

China Economy

Deflation continued to ease

China's deflationary pressure continued to ease in early 2026. CPI slowed to 0.2% YoY in Jan, primarily due to a high base effect and volatile food pricing. Core inflation remained robust driven by durable goods, tourism and jewellery prices. PPI beat market expectation again as price relation in upstream sectors passed through, particularly the non-ferrous metals, while PPI of consumer goods remained relatively subdued. We expect mild price reflation to continue in 2026 driven by the anti-involution campaign, AI-related investment and global commodities rally, which should improve corporate profitability and support capital-market performance of materials and cyclical sectors. Price reflation remains largely supply-driven right now. We expect further demand-side policies will address the imbalance, including stabilizing the property market by lowering mortgage rates and purchasing unsold property, and stimulating consumption by increasing fiscal subsidies and strengthening the social safety net. We expect the CPI and PPI to reflate from 0.1% and -2.6% in 2025 to 0.9% and 0.5% in 2026.

■ **Food price dynamics and base effects were the primary drivers behind the shift in headline CPI.** China's CPI YoY moderated to 0.2% in Jan from 0.8% in Dec, coming in slightly below the market expectation of 0.4%. In sequential terms, CPI remained flat at 0.2% MoM. Food prices showed weaker than normal seasonality ahead of the Chinese New Year (CNY) with 0% MoM and -0.7% YoY growth. Pork prices saw 1.2% MoM growth, the first time in 17 months, as live hog inventory edged down. Conversely, fresh vegetable prices saw a drop of -4.8% MoM following a prior seasonal peak. Vehicle fuel prices also declined by 1.2% MoM as global crude oil prices stayed soft. We expect headline CPI to rebound to 1.1% in Feb as food price and vehicle fuel prices pick up during the holiday season.

■ **Core CPI remained robust as durable goods price reflat.** Core inflation edged down to 0.8% YoY in Jan from 1.2% in Dec due to base effect, while its MoM expanded to 0.3%. Durable goods saw notable price reflation as the holiday approached, with household appliances and telecom equipment rising 0.7% and 0.9% MoM respectively, while transport vehicle prices edged up 0.3% MoM. Other supplies and services including gold jewellery surged 2.7% MoM in Jan, likely contributing significantly to the core inflation reading as gold prices stayed elevated. Service price growth edged up to 0.2% MoM in Jan, as tourism price and home service rose by 1.8% and 1.7% MoM while education and telecom services remained unchanged. Medical services continued their reflationary trend since April, expanding 0.4% MoM in Jan and reflecting the persistent impact of medical service price reforms, while housing rent saw another drop of 0.1% MoM.

■ **PPI sustained its recovery momentum.** The YoY contraction of PPI narrowed to -1.4% in Jan from -1.9% in Dec, beating market expectations of -1.5%. The MoM growth reached 0.4%, the highest in 28 months, driven by the pass-through of reflation. Extraction sector dropped 1.7% MoM in Jan after the rally in 2H25 as coal and crude oil & natural gas mining dropped 3.2% and 2.2% respectively, while non-ferrous metals price remained robust. Raw materials and processing sectors rose 0.7% and 0.5% MoM in Jan as chemical products manufacturing and non-ferrous metal smelting & processing rose 0.6% and 5.2% MoM. AI-related sectors including semiconductors and storage device saw notable price increase, while anti-involution sectors including lithium batteries, cement and photovoltaic equipment continued to see price reflation. However, downstream sectors remained subdued, as PPI of consumer goods stayed near flat at 0.1% in Jan MoM. Household necessities and clothing dropped by 0.1% and 0.3% MoM respectively, while durable goods rebounded 0.3% in Jan.

