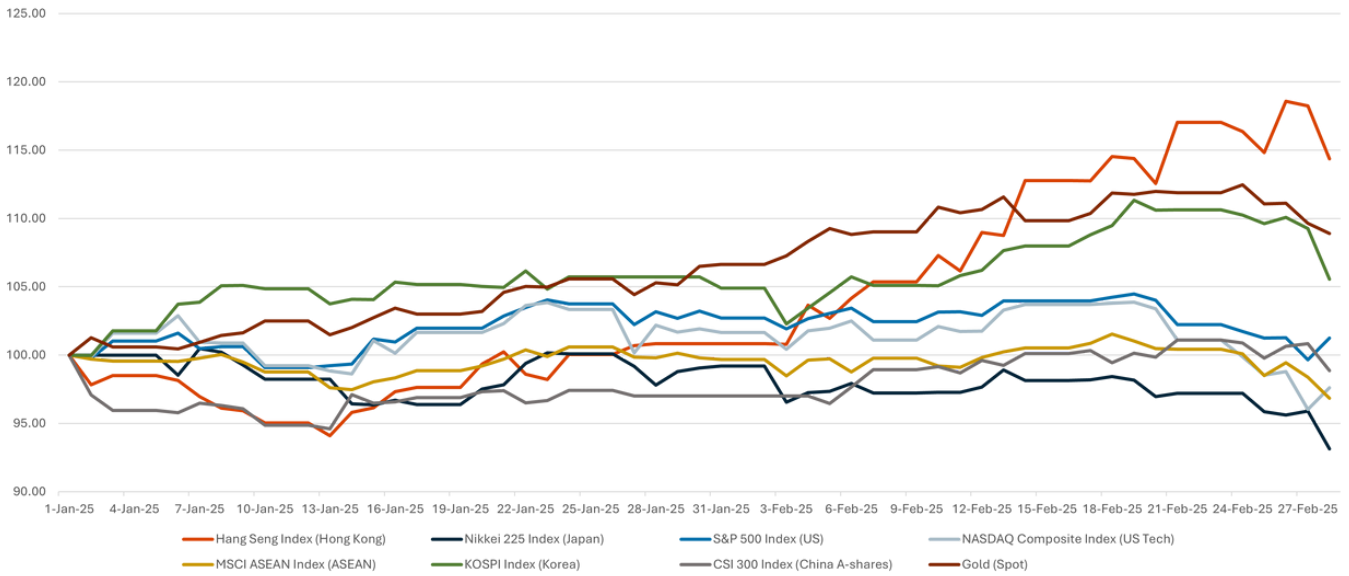


# CHINA'S FINAL AI ARRIVAL: DEEPSEEK IGNITES MARKET RALLY AND RE-RATING

## EXECUTIVE SUMMARY

- **AI Catalyst:** The AI revolution, driven by innovations like DeepSeek, is rapidly transforming China's tech landscape and re-rating its stock markets.
- **DeepSeek:** DeepSeek's breakthrough AI model, developed with a resource-efficient training process, is closing the technological gap with established US AI leaders.
- **Market Rally:** Hang Seng Index has surged 14% year-to-date as of February 28, 2025, significantly outpacing major global indices such as the S&P 500, Nasdaq and Nikkei 225.
- **Alibaba (9988 HK):** Strategic upgrades, including enhanced AI models and key partnerships with Apple, are fueling market optimism.
- **Tencent (700 HK):** Tencent's integration of DeepSeek's AI into its Weixin app is poised to provide over a billion users with cutting-edge search and communication capabilities.
- **BYD (1211 HK):** BYD's launch of its advanced "God's Eye" driver-assistance system is set to boost its competitive edge and drive significant growth in the EV market.
- **Xiaomi (1810 HK):** Xiaomi continues to strengthen its market position by developing competitively priced EVs.
- **Government Meeting:** A high-level meeting led by President Xi with top technology executives underscores the government's robust support for private sectors.

