

Tentative Relief

China's June PMI survey points to tentative stabilization in manufacturing and service activities, reducing the urgency for broad-based monetary easing in the near term.

Turning to indicators expected in the upcoming weeks, both CPI and PPI inflation appear to have peaked in June, as energy price pressures ease and the passthrough to core inflation remains insignificant. Trade sentiment also improved in June, pointing to another month of solid trade growth.

While high-frequency activity indicators likely stayed soft in June, we expect Q2 GDP growth to prove more resilient than monthly data may suggest, supported by its supply-side nature, as well as likely solid services consumption and tech capex during the period. We therefore expect Beijing's policy support to remain measured and targeted, with the policy mix skewed toward fiscal measures.

Fig 1 Our forecasts for China's major economic indicators

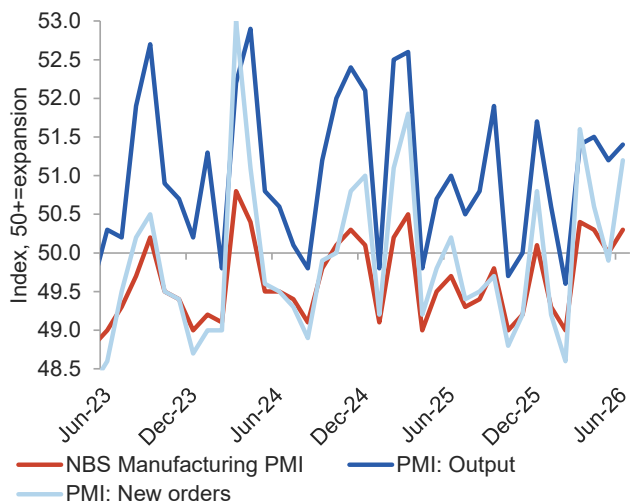
Indicators	Mar	Apr	May	Jun (forecast)
CPI (YoY %)	1.0	1.2	1.2	1.1
PPI (YoY %)	0.5	2.8	3.9	4.4
Export growth (YoY %)	2.5	14.1	19.4	20
Import growth (YoY %)	27.8	25.3	27.4	24
Trade balance (USDb)	50.2	84.7	105.4	128
New loans (CNYb)	2990	-10	520	2100
Total social financing (CNYb)	5227	625	2029	3900
M2 (YoY %)	8.5	8.6	8.6	8.5
VAI (YoY %)	5.7	4.1	4.5	4.3
Retail sales (YoY %)	1.7	0.2	-0.6	-0.5
FAI (YTD YoY %)	1.7	-1.6	-4.1	-6
GDP (YoY %)	5.0 (Q1)	--	--	4.6 (Q2)

Source: Bloomberg, Mizuho

China's official **Manufacturing PMI** surprised to the upside in June, rising to 50.3. Contrary to our expectation of production-led improvement, the stronger headline print was driven by firmer demand. The new orders sub-index rose to 51.2, from 49.9 in May, while the production sub-index only improved modestly (Fig. 2).

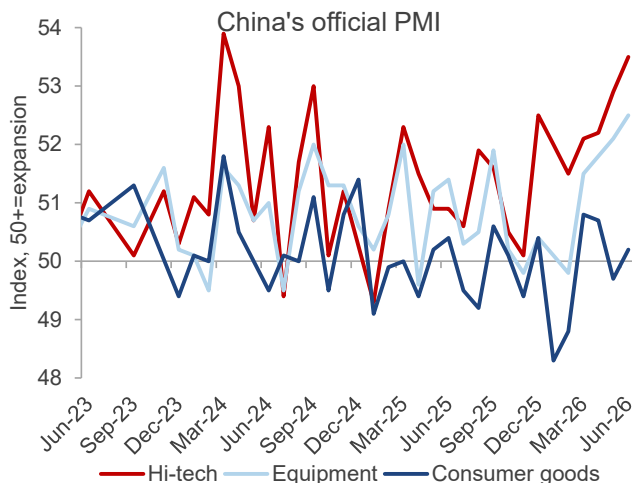
Beneath the headline, the sectoral breakdown was broadly constructive. High-tech, equipment and consumer goods manufacturing all registered a better result in June (Fig. 3). Manufacturing of basic raw materials was the only segment suffering from persistent headwinds, with its PMI down to a year-low of 47.1.

