Highlights

US and China ended the trade talk over the weekend with no concrete deals despite the talk being described as "friendly and frank" by US Commerce Secretary Ross. China failed to obtain the commitment from the Washington to stop going ahead with its tariff threats which was unexpectedly revived last week ahead of the trade talk. In a unilateral statement, China said it will not comply with any deal if US decides to go ahead with tariff after 15 June. China's willingness to compromise in sectors such as agriculture and energy failed to please Trump Administration. The flip flop stance by Trump Administration on US-China trade talk suggested that there is no easy fix to this problem.

During Trump's Presidential campaign in early 2016, he mentioned that US as a nation must be unpredictable. Trump's unpredictability approach has rallied the animal spirits in the US, waking up China hawks. This may give US advantage in the near term in negotiation. Nevertheless, in the medium term, it is forcing China to take a hard approach. China may find new allies in trade after six non-US G7 members criticized the US protectionism stance. However, it is unlikely to help. Market will continue to watch out for how President Trump wants to play his unpredictability card, which will be the new normal for global diplomatic relationships. Road ahead is expected to remain bumpy.

On policy, China announced fresh measures to deepen its de-leverage campaign. The latest measure targets the syndicated loan to big companies, which will discourage bank's excessive credit exposure to large companies via syndicated loan. In addition, China's central bank announced to expand its scope of collateral for its medium term lending facility. We think the latest expansion is positive for market sentiment. However, it may also create confusion, which may downplay market expectation on reserve requirement ratio cut as the expansion of collateral seems meaningless if China continues to cut the RRR to swap MLF to reduce the total outstanding of MLFs. There is one similar motivation behind both non-relevant policy announcements on Friday which China wants to further support SMEs funding. We expect this will be the new feature

On market, China's equity market fell despite strong inflows under stock connect ahead of MSCI inclusion. Concerns about debt default in China weighed down both equity and currency market. It has been the second consecutive week for RMB to weaken against both dollar and currency basket. This suggested the recent RMB weakness is no longer only the function of the dollar movement.

In Hong Kong, HKD was immune from broad dollar's strength due to tight front-end liquidity around month-end. After month-end, liquidity will likely loosen again and drive USDHKD to test 7.85. As Xiaomi's IPO is said to be postponed to early July, front-end liquidity may not tighten until late June. However, following the quarter-end effect, a raft of liquidity draining events including mega IPOs and dividend payout flows will come into play successively. Therefore, we expect one-month HIBOR to tick up gradually after mid-June and test 1.5% in the coming months. On the other hand, total loan growth (+17.1% yoy in April) may slow down due to several factors, including high base effect, increased borrowing costs and cautious business sentiment amid higher market volatility and lingering US-China trade conflicts. Nonetheless, given sanguine economic outlook, loan demand is expected to stay stronger than saving needs. Therefore, HKD loan-to-deposit ratio (LDR) may remain elevated after reaching 84.1% (the highest since March 2014) in April. Given the elevated HKD LDR and the prospects for higher HKD interbank funding costs, banks may continue to fight for deposits with higher interest rate, in order to meet the strong loan demand. Elsewhere, in the run-up to MSCI's inclusion of A-shares from 1 June, northbound net inflows under two stock connects reached a record of RMB 54.4 billion in May. We will see whether the strong inflows could sustain. **In Macau,** GDP (+9.2% yoy in 1Q) marked the seventh consecutive quarter of positive growth. Strong external and internal demand could continue to support growth. However, we are wary of further slowdown in private investment amid successive completion of mega entertainment projects. Possible stock market correction could also weigh on local consumer sentiment. All in all, we hold onto our view that GDP will grow by around 7% yoy this year.

