Flash Economics

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If China can no longer sustain its economy through exports, it will experience real deflation.

China's domestic demand will remain weak as a result of the property crisis, weak investment and falling household wealth.

The only way for China to achieve sufficient growth is for its exports to grow strongly enough. But this growth is threatened by the imposition of tariffs on China's exports by the United States and Europe, and by the threat of tariffs on China's exports to the United States via other countries (Mexico, South-East Asia, India, etc.).

If China's exports weaken, the country will fall into true deflation, with weak growth and inflation.

Furthermore, the slowdown in China's exports to the United States and Europe, due to tariffs on Chinese products, will be the cause of additional inflation in the United States and Europe, with the result that inflation dynamics will be very different in China and in the OECD countries.

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Weak domestic demand in China

Domestic demand in China will remain weak as a result of :

- The property crisis (Charts 1A/B);

Chart 1A
China: New starts (Y/Y as %)

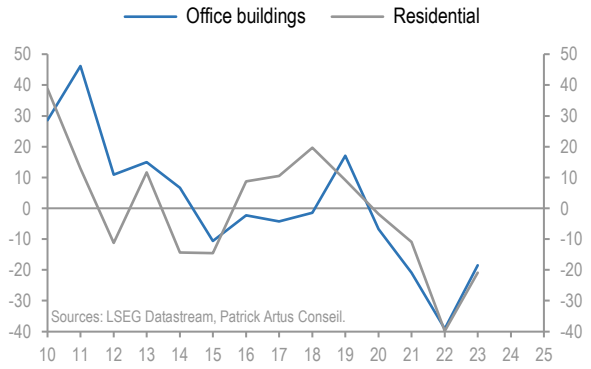
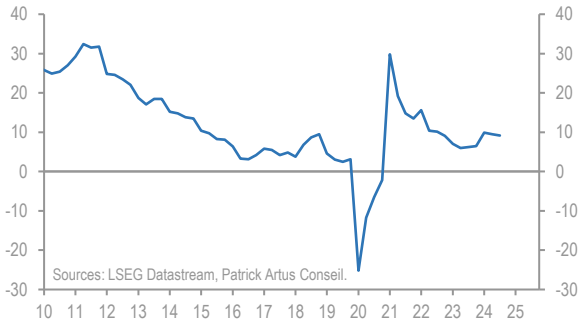


Chart 1B
China: House prices (Y/Y as %)



- Low levels of investment (Chart 2);

Chart 2
China: investment in the manufacturing industry
(Y/Y as %)



- The decline in household wealth (real estate, Charts 1A/B, equities, Chart 3).

Chart 3
China: Shanghaï Stock Exchange A Share
(01.01.2010 = 100)



For China to maintain sufficient growth, the only solution is therefore **for it to achieve fairly strong growth in its exports**, which have picked up since the second half of 2022 (**Charts 4A/B**).

Chart 4A
China: Exports of goods (in value terms, Y/Y as %)

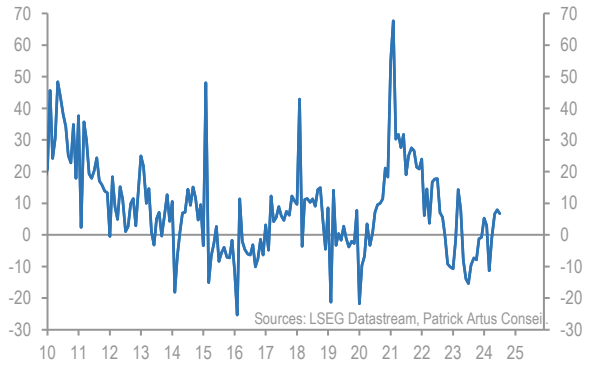
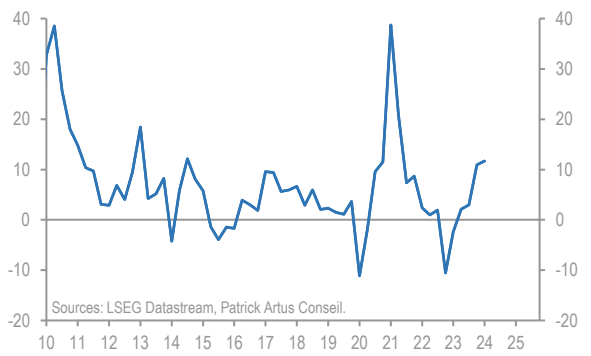


Chart 4B
China: Exports of goods (in volume terms, Y/Y as %)



