

China Economy

Weaker CPI supports policy easing

Feb CPI slipped into negative territory due to the CNY mismatch and still-weak domestic demand. The Jan-Feb MoM CAGR of CPI and core CPI lagged historical seasonality, as food, service, and goods prices remained subdued. PPI continued to dip MoM, weighed down by declining energy and ferrous metal prices while final consumption goods remained muted. The reflation in 2025 might be milder than expected due to weak employment and household income, as well as the downside pressure from the Trump tariff hikes. We expect China's CPI and PPI to recover from 0.2% and -2.2% in 2024 to 0.6% and -0.3% in 2025. Looking forward, the PBOC may cut RRR in 2Q25 and LPRs in 2H25 as the negative impact of Trump's tariffs might release and the stimulus effects of domestic policies could diminish. We expect additional RRR cuts by 50bps and LPR cuts by 20bps this year.

■ **CPI turned negative due to CNY mismatch but still reflected weaker seasonal patterns.** China's CPI YoY growth dropped to -0.7% in Feb from 0.5% in Jan, weaker than the -0.4% market expectation. CPI inflation was 0.1% YoY in Feb adjusted for CNY distortions according to the NBS. In sequential terms, CPI dipped to -0.2% in Feb from 0.7% in Jan, while Jan-Feb MoM CAGR of CPI grew by 0.25%, weaker than previous Jan-Feb seasonality at 0.8%. Food price saw a 0.4% CAGR in Jan-Feb compared to the 2.6% CAGR in historical seasonality, dragged by weak pork, vegetable and grain prices. Pork prices may remain muted as inventories of breeding sows and live hogs stay elevated. Vehicle fuel price, on the other hand, showed a stronger CAGR in Jan-Feb at 1.9%, but we expect the growth to moderate amid the dipping crude oil price. CPI in Mar might remain subdued as high-frequency data show prices of agricultural products and vegetables as well as the wholesale prices of pork and gasoline continue to drop.

■ **Core CPI dipped to negative territory for the first time since Covid.** Core inflation dropped to -0.1% YoY in Feb from 0.6% in Jan, the first time since Jan 2021. Its MoM growth dipped to -0.2% in Feb from 0.5% in Jan. The Jan-Feb MoM CAGR was also weaker at 0.15% compared to 0.24% by historical trends. Service price dropped 0.5% MoM as prices of travel, entertainment and recreational activities retreated. Overall, service price was still weak as its CAGR saw 0.2% growth in Jan-Feb compared to 0.46% in history. Telecom equipment and vehicles underperformed at -0.4% and -0.1% CAGRs compared to historical seasonality while home equipment, footwear and clothing outperformed at 0.3%, -0.1% and -0.25%. Overall, the 0.3% CAGR of goods price is weaker than its historical trend at 1%, indicating that domestic demand would still be subdued if not for the trade-in scheme.

■ **PPI continued to decline, weighed down by falling energy prices.** YoY contraction of PPI narrowed from -2.3% in Jan to -2.2% in Feb, weaker than market expectations at -2.06%. The MoM growth dipped -0.1% in Feb compared to -0.2% in Jan. For mining industries, PPI of energy including coal and oil & gas mining further dropped to -12.5% and -3.3% YoY in Feb from -10.1% and -1.3% in Jan. Ferrous metals remained suppressed at -10.6% as work resumption rate at construction sites was weaker compared to last year, while price of non-ferrous metals remained robust at 9.5% thanks to their application in high-tech manufacturing. Final consumer goods remained lethargic as apparel and durable goods saw -0.2% and 0% MoM growth while general daily necessities rose by 0.1%. We expect the decline of PPI to moderately narrow thanks to the base effect in last year and pickup in global commodity prices. Yet, the drag from weakening external demand and global trade could persist.

