華夏基金(香港)
ChinaAMC (HK)

MARKET INSIGHTS

Patience Pays in China's Economy

November 2023

Equity

The pace of sell-off in October moderated due to China's better macro data and policy measures, further US-China dialogue, and the steady DXY range which is between 105-107. Many positive signals have been seen this month. Recent policy moves have been more positive than the market expected. The m-o-m growth rate of Aggregate Financing to the Real Economy remained at a relatively high level for two consecutive months due to the increase in government bond issuance, and the significant move by Central Huijin Investment to increase its stakes in multiple banks led to an improvement of market sentiment. As Beijing made a rare mid-year budget expansion of Rmb1trn, despite the already reachable 5% real GDP target this year, the top leadership made an equally rare visit to the PBoC.

Market Performance

MSCI China index dropped by 4.36% in the month of October, the third month it had been sold off, as restrictive global liquidity conditions continued and UST yield reached a decade high. But the pace of sell-off in October moderated due to China's better macro data and policy measures, further US-China dialogue, and the steady DXY range which is between 105-107. Many positive signals have been seen this month. Tianjin, Liaoning, Jiangxi and many other places in China announced the resumption of issuing refinancing bonds, with the funds being used to repay existing debts. On Oct 11, Central Huijin Investment increased its stake in four of the country's biggest banks, and it intended to boost its holdings in the coming six months. On Oct 24, China's top parliament body has approved a 1 trillion yuan in sovereign bond issuance to help rebuild areas hit by this year's floods and improve urban infrastructure to cope with future disasters. The Hong Kong Government announced a reduction of the stamp duty rates for share transfers and a number of stamp duty related changes in respect of sales and purchases of residential property at the end of this month.

Greater China Indices	Aug Close	Monthly % Change	YTD %	52 Week Low	52 Week High	TICKER
CSI 300	3572.51	-3.17	-7.73	3450.65	4268.15	SHSZ300 Index
MSCI China	56.15	-4.36	-12.91	50.27	75.86	MXCN Index
HSI	17112.48	-3.91	-13.49	15442.76	22700.85	HSI Index
HSCEI	5861.74	-4.66	-12.58	5217.02	7773.61	HSCEI Index
Global Indices						
S&P 500	4193.80	-2.20	9.23	3708.84	4607.07	SPX Index
Dow Jones Industrial Average	33052.87	-1.36	-0.28	31429.82	35679.13	DJI Index
Nasdaq Composite	12851.24	-2.78	22.78	10207.47	14446.55	CCMP Index
FTSE 100	7321.72	-3.76	-1.74	7188.63	8047.06	UKX Index
DAX 30	14810.34	-3.75	6.37	13193.51	16528.97	DAX Index
Nikkei 225	30858.85	-3.14	18.26	25661.89	33772.89	NKY Index

Economic Data

China's manufacturing PMI index fell to 49.5 in Oct from 50.2 in Sep. The new orders sub-index fell to 49.5 in Oct from 50.5 in Sep, while the output sub-index fell to 50.9 in Oct from 52.7 in Sep. The decline in manufacturing PMI was linked to fewer working days due to National Day golden week and a high base from front-loaded demand in September. The non-manufacturing PMI index fell to 50.6 in Oct from 51.7 in Sep. The construction industry sub-index fell to 53.5 in Oct from 56.2 in Sep, the speed of infrastructure project construction maintained solid. The services sub-index fell to 50.1 in Oct from 50.9 in Sep. the PMIs of service industries such as railway and air transport, postal, telecommunication and satellite transmitter were above 55 while the PMIs of capital market services and real estate were muted.

