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Domestic Trade

Retail sales of consumer goods grow by 10.3% yoy in January to October 2016.

Ex-factory prices of industrial products continue to rise.

Both rural and urban households see high single-digit income growth in 1-3Q16.

Consumption tax adjusted on cosmetic products.

Growth in fixed asset investment falls to 8.3% yoy in January to October 2016.

China to introduce reform in allocation of spending responsibilities among central and local governments.

Confidence among entrepreneurs in secondary industry continues to improve.

Foreign Trade

Both exports and imports post year-on-year drop in October.

Exports to the US, the EU, the ASEAN, Japan and Brazil record negative growth in 1-3Q16.

Shanghai's exports contract by 8.6% yoy in 1-3Q16.

FDI grows by 4.2% in 1-3Q16.

Foreign exchange reserves fall at a faster pace.

Depreciation of the Chinese yuan against the US dollar quickens.

China to take a lead role in Asia-Pacific trade liberalization.

FUNG BUSINESS INTELLIGENCE

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Executive Summary

Domestic Trade

Retail sales of consumer goods reached 26,960.1 billion yuan in January to October 2016, up nominally by 10.3% yoy. Online retail sales of goods, which accounted for 11.8% of total retail sales, surged by 24.9% yoy in the period.

Ex-factory prices of industrial products have been rising. The producer price index of industrial products went up by 0.7% mom in October, posting month-on-month gain for four consecutive months.

Both rural and urban households saw high single-digit income growth in 1-3Q16: the per capita disposable income of rural households increased nominally by 8.4% yoy to reach 8,998 yuan; while that of urban households rose by 7.8% yoy in nominal terms to reach 25,337 yuan.

China adjusted consumption tax on cosmetic products on 1 October. The consumption tax rates for high-end cosmetic products were reduced to 15%, while the consumption tax on general cosmetic products was abolished on 1 October. The change in tax policy would provide more room for retailers to lower prices of cosmetic products.

Growth in fixed asset investment fell to 8.3% yoy in January to October 2016, due mainly to the deceleration in growth in FAI in the secondary industry.

China will introduce reform in allocation of spending responsibilities among central and local governments. On 24 August, the State Council released the 'Guiding Opinions on the Reform in Dividing Fiscal Duties and Spending Responsibilities among the Central and the Local Governments'. The reform includes clarifying the spending responsibilities among the central and the local governments as well as assigning more fiscal duties to the central government.

Confidence among Chinese entrepreneurs in the secondary industry has continued to improve. China's Entrepreneur Confidence Index for the secondary industry came in at 111.4 in 3Q16, posting quarter-on-quarter gain for two consecutive quarters.

Foreign Trade

Both exports and imports posted year-on-year drop in October. Exports and imports were down by 7.3% yoy and 1.4% yoy respectively in the month.

Exports to the US, the EU, the ASEAN, Japan and Brazil dropped by 4.3% yoy, 7.8% yoy, 5.5% yoy, 7.8% yoy and 28.3% yoy respectively in 1-3Q16. In contrast, China's exports to Russia and India managed to record positive growth of 7.1% yoy and 1.3% yoy respectively in the same period.

All top six provinces/ municipalities in terms of exports witnessed negative year-on-year growth in exports in 1-3Q16. Among these provinces and municipalities, Shanghai saw the sharpest fall in exports (minus 8.6% yoy) in 1-3Q16.

FDI grew by 4.2% yoy to reach 609.0 billion yuan in 1-3Q16. The share of the service sector in the total FDI went up to 70.7% in 1-3Q16 from 61.1% in 2015. Among industries, FDI in the 'transportation, storage and postal industry', the 'information transmission, computer services and software industry' and the 'leasing and business services industry' posted rapid growth of 92.0% yoy, 166.7% yoy and 73.8% yoy respectively in 1-3Q16.

Foreign exchange reserves have fallen at a faster pace. After dropping by US$ 7.4 billion in 2Q16, China's foreign exchange reserves went down by US$ 38.8 billion in 3Q16, and then fell by US$ 45.7 billion in October.

Depreciation of the Chinese yuan against the US dollar has quickened since early November. So far this year, the Chinese yuan has depreciated by 5.8% against the US dollar (as of 18 November).

China would take a lead role in Asia-Pacific trade liberalization, if the US turns towards protectionism. China has been pushing for the RCEP and the FTAPP. On 19 November, Chinese President Xi Jinping delivered a keynote speech at the APEC CEO Summit, calling for trade and economic cooperation and urging regional leaders to advance trade deals. In contrast, given Trump's protectionist stance, it is widely expected that the US government will tear up the TPP, and renegotiate or even withdraw from the NAFTA.

Part 1 :

Domestic Trade

A Recent developments

1. China's real GDP growth stays stable in 3Q16

According to the National Bureau of Statistics, China's real GDP growth came in at 6.7% year-on-year (yoy) in 3Q16, the same as in 1Q16 and 2Q16 (see exhibit 1). Overall, in 1-3Q16, China's nominal GDP amounted to 53.0 trillion yuan, up by 6.7% yoy in real terms.

The tertiary industry has continued to grow faster than the secondary industry. The value-added of the tertiary industry, which contributed 52.8% of China's nominal GDP in 1-3Q16, gained 7.6% yoy in real terms in 1-3Q16. It is noteworthy that the value-added of the property sector witnessed strong growth of 8.9% yoy in real terms in 1-3Q16, showing the strong performance of the sector amid the booming housing market in China. Meanwhile, the value-added of the secondary industry, which contributed 39.5% of the country's nominal GDP, increased 6.1% yoy in real terms over the same period.

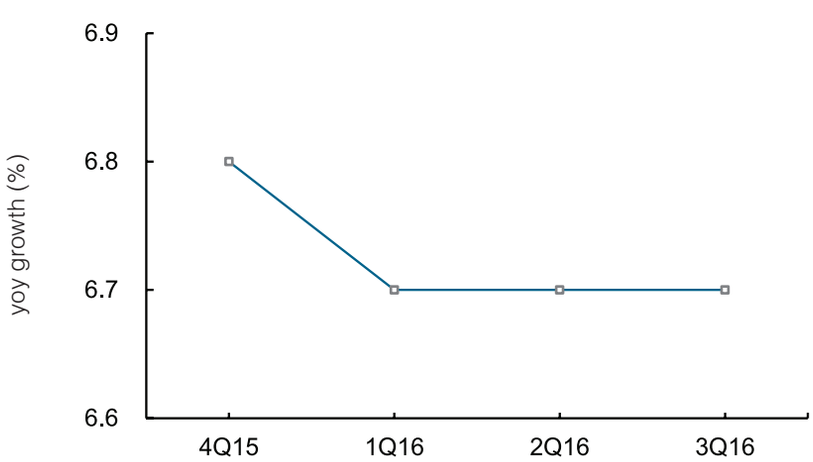
Compared to investment, consumption has played a more important role in boosting economic growth. In 1-3Q16, the contribution by final consumption expenditure to GDP growth was 71.0%, while the contribution by gross capital formation was 36.8%.[1] Net exports made a negative contribution (minus 7.8%) to the GDP growth in the same period.

Looking ahead, the Chinese government will strive to maintain stable economic growth in near term. On the monetary front, the central bank will ensure abundant liquidity to support the real economy, though monetary policy is unlikely to be very loose in order to maintain exchange rate stability and curb asset bubbles. On the fiscal front, the government will increase fiscal expenditure as well as infrastructure investment. On 5 September, Premier Li Keqiang presided at a State Council meeting, suggesting that the government should strengthen its efforts to carry out a proactive fiscal policy and should focus on areas such as poverty relief, new industries, post disaster reconstruction, water conservancy facilities and other major infrastructure.

The government will also accelerate the 'supply-side reforms', the main tasks of which include tackling the overcapacity problem, reducing housing inventories, de-leveraging, bringing down costs on enterprises and shoring up weak areas. In late August, the State Council published the 'Work Plan of Reducing Costs for Enterprises in the Real Economy'. According to the plan, various government departments will introduce a series of measures to reduce the tax burden, as well as the costs of financing, institutional transaction, labour, energy and logistics on enterprises.

All in all, we predict that, China's economic growth will be relatively stable in coming future. Going forward, we forecast the real GDP growth to be around 6.8% yoy in 4Q16. Downside risks to the economic growth persist, including the negative impact of the recent tightening on the property market and greater uncertainty over the global economy caused by Donald Trump's victory in the 2016 US Presidential Election, the Deutsche Bank crisis and the 'Brexit' decision, to name a few.

Exhibit 1 China's real GDP growth, 4Q15 to 3Q16



FY15	6.9%
4Q15	6.8%
1Q16	6.7%
2Q16	6.7%
3Q16	6.7%

Source: National Bureau of Statistics, PRC

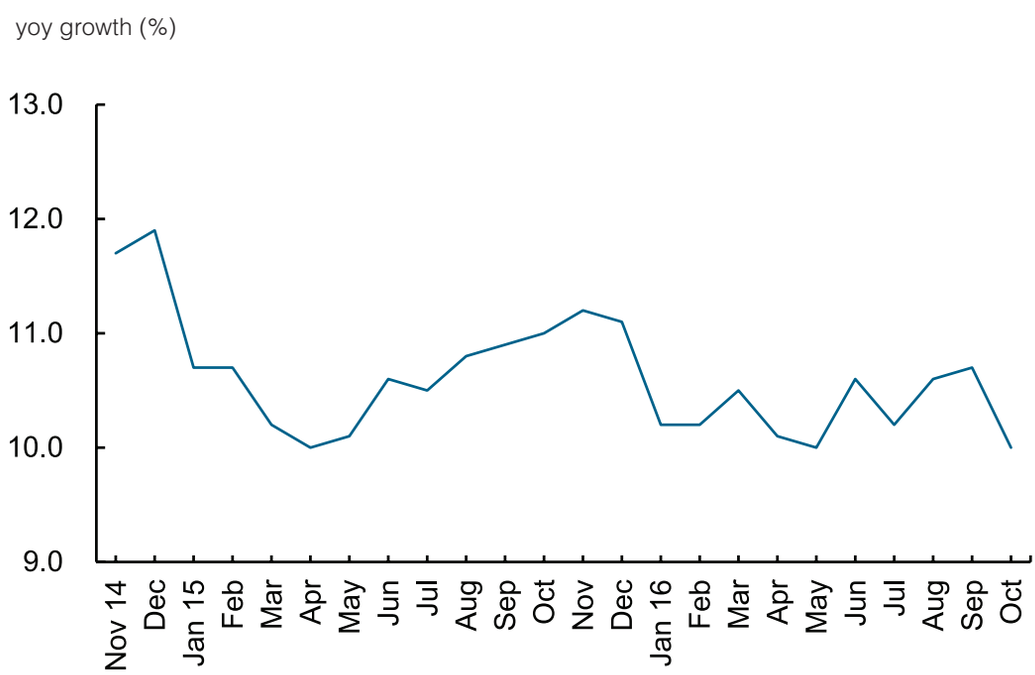
1 http://www.stats.gov.cn/tjsj/sjjd/201610/t20161019_1411444.html

2. Retail sales growth decelerates

According to the National Bureau of Statistics, the growth in China's total retail sales of consumer goods decelerated from 10.7% yoy in September to a five-month low of 10.0% yoy in October. The month-on-month (mom) growth in seasonally-adjusted retail sales also dropped from 0.86% in August to 0.81% in September and 0.71% in October. These figures indicate a moderation in consumption demand. Overall, in January to October 2016, the total retail sales of consumer goods reached 26,960.1 billion yuan. The nominal growth rate was 10.3% yoy in January to October 2016, lower than the 10.7% yoy growth seen in 2015 (see exhibits 2 and 3).

