

# Market Strategy

*January 2010*

## MARKET OUTLOOK

*Maintain year-end target for the HSI at 27,000*

The “exit strategy” of central banks and interest rate hikes in the U.S. will be major overhangs for the stock market this year. Nevertheless, strong GDP growth in China and potential appreciation of the renminbi will continue to attract inflow of funds into China and Hong Kong. We stick to our year-end target of 27,000 for the Hang Seng Index and consider 21,000-22,000 as a good entry point for long-term investors. Listed companies with better earnings visibility and growth momentum are likely to outperform. China banks, upstream oil & gold, auto, food & beverage and pharmaceutical stocks remained our favorites. Top picks are ICBC (1398), CCB (939), PetroChina (857), Zijin Mining (2899), Dongfeng Motor (489), Mengniu Dairy (2319) and Sinopharm (1099).

*Short-term trading : long container shipping and short China property developer*

China will release economic data for December later this month which are expected to show a remarkable improvement in foreign trade, faster inflation, sharp increase in property prices and robust retail sales. The expectation of recovery in exports may boost share prices of container shipping companies such as CSCL (2866) and Orient Overseas (316) in near term. Skyrocketing property prices may arouse market fears of further tightening measures on the property market. We recommend that investors should underweight China property developers although their share prices have dropped more than 20% from 52-week highs.

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## MARKET REVIEW

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*Global stock market rally continued in December despite a rebound in the US dollar*

Continued recovery in the global economy sent major stock markets higher in December despite a rebound in the US dollar. Dow Jones industrial average, Nasdaq, FTSE 100 and Nikkei 225 surged 0.8%, 5.8%, 4.3% and 12.8% respectively. Shanghai SE Composite Index advanced 2.6% but the Hang Seng Index gained only 0.2%. Spot gold price hit record high of US\$1,226 an ounce in early December and then declined some 10% to close at US\$1,097 an ounce at end-2009. Average crude oil futures price decreased by 4.6% from US\$78.2 a barrel in November to US\$74.6 a barrel in December. US dollar rose 4.5%, 1.5% and 7.9% against the euro, the pound sterling and the yen respectively.

*Coal, steel, cement and airline stocks outperformed*

Foxconn (2038), the best performing constituent of the Hang Seng Index in December, climbed 35% thanks to a strong recovery of business. China Resources Enterprise (291) soared 17% since it managed to sell its interest in a retail joint venture to Esprit (330) at an extremely high price. Tencent (700) added 18% on rumour of takeover by China Mobile (941). Coal, steel and cement stocks generally gained 8%-11% driven by the rise in coal and steel prices in China over the past two months. Air China (753) and Cathay Pacific (293) both increased 9% along with the recovery in passenger traffic.

*China banks underperformed amid worries about tightening credit*

Five largest China banks plunged 2%-4% as investors worried about tightening credit in 2010. Dongfeng Motor (489) slumped 6% due to profit taking. Insurance companies showed mixed performance. PICC P&C (2328) jumped 12% but China Life (2628) and Ping An Insurance (2318) shed 1% and 6% respectively. Strengthening US dollar weighed on gold and oil prices. PetroChina (857) fell 3%. Zijin Mining (2899) and Jiangxi Copper (358) lost 7%-9%. Power companies suffered from rising coal price. Huaneng Power (902), Datang Power (991) and China Resources Power (836) therefore shrank 2%-9%. Telecom, railway and power equipment stocks were almost steady because of their defensive nature.

*Increasing policy risks depressed China property developers*

The Chinese government introduced new measures on the property market in December including the withdrawal of sales tax incentive on resale of residential properties, lifting downpayment of land purchases to 50% and revising production target of social welfare houses from 7.5mn units by end-2011 to 15.4mn units by end-2012. Growing policy risks depressed performance of China property stocks during last month. Top tier developers like China Overseas Land (688), China Resources Land (1109) and Country Garden (2007) decreased 1-2% whilst Shimao Property (813) was unchanged. Poly HK (119) and Sino-Ocean Land (3377) cut 12% and 7% respectively. Newly listed developers such as Evergrande (3333) and Longfor (960) advanced 6% and 10% respectively due to analyst upgrades. Hong Kong property developers, except SHK Properties (16), outperformed the benchmark index given anticipation of good land auction results on December 28.

## Stock Performance Summary for December 2009

Sector	Stocks	% chg in share price in Dec 09	Reasons
	Hang Seng Index (21,872)	+0.2	Rebound in US dollar capped the upside of stock markets
	HSCEI (12,794)	-1.4	
<b>Outperform</b>			
Miscellaneous	Foxconn (2038)	+35	N/A
	Tencent (700), China Resources Enterprise (291)	+17 to +18	
	HK & China Gas (3), China Merchants (144)	+5 to +6	
HK property	Cheung Kong (1), Sino Land (83), Wharf (4), Swire Pacific (19), Hang Lung Properties (101), Henderson Land (12)	+3 to +8	Expectation of positive land auction results on December 28
Coal	China Coal (1898), Yanzhou Coal (1171)	+8 to +11	Expectation of rising coal price in 2010
	China Shenhua (1088)	+0	
Steel, cement	Angang Steel (347), Maanshan Iron & Steel (323), Anhui Conch (914), CNBM (3323)	+8 to +9	Rebound in steel price since mid-October
Airline	Air China (753), Cathay Pacific (293)	+9	Gradual recovery of business
<b>In line/ Mixed</b>			
Insurance	PICC P&C (2328)	+12	Change in accounting rules on insurance contracts in 2010
	China Life (2628), Ping An Insurance (2318)	-1 to -6	
Oil	CNOOC (883), Sinopec (386)	+2 to +7	Decline in crude oil price in the first half of December
	PetroChina (857)	-3	
HK banking	HSBC (5), Hang Seng Bank (11), BOC HK(2388)	-1 to +1	Profit taking on Bank of East Asia before share placement
	Bank of East Asia (23)	-8	
China property	China Overseas Land (688), Shimao (813), Guangzhou R&F (2777), CR Land (1109), Shui On Land (272), Country Garden (2007), Glorious Property (845), Greentown (3900)	-2 to +1	Strong government measures to stabilize property prices
	Evergrande (3333), Longfor (960), Agile (3383)	+6 to +10	
	Sino-Ocean Land (3377), Poly HK (119)	-7 to -12	
Shipping	China Shipping Development (1138)	+2	China Cosco issued profit warning for 2009 fiscal results
	China Cosco (1919), CSCL (2866)	-2 to -7	
Power equipment	Harbin Power (1133), Shanghai Electric (2727)	-1 to -2	Defensive stocks
Telecom, railway, HK utilities	China Mobile (941), China Unicom (762), CLP Holdings (2), HK Electric (6), China Railway Group (390), CCCC (1800)	-1 to +0	Defensive stocks
<b>Underperform</b>			
China banking	ICBC (1398), CCB (939), BOC (3988), CMB (3968), BoComm (3328)	-2 to -4	Worries about tightening credit
Non-ferrous metal	Jiangxi Copper (358), Zijin Mining (2899)	-7 to -9	Rebound in US dollar weighed on commodity prices
	Chalco (2600), CMOC (3993)	-0 to -3	
Power	Datang Power (991), Huaneng Power (902), China Resources Power (836)	-2 to -9	Victim of rising coal price
Miscellaneous	Dongfeng Motor (489), Cosco Pacific (1199)	-6 to -8	Technical correction



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