

Horizon Insights 2023 Investment Strategy Report

New Era, New World, and New Industry

Don Ma

2022/12/12

Horizon Insights Strategy

- **Market Strategy**
- **New Energy**
- **Consumption**
- **Healthcare**

About Us

Horizon Insights, founded in April 2015, is a Chinese institutional research firm providing investment research services to both global and Chinese institutions. We are a leading independent firm in China and work with clients to track China's economy on a real-time basis, corroborate developments on the ground, and formulate, implement and monitor China-related investment theses and strategies. Our research lines include:

- 1. Macroeconomic and commodity analysis**
- 2. Equity research by industry (tech, consumer, health care, and new energy)**
- 3. 'On The Ground' research and company surveys**

Within China, we primarily serve the country's asset management firms including mutual funds, hedge funds, and corporates. Our domestic clients account for over 90% of assets under management in the Chinese fund industry. We are the largest independent research provider covering the China A-Share market and China-related commodities market.

Outside of China, we have actively provided research services to global buy-side institutions since 2016. We have sales teams in the U.S. and Singapore expanding to meet the needs of our growing client base and currently work with some of the largest global asset managers.

Preface: Key Messages from Our 2023 Annual Report

Investors experienced an unprecedented year in 2022. This year, we witnessed a series of significant changes in terms of geopolitical risks, international relationships, climate change, and domestic policies. Therefore, markets experienced huge swings with multiple shocks in 2022, ending with investors recording the worst performance in the past 20 years.

Looking into 2023, markets will continue with much uncertainty. In our 2023 strategy annual report, we will provide a clear investment picture regarding the market by looking into the underlying drivers of the market in 2022. We believe these emerging trends will present a brand new investment framework for 2023.

In 2022, we have been growing with the market. We will continue to polish our analysis and research with this changing environment and strive to provide the best services to our customers.

Preface: Key Messages from Our Previous Reports

Horizon Insights Major Market Calls		
Date	Report Title	Market Views
2020-06	H2 Market Strategy Report: <i>The Second Half of the Bull Market</i>	Upcoming style shift
2020-12	Annual Investment Outlook: <i>Dancing on the Thin Edge</i>	Investment returns are expected to plunge in 2021
2021-07	H2 Market Strategy Report: <i>Hold Back and Wait for Opportunities</i>	Explicitly pointed out that the market is on the peak and there comes the best selling time
2021-12	Annual Investment Outlook: <i>From the Old to the New Growth Engine</i>	The market continues moving in the down trend. The economic slowdown brings a painful time
2022-03	Q1 Market Strategy Report: <i>Inflation 2.0 and Halfway through Market Correction</i>	The bearish market continues, and the price pressure of the macroeconomy shifts from rising PPI to CPI.
2022-05-08	Weekly Strategy Report: <i>Thoughts on Market Bottoming Out and Rebounds</i>	The market sets to rebound, overselling sectors are the key areas to watch out
2022-06-25	H2 Market Strategy Report: <i>Weak Recovery and Softlanding</i>	The market downturn comes to an end, with market sentiments on the top. Wait for the best buying time in September and style rebalancing.
2022-09-25	Q4 Market Strategy Report: <i>Will it Come Around When Market Expectations Go Extremely Sour.</i>	Economic Recovery and Style Shifting

Preface: Horizon Insights A-Share Market Calls

Horizon Insights A-share Market Call and Index Performance





01

From the First Derivative to the Second Derivative

2022 First Derivative Stories: Key Inflection Points in the Economy

Top-down analysis is important in 2022, because the economy is embracing a series of key inflection points that include:

- Global Demand—from strong to weak;
- Commodity Prices/Inflation Growth— from peak to trough;
- Global Liquidity Situation—from tightening to easing;
- Domestic Demand— bottoming out;
- Market Risk Premiums— bottoming out.

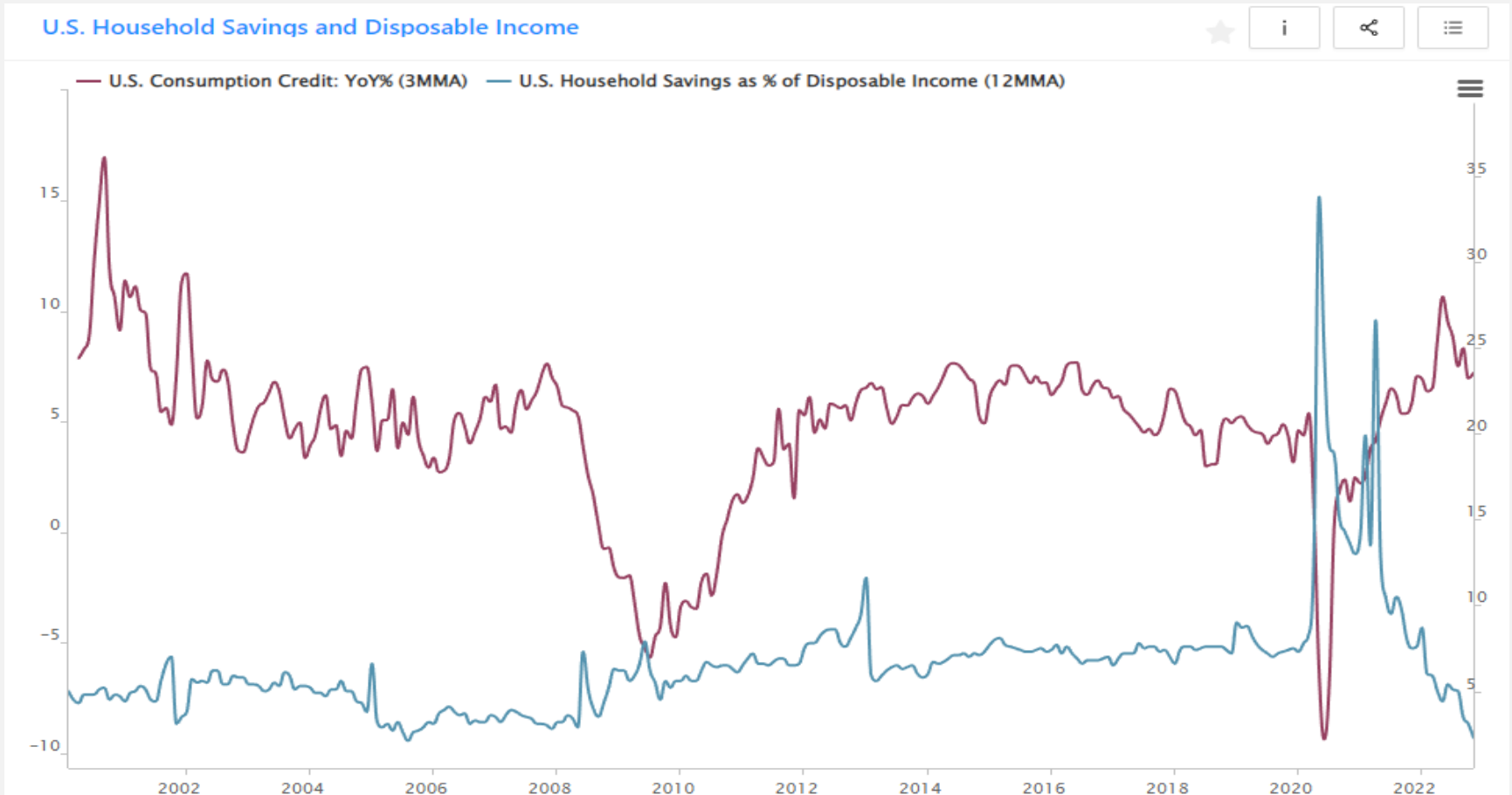
2023—From First Derivative Stories to Second Derivative Ones

In 2023, the market focuses will shift from these First Derivative Stories to Second Ones.

- Continuous Weakness in Global Demand;
- Falling Supply and Declining Prices;
- The world economy may fashion a soft-landing in 2023;
- Domestic demand will edge up from the bottom in 2023;
- Company profits at home will bottom out steadily in Q2 of 2023.

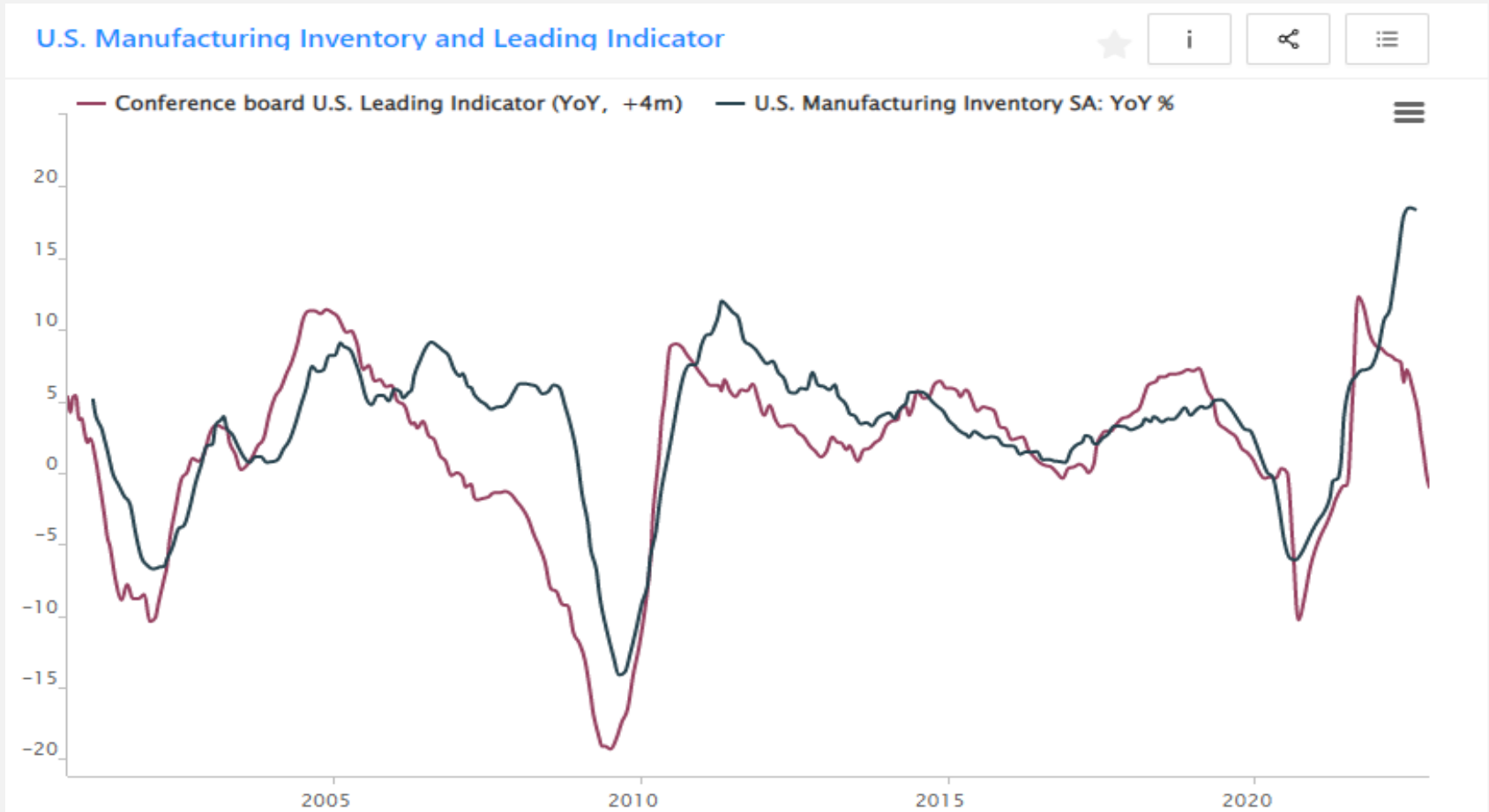
2023—From First Derivative Stories to Second Derivative Ones

