

# China Economy

## Deflation pressure remains

Sep CPI notably weakened due to the moderation of food price and sharp decrease of energy price. Core CPI growth is approaching a historic low as an indication of subdued consumer demand and oversupply pressure. Service price further declined while durable goods remained soft. PPI further plunged dragged by midstream and upstream industries especially energy products. The recent policy moves indicate China's policy shift from conservative easing to strong loosening as the policymakers focus on stabilizing the property market, boosting the stock market, rescuing local fiscal system and strengthening the banking system. However, the consumption stimulus policy is still limited. The policy focus needs to gradually shift to boosting consumption and defying deflation. To revive and reflate the economy, additional policies are needed, including fiscal transfers to households, excess capacity reduction and market-oriented reforms. We expect deflation pressure might last into next year. We estimate China's CPI and PPI growth rates may rise from 0.2% and -3% in 2023 to 0.5% and -2% in 2024 and 1.2% and 1% in 2025.

■ **CPI came in short of expectation as deflation pressure persisted.** CPI YoY growth dropped to 0.4% in Sep from 0.6% in Aug, below market expectation of 0.7%. In sequential terms, CPI notably decreased to 0% from 0.4% in Aug, indicating the intensifying deflation pressure. Food price moderated to 0.8% MoM after notably surging 3.4% in Aug as the shortage of supply due to extreme weather eased. Vegetable and meat price slowed down to 4.3% and 0.4% MoM after rising 18.1% and 3.6% in Aug. Pork prices notably moderated to 0.4% MoM growth in Sep compared to 7.3% in Aug while seafood dropped by 0.5% as the start of the fishing season has increased supply. According to high-frequency data, price of agricultural products and vegetables continued to slow down in early Oct, while pork wholesale price MoM has declined for two consecutive months. Vehicle fuel price further dropped from -2.7% YoY to -7.6% while its MoM growth dipped 2.8% in Sep after declining 2.9%, due to falling crude oil price.

■ **Core CPI growth is approaching a historic low due to subdued demand and oversupply.** Core inflation has dropped to its lowest level in history at 0.1%, except for Jan-Feb 2021. MoM growth dropped 0.1% in Sep after decreasing 0.2% in Aug. Service price continued to decline by 0.3% after dropping 0.1% in Aug. Tourism price notably dropped 6.3% while telecom, express, medical and home service remained unchanged. Housing rent dropped 0.1%, indicating the weak employment conditions while education service rose by 0.9% due to back-to-school season but still weaker than historic seasonality. Durable goods prices marginally rebounded but remained subdued as vehicle price bounced up to -0.1% in Sep following a 0.3% dip. The decline in telecom and home equipment price narrowed to 0.6% and 0.2% MoM after plunging 0.8% and 0.7% in Aug. Discretionary goods including clothing and footwear saw 0.8% and 0.6% MoM increase after dropping 0.2% and 0.3%. Looking forward, CPI may remain in the low range under 1% as food and energy prices continue to drop. Core CPI growth may pick up in Oct due to national holidays but may remain restrained in medium term due to lethargic consumer demand amid weak employment conditions and oversupplying in consumer goods.

■ **PPI markedly plunged dragged by midstream and upstream industries.** YoY contraction of PPI dipped to -2.8% in Sep after dropping 1.8% in Aug, slightly below market expectation at -2.5%. The MoM growth declined by 0.6% in Sep compared to -0.7% drop in Aug. For mining industries, PPI of coal mining, oil & gas, and ferrous metals notably dropped to -2.6%, -10.1% and -11.1% from -0.1%, -3.3% and -8% YoY in Aug, while non-ferrous

