Macro Strategy

Seeing Bottom amid a Strong Policy Commitment

- **Macro:** Chinese policymakers made a strong commitment to stabilizing market and growth. The meeting could be a watershed moment for the market. Believe the Chinese policymakers, it will be enough.
- **Strategy**: HK market is bottoming out and will enjoy moderate re-rating over the next few months. Further upside would require that the Russia-Ukraine crisis eases and inflation moderates.
- **Banking & Insurance:** Positive policy signals are likely to drive upward re-rating. We see possible MLF rate and LPR cut in near term and maintain overweight on banking & insurance sector.
- **Property:** Supply side reform to accelerate, leaving more non-SOEs to fade away. We recommend long-term market share gainers including Longfor, CR Land and COLI (688 HK, BUY).
- **Technology:** Recent selloff of tech sector is overdone. We expect no major supply chain disruption from recent Ukraine/Russian crisis and 1-week lockdown in Shanghai, Shenzhen and Dongguan. We are positive on sentiment improvement.
- **Software & IT services**: Potential U.S. sanction on China may hurt China AI. Lockdown in China will affect labor-intensive IT service sector. Sector rebound could be short term.
- **Internet:** We keep positive on sector secular growth and 2Q22E rebound, backed by potential economic stimulus and fundamental improvement ahead. Stock picks: Kuaishou, Tencent, NetEase, Meituan.
- **Renewables:** The positive sentiment would boost the sector. Oil & gas companies face high material costs, while wind power sector would benefit.
- **Capital goods:** The policy signal will help stabilize the market sentiment. H-shares now offer more attractive values compared with A-shares. We prefer Weichai Power-H and Zoomlion-H in the near term.
- **Auto:** The new-energy vehicle (NEV) sector with high growth visibility could become attractive again for investors when market volatility winds down and investor sentiment improves.
- **Healthcare:** We believe US-listed biotech companies, including Beigene (BGNE US), I-Mab (IMAB US), Hutchmed (HCM US) and Zai Lab (ZLAB US) will have large room for share price rebound. We also recommend to bottom-fish CXO names.
- **Consumer discretionary:** We prefer sportswear (neutral) > catering (neutral) > Home appliances (negative) = apparel (negative).
- **Consumer staples:** We recommend HK- and A-share dairy, HK beer and e-cigar sectors and China Feihe, Yili, Mengniu Dairy, China Resources Beer, Tsingtao Beer and SMR International.

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Macro

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The Financial Stability and Development Committee held a special meeting yesterday and made a strong commitment to stabilizing financial market and boosting economic growth. The commitment arrived after the recent panic sales in Chinese stocks and ahead of the US Fed's policy meeting.

The committed policies announced at the meeting are as follows.

1) Concrete actions must be taken to bolster the economy in 1Q22. Monetary policy should take the initiative to cope with the situation, as new loans should maintain an appropriate growth. We expect the PBOC may cut LPRs or RRR in near future to boost market confidence. A cut in interest rates is more meaningful than the RRR cut, as the major downside risk for the economy is the extremely weak demand in real estate market.

2) China must put forward a plan to effectively resolve the risks of property developers and promote their transformation to a new model in future. We expect both mortgage loan and credit for property developers may further ease to alleviate developers' cash flow pressure. Meanwhile, state-owned developers are encouraged to bail out stressed private developers with the credit support from banks. The new model in property sector means a higher share of social rental housing with SOEs or local government vehicles playing a more important role.

3) China will continue to support overseas listing of domestic enterprises. The security regulators in China and US has achieve positive progress over Chinese stocks listed in US markets. Both sides are working to formulate a detailed cooperation plan. As this issue depends on the two sides, there is still uncertainty for the final scenario. China could consider the negative list model. Those companies in the sensitive sectors will be on the negative list and the US regulator cannot directly get their audit papers, making them difficult to go listing in the US. For the companies not in the negative list, the US regulator can directly get their audit papers.

4) China should complete its rectification of internet platform companies as soon as possible. Regulation of internet platform companies should be standardized, transparent and predictable. It indicates the rectification process of internet platform companies should be close to the end. Sector regulation will enter a stage of normalization. The policy risk is expected to decline.

5) China welcomes long-term institutional investors to increase shareholdings in Chinese companies. China's banking & insurance regulator will encourage insurance companies to allocate more funds to equities and banks' wealth management companies to expand equity-linked products. The securities regulator will encourage listed companies to increase share purchase, guide fund managers to purchase their own funds and support the development of fund management business.

6) Beijing and Hong Kong should strengthen cooperation over the stability of Hong Kong's financial market.

The meeting was held before the US Fed's meeting in order to stabilize market confidence in advance and avoid the external shock further amplifying market panic. Seeing the strong policy commitment from the Chinese policymakers, investors in HK stock market rushed to close their short positions. The liquidity squeeze effect caused a sharp rise of HK stocks especially those with massive short position and sharp declines in recent two weeks. The Hang Seng Tech Index jumped by over 20% on Thursday.

The meeting could be a watershed moment for China's policy. The market generally believes 4Q21 was the bottom for policy side. But the policy magnitude was weaker than expected in the past several months. The Russian-Ukrainian conflict and the outbreak of the Omicron virus has caused additional pressure on China's financial markets and economic growth. The gap between policy supply and demand has further increased.

The meeting shows that policymakers start to plan to resolve the debt risk of property developers and to boost capital confidence in the internet sector. It will help ease investors' concerns about property market stress, lower policy risk in internet sector and enhance confidence about China's economy.

