

China Economy

Weak inflation points to easing policy stance ahead

China's consumer inflation slowed to 18-month low in March as food & energy prices retreated and domestic consumption recovery was in a gradual manner. The PPI further declined as global demand for goods dropped with a disinflation trend. Recent data showed China's economic resumption was still uneven in March as service activity strongly recovered but manufacturing performance was tepid amid weak exports. We expect China's inflation to remain low in 2Q23 and to pick up gradually in 2H23-1H24. CPI growth is expected to slightly rise from 2.2% in 2023 to 2.5% in 2024 and PPI is projected to drop 0.5% in 2023 before rising 1.6% in 2024. The weak inflation should point to easing macro policy stance this year as it indicates China's GDP growth remains below the potential growth with limited reflation risk. The priority for the Chinese policymakers is to restore confidence and growth momentum by maintaining easing macro policies and sending pro-business signals.

- CPI growth hit 18-month low as food & energy prices retreated and consumer demand remained weak.** CPI increased 0.7% YoY in March, down from 1.0% last month. Core CPI rose 0.7% YoY in March after climbing 0.6% in February as durable consumption demand remained weak and supply-side competition was tough. Within the CPI basket, food inflation slowed from 2.6% in February to 2.4% in March, while fuel price dropped 0.1% after rising 0.7%. Among food items, prices of pork and fruit rose 9.6% and 11.5% YoY in March due to low bases last year; however, vegetable price dropped 11.1% YoY in March as supply improved with the temperature. Among non-food items, prices of home appliances, vehicles and telecom equipment respectively dropped 0.2%, 3.3% and 2.2% YoY, suggesting slow demand recovery and tough competition in some durables. Prices of service items, such as education and home service, continued to rise but at a slower pace. Housing rent dropped for the 11th consecutive month as the employment and income condition for the young remained unpleasant.
- PPI further declined as overseas recession risk increased and disinflation accelerated.** PPI dropped 2.5% YoY in March after decreasing 1.4% YoY in February. PPI in coal mining, oil & gas mining, ferrous metals and non-ferrous metals respectively dropped 3.2%, 15.7%, 11.0% and 8% YoY in March as the overseas banking sector turmoil hit commodity prices in March by causing concerns about credit squeeze and economic recession. PPI in equipment was also weak as overseas capex and durable consumption slowed amid high interest rates and economic uncertainty. From the MoM perspective, PPI of ferrous metals, computers & electronics and liquor & beverage rose 1.3%, 0.4% and 0.2%, while coal, paper products and crude oil & gas dropped 1.2%, 1.1% and 0.9%.
- We maintain forecast for CPI growth at 2.2% and that for PPI growth at -0.5% in 2023.** The CPI growth may remain low in March and April and then gradually climb as the economy continues to recover. We expect the CPI growth to reach 2.2% in 2023 and 2.5% in 2024. The PPI may further decline in April before gradually improving in 2H23. We expect the PPI to drop 0.5% in 2023 and rise 1.6% in 2024.
- The weak inflation indicates easing policy stance ahead.** China's economic recovery was still uneven. Passenger flow rapidly resumed after

