Highlights

The tit-for-tat trade spat between US and China continued but on a smaller scale. US launched anti-dumping investigation on steel wheel from China after China's Commerce Department announced to impose a 178.6% tariff on sorghum imports from the US. However, it seems that the tension has no longer been restricted to trade area after the US stepped up to target China's high-tech companies and investment. **This means that the tension may enter the unchartered territory.**

The impact of 7-year denial of export privileges on Chinese telecommunications equipment and systems company ZTE is material as ZTE is likely to miss its shipment without the chipsets from the US suppliers. It is a wakeup call to some Chinese netizens, who may be over confident about China's technology. This may transform the hawkish sentiment fuelled by overconfidence to a more realistic assessment. In addition, the talk of 1977 emergency economic power act to grant President Trump more power to block China's investment as well as the report on "Supply Chain Vulnerabilities from China in US Federal Information and Communications Technology" showed that a persistent conflict between US and China in terms of technology investment may continue to dominate the headline in future although the news about US Treasury Secretary Mnuchin's possible visit to China may help ease the tension in the near term. Market is also waiting for the USTR to announce additional list of US$100 billion imports from China subject to tariff, which may mainly target at China's consumer goods.

Domestically, China's solid 1Q GDP took a backseat, overshadowed by ZTE news as well as targeted RRR cut. Although the headline GDP shows that the Chinese economy remains resilient in the first quarter, the underlying components show that the economy may slow down gradually in the coming quarters. The deceleration of infrastructure investment together with decline of off-balance sheet lending and higher funding cost are likely to weigh down on China's growth outlook, which is expected to slow down to around 6.5% in 2018.

China's bond market rallied last week fuelled by innovative reserve requirement ratio cut with debt swap feature to replace the medium term lending facility. The carefully designed RRR cut shows that China is unlikely to deviate from the path of prudent monetary policy though the cut also reinforced the consensus that China is unlikely to tighten further. On currency, the RRR cut has limited impact on RMB though liquidity injection usually is negative for currency. RMB spiked last Thursday following SAFE spokeswoman's comments on weaker dollar. Nevertheless, given RMB fixing has been persistently weaker than market consensus for the past week, it showed that China may want to cap the pace of RMB depreciation. However, the re-emerging expectation that China may eventually compromise after the US opened a new front on high-tech investment may continue to press RMB to appreciate in the near term.

In **Hong Kong,** the HKMA has intervened consecutively since April 12 and reduced the aggregate balance to HK$128.5 billion. Given a 30% reduction in aggregate balance, the month-end effect and Ping An Good Doctor's IPO, concerns about a tighter liquidity condition propelled short HKD traders to take profit in advance and strengthened the HKD. As we expect USD/HKD to stay below 7.85 before month-end, the HKMA may take a breather at this juncture. After month-end, USD/HKD may tick up again towards 7.85 and prompt renewed intervention by the HKMA. However, till mid-2018, 1) a further reduction in aggregate balance, 2) dividend payment flows, 3) potential large IPOs (like Xiaomi, Ant Financial, Grail Inc.,), 4) quarter-end effect and 5) possible June rate hike by the Fed together could push up HIBOR gradually and narrow its gap with its US counterpart. As a result, short HKD traders may become more cautious and allow HKD to rally again. We believe that aggregate balance will reduce gradually and stabilize between HK$80 billion and HK$100 billion before mid-2018. Nevertheless, we do not expect HKD to strengthen to the strong side (7.75-7.80) until synchronized global monetary tightening triggers faster capital outflows and helps to close the yield differential. In Macau, mass-market segment's revenue grew 20.1% yoy in 1Q 2018 while its share in total revenue rose slightly to 38.9%. Asia's resilient growth, a weak MOP, infrastructure improvement and a new wave of hotel openings will likely provide more impetus for the tourism sector as well as the mass-market segment.

