Market Insights

February 2023

Equity

MSCI China index rose by 12.25% in the month of January and continued the rally since late 2022, driven by the earlier and faster reopening process of China, the overall better-than-expected December macro data, investors' stronger expectation on China's growth outlook, more regulatory easing on Internet and more favorable external environment. China has been rapidly reaching its COVID herd immunity. Due to the faster-than-expected transition to herd immunity and higher-than-expected sequential growth in 4Q22, most investors see larger upside risks to their previous expectations on China's economic growth in 2023. Investors appear to be starting to build a positive consensus on China macro and financial market outlook. Chinese Vice Premier Liu He conveyed an unequivocal pro-business message at Davos, vowing that China will maintain focus on growth and stay on the path of supporting the private sector, deepening market-oriented reforms and opening up. Chinese financial technology giant Ant Group and 13 other platform companies "have basically completed business rectification" under the guidance and supervision of financial regulators, according to Guo Shuqing, Chairman of CBIRC. Looking forward, we maintain our long-term positive view on China equity market. In the coming weeks, we expect the market to consolidate after the sharp rally in the past 3 months, given more noises on geopolitical tensions and lack of further strong short-term catalysts. In terms of portfolio positioning, we are more bullish on the performance of China equities and more active in the investment process. We continue to focus on the long-term policy beneficiaries (eg. software localization and advanced manufacturing), short-term policy beneficiaries (property and property-related sectors) and reopening-related opportunities (eg. consumer, internet, financials and healthcare).

Market Performance

MSCI China index rose by 12.25% in the month of January and continued the rally since late 2022, driven by the earlier and faster reopening process of China, the overall better-than-expected December macro data, investors' stronger expectation on China's growth outlook, more regulatory easing on Internet and more favorable external environment. China has been rapidly reaching its COVID herd immunity, as the government estimates about 80% of the population has already been infected with COVID. Recent CDC data on infections, hospitalizations and deaths suggest the "exit wave" is coming to an end. China's Dec macro data generally came in above expectations, led by a significant rebound in retail sales (despite the sharp spike in COVID cases), along with moderate pickup in FAI growth and better-than-expect held up industrial production. Due to the faster-than-expected transition to herd immunity and higher-than-expected sequential growth in 4Q22, most investors see larger upside risks to their previous expectations on China's economic growth in 2023. Investors appear to be starting to build a positive consensus on China macro and financial market outlook.

Chinese Vice Premier Liu He conveyed an unequivocal pro-business message at Davos, vowing that China will maintain focus on growth and stay on the path of supporting the private sector, deepening market-oriented reforms and opening up. Chinese financial technology giant Ant Group and 13 other platform companies "have basically completed business rectification" under the guidance and supervision of financial regulators, according to Guo Shuqing, Chairman of CBIRC. Also, Didi apps were allowed to return to Apple and Android app stores. The positive regulatory progress and continuous supportive statements from Chinese government on the private economy further increased investors' risk appetite on China equities. Besides, RMB continued to appreciate against USD in January on China's bullish economic recovery outlook and the market's lower expectation on the Fed rate hikes. The north-bound net buy value under the stock connect program in January has already exceeded 2022 annual level, and the inflows may continue in the coming months.

Equity

Greater China Indices	Jan Close	Monthly % Change	YTD %	52 Week Low	52 Week High
CSI 300	4156.86	7.37	7.37	3495.95	4672.65
MSCI China	72.37	12.25	12.25	47.43	85.54
HSI	21842.33	10.42	10.42	14597.31	25050.59
HSCEI	7424.92	10.74	10.74	4919.03	8822.80
Global Indices					
S&P 500	4076.60	6.18	6.18	3491.58	4637.30
Dow Jones Industrial Average	34086.04	2.83	2.83	28660.94	35824.28
Nasdaq Composite	11584.55	10.68	10.68	10088.83	14646.90
FTSE 100	7771.70	4.29	4.29	6707.62	7906.58
DAX 30	15128.27	8.65	8.65	11862.84	15614.47
Nikkei 225	27327.11	4.72	4.72	24681.74	29222.77

Economic Data

China’s manufacturing PMI rose to 50.1 in January from 47.0 in December, back to the expansionary territory as disruptions from reopening rapidly dissipated. The new order sub-index jumped to 50.9 in January from 43.9 in December, and the output sub-index rose to 49.8 in January from 44.6 in December, on ongoing recovery in demand and resumption of production. The non-manufacturing PMI jumped to 54.4 in January from 41.6 in December, showing a sharp acceleration in both construction and services sectors. The services sub-index rebounded sharply to 54.0 in January from 39.4 in December, and the construction sub-index rose to 56.4 in January from 54.4 in December.

