

China: September inflation flirting with disinflation again

September's inflation data remind us that despite some firming in activity indicators recently, China's economic recovery remains challenged, and is perhaps behind recent rumours of a slightly more accommodative approach to central government deficits



Source: Shutterstock

0.0%

September CPI inflation

YoY%

Lower than expected

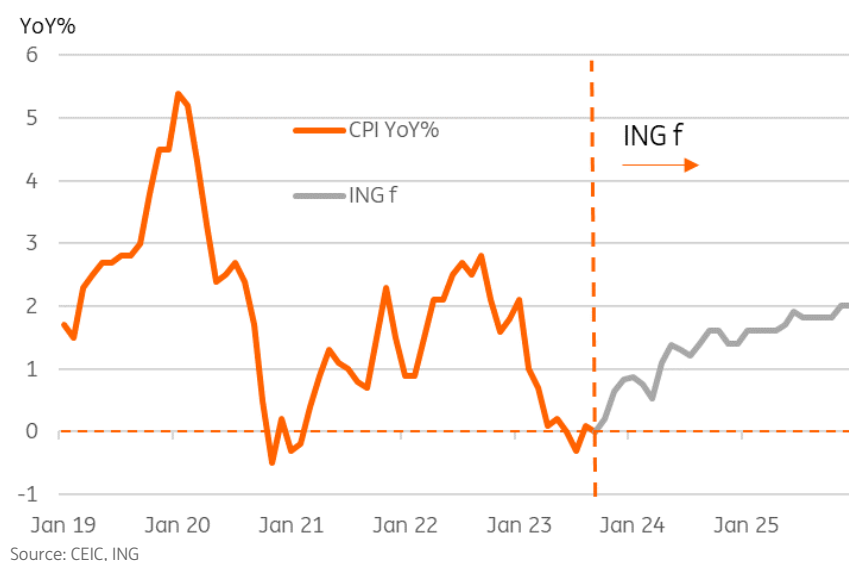
CPI flirts with disinflation again

After a brief spell in negative territory in July, China's August inflation data pulled itself back to a positive setting, though only just (0.1% YoY). We and the market were expecting this slight improvement to continue in September. Instead, the September inflation rate has fallen back to

0% YoY, and according to our calculations, this implies a small (0.1pp) decline in the underlying price level. That itself is quite disappointing because those same calculations showed that in the previous couple of months, most of the decline in inflation was due to the run-off of earlier food price shocks. The underlying run-rate of inflation back then remained encouragingly positive.

One month does not constitute a trend, however, and the base effect story, which we believe will slowly lift Chinese inflation over the coming months is still in play. However, if the underlying run rate is softer even than the conservative figures we are pencilling in, then this may be a much more nuanced improvement.

China CPI inflation (YoY%)



No room for monetary support, so maybe fiscal policy to be loosened?

Even with the sort of improvement we are anticipating, full-year inflation will likely only just push above 1% in 2024, up from our forecast of 0.5% CPI inflation for full-year 2023.

And it's not just CPI inflation where we see weakness. The PPI inflation data released today also undershot expectations, though at -2.5% YoY, they did at least improve on the -3.0% PPI inflation recorded in August. This may presage some slight improvement in industrial profit growth, which was still down 11.7% Ytd YoY% in August.

Next week, we have the 1Y medium-term lending facility rate decision. But with the PBoC engaged in a daily struggle to keep the CNY from depreciating, we think it is extremely unlikely that they will be able to respond to this inflation weakness with lower policy rates.

Instead, in recent days, we have been reading reports that the authorities may be mulling a slightly wider central government deficit to help offset or minimise the pain from the local government financing gap weighing on activity in overleveraged provinces.

There are a couple of points to make about this. Firstly, we don't discount these reports. The economy does need more support than the numerous supply-side measures we have already

seen so far. But equally, the policy intent to deleverage and draw a line under the borrowing excesses of local governments seems firm and appropriate.

Whatever does emerge from Beijing over the coming months, it likely won't be quick enough to make any meaningful difference to 2023, and at best, it should be viewed as a pain management tool for the transition to a less leveraged economy. And that is a multi-year project.

Author

Robert Carnell

Regional Head of Research, Asia-Pacific

robert.carnell@asia.ing.com

Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. ("ING") solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies)*. The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit www.ing.com.