Summary

Over the weekend, I asked a few friends in Singapore that whether they think it is good news or bad news if central bank decides to offer longer tenor liquidity support to the banking system. Most of them thought it is good news. Nevertheless, it is not really the case in China. The volatility in China's bond market spiked following the news that PBoC relaunched 14-day reverse repo for the first time since Feb 2016, which suggested that the central bank still preferred open market operation to maintain liquidity stable to interest rate and reserve requirement ratio cut. However, market also read the shift of liquidity support to longer tenor as the warning signal to curb leverage in bond market as funding cost from 14-day reverse repo is higher that from 7-day and overnight reverse repo, which may increase costs for leverage. China's bonds fell with the yields went up as knee jerk reaction to the news. However, the retracement also created opportunity for investors to buy bonds on dip as the overall trend for yields to go lower remains intact.

There are two more developing news about China's bond market last week. First, the full CNY6.8 billion payment made by SOE China Railway Materials removed the event risk on SOE bond default. It seems that the implicit guarantee remains, in particular for large SOEs. Second, Poland became the first European sovereign name to issue the "panda" bond in China's onshore interbank bond market. RMB fell against the dollar for the second week with the USDCNY touched the high of 6.68 in both onshore and offshore market ahead of Yellen's speech in Jackson Hole. The jittery ahead of Friday's Jackson Hole conference pushed the EM currency lower against the dollar. RMB index remained stable, hovering around 94 level. The retreat of JPY following the dovish comments from Kuroda may create fresh pressure on RMB. The fixing is expected to test 6.70 again this week. For this week, the focus will clearly shift to G20 meeting in Hangzhou as well as China's August PMI data.

Key Events and Market Talk	
Facts	**OCBC Opinions**
▪ PBoC re-launched 14-day reverse repo for the first time since Feb. The auction yield remained intact at 2.4%.	▪ The re-launch showed that PBoC still aims to maintain liquidity stable in the money market on the aggregate level via open market operation. This reduced the probability of interest rate and reserve requirement ratio cut in the near term. ▪ However, the shift of liquidity supply to longer tenor signalled that PBoC may want to curb leverage in bond market as funding cost from 14-day reverse repo is higher that from 7-day and overnight reverse repo, which may increase costs for leverage. ▪ The recent rally in bond fuelled by leverage on the back of stable short end funding raise the concerns about potential asset bubble risk in China's bond market. ▪ China's bonds fell with the yields went up as knee jerk reaction to the news. The bond prices may face pressure in the near term due to reduced easing expectation as well as PBoC's warning shot to leverage. However, the retracement may also create opportunity for investors to buy bonds on dip as the overall trend for yields to go lower remains intact.
▪ China's State-owned Asset Supervision and Administration Commission (SASAC) said China Railway Materials Co. has made full payment on CNY6.8 billion due this year in time to avoid default risk.	▪ The SASAC said it will analyse the SOE bond one by one and actively deal with risks to prevent bond default. In particular, the commission will put bonds maturing over the next three months in scrutiny spotlight. ▪ This move may reinforce the concept of implicit guarantee for SOE bonds.
▪ Poland became the first European sovereign name to issue the "panda" bond in China's onshore interbank bond market.	▪ The 3-year bond was priced at 3.4% and was two times oversubscribed by investors. The move marks another milestone to introduce the world's third largest bond market to the global issuers and investors. ▪ However, most of panda bond issued were swapped to USD or Euro due to enjoy cost saving due to limited usage of RMB in the global stage. This suggests that it will still take some time for RMB to be true international currency.

