

# GBA – Survey confirms recovery momentum intact

- Current sentiment index eased to the 50 neutral mark after strong Q1 jump, mirroring softer macro data
- Expectations and credit indices point to further recovery in Q3 as city and industry performances diverge
- Respondents see a broadening range of drivers for supply chain management and factory relocation

## Keep moving after a Q2 slowdown

Our GBA Business Confidence Index (GBAI), based on quarterly surveys of over 1,000 companies operating in the Guangdong-Hong Kong-Macau Greater Bay Area (GBA) and conducted in collaboration with the Hong Kong Trade Development Council (HKTDC), shows that the current performance of ‘business confidence’ eased to 50.0 in Q2-2023 after a strong jump to 51.3 in Q1 (Figures 1 and 2). We had expected a notable q/q drop in our Q2 sentiment gauge, given (1) normalisation of base effects; (2) softening of nationwide macro data QTD; and (3) that the novelty of reopening was bound to wear off. That said, the current headline print managed to avoid slipping into contractionary territory, which together with our GBAI expectations staying elevated at 58.7 suggests a mere setback rather than an end to the post-COVID recovery. Furthermore, respondents expect their cash-flow positions to continue improving in Q3, another indication of no entrenched pessimism setting in; that said, other credit sub-indices do confirm that keeping monetary conditions loose and borrowing costs low to ‘defend the bottom line’ would not hurt either.

**Kelvin Lau**  
 +852 3843 0711  
 Kelvin.KH.Lau@sc.com  
 Senior Economist, Greater China  
 Standard Chartered Bank (HK) Limited

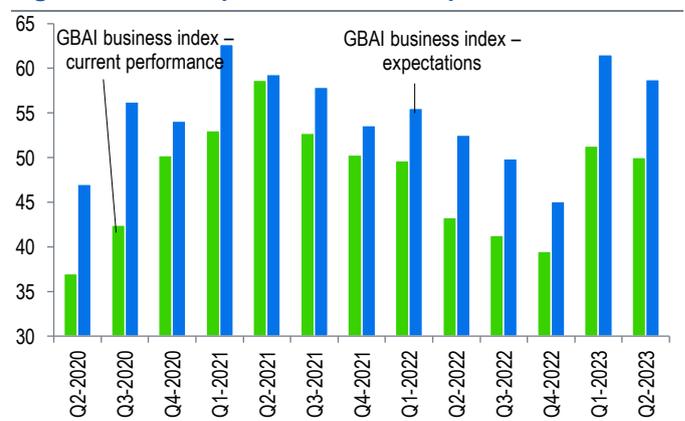
A further breakdown showed more differentiated Q2 performance across industries and cities after a quarter of uniform increase. Most notably, Shenzhen weathered weaker responses from its tech respondents by posting the highest score for ‘manufacturing and trading’ among all city sub-indices. Guangzhou and Hong Kong outperformed Shenzhen across the other four industry sub-indices, despite weaker headline prints. For thematic questions, we took a closer look at how GBA companies are responding to global supply chain migration, and more specifically what their plans are for overseas factory relocation and tapping RCEP opportunities.

Figure 1: GBAI business index and its sub-components

	Current performance			Expectations		
	Q2-2023	Q1-2023	Q4-2022	Q2-2023	Q1-2023	Q4-2022
<b>Business index</b>	<b>50.0</b>	51.3	39.5	<b>58.7</b>	61.5	45.1
1. Production/sales	49.4	49.7	38.4	63.1	67.8	45.1
2. New orders	49.8	53.1	36.9	60.8	67.1	47.6
3. Capacity utilisation	49.9	49.8	42.0	59.8	60.2	47.1
4. Raw material inventory	47.1	46.3	31.8	53.6	54.0	36.8
5. Prices of finished goods/services	51.9	54.3	52.2	59.7	60.5	52.1
6. Fixed asset investment	52.9	53.6	43.8	58.7	57.9	47.7
7. Financing scale	49.3	51.0	30.9	51.7	55.3	35.6
8. Profit	49.9	52.5	40.1	62.7	69.0	48.7

Source: HKTDC, Standard Chartered Research

Figure 2: ‘Current performance’ vs ‘expectations’ indices



Source: HKTDC, Standard Chartered Research

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## Detailed findings of the GBAI survey for Q2-2023

### *The Q2 dip in GBAI was expected*

In our last report, we warned that the strong performance of our GBAI in Q1-2023, while providing a much-welcomed confirmation of China's swift post-COVID sentiment rebound, could be difficult to repeat going forward. For one, the record q/q jumps in our headline GBAI indices in the previous quarter were amplified by the very low Q4-2022 base. We also noted that the performance of our wide range of GBAI sub-indices could become more differentiated after a quarter of uniform increases, especially with the fading of reopening tailwinds.

