

# China Economy

## Several observations on China trade YTD

According to China Customs release yesterday, Jul export/import in China +3.3%/-5.6% YoY, beating expectation. In this report, we documented several stylized trends regarding trade YTD. In light of protracted trade negotiations, global economic slowdown as well as weak domestic demand, we remain cautious regarding trade outlook in 2H19.

- **Rising trade surplus when trade activities subdued.** In the Jan-Jul period, export/import growth was +0.6%/-4.5% YoY, respectively. The fact that export growth outpaced import growth has boosted YTD trade balance to US\$ 225.7bn, vs. US\$ 162.8bn in the same period last year. It also explains a larger contribution from net export to China's GDP growth in 2H19 (~20%).
- **Wider divergence between U.S. and other trade partners of China.** Trade conflict around the globe is abruptly causing meaningful trade diversion and supply chain relocations toward a new steady state of balance. For China, YTD export to the U.S. declined 7.8% YoY, while export to EU and ASEAN increased +5.9%/+8.9% YoY. YTD import from the U.S. plunged 28.3% YoY, while import growth from EU/ASEAN/Japan was +2.3%/-0.1%/-7.4%. ASEAN has become China's second largest trading partner, surpassing the U.S.
- **Trade conflict was not the mere explanation for trade weakness.** According to our calculation, U.S. dragged overall export/import growth of China by 1.5ppt/2.3ppt YTD, respectively, whereas export/import growth rate stood at 0.6%/-4.5% YoY. That said, even without conflict with the U.S., China would report low-single-digit export growth YTD because of global economic slowdown and import growth would remain negative due to weak domestic demand and uncertainties regarding China's economic growth.
- **Major categories of goods which dragged export include,** mobile phones and parts (-15.8%), ships (-23.5%), automatic data processing equipment (-1.1%). **Major products which dragged import growth include** electronics and high-tech products plunged, including semi-conductors (-6.9%), auto and auto parts (-11.6%), LCD panel (-18.4%).
- **Trade surplus enlarged with the US.** In Jan-Jul, China's export to the U.S. declined 7.8% YoY while import from the U.S. plunged 28.3%. Trade surplus enlarged to US\$ 168.3bn, up US\$ 6.2bn from the same period last year. Vietnam emerged as one of the key beneficiaries of trade diversion, particularly regarding mobile phones and computers exports.
- **Trends that echoed China's economic transition:** 1) export growth of labor-intensive industries has been declining, 2) share of processing trade, of which value added is lower, has been shrinking.

### Data Summary

(US\$ bn)	Jan-19	Feb-19	Mar-19	Apr-19	May-19	Jun-19	Jul-19	YTD
Export	218.0	135.1	197.9	193.5	213.8	212.8	221.5	1392.6
YoY (%)	9.3	-20.8	13.8	-2.7	1.1	-1.3	3.3	0.6
Import	178.8	131.6	165.6	179.7	172.2	161.9	176.5	1166.9
YoY (%)	-1.3	-4.9	-7.8	4.0	-8.5	-7.3	-5.6	-4.5
Trade balance	39.2	3.5	32.3	13.8	41.7	51.0	45.1	225.7

Source: China Customs, CMBIS

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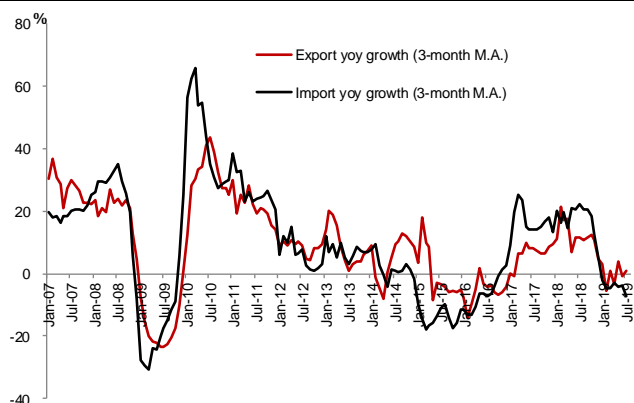
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## Trade surplus rising amid subdued trade activities

**Jul export/import +3.3%/-5.6% YoY, beating expectation.** China Customs released Jul trade figures on 8 Aug. On USD basis, overall import decreased 5.6% YoY in Jul, with rate of decline narrowing 1.7ppt from that in Jun. Overall export increased 3.3% YoY in Jul, reversing 1.3% YoY decline in Jun. Both import and export growth came in better than market anticipation.

