CreditEase Wealth: A-shares are expected to see a style change in the second half of the year, with value stocks outperforming for longer

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Summary of ideas

In early July this year, there was a brief "style switch" phenomenon in A-shares, with leading stocks switching from growth stocks represented by the GEM to value stocks represented by the Shanghai Composite Index. But soon the market enthusiasm switched back to the GEM, which is also the main line of A shares so far this year.

The shift in style from growth stocks to value stocks attracts attention because the rise in value stocks will drive the broader market to strengthen, creating the momentum for A shares to enter a comprehensive bull market. The market is paying attention to the style switch in early July this year, and is more interested in understanding whether there will be a comprehensive bull market in the future.

The A-share bull market that started in the second half of 2014 provides a good example of style switching, which can be used as a reference. Before the A-share bull market fully started, growth sectors such as technology had already started to gain momentum in 2013 due to the recovery of profit performance driven by multiple policy incentives. Value stocks such as financial and real estate began to outperform growth stocks in the second half of 2014. Benefiting from a series of favorable policies in the financial and real estate industries, the profit trend of value stocks stopped falling and turned to rise. At the same time, the central bank has repeatedly cut reserve requirements and interest rates since 2014, driving market interest rates to fall sharply, and the valuation of A-shares has increased rapidly, ushering in a comprehensive bull market.

So far in 2020, the GEM has still performed well, while the main board has performed more moderately, lagging behind the GEM. We believe that a style switch is likely to

occur in the second half of this year, and value stocks will outperform for a longer period of time, mainly because: because China's economy continues to recover, the profitability of sectors such as financial and real estate has relatively well repaired; China's monetary policy has changed from " "Easy money" will turn to "easy credit", and fiscal policy will gradually replace monetary policy to play a greater role in stabilizing the economy. Market liquidity may tighten marginally in the later period, and the benefits to growth stocks that are already highly valued will decrease.

Judging from the recent tightening of market liquidity margins and high-level statements, A-shares as a whole have room for upward growth in the second half of the year, but we must have reasonable expectations for the extent of the "bull market".

text

The second half of this year has just started, and A-shares have risen rapidly. In the five trading days from June 30 to July 6, the Shanghai Composite Index has continuously gapped up, with a cumulative increase of 12.5%, breaking through the high in April 2019 and setting a new record. The highest since February 2018. During this time period, the ChiNext Index, which performed well in the first half of the year, performed weakly, with a cumulative increase of only 6.6%. For a time, the market was full of questions about whether A-shares had undergone a style switch and whether A-shares had entered a new round of bull market.

But then the market heat returned to growth stocks again. From July 7 to July 30, the Shanghai Composite Index fell by 1.4%, and the GEM Index rose by 8.5%. In this article, we will analyze risk switching and its dominant factors, and learn from the characteristics of style switching in the last bull market to understand the late potential style switching performance of A-shares and the overall performance of A-shares.

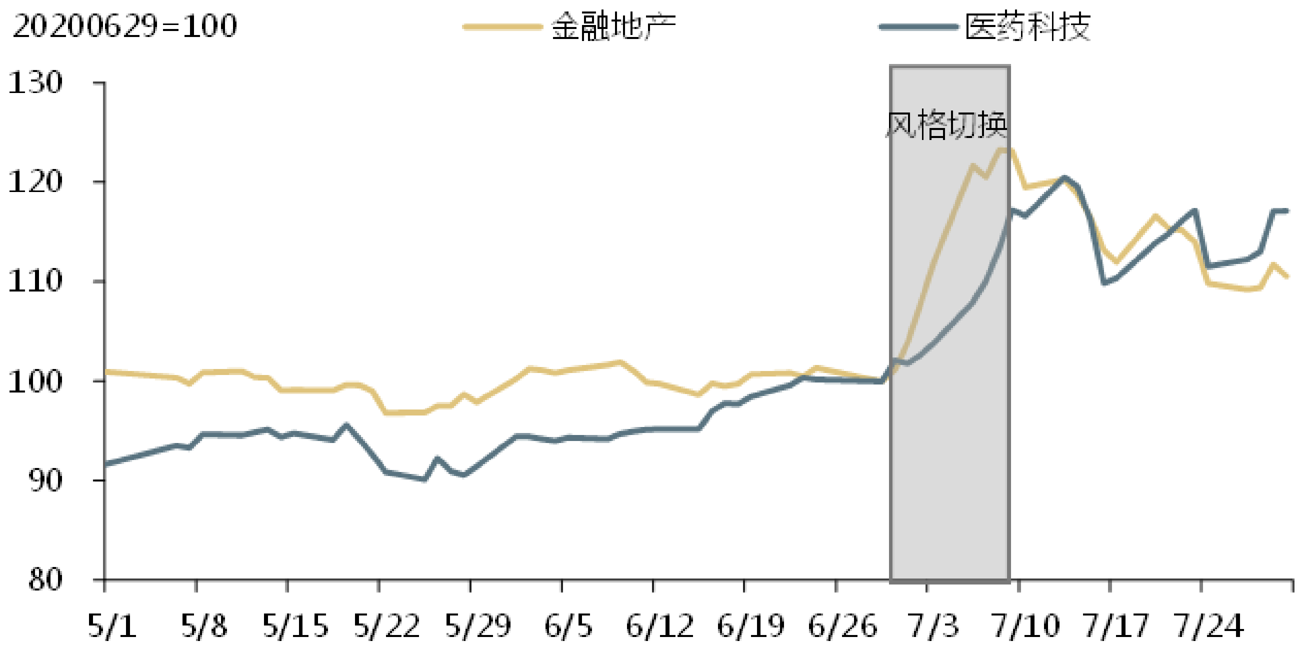
What is style switching?

Before discussing the influencing factors of style switching, we need to understand what style switching is. Generally speaking, the style switching mentioned in the market refers to the switching between the relative strengths and weaknesses of different sectors at different stages. Common style switching includes switching between small-cap stocks and large-cap stocks, switching between high-valuation stocks and low-valuation stocks, or switching between growth stocks and value stocks. The style switch in early July was that the ChiNext Index, representing growth stocks, switched from significantly outperforming the Shanghai Composite Index, representing value stocks, in the first half of the year to significantly underperforming.

Growth stocks and value stocks are not absolutely antagonistic. Growth stocks are not without value, and value stocks are not without growth. The main differences between the two lie in several aspects, including cash flow and dividends, expectations and valuation, size and industry. Growth companies usually have insufficient cash flow and rarely pay dividends, but investors are optimistic about their prospects and give them higher valuations. Growth companies are usually concentrated in industries such as medicine and biology, high technology, and software and hardware equipment. Value companies are usually more mature, have sufficient cash flow and relatively generous dividends, but lack imagination, so investors give them lower valuations. Value companies are mainly in traditional industries such as banking and real estate, and the average company size is relatively large.

Using a more representative style index to represent growth stocks and value stocks can more clearly see the style switching situation in early July. In the first half of this year, growth stocks significantly outperformed value stocks. The pharmaceutical technology index (CITIC Growth Index) rose by 18% cumulatively, while the financial real estate index (CITIC Financial Index) fell by 12% cumulatively. From June 30 to July 6, the financial real estate index rose by 21.7% cumulatively, while the medical technology index only rose by 7.9% during the same period, showing an obvious style switch.