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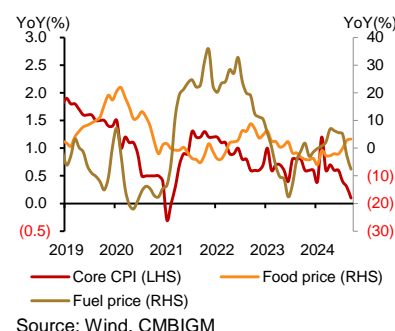
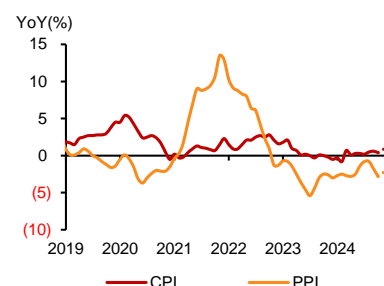
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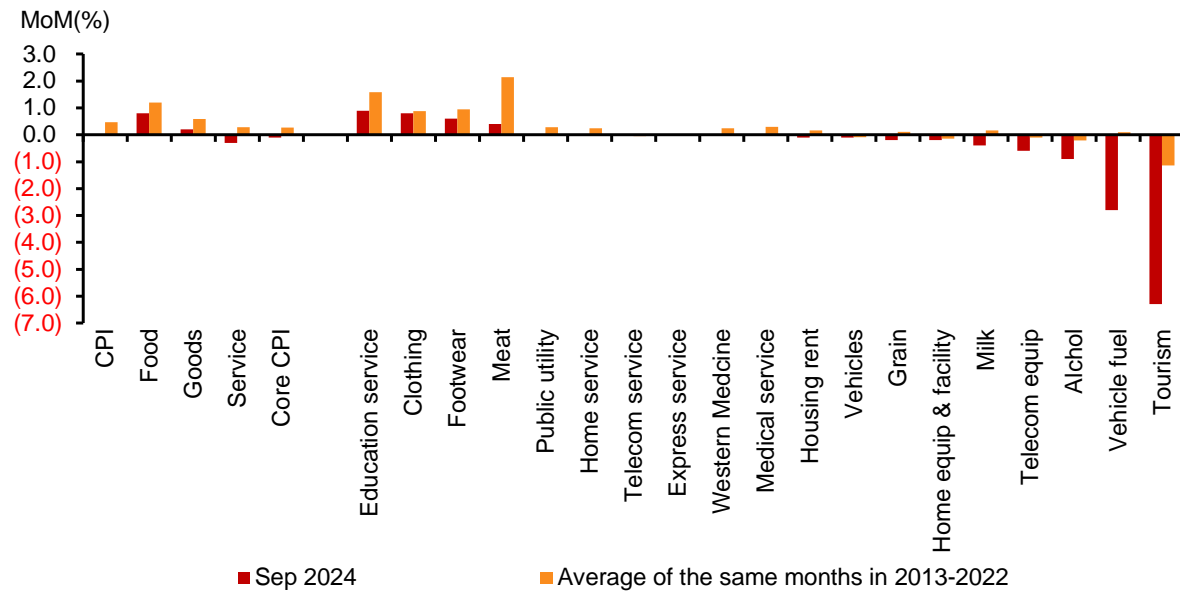
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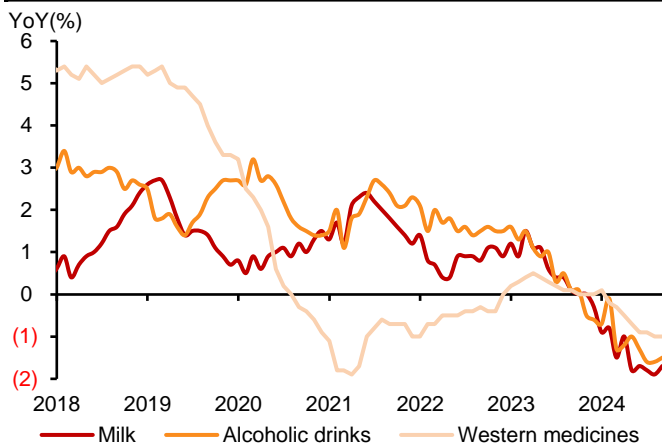


metals moderated to 5.9% from 7.6%. For mid-stream industries, PPI in intermediate goods such as ferrous metals, chemical products, non-metallic mineral products and metal products dropped 3.3%, 1%, 0.8% and 0.6% MoM respectively. For final goods, auto manufacturing saw another 0.2% MoM decline while PCs dipped by 0.1%. As we expected, PPI has widened its YoY decline and may continue to do so in the next few months before gradually improving again from late 2024. CRB commodities index has rebounded since mid-Sep, as major economies have all entered an easing cycle.

