



華夏基金(香港)  
China AMC (HK)



# MARKET INSIGHTS

August 2024

Overall, at the end of July, the Political Bureau conveyed some positive policy signals. Emphasizing the increasing unfavorable economic conditions in terms of quantity, it confirmed the commitment to unwaveringly achieve the annual growth target and strengthen countercyclical adjustments as part of the reform and development tasks for the second half of the year. Fiscal stimulus in the second quarter noticeably slowed down, coupled with ongoing credit contraction in the private sector, exerting significant pressure on growth and the market. The recent 300 billion RMB issuance of special long-term government bonds to support equipment upgrades and consumer goods replacement is a very positive signal that can further boost fiscal stimulus. At a structural level, the Political Bureau meeting mentioned supporting the development of leading enterprises, preventing vicious competition, and focusing on boosting consumption to stimulate growth. The State Council also introduced further opinions on promoting high-quality development of consumption last Saturday, bringing structural opportunities through policy support.

## Market Performance

In July, the MSCI China Index continued to show weakness, ultimately falling by 0.57%. From a macro perspective, high-frequency data indicates an increase in summer travel volume with decreasing prices, resilient exports, but weak investment activity. Second-hand housing transactions strengthened in first-tier cities, while new home transactions remained weak. On July 1st, the central bank announced plans to conduct government bond repurchase operations in the near term, utilizing an open-ended, credit-based borrowing approach for government bonds. Depending on the bond market operations, they will continue to borrow and sell government bonds. On July 8th, the central bank announced plans to conduct temporary reverse repurchase or temporary repo operations as needed and narrow the interest rate corridor. On July 9th, Premier Li Qiang emphasized the need to reform unreasonable institutional mechanisms and stimulate innovation across society during discussions with economic experts and entrepreneurs. On July 21st, the full text of the "Decision" from the Third Plenum of the Twentieth Central Committee proposed various reform measures including new urbanization, land, fiscal and tax system reforms, promoting technological innovation, and expanding high-level opening up. On July 25th, the National Development and Reform Commission and the Ministry of Finance coordinated to allocate around 300 billion yuan in special long-term government bonds to support large-scale equipment upgrades and consumer goods replacement programs. On July 30th, a meeting of the Central Political Bureau emphasized the unwavering commitment to achieving the annual economic and social development goals, calling for sustained and more forceful macroeconomic policies.

	Jul Close	Monthly % Change	YTD %	52 Week Low	52 Week High
<b>Greater China Indices</b>					
CSI 300	3442.08	-0.57	0.32	3108.35	4058.24
MSCI China	56.60	-2.19	1.16	48.75	65.75
HSI	17344.60	-2.11	1.74	14794.16	19857.39
HSCEI	6107.16	-3.55	5.87	4943.24	6986.20
<b>Global Indices</b>					
S&P 500	5522.30	1.13	15.78	4103.78	5669.67
Dow Jones Industrial Average	40842.79	4.41	8.37	32327.20	41376.00
Nasdaq Composite	17599.40	-0.75	17.24	12543.86	18671.07
FTSE 100	8367.98	2.50	8.21	7215.76	8474.41
DAX 30	18508.65	1.50	10.49	14630.21	18892.92
Nikkei 225	39101.82	-1.22	16.85	30487.67	42426.77

## Economic Data

China's manufacturing PMI index edged down to 49.4 in July from 49.5 in June. Among major sub-indexes of NBS manufacturing PMI, the new orders sub-index edged down to 49.3 from 49.5, the output sub-index decreased to 50.1 from 50.6, while the employment sub-index rose to 48.3 from 48.1. The non-manufacturing PMI fell to 50.2 in July from 51.1 in June, with a deceleration of activity in both the construction and services sector in July. The services PMI decreased to 50.0 from 50.2. According to the survey, the PMIs of railway and airline transportation, postal, telecommunication and satellite transmission services industries were above 55, while the PMIs of retail sales, capital market services and real estate services industries were below 50 in July. The construction PMI fell to 51.2 in July from 52.3 in June. NBS commented that the construction activity was impacted by adverse weather conditions such as heatwave, heavy rainfall and floods in July.

