Greater China – Week in Review

Highlights: First wave of Iran war's impact

Tommy Xie Dongming
Head of Asia Macro Research

Keung Ching (Cindy)
Hong Kong & Macau Economist

The first wave of the Iran war's impact on China has emerged through inflation, with PPI accelerating to 2.8% YoY, up from 0.5% in March. However, the breakdown suggests that the PPI rebound was driven mainly by supply-side and imported factors, as prices of production goods rose 2.1% MoM. By contrast, prices of consumer goods continued to decline by 0.1% MoM, indicating that upstream-to-downstream price transmission remains weak.

CPI showed signs of a mild recovery in April, edging up to 1.2% YoY The moderate CPI reading was partly flattered by the negative contribution from the pork-price downcycle. Meanwhile, the pass-through from higher international oil prices has started to emerge. In April, transport & communications and other goods & services saw notable YoY improvements, contributing around 0.66ppt and 0.32ppt to headline CPI, respectively.

However, indirect pass-through through the manufacturing cost chain remained modest, as overcapacity, weak end demand, and government price controls continued to absorb cost pressures. While low capacity utilisation will take time to resolve, it has also helped cushion the inflation impact.

PPI exceeded CPI for the first time since July 2022, reopening the "scissors gap" between upstream and downstream prices. This suggests that part of the imported inflation shock will likely be absorbed by corporate margins rather than fully passed on to consumers. The focus in the coming months will be mainly the passthrough effect.

On finance and credit data, China's total social financing (TSF) increased by RMB624.5bn in April, missing market consensus and coming in RMB535.4bn lower than a year earlier. Outstanding TSF growth slowed by 0.1ppt to 7.8% YoY.

The new Yuan loan to the economy contracted unexpectedly. The contraction in loans mainly reflected three factors. First, households remained reluctant to add leverage. Household loans fell by RMB340.8bn, with medium- to long-term household loans declining RMB225.0bn more than a year earlier, suggesting that property demand remains weak. Second, corporate financing continued to shift from bank loans to bond issuance, as lower bond yields made bond financing more attractive. Third, the slow pace of major project starts also weighed on corporate loan demand.

Money supply data also pointed to an uneven recovery. M1 growth eased by 0.1ppt to 5.0% YoY, possibly dragged by stronger-than-expected fiscal deposit growth. M2 growth, however, edged up by 0.1ppt to 8.6% YoY, likely supported by an increase in FX settlement, which may reflect stronger corporate willingness to sell foreign currency amid RMB appreciation.

Overall, April new loans and TSF both missed expectations. The renewed contraction in credit highlights still-weak property and consumption demand, a moderation in fiscal support at the margin, and the fact that exports alone are not sufficient to sustain corporate credit expansion.

Revised GDP growth figures for Hong Kong and Macau in the first quarter were unchanged, at 5.9% YoY and 7.1% YoY respectively. Despite calling Hong Kong's economic outlook resilient, the government maintained the full-year growth forecast at 2.5%-3.5% (our in-house forecast at 3.4%), citing uncertainties surrounding the scale and duration of the Middle East conflict, and the subsequent downside risks to growth.

Key Economic News	
Facts	**OCBC Opinions**
▪ China's total social financing (TSF) increased by RMB624.5bn in April, missing market consensus and coming in RMB535.4bn lower than a year earlier. Outstanding TSF growth slowed by 0.1ppt to 7.8% YoY. Credit to the real economy contracted by RMB400.6bn, a deeper decline than expected.	▪ The contraction in loans mainly reflected three factors. First, households remained reluctant to add leverage. Household loans fell by RMB340.8bn, with medium- to long-term household loans declining RMB225.0bn more than a year earlier, suggesting that property demand remains weak. Second, corporate financing continued to shift from bank loans to bond issuance, as lower bond yields made bond financing more attractive. Third, the slow pace of major project starts also weighed on corporate loan demand. ▪ Corporate bond financing increased by RMB452.0bn, RMB218.0bn more than a year earlier, supported by lower issuance costs amid ample liquidity and stronger institutional allocation demand. Government bond financing rose by RMB904.1bn, RMB68.8bn less than a year earlier. While government bond issuance may accelerate in May-June, the rising base from last year suggests that the YoY improvement may still be limited. ▪ Money supply data also pointed to an uneven recovery. M1 growth eased by 0.1ppt to 5.0% YoY, possibly dragged by stronger-than-expected fiscal deposit growth. M2 growth, however, edged up by 0.1ppt to 8.6% YoY, likely supported by an increase in FX settlement, which may reflect stronger corporate willingness to sell foreign currency amid RMB appreciation. ▪ Overall, April new loans and TSF both missed expectations. The renewed contraction in credit highlights still-weak property and consumption demand, a moderation in fiscal support at the margin, and the fact that exports alone are not sufficient to sustain corporate credit expansion.
▪ China's CPI showed signs of a mild recovery in April, edging up to 1.2% YoY, with MoM inflation turning positive. PPI rose more sharply, accelerating to 2.8% YoY from 0.5% in March.	▪ However, the breakdown suggests that the PPI rebound was driven mainly by supply-side and imported factors, as prices of production goods rose 2.1% MoM. By contrast, prices of consumer goods continued to decline by 0.1% MoM, indicating that upstream-to-downstream price transmission remains weak. ▪ The moderate CPI reading was partly flattered by the negative contribution from the pork-price downcycle. Meanwhile, the pass-through from higher international oil prices has started to emerge. In April, transport & communications and other goods & services saw notable YoY improvements, contributing around 0.66ppt and 0.32ppt to headline CPI, respectively. However, indirect pass-through through the manufacturing cost chain remained modest, as overcapacity, weak end demand, and government price controls continued to absorb cost pressures. While low capacity utilisation will take time to resolve, it has also helped cushion the inflation impact. ▪ PPI exceeded CPI for the first time since July 2022, reopening the "scissors gap" between upstream and downstream prices. This suggests that part of the imported inflation shock will likely be absorbed by corporate margins rather than fully passed on to

	consumers. ▪ Overall, the oil-driven price pressure should be viewed mainly as a short-term impulse. Producer inflation may peak in May before edging lower, but the inflation centre is likely to move higher. As oil prices are unlikely to fall sharply in the near term, they should remain a key driver of YoY price gains for some time.
▪ Hong Kong: Revised GDP growth figure for Hong Kong in the first quarter was unchanged, at 5.9% YoY. Despite calling Hong Kong's economic outlook resilient, the government maintained the full-year growth forecast at 2.5%-3.5% (our in-house forecast at 3.4%), citing uncertainties surrounding the scale and duration of the Middle East conflict, and the subsequent downside risks to growth.	▪ The strong growth momentum was carried forward from the final quarter last year, to the first half this year. Stellar performance in the asset markets and the resulting wealth effect supported an improvement in domestic demand. In addition, exports both benefited from the ongoing AI investment cycle. However, we expect to see some moderation in growth in the coming quarters. ▪ On consumption, it is worth noting that recent upward pressure on Hong Kong interest rates, together with ongoing signs of softness in the labor market, may weigh on consumption in coming months. As for exports, demand for electronic components remained very strong under the AI boom, and we expect double-digit export/import growth for the full year. However, from a GDP accounting perspective, net exports are expected to remain a drag on overall economic growth.