Chart 1: A brief switch from growth stocks to value stocks occurred in early July 2020



Note: CITIC Securities divides all A-shares into five style indexes. The CITIC Financial Index mainly includes banking, securities, insurance, real estate and other industries. This article collectively refers to the financial real estate index; the CITIC Growth Index mainly includes pharmaceuticals, technology hardware, Software services, capital goods and other industries are collectively referred to in this article as the Medical Technology Index.

Data source: Wind, CreditEase Wealth

Why is the market concerned about the current “style shift” in the stock market?

From an investor's perspective, when a market style switch occurs, it means that the main market direction changes, and the position structure can be adjusted accordingly to avoid "full positions but short positions" or significant underperformance. The style switch from growth stocks to value stocks attracts more attention than other types of style switches, because value stocks are often A-share heavy stocks with large markets such as banks and real estate. The rise of these stocks will drive the Shanghai Composite Index, The strength of market indexes such as the Shanghai and Shenzhen 300 has formed the momentum for A-shares to enter a comprehensive bull market.

In the second half of 2014, A-shares also experienced a style switch from growth stocks to value stocks, resulting in a comprehensive bull market that lasted for nearly a year. Therefore, **the market is paying attention to the style switch in early July this year, and is more interested in understanding whether there will be a comprehensive bull market next.**

2020 is still a partial bull market so far

In fact, the style switch in early July lasted only less than two weeks. Looking over a longer period of time, 2020 is still a local bull market. The ChiNext Index has risen by 52.6% this year, while the Shanghai Composite Index has only risen by 7.8%. The cumulative return of the Medical Technology Consumer Index, which represents growth stocks, was 35.0%, and the Financial Real Estate Index, which represents value stocks, rose by -4.2%.

From the perspective of industry segments, the top five performing sectors this year are consumer services, medicine, food and beverages, national defense and military industries, and electronic equipment, with increases of 61.7%, 59.6%, 47.3%, 45.4%, and 40.4% respectively. The five worst-performing sectors are banking, petroleum and petrochemicals, coal, steel and real estate, all of which recorded negative returns, with cumulative declines of 9.7%, 8.8%, 4.1%, 2.5% and 0.8% respectively.

Chart 2: The growth rate of the ChiNext Index in 2020 is much higher than that of the Shanghai Composite Index

		2019 第一季度	2019 第二季度	2019 第三季度	2019 第四季度	2020 第一季度	2020 第二季度	2020 第三季度至今	2019年	2020年至今	2019至今
	万得全A	30.71	-4.62	-0.09	5.64	-6.79	15.01	13.56	33.02	19.60	59.09
	创业板指	35.43	-10.75	7.68	9.14	4.10	31.05	15.64	43.79	52.58	119.40
	上证指数	23.93	-3.62	-2.47	4.02	-9.83	8.64	10.98	22.30	7.76	31.79
	沪深300	28.62	-1.21	-0.29	6.33	-10.02	13.33	13.30	36.07	13.66	54.66
上游资源	石油石化	18.53	-5.57	-6.24	4.11	-16.50	-0.28	11.58	8.85	-8.76	-0.68
	煤炭	21.81	-1.82	-5.69	1.55	-15.39	-0.60	14.01	14.75	-4.12	10.02
	有色金属	22.82	-2.19	-7.04	10.17	-14.51	11.74	21.04	24.22	13.68	41.21
中游材料	钢铁	20.86	-8.79	-10.51	3.55	-13.21	6.11	6.52	2.82	-2.46	0.29
	基础化工	31.06	-11.53	-1.23	7.22	-7.26	17.08	17.30	23.66	24.55	54.02
	建材	34.83	-3.39	-3.39	21.23	-1.30	7.39	24.97	52.99	32.33	102.46
中游制造	建筑	18.36	-9.94	-6.73	0.35	-4.71	-4.38	11.49	0.28	1.99	2.28
	轻工制造	35.26	-13.68	-1.91	11.51	-8.31	12.76	15.63	28.18	17.51	50.62
	机械	31.29	-8.17	-1.24	4.13	-6.57	12.08	14.07	25.21	18.41	48.26
	电力设备	31.77	-11.53	1.03	2.94	-2.37	19.96	20.89	22.58	40.44	72.16
	国防军工	34.14	-9.77	2.31	-2.01	-2.32	12.82	32.79	22.68	45.45	78.43
下游必选消费	商贸零售	26.33	-8.02	-6.78	-0.39	-2.56	18.59	14.58	8.72	28.69	39.92
	消费服务	22.22	2.54	2.34	-0.41	-15.20	48.70	34.45	28.16	61.72	107.26
	纺织服装	26.28	-11.71	-3.71	1.26	-4.45	-2.28	8.55	9.14	1.97	11.29
	医药	31.20	-6.50	6.86	4.95	8.22	31.83	14.55	38.21	59.59	120.57
	食品饮料	42.37	13.02	3.57	2.37	-3.77	34.93	18.88	72.84	47.32	154.63
	农林牧渔	48.80	-3.71	0.07	4.56	16.02	6.90	16.82	48.16	32.95	96.99
下游可选消费	汽车	20.38	-8.75	-2.51	11.63	-6.95	10.43	13.85	20.29	15.27	38.67
	房地产	31.75	-9.30	-5.28	11.00	-14.05	5.55	10.24	26.16	-0.83	25.11
	家电	35.09	3.48	0.19	14.24	-15.85	19.46	10.80	60.55	10.71	77.74
金融	银行	16.39	2.85	-0.71	6.00	-14.77	0.93	4.03	27.28	-9.66	14.99
	非银金融	42.39	1.61	-3.28	3.52	-15.58	5.53	17.49	47.74	3.02	52.19
TMT	电子器件	41.56	-10.52	18.63	11.29	-4.66	29.42	10.41	72.23	33.24	129.48
	通信	33.46	-7.28	0.56	2.75	0.47	7.15	4.62	30.52	11.40	45.40
	计算机	47.30	-9.70	5.03	3.79	2.86	18.99	9.55	47.53	30.28	92.20
	传媒	28.18	-15.76	0.93	12.70	-7.49	21.67	4.68	24.65	15.56	44.04
基建与运营	交通运输	24.65	-3.55	-4.95	2.27	-14.04	8.35	11.32	17.56	1.17	18.94
	电力公用	17.09	-3.78	-4.08	-0.26	-7.14	4.24	8.78	8.44	4.48	13.30
综合	综合	33.50	-13.80	-4.80	4.80	-5.23	1.96	10.10	15.62	5.50	21.98
	综合金融	25.62	-11.10	-4.73	5.55	-10.19	7.81	7.90	15.40	1.22	16.81