- **Falling Demand:** U.S. Household Savings and Credit Debt Expansion Suggest Weak Momentum in Global Demand.



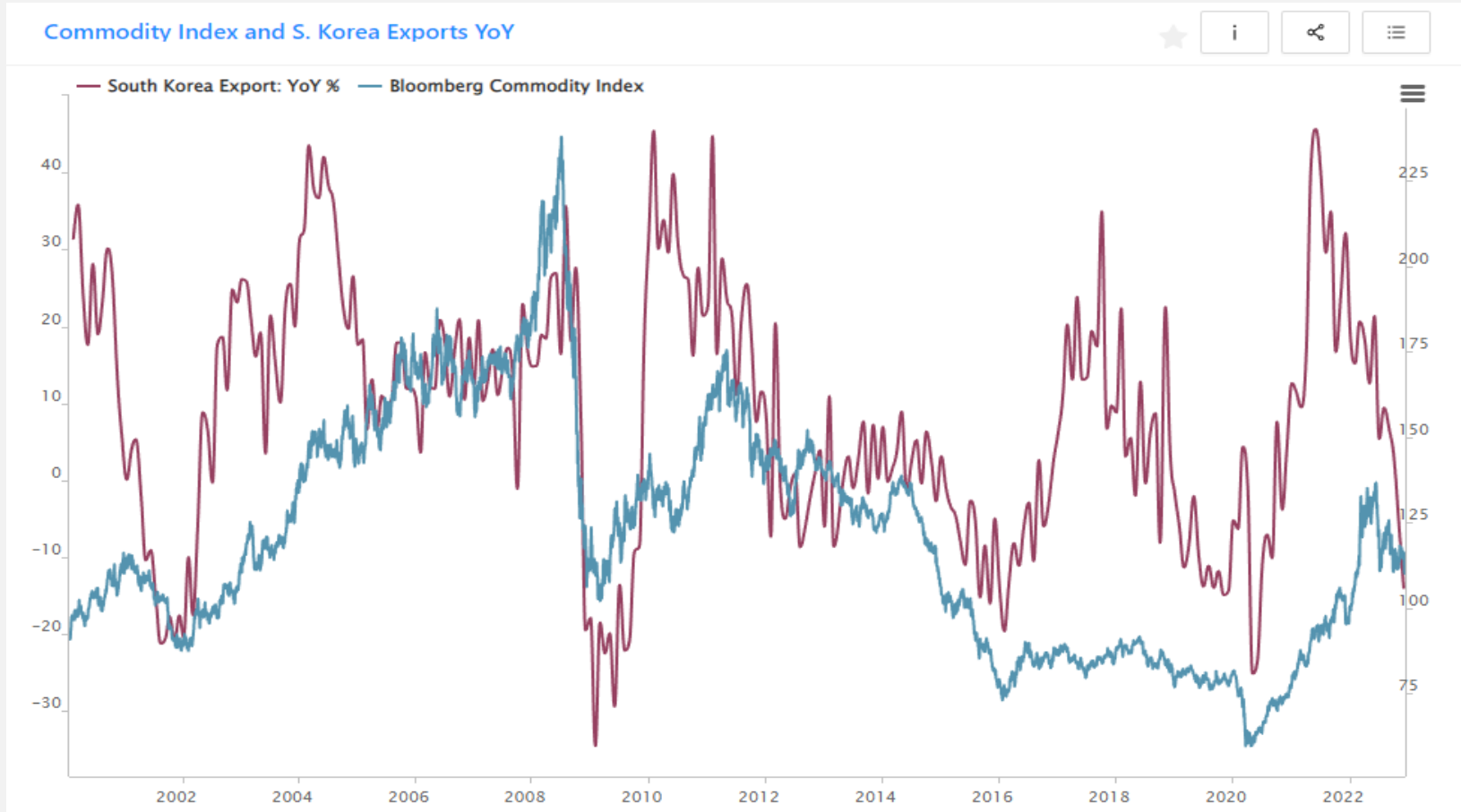
2023—From First Derivative Stories to Second Derivative Ones

- **Destocking:** U.S. Economy Sets to Slow Down as Companies to Cut Inventories



2023—From First Derivative Stories to Second Derivative Ones

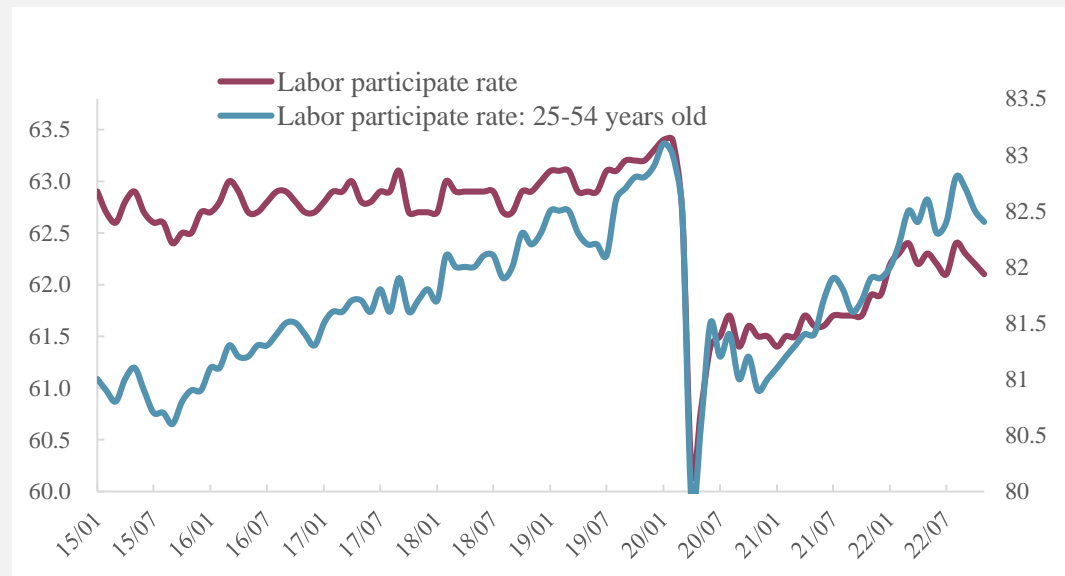
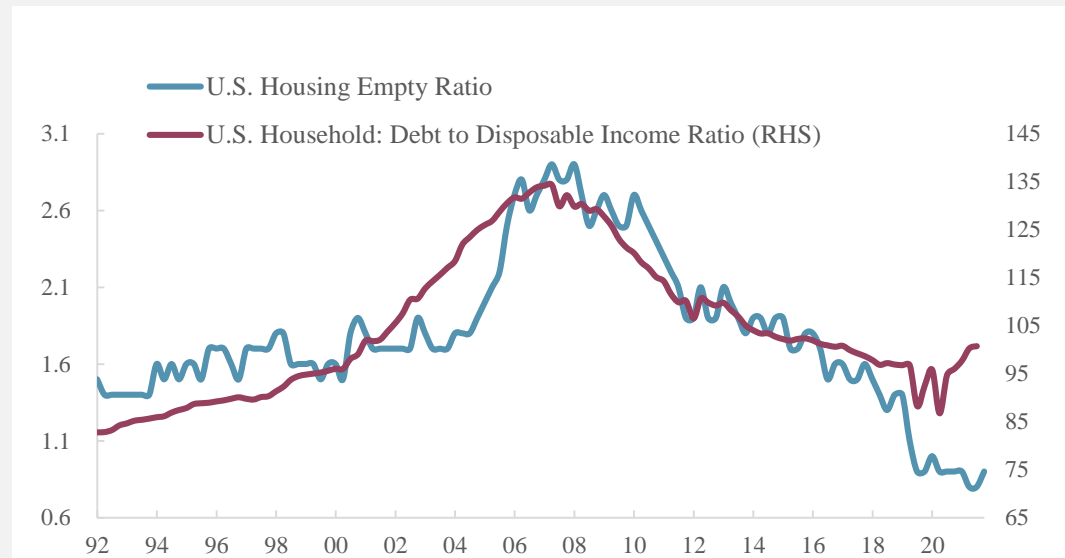
- Falling Prices: With weakening demand in the U.S. and the world, commodity prices will go down with softening supply.