The softer set of Q2 GBAI readings were therefore not a surprise. If anything, the readings could have been worse, considering that softer nationwide macro data QTD has fuelled market concerns about the sustainability of China's recovery and calls for more policy stimulus. Our Q2 headline index for current performance managed to stay neutral at 50.0, confirming a slowdown but no outright contraction.

More importantly, the more forward-looking headline GBAI expectations index remained comfortably in expansionary territory (58.7), suggesting no entrenched negative sentiment among our 1,000+ GBA business respondents. And given that GBA is a microcosm of China's diverse economic drivers making it a bellwether for overall growth, we see China managing to stay on a modest recovery path, helped by more policy support to weather lingering drags from a weak housing market, soft consumer confidence, and an uncertain external demand backdrop.

For our thematic questions this time, we looked at supply chain transformation in the region – from the shift in potential drivers for such changes to the willingness and urgency to relocate some of their production capacity overseas. We also asked respondents how ready they are to tap RCEP-related opportunities.

We list below the detailed findings from our latest GBAI survey:

### *Headline index eased but managed to stay neutral; this along with resilient investment appetite are the bright spots*

- **Falling current performance index masks diverse performance of underlying sub-indices:** The GBAI current performance index for business activity eased to 50.0 in Q2-2023, after a strong jump to 51.3 in Q1; this was expected as the prior rally was boosted by a low base, having fallen six straight quarters to 39.5 in Q4-2022. However, the index did not fall back into contractionary territory, suggesting only a softening of the recovery momentum rather than an end to the recovery, in our view.

The performance of underlying sub-indices was also more diverse this quarter after a more uniform increase in Q1. Six sub-indices had sub-50 prints this time, up from three previously (Figure 1). 'Raw material inventory' remained the lowest-scoring component at 47.1 (despite improving q/q), suggesting lingering destocking pressure this quarter. 'New orders' (-3.3pts to 49.8) and 'profits' (-2.5pts to 49.9) saw the largest q/q drops, but managed to stay a hair away from the 50 neutral mark, which was a relief amid the recent data setback.

On a more positive note, 'prices of finished goods/services' stood at an expansionary 51.9 (albeit down 2.4pts from Q1), suggesting only modest disinflationary pressure amid a lingering negative output gap, rather than entrenched deflation. 'Fixed asset investment' had the highest score of 52.9 among components, suggesting that respondents remain optimistic towards the longer-term GBA business outlook, by acknowledging the need to invest in capacity expansion in anticipation of further demand normalisation.



## On the Ground

**Headline expectations index still standing at the second highest level in two years**

- **Expectations indices point to a continued recovery:** The GBAI expectations index for business activity eased to 58.7 in Q2 from 61.5 prior. However, this is still the second highest reading in two years (or the third highest on record since the index was inaugurated in Q2-2020), consistent with more expansionary momentum in the coming quarter (Figure 2). A further breakdown showed that the headline deterioration was mostly driven by the sub-indices more reflective of short-term business performance, namely 'expected production/sales' (-4.7pts), 'expected new orders' (-6.3pts) and 'expected profits' (-6.3pts). Despite such drops, these sub-indices managed to maintain a 60+ score, making them outperformers for a second straight quarter. All this suggests a normalisation following the boost from a favourable base previously, rather than an outright setback.

Other expectations sub-indices also showed resilience, including 'expected capacity utilisation' (-0.4pts), 'expected raw material inventory' (-0.4pts) and 'expected fixed asset investment' (+0.8pts). The outperformance of 'expected fixed asset investment', like its current performance counterpart, was particularly encouraging, indicating little loss of 'animal spirits' to invest among businesses, contrasting weaker consumer and market confidence.

We recently lowered our Q2 and 2023 GDP growth forecasts for China to 5.8% y/y and 5.4%, respectively, from 7% and 5.8% previously, to reflect weaker-than-expected growth in April-May. We maintained our Q3 and Q4 growth forecasts at 5.5% y/y and 5.9% y/y, respectively, expecting improving consumer confidence and less of a drag from the housing market. Our forecast also assumes that China will likely introduce additional (albeit still measured, given the not-too-challenging official GDP growth target of 5.0% for 2023) policy support to safeguard a continued economic recovery. Note that our survey was conducted between early May and early June, before the People's Bank of China's (PBoC's) latest round of interest rate cuts, which has since boosted market expectations of more stimulus roll-out.