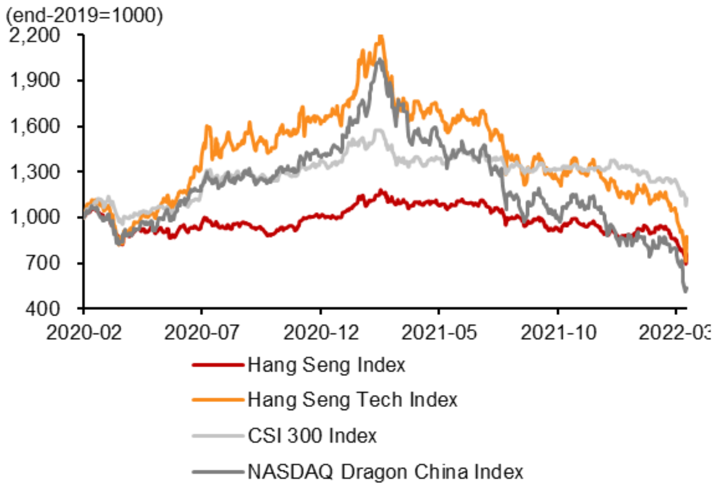
The effect of the meeting was just like what the ECB president did in July 2012. In face of the precarious euro under the accumulation of short positions, the ECB President Draghi said on 26 July 2012 he was "ready to do whatever it takes" to save the euro. He added, "Believe me, it will be enough". His words effectively stabilized the market sentiment, which became the turning point for the European debt crisis. Then in September 2012, the ECB announced the implementation of OMT, declaring the role of the "lender of last resort" and ending the Euro liquidity crisis.

For policymakers, however, it is easier said than done. After declaring the policy attitude and strong commitment, it will usher in a moment to test the credibility of the policy. Therefore, some policymakers adopt a vague strategy. But crisis moment requires the courage of a clear attitude with a strong commitment.

We believe HK stock market may see a round of rebounding after the recent sharp slump. The bottom of the stock market can only be clearly judged after you walk out of the bottom. Let us make a risky prediction. We believe HK stock market may have already seen its bottom yesterday. We may experience a rebounding in near term. In the early stage of the rebound, there will be a general rise of almost all sectors. The greater the decline before the rebound, the higher the rebound. Then it will enter a new phase with divergence for different sectors. Earnings fundamental and valuation attractiveness will be the decisive factors.

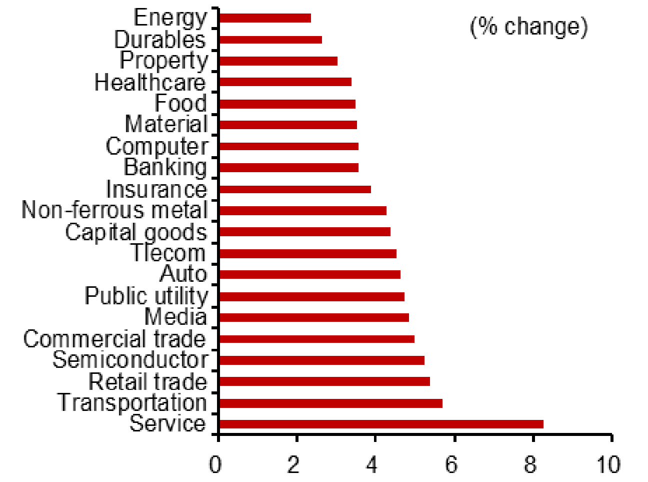
But the road to rebound will not be smooth in the future. On the one hand, as the market has higher expectations for the policy side, there will be risk that the actual policy strength may be below expectations. On the other hand, the geopolitics risk, US sanction risk and delisting risk of Chinese stocks in the US seems still there. In the medium to long term, China still faces the two major challenges. One is how to build a new growth engine driven by consumption and high tech after abandoning its land-oriented and investment-driven growth model. The other is how to create a peaceful environment for further development in face of dramatic changes in its international relations.