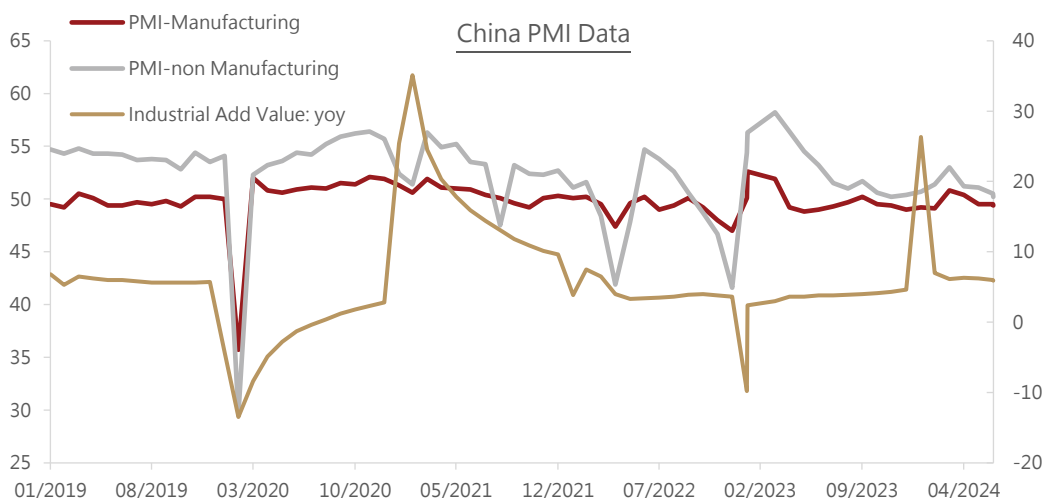
## Outlook

Looking forward, we maintain our long-term positive view of the Chinese equity market. Overall, at the end of July, the Political Bureau conveyed some positive policy signals. Emphasizing the increasing unfavorable economic conditions in terms of quantity, it confirmed the commitment to unwaveringly achieve the annual growth target and strengthen countercyclical adjustments as part of the reform and development tasks for the second half of the year. Fiscal stimulus in the second quarter noticeably slowed down, coupled with ongoing credit contraction in the private sector, exerting significant pressure on growth and the market. The recent 300 billion RMB issuance of special long-term government bonds to support equipment upgrades and consumer goods replacement is a very positive signal that can further boost fiscal stimulus. At a structural level, the Political Bureau meeting mentioned supporting the development of leading enterprises, preventing vicious competition, and focusing on boosting consumption to stimulate growth. The State Council also introduced further opinions on promoting high-quality development of consumption last Saturday, bringing structural opportunities through policy support.

In terms of portfolio positioning, we will continue to seek a balance between value and growth. We continue to focus on the long-term policy beneficiaries (e.g. software localization and advanced manufacturing) and economic recovery-related opportunities (e.g. consumer, Internet, and financials). We will prudently pay attention to some thematic opportunities, including AI and SOE re-rating.

## Risk

Sino-US relationship worsens than expectation. International geopolitics worsens than expectation; China's economy recovers less than expected.





The market's recent focus remains on the election trade, rate cut expectations, and the reversals stemming from the divergence in monetary policies across different countries. Although our base case remains a Trump victory and a divided Congress, the market consensus "Trump trade" may experience some interim reversals, impacting the overall market trading style as well as long-term fiscal policies and trade dynamics. On the rate cuts, the market's current speculation has evolved to focus on the magnitude of the September rate cut. We believe the probability of a synchronized and rapid deterioration across various industry labor markets is not high. Additionally, Japan's rate hike and yen appreciation have resulted in a significant reversal of the carry trade strategies, potentially impacting related risk assets. We believe this round of carry trade reversal may have reached a temporary pause, but in the medium term, the yen and other Asian currencies still have room for appreciation, while the pressure from early rate cuts in Latin America and other regions may relatively alleviate as developed markets generally enter an easing cycle as well.

## Market Performance

July saw some major shifts in market participants' trading themes. The trading strategies linked to the U.S. election outcome, the pullback in large-cap tech stocks, and the reversal of the yen carry trade have all contributed to substantial volatility across various risk assets. Softer inflation and employment data have led the market to anticipate the Federal Reserve beginning rate cuts in September, with Powell's implied rate-cut leanings at the month-end FOMC meeting further cementing these expectations. By the end of the month, the market had priced in over 70 bps of rate cuts for the year. During this period, fixed income assets, particularly U.S. Treasuries, has outperformed equities and commodities, with the U.S. dollar index declining by over 1.5% for the full month.

