Greater China – Week in Review

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Highlights: no loss of growth momentum

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China reported a better-than-expected 2Q growth data last week. Despite the sharp deceleration of headline growth to 7.9% yoy in 2Q from 18.3% yoy in 1Q, on two-year average, China's growth reaccelerated to 5.5% in 2Q from 5% in 1Q after adjusting for pandemic induced base effect.

China's manufacturing sector continued to recover in the first half of 2021. Share of manufacturing in China's GDP rebounded further to 27.9% in the first half of 2021, up by 1.3% for the same period of 2020. Capacity utilization rate increased further to 78.4% as of the end of 2Q, up from 77.2% in the first quarter.

Fixed asset investment in manufacturing rose further by 2% yoy in the first half on two-year average after manufacturing investment returned to pre-pandemic level for the first time in May. The fact that there is no premature de-industrialization in China is encouraging against the backdrop of more complex international relationship.

Overall, the latest data supported the view that there is no evidence of loss of growth momentum.

On trade, demand for Chinese products remained strong in June. China post double digit export growth to its major trading partners. Export to ASEAN, EU, US and Japan rose by 33.1% yoy, 27.2% yoy, 17.8% yoy and 26% yoy respectively. The resurgence of virus continued to be the catalyst to support China's export growth.

China's imports of electronic integrated circuit hit a record high of US$37.96 billion, a sign that China continued to stockpile chips amid uncertain global environment and concerns about supply disruption.

Looking ahead, the moderation of new export orders of manufacturing PMI in the past two months against the backdrop of economic reopening in the US and EU showed that the support from external demand to Chinese economy is likely to have peaked. With the pandemic induced base effect waning, we expect China's growth to decelerate further to 5.5% handle in the second half of 2021, but still closer to potential growth. For details about China's growth data, please see our report here.

On policy, the partial rollover of medium-term lending facility (MLF) this morning together with the universal RRR cut earlier reinforced expectation that PBoC is committed to keep liquidity stable at a reasonable level.

As mentioned by PBoC in the latest press conference, China's current 11% aggregate social financing growth has more or less matched nominal GDP growth**. This is a strong hint that PBoC is likely to put a brake on the recent sharp deceleration of credit growth.** As such, we think the room for

China's credit growth to slow down further is limited, which is likely to underpin the risk sentiment in the near term.

The launch of carbon exchange showed China's move towards a market-based mechanism to reduce carbon footprint. As mentioned by China's Vice Minister for Environment, a market-based mechanism is a more efficient and flexible tool as compared to previous administrative measures.

Currently only power generating industry was included in the exchange due to relatively good data quality. More industries such as cement and steel making will also be included in future. The future development of China's carbon exchange will probably depend on the data quality of estimation of carbon emission.

In **Hong Kong,** the Biden Administration has been active in responding to Hong Kong issue lately. At this juncture, this may not have much impact on Hong Kong's financial market which is instead getting new impetus. On the one hand, China reportedly plans to exempt companies listing in Hong Kong from cybersecurity review. If this is the case, it may bolster Hong Kong's strong IPO market. On the other hand, Hong Kong takes new steps to promote the development of green and sustainable finance. In particular, Carbon Market Work Stream has been set up to study the feasibility of developing Hong Kong as a regional carbon trading center to boost collaboration in the Greater Bay Area. For Hong Kong to achieve the goal of carbon neutrality by 2050, one key step would be to increase the carbon price, for example by levying carbon tax or establishing an active carbon trading center. Should Hong Kong become a regional carbon trading center, it may also help to increase competition to China's onshore Carbon Exchange and therefore increase the efficiency of both centers. On top of this, the Center for Green and Sustainable Finance is launched to help the financial industry manage the risks. Given the rising awareness of sustainability and the resultant increase in funding needs, it would be a good opportunity for Hong Kong to leverage on its strength as a global financial center to capitalize on the big trend.

On the HKD market front, 1M HIBOR fell below 0.08% again while 3M HIBOR also dropped below 0.16% to the lowest since May 2010, pointing to flush HKD liquidity. Going forward, HIBOR may stay at decade-lows as the Fed appears to have been patient about tightening. That said, we see limited downside for HIBOR especially given the prospect of busy IPO pipeline. 1M HIBOR and 3M HIBOR may find support at 0.05% and 0.1% respectively.

