Economic and Financial Monthly (Jun, 2017)

Summary

In spite of the Fed's intention to announce plans to reduce its balance sheet, monetary policy is likely to remain accommodative; In Europe, the ECB is reluctant to tighten policy, while the Bank of England is facing increasing pressure to raise interest rates; Deleveraging measures in China has slowed M2 growth to below 10%; Hong Kong's economic momentum strengthens, while the Hang Seng is outpacing other major indices worldwide.

■ U.S.: Monetary policy to remain accommodative in spite of balance sheet reduction deliberations

The Fed has made public its intention to shrink its balance sheet. However, as economic growth remains tepid, monetary policy will continue to be accommodative. Moreover, the Fed will not be selling securities outright and will only reduce reinvestments. Also, it will take a lot of time to reduce the Fed's assets, as the size of the Fed's balance sheet will not return to a normal level until 2022, according to Fed Chair Yellen. Meanwhile, Yellen stressed the gradual pace of future rate hikes and hinted that interest rates may not have much room to move higher. Therefore, the overall interest rate environment in the U.S. remains fairly accommodative.

Europe: ECB reluctant to tighten policy

Although the Euro-zone's economy continues to improve and the unemployment rate keeps declining, the ECB for the time being is keeping its asset purchase program and negative interest rate policy unchanged. The ECB's President Draghi is apparently unwilling to tighten policy as long as inflationary pressure remains mild. On the contrary, as the Pound depreciates, the Bank of England may have to raise interest rates in the second half of this year. That said, as Brexit negotiations is likely to be rather difficult, the room for rate hikes will be somewhat limited.

China: M2 growth decelerates again

China's economic momentum continues to stabilize thanks to improvements in manufacturing, robust retail sales, and strengthening international trade. GDP growth in 2017 is likely to exceed the government's 6.5% target. In May and June, M2 growth dipped below 10% for the first time since records began as a result of deleveraging measures. The reduction in excess liquidity should help control asset prices and help direct funding to the real economy. Meanwhile, M2 above 9% should be strong enough to ensure nominal GDP to grow at a relatively rapid pace.

Hong Kong: Economic momentum strengthens markedly

Thanks to improving exports, rising private consumption, and low unemployment, Hong Kong's fundamentals have become noticeably stronger than in 2016. Relatively disappointing is the continual sluggishness in retail sales, which has bottomed but is not likely to stage a strong rebound any time soon. In the first half of 2017, thanks to RMB appreciation against the dollar, improving economic growth, and low interest rates, Hong Kong stocks outperformed its major counterparts worldwide

Tristan Zhuo