Frank Liu

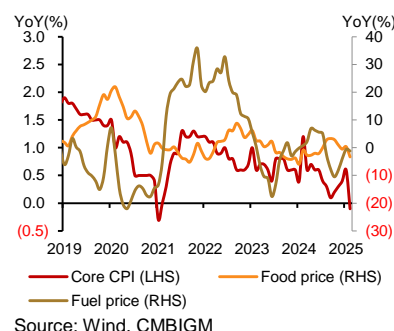
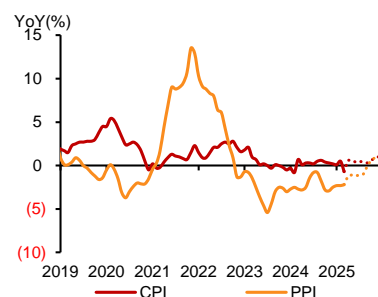
(852) 3761 8957

frankliu@cmbi.com.hk

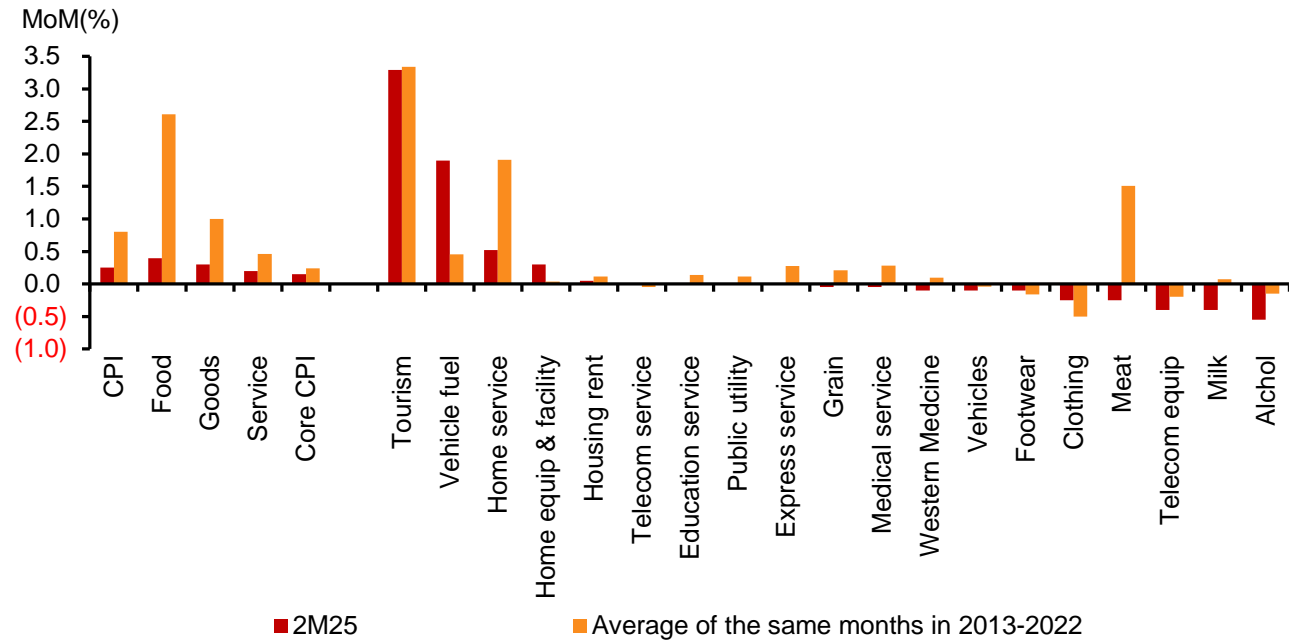
Bingnan YE, Ph.D

(852) 3761 8967

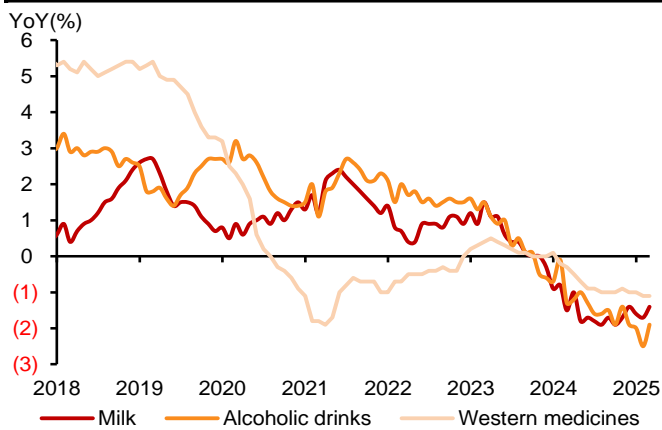
yebingnan@cmbi.com.hk



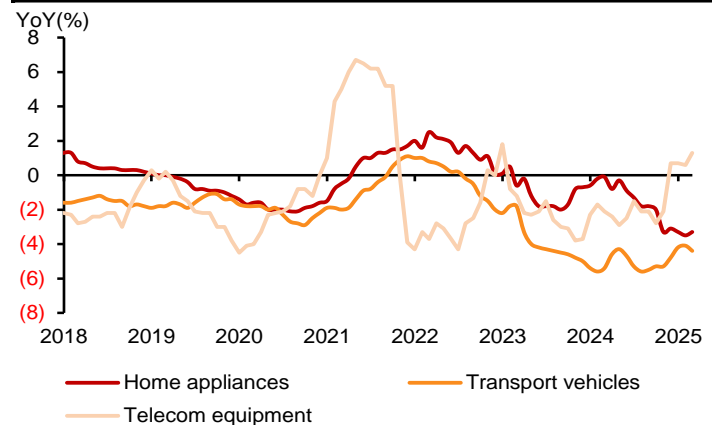
- **The reflation in 2025 might be milder than expected.** Housing and durables sales have continued to improve since 2H24, probably followed by a recovery in consumer demand in the next several months as success of DeepSeek and the revitalized equity market may strengthen consumer confidence. However, the reflation might be milder than expected as domestic demand remained subdued due to weak employment and household income, as well as the downside pressure on CPI & PPI from the Trump tariff hikes. Looking forward, the PBOC may cut RRR in 2Q25 and LPRs in 2H25 as the negative impact of Trump's tariffs might release and the stimulus effects of domestic policies could diminish. We expect additional RRR cuts by 50bps and LPR cuts by 20bps this year.

