Greater China – Week in Review

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Highlights

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China tightened its anti-pandemic measures after it put Shijiazhuang city, capital of Hebei Province with 11 million population, into lockdown. Senior officials from the National Health Commission have encouraged people not to return to hometown for the upcoming Chinese New Year holiday. The impact of the recent resurgence in Hebei on the Chinese economy remains unclear pending on the development of China's control measures. At the current scale, we think the impact is likely to be limited.

China started the new year with flushed liquidity in the banking system. Although China's PBoC net withdrew CNY465 billion via open market operation last week, interbank benchmark rate DR007 continued to drift lower to 1.71%. The excessive liquidity was partially attributable to possible re-acceleration of sale of dollar ahead of Chinese New Year. China's FX reserve increased to US$3.2165 trillion in December. There is early signal that the recent accumulation of FX reserve is no longer only driven by valuation effect but increasing demand for RMB as well.

Should corporates continue to unwind foreign currency deposits they have accumulated in the past year, it may lead to more passive RMB liquidity injection into the banking system, which may require PBoC to sterilize more via open market operation.

The concerns about the rapid RMB appreciation has led to more tweaks in macro prudential coefficient for cross border flows. The recent high frequent changes of cross border macro prudential coefficient since December have served one purpose, which showed China's intension to slow down the pace of RMB appreciation. The underlying logic is to rebalance capital flows via decreasing inflows from cross border borrowing and increasing outflows via higher cross border lending quota.

Geopolitically, President Trump finally conceded last week. Although he is leaving the office soon, Trump's legacy of unpredictability continued to shadow the fate of Chinese companies. The double U-turn of New York Stock exchange to delist three Chinese telcos confused the market last week.

Against this backdrop, China's Commerce Department unveiled a new regulation to adopt counter measures against unjustified extraterritorial application of foreign legislation. The release of new regulations ahead of inauguration of Biden Administration served the purpose of drawing China's red line in protecting Chinese companies' interests and rights.

In **Hong Kong,** retail sales value declined 4% yoy in November, the mildest since May 2019. However, for most of the retail outlets, the sales value continued to decline notably. In the very near term, the retail sector's outlook may remain sluggish due to the ongoing containment measures. Likewise, amid the virus resurgence at home and broad, the PMI for private sector, which slid to an eight-month low of 43.5 in December, may remain sluggish in the near term. This reinforces our view that GDP may continue to contract in 4Q 2020.

On a positive note, should local pandemic be brought under control and border control be lifted amid vaccine rollout, the PMI may rebound gradually and stabilize above the 45 mark while the retail sector may regain some momentum. That said, any recovery of the retail sector may be only gradual and moderate. Specifically, the government may gradually unwind the one-off relief measures. Meanwhile, it may take some time for the labour market to recover. In conclusion, given the low base from 2020, we expect retail sales value to rebound about 15% yoy this year.

Regarding the property market, though the pandemic has hit both commercial property market and residential property market, the latter's outlook may be brighter. We expect housing price to rebound about 5% yoy in 2021.

Finally, due to the heightened de-listing risk, three ADRs including Bilibili, Autohome and Baidu all reportedly planned to file for Hong Kong secondary listing in the near term. With more ADRs likely coming for secondary listing in Hong Kong and some large IPOs like Kuaishou in the pipeline, we expect Hong Kong's IPO market to remain active in the coming year. This may cap the downside of HKD interest rate and exchange rate.

