Greater China – Week in Review

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Highlights: China exceptionalism?

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For most market watchers including myself, US exceptionalism is a term we use on the regular basis to explain the market movement in the US. The equity market rally in early January this year despite the US Capitol Hill being stormed by Trump supporters reinforced expectation about US exceptionalism. Frankly speaking, I am not quite sure whether there is any country in the world which can see their equity market rally while its Congress be briefly occupied by protesters.

For long, we have not even thought about thinking about the term "China exceptionalism". Nevertheless, we started to witness some interesting changes since the pandemic. Although Covid-19 first emerged in China, the decisive and effective containment measures have brought the country back to normal within a short timeframe, turning crisis into opportunity. The latest survey conducted by research team from York University in Canada showed that Chinese citizens' trust in their national government increased to 98%. 49% respondents said they had become more trusting in the national government since the pandemic started while only 3% reported the decline of trust.

China's tight border control and strong containment measures have kept China largely isolated from a few waves of new mutations. This makes China continue to enjoy its prolonged first in first out benefit. The concept of "China exceptionalism" could become a new reaction function in the market that when there is resurgence of virus in some parts of the world, Chinese trade sector could benefit. RMB has probably been one of the key beneficiaries of this exceptionalism.

Despite still low inoculation rate, Chinese domestic residents can still enjoy the freedom of mobility without worrying too much about the virus. China's domestic trips soared by almost 120% yoy to 230 million during the five-day Labor Day holiday on the back of pent-up demand for travel. The number of total trips this year was 3.2% above the same period before the pandemic although domestic tourism revenue has not retuned to pre-pandemic level, which was still 23% below the same period in 2019.

On trade, China's total trade rose to US$484.9 billion in April, second highest in record after a record reading of US$486.3 billion in December 2020. China's total trade with ASEAN hit a record high of US$72.47 billion in April, reinforcing ASEAN's position as China's largest trading partners. Trade surplus widened to US$42.86 billion from US$13.798 billion in March.

On imports, commodity remained the key driver to surge of China's import growth in the past two months. Imports of crude oil and Iron Ore by value surged by 73.18% yoy and 89.56% yoy respectively. However, imports of crude oil by volume fell by 0.18% yoy in Aril while imports of iron ore by volume only rose by 2.98% yoy. This shows that the surge of commodity imports was mainly the result of base effect.

China's overall balance of payment remained supportive. China's current account surplus as % of GDP stabilized around 2% in the first quarter as service trade deficit continued to narrow. In addition, inflows of foreign direct investment also remained strong.

On international relationship, China headline dominated the G7 foreign minister meeting last week. Uncertainty is likely to be the key word. On China-EU, there is flipflop of news about efforts to ratify the investment deal. On China-US, the Biden Administration may carry on some of measures announced by former US President Trump to limit the US investments in certain Chinese companies. On China-Australia, China announced to suspend indefinitely all activities under China-Australia Strategic Economic Dialogue.

In **Hong Kong,** 1Q GDP growth surprised on the upside at 7.8% yoy. However, private consumption and fixed investments remained far below the levels of 1Q 2019 despite some improvements. Worse still, frozen inbound tourism remained a drag. The weaker than expected retail sales growth in March also indicates that the stabilization of local consumption was not enough to offset the stalling tourist spending. Elsewhere, PMI for private sector fell slightly from 50.5 in March to 50.3 in April. This suggests that business conditions have improved while the worst may have been over for the labour market. However, new export orders and new business from Mainland China continued to decrease as some businesses may have remained in doldrums. Meanwhile, the rate of job creation softened slightly in April, signalling only moderate recovery of the labor market. In a nutshell, on top of the buoyant external demand and the strong fiscal supports including the upcoming e-consumption vouchers, further improvement in local consumption and the revival of exports of services may be needed for a stronger economic recovery. Assuming that vaccine rollouts would accelerate and in turn warrant further relaxation of social distancing measures and border controls, retail sales may grow by around 15% yoy while the economy may expand by 5%-6% in 2021.

On the financial market front, China announced more details about the wealth management connect for the Greater Bay Area. Taking Mutual Recognition of Funds as a reference, we expect to see net inflows from Mainland China to Hong Kong under the new investment link at least at the early stage. If this is the case, it may help to improve CNH liquidity and boost HKD demand, in turn helping to cap the HIBOR's downside.

In **Macau,** daily average of visitor arrivals during Labor Day Holiday was up 25.4% from that in April. However, it was merely 21.1% of the level in the same period of 2019. This confirms the fact that inbound tourism continued to recover but still at a moderate pace.

