Fund Manager Perspective

3 August 2015

The market was very volatile in July. Initially, the SSE Composite Index fell from 4200 to around 3300 as nervousness from the end of June carried over to the beginning of July; then, the market rebounded to around 4200 due to stimulation from the CSF but began experiencing a second correction. During this time, the trading volumes of both the Shanghai and Shenzhen markets began to shrink. At the end of July, daily trading volumes were around half of what they were during the peak period. Recent hot investment areas include military industrials, state-owned enterprises reform, and the underground pipe network, but the performance of each has been short-lived and unsustained.

In the near future, the market will be in a correction stage and indices may fluctuate in a narrow range. The reasons are: 1. The CSF needs to hold the market to prevent stock market risk from spreading to the banking system, which will have relatively significant effects on the market in the short term as it can lead to a consensus expectation for the market bottom. 2. Considering the deleveraged state of the market, low equity allocation of private equity funds, and relatively low equity allocation of mutual funds, there is no strong catalyst for a significant selloff. 3. Actions such as IPO suspension, refinancing, and holdings reduction by major shareholders have halted the liquidity drain from the market. 4. Investors will be hesitatnt to enter the market due to the absence of a market highlight and a lack of income effect stemming from factors such as the poor state of the economy, the persistent stock bubble, and worse-than-expected reform policies progress.

We believe that after this period of volatility, the phenomenon of individual stocks all rising and falling together will end. Soon, directions for individual stocks will obviously diverge. Stocks that lack fundamental support will fall further, while stocks in three areas have the significant growth potential. Our direction for the month of August is as follows: 1. Industry leaders that may capitalize on IPO suspension to rapidly expand through mergers and acquisitions. 2. State-owned enterprises with much room for improvement or those with significant assets outside of the system since the expectation is that more aggressive state-owned enterprises reform policies will facilitate the reform process. 3. Companies that have much room to grow that are emerging from promising industries such as internet healthcare and e-finance as innovation continues. We will focus on our bottom-up selection process.