Bingnan YE, Ph.D

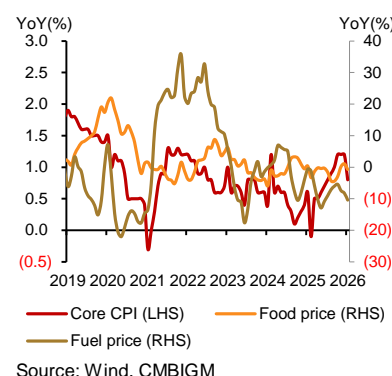
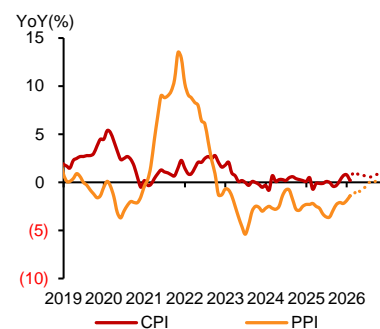
(852) 3761 8967

yebingnan@cmbi.com.hk

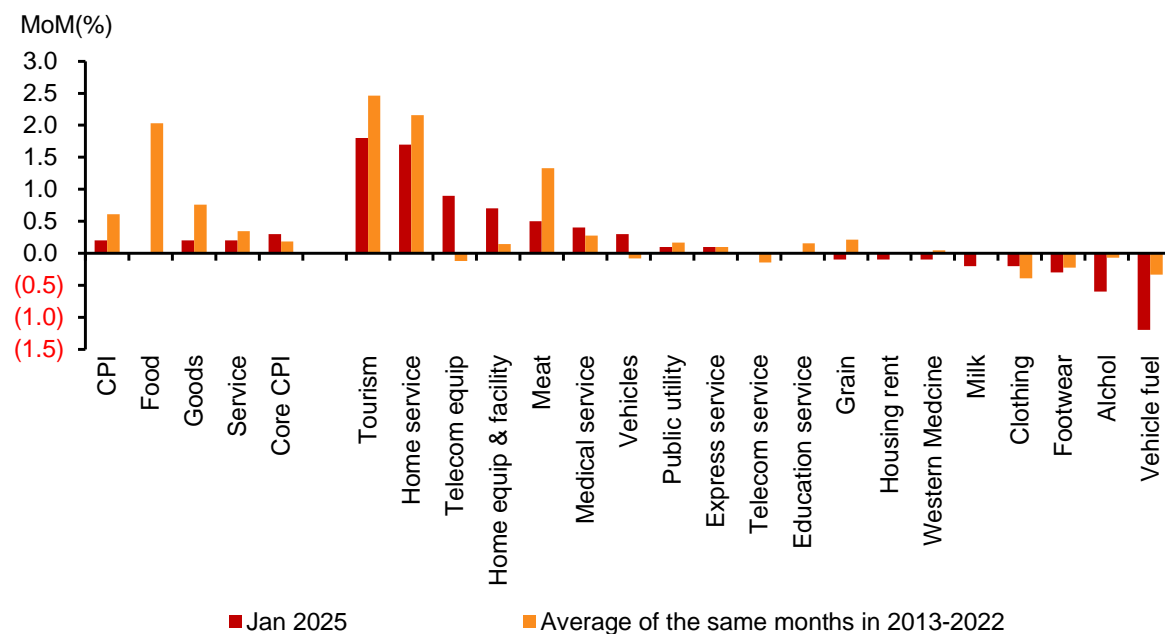
Frank Liu

(852) 3761 8957

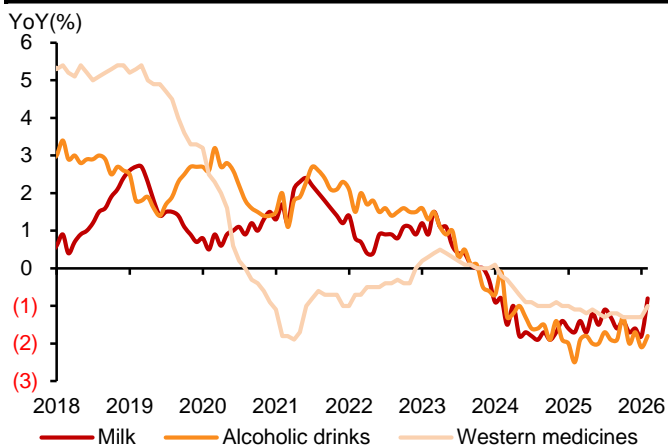
frankliu@cmbi.com.hk



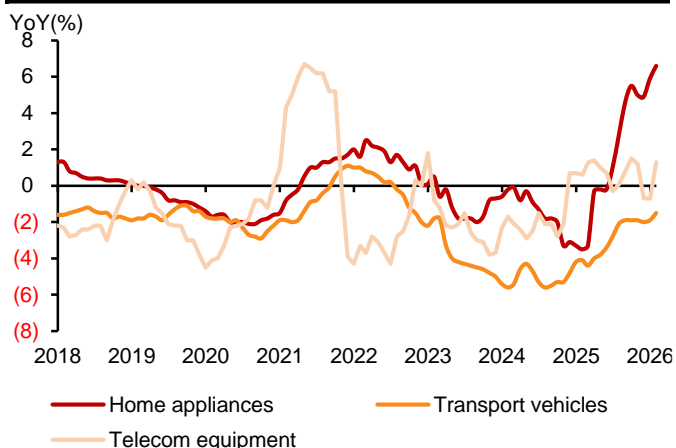
- **We expect mild price reflation driven by anti-involution campaign, AI-related investment and global commodities rally.** We expect the CPI and PPI to reflate from 0.1% and -2.6% in 2025 to 0.9% and 0.5% in 2026, thanks to the anti-involution campaign, AI-related investment and global commodities rally. The rebound in price level should improve corporate profitability and support capital-market performance especially in the materials and cyclical sectors, as we have seen the total profit growth of industrial enterprises picked up to 0.6% in 2025 from -3.3% in 2024. However, price reflation remains largely supply-driven, led by international non-ferrous metals prices, gold jewellery and vegetables, while consumer demand and downstream pricing power remained soft. Looking forward, we expect demand-side policies to focus on stabilizing the property market by lowering mortgage rates and purchasing unsold property, and stimulating consumption by increasing fiscal subsidies and strengthening the social safety net.

