Fund Manager Perspective

January 2015

The market was in a volatile state in December 2015, repeatedly fluctuating. Throughout December, the SSE Composite Index rose by 2.7% and the ChiNext Index was up 1.6%. The sectors that showed superior performance include real estate, catering and tourism, home appliances, and other value-type assets. The investment themes that outperformed include virtual reality, autonomous cars, cloud computing, and other emerging industry segments. Individual stocks that saw strong gains in earlier months saw adjustments in December as market risk appetite declined.

Most notable in December was the asset revaluation of select value stocks. We noticed that against the backdrop of asset shortage, many insurance companies purchased value assets at yearend; in a short period, funds of investment companies flooded into many individual stocks on the secondary market, triggering major changes in shareholder structure. Under the backdrop of asset shortage being the market norm in the next few years, the "Outsider Barbarians" phenomenon[1] reflects that the mid- and long-term value of quality bull stocks in traditional industries will be gradually exposed.

Looking into January 2016, we expect the market to remain volatile, segmented, and lacking in trend opportunities as we proactively seek structural opportunities during the adjustment.

On the one hand, it is increasingly clear that there will be oversupply pressure on the securities market in the upcoming period and that investors should watch out for adjustment risk for stocks facing relatively strong selling pressure. The stock market crash that occurred during the middle of last year postponed holding reductions for many non-tradable shares. The postponement is due to mature in January and pressure may rise from concentrated holding reductions. In addition, due to the implementation of new IPOs rules, the issuance of new stocks may accelerate and increase market supply leading to increased pressure on the market's valuation overall.

On the other hand, from a mid to long-term perspective, the stock market still holds strong appeal. The "asset shortage" phenomenon remains relatively widespread in 2016 and the risk/reward ratio of A shares is more attractive than that of other asset classes. At the same time, the direction of the Chinese economy's innovation and transformation development, and emerging industries compatible with this trend will produce quality enterprises with continuous growth prospects, which can provide good investment returns.

Concerning specific investment directions, we are optimistic about three directions. First, the upgrade of the consumption structure. The sustained rapid growth of new consumer industries such as media, health services, outbound tourism, and sports and education supplies provides ample investment opportunities. Second, innovation-driven industries, including the integration of traditional industries and the Internet, intelligent equipment and Industry 4.0, and innovative business models. Third, investment opportunities in traditional industries. Driven by supply-side reforms and state-owned enterprise reforms, merger and acquisition efforts in traditional industries will increase. This will improve the industry structure and investment opportunities will arise from leading firms that benefit from industry consolidation and exhibit rising P/E as well as EPS.

[1]The "Outsider Barbarians" phenomenon refers to the situation when players traditionally not heavily-associated with a market enters and accumulates a relatively significant amount of holdings.

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