Highlights

Although there is lack of details from the US-China trade talk, the extension of US-China trade talk by one day on the back of President Trump's twitter that the talk goes well gave market hopes that US-China may be able to strike the deal before the deadline. Devil is always in detail. How the US will enforce China's implementation to protect the intellectual property rights is likely to the key focus of the talk going forwards.

China's latest inflation data surprised the market on the downside, partly driven by the weak oil prices in December. Nevertheless, it also shows the weaker industry demand which may dampen the growth of industrial profit. The producer inflation is expected to remain low in the coming months. The weak inflation creates room for China to roll out more monetary easing if needed. In addition, the weaker than expected pace of fiscal stimulus may fuel expectation on more monetary easing. China's interbank liquidity turned flush last week following the announcement of RRR cut. The overnight funding cost fell to as long as 1.38%. We think the easing interbank liquidity may fuel further rally of bond market.

RMB recorded the best weekly performance against the dollar since 2005.In addition, RMB also outperformed its major trading partners. RMB's rebound was initially driven by weaker dollar due to the re-pricing of Fed rate hike expectation. The move was exaggerated by the positioning adjustment as a result of positive headline from the US-China trade talk. Although we don't believe there will be any Shanghai Accord to force RMB to appreciate, the expectation on positive development of US-China trade talk may continue to support RMB in the near term with the USDCNY may possibly test 6.70 should more corporates join the trend to sell the dollar. However, we think the current fundamental does not support the sustainable rally of RMB.

In **Hong Kong,** housing transaction volume plunged by 61% yoy to the lowest since February 2016 in December 2018. Despite that, lately, the market showed some signs of rebound. The CCL index which tracks secondary housing prices ended the longest losing streak since 2008. This may be due to easing concerns about rising interest rates, the currently limited supply of public housing, the reducing offer price of secondary and primary homes, and improved sentiments on US-China trade truce and China's monetary stimulus. The speculation on the unwinding of housing control measures also lent some support to the housing demand. Nevertheless, we expect the rebound to be short-lived as the economic outlook of China and HK remains subdued amid the still tightening global liquidity and the lingering uncertainty about trade war. On the other hand, with public housing supply to increase notably in the coming decade, private housing prices may need to drop further to attract buyers. In conclusion, we hold onto our view that housing transaction volume to remain muted and housing prices to fall by around 10% yoy in 2019. **Elsewhere**, as HKD liquidity returned to the market after year-end, we expect HIBOR to drop further before Lunar New Year with 1M HIBOR and 3M HIBOR to fall towards 1.2% and 1.7% respectively. Given flushed liquidity, the return of carry trade may push USDHKD up. Should USDHKD touch 7.85 and trigger further liquidity drainage by the HKMA, this may add onto seasonality and equity outflows in driving up HIBORs throughout 2019. However, we expect HK's capital outflow risks to be manageable given the Fed's possible pause, the efforts of the US and China to ease trade tensions, and China's stimulus measures. As such, the increase in HIBOR throughout 2019 is likely to be moderate and gradual.

Key Events and Market Talk	
Facts	**OCBC Opinions**
▪ The US-China trade talk in Beijing last week was extended by one day. ▪ President Trump twittered that the trade talk is going well.	▪ Although there is lack of details from the US-China trade talk, the extension of US-China trade talk by one day on the back of President Trump's twitter that the talk goes well gave market hopes that US-China may be able to strike the deal before the deadline. It was tipped that China's Vice Premier Liu He will visit the US at the end of January. Market will watch out for Liu He's visit to US and upcoming Davos World Economic Forum where Chinese Vice President Wang Qishan may meet his US counterparties.
▪ China's State Council unveiled more tax cut for small and micro business including subsidy to corporate income tax and higher threshold for value added tax. The new tax incentive is expected to bring down the tax burden for small business by CNY200 billion. Premier Li asks all levels of governments to control the expense. ▪ Meanwhile, China's Finance Minister said proactive fiscal policy does not mean excessive stimulus and	▪ Market has formed the consensus that China's fiscal policy will play a bigger role this year to stimulate the growth amid the rising uncertainty from the trade war and global slowdown. However, given the constraints from the high leverage ratio, China's fiscal policy may not be as proactive as some expected. The latest news from the Bloomberg quoting source also shows that China may set the fiscal deficit at below 3% for 2019. The weaker than expected pace of fiscal stimulus may fuel expectation on more monetary easing.

