# OCBC TREASURY RESEARCH

## Greater China – Week in Review

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## Highlights: three factors supporting RMB

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China's equity market managed to end higher despite still fragile sentiment last week after China stepped up its tightening in gaming sector. RMB also gained with the USDCNY ended the week below 6.45 on the back of three factors including hawkish message from PBoC official, resumption of US-China dialogue and resilient trade data.

In the press conference last week, PBoC's director of monetary policy said effective expectation management has reduced the preemptive demand for liquidity. As such, liquidity needed to keep money market stable has been lower than before. Overall, price of money rather than quantity of money is the better gauge for liquidity. As long as DR007 remains stable, PBoC is comfortable with overall liquidity situation. His comment dialled back market expectations on imminent easing.

The 90-minutes phone call which was initiated by President Biden showed the change of approach by the US administration after the recent visits to China by deputy Secretary of State Sherman and Special climate envoy Kerry failed to yield significant progress.

President Xi's comments that "getting the relationship right is not optional, but something we must do and must do well" also sent a clear message about China's commitment to repair the bilateral relationship.

The call also showed that President Biden has a non-binary view of the US-China relationship. The communication on the ground level after the call is likely to improve.

The focus in the coming months is likely to shift back to trade issues although President Xi did not make a specific demand for the US to lift tariffs in the phone call. The latest news that Biden Administration may launch an investigation into Chinese industrial subsidies under section 301 together with its allies may again put the bilateral trade relationship under test.

On economic data. China's goods trade continued to surprise on the upside in August with total trade hit a record high of US$530.3 billion. The recent outbreak of delta variants in ASEAN may prolong China's first in first out benefit as a result of pause of supply chain shift.

On inflation, the gap between PPI and CPI widened to a record high of 8.7%, signalling mounting pressures for profit margins for the downstream companies. Although elevated PPI argues for limited room for further easing, the mounting pressures faced by SMEs in the downstream may be the catalyst for Chinese central bank to cut RRR to support the real economy against the backdrop of muted transmission from PPI to CPI.

China's credit growth in August remained sluggish. Stock of aggregate social financing growth decelerated further to 10.3% from 10.7% in July. The gap between M2 and M1 widened further to 4% from 3.4% in July, a sign that corporate is cautious about future outlook. Meanwhile, the faster than expected deceleration of M1 growth was also the result of weaker property market.

**China rolled out a number of measures dedicated to the further integration of Greater Bay Area last week** including the plan to build a Guangdong-Macau in-depth cooperation zone in Hengqin and the new development plan for Qianhai. Specifically, the corporation zone in Hengqin will be built with an aim to support Macau's economic diversification, facilitate Macau residents' life and employment, enrich the practice of "one country, two systems" and connect Macau and Zhuhai to promote the development of the Greater Bay Area. The focus of modern finance development in Macau is to support the cooperation between China and the Portuguese-speaking countries, promote the financial integration between Macau and Guangdong, as well as strengthen the soft infrastructure (financial services) needed to attract companies and talents.

On the other hand, the expansion of the Qianhai economic zone may bolster the cooperation between Hong Kong and Shenzhen in terms of education, finance, high tech, medical services, legal services etc. We will monitor the upcoming 2021 Policy Address to see if there are details of Hong Kong's plan to promote the GBA's integration.

On top of these, **financial integration among the Greater Bay Area** also sees new progress as southbound bond connect, wealth management connect and Shenzhen government's first offshore bond issue will come soon. Furthermore, HK Green Finance Association hinted that they are studying the feasibility of building a united carbon market for the Greater Bay Area.

