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Abstract

In 2019global economic growth slowed down significantly, international trade and investment activities were sluggish, and there were many unstable and uncertain factors. China's economy remained generally stable with steady progress, and the quality of development gradually improved.The flexibility of the RMB exchange rate was enhanced, remaining basically stable, and exchange-rate expectations were generally stable.

In 2019 China's balance of payments maintaineda basic equilibrium. The current account surplus was USD 141.3 billion, accounting for 1.0 percent of GDP, which was still in a relatively balanced stage of development. This revealed the effects of development of the domestic economy and the optimization and adjustment of the economic structure in recent years.Specifically, the surplus in trade in goods increased, the deficit in trade in services narrowed, and investment income improved. Cross-border capital flows were generally stable, with a surplus of USD 37.8 billion in the non-reserve financial account. Direct investments maintained a certain scale of a surplus, and China is still the main destination of long-term capital investments. Portfolio investments continued a net inflow, and demandsby foreign investors for medium and long-termRMB assetallocations were still high. Other investments continued a small deficit asmarket players were becoming more rational and orderlyin theircross-border financing.In 2019 China’s balance of paymentsmaintaineda basic equilibrium and showed strong robustness and

adaptability. China's reserve assets remained basically stable and its foreign-exchange reserves reached USD 3107.9 billionat the end of the year. By the end of 2019 China's external financial assets and liabilities had increased by 4.2 percent and 6.3 percent, respectively compared with the end of 2018, with net external assets of USD 2.1 trillion.

In 2020the BOP operationsenvironment is complicated and changeable, and there have been some uncertain factors, such as the COVID-19 epidemic. But the essential factors, such as the fundamentals in the domestic economy, the policy of opening to the outside world, and market regulation mechanisms will still play a leading role. It is expected that China's current account will maintain a basic equilibrium, and cross-border capital flows will remainstable.The foreign-exchange management authorities will make great efforts to promote reform, development, and stability in the field of foreign exchange, continue to improvetrade and investment facilitation, insist on improving theforeign-exchange management system and mechanism that meet the requirements for the modernization of the national governance system and governance capacity, serve the new pattern of development of the real economy and the reform and opening up, prevent the risks of cross-border capital flows, and maintain national economic and financial security.

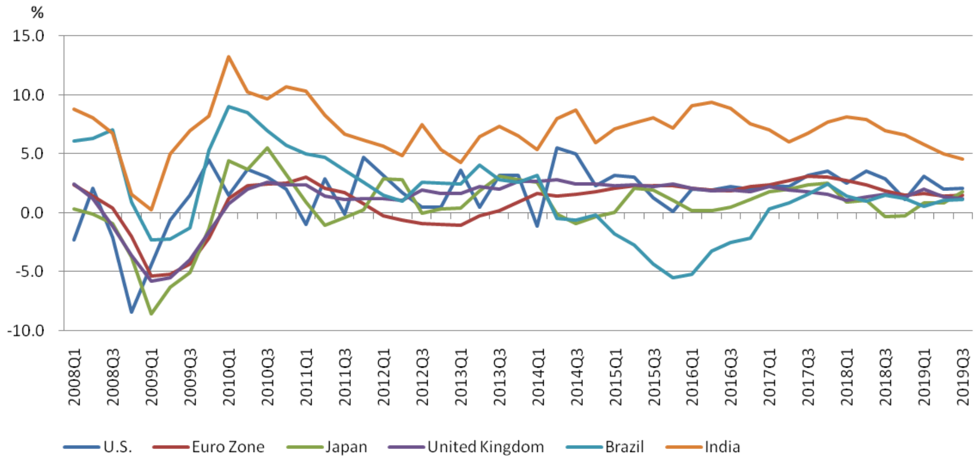
I. Overview of the Balance of Payments

（I）The Balance of Payments Environment

In 2019global economic growth slowed down in the face of downside risks and increasing uncertainties. The monetary policies of the major developed economies and of some emerging market economies were generally loose. China's economic operations continued to be within a reasonable range, and the development trend of overall stability and steady progress continued.

Global economic growth continued to slow. In 2019economic growth in the United States, Europe, and the other developed economies slowed down. However, due to the support of the loose monetary policies, there were signs of stabilization during the second half of the year. In the fourth quarter, the GDP growth rate in the United States was the same as that in the third quarter, and it remained stable. The labor market continued to tighten. Trendsin theeconomies of the euro zone tended to be flat after reaching the bottom, but downside risks remained. In 2019tthe French economy was relatively stable, which supported the economy in the euro zone, but the German economy slowed down significantly.Brexit was accelerated, the economy continued to grow at a slow speed, and inflation remained moderate. Japan's economic growth fell after rebounding in the first half of 2019. The emerging market economies were still in a state of low inflation and low growth. In January 2020 the International Monetary Fund (IMF) estimated that the growth rate in the emerging market economies in 2019 was 3.7 percent, significantly lower than the 4.5 percent in 2018 (see Chart 1-1).

Chart 1-1 The Growth Rate of the Main Economies



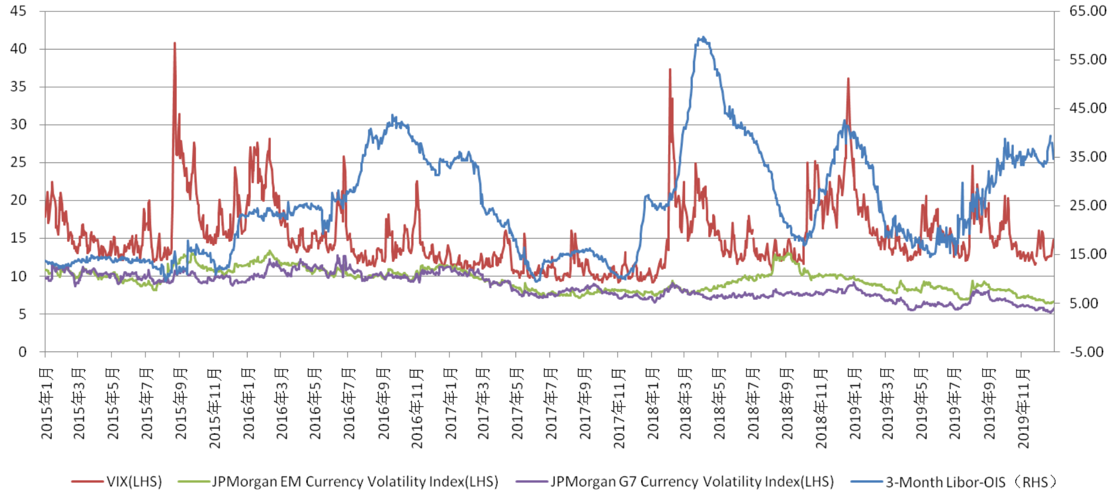
Note: The U.S. growth rate is the annualized quarterly growth, whereas the rates of the other economies are the quarterly growth rates year on year.

Data source: Huanya economic database.

Global monetary policies were generally loose. In 2019, with worries about economic prospects and the judgment that the policy interest rate was close to neutral, central banks such as the Federal Reserve and the European Central Bank turned to loosen their monetary policies from the beginning of 2019. The Federal Reserve ceased raising interest rates and then cut interest rates three successive times to 1.50 percent–1.75 percent, and carried out regular repurchases and purchases of short-term treasury bonds. During 2019, the European Central Bank adjusted forward-looking guidance on rate hikes. In September, it lowered the deposit facility interest rate by 10 basis points to –0.50 percent, the first rate-cut since 2016. It also restarted the asset purchase plan and implemented a new round of targeted long-term refinancing operations. The Bank of Japan continued to implement a loose monetary policy and planned to maintain the current extremely low interest-rate level at least until the spring of 2020. In addition, many other economies followed the YS and Europe and entered an easing cycle. In 2019 more than 40 economies, including Australia, New Zealand, South Korea, India, Brazil, Mexico, Russia, and Turkey, cut their interest rates in order to support economic growth or to achieve their inflation targets. Some of them reached or nearly reached historical low policy interest rates.

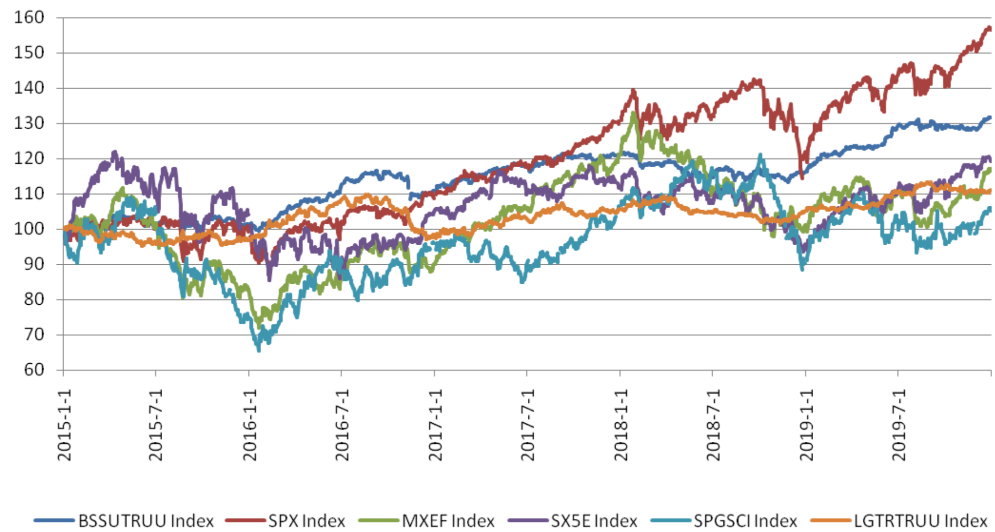
Vulnerability risksin the international financial market accumulated. In 2019, the international financial market was expected to improve during the first half of the year. During the second half of the year, volatility in the international financial market increased due to the impact of the trade frictions between China and the US as well as the poor performance of the global economy. The USD index rose 0.2 percent year on year with the devaluation of the EUR and the appreciation of the GBO and the JPY. The stock markets of the major developed economies continued to rise, driven by the global interest-rate reduction cycle, along with the S&P 500 index and the EuroStoxx 50 index rising 29 percent and 25 percent, respectively. However,the rise in the stock markets pushed up market values and increased vulnerability risks. Commodity trends rebounded, with the S&P GSCI commodity price index rising 17 percent. The yields of the major global treasury bonds in 2019 were lower than those at the beginning of the year. The yields of long-term and short-term US Treasury bonds once upside down during 2019. The yields of government bonds in several European economies were as low as zero or even negative (see Chart 1-2 and Chart1-3). At the same time, global debt levels continued to rise, increasing the vulnerability of economic and financial operations.

Chart 1-2 Interest Rates in International Financial Markets and Currency



Source: Bloomberg.

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

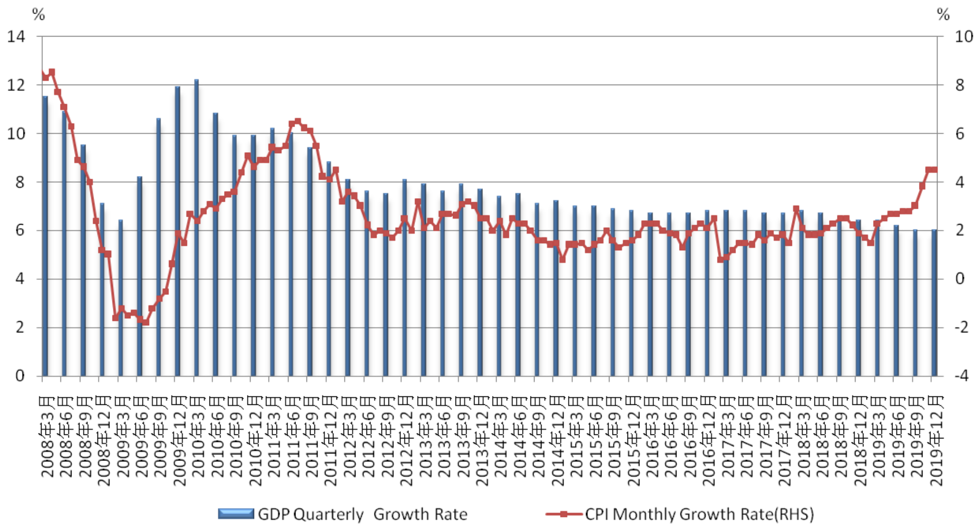


Note: BSSUTRUU and LGTRTRUU are the Bloomberg Barclays emerging market index and the developed country sovereign bond index, MXEF is the MSCI Emerging Market index, SPX is the S&P 500 index, SX5E is the Euro STOXX 50 index, SPGSCI is the S&P GSCI commodity price index—all of which are 100 at the beginning of 2015.

Source: Bloomberg.

The domestic economy was running smoothly. In 2019 China's national economy was generally stable, the economic structure continued to be optimized, and high-quality development was solidly promoted. According to preliminary statistics, the annual Gross Domestic Product (GDP) was RMB 99.1 trillion, an increase of 6.1 percent year on year in terms of comparable prices, and the Consumer Price Index (CPI) was up 2.9 percent (see Chart 1-4). Consumption growth was stable, investment was slow but stable, the scale of imports and exports was expanded, and industrial production continued to grow.

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



Source: National Bureau of Statistics.

(II) The Main Characteristics of the Balance of Payments

The current account andthe non-reserve financial account both recordedsmall surpluses. In 2019 the current account posted a surplus of USD 141.3 billion and the non-reserve financial account recorded a surplus of USD 37.8 billion (see Table 1-1).

Table 1-1 Structure of the BOP Surplus

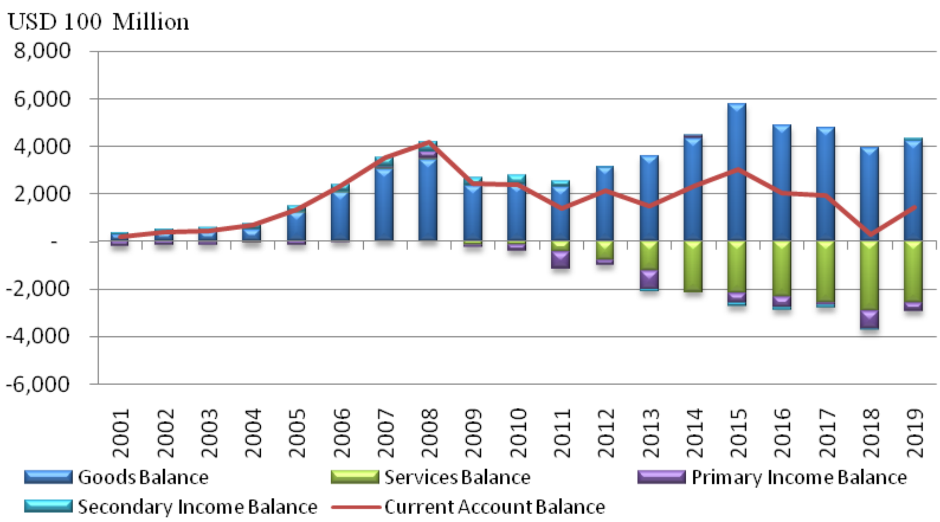
100 million USD

Item	2013	2014	2015	2016	2017	2018	2019
Current account balance	1482	2360	3042	2022	1951	255	1413
As a % of GDP	1.5%	2.3%	2.8%	1.8%	1.6%	0.2%	1.0%
Financial account excluding reserve assets	3430	-514	-4345	-4161	1095	1727	378
As a % of GDP	3.6%	-0.5%	-3.9%	-3.7%	0.9%	1.3%	0.3%

Sources: SAFE, NBS.

The surplus in trade in goods increased. Based on balance-of-payments statistics,[1]in 2019exports of trade in goods totaled USD 2399.0 billion, down 1 percent, and imports of trade in goods totaled USD 1973.7 billion, down 2 percent,thus achieving a surplus of USD 425.3 billion, up 8 percent (see Chart 1-5).

Chart 1-5 Major Items Under the Current Account



Source: SAFE.

The deficit in trade in servicesnarrowed. In 2019revenue from trade in

[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 purchasedat ports, and smuggled goods that are deducted from import and export returns.

services totaled USD 244.4 billion, up5 percent, and expenditures totaled USD 505.5 billion, down4 percent. Trade in services thus recorded a deficit of USD 261.1 billion, down 11 percent (see Chart 1-5).In particular, the transportation deficit totaled USD 59.0 billion, down 12 percent, and the travel deficit totaled USD 218.8 billion, down8 percent.

The deficit in primary income decreased.[2] In 2019revenue from primary income totaled USD 235.8 billion, down 5 percent, and expenditures totaled USD 268.8 billion, down 17 percent. The deficit in primary income totaled USD 33.0billion, down 56 percent (see Chart 1-5). In particular, the surplus in employee compensation was USD 3.1 billion, compared with USD 8.2 billion in 2018.Investment income recorded a deficit of USD 37.2 billion, down 56 percent.Revenue from outward investmentstotaled USD 219.8 billion, down 3 percent, and expenditures for inward investments, including profits and dividends of foreign-funded enterprises, totaled USD 257.0 billion, down 18 percent.

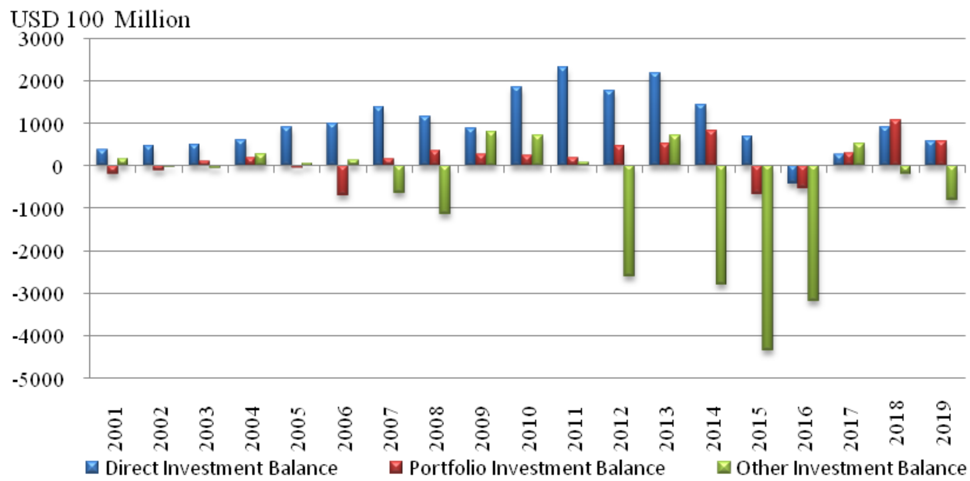
Secondary income turned from a deficit to a surplus. In 2019revenue and expenditures of secondary income totaled USD 25.9 billion and USD 15.7 billion, respectively, down 7 percent and 48percent. Secondary income recorded a surplus of USD 10.3 billion, compared with a deficit of USD 2.4 billion in 2018 (see Chart 1-5).