- **Credit conditions could loosen further:** The current performance index for credit fell to 49.3 in Q2 after rising for a third straight quarter to 51.6 in Q1 (Figure 3). The breakdown shows q/q deterioration across four of the five components, with 'non-bank financing costs' being the exception (+1.7pts to 49.5), although a below-50 reading still means rising costs. 'Bank financing costs', which deteriorated a second straight quarter to 46.9, saw more evident pressure. Softer growth also led to slower receivables turnover (48.9 vs 53.9 prior), although respondents continued to see improving cash surplus (51.2 vs 52.9 prior). All this,

**Figure 3: Respondents expecting better cash flow but higher borrowing costs**  
*Five sub-components of our GBAI credit indices – current vs expectations*

**Latest survey has yet to capture recent PBoC rate cut**

	Current performance			Expectations		
	Q2-2023	Q1-2023	Q4-2022	Q2-2023	Q1-2023	Q4-2022
<b>Credit Index</b>	<b>49.3</b>	<b>51.6</b>	<b>48.6</b>	<b>51.6</b>	<b>54.2</b>	<b>50.6</b>
1. Bank financing cost *	46.9	48.6	52.2	42.6	44.8	52.5
2. Non-bank financing cost *	49.5	47.8	53.8	43.8	47.2	52.6
3. Banks' attitude towards lending	50.1	54.8	45.6	54.9	58.4	46.9
4. Surplus cash	51.2	52.9	44.5	60.0	62.8	51.3
5. Receivables turnover	48.9	53.9	46.9	56.6	57.7	49.9

\* Index above 50 indicates lower cost; Source: HKTDC, Standard Chartered Research



## On the Ground

together with the perceived neutral-at-best lending attitude by banks (50.1), likely prompted the PBoC to cut interest rates this month in its latest attempt to preserve growth momentum and improve the overall business climate.

### *Respondents are expecting their cash-flow positions to stay healthy*

Looking ahead, however, with lending rates already at historical lows and credit growth significantly outpacing nominal GDP growth, the marginal effectiveness of further policy rate cuts is likely to diminish, in our view. For this reason, we see the PBoC merely cutting the reserve requirement by 25bps in Q3 (rather than calling for bigger stimulus) to keep liquidity ample, while maintaining relatively fast credit growth and accommodating potential issuance of more local special bonds. Most respondents agreed that there appears little room for a substantial lowering of borrowing costs for now, with the corresponding expectations sub-indices falling further below 50 in Q2. Despite such drags, the headline expectations indices for credit managed to stay expansionary (51.6) in Q2, thanks to further (albeit more moderate) improvements across the ‘banks’ attitude towards lending’ (54.9), ‘surplus cash’ (60.0) and ‘receivables turnover’ (56.6) components. Healthy cash-flow expectations likely reflect sanguine underlying growth expectations among our respondents; this could also provide an alternative explanation for GBA companies’ perceived lack of urgency to borrow (as opposed to the usual claim of a lack in confidence or funding availability).

### *Innovation and technology underperformed, possibly reflecting lingering macro and geopolitical challenges*

- **A very mixed bag of results among industry sub-indices:** All but one of our 10 industry sub-indices for business activity (five industries, each having their own current performance and expectations sub-indices) fell q/q, in line with the headline trend (Figure 4). The exception to this was the current performance index for ‘professional services’, which rose another 4.0pts to an industry-best 56.1 following a decent rebound in Q1; the sector’s expectations index also outperformed by being the lone print above the 60 mark (61.9). Beyond that, retailers and wholesalers (51.2) appeared slightly more upbeat compared with manufacturers and traders (49.9) when it came to gauging ‘current performance’. That said, the latter posted a higher expectations score (59.1, versus 58.3 for ‘retail and wholesale’).

**Figure 4: GBAI business sub-indices by sector**

Business activity	Current performance			Expectations		
	Q2-2023	Q1-2023	Q4-2022	Q2-2023	Q1-2023	Q4-2022
Manufacturing and trading	49.9	51.0	39.0	59.1	61.3	44.3
Retail and wholesale	51.2	51.4	42.2	58.3	61.2	48.8
Financial services	51.5	59.8	45.4	54.8	67.4	50.5
Professional services	56.1	52.1	38.5	61.9	65.2	46.1
Innovation and technology	43.7	54.3	42.5	49.0	61.0	49.8

Source: HKTDC, Standard Chartered Research

**Figure 5: GBAI credit sub-indices by sector**

Credit	Current performance			Expectations		
	Q2-2023	Q1-2023	Q4-2022	Q2-2023	Q1-2023	Q4-2022
Manufacturing and trading	49.0	51.5	48.5	51.4	54.1	50.7
Retail and wholesale	51.2	52.5	49.0	51.9	54.4	49.9
Financial services	46.5	53.4	46.9	50.3	56.2	52.4
Professional services	52.1	49.9	49.1	53.8	53.7	49.3
Innovation and technology	52.5	50.0	53.1	55.3	54.4	54.8

Source: HKTDC, Standard Chartered Research

## On the Ground

'Financial services' (-8.3pts and -12.6pts for 'current performance' and 'expectations', respectively) and 'innovation and technology' (-10.6pts and 11.9pts) saw the largest q/q drops among sectors. Margin pressures and credit worries amid easing recovery momentum likely weighed on financial respondents' sentiment; but their scores remained comfortably in expansionary territory. Technology respondents, on the other hand, saw their sub-indices dipping back below 50 in Q2 after a brief Q1 surge. This confirms that the tech sector continues to face many headwinds, led by the ongoing global semiconductor downcycle keeping the demand outlook from turning the corner any time soon. The weak global demand has caused a sizeable YTD decline in China's exports of a number of electronic products like computers and mobile phones to overseas markets. And then there is also the US' recent tightening of semiconductor export controls, have also adversely affected the sector's business sentiment.