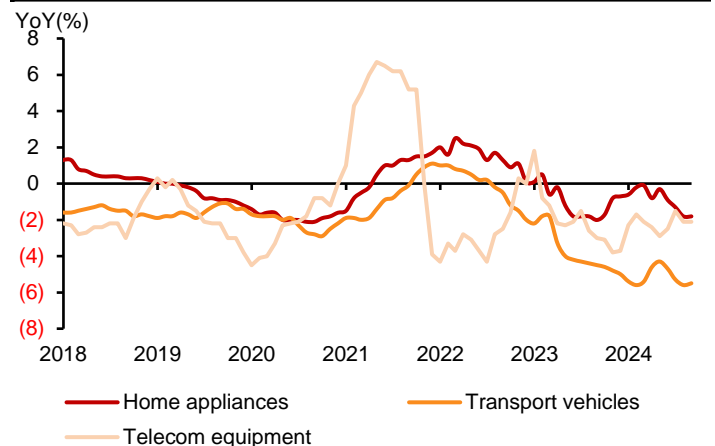
- **China needs to shift its policy focus to boosting consumption and defying deflation.** The recent policy moves indicate China's policy is shifting from conservative easing to strong loosening. The policymakers focus on stabilizing the property market, boosting the stock market, relieving local fiscal distress and strengthening the banking system. To revive and reflate the economy, China needs to gradually shift its policy focus to boosting consumption and defying deflation. Additional policies are needed, including large-scale fiscal transfers to households to boost consumer demand, effective excess capacity reduction to relieve deflation and market-oriented reforms to restore animal spirit in the economy.

