ABCI Policy Insight

2020 Central Economic Work Conference:

Macro, investment, and industry analysis of 2020 Central Economic Work Conference

Andy Yao, Economist

Macro, investment, and industry analysis of 2020 Central Economic Work Conference

Macro comments on 2020 Central Economic Work Conference

The annual Central Economic Work Conference was held in Beijing from Dec 16 to 18, 2020. President Xi Jinping reviewed the country's economic work in 2020, analyzed the current situation, and arranged for the economic tasks for 2021. Premier Li Keqiang made specific arrangements for economic work in 2021 and concluded with a speech.

The Conference affirmed that China's overall economic performance under the impact of the severe pandemic this year has been exceptional - China is the only major economy i to achieve a positive economic growth. Meanwhile, both the pandemic and external environment has cast many uncertainties. The foundation of China's economic recovery is not yet solid. The global economic recovery is still fraught with unknowns. In particular, the fiscal and monetary policies in most developed countries have reached the limit, and the global debt risk cannot be ignored.

The Conference set the tone for next year's macro policy, and pledged to maintain the consistency, stability, and sustainability of its macro policies. China will continue to adopt a proactive fiscal policy and prudent monetary policy while maintaining necessary support for the economic recovery. The operation of macro policies will be more concise and effective, and be implemented at the right time, right intensity, with the right effects, and without major and abrupt changes in direction. The ultra-loose macro policy will return to normal in 2021, but the process should be stable and gradual. This means that the overall policy in 1H21 will still be loose before progressively returning to normal in 2H21.

Proactive fiscal policy must be implemented in higher quality, effectiveness, and sustainability. With the recovering economy, we expect the proactive fiscal policy in 2020 will return to normalcy in 2021. The temporary and phased special measures introduced in 2020 in response to the pandemic is likely to be partially withdrawn in 2021 - deficit rate will be reduced while issuance of special treasury bonds will likely be halted. However, the normal fiscal policy that includes tax and fee reductions, specific-consumption measures, and measures to boost infrastructure investment will be maintained to support economic growth. We expect fiscal deficit ratio to approximate at 3.3% of GDP in 2021, down from 3.6% in 2020.

In terms of monetary policy, the Conference proposed that a prudent monetary policy should be flexible, concise, reasonable and appropriate. China will maintain the growth of money supply and social financing at rates matching with the nominal GDP growth while keeping the macro leverage ratio stable. In view of the weak inflation level and the strong appreciation pressure of RMB, we expect the PBOC to reduce RRR and interest rates in 2021, though the extent will be less than that in 2020. By the end of 2021E, the broad money supply (M2) is expected to grow by 9.5%, basically matching the nominal GDP growth. In addition, with nominal GDP growth expected to rebound substantially next year, we expect the macro leverage to fall slightly.

The Conference also identified eight key tasks for next year. The first two pertains to scientific and technological innovations. Western countries, led by the US, will step up their technology blockade against China; hence, it is crucial for China to develop a core technology breakthrough system in critical industries. China will elevate the total factor productivity through technological innovations and increasing the return on investment. We expect China to allocate more resources on high-tech industries, including the development of chips and semiconductors, software, precision machinery, and new materials. In this way, it can reduce reliance on foreign countries on core technologies. We can foresee that the high-tech sector will gain more traction next year.

The third and fourth key tasks aim at building a new development pattern with the large domestic cycle as the main body and the domestic and global cycles fostering each other. We believe this will be the way to achieve quality development. The Conference proposed that the focus should be on demand side management, especially the domestic demand. While domestic demand includes investment and consumption, we believe the emphasis should be on the latter, considering the lackluster performance in 2020 with nominal retail sales falling by 4.8% in the 11M20. We expect the consumer sector to rebound substantially in 2021.

The fifth key task is to solve the problem of seeds and cultivated land to ensure food security, which is one of the "six guarantees". The sixth key task is to strengthen anti-monopoly efforts and prevent disorderly expansion of capital. The internet technology market is characterized by “the winner-takes-all”, the leaders tend to monopolize digital information, which gives them unparalleled advantages in certain economic domains; as a result, these tech giants can easily monopolize these fields or industries entered. The Conference shows that the anti-monopoly supervision of the internet technology leaders will be greatly strengthened in 2021. The seventh key task is to resolve the housing issues in big cities and the anti-speculative stance was reiterated.

