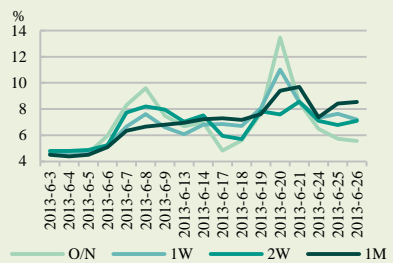


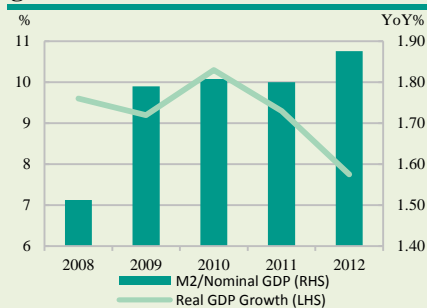
## Economics Weekly

### Ups and downs of SHIBOR in June



Source: shibor.org, ABCIS

### Credit growth outpacing economic growth



Source: Bloomberg, ABCIS

## A new era of China's liquidity management

China's new leadership vowed to deepen the economic reforms to sustain economic growth. Premier Li Keqiang and his team aim at fixing the financial imbalances and sacrificing shorter-term growth for longer-term stability. The recent crunch in the interbank market is the most obvious evidence of the new stance. The credit crunch is a consequence of the PBOC refusing to jump in with extra liquidity, part of a move to tackle rampant credit growth and an increasingly unsustainable shadow banking system. China's SHIBOR turbulence turns out to be an intended policy of the PBOC to force banks to better manage liquidity.

- Massive liquidity squeeze in June caused by several factors.** Several specific factors contributed to the credit tightness in June, including misunderstanding between the markets and the PBOC about the policy stance and implementation, corporate tax payments, strong liquidity demand around a national holiday, the impact of measures taken in May to clamp down on capital inflows and turbulence in international capital markets after the announcement of the US's QE exit timeline. The surge in the cost of short-term funds stemmed from an overstretched financial sector and a mismatch between banks' short-term funding needs and long-term loans were the structural factor leading to the abnormality of money market.
- Misallocation of liquidity and expectation bias exaggerating the crunch.** In the past, banks got used to obtain additional liquidity from the PBOC through direct and indirect channels amid shortage of capital in the market. These induced them to engage in loose liquidity management and abnormal lending activities that pose threat to the real economy. The PBOC's stance on doing little to ease the tightness is an indication that the government's priority is to restore proper allocation of capital in fulfilling an implicit target for credit growth and boosting the economic growth.
- Paving the way for further interest rate liberalization.** It is becoming clear that China's new economic leadership team is willing to accept some short-term pain for long-term gains. In our view, China's liquidity crunch won't pose systemic risks to China's economy as the financial risks emanating from the non-bank financial system are not large and systemic enough to overwhelm macroeconomic and financial stability in China. As China moves to curb reckless credit growth and enhance transparency in order to tackle the structural problems in money market, it will need to discipline the market through not only a true threat, but also interest rate reform. A more market-oriented interest rate system will further optimize the credit structure to allow the financial sector to better serve the real economy. China will accelerate the pace of pushing forward market-oriented reform in interest rate system in 2H13.

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**農銀國際**

ABC INTERNATIONAL

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**China Economic Indicators**

	2012								2013				
	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May
Real GDP (YoY%)	---	7.6	---	---	7.4	---	---	7.9	---	---	7.7	---	---
Export Growth (YoY%)	15.3	11.1	1	2.7	9.9	11.6	2.9	14.1	25.0	21.8	10.0	14.7	1
Import Growth (YoY%)	12.7	6.3	4.7	-2.6	2.4	2.4	0	6	28.8	-15.2	14.1	16.8	-0.3
Trade Balance (USD/Bn)	18.13	31.91	25.28	26.43	27.45	32.11	19.63	31.6	29.2	15.3	-0.9	18.2	20.4
Retail Sales Growth (YoY%)	13.8	13.7	13.1	13.2	14.2	14.5	14.9	15.2	12.3		12.6	12.8	12.9
Industrial Production (YoY%)	9.6	9.5	9.2	8.9	9.2	9.6	10.1	10.3	9.9		8.9	9.3	9.2
PMI - Manufacturing (%)	50.4	50.2	50.1	49.2	49.8	50.2	50.6	50.6	50.4	50.1	50.9	50.6	50.8
PMI - Non-manufacturing (%)	55.2	56.7	55.6	56.3	53.7	55.5	55.6	56.1	56.2	54.5	55.6	54.5	54.3
FAI(YTD) (YoY%)	20.1	20.4	20.4	20.2	20.5	20.7	20.7	20.6	21.2		20.9	20.6	20.4
CPI (YoY%)	3	2.2	1.8	2	1.9	1.7	2	2.4	2.0	3.2	2.1	2.4	2.1
PPI (YoY%)	-1.4	-2.1	-2.9	-3.5	-3.6	-2.8	-2.2	-1.9	-1.6	-1.6	-1.9	-2.6	-2.9
M2 (YoY%)	13.2	13.6	13.9	13.5	14.8	14.1	13.9	13.8	15.9	15.2	15.7	16.1	15.8
New Lending (RMB/Bn)	793.23	919.83	540.1	703.9	623.2	505.2	522.9	454.3	1070.0	620.0	1060.0	793	667.4

