be in excess of the required collateral or margin requirements\*\*.
- There is a risk that you will incur losses on your transactions due to changes in the market price of financial instruments based on fluctuations in interest rates, exchange rates, stock prices, real estate prices, commodity prices, and others. In addition, depending on the content of the transaction, the loss could exceed the amount of the collateral or margin requirements.
- There may be a difference between bid price etc. and ask price etc. of OTC derivatives handled by our company.
- Before engaging in any trading, please thoroughly confirm accounting and tax treatments regarding your trading in financial instruments with such experts as certified public accountants.

\* The amount of the trading commission cannot be stated here in advance because it will be determined between our company and you based on current market conditions and the content of each transaction etc.

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Corporate Name: Daiwa Securities Co. Ltd.

Registered: Financial Instruments Business Operator, Chief of Kanto Local Finance Bureau (Kin-sho) No.108

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