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Abstract

During the first half of 2020the COVID-19 epidemic spread throughout the world. The global economy faced a serious recession and turmoil in the international financial market intensified. China made overall arrangements to promote epidemic control and economic and social development. Since the second quarter, the domestic economy has been recovering steadily and the main economic indicators have improved significantly. The overall operation of the foreign-exchange market has been stable, and the flexibility of the RMB exchange rate has been enhanced so as to effectively play the role of automatic stabilizer in regulating the balance of payments.

China's balance of payments maintained a basic equilibrium during the first half of 2020. The current account recorded a surplus of USD76.5 billion, accounting for 1.2 percent of GDP. The balance remained within a reasonable range, showing strong stability and resilience in the context of the epidemic. In particular, the surplus of trade in goods increased year on year; the deficit of trade in services narrowed significantly; and cross-border capital flows were generally stable. Direct investment sand portfolio investments were the main sources of the surplus, with total surplusestotalingUSD39.4 billion. The confidence of overseas investors and their inclination to continue to invest in the Chinese market and to allocate RMB assets did not change. Cross-border bond investments were active. The global spread of the epidemic led to severe turbulence in the international financial market. However, China's cross-border

bond investments fluctuated within a reasonable range in March, but stabilized rapidly and recorded a surplus in the second quarter. During the first half of 2020, foreign-exchange reserves remained basically stable, with abasic equilibrium in the BOP. By the end of June 2020, China's net external assets reached USD 2.2 trillion, an increase of 3.6 percent over the end of the previous year.

In the second half of 2020, the global epidemic and economic situation will continue to be serious and complicated. However, the steady recovery of China's economy, the deepening of reform and opening up, and the acceleration of the establishment of a domestic and international "dual circulation" development pattern are still solid foundations for a basic equilibrium in the balance of payments. It is expected that the current account will remain within a reasonable range, cross-border capital flows will remain stable, and foreign-exchange reserves will continue to be generally stable. The foreign-exchange administration departments will adhere to the principle of making overall plans for reform and opening up and risk prevention, improve the level of liberalization and facilitation of cross-border trade and investment, support ongoing epidemic control and economic and social development, fight the battle of preventing and resolving major financial risks in the field of foreign exchange, and maintain the stability of the foreign-exchange market and national economic and financial security.

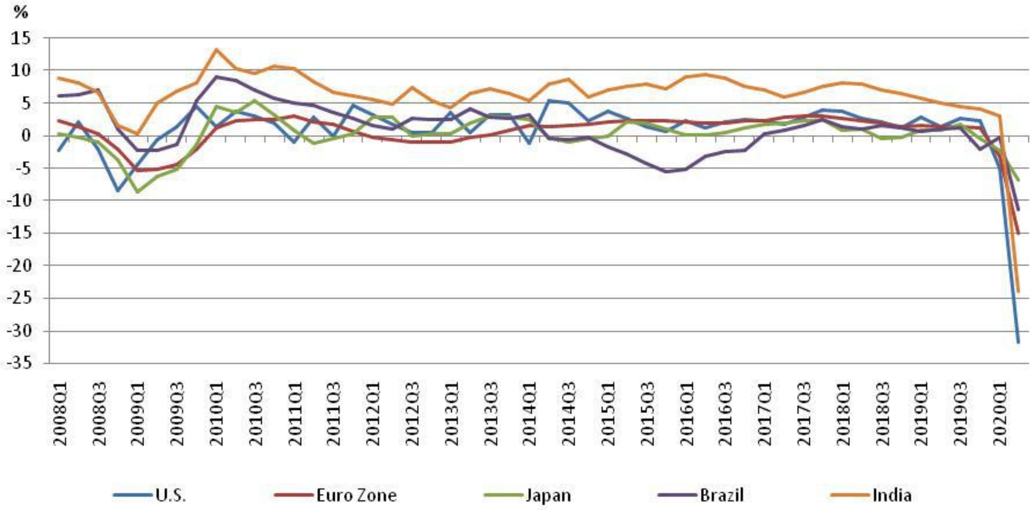
I. Overview of the Balance of Payments

(I) The Balance of Payments Environment

In the first half of 2020, Covid-19 spread throughout the world, the world economy suffered severely, and the international financial market fluctuated significantly. In the face of the epidemic, China's economy showed great resilience, with steadily recovering economic growth since the second quarter.

The rate of global economic growth rate dropped sharply. In June, the International Monetary Fund (IMF) again lowered its forecast for global economic growth in 2020 to –4.9 percent, 1.9 percentage points lower than its forecast in April. In the first half of the year, economic growth of the major developed economies rapidly declined, and the economies in the United States, the euro zone, Japan, and the United Kingdom all turned to negative growth (see Chart 1-1). In the second quarter, gross domestic product (GDP) in the United States fell by 31.7 percent on an annualized basis, compared that in with the first quarter, and the unemployment problem was also conspicuous. Economic growth in the emerging markets faced great pressure, and in the second quarter GDP inBrazil, India, Russia, South Africa, and other countries all showed negative growth. Since mid-April many countries have gradually relaxed their epidemic prevention and control measures and have promoted a resumption of work and production, showing signs ofan improvement in the world economy.

Chart 1-1 The Growth Rate of the Main Economies



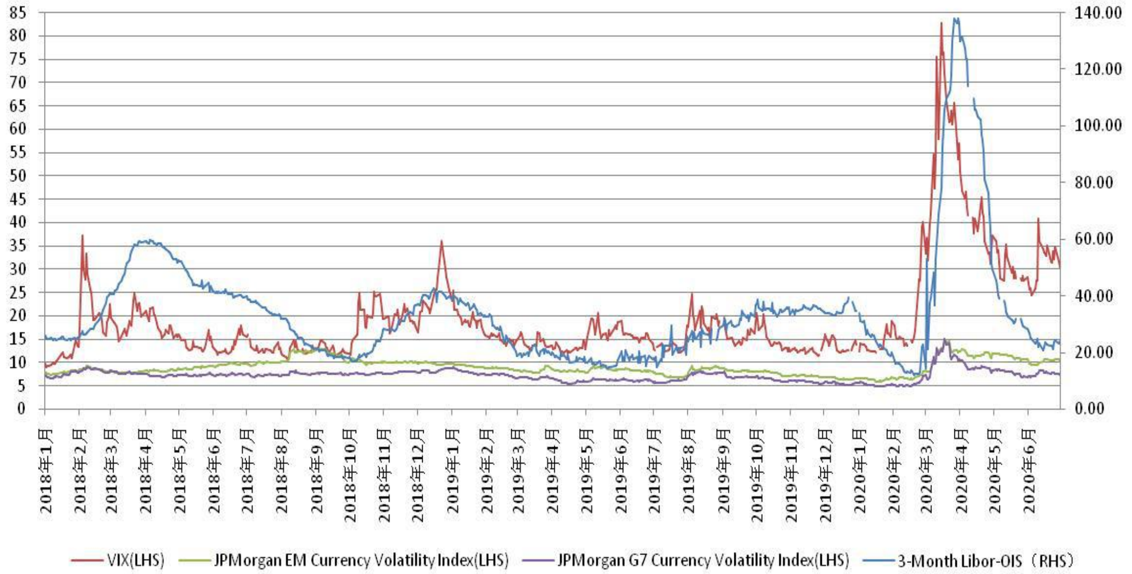
Note: The U.S. growth rate is the annualized quarterly growth, whereas the rates of the other economies are the quarterly growth rates year on year.

Source: Huanya economic database.

An ultra-loose monetary policy was launched globally. In response to the epidemic, the central banks in the major developed economies instantly cut their interest rates. The Federal Reserve and the Bank of England cut interest rates to zero. The European Central Bank and the Bank of Japan not only maintained negative interest rates but also resumed or enlarged the quantitative easing monetary policy. At the same time, they also launched structural emergency liquidity relief measures for enterprises and municipal governments, resulting in a rapid expansion in their balance sheets. Furthermore, the central banks in the emerging markets also cut interest rates, and interest rates in Brazil, Russia, India, and other economies fell to historical lows. The ultra-loose policy provided a favorable monetary environment for accelerating a global economic recovery, but the long-term low interest rate environment also increased financial vulnerabilities.

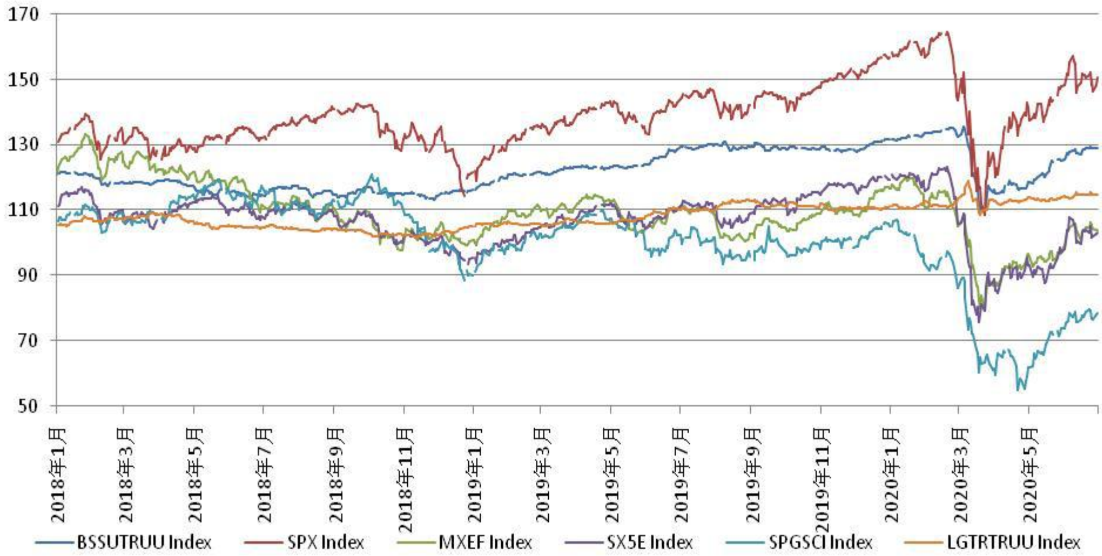
The international financial market became more volatile. In the first quarter, due to the impact of the epidemic the prices of global risk assets generally fell, and gold and other traditional safe haven assets also fell. The VIX Index, which reflects market panic, rose to its highest level since 2009. The shortage of US dollar liquidity forced the US Dollar Index to strengthen. Since the second quarter, with the Federal Reserve and the European Central Bank continuing to substantially expand their balance sheets, US dollar liquidity tensions eased, and major global stock markets rebounded rapidly. In the first half of the year, the US Dollar Index rose 1.0 percent, the emerging market currencies depreciated sharply against the US dollar, and the Emerging Market Currency Index (EMCI) fell by 11.8percent.The US Standard & Poor's 500 Index, the Euro zone Stoxx 50 Index, and the MSCI Emerging Market Stock Index fell by 4.0 percent, 13.6 percent, and 10.7 percent respectively, and the S & P GSCI Commodity Price Index fell by 25.4percent (see Charts 1-2 and 1-3).

Chart 1-2 Interest Rates in International Financial Markets and the Volatility Ratios of International Currencies



Source: Bloomberg.

Chart 1-3 Global Stocks, Bonds, and Commodity Market Prices

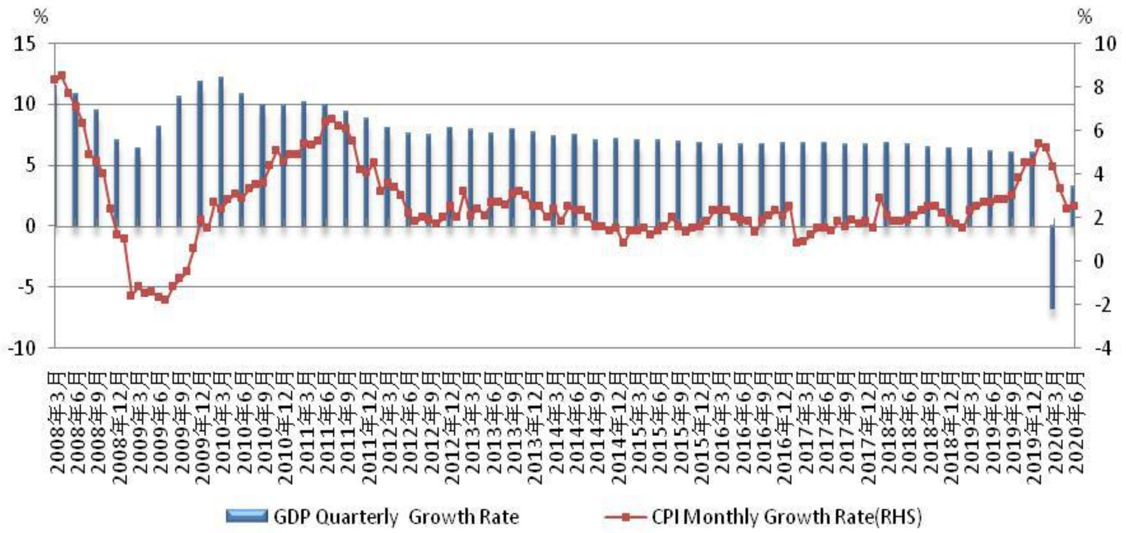


Note: BSSUTRUU and LGTRTRUU are the Bloomberg Barclays Emerging Market Index and the Developed Country Sovereign Bond Index, MXEF is the MSCI Emerging Market Index, SPX is the S&P 500 Index, SX5E is the Euro STOXX 50 Index, and SPGSCI is the S&P GSCI Commodity Price Index, all of which were 100 at the beginning of 2015.

Source: Bloomberg.

The domestic economy recovered steadily. In face of the outbreak of Covid-19 and the difficult domestic and international situations, China's economic showed great resilience. The economy recovered steadily, and the resumption of work and production improved gradually. In the second quarter, economic growth was clearly better than expected. According to preliminary calculations of the National Bureau of statistics (NBS), GDP in the first half of the year was RMB 45.7 trillion, with a year-on-year decrease of 1.6 percent. In the second quarter, GDP increased by 3.2 percent. The Consumer Price Index (CPI) rose by 2.5 percent year on year (see Chart 1-4). Consumption improved gradually, investment decreased significantly, and imports and exports were better than expected. In the medium and long term China's economy will not change in terms of stability and long-term and high-quality development.

Chart 1-4 Growth Rate of China's Quarterly GDP and Monthly CPI



Source: NBS.

Box 1

Major central banks launch ultra-loose policies to deal with the impact of the epidemic

In the first half of 2020, to deal with the impact of Covid-19 the central banks in the major countries launched ultra-loose monetary policies to ease the cash flow pressures of residents and enterprises, avoid a liquidity crisis, and prepare for a large-scale fiscal expansion to help the economy to recover. The ultra-loose monetary policies of the central banks aggravated the low interest rate environment that already existed, and a long-term persistence of the ultra-loose monetary policies may bring about an increase in financial vulnerabilities and inflation risks.

Central banks worldwide cut interest rates on a large scale. In March, the Federal Reserve and the Bank of England cut interest rates by 150 basis points and 65 basis points respectively, to the 0 interest rate range. The European Central Bank and the Bank of Japan maintained their policy interest rates at –0.5 percent and –0.1 percent, respectively. At the same time, the central banks of the major emerging market countries also cut their interest rates, with Brazil, Russia, India, and South Korea cutting their interest rates in the second quarter by 200, 150, 115, and 75 basis points, respectively, to historical lows.

Central banks in the developed economies resumed or enlarged their quantitative easing. The Federal Reserve launched unlimited quantitative easing in March, accumulating USD 2.3 trillion in bond purchases as of June, and since June it has maintained a pace of monthly bond buying of at least USD 120 billion. The European Central Bank and the Bank of England added EUR 1.47 trillion and GBP 300 billion of quantitative easing, respectively. Under the framework of yield curve control (YCC), the Central Bank of Japan increased the purchase of treasury bonds on several occasions, which was equivalent to the Fed's unlimited quantitative easing.

The central banks launched targeted financing tools to support the real economy. The Federal Reserve introduced a number of targeted financing tools, such as corporate credit instruments in the primary and secondary markets, commercial paper financing tools, fixed-term asset-backed securities lending tools, and municipal liquidity tools to support the financing of enterprises, residents, and state and municipal governments. The Euro Central Bank adjusted the operating parameters of the third round of the targeted long-term refinancing, reducing the preferential interest rate to –0.75 percent and encouraging banks to increase loans to small and medium-sized enterprises. The Bank of Japan launched about JPY 15 trillion of commercial paper and a corporate bond purchasing program to support corporate financing. The Bank of England launched a new fixed-term financing plan to provide loans to banks at an interest rate of no more than 0.25 percent to encourage lending to small and medium-sized enterprises.

Central banks injected abundant liquidity into the financial markets. The Federal Reserve injected liquidity into the short-term financing market through large-scale repos, primary dealer credit instruments, and monetary fund liquidity instruments. It also expanded the US dollar currency swap line and carried out a currency swap with 14 central banks around the world to ease cross-border US dollar liquidity shortages. The Euro Central Bank set up temporary long-term refinancing operations and long-term refinancing operations especially for the pandemic, relaxed collateral requirements, and improved bank refinancing conditions. Since March, the Bank of Japan has adopted treasury bond repo operations on several occasions to ease market liquidity pressure.

The measures to deal with the pandemic were different from those implemented for the 2008 global financial crisis. First, the measures for the pandemic were fast and powerful. For example, from March to June 2020, the Federal Reserve expanded its balance sheet by USD 2.9 trillion, significantly exceeding the USD 1.3 trillion with which it expanded its balance sheet from 2008 to 2009. Over the same period, the scale of the balance sheetsof the four central banks in the United States, Europe, Japan, and the UK was expanded by USD 5.7 trillion in total, 37 percent more than that before the outbreak. Second, policies were delivered directly to entities. In face of the 2008 global financial crisis, rescue measures were mainly directed to financial giants such as Bear Stearns, whereas this time more direct rescue measures were provided to the private sectors, such as small and medium-sized enterprises, which were more affected by the pandemic. For example, the Federal Reserve, in cooperation with the U.S. Treasury, made a breakthrough in approving loan facilities for the general enterprise loan program and the wage protection program, and directly supported SME credit in the non-financial sector for the first time since the Great Depression. Third, in a number of rescue policies designed for this crisis there was a synergy between monetary and fiscal policies. For example, the U.S. Treasury provided capital support for the Federal Reserve's financing facilities to absorb possible credit risk losses.

The ultra-loose monetary policies eased the impact of the epidemic and accelerated the economic recovery. The central banks' loose monetary policies made up for the cash gap in the private sector caused by the epidemic and injected a huge amount of liquidity into the financial market to avoid the liquidity crisis from turning into a repayment crisis and causing financial turbulence. In addition, the low interest rate environment brought about by the ultra-loose monetary policies ensured that the government could obtain low-cost financing and it created conditions for a large-scale fiscal expansion. Finally, the low interest rate environment will help to ease the pressures of deleveraging, accelerate the pace of an economic recovery after the epidemic, and reduce the possible aftereffects of the epidemic.

There should be an awareness of the rise of financial vulnerabilities and inflation risks brought about by the ongoing low interest rate environment. Covid-19 is now still out of control globally, and in the short term it will be difficult for the central banks to rescind their ultra-loose monetary policies. This will exacerbate the dilemma of low growth, low interest rates, and high uncertainties that already existed before the outbreak of Covid-19. Furthermore there levant financial risks should not be ignored. First, under the ultra-loose monetary policies, financial institutions tend to assume higher risks to obtain higher returns, resulting in rising vulnerabilities in the financial system. Second, low interest rates tend to spawn asset price bubbles. Although suffering severely from the impact of the epidemic, stock and real-estate prices in the developed countries are still approaching historical highs. Third, in the face of the epidemic, with the political pressures from the government to "rescue all," the finance departments may continuingly launch new rescue policies, even forcing the central banks to monetize the debt. Once the ultra-loose monetary policies are superimposed on the lax fiscal discipline, the upward risks of inflation will be increased.

(II) The Main Characteristics of the Balance of Payments

The current account posted a surplus, while there was a small deficit in the non-reserve financial account. In the first half of the year, the current account recorded a surplus of USD 76.5 billion, and the non-reserve financial account posted a deficit of USD 29.2 billion (see Table 1-1).

