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China Equity Mid-Year Outlook | Asia Pacific

Patience through Bumpy Final Leg of Bear Market

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We expect near-term market volatility to remain elevated, given the fluid situation domestically (Omicron) and globally (geopolitics, macro slowdown, QT kickoff). Policy easing cycle is forming, but timing and scale are contingent on Covid control, implying likely front-loaded risks.

MSCI China could be approaching the late stage of a bear market after a 14-month drawdown (51% down in absolute terms, 32% relative to MSCI EM since Feb 17, 2021), but the potential final leg is likely to be bumpy: Broader economic drag due to Omicron spread and subsequent restrictive measures imply downside-skewed earnings pressure and a capping effect of potential immediate China policy easing. Meanwhile, external concerns, such as QT overlapped with a gloomier global outlook and extended geopolitical tension, could also curb near-term re-rating opportunity. Our June 2023 base case index targets are a respective 70; 21,500; 7,330; and 4,300 for MSCI China, Hang Seng, HSCEI, and CSI300, suggesting 9%, 7%, 8%, and 10% upside vs. the 6 May market close.

We take the latest Politburo meeting signals positively, but would stay equal-weight on Chinese equities within the global EM framework in the near term. We welcome recent policymakers' reference to easing measures stepping up, with a focus on infrastructure boost, potential relaxation of property purchase restrictions and escrow fund access, and the positive role capital plays/completion of regulatory reset. That said, **our China equity framework suggests that the policy positives could be discounted by the aforementioned factors,** with downside risk more front-loaded in the near term.

Signs to get more positive: 1) (sustainable) restoration of supply chain and concrete measures to prevent Covid-disruption; roadmap of Covid-zero relaxation would be a major plus;

2) execution following the politburo announcements: easing step-up; positive guidance for regulatory reset and private enterprises; stabilization efforts for the property sector;

3) volatility getting priced in for geopolitical tension escalation and QT/recession concerns; stabilization of CNY weakness;

4) US/China audit agreement and resumption of Chinese company offshore IPOs.

Continue to prefer A-shares vs. offshore China given their better positioning to benefit from potential easing in the near term, and alignment with long-term growth opportunities (IT, industrials, green economy, etc.). Latest official launch of personal pension scheme should also support institutional participation.

See the next section for Sector preferences and Key trades for 2H2022.

Exhibit 1: Morgan Stanley Research base, bull, and bear case earnings estimates, valuations, and targets across Chinese equity indices coverage - targets trimmed for all indices we cover

	Index	Current Price	MS Target Price Jun-23	Prior MS Target (Dec-22)	MS Top-Down EPS YoY %			Consensus EPS Forecast YoY %			MS Target Fwd P/E Jun-23	Prior MS Target Fwd P/E	Consensus 12m Fwd P/E Current
					Dec-22	Dec-23	Jun-24	Dec-22	Dec-23	Jun-24			
Base Case	Hang Seng	20,002	**21,500** 7%	22,600 13%	1,930 5%	2,177 13%	2,264 10%	2,024 11%	2,311 14%	2,401 11%	9.5x	10.0x	9.5x
	HSCEI	6,810	**7,330** 8%	7,600 12%	801 5%	890 11%	917 8%	814 7%	922 13%	975 12%	8.0x	8.2x	8.0x
	MSCI China	64	**70** 9%	75 17%	5.9 8%	6.7 14%	7.1 12%	6.3 15%	7.3 16%	7.5 11%	10.0x	10.5x	9.8x
	CSI300	3,909	**4,300** 10%	4,460 14%	317 10%	355 12%	373 11%	322 12%	376 17%	400 15%	11.5x	11.8x	11.5x
Bull Case	Hang Seng	20,002	**26,500** 32%	29,200 46%	1,972 8%	2,227 13%	2,339 11%	2,024 11%	2,311 14%	2,401 11%	11.4x	12.2x	9.5x
	HSCEI	6,810	**8,820** 30%	9,700 42%	813 7%	917 13%	953 10%	814 7%	922 13%	975 12%	9.3x	10.1x	8.0x
	MSCI China	64	**85** 33%	100 56%	6.0 10%	6.9 15%	7.3 13%	6.3 15%	7.3 16%	7.5 11%	11.8x	13.0x	9.8x
	CSI300	3,909	**5,300** 36%	5,700 46%	327 14%	373 14%	393 12%	322 12%	376 17%	400 15%	13.5x	14.5x	11.5x
Bear Case	Hang Seng	20,002	**17,000** -15%	19,700 -2%	1,843 1%	1,959 6%	2,014 6%	2,024 11%	2,311 14%	2,401 11%	8.5x	9.3x	9.5x
	HSCEI	6,810	**5,830** -14%	6,500 -5%	769 1%	819 6%	838 6%	814 7%	922 13%	975 12%	7.0x	7.5x	8.0x
	MSCI China	64	**55** -14%	61 -5%	5.6 3%	5.9 6%	6.2 7%	6.3 15%	7.3 16%	7.5 11%	8.9x	9.0x	9.8x
	CSI300	3,909	**3,400** -13%	3,800 -3%	295 3%	316 7%	327 7%	322 12%	376 17%	400 15%	10.4x	11.3x	11.5x

Source: MSCI, IBES, Bloomberg, FactSet, RIMES, Morgan Stanley Research estimates. Data as of May 6, 2022.

Sector preferences

We continue to like Materials and Industrials for exposure to the infrastructure activity boost. We also continue to prefer some defensiveness through dividend yield plays and exposure to Utilities.

We stay cautious on consumption-related categories (retailing, auto, consumer staples, etc.), near term, due to Omicron headwinds, but remain nimble to potential policy relaxation and stimulus as well as pent-up demand release. We also remain on the sidelines with property as the sales slowdown may not turn around as quickly due to macro pressure.

Key trades for 2H2022

1. Wait for better risk/return opportunities before upweighting Chinese equities.
2. Within Chinese equities, continue to overweight A-shares vs. MSCI China, but be prepared for relatively back-loaded sustainable outperformance.
3. Focus on high-quality stock/theme level opportunities: Oversold high-quality names, share buyback candidates, as well as infrastructure boost beneficiaries.

China Outlook – Stay equal-weight within EM/APxJ, with limited index upside

Policy catalysts emerging targeting growth and sentiment; Stay equal-weight China, near term, due to execution hurdles and external risks

We roll over our index targets by six months, to June 2023, with slight downward adjustments in our earnings growth outlook and valuation forecast, as we believe near-term macro headwinds stemming from the spread of Omicron, global central bank tightening, and geopolitical risks, will still curb immediate market improvement. Our new base case June-2023 targets for the Hang Seng, HSCEI, MSCI China and CSI300 at 21,500, 7,330, 70, and 4,300 imply upsides of 7%, 8%, 9% and 10% (as of May 6, close), respectively.

Signs of top-down policy support emerging, with focus on key capital market concerns: Our outlook incorporates the latest positive signs of top-down policy support from China's Politburo meeting, on multiple fronts, including growth stimulation, regulatory reset wrapping up, property purchase restriction, and credit access relaxation, among others, as compared to six months ago when we published the 2022 China Equity Strategy Outlook: Navigating Risks Before Dawn (14 Nov 2021). In particular, we highlight the explicit references of "Optimizing regulation of commercial housing escrow funds" and "Completion of dedicated regulation for the platform economy," as they are directly linked to two key pressure points (property market default risk, regulatory reset) for the China equity market's lackluster performance over the past several months (the other two drags being Omicron disruption and global geopolitical tension). Read more: China Equity Strategy: Positive Signal from Politburo Meeting – Execution Key to Sustaining Sentiment Lift (29 Apr 2022).

We may be in the late stage of a bear market after 14-months of drawdown; however, global and domestic uncertainties suggest further patience may be warranted in the near term: MSCI China has been in a bear market for more than 14 months now (counting from the recent price index peak on Feb 17, 2021), and the index had fallen 51% from the peak, much longer and deeper vs. other major equity markets in the world (Exhibit 2). Even on a relative basis, MSCI China has fallen 32% vs. MSCI EM since Feb 17, 2021, giving back all outperformance since 2017, with the duration of the current underperformance cycle much longer than previous ones (Exhibit 3). **We could very well be entering the final leg of the current bear cycle, but this leg could be rather bumpy and extended,** buffeted by macro and global uncertainties, and may thus require additional patience before the market musters the ability to mount a sustainable recovery rally.

The lingering uncertainties that could deter a smooth equity market recovery, particularly in the coming couple of quarters, include, in our view, the following:

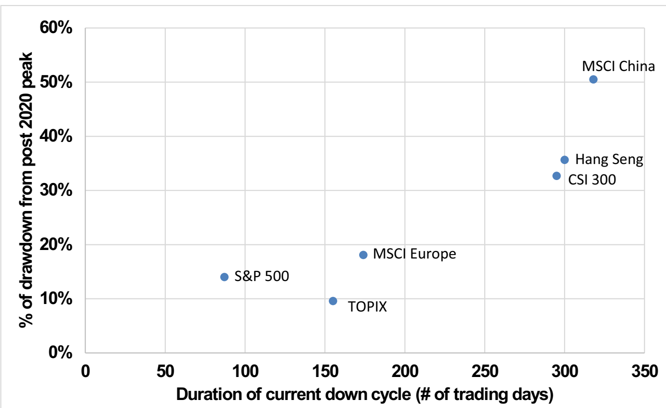
- ongoing Omicron outbreak and subsequent restrictive measures could curb both corporate earnings growth and stimulus policy implementation timing and scale;

- potentially heightened global equity market volatility led by US equities; the Morgan Stanley US equity strategy team is expecting a 1 P/E point derating for the S&P 500 by June 2023 (Read more: Global Strategy Mid-Year Outlook: The Tempest);

- a generally less favorable shift of equity market dynamics for broad EM equities, given the latest global stagflation concerns, as well as accelerating Fed rate hikes and QT kicking off;

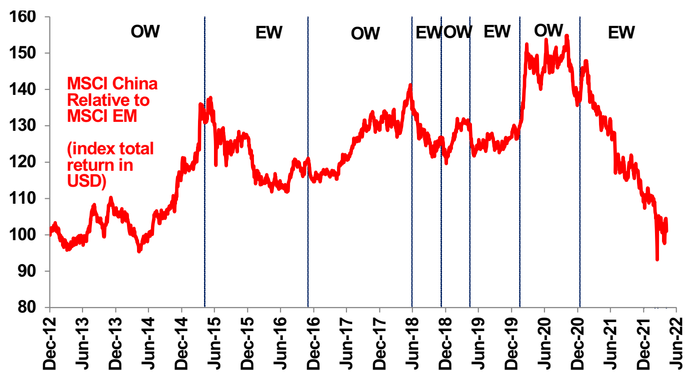
- global geopolitical tension arising from the Ukraine/Russia conflict could continue to weigh on China's ERP, with investor concerns over China's stance and other regional disputes.

Exhibit 2: Chinese equity indices vs. global equity indices in duration and % of drawdown in current downcycle – MSCI China has been in a bear market much longer and deeper vs. other major equity markets in the world



Source: MSCI, FactSet, Datastream, Morgan Stanley Research. Data as of May 6, 2022.

Exhibit 3: MSCI China vs. MSCI EM relative performance (by index total return in USD) vs. our rating history on China – 32% underperformance since 2021 peak on February 17



Source: MSCI, FactSet, Datastream, Morgan Stanley Research. Data as of May 6, 2022; Past performance is no guarantee of future results.

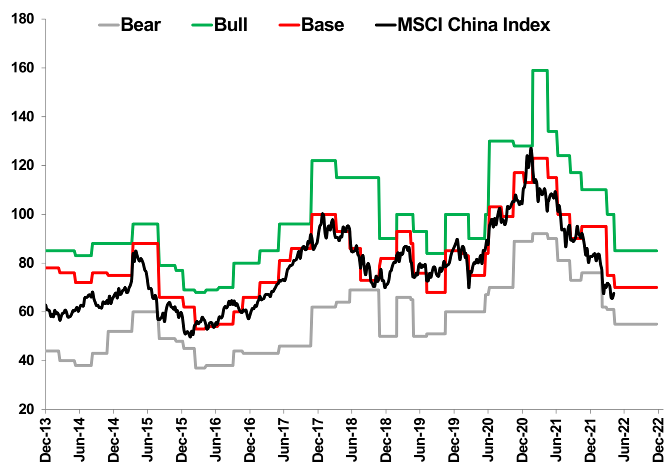
Therefore, we remain EW China within the EM/APxJ framework, and continue to expect market volatility to remain elevated, particularly in the coming few months, while waiting for more clarity around policy execution, Omicron control, and other global risk factors. Within EM broadly, we prefer ASEAN, the Middle East and Brazil, and Commodities & Financials and FCF yield. For more detailed views regarding Asia/EM equity strategy, please see 2022 Asia EM Equity Strategy Mid-year Outlook: Late-stage bear-market.

Exhibit 4: Morgan Stanley Research base, bull, and bear case earnings estimates, valuations, and targets across Asia/EM coverage – We roll over our price targets by six months, to June 2023, with slight downward adjustments of earnings growth outlook and valuation forecast

	Index	Current Price	MS Target Price Jun-23	*Prior MS Target (Dec-22)*	MS Top-Down EPS YoY %			Consensus EPS Forecast YoY %			MS Target Fwd P/E Jun-23	*Prior MS Target Fwd P/E*	Consensus 12m Fwd P/E Current
					Dec-22	Dec-23	Jun-24	Dec-22	Dec-23	Jun-24			
Base Case	TOPIX	1,916	**2,050** *7%*	*2,200* *15%*	151 *18%*	161 *7%*	164 *5%*	149 *15%*	159 *6%*	163 *6%*	12.5x	13.5x	12.5x
	MSCI EM	1,032	**1,060** *3%*	*1,160* *12%*	87 *6%*	93 *7%*	96 *7%*	91 *11%*	99 *9%*	104 *9%*	11.0x	12.0x	11.0x
	MSCI APxJ	537	**570** *6%*	*630* *17%*	42 *8%*	46 *10%*	47 *7%*	43 *11%*	47 *10%*	49 *9%*	12.0x	13.5x	12.1x
	Hang Seng	20,002	**21,500** *7%*	*22,600* *13%*	1,930 *5%*	2,177 *13%*	2,264 *10%*	2,024 *11%*	2,311 *14%*	2,401 *11%*	9.5x	10.0x	9.5x
	HSCEI	6,810	**7,330** *8%*	*7,600* *12%*	801 *5%*	890 *11%*	917 *8%*	814 *7%*	922 *13%*	975 *12%*	8.0x	8.2x	8.0x
	MSCI China	64	**70** *9%*	*75* *17%*	5.9 *8%*	6.7 *14%*	7.1 *12%*	6.3 *15%*	7.3 *16%*	7.5 *11%*	10.0x	10.5x	9.8x
	CSI300	3,909	**4,300** *10%*	*4,460* *14%*	317 *10%*	355 *12%*	373 *11%*	322 *12%*	376 *17%*	400 *15%*	11.5x	11.8x	11.5x
Bull Case	TOPIX	1,916	**2,410** *26%*	*2,570* *34%*	160 *24%*	169 *6%*	172 *5%*	149 *15%*	159 *6%*	163 *6%*	14.0x	15.0x	12.5x
	MSCI EM	1,032	**1,340** *30%*	*1,410* *37%*	96 *17%*	104 *9%*	108 *8%*	91 *11%*	99 *9%*	104 *9%*	12.5x	13.0x	11.0x
	MSCI APxJ	537	**690** *29%*	*729* *36%*	44 *14%*	49 *12%*	51 *10%*	43 *11%*	47 *10%*	49 *9%*	13.5x	15.0x	12.1x
	Hang Seng	20,002	**26,500** *32%*	*29,200* *46%*	1,972 *8%*	2,227 *13%*	2,339 *11%*	2,024 *11%*	2,311 *14%*	2,401 *11%*	11.4x	12.2x	9.5x
	HSCEI	6,810	**8,820** *30%*	*9,700* *42%*	813 *7%*	917 *13%*	953 *10%*	814 *7%*	922 *13%*	975 *12%*	9.3x	10.1x	8.0x
	MSCI China	64	**85** *33%*	*100* *56%*	6.0 *10%*	6.9 *15%*	7.3 *13%*	6.3 *15%*	7.3 *16%*	7.5 *11%*	11.8x	13.0x	9.8x
	CSI300	3,909	**5,300** *36%*	*5,700* *46%*	327 *14%*	373 *14%*	393 *12%*	322 *12%*	376 *17%*	400 *15%*	13.5x	14.5x	11.5x
Bear Case	TOPIX	1,916	**1,640** *-14%*	*1,600* *-16%*	128 *-1%*	134 *5%*	137 *4%*	149 *15%*	159 *6%*	163 *6%*	12.0x	12.0x	12.5x
	MSCI EM	1,032	**890** *-14%*	*940* *-9%*	80 *-3%*	82 *2%*	84 *4%*	91 *11%*	99 *9%*	104 *9%*	10.5x	11.0x	11.0x
	MSCI APxJ	537	**460** *-14%*	*490* *-9%*	37 *-6%*	39 *6%*	40 *6%*	43 *11%*	47 *10%*	49 *9%*	11.5x	12.5x	12.1x
	Hang Seng	20,002	**17,000** *-15%*	*19,700* *-2%*	1,843 *1%*	1,959 *6%*	2,014 *6%*	2,024 *11%*	*2,311* *14%*	*2,401* *11%*	8.5x	9.3x	9.5x
	HSCEI	6,810	**5,830** *-14%*	*6,500* *-5%*	769 *1%*	819 *6%*	838 *6%*	814 *7%*	*922* *13%*	*975* *12%*	7.0x	7.5x	8.0x
	MSCI China	64	**55** *-14%*	*61* *-5%*	5.6 *3%*	5.9 *6%*	6.2 *7%*	6.3 *15%*	*7.3* *16%*	*7.5* *11%*	8.9x	9.0x	9.8x
	CSI300	3,909	**3,400** *-13%*	*3,800* *-3%*	295 *3%*	316 *7%*	327 *7%*	322 *12%*	*376* *17%*	*400* *15%*	10.4x	11.3x	11.5x

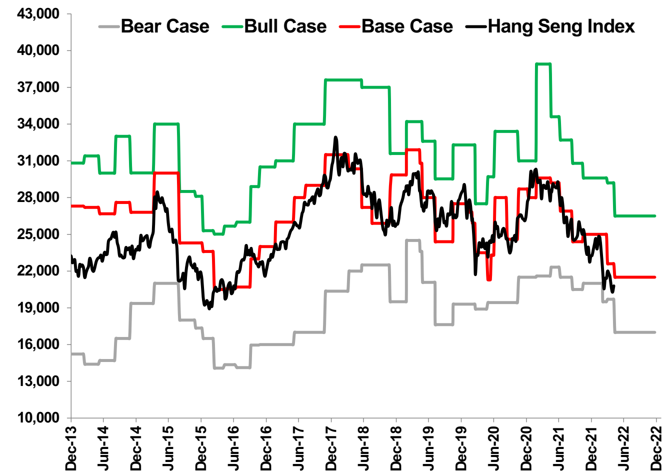
Source: RIMES, MSCI, FactSet, IBES, Datastream, Bloomberg, Morgan Stanley Research. Data as of May 6, 2022.