Key Events and Market Talk	
Facts	**OCBC Opinions**
▪ No settlement from the weekend trade talk between US Commerce Secretary Ross and Chinese Vice Premier Liu He. ▪ The trade tension escalated again after the White House said last week it will move forward with the additional tariff on US$50 billion Chinese goods.	▪ The flip flop stance by Trump Administration on US-China trade talk suggested that there is no easy fix to this problem. ▪ At the current stage, there is still lack of details about reason of flip flop. But it is probably the result of internal disputes among Trump's key trade advisors. For example, the media reported that Peter Navarro criticized Treasury Secretary Mnuchin saying his remark is sound bite. But on top of that, we think the return of hawkish comments on trade may also be related to the upcoming North Korea summit. We have seen the similar flip

	flop in this summit, which may still take place on 12 June, three days ahead of US's decision to unveil the lists. So Trump may use trade talk as the tool to push China to influence Kim Jung En to compromise. ▪ The flip flop may hurt US's credibility to some extent. But it may also be Trump's tactics. During Trump's Presidential campaign in early 2016, he mentioned that US as a nation must be unpredictable. It seems that he is using this unpredictable approach quite well. So that's probably the new normal we should be adaptable to. ▪ Trump's unpredictability approach has rallied the animal spirits in the US, waking up China hawks. The recent ZTE case is a good example. The US Congress is planning to ban the firm from the US market despite Trump softened his tone. The animal spirit is up, which may give US advantage in the near term in negotiation. Nevertheless, in the medium term, it is forcing China to take a hard approach. So, I guess the road ahead remains very bumpy. The risk of a trade war still cannot be ruled out. ▪ Next, we will see whether the unilateral tariff on Chinese tech products may violate WTO rules. Under the WTO information technology agreement, participants are committed to eliminate tariffs on IT products covered by the Agreement.
▪ The European Commission filed legal proceedings with the WTO against China's legislation to undermine intellectual property rights of EU companies.	▪ Although China may stand in the same line with the EU to fight the rising protectionism in the US. EU's latest WTO dispute with China showed that China will probably still depend on itself to walk out of the woods.
▪ China's banking and insurance regulator unveiled the new rules last week to tighten its regulation on syndicated loan as part of China's de-leverage campaign. ▪ The new rule will discourage bank's excessive credit exposure to large companies via syndicated loan. ▪ A syndicated loan mechanism will be setup for companies with outstanding credit above CNY5 billion from 3 and more banks to monitor the credit risk.	▪ The new syndicated loan monitoring system mainly targeted at medium and large companies, which is in line with government's target to contain leverage ratio in local government and SOEs sectors. This will eventually support China's de-leverage commitment. ▪ In addition, by capping the credit exposure to large companies, the regulator also hopes to free more credit quota to support SMEs. Nevertheless, it remains to be seen whether banks are willing to redistribute credit line to SMEs from SOEs due to different risk appetite. ▪ In general, we consider this as tight credit policy which may further slowdown the loan growth.
▪ China's central bank announced to expand its scope of collateral for its medium term lending facility. ▪ In addition to government bonds, policy bank bonds, AAA rated credit bonds and local government bonds, AA rated small and micro companies bond, green bond, agriculture bond as well as credit bonds will be included. Meanwhile, high grade small and micro business loan and green loan will also be considered as collateral.	▪ The expansion of collateral scope for MLF was mainly attributed to three reasons. First, it will address the concern about short of qualified collateral for MLF. Second, by accepting business loans to small and micro companies and environmental protection related projects as collateral, it will encourage banks to support SMEs funding needs, which is in line with government's direction. Third, it may also stabilize the weak sentiment in China's credit market. ▪ We think the latest expansion is positive for market sentiment. However, it may also create confusion. The latest move may downplay market expectation on reserve requirement ratio cut as the expansion of collateral seems meaningless if China continues to cut the RRR to swap MLF to reduce the total outstanding of MLFs.
▪ Northbound net inflows under two stock connects totaled RMB 54.4 billion in May, the strongest since the launch of Shanghai-Hong Kong stock connect in Nov 2014. This might have been mainly due to the	▪ In anticipation of increasing demand for RMB for A-shares investment, combined with month-end effect, offshore RMB liquidity tightened last week. Overnight CNH HIBOR jumped from 2.97% on 28 May to 6.07% on 31 May. As a result, CNH was

