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Feature: ‘Dual circulation’ strategy becomes new road map to growth in 14th Five-Year Plan

Background

The 19th Central Committee of the Communist Party of China (CPC) concluded its fifth plenary session in Beijing on 29 October. The session discussed and adopted the CPC Central Committee’s proposals for the formulation of the 14th Five-Year Plan (2021-25) for National Economic and Social Development and the Long-Range Objectives Through the Year 2035.

‘Dual circulation’ strategy to guide China’s development over next five years

The ‘dual circulation’ strategy will be one of the key directions of China’s development for the coming years. According to the CPC’s proposal released on 3 November[1], China will speed up the ‘dual circulation’ strategy to guide China’s development in the 14th Five-Year Plan period (2021-25). China will fully utilize resources to empower its domestic economy by stimulating domestic demand and further investing in technology and innovation efforts.

1. China to nurture a strong domestic market

The CPC suggested that ‘domestic circulation’ must be made smoother for an efficient operation of the ‘dual circulation’. China will seek to nurture a strong domestic market and establish a new growth model that focuses on the domestic market as the foothold of growth, according to the proposal.

To this end, China will continue to expand domestic demand by spurring consumption and investment. Together with the deepening of supply-side structural reforms and innovation-driven and high-quality supply, it is hoped that new demand will be created and domestic demand further expanded.

We expect that as China’s growth is increasingly driven by domestic consumption and investment, enterprises will find new avenues for business growth in China, especially in such areas as consumption upgrading, service consumption, e-commerce, and supply chain management.

Through boosting domestic market and enhancing technology self-reliance, China’s growth in the coming years will depend more on the ‘domestic circulation’ and be less impacted by the external environment, such as the global economic downturn and rising protectionism around the world.

[1] http://www.xinhuanet.com/politics/2020-11/03/c_1126693293.htm

2. Tech self-reliance at the top of China's development planning

The CPC proposed 'technological independence and self-reliance as the strategic support for national development'. This is the first time that tech self-reliance was given such a high level of prominence in nation development planning. In addition, China will implement an innovation-driven strategy and put innovation at the centre of its modernization drive.

In our view, the heavy emphasis on tech self-reliance and innovation indicates China is prepared to rely less on foreign technology amid the China–US decoupling trend. China's efforts in technological advancement are gaining urgency amid intensifying US sanctions against Chinese tech companies, including banning major Chinese tech companies from buying US technology and components.

As technology is the key to the next stage of China's development, we expect that detailed policies and huge investments will be announced in areas such as chips, artificial intelligence and 5G technology in the coming months.

Development goals for short and long term

The CPC's proposal also outlines some development goals and suggestions for both the short term and long term:

1. Goals for the 14th Five-Year Plan period (2021-2025)

The CPC has set goals in six areas for the 14th Five-Year Plan:

- High-quality economic growth: China will realize sustained and healthy economic development based on a marked improvement in quality and efficiency, with growth potentials to be fully tapped. The domestic market will become stronger, the economic structure will be further improved, and the innovation capacity will be significantly strengthened. The industrial base will be upgraded, and the industrial chain will be further modernized.
- Deepening reform and opening-up: China will further improve its socialist market economy and build a high-standard market system. Significant progress will be made in the reforms of the property right system and the market-based allocation of production factors, and the development of a fair competition system. China will basically form the new institutions for a higher-level open economy.
- Cultural development: A significant improvement is expected to be made in people's intellectual qualities and moral integrity, cultural and scientific qualities, as well as physical and mental health.
- Environment: China aims to make new progress in building an ecological civilization. It will continue to reduce emissions of pollutants and improve the environment.
- Well-being of the people: The well-being of the people will further improve. China will achieve fuller and higher-quality employment. The country will also see much more equitable access to basic public services.
- Governance: China will further enhance its governance capacity, improve socialist democracy and the rule of law, and demonstrate social fairness and justice. China will also accelerate the modernization of national defence and the military.

The CPC does not set a specific growth target for 2021-25. Instead, it emphasizes 'sustained and healthy economic development' based on 'a marked improvement in quality and efficiency'. This suggests that China prioritizes quality of growth over speed in its economic development in the coming five years.

2. Setting long-term goals for 2035

The CPC also sets a range of long-term objectives for China to achieve by 2035. This is the first time that long-range objectives were raised in a Five-Year Plan. China aims to basically achieve socialist modernization by 2035:

- To significantly increase China's economic and technological strength, and overall national strength. To further develop the national economy and further raise the per capita income of urban and rural residents.
- To make major breakthroughs in core technologies in key areas and become a global leader in innovation.
- To become a modernized economy. To basically achieve new industrialization, IT application, urbanization, and agricultural modernization.
- To build a new pattern of opening-up with deeper participation in international economic cooperation and competition.
- To raise China's per capita GDP to the level of moderately developed countries. To significantly expand the size of the middle-income group.
- Better governance and rule of law, cultural development, improvement in the environment, modernization of national defence and the military, and well-rounded human development for the people were also highlighted.

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The final 14th Five-Year Plan will be approved and published when the National People's Congress, China's top legislature, meets in its annual session next March. Afterwards, follow-up plans for particular industries and each province will be formulated. Businesses should stay tuned to upcoming government announcements and Fung Business Intelligence will be taking a closer look at these plans when they are released.

The CPC sets a range of long-term objectives for China to achieve by 2035, covering economic, technological, political, environmental and social aspects of the country.

