China Equity Strategy

Top Q&As from Asia and US investor meetings

Equity Strategy

China

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A cautious mood from foreign investors

We have recently completed a few weeks of marketing seeing investors in Asia and the US. Investor sentiment on Chinese equities has turned noticeably more cautious in recent periods on the back of the weaker than expected GDP growth, the more restrictive property and taxation policies and uncertainties in regards to the AI tech supply chain. Interest in Chinese equities remains elevated however with the most frequent question being what is the likely government policy response to the weaker than expected economic growth. Our sense is that investors' positions are now lighter compared with June 2026 though it may take time for these investors to re-deploy in China as they await visibility on policies and tech earnings. Sector wise, our positive call on banks has garnered significant interest from foreign investors while many investors seem perplexed and somewhat frustrated by the weak performances in the battery and some of the industrial names. Positions and interest remain very light in consumer stocks while many investors are keen to hear ideas within the biotech and CRO sectors.

Foreign investors back on the sidelines

Investor sentiment has turned negative given the lack of policy response to a weak economic print though sentiment is nowhere near the trough that was reached in 2023/2024. Investors were also disappointed by the lack of diversification in Chinese tech stocks in the July sell-off and the weaker recovery subsequently as uncertainties around FCC restrictions and lack of domestic HBM weighed on the tech stocks. Our sense is that without meaningful policy response or better visibility on the domestic AI roll-out, international investors are likely to remain on the sidelines. While the elevated oil price and US interest rates could improve Chinese equities' relative appeal vs some of the other more vulnerable markets, we do not sense foreign investors will actively add Chinese equities at current levels.

Investor Q: What are the catalysts / events that could see the market rebound?

The key catalysts or events that we would be watching out for include: 1) policies that could alleviate local government financing or boost household income, 2) SOE funds' purchases in the A-share market, 3) alleviation in memory / HBM supply in China, 4) a meaningful rebound in A-share trading volume which historically has suggested additional inflows, and 5) stronger than expected pick-up in hardware tech earnings. In tech, we do note that China's AIDC deployment should continue to accelerate over time with the US AIDC roll-out set to slow down in 2028, this may start to make China's domestic AIDC roll-out more attractive vs the global peers some time in 2027.

Investor Q: Why are you positive on the banks?

We prefer Chinese banks for the following reasons: 1) revenue growth has accelerated to c.10% in recent quarters as net interest margins have stabilised, 2) dividend yield gap vs 10 year government bond yield remains higher vs historical average while the P/B valuation is significantly cheaper vs global peers, 3) share price diversification from AI and other sectors, 4) institutional ownership remains low with continued inflows from insurance companies supporting their share prices, 5) dividend payout has increased and could continue to rise further if loan growth was to slow.

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Investor Q&A

1. What are the likely policy responses given the weaker than expected GDP growth?

According to UBS China Economics team (see here), while the current macro environment shares some similarities with that of two years ago, policymakers are more likely to pursue staged easing measures rather than a sharp policy pivot akin to the September 2024 episode.

Our economists expect policy responses to be led by investment rather than consumption, specifically they include:

- Accelerate the remaining planned broad fiscal expansion in the rest of the year, equivalent to 0.7% of GDP (relative to H225);
- Faster fiscal disbursement and policy bank financing tools to support infrastructure, AI-related investment and industrial production;
- Consumption support is likely to remain relatively mild, while a LPR or RRR cut would be a positive surprise; and
- An additional fiscal package is probable, but any expansion beyond the existing budget will likely be data-dependent and may come later in the year.

2. What are the signals / events to watch to be more positive on Chinese equities?

A weaker set of macro data especially those closely related to GDP, e.g. industrial production, could create a greater sense of urgency for policymakers to deliver additional support measures in the near term. The upcoming October Politburo meeting and December Central Economic Work Conference (CEWC) are likely to serve as key windows for policy announcements.

The key catalysts that we are watching out for include:

- Policies that could alleviate local government financing or boost household income - we note that the property policy stimulus so far has disappointed (see Property and Econ teams' reports);
- SOE funds' purchases of the A-share market;
- Alleviation in memory / HBM supply in China;
- Better than expected tech earnings; and
- A rebound in A-share trading volume.

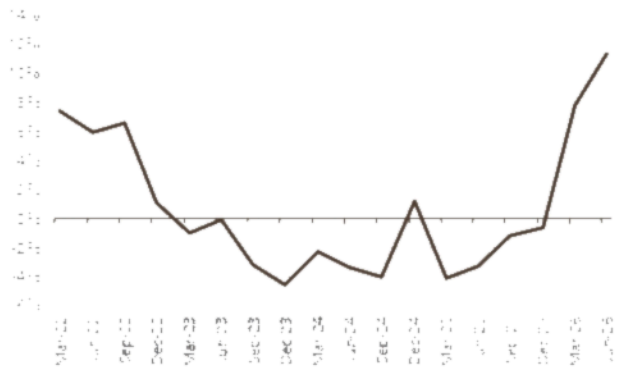
3. Why are you positive on the banks?

