REGIONAL MARKETS UPDATE

GREATER CHINA

China: Offshore (H) 4.5 Stars — Very Attractive, Onshore (A) 3.5 Stars — Attractive

- GDP was 6.8% y-o-y in 4Q 17, flat with that in 3Q 17 but higher than the expected 6.7%
- Caixin China Manufacturing PMI was 51.5 in Dec 17, higher than 50.8 in Nov 17
- Exports growth decreased moderately to 10.9% y-o-y in Dec 17, compared with 11.5% in Nov 17
- Imports growth decreased to 4.5% y-o-y in Dec 17, compared with 17.6% in Nov 17
- CPI came at 1.8% y-o-y in Dec 17, higher than 1.7% in Nov 17
- PPI rose 4.9% y-o-y in Dec 17, lower than 5.8% in Nov 17
- Retail sales grew 9.4% y-o-y in Dec 17, higher than 10.3% in Nov 17
- Urban fixed asset investment (FAI) came down to 7.2% YTD y-o-y in Dec 17, flat with that in Nov 17
- Industrial production growth was 6.2% y-o-y in Dec 17, slightly higher 6.1% in Nov 17

Hong Kong: 4.5 Stars—Very Attractive

- Nikkei Hong Kong PMI increased to 51.5 in Dec 17 from 50.7 in Nov 17
- The seasonal adjusted unemployment rate came at 2.9% in Dec 17, slightly lower than 3.0% in Nov 17
- Foreign exchange reserves in Hong Kong grew to 431.3 USD billion in December, 2.18% higher than that in November 17

Taiwan: 4.0 Stars — Very Attractive

- Nikkei Taiwan Manufacturing PMI increased to 56.6 in Dec 17, slightly higher than 56.3 in Nov 17
- Taiwan's CPI increased to 1.21% y-o-y in December from 0.34% in November 17
- Exports grew 14.8% y-o-y in Dec 17, higher than the growth rate of 14.0% y-o-y in Nov 17
- Imports increased 12.2% y-o-y in Dec 17 from 9.0% y-o-y in Nov 17

MARKET OUTLOOK

China maintained its growth resilience and reform momentum in 4Q 2017 with the GDP growth of 6.8% year-on-year higher than the expected 6.7%. The Caixin China manufacturing PMI was 51.5, topping expectation. This positive reading of expansion was due to stabilized economic growth and improved manufacturing operating conditions. Internationally, the export growth declined slightly to 10.9% in December from 12.3% in November but remained healthy. In contrast, imports declined by the biggest margin in almost two years in volume terms as purchases of industrial commodities plummeted. Domestically, industrial production inched up by 0.1 percent point to 6.2% due to accelerated growth in electricity, gas and water supply in winter. Furthermore, after 8 months' slowing down, the urban fixed asset investment (FAI) maintained a growth rate of 7.2% year-on-year in December, beating the expectation of 7.1%. By industry, FAI increased mainly in transport, storage and postal industry (14.8% vs 9.5% in 2016) and manufacturing (4.8% vs 4.2%). The CPI inflation mildly rose 1.8% year-on-y in December from 1.7% for November, mainly driven by a fast increase in non-food prices. Prices for medical products and services rose 6.6% and housing-related prices rose 2.8%, while educational, cultural and entertainment prices rose 2.1%. Meanwhile, the PPI slowed down its growth further from 5.8% in November to 4.9% in December due to the high base last year. The moderation in PPI came mainly in upstream sectors, such as the mining and raw materials sectors. Partially due to the slowing auto sales, the retail sales growth edged down to 9.4% year-on-y in December from 10.3% in November, the slowest pace registered since June 2003-excluding strong seasonal January and February.

In Hong Kong, the Nikkei Hong Kong PMI stood at 51.5 in December, up from 50.7 in November 2017. This improvement of economic expansion for the second successive month was supported by the robust demand from the mainland. With the prosperity of Hong Kong's economy, its seasonally adjusted unemployment rate dropped to 2.9% in December 2017, below 3% for the first time in 20 years. The tighter labour force was mainly observed in the real estate sector, and the foundation and superstructure works of the construction sector. Meanwhile, Hong Kong trade deficit widens to HKD 59.9 billion in December from HKD 39.7 billion in November 2017, as imports grew faster than exports. Purchases grew mainly from major suppliers such as Malaysia and Taiwan, while sales reduction was recorded in exports to the UK. Along with an improving global outlook and robust domestic demand in the near term, we expect the Hong Kong economy will maintain its solid growth in 2018.

In Taiwan, the Nikkei manufacturing PMI achieved 56.6 in December, a record high since April 2011. The improvement in operating conditions was mainly driven by a sharp and broad-based increase in new orders, including export sales. Particularly, its export orders increased 17.5% year-on-y in December, as compared to 11.6% in November. This was mainly supported by strong demand of machinery, parts of electronic product, plastics & rubber and articles thereof, base metals and articles of base metal, and information, communications and audio-video products. Furthermore, industrial production grew 1.2% year-on-year in December, following an upwardly revised 1.34% rise in November. Production rose less for manufacturing and continued to fall for mining and quarrying, while electricity and gas supply increased 6.73%. Given the improving global economic environment as well as the rising demand for technology equipment, we expected the Taiwan's export sector should remain supported.

As at 26 January 2018, the CSI 300 Index is currently trading at estimated PE ratios of 16.9X and 14.6X based on estimated earnings in 2017 and 2018 respectively, 2017 estimated PE higher than our fair PE ratio of 15.0X while 2018 estimated PE is still a discount to the fair value. The HSML100 Index is trading at 12.7X and 10.8X (based on estimated earnings in 2017 and 2018 respectively) as compared to our fair PE of 13.0X. We continue to prefer H-shares to the onshore market. We maintain our **4.5 Stars "Very Attractive" rating for the offshore Chinese equity market**. Moreover, the Hong Kong equity market is currently trading at estimated PE ratios of 14.7X and 13.1X based on estimated earnings in 2017 and 2018 respectively, below its fair value of 15.0X. Therefore, we maintain our **4.5 Stars "Very Attractive" rating for Hong Kong**. Lastly, Taiwan is trading at estimated PE ratios of 15.8X and 14.3X based on 2017 and 2018 estimated earnings respectively, slightly higher than our fair PE ratio of 14.0X. We thus maintain a **4.0 Stars "Very Attractive" rating for Taiwan**.

RECOMMENDED FUND:

FIRST STATE REGIONAL CHINA FUND

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