Figure 1: MoM Changes of China CPI in 2M25

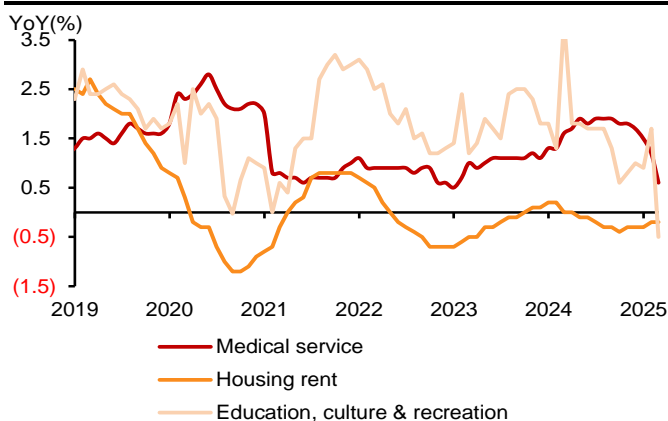
Source: Wind, CMBIGM

Figure 2: China CPI growth in staples

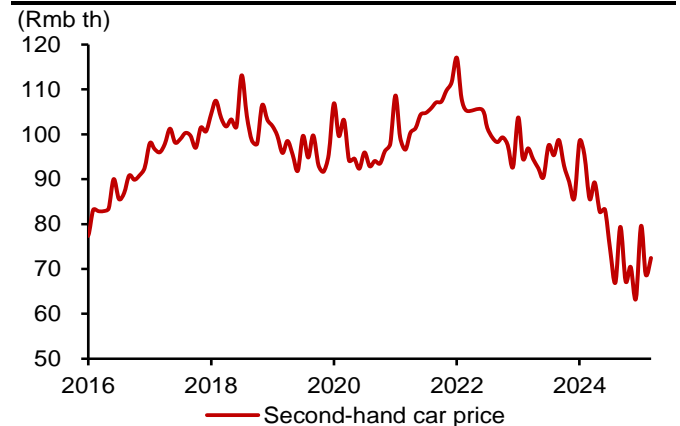
Source: Wind, CMBIGM

Figure 3: China CPI growth in durables

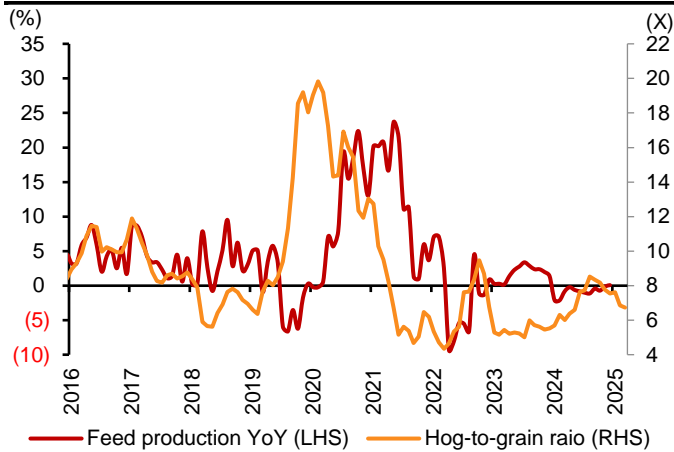
Source: Wind, CMBIGM

Figure 4: China CPI growth in services

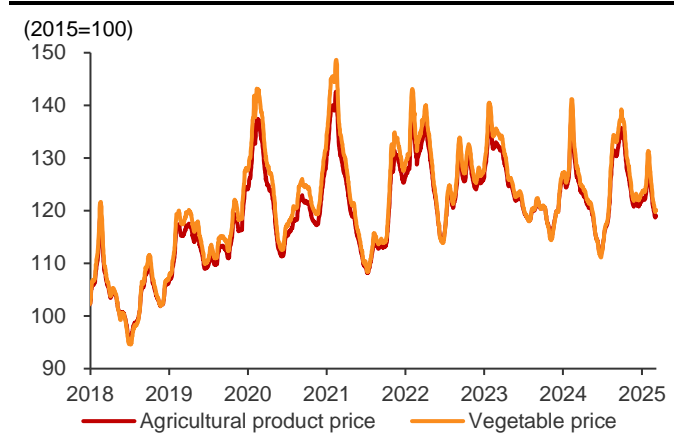
Source: Wind, CMBIGM

Figure 5: Second-hand car price in Shanghai

