

China / HK Market Weekly

Focus turns to earnings and economic data

Last week (17-21 Oct), US stocks rebounded as quarterly earnings beat and rate hike concerns slightly eased, but the HSI dropped to the lowest since 2009. This week, investors will focus on US GDP and inflation data, and quarterly earnings in the US and China. We believe the HK stock market still lacks rerating catalysts, but we see the potential for short-term technical rebounds in the HSI.

- **Market recap:** The HSI / CSI 300 / S&P 500 were -2.3% / -2.6% / +4.7% last week (Fig. 1), as strong quarterly earnings lifted US stocks, while sentiment in China/HK markets remained cautious during the 20th CPC Congress. Consumer stocks led declines in China/HK, as the central government maintained zero-Covid policy (Fig. 3).
- **Interest rates:** US interest rate hike worries slightly eased (Fig. 10 & 11), as investors are looking forward to a reduced pace of hikes starting from Dec 2022. The US PCE inflation to be announced this Friday will be closely watched ahead of the FOMC meeting on 1-2 Nov.
- **Stock Connect:** There was a big contrast in Southbound and Northbound trading. Southbound net buying increased further, but Northbound recorded five days of net selling to end the week having the most outflows in seven months (Fig. 12-15).
- **Sentiment:** The HSI Volatility Index (VHSI) is still at a panic level around 35 (Fig. 16), which contrarian theory suggests that a short-term rebound in the HSI is possible. Short-squeeze may also trigger a rebound, as short-sell ratio on HK mainboard stayed at above 20% in the previous week (Fig. 17). By sector in HK, short-sell ratios in Consumer Discretionary, Healthcare & Energy increased.
- **Earnings:** The FY22E earnings estimates of HSI / CSI 300 / S&P 500 were revised down by -0.3% / nil / -0.5% last week (Fig. 35-38). Chinese Consumer stocks suffered bigger downward revisions. Some major financial stocks (in China) and tech giants (in the US) are going to announce quarterly earnings this week, and we may see more earnings revisions.
- **Market outlook:** We believe investors are likely to stay cautious in the next two weeks, ahead of the FOMC meeting on 1-2 Nov and the US midterm election on 8 Nov. Besides, there are further downside risks to earnings consensus as many Chinese companies will report 3Q earnings. HK stock market is cheap, but we do not see significant rerating catalysts yet. Technical rebound is possible though, given that the HSI is showing a bullish RSI Triple Divergence (Fig. 7).
- **Sector view:** Commodity stocks have been relatively strong in HK market in recent days, while Consumer & Property relatively weak (Fig. 4). We expect these trends to continue in the short term, as the speculation that the Fed may consider a slower rate hike path soon should support commodity prices, while China's adherence to zero-Covid may continue to weigh on Consumer sector.
- **Things to watch this week:**
 - Thursday: US GDP (3Q); ECB monetary policy decision
 - Friday: US PCE inflation (Sep); UK new prime minister to be unveiled
 - Chinese stocks' earnings, including many financial companies
 - US stocks' earnings, including tech giants such as Apple, Amazon, Alphabet & Microsoft

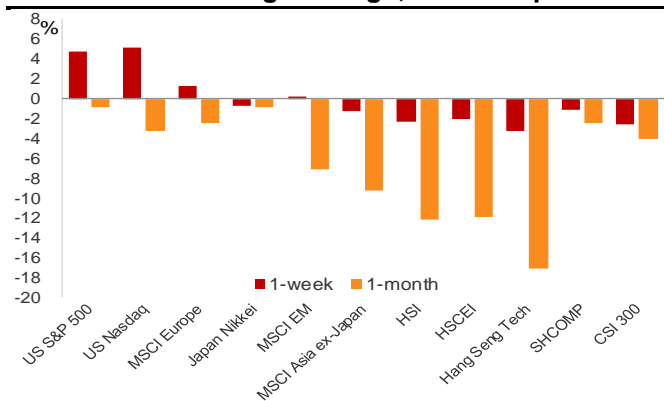
Daniel SO, CFA

(852) 3900 0857

danielso@cmbi.com.hk

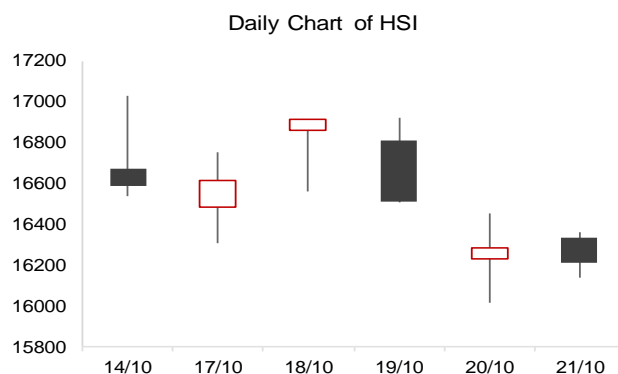
Market Recap

Figure 1: Weekly global markets' returns: US stocks rebounded on strong earnings; HK underperformed



