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UPDATE

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## China Financials | Asia Pacific

# Tracking industrial risks: Demand growth continued to notably outpace supply in June - good for risk reduction


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### Key Takeaways

- Nominal Industrial production increased 7.2% yoy (a proxy of industrial demand) while manufacturing FAI (a proxy of growth in supply) fell 1.2% yoy in June.
- June marked the 9th month of overcapacity reduction in China, which partly supported the strong manufacturing profits growth of 20.1% yoy and improved margin.
- Policy makers pushed more anti-involution initiatives amid strong export growth, a great opportunity to further de-risk the financial system.
- PPI declined 0.3% MoM, yet YoY growth expanded to 4.1% from a low base.
- Industrial mid-to-long term loan growth remained rational at 5.9% yoy in 2Q26, moderated from 6.8% yoy in 1Q26, which should help industrial credit de-risking.

**Overall manufacturing profit growth remained strong with divergence across sectors.** 37% of sectors (by liabilities) saw profitability improvement, around 40% sectors showed relatively stable profit trends and a bit more than 20% of sectors showed deterioration, which is a healthy and normal distribution, in our view. Electronic devices, chemicals, and chemical fibers posted strong profit growth on consecutive price rebounds. Conversely, alcohol, apparel, and wood manufacturing saw further profit deterioration. We believe this could help steady industrial risk digestion as well as a more balanced development when industries move through different cycles.

**Steady overcapacity control progress with a declining FAI-IP gap.** 85% of sectors (by liabilities) saw capex slowdown in June. Based on YTD average PPI growth, overall manufacturing FAI-IP gap fell to -8.4% in June, vs. -6.9% in May, with continued tightening in FAI growth. This is the 9th consecutive month of over capacity reduction, which we think should help further reduction in excess capacity. We continue to believe the rationalization pace of manufacturing growth is more sustainable for the China financial system than boosting demand.



**CHINA FINANCIALS**

Asia Pacific
Industry View **Attractive**

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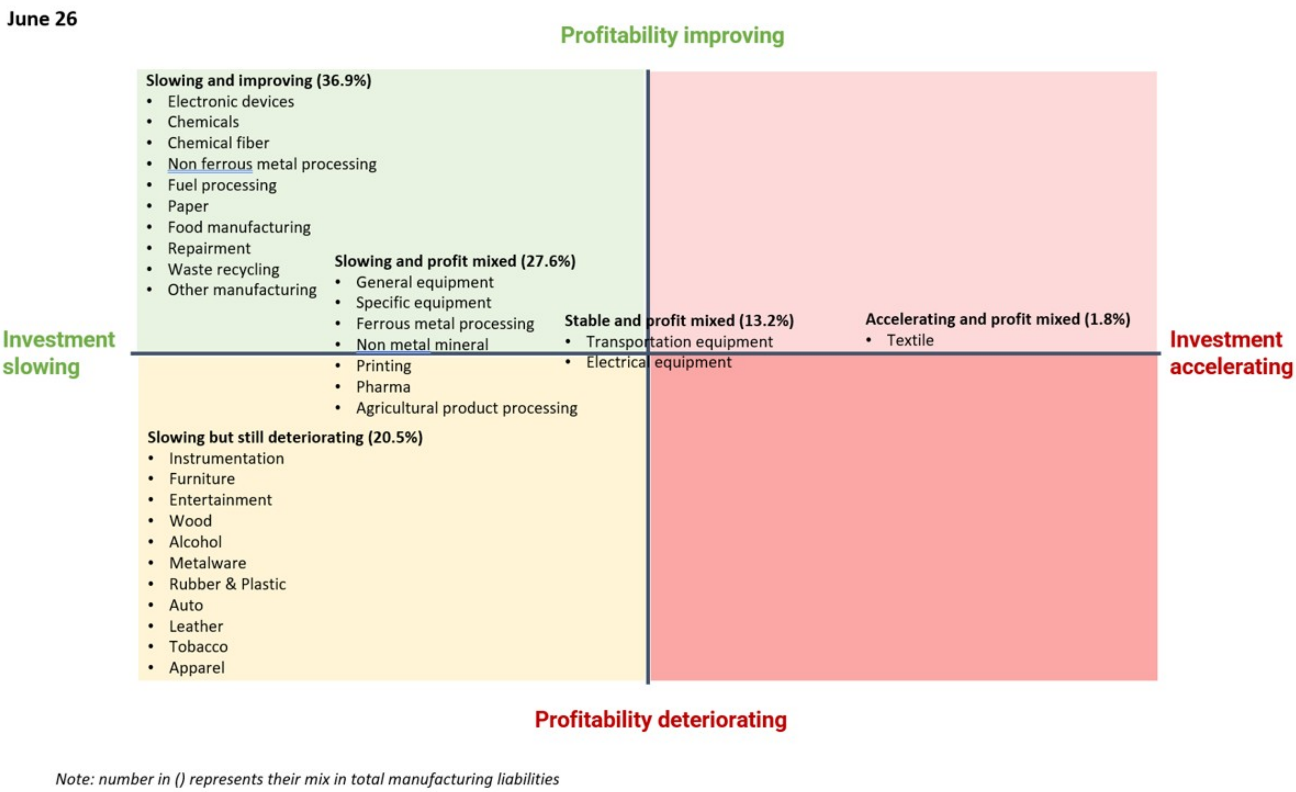
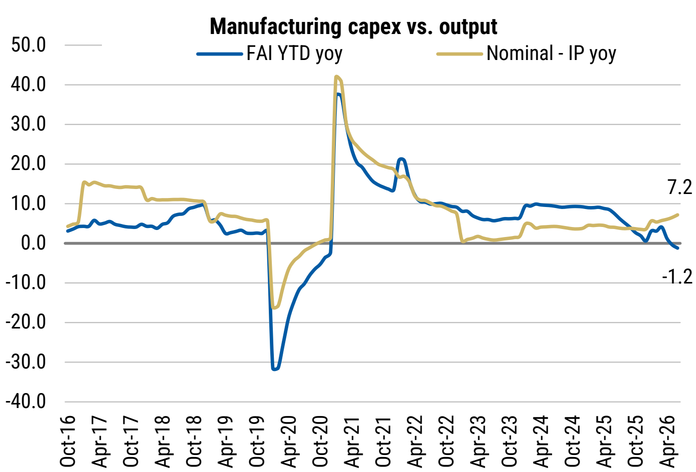
# Charts