Table 1-1 Structure of the BOP Surplus

USD 100 Million

Item	2014	2015	2016	2017	2018	2019	2020H1
Current account balance	2360	3042	2022	1951	491	1413	765
As a % of GDP	2.3%	2.7%	1.8%	1.6%	0.4%	1.0%	1.2%
Financial account excluding reserve assets	-514	-4345	-4161	1095	1306	378	-292
As a % of GDP	-0.5%	-3.9%	-3.7%	0.9%	1.0%	0.3%	-0.4%

Sources: SAFE, NBS.

The surplus in trade in goods increased. Based on balance-of-payments statistics,[1]in the first half of the year exports and imports of trade in goods totaled USD 1069.7billion and USD 885.3 billion, respectively, down5 percent and 6 percent, respectively, achieving a surplus of USD 184.4 billion or up 2 percent (see Chart 1-5).

The deficit in trade in services narrowed. In the first half of the year, revenue from trade in services totaled USD 110.2 billion, down 7percent, and expenditures totaled USD 186.8 billion, down 25 percent. Trade in services recorded a deficit of USD 76.6 billion, down 41 percent (see Chart 1-5). In particular, the transportation deficit totaled USD 19.1 billion, down31 percent, and the travel deficit totaled USD 61.9 billion, down44percent, reflecting the impact of the shrinking global trade and cross-border travel influenced by the global epidemic of COVID-19.

Primary income[2]showed a small deficit. In the first half of the year, revenue from primary income totaled USD 99 billion, down23 percent, and expenditures totaled USD 132.9 billion,up6 percent. Primary income thus recorded a deficit of USD 33.9billion compared with a surplus of USD 3.7 billion during the last year (see Chart 1-5). In particular, the surplus in employee compensation, remaining basically stable, was USD 0.7 billion. Investment

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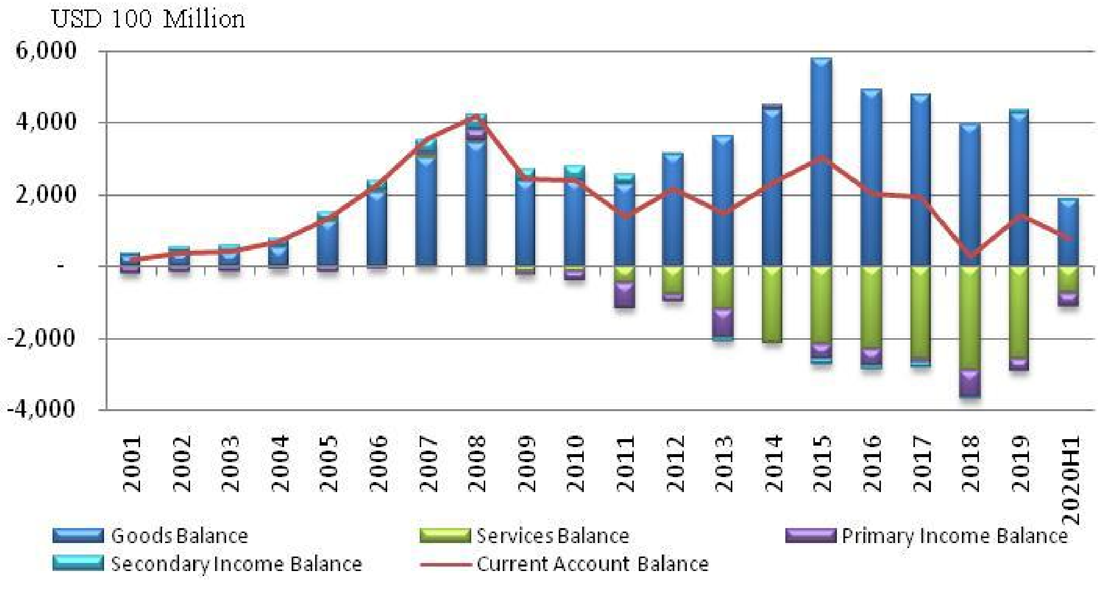
[1] BOP statistics and statistics of the General Administration of Customs with respect to trade in goods can be reconciled by the following: First, imports based on the BOP statistics equal 95 percent of imports based on the customs statistics by quoting the CIF and assuming 5 percent to be insurance and freight. Second, BOP statistics include goods repatriation, goods purchased at ports, and smuggled goods that are deducted from the import and export returns.

[2] The IMF's *Balance of Payments* and *International Investment Manual* (Sixth Edition) renamed the income item under the current account as primary income and renamed current transfers as secondary income.

income recorded a deficit of USD 35.1 billion, compared with a surplus of USD1.5 billion during the last year. Revenue from outward investments totaled USD 91.1 billion, and expenditures for inward investments, including profits and dividends of foreign-funded enterprises, totaled USD 126.2 billion.

Secondary income posted a small surplus. In the first half of the year, the revenue of secondary income totaled USD 17.3 billion, up34 percent. The expenditures of secondary income doubled over the year to reach USD 14.8 billion. Secondary income thus recorded a surplus of USD 2.5billion, down 54 percent (see Chart 1-5).

Chart 1-5 Major Items under the Current Account



Source: SAFE.

Direct investments retained a surplus. Based on the balance-of-payments statistics,[3] in the first half of the year direct investments posted a surplus of

[3]The BOP compiles and reports direct investments following balance-sheet rules, whereas the Ministry of Commerce compiles and reports direct investments by direction, with differences between the principles for reverse investments and investments among affiliates. In addition, direct investments based on BOP statistics also include unpaid and unremitted profits, retained earnings, shareholders'

USD21 billion and continued their relatively stable surplus pattern (see Chart 1-6). In particular, net outflows of outward direct investments (the net increase in direct=investment assets) amounted to USD 47.2 billion, up 1 percent. Net inflows of foreign direct investments (the net increase in direct-investment liabilities) totaled USD 68.2 billion, down 17 percent, which reflected the periodic impact of the global direct-investment downturn influenced by the global COVID-19 epidemic. But the overall scale of net inflows of foreign direct investments was still significantly higher than the low point during the same period in recent years.

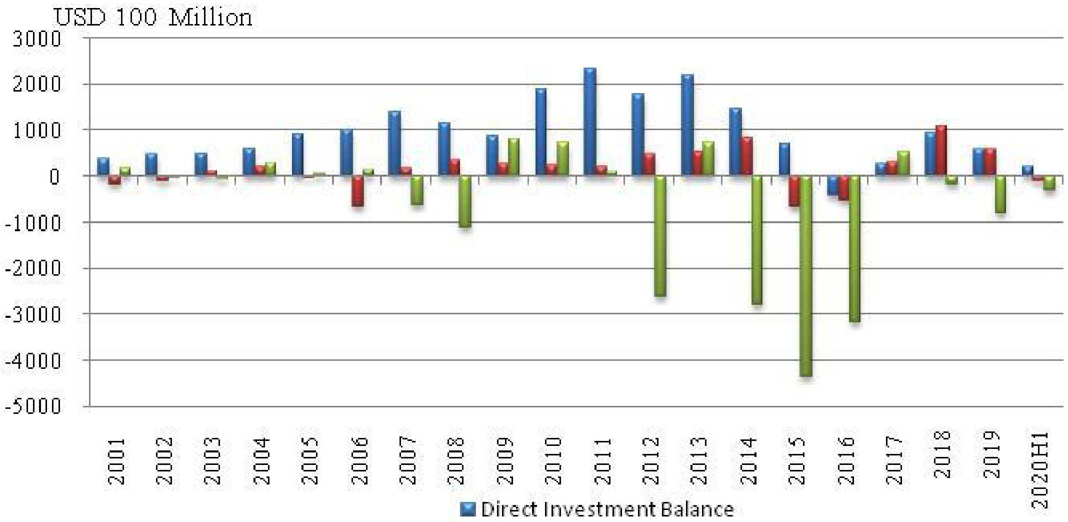
Portfolio investments recorded a small deficit. In the first half of the year, portfolio investments posted a deficit of USD 10.8 billion, mainly affected by the deficit of USD 53.2 billion in the first quarter (see Chart 1-6). But portfolio investments returned to a surplus in the second quarter. In particular, net outflows of outward portfolio investments (the net increase in assets) totaled USD 75.1 billion, up 93 percent, and the net inflows of inward portfolio investments (the net increase in liabilities) totaled USD 64.3 billion, up 4 percent.

The deficit in other investments remained stable. In the first half of the year, other investments, including loans, trade credits, and deposits, posted a deficit of USD 30.3 billion, remaining within a stable range (see Chart 1-6). In particular, net out flows of outward other investments (the net increase in assets)

loans, foreign capital utilized by financial institutions, and real-estate purchases by non-residents.

totaled USD 65.2 billion, compared with net inflows (the net decrease in assets) of USD 10.5 billion during the last year.Net inflows of inward other investments (the net increase in liabilities) totaled USD 34.8 billion, compared with net outflows (the net decrease in liabilities) of USD 23.3 billion during the last year.

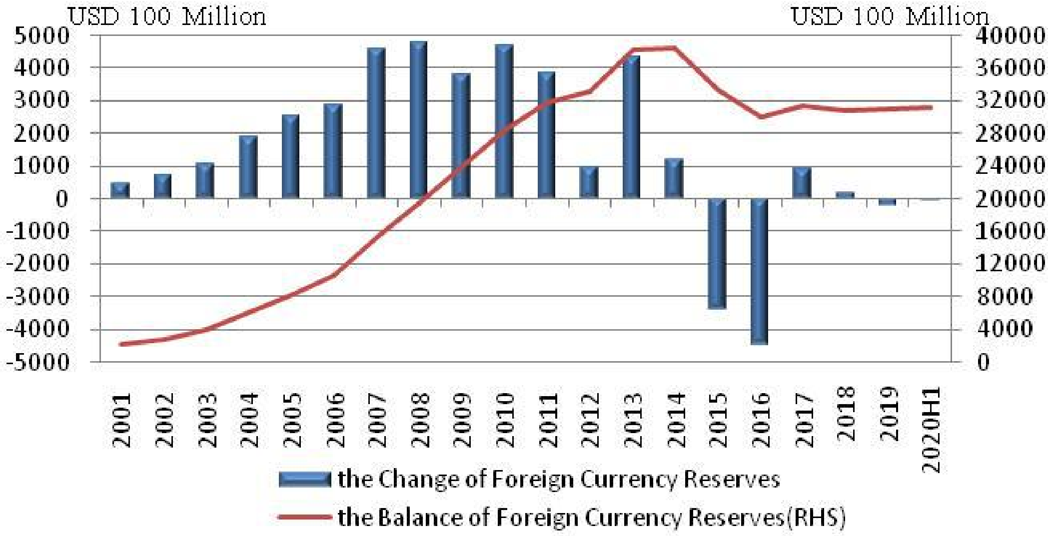
Chart1-6 Major Items under the Capital and Financial Account



Source: SAFE

Reserve assets remained stable. In the first half of 2020, reserve assets involving transactions (excluding the effects of non-transactional values, such as exchange rates and prices) decreased by USD 5.9 billion. In particular, foreign-currency reserves involving transactions decreased by USD 7 billion (see Chart 1-7). By the end of June 2020, China's foreign-currency reserves totaled USD 3112.3 billion, up USD 4.4 billion since the end of 2019.

Chart 1-7 Foreign-Currency Reserve Assets Involving Transactions



Source: SAFE.

Table 1-2 Balance of Payments during the First Half of 2020

Item	Line No.	2020H1
1. Current account	1	**765**
Credit	2	12,962
Debit	3	-12,198
1.A Goods and services	4	**1,078**
Credit	5	11,799
Debit	6	-10,721
1.A.a Goods	7	**1,844**
Credit	8	10,697
Debit	9	-8,853
1.A.b Services	10	**-766**
Credit	11	1,102
Debit	12	-1,868
1.A.b.1 Manufacturing services on physical inputs owned by others	13	65
Credit	14	67
Debit	15	-2
1.A.b.2 Maintenance and repair services n.i.e	16	21
Credit	17	36
Debit	18	-15
1.A.b.3 Transport	19	-191
Credit	20	244
Debit	21	-434
1.A.b.4 Travel	22	-619
Credit	23	84
Debit	24	-703

1.A.b.5 Construction	25	15
Credit	26	53
Debit	27	-39
1.A.b.6 Insurance and pension services	28	-32
Credit	29	23
Debit	30	-55
1.A.b.7 Financial services	31	5
Credit	32	20
Debit	33	-15
1.A.b.8 Charges for the use of intellectual property	34	-129
Credit	35	44
Debit	36	-174
1.A.b.9 Telecommunications, computer, and information services	37	13
Credit	38	178
Debit	39	-165
1.A.b.10 Other business services	40	98
Credit	41	334
Debit	42	-236
1.A.b.11 Personal, cultural, and recreational services	43	-10
Credit	44	4
Debit	45	-14
1.A.b.12 Government goods and services n.i.e	46	-1
Credit	47	15
Debit	48	-16
1.B Primary income	49	**-339**
Credit	50	990
Debit	51	-1,329
1.B.1 Compensation of employees	52	**7**
Credit	53	70
Debit	54	-63
1.B.2 Investment income	55	-351
Credit	56	911
Debit	57	-1,262
1.B.3 Other primary income	58	5
Credit	59	9
Debit	60	-4
1.C Secondary income	61	**25**
Credit	62	173
Debit	63	-148
1.C.1 Personal transfers	64	0

Credit	65	17
Debit	66	-17
1.C.2 Other secondary income	67	25
Credit	68	156
Debit	69	-131
2. Capital and financial account	70	**-234**
2.1 Capital account	71	**-1**
Credit	72	1
Debit	73	-2
2.2 Financial account	74	**-233**
Assets	75	-1,886
Liabilities	76	1,653
2.2.1 Financial account excluding reserve assets	77	**-292**
Financial assets excluding reserve assets	78	-1,945
Liabilities	79	1,653
2.2.1.1 Direct investment	80	**210**
2.2.1.1.1 Assets	81	**-472**
2.2.1.1.1.1 Equity and investment fund shares	82	-382
2.2.1.1.1.2 Debt instruments	83	-90
2.2.1.1.1.a Financial sector	84	-82
2.2.1.1.1.1.a Equity and investment fund shares	85	-95
2.2.1.1.1.2.a Debt instruments	86	12
2.2.1.1.1.b Non-financial sector	87	-389
2.2.1.1.1.1.b Equity and investment fund shares	88	-287
2.2.1.1.1.2.b Debt instruments	89	-102
2.2.1.1.2 Liabilities	90	**682**
2.2.1.1.2.1 Equity and investment fund shares	91	544
2.2.1.1.2.2 Debt instruments	92	138
2.2.1.1.2.a Financial sector	93	76
2.2.1.1.2.1.a Equity and investment fund shares	94	72
2.2.1.1.2.2.a Debt instruments	95	4
2.2.1.1.2.b Non-financial sector	96	606
2.2.1.1.2.1.b Equity and investment fund shares	97	472
2.2.1.1.2.2.b Debt instruments	98	134
2.2.1.2 Portfolio investment	99	**-108**
2.2.1.2.1 Assets	100	**-751**
2.2.1.2.1.1 Equity and investment fund shares	101	-459
2.2.1.2.1.2 Debt securities	102	-292
2.2.1.2.2 Liabilities	103	**643**
2.2.1.2.2.1 Equity and investment fund shares	104	167

2.2.1.2.2.2 Debt securities	105	476
2.2.1.3 Financial derivatives (other than reserves) and employee stock options	106	**-91**
2.2.1.3.1 Assets	107	-71
2.2.1.3.2 Liabilities	108	-21
2.2.1.4 Other investment	109	**-303**
2.2.1.4.1 Assets	110	**-652**
2.2.1.4.1.1 Other equity	111	0
2.2.1.4.1.2 Currency and deposits	112	-264
2.2.1.4.1.3 Loans	113	-523
2.2.1.4.1.4 Insurance, pension, and standardized guarantee schemes	114	-30
2.2.1.4.1.5 Trade credit and advances	115	313
2.2.1.4.1.6 Other accounts receivable	116	-147
2.2.1.4.2 Liabilities	117	**348**
2.2.1.4.2.1 Other equity	118	0
2.2.1.4.2.2 Currency and deposits	119	322
2.2.1.4.2.3 Loans	120	209
2.2.1.4.2.4 Insurance, pension, and standardized guarantee schemes	121	12
2.2.1.4.2.5 Trade credit and advances	122	-403
2.2.1.4.2.6 Other accounts payable	123	208
2.2.1.4.2.7 Special drawing rights	124	0
2.2.2 Reserve assets	125	**59**
2.2.2.1 Monetary gold	126	0
2.2.2.2 Special drawing rights	127	1
2.2.2.3 Reserve position in the IMF	128	-12
2.2.2.4 Foreign exchange reserves	129	70
2.2.2.5 Other reserve assets	130	0
3.Net errors and omissions	131	**-531**

USD 100 million

Notes:

1. This chart was compiled according to the *Balance of Payments Manual* (Sixth Edition).

2. In the financial account, a positive value for assets indicates a net decrease, whereas a negative value indicates a net increase. A positive value for liabilities indicates a net increase, whereas a negative value indicates a net decrease.

3. The chart is based on rounding principles.

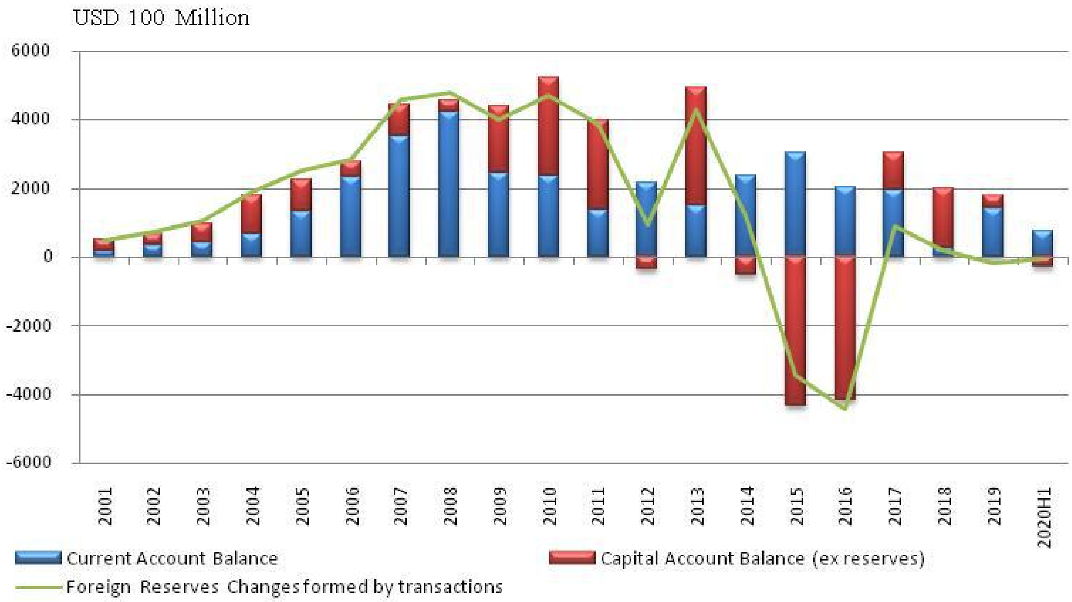
Source: SAFE.

(III) Evaluation of the Balance of Payments

China's balance of payments maintained a basic equilibrium

supported by the fundamentals of stabilization and recovery of the domestic economy. The global COVID-19 epidemic seriously impacted the global economy and international trade in 2020.The international financial market fluctuated violently and the external environment was complicated and severe. China effectively controlled the epidemic, and actively promoted policies and measures to stabilize foreign trade and foreign investment, thus steadily restoring economic development and effectively promoting a basic equilibrium in China's balance of payments. In the first half of 2020, China's balance of payments showed a balanced pattern under which the current account maintained a small surplus and the non-reserve financial account posted a small deficit. Foreign-currency reserve assets remained stable above USD 3 trillion(see Chart 1-8).

