

Sun Hung Kai Financial forecasts stable global economic growth in H2

2016

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HSI to hit 22,800

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Asian equities to outperform

Global stock markets to be suppressed by uncertain political climate

Overview:

- Projected outlook for H2: global economy to display stable growth; Chinese economy to develop steadily; India to emerge as the fastest-growing major economy; the US to hike interest rates as early as in September; and Japan to see a likelihood of more quantitative easing in July
- A positive view on equities, with Asia offering a better investment outlook
- Major indices' target levels: HSI at 22,800; HSCEI at 9,800; and Shanghai Composite at 3,400
- Investment themes for Hong Kong equities: (1) consumption upgrade; (2) industrial transformation; and (3) southbound fund flows
- Global stocks suppressed by uncertain political factors over the world with an extended high volatility of asset prices

14 June 2016, Hong Kong — Sun Hung Kai Financial Limited (“SHKF” or “Sun Hung Kai Financial”) expects the global economy to chart a stable path of growth in H2 2016. Further, among the developed markets, the US may see improvement in its economic activity compared with Q1. Its GDP in 2016 may expand at a slower pace than in 2015, yet it is projected to lead Japan and Europe in economic growth. As far as monetary policy is concerned, according to SHKF’s forecasts, the US will wait until September to raise interest rates and it is possible that Japan will scale up quantitative easing (QE) in July. On the emerging market front, economic performances of different countries may continue to vary, with Asia presenting better prospects; concurrently, there are chances that India will emerge as the world’s fastest-growing major economy, and China will be able to maintain a stable growth.

Kenny Wen, Wealth Management Strategist of SHKF, says, “We maintain our forecast that the US will only hike rates at a slow or measured pace. Moreover, it is expected that US economic activity and the global investment climate will not be dampened by the US rate increase. With the global economy showing hopes of moderate expansion, stock markets may climb higher, and we are particularly optimistic about the investment outlook in Asia.” While taking a bullish view on the future, Kenny points out uncertain economic and political circumstances could suppress global stock markets from now to the end of the year, for instance, the Brexit referendum and the US presidential election, by which the high volatility of asset prices will be extended.

Regarding investment deployment, Kenny highlights two major investment themes for the second half of 2016. First, it is the “relocation of the world’s factories”, calling for attention to investment opportunities in the Association of Southeast Asian Nations (ASEAN) and Indian markets. Next, due to a lengthened see-saw in asset prices in projection, it would be to “reduce risk via diversification”, in the light of which Asian high-yield bonds and gold flag capital appreciation potential in volatile market conditions.

Hong Kong equities: Dramatic range-bound movements; target level for HSI: 22,800; three major themes

Based on SHKF’s internal valuation model, and factoring in the diminishing effects of monetary policy and the rising default risk in China, SHKF has revised down the end-of-2016 target level for the HSI to 22,800. Moreover, in the second half of the year, Hong Kong stocks are forecast to swing up and down in a large horizontal range to exhibit an “up-down-up” pattern. In the same period, the HSCEI is expected to reach the level of 9,800, and the target for Shanghai Composite is revised to 3,400. The investment themes for Hong Kong stocks in 2016 include: (1) consumption upgrade; (2) industrial transformation; and (3) southbound fund flows. Investment opportunities derived from these themes are concentrated on China sports stocks as well as e-commerce, online payment, high-end manufacturing and brokerage stocks, along with individual stocks with a favourable valuation.

Chinese economy: Towards stabilisation; transformation to be stepped up; new economy as lighthouse for growth

Several economic leading indicators hint at stabilisation of the Chinese economy in the coming few months. China’s May official manufacturing purchasing managers’ index (PMI) remained at 50.1, inside the expansionary zone for 3 consecutive months. 8 of the 12 Chinese economic leading indicators tracked by SHKF such as new orders, output and inventories registered improvement. This suggests comprehensiveness in China’s economic stabilisation. PMI data normally precedes GDP figures by one quarter, and hence it is projected that the Chinese economy is on track for a soft landing. China is in the “transition from old to new economy”. The Chinese government will probably step up efforts to facilitate economic transformation. Overseas capital may flow into China and Hong Kong stocks to capitalise on the advancing Chinese economy, which will drive up valuations, a key support factor for stock prices.

However, senior officials in the Chinese government have implied China’s policy target keywords have shifted from “stable growth” to “reform and transformation”. It is therefore forecast that the People’s Bank of China will only cut the required reserve ratio once by the end of 2016. Less aggressive monetary policy may intensify credit risk in China, and that will lessen investors’ risk appetite, confining the upward momentum in China’s and Hong Kong’s stock markets. The three quarters from April note the peak payback period of Chinese bonds maturing in one year from now. Corporate default risk has been on the rise against a background of backward capacity elimination. Cyclical and old economy stocks will be dragged down as a result. The risk, nevertheless, remains manageable because government measures including local debt replacement and debt-equity swaps are helping reduce financing costs.

