



China Consumer: Recovery & Opportunity

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Portfolio Manager

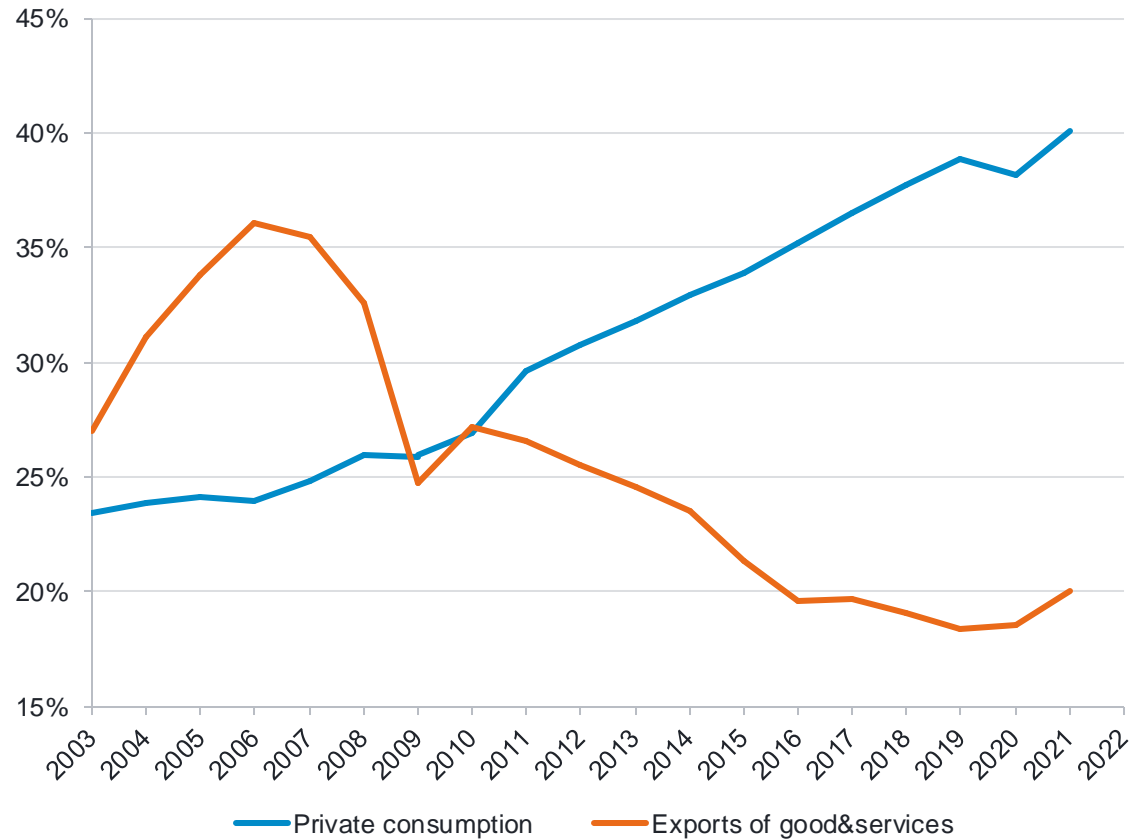


September 2023

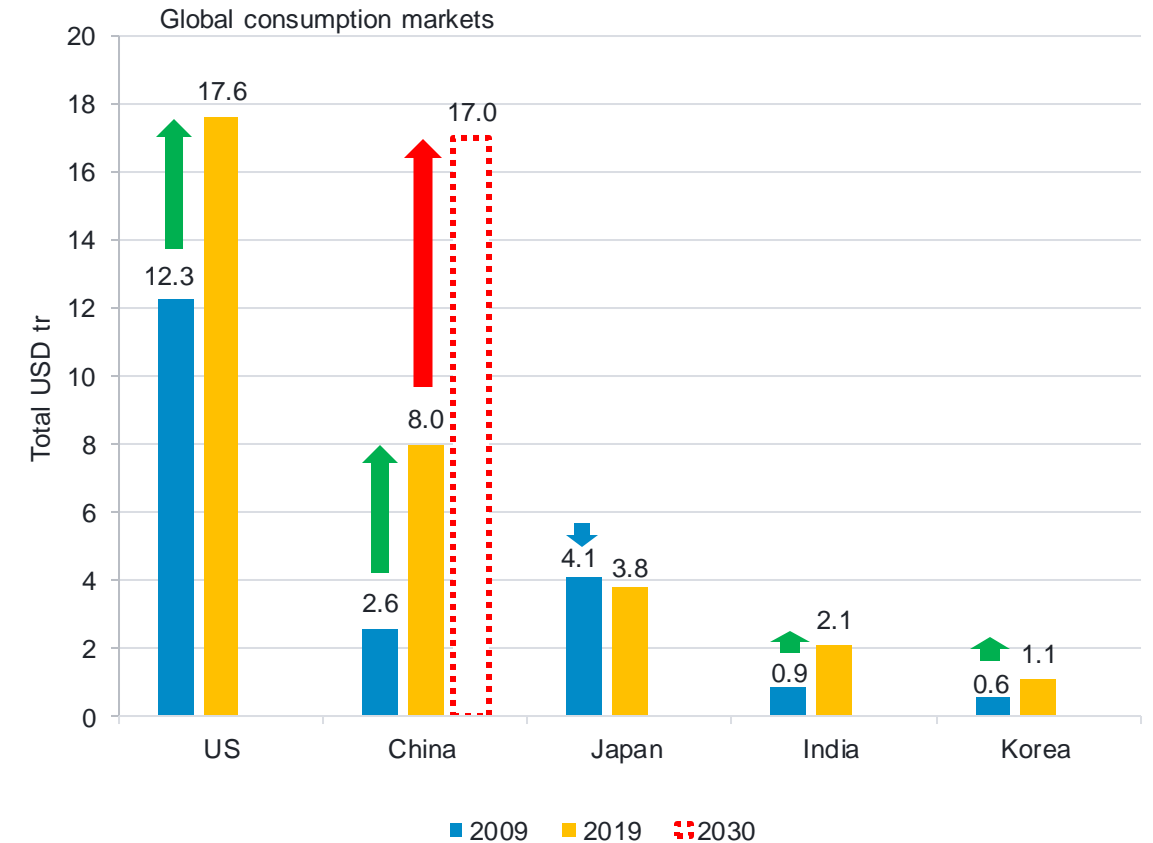
Own beneficiaries of China's structural shift toward consumption driven economy

China consumption opportunities are large and growing fast

China consumption as % of total GDP continues to grow



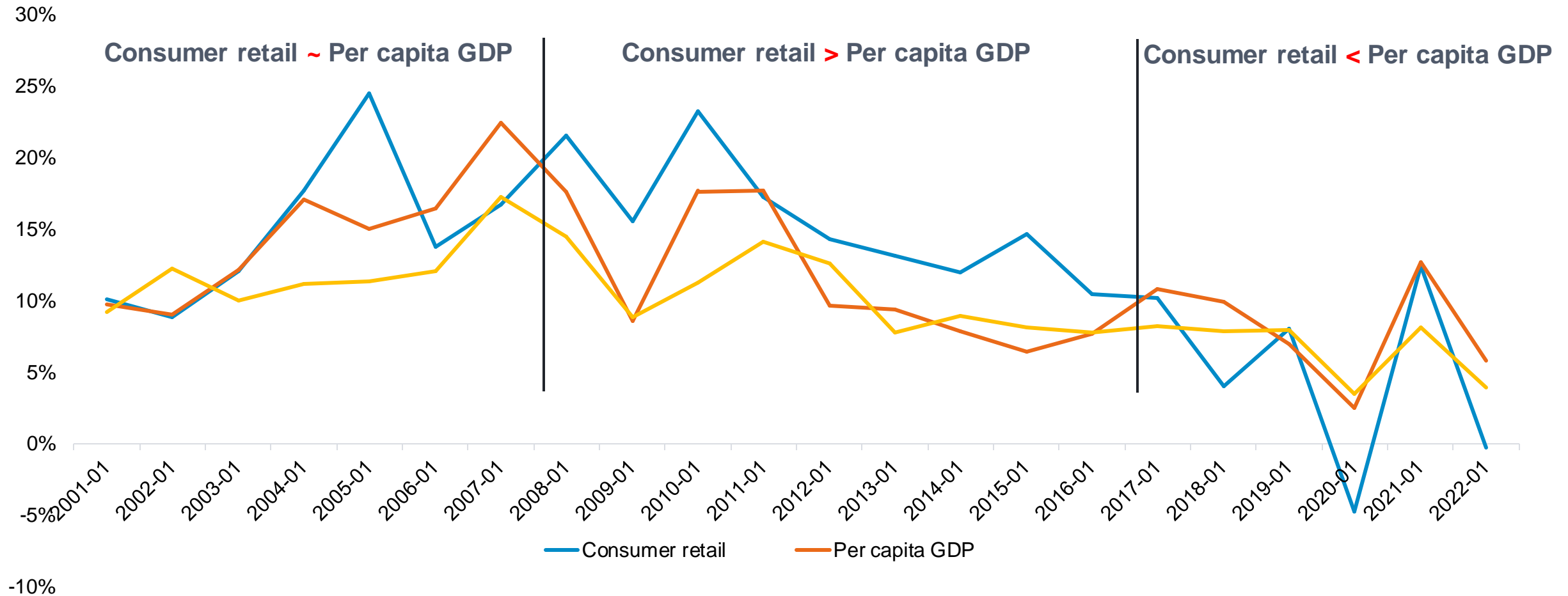
One of the fastest growing and largest consumption markets



Source: Refinitiv DataStream, Worldbank.org, August 2022.