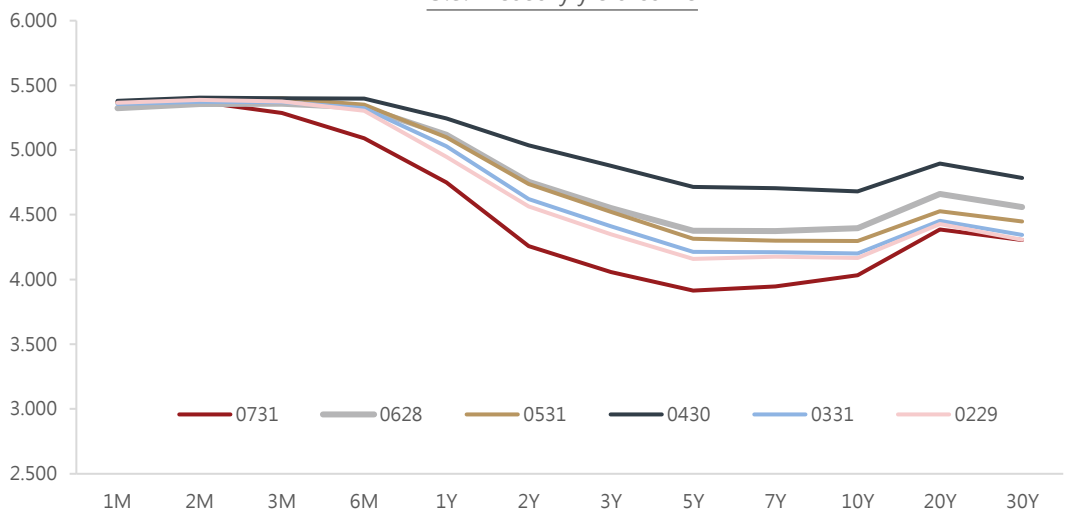
United States	Last Price %	1M chg bp	YTD chg bps	52W low%	52W high%
2Y	4.26	-50	1	4.11	5.26
5Y	3.91	-46	7	3.75	4.99
7Y	3.94	-43	6	3.78	5.03
10Y	4.03	-37	15	3.78	5.02
30Y	4.30	-26	27	3.94	5.18

China	Last Price %	1M chg bp	YTD chg bps	52W low%	52W high%
3Y	1.68	-12	-61	1.65	2.53
5Y	1.87	-11	-53	1.83	2.64
7Y	2.00	-11	-54	1.95	2.75
10Y	2.15	-6	-41	2.11	2.74
30Y	2.38	-4	-45	2.33	3.03

Japan	Last Price %	1M chg bp	YTD chg bps	52W low%	52W high%
2Y	0.46	9	40	0.00	0.47
5Y	0.67	8	46	0.16	0.68
7Y	0.81	8	45	0.30	0.83
10Y	1.06	0	44	0.56	1.11
30Y	2.18	-8	54	1.48	2.31

Germany	Last Price %	1M chg bp	YTD chg bps	52W low%	52W high%
2Y	2.53	-30	13	2.36	3.36
5Y	2.23	-25	28	1.86	2.93
7Y	2.17	-30	23	1.83	2.94
10Y	2.30	-20	28	1.89	3.03
30Y	2.51	-18	25	2.12	3.26

U.S. Treasury yield curve



# Fixed Income



In July, U.S. Treasury yields declined across the curve, exhibiting a bull-steepening trend. The 2-year Treasury yield fell significantly by 50 bps to its year-start level, while the 10-year yield dropped 37 bps to 4.03%. Rate cut expectations and the shifting Trump trade were the core factors driving the U.S. bond market. The weakening of the U.S. dollar and the high-level pullback in U.S. equities also supported the performance of Treasuries. In the credit market, the global primary market has rebounded notably, with overall credit spreads only marginally widening due to the rapid decline in underlying yields, as they were largely unaffected by macroeconomic factors and movements in other asset classes. High-yield bonds in emerging markets continued to deliver strong performance, and the global investment-grade bond index surged 2.76% in July, bolstered by the decline in interest rates.

CDX Index	Current Value	1M chg bp	YTD chg bps	52W low%	52W high%
IG CDX	52	(2)	(5)	48	83
HY CDX	331	(13)	(26)	309	533
EM CDX	169	(5)	18	155	247
<b>Bond index</b>					
ICE Asian Dollar Corporate	465	1.8%	4.5%	416	467
ICE China Issuers Dollar IG Corporate	218	1.8%	3.8%	198	219
ICE China Issuers Dollar HY Corporate	177	1.8%	15.6%	143	177
ICE US Corporate	3317	2.4%	2.4%	2929	3326
ICE US High Yield	1664	2.0%	4.6%	1457	1664
ICE Emerging Markets Corporate	452	1.8%	4.4%	401	453
Bloomberg Global-Aggregate	469	2.8%	-0.5%	429	473
Bloomberg Global-Aggregate 1-3 Year	175	1.7%	0.4%	166	175