Figure 1: MoM Changes of China CPI in Jan

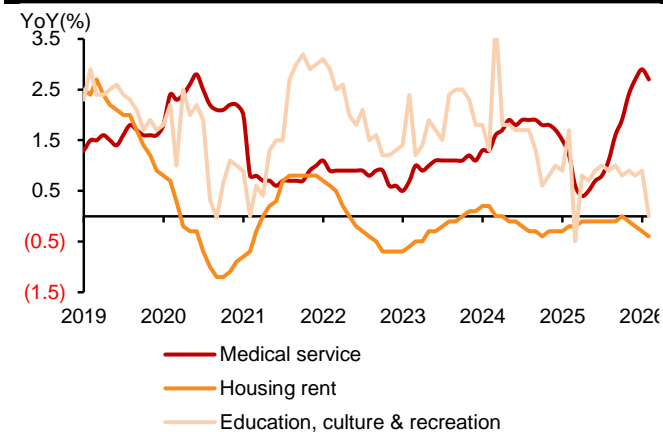
Source: Wind, CMBIGM

Figure 2: China CPI growth in staples

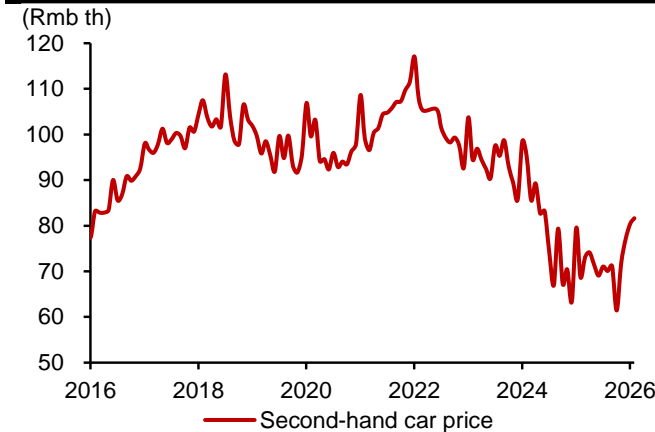
Source: Wind, CMBIGM

Figure 3: China CPI growth in durables

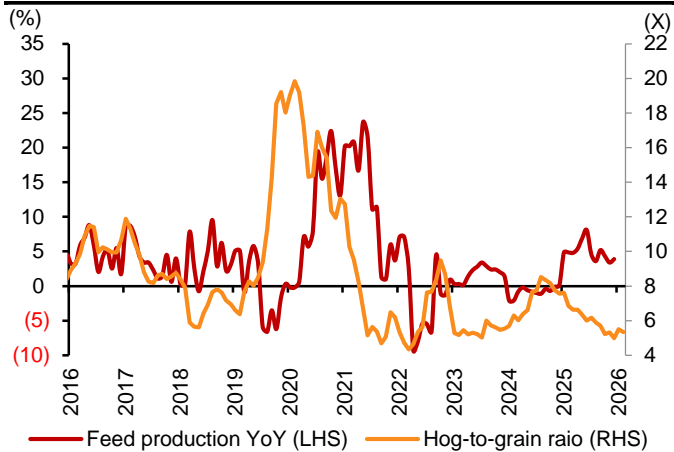
Source: Wind, CMBIGM

Figure 4: China CPI growth in services

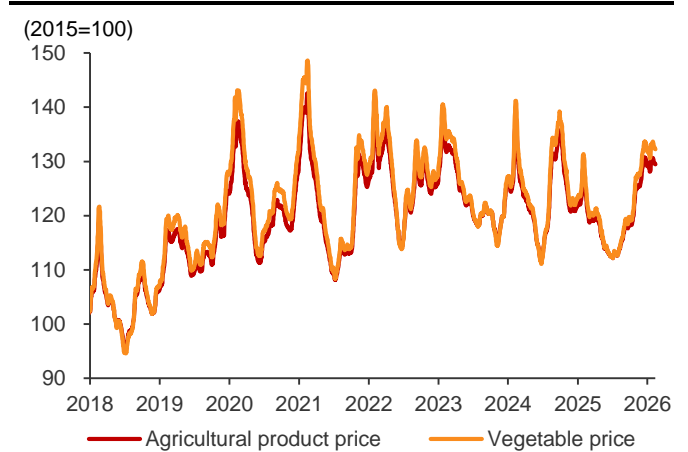
Source: Wind, CMBIGM

Figure 5: Second-hand car price in Shanghai