The eighth key task concerns carbon neutrality. China's carbon dioxide emissions will peak before 2030 to achieve carbon neutrality before 2060. We believe the development of a high-quality economy must be environmentally friendly. In the future, green economy, including new energy industry and environmental protection industry, will receive considerable support. The development of green debt and equity financing will also accelerate.

Exhibit 1: Eight key tasks of 2020 Central Economic Work Conference

1. Strengthen the national strategic scientific and technological edges
2. Enhance the independent and controllable ability of industrial chain and supply chain
3. Adhere to the strategic basis of expanding domestic demand
4. Comprehensively promote reform and opening up
5. Solve the problem of seeds and cultivated land
6. Strengthen anti-monopoly efforts and prevent the disorderly expansion of capital
7. Solve the prominent housing problems in big cities
8. Achieve carbon emission peak and carbon neutrality

Sources: 2020 Central Economic Work Conference, ABCI Securities

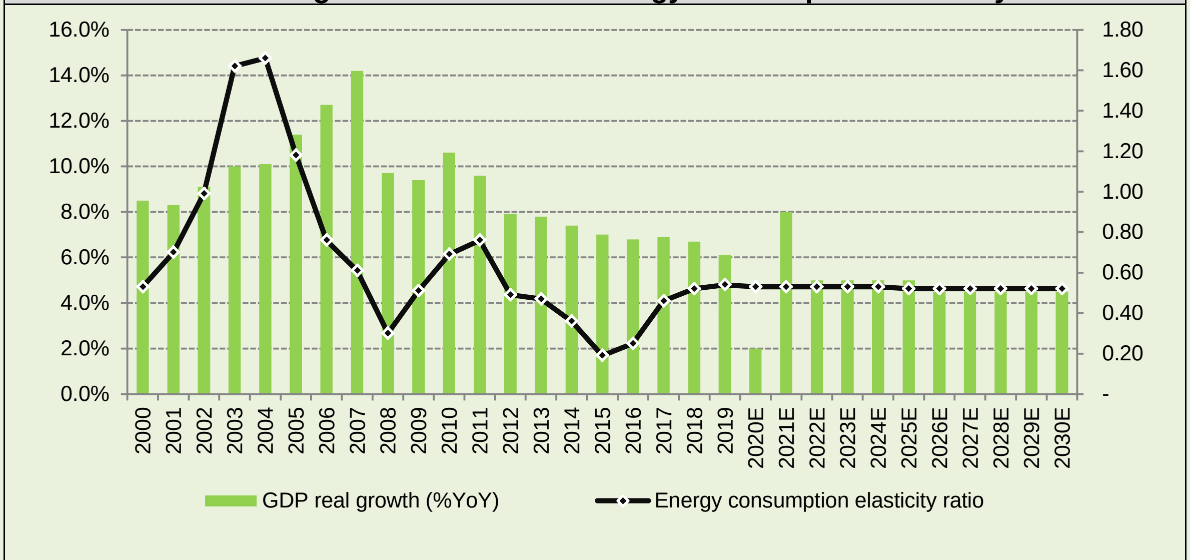
Philip Chan, Head of Research

Special Topic: Carbon Neutrality as investment theme

Carbon neutrality in 2060 is another long-term objective of China, aside from its two 100th Year plans. Carbon emission peaking in 2030 is an intermediary target. We can expect the government to enforce new measures in coming years. As such, we will investigate the long-term investment themes in the capital market.

In the next 10-40 40 years, the economic structure will shift toward the high value-added but less energy-intensive industries. We believe the structural change will help attain the carbon emission goals in 2030 and 2060. Regardless of the energy type, energy input has been an important factor in driving economic growth; therefore, to reduce reliance on energy input can help sustain economic growth. From an economic or investment perspective, energy consumption elasticity ratio (i.e. the ratio between energy consumption growth and real GDP growth) is a parameter used to measure energy efficiency in the economy. During 2004-15, the elasticity ratio was falling, signaling an improvement in energy efficiency. However, the ratio rebounded from 0.2 in 2015 to 0.54 in 2019. The energy-intensive industries were recovering in 2016-19 (the period within the 13th five-year plan). An elasticity ratio of ~0.5 means energy consumption growth is about half of the real economic growth.