China's online retail sales of goods rose strongly by 24.9% yoy to reach 3,174.0 billion yuan in January to October 2016. Consequently, the share of online retail sales in the total retail sales of consumer goods went up to 11.8% in January to October 2016 from 10.8% in 2015, indicating that online shopping has become more popular.

Exhibit 2 China's total retail sales, year-on-year nominal growth, November 2014 to October 2016



FY15	10.7%
Nov 15	11.2%
Dec	11.1%
Jan-Feb 16	10.2%
Mar	10.5%
Apr	10.1%
May	10.0%
Jun	10.6%
Jul	10.2%
Aug	10.6%
Sep	10.7%
Oct	10.0%

Source: National Bureau of Statistics, PRC

Exhibit 3 China's total retail sales, month-on-month nominal growth, May to October 2016

mom growth (%), seasonally adjusted

	May 16	Jun	Jul	Aug	Sep	Oct
Total retail sales	0.74	0.90	0.74	0.86	0.81	0.71

Source: National Bureau of Statistics, PRC

Rural retail sales have been growing slightly faster than urban retail sales. In January to October 2016, rural retail sales expanded by 10.9% yoy to reach 3,776.8 billion yuan, while urban retail sales rose by 10.2% yoy to 23,183.3 billion yuan.

Growth in both sales of goods and catering services sales decelerated: the nominal growth in catering services sales moderated from 11.7% yoy in 2015 to 10.9% yoy in January to October 2016, while the nominal growth in sales of goods fell from 10.6% yoy in 2015 to 10.3% yoy in January to October 2016.

Retail sales of goods by enterprises above a designated size[2] rose 7.8% yoy to reach 12,231.2 billion yuan in January to October 2016. By product category, sales of 'furniture' and 'building and decoration materials' posted rapid growth of 13.5% yoy and 15.1% yoy respectively, attributed to the strong sales of new homes in recent months. Besides, boosted by the cut in the purchase tax rate on passenger-vehicles with less than 1.6 litre, the growth in sales of 'automobiles' accelerated to 9.1% yoy in January to October 2016 from 5.3% yoy in 2015. In contrast, sales of 'gold, silver and jewellery' fell by 0.9% yoy in January to October 2016, indicating that the demand for jewellery from Chinese consumers has remained sluggish. Exhibit 5 demonstrates the growth in China's retail sales by product among enterprises above a designated size.

Exhibit 4 China's total retail sales, 2015 to October 2016

Nominal growth, yoy (%)	FY15	1Q16	1H16	1-3Q16	Oct
Total retail sales	10.7	10.3	10.3	10.4	10.0
Goods	10.6	10.2	10.2	10.3	10.1
Sales by enterprises above a designated size	7.9	8.0	7.6	7.9	7.7
Online sales	31.6	25.9	26.6	25.1	-
Catering services	11.7	11.3	11.2	11.0	10.0

Source: National Bureau of Statistics, PRC

3. Chinese consumers become less optimistic

The consumer confidence index[3] fell from 106.8 in July to 105.6 in August and 104.6 in September. The downtrend of the index indicates that Chinese consumers have become less optimistic recently (see exhibit 6).

4. Both rural and urban households see high single-digit growth in income

Both rural and urban households saw high single-digit growth in income in 1-3Q16, amid the stable labour market. In 1-3Q16, the per capita disposable income of rural households increased nominally by 8.4% yoy (or 6.5% yoy real) to reach 8,998 yuan; while the per capita disposable income of urban households rose by 7.8% yoy in nominal terms (or 5.7% yoy real) to reach 25,337 yuan.

2 'Enterprises above a designated size' refers to enterprises with annual sales of 5 million yuan or more and with an employee strength of 60 or more.

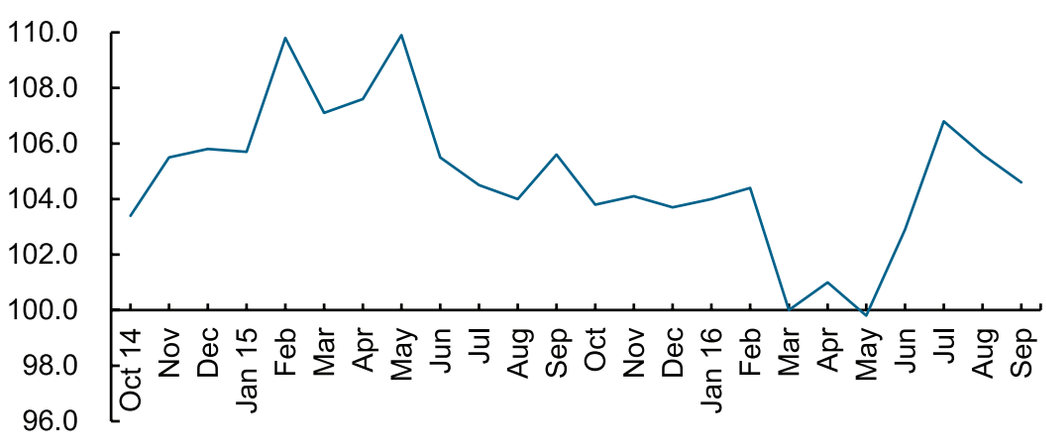
3 A reading above 100 indicates that consumers tend to be optimistic; a reading below 100 indicates that consumers tend to be pessimistic.

Exhibit 5 China's retail sales by enterprises above a designated size, by product, 2015 to October 2016

Nominal growth, yoy (%)	2015	1Q16	1H16	1-3Q16	Oct
Grain, oil and food	15.1	12.7	12.3	11.7	9.1
Beverages	15.3	9.8	10.7	11.0	8.9
Tobacco and liquor	12.7	7.6	9.2	9.1	7.9
Clothing, shoes, hats and textiles	9.8	7.2	7.0	7.2	7.5
Cosmetics	8.8	10.6	8.9	8.4	4.0
Gold, silver and jewellery	7.3	-3.9	-1.5	-1.3	2.5
Products for daily use	12.3	10.9	11.7	11.4	9.5
Sports and entertainment products	16.6	16.3	16.9	12.9	9.4
Home appliances and video equipment	11.4	7.2	7.3	7.9	7.6
Chinese and Western medicines	14.2	15.1	13.3	12.5	11.6
Stationery and office accessories	15.2	7.4	9.2	9.7	12.7
Furniture	16.1	16.2	15.6	13.9	11.0
Telecommunications equipment	29.3	18.9	14.9	12.7	3.8
Petroleum and related products	-6.6	0.4	-1.3	-0.5	4.7
Automobiles	5.3	7.7	7.7	9.1	8.7
Building and decoration materials	18.7	15.2	15.6	15.4	12.3

Source: National Bureau of Statistics, PRC

Exhibit 6 China's consumer confidence index, October 2014 to September 2016



Oct 15	103.8
Nov	104.1
Dec	103.7
Jan 16	104.0
Feb	104.4
Mar	100.0
Apr	101.0
May	99.8
Jun	102.9
Jul	106.8
Aug	105.6
Sep	104.6

Source: National Bureau of Statistics, PRC

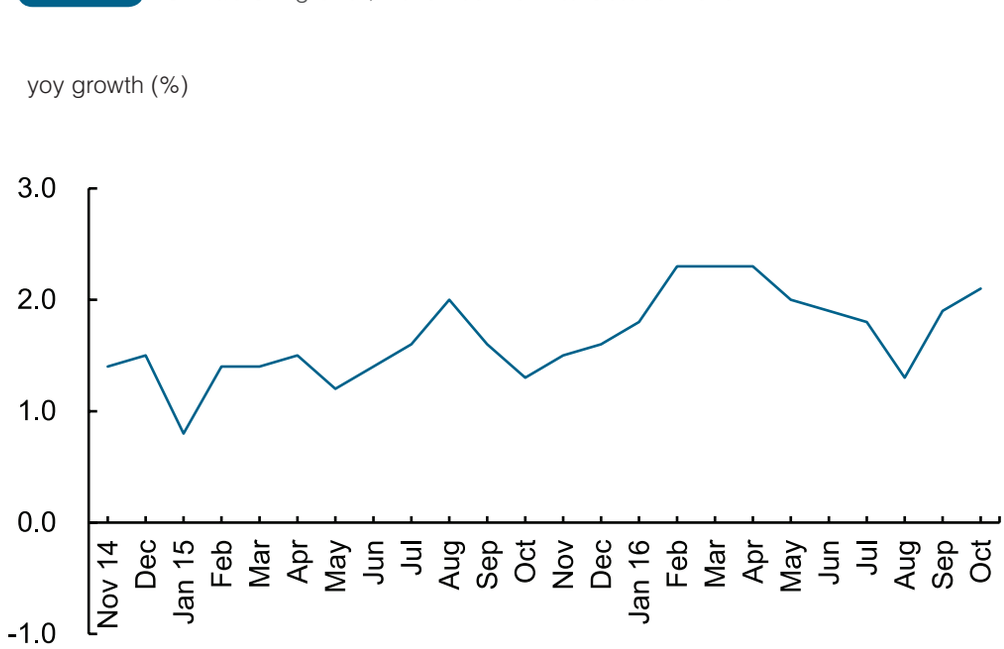
5. Consumer inflation rebounds

After falling from 1.8% in July to 1.3% in August, the year-on-year growth rate for China's consumer price index (CPI)[4] rebounded to 1.9% in September and 2.1% in October.

The rise in CPI growth in recent months was due largely to the pick-up in the year-on-year growth of the food component in the CPI, which accelerated to 3.7% in October from 1.3% in August. Meanwhile, the year-on-year growth of the non-food component in the CPI also rose to a 28-month high of 1.7% in October, driven mainly by the rise in prices of healthcare services, fees on extracurricular education and property management (see exhibits 7 and 8).

Looking ahead, we expect the food inflation to stay high in the near future, due mainly to high vegetable prices. Overall, in our view, the CPI growth is likely to stay around 2.0% in the coming months.

Exhibit 7 China's CPI growth, November 2014 to October 2016



Nov 15	1.5%
Dec	1.6%
Jan 16	1.8%
Feb	2.3%
Mar	2.3%
Apr	2.3%
May	2.0%
Jun	1.9%
Jul	1.8%
Aug	1.3%
Sep	1.9%
Oct	2.1%

Source: National Bureau of Statistics, PRC

4 The CPI, compiled by the National Bureau of Statistics (NBS) of China, measures the price of a basket of goods and services purchased by a typical household. It is noteworthy that the NBS has changed the weights assigned to the various components in the CPI basket, effective from January 2016. The weight of the food component, for example, has been reduced by 3.2 ppt; the weight of the housing component has been increased by 2.2 ppt; and the weights of other components have been adjusted by around or less than 1 ppt. The impact of the re-weighting on the CPI growth was limited, according to the NBS.

Exhibit 8 China's CPI growth by commodity, May to October 2016[5]

yoy growth (%)	May 16	Jun	Jul	Aug	Sep	Oct
Food, tobacco and liquor	4.7	3.7	2.8	1.5	2.7	3.0
Clothing	1.5	1.4	1.4	1.5	1.2	1.3
Housing	1.6	1.6	1.6	1.5	1.5	1.8
Household goods and services	0.6	0.6	0.6	0.4	0.3	0.4
Transportation and communication	-2.6	-1.8	-1.6	-1.2	-0.4	-0.4
Education, culture and recreational activities	1.2	1.4	1.6	1.3	2.0	2.1
Medical and healthcare	3.5	3.8	4.3	4.3	4.3	4.8
Other goods and services	2.2	2.6	4.4	4.5	4.4	3.6

Source: National Bureau of Statistics, PRC

The year-on-year growth rate for China's producer price index of industrial products (PPI)[6] went up from minus 1.7% in July to minus 0.8% in August, and further to 0.1% in September, returning to the positive territory for the first time in more than four years. Afterwards, the PPI growth further went up to 1.2% yoy in October (see exhibits 9 & 10).