Future Outlook

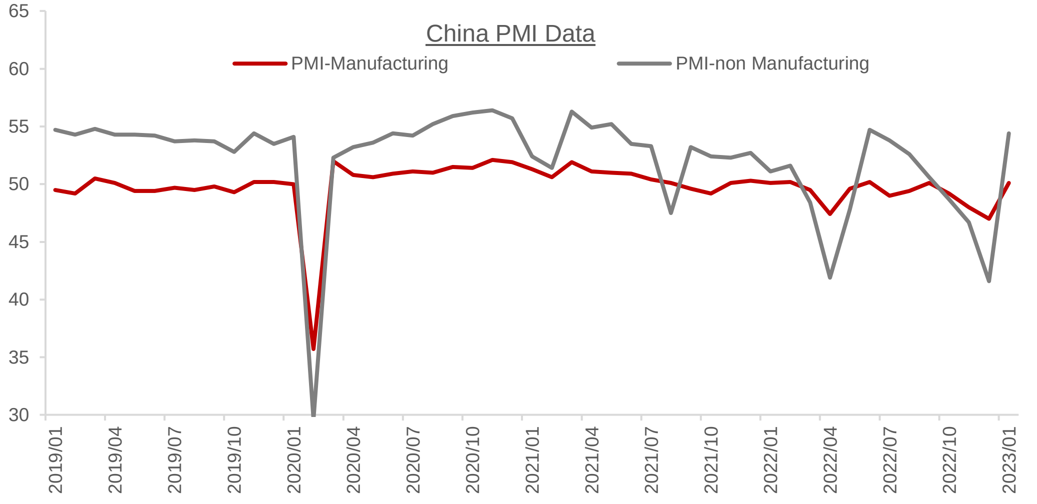
Looking forward, we maintain our long-term positive view on China equity market. With the earlier and faster reopening process together with the continued countercyclical easing policies, China’s economic growth is likely to exceed the market’s previous expectations. During the first Chinese New Year holiday, most high-frequency data showed that the domestic economic activities were gradually getting rid of the influence from COVID and the pent-up travel and consumption demand rebounded significantly. In the coming weeks, we expect the market to consolidate after the sharp rally in the past 3 months, given more noises on geopolitical tensions and lack of further strong short-term catalysts.

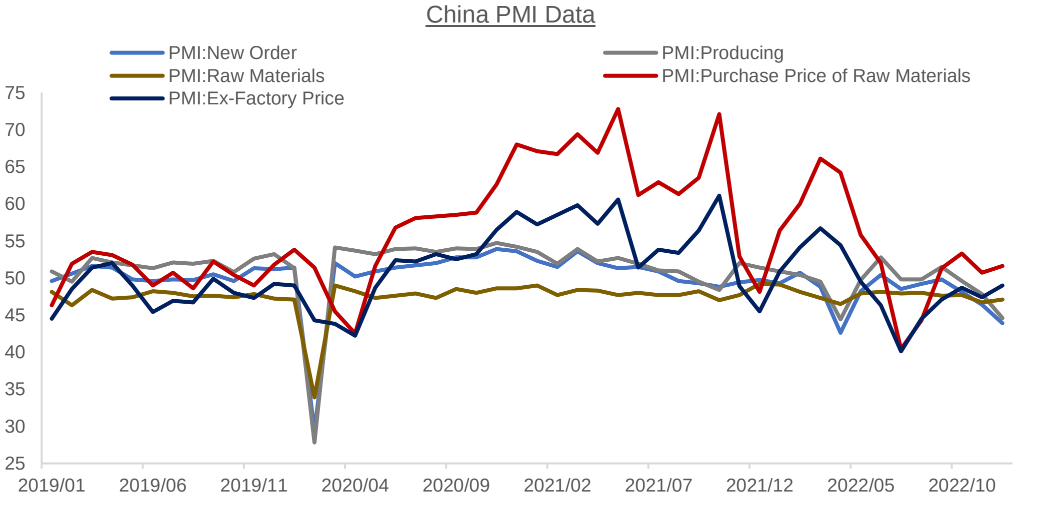
In terms of portfolio positioning, we are more bullish on the performance of China equities and more active in the investment process. In terms of style, large-caps and growth stocks may outperform value stocks during the process of investors adding China positions. We continue to focus on the long-term policy beneficiaries (eg. software localization and advanced manufacturing), short-term policy beneficiaries (property and property-related sectors) and reopening-related opportunities (eg. consumer, Internet, financials and healthcare).

