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Economic Acumen

Commentary by CEBI Research Team

In Brief

- Renminbi has strengthened on continuing basis since April 2021, with appreciation of more than 2% YTD against the U.S. dollar in 2021. Rising signs of herding behavior in China's foreign exchange market have attracted the public attention, warning against the rapid appreciation due to sizable speculative trading as renminbi hit a three-year high against the dollar and a five-year high against a trade-weighted basket of currencies, raising concerns that continued hot money inflows will lead to formation of asset bubbles.
- In response to unhealthy rally of renminbi, the PBOC raised the reserve requirement for banks' foreign exchange deposits to 7% from 5% in an attempt to reduce market's dollar liquidity and in turn stabilize renminbi against the dollar.
- We are of the view that the move will have temporary effect to curb the upside of renmimbi but will not alter medium and long-term appreciation trend. Renminbi will stay well-supported between 6.25 and 6.35 per USD for the rest of 2021.

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Navigating turbulent rally of renminbi

Renminbi has strengthened on continuing basis since April 2021 alongside China's robust economic recovery, with appreciation of more than 2% YTD against the U.S. dollar in 2021. Rising signs of herding behavior in China's foreign exchange market have attracted the attention of former and current Chinese Government officials as well as state-media, warning against the rapid appreciation of renminbi due to sizable speculative trading as renminbi hit a three-year high against the dollar and a five-year high against a trade-weighted basket of currencies, raising concerns that continued hot money inflows will lead to formation of asset bubbles. In response to unhealthy rally of renminbi, the People Bank of China (PBOC) raised the reserve requirement for banks' foreign exchange deposits to 7% from 5% in an attempt to reduce market's dollar liquidity and in turn stabilize renminbi against the dollar. In sum, the latest PBOC's move is to restore the stable path of renminbi appreciation, thus strengthening foreign exchange liquidity management for financial institutions. We are of the view that the move will have temporary effect to curb the upside of renmimbi but will not alter medium and long-term appreciation trend. Looking ahead, sturdy economic fundamentals for renminbi remain intact in 2021. China's economic recovery out of the coronavirus pandemic has been relatively swift. Strong current account surplus, abundant foreign exchange reserves, sound fiscal conditions, and stable financial systems brace for continued strength of renminbi, which will stay well-supported between 6.25 and 6.35 per USD for the rest of 2021.

Resilience of economic fundamentals along with the dollar's weakness supporting upbeat momentum of renminbi. The fundamental reason behind renminbi rally involve supportive growth momentum of China's economy and the dollar's weakness. China's economic fundamentals remain sound as China's newly released manufacturing and services for May posted 51.0 and 55.2 respectively, staying above 50 since March 2020, which indicated that economic activities continue to expand and China's economy maintains recovering momentum with good prospects. The prompt implementation of an array of measures, including higher fiscal

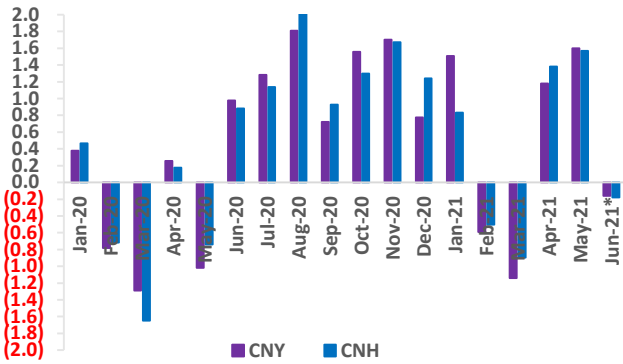
spending and tax relief as well as prudent monetary accommodation help support economic growth and employment, thus brightening outlook of renminbi. In addition, U.S. recovery momentum may lose traction on fears of tightening easy monetary stance due to rising inflation, swelling fiscal deficit due to sizable government expenditures and overshooting commodities prices due to supply-demand rebalancing with which the US dollar index has experienced volatile month-to-month decline by 2.1% and 1.6% in April and May, staying below 90 at 89.9. The recent weakness of the dollar is the major key factor to cause significant market turbulence, thus fueling economic risks of global economy and becoming major speculative driving forces for a strong renminbi.