ASEAN: Manufacturing and trading in parallel development; future to focus on profit growth

With China’s economic transformation, in the medium/long run, manufacturing enterprises may relocate their factories to ASEAN, in which the ASEAN economies will benefit. The comparatively lower labour costs in ASEAN, for example, the average manufacturing wage in Vietnam is only half of that in China’s coastal cities, coupled with its young population structure and vigorous policy to facilitate infrastructure construction, provide the right fundamentals for manufacturing industry

development. ASEAN also flashes positive factors of better profits and stabilising exchange rates. The region's investment outlook in H2 is encouraging. The target for the MSCI South East Asia Index is 760. Investors may consider buying ASEAN stocks at lows.

India: Continues to lead the world in economic momentum; stock market buoyed up by more rainfall

Apart from ASEAN, India is another beneficiary from China's economic transformation. Indian Prime Minister Modi has been promoting structural reforms since elected, which include manufacturing sector development and the launch of the Make in India programme to create jobs to boost medium/long-term economic growth. What's more, drought conditions in the country may ease; subsequently, food prices and inflationary pressure may go down, paving for a possible rate reduction by the Indian central bank in H2. The International Monetary Fund (IMF) estimates the Indian GDP growth rate to be 7.5% for both the 2016 and 2017 fiscal years, making India one of the fastest-growing economies. Coupled with rate cut expectations, Indian stocks are forecast to be buoyed up in H2, and the SENSEX may rise to 29,000.

US: Slow rate hike path will not stifle economic activity; uncertain politics dent investment attractiveness

The Federal Reserve (Fed) may wait until after the Brexit referendum produces an outcome in late June and the US Q2 GDP growth rate is released to decide on its rate hike path, that is, a verdict in September, and only one rate increase is predicted for 2016. US presidential election contenders Donald Trump and Hillary Clinton have garnered similar support rates. The uncertain political climate may send US stocks lower. Although the US economy may post a growth rate higher than Q1's 0.8% in H2, the US stock market faces limited upside with rate hike and political uncertainty and a high market P/E of 18x. The target for the S&P 500 in H2 is 2,080.

Europe: Brexit referendum impairs investment climate; scale-up of monetary policy unlikely in near future

The negative impact on the UK economy will be significant if the country departs from the European Union (EU). SHKF believes the odds are higher for the UK to stay in the EU as the UK public will eventually vote out of practical concerns. Yet, the vote to remain or leave the EU creates uncertainty that may depress the investment climate in Europe. The European Central Bank (ECB) has already expanded its QE programme in March. It is unlikely that the ECB will increase QE again in the short run. Without policy expectations, the European stock market lacks a reason to rise. The target for the MSCI Europe Index in H2 is 119.

Japan: Abe's three arrows create lots of noise but structural reforms produce meagre results

A number of Japanese economic indicators for April suggest the country has yet to come out of weak economic conditions. It is forecast that Japan will experience negative GDP growth again in Q2. Its core consumer prices dropped for the second month in a row. The Bank of Japan is expected to enlarge QE in July, however, that is estimated to give only short-term support to the Japanese economy and stock markets. The Yen has strengthened on heightened risk in the market, which may weigh on Japanese stocks further. Despite the possibility that the Nikkei 225 will climb to 17,300 in H2, the index may find it hard to stay above that level in the medium/long run and its upward potential is limited.

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About Sun Hung Kai Financial Limited

Sun Hung Kai Financial Limited (“SHKFL”), with its foundation dating back to 1969, is a 70%-owned subsidiary of Everbright Securities Company Limited (“Everbright Securities”, SSE: 601788).

Operating under the Sun Hung Kai Financial brand as well as the SHK Direct and SHK Private sub-brands, SHKFL has two core business segments, Wealth Management and Brokerage, and Capital Markets. It offers customised wealth management and investment solutions for retail, corporate and institutional clients. Backed by Everbright Securities, SHKFL provides greater access for Hong Kong and Mainland investors to a broad range of products and services.

SHKFL has an extensive branch and office network in Hong Kong, Macau and Mainland China, and offers a diversified financial trading platform to its customers. SHKFL, through its subsidiaries, currently has about HK\$82 billion* in assets under management, custody and/or advice. For more information, please visit www.shkf.com.

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This press release is based on views and opinions of the retail research team of Sun Hung Kai Investment Services Limited.