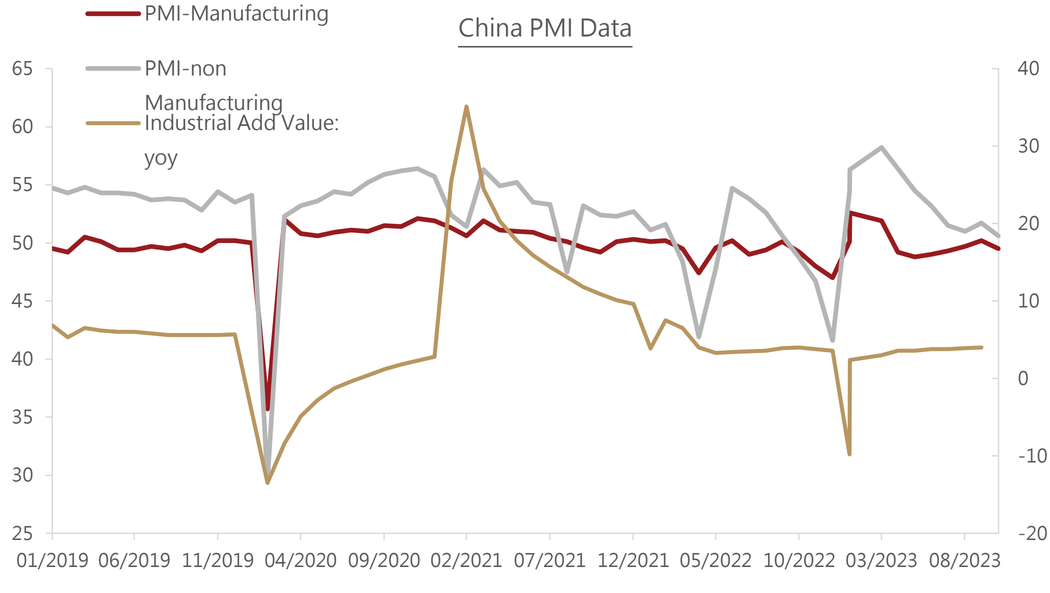
Outlook

Looking forward, we maintain our long-term positive view on China equity market. Recent policy moves have been more positive than the market expected. The m-o-m growth rate of Aggregate Financing to the Real Economy remained at a relatively high level for two consecutive months due to the increase in government bond issuance, and the significant move by Central Huijin Investment to increase its stakes in multiple banks led to an improvement of market sentiment. As Beijing made a rare mid-year budget expansion of Rmb1trn, despite the already reachable 5% real GDP target this year, the top leadership made an equally rare visit to the PBoC. In terms of equity market direct impact, we see the budget expansion as a positive move in the right direction, while more support is likely needed. Given that this is the first mid-year budget adjustment since 1998-2000, despite the 5% GDP target already looking secure this year, we think the market will view it as a signal that policy makers are willing to depart from the norm to stabilize the economy.

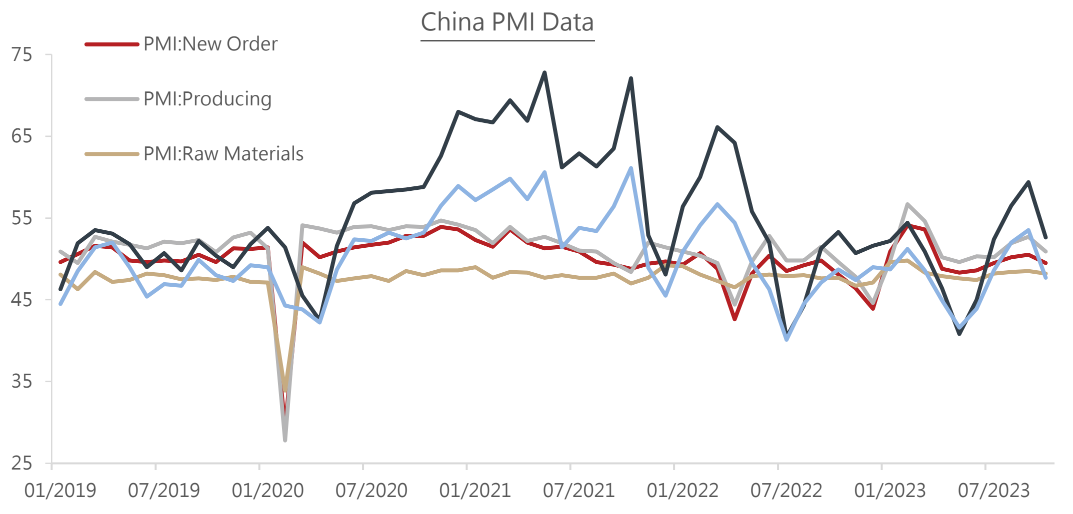
We will continue to seek a balance between value and growth. We continue to focus on the long-term policy beneficiaries (eg. software localization and advanced manufacturing), short-term policy beneficiaries (property and property-related sectors) and reopening-related opportunities (eg. consumer, Internet and financials). We will prudently pay attention to some thematic opportunities, including AI and SOE re-rating. We will also track property sales stabilization, senior level US/China economic communication, and upbeat GDP target and guidance on incremental easing at the December Central Economic Work Conference.

