



Economic Insight

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China's economic growth will moderate in 2H17/2018

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- China's economy has started the second quarter on a moderate pace due to the ongoing deleveraging, rising financing costs, and tightening financial regulatory measures.
- Industrial production, fixed asset investment, retail sales, and trade data in April were below market expectations, easing from the strong level in March.
- Despite the strong 1Q17 GDP figures, we believe China's economic growth will moderate slightly in the coming quarters. With the ongoing economic deleveraging, easing PPI inflation, and property tightening measures, we maintain our China's economic growth forecast of 6.7% for 2017E and 6.4% for 2018E.
- The PBOC is expected to keep benchmark interest rates steady in 2017 and 2018 while RRR would be slashed by 50 basis points twice every year given the mild inflationary pressure and reduction in foreign exchange.

Growth impetus is not as strong

Based on the latest data, China's economy has started the second quarter on a moderate pace due to the ongoing deleveraging, rising financing costs and tightening financial regulatory measures. Industrial production, fixed asset investment (FAI), retail sales and trade data in April were below market expectations, easing from the strong level in March.

Industrial production rose 6.5%¹ in April after growing 6.8% in 1Q and 7.6% in March. Electricity output expanded 5.4% in April, compared with the growth of 6.7% in 1Q and 7.2% in March. Meanwhile, the PMI for manufacturing, which covers 31 industries, eased to 51.2 in April from 51.8 in March.

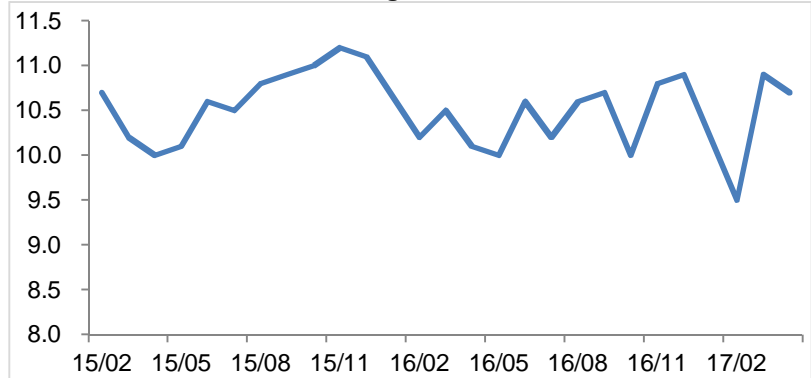
In terms of internal demand, both consumer spending and FAI growth slowed. Retail sales growth decelerated slightly to 10.7% in April from 10.9% in March as car sales slowed on partial withdrawal of tax incentives (Exhibit 1). FAI growth in urban areas also decelerated to 8.3% in April from 9.4% in March and 9.2% in 1Q, attributable to easing manufacturing FAI growth on tightening monetary condition (Exhibit 2).

On the external front, both exports and imports slowed in April (Exhibit 3). China's export growth in April was 8.0% in USD terms, weaker than 16.4% in March and the consensus forecast of 11.3%, although it was close to the export growth of 8.2% in 1Q. Imports decelerated significantly in April, rising only by 11.9%, compared with 20.3% in March and 24.0% in 1Q. With the significant decrease in import growth, trade balance widened to US\$ 38.0 billion in April from US\$ 23.9 billion in March.

