

NAVIGATING THROUGH CHANGE: HONG KONG'S CAPITAL MARKET DEVELOPMENTS

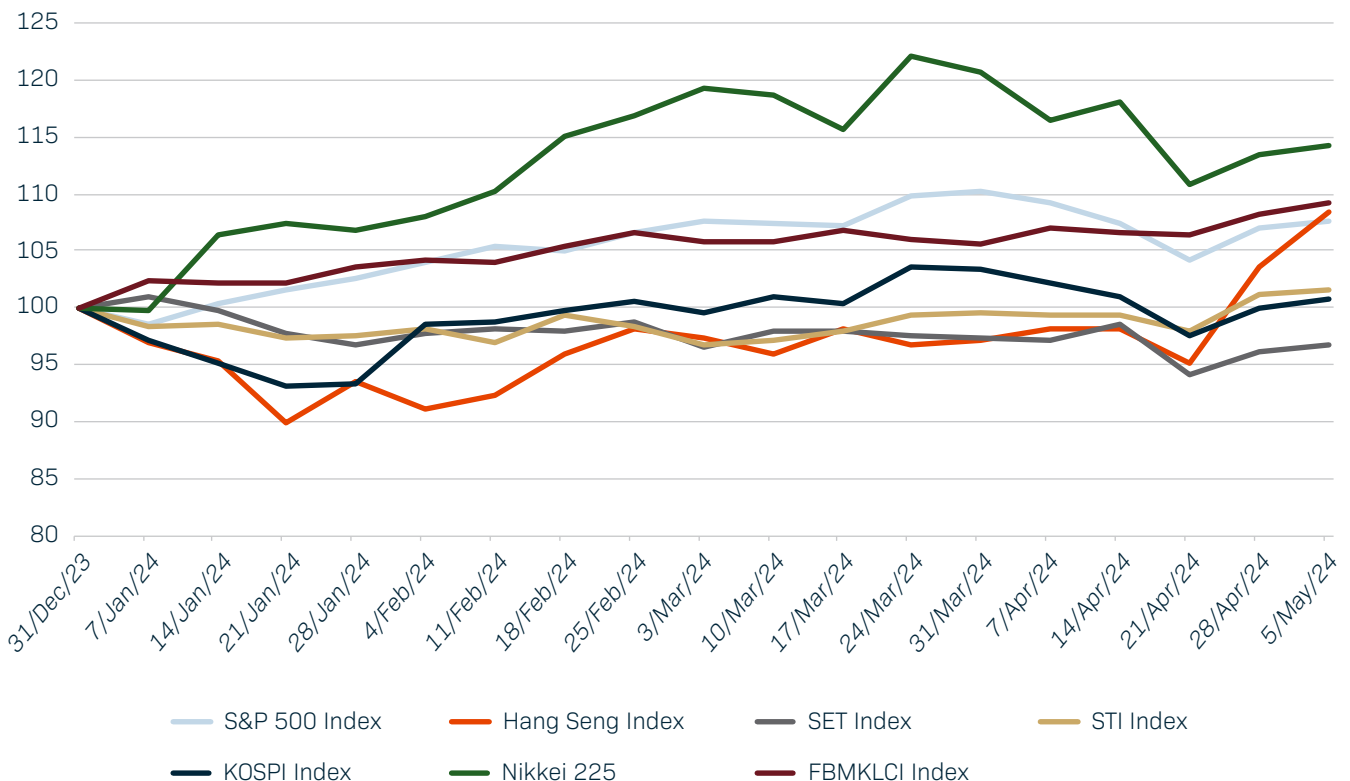
In Volume 43, issued on March 14, 2024 (<https://equitiesfirst.com/hk/firstnews-vol/outlook-on-impact-of-chinas-supportive-policies/>), we highlighted that the valuation of the Hang Seng Index was exceptionally attractive, trading at a historical low with a P/E ratio of 8x for 2024 at that time. Currently, on May 20, 2024, the Hang Seng Index was trading at 9.5x 2024 P/E after a rally.