**2025 YEAR TO DATE ASSET PRICE PERFORMANCE (%) (REBASED)**



As of February 28, 2025, China's stock market has delivered an impressive year-to-date performance, with the Hang Seng Index surging by 14%, outperforming all other major stock indices, S&P 500 (1%), Nasdaq (-2%) and Nikkei 225 (-7%). This remarkable rally can be largely attributed to the booming AI sector, which has now become the catalyst for market optimism in China. While the AI-driven surge was a key factor in powering US equity markets during 2023-2024, the momentum has finally reached the Chinese markets in the beginning of 2025, sparking a renewed wave of investor confidence and repositioning the China Internet and technology stocks to be re-rated.

**HANG SENG INDEX**



## DEEPSEEK

In January 2025, a Chinese breakthrough artificial intelligence system, DeepSeek, that has quickly garnered international attention. DeepSeek was built by a leading Chinese hedge fund, High-Flyer, in 2023. Engineered with cutting-edge architecture and refined training methodologies, DeepSeek has achieved benchmark scores that not only rival but in some cases exceed those of established US AI models such as those developed by OpenAI. Its performance in natural language understanding, problem-solving and data synthesis has set new industry standards, highlighting the remarkable strides made by Chinese innovators in closing the technological gap with their Western counterparts.

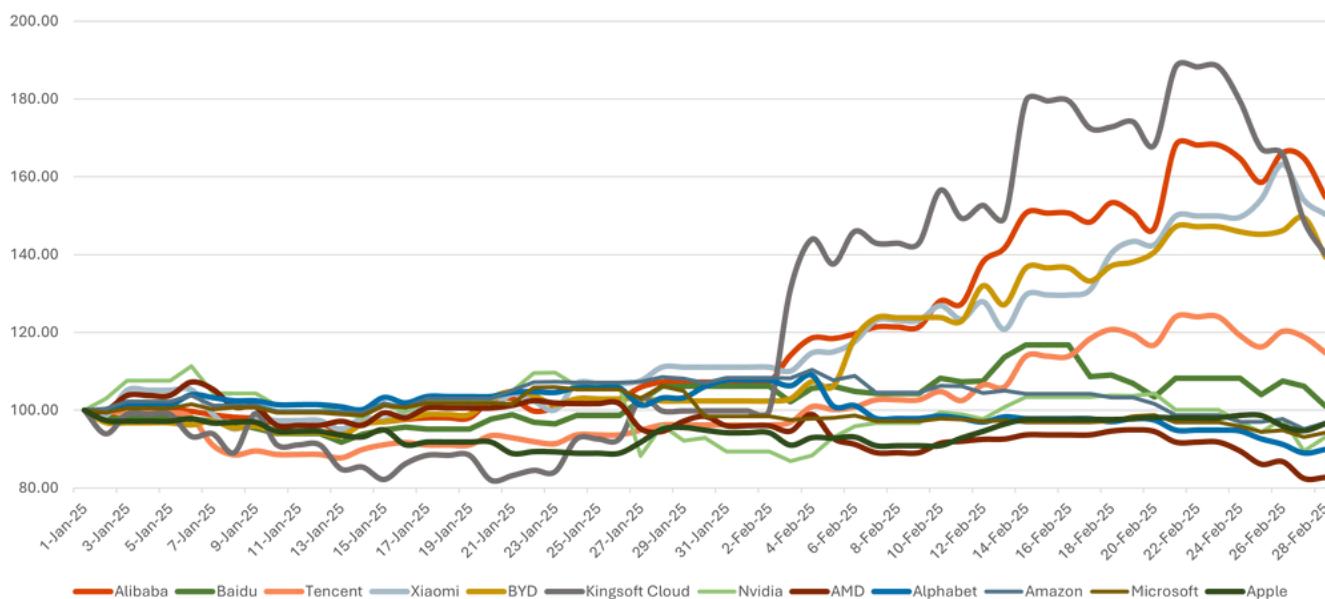
DeepSeek's R1 model is developed using an innovative training framework that sharply contrasts with traditional methods seen in competitors such as OpenAI, reducing both the required training duration and hardware investment. This efficiency is achieved by applying large-scale reinforcement learning focused on reasoning challenges, combined with a custom-designed rule-based reward system that enhances the model's ability to learn complex patterns, rather than relying on standard neural reward models. Furthermore, advanced distillation techniques compress the model's knowledge into much smaller versions, some as compact as 1.5 billion parameters, while naturally emerging reasoning capabilities develop without explicit programming. This holistic approach not only cuts costs and resource use but also paves the way toward achieving artificial general intelligence. (Source: Tech Target)

