Fundamentals, Liquidity Conditions & Yuan

- China’s credit growth accelerates further in June, reinforcing our view that the nation will keep leading the global economic recovery in the months ahead
- China’s booming stock market is expected to continue on surging margin trading and equity inflows; Meanwhile, we see rising risks of technical corrections
- We maintain our short USD/CNH position at this stage, while staying cautious on US-China relations that could dent sentiment abruptly when approaching the November presidential election

Asia Overview - Most EM Asian currencies weakened versus the dollar during Friday’s Asian session. The SGD inched up, while the JPY advanced around 0.3% despite a 3 bp rise in the 10Y UST yield.

The CNY and CNH declined 0.1% and 0.2% respectively. However, USD/CNH will likely trade lower and breach the 7.00 support level. China’s CBIRC spokesman said in a statement on Saturday that the current non-performing loans have not been fully exposed, with considerable upward pressure. The PBoC said on Friday that enforcement of the wealth management product regulation should be extended due to the coronavirus outbreak. The KRW tumbled 0.7%. USD/KRW will likely retreat towards 1,180 after fluctuating around the 1,200 mark. The younger sister of North Korean leader Kim Jong-un on Friday dismissed the chances of a meeting with the US this year, but conveyed her brother’s “best wishes” to US President Donald Trump in his endeavors. South Korea delays the “new deal” plan announcement by one day to 14 July. South Korea will almost double the ownership tax rate for individuals and corporations which own multiple homes to 6%. The TWD edged down. USD/TWD will likely reach 29.2 gradually in the weeks ahead. Taiwan Semiconductor Manufacturing Co. (TSMC) posted monthly revenue that suggested June-quarter sales surpassed market estimates.

The INR dropped 0.3%. USD/INR will likely trade in a range of 74.5-76.0 in the near term. RBI governor Shaktikanta Das addressed the seventh SBI Banking and Economics Conclave on Saturday, calling for a resolution corporation for stressed lenders. He also said that it is crucial to raise capital and build buffers for state-run and private banks to ensure credit flow and resilience. The RBI bought and sold INR 100bn each of government bonds in the secondary market in the week ended 3 July. The Indian government sold INR 340bn of bonds versus the plan to sell INR 300bn of securities on Friday. India’s foreign reserves increased to a fresh all-time high of USD 513.25bn in the week ended 3 July from USD 506.84bn a week ago. The IDR weakened 0.3%. USD/IDR is likely to consolidate around 14,500 at this stage before rallying further. The BI said on Friday that it will extend the current shortened trading hours for monetary operations in bonds and forex to 31 July. The BI will sell IDR 20tn of T-bills and government bonds on 14 July. The BI’s financing of this year’s budget deficit may help the government overcome shock from coronavirus pandemic, according to Fitch Ratings. The MYR slid 0.1%. USD/MYR is likely to stay below the downtrend line since reaching this year’s high in late March. The PHP declined 0.1%. However, USD/PHP will likely head for 49.0 after technical corrections. Philippine trade deficit swelled to USD 1.87bn in May from USD 449mn the previous month, with exports and imports tumbling 35.6% yoy and 40.6% yoy respectively. The THB fell 0.3%. USD/THB will likely trade between 31.0 and 31.5 at the moment.

Most regional equity indices resided in the red on Friday. China’s SHCOMP index dropped 1.95% amid USD 627.4mn of equity outflows, while India’s NIFTY50 index slid 0.42%. South Korea’s KOSPI index slipped 0.81% with foreign investors offloading a net USD 327.3mn of Korean shares. In the meantime, Taiwan’s TWSE index fell 0.98% although global funds added to their holdings in local main board shares by USD 8.6mn on Friday. Thailand’s SET index and Indonesia’s JCI index declined 1.12% and 0.43% respectively. Malaysia’s KLCI index ended 0.54% higher.
China • China’s credit growth accelerated further in June, with aggregate financing increasing to CNY 3.43tn from an upwardly revised CNY 3.19tn in May. More importantly, loans in the household sector and the corporate sector increased by CNY 3.56tn and CNY 8.77tn respectively in the first half. With medium and long-term loans accounting for 78.7% and 55.4% respectively, it has been supportive of China’s major industrial enterprises resuming operation and production after the coronavirus lockdowns.

China’s CPI inflation rose a bit to 2.5% yoy in June from 2.4% yoy the previous month, but will likely ease again in late Q3 and Q4 on the base effect. Meanwhile, the nation’s PPI deflation eased to 3.0% yoy from 3.7% in May, as "international commodity prices picked up, domestic manufacturing steadily recovered, and market demand continued to improve" according to the NBS.

It has reinforced our view that China will keep leading the global economic recovery in the months ahead on proactive fiscal policy and flexible monetary policy, as indicated by booming copper prices. The PBoC said China’s economic recovery will continue in the second half and beyond on new infrastructure investment, according to a press conference transcript released late Friday.

China’s outstanding balance of margin trading jumped to CNY 1.30tn as of Friday but is still well below its peak of CNY 2.27tn recorded on 18 June 2015, which indicates a prospective upside potential for China A-shares. While China’s booming stock market is expected to continue on surging margin trading and equity inflows, we see rising risks of technical corrections in the coming one to two weeks as indicated by the RSI index. It will likely lead to a pullback in Chinese government bond yields that have climbed substantially in response to the central bank’s crackdown on interest rate arbitrage, concerns over heavy sovereign debt supply and booming A-shares.

Going forward, we also stay cautious on US-China relations that could dent sentiment abruptly, particularly when approaching the November presidential election.

- US President Donald Trump said on Friday that a phase-two trade pact with China is not on his mind and “the relationship with China has been severely damaged.”
- White House economic adviser Larry Kudlow told Fox Business Network on Friday that he believes it’s “unwise” for US investors to put their money in China.
- The Trump administration plans to make an announcement this week related to escalating tensions in the South China Sea.

We maintain our short USD/CNH position at this stage. It will add to risk appetite if EU leaders reach an agreement on the European Commission’s proposal of a EUR 750bn recovery fund consisting of EUR 500bn in grants and EUR 250bn in loans at a summit set for 17-18 July.
**TODAY'S CALENDAR**

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<th>Time (HKT)</th>
<th>Economy</th>
<th>Type</th>
<th>Release</th>
<th>Period</th>
<th>Consensus</th>
<th>Actual</th>
<th>Last</th>
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<td>NFL</td>
<td>Food Prices MoM</td>
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<td>NFL</td>
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<td>5.84%</td>
<td>(Mar)</td>
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