**Highlights:**

The Chinese economy decelerated in August with all three key economic indicators missed forecast. We think the recent slowdown was mainly self-engineered as a result of tighter policy in local government financing, property and environmental policy. Although manufacturing sector remains the bright spot thanks to resilient global recovery, we think it may not be sustainable due to rising raw material prices and negative impact of environmental inspection. Looking ahead, we expect China's growth to slow down further.

China's broad money supply M2 decelerated further to 8.9% yoy in August, lowest in record. The deceleration was partially the result of China's financial deleverage, which kept the interbank placement in check. However, as aggregate social financing growth remains steady at above 13% yoy, the widening gap between aggregate social financing and M2 growth shows there is no imminent pressure for PBoC to ease monetary policy. As such, we expect PBoC to continue to keep its prudent monetary policy intact. On the positive note, PBoC net injected liquidity last week after three weeks' net withdrawal to ease liquidity pressure ahead of quarter end and golden week holiday. We think PBoC will continue its balance game to keep leverage at bay while maintaining liquidity relatively stable.

On currency, market has received the signal from China has been unease about recent pace of appreciation. As such, RMB weakened against both dollar and currency basket last week. However, we think all factors supporting RMB remained intact. Therefore, the upside for USDCNY may be limited.

In Hong Kong, overnight CNH HIBOR jumped last week as the spillover effect of onshore tight liquidity and the unwinding of some long CNH positions. Higher funding costs may help to limit CNH weakness. Given a stable RMB, HK's RMB deposits may continue to grow and in turn improve the offshore yuan liquidity. Elsewhere, in the Belt and Road Summit held last Monday, Chief Executive Carrie Lam said the government have been discussing with Mainland China on a new cooperation agreement. On one hand, Hong Kong will continue to act as a financing platform for the Belt and Road Initiative (BRI). On the other hand, we are looking forward to a closer cooperation between HK and Mainland companies to support the BRI. For example, Hong Kong's MTR plans to team up with China Railway to bid for a high-speed rail link project which connects Kuala Lumpur and Singapore.

| Key Events and Market Talk | |
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| **Facts** | **OCBC Opinions** |
| ▪ China continued to step up its campaign for blue sky. Beijing announced to ban major construction work for four months from 15 November to contain the haze problem in winter. | ▪ The suspension of major construction work in China's capital city is expected to weigh down the growth prospect. However, as China has shifted its focus to achieving a more sustainable growth in the longer run, China's commitment to environmental protection is unlikely to be derailed by short term economic volatility. As such, we expect environmental issue will be one of the key factors slowing the growth down in the coming quarters. |
| ▪ China's central bank loosened its grip on liquidity last week ahead of quarter end and golden week holiday. PBoC net injected CNY260 billion via open market operation last week after net withdrawal for three consecutive weeks. | ▪ The liquidity injection via reverse repo helped ease tight liquidity pressure ahead of key quarter-end macro prudential assessment. We think PBoC will continue its balance game to keep leverage at bay while maintaining liquidity relatively stable. |
| ▪ The offshore RMB funding cost started to climb up last week with the overnight CNH HIBOR was fixed at 3.05% on Sep 13, up from 1.51% on Sep 8, due to the spillover effect of onshore tight liquidity. In the onshore market, banks started to hoard the cash to prepare for the upcoming quarter-end as well as golden week holiday. | ▪ The rise may be also partially due to an unwinding of some long CNH positions as market became less bullish on the Yuan after the PBOC showed unease about the recent Yuan strength.<br>▪ The climb of CNH funding may limit the space for CNH correction. Given that all the factors supporting the appreciation of RMB remain in place, the market may still buy RMB on dips. As such, we expect CNH deposits will continue to rebound and improve offshore RMB liquidity. |
| ▪ In the Belt and Road Summit held last Monday, Chief Executive Carrie Lam said the government has | ▪ On the one hand, Hong Kong acts as a financing platform for projects related to the Belt and Road Initiative. Market |

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| been discussing with Mainland China on a new cooperation agreement which highlights Hong Kong's advantages under the Belt and Road initiative. The new agreement will cover key areas such as finance and capital raising, infrastructure facilities, trade and investment facilitation, project information sharing, interfacing and dispute resolution, and people-to-people bond promotion. | estimates that about 20% to 30% of the increase in loans this year was related to the Belt and Road Initiative. On the other hand, a closer cooperation between Mainland and Hong Kong to support the Belt and Road Initiative could be expected, especially under the new agreement. For example, Hong Kong's MTR planned to team up with China Railway Group to bid for a high-speed rail link project which connects Kuala Lumpur and Singapore. Meanwhile, China Railway Group also said they will team up with MTR to jointly develop rail projects along the Silk Road as they value highly of MTR's expertise in management, easy access to finance and familiarity about international rules and regulations. According to the Prime Minister of Malaysia, an international tender for the project will be called in the fourth quarter of 2017. |
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## Key Economic News