Exhibit 5: Morgan Stanley Research bull/bear/base case index target history for MSCI China



Source: RIMES, FactSet, Morgan Stanley Research forecasts. Weekly price index data as of May 5, 2022.

Exhibit 6: Morgan Stanley Research bull/bear/base case index target history for Hang Seng Index



Source: RIMES, FactSet, Morgan Stanley Research forecasts. Weekly price index data as of May 5, 2022.

Exhibit 7: APxJ/EM Market Allocation - Full Framework and Recommendations

					Quantitative Factors (60%)									MS House Macro & Micro View (40%)				
				Weight:	10%	5%	5%	5%	10%	2.5%	2.5%	10%	10%	5%	5%	10%	15%	5%
#	Market (MSCI Indices)	Active Risk (bps) Current	Active Risk (bps) Previous	Overall Score	P/B rel to Benchmark 5yr Z-Score	P/E rel to Benchmark 5yr Z-Score	Dividend Yield rel to Benchmark 5yr Z-Score	Earnings Revision Breadth (3mma)	ROE rel to Benchmark 5yr Z-Score	Net Margin 5yr Z-Score	Asset Turnover 5yr Z-Score	Relative Strength Index	Chaikin Money Flow Indicator	Currency	Macro-Economics	Sovereign & Policy Outlook	MS Equity Strategist View	MS Stock Analyst View
1	Singapore	50	50	64	-1.2	-1.7	-1.7	-0.2	-1.6	-1.3	-1.2	42	-0.3	0.1	-1.5	1	5.0	1.9
2	Brazil	50	0	52	1.4	2.1	3.2	-3.6	1.9	1.9	2.4	22	-0.3	-2.1	0.1	-1	3.3	-1.4
3	Saudi Arabia	50	50	41	-2.4	-2.1	-2.4	-	1.7	2.0	-0.6	65	0.0	NA	NA	1	2.0	0.2
4	Chile	25	25	41	0.5	1.7	1.5	10.2	2.2	1.4	-1.2	38	-0.1	-0.2	-1.2	-1	1.8	0.7
5	Australia	50	75	34	-1.8	0.0	0.7	3.6	1.3	2.9	-0.9	43	-0.1	-0.2	0.5	1	0.5	2.1
6	Indonesia	50	50	31	-0.4	-1.3	-0.2	2.1	-1.4	-0.1	-1.2	76	-0.2	3.1	1.8	0	NA	1.6
7	Taiwan	0	0	23	-1.0	1.6	-2.2	5.4	1.8	2.7	-1.3	46	0.1	0.2	0.6	0	-1.0	5.0
8	Qatar	0	0	22	-1.1	-1.7	-1.4	-	-0.6	0.7	-0.9	36	0.0	NA	NA	NA	2.0	0.0
9	South Africa	0	0	22	0.7	1.2	1.7	10.7	1.5	2.4	0.1	13	0.0	3.6	-0.2	-1	0.0	1.0
10	India	0	0	20	-2.0	-1.2	-1.5	-3.8	0.4	1.7	0.4	49	-0.1	1.5	1.1	0	0.6	1.3
11	Poland	0	0	9	1.4	4.3	1.2	0.2	2.2	1.1	-0.6	8	0.2	4.2	0.1	-1	-2.0	-0.4
12	China	0	0	5	3.1	0.1	0.9	-3.9	-2.6	-0.9	0.7	60	-0.1	0.8	0.0	-1	0.5	2.6
13	Peru	0	-50	5	0.7	1.6	-0.3	7.9	0.7	2.0	-1.5	31	0.1	-2.0	NA	-2	2.4	-3.0
14	UAE	0	0	2	-2.0	-2.1	-2.8	-	-1.2	-0.2	-1.1	54	0.3	NA	NA	1	2.0	-1.8
15	Pakistan	0	0	1	0.9	0.5	0.0	11.1	-0.2	-1.7	0.0	39	-0.4	NA	NA	NA	NA	NA
16	Egypt	0	0	1	1.6	0.6	1.5	3.5	-1.6	1.2	-1.7	62	0.2	NA	NA	NA	0.0	0.0
17	Greece	0	0	-2	-0.4	-2.3	-0.5	6.0	-1.6	-1.8	-0.5	44	0.1	1.0	NA	0	0.0	0.5
18	Philippines	0	0	-5	0.7	-0.8	-0.6	0.2	-1.5	0.4	-1.9	45	0.0	0.3	-0.6	-1	NA	1.8
19	Korea	0	0	-9	0.1	0.4	-0.4	-7.2	0.3	1.4	-0.6	69	0.1	0.8	0.1	0	-1.4	1.1
20	Czech Rep.	0	0	-12	-1.8	-1.1	-0.3	17.7	0.2	0.9	-0.6	54	0.0	2.4	-4.8	0	0.0	1.2
21	Colombia	0	0	-17	-0.3	1.2	0.6	10.6	1.4	1.9	-1.5	28	-0.1	2.0	1.6	-1	-3.1	0.0
22	Thailand	0	0	-24	-0.3	-1.9	-1.5	1.1	-1.3	-0.9	3.2	55	-0.2	2.5	-4.0	-1	NA	1.4
23	Malaysia	0	-75	-32	1.4	-0.3	0.5	-1.9	-1.0	0.9	-1.3	51	-0.2	1.7	-0.7	-1	NA	-0.6
24	Turkey	0	0	-35	-1.0	0.3	0.4	21.0	2.4	0.8	1.3	51	0.2	-5.0	1.1	-2	0.0	0.7
25	Argentina	0	-25	-36	1.0	1.0	0.1	13.6	0.2	0.1	-0.6	32	0.0	-5.0	0.9	-2	-1.0	NA
26	Hong Kong	0	0	-37	1.9	-0.8	0.1	-12.7	-1.2	0.1	-1.1	54	-0.1	0.0	-3.3	-1	-0.5	0.3
27	New Zealand	-100	-100	-38	-1.5	0.3	-0.4	-2.5	-0.5	1.1	-1.5	38	-0.2	0.1	NA	1	NA	0.5
28	Hungary	-50	0	-45	2.2	3.7	-0.4	1.2	0.8	1.3	-0.9	61	0.4	-	-0.7	-1	-2.0	-5.0
29	Mexico	-125	0	-63	0.4	0.6	-0.1	5.1	0.3	1.9	0.1	34	-0.3	0.0	-3.0	-1	-3.1	1.1

Source: Bloomberg, IBES, FactSet, RIMES, Morgan Stanley Research.

Bull-bear spread skewed towards the upside; downside risk more front-loaded

Along with our base case (60% probability), we also publish bear and bull case views (20% probability each). Our risk/reward for Chinese equities is more skewed towards our bull case which suggests upside in the range of 30-36% across different Chinese indices, vs. downside in the range of 13-15% implied by our bear case price targets.

In the bull case, we look to a scenario in which MSCI China could recover faster with resilient earnings growth in 2022 and 2023, while valuation goes through a major rerating, by over just below 2 P/E points, with global investors reestablishing their long-term investment confidence in China. Drivers for our bull case could entail some or all of the following:

1. Faster recovery of macroeconomic/supply chain disruption from Omicron, with broad reopening including consumption and services. Investor sentiment would receive a major boost if the Chinese government announces relaxation from Covid Zero policy earlier than expected (the Morgan Stanley Research current base case points to post 20th Party Congress in Oct/Nov 2022).

2. More forceful property market easing to remove market concerns over systemic risks, quicker recovery in property yoy sales trend.

3. Larger-than-expected credit expansion cycle to cushion against upcoming US Fed QT.

4. Broad resolution of ADR audit dispute and fast resumption of key Chinese tech companies' offshore IPOs.

5. Further clear signs of regulatory reset completion.

6. Earlier solution to Russia/Ukraine conflict, which should help alleviate pressure on China's equity risk premium.

In our bear case, we see only mid- to low-single-digit earnings growth for the next two years and further de-rating risks for Chinese equities, with the following potential developments as key triggers:

1. Covid-Zero policy extension, overlapping with rolling outbreaks of Covid in onshore China, causing continuous supply chain and economic disruptions throughout 2022;

2. Greater-than-expected global risk-off sentiment/volatility spike and liquidity tightness triggered by US Fed QT;

3. Major escalation in global geopolitical tension, including US/China non-tariff confrontation;

4. Lack of clarity or even escalation on regulatory tightening for platform/internet and other sectors;

5. Continuous tightening of property market, sustaining broad default risk and systemic concerns.

Downside risks are likely to be more front-loaded, timing-wise. The potential rolling disruption caused by the Covid Zero policy could peak in the coming months, given the nature of the virus and experience from other countries. The Morgan Stanley Research US economics team expects US Fed QT to kick off on June 1 and reach monthly full scale in the three months afterwards. By that time, the market hopefully should have priced in the majority of QT-led liquidity tightness, along with the growth slowdown implications. **However, emergence of any new highly-transmissible Covid variant, deterioration in global economic/liquidity condition, and/or unexpected escalation in**

geopolitical tension could derail any such front-loaded trajectory of the market risk pricing mechanism.

MS China equity framework: Marginal signs of improvement; not yet enough to warrant an upgrade

Positive signals from Politburo meeting; however, long-term ROE trajectory remains in question

We note the latest concerted efforts by Chinese policymakers around the April Politburo meeting to stabilize growth and confidence. We believe those efforts try to emphasize that economic growth remains a key policy focus. This is extremely important for global investors, as they have been attracted to investing in China for long-term sustainable earnings growth, which ultimately depends upon the overall growth trajectory of China.

Three specific points we would like to highlight from the Politburo meeting stance regarding property market and regulatory reset, and, more importantly, the role capital plays:

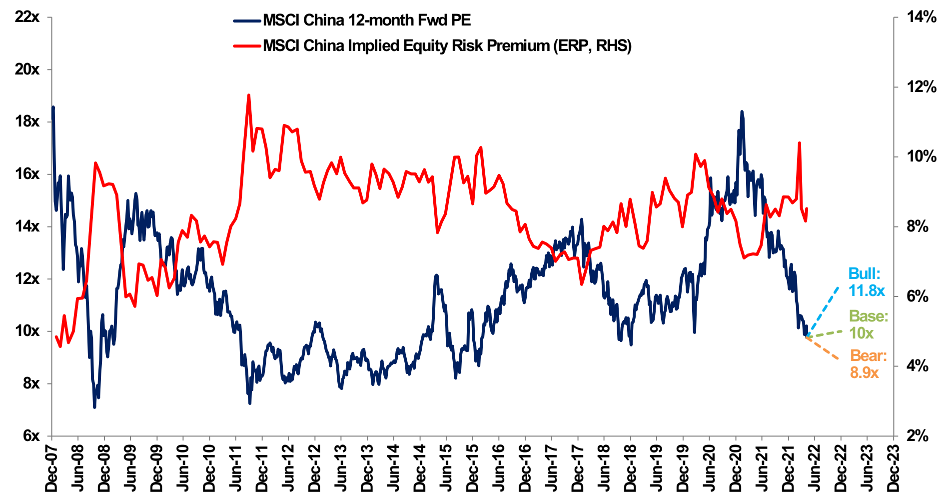
1) clear mentioning of property presales escrow funds for the first time – "Optimizing regulation of commercial housing escrow funds"(from Apr 29th Politburo meeting announcement);

2) completion of dedicated regulation for the platform economy and launch of detailed measures to support proper and healthy development of the platform economy (from Apr 29th Politburo meeting announcement);

3) recognition that "capital is good and important with proper regulation," and thus China should "enhance its positive role for the economy" (from Apr 29th Politburo study session).

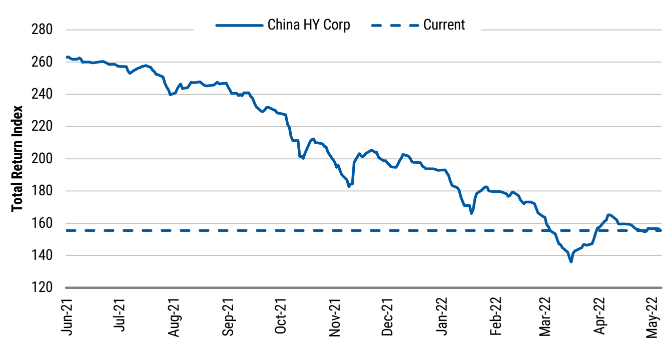
With real relaxation of access to escrow funds, default risks faced by developers could abate gradually and improve the offshore credit market risk assessment (Exhibit 9; Exhibit 10). On the other hand, reassurance that capital is essential to the Chinese economy and that regulatory reset uncertainty is to decline from here should help alleviate pressure on China's equity risk premium, as well. MSCI China's implied ERP had been largely spiking since end-June 2021 (Exhibit 8), when the regulatory reset started to impact in a significant way, with the announcement of new capital market regulation (China Equity Strategy: Capital Market Regulation Announcement: Myths, Facts, Implications [8 Jul 2021]). It has come down somewhat since mid-March given a number of supportive public statements from policymakers, but is still at the higher end of the 5-year range.

Exhibit 8: MSCI China 12-month forward P/E vs implied equity risk premium – MSCI China implied ERP has seen a major spike since 2H21 and still has further room to rise vs. historical peak levels given concerns about geopolitical conflict and Covid policy



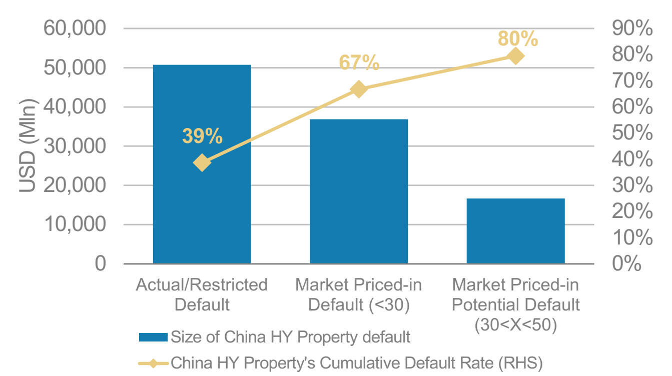
Source: Datastream, FactSet, Bloomberg, I/B/E/S, MSCI, Morgan Stanley Research. Forward P/E is weekly data as of May 6, 2022 and ERP is monthly data as of each month-end, except as of May 6, 2022 for the latest month. Market implied equity risk premium for MSCI China is derived using a three-stage Dividend Discount Model. Yield of UST 10-year is used as a proxy of risk free rate of return.

Exhibit 9: China HY Corporate Bond Index total return – YTD recorded -19%



Source: Bloomberg, Morgan Stanley Research. Data as of May 6, 2022.

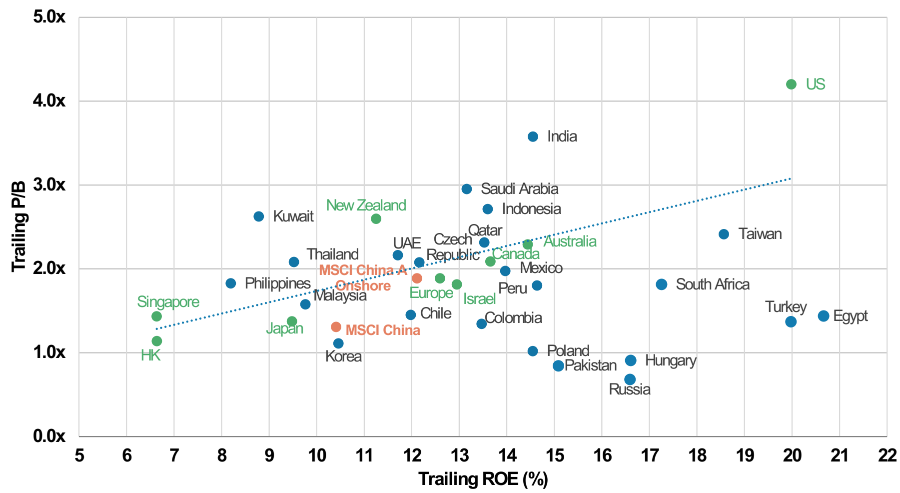
Exhibit 10: The credit market is currently pricing higher default rate for China's HY property sector



Source: Bloomberg, Morgan Stanley Research. Data as of May 6, 2022.

Regulatory reset and adherence to Covid-Zero policy have triggered skepticism from global investors, which is unlikely to dissipate easily from policy announcements alone. The divide between Covid-Zero policy and stabilizing/stimulating economic growth may not easily be resolved by announcements of major policy relaxations ahead of the 20th Party Plenary in Oct/Nov 2022. Therefore, more evidence of execution and Covid-disruption control in the medium term will likely be necessary to help regain confidence. In addition, global geopolitical conflict could continue to weigh on China as investors try to assess risks associated with China's perceived stance on the Russia/Ukraine situation, amid other events. Therefore, **MSCI China's valuation could be curbed at a discount vs. trendline as investors could expect China's long-term ROE to deteriorate as a result.**

Exhibit 11: P/B vs. ROE for global equities – We see additional near-term pressure for MSCI China on valuation amid the latest global geopolitical tension



Source: FactSet, MSCI, RIMES, Morgan Stanley Research. ROE data is monthly as of end April, 2022, and P/B data is as of May 6, 2022. Numbers are based on MSCI indices for each economy. The line of fit does not take into account the six economies of Pakistan, Hungary, Russia, Turkey, Egypt and South Africa.

Mixed signs from MS equity framework; No rush for an upgrade

We use our long-standing China equity market evaluation framework (Exhibit 12) to illustrate how the key influencing factors have evolved recently, and how their confluence could direct the index moves accordingly. The arrows in the table show the incremental dynamic shifts (improving/deteriorating) vs. the past. In general, we would like to see at least two factors exhibiting overall improvement before potentially becoming more constructive on the market.

