Highlights

Trade war, technology war or People's war, you name it. The US-China trade tension has many faces. The televised debate between China's state TV anchor and fox business news anchor ended with no fireworks. Nevertheless, it still drew lots of attention in China. The involvement of mass market in the trade talk makes things more complex.

The trade tension between China and US has escalated further from tariff barrier to non-tariff barrier. The setup of "unreliable entities" list will give China more power to retaliate via the legal and administrative measures. "A war to end a war", that's probably the main strategy China is pursuing to push the US back to negotiating table. Things may get worse before getting better.

In its White Paper on China's position on the China-US Economic and Trade consultations published on Sunday, China said it will not give ground on the issues of principle. Nevertheless, after reading the full text of the white paper, we think although the tone from the white paper is quite firm that China does not fear to fight to the end if needed, the message from the paper is not as aggressive as the message delivered by main media and social media. China still keeps the door open. This mean the progress of the bilateral trade talk could still be digital.

Domestically, PBoC published the follow-up QnA on Baoshang bank's takeover on Sunday. It said the takeover of Baoshang was an individual case and the central bank has no plan to take over other banks. China's reassurance is likely to calm down the market jittery. In addition, China stepped up its liquidity support following the rising volatility in the bond market. The PBoC net injected CNY430 billion last week, largest single week injection since the Chinese New Year holiday. Although it does not mean the imminent change of monetary policy stance, it does show that China's central bank remains flexible to safeguard the financial stability.

On currency, China continued to keep its daily fixing stable below 6.90, sending a strong signal to the market. However, the stronger dollar last week did not work in China's favour dragging the USDCNY higher to 6.93 range. The USDCNY tried to test 6.95 on Friday after former PBoC governor Zhou Xiaochuan hinted that there is no line of sand for RMB. Market will closely watch out for the daily fixing in the next few weeks whether China will continue to tweak its pricing mechanism when RMB approaching the critical level of 7.

In **Hong Kong,** front-end liquidity tightened into month-end. Going forward, market players will continue to prepare for half-year end and the dividend payment season while remaining cautious about the potential large IPOs. Apart from AB InBev's planned US$5 billion IPO, Alibaba is reportedly planning to raise US$20 billion through a second listing in HK in 2H 2019 at the earliest. Potential large IPOs combined with a slew of seasonal factors may keep 1M and 3M HIBORs elevated above 1.5% in the near term while lending short-term support to the HKD. If this is the case, the HKD fixed deposit rates may hold up well for a while. Adding on the correction in risky assets prices, it is likely for the percentage share of HKD CASA deposits in total HKD deposits to edge lower from the lowest since Feb 2009 of 57.3% seen in Apr. Nevertheless, we still believe that the funding pressure of commercial banks will not grow much further this year as three factors may help to cap the upside for HIBORs. First, USD LIBOR is under pressure as US Treasury Yield has been suppressed. Second, HK's loan demand has remained sluggish. Third, with limited USD-HKD yield differential and contained outflow risks, aggregate balance will likely stay around HK$50 billion. On the economy front, both retail and trade data surprised on the downside in Apr. Moving ahead, we are wary of further slowdown in both trade and retail activities. As US-China trade war continued to dent global demand and turned into technology war lately, HK's trade sector which focuses on the high-tech products will inevitably take a harder hit. Should RMB's depreciation risk intensify and wealth effect fade on a full-blown trade war, HK's retail sector would also feel the pain.

Key Events and Market Talk	
Facts	**OCBC Opinions**
▪ China's Ministry of Commerce announced that it will publish a list of "unreliable entities" to safeguard national security, public interest and the rights and interests of Chinese enterprises. China will take all necessary legal and administrative measures against those listed entities. Nevertheless, China will only unveil the detailed penalty later. ▪ In addition, China also said it will investigate the US delivery company Fedex for misrouting some	▪ The US-China trade tension has escalated further last week. The tension is no longer limited to the tariff. Instead, the non-tariff barrier has risen significantly.