¹ All growth rates are year-on-year except specified otherwise

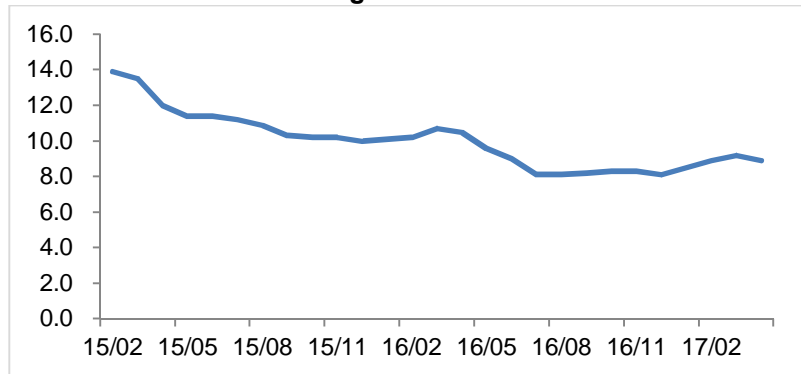


Exhibit 1: China's retail sales growth



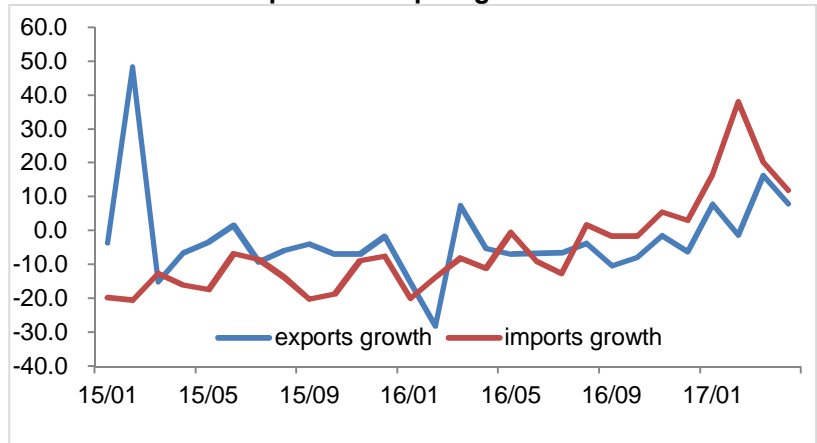
Source(s): NBS, ABCI Securities

Exhibit 2: China's FAI YTD growth



Source(s): NBS, ABCI Securities

Exhibit 3: China's export and import growth



Source(s): NBS, ABCI Securities

Inflation remained moderate in April. CPI rose moderately to 1.2% in April from 0.9% in March as decline in food prices moderated. Meanwhile, PPI decelerated to 6.4% in April from 7.6% in March on the falling commodity prices, particularly prices in oil and ferrous metal-related products.

On the monetary front, the PBOC maintained a monetary tightening bias in April on the ongoing deleveraging. The CBRC also strengthened financial regulation, particularly in the area of shadow banking system. Growth in broad money supply (M2) decelerated to



10.5% in April from 10.6% in March while the total social financing, a comprehensive measure of all types of financing for the real economy, fell to RMB 1,390billion from RMB 2,120billion during the same period.

Economic growth to moderate slightly in 2H17/2018

Despite strong 1Q GDP figures, we believe China's economic growth will moderate slightly in the coming quarters for the following reasons.

First, the ongoing deleveraging and tightening financial regulatory measures will continue to exert upward pressure on the interbank interest rates, which is likely to drive up the lending interest rates. According to the 1Q17 Monetary Policy Report by PBOC, the weighted average lending rate rose to 5.53% in March 2017, compared with 5.26% in December 2016. Meanwhile, with CBRC issuing a series of regulations, the bond financing condition is likely to remain tight.

Second, PPI inflation is likely to moderate in coming quarters with the low base effect fading away and commodity prices easing, which would reduce investment return and dampen investment sentiments in the manufacturing sector.

Third, property sales are likely to slow amid the intensified property tightening measures, which in turn would weigh on home renovation in retail sales growth. In fact, growth in new home sales, as measured in floor space area and value, were 7.7% and 10.0% in April, as compared with 14.7% and 24.4% in March.

In general, with the ongoing economic deleveraging, easing PPI inflation and property tightening measures, we maintain our China's economic growth forecast of 6.7% for 2017E and 6.4% for 2018E. Meanwhile, we reassert that PBOC would keep the benchmark interest rates steady in 2017 and 2018 while RRR would be slashed by 50 basis points twice every year given the mild inflationary pressure and reduction in foreign exchange.