Key Events and Market Talk	
Facts	**OCBC Opinions**
▪ China's national carbon trading stared last Friday at Shanghai Environment and Energy Exchange. ▪ About 2200 power generation companies are included in the first batch of carbon exchange with more than 4 billion tons of annual carbon dioxide emissions.	▪ The launch of carbon exchange showed China's move towards a market-based mechanism to reduce carbon footprint. As mentioned by China's Vice Minister for Environment, a market-based mechanism is a more efficient and flexible tool as compared to previous administrative measures. ▪ Currently only power generating industry was included in the exchange due to relatively good data quality. More industries such as cement and steel making will also be included in future once China's regulators establish a system to more accurately measure carbon emission. The future development of China's carbon exchange will probably depend on the data quality of estimation of carbon emission.
▪ PBoC rolled over CNY100bn liquidity via medium term lending facility.	▪ The partial rollover of medium-term lending facility (MLF) yesterday together with the universal RRR cut earlier reinforced expectation that PBoC is committed to keep liquidity stable at a reasonable level.
▪ USDHKD spot moved closer to 7.77. Meanwhile, 1M HIBOR fell below 0.08% again while 3M HIBOR also dropped below 0.16% to the lowest since May 2010. ▪ China's social media and e-commerce firm Xiaohongshu reportedly decided to put on hold the US IPO after China tightened the grip. China reportedly plans to exempt companies listing in Hong Kong from seeking the approval of the Cyberspace Administration of China. If this is the case, it may bolster Hong Kong's strong IPO market.	▪ Lately, USDHKD forward swap points also grinded lower gradually which points to flush HKD liquidity amid a quiet IPO market, low HKD LDR, lack of seasonal factors except ongoing dividend payment, and the muted equity flows. ▪ Going forward, we expect HIBOR to stay at decade-low for some time. Even if the Fed starts to raise rates, HIBOR's uptrend may lag behind its USD counterpart. Having said that, we see limited downside for HIBOR especially given the prospect of busy IPO pipeline. Should USD LIBOR rebound on the resolution of debt ceiling and the start of taper, it may also help to cap the downside of HIBOR. As such, 1M HIBOR and 3M HIBOR may find support at 0.05% and 0.1% respectively.
▪ Hong Kong's Green and Sustainable Finance Cross-Agency Steering Group announced to take next steps to support Hong Kong to be a leader in green and sustainable finance and help the transition of the financial ecosystem towards carbon neutrality.	▪ The Steering Group will focus on three areas. First, climate-related disclosure & sustainability reporting. This is important as the lack of a common standard has been hindering the development of global green and sustainable finance markets. ▪ Second, carbon market opportunities. Specifically, a Carbon Market Work Stream (CMWS) will be set up and co-chaired by the SFC and HKEX to study the feasibility of developing Hong Kong as a regional carbon trading center to boost collaboration in the Greater Bay Area. The CMWS will explore opportunities from the cap-and-trade carbon market and the Chinese and foreign voluntary carbon market. In fact, China also announced to launch the National Carbon Exchange in July last week, indicating that Hong Kong is moving in tandem with China to promote sustainability. For Hong Kong to achieve the goal of carbon neutrality by 2050, one key step would be to increase the carbon price, for example by levying carbon tax or establishing an active carbon trading center. Should Hong Kong become a regional carbon trading center, it may also help to increase competition to China's onshore Carbon Exchange and therefore increase the efficiency of both centers. ▪ Third, the Center for Green and Sustainable Finance is launched to help the financial industry manage the risks and

	seize the opportunities from climate change. Given the rising awareness of sustainability and the resultant increase in funding needs, it would be a good opportunity for Hong Kong to leverage on its strength as a global financial center to capitalize on the big trend.
▪ The US Treasury issued an advisory warning US companies of the risks of operating in Hong Kong amid China's increasing control over the city, including risks or business following the implementation of the National Security Law, data privacy risks, risks regarding transparency and access to critical business information and risks for businesses with exports to sanctioned entities or individuals. Meanwhile, the US Treasury imposed sanctions on seven officials from China's Hong Kong liaison office.	▪ Though the US has been active in responding to HK issue lately, unless the US takes extreme actions such as undermining Hong Kong dollar's peg system or cutting Chinese banks from the SWIFT or the US clearing system, the impact on Hong Kong's financial stability or the economy may be limited.
▪ The HKMA announced to further 90-day repayment decrement for trade facilities under the Pre-approved Principal Payment Holiday Scheme to the end of October, citing the pandemic uncertainty across the globe and the uncertainties about the economic recovery.	▪ This scheme has been extended by five times since last May. On a positive note, with the external trade and economy improving gradually, the share of corporates requiring loan extension in all eligible corporates decreased to 2.1% following the second extension from 16% when it was first introduced. Should the economy regain solid footing on the expected border reopening, it is possible for the government to gradually unwind Covid-support measures.