Key Events and Market Talk	
Facts	**OCBC Opinions**
▪ The US Commerce Department triggered a 7-year denial of export privileges on Chinese telecommunications equipment and systems company ZTE, which was agreed in March 2017 after the company was caught by illegally exporting US technology to Iran and North Korea. ▪ The denial of export privilege will ban US companies from exporting to ZTE. In addition, the UK government also issued warning to UK phone	▪ On company level, the ban is material as ZTE is likely to miss its shipment without the chipsets from the US companies, which may have significant impact on company's profit. ▪ From macro perspective, the recent move may be a blow to China's 5G ambition as ZTE is one of the key players leading 5G innovation. Meanwhile, it may also create fresh concern that the US government may open new front to confront with China to extend the recent bilateral trade tensions. ▪ In reaction, China's Commerce Ministry said it will closely

carriers not to use ZTE's equipment and services.	monitor the situation and will be prepared to take action to protect the interests of Chinese firms. China's reaction is likely to be closely monitored to see whether the incident may trigger fresh round of escalation on trade tension which cooled down slightly last week.
▪ The tit-for-tat trade spat between US and China continued on a small scale. ▪ China's Commerce Department announced to impose a 178.6% tariff on sorghum imports from the US effective from 18 Apr. ▪ In addition, US launched anti-dumping investigation on steel wheel from China while China announced temporary anti-dumping measures on synthetic rubber imports from US, EU and Singapore.	▪ Although there was no major headline about the US-China trade tension last week, the launch of anti-dumping investigation cases by both sides show that risk of further escalation cannot be ruled out. ▪ China's Commerce Department spokesman said in its regular press conference last Thursday that there are no bilateral negations yet between US and China on proposed tariff under section 301 investigations. ▪ Market is waiting for the USTR to announce additional list of US$100 billion imports from China subject to tariff, which may mainly target at China's consumer goods. ▪ Lack of development on bilateral negotiations as well as China's reiteration on fighting to the end shows that the risk still cannot be ruled out.
▪ The US Treasury department is reported to consider ways to restrict Chinese investment by invoking the 1977 emergency economic powers law.	▪ The 1977 law will give President Trump power to block transactions and seize assets should the President declare a national emergency. The law has been widely used after 911 attack to block the assets from terrorist organizations. The media report also fuelled concerns that whether the US is able to seize China's assets in the US such as US Treasury holdings in the worst-case scenario. Nevertheless, we think the seize of China's US Treasury holdings is unlikely at the current stage.
▪ The US-China Economic and Security Review Commission unveiled the report on Supply Chain Vulnerabilities from China in US Federal Information and Communications Technology last week.	▪ This paper clearly lays the foundation to highlight China's risks to US national and economic security as cyber attacks on supply chain will become easier due to rising avenues for attack under 5G and Internet of Things. ▪ The report suggests a persistent conflict between US and China is likely after the report accused China's top tech companies such as Huawei, Zhongxing and Lenovo of linking to state-led cyberespionage efforts.
▪ In its press conference last week, China's currency regulator SAFE spokeswoman said local government funding vehicles and property companies are not allowed to borrow foreign debt except special condition. Meanwhile, the sale of foreign currency from foreign debt by banks and securities firm need to obtain approval from the SAFE.	▪ As China's capital flow has returned to neutral, encouraging capital inflows is not longer the top priority for China's currency regulator. Instead, containing financial risk again top the priority list. The increase of foreign debt last year rang the bell. ▪ China's property developer has rushed to the offshore market to tap the offshore dollar bond market. Nevertheless, the supply is likely to shrink with the new rule in place.
▪ PBoC announced to cut reserve requirement ratio for most Chinese banks by 1% effective from 25 April. Only those small rural commercial banks with already low RRR will not be affected. RRR for big commercial banks will be lowered to 16% from 17%. ▪ The RRR cut will unfreeze about CNY1.3 trillion according to the PBoC estimation. However, CNY900 billion out of CNY1.3 trillion will be used to pay off the existing Medium-term lending facility (MLF). As such, the net liquidity injection is about CNY400 billion.	▪ The RRR cut is close to a universal cut, which will unfreeze about CNY1.3 trillion. However, CNY900 billion out of CNY1.3 trillion will be used to pay off the existing Medium-term lending facility (MLF). As such, the net liquidity injection is about CNY400 billion. ▪ The RRR cut with innovative debt swap feature to replace the MLF shows that China is unlikely to deviate from the path of prudent monetary policy. Nevertheless, the cut reinforced the consensus that China is unlikely to tighten further. ▪ It is supportive of risk sentiment as banks profit is expected to improve with lower funding costs. ▪ The RRR cut will unfreeze more liquidity for those smaller banks with no direct access to the central bank liquidity facility, which may in turn better support the funding demand from SMEs. ▪ The RRR cut will also play a pre-emptive role in stabilizing