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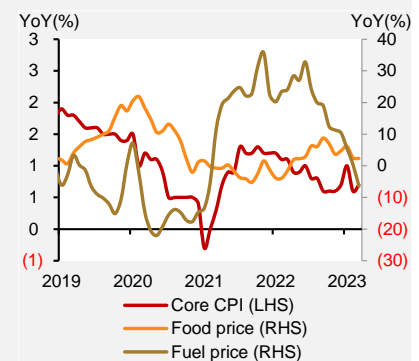
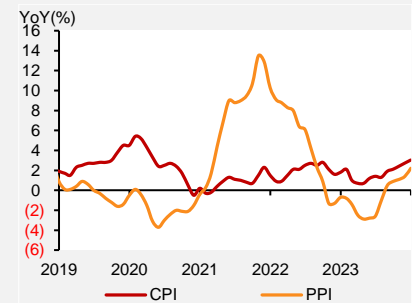
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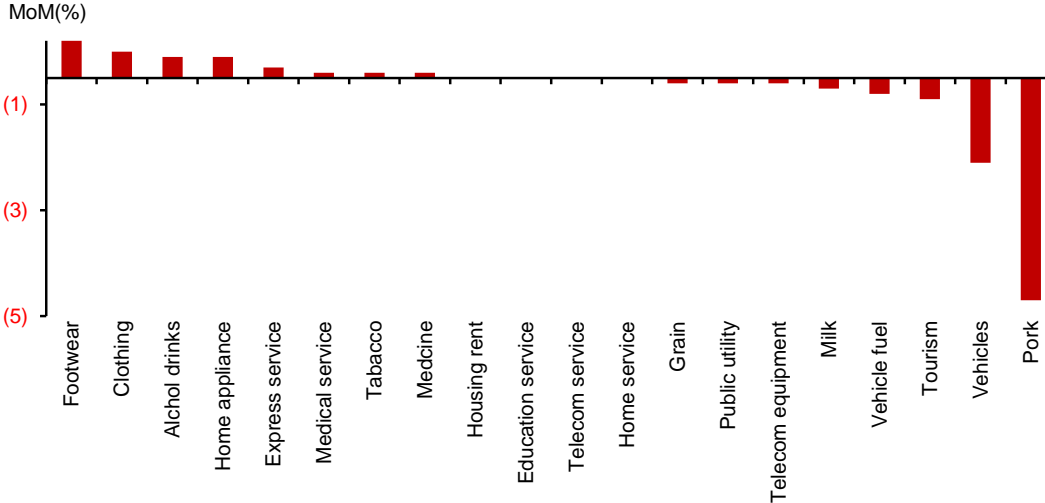
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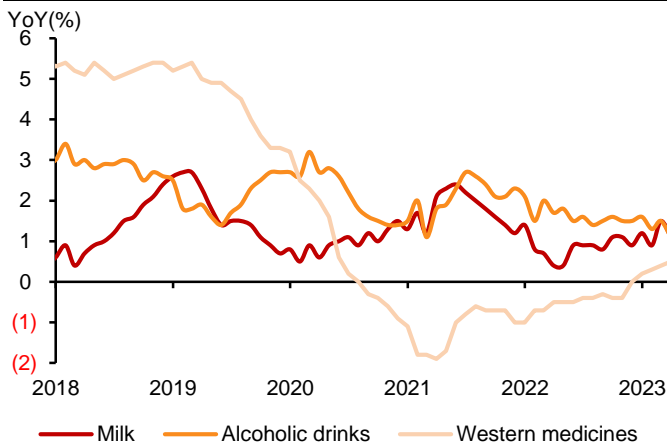
China's reopening, but consumer confidence remained weak. Service activity improved noticeably, but industrial output seemed tepid with weak exports. The weak inflation indicates China's GDP growth remains below the potential growth with limited reflation risk. The priority for the country is to restore confidence and growth momentum by maintaining easing macro policies and sending pro-business signals.