**World Economic/Financial Indicators**

Equity Index				Global Commodities						Bond Yields & Key Interest Rates		
	Closing price	Chng. WTD (%)	P/E		Unit	Price	Chng. WTD (%)	Volume (5-day average)		Yield (%)	Chng. WTD (%)	
<b>US</b>				<b>Energy</b>	NYMEX WTI	USD/bbl	95.81	2.26	248482.60	US Fed Fund Rate	0.25	0.00
DJIA	14910.14	0.75	14.52		ICE Brent	USD/bbl	102.09	1.17	239224.40	US Prime Rate	3.25	0.00
S&P 500	1603.26	0.68	15.69		NYMEX Natural Gas	USD/MM Btu	3.73	-0.98	82086.60	US Discount Window	0.75	0.00
NASDAQ	3376.22	0.57	21.22		Australia Newcastle Steam Coal Spot fob	USD/Metric Tonne	81.20	N/A	N/A	US Treasury (1 Month)	0.0101	0.00
MSCI US	1528.38	0.71	15.97		LME Aluminum Cash	USD/MT	1725.75	-1.25	50952.20	US Treasury (10 Yr)	2.5205	-0.41
<b>Europe</b>				<b>Basic Metals</b>	LME Primary Aluminum 3 Month Rolling Forward	USD/MT	1771.00	-1.23	48997.60	US Treasury (30 Yr)	3.5698	-0.34
FTSE 100	6193.62	1.27	15.91		CMX Copper Active Contract	USD/lb.	306.10	-1.11	77301.00	Japan 10-Yr Government Bond	0.838	-4.34
DAX	7952.20	2.09	15.12		LME Copper 3 Month Rolling Forward	USD/MT	6735.00	-1.22	60750.80	China 10-Yr Government Bond	3.61	4.34
CAC40	3724.68	1.82	15.57		TSI CFR China Iron Ore Fines Index	USD	113.80	-4.05	N/A	ECB Interest Rate (Refinancing)	0.5	0.00
IBEX 35	7784.10	1.09	78.06		CMX Gold	USD/T. oz	1308.40	-5.71	114458.80	1-Month LIBOR	0.1954	1.22
FTSE MIB	15385.54	0.86	191.74	CMX Silver	USD/T. oz	20.28	-7.65	40805.40	3 Month LIBOR	0.2756	1.04	
Stoxx 600	284.70	1.53	N/A	NYMEX Platinum	USD/T. oz	1399.10	-3.34	12933.20	3-Month SHIBOR	5.539	-4.34	
MSCI UK	1822.45	0.78	15.71	CBOT Corn	USD/bu	665.00	0.49	79181.80	3-Month HIBOR	0.3821	-0.37	
MSCI France	104.03	1.74	19.10	CBOT Wheat	USD/bu	670.75	-3.90	43034.80	Corporate Bonds (Moody's Seasoned)			
MSCI Germany	108.61	1.84	13.95	NYB-ICE Sugar	USD/lb.	16.98	1.43	64044.00	Aaa	4.46	0.68	
MSCI Italy	44.23	1.00	53.30	CBOT Soybeans	USD/bu.	1537.50	2.96	52994.00	Baa	5.48	1.67	
<b>Asia</b>												
NIKKEI 225	13213.55	-0.13	24.23									
S&P/ASX 200	4811.28	1.53	19.49									
HSI	20440.08	0.87	9.45									
HSCEI	9158.61	-0.85	7.49									
CSI300	2160.74	-6.76	10.72									
SSE Composite	1950.01	-5.94	10.49									
SZSE Composite	886.91	-5.56	25.81									
MSCI China	53.06	-0.19	8.94									
MSCI Hong Kong	10854.47	0.36	9.74									
MSCI Japan	663.95	-2.71	21.47									
<b>Currency</b>												
									USD/ CNY			
									NDF			
									12 Month			
Spot Exchange Rate	1.3034	1.5292	0.9315	98.1700	0.9433	1.0436	6.1489	7.7572	6.3040			
Chng. WTD (%)	-0.67	-0.82	1.04	-0.28	-0.93	0.20	-0.26	0.01	-0.11			

Note:

1. Data source: Bloomberg Finance LP, National Bureau of Statistics of China, ABCIS
2. Australia Newcastle Steam Coal Spot fob is the Australia Newcastle 6700 kc GAD fob Steam Coal Spot price published by McCloskey
3. TSI CFR China Iron Ore Fines Index is calculated with the 62% Fe specification, spot price
4. Data is updated on the date of this report

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**Definition of equity rating**

<b>Rating</b>	<b>Definition</b>
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 from 2007-2011

Time horizon of share price target: 12-month

**Definition of share price risk**

<b>Rating</b>	<b>Definition</b>
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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