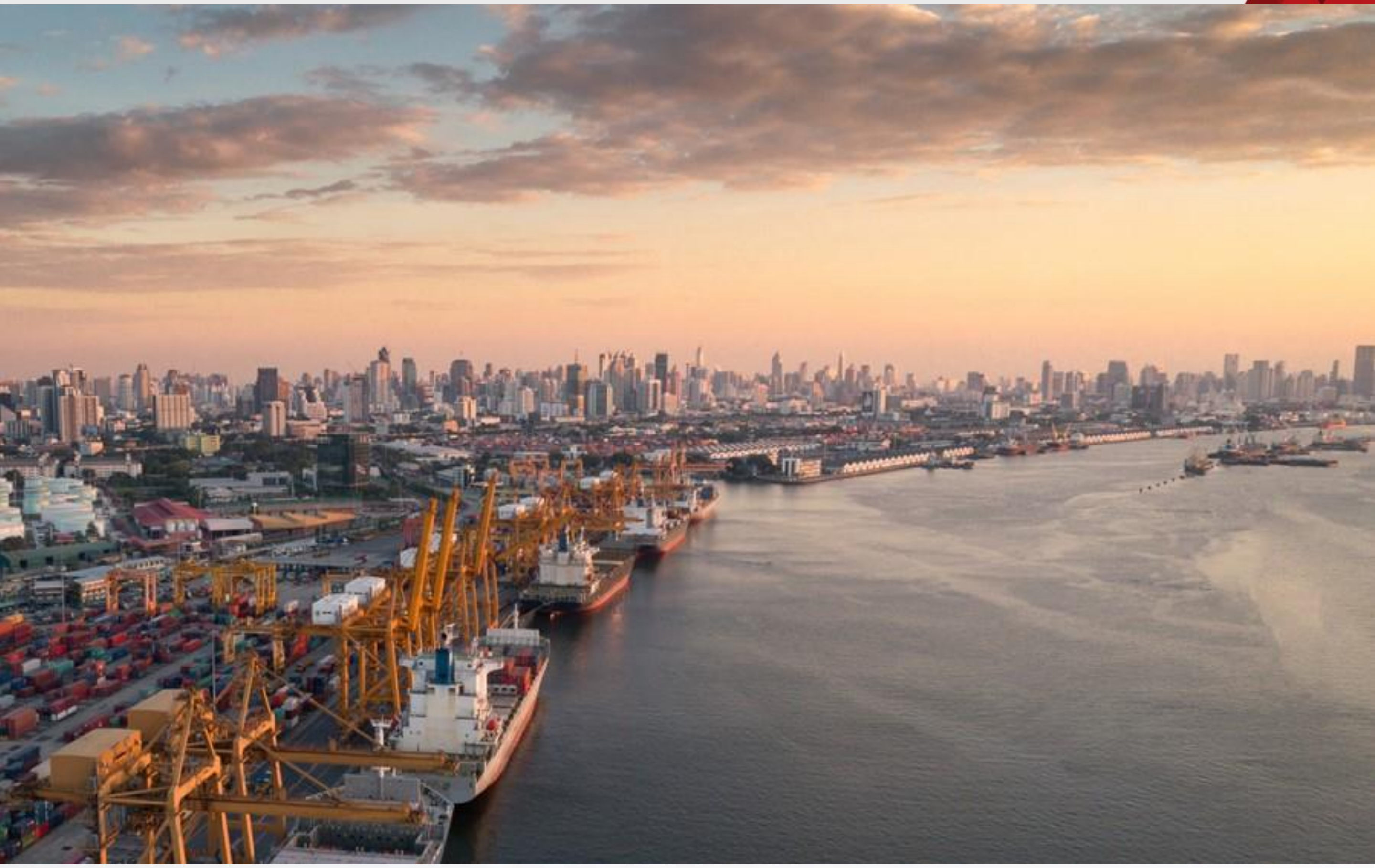
ChinaAMC(HK)



MARKET INSIGHTS

Position for recovery with differentiated alpha

May 2023

The MSCI China index fell 5.2% in April, mainly due to tensions with the US and investor concerns about the sustainability of China's economic recovery. China's manufacturing PMI fell to 49.2 in April from 51.9 in March, mainly due to weak demand and March's high base. The tourism sector recovered strongly over the May Day holiday, with domestic tourist arrivals and tourism revenues both exceeding 2019 levels. Yellen's upcoming visit to China may further confirm the trend of easing geopolitical risks. The US Federal Reserve raised interest rates by 25 basis points and hinted at a pause in the rate hike cycle, which could ease the outflow pressure on Chinese stock markets.