Part One: Domestic Trade

A. Recent developments

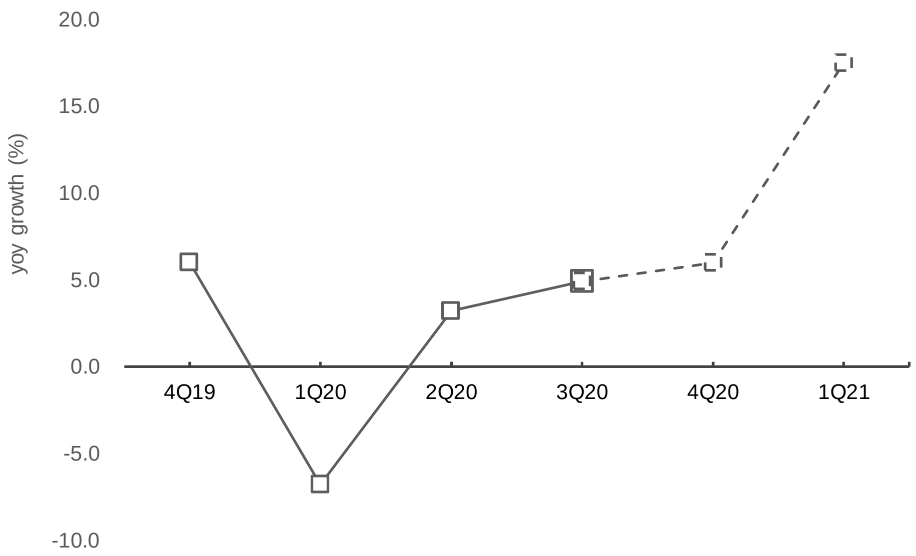
1. China's economy stages V-shaped recovery

China's real GDP growth accelerated from 3.2% year-on-year (yoy) in 2Q20 to 4.9% yoy in 3Q20 *(see exhibit 1)*. Overall, in 1-3Q20, China's nominal GDP amounted to 72.3 trillion yuan, up by 0.7% yoy in real terms.

With China's consumption starting to catch up with the much stronger rebound in production, we predict that China's real GDP growth will rise to 6.0% in 4Q20.

Exhibit 1: China's real GDP growth and forecasts, 4Q19 to 1Q21

FY19	4Q19	1Q20	2Q20	3Q20	4Q20	1Q21
6.1%	6.0%	-6.8%	3.2%	4.9%	6.0%	17.5%



Source: National Bureau of Statistics, PRC

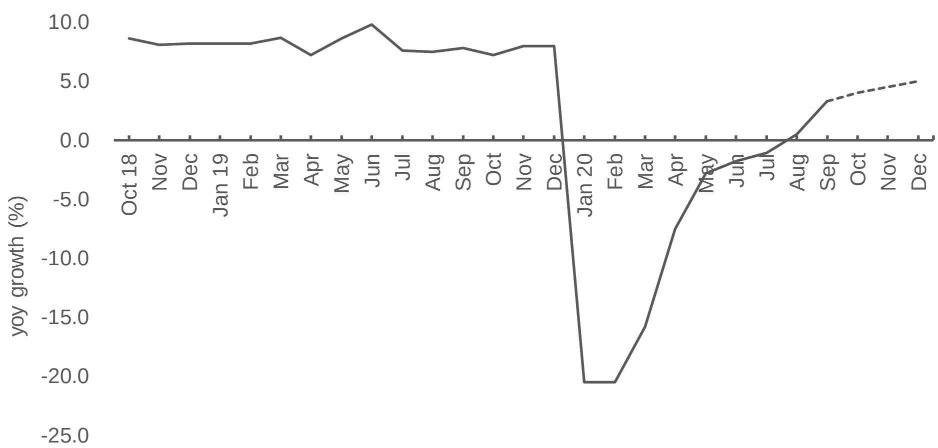
2. Retail sales return to growth in 3Q20

China's total retail sales of consumer goods were up 0.9% yoy in 3Q20, compared with a 3.9% drop in 2Q20. In 1-3Q20, China's total retail sales of consumer goods reached 27.3 trillion yuan, down by 7.2% yoy *(see exhibits 2, 3 and 4)*.

The accelerating pace of rebound in consumer spending in 3Q20 is one of the most encouraging signs of China's economic recovery. Going forward, we predict that the growth in retail sales will further recover to 4.5% yoy in 4Q20.

Exhibit 2: China's total retail sales, year-on-year nominal growth and forecasts, October 2018 to December 2020

FY19	Oct 19	Nov	Dec	Jan-Feb 20	Mar	Apr	May	Jun	Jul	Aug	Sep
8.0%	7.2%	8.0%	8.0%	-20.5%	-15.8%	-7.5%	-2.8%	-1.8%	-1.1%	0.5%	3.3%



Source: National Bureau of Statistics, PRC

Exhibit 3: China's total retail sales, month-on-month nominal growth, April to September 2020

mom growth (%), seasonally adjusted

	Apr 20	**May**	**Jun**	**Jul**	**Aug**	**Sep**
Total retail sales	0.95	0.82	1.38	0.66	1.25	2.25

Source: National Bureau of Statistics, PRC

Impact of the COVID-19 outbreak on different types of consumption was not uniform. While catering services sales plunged amid the threat of COVID-19, online retail sales of goods bucked the trend to post strong growth as people avoided going out and turned to online shopping.

Exhibit 4: China's total retail sales, 2019 to 1-3Q20

Nominal growth, yoy (%)	**FY19**	**1Q20**	**1H20**	**1-3Q20**
Total retail sales	8.0	-19.0	-11.4	-7.2
- Goods	7.9	-15.8	-8.7	-5.1
Sales by enterprises above designated size	3.9	-18.9	-9.0	-4.4
Online sales	19.5	5.9	14.3	**15.3**
- Catering services	9.4	-44.3	-32.8	**-23.9**

Source: National Bureau of Statistics, PRC

Exhibit 5: China's retail sales by enterprises above designated size, by product, 2019 to 1-3Q20

Nominal growth, yoy (%)	**FY19**	**1Q20**	**1H20**	**1-3Q20**
Grain, oil and food	10.2	12.6	12.9	10.6
Beverages	10.4	4.1	10.5	12.3
Tobacco and liquor	7.4	-14.0	-3.1	1.2
Garments, footwear, hats and textiles	2.9	-32.2	-19.6	-12.4
Cosmetics	12.6	-13.2	-0.2	4.5
Gold, silver and jewellery	0.4	-37.7	-23.6	-12.5
Commodities for daily use	13.9	-4.2	5.2	6.8
Home appliances and audio/video equipment	5.6	-29.9	-12.2	-8.0
Traditional Chinese and Western medicines	9.0	2.9	5.8	6.2
Cultural and office appliances	3.3	-3.4	1.6	3.7
Furniture	5.1	-29.3	-14.1	-9.9
Communication appliances	8.5	-3.6	5.8	7.2
Petroleum and related products	1.2	-23.5	-18.4	-16.7
Automobiles	-0.8	-30.3	-15.2	-6.3
Building and decoration materials	2.8	-23.9	-11.0	-7.5

Source: National Bureau of Statistics, PRC

In 1-3Q20, basic consumer staples categories such as 'beverages' and 'grain, oil and food' still managed to post respectable sales growth. Meanwhile, consumer discretionary categories such as 'gold, silver and jewellery' and 'garments, footwear, hats, knitwear' suffered sizeable drop in retail sales.

