Highlights:

China's economic recovery remains resilient in the first two months of 2017. The better than expected industrial production and fixed asset investment was mainly supported by three factors including reviving manufacturing sectors, strong infrastructure investment as well as improving private confidence. Surprisingly, property market was not a drag in the first two months due to increasing demand in the tier-3 and tier-4 cities.

China surprised the market again with a parallel increase in money market curve on Thursday, a few hours after the Fed rate hike. The increase of benchmark repo rate was designed to narrow the gap between official rate and market rate, which increased recently due to improving economic data as well as concerns about tighter monetary policy. The second money market rate hike within two months clearly shows that de-leverage is the main focus this year. Nevertheless, We think China will not in rush to hike benchmark lending and deposit rates any time soon given muted inflationary pressure as well as demand for economic stability prior to 19th Party Congress.

In addition, China's banking regulator further loosens the restriction on foreign banks' business in China. To comply with State Council's order to simplify administrative procedures, foreign banks are no longer required to gain prior approval from the CBRC for Treasury bond underwriting, wealth advisory and most custody businesses. Meanwhile, CBRC also encourages foreign banks in China to work with their parent companies overseas to provide financial services such as offshore bond issuance, IPOs and M&A to Chinese companies expanding overseas.

On currency, one of the most notable changes is the decline of RMB index to record low of 93.31 since PBoC launched the index in December 2015. Nevertheless, market reaction to the decline of RMB index has been muted so far. On the positive note, this suggested market has been more rational about RMB outlook. However, from policy perspective, we will continue to monitor RMB index this week to detect whether there is any potential policy shift.

Key Events and Market Talk	
Facts	**OCBC Opinions**
▪ China surprised the market again with a parallel increase in money market curve on Thursday, second time in 2017, after the Fed rate hike. ▪ 7-. 14- and 28-days reverse repo rate was raised by 10bps to 2.45%, 2.60% and 2.75%. ▪ In addition, PBoC also increased the interest rate for both 6-month and 1-year MLF rate by 10bps to 3.05% and 3.20% after injecting CNY303 billion via MLF.	▪ The increase of benchmark repo rate was designed to narrow the gap between official rate and market rate, which increased recently due to improving economic data as well as concerns about tighter monetary policy. ▪ The PBoC said in the press statement that the adjustment of money market rate is not considered as rate hike in China's context as the benchmark rate in China is lending and deposit rates. ▪ Having said that, the money market rate hike clearly shows that de-leverage is the main focus this year. ▪ Nevertheless, the CNY383 billion liquidity injection from both reverse repo and MLF suggests that PBoC tries to alleviate the impact of rate hike on the market via larger liquidity injection. This could be the new normal for this year that PBoC may strike balance between higher money market rates and generous liquidity injection. ▪ We think China will not in rush to hike benchmark lending and deposit rates any time soon given muted inflationary pressure as well as demand for economic stability prior to 19th Party Congress. ▪ As such, we see the limited impact of recent money market rate hike on the market. In fact, China's bond market gained on the day with 10-year bond futures went up by 0.66%.
▪ China's banking regulator further loosened the restriction on foreign banks' business in China.	▪ To comply with State Council's order to simplify administrative procedures, foreign banks are no longer required to gain prior approval from the CBRC for Treasury bond underwriting, wealth advisory and most custody businesses. ▪ In addition, CBRC also encourages foreign banks in China to work with their parent companies overseas to provide financial services such as offshore bond issuance, IPOs and

	M&A to Chinese companies expanding overseas.
▪ Beijing has been the 11th city to introduce additional property tightening measures since 1 March. ▪ The latest data from the National Bureau of Statistics shows that 10 out of 15 tier-1 cities and some hot tier-2 cities have reported a modest mom decline of new launch property prices in Feb. However, resale price continued to go up in most cities.	▪ Loan to value for the second purchase will be lowered to maximum 40% while the maximum loan tenure will be reduced to 25 years from previously 30 years. Meanwhile, the definition of second property was also recalibrated in a stricter context. ▪ It seems that Beijing has set the target to achieve zero percent growth for new launch prices.
▪ The USD/HKD 12-month forward points dropped to its lowest since Oct 2011 at -325 while the USD/HKD spot rate briefly rose beyond 7.77.	▪ The sharp decline of HKD swap points last week was due to speculation on the widening interest rate differential between USD and HKD due to flush HKD liquidity in HK's banking system. HK banking system's aggregate balance amounted to HKD259.6 billion. Combined with HKD964.1 billion of outstanding exchange fund bills and notes, the total amount reached about USD157.6 billion, outweighing the estimated inflows of USD130 billion since 2008. Therefore, the market believes that the rise in HIBOR will continue to lag as compared to the increase in USD LIBOR.
▪ Hang Seng China AH Premium Index dropped to 115.18 on Mar 16, the lowest since Dec 2014.	▪ The increased southbound inflows to H-shares via the two stock links have resulted in a smaller AH share premium since end of 2015. Hang Seng Mainland Properties Index rose by 29% so far this year as compared to a decline of 13% over 2016. Also, Hang Seng Chinese Enterprise Index closed at its highest since Aug 2015 on Mar 16. (1) Recent strength in the housing markets of the third and fourth tier cities, (2) a positive long-term prospect of Mainland housing market and (3) the attractive valuation of the developers' H-shares have been the major factors inducing onshore investors to tap HK stock market. However, with the AH share premium narrowing and housing cooling measures probably taking effect in 2H, we expect the flows to buy Mainland Developers' H-share may be unsustainable.
▪ Hong Kong: The number of eligible private homes on sale for the scheme offering 90% loan-to-value (LTV) ratio as decreased to below 1000. According to the Hong Kong Mortgage Corporation Limited, the number of new residential mortgage loans drawn down with an LTV ratio between 80% and 90% accounted for 29% of total applications during the first two months of 2017, compared with 36% over 2016.	▪ In Hong Kong, only the buyers of a private home priced at or below HKD4 million are eligible to apply for loans with 90% LTV ratio. With housing prices continuing to surge, the affordability of potential homebuyers is falling. Worse still, total household debt rose significantly by 79% during 2008 to 2016 and its share in GDP jumped from 51% in 2008 to 67% in 2016. Higher rates ahead mean household debt capacity is diminishing. We expect low-end housing demand to take a hit in 2H when banks are expected to raise the Prime Rate. However, the strong investment demand at home and from Mainland China may continue to drive up housing prices.