Risk

Sino-US relationship worsens than expectation. International geopolitics worsens than expectation; China's economy recovers less than expected.



Equity


China PMI Data
PMI:New Order
PMI:Producing
PMI:Raw Materials
75
65
55
45
35
25
01/2019
07/2019
01/2020
07/2020
01/2021
07/2021
01/2022
07/2022
01/2023
07/2023


China Economy Activities
40
30
20
10
0
-10
-20
-30
200
150
100
50
0
-50
-100
-150
-200
01/2016
07/2016
01/2017
07/2017
01/2018
07/2018
01/2019
07/2019
01/2020
07/2020
01/2021
07/2021
01/2022
07/2022
01/2023
07/2023
FAI: yoy
Total Retail Sales of Consumer Goods: yoy
Net Export: yoy

Markets remained volatile in October, with the 10-year US Treasury yield fluctuating in the first half of the month. The U.S. Treasury Department's quarterly financing plan shows that the issuance of long-term bonds is currently lower than expected, leaving room for adjustments based on market conditions. Economic data will continue to be the main driver for Treasury yield fluctuations. It is expected that the yield curve will remain steep, while the short end of the curve, influenced by the approach of the end of the rate hiking cycle, has a greater chance of falling back from the high range. The long end of the curve is affected by a tight financial environment, the financing pressure of enterprises, and the high level of inflation maintaining for a short time. The long-term yield will continue to fluctuate in the high range, with limited downside space.

Market Performance

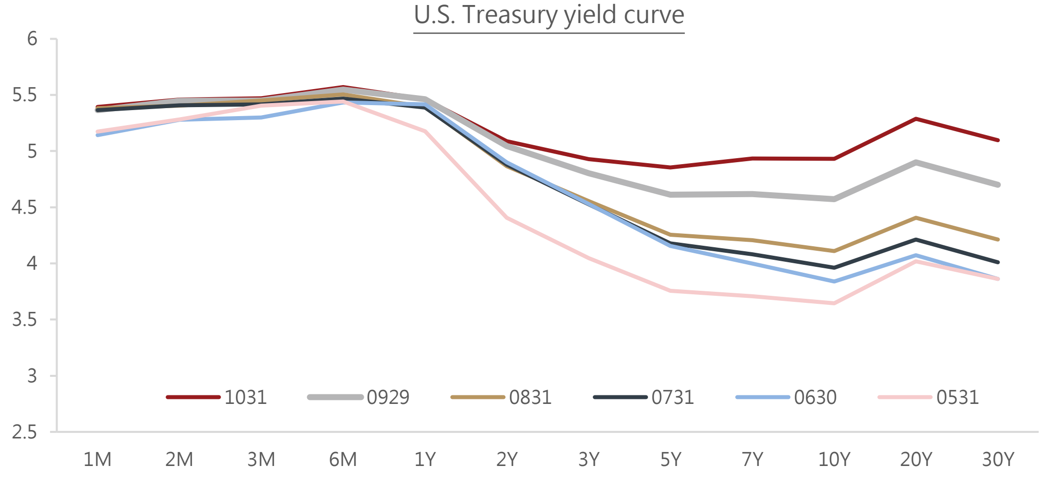
Markets remained volatile in October, with the 10-year US Treasury yield fluctuating in the first half of the month. The 10-year rate reached 5% for the first time since 2007, only to subsequently fluctuate downwards. Both the Federal Reserve and the European Central Bank announced a pause in rate hikes in November, as expected. The Fed left room for further tightening, and market expectations point to the end of the current round of US rate hikes. The US Treasury Department's total borrowing projection for the fourth quarter was less than expected compared to the previous period, providing some support to long-term US Treasuries, but the economy is resilient and a recession is unlikely to push US Treasury yields to further spike in the short term. On the asset side, high-yield bonds outperformed investment-grade bonds and equities, while the performance of commodities was mixed.