▪ China's equity market fell last Friday, led by property developers on market speculation that Shanghai may introduce more tightening measures to cool down its red-hot property market.	▪ The discussion includes tightening land purchase financing, higher downpayment ratio as well as delaying the divorced couple to be qualified for home purchase due to increasing numbers of fake divorce.
▪ S&P affirms Hong Kong's AAA sovereign rating but keeps the city's negative sovereign credit outlook intact.	▪ S&P states that sizable and stable fiscal reserve of Hong Kong, the strong external creditor position (stems from sustained current account surpluses) and above-average economic growth prospects warrant the city an "AAA" rating. The rating agency also said that the negative outlook on Hong Kong's long-term rating is aligned with that on China's. ▪ In 2Q, Hong Kong's economy picked up notably due to rebound in trading activities. Though the growth will still face headwinds, including China's anti-corruption campaign, tepid global demand and subdued local consumer sentiment, it is unlikely to decelerate significantly. The reasons include: 1) After the U.K. voted to exit the EU, global easing and investors' searching for high yields have led to robust gains in capital inflow to Hong Kong. This underpins the city's crucial financial sector's growth; 2) The expected slow rate hike pace of the Fed allows Hong Kong's crucial property market to see a rebound in the near term; 3) Should the capital inflow persist and the Fed remain dovish stance in terms of tightening, higher demand for HKD will warrant the currency's strength and lower the de-peg risk; 4) China shows signs of stabilization in growth, indicating that Hong Kong's close interconnection with China may not pose further downward risks to its economy. All in all, we believe that HK's economic growth will bottom out this year with growth of 1.1% yoy.

Key Economic News	
Facts	**OCBC Opinions**
▪ HK Export growth in value terms fell for the 15th consecutive month, printing -5.1% yoy in July (vs June's -1.0% yoy).	▪ Decline in export value widened somewhat in July after having narrowed in the preceding months, signaling an unsteady global demand condition. Region-wise, exports to Asia as a whole dropped by 5.4% yoy, led by exports to China which dipped 6.4% yoy. On the flipside, China reported its import growth from Hong Kong to have accelerated to 122.7% yoy in July (vs +70.8% in June). The ongoing discrepancy between two data shows that onshore investors are continuing to leverage on trade activities as the channel to bypass the capital control. ▪ Elsewhere, exports to other main trading partners showed some weakness, in particular UK (-19.4%), Germany (- 5.8%) and the US (-1.7%). This may reflect a looming negative effect following Brexit. Several surveys from UK institutions reported that UK enterprises began to curtail their business investment and that demand from UK shrank amid dent household sentiment. It looks to us that the soft external demand could continue to pose downward risk to HK exports. In the coming months, we expect trade growth to remain in contraction territory given (1) sluggish external demand amid the uncertainty in the aftermath of Brexit, (2) US interest rate normalization as well as (3) heightened geopolitical tensions in certain regions.

▪ The number of visitor arrivals in Macau further ticked up by 5.5% yoy in July, due to one year of consecutive increases in overnight visitors (+12.4% yoy).	▪ The share of overnight visitors rose slightly from 52% to 52.1%, refreshing its record high and underpinning the rebound in tourism activities. Specifically, visitors from five main sources (including Mainland China) all registered annual growth, the first time since last December. A raft of rosy data reinforce that the city's tourism activities keep gaining momentum amid latest hotel openings, the effect of summer holiday and the signs of stabilization in China's growth. The increased visitor arrivals also started to loosen their purse strings, narrowing the fall in retail sales value to -8.7% yoy in 2Q. On a more positive note, two mega hotel projects to be opened in 3Q are expected to help sustain the gains in overnight visitors and leisure gamblers. Adding a fresh wave of new hotels and casinos to be completed in coming 1-2 years, the city's tourism and gaming sectors are embracing for a gradual recovery. Moreover, it remains a concern that the marginal benefit of the new projects will fade in a longer term due to the absence of diversified entertainment facilities and natural wonders. Also, given a wide range of uncertainties lingering around the globe, Macau's economy which relies on tourism and gaming sectors will appear to be vulnerable to external shocks. Elsewhere, this week's Macau 2Q GDP will be in spotlight.

RMB	
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▪ RMB fell against the dollar for the second week with the USDCNY touched the high of 6.68 in both onshore and offshore market ahead of Yellen's speech in Jackson Hole. ▪ Nevertheless, RMB index recovered slightly to hover around 94 level.	▪ The falling expectation on imminent interest rate and reserve requirement ratio cut following the relaunch of 14-day reverse repo failed to support RMB. The jittery ahead of Friday's Jackson Hole conference pushed the EM currency lower against the dollar. ▪ The retreat of JPY following the dovish comments from Kuroda may create fresh pressure on RMB. The fixing is expected to test 6.70 again this week.

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