Figure 1: Chinese Stock Indexes



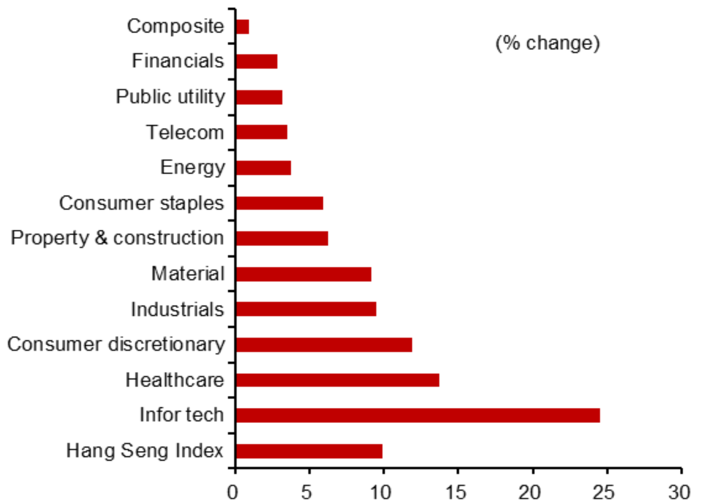
Source: Bloomberg, CMBIGM estimates

Figure 2: Wednesday Performance of A Shares



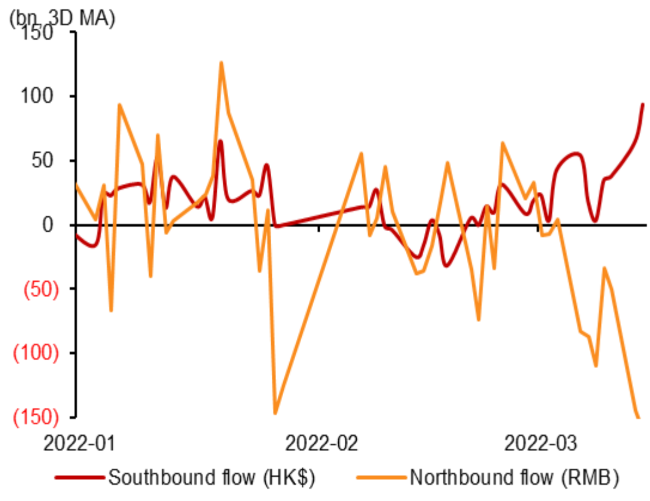
Source: Bloomberg, CMBIGM estimates

Figure 3: Wednesday Performance of HK Stocks



Source: Bloomberg, CMBIGM estimates

Figure 4: Southbound and Northbound Flows



Source: Bloomberg, CMBIGM estimates

Figure 5: Current and 15-Year Percentile Levels of PE for Global Stock Indexes

	Hang Seng index	CSI 300 index	Chinext index	S&P 500 index	NASDAQ index	Nikkei 225 index	Germany DAX	France CAC	UK FTSE 100 index
Min	7.6	7.9	17.6	10.0	13.1	9.9	7.8	7.1	6.6
30% percentile	10.9	12.1	29.2	14.9	19.8	16.2	11.9	12.3	11.9
50% percentile	11.8	13.5	34.0	16.5	21.8	17.4	13.1	14.3	13.0
80% percentile	13.7	17.2	44.7	18.5	25.2	19.9	14.4	15.7	15.2
Current value	8.8	11.7	30.4	18.5	25.7	15.3	12.2	12.1	10.8

Source: Bloomberg, CMBIGM estimates

HK Market Strategy

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The Hang Seng Index plunged by 26% in just under a month, to as low as 18,235 on 15 Mar 2022, the lowest since Jun 2012.

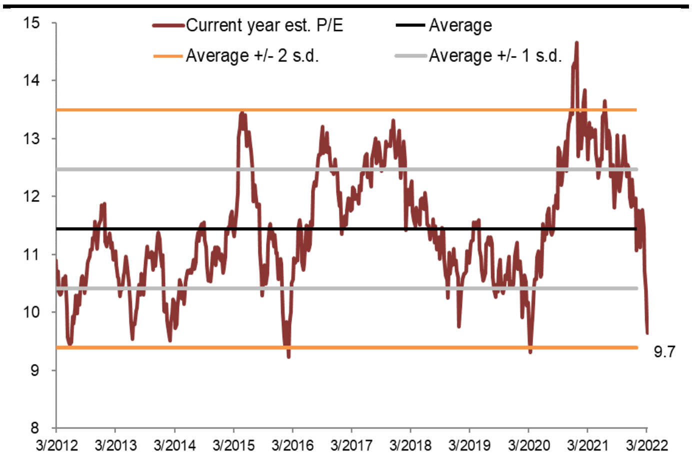
What caused the sell-offs in HK stock market?

1. **Geopolitical risk**, i.e. Russia-Ukraine conflicts.
2. **Commodity price and inflation upside risks**, exacerbated by potential disruption of supplies from Russia & Ukraine.
3. **Monetary tightening**, as central banks in the West might tighten more aggressively to combat inflation.
4. **Potential forced delisting of China stocks/ADRs** from U.S. exchanges.
5. **Sanctions risk**, as the U.S. warned China would face consequences if it helps Russia evade sanctions.
6. **Economic risk in China**, as a new wave of COVID emerged in Mainland China and HK.

At its low on 15 Mar, **the HSI's forward P/E dropped to 8.9x, the lowest since the 2008 Global Financial Crisis**.

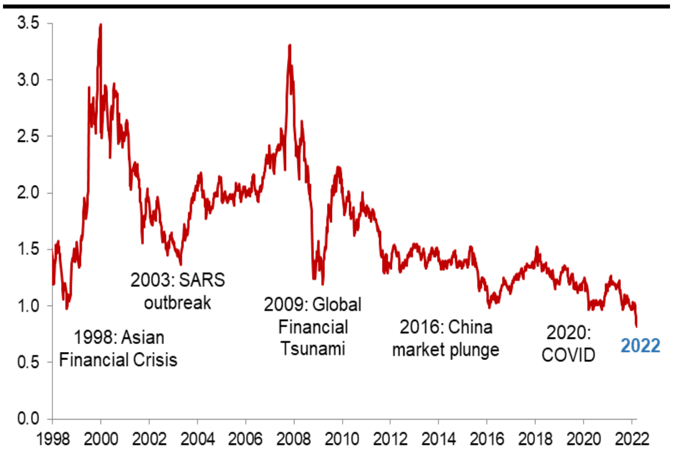
The P/B of the HSI is even more distressed, dropping to as low as 0.75x, much lower than previous troughs over the last quarter of century. Its P/B troughed every 5-7 years, excluding the black-swan event in 2020 (COVID outbreak). It is very likely at a cyclical low, in our view.