Market Performance

MSCI China index dropped by 5.20% in the month of April, due to the US-China tensions and investors' skepticism over the sustainability of China's economic recovery. Bloomberg reported that US President Biden is about to sign the Executive Order to restrict selected US direct investment in certain high-tech fields in China, which actually is a continuation and moderated version of last year's and Feb 23 debate, while cause significantly negative reaction in China equity market. China's 1Q GDP and other macro data point to a very strong growth recovery in China, led mainly by consumption and services sectors, thanks to the frontloading of reopening impulse and policy support. However, investors have not reached a consensus on the sustainability and strength of China's economic recovery, especially given the softened high-frequency economic data in April.

President Xi chaired the April Politburo meeting and discussed economic policies for the next few months. April's meeting statement maintained the "pro-growth" policy stance, and policymakers vowed to accelerate "building a modern industrial system", step up support for new-energy vehicles and artificial intelligence and enhance China's "self-reliance" in science and technology. Meanwhile, the statement acknowledged that China's 1Q data were better than expected but concluded "demand remained insufficient" and "promoting high-quality growth remained challenging". Besides, policymakers put an incrementally more positive spin on regulating platform companies. Overall, the Politburo meeting offered a balanced and measured tone on the economy, maintaining accommodative economic policy and pro-business stance.

Greater China Indices	Apr Close	Monthly % Change	YTD %	52 Week Low	52 Week High
CSI 300	4029.09	-0.54	4.07	3495.95	4530.33
MSCI China	64.35	-5.20	-0.19	47.43	77.02
HSI	19894.57	-2.48	0.57	14597.31	22700.85
HSCEI	6702.15	-3.83	-0.04	4919.03	7918.12
Global Indices					
S&P 500	4169.48	1.46	8.59	3491.58	4325.28
Dow Jones Industrial Averag	34098.16	2.48	2.87	28660.94	34712.28
Nasdaq Composite	12226.58	0.04	16.82	10088.83	13181.09
FTSE 100	7870.57	3.13	5.62	6707.62	8047.06
DAX 30	15922.38	1.88	14.36	11862.84	16011.56
Nikkei 225	28856.44	2.91	10.58	25520.23	29278.80

Economic Data

China's manufacturing PMI fell to 49.2 in Apr from 51.9 in Mar, mainly due to the insufficient demand and the high base in Mar. The new order sub-index decreased to 48.8 in Apr from 53.6 in Mar, and the output sub-index fell to 50.2 in Apr from 54.6 in Mar. The non-manufacturing PMI moderated to 56.4 in Apr from 58.2 in Mar, showing ongoing recovery in both the construction and services sectors but at a slower pace. The construction sub-index fell to 63.9 in Apr from 65.6 in Mar, as the growth momentum in infrastructure-related construction remained strong in Apr on the launch of major projects. The services sub-index fell to 55.1 in Apr from 56.9 in Mar, led by strong readings in travel and consumption-related sectors including railway transport, air transport, accommodation, cultural, sports and entertainment.