Key Events and Market Talk	
Facts	**OCBC Opinions**
▪ China tightened its anti-pandemic measures after it put Shijiazhuang city, capital of Hebei Province, into lockdown.	▪ China has completed first round of mass testing of more than 10 million residents in Shijiazhuang city identifying 354 infections. China's deputy head of the National Health Commission suggested people not to return to their hometowns for Chinese New Year celebration. Meanwhile, tighter control measures against gathering will also be beefed up though there is no detail yet. The impact of the recent resurgence in Hebei on the Chinese economy remains unclear pending on the development of China's rollout of control measures. At the current scale, we think the impact is likely to be limited.
▪ China's central bank net withdrew CNY465 billion via open market operation. However, interbank benchmark rate DR007 continued to drift lower in the first week of 2021 to 1.7157% from last year end's 2.489%.	▪ The flush liquidity in the first week of 2020 was mainly due to two factors including the carry over effect from easing cross year end liquidity and possible re-acceleration of the net foreign currency position as a result of seasonal demand ahead of Chinese New Year holiday as well as concerns about further dollar weakness. ▪ Should corporates unwind more foreign currency deposits they accumulated in the past year, it may lead to more passive RMB liquidity injection into the banking system, which may require PBoC to sterilize via open market operation.
▪ China's central bank PBoC set 10 key tasks for 2021 after concluding its annual working conference.	▪ Other than flexibility, the monetary policy will be more targeted and reasonable. This means that China's monetary policy direction could be two-way depending on the development of macro condition. In addition, RMB internalization also returns to the spotlight though PBoC said it will promote RMB internationalization in a more prudent manner.
▪ China's central bank PBoC and currency regulator SAFE announced last week that it will increase the macro prudential coefficient for domestic enterprise's cross border lending cap to 0.5 from 0.3. ▪ Meanwhile, PBoC also announced to reduce the coefficient for domestic enterprises to borrow from the offshore market to 1 from 1.25.	▪ The recent high frequent changes of cross border macro prudential coefficient since December have served the same purchase, which showed China's intension to slow down the pace of RMB appreciation. The underlying logic is to rebalance capital flows via decreasing inflows from cross border borrowing and increasing outflows via higher cross border lending quota.
▪ China's Commerce Department unveiled a new regulation to adopt counter measures against unjustified extraterritorial application of foreign legislation.	▪ Relevant government bodies will help Chinese citizen or companies who are targeted by foreign legislation against the backdrop of increasing measures from the Trump Administration to target Chinese business. With Biden Administration is expected to take over in less than 10 days, the release of new regulations ahead of inauguration of Biden Administration served the purpose of drawing China's red line in protecting Chinese companies' interests and rights.
▪ Over the past week, three ADRs including Bilibili, Autohome and Baidu all reportedly planned to file for Hong Kong secondary listing in the near term.	▪ Notably, the New York Stock Exchange is proceeding with a plan to delist three Chinese telecoms while the US officials are said to be considering banning investment in Alibaba and Tencent. The heightened delisting risk may have prompted the ADRs to consider launching secondary listing in Hong Kong. ▪ Apart from the delisting risk, there may be some other factors driving the ADRs to get listed in Hong Kong. First, for the

	companies especially the tech names, more liquidity is better for business growth. Second, should the secondary listings in Hong Kong receive strong responses like Alibaba and JD.com, it may help to restore the shareholders' confidence despite the lingering US-China tensions. Third, a secondary listing could allow the companies to achieve higher valuations. Fourth, the companies may want to maintain some exposure overseas to prepare for future offshore expansion if any. Fifth, in comparison to other popular exchanges, Hong Kong Exchange may be preferable as its new listing rules are favourable to high-tech companies and biotech companies. Finally, if being included in the stock connect, the Chinese names could benefit from the onshore investors' growing needs to diversify the risks with offshore assets. ▪ In conclusion, with more ADRs likely coming for secondary listing in Hong Kong, we expect Hong Kong's IPO market to remain active in the coming year. This may cap the downside of HKD interest rate and exchange rate.

Key Economic News

Facts	OCBC Opinions
▪ China's FX reserve increased to US$3.2165 trillion in December from US$3.1784 trillion in November.	▪ The rebound of FX reserve in December was due to both capital inflows and valuation effects. The extended dollar weakness in December as a result of improving risk sentiment globally on the back of vaccine hope contributed to the mark to market gain of non-dollar valuation. In the first three quarters of 2020, valuation effect from both asset appreciation and currency contributed to US$32.2 billion to China's FX reserve accumulation. ▪ The marginal increase of FX reserve showed for most of 2020 despite RMB appreciation showed muted capital inflows. However, the re-acceleration of FX reserve in the last two months of 2020 may trigger more dollar sale.
▪ Hong Kong's PMI for private sector slid to 43.5 in December, the lowest since April 2020. Output and new orders both fell at the fastest rate since April 2020. Meanwhile, both new business flows from Mainland China and employment dropped notably.	▪ The deteriorating business conditions in the private sector was mainly attributable to the fourth wave of Covid-19 and the resultant tightening of social distancing measures. Virus resurgence in other major economies were also to blame. Since the government has extended the existing containment measures till late January and lockdown measures in other nations are still in place, the business conditions may remain sluggish. As such, PMI may stay in the contraction territory in the coming months. This reinforces our view that GDP may continue to contract in 4Q 2020. ▪ On a positive note, once the local pandemic is brought under control and the border control is lifted due to and effective vaccine roll-out, it is possible for the business conditions to improve. In this case, it is unlikely that PMI will fall back to last year's lows. Rather, the PMI may rebound gradually and stabilize above the 45 mark in the medium term.
▪ Hong Kong's retail sales value declined 4% yoy in November, the mildest since May 2019. ▪ Hong Kong government extended the stringent social distancing measures by another two weeks	▪ The decline narrowed mainly due to low base effect and the significant increase in the sales of consumer durable goods (+21.3% yoy). Despite that, retail sales dropped for the 22nd consecutive month. Domestically, the decline in the sales of

