Summary

There have been many positive changes since March. The latest economic data confirmed that Chinese economy has entered a stabilization zone despite a weak start in January. The broad-based recovery was mainly attributable to three factors in our view including favourable global environment, stable RMB and supportive domestic monetary and fiscal policies. Global market has reacted positively to China's strong March data. Shanghai index also managed to recoup 3000 level, ending the week up by 3.15%. China's bond market was under pressure again hit by reduced easing expectation following the improving economic data. China's policy bank bonds suffered the biggest loss in 11 months. The concern about the correction of bond market also led to tighter liquidity, but was largely offset by the liquidity injection via MLF. Nevertheless, given PBoC offered a lower rate for MLF when checking demand in March, the fact that PBoC kept rate unchanged from Feb level raised concern about the less accommodative tone from PBoC. We think it might be still too early to call for the bottom out of Chinese economy as the pace of government led recovery will depend on two factors including global situation and private sector participation. The risk for the economy to slow down again cannot be ruled out should Fed restart its tightening cycle. But in the near term, the positive sentiment is likely to last for a while. On RMB, despite the stability against the dollar, RMB's quiet depreciation against its basket currency did raise concern about transparency of RMB policy. Despite improving fundamentals, the image of depreciation bias of its basket currency may still keep the USDCNY spot in check. We think the upside risk for USDCNY is still live.

Key Events and market talk	
Facts and Market talks	**OCBC Opinions**
▪ Caixin reported that given the slow progress of reducing capacity in the steel industry two months after the State Council laid out the 5-year plan to reduce crude steel production capacity by 100 to 150 million, Chinese government may impose an universal target for each province to reduce their production by 13.3%. ▪ Meanwhile, the Ministry of Land and Resources said that it will not approve the land used for steel and coal projects to support China's bid for reducing excessive capacity in those industries.	▪ China's excessive capacity in the steel industry has been the global issue. Compared with the topic of Yuan valuation, the developed economies have raised more concerns about China's steel export as they believe China's steel industry has been heavily subsidized to support the stability in the local job market. ▪ Britain's Foreign Minister urged China to accelerate its efforts to reduce over-capacity in the steel industry during his meeting with China's Foreign Minister in early April after India's Tata Steel put its UK operation for sale, threatening 15000 jobs in the UK. Meanwhile, China's Steel industry has also been the focus in the US presidential campaign. ▪ We think it is also in China's interest to reduce excessive capacity in the Steel Industry, however, it may take some time for China to find a balance between job replacement and achieving de-capacity goal.
▪ China's central bank announced new measures to allow foreign central banks investing in China's onshore interbank bond market to freely repatriate their money without regulatory approval.	▪ The move is another step for China to open up its bond market as well as capital account liberalization. It will make China's interbank bond market more appealing to foreign investors, which may attract more flows to China.

Key Economic News	
Facts	**OCBC Opinions**
▪ **Trade data:** China's export in dollar term grew by 11.5% yoy, first positive growth in nine months. The stronger than expected export growth in March was in line with improving manufacturing sentiment, confirming the stabilization of the economy. ▪ Import in dollar term fell by 7.6%, but better than expectation. The contraction of import value was still the result of weak commodity prices. However, imports by volume continued to pick up, signalling the improving domestic demand. ▪ Trade surplus in March was at US$29.86 billion.	▪ The stronger than expected trade data in March was mainly attributable to three factors in our view. First, sentiment in the global market recovered following further easing measures from ECB and BOJ and the delay of Fed tightening. Second, despite RMB stabilized against the dollar, RMB continued to weaken against the basket currency. Third, the diminishing excessive bearish sentiment against the RMB helped. Nevertheless, the foundation of the recovery is not solid yet and any hawkish signal from the Fed may reverse the optimism. ▪ Import from Hong Kong surged by 116%, raising question on the possible capital outflows.
▪ **Inflation data:** CPI grew by 2.3% in March, unchanged from Feb reading, but lower than market expectation. On sequential basis, CPI fell by 0.4% mom, mainly driven by falling food prices. ▪ PPI continued to fall by 4.3% in March as the result of excessive capacity issue. However, on sequential basis, PPI increased by 0.5%, first positive reading since January 2014 on the back of recovery in commodity prices.	▪ Although the actual reading on food prices raised the debate in the market due to disconnection between real number and feeling about the rise of pork prices, the lower than expected March CPI data is likely to cap the reflation talk for the moment. Given food prices are expected to fall further, we expect the CPI in 2Q to stay sub 2.5% level. Concern about the stagflation is likely to diminish in the near term. ▪ The first positive month-on-month reading of PPI in 26 month is encouraging, however, the gap on negative year-on-year reading is unlikely to be closed any time soon as de-capacity is still a year-long campaign.
▪ **Overseas direct investment:** China's non-financial ODI jumped by 55.4% in 1Q to US$40.3 billion according to Ministry of Commerce. Overseas acquisitions by Chinese companies were at US$16.56 billion covering 15 industries and 36 countries and regions.	▪ The rapid growth of China's overseas direct investment was partially driven by China's push of its one belt one road initiative. Despite rising concerns about China's tightening capital control in 1Q to stabilize its currency, the strong ODI data shows that overseas direct investment was not directly affected by China's increasing surveillance on capital flows. ▪ Hong Kong remained the top destination for China's ODI, accounting for 51.6%. Investment in ASEAN rose by 44% to US$2.29 billion while investment in US doubled to US$5.24 billion.
▪ **Economic Activity:** China's growth decelerated to 6.7% in 1Q, but in line with market expectation. ▪ Retail sales grew by 10.5% in March, beating market expectation of 10.4%. ▪ Fixed asset investment reaccelerated to 10.7% in 1Q, up from 15-year low of 10% in 2015. ▪ Industrial production rebounded to 6.8% beating market expectation of 5.9%. ▪ Aggregate social financing hit a record high of CNY6.52 trillion in 1Q.	▪ The stabilization of the economy was mainly attributable to three factors in our view including favourable global environment, stable RMB and supportive domestic monetary and fiscal policies. Externally, global sentiment has improved significantly after G20 meeting in Shanghai in late Feb following more easing measures from ECB and BOJ as well as dovish comments from Fed Chairwoman Yellen. The recovery of the global sentiment also lent the support to sentiment in China's financial market, which in turn help correct excessive bearish sentiment. ▪ In addition to improving global sentiment, a more stable and predictable RMB also helped calm down the market. The panic about the disorderly RMB depreciation has diminished significantly after PBoC guided market to trade RMB with reference to basket currency since January. A more predictable currency policy is important for exporters and importers, which partially contributed to the significant recovery of China's trade data in March. ▪ Domestically, Chinese economy also benefited from more expansionary monetary policy and proactive fiscal policy.