During the first three months of the year, various supportive policies were introduced, aiming to boost market confidence and stimulate economic growth. Following the publication of our report on March 14, 2024 and these positive developments, the index experienced a significant rally, **rising by 16%** between March 14 and May 20, 2024.

In this Volume 45, we continue our analysis of the events from April and May 2024, identifying the key factors that contributed to the Hang Seng Index's significant recovery. This report provides an overview of the Hong Kong capital market, focusing on the volatility and recovery of the Hang Seng Index from 2020 through 2024. During this period, various global and local events, such as regulatory changes, geopolitical tensions, and economic stimulus measures, have played crucial roles in shaping market performance. Our analysis delves into these factors, offering insights into the causes of fluctuations in market indices.

GLOBAL ASSET CLASS PERFORMANCE 2024 YEAR-TO-DATE

HANG SANG INDEX SURGED IN APRIL IN 2024 YTD (REBASED)



The Hang Seng Index experienced two distinct performance patterns in 2024: a challenging start to the year followed by a significant surge starting in April. Several factors contributed to these trends:

PERFORMANCE BEFORE APRIL 2024:

Prior to April, the Hang Seng Index underperformed compared to other global indices. This was largely due to ongoing concerns about China's economic slowdown, the debt problem of property developer companies and geopolitical tensions. These factors dampened investor sentiment and led to cautious trading in the Hong Kong market.

SURGE STARTING APRIL 2024:

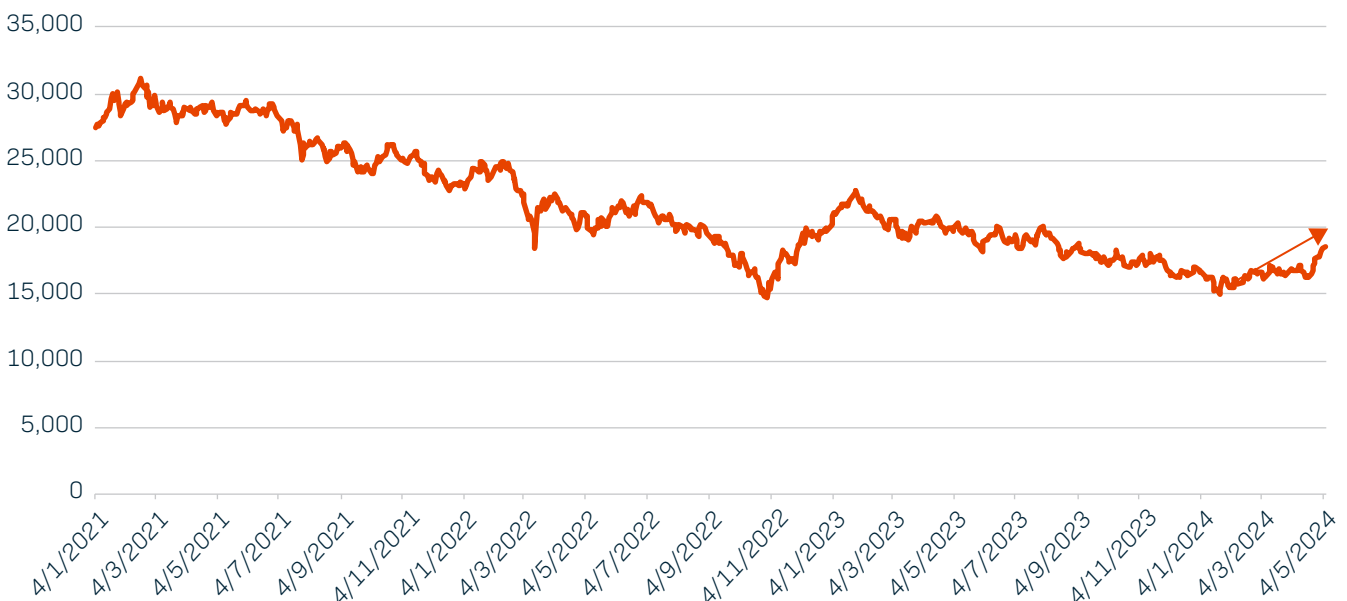
The significant upswing observed in the Hang Seng Index during April can be traced back to an array of both local and international influences. A key factor was the growing optimism surrounding China's economic resurgence. Market sentiments were buoyed by widespread anticipation of the Chinese government unveiling new economic stimulus initiatives. These measures, aimed at energizing consumer spending and bolstering real estate, played a critical role in restoring investor confidence.

