



China Sourcing Update

July 22, 2020

Major Price Indicators

Key indicators

- CPI growth rebounds to 2.5% yoy in June as rising food prices push up consumer inflation.
- Factory gate deflation eases as the year-on-year growth in PPI improved to minus 3.0% in June.
- Year-on-year growth rate of the purchaser price index of industrial products improved to minus 4.4% in June, showing moderation in China's upstream deflation.

Our forecasts

- We expect that China's CPI yoy growth will continue to go up in July. A projected rise in food inflation, lifted by the recent floods in southern China, will likely outweigh a decline in non-food inflation caused by a weak domestic demand in the month. CPI yoy growth will fall afterwards and reach near-zero levels by year end amid a sluggish domestic consumption and a high comparison base last year.
- PPI will continue to rise on a month-on-month basis, and the year-on-year growth will rebound further in the coming months, given an improving industrial demand and the rebound in global commodity prices.
- Both the year-on-year growth and month-on-month growth in input prices will continue to pick up in the coming months, as the demand for production inputs is likely to improve further with domestic industrial production now back to normal.



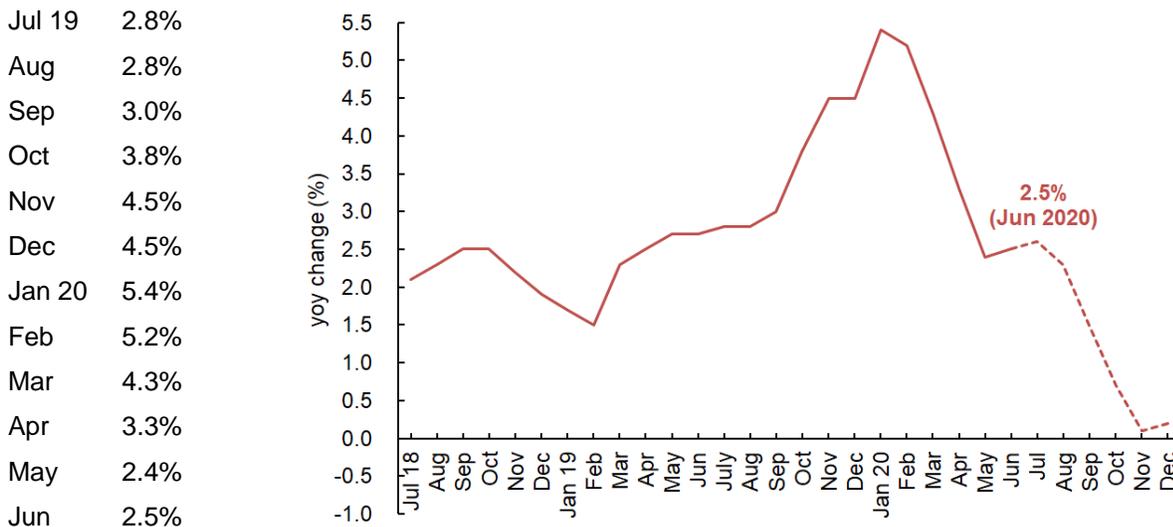
1. CPI growth rebounds to 2.5% in June

The year-on-year growth rate of China's consumer price index (CPI)¹ picked up from 2.4% in May to 2.5% in June, ending four consecutive months of decline (see exhibits 1 & 2). The re-acceleration in CPI growth in June was attributed to a rise in food inflation.

Looking ahead, we expect that China's CPI growth will continue to go up in July, as a projected rise in food inflation will outweigh a decline in non-food inflation in the month. The year-on-year growth in the food component in the CPI is likely to jump from 11.1% in June to above 12.0% in July, as the recent floods in southern China have pushed up pork and vegetable prices markedly. Meanwhile, the year-on-year growth in the non-food component is likely to slow further from 0.3% in June, due largely to a sluggish domestic demand.

From August onwards, we believe that China's CPI growth will fall gradually to near-zero levels by the end of the year for three reasons. First, the impacts of floods on inflation tend to be short-lived and last no more than two or three months. Second, the economic slowdown brought about by the COVID-19 global pandemic will dampen domestic consumption. Lastly, a high base for comparison in the last few months of 2019 will weigh on CPI growth this year.

