Greater China – Week in Review

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Highlights

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For the first time in six months, PBoC did not fully roll over the maturing MLF and TMLF. The CNY500 billion MLF injection last week was short of the aggregate of maturing CNY300 billion MLF and CNY240.5 billion targeted MLF. The net withdrawal of long-term liquidity was mainly attributable to the recent decline of NCD issuance yield, which has been below the MLF rate since the beginning of 2021.

This shows PBoC will continue to play its balancing game although its deputy Governor reiterated that there is no urgency for U-turn of monetary policy in the latest press conference.

I have at least five takeaways from the latest PBoC press conference. But my biggest takeaway is that PBoC believes its current interest rate and reserve requirement ratio are appropriate. The borrowing cost for enterprise has fallen by 51bps in 2019 to 4.61%, lowest in record. The magnitude of decline is also bigger than that of LPR. This suggests that there is no urgency for PBoC to change its monetary policy.

The recent slowdown of credit expansion and still sluggish CPI were not a concern for PBoC. PBoC expects core CPI to improve gradually. In addition, PBoC also expects M1 growth to slow down due to the decline of corporate demand deposit as companies will accelerate their investment plan.

China's trade data remained strong in December as Chinese exporters benefited from the resurgence of virus globally. For 2020, I have two main takeaways from trade data. First, the increasing confrontational stance from Trump Administration has limited impact on the US-China trade flow. Total US-China trade hit US$526.5 billion in 2020, only down marginally 2.54% from that in 2019. However, it still exceeded US$524 billion in 2016 when President Trump first took over the office. Meanwhile, China's trade surplus with the US in 2019 remained strong at US$291.7 billion, on par with US$295.6 billion in 2019.

Second, the trend of supply chain shift continued in 2020 judging by the strong trade linkage between China and ASEAN. China's trade surplus with Vietnam reached a record of US$35.33 billion, a sign of increasing supply chain collaboration between China and Vietnam.

As we are approaching Chinese New Year, the focus will be whether PBoC will implement any form of liquidity injection to ease funding for the upcoming holiday season given PBoC is unlikely to cut its reserve requirement ratio anytime soon.

In **Hong Kong,** the focus has been on the equity market where Hang Seng Index rose to a nearly one-year high, partially due to the robust southbound equity inflows. Since the start of this year, southbound flows under the stock connect have kept seeing net inflows of over HK$10 billion every day. Month-to-date southbound equity inflows reached HK$135.73 billion, on the way to break the record high seen last March. This is mainly attributable to the buy-on-dip move of the Mainland investors as the concerns about US sanctions had weighed heavily on some H-shares' price. Moving ahead, we expect the southbound equity inflows to remain strong given the attractive valuation of HK equity, the flushed global liquidity, and the sanguine investment sentiment amid optimism about global economic outlook. Meanwhile, the IPO market is expected to remain active with several renowned ADRs, medical names and tech names in the pipeline. As such, any net capital outflow looks unlikely in the near term. Aggregate balance may stay at record high for some time. That said, the downside of HKD exchange rate and interest rates may be capped by the HKD demand associated with equity inflows and large IPO such as Kuaishou.

On the fiscal condition front, due to the sharp decline in stamp duty collections and land sales premium, it is expected that the government's fiscal deficit for 2020/21 will be over HK$300 billion. As a result, the fiscal reserves may be equivalent to less than 12 months of government expenditure. To uphold the principle stipulated in Article 107 of the Basic Law, any further stimulus measures rolled out via 2021/22 Budget may be not be so generous. As such, unemployment rate and bankruptcies may increase in 1Q while strong economic recovery looks unlikely until the virus is well contained and the border control is lifted.

