Investment Strategy Update

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6 July, 2020

China stock market rips ahead fueled by government support

- ♦ **The Shanghai and Shenzhen composite index is up 13% year-to-date in US dollar terms, more than it gained in the four years before 31 December.**
- ♦ **Entities connected to the Chinese government have been buying the biggest components of the index.**
- ♦ **The CSI 300 index rallied 5.7% today after an editorial in a Chinese paper suggested a healthy bull market would be beneficial for the country.**
- ♦ **Growing participation of retail investors could foreshadow more gains ahead, but the yuan and geopolitical risks could create a hurdle for the rally.**
- ♦ **FAB AAC remains overweight high-quality investment grade bonds.**

The Chinese stock market is not entirely freewheeling like its counterpart in the US. That may sometimes be frustrating for those seeking arbitrage but it can also help on occasion. Right now, the potential for more government support has just given it a major boost.

The CSI 300, otherwise known as the Shenzhen Shanghai Composite index, rose 5.67% today, leaving it up 14% year-to-date. In dollar terms, the index is up 13.1% year-to-date and rose 6.4% today alone. To put that in perspective, between 31 December 2015 and the same date in 2019, the index had risen a meager 2.3% in dollar terms, as the yuan weakened and stocks suffered with the trade war.

Today's rise was driven by an editorial in the China Securities Journal which said that fostering a healthy bull market is now more important than ever.

For Chinese retail investors, that seems to have been the green light to buy, with several indicators of participation flashing up today. That is good news for Chinese shares. The last time mom-and-pop investors in China got involved in the stock market was in the first half of 2015, when the CSI 300 rallied 51% from 31 December, 2014, to 12 June, 2015, before dropping 43.3% between that date and 26 August. Back then, the government popped the bubble by restricting margin trading in June to curb the excessive speculation.

This time Beijing may be doing the opposite as it faces the prospect of being ostracized by US investors. Chinese pension funds and sovereign wealth funds have already increased their holdings of the largest components of the CSI 300 over the past three months, helping to boost the entire index. Unlike 2015, this time Beijing might welcome the help from its main street investors and be happy to ensure they get good returns.

The CSI 300 has risen 14% so far this year after gaining only 9.8% in the past four years

On the other side, the gains — which now have outpaced those of all major US indices — may further embolden politicians in Washington to attack Beijing.

Last week, the US Congress had already passed a law that could impose sanctions against anyone who does business with members of the Politburo, which would include China's lenders. That law is expected to be signed by President Donald Trump this week.

The President himself had weighed on pension funds of federal workers to sell all their holdings of Chinese investments and was trying to widen out the pressure to other asset managers. Meanwhile, Beijing is trying to tell everyone that they are just fine without the Americans.

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