Exhibit 12: Morgan Stanley China Equity Strategy framework – Positive policy clarification could be discounted by further earnings outlook deterioration and weakening CNY

	2018	2020 Post Covid-19	2H 2021	Mar-22	Apr-22	Post politburo meeting
1 Economic/Earnings Estimates	x	✓	Neutral	x	xx ↓	xx ↓
2 Valuation	x	✓	x	Slightly positive	Neutral ↑	Neutral
3 Liquidity	x	✓	x	Neutral	Neutral	Neutral
4 Policy Cycle	x	✓	x	Neutral/ Slightly positive	Neutral/ Slightly positive	✓ ↑
5 USDCNY trend	x	✓	Neutral	Neutral	x ↓	xx ↓
6 US/China & geopolitical tension	x	Neutral/ Slightly negative	Neutral/ Slightly negative	x	x	x
7 Regulatory	x	Neutral	x	Neutral	Neutral/ Slightly positive ↑	✓ ↑

Source: Morgan Stanley Research. Arrow in above table signals improvement/deterioration vs. prior period.

Key highlights for the 7 influential factors, and how we expect them to move, near term:

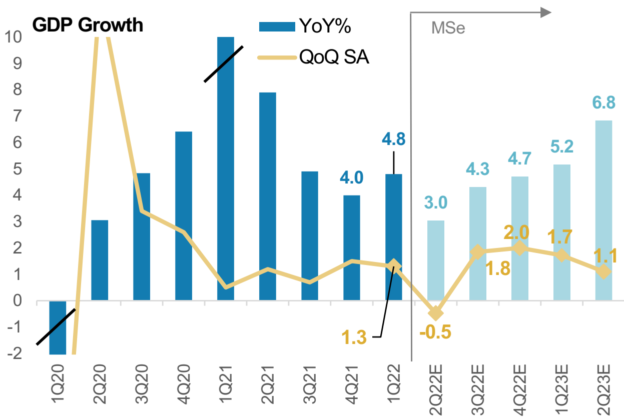
- Macro/Earnings: Negative.

More earnings estimates cuts seem necessary to reflect the macro drag from Omicron

outbreaks. Both 4Q2021 and 1Q2022 results have disappointed significantly, reflecting that the market still underestimates the magnitude of macro slowdown and the impact on corporate earnings deterioration. We expect downward revisions to continue for at least another 3-4 weeks, through May.

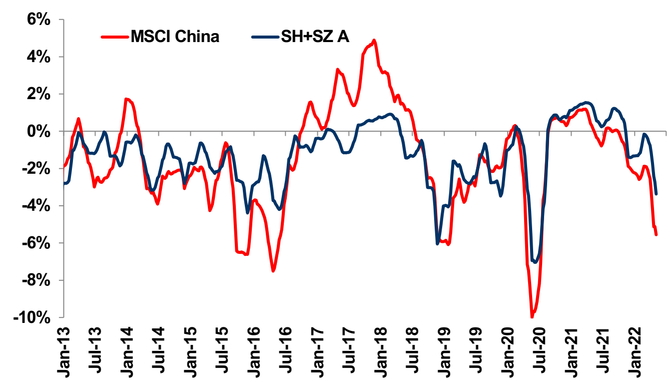
The Morgan Stanley China Economics team has recently lowered its China 2022 growth forecast, by 40bps, to 4.2%. After growing at 4.8% YoY in 1Q22, China's GDP could slip to 3.0% YoY (-0.5% QoQ SA) in 2Q22, followed by a bumpy recovery in 3Q amid subpar closed-loop production and rolling lockdowns. Acceleration in elderly vaccinations could facilitate a re-calibration in Covid policy after the Oct/Nov political reshuffle, giving way to a back-loaded recovery in 4Q and a more broad-based growth rebound to 5.7% in 2023. Sporadic lockdowns would constrain consumption, but also affect supply chains, blunting the effectiveness of policy easing and leading to a back-loaded recovery. As a result, we nudge down our 2022 earnings growth forecast to 8% and 10% for MSCI China and CSI300, respectively. We then expect a rebound in 2023 (earnings growth for MSCI China and CSI300 back to 14% and 12%, respectively), with reopening in full swing and benefitting from a low base effect.

Exhibit 13: GDP growth in China - 2Q22's growth could slip before picking up modestly in 3Q22 with full-year forecast at 4.2%



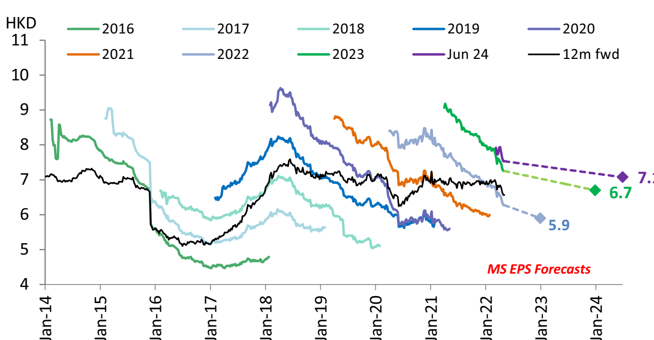
Source: NBS, Morgan Stanley Research (E) estimates.

Exhibit 14: MSCI China and A-shares consensus earnings estimate revision breadth (ERB, 3mma) – Consensus earnings estimate reductions have started to re-accelerate since March



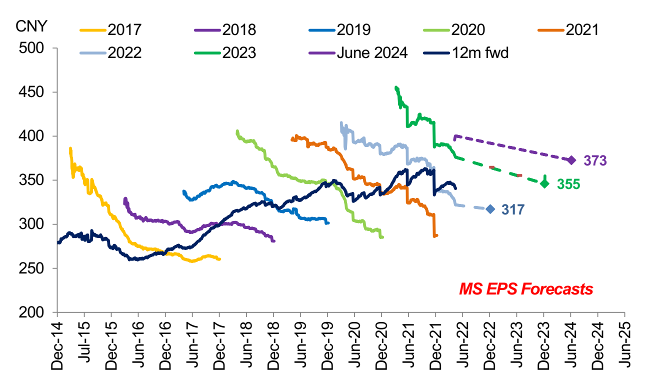
Source: MSCI, IBES, Rimes, Morgan Stanley Research. Weekly data as of May 4, 2022. Earnings Estimate Revision Breadth (ERB) = (number of upward revisions - number of downward revisions) / total number of consensus estimates.

Exhibit 15: Morgan Stanley Research's base case EPS forecasts for MSCI China for Dec-22, Dec-23 and Jun-24



Source: IBES, DataStream, Morgan Stanley Research. Weekly data as of May 5, 2022.

Exhibit 16: Morgan Stanley Research's base case EPS forecasts for CSI 300 for Dec-22, Dec-23 and Jun-24



Source: Bloomberg, Morgan Stanley Research. Weekly data as of May 6, 2022.

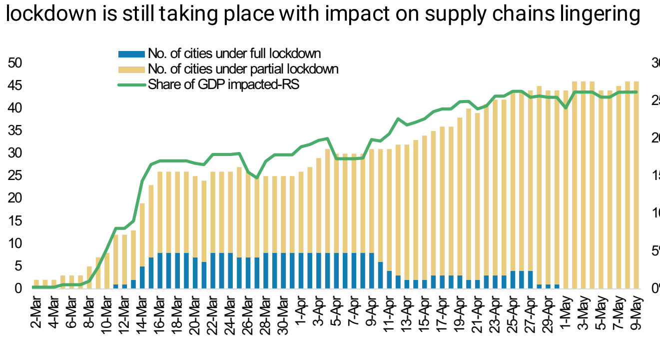
Further earnings drag from Covid-disruption continues to skew towards the downside,

as rolling lockdowns are still taking place across cities in China, amid latest government emphasis on Covid-zero. According to the MS China economics team, with 46 cities (which account for 26% of GDP and 21% of total population) still under some form of mobility restriction (versus 25 cities accounting for 18% of GDP and 13% of total population in end March) (Exhibit 17), the impact on tier-1 cities continues to linger. For example, the Chaoyang District of Beijing closed workplaces and public venues due to ongoing confirmed positive cases of Omicron in the district. Shanghai's production has been steadily resuming, with over 70% of Shanghai's 1,800 major industrial enterprises resuming work. However, recovery in capacity utilization may still lag – labour shortage could be another bottleneck, despite receding logistical headwinds, according to the Morgan Stanley China economics team. The latest channel checks by our autos team reveal that among white-listed companies in the city, capacity utilization has reached only 40-50%, so far. With President Xi reiterating the necessity of "Covid-zero" at the May 5 Politburo meeting, our economists expect supply chain headwinds to persist in coming months amid sporadic Omicron outbreaks. For more details please refer to, China Healthcare: Covid-19 China Daily Tracker.

Additional margin pressure will also come from incrementally weaker pass-through of lofty cost by manufacturers to end-consumers. Our China Economics team expects PPI to remain elevated despite moderating on a YoY basis. It would remain at 7% in 2Q22, constrained by: 1) global commodity prices staying high because of geopolitical tensions, and 2) higher freight rates and production costs stemming from domestic supply chain disruptions, particularly among downstream manufacturing sectors.

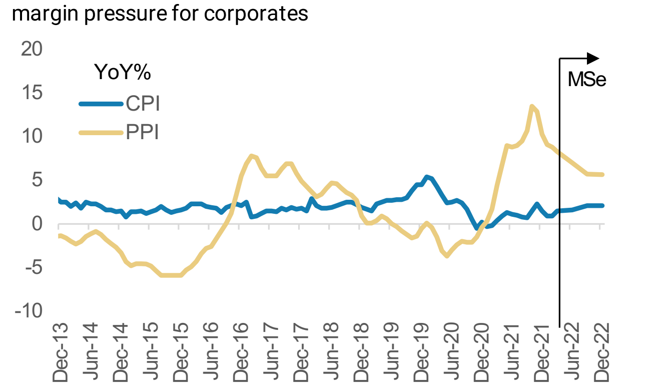
At the same time, Morgan Stanley economists expect lower CPI because of a Covid-zero drag on demand. The team has lowered its 2022 core CPI forecast by 60bps, to 1% (vs. 0.8% in 2020 and 2021), with readings in 2-3Q likely capped below 1%, before firming up mildly in 4Q, when we anticipate China would exit from Covid-zero. Therefore, the PPI/CPI gap is likely to remain sizable in coming months (Exhibit 18), which could drive margin pressure on Chinese corporates. In particular, sectors driven by domestic demand could be relatively more exposed, while export-oriented sectors could transmit higher costs to foreign importers of Chinese goods.

Exhibit 17: Number of cities under lockdown in China - 46 cities are currently under lockdown which account for 26% of GDP; rolling lockdown is still taking place with impact on supply chains lingering



Source: Government Websites, Morgan Stanley Research. Data as of May 9, 2022.

Exhibit 18: China CPI and PPI - Sizable PPI-CPI gap to stay, posing margin pressure for corporates

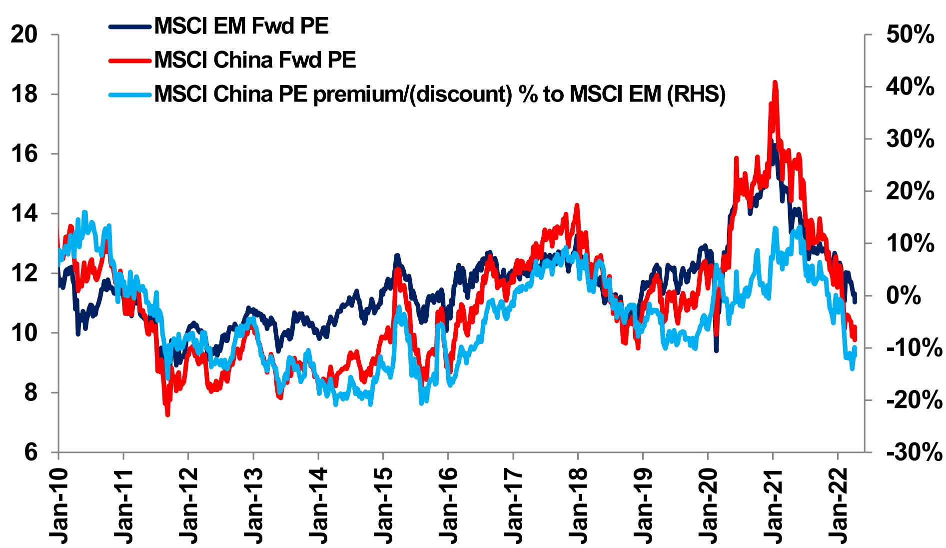


Source: NBS, Morgan Stanley Research estimates. Data as of end March, 2022 with Morgan Stanley forecasts from 2Q22 to 4Q22.

- Valuation: Neutral for now, with rerating opportunity less clear, near term. MSCI China valuation has declined by more than eight P/E points from last year's peak at 18.4x, to a 12-month forward P/E of 9.8x, a much more reasonable level. On a relative basis, MSCI China now trades at an 11% discount vs. MSCI EM in terms of 12-month forward P/E. That said, with margin pressure in the near term, and QT coming up, we do not expect any substantial re-rating in the near term, particularly amid persistent investor skepticism. Confidence is only likely to gradually recover with evidence of policy stimulus and more sustainable recovery of ROE – which could take time and be hindered by any unfavorable Covid developments.

Our new 12-month forward P/E target, at 10x for MSCI China, aims to incorporate particularly the risk-off effect from a global risk-off event, led by the US equity market. Morgan Stanley US equity strategist Michael Wilson expects a 1 P/E point derating for the S&P 500, from current consensus 12-month forward P/E 17.5x to Morgan Stanley Research estimate of 16.5x in June 2023, due to slowing macro growth on cost pressures/inflation and a hawkish Fed (read more: Global Strategy Mid-Year Outlook: The Tempest). Historically, major corrections in the US market would tend to cause global markets to move along together, as in early 2021 and 2022, amid the rapid US bond yield spike in Mar 2020, when Covid became a pandemic.

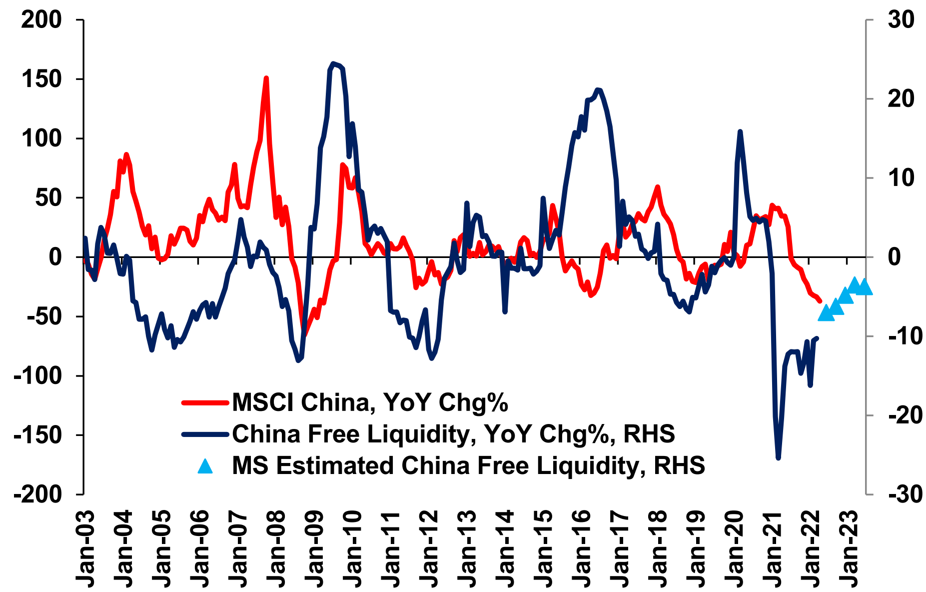
Exhibit 19: MSCI China 12-month forward P/E vs MSCI EM - MSCI China now trades at 9.8x; valuation discount relative to MSCI EM now hits 11%



Source: Datastream, MSCI, Morgan Stanley Research. Data as of May 6, 2022.

- Liquidity: Neutral. In the near term, we do not expect strong liquidity support before China's credit/monetary policy easing can be fully implemented. Our proprietary MS China free liquidity indicator has been range bound since Aug 2021, with PPI remaining elevated (Exhibit 20). Meanwhile, the significant magnitude of QT, overlaid with continuous Fed rate hikes, could trigger tighter liquidity at the global level, which could impact the Chinese market as well; the Morgan Stanley US economics team expects Fed QT to start on June 1 and phase in to the aggregate reinvestment caps set at US$95bn/month (US$60bn UST/US$35bn MBS). Therefore, in the near term, overall liquidity support could be rather limited. Policy stimulus could reach a fuller scale later rather than immediately, once the onshore Omicron situation gets under better control, which would give policymakers more room with rate cuts (20bps, per MS forecast) and RRR cuts (75bps, per MS forecast).

Exhibit 20: MS China Free Liquidity Indicator vs. MSCI China YoY return – YTD trajectory has been bumpy



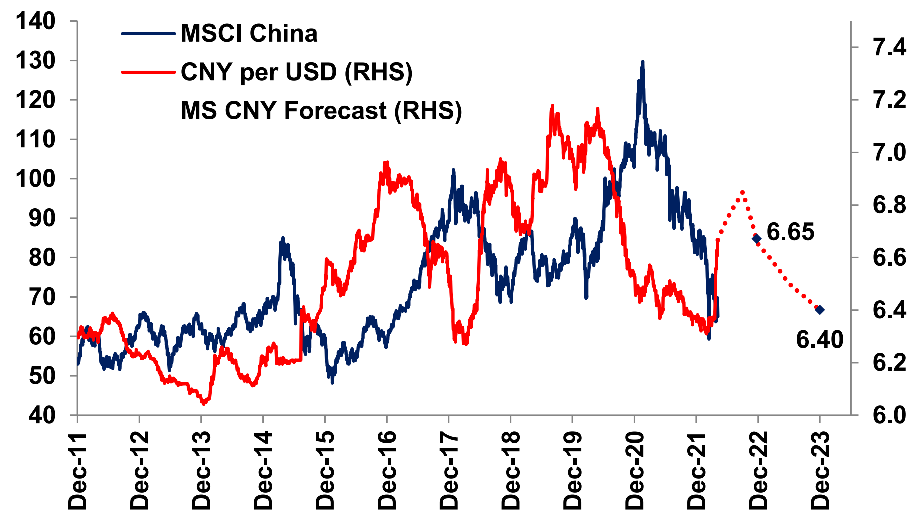
Source: MSCI, CEIC, Morgan Stanley Research estimates. MSCI China YoY change % data as of end-April 2022, and China Free Liquidity data as of end-March 2022. Free Liquidity = M1 growth less Producer price inflation less Industrial production growth. Markers represent Morgan Stanley China Economics team's estimates for 2Q22 through 2Q23.

