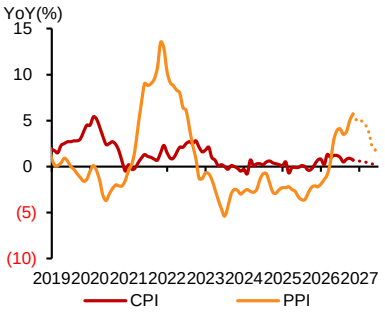
China Economy

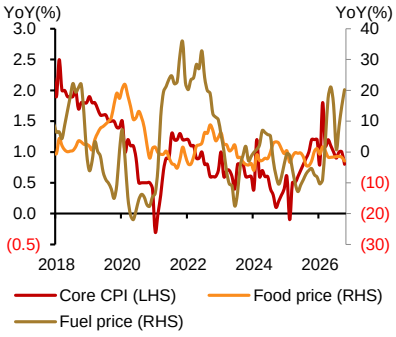
Upstream gains, downstream strains

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October's inflation data highlight a widening divergence between upstream cost pressures and final-demand pricing power due to subdued final demand. CPI eased to 0.7% YoY and core inflation softened to 0.8%, as food and gold inflation weakened; durable-goods prices remained subdued and services inflation moderated, despite sharp increases in energy and electronics prices. PPI accelerated to 5.7%, driven primarily by energy and chemicals. The divergence favors selected upstream producers but threatens downstream margins as input cost hikes outpace selling prices. Aggregate industrial profits could therefore remain strong, albeit without generating a broad recovery in hiring, wages and private investment, limiting support for consumption. Moderating PPI inflation could support a broader economic recovery if driven by a sustained decline in oil prices, which would ease downstream cost pressures and improve household purchasing power, making slower producer inflation potentially supportive of a broader economic recovery.