China will continue to keep debt level in check.	
▪ China's interbank liquidity became very flush after China announced the first universal cut since April 2016. The overnight interbank lending rate between banks fell to as low as 1.38% last week before ending the week at 1.7%, down from 2.48% at the end of 2018. Meanwhile, 7 day repo rate between banks also touched 2.21%, lowest since June 2015.	▪ China's bond market rallied on the back of flush liquidity. Market is monitoring how low of the interbank lending rate the PBoC will tolerant. Should PBoC remain quiet to allow the interbank rate to drift lower, it may confirm market's expectation that China's monetary policy has turned more simulative amid the rising downside risk for Chinese economy.
▪ 1M HIBOR and 3M HIBOR fell by over 100bps and 60bps respectively to 1.35% and 1.83% as HKD liquidity returned to the market after year-end.	▪ We expect HIBOR to drop further before Lunar New Year with 1M HIBOR and 3M HIBOR to fall towards 1.2% and 1.7% respectively. Given flushed liquidity, the return of carry trade which shorts HKD for higher-yielding USD may push USDHKD up towards 7.845 or even 7.85. Should USDHKD touch 7.85 and trigger further liquidity drainage by the HKMA, aggregate balance may reduce from the current HK$76.5 billion towards HK$50 billion. This may add onto seasonality and equity outflows (southbound equity inflows amounted to HK$82.7 billion while northbound equity inflows totaled HK$294.2 billion under stock connects in 2018) in driving up HIBORs throughout 2019. However, we expect HK's capital outflow risks to be manageable given the Fed's possible pause, the efforts of the US and China to ease trade tensions, and China's stimulus measures to cushion the economy. As such, the increase in HIBOR throughout 2019 is likely to be moderate and gradual. In conclusion, we revise down our forecasts on HIBOR for 2019 with 1M HIBOR and 3M HIBOR to test 2.75% and 2.85% respectively.

Key Economic News

Facts	OCBC Opinions
▪ China's FX reserve increased further in December for the second consecutive month by US$11 billion to US$3.07 trillion.	▪ The rebound was mainly the result of valuation effect as global bond prices rallied in December. We think capital flow to China in December is more balanced thanks to the trade truce.
▪ China's inflation softened more than expected in December. CPI decelerated to 1.9% yoy from 2.2% in November while PPI collapsed 0.9% yoy from 2.7% yoy.	▪ The deceleration of CPI is mainly the result of weaker non-food inflation, which is driven by the sharp decline of oil prices. Non-food inflation fell by 0.2% mom in December, down for the second consecutive months. The decline of non-food price was mainly due to the correction of transportation costs, which fell by 1% mom in November and 1.9% mom in December, as a result of falling oil prices. Food prices rebounded by 1.1% mom in December partly driven by the recovery of pork prices due to recent outbreak of disease. ▪ The sharp decline of PPI is mainly due to two reasons including the drop of raw material prices due to weaker industrial demand and high base effect. Given the PPI has a high correlation with China's industrial profit; we think China's industrial profit may slow down further in the coming months. With high base effect kicks in in the beginning of the year, China's PPI may decelerate further. The probability of negative reading cannot be ruled out in the first half of 2019. ▪ The weak inflation creates room for China to roll out more monetary easing if needed.
▪ China's registered urban unemployment rate fell to 3.8% in 2018 down from 3.9% in 2017.	▪ The surveyed urban unemployment rate also fell slightly in 2018. Despite the falling headline number, China's job market has

