MONTHLY REPORT

TRADE SERVICING

– WUSATA

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Market: China & HK **Submitted by**: China In-market Representative **Month & Year:** August 2023

Executive Summary

The General Administration of Chinese Customs (GACC) trade data through the first six months of 2023 show an 8.3 percent increase in the total import value of agricultural commodities compared to the same period last year, and relatively flat exports over the same period. Import volumes were mixed, with significant increases in vegetable oils and soybeans, modest increases in meats and grains, and lower volumes of cotton, dried fruits, and nuts. Higher soybean and vegetable oil imports reflect China's rebounding demand for oils and soybean meal (SBM) following the end of China's zero-covid policy in December 2022 and lower prices. Imports of grains (driven by wheat imports) were up 3.6 million metric tons (MMT) in the first half of 2023 compared to 2022. Meat imports increased 10 percent on recovering demand in the HRI sector, however cotton imports dropped 55 percent on high stocks, weak textile and apparel demand, and lack of additional import quota.

The overall increase in agricultural imports comes amid concerns that the broader economy remains sluggish, with monthly economic data showing the post-covid recovery is slowed by low consumption and retail sales, a troubled housing sector, and youth unemployment (ages 16-24) at a record high of 21.3 percent

Market Intelligence Update

China's consumer prices fall for the first time in 2 years, as fears of deflation grow

China reported inflation data for July that pointed to a modest improvement from June. The consumer price index fell by 0.3% in July from a year ago, but was up by 0.2% when compared with June, according to the National Bureau of Statistics Wednesday.

The year-on-year CPI print for July was slightly better than expectations for a 0.4% decline, according to analysts polled by Reuters. It was still the first year-on-year decline since early 2021, according to official data accessed via Wind Information.

The producer price index fell by 4.4% in July from a year ago, better than the 5.4% decline in June, the data showed.

However, the year-on-year PPI read was worse than the 4.1% forecast by a

Reuters poll.

“Both CPI and PPI are in deflation territory,” said Zhiwei Zhang, president and chief economist of Pinpoint Asset Management, in a note following the data release. “The economic momentum continues to weaken due to lacklustre domestic demand.”

“The CPI deflation may put more pressure on the government to consider additional fiscal stimulus to mitigate the challenge,” he added.

A 26% year-on-year drop in pork prices, a staple food in China, contributed to the overall decline in the CPI in July. Tourism prices rose by 13.1% from a year ago.

Core CPI, which excludes food and energy prices, rose by 0.8% from a year ago — the highest since January, according to official data accessed via Wind Information.

Producer prices will likely turn higher on a year-on-year basis before the consumer price index does, said Bruce Pang, chief economist and head of research for Greater China at JLL.

He expects consumer prices will still be dragged down in the coming months by falling pork prices and a high base effect, while core CPI may gradually rise.

Lackluster domestic demand has persisted since the pandemic. China’s consumer price index was flat in June from a year ago. Second-quarter data prompted several economists to warn of growing risk of deflation — a persistent decrease in prices over time.

Officially, China’s central bank has pushed back against such fears and said it expects consumer prices to pick up after a dip in July.

Oxford Economics expects China’s consumer price index to grow by 0.5% this year and the producer price index to fall by 3.5%.

“China’s weak demand follow-through in Q2 can be attributed to its relatively contained demand-side stimulus during Covid, years of regulatory tightening, and an ongoing housing correction,” Louise Loo, lead economist at Oxford Economics, said in a note Tuesday.

It’s a “positive development” that authorities are choosing targeted easing, rather than large-scale stimulus, Loo said.

China reported trade data Tuesday that showed a sharp plunge in both overseas and domestic demand.

Exports fell by 14.5% in July from a year ago, while imports dropped by 12.4% in U.S. dollar terms — both worse than analysts had expected.

The sharp decline in the imports figure was partly due to commodity price declines, but Loo’s estimates indicate imports declined in real volume terms by around 0.4%.

China is set on Aug. 15 to release retail sales, industrial production and other data for July.

Yum China flags weak consumption despite record quarter

Yum China, the country's biggest fast-food operator, reported record earnings for the second quarter but said it was forced to rely on discounts and other promotions to boost sales as consumption overall weakened.

Yum has more than 13,600 outlets in mainland China across a number of brands, namely KFC, Pizza Hut, Taco Bell, Lavazza and Chinese-style restaurants Little Sheep and Huang Ji Huang. On Tuesday it reported revenue of $2.51 billion and an operating profit of $257 million for April-June, up 24% and 216% on the year, respectively.

During the same period last year, major cities like Shanghai were under severe lockdown, making for a low base of comparison. However, revenue and operating profit were both more than 20% higher than the pre-COVID second quarter in 2019.