Direct investments maintained a surplus. Based on the

[2] The IMF's *Balance of Payments and International Investment Manual* (6th edition) renamed the income item under the current account as primary income and renamed current transfers as secondary income.

balance-of-payments statistics,[3]in 2019 direct investments posted a surplus of USD 58.1 billionand continued a relatively stablesituation (see Chart 1-6).In particular, net outflows of outward direct investments(the net increase inindirect-investment assets) amounted to USD 97.7 billion, down 32 percent. Net inflows of foreign direct investments(the net increase in direct-investment liabilities) totaled USD 155.8 billion, down34percent, with equity investments in the form of capital increasing by 11 percent.

Chart 1-6 Major Items Under the Capital and Financial Account



Source: SAFE.

Portfolio investments retained a surplus. In 2019 portfolio investments recorded a surplus of USD 57.9 billion (see Chart 1-6), maintaining a surplus for three consecutive years.In particular, net outflows of outward portfolio investments (the net increase in assets) totaled USD 89.4 billion, up 67percent,

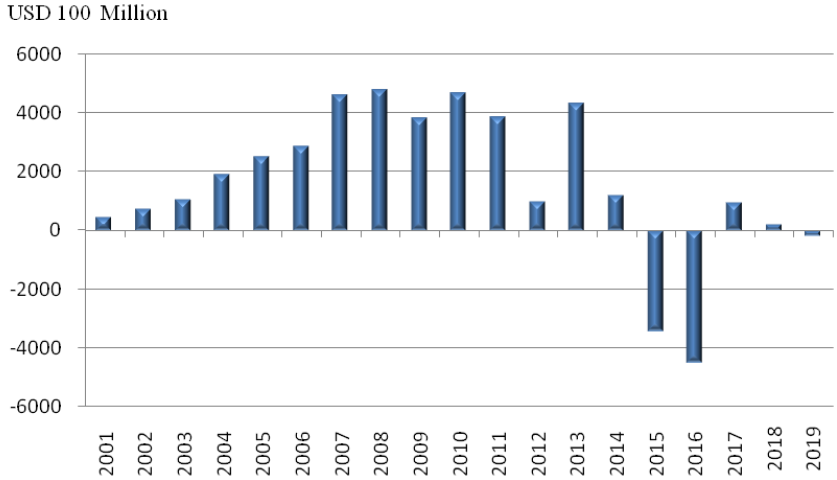
[3] The BOP compiles and reports direct investments following balance-sheet rules, whereas the Ministry of Commerce compiles and reports direct investments by direction, and there are also differences between the principles for reverse investments and investments among affiliates.In addition, direct investments based on BOP statistics also include unpaid and unremitted profits, retained earnings, shareholder loans, foreign capital utilized by financial institutions, and real-estate purchases by non-residents.

and net inflows of inward portfolio investments (the net increase in liabilities) totaled USD 147.4 billion, down 8 percent, with inward bond investments increasing by 3 percent.

The deficit in other investments increased. In 2019 other investments, including loans, trade credits, and deposits, posted a deficit of USD 75.9 billion (see Chart 1-6), whereas in 2018theyhad recorded a deficit of USD 20.4billion. In particular, net outflows of outward other investments (the net increase in assets) totaled USD 32.3 billion, down 77 percent, and the net outflows of inward other investments (the net decrease in liabilities) totaled USD 43.7 billion, whereas in 2018therewerenet inflows of USD 121.4billion.

Reserve assets remained relatively stable. In 2019 reserve assets involving transactions (excluding the effects of non-transactional values, such as exchange rates and prices)decreased by USD 19.3 billion. In particular, foreign-currency reserves involving transactions decreased by USD 19.8 billion (see Chart 1-7). By the end of 2019, China’s foreign-currency reserves totaled USD 3107.9 billion, up USD 35.2 billion since the end of 2018, mainly affected by changes in the non-transactional values, such as the exchange rates and prices.

Chart 1-7 Foreign-Currency Reserve Assets involving Transactions



Source: SAFE.

Table 1-2 Balance of Payments in2019

100 million USD

Item	**Line No.**	**2019**
1. Current account	1	**1,413**
Credit	2	29,051
Debit	3	-27,638
1.A Goods and services	4	**1,641**
Credit	5	26,434
Debit	6	-24,793
1.A.a Goods	7	**4,253**
Credit	8	23,990
Debit	9	-19,737
1.A.b Services	10	**-2,611**
Credit	11	2,444
Debit	12	-5,055
1.A.b.1 Manufacturing services on physical inputs owned by others	13	**154**
Credit	14	157
Debit	15	-4
1.A.b.2 Maintenance and repair services n.i.e	16	**65**
Credit	17	102
Debit	18	-37
1.A.b.3 Transport	19	**-590**
Credit	20	462
Debit	21	-1,052
1.A.b.4 Travel	22	**-2,188**
Credit	23	358

Debit	24	-2,546
1.A.b.5 Construction	25	**51**
Credit	26	144
Debit	27	-93
1.A.b.6 Insurance and pension services	28	**-62**
Credit	29	48
Debit	30	-110
1.A.b.7 Financial services	31	**15**
Credit	32	39
Debit	33	-24
1.A.b.8 Charges for the use of intellectual property	34	**-278**
Credit	35	66
Debit	36	-344
1.A.b.9 Telecommunications, computer, and information services	37	**80**
Credit	38	349
Debit	39	-270
1.A.b.10 Other business services	40	**194**
Credit	41	692
Debit	42	-498
1.A.b.11 Personal, cultural, and recreational services	43	**-31**
Credit	44	10
Debit	45	-41
1.A.b.12 Government goods and services n.i.e	46	**-21**
Credit	47	16
Debit	48	-37
1.B Primary income	49	**-330**
Credit	50	2,358
Debit	51	-2,688
1.B.1 Compensation of employees	52	**31**
Credit	53	143
Debit	54	-112
1.B.2 Investment income	55	**-372**
Credit	56	2,198
Debit	57	-2,570
1.B.3 Other primary income	58	**11**
Credit	59	18
Debit	60	-7
1.C Secondary income	61	**103**
Credit	62	259
Debit	63	-157

1.C.1 Personal transfers	64	1
Credit	65	40
Debit	66	-40
1.C.2 Other secondary income	67	102
Credit	68	219
Debit	69	-117
2. Capital and financial account	70	**567**
2.1 Capital account	71	**-3**
Credit	72	2
Debit	73	-5
2.2 Financial account	74	**570**
Assets	75	-1,987
Liabilities	76	2,558
2.2.1 Financial account excluding reserve assets	77	**378**
Financial assets excluding reserve assets	78	-2,180
Liabilities	79	2,558
2.2.1.1 Direct investment	80	**581**
2.2.1.1.1 Assets	81	**-977**
2.2.1.1.1.1 Equity and investment fund shares	82	-849
2.2.1.1.1.2 Debt instruments	83	-128
2.2.1.1.1.a Financial sector	84	-175
2.2.1.1.1.1.a Equity and investment fund shares	85	-191
2.2.1.1.1.2.a Debt instruments	86	16
2.2.1.1.1.b Non-financial sector	87	-802
2.2.1.1.1.1.b Equity and investment fund shares	88	-658
2.2.1.1.1.2.b Debt instruments	89	-144
2.2.1.1.2 Liabilities	90	**1,558**
2.2.1.1.2.1 Equity and investment fund shares	91	1,313
2.2.1.1.2.2 Debt instruments	92	246
2.2.1.1.2.a Financial sector	93	184
2.2.1.1.2.1.a Equity and investment fund shares	94	159
2.2.1.1.2.2.a Debt instruments	95	25
2.2.1.1.2.b Non-financial sector	96	1,374
2.2.1.1.2.1.b Equity and investment fund shares	97	1,153
2.2.1.1.2.2.b Debt instruments	98	221
2.2.1.2 Portfolio investment	99	**579**
2.2.1.2.1 Assets	100	**-894**
2.2.1.2.1.1 Equity and investment fund shares	101	-293
2.2.1.2.1.2 Debt securities	102	-601
2.2.1.2.2 Liabilities	103	**1,474**

2.2.1.2.2.1 Equity and investment fund shares	104	449
2.2.1.2.2.2 Debt securities	105	1,025
2.2.1.3 Financial derivatives (other than reserves) and employee stock options	106	**-24**
2.2.1.3.1 Assets	107	14
2.2.1.3.2 Liabilities	108	-37
2.2.1.4 Other investment	109	**-759**
2.2.1.4.1 Assets	110	**-323**
2.2.1.4.1.1 Other equity	111	-15
2.2.1.4.1.2 Currency and deposits	112	-863
2.2.1.4.1.3 Loans	113	331
2.2.1.4.1.4 Insurance, pension, and standardized guarantee schemes	114	-12
2.2.1.4.1.5 Trade credit and advances	115	368
2.2.1.4.1.6 Other accounts receivable	116	-132
2.2.1.4.2 Liabilities	117	**-437**
2.2.1.4.2.1 Other equity	118	0
2.2.1.4.2.2 Currency and deposits	119	-557
2.2.1.4.2.3 Loans	120	425
2.2.1.4.2.4 Insurance, pension, and standardized guarantee schemes	121	18
2.2.1.4.2.5 Trade credit and advances	122	-288
2.2.1.4.2.6 Other accounts payable	123	-35
2.2.1.4.2.7 Special drawing rights	124	0
2.2.2 Reserve assets	125	**193**
2.2.2.1 Monetary gold	126	0
2.2.2.2 Special drawing rights	127	-5
2.2.2.3 Reserve position in the IMF	128	0
2.2.2.4 Foreign exchange reserves	129	198
2.2.2.5 Other reserve assets	130	0
3.Net errors and omissions	131	**-1,981**

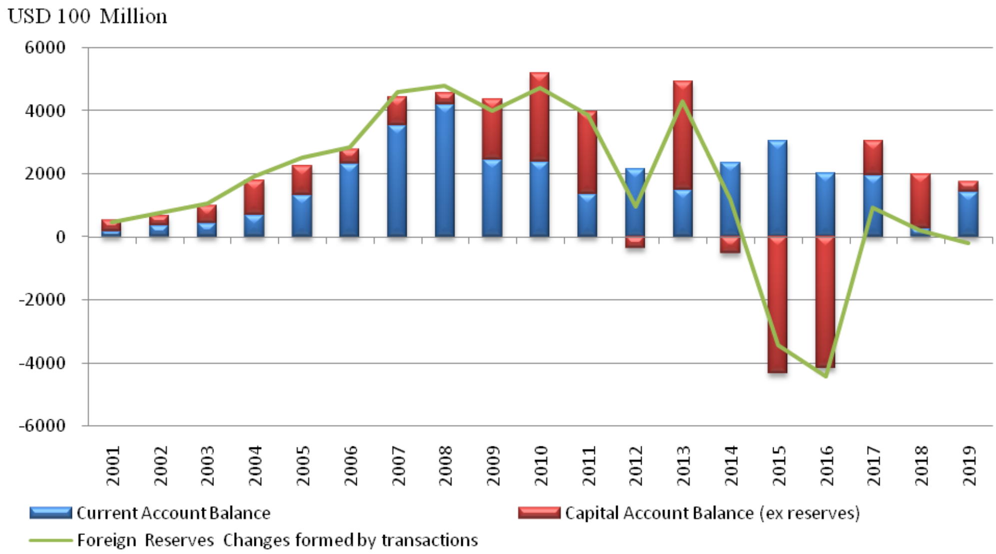
Notes:

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. This chart is based on rounding principles.

(III) Evaluation of the Balance of Payments

China's balance of payments maintaineda basic equilibrium, reflecting strong robustness and adaptability. First of all, the current account continued to be within a reasonable surplus range. Since 2016, the ratio of the surplus to GDP have remained below 2 percent, and in 2019, the ratio was 1.0 percent. **Second,** the non-reserve financial accounts have run smoothly, recording small surpluses in the recent three years.**Third,** since 2018 foreign-exchange reserves have remained stable at about USD 3.1 trillion. In recent years, the external environment has been complex and changeable, and there have beena number of uncertain factors. However, China's balance of payments maintained a basic equilibrium, which fully shows that the foundation of internal and external equilibrium and stability in China's economy is solid and will not easily change with short-term fluctuationsin the market environment.

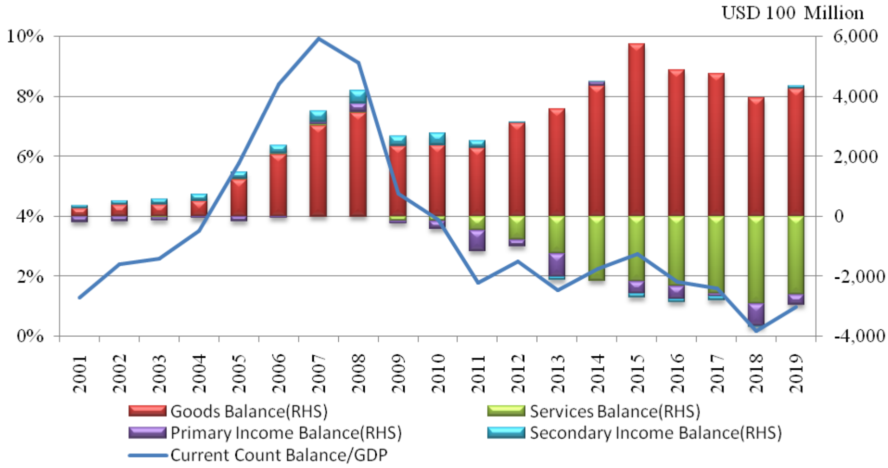
Chart 1-8Main Structure of the BOP



Source: SAFE.

The current account recorded a small surplus and continued to be within the range of a reasonable surplus. In 2019 the current account surplus was USD 141.3 billion,accounting for 1.0 percent of GDP. In 2018 the surplus was USD 25.5 billion. The rebound in the current account surplus was the result of the combined effects of the increase inthe trade-in-goods surplus, the decreaseinthe trade-in-services deficit, and the improvement in investment income. According to statistics, in 2019 the ratio of the trade-in-goods surplus to GDP was 3.0 percent, up 0.1 percentage point compared with the previous year. The deficit in trade in services accountedfor 1.8 percent of GDP, down 0.3 percentage point. The ratio of the primary income deficit to GDP was 0.2 percent, down 0.3 percentage point, mainly due to the significant drop in the deficit in investment income. In general, due to the by economic development and structural optimization and adjustment, China's current account has entered a more balanced stage of development. During this process, due to the cyclical changes in international commodity prices and the demand for some import and export products, the current account will fluctuate slightly but it will not change the overallsituation of a basicequilibrium.

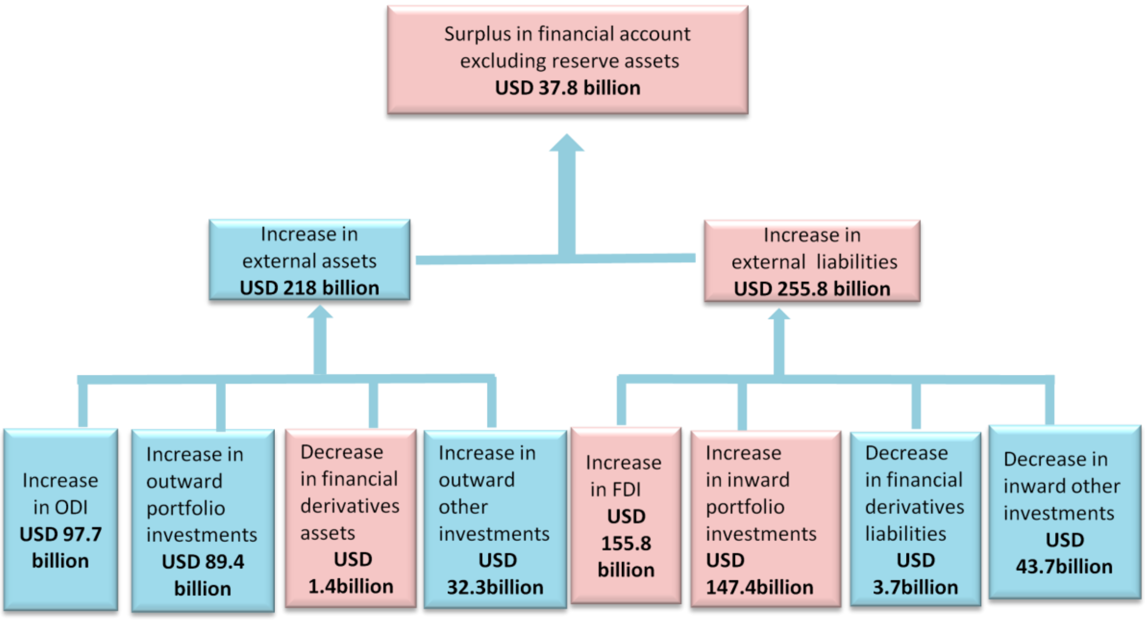
Chart 1-9 Structure of the CurrentAccount



Sources: SAFE, NBS.

The non-reserve financial accounts recorded a surplus and were relatively stable. In 2019, the surplus inthe non-reserve financial accounts reached USD 37.8 billion, continuing the trend of a net inflow.**On the one hand,** the structure of inward foreign investmentswas optimized. In 2019, net inflows of foreign direct investments and portfolio investments in China were USD 155.8 billion and USD 147.4 billion, respectively, accounting for 119 percent of all types of investments in China, whereas the average annual proportion in 2017 and 2018 was 71 percent. Foreign direct investmentsare medium and long-term investments, and 60 percent of portfolio investments, whichcome from overseas central banks, also belong to stable long-term value investments. Thus, net inflows of relevant capital will be relatively stable.**On the other hand,**market players in Chinawere rational and orderlyin theiroutward investments. In 2019, outward direct investmentstotaled USD 97.7 billion, down from the previous year.Outwardportfolio investmentstotaled USD 89.4 billion, remaining at the average level in recent years. In general, direct investments and portfolio investments for the purpose of medium and long-term asset allocations were the main sources of the surplus in the non-reserve financial accounts. The scale of capital flows from other investments with high volatility was significantly lower than that in 2015 and 2016, which indicates that the foundation for stable cross-border capital flows in China has been strengthened.

Chart 1-10 Structure of China's Cross-Border Capital Flows in 2019



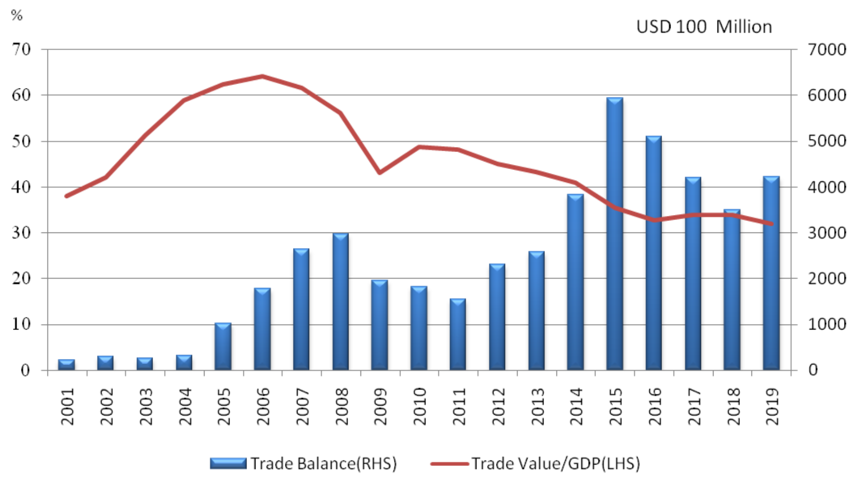
Source: SAFE.