Exhibit 1：Real GDP growth（LHS）and energy consumption elasticity ratio

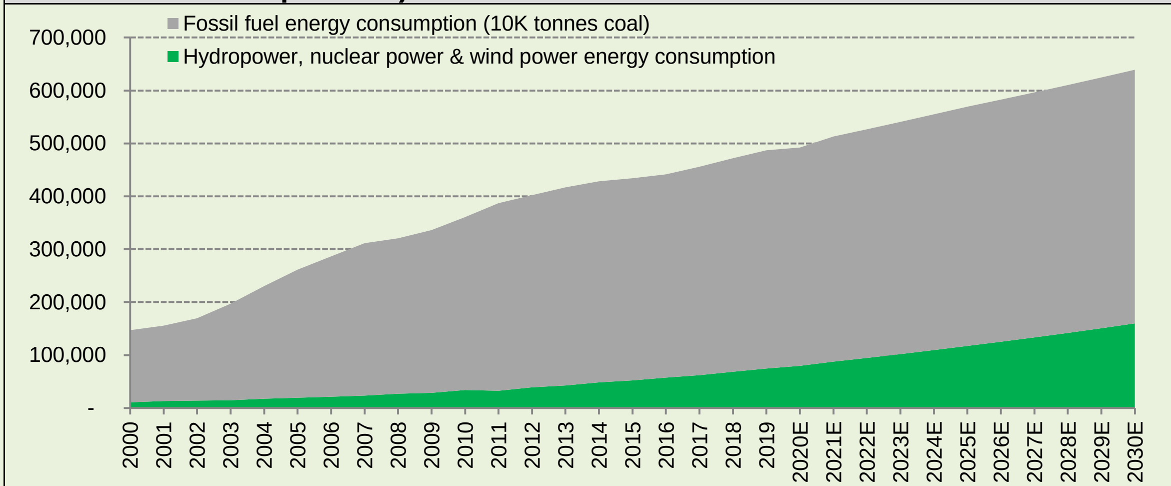


Energy consumption elasticity= Energy consumption growth / Real GDP growth

Source(s): NBS, ABCI Securities estimates

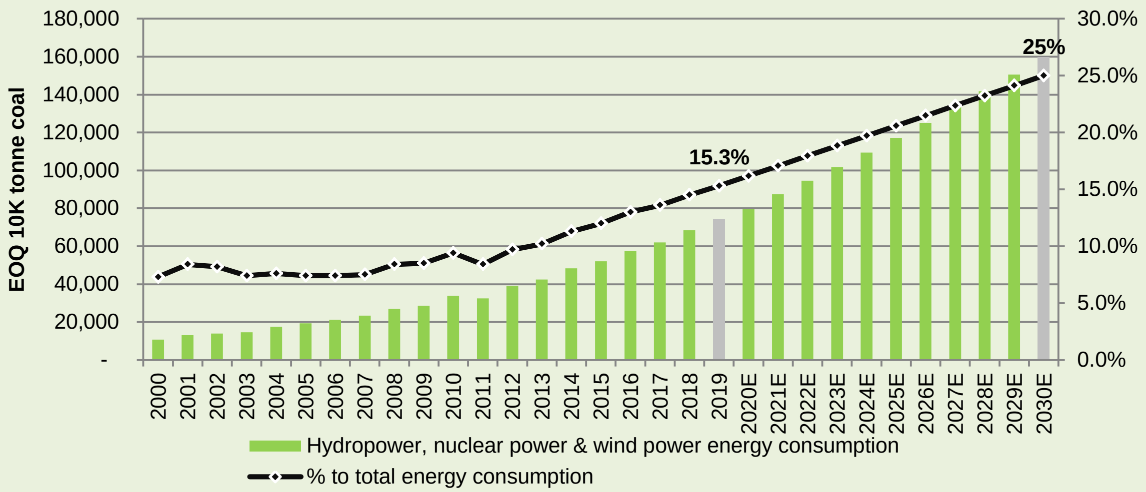
Non-fossil fuel energy demand will enter the high-growth phase. China aims to raise the proportion of non-fossil fuel energy in total energy consumption from 15.3% in 2019 to over 25% in 2030. Assuming an annual GDP growth at 4.5-5.0% in 2022E-30E and an energy consumption elasticity ratio of 0.52-0.53 over the same period, we predict energy consumption will grow at 2.6% CAGR in 2020E-30E, of which fossil-fuel energy consumption and non-fossil fuel energy consumption will increase at 1.5% and 7.2% CAGRs in 2020E-30E. Demand for non-fossil fuel energy will be in the high-growth phase, whereas the fossil-fuel energy (e.g. coal, petro, etc.) consumption will show a low or flat growth.