Exhibit 1: China's CPI growth and forecasts, July 2018 to December 2020



Source: National Bureau of Statistics

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.

Exhibit 2: China's CPI growth by commodity, January to June 2020

yoy growth (%)

	Jan 20	Feb	Mar	Apr	May	Jun
Clothing	0.6	0.5	-0.3	-0.4	-0.4	-0.4
Household articles and services	0.2	0.1	0.3	0.1	0.1	0.0
Education, culture and recreation	2.2	1.0	2.5	2.0	2.2	1.9

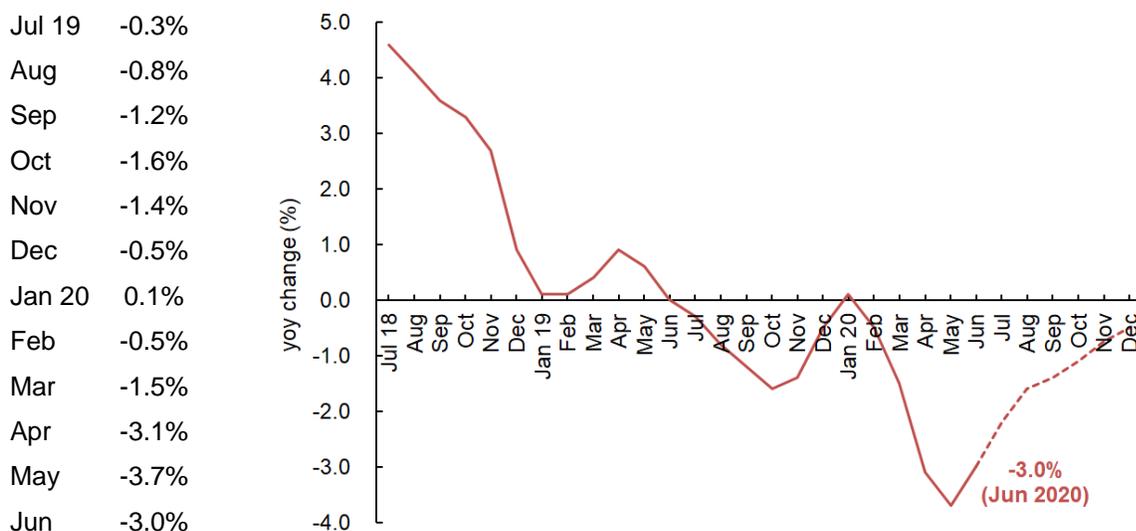
Source: National Bureau of Statistics

2. Ex-factory prices of industrial products rebound in June

China's factory gate deflation eased in June as the year-on-year growth in the producer price index of industrial products (PPI) improved from minus 3.7% in May to minus 3.0% in June (see exhibits 3 & 4). On a month-on-month basis, the PPI went up by 0.4% in June, turning around from a 0.4% drop in May. The increase in the PPI in June was mainly attributed to a rise in ex-factory prices in the crude oil, coal, chemicals, ferrous metals, and non-ferrous metals industries.

Going forward, the demand for industrial products is likely to continue to increase as domestic economic activity is set to recover further and major developed countries have also gradually reopened their economy. Besides, the rebound in global commodity prices will push up domestic prices of production inputs, adding cost pressures on manufacturers. Therefore, we expect that the PPI will continue to rise on a month-on-month basis, and the year-on-year growth will rebound further in the coming months.