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

(Ⅰ) Trade in Goods

Exports and imports of goods remained generally stable, and the degree of trade dependence steadily decreased. In the context of the complex and serious global environment, the slowdown in global economic growth, and the significant increase in internal and external challenges, China’s exports and imports of goods remained stable. According to customs statistics, in 2019 China's total exports and imports of goods amounted to USD 4.6 trillion, a slight decrease of 1 percent year on year. Exports and importsreached USD 2.5 trillion and USD 2.1 trillion, respectively. China's foreign-trade dependence (the ratio of foreign trade to GDP) was 32 percent in 2019, down 1.9 percentage points from the previous year, indicating that China's economic structure continued to improve and remained relatively stable (see Chart 2-1).

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

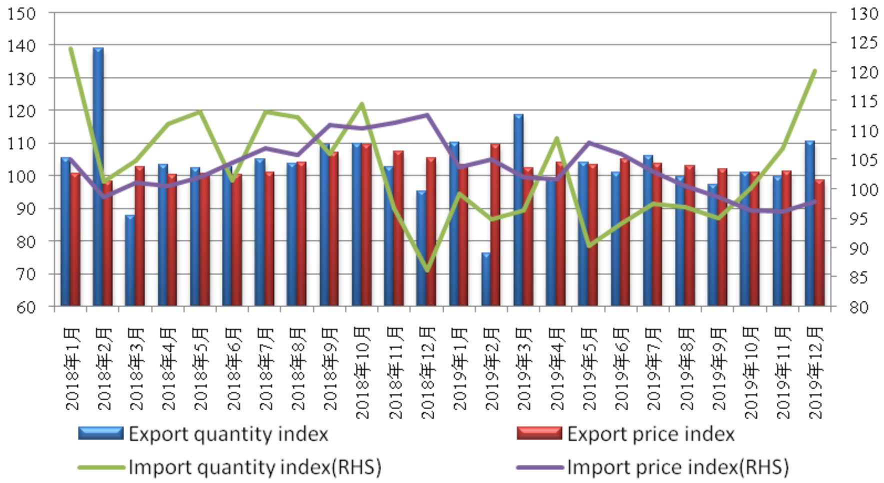


Sources: General Administration of Customs, National Bureau of Statistics.

The structure of exports and imports continued toimprove, and the

competitiveness of export commodities gradually increased. According to customs statistics (denominated in USD), in 2019 China's Export Price Index increased by an average of 3 percent per month, and China’sImport Price Index increased by an average of 2 percent per month (see Chart 2-2). The Term of Trade Index was 102, an increase of 4 percentage points from the previous year,indicating that China’scompetitive advantage in export products continued to improve due to its ability to import products equalin value to exportsin value but more in quantity. As to high value-added products, in 2019 China's trade surplus forelectronics products increased by 11 percent year on year, up 4 percent pointsfrom the previous year. China’s trade surplus for high-tech products increased by 22 percent year on year, accounting for 22 percent of the total trade surplus, andindicating that trade in high value-added products maintainedgood development. To sum up, China's trade in goodsremained stable in quantity and improvedin quality.

Chart 2-2The Volume and Price Index of Exports and Imports of Trade in Goods

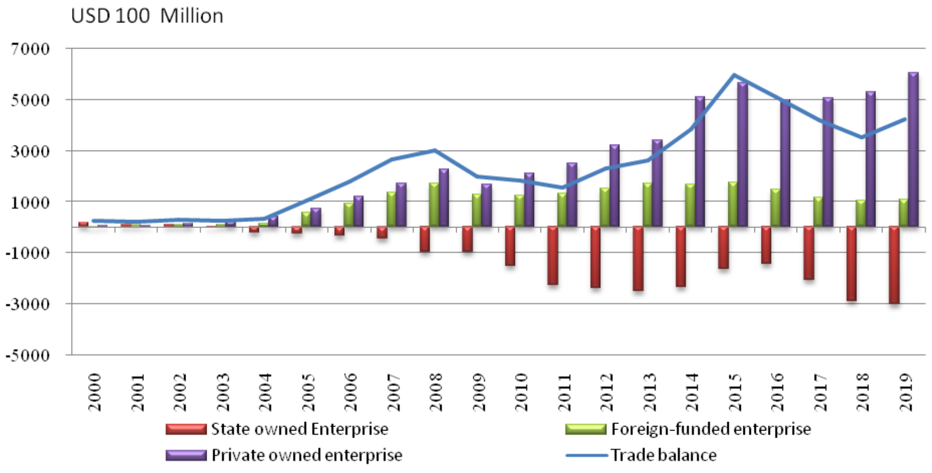


Source: General Administration of Customs.

Private enterprises became the largest foreign-trade contributor in

China, and thetrade surplus by foreign-funded enterprises increased steadily. In 2019, exports and imports of trade in goods by private enterprises reached approximately USD 2.0 trillion, up 7 percent year on year andaccounting for 43 percent of China's total foreigntrade. The ratio was 3 percentage points higher than that in 2018. For the first time, private enterprises surpassed foreign-invested enterprises and became China's largest contributor to foreign trade. The trade surplus by private enterprises amounted to USD 615 billion, up 14 percent year on year. In 2019, total trade in goods by foreign-invested enterprises amounted to USD 1.8 trillion,down 7 percent year on year (see Chart 2-3), accounting for 40 percent of China's total foreign trade anddown 3 percent year on year. The trade surplus by foreign-invested enterprises reached USD 108.2 billion, up 4 percent year on year. Total trade in goods by state-owned enterprises amounted to USD 772.5 billion, down 4 percent year on year. The ratio to total trade in goods decreased slightly by 1 percentage point.

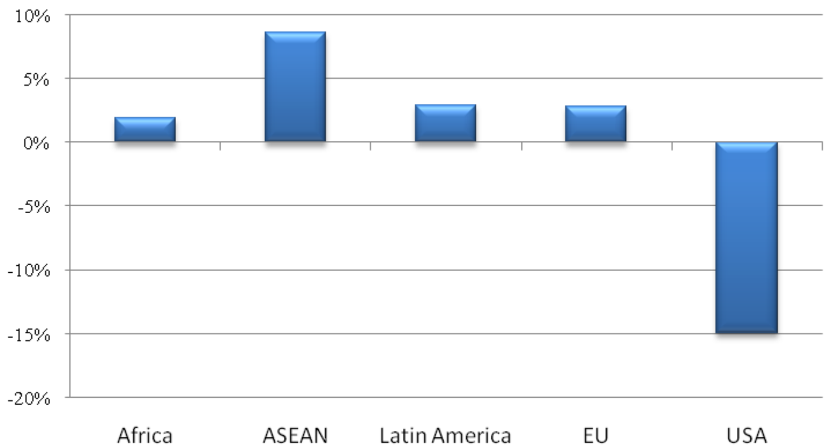
Chart 2-3 Balance of Trade in Goods in Terms of Contributors



Source: General Administration of Customs.

China’s Foreign-trade partners have become more diversified. Trade with the "Belt and Road" economies increased rapidly. In the context of Sino-US economic and trade frictions, China’s exports and imports with the United States fell by 1.9 percentage points in 2019, contributing less to the trade surplus. During the same time, Chinese enterprises managed to diversify their trade partners. Trade in goods with the EU, ASEAN, Latin American, and Africancountries increased by 2.8 percent, 8.6 percent, 2.9 percent,and 1.9 percent, respectively,year on year, up0.6, 1.2, 0.3, and 0.1 percentage pointsintheir respective proportions of China’s total foreign trade. In addition, China’s foreigntrade along the “Belt and Road” economies continued to expand. Exports and importswiththe “Belt and Road” economies accounted for 29 percent of total foreign trade, up 2 percentage points year on year.

Chart 2-4 Growth Rates of China's Trade in Goods with Major Countries and Regions in 2018 and 2019



Source: General Administration of Customs.

Box 1

Differences between Customs Merchandise Trade Statistics and Balance-of-Payments Trade Statistics

Differences exist between customs merchandise trade and trade in goods under the balance of payments. For instance, in 2019 the differences in exports, imports, and the balance for these two sets of statistics reached USD 100.6 billion, USD 103.9 billion, and USD 3.4 billion, respectively. This is mainly because customs statistics are in line with the United NationsInternational Merchandise Trade Statistics:Concepts and Definitions (IMTS2010), and thebalance-of-payments statistics are in line withthe International Monetary Fund Balance of Payments and the International Investment Position Manual (Sixth Edition) (BPM6). The statistical differences are demonstrated in Table C1-1.

First, there are differences in the statistical scope. International merchandise trade statistics covercross-border movement of commodities without taking into account change of ownership. However, in the balance of paymentstrade in goods covers changesinthe economic ownership between residents and non-residents, regardless of whether the goods move across borders.

For example, customs statistics and balance-of-payments statistics use different recording principles for offshore transfer transactions. Because goods bought and soldby offshore transfers never actually enter or leave China’s borders, no transactions will be captured by the customs statistics. However,the balance of payments will include them under trade in goodsonce a change of ownership of the goods occurs between residents and non-residents. As another example, customs statistics and balance-of-payments statistics differ in terms of recording goods entering and leaving second-line customs. For instance, company A uses imported materials to produce commodities in a special supervision zone in China, andthe goods are sold to non-resident company B. The goods are then sold to Chinese consumers by company B’s agent located within China. In this regard, the customs statistics only record imports when the original materials enter China. The balance-of-payments statistics not only record the imports of materials but also record the exports of finished products and the re-imports to Chinese consumers, which involve three transactions. Due tothe large difference between the export price of finished products and the re-import price paid by Chinese consumers, the difference between customs statistics and balance-of-payments statistics increases as this type of trade increases in volume.

Second, there are differences in thevaluation principles. First, customs use FOB valuation for exports and CIF for imports,whileboth exports and imports are valued at FOB in the balance of payments. Second, international merchandise trade statistics are based on prices when commoditiescross borders, while the valuation of good in the balance of payments is based on the price agreed upon betweenresidents and non-residents buyers and sellers. For example, domestic company A produces goods and sells them to non-resident company B, and company B sells the goodsin the international market. Company B will store the goods in China's warehousesand ship them out when needed. When leaving China's borders, the goods may be declared to Chinese customs at the prevailing pricein the international market, which is usually higher than the contract price between company A and company B. The difference on the basis of valuation can cause differences between the customs statistics and the balance-of-payments statistics in the trade in goods.

There arestatistical time differences. For example, high-value goods generally take a long time to produce. The change in the economic ownership of the goods depends on the contract between the buyers and the sellers, which usuallyoccurs in stages. However, customsstatistics will include them only when the goods move across the border.

Currently, China's balance of payments uses customs merchandise trade statistics as the data source for goods and will make the necessaryadjustments. The main adjustments are as follows. First, the balance of payments includes goods that changeownership but do not physically cross borders. Second, the balance of payments deducts goods from customs statistics that are across borders but do not change ownership. Third, the balance of payments adjusts prices, including adjusting the CIF valuation to the FOB valuation for customs imports. Due to the differences between customs merchandise source data and goods on a balance of payments basis, data differencesare inevitable. As trade forms develop, the differences may expand or narrow overtime.

Table C1-1 Reconciliation between Merchandise Source Data and Total Goods on a Balance of Payments Basis

Item	Exports	Imports
Merchandise trade statistics as provided in source data adjustments, as relevant. For example,		
+ Goods procured in ports by carriers (paragraph 10.17 (d))		
+Fishing, minerals from the seabed, and salvage sold from resident-operated vessels(paragraph 10.17 (e))		
+Goods changing ownership entering/leaving the territory illegally (paragraph 10.17 (i) / (j))		
+/-Goods lost or destroyed in transit (paragraph 10.17 (m))		
+Goods acquired from other economies for processing abroad (paragraph 10.65 (b))	Not applicable	

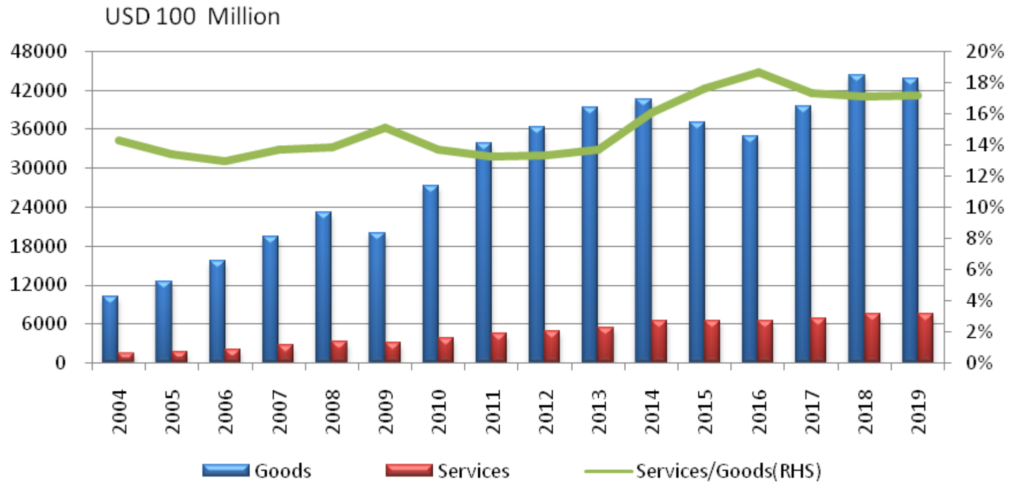
+Goods sold abroad after processing in other economies(paragraph 10.66 (b))		Not applicable
+/-Goods changing ownership in customs warehouses or other zones (paragraph 10.25)		
-Migrants'personal effects (paragraph 10.22 (b))		
-Goods imported for construction projects by non-resident enterprises (paragraph 10.22 (d))		
-Goods for repair or storage without a changeof ownership (paragraph 10.22 (e))		
-Goods sent abroad or returned after processing without a change of ownership (paragraph 10.22 (f))		
-Returned goods (paragraph 10.22 (i))		
+/-High-value capital goods, if delivery differs from change of ownership (paragraph 10.28)		
-CIF / FOB adjustment (paragraph 10.34)	Not applicable	
+Net exports of goods under merchandising (paragraph 10.44 (c))		Not applicable
+Nonmonetary gold (paragraph 10.50)		
=Total goods on a balance-of-payments basis		

Source: *Balance of Payments and International Investment Position Manual*(*Sixth Edition*) (BPM6).

(Ⅱ) Trade in Services

Trade in servicesremained relatively stable. In 2019, China's trade in servicestotaled USD 749.9 billion, a slight decrease of 1 percent year on year. The ratio of trade in services to trade in goods was 17 percent (see Chart 2-5). In particular, revenue and expenditures from maintenance and repair services, personal, cultural, and entertainment services, financial services, and computer servicesrecorded relatively higher growth rates, up 43 percent, 16 percent, 16 percent, and 16 percent, respectively.

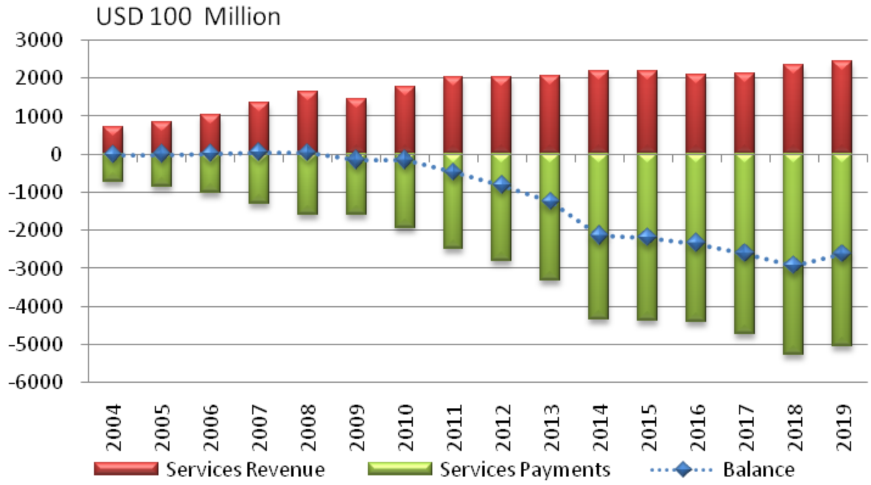
Chart 2-5 Comparison of the Total Volume of Trade in Goods and Services



Source: State Administration of Foreign Exchange.

Revenue from trade in services continued to grow. In 2019, revenue from trade in services totaled USD 244.4 billion, up 5 percentyear on year (see Chart2-6). Among the major items, revenue from other business services, such as consultation services and technical-related services, amounted to USD 69.2 billion, up 5 percent year on year and accounting for 28 percent of the total revenue. Revenue from transportation amounted to USD 46.2 billion, accounting for 19 percent and a year-on-year increase of9 percent. Revenue from travel amounted to USD 35.8 billion, accounting for 15 percent and a year-on-year decrease of 11 percent. Emerging services such as telecommunications, computer and information services, and the use of intellectual property royalties continued to grow, a year-on-year increase of 16 percent and 19 percent,respectively.

Chart 2-6 Revenue and Expenditures from Trade in Services

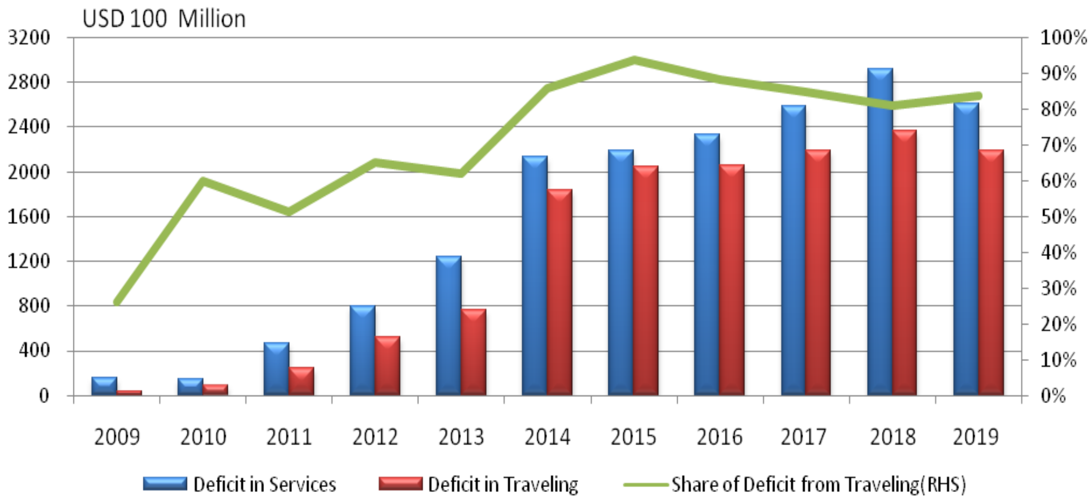


Source: State Administration of Foreign Exchange.

