Highlights:

The bad news last week was that China's bond market failed to react to targeted reserve requirement ratio cut after coming back from the golden week holiday despite equity market has been supported. The underlying driver to the different reaction of bond investors and equity investors is liquidity. The PBoC's decision to suspend open market operation last Monday, shocked bond investors as this implied a net withdrawal of CNY180 billion liquidity from the system, which expired during the holiday. The concerns about liquidity eased on Friday as a result of generous medium-term lending facility (MLF) which will inject CNY498 billion into system, more than CNY439.5 billion maturing this month.

The highly watched 19th Party Congress will start from 18 Oct and last for six days. One thing investors should bear in mind is that Party Congress is a political event rather than platform for economic policies. As such, we do not expect any major announcement regarding any economic policy. Nevertheless, leading into the Congress, we did hear more agencies out there to communicate their reform plan to commit to President Xi's ambitious reform agenda. PBoC Governor Zhou Xiaochuan's interview last week was a market mover, which supported RMB. The key takeway is that China will continue to drive openness in trade and investment, reform in currency mechanism and reducing currency intervention to open its economy. In addition, China' banking regulator also said containing financial risk will be put in a more important position.

On economic front, China's trade surplus shrank in September due to stronger than expected imports. The strong import of electronic integrated circuit is in line with strong export of electronics data reported by Singapore and Malaysia. This shows the entire electronic value chain in Asia continued to benefit from the global recovery, which may further support Asia's export story. China's September financial data beat market expectation, partially attributable to seasonal pattern. One of the notable changes is that off-balance sheet lending revived, which could be the result of recent property tightening.

On currency, stability is probably the name of game in most part of China leading into the Party Congress. However, it is no longer the case for RMB. We think China prefer two-way volatility to stability in terms of currency. The recent move helps market form expectation on RMB's two-way volatility. In addition, the second consecutive month decline of foreign currency deposit in September was another evidence of formation of RMB's two-way movement expectation.

In Hong Kong, Chief Executive Carrie Lam released her maiden policy address and proposed to support the development of Innovation and Technology industry and tackle housing issues with some new measures. On the one hand, the Government proposes to increase the supply of Starter Homes and flats under the Green Form Subsidized Home Ownership Scheme by 5,000 units next year. As such, potential home buyers may refrain from purchasing a smaller size private home at this juncture. Regularizing the Interim Scheme of Extending the Home Ownership Scheme Secondary Market to White Form Buyers could also shift some demand out of the overheated private housing market. Therefore, we believe housing market moderation (especially the secondary market) to continue in the rest of 2017. On the other hand, the proposed tax reduction may translate into growth in corporate spending of SMEs and start-ups and help to attract companies from the Mainland China and foreign countries. Finally, as the Government continues to support innovation and technology development by increasing investment, reducing tax, and participating in the development of the Greater Bay Area (GBA), we expect to see more cooperation between the high-tech companies in Hong Kong and other cities in the GBA.

Key Events and Market Talk	
Facts	**OCBC Opinions**
▪ China's bond market failed to react to targeted reserve requirement ratio cut last week after coming back from the golden week holiday despite banking shares rallied on the back of RRR news.	▪ The underlying driver to the different reaction of bond investors and equity investors is liquidity. The PBoC's decision to suspend open market operation on Monday, first trading after the golden week holiday, shocked bond investors as this implied a net withdrawal of CNY180 billion liquidity from the system, which expired during the holiday. ▪ The concerns about liquidity eased on Friday as a result of generous medium term lending facility (MLF) which will injected CNY498 billion into system, more than CNY439.5 billion maturing this month.
▪ PBoC Governor Zhou Xiaochuan said in his interview with Caijing magazine that openness in trade and investment, reform in currency mechanism and reducing currency intervention are	▪ Zhou said no country can achieve an open economy with strict foreign exchange controls. His comments implied that the capital control since late 2015 is likely to be temporary and China will remove it at certain stage.

