China Equity Strategy

Is it a good time to buy A-shares?

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Recent A-share pullback likely driven by unwinding of crowded tech positions

Since late September, the A-share market, particularly tech sectors, has seen a rapid pullback. Shrinking margin trading balances and subdued turnover point to weak investor sentiment. We think this round of A-share weakness differs from July's pullback, which was triggered by a cooling global tech narrative (Figure 2) and rapid deleveraging (Figures 3-5). The recent pullback seems to be driven more by a concentrated unwinding of elevated tech crowding (Figures 6-8), while mutual funds also face pressure related to break-even redemptions (note; Figure 9). Geopolitics, US Treasury yields and oil-price volatility have contributed to tighter dollar liquidity due to their impact on inflation expectations, weighing on market risk appetite.

Is it a good time to buy A-shares?

We note that major broad-based A-share index ETFs have seen a rapid increase in trading turnover since last Friday (Figures 10-11). Since 2024, whenever the SHCOMP has quickly pulled back below key levels (3,000 points in 2024, 3,200 points in 2025 and 3,800 points in 2026; Figure 1), ETFs have consistently recorded inflows (note). Unlike the 2024-25 episodes when ETF inflows were largely concentrated in CSI 300 ETFs, recent inflows have been more broadly distributed across CSI 300, CSI 500, CSI 1000, ChiNext Index and STAR 50 ETFs. As a result, we think the A-share market seems to be facing limited downside risks. In fact, A-share earnings appear to still be in an upcycle (note; Figures 12-14). In terms of trading data, the weekly trading turnover of the broader tech sector as a share of total A-share market turnover has fallen back to its early-April level this year (currently 37.2%, well below the historical peak of 49.7% recorded in early July; Figure 15). Trading crowding among the top-traded stocks by turnover has also declined markedly (Figure 16), suggesting that tail risks and positioning crowding have largely unwound. However, a rapid return of sidelined capital appears unlikely in the near term, as investor risk appetite may take time to recover.

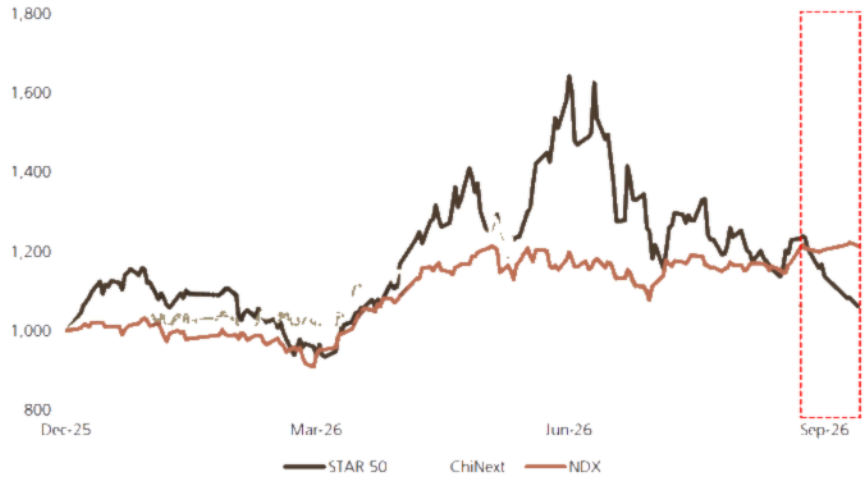
Figure 1: Key levels of the Shanghai Composite Index (SHCOMP) vs. units of major broad-based ETFs



Source: Wind, UBS-S estimates. Note: Data as of 13 October 2026.