Expenditures for trade in services declined. In 2019, expenditures for trade in servicesrecorded USD 505.5 billion, down 4 percent year on year. Among the major items, travel recorded expenditures of USD 254.6 billion, down 8 percent year on year and accounting for 50 percent of total expenditures. Transportation recorded expenditures of USD 105.2 billion, down 4 percent year on year and accounting for 21 percent of total expenditures. Expenditures on other business services, such as consultation services and technical-related services, were USD 49.8 billion, accounting for 10 percent of total expenditures anda year-on-year increase of 6 percent.

The trade-in-services deficit narrowed. In 2019, the deficit in trade in services was USD 261.1 billion, down 11 percent year on year. Travel continued to be the main source of the deficit (see Chart 2-7). The travel deficit amounted to USD 218.8 billion, down 8 percent year on year. Due to Sino-US economic and trade frictions and the tightening of overseas study policies in some economies, China’s travel deficit with the United States, Australia, and Canada declined. As the second largest deficit item among trade in services, transportation recorded a deficit of USD 59 billion, down 12 percent year on year andmainly because the decline in imports of goods contributed to the decrease in transportation expenditures.

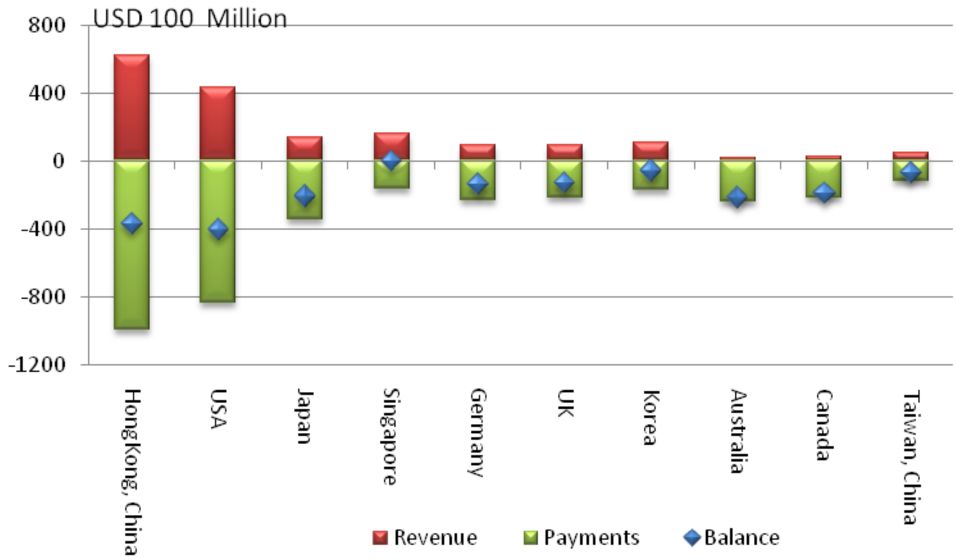
Chart 2-7 The Travel Contribution to the Deficit in Trade in Services



Source: State Administration of Foreign Exchange.

The counterparty economieswere highly concentrated. In 2019, China's top ten partners in term of trade in services were Hong Kong SAR, the United States, Japan, Singapore, Germany, the United Kingdom, South Korea, Australia, Canada, and Taiwan Province. Trade with these partners totaled USD 526 billion, accounting for 70 percent of the total trade in services. Chinaposted a deficit with its top ten major trading partners. With the exception with Singapore, South Korea, and TaiwanProvince, the deficit with the other partners narrowed to various degrees. However, the deficits with the United States, Hong KongSAR, Australia, Japan, Canada, Germany, and the United Kingdom werestill more thanUSD 10 billion (see Chart 2-8).

Chart 2-8 Trade in Services in Terms of Trade Partners in 2019



Source: State Administration of Foreign Exchange.

Box2

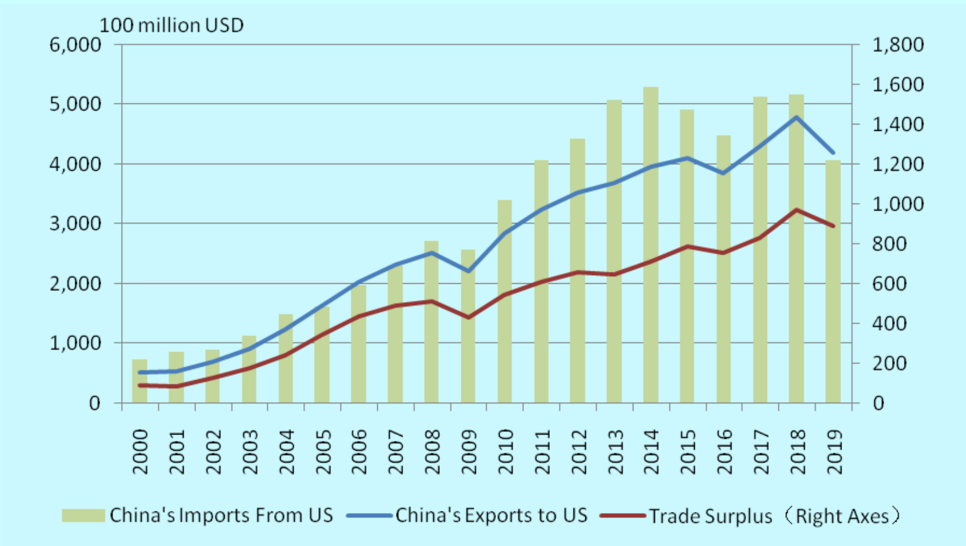
Developments and Changes inSino-US Trade in Recent Years

Against the background of economic globalization and international industrial divisions, economic and trade exchanges between China and the United States have been increasingly frequent. As the two major economies in the world, China and the United States account for nearly 30 percent of total global trade. The two countries jointly promote global economic growth and trade development, and contribute to the prosperity and stability of the world economy.

Trade in goods between the two countries continued to develop steadily. According to customs statistics, bilateral trade between China and the United States has moved from rapid growth to the stage ofsteady development. In 2019Sino-US bilateral trade in goods reached USD 540.9 billion, increasing more than five times since China joined the WTO in 2001. Specifically, bilateral trade was at a stage of rapid development from 2001 to 2008, with an average annual growth rate of 23 percent in bilateral trade volume. After the global financial crisis in 2009, growth of trade in goods gradually slowed down, so the average annual growth rate of bilateral trade was 6 percent from 2010 to 2018. In 2019, due to the influence of tariffs between the two countries, China's imports from the US and exports to the US fell by a total of 15 percent, and the surplus narrowed by 8 percent year on year (see figure C2-1).

Trade in goods between the two countries is highly complementary. As the largest developing country and developed country in the world, China and the United States are at different stages of economic development and play different roles in the global value chain. In recent years, with China gradually undertaking global processing and the manufacturing industry, exports of electronic products to the United States have increased significantly, accounting for 48 percent of total exports to the United States in 2019 (the ratio was only 33 percent in 2001).In 2019, electronic products and textiles and clothing exported to the United States accounted for nearly 60 percent of total exports to the United States. For a long time, China's imports from the United States focused on high-tech and capital- intensive products such as electronic products, aircraft, automobiles, medical equipment, and agricultural products such as soybeans. In 2019imports of the above products accounted for more than 60 percent of total imports from the United States. The two countries give full play to their comparative advantages, and bilateral trade shows complementary advantages.

Chart C2-1 Sino-US Trade in Goods



Source: General Administration of Customs.

Differences in the trade dependence of the two countries. China has continuously strengthened international exchanges and paid attention to the balanced development of trade. In 2018China's number of trade partners reached more than 230, astrade with the emerging markets and the developing countriescontinued to grow rapidly. In 2019 ASEAN had surpassed the United States to become China's second largest trading partner.According to Chinese statistics, the share of Sino-US trade in China's trade has declined slightlyin recent years. From 2000 to 2018, the proportion of trade in goods between China and the United States in the volume of China's total imports and exportsgradually dropped from 17 percent to about 13 percent. According to US statistics during the same period, the proportion of Sino-US trade in goods in the total volume ofUS imports and exportsincreased by 10 percentage points to 16 percent. In 2019, due to the impact of tariffs between the two countries, the share of Sino-US trade in China's total trade and US total trade decreased to 12 percent and 13 percent, respectively.

Rapid development of trade in services between the two countries. According to statistics of the United States Bureau of Economic Analysis, the volume of trade in services between China and the United States increased more than sevenfoldfrom 2001 to 2019, and the surplus of trade in servicesfrom the United States to China increased twentyfold. In 2015 China surpassed Canada and became the largest source country of the surplus in US trade in services.In 2019, Sino-US service trade accounted for 5.2 percent of the total US service trade, and the US service trade surplus China accounted for more than 15 percent of the US service-trade surplus.

Economic and trade cooperation between China and the United States has provided a huge market for enterprises in the two countries and higher cost-effective goods and services for consumers in the two countries, achieving mutual benefit and win-win results. In the future, China will continue to promote reform and expand its opening-up, cooperatefurther with the United States and other countries in terms of international trade, and jointly promote the healthy development of global trade.

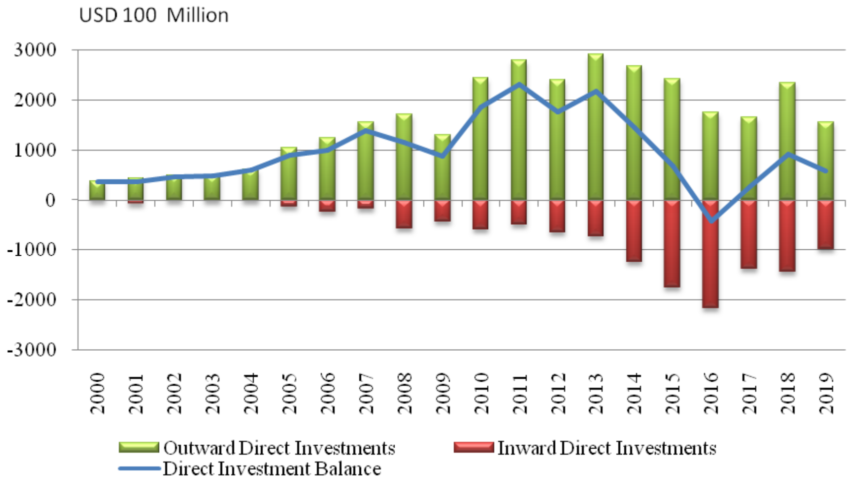
（III） Direct investments

Direct investments continued a trend of net inflows.[4] In 2019 net inflows of direct investments in China's balance of payments totaled USD 58.1

[4] The net flow of direct investments refers to the gap between the net increase in direct-investment assets (net outflow of funds)and the net increase in direct-investment liabilities (net inflow of funds). When the net increase in direct-investment assets is more than the net increase in direct-investment liabilities, a net outflow is recorded, and vice versa.

billion(see Chart 2-9), a decrease of 37 percent year on year, or equivalent to the average level during the past five years.

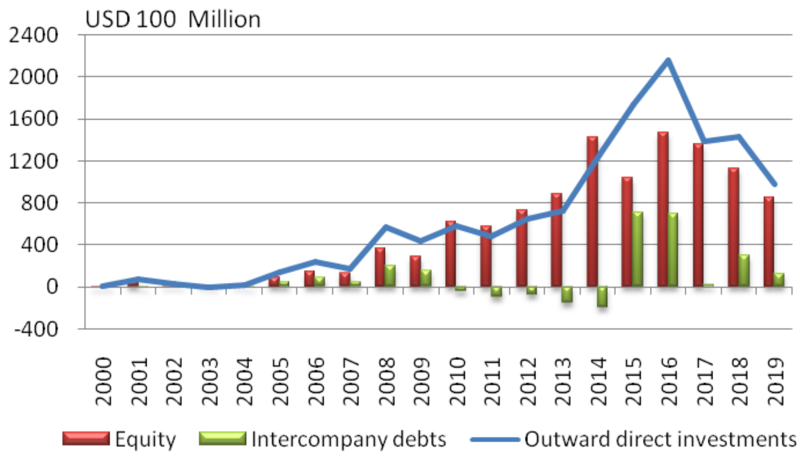
Chart 2-9 China'sDirect Investments



Source: State Administration of Foreign Exchange.

Outward direct investments (ODI) declined. In 2019 China's ODI (net increase in direct-investment assets)[5] reached USD 97.7 billion, a decrease of 32 percent year on year (see Chart 2-10).

Chart 2-10 China's Direct-Investment Assets



Source: State Administration of Foreign Exchange.

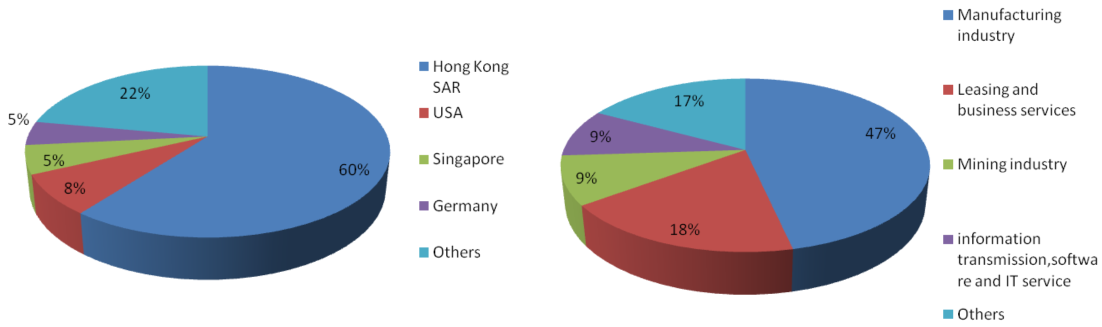
[5]A major component of direct-investment assets is outward direct investments. In addition, reverse investments by domestic foreign-funded enterprises to their parent companies are also included. A net increase in direct-investment asset transactions, which is negative in the balance-of-payments statement, represents a net outflow.

In terms of composition, China's direct-investment assets focused on equity investments supplemented by debt investments. First, equity investments reached USD 84.9 billion, a 25 percent decline year on year. Second, loans to foreign affiliates recorded USD 12.8 billion, a 58 percent decline year on year. The first half and the second half of 2019 witnessed net outflows of USD 200 million and USD 12.5 billion, respectively, including a net outflow of USD 10.1 billion during the last quarter of 2019, reflecting more active cross-border lending activities by domestic entities.

In terms of sectors, outward direct investments by China's non-financial sector and financial sector both dropped. First, direct-investment assets by the non-financial sector recorded a net increase of USD 80.2 billion, down 34 percent year on year, mainly due to a 29 percent drop in equity investments, including capital investments and re-investments of earnings. Loan assets increased USD 14.4 billion, down 51 percent yearonyear. The Hong Kong SAR was the first destination for domestic enterprises to "go global." In terms of the investors' industries, manufacturing continued to rank as the largest industry, accounting for 47 percent of the total (see Chart 2-11). Second, direct-investment assets by the financial sector recorded a net increase of USD 17.5 billion, down 16 percent year on year, mainly composed of equity investments including capital investments and re-investments of earnings, of which more than 70 percent was from the banking sector.

Chart 2-11 Direct-Investment Assets in the Non-Financial Sector, 2019

(in terms of destination and domestic industry)

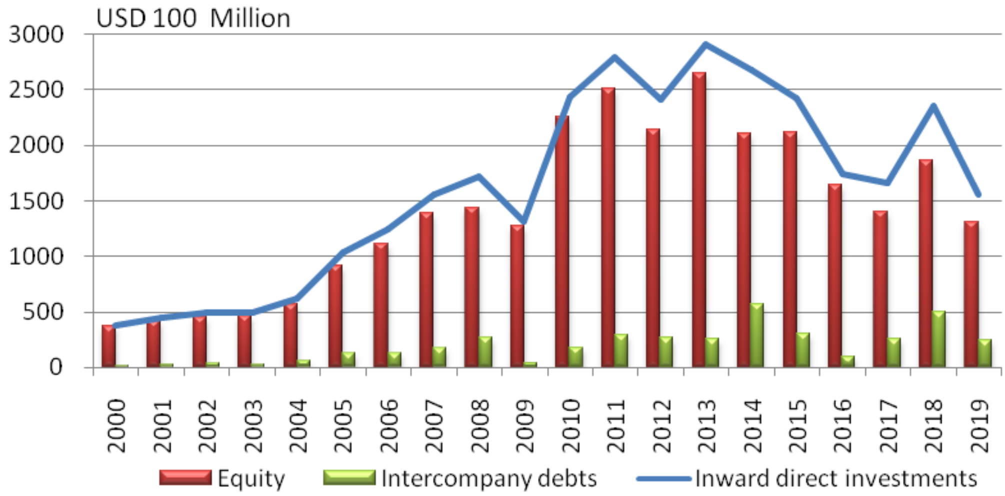


Source: State Administration of Foreign Exchange.

Inward foreign direct investments in China maintained net inflows. Net inflows of inward foreign direct investments (net increases in direct-investment liabilities) in China recorded USD 155.8 billion in 2019, down 34 percent year on year. According to a report by the United Nations Conference on Trade and Development (UNCTAD), the scale of inward foreign direct investments in China in 2019 ranked first among the developing countries and second in the world.

In terms of composition, inward foreign direct investments mainly focused on equity investments, of which the capital continued to increase. First, net inflows of equity investments in China amounted to USD 131.3 billion (see Chart 2-12); among these, equity investments in the form of capital increased 11 percent year on year, indicating that foreign investments remain confident aboutprospects for China's economic development. **Second,**loans from foreign affiliates recorded a net inflow of USD 24.6 billion. In quarterly terms, net inflows were USD 7.4 billion, USD 4.5 billion, USD 1.5 billion, and USD 11.2 billion during the four quarters, respectively, first showing a decrease, then an increase, compared to the same quarters in 2018, reflecting an upward trend in lending activities by foreign-invested enterprises.

Chart 2-12 Direct-Investment Liabilities



Source: State Administration of Foreign Exchange.

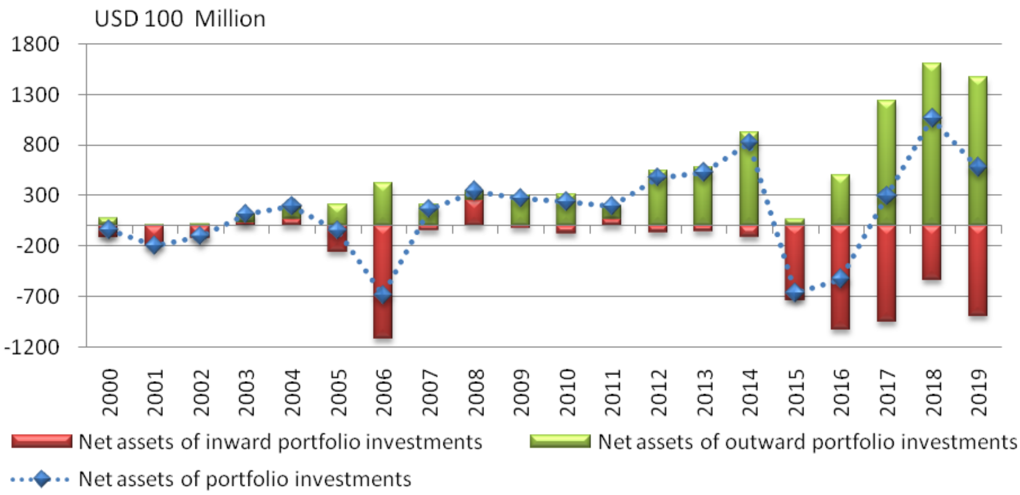
In terms of sectors,business services, information transmissions, and software and information technology services were the main industries in China's non-financial sectors in terms of absorbing inward foreign direct investments. First, direct-investment liabilities in the non-financial sector recorded a net increase of USD 137.4 billion, accounting for 90 percent of the total net inflows of direct investments to China. Among these, the leasing and business services industry absorbed the most direct investments, accounting for 24 percent of direct investments to China's non-financial sector. The manufacturing industry absorbed 16 percent, making it the third largest absorber of FDI. In the meantime, the main source of FDI remained the Hong Kong SAR, accounting for about 80 percent of the total. The Hong Kong SAR was followed by Singapore and South Korea, accounting for a total of 10 percent. **Second**, direct-investment liabilities in the financial sector recorded a net inflow of USD 18.4 billion, up 5 percent year on year.

