OCBC TREASURY RESEARCH

Greater China – Week in Review

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Highlights: the lost "golden September"

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China's domestic equity market ended higher last week led by property names. Real estate stocks rebounded sharply despite disappointed property sales and weak household sentiment. The traditional **"golden September" failed to materialize** with the average daily property sales in the first ten days of September in 30 major cities fell by 29% yoy, signalling a tough battle ahead to turn around the property market.

In addition, **the latest August credit data reinforced the concern about weak sentiment in the household sector.** Medium to long term loan to household sector only increased by CNY265.8 billion, CNY160 billion below that in August 2021. Household deposit increased by CNY828.6 billion, way above average CNY330 billion increase in August in the past four years. The deteriorating household sentiment remains the key challenge for the Chinese economy.

Nevertheless, real estate stocks outperformed on the back of more policy supports from local governments. Zhengzhou, capital city of Henan province, vowed to restart all the stalled projects within 30 days while Jinan City Development, a state-owned developer in Shandong province announced to purchase 3000 units for affordable rental house to support property market.

On positive note, corporate demand for loans rebounded. In addition**, fiscal policy remained supportive.** Fiscal deposit in August fell by CNY257.2 billion, bucking the trend of seasonal increase. This showed China has stepped up its spending.

China's CPI decelerated unexpectedly to 2.5% yoy in August from 2.7% yoy in July. **The decline of flight ticket prices during the peak season showed the rising costs from China's zero Covid strategy.**

Looking ahead, although food prices are expected to rise further ahead of the festival seasons including mid-autumn in mid-September and National Day holiday, service prices are likely to stay muted due to Covid-19 as China's national health commission encouraged people **to minimize travel during the festival season.** We now expect CPI to stay below 3% for the rest of the year. **We also revised down the whole year CPI forecast to 2.1%, which may open the door for more monetary easing.** We expect more reserve requirement ratio cut in the coming months although we see no urgency for more imminent interest rate cut.

China has stepped up its counter cyclical measures such as the outsized strong daily RMB fixing and the reduction of foreign currency reserve requirement ratio in the past week to slow down RMB depreciation. The daily fixing forecast error without the counter cyclical factors widened to more than 300bps last week. This helped keep the pace of depreciation in check. However, history shows counter cyclical measures are usually not the game changers.

The near-term depreciation pressure remains given the deteriorating trade outlook as well as uncertain growth outlook due to China's zero Covid strategy. Year to date, the dollar index has rallied by about 14% while RMB depreciated against the dollar by only about 8.2%. In other words, RMB has outperformed other major currencies due to China's sizable trade surplus. However, we cannot rule out the risk that RMB weakness may play catchup should China's trade outlook weaken. As such, we think the risk for the USDCNY to break above 7 remains.

In the near term, we will watch out for China's daily fixing. China managed to stabilize RMB back in September and October 2019 after the PBoC flattened the fixing for about two months. Whether PBoC will flatten the daily fixing this time remains to be seen.

Hong Kong's private sector expanded further in August, albeit at the lowest pace since April. PMI fell to 51.2 in August, from that of 52.3 in July, though still remained above the boom-bust line of 50. Output and new orders grew at a decelerated pace, on the back of resurgence in local Covid-19 cases and deteriorating external headwinds. External demand and new businesses from Mainland China shrank further in August, in line with the declining trend in merchandise exports in recent months. Looking ahead, we expect the PMI to fall further as both domestic and external demand weaken, and reopening measures are delayed.

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Key Events and Market Talk

Facts	OCBC Opinions
▪ In the latest State Council meeting, China's policy makers focused on four areas including employment, domestic demand, innovation and infrastructure investment.	▪ China will support the platform economy in keeping employment stable. Financial institutions will be guided to extend special loan support to key platform companies. ▪ In order to boost domestic demand, the meeting also decided to extend loan interest discounts for equipment upgrade and purchase. ▪ For the issuance of CNY500 billion local government special bond from the untapped debt limit, 70% will go to local government while 30% will be used by the central government to support the projects.
▪ PBoC announced on 5 September that it would lower foreign exchange reserve requirement ratio (RRR) for financial institutions by 200 bps to 6%, effective from 15 September.	▪ The FX RRR cut is expected to inject less than US$19 billion into the system which will help banks' ability to meet demand for foreign currency. ▪ However, the move is unlikely to be a game changer as the liquidity injection is small as compared to cross border receipts. Nevertheless, it is a strong signal that PBoC is increasingly more uncomfortable with the recent pace of RMB depreciation. ▪ China has a strong incentive to slow down the pace of RMB depreciation as part of sentiment management amid the rising uncertainty from the property mess and Covid situation.
▪ Jinan City Development, a state owned developer in Shandong province announced to purchase 3000 units for affordable rental house to support property market.	▪ The company plans to purchase the whole block with 100% self-funded capital. The large scale bulk purchase from SOEs could bolster the market sentiment setting the example for other cities to boost the demand.
▪ The Macau's tourism and gaming sector are facing further setback in periods ahead, as China tightened its antivirus measures, including advising against long-distance travel for the mid-Autumn festival and National Day holidays.	▪ The mid-Autumn festival (10-12 September this year) and October Golden Week holiday periods (1-7 October) are usually peak travel seasons. Before the pandemic and social unrest in Hong Kong, in 2018, the total visitor arrivals during October amounted to 1.6 million (accounting for 9.3% of the total arrivals that year). Nonetheless, with the ramped-up antivirus measures in Mainland China, the only place with quarantine-free travel arrangement with Macau, Macau is unlikely to see significant increase in visitors this year. Meanwhile, the number of visitor arrivals from other regions is expected to remain subdued given the 7-day quarantine requirement.