Slowing trend of exports softening growing strength of renminbi.

China's export maintained strong growth during the first four months of 2021 as exports extended an upward trend on the back of consumption rebound of major trading partners, demonstrating an upbeat momentum at 33.8% YoY in Yuan terms and supporting rebound of renminbi. Looking forward, the ongoing pandemic driven by the new variants of coronavirus, limits the pace of activities' normalization, thus depressing travel, spending, corporate investment, foreign demand for Chinese products and consumer confidence. Supply-side constraints including the global chip shortage, shipping disruption, container shortages, and skyrocketing freight rates impose barriers on the sustainable recovery of trading activities. The latest release of China's May official New Export Orders, the sub-index of manufacturing PMI, dropped below 50 at 48.8, signaling that falling overseas new shipments will undermine growth of exports. We are of the view that China's overall trade growth could show slower momentum in coming months due to the resurgent infections abroad and supply constraints in global trade, thus lowering trade surplus and cooling the recent rally of renminbi.

Renminbi integrating with global financial markets. Gearing up market-led pricing mechanism with greater transparency by the PBOC allows the value of renminbi to be reflected more by economic strengths and less by speculative trades. Strengthening economic indicators adds credence to the notion that China's economy is in a cyclical upswing which prompts policymakers to shift their focus to maintain stable growth momentum. Looking ahead, China will take a proactive approach to enhance renminbi's presence in global market and become more financially integrated with the global economy. A freer renminbi market will allow China to promote further opening of forex market and improve the fundamental value of the renminbi through more organic market growth and cross-border channels for trade and investment. It helps guide investors to focus on China's growth outlook, which aim to curb irrational market volatilities.

Fig. 1: CNY and CNH (MoM%)



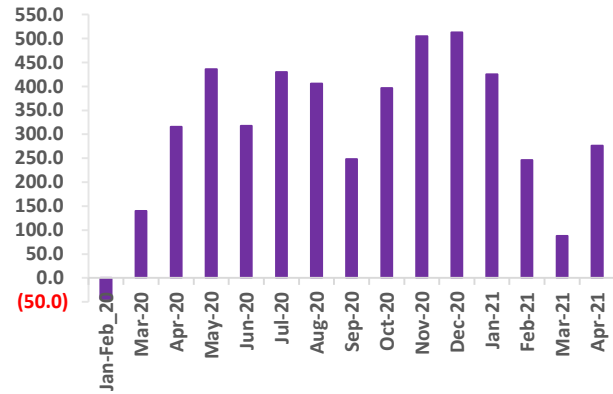
Source: Bloomberg *2nd June

Fig. 2: China Forex Reserves MoM (USD bn)



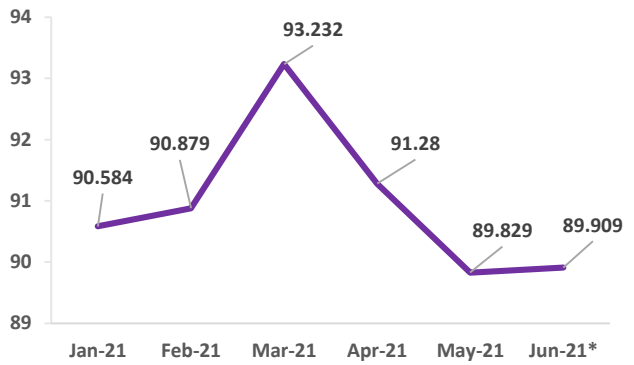
Source: Bloomberg

Fig. 3: China's Trade surplus (RMB bn)



