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Asian equities in 2017

How to navigate an exciting 12 months

- Next year has a lot to offer Asian equity investors, from changes in geopolitics to movements in core bond yields
- This will create sector rotation and thematic investment opportunities
- We also look at sectors and stocks that benefit or are at risk from shifting industry dynamics

Play interview with Herald van der Linde

Disclaimer & Disclosures: This report must be read with the disclosures and the analyst certifications in the Disclosure appendix, and with the Disclaimer, which forms part of it

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Executive summary

The combination of changes in the geo-political environment, volatility in core bond yields and reforms in various countries, taking place against a backdrop of long-term, macro-insensitive developments suggests that 2017 will be anything but dull. We offer guidance on how to navigate Asian equities in 2017 and present several sector and stock ideas.

Key investment ideas for 2017

	Theme	Sector/stocks
1	Reflation or deflation?	Prefer tech, consumer discretionary, financials if US bond yield rises; dividend plays, utilities and staples for reversal in yield
2	Large-cap, best-in-class stock idea	We look at five, but India's HDFC Bank* tops the list
3	Which sector will bottom out?	We suggest container shipping
4	Which sector will be at the peak of its ROE cycle in 2017?	Asian chemicals, as 2018 supply increases will be digested
5	What new investment theme could emerge?	Defence spending – and we have some stock recommendations
6	Small-cap idea for next year	We select Taiwan's Ennoconn
7	2017 out-of-the-box stock idea	E-Ink in Taiwan, a global leader in e-paper
8	Shenzhen Stock Connect ideas	Which stocks to focus on in this new market
9	NPL trends in 2017	This trend is a key differentiator for Asian banks
10	What stocks could surprise on dividends in 2017?	Those with prospective free cash flow and current low pay-outs – Tencent, NetEase, Largan*

**An HSBC Asia Super Ten portfolio stock*
Source: HSBC

Overview

We think 2017 is shaping up to be an exciting year, with plenty of sector rotation and thematic investing opportunities on offer. We argue that 2017 could mark a change in the established political order in Asia, with a return of deflation one of the year's defining investment themes. In this report, we offer guidance on how to navigate markets and present sector and stock ideas for the next 12 months.

Reflation, deflation and China

Since 8 November, the day of the US election, Asian equities have struggled. Higher bond yields and a stronger dollar reflect an expected shift in US fiscal and monetary policy under the new administration. But while reflation is the theme of the day at the end of 2016, deflationary pressures have been a long time in the making. Meanwhile, the already stronger USD and higher bond yields are dampening growth prospects in the region, even before a new administration can even start putting new fiscal incentives in place.

That's why we think the return of deflation could become one of 2017's defining investment themes. In Asian equities, this could suggest rotation from short duration sectors that typically outperform in a reflationary environment (such as energy, tech and consumer durables) into high duration sectors (such as F&B, healthcare, pharma and utilities). Dividend plays would fit this latter group as well.

Changes in the perception of the trajectory of the US and China business cycle will be a key factor that determines the level of volatility in Asian equities in 2017. If pro-growth policies in the US prove to be elusive, the advent of lower global bond yields could be highly supportive as long as Chinese growth is not a major concern.

Next year could also mark a change in the established political order. The realist's view is that international politics is a zero-sum game: the declining influence of one power broker allows the advancement of another. In Asia, this is China. As a consequence, we belief that the defence industry will be of great interest to investors in 2017.

In a separate chapter, we look at sector and stock specific ideas in 2017. We argue that the container shipping industry will start a very slow process of recovery, with next year marking the low point in the sector's long-term performance. Conversely, we will argue that Asian chemicals will peak in 2017. We also include ideas for a large-cap best-in-class stock, a small-cap, and an out-of-the-box idea. We also look at stocks that may emerge as dividend players. We finish with a summary of our views on countries and sectors across the region.

Investment approach

For now, we focus on domestic-oriented markets, where structural growth is unlikely to be shaken easily. China, India and Indonesia rank highest. In particular, India's valuations now look attractive, following concerns that demonetization efforts could temporarily impact growth.

Risks and uncertainty suggest it is better to look at stocks thematically

But, in a world with many moving parts, it is helpful to step back and look at the bigger picture. We think Asian investors should place more emphasis on thematic investing and, to that end, have highlighted ten themes for the next ten years that we expect to evolve irrespective of the macro backdrop (see *Asia Equity Strategy: Ten themes for next decade*, 28 June 2016). We summarize these themes elsewhere in this report, but one in particular that might be the subject of continued interest in 2017 is the Asian defence industry.

In this note, we make no changes to our market/sector weightings. For details on our market and sector weightings, please see *Asia Equity Insights Quarterly: Cash rich, investment poor*, (6 October 2016) and *The Flying Dutchman – Asian equities: New rules of engagement* (15 November 2016).

Market and sector weightings

Market	HSBC weighting	Sector	HSBC weighting
India	overweight	Utilities	overweight
Indonesia	overweight	Energy	overweight
Philippines	overweight	Consumer Discretionary	overweight
China	overweight	Technology	neutral
Taiwan	neutral	Financials	neutral
Thailand	neutral	Materials	neutral
Singapore	underweight	Telecom	neutral
Korea	underweight	Industrials	underweight
Hong Kong	underweight	Consumer Staples	underweight
Malaysia	underweight	Healthcare	underweight

Note: Sector calls are based on our 'sector radar' (for details, see *Asia Equity Insights Quarterly: Cash rich, investment poor*, 6 October 2016)
Source: HSBC

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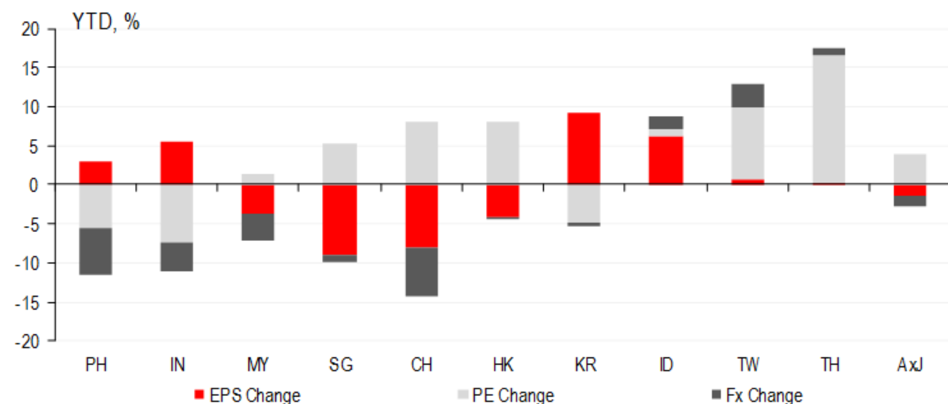
A look into 2017

- At the end of 2016, reflation is the main investment theme. But 2017 could mark a return to deflation-related trends in Asian equities
- Regional political dynamics will also change next year
- For now, we emphasise markets with large domestic components and structural growth drivers. Overweight China, India, Indonesia, and the Philippines

Year-to-date performance across Asian equity markets



Source: MSCI, Thomson Reuters Datastream, HSBC

Performance check

The chart above breaks down y-t-d market performance in USD terms into changes in three components – EPS, PE and FX. It shows that different markets have very different drivers. In the Philippines and China, FX movements have been very important. In Thailand, PE changes have dominated while EPS downgrades dictated Singapore's performance.

The two periods of weakness in Asian equities came at the start of the year and the last few weeks of 2016. Since 8 November, the day of the US elections, Asian equities have struggled. Higher bond yields and a stronger dollar reflect an expected shift in US fiscal and monetary policy under the new administration. Following Donald Trump's victory, HSBC has raised US growth prospects. We now expect US GDP growth of 2.3% in 2017e and 2.7% in 2018e. As a consequence, we expect the FOMC to tighten monetary policy by 25bp in 2016 and an additional 50bp in 2017.

Reflation – a key theme in late 2016

This is why reflation has become the investment theme that is dominating markets in the last weeks of 2016. But an expected uptick in growth and inflation goes hand in hand with a potentially more protectionist stance by the new policymakers in the US, with significant

implications for Asian equities, most of them negative for the moment. To reflect this, Asia FX has already depreciated, with consequences for domestic monetary policies. The idea of rate cuts, while still fresh only a few weeks ago, is gradually receding.

As always, movement in the RMB remains key. Weakness would have to be replicated elsewhere across the region. The MYR, in particular, has shown considerable weakness in recent weeks.

But deflation has been long in the making

But while reflation is the theme of the day, deflationary pressures have been a long time in the making, are largely structurally in nature and will not disappear quickly. Issues like aging populations, low productivity and high levels of debt are responsible, and they continue to linger. Meanwhile, the already stronger USD and higher bond yields dampen growth prospects, even before a new administration can even start putting new fiscal incentives in place. This supports HSBC's view that there are limits to the rise in US bond yields and appreciation of the USD. Indeed, the return of deflation could become one of 2017's defining investment themes.

As we witnessed earlier in 2016, there can upside to Asian equities in a scenario where bond yields fall back to levels seen earlier in the year, should the strength of the USD subside, Chinese growth hover around current levels and oil prices move higher. This is not a blue sky scenario for Asian equities – it is HSBC's base case scenario for end 2017. But before we arrive at that point, markets need to first digest the weaker currencies, higher bond yields and weaker growth across the region.

Indeed, the synchronization, or lack of it, between the US business cycle and China's will be key in 2017. In China, 2016 had been a turning point for producer prices, which moved from deflation to modest inflation. This was the result of strong infrastructure investment, a rebound in the housing market, cuts to overcapacity and some support from global commodity prices. We expect this to continue in 2017, lifting nominal GDP growth despite relatively stable real GDP growth (our economists forecast 6.5%). This will leave room for the People's Bank of China (PBoC) to keep the policy rate and the reserve requirement ratio on hold. However, a broad-based rise in inflation remains some way off, and selective tightening aside (for example, in the property market), we expect monetary conditions to remain broadly accommodative to support growth.

But a weaker than expected growth trajectory in China, especially if it should coincide with stronger growth in the US, could be problematic for Asian equities. Conversely, if pro-growth policies in the US prove to be elusive, the advent of lower global bond yields could be very supportive, as long as Chinese growth is not a major concern. Changes in the perception of these two business cycles will be a key factors that determine the level of volatility in Asian equities in 2017.

Other issues are potentially even more important for Asia. Mr. Trump's victory could mark a change in the established political order. The realist's view is that international politics is a zero-sum game: the declining influence of one power broker allows for advancement of another. In Asia, this is China.

> **“ China's military budget, second only to the US, has risen at a CAGR of 14% since 2006 and should continue to expand**

This is why we think one theme that is likely to feature is intra-Asian engagement. China will play an important role in the reshaping of the rules of engagement. Initiatives such as One Belt, One Road and the Asian Infrastructure Investment Bank (AIIB) will become more prominent. A possible revival of regional trade through agreements such as the Regional Comprehensive Economic Partnership (RCEP) is also possible. And in areas such as military co-operation, bilateral and multilateral trade agreements could become more prominent as countries aim to balance the rise of China. Elsewhere in this report we highlight defence as being an investment theme for 2017.

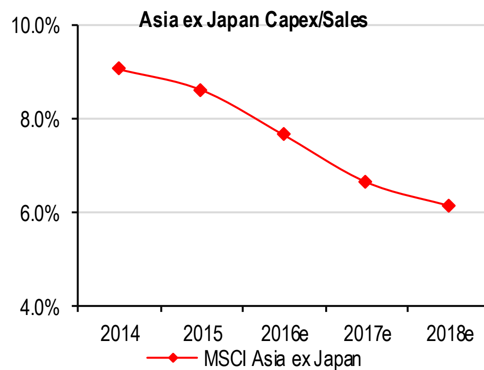
Capex cycle unlikely to recover

For now, this shift in power politics creates a world where policy uncertainty remains high. For the past three decades or so, businesspeople have been able to steer their companies based on a few hard assumptions. These were that trade barriers would continue to decline, that central bankers kept inflation in check and, more recently, interest rates would remain low, while global alliances, such as NATO, kept the world peaceful. These assumptions are gradually changing.

This limits the appetite to invest, although the allure of a stronger growth profile in the US could flow over into Asia and convince some companies to build new plants and buy new equipment. But the key assumption here is that, for now, it is difficult to see how the Asian capex cycle can recover significantly from current (weak) levels.

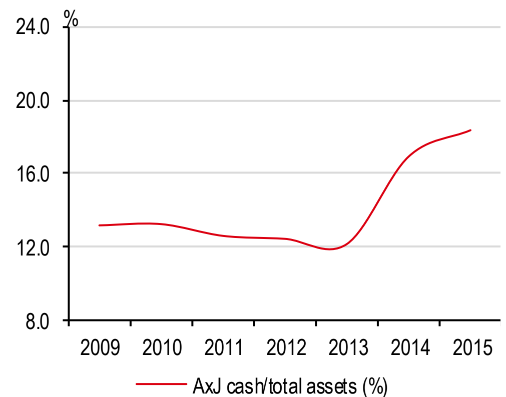
Cash levels on Asian balance sheets, already at historical highs, are likely to remain at these elevated levels. We would hope that more companies might want to re-think their dividend policies or indulge in share buybacks. But we suspect that many will simply accumulate even more cash.

No recovery in capex cycle



Source: MSCI, Thomson Reuters Datastream, HSBC

Cash levels are high in Asia



Source: MSCI, Thomson Reuters Datastream, HSBC

Growth pockets

With trade (potentially) on a back foot and investment appetite low, domestic growth drivers become increasingly important. The good news is that Asia has several. First of all, in some countries the population structure favours growth, as the size of the working population continues to increase. This is particularly the case in India and ASEAN, where demand for products continues to exceed existing supply.

India's GST and demonetization

Secondly, Asia is reforming. In India, the acceptance of a nationwide value-added tax (GST) will generate significant efficiency improvements. It should also allow companies to more effectively build supply chains across the nation. We expect this new tax to be implemented in late 2017.

In addition, the demonetization efforts in India are forcing savers to take money from under the mattress and put it into banks. This again allows for a better funding base for banks, which results in lower deposit and lending rates and, potentially, improved availability of credit. This comes at a cost. In the near term, expect some volatility in demand as consumers are busy replacing existing currency for new ones.

While this is a temporary phenomenon, it is something that investors are struggling to digest. The RBI has stated that roughly a third of banned currency came back into the banking system in just 10 days. This suggests that the whole demonetization effort should be completed by the end of 2016. Still, there are risks that the accompanying weakness in demand, especially for the small and mid-sized enterprises, increases defaults and has some adverse impact on the banking system.

> **"The return of deflation could become one of 2017's defining investment themes.**

Indonesian reform – making progress

In Indonesia, reform is also taking shape. Repatriation of funds under a tax amnesty is key here. Approximately 29% of funds have been repatriated to Indonesia, implying that more is to come before the deadline at the end of 2016. These funds will be put to work in 2017, funding government infrastructure projects. And improvements in infrastructure, as well as domestic security and a re-alignment with China, also appear high on the agenda for President Rodrigo Duterte in the Philippines.

Lastly, in China, while SOE reform is on the backburner, financial market reform continues. After a volatile start to the year, China's stable growth trajectory throughout the rest of 2016 allowed Beijing to step up efforts to cut industrial overcapacity and bad debt. New programmes – such as local government asset management companies, debt-to-equity swaps, securitization of non-performing loans, as well as debt write-offs – are all being tested. These strategies aim to shift the risk of bad debt from banks to a wider range of entities now willing to take on more risk as they search for higher yields. In the end, this approach might allow China to buy sufficient time to deal with the real problem – reducing debt on a sustainable basis.

