

# What are the next stocks to enter southbound trading?

## Potential new eligible stocks to be unveiled

The Hang Seng Composite Index (HSCI) is now under its regular semi-annual review. The review results are scheduled to be announced on 6 February and to be effective on the trading day after the first Friday of March, ie, 5 March. The southbound stock universe (SB universe) will adjust accordingly at the same time. As the potential inclusion into SB universe acted as a strong price boost to related stocks in the last review, we think similar opportunities could emerge among potential new eligible stocks that have solid fundamentals and still-attractive valuations. Please refer to Fig.2 for the valuation table of potential new eligible stocks.

## Strong outperformance of new eligible stocks in last review

A recap of stock performance in the last index review suggests that new eligible stocks started to outperform the market right after the announcement day (16 August 2017) rather than the actual effective and inclusion day (4 September). We believe expectations of incremental inflows from mainland investors was an important contributing factor. Prices of new eligible stocks, on average, jumped by 28% in the two months after 16 August, while the HSI index recorded returns of less than 5% during the same period.

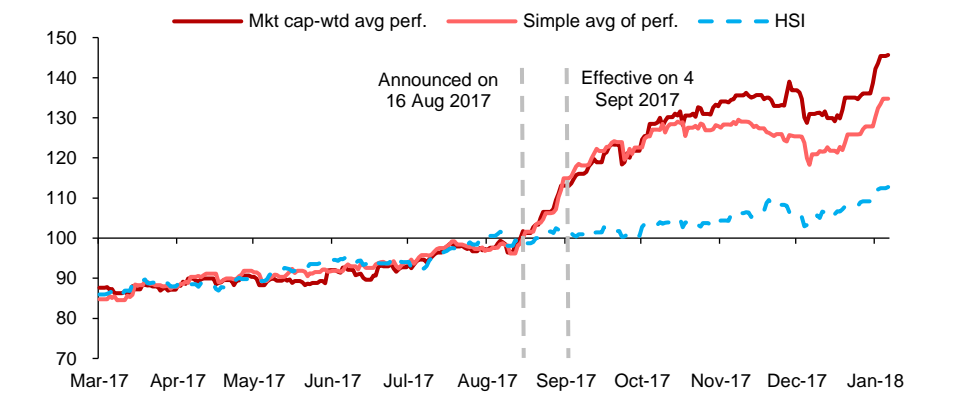
## Screening results of potential new eligible stocks

We screened a list of 32 potential new eligible stocks, based on the following eligibility criteria of SB universe: 1) constituents of the HSCI large cap and mid cap index; 2) constituents of HSCI small-cap index with an average market cap of larger than HKD5bn for the last 12 months as of the cut-off date; and 3) H-share companies with A-share listings which are not under risk alert. In terms of market cap, these companies are concentrated in the materials (accounting for 19% of the market cap of new eligible stocks), software (14%), real estate (13%), and consumer services (12%) sectors. The largest potential names include China Literature, China Hongqiao, Landing International Development, Yixin Group, and Razer.

## Remain positive but wary of short-term doldrums

The HK and China markets have performed particularly strongly so far this year, with the HSI index approaching a historical high (up 4.8%) and HSCEI registering gains of 6.5%. The strong performance was mainly due to the fund inflows from both overseas investors, represented by strong inflows of ETFs tracking Emerging Markets, and southbound investors, with average daily inflow amounting to RMB2.3bn (December 2017: RMB1.5bn). In addition, buoyant investor sentiment globally, insufficient data points on companies and macro-economy at the beginning of the year and stronger-than-expected oil prices have all helped to ignite market performance. In the first two weeks of 2018, China property (15%), coal (14.9%), basic chemicals (12%), cement and glasses (11.1%), healthcare (10.6%), and oil and petrochemicals (10.3%) were among the leading sectors. While we remain positive, we note that after such a rapid rise, the market could enter short-term doldrums and become prone to short-term volatility. We remain mostly upbeat on banks and insurers at the moment. For the long term, we continue to like: 1) select names benefiting from structural shifts in consumption; and 2) new economy sectors such as healthcare and internet leaders.

**Fig.1. Price performance of new southbound stocks included in September 2017**



Source: Bloomberg, Huatai HK Research

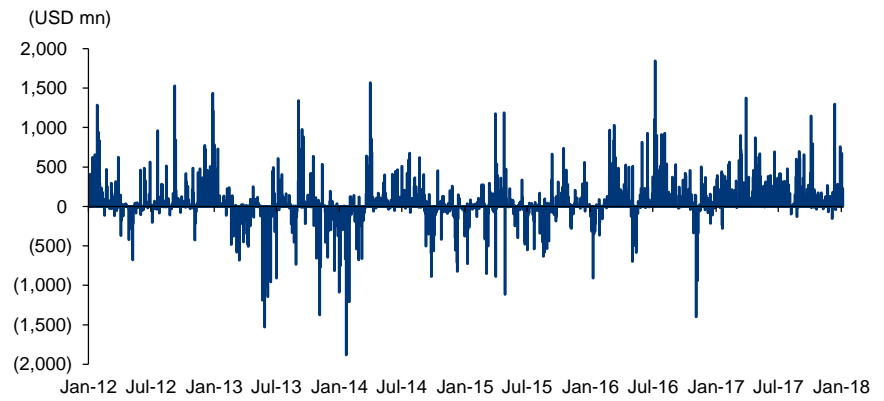
**Fig.2. Potential new eligible stocks for southbound trading**