three important pillars of China's economic openness. The direction of on-going reforms on three pillars is unchanged. And China will speed up those reforms should there be appropriate window.	▪ Although Mr. Zhou is expected to retire in January 2018, his remarks set the tone for China's financial reform in the next five years. We expect China to speed up its reform after 19th Party Congress. China is likely to unveil plans to open its financial sector during President Trump's visit in November.
▪ China's banking regulator said China's non-performing loan ratio has declined by 0.04% since the beginning of the year. And the regulator has vowed to contain financial risk under President Xi's guidance.	▪ As we are approaching 19th Party Congress this week, more agencies have come out their statement to identify their key reform agenda in the coming years. Clearly containing financial risk actively will be put in a more dominant position.
▪ In Hong Kong, Chief Executive Carrie Lam released her maiden policy address. According to Carrie Lam's maiden policy address, the Government proposes some new measures to support the development of Innovation and Technology industry, tackle housing issues, as well as improve HK's role in the Belt and Road Initiative and the Greater Bay Area.	▪ First, the long-awaited "Starter Home" scheme disappointed as only 1,000 flats will be available by end of 2018. However, knowing that the total supply of starter homes and flats under the Green Form Subsidized Home Ownership Scheme will reach about 5,000 units next year, potential home buyers may refrain from purchasing a smaller size private home at this juncture. Regularizing the Interim Scheme of Extending the Home Ownership Scheme Secondary Market to White Form Buyers could also shift some demand out of the overheated private housing market. Therefore, we believe housing market moderation (especially the secondary market) to continue in the rest of 2017. However, should global tightening proceed at a gradual pace, we expect a bullish stock market, a stable labor market and resilient local economic growth to weather some impact of moderate interest rates increase and increasing public housing supply. If this is the case, housing market may still be able to rebound in 2018 after a brief and moderate correction. ▪ Second, small to medium-sized enterprises (SMEs) as well as the start-ups are likely to benefit from the proposed tax reduction and therefore may increase spending and push wage growth. Besides, this may attract SMEs from both Mainland China and other countries to HK. ▪ Third, the proposed tax reduction for and the additional investment in the innovation and technology industry may help to boost the industry's growth. Meanwhile, the Government aims to promote innovation and technology development by participating in the development of the Greater Bay Area. As such, we believe that Hong Kong's strong research capability and large talent pool will facilitate co-operation with Mainland China in terms of innovation and technology and in turn buoy growth of the Greater Bay Area. ▪ Fourth, with regard to the Belt and Road Initiative, Hong Kong will continue to play its role as a financing hub. Also, Hong Kong could share its expertise in financial services, professional services, high value-added shipping services, tourism services, and convention and exhibition services with the countries along the Belt and Road. In addition, the Belt and Road initiative may help to deepen the offshore yuan market and therefore bolster the development of CNH businesses in Hong Kong.

Key Economic News

Facts	OCBC Opinions
▪ China's FX reserve rose for the eighth consecutive month in September to US3.108 trillion, up from	▪ The recovery of FX reserve in September was probably due to asset appreciation despite less favourable valuation effect as a

