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EQUITIESFIRST® Progressive Capital

OUTLOOK ON IMPACT OF CHINA'S SUPPORTIVE POLICIES

CHINA'S POLICY SUPPORT IN 2024

In 2024, the Chinese government has rolled out numerous supportive policies of varying magnitude, coupled with data on interest rates and economic indicators. This report intends to streamline and clarify some of these developments, offering a consolidated overview of the recent supportive initiatives and their potential impact on China's stock market and policy landscape.

It further focuses on the government's strategic initiatives to stabilize the stock market and ensure sustained economic growth. We highlight key policy measures, including the speculated stabilization fund, interest rate adjustments, leadership changes in the China Securities Regulatory Commission (CSRC) and liquidity enhancements, alongside efforts to support the property market.

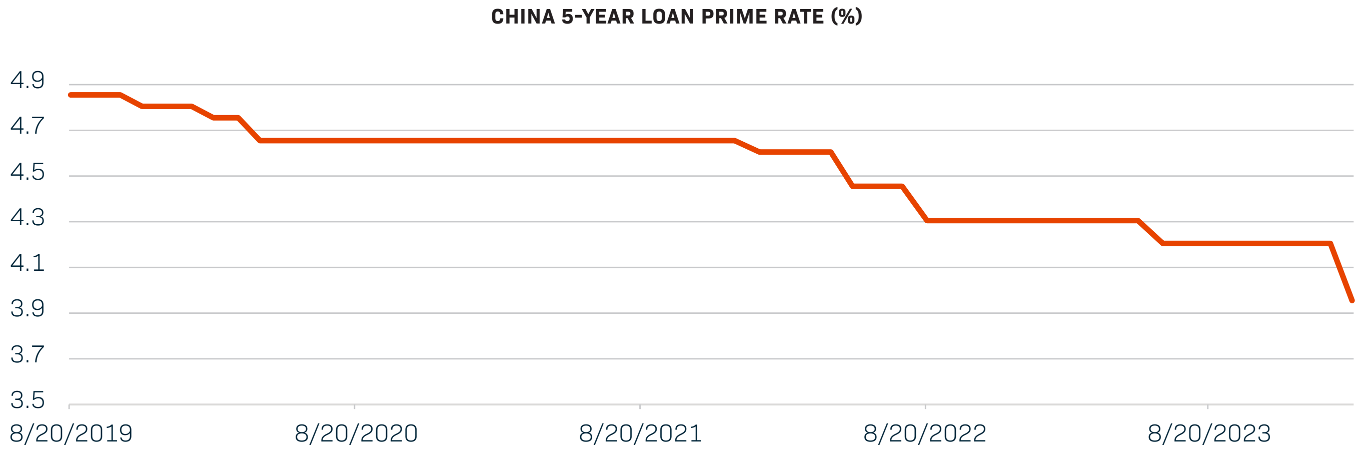
SPECULATION SURROUNDING RMB 2-TRILLION STABILIZATION FUND

Amidst fluctuations in the stock market, Bloomberg reported on 23 January that Chinese officials contemplated a robust initiative to foster stability. The proposed plan involved deploying approximately RMB 2 trillion (USD 278 billion) from the offshore accounts of state-owned entities. The intention was to leverage this fund for purchasing shares domestically via the Hong Kong exchange link. This initiative, aimed at reinforcing market equilibrium, aligned with a broader economic strategy that was underscored in a recent cabinet session led by Premier Li Qiang. The strategy highlighted the government's commitment to augment mid- to long-term capital injections to fortify the financial market's foundation and ensure its healthy progression.

This fund may be poised to have a positive impact on the stock market. The strategic infusion of funds is expected to notably stabilize market fluctuations and potentially reverse negative trends by injecting liquidity directly into the equity markets. It would signal strong government backing for the stock market, likely bolstering investor confidence domestically and internationally. This reassurance may lead to a stabilization or even an uptick in stock prices as investor sentiment improves.

