農銀國際
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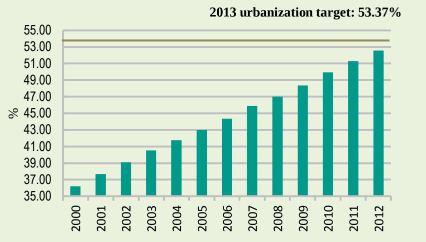
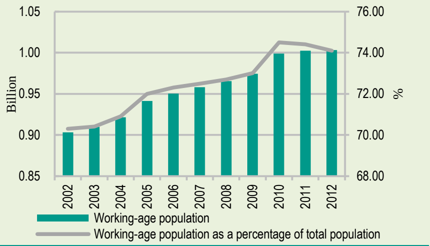
Economics Weekly

Rapid urbanization



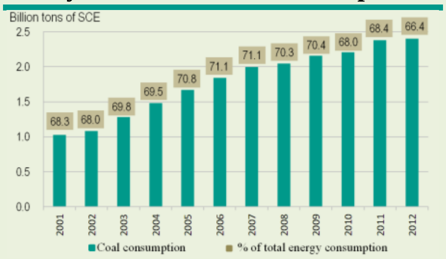
Source: National Bureau of Statistics of China

Shrinking working-age population



Note: Working-age is defined as between 15 and 64
Source: National Bureau of Statistics of China

Heavy reliance on coal consumption



Source: National Bureau of Statistics of China

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Pro-growth policies under "Chinese dream"

On March 17th, 2013, the NPC and CPPCC came to an end and China introduced the world with its fifth generation of leaders. During his inauguration speech, new President Xi Jinping again mentioned his vision of a "Chinese dream" by making China prosperous, powerful and proud. During the press conference, new Premier Li Keqiang emphasized that economic and social reforms would be the top priority and showed the government's determination to tackle existing problems with proper solutions. The new government leaders pledge to make pro-growth policies more stable, more sustainable and more balanced through acceleration of urbanization, relaxation of population policy, adoption of more clean energies, liberalization of financial markets, opening of sectors dominated by state-owned enterprises and promotion of services sectors. This has given China's policy makers greater impetus to bolster the domestic front, thus achieving economic restructuring with stabilized growth in the next ten years.

- **Urbanization is of paramount importance to China's continuing economic growth.** In an unstable and uncertain global economic environment, China is stressed to shift away from using an export-led growth model to a more balanced model that leans towards domestic consumption and investment. The consumption and investment growth driven by the urbanization process become the economic drivers to sustain economic growth. We see clear indication that the new government aims at improving different aspects of urban development, thus enhancing the quality of urbanization. However, the execution of new urbanization model will be a progressive process. Considering that China will continue to rely on investment in its growth model transition and that a vast majority of the rural areas is lagging behind in basic infrastructure, we believe that infrastructure investment will still take the lead in this new phase of urbanization process.

- **The decline in the working-age population calls for review of the existing population policies.** The "One-child Policy" received a lot of attention during the NPC and CPPCC this year since the National Bureau of Statistics of China reported, for the first time, that the working-age population in China declined in 2012. The concern is that China will not enjoy the previous high economic growth if the population keeps declining and aging. No official statement has been released regarding any further relaxation of the existing policy. Yet, during this year's NPC, the Ministry of Health and the National Commission on Family Planning were merged to form the National Health and Family Planning Commission. We believe that it is a tactical step for the government to remove the bureaucratic barriers in further relaxation on population control. We expect that pilot programs will be put forward to test the effects of removing the "One-child Policy".

- **Energy sector reform is inevitable amid public discontent over environmental problem.** Chasing the highest economic growth rate possible at all costs has been taking its toll. The environmental damages in the process of economic development manifested itself as the smog spreading across major cities and soil as well as water contamination recently, raising the public's awareness of the severity of the problem. As a result, during the NPC and CPPCC, government officials and delegates alike discussed this issue extensively. Aside from increasing the use of clean energy harnessed from natural sources, such as solar, wind, and water, we believe that energy price reform will play an important role in solving the environmental problem. If the current pilot program of natural gas price reform tested in certain provinces become successful and subsequently is implemented nation-wide, China will be able to reduce its reliance on coal, which helps alleviate the air pollution.