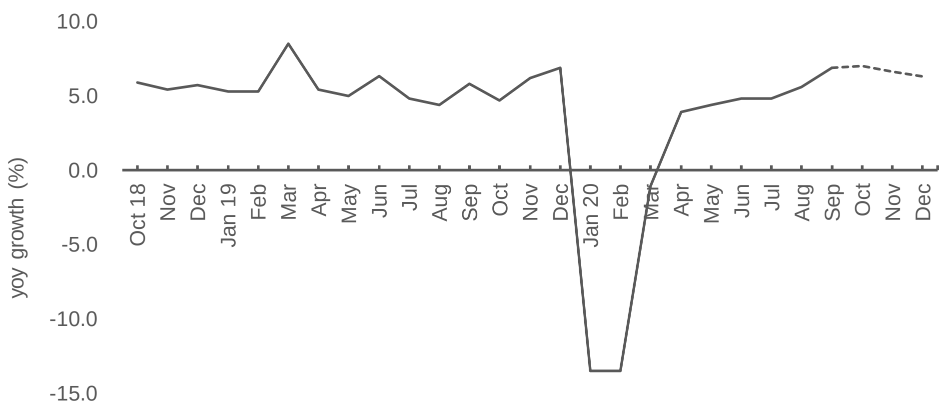
It is noteworthy that retail sales of 'gold, silver and jewellery' and 'automobiles' recorded the fastest recovery in 3Q20.

3. Industrial production back to normal growth in 3Q20

China's industrial production, measured by the value-added of industrial output (VAIO) of industrial enterprises above designated size[2], rose by a better-than-expected 6.9% yoy in September *(see exhibit 6)*. Overall, China's industrial production expanded by 1.2% yoy in 1-3Q20.

Exhibit 6: China's industrial production growth and forecasts, October 2018 to December 2020

Oct 19	**Nov**	**Dec**	**Jan-Feb 20**	**Mar**	**Apr**	**May**	**Jun**	**Jul**	**Aug**	**Sep**
4.7%	6.2%	6.9%	-13.5%	-1.1%	3.9%	4.4%	4.8%	4.8%	5.6%	6.9%



Source: National Bureau of Statistics, PRC

We expect that China's industrial production growth will average 6.6% yoy in 4Q20, as manufacturers continue to benefit from order shifts from alternative production countries. Meanwhile, the government's stimulus measures will help offset the negative impact of the global economic slowdown on China's industrial activities.

[2] 'Industrial enterprises above designated size' refer to industrial enterprises with annual revenue of 20 million yuan or more.

4. Fixed asset investment returns to growth in 3Q20

The nominal growth of China's fixed asset investment (FAI) (excluding rural households) rebounded from minus 3.1% yoy in 1H20 to 0.8% yoy in 1-3Q20. Overall, China's FAI (excluding rural households) amounted to 43.7 trillion yuan in 1-3Q20 *(see exhibit 7)*.

We predict that the growth in China's FAI will continue to pick up in 4Q20, on the back of massive government efforts to increase infrastructure investment, including fiscal boost, monetary easing and pushes from the central government to expedite project approval and construction.

Exhibit 7: China's FAI (excluding rural households) growth, April to September 2020

Year-to-date, yoy growth %	**Apr 20**	**May**	**Jun**	**Jul**	**Aug**	**Sep**
FAI (excluding rural households)	-10.3	-6.3	-3.1	-1.6	-0.3	0.8
- Manufacturing sector	-18.8	-14.8	-11.7	-10.2	-8.1	-6.5
- Infrastructure (excluding power, heat, gas and water infrastructure)	-11.8	-6.3	-2.7	-1.0	-0.3	0.2
- Real estate development	-3.3	-0.3	1.9	3.4	4.6	5.6

Source: National Bureau of Statistics, PRC

5. Fast growth in M2 and total outstanding RMB loans indicates credit easing

Both the broad money supply (M2) and the total outstanding RMB loans have grown at a fast pace recently, indicating an ease in credit conditions in China *(see exhibit 8 & 9)*.

Exhibit 8: Broad money supply (M2) and RMB loans, November 2019 to October 2020

	Broad money supply (M2)		**Total outstanding RMB loans**	
As of	**Amount (trillion yuan)**	**yoy growth**	**Amount (trillion yuan)**	**yoy growth**
End-Nov 19	196.1	8.2%	152.0	12.4%
End-Dec	198.7	8.7%	153.1	12.3%
End-Jan 20	202.3	8.4%	156.5	12.1%
End-Feb	203.1	8.8%	157.4	12.1%
End-Mar	208.1	10.1%	160.2	12.7%
End-Apr	209.4	11.1%	161.9	13.1%
End-May	210.0	11.1%	163.4	13.2%
End-Jun	213.5	11.1%	165.2	13.2%
End-Jul	212.6	10.7%	166.2	13.0%
End-Aug	213.7	10.4%	167.5	13.0%
End-Sep	216.4	10.9%	169.4	13.0%
End-Oct	215.0	10.5%	170.1	12.9%

Source: People's Bank of China

Exhibit 9: Increase in RMB loans, 2019 to October 2020

	Increase in RMB loans (trillion yuan)
FY19	**16.81**
1-3Q20	**16.26**
Nov 19	1.39
Dec	1.14
Jan 20	3.34
Feb	0.91
Mar	2.85
Apr	1.70
May	1.48
Jun	1.81
Jul	0.99
Aug	1.28
Sep	1.63
Oct	0.69

Source: People's Bank of China

China's monetary policy is shifting from broad easing to targeted support, which could be more effective in providing the needed financing for enterprises and supporting the real economy. Refraining from flood-like easing is also aimed to prevent asset speculation caused by excessive liquidity.