Fig 2 Manufacturing PMI improvement driven by firmer demand



Source: CEIC, Mizuho

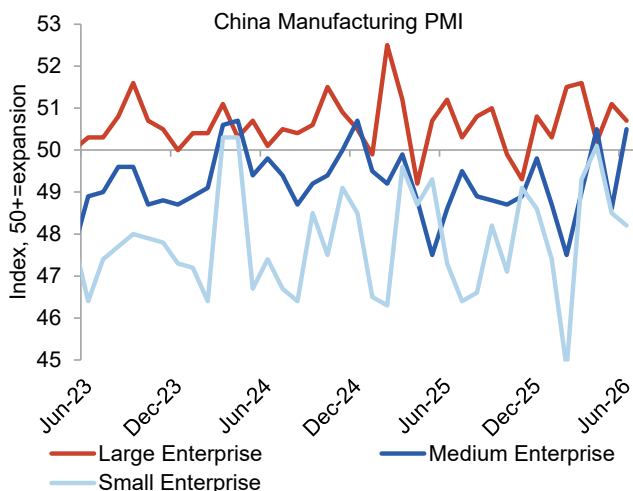
Fig 3 Sectoral breakdown was broadly constructive



By enterprise size, the strongest improvement came from medium-sized manufacturers, whose PMI rose to 50.5, matching its previous peak. PMI readings for both large and small manufacturers softened in June (Fig. 4), broadly consistent with the limited moderation seen in RatingDog manufacturing PMI, which eased to 51.7 in June.

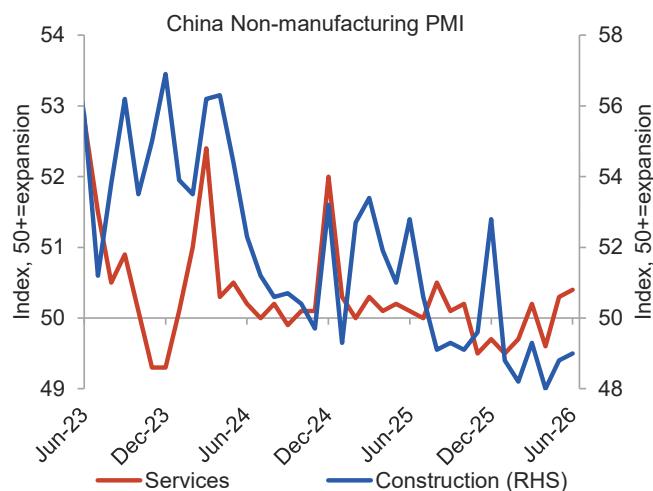
Non-manufacturing sentiment also outperformed expectations, defying expectations of a contraction and rising to 50.2 in June. The improvement was led by services, where the PMI climbed to a ten-month high of 50.4, supported by stronger activity in sectors such as telecommunications and information technology. Meanwhile, the construction PMI improved from the previous trough, indicating eased contraction (Fig. 5).

Fig 4 Small factories are less resilient amid higher input costs



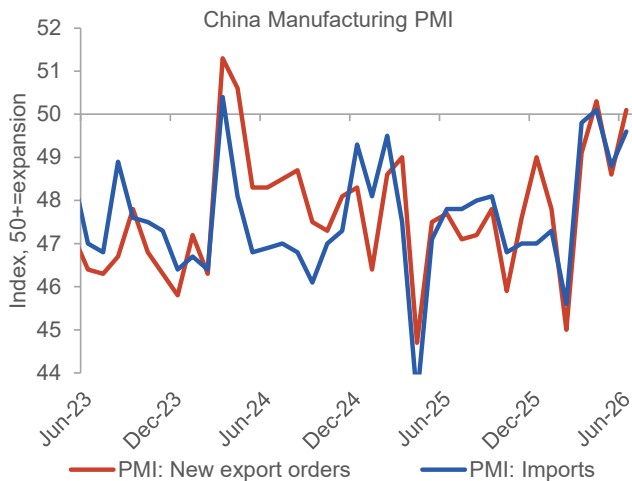
Source: CEIC, Mizuho

Fig 5 Service PMI continued to outperform



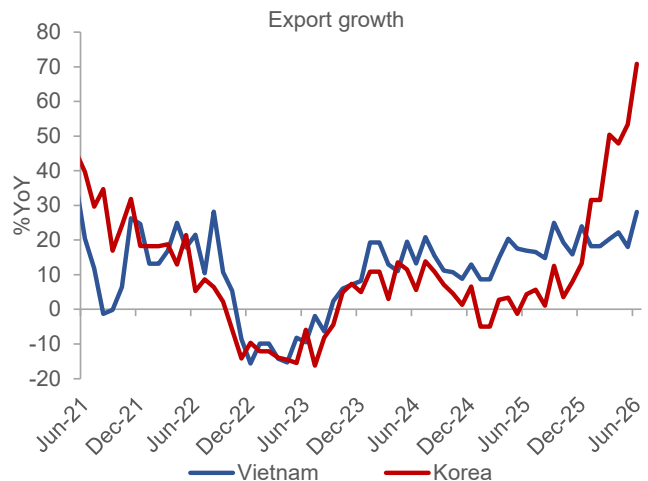
Trade-related PMI indicators also improved in June. Notably, the new export orders index returned to expansionary territory at 50.1, suggesting better trade sentiment following the US-Iran interim ceasefire agreement (Fig. 6). This, combined with relatively fast increases in export and import prices, points to another month of solid trade growth. Note that Korean exports significantly outperformed in June amid continued shortage in semiconductor supply.