Figure 6: HSI's forward P/E plunged to decade low



Source: Bloomberg, CMBIGM

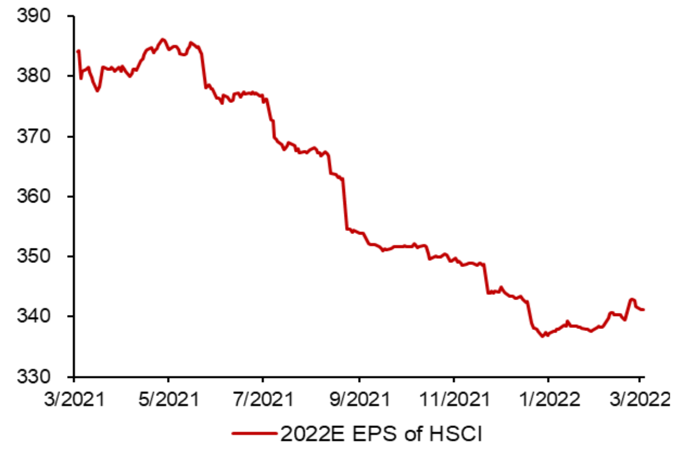
Figure 7: HSI's P/B troughed in every 5-7 years



Source: Bloomberg, CMBIGM

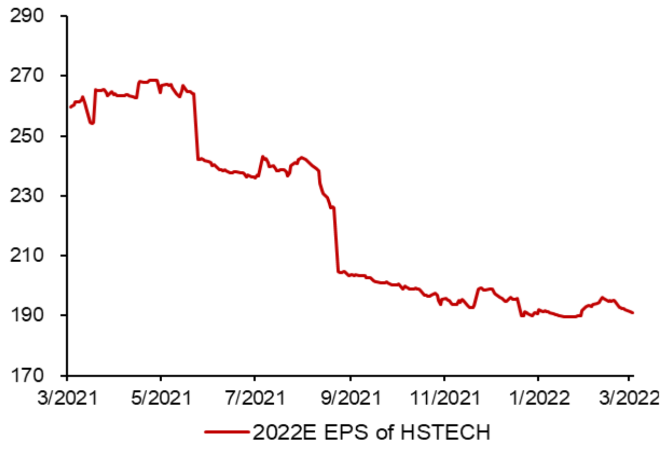
The plunge since mid-Feb have been entirely due to devaluation and had nothing to do with earnings downgrade. In fact, earnings estimate of the Hang Seng Composite Index has been being revised up YTD. Even for internet / tech stocks that suffered the heaviest sell-offs (represented by the Hang Seng TECH Index), their 2022E EPS are no worse than in early-Feb.

Figure 8: HSCI enjoying upward earnings revision



Source: Bloomberg, CMBIGM

Figure 9: HSTECH's earnings estimates stabilised



Source: Bloomberg, CMBIGM

Therefore, now the key questions is, "Which of those risks that have been priced in are now easing, and what catalysts can drive revaluation?"

Which of those priced-in risks may be easing?

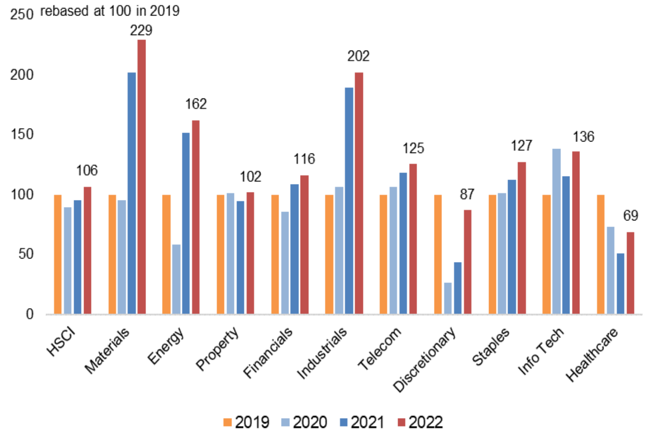
1. **Geopolitical risks**. While there are still plenty of uncertainties, Ukraine President Zelensky said on 15 Mar that Ukraine should accept it will not become a member of NATO, hinting at a potential key concession to Russia and paving the way for ceasefire talks.
2. **Commodity price and inflation upside risks.** WTI crude oil price spiked to US$130 last week, but have quickly retreated to below US$100. In case the war drags on and the West drastically cut energy imports from Russia, oil and natural gas prices may well rise gain. But for now, prices have somewhat stabilised. If ceasefire could be reached, concerns on high energy prices and inflations should ease further.
3. **Potential forced delisting of China stocks/ADRs.** China said that *"the Chinese and the U.S. regulatory bodies had maintained good communication and made positive progress on the regulation over U.S.-listed Chinese firms. The two sides are working on a concrete cooperation plan."* It may be premature to conclude that the delisting risk will be resolved, but this risk has already been known to investors for two years, and as such we believe the recent sell-offs in ADRs and related HK-listed stocks have been excessive.