Consumption growth lagging GDP growth: Structural or cyclical?

2001-2022 YoY consumption growth vs. per capita GDP growth vs. disposable income growth

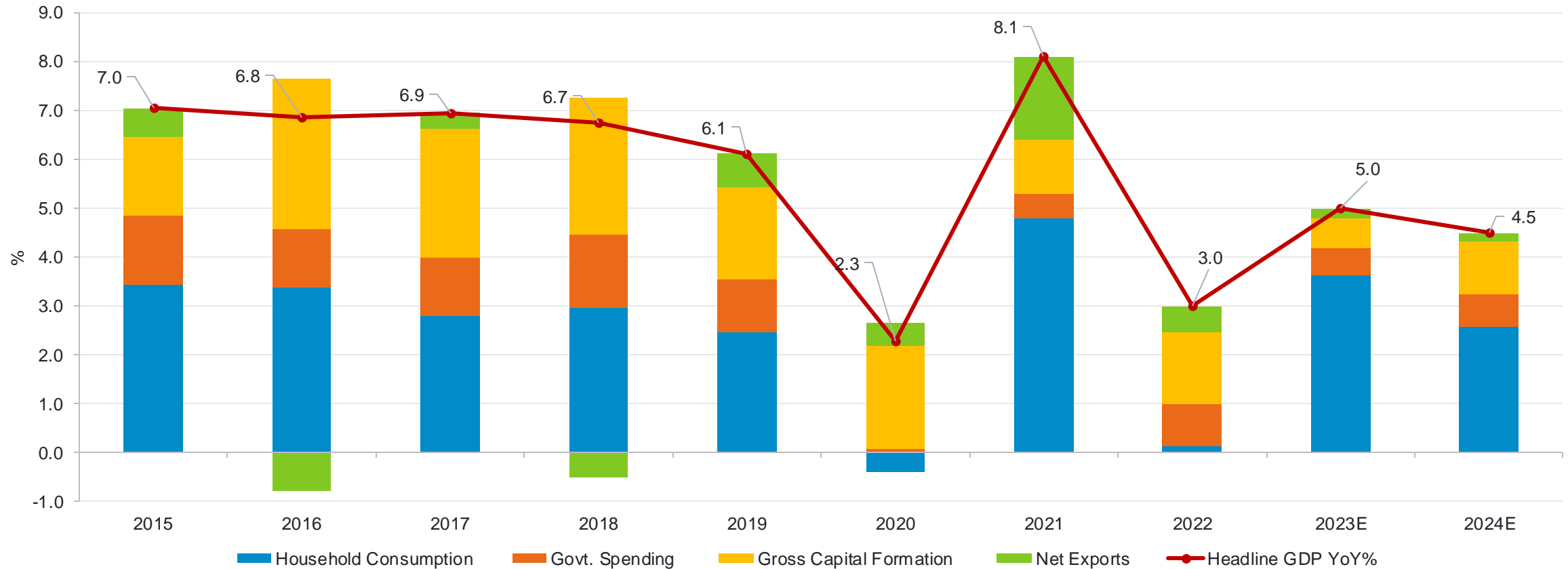


Source: NBS, 30 September 2023

GDP growth backdrop

2023 still a year of recovery driven by household consumption

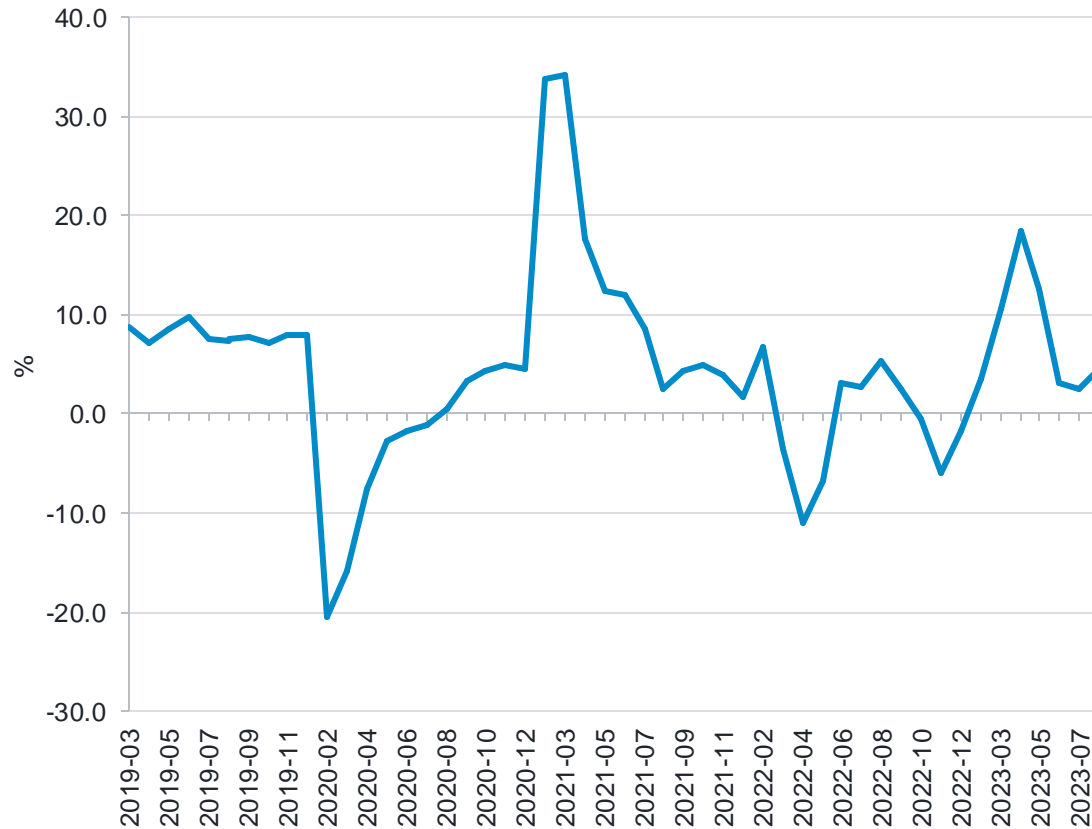
Contribution to growth



Source: NBS, Morgan Stanley Global Research, 17 July 2023

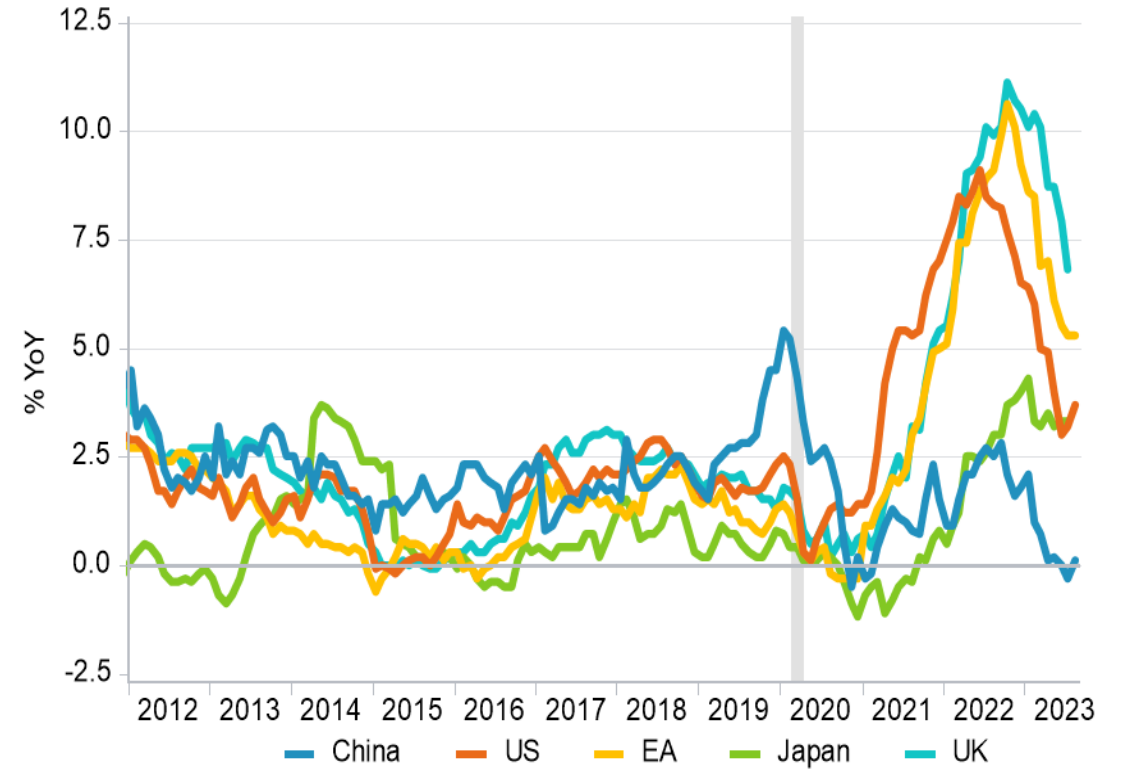
However, retail sales recovery is patchy while CPI remains weak

Real retail sales YoY



Source: NBS, Fidelity international, 31 August 2023.