The launch of DeepSeek represents a pivotal moment in the evolution of artificial intelligence, signaling a significant realignment of global technological leadership. As this powerful system begins to influence other industries ranging from finance to manufacturing, it has sparked renewed interest among investors, policymakers and research institutions worldwide. The success of DeepSeek is a clear reminder that innovation is increasingly a global endeavor, with China emerging as a leading player capable of competing and redefining the benchmarks set by traditional US leaders in AI technology.

## CHINESE STOCK MARKETS

This development proved to be a major catalyst for Chinese equities, prompting a broad re-rating that is especially visible in the internet and technology sectors. As of February 28, 2025, notable names such as Tencent (700 HK), Alibaba (9988 HK), Xiaomi (1810 HK), BYD (1211 HK) and Kingsoft Cloud (3896 HK) have all posted robust share price gains, clearly surpassing their US peers like Nvidia (NVDA US), AMD (AMD US), Microsoft (MSFT US), Alphabet (GOOGL US), Amazon (AMZN US) and Apple (AAPL US).

2025 YEAR TO DATE STOCK PRICE PERFORMANCE (%) (REBASED)



## COMPANIES

### ALIBABA (9988 HK)

ALIBABA



Shortly after DeepSeek's debut, on January 29, 2025, Alibaba unveiled an enhanced version of its Qwen 2.5 AI model, asserting that it now outperforms DeepSeek-V3 on several critical benchmarks.

Building on this momentum, on February 13, 2025, Alibaba announced a strategic collaboration with Apple to integrate its advanced AI capabilities into iPhone services in China. This partnership is designed to enrich the user experience by providing smarter, more responsive AI features, a key selling point for the latest smartphone models, and is expected to drive increased iPhone sales by appealing to consumers who now view robust AI functionality as essential. (Source: Reuters)

### TENCENT (700 HK)

TENCENT



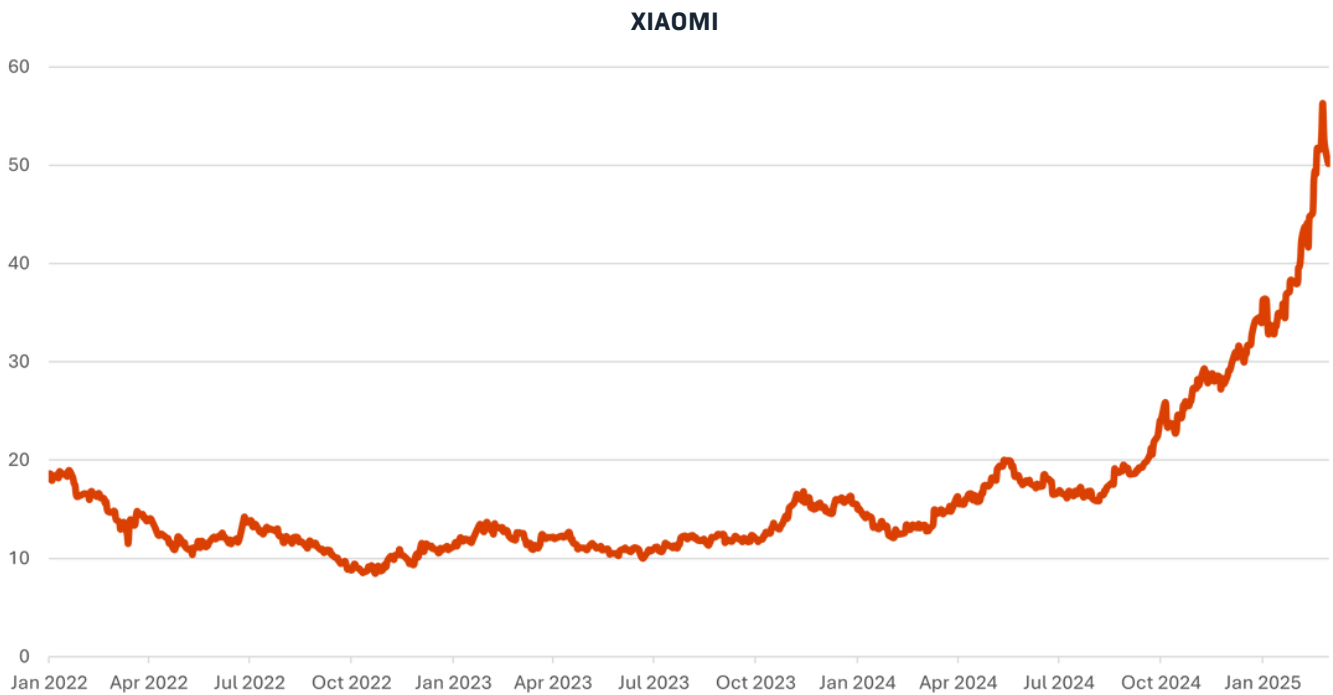
On February 16, 2025, Tencent announced that its flagship messaging app, Weixin, now integrates DeepSeek-powered AI search, enabling a transformative upgrade in user experience. This enhancement allows over a billion users worldwide to effortlessly tap into advanced AI capabilities for real-time searching, chatting and information discovery. The seamless integration not only simplifies access to AI technology but also strengthens digital interactions, making it easier for users to obtain accurate responses and personalized content.