Fig 6 Trade-related sentiment improved in June



Source: CEIC, Mizuho

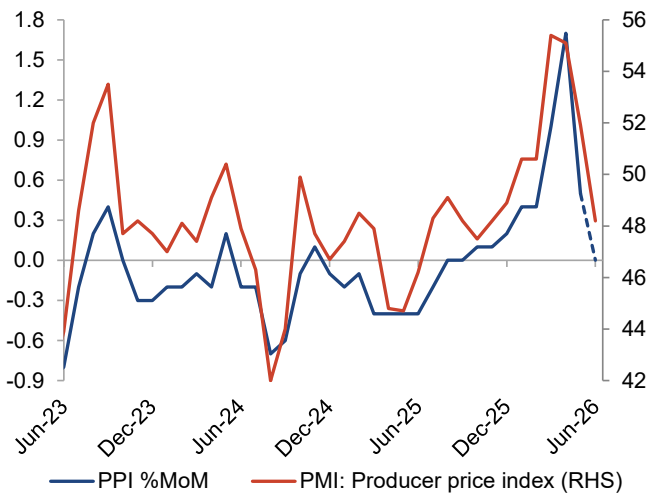
Fig 7 Korean exports outperformed on demand for semiconductors



On the inflation front, imported price pressures have finally begun to ease, with the PMI gauge for producer prices falling below the expansion threshold for the first time in six months. Against this backdrop, we expect **PPI inflation** to register a muted sequential increase in June (Fig. 8), although YoY growth is likely to accelerate to above 4%, largely reflecting last year's low base.

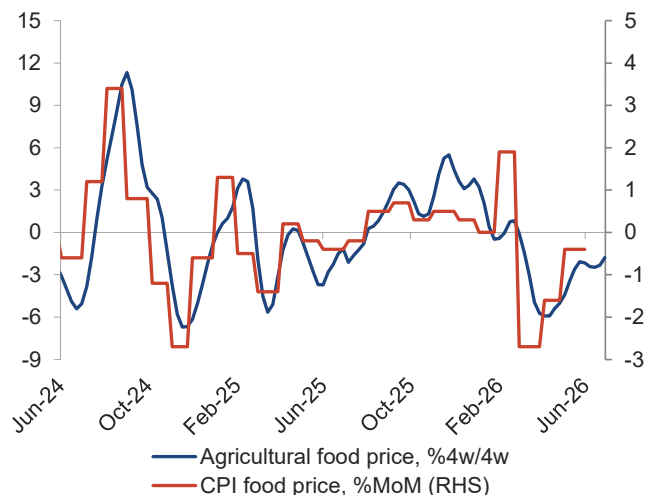
CPI inflation is also expected to moderate slightly from May, driven by lower fuel costs and continued softness in food prices. Domestic fuel prices declined by an average of 4.7% MoM in June, following a 0.6% MoM drop in May. Food prices are likely to record another sequential decline (Fig. 9), weighed down by lower pork and fruit prices. Additionally, the passthrough from higher energy costs to core CPI remains limited amid subdued domestic demand.

Fig 8 PMI gauge for producer prices fell below 50



Source: CEIC, Mizuho

Fig 9 Food prices stayed subdued in June



Turning to domestic activity, credit growth is expected to have remained resilient in June, supported by relatively accommodative front-end liquidity conditions. Notably, the PBoC injected liquidity through overnight open market operations for the first time at the end of June, with a total amount of RMB900bn at a fixing rate of 1.25%. Given that DR001 had been trading around 1.4% over the preceding weeks, this operation underscores the central bank's efforts to smooth quarter-end funding pressures through a targeted liquidity tool.

While we expect most activity indicators to remain subdued in June, particularly fixed asset investment and retail sales, we do not anticipate similar weakness in Q2 GDP growth. This partly reflects the fact that China's GDP data are primarily compiled with supply-side data, and weakness in demand-side indicators may not translate one-for-one into headline GDP growth. In addition, services consumption and a large part of technology-sector capital expenditure, which likely outperformed in Q2, are not captured by those monthly activity indicators.

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