Positive catalysts (after China's State Council meeting on 16 Mar)

1. **Stronger monetary and fiscal support.** China's State Council meeting called for *"concrete actions must be taken to bolster the economy in the first quarter"*, *"monetary policy should take the initiative to cope with the situation, while new loans should maintain an appropriate growth"*, and *"actively introduce market-friendly policies"*.
2. **Less regulatory risks.** The State Council meeting assured investors that *"any policy that has a significant impact on the capital market should be coordinated with the financial regulatory authorities in advance to maintain stable and consistent expectations."* The meeting also stressed that *"authorities should prudently introduce policies with a contractionary effect."*
3. **More buying from institutions and listcos.** Soon after the State Council meeting, various regulatory bodies echoed, vowing to *"guide insurance companies to allocate more funds to equities"*, *"encourage listed companies to increase share buybacks"*, and that *"long-term institutional investors are welcome to increase their shareholding."*

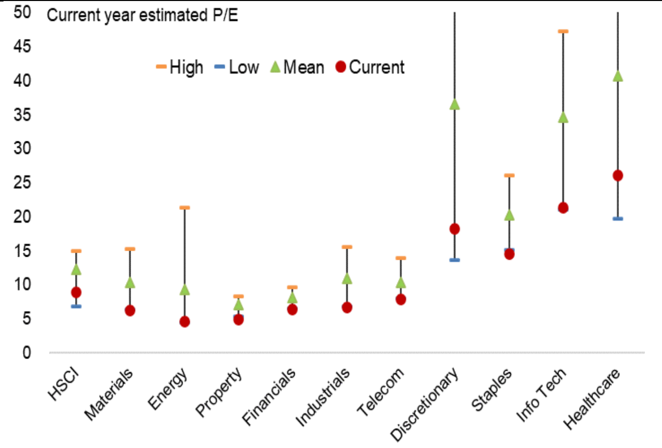
With decade-low valuations, some risks easing and more support by Beijing, **we expect Hong Kong stock market is bottoming out and enjoy moderate re-rating over the next few months.** Further upside would require that the Russia-Ukraine crisis eases and inflation in the West moderates.

Figure 10: Earnings trend by HSCI sector



Source: Bloomberg, CMBIGM

Figure 11: P/E by HSCI sector



Source: Bloomberg, CMBIGM; data since Sep 2019

Banking & Insurance

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We think the positive policy signals from the Financial Stability Committee (FSC) and CBIRC are likely to drive upward re-rating of banking and insurance sectors. We expect to see MLF rate cut and LPR drop in near term and more measures from the central government to simulate the economy.

On profitability perspective, LPR drop will lead more NIM compression; however, easing monetary policy will release banks' pressure on asset quality front. In short term, expectation on asset quality is more influential than NIM on banks' valuation. In addition, since default risk on property sector is fully priced in and CBIRC's view on property developers turns into positive, we think previous concerns on property developers' default will not cap banks valuation any more. Currently, demand on defensive assets and expectation on easing monetary policy are the catalyst on sector re-rating. In our view, banks will become more attractive for long only investors due to its low valuation and high dividend yield.

On insurance front, we believe the easing concerns over investment quality with marginal improvement on the liquidity problems of property developers will be a positive catalyst for insurance companies. And we think P&C insurers will benefit more than life insurance business, as the liability duration of P&C insurers is much shorter than the assets duration, hence more defensive against yield decline.

Maintain OVERWEIGHT on banking sector and insurance sector. We reiterate BUY on PSBC (1658 HK) as our top pick for banking sector. During last three years, PSBC (H) was trading at 0.72x FY22E P/B, while currently it is trading at 0.71x P/B, slightly below historical mean (0.72x P/B). For insurance space, we maintain PICC P&C (2328 HK) as our top pick, and also like Ping An (2318 HK) and CPIC (2601 HK) given their proactive agency upgrades. Chinese insurers' H-share valuation is currently down to a historical trough. Life insurers' H shares are trading at 0.1x -0.5x P/EV FY22E and 0.3x-0.9x P/BV FY22E, PICC P&C is now trading at 0.6x P/BV FY22E.

Property

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- The property sector was lifted today upon Vice Premier Liu He's mentions on risk prevention and mitigations for developers during the State Council meeting. Following his talk, the Ministry of Finance stated there would not be an expansion of property tax within this year. Market reaction and impact were similar to our previous estimate of when deputy-state leader would preside over and stimulate the economy.
- However, due to still weak sales sentiment (-42% YoY in first two weeks of Mar) could further double down on pandemic and rising unsold inventory in 2M22. Together with debt peak in Mar/Apr, we expect supply side reform to accelerate, leaving more non-SOEs to fade away. In addition, factoring the time lag between policy stimulants transferring into demand. We still recommend investors to gradually add long-term market share gainers including Longfor (960 HK, BUY); CR Land (1109 HK, BUY); and COLI (688 HK, BUY). For high beta, CIFI (884 HK, NR), Midea (3990 HK, NR), CGS (6098 HK, BUY), Ever Sunshine (1995 HK, BUY), Greentown Services (2869 HK, HOLD) may stand out.

Technology

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- **We believe recent selloff of tech sector is overdone**, driven by concerns over Russia-Ukraine conflict, rising inflation, slowing economy and COVID outbreak in China. While we think positive policy signals from Chinese government will boost sector sentiment in near term given, we believe the sector will remain volatile into earnings season.
- **On Russia-Ukraine conflict, we expect no major disruption in supply chain** due to shutdown of two major Neon gas suppliers in Ukraine. We believe overall impact on semi sector is manageable in the medium term given multiple-sourcing strategy, but significant price hike on neon gas is inevitable (inert gas <5% of semi cost). Overall, we think elevated geopolitical risk will boost inventory stock along supply chain and ongoing chip shortage will intensify.
- **Limited impact from 1-week lockdown in Shanghai, Shenzhen and Dongguan for mandatory testing.** Given these 3 regions are major manufacturing hubs for tech hardware, we think it will lead to short-term supply chain disruption, but the impact is limited for most companies as March is low season for tech supply chain.
- **Positive on sentiment improvement.** Overall, we believe VR/AR cycle, 5G policy support, semi localization and product innovation will remain major growth drivers for technology supply chain. We recommend to stick with sector leaders with stronger bargaining power and higher earnings visibility, including Xiaomi (1810 HK, BUY), Will Semi (603501 CN, BUY) and Maxscend (300782 CN, BUY).