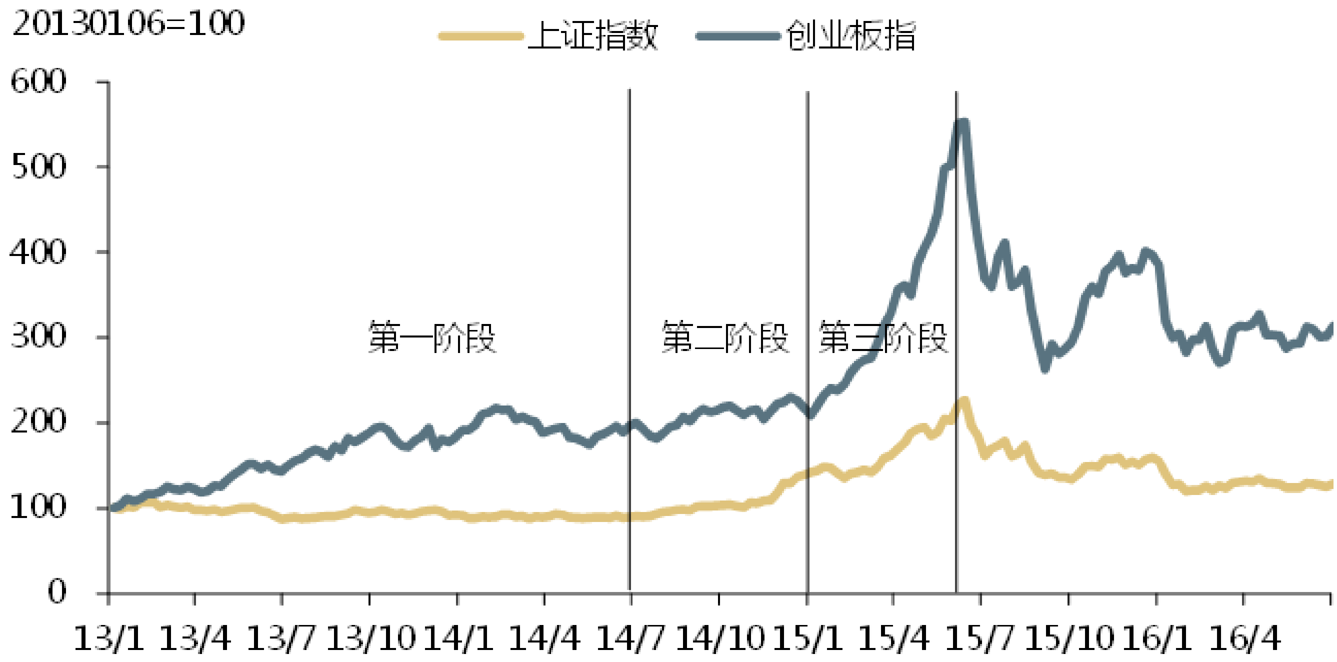
Data source: Wind, CreditEase Wealth

Profit reversal is a necessary condition for style switching - inspiration from 2014

One possible reason for the brief style switch in early July is the end of institutional position adjustments in the second quarter, from holding offensive growth stocks to more stable holdings of value stocks with lower valuations. The main reason may be related to the market's expectations for continued economic recovery. The manufacturing PMI announced on June 30 was 50.9, and the non-manufacturing PMI was 54.4, both expanding for four consecutive months. The recovery of the economy is more beneficial to traditional industries such as finance and real estate, and will bring about the recovery of profits in these industries. This is also the logic of the style switch in the second half of 2014.

From 2013 to 2015, A-shares went from a unilateral bull market to a comprehensive bull market. Looking back at the A-share market from 2013 to 2015, we can see three very clear stages: The first stage was the growth stock bull market represented by the GEM Index, which lasted from the beginning of 2013 to mid-2014. At this stage, the GEM Index rose by 97%, while the Shanghai Composite Index fell by 11%. This is a typical unilateral bull market for the GEM. In the second stage, the strength of large-cap value stocks represented by the Shanghai Composite Index drove A-shares into a bull market, which lasted from the second half of 2014 to the end of 2014. At this stage, the Shanghai Composite Index rose by 55%, significantly outperforming the GEM Index by 11%, and the market style changed. The third stage is the mad cow stage, which lasts from the beginning of 2015 to the middle of 2015. The Shanghai Composite Index and GEM Index rose by 64% and 154% respectively, with the Shanghai Composite Index exceeding 5,000 points.

Chart 3: Three stages of the A-share bull market from 2013 to 2015



Data source: Wind, CreditEase Wealth

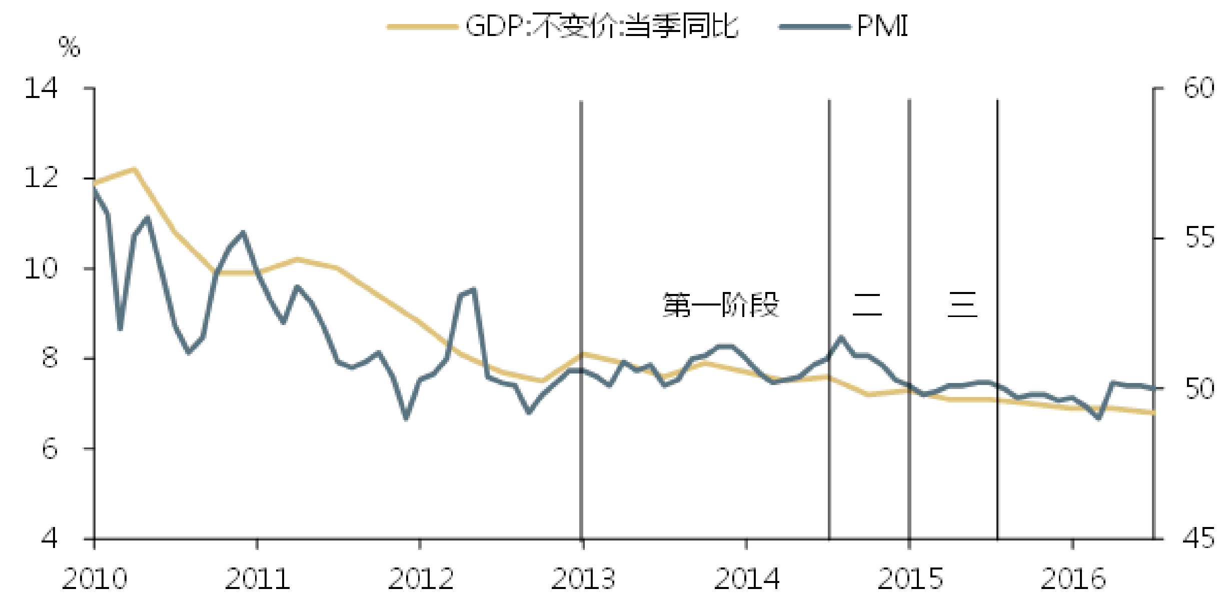
The reasons for the rise and fall of the stock market can be simply divided into profitability factors and valuation factors. The former is directly related to economic trends and industry trends, while the latter is related to market sentiment and liquidity. When we review the last bull market, we can see that the emergence of a comprehensive bull market from the second half of 2014 to the first half of 2015 requires the joint action of the two driving forces of corporate profits and liquidity, while style switching is mainly related to changes in corporate profits.

Market interest rates continued to decline in 2014, driving up stock market valuations

Between 2013 and 2015, China's economic growth has been in a slow downward trend, with GDP growth falling from 8.1% in the fourth quarter of 2012 to 6.9% in the fourth quarter of 2015. The manufacturing PMI fluctuated, and once fell into the contraction range. The average level has dropped significantly compared with around 53 in 2010-2012.

