

China Economy

In mild reflation

China's deflationary pressure continued to ease in end-2025. CPI edged up driven by food and gold jewellery prices. Consumer goods rebounded as holiday approaches while service price remained flat. Contraction of PPI notably narrowed driven by non-ferrous-related price, while downstream sectors remained subdued. We expect mild price reflation in the short term, driven by anti-involution campaign and global commodities rally, which should improve corporate profitability and support capital market performance. However, the sustainability of price reflation over the medium and long term remains uncertain. Price gains have been concentrated in the upstream sectors, while end-demand remains weak. Chinese policymakers may require more time to reach consensus on prioritising economic rebalancing and to steer policy support away from local governments and enterprises towards households and consumers. We expect the CPI and PPI to reflate from 0.1% and -2.6% in 2025 to 0.7% and -0.5% in 2026.

■ **Food price drove the rebound of CPI.** China's CPI edged up to 0.8% YoY in Dec from 0.7% in Nov, in line with market expectation. In sequential terms, CPI recovered to 0.2% in Dec from -0.1% in Nov. Food price remained the major driver as its YoY growth rose to 1.1% in Dec, boosting headline CPI by 0.2pp. Vegetable price YoY growth climbed to 18.2%, while its MoM pace slowed from 0.5% in Nov to 0.3% in Dec. Pork price saw another drop at -1.7% MoM in Dec, as live hog inventory remained abundant. Vehicle fuel price dropped 1.1% MoM in Dec as global crude oil price remained subdued. We expect the CPI to drop to 0.1% YoY in Dec due to higher base last year, while high frequency data showed vegetable and vehicle fuel prices continued to drop.

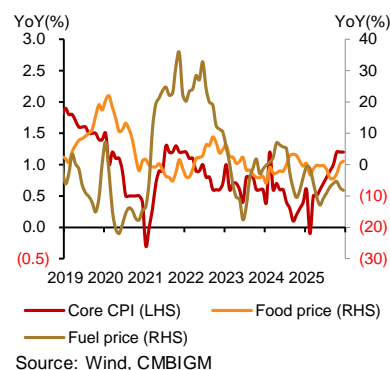
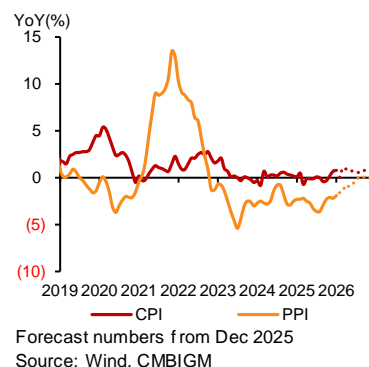
■ **Core CPI remained elevated.** Core inflation stayed flat at 1.2% YoY in Dec, while its MoM rose 0.2%. Durable goods saw notable price reflation as Chinese New Year is approaching. Home equipment, telecom equipment and vehicles rose 1.4%, 3% and 0.1% MoM respectively in Dec. According to NBS, gold jewellery further rose to 68.5% YoY in Dec from 58.4%, contributing at least 0.5pp to core inflation. Service price remained flat at 0% MoM in Dec, with its YoY growth moderated to 0.6% in Dec from 0.7%. Education, telecom and express services stayed unchanged while home and tourism service expanded by 0.1% MoM. Medical service has been reflatting since Apr, expanding 0.2% MoM in Dec reflecting the impact of medical service price reforms.

■ **PPI sustained its recovery momentum.** The YoY contraction of PPI edged up to -1.9% in Dec from -2.2% in Nov, beating market expectations at -2%. The MoM growth increased for the third month at 0.3% driven by upper stream sectors including mining and raw materials, rising 0.8% and 0.6% respectively. Extraction of coal and non-ferrous metals rose 1.3% and 3.7% in Dec, while the mining of crude oil and gas declined 1.3%. NBS officials pointed out that deflation in major anti-involution sectors continued to improve, including lithium batteries, cement and NEVs. Downstream sectors remained subdued, as PPI of consumer goods stayed flat at 0% MoM in Dec. Household necessities and clothing rose by 0.5% and 0.2%, while durable goods dropped 0.2% and 0.1% MoM.

