MARKET COMMENTARY

China Tech: Regulatory pressure mostly discounted. The sector is getting relatively attractive vs. US one

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- **Chinese regulators have recently strengthened regulations on online platforms, pledging to combat big data-enabled price discrimination against customers and monopolistic behaviours.**
- **This additional regulation pressure is mostly discounted by investors who monitored the adverse regulatory news flow since the last summer or even February 2021.**
- **Since mid-July, prices of involved stocks and the MSCI China are down by nearly 20% and more than 50% since mid-February (-35% for the MSCI China).**
- **As a result, the MSCI China index is now fairly valued in our opinion from being expensive (30%) in February last year, while the Chinese MSCI Tech index looks quite cheap judging from our fair value model, with investors' positioning very muted.**
- **Currently, we do not recommend buying aggressively the China Tech as it could be affected by further negative spillovers coming from the US Tech sector, which remains rather expensive and is under pressure from increasing US real yields.**
- **The spread of Omicron and China's zero-tolerance COVID approach during the winter Olympics is likely to have negative effect on growth. We expect monetary and fiscal policy to become more supportive after the Olympics (starting from the end of February) to support the economy.**
- **While waiting for clearer signs of a more benign policy (both monetary and fiscal), we would recommend shifting some positions from US, and US Tech stocks in particular, into China and China's Tech stocks.**

China's top regulators - including the national development and reform commission (NDRC) - have recently released a guideline which would regulate various aspects of online platform businesses. The intention is to combat big data-enabled price discrimination against customers and monopolistic behaviours. Originally, the news flow also included regulation of their investments in financial institutions and fund-raising control, which was denied by the regulator as being incorrect.

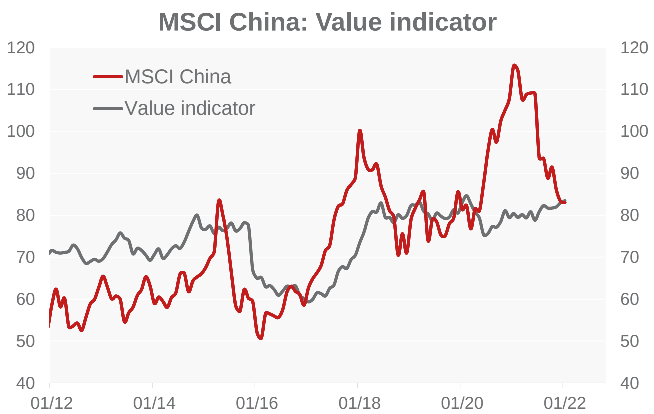
This pressure from the additional regulation is mostly discounted by investors who monitored the adverse regulatory news flow since the last summer or even February 2021.

So, from this point of view, this last news adds little to the overall picture.

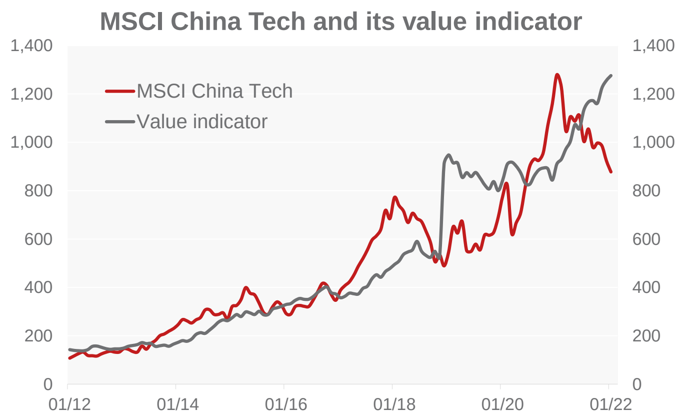
Since mid-July, prices of involved stocks and the MSCI China are down by nearly 20% and more than 50% since mid-February (-35% for the MSCI China).

Source: Datastream, GIAM

After such collapse, the MSCI China index is now fairly valued in our opinion from being expensive at that time, while the Chinese MSCI Tech index has become theoretically quite cheap – based on our fair value indicator (see note).