Forecast numbers from Nov 2026
Source: Wind, CMBIGM

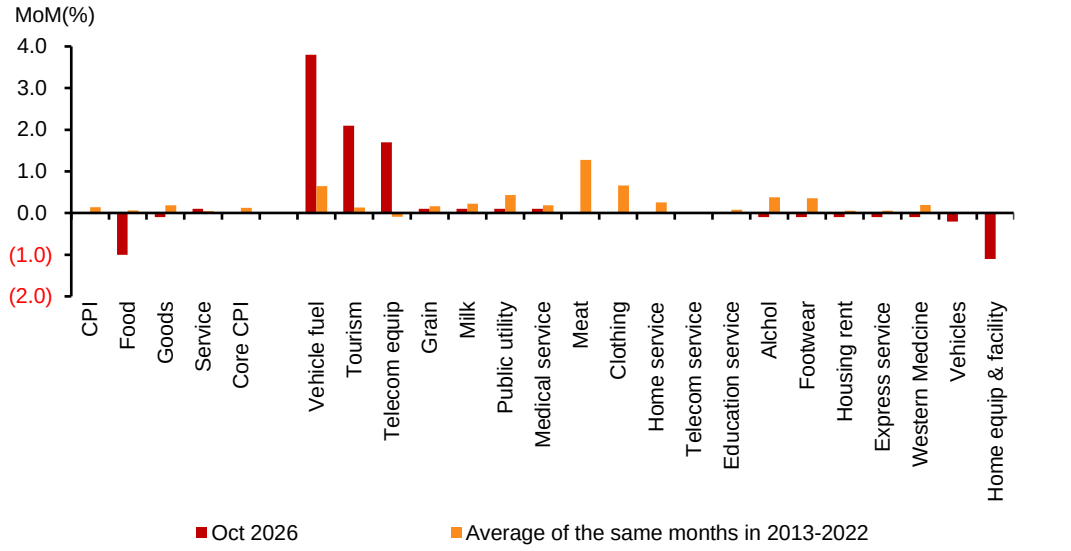


Source: Wind, CMBIGM

- **CPI moderated as food and gold's contribution outweighed gasoline's.** CPI slowed to 0.7% YoY in October from 0.9% in September, below market expectations at 0.8%. MoM was unchanged following a 0.2% increase. Food prices fell 1.0% MoM, with fresh vegetables down 5.8% and pork down 1.0%. Gold jewellery inflation slowed sharply to 4.5% YoY from 22.5%, while vehicle fuel accelerated to 20.2%. Food and gold together reduced their contributions to annual headline inflation by approximately 0.29ppt, outweighing a 0.16ppt increase in gasoline's contribution. We've seen a gradual recovery in pork price after the government intervention, as declining breeding sow inventory has driven up the pork wholesale price.
- **Core inflation is becoming more dependent on a technology-price impulse.** Core CPI eased to 0.8% YoY in October from 1.0% in September and remained flat MoM for a second consecutive month. The gold correction explains part of the slowdown, but pricing outside gold and electronics remains subdued. Home-appliance prices fell 1.1% MoM, vehicle prices declined 0.2%, and rents slipped another 0.1%. Services inflation softened to 0.7% YoY despite the holiday-related rebound in tourism. Communication-equipment prices remained an exception, rising 16.1% YoY, but their monthly increase slowed to 1.7% from 3.6%. Further up the supply chain, electronics producer-price growth moderated to 0.1% MoM from 0.4%, suggesting that the technology-price impulse could fade before household-facing inflation strengthens.
- **PPI accelerated, but price transmission remains concentrated in intermediate inputs.** PPI rose to 5.7% YoY in October from 5.0% in September, beating market expectations at 5.4%, although monthly inflation slowed to 0.7% from 1.2%. Energy is the major driver, as fuel processing and crude oil & gas extraction increased 6.1% and 6% respectively. Chemical-product prices rose 3.1% MoM, accelerating from 2.4%, while coal moderated to 2.7% from 9.5%. Paper products, smelting of ferrous and non-ferrous metals, machinery, automobile and other transportation equipment remained subdued. Consumer-goods PPI fell 0.1% MoM after two consecutive increases, and durable-goods prices also declined 0.1%. Meanwhile, producer purchase prices increased 1.1% MoM, exceeding factory-gate inflation of 0.7%. The divergence signals continued pressure on firms unable to pass higher costs through to customers.
- **The PPI–CPI divergence can lift aggregate industrial profits while weakening the breadth of the economic recovery.** The gap between PPI and CPI widened to 5.0ppt from 4.1ppt, as profits are increasingly being

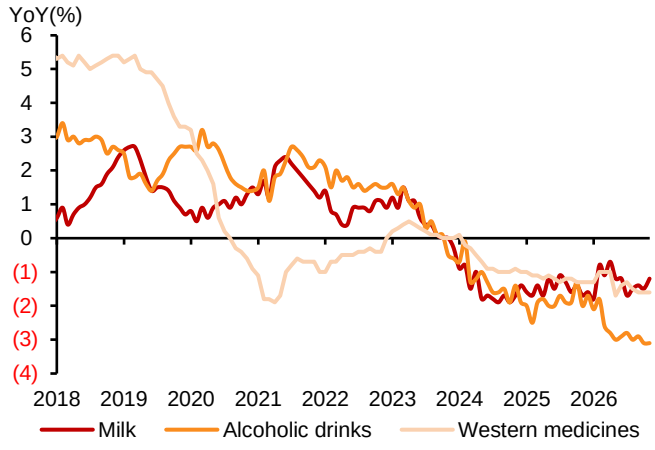
redistributed towards energy and selected materials producers, while downstream manufacturers face higher costs and limited selling-price increases due to weak final demand. Aggregate industrial profits could consequently remain strong even as profitability deteriorates across a wider range of firms. The concentrated upstream gains may provide less support to the hiring-wages-consumption/private investment cycle than a broad earnings recovery. Moderating CPI offers households some purchasing-power relief from rising energy cost, but that benefit could be offset if employers respond to margin pressures by restraining pay and recruitment. We therefore see the divergence as a potential headwind to domestic demand, despite stronger nominal industrial revenues. Conversely, a sustained oil-price decline could improve downstream margins and household purchasing power even as PPI falls, which we believe could cultivate a healthier adjustment.