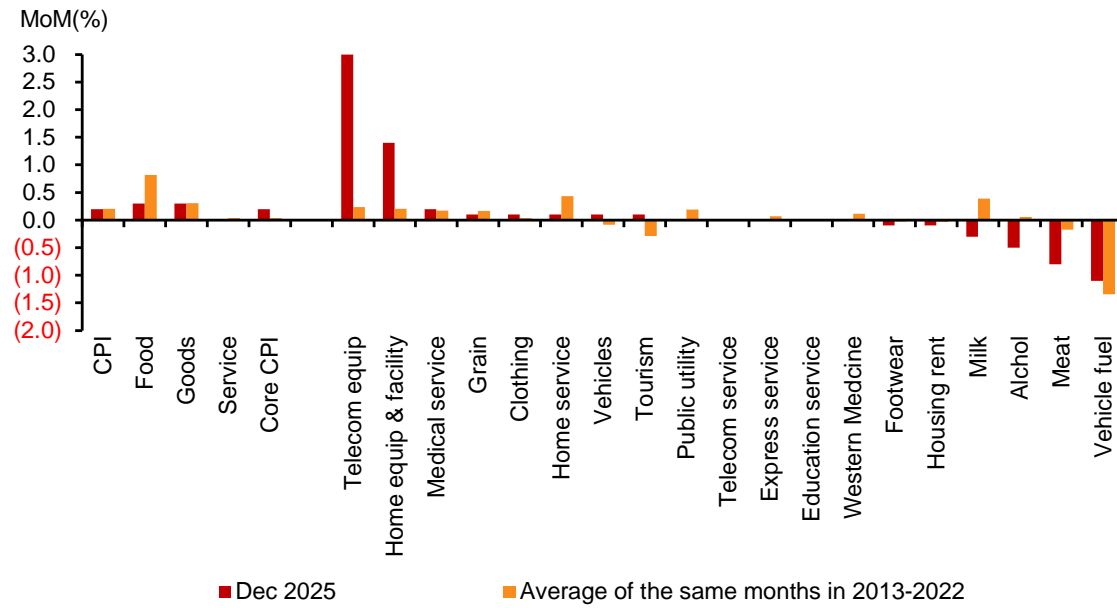
■ **We expect mild price reflation driven by anti-involution campaign and global commodities rally.** Despite recent recovery, CPI and PPI both softened in 2025 to 0.1% and -2.6% from 0.2% and -2.2% in 2024. We expect the CPI and PPI to reflate to 0.7% and -0.5% in 2026 thanks to the anti-involution campaign and global commodities rally. In the near term, a rebound in price level should improve corporate profitability and support the