	China's credit expansion to ease the tighter monetary condition. More cuts with similar feature may come.
▪ The HKMA has intervened consecutively since April 12 and reduced the aggregate balance to HK$128.5 billion. This pushes the HIBOR curve upwards. 12-month USD/HKD forward points also narrowed gradually from -630 (April 12) to around -435. More notably, 1-year HKD Interest Rate Swap edged up steadily from 1.67% (April 12) to 1.92%. ▪ On April 19, USD/HKD spot rate edged down from the weak end of 7.85 to a one-month low of 7.8441 while 3-month HIBOR also rose to a more than nine-year high of 1.337%.	▪ Given a 30% reduction in aggregate balance, the month-end effect and Ping An Good Doctor's IPO, concerns about a tighter liquidity condition propelled short HKD traders to take profit in advance and strengthened the HKD. As we expect USD/HKD to stay below 7.85 before month-end, the HKMA may take a breather at this juncture. ▪ After month-end, USD/HKD may tick up again towards 7.85 and prompt renewed intervention by the HKMA. However, till mid-2018, 1) a further reduction in aggregate balance, 2) dividend payment flows, 3) potential large IPOs (like Xiaomi, Ant Financial, Grail Inc.,), 4) quarter-end effect and 5) possible June rate hike by the Fed together could push up HIBOR gradually and narrow its gap with its US counterpart. As a result, short HKD traders may become more cautious and allow HKD to rally again. We believe that aggregate balance will reduce gradually and stabilize between HK$80 billion and HK$100 billion before mid-2018. ▪ After mid-2018, a further reduction in aggregate balance is possible, should more US treasury bond issuance and Fed's faster tightening cause LIBOR's increase to reaccelerate and the interest rate gap to widen again. When aggregate balance reduces further to around HK$50 billion and the yield differential narrows to about 50bps, carry trade activities are expected to reduce substantially. All in all, we expect USD/HKD will retreat to 7.83 by end of this year. Nevertheless, we do not expect HKD to strengthen to the strong side (7.75-7.80) until synchronized global monetary tightening triggers faster capital outflows and helps to close the yield differential.
▪ Southbound equity flows have exhibited net outflows for five consecutive trading days since 12 April. Taking northbound equity flows into account, we found that over RMB35 billion has flown into Mainland China from HK under the stock connect programs since the start of April. This represents the largest net equity outflows from HK to China since November 2014 when Shanghai-Hong Kong stock connect was launched.	▪ The robust northbound equity inflows might have been due to bottom fishing as well as the upbeat sentiment in the run-up to the inclusion of A-shares in MSCI emerging market index. A stable RMB also helped to increase the attractiveness of RMB assets. Furthermore, the PBOC's targeted RRR cut and continuous injection of liquidity to banking system also boded well for the onshore equity market. As a result, Mainland investors might have preferred onshore market over HK market and resulted in net equity outflows from HK. Moving forward, the daily quota for stock connect programs will be expanded starting May 1. Whether this will increase capital outflow from HK to China will be closely watched.