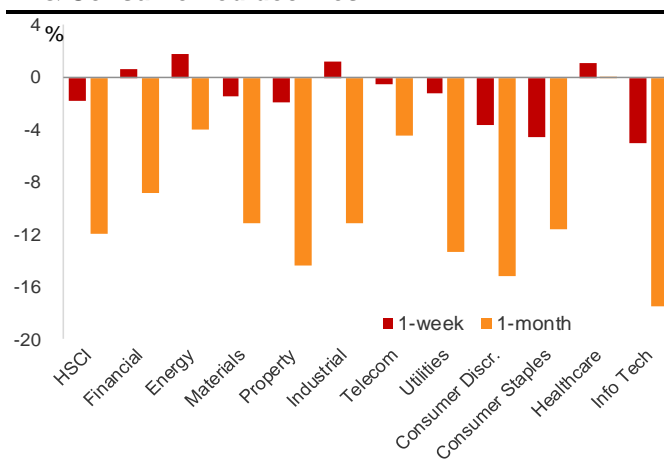
Source: Bloomberg, CMBIGM

Figure 2: HSI dropped to as low as 16010, the lowest since 2009



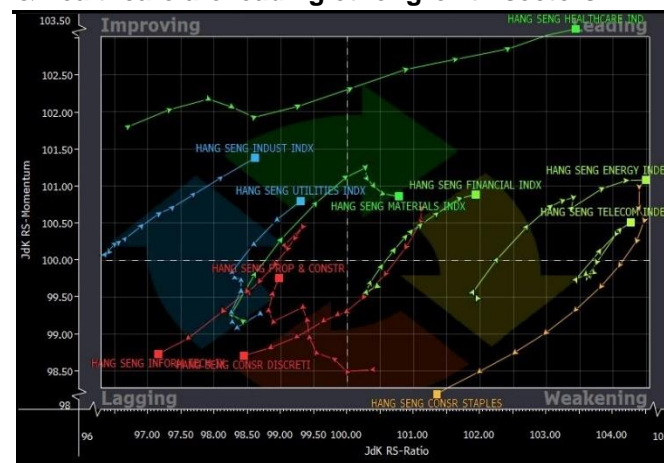
Source: Bloomberg, CMBIGM

Figure 3: Hang Seng Composite Index sectors: IT & Consumer led declines



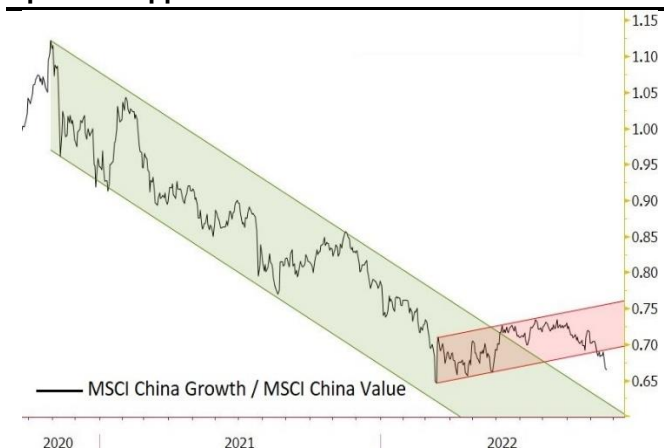
Source: Bloomberg, CMBIGM

Figure 4: Daily RRG of HSCI shows value sectors & healthcare are leading other growth sectors



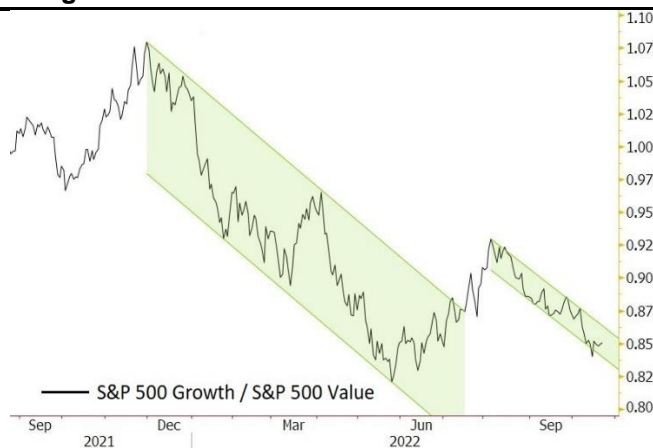
Source: Bloomberg, CMBIGM

Figure 5: China Growth stocks have confirmed weakness relative to Value stocks, breaking the uptrend support



Source: Bloomberg, CMBIGM

Figure 6: US Growth stocks formed another downward channel relative to Value stocks, as rising interest rates bode ill for Growth stocks



Source: Bloomberg, CMBIGM

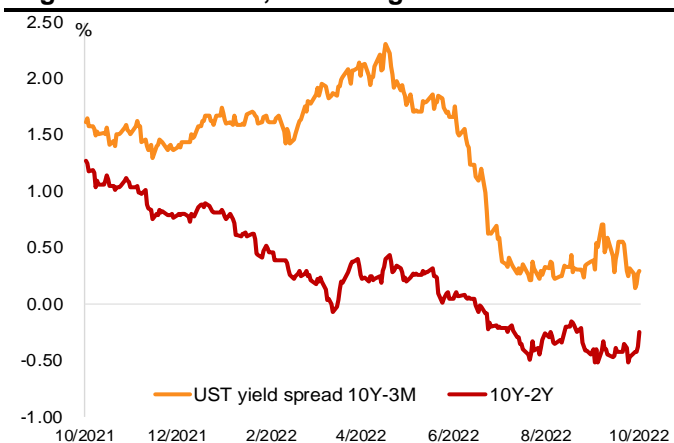
Figure 7: HSI is on the verge of technical rebound, after falling to the bottom of downward channel, and with an RSI Triple Divergence



Source: Bloomberg, CMBIGM

Fund Flows

Figure 8: UST 10-yr & 2-yr spread have been negative for months, indicating recession risks



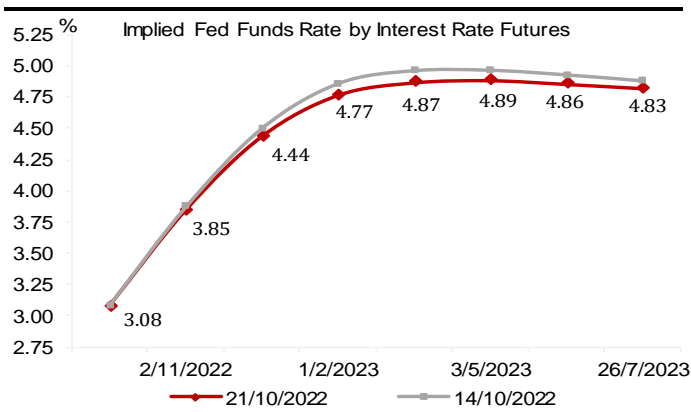
Source: Bloomberg, CMBIGM

Figure 9: USD Index still hold above short- & medium-term uptrends, a bad sign for EM flows