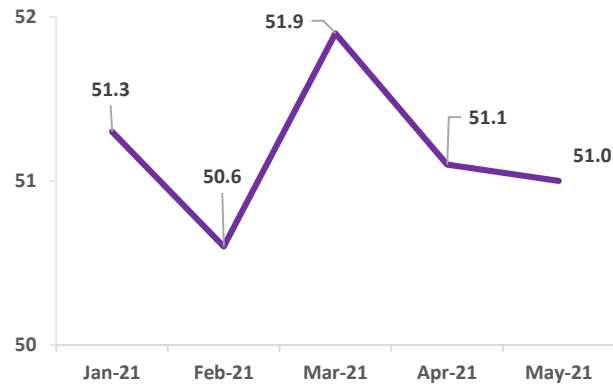
Source: Bloomberg

Fig. 4: U.S. Dollar Index



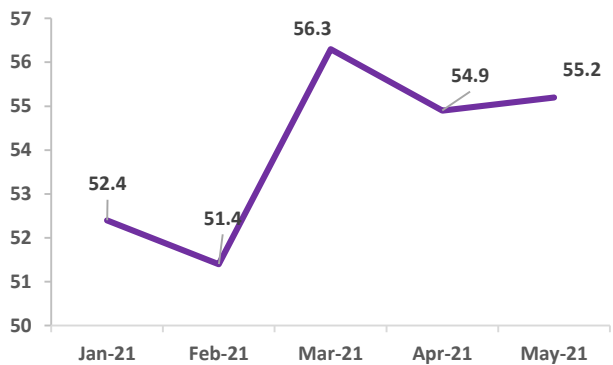
Source: Bloomberg *2nd June

Fig.5. China Manufacturing PMI



Source: Bloomberg

Fig. 6: China Non-Manufacturing PMI



Source: Bloomberg

China economic indicators

	2018	2019	1Q2020	2Q2020	3Q2020	4Q2020	2020	1Q2021
Real GDP (YoY%)	6.6	6.0	(6.8)	3.2	4.9	6.5	2.3	18.3
PMI								
Manufacturing (%)	49.4	50.2	45.9	50.8	51.2	51.8	51.9	51.3
Non-Manufacturing (%)	53.2	53.5	45.3	53.7	55.1	56.1	55.7	53.4
Exports (RMB YoY %)	7.1	5.0	(11.7)	4.2	9.8	10.9	4.0	38.7
Imports (RMB YoY %)	12.9	1.7	(1.0)	(5.6)	4.7	0.04	(0.4)	19.3
Trade Balance (RMB/bn)	2324.7	2912.0	95.9	1068.5	1082.1	1407.7	3654.1	750.9
Exports (USD YoY %)	9.9	0.5	(13.6)	(0.2)	8.4	16.6	3.6	48.9
Imports (USD YoY %)	15.8	(2.7)	(3.1)	(9.5)	3.6	5.4	(0.7)	28.2
Trade Balance (USD/bn)	350.9	421.1	12.7	151.7	153.7	209.3	526.9	115.1
CPI (YoY %)	2.1	2.9	4.9	2.7	2.3	0.1	2.5	0.0
PPI (YoY %)	3.5	(0.3)	(0.6)	(3.3)	(2.2)	(1.3)	(1.8)	2.1
FAI (YTD/ YOY %)	5.9	5.4	(16.1)	(3.1)	0.8	2.9	2.9	25.6
Real Estate Investment (YTD YoY %)	9.5	9.9	(7.7)	1.9	5.6	7.0	7.0	25.6
Industrial Production (YoY %)	6.2	5.7	(8.4)	4.4	5.8	7.1	2.8	24.5
Retail Sales (YoY%)	9.0	8.0	(19.0)	(3.9)	(0.4)	3.2	(3.9)	33.9
New Lending (RMB/bn)	16166.3	16817.5	7096.6	4990.9	4166.7	3378.7	19632.9	7667.9
M2 (YoY %)	8.1	8.7	10.1	11.1	10.9	10.1	10.1	9.4
Aggregate Financing (RMB bn)	19258.4	25673.5	11111.0	9757.4	8747.4	5176.0	34791.8	10266.2

