Highlights

No last-minute de-escalation as someone hopes. New tariff took effect on Sunday. Nevertheless, the improvement of market sentiment last week was not the result of pray for last-minute miracle but the official confirmation by China side that the door for negotiation remains open and China is likely to send their trade delegation to US sometime in September to meet its counterparty in person.

President Trump's quotation on weaker Yuan help alleviate impact of tariff on US consumers in reaction to the new tariff is a bit awkward as it deviates from his previous criticism of RMB's depreciation. We think it probably may not be his endorsement on weaker Yuan. Nevertheless, it may send the signal to market that Trump may flipflop his currency view.

RMB has been kept in a narrow range last week after the USDCNY fixing has been set at 7.08 range for four consecutive days. The key focus this morning will be whether China will allow the USDCNY fixing to be set above 7.10 after new tariff took effect on Sunday. The pair may test 7.20 should the fixing break 7.10.

China's manufacturing sector continued to soften. Although there is no new fresh stimulus announced by China's financial stability committee meeting over the weekend, China did roll over new 20 measures targeting at consumption such as promoting car sales and purchase of environmental friendly electronic products. China's stimulus to boost consumption rather than direct prime-pump may have limited spill over effect on the regional economies.

In **Hong Kong**, July's economic indicators reveal that the economy felt pain from the double whammy of trade war and heightened political uncertainty. **On the trade sector front**, exports and imports dropped for the ninth and eighth consecutive month respectively in July. With trade war re-escalating in September and to further weigh down external demand and Asia's electronic value chain, combined with a strong HKD and high base effect, HK's exports may continue to drop in the coming months. On the other hand, with trade war and social unrest clouding the domestic growth outlook and weakening consumption sentiments, imports may stay sluggish. In a nutshell, we expect both exports and imports to show single-digit negative growth over 2019. **On the retail sector front**, retail sales dropped at a fastest pace since February 2016 by 11.4% yoy in July as tourist spending weakened further on heightened political uncertainty, a stronger HKD, trade war fears and Asia's economic slowdown. Meanwhile, local consumption softened amid the negative wealth effect from stock and housing market correction, increasing concerns about retrenchment and the ongoing protests which disrupted the normal operation of shops and deterred local consumers from going out. Going forward, we expect the decline in retail sales to worsen in August. Should protests prolong and trade war escalate further in the rest of this year, retail sales may drop by 10% over 2019. **In financial sector**, the stable HKD deposits (0% mom in July), aggregate balance and USDHKD spot together suggest no massive outflows so far. However, the downside of HKD rates may be capped by the upcoming quarter-end, potential large IPO and lingering concerns about capital outflow risks. As such, commercial banks may continue to face relatively high funding pressure and refrain from lowering the prime rate any time soon.

<table>
<tr><th colspan="2">Key Events and Market Talk</th></tr>
<tr><th>Facts</th><th>OCBC Opinions</th></tr>
<tr><td>

The new round of tariff imposed by both US and China took effect on Sunday as previously planned.
President Trump said in Twitter on Sunday quoting one economist that tariff will not impact the US consumers that much as the depreciation of Chinese currency gives US importers a discount.
There is no personal contact between two Presidents over the weekend. However, effective communication between trade teams remains as confirmed by both China's foreign ministry and President Trump last week.

</td><td>

No last-minute de-escalation as someone hopes. Nevertheless, the improvement of market sentiment last week was not the result of pray for last-minute miracle but the official confirmation by China side that the door for negotiation remains open and China is likely to send their trade delegation to US sometime in September to meet its counterparty face-to-face.
Nevertheless, given China has entered its last-month of preparation for big National Day Parade on 1 Oct, we think the chance of breakthrough is unlikely within the next 30 days.
President Trump's quotation on weaker Yuan help alleviate impact of tariff on US consumers is a bit awkward as it deviates from his previous criticism of RMB's depreciation. We think it probably may not be his endorsement on weaker Yuan. Nevertheless, it may send the signal to market that Trump may flipflop his currency view.