Yi Gang, Governor of the People's Bank of China (PBoC), said on 18 October and 21 October that the central bank will pursue a prudent monetary policy that is more flexible, appropriate and targeted while striking a balance between stabilizing growth and forestalling risks. Also, the central bank will focus on giving financing support to small enterprises and private enterprises by providing commercial banks with liquidity and incentives.

6. PMI indicates strong recovery of manufacturing sector

China's manufacturing PMI rose from 51.1 in July to 51.5 in September, and then stayed high at 51.4 in October. The robust headline PMI readings in recent months indicate that the manufacturing sector is continuing its strong recovery from the COVID-induced slowdown. (*see exhibit 10*).

Production activities have expanded at a relatively fast pace in recent months, as shown by the strong output index throughout July to October. The expansion was supported by a fast growth in overall new orders: The new orders index rose from 51.7 in July to 52.8 in October, indicating a quicker pick up in overall market demand lately.

Prices of industrial products have risen: The ex-factory prices index stayed above 52.0 in July to October. The rise in product prices was partly attributed to the surge in the prices of materials: The input prices index went up from 58.1 in July to 58.8 in October, well above the neutral level of 50.

The business expectations index rose from 57.8 in July to 59.3 in October. The index has been well above the critical 50-mark in recent months, indicating that purchasing managers in China have been optimistic about the near-term outlook for their respective industries.

China's manufacturing PMI stays robust at 51.4 in October, indicating that the manufacturing sector continues to recover. Production activities continued to recover at a fast pace. New orders also grew further, indicating a continued improvement in overall demand. Prices of industrial products rose, due partly to the jump in the prices of materials.

Looking ahead, we predict that the manufacturing PMI will fluctuate within 51.0 to 51.5 in the next few months, pointing to a stable recovery of the manufacturing sector and the economy.

Exhibit 10: China's manufacturing PMI at a glance, October 2020

Index	Seasonally adjusted index	Index compared with the previous month	Direction
PMI	51.4	Lower ▼	Expanding
Output	53.9	Lower ▼	Expanding
New Orders	52.8	Unchanged –	Expanding
New Export Orders	51.0	Higher ▲	Expanding
Backlogs of Orders	47.2	Higher ▲	Contracting
Stocks of Finished Goods	44.9	Lower ▼	Contracting
Purchases of Inputs	53.1	Lower ▼	Expanding
Imports	50.8	Higher ▲	Expanding
Input Prices	58.8	Higher ▲	Rising
Ex-factory Prices	53.2	Higher ▲	Rising
Stocks of Major Inputs	48.0	Lower ▼	Contracting
Employment	49.3	Lower ▼	Contracting
Suppliers' Delivery Time	50.6	Lower ▼	Quickening
Business Expectations	59.3	Higher ▲	Optimistic

Source: China Federation of Logistics & Purchasing; National Bureau of Statistics, PRC

7. NMI indicates accelerated recovery in non-manufacturing sector

China's Non-manufacturing Business Activity Index, which is quoted as the Non-manufacturing Purchasing Managers' Index (NMI), rose from 54.2 in July to 56.2 in October (*see exhibit 11*). The index readings indicate that the recovery in the non-manufacturing sector has accelerated.

After rising from 51.5 in July to 54.0 in September, the new orders index retreated to 53.0 in October, indicating a moderation in the growth of new orders.

The sales prices index fell below the critical 50-mark in September and October, meaning that enterprises have lowered their service charges recently. Meanwhile, the input prices index went up from 50.6 in September to 50.9 in October, indicating that input prices have increased at a faster pace recently.

The business expectation index came in at 62.9 in October, well above the critical 50-mark, suggesting that purchasing managers in the non-manufacturing sector have remained optimistic about the near-term outlook for their respective industries.

We expect that China's non-manufacturing sector will sustain its recovering momentum and that the NMI will fluctuate around 55.0 in the next few months.

Exhibit 11: China's Non-manufacturing Purchasing Managers' Index (NMI) at a glance, October 2020

Index	Seasonally adjusted index	Index compared with the previous month	Direction
Business activity	56.2	Higher ▲	Expanding
New orders	53.0	Lower ▼	Expanding
Input prices	50.9	Higher ▲	Rising
Sales prices	49.4	Higher ▲	Falling
Business expectations	62.9	Lower ▼	Optimistic

Source: China Federation of Logistics & Purchasing; National Bureau of Statistics, PRC

B. Policy updates and outlook

1. China to boost new modes of consumption

China aims to prompt the growth of new modes of consumption as a way to boost domestic consumption, which is the more important part of the 'dual circulation' strategy.

On 21 September, the State Council issued a guideline on accelerating the development of new modes of consumption led by new business formats and models, including online shopping, mobile payment, and omni-channel integration.[3] The guideline put forward 15 policies in four areas, including promoting the integration of online and offline consumption, improving infrastructure for new modes of consumption, optimizing the environment for the growth of new modes of consumption, and strengthening policy support for new modes of consumption.

According to the guideline, by 2025, China will have fostered a number of demonstration cities and leading enterprises for new modes of consumption, increased the share of online retail sales of physical goods in the total retail sales of consumer goods, and promoted 'Internet+ services' and other new business formats and models for consumption.

2. China issues work plan to expand domestic demand and promote consumption

The 19 measures could be grouped into four main areas: promotion of online access to offline services, developing new modes of service consumption, upgrading physical goods consumption, and providing more support for enterprises.

On 29 October, the National Development and Reform Commission (NDRC) and 13 other government departments jointly issued the *Work Plan for Expanding Domestic Demand and Promoting Consumption in the Near Future*. The Work Plan outlines 19 measures in four areas, including:

- Promoting the expansion of online sporting events, online education courses and online museums;
- Reviving the restaurant and tourism industries;
- Encouraging new modes of service consumption such as information services.
- Providing community services such as breakfast shops, barbershops, elderly homes and day care centres in districts where such services are lacking;
- Encouraging households to replace their old home appliances with new ones;
- Speeding up the construction of 5G network base stations;
- Helping export companies sell their products to domestic consumers; and
- Providing stronger support for manufacturers, private enterprises, small and micro enterprises and foreign-invested enterprises.