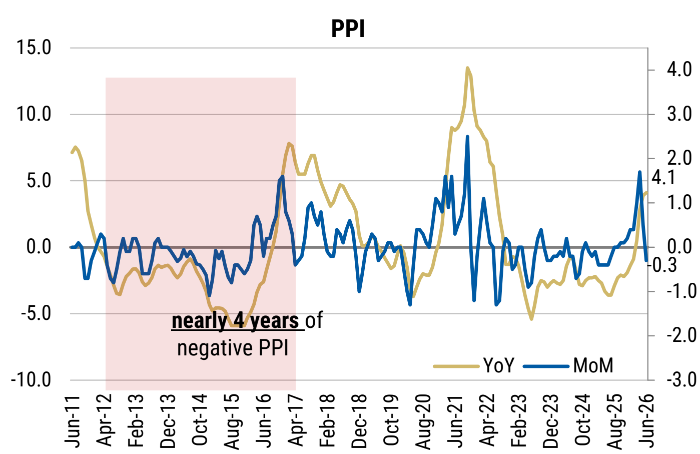
**Exhibit 1:** 85% (in terms of liabilities) of sectors slowed capex in June 2026; 37% of sectors showed better profit trends in June




Source: NBS, CEIC, Morgan Stanley Research. Note: number in () represents their mix in total manufacturing liabilities.

**Exhibit 2:** Manufacturing FAI and IP gap declined to -8.4%, from -6.9% last month, on further tightening FAI growth; PPI declined 0.3% MoM but up 4.1% YoY.