Chart 1-8 Structure of the BOP

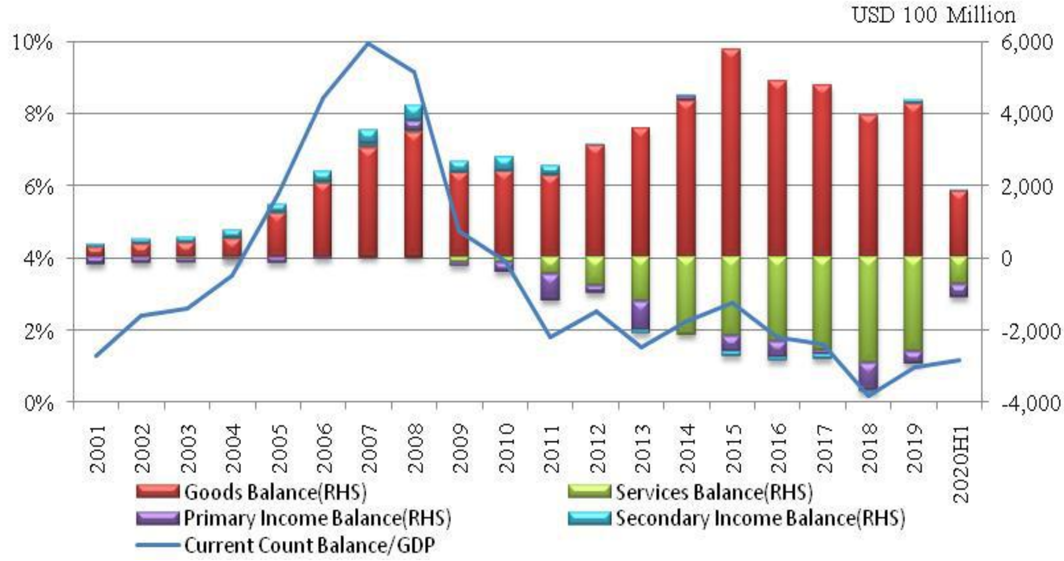


Source: SAFE.

The current account posted a surplus and remained within a

reasonable range. In the first half of 2020, the current account recorded a surplus of USD 76.5 billion, up 26 percent and accounting for 1.2 percent of GDP (see Chart 1-9). In particular, the current account posted a deficit of USD33.7 billion in the first quarter and reached a surplus of USD110.2 billion in the second quarter. On the whole, the current account maintain eda surplus despite the impact of the epidemic, showing strong stability and resilience. In terms of the main items, the ratio of the surplus of trade in goods to GDP was 2.8 percent, up 0.2 percent. In the second quarter, with the rapid recovery of enterprise production activities, the surplus of trade in goods increased significantly compared with the first quarter, and its ratio to GDP rose to 4.6 percent. In the first half of 2020, the ratio of the deficit of trade in services to GDP was –1.2 percent, down0.7 percent, mainly due to the rapid decline of travel expenditures, which reflected the impact of the epidemic in restraining demand for overseas tourism and studying abroad. The total deficits of primary income and secondary income, with relatively stable changes, accounted for –0.5 percent of GDP.

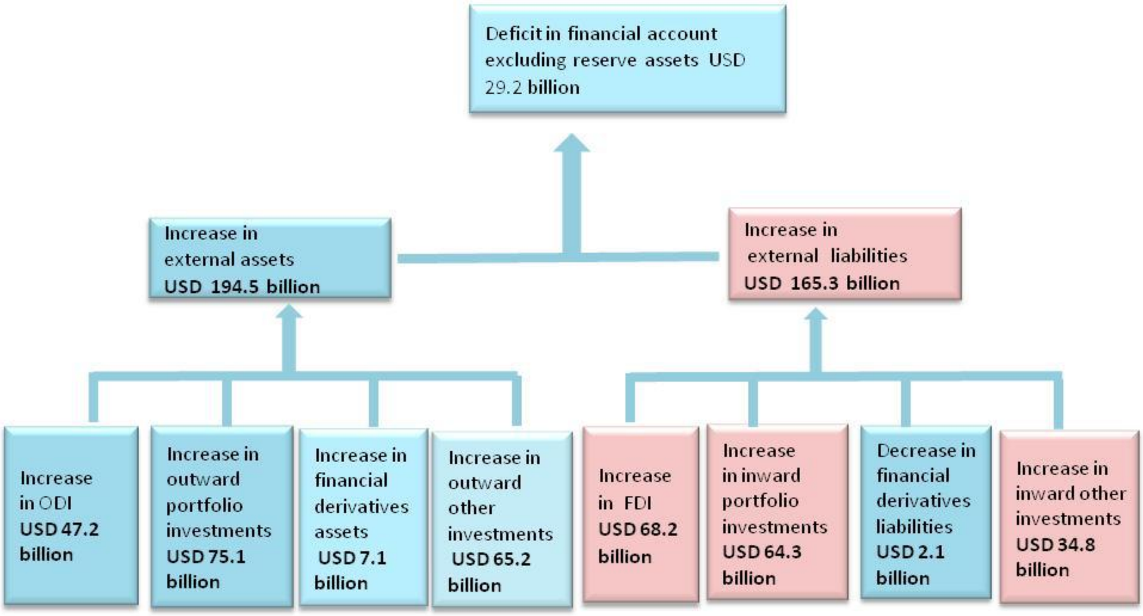
Chart 1-9 Structure of the Current Account



Sources: SAFE, NBS.

Cross-border capital flows remained stable, and medium-and long-term foreign capital maintained net inflows. In the first half of the year, the non-reserve financial account maintained a basic balance, recording a deficit ofUSD29.2 billion, significantly lower than that in 2015–2016, when outflow pressures were higher. On the one hand, direct investments and debt securities were major contributors to the surplus, posting a surplus of USD 21 billion and USD 18.4 billion, respectively, in the first half of the year, and they have been stable in recent years. In particular, 60 percent of the debt securities were held by overseas central banks, which are medium and long-term stable investments, and they have been growing steadily in recent years. China's economic recovery occurred early, the opening-up is making constant progress, and the return on RMB assets is relatively good. Thus, there is no change in the confidence and the trend of overseas investors to invest in the Chinese market and to increase their holdings of RMB assets in the medium and long term. On the other hand, the short-term fluctuations of cross-border capital flows under the stock item was generally within a reasonable and risk=controllable range despite the impact of severe fluctuations in the international financial market. In the first half of the year, the deficit of equity investments was USD 29.2 billion, mainly because overseas liquidity was tighter; there were severe fluctuations in the international financial market in March, cross-border capital generally flowed out from the emerging markets, and at the same time foreign investors reduced their holdings of China's stocks. Furthermore, domestic investors increased their holdings of Hong Kong stocks to better realize an appreciation of assets. China's cross-border bond investments stabilized rapidly and recorded a surplus of USD 17.3 billion in the second quarter. In the first half of the year, there was a deficit of USD 30.3 billion under other investments. In particular, China's outward investments and foreign inward investments, including loans and deposits, increased, indicating that the relevant investment and financing activities were steadily increasing.

Chart 1-10 Structural Analysis of China’s Cross-border Capital Flows in the First Half of 2020



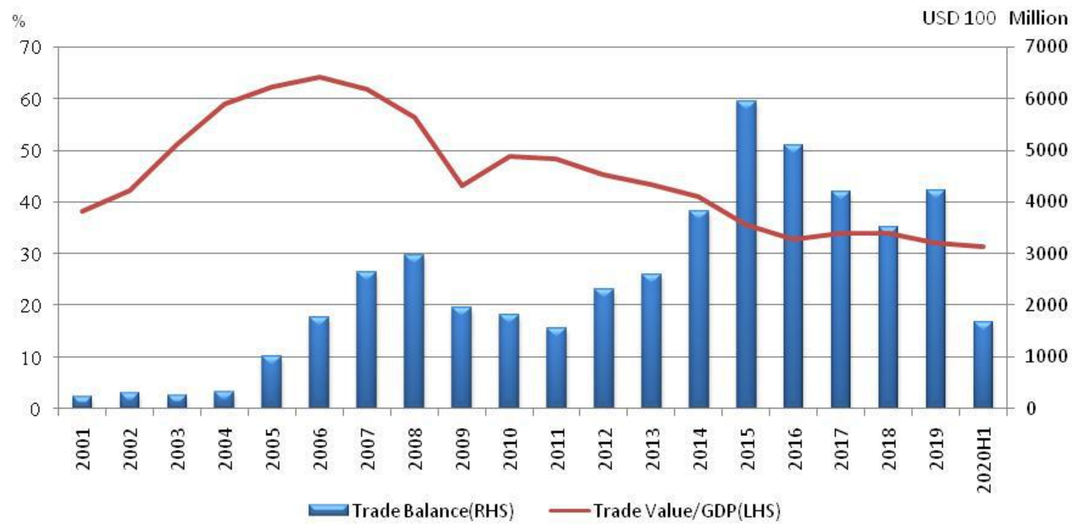
Source: SAFE.

II. Analysis of the Major Items in the Balance of Payments

(1) Trade in Goods

The surplus in trade in goods remained stable after a moderate decrease. In the first half of 2020, global trade decreased due to the wide spread of the Covid-19epidemic. According to the latest statistics of the World Trade Organization (WTO), exports and imports of global trade in goods in the first half of 2020 fell by 14 percent year on year. China's foreign trade remained stable after a moderate decrease. According to customs statistics, in the first half of 2020China's exports and imports totaled USD 2.0 trillion, a slight decrease of 6 percent year on year. The trade surplus reached USD 167.9 billion, a slight decrease of 5 percent year on year. In the first quarter of 2020, the trade surplus decreased significantly due to the outbreak of the Covid-19epidemic and its impact on production. In the second quarter of 2020, when work and production resumed in China the trade surplus increased 49 percent year on year. In the first half of the year, China's dependence on foreign trade (the ratio of foreign trade to GDP) was 31 percent, a decrease of 0.9 percentage point year on year, indicating that China continued to improve its economic structure (see Chart 2-1).

Chart 2-1 The Balance of Trade in Goods and Dependence on Foreign Trade

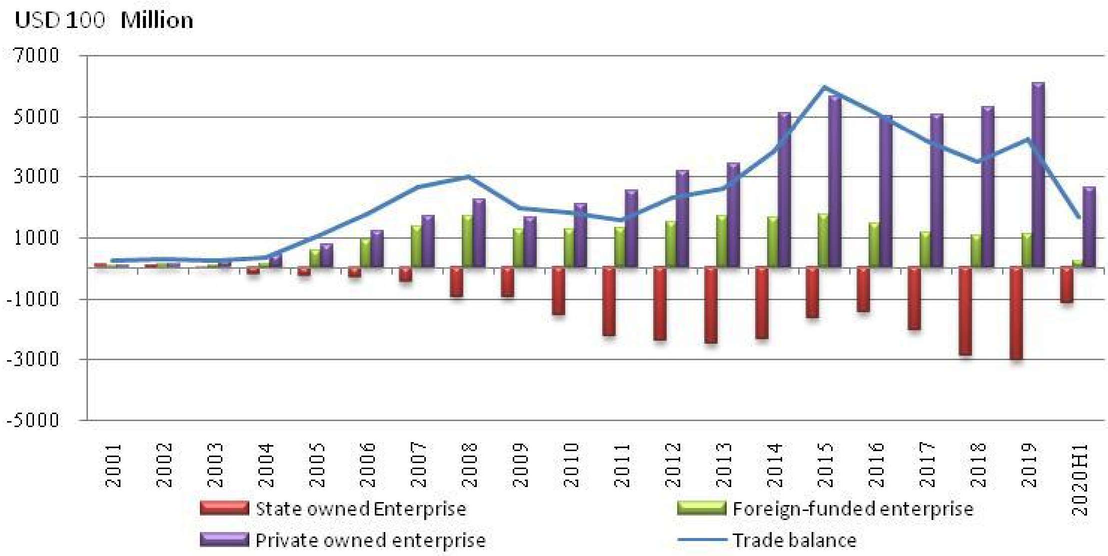


Sources: General Administration of Customs, NBS.

Private enterprises contributed to approximately one-half of foreign trade, and state-owned enterprises significantly improved their trade conditions. In the first half of 2020, exports and imports by private enterprises totaled USD 921.7 billion, up 1.3 percent year on year, accounting for 45 percent of total foreign trade, up 3 percentage points from the first half of 2019. Exports and imports by foreign-invested enterprises totaled USD 791.7 billion, accounting for 39 percent of total foreign trade, down 1 percentage point from the first half of 2019. Exports and imports by state-owned enterprises totaled

USD 316.2 billion, contributing 2 percentage points less than that in the first half of 2019. The trade deficit of state-owned enterprises reached USD 116.2 billion, a year-on-year decrease of 22 percent. The trade surplus of foreign-invested enterprises and private enterprises amounted to USD 21.6 billion and USD 262.4 billion, respectively (see Chart 2-2).

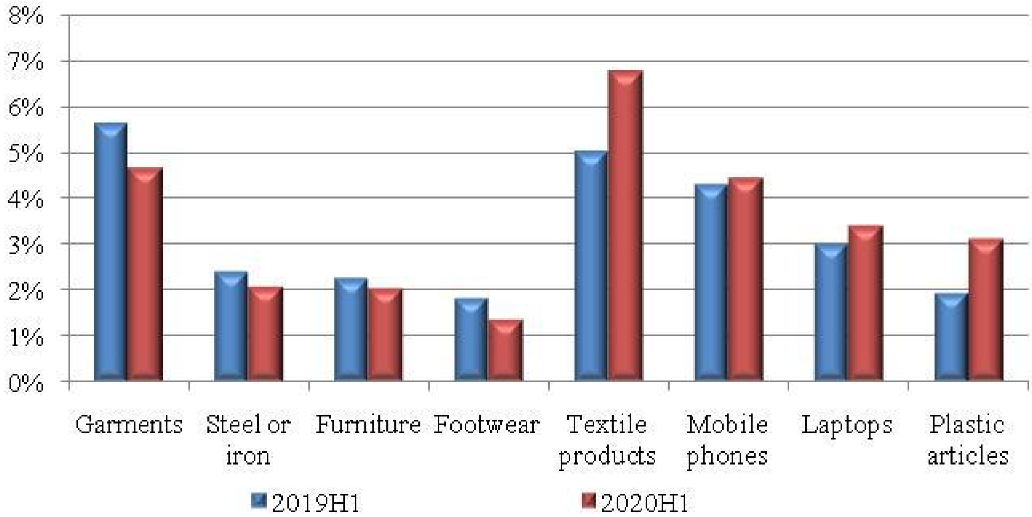
Chart 2-2 TheBalance of Trade in Goods in Terms of Contributors



Source: General Administration of Customs

The structure of exports improved, with rapid growth in high-tech products and epidemic-prevention products. In the first half of 2020, China demonstrated strong competitiveness in high value-added products. Exports of electro-mechanical products reached USD 643.6 billion, accounting for 59 percent of total exports and up 0.4 percentage point from the first half of 2019. Exports of epidemic-prevention products increased rapidly, among which, exports of textiles, including face masks, increased by 27.8 percent. Exports of pharmaceutical items and medicines increased by 19.5 percent (see Chart 2-3). This rapid growth also reflects China's efforts, after successfully curbing the epidemic domestically, to maintain global public health security by working together with other economies.

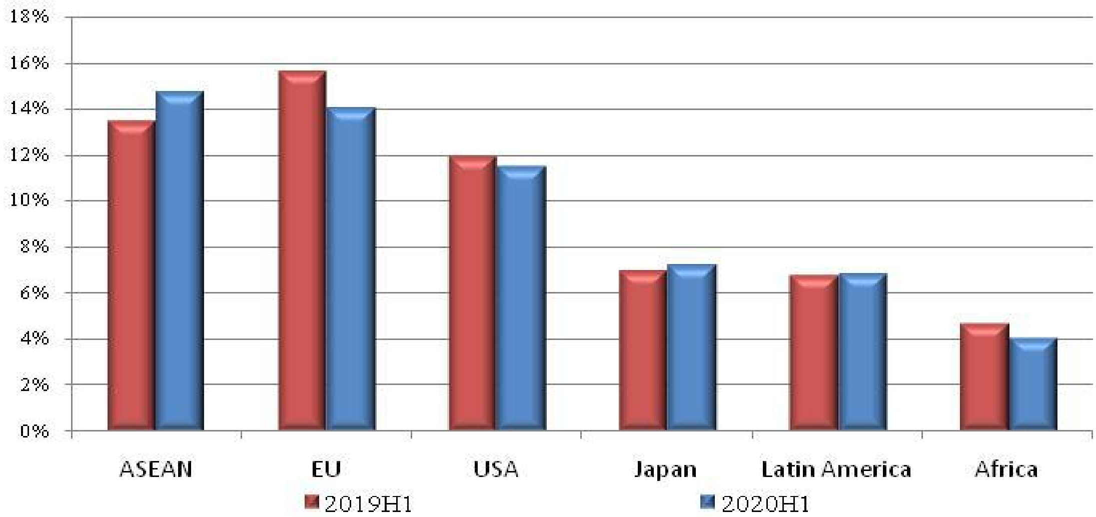
Chart 2-3 Changes in the Proportion of China'sKey Commodity Exports



Source: General Administration of Customs

China's foreign trade markets continued to be more diversified. Trade exchanges with ASEAN and Africa increased. In terms of exports and imports, ASEAN surpassed the EU and the United States, becoming China's largest trade partner in the fourth quarter of 2019. This trend continued during the first half of 2020. China's exports and imports of goods to ASEAN totaled approximately USD 300 billion, accounting for 15 percent of China's total foreign trade, up 1 percentage point year on year (see Chart 2-4). From the perspective of net exports, China maintained a surplus with its top three trade partners in the first half of 2020. The trade surplus with the United States, the European Union, and ASEAN reached USD 120.9 billion, USD 60 billion, and USD 30.4 billion, respectively, accounting for 72 percent, 36 percent, and 18 percent, respectively, of China's total surplus. At the same time, China's trade surplus with Africa grew rapidly, accounting for 9 percent of China's total trade surplus, up 6 percentage points year on year.

Chart 2-4 The Ratio of Exports and Imports between China and its Major Trade Partners

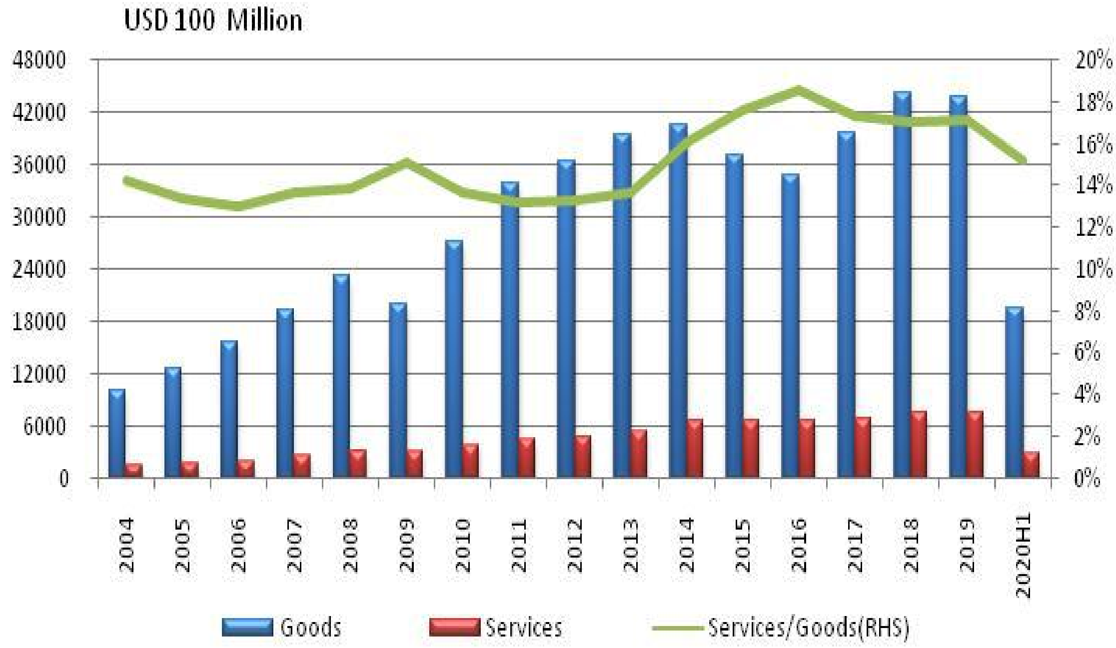


Note: The ratio is based on data denominated in USD.
Source: General Administration of Customs

（Ⅱ）Trade in Services

Affected by the Covid-19 epidemic, the total volume of trade in services decreased. In the first half of 2020, China's trade in services totaled USD 297 billion, down 19 percent year on year, and the ratio of trade in services to trade in goods was 15 percent (see Chart 2-5). In the context of the global combat against the epidemic and the border controls among various economies, China's revenue and expenditures from travel fell by 46 percent year on year. Revenue from computer services and the use of intellectual property increased 18 percent and 4 percent, respectively, year on year.