Figure 1: MoM changes of China CPI



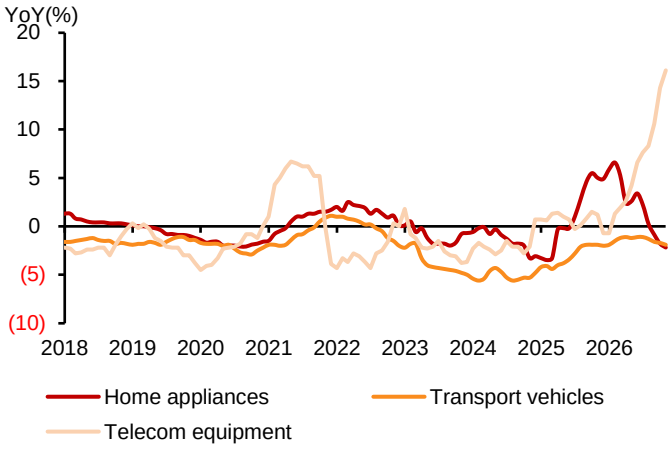
Source: Wind, CMBIGM

Figure 2: China CPI growth in staples



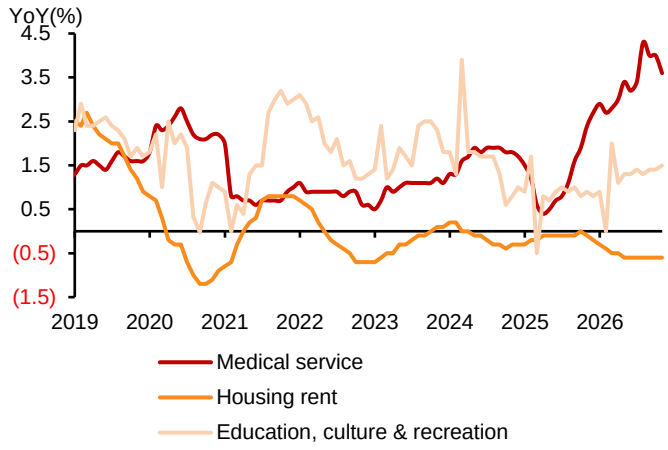
Source: Wind, CMBIGM

Figure 3: China CPI growth in durables



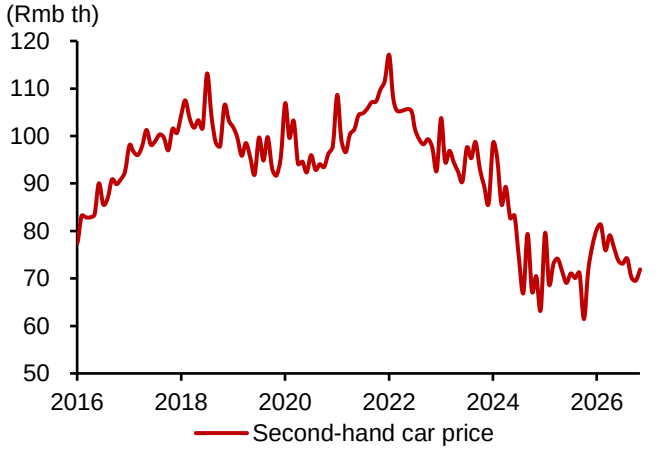
Source: Wind, CMBIGM

Figure 4: China CPI growth in services



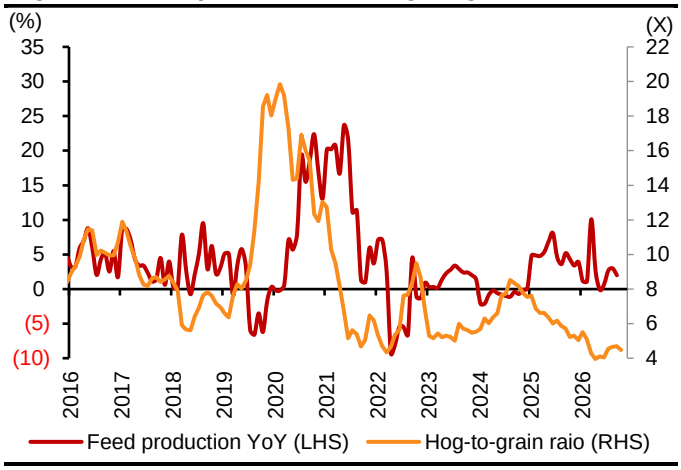
Source: Wind, CMBIGM

Figure 5: Second-hand car price in Shanghai



