

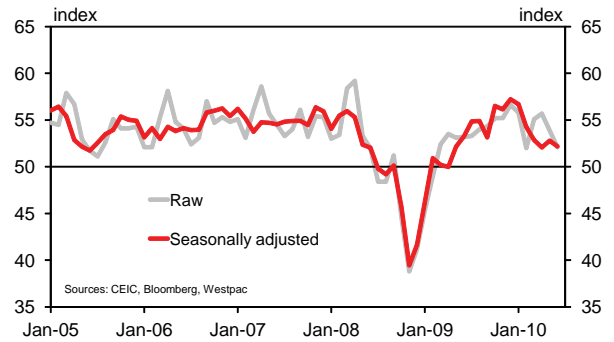
27 July 2010

- There is a great deal of focus on the upcoming July PMI. Recall that the headline for June came in at 52.1 which compares to 53.9 in May and 55.7 in April. These published numbers are not adjusted for seasonality. Now, even a hatchling yet to take its first flight knows that Chinese economic activity is highly seasonal. Specifically for the PMI, June is the only month where the seasonal factor is worth less than ½ an index point on the headline. The average monthly seasonal factor (absolute terms) is worth 1.3 index points on a base of 50. July is slightly above average at +1.4. *This raises the very real possibility that the July headline prints at or below 50.* The logic is as follows: a 0.8pt decline in the seasonally adjusted outcome, from 52.2 to 51.4, which seems a reasonable (even conservative) expectation based on the slowing momentum of the economy, would put the published number on the cusp of contraction at 50.0. On this basis, it is worthwhile thinking how global risk appetite would respond to a number printing sub-50: **Phat Dragon** is certainly doing so.
- Chongqing plans to build some 30 million sqm of public housing for 1½million urbanites over the next three years. The Mayor of the city, whose population is estimated to be as high as 30 million people, is looking to Singapore's twin track model (where around four fifths of housing is government supplied) for inspiration. By way of context, 119 million sqm of residential floor space was under construction in the city in 2009, implying this plan is equivalent to around 8% of 2009 activity levels on an annual basis through 2012. **Phat Dragon's** monopoly on bamboo scaffold in those parts just got even sweeter.
- Obligatory iron ore spot market update: **Phat Dragon** is of the opinion that the reservation price of local producers was reached when the market fell below \$US120/t last week. Local miners have far higher costs and lower grades than the global majors, with average ferrous ore content around 25%, a weak logistics set-up and lower capital intensity. The jump from \$US117 to \$US133 over the last nine days presumably reflects locals withdrawing supply with the price so unattractive. That suggests that \$US120/t or so will serve as a floor for the market even as we enter the seasonally weak August month. Shipping costs continue to crater though, with Dampier-Qingdao freight rates now almost half of the May level.
- Along with two co-authors, **Phat Dragon** has released a work in progress estimate of the *timing* and *level* of the peak in China's steel demand. The level is expected to be in the upper half of a range from 700 to 800kgs per head, versus 380kgs in 2008, the timing is c.2024 at a GDP/capita level almost three times that of the starting point.
- The new Bugatti Veyron has reclaimed its position as the world's fastest production car, with a top speed of 431kph. Curiously enough, that is the same top speed as Shanghai's Maglev railway with its in-carriage digital speedometers. Besides the obvious style advantage, **Phat Dragon's** preference for the Bugatti over the Maglev is simple: the latter has usually stopped running by the time the direct flight from Sydney hits the tarmac - and the Veyron doesn't terminate in the middle of suburban nowhere.
- **Stats of the week: The Eastern provinces account for 88% of exports and 77% of inward FDI.**

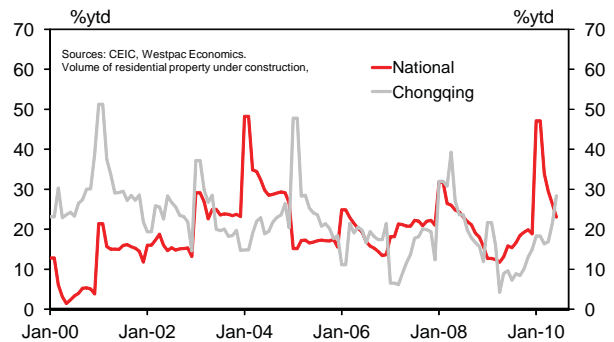
Phat dragon

a weekly chronicle of the Chinese economy

The NBS manufacturing PMI: headline



Residential investment in Chongqing



Chinese daily spot iron ore (TSI)