</td></tr>
</table>

▪ China's State Council unveiled 20 measures to stabilize consumption expectation and boost confidence in consumption led by promoting car sales and purchase of environmental friendly electronic products. ▪ Meanwhile, the State Council also announced it will guide the fiscal money to support consumption.	▪ China's retail sales growth decelerated further this year partially due to the weak car sales. Given car sale has been the largest single sales item, accounting for 29% of total retail sales in 2018, promoting car sales is probably the easiest way to unlock the consumption potential. According to the State Council, China will gradually ease or remove the restriction on car sales. Meanwhile, it also encourages local government to support the sales of new energy cars. Nevertheless, given the funding constraints of local governments, it remains to be seen how local governments can support the new energy car sector. ▪ Other than direct support to car sales, the State Council also announced to authorize local municipal governments to approve the retail sales of petrol and gas. China also plans to build more petrol stations in rural areas to boost the consumption of petrol. This will also indirectly support the car sales. ▪ In addition, China will also encourage consumers to swap their old electronic products with new energy saving electronic products to boost consumption. ▪ Meanwhile, China also encourages exporters to sell their products domestically. This will also help counter the impact from the trade war.
▪ China's financial stability committee concluded its latest meeting over the weekend. The meeting reiterated the prudent monetary policy but will put fiscal policy, monetary policy and financial policy together to work together to support the growth. ▪ In addition, the committee said it will deepen the reform of capital market to attract longer term investors.	▪ There was no new message from the latest committee meeting. China is likely to continue to leverage on current toolboxes to support the growth.
▪ According to the PBOC's statement, the PBOC's Governor Yi Gang talked with HKMA's CE Norman Chan during the Executives' Meeting of East Asia Pacific Central Banks. They exchanged views on financial cooperation in the Greater Bay Area (GBA).	▪ According to the GBA development Plan, banks in the bay area will launch cross-border RMB interbank lending, RMB spot, forward and other derivative products as well as wealth management products. Meanwhile, enterprises in the bay area will issue cross-boundary RMB bonds. Taken all together, it reinforces that HK will help to push forward RMB internationalization. ▪ Besides, the scope will be widened and the channels will be expanded for cross-border investment between HK and Mainland China. Both HK and Mainland China will also promote cross-border transactions of financial products such as funds and insurance. First, the launch of wealth management connect, ETF connect, etc could be expected to support China's capital account liberalization. Second, HK will allow China's expanding middle-class and the growing high-net-worth individuals to diversify asset allocation and hedge relevant risks. Third, with foreign investors increasing their holdings of A-shares and onshore bonds, they may also need to hedge related FX and interest rate risk in HK. Fourth, with HK citizens allowed to open onshore bank account via offshore banks, it may pave way for further financial integration across the border.