Political dynamics

Domestic politics can sometimes push reform agendas down the list of priorities, especially if growth or currencies weaken. But in some countries political dynamics appear to be moving in the opposite direction – the weaker political position of key domestic policymakers is making reform more difficult. Alleged corruption scandals are often the issue here and this is why protesters have been on the streets in Seoul and Kuala Lumpur in the few last weeks.

Protesters have been on the streets in Seoul and Kuala Lumpur

In Indonesia, some Islamic organizations have asked for an investigation into Jakarta's mayor Basuki Tjahaja Purnama (commonly known as Ahok) based on his comments about the voting behaviour of Muslims. While this might have little to do with government policies, Ahok is a close ally of President Joko Widodo. The removal of the mayor in upcoming elections in February could have an impact on support for the president and his reform policies.

China has a twice-a-decade party congress in October which will feature changes to the seven-member Politburo Standing Committee, the 25-member Politburo and the Central Commission for Discipline Inspection. More changes are also likely to be introduced in the layers lower down the power structure. This large scale change in the bureaucracy implies a lot of politicking behind the scenes. It could mean that reform momentum slows or that new people emerge at the top of the decision-making pyramid that have new ideas on how to reform China.

One country where the president has the power to get things going is the Philippines, where President Duterte is seeking emergency powers to address the traffic gridlock in Manila.

Investment approach

For now, we focus on domestic-oriented markets, where structural growth is unlikely to be shaken easily. China, India and Indonesia rank highest. In particular, India's valuations now look attractive, following concerns that demonetization efforts could temporarily impact growth.

Risks and uncertainty suggest it is better to look at stocks thematically

But, in a world with many moving parts, it is helpful to step back and look at the bigger picture. We think Asian investors should place more emphasis on thematic investing and, to that end, have highlighted ten themes for the next ten years that we expect to evolve irrespective of the macro backdrop (see *Asia Equity Strategy: Ten themes for next decade*, 28 June 2016). We summarize these themes elsewhere in this report, but one in particular that might be the subject of continued interest in 2017 is the Asian defence industry, as mentioned earlier.

Market and sector weightings

Market	HSBC weighting	Sector	HSBC weighting
India	overweight	Utilities	overweight
Indonesia	overweight	Energy	overweight
Philippines	overweight	Consumer Discretionary	overweight
China	overweight	Technology	neutral
Taiwan	neutral	Financials	neutral
Thailand	neutral	Materials	neutral
Singapore	underweight	Telecom	neutral
Korea	underweight	Industrials	underweight
Hong Kong	underweight	Consumer Staples	underweight
Malaysia	underweight	Healthcare	underweight

Note: Sector calls are based on our 'sector radar' (for details, see *Asia Equity Insights Quarterly: Cash rich, investment poor*, 6 October 2016)
Source: HSBC

Having set the stage for 2017, in the next chapter we look at ten equity-specific ideas for 2017.

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A different angle

- We look at the 2017 outlook for equities by asking the right questions
- For example, which sectors could face a reversal in fortune and which stocks and themes will attract attention?
- Key issues are yield reversion, dividend surprises and out-of-the-box stock ideas

Ten ideas for 2017

In this chapter we look at Asian equities in 2017 from a different angle – by asking and answering a series of questions. For example, is there a stock that investors might have forgotten about and could make a comeback, however unlikely that might appear at the moment (late 2016)? Or which stock is forecasted to make the largest turnaround in earnings?

We also question if 2017 marks the bottom or peak in the long-term cycle for selected industries. Some industries might, due to consolidation or other events, start a process of recovery after years of distress and falling profitability. Meanwhile, other sectors featuring high PEs and strong profitability might see new entrants start to eat away at profit margins, allowing the cycle to slowly turn.

Key investment ideas for 2017

	Ideas for 2017	Sector/ stocks
1	Reflation or deflation?	Prefer tech, CD, FN if US bond yield rises; dividend plays, utilities and staples for reversal in yield
2	Large-cap best-in-class stock idea	We look at five, but at the top of the list is India's HDFC Bank*
3	Which sector will bottom?	We suggest Container Shipping
4	Which sector will be at the peak of its ROE cycle in 2017?	Asian Chemicals as 2018 supply increases will be digested
5	What new investment theme could emerge in 2017?	Defence spending –and we have some stock recommendations
6	Small-cap idea	We select Taiwan's Ennoconn
7	Out-of-the-box stock idea	E-Ink in Taiwan, a global leader in e-paper
8	Shenzhen Stock Connect ideas	Which stocks to focus on in this new market
9	NPL trends in 2017	NPL trends is a key differentiator for Asian banks
10	What stocks could surprise on dividends next year?	Those with prospective free cash flow and current low pay-out – Tencent, NetEase, Largan*

*An HSBC Asia Super Ten portfolio stock
Source: HSBC

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What about reflation vs deflation trades?

Answer: Look for yield reversion plays in 2017

Reflation is the theme of the day. Energy, banks and insurance have outperformed in the last few weeks. But deflationary pressures have been a long time in the making, are largely structurally in nature and will not disappear quickly. Aging populations, low growth in productivity and high levels of debt are at the very root of this issue, which continues to linger. Meanwhile, the already stronger USD and higher bond yields dampen growth prospects, even before a new administration can even start putting new fiscal incentives in place. This supports HSBC's view that there are limits to the rise in US bond yields and appreciation of the USD.

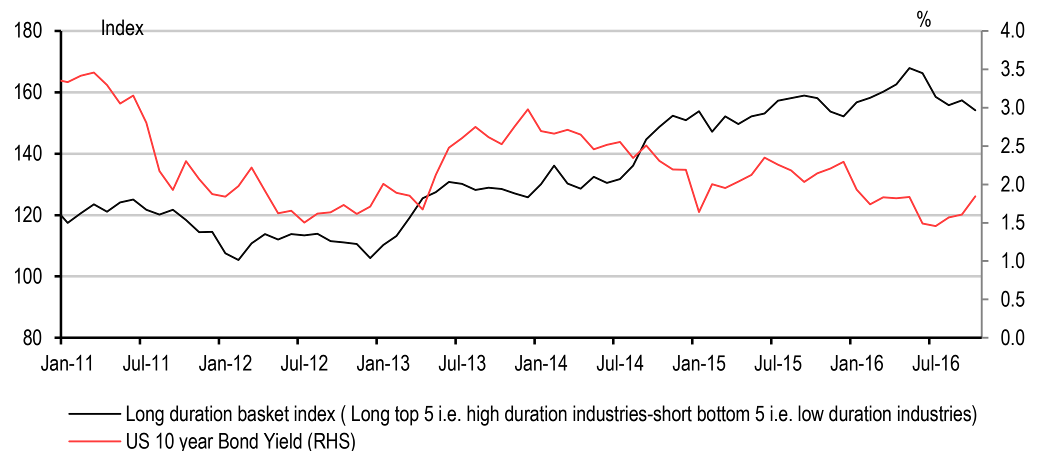
Thus, the return of deflation could become one of 2017's defining investment themes. While core bond yields currently rise, they could fall later in 2017. This, again, would suggest that sector rotation, between those that benefit from reflation and those that benefit from deflationary trends, will be key. The question now is, which sectors are they?

Equity duration

To assess this, we look at equity duration, a credit concept can be used in equities as well. We have written about this in the past (see: *The Flying Dutchman: Asian equities and the global bond yields*, 12 May 2015).

The chart below illustrates this equity duration concept at work – there is a negative relationship between high duration sectors' performance and bond yields. Investors should rotate between low and high duration sectors as bond yields rise or fall.

High duration sectors underperform when bond yields rise



Source: HSBC

The question is which sectors are high, and which low? This is illustrated in the next table. When yields peak, investors should switch from short duration sectors such as energy, tech and consumer durables into high duration sectors such as F&B, healthcare, pharma and utilities. Dividend plays fit this classification as well.

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Sector performances and yield reversal

If US bond yields rise	
Sector	**Preferred industries (short or low duration)**
IT	Tech hardware, Semiconductors
CD	Consumer Durables, Commercial services
FN	Real Estate, Diversified Financials, Banks
MT	Materials
If bond yields decline	
Sector	**Preferred industries (long or high duration)**
UT	Utilities
CS	Household products, Food & Beverage, Food retailing
TS	Telecom
HC	Healthcare Equip, Insurance
	Software & services

Source: HSBC

Large-cap best-in-class stock idea

Answer: India's HDFC Bank

In the past, we have written about Asia's best-in-class companies. These are companies that have what it takes to generate high levels of profitability in the next few years due a strong brand, an agile management or other company specific attributes.

Within this list of just over 50 companies across Asia, we revisited this list and looked at the top five stocks (in market cap) ranked by upside to analyst target price. This list is shown below. The Chinese internet names dominate, but India's HDFC Bank – *an HSBC Asia Super Ten portfolio stock* – is at the top of the list.

Top five largest best-in-class names in Asia, ranked by upside to target price

BLM code	Company	Rating	Market cap (USDm)	Upside* to TP (%)
HDFCB IN	HDFC Bank*	Buy	44,259	37
HDFC IN	HDFC	Buy	28,776	22
BIDU US	Baidu	Buy	57,787	34
BABA US	Alibaba Group*	Buy	226,030	33
700 HK	Tencent Holdings	Buy	235,521	28

At close of 2 December 2016
**An HSBC Asia Super Ten portfolio stock*
Source: HSBC

Despite weak loan demand in India, HDFC Bank's retail loan growth remains high (over 20% as per November 2016), led by auto and personal loans, which are 40% of all retail loans. In addition, its CASA franchise remains solid and asset quality is excellent, with a gross NPL ratio of 1%. Our analyst forecasts 20% earnings CAGR over the next three years.

More on HDFC Bank: *2QFY17 – safe harbour in a stormy environment* (26 October 2016)

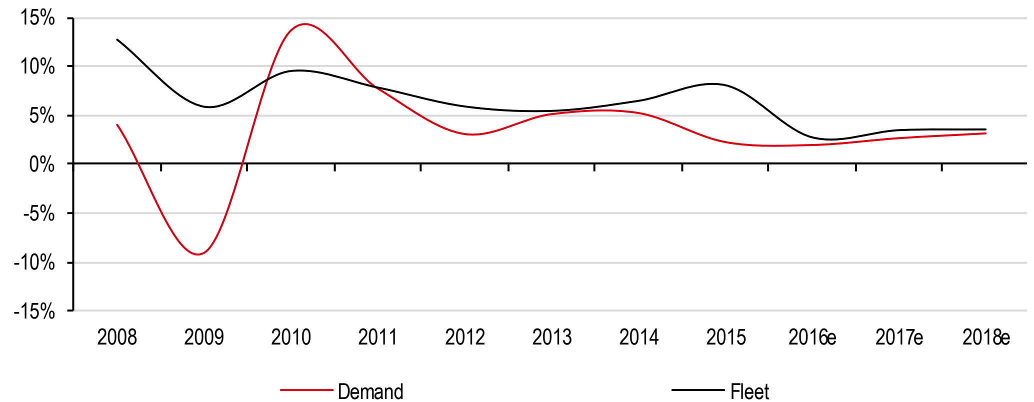
Which sector will bottom in 2017?

Answer: Container shipping

This section looks at long-term sector dynamics across the region and asks which sector is at a long-term bottom with regards to sector performance.

At the end of 2016, there were many container ships and too little trade to fill them up. This demand-supply mismatch has existed since the 2009 global financial crisis, which hit the container shipping industry hard. Barring 2010, when stimulus and restocking in the US led to a temporary recovery, the industry has in aggregate lost money. Normally, industries consolidate in such an environment, as companies go bankrupt or exit the industry. But low interest rates and state backing allowed even the weaker players to survive.

Demand-supply gap could narrow in 2016-18e, but a meaningful sector profit recovery is unlikely until after 2018e



Source: Clarksons Research Services, HSBC estimates

The dynamics have started to change in the last 18 months, with a series of consolidations and several bankruptcies. We now think that the demand-supply situation can start to find a balance. This process could accelerate in 2017, allowing a balanced market by 2019-20.

The winners will have two distinct characteristics – they will have scale advantages or be niche players. In Asia, we prefer SITC due to its focus on intra-Asia, which makes it relatively immune from weak inter-continental trade flows.

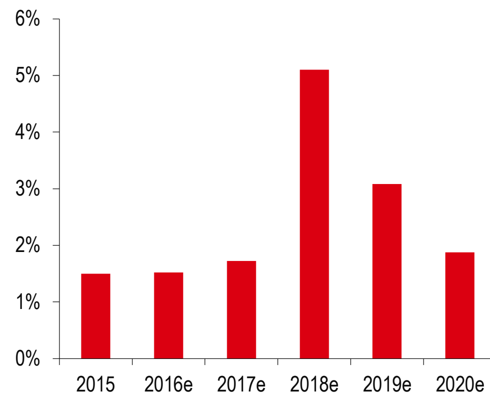
More details here: *Global Container Shipping: SCFI slips for the third consecutive week* (21 November 2016)

Which sector will be at the peak of its ROE cycle in 2017?

Answer: Asian chemicals
This section looks for a sector that has been performing well but is likely to peak in 2017. We believe the chemicals sector fits the bill.

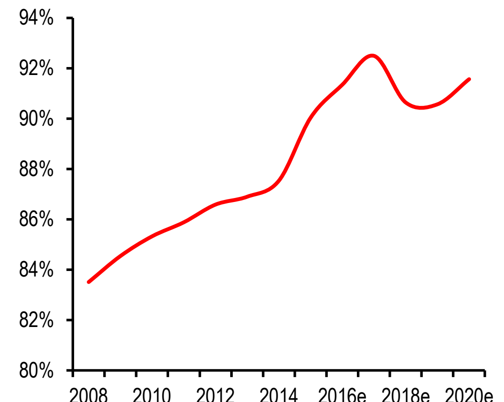
Over 2017-18 our analysts expect to see as many as eight new ethylene crackers come on stream, adding substantial new ethylene capacity (8.6m tons, to be exact). This wave of new capacity, when it hits in 2018, will take global ethylene capacity growth from 1.7% in 2017 to 5.1% in 2018.

Global ethylene capacity growth



Source: IHS Chemical, HSBC estimates

Global ethylene operating rates (%)



Source: IHS Chemical, HSBC estimates

With the peak of supply additions coming in 2018e, supply will likely remain lower than demand in 2017. Operating rates and spreads should therefore be above normalised levels.

However, the closer we get to 2018, the more visible the wave of new supply becomes. Once consensus starts to discount that in estimates, even if spreads remain elevated in the near term, we believe share prices will start to discount new supply.

A stock exposed to this sector is LG Chemical (051910 KS, KRW231,500, Buy) which benefits from higher PVC prices. It is the second-largest producer in Asia, ex-China.

More details here: *Asia Refining: The momentum continues* (14 November 2016)

2017 out-of-the-box stock idea?

Answer: E-Ink in Taiwan (8068 TT)

We ran through our database to look for stocks that have fallen out of favour, but where industry dynamics have started to turn and consensus might be wrong. Our 2017 out-of-the-box idea is Taiwan's E-Ink. E-Ink is the originator and global leader in ePaper technology. It has a 95% global market share in e-paper.

Electronic paper and e-paper are display devices that mimic the appearance of ordinary ink on paper. Unlike conventional backlit flat panel displays that emit light, electronic paper displays reflect light like paper. There are plenty of other applications, ranging from architectural designs to museum brochures and digital signatures on contracts.

While this sounds promising, this company has had some difficult years. In the last few years, eReaders were not the consumer craze that the company had hoped for. Indeed, the main driver of earnings was not e-paper but a fee for a technology widely used by panel makers for which they own a patent. The company hardly booked any earnings over 2013-15.

However, the number of applications for e-paper are on the rise. An example is the increased use of electronic shelf labels. Store operators can change prices wirelessly while the lithium battery behind the tag can last years. Another development is to use the e-paper display to replace the baggage stickers for checked luggage at airports or train stations.