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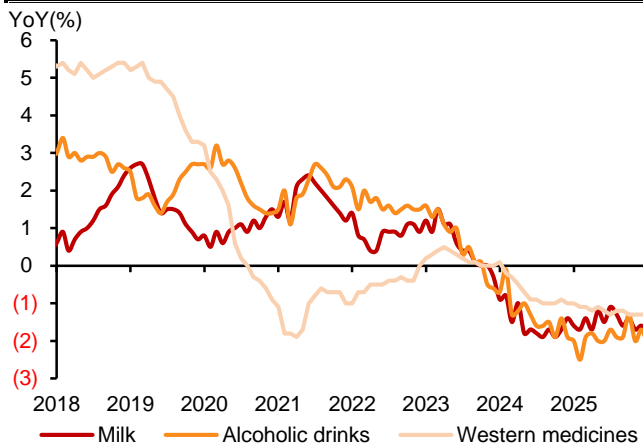
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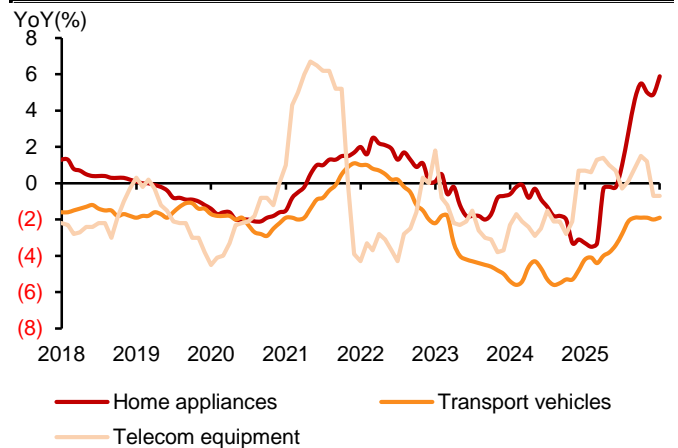
performance in the capital market. However, the sustainability of price reflation over the medium and long term remains uncertain. At present, price gains have been concentrated in the upstream sectors, while end-demand remains weak. Chinese policymakers may require more time to reach consensus on prioritizing economic rebalancing, and to steer policy support away from local governments and enterprises towards households and consumers. Without strong fiscal support to consumers and aggressive overcapacity reduction, the deflationary pressure may last longer than expected.