Key Events and Market Talk	
Facts	**OCBC Opinions**
▪ China's top economic planner NDRC announced last week that it is suspending indefinitely all activities under the China-Australia Strategic Economic Dialogue.	▪ The China-Australia Strategic Economic Dialogue which was first launched in 2014 aiming to promote the communication on key bilateral investment and economic areas. The suspension clearly showed the further deterioration about bilateral relationship. Nevertheless, the ministerial level communication channel remains open. As such, it remains to be seen whether there will be any more concrete economic impacts on both countries.
▪ China announced more details about the wealth management connect for the Greater Bay Area.	▪ For the new connect scheme, both the maximum net northbound inflows and the maximum net southbound inflows are not allowed to exceed the aggregate quota which is tentatively set at RMB150 billion. The individual investment quota is RMB1 million. On the one hand, eligible residents in the nine cities of Guangdong who have more than two-year investment experience and no less than RMB1 million net financial assets or no less than RMB2 million financial assets over the past three months will be allowed to invest in southbound wealth management products. On the other hand, the eligible investors in Macau and HK can invest in northbound non-principal protected wealth management products and mutual funds with relatively low risks. ▪ If taking Mutual Recognition of Funds as a reference where cumulative net subscription for Mainland funds and Hong Kong funds reached RMB0.66 billion and RMB15.06 billion respectively as of end-March 2021, we expect to see net inflows from Mainland China to Hong Kong under the new investment link at least at the early stage. If this is the case, the new connect scheme may help to improve CNH liquidity and boost HKD demand.

Key Economic News	
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▪ China's export in April surged by more than expected 32.3% yoy while import growth accelerated further to 43.1% from 38.1% in March. ▪ Trade surplus widened to US$42.86 billion from US$13.798 billion in March.	▪ China's total trade rose to US$484.9 billion in April, second highest in record after a record reading of US$486.3 billion in December 2020. China's total trade with ASEAN hit a record high of US$72.47 billion in April, reinforcing ASEAN's position as China's largest trading partners. Total trade between China and ASEAN in the first four months of 2021 accounted for 14.7% of China's total trade, higher than 14% share of China EU trade and 12.4% share of China US trade. The increasingly strong intra-regional activity is supportive of regional development. ▪ Demand from US and EU remained strong with exports to US and EU rose by 31.16% and 23.81%yoy respectively. ▪ On imports, commodity remained the key driver to surge of China's import growth in the past two months. Imports of crude oil and Iron Ore by value surged by 73.18% yoy and 89.56% yoy respectively. However, imports of crude oil by volume fell by 0.18% yoy in Aril while imports of iron ore by volume only rose by 2.98% yoy. This shows that the surge of commodity imports was mainly the result of base effect. Given

	raw material prices continue to rise and China's reluctance to boost infrastructure investment, we think China's demand for commodity may soften in the coming months.
▪ China's FX reserve rebounded by US$28.2 billion to US$3.1982 trillion in April.	▪ The rebound was mainly the result of valuation effect as the US dollar weakened in April, which drove up the valuation of non-dollar assets in China's portfolio.
▪ China's current account surplus remained sizeable at US$75.1 billion in the first quarter. ▪ Under capital account, surplus of direct investment widened to US$70.5 billion.	▪ Service trade deficit continued to narrow in the first quarter to US$22.3 billion from US$47 billion in the first quarter of 2020. ▪ Current account surplus as % of GDP at 2% remained within a reasonable range. ▪ Foreign direct investment in the first quarter rose to US$93.1 billion, highest since March 2013. However, overseas direct investment fell to US$22.6 billion.
▪ Hong Kong's 1Q GDP expanded at the fastest pace in 11 years by 7.8% yoy (or 5.3% qoq S.A.), ending six consecutive quarters of contraction and far better than expected.	▪ Apart from low base effect, the strong recovery was mainly driven by external demand revival (exports of goods advanced by 30.6% yoy), extension of fiscal stimulus (government expenditure grew by 6.7% yoy) as well as improvement of local consumption (private expenditure rose for the first time since 2Q 2019 by 1.6% yoy) and fixed investments (up for the second consecutive quarter by 4.5% yoy). ▪ However, if taking a two-year average to net out the base effect, GDP, private consumption, fixed investments and exports of services were lower than the levels of 1Q 2019. In other words, Hong Kong's economic recovery is still uneven and incomplete. ▪ Going ahead, the economy may continue to regain steam on the buoyant external demand and the strong fiscal supports including the upcoming e-consumption vouchers. Nonetheless, for the economy to show stronger recovery, we may need to see further improvement in local consumption and the revival of exports of services, both of which will hinge on the pace of vaccine rollout. ▪ In a nutshell, since 1Q GDP surprised to the upside, we upgrade our 2021 GDP forecast from 4.1% yoy to 5%-6% yoy on assumption that border controls will be further relaxed in 2H.
▪ Hong Kong's retail sales surprised to the downside with a growth of 20.1% yoy in March.	▪ Though the sales value of clothing, footwear and allied products (+75.5% yoy), goods in department stores (+2.2% yoy) and jewlery, watches and clocks (+81% yoy) and other consumer goods (+27.8% yoy) grew amid low base effect, they were all fall from the levels of March 2019. This indicates that the stabilization of local consumption was not enough to offset the stalling tourist spending. Also notable is that the sales of goods in supermarkets normalized amid the subsided local infections and therefore dropped for the third consecutive month by 16.1% yoy amid high base effect. ▪ Going ahead, the upcoming e-consumption vouchers may lend some support to the retail sector. However, the retail sector may not see full recovery until containment measures are further loosened and the labor market improves. Assuming that vaccine bubbles will help to accelerate the vaccine rollouts and in turn warrant further relaxation of social distancing measures and border controls, we hold onto our view that retail sales may grow by around 15% yoy in 2021,