Our analyst expects the company to almost break-even at the operating level in 2016 (a loss of TWD200m, down from TWD1.5-2bn in previous years). He then expects EPS to go from TWD1.25 in 2016 to TWD1.96 in 2017. Ironically, the patent fee – which was the main earnings driver and booked as non-operational income – is set to decline.

More details here: *Lower licensing fee, but OP surprise continues* (15 November 2016)

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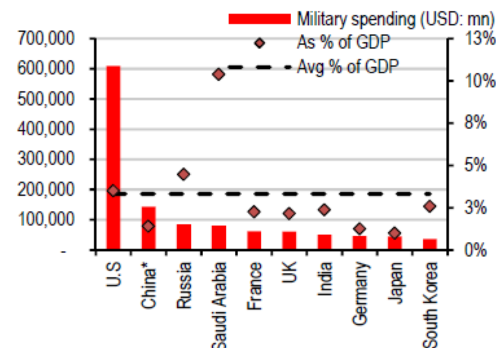
New investment theme in 2017?

Answer: Defence on the offence

Asia's defence spending is surging and the recent rapid growth is only set to continue. According to SIPRI (the Stockholm International Peace Research Institute), Asia's total defence spending has increased 75% over the last decade, significantly faster than the 1% growth across the Americas and Europe's 7% increase over the same period. SIPRI estimates that Asia spent USD192bn more in 2015 on military expenditure than in 2005.

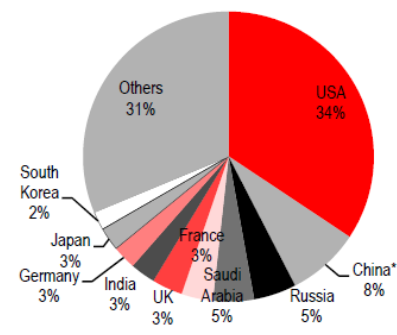
China's military budget, second only to the US, has risen at a CAGR of 14% since 2006 and should continue to expand. This has attracted substantial attention but India's increasing defence spending is also expected to become a more visible theme over the next decade.

Top ten military spenders and spending to GDP (%)



*HSBC estimates based on 2013 China's Defence While Paper and Ministry of Finance
Source: Stockholm International Peace Research Institute (SIPRI)

Share of global military spending



*Data is HSBC estimate based on 2013 China's Defence White Paper and Ministry of Finance
Source: SIPRI

There are two reasons to expect this trend to continue. First, both China and India have embarked on efforts to modernise their military capabilities. Second, there has been a general uptick across the region in new capabilities. The region has, for example, seen substantial investments in naval assets (especially submarines), missile technologies (both offensive and defensive), 4th and 5th generation fighter capabilities and cyber-warfare and electronic warfare systems.

The defence industry has some relative attractions for investors. It is dominated by high barriers to entry (including high R&D spending and government relationships), few competitors (as countries try to reduce their reliance on foreign suppliers), relatively visible and secure revenue streams, and a continuous product development roadmap.

A number of companies are well placed to benefit from these developments. Here are some examples:

- China's warship market is dominated by two shipbuilding giants: **China Shipbuilding Industry Corporation (CSIC)** and **China State Shipbuilding Corporation (CSSC)**. CSICL (601989 CH, RMB7.44, Reduce) and COMEC (317 HK, HKD11.94, Buy) are their listed companies.
- **China Aviation Optical** (002179 CH, RMB36.99, Buy), also called JONHON, is the leading defence-integrated connection solution provider in China.
- **Haige Communications** (002465 CH, RMB11.88, Buy) is China's leading provider of radio and satellite communications equipment and services, putting it at the forefront of the modernisation of the military (the company's main customer).

- **Larsen & Toubro** (LT IN, INR1361.85, Buy) stands to benefit the most from India's increasing defence spending, in our view. The company expects the defence sector to contribute c10-15% of the order backlog over the next three years. (see *India Industrials: Green shoots emerging*, 22 April 2016).
- In Korea, **Hanwha Techwin** (012450 KS, KRW42,650, Buy) will accelerate its transformation into a defence company.

Best 2017 small-cap idea?

Answer: Ennoconn (6414 TT)
The Internet of Things (IoT) has reached the factory floor, with applications ranging from energy management and industrial robots to analysing production performance and quality control. Our analysis shows that IoT has moved on from the first stage of cutting costs – sensors now cost less than USD1 – to improving connectivity and data analysis. 2017 should be a turning point.

This has major implications for companies involved in semiconductors, industrial PCs, cloud software and hardware. We think a beneficiary in Asia will be Ennoconn. For this company, analyst Jenny Lai argues that the fast growth witnessed in 2016 is the minimum to expect in 2017e. She attributes growth drivers to new orders. The company also plans to expand geographically and build an industrial brand business. Ennoconn's derives over 70% of its revenue from the US and Europe markets, leaving Asia offering significant potential to drive long-term growth.

More details here: *The Industrial Internet of Things: The next step – smarter, faster and better connected* (22 November 2016)

What about Shenzhen equities in 2017?

Answer: Interesting, but do your homework first. Here are five companies to zoom in on
The Shenzhen-Hong Kong Stock Connect programme will be launched on 5 December, representing another milestone in the opening up of China's capital markets. Given that many companies are not yet well known, it might take some time for investors to build substantial positions in this market. But it is a market that is hard to ignore – together with the Shanghai-Hong Kong Stock Connect, this market allows access to over 1,400 new stocks, or some 80% of the total A-share market capitalization. It offers opportunities to buy a range of stocks currently unavailable in the Hong Kong and Shanghai markets with distinctive features related to size, private ownership, and new economy exposure.

But for those new to the market, which stocks should one focus on first? Here are our five picks:

- **Hikvision** is the market leader in China and the world's second-largest provider of video surveillance, security equipment and services.
- **Wangsu Science & Technology** – *an HSBC Asia Super Ten portfolio stock* – is the largest content delivery network (CDN) services provider in China, with 2016e market share at c50%.
- **Shenzhen Inovance** is majority-owned by senior management and focuses on industrial automation products. It partners with Yutong, China's largest bus vendor, to manufacture environmentally friendly vehicles.
- **Wuliangye Yibin** is the No 2 baijiu (Chinese liquor) brand of spirits in China after Kweichow Moutai.

- **Wanda Cinema Line** is a top cinema operator in China, with c15% market share in terms of box office revenue.

More details here: *Shenzhen-Hong Kong Stock Connect: An essential guide* (10 November 2016)

NPL trends key to bank sector performance in 2017

Answer: They vary in different markets
Banks across the region are facing a difficult operating environment. Demand for loans is low, interest rates have declined and the regulatory environment is becoming increasingly complex. Asset quality is therefore often a defining factor across the region, with markets where non-performing loan (NPL) risk decline being more favourable than those where bad assets are being accumulated by the banking system.

The Philippines is the only banking sector that appears relatively immune to the challenges seen so far. We continue to expect sustained and strong credit growth with minimal asset quality risk in the system. Elsewhere in ASEAN, we expect the protracted asset quality problems in Thailand and Indonesia to peak out by end 2016, which means credit cost should at the very least stabilize in 2017.

In China, we expect no significant changes to banks' fundamentals. We forecast stable margins, orderly NPL recognition and capital strength above requirement for most banks. A key upside risk to Chinese banks include the expansion of the existing NPL securitization plan and more asset managers to buy and transfer bank NPLs out of the banking system. Conversely, a key downside risk includes further debt equity swap programmes and public private partnership programmes posing new capital and liquidity risks for banks with increased involvement with equity.

In Korea, we expect the existing earnings trend to continue in 2017, backed by stable margin, low credit cost and tight cost control. Further risk of NIM contraction is likely to be limited as the pricing environment is improving post 2015 government-led mortgage reform, and banks have begun to raise lending rate spreads. Also, despite ongoing corporate restructuring, we expect to see stable credit cost trend backed by improved level of new NPL formation after years of asset clean-up efforts at large commercial banks.

In India, the focus has been on demonetization. HSBC banks analyst Sachin Sheth believes that this will attract consumers to electronic transaction channels. This is positive for private banks which have superior technology and products than public sector banks. However, demonetization could impact asset quality, especially for real estate developers and gems and jewellery companies.

Which stocks could surprise on dividends in 2017?

Answer: Quite a few, including Tencent, NetEase, and Largan (*an HSBC Asia Super Ten portfolio stock*)
Asia is not witnessing any recovery in capex, which has implications for equities. For example, dividend pay-out ratios should rise further. Some companies that have not paid dividends in the past might well opt to do so in the future. They won't show up in current dividend yield screens, given still low yields and pay-out ratios.

Below, we identify companies that could start to pay much higher dividends in the future as their balance sheets swell with cash. We do this by looking at prospective free cash flow, existing cash balances and current low pay-out ratios (that could rise in 2017). The top 10 stocks are listed in the following table.

Future dividend plays

Stock code	Company	Sector	Country	Mcap (USDm)	ADTV (USDm)	FCF margin 2015	FCF margin 2016e	FCF margin 2017e	Cash/assets 2015	Cash/assets 2016e	Cash/assets 2017e	Pay-out ratio 2015	Pay-out ratio 2016e	HSBC rating	HSBC target price	2 Dec closing price
700 HK	Tencent Holdings	Tech	China	233,367	361	91%	97%	62%	26%	30%	48%	9%	9%	Buy	HKD245	HKD191
NTES US	NetEase	Tech	China	28,644	245	26%	27%	27%	50%	55%	58%	22%	18%	Buy	USD266	USD220.59
3008 TT	Largan Precision*	Tech	Taiwan	15,175	76	36%	40%	37%	55%	65%	70%	28%	20%	Buy	TWD4,473	TWD3,610
300017 CH	Wangsu Sci & Tech*	Tech	China	6,675	89	17%	20%	23%	30%	57%	55%	6%	12%	Buy	RMB89	RMB57.95
TECHM IN	Tech Mahindra	Tech	India	6,768	11	20%	21%	21%	16%	22%	26%	21%	20%	Buy	INR510	INR473.4
300251 CH	Enlight Media	Cons Disc	China	4,749	35	25%	29%	31%	18%	20%	19%	28%	17%	Buy	RMB14	RMB11.15
000089 CH	Shenzhen Airport	Industrials	China	2,674	14	24%	46%	30%	15%	25%	31%	11%	25%	Hold	RMB9.5	RMB8.98
1970 HK	IMAX China	Cons Disc	HK	1,747	4	30%	29%	31%	41%	71%	70%	0%	16%	Hold	HKD40	HKD38.0
8069 TT	E Ink Holdings	Tech	Taiwan	790	10	15%	23%	23%	21%	25%	31%	0%	26%	Buy	TWD25.5	TWD22.1
6826 HK	Shanghai Haohai Biotech	Healthcare	HK	768	1	24%	26%	21%	77%	75%	71%	0%	21%	Buy	HKD50	HKD37.1

**An HSBC Asia Super Ten portfolio stock*
Source: HSBC

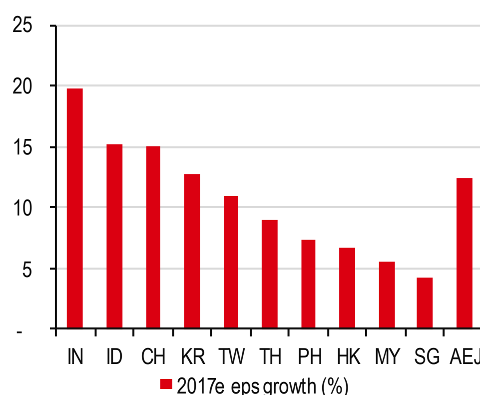
HSBC

Asian market views

- 2017 is likely to be a year of uncertainty, so focus on markets with strong domestic components
- Reform will perform, stay with structural growth ideas
- We are overweight on India, Indonesia, China and the Philippines; underweight on Singapore, Malaysia, Hong Kong and Korea

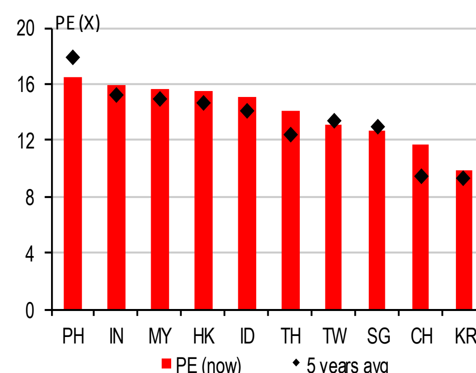
Reform will perform

2017 earnings growth estimates



Source: MSCI, Thomson Reuters Datastream, HSBC

12m-fwd PE estimates



Source: MSCI, Thomson Reuters Datastream, HSBC

In this chapter, we summarise our country views for 2017. In general, at the end of 2016 we advocate an investment strategy that emphasizes structural growth stories, with low external exposure and strong domestic demand. We are Overweight India, Indonesia, China and The Philippines.

India

Structural reform momentum remains intact

We are Overweight India. Key here is that India continues to push through tough structural reforms. India is progressing with a tax unification proposal (GST) that, while still somewhat complex, will create a new tax environment that allows Indian companies to more effectively build supply chains across the country. In addition, the latest anti-corruption drive through demonetization should be a long term positive for doing business in the country. While these reforms could bring some near-term pain and a build-up of NPLs in the banks in 2017, we expect a positive long-term impact on growth.

Consensus is forecasting 18% earnings growth in 2017. This appears a bit on the high side – we expect earnings growth to be around 13% next year. The reasons for our caution include a higher base for CY17 earnings, some recovery in commodity prices and an elusive private sector capex recovery. However, 12% earnings growth is still quite high in the regional context,

and is positive for equities. That said, one key issue in Indian equities is the wide divergence in valuations. Thus, stock/sector selection is imperative when seeking higher returns.

Among sectors, we continue to like consumer over investment names, especially those with a rural focus. In addition to higher agricultural prices, higher minimum support prices and a better monsoon, there are other catalysts like infrastructure improvement and crop insurance schemes. Any fall in consumer staples would present a good opportunity to buy some structurally sound stories in the sector. We also like financials (banks) which benefit from higher liquidity in the near-term, although we need to keep a close eye on NPL formation. In the long term, the move to push consumers towards electronic transaction channels vs cash also bodes well for private banks which have superior technology and products than PSU banks.

Indonesia

We are positive on Indonesia in the regional context. We continue to regard Indonesia as one of the prominent structural growth stories in the region and the recent equity market correction is a good buying opportunity. The combination of a tax amnesty, a build out of much-needed infrastructure and the roll-out of a healthcare scheme should support growth going into the New Year. With regards to the tax amnesty programme and repatriation, approximately 29% of funds have been repatriated to Indonesia by the end of November, implying that more is to come. These repatriated funds will be put to work in 2017, allowing for funding of government infrastructure projects. Looking ahead, the equity market's performance may hinge on a stronger earnings outlook and continuation of the positive earnings revision ratio trend.

Some have pointed at rising political risk following demonstrations against the Jakarta mayor, a Christian who had made some comments on Islam. While this might have little to do with government policies, the mayor is a close ally of President Joko Widodo. The removal of the mayor in upcoming elections in February could have an impact on support for the president and his policies.

Infrastructure investment remains a key theme

Based on the macro-environment, we see consensus forecast for 11% EPS growth for 2017 as quite reasonable. We are expecting a pick-up in economic activity due to greater and more efficient fiscal spending, stronger commodity prices and resilient consumer spending. Infrastructure investment remains a key theme for the market, as Indonesia looks to modernise its road-rail network. In addition, our banks' analysts expect the asset quality concerns to peak-out by end 2016, which means credit cost should at the very least stabilize in 2017. This should benefit Indonesian banks.