Figure 1: MoM Changes of China CPI in March



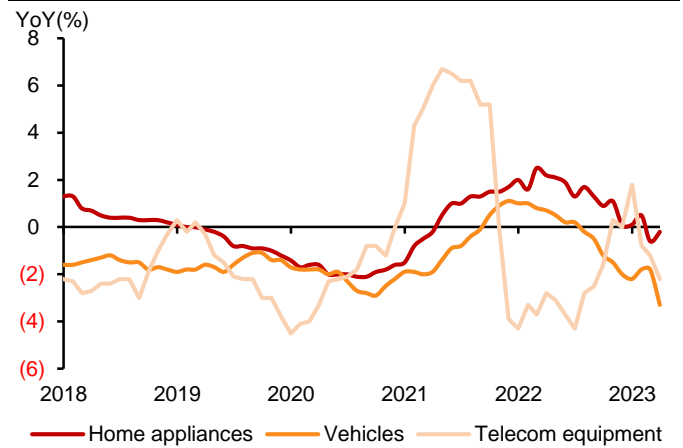
Source: Wind, CMBIGM estimates

Figure 2: China CPI Growth in Staples



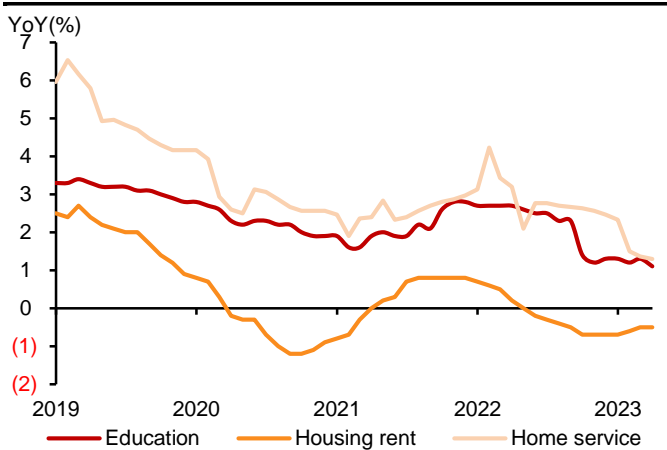
Source: Wind, CMBIGM

Figure 3: China CPI Growth in Durables



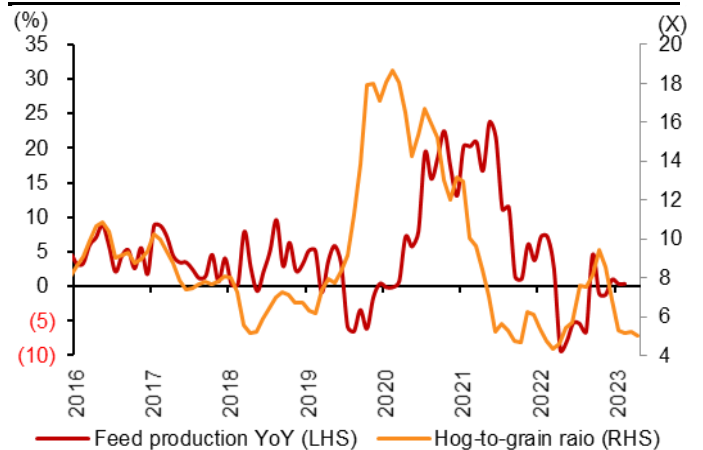
Source: Wind, CMBIGM

Figure 4: China CPI Growth in Services



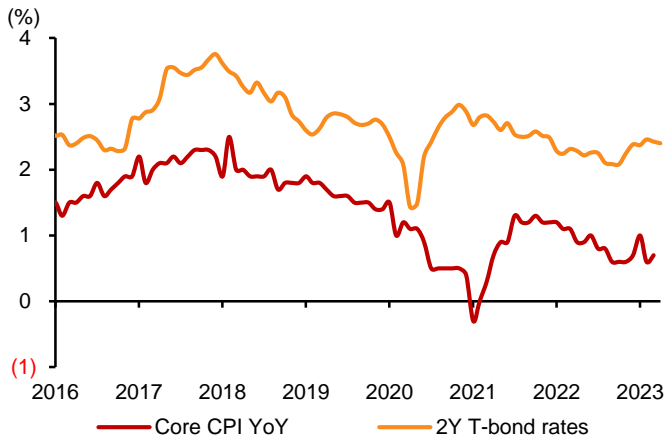
Source: Wind, CMBIGM