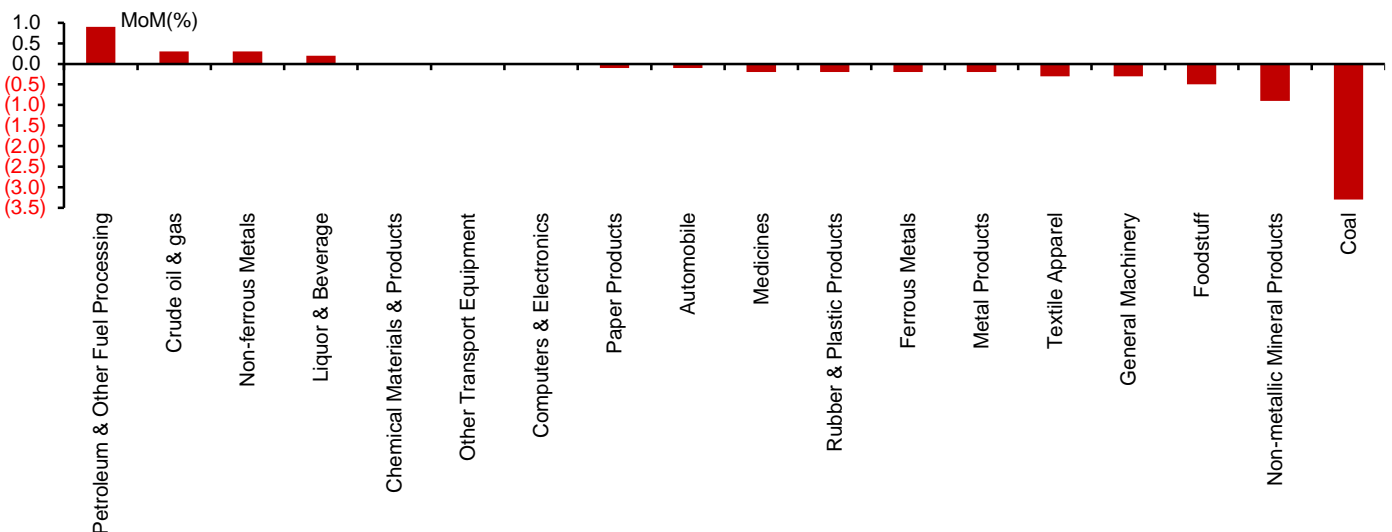
Source: Wind, CMBIGM

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

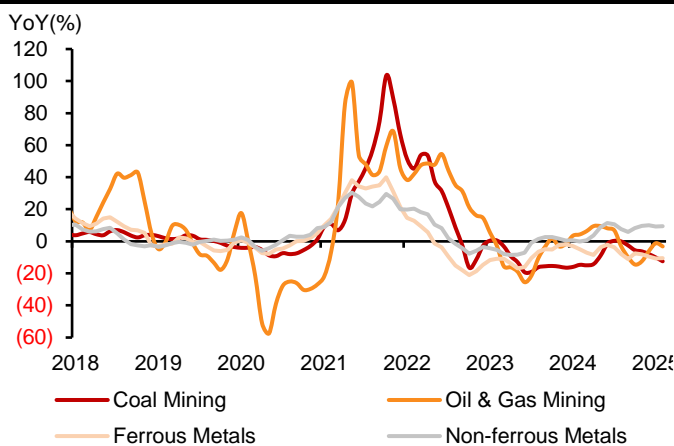
Source: Wind, CMBIGM

Figure 7: Agricultural and vegetable price

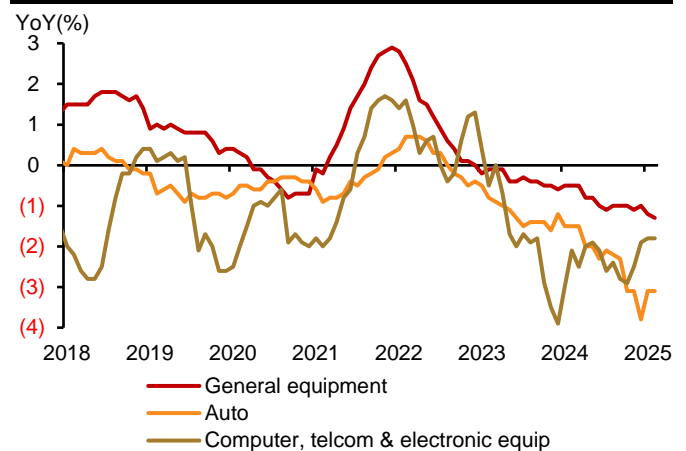
Source: Wind, CMBIGM

Figure 8: MoM changes of China PPI in Feb

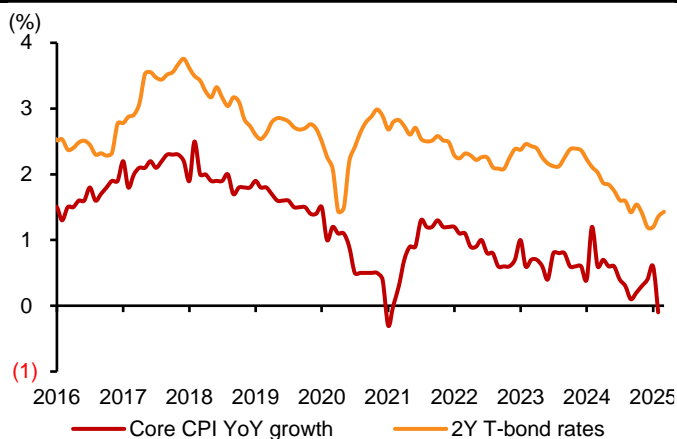
Source: Wind, CMBIGM

Figure 9: China PPI in energy & metals

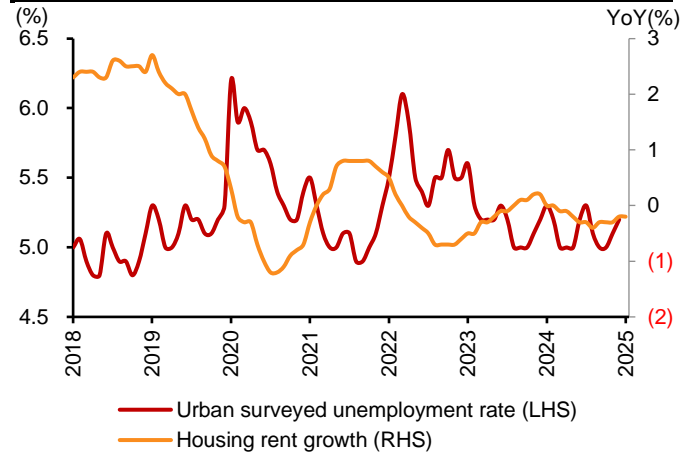
