

China's Economy, Monetary Policy and Yuan

- China will continue leading the global economic recovery in the months ahead, with its factory activity expanding for the seventh consecutive month in September
- The PBoC pledges to make its monetary policy more flexible and targeted, which suggests the Chinese central bank doesn't intend to roll out more aggressive monetary easing measures for the rest of the year
- The yuan is expected to retain its yield and growth advantage in our view
- We maintain our short USD/CNH position, with the offshore yuan expected to follow a broader market tone during the eight-day golden week holiday

Asia Overview - Most EM Asian currencies advanced versus the dollar during Wednesday's Asian session. The SGD increased about 0.3%, while the JPY rallied 0.2% despite a 3.5 bp rise in the 10Y UST yield.

The CNY and CNH gained 0.4% and 0.5% respectively. USD/CNH is likely to slide further towards 6.75 in the near term. China sets TLAC rules for Global Systemically Important Banks (G-SIBs). USD/KRW will likely fluctuate in a range of 1,160-1,180 for now. The TWD gained 0.1% amid equity inflows. USD/TWD is likely to trade near 29.0 at this stage. The CBC sold TWD 170bn of 364-day NCDs at a record low average rate of 0.253% on Wednesday.

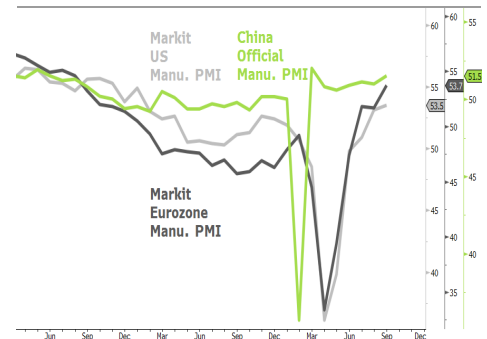
The INR rallied 0.1%. USD/INR is likely to trade in a range of 73-74 at the moment. Finance Minister Nirmala Sitharaman said in a newspaper interview published on Wednesday that India will name new MPC members in "a few days." India's current account balance recorded an all-time high surplus of USD 19.8bn in the April-June quarter, compared to a surplus of USD 0.6bn in the preceding quarter. India's external debt stood at USD 554.5bn at end-June, increasing to 21.8% of GDP from 20.6% as of 31 March. The finance ministry said on Wednesday that the government will borrow INR 4.34tn in the second half of the current fiscal year, while sticking to the annual borrowing target of INR 12tn that was revised in May from INR 7.8tn approved in the Budget 2020-21. India and China "positively" evaluate the outcome of the sixth round of talks of their army commanders. The IDR advanced 0.1%. USD/IDR is likely to trade between 14,500 and 15,000, with odds of breaching the upper bound. PBoC Governor Yi Gang and BI Governor Perry Warjiyo agree to boost use of local currencies in trade and direct investment settlement, according to the MoU signed on Wednesday. The MYR inched up. USD/MYR will likely hover around 4.15 at this stage, susceptible to domestic political turmoil. The PHP edged up. USD/PHP will likely consolidate around 48.5 at the moment. The government's outstanding debt rose 4.9% mom to PHP 9.62tn in August from PHP 9.16tn a month earlier. BSP Governor Benjamin Diokno said on Wednesday that the central bank has injected a total of PHP 1.5tn, or 7.6% of GDP, into financial system since the pandemic. Diokno also said that he expects the peso to trade between 48.50-48.70 to a dollar for now. The THB dropped about 0.2%. USD/THB will likely trade higher towards 31.8. Thailand's current account surplus widened to USD 2.996bn in August from USD 1.787bn the previous month. The nation's fiscal deficit reached THB 614.4bn, or 3.9% of GDP, in the first nine months of FY2019-2020. Thailand's economic panel will meet on 7 October to consider additional stimulus measures, including tax incentives.

