CAPITAL ECONOMICS 凯投宏观

CHINA DATA RESPONSE

Consumer & Producer Prices (Jun.)

Price pressures set to remain subdued this year

- **Producer price deflation deepened further last month to its lowest in more than seven years, and consumer price inflation dropped to a 28-month low of 0%. Core inflation continued to fall as the initial impact of reopening faded. We expect inflation to rise gradually later this year, but the upside will be limited, leaving room for further policy easing.**

- CPI inflation declined from 0.2% y/y in May to 0.0% last month, below expectations (the Bloomberg median and our forecast were 0.2%). (See Chart 1.) Food price inflation picked up, but this was more than offset by a fall in core inflation, from 0.6% y/y to 0.4%, and a decline in fuel price inflation to a 31-month low. The former reflected slower price rises in travel and other in-person services, which reversed some of their earlier acceleration driven by the impact of reopening. (See Chart 2.)

- Producer price deflation deepened from -4.6% y/y in May to -5.4% last month (Bloomberg and CE: -5.0%). (See Chart 3.) This could be attributed, in part, to a higher base for comparison, as global commodity prices were surging a year ago following Russia's invasion of Ukraine. But factory-gate prices also dropped by 0.8% in month-on-month terms. The biggest declines were in energy, metal and chemical prices, with consumer durable prices also retreating (see Chart 4). This is due to weak demand both within and outside China.

- **PPI deflation is likely to ease somewhat in the second half of the year, partly because infrastructure spending should put a floor under commodity prices. And core inflation could rise gradually, as a relatively tight labour market puts greater upward pressure on wages.** Fuel price deflation, a key factor behind subdued headline inflation recently, will probably wane over the coming months. As such, we expect headline inflation to rise to around 1% by the end of this year. But this would still be soft and won't constrain the PBOC's ability to loosen policy further. That said, with credit demand weak, and the currency under pressure, we think the bulk of support will come through fiscal policy. We expect only another 10bp of policy rate cuts this year.

Chart 1: Consumer Prices (% y/y)

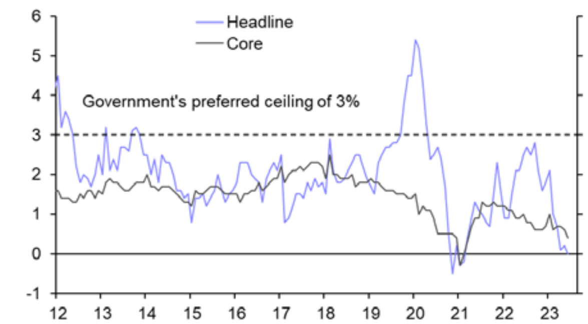


Chart 2. CPI – Tourism Services (% y/y)

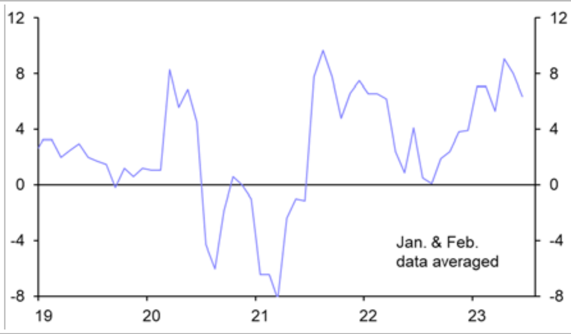


Chart 3: Producer Prices

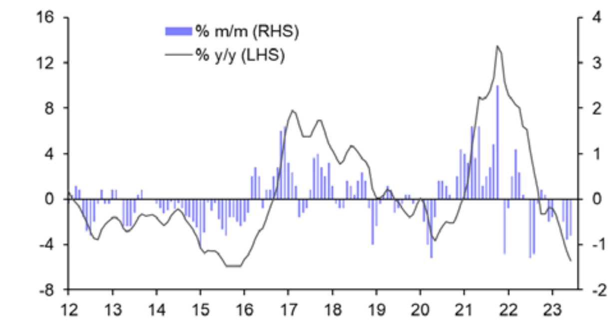
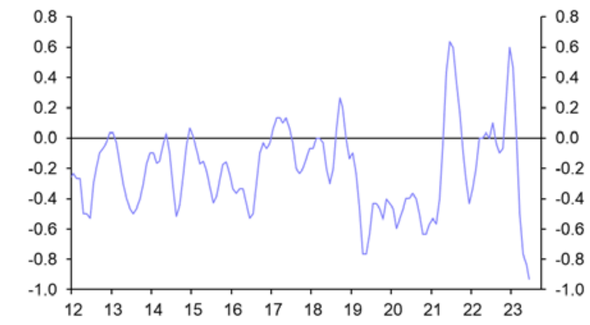


Chart 4. PPI – Durable Consumer Goods (% 3m/3m)



Sources: CEIC, Capital Economics

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