Figure 5: Hog-to-grain Ratio in China



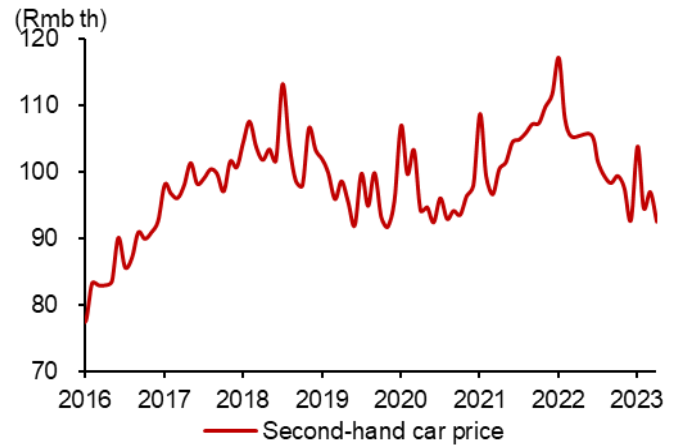
Source: Wind, CMBIGM

Figure 6: China Core CPI Growth & 2Y T-bond Rates



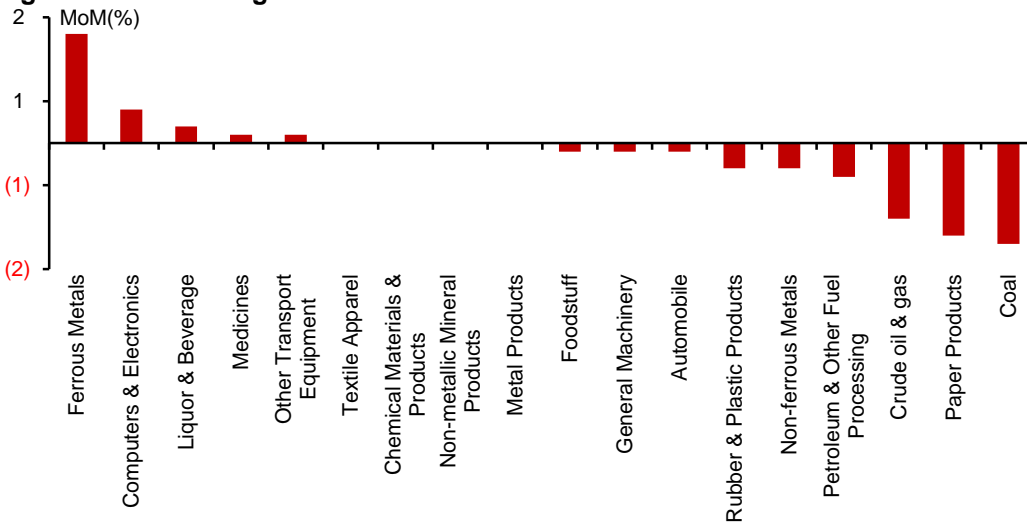
Source: Wind, CMBIGM

Figure 7: Second-hand Car Price in Shanghai



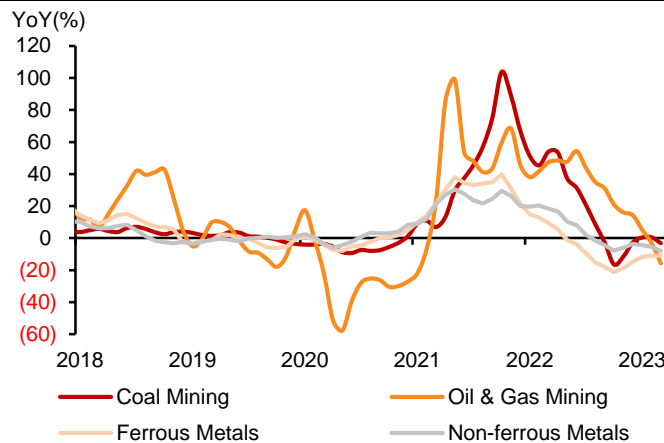
Source: Wind, CMBIGM

Figure 8: MoM Changes of China PPI in March



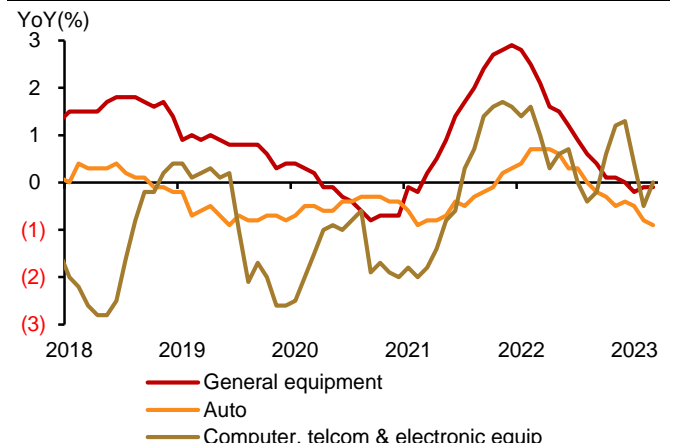
Source: Wind, CMBIGM estimates

