



Major Price Indicators

- CPI growth falls in August
- Ex-factory prices of industrial products trend downward

Raw Material Prices

- Cotton price indices continue to fall
- Price index of viscose staple fiber trends upward
- Price index of ABS resin drops

Other Costs of Production

- Benchmark Qinhuangdao coal prices bottom out
- China Containerized Freight Index slides
- Chinese yuan appreciates against the US dollar in recent months

Highlights

- Minimum wage levels in Henan and Zhejiang are adjusted upward
- Fuel prices are adjusted four times between late June and mid-September
- Price index for US imports from China declines



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Part One: Major Price Indicators

1. CPI growth falls in August

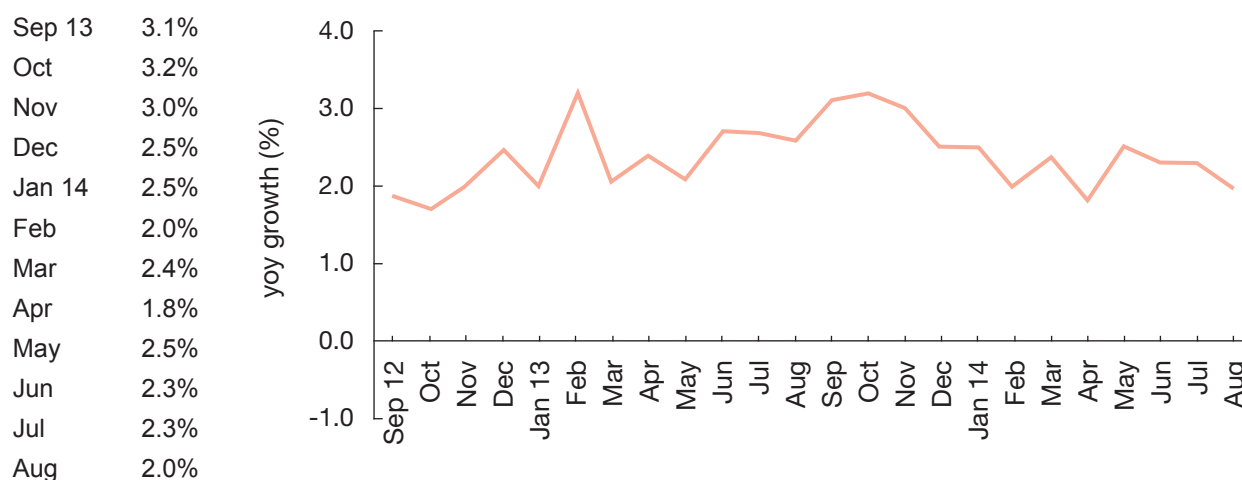
The yoy growth rate of China's consumer price index (CPI)¹ stayed stable at 2.3% yoy in June and in July, and then fell to 2.0% yoy in August.

The drop in the CPI growth in August was largely due to the slowing growth of food prices. The growth of the food component in the CPI went down from 3.6% yoy in July to 3.0% yoy in August. Meanwhile, the growth of the non-food component in the CPI was 1.5% yoy in August, compared to 1.6% yoy in July (see exhibits 1 and 2).

On a month-on-month (mom) basis, China's CPI gained 0.1% mom and 0.2% mom in July and August respectively.

Looking ahead, we expect the yoy growth of CPI to drop further in September, given the higher comparison base in September last year. CPI yoy growth may show a rebound afterwards, as pork prices will probably rise in October and November.

Exhibit 1: China's CPI growth, September 2012 to August 2014



Source: National Bureau of Statistics, PRC

Exhibit 2: China's CPI growth by commodity, March to August 2014

	yoy growth (%)					
	Mar 14	Apr	May	Jun	Jul	Aug
Clothing	2.3	2.3	2.5	2.6	2.6	2.6
Household services, maintenance and renovation	1.2	1.2	1.2	1.2	1.1	1.1
Recreational, educational products & services	2.1	2.0	2.1	2.1	2.1	1.9

Source: National Bureau of Statistics, PRC

¹ 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.

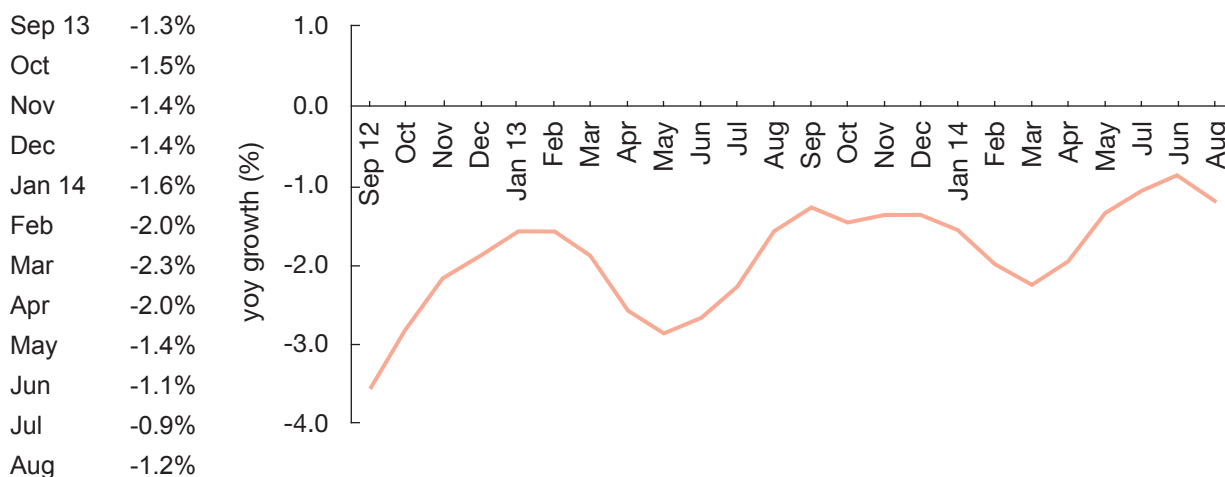
2. Ex-factory prices of industrial products continue to drop

The yoy growth rate for China's producer price index of industrial products (PPI)² rose all the way from minus 2.3% in May to minus 0.9% in July, before falling to minus 1.2% in August (see exhibits 3 & 4).

On a mom basis, the PPI fell by 0.2%, 0.1% and 0.2% in June, July and August respectively, indicating that ex-factory prices of industrial products have continued to drop.

Looking ahead, we expect China's PPI to stay low in the near term, especially as the domestic prices of production inputs remain soft.

Exhibit 3: China's PPI growth, September 2012 to August 2014



Source: National Bureau of Statistics, PRC

Exhibit 4: China's PPI growth by selected industry, March to August 2014

	yoy growth (%)					
	Mar 14	Apr	May	Jun	Jul	Aug
Textile industry	-0.2	-0.5	-0.4	-0.4	-0.3	-0.6
Textile and clothing	0.3	0.2	0.3	0.3	0.2	0.2
Timber processing & wood, bamboo, cane, palm fiber and straw products	0.5	0.6	0.9	1.3	1.3	1.3

Source: National Bureau of Statistics, PRC

² 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.