Equity

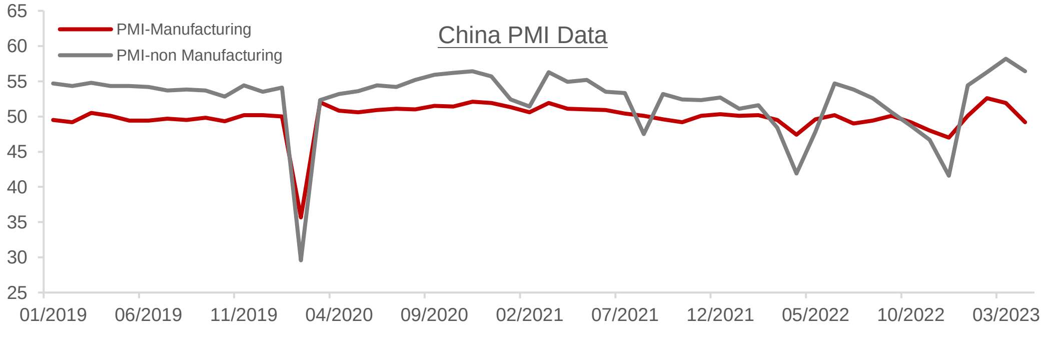
Outlook

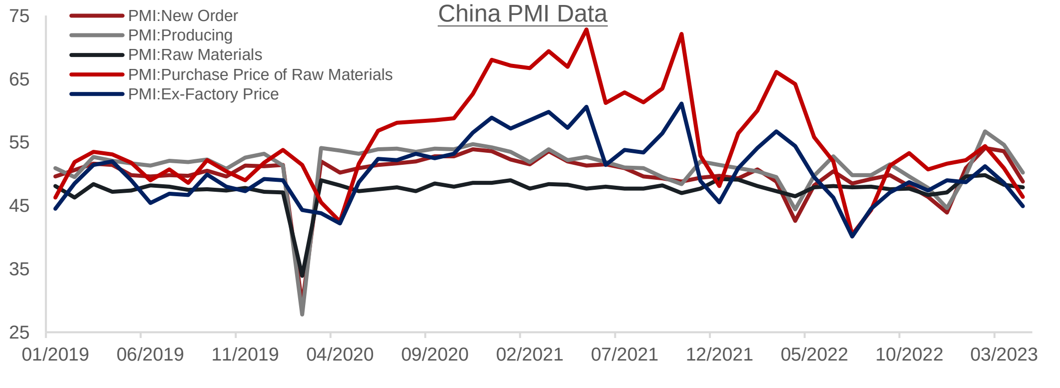
Looking forward, we maintain our long-term positive view on China equity market. China saw strong tourism recovery during the Labor Day holiday although the manufacturing PMI fell into contraction territory in April and services PMI moderated after a fast recovery in February and March, with domestic visitors and tourism revenue both exceeding 2019 levels. The overall geopolitical risk is showing a moderate trend and recent speeches by Yellen and Sullivan suggest Biden Administration is adopting a less confrontational approach, likely to minimize economic risk in an election year. Yellen's upcoming visit to China could further cement such a de-escalation. The FOMC hiked rates by 25bps and hinted at a pause in the hiking cycle, which may alleviate the outflow pressure faced by China equity market.

In terms of portfolio positioning, we will continue to seek a balance between value and growth. 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). Also, we will prudently pay attention to some thematic investment opportunities, including the ChatGPT/AI and SOE re-rating.

Risk

Expansion of risk events in the financial systems of European and American countries; 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.





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In April, global market cautiously improved due to easing US banking pressure. Risk aversion returned at month-end as US debt ceiling approached and JP Morgan Chase acquired First Total Bank after the FDIC stepped in. Investors became worried about macro risks, especially in small and medium-sized US banks. Though headline CPI fell, core CPI rose, indicating sustained pressure on sticky inflation, which is the Fed's main concern. China's economic recovery momentum has slowed. It's important to pay attention to the starting point of interest rate cuts rather than the end point of interest rate hikes, which was essentially determined by the Federal Reserve at the May FOMC meeting. We still expect the Fed to cut interest rates once or twice in Q4, faster and more extensively than initially predicted earlier this year.

Market Performance

Global markets cautiously recovered in April. In the first half of the month, the Federal Reserve and multiple market data showed that the overall pressure on the US banking system continued to ease, and market sentiment continued to recover with the expectation that rate hikes would peak. However, at the end of the month, as the US debt ceiling approached and First Republic Bank was taken over by the FDIC and sold to JPMorgan Chase, investors' concerns about macro risks, especially for small and medium-sized banks in the United States, heated up again, and risk aversion returned. Throughout the month, major asset classes were mixed in performance, US bond rates fluctuated, and most risk assets rose and then fell.