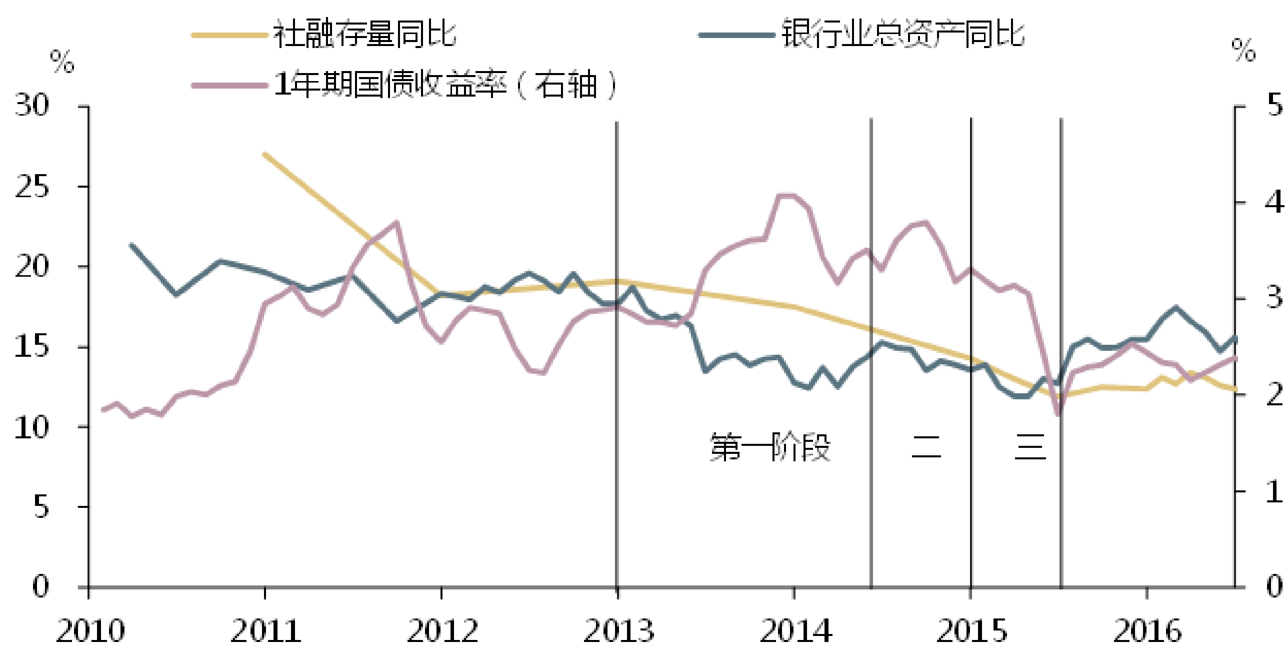
As the money shortage problem eased in the second half of 2013, the central bank began to increase monetary easing in 2014 to support the economy. Domestic market interest rates dropped significantly and liquidity improved significantly. In 2014, the central bank carried out two targeted RRR cuts and one interest rate cut. In 2015, it carried out five RRR cuts and interest rate cuts. Although the stock of social financing did not rebound year-on-year until the end of 2015, financing costs have continued to decline since the beginning of 2014. The 1-year government bond yield (together with the interest rate on interbank certificates of deposit and 7 days) fell from about 4% at the beginning of 2014 to 2015. 2% year-on-year. The low interest rate environment drove the stock market to accelerate in the second half of 2014. The valuation of the Shanghai Composite Index climbed from less than 10 times in mid-2014 to 23 times in mid-2015, and the valuation of the ChiNext Index increased from around 50 times. rose to 135 times.

Chart 4: China's economic growth declined overall from 2013 to 2015



Data source: Wind, CreditEase Wealth

Chart 5: Domestic liquidity began to improve in 2014



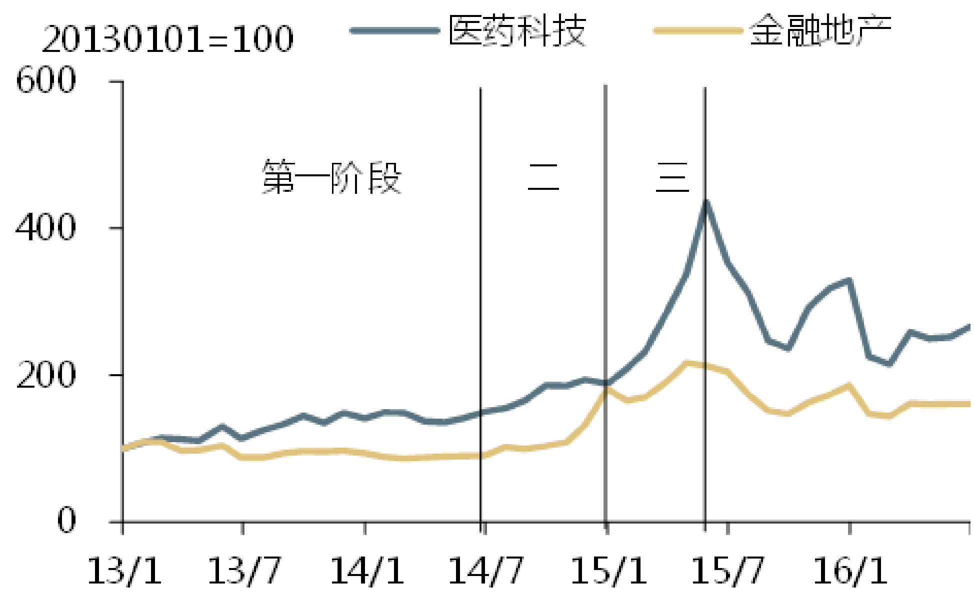
Data source: Wind, CreditEase Wealth

Earnings changes dominate growth stock bull run and style switch in second half of 2014

The earnings of growth stocks continued to improve from 2013 to 2015. Although the overall economic performance was poor at that time, the profits of growth sectors such as medicine and technology continued to improve, with the average EPS year-on-year growth rate rising from -25.5% at the beginning of 2013 to 10.7% in mid-2015. The improvement in profitability of these industries is due to macroeconomic transformation and policy support. The concept of "Internet +" appeared for the first time in 2012. In February 2013, the General Office of the State Council issued the "Opinions on Strengthening the Main Position of Enterprises in Technological Innovation and Comprehensively Improving Enterprise Innovation Capabilities." On April 18, General Secretary Xi Jinping pointed out the construction of an innovative country. After this month, the “Twelfth Five-Year Plan” for strategic emerging industries such as communications and the Internet will be launched one after another. At the same time, with the implementation of 4G licenses, the scale of mobile Internet exploded in 2013. The profitability performance of growth stocks continued to improve from 2013 to 2015, coupled with the improvement in liquidity after 2014, growth stocks completed a double-click of profitability and valuation.

