Economic Analysis

Recessionary trade surplus continued through September, helping to offset tension of capital flight

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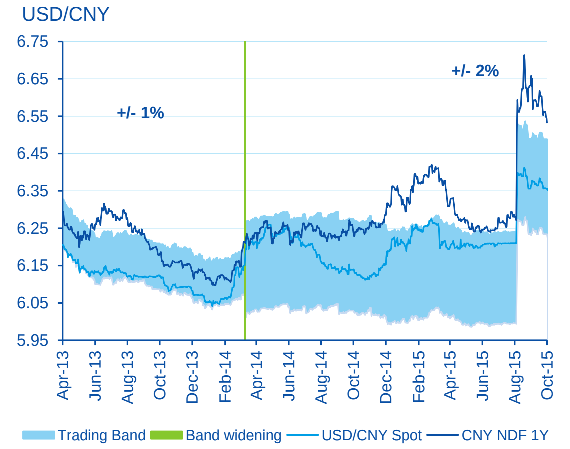
The "recessionary trade surplus", a widening trade surplus resulting from a mix of weak exports and even weaker imports, continued through September, unaffected by recent fluctuations of the RMB exchange rate. September exports registered a year-on-year decline of -4.5% y/y (consensus: -6.0%), marginally narrowed from the August outturn of -5.5% y/y. In the meantime, imports slid further by -20.5% y/y (consensus: 16.0% y/y) from -13.8% y/y in August. As a result, trade surplus maintained at USD 59.15 bn in September, compared to USD 60.24 bn in the previous month (Figure 2). The recessionary trade surplus is due in large part to the sluggish domestic demand, which has not shown any significant improvement despite the authorities' stepped-up easing efforts. Meanwhile, the increasing external uncertainty, in particular surrounding the Fed's monetary policy normalization process, continued to weigh on China's shipments. On the positive side, the trade surplus, albeit mainly resulting from weak imports, has lent a great support to the authorities in their campaign of stabilizing the RMB exchange rate and stemming capital outflows after the August devaluation.

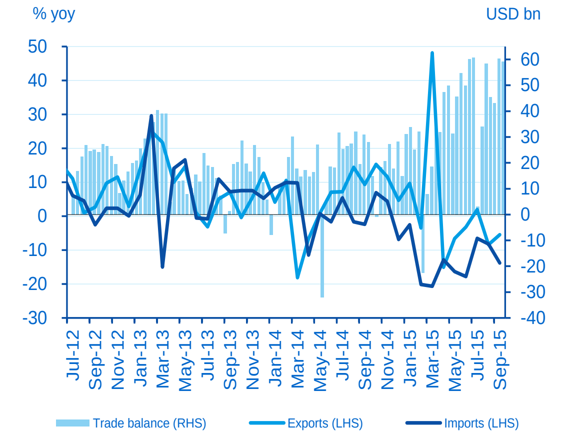
- **Exports were dragged by the processing trade and raw materials, indicating weak external demands**. Several sub-categories of processing trade decreased significantly in September. Such a trend is more related with the demographic change due the strictly enforced "birth control" policy and its resultant upward pressure on labor costs. Theoretically, it is more difficult to boost the process trade by currency depreciation because it will make the import part of the processing trade more expensive. That being said, China cannot count on the RMB depreciation to revive its processing trade. Moreover, raw materials exports, such as coal and precious metals, declined by -26.8% y/y and -67.9% y/y respectively, reflecting the sluggish external demand.
- **The anemic imports were caused by both falling commodity prices and weak domestic demand.** Almost all commodity imports registered significant declines in value, although in terms of volume, crude oil, liquefied petroleum gas and copper ore have registered year-on-year growth increasing. In addition, imports of capital goods, such as LCD panels, automobile chassis and machine tools, significantly dropped in terms of both value and volume, as domestically investment demand remained subdued.
- **A solid trade surplus is important at this juncture.** Like in August, the trade surplus reached a level of around USD 60 bn in September. This could help the authorities to restore the stability of the RMB exchange rate in the aftermath of the unexpected devaluation in August. As capital accelerates to flow out of China over the concern of further currency depreciation, the trade surplus functions to offset the deficit under the capital account and stem the fast decline in foreign reserves. Thanks to the trade surplus, China's foreign reserves still amounted to USD 3514 bn as of end-September, down by USD 43 bn from its end-August level. (Figure 3) The evolution of foreign reserves has been in line with the benign scenario projected in our thematic report (see our recent Economic Watch). (Figure 4)

Figure 1
RMB sharp depreciation in August has not stimulated exports significantly in September



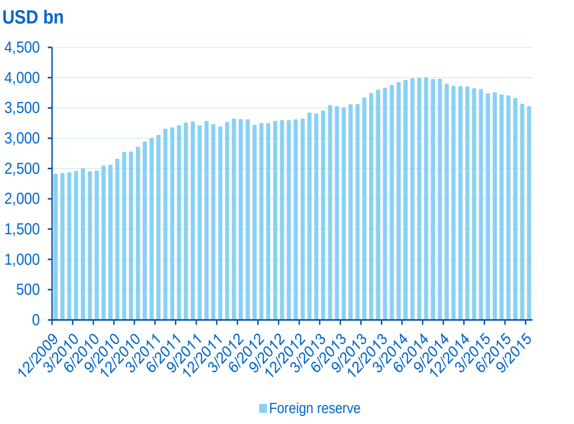
Source: CEIC and BBVA Research

Figure 2
Exports picked up marginally due to the sharp RMB depreciation while imports are still weak



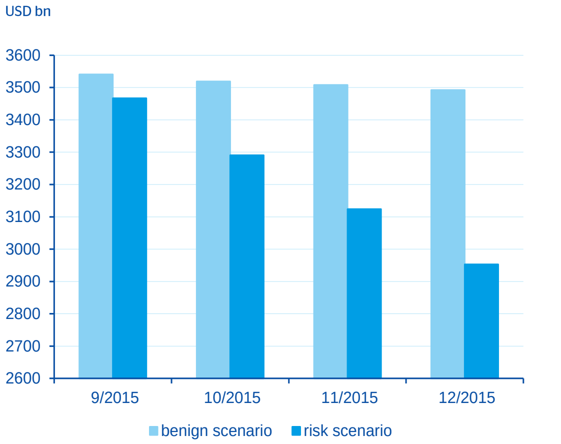
Source: CEIC and BBVA Research

Figure 3
Foreign reserve decreased less than that of the last month, due to the solid trade surplus



Source: CEIC and BBVA Research

Figure 4
The evolution of foreign reserves has been in line with our benign scenario forecasting



Source: CEIC and BBVA Research

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