Part Two: Raw Material Prices

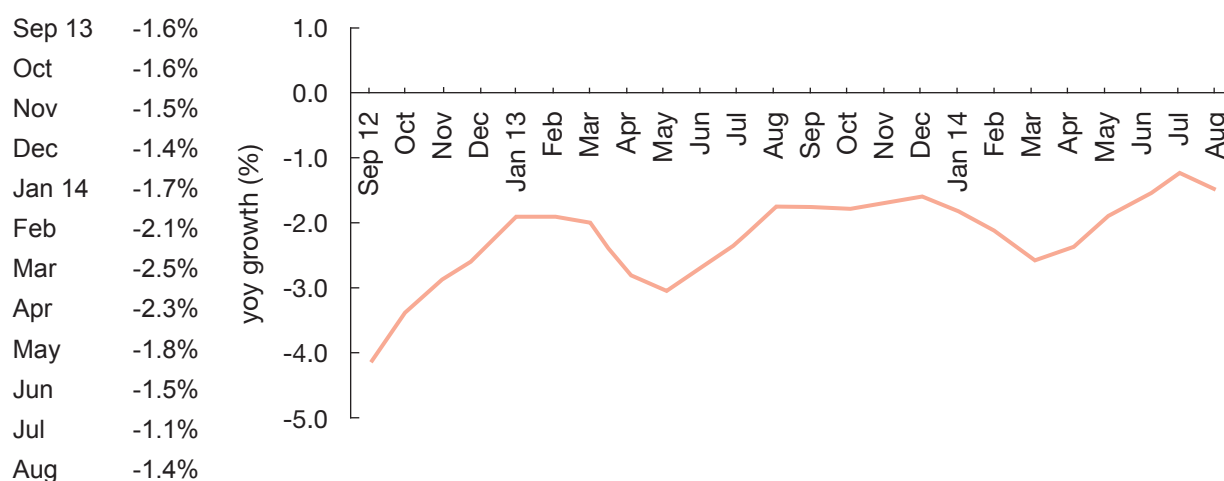
1. Domestic prices of production inputs drop in August

The yoy growth rate of the purchaser price index of industrial products went up all the way from minus 2.5% in March to minus 1.1% in July, before falling to minus 1.4% yoy in August (see exhibits 5 & 6). On a mom basis, after edging down by 0.1% in June, the purchaser price index stayed unchanged in July, and then dropped by 0.1% in August. These figures indicate the continued decrease in the domestic prices of production inputs.

It is noteworthy that the input prices sub-index of China's manufacturing PMI, a leading indicator of upstream prices, dropped below the neutral level of 50 in August.

Going forward, we expect the domestic prices of production inputs to fall further in the coming months, due to the weak domestic demand and the recent drop in global commodity prices.

Exhibit 5: Growth of China's purchaser price index of industrial products, September 2012 to August 2014



Source: National Bureau of Statistics, PRC

Exhibit 6: China's purchaser price index of industrial products by selected commodity, March to August 2014

	yoy growth (%)						
	Mar 14	Apr	May	Jun	Jul	Aug	
Fuel & power	-	-3.1	-2.7	-2.0	-1.3	-1.0	-1.6
Non-ferrous metals		-7.4	-6.1	-4.3	-3.6	-1.1	-1.5
Raw materials for the chemical industry		-2.6	-2.1	-1.8	-1.2	-0.5	-0.3
Timber and paper pulp		-0.8	-0.6	-0.7	-0.5	-0.4	-0.5
Textile raw materials		-0.6	-0.9	-1.0	-1.1	-1.1	-1.2

Source: National Bureau of Statistics, PRC

(i) Purchaser price index of fuel & power

The growth rate of the purchaser price index of fuel and power rose all the way from minus 3.1% yoy in March to minus 1.0% yoy in July, but then fell to minus 1.6% yoy in August (see exhibit 6).

(ii) Purchaser price index of non-ferrous metals

The growth rate of the purchaser price index of non-ferrous metals picked up from minus 3.6% yoy in June to minus 1.1% yoy in July, before sliding to minus 1.5% yoy in August (see exhibit 6).

(iii) Purchaser price index of raw materials for the chemical industry

The purchaser price index of raw materials for the chemical industry posted a slighter drop in recent months, down by 1.2% yoy, 0.5% yoy and 0.3% yoy in June, July and August respectively (see exhibit 6).

(iv) Purchaser price index of timber and paper pulp

The growth rate of the purchaser price index of timber and paper pulp has hovered around minus 0.5% yoy in the past few months (see exhibit 6).

(v) Purchaser price index of textile raw materials

The purchaser price index of textile raw materials posted negative yoy growth of minus 1.1% yoy, minus 1.1% yoy and minus 1.2% yoy in June, July and August respectively (see exhibit 6).

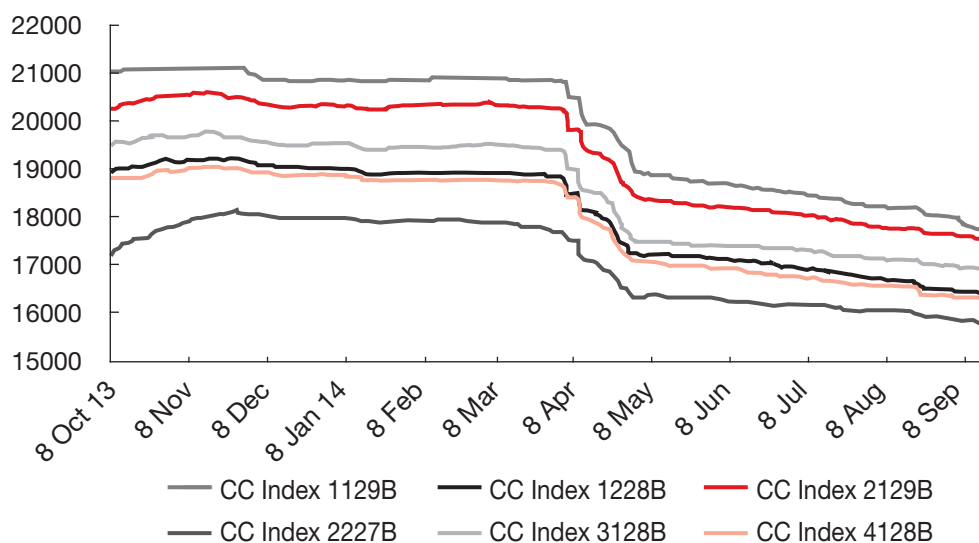
2. Cotton price indices continue to fall

The price indices³ of cotton have continued to trend downward in recent months. The CC Index 3128B, for example, fell to 16,825 on 19 September, compared to 17,332 on 30 June (see exhibit 7).

Looking ahead, the domestic cotton prices are set to stay low in the near term, amid the soft demand for cotton and the fall in global cotton prices. Nevertheless, we do not expect cotton prices to drop much, due to the decrease in domestic cotton output. At the press conference held by the National Development and Reform Commission (NDRC) on 22 September, a senior NDRC official suggested that China's total cotton output would drop by 0.5 million tonnes from the previous year to 6.5 million tonnes this year, owing to the reduction in cotton planting areas.⁴ Besides, the government has stopped selling its state reserves of cotton since September. In our view, the government will not restart selling its cotton reserves at least until the second quarter of next year.

³ The indices, compiled by the China Cotton Association, track cotton prices quoted from two hundred textile enterprises.
<http://www.china-cotton.org/>

⁴ http://www.china.com.cn/zhibo/2014-09/22/content_33570134.htm

Exhibit 7: China's cotton price indices, October 2013 to September 2014

*Since 8 October 2013, the China Cotton Association has officially published the price indices of cotton based on a new classification for cotton. The price indices based on the previous classifications for cotton (i.e. CC Index 229, CC Index 328 and CC Index 527) were discontinued on 8 October 2013.

Source: China Cotton Association

3. The Nanjing Wool Market Composite Index stays high

The Nanjing Wool Market Composite Index⁵, one of the major wool price indices in China, went up from 72.20 yuan per kg at end-May to 72.55 yuan per kg at end-June, and then stayed high at 72.53 yuan per kg at end-July (see *exhibit 8*). We believe that the wool prices were mainly supported by the relatively strong Australian dollar in June and July. The wool price index is significantly affected by the currency movement of the Australian dollar, as China imports a large amount of wool from the country, one of the major wool exporters in the world.

Going forward, the wool prices are set to trend downward in the near term, due largely to the recent depreciation of the Australia dollar against the Chinese yuan.