Global headline CPI rates



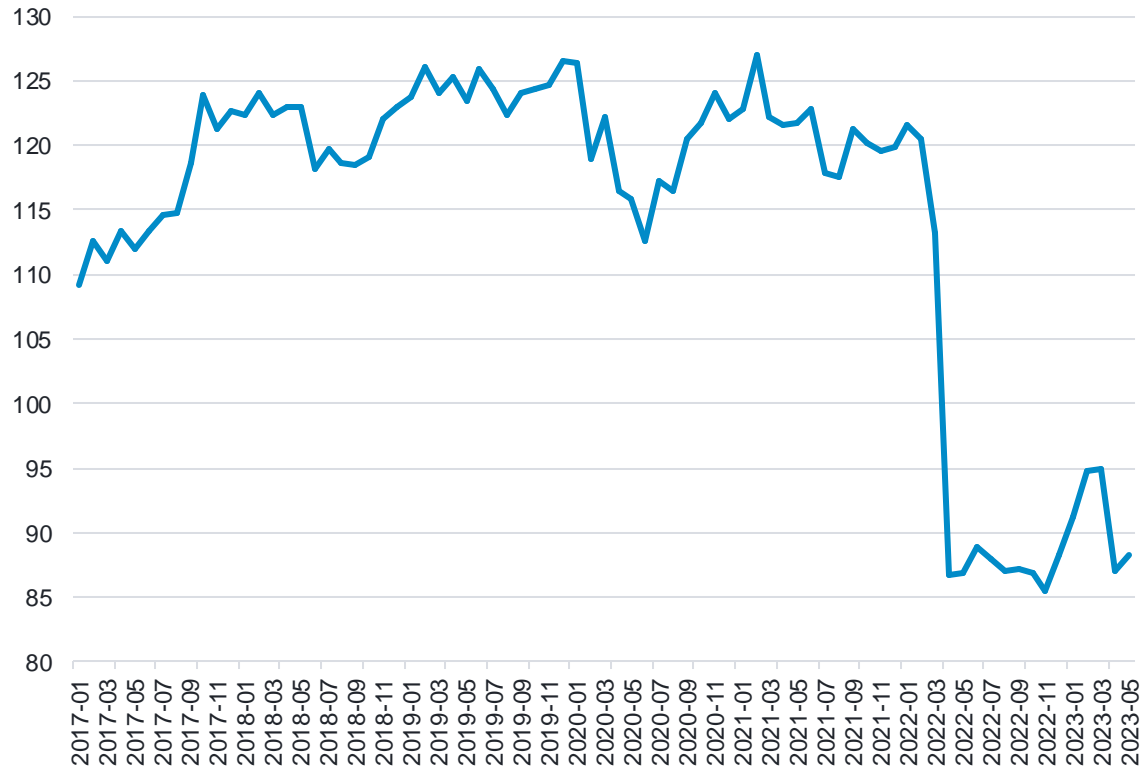
Source: NBS, MS Estimate, September 2023

Ample room for China consumer recovery

Excess household savings to provide additional support once the confidence turns upward

Consumer confidence index

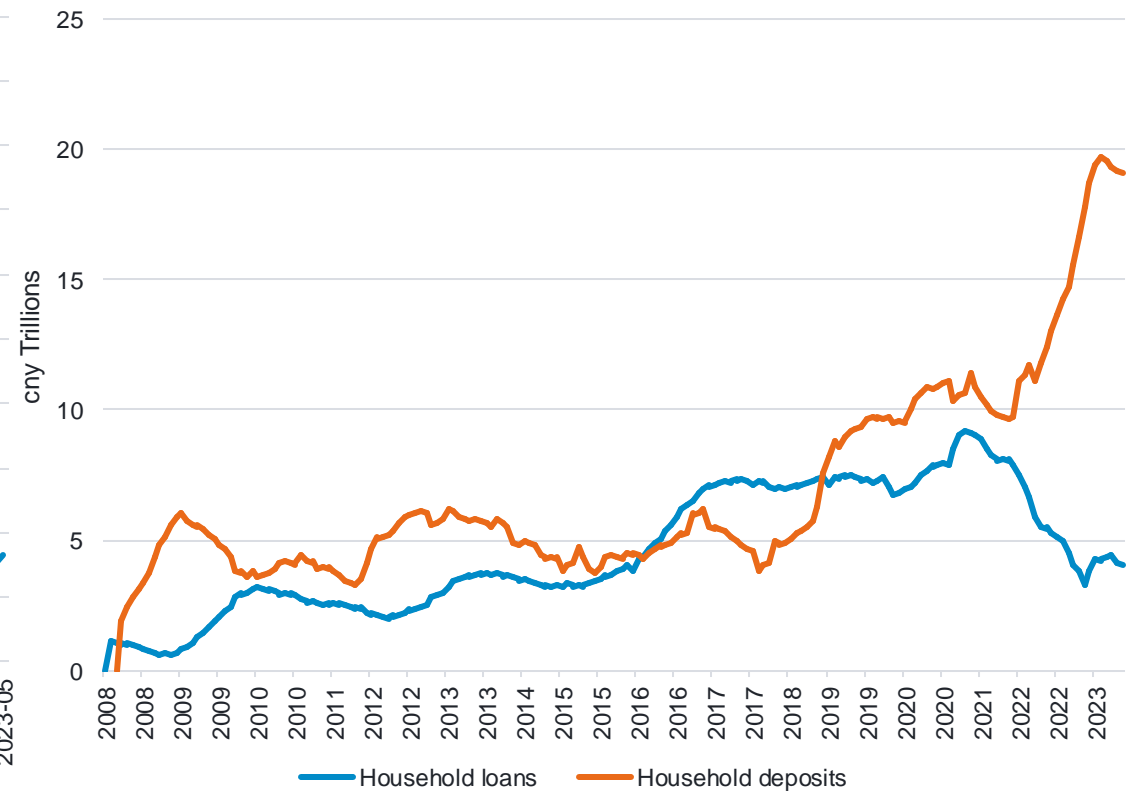
Confidence remains weak



Source: NBS, Fidelity international, 31 May 2023.

China's household deposit vs loans

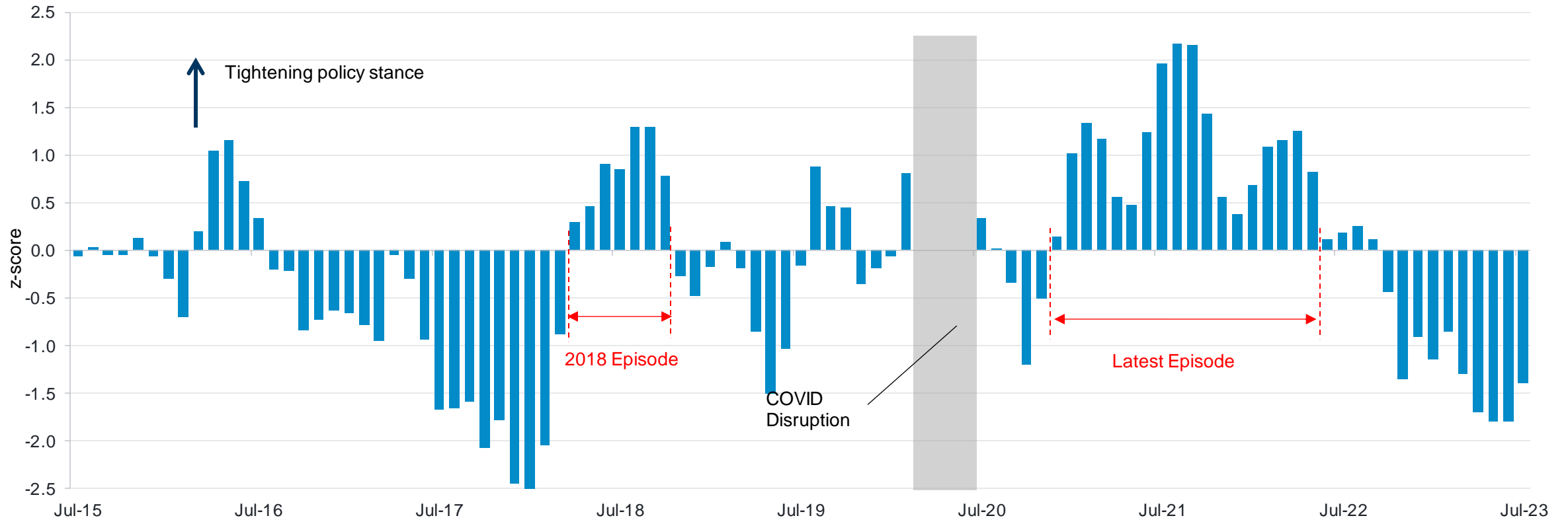
Household deposits and loans have diverged since 2022



Source: Fidelity International, Bloomberg, 31 August 2023.

