BNY MELLON
iFlow
MACRO MORNING BRIEFING

**February 29, 2024**

# China Sentiment On The Mend

China's capital markets endured extreme volatility at the beginning of this year. By early February, the Shanghai Composite was down nearly 10% from where it ended 2023, the selloff triggered by derivatives-related capitulation, and the CSI 1000, a popular index linked to so-called snowball derivatives, down as much 27% in 2024. The total outstanding balance of margin transactions on the Shanghai, Shenzhen and new Beijing (established in September 2021) stock exchanges offers some insight into domestic investors' sentiment. After peaking just shy of CNY 1600bn around the turn of the year, that balance went on to plunge roughly 14% before bottoming around CNY 1375bn prior to the Lunar New Year.

Investor sentiment has stabilised since China's markets reopened, in part supported by positive retail spending and travel data from the holiday period. Also playing a role has been a series of policy directives, including strengthened market supervision and a large 50bp reduction in 5y Loan Prime Rate. The Shanghai Composite has recovered most of its early-2024 losses and is now only marginally lower on the year. The CSI 1000 has recovered ground as well but is -12% year-to-date (as of Feb. 28). Improved sentiment is clearly reflected in the comeback in margin transactions (see chart below).

Interestingly, throughout the volatility that commenced in mid-January, foreign investor interest in China A-shares, as proxied by Stock Connect Northbound flows, was relatively stable. Moderate demand during the downtrend and accelerated demand as equities turned higher could be viewed as a tentative sign of the market bottoming.

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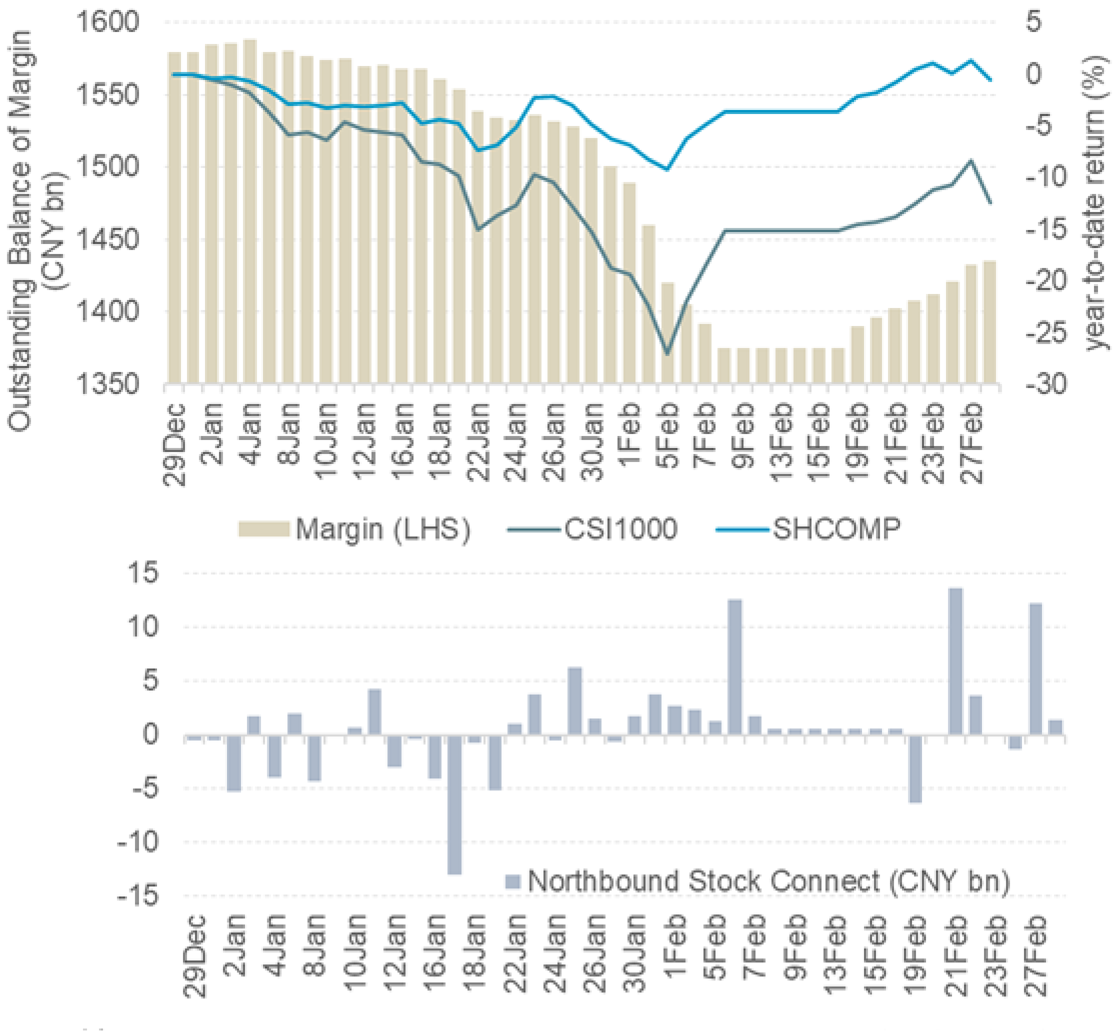
**Exhibit #1: China Equity Volatility & Balance Of Margin Transactions**




Source: BNY Mellon Markets, Bloomberg L.P.