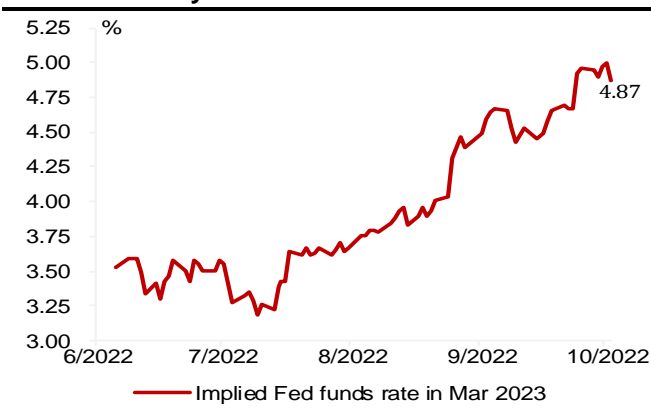
Source: Bloomberg, CMBIGM

Figure 10: Fed rate hike concerns slightly ease last week



Source: Bloomberg, CMBIGM

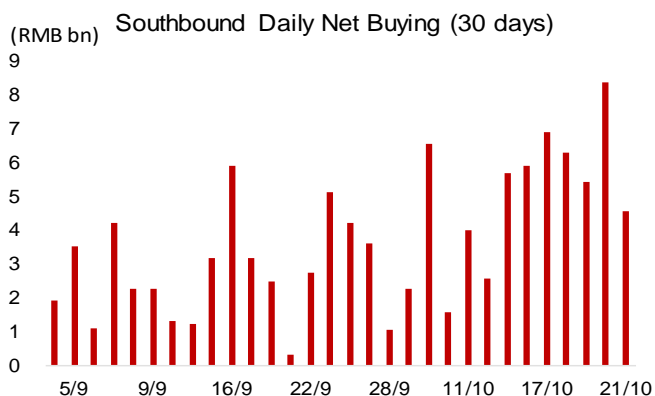
Figure 11: Implied Fed funds rate in Mar 2023 retreated mildly



