

Softer-than-expected June inflation continues to bolster the case for easing in China

China's CPI inflation slowed to a 3-month low of 0.2% YoY in June on softer-than-expected non-pork food prices but remained in positive territory for the fifth consecutive month



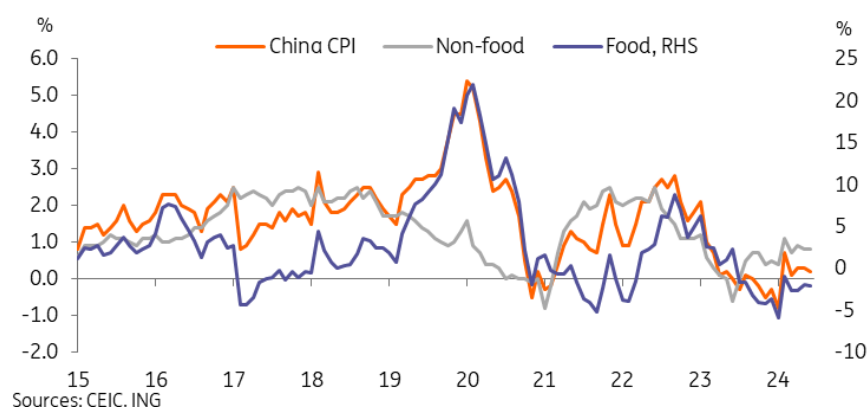
Source: Shutterstock

0.2% YoY

China's June CPI inflation

Lower than expected

China's inflation remained barely in positive territory in June



Inflationary pressures remained subdued

China's June CPI inflation edged down to 0.2% YoY, down slightly from 0.3% YoY, and coming in weaker than forecasts for a slight uptick to 0.4% YoY. Inflation has been very flat in the last four months, fluctuating between 0.1-0.3% YoY. In month-on-month terms, June's CPI inflation dropped to -0.2%, and inflation has now seen two consecutive months of decline.

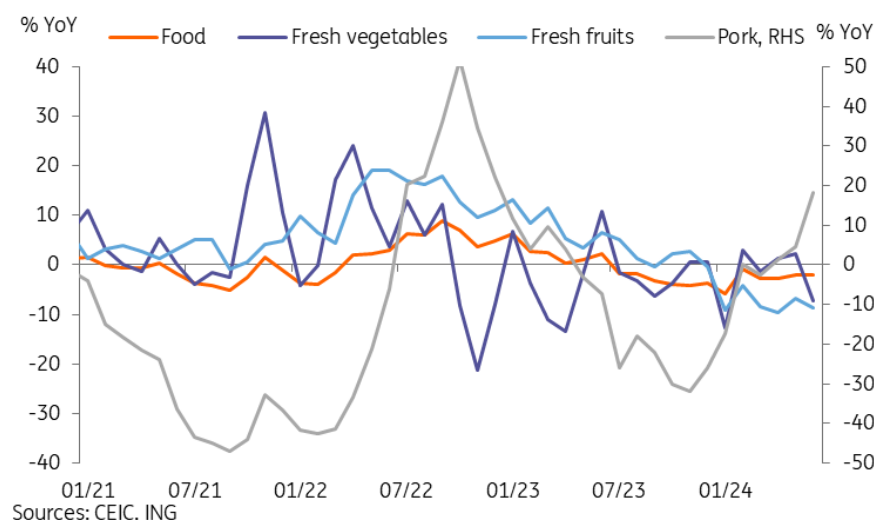
This month's slightly softer read came on the back of several factors:

1. Food prices (-2.1% YoY) saw a sharper-than-expected decline in June. This was due to a larger drag from fresh vegetables (-7.3%), fresh fruits (-8.7%), as well as beef (-13.4%) and mutton (-7.1%), which offset a strong recovery of pork prices (18.1%). The pork cycle is largely proceeding as expected, but the drag from other food prices has lingered.
2. Non-food inflation (0.8% YoY) continued to see drags from several categories. Vehicles (-5.3%), household appliances (-1.3%), and communications devices (-1.5%) continued to drag inflation, while rents (-0.2%) fell further into negative territory as well.

Weak consumer confidence continues to drive consumption in the direction of seeking better value-for-money purchases, and competition in the EV sector continues to drive prices down, suppressing overall inflation.

PPI inflation showed a slightly more favourable read, with a smaller contraction of -0.8% YoY, up from -1.4% YoY in May, and reaching a 17-month high. Producer prices have remained in deflation since September 2022, but should exit deflation in the second half of the year if the current trajectory holds.

Food prices continued to be suppressed despite a strong uptick of pork prices



Inflation may see a moderate increase in the second half of the year, conditions remain ripe for more monetary easing

Through the first half of the year, China's CPI inflation is barely positive at 0.1% YoY, as the -2.7% YoY drag from food prices in the year to date weighed heavily on the headline level. While non-food inflation has fared relatively better at 0.8% YoY through the first half of the year, inflation remains well short of the typical 2% inflation target.

Moving forward, we expect inflation to trend gradually higher in the second half of the year. Recent data has indicated this process could be a little slower than previously anticipated.

Soft inflation and weak credit data are presenting a compelling case for further monetary policy easing from the PBOC in the coming months. The PBOC may prefer to first utilise another required reserve ratio (RRR) cut, but the February RRR cut showed this policy tool is seeing diminishing returns and effectiveness. We continue to see real interest rates as too high for the current state of the economy and believe the economy would benefit more from rate cuts. While we believe the PBOC has likely held back on cuts in order to avoid adding to RMB depreciation pressure, we expect to see 1-2 rate cuts in the second half of the year, with a stronger case for cuts if the Fed begins its rate cut cycle.

Author

Lynn Song

Chief Economist, Greater China

lynn.song@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.