



# CHINA ECONOMICS WEEKLY

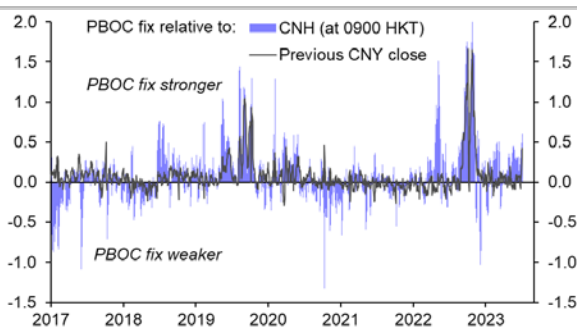
## Export curbs will become blunt with use

### Stronger RMB by year-end

The PBOC's Q2 Monetary Policy Report, published last Friday, included new language pledging to "prevent large fluctuations in the exchange rate". Then, with the renminbi approaching 7.3/\$ at the start of this week, the PBOC pushed back more firmly. It set its daily fixes for the onshore exchange rate notably stronger than both the offshore CNH rate and the previous day's USD/CNY close. There were rumours of intervention by state banks.

These efforts have slowed the renminbi's slide for now and, compared to last October, when the 7.3/\$ line was last threatened, the PBOC has not had to work particularly hard. (See Chart 1.)

Chart 1: Move in CNY fix set by PBOC (% , 7d ave.)



Sources: CEIC, Refinitiv, Capital Economics

Looking ahead, further disappointing data from China or further dollar strength could soon weaken the renminbi again. Conversely though, with sentiment so depressed it wouldn't take much to generate some upside surprises – the upcoming Q2 GDP data could be one trigger, given how flattering the base will be. And if we're right in our expectation that US yields will drop later in the year, that important driver of recent renminbi weakness will reverse. We still [expect](#) the renminbi to have passed back through 7 by the end of the year.

### Periodic restrictions

The gallium and germanium export controls announced by China's commerce ministry this week appear to be retaliation for curbs imposed by the US and some allies on China's ability to source

technology and tools needed by the chip industry. Both metals can be used as inputs for semiconductors and feature on US government and European Commission lists of "critical" minerals. Development of gallium nitride semiconductors is a target in China's [Five-Year Plan](#).

The move leverages China's one area of dominance in the semiconductor supply chain: mining and refining of critical minerals. 94% of the world's gallium and 83% of germanium are currently sourced from China. Tightly-applied export controls would cause significant disruption, and one official suggested they are "just the start". Over the medium term though, such restrictions would give other countries incentives to develop alternative sources of supply. Gallium and germanium are produced as byproducts in refining other commodities. In principle, they could be made in many other places. Germany, for example, produces small amounts of germanium (France, sadly, does not make gallium).

The clearest pre-cursor to this week's export curbs is the restriction that China put on rare earth shipments to Japan in 2010. Even though that curb wasn't in place for long, it spurred [successful efforts](#) by Japan to find suppliers outside China: they now supply half of Japan's rare earths, from 2% in 2010. Indeed, for minerals like these, for which supply outside China is only constrained in the near-term, China's strategic interests may be better served by trying to hold on to its position as the world's dominant supplier. It wouldn't be a surprise if these restrictions – which require exporters to apply for export licenses – end up being little used.

US restrictions also give Chinese chip firms strong incentives to reduce their dependence on Western suppliers. But that's a harder task given the technical complexity of chipmaking and the breadth of [Western dominance](#) in the sector.

### The week ahead

The key upcoming release is of June's export data on Thursday. Risks are all on the downside.

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## Data Previews

### Net New Bank Loans, M2, AFRE (Jun.)

9<sup>th</sup> – 15<sup>th</sup> Jul.

Forecasts	Time (China)	Previous	Consensus	Capital Economics
Net New Bank Loans (RMB)	-	+1,363bn	+2,300bn	+1,900bn
M2 (% y/y)	-	(+11.6%)	(+11.2%)	(+11.4%)
Aggregate Financing “AFRE” (RMB)	-	+1,560bn	+3,000bn	+2,600bn

#### Weak demand holding back credit growth

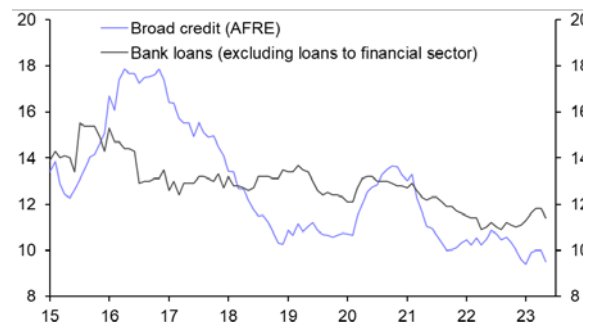
Broad credit growth slowed sharply in May, reversing all of the post-zero-COVID rebound. (See Chart 2.) We expect it to have decelerated further in June, adding to the headwinds to the economy in the second half of the year.