Source: Wind, CMBIGM

Figure 10: China PPI in equipment

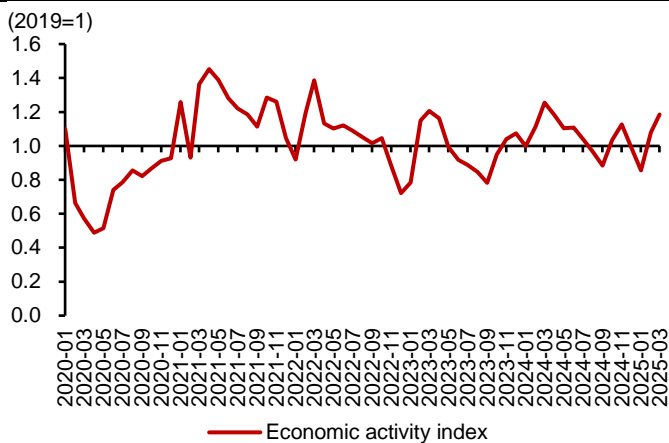
Source: Wind, CMBIGM

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

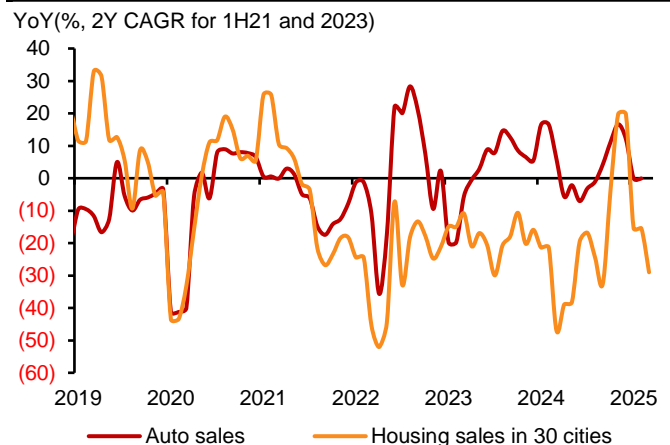
Source: Wind, CMBIGM

Figure 12: Unemployment rate and rent growth

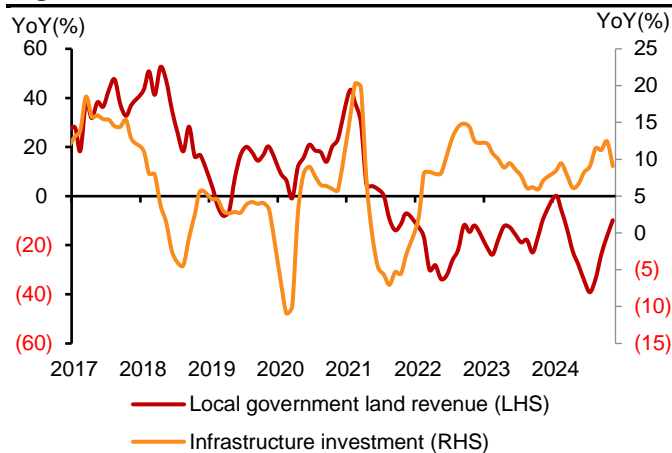
Source: Wind, CMBIGM estimates

Figure 13: China Economic Activity Index

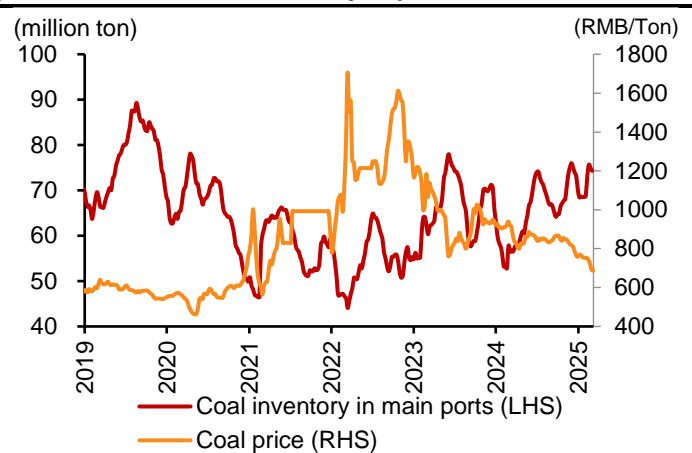
Source: Wind, CMBIGM