Concurrently, specific policy relaxations, such as the easing of property purchase restrictions in several cities, further invigorated the market. This regulatory softening was designed to spur domestic investments and reactivate the housing sector, which is a substantial component of the national economy.

Additionally, news reported that there was an increasing foreign investment in Chinese equities. Attracted by what were perceived as historically low valuations, international funds began to actively acquire stakes in Chinese equities. This influx of foreign funds not only underscored the global investment community's renewed interest in China's stock market but also significantly contributed to the rapid rise of the Hang Seng Index in April.

**THE FALL AND RECOVERY OF HANG SANG INDEX
PERFORMANCE 2021 - 2024 YEAR-TO-DATE**

HANG SANG INDEX BOTTOM OUT?



The Hang Seng Index's performance from 2021 to 2024 reflects significant market volatility influenced by various economic and political factors. Here is a breakdown of the major events each year and their impacts.

2021 (DECLINED BY 14% FROM 27,231 TO 23,397):

The index faced a sharp downturn largely due to regulatory crackdowns in China on various sectors, including Internet and education, which significantly affected companies listed in Hong Kong. This was compounded by rising concerns over the financial health of major property developers like Evergrande.

2022 (DROPPED ANOTHER 15% FROM 23,397 TO 19,781):

The market continued to struggle with the fallout from regulatory actions and the global economic environment did not help much. There were also ongoing concerns about China's property sector and the broader economic slowdown, dragged by the zero-COVID policy, which kept the market under pressure.

2023 (FELL BY 14% FROM 19,781 TO 17,047):

There was an initial optimism as China moved away from its zero-COVID policy, which was expected to revive economic activities and benefit the stock market. However, the optimism was short-lived as the Chinese economy faced other internal challenges, including a continuing slowdown in the property market and weak consumer confidence which kept the index low for most of the year.