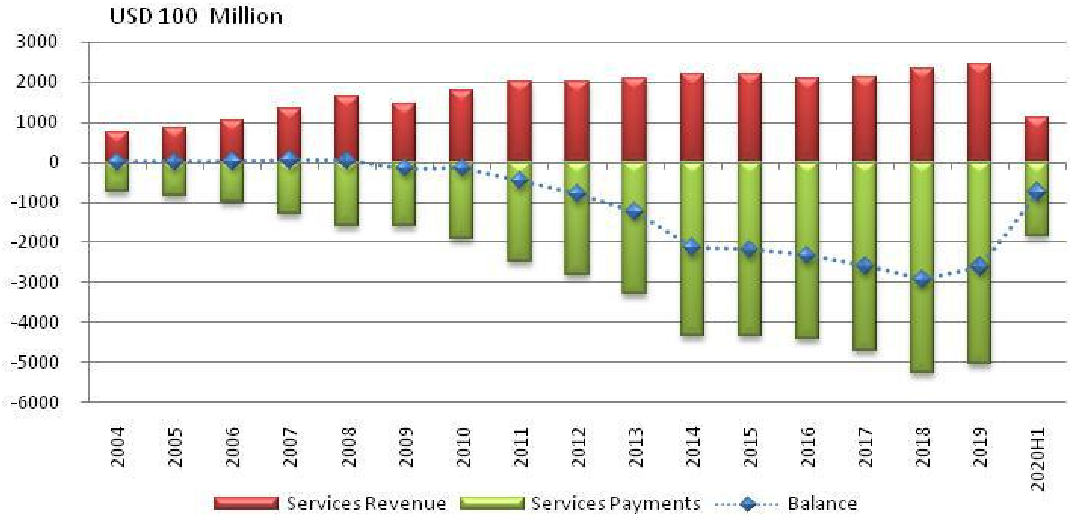
Chart 2-5 Comparison of the Total Volume of Trade in Goods and Services



Source: State Administration of Foreign Exchange

Revenue from trade in services declined slightly. In the first half of 2020, revenue from trade in services was USD 110.2 billion, down 7 percent year on year (see Chart 2-6). Among the major items, revenue from other business services, such as consultancies and technical services, amounted to USD 33.4 billion, down 1 percent year on year and accounting for 30 percent of total revenue. Revenue from transportation amounted to USD 24.4 billion, up 10 percent year on year and accounting for 22 percent of total revenue. Revenue from computer and information services amounted to USD 17.8 billion, up 10 percent year on year and accounting for 16 percent.

Chart 2-6 Revenue and Expenditures of Trade in Services

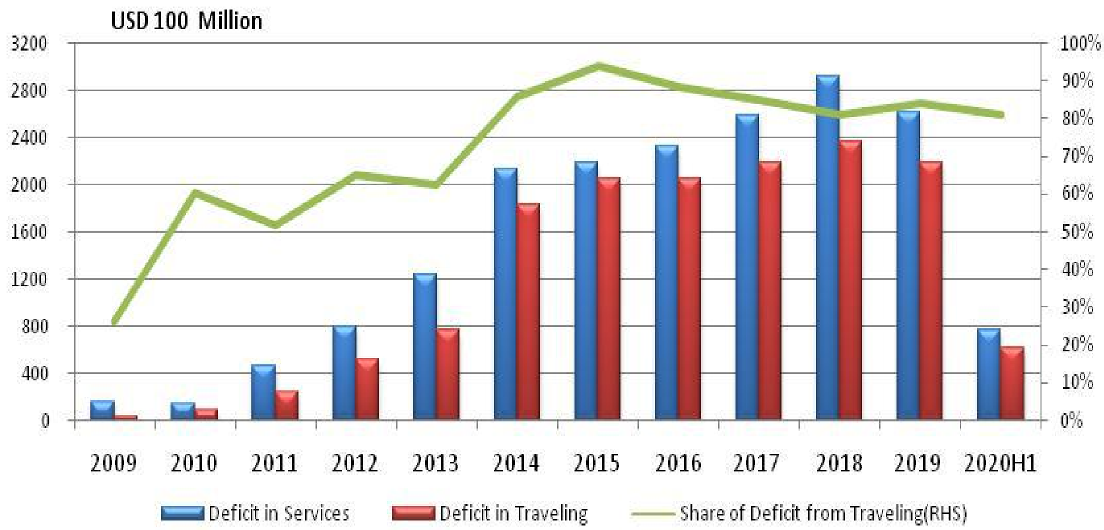


Source: State Administration of Foreign Exchange.

Expenditures for trade in services declined sharply. In the first half of 2020, expenditures for trade in services were USD 186.8 billion, down 25 percent year on year. Among the major items, travel recorded expenditures of USD 70.3 billion, down 45 percent year on year and accounting for 38 percent of total expenditures. Transportation recorded expenditures of USD 43.4 billion, down 13 percent year on year and accounting for 23 percent of total expenditures. Expenditures on other business services, such as consultancies and technical-related services, reached USD 23.6 billion, approximately the same amount as that in the first half of 2019 and accounting for 13 percent of total expenditures.

The trade-in-services deficit narrowed significantly. In the first half of 2020, the deficit in trade in services was USD 76.6 billion, down 41 percent year on year. Travel continued to be the main source of the deficit (see Chart 2-7). The travel deficit amounted to USD 61.9 billion, down 44 percent year on year, mainly due to the sharp decrease in the number of Chinese outbound tourists in the context of the epidemic. Transportation and the use of intellectual property remained the second and third largest deficit items among trade in services. The transportation deficit. At USD 19.1 billion and down 31 percent year on year, was mainly due to the decrease in freight expenditures for imports. The use of intellectual property, recording recorded a deficit of USD 12.9 billion and down 8 percent year on year, was mainly due to an increase in revenue.

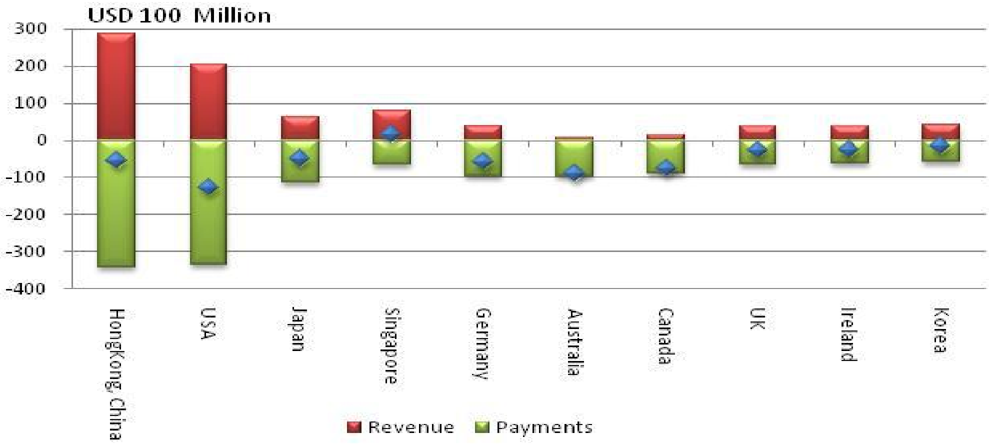
Chart 2-7 The Contribution of Travel to the Deficit of Trade in Services



Source: State Administration of Foreign Exchange.

China's trade partners were highly concentrated. In the first half of 2020, China's top ten partners in term of trade in services were Hong Kong SAR, the United States, Japan, Singapore, Germany, Australia, Canada, the United Kingdom, Ireland, and South Korea. Trade with these partners totaled USD 213.7 billion, accounting for 72 percent of the total trade in services. With the exception with Singapore, China posted deficits with its9 other major trade partners (see Chart 2-8), but the deficits were generally narrowing.

Chart 2-8 China's Trade in Services in Terms of Trade Partners During the First Half of 2020



Source: State Administration of Foreign Exchange.

Box 2

China's transport by sea grew steadily and showed strong resilience

Trade in services has currently become a new driving force to support China's foreign trade. Overseas shipping, as one of the main industries that "went global" to fully participate in global competition, is relatively large in scale and has competitive advantages. Cross-border revenue and expenditures of China's transport by sea in 2019 totaled USD 52.1 billion, an average annual growth rate of 5.6 percent since 2009. Overseas shipping has played a positive role in enhancing the competitiveness of China's transportation services, ensuring the smooth flows of important resources and promoting a balanced BOP situation. In the first half of 2020, despite the outbreak of COVID-19 and the shocks to the global transportation industry, China's sea transportation services continued to grow and demonstrated strong resilience.

The total volume of sea transportation increased steadily. In the first half of 2020, the cross-border revenue and expenditures of sea transportation services totaled USD 26 billion, a year-on-year increase of 4 percent. The deficit was USD 1.1 billion, narrowing by 57 percent year on year. Specifically, revenue increased by USD 1.2 billion and expenditures decreased by USD 200 million. Despite the rapid development of transportation by air, sea transportation remained the major mode of cargo transportation, accounting for 53 percent of the total volume of transportation services.

Revenue from freight by sea increased significantly. In the first half of 2020, the cross-border revenue and expenditures of freight by sea totaled USD 20.1 billion, a year-on-year increase of 6 percent. The deficit was USD 3.2 billion, narrowing by 24 percent. Among these, revenue was USD 8.5 billion, an increase of USD 1.1 billion. The increase was mainly for three reasons. First, there was a strong demand for oil transportation. In the first half of 2020, the average of the Baltic Crude Oil Transportation Index (BDTI) increased by 34 percent year on year. Among the top 10 companies enjoying the largest increase in sea freight revenue, three were oil transportation companies, which enjoyed an increase of USD 110 million in their cross-border revenue. Second, revenue of the leading freight logistics companies increased steadily. Among the top 10 companies enjoying the largest increase in sea freight revenue, three were freight logistics companies, which enjoyed an increase of USD 220 million in revenue. Third, revenue from special sea transportation continued to grow. For example, in terms of scale and comprehensive strength, one leading company in the industry, which owns the world's largest special cargo fleet, including semi-submersible vessels and multi-purpose heavy lift vessels, had ample orders in hand in the first half of 2020. Its revenue from sea transportation increased by approximately USD 70 million year on year.

Expenditures for passenger transport by sea fell sharply. In the first half of 2020, cross-border revenue and expenditures of passenger transport by sea totaled USD 83.32 million, a year-on-year decrease of 75 percent. Affected by the 40 percent drop in cross-border tourism payments, expenditures for passenger transport by sea fell to USD 60.86 million, a decrease of 81 percent. For example, in the first half of 2020expenditures for passenger transport by one leading cruise company decreased by USD 210 million, accounting for 81 percent of the total decline in this mode of transportation.

Development and innovation sin port services accelerated. Driven by larger container vessels, the scale of terminal operations, and technological progress, China's port companies made innovations in services and accelerated the pace of integration. Other transport services by sea, such as port maintenance, port services, transportation commissions, and packaging services, are developing rapidly. In the first half of 2020,cross-border revenue and expenditures totaled USD 5.8 billion, a year-on-year increase of 3 percent. Among these, revenue reached USD 4 billion, an increase of 4 percent and accounting for 32 percent of the total transportation revenue by sea; the surplus was USD 2.2 billion, one of the most important surplus items under trade in services.

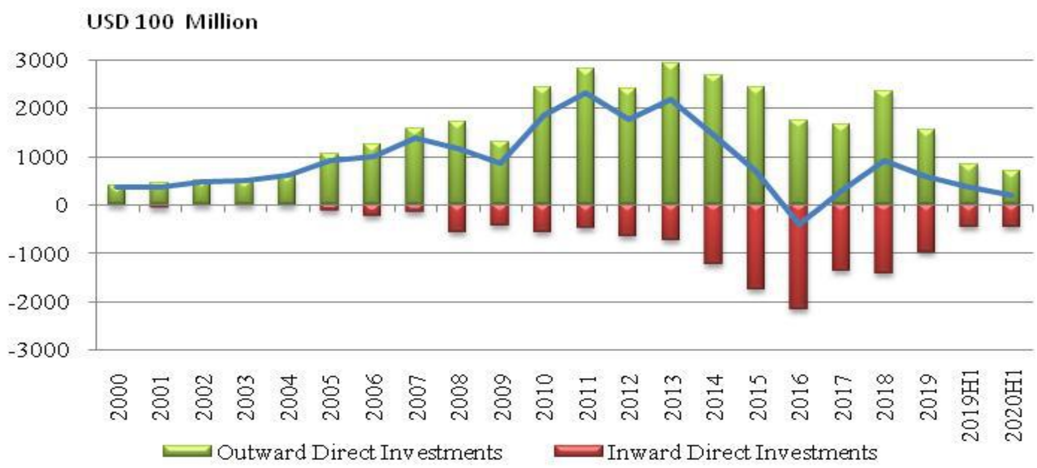
Sea-rail coordinated transportation showed advantages. During the epidemic, transport by air was blocked in various countries, while transport by rail developed at a high rate. Sea-rail combined transportation was favored and popular because of the flexibility and convenience. For instance, the China Railway Express can operate at a minimum of 41 to 50 train compartments. The freight rate per unit by rail is just one-third of that by air. According to the China National Railway Group statistics, in the first half of 2020 China Railway Express operated 5,122freight trains and delivered 460,000 TEUs of goods, an increase of 36 percent and 41 percent, respectively, year on year.

In the future, China will accelerate the healthy development of the shipping industry, increase the right to transport goods, encourage improvements in the quality and efficiency of national vessel services, and actively participate in competition. China will also promote in-depth cooperation between ports and shipping companies and will develop multi=modal transport by sea, railway, and roads to provide point-to-point services and to expand the industrial chain. Continuously improving the level of facilitation of trade and investment of shipping companies and facilitate in gcross-border fund settlements, China will effectively reduce the foreign-exchange management and settlement costs of transport by sea, port services, and multi-modal transportation industries to provide strong support for the development of China's freight services by sea.

(III) Direct Investments

Direct investments recorded a net inflow. In the first half of 2020, the net inflow of direct investments in China’s balance of payments totaled USD 21 billion (see Chart 2-9).

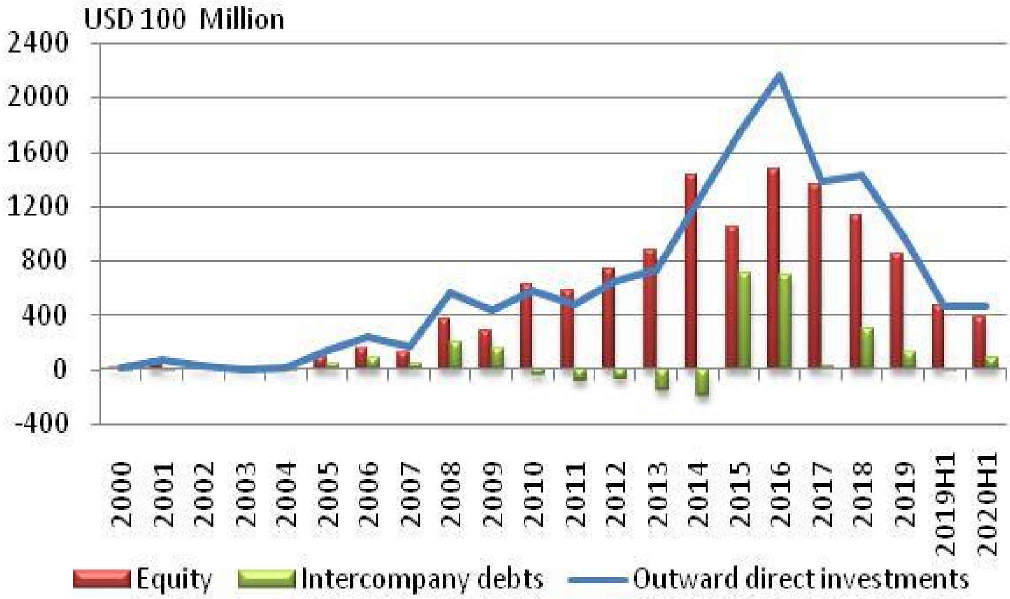
Chart 2-9 China’s Direct Investments



Source: State Administration of Foreign Exchange.

Outward direct investments (ODI) remained stable. In the first half of 2020, China's ODI (net increase in direct-investment assets) was USD 47.2 billion, an increase of 1 percent year on year (see Chart 2-10). Outward direct investments of domestic enterprises remained rational.

Chart 2-10 China's Direct-Investment Assets



Source: State Administration of Foreign Exchange.

In terms of the composition of direct investments, equity investments made up the major part and loan assets were minor. First, equity investments totaled USD 38.2 billion, an18 percent decline year on year. Among these, equity investments were USD 17.3 billion and USD 20.9 billion, respectively, during the first quarter and second quarters. Second, loans to affiliates amounted to USD 9 billion, of which USD 700 million was in the first quarter and USD 8.3 billion was in the second quarter. The increase in loan assets in the second quarter was mainly because in the second quarter many enterprises provided funds, through centralized operations of multinational companies and other capital allocation methods, to relieve affiliates.

In terms of sectors, outward direct investments by China's non-financial sector increased steadily, while those by financial sectors remained stable. **First,** direct-investment assets by non-financial sectors recorded a net increase of USD 38.9 billion, up 1percent year on year, mainly due to an increase of loan assets to affiliates. Among the domestic "going-global" industries, the manufacturing industry continues to rank in first place, accounting for 49 percent of the total. **Second**, direct-investment assets by the financial sector recorded a net increase of USD 8.2 billion, equivalent to that in the same period of the last year.

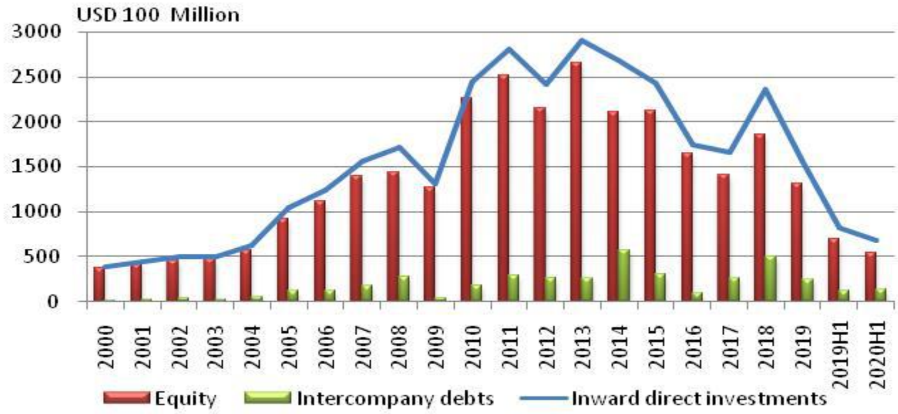
Inward foreign direct investments in China maintained large net inflows. In the first half of 2020, net inflows of inward direct investments (net increases in direct-investment liabilities) in China recorded USD 68.2 billion, with an increase in net inflows of loans from foreign affiliates and a decrease in equity investments.

In terms of the composition, inward foreign direct investments have been mainly composed of equity investments, supplemented by loans from foreign affiliates. In the first half of the year, net inflows of equity investments in China amounted to USD 54.4 billion (see Chart 2-11), and loans from affiliates recorded a net increase of USD 13.8 billion. According to UNCTAD’s forecast, global foreign direct investment will decrease by 40 percent in 2020, mainly because the Covid-19 epidemic and the global economic recession will affect the willingness and investment ability of cross-border enterprises. With regard to

China, with major progress made in the overall prevention and control of the epidemic, the economy recovering gradually, and the profit situation of enterprises improving, China is expected to attract foreign investment capital inflows.

In terms of sectors, the manufacturing industry and the non-bank financial industry are the main direct-investment absorbers of China's non-financial sector and financial sector. **First**, the non-financial sector absorbed USD 60.6 billion of inward direct investments, accounting for nearly 90 percent of the total. In the first half of 2020, the manufacturing industry absorbed 22 percent of the total inward direct investments to China’s non-financial sector, making it the biggest absorber of inward direct investments. The information and technology services industry, and the leasing industry and business service industry rank second and third among China's non-financial sector in terms of attracting in ward direct investments, accounting for 20 percent and 15percent, respectively. In the meantime, the main source of FDI remained the Hong Kong SAR, accounting for more than 70 percent of the total. The Hong Kong SAR was followed by Singapore and South Korea, accounting for 9 percent of the total. **Second,** direct-investment liabilities in the financial sector recorded a net inflow of USD 7.6 billion, down 13percent compared with the same period of the last year. Among these, the non-bank financial industry absorbed USD 4.6 billion of direct investments in China, an increase of 36 percent over the same period of 2019.