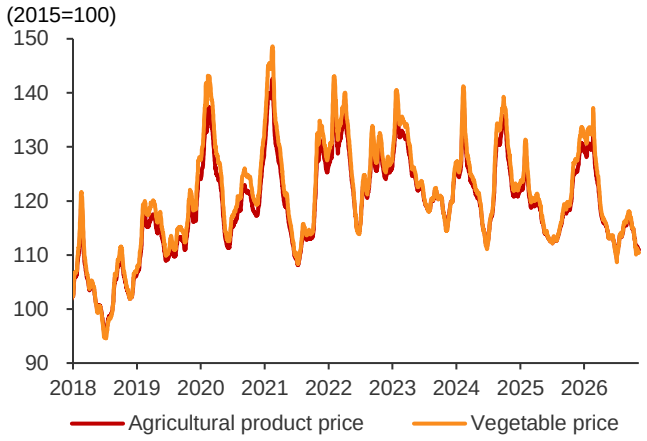
Source: Wind, CMBIGM

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



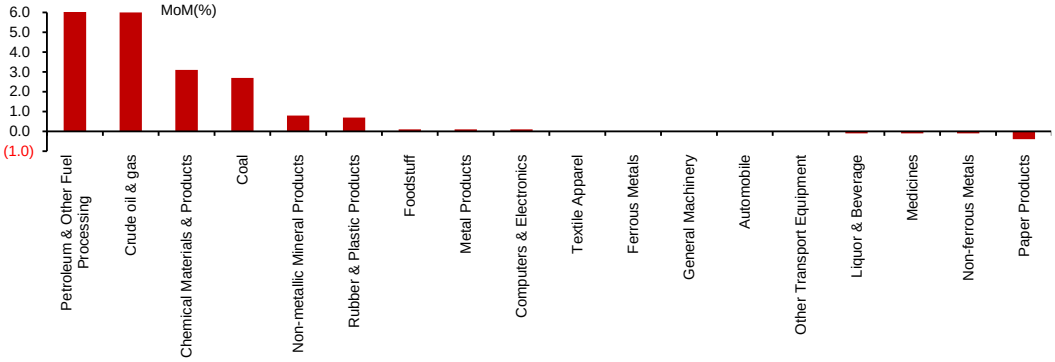
Source: Wind, CMBIGM

Figure 7: Agricultural and vegetable prices



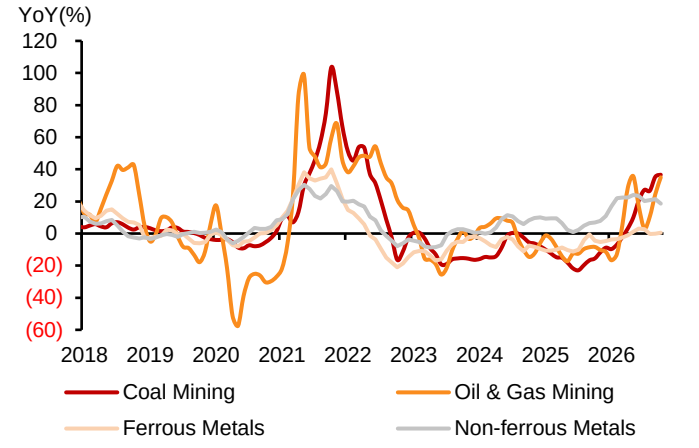
Source: Wind, CMBIGM

Figure 8: MoM changes of China PPI



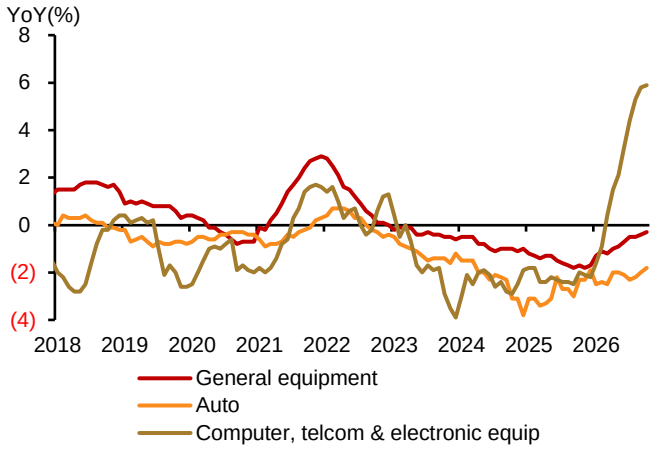
Source: Wind, CMBIGM

Figure 9: China PPI in energy & metals



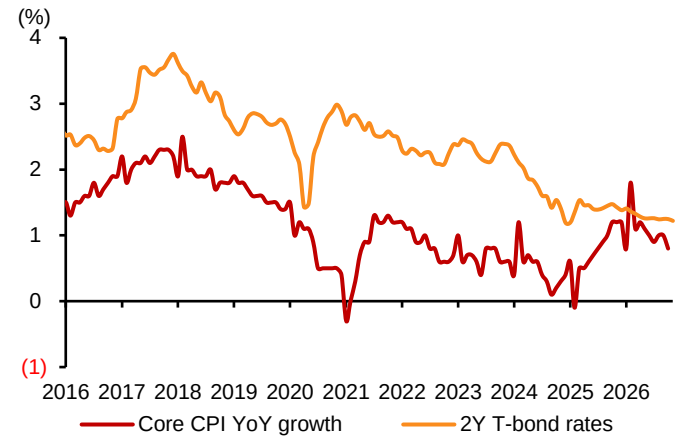
