Fund Manager Perspective

September 2015

The market faced a second significant slump after the stock market crash. The first half of the month saw steadily climbing of a weak market, but on August 18th the Shanghai Composite Index sharply fell, losing 26.2% in the span of 7 business days. Over the entire month, the Shanghai Composite Index fell 13.5%, the Shenzhen Component Index fell 14.9%, the SME Index fell 14.1%, and the ChiNext index tumbled 25.9%.

This slump is August is more detrimental than the first wave of selling that began in mid-June. On the one hand, the sharp decline was faster this time, leaving no time for investors to respond; on the other hand, no individual stocks or industry sectors proved resistant or showed significant excess returns during this slump. Although on August 26th the central bank announced additional cuts to the interest rate and reserve requirements, it was unable to turn the market around. As the fantasy of a successful bailout crumbles, the market enters a new stage of finding the bottom.

The reason for all this is the myriad of changes in the last month that occurred internally and externally in the A-share market. Investor were worried about the low industrial production growth data released in July, while the sudden 1.9% depreciation of the RMB by the central bank caused concerns regarding RMB devaluation. The global capital market also followed with a significant correction. At the end of August, a number of senior officers of CITIC Securities, once portrayed as the state champion for the market bailout, received requests to assist in investigating the market meltdown, complicating the entire political and economic environment. At the same time, the stock market continued to fall further, leading to the large scale discounting of classified leveraged funds, which further increased selling pressure.

Since the peak on June 15th until the end of August, the market had experienced two rounds of large corrections. The low point of the Shanghai Composite Index was 2850.7, almost half of 5178.2 from where it started. Around 40 stocks dropped below issue price, while valuation indicators like PE have returned to a lower level comparable to last year and even the year before. In terms of absolute value, it is true that many companies and stocks have fallen into the value investment range; with a vast majority of institutional investors' positions close to the lower limit and signs of overreaction in terms of market panic, the market may hit bottom soon.

In terms of investments, we believe that right now it is imperative to strictly select individual securities. Only companies that are in line with industry developments, have excellent management teams, have relatively fast growth, and the price of which has stayed in the value investment range are worth buying and holding. From a sector allocation viewpoint, the structural adjustment of the healthcare industry has continuously contributed potentially quality growth companies in the medical services field. The performance of the entire new energy vehicle supply chain has also quietly provided new stimulants for the economy.

At this point, we believe that, despite rampant short sells and a bleak market, we will soon reach the light at the end of the tunnel.