OCBC TREASURY RESEARCH

Greater China – Week in Review

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Highlights: Expectation matters

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The Chinese economy rose by 8.1% yoy in 2021. In nominal term, the economy rose by 12.8% yoy to CNY114.37 trillion. This means the economy is 16% larger than pre-Covid level. This is a remarkable achievement given most of the major developed economies just reached or surpassed pre-Covid levels slightly in 2021.

China has been ahead of the curve in tightening on three macro fronts in 2021 including prudent monetary policy, strict debt management and tightening property measures. What China did differently in 2021 may be partially responsible for the underperformance of China's equity, but it also means more policy ammunition for 2022. You may refer to our special reports published here. The consensus has been reached in the market that growth has been placed in a more important position in China.

PBoC surprised the market with double cuts including both 1-year MLF rate and 7-day reverse repo rate on 17 January although the reduction of 1-year LPR and 5-year LPR on 20 January were in line with expectation. This reinforces the expectation that PBoC is in front loading mode.

PBoC deputy Governor Liu Guoqiang has laid out a most straightforward roadmap on how PBoC plans to support the real economy in the press conference last week. Other than widening the use of its policy tools to prevent credit growth from collapsing, PBoC will become more forward looking to move ahead of the curve. PBoC should respond to market's focus in a timely manner as any delay of response may create larger hurdle in future.

Clearly, **China has stepped up its expectation management** to reassure that high priority has been given to stabilize the economic growth. Since the second half of 2021, confusion about the role of private economy due to regulatory crackdown and property tightening has weakened expectation on the relationship between state and market. The latest rate cuts will help investors to restore their confidence in China.

Given China's policy makers have changed the mindset to meet market expectation, we think China will not hesitate to roll out more easing measures if sentiment sours or economic recovery loses momentum.

Nevertheless, China's renewal of anti-corruption campaign ahead of the 20th National People Congress may unease some investors. The target at the monopoly of online platforms and the collusion between capital and power may raise the confusion again regarding the operating environment of those tech companies.

The earlier than expected front loaded monetary easing failed to stop RMB from strengthening further. RMB has strengthened against both dollar and its major current basket ahead of the Chinese New Year holiday. This was probably due to seasonal demand for RMB. In addition, China's strong trade surplus and persistent demand for RMB assets continued to keep RMB supported. Given RMB's unique value proposition to offer diversification benefit during the Fed tightening cycle, we expect the room for RMB to weaken in the upcoming cycle is likely to be limited.

In addition, China's currency regulator SAFE expects the country's balance of payment and foreign exchange markets to be more resilient to the upcoming Fed tightening cycle due to three factors including flushed onshore dollar liquidity, more attractiveness of RMB assets and limited inflows from cross border dollar loans and trade finance in the current easing cycle.

In **Hong Kong**, labour market firmed up further with jobless rate fell another 0.2 percent point to 3.9% in the three months ending December. Yet, the latest tightening of social distancing measures and Omicrons worries could pose some upside risks to unemployment rate in Hong Kong, in particular for domestic consumption and tourism related sectors. The officials have warned that COVID-19 infections could be growing exponentially in the city, with 140 cases reported on Sunday, the highest daily number in more than one year.

More clarity on **Macau's** gaming law has calmed market's nerve, pushing casino operators' share price to recent highs. Yet, in order to sustain economic recovery, Macau needs friendly gaming law, as well as more tourists. For 2021, the total visitor arrivals surged by 30.7% over the extremely low base a year ago, but remained 80.4% below the pre-pandemic level. Prospects of gaming sector continued to be haunted by the lingering pandemic, slowing Chinese economy and turned away VIPs in the near term. On a positive note, China plans for a steady development of inbound and outbound travel once the international spread of Covid-19 is under control, could bring good news to Macau.