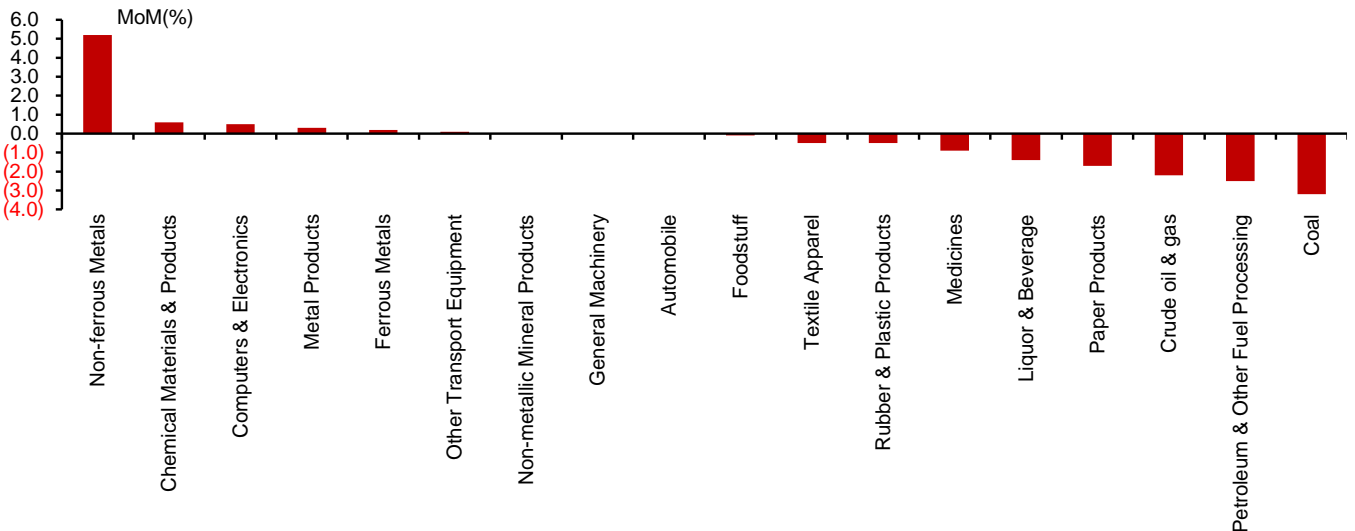
Source: Wind, CMBIGM

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

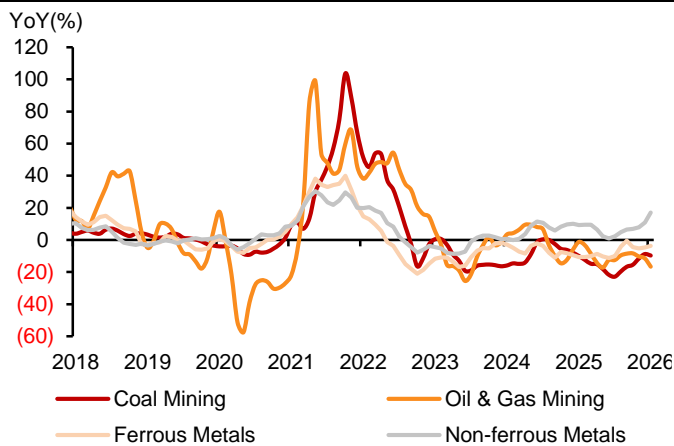
Source: Wind, CMBIGM

Figure 7: Agricultural and vegetable price

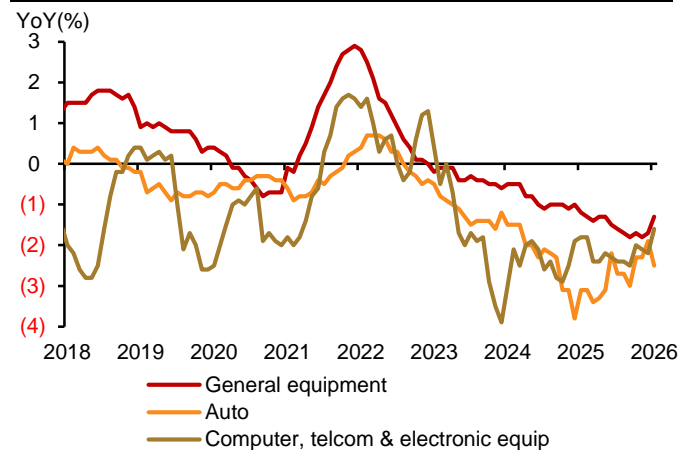
Source: Wind, CMBIGM

Figure 8: MoM changes of China PPI in Dec

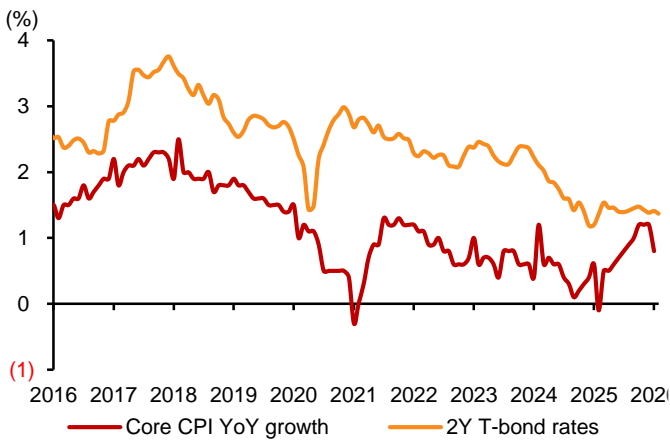
Source: Wind, CMBIGM

Figure 9: China PPI in energy & metals