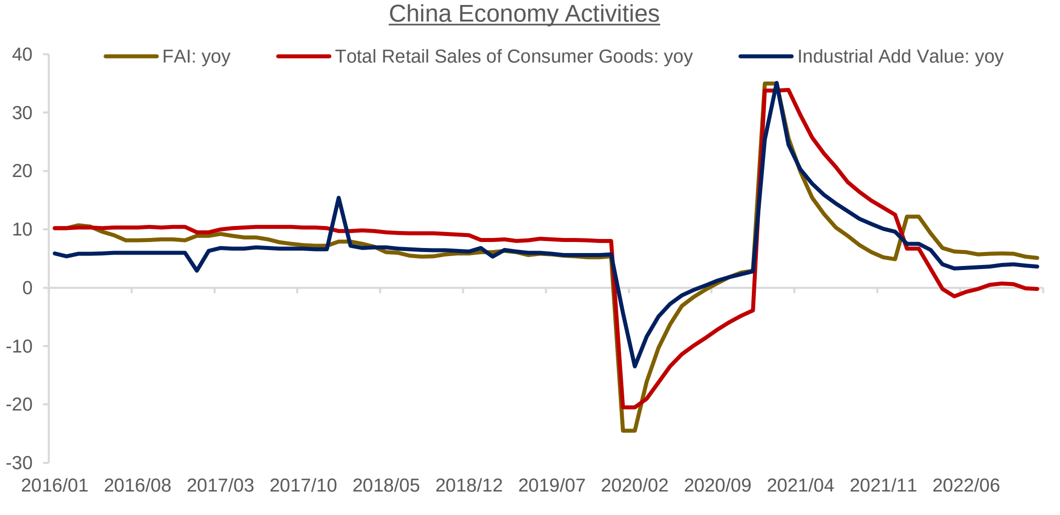
Risk

Inflationary pressure passed to downstream sectors; foreign monetary policies being tightened due to higher-than-expected inflation; Sino-US relationship worsens than expectation. Russia-Ukraine War worsens than expectation; China's economy recovers less than expected after the directional adjustment of policy.

Data Source: unless otherwise specified, the data in this report extracted from Bloomberg and Winds, as of 31 January 2023. Data shown is for informational and reference purposes only, historical data does not represent future trend of development.







Data Source: unless otherwise specified, the data in this report extracted from Bloomberg and Winds, as of 31 January 2023. Data shown is for informational and reference purposes only, historical data does not represent future trend of development.

Fixed Income

Global markets had a strong opening in 2023. As China's pandemic passed its peak, economic activities notably recovered. With U.S. inflation subsiding, the rate-hike cycle came near its end. In the Eurozone, recession fears were mitigated by recent data. Against this backdrop, market sentiment visibly improved. Market pricing of the peak of the policy rate declined, and market expectations of the how long the Fed would maintain the policy rate is also shorter than the official guidance. Corporate bonds enjoyed strong performance into the year, thanks to the decline of U.S. Treasury yields and the tightening of credit spreads. For China's USD bonds, spreads continued to tighten owing to lack of supply and rebound in asset prices. The Federal Reserve increased its policy rate by in the February FOMC meeting, as expected. The emerging market also has positive prospects of recovery as the dollar index falls and China's economy rebounds. Meanwhile, we need to heed for the short-term and long-term market impact of risk events such as Japan's monetary policy change, deterioration in China-U.S. relations, U.S. debt limits, etc. High frequency data during the Chinese New Year shows a stronger-than-expected economic recovery after the pandemic has passed its peak. As U.S. economic data cooled down, Powell's press conference after the February FOMC meeting was seen as more dovish than prior expectations.

