

Macro Weekly: Chinese production shows signs of bottoming as policy stance signals more support

This week's highlights

- **Production bottoming in China as new viral cases decline**

China's epidemic prevention and control has proven effective, with the number of newly diagnosed and newly suspected cases on the decline. Against this backdrop, the State Council has asked local governments to carry out differentiated prevention measures and avoid over restricting people flows. The coastal economic engines – Guangdong and Zhejiang – have expedited the recruitment of migrant workers by providing "door-to-door" transportation services and streamlining health checks. High-frequency data including coal consumption at power plants has shown signs that production is bottoming out. We maintain our view that the manufacturing sector will begin to recover at the end of Feb.

- **China's Politburo promotes a more expansionary fiscal stance while PBoC signals a deposit rate cut**

China's Jan bank loans and total social financing (TSF) came in firmer than expected. While bank lending growth moderated as we expected, buoyant local government bond issuance helped overall TSF growth hold steady. We expect the issuance of local government bonds and policy financial bonds to re-accelerate in coming weeks as the recent Politburo meeting indicates a more expansionary fiscal policy. Liquidity easing is likely to remain measured in the near-term. Noting ample liquidity in the markets (Fig 1), the PBoC has been rolling back liquidity injections in recent weeks. It also reiterated a "no broad easing" decree in its latest monetary policy report. That said, following reductions in the LPR, the PBoC signaled the benchmark deposit rate could be lowered when appropriate. As for credit policy, we believe support will mainly target mitigating the impact on affected sectors, including catering, hospitality, entertainment, transportation and tourism services. In contrast, credit policy for the property sector will remained unchanged.

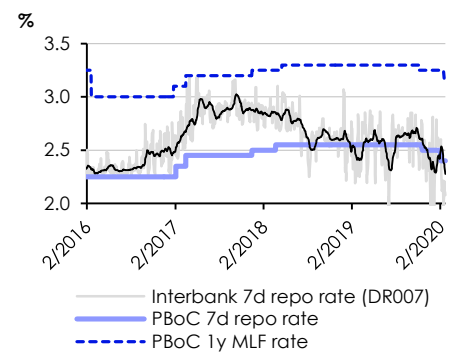
- **Policymakers step up support for consumer sector**

The State Council decided to waive part of the social security payments for companies for up to five months. Outside Hubei, SMEs will be exempted from paying certain social security fees from Feb to Jun, and those for large enterprises will be cut in half from Feb to Apr. Meanwhile, companies in Hubei will enjoy full exemption until Jun. Contributions to the housing provident funds may also be postponed. Meanwhile, the Ministry of Commerce has released measures to support foreign trade, FDI and consumption by simplifying administrative procedures and advancing fiscal spending towards affected sectors. These measures will support online consumption and new business models such as contactless delivery. As for the housing sector, more cities are beginning to ease up on land payments due from developers. A number of cities, including Wuxi, Fuzhou, Xiamen and Suzhou, have also relaxed pre-sale requirements.

- **Markets retreat on viral outbreak outside China; manufacturing data holds up**

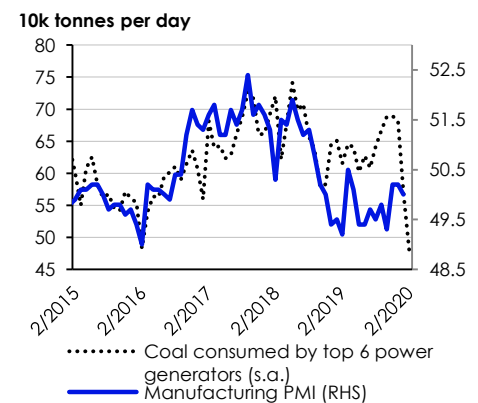
Feb Markit PMI reports for the euro area point to a solid recovery in the region's manufacturing sector despite the virus outbreak. Although US Markit PMI weakened, regional manufacturing reports defied market expectations by strengthening further in Feb. Nevertheless, market concerns about the COVID-19 outbreak outside China drove equity indexes to decline. The FX and rates markets also remained cautious while the 10-year UST yield fell below 1.5%. The Dollar Index climbed to nearly 100, causing the renminbi to dip.

Fig 1. Interbank liquidity remains ample



Source: CEIC, CCBIS

Fig 2. China's Manufacturing PMI expected to weaken



Source: CEIC, CCBIS

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What's next?

• China Feb manufacturing to suffer small dip

We expect China's official PMI to see a sharp but temporary decline in Feb given the suspension of production after the virus outbreak. Coal consumption by major power plants fell sharply in Feb (Fig 2), but appeared to bottom out thereafter. Most of the consumer services sector was still in suspended animation, however. As for the financial markets, the issuance of local government bonds was muted month to date. Land auctions in first-tier cities were buoyant and followed up with a relaxation of regulations on pre-sales in second-tier cities. Whether or not these relaxation measures will boost housing sales in the following weeks is still undetermined.

• US PCE inflation edges up, but euro area CPI remains sluggish

Following the upbeat Jan PPI report, the market expects US core PCE inflation to edge up to 1.7% YoY in Jan, which would still be weaker than the Fed target. In the euro area, market consensus forecasts weakening inflation in Feb to around 1% YoY, likely remaining unchanged in 2020F from 2019.

Table 1: Upcoming data releases and events

Date	Time	Country*	Data release	Period	Bloomberg	CCBIS	Prior
25 Feb	23:00	US	Conf. Board Consumer Confidence	Feb	132.5	--	131.6
27 Feb	18:00	EC	Economic Confidence	Feb	101.5	--	102.8
27 Feb	21:30	US	Durable Goods Orders	Jan P	-1.5%	--	2.4%
28 Feb	18:00	EC	CPI Estimate YoY	Feb	1.2%	--	1.4%
28 Feb	21:30	US	PCE Core Deflator YoY	Jan	1.7%	--	1.6%
29 Feb	9:00	CH	Manufacturing PMI	Feb	46	48	50

Date	HK time	Country	Central bank speaker/event
25 Feb	4:00	US	• Fed's Mester speaks on economy at NABE Conference
26 Feb	4:15	US	• Fed's Clarida addresses NABE Conference in Washington
26 Feb	19:00	EC	• ECB Governing Council member Makhlouf speaks in Berlin
28 Feb	0:30	US	• Fed's Evans speaks in Mexico City
28 Feb	18:00	EC	• Bundesbank President Weidmann speaks in Frankfurt
28 Feb	22:15	US	• Fed's Bullard discusses the economy and monetary policy

* CH = China, EC = Euro area

Source: Bloomberg, CCBIS estimates

Rating definitions:

Outperform (O) – expected return > 10% over the next twelve months
Neutral (N) – expected return between -10% and 10% over the next twelve months
Underperform (U) – expected return < -10% over the next twelve months

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