- Policy cycle & Regulatory: Positive, but could be deterred by Covid-zero measures. As discussed in "Positive signals from Politburo meeting; however, long-term ROE trajectory remains in question," we do believe the latest policy stance sends a strong signal that the focus is shifting back to economic growth. Execution remains key, which will likely take at least a couple of months to pass through.

- FX trend: Negative in the near term. The Morgan Stanley rates and FX team continues to expect CNY to underperform in the near term as China's balance of payments turns less supportive, with the disruption to supply chains from China's Covid restrictions weighing on exports and bond market inflows turning into outflows in recent months (Exhibit 22). Given the softer economic fundamentals, the PBOC could tolerate some currency weakness in order to help support exporters and growth. With the recent USD/CNY rally, exporters, who are trend followers, may also prefer to hold more USD rather than CNY, removing a source of support for the currency (Exhibit 23). Morgan Stanley economists and FX strategists see USD/CNY trading up to 6.85 by 3Q22. In 4Q22, the team expects USD to start to weaken and China's growth outlook to improve, with the government potentially shifting towards gradual relaxation of the Covid-zero policy, spurring a USD/CNY turnaround. We see USD/CNY ending the year at 6.65 and reaching 6.50 by 2Q23.

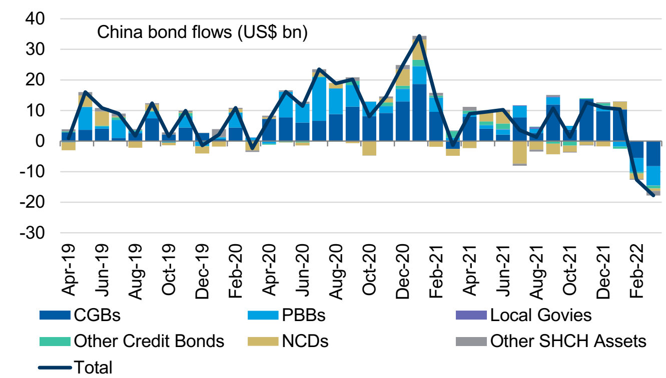
A weaker CNY against USD is generally negative for Chinese equities, as the earnings growth would look more subdued given the translational effect (Exhibit 21). The inversion trend of US/China 10-year bond yield could also discount CNY-denominated assets' attractiveness until investors are convinced by China's growth potential again.

Exhibit 21: MSCI China vs. USDCNY – MS expects CNY to weaken by 3Q22 before appreciation from 4Q22



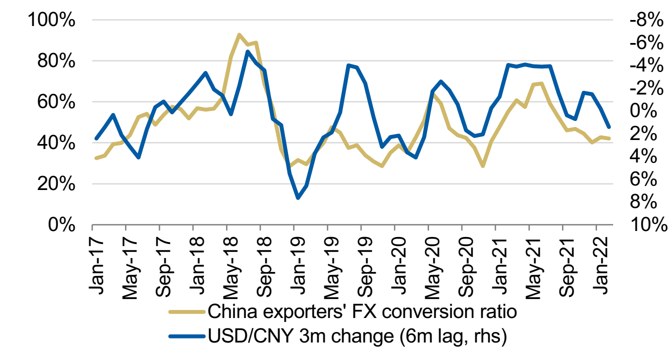
Source: CEIC, Morgan Stanley Research. Data as of May 6, 2022. MS China Economics team expects USDCNY to reach 6.65 by end-2022 and 6.4 by end-2023.

Exhibit 22: China bond flows - China's bond market has seen two consecutive months of outflows



Source: CEIC, Morgan Stanley Research. Data as of end March, 2022.

Exhibit 23: China exporter FX conversion ratio vs. USDCNY - Exporters' FX conversion moves with USD/CNY with a lag



Source: CEIC, Bloomberg, Morgan Stanley Research. Data as of end February, 2022.

- Geopolitical tension and US/China relationship: Drag to continue, with midterm elections in late 2022. We continue to expect a negative impact from the current Ukraine/Russia situation on China's ERP assessment, given investor concerns over potential geopolitical conflict areas. On the US/China relationship, we note positive progress being made on the ADR audit dispute front, while uncertainty still lingers with US domestic policy developments around tariffs, Make It In America Act (MIIA), and other non-tariff measures. Some investors may have become excited by the recent news around USTR tariff review and the possibility of the termination of certain tariffs. However, the review will not be concluded until late August, and the administration could also launch a Section 301 investigation ahead of the US midterm elections in November, as it might be difficult for the administration to lower tariffs unilaterally during the midterm election cycle.

Therefore, the overall impact around trade/non-trade and other US domestic policy moves will likely be mixed, with potentially more clarity in a few months regarding US/China audit agreement, and a finalized draft of the MIIA Act. For more details please visit, Public Policy Brief: What If? US/China Catalysts (12 Apr 2022), China Equity

Strategy: CSRC Revising Overseas Listing Confidentiality Rules (3 Apr 2022).

Exhibit 24: What could be a potential solution of US/China audit disputes – Chance for a bilateral agreement is higher with CSRC's revision to confidentiality rule

Date	CSRC comments on US/China audit dispute since 2H20
8-Aug-20	CSRC stressed dialogue with US regulators for achieving win-win results.
20-Aug-20	SRC signaled willingness to work with US regulators over audit inspections and to strengthen communication regarding the market.
5-Dec-21	CSRC responded that it respects Chinese companies' independent choice of overseas listing venues in compliance with relevant laws and regulations.
24-Dec-21	CSRC issued the Provisions of the State Council on the Administration of Overseas Securities Offering and Listing by Domestic Companies, in order to improve the regulatory system for overseas listings.
18-Jan-22	CSRC pledged at its annual work conference that it would strengthen China-US cooperation on audit regulation in the capital markets, and would move faster to implement policies and regulations related to the overseas listing of companies in 2022.
11-Mar-22	CSRC stated in its press release that positive progress has been achieved recently on resolving the audit dispute issue, through continuous communication and dialogue among CSRC, China's Ministry of Finance and the US PCAOB.
2-Apr-22	CSRC published consultation paper on revisions to "Provisions on Strengthening Confidentiality and Archives Administration of Overseas Securities Offering and Listing by Domestic Companies", signaling China's proactive stance in resolving the audit dispute.

Source: Morgan Stanley Research.

Exhibit 25: Latest on US/China tension – Three US domestic policy events in 2022 and market implications

Catalyst	Fundamental Impacts	Market Impacts
Section 301 Investigation	• Drag on bilateral trade of affected sectors • Discourage manufacturing capex	↗ **USD/CNY:** potential short term spike, with downside risk to CNY if PBOC decides not to intervene ↘ **China Equities:** further downside risks to already cautious view as broad sentiment dampens; potential 0.5pt P/E derating for offshore China equity market. Healthcare, IT, and Consumer likely to be hit more given US revenue exposure.
Make It in America Act	• China would continue to promote "domestic economic circulation" • Potential downside to China FDI and export competitiveness over the long term if other countries enact similar legislation • Upside for MNCs with less market share in China, with downside risk if provisions are included and/or reconciliation not reached	• **USD/CNY:** muted impact • **China Equities**: impact dependent on inclusion of AHFCAA provisions in competition bill and resolution of ADR audit dispute.
Escalation of Non-Tariff Barriers	• Reciprocal efforts to accelerate self-sufficiency in software and semiconductors in China • Continued regulatory reform of equity market to attract capital inflows	↗ **USD/CNY:** could move higher if China responds with similar actions including the launch of an 'unreliable entities list,' downside risk to CNY due to concerns around foreign companies' FDI into China ↘ **China Equities**: downside risks to already cautious view given a more negative impact than direct tariff hikes; sentiment dampening and more prolonged valuation de-rating, and potential index removal, though A-shares are better positioned given higher exposure to domestic growth opportunities

Source: China State Council, US Commerce Department, US SEC, White House, Office of the USTR, US FCC, US Treasury, Morgan Stanley Research.

Path to a better place/signs we search for

As we discussed, we believe that current market dynamics could represent the final leg of an extended bear market for Chinese equities, but any urgency to upgrade our outlook should be curbed, as we believe near-term market volatility could remain heightened because of uncertainty around Omicron, and curbing of easing policies as a result, as well as global events related to geopolitical conflict and central bank policy. To translate the sentiment lifting effect from the April 29 Politburo meeting into a more sustained equity market recovery, we would need a sustainable recovery path in the macroeconomic picture and the supply chain from Omicron disruption, removal/reduction of regulatory reset overhang, a real inflection in earnings growth, and/or equity market liquidity improvement. Therefore, we are closely monitoring:

1) recovery speed and, more importantly, sustainability of the supply chain, particularly any concrete measures to prevent the disruption seen since March from happening again; indication of an exit strategy from Covid-zero would, in our view, be a major plus;

2) execution following the Politburo announcements around positive guidance for regulatory reset wrap-up and private enterprises;

3) stabilization effort for the property sector, including relaxation of escrow funds for developers;

4) stepping-up of domestic easing measures on both the monetary and policy fronts (timing and magnitude could be contingent on the Omicron situation), particularly improved credit access by private companies. In particular, we would monitor the reaction in the onshore bond market, which could serve as a proxy for immediate policy follow-throughs;

5) waning of discounting effect of liquidity and risk sentiment from global geopolitical tensions and upcoming Fed quantitative tightening, and stabilization of CNY weakness;

6) US/China audit dispute agreement and resumption of offshore IPOs for Chinese companies, particularly in the US market.

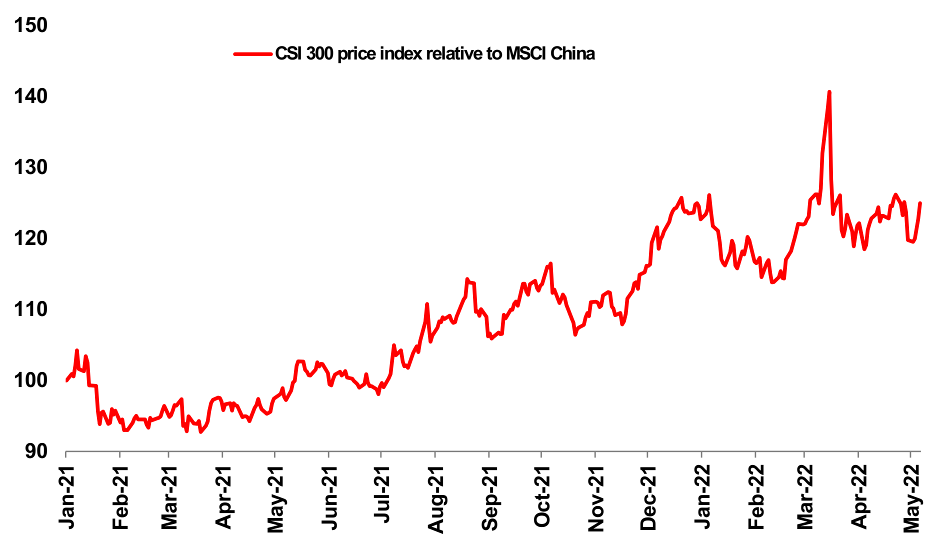
China A-share market: Stay overweight relative to offshore, in light of easing step-up

CSI300 outperforming MSCI China by 14ppt since we published our 2022 outlook

We have been recommending that investors overweight China A-shares within their broad Chinese equity portfolio. As of May 6, 2022 close, CSI300 has actually outperformed MSCI China by 14ppt since Nov 15, 2021 when we published our 2022 new year outlook (Exhibit 26). YTD, the relative performance between the two indices has been largely on par, however, with CSI300 outperforming substantially until mid-March, with MSCI China then catching up.

The inflection of the relative performance in March is closely linked to two events, in our view: 1) The speech delivered by Vice Premier Liu He on March 16th 2022, which had served as a quite positive boost to offshore internet/ADR companies, as he had specifically mentioned that positive progress has been achieved on the US China audit dispute front, with a detailed resolution being worked on, while support will be provided for all corporates seeking overseas listings (China Equity Strategy: Policymakers Clarifying Stance – Positive on Sentiment, and More Signs to Watch (16 Mar 2022)). 2) An unexpected Omicron outbreak onshore, with sentiment impact particularly skewed towards onshore-based investors, who constitute the majority of the investor base for the A-share market.

Exhibit 26: CSI 300 relative performance vs MSCI China – CSI 300 has outperformed MSCI China by 14ppt since our last outlook update on 15 Nov 2021



Source: Datastream, MSCI, Morgan Stanley Research. Data as of May 6, 2022.

Stay overweight A-shares vs. offshore China market; outperformance likely to be back-loaded

We continue to believe that the A-share market (as proxied by CSI300) should retain its outperformance vs. the offshore market (proxied by MSCI China) going into 2H2022, particularly for the following reasons:

More direct beneficiary of onshore easing measure stepping-up: Historical analysis of past easing cycles suggests that the A-share market has tended to outperform the offshore indices by mid-single-digit percentage points, post major easing measures, such as RRR cuts and rate cuts (China Equity Strategy: History Recap: Chinese Equity Performance Post RRR Cuts (13 Jul 2021); China Equity Strategy: Reiterate OW A-Shares Upon PBOC Rate Cut Move (17 Jan 2022)), as illustrated in Exhibit 27 and Exhibit 28.

Exhibit 27: Chinese equity indices return post prior PBOC announcements of RRR cuts* since 2018 – A-share market has reacted much more positively, historically, within six months of RRR cut announcements vs. offshore indices

RRR cut type	RRR cut annoucement date	Market performance post RRR cut announcements (1-month)					Market performance post RRR cut announcements (3-month)					Market performance post RRR cut announcements (6-month)				
		MSCI China	CSI 300	CSI 500	Hang Seng Index	HSCEI	MSCI China	CSI 300	CSI 500	Hang Seng Index	HSCEI	MSCI China	CSI 300	CSI 500	Hang Seng Index	HSCEI
Targeted	1/17/2018	(3.9%)	(6.6%)	(8.2%)	(4.6%)	(4.7%)	(4.0%)	(7.3%)	(2.9%)	(3.4%)	(4.2%)	(12.3%)	(20.8%)	(18.3%)	(11.7%)	(16.8%)
Broad-based	4/17/2018	4.2%	4.7%	2.2%	3.6%	4.5%	(4.0%)	(7.5%)	(12.8%)	(4.6%)	(9.0%)	(13.7%)	(8.3%)	(18.5%)	(9.8%)	(9.6%)
Targeted	6/20/2018	(6.8%)	(5.6%)	(0.8%)	(5.3%)	(8.1%)	(17.7%)	(11.9%)	(9.7%)	(11.3%)	(11.0%)	(16.6%)	(10.5%)	(13.4%)	(9.7%)	(6.5%)
Broad-based	10/7/2018	1.6%	(0.0%)	(4.5%)	1.1%	2.8%	(4.6%)	(8.5%)	(10.3%)	(2.7%)	(3.9%)	12.4%	16.5%	21.0%	11.1%	10.8%
Broad-based	1/4/2019	12.5%	7.0%	2.0%	9.0%	10.3%	18.8%	27.6%	31.7%	13.4%	13.5%	12.0%	26.3%	19.2%	11.1%	8.9%
Targeted	5/7/2019	(10.8%)	(3.3%)	(3.6%)	(8.9%)	(8.2%)	(4.5%)	4.0%	(1.0%)	(4.1%)	(3.9%)	(7.1%)	4.7%	0.6%	(8.8%)	(6.5%)
Broad-based	9/6/2019	(3.2%)	(3.4%)	(4.1%)	(3.3%)	(2.7%)	2.1%	(3.0%)	(5.0%)	(1.3%)	(1.2%)	10.7%	5.1%	12.2%	2.3%	3.5%
Broad-based	1/1/2020	(2.0%)	(2.3%)	2.1%	(3.7%)	(4.9%)	(11.2%)	(9.1%)	(1.0%)	(16.5%)	(14.7%)	1.5%	(1.9%)	8.9%	(13.2%)	(11.3%)
Targeted	3/13/2020	1.5%	(3.2%)	(4.6%)	1.1%	1.7%	10.9%	2.7%	2.3%	3.1%	4.3%	31.6%	24.4%	22.6%	5.8%	5.5%
Targeted	4/3/2020	6.5%	5.4%	4.8%	6.1%	5.8%	16.2%	11.5%	13.4%	5.7%	3.8%	29.9%	27.6%	26.7%	5.2%	3.3%
Broad-based	7/9/2021	(7.5%)	(2.9%)	2.0%	(4.3%)	(6.2%)	(12.5%)	(4.0%)	4.4%	(10.1%)	(11.7%)	(18.6%)	(2.9%)	7.0%	(15.1%)	(17.0%)
Broad-based	12/6/2021	(0.5%)	1.0%	1.6%	(0.3%)	(1.0%)	(6.6%)	(6.4%)	(5.3%)	(2.7%)	(3.0%)					
Broad-based	4/15/2022															
Average return of broad RRR cut announcements:		**0.7%**	**0.6%**	**0.2%**	**0.3%**	**0.4%**	**(2.6%)**	**(1.6%)**	**0.2%**	**(3.5%)**	**(4.3%)**	**0.7%**	**5.8%**	**8.3%**	**(2.2%)**	**(2.5%)**
Average return of targeted RRR cut announcements:		**(2.7%)**	**(2.7%)**	**(2.5%)**	**(2.3%)**	**(2.7%)**	**0.2%**	**(0.2%)**	**0.4%**	**(2.0%)**	**(2.2%)**	**5.1%**	**5.1%**	**3.7%**	**(3.8%)**	**(4.2%)**
Average return of total RRR cut announcements:		**(0.7%)**	**(0.8%)**	**(0.9%)**	**(0.8%)**	**(0.9%)**	**(1.4%)**	**(1.0%)**	**0.3%**	**(2.9%)**	**(3.4%)**	**2.7%**	**5.5%**	**6.2%**	**(3.0%)**	**(3.2%)**

Source: CEIC, Reuters.com, PBOC, State Council, Xinhua Net, MSCI, Datastream, Morgan Stanley Research. Data as of May 6, 2022. *RRR cuts, in both broad-based and targeted form, by PBOC since 2018 are as follows: 1: (Jan 17, 2018) Targeted RRR cut for inclusive finance; 2: (Apr 17, 2018) Broad-based RRR cut by 100bps except policy banks; 3: (Jun 20, 2018) Targeted RRR cuts by 50bps to support small businesses; 4: (Oct 7, 2018) Broad-based RRR cut by 100bps for all banks; 5: (Jan 4, 2019) Broad-based RRR cut by 100bps in two phases with 50bps cut for each; 6: (May 7, 2019) Targeted RRR cut for some small and medium-sized banks; 7: (Sept 6, 2019) Broad-based RRR cut by 50bps for all banks; An extra 100bps for city commercial banks in two phases with 50bps cut for each; 8: (Jan 1, 2020) Broad-based RRR cut by 50bps for all banks; 9: (Mar 13, 2020) Targeted 50-100bps RRR cut for eligible banks passing inclusive finance assessment and an extra 100bps for eligible joint-stock commercial banks; 10: (Apr 3, 2020) Targeted 100bps RRR cut for rural banks and eligible city commercial banks in two phases with 50bps cut for each; 11: (Jul 9, 2021) Broad-based RRR cut by 50bps for all banks; 12: (Dec 6, 2021) Broad-based RRR cut by 50bps for all banks; 13: (Apr 15, 2022) Broad-based RRR cut by 25bps for all banks and an extra 25bps for small commercial banks and selected rural lenders.