Following the July pullback and with the tech sector near-term performance impeded by component shortages, geopolitical uncertainty and crowded positioning, we expect investors to seek greater portfolio diversification.

We believe banks are well positioned in a subdued macroeconomic environment and amid persistently low domestic bond yields. In addition the sector has delivered improving topline growth in recent quarters while continuing to trade at undemanding valuations relative to global peers.

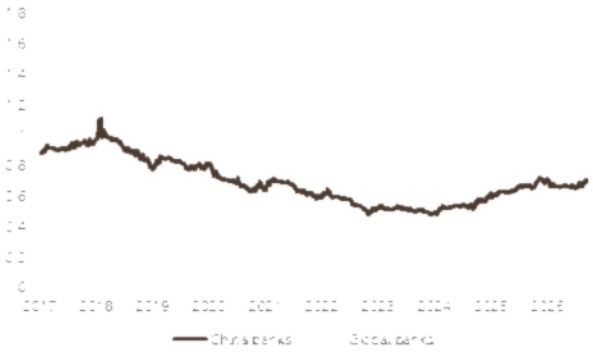


Figure 1: Major China SOE banks quarterly net interest income growth



Source: FactSet, UBS

Figure 2: China vs global banks P/B



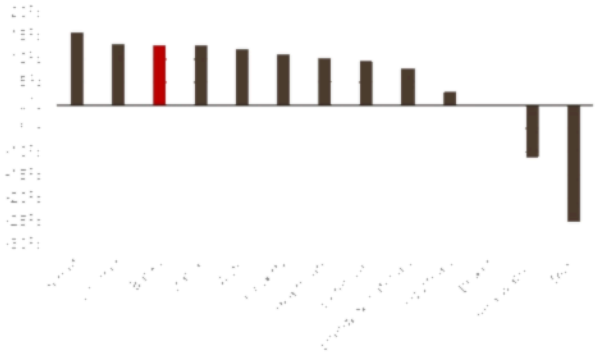
Source: FactSet, UBS

Figure 3: China, global banks and MSCI World performance



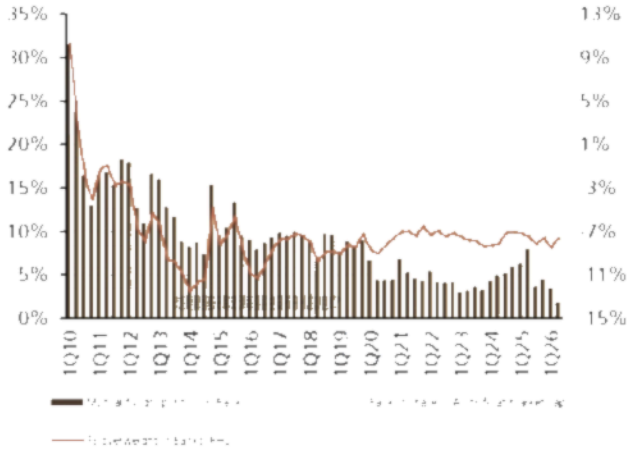
Source: FactSet, UBS, correlation of daily share price performance shown

Figure 4: China sector performance in July 2026 (AI sell off)



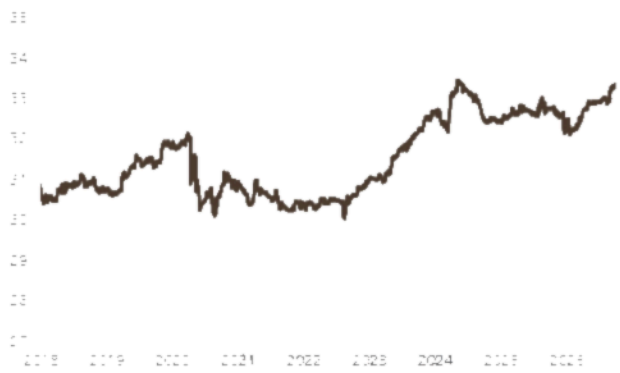
Source: FactSet, UBS

Figure 5: Onshore mutual funds positioning in Banks



Source: Wind, UBS

Figure 6: China banks forward payout ratio



Source: FactSet, UBS

As a reminder, we continue to adopt a barbell strategy. Our top sector and stock picks are shown below.

