Highlights:

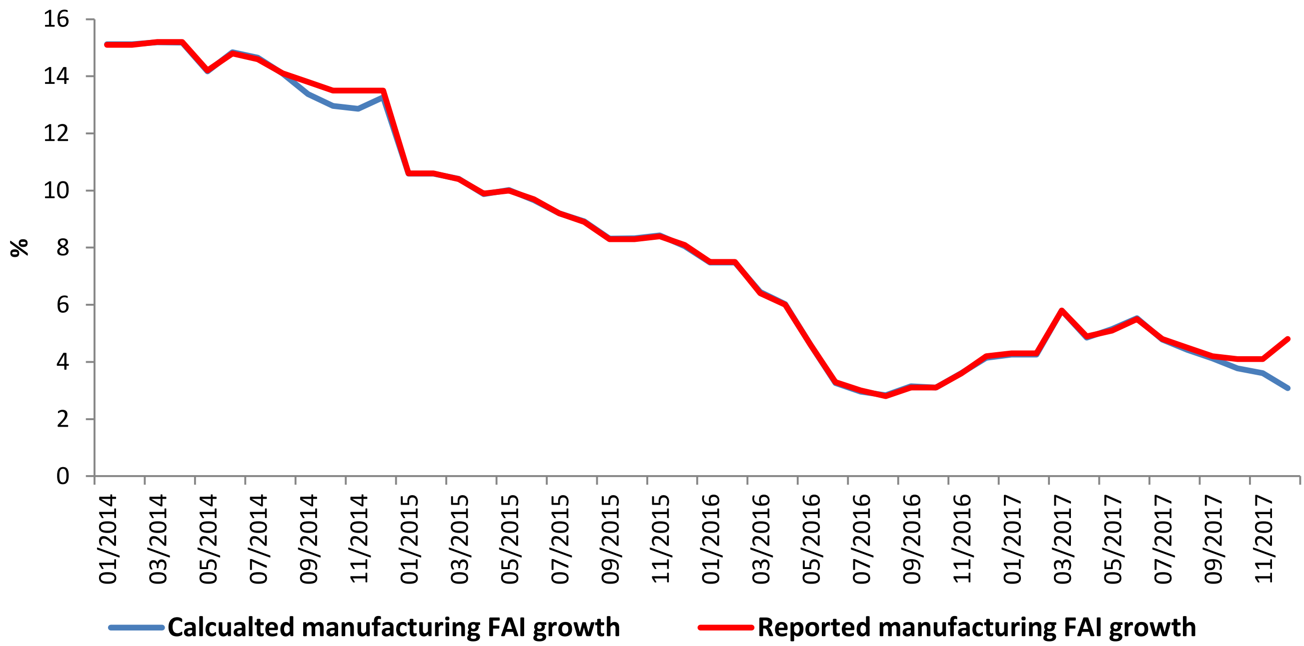
The Chinese economy reaccelerated to 6.9% yoy in 2017 from 6.7% yoy in 2016. Despite negative impact of higher funding costs and environmental protection rules, the economy remained resilient in the second half of 2017. The better than expected growth was mainly attributable to two factors in our view including ongoing economic transformation and improving external demand. Looking ahead, we expect the Chinese economy to slow down to 6.5% gradually in 2018 as we think the elevated funding costs may eventually weigh down the growth outlook.

The Chinese regulator has become more open-minded to unveil those fraud cases such as fake GDP data and bad loan cover up. The latest scandals in Shanghai Pudong Development Bank's bad loan cover up may raise renewed concerns about China's data quality. However, on the positive note, it means China is moving towards a more transparent system. On fake GDP, the local fraud cases may not have material impact on China's national GDP as the aggregate provisional GDP tends to be higher than national GDP by couple of trillions due to different statistical methods.

The rapid appreciation of RMB has caught market by surprise. We think the stronger RMB is still mainly the function of weak broad dollar. However, without the adjustment of counter cyclical factor, the pressure has been transferred from USDCNY to RMB index. The pressure for RMB to appreciate against its major trading partners is building up. Although the USDCNY fixing was set at higher than expected level of 6.4112 this morning, the RMB index rose further to 95.33. The QnA published by China's Forex Market Self-Discipline Mechanism Secretariat last Friday is a timely reminder that the CCF is still alive. As we have been arguing in the past, RMB index is a more important parameter for China's policy makers. Should RMB index rise further, China may restart the counter cyclical factor to alleviate the pressure on RMB appreciation.