[3] http://www.gov.cn/zhengce/content/2020-09/21/content_5545394.htm

Part Two: Foreign Trade

A. Recent developments

1. Strong export performance in 3Q20 signals recovering external demand

In 1-3Q20, China's exports edged down by 0.8% yoy to US$1,811.4 billion, while China's imports fell by 3.1% yoy to US$1,485.3 billion (*see exhibits 12, 13 and 14*).

The strong recovery of China's exports in 3Q20 signals that external demand is recovering, which bodes well for China's economic recovery in 4Q20.

Exhibit 12: China's quarterly foreign trade data, 4Q19 to 3Q20

	Exports		Imports		Trade Balance
	Amount (USD billion)	*yoy growth*	*Amount (USD billion)*	*yoy growth*	*Amount (USD billion)*
FY19	**2,499.5**	**0.5%**	**2,078.4**	**-2.7%**	**421.1**
4Q19	673.1	1.8%	546.3	3.2%	126.7
1Q20	477.9	-13.4%	464.8	-3.0%	13.1
2Q20	620.8	0.1%	466.2	-9.7%	154.7
3Q20	712.7	**8.8%**	554.4	3.2%	158.3

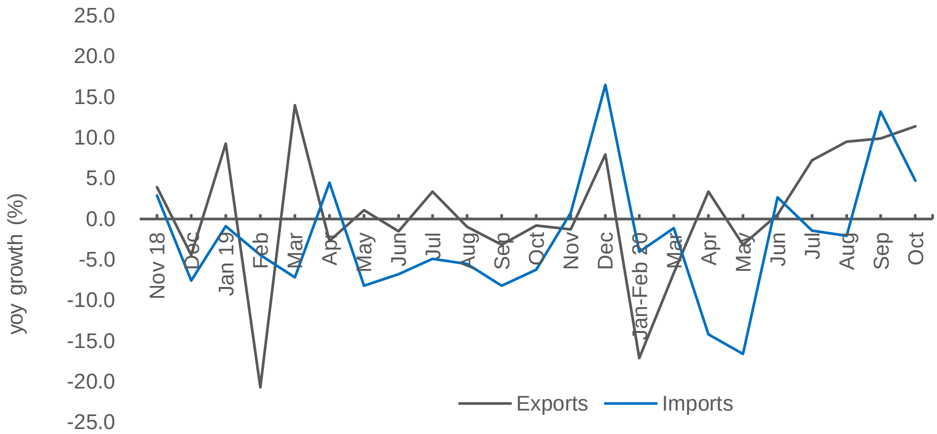
Source: China Customs

Exhibit 13: China's monthly foreign trade data, November 2019 to October 2020

	Exports		Imports		Trade Balance
	Amount (USD billion)	*yoy growth*	*Amount (USD billion)*	*yoy growth*	*Amount (USD billion)*
November 19	221.4	-1.3%	184.3	0.8%	37.2
December	238.6	7.9%	191.4	16.5%	47.2
Jan-Feb 2020	292.8	-17.1%	299.7	-4.0%	-6.9
March	185.1	-6.6%	165.1	-1.1%	20.1
April	200.1	3.4%	154.9	-14.2%	45.2
May	207.5	-3.2%	144.1	-16.6%	63.0
June	213.6	0.5%	167.2	2.7%	46.4
July	237.6	7.2%	175.3	-1.4%	62.3
August	235.3	9.5%	176.3	-2.1%	58.9
September	239.8	9.9%	202.8	13.2%	37.0
October	237.2	11.4%	178.7	4.7%	58.4

Source: China Customs

Exhibit 14: Growth rates of exports and imports, November 2018 to October 2020



Source: China Customs

Exhibit 15: Exports by category, 2019 to 1-3Q20

yoy growth (%) of export value, in USD	**2019**	**1H20**	**1-3Q20**
Textile yarn, fabrics and textile products	0.9	27.8	**33.7**
Garments and clothing accessories	-4.0	-19.4	-10.4
Footwear	1.7	-30.2	-25.3
Toys	24.2	-12.1	-1.9
Furniture and parts	0.8	-11.6	2.3
Lighting fittings and parts	9.6	-6.5	6.3
Suitcases and handbags	0.5	-30.2	-27.2
Refined oil	7.0	-15.1	-28.3
Steel	-11.3	-18.7	-20.4
Mechanical and electrical products	-0.1	-5.5	0.5

Source: China Customs

The strong increase in textile exports in 1-3Q20 was driven by a surge in overseas demand for personal protective equipment such as masks, gloves and isolation suits. With no end in sight to the COVID-19 pandemic, overseas demand for these goods will continue to boost China's exports in the near future.

Exhibit 16: Imports by category, 2019 to 1-3Q20

yoy growth (%) of import value, in USD	**2019**	**1H20**	**1-3Q20**
Soybeans	-7.2	12.7	11.8
Iron ores	33.6	10.2	9.5
Crude oil	0.4	-23.0	**-22.9**
Steel	-14.1	-0.3	18.0
Textile yarn, fabrics and textile products	-12.1	-11.4	-11.4
Vehicles and vehicle chassis	-4.3	-12.1	-17.6
Integrated circuits	-2.1	12.2	13.8
Plastics	-5.5	-9.9	-5.1

Source: China Customs

The drop in China's imports in 1-3Q20 was led by the decrease in the import value of crude oil. However, it should be noted that the decrease was driven by a fall in crude oil prices rather than import quantities: China's import of crude oil totalled 369.0 million metric tons in 1-3Q20, up 12.7% yoy.

2. ASEAN remains China's largest trading partner in 1-3Q20

In 1-3Q20, the ASEAN was still China's largest trading partner and the US also retained its status as China's largest export market (*see exhibits 17 and 18*).

China's exports to certain developing economies such as the ASEAN remained robust in 1-3Q20. We expect that developing economies will continue to be growth spots for China's exports in the near future.