***Shenzhen outperformed despite headwinds on the innovation and technology front***

- More recovery ahead across GBA cities:** In our last report, we noted that during the early months of GBA's post-COVID rebound, no cities were left behind – all six of our GBA city sub-indices staged strong Q1 q/q jumps after the speedy reopening of borders, allowing cities to share the substantial boost from each other's COVID policy pivots and the resulting economic normalisation. For Q2, we saw more diverse city performance among the current performance sub-indices (Figure 6). Most notably, Shenzhen and Dongguan improved for a second straight quarter and were the only ones remaining above 50, while other city sub-indices fell. Shenzhen weathered weaker responses from its tech respondents by posting the highest score for 'manufacturing and trading' among all city sub-indices. Guangzhou and Hong Kong, the other two GBA core cities, outperformed Shenzhen across the other four industry sub-indices.

In any case, we continue to take comfort from the fact that all city expectations indices stood comfortably in the 50+ expansionary territory, consistent with our view of a sustained recovery momentum in the coming quarters. That includes Hong Kong, which despite returning to the lowest score of the pack, still managed to record a solid 54.7 expectations print (led by retail and professional services), making it two straight quarters of expansion.

**Figure 6: GBAI business sub-indices by city**

Business activity	Current performance			Expectations		
	Q2-2023	Q1-2023	Q4-2022	Q2-2023	Q1-2023	Q4-2022
Hong Kong	49.3	51.6	41.7	54.7	58.7	48.4
Guangzhou	48.6	49.9	37.6	55.7	67.7	43.1
Shenzhen	51.9	51.5	38.8	60.4	60.8	47.1
Foshan	47.6	55.1	43.9	58.5	59.0	44.2
Dongguan	56.4	53.5	34.5	64.3	69.6	37.1
Macau and other cities	43.6	48.9	41.9	58.0	56.8	42.8

Source: HKTDC, Standard Chartered Research

**Figure 7: GBAI credit sub-indices by city**

Credit	Current performance			Expectations		
	Q2-2023	Q1-2023	Q4-2022	Q2-2023	Q1-2023	Q4-2022
Hong Kong	47.2	51.5	45.9	49.3	51.8	48.4
Guangzhou	51.9	52.4	47.6	51.9	54.7	49.1
Shenzhen	48.2	51.8	50.7	52.1	55.9	54.4
Foshan	49.6	49.9	47.5	51.9	53.1	49.2
Dongguan	50.9	53.1	48.3	51.9	56.0	46.5
Macau and other cities	50.5	50.4	47.3	51.5	50.6	47.0

Source: HKTDC, Standard Chartered Research



### Key takeaways from our thematic questions

Our thematic questions for Q2 focused on gauging (1) the speed and impact of global supply chain migration; (2) the shift in drivers behind such supply chain transformations; (3) whether respondents have plans to relocate capacity overseas; and (4) if so, the targeted destinations and scale for relocation. We also asked businesses about their readiness to tap emerging RCEP opportunities.

#### Global supply chain migration is accelerating

#### Reshaped by global supply chain migration

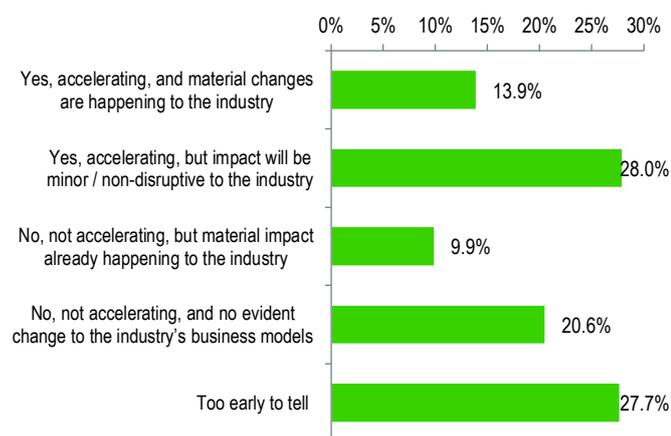
We asked our respondents whether they are seeing an acceleration in global supply chain migration, and whether that will reshape how businesses run in their industry in the GBA. 42% respondents said global supply chain migration is accelerating, but within that only one-third said that would bring material changes to their industry (Figure 8). Another 10% of all our 1,000+ GBA respondents said they do see a material impact already happening in their respective industries despite no acceleration in supply chain migration. Overall, a total of 24% sees a material impact regardless of the pace of transformation, versus over 48% describing any impact as minor or non-disruptive. A remaining 28% chose 'too early to tell'.