Exhibit 4: Economic forecasts

Economic indicators	2016	2017E	2018E
Real GDP growth, %	6.7	6.7	6.4
FAI growth, %	8.1	9.0	8.0
Retail Sales growth, %	10.4	10.0	10.0
Export growth in USD terms, %	-7.7	4.0	3.0
Import growth in USD terms, %	-5.5	10.0	5.0
Industrial Production growth, %	6.0	6.5	6.0
CPI, %	2.0	2.0	2.0
M2 growth, %	11.3	10.5	10.0
Aggregate Financing, RMB bn	17,800	19,000	20,000
New Yuan Loans, RMB bn	12,600	13,500	14,500
Spot CNY per US dollar, End-year	6.9450	7.100	7.300

Source(s): NBS, PBOC, ABCI Securities



China Economic Indicators

	2016										2017			
	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr
Real GDP (YoY %)	6.7	---	---	6.7	---	---	6.7	---	---	6.8	---	---	6.9	---
Export Growth (USD, YoY %)	11.5	(1.8)	(4.1)	(4.8)	(4.4)	(2.8)	(10.0)	(7.3)	0.1	(6.1)	7.9	(1.3)	16.4	8.0
Import Growth (USD, YoY %)	(7.6)	(10.9)	(0.4)	(8.4)	(12.5)	1.5	(1.9)	(1.4)	6.7	3.1	16.7	38.1	20.3	11.9
Trade Balance (USD bn)	29.9	45.6	50.0	48.1	52.3	52.1	42.0	49.1	44.6	40.8	51.3	(9.1)	23.9	38.0
Retail Sales Growth (YoY %)	10.5	10.1	10.0	10.6	10.2	10.6	10.7	10.0	10.8	10.9	9.5	9.5	10.9	10.7
Industrial Production (YoY %)	6.8	6.0	6.0	6.2	6.0	6.3	6.1	6.1	6.2	6.0	6.3	6.3	7.6	6.5
PMI - Manufacturing (%)	50.1	50.1	50.0	49.9	50.4	50.4	50.4	51.2	51.7	51.4	51.3	51.6	51.8	51.2
PMI - Non-manufacturing (%)	53.5	53.1	53.7	53.9	53.5	53.7	53.7	51.2	50.9	51.9	54.6	54.2	55.1	54.0
FAI (YTD) (YoY %)	10.7	10.5	9.6	9.0	8.1	8.1	8.2	8.3	8.3	8.1	8.9	8.9	9.2	8.9
CPI (YoY %)	2.3	2.0	1.9	1.8	1.3	1.9	1.9	2.1	2.3	2.1	2.5	0.8	0.9	1.2
PPI (YoY %)	(3.4)	(2.8)	(2.6)	(1.7)	(0.8)	0.1	0.1	1.2	3.3	5.5	6.9	7.8	7.6	6.4
M2 (YoY %)	12.8	11.8	11.8	10.2	11.4	11.5	11.5	11.6	11.4	11.3	11.3	11.1	10.6	10.5
New Lending (RMB bn)	1370	556	986	1380	464	949	1220	651	795	1040	2030	1170	1020	1100
Aggregate Financing (RMB bn)	2404	751	660	1629	488	1470	1720	896	1740	1630	3740	1150	2120	1390