Software & IT Services

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- **Continuous Russia-Ukraine dispute could impact global chip supply**. As Neon is needed and that Ukrainian companies manufacture >70% of Neon globally, chip production still faces risk of disruption if Russia-Ukraine dispute continues. This could affect data center supply chain and hence affecting IDC move-in/ utilization.
- **Potential U.S. sanction on China may hurt China AI**. There is growing concern that U.S. may impose sanctions on China if the latter provides military assistance to Russia in Ukraine's invasion. As advanced chips being used in AI require US technology in design and manufacturing, further sanctions could affect China's AI development, negative to SenseTime (20 HK, BUY), Hikvision (002415 CH, BUY) and Dahua (002236 CH, HOLD).
- **Lockdown in China will affect labour-intensive IT service sector.** The spread of Omicron in China has induced tighter nationwide restrictions. This could affect IT projects delivery and implementation schedule. The strengthening control in people movement will impact IT service companies most such as Chinasoft (354 HK, BUY) and iSoftStone (301236 CH, NR).
- **Sector rebound could be short term**. Oversold US-listed Chinese companies including **GDS (GDS US, BUY), Kingsoft Cloud (KC US, BUY)** could see the biggest rebound. However, we think the recent recovery is sentiment-driven and may not last long if geopolitical/ macro problems remain unresolved.

Internet

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Policy trough to drive up sector sentiment

The meeting of the financial stability and development committee under CSC marked a clear signal of policy trough for China Internet sector, given: 1) positive attitude towards the auditory issue on ADRs delisting; and 2) largely mitigated the concern about further tightening regulation in the platform economy. We are also impressed by such supportive statement (e.g. “encourage to release positive policies”, “policies consistent with financial market stabilization”), suggesting more regulation catalysts to come.

We expect the meeting to directly drive up sector sentiment (even back to the level), with regulatory overhang to lift, stabilization of market sentiment and LO fund flow. Sector stock price surged 25% yesterday, mainly on HF short cover (while LO not much engaged). Sector valuation revised up to 11x FY22E P/E (14% earnings growth in FY22E), still far below 5-year historical average multiple.

Looking ahead, we suggest to focus on: 1) FOMC tone; 2) the progress of the ADRs delisting issue; 3) China’s geopolitical risks under Russia-Ukraine crisis; and 4) 1Q22 & FY22E guidance of core names in earnings result. We keep positive on sector secular growth and 2Q22E rebound, backed by potential economic stimulus and fundamental improvement ahead.

Stock picks:

Kuaishou (1024HK, BUY): solid fundaments with resilient growth & clear breakeven schedule in FY22E; low regulatory risks; attractive valuation

Tencent (700 HK, BUY): low market expectation; confident on LT fundaments backed by games globalization and videolization; catalysts: game license resumption, ads recovery, stock buyback.

NetEase (9999 HK, BUY): defensive player with strong game pipeline and LT margin expansion; low regulatory risks;

Meituan (3690 HK, BUY): strong high barrier with expanding TAM; short-term headwinds priced in.

Renewables

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The meeting mentioned a few about renewable energy, but the positive market sentiment also boosted the renewables sector. Below are the latest fundamentals analysis on renewable sectors:

Oil sector

Recently, the oil prices fell from the highs of 130-140 USD/barrel due to Russia-Ukraine conflicts easing and the U.S actively mediating the Middle East oil-producing countries to enlarge oil production. But the global oil price may not go further down in the short term as the sizeable global oil supply gap cannot be sufficiently filled.

Hence, the relatively high global oil price will impact domestic oil imports cost, furthermore, pushing up domestic oil prices. Oil companies like China's three major oil companies (NOCs) - CNPC (857 HK, N.R.), CNOOC (883 HK, N.R.), CPCC (386 HK, N.R.) will benefit from it. The latest round of oil gas adjustment will be on 17th Mar 2022.

Figure 32: Domestic oil price adjustment cycle and adjustment range (2022)

Price Adjustment Window	Gasoline(yuan/ ton)	Diesel Fuel(yuan/ ton)
3rd Mar 24:00pm	↑260	↑255
17th Feb 24:00pm	↑210	↑200
29th Jan 24:00pm	↑310	↑300
17th Feb 24:00 pm	↑345	↑330
Total	↑1125	↑1085

Source: NDRC, Bloomberg, CMBIGM estimates

Figure 13: Domestic oil price adjustment cycle and adjustment range (2021)

Price Adjustment Window	Gasoline(yuan/ ton)	Diesel Fuel(yuan/ ton)
3rd Mar 24:00pm	↑260	↑250
17th Feb 24:00pm	↑275	↑265
29th Jan 24:00pm	↑75	↑70
17th Feb 24:00 pm	↑185	↑180
Total	↑795	↑765

Source: NDRC, Bloomberg, CMBIGM estimates

Gas Sector

- Previously, the Russia-Ukraine conflict tightens global oil and gas supply, pulling up global natural gas prices. As China's LNG external purchase proportion is relatively high, the cost of LNG imports rises as global higher natural gas lift. Thus, higher LNG imports cost will pressure city gas companies' dollar margins and profit.
- Yet, as the Russia-Ukraine crisis tends to ease recently and global LNG demand will gradually go into the typical off-season, the high natural gas price may temperate. Further, the dropped gas price can lower downstream city gas companies' costs like ENN (2688 HK, N.R.), China Gas (384 HK, N.R.), CRG (1193 HK, N.R.), relieving some pressure on the dollar margins and profits in short-term.