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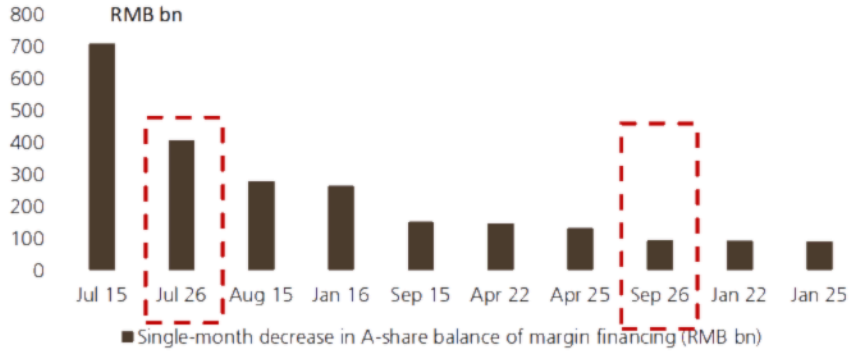
Figure 2: Recent performance of the STAR 50 and the ChiNext Index has diverged significantly from the Nasdaq 100



Source: Wind, UBS-S. Note: Data as of 12 October 2026. 31 Dec 2025 = 1000. All indices are measured in local currency terms.

We note that the STAR 50 Index and the ChiNext Index have generally moved in tandem with the Nasdaq 100 since the start of 2026. More recently, however, their performance has diverged, suggesting that the current A-share correction has had only a limited correlation with the global tech narrative.

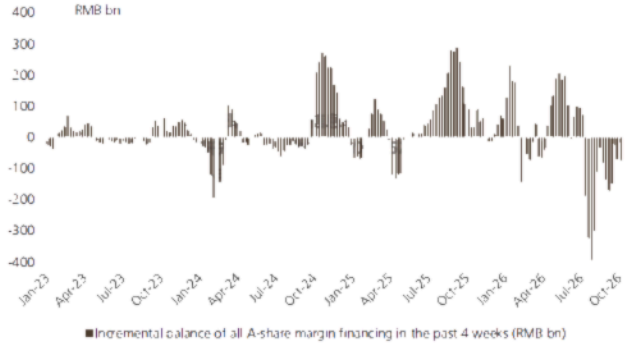
Figure 3: Top 10 largest monthly declines in A-share margin financing balances (historical record)



Source: Wind, UBS-S

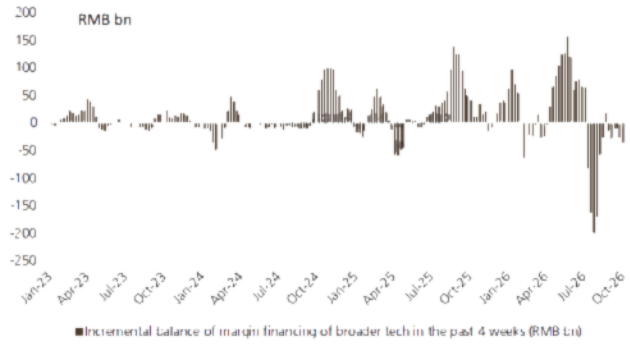
We note that the A-share margin financing balances fell sharply by Rmb408bn in July 2026. This was the second-largest monthly decline on record, surpassed only by the Rmb709.2bn drop in July 2015. The magnitude of the decline exceeded that recorded during the August 2015 A-share selloff, the January 2016 circuit-breaker episode, the worsening COVID situation in China in April 2022 and the escalation of China-US trade tensions in April 2025. More recently, the pace of the decline in margin financing balances has moderated at the margin, with margin balances declining by Rmb96.5bn in September 2026.

Figure 4: Change in A-share margin financing balances over the trailing four-week period



Source: Wind, UBS-S. Note: Data as of 9 October 2026.

