

## Macro Weekly: Economic outlook temporarily clouded by coronavirus outbreak

### This week's highlights

- **Breakout of 2019-nCoV likely a temporary drag on China growth in 1Q**

By 1 Feb, there were over 14k confirmed novel coronavirus (nCoV) cases in mainland China, over 60k suspected or under-observation cases, and 304 deaths. The silver lining was that on 1 Feb the number of cured cases, at 328, for the first time exceeded the number of deaths from the virus. The Chinese government has adopted a battery of infection prevention and epidemic control measures, including extending the holidays and traffic restrictions. The spread of the virus outside of China prompted the WHO to declare an international public health emergency, leading to travel bans by several countries. Against this backdrop, we expect the growth rate of certain service industries such as transportation, hospitality, catering and outdoor entertainment, to record notable declines in the first quarter. Lockdowns in China have also created difficulties for workers returning to work after the holidays.

The outbreak is a setback for the economic recovery that was underway in China. Our base-case scenario has new confirmed cases peaking in the next two weeks or so before economic activity regains momentum. Under this scenario, 1Q GDP growth would fall 1 ppt to c.5%. Production would begin to recover in Mar, driving overall growth to recover in 2Q, with GDP growth for 2020F of around 5.7%, lower than the 6.0% we had previously anticipated. Should the outbreak last longer than we expect, the economic impact on 1Q growth would be larger and full year growth could fall to 5.4%.<sup>1</sup> Offshore renminbi has depreciated nearly 2% against the US dollar over the past two weeks (Fig 1). We expect the exchange rate to come under pressure in the near term and hover around 6.9-7.0. We would expect the renminbi to return to modest appreciation once the outbreak is brought under control.

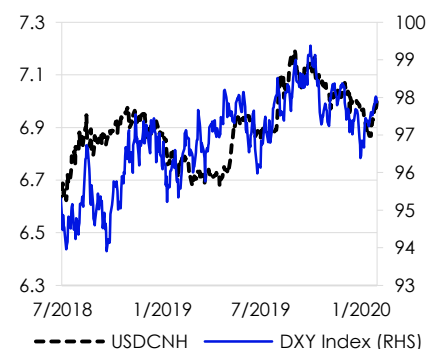
- **China's policymakers to step up liquidity and targeted credit support**

China's financial regulators and the Ministry of Finance jointly announced supportive policies in response to the nCoV outbreak. The PBoC reiterated that it would maintain loose liquidity conditions through open market operations, standing lending facilities, relending and re-discount tools. It also indicated that reverse repo operations will resume immediately after the Chinese New Year (CNY) holidays. Preferential financial services will be provided to regions, industries and enterprises hardest hit by the epidemic. Key producers of medical supplies will be allowed to borrow at lower interest rates through either fiscal-subsidized loans or the central bank's targeted relending program. In addition, the CSRC will allow delayed financial reporting for listed companies. We expect the central bank to continue with targeted credit support and liquidity operations in the near term. Fiscal support, including increased healthcare spending and tax reductions for affected services sectors are also likely.

- **China PMI yet to reflect impact of epidemic**

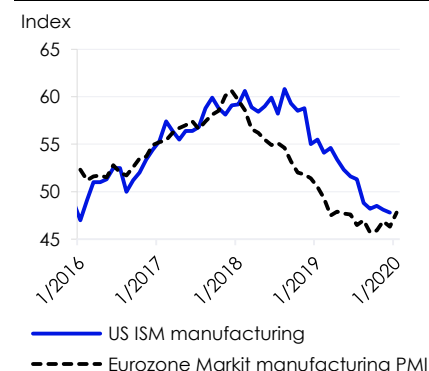
China's services and construction PMIs strengthened in Jan; however, surveys conducted before CNY would not reflect the impact of the outbreak. Manufacturing PMI eased in Jan due to the earlier CNY holidays, in line with our expectation. A breakdown of the results reveals that domestic demand continued to strengthen, likely driven by accelerated infrastructure spending thanks to a record issuance of special local government bonds in Jan. Meanwhile, latest overseas manufacturing data suggests the recovery taking place in the sector is well on track. Markit Eurozone Manufacturing PMI continued to rise (Fig 2) while Markit US Manufacturing PMI moderated in Jan, but stayed above 50.

**Fig 1. Renminbi exchange rate under pressure**



Source: CEIC, CCBIS

**Fig 2. Markit Euro Area PMI continued to recover, while consensus expects a rebound in US ISM**



Source: CEIC, CCBIS

**Li Cui**

(852) 3911 8274  
[cui@ccbintl.com](mailto:cui@ccbintl.com)

**Claire Huang**

(852) 3911 8012  
[clairehuang@ccbintl.com](mailto:clairehuang@ccbintl.com)

**Ying Xue**

(852) 3911 8013  
[xueying@ccbintl.com](mailto:xueying@ccbintl.com)

<sup>1</sup> CCBIS- [The Big Picture - First battle in the Year of Rat – How will the Wuhan coronavirus affect the economy?](#) (2 Feb 2020)

- **Fed identifies novel coronavirus as an uncertainty for the economic outlook**

At its Jan meeting, the FOMC kept its interest rate policy unchanged. Chairman Powell noted that some of the uncertainty around trade has diminished and suggested global growth may be stabilizing. The Fed will monitor remaining uncertainties, including those posed by the new coronavirus. The interest rate futures market is now expecting the Fed to cut rates as early as Jul this year. Prompted by rate cut expectations and risk aversion, the 10-year US Treasury yield fell 30 bp to 1.51% over the past two weeks.