Figure 14: China auto & housing sales

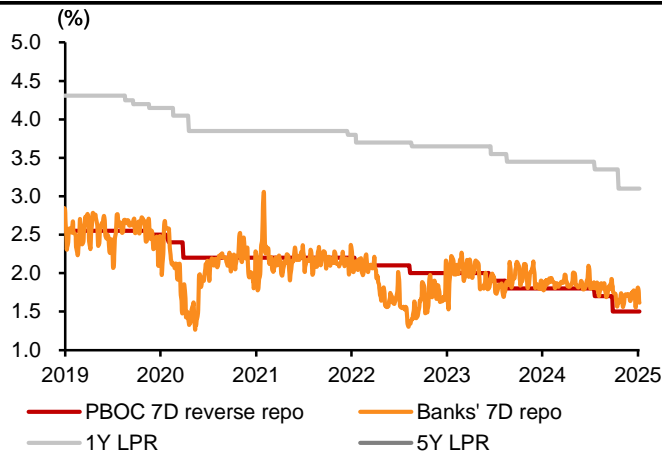
Source: Bloomberg, CMBIGM

Figure 15: Infrastructure investment in China

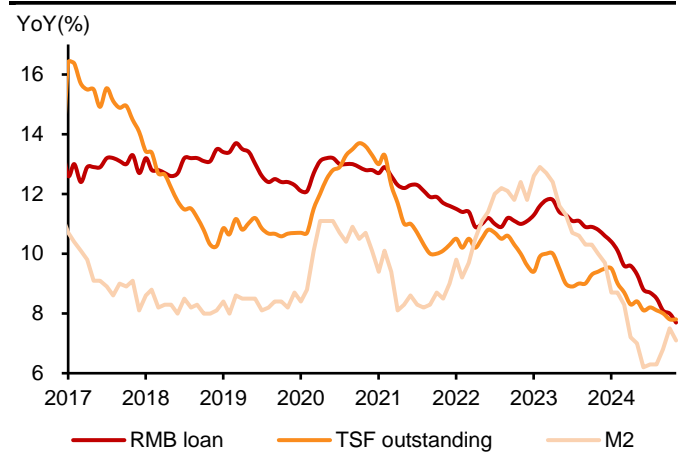
Source: Bloomberg, CMBIGM

Figure 16: China coal inventory & price

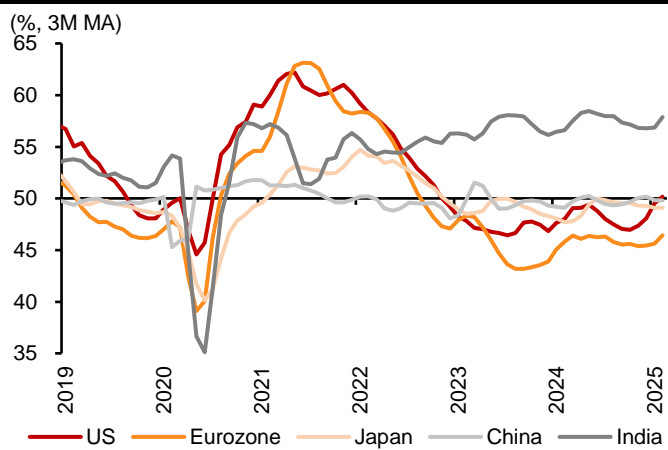
Source: Wind, CMBIGM

Figure 17: PBOC policy rates & liquidity condition

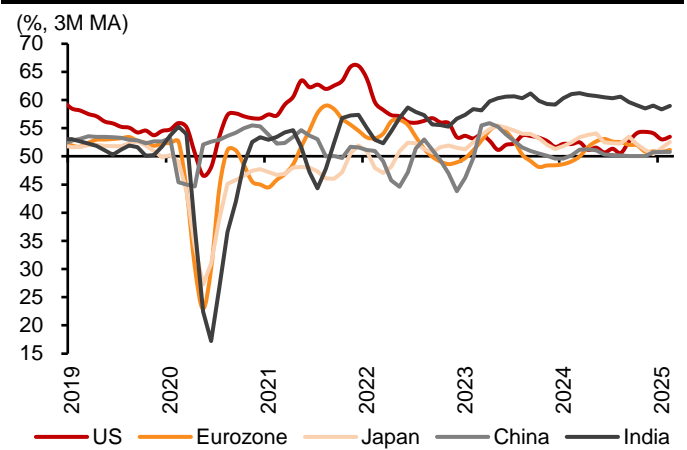
Source: Bloomberg, CMBIGM

Figure 18: China credit growth