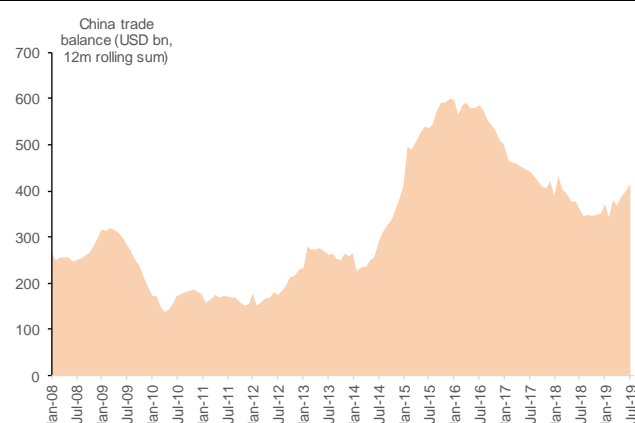
**Trade surplus accumulated while trade subdued.** In the Jan-Jul period, export/import growth was +0.6%/-4.5% YoY, respectively. The fact that export growth, though weak in itself, continued to outpace import growth, boosting YTD trade balance to US\$ 225.7bn, vs. US\$ 162.8bn in the same period last year. Figure 2 below illustrates a clear pattern of trade balance accumulation (on 12-m rolling sum basis) when trade subdued but export outperformed import. This also explains a larger contribution from net export to China's GDP growth in 2H19 (~20%).