**Figure 1: MoM Changes of China CPI in Sep**

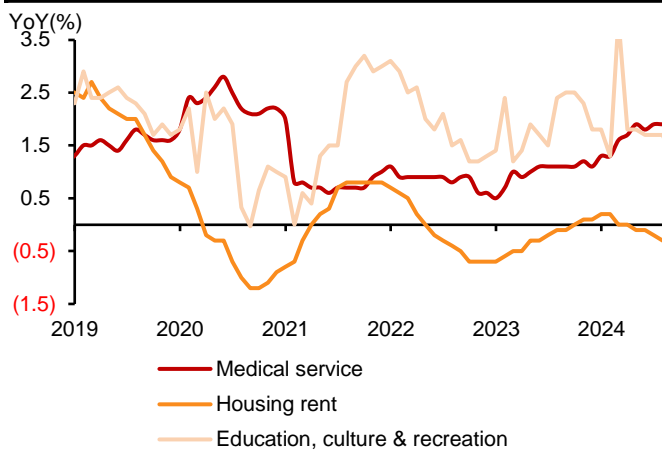
Source: Wind, CMBIGM

**Figure 2: China CPI Growth in Staples**

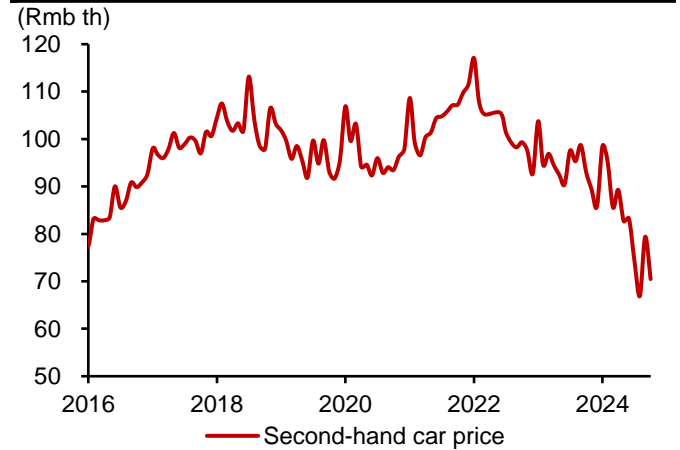
Source: Wind, CMBIGM

**Figure 3: China CPI Growth in Durables**

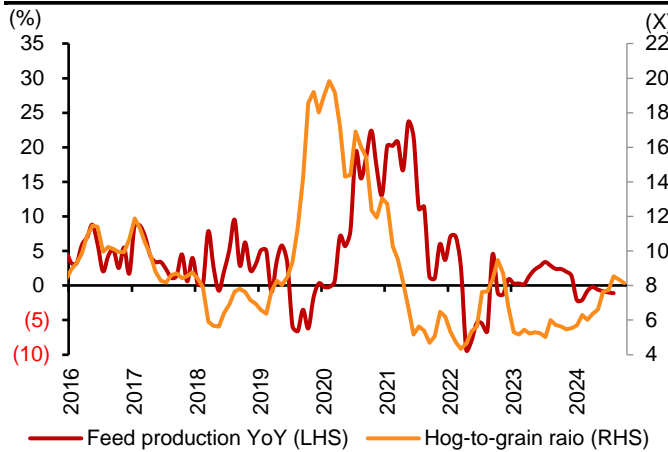
Source: Wind, CMBIGM

**Figure 4: China CPI Growth in Services**

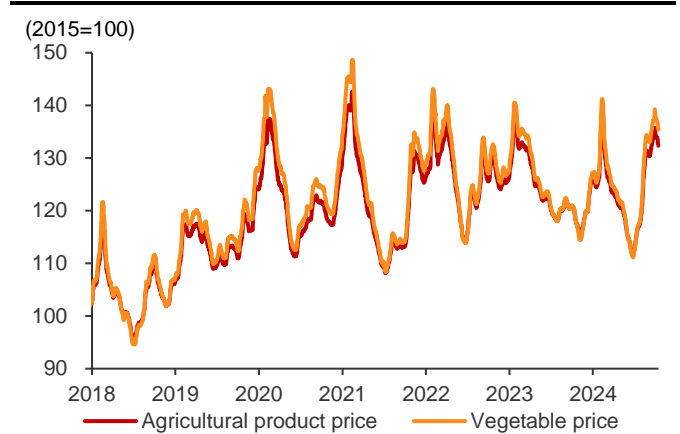
Source: Wind, CMBIGM

