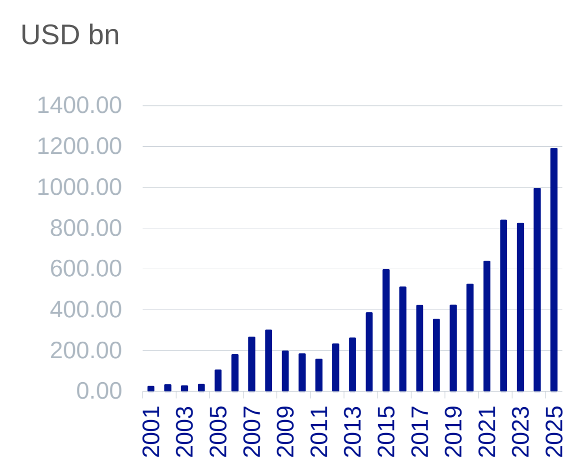
China | Understanding China's expanding trade surplus puzzle

Jinyue Dong, Le Xia

A rising puzzle of China's trade surplus is that during Trump's tariff war since February 2025, the trade surplus presumably should shrink as China's exports to the US that is China's most important trade partner should significantly decline amid rising tariffs. By contrast, China's trade surplus has been increasing over time in 2025, its balance increased from USD 273.16 billion in Q1 2025 to USD 315.86 billion in Q4 2025, the historical high regarding to the quarterly data. It is estimated that China's current account balance to GDP ratio will also reach 3.5%, another historical high since 2011. (Figure 1 and 2)

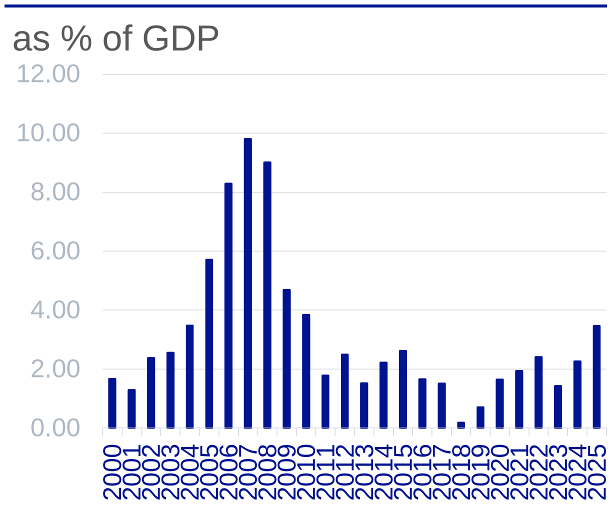
In history, China's trade balance has experienced three stages of development. In the first phase, from 2001 since China joined WTO to historical peak in 2007 before the Global Financial Crisis (GFC), China's trade balance increased dramatically from USD 24.11 billion to USD 263.94 billion. The current account balance to GDP ratio had been increasing over time from 1.3% in 2001 to 9.8% in 2007 amid China's involvement to global labor division and global supply chain. Here we use "current account to GDP ratio" instead of "trade surplus to GDP" as it is more convenient for international comparison and also because China's primary and secondary income combined has a ignorable size compared with trade balance under current account.

Figure 1. TRADE BALANCE HAS BEEN SIGNIFICANTLY HIGH IN 2025 AMID TARIFF WAR…



Source: BBVA Research and CEIC

Figure 2. …SO DID THE CURRENT ACCOUNT TO GDP RATIO



Source: BBVA Research and CEIC

In the second phase, from 2008 the outbreak of GFC to 2019 before Covid-19 pandemic, as advanced economies experienced unprecedented Global Financial Crisis, the external demand had been declining since the outbreak of GFC and China had also experienced economic transformation from external demand driven economy to infrastructure investment and real estate driven economy. During this time, China's trade surplus has experienced some ups-and-downs and its current account to GDP ratio had significantly declined from 9% in 2008 to 0.7% in 2019.

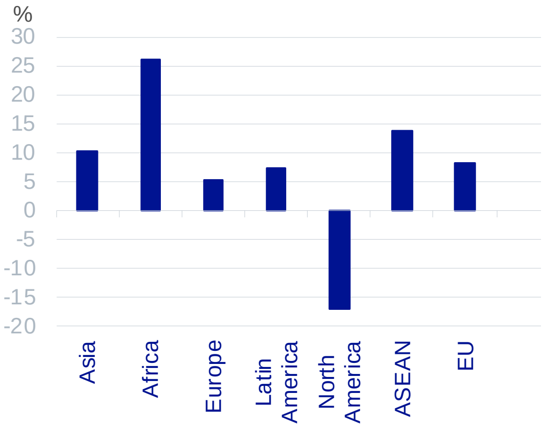
In the third period, from 2020 till now, China's trade surplus and current account have been increasing over time again, as China's "first-in, first'-out" strategy during the pandemic time made China's business cycle and policy cycle unsynchronized with the advance economies in the world. (Figure 1 and 2)

In this report, we are trying to explain the puzzle that why China' trade surplus balance has kept expanding in 2025 during the trade war with the US. It is equivalent to analyze why the exports growth is faster than the imports growth, in other words, why China still had strong exports but at the same time weak imports during the trade war time.