Key Economic News

Facts	OCBC Opinions
▪ China's official PMI slipped to 49.5 in August from 49.7 in July, below 50 for the fourth consecutive months. ▪ PMI for large and medium sized companies fell further while PMI for small companies rebounded slightly.	▪ On demand side, new order fell to 49.7 from 49.8. However, new export orders rebounded slightly to 47.2 from 46.9 despite the escalation of trade war in August. ▪ Production was largely unaffected by trade war at 51.9 in August. ▪ Purchasing price index fell to 48.6, lowest since January. This implies that China's PPI to remain weak in August. The lower cost is positive form companies' profit. ▪ Employment index fell to 46.9 from 47.1. The re-escalation of trade war is likely to weigh down on the job market in manufacturing sectors. Noting that China's surveyed unemployment rate rose to 5.3% in July.
▪ Hong Kong's total loans and advances continued to grow moderately by 3.6% yoy in July.	▪ Internally, trade finance dropped for the 11th consecutive month and was down by 8.5% yoy with total trade falling for the 9th straight month in July amid prolonged trade tensions. Besides, loans for use in HK (excluding trade finance) increased at a moderate pace by 4.7% yoy as the elevated local borrowing costs, sour business sentiments and housing market correction might have partially offset the support from trade war de-escalation and Fed's rate cut expectations in July. Externally, the growth of loans for use outside of HK held static at 3.5% yoy, suggesting benign loan demand from Mainland China. ▪ Looking forward, as trade war escalated further and local political uncertainty heightened, combined with elevated local rates which prompted some banks to lift mortgage rates, we expect loans for use in HK (including trade finance) to remain subdued. Meanwhile, loans for use outside of HK may stay sluggish as well amid China's economic slowdown, the PBOC's efforts to support the funding needs of SMEs, the light pipeline of overseas business expansion of Mainland companies and the curb on offshore finance of Mainland property developers In a nutshell, we expect total loans to register low single-digit growth this year.
▪ HKD loan-to-deposit ratio (LDR) retreated slightly from the highest since January 2003 of 89.3% in June to 88.9% in July as HKD loans decreased by 0.4% mom and HKD deposits were unchanged.	▪ In terms of HKD deposits, due to the trade war de-escalation and increased speculation on Fed's aggressive rate cut in July, the slightly improved investment sentiments supported HKD CASA deposits to rebound by 1.2% mom. Meanwhile, with the eased HKD liquidity prompting commercial banks to reduce HKD fixed deposit rates, HKD fixed deposits retreated by 1.5% mom. As such, the percentage share of HKD CASA deposits in total HKD deposits rallied slightly to 56.5% in July but remaining much lower than the monthly average of 62.8% in 2018. This combined with the high HKD LDR suggests that the funding pressure on commercial banks remained high, which helps to explain why banks stay put on prime rate despite Fed's July rate cut. ▪ Though HKD rates have been elevated amid seasonality, potential large IPO and concerns about potential capital outflows, the rates appeared to have peaked in early July. As such, the funding pressure on the commercial banks may not intensify much further. Rather, we expect HKD rates to fall gradually along with their USD counterparts and continue to cap the upside of HKD fixed deposits. ▪ However, against the backdrop of trade war re-escalation and

	ongoing social unrest, both HKD CASA deposits growth and HKD loan growth may remain subdued. As such, both HKD loan-to-deposit ratio and the percentage share of HKD CASA deposits in HKD deposits may hover around the current levels in the near term. In a nutshell, we hold onto our view that commercial banks will keep the prime rate unchanged in the near term despite Fed's rate decisions.
▪ HK's RMB deposits rebounded by 2% mom to RMB616 billion in July.	▪ As RMB stabilized and US-China trade war de-escalated in July, offshore investors' interests in RMB deposits appeared to have improved. However, moving into August, the sharp depreciation in RMB amid trade war re-escalation may reduce offshore investors' interests in RMB assets. Despite that, we do not expect HK's RMB deposits to fall too drastically in the near term as RMB's outlook has been improved notably as compared to previous years and the yield of RMB is still relatively attractive thanks to the PBOC's neutral stance.
▪ After declining for five consecutive months, HK's retail sales dropped at a fastest pace since February 2016 by 11.4% yoy in July.	▪ The sales of clothing, footwear and allied products (-12.6% yoy, the weakest since February 2016), jewellery, watches and clocks (-24.4% yoy, the softest since August 2016) as well as medicines and cosmetics (-16.1% yoy, a record low) all showed double-digit decline. Due to the heightened political uncertainty, inbound tourism has taken a hard hit with visitor arrivals and Mainland visitors both decreasing for the first time since January 2018 by 4.8% yoy and 5.5% yoy respectively in July. This combined with a stronger HKD (especially against the RMB), trade war fears and Asia's economic slowdown have added downward pressure on the already weak tourist spending. On the other hand, the sales of food, alcoholic drinks and tobacco (-2.3% yoy), consumer durable goods (-13.2% yoy) and goods in department stores (-10.4% yoy, the lowest since August 2016) all plunged as well. With the ongoing protests disrupting the normal operation of some shops and making some local consumers reluctant to go out, coupled with the negative wealth effect from stock and housing market correction and increasing concerns about retrenchment (unemployment rate rose from over two-decade low), local consumption might have softened as well. ▪ Going forward, things could get worse before they get better. As such, we expect the decline in retail sales (-3.8% yoy in Jan-Jul 2019) to worsen in August. Should protests prolong and trade war escalate further in the rest of this year, retail sales may drop by 10% over 2019. This suggests that the unemployment of the retail sector could edge higher. Meanwhile, given the faltering outlook of the retail sector, retail shop price (-3% yoy in June) and rental (+1% yoy in June) are set to drop in the coming months.
▪ HK's exports (-5.7% yoy) and imports (-8.7% yoy) dropped for the ninth and eighth consecutive month respectively in July.	▪ The milder decline in exports might have been attributed to the improved external demand thanks to trade war de-escalation and expectations of global monetary easing in July. As such, exports to Mainland China, Japan and Thailand dropped at a slower pace while those to Taiwan and Singapore increased by 21.1% yoy and 1.8% yoy respectively. In contrast, due to sluggish local demand, imports to ten major partners all decreased. ▪ Moving into August, exporters and importers might have front-loaded the orders and in turn distorted the trade