**Figure 5: Second-hand Car Price in Shanghai**

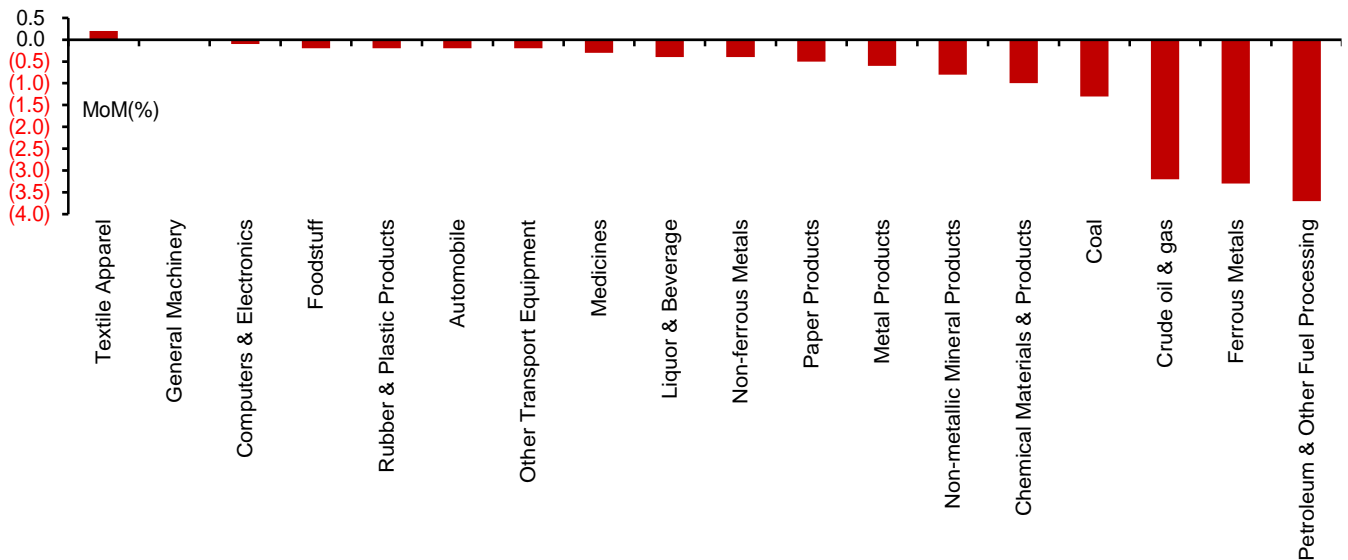
Source: Wind, CMBIGM

**Figure 6: Feed Production & Hog-to-Grain Ratio**

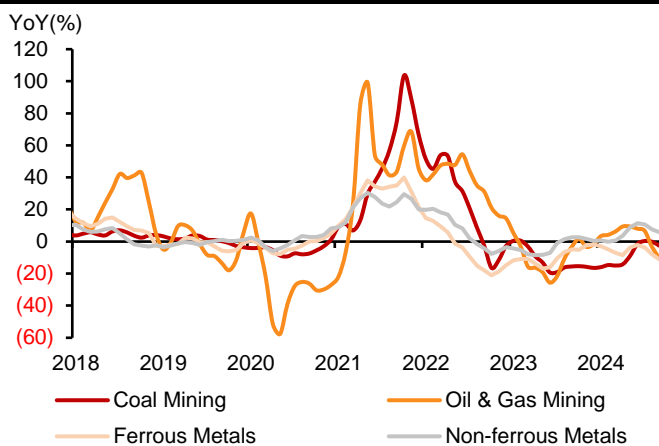
Source: Wind, CMBIGM

**Figure 7: Agricultural and Vegetable Price**

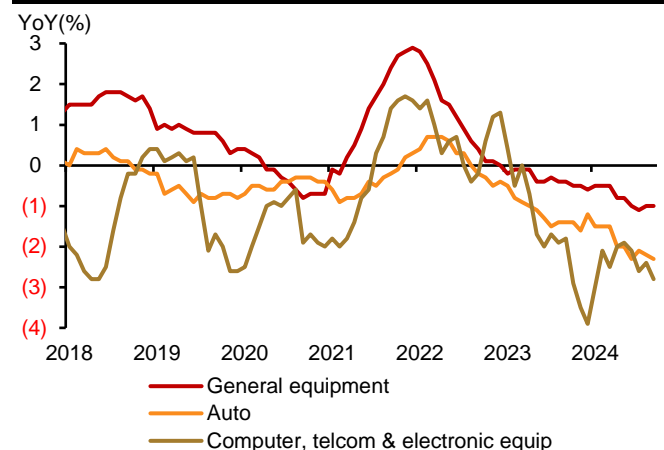
Source: Wind, CMBIGM

**Figure 8: MoM Changes of China PPI in Sep**

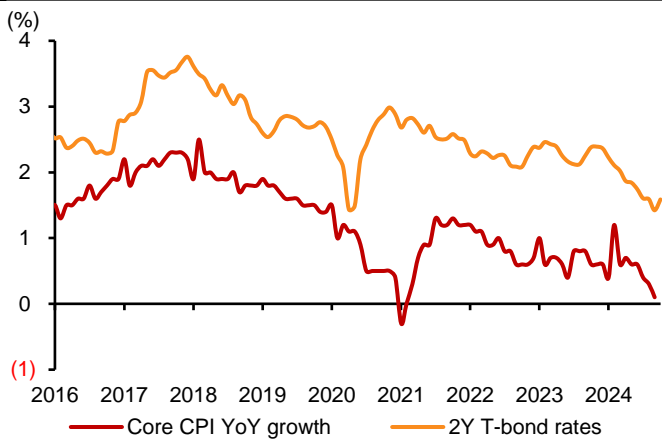
Source: Wind, CMBIGM