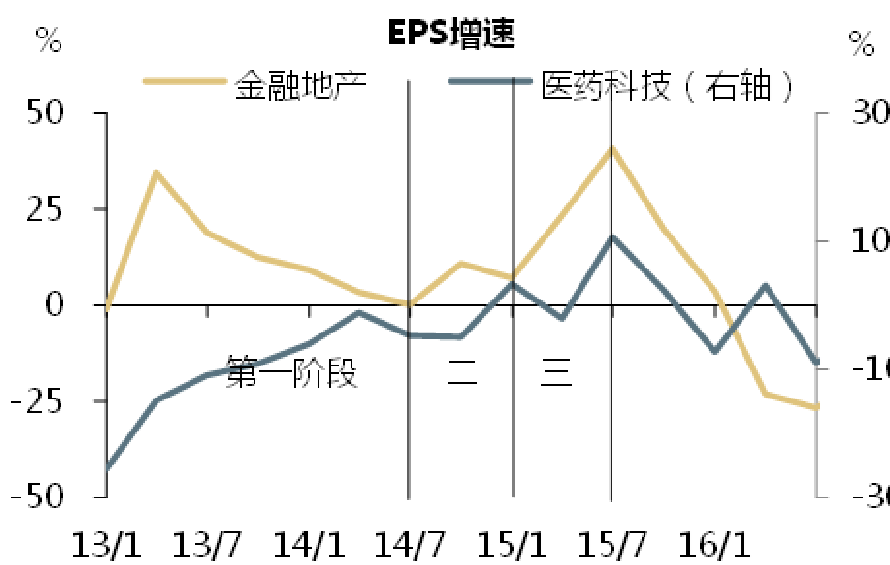
The style switch in the second stage is due to the reversal in the earnings of value stocks. The profits of value sectors such as financial real estate continued to weaken in the first stage, but began to improve in the second half of 2014, with EPS growth continuing to climb from around 0% to 40.9% in mid-2015. This substantial improvement in profitability is also closely related to a series of policies introduced by the government at that time. In terms of finance, in addition to two targeted reserve requirement ratio cuts and one interest rate cut, the government also restarted the long-suspended IPO in the second half of 2014, launched the Shanghai-Hong Kong Stock Connect system, and continued to accelerate the registration system reform. The insurance industry’s "New Country Ten Rules" release. In terms of real estate: Starting in May 2014, local governments gradually relaxed purchase restrictions; in June 2014, the China Banking Regulatory Commission expressed strong support for the demand for first-time housing; in September 2014, local governments added preferential interest rates for first-time home loans, relaxed first-time home certification, provident fund Loans and other stimulus measures; in October 2014, the central bank stated that it would relax its second-home loan policy. These policies have jointly promoted a significant improvement in the profits of banking, securities, insurance, real estate and other sectors, and driven the stock prices to rise rapidly.

Exhibit 6: Growth stocks underperform value stocks in the second stage



Data source: Wind, CreditEase Wealth

Chart 7: The profits of value stocks improved significantly in the second and third stages.



Data source: Wind, CreditEase Wealth

Chart 8: A-share style switching occurred in the second half of 2014

Group	Industry	2013 第一季度	2013 第二季度	2013 第三季度	2013 第四季度	2014 第一季度	2014 第二季度	2014 第三季度	2014 第四季度	2015 第一季度	2015 第二季度	2015 第三季度	2015 第四季度	2016 第一季度	2013年	2014年	2015年
	万得全A	0.72	-8.62	16.59	-0.72	-3.12	3.28	23.55	24.40	28.69	22.13	-28.74	31.69	-17.92	5.44	52.44	38.50
	创业板指	21.38	16.76	35.21	-1.46	1.79	5.58	10.95	-3.57	58.66	24.80	-22.57	29.33	-17.53	82.73	12.83	84.41
	上证指数	-1.43	-11.51	9.88	-2.04	-3.91	0.32	16.07	37.20	15.87	12.96	-24.68	16.49	-15.12	-6.75	52.87	9.41
	沪深300	-1.10	-11.80	9.47	-2.71	-7.88	0.61	13.99	44.36	14.64	9.41	-23.59	17.37	-13.75	-7.65	51.66	5.58
上游资源	石油石化	12.06	-8.36	1.15	3.64	-3.57	1.22	16.95	9.56	16.98	22.49	-36.09	13.93	-13.19	7.22	24.21	3.03
	煤炭	-11.84	-29.05	7.11	-10.80	-16.73	2.47	27.67	21.97	12.10	20.75	-37.55	12.82	-8.27	-40.30	32.13	-7.71
	有色金属	-8.70	-24.64	14.51	-10.26	-3.12	5.80	29.31	11.75	24.53	14.26	-37.39	37.42	-10.78	-29.75	46.27	16.14
中游材料	钢铁	-4.90	-18.15	7.99	-0.18	-5.29	2.68	30.35	33.90	25.68	27.75	-42.39	8.01	-18.59	-16.49	69.29	-6.40
	基础化工	11.86	-14.16	12.60	1.23	-0.68	1.00	30.63	3.34	42.92	28.02	-28.83	45.97	-19.87	8.49	33.35	80.42
	建材	-4.30	-13.10	8.93	3.98	-6.06	1.67	24.49	15.62	27.65	19.23	-27.82	36.51	-17.01	-6.16	37.35	43.88
中游制造	建筑	-4.64	-6.78	2.78	-0.98	-7.46	1.40	27.20	68.79	29.53	9.64	-25.46	15.90	-17.24	-9.96	99.90	15.78
	轻工制造	10.65	-8.43	24.80	-0.67	4.44	3.23	25.34	-2.17	48.70	39.65	-28.46	39.86	-19.73	23.88	30.95	97.11
	机械	-1.41	-13.27	15.29	7.40	-1.70	2.58	31.47	12.23	40.78	35.61	-30.60	32.35	-22.04	4.84	46.86	65.37
	电力设备	4.63	1.12	22.23	3.49	3.67	1.02	29.50	1.91	47.79	27.02	-30.19	40.47	-19.55	32.27	38.34	71.25
	国防军工	21.77	-12.13	20.04	8.64	-8.61	17.55	44.90	7.09	25.76	41.61	-32.51	27.59	-20.78	38.90	58.82	38.28
下游必选消费	商贸零售	-0.49	-11.15	44.87	-5.33	-4.94	-2.33	30.49	14.47	40.16	18.67	-28.20	29.86	-21.04	17.95	38.38	48.04
	消费服务	6.54	-12.86	35.79	-3.13	6.76	4.50	29.61	3.39	55.32	34.90	-18.48	40.02	-18.89	19.98	47.63	122.86
	纺织服装	1.60	-12.08	18.55	3.61	1.04	-1.41	33.37	8.97	47.94	33.41	-27.89	45.54	-17.15	8.38	43.40	94.68
	医药	22.39	-3.85	19.91	-1.85	-0.88	1.03	19.18	-0.02	38.43	25.70	-21.85	30.86	-19.54	37.85	17.98	64.74
	食品饮料	-5.85	-3.53	5.47	-4.32	-5.15	0.04	16.44	11.24	14.40	27.12	-25.30	21.28	-8.01	-9.01	21.30	25.53
	农林牧渔	0.02	-11.97	23.30	12.15	-10.68	3.01	34.73	-0.16	42.87	33.59	-27.96	39.47	-18.26	17.82	25.11	82.72
下游可选消费	汽车	2.29	-2.64	16.73	1.99	-0.53	6.07	25.23	5.84	36.42	19.55	-24.85	34.40	-15.29	17.41	39.74	53.23
	房地产	-7.34	-4.98	8.84	-6.97	1.30	-0.58	24.47	42.36	25.18	21.01	-27.22	46.80	-22.16	-11.69	78.15	55.40
	家电	8.58	-4.49	12.88	18.26	-5.70	5.05	12.00	14.78	34.86	31.81	-34.50	40.81	-15.26	38.29	25.16	48.81
金融	银行	3.48	-9.17	8.90	-6.68	-3.50	2.38	8.60	60.13	-2.67	12.55	-10.70	12.71	-7.74	-4.84	71.83	3.57
	非银金融	-7.53	-13.88	12.33	4.91	-13.60	4.34	18.25	116.39	5.62	-6.36	-33.24	33.33	-13.96	-5.40	129.76	-18.66
TMT	电子器件	16.34	2.02	20.61	0.55	-2.07	8.93	21.10	-7.46	45.31	31.69	-28.65	44.43	-19.58	42.41	16.82	80.94
	通信	13.24	6.75	30.89	-6.12	2.75	9.08	23.06	-0.67	58.21	33.35	-25.07	46.13	-20.61	45.25	35.93	115.46
	计算机	12.91	5.37	43.88	5.85	7.29	13.65	29.13	3.62	95.96	19.65	-32.07	54.02	-28.09	75.72	56.98	125.97
	传媒	12.19	31.08	76.13	-17.27	-1.80	8.03	13.46	-0.42	61.95	20.29	-30.33	35.59	-23.01	102.56	19.57	71.70
基建与运营	交通运输	1.38	-15.46	23.68	1.11	-3.45	-2.76	31.09	39.26	27.15	36.97	-30.38	12.22	-21.50	5.66	71.55	30.66
	电力公用	12.37	-7.02	6.49	3.03	-5.78	2.55	28.66	32.48	16.62	30.11	-30.83	17.98	-20.71	13.48	63.18	18.14
综合	综合	7.75	-7.96	37.24	-0.66	-2.32	-0.65	31.20	18.94	33.97	31.88	-36.03	62.64	-19.28	30.93	52.37	74.74

