Chief Investment Office

11 July 2025 **Equities**

China Strategy – Turning the Corner

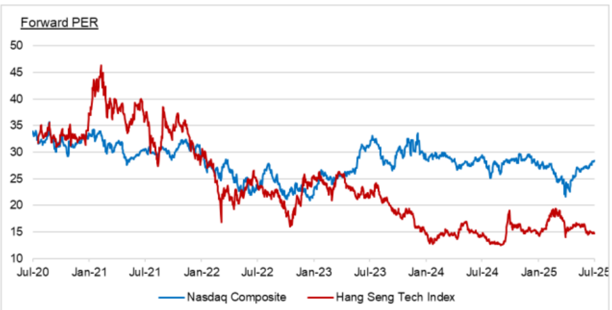
We had **upgraded HK/China market** to **Overweight** (*from Neutral*) in our 3Q2025 outlook. We believe that **Asia is a key beneficiary** of a **weaker US dollar** and **global rebalancing** with HK/China being **one of the markets** attracting inflows. Our Hang Seng Index (HSI) target is raised to **26,430** on the back of a re-rating to 11.2x PER (+1sd above 5-year mean).

Why Overweight China?

1. **Peak tariffs are likely behind us.** Chinese equities have shown resilience in the face of trade tensions, with the HSI up 20% YTD. From the unprecedented 145% peak tariffs to the 90-day US-China framework, there is clear evidence of de-escalation, although the situation remains fragile. Whilst **China's tariff will likely remain higher** than global averages, we believe **China is better prepared** to counter tariffs risks in Trump 2.0. Markets have also become **more de-sensitized** to bad news.

2. **AI remains a structural tailwind.** Sparked by DeepSeek's breakthrough in January 2025, **Gen-AI models are being rapidly integrated across diverse industries** in China, driving productivity gains and new avenues of growth. This has fueled the strong performance in the Hang Seng Tech (HSTECH) index (+16.8% YTD) outperforming the Nasdaq (+6.7% YTD) in 1H25. As Chinese AI capabilities converge with Western counterparts, we believe the **valuation disparity** between **HSTECH** (16.4x FY25F PER with 20% estimated earnings growth) and **Nasdaq** (31.5x PER for 6.9% growth) should also narrow.

Figure 1: HSTECH index trades at a discount to Nasdaq

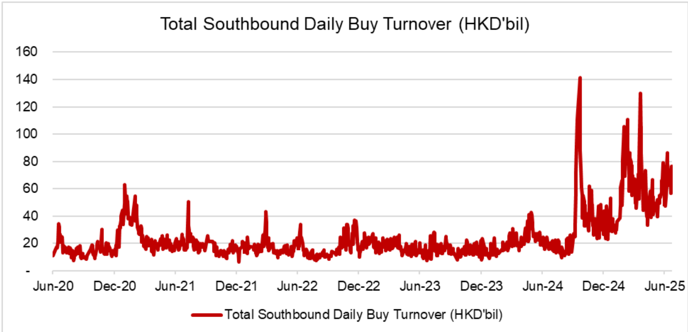


Source: Bloomberg (as at 10 July 2025)

3. **Of share buybacks, IPOs and the Southbound surge.** Government directive to increase shareholder value are driving **increase in share buyback**, offering crucial **downside support for the market**. **IPO momentum in Hong Kong** has seen a **remarkable surge in 1H25** with 44 IPOs raising USD14bn (8-fold jump from FY24's USD1.8bn). Notable IPOs in 1H25 include *CATL* (leading EV battery maker) and *Mixue* (China's top bubble tea chain). The momentum is **expected to sustain in 2H2025** with over 200 companies submitting applications, boosting market liquidity.

Southbound flows from mainland investors into HK equities rose to of USD90bn in 1H25, fueled by two factors - historically low sovereign bond yields of 1.66% driving investors to **higher-yielding assets** and **exposure to tech giants** that are not listed on the mainland.

Figure 2: Southbound flows surged since late 2024



Source: Bloomberg (as at 10 July 2025)

4. **Ample policy levers.** Since late September 2024, China has pivoted toward more pro-growth policies, **deploying liquidity** through rate cuts, **stabilizing capital markets**, **boosting consumption** through trade-in programs and raised its **fiscal deficit target to 4% of GDP**. We believe further stimulus will depend on outcome of tariff negotiations and we do not expect significant stimulus in the July Politburo meeting.

5. **Attractive valuations**. The HSI currently trades at **10.3x PER**, a discount to the MSCI EM ex-China's index at 13.6x PER and the S&P500 index at 22.2x PER, which could fuel fund flows due to relatively cheaper valuations.

How should investors position in China?

Stock baskets – reiterate **barbell strategy** of buying yielders and quality stocks on dips.

Southbound flows beneficiaries	AI/tech plays	Consumer laggards
China Mobile (941 HK)	Tencent (700 HK)	Yum China (9987 HK)
Ping An Insurance (2318 HK)	BYD (1211 HK)	Haidilao (6862 HK)
China Construction Bank (939 HK)	Trip.com (9961 HK)	
Link REIT (823 HK)	Sunny Optical (2382	
AIA (1299 HK)		
Hong Kong Exchange (388 HK)		

Funds & ETFs

Funds
Principal Greater China Equity
ETFs
Hang Seng China Enterprises Index ETF (2828 HK)
Tracker Fund of Hong Kong Ltd (2800 HK)
CSOP Hang Seng Tech Index ETF (3033 HK)

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