Exhibit 8: Nanjing Wool Market Composite Index, August 2013 to July 2014

	Aug 13	Sep	Oct	Nov	Dec	Jan 14	Feb	Mar	Apr	May	Jun	Jul
Month-end index (yuan/kg)	70.28	71.18	72.75	73.00	72.67	72.05	71.75	71.45	72.15	72.20	72.55	72.53

Source: The Nanjing Wool Market

⁵ <http://www.woolmarket.com.cn/>

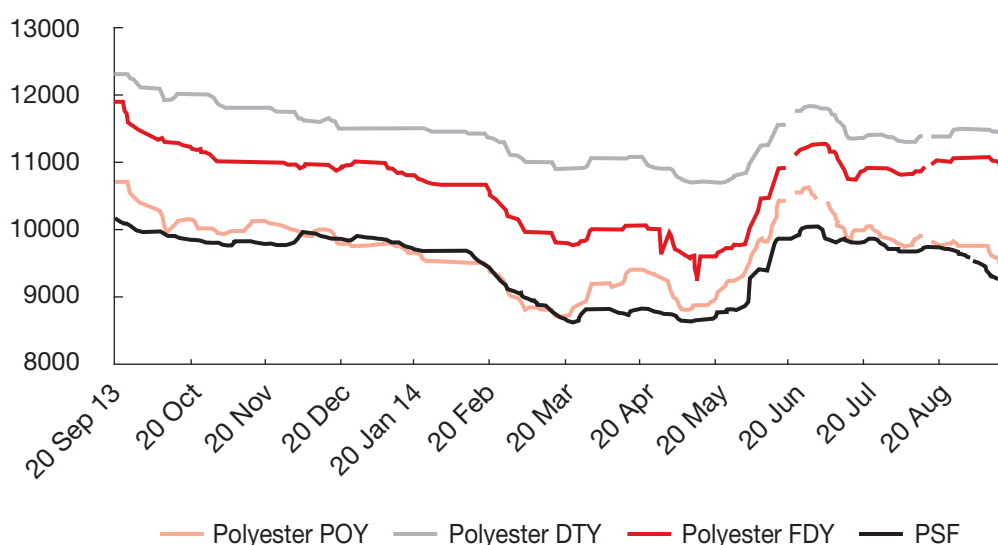
4. Price indices of polyester POY and PSF trend downward

After rising markedly between late May and late June, the price indices of polyester⁶ recorded a drop in the first half of July.

Since mid-July, the price trends of different types of polyester have diverged. For example, the price indices of polyester DTY and polyester FDY have shown a slight fluctuation. Meanwhile, the price index of polyester POY and PSF have been generally on a downward trend since late July (see exhibit 9).

Looking ahead, we expect the polyester prices to trend downward in the near term, due to the drop in upstream prices as well as the high stockpiles of polyester.

Exhibit 9: Price indices of polyester, September 2013 to September 2014



Source: China Chemical & Fiber Economic Information Network

5. Price index of acrylic staple fiber stays stable

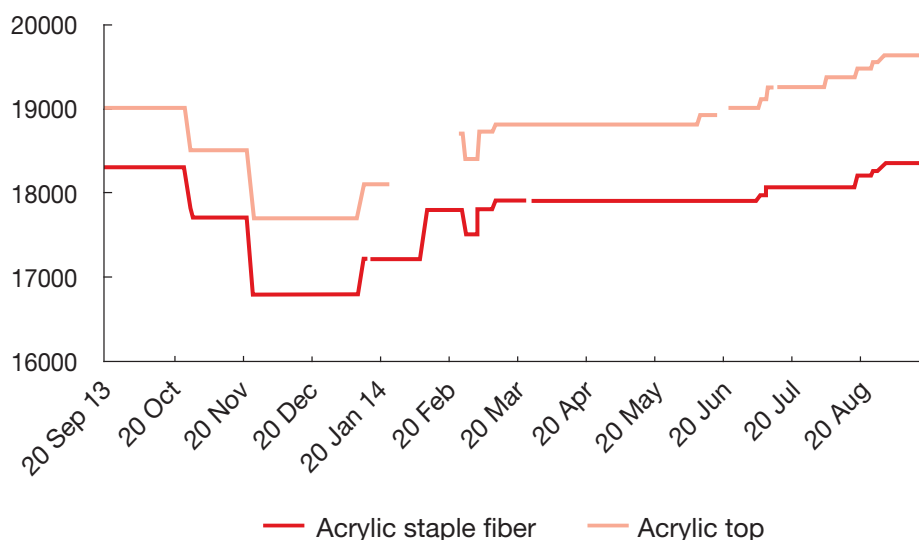
The price index of acrylic staple fiber⁷ rose from 17,900 on 7 July to 18,075 on 11 July, and then stayed flat until 19 August (see exhibit 10). Afterwards, the price index went up further to 18,350 on 1 September. We believe the rise in the prices of acrylic staple fiber was due largely to the increase in the prices of acrylonitrile, the major raw material of acrylic staple fiber, in July and August. Since early September, the price index has stayed stable again.

Looking forward, we think it is unlikely that the downstream demand for acrylic staple fiber will show significant improvement in the near term, and thus the future price movements of acrylic staple fiber will mainly depend on the price movements of acrylonitrile.

⁶ The indices are compiled by the China Chemical & Fiber Economic Information Network (CCFEI).

⁷ The indices are compiled by the China Chemical & Fiber Economic Information Network (CCFEI).

Exhibit 10: Price indices of acrylic, September 2013 to September 2014



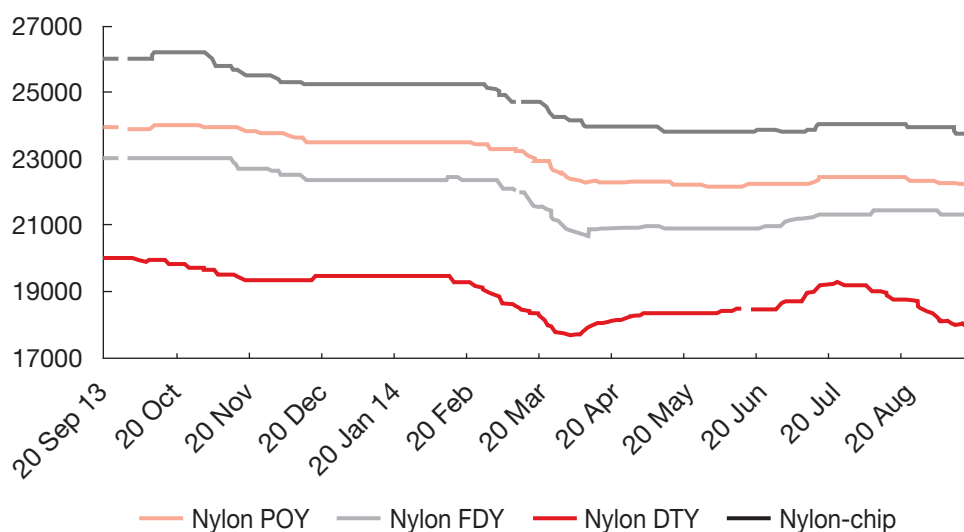
Source: China Chemical & Fiber Economic Information Network

6. Price indices of nylon FDY and nylon DTY stay relatively stable

Since early April, the price indices of nylon FDY and nylon DTY have stayed relatively stable (see exhibit 11).⁸ Nevertheless, the price index of nylon-chip rose all the way from 17,700 on 3 April to 19,250 on 23 July. The price index plateaued in following weeks, and has trended downward since early August, dropping all the way to 17,800 on 19 September.

It is noteworthy that the prices of caprolactam, one of the major raw materials of nylon, have been falling recently. We believe this will put downward pressure on nylon prices.