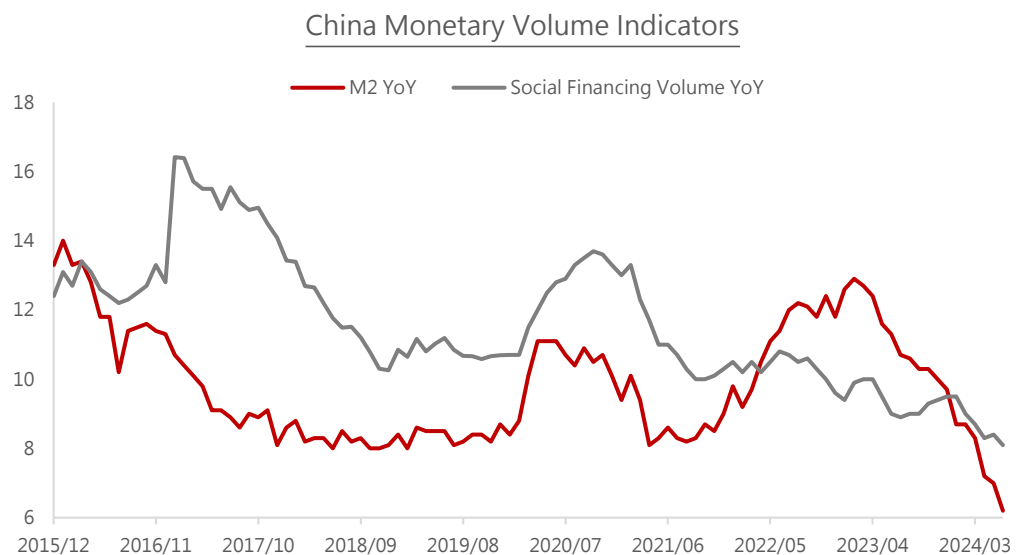
## Economic Data

In July, U.S. inflation data continued to cool, with core CPI and PCE year-over-year declining to 3.3% and 2.6% respectively. Excluding the impact of immigration, several employment data points further signaled a softening labor market, with the unemployment rate reaching 4.1%. The Federal Reserve highlighted the increased importance of employment in its monetary policy decisions during the FOMC meeting. Consumer spending has remained relatively resilient, outperforming expectations, but the market appears to harbor some doubts about the sustainability of this trend. In the high-interest rate environment, investment components like industry and real estate have exhibited relatively weaker performance. In other markets, European economic data for the second quarter was slightly better than market expectations, with the ECB maintaining its policy stance. Meanwhile, Japan continues to face elevated inflationary pressures, and the Bank of Japan responded with a 15 bp rate hike, ensued by a significant appreciation of the yen.

## Outlook

The market's recent focus remains on the election trade, rate cut expectations, and the reversals stemming from the divergence in monetary policies across different countries. As Biden withdraws and Harris's nomination gains more recognition within the Democratic Party, the gap between the two parties has been gradually narrowing towards the end of the month. Harris's vice-presidential nomination and her own characteristics may introduce some disturbances to the electoral prospects in the swing states. Although our base case remains a Trump victory and a divided Congress, the market consensus "Trump trade" may experience some interim reversals, impacting the overall market trading style as well as long-term fiscal policies and trade dynamics. On the rate cuts, the market's current speculation has evolved to focus on the magnitude of the September rate cut. We believe the probability of a synchronized and rapid deterioration across various industry labor markets is not high currently. Unless there is a significant risk asset selloff, the overly aggressive rate cut expectations may see a temporary pullback. Additionally, Japan's rate hike and yen appreciation have resulted in a significant reversal of the carry trade strategies that had been effective for an extended period, potentially impacting related risk assets. We believe this round of carry trade reversal may have reached a temporary pause, but in the medium term, the yen and other Asian currencies still have room for appreciation, while the pressure from early rate cuts in Latin America and other regions may relatively alleviate as developed markets generally enter an easing cycle as well.

On the interest rate front, the yield curve is expected to continue steepening for the remainder of the year, with the 10-year and 2-year yield spread having the potential to turn positive after the first one or two rate cuts. As the rate cut trajectory is predicated on a soft landing assumption, the downward speed and magnitude of short-end rates will not be substantial in the initial stages of rate cuts, thereby limiting the downside potential for long-end yields as well. The ability of the 10-year yield to break below 4% may determine the trading range for US Treasuries in the near term, and the overall interest rate volatility is expected to gradually narrow in the second half of the year. In terms of credit, the underlying fundamentals of US corporates have been largely healthy in the first half of the year, whether it is net interest margins, non-performing loan ratios, capital positions, or corporate revenue, profits, and leverage. However, some industries have seen a downward revision in their guidance. From a valuation perspective, we have observed that 'all-in yield' buyers have continued to provide support, preventing a significant widening of credit spreads during the rate decline. While we still see valuation downside risks, the natural hedge between credit spreads and benchmark rates as inflationary concerns subside may enhance the medium-term risk-adjusted performance of credit. From a technical perspective, the increased new issuance supply in July has been well-absorbed, and the impending rate cuts are expected to be relatively favorable for fixed income assets compared to other asset classes, providing continued support. Assuming a smooth rate cut trajectory leading to an economic soft landing, we are currently adjusting our views to be relatively cautious on interest rate duration and neutral on credit duration, seeking relative value opportunities in the differentiated industries and regions.





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