1. Why China still had strong exports in 2025 trade war era?

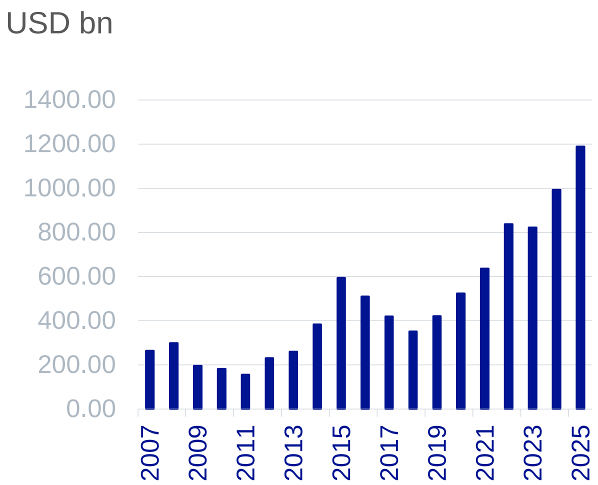
First, export country's substitution effect plays an important role to explain China's rising exports growth. Export country's substitution effect here particularly means that the growth of Chinese exports to non-US regions were much stronger than the exports to the US during the tariff time, which not only could offset the dipping exports to the US but also increase the total exports growth figure. (Figure 3)

Figure 3. CHINA'S EXPORTS TO THE NON-US REGIONS WERE MUCH STRONGER THAN THE EXPORTS TO THE US



Source: BBVA Research and CEIC

Figure 4. FRONT-LOADING EVEN BEFORE TRUMP OFFICIALLY ANNOUNCED THE TARRIF ON CHINA



Source: BBVA Research and CEIC

Figure 3 plots the 2025 January to December year-on-year exports growth rates from China to different regions. It is obvious that although China's exports to the US declined to -17% in 2025 due to the Trump's tariff war, Chinese exports to all the non-US regions such as Africa (26%), EU (8.2%), Latin America (7.2%), Asia (10.3%) etc. are significantly on the rise.

This type of country substitution could be contributed by Chinese authorities' "One-Belt, One-Road" initiative which has built a good economic and political relationship with Africa, Latin America, Asia and also European countries. In addition, China's comparative good relationship with the Europe during the US trade war, together with the deepening of supply chain vertical specialization within Asian economies (particularly China-ASEAN) could also explain this country substitution effect.

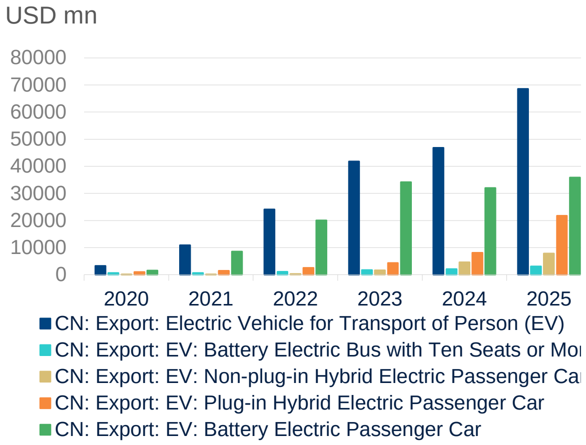
Second, front-loading still played a role to support China's exports to the US during the trade war period, although we observed the whole-year exports to the US declined. At end-2024, even before his inauguration, the US importers were starting to increase their orders from China to accumulate their inventory after Trump threatened to increase tariffs for Chinese imports during Trump's election campaign. Figure 4 shows that from October 2024 to March 2025 (except for Feb 2025 only), China's exports to the US had maintained mostly double-digit growth. That means, front-loading behavior of the US importers helped to support Chinese exports to the US during the tariff war period, without that, China's exports to the US could be even lower. (Figure 4)

Third, China's overcapacity issue particularly in the green economy sector pushed these products to be exported to foreign countries as domestic market cannot consume all of them. Due to the national strategy to support high-end manufacturing and green economy related sectors, China's green economy sector has experienced an unprecedented development in the past several years.