Exhibit 1: Fossil fuel energy and non-fossil fuel energy consumption (equivalent to standard coal equivalent)



Note: We assume a real GDP growth at 4.5-5.0% in 2022E-30E and energy consumption elasticity at 0.52-0.53.
Source(s): NBS, ABCI Securities estimates

Exhibit 2: Hydro, nuclear and wind power energy consumption（LHS）, Non-fossil fuel energy consumption-to-total energy consumption ratio（RHS）



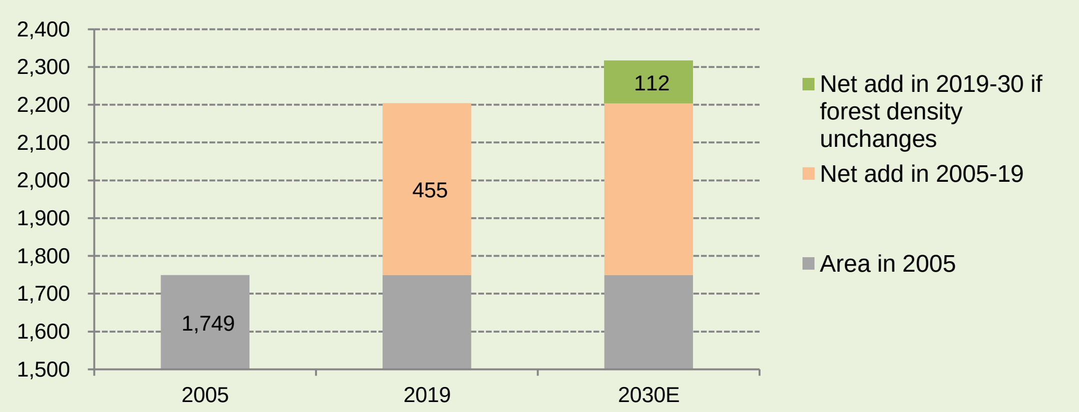
Note: We assume a real GDP growth at 4.5-5.0% in 2022E-30E and an energy consumption elasticity at 0.52-0.53.
Source(s): NBS, ABCI Securities estimates

Investments in clean energy projects will increase significantly in the next decade. China is targeting to raise the total installed capacity of wind and solar power to above 1.2bn KW by 2030; their installed capacities were 0.21bn KW and 0.20bn KW at end-2019 and subsequently rose to 0.23bn KW and 0.22bn KW in 10M20. To achieve the 2030 target, the combined installed capacity of wind and solar power will grow at 10.3% CAGR in 2020-30 (or a net addition of 0.75 bn KW in 2020-30). The additional installed capacity of wind and solar power was 0.053bn KW in 2019 and 0.04bn KW in 10M20. For the next decade, a total of 0.075bn KW of combined installed capacity will be added per annum on average. The demand for new installed capacity will drive growth in the supply chains of wind and solar power equipment. Hence, the government's goal to increase installed capacity of wind and solar power will catalyze development in the upstream industries.

The government's supportive policy on NEV industry will benefit the supply chain. Developments of electrified railway, underground railway, and NEV will help control carbon emission in cities while passing the emission burden to upstream industry in power generation. Reducing reliance on fossil fuel in power generation is necessary for lowering carbon emission in the transportation industry. The government sets the proportion of NEV sales to total auto sales at 20% by 2025. By 2030, NEV sales will become the majority in auto sales. In July 2020, China liberalized the NEV industry by allowing foreign automakers to hold a controlling stake in their NEV production plants in the country. We forecast output growth of NEV will increase from the 21% CAGR in 2016-20E to 40% CAGR in 2020E-30E. The output growth will reach 12% CAGR in 2025E-30E, assuming that NEV sales will account for 55% of total auto sales in 2030E.

Carbon neutrality means increased competition for land resources. It is difficult to increase the total amount of land resources unless the sea is reclaimed. The area of farmland cannot be reduced to ensure food supply. Forest and non-agricultural land will inevitably become the resource of contention. The concept of carbon neutrality is that carbon emission is equal to the absorption of carbon by forests. In our forecast, fossil fuel energy consumption will grow by ~1.2% in 2020E-30E. As the main source of carbon absorption, forest grows slowly and its total area is restricted by human land use. Therefore, if more land resources are left to forests to absorb carbon, less non-agricultural land resources will be left for human use. From an investment perspective, the improvement of air quality and the increase of green land coverage can improve the quality of life, while the reduction of available land resources will eventually drive up the economic value of land. Based on the national goal of increasing forest stock by 6bn m^3 in 2005-30, forest volume will expand from 12.46bn m^3 in 2005 to 17.56 bn m^3 in 2019 and 18.46bn m^3 in 2030. If the forest density remains unchanged, we estimate that a net increase of 112000 sqkm (almost equivalent to 100 times the land area of Hong Kong) in forest area will be needed in 2019-30. Of course, the increase in forest area will mean that the land available for non-agricultural uses will be reduced. Scientists need to develop ways to accelerate forest growth and density in order to reduce the pressure on forest land-use demand in the future.