Policy/regulatory stance turned supportive

Private-owned enterprise regulation proxy since 2015

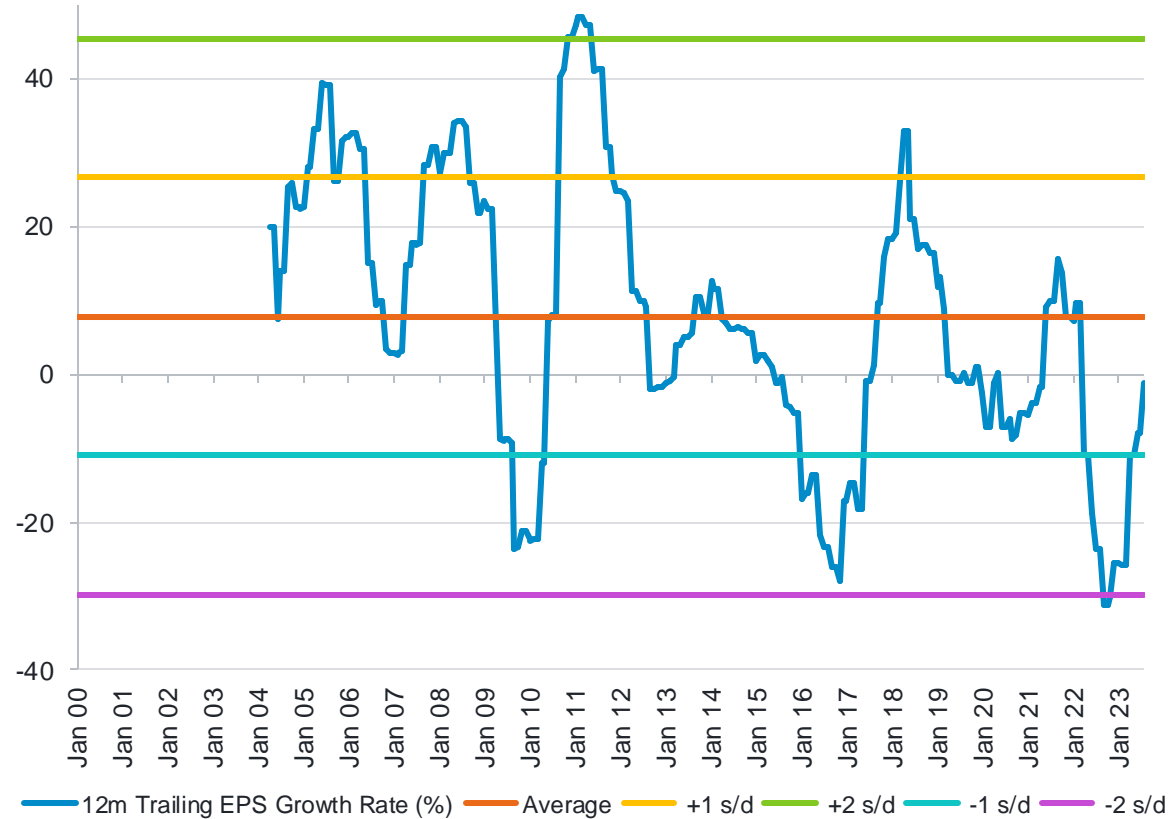


Note: POE Regulation Proxy reflects the text-mining results of new s among POE-heavy sectors. Data points during Mar-Jun 2020 have been removed due to COVID disruptions. August 2023.

Earnings growth bottoming out at a trough level

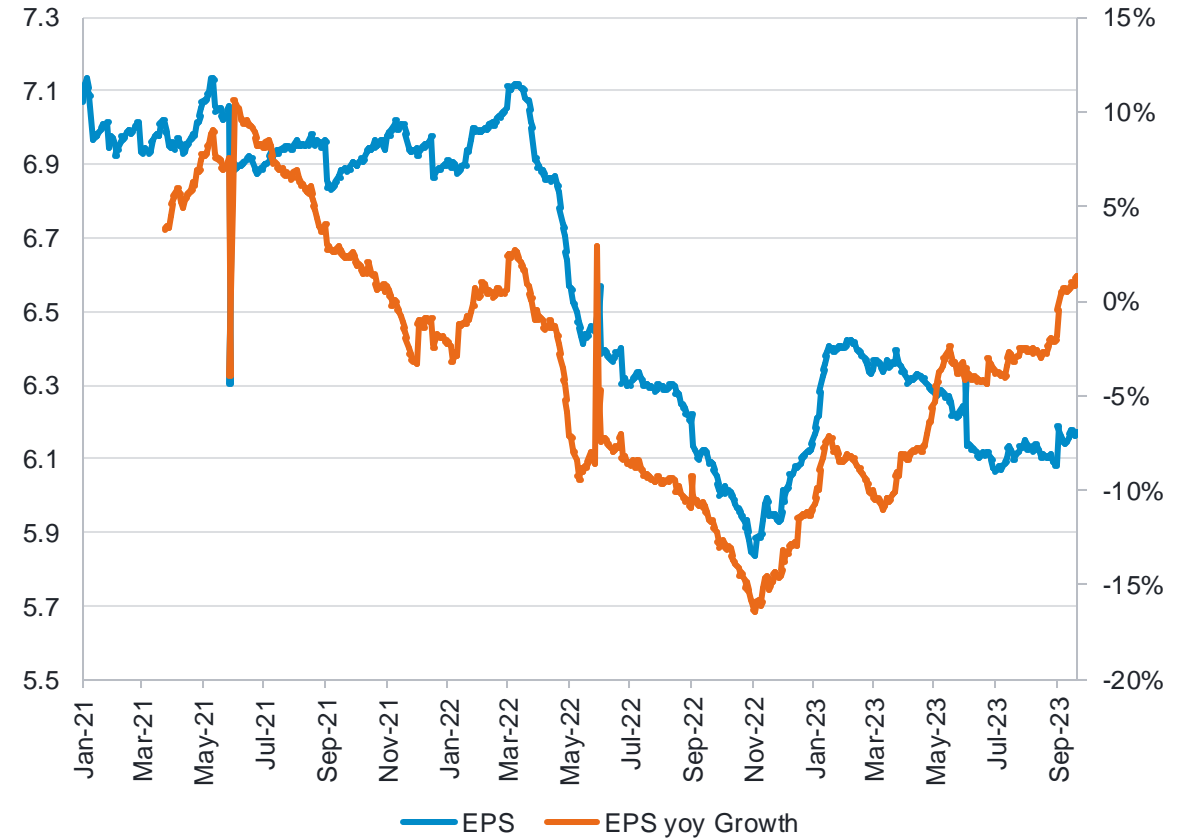
MSCI China EPS growth: last 12 months vs. next 12 months

Last 12m EPS Growth (%)



Source: Fidelity International, IBES, Refinitiv DataStream, 31 August 2023.