Elsewhere, both Hong Kong and Macau are set to loosen the travel restriction measures. Hong Kong will allow local residents from Mainland China and Macau as well as non-local residents from these two places to enter without being subject to mandatory quarantine. Meanwhile, Macau will allow Hong Kong's non-local residents who have got permits to stay, work or study in Macau to enter, subject to 14-day quarantine. These measures may not be a game changer but may pave way for further border reopening between the two cities.

| Key Events and Market Talk | |
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| **Facts** | **OCBC Opinions** |
| ▪ The 90-minute phone call between US President Biden and Chinese President Xi reiterated the need to avoid the conflict amid global competition. | ▪ The phone call which was initiated by President Biden showed the change of approach by the US administration after the recent visits to China by deputy Secretary of State Sherman and Special climate envoy Kerry failed to yield significant progress.<br>▪ President Xi's comments that "getting the relationship right is not optional, but something we must do and must do well" also sent a clear message about China's commitment to repair the bilateral relationship.<br>▪ The call also showed that President Biden has a non-binary view of the US-China relationship. The communication on the ground level after the call is likely to improve.<br>▪ The focus in the coming months is likely to shift back to trade issues although President Xi did not make a specific demand for the US to lift tariffs in the phone call. |
| ▪ Director of PBoC monetary policy department said in the latest press conference that the gap for monetary base is not big. | ▪ PBoC believes that effective expectation management has reduced the preemptive demand liquidity. As such, the liquidity needed to keep money market stable has been lower than before. Against this backdrop, PBoC suggests the use of excessive reserve to gauge the market liquidity may not be as accurate as before. As such, price of money rather than quantity of money is the better gauge for liquidity. As long as DR007 remains stable, PBoC is comfortable with overall liquidity situation.<br>▪ The latest comments may dial back market expectations on imminent easing policy. |
| ▪ HKMA announced the Implementation Arrangements for the Cross-boundary Wealth Management Connect Pilot Scheme in the Guangdong-Hong Kong-Macau Greater Bay Area. Hong Kong bank and partner with different Mainland Chinese banks under the Southbound and Northbound scheme respectively. | ▪ For southbound, the available wealth management products will include 1) Hong Kong-domiciled SFC-authorised funds, 2) bonds; and 3) RMB, HKD and other currency deposits. According to SFC, the number of Hong Kong-domiciled SFC-authorized funds increased by 6% yoy to 810 as of end-2020. HKMA's official hinted that there are over 20 banks showing interests in participating in the scheme and he expects that there will be about 200 wealth management products eligible for sale under southbound scheme.<br>▪ Wealth Management Connect scheme will be launched 30 days after the details are announced. As such, the scheme may be launched during mid-October to November. According to the HKMA's official, high-net-worth households in the Greater Bay Area take up over 20% of those in China as a whole. This together with the previous survey which shows most prospective investors' great interests in Hong Kong's funds indicates that the new connect scheme may translate into huge business opportunities for Hong Kong's banking industry.<br>▪ Notably, Hong Kong customers are required to travel to Mainland China to complete the account opening procedures before investing via the northbound scheme. However, the border control remains in place. As such, we will see if northbound scheme could also allow remote account opening by attestation like southbound scheme. This initiative may set |