But China's export growth is threatened by protectionism

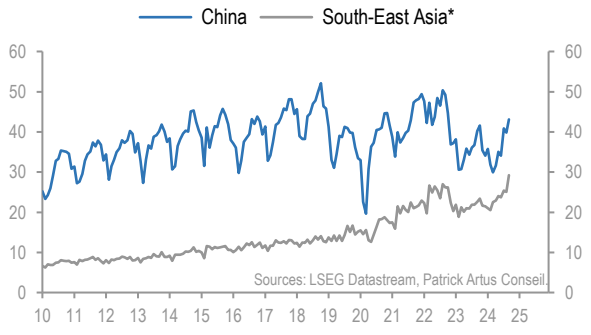
Tariffs imposed by the United States on Chinese products are 25% on steel, aluminium, electric batteries and harbour cranes, 25-50% on medical products, 50% on semi-conductors and solar cells, 100% on electric vehicles...

The European Union has imposed tariffs on steel, electric bicycles, tyres, kitchen utensils and chemical products, **in response to dumping by Chinese producers**. Tariffs of 8-35% have also been imposed on imports of Chinese electric cars.

Donald Trump has announced that he will impose tariffs on all US imports, with additional tariffs of 10-20% on imports from all countries, 60% on imports from China and 200% on cars imported into the US from Mexico.

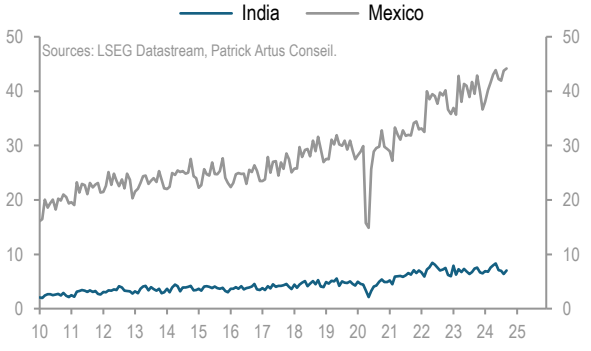
This would prevent China from circumventing the tariffs on Chinese products imported into the United States; observation of US imports from South-East Asian countries, India and Mexico shows that China has been channelling its exports to the United States through third countries (**Charts 5A/B**).

Chart 5A
United States : Imports from China and South-East Asia (monthly, USD bn)



(*) Indonesia, Malaysia, Philippines, Thailand, Vietnam

Chart 5B
United States : Imports from India and Mexico (monthly, USD bn)



Furthermore, it is likely that other countries would **retaliate** if the US imposed tariffs on their exports to the US.

Summary: Widespread protectionism would trigger a deflationary crisis in China

If protectionism becomes widespread, China will no longer be able to offset its weak domestic demand with dynamic exports. The result would be **deflation**, with weak growth and inflation **(Charts 6/7).**

Chart 6
China: Real GDP (Y/Y as %)

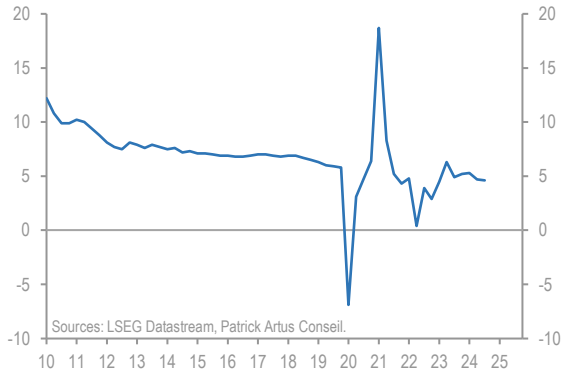
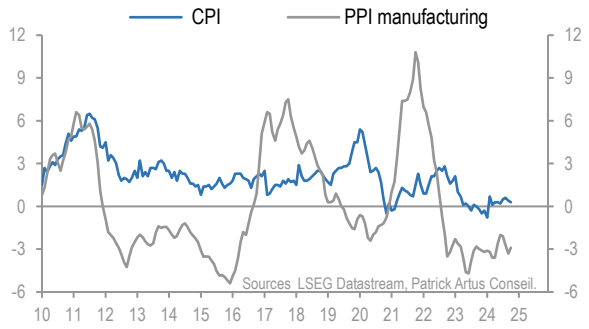


Chart 7
China: Consumer price index and producer price index for manufacturing (Y/Y as %)



The decline in China's exports to the United States and Europe would also create **a situation of stagflation in the United States and Europe**: weakening growth with the decline in purchasing power, and higher inflation due to the rise in the price of imported goods as a result of the impact of tariffs on import prices.

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