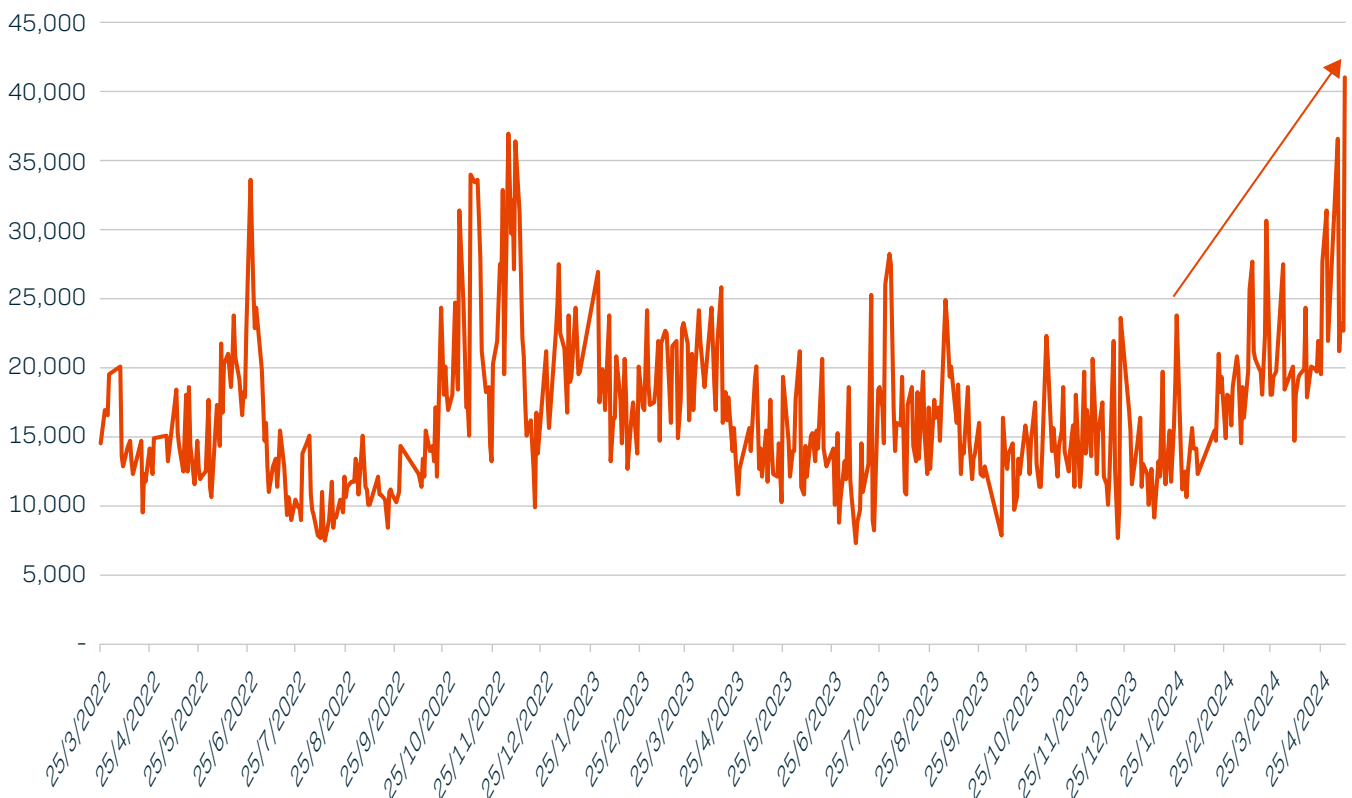
2024 (ADVANCING 11% YEAR-TO-DATE TO 18,963 AS OF MAY 10, 2024):

The Hang Seng Index saw a notable uptick, showing signs of recovery. This surge can be attributed to several factors. Expectations of fiscal stimulus or monetary easing measures by the Chinese government aimed at revitalizing economic growth contributed positively. Increasing share buyback activities as valuations became attractive. In addition, Hong Kong government introduced the removal of additional property stamp duty also boosted the market sentiment.

The recent surge in 2024 suggests that investors are possibly seeing a stabilization in the market conditions and are optimistic about the economic policies that might lead to sustainable growth in China.

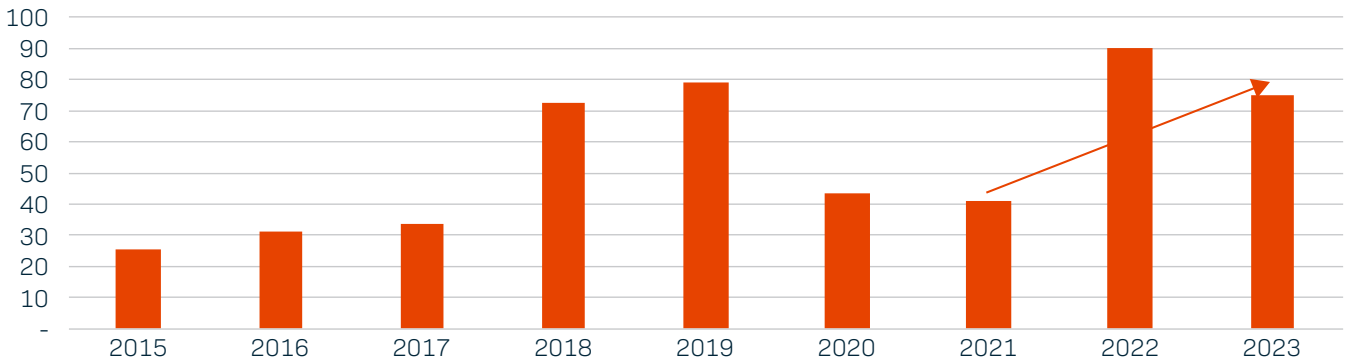
SOUTHBOUND BUY TURNOVER

SOUTHBOUND DAILY BUY TURNOVER SURGING IN 2024 (HKD MN)