Market Performance

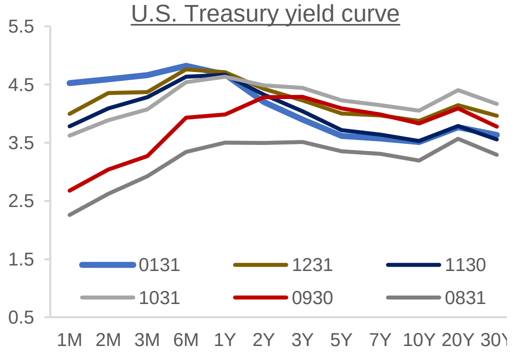
Global markets had a strong opening in 2023. As China's pandemic passed its peak, economic activities notably recovered. With U.S. inflation subsiding, the rate-hike cycle came near its end. In the Eurozone, recession fears were mitigated by recent data. Against this backdrop, market sentiment visibly improved. Market pricing of the peak of the policy rate declined, and market expectations of the how long the Fed would maintain the policy rate is also shorter than the official guidance. U.S. Treasury yields declined in the first half of the month, and moved sideways in the second half, with the 2-year and 10-year yield inversion going deeper. Asset classes that relatively underperformed in 2022 tended to outperform in the first month of 2023, with gold leading in performance.

United States	Last Price %	1M chg bp	YTD chg bps	52W low%	52W high%
2Y	4.20	-22	-22	1.13	4.80
5Y	3.62	-39	-39	1.52	4.50
7Y	3.57	-40	-40	1.62	4.44
10Y	3.51	-37	-37	1.67	4.34
30Y	3.63	-33	-33	2.06	4.42

China	Last Price %	1M chg bp	YTD chg bps	52W low%	52W high%
3Y	2.51	9	9	2.14	2.55
5Y	2.70	7	7	2.36	2.77
7Y	2.86	4	4	2.58	2.91
10Y	2.90	6	6	2.61	2.96
30Y	3.28	8	8	3.08	3.42

Japan	Last Price %	1M chg bp	YTD chg bps	52W low%	52W high%
2Y	(0.02)	-6	-6	-0.11	0.07
5Y	0.19	-4	-4	-0.04	0.34
7Y	0.41	-4	-4	-0.02	0.58
10Y	0.50	7	7	0.13	0.58
30Y	1.60	-1	-1	0.78	1.72

Germany	Last Price %	1M chg bp	YTD chg bps	52W low%	52W high%
2Y	2.65	-11	-11	-0.79	2.77
5Y	2.31	-27	-27	-0.42	2.58
7Y	2.27	-31	-31	-0.33	2.57
10Y	2.29	-29	-29	-0.10	2.57
30Y	2.22	-32	-32	0.10	2.55

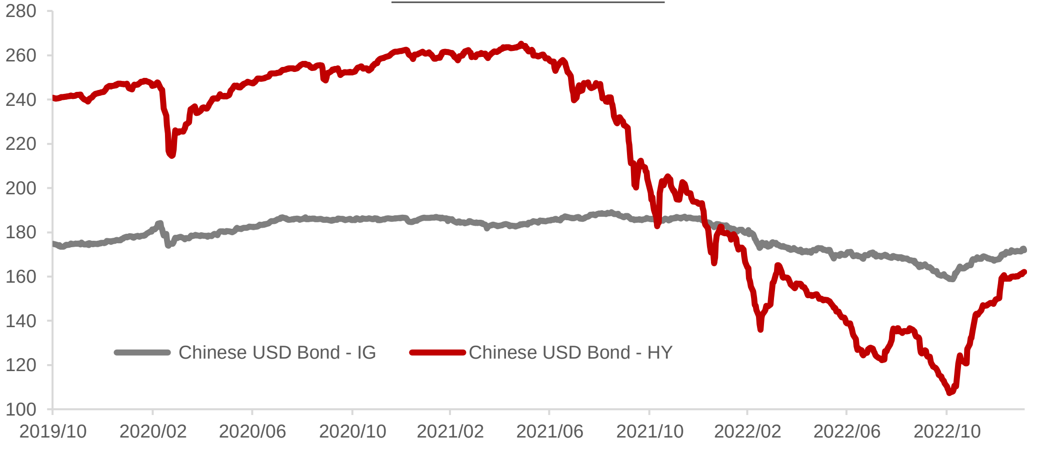


Data Source: unless otherwise specified, the data in this report extracted from Bloomberg and Winds, as of 31 January 2023. Data shown is for informational and reference purposes only, historical data does not represent future trend of development.