The Philippines

We are positive on the Philippines in the regional context. Resilient domestic demand and investment-led growth has made the country somewhat insulated to the macro slowdown affecting other markets. The recent sell-off seen in the equity market following the US presidential election has pushed the elevated valuations down to more reasonable levels. With foreign holdings falling to near five-year lows, we see ample opportunity for a rebound, given that fundamentals remain sound. In this scenario, consensus expectations of 7.4% EPS growth for 2017 looks low to us and could surprise on the upside.

A new attitude to foreign relations appears to be gradually unfolding

Domestically, it's well reported that President Duterte has a strong law and order agenda, while a new attitude to foreign relations appears to be gradually unfolding. However, so far we believe there is a difference between the rhetoric and actual policies, so the impact on equities from some of the new measures will likely be small.

Among sectors, we like consumer companies that benefit from a strong domestic demand environment. We are also constructive on property stocks, given the positive macro outlook and strong infrastructure development, which should benefit land prices. Meanwhile, the banking sector appears relatively immune to the challenges seen so far. We continue to expect

sustained and strong credit growth, with minimal asset quality risk in the system. For utilities, liberalisation of the retail market, including a power tariff cut in mid-2017, is likely to introduce more competition among power companies (distributors and generators).

China

Large domestic market and low fund holdings are the key

We are overweight on the China equity market in the regional context. Our view on growth in China has not changed. However, in an environment where risk to domestic growth is lower than to export growth in 2017, we prefer markets with a large domestic component. In addition, mutual funds' position in Chinese equities is low. This means that immediate selling pressure (in the wake of higher global bond yields) is much more muted.

While bilateral trade disruptions should not be dismissed given previous comments by incoming US President Donald Trump, we point out that such an aggressive lose-lose policy could be blocked or toned down by the US Congress.

Further, China's A-share market tends not to correlate with global major market indices such as S&P500, with a correlation coefficient around 0.3 versus that of 0.6 for the HK market and MSCI China. Shenzhen-listed stocks in particular offer more country diversification compared to larger multinational stocks in developed or emerging market universes. This is also reflected by A-share's lower export exposure; or 13-14% revenue vs. 17% for the MSCI China universe.

Finally, higher RMB volatility will lead to stronger southbound inflows for the HK market. We have found strong and positive correlations (c90%) between the southbound-northbound net flows and the pace of RMB depreciation, reflecting mainland investors' anxiety to utilize current limited channels to invest offshore financial assets and diversify their FX exposure.

Taiwan

Stronger expectations of new Apple product launch

We are neutral on Taiwan in the regional context. After a year of flattish earnings growth, Taiwan is positioned to see 14% earnings recovery in 2017e. Lack of significant new tech product was one of the reasons that Taiwan saw limited growth in 2016, aside from slower growth of global smartphone demand and tougher competition from China on the tech supply chain. However, 2017 is another year with stronger expectations of new Apple product launch that could potentially lead to growth recovery of the supply chain in Taiwan. With the earnings recovery, we expect Taiwan's ROE to recover from 12.1% in 2016e to 13.2% in 2017e.

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Domestically, political uncertainty was high in Taiwan last year because of presidential election. The most immediate impact to the domestic economy after the election was perhaps the number of incoming Chinese tourists, which still shows no sign of growth recovery. In addition, with our expectations of TWD to depreciate against USD in 2017, potential outflow of foreign investments could be a major risk for Taiwan market next year, especially after strong buying by foreign investors in 2016.

Within tech, our analysts are positive on foundry, display, automation, industrial PC and selective tech components, but conservative on OSAT, PC ODM, and handset. Within Taiwan non-tech, our analysts are positive on telcos, cement, neutral on financials, petrochemicals, energy, and cautious on transportation and textile.

Thailand

We are neutral on Thailand in the regional context, given its modest economic outlook for 2017. Growth appears to be weak but on a steadier path with the government managing to get infrastructure projects moving. Several public investment projects – motorways, mass transit system and railways – have progressed to the bidding stage in recent months. Better fiscal spending and resilient farming and tourist income should support GDP next year.

However, investment from the private sector remains elusive. We also see some downside risks ahead, from global economic uncertainty and weakness in Thailand's household income growth. Support from goods exports looks limited as well, given that country's manufacturing PMI has continued to contract in recent months.

In the current environment consensus has been cutting 2017 earnings numbers and now expects EPS growth to come in at 9.0% for 2017, down from 13.5% a couple of months ago. Meanwhile, the market has yet to price in lower earnings – with a 12-month forward PE of 14.1x it is trading at a c14% premium to its five-year average.

Coronation of the new king in 2017

In 2017, political developments will remain a key theme for investors. The country awaits the coronation of its new king, Crown Prince Maha Vajiralongkorn, following the death of his father the hugely popular King Bhumibol Adulyadej who ruled for over 70 years. New dynamics will be at play between the monarchy and the junta government.

In terms of sectors, we like banks in Thailand. There is growing evidence of NPLs peaking soon. As a result, we believe that credit cost will peak this year, leading to a significant rebound in earnings growth by 2017. We remain cautious on Thailand's property market (on missing pre-sales targets) and telecoms (concerns about competition and high spectrum cost).

Singapore

Risk from rising protectionism

We are underweight on Singapore in the regional context. Singapore is an open economy with high exposure to global trade, making it vulnerable to the risk of rising protectionism. While there are other trade deals on the horizon and ASEAN integration continues, a meaningful boost to trade volumes in 2017 is unlikely. Export weakness and languishing oil prices continue to weigh on the oil-related manufacturing sectors (such as marine/offshore engineering). Our economist sees a weak 2017 ahead, amid downside risks stemming from policy uncertainty in the US and EU.

Meanwhile, consensus remains guarded, forecasting a 4.3% earnings growth for next year on a weak base, following a c8% earnings contraction pencilled in for this year. We see downside risk to 2017 estimates in a volatile global environment. Thus, despite attractive valuations and high yield, we see limited upside to the equities. Mutual funds are also underweight on equities in Singapore, and we see a limited possibility of improvement in the near future due to a lack of growth catalysts.

Among Singapore's sectors, we continue to see downside to banks (NPLs and debt saturation), consumers (weak sentiment) and telecoms (new entrant risk). Looking from a bottom-up perspective, we see some opportunities in high-yield stocks. HSBC analyst Pratik Ray expects policy rationalisation in 2017, which should translate into improved volumes and asset churn. While SREITs have done well, he continues to find pockets of opportunities, particularly among the office and hotel REITs.

Malaysia

Malaysian equities face numerous headwinds

We are underweight on Malaysia in the regional context. Risks to the equity market remain on the downside, given a subdued macro outlook, as well as pressure on external accounts. Consumer demand is constrained by high household debt and companies have seen their margins eroded in a soft demand environment that has been punctuated by rising input prices.

Against this backdrop, there is only so much the revenue-constrained government can do in terms of providing fiscal stimulus. Our economists believe that the cash hand-outs outlined in the 2017 Budget could translate into stronger consumer spending, particularly earlier in the year. A possible snap election could further boost activity. Nevertheless with consumer confidence low and the labour market slowly weakening, it remains to be seen if such a bounce can be sustained.

Meanwhile, the recent move by the central bank, BNM, to stop foreign banks from trading the ringgit in the offshore non-deliverable forwards market (NDF) could be seen by some as a capital control measure, hurting investor sentiment.

Among sectors, we think utilities provide a good investment opportunity as power demand growth has been supported by GDP improvement and hot weather, despite weak industrial demand. We are negative on banks because we believe there is considerable downside risk to earnings stemming from NIM pressure, slowing loan growth, and rising credit cost. We also remain cautious on telecoms. The industry structure is challenging (regulatory uncertainty and heightened competition) and valuations are rich (relative to regional peers). We do see some bottom-up opportunities in consumer.

Korea

Direction of politics and exports important in 2017

We are underweight on Korea in the regional context. Business sentiment remains subdued as a series of headlines detailing the nascent restructuring of heavy industries, the bankruptcy of Korea's largest shipping company, and smartphone recalls, continue to weigh on confidence. Recently, President Park's very low approval ratings (5%, according to Gallup Korea) have raised concerns over her ability to govern until the next scheduled presidential election in December 2017. If she steps down or is impeached, there will be a new election in 60 days. There could be concerns that fiscal policy, private investment and economic sentiment all slow temporarily amid this political uncertainty.

Among sectors, we are positive on Korean banks where we expect the solid earnings trend to continue in 2017, backed by stable margin, low credit cost and tight cost control. Within the tech sector, we think Korean dominance in the memory industry will continue in 2017, especially in the DRAM segment, given a high technology barrier of entry. Samsung and Hynix will maintain near 80% global DRAM market share for the next two years, in our opinion.

For Korean automakers, we expect domestic sales to remain sluggish through 1H17, which could trigger pricing pressure and margin deterioration for the sector. In terms of Korea industrials, we think overseas new orders will continue to slow down in the low oil price environment.

Hong Kong

Higher US rates negative for HK equities

We are underweight on Hong Kong in the regional context. While domestic demand has been resilient in recent months, activity may soften again after the recent increase in real estate stamp duty, an imminent Fed rate hike and uncertainty about US policy after the election. A stronger USD and higher interest rates are negative for the capital market in general, given that HKD is pegged to USD.

Meanwhile, primary sales in the property market have continued to strengthen, underlined by the recent project launches which generated strong sell-through rates. We expect the home price growth to remain positive in the near term but highlight that the key downside risks will be driven from the macro side, including potential policy risk if property prices continue to grow at a rapid pace which lead to further deterioration in housing affordability.

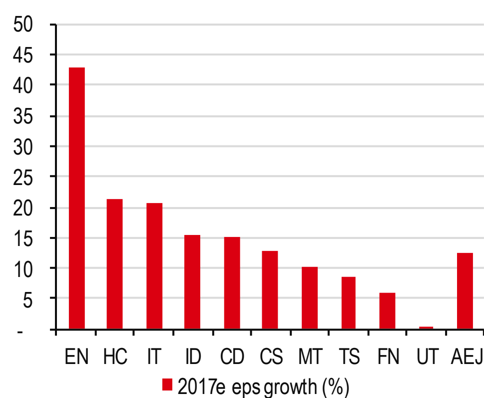
A successful launch of the Shenzhen-Hong Kong Stock Connect is an upside risk to our view. HSBC's equity strategist, Steven Sun, believes that the Shenzhen-Hong Kong Stock Connect is likely to boost Hong Kong's small-caps, based on the performance of the Shenzhen market.

Asian sector views

- In this section, we discuss the 2017 outlook and investment themes for Asian sectors and industries
- We are overweight on utilities, energy and consumer discretionary; underweight on consumer staples, industrials and healthcare
- Industries with a positive outlook in 2017 include Asia refiners, Korea memory markers, Hong Kong utilities and India steel and zinc players

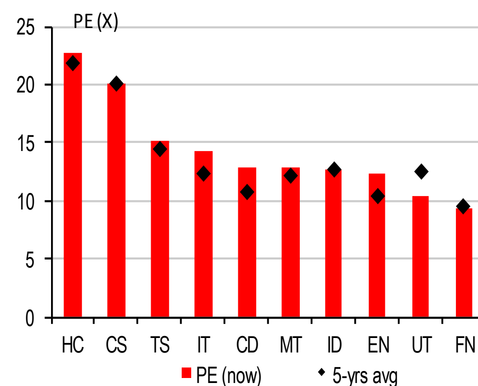
A thematic approach

2017e earnings growth estimates



Source: MSCI, Thomson Reuters Datastream, HSBC

12-month forward PE estimates



Source: MSCI, Thomson Reuters Datastream, HSBC

In this chapter, we summarize our sector views across the region. Overall in Asia, we are overweight on utilities, energy and consumer discretionary sectors, and underweight on consumer staples, industrials and healthcare.

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Banks

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China banks

We don't see surprises to fundamentals and expect stable margin, orderly NPL recognition and capital strength above requirements. We are cautious on valuation as banks' dividend yield premium to treasury and wealth management products has reversed back to the five-year average. Key upside risks include expansion of the NPL securitization plan and more asset management companies to help buy and transfer bank NPLs out of the system, retail banking and wealth management business enhancing ROE. Key downside risk include further debt equity swap programmes and public private partnerships posing new capital and liquidity risks to banks with increased involvement with equity

Korea banks

We expect the solid earnings trend to continue for Korean banks in 2017, backed by stable margin, low credit cost and tight cost control. While the HSBC economist expects two more rate cuts in 4Q16 and 1Q17, we think the magnitude of NIM contraction is likely to be limited as the pricing environment is improving post 2015 government-led mortgage reform and banks have begun to raise lending rate spreads. Also, despite ongoing corporate restructuring, we expect the stable credit cost trend to be backed by an improved level of new NPL formation after years of asset clean-up efforts at large commercial banks. However, with a greater focus on RoRWA (Return on Risk-weighted Assets) and tighter lending requirements on mortgages, the pace of loan growth is likely to slow to 4%.

ASEAN banks

Philippine banks, our top pick in ASEAN

Most banks within the five ASEAN markets we cover will likely continue to face a challenging time in 2017. Specifically, banks in Singapore and Malaysia look squeezed as top-line growth prospects remain soft while asset quality continues to weaken. On a brighter note, we expect the protracted asset quality problems in Thailand and Indonesia to peak by end-2016, which means credit cost should at the very least stabilize in 2017. Much depends on the outlook for GDP. In Indonesia's case, we are expecting a pick-up in economic activity premised on greater and more efficient fiscal spending, stronger commodity prices and resilient consumer spending. In Thailand, we expect better fiscal spending and resilient farming and tourist income to support GDP. The Philippines is the only banking sector that is relatively immune to the challenges seen so far. We expect continued strong credit growth, with minimal asset quality risk in the system.

Consumer and retail

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Consumer Staples: Given the high level of uncertainty on the macro front, growth is moderating across various regions. At the same time, competition from on-line and foreign brands is not likely to ease. Consumption is still under pressure and we need to lower expectations as earnings turnaround may be slower than what market expects. Given high level of uncertainty on the macro front, we believe earnings visibility has become more critical for stock performance.

In this context, we like Global Brands (787 HK, Buy), a beneficiary of US consumption recovery story, and Kweichow Moutai (600519 CH, Buy) on the potential earnings upside and expect both stocks to re-rate. We also like beverage company Uni-President (220 HK, Buy) for its margin expansion story.

Consumer Discretionary

We believe competition with e-commerce should continue in 2017. Traditional retailers across different regions lost huge amount of business to on-line competitors. In addition, we expect the sector could be under pressure as this is typically the case when the Fed hikes, on concerns that higher debt payments will curtail spending.

HSBC

Autos

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The domestic market remains the key to profitability for Korean automakers. Sales plunged in 3Q16 as the special consumption tax cut for car purchases ended in late June 2016. We expect domestic sales to remain sluggish through 1H17, which could trigger pricing pressure and margin deterioration for the sector.

Korean automakers have faced increasing challenges from their labour union in recent years. There are often threats of strikes during the annual wage negotiations, which have occasionally disrupted the supply and limited sales of vehicles. We expect Hyundai Group's failure to resolve recurring wage disputes to keep dragging down domestic production levels. This could put pressure on the automaker's inventory levels and the company's ability to meet demand in both the local and export markets.

In December 2015 the government revealed a new five-year "green car" plan for 2016-20. The plan aims to boost production of eco-friendly vehicles to as many as 920,000 units per annum by 2020 from 80,000 as of 2015. Its main goal is to reduce greenhouse gas emissions and generate new growth momentum for the automotive industry. By vehicle type, the country aims to have about 820,000 hybrid electric vehicles, 200,000 electric vehicles (EVs), 50,000 PHEVs and 9,000 fuel-cell electric-vehicles (FCEVs) by 2020. The government will set aside about KRW150bn for assisting R&D of EVs and is also planning to establish nearly 1,400 EV charging stations throughout South Korea by 2020. However, increasing EV related exposure should hurt OEM profitability with lack of economies of scale, in our view.