	numbers. This however is expected to be transitory. With US-China trade war re-escalating in September and to further weigh down external demand and Asia's electronic value chain, HK's exports (high-tech products took up over 50% of total exports) will likely take a further hit. High base during September to October 2018 as well as a relatively strong HKD could also worsen the decrease in exports after August. On the other hand, with trade war and social unrest clouding the domestic growth outlook and weakening consumption sentiments, imports may stay sluggish. In a nutshell, we expect both exports and imports to continue falling in the coming months and show single-digit negative growth over 2019. If this is the case, the unemployment rate of the trade sector will likely go up again while HK ports' container throughput may tumble further.
▪ Macau's unemployment rate increased to 1.8% during the three months through July 2019 after stabilizing at an over four-year low of 1.7% for eight consecutive three-month periods. Meanwhile, employed population dropped from 387,200 to 387,100 while labor force participation rate fell from 70.4% to 70.3%.	▪ Zooming in, the employed population of hotels and similar activities and that of gaming sector continued to increase by 5.1% yoy and 1.5% yoy respectively, owing to robust tourism and mass-market gaming. However, the employed population of retail sector and that of restaurant & similar activities continued to decrease by 5.3% yoy and 6.3% yoy respectively amid weak spending of tourists and local households. Meanwhile, the employed population of construction sector decreased further by 8% yoy due to the lack of infrastructure, entertainment and housing projects under construction. ▪ In fact, Macau's economy has slipped into a technical recession in 2Q and is fraught with multiple headwinds including trade war, a strong MOP against RMB, Asia's economic slowdown and the spill-over effect of HK's social unrest. Against this backdrop, we are concerned that the overall hiring sentiments will worsen and push the unemployment rate up further. Hopefully, the new government will roll out stimulus measures to alleviate the downward pressure on the labour market.

RMB	
Facts	**OCBC Opinions**
▪ RMB rebounded initially following the news that China and US continued to engage in trade talk. However, RMB weakened in the later part of the week as a result of broad dollar rally, partially fuelled by dovish ECB.	▪ The buy dollar on dips mentality continued to dominate the FX market. Nevertheless, RMB has been kept in a narrow range last week after the USDCNY fixing has been set at 7.08 range for four consecutive days. ▪ The key focus this morning will be whether China will allow the USDCNY fixing to be set above 7.10 after new tariff took effect on Sunday. The pair may test 7.20 should the fixing break 7.10.

OCBC Greater China research

Tommy Xie Xied@ocbc.com

Carie Li Carierli@ocbcwh.com

Co.Reg.no.:193200032W