	which however is still over 10% lower than the level of 2019.
▪ Hong Kong's PMI for private sector fell slightly from 50.5 in March to 50.3 in April. New orders stabilized and ended three years of declines while business activity expanded for the first time in more than three years. Meanwhile, business confidence rose to the highest since February 2014 and employment advanced for the third consecutive month.	▪ This reinforces the fact that business conditions improved amid the subsided local infections, the relaxation of local social distancing measures and vaccine rollout. The data also suggests that the worst may have been over for the labour market. ▪ However, new export orders and new business from Mainland China continued to decrease. This indicates that some businesses may have remained in doldrums amid lingering pandemic uncertainty, the slow vaccine rollout in Asia and the ongoing border controls. Also notable is that the rate of job creation softened slightly in April. Besides, though purchase cost increased at the fastest pace in 34 months and labour costs also rose, companies continued to cut selling prices amid fierce competition. Taken all together, it shows that the pace of recovery in both business conditions and labour market remains moderate. As such, local inflationary pressure may remain contained in the near term.
▪ Hong Kong's exchange fund posted a mild investment income of HK$11.6 billion in 1Q 2021, down 89% qoq.	▪ Bonds investments which locked in a huge loss of HK$16 billion in 1Q amid surging long-term government bond yields on inflation and tapering fears. On the other hand, the investment return of HK equities and overseas equities reached HK$7.6 billion (-68% qoq) and HK$18.8 billion (-66% qoq) respectively. The strong gains in global equities during January were largely wiped out in the following two months amid rising US Treasury yields and concerns about the PBOC's pre-mature tightening. Finally, foreign exchange income dropped over 93% qoq to HK$1.2 billion as the broad dollar index rose during the first quarter. ▪ Going ahead, as both the Fed and the PBoC have no intention to adjust the monetary policy in the near term, global bond market may not have much downside while global equity market may consolidate. On the other hand, broad dollar index is expected to trade in range. In conclusion, we expect exchange fund to see moderate investment return for another quarter in 2Q.
▪ Hong Kong's housing price index rose for the fourth consecutive month by 2.6% yoy to the highest since July 2019 in March. As of 2nd May, another secondary home price tracker CCL index also climbed to the highest since September 2019, just 3.8% away from historical high. ▪ Housing transaction volume increased for the 11th consecutive month and surged by 78.6% yoy to 7325 deals in April. Approved new mortgage loans rose for the seventh consecutive month by 60% yoy in March.	▪ The strong growth of the housing market was mainly attributable to subsided local infections, low local rates and the persistent imbalance between supply and demand. Regarding supply, housing completion plunged by 41% yoy to 2200 units in 1Q while housing construction (+144.4% yoy to 2200 units in 1Q) was still much lower than the same period average of 4920 units over the past five years. ▪ Moving ahead, we do expect the housing market to remain resilient as local rates may stay low for some time given Fed's dovish tone while home supply may remain scarce in the short to medium term. However, some negative factors may cap the upside of housing prices. First, the sliding housing rental (down for the 18th straight month in March) amid the reduction in foreign workers and students as well as the elevated unemployment rate. Second, the selling pressure from small businessowners and the emigrants may have been the reason behind the lagged price growth of the medium to large homes (100-159.9 square meters). As such, in the near

	term, the housing market may remain divided. Should containment measures be relaxed and support economic recovery, further rebound in local demand and the return of external demand may buoy a more balanced housing market. In conclusion, we tip an up to 5% yoy increase in housing price index by the end-2021.
▪ Macau: daily average of visitor arrivals during Labor Day Holiday reached 33,431, up 158.2% from that during Lunar New Year and up 25.4% from that in April. Hotel occupancy rate also climbed to 83.2%.	▪ However, the daily average of visitor arrivals was merely 21.1% of the level in the same period of 2019. This confirms the fact that inbound tourism continued to recover but still at a moderate pace.

RMB	
Facts	**OCBC Opinions**
▪ The USDCNY tumbled to 6.41-42 range last Friday on the back of collapse of US dollar.	▪ RMB index hovered around recent high of 97 as market expected China's export sector to benefit from the recent new wave of virus in Asia.

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