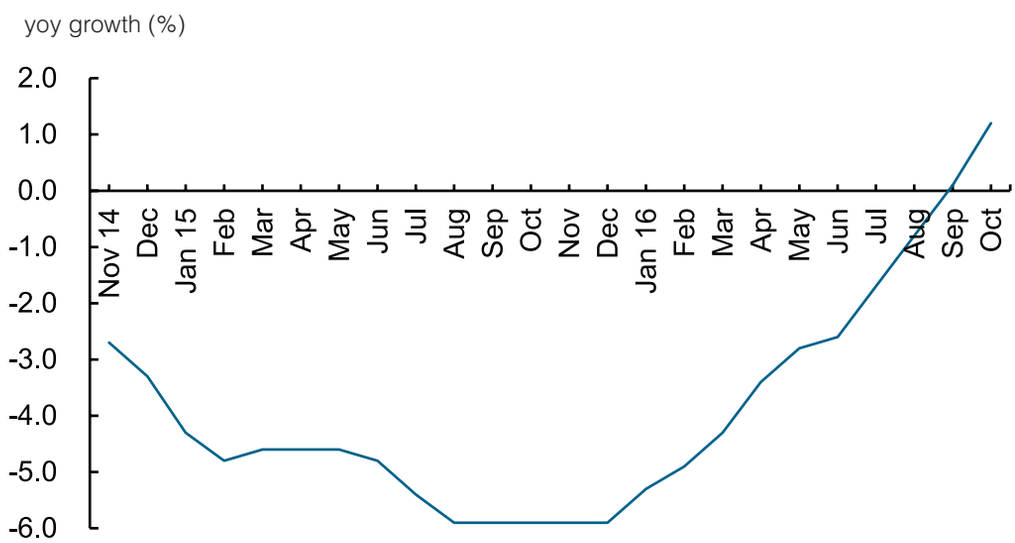
On a month-on-month basis, the PPI rose by 0.7% in October, posting gain for four consecutive months. The rise in the PPI in October was mainly due to the increases in the ex-factory prices of the 'manufacture and processing of ferrous metals', 'manufacture and processing of nonferrous metals', 'manufacture of chemical materials and products', 'processing of petroleum' and 'mining and washing of coal' industries in the month.

Going forward, driven by the increase in prices of production inputs, the year-on-year growth in the PPI is expected to stay in the positive territory in the near future.

5 The NBS has re-categorized the categories in the CPI basket, effective from January 2016. For example, the old category of 'household goods and maintenance services' has been re-categorized into a new category called 'household goods and services' and the category of 'other goods and services'. The old category of 'recreational, educational products and services' has been re-categorized into a new category called 'education, culture and recreational activities' and the category of 'other goods and services'.

6 The PPI, compiled by the National Bureau of Statistics of China, measures the prices of industrial products when they are sold for the first time after production.

Exhibit 9 China's PPI growth, November 2014 to October 2016



Nov 15	-5.9%
Dec	-5.9%
Jan 16	-5.3%
Feb	-4.9%
Mar	-4.3%
Apr	-3.4%
May	-2.8%
Jun	-2.6%
Jul	-1.7%
Aug	-0.8%
Sep	0.1%
Oct	1.2%

Source: National Bureau of Statistics, PRC

Exhibit 10 China's PPI growth by selected industry, May to October 2016

yoy growth (%)	May 16	Jun	Jul	Aug	Sep	Oct
Textile	-2.6	-2.3	-1.4	-0.8	-0.4	0.3
Textile wearing apparel and ornament	0.5	0.6	0.7	0.4	0.3	0.3
Timber processing & wood, bamboo, cane, palm fiber and straw products	-0.5	-0.3	0.4	-0.2	-0.2	0.0

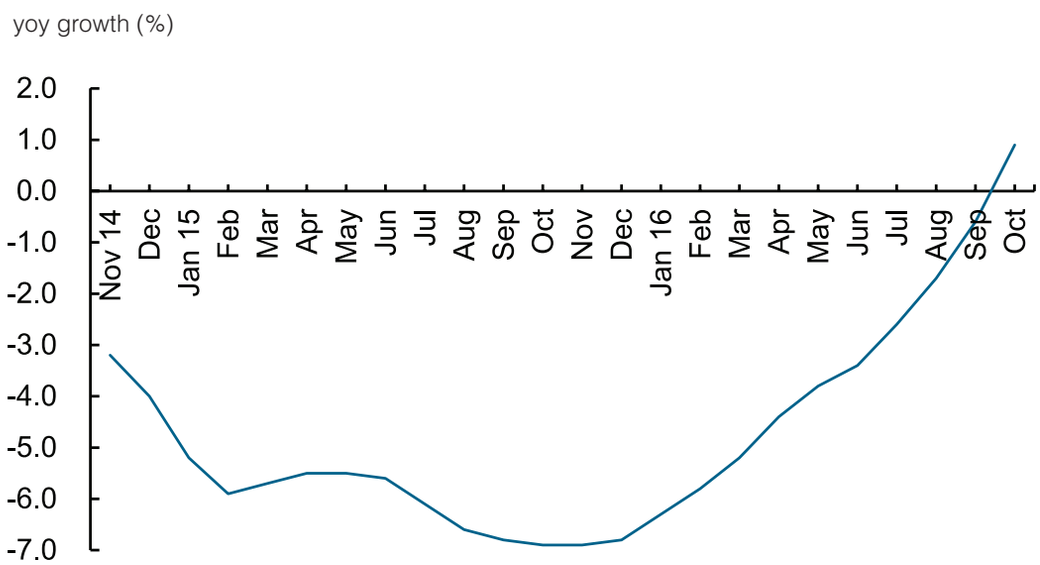
Source: National Bureau of Statistics, PRC

On a month-on-month basis, the purchaser price index of industrial products rose by 0.9% in October, posting gain for eight consecutive months. The increase in the purchaser price index in recent months can be attributed to the bottoming out of global commodity prices and the Chinese government's efforts to cut excessive industrial capacity, in our view.

The year-on-year growth rate for the purchaser price index of industrial products has also turned positive, registering 0.9% in October (see exhibits 11 & 12).

The input prices sub-index of China's manufacturing PMI, a leading indicator of upstream prices, has stayed above the critical 50-mark for ten straight months from February through November, indicating that prices of production inputs have been on an upward trend. Thus, we believe that the year-on-year growth rate for the purchaser price index of industrial products will stay in the positive territory or even rise further in coming months.

Exhibit 11 Growth in China's purchaser price index of industrial products, November 2014 to October 2016



Nov 15	-6.9%
Dec	-6.8%
Jan 16	-6.3%
Feb	-5.8%
Mar	-5.2%
Apr	-4.4%
May	-3.8%
Jun	-3.4%
Jul	-2.6%
Aug	-1.7%
Sep	-0.6%
Oct	0.9%

Source: National Bureau of Statistics, PRC

Exhibit 12 China's purchaser price index of industrial products by selected commodity, May to October 2016

yoy growth (%)	May 16	Jun	Jul	Aug	Sep	Oct
Fuel and power	-8.3	-7.2	-6.2	-5.0	-1.9	1.8
Non-ferrous metal materials and wires	-7.0	-5.7	-2.5	-0.3	0.3	2.2
Chemical raw materials	-4.1	-4.2	-3.6	-2.5	-1.6	-0.1
Wood and pulp	-0.7	-0.8	-0.8	-0.6	-0.7	-0.3
Textile raw materials	-1.3	-1.2	-0.4	0.1	0.1	1.0

Source: National Bureau of Statistics, PRC

6. Growth in industrial production decelerates

The growth rate for China's industrial production (IP), measured by value-added of industrial output (VAIO), fell from 6.3% yoy in August to 6.1% yoy in September and October (see exhibit 13).[7] The deceleration in IP growth could be associated with production suspension of many manufacturers in eastern provinces. Several local governments in eastern provinces ordered manufacturers in certain industries such as textile, dyeing and petrochemical to cut or even suspend production ahead of and during the G20 Leaders Summit in Hangzhou on 4-5 September, in a bid to improve the air quality in the city. Overall, in January to October 2016, China's IP expanded by 6.0% yoy, slightly slower than the 6.1% yoy growth recorded in 2015.

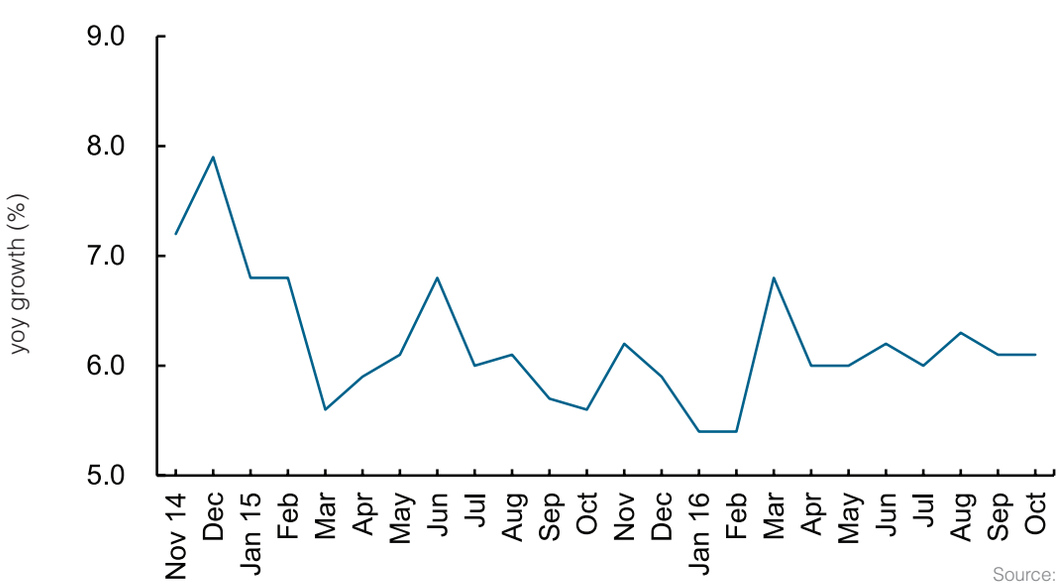
In the coming months, industrial activities will be supported by the positive impact of the government's moves to boost domestic demand. Meanwhile, challenges facing Chinese manufacturers include the greater economic uncertainty caused by Donald Trump's victory in the 2016 US Presidential Election, the Deutsche Bank crisis and the 'Brexit' decision, recent tightening on property market in China, heavy debt burden, increasing labour and environmental costs, intense competition in the international market, a rise in foreign trade protectionism and weaker luxury spending. Overall, we expect that the industrial production (VAIO) growth will accelerate to 6.5% yoy in 4Q16.

7. Industrial profits grow by 8.4% yoy in 1-3Q16

The growth in the total profits earned by large and medium industrial enterprises above a designated size[8] decelerated from 19.5% yoy in August to 7.7% yoy in September, due largely to the rise in comparison base in the same period of the previous year. Overall, in 1-3Q16, China's industrial profits amounted to 4,638.1 billion yuan, up by 8.4% yoy (see exhibit 14).

Among the sectors, profits of the manufacturing sector recorded double-digit growth of 13.5% yoy in the first nine months of 2016. In contrast, profits of the mining sector plunged by 62.1% yoy, while profits of the electricity, heat, gas and water sector dropped by 3.6% yoy over the same period.