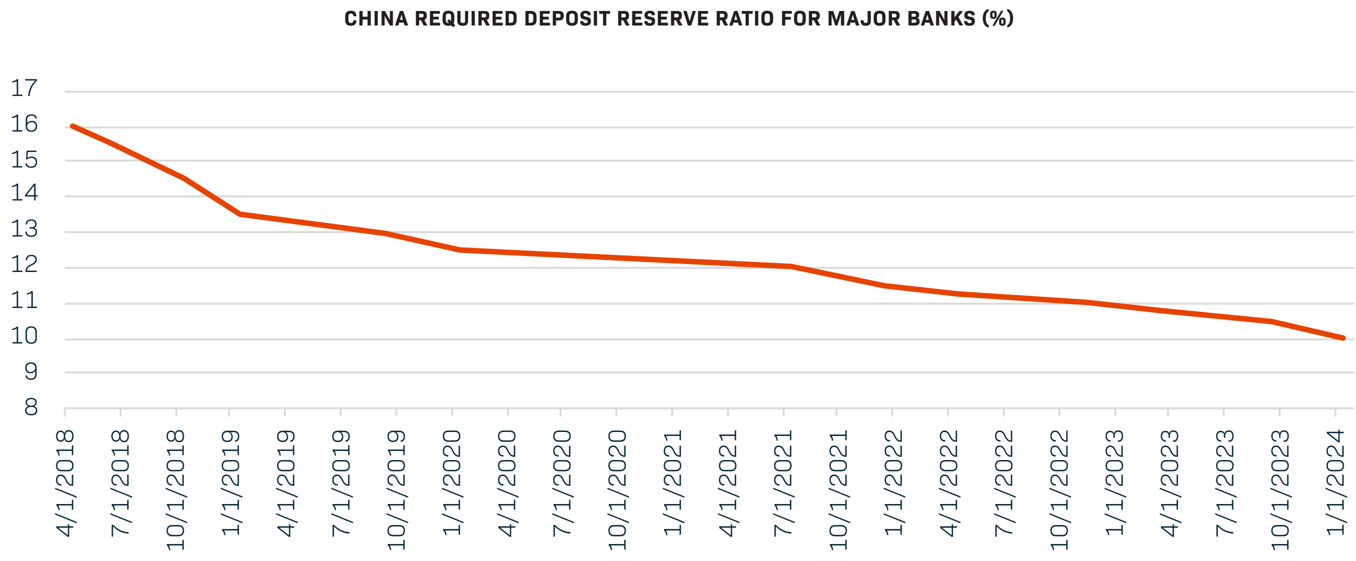
However, the success of this intervention will depend on various factors, including the execution of the purchases, the global economic climate and investor reactions to government policies. While the immediate impact might be positive, maintaining momentum will require continued confidence in the government's economic management and the underlying fundamentals of the Chinese economy.

INTEREST RATE ADJUSTMENT



The People's Bank of China (PBOC) made a significant move by decreasing the five-year loan prime rate (LPR) to 3.95% from 4.2%. This adjustment, the most substantial since 2019, set a new precedent for commercial banks in recalibrating property loans. The magnitude surpassed original market predictions and aimed to invigorate the real estate sector and mitigate deflationary pressures.

LIQUIDITY ENHANCEMENT THROUGH RRR REDUCTION



In a strategic effort to rejuvenate the faltering Chinese economy, the PBOC also revised its monetary policies, notably by slashing the reserve requirement ratio (RRR) by 50 basis points on 5 February. This decisive cut, the largest in two years, mandated banks to hold less cash in reserve. As the first RRR adjustment of the year, it was expected to inject approximately RMB 1 trillion (USD 139 billion) into the economy, surpassing analysts' forecasts. This initiative was part of a comprehensive strategy to foster a robust recovery post-COVID, addressing the ongoing housing downturn and the dampening of global demand.

Source: Bloomberg

STABILIZING PROPERTY: WHITELIST MECHANISM

Major Chinese banks channeled substantial funds into residential construction projects to ensure the completion of homes that had been pre-sold but remained unfinished. The financial infusion constituted a strategic initiative within the "whitelist mechanism," aimed at revitalizing the flagging real estate sector as a cornerstone of Beijing's economic revival strategy.

China Construction Bank (CCB), a leading state-owned commercial bank, engaged in more than 2,000 projects under this mechanism. It greenlit almost 100 projects pending disbursements totaling more than RMB 20 billion (approximately USD 2.78 billion). Initiated by the housing ministry at the year's onset, the whitelist mechanism encouraged provincial governments to identify and recommend financially viable local residential projects for further banking support, focusing on the project's financial health rather than that of the developers.