Source: Wind, CMBIGM

Figure 10: China PPI in equipment



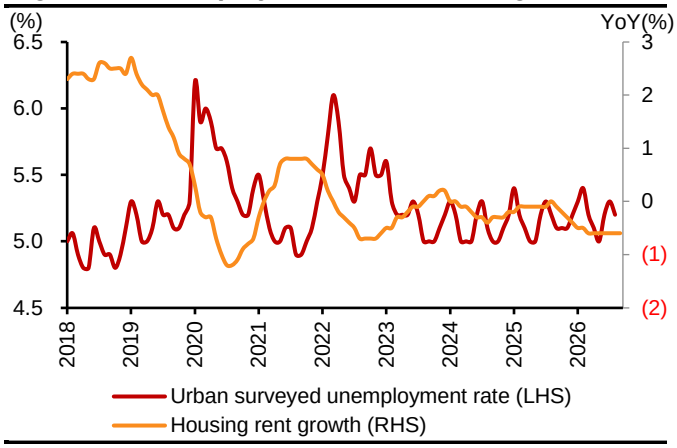
Source: Wind, CMBIGM

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



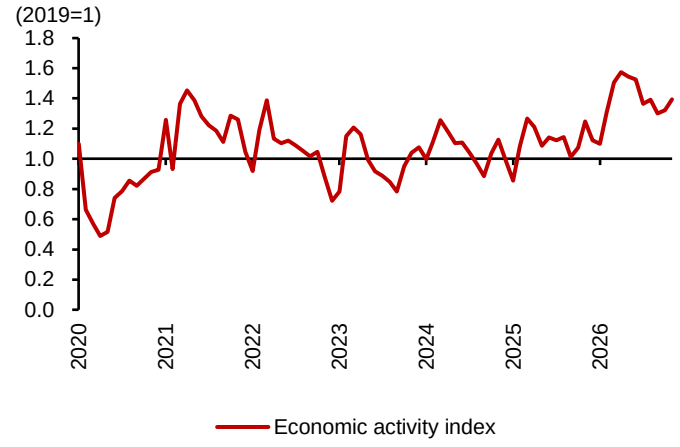
Source: Wind, CMBIGM

Figure 12: Unemployment rate and rent growth



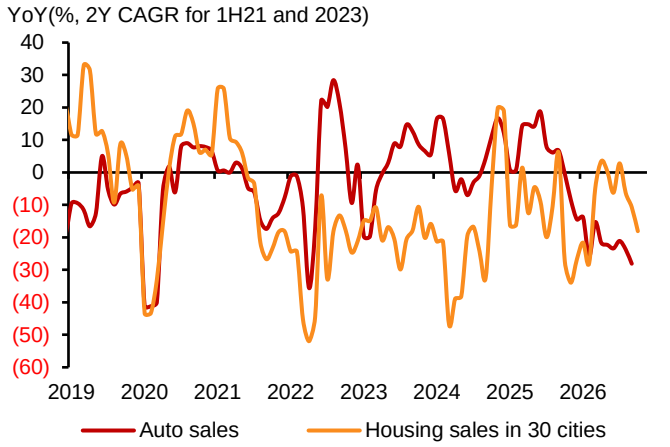
Source: Wind, CMBIGM estimates

Figure 13: China Economic Activity Index



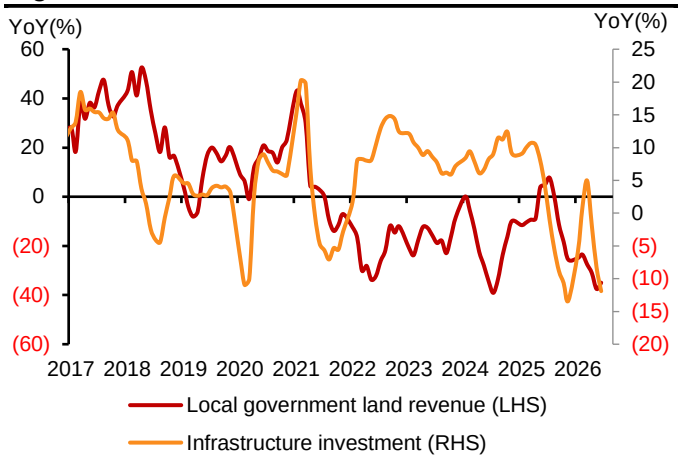
Source: Wind, CMBIGM