（IV） Portfolio investments

Portfolio investments maintained an inflow. In 2019 the net inflow (increase in net liabilities)[6] of portfolio investmentswas USD 57.9 billion, down 46 percent year on yearand up 96 percentfrom that in 2017 (see Chart 2-13). In terms of trading instruments, in 2019 the net inflow of equity investments was USD 15.6 billion, down 64 percent year on year; the net inflow of bond investmentswas USD 42.4 billion, down 34 percent. Both inward and outwardportfolio investmentsremained at a high level, indicating that the positive attitude and effective measures by the Chinese government to support the orderly opening of the financial market not only attracted overseas investors but also provided multiple channels for domestic investors to allocate assets overseas and to improve the liquidity and vitality of the financial market.

[6]In the balance-of-payments statement, positive liabilities indicate a net inflow.

Chart 2-13 Net Flows under Portfolio Investments



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

Source: SAFE.

China's outward portfolio investments increased. In 2019 China's net outward portfolio investments (net increase in assets)[7] were USD 89.4 billion, with a year-on-year increase of 67 percent. Among these, equity investments reached USD29.3 billion, bond investments reached USD 60.1 billion, up 66 percent and 68 percent year on year, respectively, reflecting that domestic investors' demands for overseas asset allocations were well met. On a quarterly basis, outwardportfolio investments rose gradually, at USD 16.2 billion, USD 22.8 billion, USD 24.2 billion, and USD 26.2 billion, respectively,during the four quarters.

In terms of major channels, **first,** domestic banks and other financial institutions invested USD 51 billion, with a year-on-year increase of 39 percent;

[7]In the balance-of-payments statement, negative assets indicate a net outflow.

second,domestic residents purchased USD32.2 billion in overseas securities assets via the Shanghai-Hong Kong Connect and the Mutual Recognition of Funds, 2.8 times more than that in the last year; **third,** domestic institutional investors (QDIIs and RQDIIs) invested a total of USD 6.2 billion in non-resident-issued bonds, up 77 percent; **fourth,** outstanding acceptances of letters of credit by foreign banks increased by USD 300 million, whereas in 2018, they decreased by USD 2.3 billion. In addition, domestic residents reduced their net holdings of non-resident-issued bonds by USD 300 million, whereas in 2018, they increased their holdings by USD 7.2 billion.

Net inflows of inwardportfolio investments maintained a relatively high scale. In 2019 inward portfolio investments recorded a net inflow (net increase in liabilities)[8]ofUSD 147.4 billion, down 8 percentyear on year. In particular, net inflows of portfolio investments in domestic bonds market wereUSD 102.5 billion, reaching a new record high. They increased by 3 percent year on year and accounted for 70 percent of the total net inflows of portfolio investments;net inflowsin equity reached USD 44.9 billion, down 26percent. The decrease in net inflows of equity was mainly due to the decrease in IPOs and new-share-issues of listed companies in the Hong Kong stock market. Net inflows via theLand Stock Connectwere still at a high level and registeredsignificant growth. On a quarterly basis,net inflows of portfolio investmentsfluctuated but remained at a high level, at USD 35.7 billion, USD

[8] In the balance-of-payments statement, positive liabilities indicate anet inflow.

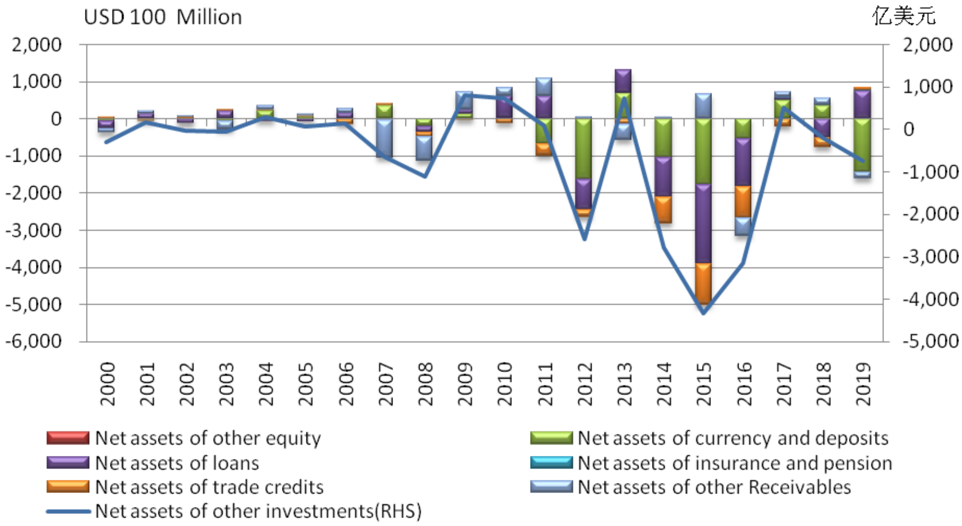
26.4 billion, USD 44.2 billion, and USD 41.1 billion, respectively, in the four quarters.

In terms of major channels, **first,**foreign institutions invested USD 78 billion in the domestic securities market through QFIIs, RQFIIs, the inter-bank bond market, and so forth, with an increase of 15 percent year on year; **second,**investments via the Shanghai–Hong Kong Connect and the Shenzhen–Hong Kong Connect were USD 50.4 billion, with an increase of 13 percent year on year; **third,** non-residents purchased USD 22.3 billion in domestic-resident-issued overseas stocks and bonds, of which bonds issued by Chinese resident institutions (including China's central bank) were the majority.Investmentsvia this channel decreased by 60 percent year on year. In addition, bank acceptances of forward letters of credit (with drafts) recorded a net outflow of USD 3.4 billion, down nearly 60 percent. In general, with the acceleration of the opening up of financial markets, the expansion of the MSCI, and the inclusion of RMB bonds in the Bloomberg Barclays global composite index, the investment scale of equity and bond securities in China in 2019 remained at a high level.

(V) Other investments

Other investments posted a deficit. In 2019 other investments registered a net outflow (an increase in net assets) of USD 75.9 billion, compared with a net outflow of USD 20.4 billion in 2018 (see Chart 2-14). In particular, currency and deposits recorded a net outflow of USD 142.1 billion, loans recorded a net inflow of USD 75.7 billion, trade credits recorded a net inflow of USD 8 billion, and other accounts payables and receivables recorded a net outflow of USD 16.8 billion.

Chart 2-14 Net Flows of Other Investments



Assets under other investments declined. In 2019 the net outflow of other investments (net increase in assets) reached USD 32.3 billion, down 77 percent year on year. In particular, trade credit assets such as export receivablesrecorded an inflow of USD 36.8 billion, whereas in 2018 theyrecorded an outflow of USD 65.3 billion. This is mainly because during the collection period cycle of enterprise payments, in the first quarter of 2019 the collection of export revenue was relatively fast, along with an increased net inflow under trade credits (assets decreased). In the second and third quarter of 2019, exports grew while the collection of receivables was delayed and trade credits showed a net outflow (assets increased). The net outflow of overseas deposits was USD 86.3 billion, a year-on-year increase of 4.8 times; the net inflow of recovered overseas loans was USD 33.1 billion, compared with a net outflow of USD 81.8 billion in 2018;other receivables registered a net outflow of USD 13.2 billion, whereas in 2018 there was a net inflow of USD 22.4 billion.

The liabilities of other investments registered a net outflow. In 2019inward other investments registered a netoutflow (net decrease in liabilities) of USD 43.7 billion, whereas in 2018there was a net inflow of USD 121.4 billion. Among these, due to the impact of the decline in imports,trade credit liabilities, such as import payables of enterprises, registered a net outflow of USD 28.8 billion, compared with a net inflow of USD 40.8 billion in 2018; the net inflow of foreign loans was USD 42.5 billion, up by 32 percent yearonyear; foreign deposits recorded a net outflow of USD 55.7 billion, compared with a net inflow of USD 51.4 billion in 2018; the net outflow of other payables was USD 3.5 billion, up 12 percent yearon year.

Box 3

Growth of China's External Debt Slowed Down in 2019, with a Structural Optimization and Controllable Risks

Currently, China's foreign debt scale is reasonable, the structure continues to be optimized, the main indicators of foreign debt are within internationally recognized security line, and China's foreign debt risk is generally controllable. On the whole, the growth of the balance of foreign debt is in line with China's economic development and the process of continuous expansion and opening up.

1、The growth of foreign debt slowed down and the structure continued to be optimized

The total scale of foreign debt increased, but the growth rate slowed down. By end-December 2019, the balance of China's full caliber foreign debt had reached USD 2057.3 billion (excluding the external liabilities of Hong Kong SAR, Macao SAR, and Taiwan Province, the same below), an increase of USD 74.5 billion, or 3.8percent over end-December2018. The quarter-on-quarter changes in 2019 were 0.3percent, 1.3percent, 1.7percent, and 0.4percent, respectively, with the growth rate slowing down. From the perspective of the term structure, the balance of medium-term and long-term foreign debts grew by USD 158.4 billion, an increase of 23percent; the balance of short-term foreign debts dropped by USD 83.8 billion, a decrease of 7percent; the balance of domestic currency foreign debts grew by USD 70.9 billion, an increase of 10.8percent; the balance of foreign-currency foreign debts grew by USD 3.6 billion, an increase of 0.3percent; from the perspective of the type of debtors, compared with end-December 2018, the balance of broad government foreign debts grew by USD 38.7 billion , an increase of 17percent; the bank's external debt balance grew by USD 19.2 billion, an increase of 2percent.

The stock structure of foreign debt is reasonable. By end-December 2019, in terms of the currency structure, the foreign debt in local currency accounted for about one-third, and the balance of foreign debt in local currency and foreign currency was USD 727.9 billion and USD1329.4 billion, respectively; in terms of the term structure, the proportion of medium-term and long-term foreign debt and short-term foreign debt was 40.6percent, and the balance was USD 852 billion and USD 1205.3 billion, respectively; in terms of debt instruments, debt securities, loans, currencies, and deposits accounted for nearly 70percent, with the proportion of debt securitiesexceeding one quarter; from the perspective of the type of debtor, the banks' external debt accounted for nearly 50 percent. The external debt balances of banks, enterprises (including direct investments: inter-company loans), and the general government (including the central bank) were USD 918 billion, USD 832.1 billion, and USD 307.2 billion, respectively, accounting for 45 percent, 40 percent, and 15 percent, respectively.

The external debt structure continued to be optimized. Compared with end-December 2018, the scale of foreign debt in local currency and medium and long-term foreign debt continued to rise steadily. The proportion of foreign debt in local currency increased from 33percent to 35percent, and the proportion of medium and long-term foreign debt increased from 35percent to 41percent. Benefiting from the opening of the domestic inter-bank bond market, the purchase of domestic bonds by foreign investors increased and the scale of debt securities increased rapidly, accounting for a substantial increase from 8percent at end-December 2014 to 26percent.

2、The external debt risk is generally controllable

The total size of the foreign debt was not large. At end-September 2019,[9] China's foreign debt balance ranked 13th in the world. The foreign debts of the United States, Britain, and Japan were 10 times, 4 times, and 2 times that of China, respectively. Compared with the countries with the same economic scale, the absolute scale of China's foreign debt was not large.

Foreign debt risk indicators were stable. At end-December 2019, the debt ratio of China's foreign debt (the ratio of the foreign debt balance to GDP) was 14percent, the debt ratio (the ratio of the foreign debt balance to the trade export income) was 78percent, the debt service ratio (the ratio of foreign debt repayments to trade export income) was 6.7percent, and the ratio of the short-term foreign debt to foreign-exchange reserves was 39percent, all of which werewithin the internationally recognized security line (20percent, 100percent, 20percent, 100percent), far lower than theoverall level in both the developed and the emerging countries.

Foreign debt and foreign assets grew steadily and harmoniously. By end-December 2019, China's foreign assetshad increased by 20percent compared with end-December 2014, and the growth rate of foreign debt during the same period was 16percent, or slightly lower than the growth rate of foreign assets. On the whole, growth of the foreign debt balance was in line with China's economic development and the process of continuous expansion and opening up.

Stability of the foreign debt structure was enhanced. Driven by the growth of

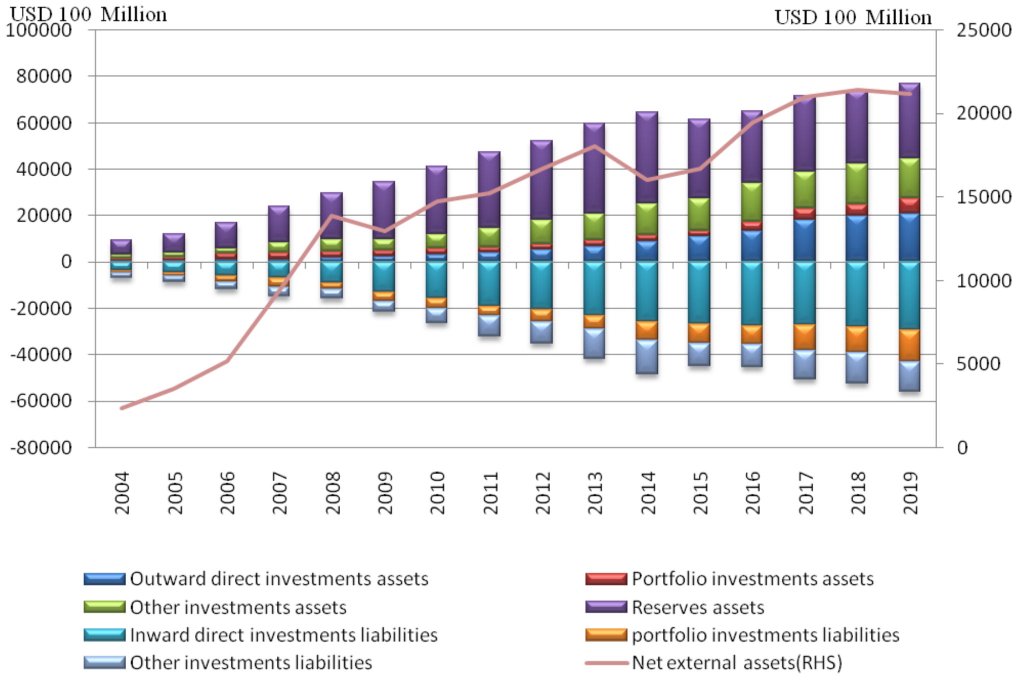
[9]The statistics are from data published on the World Bank website in January 2020.

medium-term and long-term foreign debt, local currency foreign debt, and debt securities, the structure of foreign debt continued to stabilize. In particular, as a "risk sharing" capital inflow, debt securities played the role of a stabilizer of the foreign debt structure. At end-December 2019, the balance of debt securities was USD 529.3 billion, of which more than 80percent was medium and long-term foreign debt and nearly 70percent was RMB bonds, with low risks of maturity and a currency mismatch. From the perspective of the composition of investment, foreign investors mainly invested in medium-term and long-term RMB treasury bonds, and the main investors were foreign central banks, whose purpose was to allocate assets for the long term, not for short-term profits, and their investments had an inherent stability.

III. International Investment Position

China's external financial assets and liabilities[10] were both on the rise. At end-December 2019, China's external financial assets reached USD 7714.5billion, representing growth of 4.2percent compared to end-2018; external liabilities reached USD 5590.5 billion, up 6.3 percent; and net assets reached USD 2124.0 billion, down1.0 percent (see Chart 3-1).

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



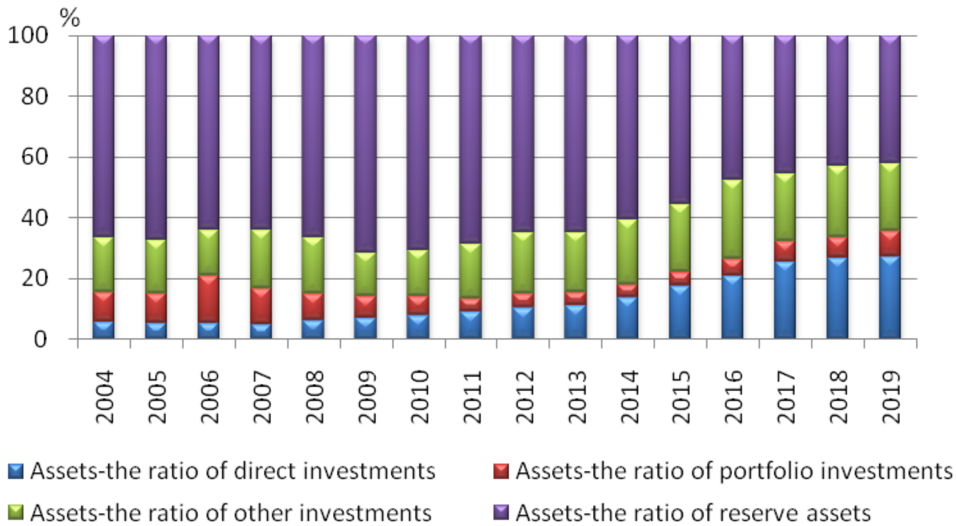
Source: SAFE.

Reserve assets remained the largest component of total external assets,

[10]External financial assets and liabilities include direct investments, portfolio investments, and other investments, such as loans and deposits. 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.

and private-sector holdings continued to rise. Among the external financial assets, at end-December 2019 reserve assets amounted to USD 3222.9 billion, up by 1.9 percent, of which USD 19.3 billion was due to BOP transactions and USD 74.2billion was due to changes in exchange rates and prices other than BOP transactions. As the largest component, reserve assets accounted for 42 percent of total external assets, a historical low since China's first IIP statement at end-December 2004. Direct-investment assets amounted to USD 2094.5billion, accounting for 27 percent of total assets, up by 0.4 percentage point. Portfolio-investment assets amounted to USD646.0 billion, accounting for 8 percent, up by 1.6 percentage points.Financial-derivative assets amounted to USD6.7 billion, accounting for 0.1 percent. Other investments, such as loans and deposits, amounted to USD 1744.3 billion, accounting for 23percent,down by 1 percentage point(see Chart 3-2).