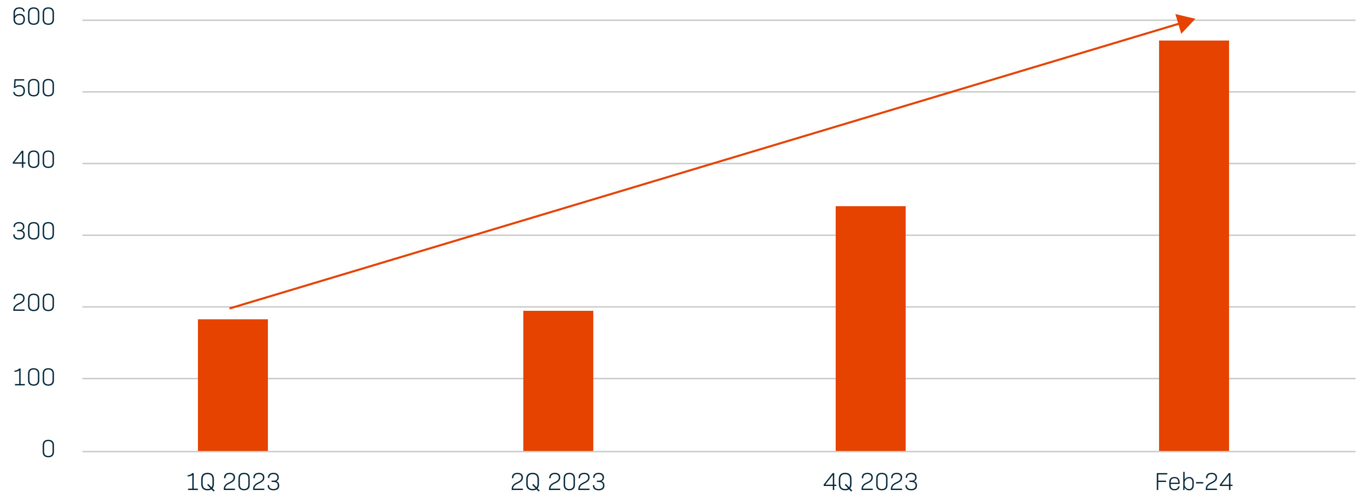
This move was part of a broader initiative by authorities to bolster funding for certain property developers, with more than 100 cities establishing an urban real estate financing coordination mechanism. This setup aimed to enhance collaboration between local governments, housing departments and financial institutions, addressing the financing needs of real estate projects effectively.

As of February 2024, with bank credit to property financing projects surpassing RMB 160 billion (approximately USD 22.2 billion), this collaboration underscored the Chinese government's commitment to stabilizing the property market and fostering sustainable growth within the sector.

STATE-OWNED FUNDS SUPPORT VIA ETF

In a concerted effort to stabilize domestic stock prices amidst market fluctuations, China's state-owned funds have intensified their market activities since late June 2023. This strategic move came in the wake of significant asset growth in major exchange-traded funds (ETFs) that are pivotal in tracking benchmark stock indices. According to data analyzed by Goldman Sachs, SCMP and supplemented with market estimates, the net assets of the top ETFs in China — managed by industry stalwarts such as E Fund Management, Huatai-PineBridge Asset Management, China Asset Management and Harvest Fund Management — reached approximately RMB 569 billion as of February this year.

NET ASSETS OF TOP CHINA ETFs (RMB BN)



These ETFs, dedicated to mirroring the performance of the CSI 300 Index and the top 50 stocks of the Shanghai Stock Exchange, had shown remarkable growth in their combined net assets from RMB 185 billion at the end of the first quarter of 2023 to RMB 194 billion by 30 June, culminating at RMB 339 billion by the end of 2023.

This influx of capital was characterised by market observers as indicative of an aggressive stance on market intervention by the state-owned funds, especially in response to the market downturn. The strategic infusion of funds into these ETFs underscored the government's commitment to bolstering the stock market and reflected the broader efforts to instill confidence among investors and support the underlying market infrastructure.

