

Offshore Renminbi Weekly Report

<Forex> CNH held steady despite the continuing deflation data
 <Interest Rates > PBoC is set to cut 1Y MLF yield
 <Equity > Spillovers from shadow banking sector dampened China equities

Weekly Price Change	Week Open	Week High	Week Low	Week Close	Weekly change (※)
USD/CNH	7.1654	7.1897	7.1544	7.1743	-9
USD/CNY	7.1474	7.1768	7.1457	7.1659	+51
CNY PBoC Fixing	7.1006	7.1087	7.1006	7.1050	+53
Shanghai Composite Index	2,923.46	2,924.46	2,867.72	2,881.98	-6

※pips in USD/CNY,USD/CNH

Weekly Price Change	HK Close	Weekly Change	HK Close	Weekly Change
CNH Forward (1yr)	-1,732	-45	CNH HIBOR (3mth)	3.04%
CNH Currency Swap (3yr)	3.04%	-0.42 ppt	CNH Implied yield (1Y)	2.26%

【Last week's review and forecasts】

The CNH pared back some of its loss to near 7.17 level after hitting its one-month low of 7.1897 level. The PBoC's stronger easing bias and the increasing concern over the spillovers from the shadow banking sector weighed on RMB sentiment. In response, the PBoC ramped up its CNY fixing policy support to defend the currency, with the actual CNY fixing – estimate widening to its 6-week high of -609 pips. The China data calendar was busy, with deflation persisting for 3 straight months. Meanwhile, China trade figures for December improved, with exports and imports up 2.3%YoY and 0.2%YoY, respectively. Separately, Chinese local media reported that some cities employed the low-cost funding from the PBoC to purchase unsold homes and convert them into rental housing. While the policy makers are taking new initiatives to support property markets, investors are likely to remain cautious on the housing market until the recovery in housing figures is seen.

The PBoC added fuel to the fire by making even more dovish comments amid mounting expectation for an imminent rate cut in January. PBoC's Zou Lan, head of the central bank's monetary policy department, said that the central bank may use open market operations, medium-term lending facilities and reserve requirements to provide strong support for reasonable growth in credit. His dovish comment opened the door for the simultaneous cuts in rate and Reserves Requirement Ratio (RRR) before the Chinese New Year on 10 Feb. In the meantime, the PBoC net drained CNY liquidity for second consecutive week, net withdrawing CNY 189bn via the Open Market Operations (OMOs). 7-day interbank repo rate picked up to above 1.8%.

There are plenty of data and policy decisions to consider next week. Considering PBoC's strong easing bias and persistent deflation, the PBoC is set to resume its rate cut cycle by lowering 1Y MLF yield by 10bps. In the meantime, the PBoC is likely to keep its CNY fixing policy support to defend the currency against the Fed-PBoC monetary divergence. On the data front, Q4 GDP is expected to pick up on the recovery in consumption due to the pro-growth measures and the low-based effect. Retail sales for December is expected to remain supportive on the holiday spending, while industrial production will hold steady. The sluggish property market will drag on fixed assets investment, counteracting the positive impact from the infrastructure construction funded by government bond issuances.

【Data & Policy Updates】

China CPI and PPI decline narrowed to -0.3%YoY (vs. -0.4%YoY expected) and -2.7%YoY (vs. -2.6%YoY expected) from prior -0.5%YoY and -3.0%YoY, respectively. The falling food prices, down -3.7%YoY, remained the key reason for deflation, while the recreation, medical care and clothing items contributed to inflationary pressure. Excluding food prices, core CPI remained unchanged for third consecutive months at 0.6%YoY. On a monthly basis, CPI inflation reversed its decline and rose by 0.1% due to the logistic disruptions caused by cold weather conditions and the pick-up in demand before the New Year Eve.

< China CPI deflation persisted for 3 months >



< USD/CNY, USD/CNH vs. USD/CNY fixing >



(Sources: Bloomberg, Mizuho HK)

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