Key Economic News

Facts	OCBC Opinions
▪ China's CPI decelerated unexpectedly to 2.5% yoy in August from 2.7% yoy in July. ▪ PPI also moderated further to 2.3% yoy from 4.2% yoy. ▪ The gap between PPI and CPI inverted for the first time since December 2020.	▪ On sequential basis, CPI fell by 0.1% mom due to the decline of non-food prices, which fell by 0.3% mom as a result of falling oil prices and travel costs hit by the resurgence of Covid19. Petrol and diesel cost fell by 4.8% mom and 5.2% mom respectively, dragging the sequential CPI reading down by 0.2%. In addition, air ticket prices also fell by 7.5% mom despite summer holiday due to Covid-19. ▪ Food prices, however, extended its gain. Of which, pork prices rose by 0.4% while vegetable prices increased by 2% mom due to the extreme hot weather.

	▪ Looking ahead, although food prices are expected to rise further ahead of the festival seasons including mid-autumn in mid-September and National Day holiday, service prices are likely to stay muted due to Covid-19 as government encourage people to minimize travel during the festival season. We now expect CPI to stay below 3% for the rest of the year. We also revised down the whole year CPI forecast to 2.1%. ▪ The decline of flight ticket prices during the peak season showed the rising costs from China's zero Covid strategy. ▪ From policy perspective, it seems that CPI may become less constraint for monetary policy.
▪ China's aggregate social financing rose by CNY2.43 trillion in August. New Yuan loan increased by CNY1.25 trillion. The growth of aggregate social financing stock, however, decelerated to 10.5% yoy from 10.7% yoy. ▪ M2 growth accelerated further to 12.2% yoy in August from 12% yoy in July.	▪ The deceleration of aggregate social financing was mainly attributable to slower issuance of local government special bond and corporate bond. ▪ On positive note, both on-balance sheet lending and off-balance sheet lending rebounded strongly. New Yuan loan increased by CNY1.25 trillion, CNY300 billion above last August level. The improvement of on-balance sheet lending was mainly due to the improving corporate demand thanks to China's interest rate cut in August and more stimulus. Medium to long term loan to corporate increased by CNY735.3 billion, CNY213.8 billion above the level last August. ▪ Nevertheless, sentiment in household sector remained weak. Medium to long term loan to household sector only increased by CNY265.8 billion, CNY160 billion below that in August 2021. Household deposit increased by CNY828.6 billion, way above average CNY330 billion increase in August in the past four years. The deteriorating household sentiment remains the key challenge for Chinese economy. ▪ Fiscal policy remained supportive. Fiscal deposit in August fell by CNY257.2 billion, bucking the trend of seasonal pattern. This showed China has stepped up its spending.
▪ China's exports in dollar term rose by 7.1% yoy in August while imports grew by 0.3% yoy. ▪ Trade surplus narrowed from the record high of US$101.2 billion in July to US$79.3 billion in August. ▪ Total trade growth decelerated to 4.1% yoy in August from 11% yoy in July.	▪ The external demand softened. Exports to the US fell by 3.77% yoy, the first year on year decline since May 2020. ASEAN is the only bright spot with China's exports to ASEAN grew by 25.13% yoy although it moderated to 33.49% yoy. ▪ China's demand for chips weakened further with imports of integrated circuit fell by 12.4% by value. The weak prospect on semiconductor supply chain may further weigh down trade outlook.
▪ Hong Kong's private sector expanded further in August, albeit at the lowest pace since April. PMI fell to 51.2 in August, from that of 52.3 in July, though still remained above the boom-bust line of 50. Output and new orders grew at a decelerated pace, on the back of resurgence in local Covid-19 cases and deteriorating external headwinds.	▪ Firms generally increased levels of purchasing activity and expanded inventories, in the wake of increased demand. Input cost pressure rose further, and companies had passed the higher costs on to their customers. Employment levels declined for a second consecutive month in August as the result of companies' cost-saving efforts. ▪ External demand and new businesses from Mainland China shrank further in August, in line with the declining trend in merchandise exports in recent months. Looking ahead, we expect the PMI to fall further as both domestic and external demand weaken, and reopening measures are delayed.

RMB

Facts	OCBC Opinions
▪ The USDCNH briefly tested 7 and fell due to the retreat of broad dollar index.	▪ China has stepped up its counter cyclical measures such as the outsized strong daily RMB fixing and the reduction of foreign currency reserve requirement ratio in the past week. The daily fixing forecast error without the counter cyclical factors widened to more than 300bps last week. This helped keep the pace of depreciation in check. However, history shows counter cyclical measures are usually not the game changers. ▪ The near-term depreciation pressure remains given the deteriorating trade outlook as well as uncertain growth outlook due to China's zero Covid strategy. Year to date, the dollar index has rallied by about 14% while RMB depreciated against the dollar by only about 8.2%. In other words, RMB has outperformed other major currencies due to China's sizable trade surplus. However, we cannot rule out the risk that RMB weakness may play catchup should China's trade outlook weaken. As such, we think the chance for the USDCNY to break above 7 remains. ▪ In the near term, we will watch out for China's daily fixing. China managed to stabilize RMB in September and October 2019 after the PBoC flattened the fixing for about two months. Whether PBoC will flatten the daily fixing this time remains to be seen.

Treasury Research & Strategy

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