Exhibit 13 China's industrial production growth, November 2014 to October 2016



Nov 15	6.2%
Dec	5.9%
Jan-Feb 16	5.4%
Mar	6.8%
Apr	6.0%
May	6.0%
Jun	6.2%
Jul	6.0%
Aug	6.3%
Sep	6.1%
Oct	6.1%

Source: National Bureau of Statistics, PRC

7 The National Bureau of Statistics has changed the method of compiling the value added for industry (industrial production, IP), effective January 2011. The statistical threshold for industrial enterprises has been raised to cover those with annual revenues of 20 million yuan or above, up from the previous threshold of 5 million yuan or above.

8 'Industrial enterprises above a designated size' refers to industrial enterprises with annual sales of 20 million yuan or more.

Exhibit 14 China's industrial profits growth, April to September 2016

yoy growth (%)	Apr 16	May	Jun	Jul	Aug	Sep
Total profits made by industrial enterprises above a designated size	4.2	3.7	5.1	11.0	19.5	7.7

Source: National Bureau of Statistics, PRC

8. Secondary industry drags down growth in total fixed asset investment

The growth in China's nominal fixed asset investment (FAI) (excluding rural households) moderated to 8.3% yoy in January to October 2016 from 10.0% yoy in 2015, due mainly to the deceleration in growth in FAI in the secondary industry.[9] In January to October 2016, China's nominal FAI (excluding rural households) amounted to 48.4 trillion yuan (see exhibit 15).

Due partly to the overcapacity problem, the growth in FAI (excluding rural households) in the secondary industry fell to 2.9% yoy in January to October 2016, down from the 8.0% yoy growth recorded in 2015. In contrast, the growth in FAI (excluding rural households) for real estate development accelerated to 6.6% yoy in January to October 2016 from 1.0% yoy in 2015, as the booming housing market has encouraged property developers to make property investment. Meanwhile, FAI in infrastructure (excluding power, heat, gas and water infrastructure) grew rapidly by 19.4% yoy in January to October 2016, supported by the government move to drive the infrastructure investment.

Going forward, the government has started tightening the property markets in various cities in China, and therefore, we expect property developers to slow their investment in real estate development. On the other hand, the government has increased its efforts to boost investment in the country recently. According to the report on the State Council meeting published on the government website on 6 September, the government will accelerate the progress of the major projects identified in the 13th Five-year Plan, relax the restrictions in investment in infrastructure in selected areas, promote Public-Private Partnership (PPP) projects and encourage central state-owned enterprises to make investment in weak areas such as power grids and telecommunication infrastructure in rural areas. All these efforts may help offset the potential impact of property tightening on the investment in real estate development.

Exhibit 15 China's FAI (excluding rural households) growth, May to October 2016

	May 16	Jun	Jul	Aug	Sep	Oct
FAI (excluding rural households) *(year-to-date, yoy growth %)*	9.6	9.0	8.1	8.1	8.2	8.3
FAI (excluding rural households) *(mom growth %, seasonally adjusted)*	0.59	0.62	0.52	0.58	0.59	0.58

Source: National Bureau of Statistics, PRC

9 The National Bureau of Statistics has expanded coverage of the monthly statistics for FAI from the urban areas to rural enterprises and institutions, effective from 2011. Thus: 'FAI (excluding rural households)', the new indicator, has been released by the bureau as from March 2011 to replace 'urban FAI', the previous indicator. Also, a new statistical criterion has been adopted. The statistical threshold for the size of investment projects has been adjusted upwards from 500,000 yuan to 5 million yuan.

B Highlights

1. China adjusts consumption tax on cosmetic products

On 30 September, the Ministry of Finance and the State Administration of Taxation jointly announced to adjust consumption tax on cosmetic products, effective from 1 October.[10]

The consumption tax rates for high-end cosmetic products were reduced to 15%, while the consumption tax on general cosmetic products was abolished on 1 October. According to the announcement, high-end cosmetic products refer to those items at ex-factory prices (before value-added-tax) or import prices (before value-added-tax) higher than or equal to 10 yuan per millilitre or 15 yuan per piece.

The revision of the consumption tax policy would provide more room for retailers to lower prices, which should in turn attract more Chinese consumers to make purchases of cosmetic products in the mainland. This policy change can therefore be viewed as part of the government's efforts to boost domestic consumption.

2. China to introduce reform in allocation of spending responsibilities among central and local governments

On 24 August, the State Council released the 'Guiding Opinions on the Reform in Dividing Fiscal Duties and Spending Responsibilities among the Central and the Local Governments'.[11] One of the major purposes of the reform is to improve the efficiency of public services through clarifying the responsibilities among the central and the local governments. Particularly noteworthy is that the reform will assign more fiscal duties to the central government, which has more financial resources in comparison to local governments.

According to the document, the central government should be responsible for providing public services related to the exercise of national sovereignty, the maintenance of a united market, and other national-wide public services; the local governments should be responsible for providing public services at local levels; and cross-provincial public services should be jointly provided by the central and the local governments. It is targeted that reform in major areas will be completed by 2019-2020.

We believe that, if successful, the reform will help improve people's livelihood in China.

3. Growth in RMB loans moderates

The growth in RMB loans has moderated in recent months. As at the end of October, the total outstanding RMB loans gained 13.1% yoy, compared to the growth of 14.3% yoy as at the end of June. Meanwhile, the broad money supply (M2) grew by 11.6% yoy as at the end of October 2016 (see exhibit 16).

In October, the total outstanding RMB loans increased by 651.3 billion yuan. The RMB loans to households contributed 66.5% of the increase in total RMB loans in the month. Driven mainly by the demand for housing mortgages, the total outstanding RMB loans to households gained 433.1 billion yuan in October. Meanwhile, the total outstanding RMB loans to non-financial business and other sectors expanded by 168.4 billion yuan in the month.

Looking ahead, the central bank will ensure abundant liquidity to support the real economy, though monetary policy is unlikely to be very loose in order to maintain exchange rate stability and curb asset bubbles. And as the property tightening measures launched in recent months are likely to weaken the demand for housing mortgages, we expect the growth in RMB loans to soften further in near future.

10 http://www.chinatax.gov.cn/n810341/n810755/c2279432/content.html

11 http://www.gov.cn/zhengce/content/2016-08/24/content_5101963.htm

Exhibit 16 Broad money supply (M2) and RMB loans, November 2015 to October 2016

	Broad money supply (M2)		Total outstanding RMB loans	
As of	Amount (trillion yuan)	yoy growth	Amount (trillion yuan)	yoy growth
End-Nov 15	137.4	13.7%	93.4	14.9%
End-Dec	139.2	13.3%	94.0	14.3%
End-Jan 16	141.6	14.0%	96.5	15.3%
End-Feb	142.5	13.3%	97.2	14.7%
End-Mar	144.6	13.4%	98.6	14.7%
End-Apr	144.5	12.8%	99.1	14.4%
End-May	146.2	11.8%	100.1	14.4%
End-Jun	149.1	11.8%	101.5	14.3%
End-Jul	149.2	10.2%	102.0	12.9%
End-Aug	151.1	11.4%	102.9	13.0%
End-Sep	151.6	11.5%	104.1	13.0%
End-Oct	152.0	11.6%	104.8	13.1%

	Increase in RMB loans (trillion yuan)
FY15	11.72
Jan-Oct 16	10.16
Nov 15	0.71
Dec	0.60
Jan 16	2.51
Feb	0.73
Mar	1.37
Apr	0.56
May	0.99
Jun	1.38
Jul	0.46
Aug	0.95
Sep	1.22
Oct	0.65

Source: People's Bank of China

4. 'Total social financing' increases by a larger amount in January to October

The increase in 'total social financing' (covering sources of financing such as RMB loans to the real sector, foreign currency loans to the real sector, trust loans, entrusted loans, bank acceptance bills, corporate bonds, equity issuance and other instruments) amounted to 14.4 trillion yuan in the first ten months of 2016, larger than the increase seen in the same period of the previous year (i.e. 12.6 trillion yuan) (see exhibit 17).

Compared to FY15, RMB loans, trust loans, entrusted loans, corporate bonds and equity issuance played a more important role in driving up 'total social financing' in the first ten months of this year. For example, RMB loans contributed 73.8% of the increase in 'total social financing' in January to October, compared to the 73.1% share in the previous year.

Exhibit 17 Increase in total social financing, 2015 to January-October 2016

	FY15		Jan-Oct 16	
	Amount (billion yuan)	Share (%)	Amount (billion yuan)	Share (%)
Total social financing	15,410	100.0	14,350	100.0
RMB loans to the real sector	11,269	73.1	10,597	73.8
Foreign currency loans to the real sector	-643	-4.2	-494	-3.4
Trust loans	43	0.3	533	3.7
Entrusted loans	1,591	10.3	1,585	11.0
Bank acceptance bills	-1,057	-6.9	-2,230	-15.5
Corporate bonds	2,825	18.3	2,850	19.9
Equity issuance	760	4.9	1,073	7.5

Source: People's Bank of China

C Outlook

1. Entrepreneur Confidence Index records quarter-on-quarter gain for the second consecutive quarter

China's Entrepreneur Confidence Index (ECI) for the secondary industry rose by 2.1 pts from the previous quarter to a four-quarter high of 111.4 in 3Q16. The index has posted quarter-on-quarter gain for two consecutive quarters, indicating the continuous improvement in confidence among Chinese entrepreneurs in the industry (see exhibit 18).[12]

The ECIs for the 'manufacturing' and 'mining' sectors recorded quarter-on-quarter increases, while the ECI for 'electricity, gas & water' sector registered a slight quarter-on-quarter drop in 3Q16. It is noteworthy that, though still in the 'pessimistic' zone', the ECI for the 'mining' sector went up sharply by 11.3 pts from the previous quarter to 86.9 in 3Q16, indicating that entrepreneurs in this sector have become less pessimistic. This may be explained by the rise in prices of raw materials and commodities in past few months (see exhibit 19).

2. PMI indicates growth acceleration of China's manufacturing sector

China's manufacturing Purchasing Managers' Index (PMI) has been on an upward trend in recent months. The index rose all the way from 49.9 in July to 51.7 in November, the highest level since August 2014. The latest trend in the PMI indicates that the growth in the manufacturing sector in China has continued to accelerate (see exhibit 20).

One of the main drivers behind the rising PMI was the faster growth in new orders. The new orders index went up strongly from 50.9 in September to 52.8 in October, and further to a 28-month high of 53.2 in November.[13] Meanwhile, the new export orders index rose from 49.2 in October to 50.3 in November. The index returned to the expansionary zone in November, indicating that the month-on-month growth in new export orders has turned positive recently.

Amid the better demand, the output index climbed from 53.3 in October to 53.9 in November. The latest reading is the highest in 28 months, indicating the quick growth in output in November.

Purchasing activities have also increased at a relatively fast pace in recent months. The purchases of inputs index went up from 51.9 in September to 52.4 in October, and further to 52.9 in November.

Both the stocks of finished goods index and the stocks of major inputs index have remained below the critical 50-mark in the past few months, indicating that destocking activities have continued.

The input prices index went up all the way from 51.3 in June to 68.3 in November, showing that prices of production inputs have gone up at a quicker pace. Cost pressure on manufacturers has been building up.

After staying high at 58.2, 58.4 and 58.5 in August, September and October respectively, the business expectations index fell to 55.5 in November. The latest index reading indicates that purchasing managers have become less optimistic about the near term outlook for their respective industries.

12 China's Entrepreneur Confidence Index (ECI) ranges from 0 to 200. A reading above 100 indicates that entrepreneurs tend to be optimistic; a reading below 100 indicates that they tend to be pessimistic.

13 The 'new orders index' covers both domestic and export orders. That is to say, the manufacturers are not asked to differentiate between domestic and export orders when filling in questionnaires.