Wind Power Sector

- Russia-Ukraine conflict buffered global energy supply; several countries announced accelerating the development and application of renewable energy. China is also dedicated to developing renewable energy. As the Fifth Session of the Thirteen CPPCC mentioned, wind power is expected to become the third-largest power supply in China. Hence, the wind power sector is fast-growing. China Long Yuan (916 HK, N.R.) and Goldwind (2208 HK, N.R.) will benefit.

Capital goods

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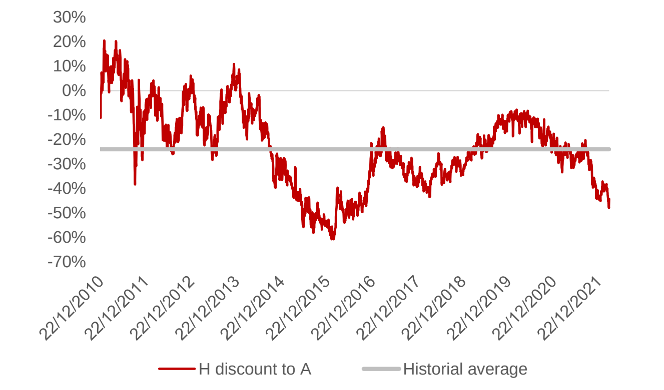
Construction machinery / HDT – We see the improvement in excavator and wheel loader sales in Feb an initial sign of recovery, and we continue to expect the infrastructure spending growth this year will stop the machinery demand from further deterioration. We believe the policy signal yesterday will help stabilize the market sentiment. Following weeks of market sell-off, H-shares now offer more attractive values compared with A-shares. We prefer **Weichai Power-H (2338 HK, BUY)** and **Zoomlion-H (1157 HK, BUY)** in the near term.

- **Zoomlion** – Zoomlion just proposed to repurchase H-share (max: 10% of the total o/s H shares). It's worth noting that the current share price of HK$4.59 is below the management's subscription price in the placement last year (HK$5.86). Therefore, we see strong incentive for the management to boost the share price performance going forward. Zoomlion-H is trading at 44% discount to A-share, significantly below the historical average of 24%. Trading at 5x 2022E, we believe risks are largely in the price.

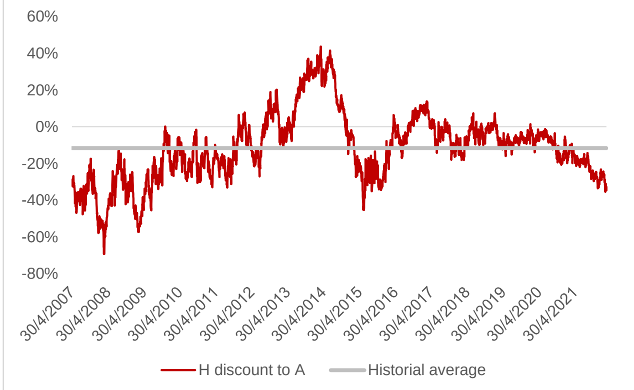
- **Weichai Power** – The latest connected transaction agreement between **Sinotruk (3808 HK, BUY)** and Weichai Group (parent company of Weichai Power) suggested that the former's sales strategy will likely remain aggressive this year, which we believe is a key driver for Weichai Power to maintain its HDT engine market share. On the other hand, we expect a recovery of **KION (KGX GR)** share price will lend support to Weichai's SOTP valuation. Weichai-H is trading at 33% discount A-share, below the historical average of 12%.

Figure 44: Zoomlion - H discount to A



Source: Bloomberg, CMBIGM

Figure 15: Weichai – H discount to A



Source: Bloomberg, CMBIGM

Auto

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- We believe the new-energy vehicle (NEV) sector with high growth visibility could become attractive again for investors when market volatility winds down and investor sentiment improves.
- i) NEV sales in the first two months of 2022 exceeded our prior expectation. For the first two weeks of March, NEV market share further increased to 28% in terms of retail sales volume, the highest in history. Although we are of the view that the monthly pattern this year should be different from last year and the lockdown in some cities in March could create some noise to production and sales in the short term, we believe our full-year NEV sales forecast of 5mn units could be a bit conservative.
- ii) Market has been worried about OEMs' margin dent from raw-material price hike. Assuming everything else being constant, we calculate that rising battery prices along with steel/aluminium price volatility may cut NEV makers' gross margin by 5-8 ppts. However, OEMs could partly offset such dent by cost savings on other components and economies of scale. In addition, given the capacity expansion plan of upstream suppliers, we expect the raw-material costs related to batteries to go down in 2H22. The recent share price declines have reflected market's excessive worry, in our view.
- iii) We still prefer leading NEV start-ups, including Li Auto (LI US/2015 HK, BUY/BUY), Xpeng (XPEV US/9868 HK, BUY/BUY) and NIO (NIO US/9866 HK, BUY/NR). Among traditional OEMs, we like Great Wall Motor (2333 HK/601633 CH, BUY/BUY) more than Geely (175 HK, HOLD). Investors tend to regard BYD (1211 HK/002594 CH, HOLD/HOLD) as NEV segment Beta, and therefore its share price may rally along with sentiment recovery.