Healthcare

China pharma

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China's healthcare industry is going through a painful period of rapid change in policy and regulations, which is hurting companies' growth and profitability. The objective is to improve industry standards and control healthcare costs, a long term positive. Key issues to watch in 2017 include the following: (1) All drug tenders are expected to be completed in early 2017; the price of old products will likely decrease and the penetration of new products will likely increase. (2) The National Reimbursement Drug List (NRDL) is likely to be revised in early 2017, which should boost drug usage and volume growth. (3) Consistency evaluation: the deadline for consistency evaluation is end-2018. It will not only delay the launch of drugs in the pipeline but also erode margin due to rising R&D costs. (4) The two-invoice system is likely to be implemented in 10 or more provinces in 2017, which will help drive consolidation in the fragmented pharmaceutical distribution sector. All in all, 2016 and 1H17 should be the low point for China's healthcare industry, and we expect a sustained recovery to follow in 2H17.

India pharma

India pharma has really struggled in 2016. The main issue has been concern about generic drug pricing in the US, with fears around possible penalties because of an ongoing Department of Justice probe. In addition, the market had to digest ongoing delays in generic approvals owing to continuing regulatory woes as well as increasing costs led by R&D. But 2017 could be the year of resolution, when regulatory woes ease as Indian companies come out of an FDA compliance alert. Additionally, while GDUFA I (generic drug user fee act, version 1) comes close to its final year (in a 5-year life period), we believe the FDA will focus on setting the stage for GDUFA II. This might introduce issues such as priority reviews for generics and increased communication between the industry and the FDA to facilitate complex generic approvals. This would augur well for the industry at large, including Indian generics. This is one reason why we expect more approvals in 2017. A last round of consolidation among customers (Wal-Mart and McKesson) could impact market shares and pricing in mid-2017, so this will be something to watch. Locally, Indian demand for pharma should offer some relief with a pick-up in volumes and the softening impact of increasing local price controls and other local regulatory changes.

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Industrials (Infrastructure)

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In Korea, revenue growth for the construction companies remains weak. Overseas new orders – often from the petrochem industry – will continue to slow down in a low oil price environment. We expect new orders from the petrochem industry will not materialize unless the oil price remains sustainably above USD 80/barrel. Meanwhile, Korean construction companies have seen a shift in their order book since shipbuilders and E&Cs have not won new orders for the past three years. One advantage of this is that we do not expect any big losses from the existing order backlog, as the quality of the order book has improved.

Insurance

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Korean non-life insurers' loss ratios will continue to improve in both auto and long-term, on the back of price hikes and re-pricing. While the pace of auto loss ratio improvement is expected to slow from c8ppt in 2016e, our re-pricing cycle analysis suggests that the risk loss ratio is likely to turn from 2017 with the accumulating re-pricing effect.

As for the life insurers, the operating environment is likely to remain challenging with a continued low interest rate environment. We expect their negative spreads to widen given a large portion of fixed-rate reserves and also due to the crediting rate hitting the minimum guarantees for floating-rate policies. We continue to prefer non-life insurers over life insurers given better earnings visibility and because they are less sensitive to interest rates.

Internet

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China

We see three key trends in China Internet in 2017. First, we expect subscription-based media to raise the value of intellectual property for entertainment content. For example, companies such as Baidu and Tencent will put their most popular video and music content behind the pay wall, and users will increasingly pay a monthly subscription for exclusive content. Second, we expect companies and organizations to focus on mining and monetizing their data assets. For example, Baidu will generate material revenue from its AI-driven news feed, which delivers personalized content to users based on their search history. Companies will increase the adoption of cloud services to understand and optimize their data, benefiting Alibaba – *an HSBC Asia Super Ten portfolio stock* – which already operates the biggest commercial cloud business in China. Third, we believe potential IPOs of large Internet businesses in e-finance and O2O next year could serve as catalysts for the sector, enhancing visibility and potentially driving industry consolidation.

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Real Estate

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China

Chinese developers are well positioned to weather market uncertainty. Developers have had an impressive year from an operational standpoint in 2016. With an average contracted sales run rate of 72% and 74% y-o-y growth in 9M16, developers are well on track to completing their contracted sales targets while some have already exceeded their target. With the latest round of policy tightening measures announced in October, targeting regions with low inventory and high growth in average selling prices (ASPs), the outlook for next year will be more uncertain. However, we remain convinced that developers' current state of operations is much stronger than the previous cycle in 2011 amid strong sales performance and an accommodative credit environment. We note that in the previous cycle, developers' cash flows were under pressure amid shrinkage in corporate lending, a prolonged lag in mortgage disbursements and lacklustre sales performances. The key question is how well physical market demand will hold up next year, but the market is unlikely to gain much clarity of this until 2Q17.

Hong Kong

Hong Kong property sees renewed expectations of policy risks

There are renewed expectations of policy risks. Hong Kong primary sales momentum has continued to strengthen, underlined by the recent successes in primary launches which generated strong sell-through rates. We expect price growth to remain positive in the near term but highlight that the key downside risks will to be driven by the macro side. These include potential policy risk if property prices continue to grow at a rapid pace, leading to further deterioration in housing affordability. Renewed expectation for rate hikes is also a key factor that may affect property market sentiment.

Resources and Energy

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Oil

Key drivers for global oil markets in 2017 are likely to include: a gradual recovery of upstream profitability as crude oil markets naturally rebalance, a renewed focus on OPEC decision-making and output which will require close monitoring of monthly output figures, and a more thorough assessment of corporate resources, cash flows and operating profitability as we exit the trough.

Natural gas

Given our rising crude oil price deck in 2017-18, we expect natural gas should follow crude higher. During 2016, both piped natural gas (PNG) and liquefied natural gas (LNG) prices followed oil prices lower. On the way back up, gas prices are likely to have a wider pricing gap to reflect the relative oversupply of LNG in the global market along with the normal formula related time lag. This wider pricing gap has the potential to create room for imported natural gas to increase penetration in key markets, including China, Thailand and India, and benefit gas importers, transporters and end users.

In China, volume growth and price reforms are being introduced to encourage market pricing. Over the past year, the Chinese gas market benefited from falling natural gas prices and strong policy support. We expect the positive volume trends to continue and potentially accelerate in 2017. According to the 13th Five-year Plan, the share of natural gas in primary energy consumption mix will increase from c6% in 2015 to 10% in 2020, suggesting compound annual growth of more than 10% pa. A more efficient pricing system is required to lower gas consumption cost and stimulate end-user demand. The Chinese government has initiated the long-haul pipeline tariff reform in 2016. Further consolidation of the reform will be crucial to the marketization of gas prices. With the new regulation becoming effective in 2017, we will closely monitor (1) disclosure of detailed operating costs of pipelines, (2) the pricing of the pipeline tariff based on an 8% IRR, and (3) the involvement of third-parties in the pipeline transmission.

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Refining

We estimate the regional benchmark refining margin will remain at USD7-8/b on average in 2017 versus a 10yr average of USD6/b. The realised margin, considering lower utility costs, transportation cost, and feedstock discounts, should be higher than the benchmark refining margin and thus the profitability for the sector will be maintained at peak cycle level.

For downstream business, we believe refinery runs will continue to grow on the back of lucrative margins and rapid development of teapots. However, moderate economic growth points to the fact that the domestic market may be getting saturated. Therefore, oversupply of refined products will continue to be the case in 2017. We foresee more exports of refined products.

We believe the refining sector will still be the bright spot on the back of limited capacity additions vs. relatively benign demand growth, especially in the transportation sector. The crude price discount supports the Asian refining margin as excess supply in the upstream crude oil market, especially in the Middle East region, allows Asian refiners to purchase feedstock at a favourable price. In contrast, US refiners cut operating rates after losing feedstock cost advantages as domestic crude oil production declined. This, in turn, creates much more room for Asian refiners in the export markets.

Chemicals

We expect Chinese coal prices, which have remained elevated through 2016, to decline in 2017 for supply reasons. Higher coal prices in China primarily impact three chemicals products: PVC, methanol and urea. In these three chains, c34% of global capacity is based on Chinese coal, and higher prices for coal impact absolute production costs in China as well as relative competitiveness. Of the three, we see the biggest impact on PVC.

We expect supply growth to overwhelm demand growth in 2018-19e. Our cycle view remains unchanged: spreads are likely at peak levels and as new supply comes on stream they should decline. Our model has the peak of supply additions weighted in 2018e, so spread remains strong in 2017e. However, as 2018 approaches and the wave of supply becomes visible, equities will likely start to discount new supply.

Resources

Chinese coal: The coal industry remains in the sights of the policymakers. It has been the subject of much attention in 2016 after forced production closures created market shortages. Chinese coal prices have been rallying on the shortages. Although the government is now encouraging production to boost spot supply heading into winter, we do not see an imminent supply response. We believe prices will remain high in 2016 and it could be 2017 before there is any meaningful correction.

Constructive on the Indian steel and zinc

India Steel: We are a lot more constructive on the Indian steel space, following the decision by the Indian government to impose anti-dumping duty on steel originating from China. In addition, a similar measure by the EC will also open up new markets for the Indian steel companies. We have a Buy rating on Tata Steel and JSW Steel.

India non-ferrous sector: We are more constructive on zinc than aluminium, given our expectations of a rising deficit in zinc and our fears of rising production in aluminium. We have a Buy rating on Hindustan Zinc, the second largest zinc miner in the world. We have a Buy rating on Hindalco despite our views on primary aluminium as we are optimistic on HNDL’s downstream business.

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Technology

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Memory and flexible OLED

Memory: We are bullish on the memory sector, and we think the memory upcycle will be extended to 2017e, for three main reasons: (1) the DRAM capex decline will continue by 22% in 2017e after an 11% decline in 2016e; (2) intensifying supply constraints due to a longer tech migration period and declining cell efficiency (potential structure change in DRAM bit composition) curbing annual bit growth; and (3) surging 3D NAND demand due to extending applications to solid state disks (SSD), smartphones and flash cards, to absorb memory capex. We think such robust demand will consume fast-growing 3D NAND capacity while commercialization of 3D NAND at non-Samsung players may be further delayed. We forecast the DRAM market to grow 11% in 2017e, to USD45bn, and the NAND market to expand 10% in 2017e, to USD35bn, with the overall memory market reaching USD79bn in 2017e – 11% y-o-y growth. We think Korean dominance in the memory industry will continue, especially in the DRAM segment, given a high technology barrier of entry for newcomers. We think Samsung and Hynix will maintain near 80% global DRAM market share for the next two years.

Flexible OLED: We are bullish on the OLED sector in 2017e as we think the mega trend of LCD to OLED transition will accelerate in 2017e; we expect OLED adoption ratio for smartphones to reach 34% by 2017e from 13% in 2015. We attribute this to 1) Apple's adoption of OLED display in its new iPhone in 2H17 for the first time, (2) faster OLED adoption at Samsung smartphone to 80% of the total by 2017e from 40% in 2015, and (3) stronger China smartphone shipments and aggressive OLED adoption. As price parity between rigid OLED and LCD has occurred from 2Q16, the OLED transition has been accelerating in the smartphone industry. Samsung will keep its dominance, with above 95% market share, given aggressive capacity ramp-up and technology readiness. However, LGD will also benefit as it will start meaningful commercialization of flexible OLED from 2Q17. We think Samsung outputs will be tied up with Samsung and Apple, and LGD will get overflow orders from Chinese and other smartphone makers, leading to market share gain. In the meantime, we think mass production of Chinese and Japanese players will start from late 2018 or 2019e at earliest. Therefore, dominance by Korea makers will continue.

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EV and Batteries

We see clear signs of long-term growth prospects for electric vehicles (EVs): (1) The mass EV market should start in 2017e. Vehicles with driving range of 400km on a single charge with a price tag of USD35,000 will come to the market. (2) Current EV models are already competitive vs. internal combustion engines even at very low oil prices (the rising fuel price is a tailwind). Lastly, (3) EV penetration is rising in the US and even Germany, an iconic country for the internal combustion engine, has passed a resolution, albeit a non-binding one, calling for a ban on internal combustion engines by 2030.

We expect global PHEV/BEV sales to show a robust CAGR of 30% from 2015 to 2025, with penetration reaching 7.8% (8.1m units) in 2025, up from 0.7% (591,000 units) in 2015. This is likely to be supported by EV market growth in China and a sharp fall in battery prices amid stricter regulations on fuel efficiency and greenhouse gas emissions globally. As the market for electrical vehicles expands, we expect EV battery demand to grow at a 29% CAGR, from 15GWh in 2015 to 193GWh in 2025.

Tech hardware, industrial PC and Automation

For the global PC market, we are seeing incremental positive data points to support a stabilization of the market in 2017. As such, HSBC's global PC shipment forecast reflects a flat 2017 on y-o-y basis, versus -6% expected for 2016 and -10% in 2015. The positive catalysts include better sales on gaming, 2-in-1 convertible and chromebook PC. All of these account for

20-25% of the total PC market and are growing relatively faster owing to consumer interest. In addition, the commercial market is also seeing better demand after Microsoft announced that the introduction of the next generation of Windows would be delayed. This helps to drive the replacement cycle as corporates no longer need to worry about the transition to different generations of operating systems.

We are believe that the recent cost hike on key components, including panel and memory, should be a near-term wildcard for demand. In general PC OEMs have low profitability, so it is difficult to absorb additional costs and they need to pass through the higher cost to consumers. This might negatively impact end-demand in 4Q16-1Q17, implying that market stabilization is unlikely to be achieved until 2H17. Given that the sector will remain a mixed bag in the near-term, we do not have any Buy ideas in the PC sector for now.

A structural theme to watch is the Industrial IoT Internet of Things (IIoT). The IIoT is the application of the IoT to the manufacturing industry, particularly industrial automation, via devices connected by communications software. In 2017, the commercial availability of new LPWA (low-power wide area) networks could facilitate better data communication, which will make IIoT adoption easier. This should benefit industrial PC and automation companies under our coverage, including Advantech, Ennoconn, Airtac and Delta.

Telecom and Media

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Asia Telecom

Regulation and policy remains the most important driver of Asia telecom stocks, in our view. In many markets, the large sums required to create a high-quality data network effectively creates a natural monopoly. This has resulted in asset consolidation in China (in China Tower), and we see increased risk of regulatory intervention in Indonesia (where PT Telkom has a strong position in the regions). In Australia, the regulator is considering whether to declare national roaming, while in the Philippines the government may invest in infrastructure to speed network rollout.

In markets such as Korea and Japan, the investments to support data are largely complete, price is limiting usage, and networks are at parity. Here we have strong visibility on capex and free cash flows – the question then becomes whether these operators can successfully invest for growth. We see strong demand for data services in Indonesia and the Philippines, but a high degree of uncertainty as to how governments and operators can work together to improve network coverage. In Thailand we believe competition and high spectrum costs will restrict the growth outlook for its telecom sector.

We are neutral to optimistic across our coverage universe.

- Key Buy-rated stocks include those where we see a recovery in earnings, such as China Unicom, KT Corp and NTT DoCoMo. We have Buy ratings on NTT and PCCW due to what we see as the 'option-value' on their Global Cloud business and 'Over The Top' content capability respectively. In Taiwan, we look for a shift to tiered data pricing, and see Far EasTone as the best placed to benefit from this as the company is most exposed to an improvement in the wireless business. We like the fundamental outlook in the Philippines and Indonesia, but see risks of asymmetric regulation for PT Telkom in Indonesia, underpinning our preference for XL Axiata and IndoSat. In the Philippines we prefer PLDT, which we believe has greater surplus capacity and more potential to catch up in data. In Singapore we like SingTel on valuation and benefits from NetLink Trust.

- We have a Reduce rating on Idea. We believe Idea Cellular may lose market share in the medium term. The key concern is the ability of the company to fund medium-term capex and spectrum acquisitions.