Corporate bonds enjoyed strong performance into the year, thanks to the decline of U.S. Treasury yields and the tightening of credit spreads. Strong buying interests well digested the record-breaking supply of new bond issuance in the U.S. in January, with the emerging markets also attracting large inflows. For China's USD bonds, spreads continued to tighten owing to lack of supply and rebound in asset prices. Higher quality issuers saw yields of their short-duration bonds fall below 5%. LGFV names with weak credit profiles underperformed as local governments face fiscal pressure. For high quality property developers, their USD bonds climbed higher as various policy support measures came into play. As a whole, in January China's investment-grade bonds climbed by 2.4%, and high-yield bonds went higher by 12%.

CDX Index	Current Value	1M chg bp	YTD chg bps	52W low%	52W high%
IG CDX	71	(11)	(11)	60	114
HY CDX	430	(54)	(54)	338	640
EM CDX	222	(17)	71	206	395
Bond index					
ICE Asian Dollar Corporate	430	3.2%	3.2%	384	463
ICE China Issuers Dollar IG Corporate	201	2.4%	2.4%	185	215
ICE China Issuers Dollar HY Corporate	216	12.0%	12.0%	115	262
ICE US Corporate	3104	3.9%	3.9%	2809	3433
ICE US High Yield	1456	3.9%	3.9%	1345	1546
ICE Emerging Markets Corporate	413	3.1%	3.1%	373	461
Bloomberg Global-Aggregate	461	3.3%	3.3%	416	524
Bloomberg Global-Aggregate 1-3 Year	170	1.8%	1.8%	159	181

Chinese USD Bond Index



Economic Data

U.S. fourth quarter GDP increased by 2.9%, overshooting expectations. December unemployment dropped to 3.5%, and inflation continued to subside as labour cost slowed down in the fourth quarter. High frequency data such as PMI and housing were still weak, leading to disagreement among market participants on whether the economy could manage a soft landing. In the Eurozone, as the fourth quarter GDP expanded, the region could potentially avoid a recession this year.

In China, the end of the first pandemic wave came sooner than expected, as consumption and traveling recovered significantly during the Chinese New Year and most economic indicators beat estimates.

Outlook

The Federal Reserve increased its policy rate by 25bp in the February FOMC meeting, as expected. The market's interpretation of the Fed's speech was dovish, and market pricing of policy turnaround is notably earlier than the official guidance. Therefore, it is worth noting whether future Fed officials' hawkish stance will exhibit subtle changes, which could offer crucial indication on whether asset prices are able to continue the year-to-date climb. Though inflation is almost confirmed to have peaked in the short run, it remains uncertain in the medium term whether price levels would fall back to the Fed's target range, or potentially creep up again as demand in China recovers. U.S. high frequency data exhibits significant divergence but overall shows economic momentum abating. That being said, U.S. economy still possesses resilience and recession is not expected to hit in the short run. Moreover, considering the response lag of monetary policy, the extent of the Fed's rate decreases could be smaller than market expectation. As for interest rates, in the medium term as the rate-hike cycle came to an end, we expect the 2-year U.S. Treasury yield to fluctuate downwards, and the 10-year rate to trade within the 3.3% to 3.6% range, with the shape of the yield curve gradually normalizing. As the energy crisis is mitigated and the low base effects since the second quarter of last year, Europe's economy could show signs of recovery. The emerging market also has positive prospects of recovery as the dollar index falls and China's economy rebounds. Meanwhile, we need to heed for the short-term and long-term market impact of risk events such as Japan's monetary policy change, deterioration in China-U.S. relations, U.S. debt limits, etc.