Chart 2-11 Direct-Investment Liabilities



Source: State Administration of Foreign Exchange.

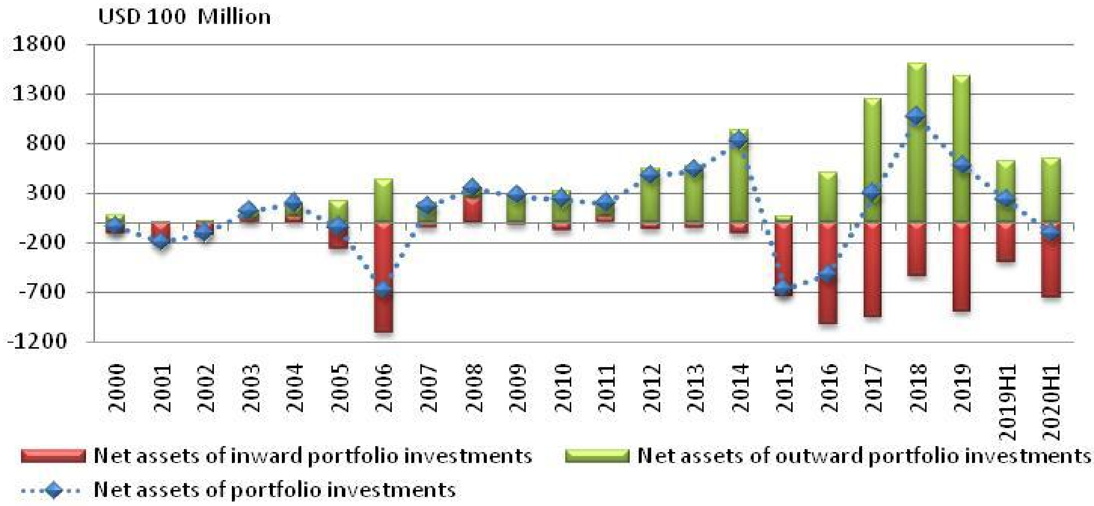
In recent years, China has become more closely connected with the world in terms of direct investments. On the one hand, as of the end of 2019 the stock of ODI was USD 20945 billion and China had established enterprises in 188 countries (regions). On the other hand, by the end of 2019 the stock of foreign direct investments in China reached USD 2928.1 billion, with relevant funds coming from more than 200 countries (regions). This fully reflects the profound proceeds of China's two-way direct investments, China’s continuing globalization, and the close interdependence of China with the rest of the world.

(IV) Portfolio Investments

Portfolio investments recorded small net outflows. In the first half of 2020, the net outflows of portfolio investments in China were USD 10.8 billion, compared with net inflows of USD 23 billion in the first half of 2019 (see Chart 2-12). In the first quarter of 2020, there was a large net outflow of portfolio investments. In the second quarter, portfolio investments rebounded and recorded a historical high of net inflows.

China's outward portfolio investments were active. In the first half of 2020, China's net outward portfolio investments (net increase in assets) were USD 75.1 billion, compared with USD 39 billion in the same period of 2019. Equity investments reached USD 45.9 billion, compared with USD 5.3 billion in the same period of 2019.Bond investments reached USD 29.2 billion, down 13 percent year on year.

Chart 2-12 Net Flows Under Portfolio Investments



Note: Positive outward portfolio investments indicate a decrease in equity or bond outward investments, and vice versa. Positive inward portfolio investments indicate an increase in equity or bond inward investments, and vice versa.

Source: State Administration of Foreign Exchange.

In terms of major channels for outward portfolio investments, first, China invested USD 39 billion in overseas equities via the Shanghai–Hong Kong Connect and the Mutual Recognition of Funds; second, domestic banks and other financial institutions invested USD 29.1 billion in overseas securities; third, QDII and RQDII invested a total of USD 5.2 billion in overseas securities; fourth, China invested USD 1.8 billion in domestically-issued panda bonds. The growth in outward portfolio investments indicates that Chinese investors had become more active and more sensitive to overseas investments.

Inward portfolio investments maintained net inflows. In the first half of 2020, inward portfolio investments recorded net inflows (net increase in liabilities) of USD 64.3 billion, up 4 percent year on year. Among these, net inflows of foreign investments in domestic equities amounted to USD 16.7 billion, up 129 percent; net inflows of bond investments amounted to USD 47.6 billion, down 13 percent.

In terms of the major channels for inward portfolio investments: first, foreign investors invested USD 55.6 billion in the domestic securities market, mainly via the Bond Connect and direct investments in the inter-bank bond markets; second, investments via the Stock Connect were USD 16.7 billion; third, QFII and RQFII recorded a total net outflow of USD 2.2 billion. In addition, banks' acceptance of us an celetters of credit decreased by USD 5 billion, and non-residents' holdings of stocks and bonds issued overseas by Chinese institutions, including RMB notes issued in Hong Kong SAR by the People's Bank of China, decreased by USD 900 million. In the first half of 2020, despite the impact of the Covid-19 epidemic on global investments, foreign portfolio investments in China increased year on year, indicating that the steady recovery of China's economy and the resumption of work and production was gradually increasing the attractiveness of the domestic securities market.

Box 3

In recent years, the scale of foreign capital inflows in China's securities market has increased with a reasonable structure

In recent years, China's economic growth has been stable, the securities market has gradually formed a high-quality, multi-channel opening pattern, and the convenience for foreign investors to invest in the domestic securities market for foreign investors has continuously improved. Since 2016, the inter-bank bond market has been fully opened to foreign institutional investors, the Shenzhen–Hong Kong Stock Connect and Bond Connect have been opened, and the restrictions on investment quotas for qualified foreign institutional investors have been lifted. At the same time, the overall return of China's bond market is higher than that of the major developed countries, the development potential of the equity market is large, the demand for foreign investors to allocate China's securities assets is rising, and the scale of foreign capital inflows is steadily increasing. Statistics from the SAFE show that from the first half of 2016 to the second half of 2020, the net holdings of China's bonds and stocks (including funds) increased by USD 467.3 billion. Since 2020, while the novel corona virus pneumonia has seriously affected the global economy, China's epidemic prevention and control and economic recovery have been improving. As the first major economy in the world to achieve positive economic growth, renminbi assets were more favored by overseas investors. In the first half of 2020, foreign investors increased their holdings of China's bonds and stocks by USD 72.9 billion.

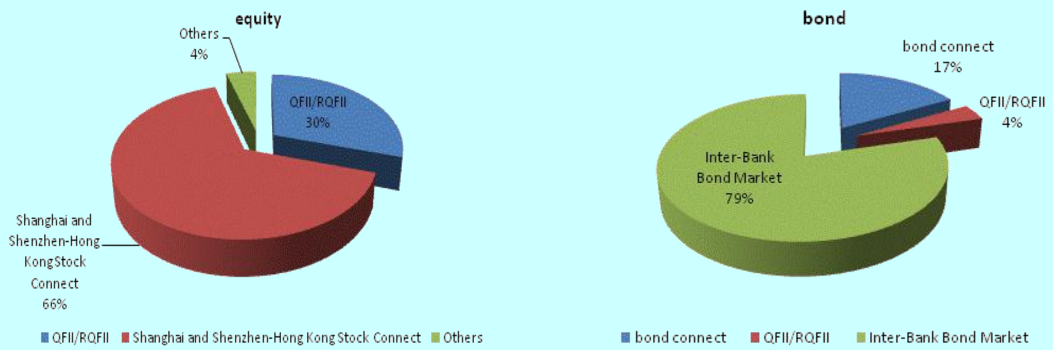
The scale of foreign investors' holdings of China's securities has increased significantly, and the proportion of foreign investors' positions in China's securities market has increased steadily. At the end of June 2020, the scale of domestic bonds and stocks held by foreign investors was USD 737.5 billion, 2.2 times higher than that at the end of 2015.In particular, the scale of domestic bonds held by foreign investors increased from USD 121.1 billion to USD 369.1 billion, marking a doubling of growth, and its proportion in the custody balance of the domestic bond market increased from 1.6 percent to 2.4 percent. The size of domestic shares held by foreign investors increased from USD 108.8 billion US to USD 368.4 billion, marking growth of 2.4 times, and its proportion in the total market value of A-shares in circulation increased from 1.5 percent to 4.5 percent (see Figure C3-1).

Figure C3-1 Stock of Overseas Investors Investing in the Domestic Securities Market

Source: State Administration of Foreign Exchange.

Foreign investors mainly invest in China's securities market through direct entry into the inter-bank bond market（CIBM）and the Stock Connect. Since 2016, the CIBM has gradually become the main channel for overseas investors to invest in the domestic bond market; after the opening of the Shenzhen–Hong Kong Stock Connect, the Shanghai–Hong Kong Stock Connect, and the Shenzhen–Hong Kong Stock Connect have become the main channels for overseas investors to allocate domestic stock assets. At the end of June 2020, 79 percent (USD 293.2 billion) of domestic bonds held by foreign investors went through the CIBM channel, with the scale increasing by two times compared with that at the end of 2015; 66 percent (USD 242.2 billion) of domestic stocks held by foreign investors went through the Shanghai and Shenzhen Stock Connect Channels, with a nearly twelvefold increase compared with the end of 2015 (see Figure C3-2).

Figure C3-2Channel Structure of Overseas Investors Investing in the Domestic Securities Market at the End of June 2020

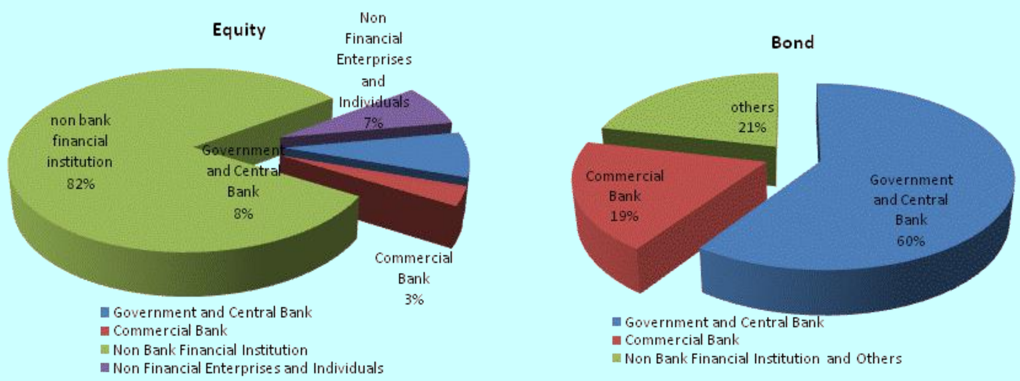


Source: State Administration of Foreign Exchange.

The structure of foreign holders is basically stable. The main foreign investors in

the domestic stock market are from the non-bank financial sector, while foreign governments and central banks are the main investors in the domestic bond market. At the end of June 2020, 82 percent (USD 300.5 billion) of foreign investors' equity investments in China were held by non-bank financial investors, with a scale nearly five times higher than that at the end of 2015. Among China's bond investments, 60 percent (USD 219.8 billion) was held by foreign governments and central banks, with a scale more than twice that of the end of 2015 (see Figure C3-3).On the whole, since 2015, foreign non-bank financial investors have been the main force among the stock holders, and the proportion of their position has gradually increased; among the debt holders, the structure dominated by foreign governments and central banks has remained stable and the role of the "ballast stone" has been significant.

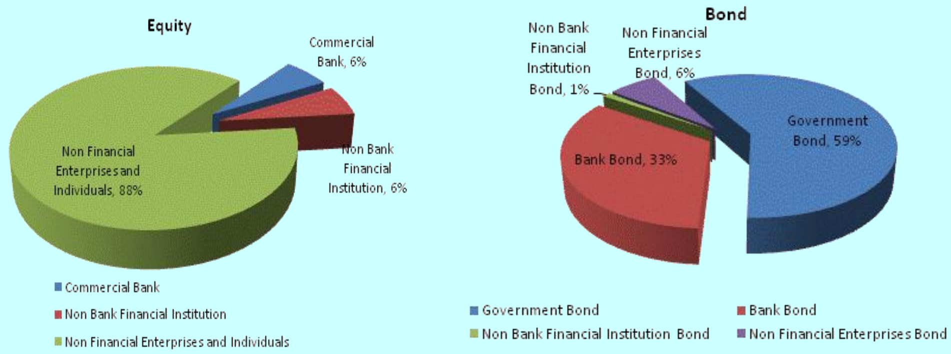
Figure C3-3 Structure of Foreign Holders at the End of June 2020



Source: State Administration of Foreign Exchange.

The structure of investment targets held by foreign investors is stable, mainly consisting of stocks issued by domestic non-financial companies and bonds issued by governments, which is basically the same as the structure of foreign investment targets in the major international markets; while long-term bonds are increasingly favored by foreign investors. Since 2016, with a stable proportion, 90 percent of the market value of foreign investors' stock positions have become stocks issued by domestic non-financial enterprises. In bond positions, treasury bonds are the dominator and the proportion increased slightly. At the end of June 2020, 59 percent (USD 217.9 billion) of bonds held by foreign investors were treasury bonds, more than four times that at the end of 2015; 91 percent (USD 336.6 billion) of bond positions were long-term bonds, which was twice as many as that at the end of 2015 (see Figure C3-4).

Figure C3-4 Structure of Domestic Securities Held by Foreign Investors at the End of June 2020

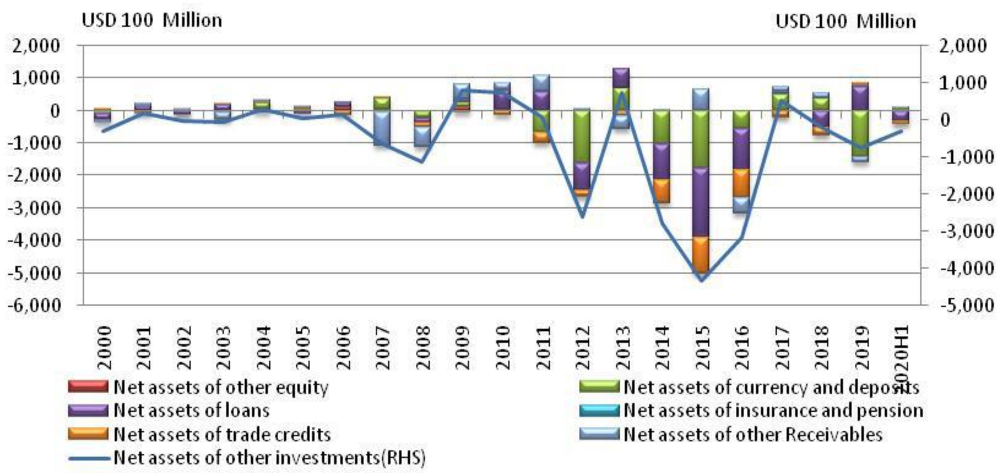


Source: State Administration of Foreign Exchange.

(V). Other Investments

Other investments showed a deficit. In the first half of 2020, other investments registered a deficit (an increase in net assets) of USD 30.3billion (see Chart 2-13).In particular, currency and deposits recorded a net inflow of USD 5.8 billion, loans recorded a net outflow of USD 31.5 billion, trade credits recorded a net outflow of USD 8.9 billion, and other account payables and receivables recorded a net inflow of USD 6.2 billion.

Chart 2-13 Net Flows of Other Investments



Source: State Administration of Foreign Exchange.

Assets under other investments registered a net out flow. In the first half of 2020, external assets under other investments recorded a net outflow of USD 65.2 billion, compared to USD 10.5 billion in the same period of 2019. In particular, overseas loans registered a net outflow of USD 52.3 billion, a net decrease of USD 19 billion from the same period of 2019, mainly due to the domestic banks' outward lending to ease the liquidity shortage of overseas branches. Trade-credit assets, such as export receivables, registered a net inflow of USD 31.3 billion, down 47 percent year on year. This was mainly because in the first quarter, affected by the pandemic, goods exports of foreign trade enterprises experienced a periodic decline, making the account receivables decrease. However, with exports recovering in the second quarter, the account receivables brought about by exports increased. Overseas deposits recorded a net flow of USD 26.4 billion, down 46 percent year on year. Other account receivables registered a net outflow of USD 14.7 billion, down 10percent year on year.

Liabilities under other investments registered a net inflow. In the first half of 2020, other investments from abroad registered a net outflow of USD 34.8 billion, compared to USD 23.3 billion in the same period of 2019. In particular, currency and deposit liabilities recorded a net inflow of USD 32.2 billion, compared to a net outflow of USD 42.8 billion in the same period of2019; trade-credit liabilities such as import payables recorded a net outflow of USD 40.3 billion, mainly because in the first quarter enterprises paid the import account payables of the previous periods, while in the second quarter the increases in account receivables were limited by the declining imports; loan liabilities recorded a net inflow of USD 20.9 billion, down 66percent, mainly because inter-bank borrowing from overseas banks declined.

Box 4

China's external debt has grown steadily, with cross-border financing for enterprises becoming more convenient

At the end of June 2020, China's outstanding full-scale external debt was USD 2,132.4 billion, up by 3.7 percent year on year, with an increase of USD 75.1 billion over the end of 2019.The steady growth of the external debt is in line with the objective need of China's economic development and reflects the effects of China's economic opening-up, its external debt facilitation policy, and recognition of international investors on China's market. At present, the scale of external debt is reasonable, with the structure continuously optimized; the main safety indicators are all within the internationally recognized safety line, and the risks from the external debt are generally under control.

(I) In the first half of the year, the growth rate of the external debt was stable and the structure of the external debt continued to improve

On the whole, external debt growth was stable. In the first and second quarters of 2020, the total external debt increased by USD 37.3 billion and USD 37.8 billion, respectively, with the quarter-on-quarter growth rate at 1.8 percent. The quarterly growth rate in 2019 was 0.3 percent, 1.3 percent, 1.7 percent, and 0.4 percent, respectively. The overall growth rate was stable.

The structure of the external debt continued to improve. Compared with the end of 2019, the currency structure and the term structure of the external debt both have improved. In terms of the currency structure, the foreign-currency external debt was USD 1,328.7 billion, accounting for 62 percent of the total external debt; the domestic currency external debt was USD 803.7 billion, or 38 percent of the total and up 3 percentage points from the end of 2019.In terms of the term structure, the medium- and long-term external debt was USD 909 billion, or 43 percent of the total; the short-term external debt stood at USD 1223.4 billion, or 57 percent of the total, down 2 percentage points from the end of 2019.

The increase in the bond and currency deposit balance is the main source of the growth of the external debt. In the first half of 2020, bonds and bond and currency deposit balances increased by USD 37.4 billion and USD 30.6 billion, respectively, contributing 50 percent and 41 percent, respectively, to the growth of the outstanding external debt. Against the background of the global negative interest rates, China's economy has continued to recover steadily. The bond market has continued to open up and RMB bonds are favored by foreign investors. In addition, as the Sino-US rate differential continued to widen, non-resident deposits in domestic banks have increased.

(II) Promoting reform to facilitate cross-border financing and expand the financing scope of enterprises

In the first half of 2020, the overseas epidemic situation and the world economic condition became more complicated, and uncertainties in the external environment increased. The People's Bank of China and the SAFE have continued to promote reform of cross-border financing facilitation, providing strong support for the development of the real economy and the resumption of enterprise production.

First, we raised the macro-prudential regulation parameters for cross-border financing of domestic institutions to provide more space for enterprises to raise funds overseas. In March 2020, the People's Bank of China and the SAFE raised the macro-prudential adjustment parameters of cross-border financing from 1 to 1.25.After this policy adjustment, the upper limit of the risk-weighted balance of cross-border financing for enterprises was raised from 2 times to 2.5 times the original net assets, and the scope for domestic institutions, excluding government financing platforms and real-estate enterprises, for borrowing external debt has been further expanded. In the current environment of low interest rates in overseas markets, this policy adjustment provides more space for enterprises to raise funds abroad.

Second, we expanded the pilot scope of the external debt facilitation quotas and effectively supported high-tech enterprises in using overseas financing. To support light assets and high-growth high-tech enterprises' cross-border financing demands, improve the convenience and flexibility of cross-border financing, and reduce the cost of enterprise financing, on the basis of the experience of the pilot external debt facilitation quotas in Beijing Zhongguancun, the SAFE extended the pilot zones to Shanghai (free trade area), Hubei (free trade area and the Wuhan East Lake New Technology Development Zone), and Guangdong and Shenzhen (Greater Bay Area), to allow qualified high-tech enterprises to independently borrow external debt within no more than the equivalent of USD 5 million. At the same time, the SAFE further streamlined the external debt policies of Haidian District, Zhongguancun Science City, Beijing, by raising the amount of external debt facilitation from USD 5 million to USD 10 million.

