China’s manufacturing strengthened more than anticipated this month, a sign the recovery is gaining momentum as leaders struggle with surging home prices and local-government debt.

The preliminary 50.9 reading for a Purchasing Managers’ Index (EC11FLAS) released today by HSBC Holdings Plc and Markit Economics compared with a 50.4 median estimate from analysts surveyed by Bloomberg News. Readings above 50 indicate expansion.

Stocks fell as the manufacturing report was overshadowed by concern that the government could tighten credit and clamp down further on the property market. Money-market rates jumped the most in more than two months today, while a report earlier this week showed home prices in four major cities rose the most since January 2011 in September.

“The pickup in the flash PMI suggests that economic momentum may hold up in October, but we maintain our view that growth will slow” in the fourth quarter and 2014 “as monetary policy tightens to contain inflation and financial risks,” Zhang Zhiwei, chief China economist at Nomura Holdings Inc. in Hong Kong, said in a note today.

Last month’s final level of 50.2 differed from an initial 51.2, the biggest gap since HSBC began giving advance figures in 2011.

The benchmark Shanghai Composite Index (SHCOMP) of stocks fell 0.2 percent at the 11:30 a.m. local-time break, while the yuan touched a 20-year high of 6.0815 per dollar and the Australian dollar gained.

**Control Risks**

Officials are wrestling with controlling risks from shadow banking and local-government debt while keeping growth above a “bottom line” of 7 percent. The government has rolled out fiscal stimulus, including spending on railways and replacing shantytowns, to support expansion without cutting interest rates or banks’ reserve requirements.

China yesterday allowed more local governments to issue short-term debt to help pay off maturing bonds and loans, a move that may help to contain risks from a surge in borrowing, the Wall Street Journal reported today, citing a person with direct knowledge of the matter that it didn’t identify.

China’s one-year interest-rate swap rose today by the most in two months after the People’s Bank of
China refrained from injecting funds via reverse-repurchase agreements for a third straight auction.

Premier Li Keqiang said this week that the nation is on track to achieve its economic goals in 2013 after expansion accelerated to 7.8 percent last quarter from a year earlier.

**Speeding Reforms**

“This momentum is likely to continue in the coming months, creating favorable conditions for speeding up structural reforms,” Qu Hongbin, HSBC chief China economist in Hong Kong, said in a statement.

Elsewhere today in the Asia-Pacific region, New Zealand’s trade deficit narrowed in September from the previous month, while Vietnam’s inflation slowed in October. In Europe, Markit will also report PMI gauges for France, Germany and the euro area, and the U.S. provides the August trade balance.

The final reading of the HSBC-Markit China manufacturing PMI will be released on Nov. 1. The National Bureau of Statistics publishes the government’s manufacturing PMI, with a bigger sample size, on the same day.

The Flash PMI from HSBC and Markit is based on 85 percent to 90 percent of responses to surveys sent to more than 420 manufacturers. The survey showed output, new orders and export orders rising at a faster pace while employment declined at a slower rate, HSBC said.

**Holding Up**

“What this number shows is that China’s economy is still on course for decent growth -- not the kind of spectacular growth that we were used to in the past, but enough growth to keep it above the government’s bottom line,” Louis Kuijs, chief China economist at Royal Bank of Scotland Group Plc in Hong Kong, said in a Bloomberg Television interview.

“China is holding up pretty well” compared to other countries amid talk that the U.S. Federal Reserve will slow its monetary stimulus, Kuijs said. “When financial conditions are loose, everybody is doing fine and everybody is growing; but then, when the Fed starts to talk about tapering, you see who is vulnerable to these things -- China is not.”

Analysts see growth slipping to 7.6 percent this quarter and 7.4 percent in 2014, based on median estimates in a Bloomberg survey this month, compared with the government’s 7.5 percent goal for 2013.

Data earlier this month showed exports fell 0.3 percent in September from a year earlier, a decline that reflected limits on global demand as well as distortions caused by past fake invoicing. Industrial production rose 10.2 percent, down from August’s 10.4 percent pace, the first slowdown in three months.

ZTE Corp. (000063), the third-largest smartphone vendor in China, said this week that it will probably turn a full-year profit in 2013, after a loss last year, following a 241.6 million yuan ($40
million) profit in the third quarter.

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