

China Bulletin: Market View

USDCNY Exchange Rate Implied by Gold Price



The rapid depreciation of CNY against USD and the sudden rise of volatility in overseas markets caught domestic Chinese investors off guard. Triggering reduced risk sentiment, and selloffs in both equity and bond markets. The depreciation expectation, measured by the price difference of gold spot traded in SHFE and COMEX, suggests the depreciation is mainly driven by external shock, instead of domestic outflows. Although the increasingly apparent divergence of monetary policy in China and the US implies a weaker CNY against USD, broad-based depreciation of CNY against a basket of currencies remains very unlikely. The turmoil in overseas markets may cause some outflows from China's capital markets and short-lived selling pressure, however the ongoing recovery and expected accommodative monetary policy point to outperformance of China's equity market versus global peers.

The latest housing market policy, granting home sellers income tax relief and allowing certain cities to lower interest rates, shows policy makers' determination and support.

Home sellers who buy another home within a year are eligible to be refunded their income tax on profits from the sale, which could be considerable given the tax is 20% price incremental, and housing prices have almost quintupled in the last 20 years. Cities seeing a year-on-year and quarter-on-quarter decline in housing prices in 22Q2 can adjust interest rates on a family's first residential mortgage loan till the end of 2022. The conditions are quite strict and reaffirm that housing prices are the primary constraint on any potential easing of housing policy. Positive policy should accelerate the turning point of the housing sector, yet it is still very difficult to predict how long it will take to restore market confidence. Best case the housing market could get through the current crisis as early as 23Q1, boosting China's growth outlook for next year. To reiterate, a non-bleeding housing market that doesn't drag down economic growth is the best scenario we can expect.

Latest PMI shows that the recovery and confidence remain fragile, especially among small manufacturers. Detailed analysis shows early signs of external demand weakening, as export orders retreat slightly from last month and exporter confidence has declined further. If the overseas turmoil continues, the drag from declining exports may start to bite as early as 22Q4. Domestic demand, especially fixed asset investment, may improve once the drag from the real estate sector wanes due to policy easing. The export downturn is only cyclical in our view, and structural drag forces may be about to reach their peak.

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