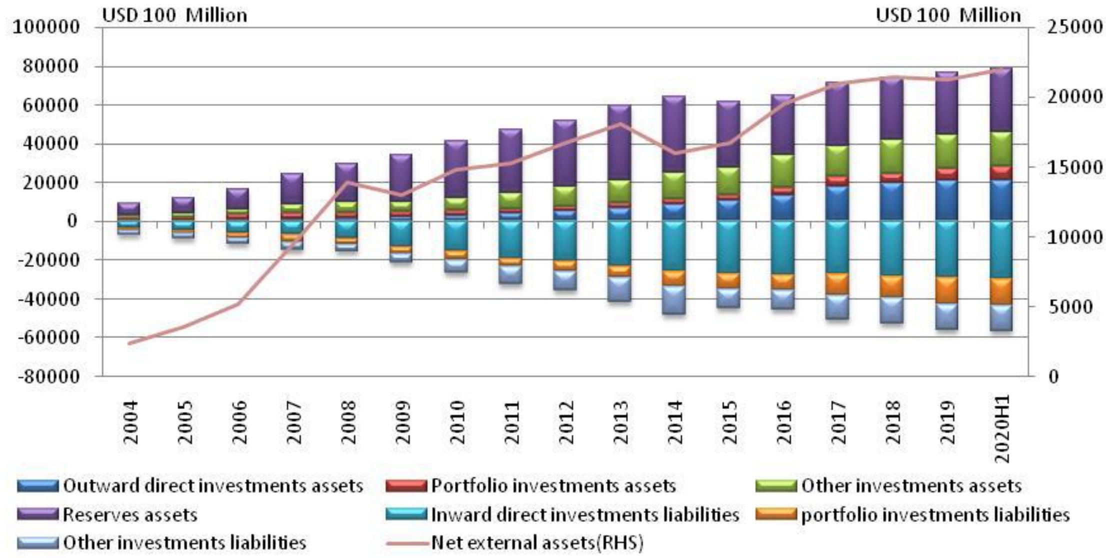
Third, the SAFE carried out a one-time foreign debt registration pilot program to save enterprise costs. To further promote the reform of "Delegation, Regulation, and Service" and to facilitate cross-border trade financing, since January 2020 the SAFE has carried out a one-time foreign debt registration pilot in Guangdong, Shenzhen (Greater Bay Area) Hainan, Hubei (free trade area and the Wuhan East Lake New Technology Development Zone), Beijing Zhongguancun Science City), Shanghai (Lingang New Experimental Zone in the Free Trade Area), and other pilot areas. The pilot enterprises have cancelled the one-by-one registration and management requirement for external debts. The pilot enterprises can do a one-time registration of their external debts at the local SAFE office and borrow foreign debt in dependently within the registered amount. One-time external debt registration simplifies the business process of handling external debt and saves time, manpower, financial, and other costs for the pilot enterprises.

Since the second quarter, the effects of the reform policies for external debt facilitation reform have gradually appeared, and the external debt of enterprise sectors has steadily increased. In general, the reform of external debt facilitation has expanded the financing scope of market entities. In the future, enterprises can make full use of both domestic and international resources and markets to enrich financing channels, reduce financing costs, and carry out various production and operational activities more efficiently according to their own will and needs.

III. International Investment Position

China's external financial assets and liabilities[4] were both on the rise. At end-June 2020, China's external financial assets reached USD 7860.2 billion, up 1.9 percent from end-2019; external liabilities reached USD 5660.5 billion, up 1.3 percent; and net assets reached USD 219.97 billion, up 3.6 percent (see Chart 3- 1).

Chart 3-1 External Financial Assets, Liabilities, and Net Assets



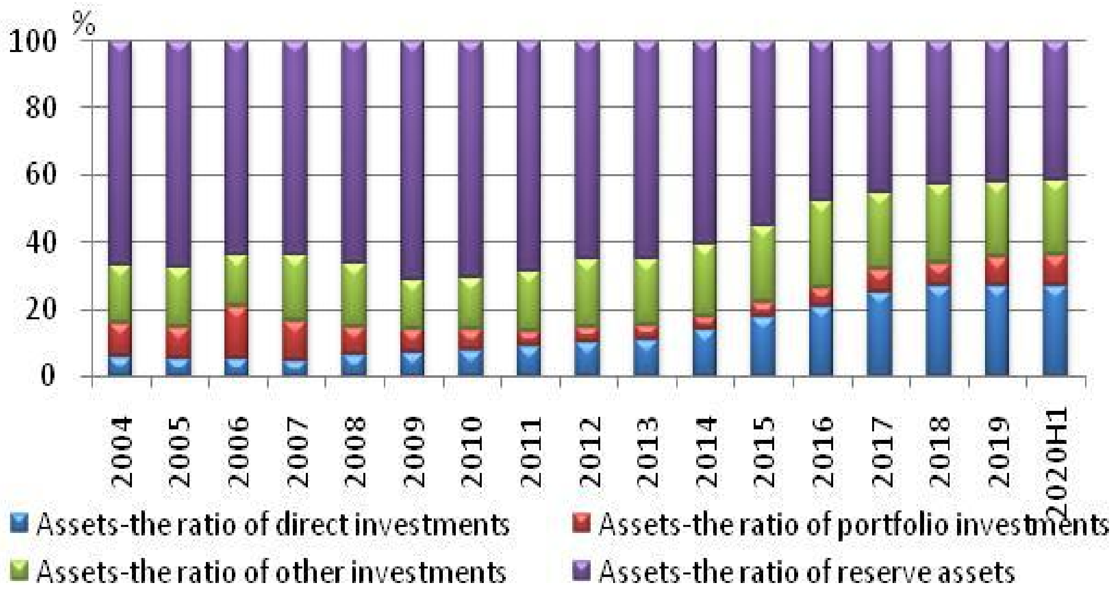
Source: State Administration of Foreign Exchange.

Reserve assets remained the largest component of total external assets, and private-sector holdings continued to rise. Among the external financial assets, at end-June2020reserve assets amounted to USD 3243.3 billion, up 0.6

[4]External financial assets and liabilities include direct investments, portfolio investments, and other investments, such as deposits and loans. Outward direct investments are included as financial assets because the equity issued by non-resident direct-investment enterprises and held by domestic investors is the same type of financial instrument as the equity investment in portfolio investments. The difference is that direct investments require a higher threshold of equity holdings to reflect a significant influence or control over the production and operations of the enterprises. Inward direct investments belong to external financial liabilities because foreign investors hold equity in foreign-owned companies.

percent from end-2019. As the largest component of external financial assets, reserve assets accounted for 41 percent of China's total external financial assets, down 1 percentage point from end-2019. Direct-investment assets amounted to USD 2124.7 billion, accounting for 27 percent of total assets, the same proportion as that at end-2019. Portfolio-investment assets amounted to USD 700.6 billion, accounting for 9 percent, up 1 percentage point. Financial-derivative assets amounted to USD 9.9 billion, accounting for 0.1percent.Other investments, such as loans and deposits, amounted to USD 1781.7 billion, accounting for 23 percent, the same proportion as that at end-2019 (see Chart 3-2). At end-June 2020, RMB-denominated assets in China's external assets amounted to USD 461.4 billion, accounting for 10 percent of external non-reserve assets, and the proportion remained stable.

Chart 3-2 Changes in the Structure of China's External Financial Assets



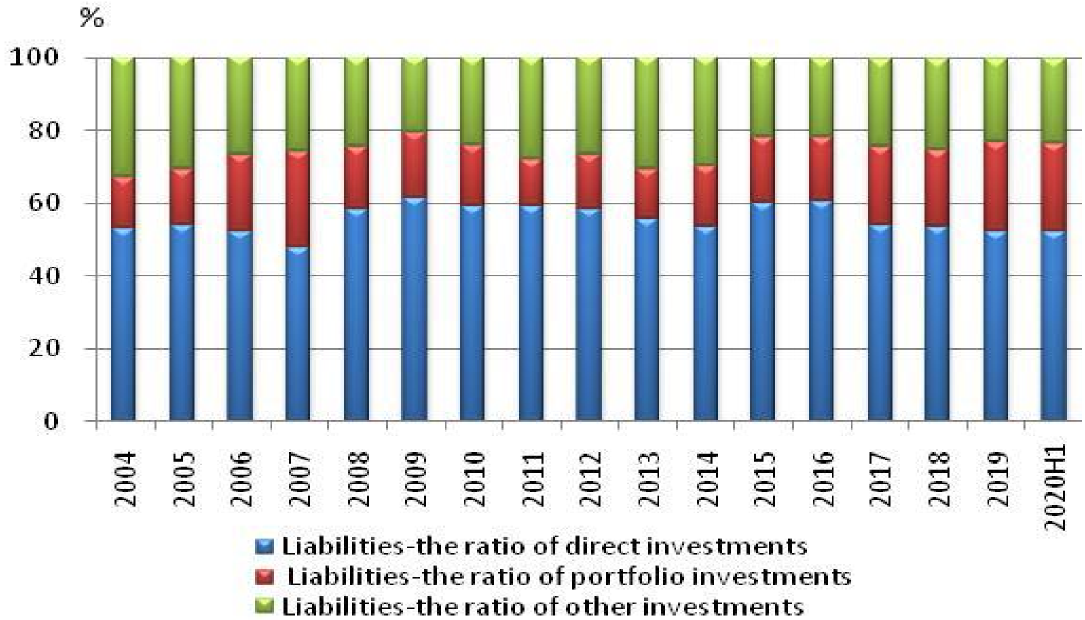
Source: State Administration of Foreign Exchange.

Foreign direct investments remained the major item in external

liabilities, and the proportion of portfolio investments in the domestic market grew steadily. Among the external liabilities, FDI[5] totaled USD 2947.2 billion at end-June 2020, up 0.7 percent from end-2019, accounting for 52 percent of total external liabilities and remaining the largest component. Foreign portfolio-investment liabilities amounted to USD 1378.3 billion, accounting for 24 percent, and foreign investments in China’s domestic securities market continued to increase. At end-June 2020, foreign investors’ holdings of China’s domestic securities were approximately USD 737.5 billion. Among these, foreign holdings of stocks accounted for 4.5 percent of the total market value of A-shares, up 0.1 percentage point from end-2019; holdings of bonds accounted for 2.4 percent of total domestic bonds under custody, also up0.1 percentage point. The steady opening up and the deepening reform of China's financial market have contributed to the increase. In addition, RMB-denominated liabilities totaled USD 742 billion, accounting for 54 percent of the total liabilities under securities and an increase of 15 percentage points from end-2015. RMB internationalization makes RMB products more attractive to investors. Other investment liabilities, such as loans and deposits, amounted to USD 1324.4 billion, accounting for 23 percent and the same proportion as that at end-2019 (see Chart 3-3).

[5]The inward FDI positionincludes FDI stocks of both the non-financial sector and the financial sector. The position also reflects the impact of revaluations.

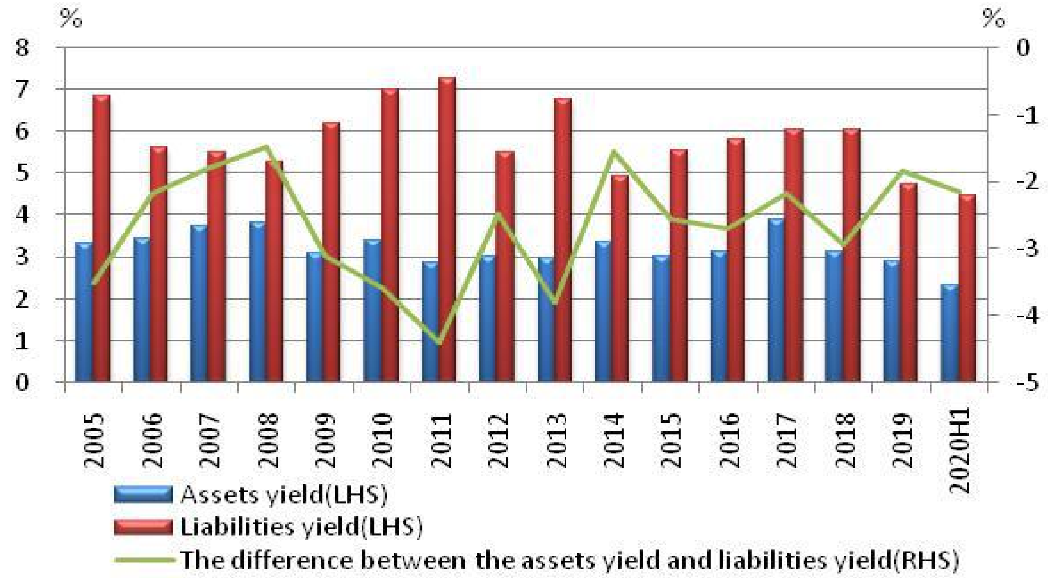
Chart3-3 The Structure of External Liabilities



Source: State Administration of Foreign Exchange.

Due to the wide spread of the Covid-19 epidemic, outward investment income decreased, but inward investment income increased. At end-June 2020, China's net investment income recorded a deficit of USD 35.1 billion (see Chart 3-4). In particular, revenue from outward investments totaled USD 91.1 billion and income payments for inward investments totaled USD 126.2 billion. In the second quarter of 2020, China was the first major economy to resume work and production. With a relatively high rate of return, FDI continued to flow into China. In addition, when the major economies adopted negative interest rates, RMB assets continued to provide relatively high returns and attracted foreign investors to invest in China.

Chart 3-4 Changes in the Rate of Return on China's External Assets and Liabilities



Source: State Administration of Foreign Exchange.

Table 3-1 China's International Investment Position at the End of June 2020

Unit: US $100 million

	Line No.	2020H1
Net International Investment Position[6]	1	**21,997**
Assets	2	**78,602**
1 Direct investments	3	**21,247**
1.1 Equity and investment fund shares	4	18,023
1.2 Debt instruments	5	3,224
1.a Financial sector	6	2,751
1.1.a Equity and investment fund shares	7	2,664
1.2.a Debt instruments	8	87
1.b Non-financial sector	9	18,496
1.1.b Equity and investment fund shares	10	15,359
1.2.b Debt instruments	11	3,137
2 Portfolio investments	12	**7,006**
2.1 Equity and investment fund shares	13	4,106
2.2 Debt securities	14	2,900
3 Financial derivatives (other than reserves) and employee stock options	15	**99**
4 Other investments	16	**17,817**
4.1 Other equity	17	84
4.2 Currency and deposits	18	4,162

[6] Net position refers to assets minus liabilities; "+" refers to net assets; "-" refers to net liabilities. The notations in this table are based on the principle of rounding.

4.3 Loans	**19**	7,488
4.4 Insurance, pensions, and standardized guarantee schemes	**20**	164
4.5 Trade credits and advances	**21**	5,290
4.6 Other accounts receivable	**22**	628
5 Reserve assets	**23**	**32,433**
5.1 Monetary gold	**24**	1,108
5.2 Special drawing rights	**25**	110
5.3 Reserve position in the IMF	**26**	96
5.4 Foreign currency reserves	**27**	31,123
5.5 Other reserve assets	**28**	-3
Liabilities	**29**	**56,605**
1 Direct investments	**30**	**29,472**
1.1 Equity and investment fund shares	**31**	26,902
1.2 Debt instruments	**32**	2,570
1.a Financial sector	**33**	1,633
1.1.a Equity and investment fund shares	**34**	1,447
1.2.a Debt instruments	**35**	186
1.b Non-financial sector	**36**	27,839
1.1.b Equity and investment fund shares	**37**	25,455
1.2.b Debt instruments	**38**	2,384
2 Portfolio investments	**39**	**13,783**
2.1 Equity and investment fund shares	**40**	8,471
2.2 Debt securities	**41**	5,312
3 Financial derivatives (other than reserves) and employee stock options	**42**	**107**
4 Other investments	**43**	**13,244**
4.1 Other equity	**44**	0
4.2 Currency and deposits	**45**	4,545
4.3 Loans	**46**	4,827
4.4 Insurance, pensions, and standardized guarantee schemes	**47**	147
4.5 Trade credits and advances	**48**	3,241
4.6 Other accounts payable	**49**	388
4.7 Special drawing rights	**50**	96

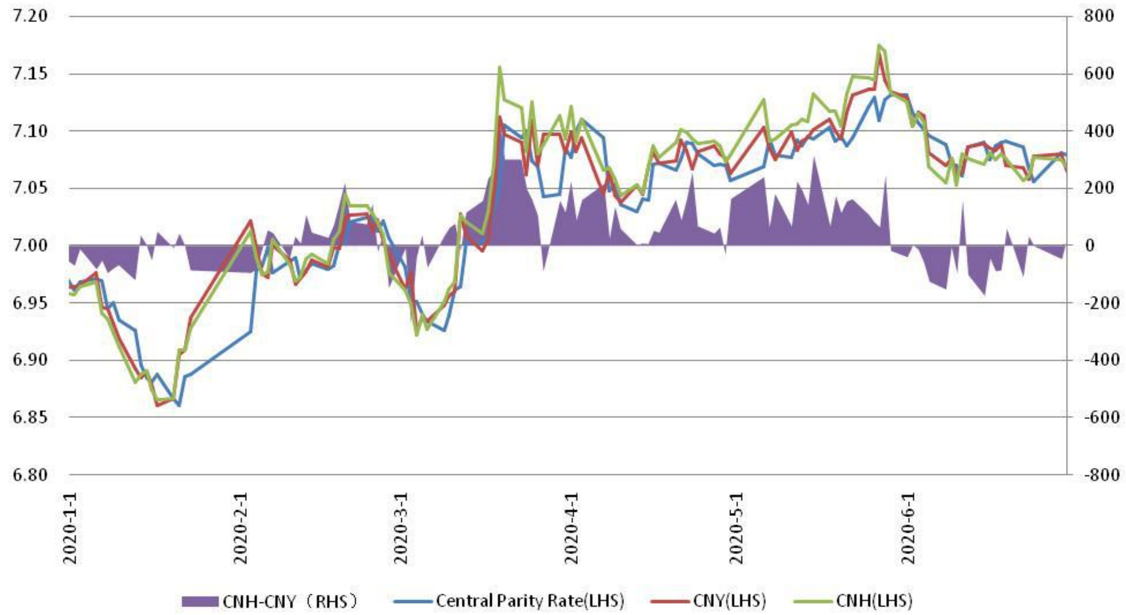
Source: State Administration of Foreign Exchange.

IV. The Operation of the Foreign-Exchange Market and the RMB Exchange Rate

(I) Trends in the RMB Exchange Rate

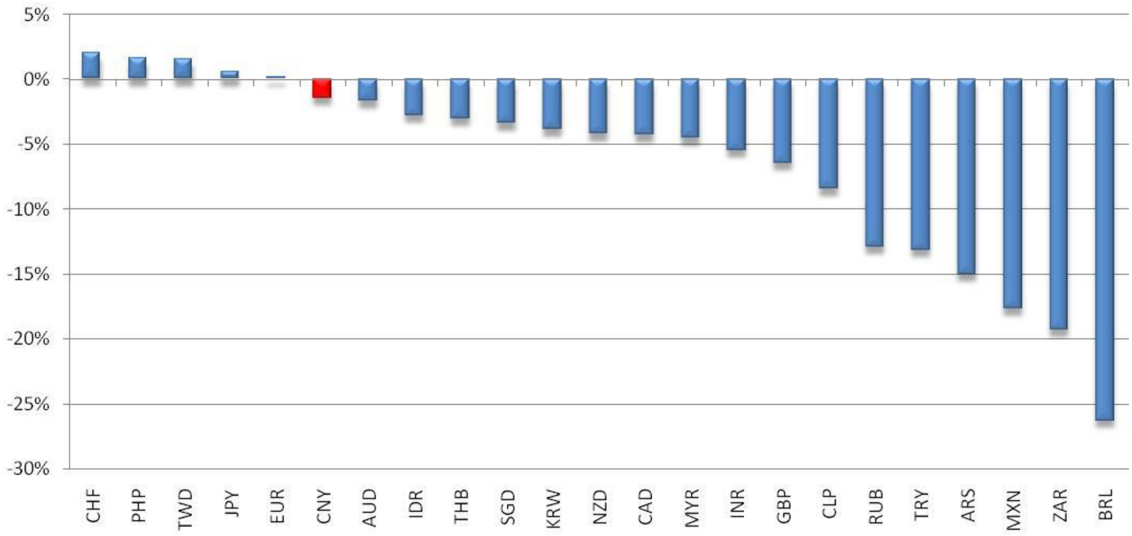
The RMB exchange rate was relatively stable against the USD. On the whole, the exchange rate of the RMB against the USD remained stable. Since 2020, the COVID-19 epidemic has resulted in a global economic recession, causing serious fluctuations in the international financial market and producing two-way fluctuations in the exchange rate of the RMB against the USD. At the end of June, the central parity of the RMB against the US dollar was 7.0795, a depreciation of 1.46 percent compared with that at the end of last year.CNY and CNH spot trading prices have depreciated by 1.44 percent and 1.54 percent in total (see Chart 4-1). The average daily spread in the domestic and foreign markets is 101 basis points, slightly higher than the average daily spread during the whole of last year (96 basis points).Although the RMB has weakened against the USD, it remains a solid performer among global currencies (see Chart 4-2).

