

# Fund Manager Perspective

06 July 2015

Last week, the China stock market tumbled, with all indices experiencing significant losses. The Shanghai Composite Index closed down 12.07% at 3686.92, while the Shenzhen Component Index finished the week 14.95% lower at 12246.06. The SME Board dropped 13.30% to 8068.07 and the ChiNext Index fell 10.80% to 2605.28.

There is urgent need to restore investor confidence as this round of declines display obvious characteristics of irrational sentiments, aggravated by surfacing market inefficiencies. In terms of investing, it is pointless to hold a bearish view at this point. Instead, we recommend believing that government policies are able to correct market inefficiencies. However, after this round of volatility, significant differentiation of assets will surely begin. Flimsy stocks will not make it out of this round, while solid stocks will form the cornerstone of core allocations.

This is an unforgettable weekend for China's capital market. Deleveraging triggered a panic and the stock market crashed, possibly triggering some forms of financial crisis. Over the weekend, regulators worked closely with financial institutions to come up with plans to prop up the market. The plans involve 21 brokerages pumping 120 billion RMB into Blue Chip ETFs, the temporary suspension of IPOs and Central Huijin Investment bailing out the market. The final touch to signal the end of the short term market liquidity crisis was the announcement that the PBoC will inject capital into the China Securities Finance Corporation to help stabilize the stock market.

We expect the stock market to return to rallying this week. Having experienced a memorable shock, the market will return to a normal leverage ratio range. More rapid leverage-driven rallying seen in the first half of the year will be unlikely, structural partitioning will become the main feature in the second half of the year.