China Media

In 2017, we expect box office revenue to recover and live broadcasting to maintain strong momentum. China's total box office revenue growth has slowed from 50% in 2015 to 6-8% y-o-y in 2016 y-t-d. The main reasons for the deceleration are (1) lack of box office blockbusters, (2) lower film ticket subsidies from the online ticket distributors, and (3) stricter censorship and monitoring of box office statistics. We believe the worst is behind us and see low risk of further deceleration. We remain optimistic on the long term growth potential and expect box office revenue to resume strong growth in 2017. In addition, the live broadcasting sector should continue to grow rapidly. A growing portion of Internet users are viewing live broadcasts for entertainment purposes and social features. Market leaders are accelerating monetization and should be able to help drive industry consolidation. We expect live broadcasting sector revenue to achieve 65% growth in 2017.

Transport

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2016 was an interesting year featuring many diverging sector themes. Currency volatility, the oil price collapse and rally, Brexit and bankruptcies dominated, while there was no clear improvement in underlying fundamentals. There is a general sense of caution going into 2017, with little visibility of an economic or trade recovery and noise about protectionism increasing.

Asia marine and logistics

The shipping sector continues to battle with persistent overcapacity and the outlook is unlikely to change in 2017. Following Hanjin Shipping's bankruptcy, themes such as consolidation and further bankruptcies should dominate the space. Barring a few niche players like SITC, we expect the sector to continue to report losses in 2017. For ports sector, investor focus should shift to pockets of growth and structural themes unaffected by sluggish trade growth, such as India ports. In China, the preference should move towards stable yield amid slower growth. Logistics is expected to remain an area of interest, with the recent listing of ZTO Express, one of China's largest express courier companies.

Asia aviation

The outlook is challenging for premium airlines in the region

Chinese airlines with large market shares in top tier cities will continue to do relatively well. However, we think there is overcapacity in many international markets and the competition with global peers is intensifying. ROE could trend slightly lower given the headwinds in lower tier cities and the international market, but it remains at relatively attractive levels of around 10%. The major risk is forex losses from RMB depreciation and the slowdown in outbound travel. Among premium regional airlines in Asia, the outlook is more challenging. The aggressive capacity injection by Chinese and Gulf airlines will pressure yields and traffic volumes in the long haul markets. In addition, premium demand is expected to remain weak amid global macro weakness. Meanwhile, major Chinese airports should show steady profit growth now that major operating expenses appear to be under control.

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Utilities

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China

China IPPs' earnings will continue to contract due to poor fundamentals, including overcapacity, an unfavourable demand trend and unfriendly regulations. We believe the sector deserves a PB of less than 1.0x in the current down cycle, with ROE contracting. Nuclear IPPs have downside risks on utilisation as they will need to share the burden from slower power demand growth. Additional risks come from a discount in tariffs due to the market trading of power.

China wind operators are expected to have better utilisation, the guaranteed utilisation hour policy announced in May 2016. Proposed cuts in tariffs from 2018 will have only a minimal impact on earnings. Therefore wind farms should be able to deliver more than 12% equity IRR. We believe the sector deserves a 1.4x PB and the recovery in valuation should continue.

China solar companies have potential downside from a deep tariff cut recently proposed by the government. Another round of investment has already been triggered to avoid such cuts, which will benefit the upstream solar products segment and offset the downside from the solar farms. We think market potential remains intact as SOEs continue to invest to meet their energy mix target for 2020.

China downstream gas distributors are facing an uncertain regulatory outlook, with downside risks from caps on retail gas prices and lower dollar margins, and upside risks from lower gas transmission costs in midstream and upstream.

China environmental: The 13th FYP guided a 17% and 23% 2015-20 CAGR for waste to energy (WTE) and biomass capacities. Momentum has been building thanks to the aggressive approval of PPP projects in the environmental sector. Potential cuts in WTE power tariffs could be compensated for by higher waste processing fees.

Hong Kong

Hong Kong utilities still look attractive for their defensive qualities, with possible upsides from M&A and organic growth. Regulatory uncertainty in Hong Kong remains but we believe this has already been priced in. CKI's overseas assets offer high earnings visibility, despite the negative impact from a weaker GBP. We also like PAH for its net cash, which is a cushion against an interest rate hike, and increases the likelihood of a special dividend.

Korea

Power demand growth was steady in 1H16, with an improving power mix. We have a Buy rating on Kepco (*a constituent of the HSBC Asia Super Ten and GEMs Super 15 portfolios*) as we believe that concerns over tariff adjustments and a fuel price hike seem priced in; valuation downside also appears limited. The government's intention to list Kepco's power generating subsidiaries and privatise the retail market will increase transparency in Korea's power and tariff system. But such reforms will need more time to be rolled out.

ASEAN

In the Philippines, the Energy Regulatory Council will likely to cut the power tariff from July 2017. Ongoing liberalisation of the retail market is likely to increase competition between power companies (distributors and generators). In Malaysia, power demand growth has been supported by GDP improvement and hot weather, despite weak industrial demand. We like Tenaga, as regulation has formalised the fuel cost pass-through, which has improved earnings visibility.

HSBC

Valuation and risks

List of stocks with analyst details

Stock code	Company	Mcap (USDm)	HSBC rating	HSBC target price	2 Dec closing price	Upside/ downside	HSBC analyst*	Analyst details
2395 TT	Advantech	5,026	Buy	TWD306	TWD253.5	21%	Lai, Jenny	jennylai@hsbc.com.tw, +8862 6631 2860
1590 TT	Airtac	1,341	Buy	TWD327	TWD239	37%	Lai, Jenny	jennylai@hsbc.com.tw, +8862 6631 2860
BABA US	Alibaba Group**	219,882	Buy	USD120	USD90.48	33%	Tsang, Chi	chitsang@hsbc.com.hk, +852 2822 2590
BIDU US	Baidu Inc	56,814	Buy	USD216	USD161.67	34%	Tsang, Chi	chitsang@hsbc.com.hk, +852 2822 2590
002179 CH	China Aviation Optical	3,236	Buy	CNY52.9	CNY36.99	43%	Li, Emily	emily.c.li@hsbc.com.hk, +852 29966599
762 HK	China Unicom	29,330	Buy	HKD12	HKD9.5	26%	Anderson, Neale	neale.anderson@hsbc.com.hk, +852 2996 6716
1038 HK	CKI	22,094	Buy	HKD78	HKD64.65	21%	Li, Evan	evan.m.h.li@hsbc.com.hk, +852 2996 6619
317 HK	COMEC	911	Buy	HKD33.2	HKD11.94	178%	Li, Emily	emily.c.li@hsbc.com.hk, +852 29966599
601989 CH	CSICL	19,835	Reduce	CNY5.4	CNY7.44	-27%	Li, Emily	emily.c.li@hsbc.com.hk, +852 29966599
2308 TT	Delta	12,739	Buy	TWD193	TWD156.5	23%	Lai, Jenny	jennylai@hsbc.com.tw, +8862 6631 2860
8069 TT	E Ink Holdings	790	Buy	TWD25.5	TWD22.1	15%	Tsai, Jerry	jerrycytsai@hsbc.com.tw, +8862 6631 2863
300251 CH	Enlight Media	4,749	Buy	CNY14	CNY11.15	26%	Liu, John	john.q.liu@hsbc.com.hk, +852 2822 4392
6414 TT	Ennocon	1,048	Buy	TWD575	TWD439	31%	Lai, Jenny	jennylai@hsbc.com.tw, +8862 6631 2860
4904 TT	Far Eastone	7,485	Buy	TWD90	TWD73.3	23%	Anderson, Neale	neale.anderson@hsbc.com.hk, +852 2996 6716
002465 CH	Haige Communication	3,701	Buy	CNY19.7	CNY11.88	66%	Li, Emily	emily.c.li@hsbc.com.hk, +852 29966599
012450 KS	Hanwha Techwin	1,932	Buy	KRW67000	KRW42650	57%	Seo, Ricky	rickyjuilseo@kr.hsbc.com, +822 37068777
HDFC IN	HDFC	28,801	Buy	INR1512	INR1236.8	22%	Sheth, Sachin	sachinsheth@hsbc.co.in, +91 22 2268 1224
HDFCB IN	HDFC Bank**	44,610	Buy	INR1632	INR1189.1	37%	Sheth, Sachin	sachinsheth@hsbc.co.in, +91 22 2268 1224
002415 CH	Hikvision	22,302	Buy	CNY32.2	CNY25.17	28%	Li, Emily	emily.c.li@hsbc.com.hk, +852 29966599
HNDL IN	Hindalco	5,123	Buy	INR200	INR168.75	19%	Mistry, Jigar	jigarmistry@hsbc.co.in, +91 22 22681079
HZ IN	Hindustan Zinc	16,923	Buy	INR290	INR272.55	6%	Mistry, Jigar	jigarmistry@hsbc.co.in, +91 22 22681079
IDEA IN	Idea	3,887	Reduce	INR62	INR73.45	-16%	Sharma, Rajiv	rajivsharma@hsbc.co.in, +91 22 22681239
1970 HK	IMAX China	1,747	Hold	HKD40	HKD38	5%	Liu, John	john.q.liu@hsbc.com.hk, +852 2822 4392
ISAT IJ	IndoSat	2,532	Buy	IDR7800	IDR6300	24%	Anderson, Neale	neale.anderson@hsbc.com.hk, +852 2996 6716
JSTL IN	JSW Steel	5,884	Buy	INR2090	INR1656.65	26%	Mistry, Jigar	jigarmistry@hsbc.co.in, +91 22 22681079
015760 KS	Kepco***	23,787	Buy	KRW67000	KRW43450	54%	Lee, Yeonjung	yeonlee@kr.hsbc.com, +822 3706 8778
030200 KS	KT Corp	6,580	Buy	KRW45000	KRW29550	52%	Anderson, Neale	neale.anderson@hsbc.com.hk, +852 2996 6716
3008 TT	Largan Precision**	15,175	Buy	TWD4473	TWD3610	24%	Lu, Bruce	bruce.kl.lu@hsbc.com.tw, +886 2 66312861
LT IN	Larsen & Toubro	18,665	Buy	INR1723	INR1361.85	27%	Narkar, Ashutosh	ashutoshnarkar@hsbc.co.in, +91 22 22681474
051910 KS	LG Chem	13,083	Buy	KRW320000	KRW231500	38%	Yoo, Dennis	dennishcyoo@hsbc.com.hk, +852 2996 6917
034220 KS	LG Display	17,008	Buy	KRW35100	KRW27900	26%	Tsai, Jerry	jerrycytsai@hsbc.com.tw, +8862 6631 2863
NTES US	NetEase Inc.	28,644	Buy	USD266	USD220.59	21%	Tsang, Chi	chitsang@hsbc.com.hk, +852 2822 2590
9437 JP	NTT DoCOMo	90,329	Buy	JPY3500	JPY2597	35%	Anderson, Neale	neale.anderson@hsbc.com.hk, +852 2996 6716
6 HK	PAH	19,729	Buy	HKD90	HKD71.7	26%	Li, Evan	evan.m.h.li@hsbc.com.hk, +852 2996 6619
8 HK	PCCW	4,459	Buy	HKD6.3	HKD4.48	41%	Anderson, Neale	neale.anderson@hsbc.com.hk, +852 2996 6716
TEL PM	PLDT	5,531	Buy	PHP2200	PHP1270	73%	Anderson, Neale	neale.anderson@hsbc.com.hk, +852 2996 6716
TLKM IJ	PT Telekom	29,145	Hold	IDR4600	IDR3910	18%	Anderson, Neale	neale.anderson@hsbc.com.hk, +852 2996 6716
005930 KS	Samsung Electronics	207,184	Buy	KRW2150000	KRW1727000	24%	Seo, Ricky	rickyjuilseo@kr.hsbc.com, +822 37068777
000089 CH	Shenzhen Airport	2,674	Hold	CNY9.5	CNY8.98	6%	Xu, Jack	jack.y.xu@hsbc.com.hk, +852 2996 6566
300124 CH	Shenzhen Inovance	4,867	Buy	CNY24	CNY20.9	15%	Chow, Anderson	andersonchow@hsbc.com.hk, +852 2996 6669
6826 HK	SHi Haohai Biotech	768	Buy	HKD50	HKD37.1	35%	Zhao, Zhijie	zhijie.zhao@hsbc.com.hk, +852 2996 6591
ST SP	SingTel	43,193	Buy	SGD4.853448	SGD3.76	29%	Choudhary, Piyush	piyush.choudhary@hsbc.com.sg, +65 6658 0607
1308 HK	SITC	1,584	Buy	HKD5.4	HKD4.7	15%	Jain, Parash	parashjain@hsbc.com.hk, +852 2996 6717
000660 KS	Sk Hynix	27,564	Buy	KRW58000	KRW44400	31%	Seo, Ricky	rickyjuilseo@kr.hsbc.com, +822 37068777
TATA IN	Tata Steel	5,800	Buy	INR500	INR406.4	23%	Mistry, Jigar	jigarmistry@hsbc.co.in, +91 22 22681079
TECHM IN	Tech Mahindra	6,768	Buy	INR510	INR473.4	8%	Aggarwal, Yogesh	yogeshaggarwal@hsbc.co.in, +9122 2268 1246
TNB MK	Tenaga Nasional	17,783	Buy	MYR17.8	MYR14.04	27%	Bhatnagar, Tarun	tarunbhatnagar@hsbc.co.in, +65 66580614
700 HK	Tencent Holdings	233,367	Buy	HKD245	HKD191	28%	Tsang, Chi	chitsang@hsbc.com.hk, +852 2822 2590
002739 CH	Wanda Cinema Line	11,224	Buy	CNY85	CNY65.83	29%	Liu, John	john.q.liu@hsbc.com.hk, +852 2822 4392
300017 CH	Wangsu Sci & Tech**	6,675	Buy	CNY89	CNY57.95	54%	Liu, John	john.q.liu@hsbc.com.hk, +852 2822 4392
000858 CH	Wuliangye Yibin	19,703	Buy	CNY41	CNY35.75	15%	Leung, Christopher	christopher.k.leung@hsbc.com.hk, +852 29966531
EXCL IJ	XL Axiata	1,786	Buy	IDR3200	IDR2260	42%	Anderson, Neale	neale.anderson@hsbc.com.hk, +852 2996 6716
600519 CH	Kweichow Moutai	58,688	Buy	CNY380	CNY321.77	18%	Leung, Christopher	christopher.k.leung@hsbc.com.hk, +852 29966531
220 HK	Uni-President	3,035	Buy	HKD6.4	HKD5.45	17%	Leung, Christopher	christopher.k.leung@hsbc.com.hk, +852 29966531
007070 KS	GS Retail	3,116	Buy	KRW77000	KRW47450	62%	Choi, Karen	karen.choi@kr.hsbc.com, +822 3706 8781
787 HK	Global Brands	1,350	Buy	HKD1.5	HKD1.23	22%	Leung, Christopher	christopher.k.leung@hsbc.com.hk, +852 29966531

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**An HSBC Asia Super Ten portfolio stock*
***A constituent of the HSBC Asia Super Ten and GEMs Super 15 portfolios*
Source: HSBC estimates