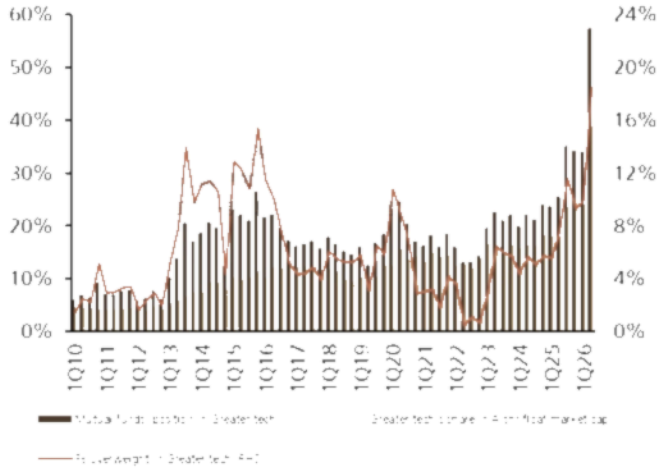
Figure 5: Change in the margin financing balances of A-share broader tech sector over the trailing four-week period



Source: Wind, UBS-S. Note: Data as of 9 October 2026. The broader tech sector includes electronics, telecommunications, computers and national defence.

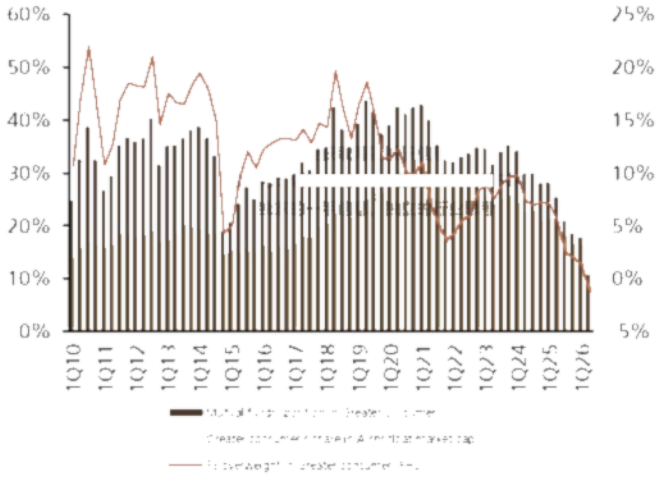
We think elevated positioning concentration in some sectors such as electronics and telecoms amplified short-term volatility. In mutual funds' Q2 reports, we note a significant rise in the overweight ratio of the broader tech sector, reaching an all-time high of 18.5%. This surpassed the previous peak of 16.2% in Q415 and approached the historical peak of 22.8% recorded for the broader consumer sector in Q310.

Figure 6: Mutual funds' overweight ratio in the broader tech sector rose sharply in Q226



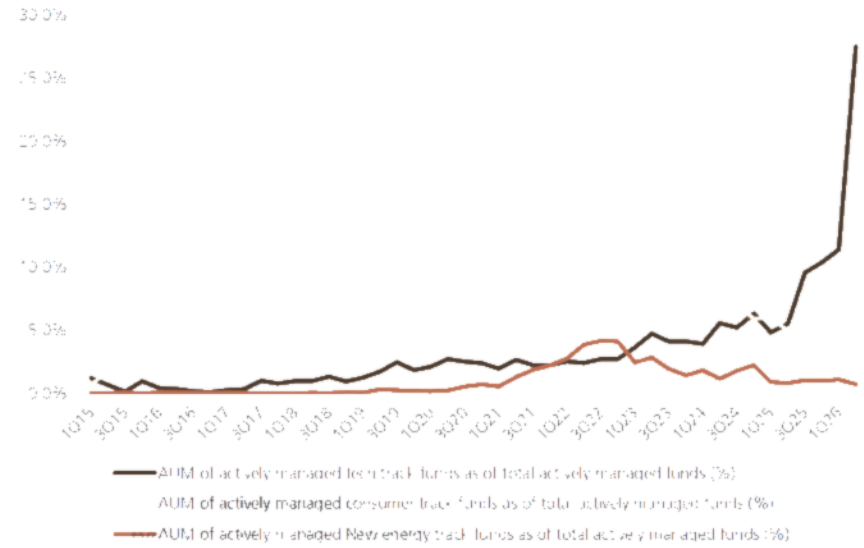
Source: Wind, UBS-S estimates. Note: The broader tech sector includes electronics, telecom, computers and national defence.