Exhibit 18 China's Entrepreneur Confidence Index (Secondary Industry), 4Q14 to 3Q16

	4Q14	1Q15	2Q15	3Q15	4Q15	1Q16	2Q16	3Q16
Entrepreneur Confidence Index (Secondary Industry)	115.1	120.6	114.5	112.1	108.9	108.7	109.3	111.4

Source: National Bureau of Statistics, PRC

Exhibit 19 Entrepreneur Confidence Index by sector, 2Q16 and 3Q16

	2Q16	3Q16	Compared with the previous quarter
Secondary industry	109.3	111.4	Higher
Mining	75.6	86.9	Higher
Manufacturing	110.5	114.4	Higher
Electricity, gas & water	123.6	123.2	Lower

Source: National Bureau of Statistics, PRC

Exhibit 20 China's manufacturing PMI at a glance, November 2016

Index	Seasonally Adjusted Index	Index Compared with the Previous Month	Direction
PMI	51.7	Higher	Expanding
Output	53.9	Higher	Expanding
New orders	53.2	Higher	Expanding
New export orders	50.3	Higher	Expanding
Backlogs of orders	46.7	Higher	Contracting
Stocks of finished goods	45.9	Lower	Contracting
Purchases of inputs	52.9	Higher	Expanding
Imports	50.6	Higher	Expanding
Input prices	68.3	Higher	Rising
Stocks of major inputs	48.4	Higher	Contracting
Employment	49.2	Higher	Contracting
Suppliers' delivery time	49.7	Lower	Slowing
Business expectations	55.5	Lower	Optimistic

Source: China Federation of Logistics & Purchasing; National Bureau of Statistics, PRC

3. Non-manufacturing sector expands at a faster pace

China's Business Activity Index, which is quoted as the Non-manufacturing Purchasing Managers' Index (NMI), rose all the way from 53.5 in August to 54.7 in November, the highest level since July 2014. The latest index reading indicates that the non-manufacturing sector has expanded at a faster pace recently (see exhibit 21).

The growth acceleration of the non-manufacturing sector has been boosted by a continuous increase in new orders. The new orders index came in at 51.8 in November, staying above the critical 50-mark for three consecutive months.

Enterprises have been raising their service charges. The sales prices index registered 50.4, 50.1, 51.5 and 51.4 in August, September, October and November respectively, above the critical 50-mark. An important reason for the hike in service charges was the sustained increase in the costs of inputs. In fact, the input prices index has stayed above 50 since February this year.

The business expectation index recorded 59.4, 61.1, 60.6 and 60.7 in August, September, October and November respectively, well above the critical 50-mark. Purchasing managers in the non-manufacturing sector have been optimistic recently.

Exhibit 21 China's non-manufacturing purchasing managers' index (NMI) at a glance, November 2016

Index	Seasonally Adjusted Index	Index Compared with the Previous Month	Direction
Business activity	54.7	Higher	Expanding
New orders	51.8	Higher	Expanding
Input prices	53.5	Lower	Rising
Sales prices	51.4	Lower	Rising
Business expectations	60.7	Higher	Optimistic

Source: China Federation of Logistics & Purchasing; National Bureau of Statistics, PRC

Part 2 :

Foreign Trade

A Recent developments

1. Both exports and imports post yoy drop in October

China's export growth deteriorated to minus 6.3% yoy in 3Q16 from minus 4.4% yoy in 2Q16 (see exhibits 22, 23 and 24). The weak export performance in 3Q16 was due largely to the weakening external demand, and the production suspension of many manufacturers in eastern provinces. To improve the air quality in Hangzhou, several local governments in eastern provinces ordered manufacturers in certain industries such as textile, dyeing and petrochemical to cut or even suspend production ahead of and during the G20 Leaders Summit in Hangzhou on 4-5 September. Overall, in 1-3Q16, China's exports amounted to US$ 1,537.0 billion, down by 7.5% yoy.

China's exports to most of its major trading partners showed negative yoy growth in the first three quarters of this year. Exports to the US, the EU, Japan, the ASEAN and Brazil dropped by 4.3% yoy, 7.8% yoy, 5.5% yoy, 7.8% yoy and 28.3% yoy respectively in 1-3Q16. In contrast, China's exports to Russia and India managed to record positive growth of 7.1% yoy and 1.3% yoy respectively in 1-3Q16, indicating that the demand for Chinese products from these two emerging countries has strengthened.

China's imports fell at a slower pace, by 4.7% yoy, in 3Q16, after dropping by 13.5% yoy and 6.8% yoy respectively in 1Q16 and 2Q16. Overall, in 1-3Q16, China's imports totalled US$ 1,140.7 billion, down by 8.2% yoy.

It is also noteworthy that China's imports of some major commodities increased during the period, taking advantage of the drop in commodity prices. China's imports of iron ore, crude, coal and copper increased by 9.1% yoy, 14.0% yoy, 15.2% yoy and 11.8% yoy, respectively, in volume terms in 1-3Q16.

In October, both China's exports and imports posted yoy drop, down by 7.3% and 1.4% respectively. The latest figures indicate that the foreign demand for Chinese products and the domestic demand for imported products have remained weak recently.

China's trade surplus remained high at US$ 146.3 billion in 3Q16, up from US$ 143.7 billion in 2Q16. Such a massive trade surplus may encourage foreign politicians to advocate tough trade policies on Chinese products, posing risk to China's exports.

Exhibit 22 China's quarterly foreign trade data, 4Q15 to 3Q16

USD billion (yoy growth)

	Exports		Imports		Trade Balance
FY15	2,276.6	(-2.8%)	1,682.1	(-14.1%)	594.5
4Q15	613.8	(-5.0%)	438.0	(-11.8%)	175.8
1Q16	463.9	(-9.6%)	338.2	(-13.5%)	125.7
2Q16	534.2	(-4.4%)	390.6	(-6.8%)	143.7
3Q16	559.8	(-6.3%)	413.5	(-4.7%)	146.3

Source: China Customs

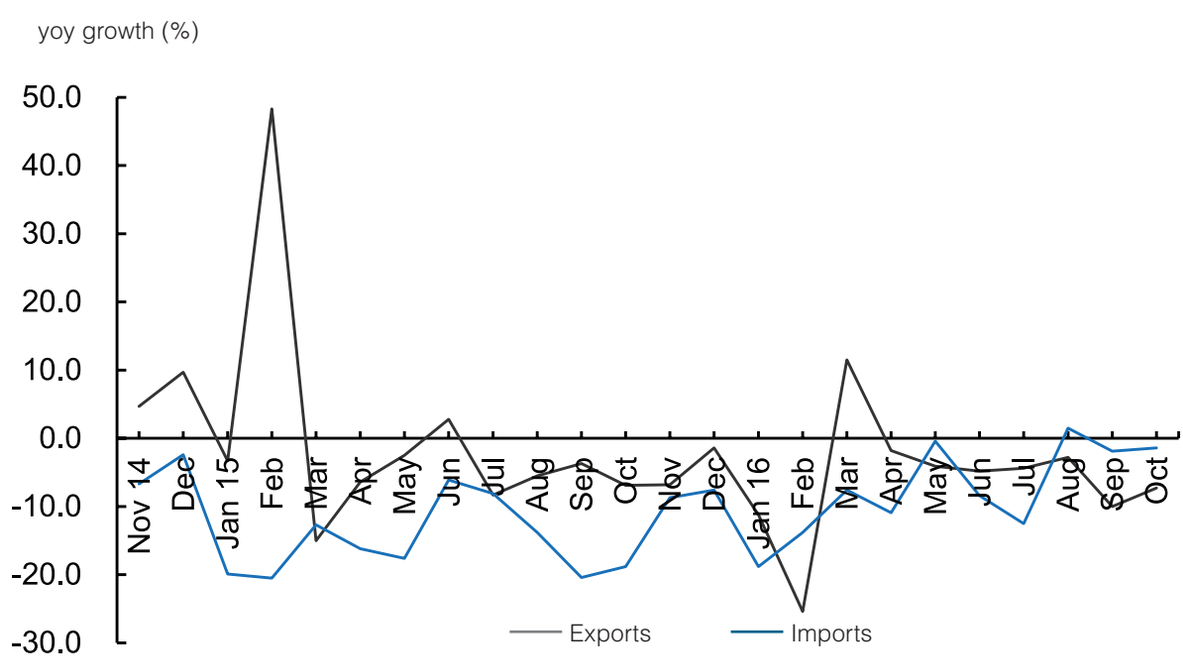
Exhibit 23 China's monthly foreign trade data, November 2015 to October 2016

USD billion (yoy growth)

	Exports		Imports		Trade Balance
November 2015	197.2	(-6.8%)	143.1	(-8.7%)	54.1
December	224.2	(-1.4%)	164.1	(-7.6%)	60.1
January 2016	177.5	(-11.2%)	114.2	(-18.8%)	63.3
February	126.1	(-25.4%)	93.6	(-13.8%)	32.6
March	160.8	(11.5%)	131.0	(-7.6%)	29.9
April	172.8	(-1.8%)	127.2	(-10.9%)	45.6
May	181.1	(-4.1%)	131.1	(-0.4%)	50.0
June	180.4	(-4.8%)	132.3	(-8.4%)	48.1
July	184.7	(-4.4%)	132.4	(-12.5%)	52.3
August	190.6	(-2.8%)	138.5	(1.5%)	52.0
September	184.5	(-10.0%)	142.5	(-1.9%)	42.0
October	178.2	(-7.3%)	129.1	(-1.4%)	49.1

Source: China Customs

Exhibit 24 Growth rates of exports and imports, November 2014 to October 2016



Source: China Customs

Exhibit 25 Exports by category, 2015 and 1-3Q16

yoy growth (%) of export value, calculated in USD	2015	1-3Q16
Textile materials and products	-2.3	-3.6
Garments and clothing accessories	-6.4	-7.5
Footwear	-4.8	-12.7
Toys	10.8	9.9
Coal	-28.3	20.4
Crude oil	215.0	-53.0
Refined oil	-25.9	-4.1
Steel	-11.3	-14.9
Mechanical and electrical products	0.1	-7.6

Source: China Customs

Exhibit 26 Imports by category, 2015 and 1-3Q16

yoy growth (%) of import value, calculated in USD	2015	1-3Q16
Cereal and cereal flour	51.1	-38.2
Soybean	-13.6	-6.2
Iron ore	-38.3	-6.4
Crude oil	-41.1	-20.6
Refined oil	-39.0	-27.4
Steel	-20.0	-12.1
Textile yarns, fabric and textile products	-6.4	-15.8
Vehicles and vehicle chassis	-26.1	-6.2

Source: China Customs

2. Both general trade exports and processing trade exports continue to post year-on-year negative growth in 3Q16

Both the general trade[14] exports and the processing trade[15] exports continued to post year-on-year negative growth in 3Q16. It is noteworthy that the growth of the general trade exports deteriorated to minus 9.9% yoy in 3Q16 from minus 1.1% yoy in 2Q16. Meanwhile, the processing trade exports fell by 8.7% yoy in 3Q16, compared with the 12.1% yoy decline in 2Q16 (see exhibit 27).

Both the general trade imports and the processing trade imports posted smaller year-on-year drop in 3Q16, compared to 2Q16. After falling by 3.6% yoy in 2Q16, the general trade imports contracted slightly by 0.3% yoy in 3Q16. In the meantime, the processing trade imports were down by 7.9% yoy in 3Q16, compared to the 15.3% yoy drop in 2Q16. In our view, the fall in the processing trade imports in 3Q16 suggests that the processing trade exports are likely to continue to show negative growth in the near future, as processing trade imports serve as a leading indicator of processing trade exports performance.

Correspondingly, the share of processing trade in China's total trade stayed low at 30.0% in 3Q16. Nevertheless, with a large surplus of US$ 82.1 billion in 3Q16, processing trade still plays an important role in China's foreign trade.