#### Shifting priorities for supply-chain management

We then asked respondents how their business priorities have changed in recent years when managing their supply chains. Among the 10 options we provided (as shown in Figure 10), more than half of the respondents remained neutral. Nonetheless, all options saw more respondents voting 'more important' than 'less important', and by a wide net positive margin of 28.5ppt on average. The increased importance being attached to creating supply chain flexibility ('just-in-case'), for example, did not seem to take away from the need to also maximise efficiency (with 'just-in-time'). One could see this as a general rise in awareness for better supply side management, having dealt with an expansive range of business, macro and geopolitical challenges in recent years.

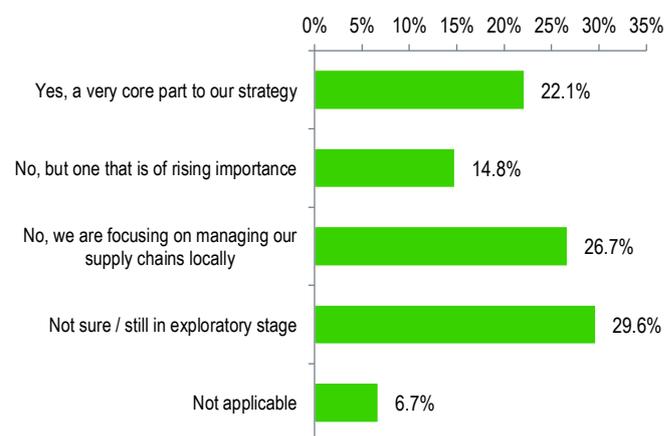
But if one is to really pick the top three fastest growing drivers of supply chain transformation, they are 'improving quality and services' (+36ppt), 'diversifying supplier base (especially for critical components)' (+32ppt), and 'better utilising resources of different production locations (e.g. land and labour)' (+32ppt).

Figure 8: Are you seeing an acceleration in global supply chain migration, and how will that reshape your industry? % of respondents



Source: HKTDC, Standard Chartered Research

Figure 9: Is moving production capacity overseas a core part of your supply chain management strategy? % of respondents



Source: HKTDC, Standard Chartered Research



## On the Ground

### Moving production capacity overseas

When asked whether moving production capabilities overseas is a core part of their supply chain management strategy, over 22% gave a resounding 'yes' response (Figure 9). Another 15% said relocating overseas is not part of their core strategy yet, but is one that is of rising importance. These two options together accounted for 37% votes, besting those saying they are 'focusing on managing supply chains locally' (27%), or those still unsure or 'still in exploratory stage' (30%).

### A growing list of push factors for relocating some capacity overseas

#### Exogenous drivers for factory relocation

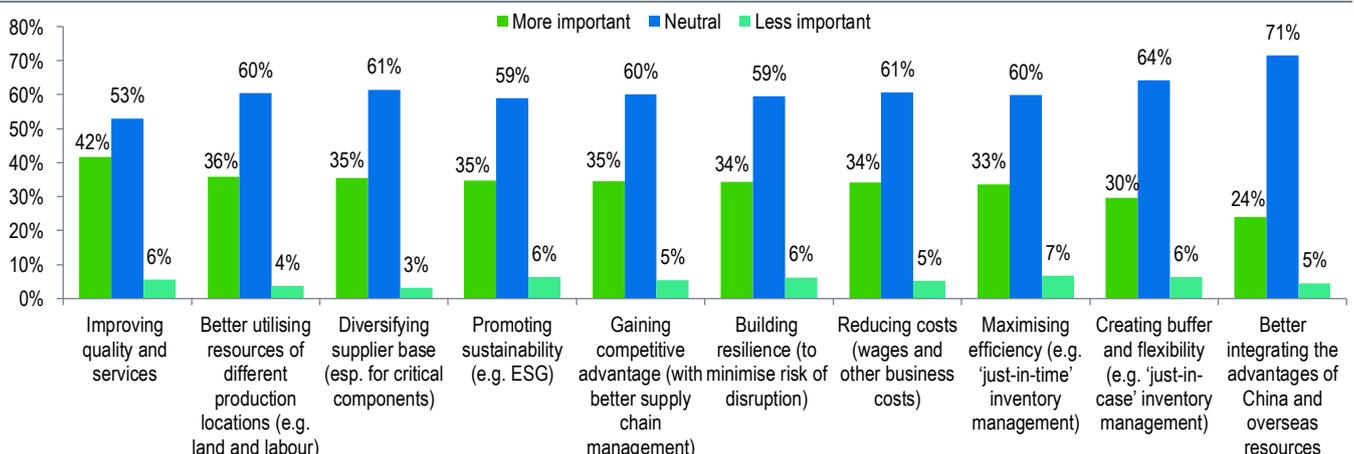
'Technology advancement' garnered the most votes for being a 'strong driver' (29%) outside of the usual business factors when considering relocating production capacity outside of China (Figure 11). 'Tech-related tariffs and sanctions' (26%) and 'expanding to new markets' (24%) rounded out the top three spots. 'Labour shortage / wage pressure in the GBA' (71%) leapfrogged to the top spot if one includes 'potential / growing driver' votes – a reminder that while geopolitical considerations might be more topical of late, labour and wage pressures remain a valid and important traditional push factor for GBA manufacturers to consider moving factories overseas. By this same measure of counting both 'strong driver' and 'potential / growing driver' votes, 'RCEP and other FTA benefits' also managed to climb to fourth place (66%), bumping 'technology advancement' (65%) out of the top spots.

