Summary

Last week, the RMB was under notable downward pressure with the offshore Yuan refreshing its record-low and even testing the crucial level of 6.8. On this, most officials stated that the depreciation of RMB was mainly attributed to the strength in USD while there is no basis for a continuous drop in the RMB. Besides, the depreciation of CNH in the spot market did not exert spillover effect to the future or forward market. This indicates that the market becomes more adaptive to the higher volatility of the Yuan and believes that disorderly large fall in the Yuan is unlikely.

Onshore investors' purchase of investment-linked life insurance in Hong Kong by UnionPay cards is suspended from Oct 29 onwards. Recent announcement by the UnionPay International indicates that the top leadership intends to tighten controls over capital outflows. As the quota of individual foreign exchange is nearly used up, we believe that any capital outflows will be controllable in near term. More importantly, due to FBI E-mail bombshell, the uncertainty of US election intensifies and hits the greenback. This eases downward pressure on the RMB and enables the currency to show renewed two-way volatility. On the other hand, with the market gradually pricing in Fed's Dec rate hike, the upward pressure on the USD may be limited and thereby alleviate the depreciation risks of the Yuan in near term.

Elsewhere, in an unusual manner, China's President Xi Jinping chaired the politburo meeting on economic issues last Friday, one day after concluding the 6th plenum meeting. Curbing asset bubbles and safeguarding financial risk have topped the meeting. The less dovish signal, which reinforced market belief that top leadership has put priority on containing asset bubble than spurring growth, justified the recent volatility in China's onshore bond market. The bond market was sold off drastically early next week due to the rise of short end money market rate and news that PBoC may have added the wealth management products into its macro prudential assessment system on broad credit expansion. Clearly, China's bond market has been the battleground for policy makers to demonstrate their policy direction to contain leverage and asset bubble. The battle may continue with money market likely to be the victim in the near term.

Jun Ma of the PBOC clarified that the off balance sheet wealth management products are not officially included into the MPA of credit growth. This may ease some downward pressure on the bond market. However, Ma also mentioned that the central bank is doing the preparation works. Should the new policy be carried out, bond market sentiment will inevitably be dampened in the short term. But in the longer term, the monetary policy is unlikely to be tightened while limitation of investment channels may also persist. Given these two factors, banks' capital will still flow into the bond market. Also, foreign capital inflows to onshore bond market for yields hunting will lend some support to the bond market. This week, eyes will be on China's Oct PMI to see whether the economy is stabilizing.

Key Events and Market Talk	
Facts	**OCBC Opinions**
▪ In an unusual manner, China's President Xi Jinping chaired the politburo meeting on economic issues last Friday, one day after concluding the 6th plenum meeting. Curbing asset bubbles and safeguarding financial risk have topped the meeting.	▪ The less dovish signal, which reinforced market belief that top leadership has put priority on containing asset bubble than spurring growth, justified the recent volatility in China's onshore bond market. The bond market was sold off drastically early next week due to the rise of short end money market rate and news that PBoC may have added the wealth management products into its macro prudential assessment system on broad credit expansion. Clearly, China's bond market has been the battleground for policy makers to demonstrate their policy direction to contain leverage and asset bubble. The battle may continue with money market likely to be the victim in the near term.
▪ Local media reported that the off balance sheet wealth management products may be included into the macro prudential assessment of credit growth. Bond market tumbled in the aftermath of the news report.	▪ The rapid expansion of off balance sheet wealth management products in the past few years has raised concerns about the credit bubble. About half of those wealth management products have been invested in bond market. As such, the concern is that the regulatory framework may dampen the demand for bond in the near term. However, Jun Ma of the PBOC clarified that the off balance sheet wealth management products are not officially included into the MPA of credit growth and the central bank is still doing the preparation works. This may help ease some downward pressure on the

