



Aberdeen

# China/Hong Kong Update

## Market Overview

- China and Hong Kong equities rebounded in June, despite fears that China's growth may stall because of both regulatory tightening in the domestic property sector and the implementation of austerity measures in Europe.
- Sentiment was particularly buoyed, albeit temporarily, by Beijing's decision to increase the flexibility of its exchange rate. While largely symbolic, the move nonetheless demonstrates a willingness to resume currency reform. Also, a gradual and orderly rise in the yuan over the medium term should encourage domestic demand and redress economic imbalances.
- Separately, the mainland's banking regulator warned of rising bad debts. It ordered big lenders to conduct quarterly stress tests on property loans, while rules to regulate financing entities associated with local governments were also issued.
- At the same time, Beijing raised domestic natural gas prices, but lowered fuel prices because of cheaper crude oil costs. China and Taiwan also signed a trade pact to boost commercial ties.
- Increasingly, investors are turning pessimistic about the Chinese economy in light of signs of moderating growth; the Shanghai Composite Index has slumped by approximately 26% since the start of the year. As well as domestic policy tightening and weak export markets, there are fears that fundraising by Chinese banks could overwhelm demand – and drag prices lower. Yet we maintain our firm belief in our holdings' bright medium-term prospects, given their balance sheet strength and management quality.

## Model Portfolio News

During the month, we topped up China Resources Enterprise and XinAo Gas on price weakness. The latter's stock price had slumped following media allegations of bribery by its former chief executive, which the company denied.

Note:

*The changes mentioned in this part refer to our model portfolio, which is the basis for actual portfolios we manage that have similar investment objectives. However, there might be minor variations among these, so the above descriptions might not apply to the actual portfolios.*

## Corporate News

Thanks to their healthy balance sheets, our holdings have been able to seize new growth opportunities. **Yanlord**, together with Ho Bee Investment, acquired six prime residential sites in Tangshan, China, which could open up fresh prospects for the developer. **Sun Hung Kai Properties** won the bid for a site in Ho Man Tin; the price of HK\$10.9 billion reflected a positive longer-term outlook for the territory's luxury residential market. Elsewhere, **China Resources Enterprise** purchased an 80% stake in Hong Kong coffee chain Pacific Coffee, adding to its extensive network in China. **Pacific Basin Shipping** bought back US\$2 million of its convertible bonds.

In other news, **Swire Pacific** proposed to acquire Cathay Pacific's 15% stake in **Hong Kong Aircraft Engineering Company** for HK\$2.62 billion. Earnings reports were also upbeat: **Café de Coral** posted decent full-year results driven by margin expansion and good cost control, while **Li Ning** reported sales order growth of 20.3% during its fourth-quarter trade fair.

We hold all the companies highlighted.

## Key Economic Numbers

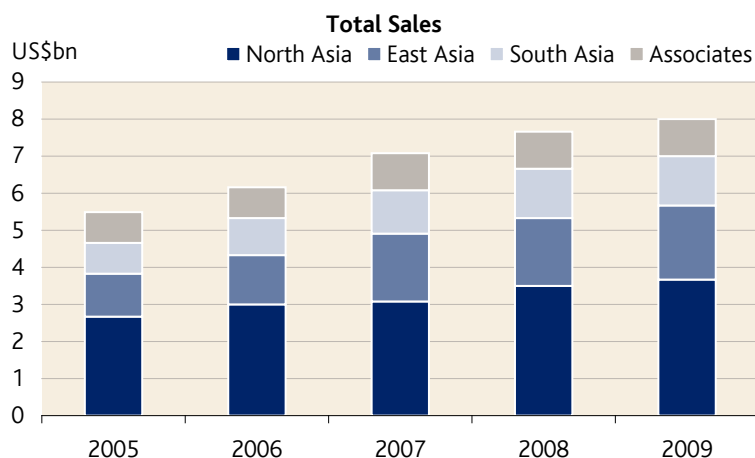
**53.9** The pace of Chinese manufacturing growth eased in May; the Purchasing Managers' Index fell to 53.9, from 55.7 in April. While the data suggested that tighter government policies are working, they also added to concerns of an economic correction.

**3.1** % China's inflation hit a 19-month high of 3.1% in May, exceeding Beijing's target of 3% for the year. But a confluence of factors, including declining food and commodity prices as well as slowing economic activity, could keep a lid on prices. A stronger yuan should also help contain imported inflation pressures.

**18.7** % Retail sales growth on the mainland climbed to 18.7% year-on-year in May as consumer confidence returned to near pre-crisis levels. The recent spate of wage hikes should support private consumption in the coming months, too.

## China/Hong Kong Update

### Focus – Dairy Farm: Satisfying Asian shoppers



Source: Company data, Apr 10

A leading pan-Asian retailer, Dairy Farm's businesses – which include supermarkets, hypermarkets, health and beauty stores, convenience stores, home furnishings stores and restaurants – have established brand names and enjoy strong customer recognition and support. This, along with its position as a retailer of predominantly non-discretionary items, has underpinned its performance over the years. We expect Dairy Farm's prospects to remain positive in view of its secure financial position as well as exposure to rising domestic consumption in Asia.

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