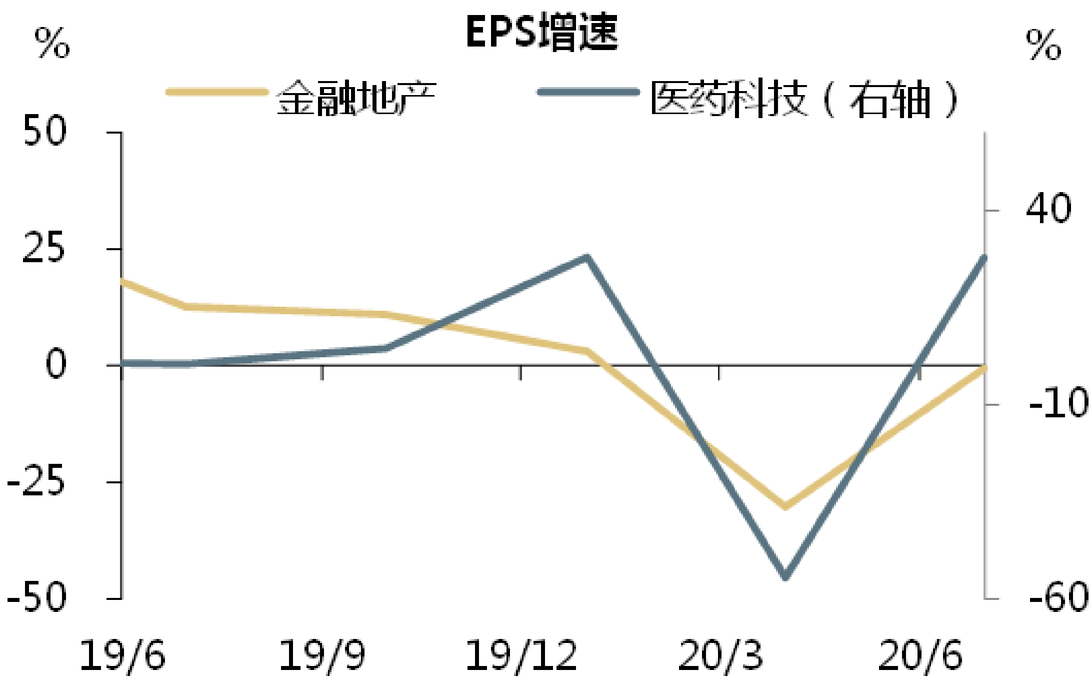
Data source: Wind, CreditEase Wealth

There may be another style switch in the second half of 2020

Affected by the COVID-19 epidemic, A-share industries generally experienced negative profit growth in the first quarter of 2020, but their profit growth rates rebounded rapidly in the second quarter. The average year-on-year profit growth rate of sectors such as pharmaceutical technology in the second quarter has risen from 54.5% in the first quarter to 27.9%, while the profit growth rate of the financial and real estate sector has only rebounded to around 0% from a 30.2% drop in the first quarter. The faster recovery of earnings of growth stocks does not support the switch of market style from growth stocks to value stocks. We believe that there is a high probability of style switching in A-shares in the second half of 2020, and value stocks are expected to perform to a certain extent. There are several main reasons:

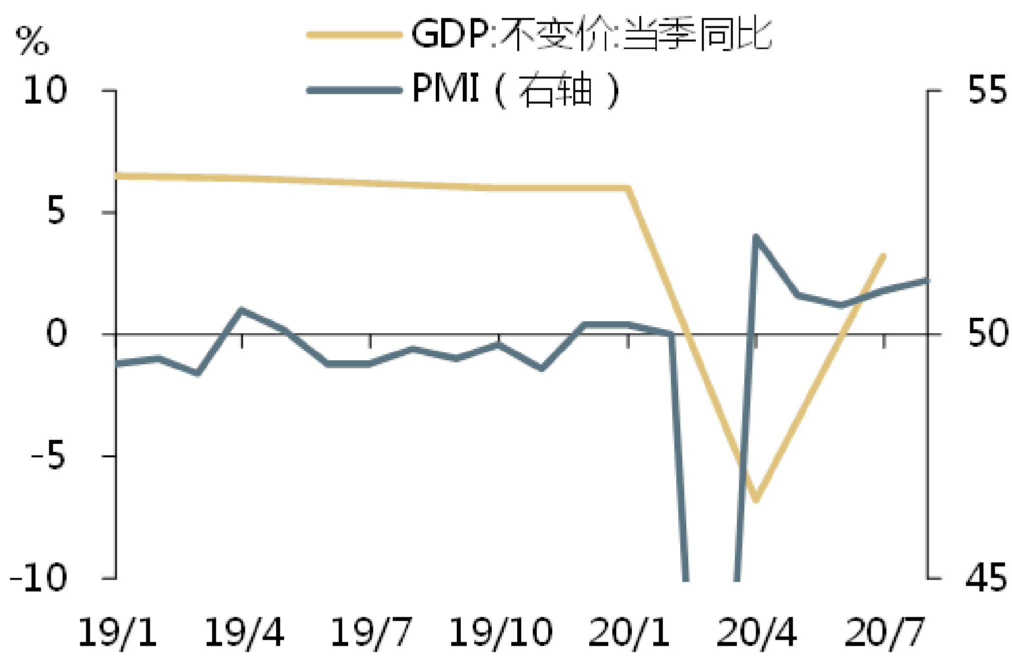
First, China's economic growth continues to pick up, and the profit margins of value stocks such as financial and real estate have improved even more. China's second-quarter GDP growth rate announced not long ago reached 3.2%, far exceeding market consensus expectations. We pointed out in the "Asset Allocation Strategy Guidelines for the Second Half of 2020" that under the baseline scenario, China's GDP growth rate in the third quarter and fourth quarter was 4.9% and 6.9% respectively, and the full-year growth rate in 2020 was 1.8%. Based on the current momentum of economic recovery, this number may be revised upward.