Figure 1: MoM Changes of China CPI in Dec

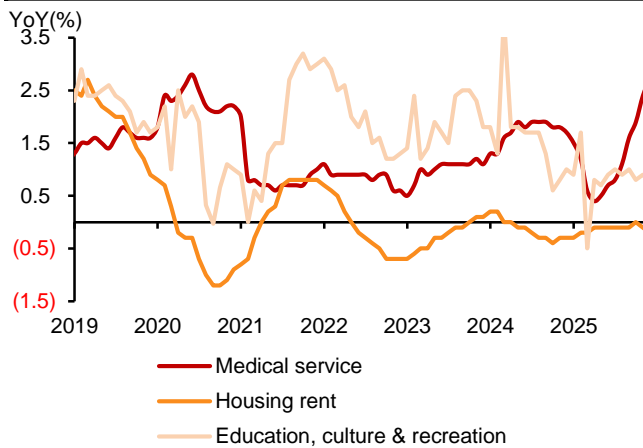
Source: Wind, CMBIGM

Figure 2: China CPI growth in staples

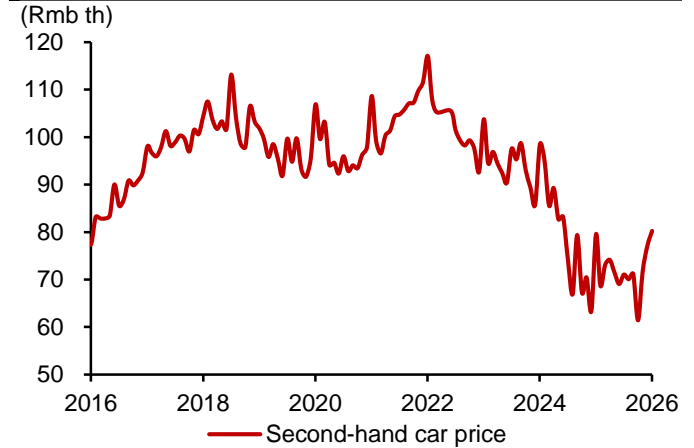
Source: Wind, CMBIGM

Figure 3: China CPI growth in durables

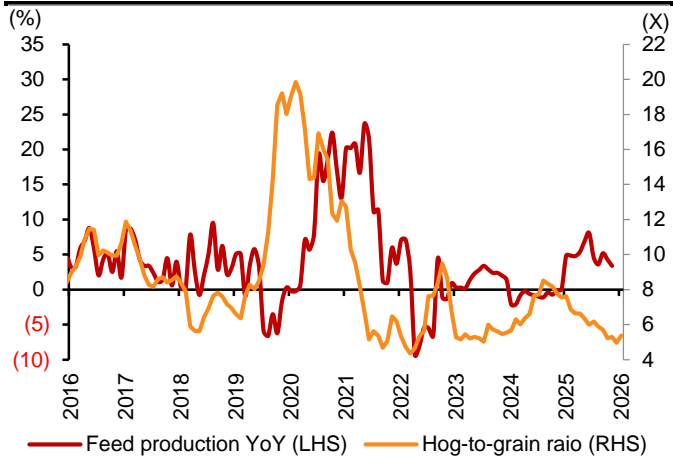
Source: Wind, CMBIGM

Figure 4: China CPI growth in services

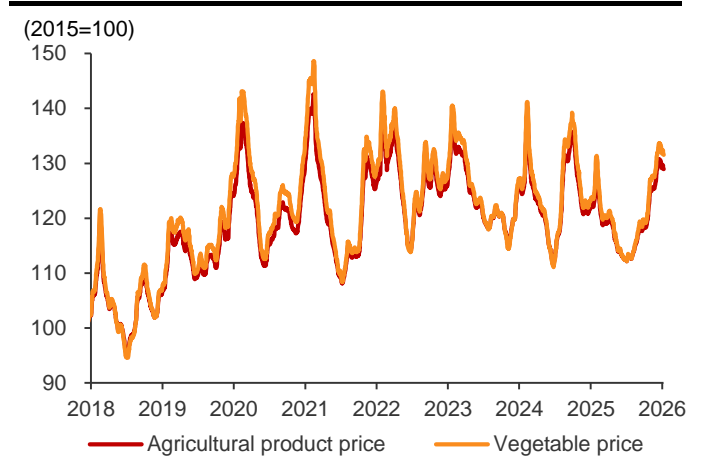
Source: Wind, CMBIGM

Figure 5: Second-hand car price in Shanghai