**Figure 1: Overall export/import growth**



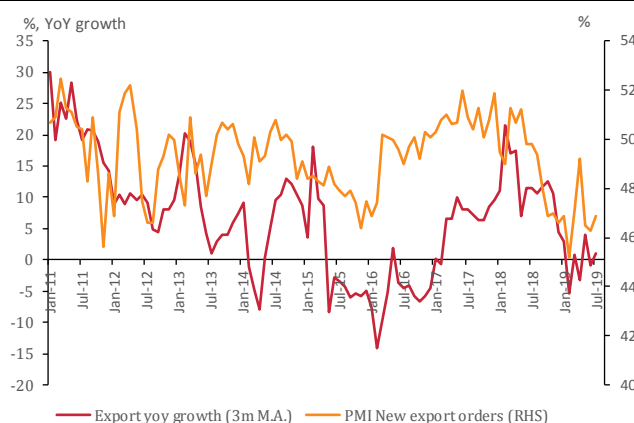
Source: China Customs, Wind, CMBIS

**Figure 2: China trade balance**



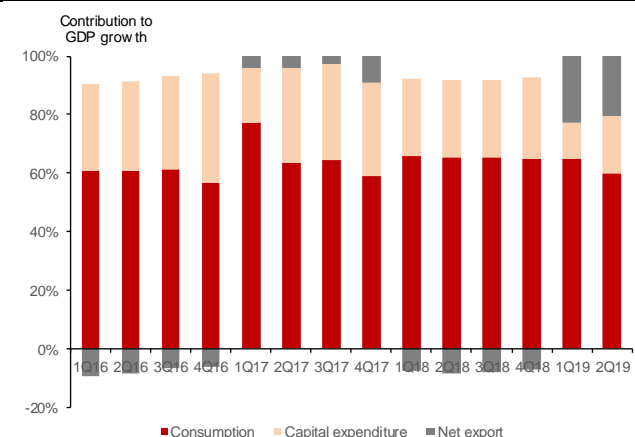
Source: China Customs, Wind, CMBIS

**Figure 3: New export order as a leading indicator for export growth**



Source: China Customs, NBS, Wind, CMBIS

**Figure 4: Net export contributed to ~20% of GDP growth in 1H19**



Source: China Customs, Wind, CMBIS

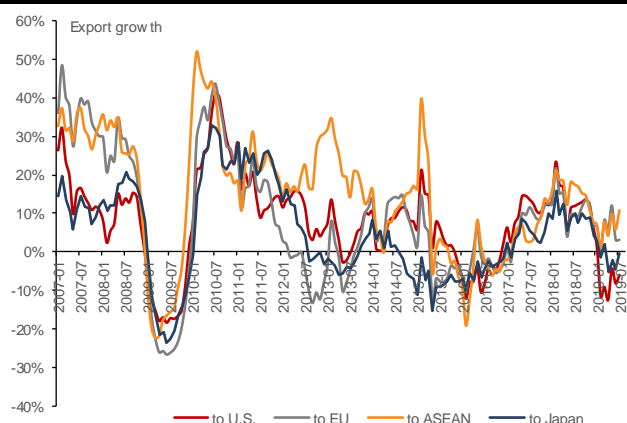
## Wider divergence between key trade partners

The EU, ASEAN countries, U.S. and Japan all together, were destinations of 54% of exports from China and originations of 41% of imports into China in 2018. They contributed to USD 475.6bn trade surplus while total trade balance of China stood at USD 351.8bn in 2018.

**Wider divergence between U.S. and other trade destinations of China.** Trade conflict around the globe, not just that between China and the U.S., is abruptly causing meaningful trade diversion and supply chain relocations toward a new steady state of balance. For China, (1) YTD export to the U.S. declined 7.8% YoY, or net decline of US\$ 20.8bn from the same period last year, while export to EU and ASEAN increased +5.9%/+8.9% YoY, respectively. (2) YTD import from the U.S. plunged 28.3% YoY or net decrease of US\$27.7bn from the same period last year, while import growth from EU/ASEAN/Japan was +2.3%/-0.1%/-7.4%, respectively.

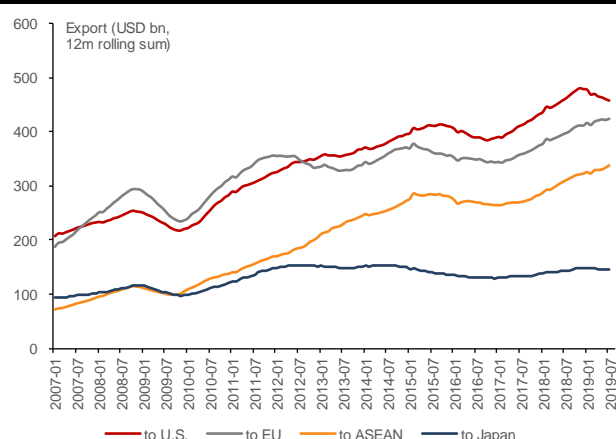
**ASEAN has become China's second largest trading partner, surpassing the U.S.** Trade diversions occur due to escalating trade tensions between China and U.S. As a result, both China's export to ASEAN and import from ASEAN countries speeded up. ASEAN has thus become the second largest trading partner to China, with total trading value of US\$ 345.7bn YTD, second only to EU (US\$ 400.2bn).