prepositioning of active funds in the run-up to MSCI's inclusion of A-shares from 1 June.	slightly stronger than its onshore counterpart. Moving forward, given the PBOC's efforts to increase offshore RMB liquidity, the volatility of liquidity condition is expected to reduce.
▪ According to the statement of Hong Kong Exchanges & Clearing (HKEX), the HKEX will launch MSCI Asia ex-Japan futures on 11 June. This will be the first regional stock index futures launched in HK. The underlying index comprises of shares of US-listed Mainland companies and those of HK and some other Asia markets.	▪ This will allow investors in Hong Kong to get more exposure to the global equity market in a more efficient way. Meanwhile, it may pave way for the HKEX to launch other global stock index futures. With MSCI including A-shares in its emerging market index from 1 June, the HKEX may also launch MSCI emerging market futures, in order to deepen the development of HK's equity futures market and increase the opportunities for investors to manage risks and diversify their portfolios.
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Key Economic News	
Facts	**OCBC Opinions**
▪ China's official PMI rebounded in May to 51.9 from 51.4 in April supported by the improvement of demand and production.	▪ Both new export orders and new orders improved to 51.2 and 53.8 from 50.7 and 52.9 respectively. Production recovered to 54.1 from 53.1 probably due to the restart of production in Spring. Purchasing price index also recovered to 56.7 from 53, a sign that China's producer prices index may have bottomed out. We expect China's PPI to rebound to about 3.7% in May from 3.4% in April. The latest PMI data show that the US-China trade tension has limited impact on China's growth at the current stage.
▪ HK's exports and imports remained strong in April and were up by 8.1% yoy and 11.1% yoy respectively.	▪ By major trading partners, imports from Mainland China, Taiwan, Japan and the US increased by 9.6%, 23.8%, 10.5% and 1.2% on a yearly basis respectively. Exports to Mainland China and the US surged by 12.9% yoy and 11.7% respectively. HK's rosy trade data could serve as an indicator of strong external demand since HK is the major re-export port connecting China and the rest of the world. However, April's data could also be distorted by the front-loading of trade activities in anticipation of potential tariff charged by the US from early June. Recently, US-China trade tensions escalated again with Trump planning to lift tariffs on Chinese imports. Therefore, we will closely watch the trade talk between the two countries. If two countries fail to reach an agreement on details, the lingering trade conflict may finally take its toll on HK's trade activities.
▪ HK's total loans and advances increased notably by 17.1% yoy in April. However, the data was distorted by the large IPO in late April.	▪ Specifically, loans for use in HK (excluding trade finance), which accounted for 65% of total loans and advances, increased notably by 19.4% yoy mainly due to strong demand for IPO loans. In addition, trade finance growth remained strong at 11.8% yoy as trade activities have been supported by sanguine external demand. Moving forward, local loans growth may slow down due to high base effect and cautious business sentiment on high market volatility and lingering US-China trade conflicts. Besides, with HKD funding costs trending higher, banks have lifted mortgage rates and are set to kick off prime rate hike cycle around mid-2018. This could weigh down mortgage loan demand (-5.6% mom in Apr 2018). ▪ On the other hand, the growth of loans for use outside of Hong Kong has decelerated for the fifth consecutive month from 20.8% yoy in Nov 2017 to 13.2% yoy in Apr 2018. This was mainly due to expectations for looser liquidity in the aftermath of the targeted RRR cut from late Apr 2018. Moving forward,