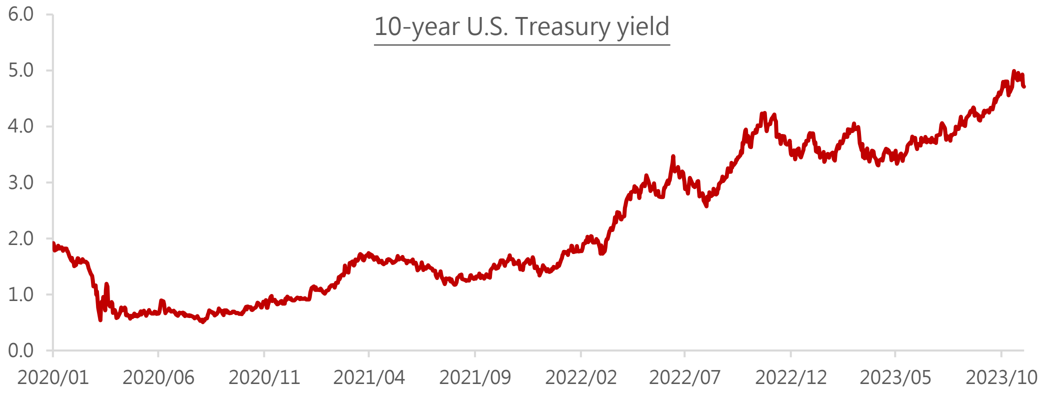
United States	Last Price %	1M chg bp	YTD chg bps	52W low%	52W high%
2Y	5.09	3	66	3.55	5.26
5Y	4.85	23	85	3.20	4.99
7Y	4.93	29	97	3.24	5.03
10Y	4.93	36	106	3.25	5.02
30Y	5.09	39	113	3.40	5.18

China	Last Price %	1M chg bp	YTD chg bps	52W low%	52W high%
3Y	2.42	4	0	2.18	2.57
5Y	2.54	1	-9	2.34	2.77
7Y	2.69	-1	-13	2.51	2.91
10Y	2.69	1	-15	2.54	2.96
30Y	3.00	0	-20	2.88	3.32

Japan	Last Price %	1M chg bp	YTD chg bps	52W low%	52W high%
2Y	0.15	11	11	-0.09	0.17
5Y	0.46	15	23	0.05	0.49
7Y	0.70	18	24	0.08	0.73
10Y	0.95	19	53	0.18	0.97
30Y	1.87	14	26	1.11	1.91

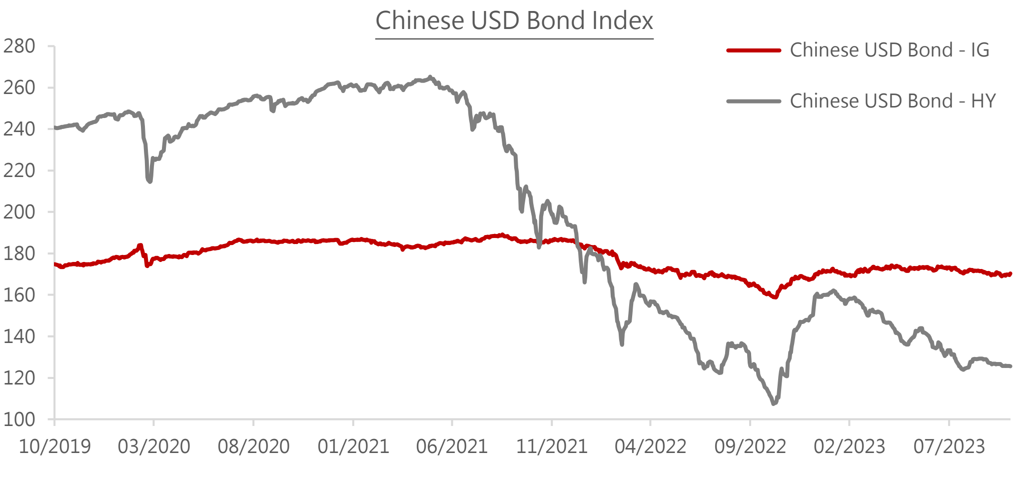
Germany	Last Price %	1M chg bp	YTD chg bps	52W low%	52W high%
2Y	3.02	-27	25	1.96	3.38
5Y	2.66	-24	8	1.74	2.93
7Y	2.69	-20	12	1.74	2.94
10Y	2.81	-12	24	1.74	3.03
30Y	3.09	0	55	1.60	3.26