Source: Bloomberg, CMBIGM

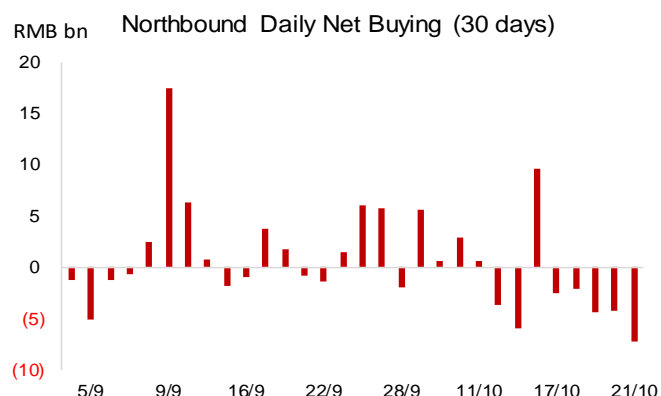
SH/SZ-HK Stock Connect

Figure 12: Southbound inflows rising in recent weeks



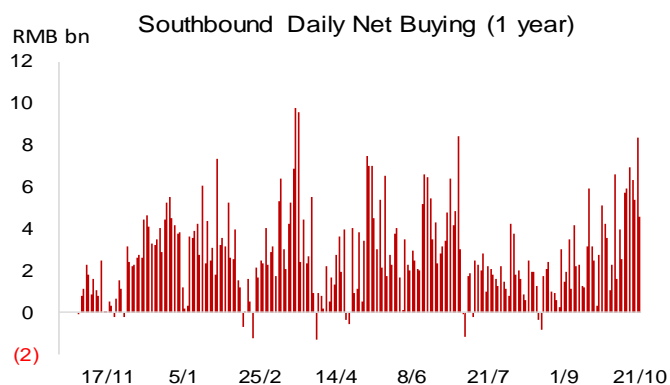
Source: Bloomberg, CMBIGM

Figure 13: Northbound net inflows were negative



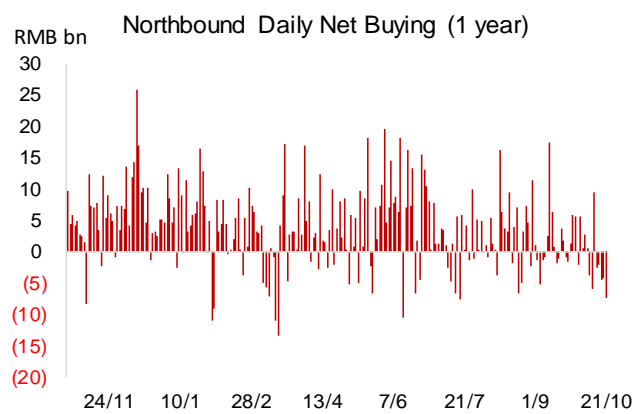
Source: Bloomberg, CMBIGM

Figure 14: Southbound net buying rebounding since Sep



Source: Bloomberg, CMBIGM

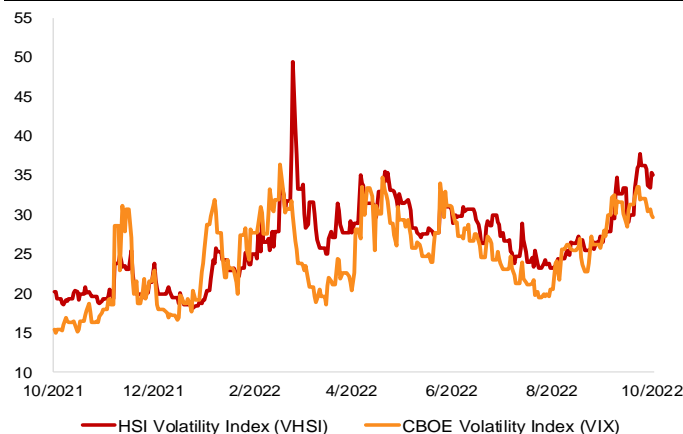
Figure 15: Northbound inflows shrinking



Source: Bloomberg, CMBIGM

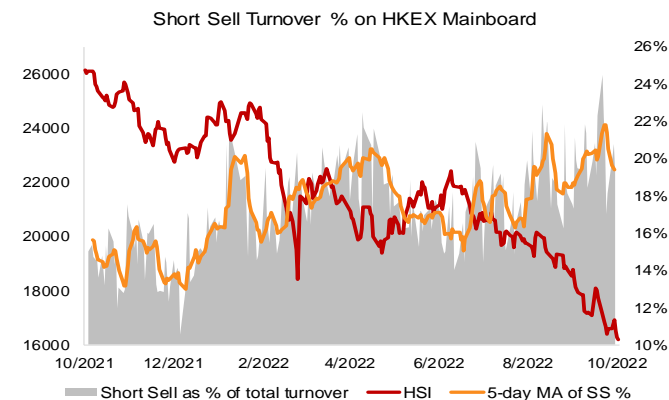
Sentiments

Figure 16: "Fear Index" VHSI is still elevated at 35



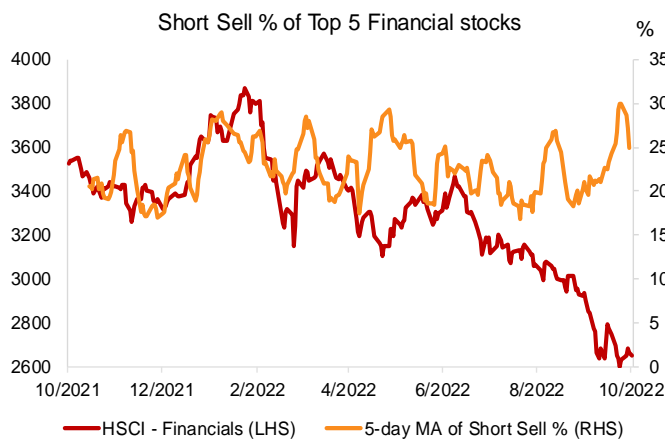
Source: Bloomberg, CMBIGM

Figure 17: Short sell % on HK mainboard still at elevated levels around 20%



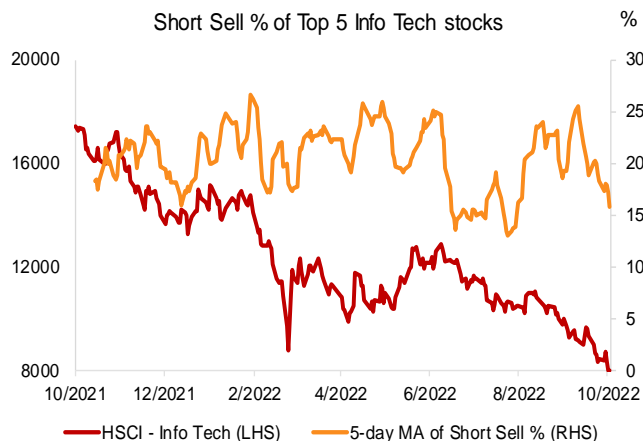
Source: Bloomberg, CMBIGM

Figure 18: Short sell % in HK - Financials



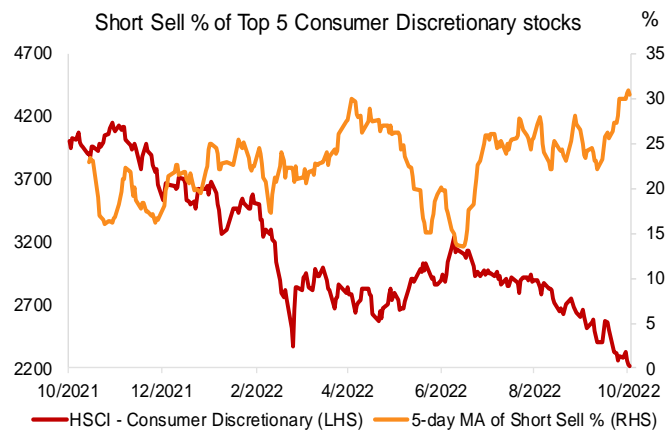
Source: Bloomberg, CMBIGM

Figure 19: Short sell % in HK – Info Tech



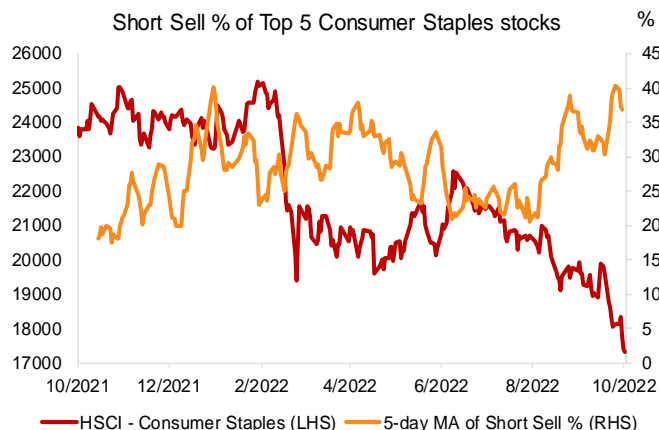
Source: Bloomberg, CMBIGM

Figure 20: Short sell % in HK – Consumer Discretion.