	Apr 20	May 20	Jun 20	July 20	Aug 20	Sept 20	Oct 20	Nov 20	Dec 20	Jan 21	Feb 21	Mar 21	Apr 21
Real GDP (YoY%)	-	-	3.2	-	-	4.9	-	-	6.5	-	-	18.3	-
PMI													
- Manufacturing %	50.8	50.6	50.9	51.1	51.0	51.5	51.4	52.1	51.9	51.3	50.6	51.9	51.1
- Non-manufacturing%	53.2	53.6	54.4	54.2	55.2	55.9	56.2	56.4	55.7	52.4	51.4	56.3	54.9
Exports (RMB YoY %)	7.7	1.2	4.0	10.0	11.2	8.2	7.2	14.5	10.9	16.5	139.4	20.7	22.2
Imports (RMB YoY %)	(10.4)	(12.7)	5.9	1.4	(0.8)	11.2	0.6	(1.4)	(0.2)	18.9	10.6	27.8	32.2
Trade Balance (RMB/bn)	315.5	435.7	317.4	429.1	405.0	248.0	395.7	502.8	509.2	420.7	243.7	86.4	276.5
Export (USD YoY %)	3.1	(3.5)	0.2	6.8	9.1	9.4	10.9	20.6	18.1	24.7	154.8	30.6	32.3
Import (USD YoY %)	(14.4)	(16.7)	2.3	(1.6)	(2.3)	12.7	4.4	3.9	6.5	27.3	17.6	38.2	43.1
Trade Balance (USD/bn)	45.0	61.9	44.8	60.5	57.3	35.6	57.5	74.8	77.0	64.2	37.3	13.5	42.9
CPI (YoY %)	3.3	2.4	2.5	2.7	2.4	1.7	0.5	(0.5)	0.2	(0.3)	(0.2)	0.4	0.9
PPI (YoY %)	(3.1)	(3.7)	(3.0)	(2.4)	(2.0)	(2.1)	(2.1)	(1.5)	(0.4)	0.3	1.7	4.4	6.8
FAI (YTD/ YOY %)	(10.3)	(6.3)	(3.1)	(1.6)	(0.3)	0.8	1.8	2.6	2.9	-	35.0	25.6	19.9
Real Estate Investment (YTD/ YoY %)	(3.3)	(0.3)	1.9	3.4	4.6	5.6	6.3	6.8	7.0	-	38.3	25.6	21.6
Industrial Production (YoY %)	3.9	4.4	4.8	4.8	5.6	6.9	6.9	7.0	7.3	-	35.1	14.1	9.8
Retail Sales (YoY%)	(7.5)	(2.8)	(1.8)	(1.1)	0.5	3.3	4.3	5.0	4.6	-	33.8	34.2	17.7
New Lending (RMB/bn)	1697.8	1482.1	1811.0	992.7	1278.3	1895.7	689.8	1433.7	1255.2	3578.3	1359.4	2730.3	1470.0
M2 (YoY %)	11.1	11.1	11.1	10.7	10.4	10.9	10.5	10.7	10.1	9.4	10.1	9.4	8.1
Aggregate Financing (RMB bn)	3102.7	3186.6	3468.1	1692.8	3585.3	3469.3	1392.9	2135.5	1647.6	5175.8	1723.9	3366.5	1850.7
Urban Unemployment Rate (%)	6.0	5.9	5.7	5.7	5.6	5.4	5.3	5.2	5.2	5.4	5.5	5.3	5.1
Urban Unemployment Rate in 31 major cities (%)	5.8	5.9	5.8	5.8	5.7	5.5	5.3	5.2	5.1	-	5.5	5.3	5.2

World Economic/Financial Indicators

Global Indices			
Index	Closing Price	P/E	One Week chg(%)
U.S.			
DJIA	34,600.38	26.18	0.84
S&P 500	4,208.12	29.85	0.48
NASDAQ	13,756.33	90.03	0.73
EUR			
FTSE 100	7,108.00	51.44	1.11
DAX	15,602.71	33.44	0.98
CAC40S	6,521.52	46.68	2.03
STOXX EUR 600	451.34	38.31	1.37
Asia			
HSI	29,297.62	13.71	0.45
HSCEI	10,951.84	14.39	0.89
CSI300	5,289.97	17.84	(0.58)
SSE Composite	3,597.14	16.22	0.11
SZSE Composite	2,400.90	36.36	0.85
NIKKEI 225	28,946.14	20.32	1.06
KOSPI	3,224.23	20.59	1.76
TWSE	17,165.04	18.06	3.13
S&P/ASX 200	7,217.82	52.24	1.77
MSCI Index			
MSCI WORLD	2,985.97	29.83	0.55
MSCI DEVELOPED	714.42	27.25	0.83
MSCI EMERGING	1,388.47	17.38	2.70
MSCI US	4,077.56	29.85	0.50
MSCI UK	1,997.15	49.02	1.11
MSCI France	187.03	53.88	1.77
MSCI Germany	169.94	33.71	0.99
MSCI China	111.27	14.16	2.09
MSCI Hong Kong	17,228.09	46.22	(1.19)
MSCI Japan	1,191.56	20.14	1.28

* As of 2021/06/02 closing for all markets.