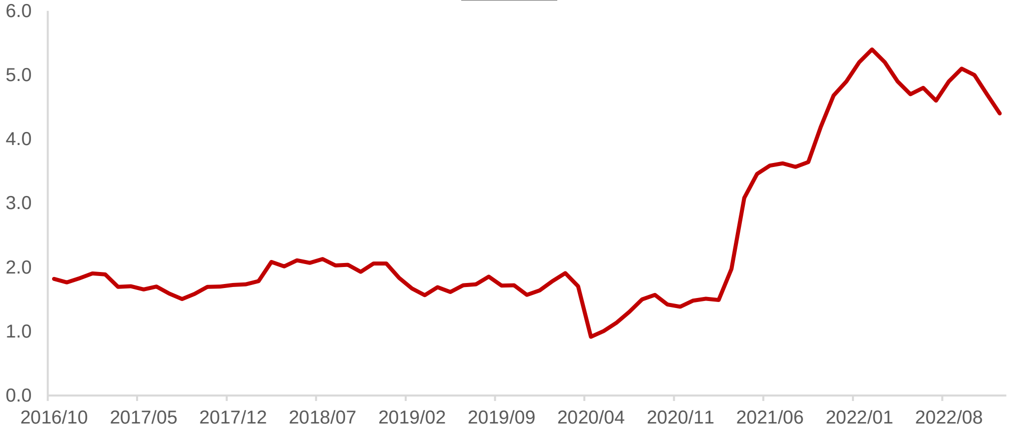
For corporate bonds, investment-grade bonds generally tightened by 10-20bps across sectors since the start of the year. After the new round of good performance, global credit spreads have reached a relatively expensive level compared to the valuations during start of the Russo-Ukrainian War last year. Overall, the spillover effects of China's recovery and the divergence of economic conditions between U.S. and Europe could encourage market sentiment, leading to a better-than-anticipated outperformance of risk assets since the start of the year. From the perspective of spread valuation, it remains unlikely for overall credit spreads to continue tighten further drastically, while market corrections could also occur in stages. We are closely monitoring the risk of an overbought market, and watch for opportunities to increase positions during subsequent corrections. In China's USD bond market, overall spread in the investment-grade space is at the lowest level over the last year. On the one hand, expectations of the economic outlook have reached higher as China shifts its pandemic policy. On the other hand, yields continued to be squeezed down by the lack of new bond supply and sustained inflows. In the short run, technical factors could still offer support to the market, while the recovery of consumption remains to be seen, and the risk in the LGFV sector is also worth monitoring this year. In the real estate sector, sales still remain sluggish, although housing price expectations have improved. Given firm policy support to the sector, property bond prices could enter stage of stabilization after substantial rebounds.

High frequency data during the Chinese New Year shows a stronger-than-expected economic recovery after the pandemic has passed its peak. With the January PMI also going back to expansionary territory, economic fundamentals for bonds are not favourable. As markets have accumulated high expectations of economic recovery, positions were light for medium-to-long tenors of financial bonds, with government bond futures trading in heavy backwardation before the Chinese New Year. Therefore after the holiday, as the central bank continues open market injection and liquidity remains abundant, the backwardation of government bond futures was substantially alleviated, leading to short squeeze and cash bond yields' falling. Meanwhile, yields of NCDs with tenors longer than six months continue to climb, supply of government bonds remains at high levels, and economic fundamentals are strongly liable for rebounds in the short term. Against such backdrop, bond yields are not likely to decline significantly. As impact from technical factors wane off, medium and long-term yields are still more likely to go up than down.