Exhibit 3: Forest area ('000 sq.km.)



Source(s): NBS, ABCI Securities estimates

Policy Insight

China Banks Sector

Johannes Au, Analyst

Related Policy:

- Maintain a flexible and appropriate monetary policy; ensure growth in money supply and total social financing matches with that of the nominal GDP; maintain a stable macro leverage ratio; achieve economic recovery while sufficiently preventing risk; broaden capital channels for banks.

- To strengthen regulations and improve supervision capabilities; curbing monopolies and unfair competition; financial innovation must be carried out under close supervision.

- Promote reform and open up to competition. Build a high-level socialist market economic system, achieve a high level of market openness, and promote reforms that facilitate the opening up and vice versa.

- Increase financial support for technological innovation, MSEs, and green development sectors; deepen liberalization of interest rates and exchange rates.

- Maintain economic growth at a reasonable range; continue to increase market vitality; improve policies for tax reduction and fee reduction; strengthen inclusive financial services; exert greater efforts in reforms and innovations, especially those that will benefit medium, small, and micro enterprises and individual business owners.

Industry impacts:

- The Central Economic Work Conference affects the banking industry mainly in two ways. First, it seeks to balance economic recovery with risk prevention through a stable and flexible monetary policy. Avoiding major financial risks remains to be a high policy priority, and emphasis is placed on strengthening regulations and enhancing supervisory capabilities; specifically, financial innovations can only be developed under close supervision. We can expect the supervision over FinTech and new financial products to tighten in the future. Policy risk has always been the biggest risk factor in the banking sector, although strict supervision and disciplined operation will be beneficial for the industry in the long run. Nonetheless, the introduction of new policies will increase short-term stock price volatility.

- Second, it seeks to promote reform, develop a high-level socialist market economic system, and advance to opening up the market to a higher level. Measures to achieve these goals include the further liberalization of interest rate and the opening up the financial sectors to foreign players. Driven by the LPR reform in 2019, average lending interest rate fell gradually from 5.62% in Sep 2019 to 5.12% in Sep 2020, down 50bps YoY, according to the PBOC. Although average lending rate started to stabilize in 3Q20, we expect downward pressure to persist in 2021 in a bid to reduce social financing costs. The pace of decline will be slower in 2021.

- Increased competition will be a natural result of opening up the financial sector to foreign players; however, foreign banks currently account for less than 1ppt of market share in China. Therefore, we believe the impact on Chinese banks will be very limited.

- With the COVID-19 outbreak in 2020, banks were directed to increase support for SMEs, MSEs, individual business owners, and inclusive finance. All these have resulted in a moderate structural adjustment in the credit portfolio among banks. The Conference proposes to expand the coverage of financial support to technological innovations and green development sector. Hence, we can expect further adjustment in the credit portfolio.

- Asset quality risk has always been a concern. Assuming no major resurgence in the pandemic and economic growth in China to stay a reasonable range, we believe asset quality risks will gradually decline. The system NPL ratio has been stabilized at 1.91%-1.96% in 2020 while risk buffer has increased - system provisioning ratio rose from 3.46% in Dec 2019 to 3.53% in Sep 2020. To be conservative, we estimate the system NPL ratio would edge up a few bps QoQ for the next few quarters.

- In view of the expanding balance sheet, the Conference once again highlights the need to enhance banks' capital position through multiple channels. This indicates the importance of replenishing capital for sustainable loan growth. In contrast to the high capital level in large commercial banks over the past years, the capital needs of district banks are relatively high.

- Generally speaking, no major changes in policy direction are purported in the Conference. As stated in our 2021 Economic Outlook and Investment Strategy Report, we are optimistic on the China banks sector.

China Securities Sector

Steve Chow, Analyst

Related Policy:

- Improve the governance of financial institutions; promote the healthy development of the capital market; improve the quality of listed companies; combat various debt evasion behaviors.
- Improve legislations for the bond market and increase financial support for technological innovations, MSEs, and environment protection.

