Highlights:

China's growth data continued to shine with the latest PMI accelerating to 51.6 in Feb. This may add optimism to 1Q GDP, which is expected to accelerate to 7%. However, the support from restocking demand may start to phase out. As such, we expect the growth may gradually decelerate from the second quarter onwards.

China's Premier Li Keqiang delivered a reform-minded 2017 Government Work Report on Sunday. China officially lowered its growth target to around 6.5% though keeping the option to try higher from previous year's 6.5-7% range. The lower growth target despite improving economic data in the past few months paved the way for reform and containing financial risk. Given de-leverage and containing financial risk are likely to be the key focuses this year, we think monetary policy is likely to remain tight bias this year. However, we don't expect China to move towards full-scale tightening such as hike of benchmark deposit and lending rate due to contained inflation risk. This was echoed by PBoC deputy Governor Yi Gang, who expects CPI to stay within 2.5-3% range in 2017.

One of the most notable changes in this year's work report is on RMB. The sentence about "continue to improve market based currency mechanism and maintain RMB relatively stable at a reasonable level" was removed from the part of financial reform. The shift of policy tone signals to us that currency reform is likely to take a pause this year. China is unlikely to aggressively pursue more currency reform as well as pushing RMB internationalization. Overall we think RMB is likely to play a role of supporting actor this year while the leading actors will be de-leverage. This reinforced our view that RMB's volatility this year is unlikely to be self-engineered and it may depend on the dollar movement.

In Hong Kong, property prices continued to go higher. We will discuss three possible reasons why the recent housing measures failed to cool down the property market. For this week, market will continue to focus on China's National People's Congress as well as China's economic data.

Key Events and Market Talk	
Facts	**OCBC Opinions**
▪ Premier Li Keqiang delivered his 2017 Government Work Report. This is a reform minded report with higher tolerance for slower growth.	▪ Three highlights from the Work Report. ▪ **First,** China lowered its 2017 growth target as expected to "around 6.5% but trying higher if possible" from previously "6.5% to 7%". The lower growth target despite improving economic data in the past few months paved the way for reform and containing financial risk. ▪ Clearly de-excessive capacity, de-inventory and de-leverage will be the key focus for China in 2017. Premier Li kicked off his nine key tasks for 2017 in his speech with setting the quantitative target for cutting excessive capacity. China plans to cut 150 million metric tons of coal and 50 million metric tons of steel. In addition, he also suggests tier 3 and 4 cities taking different approaches to lower their excessive housing inventories. Among all, the most important thing will be to lower corporate leverage. ▪ **Second,** policy will be more conservative with policy support shifted from monetary policy to fiscal policy. China will lower its M2 growth and aggregate social financing growth targets to 12%. The deceleration of aggregate social financing growth from actual 12.8% in 2016 to targeted 12% in 2017 signals less credit support. This supports our view that China's growth is expected to slow again in the second half. ▪ To recap, the stabilization of China's growth in 2016 was mainly supported by three factors including property market, easing monetary policy and proactive fiscal policy. Without the support from property market and monetary policy, the fiscal policy alone is unlikely to stop the growth from slowing down again. We expect China's growth to accelerate to 7% in the first quarter on the back of base effect and supportive credit data but may gradually slow down from 2Q onwards.

	▪ **Third,** on currency, there was notable shift in language about RMB. The word RMB was only mentioned three times this year as compared to 6 times each in the past two years' reports. The sentence about "continue to improve market based currency mechanism and maintain RMB relatively stable at a reasonable level" was removed from financial reform. Instead, Premier Li said China will continue its direction of market based reform and maintain RMB's stable position in global monetary system. This shift of policy tone signals to us that China may feel they have achieved the target of currency reform, which is likely to take a pause this year. China is unlikely to aggressively pursue more currency reform as well as pushing RMB internationalization. Overall we think RMB is likely to play a role of supporting actor in this year while the leading actors will be de-leverage. This reinforced our view that RMB's volatility this year is unlikely to be self-engineered and it may depend on the dollar movement.
▪ PBoC deputy Governor Yi Gang expected CPI to stay within 2-3% in 2017. As such, monetary policy will remain prudent. ▪ In addition, he also said China will not allow currency depreciation to support export.	▪ Yi's comments basically echoed the tone from PBoC's latest 4Q monetary policy report. The outlook of China's monetary policy will depend on two factors this year including inflation outlook and asset bubbles. Given inflation is expected to stay below 3% in 2017, we think the room for full-scale tightening such as hike of benchmark deposit and lending rate is limited.

Key Economic News

Facts	OCBC Opinions
▪ China's official PMI rose to 51.6 in February, up from 51.3 in January. ▪ Both new orders and new export orders accelerated to 53 and 50.8 from 52.8 and 50.3 respectively, implying improving demand.	▪ China's PMI in the first two months of 2017 painted a rosy picture. The improving demand thanks to strong credit growth is likely to add optimism into the 1Q economic growth. We expect 1Q GDP to accelerate to about 7%. ▪ However, the narrowing gap between new orders and finished goods inventory to 5.4, down from the peak of 8.8 in December 2016, shows the restock is underway. The support from restocking demand may start to phase out. As such, we expect the growth may gradually decelerate from the second quarter onwards. ▪ On price level, the input price index remained elevated at 64.2 in Feb, little change from 64.5 in January. This may imply a strong PPI in Feb. We expect the PPI to accelerate further to 8.1% in Feb on the back of base effect. Nevertheless, we think PPI may peak in Feb and fall gradually from March onwards.
▪ Housing prices continued to rise in Hong Kong with Centa-City Leading Index (CCL) refreshing its new high at 147.74 for the week ended 19 February.	▪ Last year's housing cooling measures appeared to have merely tamed housing transactions, but failed to drag down housing prices due to three main reasons. First, home supply in the secondary market reduced notably as homeowners are reluctant to sell their property due to higher cost of second home purchases following last year's cooling measures. Second, lower mortgage rates and sweeteners offered by property developers have lured more homebuyers to the primary market. Third, Hong Kong dollar's peg to USD and China's housing cooling measures have prompted Mainland corporates to aggressively buy lands in HK, in turn driving up the housing prices in the neighborhood. Looking ahead, tight secondary housing supply and huge demand could alleviate the impact of increasing new home supply and higher interest rates. This indicates that housing prices are unlikely to witness