Key Events and Market Talk	
Facts	**OCBC Opinions**
▪ PBoC injected less than expected CNY500 billion liquidity via 1-year MLF in January.	▪ The CNY500 billion 1-year MLF injection was lower than the aggregate of maturing CNY300 billion MLF and CNY240.5 billion targeted MLF. Since August 2020, PBoC has rolled over more than matured MLF for five consecutive months. This is the first time in six months that PBoC net withdrew the medium-term liquidity offering because the 1-year NCD issuance yield has fallen below the 1-year MLF rate since the beginning of 2021. This signaled that the demand for MLF may have declined. ▪ Overall, we think the less than expected MLF injection signaled that PBoC will continue to keep a balanced towards monetary policy. Although it will not opt for U-turn of monetary policy, it will also keep a close eye on liquidity situation and is likely to keep a relatively tight balance.
▪ PBoC deputy Governor reiterated that there is no urgency for U-turn of monetary policy in the latest press conference.	▪ There are five takeaways from the press conference. ▪ First, on inflation, PBoC expects core CPI to improve gradually though the room for significant rebound of headline CPI is limited as food prices are unlikely to surge due to recovery of supply. ▪ Second, on shadow banking, the stock of shadow banking has declined by CNY2 trillion to CNY32 trillion. ▪ Third, the PBoC remained alerted to external risks including the higher market volatility as a result of divergence between the real economy and financial market, higher volatility of two-way capital flow as a result of excessive global easing and the risk of higher debt in low income countries. ▪ Fourth, PBoC said the current interest rate and reserve requirement ratio are appropriate. The borrowing cost for enterprise has fallen by 51bps in 2019 to 4.61%, lowest in record. The magnitude of decline is also bigger than that of LPR. This suggests that there is no urgency for PBoC to change its monetary policy. ▪ Fifth, PBoC will try to ensure M2 growth and aggregate social financing growth to match nominal economic growth. However, he also said match does not mean equal and it is a medium-term target, which will not be assessed based on monthly or quarterly data. This will give policy more flexibility to achieve its targets.
▪ Since the start of this year, southbound flows under the stock connect have kept seeing net inflows of over HK$10 billion every day. Month-to-date southbound equity inflows reached HK$135.73 billion, on the way to break the record high seen last March. ▪ Partially due to the strong southbound equity inflows, Hang Seng Index rose to a nearly one-year high while USDCNH 12M forward swap points dropped to a nearly six-month low.	▪ The concerns about US sanctions had hit the H-shares hard especially after the NYSE de-listed three Chinese telecoms. However, the panic sell-off did not sustain. Instead, the plunge in the share price has been considered opportunities to buy on dips, in particular for the Mainland investors who favoured Tencent, China Mobile, CNOOC and SMIC the most. Notably, China Mobile's H-share price ended up 13.5% last week. ▪ Apart from the buy-on-dip move, several other factors may have been boosting southbound equity inflows as well. These factors include the strong fundamental of the Chinese big names, the relatively attractive valuation of Hong Kong's equity, the flushed global liquidity, and the sanguine

	investment sentiment amid optimism about global economic outlook. Besides, it confirms that Chinese investors have increasing needs to diversify their portfolio with offshore assets. ▪ Given the strong equity inflows and the busy IPO pipeline, HKD demand may remain solid and in turn cap the downside of HKD rates and USDHKD spot.

Key Economic News

Facts	OCBC Opinions
▪ China's export and import growth beat market expectation in December. Export in dollar term grew by 18.1% yoy while imports grew by 6.5% yoy. ▪ China's trade surplus in December rose further to a record of US$78.17 billion from US$75.4 billion in December.	▪ China's exports to G3 economies remained strong. Exports to US continued to increase by 34.5% after hitting a record of US$51.97 billion in absolute term in November 2020. In addition, exports to EU and Japan also rose by 4.33% yoy and 8.23% respectively. ▪ Trend of supply chain shift continues as China's exports to ASEAN remains strong. China's exports to ASEAN accelerated to 18.37% yoy. In addition, China's trade surplus with Vietnam reached a record of US$35.33 billion, a sign of increasing supply chain collaboration between China and Vietnam. ▪ Oil remained the key drag on import growth with oil import fell by 43.21%. Nevertheless, both imports of electronic integrated circuit and iron ore remained strong, up by 26.48% yoy and 31.97%. This shows still resilient domestic demand.
▪ China's credit expansion slowed in December. Aggregate social financing growth decelerated to 13.3% from 13.6% in November and peak of 13.7% in October. In addition, both M1 and M2 growth also slowed to 8.6% and 10.1% respectively from 10% and 10.7%.	▪ The slightly slower than expected credit growth was mainly attributable to four factors including ongoing contraction of off-balance sheet lending led by the shrink of trust loan, weak credit bond issuance as a result of rising default risk, cooling property market due to tighter measures and weakening propensity to consumption. ▪ Nevertheless, overall structure of credit expansion remained strong with medium to long term loan growth remained steady. Looking ahead, we think December data reinforced our view that China's credit expansion may have peaked. Against the backdrop of increasing focus on maintaining macro leverage ratio, we expect China's credit expansion may slow further in the coming months. This may be supportive of China's bond market in the near term.
▪ China's CPI rebounded to 0.2% yoy in December from -0.5% yoy in November.	▪ On sequential basis, CPI rose by 0.7% mom mainly driven by the rebound of food prices, which jumped by 8.5% mom after contracting for two consecutive months. In addition, the rebound of oil prices in the past few years also drove up transportation cost with fuel cost increased by 5.1% mom. However, core CPI slipped lower to 0.4% yoy, record low since China published this data. This new low of core CPI was probably the result of extreme cold winter and resurgence of virus in some parts of the country. Looking ahead, given the high base effect, we expect China's CPI to fall back to negative territory again in January and February. As such, there is no urgency for China to think about U-turn of its monetary policy in the near term.

