CAPITAL ECONOMICS
凯投宏观

CHINA DATA RESPONSE

Consumer & Producer Prices (May)

Inflation remains low as initial reopening effects begin to fade

- **Producer price deflation deepened further last month to a 87-month low. Consumer price inflation edged up but remained depressed. Core inflation slipped slightly, suggesting that the immediate inflationary impact of reopening was easing last month. We still think a tightening labour market will eventually put some upward pressure on inflation later this year. But it will remain well within policymakers' comfort zone.**
- After falling to its lowest in more than two years in April, CPI inflation rose from 0.1% y/y to 0.2% last month (the Bloomberg median was 0.2% and our forecast was 0.1%). (See Chart 1.) This was driven by a pick-up in food price inflation, which more than offset a slight fall in core inflation, from 0.7% y/y to 0.6%, and a decline in fuel price inflation to a 28-month low. The former reflects slower price rises in travel and other in-person services, which reversed some of their earlier reopening-driven acceleration. (See Chart 2.) **This suggests that the uptick in services inflation caused by the immediate snap back in activity following reopening is fading and has yet to be replaced by more sustained price pressures.**
- Producer price deflation deepened from -3.6% y/y in April to -4.6% last month (Bloomberg: -4.3% and CE: -4.5%). (See Chart 3.) This was partly driven by a higher base for comparison too. But factory-gate prices also dropped by 0.9% in month-on-month terms. The biggest declines were in energy and metal prices, although consumer durable prices dropped back too (see Chart 4). **This is primarily due to weak demand outside of China.**
- We still think a tightening labour market will put upward pressure on services inflation in the coming months. But the government's ceiling of "around 3.0%" for the headline rate is unlikely to be tested and we doubt inflation will become a barrier to increased policy support. Instead, the main constraint facing policymakers has to do with financial risks. We expect the PBOC to ease policy somewhat in the near-term but that, in order to limit the impact on bank margins, it will favour tools such as window guidance and RRR reductions instead of policy rate cuts.

Chart 1: Consumer Prices (% y/y)

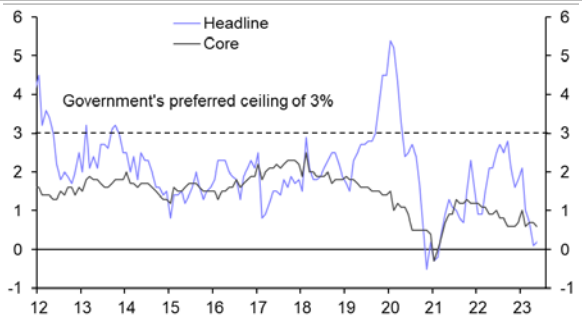


Chart 2. CPI – Tourism Services (% y/y)

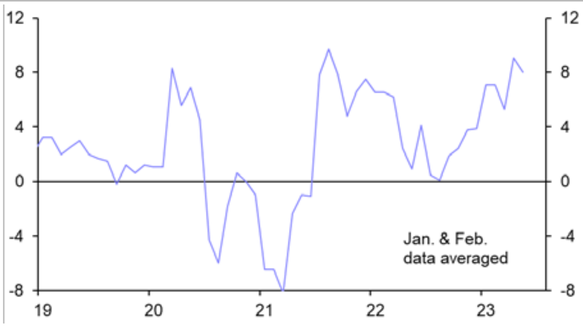


Chart 3: Producer Prices

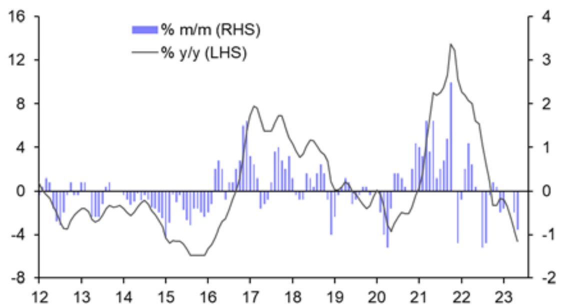
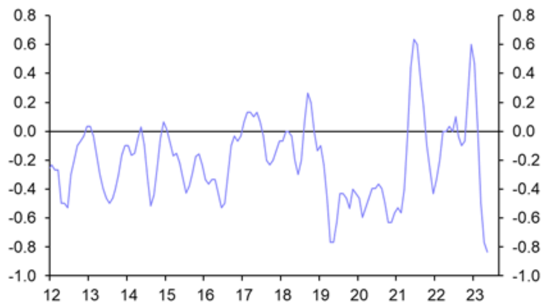


Chart 4. PPI – Durable Consumer Goods (% 3m/3m)



Sources: CEIC, Capital Economics

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