Figure 7: Sector preferences

Most preferred	Least preferred
Tech hardware	Construction
Internet	Auto OEM
"Going Abroad" stocks	Consumer
Non-ferrous metal	
Banks	

Source: UBS

Figure 8: Most preferred names

Most preferred names

Stock Code	Company name	Lead analyst	UBS rating	Last close	Price target	FY26 P/E	UBSe FY26 EPS growth	UBSe vs consensus FY26 earnings	Forward div yield	YTD return
9888 HK	Baidu	Wei Xiong	Buy	84.55	155.00	15.1	-52%	-3%	3%	-35%
3606 HK	Fuyao Glass	Nora Mi n	Buy	54.90	80.00	12.1	10%	5%	5%	-15%
2899 HK	Zijin Mining Group - H	Sharon Ding	Buy	32.24	57.80	8.9	60%	2%	4%	-8%
002371 SZ	NAURA Technology Group	Jimmy Hu	Buy	600.38	905.00	67.1	23%	-8%	0%	37%
0700 HK	Tencent Holdings	Kenneth Fong	Buy	427.20	770.00	12.6	0%	-1%	1%	-27%
300750 SZ	Contemporary Amperex Technology	Paul Gong	Buy	288.79	600.00	12.6	42%	3%	4%	-20%
600183 SS	Shengyi Technology	Edward Liu	Buy	139.28	192.00	41.5	136%	7%	2%	87%
BABA N	Alibaba Group	Kenneth Fong	Buy	167.74	226.00	15.4	-26%	-7%	1%	-26%
1211 HK	BYD Company Limited	Paul Gong	Buy	75.25	135.00	17.0	8%	-11%	2%	-20%
0883 HK	China National Offshore Oil Corporation	Amy Gu	Buy	23.64	33.60	5.7	39%	5%	7%	-16%
2259 HK	Zijin Gold International	Sharon Ding	Buy	143.90	203.00	16.6	79%	-8%	2%	-3%
002850 SZ	Shenzhen Kedali Industry	Nora Mi n	Buy	155.70	268.00	17.7	40%	8%	2%	2%
601229 SS	Bank of Jiangsu	Heeen L, CFA	Buy	12.39	14.00	6.3	10%	-5%	5%	22%
0939 HK	China Construction Bank	May Yan	Buy	9.74	10.20	6.6	0%	-5%	5%	29%

Addition

Stock Code	Company name	Lead analyst	UBS rating	Last close	Price target	FY26 P/E	UBSe FY26 EPS growth	UBSe vs consensus FY26 earnings	Forward div yield	YTD return
0981 HK	SMIC	Jimmy Hu	Buy	60.70	102.40	50.0	81%	-11%	0%	-15%
688525 SS	GKMT Corporation	Jimmy Hu	Buy	54.64	80.00	17.7	9553%	3%	1%	630%

Removal

Stock Code	Company name	Lead analyst	UBS rating	Last close	Price target	FY26 P/E	UBSe FY26 EPS growth	UBSe vs consensus FY26 earnings	Forward div yield	YTD return
GDS O	GDS	Sara Wang	Buy	31.26	52.00	23.3	79%	4%	0%	-12%
600584 SS	JCET Group	Jimmy Hu	Buy	64.47	135.00	43.7	72%	-9%	0%	79%
3908 HK	China International Capital - H	Dennis Ba	Buy	19.47	31.40	5.9	39%	-7%	3%	-1%
002532 SZ	Tianshan Aluminum Group	Sharon Ding	Buy	12.18	18.10	6.8	72%	-7%	8%	-21%

Source: UBS estimates

4. How are investors positioned given the sell-off in tech recently?

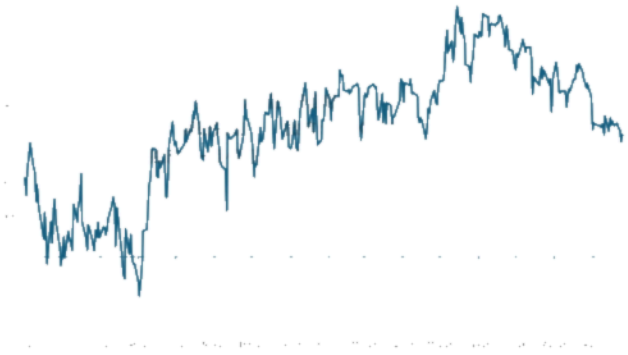
According to UBS Quant Research crowding score data, positioning in a basket of China AI hardware names has normalized from its June peak and is now back to levels seen in early 2026.

Onshore retail sentiment also appears to have softened since July. This is reflected in declining A-share market turnover and margin financing balance back to April levels.