	bond market. ▪ On the other hand, the rating agency Moody's stated that Chinese shadow banking expanded by 19% yoy in 1H and has doubled to CNY58 trillion over the past five months, accounting for nearly 82% of GDP. Should the government increases scrutiny on banks' off balance sheet wealth management products, the growth of shadow banking may be further constrained.
▪ The Shanghai Stock Exchange (SSE) was said to tighten control over bond issuance by property developers and companies struggling with overcapacity.	▪ The Shanghai Stock Exchange (SSE) requires that the funds raised by bond issuance of the property developers cannot be used for land purchase. Furthermore, both Guangzhou and Beijing governments cap the price for residential-use lands in auction. Meanwhile, Beijing government even set limit on the sales price for the residential property units. Elsewhere, the Political Bureau reiterated its focus on control of asset bubble and financial risks. Taken all together, we expect that the top levels may allow the GDP growth to moderate somehow in the coming quarters as the support from the property market may diminish. Besides, credit growth is expected to slow due to curb on loans to homebuyers and property developers.
▪ The National Association of Financial Market Institutional Investors (NAFMII) loosened the entry requirement for non-financial qualified institutional investors to interbank bond market.	▪ The investors should be in continuous operation for no less than one year. Also, the net financial assets owned or managed by the registered investment companies or other organizations should be no less than CNY10 million. Other enterprises are required to have no less than CNY10 million of net assets should they want to enter the interbank bond market. With a wider range of participants entering the interbank bond market, the market's development is expected to deepen. Further improvement in the interbank bond market will also help lure more foreign inflows.
▪ China UnionPay International announced that the use of its credit and debit cards for insurance purchases in Hong Kong will be curbed expect for accident and medical coverage.	▪ The purchase of insurance under current account is allowed while that under capital account, such as investment-linked insurance products, will be suspended. In fact, despite the USD5, 000 cap on each overseas payment made by UnionPay cards, investment-linked life insurance products have been a prevailing way for the onshore investors to diversify their portfolio and hedge against RMB risks. According to HK Office of the Commissioner of Insurance, the new office premiums from policies issued to Mainland visitors surged by 138% yoy to HKD16.9 billion in 2Q, reaching the record high. Recent announcement by the UnionPay International indicates that the top leadership intends to tighten controls over capital outflows, in order to ease the downward pressure on the RMB amid Fed's Dec rate hike.
▪ HKMA announced that it has designated two more banks as Primary Liquidity Providers (PLPs) for offshore RMB market in Hong Kong in addition to the existing seven banks.	▪ As the PBOC appears to increase its tolerance of higher liquidity of the RMB, market concern about further depreciation in RMB may prompt more offshore investors to short the currency. In this January and September, the PBOC had intervened in the offshore market and pushed up the CNH HIBOR. As a result, the HKMA had to inject RMB liquidity and leveraged the PLPs to increase the liquidity. With the increased number of PLPs, the CNH market will be find it easier to defend risks associated with currency depreciation. This will also pave the way for further development of the offshore RMB market in Hong Kong and to facilitate RMB internationalization.

▪ HKMA took action to curb illegal second mortgage.	▪ Should the homeowners apply for any top up loans to the financial companies owned by property developers after they borrowed from the banks in terms of first mortgage and did not notify the banks, Land Registry will notify the banks. As a result, the homeowners may be asked to pay higher mortgage rates, make loan repayment or provide more collateral. Though the new rule does not apply to the homeowners whose mortgage loans have been approved, the new buyers will be regulated and help ease the credit risks added to the banks. However, the new rule is unlikely to hit the housing market as a majority of potential buyers are not reliant on second mortgage.