Key Economic News	
Facts	**OCBC Opinions**
▪ China's trade data surprised on the upside in June. Export in dollar term rose by 32.2% yoy while import in dollar term rose by 36.7%. ▪ Trade surplus widened to US$51.5 billion from USR45.5 billion in May.	▪ Demand for Chinese products remained strong in June. China post double digit export growth to its major trading partners. Export to ASEAN, EU, US and Japan rose by 33.1% yoy, 27.2% yoy, 17.8% yoy and 26% yoy respectively. The resurgence of virus continued to be the catalyst to support China's export growth. ▪ Nevertheless, the share of US-China total trade fell again to 11.9% in the second quarter of 2021 from 13.7% in 4Q 2020 and 12.7% in 1Q 2021 as the change of leadership in the US failed to rollback the tariff. ▪ The stronger than expected import growth was mainly attributable to two factors including surging commodity prices and strong demand for integrated circuit. Imports of crude oil and iron ore by value rose by 62.8% yoy and 83.3% yoy respectively in June. However, China's imports of crude oil and iron ore by volume fell by 24.5% yoy and 12% respectively. The decline of crude oil import by volume was the highest since 2001. China's import of crude oil by volume in the first half of 2021 fell by 3%, first decline since the first half of 2013, due to higher import prices. The average crude oil import prices rose by 20.5% in the first quarter. In contrast, despite 67% surge of average import prices for iron ore, China's imports of iron ore still rose by 2.6% yoy. ▪ China's imports of electronic integrated circuit hit a record high of US$37.96 billion, a sign that China continued to stockpile chips amid uncertain global environment and

	concerns about supply disruption.
▪ China's economic growth decelerated to 7.9% yoy in the second quarter from 18.3% yoy in the first quarter in line with expectation as low base effect fades away. Sequentially, China's growth reaccelerated to 1.3% qoq sa in 2Q from downward revised 0.4% qoq sa in 1Q.	▪ China's GDP growth decelerated in the 2Q as expected. However, on two-year average, China's growth reaccelerated to 5.5% in 2Q from 5% in 1Q. ▪ No signs of loss of growth momentum as most indicators recovered further on two-year average growth. ▪ No premature de-industrialization. Share of manufacturing in China's GDP rebounded further to 27.9% in the first half of 2021. ▪ Improving domestic demand but more need to be done. The relative slow wage growth and elevated youth unemployment are still key hurdles for China's consumption recovery. ▪ With the pandemic induced base effect waning, we expect China's growth to decelerate further to 5.5% handle in the second half of 2021. ▪ As credit growth has basically matched nominal GDP growth, China will put a brake on further deceleration of credit growth, which will underpin risk sentiment in the near term.
▪ Macau's gaming revenue rose by 684.7% yoy to MOP25.38bn in 2Q amid low base effect and the strong rebound of mass market revenue (+16.3% qoq or +1095.5% yoy) on holiday effect.	▪ In contrast, VIP revenue dropped 6.8% qoq to MOP8.5bn, partially due to China's crackdown on cross-border gambling. As a result, the share of VIP revenue in gross gaming revenue fell to 33.5%, the lowest since record. Given the tempered demand from high rollers, it may be harder for the gaming sector to return to pre-pandemic levels. On a positive note, should border reopen for Hong Kong visitors and China's local epidemic remain well-contained, it may provide additional impetus for the mass market segment which has become the main growth driver of the gaming sector. As such, gross gaming revenue may rebound gradually in 2H 2021.

RMB	
Facts	**OCBC Opinions**
▪ The USDCNY continued to be traded in a narrow range of 6.45-6.50 last week.	▪ RMB remained resilient against its major trading partner despite the rising two-way movement in the FX market. RMB index extended its gain to stand above 98 firmly. We think the near-term outlook of RMB will still depend on dollar movement.

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