Figure 5: Export growth by key regions

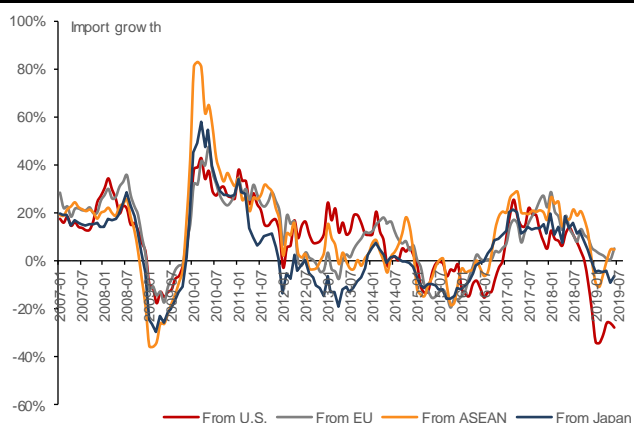


Source: China Customs, Wind, CMBIS

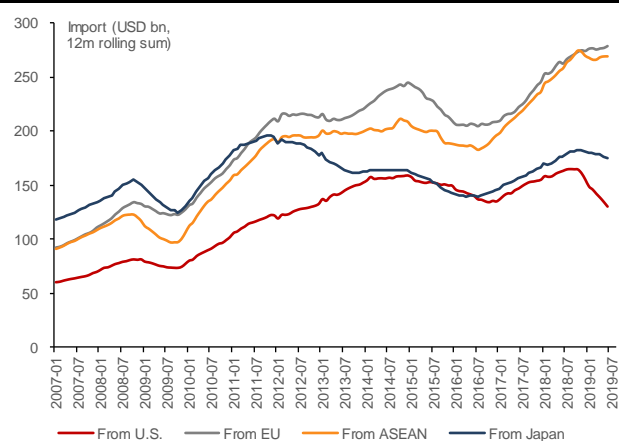
Figure 6: Export to key regions (12m rolling sum)