Source: Goldman Sachs, SCMP

The ETF purchase by the government is reminiscent of similar actions undertaken by the Bank of Japan. We provided a detailed analysis in the previous issue of FirstNews, Volume 42 (Feb 2024), focusing on the outlook for Japan.

In February, Central Huijin Investment, an affiliate of the China Investment Corp with assets worth USD 1.24 trillion and plays a crucial role as a strategic investor in China's leading banks, recently announced its decision to boost its investments in ETFs. The increase was part of a broader strategy aimed at enhancing the stability of the market.

The specifics of the investment, including the total amount committed to these ETF purchases, were not disclosed. This action underscored the government's commitment to supporting the financial ecosystem and ensuring the sustained stability of the market amidst fluctuating conditions.

In a recent statement, the CSRC highlighted the A-share market's historically low valuations, pointing out its prominence for medium- and long-term investment appeal, a perspective shared and acted upon by institutional investors such as Central Huijin. The CSRC expressed its steadfast support for Central Huijin's continued investments and pledged to streamline its market participation by enhancing the accessibility and efficiency of investment channels.

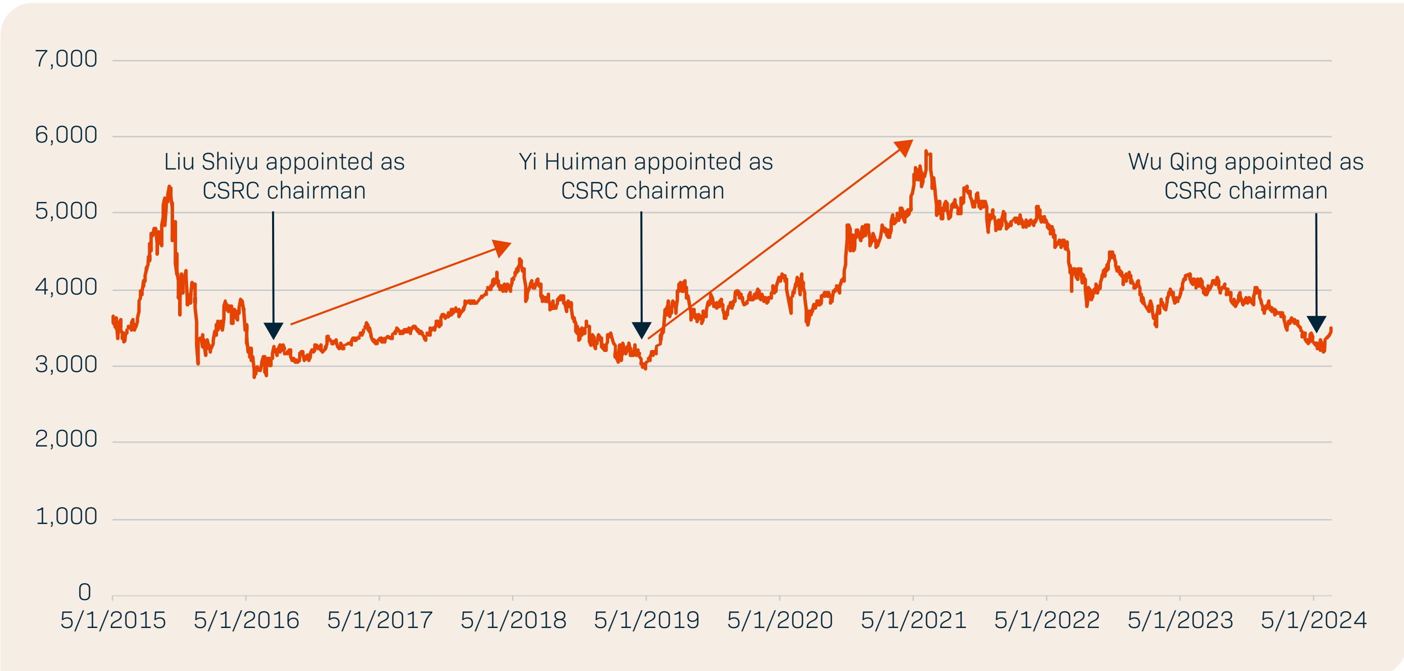
LEADERSHIP TRANSITION AT CHINA'S SECURITIES REGULATORY BODY

The Chinese government recently announced a significant leadership change at the helm of the CSRC, marking a strategic move in its financial oversight framework. Yi Huiman has been succeeded by Wu Qing as the new chairman of the CSRC. Wu Qing brings a wealth of experience from the financial regulatory arena, having previously served as a prominent deputy in Shanghai's municipal government.