In Hong Kong, focus of market has shifted from liquidity condition to the bull market. Hang Seng Index closed at its record high for the fourth consecutive trading day on 19 Jan 2018. On the one hand, flush liquidity and sustained economic growth across the globe have boosted risk appetite and driven rotation from bonds into equities and into emerging markets, including HK stock market. On the other hand, Mainland investors continued to show huge interests in HK stocks due to attractive valuation and increasing needs to diversify their portfolios. In the near term, wealth effect may underpin household spending and housing demand. In the longer term, global monetary tightening and US tax reform remain a concern as these two factors could trigger capital outflows. Elsewhere, unemployment rate dropped to a nearly two-decade low at 2.9% in 4Q 2017. Positive outlook of the major sectors on the back of strong external and internal demands will continue to support labor demand and help to sustain a tight labor market in 1H 2018. In Macau, the share of mass-market revenue ticked up to 38.8% from 37.4% in 4Q 2017. A new wave of mega project openings, further growth across Asia and completion of Hong Kong-Zhuhai-Macau Bridge together are set to boost tourism activities. This will in turn support mass market segment which could contribute more to gaming growth this year.

Chart of the week: The widening gap between calculated and reported growth of manufacturing investment shows that China may start to revise previous data to improve data quality.



Key Events and Market Talk	
Facts	**OCBC Opinions**
▪ China's central bank said last Friday that it will launch a counter cyclical coefficient to cross border RMB financing to better manage cross border capital flows.	▪ The ceiling of RMB cross border financing will depend on two parameters including bank's outstanding of total RMB deposits and counter cyclical factor, which will be set at 3% currently. The impact is unlikely to be significant in the near term. Nevertheless, we think the new coefficient is in line with China's plan to reboot RMB internationalization to allow the accumulation of offshore RMB liquidity pool
▪ The PBoC injected huge amount of liquidity into the system last week via both open market operation and medium term lending facility to meet funding demand ahead of tax payment.	▪ The PBoC net injected CNY590 billion via open market operation and conductedCNY398 billion 1-year MLF ahead of maturity of CNY289.5 billion MLF in January. The latest massive liquidity injection shows PBoC's policy flexibility to keep short end liquidity stable.
▪ China's Forex Market Self-Discipline Mechanism Secretariat published the Q&A on the use of counter cyclical factor in RMB's fixing mechanism last Friday.	▪ The organization, which consists of key interbank forex market players, said most of its members have adjusted the counter cyclical factor back to neutral. However, the formula, which includes CCF, has not been changed. As such, the CCF is likely to be triggered again should market condition change again. ▪ Although the recent rally of RMB against the dollar was mainly driven by the weak broad dollar, the pressure has been transferred to RMB Index, which started to pick up gradually in the past few days. Should RMB index continue to go up, we think the chance for restart of CCF to slow down the RMB appreciation cannot be ruled out.
▪ The Chinese regulator has become more open-minded to unveil those fraud cases such as fake GDP data and bad loan cover up.	▪ China's banking regulator CBRC announced a total CNY462 million fines on Shanghai Pudong Development Bank for its Chengdu Branch's fraud cases to cover bad loan. The branch was reported to issue CNY77.5 billion credit line to 1493 shell companies. The loss could be up to CNY10 billion according to local newswire. In addition, the branch management as well as staff in local banking regulator will also face severe penalty. The scandal may raise renewed concerns about China's loan quality. ▪ In addition, more local governments admitted fake data. The Baotou city in China's Inner Mongolia Autonomous Region revised its fiscal revenue in 2017 lower by nearly 50% due to previous fake additions after one district of Tianjin revised its nominal GDP down significantly.
▪ Hang Seng Index closed at its record high for the fourth consecutive trading day on 19 Jan 2018.	▪ On the one hand, flush liquidity and synchronized global recovery have boosted risk appetite and driven rotation from bonds into equities and into emerging markets, including HK stock market. On the other hand, Mainland investors continued to show huge interests in HK stocks due to attractive valuation (Hang Seng China AH Premium Index has long hovered above 125) and increasing needs to diversify their portfolios. Specifically, the daily average of southbound equity flow reached RMB3.58 billion during the first 14 trading days so far this year, the highest level since the launch of Shenzhen-Hong Kong stock connect. The daily turnover of HK stock market averaged at HK$146.67 billion so far this year which is 67.3% higher than the average of HK$87.64 billion over 2017. ▪ In the near term, wealth effect is likely to underpin household spending and housing demand. Besides, strong demand for HKD assets may help to reduce the downward pressure from

	wide yield differential on HKD. In the longer term, global monetary tightening and US tax reform remain a concern as these two factors could trigger capital outflows.
▪ Apart from new IPO rules which allow dual-class shares, HKEX's chief executive revealed their plan to launch A-share derivatives as MSCI will include A-share in Jun 2018. Also, he believes that it is possible to launch ETF connect this year despite difficulties in reaching agreements with Mainland exchanges and clearing houses in terms of the rules.	▪ As HKEX is set to loosen the regulation on IPO, we expect to see more large IPOs which may as a result boost market sentiment. Besides, with more cross-border investment schemes to be launched, HK stock market may lure more flows from Mainland China, which will bolster further growth in the turnover. With the stock market to expand further, companies from countries along the new silk road may also be attracted to go public in HK.
▪ It is reported that pensions regulator is considering the proposal which allows first-time buyers to withdraw their Mandatory Provident Fund savings for home purchase. Also, market is advocating for a downward adjustment to the upper limit of property value from HK$4 million to HK$6 million for the maximum LTV ratio of 90%.	▪ As housing prices continue to surge, prospective first-home buyers find it harder and harder to enter the market. The transaction volume of residential property priced no more than HK$5 million accounted for 36% of total transaction volume in 2017, much lower than 51% in 2016. Therefore, it is reasonable for the government to sort out a solution to address the issue. However, adjusting the cooling measures may not be an efficient way. Rather, the government should develop more residential lands and strive to increase both private and public home supply. Otherwise, pent-up demand from rising population will continue to push up the housing market in the long term.