Exhibit 11: Price indices of nylon, September 2013 to September 2014



Source: China Chemical & Fiber Economic Information Network

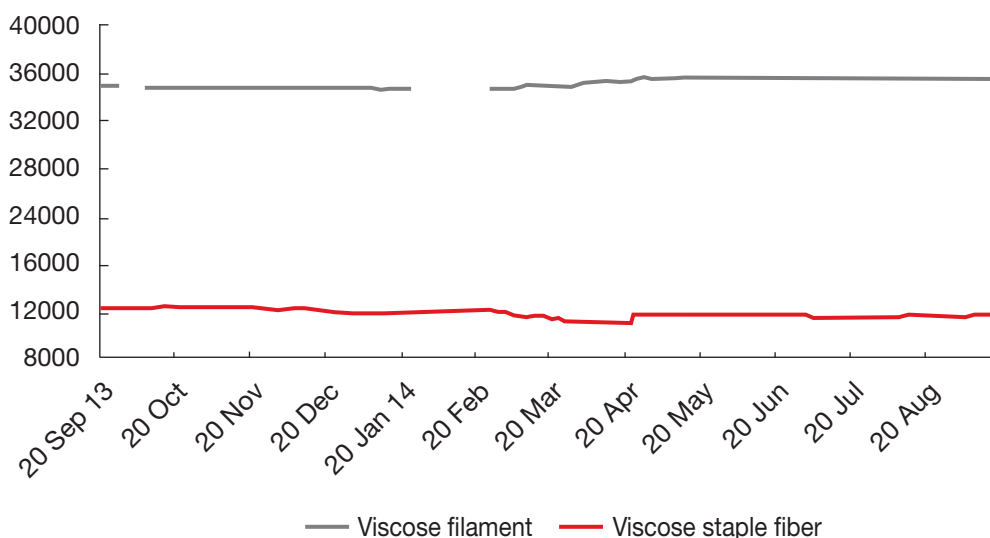
⁸ The index is compiled by the China Chemical & Fiber Economic Information Network (CCFEI).

7. Price index of viscose staple fiber trends upward

The price index of viscose staple fiber dropped from 12,030 on 20 June to 11,810 on 23 July, the lowest level since late April (see exhibit 12). The price index then stayed stable in the following week. Since early August, the price index has trended upward, rising all the way to 12,080 on 19 September.

According to the local media, the downstream demand for viscose staple fiber, albeit still weak, has shown improvement recently. Looking ahead, we expect the prices of viscose staple fiber to stay firm in the near term.

Exhibit 12: Price indices of viscose, September 2013 to September 2014



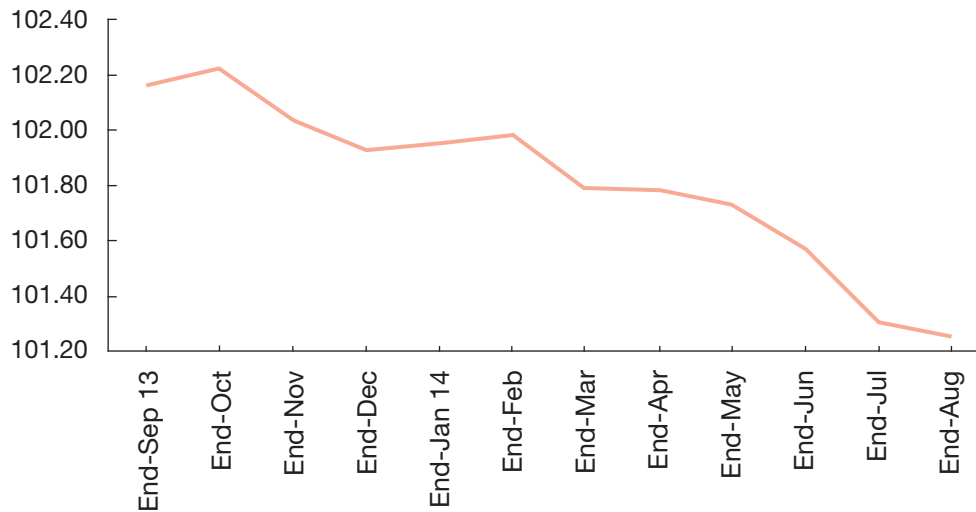
Source: China Chemical & Fiber Economic Information Network

8. Price index of silk trends downward

Caused mainly by the fall in prices of raw silk and the weak foreign demand for silk, the price index of silk has continued its downward trend in recent months. The price index dropped from 101.57 at end-June to 101.33 at end-July, and then edged down to 101.32 at end-August (see exhibit 13).

Looking ahead, silk prices are likely to stay soft in the near term. According to the local media, the foreign demand for silk has yet to show signs of recovery.

Exhibit 13: Price index of silk, September 2013 to August 2014



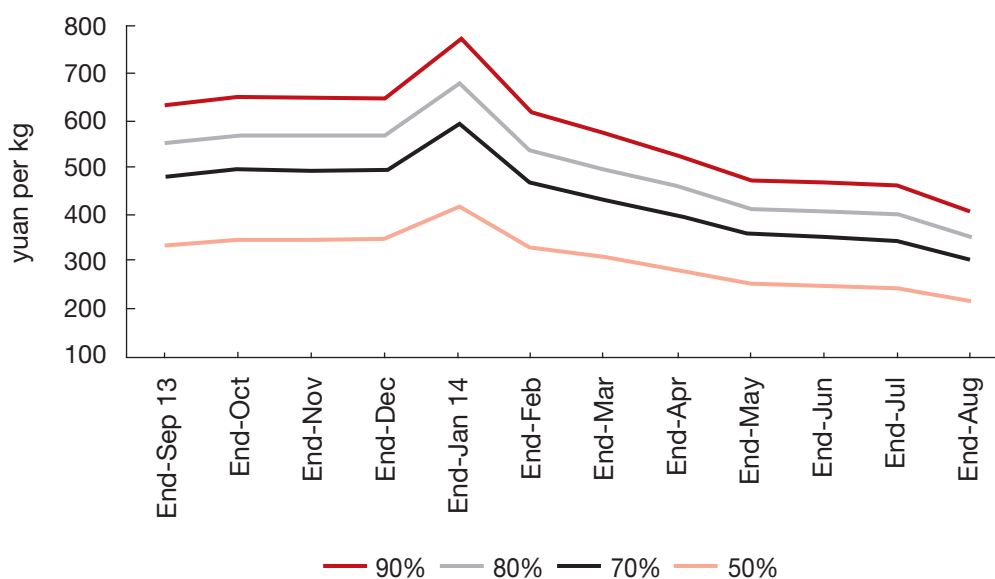
Source: Ministry of Commerce

9. Prices of various types of grey goose down fall

The prices of grey goose down have been falling in recent months (see exhibit 14). The price of 70% grey goose down, for instance, went down from 354.2 yuan per kilogram at end-June to 305.2 yuan per kilogram at end-August.

In our view, the drop in the prices of grey goose down was attributable to the sluggish downstream demand in the warm season. Looking ahead, we expect the grey goose down prices to stay low in the near future.

Exhibit 14: Prices of grey goose down, September 2013 to August 2014



Source: cn-down.com

10. Price index of ABS resin drops

The price index of ABS resin⁹ rose by 0.3% mom in June (see exhibit 15). Afterwards, the price index edged down by 0.1% mom in July and went down further by 1.0% mom in August, amid the weak downstream demand for ABS resin.

Going forward, the prices of ABS resin are likely to trend downward in the near term, due to the recent fall in the global prices of crude. (Acrylonitrile, butadiene and styrene, the major raw materials of ABS resin, are derived from petroleum.)