Industry impacts:

- The securities industry is not discussed in detail during the Conference, but the long-term policy goal, which is to increase the proportion of direct financing and promote the healthy development of the multi-level capital market, remains largely unchanged. This is beneficial to investment banking businesses such as equity financing and bond financing.
- The Conference proposes to improve the legal system in the bond market and increase financial support for technological innovation, MSEs, and environmental protection. Overall, this is consistent with the policy goal of supporting enterprises to increase bond financing, as suggested in the previous government work report. The Conference provides further details on the targeted industries to facilitate policy implementation.
- The government work report proposes to increase special bonds for local governments; however, the suggestion was not mentioned in the Conference, which could imply policy adjustments.
- Overall, the meeting is beneficial to investment banking business in the securities industry.

Policy
Insight

China Property Sector

Kenneth Tung, Analyst

Related Policy:

- Reiterate its anti-speculative stance in home purchase; implement region-specific housing measures; adopt multiple strategies to promote the stable and healthy development of the real estate market in China.

- Expedite the construction of affordable rental housing; improve long-term rental housing policies; rent-and-purchase housing will gradually be entitled to enjoy equal rights in public services; standardize the development of the long-term rental housing market. Land supply should be tilted towards the construction of rental housing, and plans for rental housing should be listed out. The land plan should explore the use of collective construction land and the idle land owned by enterprises and institutions for rental housing. Both state-owned and private enterprises must play a functional role. It is necessary to reduce the tax burden on rental housing, foster orderliness in the rental market, regulate market behavior, and adjust rent levels.

- Expedite urban renewal development and promote the renovation of old cities and towns

Industry impacts:

- **Anti-speculation stance unchanged.** The Conference reiterates it anti-speculation stance and specific measures should be adopted based on the local condition. It recognizes that housing issue is more prominent in big cities, which can be taken as a hint that relevant policies in tier-1/2 cities may step up further. In contrast, the tightening of monetary compensation of shantytown renovation in tier 3/4 cities has driven down housing demand, thus allowing room for policy relaxation. Property market in the high-tier cites show limited signs of cooling - in Nov 2020, second-hand residential housing prices intier-1 cities rose by ~8.3% YoY; the growth rate was significantly higher than the 2.1%/ 1.5% YoY increase in tier 2/3 cities. Nonetheless, thanks to the price-limiting policies, new home prices in tier-1 cities rose by 3.9%, close to the 4.2% /3.8%YoY increase in tier-2/3 cities.

- **Regulating long-term rental housing market.** Capital chain rupture of apartment rental companies shows the need for further regulation in the long-term rental industry. The Conference proposes to reduce the operating pressure of long-term rental apartment companies through the supply side and the cost side, especially by reducing the high land prices. Increasing the supply of land for rental housing may lower the land prices and reduce the initial investment of long-term rental apartment companies. Reducing the rental housing taxes could also ease the pressure on operating expenses.

- **Renovation of old urban communities may speed up the renewal of old towns, presenting new business opportunities for property management companies (PMCs).** The Conference stresses on the execution of urban renewal projects; hence the approval process of developers' urban redevelopment projects may be accelerated. In particular, high-tech industries are emerging rapidly while old industries are shrinking fast or exiting the market. Expediting the conversion of old factory land to residential buildings can better utilize valuable land resources. On the other hand, promoting the transformation of old towns and cities present enormous opportunities to PMCs. In July, the State Council issued the "the Opinions on Comprehensively Promoting the Reconstruction of Old Communities in Urban Areas" that proposes 39,000 old communities in urban areas, which involves 7mn residents, to be renovated in 2020. By 2022, the policy framework for the renovation of old urban communities will be established. The government will provide financial subsidies to encourage residents to invest in upgrading the complementary facilities such as the installation of energy-saving systems, elevators in old buildings, and smart systems.

Policy Insight

China Alternative Energy

Kelvin Ng, Analyst

Related Policy:

- China's carbon dioxide emissions will strive to peak before 2030 to achieve carbon neutrality by 2060.
- Formulate an action plan for carbon emission peak by 2030; support certain regions with the right conditions to reach the emission peak first.
- Accelerate the optimization of the industrial structure and energy structure; expedite the consumption peak for coal and development for new energy sources; establish energy use quota and carbon emission trading market; improve the dual control on energy consumption and intensity.