14 'General trade' refers to China's import or export of goods by enterprises holding import-export rights. According to China's National Bureau of Statistics, the scope of general trade covers: Imports and exports using loans or aids; the import of materials by foreign invested enterprises (FIEs) for processing of goods for sale in the domestic market; the export of goods purchased by FIEs or manufactured by processing domestically-produced materials; the import of food and beverages by restaurants and hotels; the supply of domestically-produced fuels, materials, parts and components to foreign vessels or aircraft; the import of goods as payment in kind, in lieu of wages in labour service cooperation projects with foreign countries; and the export of equipment and materials by enterprises in China for their investment abroad.

15 'Processing trade' refers to the business of importing all or part of the raw and auxiliary materials, parts and components, accessories and packaging materials from abroad, and re-exporting the finished products after processing or assembly by enterprises within the Chinese Mainland.

Exhibit 27 China foreign trade (general and processing trades), 2015 to 3Q16

Item	yoy growth (%)			Share (%)		
	FY15	2Q16	3Q16	FY15	2Q16	3Q16
Exports	-2.8	-4.4	-6.3	100.0	100.0	100.0
Of which:						
General Trade	1.1	-1.1	-9.9	53.5	56.6	51.2
Processing Trade	-9.8	-12.1	-8.7	35.0	31.4	33.4
Imports	-14.1	-6.8	-4.7	100.0	100.0	100.0
Of which:						
General Trade	-16.8	-3.6	-0.3	54.9	57.8	57.2
Processing Trade	-14.8	-15.3	-7.9	26.6	23.5	25.4
Total of Imports and Exports	-8.0	-5.3	-5.6	100.0	100.0	100.0
Of which:						
General Trade	-7.5	-2.2	-5.8	54.1	57.1	53.8
Processing Trade	-11.6	-13.2	-8.4	31.4	28.1	30.0

Source: China Customs

3. Sino-US trade falls by 9.2% yoy in 1-3Q16

The EU was still China's largest trading partner, accounting for 15.1% of China's total foreign trade in 1-3Q16. Sino-EU trade amounted to US$ 405.3 billion in 1-3Q16, down by 3.5% yoy. Specifically, China's exports to the EU fell by 4.3% yoy in 1-3Q16, compared to the 4.0% yoy drop in 2015; the growth of China's imports from the EU improved to minus 2.3% yoy in 1-3Q16 from minus 14.5% yoy in 2015 (see exhibits 28 and 29).

The US continued to be China's second largest trading partner in 1-3Q16, accounting for 14.0% of China's total foreign trade. Sino-US trade fell by 9.2% yoy in 1-3Q16, after registering a weak growth of 0.6% yoy in 2015. China's export growth to the US turned negative, registering minus 7.8% yoy in 1-3Q16, compared to the positive growth of 3.4% yoy in 2015. Meanwhile, China's import growth from the US deteriorated to minus 12.9% yoy in 1-3Q16 from minus 6.5% yoy in 2015.

The Association of South East Asian Nations (ASEAN) accounted for 12.1% of China's total foreign trade in 1-3Q16. China's trade with ASEAN dropped by 6.7% yoy to US$ 324.1 billion in 1-3Q16. Of which, China's exports to ASEAN shrank by 7.8% yoy, and China's imports from ASEAN contracted by 5.3% yoy, in 1-3Q16.

Sino-Japanese trade contracted by 3.2% yoy to US$ 200.0 billion in 1-3Q16. China's exports to Japan fell by 5.5% yoy, while China's imports from Japan slid 1.2% yoy in 1-3Q16.

4. China's exports to Russia gain 7.1% yoy in 1-3Q16

In 1-3Q16, the growth of China's exports to Russia accelerated quickly to 7.1% yoy, up from minus 35.2% yoy in 2015. The recovery in the exports to Russia could be attributed to the recent improvement in the country's economy. Meanwhile, the growth of China's imports from Russia improved to minus 6.4% yoy in 1-3Q16 from minus 20.0% yoy in 2015 (see exhibits 28 and 29).

China's exports to India managed to record a positive growth of 1.3% yoy in 1-3Q16. In contrast, China's imports from India dropped markedly by 15.6% yoy over the same period. Overall, the growth of Sino-Indian trade worsened to minus 1.9% yoy in 1-3Q16 from 1.5% yoy in 2015.

Sino-Brazilian trade dropped by 6.6% yoy in 1-3Q16. China's exports to Brazil fell by 28.3% yoy in 1-3Q16. In contrast, China's import from Brazil expanded by 7.7% over the same period.

Together, these three BRIC members accounted for 5.6% of China's total exports and 5.9% of China's total imports in 1-3Q16, up from 5.3% and 5.4%, respectively, in 2015.

Exhibit 28 China's trading partners, 1-3Q16

Country/ Region	Trade value (USD billion)	Share of total trade (%)	Export value (USD billion)	Import value (USD billion)	yoy growth (%)		
					Total trade	Exports	Imports
EU	405.3	15.1	250.8	154.5	-3.5	-4.3	-2.2
US	374.0	14.0	279.2	94.8	-9.2	-7.8	-12.9
ASEAN	324.1	12.1	187.4	136.7	-6.7	-7.8	-5.3
Japan	200.0	7.5	95.0	105.1	-3.2	-5.5	-1.2
Brazil	51.8	1.9	15.7	36.0	-6.6	-28.3	7.7
Russia	50.3	1.9	27.0	23.3	0.4	7.1	-6.4
India	52.3	2.0	43.9	8.5	-1.9	1.3	-15.6

Source: China Customs

Exhibit 29 China's trading partners, comparing growth rates for 2015 and 1-3Q16

yoy growth (%)

Country/Region	Total Trade		Exports		Imports	
	2015	1-3Q16	2015	1-3Q16	2015	1-3Q16
EU	-8.2	-3.5	-4.0	-4.3	-14.5	-2.2
US	0.6	-9.2	3.4	-7.8	-6.5	-12.9
ASEAN	-1.7	-6.7	2.1	-7.8	-6.6	-5.3
Japan	-10.8	-3.2	-9.2	-5.5	-12.2	-1.2
Brazil	-17.3	-6.6	-21.4	-28.3	-14.5	7.7
Russia	-28.6	0.4	-35.2	7.1	-20.0	-6.4
India	1.5	-1.9	7.4	1.3	-18.2	-15.6

Source: China Customs

5. All top six provinces/ municipalities in terms of exports witness negative year-on-year growth in exports in 1-3Q16

All top six provinces and municipalities in terms of value of exports – Guangdong, Jiangsu, Shanghai, Zhejiang, Shandong and Fujian – witnessed negative year-on-year growth in exports in 1-3Q16 (see exhibit 30).[16] Among these provinces, Shanghai saw the sharpest fall in exports, which went down by 8.6% yoy in 1-3Q16.

Several provinces, however, witnessed positive growth in exports in 1-3Q16. Exports from Shanxi, Hubei, Shaanxi, and Xinjiang expanded by 12.0% yoy, 1.4 % yoy, 7.3% yoy, and 2.2% yoy respectively in 1-3Q16.

16 China's top six provinces and municipalities in terms of value of exports – Guangdong, Jiangsu, Shanghai, Zhejiang, Shandong and Fujian – jointly accounted for 79.3% of China's total China's exports in 1-3Q16.

Exhibit 30 Top six provinces and municipalities in terms of value of exports, 1-3Q16

Provinces/ Municipalities	Value of exports (USD billion)	yoy growth (%)	Share of total exports (%)
Guangdong	475.8	-8.2	31.0
Jiangsu	244.2	-6.1	15.9
Zhejiang	204.0	-3.7	13.3
Shanghai	120.9	-8.6	7.9
Shandong	107.4	-2.3	7.0
Fujian	65.0	-8.2	4.2

Source: China Customs

6. FDI in Renminbi terms records positive year-on-year growth in three of the last four months

China's foreign direct investment (FDI) in Renminbi terms gained 1.2% yoy in September, recording positive year-on-year growth in three of the last four months. Overall, in 1-3Q16, China's FDI amounted to 609.0 billion yuan, up by 4.2% yoy (see exhibit 31).

FDI in the service sector increased by 9.0% yoy to 430.7 billion yuan in 1-3Q16. The share of the service sector in China's total FDI reached 70.7% in 1-3Q16, up from 61.1% in 2015. Among the industries in the service sector, FDI in the 'transportation, storage and postal industry', the 'information transmission, computer services and software industry' and the 'leasing and business services industry' posted rapid growth of 92.0% yoy, 166.7% yoy and 73.8% yoy respectively in 1-3Q16.

Among the industries in the manufacturing sector, FDI in the 'pharmaceutical industry', the 'general machinery industry', the 'transport equipment industry' and the 'specialized machinery industry' grew by 67.4% yoy, 12.2% yoy, 9.7% yoy and 4.6% yoy respectively over the same period.

Among the regions, FDI in the western region rose by 18.2% yoy to reach 41.8 billion yuan in 1-3Q16. Meanwhile, FDI in the eastern region amounted to 536.0 billion yuan in 1-3Q16, up by 8.0% yoy.

The top ten countries/ regions in terms of FDI value jointly accounted for 94.4% (574.6 billion yuan) of China's total FDI in 1-3Q16. Among which, FDI from the US, Germany, the UK, Sweden and South Korea grew strongly by 67.1% yoy, 118.9% yoy, 95.8% yoy, 51.7% yoy and 28.3% yoy, respectively, during the period.

Exhibit 31 China's FDI, October 2015 to September 2016

	Amount (billion yuan)	yoy growth
FY15	781.4	6.4%
1-3Q16	609.0	4.2%
October 15	54.7	4.2%
November	64.9	1.9%
December	77.0	-5.8%
January 16	88.3	3.2%
February	53.6	1.8%
March	82.3	7.8%
April	62.6	6.0%
May	56.8	-1.0%
June	98.2	9.7%
July	49.8	-1.6%
August	57.3	5.7%
September	60.2	1.2%

Source: Ministry of Commerce, PRC

7. China's foreign exchange reserves decrease at a faster pace

After falling by US$ 7.4 billion in 2Q16, the foreign exchange reserves decreased by US$ 38.8 billion in 3Q16, and then fell at a faster pace, by US$ 45.7 billion, in October. As at the end of October 2016, the foreign exchange reserves amounted to US$ 3.12 trillion (see exhibit 32). We believe that the quicker drop in the foreign exchange reserves was mainly due to the acceleration in hot money outflows.

Looking ahead, we predict that China's foreign exchange reserves will fall further in coming future due to hot money outflows and increase in overseas investment. The recent depreciation of the Chinese yuan against the US dollar and the market expectations on the US interest rate hike in coming future will continue to encourage hot money outflows from China. Besides, Chinese enterprises have become more active in making overseas investment. In the first nine months of 2016, China's outbound direct investment increased markedly by 53.7% yoy to reach 882.8 billion yuan.

Exhibit 32 Foreign exchange reserves by quarter, 4Q15 to 3Q16

USD billion	Accumulation	End of the quarter
FY15	-512.7	
4Q15	-183.8	3,330.4
1Q16	-117.8	3,212.6
2Q16	-7.4	3,205.2
3Q16	-38.8	3,166.4

Source: State Administration of Foreign Exchange, PRC

B Highlights

1. Depreciation of Chinese yuan against the US dollar quickens

The daily fixing rate (also known as the central parity rate) of the Chinese yuan against the US dollar has depreciated in recent months (see exhibit 33).[17] The daily fixing rate of the Chinese yuan against the US dollar depreciated to 6.8796 on 18 November, compared to the recent peak of 6.6056 on 17 August. Meanwhile, the USD-CNY spot exchange rate has also weakened in past few months.[18] Particularly noteworthy is that the depreciation of the Chinese yuan against the US dollar has quickened since early November. On 18 November, the USD-CNY spot exchange rate came in at 6.8912, compared to 6.7591 on 4 November. So far this year, the Chinese yuan has depreciated by 5.8% against the US dollar (as of 18 November).