While for MSCI China in general, foreign institutional investors' positioning in Chinese equities improved to -0.9% underweight in 2Q26, the highest level in the last 5 years. We believe this likely reflected a number of factors including: 1) their higher holding of A-shares which outperformed MSCI China (we estimate active funds are on average 4-5ppts overweight A-shares vs the benchmark), 2) forced selling in Korea and Taiwan due to allocation constraints resulting in inflows to other regions such as China, 3) record northbound / foreign inflows into A-shares, 4) participation in the HK IPOs and

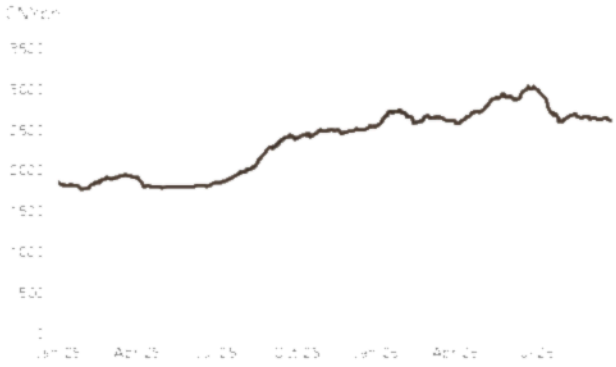
placements. That said, due to stronger performance in other regions, in absolute terms China's allocation has declined to 7.6% of the active managers' portfolios in 2Q26. Our monthly positioning tracker for the top 40 investors suggests that China positions have remained largely unchanged since June.

Figure 9: Average crowding scores of China AI hardware names



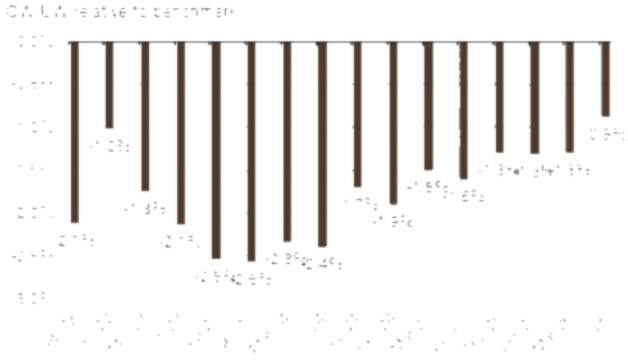
Source: UBS Quant Research Note: Last data point up to 25 Sep 2026

Figure 10: China margin purchase financing outstanding balance



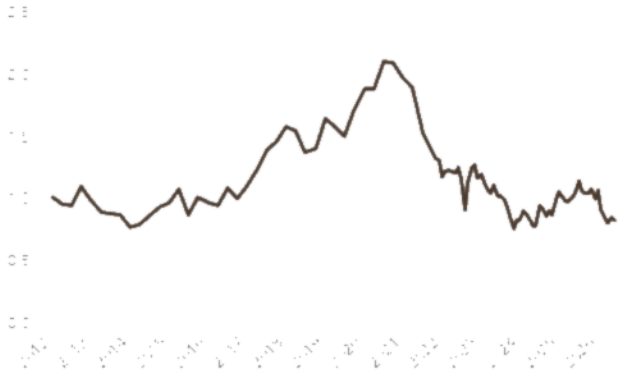
Source: CEIC, UBS

Figure 11: Actively managed funds' Chinese equity holdings vs benchmarks over time



Source: FactSet, UBS

Figure 12: Top 40 global investor positioning in Chinese equity (% of portfolio)



Source: FactSet, UBS Note: Last data as of Aug 2026

5. Which part of the tech supply chain would you invest?

We have set out a list of criteria for potential winners in the AI race (see here for more details)

- **Key supply chain bottlenecks** including:
  - **Memory** companies given ongoing HBM shortage and disciplined overall global capacity expansion;
  - **Semi fab companies** whose high end capacity determine the level of compute that can be produced;
  - **Semi-cap equipment** companies which are facilitating the domestic capacity expansion and are also benefiting from domestic substitution.
- **Industry leaders** as the barrier to entry for high end tech components has grown exponentially for AI tech hardware;
- **Exporters** given the higher profitability of overseas markets compared with the domestic market, supported by their established market share gains and proven competitiveness abroad.

Valuation Method and Risk Statement

For various stocks across the industries we cover in the Hong Kong and mainland China stock markets, we use a variety of valuation approaches, including DCF models, Gordon growth model analysis and relative valuation analysis using various multiples such as PE, EV/EBITDA and P/BV.

We think the risks facing China's equities include a hard landing for the property market, a capital exodus associated with currency depreciation and slow structural reform progress. In our view, any government policies that do not adequately address these risks could result in a shock to the market. For example, an excess of stimulus policies could pose a risk to the transition from an investment-driven to a consumption-driven economy and increase the debt of government and state-owned enterprises.