Figure 7: Mutual funds' position/overweight ratio in the greater consumer sector



Source: Wind, UBS-S estimates. Note: The broader consumer sector includes agriculture, food and beverage, healthcare, home appliances, textiles, light manufacturing, social services, commercial trade, beauty treatments and conglomerates.

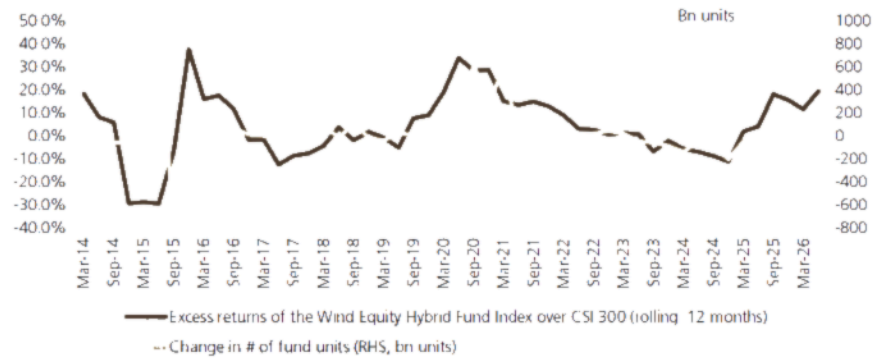
Figure 8: AUM of actively managed tech, consumer and new energy track funds as a % of total actively managed funds



Source: Wind, UBS-S estimates. Note: We define actively managed sector track funds as those where at least seven of the 10 largest holdings are from a specific sector and their combined weighting exceeds 50%. Tech funds cover electronics, telecoms, computer and national defence. Consumer funds cover agriculture, food and beverage, healthcare, home appliances, textiles, light manufacturing, social services, commercial trade, beauty treatments and conglomerates. New energy funds cover electrical equipment, utilities and autos.

We define actively managed sector tracking funds as those where at least seven of the 10 largest holdings are from a specific sector and their combined weighting exceeds 50%. We note the size of actively managed technology tracking funds has increased rapidly as a share of total actively managed mutual fund assets since Q225, to a record high of 27.5% in Q226. Given regulatory controls on "broad-mandate funds with concentrated sector exposure", mutual funds may have rebalanced their sector allocations since Q326.

Figure 9: Equity hybrid fund index's excess return relative to the CSI 300 vs. changes in units of actively managed equity funds

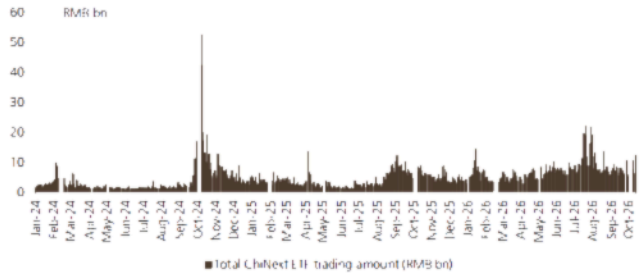


Source: Wind, UBS-S estimates. Note: Data as of June 2026.

Some mutual fund investors redeemed their holdings after returning to break-even in Q226. Some investors who purchased mutual funds during the market upswing in May-June may opt to redeem their holdings after recouping their losses during the August market rebound. This could create some selling pressure for the A-share market in the short term.

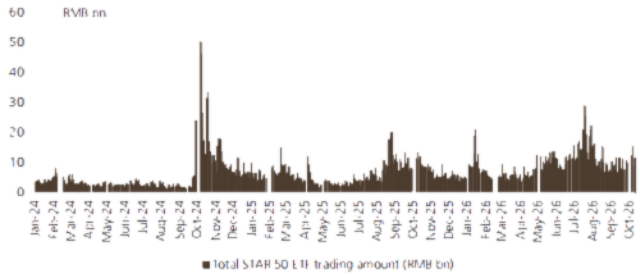
We note that turnover in some broad-based ETFs expanded rapidly during the recent sharp market pullback, followed by sustained large-scale net inflows over the subsequent trading days. Unlike the 2024-25 episode, when large net inflows mainly went to CSI 300 ETFs, recent net inflows have been spread across CSI 300 ETFs, CSI 500 ETFs, CSI 1000 ETFs, ChiNext ETFs and STAR 50 ETFs.