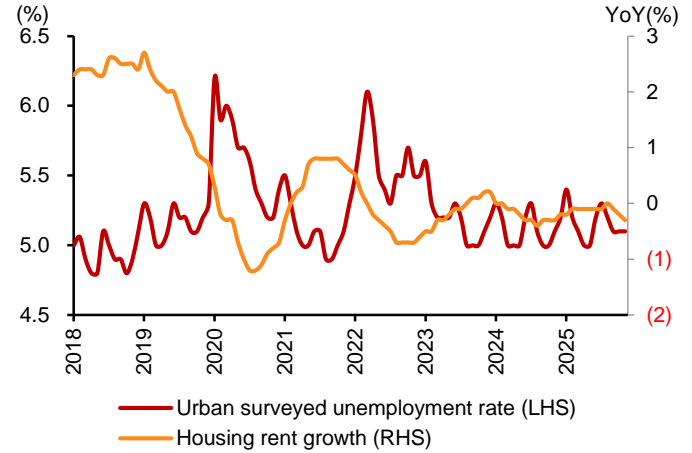
Source: Wind, CMBIGM

Figure 10: China PPI in equipment

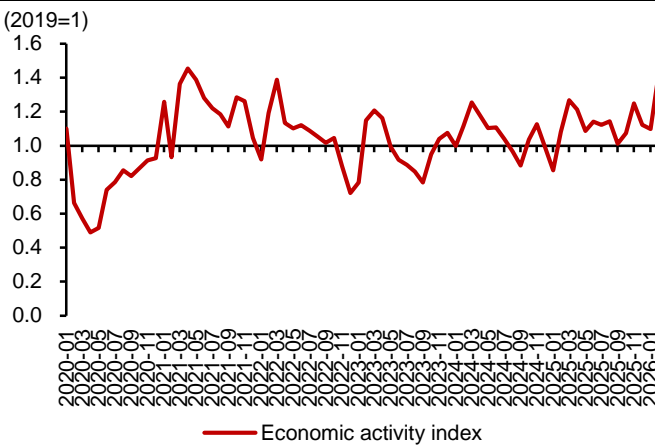
Source: Wind, CMBIGM

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

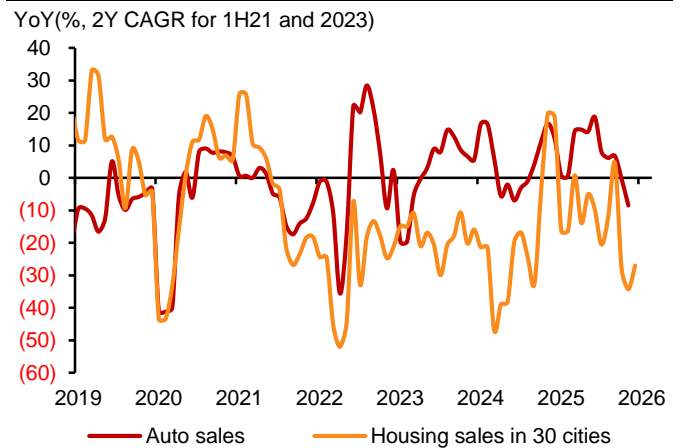
Source: Wind, CMBIGM

Figure 12: Unemployment rate and rent growth

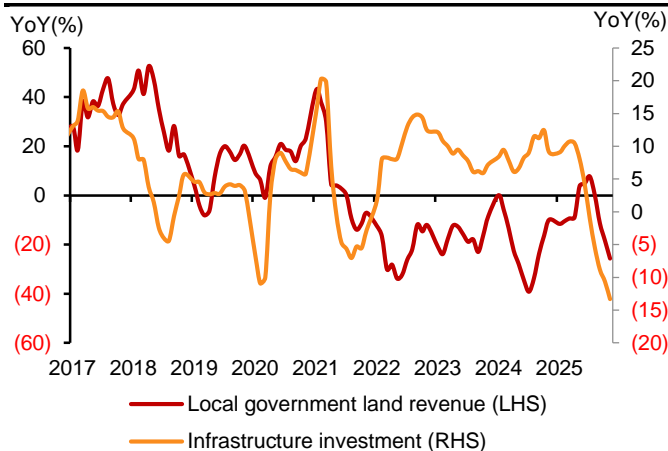
Source: Wind, CMBIGM estimates

Figure 13: China Economic Activity Index

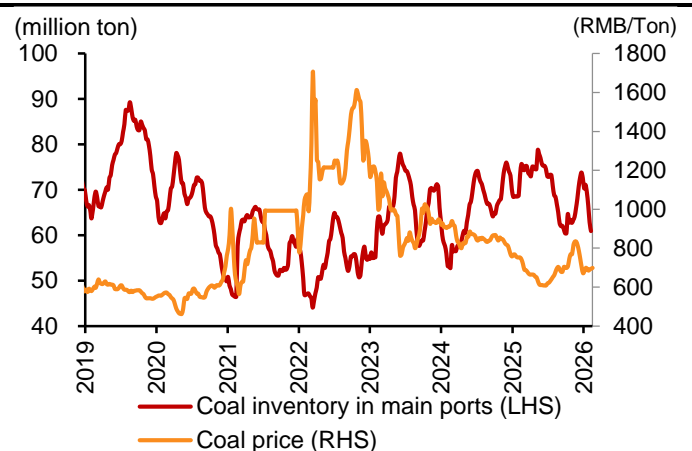