His expertise in securities regulation and proven track record of leadership within China's financial markets are anticipated to be invaluable as he steers the CSRC through the prevailing challenges. The leadership transition occurs amidst a period of volatility within China's stock markets, highlighted by the downward trend of key indices.

Wu Qing's appointment is seen as a decisive step towards stabilizing the markets and navigating the complex regulatory landscape, with the aim of fostering a more resilient and robust financial system.

SHANGHAI SHENZHEN CSI 300 INDEX

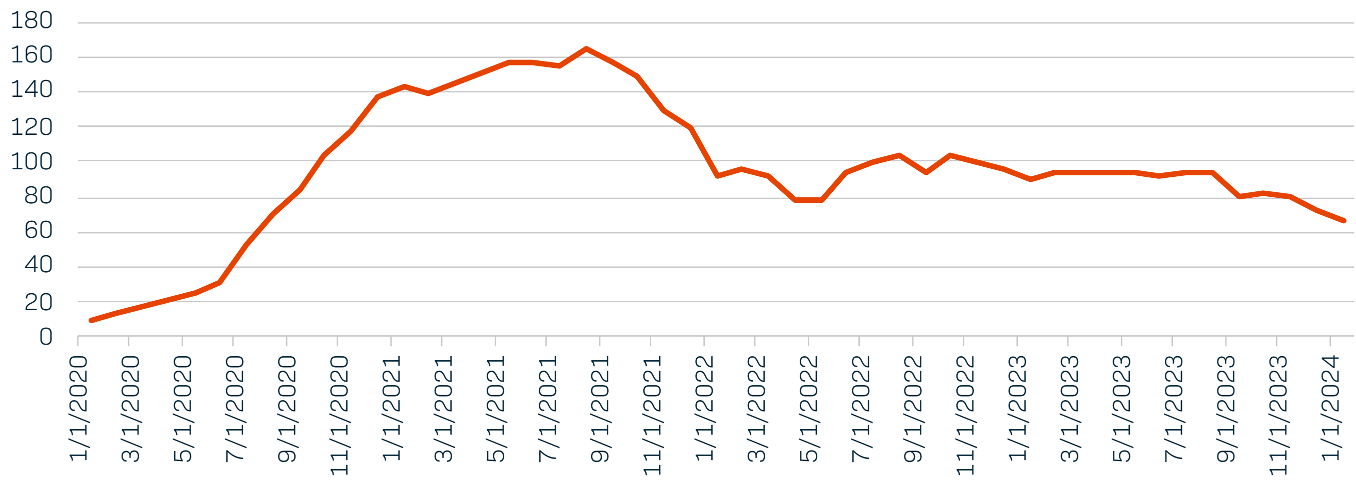


Historically, the appointment of a new CSRC chairman has coincided with an uptick in the domestic A-share market. Observers now anticipate whether this trend will persist under the latest leadership change or will this time be different?

Source: Bloomberg

CURBING SHORT SELLING

CHINA MARGIN TRADING - OUTSTANDING BALANCE OF SHORT SELLING (RMB BN)



Recently, the CSRC implemented a ban on utilizing restricted shares as leverage and short selling. These shares, often held by strategic investors, are typically not tradable until their lock-up period concludes. The ban aims to stabilize the market by limiting the short-selling practices involving these non-public shares.

With the recent enforcement of these restrictions, the outstanding balance of short selling was significantly reduced to around RMB 65 billion (-29% YoY), from RMB 91 billion a year ago, its lowest level since July 2020. Reduction of short selling pressures should support market sentiment in the short term.

EYES ON THE NATIONAL PEOPLE'S CONGRESS

Investors kept a close watch on the National People's Congress meetings held in early March. They particularly focused on indications of the Chinese government's continued proactive stance and provision of supportive policies, as well as the potential impact of any major policy announcement. In the upcoming reports, we will continue to monitor and analyze the resulting impact of these policies.