Figure 10: Daily turnover of ChiNext ETFs



Source: Wind, UBS-S. Note: Data as of 13 October 2026.

Figure 11: Daily turnover of STAR 50 ETFs



Source: Wind, UBS-S. Note: Data as of 13 October 2026.

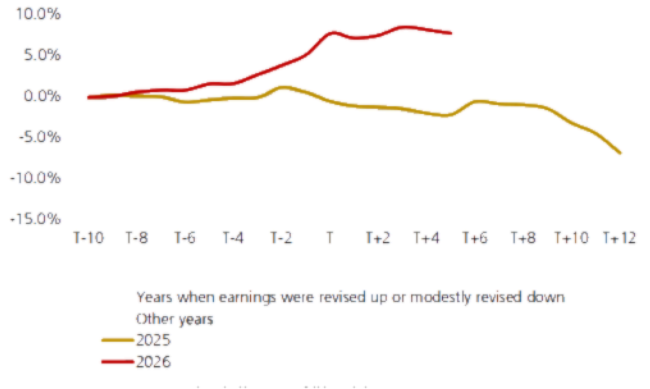
Figure 12: Earnings growth of all A-shares (YoY)

	2020	2021	2022	2023	2024	2025	Q1 2026	Q2 2026	H1 2026
All A-share	2.7%	20.8%	2.1%	-1.1%	-3.0%	2.9%	9.3%	29.4%	19.5%
A-shr excl. financials	4.1%	29.9%	3.0%	-3.0%	-14.1%	-1.3%	15.9%	26.9%	21.7%
A-shr excl. financials, Sinopec & Petro China & CNOOC	8.8%	23.7%	-1.3%	-2.9%	-16.2%	0.5%	17.0%	25.4%	21.5%
A-shr excl. financials, oil&petrochemicals and chemicals	5.0%	8.5%	-0.5%	7.8%	-15.5%	-2.6%	10.6%	14.4%	12.7%
Financials	1.3%	17.2%	11.1%	1.2%	10.3%	6.7%	2.1%	32.3%	17.0%
Main Board	0.8%	19.7%	1.4%	0.5%	-1.3%	1.5%	5.7%	23.7%	14.7%
STAR Board	87.1%	94.0%	12.7%	-48.8%	-33.6%	54.3%	667.0%	369.8%	437.6%
STAR Board excl. CXMT	87.1%	94.0%	12.7%	-39.1%	-38.5%	26.6%	195.6%	105.3%	129.8%
ChiNext Board	35.7%	22.8%	10.7%	-9.3%	-12.6%	21.7%	22.7%	41.8%	32.7%

Source: Wind, UBS-S

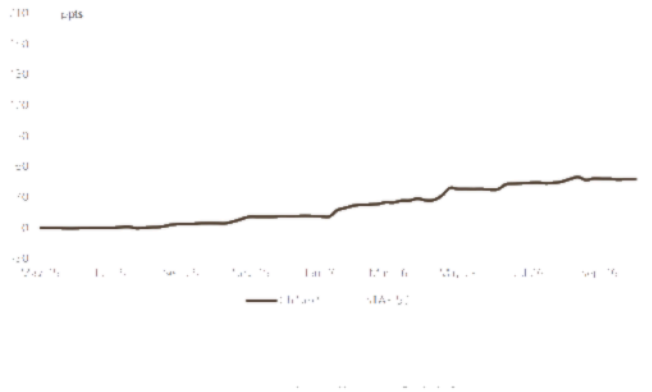
All A-share earnings growth accelerated to 29.4% in Q226, from 9.3% in Q126, leading to a 19.5% earnings gain in H126 (see report). We forecast all A-share earnings growth of 15% for full-year 2026. Notably, despite recent A-share pullbacks, consensus earnings forecasts have remained elevated.