Government bond issuance has slowed as the boost from the front-loading of fiscal borrowing has faded. Mortgage demand has weakened too – home sales are on a downward trajectory again after a brief recovery at the beginning of the year. And a PBOC quarterly survey last week confirmed that broader loan demand is **subdued** – the survey suggested that demand is barely higher than during the worst of the zero-COVID disruption.

The LPR cut on 20<sup>th</sup> June came too late in the month to have made much difference to the monthly data.

But with loan demand depressed, much more than a 10bp would be needed anyway.

Chart 2: Broad Credit & Bank Loans (outstanding, % y/y)



Sources: CEIC, Capital Economics

### CPI, PPI (Jun.)

Mon. 10<sup>th</sup> Jul.

Forecasts	Time (China)	Previous	Consensus	Capital Economics
CPI (% y/y)	09.30	(+0.2%)	(+0.2%)	(+0.2%)
PPI (% y/y)	09.30	(-4.6%)	(-5.0%)	(-5.0%)

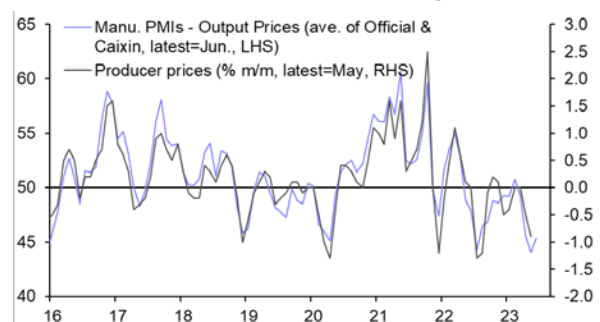
#### Price pressures probably stay subdued

Factory-gate deflation hit a seven-year low in May, and we think it will have deepened further in June. This could be attributed, in part, to a higher base for comparison, as global commodity prices were surging a year ago following Russia’s invasion of Ukraine. But commodity prices have continued to drop back in recent weeks, and the manufacturing PMIs suggest that output prices continue to fall at a reasonably fast rate. (See Chart 3.)

CPI inflation edged up in May from a two-year low. High frequency data suggest that the headline rate won’t have changed much in June. Core inflation will probably have stayed subdued as the impact of reopening has fizzled out. A rise in food inflation is

likely to have been offset by a continued decline in energy inflation.

Chart 3: Producer Prices & PMI Output Prices



Sources: CEIC, S&P Global, Capital Economics



### Trade (Jun.)

Thu. 13<sup>th</sup> Jul.

Forecasts	Time (China)	Previous	Consensus	Capital Economics
Exports (USD, % y/y)	-	(-7.5%)	(-9.5%)	(-10.0%)
Imports (USD, % y/y)	-	(-4.5%)	(-4.7%)	(-3.5%)
Trade Balance (USD)	-	+66bn	+74bn	+50bn

#### *Exports probably fell again while the contraction in imports narrowed*

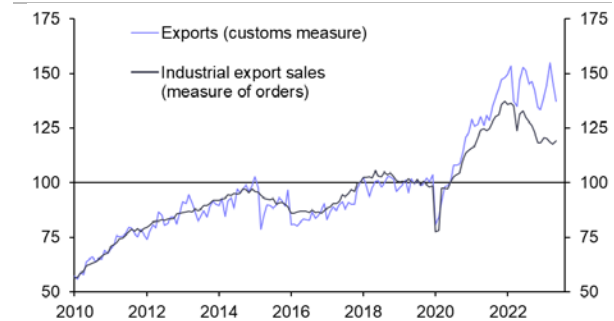
Export values contracted year-on-year in May for the first time in three months. More importantly, they declined a hefty 6.4% m/m in seasonally-adjusted m/m terms – almost completely reversing the rise in exports in the two preceding months.

That still leaves exports looking strong. Despite sizeable swings since the start of last year, they are still well above both their pre-pandemic level and trend. Other countries in the region have seen shipments drop back. China’s own industrial firms have reported a sizeable drop-off in orders. (See Chart 4.) And exports orders on the PMIs have been consistent with exports falling for most of the past year.

In contrast, the contraction in import values narrowed in May and they rose 6.8% in seasonally-adjusted m/m terms, as the reopening recovery in

passenger travel boosted fuel imports. We expect more of the same in June, with fuel imports continuing to be supported by the recovery in international travel to and from China.