World Economic/Financial Indicators

Equity Indices				Global Commodities				Bond Yields & Key Rates			
	Closing price	Chg. WTD (%)	P/E	Unit	Price	Chg. WTD (%)	Volume (5-Day avg.)		Yield (%)	Chg. WTD (Bps)	
U.S.				Energy				US Fed Fund Rate			
DJIA	20,981.94	0.41	18.49	NYMEX WTI	USD/bbl.	49.09	2.61	681,633	1.00	0.00	
S&P 500	2,402.32	0.48	21.41	ICE Brent Oil	USD/bbl	52.11	2.50	330,558	4.00	0.00	
NASDAQ	6,149.67	0.46	32.96	NYMEX Natural Gas	USD/MMBtu	3.36	(1.81)	177,183	US Discount Window	1.50	0.00
MSCI US	2,288.05	0.49	21.82	China Qinhuangdao Port Thermal Coal ²	USD/Metric Tonne	61.80	N/A	N/A	US Treasury (1 Yr)	0.6847	2.54
Europe				Basic Metals				US Treasury (5Yr)			
FTSE 100	7,476.93	0.56	35.30	LME Aluminum Cash	USD/MT	1,902.25	0.89	8,012	US Treasury (10 Yr)	2.3397	1.40
DAX	12,821.91	0.40	20.27	LME Aluminum 3 -mth. Rolling Fwd.	USD/MT	1,905.50	0.77	27,886	Japan 10-Yr Gov. Bond	0.0460	(0.10)
CAC40	5,397.86	(0.14)	19.99	CMX Copper Active	USD/lb.	5,599.25	0.94	8,252	China 10-Yr Gov. Bond	3.6200	(3.20)
IBEX 35	10,960.90	0.59	19.60	LME Copper 3- mth Rolling Fwd.	USD/MT	5,613.00	0.96	23,377	ECB Rate (Refinancing)	0.00	0.00
FTSE MIB	21,693.94	0.55	N/A	Precious Metals				1-Month LIBOR			
Stoxx 600	395.57	(0.02)	25.99	CMX Gold	USD/T. oz	1,234.40	0.55	215,110	3 Month LIBOR	1.1796	(0.08)
MSCI UK	2,168.31	0.26	35.97	CMX Silver	USD/T. oz	16.71	1.85	71,307	O/N SHIBOR	2.7460	(4.51)
MSCI France	154.50	0.21	19.75	NYMEX Platinum	USD/T. oz	936.10	2.03	13,820	1-mth SHIBOR	4.0477	0.09
MSCI Germany	158.58	0.03	20.60	Agricultural Products				3-mth HIBOR			
MSCI Italy	60.44	0.58	N/A	CBOT Corn	USD/bu	366.50	(1.21)	146,638	Corporate Bonds (Moody's)		
Asia				CBOT Wheat	USD/bu	422.50	(2.37)	64,564	Aaa	3.86	(4.00)
NIKKEI 225	19,919.82	0.18	19.11	NYB-ICE Sugar	USD/lb.	15.85	2.19	46,048	Baa	4.58	(2.00)
S&P/ASX 200	5,850.52	0.23	20.00	CBOT Soybeans	USD/bu.	965.75	0.29	96,791			
HSI	25,335.94	0.71	14.25								
HSCEI	10,433.69	1.47	8.80								
CSI300	3,428.65	1.28	15.13								
SSE Composite	3,112.96	0.96	16.90								
SZSE Composite	1,865.27	2.48	27.29								
MSCI China	70.34	0.67	15.46								
MSCI Hong Kong	14,154.71	0.34	14.51								
MSCI Japan	943.03	(0.05)	16.55								

Note:

1. Data sources: Bloomberg, National Bureau of Statistics of China, ABCIS (updated on date of report)
2. The price is Coal 5500 kcal/kg FOB Spot Price

Currency

	Euro/USD	GBP/USD	AUD/USD	USD/JPY	USD/CHF	USD/CNY	USD/HKD	USD/CNY NDF 12-mth Spot pr.
Spot Rate	1.1033	1.2936	0.7424	113.48	0.9925	6.8925	7.7866	7.0770
Chg. WTD (%)	0.93	0.36	0.50	(0.09)	0.85	0.10	0.09	0.20



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Definition of equity rating

Rating	Definition
Buy	Stock return \geq Market return rate
Hold	Market return - 6% \leq Stock return < Market return rate
Sell	Stock return < Market return - 6%

Stock return is defined as the expected % change of share price plus gross dividend yield over the next 12 months

Market return: 5-year average market return rate

Time horizon of share price target: 12-month

Definition of share price risk

Rating	Definition
Very high	$2.6 \leq$ 180 day volatility/180 day benchmark index volatility
High	$1.5 \leq$ 180 day volatility/180 day benchmark index volatility < 2.6
Medium	$1.0 \leq$ 180 day volatility/180 day benchmark index volatility < 1.5
Low	180 day volatility/180 day benchmark index volatility < 1.0

We measure share price risk by its volatility relative to volatility of benchmark index. Benchmark index: Hang Seng Index.

Volatility is calculated from the standard deviation of day to day logarithmic historic price change. The 180-day price volatility equals the annualized standard deviation of the relative price change for the 180 most recent trading days closing price.

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