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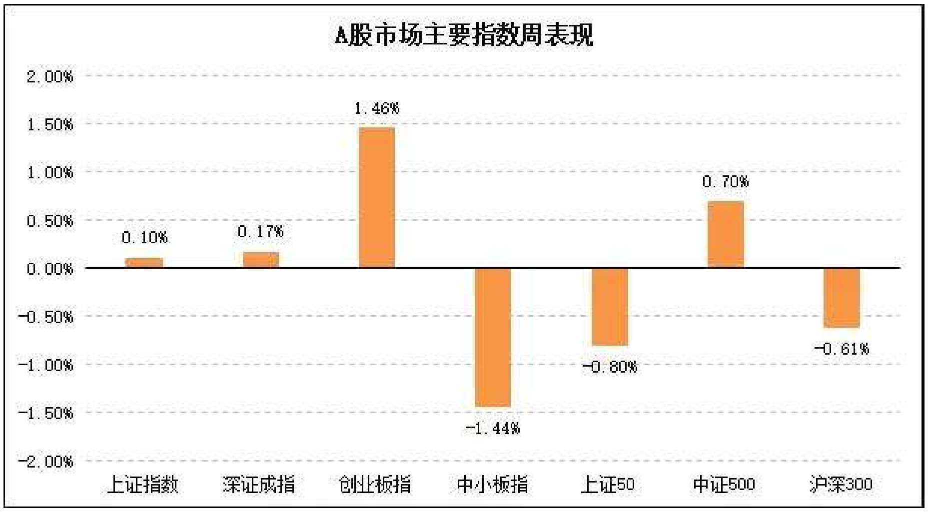
Rosefinch Weekly

A-share Shrugs off Omicron; Focus on Favorable Sectoral Outlook

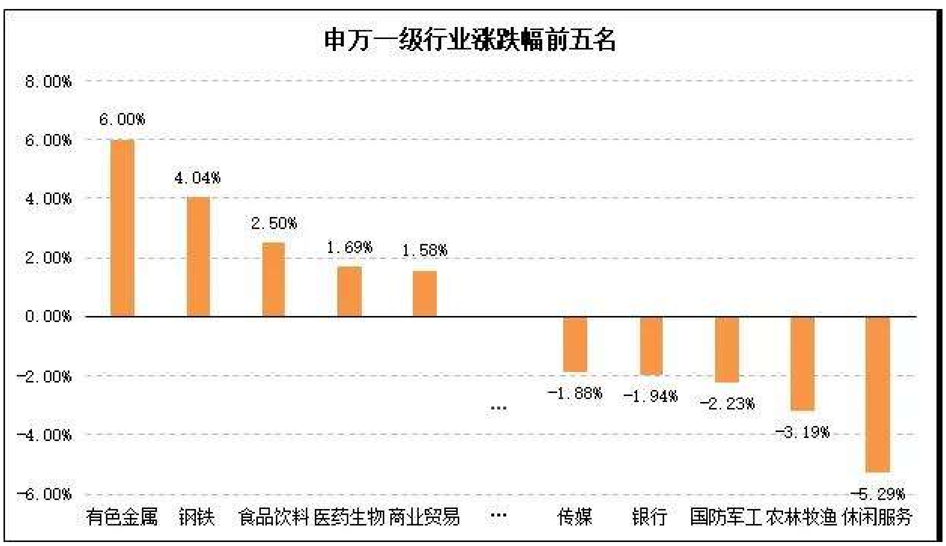
1. Market Review

For the last week: SSE was +0.10%, SZI was +0.17%, GEM was 1.46%, SSE50 was -0.80%, CSI300 was -0.61%, and CSI500 was +0.70%.



Source: Wind, Rosefinch.

Amongst the ShenWan Primary industries, 15 out of 28 rose with non-ferrous metal, steel, food & beverages, biopharmaceutical, and commercial trade leading the way.



Source: Wind, Rosefinch

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Market activity gained slightly. Last week Northbound was net +5.7 billion RMB, and Southbound net -0.24 billion HKD.

Source: Wind, Rosefinch. Blue is cumulative Northbound flow and unit is 100 million RMB; yellow is cumulative Southbound flow and unit is in 100 million HKD.

2. Market Outlook

There were little data last week aside from the Oct industrial profits, which showed a solid +24.6% yoy at 818.7 billion RMB. This was higher than September's +16.3% yoy. There was notable dispersion in performances across different enterprise: the high-tech industry like electronics maintained high profit growth while mid- to down- stream traditional enterprises had weaker profits. The soft end-demand is still affecting the profit splits among the different stages of the industrial value chain, and the growth in industrial profits doesn't signal robust economic growth yet.

On policy side, we noted Vice Premier LIU He published an editorial in People's Daily titled "Necessity of Realizing High-Quality Growth". High quality development is a requirement of China's new development phase, with quality the more important factor vs quantity in a more constraint environment. From macro policy perspective, the key is stability which can be delivered via combination of cross-cycle and countercyclical policies. The macro goal is to reduce volatility in economic growth, while maintaining the baseline of preventing systematic risk. The subsequent macro policy will avoid aggressive stimulus. maintain stable economic growth, and emphasis structural policy support for carbon-neutral initiatives and technological innovations.

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The real estate industry policy is seen as a supply-side issue, and we probably won't see it being used as economic stimulant via excessive policy loosening. There are some recent limited loosenings in real estate policy, such as 5% increase of down-payment fund utilization in Chengdu, some increase in funding by state-backed developers, less stringent requirements for 3rd round of land auction, etc. The private-owned developers still face a tough operating environment where financial institutions remaining cautious on their corporate bonds. There's continued asset liquidation by real estate companies, with many sounding battle alerts to motivate staff. We see many signs that indicate the real estate sector is still in downward trend, albeit as a slightly slower pace. It's a long way from the light at end of the tunnel.

Last week's A-share market saw some market adjustments in decent volume. Cyclical and new energy sectors took turns leading the way, though without huge momentum. Cyclical sector benefited from expected policy loosening for real estate sector, resumption of steel manufacturing, and rebounding from previous drops. We see this rebound as limited both in magnitude and duration, especially in light of the long-term downward trend in real estate sector. Main focus should remain on the favorable sectors with strong outlooks. The policy still favors real economy and not the real estate sector. The cyclical sector is still digesting the policy impacts and does not have clear allocation value. Meanwhile, the emergence of Omicron variant accelerated market expectation of policy support. China's pandemic policy and successful track record alleviate A-share's anxiety on the new pandemic wave and will likely cause A-share to outperformance oversea market in this round.

Commodity market sentiment has rebounded somewhat, though the trend hasn't reversed. Market is still reeling from the thermal coal price collapse, with expectation of year end policy support to provide bottom in pricing. Oil price volatility remains high while US is calling for release of strategic oil reserve. The Omicron introduces new uncertainties led to reduction in future demand and the 10% drop in oil price. We still need to see more data about the impact of Omicron, though the panic driven selloff may offer some opportunities.

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