- **Sector beneficiaries of reform measures will outperform.** As the government is about to kick-start railway construction projects to accelerate the urbanization process, railway construction companies, such as **Guangshen Rail (525 HK)** and **CSR (1766 HK)** will be able to capitalize on the railway network expansion and increasing construction volume. The relaxation of "One-child Policy" will benefit the health care, insurance, and consumer industry. **Biostime (1112 HK)** is our top pick. We also believe that **Kunlun Energy (135 HK)** and **ENN Energy (2688 HK)** will benefit from the energy sector reform.

China Economic Indicators

	2012										2013	
	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb
Real GDP (YoY%)	8.1	---	---	7.6	---	---	7.4	---	---	7.9	---	---
Export Growth (YoY%)	8.9	4.9	15.3	11.1	1	2.7	9.9	11.6	2.9	14.1	25.0	21.8
Import Growth (YoY%)	5.3	0.3	12.7	6.3	4.7	-2.6	2.4	2.4	0	6	28.8	-15.2
Trade Balance (USD/Bn)	5.18	18.53	18.13	31.91	25.28	26.43	27.45	32.11	19.63	31.6	29.2	15.3
Retail Sales Growth (YoY%)	15.2	14.1	13.8	13.7	13.1	13.2	14.2	14.5	14.9	15.2	12.3	
Industrial Production (YoY%)	11.9	9.3	9.6	9.5	9.2	8.9	9.2	9.6	10.1	10.3	9.9	
PMI - Manufacturing (%)	53.1	53.3	50.4	50.2	50.1	49.2	49.8	50.2	50.6	50.6	50.4	50.1
PMI - Non-manufacturing (%)	58	56.1	55.2	56.7	55.6	56.3	53.7	55.5	55.6	56.1	56.2	54.5
FAI(YTD) (YoY%)	20.9	20.2	20.1	20.4	20.4	20.2	20.5	20.7	20.7	20.6	21.2	
CPI (YoY%)	3.6	3.4	3	2.2	1.8	2	1.9	1.7	2	2.4	2.0	3.2
PPI (YoY%)	-0.3	-0.7	-1.4	-2.1	-2.9	-3.5	-3.6	-2.8	-2.2	-1.9	-1.6	-1.6
M2 (YoY%)	13.4	12.8	13.2	13.6	13.9	13.5	14.8	14.1	13.9	13.8	15.9	15.2
New Lending (CNY/Bn)	1011.44	681.8	793.23	919.83	540.1	703.9	623.2	505.2	522.9	454.3	1070.0	620.0

World Economic/Financial Indicators

Equity Index

	Closing price	Chng. WTD (%)	P/E
US			
DJIA	14511.73	-0.02	14.14
S&P 500	1558.71	-0.13	15.37
NASDAQ	3254.19	0.16	24.55
MSCI US	1488.82	-0.12	15.66
Europe			
FTSE 100	6391.13	-1.52	18.17
DAX	7917.67	-1.56	13.71
CAC40	3791.60	-1.36	14.61
IBEX 35	8386.10	-2.70	28.94
FTSE MIB	15927.45	-0.83	82.78
Stoxx 600	295.10	-0.79	19.18
MSCI UK	1904.14	-0.90	18.25
MSCI France	107.34	-0.36	18.90
MSCI Germany	112.32	-0.46	12.96
MSCI Italy	47.14	-0.55	N/A
Asia			
NIKKEI 225	12635.69	0.60	25.40
S&P/ASX 200	4959.41	-3.14	20.56
HSI	22225.88	-1.36	10.98
HSCEI	10944.35	-0.69	9.13
CSI300	2614.99	2.96	13.05
SSE Composite	2324.24	2.01	12.85
SZSE Composite	958.39	2.69	27.53
MSCI China	60.47	-0.40	10.41
MSCI Hong Kong	11517.99	-1.10	11.05
MSCI Japan	646.69	-0.69	22.85