Source: Wind, CMBIGM

Figure 14: China auto & housing sales

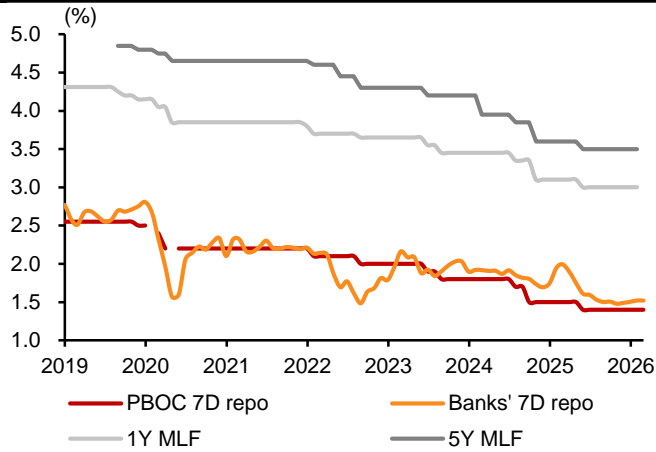
Source: Bloomberg, CMBIGM

Figure 15: Infrastructure investment in China

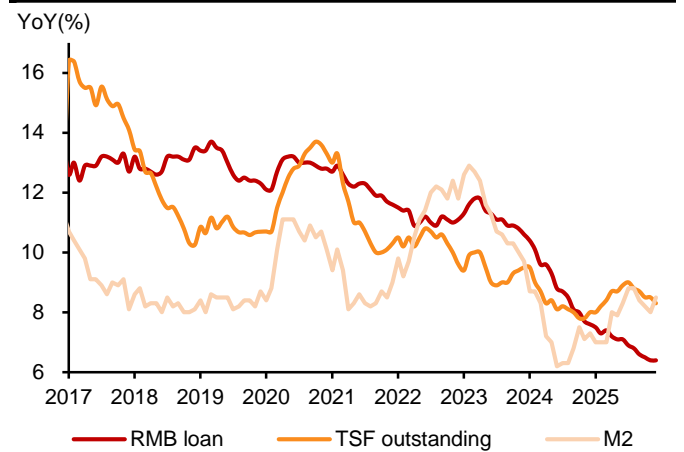
Source: Bloomberg, CMBIGM

Figure 16: China coal inventory & price

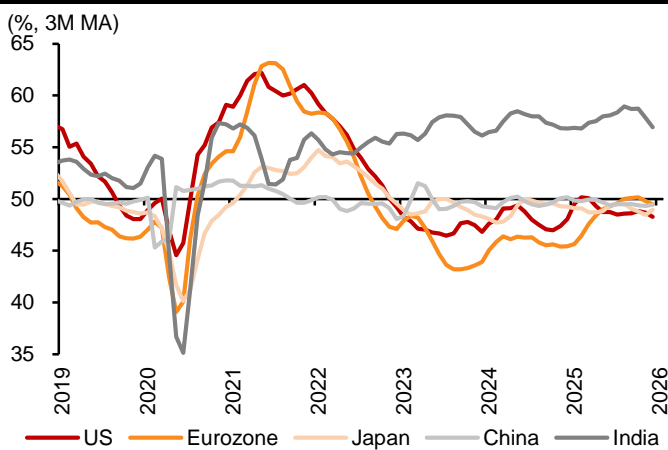
Source: Wind, CMBIGM

Figure 17: PBOC policy rates & liquidity condition

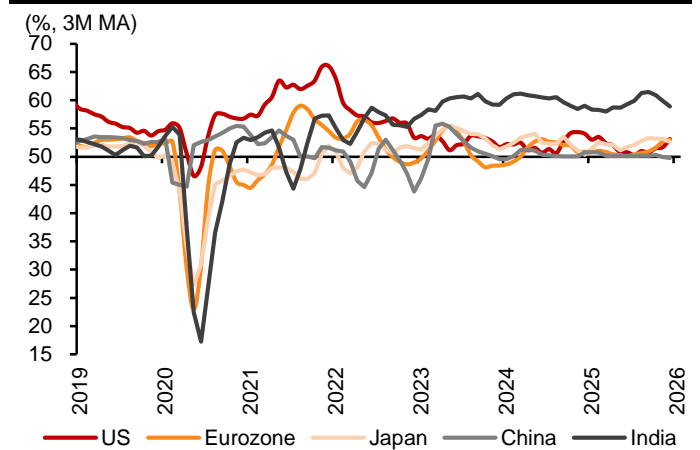