Chart 3-2 The Structure of External Financial Assets

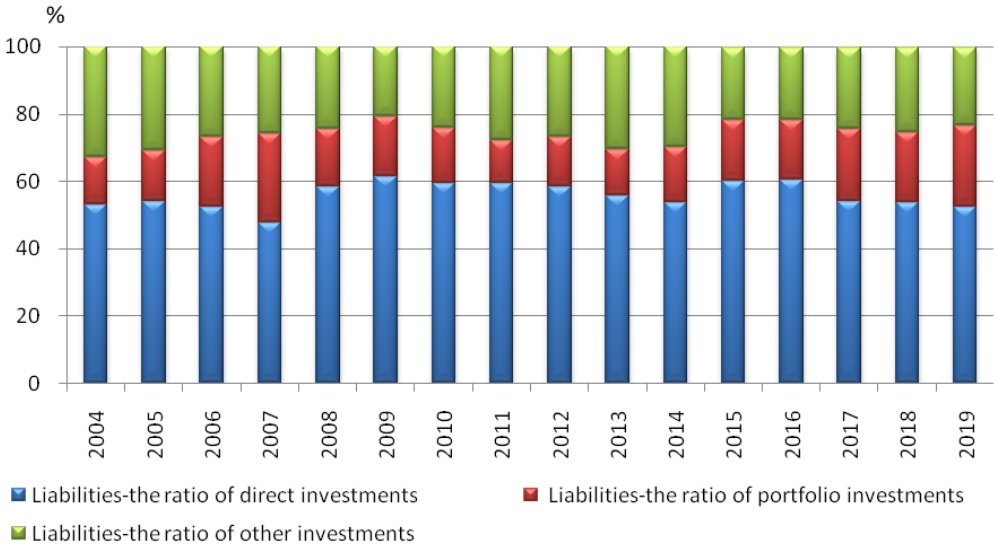


Although foreign direct investments remained the major item in

external liabilities, the proportion of portfolio investments grewrapidly. Among theexternal liabilities, FDI totaled USD 2928.1 billion at end-December 2019,[11] up 3.6 percent. Continuing as the largest component, FDI accounted for 52 percent of total external liabilities, 1.4 percentage points less than that at end-December 2018. Portfolio-investment liabilities amounted to USD 1364.6 billion, accounting for 24 percent, up by 3.6 percentage points, reflecting the great progress that overseas investment made in China's domestic securities market.At end-December 2019, the market value of foreign investors' positions in China's domestic securities market was about USD 650 billion, of which the stock position accounted for 4.3percent of the total market value of A-shares, 1.1 percentage points higher than that at end-December 2018; the bond position accounted for 2.3percent of total domestic bonds in custody, 0.2 percentage point higher than that at end-December 2018, reflecting the result of steady expansionof the opening up and the deepened reform of China's financial market.Other investments, such as loans and deposits, amounted to USD 1291.3 billion, accounting for 23 percent,down by 2.2 percentage points (see Chart 3-3).

[11]The inward FDI positionincludes FDI stocks of both the non-financial sector and the financial sector. The position includes inter-company lending as well as other debt positions among the relevant offices. The statistics also reflect the impact of revaluations.

Chart 3-3 The Structure of External Liabilities



Box 4

External Assets and Liabilities in China's Banking Sector at end-December 2019

By end-December 2019, the scale of external assets and liabilities in China's banking sector had increased, whereas net liabilities had decreased. External assets reached USD 1170.9 billion,[12] a year-on-year increase of 5 percent and accounting for 15 percent of China's external assets.[13]The external liabilities of China's banking sector reached USD 1330.1 billion, a year-on-year increase of 3 percent and accounting for 24 percent of China's external liabilities. China's net liability position was USD 159.1 billion, down 12 percent yearon year.

Among the external financial assets, loans and deposits accounted for over 70 percent of the outstanding claims and the percentage share of debt securities was the same as that of equity assets. External loans and deposit assets of China's banks totaled USD 832.1 billion, basically the same as that in the last year, accounting for 71 percent of the banking sector's total external assets, and mainly consisting of loan assets. Investments in

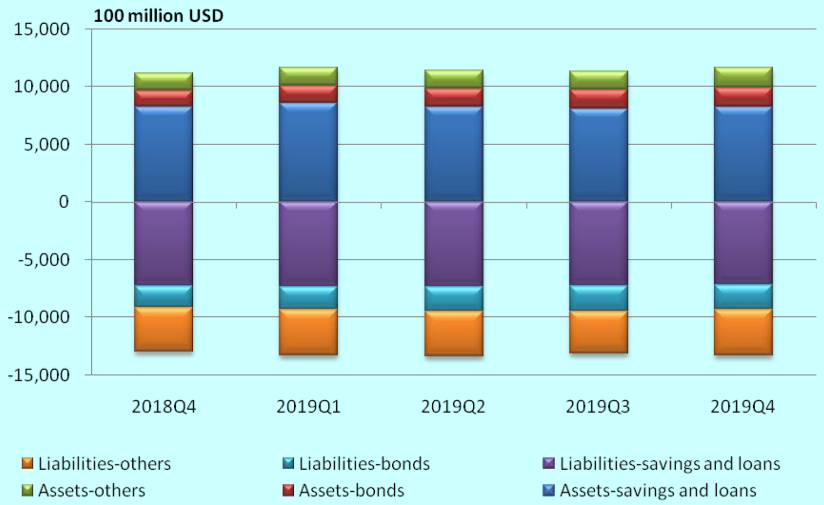
[12]The data are derived from the *Statistical Report on External Assets and Liabilities* of the State Administration of Foreign Exchange. Since end-December 2015, China has participated in the international banking statistics of the Bank for International Settlements and it began to submit cross-border financial assets and liabilities of Chinese banks on a quarterly basis. This box is based on data reported at end-December 2019.

[13] The positions of external assets include international reserve assets. If international reserve assets are excluded, the banks' external assets constitute 26 percent of China's total external assets.

overseas bonds was USD 163.0 billion, up 19 percent, accounting for 14 percent of the banks' total external assets, mainly due to increased holdings of shares issued in the US and Hong Kong markets. Other assets such as investments in overseas equity and financial derivatives totaled USD 175.9 billion, up 18 percent and accounting for 15 percent of the banks' total external assets, mainly due to increased outward direct investments in equity (see Chart C4-1).

Among the external liabilities, more than one-half were deposits and loans. The portion of debt securities increased, whereas the portion of other investments declined. Loans and deposits in China's banking sector amounted to USD 721.5 billion, a year-on-year decrease of 1 percent and accounting for 54 percent of the banks' external liabilities. This was mainly due to the decrease in deposits from the overseas banking sector. Debt securities amounted to USD 212.7 billion, an increase of 15 percent and accounting for 16 percent of external liabilities. This was mainly due to an increase in bonds issued by the domestic banking sector in overseas markets and an increase in foreign investors' holdings of bonds issued in the domestic market. Other investments such as financial derivatives and equity liabilities amounted to USD 395.9 billion, a year-on-year decrease of 3 percent and accounting for 30 percent of external liabilities.

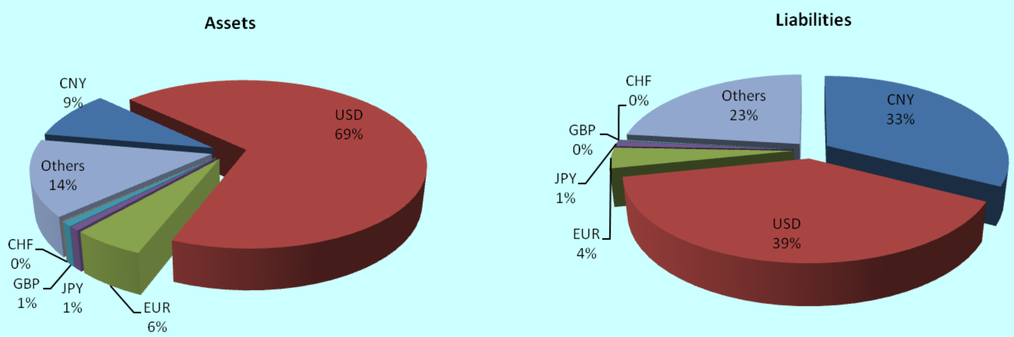
Chart C4-1 The Structure of External Assets and Liabilities in China's Banking Sector



Source: SAFE.

In terms of currency, China's banking sector recorded net foreign-exchange external assets and net RMB liabilities. At end-December 2019, the banks' external USD assets amounted to USD 806.7 billion, a year-on-year increase of 4 percent and accounting for 69 percent of the banks' total external assets. The major contributors were the expansion of USD debt securities. RMB assets amounted to USD 109.2 billion, a decrease of 10 percent year on year and accounting for 9 percent of the banks' total external assets. The decrease in RMB bond investments played a major role. External assets in other foreign currencies amounted to USD 255.1 billion, 22 percent of the external assets. USD liabilities amounted to USD 520.5 billion, an increase of 3 percent year on year and accounting for 39 percent of the external liabilities. RMB liabilities amounted to USD 433.5 billion, an increase of 7 percent and accounting for one-third of the external liabilities, which were mainly due to the increased holding of RMB debts by foreign investors. External liabilities in other foreign currencies amounted to USD 376.1 billion and accounted for the remaining 28 percent of the external liabilities. In terms of net assets and liabilities, Chinese banks recorded net liabilities of USD 324.3 billion in RMB, a year-on-year increase of 14 percent, and net assets of USD 165.2 billion in foreign currencies, an increase of 60 percent year on year (see Chart C4-2).

Chart C4-2 The Structure of External Assets and Liabilities in China's Banking Sector by Currency



Source: SAFE.

In terms of counter-party sectors, the non-banking sectors and the banking sectors shared the same proportionsof external assets, whereas the non-banking sectors dominated in external liabilities. At end-December 2019, the external assets of China's banking sector in the overseas banking sector amounted to USD 588.2 billion, an increase of 7 percent year on year. The increase was due to the appreciation of overseas equity assets. External assets in overseas non-banking sectors amounted to USD 582.7 billion, up2 percent year on year and accounting for 50 percent of the banking sector's total external assets. The increase was mainly due to the increased holdings of bonds issued by overseas non-banking sectors. Chinese banks' external liabilities in overseas banks amounted to USD 536.1 billion, down7 percent year on year and accounting for 40 percent of the banks' total external liabilities. External liabilities in the overseas non-banking sectors amounted to USD 794.0 billion, up 10 percent and accounting for 60 percent of the total, mainly due to the increased deposits by overseas non-banking sectors. From the perspective of net assets and liabilities, Chinese banks had net assets of USD 52.1 billion in overseas banks, whereas in the previous year, it had net liabilities of USD 28.0 billion. Chinese banks had net liabilities of USD 211.3 billion in overseas non-banking sectors, an increase of 38 percent.

In terms of counter-party countries/regions in the external position, the advanced economies and offshore centers were the major counter-parties. The top three debtor economies of Chinese bank investments were: Hong Kong SAR (USD 322.7 billion), the U.S. (USD 122.1 billion), and the British West Indies (USD 52.3 billion), accounting for 28 percent, 10 percent, and 4 percent, respectively, of Chinese banks' total external assets. The top three creditor economies of the external liabilities of Chinese banks were: Hong Kong SAR (USD 674.8 billion), Singapore (USD 137.0 billion), and Taiwan Province of China (USD 93.5 billion). They contributed 51 percent, 10 percent, and 7 percent, respectively, of total investments in Chinese banks (see Chart C4-3).

Chart C4-3 The Structure of External Assets and Liabilities of China's Banking Sector by Country/Region

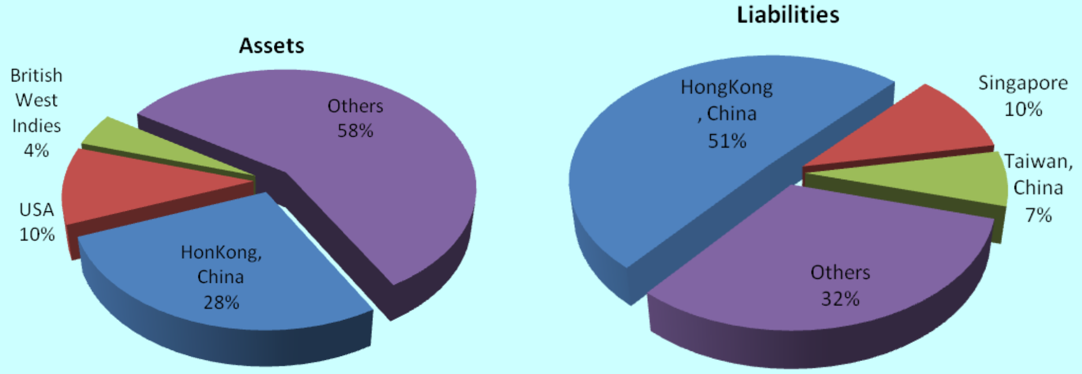


Table C4-1 Table on the Structure of External Assets and Liabilities in China's Banking Sector at End-2019

Unit：100 million of USD

		Assets		**Liabilities**		**Net assets**
		Amounts	Ratio	Amounts	Ratio	Amount
By Tools	Deposits and loans	8321	71%	7215	54%	1106
	Debt securities	1630	14%	2127	16%	–497
	Other	1759	15%	3959	30%	–2200
By Sectors	Bank	5882	50%	5361	40%	521
	Non-bank	5827	50%	7940	60%	–2113
By currencies	CNY	1092	9%	4335	33%	–3243
	USD	8067	69%	5205	39%	2862
	EUR	646	6%	519	4%	128
	JPY	95	1%	141	1%	–45
	GBP	108	1%	22	0%	84
	Other	1701	15%	3078	23%	–1377
Total		**11709**	**100%**	**13301**	**100%**	**–1591**

Source: SAFE.

Table 3-1 China's International Investment Position at End-December 2019

Unit: US $100 million

	Line No.	2019
Net International Investment Position[14]	**1**	**21,240**
Assets	**2**	**77,145**
1 Direct investments	**3**	**20,945**
1.1 Equity and investment fund shares	**4**	17,811
1.2 Debt instruments	**5**	3,135
1.a Financial sector	**6**	2,839
1.1.a Equity and investment fund shares	**7**	2,739
1.2.a Debt instruments	**8**	100
1.b Non-financial sector	**9**	18,107
1.1.b Equity and investment fund shares	**10**	15,072
1.2.b Debt instruments	**11**	3,035
2 Portfolio investments	**12**	**6,460**
2.1 Equity and investment fund shares	**13**	3,738
2.2 Debt securities	**14**	2,722
3 Financial derivatives (other than reserves) and employee stock options	**15**	**67**
4 Other investments	**16**	**17,443**
4.1 Other equity	**17**	84
4.2 Currency and deposits	**18**	4,179
4.3 Loans	**19**	6,963
4.4 Insurance, pensions, and standardized guarantee schemes	**20**	135
4.5 Trade credits and advances	**21**	5,604
4.6 Other accounts receivable	**22**	479
5 Reserve assets	**23**	**32,229**
5.1 Monetary gold	**24**	954
5.2 Special drawing rights	**25**	111
5.3 Reserve position in the IMF	**26**	84
5.4 Foreign currency reserves	**27**	31,079
5.5 Other reserve assets	**28**	0
Liabilities	**29**	**55,905**
1 Direct investments	**30**	**29,281**
1.1 Equity and investment fund shares	**31**	26,748

[14] 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.

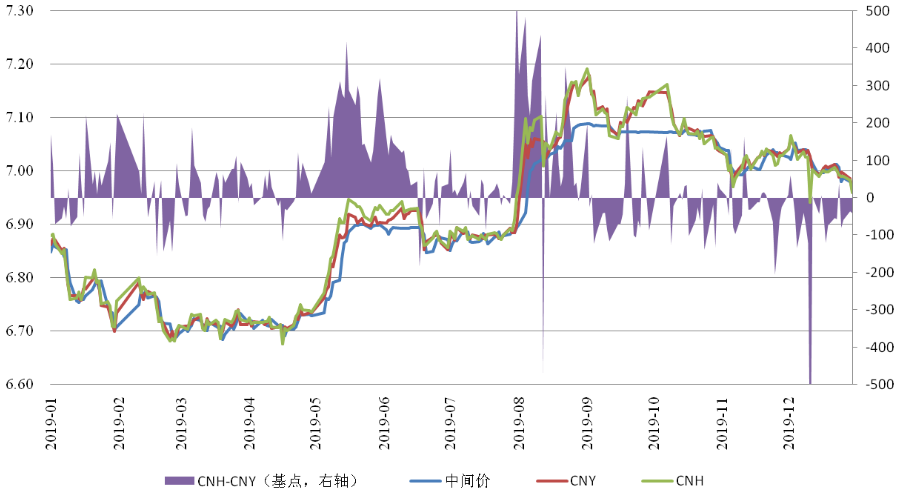
1.2 Debt instruments	**32**	2,533
1.a Financial sector	**33**	1,605
1.1.a Equity and investment fund shares	**34**	1,426
1.2.a Debt instruments	**35**	179
1.b Non-financial sector	**36**	27,676
1.1.b Equity and investment fund shares	**37**	25,321
1.2.b Debt instruments	**38**	2,354
2 Portfolio investments	**39**	**13,646**
2.1 Equity and investment fund shares	**40**	8,617
2.2 Debt securities	**41**	5,029
3 Financial derivatives (other than reserves) and employee stock options	**42**	**65**
4 Other investments	**43**	**12,913**
4.1 Other equity	**44**	0
4.2 Currency and deposits	**45**	4,245
4.3 Loans	**46**	4,605
4.4 Insurance, pensions, and standardized guarantee schemes	**47**	135
4.5 Trade credits and advances	**48**	3,644
4.6 Other accounts payable	**49**	189
4.7 Special drawing rights	**50**	97

Source: State Administration of Foreign Exchange.
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.

(I) Trends in the RMB Exchange Rate

The RMB exchange rate was relatively stable against the USD. At the end of December 2019, the mid-price of the RMB exchange rate against the USD was 6.9762,a depreciation of1.62percent from end-2018.The RMB spot exchange rate against the USD in the inter-bank foreign-exchange market (CNY) and in the offshore market (CNH) depreciatedby1.44percent and1.14 percent,respectively (see Chart 4-1). The average daily spread between the CNH and the CNY was 96 bps, lower than the 102 bps in 2018. At the beginning of August2019, asSino-US trade frictions further escalated,driven by market factors the RMB exchange rate against the USDdepreciated to 7. Since September 2019, exchange-rate expectations havetended tobe stable.The RMB exchange rate against the USD andagainst a basket of currencies both appreciated; the offshore and onshore RMB exchange rate against the USD appreciatedbelow7 on multiple occasions, and stabilized below 7 after December2019. During 2019, the RMB exchange rate flexibilitysignificantly increased, playing a role as an "automatic stabilizer" in adjusting the macro economy and the international balance of payments.