Huawei parcels to the US.	
▪ China unveiled the white paper on China's position on the China-US Economic and Trade consultations on Sunday. The paper said "The US government should bear the sold and entire responsibility for severe setback". Meanwhile China also listed three examples of US backtrackings in the negotiation saying "the more the US government is offered, the more it wants" ▪ In addition, the white paper concluded that China will not give ground on the issues of principle. "China is open to negotiation, but will also fight to the end if needed." ▪ In the press conference, China's Vice commerce minister Wang Shouwen did not comment whether President Xi and President Trump will meet in the upcoming G20 meeting. However, he also said market should not over read China's setup of "non-reliable list".	▪ The white paper elaborates further about the reason for the stall of the US-China trade talk. The key hurdle for a trade deal is probably the different understanding about the sovereign issues. According to the white paper some of the mandatory requirements insisted by the US side has concerned China's sovereign affairs. ▪ It seems that China has drew its line of sand clearly and passed the ball back to the US side. Should the Trump Administration refuse to compromise, the chance for both sides to restart the talk may be much lower. ▪ The previous hope that G20 may mark the end of the current US-China trade tension is unlikely to materialize. At best, the G20 meeting may mark the restart of the trade talk. ▪ Nevertheless, after reading the full text of the white paper, we think although the tone from the white paper is quite firm that China does not fear to fight to the end if needed, the message from the paper is not as aggressive as the message delivered by main media and social media. China still keeps the door open. This mean the progress of the bilateral trade talk could still be digital.
▪ The US Trade Representative announced on 31 May that products exported from China to the US prior to 10 May will remain subject to additional 10% tariff if they enter into the US before 15 Jun, extended slightly from previous deadline for 1 Jun.	▪ The limited extension is unlikely to have significant impact on the market.
▪ PBoC published the follow-up QnA on Baoshang bank's takeover on Sunday. It said the takeover of Baoshang was an individual case and the central bank has no plan to take over other banks.	▪ The QnA gave a detailed explanations on central bank's unexpected move to take over the bank. The Baoshang bank was 89% owned by a financial conglomerate, which the Chairman was under investigation. The bank has faced a severe credit event as the main shareholder has borrowed illegally from the bank they controlled. ▪ China's reassurance on no planned takeover of other banks in the near term is likely to calm down the market jittery.
▪ China stepped up its liquidity support following the rising volatility in the bond market. The PBoC net injected CNY430 billion last week, largest single week injection since the Chinese New Year holiday.	▪ The massive liquidity injection helped contain the volatility seen in the bond market following the takeover of Baoshang bank. Meanwhile, it doesnot mean the imminent change of monetary policy stance, it does show that China's central bank remains flexible to safeguard the financial stability.
▪ PBoC announced the setup of Deposit Insurance Fund Management companies to manage its funds.	▪ It is a move to standardize the management of insurance fund.
▪ PBoC Governor Yi Gang reiterated China's target to lower the funding costs for small and micro companies by 100bps as well as 30% loan growth target for small and micro companies. Meanwhile, he also said China will consider scrapping the publish of benchmark lending and deposit rate as part of China's interest rate liberalization.	▪ Given China's reassurance to support the funding demand for small and micro companies, we think China will remain flexible on its monetary policy.
▪ Former PBoC Governor Zhou Xiaochuan said there is no need for China to change its pricing mechanism just because of the price approaches the critical level of 7.	▪ RMB weakened following the release of Zhou Xiaochuan's interview as a knee jerk reaction. Market has been debated whether there is any line of sand for RMB. Market will closely watch out for the daily fixing in the next few weeks as clearly China tweaked its fixing pricing mechanism in the past two weeks.
▪ Shenzhen's Deputy Governor announced that	▪ The favorable tax policy together with the financial integration

talents in shortage who work in the Greater Bay Area will enjoy a 15% cut on personal income tax.	(such as cross-border payment, account-opening and remittance) across the Greater Bay Area will likely pave way for the free-flow of human resources among the bay area.
▪ It is reported that Alibaba Group Holding Ltd. is planning to raise US$20 billion through a second listing in HK in 2H 2019 at the earliest.	▪ The reason behind could be the renewed US-China trade tensions as well as the Hong Kong Exchange's revamp of listing rules last year which helped to lure high-tech companies (such as Xiaomi and Meituan) to launch IPO in HK. With the dual-class shares to be included into the stock connect schemes from July, the expected second listing of Alibaba in HK may help to attract more equity inflows from Mainland to HK under the stock connect schemes. ▪ On the interest rate front, despite the muted investor sentiments, such a large size of second listing by such a renowned Chinese name will likely lock up a substantial amount of HKD liquidity. In addition, AB InBev, World's largest brewer, is planning to raise US$5 billion via IPO in HK probably in July. The potential large IPOs together with the seasonal factors could keep 1M and 3M HIBORs above 1.5% in the coming months. Adding on the suppressed USD LIBOR, the limited yield differential may help to contain the risk of USDHKD touching 7.85.

