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Liquidity Remains Steady

Last week saw June fiscal data where monthly public revenue rose +5.3% YoY and +11% vs May. The improvement was largely due to economic recovery following pandemic disruptions. While the company operating environments have improved, the real estate related income has dropped -39.4%, indicating the relative cool real estate market is still exerting pressure on the government's fiscal balances.

On policy front, Premier Li Keqiang highlighted the macro policy at the World Economic Forum Special Virtual Dialogue with Global Business Leaders on July 19th. He stressed the need for steady growth, while at the same time cautioned against excessive stimulus that overreach future potential for sake of high growth targets. For the macro policies, steady growth is still the main goal and the fundamental pillar to protect employment and social well-being. The Central government has been aware of the structural risks that overflooding liquidity creates on debt risk and excess capacity. The steady growth policy has been implementing for last month or so, we are therefore still in observation period on the policy. By holding back on overly aggressive fiscal or monetary stimulus, government is creating cushions for future policy responses.

The liquidity condition in China is generally steady now, but it'll be hard to have significant loosening from here. Last week's LPR was left unchanged, which is another reflection of the steady approach. Specific future policy guidance will depend on the month end Politburo meeting.

Compared to the low volumes of new home sales, the secondary housing market transactions saw high volume. This shows homebuyers' shift from new homes to existing homes given the uncertainty of home deliveries by stretched developers. This of course decreases investment activities related to new housing projects. CBRC and various local governments are actively pushing for timely delivery of various housing projects. But this will take

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some time to recover the new home sales, since people will wait until evidence of timely delivery of existing projects.

In the global market last week, US shares outperformed European shares. US and European markets usually are interconnected and have high correlations. The wedge between the two markets is the serious energy security issue faced by European nations. Market was watching closely the resumption of Russian natural gas delivery via the Nord Stream 1 pipeline. As of late last week, the supply has resumed to pre-maintenance levels. While the short-term uncertainty has dropped, the future stability of such Russian gas supply remains in question. Market had attached high hopes to Biden's Mid-East trip, but there were little signs of increased production at the end of his trip. On monetary policy front, ECB and BOJ held monetary policy meetings last week. BOJ insisted on loose monetary policy and didn't expect sustained inflation risk. ECB hiked 50 bps for the first time in 10 years. To counter potential disruptive price action against more indebted European nations, ECB also unveiled the Transmission Protection Instrument (TPI) for bond purchases. With Europe pressed hard by both rate hike and inflation, they have a greater recession risk than the US. US yield curve remains inverted as market revised lower future hike expectations. 2y yield came off to 2.98% while 10y yield is now at 2.75% due to recessionary fears. FED is now expected to hike by 75 bps in this week's meeting on July 26-27.

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