Figure 9: China PPI in Energy & Metal



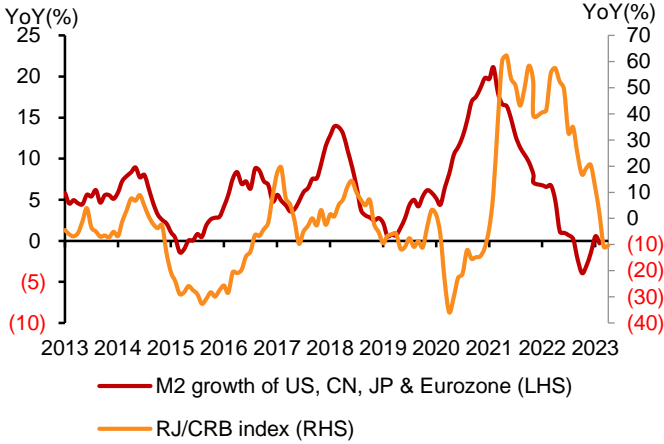
Source: Wind, CMBIGM

Figure 10: China PPI in Equipment



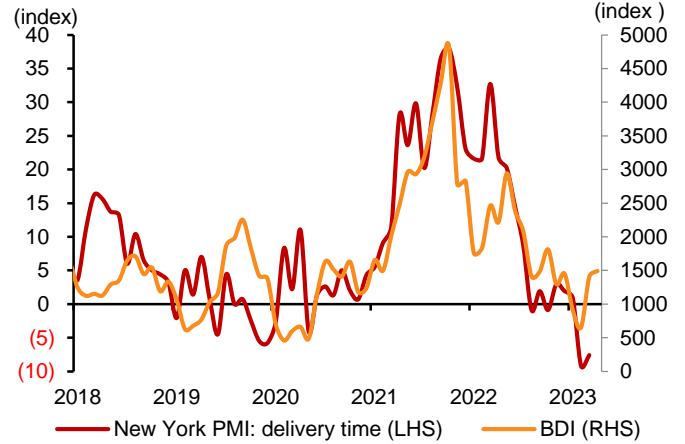
Source: Wind, CMBIGM

Figure 11: Global M2 Growth & Commodity Inflation



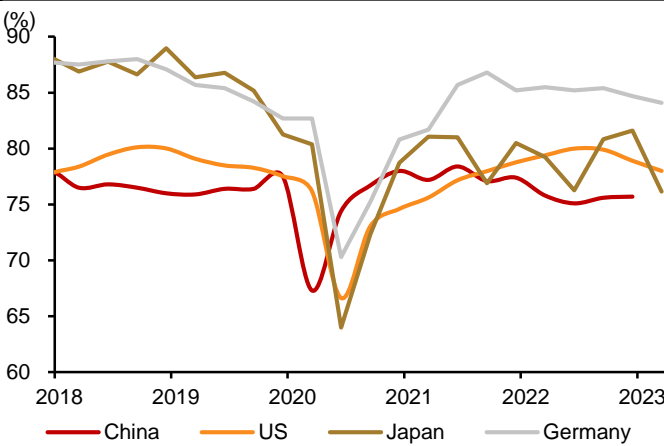
Source: Wind, CMBIGM

Figure 12: Global Supply Chain Pressure



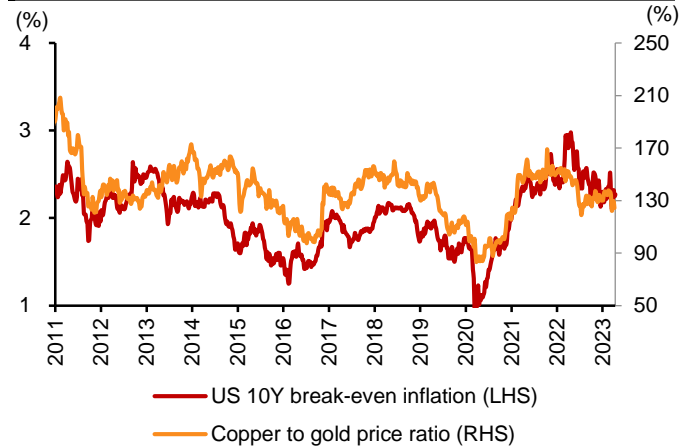
Source: Wind, CMBIGM