#### Walking the relocation walk

Speaking of RCEP, its members are among the popular destinations for factory relocation (Figure 12). That includes ASEAN (2.3%), Japan / South Korea (1.4%), and Australia / New Zealand (0.9%). These numbers increased to 3.1%, 1.7% and 1.2%, respectively, when we asked whether they have plans to move / expand capacity there. Beyond ASEAN, India / South Asia had 2.4% votes for those who already moved capacity there, and a big jump to 4.2% when asked of their future plans. That said, in the grander scheme of things, 91% respondents said they have not moved any capacity overseas, and 87% reported no plans of doing so for now.

Similarly, when asked how much of their current capacity is now outside of China, 91.2% of respondents said 0%, versus 5.4% choosing 1-30%, and a remaining 3.4% saying more than 30% (Figure 13). These numbers became 84.2%, 8.7% and 7.1%, respectively, when we asked what levels they plan to reach in the next three years

Figure 10: How have the following business priorities changed in recent years for your supply chain management? % of respondents



Source: HKTDC, Standard Chartered Research



## On the Ground

(2024-26). All this suggests that despite the broadening range of drivers pushing companies to think about relocating production overseas, few have so far walked the walk. This also confirms no exodus of GBA companies out of China.

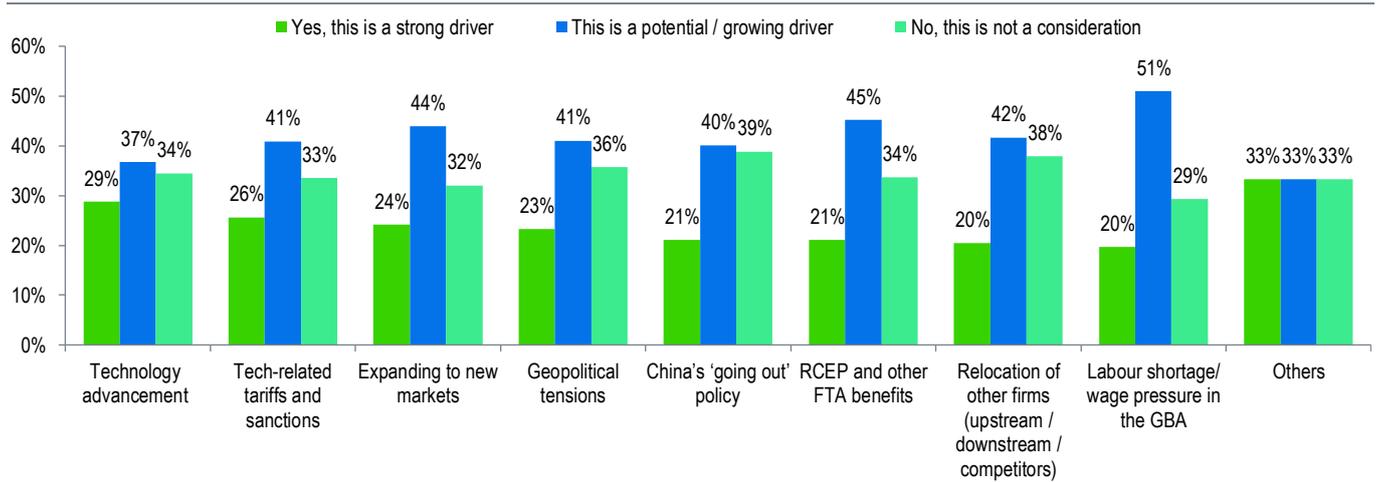
### Gauging hurdles and challenges

We then asked respondents what their biggest hurdles / concerns are for relocating production capacity overseas (Figure 14). 'Cost of production higher than expected' topped the list at 34.6%, followed by 'poor labour quality and productivity' at 29.9%, and 'lack of good suppliers / proximity to suppliers' at 22.8%.