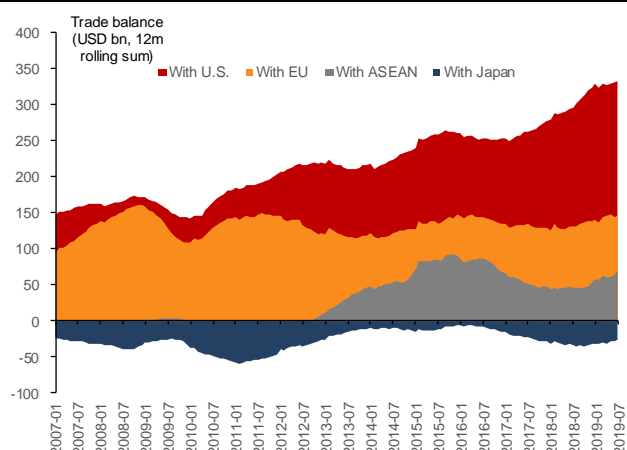
Source: China Customs, Wind, CMBIS

**Figure 7: Import growth by key regions**

Source: China Customs, Wind, CMBIS

**Figure 8: Import from key regions (12m rolling sum)**

Source: China Customs, Wind, CMBIS

**Figure 9: Trade balance with key countries/regions**

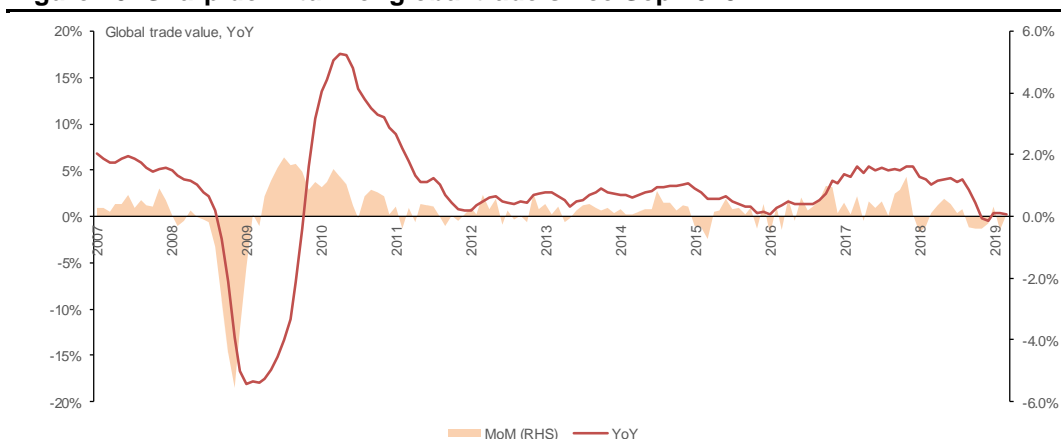
Source: China Customs, Wind, CMBIS

## What explains trade weakness?

### Trade conflict with the U.S, but more importantly, weak domestic demand and slowdown of global economy

Undoubtedly, protracted China-US tensions and back-and-forth in trade negotiations represented major source of disturbance to trade activities. According to our calculation, **U.S. dragged overall export/import growth of China by 1.5ppt/2.3ppt YTD**, respectively, whereas export/import growth rate stood at 0.6%/-4.5% YoY. That being said, even without disturbance from trade fight with the U.S., China would report low-single-digit export growth in Jan-Jul 2019 because of global economic slowdown. Import growth would remain in the negative territory due to weak domestic demand and uncertainties regarding China's economic growth.

Figure 10: Sharp downturn of global trade since Sep 2019

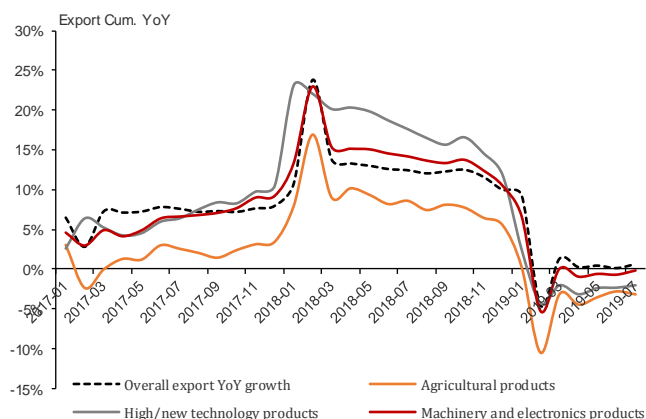


Source: CPB World Trade Monitor, CMBIS

## Trade by major category of goods

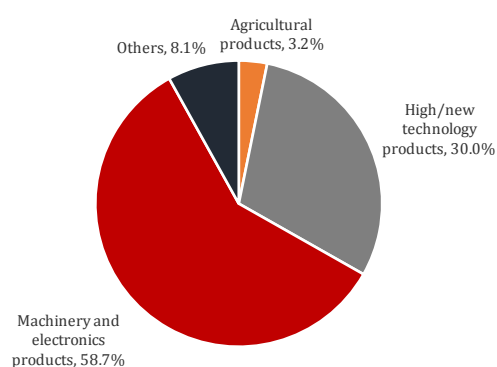
Export of agriculture products and high/new tech products declined 3.1% and 1.9% YoY in the Jan-Jul period, corresponding to net decrease of US\$ 1.4bn/US\$ 7.7bn, respectively. Major products that dragged export growth include, mobile phones and parts (-15.8% or -US\$ 14bn), ships (-23.5%, or -US\$ 3.4bn), automatic data processing equipment (-1.1%, or -US\$ 1bn).

**Figure 11: Export growth by major category of goods**



Source: China Customs, Wind, CMBIS

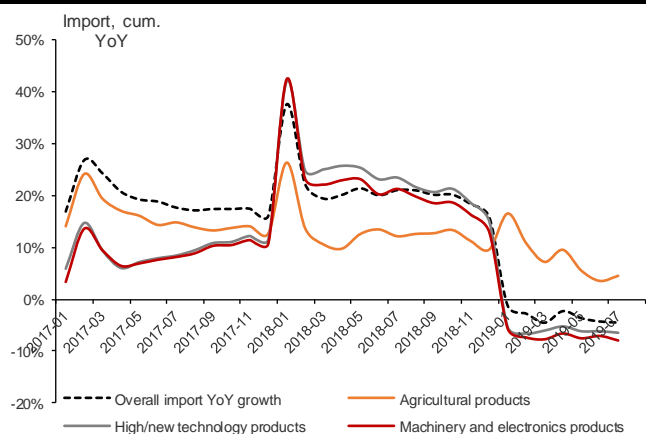
**Figure 12: Breakdown by major exports, 2018**