Industry impacts:

- **We believe that China's directions to reduce air pollution and carbon emissions remain unchanged; hence, the prospects of the alternative energy industry will be positive**. Since the cost of power generation differs for each alternative energy source, the industry prospects will vary. When the cost of alternative energy generation is high, local governments may step in to subsidize in the form of tariffs, which in turn will add to their financial burden. The National Energy Administration and the National Development and Reform Commission announced the "subsidy-free tariff" policy in 2019, eliminating most of the tariff subsidies for alternative energy sources and marking the path of high-quality development. We believe that if the country strives to achieve carbon neutrality by 2060, the healthy development of the national carbon emission trading market will be crucial.
- **National carbon emission trading market:** It requires the coal-fired power generation units to purchase carbon emission quotas from the alternative energy industry. Carbon emission quotas are free carbon emission quotas that carbon-emitting companies received each year. Once their actual carbon emissions exceed the quotas, the companies would need purchase additional ones in the carbon emission trading market; conversely, the quota surplus can be sold in the market. Companies must continue to reduce emissions to cope with the reducing free quotas.

Policy Insight

- **Dual control system of energy consumption:** It refers to the dual control of total energy consumption and intensity. The goal is that by 2020, the national energy consumption per RMB 10,000 of GDP will be reduced by 15% compared with 2015, and the total energy consumption will be capped at 5bn tonnes of standard coal equivalent. Local governments are encouraged to reduce coal-fired power consumption and increase energy utilization rate.

- Rapid expansion of the installed capacity for alternative energy sources will promote carbon neutrality.

  - **Hydropower：** The hydropower industry has low power generation costs and does not require tariff subsidies; therefore, the impact of the "subsidy-free tariff" policy is limited. The positive impact of the national carbon emission trading market is not significant for this sub-segment. The development of hydropower industry is constrained by geography and climate. In China, hydropower stations have been established in almost all major rivers; therefore, the growth rate of installed capacity would only increase at a low to medium single-digit level in the long run
  - **Nuclear power：** Nuclear power is the best alternative to coal-fired power because 1) its utilization hour is high, 2) the cost of power generation is similar to that of the coal-fired; 3) no greenhouse gas emission; 4) its capacity is less constrained by geographical factors. The biggest risks of nuclear power are on safety and the massive initial investment needed. The impact of the "subsidy-free tariff" policy has limited impact on the development of nuclear power, and direct benefits of the national carbon emissions trading market will not be obvious for the sub-segment because nuclear power operators are state-owned.
  - **Wind power：** The cost of wind power generation is ~RMB 0.1/kWh higher than the coal-fired power. On a cost basis, large-scale power plants in areas with abundant wind resources will have an advantage. The introduction of the "subsidy-free tariff" policy will drive smaller wind power companies out of the market. Therefore, the overall installed capacity growth rate of the wind power industry will slow down after 2021. In our view, for the wind power industry to grow rapidly again, the national carbon emissions trading market will be crucial to growth in wind power industry.
  - **Solar power：** Generation cost of solar power is ~RMB 0.3/kWh higher than that of the coal-fired because 1) daylight limits the utilization hour and 2) the low conversion rate is still a major technological bottleneck. The introduction of the “subsidy-free tariff” policy has the greatest impact on the solar power generation industry because many are unable to reach the breakeven point and may exit the market. Support from the national carbon emission trading market will be indispensable

Policy Insight

China Education Sector

Paul Pan, Analyst

Related Policy:

- Improve the vocational education system and ensure more high-quality employment

Industry impacts:

- The emphasis on vocational education indicates that more relevant policies would be released.
- More room for growth in the vocational education sub-segment. According to the Government Work Report released earlier in 2020, the government targets to increase the total number of additional enrollment of higher education institutions by 2mn and to enroll a total of 35mn of student in vocational or technical training.
- Vocational education is mainly provided by higher education institutions, meaning that favorable policies would benefit the private education companies in the sub-segment. In addition, the proportion of private institutions in the higher education market was only 6.4% in 2019; therefore, room for growth is ample. We believe the boost of national vocational education offer a crucial opportunity for private higher education institutions to expand their presence in the next few years.

Policy Insight

China Consumer Sector

Paul Pan, Analyst

Related Policy:

- Increasing employment, improving social insurance, and optimizing income distribution structure by expanding the middle class are keys to increasing consumption.
- Improve the quality of life while expanding consumption; cancellation of regulations concerning administrative purchase limit; cultivate the consumption potential of rural counties and townships.
- To explore the full potential of domestic consumption; expanding consumption and effective investment to improve quality of life

Industry impacts:

- The Conference discussed the new normal after the pandemic; average per capita spending growth has stayed below the income growth, reflecting a conservative attitude in spending. In our view, the Conference stresses on formulating measures to stimulate consumption. The government intends to stimulate consumption indirectly through improving security and life quality. Since the pandemic has yet to run its course both inside and outside China, consumers will continue to tighten their spending; hence, the consumer staples sub-segment will be more defensive.
- The Conference emphasizes on exploring consumption potential in counties and townships, which could imply more favorable policies targeted at these rural regions. We believe leaders in the consumer industry will be more equipped to expand their network and or deepen market penetration in these areas.