Source: Bloomberg, CMBIGM

Figure 18: China credit growth

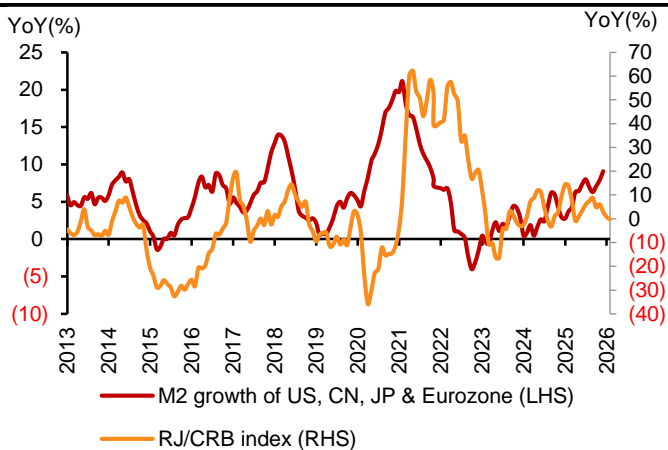
Source: Wind, CMBIGM

Figure 19: Manufacturing PMI of major economies

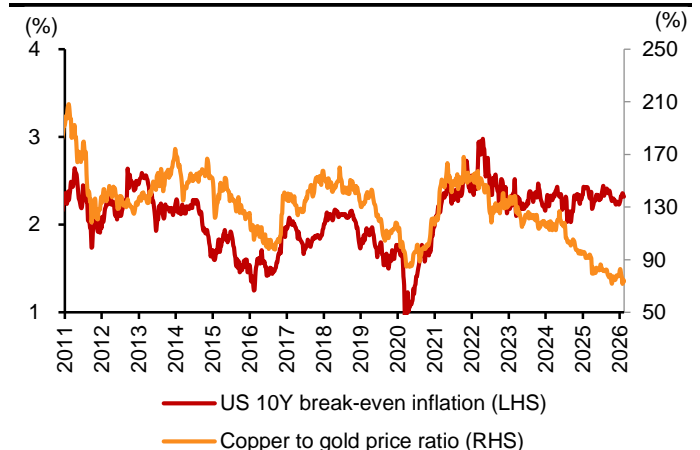
Source: Bloomberg, CMBIGM

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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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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