In our view, the main reason for the recent depreciation of the Chinese yuan against the US dollar was hot money outflows from China to the US driven by the expectations of a quicker rise in the US interest rate. It is noteworthy that Trump's proposal of fiscal stimulus will need more government borrowing and is highly inflationary, the US interest rate is expected to increase at a quicker pace under Trump's presidency.

The daily fixing rate of the Chinese yuan against the Euro has fluctuated at low levels in recent months (see exhibit 34). The daily fixing rate stayed between 7.3102 and 7.5379 throughout August to mid-November (as of 18 November). On 18 November, the daily fixing rate was 7.3102, implying that daily fixing rate of the Chinese yuan against the Euro has depreciated by 2.9% so far this year (as of 18 November).

According to the Bank for International Settlements, the real effective exchange rate (REER) of the yuan rebounded slightly from 120.77 in August to 121.16 in September, before edging down to 121.06 in October.[19] Overall, in the first ten months of 2016, the Chinese yuan depreciated in real terms against its trading partners by 7.1% (see exhibit 35).

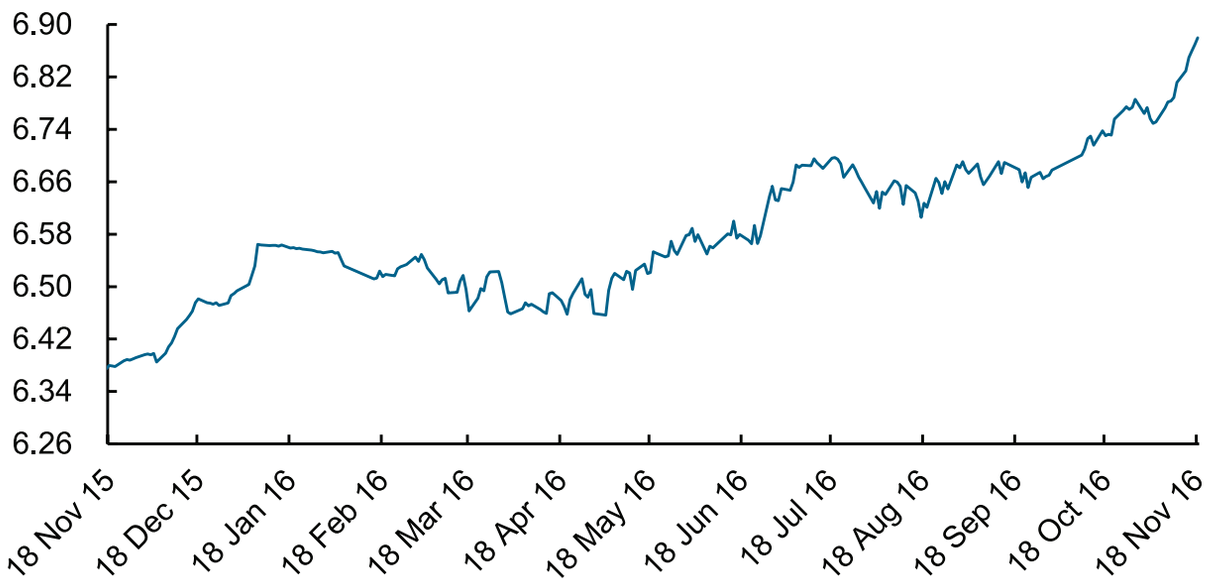
Looking ahead, we predict the exchange rate of the Chinese yuan against the US dollar to stay weak in coming months. Nevertheless, we do not expect the Chinese yuan to continue to depreciate against the US dollar in the long term, supported by the stable growth of the Chinese economy, massive trade surplus as well as the increasing demand for yuan-denominated assets. The Chinese yuan has been included in the IMF's Special Drawing Right (SDR) basket starting from 1 October 2016. The inclusion is likely to improve demand for yuan-denominated assets from central banks across the world.

17 According to the PBOC, the daily fixing rate (also known as the central parity rate) of the Chinese yuan against the US dollar is directly formed by market makers based on the closing rate of the previous day, the supply-demand conditions in the market and the movements of major international currencies.

18 The daily trading band of the Chinese yuan against the US dollar is ±2.0% around the daily fixing rate.

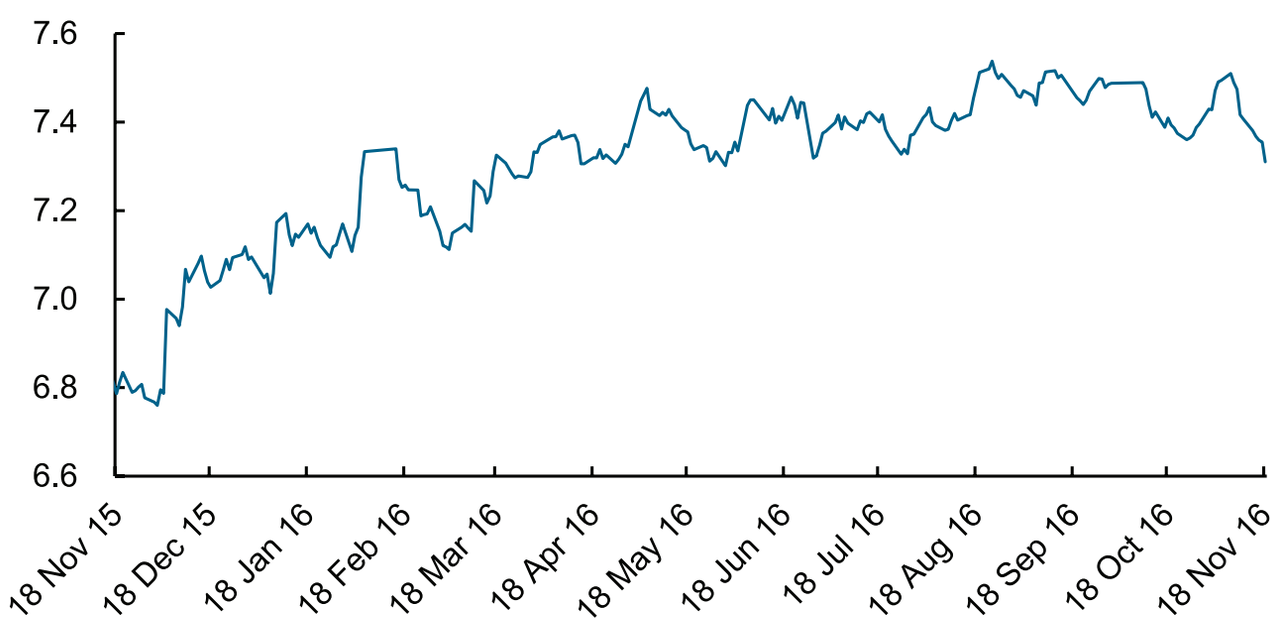
19 The Bank for International Settlements (BIS) calculates effective exchange rate (EER) indices for a total of 61 economies (including individual Eurozone countries and, separately, the Eurozone as an entity). Nominal EERs are calculated as geometric weighted averages of bilateral exchange rates. Real EERs are the same weighted averages of bilateral exchange rates adjusted by relative consumer prices. The weighting pattern is time-varying, and the most recent weights are based on trade in 2011-13.

Exhibit 33 USD-CNY daily fixing rate, November 2015 to November 2016



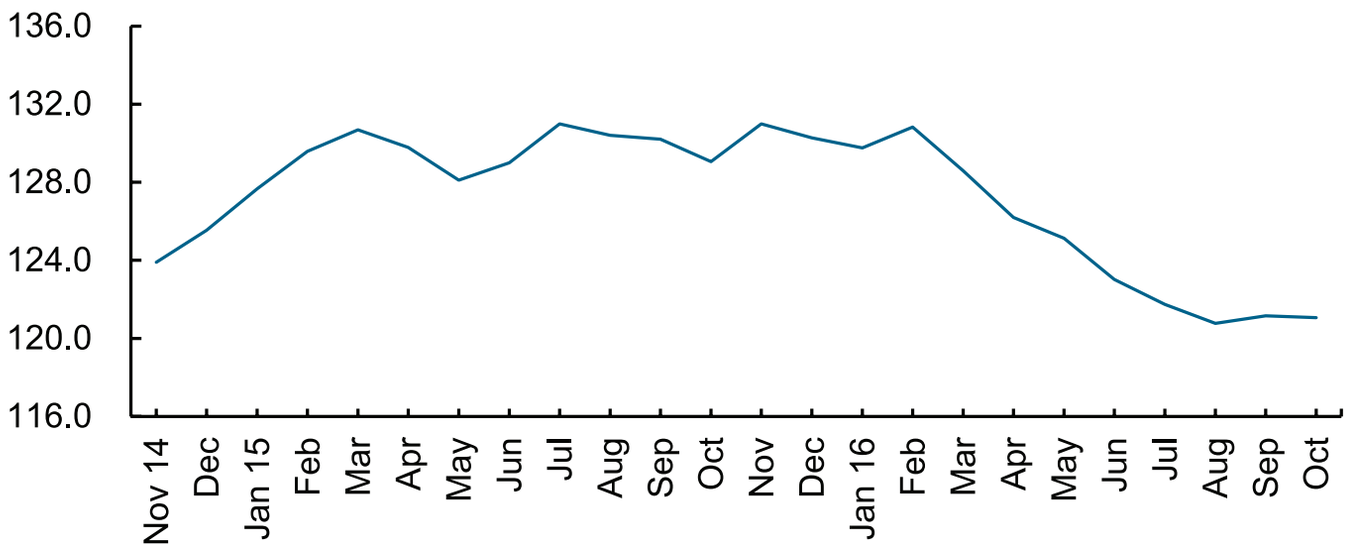
Source: State Administration of Foreign Exchange

Exhibit 34 EUR-CNY daily fixing rate, November 2015 to November 2016



Source: State Administration of Foreign Exchange

Exhibit 35 Real effective exchange rate of the Chinese yuan, November 2014 to October 2016



Source: Bank for International Settlements

2. Different responses to depreciation of Chinese yuan from exporters at Canton Fair

The 120th China Import and Export Fair (more widely known as the Canton Fair), was held in October in mid-October to early November.[20]

According to the media reports, in response to the depreciation of the Chinese yuan against the US dollar, some exporters at the fair lowered the prices of their products in US dollar terms.[21] However, some exporters still had to raise prices of their products, as they said the impact of the weakening in the Chinese yuan was more than offset by the increase in labour costs.[22]

3. Trump victory brings about uncertainties over G20 leaders' agreement on opposing trade protectionism

The G20 Leaders Summit was held on 4-5 September 2016 in Hangzhou in China.

During the meeting, the leaders from the G20 member countries reached a number of agreements on various aspects. Regarding trade, the G20 leaders agreed to oppose protectionism on trade and investment and to extend their commitments to standstill and rollback of protectionist measures till the end of 2018, according to the G20 Leaders' Communique published on 5 September.[23] We believe that such an announcement shows their determination to fight trade protectionism, which should be positive to the development of China's exports.

However, the Donald Trump victory in the US Presidential Election in early November brings about uncertainties over the fulfillment of the above promises: the stances and policy agenda of Trump are highly protectionist, which includes imposing prohibitive tariffs on imports from China.

4. China to take a lead role in Asia-Pacific trade liberalization

On 19 November, Chinese President Xi Jinping delivered a keynote speech at the Asia Pacific Economic Cooperation (APEC) CEO Summit, calling for trade and economic cooperation and urging regional leaders to advance trade deals. In his speech, Xi stated that the APEC should steadfastly promote the construction of the Free Trade Area of the Asia-Pacific (FTAAP), and that China would work for the early conclusion of the negotiations on the Regional Comprehensive Economic Partnership (RCEP).