Southbound Daily Buy Turnover illustrates a notable trend in investment activity, where investors from Mainland China significantly increased their purchases of Hong Kong stocks year-to-date. Initially, the buying activity showed fluctuations with several peaks and troughs, but starting from around January of 2024, there was a distinct and steady rise in the value of transactions. This surge indicates a growing confidence and strategic interest among Mainland investors in the Hong Kong stock market, potentially driven by relaxing regulatory changes, market conditions and attractive valuation of Hong Kong-listed companies, suggesting a possibly optimistic outlook towards the future prospects of the Hong Kong-listed companies from the Mainland China investors.

HONG KONG-LISTED COMPANY SHARE BUYBACK (USD BN)



Share buybacks by Hong Kong-listed companies reveals a clear trend of increasing activities, particularly pronounced in 2022 and 2023. This uptick in share repurchases was likely influenced by weaker stock price performance and attractive valuations during these years, suggesting that company management perceived their stocks as undervalued. In response, they escalated their share buyback programs as a strategic move to support share prices. This trend reflects a broader strategy where companies capitalize on lower market valuations to return value to shareholders, enhancing earnings per share and investor confidence amid market uncertainties.

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



There is a clear downward trend in the valuation metric for the Hang Seng Index. Initially, the P/E ratio starts off higher, fluctuating around 10 to 12 times earnings, but from around 2021 onward, there is a visible decline, reflecting lower market valuations of the companies making up the index. This gradual decrease in the P/E ratio could indicate a growing perception of risk or pessimism about earnings potential among Hong Kong-listed companies and the macro environment.

SPECULATION OF CHINA'S QE?

The market has a speculation that China will launch more stimulus to support the economy. China may have its own version of "quantitative easing" (QE), which major economies such as US and Japan have implemented.

In October 2023, at a major financial conference, "The People's Bank of China must slowly increase the trading of treasury bonds in its open market operations" Xi delivered a speech that was initially unpublished but later included in a book released in March 2024.

Recently, Reuters reported that a senior official from China's central bank has indicated that the People's Bank of China (PBOC) might incorporate treasury bond trades in the secondary market as part of its monetary policy tools for managing liquidity. This approach reflects the country's efforts to support its economy, which has shown signs of growth but still faces some challenges. The treasury bond market, being one of the largest globally, has seen improved liquidity, making these trades feasible. The central bank remains optimistic about long-term economic growth despite short-term fluctuations in treasury bond yields. Further, a substantial issuance of special long-term treasury bonds is planned to support key sectors.

POLICY SUPPORT ON HONG KONG STOCK MARKET

On April 19, 2024, the China Securities Regulatory Commission (CSRC) announced measures to enhance collaboration with Hong Kong by introducing five strategic initiatives designed to bolster Hong Kong's role as a global financial center. These initiatives are set to foster joint development between the capital markets of Mainland China and Hong Kong.

Key among these measures is the plan to ease the eligibility requirements for exchange-traded funds (ETFs) within the Stock Connect scheme that bridges the two financial markets. Additionally, the CSRC plans to simplify the IPO listing process for Chinese companies in Hong Kong.

The commission will also improve its coordination with relevant departments to aid leading Mainland companies in their efforts to list in Hong Kong. Further initiatives include granting access for qualified real estate investment trusts (REITs) from both the Mainland and Hong Kong to the Shanghai-Shenzhen-Hong Kong Stock Connect and the introduction of yuan-denominated stock trading counters in Hong Kong.

These steps are being taken in response to a significant downturn in Hong Kong's IPO market recently.

CHINA'S LATEST NINE GUIDELINES

On April 13, 2024, State Council of China outlines a comprehensive strategy to enhance the regulation and overall quality of the country's capital markets. This strategy is detailed in nine specific guidelines aimed at strengthening market supervision, promoting transparency and managing financial risks more effectively.