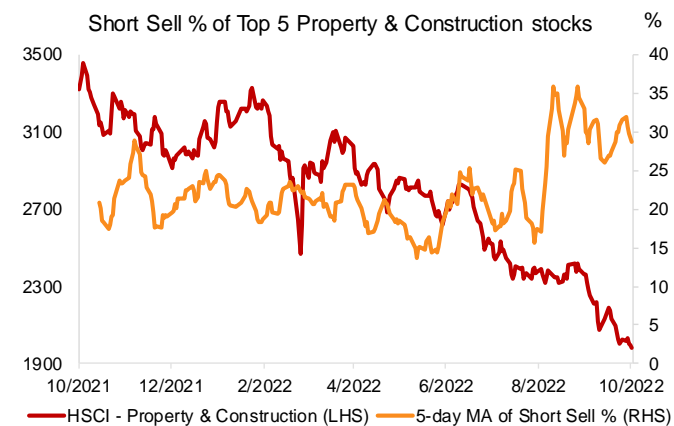
Source: Bloomberg, CMBIGM

Figure 21: Short sell % in HK – Consumer Staples



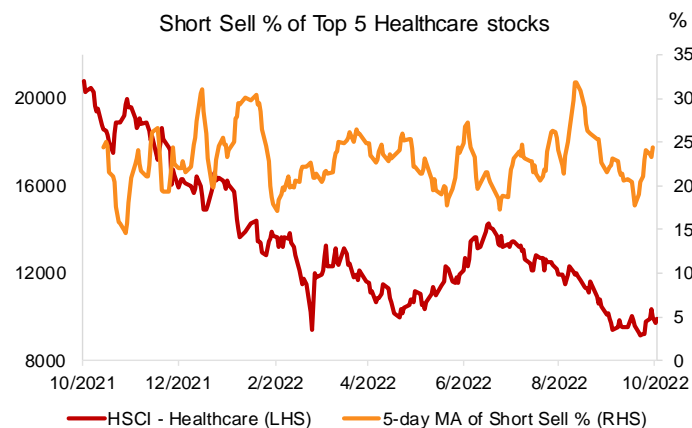
Source: Bloomberg, CMBIGM

Figure 22: Short sell % in HK - Property



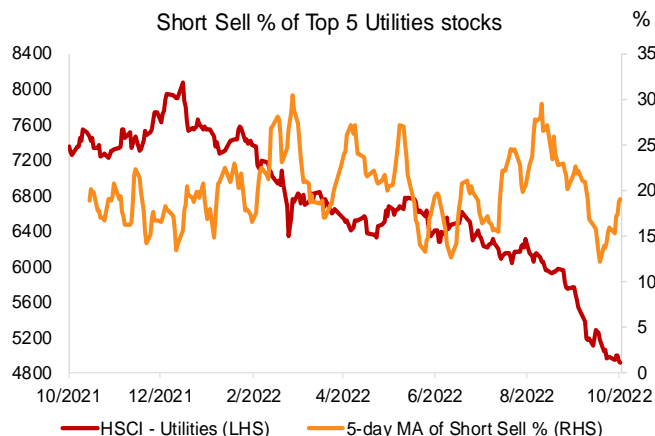
Source: Bloomberg, CMBIGM

Figure 23: Short sell % in HK – Healthcare



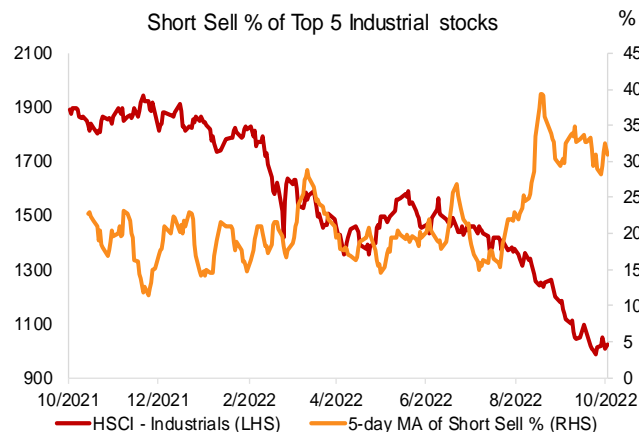
Source: Bloomberg, CMBIGM

Figure 24: Short sell % in HK – Utilities



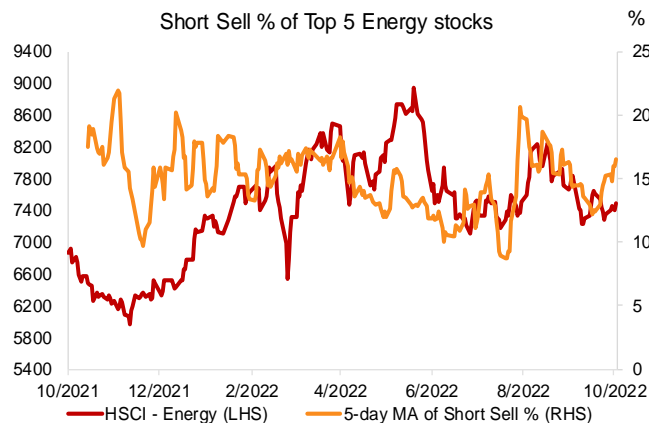
Source: Bloomberg, CMBIGM

Figure 25: Short sell % in HK – Industrials



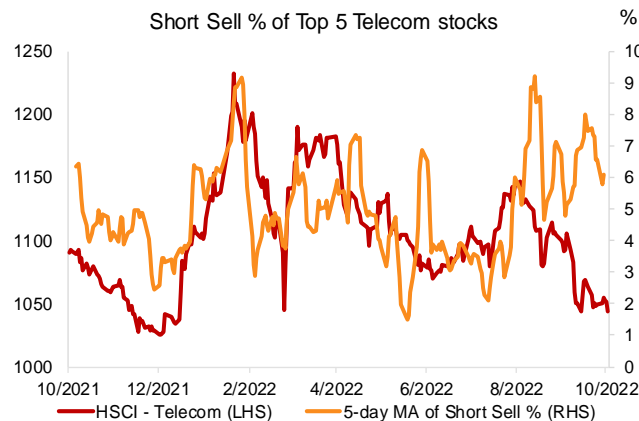
Source: Bloomberg, CMBIGM

Figure 26: Short sell % in HK – Energy



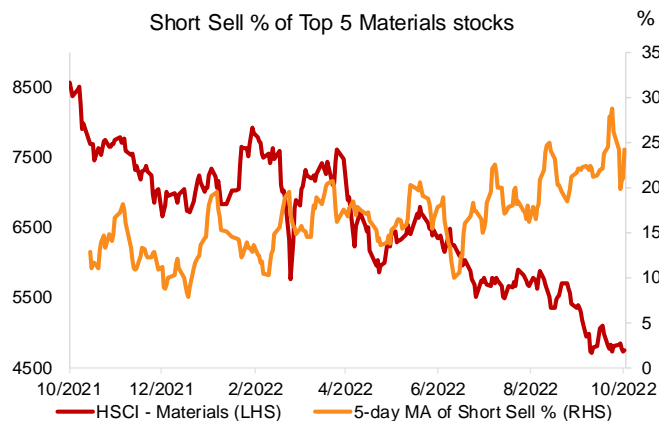
Source: Bloomberg, CMBIGM

Figure 27: Short sell % in HK – Telecom



Source: Bloomberg, CMBIGM

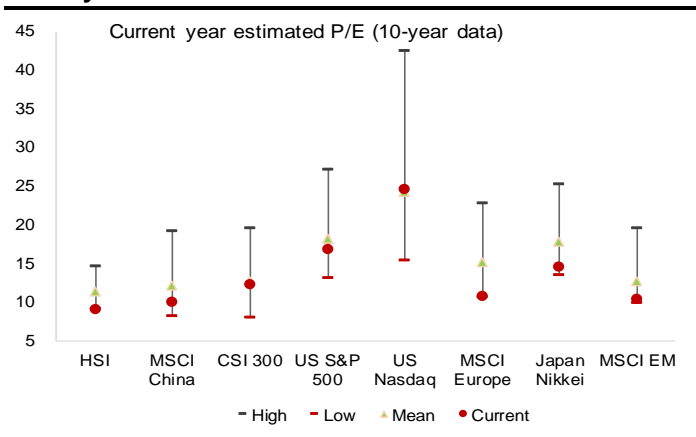
Figure 28: Short sell % in HK – Materials



