

## Economic Analysis

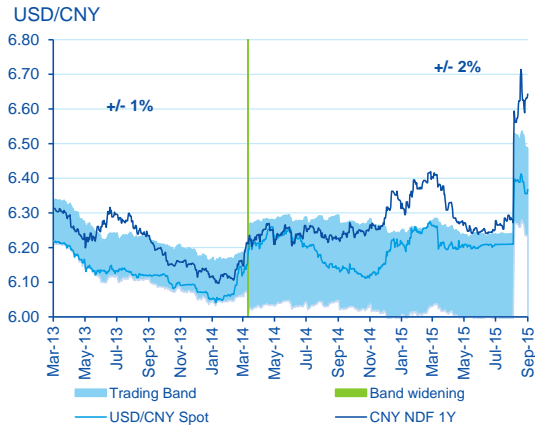
## August trade and foreign reverses data reveal accelerating capital outflows after the unexpected currency devaluation

Le Xia

China's recessionary trade surplus, a widening trade surplus resulting from a mix of weak exports and even weaker imports, continued in August, as reflected in today's announced August trade data. In particular, the year-on-year growth of exports fell short of our expectation despite its low base in the same period of last year, indicating that the unexpected 3% currency devaluation (Figure 1), which was announced on August 11<sup>th</sup>, has failed to boost exports immediately. More importantly, the widening trade surplus, coupled with a significant diminishment of foreign reserves (down by a record USD 93.9 bn in August as reported yesterday), suggest that the authorities have spent an enormous amount of money in stabilizing the market confidence in the exchange rate after their rash move of the currency devaluation. Looking ahead, the authorities are likely to defend the exchange rate at the expense of more reserves loss. We project that China's foreign reserves could decline to USD 3.30 trillion as of the end-year, compared to 3.56 trillion at end-August. In the meantime, the authorities will tighten capital account restrictions and implement more macro-prudential measures to stem capital outflows.

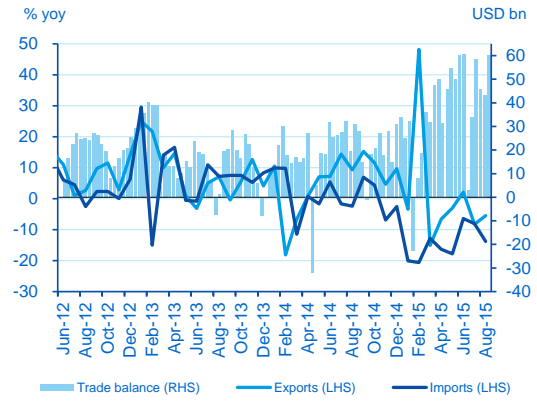
- **Both exports and imports registered remarkable year-on-year declines.** In particular, exports registered a year-on-year decline of -5.5% y/y in August, narrowed from -8.3% y/y in July while below our expectation (BBVA: -3.0% y/y versus consensus: -6.6% y/y). In the meantime, imports slide further by -13.8% y/y, from -8.1% y/y in July (BBVA: -12.0% versus consensus: -7.9% y/y). Accordingly, trade surplus increased to USD 60.24 bn in August compared to USD 43.03 bn in the previous month (Figure 2), well above market expectations (BBVA: USD 62.62 bn versus consensus: USD 48.0 bn).
- **The currency factor continued to weigh on exports.** The Chinese RMB's strength against other major currencies (except for the USD) contributed to the decline in shipments. For example, exports to European countries and Japan were especially weak due to their currency depreciation against the RMB since early this year. Meanwhile, imports were dragged by both weak domestic demand and falling commodity prices. In terms of volume, crude oil, liquefied petroleum gas and copper ore even registered year-on-year growth in August although their import value has dipped significantly.
- **Foreign reserves registered a record decline in August due to accelerating capital outflows.** China's foreign reserves declined by USD 93.9 billion in August, the largest single-month drop in history. (Figure 3) If we use the sum of monthly foreign reserves change and trade surplus as a rough estimate for capital outflows in the month, the August reading shows that the size of capital outflows almost doubled compared to the previous month, mainly due to accelerating capital outflows in response to the unexpected currency devaluation. (Figure 4) Now China's authorities seem to back down from their previous attempt to devalue the currency and increase the exchange rate flexibility. They are now keen to maintain investors' confidence in the RMB exchange rate so as to avert the vicious cycle of currency depreciation and capital outflows. The new goal seems achievable but needs to pay dearly from their pocket of foreign reserves.

**Figure 1**  
**RMB depreciated by 3% after the PBoC announced new fixing price formation mechanism**



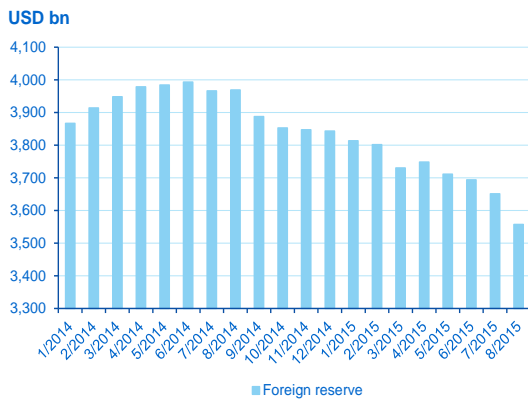
Source: CEIC and BBVA Research

**Figure 2**  
**The sluggish trade data indicated the RMB depreciation has failed to boost exports**



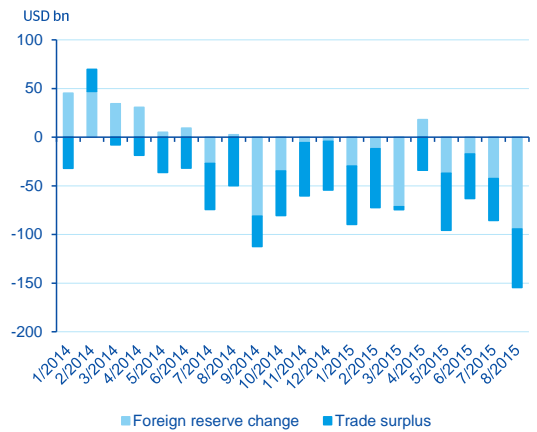
Source: CEIC and BBVA Research

**Figure 3**  
**Foreign reserves declined by USD 93.9 billion in August, the largest single-month drop**



Source: CEIC and BBVA Research

**Figure 4**  
**The size of capital outflows in August almost doubled compared to the previous month**



Source: CEIC and BBVA Research

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