Figure 14: China auto & housing sales



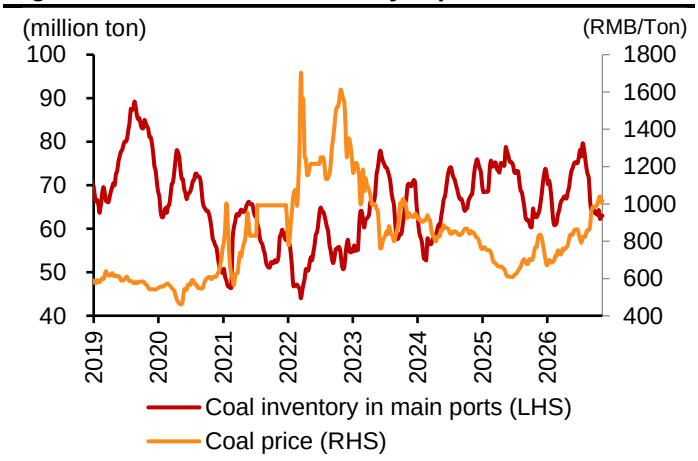
Source: Bloomberg, CMBIGM

Figure 15: Infrastructure investment in China



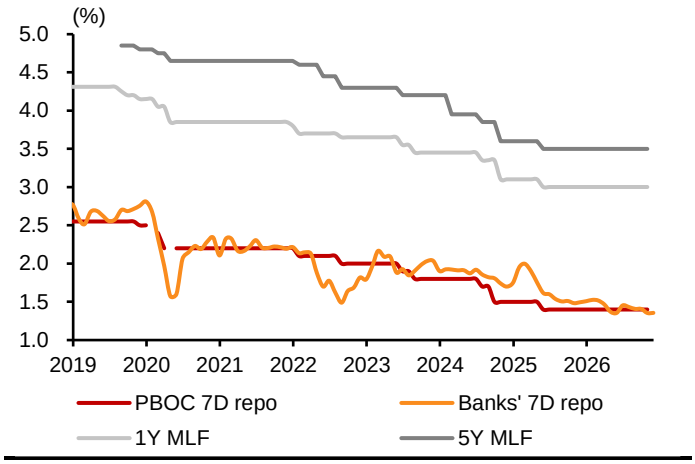
Source: Bloomberg, CMBIGM

Figure 16: China coal inventory & price



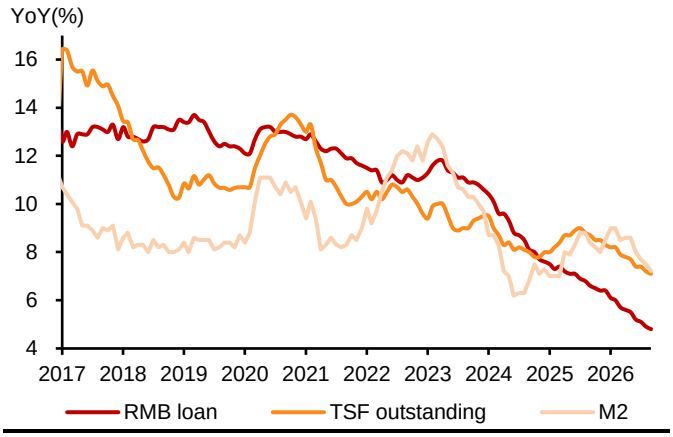
Source: Wind, CMBIGM

Figure 17: PBOC policy rates & liquidity condition



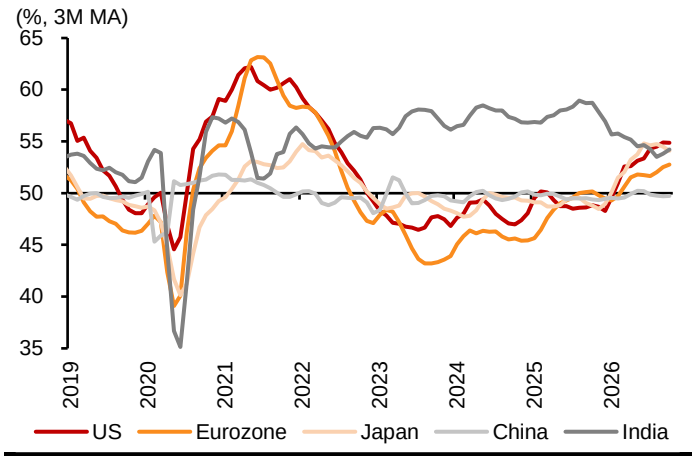
Source: Bloomberg, CMBIGM

Figure 18: China credit growth