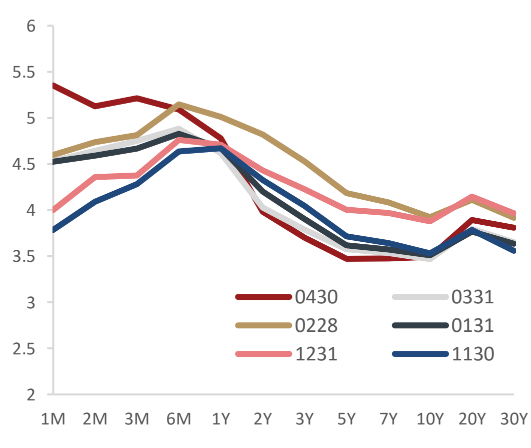
United States	Last Price %	1M chg bp	YTD chg bps	52W low%	52W high%
2Y	4.01	-2	-42	2.44	5.08
5Y	3.48	-9	-52	2.58	4.50
7Y	3.46	-7	-51	2.56	4.44
10Y	3.42	-5	-45	2.51	4.34
30Y	3.67	2	-29	2.85	4.42

China	Last Price %	1M chg bp	YTD chg bps	52W low%	52W high%
3Y	2.44	-7	2	2.14	2.57
5Y	2.62	-6	0	2.36	2.77
7Y	2.76	-7	-6	2.58	2.91
10Y	2.78	-8	-6	2.61	2.96
30Y	3.15	-8	-5	3.08	3.36

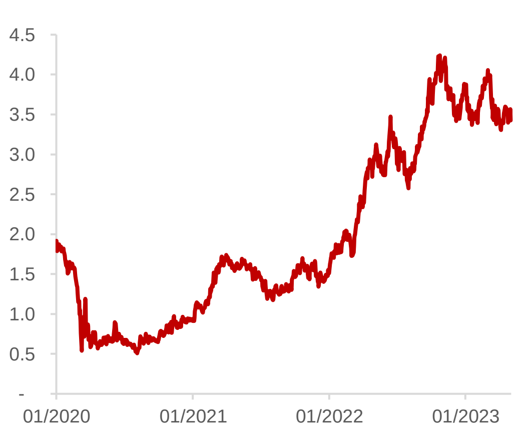
Japan	Last Price %	1M chg bp	YTD chg bps	52W low%	52W high%
2Y	(0.04)	2	-8	-0.11	0.07
5Y	0.11	1	-12	-0.04	0.34
7Y	0.22	-1	-24	0.02	0.58
10Y	0.39	4	-3	0.16	0.58
30Y	1.23	-3	-38	0.95	1.72

Germany	Last Price %	1M chg bp	YTD chg bps	52W low%	52W high%
2Y	2.69	1	-7	0.03	3.38
5Y	2.31	0	-27	0.39	2.90
7Y	2.29	1	-28	0.45	2.82
10Y	2.31	2	-26	0.68	2.77
30Y	2.42	5	-13	0.95	2.71

U.S. Treasury yield curve



10-year U.S. Treasury yield



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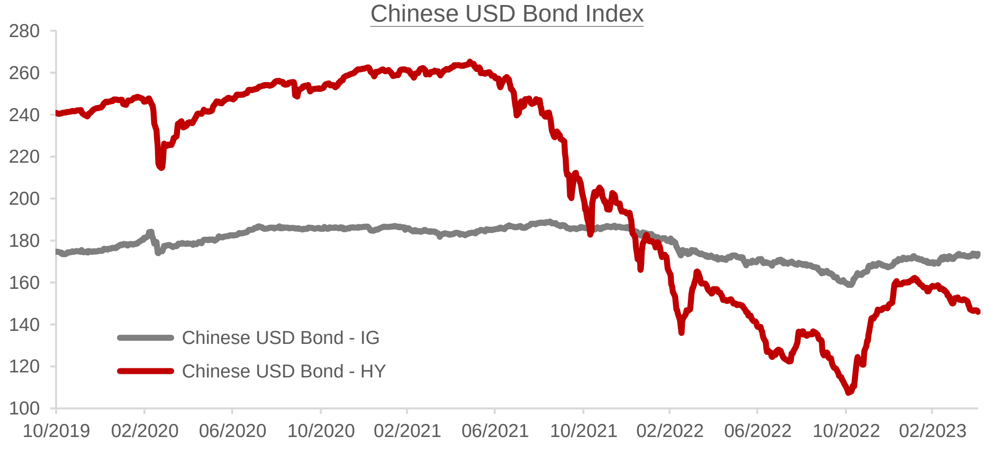
For corporate bonds, credit spreads fluctuated narrowly, recording a small positive return overall, and performance of European and American bank bonds differed, with the various grades of bonds of large banks recovering nearly 80% of the widening range from the market's high point in March, while bonds of small banks rebounded weakly or even fell further. As for Chinese USD bonds, the scarcity of domestic assets further supported bonds issued by Chinese state-owned enterprises with a background of state-owned capital, while real estate suffered a decline due to gradually falling sales and negative individual credit sentiment. Overall in April, Chinese investment-grade bonds rose 1% and high-yield bonds fell by 6.7%.