**Figure 9: China PPI in Energy & Metals**

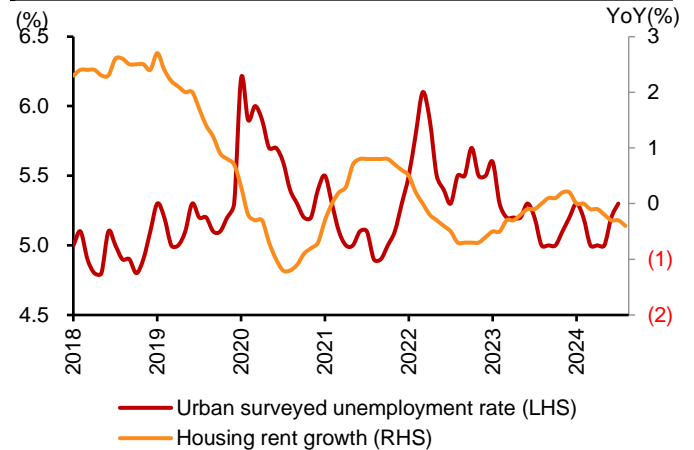
Source: Wind, CMBIGM

**Figure 10: China PPI in Equipment**

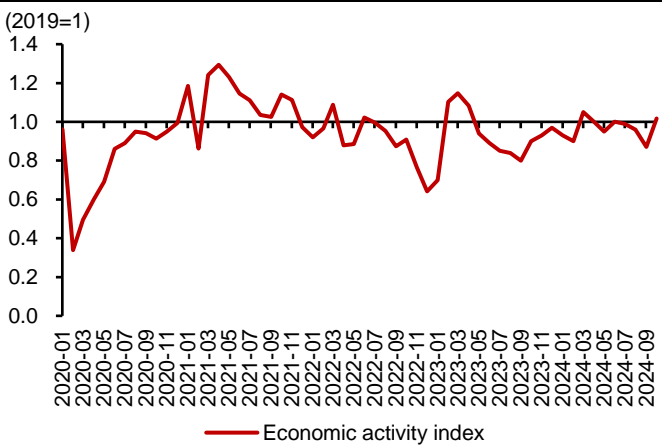
Source: Wind, CMBIGM

**Figure 11: China Core CPI Growth & 2Y T-bond Rates**

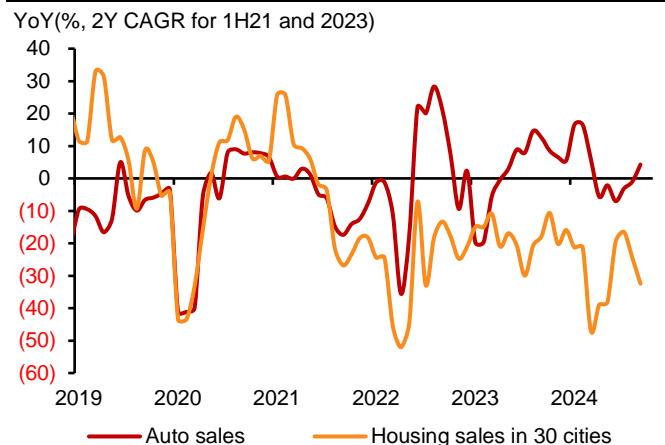
Source: Wind, CMBIGM

**Figure 12: Unemployment rate and rent growth**

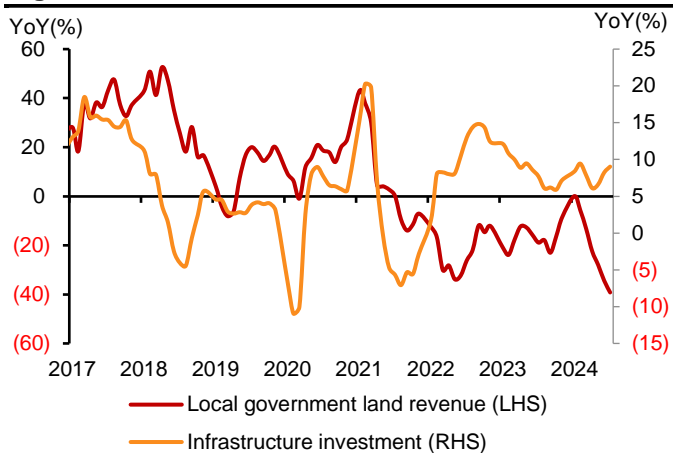
Source: Wind, CMBIGM estimates