The record quarter came amid a "challenging" environment, according to the company's chief financial officer, Andrew Yeung. "Consumers continue to be value-conscious," he said, adding that Yum's sales "materially weakened after the May 1 holiday." The May Day break is one of the long vacation periods in mainland China.

Yeung attributed that weakness to two main factors: an uptick in COVID infections starting from late April and challenging macroeconomic conditions. The remedy was to "swiftly launch attractive offers to drive sales," Yeung said.

CEO Joey Wat elaborated on how the company tried to loosen people's purse strings.

"Customers are very value cautious, that's for sure," she told analysts and investors during an online conference call on Tuesday (August 1). "It's not enough if we just focus on promotion. It has to be a [combination of] promotion, fun and good food," she said. One example was Hello Kitty toys handed out to attract children and parents.

Wat said the company focused on a "few effective promotions." In the case of KFC, these include "Crazy Thursday" and "Sunday buy more save more," while Pizza Hut has "Scream Wednesday" and Taco Bell has "Taco Tuesday."

Despite the tough environment, Yum is focused on expanding its network. It stepped up store openings in the first half, with 655 net new outlets added during the six months. There are now more than 3,000 Pizza Huts in mainland China, while Shanghai alone has over 500 KFCs. The full-year target remains between 1,100 and 1,300 net new stores, with a capital expenditure of up to $900 million.

"The most critical thing that we are looking for is incremental sales, especially incremental same-store sales," said Wat, adding that Yum would also open more stores in smaller cities.

Still, confidence regarding consumption, even for smaller items like fast food, appeared subdued during the past quarter. "Consumption during the holidays and festivals was amazingly [good], but in between it was a bit more depressed," the CEO said.

Lorraine Tan, equity research director at Morningstar Asia, shared a similar view on consumption in the country.

"We were hoping that China's consumer confidence could start to really show signs of improvement in the third quarter," she told reporters on Tuesday, but added that "policies need to do a little more to sustain the uptick in consumer confidence." Strengthening the real estate sector, she said, will be "key" to restoring the country's appetite for consumption.

China lifts anti-dumping tariffs on Australian barley after three years, easing supply concerns

China on Friday (August 4) lifted tariffs on Australian barley imports starting Aug. 5, a move that points to improving bilateral relations and would alleviate supply concerns after Russia suspended a humanitarian corridor to deliver key Ukrainian grains to global markets.

These anti-dumping tariffs and countervailing duties were imposed in mid-2020 at the height of diplomatic tensions between China and Australia. Beijing slapped import tariffs on several Australian exports from wine and red meat to lobsters and timber. Besides this barley announcement, China also resumed

Australian coal imports in January.

The Chinese Ministry of Commerce “has ruled that it is no longer necessary to continue to impose anti-dumping duties and countervailing duties on imports of barley originating in Australia in view of changes in the Chinese barley market,” it said in a statement Friday. No further details on these changes were provided.

In April, Australia agreed to “temporarily suspend” its World Trade Organization complaint against China for its 2020 decision to impose 80.5% duties on Australian barley, paving the way for Beijing to expediate its review of the tariff decision. These tariffs were slated to expire next week.

“We welcome this outcome, which paves the way for our barley exporters to re-enter the Chinese market – benefiting Australian producers and Chinese consumers,” Australia’s trade minister Don Farrell, foreign minister Penny Wong and agriculture minister Murray Watt said in a joint statement. “The removal of these duties means that Australia will now discontinue legal proceedings at the WTO.”

Farrell, Wong and Watt said they expect a similar process for the removal of duties on Australian wine. In March 2021, China introduced a crushing five-year tariff of up to 218% on Australian wine.

Australia is one of the few developed nations on Earth that exports more into China than it imports from China. Their bilateral relationship deteriorated after Australia supported a call for an international inquiry into China’s handling of the coronavirus pandemic, which was first reported in the Chinese city of Wuhan.

The move will also likely open up another source of barley imports for China, which would ease concerns about food price inflation emanating from Russia’s withdrawal last month from a landmark agreement known as the Black Sea Grain Initiative.

Over the last year, the agreement facilitated the passage of more than 1,000 ships carrying nearly 33 million metric tons of Ukrainian wheat, barley, corn and sunflower meal.

China, one of Moscow’s closest strategic allies and the world’s second-largest economy, was the indisputable top recipient of Ukrainian agricultural products — including about a quarter of outbound barley volume, according to data provided by the United Nations Thursday.

The United States and its Western allies are looking to China to help resolve the calamitous domino effect of Russia’s exit from the crucial U.N.-backed agriculture deal.