



China Sourcing Update

August 10, 2018

Major Price Indicators

1. CPI growth accelerates in July

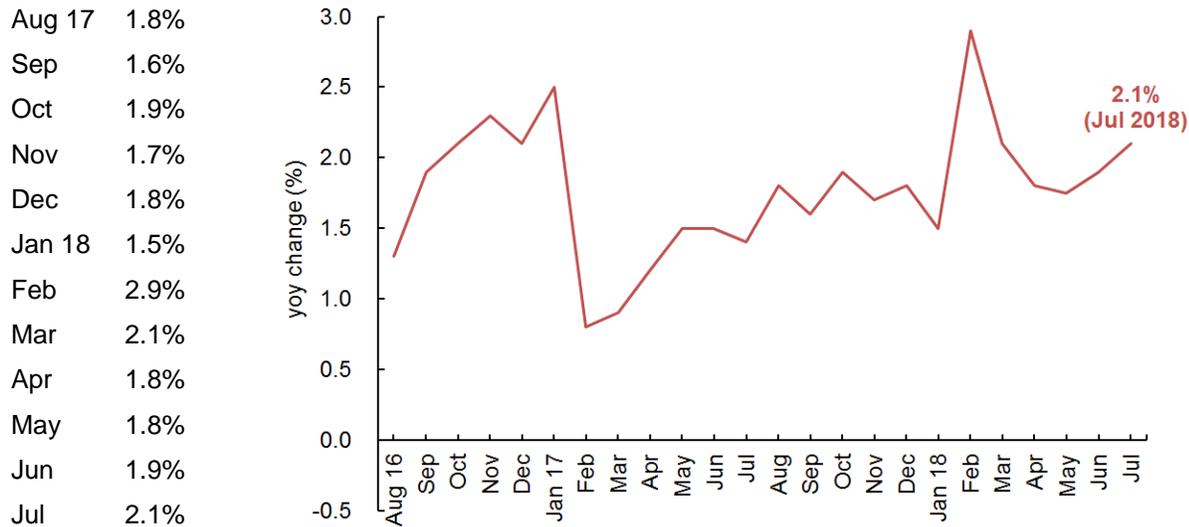
The year-on-year growth rate of China's consumer price index (CPI)¹ went up from 1.9% in June to 2.1% in July, which was above market expectations (*see exhibits 1 & 2*).

China's CPI growth picked up in July as both food and non-food inflation accelerated. The year-on-year growth in the food component in the CPI increased from 0.3% in June to 0.5% in July, thanks to a smaller year-on-year decline in pork prices; while the year-on-year growth in the non-food component increased from 2.2% in June to 2.4% in July, due partly to higher fuel prices.

On 6 July, China's 25% retaliatory tariffs on US\$34 billion worth of US imports came into effect. Since the targeted products are mostly agricultural products (including soybeans, which are mostly used as a livestock feed) and aquatic products, the tariffs will likely push up food prices, in particular pork prices, in China. Thus, we expect that China's food inflation and the CPI growth in turn will trend slightly upward in the coming months.

¹ The CPI, compiled by the National Bureau of Statistics (NBS) of China, measures the price of a basket of goods and services purchased by a typical household. It is noteworthy that the NBS has changed the weights assigned to the various components in the CPI basket, effective from January 2016. The weight of the food component, for example, has been reduced by 3.2 ppt; the weight of the housing component has been increased by 2.2 ppt; and the weights of other components have been adjusted by around or less than 1 ppt. The impact of the re-weighting on the CPI growth was limited, according to the NBS.

Exhibit 1: China's CPI growth, August 2016 to July 2018



Source: National Bureau of Statistics, PRC

Exhibit 2: China's CPI growth by commodity, February to July 2018²

yoy growth (%)

	Feb 18	Mar	Apr	May	Jun	Jul
Clothing	1.1	1.1	1.1	1.1	1.1	1.2
Household articles and services	1.8	1.6	1.5	1.5	1.5	1.6
Education, culture and recreation	3.7	2.2	2.0	1.9	1.8	2.3

Source: National Bureau of Statistics, PRC

2. Ex-factory prices of industrial products go up in July

The year-on-year growth in China's producer price index of industrial products (PPI) edged down from 4.7% in June to 4.6% in July (see exhibits 3 & 4).