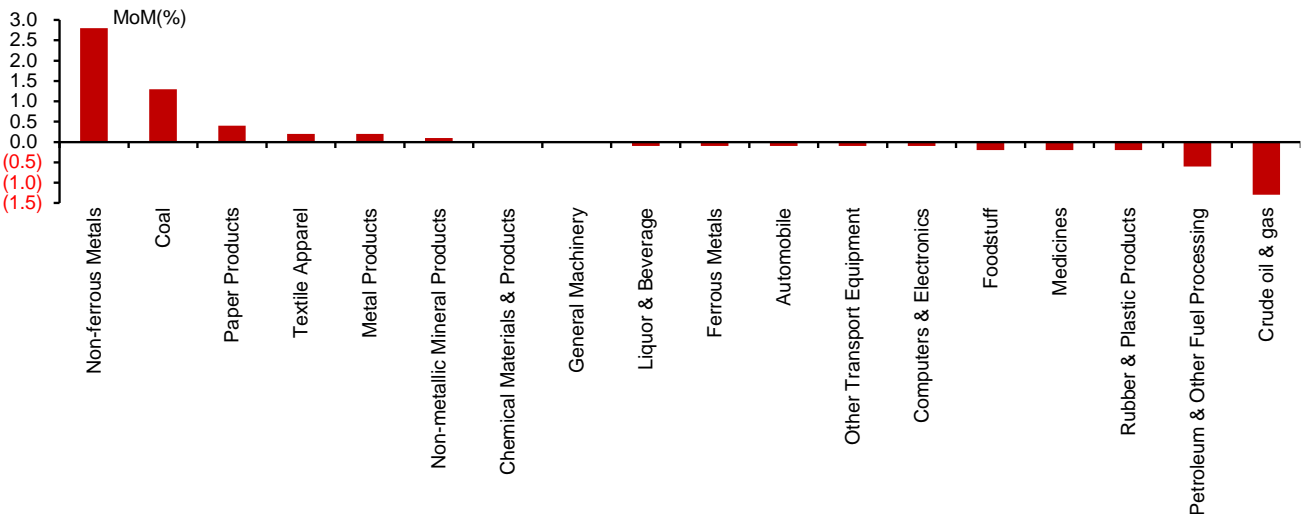
Source: Wind, CMBIGM

Figure 6: Feed production & hog-to-grain ratio

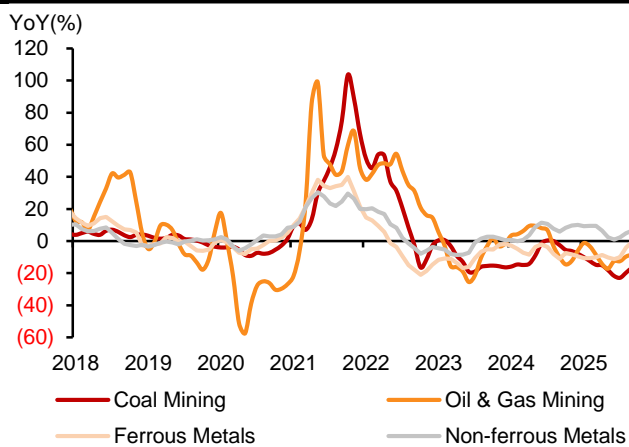
Source: Wind, CMBIGM

Figure 7: Agricultural and vegetable price

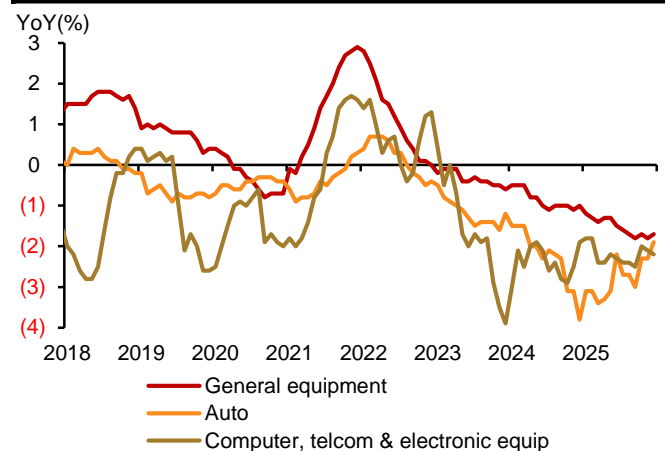
Source: Wind, CMBIGM

Figure 8: MoM changes of China PPI in Dec

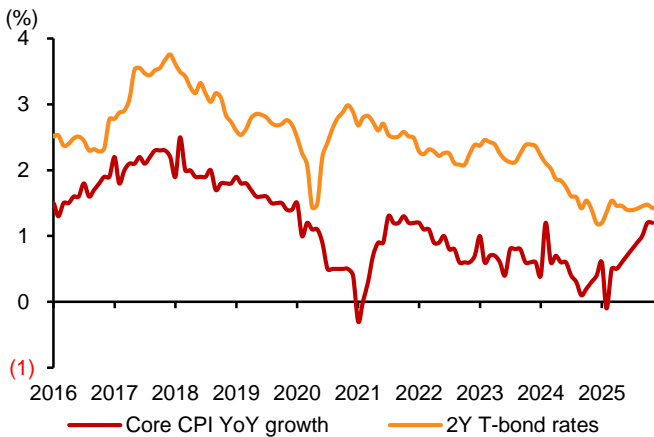
Source: Wind, CMBIGM

Figure 9: China PPI in energy & metals

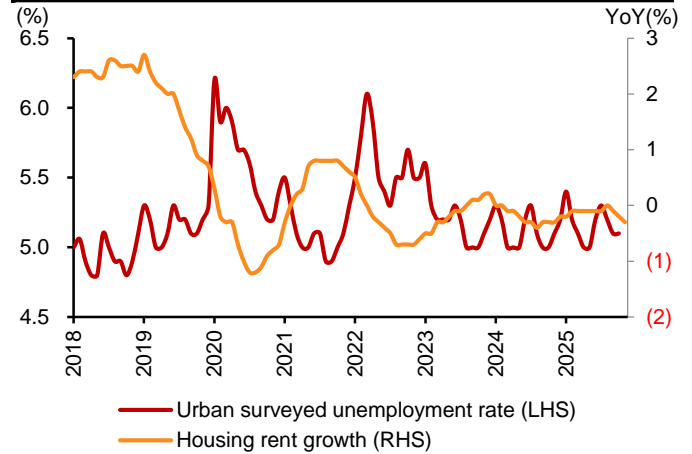