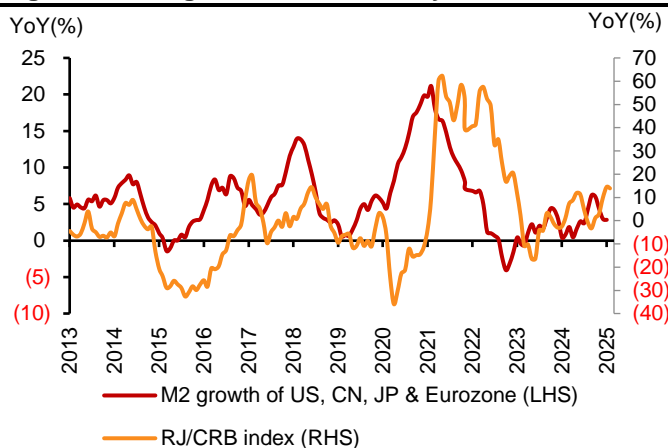
Source: Wind, CMBIGM

Figure 19: Manufacturing PMI of major economies

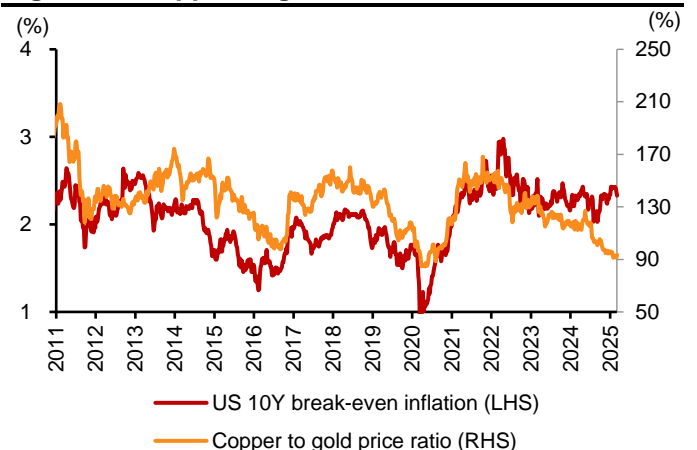
Source: Bloomberg, CMBIGM

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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CMB International Global Markets Limited

Address: 45/F, Champion Tower, 3 Garden Road, Hong Kong, Tel: (852) 3900 0888 Fax: (852) 3900 0800

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