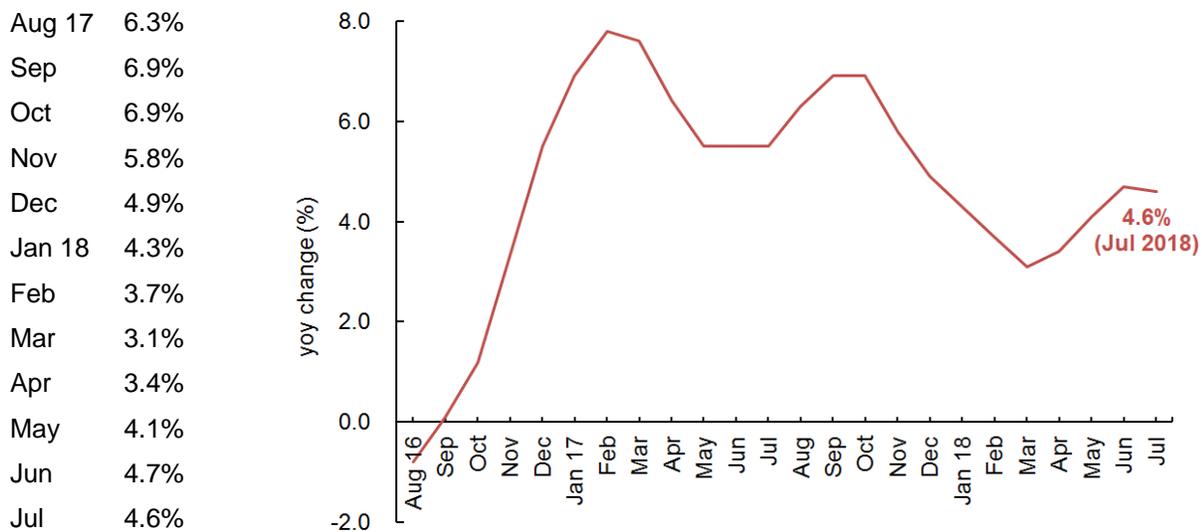
On a month-on-month basis, the PPI climbed by 0.1% in July, posting month-on-month rise for three consecutive months. The rise in the PPI in the month was caused mainly by an increase in the ex-factory prices in the 'manufacture of computer, communication

² Starting from January 2016, the old category of 'household facilities, articles and maintenance services' has been re-categorized into a new category called 'household articles and services' and the category of 'other articles and services'. The old category of 'recreation, education, culture articles and services' has been re-categorized into a new category called 'education, culture and recreation' and the category of 'other articles and services'.

equipment and other electronic equipment’, ‘mining and washing of coal’ and ‘extraction of petroleum and natural gas’ industries.

In our view, China’s tariffs imposed on US\$50 billion worth of US imports³ and the recent depreciation of the Chinese yuan are likely to raise the import prices of materials and intermediate goods, which could put slight upward pressures on producer price inflation. That being said, we expect the year-on-year growth in the PPI to fall sharply in the coming months till year-end, due partly to a higher base for comparison in the same period last year.

Exhibit 3: China’s PPI growth, August 2016 to July 2018



Source: National Bureau of Statistics, PRC

Exhibit 4: China’s PPI growth by selected industry, February to July 2018

	yoy growth (%)					
	Feb 18	Mar	Apr	May	Jun	Jul
Textile	1.7	1.7	1.7	1.9	2.1	2.3
Textile wearing apparel and ornament	0.7	0.4	0.5	0.6	0.6	1.1
Processing of timbers, manufacture of wood, bamboo, rattan, palm, and straw products	1.2	1.2	1.6	1.7	1.9	2.0