Exhibit 28: Chinese equity indices return post prior announcements of rate cuts* since 2012 – A-share market has reacted much more positively historically within 6 months of rate cut announcements vs. offshore indices

Rate cut type	Annoucement date	Market performance post rate cut announcements (1-month)					Market performance post rate cut announcements (3-month)					Market performance post rate cut announcements (6-month)				
		MSCI China	CSI 300	CSI 500	Hang Seng Index	HSCEI	MSCI China	CSI 300	CSI 500	Hang Seng Index	HSCEI	MSCI China	CSI 300	CSI 500	Hang Seng Index	HSCEI
Benchmark lending rate & deposit rate	6/7/2012	3.8%	(4.4%)	(4.5%)	6.1%	2.4%	0.5%	(13.0%)	(12.6%)	4.7%	(1.4%)	12.4%	(14.3%)	(16.4%)	16.4%	10.8%
Benchmark lending rate & deposit rate	7/5/2012	(1.1%)	(3.9%)	(6.5%)	(0.6%)	(0.3%)	1.5%	(7.4%)	(8.1%)	4.8%	0.7%	14.6%	(1.9%)	(9.0%)	14.4%	17.0%
Benchmark lending rate & deposit rate	11/21/2014	1.9%	31.0%	9.8%	(1.4%)	9.1%	9.4%	34.3%	14.7%	5.3%	14.1%	28.9%	76.4%	63.1%	17.7%	34.5%
Benchmark lending rate & deposit rate	2/28/2015	(0.9%)	11.2%	18.9%	(1.4%)	(2.4%)	17.4%	38.6%	62.5%	12.8%	18.4%	(6.2%)	14.0%	43.3%	(3.4%)	(9.2%)
Benchmark lending rate & deposit rate	5/10/2015	(2.2%)	14.7%	35.9%	(1.2%)	(1.0%)	(18.1%)	(16.3%)	(5.8%)	(10.7%)	(20.8%)	(21.1%)	(21.7%)	(13.0%)	(16.0%)	(23.5%)
Benchmark lending rate & deposit rate	6/27/2015	(8.6%)	(3.7%)	(7.2%)	(5.8%)	(10.8%)	(20.5%)	(25.0%)	(33.5%)	(17.8%)	(23.4%)	(23.1%)	(16.8%)	(19.7%)	(19.5%)	(28.9%)
Benchmark lending rate & deposit rate	8/25/2015	4.3%	9.7%	(2.9%)	1.8%	3.4%	7.1%	23.5%	18.0%	4.0%	5.9%	(11.3%)	(2.6%)	(12.6%)	(9.9%)	(15.3%)
Benchmark lending rate & deposit rate	10/23/2015	(2.0%)	5.7%	9.4%	(1.7%)	(4.1%)	(19.5%)	(12.7%)	(17.4%)	(15.7%)	(23.3%)	(12.8%)	(10.8%)	(13.6%)	(12.0%)	(19.0%)
LPR	8/20/2019	3.2%	2.7%	5.5%	2.1%	3.6%	5.6%	3.1%	0.2%	3.2%	5.5%	10.8%	(0.1%)	2.5%	1.7%	3.0%
LPR	9/20/2019	(0.9%)	(1.7%)	(4.7%)	1.1%	1.6%	6.5%	0.8%	(2.5%)	4.7%	4.5%	7.6%	5.2%	10.7%	(1.1%)	0.8%
MLF	11/5/2019	(1.9%)	(3.8%)	(2.0%)	(4.7%)	(4.8%)	5.6%	0.0%	7.0%	1.0%	0.9%	(1.7%)	(4.9%)	6.3%	(14.1%)	(11.6%)
7-day reverse repo rate & LPR	11/18/2019	5.1%	2.0%	5.6%	3.1%	2.1%	7.4%	0.2%	10.1%	2.1%	0.9%	(1.0%)	0.1%	9.4%	(11.5%)	(9.1%)
14-day reverse repo rate	12/18/2019	5.0%	3.3%	5.6%	3.2%	2.5%	(4.8%)	(0.1%)	6.8%	(9.5%)	(8.7%)	0.4%	(1.2%)	6.4%	(12.8%)	(9.6%)
7-day reverse repo rate	2/3/2020	2.9%	10.3%	15.2%	(0.2%)	2.1%	(1.3%)	3.6%	7.2%	(7.9%)	(3.8%)	17.4%	26.9%	32.9%	(4.9%)	0.3%
MLF & LPR	2/17/2020	(16.9%)	(8.6%)	(7.0%)	(17.5%)	(15.8%)	(5.7%)	(2.9%)	(1.8%)	(12.0%)	(8.8%)	10.5%	17.0%	20.5%	(12.5%)	(8.4%)
7-day reverse repo rate	3/29/2020	4.6%	2.3%	2.7%	1.5%	1.6%	15.6%	10.5%	12.6%	4.9%	4.9%	27.4%	24.7%	22.9%	4.3%	2.6%
MLF & LPR	4/15/2020	2.8%	4.5%	5.1%	0.1%	1.1%	24.0%	25.7%	24.0%	8.2%	10.5%	22.5%	20.8%	17.5%	(2.8%)	(3.4%)
LPR	12/20/2021	4.1%	(2.3%)	(0.5%)	6.5%	5.2%	(22.3%)	(14.5%)	(12.1%)	(14.1%)	(18.5%)					
MLF & LPR	1/17/2022	(1.6%)	(4.5%)	(6.5%)	1.4%	1.8%	(17.8%)	(14.0%)	(15.8%)	(12.4%)	(14.8%)					
Average return of LPR cut (or equivalent) announcements:		**0.1%**	**5.4%**	**4.8%**	**0.5%**	**0.6%**	**-2.9%**	**1.0%**	**0.3%**	**-1.7%**	**-3.5%**	**0.0%**	**2.7%**	**3.5%**	**-1.2%**	**-3.0%**
Average return of other types of rate cut announcements:		**0.0%**	**0.7%**	**2.3%**	**-1.6%**	**-1.2%**	**2.9%**	**2.9%**	**6.3%**	**-3.2%**	**-2.4%**	**10.8%**	**11.9%**	**16.6%**	**-7.8%**	**-5.6%**
Average return of all rate cut announcements:		**0.1%**	**3.4%**	**3.8%**	**-0.4%**	**-0.1%**	**-0.5%**	**1.8%**	**2.8%**	**-2.3%**	**-3.0%**	**4.4%**	**6.5%**	**8.9%**	**-3.9%**	**-4.1%**

Source: CEIC, Reuters.com, PBOC, State Council, Xinhua Net, MSCI, Datastream, Morgan Stanley Research. Data as of May 6, 2022. *rate cuts, by PBOC since 2012 as follows: 1: (Jun 7, 2012) one-year benchmark lending rate and one-year deposit rate both cut by 25bps; 2: (July 5, 2012) one-year benchmark lending rate cut by 31bps and one-year deposit rate cut by 25bps; 3: (Nov 21, 2014) one-year benchmark lending rate cut by 40bps and one-year deposit rate cut by 25bps; 4: (Feb 28, 2015) one-year benchmark lending rate and one-year deposit rate both cut by 25bps; 5: (May 10, 2015) one-year benchmark lending rate and one-year deposit rate both cut by 25bps; 6: (June 27, 2015) one-year benchmark lending rate and one-year deposit rate both cut by 25bps; 7: (August 25, 2015) one-year benchmark lending rate and one-year deposit rate both cut by 25bps; 8: (Oct 23, 2015) one-year benchmark lending rate and one-year deposit rate both cut by 25bps; 9: (Aug 20, 2019) launch of LPR mechanism with inception 1-year and 5-year LPR 10bps and 5bps higher than prior corresponding benchmark lending rate respectively; 10: (Sep 20, 2019) 1-year LPR was cut by 5bps; 11: (Nov 5, 2019) MLF rate was cut by 5bps; 12: (Nov 18, 2019) 7-day reverse repo rate lowered by 5bps & (Nov 20, 2019) 1-year and 5-year LPR both were cut by 5bps; 13: (Dec 18, 2019) 14-day reverse repo rate lowered by 5bps; 14: (Feb 3, 2020) 7-day reverse repo rate lowered by 10bps; 15: (Feb 17, 2020) MLF rate was cut by 10bps & (Feb 20, 2020) 1-year LPR was cut by 10bps and 5-year LPR cut by 5bps; 16: (Mar 29, 2020) 7-day reverse repo rate lowered by 20bps; 17: (Apr 15, 2020) MLF rate was cut by 20bps & (Apr 20, 2020) 1-year LPR was cut by 20bps and 5-year LPR cut by 10bps; 18: (Dec 20, 2021) 1-year LPR was cut by 5 bps; 19: (Jan 17, 2022) 1-year MLF rate was cut by 10 bps & (20 Jan, 2022) 1-year LPR was cut by 10bps and 5-year LPR cut by 5bps. Note that LPR cut (or equivalent) refers to benchmark lending rate & deposit rate cut or LPR cut; other types of rate cut refers to MLF cut, 7-day reverse repo rate cut, 14-day reverse repo rate cut, or any combination of these types of rate cut with subsequent LPR rate cut. Some events involved two types of rate cuts due to the proximity of their announcement dates.

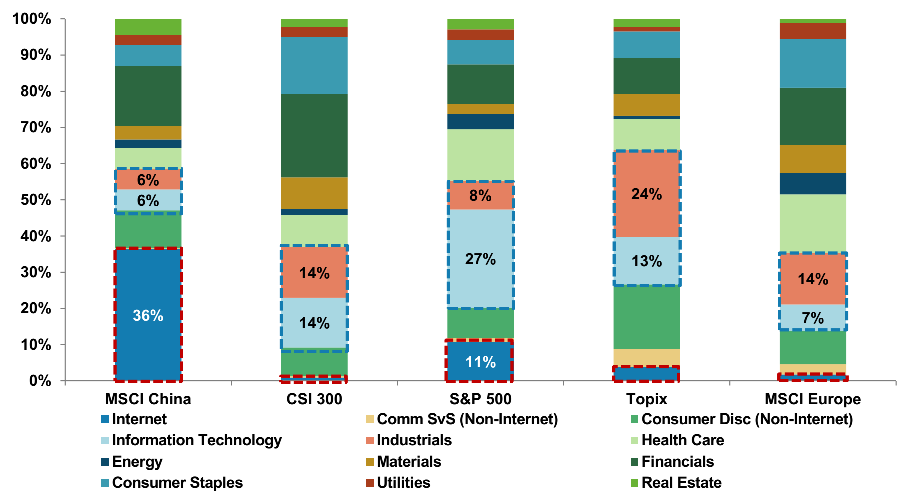
A-share market less sensitive to near-term USDCNY weakness: As discussed earlier, we expect further depreciation of USDCNY, to around 6.85 as of end 3Q22, with pressure from fund outflows, supply chain disruptions and potential slower export growth and less exporter conversion activities. Earnings for the offshore indices would appear even less attractive given the translational impact for offshore investors, while the A-share market should remain relatively less sensitive to the currency moves, given that it is not entirely connected with the global capital market, and that domestic investors have relatively fewer investment vehicles to choose from.

Better alignment with long-term thematic opportunities: We have been long holding the view that the next generation of structural investment opportunities would come from the categories/sectors better aligned with Chinese top-down policy initiatives around "sustainable growth" under the new regulatory framework. Such sustainability initiatives involve:

- National security on the data and cyber security front, as well as technology independence: software, tech hardware, semis
- Environmental sustainability: High-end manufacturing, green economy, alternative energy, EV supply chains
- Social stability & common prosperity: mass-market catering for native consumer brands

Therefore, Information Technology and Industrials, as we believe, are structurally better aligned with national growth strategy, and should enjoy long-term top-down policy support as well as faster growth vs. other industries. IT (Tech Hardware, software, semi) fits well with the prioritization of data/cyber-security and technology self-sufficiency, while high-end manufacturing, automation, green economy related machinery and equipment within Industrials cater to the pressing need for sustainable growth in light of the aging demographic and China's commitment to carbon neutrality by 2060. Compared to offshore, which has been overly concentrated in the Internet sectors (36% index weight of MSCI China as of end April 2022, coming down from 47% at market peak back in Feb 2021), CSI300's current exposure to IT and Industrials together is at 28%, vs. MSCI China's 12%. This suggests that the A-share market hosts a lot more segment and single stock opportunities that could benefit from this medium/long-term growth theme (Exhibit 29).

Exhibit 29: Sector mix of major equity indices – CSI300 has very limited exposure to internet vs MSCI China's 36%, and its exposure to IT and Industrials, collectively, is 28% vs MSCI China's 12%



Source: FactSet, Datastream, Morgan Stanley Research. Data as of end April 2022. *Internet includes Media & Entertainment under GICS industry group and Internet & Direct Marketing Retail under GICS industry.

Official launch of personal pension scheme to support long-term institutional participation: The State Council issued 'Opinions on Private Pension Development' on April 21, signaling the official launch of the personal pension scheme, the Third Pillar of China's retirement fund system. It is an account-based scheme that allows residents to voluntarily purchase a variety of financial products with tax benefits. Contributions are capped at Rmb12K per annum, and benefits will be paid out when the individual reaches retirement age. Banks, insurers, wealth management and fund companies can all participate in this scheme as product providers, with certain regulatory approvals.

This development is well within our expectation – recall that, in our 2022 new year outlook, we had noted that Chinese policymakers had shown unprecedented interest in expediting the development of a Third Pillar private pension, and we were expecting something to occur within 2022. MS China insurance team estimates it makes up only 1-2% of total household wealth (predominantly in the form of bank deposits and properties still) – vs. 30%+ for some developed markets. The team also estimates this newly announced tax support could at least encourage current taxpayers to start saving for their retirement with a potential AUM of ~Rmb1trn (assuming there are ~100mn taxpayers). Of course not all of this money will get allocated immediately, or all allocated to equities, but it does mark the start of a long-term institutional inflow source, which should further improve the A-share market investment environment and dynamics.

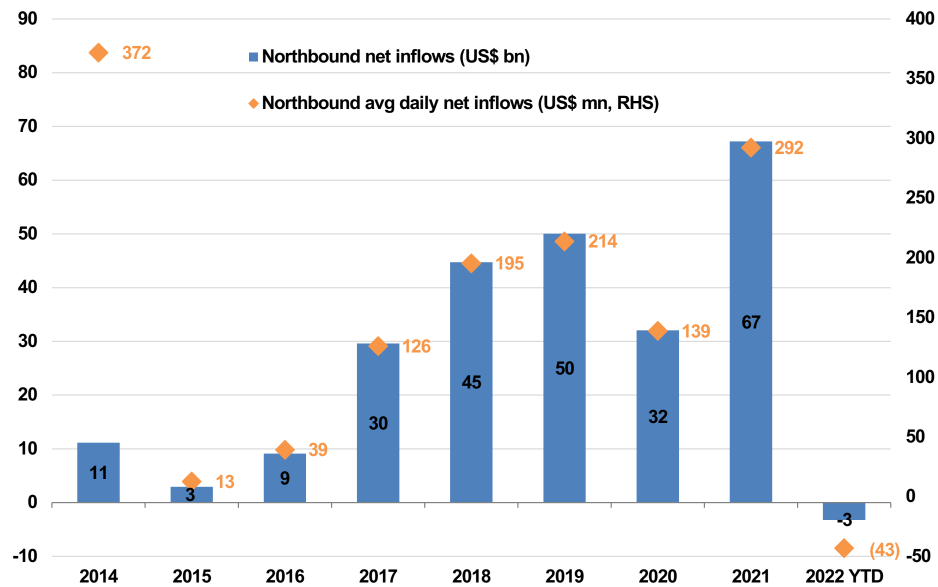
Outperformance of A-share market vs. offshore could be more back-loaded: This is because our view is based on the conviction that policymakers will step up easing measures significantly, which should directly benefit the A-share market more than it does the offshore market. However, we do believe that the timing and magnitude of any such potential easing actions would be contingent on onshore authorities' handling of the current Omicron situation - i.e., those actions would be curbed when stringent social distancing/lockdown measures are still in place. Our analysis of historical easing events shows that, usually, A-share outperformance tends to advance more, approximately one month after the announcement/action. We therefore would advise more patience with any such onshore vs. offshore strategy, and would expect better results potentially in/after summer.

Addressing investor concerns – Is global investors' interest in A-shares declining?

We can understand such concerns, as the Northbound Stock Connect channel, being arguably the easiest channel to check foreign in/outflows for the A-share market, has experienced significant outflows in 2022, so far (Exhibit 30). YTD, there has been a net outflow of US$3bn, implying an average daily outflow of US$43mn, which seems high, vs. an average daily inflow in the range of US$130 - 300mn for the past 5 years (2017-2021).

