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China Economics

Signs of Stabilization Ahead of Politburo? – Jun/Q2 Data Preview

CITI'S TAKE

June data is likely to show tentative stabilization, with exports leading growth and retail sales potentially turning positive on accelerating trade-in subsidies. Likely soft investment and weak credit nonetheless reinforce the case for easing – July's LPR decision is the earliest test point.

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Signs of stabilization ahead of Politburo? — We maintain our growth forecast at 4.5%YoY for 26Q2E, which could mark the trough for the year (see: China Outlook 26H2: AI Supercycle Cuts into the K-shaped Economy). Monthly indicators could show signs of stabilization. Industrial production is likely to hold steady at 4.6%YoY thanks to AI-centric exports and investment. Retail sales may turn positive at 0.6%YoY on a more favorable base and – more importantly – accelerating trade-in subsidies. Daily average subsidized sales quickened to ~RMB8.8bn in Jun 1-20 compared with ~RMB5.4bn in Jan-May (people.com, Jun 22nd and Jun 20th). Investment remains a drag: we expect cumulative contraction in FAI to deepen to -4.5%YoY Ytd, though the monthly pace of decline could narrow to a mid-single digit. This set of data is unlikely to shift the tone of the mid-year Politburo meeting. We continue to see only piecemeal consumer support, with July as the earliest window for an LPR cut following the surprisingly low O/N reverse repo rate.

Will exports continue to lead growth? — We forecast China's exports to stay strong at 18.0%YoY in June, with imports also elevated at 25.0%YoY, leaving the trade surplus at ~US$119.5bn. Export momentum is likely to remain solid, supported by easing Middle East tensions and the ongoing global AI supercycle. This is consistent with the rebound in June PMI new export orders and improving high-frequency volume data, with cargo throughput up 1.3%YoY in the first four weeks of June. For imports, robust AI-related demand is the key tailwind, evidenced by South Korea's exports to China rising 92.1%YoY in June. However, softer commodity prices may partially offset headline import growth.

Disinflation after oil shock? — We pencil in June CPI at 1.1%YoY and PPI at 4.3%YoY. The oil shock appears largely behind us, with price-related PMI indices moderating and Brent down -20.2%MoM. Yet we tend not to overestimate the downside risk: coal prices extended their rise into June and could have broader spillover effects than oil & gas. AI inflation may also surface further in PPI. On CPI, the picture is little changed – food prices are tracking broadly in line with seasonality (pork -1.9%MoM, vegetables +2.0%MoM, fruit -3.2%MoM), while oil and gold prices weighing on the headline, partly offset by firmer travel prices around Dragon Boat Festival and into the summer season.

The return of monetary easing? — New credit data looks set to disappoint again with the PBoC's third consecutive window guidance (Reuters, Jun 26th) and subdued bills discount rates throughout the month. We expect new RMB loans at RMB1,800bn (vs. RMB2,240bn last June) and new Total Social Financing at RMB3,500bn (vs. RMB4,225bn), with government bond issuance (~RMB800bn) and corporate bond financing (~RMB500bn) providing the main support to the latter. Monetary growth is also likely to retreat as a higher base kicks in. We expect M1 growth at 3.5%YoY and M2 at 8.1%YoY. Together, this reinforces the case for further monetary easing, with July's LPR decision a key test point to watch.

See Appendix A-1 for Analyst Certification, Important Disclosures and Research Analyst Affiliation

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Figure 1. June data is likely to show tentative stabilization, yet sluggish investment could reinforce the case for easing

Indicators	Date	For	Citi Fcast	Prior	Indicators	Date	For	Citi Fcast	Prior
FX Reserves (US$ bn)	Jul 7	Jun	3,450	3,442	M1 (%YoY)	Jul 9~15	Jun	3.5	5.5
Exports Growth (%YoY)	Jul 14	Jun	18.0	19.4	M2 (%YoY)			8.1	8.6
Imports Growth (%YoY)			25.0	27.4	New RMB Loans (RMB bn)			1,800	520
Trade Balance (US$ bn)			119.5	105.4	Total Social Financing (RMB bn)			3,500	2,026
CPI (%YoY)	Jul 9	Jun	1.1	1.2	GDP (%YoY)	Jul 15	Q2	4.5	5.0
PPI (%YoY)			4.3	3.9	Industrial Production (%YoY)		Jun	4.6	4.5
					Retail Sales (%YoY)			0.6	-0.6
					FAI (%YoY Ytd)			-4.5	-4.1

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Source: China Customs, NBS, PBoC, Wind, Citi Research