Figure 13: Manufacturing Capacity Utilisation Ratio



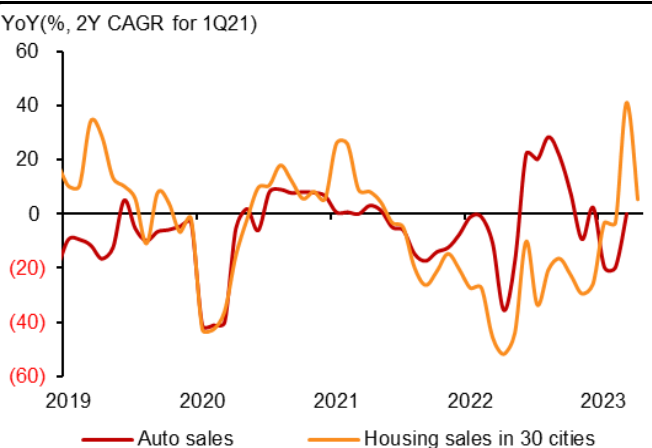
Source: Wind, CMBIGM

Figure 14: Copper-to-gold Ratio



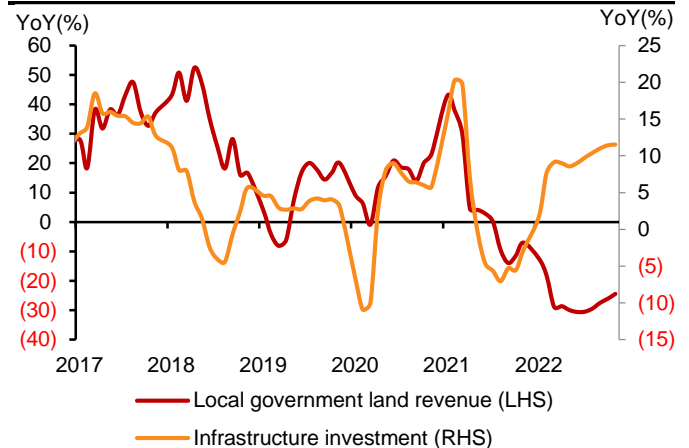
Source: Bloomberg, CMBIGM

Figure 15: China Auto & Housing Sales



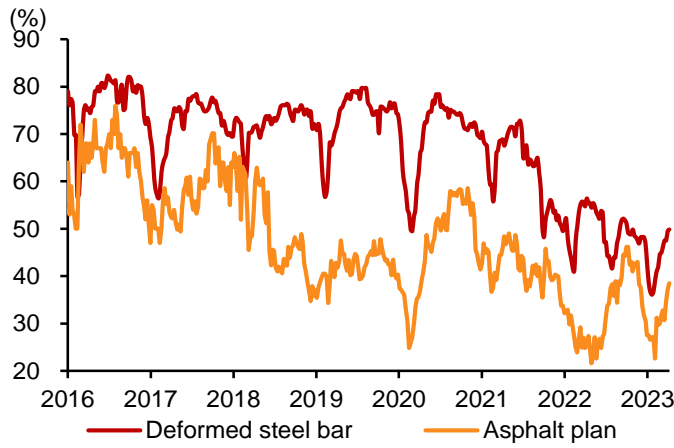
Source: Bloomberg, CMBIGM

Figure 16: Infrastructure Investment in China



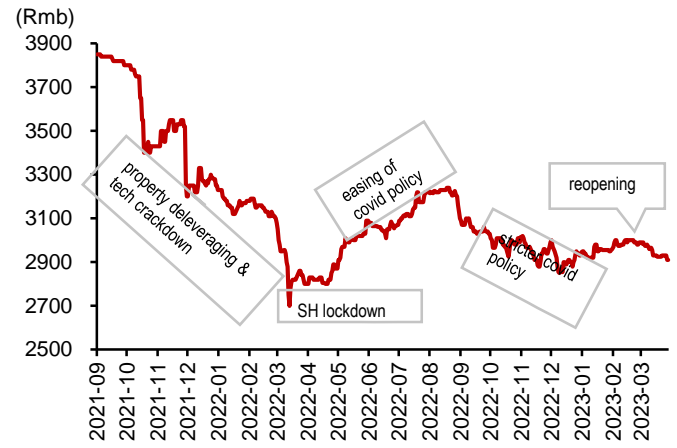
Source: Wind, CMBIGM