Source: NBS, CEIC, Morgan Stanley Research

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|---|---|---|---|---|---|---|---|
| Stock Rating Category | Count | % of Total | Count | % of Total IBC | % of Rating Category | Count | % of Total Other MISC |
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| Equal-weight/Hold | 1577 | 43% | 390 | 42% | 25% | 769 | 44% |
| Not-Rated/Hold | 3 | 0% | 1 | 0% | 33% | 1 | 0% |
| Underweight/Sell | 544 | 15% | 89 | 10% | 16% | 204 | 12% |
| Total | 3,668 | | 933 | | | 1731 | |

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|---|---|---|
| **Chiyao Huang** | | |
| China International Capital Corp. Ltd. (3908.HK) | O (02/28/2025) | HK$21.48 |
| China Merchants Securities Co Ltd (600999.SS) | U (09/29/2022) | Rmb17.56 |
| China Merchants Securities Co Ltd (6099.HK) | U (10/29/2024) | HK$14.45 |
| CITIC Securities Co. (6030.HK) | O (07/10/2026) | HK$27.32 |
| CITIC Securities Co. (600030.SS) | O (08/07/2025) | |
| East Money Information Co Ltd (300059.SZ) | E (09/19/2025) | |
| Futu Holdings Ltd (FUTU.O) | O (11/18/2024) | |
| Galaxy Securities (6881.HK) | E (02/27/2020) | |
| Galaxy Securities (601881.SS) | U (09/29/2022) | |
| GF Securities (000776.SZ) | E (08/07/2025) | |
| GF Securities (1776.HK) | E (01/06/2023) | |
| HTSC (601688.SS) | E (09/23/2024) | |

| | | |
|---|---|---|
| HTSC (6886.HK) | E (09/23/2024) | HK$16.85 |
| **Richard Xu, CFA** | | |
| Agricultural Bank of China Limited (601288.SS) | E (05/07/2019) | Rmb7.11 |
| Agricultural Bank of China Limited (1288.HK) | O (10/19/2020) | HK$6.51 |
| Bairong Inc. (6608.HK) | E (09/09/2025) | HK$5.22 |
| Bank of Beijing Co Ltd (601169.SS) | E (08/17/2022) | Rmb5.21 |
| Bank of Chengdu Co Ltd (601838.SS) | O (08/17/2022) | Rmb18.71 |
| Bank of China Limited (601988.SS) | E (05/07/2019) | Rmb6.14 |
| Bank of China Limited (3988.HK) | O (01/10/2020) | HK$5.54 |
| Bank of Communications (3328.HK) | U (05/20/2022) | HK$7.67 |
| Bank of Communications (601328.SS) | U (09/05/2014) | Rmb7.32 |
| Bank of Hangzhou Co Ltd (600926.SS) | E (08/17/2022) | Rmb16.50 |
| Bank of Ningbo Co. Ltd (002142.SZ) | O (08/17/2022) | Rmb32.90 |
| China CITIC Bank Corporation Limited (601998.SS) | E (04/16/2025) | Rmb7.93 |
| China CITIC Bank Corporation Limited (0998.HK) | O (04/16/2025) | HK$7.85 |
| China Construction Bank Corp. (0939.HK) | O (10/11/2012) | HK$9.36 |
| China Construction Bank Corp. (601939.SS) | E (05/07/2019) | Rmb10.97 |
| China Everbright Bank Co Ltd (6818.HK) | U (05/12/2023) | HK$3.27 |
| China Everbright Bank Co Ltd (601818.SS) | U (05/20/2022) | Rmb3.19 |
| China Merchants Bank (600036.SS) | O (01/07/2019) | Rmb40.55 |
| China Merchants Bank (3968.HK) | O (09/20/2018) | HK$51.20 |
| China Minsheng Banking Corp. (600016.SS) | O (08/28/2025) | Rmb3.63 |
| China Minsheng Banking Corp. (1988.HK) | O (05/12/2023) | HK$3.67 |
| Chongqing Rural Commercial Bank (3618.HK) | U (05/12/2023) | HK$6.68 |
| Hua Xia Bank (600015.SS) | U (06/30/2015) | Rmb7.03 |
| Industrial and Commercial Bank of China (1398.HK) | O (08/09/2013) | HK$7.64 |
| Industrial and Commercial Bank of China (601398.SS) | E (09/19/2022) | Rmb8.15 |
| Industrial Bank Co. Ltd. (601166.SS) | O (02/25/2019) | Rmb19.10 |
| Lufax (LU.N) | | US$1.53 |
| Ping An Bank (000001.SZ) | O (05/07/2019) | Rmb11.61 |
| Postal Savings Bank of China Co Ltd (1658.HK) | O (11/01/2016) | HK$5.11 |
| Qifu Technology Inc (QFIN.O) | O (08/25/2020) | US$13.76 |
| Shanghai Pudong Development Bank (600000.SS) | E (08/05/2025) | Rmb9.71 |

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