Source: Wind, CMBIGM

Figure 10: China PPI in equipment

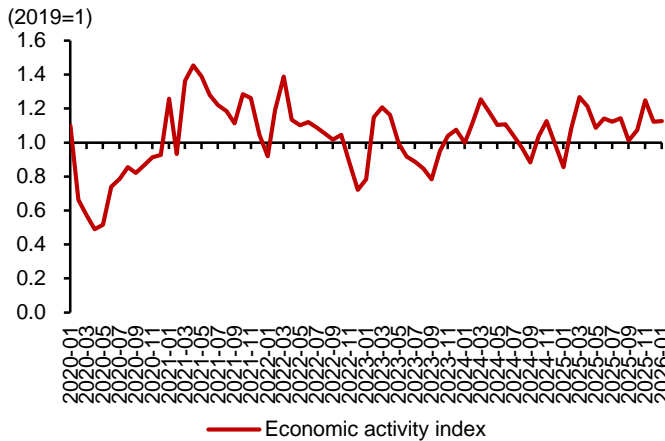
Source: Wind, CMBIGM

Figure 11: China core CPI growth & 2Y T-bond rates

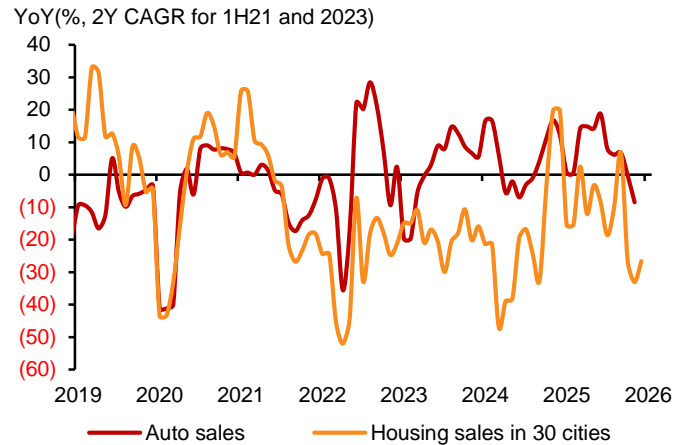
Source: Wind, CMBIGM

Figure 12: Unemployment rate and rent growth

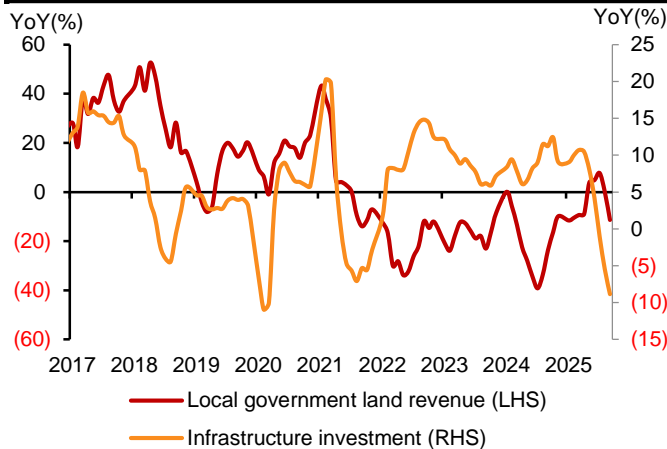
Source: Wind, CMBIGM estimates

Figure 13: China Economic Activity Index

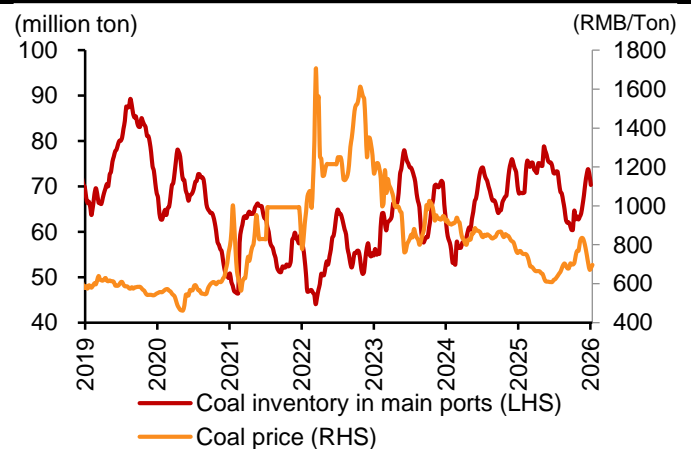