Key Economic News	
Facts	**OCBC Opinions**
▪ The Chinese economy reaccelerated to 6.9% yoy in 2017 from 6.7% yoy in 2016. ▪ For breakdown, industrial production in December reaccelerated to 6.2% yoy from 6.1% yoy. Fixed asset investment rose by 7.2% yoy in 2017. However, retail sales decelerated to 9.4% yoy in December from 10.2% yoy in November.	▪ Despite negative impact of higher funding costs and environmental protection rules, the economy remained resilient in the second half of 2017. The better than expected growth was mainly attributable to two factors in our view including ongoing economic transformation and improving external demand. ▪ Although the share of consumption to GDP growth fell to 58.8% in 2017 from 64.6% in 2016, consumption and service sectors have played an increasing important role in China's economy. In addition, contribution of net export of goods and service to GDP growth rose to 0.63% in 2017, highest since China started to unveil this data in 2009. Without the strong support from external demand, China's growth would slow down to 6.3% in 2017. ▪ Looking ahead, we expect the Chinese economy to slow down gradually in 2018 as we think the elevated funding costs may eventually weigh down the growth outlook. ▪ One interesting observation from December data is that the gap between calculated growth of reported absolute manufacturing investment (at 3.1%) and reported growth rate of manufacturing investment (at 4.8%) widened significantly. This suggested that China may have started to revise the previous data to improve data quality.
▪ HK's unemployment rate dropped to a nearly two-decade low at 2.9% in the fourth quarter of 2017.	▪ First, jobless rate of the trade sector and financial sector decreased to 2.3% and 1.9% respectively, both hitting their lowest level since 1998 amid resilient global economic growth. Second, the unemployment rate of the consumption- and tourism-related sector stabilized at 4.3%, the lowest since 4Q 2014, amid improved tourism activities and strong domestic demand. Finally, construction sector's unemployment rate

	improved to the strongest level since the three months through Feb 2017 at 4.1%, owing to robust property and infrastructure construction activities. Moving forward, we expect benign global economic growth will continue to support HK's trade sector and tourism sector. Tight labor market, moderate wage growth as well as wealth effect from stock and housing markets, on the other hand, will support local consumption. Besides, property developers are likely to accelerate construction before local rate hikes curb housing demand, while fiscal stimulus will continue to support infrastructure construction. All in all, positive outlook of the major sectors will continue to support their labor demand and help to sustain a tight labor market at least in the first half of 2018.
▪ In 4Q 2017, Macau's VIP revenue edged up for the fifth consecutive month by 21.9% yoy while mass-market revenue grew at its fastest pace since 2Q 2014 by 17% yoy.	▪ It is noteworthy that the share of VIP revenue in total gaming revenue reduced to 56.2% from 57.7% while that of mass-market revenue ticked up to 38.8% from 37.4%. In addition, the growth of VIP revenue was the weakest since 1Q 2017. This may be attributed to high-base effect. Also, policy risk like anti money-laundering measures and tightening regulation on junket operators might have decelerated the growth of high-rollers. Moving forward, potential capital outflow risks and higher funding costs may hinder junket operators from providing credit extensions for VIP gamblers. Therefore, we expect VIP segment to make less contribution to gaming growth this year. In contrast, a new wave of mega project openings, further growth across Asia and completion of Hong Kong-Zhuhai-Macau Bridge together are set to boost tourism activities. This will in turn render support to mass market segment. Wealth effect from stock market and a weaker HKD may also encourage recreational gamblers to increase their betting amount. As such, mass-market segment could contribute more to gaming growth this year. All in all, we expect gaming sector to sustain its growth albeit at a slower pace (10%-15%) amid high-base effect.

RMB	
Facts	**OCBC Opinions**
▪ RMB extended its gain last week riding on weak broad dollar. The USDCNY broke down 6.40 briefly before ending above 6.40.	▪ We think the stronger RMB is still mainly the function of weak broad dollar. However, without the adjustment of counter cyclical factor, the pressure has been transferred from USDCNY to RMB index. RMB index broke 95 up and ended the week at 95.25. Although the USDCNY fixing was set at higher than expected level of 6.4112, the RMB index rose further to 95.33. Should RMB index rise further, China may restart the counter cyclical factor to alleviate the pressure on RMB appreciation.

OCBC Greater China research

Tommy Xie
Xied@ocbc.com

Carie Li
Carierli@ocbcwh.com