

China: Trade data hints at weak exports ahead

China's imports for May were very weak. As China's imports are mostly export-order driven, this means that exports in the coming months will be weak as well. The People's Bank of China will not depreciate the yuan to help exports because that won't help



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China imports shrank the fastest since 2016

Imports shrank by 16.7% year-on-year in May, which is the deepest contraction since January 2016 when imports shrank 19.5% YoY.

Though exports shrank only slightly in May (-3.3% YoY), the deep dive of imports means that exports in the coming months will be weak. This is because some imports are used as parts for export products. This also implies foreign buyers did not expect a rebound of demand for their products.

Another reason that exports were less dismal than imports is because of some Covid-19 related shipments, e.g. garments and textiles, which rose 41% month-on-month in May after +64% MoM in April, and medical supplies, which increased 38% MoM in May after +41% MoM in April. Demand for these Covid-19 related goods and supplies should slow down when Covid-19

subsidies. This is also one of the reasons we believe that this less dismal export growth may not be sustainable.

Electronics could be hit hard

In this note, we would like to focus on the trade of electronics as they contribute around half of the total trade of China. Mechanical and electrical products contributed 58% of total exports and 47% of total imports.

Imports in this category fell 7% YoY in May, and this is even after a low base effect from last year, which was -11% YoY in May 2019. In other words, without the base effect, imports of mechanical and electronic parts would have fallen even more in May 2020.

In dollar terms, imports of mechanical and electrical products fell to a very low level of US\$68.11 billion in May. The last time we saw a lower amount was in February 2018 and 2019, which was reasonable as the Chinese New Year fell in those months. Then it was back in May 2017, which recorded US\$66.91 billion for imports in this category, when it was below the current level.

The most important trade item, mechanical and electronic products, has been in bad shape as global demand for upgrades of gadgets has been shrinking.

Remote work arrangements have induced some demand for laptops, pads, and accessories like cameras and microphones, but these are not the major products that have driven strong growth in electronics over the past years. This could change if remote work is the new norm, and could provide a bit of support for electronics for a few years.

But the main growth engine for electronics has come from smartphone upgrades. Before the outbreak of Covid-19 we had expected 2020 to be a boom year for handsets and other gadgets due to 5G. Now, this demand has obviously been deferred by high unemployment in most major economies. As such, demand for electronic parts and equipment for producing advanced technological products should be dismal. Because of the large contribution of mechanical and electronic parts' to global trade, overall exports and imports will be under pressure until global consumption picks up.

Technology war will dampen trade growth

The technology war is once again one of the frictions between the US and China. China claims that it will retaliate against the US action of including 33 Chinese entities to its "entity list" of export controls, which should hurt the transfer of technology.

China's spokesman from the Ministry of Commerce said that China ["will take all necessary measures to safeguard Chinese companies' legitimate rights and interests"](#). If China retaliates with its own unreliable entity list of US companies, likely to include some US technology companies, there will be even less trade of technological parts and products between the US and China.

Hopefully, other economies will fill the gap because otherwise, the technology war will hurt trade in technology parts and products even more, and could last longer.

USD/CNY is not a tool for retaliation

We don't think the People's Bank of China, China's central bank, will use the exchange rate to help exports, or as a tool for retaliation.

Yuan depreciation cannot change the landscape of weak global demand and cannot slow down friction between the US and China. These two are the key problems now faced by Chinese exporters.

The PBoC is expected to allow USD/CNY to move with the dollar index in tandem. This will give some transparency to the market. More importantly, the PBoC is unlikely to shock the market like it did in 2015, which created market chaos, when there are so many uncertainties from Covid-19 and friction between the US and China.

We keep our forecast of USD/CNY for the end of 2020 at 7.05.

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