ROBUST GROWTH IN CHINESE NEW YEAR HOLIDAY SPENDING AND TRAVEL FOR 2024

During the Chinese New Year holiday in 2024, China experienced a consumption recovery. According to the Ministry of Culture and Tourism, domestic tourists collectively spent RMB 632 billion (USD 88 billion) during the festival, marking a 50% rise from the previous year's holiday period. In addition, a total of 474 million domestic trips were made across the country, representing a 34% increase year-on-year and a 19% growth compared to 2019 travel data. (Source: SCMP)

According to the Ministry of Commerce, the retail and catering sectors enjoyed an 11% year-on-year increase in sales, driven by consumer interest in smart home appliances, food and beverage, and traditional clothing.

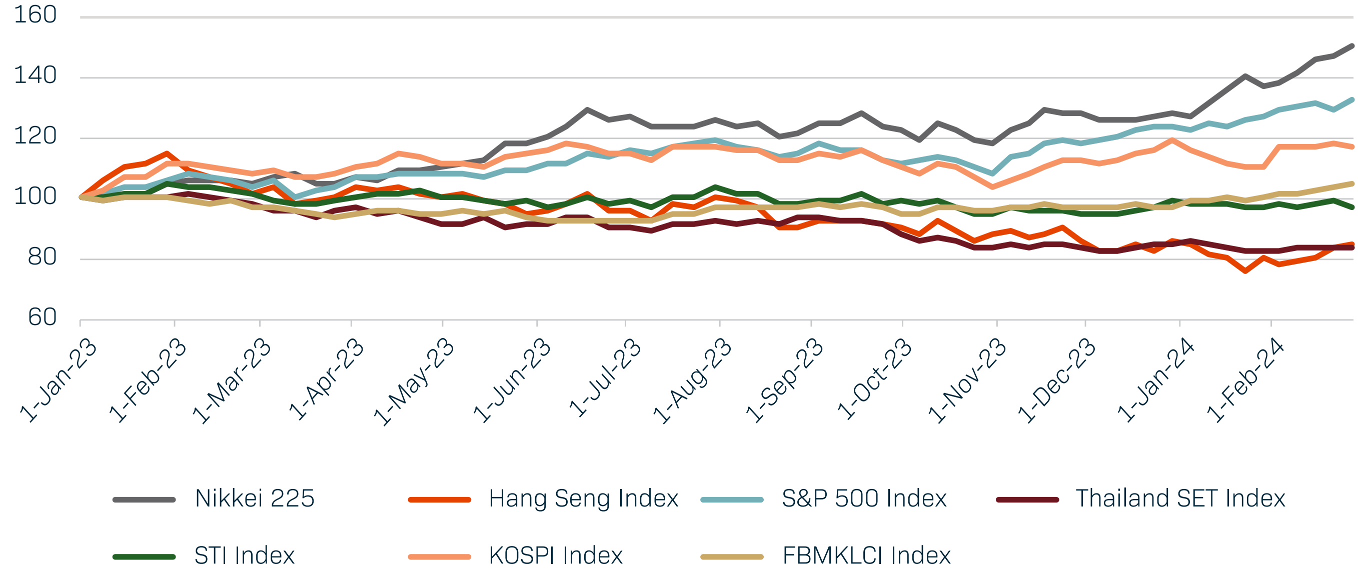
In addition, China's total box office amounted to RMB 8 billion (USD 1.1 billion), marking an 18.5% increase from the holiday period of 2023, according to the China Film Administration, underscoring the entertainment sector's contribution to the overall consumption upswing.

Source: Bloomberg, SCMP

GLOBAL MARKET INDEX PERFORMANCE

In addition to summarizing the recent policy support from the Chinese government which has garnered investor interest, we also provide an overview of recent asset price performance across various countries, along with related data. We hope this offers a clearer understanding of the recent developments.

