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Rosefinch Research | 2023 Series # 2

The Road Ahead

The year 2022 is called a Macro-Year where macro factors dominated headlines. Whether it's the surprised ongoing Russia-Ukraine War, the worse than expected European and US inflation data, the aggressive FED hiking cycle, or the fast-changing pandemic situation, these factors have impacted both supply and demand sides of the market dynamics. A-share markets also went through two-rounds of roller-coaster rides: 1Q tanking, 2Q rebound, 3Q drop, and 4Q recovery. Whoever invested in the market were pulled left and right by the fear and greed. Now that we're in 2023, the inflation and FED expectations are shifting, and Chinese economy is finally opening up again. The pivotal year may have finally arrived. How will 2023 evolve? Will macro factors still "shock and awe" the market? Which sectors or industries will be the market favorites? Will the new technology bring up transformational changes? The Rosefinch team has put together 8 key questions and our thoughts below.

1. How do you see the 2023 asset performances?

From asset allocation perspective, the 2023 macro environment is favorable for the equity products. On one hand, the equity/bond relative value reflects market's risk preferences, where extreme relative values often signal subsequent reversions. The current relative valuation favors a future rebound of equity market relative to bond market. On the other hand, the fundamentals have a more likely upside as global financial situation stabilizes. Within the equity market, the high-tech manufacturing sector is strongly favored by both government policy support and their own respective growth trends. Rosefinch has been focusing on the advanced manufacturing sector ever since our founding 15 years ago, with 3 full research teams

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dedicated to some key industries: team #1 on hydrogen, energy storage, new material; team #2 on automobile and aerospace; team #3 on new energy equipment.

2. How will the stock market perform in 2023?

After a year of volatile corrections, A-share is at a risk recovery stage with the market low behind us. Chinese manufacturing industries remain competitive in global markets and will support a strong RMB which in turn allows a more independent monetary policy. In 2023, we expect Chinese economy to recover and grow, which will drive up corporate profitability steadily. For the Chinese equity market, we may see a continuation of the slow bull market that started back in end of 2018.

For the government policy makers, they'll likely refrain from excessive stimulus for real estate or infrastructure sectors just to push up short-term growth rates. Instead, the government policy will likely focus on reform, promote confidence, stimulate enthusiasm, and push for high-quality economic growth. We have said previously that under China's new developmental model, the Chinese economy's cyclical volatility will decrease, with growth rates gradually slowing. In this environment, it's important to capture the structural investment opportunities presented by the slow bull market.

3. Will market liquidity be sufficient in 2023?

The overall liquidity remains ample, which will be favorable for the equity market. In 2022, US and European economies had to hike rates to combat worsening inflation. In 2023, as inflationary pressure recedes, FED has passed its most aggressive hiking phase. The 10y UST yields had peaked around 4.3%, and USD index has peaked 10% from its September peak. As China adjusts its pandemic policy and increases its economic growth expectations, RMB has appreciated which provides more flexibility for PBOC's monetary policy. According to the government's 2023 Central Economic Work Conference, the goal for the 2023 monetary policy is "the steady monetary policy should be targeted and precise, should maintain reasonable and ample liquidity, and keep broad money supply and social financing growth in line with nominal economic growth." We therefore expect 2023's China Monetary Policy to be relatively friendly for equity markets. It's worth noting that during 2022, the pandemic had negative impact on enterprise and household confidence which made their investment and consumption behaviors very cautious. This is reflected in the record high deposits at commercial banks. As stock market rallies in 2023, we may see further shifts from household savings into capital market.

4. Which industries will be key focus in 2023?

We believe the key industries are those highlighted in the 20th CCP congress that are related to high innovation and high-quality development. These include digital economy, green economy, and energy security development. Our six research teams are expanding along these areas with particular emphasis on 3060+ areas which is particularly relevant to the green economy.

5. How will the New Energy Sector play out in 2023? Will the large correction in 2022 continue?

Rosefinch believes the 2022 correct was temporary. We still favor the middle to long term potential of the New Energy sector. In 2020, the wind and solar energy generation was only 10% of total power generation, whereas this ratio is expected to go up to over 60% in future as we move towards Carbon-neutrality. As the global economy and electricity consumption grows over time, we estimate the annual installed capacity for wind or solar generation will likely increase 10 times. Even if unit costs decrease over time, it'll still be a 5 to 7 times increase in monetary terms.

6. Will the New Energy Car sectors maintain the high growth rates from the past few years?

According to data from Oct 2022, the New Energy vehicles account for over 30% of new vehicles, which is a large jump from the 5% as of 1Q2020. Given the higher base, we'll probably see a lower rate of increase in 2023. This drop in growth rate may lead to two results: first the upstream chokeholds may loosen slightly, with the supply growth overtaking demand growth, which in turn reduces costs of productions; second the industry chain competition will intensify for both the midstream and downstream segments. This puts more challenge to the comprehensive capabilities of car manufacturers, who must develop new models, increase product quality, cope with evolving technologies. Their R&D and enterprise organization will be under tremendous pressure, and only the best will survive and then thrive.

Overall, there are about 310 million vehicles in China with just over 10 million New Energy vehicles or just over 3.2%. Globally, there are about 2 billion vehicles with roughly 20 million New Energy vehicles or just 1%. This means the road for the New Energy vehicles is long with huge potential ahead still.

7. What are the 2023 opportunities during the consumption recovery?

Since end of December, various consumption-related stocks in brand consumption, logistics, or agriculture have rebounded, reflecting market's renewed confidence for consumer sector. Currently, we note that for many excellent companies, they have under-performed their average ROE for the last two years. We expect their performances to revert to the ROE over time.

8. Which 3060+ technologies may have transformational impact on the industries?

Photovoltaic industry's key future development is the industrialization of the PERC technology that crosses the 28% threshold. While we're still at early stages of technological developments, once made scalable, it'll make a transformational impact on the entire industry supply chain. HJT is also worth following since it recently achieved energy conversion rate of 26.81%. Aside from PV equipment, energy storage is also a core topic for 3060+.

By 2025, non-hydro renewable energy generation will be almost 20% of total generation. Therefore the need for over 4-hr energy storage will appear. When these renewable energy generation gets to 50% of

total, we'll see needs for longer energy storage of days or even weeks. The current electro-chemical storage models are insufficient for such long-term energy storage needs. Some promising long-term energy storage paths include hydrogen, liquid battery, and compressed air energy storages. All of these approaches have prototypes undergoing testing now. We believe hydrogen is the most promising one, as the demand for hydrogen as energy source will far exceed industrial demand.
When it comes to applications of New Energy, we may see transformational changes in the auto-driving technology. The developments in auto-driving will not only accelerate the developments of the semi-conductor chips and AI fields, but also impact robotics and eventually to all things connected. After all, to achieve true auto-driving, we must master the modeling, calculating power, and massive data analysis.

The future is exciting indeed! We at Rosefinch look forward to journey with you to a bright 2023 together.

We hope that by sharing Rosefinch's views, we add value to your day.

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