Key Economic News	
Facts	**OCBC Opinions**
▪ China's official PMI softened further to 49.4 in May from 50.1 in April. ▪ PMI for small enterprises weakened again to 47.8 from 49.8 though PMI for big enterprises remained above the threshold line at 50.3.	▪ The decline of May PMI was mainly attributable to three factors. First, the seasonal distortion, which boosted the March data, has faded away. Second, the re-escalation of US-China trade war also dampened manufacturer's confidence. China's new export index fell significantly to 46.5 in May from 49.2 in April. Third, the shift of monetary policy to neutral in April may also weigh down on sentiment. Domestic demand also weakened with new order index slipped to below 50 at 49.8 from 51.4. ▪ Employment index continued to trend down to 47, lowest since Lehman crisis, signalling the rising pressure on job market amid the slowdown in the global economy and rising protectionism. ▪ Purchasing price index also fell further to 51.8 from 53.1, a sign of easing pressures on import price. This may suggest that China's PPI may have peaked. With high base effect kicking in in the next few months, the chance for PPI to retreat back to zero cannot be ruled out.
▪ HK's trade data for Apr 2019 surprised on the downside with exports and imports falling by 2.6% yoy (the sixth yearly decline in a row) and 5.5% yoy (the fifth yearly decrease in a row) respectively. Trade deficit shrank by more than expected to HK$35.1 billion.	▪ Though exports to Mainland China dropped at a much slower pace by 1.3% yoy as compared to the 10.1% yoy decline in the previous month, exports to other major trading partners including the USA (-17% yoy), India (-15.3% yoy), Japan (-12.5% yoy), Taiwan (-24.4% yoy) and Vietnam (-12.4% yoy) all decreased notably. This confirms that the green shoots in China's economy did not help to revive other Asian countries' growth and demand while US-China trade war continued to materialize. On the other hand, despite the rebound in commodity prices in Apr, imports dropped at a faster pace, reflecting weak demand at home and abroad. Over the first four months of this year, container throughput of HK's port dropped by 7.6% yoy to 5.99 million TEU, ranking the eighth (as compared to the 7th last year) among the global major

	ports. ▪ Moving ahead, we are wary of further contraction in HK's trade activities as the US-China trade war escalation is set to put a lid on global economic recovery and hit global demand. Also, any further tumble in the trade activities between the US and China may hurt HK's trade sector as HK is the main re-export port of China. More notably, with the trade war turning into technology war, Asia's whole electronic value chain may take a harder hit. The same would be true to HK's trade sector which focuses mainly on the high-tech products. Exports and imports of electrical machinery, telecommunications and office machines took over 68% of total exports and 60% of total imports respectively in Apr. In conclusion, we expect exports and imports will see around 0% growth in 2019. Should US-China trade war escalate, HK's trade activities are likely to weaken further.
▪ HK's retail sales dropped for the third consecutive month by 4.5% yoy in Apr 2019 as visitor arrivals also increased at a slower pace by 5.2% yoy during the same period.	▪ Specifically, the sales of food, alcoholic drinks and tobacco as well as those of goods in supermarkets continued to increase by 0.8% yoy and 1.1% yoy respectively. This was mainly supported by the wealth effect from stock market and property market rally as well as the tight labor market. In contrast, the sales of clothing, footwear & allied products (-2.6% yoy), consumer durable goods (-10.5% yoy) and jewelry, watches & clocks (-11.4% yoy) all continued to drop. This was due to drop due to cautious consumption sentiment of both local households and inbound visitors. Moving into May, the Labor Day Holiday combined with infrastructure improvement might have lent some support to HK's inbound tourism and the sales of low-end products. Nevertheless, as the re-escalation of US-China trade war led to stock market correction and added renewed downward pressure on RMB, local consumption and visitor spending will likely take a hit and result in a broad-based slowdown in the retail sector over the coming months.
▪ HK's total loans growth decelerated to the weakest level since Jun 2016 at 0.5% yoy in Apr 2019.	▪ Internally, trade finance dropped for the eighth month in a row by 7.8% yoy amid weakening trading activities. Loans use in HK (excluding trade finance) retreated by 0.1% yoy, marking the first decline since Jan 2010 despite stock market and property market rally. This could be attributed to two factors. First, investor sentiments remained cautious due to the faltering global growth outlook and lingering trade war risks. Second, after the aggregate balance shrank by 29% YTD to HK$54 billion, the seasonal factors gradually drove up HIBORs (or borrowing costs). Moving ahead, as US-China trade war re-escalated in early May, we are wary of further weakness in local loan demand. ▪ Externally, the growth in loans for use outside of HK decelerated again to 3.5% yoy in Apr from 4.2% yoy in Mar. Though offshore financing remained less costly after the PBoC shifted to a structural easing stance, Mainland companies' offshore funding demand is set to be tamed by the weakening RMB and China's curb on new offshore bond issuance by property developers and LGFVs. In conclusion, we expect total loan growth to remain subdued and only see low single-digit growth in 2019.
▪ HKD loan-to-deposit ratio retraced lower from a nearly 16-year high of 87.8% in Mar to 87.3% in Apr	▪ HKD CASA deposits rebounded by 0.8% mom thanks to the rally in risky assets prices which encouraged the customers to