**Figure 13: China Economic Activity Index**

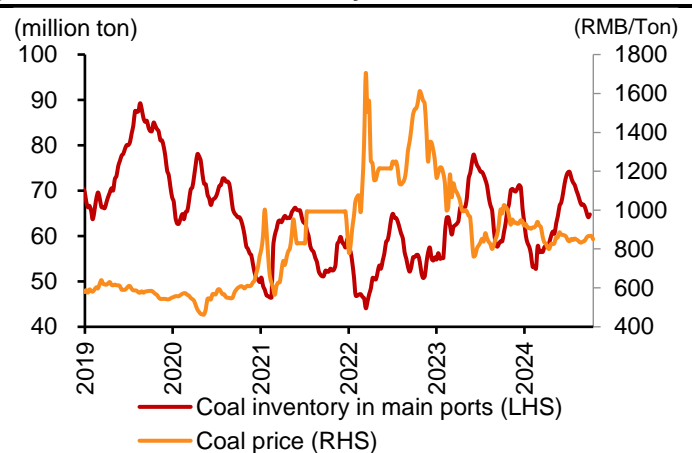
Source: Wind, CMBIGM

**Figure 14: China Auto & Housing Sales**

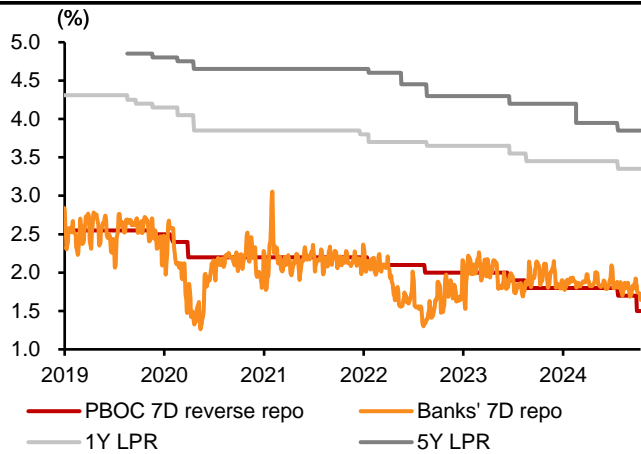
Source: Bloomberg, CMBIGM

**Figure 15: Infrastructure Investment in China**

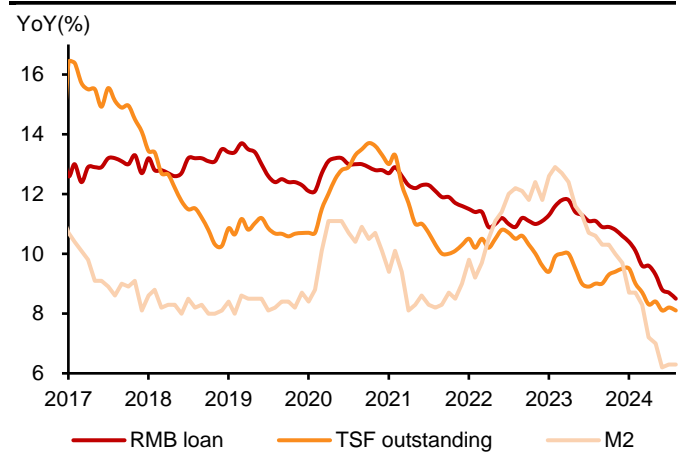
Source: Bloomberg, CMBIGM

**Figure 16: China Coal Inventory & Price**

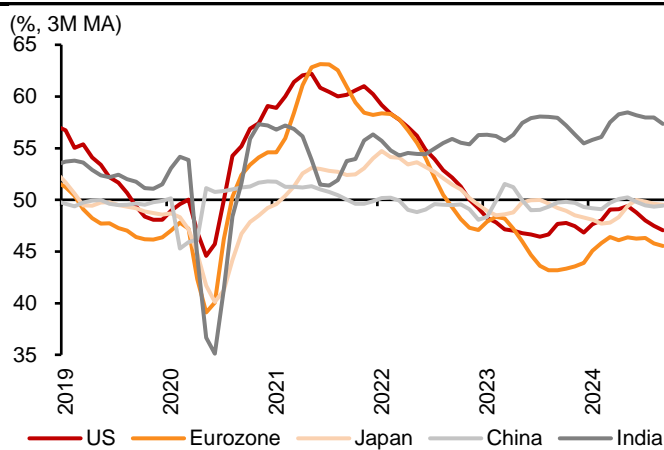
Source: Wind, CMBIGM