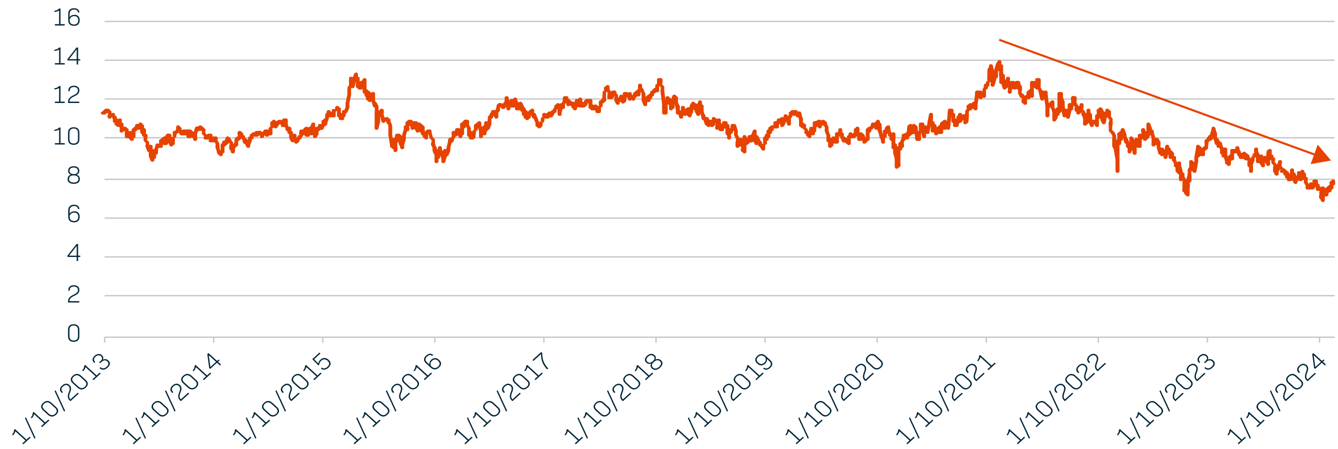
2023 AND 2024 YTD ASSET PRICE PERFORMANCE (%) (REBASED)



Amid a slower-than-anticipated economic recovery in China and escalating global interest rates, the Hang Seng Index has consistently underperformed compared to major world indexes over the past two years. Similarly, stocks listed in Hong Kong have also been subjected to the pressures of rising interest rates.

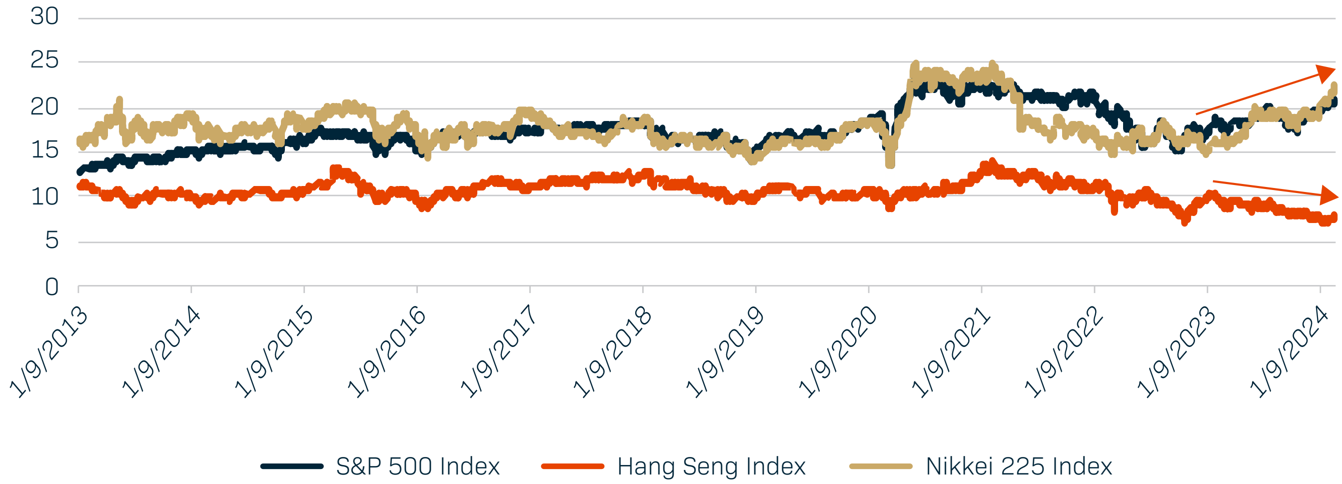
VALUATION GAP

HANG SENG INDEX FORWARD 12-MONTH P/E (X)



Source: Bloomberg

HANG SENG INDEX, S&P 500 INDEX AND NIKKEI 225 INDEX FORWARD 12-MONTH P/E (X)



This resulted in the de-rating of the Hang Seng Index to 8x 2024 P/E, significantly below its historical average of 11x. Consequently, the P/E gap between the Hang Seng Index and the S&P 500 Index has widened to an unprecedented level, with the S&P 500 trading at a premium of 160% over the Hang Seng Index. The market views the widening gap as a reflection of the negative news regarding China's lackluster economic growth.