Exhibit 17: China's trading partners, 1-3Q20

Country/Region	Trade value (USD billion)	Share of total trade (%)	Export value (USD billion)	Import value (USD billion)	yoy growth (%) Total trade	Exports	Imports
ASEAN	481.8	14.6	267.1	214.7	5.0	**4.9**	5.1
EU	461.2	14.0	279.5	181.7	0.4	3.1	-3.6
US	401.5	12.1	310.0	91.4	-0.6	-0.8	-0.2
Japan	229.8	7.0	103.4	126.4	-1.1	-2.7	0.3
Brazil	86.5	2.6	23.4	63.1	4.0	-6.3	8.3
Russia	78.8	2.4	35.9	43.0	-2.0	0.1	-3.8
India	60.5	1.8	45.2	15.3	-13.1	-19.7	14.6

Source: China Customs

Exhibit 18: China's trading partners, comparing growth rates for 2019 and 1-3Q20

yoy growth (%)

Country/Region	Total trade		Exports		Imports	
	2019	1-3Q20	2019	1-3Q20	2019	1-3Q20
ASEAN	9.2	5.0	12.7	**4.9**	5.0	5.1
EU	3.4	0.4	4.9	3.1	1.1	-3.6
US	-14.6	-0.6	-12.5	-0.8	-20.9	-0.2
Japan	-3.9	-1.1	-2.6	-2.7	-4.9	0.3
Brazil	3.7	4.0	5.5	-6.3	2.9	8.3
Russia	3.4	-2.0	3.6	0.1	3.2	-3.8
India	-2.8	-13.1	-2.4	-19.7	-4.5	14.6

Source: China Customs

3. Leading export provinces register export drop in 1-3Q20

China's top six provinces and municipalities in terms of value of exports – Guangdong, Jiangsu, Zhejiang, Shandong, Shanghai and Fujian – jointly accounted for 75.9% of China's total exports in January to September 2020, down from 76.5% in 2019 (*see exhibit 19*).

In a somewhat surprising development, exports from Hubei, once hit hard by the COVID-19 outbreak, grew by 13.2% yoy in 1-3Q20.

Several provinces still managed to record double-digit export growth in 1-3Q20. For example, exports from Sichuan, Jiangxi and Yunnan jumped 23.6% yoy, 21.8% yoy and 20.6% yoy respectively in the period.

Exhibit 19: Top six provinces and municipalities in terms of value of exports, January to September 2020

Provinces/ Municipalities	Value of exports (USD billion)	yoy growth (%)	Share of total exports (%)
Guangdong	514.2	-1.2	28.4
Jiangsu	284.4	-5.4	15.7
Zhejiang	249.7	-1.0	13.8
Shandong	127.6	0.6	7.0
Shanghai	120.9	-2.4	6.7
Fujian	77.7	-3.5	4.3

Source: China Customs

4. Surge in FDI in 3Q20 indicates confidence in China's long-term prospects

China's foreign direct investment (FDI) surged by 20.4% yoy in 3Q20, an acceleration from an 8.4% yoy growth in 2Q20. Overall, in 1-3Q20, China's FDI amounted to 718.8 billion yuan, up by 5.2% yoy (*see exhibit 20*).

The rise in FDI into China indicates foreign investors' confidence in China's long-term prospects, despite the global economic downturn and all the talk of China—US decoupling.

China is witnessing a new trend in foreign investment activities, with FDI in China's high-tech service sector soaring by 26.4% yoy in 1-3Q20.

Exhibit 20: China's FDI, October 2019 to September 2020

	Amount (billion yuan)	yoy growth
FY19	**941.5**	**5.8%**
1-3Q 2020	**718.8**	**5.2%**
October 19	69.2	7.4%
November	93.5	1.5%
December	95.5	3.5%
January 20	87.6	4.0%
February	46.8	-25.6%
March	81.8	-14.1%
April	70.4	11.8%
May	68.6	7.5%
June	117.0	7.1%
July	63.5	15.8%
August	84.3	18.7%
September	99.0	25.1%

Source: Ministry of Commerce, PRC

5. Chinese yuan appreciates against US dollar over past three months

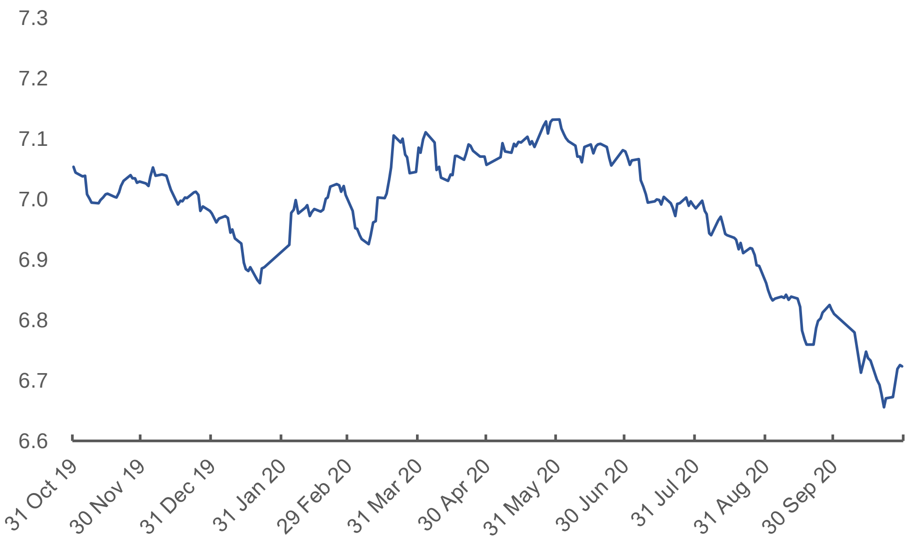
The daily fixing rate (also known as the central parity rate) of the Chinese yuan against the US dollar appreciated from 6.9848 on 31 July to 6.7232 on 30 October (*see exhibit 21*).[4] So far this year, the daily fixing rate of the Chinese yuan had appreciated by 3.8% (as of 30 October) against the US dollar.

Meanwhile, the daily fixing rate of the Chinese yuan against the Euro appreciated from a recent low of 8.2882 on 31 July to 7.8463 on 30 October. So far this year, the daily fixing rate of the Chinese yuan had depreciated by 0.4% (as of 30 October) against the Euro (*see exhibit 22*).