Key Events and Market Talk	
Facts	**OCBC Opinions**
▪ China's currency regulator SAFE expects the country's balance of payment and foreign exchange markets to be more resilient to the upcoming Fed tightening cycle.	▪ SAFE's optimism is based on three factors including flushed onshore dollar liquidity, more attractiveness of RMB assets and limited inflows from cross border dollar loans and trade finance in the current easing cycle. ▪ First, China's foreign currency deposits increased by US$160 billion in the past two years providing the buffer to the change of Fed balance sheet. ▪ Second, the low correlation between Chinese assets and foreign assets as well as China's further openness of its financial market foreign investors may continue to provide diversification benefit in the upcoming tightening cycle. ▪ Third, the growth of capital inflows from cross border foreign currency loan and trade finance was much smaller compared to the previous easing cycle from 2009-2013. As such, the pressure for deleverage is much smaller as compared to before.
▪ China's State Council announced to extend some expired tax and fee cuts.	▪ 11 preferential tax and fee policies involving technology, job creation, business startup, medical care etc to the end of 2023. IN addition, China will also strengthen the supply of coal, electricity, oil, gas and transportation services during the upcoming Spring Festival.
▪ China concluded its sixth plenary session of the 19th CPC Central Commission for Discipline Inspection. ▪ China renewed its anti-corruption campaign ahead of the 20th National People's Congress.	▪ China will strengthen investigation and punishment the disorderly expansion of capital and monopoly of some online platforms to cut off the collusion between capital and power. ▪ In addition, the meeting also said it will show no mercy to the persons who try to build political gangs, small circles and interest groups. ▪ The target at the online platforms and the collusion between capita and power may raise the confusion again regarding the operating environment of those tech companies.
▪ China's 1-year LPR was fixed lower by 10bps on 20 January following a surprise reduction of 1-year MLF rate on 17 January. ▪ In addition, 5-year LPR was also fixed lower by 5bps.	▪ Although 5-year LPR is not tailored to any sector, the reduction of 5-year LPR is still a relief to China's property sector given China's mortgage rate is pegged to 5-year LPR. ▪ With China's policy setting shifts to expectation management, China will not hesitate to roll out more easing measures in the first quarter.
▪ During the press conference on 18 January, PBoC's deputy Governor Liu Guoqiang has laid out a clear roadmap on PBoC's plan to support the real economy in 2022.	▪ In order to stabilize the economy, PBoC will focus on three areas. First, PBoC would widen the use of its policy tools to prevent credit growth from collapsing. Second, financial institutions should be more proactive to roll out the targeted measures to look for the good projects and optimize the economic structure. Third, PBoC will front load its policies and become more forward looking to move ahead of the curve. PBoC should respond to market's focus in a timely manner as any delay of response may create larger hurdle in future.
▪ The International Monetary Fund (IMF) called on the government to roll out another round of relief measures, including digital consumption voucher scheme and social welfare assistance, to vulnerable individuals and businesses. The IMF also noted that the recovery of local economy	▪ According to IMF, despite its "Covid zero" policy, Hong Kong remained as an international financial centre, given the resilient domestic economy, unscathed institutional strength, and potential inclusion into the RCEP. On housing prices, IMF believed Hong Kong's property market is unlikely to see drastic price correction notwithstanding policy normalization around

(+6.9% yoy in the first three quarter of 2021) was largely uneven, with private consumption lagging other components. Given the uncertainties facing the global economy, premature withdrawal of fiscal stimulus could derail economic recovery. A gradual return to a balanced budget would be more desirable.	globe, citing prudent demand side management measures and sufficient buffer. All in all, the balance of risks facing Hong Kong's economy are tilted to the downside.