Chart 4-1 Trends in the RMB Spot Exchange Rate Against the USD in the Domestic and Offshore Markets, 2020H1



Sources: CFETS, Reuters.

Chart 4-2 Exchange-Rate Fluctuations of the Major Developed and Emerging Market Currencies Versus the USD in 2020H1

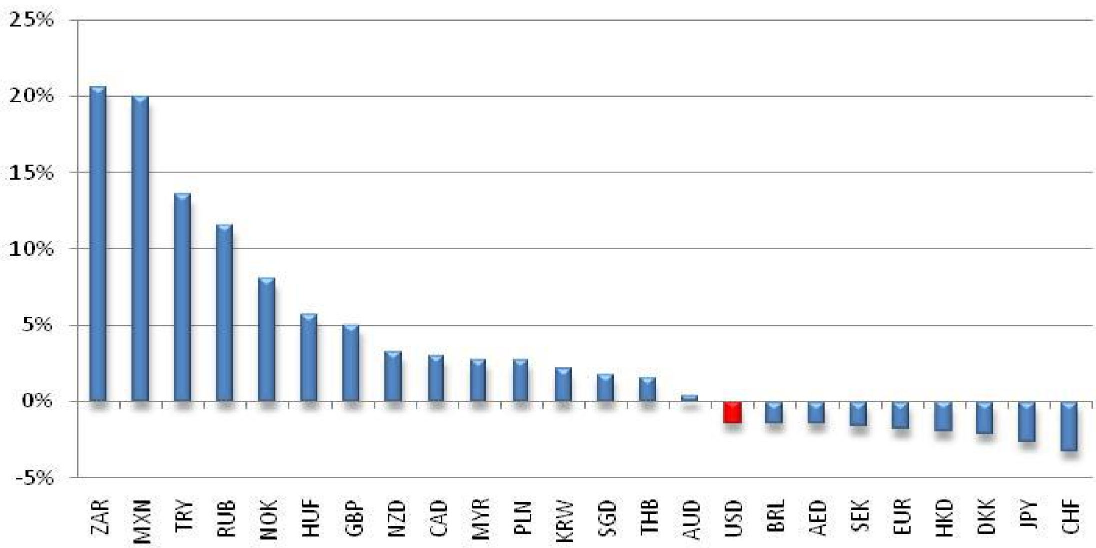


Source: Bloomberg.

The RMB exchange rate versus the other major currencies went in different directions. At the end of June 2020, the mid-price of the RMB exchange rate against the EUR, 100JPY, GBP, AUD, and CAD stood at

7.9610,6.5808,8.7144,4.865, and 5.1843, respectively, a depreciation of 1.83 percent, a depreciation of 2.62 percent, an appreciation of 5 percent, an appreciation of 0.38 percent, and an appreciation of 3.04 percent, respectively, compared with the previous year(see Chart 4-3).

Chart 4-3The Central Parity of the RMB Against the Major Developed and Emerging Market Currencies

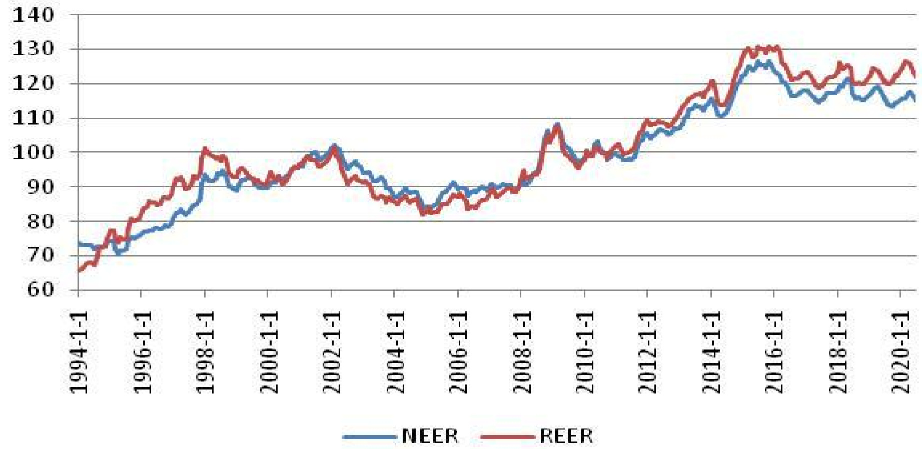


Source: CFETS.

The RMB exchange rate was basically stable against the basket of currencies. According to CFETS data, at the end of June 2020 the RMB exchange-rate indexes of the CFETS, the BIS basket of currencies, and the SDR basket of currencies were 92.05,95.87and 90.78,respectively, an appreciation of 0.72percent, an appreciation of 0.72 percent, and a depreciation of 0.27 percent, respectively, from the end of the previous year.

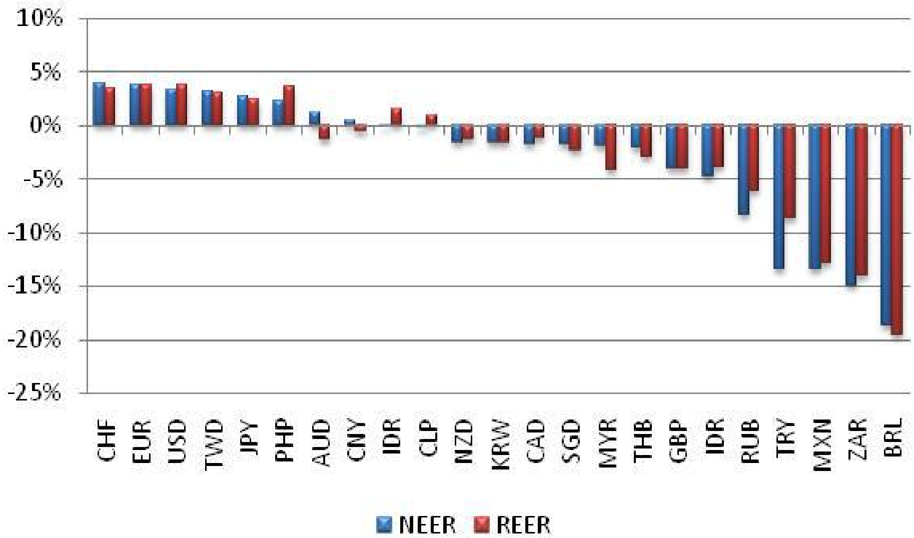
According to the BIS, the nominal effective exchange rate of the RMB appreciated by 0.2 percent in the first half of 2020. Deducting for inflation, the real effective exchange rate of the RMB depreciated by 0.4percent (see Chart 4-4). The RMB is one of the most stable currencies among the 60 global currencies monitored by the BIS (see Chart 4-5).

Chart 4-4 Trends in the Effective RMB Exchange Rate



Source: BIS.

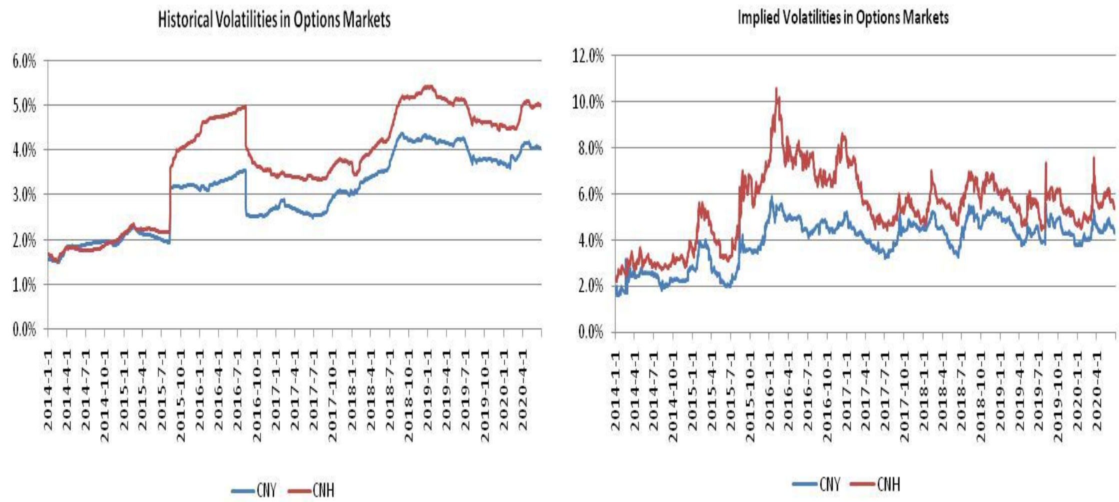
Chart 4-5Effective Exchange-Rate Movements of theMajor Developed and Emerging Market Currencies in the First Half of 2020



Source: BIS.

The two-way fluctuation of the RMB exchange rate has become more flexible. In the first half of the year, the RMB exchange rate rose and fell, floating in both directions more flexibly, thus effectively functioning as an automatic stabilizer in international payments. At the end of June 2020, the one-year historic volatility of the RMB exchange rate against the USD in the domestic and offshore markets stood at 4.0 percent and 5.0 percent, up 0.3 percent and 0.4 percent from the beginning of 2020, respectively, which was a historical high historical. From the beginning of the year, the implied volatility in the options market was 4.3 percent and 5.4 percent, up 0.5 and 0.6 percentage points, respectively (see Chart 4-6).

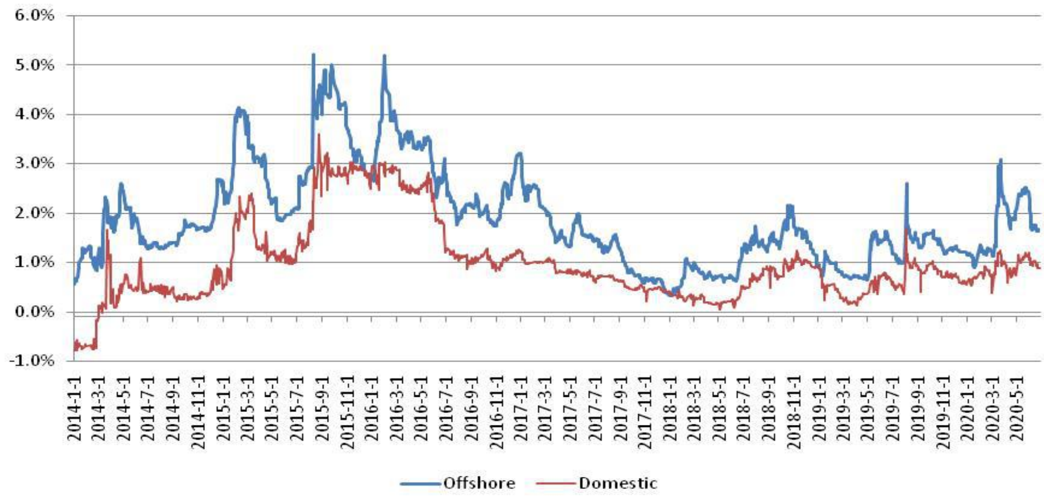
Chart 4-6 The Volatility of the 1-Year RMB Exchange Rates Against the USD in the Domestic and Offshore Markets



Source: Bloomberg.

The options markets showed that RMB exchange-rate expectations were stable. In the first half of 2020, domestic and offshore risk reversals (the difference between the volatility of the USD call / RMB put options and the USD put /RMB call options)first rose and then fell, and the annual high was much lower than the historical high, indicating that exchange-rate expectations were relatively stable. At the end of June, the risk reversal indicators at home and abroad were 0.88 percent and 1.48 percent, respectively, compared with 0.61 percent and 1.18 percent at the end of the last year (see Chart 4-7).

Chart 4-7 The 1-Year Risk Reversals of the RMB Against the USD in the Domestic and Offshore Options Markets



Source: Bloomberg.

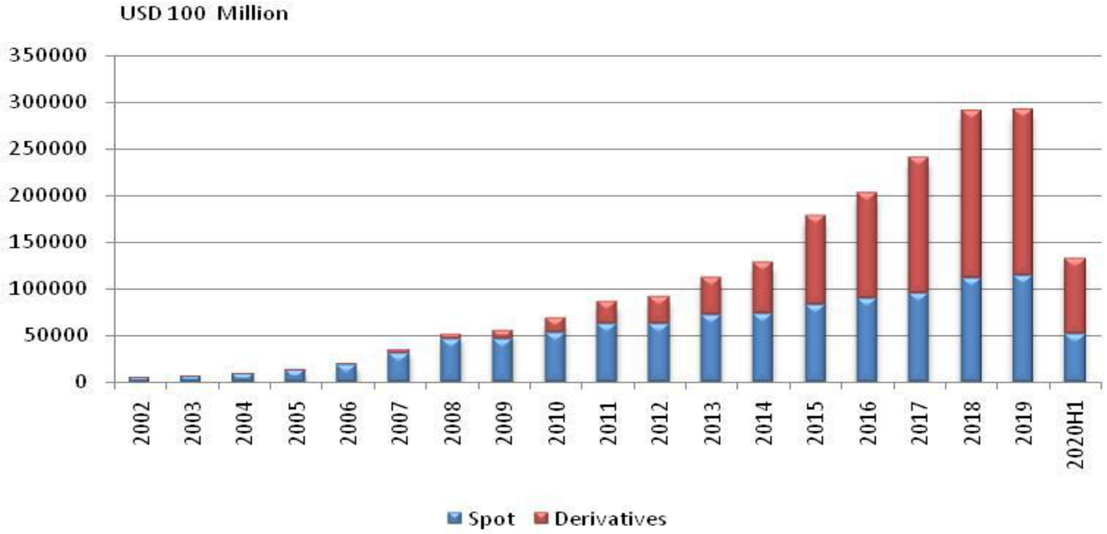
(II) Transactions in the Foreign-Exchange Market

In the first half of 2020, the cumulative trading volume of the RMB/foreign-currency market totaled USD13.17 trillion, down 13.7percent from the same period of the previous year (see Chart 4-8), with an average daily trading volume of USD112.6 billion. Market transactions contracted significantly in the first quarter due to the impact of the epidemic, but they gradually picked up in the second quarter as the economy resumed work and production.In the first half of the year, the total trading volume in the client market and the inter-bank market were USD2.10 trillion and USD 11.07trillion,[7] respectively. The resilience of real economic activity and the increased

[7]The client market uses the total volume of both purchases and sales of foreign exchange. The inter-bank market uses the unilateral trading volume. The same as below.

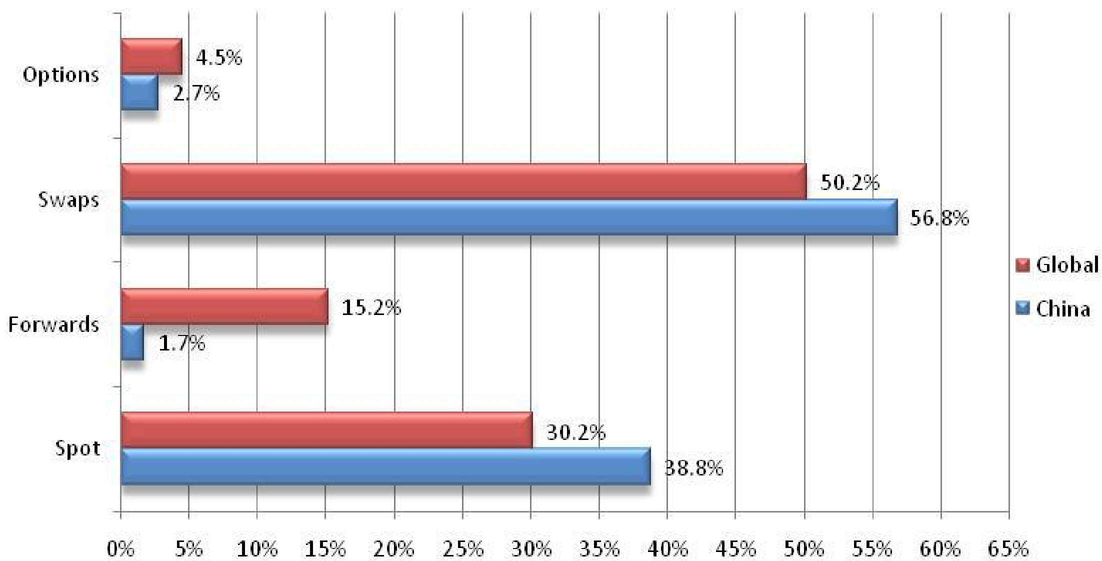
flexibility of the RMB exchange rate continued to release corporate demand for foreign-exchange transactions. Spot and derivative transactions witnessed a trading volume of USD5.11trillion and USD8.07trillion, respectively (see Table 4-1). Derivatives accounted for 61percent of the share of total transactions in the foreign-exchange market (see Chart 4-9).

Chart 4-8 Trading Volume in China's Foreign-Exchange Market



Sources: SAFE, CFETS.

Chart 4-9A Comparison of the Structure of Products in the Domestic and Global Foreign-Exchange Markets



Note: China's data are for the first half of 2019, and the global data are adopted from the

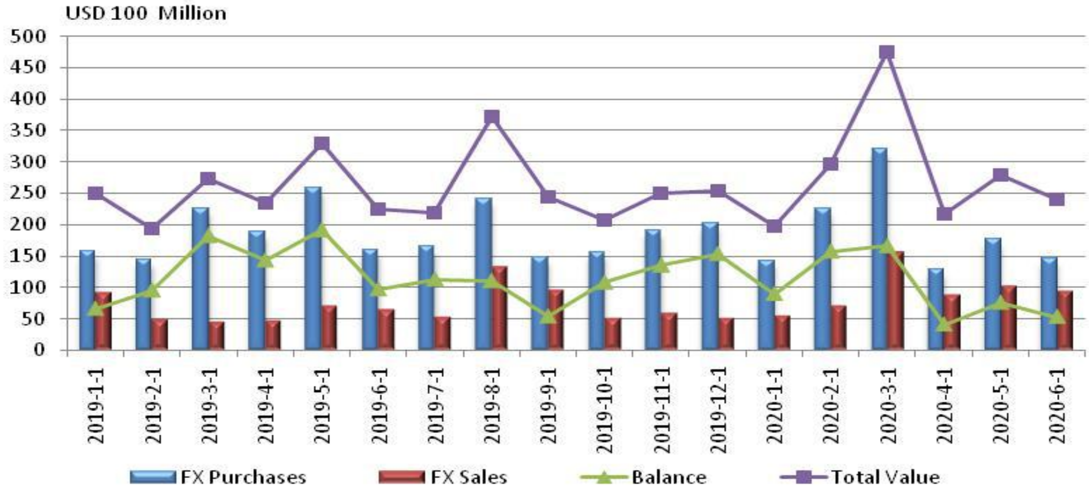
BIS survey in April 2019.

Sources: SAFE, CFETS, BIS.

Spot foreign-exchange transactions fell slightly. In the first half of the year, the spot foreign-exchange market saw a trading volume of USD 5.11 trillion, down 9 percent from the same period of the previous year. In terms of market distribution, spot purchases and sales of foreign exchange in the client market totaled USD 1.68 trillion (including the banks' proprietary trading, but excluding the performance of forwards), up 2 percent from the previous year. The spot inter-bank foreign-exchange market saw a trading volume of USD 3.43 trillion, down 14 percent from the previous year. The share of USD transactions was 96 percent.