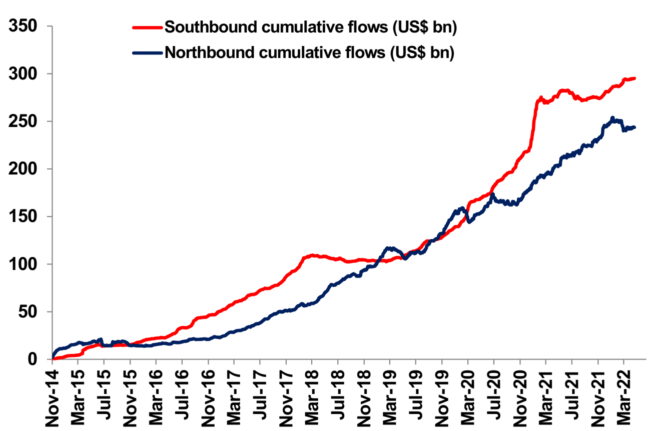
However, we would not be too perturbed by these outflows, as we believe they are more likely to be temporary rather than permanent, and global investors' interest as well as net positions in A-shares have not shown concrete signs of reduction. Exhibit 31 shows the long-term cumulative trend of Northbound and Southbound flows. The total net outflow for the current cycle had lasted for 37 trading days (27 Jan 2022 - 25 Mar 2022), with a total amount of US$13.6bn. This latest outflow episode is the second largest in Stock Connect Northbound history so far, in dollar terms, second to the episode in Feb/Mar 2020 (US$15.4bn in total) triggered by the global outbreak of Covid. In duration terms, it ranks as No. 3, compared to the longest streak of outflow period in Jul - Sep 2020 (57 trading days in total) as triggered by profit taking post the A-share bull run and the second-longest during March - May 2019 lasting for 54 trading days. Moreover, these episodes of outflows have proven to be more transitory than permanent, while the latest outflow in Feb and Mar also seems to have stopped. Inflows have resumed since Mar 26, 2022, with cumulative inflows of US$3.5bn, so far. Meanwhile, foreign ownership as a percentage of A-share market capitalization has largely stabilized, after a temporary dip in late 2021 (Exhibit 32).

Exhibit 30: Northbound annual net inflows and average daily net inflows since Stock Connect launch – 2022 YTD net outflows hit US$3bn



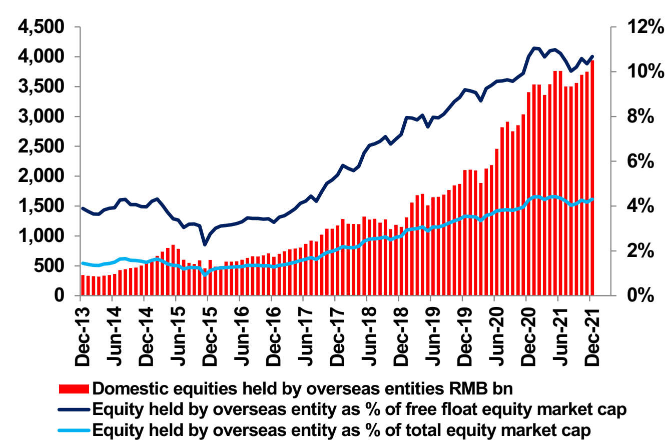
Source: CEIC, Shanghai Stock Exchange, Shenzhen Stock Exchange, HKEX, Morgan Stanley Research. Data as of May 6, 2022.

Exhibit 31: Northbound and Southbound cumulative flows since Stock Connect launch – YTD Southbound momentum has remained resilient, and recent notable Northbound outflows have stabilized since late March



Source: CEIC, Morgan Stanley Research. Data as of May 6, 2022.

Exhibit 32: Foreign ownership of A-shares – 10.7% of total free float market cap as of end-4Q21

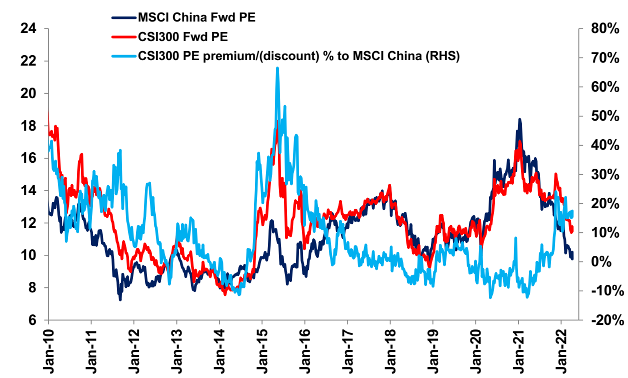


Source: CEIC, WIND, Bloomberg, FactSet, Morgan Stanley Research. Data as of end-4Q 2021.

Addressing investor concerns – Is the A-share market too expensive?

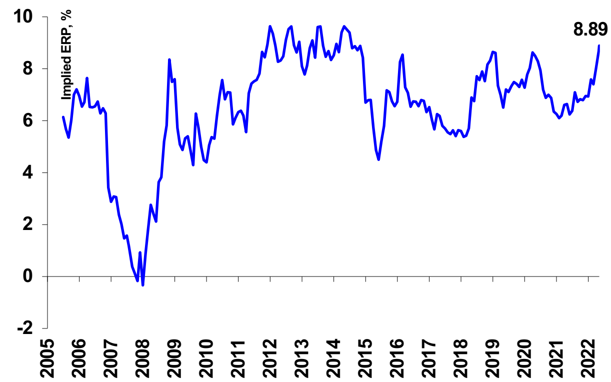
CSI300 currently trades at 11.5x consensus 12-month forward P/E – a 17% premium vs. MSCI China's consensus P/E at 9.8x (as of May 6, 2022). This premium level does sit at the high-end of the relative valuation history for the past five years. That said, CSI300 as an equity index has also gone through composition rebalancing, with the weight of growth stocks increasing over time, i.e., the recent rebalancing event in Dec 2021, which included large-cap growth stocks, such as CATL and Mindray, in the index for the first time (Exhibit 33).

Exhibit 33: 12-month forward P/E CSI 300 vs. MSCI China – Relative valuation premium of A-shares vs. offshore equities at 17%



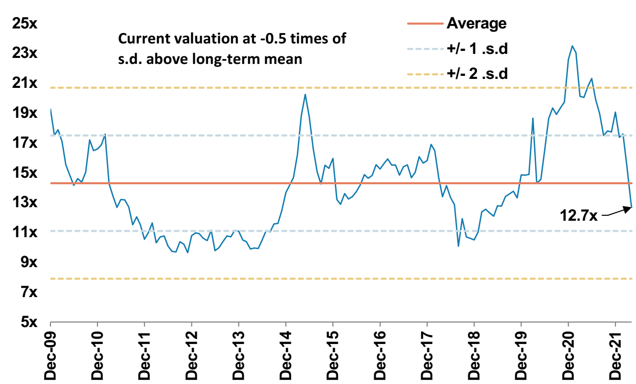
Source: Datastream, Bloomberg, MSCI, I/B/E/S, Morgan Stanley Research. Data as of May 6, 2022.

Exhibit 34: Shanghai Composite Index Implied Equity Risk Premium – Current level approaching historical peak



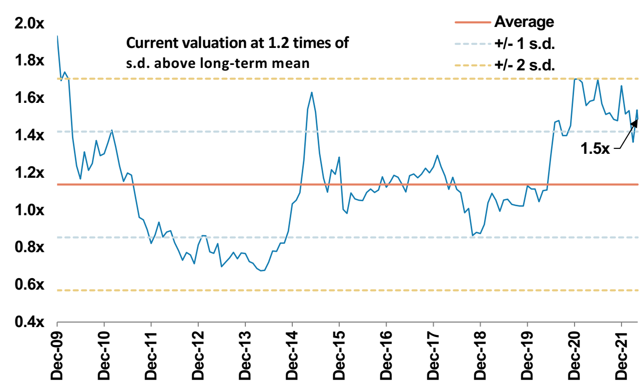
Source: FactSet, Bloomberg, IBES, Morgan Stanley Research. Data as of May 6, 2022.

Exhibit 35: CSI 300 EV/EBITDA (ex-Financials and REITs) – Current level is 0.5 SD below its long-term average



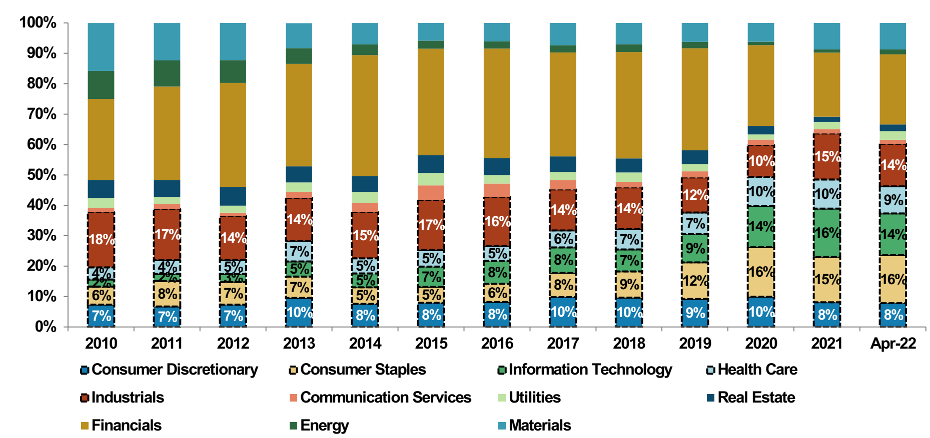
Source: MSCI, RIMES, FactSet, Worldscope, Morgan Stanley Research. Data as of May 6, 2022. OveSall valuation is derived based on harmonic mean (weighted by free-float market cap) of the valuation of all constituents ex-Financials and REITs.

Exhibit 36: CSI 300 P/Sales (ex-Financials and REITs) – Current level is still 1.2 SD above its long-term average



Source: MSCI, RIMES, Factset, Worldscope, Morgan Stanley Research. Data as of May 6, 2022. Overall valuation is derived based on harmonic mean (weighted by free-float market cap) of the valuation of all constituents ex-Financials and REITs.

Exhibit 37: CSI 300 sector-level index weight breakdown – The representation of Consumer Discretionary+Staples, IT, Health Care and Industrials have been rising over time, particularly in end-2020



Source: Datastream, FactSet, China Securities Index Company, Morgan Stanley Research. Data as of each year-end in 2010-2021, except as of end April 2022.

We recommend Morgan Stanley A-share thematic stock-picking to leverage the structural opportunities

We have long been recommending a thematic stock-picking approach in the A-share market. Such an approach identifies the fast-growing thematic structural categories and then picks the category leaders that enjoy organic growth in both market size and market share. Our latest picks are as shown in Exhibit 38, and they reflect our preferences for medium-/long-term regulatory thematic exposure as discussed earlier.

Exhibit 38: Morgan Stanley China A-share Thematic Focus List

Company Name	Ticker	Rating	Market	GICS Sector	Mkt Cap (US$bn)	Date Added	Total US$ Returns Since Added	12M Total Return Perf.		Last Price	Upside to Target Price	MS P/E 2022E	MS P/E 2023E	MS P/Book 2022E	MS Div. Yld 2022E	MS P/Sales 2022E	Analyst
Baoshan Iron & Steel	600019.SS	OW	China	Materials	19.9	15-Dec-21	-17.2%	-28.7%	X	6.1	59.3%	5.9x	5.1x	0.7x	8.8%	0.3x	Zhang, Rachel
DR Laser	300776.SZ	EW	China	Information Technology	3.3	25-Feb-21	58.3%	68.1%	X	200.1	9.9%	37.8x	26.7x	6.0x	0.4%	12.8x	Zhang, Joy
Ganfeng Lithium Co. Ltd.	002460.SZ	EW	China	Materials	19.7	17-Jun-21	-12.3%	-7.0%	X	104.1	39.3%	10.2x	11.1x	5.6x	2.0%	3.8x	Zhang, Rachel
Haier Smart Home Co Ltd	600690.SS	EW	China	Consumer Discretionary	35.2	7-May-21	-19.3%	-23.9%	X	25.6	25.2%	15.9x	13.9x	-	2.4%	1.0x	Lou, Lillian
Kweichow Moutai Company Ltd.	600519.SS	OW	China	Consumer Staples	327.0	13-Jun-19	111.4%	-10.5%	X	1793.0	29.9%	36.5x	31.3x	10.1x	1.2%	17.7x	Lou, Lillian
NARI Technology	600406.SS	OW	China	Industrials	26.3	13-Jun-19	130.9%	20.3%	X	31.5	22.1%	26.7x	23.1x	4.1x	1.3%	3.7x	Hou, Eva
Qi An Xin Technology Group Inc	688561.SS	OW	China	Information Technology	4.8	11-Jan-22	-44.3%	-47.2%		49.7	151.5%	127.3x	33.7x	3.4x	0.0%	4.0x	Liu, Yang
S.F. Holding Co Ltd	002352.SZ	OW	China	Industrials	36.4	21-Jul-20	-23.5%	-24.6%	X	49.2	54.0%	35.5x	26.1x	2.8x	0.6%	0.9x	Fan, Qianlei
Shandong Nanshan Aluminium Co.	600219.SS	OW	China	Materials	5.5	16-Sep-21	-42.9%	-22.7%		3.1	78.0%	9.7x	7.3x	0.8x	1.0%	1.1x	Zhang, Rachel
Sino Wealth Electronic	300327.SZ	OW	China	Information Technology	2.7	5-Aug-21	-8.7%	24.7%	X	59.0	61.0%	38.0x	29.0x	10.0x	1.0%	8.8x	Yen, Daniel

Source: OW = Overweight. MSCI, RIMES, Morgan Stanley Research. Data as of May 6, 2022. The CNY total return of the selected stocks in the A-share thematic list since inception on February 18, 2016, is +159.5% (Shanghai Stock Exchange Composite Index total return +19.9%). This assumes the group of selected stocks constitutes an equal-weighted portfolio, rebalanced whenever positions are added or subtracted. The absolute performance of the selected stocks in the past 12 months is -8.5%, while performance relative to the Shanghai Composite Index in the past 12 months is +2.1%. Results shown represent total absolute returns (including dividends) and exclude brokerage commissions. These figures are not audited. Past performance is no guarantee of future results.

Where we could be wrong about the A-share market

1. Extended rolling lockdowns due to Omicron control would likely further weigh on domestic sentiment and cause incremental disruption to domestic social and economic activities.

2. Major reversal of regulatory tightening measures on the offshore concentrated sectors, such as Internet, and/or easing of US/China tension through tariff reduction, ADR audit agreement, and/or US IPO resumption.

3. Much more aggressive CNY appreciation relative to the USD, which would add more positive translational impact to the offshore Chinese equities.

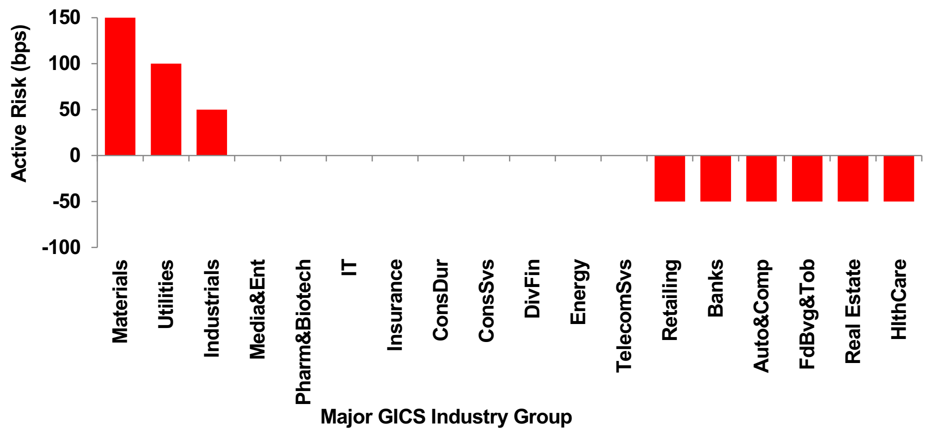
4. Unexpected regulatory tightening towards A-share market concentrated sectors, such as Consumer Staples (i.e., staples consumption taxes), Healthcare, IT and Industrials.

Sector allocation: Stay overweight in Industrials + Materials for infrastructure exposure

With sector allocation, we retain our current recommendation:

- Overweight: Industrials, Materials, Utilities
- Underweight: E-Commerce, Real Estate, Healthcare, Food Beverage & Tobacco.

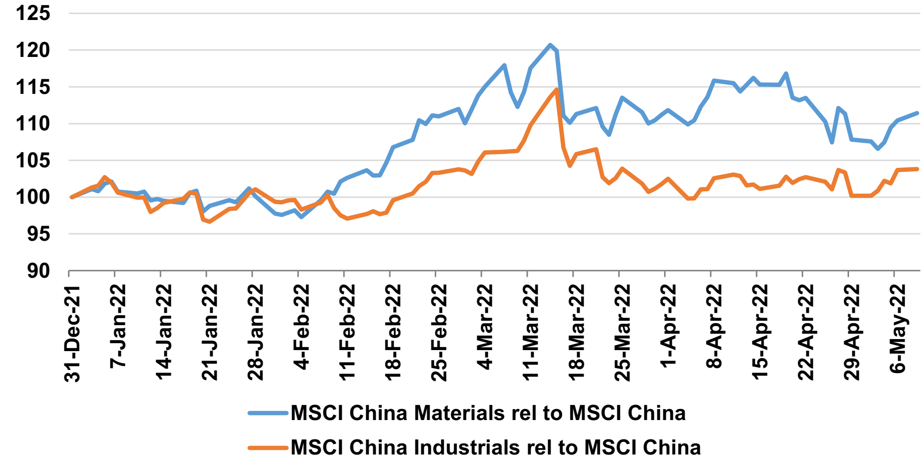
Exhibit 39: China - sector/industry group allocation recommendation



Source: Morgan Stanley Research

Continue to prefer Materials and Industrials for infrastructure activity boost: We have been long holding overweight positions in Materials and Industrials for their exposure to infrastructure because of our strong conviction in infrastructure activities as a key driver for macro growth since late 2021. Our logic is straightforward: Among the three key macro drivers for China GDP – consumption, export, investment – headwinds for consumption (due to Covid-related restrictions) and export (export competitors' reopening, global stagflation concerns) have been building, while investment is left as the sole pillar. Within investment, infrastructure spending is something that the government could control directly, while other investments, including private capex and property, are also facing significant pressure this year. YTD, by sector, Industrials and Materials have, respectively, outperformed the MSCI China index by 4 ppt and 11 ppt (Exhibit 40).