## BYD (1211 HK)



China's rapid advancements in AI are now reshaping valuations across its electric vehicle sector. On February 11, 2025, BYD unveiled its new "God's Eye" driver-assistance system, a sophisticated three-tier autonomous driving platform integrated into most of its models. This innovative system enables features such as automated highway ramp entry and exit, precise lane keeping, adaptive cruise control, autonomous lane changes and obstacle avoidance. Market analysts anticipate that BYD's enhanced autonomous capabilities will not only boost its competitive edge but also drive significant sales momentum, thereby positively re-rating the entire EV industry in China.

**XIAOMI (1810 HK)**



The surge in AI technology is driving a broader transformation across China's tech landscape, notably enhancing the smartphone and electric vehicle sectors. Xiaomi, a frontrunner in smartphone manufacturing, is leveraging this momentum by integrating advanced AI features into its devices to deliver more intelligent and personalized user experiences.

Additionally, Xiaomi expanded its portfolio last year with the launch of a competitively priced EV equipped with autonomous driving functions, further fueling the intense rivalry in China's rapidly evolving EV market. This convergence of AI with consumer electronics and automotive technology reinforces Xiaomi's market leadership in the technology industry.

**KINGSOFT CLOUD (3896 HK)**



Kingsoft (3896 HK) stands as one of China's foremost software and cloud service providers. As AI technology gains momentum, fueled by breakthroughs like DeepSeek that enable more cost-effective applications, the market is set to experience a significant uptick in demand for AI-driven solutions. This evolution is expected to drive robust growth in cloud and data center usage, positioning Kingsoft to capture new opportunities and benefit substantially from the expanding digital infrastructure landscape.