Foreign-exchange forward transactions increased. In the first half of the year, the forward market saw a cumulative trading volume of USD 221.7billion, up 15 percent year on year. In terms of market distribution, in the client market purchases and sales of forwards in foreign exchange totaled USD 170.4 billion. Purchases and sales of forwards were USD 114.4billion and USD 55.9 billion, respectively (see Chart 4-10). Short-term 6-month transactions accounted for 71 percent of the total transactions, basically unchanged from 2019. The inter-bank forward market saw a cumulative trading volume of USD 51.3billion, up 20 percent year on year.

Chart 4-10 The Trading Volume of Purchases and Sales of Forward Foreign-Exchange Transactions in the Client Market



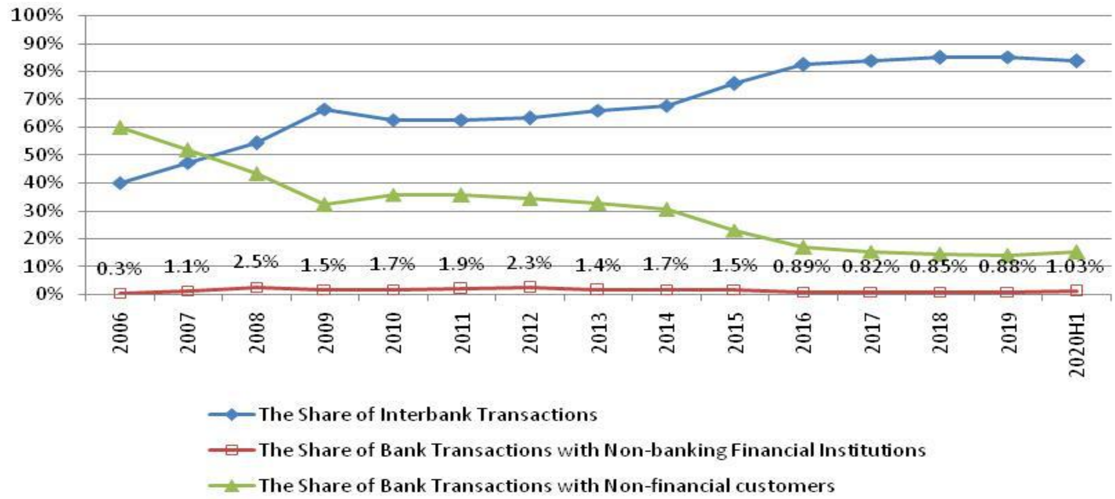
Source: SAFE.

Swap transactions declined. In the first half of the year, cumulative foreign-exchange and currency-swap transactions totaled USD 7.48trillion, down 17percent from the same period of the last year. In terms of market distribution, cumulative foreign-exchange and currency-swap transactions in the client market reached USD122.4billion, up 115 percent from the previous year. Spot purchases/forward sales and spot sales/forward purchases reached USD90.1billion and USD 32.3billion, respectively, up78 percent and426percentfromthe same period of the last year, respectively. The cumulative foreign-exchange and currency-swap transactions in the inter-bank market reached USD7.36trillion, down 18.0percent from the same period of the last year. Global dollar liquidity was tight in March, and the volume of inter-bank swaps increased significantly from January and February, indicating that banks are actively using swaps to manage liquidity in local and foreign currencies.

Options transactions fell. In the first half of the year, the trading volume of options totaled USD 360.4billion, down 20 percent from the same period of the last year. In terms of market distribution, the client market saw a total trading volume of USD133.4billion, down 0.2percent. The inter-bank market saw a total trading volume of USD 227.0 billion, down 29 percent.

The structure of foreign-exchange market participants remained stable. Proprietary transactions by banks continued to dominate (see Chart 4-11). The share of inter-bank trading in the overall foreign-exchange market declined slightly from 85.2 percent in 2019 to 83.7 percent, while the market share of non-financial clients and non-bank financial institutions increased from 14.0 percent and 0.9 percent to 15.2 percent and 1.0 percent, respectively. In the first half of the year, foreign institutions made a total of USD 383.4 billion in transactions in the inter-bank foreign-exchange market, an increase of 89.1 percent year on year, continuing the 2018 and 2019 trend of high growth, and reflecting the positive effects of the opening up of China's capital market and foreign-exchange market.

Chart 4-11 The Structure of the Participants in China’s Foreign-Exchange Markets



Sources: SAFE, CFETS.

Table 4-1 Transactions in the RMB/Foreign-Exchange Market, the First Half of 2020

Product	**Trading Volume (100 million USD)**
Spot	**51,075**
Client Market	**16,769**
Interbank Foreign Exchange Market	**34,306**
Forward	**2,217**
Client Market	**1,704**
Less than 3 months (including 3 months)	667
3 months to 1 year (including 1 year)	843
More than 1 year	193
Interbank Foreign Exchange Market	**513**
Less than 3 months (including 3 months)	402
3 months to 1 year (including 1 year)	77
More than 1 year	34
Foreign Exchange and Currency Swaps	**74,829**
Client Market	**1,224**
Interbank Foreign Exchange Market	**73,605**
Less than 3 months (including 3 months)	63,947
3 months to 1 year (including 1 year)	9,273
More than 1 year	385
Options	**3,604**
Client Market	**1,334**
Foreign Exchange Call Options/RMB Put Options	675
Foreign Exchange Put Options/RMB Call Options	659
Less than 3 months (including 3 months)	490
3 months to 1 year (including 1 year)	687
More than 1 year	157

Interbank Foreign Exchange Market	**2,270**
Less than 3 months (including 3 months)	1,560
3 months to 1 year (including 1 year)	705
More than 1 year	6
Total	**131,725**
Client Market	21,031
Interbank Foreign Exchange Market	110,694
Including: Spots	51,075
Forwards	2,217
Foreign Exchange and Currency Swaps	74,829
Options	3,604

Note: The trading volumes here are all unilateral transactions and the data employ rounded-off numbers.

V. Outlook for the Balance of Payments

In the second half of 2020, the global epidemic and economic situations are still complicated and serious, protectionism and unilateralism are on the rise, and there are many unstable and uncertain factors in the external environment. However, the steady recovery of China's economy, the deepening of reform and opening up, and the acceleration of the formation of a new development pattern, with the domestic big cycle as the main body and mutual promotion of domestic and international dual circulation, are still the solid foundation for China to maintain a basic equilibrium in the balance of payments.

Domestic economic fundamentals will continue to play an essential role in promoting an equilibrium in the balance of payments. First, China's epidemic situation has basically been effectively controlled, and the economy has recovered steadily and is continuing to improve. In the second quarter of

2020, China's GDP increased by 3.2 percent year on year, significantly better than expected. According to the latest forecast of the International Monetary Fund, China may be the only major economy with positive growth in 2020 and it will continue to play a fundamental role in stabilizing market expectations and confidence. Second, China adheres to deepening reform and opening up, continuously improving the business environment, the level of trade, and investment facilitation, and constantly improving the degree of legalization, marketization, and internationalization of the financial market, so as to lay a foundation to continue to attract foreign investment. Third, the flexibility of the RMB exchange rate has been enhanced and has been basically stable. On the one hand, it helps to stabilize the risk of external shocks and to play an automatic stabilizing role in adjusting the balance of payments; on the other hand, it is conducive to the overall stability of market expectations, promoting rational trading of market participants and effectively promoting a balance of supply and demand in the foreign-exchange market.

The current account balance will be kept within a reasonable range. First of all, supply and demand should be improved simultaneously to keep the trade surplus of goods basically stable. On the one hand, domestic economic vitality should be gradually restored, the effects of policies and measures such as stabilizing foreign trade are continuing, new trade forms such as cross-border e-commerce and online shopping are booming, and the foreign supply capacity of trade departments will continue to improve steadily .On the other hand, some foreign countries are promoting a resumption of work and production. Recently, some advanced economic indicators, such as the Manufacturing Purchasing Manager Index (PMI) in the developed countries of Europe and North America hit the bottom and rebounded, indicating that external demand may improve in the second half of the year. Second, the epidemic is restricting cross-border flows of people, and the service trade deficit will remain low. At present, the epidemic in foreign countries is still spreading. Those countries are still maintaining relatively strict entry-exit restrictions, therefore the demand of Chinese residents for cross-border travel and study abroad will be curbed and the service trade deficit will continue to show a downward trend. Under the condition that trade in goods maintains a certain surplus and the deficit of trade in services narrows, it is expected that the current account will show a small surplus for the whole year and it will continue to be in a relatively balanced range.

Cross-border capital flows are expected to remain generally stable. On the one hand, foreign investors will continue to invest in the domestic market in a stable and orderly manner. The domestic financial market is still attractive to global capital. Against the background of the super-loose monetary policies of the major developed countries, assets with higher returns are increasingly scarce in the world. However, China's monetary policy remains stable, and returns on RMB assets is relatively good. For example, as of September 24 the difference in the yield of 10-year Treasury bonds between China and the United States was

2.4 percentage points, 1.2 percentage points larger than that at the end of 2019.The scale of China's bond market and stock market ranks second in the world, but the proportion of foreign capital is only about 2 percent to 4 percent. In the future, with the steady progress of the opening up of the financial market, foreign capital inflows to China will have greater space and momentum for growth. At the same time, foreign direct investments will flow steadily. Since the second quarter of 2020, in the context of shrinking global direct investment, according to statistics from the Ministry of Commerce, my China's use of foreign investment has increased for five consecutive months year on year, reflecting the first economic recovery. At present, as the domestic economy is recovering steadily, the main economic indicators such as consumption and investment are gradually improving. Therefore, the "magnetic effect" of a strong domestic market will continue to show, attracting foreign investors to invest and develop business in China. On the other hand, China's outward investments will maintain a rational and stable development trend. Against the background of the continuous spread of the epidemic across the globe, the "going out" of foreign direct investment by Chinese enterprises will continue to advance steadily. With the rapid development of the domestic capital market and the two-way opening of the financial market, Chinese investors can better allocate assets in domestic and overseas markets and realize value maintenance and an appreciation of assets.

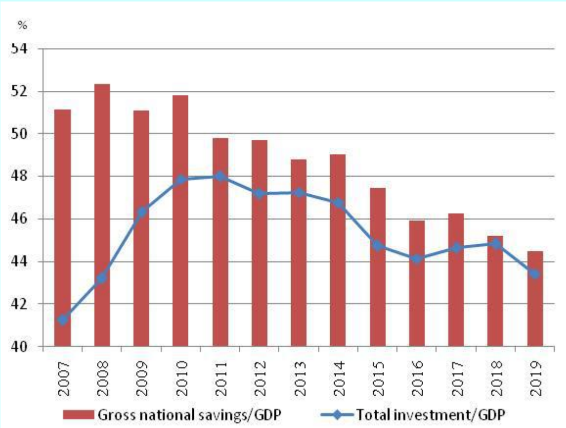
Box5

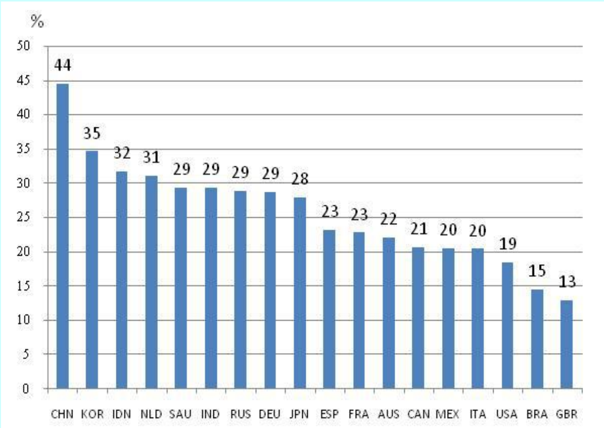
There is a long-term basis for China's current account to maintain a basic balance

Since China's accession to the World Trade Organization (WTO) in 2001, China's current account surplus has experienced a process from rapid growth to a basic balance. In 2007, the ratio of the current account surplus to GDP reached a peak of 9.9 percent, and then fell back to about 2 percent in 2011, and then to less than 1 percent in 2018 and 2019. In the first half of 2020, it will continue to be within a reasonable and equilibrium range. On the whole, the evolution of China's current account is the result of the transformation and upgrading of the domestic economy and the optimization of the economic structure, which reflects the transformation of China's economy to a new pattern in which the domestic economic cycle plays a leading role. At present, a pattern of a basic equilibrium in China’s current account that will not easily change has been formed.

First, the relatively high savings rate and gradually stable investment rate are the supporting structural factors for the basic balance in China's current account. The balance in the current account is determined by the gap between savings and investments. On the one hand, China's economic structure has been constantly adjusted in recent years, and the savings rate has gradually dropped, but it is still at a high level in the world. According to statistics of the International Monetary Fund, China's savings rate reached 44 percent in 2019, ranking first among the top 20 countries in terms of GDP. On the other hand, with the continuous optimization of China's economic structure, investors are paying more attention to investment efficiency, and the investment rate is more stable (see Chart C5-1).

Chart C5-1 The Global Level of China's Savings Rate and its Comparison with the Investment Rate

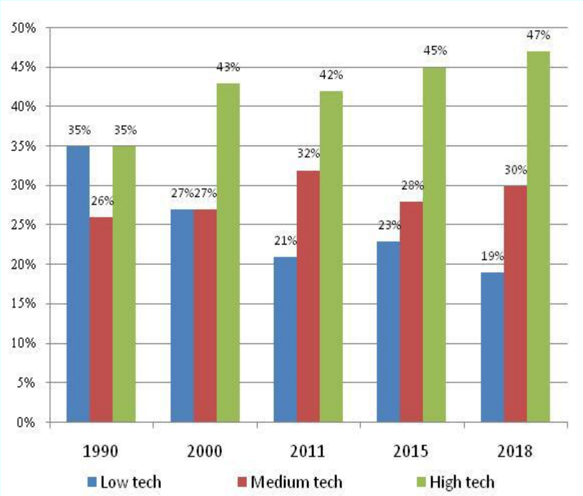


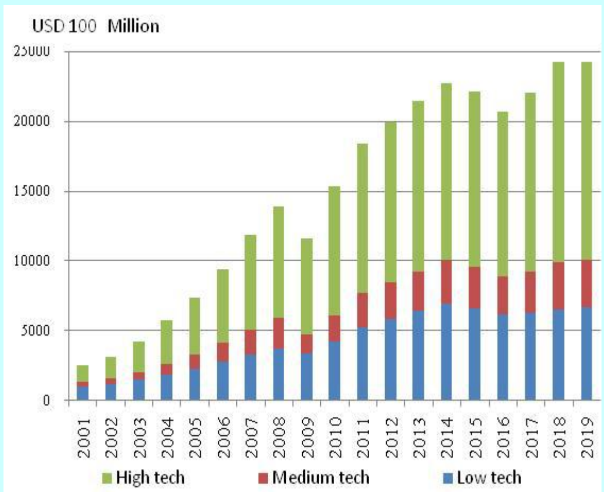


Source: IMF.

Second, the transformation and upgrading of the manufacturing industry will help to improve the quality and efficiency of trade in goods. Since the reform and opening up, China's manufacturing industry has made great progress. The added value of China's manufacturing industry has continued to rank first in the world since 2011. In recent years, the transformation and upgrading of the manufacturing industry has been continuously and effectively promoted, and it has gradually moved from the primary stage of industrialization to the middle and late stage. In this process, the proportion of high-tech products, such as chemical products, electro-mechanical products, precision instruments, and automobiles, in the total output value of the manufacturing industry has increased significantly, while the proportion of products such as textile and clothing, wood furniture, and so on is decreasing. Against the background of the gradual improvement in the level of the manufacturing industry, the structure of exports has been continuously optimized. In 2019, exports of high-tech products reached USD 1.4 trillion, accounting for 56 percent of total exports, 15 percent higher than that in 2000 (see Chart C5-2).In addition, improvements in the level of domestic manufacturing can also better meet domestic demand.

Chart C5-2 Development of Manufacturing Technology in China

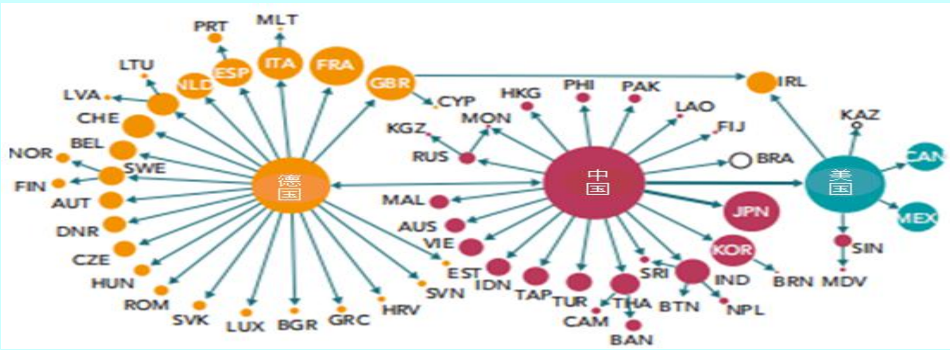




Sources: UNIDO; Customs.

Third, China has a relatively complete modern industrial system, and its position in the global industrial chain and supply chain is generally stable. First, China's manufacturing industry has a complete range of industry categories. It is the only country with all 41 industrial categories, 191 medium categories, and 525 small categories. It has become a key link in the global industrial chain. In terms of imports and exports of electro-mechanical equipment and parts, which account for the largest proportion, China is an important node connecting Japan, South Korea, and Taiwan with the European and American markets. Second, China's position in the global industrial chain has been significantly improved, becoming the core supplier of global goods and services, and the main source of imports from other countries (see Chart C5-3). Third, the economic models in central, eastern and western regions of China have their own advantages and are highly complementary. There are a large number of skilled workers. They still have comparative advantages to retain domestic industries and they continue to undertake international industrial transfers.

Chart C5-3 Structure of the Global Trade Supply Chain



Source: OECD.

The new "dual circulation" development pattern in which the domestic economic cycle plays a leading role and the domestic and international cycles promote each other will lay a solid foundation for the stable operation of the balance of payments in the medium and long terms. Under the new development pattern, the characteristic whereby the domestic market leads the national economic cycle will become more obvious, the potential of domestic demand for economic growth will be continuously released, and market opportunities provided for other countries will become broader, which will become a strong gravitational field to attract international commodities and factor resources. At the same time, China will continue to enhance its ability to innovate independently, to maintain the stability of the industrial chain, and to optimize the supply system, which not only will improve adaptability for domestic demand but also will maintain an international competitiveness, which will contribute to a higher quality development trend for China’s trade in goods and services and will contribute to the maintenance of a balanced current account within a reasonable range.

In the second half of 2020, China's foreign-exchange administration will continue to take Xi Jinping's new socialist ideology with Chinese characteristics as a guide, will better coordinate the work of epidemic prevention and control and economic and social development, doing a solid job of the "six stabilities," fully implementing the task of the "six guarantees," persisting in reform and opening up and risk prevention, promoting a higher level of financial market opening, actively responding to external shocks, and striving to maintain a basic equilibrium in the balance of payments.

On the one hand, we should deepen reform and opening up in the field of foreign exchange, improve the level of cross-border trade and investment liberalization and facilitation, and coordinate and support the normalization of epidemic prevention and control and economic and social development. We should continue to improve the foreign exchange "green channel" for epidemic prevention, accelerate the implementation of trade and investment facilitation measures, continue to expand the trade and foreign-exchange payment facilitation pilot, and promote the electronic filing of foreign-exchange payments for trade in services. We should further study innovative measures to utilize foreign capital to create a more convenient and friendly investment environment for domestic and foreign investors, explore the reform of cross-border investment management for private equity investment funds, and continue to steadily expand the two-way opening and interconnection of financial markets. We will coordinate to promote the construction of the Free Trade Zone pilot, the Shanghai International Financial Center and the Yangtze River Delta integration, the Guangdong Hong Kong Macao Bay Area, and Hainan Free Trade Port, and explore more facilitation and opening-up policy measures.

On the other hand, we should firmly establish bottom-line thinking, make efforts to prevent and resolve major financial risks in the field of foreign exchange, and maintain the stability of the foreign-exchange market and national economic and financial security. We should strengthen the two-way monitoring of cross-border capital flows, macro prudential management of cross-border capital flows, and market-oriented regulation of pro-cyclical behavior in the foreign-exchange market; improve supervision of the foreign-exchange market, protect the legitimate rights and interests of foreign-exchange consumers and investors; crack down on illegal foreign-exchange activities such as underground banks and cross-border gambling with a "zero tolerance" attitude to safeguard the healthy development of the foreign-exchange market; and improve the operation and management of foreign-exchange reserves, strengthen operations and management modernization levels, and ensure the safety, liquidity, and value maintenance and appreciation of foreign-exchange reserve assets.