CDX Index	Current Value	1M chg bp	YTD chg bps	52W low%	52W high%
IG CDX	76	(0)	(6)	66	114
HY CDX	466	3	(18)	400	640
EM CDX	238	8	86	205	395
Bond index					
ICE Asian Dollar Corporate	431	0.8%	3.4%	384	432
ICE China Issuers Dollar IG Corporate	203	1.0%	3.5%	185	204
ICE China Issuers Dollar HY Corporate	183	-6.7%	-4.9%	115	218
ICE US Corporate	3116	0.8%	4.3%	2809	3142
ICE US High Yield	1467	0.9%	4.7%	1345	1481
ICE Emerging Markets Corporate	414	0.8%	3.1%	373	417
Bloomberg Global-Aggregate	461	0.4%	3.5%	416	477
Bloomberg Global-Aggregate 1-3 Year	171	0.3%	1.9%	159	172



Economic Data

In terms of inflation, US CPI continued to fall, but the core CPI rebounded, and the first-quarter PCE exceeded expectations, indicating that the Fed's most concerned sticky part of the inflation still exists. In terms of economic data, US GDP in the first quarter was lower than expected, but the consumption sector remains strong when viewed by sub-items, and PMI data continues to indicate strong services and weak manufacturing. Along with the gradual easing of the banking crisis, the expected timing of the Fed's interest rate cut has been delayed. In China, the momentum of economic recovery weakened, and the April PMI fell across the board, as structural problems still persisted. In terms of progression in the economic cycle, Europe is still slightly lagging behind the United States.