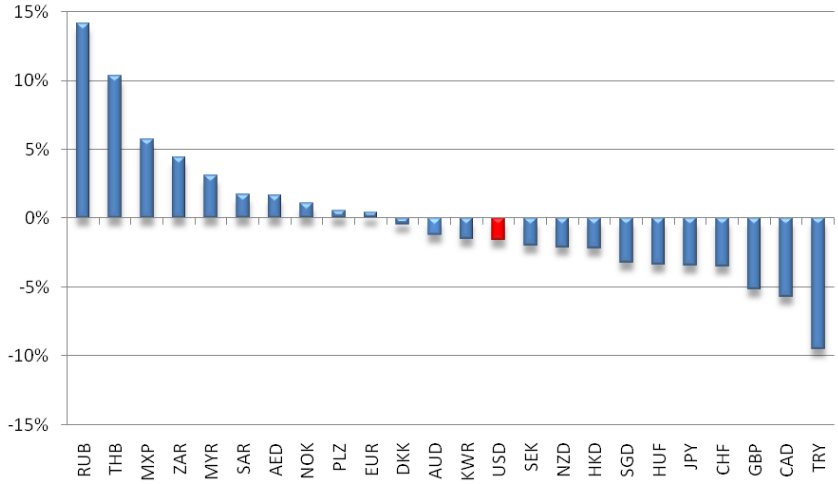
Chart 4-1 Trends in the RMB Spot Exchange Rate Against the USD in the Domestic andOffshore Markets, 2019



Sources: CFETS, Reuters.

Trends inthe RMB exchange rates against other major international currencies diverged. At the end of2019, the mid-price of the RMB exchange rate against the EUR,100JPY, GBP, AUD, and CAD stood at 7.8155，6.4086，9.1501,4.8834, and 5.3421,respectively, an appreciation of 0.41percent,a depreciation of 3.43 percent, 5.18 percent,1.21 percent,and 5.69 percent,respectively (see Chart 4-2).

Chart 4-2 The Amplitude of the RMB Daily Reference Rates Against the Major Developed and Emerging Market Currencies

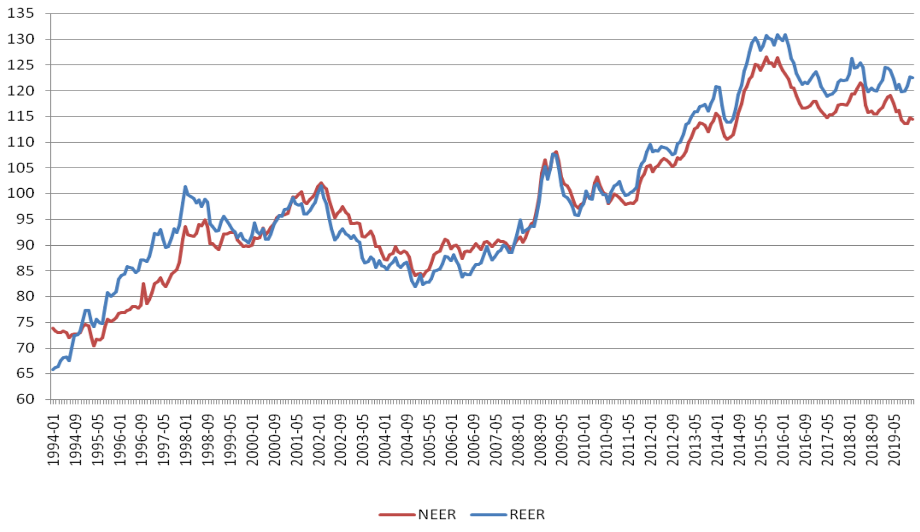


Source: CFETS.

The RMB exchange rate was basically stable against the basket of currencies. According to CFETS data, at the end of 2019 the RMB exchange-rate indexes against the CFETS, the BIS basket of currencies, and the SDR basket of currencies were 91.39, 95.07, and 91.81,respectively, a depreciation of 2.02 percent, 1.76 percent, and 1.42 percent,respectively, from the end of the previous year.

According to the BIS, the nominal effective exchange rate of the RMB depreciated by 1.5 percent in 2019; deducting for inflation, the real effective exchange rate of the RMB appreciated by 1.1percent (see Chart 4-3). Since the reform of the exchange-rate regime in 2005, the nominal and real effective exchange rates of the RMB appreciated by32.3 percent and 41.6 percent, respectively.

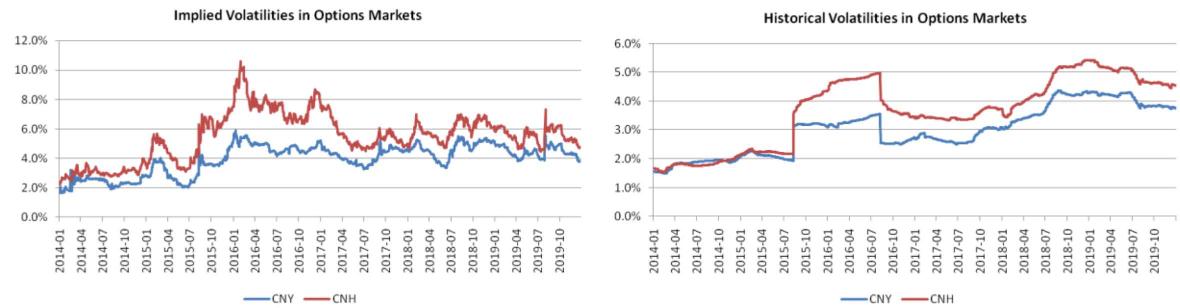
Chart 4-3 Trends in the Effective RMB Exchange Rate



Source: BIS.

The RMB exchange rate fluctuated in both directions with high flexibility. At the end of 2019,the one-yearhistoric volatilityof the RMB exchange rate in the domestic and offshore markets stood at 3.8 percent and 4.6 percent,respectively, down 0.5 percent and 0.9 percent from the beginning of 2019,respectively, still remaining at a historic high level. The implied volatilities in the domestic and offshore options markets reached 3.8 percentand 4.7 percent, respectively, down1.4 percent and 1.3 percent from the beginning of 2019, respectively (see Chart 4-4).

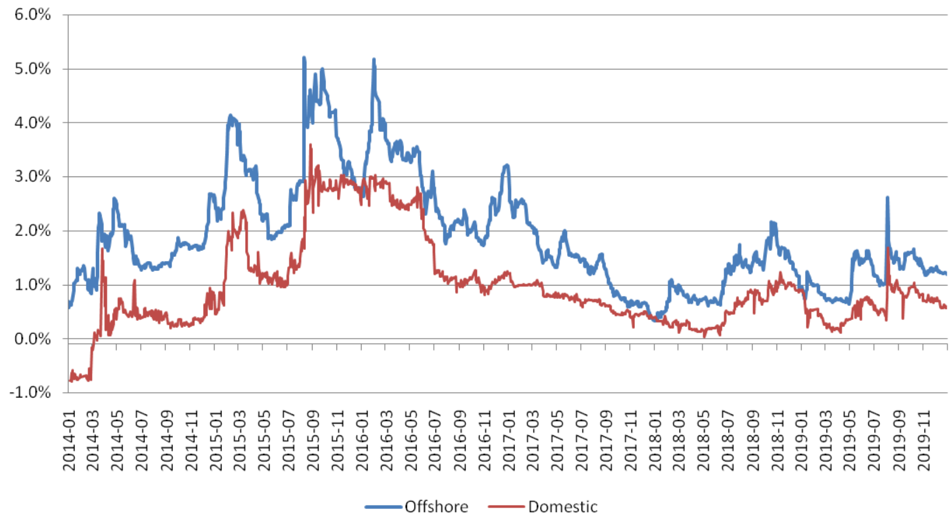
Chart 4-4 Volatility of the 1-Year RMB Exchange Rates Against the USD in the Domestic and Offshore Markets



Source: Bloomberg.

The options market showed stable expectations of the RMB exchange rate. In 2019 domestic and offshore risk reversal indexes (the difference between the volatility of the USD call/RMB put options and the USD put/RMB call options) were 0.61 percent and 1.18 percent,respectively. They were 0.92 percent and 0.93percent,respectively,at the end of the last year (see Chart 4-5).During the entire year of 2019, the domestic risk reversal indexes first declined,then went up, and finally declined, while the highest level in 2019 was far below the historic high, thus indicating that exchange-rate expectations were stable.

Chart 4-5 The 1-Year Risk Reversal Indexes of the RMB Against the USD in the Domestic and Offshore Option Markets



Source: Bloomberg.

Box5

With the RMB Exchange Rate Fluctuating in Both Directions,Enterprises Still Need to Strengthen Risk Management

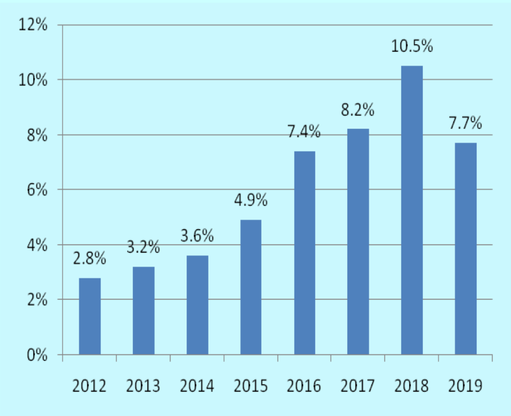
In recent years, the degree of marketizationof the RMB exchange rate significantly increased andexchange-rate flexibility was obviouslyenhancedas thedual-direction fluctuations normalized. In 2019 the SAFE conducted a survey of more than 2,400 enterprises across China about exchange-rate risk management. The results indicate that spot transactionswere still the first choice of most companies. Enterprises worry that derivatives transactions might induce losses and their awareness of exchange-rate risk management still needed to be strengthened.

(I) The degree of marketization of the RMB exchange rate has increased significantly.

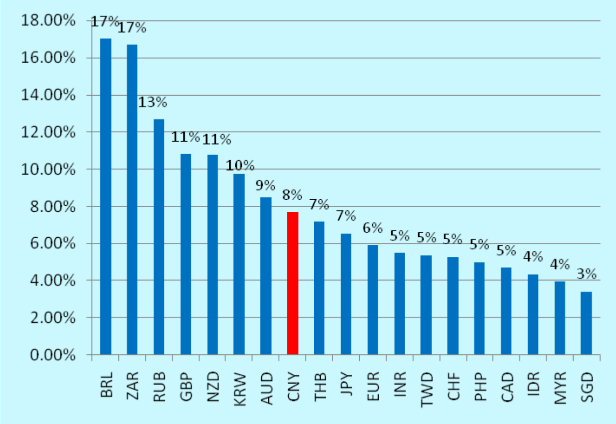
In 2019 the RMB exchange rate remained stable at a reasonable level and its flexibility increased. From the perspective of its performance during the entire year, due to the influence of the escalation of trade protectionism and the increasing volatility in the financial market, the exchange rates of many currencies against the USD depreciated. For example, the Euro exchange rate against the USD depreciated by 2.3 percent and the index of emerging market currencies depreciated by 1.3 percent. Directly impacted by the Sino-US economic and trade frictions, the RMB onshore spot exchange rate against the USD (CNY) depreciated slightly by 1.4 percent, and its performance ranked middle among global non-USD currencies. In terms of volatility, in 2019 the fluctuation of the RMB exchange rate against the USD reached 7.7 percent between the highest point and the lowest point, a comparatively high level in recent years. Compared with other major currencies, the elasticity of the dual-direction fluctuations of the RMB ranked middle and generally remained at a relatively appropriate level.

Chart C5-1 RMB Exchange-Rate Fluctuations

Annual volatility of the RMB exchange rate against the USD (CNY)



Fluctuations of exchange rates of the major currencies against the USD in 2019



Source: Bloomberg.

（II）Gradual full development of domestic foreign-exchange derivatives markets.

In 1994, China started the RMB exchange-rate system reform oriented toward a managed floating system, and demands for exchange-rate hedging gradually emerged. In 1997a foreign-exchange forward transactions pilot program was launched. After the 2005exchange-rate regime reform, development of foreign-exchange derivatives markets accelerated dt. In 2019, the trading volume of derivatives transactions in the domestic foreign-exchange market totaled USD 17.8 trillion, almost 579 times the volume in 2005.

The foreign-exchange derivatives marketsbasically providesmature international products. Currently, the market offers spots, forwards, foreign-exchangeswaps, currencyswaps, and options products (European options and other products). In 2019 the client market of derivatives saw a trading volume of USD 693 billion, with forwards, swaps, and options accounting for 44 percent, 17 percent, and 39 percent, respectively.

The participating banks in foreign-exchange derivatives basically covered the demands of the market. By the end of 2019, therewere 518 and 105 financial institutions with spot and derivative transaction qualifications,respectively. Their services covered all regions,, basically without omissions.

(III)The main shortcoming of the market is in that exchange-rate risk management of enterprises is weak.

The special survey indicates the following characteristics of enterprises' current hedging transactions. First, largerscale andhigh risk-exposure enterprises have stronger awareness of risk hedging. Second, small and medium-sized enterprises tend to passively manage exchange-rate risks only when RMB fluctuations are increasing and when exchange-rate risks are enlarging. Third, the degree of understanding of foreign-exchange derivatives determines the participation of enterprises. Most companies engage in fewer transactions because they are unfamiliar with the products. Fourth, some enterprises are reluctant to use foreign-exchange derivatives for hedgingsince they worry about losses or other costs. Fifth, enterprises are extremely sensitive to exchange losses and profits,and theirevaluation of hedging effects needs to be further optimized. Sixth, there are significant differences in foreign-exchange hedging among enterprises of different regions and types. The eastern region, state-owned enterprises, and large foreign enterprises perform relatively better.

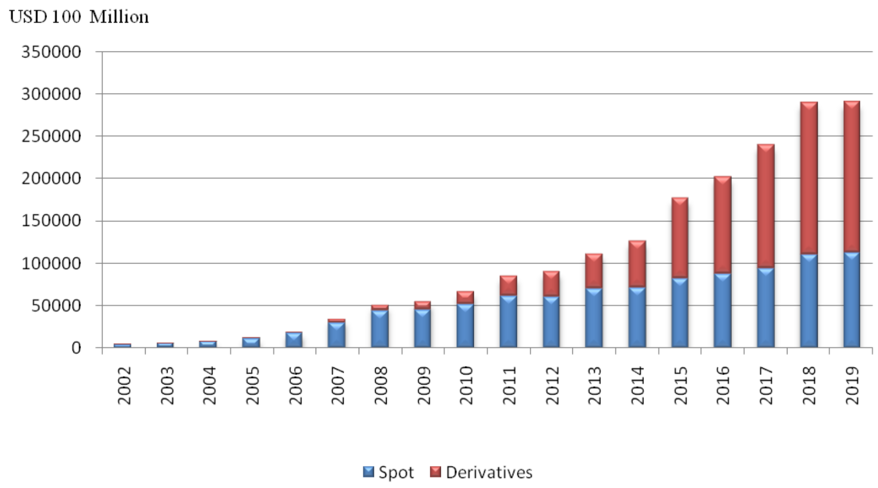
As the entities of exchange-rate risk management, enterprises' exchange-rate risk management concepts and capabilities determine the speed and breadth of the development of China's foreign-exchange derivative market.A top priority will be to vigorously cultivate enterprises' exchange-rate hedging awareness and ability and especially to guide enterprises to build "risk neutrality" when deepening the development and opening of the foreign-exchange market in the future.On the one hand, while focusing on the financial supply side structural reforms, the SAFE will continue to deepen the development of the foreign-exchange market. We will focus on the enterprises' need for exchange-rate hedging, gradually expand the coverage of foreign-exchange derivatives, appropriately enlarge the trading entities, and improve the management of transactions based on actual demands so that we can better meet the hedging demands of market entities.On the other hand, we will improve monitoring and risk prevention in the foreign-exchange market. Oriented toward serving the real economy and meeting the actual needs of enterprises, we will further strengthen market education and training to guide enterprises to enhance their awareness and ability to manage exchange-rate risks. Enterprises should focus on their main businesses to avoid exchange-rate speculation, to reasonably evaluate risks and transactions, and to participate in the foreign-exchange market both legally and effectively.

(II) Transactions in the Foreign-Exchange Market

In 2019the cumulative trading volume of the RMB/foreign-currency market totaled USD29.12trillion, an increase of 0.2 percent from the same period of the previous year (see Chart 4-6), with an average daily trading volume of USD 119.3 billion. The total trading volume in the client market and the inter-bank market was USD4.11 trillion and USD 25.01trillion,[15] respectively. Spot and derivative transactions witnessedtrading volumes of USD11.36 trillion and USD17.76 trillion, respectively (see Table 4-1). According totheBIS survey offoreign-currency and derivatives markets in 2019, the RMB has become the 8th most traded currency in the world, accounting for a 4.3 percent share of the volume of global foreign-currency trading.

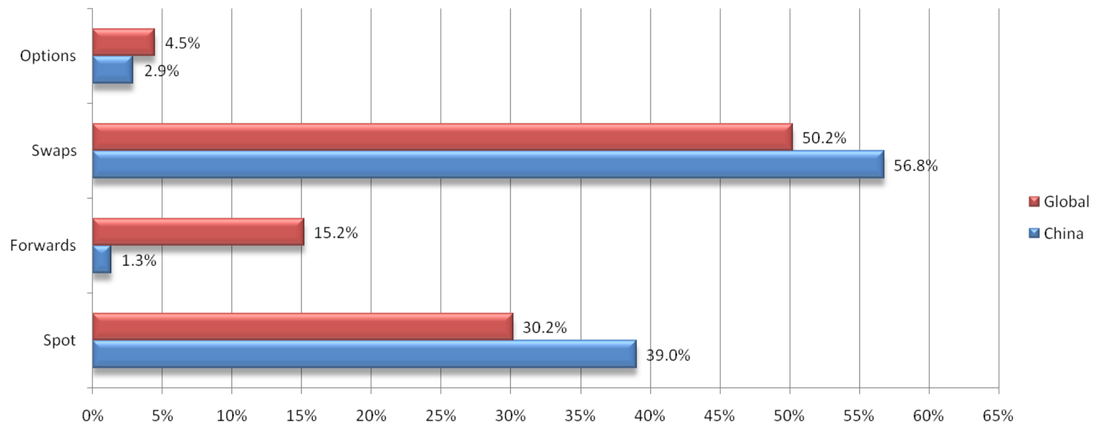
[15]The client market uses the total volume of both purchases and sales of foreign exchange. The inter-bank market uses the unilateral trading volume. The same as below.

Chart 4-6 Trading Volume in China's Foreign-Exchange Market



Sources: SAFE, CFETS.

Chart 4-7A Comparison of the Structure of Products in the Domestic and Global Foreign-Exchange Markets



Note: The data for China were due from the BIS by the end of2019,and the globaldatawere due by end-April,2019.
Sources: SAFE, CFETS, BIS.