	been under rising pressure due to rising uncertainty from the trade war and global slowdown. China is likely to roll out more supporting measures in 2019 to stabilize the job market.
▪ Hong Kong's housing price index was down for the fourth consecutive month by 3.5% mom in November. During the same month, approved new mortgage loans dropped for the third consecutive month to the lowest since December 2017. Worse still, housing transaction volume plunged by 61% yoy to 2060 deals in December 2018, the lowest since February 2016.	▪ The correction in housing market was attributed to several unfavorable factors. First, prospects of higher borrowing costs. Second, lower wealth effect amid the correction in both housing market and stock market. Third, weakening outlook of wage growth due to local economic slowdown. Fourth, softer demand from Mainland China on China's slowdown and tight capital controls. Fifth, the shifting of housing demand from private to public sector on the back of government's promise to increase public housing supply. ▪ Despite that, lately, the market showed some signs of rebound. The CCL index which tracks secondary housing prices ended the longest losing streak since 2008 during the week ended 30th December 2018. This may be due to several reasons. First, concerns about rising interest rates eased as the Fed showed a dovish stance. Second, the limited supply of new public housing at this moment and the reducing offer price of secondary and primary homes prompted some potential buyers to return to the private market. Third, economic outlook became less sluggish after the US and China agreed on trade war ceasefire and the PBOC unleashed a raft of easing measures. Fourth, HK officials' talk raised market speculation on the unwinding of housing control measures. ▪ Nevertheless, we expect the rebound to be short-lived. On the one hand, as the Fed may still raise rates twice this year and the uncertainties about US-China trade war continue to linger, the economies of both China and HK are not out of the woods yet. On the other hand, with the public housing supply to increase notably in the coming decade, private housing prices may need to drop further to attract buyers. In conclusion, we hold onto our view that housing transaction volume to remain muted and housing prices to fall by around 10% yoy in 2019. The market of smaller flats may take a harder hit with an expected decrease of 15% yoy in prices for 2019.
▪ Macau's housing transaction volume dropped for the third consecutive month by 37.2% yoy to 588 deals while approved new mortgage loans retreated by 11.6% yoy to MOP3.59 billion in November. During the same month, average housing price (+12.2% YTD) dropped by 6% mom to MOP108,924/square meter.	▪ The tepid data reinforces our view that October's rebound was short-lived amid several unfavorable factors. First, housing control measures from early last year effectively dented speculative demand with the share of home buyers with more than one flat sliding sharply from 44.9% in February 2018 to 3.6% in November 2018. Second, investor sentiments have softened gradually from last June amid higher borrowing costs (banks lifted prime rate for the first time since 2006) and US-China trade war. Third, wealth effect subsided with HK stock market correction. Fourth, HK's housing market slowdown might have had some spill-over effect on Macau's market. ▪ In conclusion, we expect housing translation to remain subdued despite the abating concerns about a hawkish Fed and US-China trade war escalation. The expected deceleration of Macau's gaming growth and economic growth would also continue to weigh on housing demand. Nevertheless, with unemployment rate falling to the lowest level since 2015 and housing measures continuing to support first-home buyers (represented 83.3% of total homebuyers in November 2018), average housing price may hold up well and oscillate around MOP100,000/square meter. Also, as housing starts falling for the third consecutive

	year by 52% in 2018, limited future housing supply would cap the downside for housing prices.

RMB	
Facts	**OCBC Opinions**
▪ RMB recorded the best weekly performance against the dollar since 2005. The USDCNY ended the week at around 6.75. What's more RMB also rallied against its major trading partners with the spot RMB index rose to around 93.8 from below 93 level.	▪ RMB's rebound was initially driven by weaker dollar due to the re-pricing of Fed rate hike expectation. The move was exaggerated due to positioning adjustment as a result of positive headline from the US-China trade talk. Although we don't believe there will be any Shanghai Accord to force RMB to appreciate, the expectation on positive development of US-China trade talk may continue to support RMB in the near term with the USDCNY may possibly test 6.70 should more corporates join the trend to sell the dollar. ▪ However, we think the current fundamental does not support the sustainable rally of RMB. To recall, RMB depreciation in 2018 was mainly driven by three factors including stronger dollar, US-China trade war and US-China interest rate differential. Although dollar has weakened recently, the factors from the US-China trade war and policy divergence remain uncertain. In fact, we expect the US-China interest rate differential to narrow further as China has been easing more decisively. This may weigh down the RMB outlook in future.

OCBC Greater China research

Tommy Xie
Xied@ocbc.com

Carie Li
Carierli@ocbcwh.com

Co.Reg.no.:193200032W