Chart 9: Growth stock profits recovered faster in the second quarter of 2020



Data source: Wind, CreditEase Wealth

Chart 10: The economy is likely to continue to rebound in the second half of 2020



Data source: Wind, CreditEase Wealth

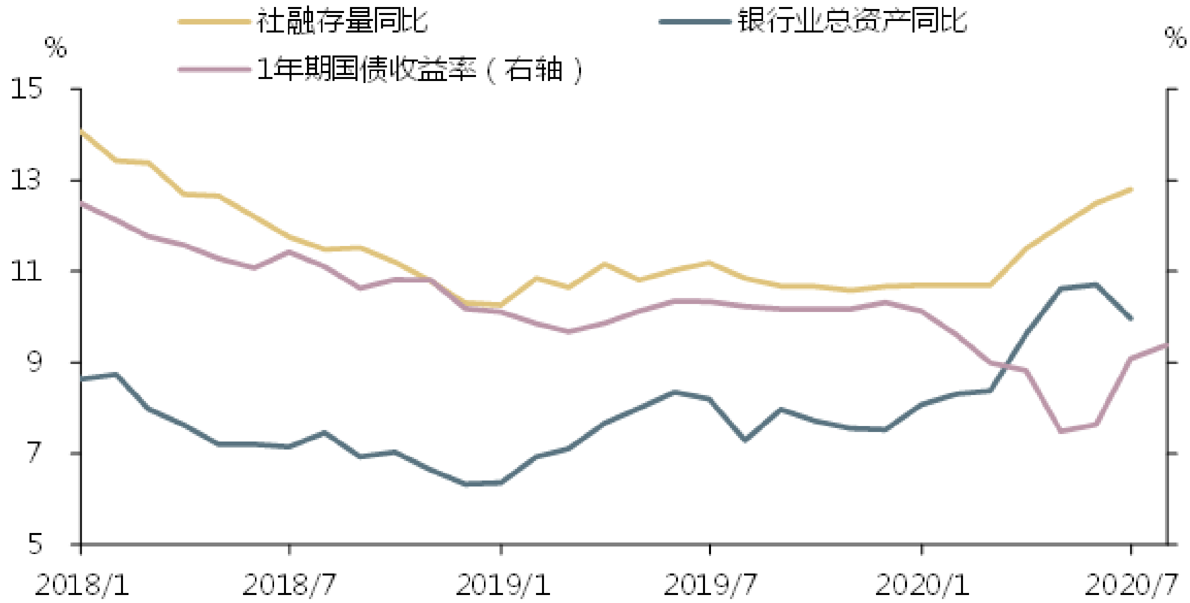
Economic recovery is good for the entire A-share industry, but the profits of pharmaceutical, technology and other sectors have been quickly restored after the second quarter, while the financial and real estate sectors have not been repaired sufficiently. This may be related to the characteristics of the industry: the impact of the epidemic on traditional industries is more lasting. , but the demand for personal contact in industries such as medicine and technology is relatively low. Not only can they adapt to the home isolation situation during the epidemic more quickly, some companies can actually benefit from this. As the economy gradually normalizes, traditional industries will see further earnings recovery in the later period, while the earnings of growth stocks may remain stable. From the perspective of marginal changes, the earnings improvement of value stocks will be greater.

Second, as the policy changes from loose money to loose credit, liquidity may tighten marginally, which is not conducive to highly valued sectors. In the first quarter of 2020, central banks of various countries have carried out large-scale policy easing measures in response to the COVID-19 epidemic. The People's Bank of China is no exception. It not only successively lowered the medium-term lending facility (MLF), reverse repurchase interest rate and deposit reserve ratio, but also asked banks to It provided 1.8 trillion yuan in cheap re-loans and also extended the loan repayment time limit for small and medium-sized enterprises. Market interest rates continued to fall in the first quarter of this year, with the 1-year treasury bond yield falling from 2.6% at the beginning of the year to about 1.2% in April.

However, after May, the central bank’s easing policies began to tighten, and many central bank officials publicly stated that they would strictly prevent financial arbitrage and idling of funds caused by stimulus policies. Governor Yi Gang said in mid-June that “financial support policies during the epidemic response are phased and must be advanced in advance.” Consider the timely exit of policy instruments.” Market interest rates have now returned to pre-epidemic levels. However, the central bank has not yet comprehensively tightened monetary policy. Instead, it has shifted from "loose money" to "loose credit" and used various structural tools to allow funds to flow directly to small, medium and micro enterprises. This is also a main reason why the current growth rate of social financing stock remains high.

The gradual recovery of the economy, changes in the central bank's policy thinking, and a greater role of fiscal policy may lead to high market interest rates and further slowdown in liquidity. This will be detrimental to growth stocks whose valuations are generally high, and some hotly-hyped sectors may face significant corrections.

Chart 11: After April 2020, loose money will shift to loose credit



Data source: Wind, CreditEase Wealth

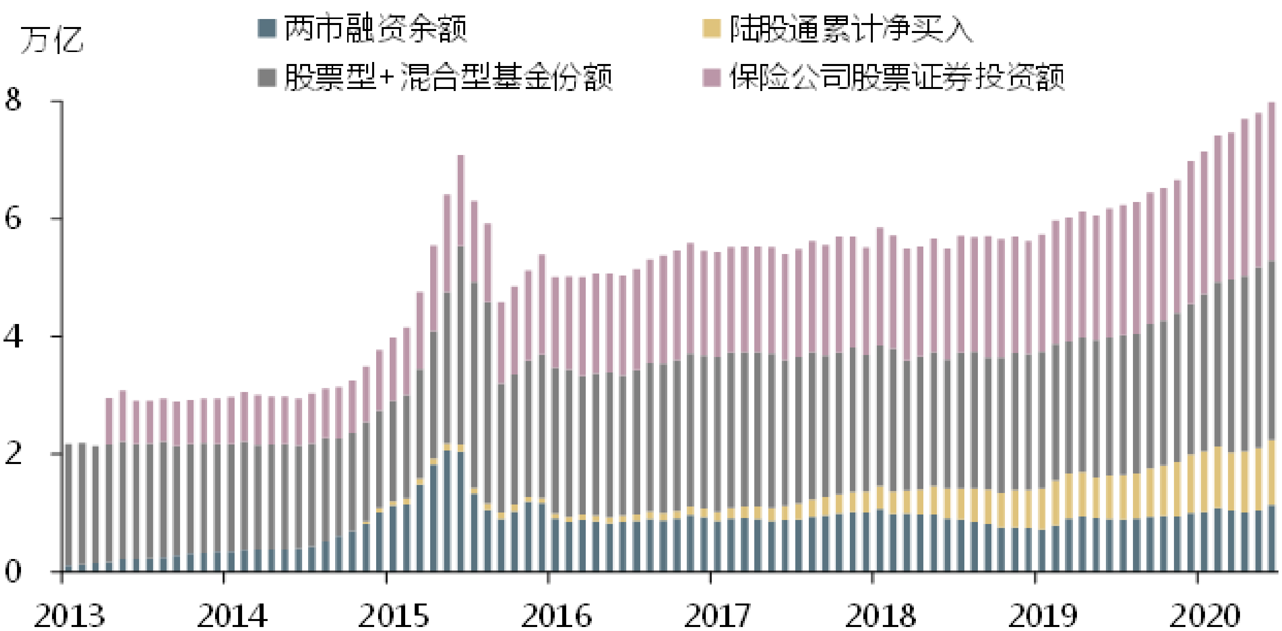
There is room for upside in A-shares in the later period, and "core assets" may continue to be popular