Source: Bloomberg, CMBIGM

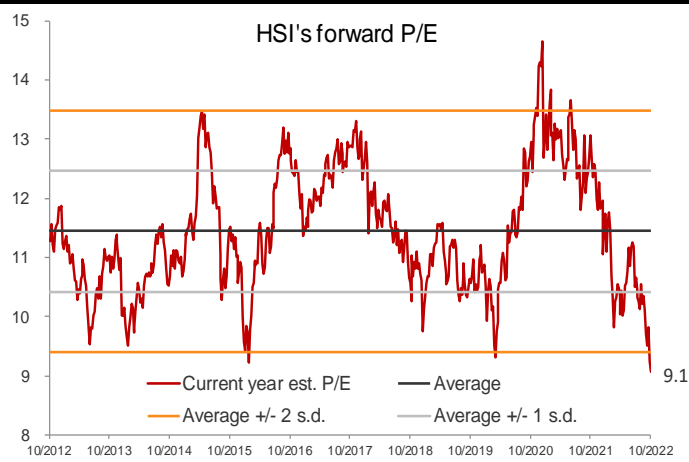
Earnings & Valuations

Figure 29: Major stock markets' forward P/E vs. 10-yr history



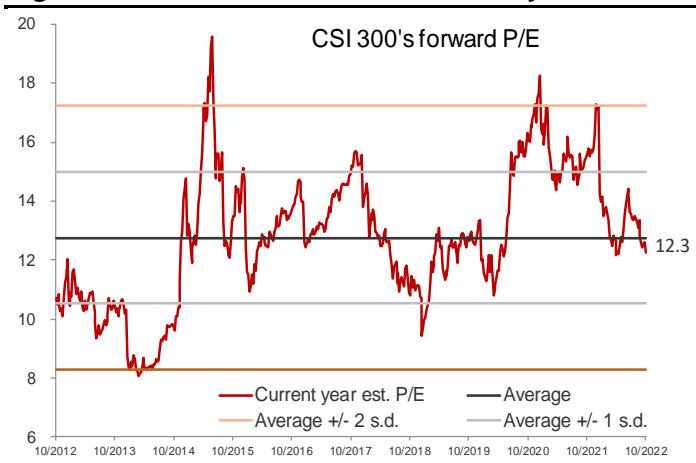
Source: Bloomberg, CMBIGM

Figure 30: HSI's forward P/E at 2 s.d. below average



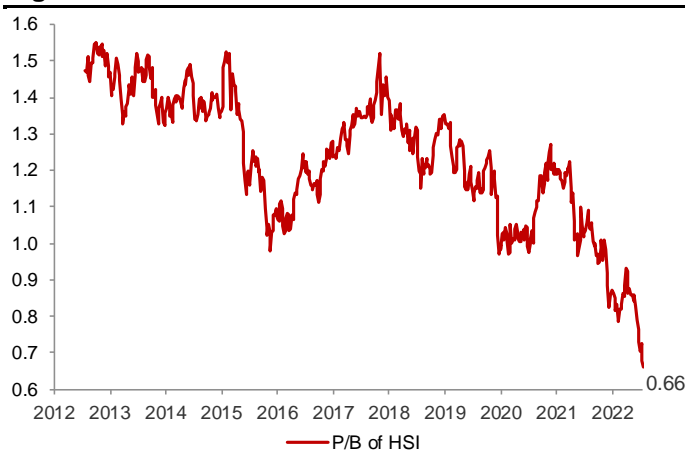
Source: Bloomberg, CMBIGM

Figure 31: CSI 300's forward P/E near 10-yr mean



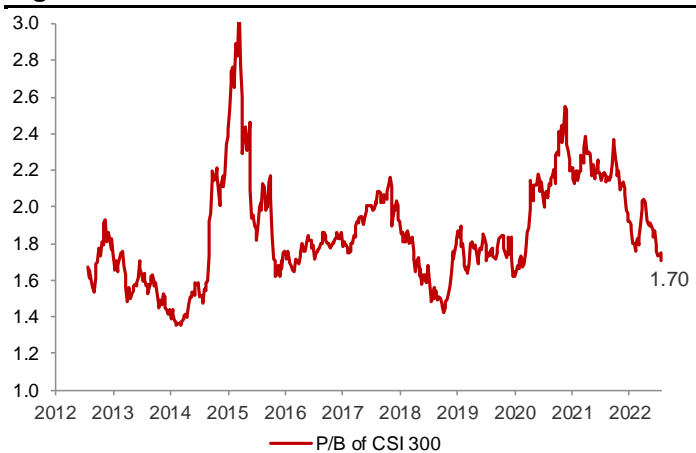
Source: Bloomberg, CMBIGM

Figure 32: HSI's P/B



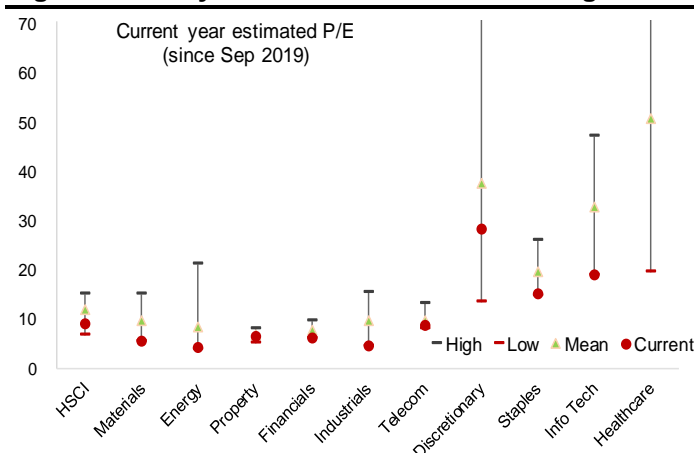
Source: Bloomberg, CMBIGM

Figure 33: CSI 300's P/B



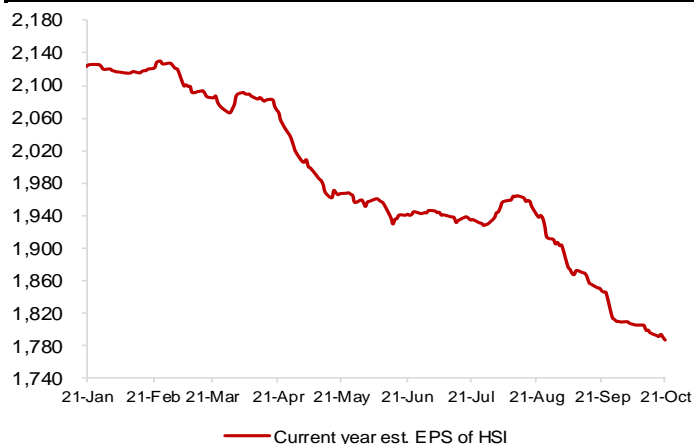
Source: Bloomberg, CMBIGM

Figure 34: Many HSCI sectors' P/E are at troughs



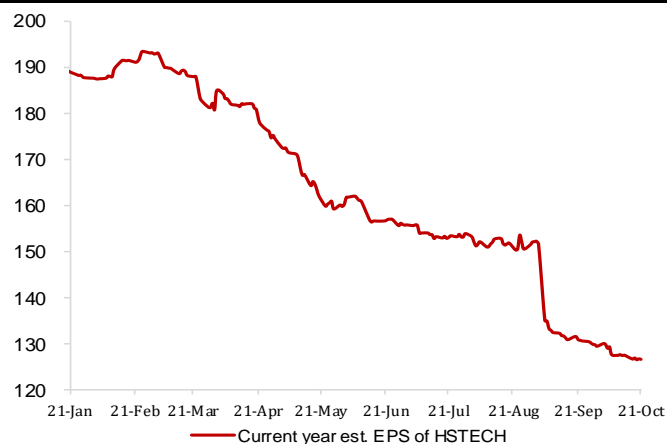
Source: Bloomberg, CMBIGM

Figure 35: EPS estimates of HSI were revised down by 0.5% last week, due largely to RMB depreciation



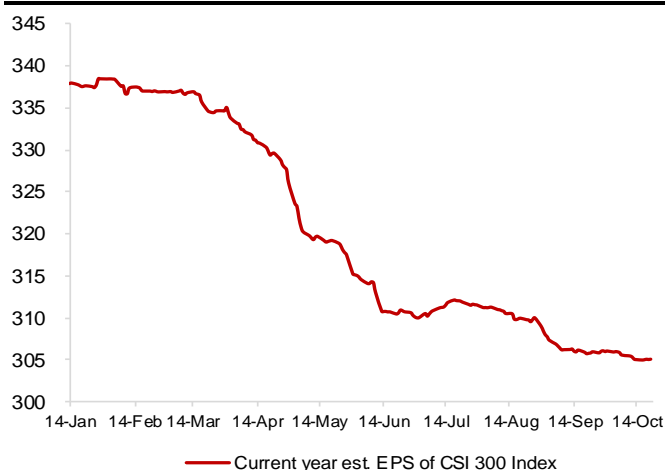