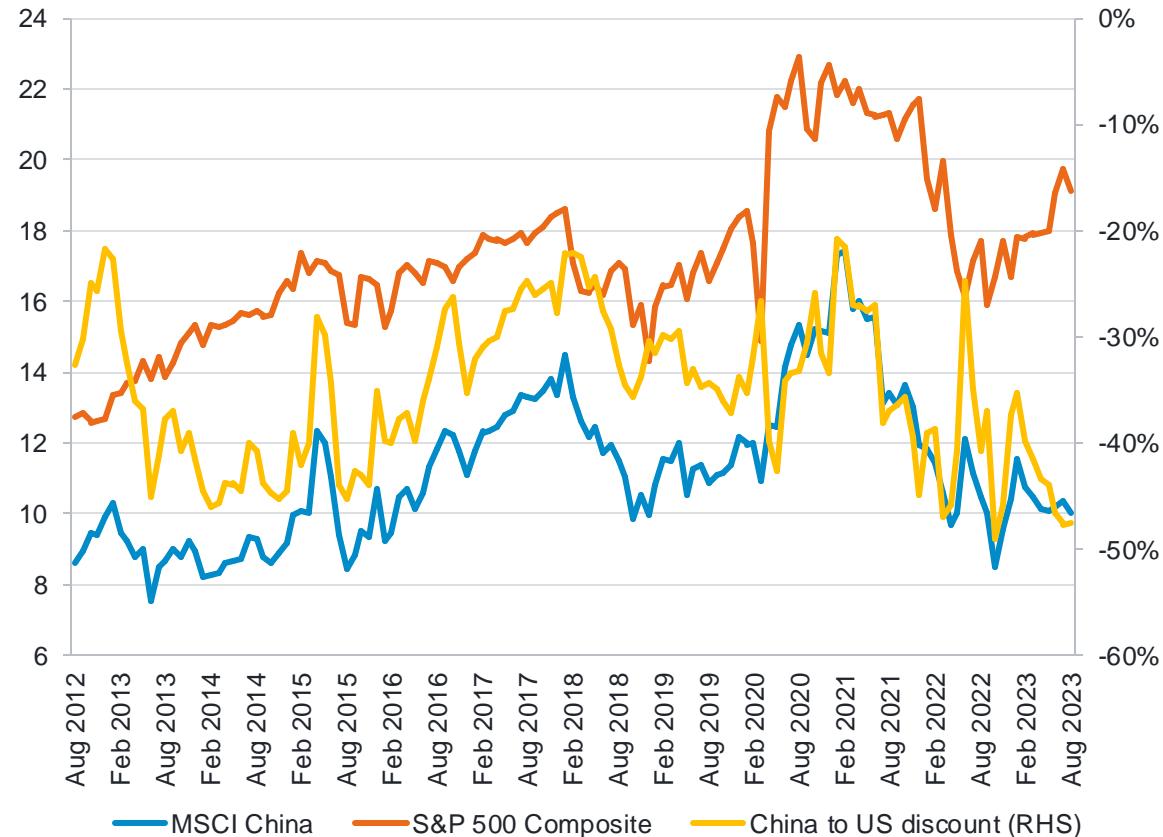
12m fwd EPS Growth (%)



Source: Fidelity International, Bloomberg, 21 September 2023.

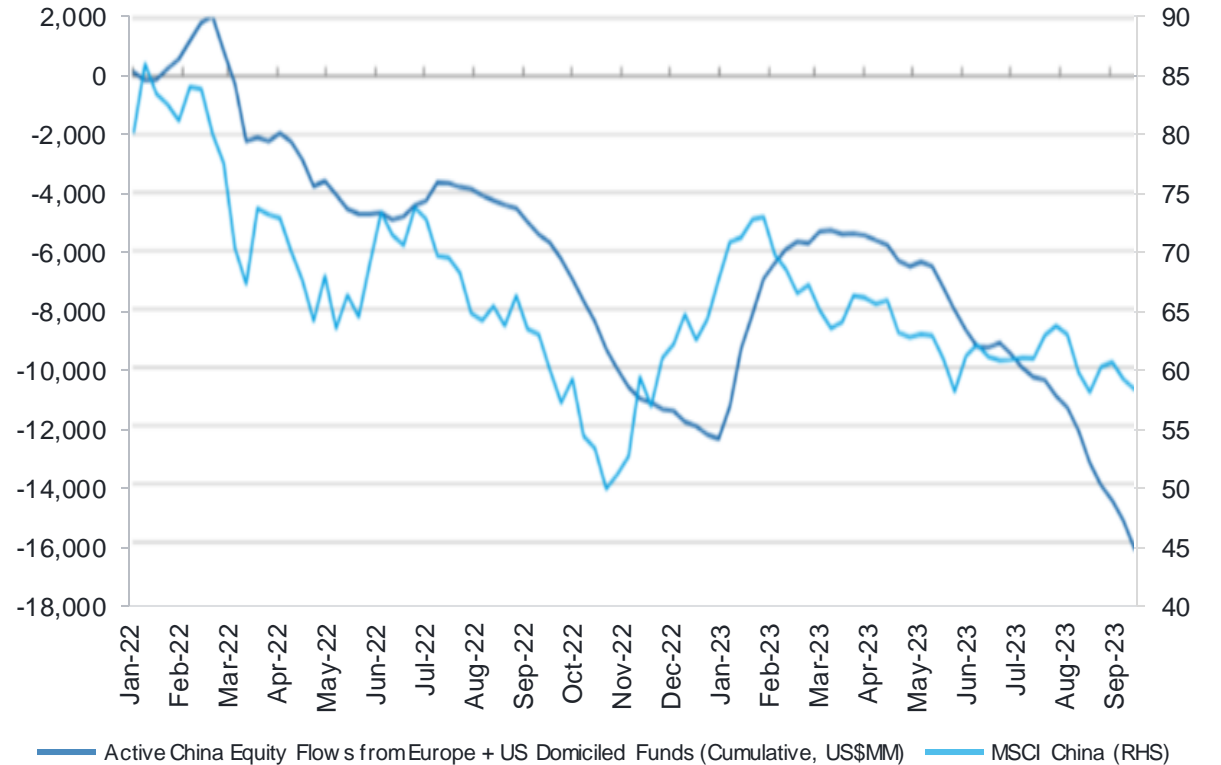
Attractive valuations and weak sentiment offer opportunity

12 Month Forward Price-to-Earnings



Source: Refinitiv DataStream, 31 August 2023. RHS stands for Right hand side.

China cumulative active equity flows by Europe & US domiciled funds – active outflows from Europe and US equity



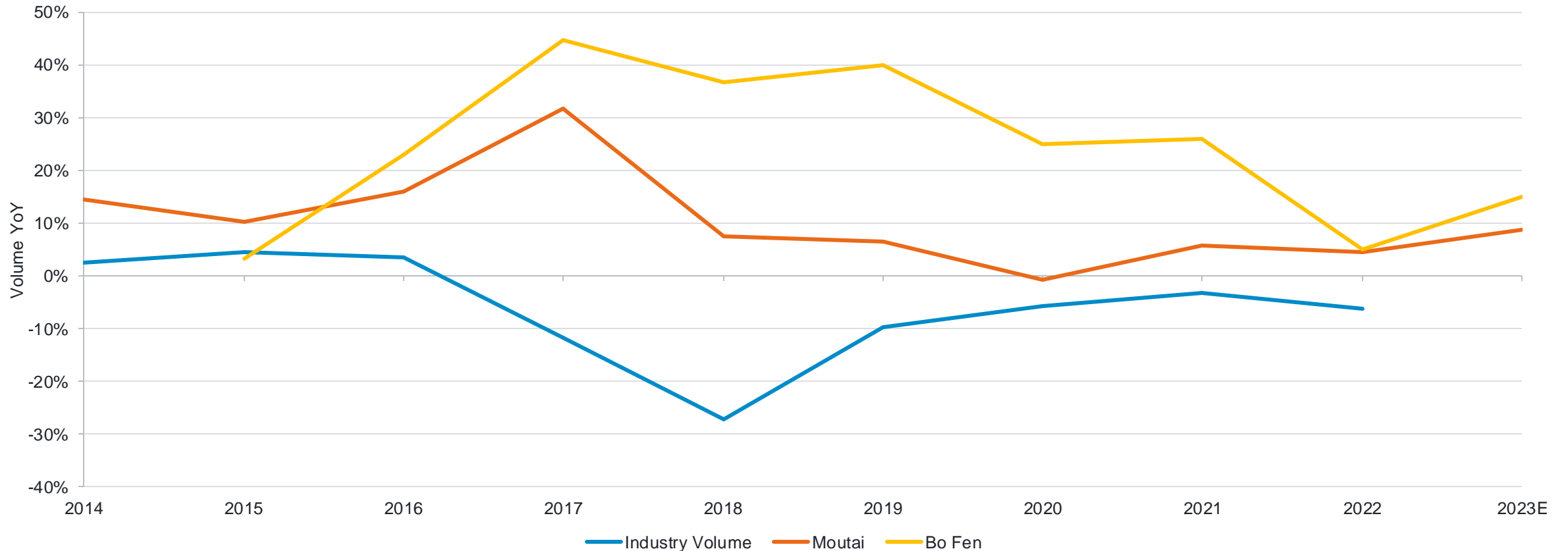
Source: EPFR Global Country Equity Flows Database, Morgan Stanley Research, 20 September 2023.

