Hong Kong Stocks Jump to 2015 High as Fed, China Energize Bulls

2017-03-16 08:14:05.699 GMT

By Richard Frost

(Bloomberg) -- Hong Kong equities are back at heights unseen since China devalued its currency in August 2015.

A dovish Federal Reserve, China growth optimism and steady mainland inflows combined to fuel a 2.1 percent rally in the Hang Seng Index on Thursday, the biggest advance in almost 10 months. The gain also pushed the gauge firmly above the 24,000 level -- an effective ceiling for the past seven years. China Unicom Hong Kong Ltd. and Link REIT were among the day's best performers, while Cathay Pacific Airways Ltd. was one of only two decliners after posting a loss on Wednesday.

Hong Kong-listed equities are particularly vulnerable to shifts in sentiment toward U.S. monetary policy thanks to a currency peg with the greenback, while the increasing dominance of Chinese companies on the city's benchmarks means national economic indicators have a powerful pull. With investors relieved the Fed didn't increase the projected pace of rate hikes and fears of a Chinese hard landing receding, the serially under-performing Hang Seng Index may have room to rally further.

The Hang Seng Index has risen 14 percent over the past five years, trailing the 70 percent gain by the S&P 500 Index or the

38 percent advance by the Stoxx Europe 600 Index. The Hong Kong benchmark trades at 1.3 times net assets, compared with 3.1 for the U.S. gauge and 1.8 for the European measure.

After a torrid fourth quarter, when the Hang Seng Index lost more than 5 percent as the yuan tumbled, the measure has had a brighter 2017. Brokerages have turned increasingly bullish on Chinese shares traded offshore, with Goldman Sachs Group Inc.

lifting its estimate for the MSCI China Index this week and projecting a faster pace of earnings growth.

A stabilizing yuan has added to investor confidence.

China's economy started the year on a firm footing as its old growth engines gathered pace, home sales remained resilient and steel to aluminum rebounding.

Hong Kong-traded shares have also been buoyed by inflows by mainland investors through exchange links with Shanghai and Shenzhen. Goldman Sachs estimates such flows will total $54 billion this year.

Long-term investors will recognize, however, that while these major drivers are fueling Hong Kong stock gains, the failure of any one of these engines could quickly shift the rally into reverse, as seen periodically last year and in 2015.

--With assistance from Philip Glamann.

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