Source: Wind, CMBIGM

Figure 14: China auto & housing sales

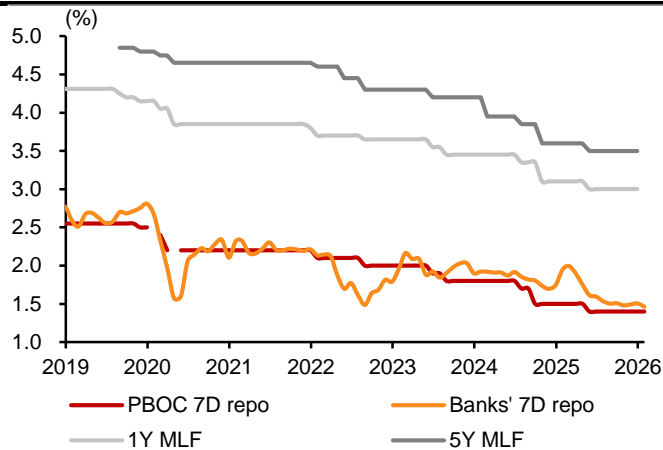
Source: Bloomberg, CMBIGM

Figure 15: Infrastructure investment in China

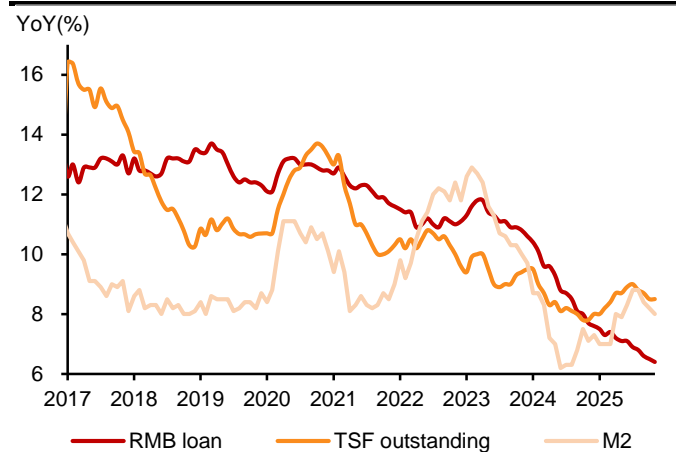
Source: Bloomberg, CMBIGM

Figure 16: China coal inventory & price

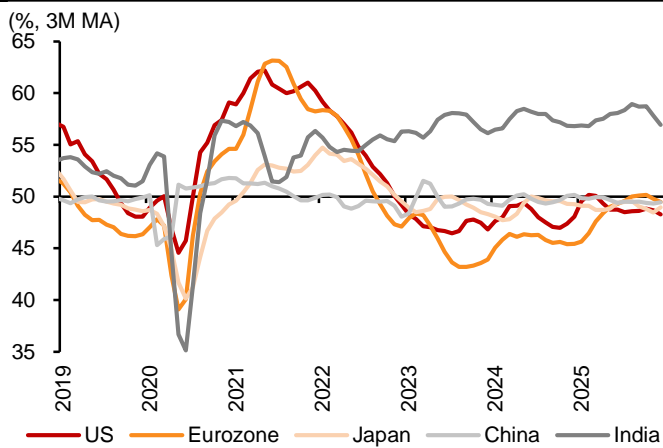
Source: Wind, CMBIGM

Figure 17: PBOC policy rates & liquidity condition

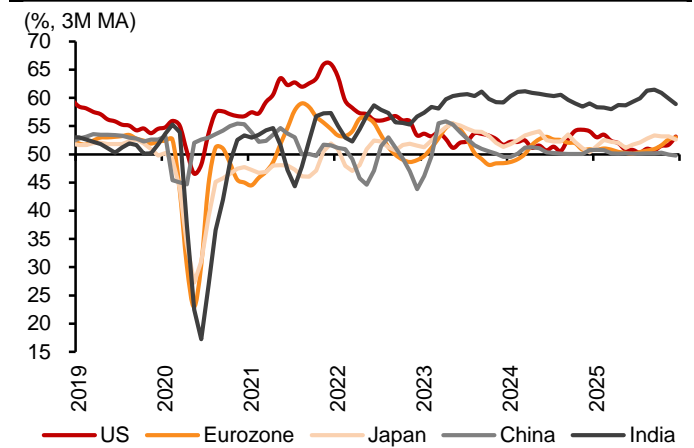
Source: Bloomberg, CMBIGM