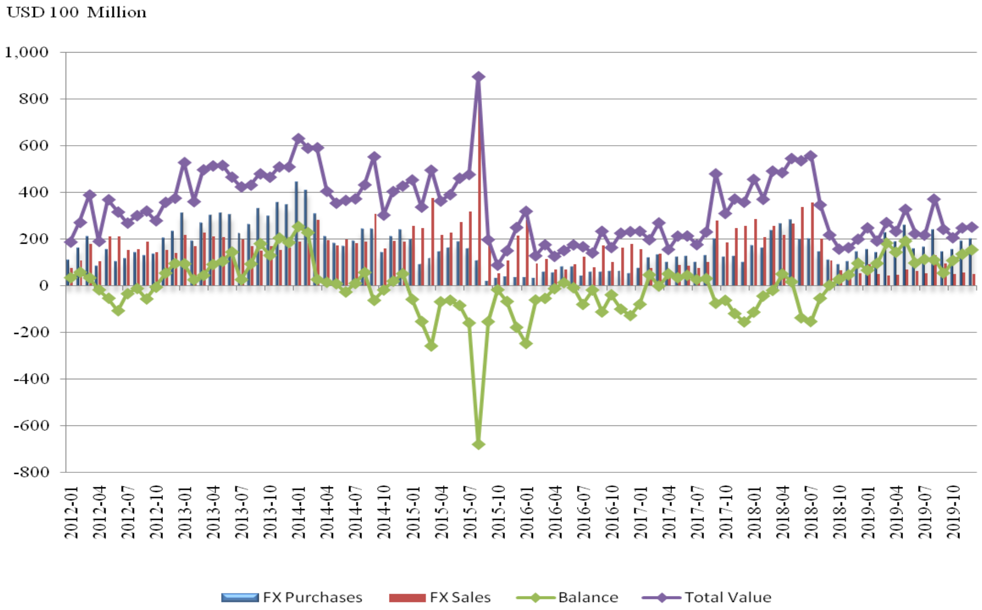
Steady growth of foreign-exchange spot transactions. In 2019the spot foreign-exchange market saw a trading volume of USD11.36 trillion,up 3 percent from the same period of theprevious year. Spot purchases and sales of foreign exchange in the client market totaled USD 3.42 trillion (including banks, but excluding implementation of forwards), down 0.4 percent from the previous year. The spot inter-bank foreign-exchange market saw a trading volume of

USD 7.94trillion, up 4 percent from the previous year; the share of USD transactions was 96 percent.

Foreign-exchange forward transactionsdeclined. In 2019the forward market saw a trading volume of USD380.6billion, down 30 percent from the previous year. In the client market, purchases and sales of forwards in foreign exchange totaled USD 304.7billion, Purchases andsalesof forwards were USD224.9billion and USD 79.8 billion, down 33 percent, respectively, up 43.7 percent, respectively, and down 67 percent,respectively (see Chart4-8). Short-term 6-month transactions accounted for 70 percent of the total transactions, up5.0 percent from the previous year. In the inter-bank foreign-exchange market, forwards transactions totaled USD 76.0 billion, down 13 percent from the previous year.

Swap transactions declined. In 2019 cumulative foreign-exchange and currency-swap transactions totaled USD 16.53 trillion,down1percent from the previous year. Cumulative foreign-exchange and currency-swap transactions in the client market reached USD119.5billion, up 15 percent from the previous year,spot purchases/forward sales and spot sales/forward purchases stood at USD 103 billion and USD 16.5 billion, respectively, up12 percent and 41percent fromthe previousyear,respectively.The cumulative foreign-exchange and currency-swap transactions in the inter-bank market reached USD 16.41 trillion,down1 percent from the previous year. Swaps are an important tool for banks to manage liquidity in domestic and foreign currencies, particularly for short-term transactions. Transactionswithin3months accounted for 86 percent of the total transactions.

Chart 4-8 The Trading Volume ofPurchases and Sales of Forward Foreign-Exchange Transactions in the Client Market

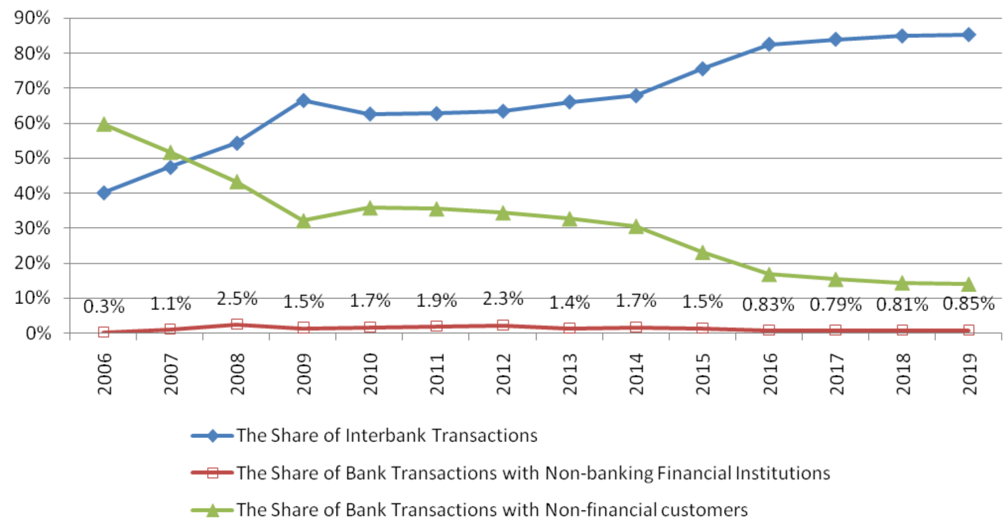


Source: SAFE.

Faster growth in options transactions. In 2019the trading volume of options totaled USD 850billion, up 0.3 percent from the previous year. The client market saw a total trading volume of USD 268.8 billion, up14 percentfrom the previous year. The inter-bank market saw a total trading volume of USD 581.2 billion, down 5 percent from the previous year.

Foreign-exchange market participants remained stable. Proprietary transactions by banks continued to dominate (see Chart 4-9). In 2019 the share of inter-bank transactions among all foreign-exchange transactions was up to 85.2 percent,from84.8 percent in 2018. The share of bank transactions with non-financial customers declined from 14.4 percent to 14.0 percent. The share of non-banking financial institutions was 0.8 percent, basically the same as that in 2018. According to the BIS survey of foreign-currencies and derivatives markets in 2019, the share of non-bank financial institutions, including hedge funds and investment banks, was 30 percent in international foreign-currencies markets, indicating that there is still room for diversificationof the participants.

Chart 4-9 The Structure of Participants in China's Foreign-Exchange Markets



Sources: SAFE, CFETS.

Table 4-1 Transactions in the RMB/Foreign-Exchange Markets, 2019

Product	Trading Volume (100 million USD)
Spot	**113561**
Client Market	**34188**
Interbank Foreign Exchange Market	**79374**
Forward	**3806**
Client Market	**3047**
Less than 3 months (including 3 months)	1474
3 months to 1 year (including 1 year)	1318
More than 1 year	255
Interbank Foreign Exchange Market	**760**
Less than 3 months (including 3 months)	546
3 months to 1 year (including 1 year)	176
More than 1 year	37

Foreign Exchange and Currency Swaps	**165329**
Client Market	**1195**
Interbank Foreign Exchange Market	**164134**
Less than 3 months (including 3 months)	141884
3 months to 1 year (including 1 year)	21344
More than 1 year	906
Options	**8500**
Client Market	**2688**
Foreign Exchange Call Options/RMB Put Options	1355
Foreign Exchange Put Options/RMB Call Options	1333
Less than 3 months (including 3 months)	1006
3 months to 1 year (including 1 year)	1442
More than 1 year	241
Interbank Foreign Exchange Market	**5812**
Less than 3 months (including 3 months)	3779
3 months to 1 year (including 1 year)	2011
More than 1 year	23
Total	**291196**
Client Market	**41118**
Interbank Foreign Exchange Market	**250079**
Including: Spots	113561
Forwards	3806
Foreign Exchange and Currency Swaps	165329
Options	8500

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

Sources: SAFE, CFETS.

V. Outlook for the Balance of Payments

In 2020 China's balance of payments is expected to continue its overall pattern of a basic balance. Although there are still many unstable and uncertain factors influencing the status of the balance of payments, including the novel corona-virus pneumonia that will affect the global economy and international trade development, the international financial market will show volatility as therisks of geopolitical conflictswill continue to be high; the factors on the ground, such as economic fundamentals, the opening-up policy, and the market-regulation mechanism, will still play a leading role, so the current account will remain within a reasonable range andwill be conducive to the overall stability of cross-border capital flows.

In the future, the internal foundation for China's balance of payments will remain stable. In recent years, against the backdrop of the complex and changeable internal and external environments, China's balance of payments maintained a basic balance, reflecting the supporting role played by domestic fundamentals, including the stable domestic economy, the gradual optimization of the economic structure, the active and effective macro-controls, the continuous expansion of the opening-up, and the increasingly mature foreign-exchange market. From the perspective of future trends: first, the long-term stable and positive trendsin the domestic economy will not change, which will help consolidate market and investor confidence. China's economic development has enough resilience and huge potential, and there is relatively large space for counter-cyclical adjustments of macro policies. The continuous deepening of the supply-side structural reforms will provide effective support for smooth economic operations. Second,the potential and space for reform and opening up are still large, which will help to attract foreign capital to invest in the domestic market. For example, the Foreign Investment Law and the new Securities Law will be fully implemented in 2020. The financial sector will be openedmore rapidly to the outside world, the business environment will be continuously optimized, and the level of facilitation of cross-border trade and investment will be further improved. Third, the maturity of the foreign-exchange market will be improved, which will help to enhance the market-adjustment capability of the balance of payments. With the gradual improvement in the RMB exchange-rate formation mechanism, exchange-rate flexibility has been continuously enhanced, playingan important role in allocating foreign-exchange resources, stabilizing the balance of payments, and enhancing macro-economic resilience; at the same time, the foreign-exchange balance behavior of market subjects will be more rational and orderly, which will have more of an effect on short-term risks; in addition, macro-prudential management of cross-border capital flows in China has accumulated rich experience andthe foreign-exchange market has also maintained good order.

The current account is expected to maintain a basic balance. First, trade in goods will maintain a reasonable surplus. Although the pneumonia epidemic will have an impact on the export and import of goods, China's manufacturing industry chain is complete, with accelerated transformation and upgrading, and the international competitiveness of related products is still strong. Therefore,China’s position in the international division of labor is generally stable. At the same time, the conclusion of the first phase of the economic and trade agreement between China and the United States is conducive to economic and trade exchanges between the two countries,which will enhanceglobal trade confidenceand will play a role in promoting foreign-trade imports and exports. In addition, the fall of international crude oil prices will also reduce the amount of China's relevant imports. Second, the services trade deficit will continue to develop steadily. Since 2015, the growth rate of China's services trade deficit has remained at a relatively low level, and in 2019, there was a slight decline, reflecting the change in the residents' consumption concepts and improvement in the country's soft power. In the future, with economic development and improvementsinthe quality of domestic servicesand the level of education, the services trade deficit will mainly be stable and may continue to narrow. Third, optimization of the foreign-investment structure will allow the investment-income deficit to continue to improve. In recent years, as the balance of foreign assets in the form of direct investments has been growing steadily, the related outward investment income will gradually increase, and the investment income deficit will gradually narrow. In addition, at present China's savings rate is still over 40percent, ranking the top in the world, which will help to maintain the current-account balance within a reasonable range for the medium and long-term.

Cross border capital flows will mainly remain steady. First, China's economic growth is robust and outstanding in the world, which is conducive to the stability of inward direct investments and other medium and long-term capital inflows. In recent years, with the overall decline in global direct investments, the utilization of foreign capital by non-financial enterprises in China has increased.In 2019 the scale of attracting direct investment ranked first amongthe developing countries and second in the world, showing strong resilience.In the future, China's opening up will be further expanded, itsbusiness environment will be further improved, and the overall direct investment surplus is expected to continue. Second, with the continuous promotion of financial-market reform and opening up, foreign capital investments in the domestic securities market will maintain a growing trend. At present,the size of both China's bond market and China’s stock market ranks second in the world, but the proportion of foreign investment is still low, and there ismuch room for improvement in the future. At the same time, China's bond yield rate and stock valuations have a comparative advantage in the global market, which is more attractive to foreign investors. Third, the short-term fluctuations of cross-border funds under other investments have declined and stability has increased. According to development trends in recent years, the changes in other investment are more stable. Mainly due to the increasing two-way floating elasticity of the RMB exchange rate and the differentiated expectations of the exchange rate, market participants' pro-cyclical arbitrage activities have decreased. In the future, with the foreign- exchange market becoming more mature and the main body of the market trading more rationally, other investments will show small overall fluctuations.

Box 6

Investment Income in China's Balance of Payments Will Gradually Improve

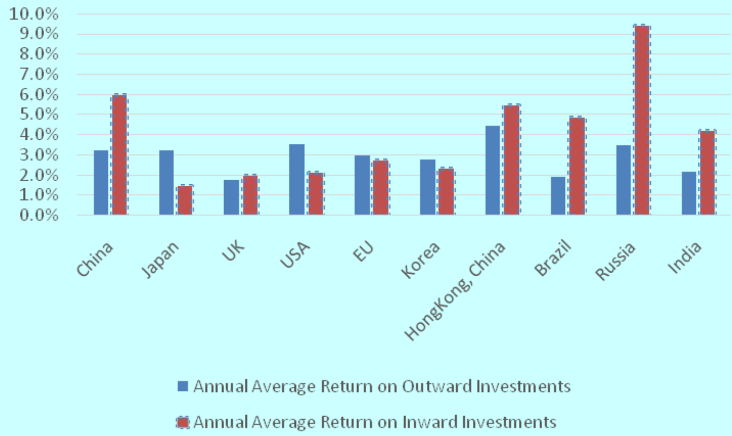
The International Investment Position statement and the balance of payments are related to each other through the financial account and the investment income account, from which we can analyze the investment income status in China's balance of payments. Statistics show that by end-December 2019, the stock of all kinds of foreign investment (including reserve assets and non-reserve assets) in China was USD 7.7 trillion, and the stock of all kinds of foreign investment in China was USD 5.6 trillion. During the same period, investment income revenue (profits, dividends, and interest) of all kinds of outward investment from China to the rest of world was USD 219.8 billion, and investment incomeexpenditures of all kinds of investments in China from the world was USD 257 billion. That is to say, in 2019 China's return on outward investments to the rest of the world was 2.9percent, and the return forinward investments in China from the rest of the world was 4.7percent.

In recent years, the return on outward investments and the return on inward investments have remained relatively stable. Since 2008 the return rate of China's outward investmentshas remained around 3percent. Against the backdrop of a decline in the global interest rate and the emergence of a negative interest rate in some countries and regions, China's outward investment income remained stable, indicating that relevant operations were relatively robust. Since 2008, in spite of fluctuations,inward-investment income has remained at a high level of around 5percent. For a long time, China's economic growth has been at a leading level in the world, with great economic growth potential and strong resilience. Foreign investors actively invested in the domestic market and shared the fruits of China's economic growth.

From the perspective of a global comparison, both the returns on outward

investments for China and the returns on foreign investments in China are at higher levels in the world. In a horizontal comparison, the economy with the highest average return on outward investmentsduring the past decade was Hong Kong SAR, with a rate of 4.4percent, followed by the United States and Russia with ratesof 3.5percent. The return on outward investments for China was higher than that of the European Union, the United Kingdom, Japan, South Korea, and other countries and regions. In the pastdecade, the economies providing high annual returns on inward investments were Russia, China, Hong Kong SAR, Brazil, and India. In general, the emerging markets provided higher returns on inward investments (see figure C6-1).

C6-1 Comparison of annual returns of cross-border investments for the major economies during the past decade



Note: The current year's outward investment rate of return = the current year's investment income / ((the stock of foreign assets at the end of the previous year + the stock of foreign investment at the end of the current year) / 2); the calculation of the current year's inward investment rate of return is the same. The data for Russia are from 2013 to 2018.

Data source: International Monetary Fund, State Administration of Foreign Exchange.

The deficit in China's investment income in the balance of payments is determined by the structure of China's foreign assets and liabilities. Over the years, as can be seen from the above comparison,the phenomenon whereby China's investment income has always registered a deficithas been mainly due to the high income of inward foreign investments, which is closely related to the structure of China's foreign assets and liabilities. China's inward direct investments account for more than one-half of its total liabilities, which is a long-term stable investment requiring a higher rate of return than other types of liabilities, whereasthe reserve assets accounted for more than 40percent of China's foreign assets, stressing more on liquidity with a lower rate of return than direct investments.

With the gradual optimization of the structure of China’s foreign assets and liabilities, the investment income deficit has gradually improved. In recent years, China's investment income deficit has generally narrowed, from USD 94.5 billion in 2013 to USD 37.2 billion in 2019. On the one hand, in recent years the proportion of outward investments in the form of direct investments has increased as a whole, increasing the income of outward investments; on the other hand, the expansion and opening-up of the domestic financial market has been gradually promoted, and securities investments in China have grown rapidly and their proportionhas increased, resulting in slower growth of total investment income expenditures in China. From the perspective of future trends, considering the current situation of the small proportion of foreign investment in China's financial market and the demand for domestic enterprises to go global, China's foreign asset–liability structure will continue to be optimized, and the investment-income deficit is expected to further narrow.

In 2020 China's foreign-exchange administration will take Xi Jinping's new socialist ideology with Chinese characteristics as the guide, thoroughly implement the spirit of the 19th National Congress of the Communist Party of China and the Second, Third, and Fourth Plenary Sessions of the 19th CPC Central Committee, conscientiously implement the deployment of the central economic work conference, do solid work in reform, development, and stability in the field of foreign exchange, continue to improve the level of trade and investment facilitation, and constantly improve the foreign-exchange management system and mechanism that are compatible with the requirements for the national governance system and for the modernization of governance capabilities.

On the one hand, we will deepen reform and opening-up in the field of foreign exchange, serve the country's new pattern of comprehensive opening-up, and serve the development of the real economy.We will conscientiously promote trade and investment liberalization, facilitation and high-quality development,implement the twelve facilitation measures adopted by the Executive Committee of the State Council, introduce more foreign-exchange facilitation policies and measures, support new trade formats, promote the construction of cross-border financial block chain service platforms, reduce the impact of the novel corona-virus pneumonia infection on trade and investment activities, and enhance the ability of foreign-exchange management to serve the real economy.

We will steadily and orderly open up capital projects, support financial-market connectivity and two-way opening up,establish and improve an open and competitive foreign-exchange market, enrich supply and demand inthe foreign-exchange market, improve infrastructure construction inthe foreign-exchange market, and meet the risk-hedging needs of market entities. We will further promote the reform of "deregulation services," and support the pilot free trade zone, the Hainan free trade port, Guangdong, the Hong Kong SAR,the Macao Bay Area, and other foreign-exchange management reforms. On the other hand, we should strengthen bottom-line thinking, guard against cross-border capital-flow risks, and safeguard national economic and financial security. The market will continue to play a decisive role in the formation of the exchange rate and we will keep the RMB exchange rate basically stable at a reasonable and balanced level. We will continue to improve the "macro prudential + micro regulatory"management framework in the foreign-exchange market, improve the monitoring, early warning, and response mechanism for macro-prudential management of cross-border capital flows, enrich the policy toolbox, maintain basic stability in the foreign-exchange market, and guard against systemic financial risks. We will conduct authenticity verifications, behavioraloversight, and micro-prudential supervision of the trading behavior of various entities in the foreign-exchange market, manage and maintain order in the foreign-exchange market, crack down on illegal activities in the field of foreign exchange, and maintain the consistency, stability, and predictability of law-enforcement standards across cycles. We will improve the operation and management of foreign-exchange reserves, improve the modernization of operations and management, and ensure the safety, liquidity, maintenance, and appreciation of foreign-exchange reserves.