Exhibit 15: Price index of ABS resin, September 2013 to August 2014

	Sep 13	Oct	Nov	Dec	Jan 14	Feb	Mar	Apr	May	Jun	Jul	Aug
ABS resin (mom growth %)	-0.1	-0.5	-0.5	0.0	0.1	-0.5	-0.2	0.8	-0.2	0.3	-0.1	-1.0
ABS resin (yoy growth %)	-4.6	-5.3	-2.5	-1.1	-3.8	-6.6	-4.5	-1.2	-1.0	-1.4	-1.0	-1.9

Source: China Logistics Information Center

11. Price index of PP edges down in August

After gaining 1.2% mom in June, the price index of polypropylene (PP)¹⁰ rose further by 0.7% mom in July (see exhibit 16). The price index then edged down by 0.3% mom in August.

It is noteworthy that the domestic prices of crude, a major raw material of PP, have been on a downward trend in the past few months. For example, the Daqing crude price has fallen by 23.4% since late June (as of 8 October). The drop in crude prices is likely to put downward pressure on PP prices in coming months.

Exhibit 16: Price index of PP, September 2013 to August 2014

	Sep 13	Oct	Nov	Dec	Jan 14	Feb	Mar	Apr	May	Jun	Jul	Aug
PP (mom growth %)	7.7	1.6	2.0	2.1	-2.6	-3.7	-0.9	1.2	1.4	1.2	0.7	-0.3
PP (yoy growth %)	-3.2	-0.8	2.2	6.3	4.7	1.1	2.2	4.7	6.6	7.8	10.9	10.4

Source: China Logistics Information Center

⁹ The index is compiled by the China Logistics Information Center (CLIC). The CLIC is a sub-division of the China Federation of Logistics & Purchasing (CFLP), which is the first logistics and purchasing industry association approved by the State Council. One of the CFLP's missions is to push forward the circulation of factors of production in China.

¹⁰ The index is compiled by the China Logistics Information Center (CLIC).

12. Price index of natural rubber drops slightly in August

The price index of natural rubber¹¹ rose by 0.2% mom and 0.7% mom in June and July respectively, and then dropped slightly by 0.3% mom in August (see exhibit 17).

According to the media reports, the downstream demand for natural rubber has remained sluggish recently. Against this backdrop, it is likely that the prices of natural rubber will fall further in the near term.

Exhibit 17: Price index of natural rubber, September 2013 to August 2014

	Sep 13	Oct	Nov	Dec	Jan 14	Feb	Mar	Apr	May	Jun	Jul	Aug
Natural rubber (mom growth %)	6.4	0.3	-2.4	-1.5	-5.6	-8.0	-4.9	1.1	-4.3	0.2	0.7	-0.3
Natural rubber (yoy growth %)	-16.3	-21.0	-20.1	-20.9	-28.2	-34.2	-32.5	-24.3	-24.8	-20.2	-13.6	-19.3

Source: China Logistics Information Center

13. Prices of various types of non-ferrous metals trend upward

The price index of non-ferrous metals has continued its upward trend, gaining 0.3% mom, 3.1% mom and 1.3% mom in June, July and August respectively (see exhibits 18, 19, 20, 21 & 22).¹²

Looking forward, the uptrend of the prices of non-ferrous metals is unlikely to continue in near future. A major reason is that the domestic demand for non-ferrous metals has yet to show significant improvements. Besides, the recent rise in the prices of non-ferrous metals may encourage producers to increase their output, which will in turn increase the supply of non-ferrous metals.

Exhibit 18: Price index of non-ferrous metals, September 2013 to August 2014

	Sep 13	Oct	Nov	Dec	Jan 14	Feb	Mar	Apr	May	Jun	Jul	Aug
Non-ferrous metals (mom growth %)	0.4	0.6	-1.2	-0.9	0.0	-3.0	-4.1	1.8	3.5	0.3	3.1	1.3
Non-ferrous metals (yoy growth %)	-7.3	-6.6	-5.1	-6.9	-7.3	-9.6	-11.5	-7.9	-4.3	-3.5	1.6	1.5

Source: China Logistics Information Center

¹¹ The index is compiled by the China Logistics Information Center (CLIC).

¹² The indices are compiled by the China Logistics Information Center (CLIC).

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Exhibit 19: Price index of copper, September 2013 to August 2014

	Sep 13	Oct	Nov	Dec	Jan 14	Feb	Mar	Apr	May	Jun	Jul	Aug
Copper (mom growth %)	1.1	-0.8	-2.0	-0.3	1.8	-3.3	-8.4	3.0	4.4	-0.1	2.8	-1.1
Copper (yoy growth %)	-9.6	-10.9	-8.7	-10.2	-9.8	-12.5	-17.6	-11.7	-7.5	-5.1	0.4	-3.5

Source: China Logistics Information Center

Exhibit 20: Price index of aluminum, September 2013 to August 2014

	Sep 13	Oct	Nov	Dec	Jan 14	Feb	Mar	Apr	May	Jun	Jul	Aug
Aluminum (mom growth %)	0.1	1.3	-0.8	-1.2	-1.4	-5.3	-3.9	0.6	2.9	0.8	2.7	3.1
Aluminum (yoy growth %)	-6.9	-5.0	-4.5	-5.2	-6.0	-9.2	-11.8	-11.1	-8.9	-9.1	-4.8	-1.6

Source: China Logistics Information Center

Exhibit 21: Price index of lead, September 2013 to August 2014

	Sep 13	Oct	Nov	Dec	Jan 14	Feb	Mar	Apr	May	Jun	Jul	Aug
Lead (mom growth %)	0.5	-1.2	-0.6	-1.0	0.6	-0.6	-1.2	0.1	1.2	0.4	0.9	3.2
Lead (yoy growth %)	-7.3	-8.6	-5.8	-5.8	-5.1	-6.3	-5.5	-2.6	0.9	0.8	2.6	2.1

Source: China Logistics Information Center

Exhibit 22: Price index of zinc, September 2013 to August 2014

	Sep 13	Oct	Nov	Dec	Jan 14	Feb	Mar	Apr	May	Jun	Jul	Aug
Zinc (mom growth %)	-0.4	1.3	-0.4	-0.5	0.2	-0.3	-1.3	0.5	2.1	1.2	7.2	1.7
Zinc (yoy growth %)	-1.5	0.6	2.5	-1.2	-1.6	-3.3	-1.4	1.7	4.0	4.2	11.7	11.7

Source: China Logistics Information Center

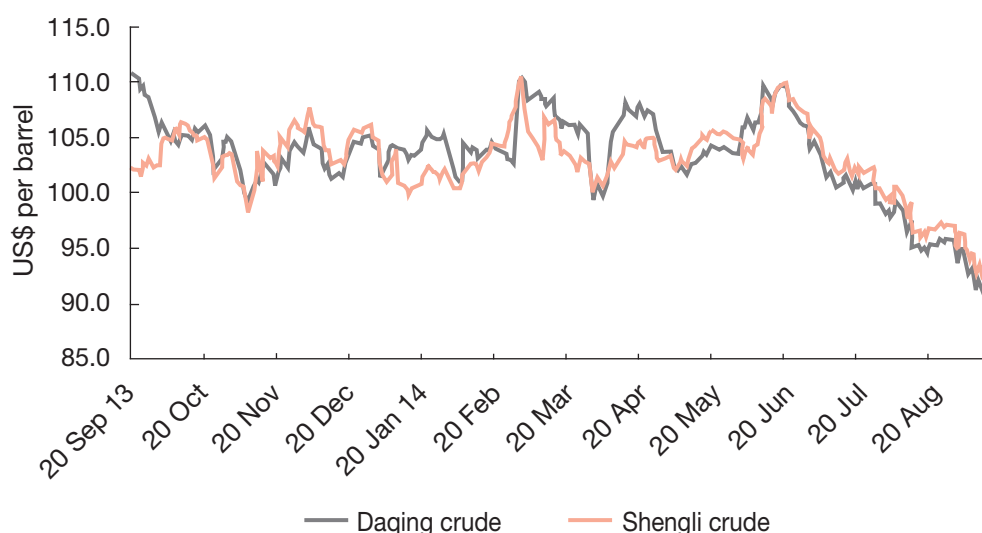
Part Three: Other Costs of Production (Energy, Transportation and Labour) and Exchange Rate

1. China's crude prices trend downward

In line with the movement of global crude prices, China's crude prices have been on a downward trend in recent months.¹³ The Daqing¹⁴ crude price, for example, fell from US\$ 109.6 per barrel on 23 June to US\$ 90.0 per barrel on 19 September (see exhibit 23).