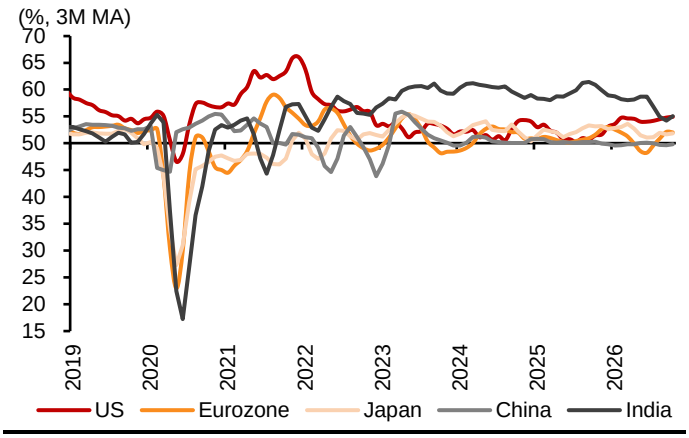
Source: Wind, CMBIGM

Figure 19: Manufacturing PMI of major economies



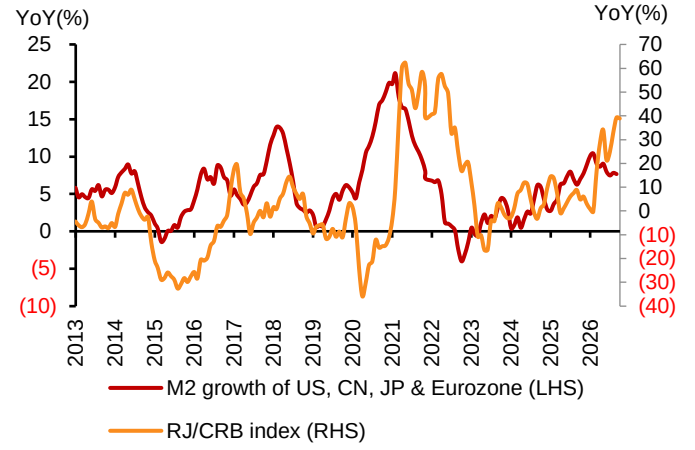
Source: Bloomberg, CMBIGM

Figure 20: Service PMI of major economies



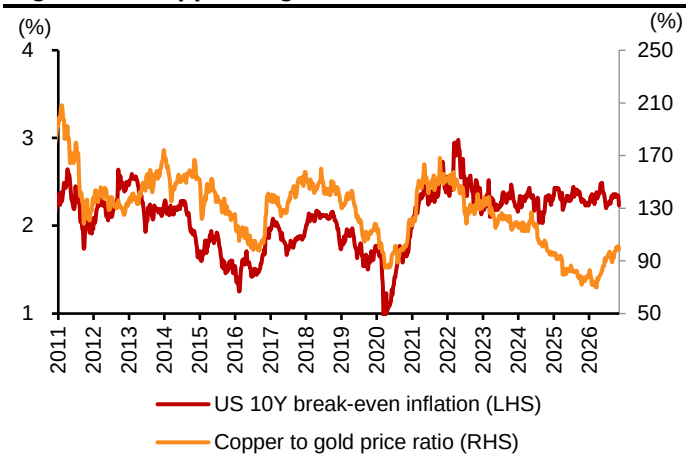
Source: Wind, CMBIGM

Figure 21: M2 growth & commodity inflation



Source: Bloomberg, CMBIGM

Figure 22: Copper-to-gold ratio



Source: Wind, CMBIGM

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