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| | the basis for future cross-border investment such as insurance connect, etc. |
| ▪ Hong Kong's Chief Executive Carrie Lam hinted that Shenzhen government will issue the first China's local government bond in Hong Kong in October. | ▪ With China's local government participating in offshore RMB bond market, it will help to improve the yield curve of RMB bonds in Hong Kong, support RMB internationalization and promote the collaboration among the Greater Bay Area. However, given the relatively small issue size (no more than RMB5 billion), it is unlikely to have material impact on offshore yuan market. |
| ▪ China announced the new development plan for Qianhai to bolster the economic integration of the Greater Bay Area. China will expand Shenzhen's Qianhai economic zone eight times. | ▪ The expansion of the Qianhai economic zone may bolster the cooperation between Hong Kong and Shenzhen in terms of education, finance, high tech, medical services, etc. Regarding financial integration, this economic zone may be an innovative testing ground for financial connect schemes, cross-border use of RMB and FX management and cross-border trade of commodity spot. According to the plan, we may expect Hong Kong to continue playing an important role to support China with its expertise in professional services and its unique status as international financial sector. China may also help to mitigate Hong Kong's constraints including scarce land supply and the relatively slow development of high-tech sector |
| ▪ China announced the plan to build a Guangdong-Macau in-depth cooperation zone in Hengqin, which will mainly support Macau's economic diversification, facilitate Macau residents' life and employment, enrich the practice of "one country, two systems" and connect Macau and Zhuhai to promote the development of the Greater Bay Area. | ▪ For economic diversification, Macau and Hengqin will together develop technology research, high-end manufacturing, traditional Chinese medicine and other Macau's local signature businesses, culture and tourism, conventions and exhibitions, as well as modern finance (including innovation in wealth management connect, bond market and finance lease, etc.). Supportive measures including preferential tax policies will be implemented to attract companies and talents. There will be relaxed rules on trade of goods, cross-border travel, cross-border financial management, market access and cross-border flow of online data.<br>▪ As Covid-19 outbreak and China's crackdown on overseas gambling have impeded the recovery of Macau's two pillar industries including tourism and gaming, it is imminent for the city to diversify the economy. During the course of economic diversification, we may see deeper collaboration between Macau and the rest of Greater Bay Area. For example, Hong Kong may be taken as a reference to develop modern finance in Macau.<br>▪ The focus of modern finance development in Macau is to support the cooperation between China and the Portuguese-speaking countries, promote the financial integration between Macau and Guangdong, as well as strengthen the soft infrastructure (financial services) needed to attract companies and talents. As such, it is unlikely to threaten Hong Kong's role as the key financial centre to connecting China and the world. |
| ▪ The Return2hk Scheme for Hong Kong residents from Mainland China and Macau has resumed from 8th September. Meanwhile, the Come2hk scheme for non-local residents from Mainland China and Macau will be launched on 15th September with a quota of 2000 visitor arrivals per day. Visitor arrivals under the two schemes | ▪ This is unlikely to be a game changer for the subdued tourism-related sectors of Hong Kong as these schemes are unilateral and the application for exit/entry permit for travelling to and from HK has not yet resumed in China.<br>▪ Nevertheless, if it paves way for further reopening of the border with Macau, Guangdong or China as a whole, the resumption of cross-border travel may provide additional |

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| will be exempted from mandatory quarantine. | impetus for Hong Kong's economic recovery. |
| ▪ Macau will allow Hong Kong's non-local residents who have got permits to stay, work or study in Macau to enter. These visitors should have been fully vaccinated and will be subject to 14-day quarantine. Application will start from 15th Sep. | ▪ This together with HK's Come2HK scheme may pave way for further border reopening between the two cities. |
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## Key Economic News

| Facts | OCBC Opinions |
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| ▪ China's CPI in August decelerated further to 0.8% yoy from 1% yoy in July.<br>▪ However, PPI accelerated to 9.5% yoy in August from 9% in July. | ▪ On sequential basis, China's CPI rose by 0.1% month-on-month, down from 0.3% mom in July. For breakdown, CPI food prices rose by 0.8% mom while non-food prices fell by 0.1% mom. The rise of food prices led by increase of vegetable and egg prices due to floods was partially offset by the decline of non-food prices due to falling oil prices and travel related costs as a result of sporadic outbreak of delta variant in August. Core CPI decelerated to 1.2% yoy in August from 1.3% yoy in July.<br>▪ China's PPI hit the highest level since August 2008 due to rising raw material prices. PPI rose by 0.7% mom, mainly driven by raw material prices for production, which grew by 0.9% mom while raw material prices for living was flat.<br>▪ Looking ahead, China's CPI is expected to stay low in September due to base effect. However, PPI may test higher further as commodity prices remained elevated.<br>▪ The gap between PPI and CPI widened to a record high of 8.7%, signalling mounting pressures for profit margins for the downstream companies. Although elevated PPI argues for limited room for further easing, the mounting pressures faced by SMEs in the downstream may be the catalyst for Chinese central bank to cut RRR to support the real economy against the backdrop of muted transmission from PPI to CPI. |
| ▪ China's goods trade continued to surprise on the upside in August. Export in dollar term rose by 25.6% yoy while import in dollar term increased by 33.1% yoy.<br>▪ China's total trade hit a record high of US$530.3 billion in August. | ▪ The strong export growth in August was mainly supported by strong demand from advanced economies including Europe, US and Japan. Noting that exports to Europe, US and Japan accelerated to 29.4% yoy, 15.5% yoy and 19.5%. In contrast, demand from ASEAN consolidated in August. The recent outbreak of delta variants in ASEAN may prolong China's first in first out benefit as a result of pause of supply chain shift.<br>▪ On imports, the decline of imports of key commodities by volume including crude oil and iron ore narrowed significantly to 6.2% yoy and 2.9% yoy from previous contraction of 20%. Against the backdrop of base effect, imports of crude oil and iron ore by value surged by 59.77% and 95% yoy respectively.<br>▪ Looking ahead, we remained cautious on China's export outlook due to two reasons. First, the recent decline of China's export order index of PMI showed softening external demand may eventually weigh on China's export growth. Second, the recent improvement of Covid-19 situation in some countries in Asia may also redirect some orders back to their home markets. Nevertheless, China's exceptionalism in terms of virus containment measures indicate that China's trade slowdown is unlikely to be significant. |