Internet Media & Consumer Commerce

Steve Chow, Analyst

Related Policy:

- Strengthen the national R&D; formulate and implement a 10-year action plan for basic research; set up basic research centers; support the formation of international and regional R&D innovation centers.
- Support the role of enterprises in R&D and encourage leading enterprises to form strategic partnership SMEs in R&D activities.
- Support the innovation and development of platform enterprises and enhance global competitiveness; improve the legal framework for platform enterprises in the area of antitrust, data collection, and consumer rights protection; strengthen regulations, enhance supervision capabilities, and oppose monopoly and unfair competition. FinTech innovation must be carried out under close supervision.
- Optimize the income distribution structure and expand the middle class; removal of certain administrative restrictions on consumption; fully unleash the consumption potential in rural regions.

Industry impacts:

- Overall, the Conference supports the ongoing R&D and development of the new-economy industry, especially the ones in basic research.
- Support leading companies to build innovation consortia with SMEs, fostering strategic partnership or strategic investment activities within the industry.
- The government plans to strengthen the regulation targeting at the commercial behavior of the internet platform to prevent monopoly and unfair competition. This may change the commercial behavior of some companies, strengthen the protection of consumer rights, and promote a healthier industry ecology in the long run.
- FinTech may become one of the focuses in future regulations. The current business model of large-scale FinTech platforms may change, but the overall financial risks will also be reduced.
- Measures to expand consumption and tap consumption potential in rural regions are beneficial to the e-commerce industry.

Policy Insight

China Telecom Sector

Ricky Lai, Analyst

Related Policy:

- Expand domestic consumption demand - the formation of a strong domestic market is pivotal in building a new development model driven by consumption, savings, and investment.

- It is necessary to expand investment in manufacturing improvement and technological innovations.

Industry impacts:

- In 2021, telecom operators will launch the standalone 5G networks to strengthen the quality of telecom network. There are 700,000 5G base stations in China. We expect that the 5G penetration rate will further increase in 2021, and the domestic demand for data will increase. As of Oct 2020, domestic 5G users have exceeded 150mn. Telecom operators are promoting the growth of 5G users by launching the latest 5G smartphones and launching competitive service packages. Driven by lower service charges and the launch of affordable 5G smartphones, we expect telecom companies to develop emerging services such as IPTV, internet data centers, big data, cloud computing, and AI. China's 5G users will exceed 300mn in 2021E.

- Domestic consumption demand will be strengthened, and the demand for mobile phones is expected to improve in 2021. The shipments of 5G mobile phones of major mobile phone brands may increase significantly. The world will usher in a wave of 5G smartphone replacements and the penetration of 5G mobile phones will accelerate to 774mn units in 2023, accounting for 51.4% of all smartphone shipments. Our estimated CAGR for the global smartphone shipments in 2019-23E is 179.9%- the substantial growth will benefit domestic mobile phone makers and component developers.

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Disclosures

Analyst Certification

The analysts, CHAN Sung Yan, AU Yu Hang, Johannes, CHOW Sau Shing, LAI Pak Kin, NG King Chuen, PAN Hongxing, TUNG Yiu Kei, Kenneth, YAO Shaohua, being the persons primarily responsible for the content of this research report, in whole or in part, hereby certify that all of the views expressed in this report accurately reflect my personal view about the subject company or companies and its or their securities. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed in this report. I and/or my associates have no financial interests in relation to the listed company (ies) covered in this report, and I and/or my associates do not serve as officer(s) of the listed company (ies) covered in this report.

Definition of equity rating

Rating	Definition
Buy	Stock return ≥ Market return rate (10%)
Hold	- Market return (-10%) ≤ Stock return < Market return rate (10%)
Sell	Stock return < - Market return (-10%)

Stock return rate: expected percentage change of share price plus gross dividend yield over the next 12 months
Market return rate: average market return rate since 2008 (HSI total return index 2008-19 CAGR at 10%)

Time horizon of share price target: 12-month

Stock rating, however, may vary from the stated framework due to factors including but not limited to: corporate governance, market capitalization, historical price volatility relative to corresponding benchmark index, average daily turnover of the stock relative to market capitalization of the stock, competitive advantages in corresponding industry, etc.

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