Source: NBS, Wind CMBIS

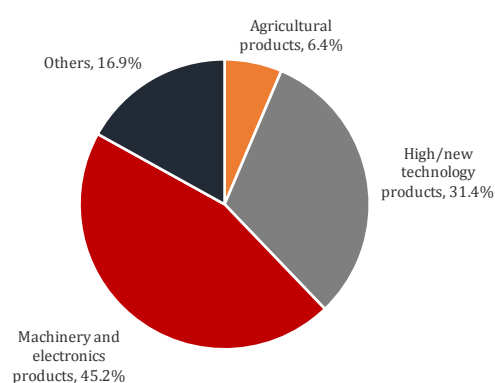
**Import of machinery, electronics, high-tech products plunged.** Import of machinery & electronics products and high/new technology products declined 8.0%/6.6% YoY in Jan-Jul, respectively, or net decrease of US\$ 68bn YoY. Major products that dragged import growth include, semi-conductors (-6.9% or -US\$ 12.2bn YoY), auto and auto parts (-11.6% or -USD 6bn), LCD panel (-18.4% or -US\$ 3bn YoY).

**Figure 13: Import growth by major category of goods**



Source: China Customs, Wind, CMBIS

**Figure 14: Breakdown by major imports, 2018**



Source: NBS, Wind CMBIS

## Trade with the U.S.

In Jan-Jul 2019, China's export to the U.S. declined 7.8% YoY while import from the U.S. plunged 28.3%. Trade surplus enlarged to US\$ 168.3bn, up US\$ 6.2bn from the same period last year.

**Figure 15: Trade with the US – imports plunging faster than exports**

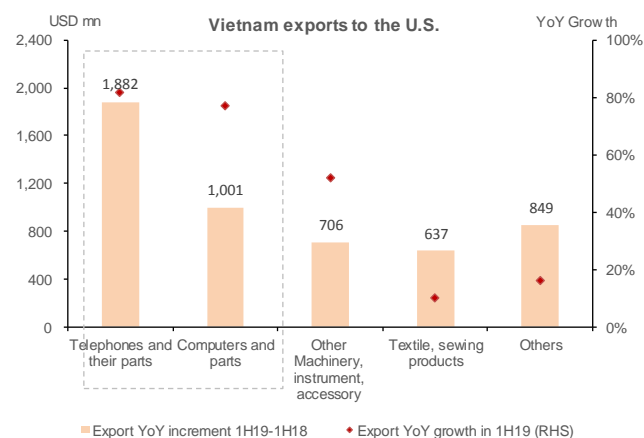


Source: China Customs, Wind, CMBIS

Note: 12-month moving sum plotted

**Vietnam emerging as one of the key beneficiaries of trade diversion.** Vietnam exports to the U.S. increased 27% YoY in 1H19, or by a net of US\$5.1bn. Telephones and parts (up 82% YoY) accounted for 37.1% of the export increments, followed by computers and parts (19.7% share, up 77% YoY), other machinery & instruments (13.9% share, up 52% YoY), textile & sewing products (12.6% share, up 10% YoY). While China's exports of HS85 products (mainly electronic products) decreased US\$ 3.16bn in 1H19 from the same period last year, Vietnam's exports of telephones and computers to the U.S. increased US\$ 2.88bn.