2023—From First Derivative Stories to Second Derivative Ones

A Soft-landing in 2023

- **Healthy Balance Sheets.** Different from 2008, the household sector is quite healthy right now, with debt to disposable income ratio at a low level.
- **Insufficient Supply in the Real Estate Sector.** Also, there is no sign of bubble in the real estate, because U.S. empty housing ratio is at a record low. That suggests insufficient supply despite rising prices.
- **Tight Job Market:** Meanwhile, the labor market is tight because of issues such as early retirements and health concerns. No mass job loss is expected despite Fed rate hikes.



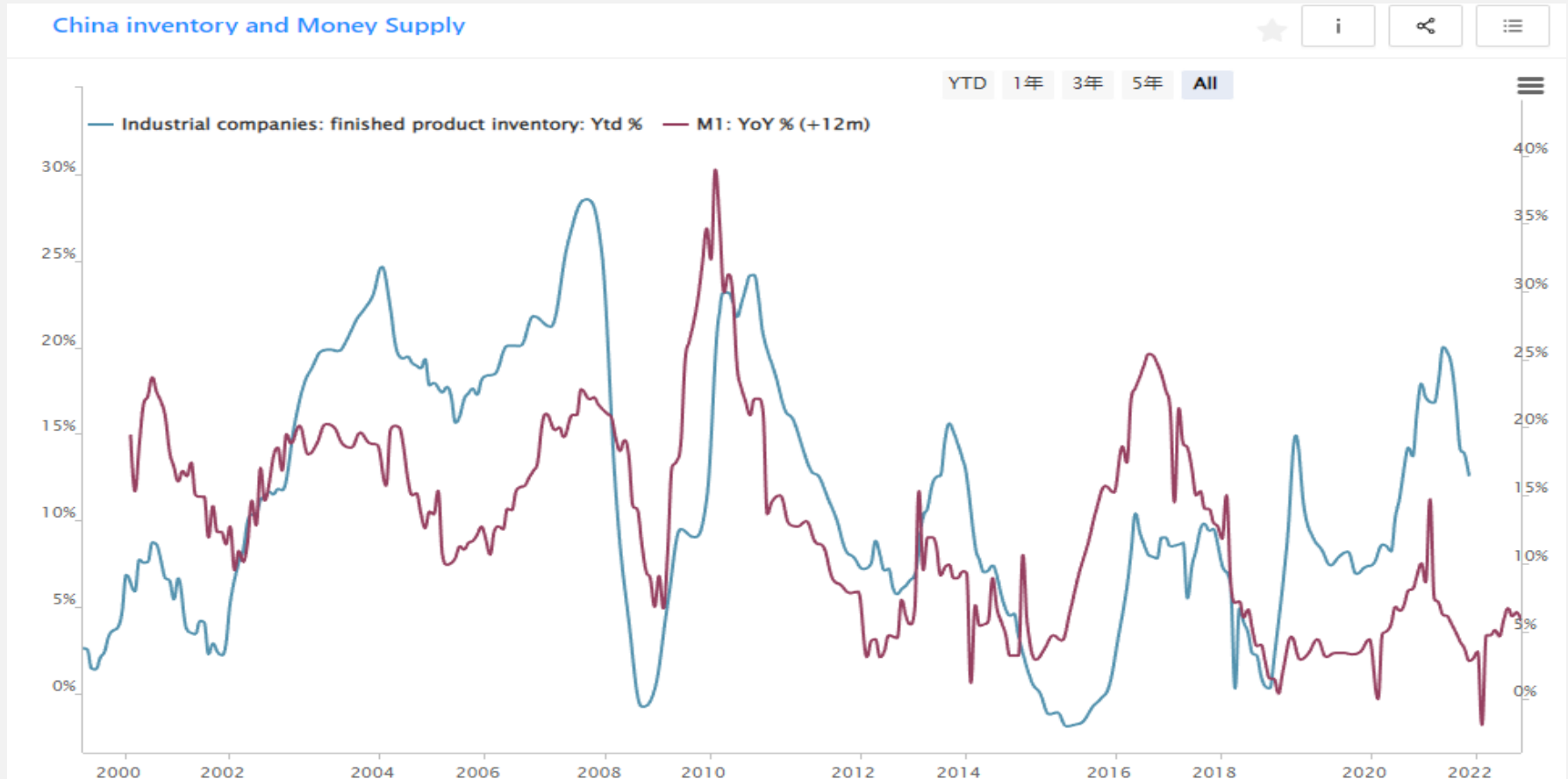
2023—From First Derivative Stories to Second Derivative Ones

- **Economic Recovery at Home.** Climbing out from the trough, domestic demand will improve continuously in 2023. The overall economic growth will be much better than that of 2022.



2023—From First Derivative Stories to Second Derivative Ones

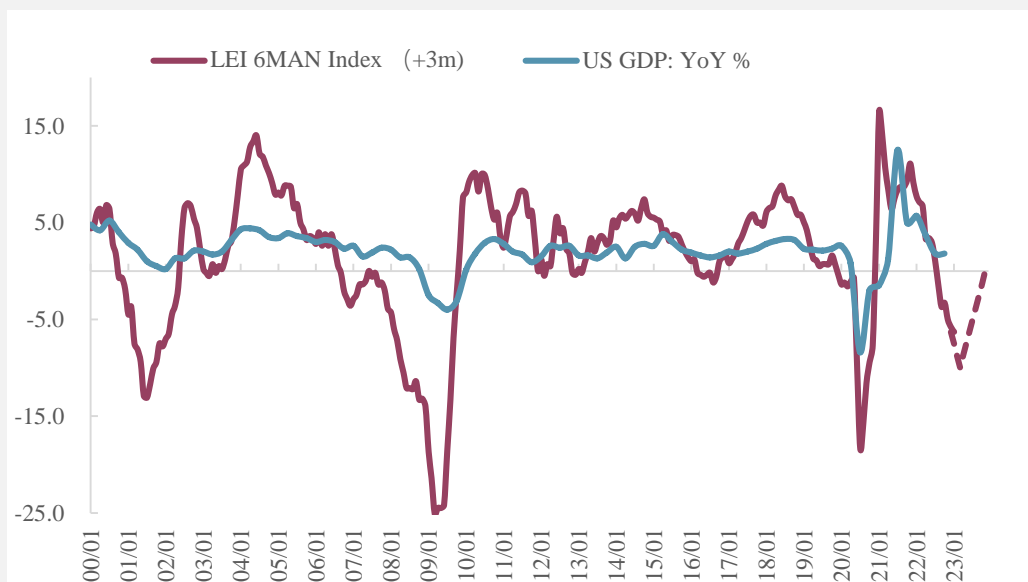
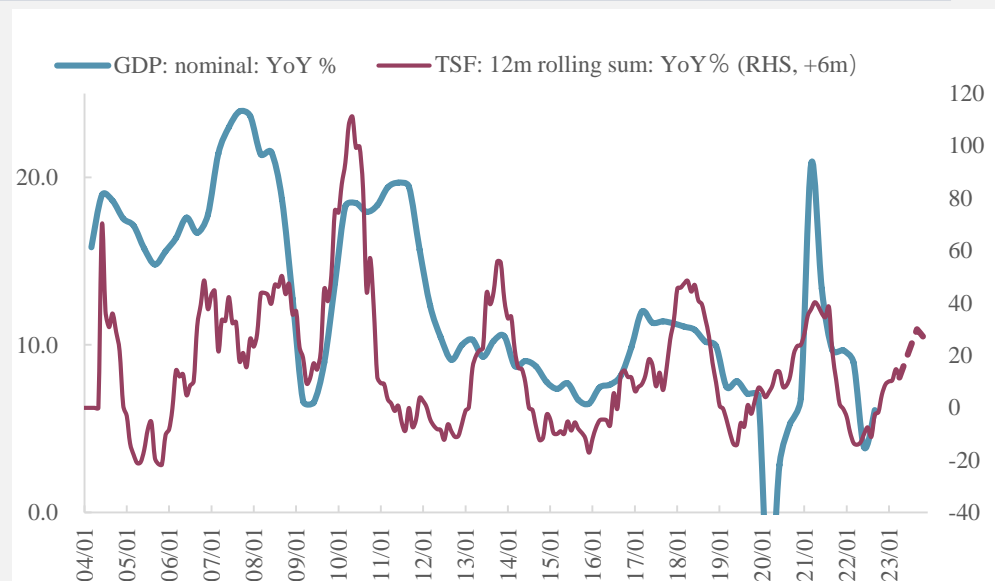
- **Recovery Order:** With the credit growth rebounding, we will see a turnaround in company inventories, and company earnings will recover from the bottom.