US$3.091 trillion in August.	result of stronger broad dollar. In addition, the volatile RMB movement, which strengthened strongly in the first half of the month but weakened dramatically in the second half of the month did not stop China from achieving a more balanced capital flow picture. ▪ Given RMB's two-way movement expectation has been formed recently, we expect China's FX reserve to remain stable on the back of more balanced capital flow picture.
▪ China's export grew by 8.1% yoy in Sep while import rose by 18.7% yoy. As a result of stronger than expected import, China's trade surplus narrowed further to US$28.5 billion in Sep.	▪ Exports to EU and US reaccelerated to 10.4% yoy and 13.75% yoy in Sep due to low base. In addition, exports growth to ASEAN also recovered to 10.78% yoy in Sep although exports to East Asia remained weak with exports to Japan only grew by 0.05% yoy. ▪ For imports, imports of electronic integrated circuit reaccelerated to half year high of 18.4% yoy in Sep. This is in line with strong export of electronics data reported by Singapore and Malaysia. This shows the entire electronic value chain in Asia continued to benefit from the global recovery, which may further support Asia's export story. In addition, demand for commodity also improved. Imports of crude oil and iron ore by volume rose by 11.95% yoy and 10.58% yoy respectively. ▪ China's trade surplus with the US widened to a record high of US$28.08 billion in September. This may not bode well for the bilateral trade relationship between US and China. Trade is likely to continue to be the focus ahead of US President Trump's visit to China in November.
▪ China's September financial data beat market expectation. Total new Yuan loan increased by CNY1.27 trillion while aggregate social financing jumped to CNY1.82 trillion. ▪ Broad money supply M2 reaccelerated to 9.2% yoy from record low of 8.9%.	▪ For breakdown of new Yuan loan, the leverage of household sector continued to increase at a rapid pace. Total medium to long term loan to household sector remained strong at CNY478.6 billion despite China further tightened property rules. Short term loan to household sector also increased by CNY253.7 billion. Nevertheless, given China tried to ban consumption loan from entering the property market, short term loan to household sector may slow in the coming months. Medium to long term loan to corporate also remained steady at CNY502.9 billion signalling booming economic activity. ▪ Off-balance sheet lending rebounded in September, partially led to spike of aggregate social financing. Entrusted loan recovered to CNY77.5 billion while trust loan remained strong at CNY241 billion. The rebound of off-balance sheet lending is probably the result of property tightening, which drove funding needs back to off-balance sheet. ▪ On deposit, foreign currency deposit fell by US$13.1billion, down for the second consecutive month. The highest single month unwind of foreign currency deposit since November 2015 signalled the return of expectation on RMB's two-way movement. ▪ In addition, fiscal deposit fell by CNY397.2 billion, in line with seasonal pattern. The decline of fiscal deposit in August and September shows that proactive fiscal policy. This also explains why PBoC has been reluctant to inject the liquidity via open market operation in the past two months as proactive fiscal policy has provided liquidity to the system. ▪ In conclusion, although the strong financial data in September can be partially attributable to seasonal pattern, it does reflect

	the strong underlying growth momentum, which has exceeded our previous expectation. Nevertheless, given loan quota is likely to be limited in the last quarter, we think the magnitude of credit expansion in the past few months is unlikely to be sustainable.
▪ Macau's housing transactions dropped by 19.4% yoy in August to 652 deals, marking the first year-on-year decline since February 2016. In the same month, approved new mortgage loans fell for the first time since December 2016 by 13.6% yoy. Housing market remained relatively quiet due to new cooling measures, summer holiday effect and bad weather.	▪ We expect housing transactions and mortgage loans will remain tepid in the rest of 3Q as housing market sentiment may take time to recover after the two typhoons. However, with the launch of new home projects in 4Q (housing completions surged by 1260% yoy during the first eight months of 2017), we expect housing transactions in the primary market to rebound on a stable labor market and resilient domestic economic growth. Therefore, though the secondary housing market demand may continue to be curbed by cooling measures and prospects for higher rates, total housing transactions may still increase on a quarterly basis in 4Q. Average housing price is expected to oscillate around current level at MOP95,000 per square meter in the rest of 2017. ▪ In the longer term, we note that housing starts have fallen by 15% yoy during the first eight months of 2017 after sliding by 6% yoy in 2016. This means that the long-term home supply will increase at a rather slow pace. Also, the supply of public housing is likely to remain moderate in the coming years according to Macau Housing Bureau. Given limited new home supply together with strong demand on local economic recovery and a stable labor market, housing market is expected to remain resilient despite moderate growth in interest rates.

RMB	
Facts	**OCBC Opinions**
▪ RMB rallied again last week following PBoC Governor Zhou Xiaochuan's interview on further currency reform with the USDCNY ended below 6.60. In addition, RMB also appreciated against its currency basket with RMB index rebounded to around 95 level.	▪ Stability is probably the name of game in most part of China leading into the Party Congress. However, it is no longer the case for RMB. We think China prefer two-way volatility to stability. The recent move helps market form expectation on RMB's two-way volatility.

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