Key Economic News	
Facts	**OCBC Opinions**
▪ The Chinese economy decelerated slightly to 6.8% yoy in 1Q from 6.9% yoy in 2017, but still well above government's target of around 6.5% yoy. ▪ Fixed asset investment decelerated to 7.5% yoy in the first quarter from 7.9% in the first two months. ▪ Industrial production also slowed down to 6% yoy in March. ▪ Retail sales, however, rebounded to 10.1% yoy in March from 9.4% yoy.	▪ Although the headline GDP shows that the Chinese economy remains resilient in the first quarter, the underlying component shows that the economy may slow down gradually in the coming quarters. Infrastructure investment decelerated notably to 13% in 1Q 2018 from 19% in 2017 as a result of tightening on local government financing as part of China's structural deleverage campaign to contain the financial risk. The deceleration of infrastructure investment together with decline of off-balance sheet lending and higher funding cost are likely to weigh down on China's growth outlook. We expect China's growth to slow down to around 6.5% in 2018.

▪ China's capital flow remains largely balanced in March. China's central bank net purchase CNY7.84 billion worth of foreign currency. However, the sale of foreign exchange by banks on behalf of clients recorded a small deficit at US$2.61 billion.	▪ On the positive note, the sale of dollar forward rose significantly to US$23.66 billion, close to long dollar forward position. The relatively balance forward position shows that the divergent opinion on RMB outlook. This will be the foundation for RMB's two-way movement.
▪ HK's Unemployment rate stayed at a two-decade low of 2.9% in 1Q 2018.	▪ Supported by further economic recovery of Asian countries and a weaker HKD, tourism related industries showed further improvement in its employment with its jobless rate unchanged at a three-year low of 4.2%. In contrast, as the conflict between US and China flared up and exerted further uncertainties on the HK's trade outlook, the jobless rate of trade sector rose slightly to 2.4% from 2.3%. Meanwhile, the unemployment rate of financial sector increased from 1.9% to 2.1%, mainly driven by the asset market fluctuations in 1Q which harmed the hiring sentiments of financial industries. Moving forward, we are still wary of US-China trade tension and slowing manufacturing activities of the globe as both could weigh on HK's trade sector and its overall economy, in turn taking a toll on the labor market. In addition, given high volatility of the asset markets and potential housing market correction amid prospects for higher interest rates, the financial sector and its employment could also take a hit. Therefore, we expect unemployment rate to increase in the coming months.
▪ Macau's gaming revenue rose 21% yoy to MOP76.5 billion in 1Q 2018.	▪ By segment, VIP gaming revenue expanded 21% yoy with its share in total gaming revenue stabilizing at 56.1%. As junket operators continued to extend credits to high rollers and held events after the Lunar New Year to lure VIP gamblers, VIP segment remained supported. On the other hand, mass-market segment's revenue grew 20.1% yoy while its share in total revenue rose slightly to 38.9%. Asia's resilient growth, a weak MOP, new hotel opening as well as the effect of Lunar New Year Holiday have been the major factors bolstering tourism activities and mass-market segment. Moving forward, we remain wary of the sustainability of VIP segment's remarkable increase given lingering policy risks. Prospects for higher interest rates may also impede junket operator from lending to rich gamblers. In contrast, infrastructure improvement and a new wave of hotel openings will likely provide more impetus for the tourism sector as well as the mass-market segment. Nevertheless, gaming growth driven by mass-market could be moderate as compared to that led by VIP demand. Adding on high base effect, we hold onto our view that total gaming revenue growth will slow to 10%-15% in 2018.

RMB

Facts	OCBC Opinions
▪ RMB jumped against the dollar on Thursday in reaction to China's currency regulator spokeswoman's comments on weaker dollar.	▪ On currency, the RRR cut has limited impact on RMB though liquidity injection usually is negative for currency. Nevertheless, given RMB fixing has been persistently weaker than market consensus for the past week, it showed that China may want to cap the pace of RMB depreciation. However, the re-emerging expectation that China may eventually compromise after the US opened a new front on high-tech investment may continue to press RMB to appreciate in the near term.

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