Valuation and risks

Code	Company	Valuation methodology	Risks to our view
2395 TT	Advantech	Our target price of TWD306 is based on 28.4x 2017e EPS (the historical PEG has been 1.87x since 2014).	Downside risks: Local currency volatility such as continued EUR depreciation, which could result in lower margins, unless the company raises prices. The company's component costs are mainly in USD, so USD appreciation will have a negative impact on profitability. Other risks include a slowdown in regional demand.
1590 TT	Airtac	Our TP is based on a PE multiple of 24.3x (average forward PE over 2Q13-2Q14, the last period of the company's rapid expansion of margin) applied to 2017 estimates.	Downside risks: The biggest uncertainty we see in the share is the RMB depreciation which might result in more foreign exchange losses.
BABA US	Alibaba Group	We use a sum-of-the-parts approach to value Alibaba, which yields a target price of USD120, consisting of USD101 per share for Alibaba Group, based on a DCF approach with a WACC of 10.1% (consisting of an equity risk premium of 6%, a risk-free rate of 2.5%, and a beta of 1.498), USD8 per share for its entitlement to a 33% stake in Ant Financial, USD9 per share for its investment portfolio at book value, and USD3 per share in net cash as of end-March 2017e. *Alibaba is an HSBC Asia Super Ten portfolio stock.*	Key downside risks include worse-than-expected mobile monetization or lower margins.
BIDU US	Baidu Inc	Our target price is derived by applying a 1 PEG to our 2017e EPS and 2017-20e EPS CAGR of 27%.	The key downside risks to our rating are the speed to review its advertisers and its impact on earnings, worse-than-expected technology change, execution and competition.
002179 CH	China Aviation Optical	We have a Buy rating and DCF-based TP of RMB52.9. Our key assumptions are: a WACC of 7.5%, a RFR of 2.5%, which is in line with HSBC equity strategy team's latest assumption, a terminal growth of 2.5%, and an equity beta of 1.14 based on Bloomberg.	Key downside risks: Decreasing profit margins of electronic connectors, elimination of support policies for EVs.
762 HK	China Unicom	We use a DCF-based sum of-the-parts model to capture China Unicom's stake in China Tower based on DCF. We apply a 15% holdco discount to the fair value of the stake. We apply a cost of equity of 8.5%, cost of debt of 5% and a debt-to-capital ratio of 40% which results in a WACC of 6.6%. We apply a terminal growth rate of 1%.	Key downside risks include: more competition which results in slower revenue growth, more inelastic data demand, higher-than-expected marketing and network costs which creates margin pressures and slower-than-expected pickup in bundling rate.
1038 HK	CKI	Our TP of HKD78 is based on a DCF valuation, using a risk-free rate of 2.5%, cost of equity of 5.5% and an equity beta of 0.6.	Downside risks: Weakening GBP and AUD, which could erode income from overseas business; worse-than-expected outcome to the next tariff resets for businesses in Australia; rate hikes by the US Fed; and inability to strike meaningful acquisitions.
317 HK	COMEC	We use a sum-of-the-parts methodology to derive our target price of HKD33.20. We estimate a 30% annual growth rate in the defence-related sector based on China's defence budget growth rate and higher allocation to advanced military equipment. We assign a 1.0x PEG to COMEC, equal to a PE ratio of 30x (applied to our 2016e estimates). Other business (including civilian shipbuilding & maintenance, mechanical & electrical products and engineering): we value the other business using a 1.3x PB based on the past one-year historical performance.	Weaker-than-expected asset injections; we assume high-quality assets, such as Jiangnan and Hudong Zhonghua, will be injected into COMEC; if the injection process is delayed, the company may underperform; we assume the civil shipbuilding business will stage a moderate recovery in the medium term; if it is weaker than our assumption, it may hurt the core business.
601989 CH	CSICL	We derive our target price of RMB5.40 based on a sum of-the-parts approach. We value the national defence-related segment based on PE as we expect this business to experience stable sales momentum. We anticipate a 30% annual growth rate in the defence related sector based on China's defence budget growth rate and higher allocation to advanced military equipment, the PEG ratio would reach 1.0x, representing a PE ratio of 30x on our 2016e estimates. Other businesses (including civilian shipbuilding and equipment, energy and transportation equipment, ocean engineering): we use PB to value the other part of the business. Historically, the average PB for this business has been stable at 1.0x, without taking asset injections into consideration.	Key upside risks: We expect SOE reform to bring many benefits; if improvements, such as management incentive schemes and better pricing methods are implemented ahead of schedule, we think CSICL's stock price could be lifted; more inflow of military orders than expected; and a strong recovery of the civilian shipbuilding segment.
2308 TT	Delta	We base our fair value target price of TWD193 on a target PE multiple of 20.1x mid-cycle PE applied to 2017e earnings of TWD9.58. Our mid-cycle PE represents the average PE since mid-2013.	Downside risks: competitive pressures in legacy power products due to sluggish demand as well as increased investment leading to higher operating expenses; macro uncertainties, which could potentially impact global spending on industrial automation.
8069 TT	E Ink Holdings	We see fair value at 1.0x FY17e BVPS of TWD25.54, which gives us a fair-value target price of TWD25.5. 1.0x PB is the high end of the range for E Ink since 2013, which marks the year that non-reader and licensing fee income replace the e-reader as the main earnings catalysts. We believe the company could continue to surprise on OP from increasing scale, better product mix, and potential OPEX improvement of LCD shutdowns in 2017.	The main downside risks are weaker-than-expected eReader and smartphone demand, and a more severe decline in licensing fee income.
300251 CH	Enlight Media	We derive our target price using a DCF methodology. We apply 2.5% risk free rate, 6.0% market risk premium, 1.16 beta and 5% cost of debt to derive a WACC of 8.0%. Our target price implies a 42x 2017e PE.	Downside risks: (1) worse-than-expected box office performance of key films and (2) lower-than-expected margins in 2016e and 2017e, due to rising production costs.
6414 TT	Ennoconn	We base our target price on a forward multiple of 25.5x on 2017e earnings. Advantech's historical average PE (2012 to current) is 21.4x, and one standard deviation above the historical mean is 26.2x. We use the one standard deviation above average as our benchmark but make a slight discount considering Ennoconn's smaller market share.	Key downside risks: Short-term challenges in integrating Casewell business into Ennoconn's platform and rising competition for networking security products.

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Valuation and risks

Code	Company	Valuation methodology	Risks to our view
4904 TT	Far Eastone	We use DCF to evaluation the company. We apply an equity beta assumption of 0.6, a risk-free rate of 3% and an equity risk premium of 6%. This returns a cost of equity of 7.5%. Our WACC estimate for Far EasTone is 7.5%. We apply a 0% terminal growth rate for the company.	Key downside risks include: a rotation out of yield stocks due to interest rate increases; further price competition; and higher competition in the spectrum auction expected in 2H17.
002465 CH	Haige Communication	We have a Buy rating and DCF-based target price of RMB19.7 on the stock. Our key assumptions are a WACC of 7.3%, a RFR of 2.5% (per HSBC's strategists), and a COE of 8.5%. We rate the stock Buy.	Key downside risks include slower-than-expected production of satellite equipment, poor M&A execution, and the withdrawal of government subsidies.
012450 KS	Hanwha Techwin	Our target price is based on a target PE of 22.0x – the 10-year average PE multiple of competing defence companies. We apply this multiple to 2H16e-1H17e earnings	Key downside risks: (1) higher-than-expected restructuring costs, (2) delays in developing a schedule for new business areas, (3) a delayed materialisation of synergy effect from the Doosan DST acquisition after the physical merger, and (4) lower-than-expected spending by the Korea government in defence budget due to expansion of government deficit.
HDFC IN	HDFC	Our target multiple of 3.6x book and target price of INR1,512. We believe the company's record of maintaining stable margins and asset quality make it a defensive oasis, especially during volatile periods.	Downside risks: (1) competitive pressures, which could slow business growth or impact margins, and (2) asset quality risks.
HDFCB IN	HDFC Bank	HDFC Bank is valued using single stage Gordon growth model based on a weighted average ROE of 18.1% and growth rate of 9.5%. Cost of equity of 9.0%, giving us HSBC cost of equity of 11.5% leading to a justified P/AB multiple of 4.4x. Our fair value target price of INR1,632 has been derived discounting back our 1-yr forward stock value which is obtained by multiplying the Gordon Growth based P/ABV with the rolled forward 12 months forward ABV. *HDFC Bank is an HSBC Asia Super Ten portfolio stock.*	Key risks include (1) slower-than-expected loan growth and (2) worse-than-expected asset quality.
002415 CH	Hikvision	DCF methodology was used to derive the target price, applying a WACC of 6.9%, a RFR of 2.5%, an equity risk premium of 6.0%, target gearing ratio of 25%, a beta of 1.0 based on Bloomberg, and a terminal growth rate of 2.0%.	Key downside risks: (1) If the company's R&D lags behind that of peers and products fail to meet customer needs, it could hurt sales and the share price. (2) If overseas sales decline due to intense competition and the exchange rate is detrimental to the company, sales could be lower than we expect. (3) Poor execution on new business from upcoming M&A activity could hurt the stock's performance. Lastly, in the short term, (4) if local governments cut their security expenditure, it could hurt the share price.
HNDL IN	Hindalco	We value HNDL on a FY18e EV/EBITDA-based sum-of-the parts approach, with multiples of 5.5x for the standalone and 6.0x for Novelis, and discount the valuation base to 2018e based on our assumption of cost of equity. We include a value from HNDL's investments in various group companies at a 20% discount to their respective market values on a conservative basis. The valuation of NVL forms c63% of consolidated Enterprise Value of HNDL in our sum of-the-parts target price. Novelis's increasing share of sales to the higher margin Automotive sector and low cost operations for Hindalco, which should help maintain margins for the standalone business	Downside risks: Lower-than-expected aluminium prices and Copper TC/RCs form key risks. While we expect Novelis' performance to improve, the overhang of exposure to developed markets remains and prolonged macro weakness in these markets could hurt shipments and earnings. Also, NVL's auto sheets segment is leveraged to the focus on tightening of fuel efficiency and emission norms and hence policy backtracking could hurt volume growth.
HZ IN	Hindustan Zinc	Improving fundamentals for zinc gives a FY18e EV/EBITDA multiple for HZ to 8.0x for its resident zinc and lead business. We believe a higher multiple for HZ is justified given persistent deficit for the zinc market over the medium term. We have a Buy rating as zinc is our preferred commodity with prices expected to rise significantly from currently levels as the deficit widens on improving supply-demand dynamics.	Downside risks: Lower-than-expected zinc/lead/silver prices; higher than expected power and fuel cost and increase in stripping costs as well as lower production from RAM, as mines go underground.
IDEA IN	Idea	For our DCF model, we assume a cost of equity of 9.0%, a cost of debt of 9.5% (long-term debt-to-equity ratio of 0.3), and a WACC of 9.0%, at a fair value of INR62 per share. Reduce rating given that the stretched balance sheet and increased competitive intensity the company faces in the data space.	Upside risks include Idea managing data revenue growth at par with Bharti and 4G entrants, as well as the ability to monetize tower assets before spectrum auctions or anytime soon. Idea's ability to participate in sector consolidation is another key upside risk. If Idea were to focus more on its established markets and divest from its new circles, we would view this as positive. The ability to move to network sharing with incumbent telcos on 4G and to benefit from fibre sharing could be significant positives for Idea, as these would reduce pressure on the balance sheet and enhance the company's ability to participate in data growth.
1970 HK	IMAX China	Our target price of HKD40 is derived from a DCF model, calculating a WACC of 7.1% (risk free rate =2.5%, market risk premium = 5%, terminal growth rate = 4%)	Upside risks: (1) potential blockbuster such as Legend of Ravaging Dynasties, and The Great Wall, (2) more IMAX screens orders ahead, and (3) better IMAX films pipeline in 2017 compared to 2016, including Transformers, Star Wars. Downside risks: (1) further slowdown of box office in Q4 and 2017 and (2) less revenue sharing ratio because of competition from new screen technologies, such as Dolby.
ISAT IJ	IndoSat	We calculate a fair value target price of IDR7,800 for Indosat using a DCF-based methodology. A cost of equity of 9%; a debt/capital ratio of 50%, a terminal growth rate of 1%. This returns a WACC of 7.5%, and our fair value of IDR7,800.	Key downside risks are higher competition than expected, and foreign exchange-related weakness.

Valuation and risks

Code	Company	Valuation methodology	Risks to our view
JSTL IN	JSW Steel	A fair value target price of INR2,090/share for JSW Steel. We value JSW Steel on a FY18e EV/EBITDA of 6.5x.	Key downside risks include lower than estimated domestic demand which is likely to put pressure on realisations as well as margins. Sustained increase in the input costs are likely to impact profitability if the company is not able to pass on to the end users
015760 KS	Kepco	We think Kepco deserves to trade at a higher valuation than the current level of 0.4x 2017e PB given its better earnings presence. Kepco's 10-year historical trading average was 0.5x PB. For our target price of KRW67,000, we apply our target PB multiple of 0.55x (trading average during 2014-15 when Kepco turned into a profit generating company after 6 years of losses) to our 2017e BVPS. *Kepco is a constituent of the HSBC Asia Super Ten and GEMs Super 15 portfolios.*	Key downside risks: (1) introduction of regulations for the power industry that could affect power tariffs; (2) possible changes in the government's stance on Korea's power plant builds, which could impact Kepco's cost structure; and (3) significant raw material price hikes, which could increase Kepco's fuel purchasing costs.
030200 KS	KT Corp	In our DCF valuation, an 8% cost of equity and add a 5% country risk premium (effectively a CoE of 13%). Our cost of debt of 5% and debt-to-capital ratio of 30% result in a 10.2% WACC. A 0.5% terminal growth rate.	Key downside risks include (1) higher-than-expected mobile competition, (2) higher-than-expected capex, (3) political pressure on tariffs ahead of the elections, and (4) faster-than-expected declines in the wireline business.
3008 TT	Largan Precision	Our target price of TWD4,473 is based on a target multiple of 20x applied to 2017e EPS. We believe 20x PE multiple for Largan is justified by (1) 24% earnings CAGR in the next two years versus a 4% earnings decline in 2016 and (2) Sunny Optical's current valuation (24x 2017e) implied c25x multiple for its lens business. *Largan Precision is an HSBC Asia Super Ten portfolio stock.*	Downside risks include (1) lower-than-expected dual-camera adoption rate on iPhones and China smartphones in 2017/2018, (2) lower-than-expected global smartphone demand, (3) slower than expected smartphone lens spec migration, (4) faster-than-expected yield rate ramp of competitors or lower than expected yield rate of Largan itself, (5) severe shortage of any smartphone components, and (6)TWD appreciation against the USD. 90% of Largan's revenue is based on USD while most costs are in TWD.
LT IN	Larsen & Toubro	We value L&T's core EPC business at a target one-year forward PE of 25.4x (1.5 standard deviation above its past business cycle mean). We value L&T's subsidiaries at a combined INR436 per share, incorporating a 10% holding company discount. Our target price implies the stock will trade at a December 2017e PE of 23.7x, while it is currently trading at 18.5x. We regard new orders revival during FY17 and earnings recovery over the next few quarters as the key stock price catalysts.	Slower-than-expected pick-up in execution Our revised forecasts for L&T factor in an improvement in execution and new orders over the next two years. Our view is based on recent data points, which suggest the investment cycle is picking up. A relapse in the business cycle, as witnessed during 2015, is therefore a risk to our investment thesis and forecasts for L&T. Cancellation of orders in the existing order book We expect revenue growth in L&T's domestic business to accelerate over the next two years, growing at a 16% CAGR. Our forecasts are backed by a healthy backlog and strengthening lead indicators, which point to an improvement in project execution. Slower-than-expected growth in sales as a result of order cancellations is therefore a key risk to our forecasts.
051910 KS	LG Chem	We use a sum-of-the-parts methodology: (1) for Chemical, we apply a 6.5x EV/EBITDA multiple (Korea market average) to normalised two-year forward average EBITDA, (2) for IT and electronic materials, we apply a 6.5x EV/EBITDA multiple (Korea market average) to normalised two-year forward average EBITDA of KRW434bn, and (3) for Battery, we apply 12.2x EV/EBITDA (average 2016e EV/EBITDA multiple of regional EV battery makers peers).	Key downside risks: A rise in oil prices could squeeze petrochemical margins; KRW depreciation; weaker-than-expected display panel demand could hurt results as LG Chemical also has significant business exposure to the display-focused IT industry.
034220 KS	LG Display	We see fair value at 0.9x average of our 2016e and 2017e BVPS of KRW38,945, which gives us a fair-value target price of KRW35,100. We chose a 0.9x PB multiple because it is the midpoint of its trading range in 2014 and we see the magnitude of the display sector's recovery and margin performance in 2H16 being comparable to that of 2H14.	The key downside risk for LGD is a slowdown in size migration. Company-specific risks include (1) aggressive investment in OLED, which has yet to be commercially proven for large sized applications; and (2) high volatility in Apple's product cycles.
NTES US	NetEase Inc.	Our target price is derived from a 1x PEG based on our 2017e EPS of RMB128.66.	Key downside risks: (1) game delays which lead to lower-than-expected revenue contribution, (2) weaker-than-expected adoption of games, (3) higher operating costs, and (4) stricter regulation on online game and other business.
9437 JP	NTT DoCoMo	In our DCF valuation, we apply a WACC of 8.5% and a terminal growth rate of 0%.	Key downside risks: higher-than-expected competition, potential increases in capex to manage increased data demand, faster-than-expected voice revenue declines, and higher-than-expected costs to develop new business areas.
6 HK	PAH	Our DCF-based target price of HKD90 is based on a cost of equity of 5%, risk-free rate of 2.5% and an equity beta of 0.6.	Downside risks: Weakening GBP and AUD, which would lower income from overseas business; worse-than-expected outcome of the next tariff reset for businesses in Australia in 2015-16; lower-than-expected permitted return under the renewed SOC in Hong Kong.
8 HK	PCCW	In our sum of-the-parts valuation, we use a DCF to value HKT Trust; we value the media business at a 6.7x 2016e EBITDA multiple, and the solutions business at an 11.3x 2016e EBITDA multiple. A 25% holding company discount is applied.	Key downside risks: uncertainty over acquisition strategy, greater competition in wireless and wireline market, greater competition in the media market in Hong Kong and Asia, slowing growth in the solutions segment.