Are China equities out of the woods? It's hard to answer with certainty, but we would like to think that the worst is behind, and that another episode of margin call-related capitulation seems unlikely. To be sure, the road to recovery for investor sentiment is a long one. Several challenges remain, especially with regard to a recovery in the real estate sector. Normalisation of the credit-transmission mechanism with banks speeding up lending growth and ongoing developed markets-China trade tensions warrant continued monitoring.

Next in focus are the dual sessions of the Chinese People's Political Consultative Conference (CPPCC) on March 3 and the National People's Congress (NPC) March 5, which will bring specific economic targets on GDP growth, the fiscal deficit, inflation, the local government bond quota and the unemployment rate. We will be paying special attention to the budget deficit, which was revised from -3.0% to -3.8% of GDP last October.

**Exhibit #2: China Official Economic Targets**

| | 2021 | 2022 | 2023 |
|---|---|---|---|
| GDP | > 6.0 | 5.5 | around 5% |
| CPI | 3.5 | 3 | 3 |
| Unemployment rate | 5.5 | < 5.5 | 5.5 |
| Budget deficit (% of GDP) | -3.2 | -2.8 | 3.0 (revised to 3.8% in Oct23) |
| Local govt bond quota (CNY bn) | 3650 | 3650 | 3800 (additional 1000bn of Special Treasury bonds in Q4 2023) |

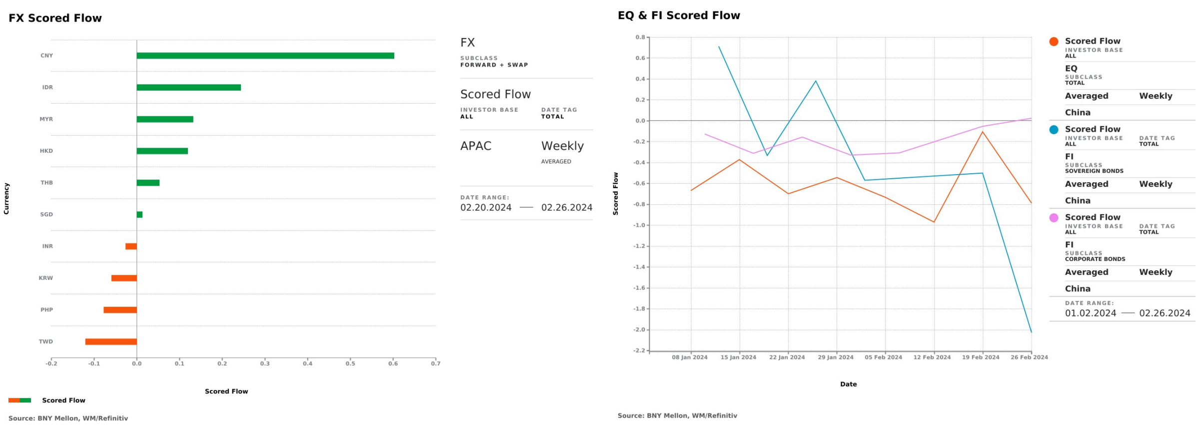
Source: BNY Mellon Markets, Bloomberg L.P.

APAC FX flows were moderate and mixed over the past week – except for large inflows into CNY: weekly average scored flows of 0.60 (as of Feb. 26). As a region, APAC FX continues to occupy the underheld and profitable quadrant of our scored holdings and profitability scatter chart; LatAm currencies are overheld and profitable, and CEE and EMEA currencies overheld and unprofitable. G10 is near neutral in positioning. Also noteworthy in APAC FX were inflows into THB and MYR after 12 and seven weeks of outflows, respectively.

APAC equity flows were mixed overall, but with large selling a feature in Singapore, India, and China. APAC sovereign bonds faced broad selling.

iFlow shows continued selling pressure on China equities and government bonds, but China corporate bond flows neutral (see below). This is at odds with the swift rebound in asset prices post-Lunar New Year. We're watching for a potential turnaround in iFlow sentiment.

### Exhibit #3: CNY Inflows, But China Equity & Government Bond Outflows




Source: BNY Mellon Markets, Bloomberg L.P.

**Please direct questions or comments to:** iFlow@BNYMellon.com

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