### Tapping RCEP opportunities

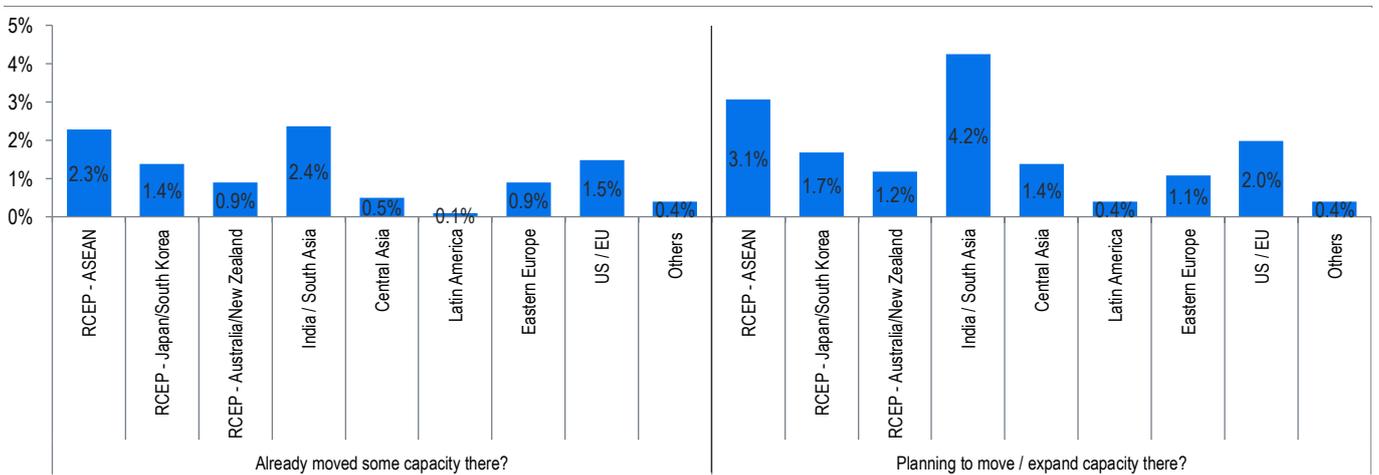
Challenges come with opportunities, and the RCEP has plenty to offer, in our view. Our final thematic question this time tried to understand respondents' readiness to tap these opportunities (Figure 15). 13% of respondents chose a combination of options indicating that they already do sourcing, production or sales with other RCEP members. Another 17% said they are 'still at a planning / strategising stage', versus 35% saying 'no such plans for now' and 25% needing more info.

**Figure 11: Are these factors outside of your business driving the relocation of your production capacity overseas?**  
% of respondents



Source: HKTDC, Standard Chartered Research

**Figure 12: Where has your company moved capacity to? And if you are planning to move (or move more), where to?**  
% of respondents