2023—From First Derivative Stories to Second Derivative Ones

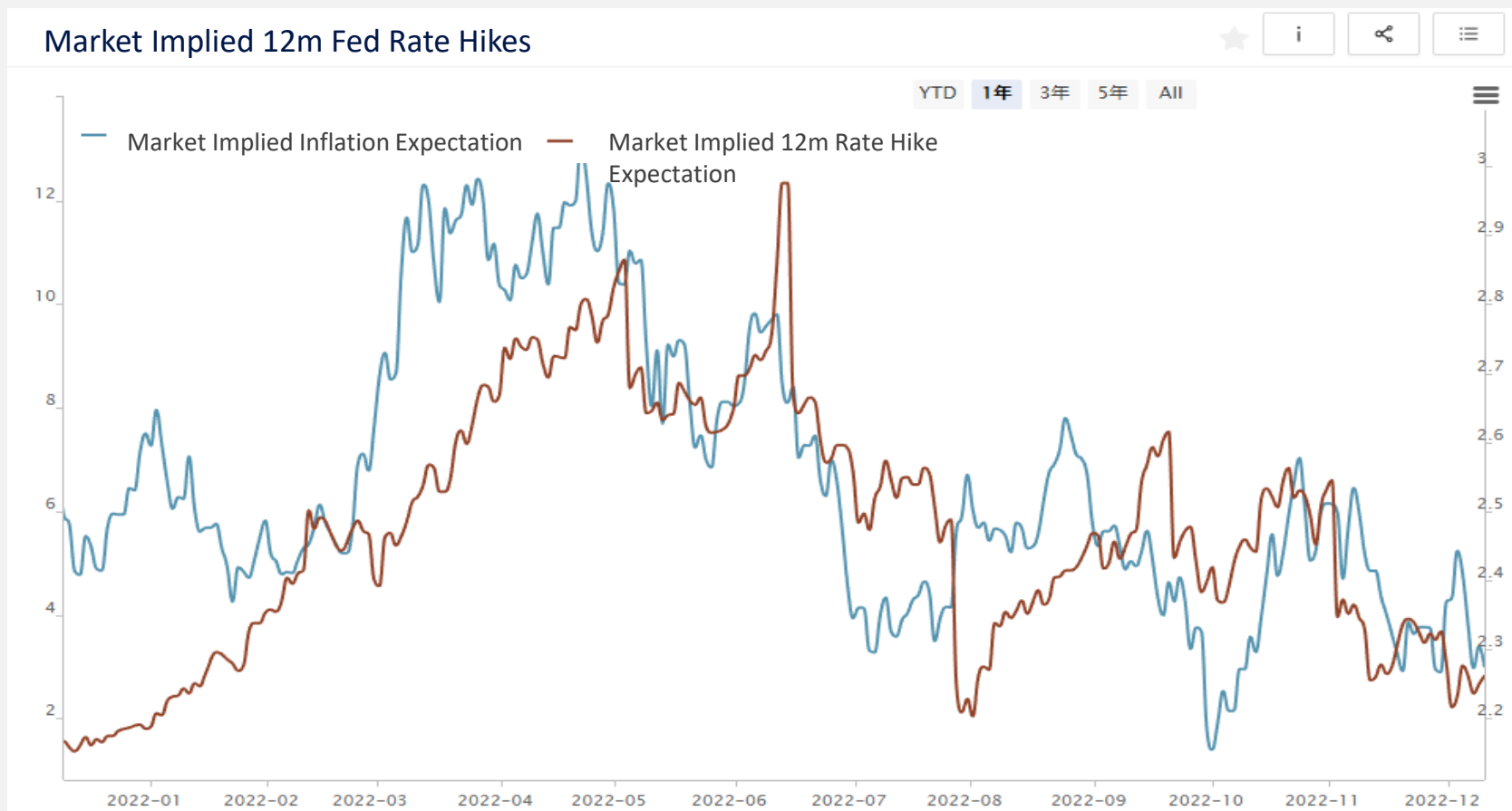
Mismatching Pace of Economic Recovery Between China and the U.S.

- **Modest recovery in China with headwinds being left behind:** a turnaround in Covid-zero policy and continuous property policy from the government.
- U.S. declines into a recession in H1 because of Fed QT.



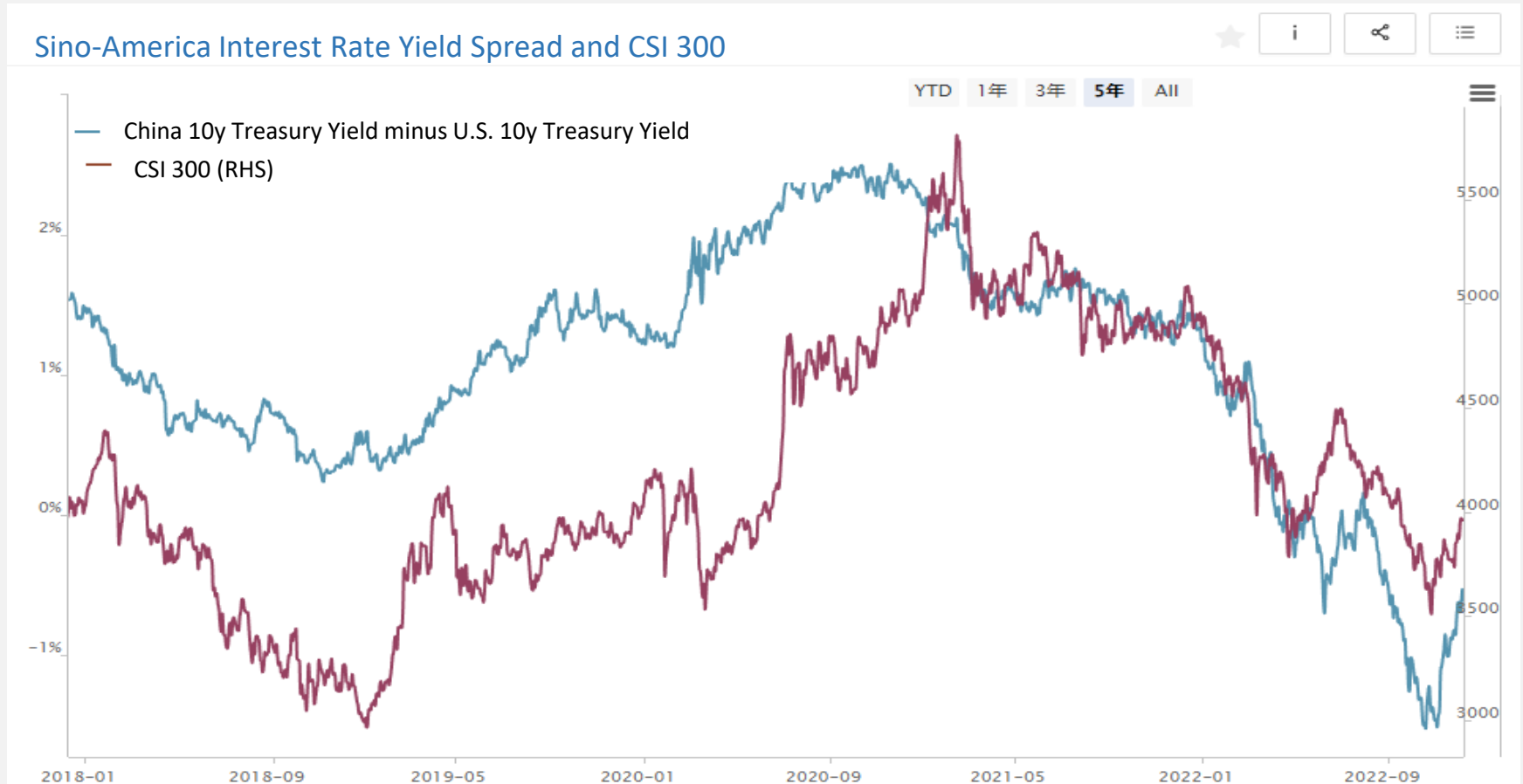
2023—From First Derivative Stories to Second Derivative Ones

- Monetary Policy in the U.S.: Dovish Pivot with Falling Price Pressure



2023—From First Derivative Stories to Second Derivative Ones

Overall, the economy has followed a similar rule in history. Despite with different drivers, it also swings from recession, recovery, prosperity and stagflation.



2023—From First Derivative Stories to Second Derivative Ones

2023 Macro-economic Environment:

In 2022: China's credit growth is flat, with the PPI growth going down;

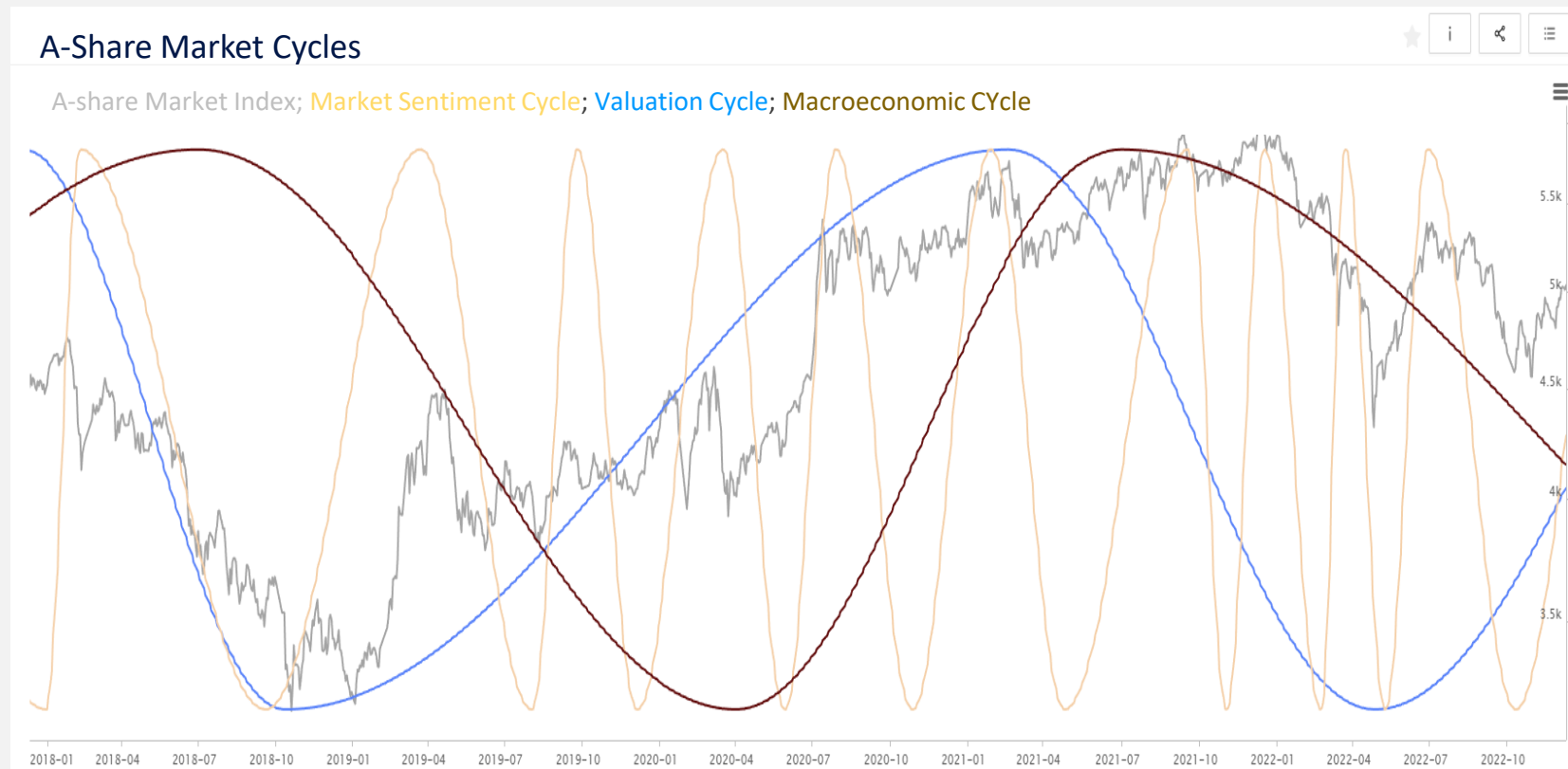
In 2023: China's credit and PPI growth will both edge up together;

Growth to outperform value: In history, growth stocks outperform value when the economy swings from recession to recovery .



