Market & Economic Overview

- The MSCI Zhong Hua Index rebounded sharply in October as Premier Wen Jiabao’s remarks on potential policy fine-tuning buoyed hopes that Beijing may ease monetary policy.
- The government unveiled a series of measures to support small businesses, including easier access to bank loans and a trial reform for value-added taxes in Shanghai aimed at lowering tax burdens. Beijing also launched a pilot scheme to allow local governments to issue bonds directly, which could help avert potential debt defaults.
- China’s economy slowed for a third consecutive quarter, largely a result of policymakers’ efforts to cool growth and rein in inflation. Urban fixed asset investment continued to moderate, while retail sales and industrial production rose. Inflation eased slightly in September but remains outside the central bank’s comfort zone.
- Market uncertainty is likely to prevail in the near term. Initial optimism about Europe’s progress in tackling its debt crisis is waning, while growth prospects for the US economy are still cloudy. At home, signs of economic deceleration are making investors nervous about an abrupt downturn.
- But the latest figures suggest China remains on track for a policy-induced soft landing. The International Monetary Fund expects China to grow by 9.5% this year, while the World Bank’s forecast is 9.3%.

Key Economic Numbers

9.1% **China**’s third-quarter GDP expanded by 9.1% year-on-year. Although still significant in absolute terms, it was the slowest pace of growth recorded in more than two years. Exports were weak but domestic consumption remained resilient.

6.1% **Consumer prices** in China rose 6.1% in September from a year earlier, down from 6.2% in August. Food prices, however, increased by more than 13%.

50.4 The mainland’s official **Purchasing Managers’ Index** was 50.4 in October, compared to 51.2 in September. But the HSBC PMI rebounded to 51.
Model Portfolio News

During the month, we exited our position in Li Ning in view of better opportunities elsewhere. The sportswear company posted disappointing results because of recent restructuring efforts and challenging industry conditions. Conversely, we added to HSBC Holdings and AIA on price weakness.

Note:
The changes 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, so the comments may not apply to all portfolios.

Corporate News

Our holdings posted generally solid quarterly results despite global economic headwinds. PetroChina and CNOOC benefited from steady output and higher prices. China Merchants Bank reported solid profit growth, while its non-performing loan ratio fell. China Mobile’s profits met expectations, underlining its resilience and market leadership amid intense competition. AIA was helped by strong new business growth. Charm Communications’ results were bolstered by its advertising arm. ASM Pacific Technology’s performance was mixed, however, reflecting the cyclical nature of its business.

We hold all the companies highlighted.

Focus – AIA: Another strong quarter

Despite the challenging operating backdrop, AIA posted another set of solid results in the third quarter. The value of new business, in particular, was up by 53% year-on-year, rising to US$245 million, thanks to re-pricing, a better product mix and new initiatives. AIA remains one of the best proxies for the Asian growth story; we have added to our position accordingly, in view of recent price correction.
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