Regional equity indices diverged on Wednesday. China's SHCOMP index slid 0.20% amid USD 187.7mn of equity outflows, while India's NIFTY50 index rallied 0.22%. South Korea's onshore markets are closed Wednesday to Friday for a public holiday. In the meantime, Taiwan's TWSE index advanced 0.38% as global funds added to their holdings in local main board shares by USD 168.9mn on Wednesday. Malaysia's KLCI index ended 0.06% higher. However, Thailand's SET index and Indonesia's JCI index closed down 1.61% and 0.19% respectively.

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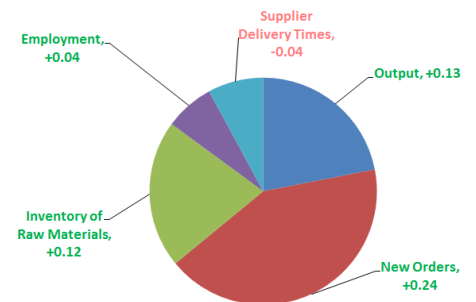
Qi Gao
FX Strategist (Asia)
 +65 6305 8396
qi.gao@scotiabank.com

Manufacturing PMI: US, Eurozone and China



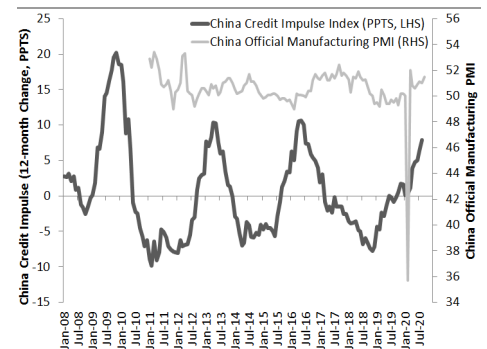
Source: Bloomberg & Scotiabank FICC Strategy

Contribution to A 0.5 Points Rise in China's September Official Manufacturing PMI



Source: Bloomberg & Scotiabank FICC Strategy

China Credit Impulse Index (12-month Change) vs. China Official Manufacturing PMI



Source: Bloomberg & Scotiabank FICC Strategy

China • China will continue leading the global economic recovery in the months ahead, with its factory activity expanding for the seventh consecutive month in September.

The nation's official manufacturing PMI rallied to 51.5 in September from 51.0 in the previous month. The *output* sub-index rebounded to 54.0 from 53.5 in August, while the *new orders* sub-index climbed further to 52.8 from 52.0 a month ago. More importantly, the reopening of the global economy and improving external demand lifted the *new export orders* sub-index further to 50.8, above the boom-bust line of 50 for the first time this year, from 49.1 in August.

China's credit impulse index increased further in August, which will help spur economic growth. In addition, China's fiscal spending drops 2.1% yoy to CNY 14.99tn in the first eight months, improving from a 3.2% fall in the January-July period.

In the meantime, China's central bank pledged to make its monetary policy more flexible and targeted at its third-quarter monetary policy meeting held on 25 September, deleting the text that "to strengthen macro policy adjustment" from the postmeeting statement released on Monday. The PBoC also vowed to deepen market-oriented interest rate reform and guide loan rates lower going forward.

It suggests the Chinese central bank doesn't intend to roll out more aggressive monetary easing measures for the rest of the year. PBoC adviser Ma Jun told Tencent Finance on the sidelines of the 2020 Global Wealth Management Forum held in Beijing on 5-6 September that China may basically complete the task of economic recovery in the first quarter of next year, with macroeconomic policies returning to normal at that time.

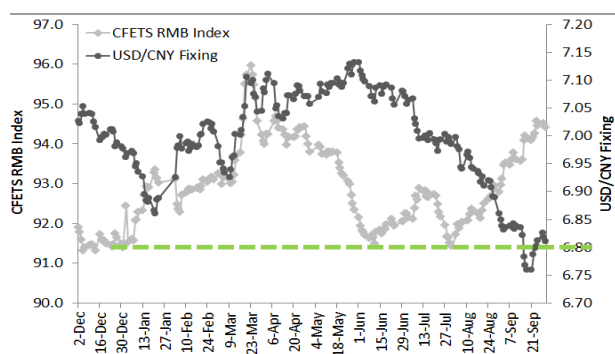
In addition, the PBoC has reiterated China will keep opening up the financial sector to attract more foreign investment, supportive of the yuan exchange rate in the medium term in our view.