Although we believe that there is a high probability that A-shares will switch styles again in the second half of the year, and that there is room for upward growth in A-shares as a whole, it will be difficult to develop into a comprehensive bull market like the second half of 2014 to the first half of 2015, especially if there is another mad bull. appeared because the policy support for liquidity was insufficient. Looking over the long term, we believe that there will be a long-term structural bull market for A-shares - a "core asset" bull market.

A-share investors are gradually becoming institutionalized. After five years of investor training and policy changes, the investor structure of A-shares has changed significantly. Institutional investors, including foreign capital, account for more than 20% of the stock market value, gradually approaching the proportion of individual investors (The remaining nearly 50% are general legal persons), and the influence of the organization increases. When we compare the four major incremental funding sources of A-shares at the peak of the bull market in 2015, we can also clearly see the institutional trend of A-shares. Southbound Stock Connect was officially launched at the end of 2014. From June 2015 to now, the cumulative net buying scale has increased from 120 billion to 1.1 trillion. During the same period, insurance funds have increased from 1.5 trillion to 2.7 trillion, and the shares of stocks and hybrid funds have increased from 1.5 trillion to 2.7 trillion. 3.3 trillion fell slightly to 3 trillion, and the financing balance of the two cities dropped sharply from 2 trillion to 1.1 trillion.

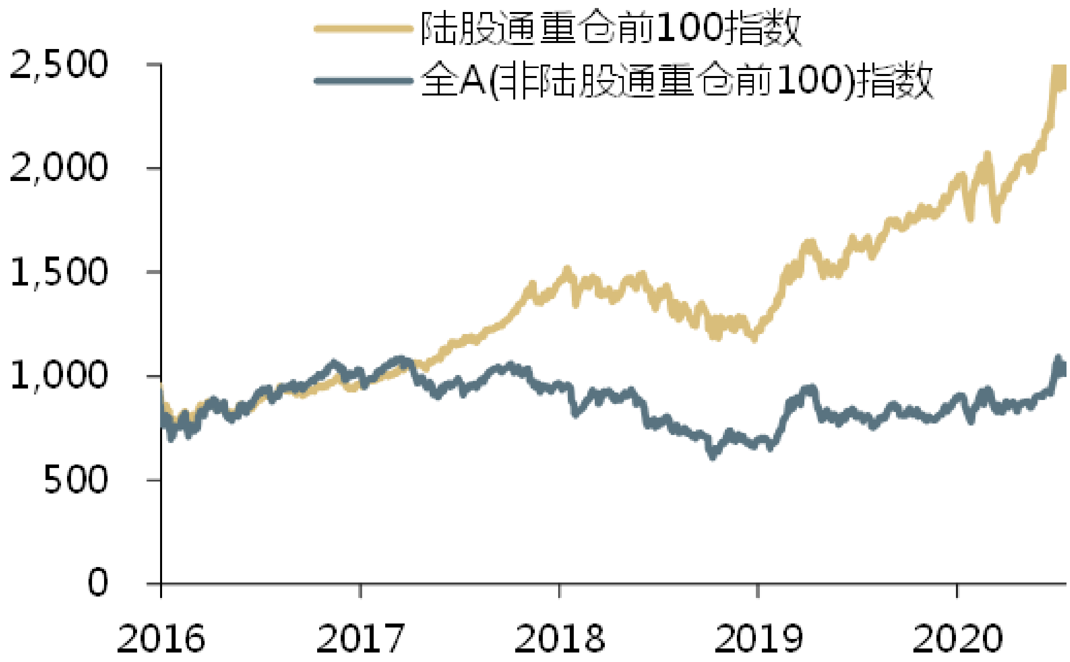
Long-term funds prefer "core assets". The capital of Northbound Trading and insurance funds, which have increased significantly in scale, are more inclined to be allocated to companies with higher profitability, stable growth, sustainable financial structure and good management. These companies have core competitive advantages. "core assets". The performance of core assets, represented by the top 100 indexes of Mainland China Stock Connect (Shanghai-Hong Kong Stock Connect + Shenzhen-Hong Kong Stock Connect), has significantly outperformed non-core asset stocks in the past three years. This differentiation phenomenon will also continue to grow as A-shares are further institutionalized. intensify. Moreover, we believe that neither changes in market liquidity nor the impact of external black swan events will affect the long-term bullish trend of core assets.

Chart 12: Changes in trends of the four major sources of funds for A-shares



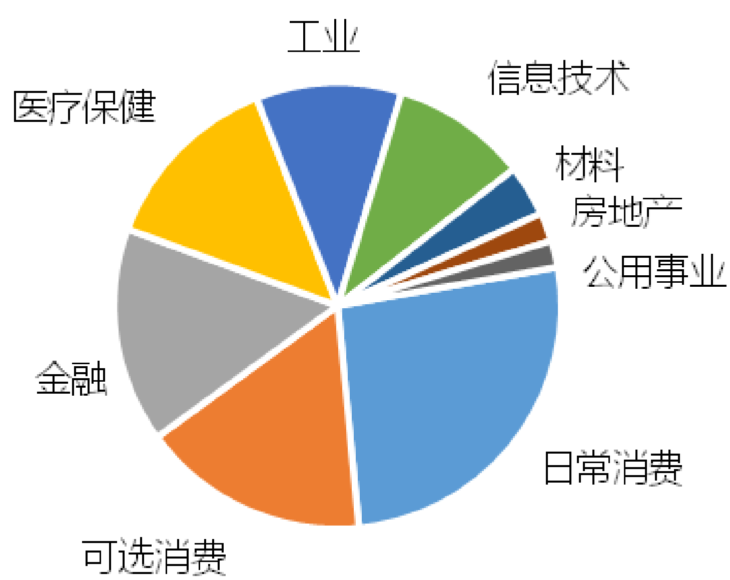
Data source: Wind, CreditEase Wealth

Chart 13: Growth stocks continue to outperform value stocks this year



Data source: Wind, CreditEase Wealth

Chart 14: The top 100 stocks with the largest holdings on the Mainland Stock Exchange are divided by market value.



Data source: Wind, CreditEase Wealth

statement:

The sources of economic data in this report are Wind, Bloomberg and other databases, and the market data are from Wind, Bloomberg and other databases.

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