These measures include tightening the criteria for securities issuance and listings, enhancing the regulatory framework around trading practices and improving protections for investors. Additionally, the guidelines focus on integrating medium to long-term capital into the market, fostering innovation and ensuring that the financial sector aligns with the broader goals of national modernization.

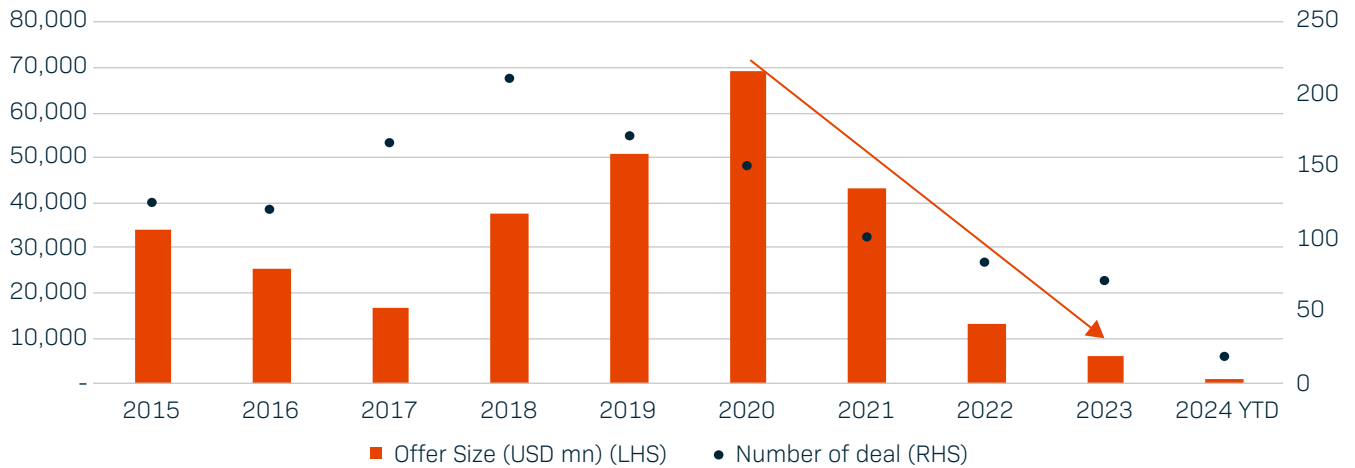
The ultimate aim is to develop a robust, transparent and dynamic capital market by 2035, which aligns with China's vision of becoming a global financial powerhouse.

The strategic guidelines released by the State Council are set to substantially enhance the capital markets of Mainland China and Hong Kong. By tightening the criteria for securities issuance and enhancing the oversight of trading practices, these guidelines aim to elevate the quality and reliability of the market, thereby attracting more robust and serious investment.

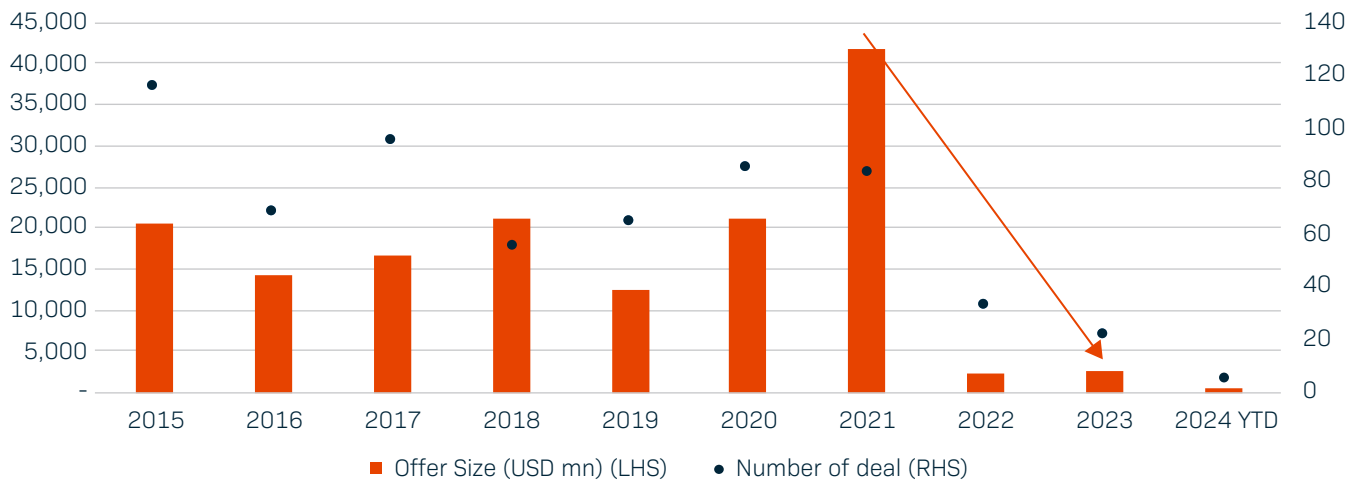
The emphasis on integrating medium to long-term capital is particularly crucial. It aims to shift the focus from short-term speculative gains to longer-term, stable investments, fostering a healthier financial ecosystem. This would not only support local economic growth but also enhance their competitive edge internationally, drawing in more foreign fund flow and investment.