Source: National Bureau of Statistics, PRC

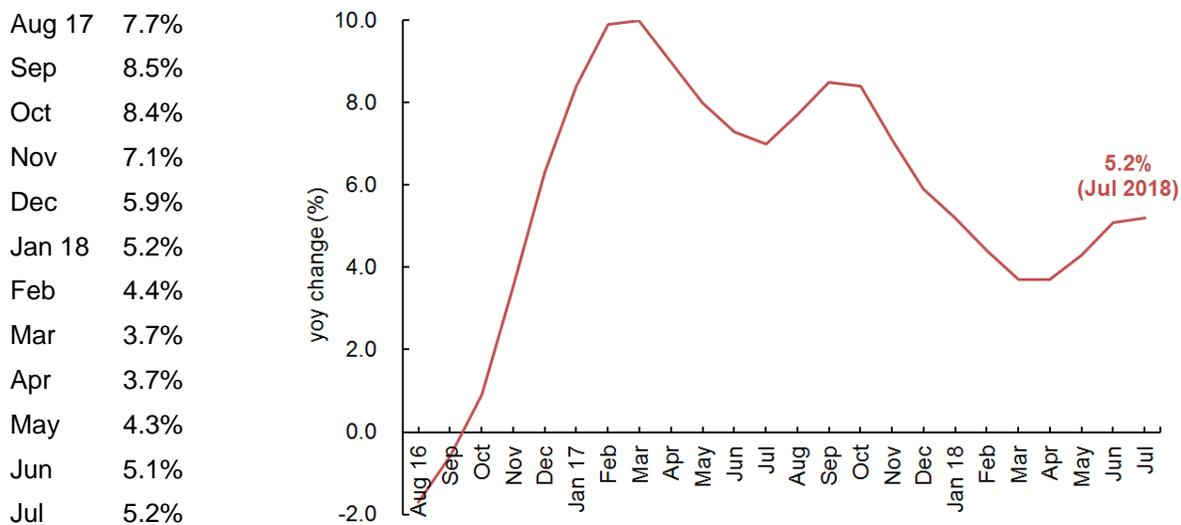
³ Of which, US\$34 billion kicked in on 6 July, and the remaining US\$16 billion will take effect on 23 August.

3. Domestic prices of production inputs rise in July

The year-on-year growth rate of the purchaser price index of industrial products inched up from 5.1% in June to 5.2% in July (see exhibits 5 & 6). On a month-on-month basis, the purchaser price index increased by 0.1% in July, a smaller rise than the 0.4% growth recorded in the previous month.

In our view, the retaliatory tariffs levied on US\$50 billion worth of US goods by China⁴ and the Chinese yuan's recent weakness are likely to lead to a rise in the prices of imported production inputs, which could drive up purchaser price inflation. That being said, the year-on-year growth in the purchaser price index is likely to decline markedly in the rest of the year, due mainly to a higher comparison base in the same period last year.

Exhibit 5: Growth of China's purchaser price index of industrial products, August 2016 to July 2018



Source: National Bureau of Statistics, PRC

⁴ Of which, US\$34 billion kicked in on 6 July, and the remaining US\$16 billion will take effect on 23 August.

**Exhibit 6: China's purchaser price index of industrial products
by selected commodity, February to July 2018**

yoy growth (%)

	Feb 18	Mar	Apr	May	Jun	Jul
Fuel and power	6.0	4.9	4.6	5.5	8.1	9.9
Non-ferrous metal materials and wires	8.3	6.8	6.4	7.6	7.9	5.6
Chemical raw materials	4.3	3.4	4.2	5.3	5.8	5.7
Wood and pulp	6.4	6.5	7.0	7.8	7.4	7.1
Textile raw materials	1.7	1.7	1.7	1.7	2.1	2.4

Source: National Bureau of Statistics, PRC

(i) Purchaser price index of fuel and power

The purchaser price index of fuel and power increased at a faster pace, by 9.9% yoy, in July, after rising by 8.1% yoy in June (see exhibit 6).

(ii) Purchaser price index of non-ferrous metal materials and wires

The year-on-year growth rate of the purchaser price index of non-ferrous metal materials and wires plunged to 5.6% in July from 7.9% in the previous month (see exhibit 6).

(iii) Purchaser price index of chemical raw materials

The year-on-year growth rate of the purchaser price index of chemical raw materials registered 5.7% in July, down from 5.8% in June (see exhibit 6).

(iv) Purchaser price index of wood and pulp

The year-on-year growth rate of the purchaser price index of wood and pulp eased to 7.1% in July from 7.4% in the previous month (see exhibit 6).

(v) Purchaser price index of textile raw materials

The purchaser price index of textile raw materials gained 2.4% yoy in July, compared with the 2.1% yoy growth in June (see exhibit 6).

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