The Market Pace will Become Less Important in 2023

- **Market Already Bottoming Out:** as the market sentiment and valuation bottomed out in Q2 of 2022, the A-share market has finished its downward movement already.
- **Earnings to recovery in Q2 of 2023:** With the macro setting in 2023 (demand recovery at home versus falling demand overseas), the PPI growth will continue to trend down, and we expect company earnings to bottom out in Q2 of 2023.





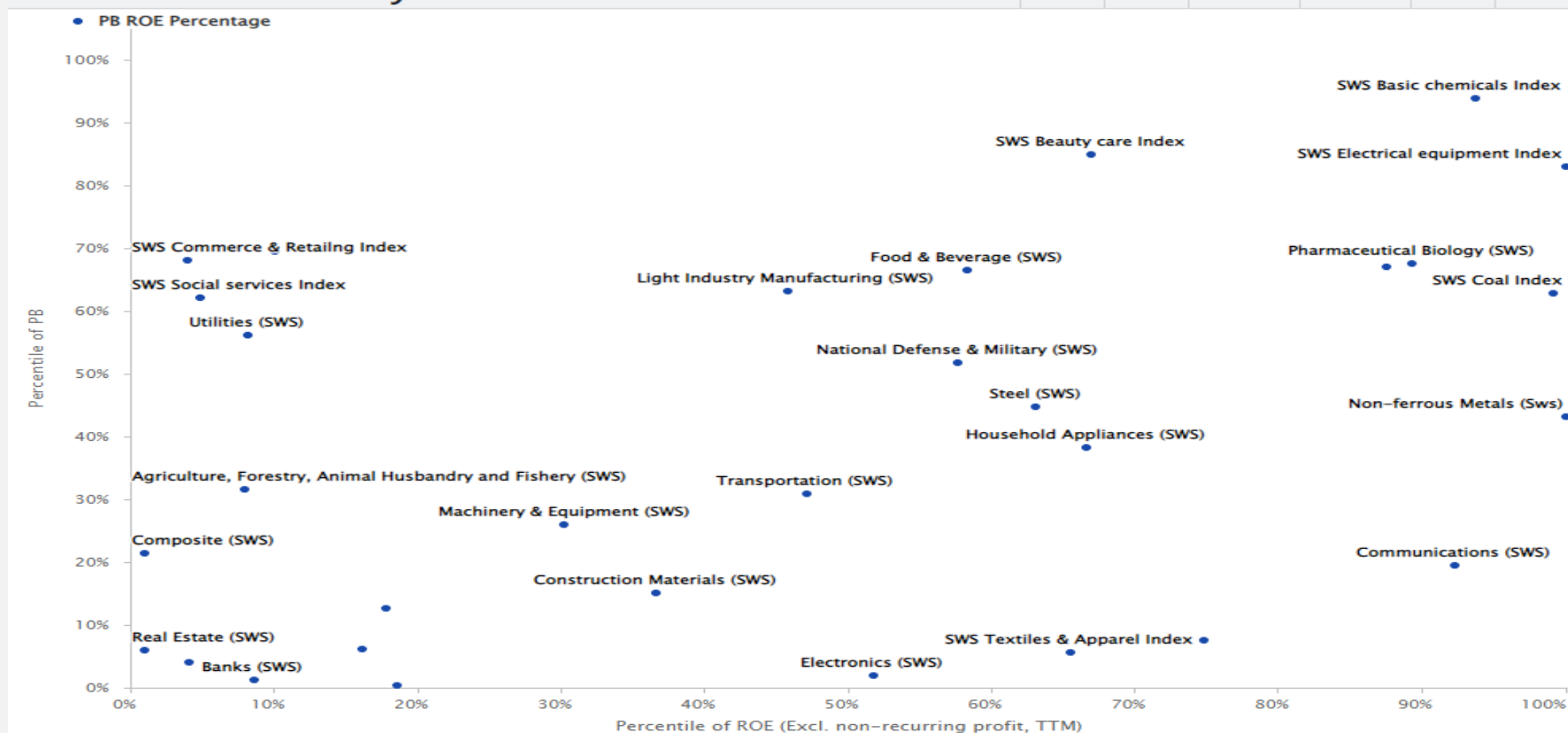
02

Looking for the New Trend

Investment Theme: Dilemma Reversal Strategy not yet Ending

- **Cautious Mood:** with many sectors still in the right lower hand (*high ROE but low PB*), the market is cautious.
- **Reopening Trade:** despite reopening hopes, the market appears concerned, with low valuation sectors still at the bottom. Pessimistic expectations are there on electronic and oil stocks.

PB ROE Percentile by Sectors



Sector Reversal is A Clear Investment Thread in 2023.

- Services sectors set to have improving prosperity in 2023.



From Reversal to New Industrial Development—Dividend Strategy

High-dividend Strategy, which avoid low-valuation traps, can provide stable investment returns.

- **Stock Changing Period:** January Each Year
- **Stock Selection Rules:** exclude stocks in the bottom 30% (falling ROE_TTM) and choose the top 10 companies with the highest dividend yields.
- **Strategy Performance:** from 2010 till now, an annual investment return: 14.62%. For most of time, our high-dividend strategy outperformed the A-share market index, with the maximum drawdown of 48.07%, better than the market's 55.99%.

Back testing Period: From 2010 to 2022/11/22 (ROE)



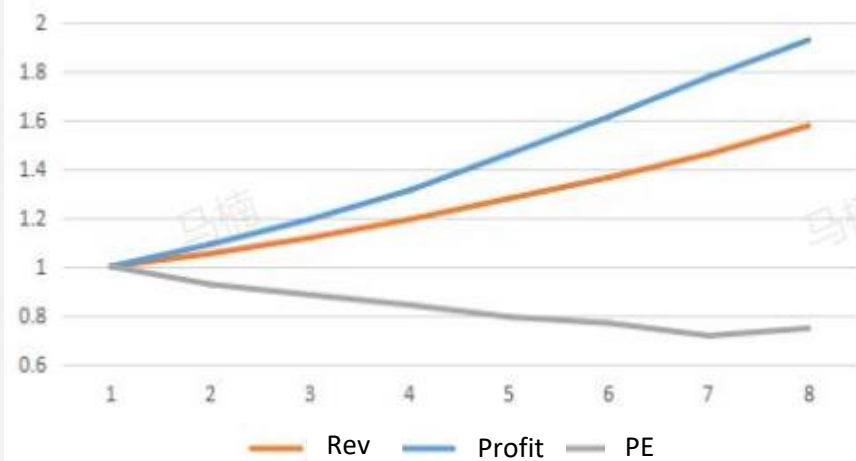
Historical Lessons: Profits Support High Market Valuation

According to our calculation, market multiples declined for high-valuation stocks, regardless winners and losers.

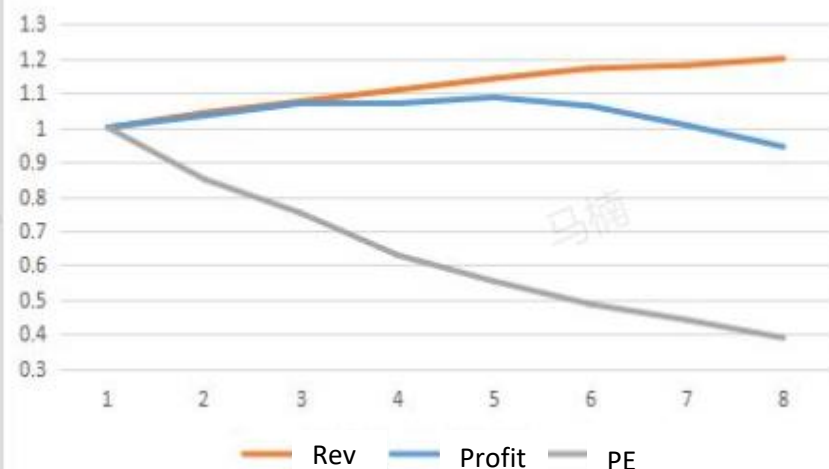
- For high-valuation winners, PE readings usually fell by 20% (thanks to robust earnings).
- For high-valuation losers, PE multiples plunged by 60%.
- Continuous profit high growth rates are the key driver for high-valuation winners to outperform the market.