Exhibit 40: Relative performance of MSCI China Industrials and Materials vs. MSCI China (rebased on end-2021=100) – Industrials and Materials have outperformed MSCI China by 4ppt and 11ppt YTD



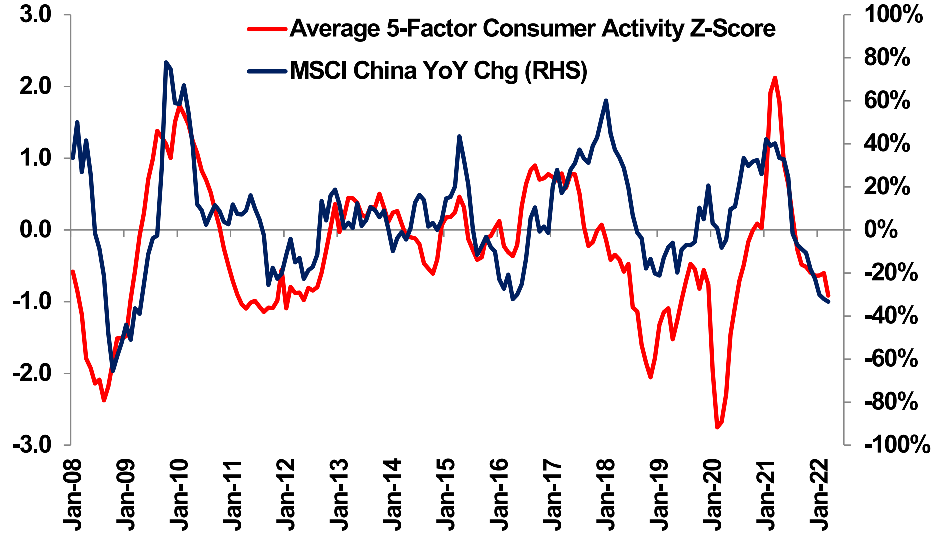
Source: Datastream, MSCI, Morgan Stanley Research. Data as of May 9, 2022.

President Xi reinforced and strengthened the message once more at the Central Financial and Economic Affairs Commission, by calling for "comprehensively advancing infrastructure investment" on Apr 26. Following the past 11 meetings since 2018, which usually focused on regulatory tightening, this is the first time the Commission has sent a clear signal to boost cyclical growth. This meeting could be a game changer also in the sense that it specified that evaluation of infrastructure projects should consider positive externalities, which could imply faster approvals. Key areas to focus are: 1) energy security, 2) digitalization infrastructure, 3) transportation/logistics in major city clusters, 4) water conservancy, and 5) rural infrastructure. For more information please visit here. **We feature 31 Morgan Stanley Research covered stocks as beneficiaries of the theme, please see Exhibit 45for the list.**

We continue to prefer some defensiveness through dividend yield plays and exposure to Utilities as a sector to weather potential near-term volatility, as discussed in this report, before the end of summer.

We stay cautious on consumption-related categories (retailing, auto, consumer staples, etc.), near term, due to Omicron headwinds, but remain nimble to potential policy relaxation and stimulus as well as pent-up demand release. Our MS proprietary China Consumer Activity Z-score shows that notable deterioration has restarted as a result of Omicron drag. The early-2020 experience suggests that the negative impact should persist for longer and be bigger (Exhibit 41). We still believe that any meaningful recovery in consumer activities is unlikely to appear in another couple of months or so, and we therefore see no rush to jump in right now.

Exhibit 41: China Five-factor Consumer Activity Z-Score vs. MSCI China YoY change – Consumption growth deteriorated sharply in March, after largely stabilizing in Dec 2021-Feb 2022



Source: MSCI, CEIC, Morgan Stanley Research. MSCI China YoY change data as of end-April 2022. Consumer z-score data as of end-March 2022. Five factors: 1) household loan yoy change; 2) consumer confidence index (CCI) yoy change; 3) passenger car sales yoy change; 4) air passenger traffic yoy change; 5) retail sales in catering yoy change.

Key trades going into 2H2022

1) Overweight A-shares vs. offshore Chinese equities, as discussed in the A-share market section, be prepared for relatively back-loaded more sustainable outperformance. Recommend A-share thematic stock list for single name ideas (Exhibit 38).

2) Wait for a better risk/return opportunity to upweight broad Chinese equities, potentially signaled by more clarity on the roadmap of Covid-zero relaxation/precaution against supply chain disruption, and/or major step-up of easing measures, and improvement of offshore listing environment. Such timing is more likely to appear during or after summer, as based on our current estimates.

3) Focus on stock-level and theme opportunities: We continue to highlight three themes of stock picking in the current volatile environment:

- Oversold high-quality names (Exhibit 42, Exhibit 43): Chinese equities, onshore and offshore, have experienced a significantly sell-off YTD. We take the messages from the Politburo Meeting and Central Economic Committee, both chaired by President Xi, positively, and we see clearer signs of top-down policy support emerging, with focus on key capital market concerns. We think this may be the final leg for the bear market; hence, it makes sense to consider stocks with strong fundamentals but that have been oversold lately. We provide screens of Chinese stocks with the greatest valuation de-rating since 4 March but that are OW-rated by our industry analysts. Read more: China Equity Strategy: Oversold Bottom-up Chinese Stock Ideas (16 Mar 2022).

- Share buyback candidate names (Exhibit 44): Chinese companies have been much more active in announcing buyback plans YTD. We believe this trend will continue for longer as it is reinforced by the CSRC statement on Mar 16 explicitly encouraging listed companies to conduct share buybacks. Historical evidence shows that the market tends to react positively to share buyback announcements, at least in the short term, especially for the Chinese ADR group. We screen for Chinese stocks best positioned as share buyback candidates based on balance sheet strength, valuation discount, etc. Read more: China Equity Strategy: Share Buyback: Historical Market Reaction Analysis and Stock Screen (25 Mar 2022).

- Top stock beneficiaries from infrastructure boost (Exhibit 45): Infrastructure capex retakes centre stage in China's economic growth outlook, following a call from the country's top leadership on April 26 at a meeting of the Central Financial and Economic Affairs Commission. This is the first time the commission has sent a clear signal to boost cyclical growth. Our China Economics team expects the infrastructure FAI CAGR to accelerate to 5.5% in 2022-23 (vs. 2% in 2018-21) via better deployment of LGSB funds and more relaxed project evaluation under Beijing's new guidance. We survey Morgan Stanley Greater China sector analysts for a 31-stock list as top beneficiaries on the theme – Read more: China Equity Strategy: Top Picks on Infrastructure Theme (28 Apr 2022).

Exhibit 42: Chinese/HK stocks that are OW rated by Morgan Stanley Research and ranked in the Top 50 as measured by the degree of consensus valuation de-rating between 4 March - 6 May 2022

Ticker	Company name	GICS sector	Analyst (Primary)	Stock rating	Mkt cap.	% change of P/E* (consensus, Mar 4-May 6)	Price to earnings (MS estimate)		EPS Growth (MS estimate)		Dividend yield (MS estimate)		Upside to target price
					US$ mn	12m FWD	2022e	2023e	2022e	2023e	2022e	2023e	
LI.O	Li Auto Inc.	Consumer Discretionary	Hsiao, Tim	Overweight	18,925	(73.1%)	NM	72.4x	-862%	161%	0.0%	0.0%	96%
1772.HK	Ganfeng Lithium Co. Ltd.	Materials	Zhang, Rachel	Overweight	20,047	(59.3%)	7.2x	7.8x	164%	-8%	2.8%	2.6%	89%
002531.SZ	Titan Wind Energy Suzhou Co Ltd	Industrials	Hou, Eva	Overweight	2,517	(52.9%)	10.5x	7.8x	18%	35%	2.5%	3.5%	211%
002008.SZ	Han's Laser	Industrials	Zhang, Joy	Overweight	4,345	(48.4%)	13.3x	11.6x	9%	15%	2.3%	2.6%	113%
688388.SS	Guangdong Jia Yuan Technology Co.,	Industrials	Zhang, Rachel	Overweight	2,326	(48.3%)	17.6x	12.5x	59%	41%	1.5%	2.4%	98%
688608.SS	Bestechnic Shanghai Co Ltd	Information Technology	Yen, Daniel	Overweight	2,009	(47.6%)	39.7x	23.0x	-17%	73%	0.5%	0.9%	88%
YY.O	JOYY Inc.	Communication Services	Poon, Alex	Overweight	3,337	(45.5%)	57.5x	28.3x	166%	103%	NA	NA	34%
603799.SS	Zhejiang Huayou Cobalt Co Ltd	Materials	Zhang, Rachel	Overweight	13,255	(44.9%)	14.0x	22.6x	95%	-38%	1.4%	0.9%	68%
300001.SZ	Qingdao TGOOD Electric Co Ltd	Industrials	Hou, Eva	Overweight	2,071	(44.4%)	27.5x	20.6x	69%	34%	0.2%	0.3%	189%
1951.HK	Jinxin Fertility Group Ltd	Health Care	Hu, Yolanda	Overweight	1,399	(44.0%)	18.5x	13.5x	52%	37%	2.5%	3.5%	86%
600219.SS	Shandong Nanshan Aluminium Co.	Materials	Zhang, Rachel	Overweight	5,540	(43.5%)	9.7x	7.3x	12%	33%	1.0%	1.4%	78%
300443.SZ	Jinlei Technology Co Ltd	Industrials	Hou, Eva	Overweight	918	(43.1%)	10.1x	9.6x	20%	5%	1.6%	1.7%	191%
2600.HK	Aluminum Corp. of China Ltd.	Materials	Zhang, Rachel	Overweight	10,350	(40.7%)	4.8x	4.3x	89%	12%	2.7%	3.0%	89%
9909.HK	Powerlong Commercial Management	Real Estate	Zhu, Cara	Overweight	615	(40.0%)	7.0x	5.1x	32%	36%	7.5%	10.1%	59%
ACMR.O	ACM Research Inc	Information Technology	Chan, Charlie	Overweight	288	(39.3%)	25.8x	14.9x	-66%	73%	1.1%	0.0%	88%
603915.SS	Jiangsu Guomao Reducer Co Ltd	Industrials	Luo, Kevin	Overweight	1,339	(38.8%)	14.0x	10.8x	34%	29%	1.7%	2.4%	184%
2015.HK	Li Auto Inc.	Consumer Discretionary	Hsiao, Tim	Overweight	19,604	(38.8%)	NM	75.0x	-862%	161%	0.0%	0.0%	87%
603501.SS	Will Semiconductor Co Ltd Shanghai	Information Technology	Chan, Charlie	Overweight	18,344	(38.6%)	28.5x	25.3x	-4%	13%	1.8%	2.0%	64%
688036.SS	Shenzhen Transsion Holdings Co Ltd	Information Technology	Meng, Andy	Overweight	9,726	(38.3%)	14.0x	11.4x	24%	23%	2.1%	2.6%	190%
300450.SZ	Wuxi Lead Intelligent	Industrials	Zhang, Joy	Overweight	10,183	(38.1%)	23.9x	18.2x	79%	31%	1.2%	1.7%	114%
1811.HK	CGN New Energy Holdings	Utilities	Lee, Simon	Overweight	1,711	(37.7%)	7.1x	6.2x	30%	14%	2.8%	3.2%	28%
600516.SS	FangDa Carbon New Material Co. Ltd.	Industrials	Chan, Sara	Overweight	3,803	(37.1%)	18.8x	14.6x	24%	29%	0.0%	0.0%	104%
600577.SS	Tongling Jingda Special Magnet Wire	Industrials	Zhang, Rachel	Overweight	1,199	(36.2%)	8.5x	6.9x	63%	23%	4.3%	5.6%	80%
1308.HK	SITC International Holdings Company	Industrials	Fan, Qianlei	Overweight	8,909	(36.2%)	7.2x	7.6x	10%	-5%	9.8%	9.2%	53%
PDD.O	Pinduoduo	Consumer Discretionary	Wang, Eddy	Overweight	52,135	(35.7%)	30.6x	21.5x	53%	43%	0.0%	0.0%	52%
601600.SS	Aluminum Corp. of China Ltd.	Materials	Zhang, Rachel	Overweight	10,350	(34.6%)	7.9x	7.1x	89%	12%	1.6%	1.8%	70%
1347.HK	Hua Hong Semiconductor Ltd	Information Technology	Wu, Ray	Overweight	4,773	(34.1%)	14.6x	21.7x	54%	-33%	1.1%	1.7%	66%
9666.HK	Jinke Smart Services Group Co.	Real Estate	Zhu, Cara	Overweight	1,772	(33.4%)	8.3x	6.4x	35%	29%	4.8%	6.2%	106%
300747.SZ	Raycus Fiber Laser	Information Technology	Zhang, Joy	Overweight	1,887	(33.2%)	19.7x	14.0x	34%	41%	0.8%	2.5%	164%

Source: Datastream, FactSet, ModelWare, I/B/E/S, Morgan Stanley Research. Data as of May 6, 2022. * % change of P/E based on the scale of consensus 12-month forward P/E derating between 3 March price close and 6 May price close.

Exhibit 43: A-share stocks that are OW rated by Morgan Stanley Research and ranked Top 50 as measured by the degree of consensus valuation de-rating, and with Northbound outflows between 4 March - 5 May 2022

Ticker	Company name	GICS sector	Analyst (Primary)	Stock rating	Mkt cap.	% change of P/E* (consensus, Mar 4-May 6)	Price to earnings (MS estimate)		EPS Growth (MS estimate)		Dividend yield (MS estimate)		Upside to target price	Northbound outflows as % of Northbound holdings** (Mar 4-May 5)
					US$ mn	12m FWD	2022e	2023e	2022e	2023e	2022e	2023e		
300001.SZ	Qingdao TGOOD Electric Co Ltd	Industrials	Hou, Eva	Overweight	2,071	(44.4%)	27.5x	20.6x	69%	34%	0.2%	0.3%	189%	(4.1%)
603501.SS	Will Semiconductor Co Ltd Shanghai	Information Technology	Chan, Charlie	Overweight	18,344	(38.6%)	28.5x	25.3x	-4%	13%	1.8%	2.0%	64%	(7.7%)
600516.SS	FangDa Carbon New Material Co. Ltd.	Industrials	Chan, Sara	Overweight	3,803	(37.1%)	18.8x	14.6x	24%	29%	0.0%	0.0%	104%	(18.0%)
601600.SS	Aluminum Corp. of China Ltd.	Materials	Zhang, Rachel	Overweight	10,350	(34.6%)	7.9x	7.1x	89%	12%	1.6%	1.8%	70%	(6.7%)
300747.SZ	Raycus Fiber Laser	Information Technology	Zhang, Joy	Overweight	1,887	(33.2%)	19.7x	14.0x	34%	41%	0.8%	2.5%	164%	(10.0%)
300347.SZ	Hangzhou Tigermed Consulting	Health Care	Hu, Yolanda	Overweight	10,703	(30.9%)	29.9x	26.6x	-10%	13%	0.5%	0.6%	77%	(9.5%)
002601.SZ	LB Group Co Ltd	Materials	Li, Albert	Overweight	6,456	(30.3%)	8.0x	7.6x	15%	5%	7.9%	8.3%	85%	(3.6%)

Source: Datastream, FactSet, ModelWare, I/B/E/S, Morgan Stanley Research. Data as of May 6, 2022. * % change of P/E based on the scale of consensus 12-month forward P/E derating between 3 March price close and 6 May price close. ** Only Northbound eligible stocks with outflows during 4 March to 5 May (inclusive) as % of total Northbound holdings as of March 3, 2022 are included (Northbound closed on 6 May 2022).