as HKD loans increased by 1.1% mom while HKD deposits rose by 1.6% mom.	increase CASA deposits for investments. HKD fixed deposits rose by 2.7% mom probably due to higher fixed deposit rates on higher HIBOR. As such, the percentage share of HKD CASA deposits in total HKD deposits edged lower to 57.3%, the lowest since Feb 2009. ▪ Moving into May, as commercial banks prepared for the seasonal factors in advance, some banks further raised fixed deposit rates. Combined with the stock market correction since early May amid trade war escalation, fixed deposits are likely to rebound in the near term. In 2H 2019, the potential large IPOs together with seasonal factors may keep HIBORs and HKD fixed deposit rates elevated. Nevertheless, we still believe that the funding pressure of commercial banks will not grow much further this year as three factors may help to cap the upside for HIBORs. First, USD LIBOR is under pressure as US Treasury Yield has been suppressed by trade war concerns and rising speculation of Fed rate cuts. Second, loan demand remains sluggish given the worsening economic outlook and the trade war escalation. Third, with limited USD-HKD yield differential and contained outflow risks, aggregate balance will likely stay around HK$50 billion in the near term. In conclusion, we hold onto our view that the chance of prime rate hike is low this year.
▪ HK's RMB deposits increase by 2% yoy or 1.7% mom to RMB612 billion in Apr 2019.	▪ This might be attributed to the resilient offshore demand for RMB assets which provided a relatively higher yield after the PBoC shifted to a structural easing stance. With the re-escalation of US-China trade war in early May, China's market saw capital outflows while RMB faced renewed downward pressure, signaling weaker interests in RMB assets of offshore investors. Nevertheless, due to the rising speculation on Fed's rate cuts and increasing concerns about trade war risks, global government bond yields tumbled. This helps to keep RMB rates relatively high. In conclusion, unless RMB's depreciation risks intensify on further escalation of US-China trade war and broad strength of USD, we do not expect HK's RMB deposits to plunge drastically.
▪ Macau's unemployment rate was unchanged at a more than four-year low of 1.7% during the three-month period through Apr 2019.	▪ Despite that, the employed population dropped to the lowest level since mid-2018 at 385300 while labor force participation rate slid to a more than one-year low of 70%. The employment of different industries was also mixed. Specifically, the employed population of the gaming sector rose for the second consecutive month by 4.7% yoy to the highest level since early 2015 despite the weakening gaming activities. Meanwhile, the employed population of hotel and similar activities rose by 5.4% yoy to the strongest since late 2018, thanks to resilient tourism. On the other hand, however, the growth of employed population of construction sector softened to the weakest since late 2018 at 1.6% yoy with the successive completion of new mega projects. Besides, the employed population of retail sector as well as restaurant and similar activities dropped by 6.5% yoy and 11.3% yoy respectively, mainly due to cautious consumption sentiments of both local households and inbound visitors. Moving forward, total unemployment rate may be sticky around 1.7% as it is a lagging indicator. Nevertheless, with tourism, retail and gaming sectors all succumbed to external headwinds including renewed US-China trade war, we suspect the sustainability of the low

	unemployment rate in the medium term.
RMB	
Facts	**OCBC Opinions**
▪ RMB weakened slightly against the dollar last week as a result of stronger dollar. Nevertheless, RMB index remained stable.	▪ China continued to keep its daily fixing stable below 6.90, sending a strong signal to the market. However, the stronger dollar last week did not work in China's favour dragging the USDCNY higher to 6.93 range. The USDCNY tried to test 6.95 on Friday after former PBoC governor Zhou Xiaochuan hinted that there is no line of sand for RMB.

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