High-Valuation Stock Performance: Revenue, Profit and Market Valuation (Rebased)

50 Plus Multiple Winners

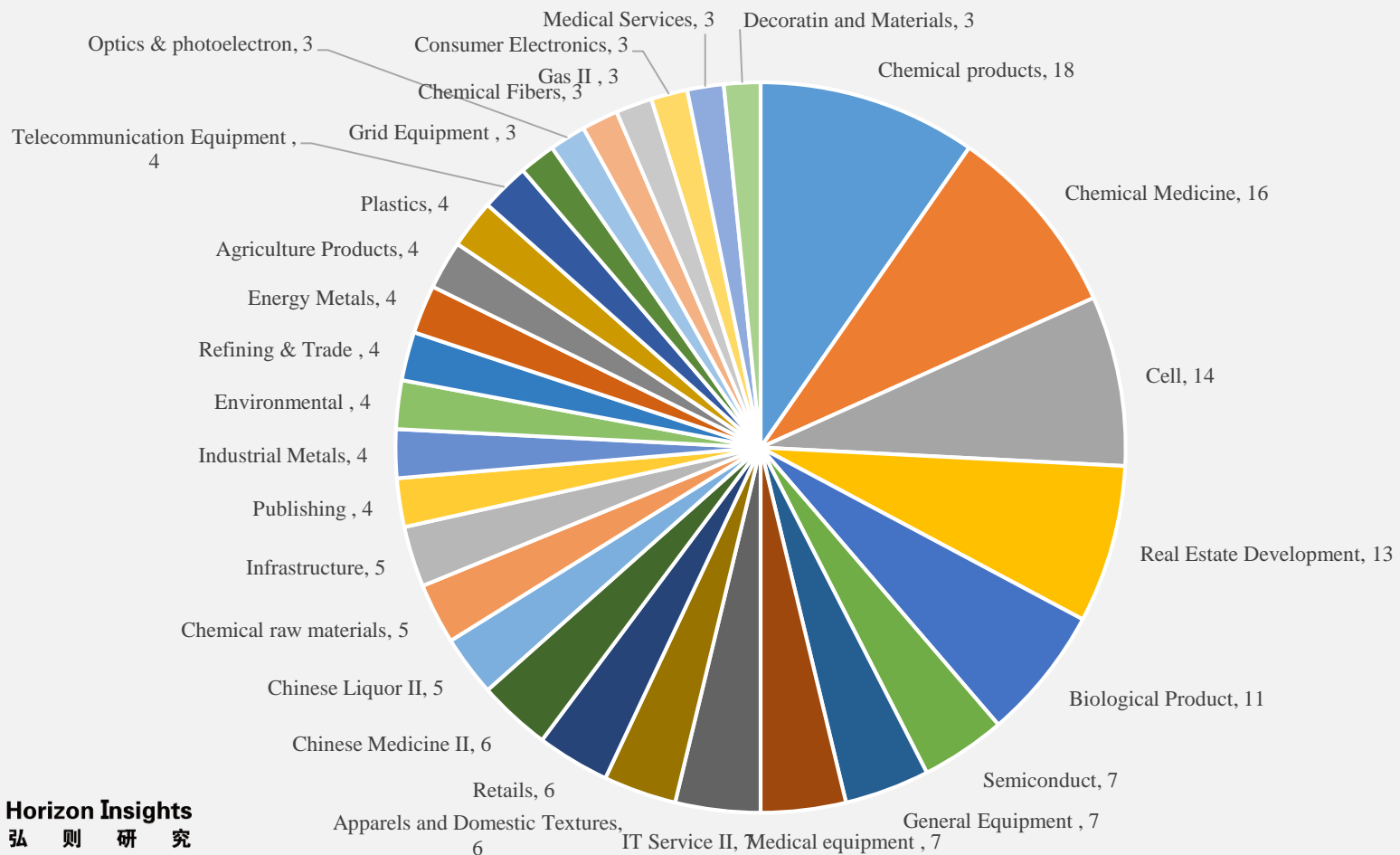


50 Plus Multiple Losers



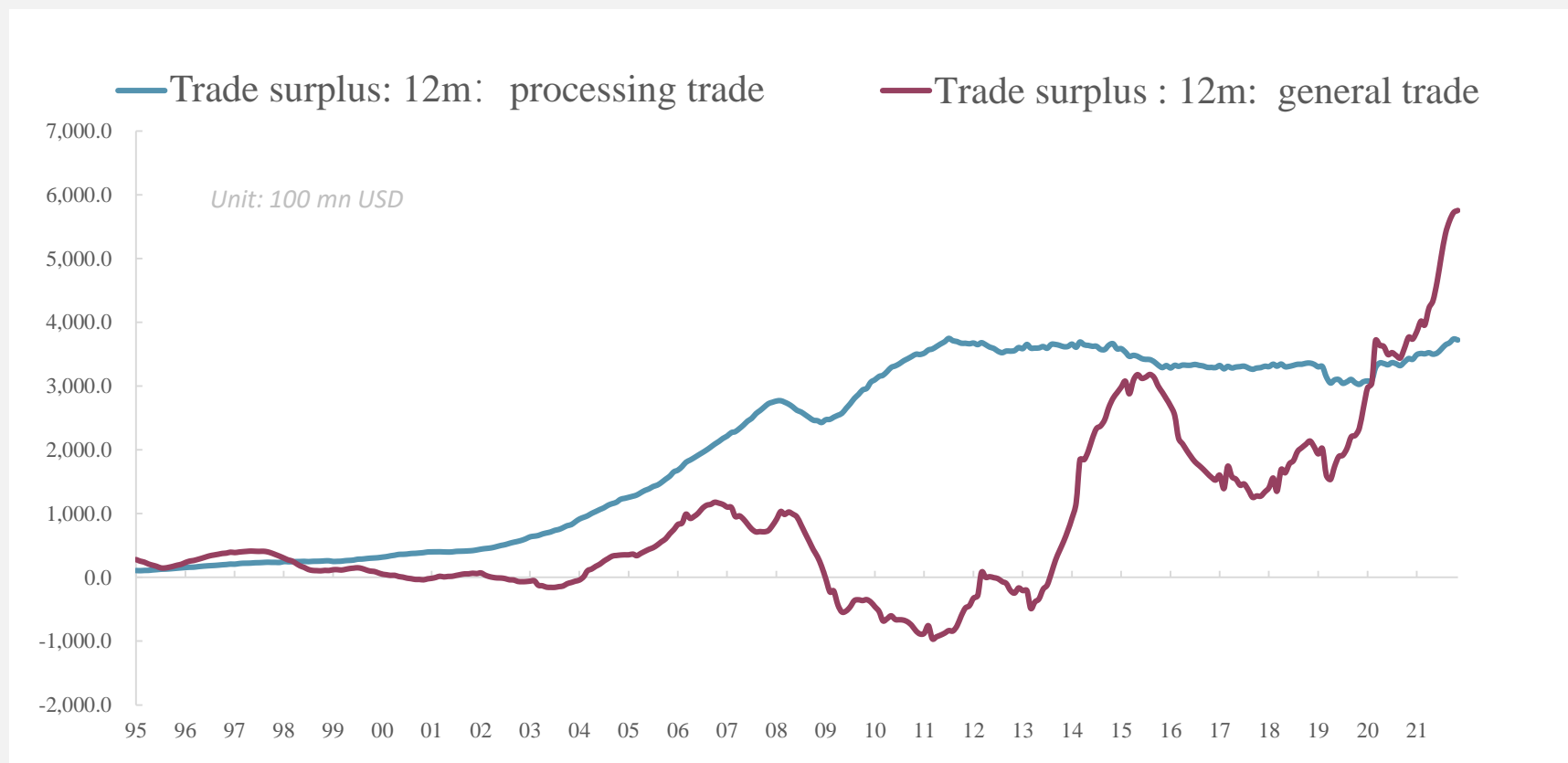
Capacity Expansion—Prior-condition for Profit to Double up

- **Selection Standard:** top 300 companies with highest construction under process as % of total fixed asset investment;
- **Key Areas to Watch:** Chemical products, chemical medicine, electric battery, and biological products.



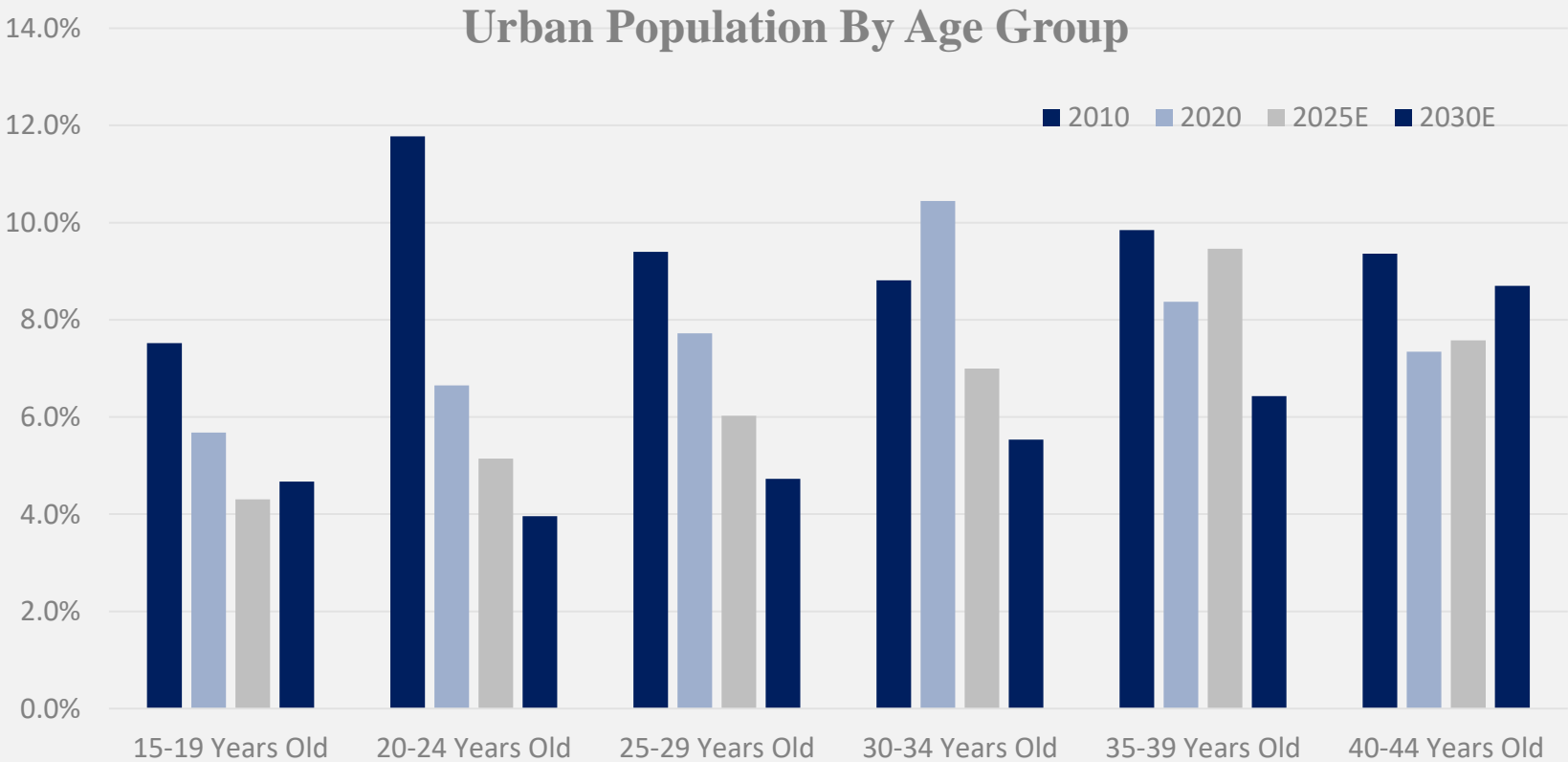
New Growth Leads—the Rise of Local Brands