According to the *Monthly Oil Market Report* published by the Organization of the Petroleum Exporting Countries (OPEC) in September, the global oil demand is predicted to increase by 1.05 million barrels a day in 2014.¹⁵ The report also projects that the non-OPEC oil production will rise by 1.68 million barrels a day in 2014. Also noteworthy is that the total crude output of OPEC, whose members supply about 33% of the world's crude oil, has been increasing in recent months, according to the secondary sources quoted by the report. We therefore expect that the growth of global oil output will outpace the growth of global oil demand, and that the global crude prices will stay low, in the near term.

Exhibit 23: China's crude prices, September 2013 to September 2014



Source: ifeng.com

2. Wholesale price index of refined oil products falls in August

After falling by 1.1% mom in June, the wholesale price index of refined oil products edged up by 0.1% mom in July, but then dropped again by 2.6% mom in August (see exhibit 24).¹⁶ The fluctuation in the price index was mainly driven by the government moves to adjust the prices of refined oil on 24 June, 22 July and 19 August, in our view.

¹³ From the year 2000 onwards, China's crude prices were determined with reference to global crude prices.

¹⁴ Daqing Field is the largest oil field in China.

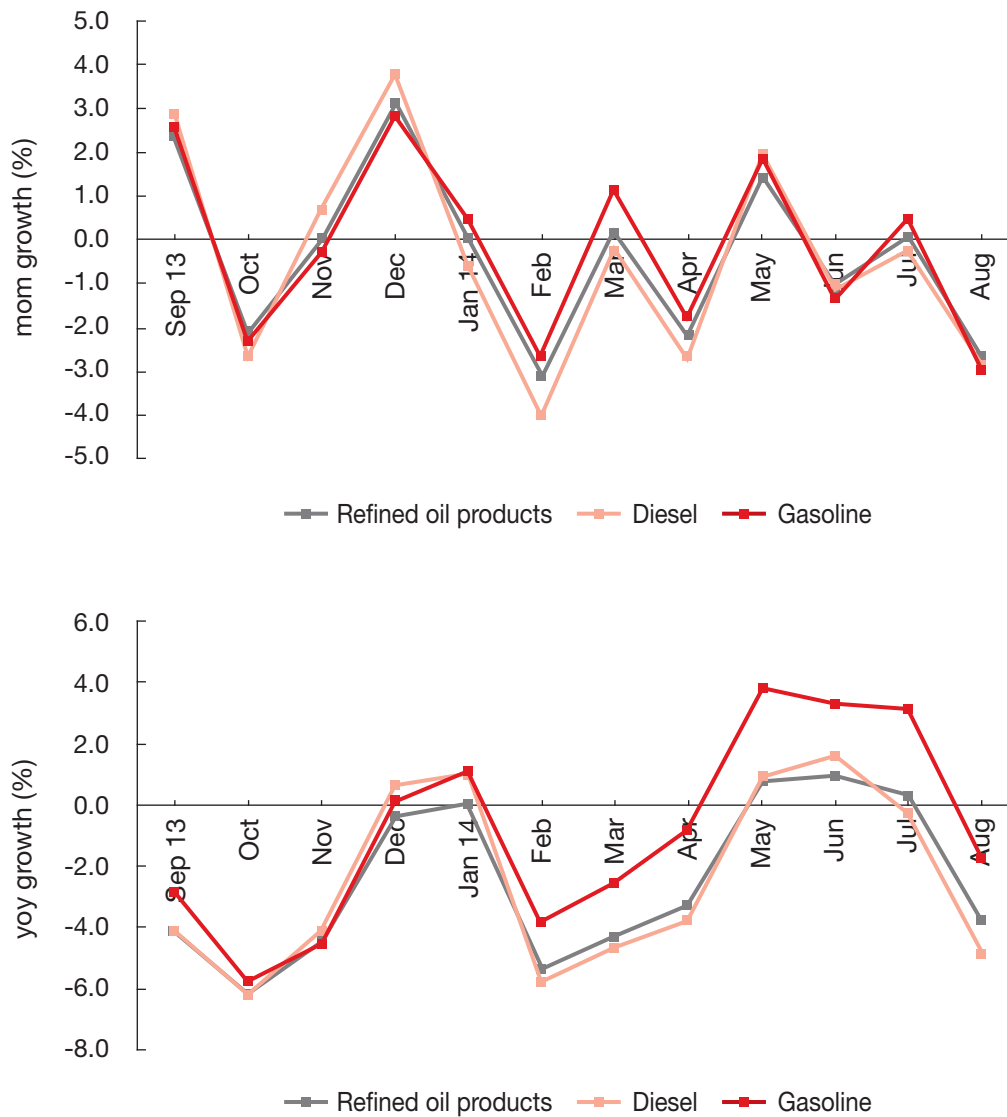
¹⁵ http://www.opec.org/opec_web/static_files_project/media/downloads/publications/MOMR_September_2014.pdf

¹⁶ The index is compiled by the China Logistics Information Center (CLIC).

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Looking ahead, the future movement of the wholesale prices of refined oil products will depend mainly on the movement of global crude prices. According to the pricing mechanism of refined oil, the fuel prices will be adjusted every 10 working days, based on the change in a basket of global crude prices. If the computed amount of fuel price change is less than 50 yuan per tonne, no adjustment will be made, and the amount will be accumulated for the next round of adjustment.

Exhibit 24: China's wholesale price indices of refined oil products, September 2013 to August 2014



Source: China Logistics Information Center

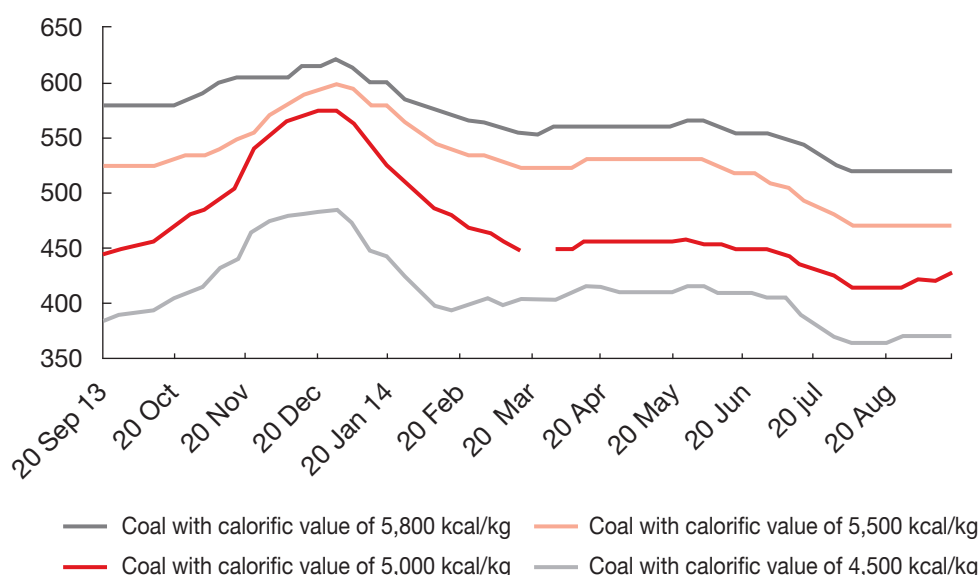
3. Benchmark Qinhuangdao coal prices bottom out

The benchmark Qinhuangdao coal prices trended downward from early July to early August, as major coal producers in China reduced the prices of their products in a bid to boost sales (see *exhibit 25*). The price of coal with calorific value of 5,800 kcal/ kg, for instance, went down from 555 yuan per tonne on 30 June to 520 yuan per tonne on 4 August, the lowest level since early October 2007.