The FTAAP, as a major instrument to further APEC's regional economic integration agenda, will be pursued as a comprehensive free trade agreement including all 21 APEC members, while the RCEP, backed by China, is a free trade agreement involving China, Japan, South Korea, Australia, New Zealand, India, and the 10 members of the Association of Southeast Asian Nations (ASEAN).

Xi's call for further trade cooperation is in contrast to Donald Trump's protectionist stance. Trump's victory in the US presidential election implies a change in the US trade policies. It is widely expected that a Trump administration will tear up the Trans-Pacific Partnership (TPP), and renegotiate or even withdraw from the North American Free Trade Agreement (NAFTA).

Looking ahead, we expect that China will take a lead role in Asia-Pacific trade liberalization in the coming future. Both the TPP and the RCEP were regarded as valid paths to the realization of the FTAAP. However, with the uncertainty over the TPP, the China-backed RCEP has now emerged as perhaps the only path to the FTAAP. China has been pushing the RCEP, which notably excludes the US, as an alternative to the TPP, which does not include China.

20 The China Import and Export Fair is China's largest and oldest trade exhibition.

21 http://www.scmp.com/news/china/economy/article/2039678/cheaper-yuan-brings-little-cheer-chinese-exporters-canton-fair

22 http://asia.nikkei.com/Business/Trends/Made-in-China-losing-edge-at-trade-fair?page=2

23 http://europa.eu/rapid/press-release_STATEMENT-16-2967_en.htm

C Outlook

1. US economic growth accelerates in 3Q16

The US real GDP advanced by an annual rate of 2.9% in 3Q16, an acceleration from the real annual growth of 1.4% in 2Q16 (see exhibit 36).

Indicators show positive signs for the US manufacturing sector. According to the Institute for Supply Management, the manufacturing Purchasing Managers' Index (PMI) rebounded from 49.4 in August to 51.5 in September and 51.9 in October, indicating a reacceleration in the growth of the manufacturing sector. Besides, industrial production gained 0.1% mom in September, recording positive month-on-month growth in three of the last four months (see exhibit 37). Meanwhile, after expanding by 0.2% mom in August, the new orders for manufactured durable goods fell by 0.3% mom in September on a seasonally adjusted basis.

The non-manufacturing index (NMI), compiled by the Institute for Supply Management, rose sharply from 51.4 in August to 57.1 in September, the highest level since November last year, before dropping to 54.8 in October. In fact, the index reading in October is the same as its average for the past 12 months, indicating that the non-manufacturing sector has still been on solid footing.

The retail sector has fared relatively well in recent months. The US retail sales gained 0.8% mom in October, recording positive month-on-month growth in six of the past seven months. However, the Reuters/University of Michigan Index of consumer sentiment fell from 91.2 in September to 87.2 in October, the lowest level since October last year, indicating that US consumers have become less optimistic (see exhibit 38).

The pace of job creation has decelerated in recent months. The non-farm payroll employment rose by 191,000 and 161,000 in September and October respectively. Meanwhile, the US unemployment rate edged down from 5.0% in September to 4.9% in October (see exhibit 39).

The result of the US Presidential Election was announced on 9 November. A Trump victory brings about uncertainties on the US economy. As many policy suggestions proposed by Trump are controversial, it is highly uncertain which of his proposed policies will be realized. Against this backdrop, business investment and consumption may slow, thereby exerting negative effect on the economy. However, we see some upside risks to the US economy in the short term, if fiscal stimulus measures such as tax cuts and increase in infrastructure spending can be carried out.

Exhibit 36 US national accounts, 2014 to 3Q16

Annual growth (%)	2014	2015	4Q15	1Q16	2Q16	3Q16
Real GDP	2.4	2.6	0.9	0.8	1.4	2.9

Source: US Department of Commerce

Exhibit 37 US industrial sector, April to September 2016

mom growth (%), seasonally adjusted	Apr 16	May	Jun	Jul	Aug	Sep
Industrial production	0.4	-0.2	0.5	0.5	-0.5	0.1
New orders for manufactured durable goods	3.2	-2.9	-4.3	3.6	0.2	-0.3

Source: US Federal Reserve, US Department of Commerce

Exhibit 38 US consumer market, May to October 2016

	May 16	Jun	Jul	Aug	Sep	Oct
Retail and food services sales *(mom growth %, seasonally adjusted)*	0.2	0.7	0.1	0.0	1.0	0.8
Reuters/University of Michigan index of consumer sentiment	94.7	93.5	90.0	89.8	91.2	87.2
CPI *(yoy growth %)*	1.0	1.0	0.8	1.1	1.5	-

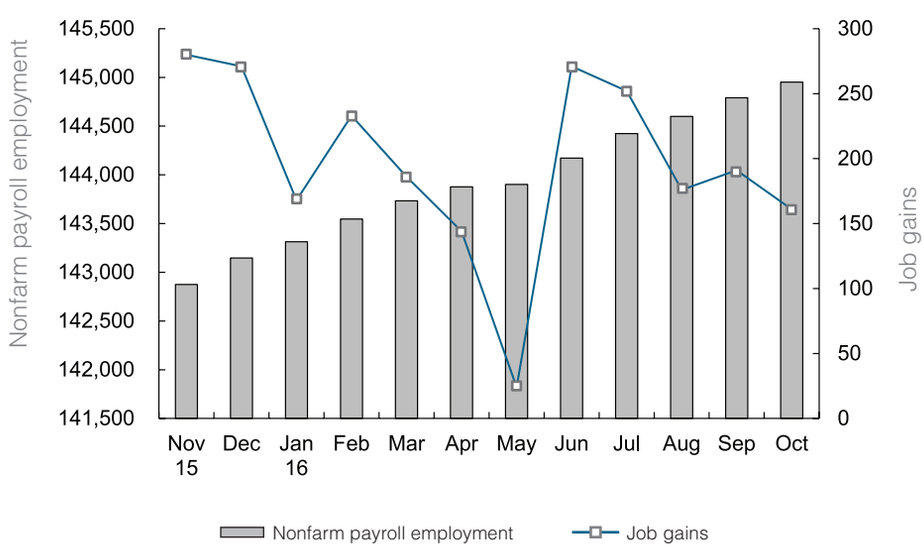
Source: US Department of Commerce, Reuters/University of Michigan Surveys of Consumers, US Department of Labor

Exhibit 39 US employment

	Unemployment rate (%)
2014	6.2
2015	5.3
Nov 15	5.0
Dec	5.0
Jan 16	4.9
Feb	4.9
Mar	5.0
Apr	5.0
May	4.7
Jun	4.9
Jul	4.9
Aug	4.9
Sep	5.0
Oct	4.9

Yearly figures: Annual average
Monthly figures: Seasonally adjusted

Nonfarm payroll employment, November 2015 to October 2016
In thousands, seasonally adjusted



Source: US Department of Labor

2. Eurozone economic growth stays stable in 3Q16

The Eurozone economic growth stayed stable in 3Q16.[24] The real GDP growth in the Eurozone came in at 0.3% qoq in 3Q16, the same as in 2Q16 (see exhibit 40).

Latest indicators point to an acceleration in economic activities in October. According to the global survey firm Markit Economics, the Eurozone services PMI went up to 52.8 in October from 52.2 in September, indicating that the services sector in the Eurozone has expanded at a faster pace recently. Meanwhile, the Eurozone manufacturing PMI rose from 51.7 in August

24 Lithuania has become the 19th member of the Eurozone as from 1 January 2015. Other member countries include Austria, Belgium, Cyprus, Estonia, Finland, France, Germany, Greece, Ireland, Italy, Latvia, Luxembourg, Malta, the Netherlands, Portugal, Slovakia, Slovenia and Spain.

to 52.6 in September and 53.5 in October, indicating a quicker growth of the manufacturing sector in the region.

On a seasonally adjusted basis, the retail trade volume in the Eurozone fell by 0.2% mom in September, posting negative month-on-month growth for two consecutive months (see exhibit 41).

The labour market conditions have shown no sign of improvement recently. The seasonally-adjusted unemployment rate stayed high at 10.0% throughout July to September (see exhibit 42). In contrast, the Eurozone's economic sentiment indicator (ESI) rose from 103.5 in August to 104.9 in September, and further to a ten-month high of 106.3 in October, indicating an improvement in economic sentiment (see exhibit 43).

Looking ahead, the growth of the Eurozone economy is expected to moderate in the coming year, as the uncertainties triggered by the Brexit vote result may slow economic activities. According to the latest projections by the IMF, the Eurozone's real GDP growth is forecast to fell from 2.0% in 2015 to 1.7% in 2016 and 1.5% in 2017.[25]

Exhibit 40 Eurozone's real GDP growth, 2014 to 3Q16

	2014	2015	4Q15	1Q16	2Q16	3Q16
Real GDP *(qoq growth %)*			0.5	0.5	0.3	0.3
Real GDP *(yoy growth %)*	0.9	2.0	2.0	1.7	1.6	1.6

* The figure in 2014 does not reflect Lithuania's membership of the Eurozone, which began on 1 January 2015.

Source: Eurostat

Exhibit 41 Eurozone consumer market, April to September 2016

	Apr 16	May	Jun	Jul	Aug	Sep
Volume of retail trade *(mom growth %, seasonally adjusted)*	0.2	0.4	0.1	0.3	-0.2	-0.2
Annual inflation (%)	-0.2	-0.1	0.1	0.2	0.2	0.4

Source: Eurostat

Exhibit 42 Eurozone labour market, April to September 2016

seasonally adjusted	Apr 16	May	Jun	Jul	Aug	Sep
Unemployment rate (%)	10.1	10.1	10.1	10.0	10.0	10.0

Source: Eurostat

25 IMF, World Economic Outlook, October 2016

Exhibit 43 Eurozone economic sentiment indicator, May to October 2016

seasonally adjusted	May 16	Jun	Jul	Aug	Sep	Oct
Economic sentiment indicator	104.6	104.4	104.5	103.5	104.9	106.3

Source: Eurostat

3. China's exports are expected to show negative year-on-year growth in 4Q16

In its World Economic Outlook released on 4 October this year, the IMF predicts that the world economic growth will decelerate from 3.2% in 2015 to 3.1% in 2016, before rising to 3.4% in 2017. It is noteworthy that the IMF sees a more subdued outlook for the advanced economies after the Brexit vote result announced on 24 June and the relatively weak growth of the US economy in 1H16.

Looking ahead, amid a slowing global economy, we expect China's exports to continue to show negative year-on-year growth in 4Q16. Challenges facing Chinese exporters include uncertainties fuelled by Trump's victory, increasing labour and environmental costs, intense competition in the international market and a rise in foreign trade protectionism. Nevertheless, the recent depreciation of the Chinese yuan against the US dollar may provide room for exporters to lower prices of their products in the US dollar terms.

Exhibit 44 Latest GDP growth forecasts by the IMF

yoy growth (%)	2015	2016 (Forecasts)	2017 (Forecasts)
World economy	3.2	3.1	3.4
Advanced economies	2.1	1.6	1.8
US	2.6	1.6	2.2
Eurozone	2.0	1.7	1.5
Japan	0.5	0.5	0.6
UK	2.2	1.8	1.1
Emerging market and developing economies	4.0	4.2	4.6
China	6.9	6.6	6.2
India *	7.6	7.6	7.6
Brazil	-3.8	-3.3	0.5
Russia	-3.7	-0.8	1.1

* Data and forecasts are presented on a fiscal year basis. India's fiscal year runs from 1 April to 31 March.

Source: IMF, World Economic Outlook, October 2016

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