Investment Themes and Stock Selection

Accelerating bipolarization trend

Bipolarization benefits both premium and value focused segments at the expense of mid-end

- Industry volume has halved since 2016, while Moutai and Bo Fen kept growing and are forecast to stay resilient in 2023

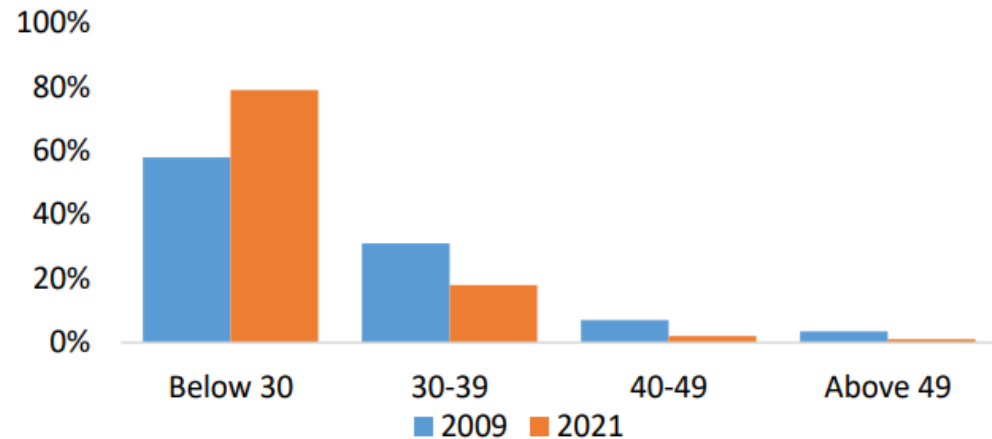


Source: Industry Association, Annual Reports, Fidelity International, 31 August 2023.

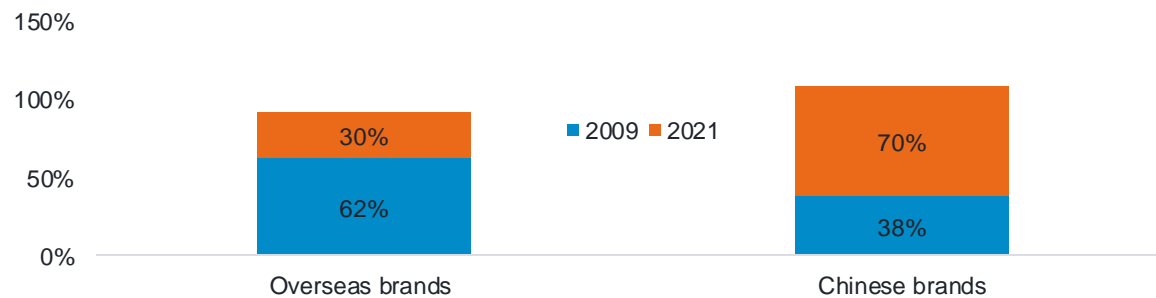
The rise of Chinese local brands in China

Consumer's growing preference for domestic brands

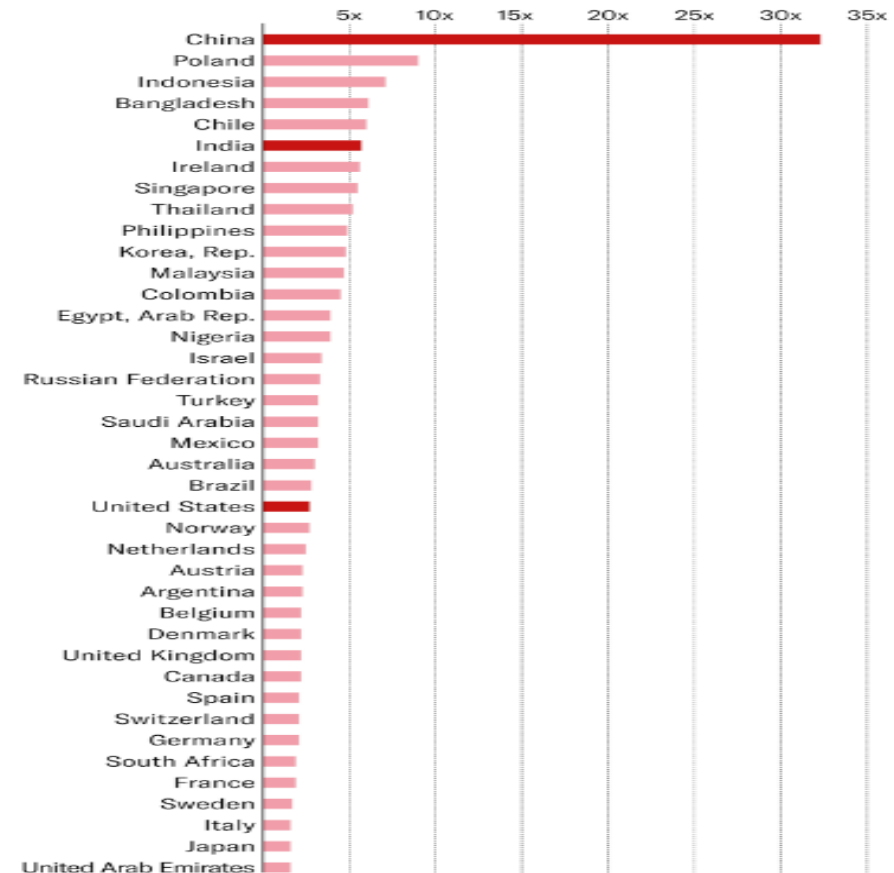
Searches for domestic brands by age on Baidu



% of online searches of brands on Baidu



Per capita GDP growth in the top 40 global economies, 1990 - 2019

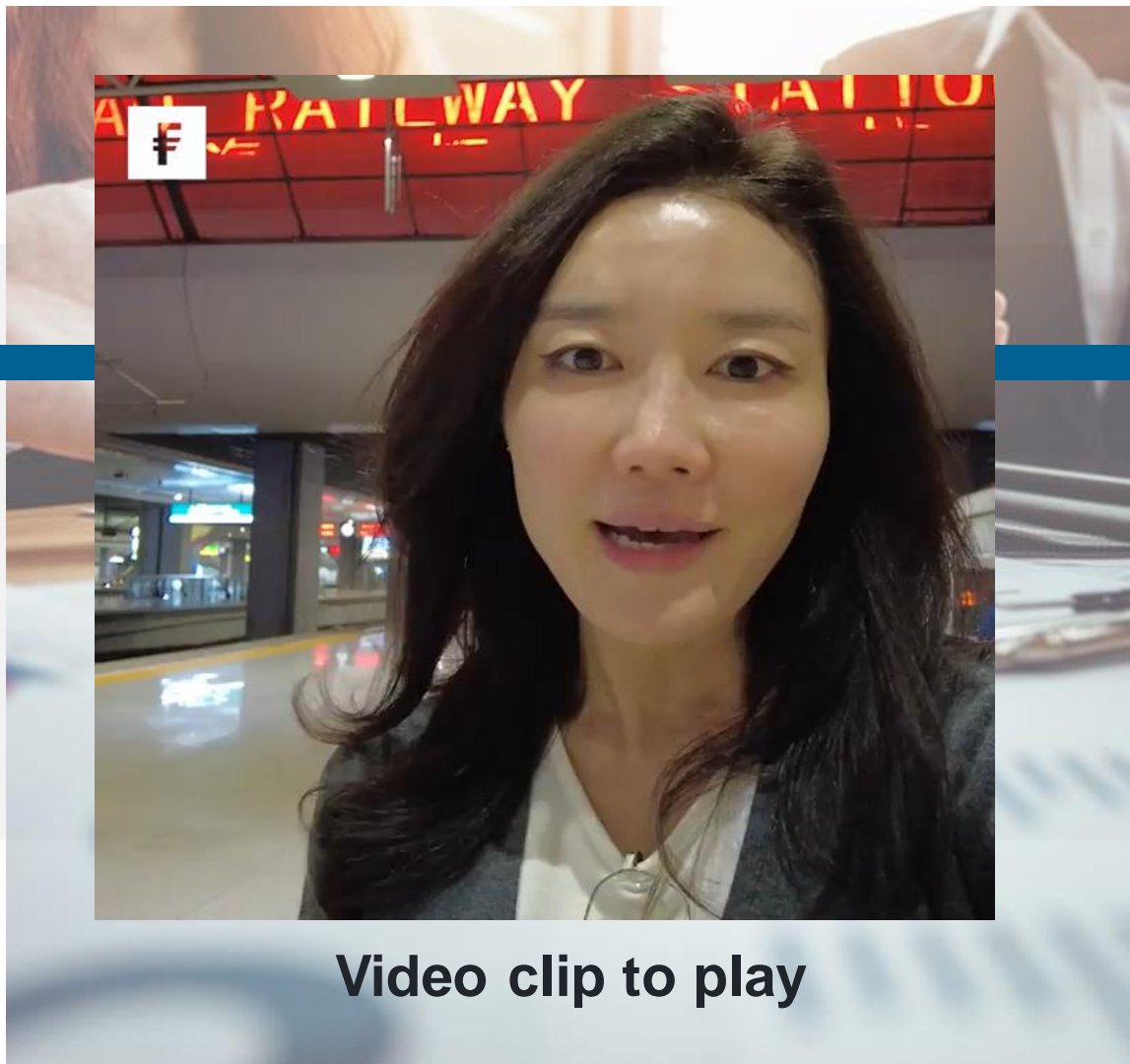


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Source: Baidu Search Index, GS (based on their survey), 31 August 2023

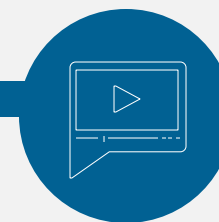
Source: The World Bank, calculations made by Young China Group, 31 May 2021.

