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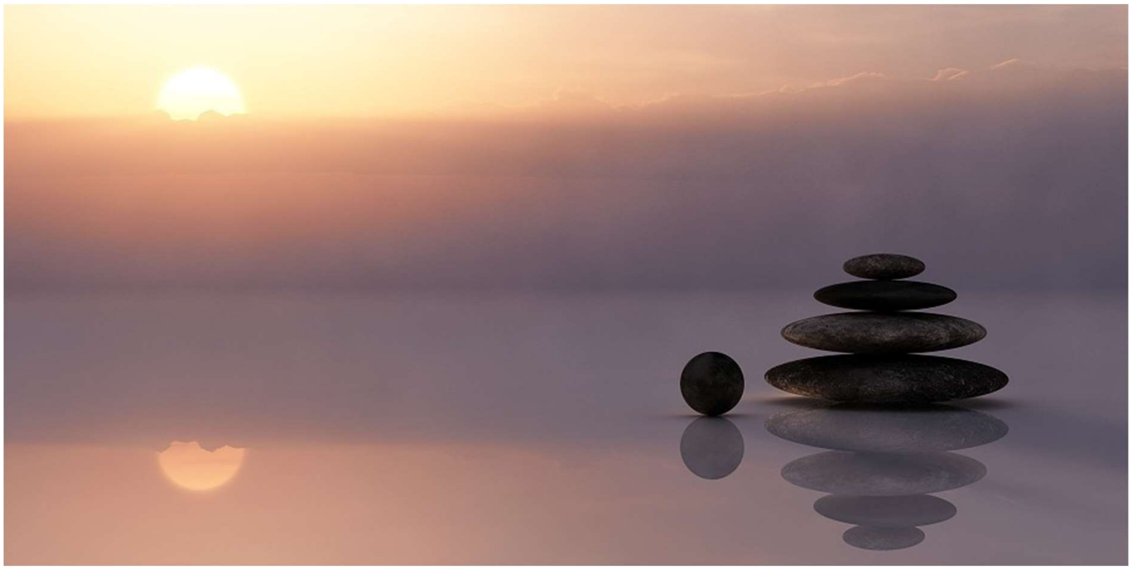
Rosefinch Research | 2022 Series # 14

Market Usually Bottoms Before the Economy



Last week China's A-share had a V-shaped rebound. At start of the week, news of pandemic spreading through Beijing caused panic with strong selling wave hitting the market. In fact, we are starting to see signs of market bottoming out. From the relative pricing of stock to fixed income market, the stock risk premium is approaching the extreme level last reached in Mar 2020. Market turnover is also nearing historical lows, with daily volume under 800 billion RMB. This reflects investors' sidelined posture, indicating market is now at extreme oversold level. In the 2nd half of last week, as Shanghai pandemic news improved, Beijing situation remained under control, and key government policy meetings took place, market rebounded quickly and finished slightly up for the week. **Looking back, the time of worst market sentiment is often the market bottom.**

There were a number of high-level senior government meetings last week that emphasized economic stability. Monday's working meeting discussed "steady employment, steady pricing, and steady supply" to stabilize economic fundamentals. Tuesday's central government finance committee discussed comprehensive strengthening of infrastructure construction. Wednesday's state council meeting focused on creating steady employment and relieving supply chain blocking points. The highlight of the week was on Friday where the Politburo gave market a shot on the arm regarding the state of economic growth. **The most proactive signal released at the Politburo meeting was to fully commit to the 5.5% growth rate**, thus removed market's worry of lowering the target growth rate. Even though pressure is increasing, and the task is challenging, the steady growth target was not revised. The steady growth is also a foundation for steady employment.

We summarized some key takeaways from the Politburo meetings:

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1. On the pandemic front, there's no wavering of the dynamic zero policy. We'd expect continued strict adherence to the policy across China in both national and regional levels. At the same time, the meeting also highlighted the need to reduce pandemic impact on the economy, to maintain normal manufacturing activities, and to avoid unnecessary economic shocks from over-stringent pandemic policy implementations. **Going forward then, we'd expect strict policy overall, but with some protection for manufacturing or supply chain management.** It's likely that the extreme lockdowns to prevent infection will become less frequent.

2. **The Politburo affirmed the annual growth rate target of 5.5%.** Previously the market had some doubt on the feasibility of reaching the target. While the pandemic has caused temporary shocks, the government remains committed to maintain stability. At the same time, there may be some flexibility on the growth target, though the priority is still to aim for economic growth.

3. On overall policy framework, the focus is on implementing existing policy initiatives first, such as tax and fee reduction. The government will increase the launching of new initiatives and the magnitude of such supportive measures in order to achieve its counter-cyclical effects and change market's pessimistic expectations. At the same time, the government is cautious to not over-stimulate which will cause a whole series of other problems down the line.

4. The core of steady growth is to stabilize key entities, especially those businesses impacted by the pandemic, the SME, and self-employed businesses. Because the current employment pressure is high, we must support the hiring entities, create sufficient employment opportunities, in order to offset the pandemic impacts. By quicken the pace of tax rebate and fee reductions, and increase financial support for SME, the government will create a more supportive operating environment for SME. We may see more structural monetary policy initiatives to support such approaches.

5. **Fiscal policy remains the key engine for macro policy support.** Two key focus areas are ensuring social well-being, and starting infrastructure construction. Politburo confirmed the importance of infrastructure spending, including digital technology, industrial upgrade, supply chain enhancement, and digital network build out for transportation, electricity, and hydropower. Overall, we expect infrastructure construction to have steady funding and make a more substantial impact going forward.

6. The politburo mentioned steady pricing with focus on increasing energy and agricultural supplies. As the emphasis is on expanding demand, the monetary policy is unlikely to be overly tight. We expect the monetary policy to be supportive in nature, not with large loosening, but with more effective refinancing policy tools.

7. There's still risk associated with real estate sector, so politburo again cautioned on avoiding excessive rise in real estate price or too much leverage in real estate financing. Given the current weak environment for real estate sector, the government has endorsed the rationale to support steady real estate market via localized looser policies. In addition, there was discussion of systematic framework to avoid developer depleting liquidity and avoid excessive regulation that damage the project entities. Overall, we see the Politburo taking a softer tone on the margin towards the real estate market. **We have reached the low point of regulatory**

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restrictions for real estate market, with some hope of more supportive policies ahead.

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