Given this historical low level, it is not surprising that the Chinese government is reportedly gearing up to introduce several supportive policies aimed at revitalizing the market and the economy.

Meanwhile, both the S&P 500 Index and the Nikkei 225 Index have seen strong re-ratings from their lowest points in October 2022.

RENMINBI DEPRECIATION

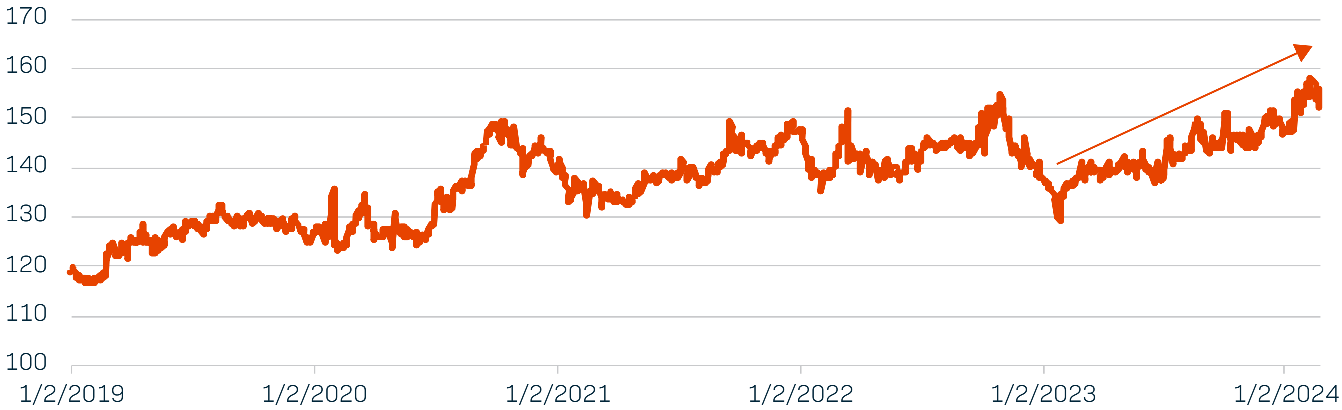
USDRMB EXCHANGE RATE

The depreciation of the renminbi since February 2022 has also contributed to the downward pressure on the Chinese stock market as the asset value, when converted to renminbi, has decreased for foreign investors. It also indicated the market's concerns about the domestic economy's strength, potentially leading to reduced investor confidence in Chinese stocks. Listed Chinese companies with significant foreign-denominated debt are finding their liabilities increasing in local currency terms, affecting their financial health and stock performance. Renminbi depreciation can also lead to capital outflows as investors consider transferring their investments to more stable currencies or markets, adding further pressure to the Chinese stock market.

Source: Bloomberg

RISING CHINA AH PREMIUM

HANG SENG STOCK CONNECT CHINA AH PREMIUM INDEX



Since February 2023, we have observed a widening price gap between stocks with dual listings in mainland China and Hong Kong. This may suggest that global investors are gradually losing confidence in China's economic recovery post-COVID. However, we may see global investors regaining interest in China this year following the recent introduction of supportive policy measures.

In conclusion, the comprehensive measures enacted by the Chinese government, particularly through policy support and strategic interventions, are poised to shape the trajectory of the nation's economic recovery and market stabilization. These efforts, exemplified by the growth recorded during the Chinese New Year period and strategic adjustments in financial oversight, indicate a proactive stance towards fostering economic resilience. Investors and stakeholders are keenly observing the outcomes of these initiatives, looking to gauge their effectiveness in navigating the complex landscape of China's evolving market and economic dynamics.

This report aims to equip readers with a thorough understanding of recent economic activities, policy shifts and their implications, enabling a clearer view of the market's direction and the government's strategic responses.

Source: Bloomberg

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