**Chart 4: Exports & Industrial Export Sales**  
(\$, 2019=100, CE seas. adj.)



Sources: CEIC, Capital Economics



# Economic Diary & Forecasts

## Upcoming Events and Data Releases

Date	Country	Release/Indicator/Event	Time (China)	Previous*	Median*	CE Forecasts*
<b>July</b>						
Mon 10 <sup>th</sup>		<b>Chn</b> Consumer Prices (Jun.)	(09.30)	(+0.2%)	(+0.2%)	(+0.2%)
		<b>Chn</b> Producer Prices (Jun.)	(09.30)	(-4.6%)	(-5.0%)	(-5.0%)
Thu 13 <sup>th</sup>		<b>Chn</b> Exports (Jun., USD)	-	(-7.5%)	(-9.5%)	(-10.0%)
		<b>Chn</b> Imports (Jun., USD)	-	(-4.5%)	(-4.7%)	(-3.5%)
		<b>Chn</b> Trade Balance (Jun., USD)	-	+65.8b	+74.4b	+50.0b
Also expected during this period:						
9 <sup>th</sup> – 15 <sup>th</sup>		<b>Chn</b> M2 Money Supply (Jun., RMB)	-	(+11.6%)	(+11.2%)	(+11.4%)
		<b>Chn</b> Net New Lending (Jun., RMB)	-	+1363b	+2300b	+1900b
10 <sup>th</sup> – 15 <sup>th</sup>		<b>Chn</b> Aggregate Financing “AFRE” (Jun., RMB)	-	+1560b	+3000b	+2600b
11 <sup>th</sup> – 18 <sup>th</sup>		<b>Chn</b> Foreign Direct Investment (Jun., RMB)	-	(+0.1%)	-	-

### Selected future data releases and events:

#### July

Sat 15 <sup>th</sup>		<b>Chn</b> Home Prices (70 Cities, Jun.)
Mon 17 <sup>th</sup>		<b>Chn</b> 1-Year Medium Term Lending Facility Rate (Jul.)
		<b>Chn</b> GDP (Q2)
		<b>Chn</b> Spending and Activity Data (Jun.)
Tue 18 <sup>th</sup>		<b>HK</b> Unemployment Rate (Jun.)
Thu 20 <sup>th</sup>		<b>Chn</b> 1-Year Loan Prime Rate (Jul.)
		<b>Chn</b> 5-Year Loan Prime Rate (Jul.)
		<b>HK</b> Consumer Prices (Jun.)
Fri 21 <sup>st</sup>		<b>Chn</b> Foreign Exchange Net Settlement and Receipts (Jun.)
Also expected during this period:		
TBC		<b>Chn</b> Government Revenue and Expenditure (Jun.)
TBC		<b>Chn</b> PBOC Balance Sheet Data (Jun.)

## Main Economic & Market Forecasts

%q/q annualised (%y/y), unless stated	Latest	Q2 2023	Q3 2023	Q4 2023	Q1 2024	2022	2023f	2024f	2025f
Official GDP	+2.2(+4.5)*	(8.1)	(5.3)	(5.9)	(4.8)	(6.0)	(4.6)	(4.2)	(6.0)
GDP (CE CAP-derived estimates)	+7.0(+4.2)*	(11)	(7.6)	(11.2)	(4.8)	(8.5)	(4.5)	(4.0)	(8.5)
Consumer Prices	(+0.2)**	(0.2)	(0.0)	(0.5)	(1.7)	(0.5)	(2.0)	(1.5)	(0.5)
Producer Prices	(-4.6)**	(-4.1)	(-2.6)	(-1.9)	(-1.2)	(-2.5)	(-0.7)	(-0.9)	(-2.5)
Broad Credit (AFRE)	(+9.5)**	(9.9)	(10.0)	(10.8)	(9.5)	(10.8)	(8.9)	(8.3)	(10.8)
Exports (US\$)	(-7.5)**	(-10.0)	(-16.0)	(-5.5)	(-10.0)	(-8.0)	(-3.0)	(2.5)	(-8.0)
Imports (US\$)	(-4.5)**	(-6.0)	(-11.0)	(-3.0)	(15.5)	(-7)	(7.5)	(1.5)	(-7)
RMB/\$ <sup>†</sup>	7.24	7.25	7.05	6.90	6.80	6.90	6.50	6.40	6.90
7-day PBOC reverse repo <sup>†</sup> %	1.90	1.90	1.80	1.80	1.80	1.80	1.80	1.80	1.80
1-year Loan Prime Rate <sup>†</sup> (LPR) %	3.55	3.55	3.45	3.45	3.45	3.45	3.45	3.45	3.45
1-year MLF Rate <sup>†</sup> %	2.65	2.65	2.55	2.55	2.55	2.55	2.55	2.55	2.55
10-year Government Bond Yield <sup>†</sup> %	2.68	2.69	2.80	2.80	2.70	2.90	2.70	2.60	2.90
RRR (major banks) <sup>†</sup> %	10.75	10.75	10.50	10.25	10.25	10.25	10.25	10.25	10.25
CSI 300 Index <sup>†</sup>	3,829	3,837	3,885	3,950	4,088	3,872	3,950	4,500	5,100
Hong Kong GDP	(+2.7)*	(4.0)	(9)	(10.5)	(7)	(-3.5)	(6.5)	(7.5)	(6.5)
Hang Seng Index <sup>†</sup>	18,435	18,984	19,350	19,750	23,500	19,781	19,750	23,500	27,000

Sources: Bloomberg, Refinitiv, CEIC, Capital Economics \*Q1; \*\*May; <sup>†</sup> End of period



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