**Figure 17: PBOC Policy Rates & Liquidity Condition**

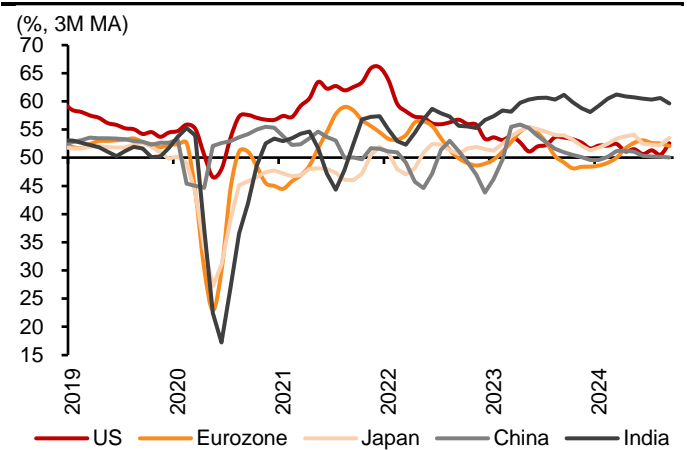
Source: Bloomberg, CMBIGM

**Figure 18: China Credit Growth**

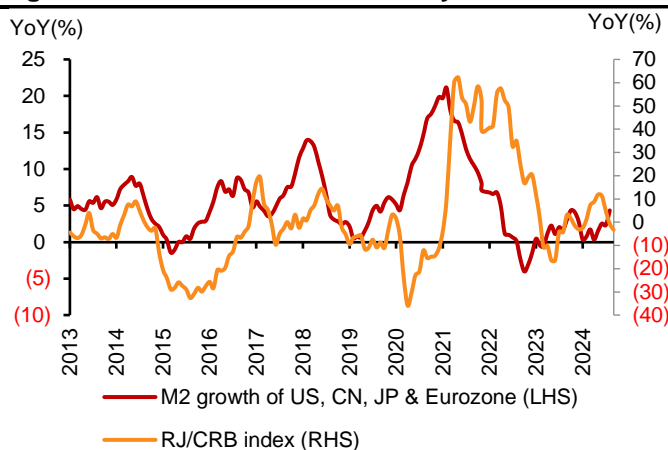
Source: Wind, CMBIGM

**Figure 19: Manufacturing PMI of Major Economies**

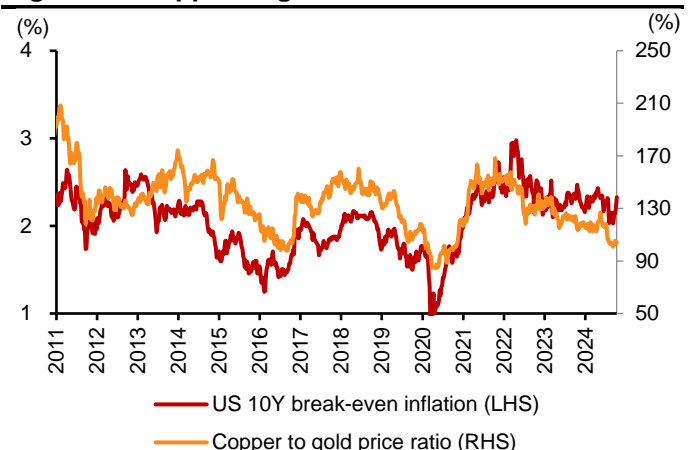
Source: Bloomberg, CMBIGM

**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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