HK IPO DATA

HONG KONG IPO



HONG KONG SECONDARY OFFERING



These two graphs show a noticeable trend in both initial public offerings (IPOs) and secondary offerings in Hong Kong, particularly highlighting the differences in market activity before and after 2020. From 2015 through 2020, there was a general upward trend for the size of IPOs, peaking in 2020.

However, post-2020, there has been a significant decline in both the number of deals and the capital raised through these offerings. This downward trajectory could be attributed to various factors such as COVID impact, regulatory changes, market volatility, geopolitical tensions and shifts in investor confidence. The year 2020 appears as a turning point where the market dynamics shifted, leading to reduced activity and smaller deal sizes in subsequent years, which continued into 2023 and 2024 year-to-date. This change reflects broader economic conditions and possibly a recalibration of investment strategies within the region.

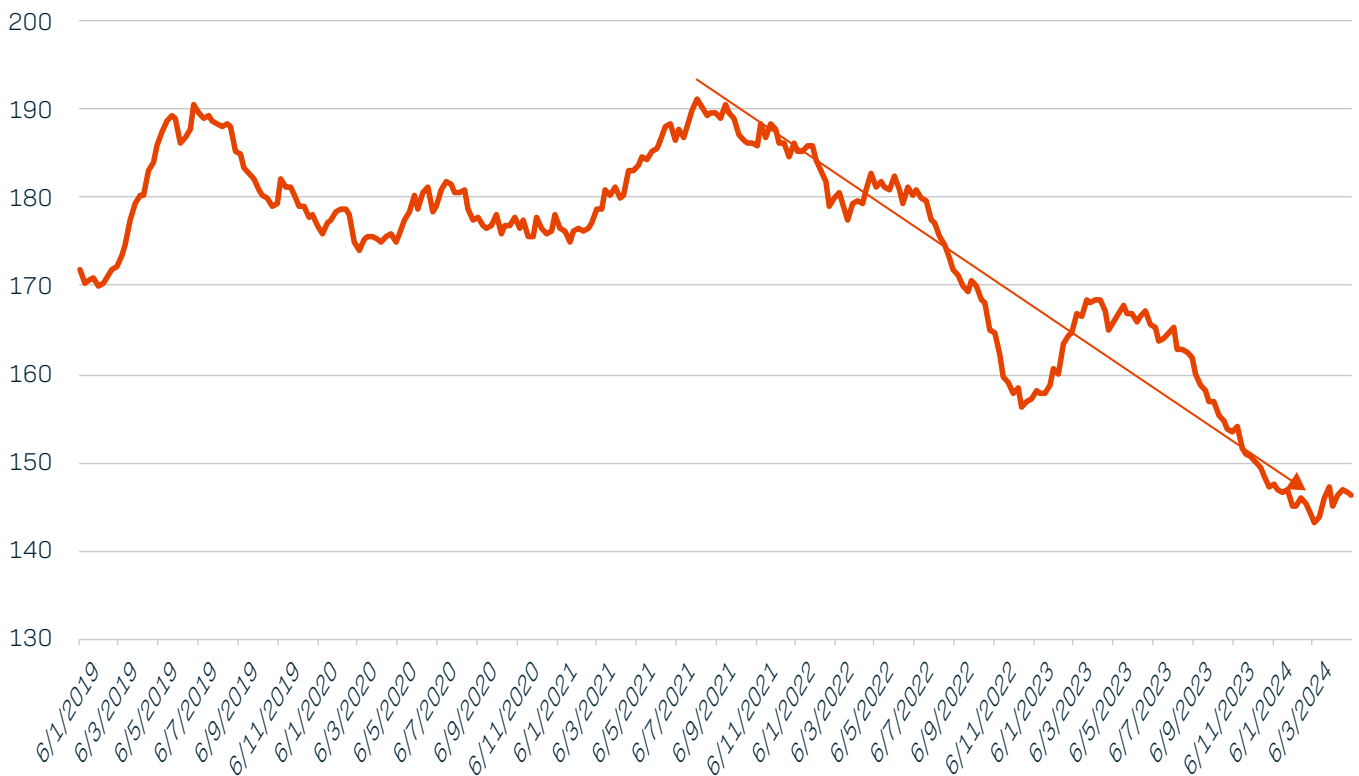
STOCK STAMP DUTY CUT

In a strategic move to enhance market liquidity and make the Hong Kong stock market more attractive to both domestic and international investors, the government has implemented key financial measures. These include a reduction in trading fees and a significant cut in stamp duty on transactions, now lowered to 0.1% per side from 0.13% previously. These initiatives are designed to reduce the cost of trading, thereby encouraging higher trading volumes and greater participation from a broader range of investors. By making these changes, the government aims to bolster the financial market's competitiveness and ensure it remains a leading global financial hub.

REMOVAL OF HONG KONG PROPERTY STAMP DUTY

In a significant move aimed at rejuvenating the Hong Kong property market, the Financial Secretary of the HKSAR announced in the 2024/25 Budget that all additional stamp duties related to residential property transactions would be removed effective from 28 February 2024. This includes the Special Stamp Duty (SSD), Buyer's Stamp Duty (BSD), and New Residential Stamp Duty (NRSD), which were originally designed to curb property speculation and stabilize housing prices. By eliminating these duties, the government hopes to lower the entry barriers for buyers, thus increasing demand and potentially driving up property prices in the short term.