- **Improving export structure:** before August of 2021, processing trade has been a major pillar for Chinese trade surplus. From 2020, however, general trade has generated more in terms of trade surplus. Such a change signals improving manufacturing ability of China.



From Demographic Change to See Consumption Trend

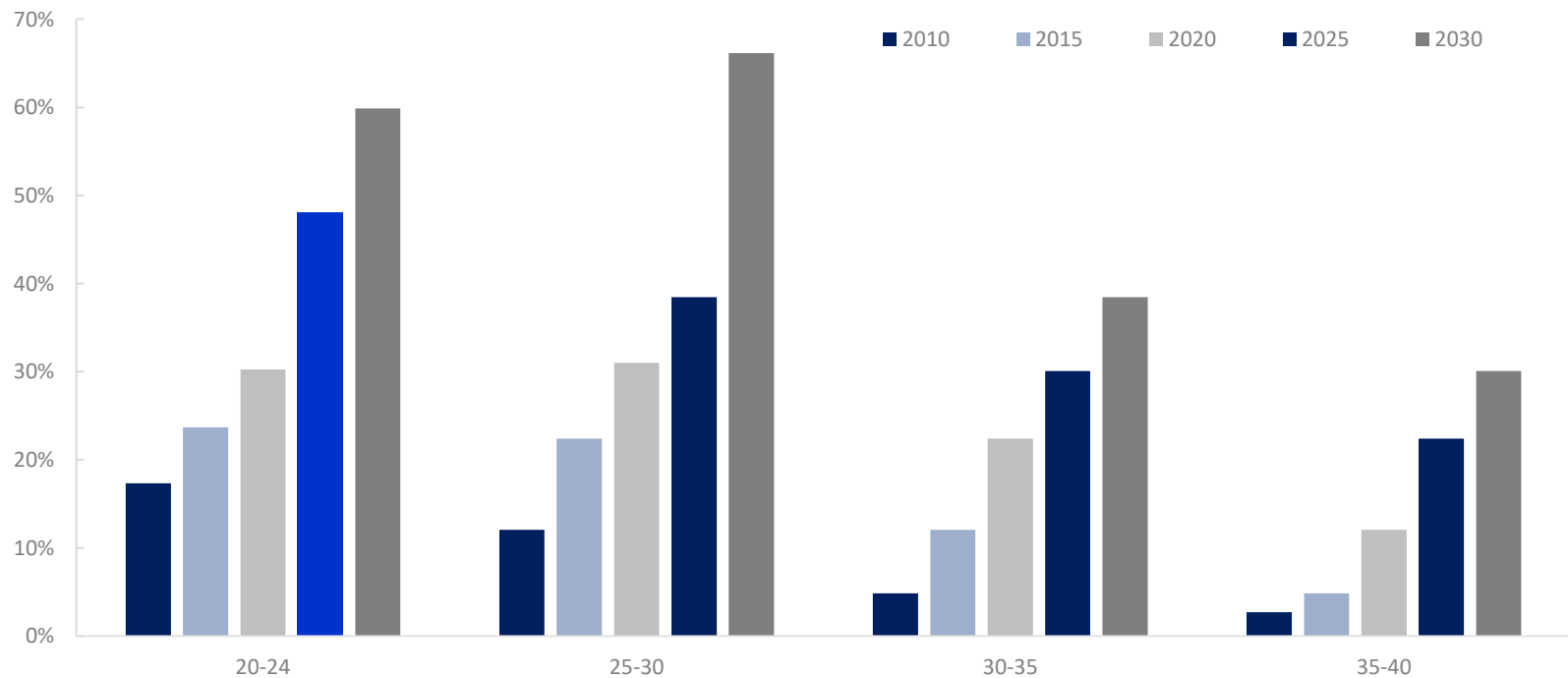
- **When the 80's to enter their 40+:** Right now, China's 80's and 90's will enter their prime age, a wave of population peak for the age of 40+.
- **Healthcare & family-related demand** will have stable growth as a group of people will enter their 40's in the next five years



From Demographic Change to See Consumption Trend

- **More Well-educated Young People:** Meanwhile, the ratio of college education for the young people (less than 30 years old) will rise up, as a result of broader government efforts.
- **25 years old & mass consumption brands:** 25 years old will become the threshold for consumption: demand for low-and-middle price necessary products will rise. New brands for mass consumption will increase accordingly.

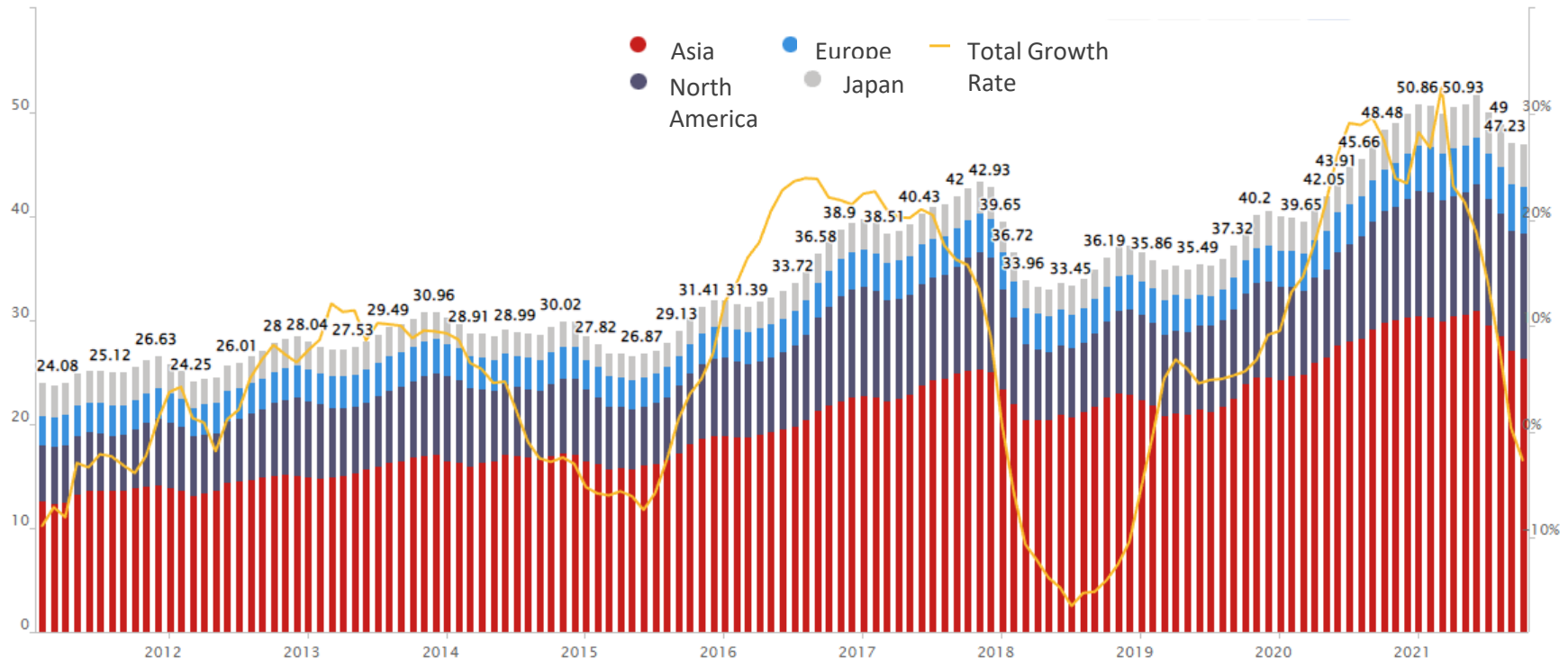
College Graduation as % of Total By Age Group



Industrial Trend—Time to Prepare for 2024-2025

- **Semiconductor industry sets to bottom out in Q2 of 2023:** with a cyclical move of 4 years, we think the semiconductor industry will bottom out in Q2 of 2023, after it entered the downward trend since June of 2021.