	with offshore funding costs ticking up while onshore liquidity condition stabilizing, we expect Mainland companies' needs of overseas financing will reduce slightly. Curbs on irrational overseas expansion of Mainland companies could also weigh on the corresponding loan demand. ▪ Elsewhere, HKD loan-to-deposit ratio rose to 84.1%, the highest level since Mar 2014, as HKD loan growth (+25.9% yoy) outpaced HKD deposit growth (+13.7% yoy). We expect HKD loan-to-deposit ratio will remain elevated due to sanguine economic outlook. Adding that HIBOR will likely tick up gradually in the coming months, banks may continue to compete for deposits with higher interest rate.
▪ HK's retail sales registered double-digit annual growth for the third consecutive month and were up 12.3% yoy in April. The revival of tourism activities as well as upbeat local consumer sentiment are the two main drivers of retail sector's recovery.	▪ Specifically, sales of jewelry, watch and other luxurious goods jumped 24.6% yoy. Sales of medicines and cosmetics and those of clothing, footwear and allied products surged 17.9% yoy and 6.7% yoy respectively. This reflects the improved tourism activities. Sustained growth across Asia especially China has supported HK's inbound tourism. A weaker HKD against major currencies, in the meantime, boosted visitors' purchasing power. On the other hand, the sales of consumer durable goods climbed 15.3% yoy and those of goods in department stores also rose 12.6% yoy. This might have been resulted from sanguine local consumer sentiment. With unemployment rate falling to an over twenty-year low and economic outlook remaining positive, expectations for faster wage growth could continue to encourage households to increase spending. All in all, we expect retail sector to remain elevated in the coming months. However, any correction in the stock market and housing market amid rate hikes in 2H 2018 could weigh on consumer sentiment. We hold onto our view that retail sales will increase by 5%-8% in 2018.
▪ Macau's GDP advanced 9.2% yoy in 1Q 2018, marking the seventh consecutive quarter of positive growth amid strong external and internal demand.	▪ Externally, exports of gaming services and other tourism services increased by 16.5% yoy and 19.6% yoy respectively. With the government striving to diversify the economy away from overreliance on gaming, the resultant increase in non-gaming elements has boosted the tourism sector and allowed recent economic recovery to be more solid than the past. Asia's resilient growth and a weaker MOP have also lent supports to the tourism activities. As a result, gross gaming revenue grew 20.5% yoy in 1Q 2018. Meanwhile, total visitor arrivals increased 8.6% yoy while total spending of visitors climbed 22% yoy in 1Q 2018. ▪ Internally, private consumption grew at the fastest pace since 1Q 2015 by 4.8% yoy, mainly attributed to positive earnings prospects. Given the strong performance of gaming and tourism activities, hiring sentiments remained upbeat and allowed unemployment rate to stay low at 1.9%. Also, tight labor market translated into wage inflation with median monthly employment earnings rising for the second straight quarter by 6.67% yoy in 1Q 2018. Besides, government investment in fixed assets jumped by 132.5% yoy as a slew of infrastructure projects are under construction. In contrast, successive completion of mega entertainment projects has led to a 21.1% decline in private construction investment. ▪ Moving forward, we expect sustained global growth and a weaker MOP will continue to support Macau's exports of goods and services. Also, the upcoming completion of new mega entertainment projects and the Hong Kong-Zhuhai-Macau Bridge

	could provide more impetus for the tourism and the gaming sector (gaming revenue grew 19.4% yoy during Apr and May). As such, positive economic outlook could boost wage growth as well as private consumption. Besides, infrastructure investment is likely to hold up well on the back of fiscal stimulus. Nevertheless, we are wary of further slowdown in private investment. Any correction in the stock market in 2H 2018 could also weigh on local consumer sentiment. All in all, we hold onto our view that GDP will grow by around 7% yoy this year.
▪ Macau's unemployment rate remained unchanged at 1.9% over the three months through Apr 2018. The total labor force climbed to 388,900, the highest since 3Q 2017. Total employed population also rose to 381,500, the strongest since the three months through Aug 2017.	▪ By industry, the employment of construction industry surged by 6.3% mom given a slew of infrastructure projects and mega entertainment projects under construction. The employment of hotel, restaurants and similar activities and that of retail sector picked up by 2.14% mom and 1.8% mom respectively, supported by buoyant tourism activities. In contrast, the employment of gaming sector dropped by 2% mom as policy risks might have suppressed hiring demand. Moving forward, the labor market is likely to remain tight given the sanguine economic outlook. As such, employers may be propelled to increase wage at a faster pace. This will likely boost private consumption and housing demand.

RMB	
Facts	**OCBC Opinions**
▪ The USDCNY broke 6.40 riding on the strong broad dollar after the DXY tested 95 last week. RMB index softened also to 92.33	▪ It has been the second consecutive week for RMB to weaken against both dollar and currency basket. This suggested the recent RMB weakness is no longer only the function of the dollar movement. ▪ The weakness was probably due to two reasons including concerns about credit risk and uncertainty about the trade outlook.

OCBC Greater China research
Tommy Xie Xied@ocbc.com
Carie Li Carierli@ocbcwh.com

Co.Reg.no.:193200032W