▪ Hong Kong's stamp duty collections for property dropped for the second consecutive year by about 38% yoy to about HK$13 billion in 2020, reaching record low. The decline was led mainly by the drop of the collections of buyer's stamp duty. Adding to the downward pressure is the abolition of double stamp duty for non-residential property from late November. ▪ For the fiscal year 2020/21, the premium of land sales has so far amounted to merely HK$36.1 billion, down by 67.2% yoy.	▪ Due to the sharp decline in stamp duty collections and land sales premium, it is expected that the government's fiscal deficit for 2020/21 will be over HK$300 billion. As a result, the fiscal reserves may be equivalent to less than 12 months of government expenditure. As such, there has been talks about tax hike lately, which however looks unlikely at the moment given the faltering economic growth outlook. ▪ However, according to the Article 107 of the Basic Law, Hong Kong government shall follow the principle of keeping the expenditure within the limits of revenues in drawing up its budget, and strive to achieve a fiscal balance, avoid deficits and keep the budget commensurate with its GDP growth rate. This helps to explain the shrinking size of the latest rounds of anti-epidemic funds and signals that any further stimulus measures rolled out via 2021/22 Budget may be not be so generous. ▪ As such, unemployment rate and bankruptcies may increase in 1Q while strong economic recovery looks unlikely until the virus is well contained and the border control is lifted.
▪ Hong Kong: The total bankruptcy petitions presented increased 6.6% yoy to a four-year high of 8693 in 2020. The total compulsory winding-up petitions presented also rose 7.2% yoy to a four-year high of 449 last year.	▪ Still, the number may have been underestimated as the public administration sectors sometimes only offered limited services amid work from home arrangement. As the Employment Support Scheme ended in November and the government has imposed stringent social distancing measures to contain virus since late November, the business conditions may remain sluggish in the near term while the jobless rate may edge higher in the coming months. In other words, the number of bankruptcies may go up further in 1H 2021.
▪ Macau's average housing price dropped by 1.6% mom or 4.2% yoy to MOP106,836/square meter in November. During the same month, housing transaction volume decreased for the fifth consecutive month by 5.9% yoy to 602 deals. Approved residential mortgage loans also fell for the second consecutive month by 14.5% yoy to MOP2.9 billion in November. ▪	▪ More notably, local buyers who have hold more than one flat accounted for 2.6% of total local home buyers in November, down from 5.8% in October. This reinforces the fact that the housing market has remained muted probably due to the still subdued economic outlook amid lingering pandemic uncertainty. ▪ Moving ahead, though scarce home supply, low interest rates and stock market rally combined may provide some impetus for the housing market, the market's upside may be limited due to several reasons. First, the economic recovery is likely to be slow and gradual as it takes some time for the vaccines to be widely available. In other words, the labor market and investment sentiment may remain sluggish in the near term. Second, as the government has rolled out the supportive measures for local first-home buyers (accounting for 85.4% of total local buyers in November) since early

	2018, there may not be much potential first home buyers left in the market. ▪ In a nutshell, we expect average housing price to rebound by up to 5% yoy in 2021.

RMB	
Facts	**OCBC Opinions**
▪ RMB weakened slightly against the dollar last week as a result of rebound of broad dollar index but the USDCNY stood below 6.50 firmly.	▪ RMB gave up initial gains after the higher than expected USDCNY fixing on Wednesday as market started to worry whether China will increasingly guide the USDCNY in anticipation of seasonal demand for RMB ahead of Chinese New Year holiday.

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