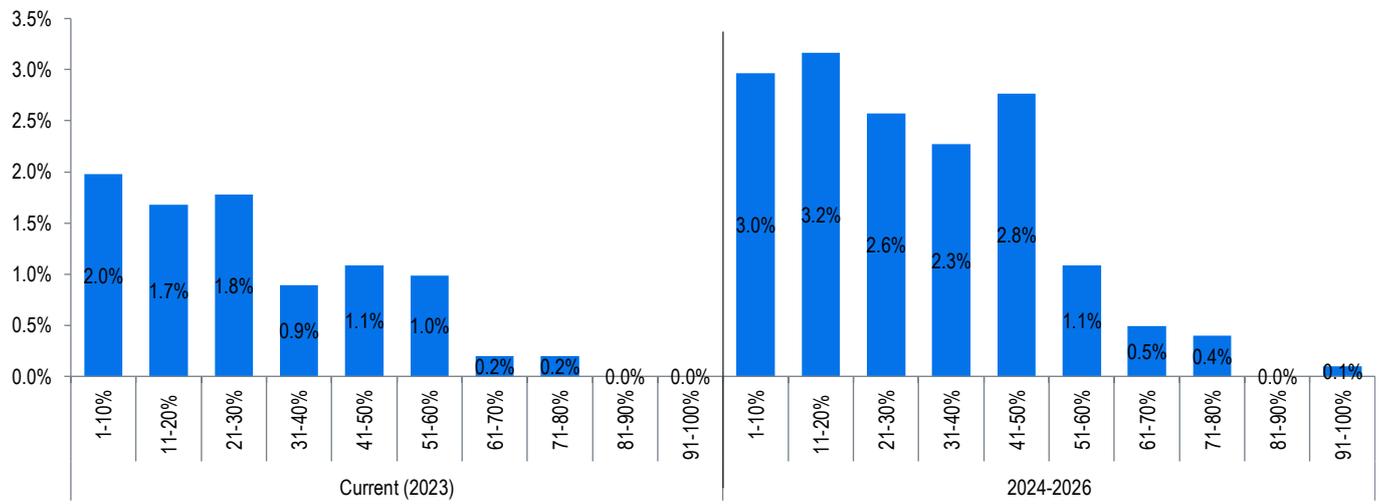


Source: HKTDC, Standard Chartered Research



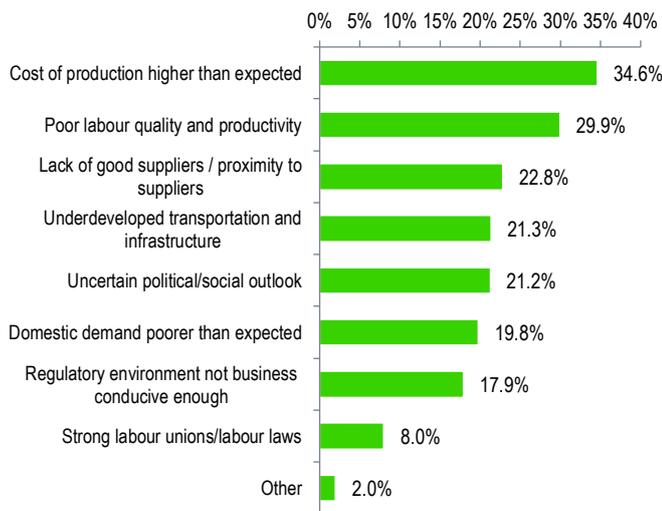
## On the Ground

**Figure 13: What % of your current capacity is now outside of China? What level do you plan to reach in the next three years (2024-26)? (% of respondents)**



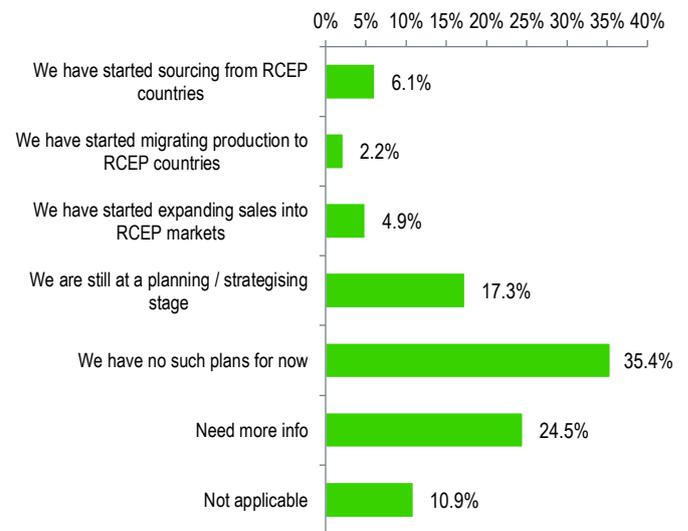
Source: HKTDC, Standard Chartered Research

**Figure 14: What are the main hurdles / concerns for relocation of production capacity outside of China? (% of respondents)**



Source: HKTDC, Standard Chartered Research

**Figure 15: How ready is your company to tap RCEP opportunities? (% of respondents)**



Source: HKTDC, Standard Chartered Research



## On the Ground

**Appendix: How the GBAI works**

*The GBAI is a diffusion index based on responses from no less than 1,000 enterprises across 11 GBA cities and key industry sectors*

The GBAI is compiled based on a quarterly survey conducted by the HKTDC in collaboration with Standard Chartered. Every quarter, no less than 1,000 enterprises in key business sectors across the GBA provide valuable feedback on a range of subjects, including their current business situation and credit conditions, and their outlooks on these subjects for the coming quarter. The GBAI also asks respondents thematic questions that help us understand what drives their business decisions and plans, and how this might shape the GBA's future.

**Index calculation:** The GBAI comprises two main business indices, one gauging 'current performance' (in this case Q2-2023), and the other looking at 'expectations' (Q3-2023). Each index is calculated as an average of eight sub-indices that reflect different aspects of business activity, as outlined in Figure 1. Respondents indicate the corresponding changes, actual or expected, in three ways: up, same or down; a diffusion index is then calculated using the following formula:

$$\text{Up\%} \times 100 + \text{Same\%} \times 50 + \text{Down\%} \times 0$$

An index reading above 50.0 means that respondents are generally optimistic about the business environment in the coming quarter, while a reading below 50.0 indicates predominantly pessimistic sentiment. A reading of 50 is neutral.

The two credit indices are calculated in the same way, but with five of their own sub-components that focus on measuring the costs and ease of obtaining credit, and respondents' willingness and/or eagerness to do so (Figure 4).

**Figure 16: GBAI**

*Number of respondents*

By city		By industry	
	Targeted respondents		Targeted respondents
Hong Kong	200	Manufacturing and trading	500
Guangzhou	200	Retail and wholesale	200
Shenzhen	200	Financial services	125
Foshan	100	Professional services	125
Dongguan	100	Innovation and technology	50
Huizhou		<b>Total</b>	<b>1,000</b>
Zhongshan			
Jiangmen	200		
Zhuhai			
Zhaoqing			
Macau			
<b>Total</b>	<b>1,000</b>		

Source: HKTDC, Standard Chartered Research



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Document approved by  
**Shuang Ding**  
Chief Economist, Greater China and North Asia

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