However, the strong policy support at the same time also induced severer overcapacity in the "New Trio" sector, including electric vehicles, lithium batteries, and solar cells. The domestic market cannot absorb these overcapacity products; thus, they have to export to foreign countries, leading to a significantly higher growth rate of green products exports compared with the aggregate export growth. (Figure 5 and 6)

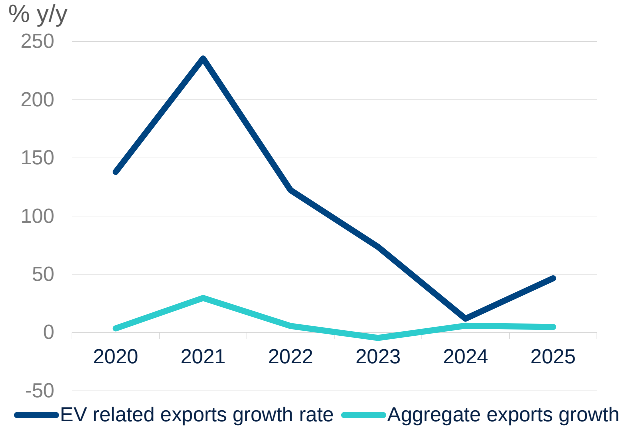
The authorities currently are pushing forward "Anti-involution" campaign to address the supply-demand mismatch issue which refers to government-backed efforts to combat "involution" that describes excessive, unproductive competition among firms leading to diminishing returns, worker exhaustion, price wars and accelerating deflation. However, there are still challenges ahead. Compared with China's supply-side reform back to 2015-2017 in which China deleveraged the state-owned overcapacity sectors, most of this round of "anti-involution" are in the private sector. Another big challenge is the possibility of job losses. (Figure 7 and 8)