**BAIDU (9888 HK)**



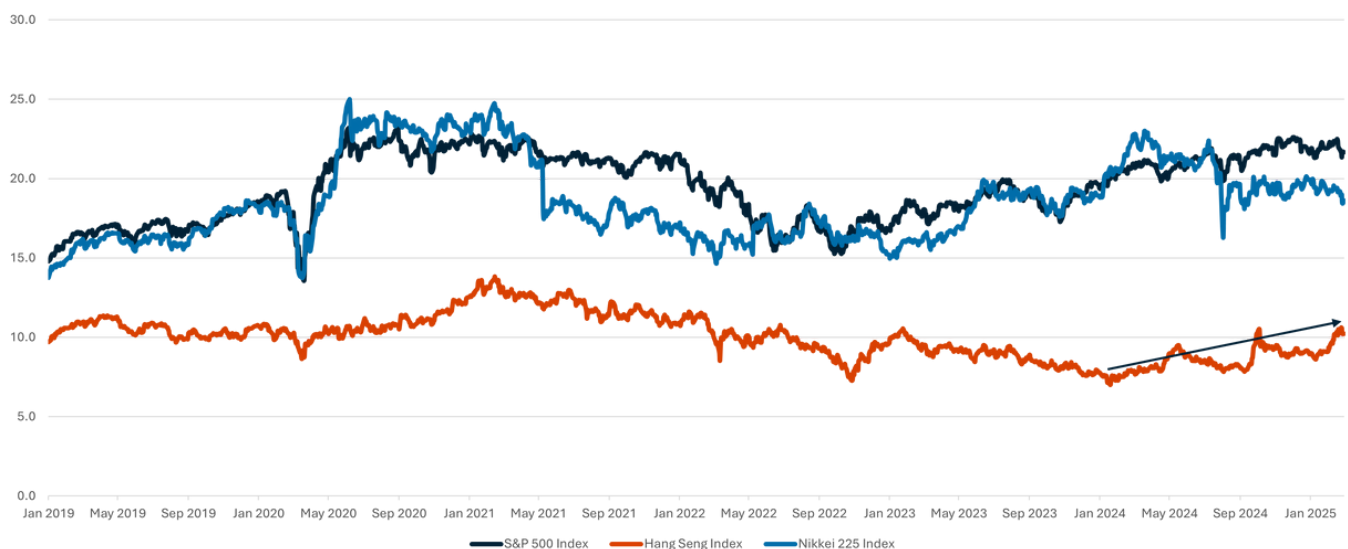
Baidu recently announced an ambitious upgrade to its search engine by integrating both DeepSeek's advanced AI capabilities and its own Ernie large language model. This dual integration is designed to deliver more intelligent, context-aware search results, enhancing not only speed but also accuracy by leveraging the complementary strengths of both platforms. By harnessing DeepSeek's resource-efficient algorithms alongside Ernie's sophisticated natural language understanding, Baidu aims to provide users with richer, more personalized content and deeper insights in real time.

## MACRO NEWS

Beyond the company-specific headlines, the macroeconomic landscape and policy environment have received a significant boost following DeepSeek's launch. On February 17, President Xi convened a high-level meeting with some of China's most influential technology leaders, including Jack Ma of Alibaba, Ren Zhengfei of Huawei, Wang Chuanfu of BYD, Lei Jun of Xiaomi and Liang Wenfeng of DeepSeek. This gathering is widely seen as a strong affirmation from the Chinese government of its commitment to supporting privately owned firms, which are considered pivotal for driving both economic growth and technological innovation. Investors and market observers interpret the meeting as a clear signal that the Chinese government is ready to back the nation's tech sector.

## ATTRACTIVE VALUATION

MAJOR INDEX VALUATIONS OVER TIME: HANG SENG VS NIKKEI VS S&P 500



Despite this year's rally, the Hang Seng Index remains at approximately 11x 2025 forward earnings, well below the S&P 500's 22x and the Nikkei 225's 19x. Global investors only began reassessing Chinese equities in January 2024, when the Hang Seng stood at a historic low of around 7x. Momentum truly shifted in January 2025 with the debut of DeepSeek-R1, showcasing China's accelerating AI prowess and reviving confidence in the fundamentals of its tech sector.

As valuations climb, the main question is how far global investors are willing to close the gap between the Hang Seng Index and its higher-valued US peers, especially given the traditionally low multiples assigned to Chinese markets.



## SUMMARY

China's AI revolution, spearheaded by breakthroughs like DeepSeek, has not only redefined the nation's technological landscape but also spurred a broad re-rating of its stock markets. The surge in AI innovation, characterized by cost-effective, high-performance models and strategic integrations by tech giants such as Alibaba, Tencent, Xiaomi and BYD, has driven the Hang Seng Index to outpace global peers significantly. Meanwhile, the government's robust policy support, exemplified by President Xi's high-profile meeting with top industry leaders, underscores a strong commitment to fostering private sector innovation. This convergence of technological advancement, market optimism and Chinese government backing is reshaping sectors from AI, Internet, smartphones and cloud services to electric vehicles, positioning China stock markets as attractive investment opportunities in 2025.

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