- FTSE Russell announced on 24 September that it will add Chinese government bonds to its flagship World Government Bond Index (WGBI). The inclusion will lift foreign holdings of the Chinese sovereign debt and attract additional bond portfolio inflows worth about USD 150bn according to our estimate.
- Earlier on 21 September, the PBoC and the SAFE (China's FX regulator) issued draft guidelines aimed at simplifying rules and uniformizing regulations to help expedite inbound bond investment. As of June 2020, foreign entities held CNY 2.46tn and 2.57tn of China's domestic RMB equities and bonds respectively according to the PBoC data.

In our opinion, the yuan will retain its yield and growth advance into Q1 2021 with China's stronger fundamentals and less dovish monetary policy stance, which will likely prompt foreign investors to raise their holdings in RMB-denominated assets.

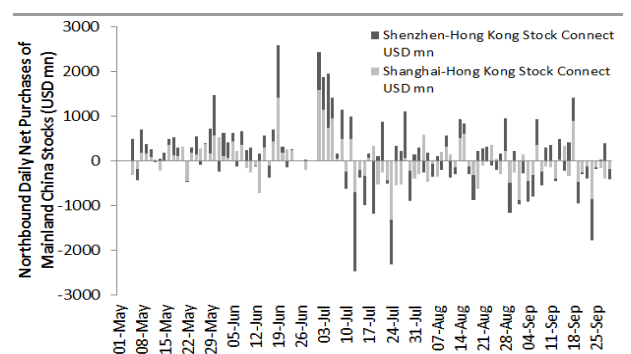
We maintain our [short USD/CNH](#) position, with the offshore yuan expected to follow a broader market tone during the eight-day golden week holiday on 1-8 October.

Scotiabank CFETS RMB Index vs. USD/CNY Fixing



Source: Bloomberg & Scotiabank FICC Strategy

Northbound Daily Net Purchases of Mainland China Stocks



Source: Bloomberg & Scotiabank FICC Strategy

TODAY'S CALENDAR

Time (HKT)	Economy	Type	Release	Period	Consensus	Actual	Last	Significance
08:00	KR	TRADE	Exports YoY	Sep	3.5%		-10.1%	med-high
08:00	KR	TRADE	Imports YoY	Sep	-5.1%		-15.8%	med-high
08:00	KR	TRADE	Trade Balance	Sep	\$8,900mn		\$3,838mn	med-high
08:30	SG	DATA	URA Private Home Prices QoQ	Q3 P			0.3%	med
12:00	ID	INFL	CPI YoY	Sep	1.40%		1.32%	high
12:00	ID	INFL	CPI NSA MoM	Sep	-0.03%		-0.05%	med-high
12:00	ID	INFL	CPI Core YoY	Sep	2.00%		2.03%	med-high
15:30	TH	DATA	Business Sentiment Index	Sep			45.7	med
16:00	PH	BSP	BSP Overnight Borrowing Rate	Oct 1	2.250%		2.250%	high
16:00	PH	BSP	BSP Standing Overnight Deposit Facility Rate	Oct 1	1.750%		1.750%	high

CONTACTS - GLOBAL FX STRATEGY

Shaun Osborne
 Chief FX Strategist
 T +1 416 945 4538
shaun.osborne@scotiabank.com

Qi Gao, FRM
 FX Strategist (Asia)
 T +65 6305 8396
qi.gao@scotiabank.com

Juan Manuel Herrera
 FX Strategist (G10)
 T +1 416 866 6781
juanmanuel.herrera@scotiabank.com

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