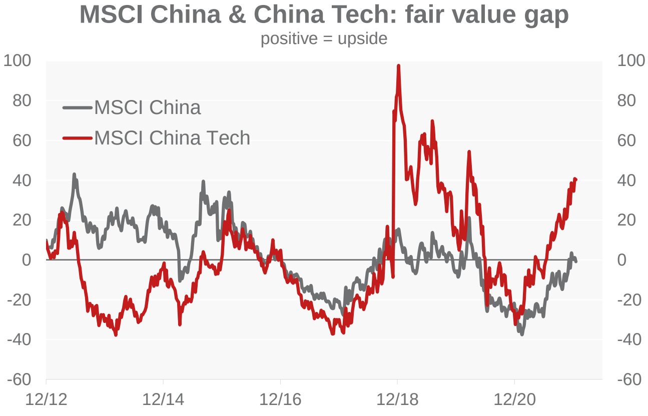
Source: Datastream, GIAM calculations



Source: Datastream, GIAM calculations

NOTE: Fair Value Indicator = 12M FW EPS / (10Y Rate + α); Value Gap = % diff. between Fair Value and Price; Negative Value Gap = Downside Risk;

α = constant such that the average fair value gap since 2013 is approximately zero



Source: Datastream, GIAM calculations

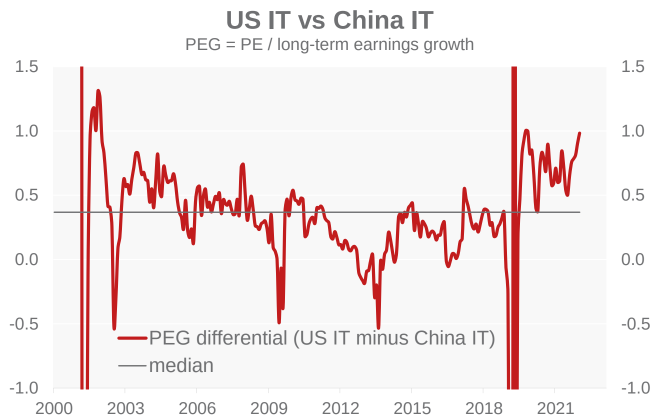
One caveat is that the **US Tech sector** looks quite expensive at the moment (both in absolute terms and vs. the broader S&P500 index) and its PE is pressured by increasing real yields. So, in absolute terms, we don't recommend buying aggressively the CH Tech as it could be affected by negative spillovers coming from the US Tech one.

Also, we believe that China's monetary and fiscal policy have chance to increase their support though not immediately but rather starting from the end of February, after the end of Olympics, with clearer signs of peaking Omicron wave.

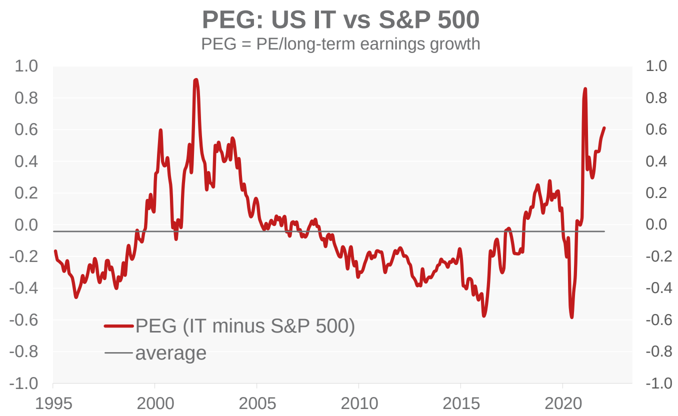
That said, monetary and fiscal policy momentum in China is already diverging from the US one and definitively more supportive. Positioning on Chinese stocks is very light, too, albeit US investors would probably not rush to buy Chinese stocks in the short term, given the continuing political frictions. But EU and Asian investors could start to.

In the end, waiting for clearer signs of a more supporting policy (both monetary and fiscal), we would recommend shifting some positions from US, and US Tech stocks in particular, into China's and China Tech stocks.

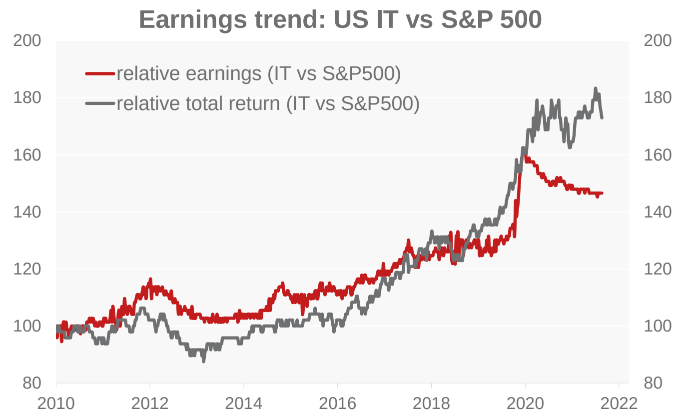
Source: Datastream, GIAM calculations



Source: Datastream, GIAM calculations



Source: Datastream, GIAM calculations



Source: Datastream, GIAM calculations

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