**Figure 16: Vietnam exports to the U.S. of telephones and computers increased US\$2.88bn YoY in 1H19**



Source: General Statistics Office of Vietnam, CMBIS

**Figure 17: Meanwhile, China's exports of HS 85 products decreased US\$ 3.16bn YoY in 1H19**

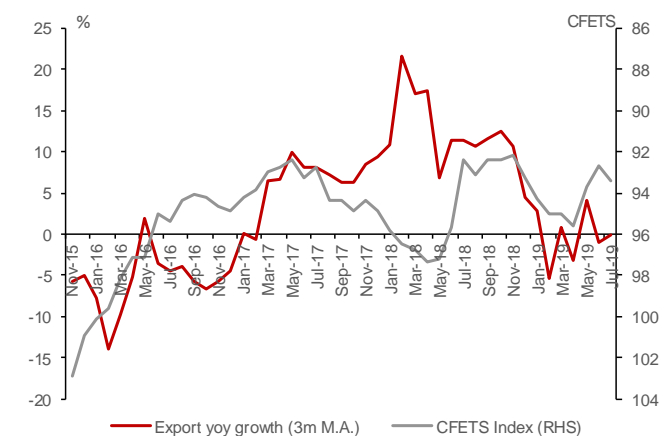


Source: China Customs, Wind CMBIS

## Will RMB depreciation boost China's export?

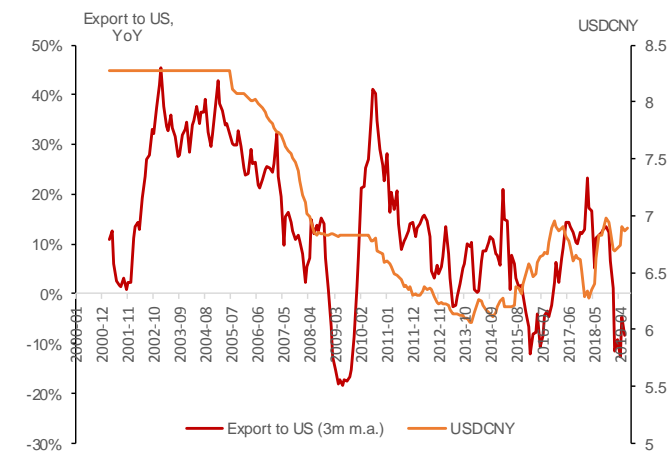
When plotting China's export vs. the value of RMB, we find that overall export growth has been moving more or less in tandem with the CFETS Index (a measure of RMB value against a basket of trade-weighted currencies). However, a weaker RMB does not help much in boosting exports to the U.S. when so many tariff and non-tariff barriers are in place.

**Figure 18: Overall export growth vs. CFETS Index**



Source: China Customs, Bloomberg, CMBIS

**Figure 19: Export growth to the US vs. USDCNY**



Source: China Customs, Bloomberg, CMBIS

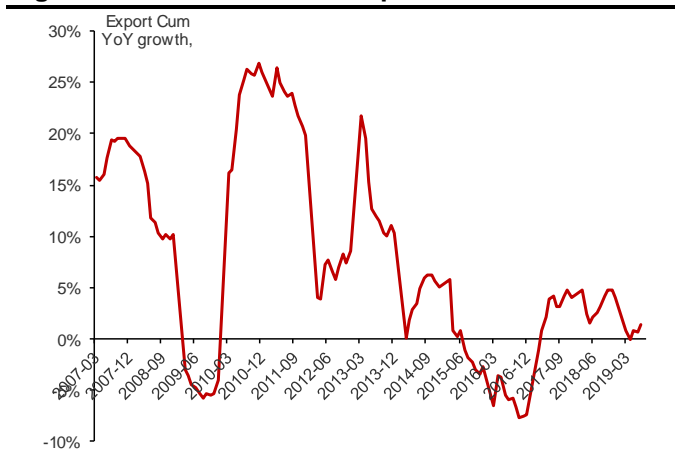


## Changing trade pattern echoes China's economic transition

### 1) Export growth of labor-intensive industries has been declining

Export of labor-intensive industries increased 1.3% YoY in Jan-Jul 2019. Growth rate has been declining since 2017.