Since early August, the benchmark Qinhuangdao coal prices have bottomed out. The price of coal with calorific value of 5,800 kcal/ kg has stayed stable at 520 yuan per tonne in recent weeks.

Looking ahead, we expect the domestic coal prices to stay low in the near term, amid the weak demand for coal. However, it is rumoured that, to support the coal sector, the Chinese government will control total output and imports of coal soon. In our view, if the government takes such actions, the domestic coal prices may show a rebound.

Exhibit 25: Qinhuangdao coal prices, September 2013 to September 2014



Source: Cqcoal.com

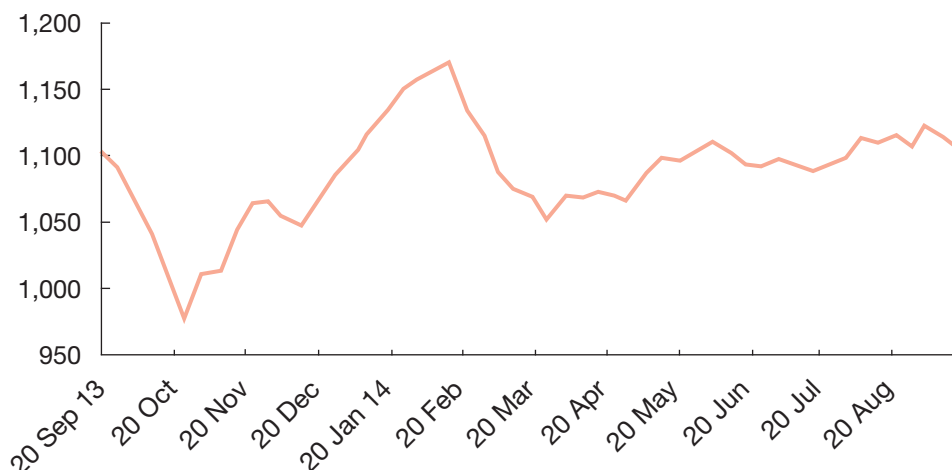
4. China Containerized Freight Index slides

After trending slightly downward from early June to mid-July, the China Containerized Freight Index (CCFI) showed a rebound in the following weeks (see *exhibit 26*). The index reached 1,121.48 on 5 September, the highest level since late February this year.

However, with major shipping companies expanding the active capacities of their carriers, the index has slid since early September, falling to 1,104.76 on 19 September.

Looking ahead, we expect the container freight rates to drop further in the near term, as the peak season generally ends in late September.

Exhibit 26: China Containerized Freight Index, September 2013 to September 2014



Source: Shanghai Shipping Exchange

5. Migrant workers' income gained 10.3% yoy as of end-June

According to the National Bureau of Statistics of China, the average monthly income of migrant workers in China rose to 2,733 yuan as of end-June, representing a growth of 10.3% yoy. The growth rate was close to the growth of 10.1% yoy recorded as of end-March, indicating that the wage growth of migrant workers stayed stable in 2Q14.

6. Chinese yuan appreciates against the US dollar in recent months

After depreciating against the US dollar in the first five months of 2014, the daily fixing rate (also known as the central parity rate) of the Chinese yuan showed a strong rebound in early June (see exhibit 27). The daily fixing rate appreciated from 6.1695 on 30 May to 6.1451 on 10 June, and has fluctuated within the range of 6.1425 to 6.1707 since then (as of 24 September).¹⁷ The USD-CNY spot exchange rate has risen since early June. The spot exchange rate went up to 6.1346 on 24 September, compared to the recent low of 6.2548 seen on 5 June.

The daily fixing rate of the Chinese yuan against the Euro has also appreciated in recent months (see exhibit 28). The daily fixing rate was 7.8988 on 24 September, compared to the recent low of 8.5756 on 7 May.

According to the Bank for International Settlements, the real effective exchange rate (REER) of the yuan has rebounded lately.¹⁸ The REER of the yuan rose all the way to 116.68 in August, after dropping from 114.68 in April to 113.95 in May, the lowest level since March 2013. Overall, the Chinese yuan depreciated by 1.7% in real terms against its trading partners in the first eight months of 2014 (see exhibit 29).

¹⁷ 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.

¹⁸ 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.

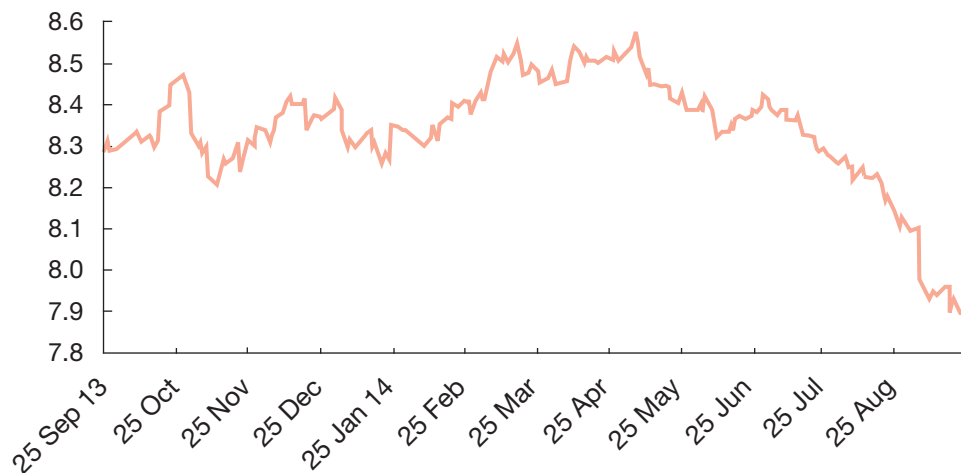
Going forward, we expect the appreciation of the Chinese yuan against the US dollar to continue in the near term, as the recent improvement in the Chinese economy may attract larger hot money inflows. Besides, China is likely to maintain the massive trade surplus, given the continuous recovery of the world economy. In the medium to long term, we maintain that the yuan will appreciate at a slow and gradual pace against the US dollar.

Exhibit 27: USD-CNY daily fixing rate, September 2013 to September 2014



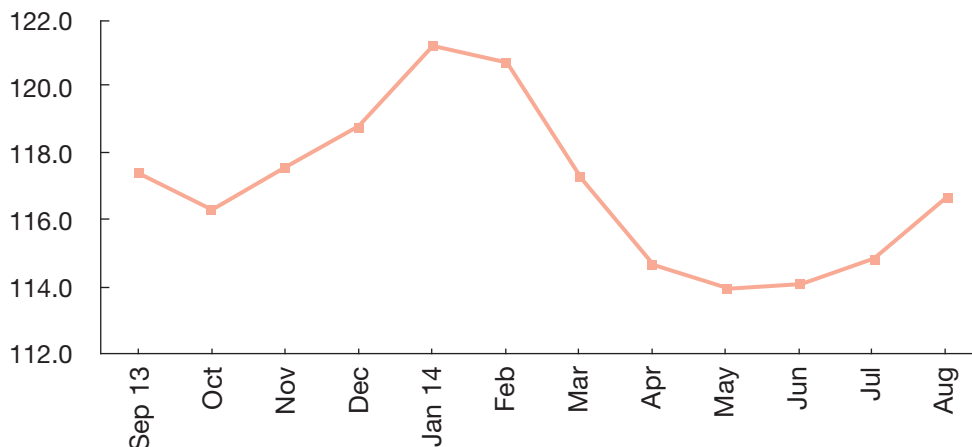
Source: State Administration of Foreign Exchange

Exhibit 28: EUR-CNY daily fixing rate, September 2013 to September 2014



Source: State Administration of Foreign Exchange

Exhibit 29: Real effective exchange rate of the Chinese yuan, September 2013 to August 2014



Source: Bank for International Settlements

Part Four: Highlights

1. Minimum wage levels in Henan and Zhejiang are adjusted upward

In recent months, the local governments in Henan and Zhejiang increased the minimum wage levels in their jurisdictions. See below for more details.