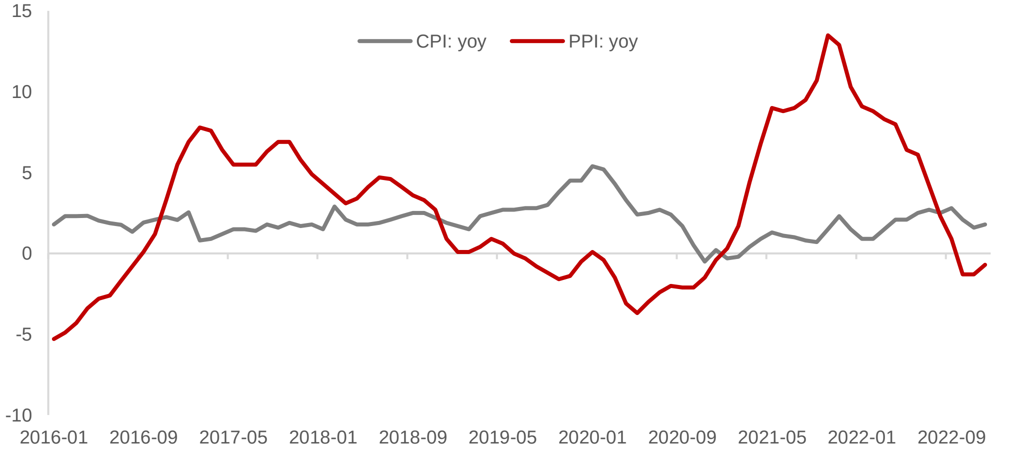
Data Source: unless otherwise specified, the data in this report extracted from Bloomberg and Winds, as of 31 January 2023.
Data shown is for informational and reference purposes only, historical data does not represent future trend of development.

As U.S. economic data cooled down, Powell's press conference after the February FOMC meeting was seen as more dovish than prior expectations, and the dollar index fell further below 101. The yuan is poised to remain strong, owing to factors such as China's economic recovery, the weakening dollar index, and increase in corporate interests for foreign exchange settlement. The extent and longevity of the dollar's weakening was greater than expectation: since the peak in November 2022, there have been almost no sizable rebounds. Short positions of USDCNH are not crowded. If the dollar rebounds, there would remain strong buying interests of the yuan against the dollar. As for technical levels, the central bank buys the dollar at 6.7, mitigating the speed of the yuan's appreciation. On the one hand, failure to sustain at this level would send the USDCNH down to 6.6. On the other hand, pressure from short-sellers loom over 6.75.

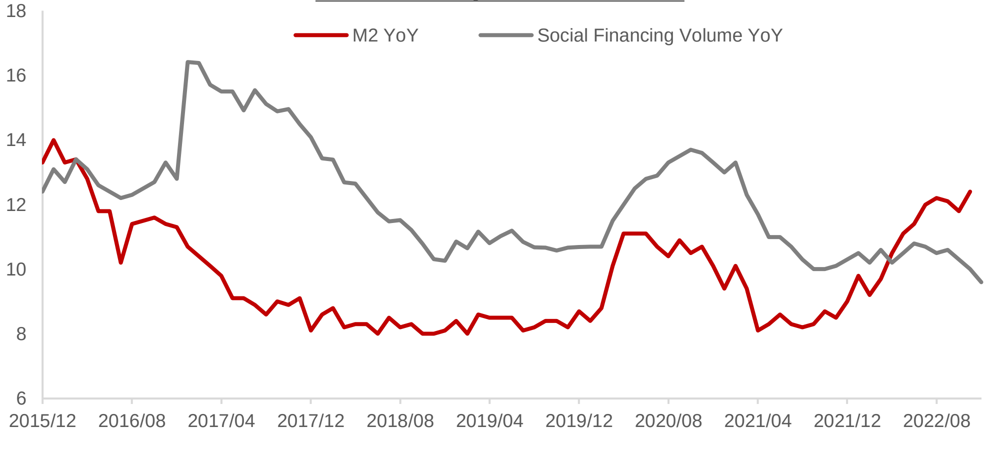
US PCE



China Inflation Indicators



China Monetary Volume Indicators



Data Source: unless otherwise specified, the data in this report extracted from Bloomberg and Winds, as of 31 January 2023. Data shown is for informational and reference purposes only, historical data does not represent future trend of development.

华夏基金(香港)
ChinaAMC (HK)

37/F, Bank of China Tower, 1 Garden Road, Hong Kong

www.chinaamc.com.hk

China Asset Management (Hong Kong) Limited

Phone: (852) 3406 8688

Fax: (852) 3406 8500

Product inquiry and client service

Email: hkservice@chinaamc.com

Phone: (852) 3406 8686

Follow us: ChinaAMC (HK)

WeChat LinkedIn Facebook