### What's next?

- **China trade growth to dip temporarily into negative territory in Jan**

We expect Chinese export and import growth to turn negative in Jan due to the earlier CNY this year, with growth bouncing back over the subsequent months. The coronavirus outbreak will have a modest negative impact on trade growth in the near term; however, we do not believe it will derail the recovery in global manufacturing. We maintain our view that China trade will continue to rebound this year.

- **US data to rebound in Jan**

The US will release Jan ISM and labor market data next week. Markets are expecting both manufacturing and non-manufacturing ISM to rebound as uncertainty surrounding trade policy has subsided post the recent US-China trade agreement. Consensus is also expecting non-farm payrolls to record a bigger gain of 160k in Jan with a pickup in average hourly wage growth to 3% YoY.

**Table 1: Upcoming data releases and events**

| Date  | Time  | Country* | Data release                   | Period | Bloomberg  | CCBIS   | Prior      |
|-------|-------|----------|--------------------------------|--------|------------|---------|------------|
| 3 Feb | 9:30  | CH       | Industrial Profits YoY         | Dec    | --         | --      | 5.40%      |
| 3 Feb | 9:45  | CH       | Caixin China PMI Mfg           | Jan    | 51         | --      | 51.5       |
| 3 Feb | 23:00 | US       | ISM Manufacturing              | Jan    | 48.4       | --      | 47.2       |
| 5 Feb | 18:00 | EC       | Retail Sales MoM               | Dec    | -0.9%      | --      | 1.0%       |
| 5 Feb | 23:00 | US       | ISM Non-Manufacturing Index    | Jan    | 55.1       | --      | 55         |
| 7 Feb | --    | CH       | Exports YoY                    | Jan    | -4.5%      | -6.5%   | 7.6%       |
| 7 Feb | --    | CH       | Imports YoY                    | Jan    | 2.0%       | -17.6%  | 16.3%      |
| 7 Feb | --    | CH       | Trade Balance                  | Jan    | \$36.75b   | \$56.0b | \$46.79b   |
| 7 Feb | --    | CH       | Foreign Reserves               | Jan    | \$3095.00b | --      | \$3107.92b |
| 7 Feb | 21:30 | US       | Change in Nonfarm Payrolls     | Jan    | 160k       | --      | 145k       |
| 7 Feb | 21:30 | US       | Unemployment Rate              | Jan    | 3.5%       | --      | 3.5%       |
| 7 Feb | 21:30 | US       | Average Hourly Earnings YoY    | Jan    | 3.0%       | --      | 2.9%       |
| 7 Feb | 21:30 | US       | Labor Force Participation Rate | Jan    | --         | --      | 63.2%      |

| Date  | HK time | Country | Central bank speaker/event                                     |
|-------|---------|---------|--|
| 3 Feb | 17:15   | EC      | • ECB Vice President Guindos speaks in Athens                  |
| 4 Feb | 2:00    | EC      | • ECB President Lagarde attends reception in Frankfurt         |
| 4 Feb | 5:00    | US      | • Fed's Bostic discusses big data, AI and machine learning     |
| 5 Feb | 16:10   | EC      | • ECB Vice President Guindos speaks in Frankfurt               |
| 5 Feb | 20:15   | EC      | • ECB President Lagarde speaks in Paris                        |
| 6 Feb | 5:10    | US      | • Fed's Brainard discusses payment innovations                 |
| 6 Feb | 16:00   | EC      | • ECB President Lagarde speaks in Brussels                     |
| 6 Feb | 22:00   | EC      | • ECB's Villeroy speaks in Paris                               |
| 6 Feb | 22:15   | US      | • Fed's Kaplan discusses economic outlook in Dallas            |
| 7 Feb | 8:15    | US      | • Fed's Quarles discusses monetary policy and economic outlook |
| 8 Feb | 0:00    | US      | • Fed releases semi-annual monetary policy report to Congress  |

\* CH = China, EC=Euro area. Source: Bloomberg, CCBIS estimates

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**Outperform (O) – expected return > 10% over the next twelve months**

**Neutral (N) – expected return between -10% and 10% over the next twelve months**

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**CCB International Securities Limited**  
**12/F, CCB Tower, 3 Connaught Road, Central, Hong Kong**  
**Tel: (852) 3911 8000 / Fax: (852) 2537 0097**