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| ▪ China's credit growth in August remained sluggish. Stock of aggregate social financing growth decelerated further to 10.3% from 10.7% in July.<br>▪ Both M2 growth and M1 growth slowed down to 8.2% yoy and 4.2% yoy respectively from 8.3% yoy and 4.9% yoy in July. | ▪ The tightening grip in property space has further weighed down on credit growth. China's medium-term loan to household rebounded slightly to CNY425.9 billion in August from CNY397.4 billion in July. However, it is lower than seasonal pattern for August.<br>▪ In addition, loan growth in August was also affected by the resurgence of virus with short term loan to household also slowed due to falling people mobility.<br>▪ Loan to corporate sector rebounded in August. However, it was mainly supported by short term bill financing with medium term loan to corporate falling short of the level in the same time last year. Nevertheless, given China has stepped up its support to SMEs funding needs, loan to corporate may recover gradually.<br>▪ For the break down of aggregate social financing, the local government bond issuance accelerated to CNY973.8 billion in August, but still short of CNY1.379 trillion recorded in August 2020. Nevertheless, we think the issuance of local government bond in the next four months is likely to support the rebound of social financing growth.<br>▪ On the positive note, corporate bond issuance accelerated to CNY434.1 billion, highest since April 2020. The acceleration of corporate bond was attributable to lower interest rate and tighter credit spread.<br>▪ The gap between M2 and M1 widened further to 4% from 3.4% in July, a sign that corporate is cautious about future outlook. Meanwhile, the faster than expected deceleration of M1 growth was also associated with weaker property sales. |
| ▪ Macau's average housing price dropped for the second consecutive month by 1% mom to MOP102,240/square meter in July. Housing transaction volume declined notably by 20% mom or 22.1% yoy to 560 deals in July, the lowest since March 2021. Approved new residential mortgage loans also decreased for the second consecutive month by 50.7% yoy to MOP4.1 billion in July. | ▪ The subdued housing market was mainly attributable to the elevated unemployment rate, low housing rental, concerns about economic growth outlook and stock market rout amid China's virus resurgence. The Delta variant outbreaks in China appear to have weighed down Macau's economy during August. Stock market remained sluggish during the month as well. As such, housing market may have taken another hit in August.<br>▪ On a positive note, both investor sentiment and Macau's economy may have rebounded as China's local epidemic has been brought under control. The travel restriction measures between Macau and Hong Kong have been partially relaxed as well. This adds onto the tight housing supply (housing completion and housing start rose by 8.2% yoy and 321.9% yoy respectively during the first seven months of 2021 but remained low) may support a rally in the housing market. However, as the purchasing power of first-home local buyers (represented 82.4% of total local home buyers in July) may have diminished while the housing control measures may continue to weigh (local home buyers with no less than one flat took up 2.6% of total local home buyers in July), the upside of the housing market may remain capped. We hold onto our view that Macau's average home price will grow by up to 3% yoy by end of this year. |

## RMB

| Facts | OCBC Opinions |
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| ▪ The USDCNH ended the week below 6.45 despite consolidation of broad dollar. | ▪ RMB strength was on the back of three factors including hawkish message from PBoC official, resumption of US-China dialogue and resilient trade data. |

# Treasury Research & Strategy

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