The corporate bond market has been under the joint impact of the continuous flow of news about the Israel-Palestine conflict, together with the high and volatile interest rates. The credit spread of US investment-grade bonds has fluctuated widely, with the credit spread of Chinese investment-grade dollar bonds primarily fluctuating and narrowing slightly. The third-quarter corporate quarterly reports from the US show that the overall performance of corporate income and profitability is better than expected, with clear sectoral differences. The sectors most affected by high interest rates have seen a larger spread in credit spreads. On the Chinese side, domestic stimulus policies have led to a narrowing wave of credit spreads for investment-grade bonds, despite a significant drop in prices of the high-yield real estate sector due to further declines in sales and negative news flows coming from developers. The monthly decline in Chinese investment-grade bonds was 0.5%, with a decline in high yield of 2.3%.

CDX Index	Current Value	1M chg bp	YTD chg bps	52W low%	52W high%
IG CDX	80	7	(3)	62	94
HY CDX	517	44	33	400	554
EM CDX	228	6	77	188	279
Bond index					
ICE Asian Dollar Corporate	418	-0.5%	0.3%	384	432
ICE China Issuers Dollar IG Corporate	199	-0.2%	1.1%	186	204
ICE China Issuers Dollar HY Corporate	144	-2.6%	-25.1%	117	218
ICE US Corporate	2947	-1.8%	-1.4%	2840	3133
ICE US High Yield	1467	-1.0%	4.7%	1366	1503
ICE Emerging Markets Corporate	403	-0.9%	0.5%	374	417
Bloomberg Global-Aggregate	431	-0.9%	-3.4%	422	467
Bloomberg Global-Aggregate 1-3 Year	167	0.1%	-0.5%	160	171



Economic Data

The U.S. economy has shown impressive performance, with the GDP growth rate in the third quarter compounded annually at 4.9%. The market generally believes that the strong growth in the third quarter may not be sustained, and the growth in the fourth quarter is expected to decline. The full-year growth is expected to exceed 2%. The employment data is somewhat varied, with the unemployment rate remaining stable at a high level. The UAW strike has ended, and the temporary agreement indicates that labor costs will continue to rise. The data on non-farm payrolls and job vacancies has shown a significant increase. Both the rise in labor costs and the high level of unemployment will continue to influence inflation data. It is necessary to pay attention to further changes in employment data. On the inflation front, the data in September exceeded expectations, mainly due to the increase in energy prices. The prices of core goods have been falling continuously for several months, and the prices of core services have risen noticeably. The distance to the return of inflation to the target level is still significant. In terms of retail data, September saw a significant increase in retail sales, indicating that consumers' consumption power is strong and has not been significantly suppressed by high interest rates. The increase in new housing sales indicates an optimistic expectation for economic growth. However, retail in Europe has been affected by high interest rates, with a significant drop in the Eurozone, and economic growth has also slowed. It is generally expected that Europe has reached the end of this round of rate hikes. Japan has raised its inflation expectations and made a mild adjustment to the YCC policy, taking the 1% upper limit of the 10-year government bond yield as a reference point, allowing it to break through.