Global Commodities

		Unit	Price	Chng. WTD (%)	Volume (5-day average)
Energy	NYMEX WTI	USD/bbl	92.85	-0.64	125214.80
	ICE Brent	USD/bbl	108.29	-1.39	156209.40
	NYMEX Natural Gas	USD/MM Btu	3.94	1.81	173865.40
	Australia Newcastle Steam Coal Spot fob	USD/Metric Tonne	89.15	N/A	N/A
Basic Metals	LME Aluminum Cash	USD/MT	1900.75	-1.17	53510.40
	LME Primary Aluminum 3 Month Rolling Forward	USD/MT	1939.00	-1.27	33149.20
	CMX Copper Active Contract	USD/lb.	343.80	-2.00	414.20
	LME Copper 3 Month Rolling Forward	USD/MT	7620.00	-1.70	52001.80
	TSI CFR China Iron Ore Fines Index	USD	134.10	-0.37	N/A
Precious Metals	CMX Gold	USD/T. oz	1606.70	0.89	142535.80
	CMX Silver	USD/T. oz	28.78	-0.12	91.60
	NYMEX Platinum	USD/T. oz	756.40	-2.24	6.00
Agricultural Products	CBOT Corn	USD/bu	732.25	2.13	109934.40
	CBOT Wheat	USD/bu	736.00	1.80	51086.80
	NYB-ICE Sugar	USD/lb.	18.38	-2.70	45905.40
	CBOT Soybeans	USD/bu.	1430.00	0.28	95433.20

Bond Yields & Key Interest Rates

	Yield (%)	Chng. WTD (%)
US Fed Fund Rate	0.25	0.00
US Prime Rate	3.25	0.00
US Discount Window	0.75	0.00
US Tresury (1 Month)	0.071	0.00
US Tresury (10 Yr)	1.952	-1.88
US Tresury (30 Yr)	3.1884	-0.72
Japan 10-Yr Government Bond	0.582	-6.88
China 10-Yr Government Bond	3.61	0.56
ECB Interest Rate (Refinancing)	0.75	0.00
1-Month LIBOR	0.2047	0.74
3 Month LIBOR	0.2841	1.43
3-Month SHIBOR	3.8794	-0.11
3-Month HIBOR	0.3829	0.37
Corporate Bonds (Moody's Seasoned)		
Aaa	3.90	-2.26
Baa	4.82	-1.63

Currency

	Euro/USD	GBP/USD	AUD/USD	USD/JPY	USD/CHF	USD/CAD	USD/CNY	USD/HKD	USD/ CNY NDF 12 Month
Spot Exchange Rate	1.2906	1.5137	1.0385	95.7900	0.9461	1.0250	6.2140	7.7623	6.3095
Chng. WTD (%)	-1.30	0.15	-0.23	-0.53	-0.78	-0.55	0.05	0.01	-0.10

Note:
1. *Data source: Bloomberg Finance LP, National Bureau of Statistics of China, ABCIS*
2. *Australia Newcastle Steam Coal Spot fob is the Australia Newcastle 6700 kc GAD fob Steam Coal Spot price published by McCloskey*
3. *TSI CFR China Iron Ore Fines Index is calculated with the 62% Fe specification, spot price*
4. *Certain data is not reported as of the date of this report*

Disclosures

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Definition of equity rating

ting	Definition
Buy	Stock return ≥ Market return rate
Hold	Market return – 6% ≤ Stock return < Market return rate
Sell	Stock return < Market return – 6%

Stock return is defined as the expected % change of share price plus gross dividend yield over the next 12 months
Market return: 5-year average market return rate from 2007-2011
Time horizon of share price target: 12-month

Definition of share price risk

Rating	Definition
Very high	2.6 ≤180 day volatility/180 day benchmark index volatility
High	1.5 ≤ 180 day volatility/180 day benchmark index volatility < 2.6
Medium	1.0 ≤180 day volatility/180 day benchmark index volatility < 1.5
Low	180 day volatility/180 day benchmark index volatility < 1.0

We measure share price risk by its volatility relative to volatility of benchmark index. Benchmark index: Hang Seng Index. Volatility is calculated from the standard deviation of day to day logarithmic historic price change. The 180-day price volatility equals the annualized standard deviation of the relative price change for the 180 most recent trading days closing price.

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