Figure 18: China credit growth

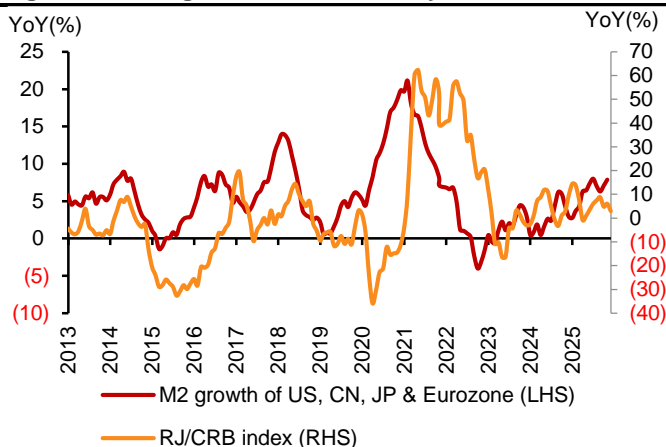
Source: Wind, CMBIGM

Figure 19: Manufacturing PMI of major economies

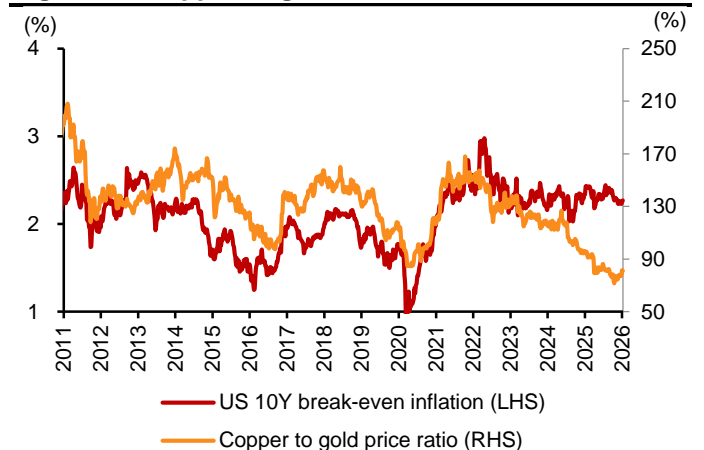
Source: Bloomberg, CMBIGM

Figure 20: Service PMI of major economies

Source: Wind, CMBIGM

Figure 21: M2 growth & commodity inflation

Source: Bloomberg, CMBIGM

Figure 22: Copper-to-gold ratio

Source: Wind, CMBIGM

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