CENTALINE PROPERTY CENTA-CITY LEADING INDEX »



This tax relief is expected to stimulate both the primary and secondary housing markets, which have seen a downturn in recent years. With the removal of these duties, the market could see an influx of both local and foreign buyers, including those from mainland China, who may now find Hong Kong's residential properties more attractive investments. The overall aim of these measures is to boost market activity and help the property market recover from its prolonged slump.

BAD WEATHER ARRANGEMENT

In response to the challenges posed by severe weather events, the Hong Kong Stock Exchange (HKEX) has initiated consultations and plans to keep trading sessions operational during such conditions. This initiative aims to maintain market continuity and stability, even in the face of disruptions typically caused by adverse weather. By implementing robust technological and operational frameworks, HKEX ensures that trading activities can continue safely and efficiently, minimizing financial and operational risks. This proactive approach underscores HKEX's commitment to upholding a resilient financial infrastructure that can withstand various environmental challenges, thereby supporting traders and investors who rely on consistent market access.

Over the past five years, the Hong Kong capital market has experienced a rollercoaster of highs and lows, influenced by a complex interplay of internal and external factors. The period from 2020 to 2024 has been particularly notable for its dramatic shifts, driven by regulatory measures, global economic challenges and strategic policy implementations. Despite these challenges, the market has shown resilience and signs of recovery, particularly in 2024, spurred by favorable policies and increasing foreign investment interests. This report has highlighted the critical events and trends that investors might consider as they navigate the future landscape of Hong Kong's financial market with the region continuing to adapt and evolve.

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