Key Economic News	
Facts	**OCBC Opinions**
▪ The Chinese economy decelerated further to 4% yoy in the fourth quarter from 4.9% yoy in the third quarter, better than market expectation.	▪ On sequential basis, the Chinese economy grew by 1.6% qoq in 4Q after China revised up previous three quarters qoq readings to 0.3%, 1.3% and 0.7% from 0.2%, 1.2% and 0.2% respectively. For the whole year of 2021, the Chinese economy grew by 8.1% yoy. On two-year average adjusting for the pandemic distortion, China grew by 5.1% yoy on average in the past two years, within the reasonable range of trend growth. ▪ In nominal term, the Chinese economy rose by 12.8% yoy to CNY114.37 trillion. This means the economy is 16% larger than pre-Covid level while most of the major developed economies just reached or surpassed pre-Covid levels slightly in 2021.
▪ Hong Kong: Hong Kong's jobless rate fell another 0.2 percent point to 3.9% in the three months ending December, down from 4.1% seen in September-November. Over the same period, underemployment rate edged down to 1.7%, from 1.8% in the previous month.	▪ Comparing to that in September-November, notable declines in unemployment rates were seen in retail, accommodation and food services sectors (down 0.9 percentage point to 5.4%) and construction sector (down 0.5 percentage point to 5.1%), likely due to the improved consumption sentiment and sustained economic recovery. Yet, it is noted that the tightness in labour market can also be attributed to the continuous decline in labour force since July 2019. ▪ The latest tightening of social distancing measures and Omicrons worries could pose some upside risks to unemployment rate in Hong Kong, in particular for domestic consumption and tourism related sectors. In the near term, we expect the pace of recovery for labour market may start to slow down or even pause, while further decline below from the pre-pandemic level of sub-3% may remain unlikely by the end of 2022.
▪ Hong Kong: Hong Kong's headline composite CPI rose by 2.4% yoy in December, notably higher than that of November at 1.8%, partly due to the lower base of comparison a year ago during the fourth wave of infection. The rising food and utility bills continued to weigh on living costs, while rental cost fell further. Going forward, we expect the inflation to stay largely tame amid local Omicron outbreak, despite some external price pressures.	▪ Analyze by component, enlarged year-on-year increases for electricity, gas and water (+54.2% yoy), clothing and footwear (+8.7% yoy) and meal outs and takeaway food (+3.7% yoy), pushed up the inflation in December. Netting out the effect of government's one-off relief measures, the underlying inflation picked up to 1.4% yoy in December (+1.2% yoy in November). For 2021 as a whole, the underlying CPI rose by a record low of 0.6% over the previous year, as the underlying rental cost saw decline (-0.7% yoy) for the first time since the data series started in 2007. ▪ Going forward, we expect the inflation to stay largely tame as consumption activities likely to be dented by local epidemic situation. Nonetheless, some external price pressures may loom, owing to pandemic induced logistic disruptions both in the Mainland and overseas.

▪ Macau: Macau's gaming revenue grew marginally by 1.7% qoq in the last quarter, against the backdrop of intensified crackdown on junket. VIP revenue dropped 17.8% qoq to MOP4.5bn in the fourth quarter last year, while that of mass market including slot machines rose by 12.3% qoq. Subsequently, the share of mass sector (including slot machines) rose to record high of 68.3%, from that of 62.5% in the third quarter. ▪ Macau: The Legislative Assembly published the draft bill on amendments to gaming law, outlining the ban on dedicated junket rooms and revenue sharing arrangements between junkets and casino's concessionaires.	▪ For the full year of 2021, the share of VIP to total gross gaming revenue fell to 32.8%, from that of 43.5% last year. With more casino operators ceasing collaboration with junkets, the ratio is set to decline further. Leaving any further rooms to grow for the gaming revenue in the future entirely to the mass market sector. ▪ On regulatory front, under the proposal on gaming law amendment, the government will continue issuing junket licenses to approved VIP promoters but will restrict each licensed promoter to "only carry out the activity of promoting games in one concessionaire".
▪ Macau: Visitor arrivals increased by 24.5% yoy or 2.4% mom to 820,870 in December 2021, conceivably due to hosting of mega-sized events which drew more visitors to Macau. Zooming in, the share of overnight visitors in total visitor arrivals rebounded from 35.9% in November to 48.0% in December. For 2021, the total visitor arrivals surged by 30.7% over the extremely low base a year ago, but remained 80.4% below the pre-pandemic level.	▪ As more local cases were detected in in Guangdong (i.e. Shenzhen and Zhuhai), the major source of tourists, Macau's tourism sectors in January and February this year is likely to bring to a standstill. Our rhetoric hence repeats again, that Macau's economic recovery will remain bumpy due to the strict implementation of "Covid zero" strategy in the region and lingering pandemic. Before the end of pandemic, we expect to see more relief measures by the government to lessen the pain felt by the tourism and gambling related sectors.

RMB	
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▪ The USDCNY ended the week below 6.35 for the first time since the start of the US-China trade war.	▪ The earlier than expected front loaded monetary easing failed to stop RMB from strengthening further. RMB has strengthened against both dollar and its major current basket ahead of the Chinese New Year holiday. This was probably due to seasonal demand for RMB. In addition, China's strong trade surplus and persistent demand for RMB assets continued to keep RMB supported. ▪ Given RMB's unique proposition to offer diversification benefit during the Fed tightening cycle, we expect the room for RMB to weaken in the upcoming cycle is likely to be limited.

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