The rise of Chinese local brands in China



Video clip to play

Hyomi Jie | Portfolio Manager



Nationalism: Opportunities for Chinese brands

Proya's brand power rising – from 23rd to 3rd in 5 years

Cosmetic brand rank on the T-mall platform

Ranking	Double 11 in 2019	618 in 2020	Double 11 in 2020	618 in 2021	Double 11 in 2021	618 in 2022	Double 11 in 2022	618 in 2023
1	L'OREAL	L'OREAL	L'OREAL	L'OREAL	L'OREAL	L'OREAL	L'OREAL	L'OREAL
2	Estee Lauder	Lancome	Olay	Estee Lauder	Estee Lauder	Olay	Estee Lauder	Lancome
3	Olay	Estee Lauder	Estee Lauder	Lancome	Lancome	Estee Lauder	Lancome	PROYA
4	Lancome	Elizabeth Arden	Lancome	Olay	The history of whoo	Lancome	Olay	Estee Lauder
5	Winona	Olay	The history of whoo	SHISEIDO	Winona	PROYA	PROYA	Olay
6	SK-II	SK-II	SHISEIDO	Winona	SHISEIDO	LA MER	Winona	LA MER
7	CHANDO	HomeFacialPro	SK-II	SK-II	PROYA	Winona	LA MER	HR
8	The history of whoo	SHISEIDO	SULWHASOO	PROYA	HR	SHISEIDO	SK-II	SK-II
9	PECHOIN	CHANDO	Winona	LA MER	SK-II	SKINCEUTICALS	HR	SKINCEUTICALS
10	HomeFacialPro	Winona	SKINCEUTICALS	SKINCEUTICALS	LA MER	Kiehl ' s	SHISEIDO	Winona
11	SHISEIDO	Freeplus	Kiehl ' s	The history of whoo	Kiehl ' s	HR	SKINCEUTICALS	SHISEIDO
12	wis	COGI	LA MER	Freeplus	CHANDO	SK-II	Kiehl ' s	Clarins
13	SKINCEUTICALS	Kiehl ' s	HR	Dr.Yu	Olay	QuadHA	Guerlain	Laroche Posay
14	SULWHASOO	A.H.C	CHANDO	Kiehl ' s	SKINCEUTICALS	Clarins	CPB	Guerlain
15	Elizabeth Arden	okady	Elizabeth Arden	Dr.Jart+	SULWHASOO	Laroche Posay	QuadHA	Kiehl ' s
16	Freeplus	Dr.Yu	Freeplus	HR	Dr.Jart+	Freeplus	Clarins	Cosme Decorte
17	Guerlain	innisfree	Clarins	Cosme Decorte	Clarins	Cosme Decorte	Sisley	Comfy
18	AFU	LA MER	PROYA	SULWHASOO	Guerlain	CHANDO	CHANDO	Sisley
19	HR	Laroche Posay	Cosme Decorte	CHANDO	Freeplus	Guerlain	Cosme Decorte	CHANDO
20	Kiehl ' s	Mask Family	Dr.Jart+	ANESSA	Dr.Yu	Sisley	-	Curel
21	innisfree	Curel	CPB	Laroche Posay	CPB	Mistine	-	-
22	LA MER	PROYA	Guerlain	Curel	Elizabeth Arden	Curel	-	-
23	PROYA	HR	Curel	Clarins	Cosme Decorte	Fresh	-	-



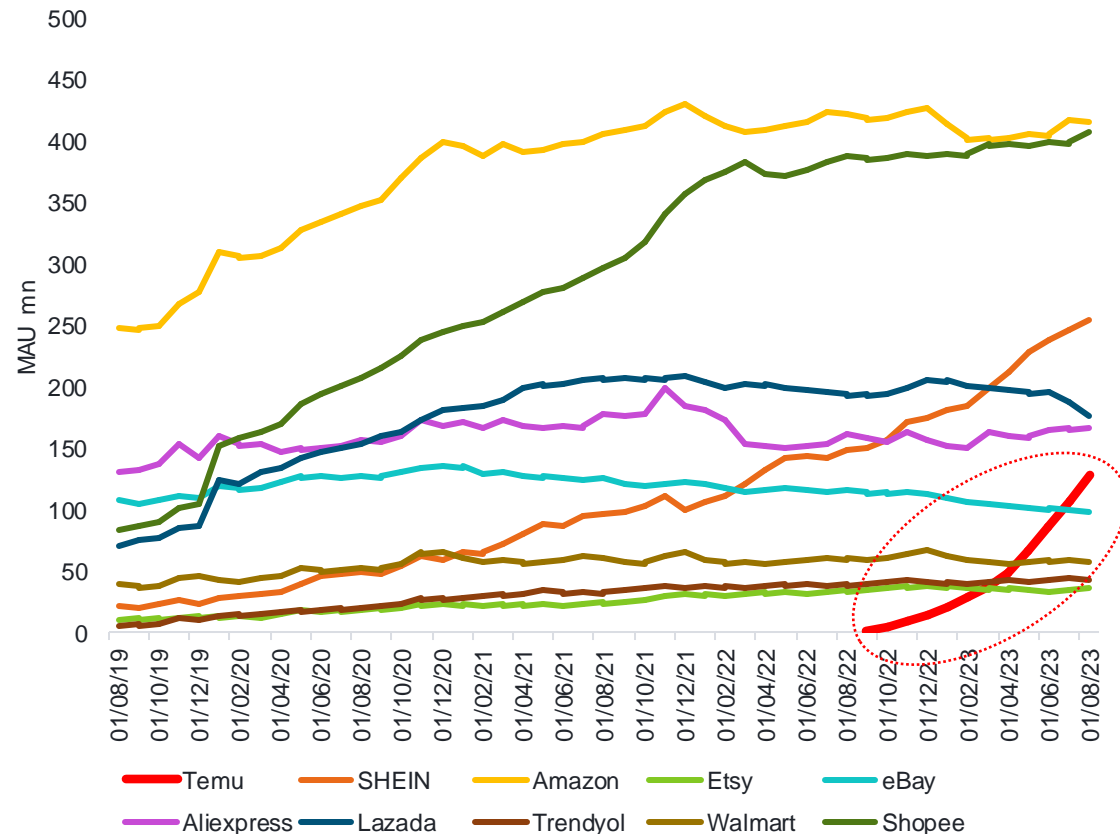
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Source: T-mall report, Fidelity international, 31 August 2023. Third party logos, trademark, copyright and other intellectual property rights are and remain the property of their respective owners.