	China's aggregate social financing hit an all-time high of CNY6.53 trillion in 1Q, signalling expansionary credit policy despite China kept its benchmark interest rate unchanged. Meanwhile, infrastructure investment reaccelerated to 19.6% in 1Q from 15% in the first two months on the back of fiscal support. ▪ Looking ahead, we expect China's monetary and fiscal policies to remain supportive, in particular, after taking local government debt swap program and upcoming debt for equity swap program into account. However, having said that, we think it might be still too early to call for the bottom out of Chinese economy as the pace of government led recovery will depend on two factors including global situation and private sector participation. The risk for the economy to slow down again cannot be ruled out should Fed restart its tightening cycle. Meanwhile, the deceleration of private investment to a record low of 5.7% also suggests the caution of private sectors despite increase of government spending. Nevertheless, despite challenges remain, our call for China to grow about 6.7% this year remains unchanged.
▪ IMF expected Hong Kong to slow to 2.2% this year, slightly better than 1% - 2% estimated by the HK government, in its latest World Economic Report.	▪ China's economy showed signs of recovery. This is also the reason behind the IMF's upward revision to China's GDP growth from 6.3% to 6.5%, albeit a downward revision to the global growth. Should the recovery of China's manufacturing sector and exports growth turn out to be sustainable throughout this year, HK's trade sector could also regain its footings in 2016. In all, we see a 2.1% annual growth of HK's economy in 2016, as improvement in the trade sector may not be significant enough to offset the prolonged weakness in the retail sector.
▪ Approvals for new residential mortgage loans (RMLs) in Macau slumped by 57.1% yoy (-29.5 mom) to MOP2.26 billion in February.	▪ Clearly, the sentiment remains subdued as neither the gaming sector nor the tourism activities are showing strong recovery. In the latest world economic outlook report, IMF firstly published Macau's GDP forecast, estimating the growth to contract by 7.2% in 2016. Given dimmer economic outlook, slower salary growth is expected across all sectors, side-lining the prospective home buyers farther from the property market. As a result, subdued demand drove the private housing transaction down by 6.5% yoy to 304 units in February, hitting a seven-year low. On the supply front, the completion of residential units in 2015 jumped to the highest since 1999. Adding that thousands of public housing units will be completed this year, the housing prices are set to head down further after dipping 6.1% in February from end of last year. We expect the housing prices to drop 10% – 15% on yearly basis by end of this year.

RMB	
Facts	**OCBC Opinions**
▪ Pretty boring week for the USDCNY spot market as the pair was traded in a narrow range of 6.46-6.49. However, RMB index quietly depreciated further to 97.38 from 97.64 on 8 Apr. RMB index has depreciated by slightly more than 3.5% year to date.	▪ In the near term, 97 is likely to be the floor for RMB index. Any break of 97 is likely to raise concern about whether Chinese leader's pledge of stability against the basket currency is convincing enough. ▪ Despite improving fundamentals, the image of depreciation bias of its basket currency may still keep the USDCNY spot in

	check. We think the upside risk for USDCNY is still live.

Liquidity	
Facts	**OCBC Opinions**
▪ PBoC injected CNY285.5 billion liquidity via 3 month and 6 month medium term lending facility (MLF). The interest rate remained unchanged at 2.75% for 3 month and 2.85% for 6 month.	▪ The liquidity injection via MLF helped to bring down the interbank funding cost slightly after 7 day repo fixing rose to 2.5% last Wednesday. However, given PBoC offered a lower rate for MLF when checking demand in March, the fact that PBoC kept rate unchanged raised concern about the less accommodative tone from PBoC.

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