Outlook

The U.S. economy's third-quarter data overall is robust, although investors debate on how much further the trend could continue. With the Federal Reserve's 'higher for longer' view still widely accepted by the market, Treasury yields will continue to fluctuate in the at a high level, and the Federal Reserve will continue to adjust its interest rate policy based on data. The third-quarter inflation slowed, and the non-farm employment data showed a significant increase while labor costs still have room to grow. The high level of unemployment will continue to suppress the rapid growth of inflation. The U.S. Treasury Department's quarterly financing plan shows that the issuance of long-term bonds is currently lower than expected, leaving room for adjustments based on market conditions.

Economic data will continue to be the main driver for Treasury yield fluctuations. It is expected that the yield curve will remain steep, while the short end of the curve, influenced by the approach of the end of the rate hiking cycle, has a greater chance of falling back from the high range. The long end of the curve is affected by a tight financial environment, the financing pressure of enterprises, and the high level of inflation maintaining for a short time. The long-term yield will continue to fluctuate in the high range, with limited downside space. Attention should be paid to the impact of geopolitical events on interest rates and the possibility of recession triggered by data exceeding expectations. Japan has relaxed the hard cap of 1% on the 10-year government bond yield, and increased inflation expectations. The Eurozone inflation fell back from previous highs, with economic growth slowing and high interest rates affecting the economy, which may prompt the ECB to start the rate-cut process sooner than the US.

For credits, investors still lack a clear direction for spreads and duration. On one hand, short-term bond yields remain attractive and are sought after by buyers. On the other hand, long-term bonds are not only affected by the volatile Treasury yields but also potential new issuances that may reprice existing spreads. The third-quarter results of US issuers were better than expected, partially alleviating the outflow of funds from investment-grade funds and ETFs, and reducing the widening of some spreads. It is expected that the issuance of US bonds in November will slightly increase compared to October, and the demand for US credits will also grow accordingly. Credit spreads will continue to fluctuate, with the stabilization of Treasury yields and the resilience of economic growth, providing room for spreads to narrow.

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

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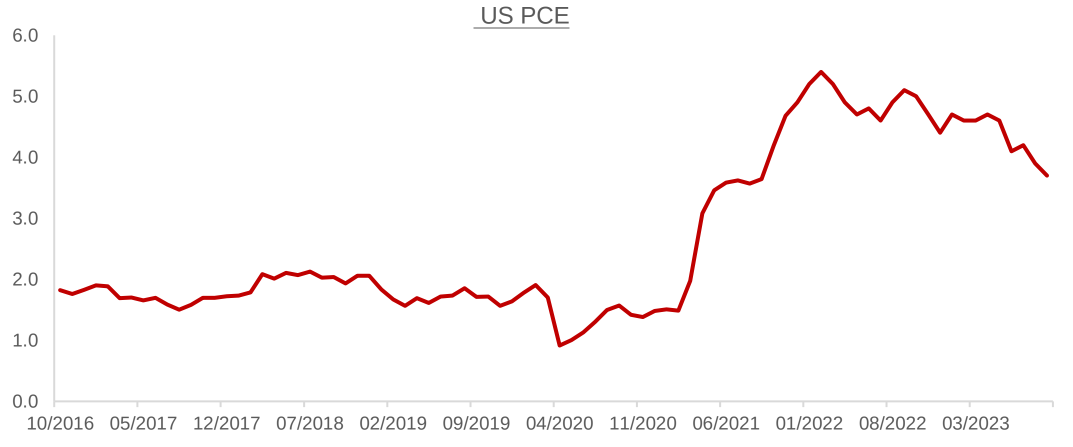
Compared to last month, the Federal Reserve has slightly shifted towards a more dovish stance, and the spread of high-rated bank sectors may have more room to tighten compared to other high-rated companies. Chinese corporate bonds are expected to be more differentiated, with both onshore and offshore spreads continuing to attract buyers, and the spreads of high-rated SOE bonds will continue trading at low levels. Overall, from a technical perspective, US Treasury yields are at a temporary high level, presenting opportunities for selective positioning. At the same time, as credit continues to be supported by ongoing capital inflows, there is room for credit spreads to tighten. However, caution should still be exercised regarding the risk of widening credit spreads.



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