Economic Analysis

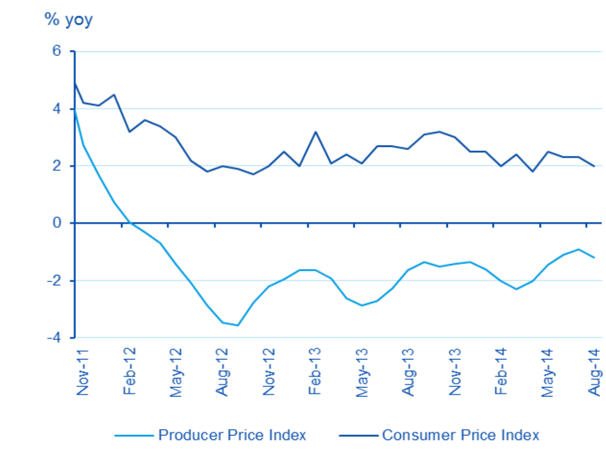
A combination of subdued inflation and weak imports suggests that more easing measures lie ahead

Le Xia and Jinyue Dong

Headline CPI inflation softened further to 2.0% y/y in August from 2.3% y/y in the previous month, while PPI deflation widened to -1.2% y/y from -0.9% y/y in July. The subdued inflation outturns provided room for further policy easing in the second half of the year, which is needed to spur sluggish domestic demand. Separately, the authorities announced trade data on Monday, among which, exports continued its strong performance whereas imports remained weak. Looking ahead, we anticipate that the authorities will deploy more "targeted" easing policies in the rest of the year, so as to sustain economic growth aligned with their annual target of 7.0-7.5%. Moreover, the government is set to press ahead with structural reforms, providing new impetus for the economic rebalancing. We therefore maintain our growth projection of 7.2% for this year.

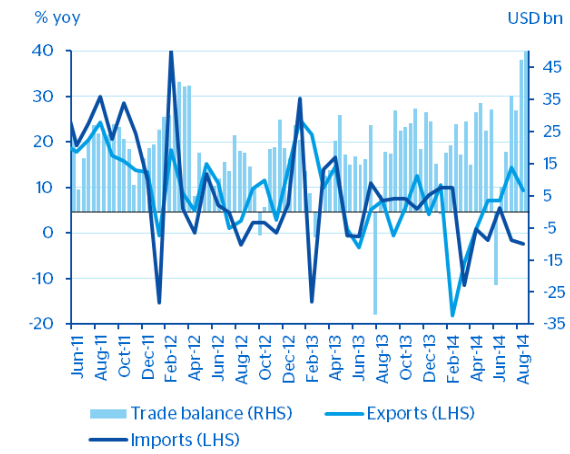
- **Headline CPI remained subdued while PPI deflation persisted.** CPI inflation decelerated to 2.0% y/y in August (Consensus: 2.2%) from 2.3% y/y in July, well within the government's 3.5% tolerance target. By component, food prices grew by 3.0% y/y while non-food prices increased by 1.6% y/y. PPI inflation declined to -1.2% y/y (Consensus: -1.1%) from -0.9% y/y in the previous month, partly due to the overcapacity problem in upstream industries and sluggish domestic demand. (Figure 1) Continued subdued inflation provides room for more pro-growth initiatives, which, we believe, are likely to come in the forms of "targeting easing" as we forecasted in our latest *China Economic Watch*.
- **Exports grew steadily whereas imports remained weak on sluggish domestic demand.** China's exports increased by 9.4% y/y (Consensus: 9.0%) in August, down from 14.5% in the previous month. Meanwhile, imports unexpectedly declined by -2.4% y/y compared with -1.6% in July, mainly due to the sluggish commodity price as well as anemic domestic demand. As a result, trade surplus expanded to USD 49.8 bn (Consensus: 40.0 USD bn), from the surplus of USD 47.3 bn in the previous month. (Figure 2) The expanding trade surplus has increased the RMB's appreciation pressure and contributed to the recent rebound of the currency. Although the external demand is still subject to great uncertainty, we anticipate China's exports to grow steadily and partially offset weak domestic demand in the coming months. One of its side effects is that the ongoing rebalancing of the economy might be derailed as trade surplus rises again.

Figure 1
CPI remains subdued while PPI deflation persists



Source: CEIC and BBVA Research

Figure 2
The trade surplus has continued to expand



Source: CEIC and BBVA Research

DISCLAIMER

This document has been prepared by BBVA Research Department, it is provided for information purposes only and expresses data, opinions or estimations regarding the date of issue of the report, prepared by BBVA or obtained from or based on sources we consider to be reliable, and have not been independently verified by BBVA. Therefore, BBVA offers no warranty, either express or implicit, regarding its accuracy, integrity or correctness.

Estimations this document may contain have been undertaken according to generally accepted methodologies and should be considered as forecasts or projections. Results obtained in the past, either positive or negative, are no guarantee of future performance.

This document and its contents are subject to changes without prior notice depending on variables such as the economic context or market fluctuations. BBVA is not responsible for updating these contents or for giving notice of such changes.

BBVA accepts no liability for any loss, direct or indirect, that may result from the use of this document or its contents.

This document and its contents do not constitute an offer, invitation or solicitation to purchase, divest or enter into any interest in financial assets or instruments. Neither shall this document nor its contents form the basis of any contract, commitment or decision of any kind.

In regard to investment in financial assets related to economic variables this document may cover, readers should be aware that under no circumstances should they base their investment decisions in the information contained in this document. Those persons or entities offering investment products to these potential investors are legally required to provide the information needed for them to take an appropriate investment decision.

The content of this document is protected by intellectual property laws. It is forbidden its reproduction, transformation, distribution, public communication, making available, extraction, reuse, forwarding or use of any nature by any means or process, except in cases where it is legally permitted or expressly authorized by BBVA.