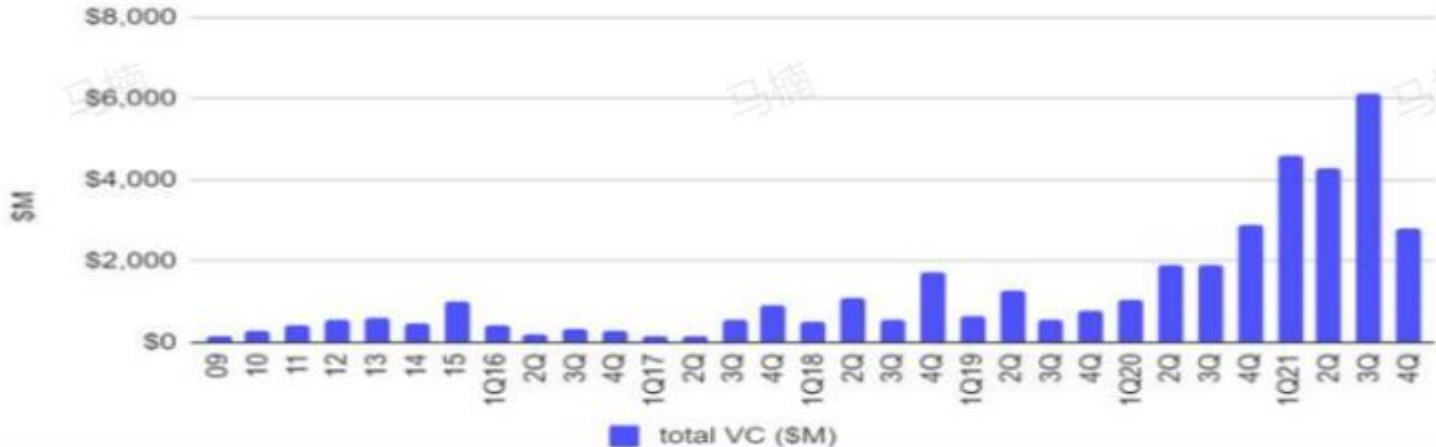
Global Semiconductor Sales By Country and Year-over-Year Growth Rate



Industrial Trend—Time to Prepare for 2024-2025

- Synthetic Biology.

Synthetic biology Overseas Fund Raising (100 mn USD)



Synthetic biology Overseas Investment Scale per Project and Number of Cases

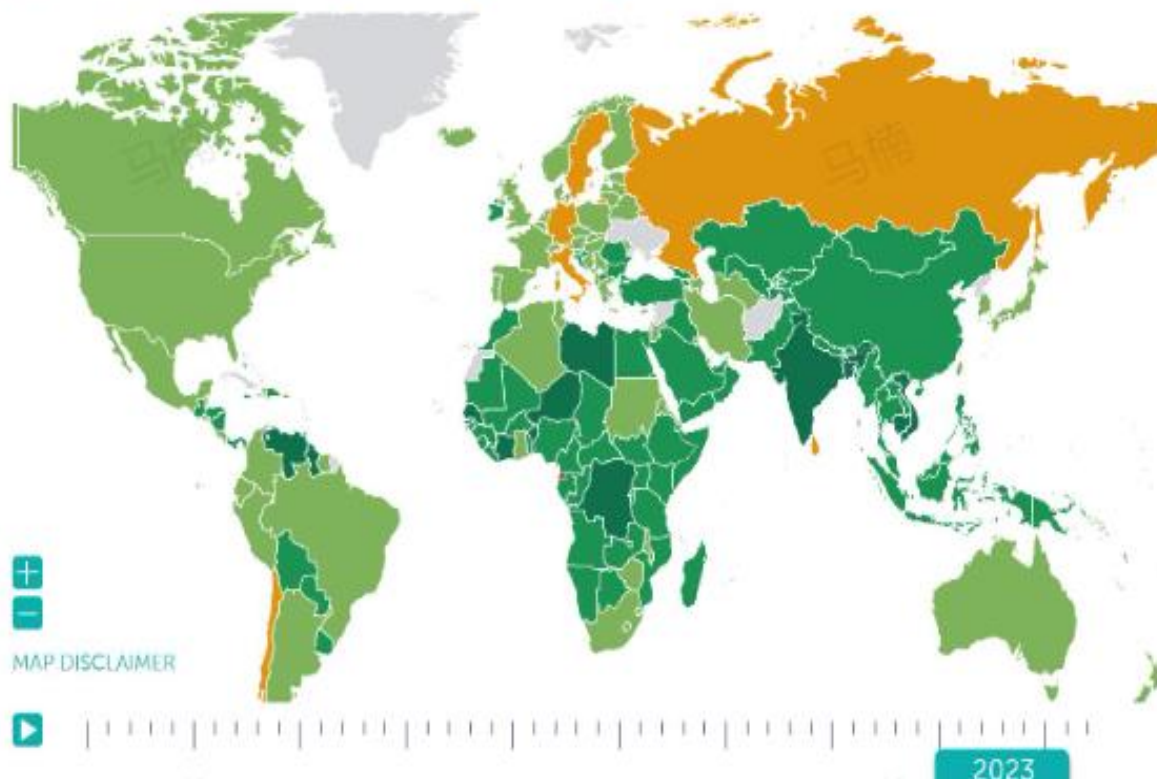


World Economy—G2 or G4?

The New Growth Engine: India and ASEAN countries

MAP (2023)

● 6% or more
 ● 3% - 6%
 ● 0% - 3%
 ● -3% - 0
 ● less than -3%
 ● no data



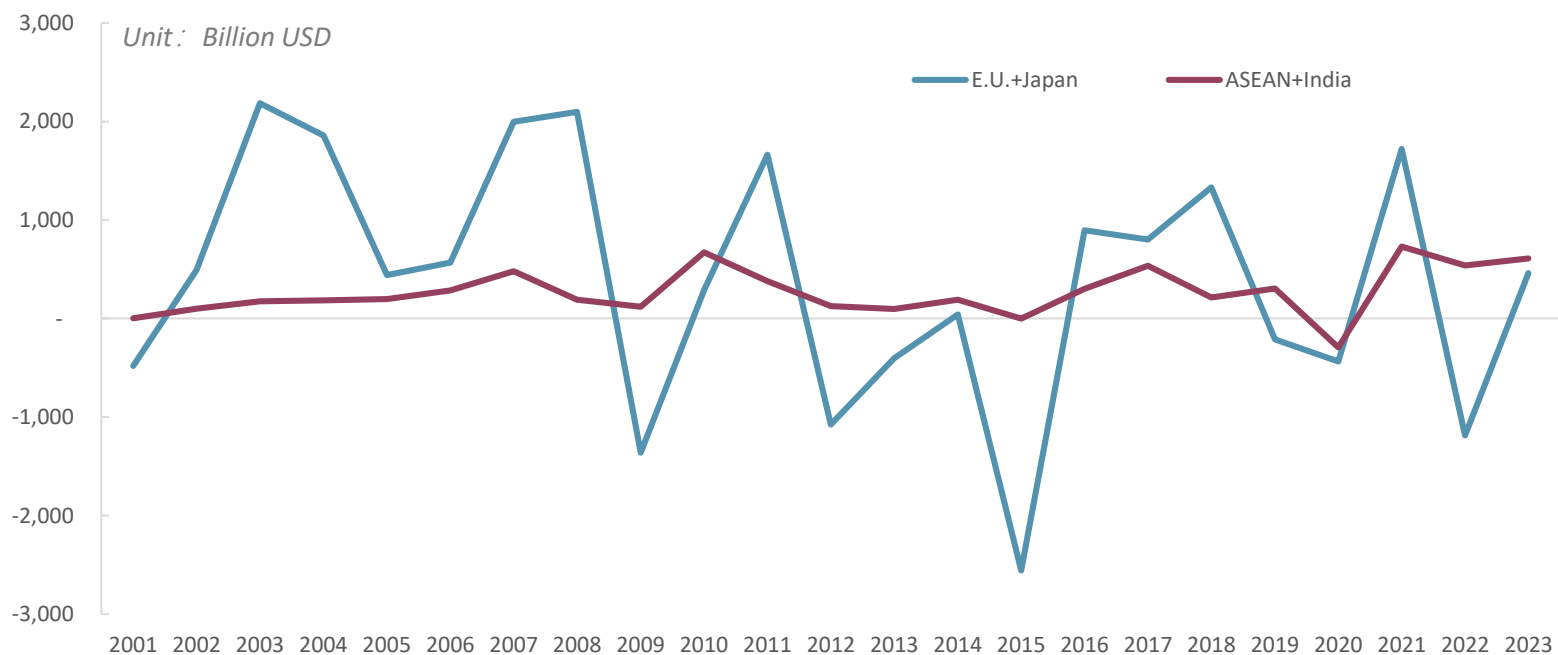
LIST (2023)

Country	Region	Analytical group	Value
		Analytical group	Value ^
		ASEAN-5	4.9
		Emerging and Developing Asia	4.9
		Emerging market and developing economies	3.7
		Sub-Saharan Africa	3.7
		Middle East and Central Asia	3.6
		World	2.7
		Other advanced economies	2.3
		Latin America and the Caribbean	1.7
		Advanced economies	1.1
		Major advanced economies (G7)	0.8
		European Union	0.7
		Emerging and Developing Europe	0.6

World Economy—G2 or G4?

- In 2023, India and ASEAN Countries will outrun the European Union and Japan to contribute more GDP gains.

Incremental GDP: E.U.+Japan versus ASEAN +India



In Summary

- **Macro economy will play a less important role in 2023.** Overall, the economy will continue with what has been developed in 2022. Interest rate yield spreads between the U.S. and China, RMB exchange rates, and the relationship between PPI and Chinese credit growth will have some impact on the market, both on the pace and on the structure of the A-share market.
- **From recession to recovery, we expect the market to deliver an investment return of 10% in 2023.** Widening investment returns will be seen among different sectors. Specifically, dilemma reversals, improving consumption, and industrial upgrading are key areas we eye great opportunities in 2023. With economic recovery, we expect the downstream sectors will outperform the upstream ones. And domestic demand will be stronger than export demand next year.
- **Most importantly, for 2023, it is the time to find the growth opportunity and prepare for the upswing in 2024 and 2025.** In the short run, the demand side story matters the most. While in the long run, it is the supply side decides the long-term development trend. Therefore, we see demographic change in the next 5 years will bring in huge changes for investment opportunities. So does the new industrial development. Mass consumption will breed more new brands. Revolutionary changes will be seen in biological technology, and a new cyclical force in technology is also a key area to closely watch in 2023.



Thanks!

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