Valuation and risks

Code	Company	Valuation methodology	Risks to our view
TEL PM	PLDT	We value PLDT using a sum-of-the-parts model to derive a target price of PHP2,200 – DCF for the core telco business and the three-month average market price for Manila Electric Co (MER PM, PHP266, Hold, covered by Tarun Bhatnagar) and Rocket Internet (not rated). For the core telco business we continue use a DCF valuation, in line with other stocks under our coverage. We prefer DCF given its focus on medium-term cash flows and uncertainty over future levels of dividend payment. We apply a cost of equity of 7.5%, a target debt-to-capital ratio of 30% and a tax rate of 30%. This returns a WACC of 6.3% and a target price of PHP2,200.	Key downside risks: loss of wireless market leadership and irrational competition from existing and/or new competition.
TLKM IJ	PT Telekom	We calculate a fair value target price of IDR4,600 for PT Telkom using a sum of the parts DCF based methodology, in which we apply: a cost of equity of 9%; a debt/capital ratio of 35%; a terminal growth rate of 3% for the Telkomsel wireless business, and 1% for the wireline business. This returns a WACC of 7.2%, and gives a fair value target price of IDR4,600.	Key upside risks are limited or ineffective network sharing, and continued strong financial results. Key downside risks are brand weakening as other operators roll out 4G, and further intensified and irrational competition.
005930 KS	Samsung Electronics	Our target price is based on a target PB multiple of 1.5x, which is the historical 10-year average multiple, applied to our 2017e book value.	Key downside risks include (1) a fall in demand caused by a global economic slowdown or appreciation of the KRW, which could lead to weaker earnings; (2) further intense competition from emerging mobile companies and potential competition in NAND; (3) from a technology perspective, any unexpected difficulty in mass-producing foldable smartphones; (4) weaker-than-expected smartphone growth, especially in the high-end segment; and (5) weaker traction of foldable smartphones among end users.
000089 CH	Shenzhen Airport	Our target price of RMB9.50 based on a WACC of 8.8% (risk-free rate 2.5% and equity beta of 1), we arrive at a fair value of RMB9.50 per share.	Upside risks: a significant hike in peak hour movement, better-than-expected international volumes. Downside risks: suspension of new flights, expensive capex, and termination of Terminal A/B lease contract and connected transactions with its parent.
300124 CH	Shenzhen Inovance	We value Inovance on a relative PEG valuation with its A-share automation peers. We derive our target price of RMB24 from forecast EPS and a PEG ratio of 2.2x in 2016e, benchmarked to its A-share automation peers on a relative scale.	Key downside risks: weaker-than-expected elevator demand growth; policy risks arising from new energy vehicles; slower-than-expected market share gains for EV or urban mass transit product and potential overseas acquisition.
6826 HK	Shanghai Haohai Biotech	Our target price of HKD50 is based on 22x 2016e PE The multiple is comparable to Bloomage's (963 HK, HKD12.28, Buy) target price-implied valuation multiple, as we expect Haohai to perform strongly in the cosmetic surgery market.	Downside risks include higher-than-expected price cuts for ortho HA injections and competition from new entrants in the cosmetic surgery space.
ST SP	SingTel	We value Singapore, Optus operations and regional associates using DCF. For Singapore and Optus, we apply (1) a cost of equity of 8.8% and a cost of debt of c5.0%, (2), a beta of 1.15, (3) a tax rate of 23.5% and a terminal growth rate of 1%, (4) this returns a WACC of 7.6% for both the Singapore and Optus operations.	Key downside risks: (1) a greater-than-anticipated negative impact from the entry of a fourth operator in Singapore, leading to steeper-than-expected ARPU decline or market share erosion: (2) greater-than-anticipated competition in Australia (as Telstra steps up its capex intensity) could pose downside risk (Optus contributed c23% of group's free cash flow in FY16); and (3) any significant adverse exchange rate fluctuations that could diminish the value of the non- Singapore parts of the business, which contributed c68% to group's free cash flow in FY16.
1308 HK	SITC	We value SITC's shares based on a price-to-book approach. Our target price of HKD5.40 is based on a 2.0x target price-to-book multiple similar to the average of its mean and highest 12-month forward PB multiples since 2011.	Key downside risks: slower-than-expected economic development in China; a continued slowdown in intra-Asia trade growth; a sharp rise in bunker fuel prices; increase in trade protectionism or delays in the implementation of trade liberalisation agreements currently under negotiations; the stock has low liquidity (its average daily trading value was just USD1m in the past six months).
000660 KS	SK Hynix	Our target price is based on a target multiple of the 10-year average PB of 1.6x applied to our 2017e book value. We use the historical average multiple to factor in ROE improvement as well as the demand-driven DRAM upcycle reflecting better fundamentals.	Key downside risks include (1) greater KRW appreciation than expected, (2) weakness in the JPY which could undermine competitiveness, and (3) a potential fall in PC demand caused by a global economic slowdown.
TATA IN	Tata Steel	We value TATA on a FY18e EV/EBITDA based sum-of-the-parts approach, with multiples of 6.5x (higher than through cycle multiple as in a down-cycle the multiples tend to expand) for its Indian and European and other Asian steelmaking operations.	Downside risks include muted domestic demand leading to pressure on realisations. Lower offtake from the European operations due to weak economic conditions or higher uncertainty due to the UK Brexit vote is a further downside risk. Higher coking coal prices on a sustained basis could also impact margins.
TECHM IN	Tech Mahindra	We value the company on 15x 12-month forward basis	Downside risks: Further weakness in the network services space may drag on revenue growth and is a downside risk to our estimates. Low margins on new deals could lead to lower-than-expected earnings. TechM has an active M&A policy which may give rise to integration issues relating to new acquisitions.

Valuation and risks

Code	Company	Valuation methodology	Risks to our view
TNB MK	Tenaga Nasional	We use a blend of three methodologies: DCF, PE and PB to value Tenaga. We continue to allot a 50% weight to DCF and 25% each to PE (target PE of 11.0x on FY17 EPS) and PB (target PB of 1.4x on FY17 BVPS). Our target price is based on DCF valuation (2.5%) risk-free rate and 4.0% equity risk premium and a beta of 1.1) and implies a 14.4x FY17e PE.	Downside risks include higher-than-expected coal or LNG costs than allowed by the regulator; lower-than-expected volumes; and higher-than-expected MYR depreciation.
700 HK	Tencent Holdings	We use a sum of-the-parts methodology. Based on 2017e estimates, we value PC gaming business at 12-17x 2017e NOPAT, amounting to HKD30-43/share. We value the smartphone gaming business at 25-30x 2017 NOPAT, translating into HKD69-82/share. We value subscription and digital content business at 30-35x 2017e NOPAT. This amounts to HKD42-48/share. Total VAS is valued at HKD140-173/share. We value online advertising business at 30-35x 2017e NOPAT. This amounts to HKD10-12/share. The Other segment includes Internet finance, Tencent Pictures, cloud and others which we value using 5-10x 2017 revenue. This yields HKD22-43/share. We continue to include Tencent's investments in associates and available-for-sale financial assets at book value and net cash, HKD16/share and HKD1/share.	Key downside risks include (1) Tencent's failure to continue to offer expansion packs and features that lead to higher monetisation of games, (2) failure to take advantage of the leading position in the digital consumptions, especially video, music, and sports, that leads to less user engagement on the platform, (3) Tencent's ability to generate revenue from WeChat below our forecast, and (4) online advertising being below expectations.
002739 CH	Wanda Cinema Line	We derive our target price of RMB85 with DCF valuation (2.5% risk free rate, 6.0% market premium, 1.17 beta, 8.5% WACC, 3% terminal growth rate).	Downside risks: (1) worse-than-expected box office revenue performance in domestic China and (2) lower-than-expected market share due to increasing competition.
300017 CH	Wangsu Science & Technology	We derive our target price of RMB89 by applying a 35x PE to our 2017e EPS of RMB2.53. *Wangsu Science & Tech is an HSBC Asia Super Ten portfolio stock.*	Key downside risks: (1) competition in the CDN market, especially from China's internet giants, (2) poorer-than-expected performance in cloud computing, and (3) potential bankruptcy of start-up internet clients, which could affect account receivables.
000858 CH	Wuliangye Yibin	Our DCF-based target price of RMB41.00 implies a 17.5x 2017e PE. We use a WACC of 7.6% in our DCF model, and it is based on a risk-free rate of 2.5%, an equity risk premium of 6% for China, and an equity beta of 0.84.	Key downside risks include political and macro risks, higher-than-expected selling expenses, and changes in government policy on taxation.
EXCL IJ	XL Axiata	We use a DCF methodology to value XL Axiata stock. Our DCF inputs are: cost of equity of 9% in line with the recommendation by the HSBC equity strategy team; debt to capital ratio of 50%; and a cost of debt of 5%. This returns a WACC of 6.4%. We apply a terminal growth rate of 1%.	Downside risks include: execution failure, resulting in the company being unable to attract high-ARPU and low churn subscribers. Irrational competition in the market, if the operators shift their focus back to subscriber market share acquisition, leading to lower levels of monetization and profitability. Revenue cannibalization, as customers switch from voice and data services to packet data.
600519 CH	Kweichow Moutai	Our target price of RMB380 is based on a three-stage DCF model with the following assumptions – WACC of 6.9%, risk-free rate of 2.5%, equity risk premium of 6%, equity beta of 0.73 and terminal growth rate of 2%	Key downside risks include a weaker-than-expected macro environment and changes in government policy on taxation.
220 HK	Uni-President China	Out target price is based on a three-stage DCF model with the following assumptions – WACC of 7.0%, risk-free rate of 2.5%, equity risk premium of 6%, equity beta of 0.90 and terminal growth rate of 1%	Key downside risks include unsuccessful product roll-outs, a worse-than-expected pricing environment due to competition, and higher-thanexpected A&P expenses.
007070 KS	GS Retail	We use a sum of-the-parts valuation approach. We value the convenience store division at a 16.5x 2017e EV/EBITDA – at a 30% premium to the average target multiple for consumer staples under our coverage because of its superior growth prospects despite its low margin. We conservatively assign zero value to the supermarket division and a KRW760bn value to Parnas Hotel in line with its acquisition valuation.	Key downside risks include: (1) Inability to turnaround the supermarket and hotels divisions, (2) entering into overseas market, such as Indonesia, (3) new store openings cannibalizing existing stores, and (4) poor food safety and hygiene issues.
787 HK	Global Brands	Our target price of HKD1.50 is based on 7x 2017e EV/EBITDA, benchmarking to US department store operators as GBG wholesales its products to major US department stores.	Key downside risks include weak US demand, unfavourable FX conditions and raw material price trends, and higher-thanexpected brand and staff investments.

Source: HSBC estimates

Disclosure appendix

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Company	Ticker	Recent price	Price date	Disclosure
ADVANTECH	2395.TW	251.50	5 Dec 2016	6, 7
AIRTAC	1590.TW	242.00	5 Dec 2016	7
ALIBABA GROUP	BABA.N	90.99	5 Dec 2016	5, 6
BAIDU INC	BIDU.OQ	164.32	5 Dec 2016	6
CHEUNG KONG INFRA	1038.HK	64.45	5 Dec 2016	1, 2, 5, 6, 7, 11
CHINA UNICOM	0762.HK	9.41	5 Dec 2016	6, 11
CSSC OFFSHORE & MARINE	0317.HK	12.06	5 Dec 2016	7
DELTA ELECTRONICS	2308.TW	155.50	5 Dec 2016	6, 7
E INK HOLDINGS	8069.TWO	22.55	5 Dec 2016	6
GLOBAL BRANDS GROUP	0787.HK	1.24	5 Dec 2016	5, 6, 7
HDFC	HDFC.NS	1215.55	5 Dec 2016	5, 6, 7
HDFC BANK	HDBK.BO	1196.35	5 Dec 2016	5, 6, 7
HIKVISION	002415.SZ	25.42	5 Dec 2016	6, 7
HINDALCO	HALC.BO	174.50	5 Dec 2016	6
IDEA CELLULAR LTD	IDEA.NS	72.65	5 Dec 2016	7
IMAX CHINA	1970.HK	38.60	5 Dec 2016	7
JSW STEEL LTD	JSTL.BO	1648.55	5 Dec 2016	6
KT CORP	030200.KS	29500.00	5 Dec 2016	6
LARGAN PRECISION	3008.TW	3580.00	5 Dec 2016	4, 6, 7
LARSEN & TOUBRO	LART.BO	1356.15	5 Dec 2016	2, 6, 7
NETEASE INC	NTES.OQ	226.17	5 Dec 2016	6, 7
PCCW	0008.HK	4.51	5 Dec 2016	4, 6, 7
PHILIPPINE LONG DISTANCE TELEP	TEL.PS	1280.00	5 Dec 2016	6
POWER ASSETS HOLDINGS	0006.HK	72.00	5 Dec 2016	1, 4, 5, 6, 11
SHENZHEN INOVANCE TECH	300124.SZ	21.05	5 Dec 2016	7
SINGAPORE TELECOM	STEL.SI	3.77	5 Dec 2016	1, 5, 6
SK HYNIX INC.	000660.KS	44400.00	5 Dec 2016	7
TATA STEEL	TISC.BO	413.50	5 Dec 2016	6
TECH MAHINDRA	TEML.BO	462.40	5 Dec 2016	6
TENAGA NASIONAL	TENA.KL	14.02	5 Dec 2016	1, 4, 5, 6
TENCENT HOLDINGS LTD.	0700.HK	190.00	5 Dec 2016	2, 4, 5, 6, 11
UNI-PRESIDENT CHINA	0220.HK	5.30	5 Dec 2016	6
WANGSU SCIENCE AND TECH	300017.SZ	58.10	5 Dec 2016	7
WULIANGYE YIBIN CO LTD	000858.SZ	35.54	5 Dec 2016	7

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