Exhibit 44: Stock screen of MS-covered Chinese/HK equities best positioned to carry out share buyback plans based on balance sheet strength, consensus valuation derating since prior market peak on February 17, 2021, MS stock rating and market cap (sorted by market cap)

Ticker	Company name	Primary analyst	GICS sector	Market cap (US$ mn)	Trailing 12M FCF (US$ mn)	Net cash/ market cap	Net debt/ equity	Valuation metrics: % chg of consensus 12M FWD P/E (since 17 Feb 2021's close)	Valuation metrics: % chg of consensus 12M FWD P/S (since 17 Feb 2021's close)	Valuation metrics: % chg of consensus 12M FWD EV/EBITDA (since 17 Feb 2021's close)	MS Stock rating	If company announced share buyback plans in 2022 (Y/N)
600519.SS	Kweichow Moutai Company Ltd	Lou, Lillian	Consumer Staples	336,946	8,636	1.4%	(21.3%)	(42.5%)	(42.4%)	(42.4%)	Overweight	
BABA.N	Alibaba Group Holding	Yu, Gary	Consumer Discretionary	242,331	NA	25.6%	(40.6%)	(50.2%)	(67.5%)	(54.3%)	Overweight	Y
0941.HK	China Mobile Limited	Yu, Gary	Communication Services	133,580	19,344	47.7%	(33.5%)	(5.8%)	(7.4%)	3.8%	Overweight	Y
000858.SZ	Wuliangye Yibin Company Ltd.	Lou, Lillian	Consumer Staples	91,198	2,548	13.9%	(70.0%)	(61.0%)	(61.4%)	(63.9%)	Overweight	
JD.O	JD.com, Inc.	Wang, Eddy	Consumer Discretionary	74,343	3,673	33.2%	(75.0%)	(44.8%)	(59.1%)	(48.6%)	Overweight	
0883.HK	CNOOC	Lu, Jack	Energy	61,996	9,616	7.0%	(5.6%)	(56.8%)	(30.7%)	(36.1%)	Overweight	
NTES.O	NetEase, Inc	Poon, Alex	Communication Services	61,093	3,617	20.5%	(82.6%)	(37.1%)	(40.4%)	(42.8%)	Overweight	
300760.SZ	Mindray Bio-Medical	Hu, Yolanda	Health Care	55,501	1,158	4.3%	(52.3%)	(54.9%)	(52.5%)	(54.4%)	Overweight	Y
601012.SS	LONGi Green Energy Technolog	Lee, Simon	Information Technology	54,278	1,211	1.3%	(19.3%)	(42.9%)	(45.7%)	(41.7%)	Overweight	
002415.SZ	HIKVision Digital Technology	Meng, Andy	Information Technology	49,109	1,124	7.8%	(29.8%)	(56.9%)	(60.1%)	(59.1%)	Overweight	Y
PDD.O	Pinduoduo	Wang, Eddy	Consumer Discretionary	48,287	3,953	45.4%	(186.1%)	(96.7%)	(86.4%)		Overweight	
601888.SS	China Tourism Group Duty Free	Ling, Hildy	Consumer Discretionary	47,811	706	4.0%	(34.8%)	(61.7%)	(61.2%)	(60.6%)	Overweight	
600809.SS	Shanxi Xinghuacun Fen Wine Fa	Lou, Lillian	Consumer Staples	46,299	1,698	3.8%	(77.5%)	(64.6%)	(52.6%)	(63.6%)	Overweight	Y
600887.SS	Yili Industrial	Lou, Lillian	Consumer Staples	33,677	1,319	5.4%	(7.0%)	(35.0%)	(29.8%)	(30.8%)	Overweight	Y
1876.HK	Budweiser Brewing Company A	Lou, Lillian	Consumer Staples	32,730	1,297	5.6%	(16.8%)	(35.0%)	(36.5%)	(39.2%)	Overweight	
000651.SZ	Gree Electric Appliances Inc of	Lou, Lillian	Consumer Discretionary	30,047	NA	24.9%	(25.9%)	(49.0%)	(47.6%)	(41.0%)	Overweight	
2020.HK	ANTA Sports Products	Wei, Dustin	Consumer Discretionary	28,865	1,611	3.6%	(23.1%)	(51.0%)	(55.6%)	(53.8%)	Overweight	
1810.HK	Xiaomi Corp	Meng, Andy	Information Technology	28,787	480	35.0%	(44.4%)	(72.4%)	(68.3%)	(76.0%)	Overweight	Y
600276.SS	Jiangsu Hengrui	Wu, Sean	Health Care	27,998	365	10.2%	(48.4%)	(51.5%)	(58.5%)	(54.2%)	Overweight	Y
601919.SS	COSCO Shipping Holdings Ltd	Fan, Qianlei	Industrials	27,536	25,278	28.3%	(40.7%)	(75.6%)	(8.6%)	(84.4%)	Overweight	
601138.SS	Foxconn Industrial Internet Co.	Shih, Sharon	Information Technology	27,310	567	13.6%	(19.8%)	(36.6%)	(36.1%)	(36.8%)	Overweight	Y
600406.SS	NARI Technology	Hou, Eva	Industrials	26,281	283	3.9%	(18.5%)	(6.8%)	(7.5%)	(10.9%)	Overweight	Y
600585.SS	Anhui Conch Cement Co. Ltd	Zhang, Rachel	Materials	23,293	NA	52.9%	(37.8%)	(18.0%)	(26.9%)	(24.1%)	Overweight	
300124.SZ	Shenzhen Inovance Technology	Luo, Kevin	Industrials	19,014	97	1.5%	(1.2%)	(55.8%)	(57.3%)	(53.0%)	Overweight	Y
2313.HK	Shenzhou International Group	Cheng, Terence	Consumer Discretionary	18,671	246	6.6%	(18.0%)	(37.6%)	(49.8%)	(39.7%)	Overweight	
2331.HK	Li Ning	Wei, Dustin	Consumer Discretionary	18,336	774	11.8%	(65.2%)	(53.0%)	(29.9%)	(52.4%)	Overweight	
LI.O	Li Auto Inc.	Hsiao, Tim	Consumer Discretionary	17,886	651	37.1%	(97.5%)		(49.6%)	(93.5%)	Overweight	
YUMC.N	Yum China Holdings Inc.	Lou, Lillian	Consumer Discretionary	17,037	703	6.8%	(20.5%)	0.8%	(42.5%)	(32.6%)	Overweight	Y
0291.HK	China Resources Beer Holdings	Lou, Lillian	Consumer Staples	16,903	583	5.2%	(23.1%)	(47.8%)	(40.9%)	(45.3%)	Overweight	
0175.HK	Geely Automobile Holdings	Yeung, Jack	Consumer Discretionary	14,808	2,126	21.3%	(30.8%)	(48.4%)	(68.9%)	(65.7%)	Overweight	Y
0762.HK	China Unicom	Yu, Gary	Communication Services	14,539	6,098	43.4%	(11.9%)	(29.9%)	(28.4%)	(54.9%)	Overweight	Y
2382.HK	Sunny Optical	Meng, Andy	Information Technology	13,987	707	7.9%	(33.0%)	(57.1%)	(49.4%)	(62.2%)	Overweight	Y
LU.N	Lufax	Xu, Richard	Financials	12,656	841	25.3%	(21.9%)	(73.1%)	(74.3%)	(71.3%)	Overweight	Y
002027.SZ	Focus Media Information Techn	Xu, Rebecca	Communication Services	12,336	1,478	6.7%	(29.4%)	(63.2%)	(57.2%)	(62.5%)	Overweight	
6098.HK	Country Garden Services Holdin	Liu, Chloe	Real Estate	12,246	491	12.4%	(25.3%)	(72.1%)	(78.0%)	(77.1%)	Overweight	Y
000596.SZ	Anhui Gujing Distillery Compan	Lou, Lillian	Consumer Staples	12,206	1,297	18.4%	(95.2%)	(29.4%)	(36.3%)	(33.8%)	Overweight	
603986.SS	GigaDevice Semiconductor Beij	Yen, Daniel	Information Technology	11,912	195	11.6%	(61.8%)	(59.5%)	(54.9%)	(59.4%)	Overweight	
1093.HK	CSPC Pharmaceutical Group	Hu, Yolanda	Health Care	11,721	534	14.2%	(40.9%)	(24.3%)	(14.5%)	(27.2%)	Overweight	Y
BEKE.N	KE Holdings Inc	Tsai, Steven	Real Estate	11,177	336	68.3%	(72.6%)	(64.1%)	(77.7%)	(76.7%)	Overweight	
1209.HK	China Resources Mixc Lifestyle	Liu, Chloe	Real Estate	10,657	361	17.8%	(84.7%)	(56.2%)	(50.8%)	(64.2%)	Overweight	
002920.SZ	Huizhou Desay SV Automotive	Wang, Shelley	Consumer Discretionary	10,051	58	2.3%	(3.6%)	(43.7%)	(35.1%)	(60.8%)	Overweight	

Source: FactSet, Wind, Bloomberg, ModelWare, I/B/E/S, Datastream, Refinitiv Eikon, Morgan Stanley Research. Data as of May 6, 2022. The above screen is derived based on following criteria: 1) Balance sheet strength measured by a) positive trailing 12-month free cash flow; b) positive net cash to market cap ratio; c) negative net debt to equity ratio; 2) OW rated by MS research analysts; 3) Consensus valuation discounted since 17 Feb 2021, prior China market peak, measured by derating of consensus 12-month forward P/E or 12-month forward P/S or 12-month forward EV/EBITDA; 4) Market cap above US$10bn as of May 6, 2022.

Exhibit 45: Top China stock beneficiaries from the infrastructure push (sorted by GICS sector and analyst name)

Ticker	Company name	GICS sector	Analyst (Primary)	Mkt cap.	Price to earnings (MS estimate)		EPS Growth (MS estimate)		Dividend yield (MS estimate)		Upside to target price
				US$ mn	2022e	2023e	2022e	2023e	2022e	2023e	
0700.HK	Tencent Holdings Ltd.	Communication Services	Yu, Gary	421,039	26.3x	22.7x	-51%	16%	1.3%	0.6%	37%
BIDU.O	Baidu Inc	Communication Services	Yu, Gary	43,401	24.0x	14.4x	16%	66%	0.0%	0.0%	54%
0941.HK	China Mobile Limited	Communication Services	Yu, Gary	139,582	7.4x	6.9x	3%	7%	8.6%	9.7%	37%
0728.HK	China Telecom	Communication Services	Yu, Gary	32,875	7.8x	6.9x	5%	15%	8.6%	10.6%	42%
0788.HK	China Tower Corp Ltd	Communication Services	Yu, Gary	19,732	15.7x	16.4x	13%	-4%	4.2%	4.2%	14%
0762.HK	China Unicom	Communication Services	Yu, Gary	14,540	6.0x	5.4x	12%	12%	8.6%	9.6%	47%
BABA.N	Alibaba Group Holding	Consumer Discretionary	Yu, Gary	235,031	23.4x	15.4x	-46%	33%	0.0%	0.0%	55%
2343.HK	Pacific Basin Shipping	Industrials	Fan, Qianlei	2,285	2.6x	2.5x	26%	3%	19.1%	19.6%	75%
600406.SS	NARI Technology	Industrials	Hou, Eva	26,203	26.7x	23.1x	16%	16%	1.3%	1.5%	22%
0390.HK	China Railway Group	Industrials	Luo, Kevin	23,759	3.8x	3.4x	8%	11%	3.7%	4.0%	8%
1186.HK	China Railway Construction	Industrials	Luo, Kevin	15,585	2.1x	1.9x	13%	14%	7.0%	8.0%	93%
1800.HK	CCCC	Industrials	Luo, Kevin	20,686	2.6x	2.3x	17%	15%	6.5%	7.6%	19%
0552.HK	China Communication Service Co Ltd	Industrials	Yu, Gary	3,141	6.4x	6.2x	4%	3%	6.0%	6.1%	21%
601231.SS	Universal Scientific Ind. (Shanghai)	Information Technology	Chan, Charlie	4,215	15.6x	15.2x	-3%	2%	2.5%	2.5%	26%
300373.SZ	Yangjie Technology	Information Technology	Dai, Daisy	5,513	34.7x	28.7x	35%	21%	0.4%	0.6%	(5%)
600460.SS	Hangzhou Silan Microelectronics Co. L	Information Technology	Dai, Daisy	8,352	38.9x	28.4x	-6%	37%	0.2%	0.5%	57%
000977.SZ	Inspur Electronic Information	Information Technology	Kao, Howard	5,496	14.0x	11.5x	22%	21%	0.9%	1.1%	24%
0992.HK	Lenovo	Information Technology	Kao, Howard	12,001	6.6x	7.5x	67%	-19%	6.3%	11.4%	8%
601012.SS	LONGi Green Energy Technology Co L	Information Technology	Lee, Simon	54,437	26.0x	21.1x	31%	23%	0.9%	1.1%	49%
002410.SZ	Glodon Co. Ltd.	Information Technology	Liu, Yang	8,647	60.2x	43.8x	47%	38%	0.7%	0.9%	38%
002415.SZ	HIKVision Digital Technology	Information Technology	Meng, Andy	48,784	18.6x	15.6x	3%	19%	2.6%	2.7%	52%
0763.HK	ZTE Corporation	Information Technology	Meng, Andy	14,903	7.5x	6.6x	6%	15%	3.6%	11.4%	90%
6869.HK	Yangtze Optical Fibre and Cable JSC L	Information Technology	Meng, Andy	2,058	7.2x	6.1x	21%	18%	3.1%	3.1%	57%
601138.SS	Foxconn Industrial Internet Co. Ltd.	Information Technology	Shih, Sharon	25,895	8.6x	7.6x	6%	13%	2.3%	2.6%	37%
603290.SS	StarPower Semiconductor Ltd	Information Technology	Wu, Ray	7,568	84.3x	69.4x	52%	22%	0.2%	0.2%	33%
002010.SZ	Transfar Zhilian Co Ltd	Materials	Fang, Wei	2,937	9.4x	8.6x	16%	9%	2.7%	2.9%	77%
000898.SZ	Angang Steel Company Limited	Materials	Zhang, Rachel	4,735	5.2x	4.6x	-10%	14%	5.8%	6.6%	42%
0914.HK	Anhui Conch Cement Co. Ltd	Materials	Zhang, Rachel	30,316	5.8x	5.8x	-2%	-1%	6.6%	6.5%	31%
3323.HK	China National Building Material Comp	Materials	Zhang, Rachel	10,939	4.2x	3.7x	8%	11%	9.6%	10.7%	38%
600019.SS	Baoshan Iron & Steel	Materials	Zhang, Rachel	20,178	5.9x	5.1x	-4%	17%	8.8%	10.3%	59%
600808.SS	Maanshan Iron & Steel	Materials	Zhang, Rachel	4,049	5.5x	5.0x	-1%	10%	9.2%	10.1%	24%

Source: ModelWare, Morgan Stanley Research. Data as of May 6, 2022.

4) Our China/Hong Kong Focus List for stock picking as a balanced demonstration of our top-down and sector view. It features 15 stocks selected by us with reference to our listing jurisdiction preference (A-shares, HK listed or ADRs), sector and thematic preferences. We also take into account stock rating by our sector analysts and their detailed company view. Constituents usually carry an OW rating.

Exhibit 46: Morgan Stanley China/HK Focus List

Company Name	Ticker	Rating	Market	GICS Sector	Mkt Cap (US$bn)	Date Added	Total US$ Returns Since Added	12M Total Return Perf.		Last Price	Upside to Target Price	MS P/E 2022E	MS P/E 2023E	MS P/Book 2022E	MS Div. Yld 2022E	MS P/Sales 2022E	Analyst
AIA Group	1299.HK	OW	Hong Kong	Financials	114.3	3-Sep-14	84.5%	-25.2%	X	74.0	67.6%	16.3x	14.7x	1.8x	2.1%	2.4x	Jiang, Jenny
Anhui Conch Cement	0914.HK	OW	China	Materials	29.9	22-Feb-22	-6.6%	-7.5%	X	42.0	31.0%	5.8x	5.9x	0.9x	6.5%	1.1x	Zhang, Rachel
Baoshan Iron & Steel	600019.SS	OW	China	Materials	19.9	15-Dec-21	-17.2%	-28.7%	X	6.1	59.3%	5.9x	5.1x	0.7x	8.8%	0.3x	Zhang, Rachel
China Oilfield Services	2883.HK	OW	China	Energy	7.4	22-Feb-22	-9.9%	4.9%	X	8.0	45.1%	9.8x	7.5x	0.8x	3.1%	1.5x	Li, Albert
China Yangtze Power	600900.SS	OW	China	Utilities	75.5	11-Jan-22	-3.7%	14.6%	X	22.7	3.4%	19.5x	17.9x	2.7x	3.6%	9.0x	Lee, Simon
Ganfeng Lithium	1772.HK	OW	China	Materials	19.7	17-Jun-21	-19.0%	-13.2%	X	86.2	89.1%	7.3x	7.9x	4.0x	2.8%	3.8x	Zhang, Rachel
Haier Smart Home	600690.SS	EW	China	Consumer Discretionary	35.2	7-May-21	-19.3%	-23.9%	X	25.6	25.2%	15.9x	13.9x	-	2.4%	1.0x	Lou, Lillian
HKT Trust and HKT	6823.HK	OW	Hong Kong	Communication Services	10.9	24-Mar-21	9.2%	4.5%	X	11.3	15.2%	18.7x	16.7x	2.4x	6.5%	2.5x	Yu, Gary
Kunlun Energy	0135.HK	OW	China	Utilities	7.0	4-Mar-22	-15.3%	6.9%		6.4	56.5%	8.7x	8.9x	0.8x	3.5%	0.3x	Lee, Simon
Link REIT	0823.HK	OW	Hong Kong	Real Estate	18.2	2-Dec-21	-0.7%	-6.1%	X	67.0	17.9%	20.5x	19.3x	0.8x	4.9%	11.9x	Choudhary, Praveen
NARI Technology	600406.SS	OW	China	Industrials	26.3	13-Jun-19	130.9%	20.3%	X	31.5	22.1%	26.7x	23.1x	4.1x	1.3%	3.7x	Hou, Eva
Shandong Gold Mining	1787.HK	EW	China	Materials	11.3	4-Mar-22	-10.0%	-9.6%	X	13.5	24.1%	20.1x	22.0x	1.7x	0.4%	1.1x	Chan, Sara
Shandong Nanshan Aluminium	600219.SS	OW	China	Materials	5.5	23-Aug-21	-45.5%	-22.7%		3.1	78.0%	9.7x	7.3x	0.8x	1.0%	1.1x	Zhang, Rachel
Sino Wealth Electronic	300327.SZ	OW	China	Information Technology	2.7	5-Aug-21	-8.7%	24.7%	X	59.0	61.0%	38.0x	29.0x	10.0x	1.0%	8.8x	Yen, Daniel
Tencent Holdings	0700.HK	OW	China	Communication Services	421.0	19-Jan-22	-21.7%	-41.5%	X	349.2	37.5%	26.6x	22.9x	3.3x	1.2%	4.7x	Yu, Gary

Source: OW = Overweight. Source: ModelWare, RIMES, FactSet, Morgan Stanley Research. Data as of May 6, 2022. The US$ total return of the Morgan Stanley HK/China Equity Strategy Focus List since inception on September 3, 2014 is 60.8% (MSCI China Index total return 10.0%). This assumes the Focus List constitutes an equal-weighted portfolio, rebalanced whenever positions are added or subtracted. Results shown represent total absolute return (including dividends) and exclude brokerage commissions. These figures are not audited. Past performance is no guarantee of future results. (X) indicates stock has outperformed MSCI China Index since inclusion in the Focus List.

Exhibit 47: Performance of China/HK Focus List - +1849 bps alpha over 12 months

Name	Performance, US $			
	12 Months		1 Month	
	Absolute	Relative	Absolute	Relative
China/HK Focus List	-20.7%	18.5%	-8.1%	5.6%

Source: MSCI, RIMES, Morgan Stanley Research. Data as of May 6, 2022. China/HKFocus List performance is relative to MSCI China Index. These figures are not audited. Past performance is no guarantee of future results. Data is total return based and excludes brokerage commissions.

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	COVERAGE UNIVERSE		INVESTMENT BANKING CLIENTS (IBC)			OTHER MATERIAL INVESTMENT SERVICES CLIENTS (MISC)	
STOCK RATING CATEGORY	COUNT	% OF TOTAL	COUNT	% OF TOTAL IBC	% OF RATING CATEGORY	COUNT	% OF TOTAL OTHER MISC
Overweight/Buy	**1424**	**40%**	**374**	**44%**	**26%**	**626**	**40%**
Equal-weight/Hold	**1564**	**44%**	**373**	**44%**	**24%**	**705**	**45%**
Not-Rated/Hold	**0**	**0%**	**0**	**0%**	**0%**	**0**	**0%**
Underweight/Sell	**564**	**16%**	**95**	**11%**	**17%**	**219**	**14%**
TOTAL	**3,552**		**842**			**1550**	

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