till 20 January. Besides, the government does not rule out the possibility of further tightening the measures should the Covid-19 situation worsen further ahead of Lunar New Year.	clothing, footwear and allied products widened from -10.7% yoy in October to -14.1% yoy in November. Meanwhile, the sales of goods in department stores retreated by 12.4% yoy as the consumption-related activities have been disrupted again by the fourth wave of Covid-19. Externally, sales of jewelry, watches and clocks (-16.1% yoy) as well as medicines and cosmetics (-34.8% yoy) continued to drop notably as visitor arrivals dropped over 95% for the tenth consecutive month by 99.8% yoy in November. ▪ In the very near term, the retail sector's outlook may remain sluggish due to the ongoing containment measures. That said, in the medium term, we do expect the retail sector to regain some momentum should local pandemic be brought under control and international travel resume on vaccine rollout. Still, the pace of recovery may be only gradual and moderate. Specifically, the government may gradually unwind the one-off relief measures. Meanwhile, it may take some time for the labour market to recover. In conclusion, given the low base from 2020, we expect retail sales value to rebound about 15% yoy this year.
▪ According to Savills, a global real estate services provider, the rental of commercial properties dropped 5.1% qoq in 4Q 2020 and fell by 16.6% yoy for 2020 as a whole, the sharpest rate since 2009. The vacancy rate of Grade-A offices rose from 4.7% as of end-2019 to 8.4% as of end-2020. ▪ The transaction volume of industrial and commercial properties dropped by about 13% yoy to about 4226 deals in 2020, the lowest since 2001, according to Centaline Commercial (Hong Kong).	▪ On one hand, the rental of the commercial properties in Hong Kong Island's CBDs led the decline amid cost concerns and increasingly flexible work arrangement. On the other hand, in order to lure demand, landlords of the commercial properties in Kowloon East offered notable rental concession. ▪ Going forward, due to low base effect and the optimism about economic outlook on positive news of vaccine development, the rental of commercial properties may see low single-digit growth this year. However, the structural change to the work arrangement indicates that the rental of commercial properties may not return to the pre-virus levels anytime soon.
▪ Hong Kong's housing price index dropped for the first time in three months by 1.3% yoy in November. Meanwhile, CCL index, which tracks the secondary home prices, slid by 1.1% yoy in 2020, the first decline in 12 years. Also, housing transaction volume printed 6067 deals in December, barely changed from the prior month.	▪ Taken all together, it points out that the housing market retreated probably due to the virus resurgence which has hit investment sentiments and disrupted economic activities. ▪ Moving into 2021, we expect the overall housing market to rebound given several favourable factors. First, should vaccine rollout help to contain the virus, the housing market may be supported by the pent-up demand. Second, since the Fed is expected to keep rates unchanged near zero, local borrowing costs may stay lower for longer as well. Third, investment demand may be supported by the positive wealth effect from stock market rally on optimism about economic outlook. Fourth, as Covid-19 has disrupted the construction activities and the government has withdrawn the vacancy tax bill, the resultant slow increase in home supply means that the imbalance between supply and demand may persist. ▪ However, the recovery of housing market may be uneven. Specifically, for the small to medium size flats priced no higher than HK$10 million, the market outlook may be relatively positive due to the mortgage relief for first-home local buyers. In contrast, the upside of the larger flat market may be capped by two factors. First, some homeowners may sell their luxurious properties at deeply discounted price amid cash flow

	pressure or the need to dispose local assets ahead of migration. Second, the declining housing rental (larger flats' rental fell for the 14th straight month for) may deter some investment demand. ▪ In conclusion, we expect housing transaction volume to rebound moderately and overall housing price index to rally about 5% yoy in 2021. The price of small to medium size homes may grow at a faster pace than the larger flats.

RMB	
Facts	**OCBC Opinions**
▪ RMB started 2021 with strong momentum with the USDCNY broke below 6.50. The pair ended the week at around 6.46.	▪ RMB gave up some gains after China rolled out more measures to decrease capital inflows via cross border borrowing and broaden channel of capital outflow via cross border lending. The recent high frequency of policy finetuning showed that China wanted to slow down the pace of RMB appreciation. This may counter the seasonal demand for RMB ahead of Chinese New Year holiday. We expect the USDCNY to be traded in a relative narrow range in the coming weeks.

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