	notable correction this year.
▪ Exports and imports retreated 1.2% yoy and 2.7% yoy respectively in January. As a result, trade deficit narrowed to HKD12.3 billion.	▪ Specifically, overseas shipments to major Asian trading partners, including Mainland China, Vietnam, Philippines and Japan, all dropped. In comparison, exports to western countries like Germany and the USA reversed the downward trend. On the other hand, subdued domestic demand outweighed higher commodity prices in dragging down imports. However, the effect of the Lunar New Year Holiday might have distorted the trade figures. Therefore, we are waiting for February's trade data to have a clear picture of HK's trade sector. Looking ahead, on the back of its fiscal stimulus, any improvement in the US economy will be favorable to HK's trade sector. On the contrary, the rise of protectionism and a stronger HKD may have a negative effect on the sector. Elsewhere, the decrease in HK's exports of gold to Mainland China (-50.7% mom in January) indicates that China's capital controls have been taking effect.
▪ As HK banks continued to cut mortgage rates, new residential mortgage loans approved jumped by 81.4% yoy to HKD28.2 billion in January.	▪ However, higher interest rates ahead may limit the growth in residential mortgage loans. On the contrary, the increasing dominance of primary housing market amidst last year's housing cooling measures is expected to underpin the loan demand of property developers for land purchases and housing constructions. Therefore, loans for use in Hong Kong (+8.8% yoy in January) are likely to grow moderately in 2017. ▪ On the other hand, loans for use outside Hong Kong continued to grow robustly by 8.1% yoy in January. Factors contributing to the growth includes (1) the tightening bias of the PBoC, (2) credit expansion controls in the onshore market and (3) policy support for offshore financing, may prompt Mainland corporates to increasingly turn to the offshore market for fund raising.
▪ HK's RMB deposits (-38.7% yoy to 522.5 billion) were down further to the lowest level since April 2011 in January due to China's tightening measures on cross border RMB payments as well as lingering concerns about a renewed RMB depreciation.	▪ Adding on the tightening bias of the PBOC, CNH liquidity will likely remain volatile this year while the gap between CNH and CNY may persist. However, in the near term, with HK banks lifting RMB deposit rates and the RMB remaining relatively stable, the volatility of CNH liquidity may be reduced.
▪ Decline in HK's retail sales moderated further to -0.9% yoy in January. The increases were mainly seen in the sales of food, goods in supermarkets and fuels due to the effect of the Lunar New Year Holiday. On the contrary, declines remained prominent in the sales of clothing, footwear and allied products (-3.6% yoy), consumer durable goods (-17.8% yoy). Also, sales of jewelry, watches and clocks and valuable gifts retreated by 3.9% yoy.	▪ Though total visitor arrivals (+4.8% yoy) increased for the second consecutive month in January, tourists' purchasing power appeared to have been suppressed by a stronger HKD. Furthermore, though we expect domestic consumption to grow moderately on a stable labor market and fiscal stimulus, households tend to consume online or overseas as a stronger HKD makes foreign goods and services cheaper. Therefore, even with low base effect, we expect merely 1% to 3% growth in retail sales this year.
▪ Macau: unemployment rate rose slightly to 2.0% in the three months through January after remaining static at 1.9% for 17 consecutive months.	▪ The advancement in the retail sector (4Q retail sales value marked its positive gain for the first time since 2Q 2014) underpinned hiring sentiments. The same is true to the gaming sector after its labor redundancy was eliminated. However, a stronger MOP and policy risks may hit the gaming and retail sectors. Furthermore, as there is only one hotel project scheduled to be completed this year, labor demand in the construction sector as well as for the hotel, restaurant and similar sectors have been decreasing. Nevertheless, tight labor supply will still warrant a resilient labor market. We expect unemployment rate to stabilize around 2% throughout 2017

	with wage growth stagnating for a longer period due to uncertain outlook at home and abroad.
▪ Junket operators might have held some events, as usual, following the Chinese New Year Holiday to attract VIP gamblers. As a result, gross gaming revenue (GGR) was up 17.8% yoy to a two-year high at MOP22.99 billion in February.	▪ The rosy data reinforces that January's slowdown in GGR growth was short-lived. However, the outlook of the gaming sector is relatively mixed. With a full smoking ban off the table, downward risks on the VIP segment are partially eased. China's stabilization in 1H will also lend more support to the gaming sector. On the flip side, VIP demand could shrink due to policy risks and the expected correction of Mainland property market in 2H. Additionally, a stronger MOP and the abating attractiveness of new hotels will likely limit the improvement in the mass-market segment. Therefore, we expect growth of 5% to 7% in GGR over 2017.

RMB	
Facts	**OCBC Opinions**
▪ RMB weakened against the dollar with both USDCNY and USDCNH tested 6.90 as a result of stronger dollar. However, RMB index tracked the dollar index higher to end the week at 94.28, up from 93.84.	▪ The gap between onshore CNY and offshore CNH has been largely closed as offshore RMB liquidity stabilized. As highlighted by Premier Li Keqiang on Sunday, we think RMB is likely to take a back seat this year and China is unlikely to pursue more reforms on currency. As such, we expect RMB to remain stable against the currency basket.

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