Exhibit 3: China's PPI growth and forecasts, July 2018 to December 2020



Source: National Bureau of Statistics

**Exhibit 4: China’s PPI growth by selected industry,
January to June 2020**

yoy growth (%)

	Jan 20	Feb	Mar	Apr	May	Jun
Textile	-3.0	-3.0	-3.2	-4.5	-5.4	-5.6
Textile wearing apparel and ornament	-0.5	-0.5	-0.9	-1.0	-1.0	-0.9
Processing of timbers, manufacture of wood, bamboo, rattan, palm, and straw products	0.3	0.0	-0.1	-0.7	-0.7	-1.3

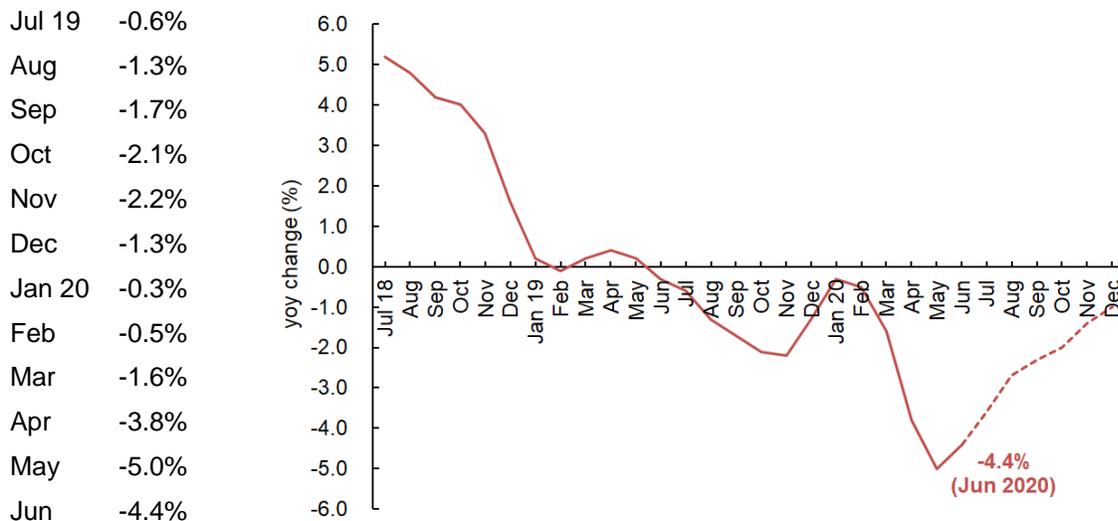
Source: National Bureau of Statistics, PRC

3. Domestic prices of production inputs pick up in June

The year-on-year growth rate of the purchaser price index of industrial products improved from minus 5.0% in May to minus 4.4% in June, showing moderation in China’s upstream deflation (see exhibits 5 & 6). On a month-on-month basis, the purchaser price index went up by 0.4% in June, after dropping by 1.2% in May.

Going forward, as domestic industrial production has returned to normal, the demand for production inputs is likely to improve further in the near future. Therefore, we expect that both the year-on-year growth and month-on-month growth in input prices will continue to pick up in the coming months.

Exhibit 5: Growth and forecasts of China’s purchaser price index of industrial products, July 2018 to December 2020



Source: National Bureau of Statistics

**Exhibit 6: China's purchaser price index of industrial products
by selected commodity, January to June 2020**

yoy growth (%)

	Jan 20	Feb	Mar	Apr	May	Jun
Fuel and power	-0.2	-1.0	-4.0	-11.4	-15.5	-14.2
Non-ferrous metal materials and wires	-0.7	-1.2	-4.8	-6.6	-5.5	-3.3
Chemical raw materials	-6.1	-6.0	-7.2	-9.3	-10.3	-9.4
Wood and pulp	-2.9	-2.7	-2.0	-2.7	-3.3	-2.9
Textile raw materials	-2.8	-2.8	-2.9	-3.6	-4.1	-4.0

Source: National Bureau of Statistics

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For more information, please visit www.funggroup.com.

CONTACT

Helen Chin
Vice President
helenchin@fung1937.com
(852) 2300 2471

William Kong
Senior Research Manager
williamkong@fung1937.com
(852) 2300 2404

Global Sourcing
Fung Business Intelligence
1/F LiFung Tower
888 Cheung Sha Wan Road
Kowloon, Hong Kong

T: (852) 2300 2470
F: (852) 2635 1598
E: fbicgroup@fung1937.com
W: <http://www.fbicgroup.com>



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