Global Commodities			
	Unit	Price	One Week chg(%)
Energy			
NYMEX WTI	USD/bbl	68.83	4.18
ICE Brent Oil	USD/bbl	71.35	3.60
NYMEX Natural	USD/MMBtu	3.08	5.56
Basic Metals			
LME Aluminum	USD/MT	2,423.40	3.65
CMX Copper	USD/lb.	459.15	1.89
LME Steel Rebar	USD/MT	755.00	(2.52)
LME Lead Cash	USD/MT	2,234.74	3.69
Precious Metals			
CMX Gold	USD/T. oz	1,895.93	(0.64)
Gold Futures	USD/T. oz	1,909.90	0.49
CMX Silver	USD/T. oz	27.79	(1.19)
NYMEX Platinum	USD/T. oz	1,184.42	(1.69)
Agricultural			
CBOT Corn	USD/bu	675.00	8.83
CBOT Wheat	USD/bu	687.50	4.72
NYB-ICE Sugar	USD/lb.	17.68	3.76
CBOT Soybeans	USD/bu.	1,413.75	4.94

Money market		
	Yield (%)	One Week chg(%)
US Fed Fund Rate	0.25	0.00
US Prime Rate	3.25	0.00
US Discount Window	0.25	0.00
ECB Rate (Refinancing)	0.00	0.00
BOJ Policy Rate	(0.10)	0.00
US Treasury (1 Mth)	(0.00)	0.01
US Treasury (1 Yr)	0.04	0.00
US Treasury (5 Yr)	0.79	0.01
US Treasury (10 Yr)	1.59	0.01
US Treasury (30 Yr)	2.27	0.02
1-Month LIBOR	0.0888	(0.001)
3 Month LIBOR	0.1285	(0.01)
Japan 1-Yr Gov. Bond	(0.11)	0.007
Japan 10-Yr Gov. Bond	0.08	0.01
German 1-Yr Gov. Bond	(0.63)	(0.01)
German 10-Yr Gov. Bond	(0.20)	0.01
China LPR (1-year)	3.85	0.00
China 1-Yr Gov. Bond	2.35	(0.04)
China 5-Yr Gov. Bond	2.93	0.04
China 10-Yr Gov. Bond	3.10	0.031
O/N SHIBOR	2.04	0.05
1-mth SHIBOR	2.40	(0.01)
HK Base rate	0.05	0.00
O/N HIBOR	0.04	(0.0024)
1-mth HIBOR	0.09	0.001
O/N CNH HIBOR	1.07	(1.3)
1-mth CNH HIBOR	2.44	(0.14)
Corporate Bonds (Moody's)		
Aaa	2.93	0.04
Baa	3.59	0.02

Currency market		
	Spot Rate	One Week chg(%)
US Dollar Index	89.91	(0.15)
Euro/USD	1.2174	(0.52)
GBP/USD	1.4125	(0.33)
AUD/USD	0.7722	(0.76)
USD/CAD	1.2081	0.06
USD/JPY	109.85	0.91
USD/CHF	0.9020	0.83
USD/CNY Midpoint	6.3773	(0.51)
USD/CNY	6.3811	(0.15)
USD/CNY NDF-12-mth	6.5434	0.02
USD/CNH	6.3881	0.15
USD/HKD	7.7595	(0.03)
CNY/HKD	1.2161	0.12
CNH/HKD	1.2147	(0.17)
USD/KRW	1,113.20	(0.33)
USD/TWD	27.71	(0.35)
USD/SGD	1.32	0.10
USD/INR	73.08	0.42

All data sources: Bloomberg

Disclosures

Analyst Certification

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