According to the Bank for International Settlements, the Chinese yuan appreciated in real terms against its trading partners by 2.2% in 1-3Q20 (*see exhibit 23*).

Looking ahead, we predict that the exchange rate of the Chinese yuan against the US dollar will fluctuate around the current levels in the near term. While China-US tensions could add volatility to Chinese yuan's exchange rate, China's strong economic recovery, a weak US dollar, and the large interest-rate differential between China and developed economies will continue to support the Chinese yuan.

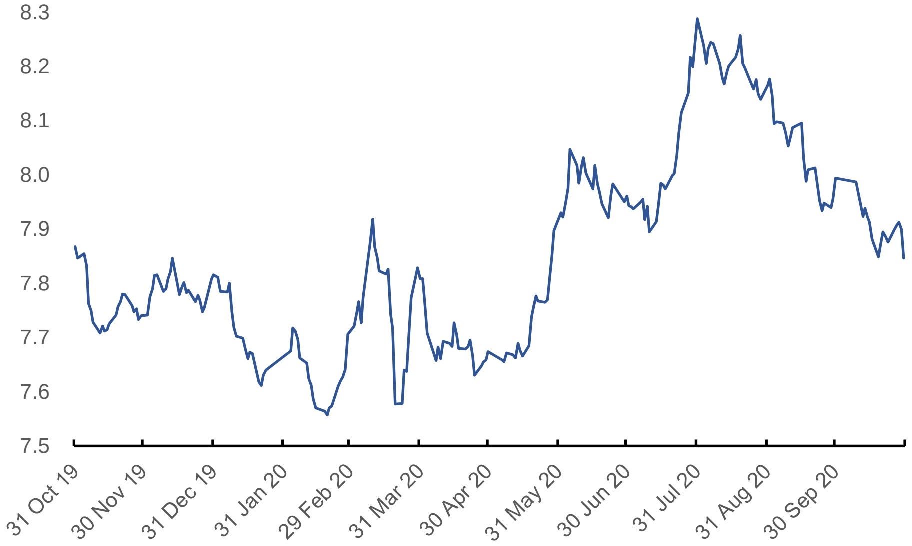
Exhibit 21: USD-CNY daily fixing rate, October 2019 to October 2020



Source: State Administration of Foreign Exchange

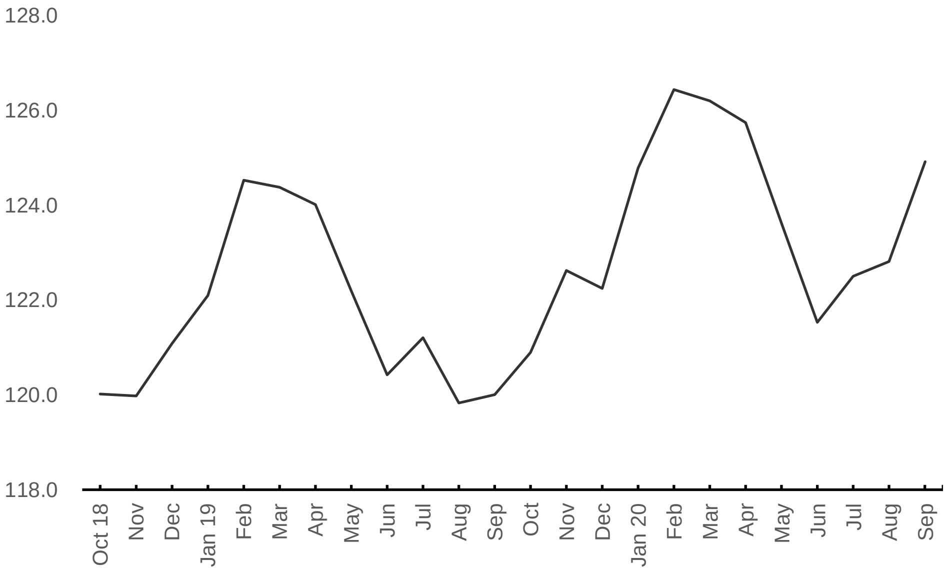
[4] According to the PBOC, the daily fixing rate of the Chinese yuan against the US dollar is directly formed by market makers based on the closing rate of the previous day, the movements of major international currencies, and 'counter cyclical factor', which has been gradually phased out since October this year.

Exhibit 22: EUR-CNY daily fixing rate, October 2019 to October 2020



Source: State Administration of Foreign Exchange

Exhibit 23: Real effective exchange rate of the Chinese yuan, October 2018 to September 2020



Source: Bank for International Settlements

B. Highlights

1. China policy of the US likely to be more pragmatic under a Biden administration

Democratic candidate Joe Biden is projected to win 306 Electoral College votes (out of 538) in the US presidential election, crossing the threshold for victory, based on the votes reported as of 1:00 am on 12 November (US Eastern time).[5]

Biden pledged a tough stance against China on trade, but he is harshly critical of Trump's approach to China. Biden said that while China should be held accountable for its 'unfair trade practices' and he would 'take aggressive trade enforcement actions against China', Trump has mismanaged the response. Rather than engaging a 'go-it-alone' trade war, Biden said he would form a united front with allies to bring multilateral pressure on China to tackle the trade issues.

Biden also criticized Trump's tariff war and the 'Phase One trade deal' with China as harmful to US consumers and farmers. He said he would re-evaluate the additional tariffs on Chinese products upon taking office. However, he has not indicated whether he would keep or abandon the 'Phase One Trade Deal' with China.

Biden also condemned Trump administration as weak towards perceived human rights issues in China. Biden said he would sanction Chinese officials responsible for 'human rights abuses' in Tibet and step up support for the Tibetan people.

Biden's campaign advisers said a Biden administration would prioritize domestic issues over international matters like trade. Thus, China policy is likely to take a back seat to domestic issues as policy focus of the US. The China policy under a Biden administration is also likely to be more pragmatic, and there would be more cooperation in areas like public health and climate change.

Although some changes in the US's China policy are expected under a Biden presidency, a fundamental U-turn in China-US relations is still doubtful, and we do not expect China-US tensions to ease significantly.