Key Economic News	
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▪ China industrial profit growth decelerated notably to 7.7% yoy in September from 19.5% yoy in August.	▪ This is in line with the slowed industrial production in September. The dissipating base effect is also the reason behind the slowdown. One bright spot is that the mining sector's profits reversed its downward trend firstly since Oct 2013. Moreover, given that PPI ended its longest streak of decline in September on recovery of global commodity prices, the industrial profits may regain some growth traction. However, as the government stresses heavily on risk controls including deleverage and housing cooling measures, upward pressure on industrial profits is likely to be limited in the near term.
▪ According to SAFE, by end of September, Hong Kong-domiciled funds sold in the onshore market under the mutual fund recognition scheme reached 8.39 billion yuan.	▪ In comparison, the southbound sales of Mainland China-domiciled funds in Hong Kong were merely 96.8 million yuan, representing 11.5% of the northbound sales. This clearly reflects that Hong Kong funds are more popular on the mainland than the other way round, especially given the increasing need of onshore investors to hedge against RMB risks. Also, it is considered an alternative way to diversify the portfolio since the QDII quota has been largely used up. Due to tighter control over capital outflows, such as the recent curbs on investment-linked insurance purchase in Hong Kong, we expect that the gap between the southbound sales and the northbound ones under the mutual fund recognition scheme will continue to widen.
▪ Hong Kong: Export growth in value terms increased 3.6% yoy in September.	▪ Expansion in exports to the Asian rendered the key growth impetus. Region-wise, exports to Asia as a whole grew further by 4.9% yoy, led by exports to Taiwan, India and China, which increased 27.9% yoy, 20.8% yoy and 5.1% yoy respectively. On the flipside, China reported its import growth from Hong Kong as -3.2%, the first negative growth in recent years. This was mainly attributed to strengthened administrative measures on cross border capital flow and the narrowing gap between CNH and CNY, which limited the opportunity for carry trade. However, we remain wary of the reignition of the over-invoicing activity given the continuous high volatility and depreciation pressure of RMB in recent months. Elsewhere, exports to other main trading partners showed some weakness, in particular exports to Germany (-16.3%), US (-1.2%) and the UK (-0.8%). Though the export regains some traction in recent months, external environment is still fraught with considerable uncertainties, including (1) fragile

	recoveries of some advanced economies, (2) monetary policy divergence among major central banks and (3) concern on a hard Brexit.
▪ Macau: Visitor arrivals rebounded by 0.5% yoy in September due to the effect of Mid-Autumn Festival and two new hotel openings.	▪ Notably, the share of overnight visitors rose to record-high at 54%. As a result, the 11.8% gain in overnight tourists well offset the 10.2% decline in same-day visitors. This also explains the strong 7.4% yoy increase of gaming revenue in September. However, besides the increase in visitors from Mainland China, Taiwan and South Korea, what is more noteworthy is that the number of Hong Kong visitors dipped for the second straight month despite two new hotel openings and a series of preferential offers. Looking ahead, as there were 7% more of Mainland tourists to the town as compared to the same period last year during the Golden Week Holiday, this would have been a boost to the gaming sector. However, as the seasonal factor fades, we suspect that the appeal of new projects will be able to last in the medium term, especially given that only one more project is scheduled to be completed next year. With that said, the stabilizing gaming sector may find it hard to gain further traction.

RMB	
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▪ The PBOC set Yuan midpoint lower for most of last week mainly due to broad-based dollar strength on the rising expectations of Fed's Dec rate hike.	▪ This time, the depreciation of CNH in the spot market did not exert spillover effect to the future or forward market. The market clearly becomes more adaptive to the higher volatility of the Yuan. Most official media and spokesman believe that recent downward pressure on the Yuan is mainly attributed to the dollar strength and there is no basis for a long-lasting decline trend of the Yuan. The fixing price largely in line with expectations also proved that it has been set on a market-driven basis. ▪ However, increasing capital outflows amid seasonal factors as well as further strength of the greenback may add further downward risks onto the Yuan. Fortunately, due to FBI E-mail bombshell, the uncertainty of US election intensifies and hits the greenback. This eases downward pressure on the RMB and enables the currency to show renewed two-way volatility. On the other hand, with the market gradually pricing in Fed's Dec rate hike, the upward pressure on the USD may be limited and thereby alleviate the depreciation risks of the Yuan in near term.

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