Key Economic News

Facts	OCBC Opinions
▪ China's economic recovery remains resilient in the first two months of 2017. ▪ Industrial production grew by 6.3% yoy in the first two months. ▪ Fixed asset investment accelerated to 8.9% yoy. ▪ However retails sales slowed to 9.5%.	▪ The latest growth data painted fairly rosy picture in China's manufacturing sectors, in line with recent strong PMI data. Industrial production in manufacturing sectors grew by 6.9% yoy in the first two months, offsetting the decline of mining outputs. In addition, the upgrade of value chain in manufacturing seems to be underway. For example, production of both general purpose equipment machinery and

	special purpose equipment machinery increased by 10.6% and 11.5% yoy respectively, highest since July 2014. Meanwhile, fixed asset investment in manufacturing sector also accelerated to 4.3% yoy. ▪ The stronger than expected fixed asset investment was mainly attributable to three factors including strong infrastructure investment, improving private sentiment as well as steady property market. Infrastructure investment grew by 27.3% yoy, highest in record. Private investment also re-accelerated to 6.7% yoy , highest since March 2016. Investment in property market accelerated to 8.9% yoy from 6.9% in 2016 despite cooling measures. The stronger investment was supported by property sales, which increased by 25.1% yoy. It seems there has been spill over effect from higher tier cities to lower tier cities. ▪ Retail sales unexpectedly slowed to 9.5% in the first two months, driven by the slowdown of car sales, which fell by 1% probably due to expiration of tax subsidy.
▪ China's financial institutions net purchased US$10.1 billion foreign currency on behalf of clients in Feb. ▪ Foreign exchange position in PBoC also fell by CNY58.1 billion in Feb.	▪ Both forex purchase data and financial institutions net purchase of foreign currency showed that there was a mild capital outflows in Feb. This is in contrast to the rebound of FX reserve, which was probably due to capital gain in reserve assets. ▪ Nevertheless, we do expect pressure on capital outflows to moderate due to more rational expectations on RMB exchange rate.
▪ HK's seasonally adjusted jobless rate held static at 3.3% in the three months through February.	▪ Specifically, the jobless rate in financing, insurance, real estate, professional and business services industry dipped to 2.2%. This was attributed to an improvement in the stock market and strong investment demand from Mainland China and the boom in property market. Besides, the unemployment rate in retail, accommodation and food services industry dropped to a one-year low at 4.8% due to rebound in the number of inbound tourists. As a result, the increase in the jobless rate of trade sector (2.9%) and construction sector (3.8%) was well offset. In the near term, recovery in the economy together with a tight labor supply may help to sustain the resilience in the labor market. However, an expected slowdown in China's growth in 2H and the looming global uncertainties are still likely to weigh.
▪ Macau's housing transactions dropped by 43.6% mom to 709 units in January while new residential mortgage loans approved tumbled by 16% mom to MOP3.5 billion. In the same month, average housing prices fell by 14% mom to MOP89,727/sqm.	▪ However, these three indicators all showed positive growth on yearly basis. Therefore, the monthly decreases may be attributed to seasonality while the housing market has been stabilizing on the back of economic recovery. Moving forward, housing market's outlook is rather mixed. Moderate economic recovery, stagnant wage growth, global uncertainties and higher interest rates may tame housing market sentiment. With home supply increasing, should the Fed raise rates at a faster pace and prompt Macau's banking system to lift the Prime Rate, we expect average housing prices to drop around 5% yoy in 2017. Demand for residential mortgage loans may also reduce as a result. On the flip side, the government will reclaim several undeveloped plots of lands which were granted to builders after the leases expire. This may slow down the increase in housing supply. A slower-than-expected rate hike pace by the Fed may also limit the downside of the housing market. If this is the case, a 3% to 5% annual growth

	in housing prices is forecasted.

RMB	
Facts	**OCBC Opinions**
▪ RMB ended the week little change against the dollar as dollar was sold off after less hawkish Fed rate hike. The USDCNY ended the week slightly above 6.90. ▪ However, RMB weakened against the currency basket with RMB index slipped to 93.31, lowest in record since China launched RMB index in December 2015.	▪ The sharp decline of RMB index to record low since the launch was a big surprise to us given China has kept RMB index stable around 94 for quite a while. ▪ Market reaction to the decline of RMB index has been muted so far. This suggested market is less panic about RMB outlook. ▪ We will continue to monitor the change of RMB index to detect whether there is any potential policy shift.

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