Figure 5. DUE TO OVERCAPACITY, EV AND RELATED BATTERY ELECTRIC CAR EXPORTS HAVE REACHED HISTORICAL HIGH IN 2025



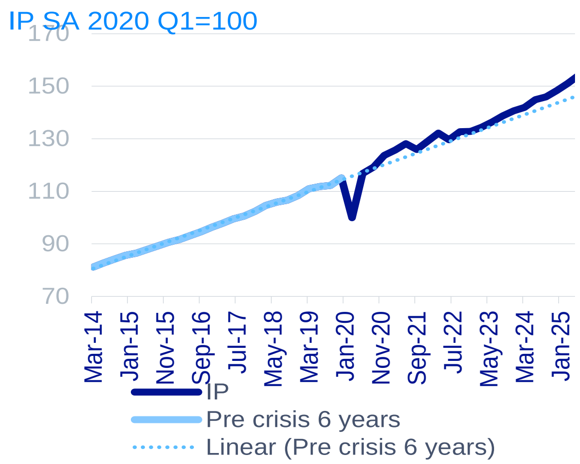
Source: BBVA Research and CEIC

Figure 6. EV RELATED GROWTH RATE HAS BEEN SIGNIFICANTLY HIGHER THAN THAT OF THE AGGREGATE EXPORT GROWTH



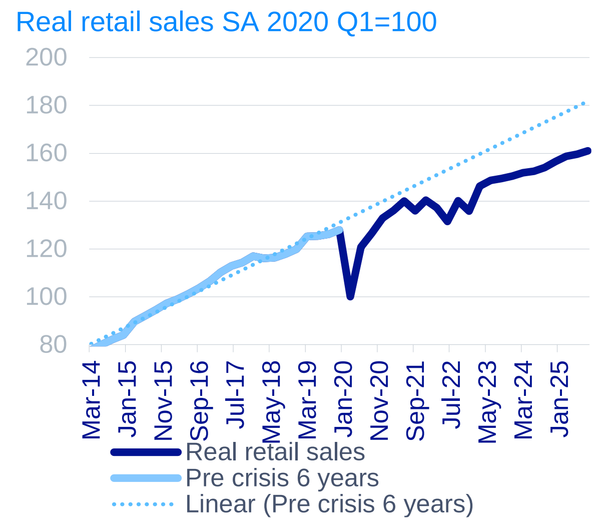
Source: BBVA Research and CEIC

Figure 7. INDUSTRIAL PRODUCTION TREND IS HIGHER THAN PRE-PANDEMIC TREND…



Source: BBVA Research and CEIC

Figure 8. …BUT RETAIL SALES TREND IS SIGNIFICANTLY LOWER THAN PRE-PANDEMIC



Source: BBVA Research and CEIC

2. Why China had weak imports in 2025?

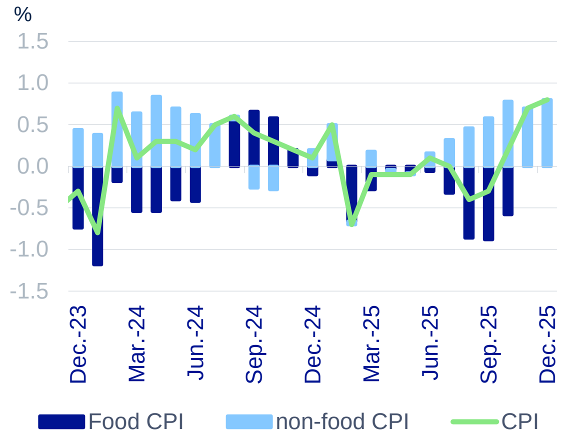
First, weak domestic demand and sluggish market sentiments are the main reason for weak imports growth in 2025. Chinese economy has slowed down its high growth momentum after the Covid-19 pandemic, dragged mainly by domestic headwinds including overcapacity, weak consumption sentiments and housing market crash. Deflation environment has also persisted for several years, which together with other risk factors, further deteriorated the market sentiments. (Figure 9-11)

Second, imports substitution effect also plays an important role to explain weak imports. During the tariff war period, as the US restricted China's high-tech imports from the

US and other US allies, the import growth regarding to this part has been significantly slowed. Moreover, due to China's policy to prioritize high-tech development and high-end manufacturing sector in a bid for sustaining national security, some intermediate goods such as chips that were previously highly depending on imports now substituted by domestic production.

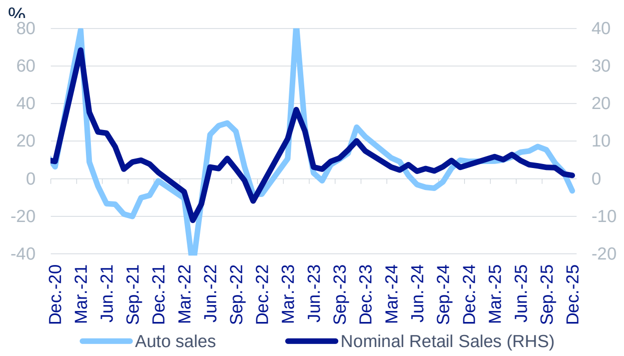
Figure 12 shows that among the categories of imports that suffered the negative growth in 2025, they are actually from industries not only in technology sector, but also from medical sector, automobile, and natural sources such as natural gas, as well as some traditional sector such as textile. (Figure 12)

Figure 9. DEFLATION ENVIRONMENT PERSISTS



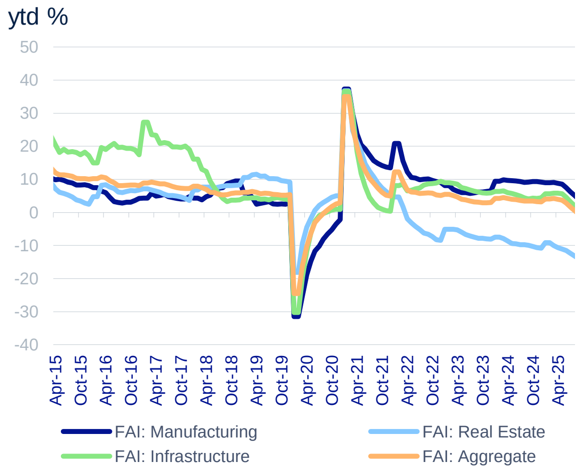
Source: BBVA Research and CEIC

Figure 10. RETAIL SALES DIPPED TO THE HISTORICAL LOW



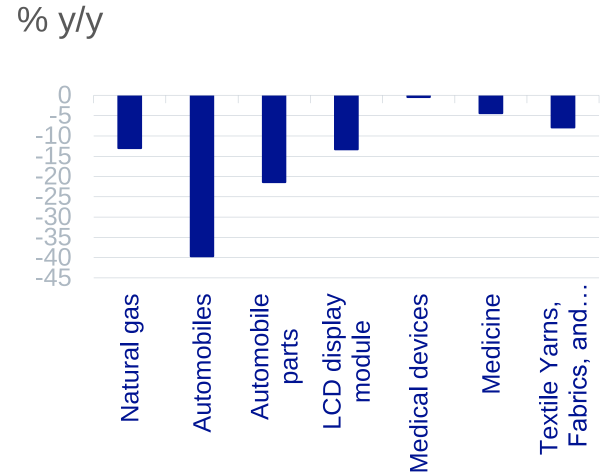
Source: BBVA Research and CEIC

Figure 11. FIXED ASSET INVESTMENT HAS ALSO BEEN DECLINING TO HISTORICAL LOW



Source: BBVA Research and CEIC

Figure 12. IMPORTS SUBSTITUTION EFFECT LOWERED THE IMPORTS GROWTH



Source: BBVA Research and CEIC

DISCLAIMER