Figure 13: CSI 300 earnings growth forecast adjustment (2014-26)



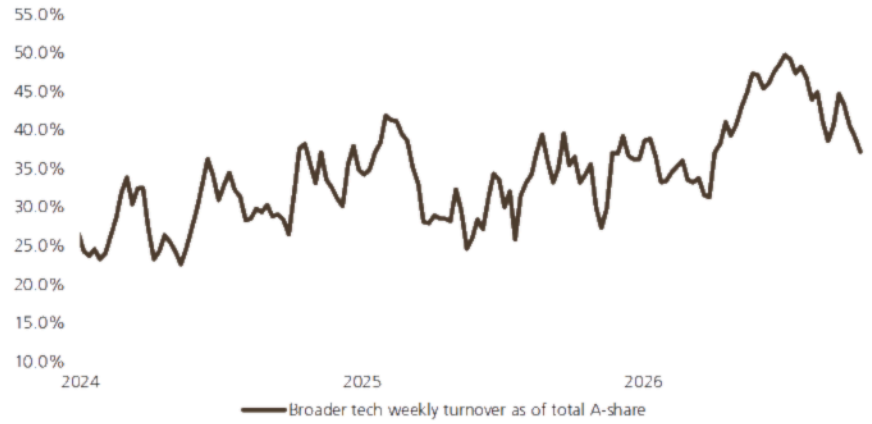
Source: Go-goal, UBS-S. Note: T refers to Go-goal consensus earnings growth for the CSI 300 in April of the respective year. For example, T in 2023 refers to April 2023. Years when earnings forecasts were revised up or modestly revised down include 2017, 2019 and 2021.

Figure 14: Revisions to consensus 2026 earnings growth estimates of ChiNext and STAR 50



Source: Go-goal, UBS-S

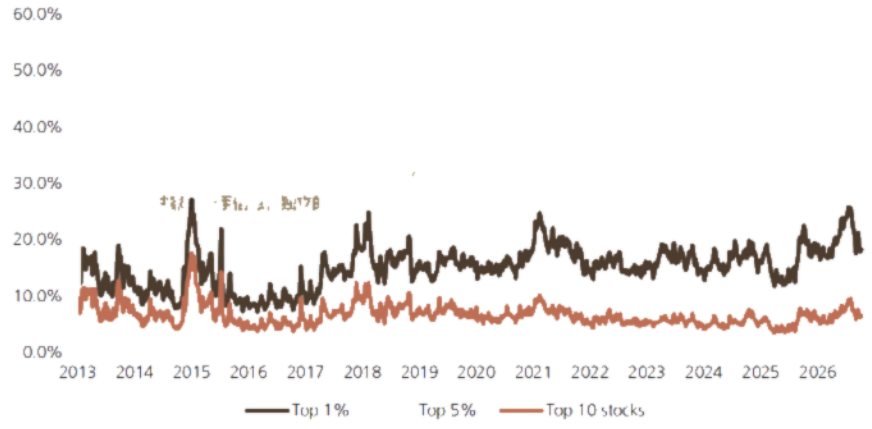
Figure 15: Broader tech sector as a % of weekly turnover for all A-shares



Source: Wind, UBS-S. Note: Data as of 12 October 2026. The broader tech sector includes electronics, telecoms, computers and national defence.

From a trading perspective, data shows the broader tech sector's share of total A-share weekly turnover has retreated to the levels seen in early April 2026 (currently at 37.2%, much lower than the historical peak of 49.7% in early July). This suggests crowding in tech sectors has largely eased.

Figure 16: Turnover of the top 1%/5%, and top 10 stocks (by turnover) as a % of all A-shares



Source: Wind, UBS-S. Note: Data as of 9 October 2026.

Turnover of the top 1%/5% and top 10 stocks (by turnover) as a % of all A-shares also fell to the levels seen in early April 2026.

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.