Fund Manager Perspective

March 2015

There were only 3 weeks of trading days during February due to Chinese New Year. The market was mostly steady in the first two months of 2016, showing signs of rebound, but taking a severe dive in the last week.

Due to the looser monetary environment and lower likelihood of a US interest rate hike in early February, the market experienced a 2 week-long rebound and lasting investment themes including supply-side reform emerged. Statistics disclosed later in the month indicated that domestic industrial production continued to shrink, while there is continued inflation due to looser monetary policy. As the increased liquidity hasn't effectively entered the real economy, subsequent monetary policy expectation depends heavily on the central bank's quantitative market operations and reserve ratio adjustments. While the marginal effect of the above mentioned factors on the stock market is decreasing, the stock market lacks the fundamentals for a prolonged rally in nature. Meanwhile, the sharp rise in US inflation re-heated the expectation of US dollar interest rate increase and fuelled the US dollar index. These external factors lead to the tumbling late this month. Due to the policy loosening up for the real estate market in tier 2 and tier 3 cities, property prices in the tier 1 and tier 2 cities spurt this month. The buzzing real estate market distracted capital from the stock market to a certain degree. The effect will warrant more attention should the real estate market continue to heat up.

In February, large-cap stocks outperformed small-cap stocks. Representing large-cap stock indices, the SSE Composite Index lost 1.81% and the CSI 300 index dropped 2.33%. Meanwhile, the CSI 500 index, SME index and ChiNext Index, which represent small-cap stocks, decreased 2.17%, 4.38% and 5.17% respectively. In terms of industry performance, those that represent supply-side reform such as non-ferrous metal and mining industry, as well as those that are affected by culture cycles such as agriculture, forestry, animal husbandry, and fishery gained greatly. In comparison, previously well-performing industries such as media, telecommunications, and computers posted more significant losses. Overall, small-cap stocks showed larger fluctuation, gaining more relative to large-cap stocks in the first two weeks and falling more later in the month.

The market is at a delicate period. For one thing, the loose monetary environment and reform of supply-side policies will continue. Considering that the NPC and CPPCC are up-coming, current hotspots will likely not cool off. Additionally, the real economy is in a transitional period; traditional industries need to reduce capacity, a new direction for economic development is not set, and the stock market lacks the fundamentals for higher valuation. At the same time, external circumstances vary sharply, especially the changing expectation of US rate hike which constricts the scale of loosening monetary policy.

The market correction in late February indicates the market lacks the confidence for a continued rally and most of the activities lie in gaming with policies in certain sectors. The central bank lowering reserve requirements in the last day of the month is viewed as a move to influence sales in the real estate market. In March, close attention should be paid to the information released by the NPC and CPPCC. From a long-term perspective, the current market overall valuation remains low, but there are too many interference factors in the short run. Strategically, investors should focus on new information from both domestic and overseas markets, and seek interim investment opportunities brought about by the easing monetary policy and national economic transition.