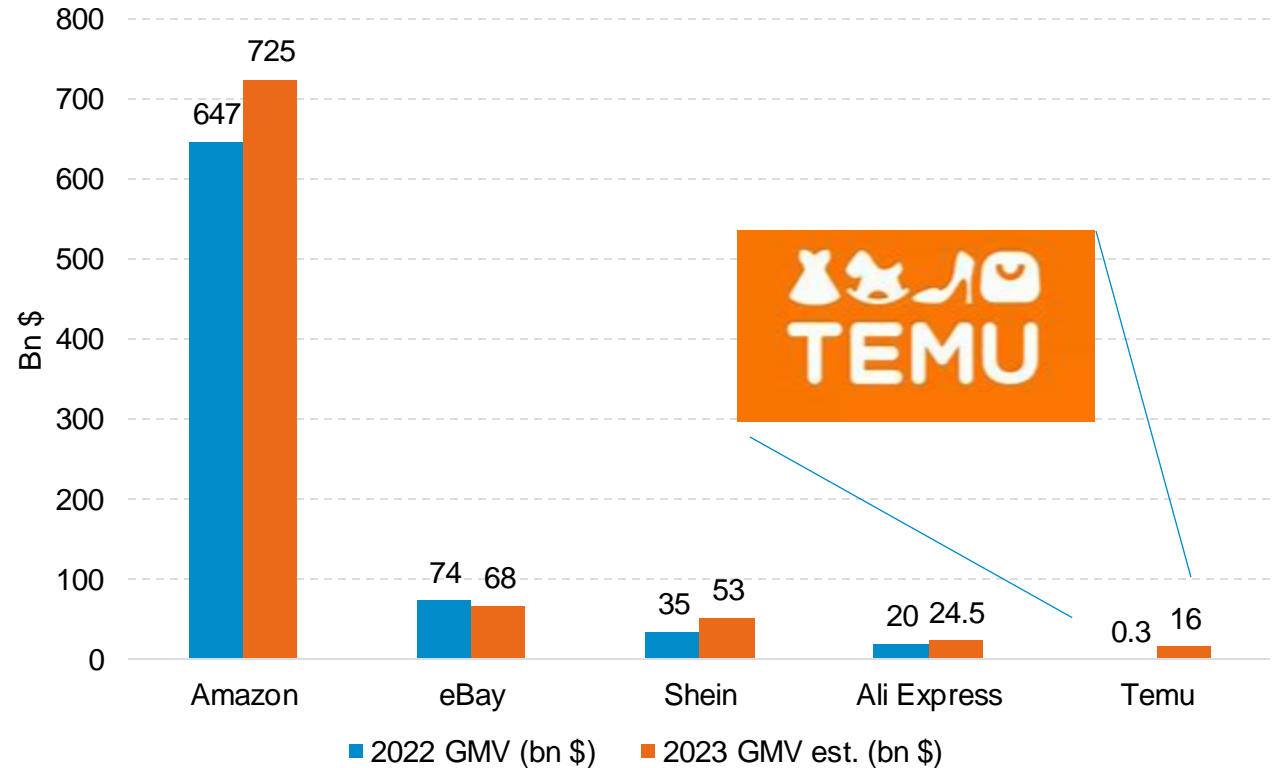
Increasing brand awareness ex-China

Chinese brands success in overseas markets

Major e-commerce companies: Monthly active users (MAU)



Gross merchandise volume (GMV): Key Overseas E-commerce Companies



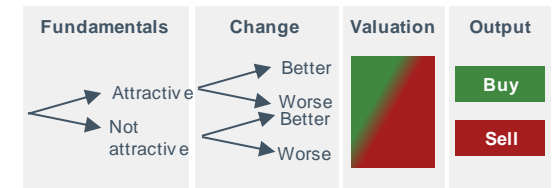
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Yum China

The largest restaurant company in China[^]



Bipolarization



Fundamentals

Search for long-term value creators

- The company is the most localised western restaurant chain in China given its early entry and strong focus to adapt and innovate.
- It generates revenue through its own restaurants and franchise fees – has exclusive rights to operate and sub-license KFC, Pizza Hut and other brands such as Little Sheep and Taco Bell.
- The company has made significant efforts in digitalisation, marketing, and is supported by its strong supply chain.
- They have strong offerings combining good food quality, value for money, store ambience, food safety, convenience at a price point that is very competitive.
- Strong management ability, with track record of good execution. It has over 35 years' experience in China and has launched local brands as well as traditional western fast foods.

Change

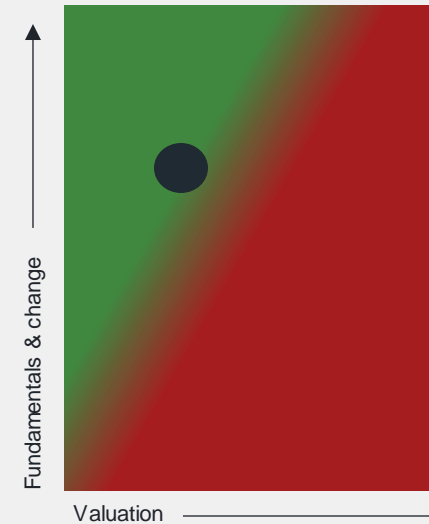
Identify incremental change

- Beneficiary of consumption recovery.
- Further potential penetration opportunity with expansion into tier 2 or 3 cities.
- Focus on improving underperforming stores and accelerating operational improvements.

Valuation

Evaluate intrinsic value

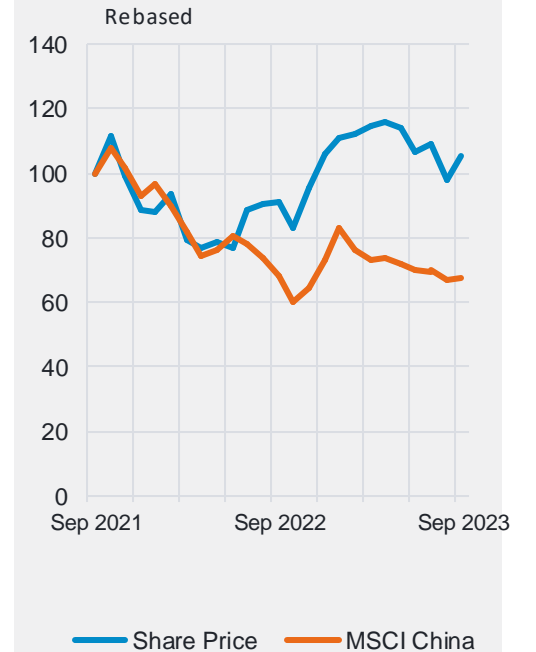
- 11.9x EV/EBITDA 2023E
- Target 28.3x FY23PE
24.4x FY24PE



Output

Investment decision

- 3.3% position*



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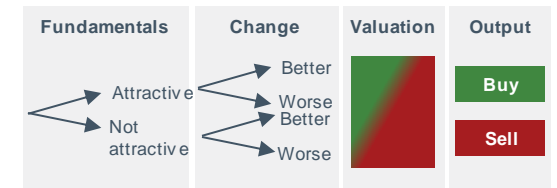
Source: Fidelity International, Refinitiv DataStream, September 2023. *as at 31 August 2023. ^ Based on sales. Third party logos, trademark, copyright and other intellectual property rights are and remain the property of their respective owners.

PDD Holdings Inc

3rd largest E-commerce platform in China[^]



Bipolarization
Rise of local brands



Fundamentals

Search for long-term value creators

- PDD Holdings owns and operates a portfolio of businesses. Through these businesses, it is the group's goal to redefine how online marketplaces are experienced by consumers.
- The direct connection of suppliers and consumers is in line with the Next-Gen Manufacturing approach that PDD Holdings has pioneered. It is a new model of manufacturing that uses insights into consumer preferences through their interactions with digital platforms.
- Through PDD Holdings' sophisticated network of suppliers, vendors, and merchants, Temu is able to bring the best products and merchandise to consumers all over the country.
- They are the number 1 player in community group buying (CGB).

Change

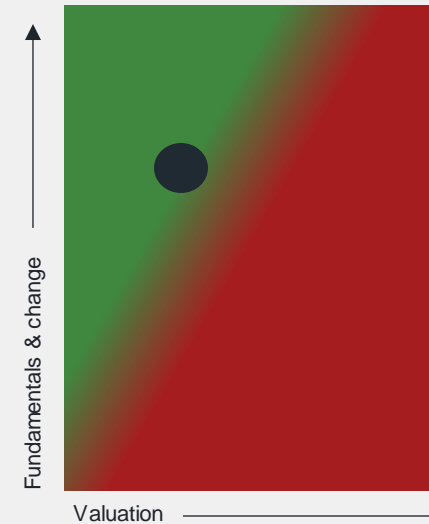
Identify incremental change

- Domestic business: As the low-price platform with exceptional supply chain management, Pinduoduo is a beneficiary of accelerating consumption bipolarization trend.
- Temu's global monthly active users (MAU) has overtaken Walmart and likely to surpass others major players soon.

Valuation

Evaluate intrinsic value

- 19.8x EV/EBITDA 2023E
- Target 20.6x FY23PE
16.4x FY24PE



Output

Investment decision

- 6.4% position*



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Source: Fidelity International, Refinitiv DataStream, September 2023. *as at 31 August 2023. ^ Based on GMV. Third party logos, trademark, copyright and other intellectual property rights are and remain the property of their respective owners.

Summary

- Key drivers of the de-rating - combination of mainly cyclical factors but also structural growth expectation changes. These drivers have been turning incrementally positive.
- China has shown a supportive stance to the economy - leadership's recognition of the underlying issues and willingness to tackle these problems.
- There has been more frequent stimulus since July - some economic activity pick-up, albeit at a gradual pace.
- Property sector easing helpful, the sector is important for Chinese markets overall performance and more notably to the consumer exposed sectors.
- China leadership aim 1) stabilize & increase domestic demand; 2) employment; 3) low-income group & less developed regions. These policies look in-line with President Xi's idealism while also targeting to stabilize consumption and turn around the deflation/recession trend.
- Consumption recovery could gain further momentum if consumer confidence rebounds. Previous macro challenges have dampened investor sentiment and weighed on valuation.
- Despite recent weakness in consumption, we still see ample scope for recovery and more importantly businesses exposed to structural themes such as local brands & bipolarization trends will offer better growth and higher return opportunities.

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