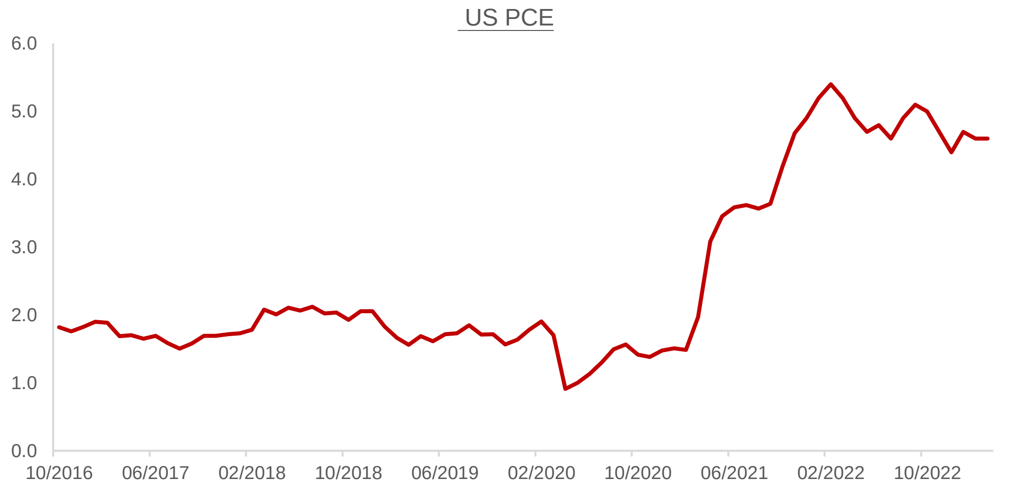
Outlook

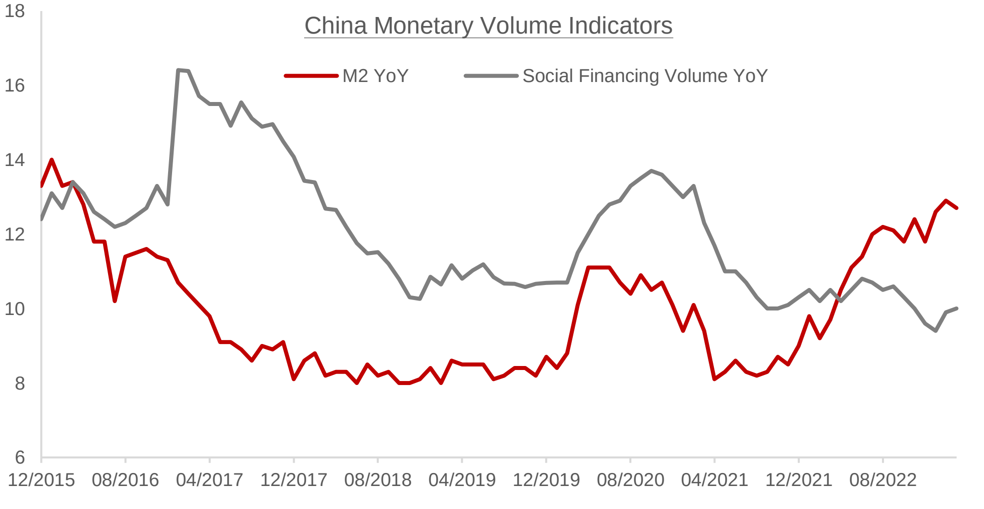
There still exists significant pricing disagreement among different assets in the market. On the one hand, the implied volatility of global equity assets is low, indicating that investors generally agree on the potential risk of future declines in stocks. On the other hand, the volatility of bonds, especially US Treasuries, is relatively high. We also believe that wide fluctuations will continue to be the main trend in the medium- to long-term US Treasury bond market, influenced by multiple factors such as debt ceilings and bank risks. The market had some prior expectations for a rapid takeover of FRC again, considering that the regulation of regional banks in the United States lags far behind that of systemic banks. With investors' growing concerns about US regional banks, similar runs or negative events may still occur in the future. However, the overall US economic and financial system is currently relatively healthy, and the impact of expected events on the market may gradually decrease, but we need to be cautious against other black swan events.

In terms of the US economy, existing data still shows that the slowdown in inflation and economic growth is slower than market expectation, but it is believed that recession will still occur, though perhaps late. If combined with financial risk and stagflation risk, the depth may be greater. As the market gradually shifts from the early period of stock-bond correlation to stock-bond opposition, signalling the end of interest rate hikes, we believe that the current focus should be on the starting point of interest rate cuts rather than the endpoint of rate hikes (the May FOMC meeting has basically confirmed this). We continue to expect the Fed to cut interest rates 1-2 times in the fourth quarter of this yea, but the speed and magnitude of initial rate cuts will be faster and greater.

For corporate bonds, the enthusiasm of global investors for this asset class has kept overall credit spreads at relatively expensive valuation levels. Since the banking crisis in March, the fluctuation range of long-term investment-grade credit spreads has been significantly lower than that of benchmark interest rates, indicating that market concerns are still limited to individual or certain sectors and have not yet spread to the entire market. With the peak of interest rate hikes, the medium-term dimension of US Treasury yields is showing a bullish trend, but we still believe that the market will not experience a unilateral decline in interest rates or widening credit spreads. Continuous volatility is still a high probability event. Considering that the yield curve is still deeply inverted, from the perspective of yield after volatility adjustment, it is more effective to hold some short- and medium-term bonds and build positions in high-rating bonds in defensive sectors when interest rates rise or in high-quality bonds affected by short-term risk sentiment adjustment.

Regarding Chinese offshore dollar bonds, the mismatch between the economic cycles of China and the United States has led to a sustained difference in yields between investment-grade domestic and dollar bonds. Long-term convergence in expectations for interest rates and expected scarcity of assets would offer robust technical support for high-quality dollar bonds. There are still good opportunities for investing in Chinese USD bonds when there is appropriate bond supply at suitable prices. In terms of property bonds, high-frequency data shows that sales have weakened to some extent. The low supply in first- and second-tier cities and low demand in third- and fourth-tier cities continue to put pressure on sales. However, if the economy continues to weaken, policy support to the real estate sector could return, and contrarian investing would become the main tactic for the sector.





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