**Figure 20: Labor-intensive exports**

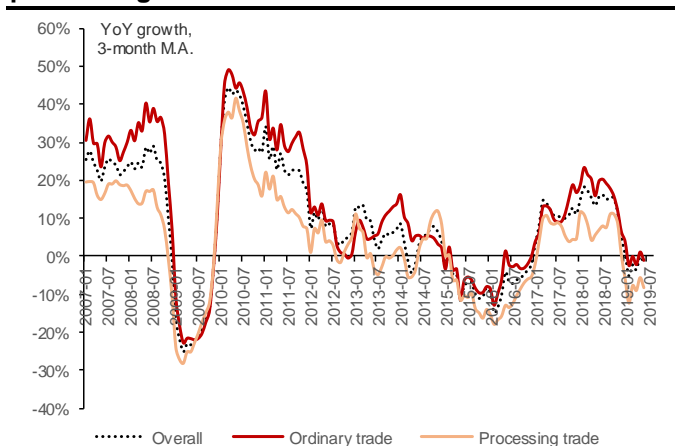


Source: China Customs, Wind, CMBIS

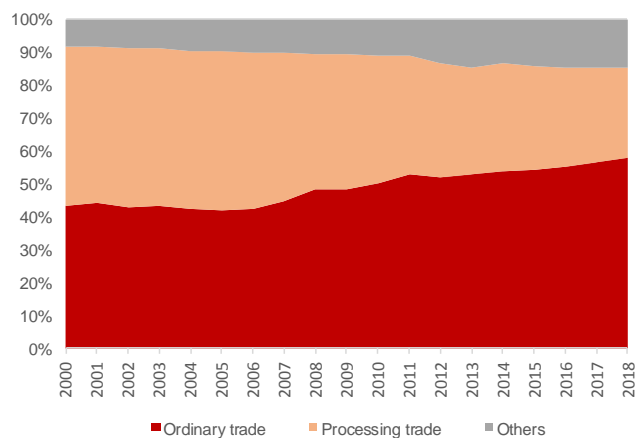
### 2) Share of processing trade is shrinking

Processing trade involves domestic firms importing raw materials or intermediate components from abroad, processing them locally, and exporting the finished value-added goods. Processing trade used to account for 49% of total import and export back in 2000. Now the percentage has declined to 27.4% in 2018. In Jan-Jul 2019, the percentage of processing trade was 25.0%, down 1.6ppt from the same period last year, while that of ordinary trade was 70.7%, up 1ppt. Value added of ordinary trade is approximately 2x that of processing trade.

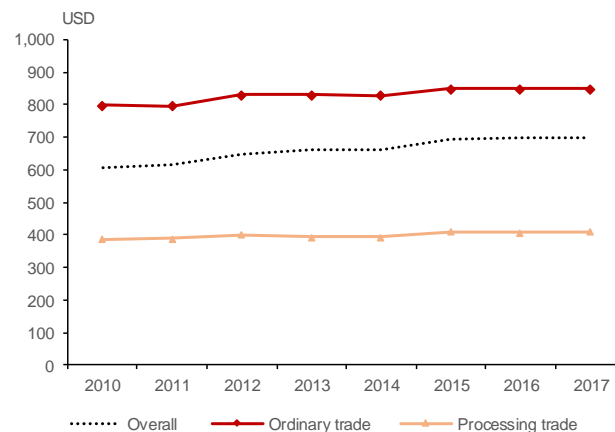
**Figure 21: Growth of ordinary trade outpaced processing trade**



Source: China Customs, Wind, CMBIS

**Figure 22: Ordinary vs. processing trade**

Source: China Customs, Wind, CMBIS

**Figure 23: Value added per USD 1,000 exports**

Source: NBS, Wind, CMBIS

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