| Facts | OCBC Opinions |
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| ▪ The Chinese economy decelerated in August with all three key economic indicators missed forecast.<br>▪ Chinese industrial production growth slowed to 6% yoy in August from 6.4% yoy in July.<br>▪ Fixed asset investment in the first eight month decelerated noticeably to 7.8% yoy from 8.3% yoy in the first seven month.<br>▪ Retail sales growth also slowed down to 10.1% yoy in August. | ▪ Despite the weaker than expected headline growth, manufacturing activity remained resilient in August. Industrial production in manufacturing sector grew by 7.2% yoy in the first eight months, higher than 6.8% yoy growth in 2016. This is in line with the picture painted by improving PMI reported in the beginning of months, which rebounded from 51.4 to 51.7 in August. The resilient manufacturing probably benefited from still resilient global recovery story.<br>▪ However, as investment in manufacturing sector started to cool with fixed asset investment growth decelerated to 4.5% in the first eight month from 4.8% in the seven month, we think the strong activities in manufacturing sectors may not be sustainable, in particular when the impact of environmental inspection started to take effect gradually.<br>▪ Other than manufacturing sector, most economic activities slowed in August mainly due to tighter policy in local government funding, property as well as environmental protection.<br>▪ Infrastructure investment growth decelerated to 19.8% in the first eight month from 20.9% in the first seven month. The slowdown was the result of new regulation 50 and 87 to tighten regulation on local government debt issuance and financing activities to contain local government debt risk.<br>▪ On property, property sales by value decelerated to 12.7% in the first eight month from 14% in the first seven month while property investment grew by 7.9% yoy in the first eight month.<br>▪ In addition, the recent unprecedented tight environmental inspection, which closed down factories, also started to dampen private sentiment with private investment growth decelerated to 6.4% yoy in the first eight months from first half's 7.2% yoy.<br>▪ To conclude, we think the recent slowdown was mainly self-engineered as a result of tighter policy in local government financing, property and environmental policy. Although manufacturing sector remains the bright spot thanks to |

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| | resilient global recovery, we think it may not be sustainable due to rising raw material prices and negative impact of environmental inspection. Looking ahead, we expect China's growth to slow down further. |
| ▪ China's broad money supply M2 growth continued to decelerate to 8.9%, lowest in record, despite still strong loan growth.<br>▪ Aggregate social financing increased by more than expected CNY1.48 trillion while new Yuan loan also increased by more than expected CNY1.09 trillion. | ▪ For breakdown of new Yuan loan, loan demand from household sector remained strong while loan demand from corporate sector softened a bit. Medium to long term loan to household sector remained steady at CNY447 billion despite tighter property policy. Short term loan to household sector increased to CNY216 billion as banks shift their focus to promoting consumption loan after mortgage demand was capped by property policy.<br>▪ For breakdown of deposit, fiscal deposit fell by more than expected CNY390 billion in August, signalling easing fiscal policy. This justified why PBoC was reluctant to inject liquidity in its open market operation in August due to liquidity injection via easing fiscal policy.<br>▪ Net corporate bond issuance increased by CNY106.3 billon in August, recovering for the second consecutive month after sentiment over bond market stabilized. Entrusted loan fell by CNY8.2 billion in August due to tighter regulation on off balance sheet lending.<br>▪ Interesting to note, foreign currency deposit fell by US$7 billion in August, down for the first time since July 2016. This proved the unwind of long dollar positions during RMB appreciation. We expect foreign currency deposit to fall further in September. |
| ▪ China's foreign exchange purchase by central bank fell by CNY0.8 billion in August despite hopes that FX purchase may turn positive after RMB's rapid appreciation. | ▪ China's foreign exchange purchase by central bank has been falling for 22 consecutive months due to capital outflows. We think the consecutive outflow pressure may come to an end due to dissipating concerns about RMB depreciation. As such, we expect this data to return to positive in September.<br>▪ Market will look at FX settlement and sale data released by SAFE, due on Monday to gauge the picture of capital flows. |
| ▪ Macau's housing transactions fell for the second consecutive month by 15.7% mom to 771 deals in July. Meanwhile, average housing price decreased by 0.2% yoy in July, the first drop since September 2016. Furthermore, approved new mortgage loans for residents slid by 19.4% mom to MOP 3.82 billion. | ▪ As new cooling measures suppressed investment demand, the housing market appeared to have been calming. The effect of summer holiday also led to a quiet housing market. Furthermore, two typhoons might have hit domestic economy and hurt housing market sentiment. Therefore, we expect housing transactions will continue to retreat in the rest of 3Q. Nevertheless, gradual economic recovery is likely in the fourth quarter, during which there will be a raft of new home project launches (housing completions jumped by 1253% yoy during the first seven months). That said, we believe housing market will pick up some traction in 4Q. Average housing price is expected to grow by 0% to 5% yoy over 2017. |

| RMB | |
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| **Facts** | **OCBC Opinions** |
| ▪ RMB weakened significantly last week against the dollar after China unwound two macro prudential measures supporting RMB.<br>▪ Meanwhile, RMB index also retraced to below 95. | ▪ Clearly market has received the signal from China has been unease about recent pace of appreciation. As such, the USDCNY climbed back to around 6.55 from below 6.50 reading. However, we think all factors supporting RMB remained intact. Therefore, the upside for USDCNY may be |

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| | limited. |

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