Henan province

Effective on 1 July 2014, the levels of minimum monthly wage in various regions within Henan province were adjusted upward to 1,400 yuan, 1,250 yuan and 1,100 yuan.¹⁹

Zhejiang province

On 1 August 2014, the levels of minimum monthly wage in various regions within Zhejiang province were raised to 1,650 yuan, 1,470 yuan, 1,350 yuan and 1,220 yuan respectively, up from the previous levels of 1,470 yuan, 1,310 yuan, 1,200 yuan and 1,080 yuan respectively.²⁰

In accordance with the 12th Five-year Plan, the minimum wage levels in China are targeted to rise by at least 13% per annum during 2011-2015. So far this year, the local governments in 16 of the 31 provinces/municipalities/autonomous regions in the country have raised the minimum wage levels in their jurisdictions. We expect that the minimum wage levels in some more provinces, municipalities or autonomous regions will be increased in the rest of this year.

19 http://www.chinajob.gov.cn/LabourRelations/content/2014-07/31/content_959422.htm

20 http://zfxgk.zj.gov.cn/xxgk/jcms_files/jcms1/web57/site/art/2014/8/1/art_9501_55641.html

2. Local governments in a few provinces issue new guidelines on salary rise

Over the past few months, local governments in provinces such as Guizhou, Fujian, Jiangxi and Jilin issued new guidelines on salary rise (see *exhibit 30*).

For instance, according to the announcement issued by the Guizhou provincial government, enterprises with improving performance in the province are recommended to raise the salaries of their workers by around 12%, the pay rise benchmark for 2014. Enterprises with good performance are recommended to offer pay rise of at most 15.2% to their workers in 2014; while enterprises with worsening performance should consider raising the salaries of their workers by at least 2.7%, the lower limit of the pay rise benchmark.²¹

Although these guidelines are not mandatory for employers to follow, they will affect workers' expectations of salary rise and are thus regarded as an important reference.

Exhibit 30: Guidelines on salary rise issued by local governments, June to September 2014

Province/ municipality/autonomous region	Upper limit	Benchmark	Lower limit	Issue date
Guangzhou	17%	11%	5%	June 2014
Guizhou	15.2%	12%	2.7%	June 2014
Fujian	17%	12%	3.5%	August 2014
Hebei	22%	14%	6%	August 2014
Jiangxi	-	14%	6%	August 2014
Jilin	16%	12%	4%	August 2014

Source: Announcements by various local governments

3. Fuel prices are adjusted four times between late June and mid-September

In response to the price movements of global crude oil between late June and mid-September, the Chinese government cut maximum retail prices of gasoline and diesel on 22 July, 19 August, 1 September and 17 September. Overall, maximum retail prices for gasoline and diesel have been reduced by 6.8-8.3% after these four adjustments. The fall in fuel prices is set to decrease transportation costs, as well as the energy costs of manufacturers who run their own electrical generators.

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 22 working days and the 4% price change threshold has been removed, the Chinese government has adjusted fuel prices more frequently under the new pricing mechanism.

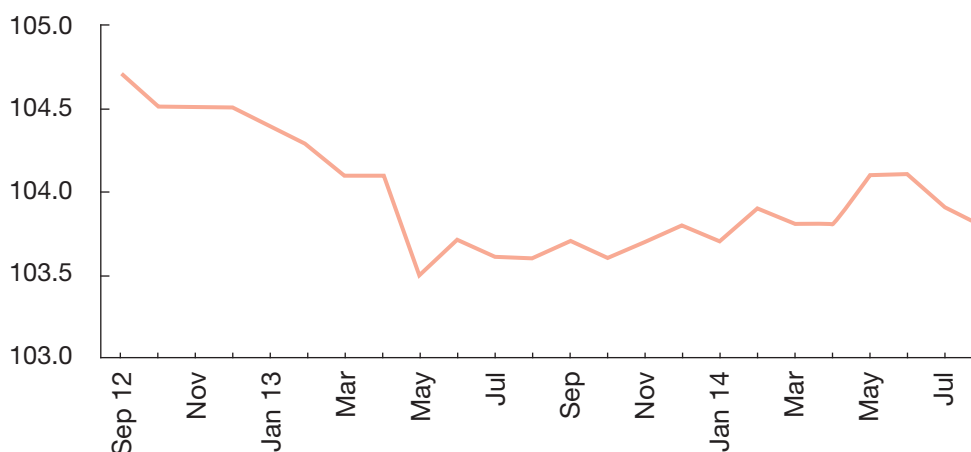
²¹ <http://www.chinanews.com/sh/2014/06-19/6298142.shtml>

4. Price index for US imports from China drops

Compiled by the US Department of Labor, the price index for US imports from China dropped from the recent peak of 104.1 in June to 103.9 in July and 103.8 in August (see exhibit 31). Also noteworthy is that, as compared to the same month of the previous year, the index gained 0.2 points in August.

Going forward, we expect the price index to fall further in the near term, as the downtrend of the ex-factory prices of Chinese products is likely to continue.

Exhibit 31: Price index for US imports from China, September 2012 to August 2014



Source: US Department of Labor

5. China's exports post high single-digit growth in August

China's export growth improved from 7.2% yoy in June to 14.5% yoy in July, and then stayed high at 9.4% yoy in August (see exhibits 32, 33 and 34). Export demand has continued to strengthen. Overall, in the period January to August, China's exports amounted to US\$ 1,483.5 billion, up by 3.8% yoy. Over the same period, China's exports to the US and the EU posted positive growth of 7.0% yoy and 10.9% yoy respectively, showing relatively strong demand from the major developed economies.

China's trade surplus increased from US\$ 31.6 billion in June to US\$ 47.3 billion in July, before rising further to the record high of US\$ 49.8 billion in August. The marked increase in exports was the main reason behind the rising trade surplus. In our view, the massive trade surplus in recent months is likely to cause intense international pressure for renminbi appreciation. Against this backdrop, the appreciation of the Chinese yuan against the US dollar is set to continue in the near term.

Looking ahead, we expect that China's exports will register high single-digit growth in coming months, due largely to improving demand from the advanced economies.

Exhibit 32: China's quarterly foreign trade data, 3Q13 to 2Q14

USD billion (yoy growth)

	Exports	Imports	Trade Balance
FY13	2,210.0 (7.9%)	1,950.3 (7.3%)	259.8
3Q13	562.2 (3.9%)	500.7 (8.4%)	61.5
4Q13	595.3 (7.5%)	504.8 (7.2%)	90.5
1Q14	491.3 (-3.4%)	474.6 (1.6%)	16.7
2Q14	570.8 (4.9%)	484.9 (1.4%)	85.9

Source: China Customs

Exhibit 33: China's monthly foreign trade data, September 2013 to August 2014

USD billion (yoy growth)

	Exports	Imports	Trade Balance
September 13	185.6 (-0.3%)	170.4 (7.4%)	15.2
October	185.4 (5.6%)	154.3 (7.6%)	31.1
November	202.2 (12.7%)	168.4 (5.3%)	33.8
December	207.7 (4.3%)	182.1 (8.3%)	25.6
January 14	207.1 (10.6%)	175.3 (10.0%)	31.9
February	114.1 (-18.1%)	137.1 (10.1%)	-23.0
March	170.1 (-6.6%)	162.4 (-11.3%)	7.7
April	188.5 (0.9%)	170.1 (0.8%)	18.4
May	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

Source: China Customs

Exhibit 34: Growth rates of exports and imports, September 2012 to August 2014

Source: China Customs



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