Ticker	Name	Industry group	Mkt cap (HKDbn)	Freefloat	12M avg	3M ADT (HKDmn)	2018E PE	2018E EPS growth (%)	2019E EPS growth (%)	2018E PB	2018E ROE (%)
				mkt cap (HKDbn)	mkt cap (HKDbn)						
772 HK	CHINA LITERATURE	Software & Services	77.2	18.3	78.6	800.6	74.1	95.0	57.1	4.5	6.0
1378 HK	CHINA HONGQIAO	Materials	86.4	22.3	56.6	145.9	6.3	60.1	2.9	1.1	18.2
582 HK	LANDING INTL	Consumer Services	49.4	23.9	17.8	120.2	N/A	N/A	N/A	N/A	N/A
2858 HK	YIXIN GROUP LTD	Diversified Financials	41.5	16.4	42.2	401.3	28.9	168.6	82.4	2.3	7.0
1337 HK	RAZER INC	Tech Hardware & Equip	34.9	13.7	35.7	228.2	N/A	91.7	333.3	8.7	-6.2
127 HK	CHINESE ESTATES	Real Estate	25.8	6.5	24.1	25.1	N/A	N/A	N/A	N/A	N/A
2232 HK	CRYSTAL INTL	Cons Durables & Apparel	23.5	4.4	20.8	64.9	14.6	20.0	18.1	2.9	20.5
45 HK	HK&S HOTELS	Consumer Services	19.3	5.4	17.7	11.4	25.3	-5.9	-16.7	0.5	2.4
754 HK	HOPSON DEV	Real Estate	17.8	4.5	16.7	6.3	12.7	6.8	1.6	N/A	N/A
520 HK	XIABUXIABU	Consumer Services	14.3	4.7	9.2	44.1	21.1	25.0	23.5	4.9	24.8
839 HK	CHINA EDUCATION	Consumer Services	14.8	2.8	13.2	57.9	N/A	N/A	N/A	N/A	N/A
1269 HK	CHINA FIRST CAPI	Autos & Components	14.7	9.0	14.7	13.7	N/A	N/A	N/A	N/A	N/A
1608 HK	VPOWER GROUP INT	Capital Goods	13.0	2.3	12.0	1.4	16.2	92.0	30.0	4.1	24.3
189 HK	DONGYUE GROUP	Materials	11.2	5.6	6.9	45.0	7.3	-7.0	5.9	N/A	13.3
6068 HK	WISDOM EDU	Consumer Services	10.1	2.7	6.4	17.8	23.3	38.4	30.4	4.0	17.8
512 HK	CHINA GRAND PHAR	Pharms, Biotech	9.4	3.7	5.4	7.2	21.1	33.3	25.0	N/A	N/A
832 HK	CENTRAL CHINA	Real Estate	9.0	2.4	6.3	11.9	5.1	26.3	8.5	0.8	17.1
860 HK	O LUXE HOLDINGS	Cons Durables & Apparel	9.8	6.5	5.3	23.9	N/A	N/A	N/A	N/A	N/A
1579 HK	YIHAI INTL	Food, Bev & Tobacco	9.6	3.6	5.3	8.5	23.8	33.9	21.2	4.4	19.7
2669 HK	CHINA OVERSEAS	Real Estate	7.7	3.0	5.3	23.4	19.7	26.6	17.6	6.2	35.6
1589 HK	CHINA LOGISTICS	Real Estate	7.2	1.9	8.6	4.7	61.0	189.2	N/A	N/A	N/A
1681 HK	CONSUN PHARM	Pharms, Biotech	7.7	2.4	5.1	13.9	13.3	16.2	15.4	2.4	22.8
1140 HK	OP FIN INV	Diversified Financials	6.9	2.0	5.1	4.8	N/A	N/A	N/A	N/A	N/A
2001 HK	CHINA NEW HIGHER	Consumer Services	6.9	2.9	5.1	20.9	18.1	36.6	24.1	2.8	16.5
906 HK	CPMC HOLDINGS	Materials	6.7	2.2	5.6	22.7	11.7	29.2	15.6	1.0	8.8
1176 HK	ZHUGUANG HLDG	Real Estate	6.7	2.5	6.2	4.9	N/A	N/A	N/A	N/A	N/A
2099 HK	CHINA GOLD INTL	Materials	6.1	3.7	5.4	14.5	11.6	21.4	11.8	0.5	4.6
1089 HK	LEYOU TECH HLDG	Software & Services	5.5	2.3	5.2	11.5	N/A	N/A	N/A	N/A	N/A
78 HK	REGAL HOTEL INTL	Consumer Services	5.2	1.3	5.0	3.8	N/A	N/A	N/A	N/A	N/A
517 HK	COSCO SHIPPING	Transportation	4.8	1.6	5.0	4.1	15.7	-9.1	N/A	0.6	3.9
1003 HK	HUANXI MEDIA GR	Media	4.7	1.6	5.9	10.8	N/A	N/A	N/A	N/A	N/A
508 HK	DINGYI GP INV	Diversified Financials	4.5	1.2	5.0	9.3	N/A	N/A	N/A	N/A	N/A

Note: above forecasts data are based on Bloomberg consensus forecasts; price data as at 15 January 2018; ADT = average daily turnover

Source: Bloomberg, Huatai HK Research estimates

**Fig.3. Fund flows of 50 largest ETFs tracking emerging market equities**



Source: Bloomberg, Huatai HK Research

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