2. China-US tech war heats up

The Trump administration is considering restrictions on China's Ant Group and Tencent over 'national security threats' posted by their digital payment platforms, Alipay and WeChat Pay respectively, according to a Bloomberg report dated 7 October.

The US government has been taking separate action against Tencent's WeChat app which would prohibit Apple and Google from offering WeChat for download in US app stores, but a US federal court temporarily halted the ban.

The floating of new potential sanctions against Chinese tech companies suggests that the China-US tech war is unlikely to abate any time soon.

[5] For a more complete analysis of Biden's policy stance on China, see "What would a Biden presidency mean for China and trade?", Fung Business Intelligence, 9 November 2020. https://www.fbicgroup.com/sites/default/files/What%20would%20a%20Biden%20presidency%20mean%20for%20China%20and%20trade.pdf

3. Chinese government to further stabilize foreign trade and foreign investment

The State Council released *Opinions on Further Stabilizing Foreign Trade and Foreign Investment* on 12 August and proposed 15 policy measures,[6] including:

- Promoting the use of export credit insurance to protect enterprises against non-payment risks and provide financing for them;
- Encouraging the development of innovative business models for trade such as market procurement and trading;
- Expanding online channels of foreign trade, and local governments and key industry associations are encouraged to hold online exhibitions; and
- Providing fiscal and financial support for foreign trade enterprises and foreign-invested enterprises, such as tax cuts, expedited rebate of export taxes, and easier financing.

The circular represents another effort of the Chinese government to alleviate the woes of foreign trade enterprises and foreign-invested enterprises, as well as to keep growth on track as the pandemic sees no sign of abating overseas.

6 http://www.gov.cn/zhengce/content/2020-08/12/content_5534361.htm

C. Outlook

1. US and Eurozone record smaller contraction in 3Q20

The US real GDP contracted by 2.9% yoy in 3Q20, marking an improvement from minus 9.0% yoy in 2Q20 (*see exhibit 24*). Meanwhile, the Eurozone economy[7] contracted by 4.3% yoy in 3Q20, up from a 14.8% yoy drop in 3Q20 (*see exhibit 25*).

As the number of new COVID-19 cases has surged to record high levels in the US and the EU in recent weeks, we expect that both the US and Eurozone economies will continue to post year-on-year contraction in 4Q20.

Exhibit 24: US real GDP growth, 2018 to 3Q20

	2018	2019	4Q19	1Q20	2Q20	3Q20
Real GDP *(annual growth[8] %)*			2.4	-5.0	-31.4	33.1
Real GDP *(yoy growth %)*	3.0	2.2	2.3	0.3	-9.0	-2.9

Source: US Department of Commerce

Exhibit 25: Eurozone's real GDP growth, 2018 to 3Q20

	2018	2019	4Q19	1Q20	2Q20	3Q20
Real GDP *(qoq growth %)*			0.0	-3.7	-11.8	12.7
Real GDP *(yoy growth %)*	1.9	1.3	1.0	-3.3	-14.8	-4.3

Source: Eurostat, IMF

[7] The member countries of the Eurozone include Austria, Belgium, Cyprus, Estonia, Finland, France, Germany, Greece, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, the Netherlands, Portugal, Slovakia, Slovenia and Spain.
[8] The 'annual growth rates' of the US GDP are the annualized rates of quarterly GDP growth.

2. IMF projects less severe contraction for world economy

In the *World Economic Outlook* released in October, the IMF forecast that the global economy will contract by 4.4% in 2020, up from a 4.9% drop predicted in June. As such, the global economy will experience a less severe recession than previously expected (*see exhibit 26*).

Despite weak global economic outlook in the near term, we forecast that China's exports will post single-digit year-on-year growth in 4Q20, due mainly to production disruptions in alternative production countries.

Exhibit 26: Latest GDP growth estimates and forecasts by the IMF (2019 to 2021)

yoy growth (%)

	2019 (Estimates)	2020 (Forecasts)	2021 (Forecasts)
World economy	2.8	-4.4	5.2
Advanced economies	1.7	-5.8	3.9
- US	2.2	-4.3	3.1
- Eurozone	1.3	-8.3	5.2
- Japan	0.7	-5.3	2.3
Emerging market and developing economies	3.7	-3.3	6.0
- China	6.1	1.9	8.2
- India*	4.2	-10.3	8.8
- Brazil	1.1	-5.8	2.8
- Russia	1.3	-4.1	2.8
- ASEAN-5[9]	4.9	-3.4	6.2

** Data and forecasts are presented on a fiscal year basis.*
Source: World Economic Outlook released in October 2020, IMF

[9] ASEAN-5 refers to Indonesia, Malaysia, Philippines, Thailand and Vietnam.

Fung Business Intelligence

Fung Business Intelligence collects, analyses and interprets global market data on sourcing, supply chains, distribution, retail and technology.

Headquartered in Hong Kong, it leverages unique relationships and information networks to monitor, research and report on these global issues with a particular focus on business trends and developments in China. Fung Business Intelligence makes its data, impartial analysis and specialist knowledge available to businesses, scholars and governments through regular research reports and business publications.

As the knowledge bank and think tank for the Fung Group, a Hong Kong-based multinational corporation, Fung Business Intelligence also provides expertise, advice and consulting services to the Group and its business partners on issues related to doing business in China, ranging from market entry and company structure, to tax, licensing and other regulatory matters.

Fung Business Intelligence was established in the year 2000.

Fung Group

Fung Holdings (1937) Limited, a privately-held business entity headquartered in Hong Kong, is the major shareholder of the Fung Group of companies, whose core businesses operate across the entire global supply chain for consumer goods including sourcing, logistics, distribution and retail. The Fung Group comprises over 34,000 people working in more than 40 economies worldwide. We have a rich history and heritage in export trading and global supply chain management that dates back to 1906 and traces the story of how Hong Kong and the Pearl River Delta emerged as one of the world's foremost manufacturing and trading regions. We are focused on both creating the Supply Chain of the Future to help brands and retailers navigate the digital economy as well as creating new opportunities, product categories and market expansion for brands on a global scale.

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