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China's CPI and PPI rebounded in July

ABCI Research

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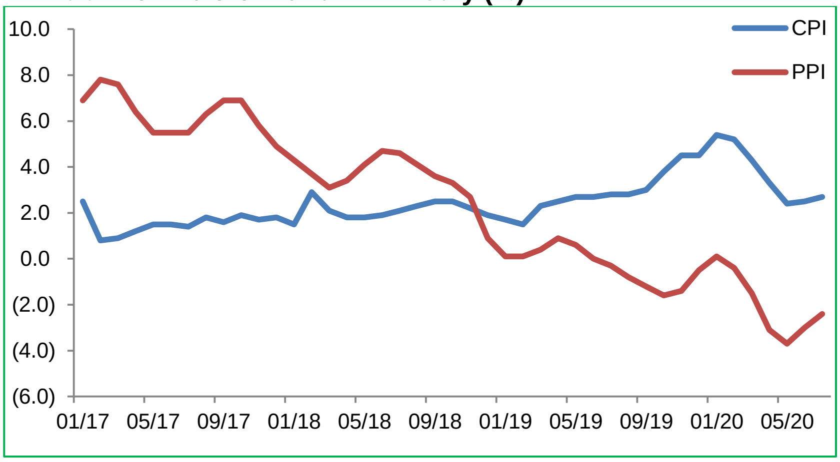
- China's CPI inched up to 2.7% in July from 2.5% in June, slightly above the market expectation of 2.6%, driven by acceleration in food price inflation amid heavy rainfall in Yangtze River region
- PPI rebounded further to -2.4% in July from -3.0% in June, slightly above the market expectation of -2.5%, driven by higher prices in global energy and other raw materials
- Looking ahead, we expect overall inflation to moderate, with the CPI easing due to high base for pork prices and the PPI staying in deflation despite a narrowing price decline. Current and future inflation expectations provide favorable conditions to maintain a loosened monetary policy to offset the impact of COVID-19 on the economy. The rates for one-year LPR and five-year LPR are expected to be 3.65% (current: 3.85%) and 4.55% (current: 4.65%) for end-2020E. RRR would continue to trend down, and we expect the rate for large commercial banks to be 10.5% (current: 11.0%) and the one for medium commercial banks to be 8.5% (current: 9.0%) for end-2020E

China's CPI inched up to 2.7%[1] in July from 2.5% in June, slightly above the market expectation of 2.6% (Exhibit 1). Overall food inflation rebounded to 13.2% in July from 11.1% in June, driving up CPI by 2.68ppt. Non-food prices edged down to 0.0% in July from 0.3% in June. The core CPI inflation, excluding food and energy, slowed to 0.5% in July from 0.9% in June. On a MoM basis, CPI inflation edged up to 0.6% in July from -0.1% in June. In 7M20 while consumer prices rose by 3.7% YoY.

Exhibit 1: China's CPI and PPI in July (%)



Source(s): NBS, ABCI Securities

The higher CPI in July was mainly driven by rising food prices amid heavy rainfall in Yangtze River region. For food, pork prices rose by 85.7% in July (June: 81.6%) and drove up headline CPI by 2.32ppt. Notably, pork prices rose by 10.3% MoM in July as a result of negative impact on the transportation of pigs due to floods in Yangtze River region. Prices of beef and mutton rose by 17.9% and 11.1%, lifting CPI by 0.58ppt. Fresh vegetable price rose by 7.9% in July, while prices of fruits and eggs dropped by 27.7% and 14.5%. For non-food items, healthcare prices rose 1.6%, and education services

[1] All growth rates are YoY except specified otherwise

rose 2.2%; in contrast, transport and communications prices fell by 4.4%, mainly led by transportation-related fuel price that fell by 15.5% due to the high base effect. Meanwhile, tourism prices and residential prices fell by 4.3% and 0.7%.

PPI rebounded further to -2.4% in July from -3.0% in June, slightly above the market expectation of -2.5%. Inflation in producer industries edged up to -3.5% in July from -4.2% in previous month, dragging down PPI by 2.56ppt. Inflation in consumer goods industries advanced slightly to 0.7% in July from 0.6% in June, boosting PPI by 0.19ppt. PPI was unchanged at 0.9% MoM in July. For 7M20, producer prices fell by 2.0% YoY.

The rebounding PPI in July was driven by higher prices in global energy and other raw materials. Oil and natural gas extraction prices, a PPI sub-item, rose by 12.0% MoM in July, while prices of oil, coal, and other fuel processing industries rose by 3.4% MoM; meanwhile, on a MoM basis, PPI inflation for the ferrous and non-ferrous industries also rose to 1.1% and 3.1% in July. The significant advancement in July PPI will lift the earning expectations of industrial enterprises.

Overall, July inflation data suggest a mild inflationary pressure as the core CPI, which removes the more volatile food and energy prices, remained low. Looking ahead, we expect overall inflation to moderate, with the CPI easing due to high base for pork prices and the PPI staying in deflation despite a narrowing price decline. Current and future inflation expectations provide favorable conditions to maintain a loosened monetary policy to offset the impact of COVID-19 on the economy. The rates for one-year LPR and five-year LPR are expected to be 3.65% (current: 3.85%) and 4.55% (current: 4.65%) for end-2020E. RRR would continue to trend down, and we expect the rate for large commercial banks to be 10.5% (current: 11.0%) and the one for medium commercial banks to be 8.5% (current: 9.0%) for end-2020E.

Disclosures

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Definition of equity rating

Rating	Definition
Buy	Stock return rate≥ Market return rate (10%)
Hold	- Market return rate (-10%) ≤ Stock return rate < Market return rate (+10%)
Sell	Stock return < - Market return (-10%)

Notes: Stock return rate: expected percentage change of share price plus gross dividend yield over the next 12 months
Market return rate: average market return rate since 2008 (HSI total return index 2008-19 CAGR at 10%)

Time horizon of share price target: 12-month

Stock rating, however, may vary from the stated framework due to factors including but not limited to: corporate governance, market capitalization, historical price volatility relative to corresponding benchmark index, average daily turnover of the stock relative to market capitalization of the stock, competitive advantages in corresponding industry, etc.

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