Source: Bloomberg, CMBIGM

Figure 36: EPS estimates of HSTECH Index were revised down by 0.6% last week



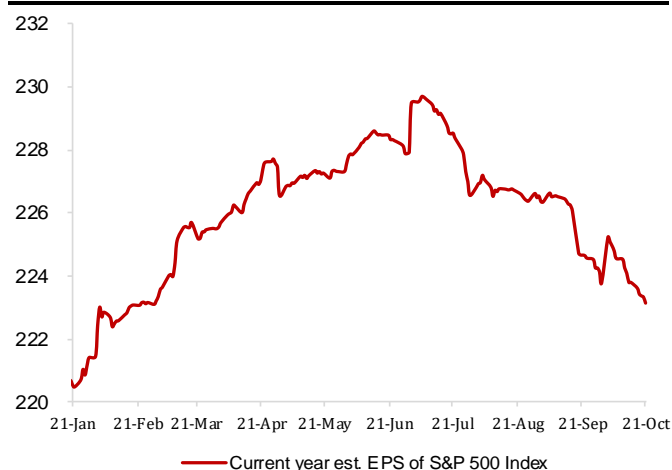
Source: Bloomberg, CMBIGM

Figure 37: EPS estimates of A-shares were flat last week



Source: Bloomberg, CMBIGM

Figure 38: EPS estimates of US S&P 500 were revised down by 0.3% last week



Source: Bloomberg, CMBIGM

Disclosures & Disclaimers

Analyst Certification

The research analyst who is primary responsible for the content of this research report, in whole or in part, certifies that with respect to the securities or issuer that the analyst covered in this report: (1) all of the views expressed accurately reflect his or her personal views about the subject securities or issuer; and (2) no part of his or her compensation was, is, or will be, directly or indirectly, related to the specific views expressed by that analyst in this report.