Healthcare

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- US and Chinese regulators have been working to improve audit oversight and cooperation. The Chinese government has stated that they want to improve cooperation on bilateral audit oversight given the importance of global capital markets to both economies. With the three-year provision in the HCFAA (or two years with AHCFAA), there appears to be ample time for a satisfactory resolution of this issue. We believe US-listed biotech companies, including Beigene (BGNE US), I-Mab (IMAB US), Hutchmed (HCM US) and Zai Lab (ZLAB US) will have large room for share price rebound.
- We also recommend to bottom-fish CXO names. Leading China-based CXOs reported revenue growth acceleration in 1Q22 amid an unstable geopolitical situation. The impressive growth momentum in 1Q22 bodes well for the strong full-year growth of China CXO sector. We think it is a good timing to bottom fish leading Chinese CXO names, given their solid earnings growth and historical low forward PE valuation. Top picks are WuXi Bio (2269 HK) and WuXi AppTec (603259 CH, 2359 HK). We expect WuXi Bio to benefit from the increasing demand in non-COVID CMO projects thanks to its rich project pipelines. We believe WuXi AppTec will further strengthen its leading position as an integrated one-stop CRO/CDMO service provider and will record accelerating earnings growth in 2022 thanks to significant contribution from COVID-related CMO orders.

Consumer Discretionary

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- We do think the recent market crash was driven more by the fall in valuation than the cut in earnings estimates, therefore, once the investors sentiment improves or confident restores, share prices will certainly have a meaningful rebound.
- We think the major market concerns right now are: 1) potential de-listing of Chinese ADRs, 2) conflict between the Russia and Ukraine (which have real impact on costs inflation), 3) national-wide covid outbreaks in mainland China and 4) trend of US interest rate hike in the next few quarters.
- In our view, problem (1) and (3) are more short-term and are likely to improve soon, because the authorities in US and China are seems to be resolving the difference very hard and the covid situation should be under control, given a period of time, thanks to the rigid social distancing policies in China. However, for problem (2) and (4), we do wish these to be resolved soon but it is still highly uncertain, if the conflict continue, inflation may become more significant and rate hike may become more long-term and larger in magnitude. But all in all, we do think the sentiment is likely to improve onwards.
- In terms of sector picks, we prefer sportswear (neutral) > catering (neutral) > Home appliances (negative) = apparel (negative). Because the earnings cut, due to current covid outbreak, are quite limited for brands like Xtep, therefore we do think Xtep (1368 HK), Li Ning (2331 HK) and Anta (2020 HK) are all good bargains. Catering brands like Yum China are certainly impacted negatively in during the pandemic, but the earnings cut once again, should have more than priced in after the share prices crash, hence, JMJ (9922 HK), HDL (6862 HK) are all attractive now. Home appliances are facing weakening demand in the overseas and strong CNY, as well as the surge in raw material prices, it is hard to see any short-term catalysts. Apparel sector is impacted negatively by pandemics.

Consumer Staples

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- Recently, HK and A-share Consumer Staples sector had a notable correction. We think it is partially due to investors worried about a possible spillover of international raw mat price hike into China, but mainly affected by panic and speculative sell-off escalated by external shocks including international geopolitical conflicts and the approach of tapering by several foreign countries.
- On the demand side, there have been no significant changes for Consumer Staples sector. Since March 2022, nearly 20 A-share F&B companies have released Jan-Feb 2022 financial data, which posted an overall positive trend. Although the number of companies disclosing data is limited, we believe these results were still indicative about the overall fundamentals of the sector though the no. of releasing companies was limited.
- In terms of market performance, Consumer Staples had relatively limited correction compared to the overall market. MTD (by 16th Mar, 2022), HSI Consumer Staples Index (-16.72%) outperformed the MSCI China Index (- 24.88%) by 8.17%. Among the main HK share sub-sectors tracked, dairy (-10.49%) and food (-11.31%) were the relatively best performers, while e-cigar (-35.99%) the worst performer. Among main A-share sub-sectors tracked, dairy (-6.93%), meat products (-8.65%) and baijiu (-9.52%) were ther relative best performers, snacks (-18.24%) and soft drinks (-13.49%) the worst performers. Among main stocks tracked, Yili (-6.07%), China Feihe (-10.09%) had relatively smaller fall, RLX Tech (-44.48%), Smoore (-39.86%) and Nongfu Spring (-25.23%) recorded the largest rebalance. In addition, HK-listed breweries experienced a larger correction MTD (-18.62%) compared to its A-share correspondent (-9.59%). We believe it is mainly due to a higher foreign stake in related HK stocks and the need of increasing cash of different foreign institutions through the liquidation of at least part of their allocation to emerging markets.
- We think sub-sectors and stocks whose robust fundamentals have been proved by recent financial results and with reasonable valuations would most likely take the lead in a subsequent rebound once the market would have bottomed out. Any corrections due to market sentiment bumping thereafter would be a good timing to accumulate such stocks. In addition, sub-sectors most hardly hit by non-fundamental factors during the recent market turmoil, such as HK beer and e-cigar, could also offer better rebound opportunity, in our view, with the market returning back to rationality and several external uncertainties being settled. We recommend HK- and A-share dairy, HK beer and e-cigar sectors, and China Feihe (6186HK, BUY), Yili (600887CH, BUY), Mengniu Dairy (2319HK, BUY), China Resources Beer (291HK, BUY), Tsingtao Beer (168HK, BUY), And SMR International (6969HK, BUY).

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