Figure 17: Operation Rate in China



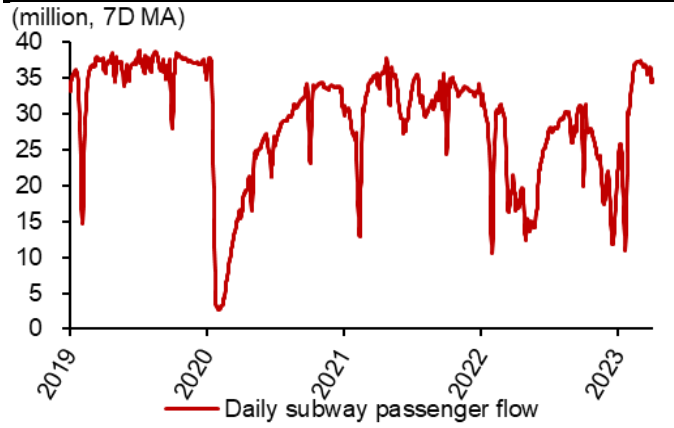
Source: Bloomberg, CMBIGM

Figure 18: MOUTAI Wholesale Reference Price



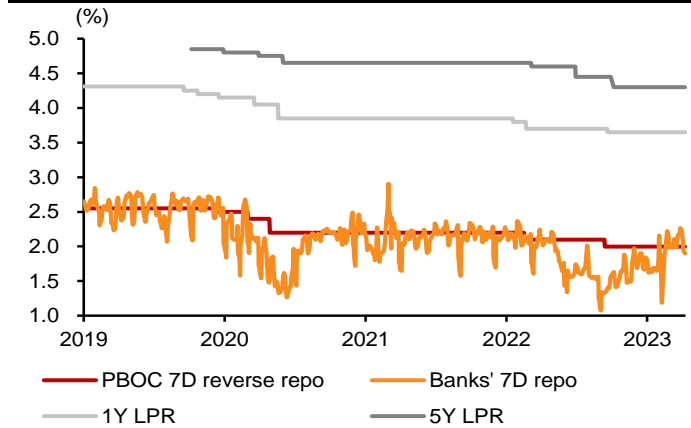
Source: Wind, CMBIGM

Figure 19: Mobility Indicators in China's Tier-1 Cities



Source: Bloomberg, CMBIGM

Figure 20: PBOC Policy Rates & Liquidity Condition



Source: Wind, CMBIGM

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