Besides, the analyst confirms that neither the analyst nor his/her associates (as defined in the code of conduct issued by The Hong Kong Securities and Futures Commission) (1) have dealt in or traded in the stock(s) covered in this research report within 30 calendar days prior to the date of issue of this report; (2) will deal in or trade in the stock(s) covered in this research report 3 business days after the date of issue of this report; (3) serve as an officer of any of the Hong Kong listed companies covered in this report; and (4) have any financial interests in the Hong Kong listed companies covered in this report.

CMBIGM Ratings

BUY : Stock with potential return of over 15% over next 12 months
HOLD : Stock with potential return of +15% to -10% over next 12 months
SELL : Stock with potential loss of over 10% over next 12 months
NOT RATED : Stock is not rated by CMBIGM

OUTPERFORM : Industry expected to outperform the relevant broad market benchmark over next 12 months
MARKET-PERFORM : Industry expected to perform in-line with the relevant broad market benchmark over next 12 months
UNDERPERFORM : Industry expected to underperform the relevant broad market benchmark over next 12 months

CMB International Global Markets Limited

Address: 45/F, Champion Tower, 3 Garden Road, Hong Kong, Tel: (852) 3900 0888 Fax: (852) 3900 0800

CMB International Global Markets Limited ("CMBIGM") is a wholly owned subsidiary of CMB International Capital Corporation Limited (a wholly owned subsidiary of China Merchants Bank)

Important Disclosures

There are risks involved in transacting in any securities. The information contained in this report may not be suitable for the purposes of all investors. CMBIGM does not provide individually tailored investment advice. This report has been prepared without regard to the individual investment objectives, financial position or special requirements. Past performance has no indication of future performance, and actual events may differ materially from that which is contained in the report. The value of, and returns from, any investments are uncertain and are not guaranteed and may fluctuate as a result of their dependence on the performance of underlying assets or other variable market factors. CMBIGM recommends that investors should independently evaluate particular investments and strategies, and encourages investors to consult with a professional financial advisor in order to make their own investment decisions.

This report or any information contained herein, have been prepared by the CMBIGM, solely for the purpose of supplying information to the clients of CMBIGM or its affiliate(s) to whom it is distributed. This report is not and should not be construed as an offer or solicitation to buy or sell any security or any interest in securities or enter into any transaction. Neither CMBIGM nor any of its affiliates, shareholders, agents, consultants, directors, officers or employees shall be liable for any loss, damage or expense whatsoever, whether direct or consequential, incurred in relying on the information contained in this report. Anyone making use of the information contained in this report does so entirely at their own risk.

The information and contents contained in this report are based on the analyses and interpretations of information believed to be publicly available and reliable. CMBIGM has exerted every effort in its capacity to ensure, but not to guarantee, their accuracy, completeness, timeliness or correctness. CMBIGM provides the information, advices and forecasts on an "AS IS" basis. The information and contents are subject to change without notice. CMBIGM may issue other publications having information and/ or conclusions different from this report. These publications reflect different assumption, point-of-view and analytical methods when compiling. CMBIGM may make investment decisions or take proprietary positions that are inconsistent with the recommendations or views in this report.

CMBIGM may have a position, make markets or act as principal or engage in transactions in securities of companies referred to in this report for itself and/or on behalf of its clients from time to time. Investors should assume that CMBIGM does or seeks to have investment banking or other business relationships with the companies in this report. As a result, recipients should be aware that CMBIGM may have a conflict of interest that could affect the objectivity of this report and CMBIS will not assume any responsibility in respect thereof. This report is for the use of intended recipients only and this publication, may not be reproduced, reprinted, sold, redistributed or published in whole or in part for any purpose without prior written consent of CMBIGM.

Additional information on recommended securities is available upon request.

For recipients of this document in the United Kingdom

This report has been provided only to persons (I) falling within Article 19(5) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 (as amended from time to time) ("The Order") or (II) are persons falling within Article 49(2) (a) to (d) ("High Net Worth Companies, Unincorporated Associations, etc.") of the Order, and may not be provided to any other person without the prior written consent of CMBIGM.

For recipients of this document in the United States

CMBIGM is not a registered broker-dealer in the United States. As a result, CMBIGM is not subject to U.S. rules regarding the preparation of research reports and the independence of research analysts. The research analyst who is primary responsible for the content of this research report is not registered or qualified as a research analyst with the Financial Industry Regulatory Authority ("FINRA"). The analyst is not subject to applicable restrictions under FINRA Rules intended to ensure that the analyst is not affected by potential conflicts of interest that could bear upon the reliability of the research report. This report is intended for distribution in the United States solely to "major US institutional investors", as defined in Rule 15a-6 under the US, Securities Exchange Act of 1934, as amended, and may not be furnished to any other person in the United States. Each major US institutional investor that receives a copy of this report by its acceptance hereof represents and agrees that it shall not distribute or provide this report to any other person. Any U.S. recipient of this report wishing to effect any transaction to buy or sell securities based on the information provided in this report should do so only through a U.S.-registered broker-dealer.

For recipients of this document in Singapore

This report is distributed in Singapore by CMBI (Singapore) Pte. Limited (CMBISG) (Company Regn. No. 201731928D), an Exempt Financial Adviser as defined in the Financial Advisers Act (Cap. 110) of Singapore and regulated by the Monetary Authority of Singapore. CMBISG may distribute reports produced by its respective foreign entities, affiliates or other foreign research houses pursuant to an arrangement under Regulation 32C of the Financial Advisers Regulations. Where the report is distributed in Singapore to a person who is not an Accredited Investor, Expert Investor or an Institutional Investor, as defined in the Securities and Futures Act (Cap. 289) of Singapore, CMBISG accepts legal responsibility for the contents of the report to such persons only to the extent required by law. Singapore recipients should contact CMBISG at +65 6350 4400 for matters arising from, or in connection with the report.