CHINA MUSINGS

Cash return is the best hedge to higher US rates (and lower China rates)

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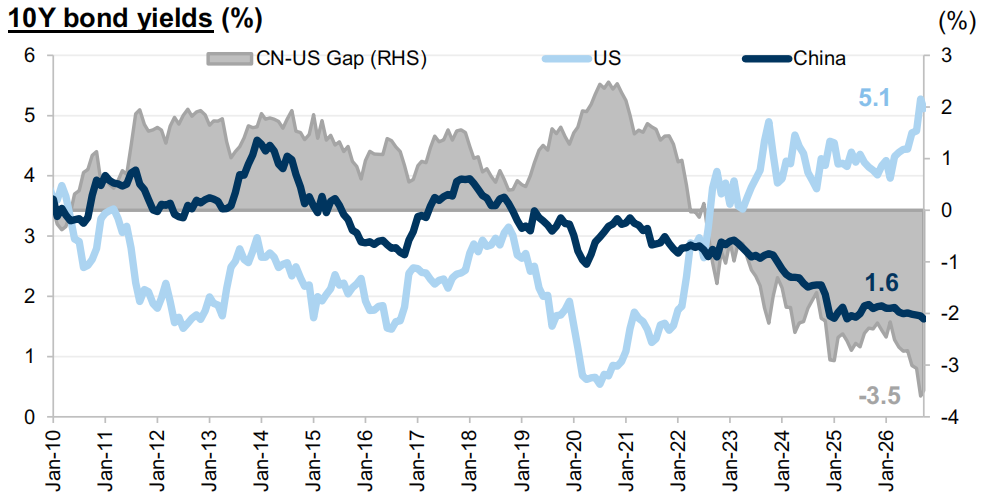
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1. A tale of two rate stories. Our US economics team expects the Fed to deliver one more 25bps rate increase in its December meeting and then keep rates unchanged thereafter until 2H27. 10-year US government bond yields, together with those in a number of DM and EM markets globally, have reached their decade highs in recent days, and the rates market is pricing in a rise of around 90bps in the Fed Fund rate to the end of 2027. However, China 10Y CGBs are hovering at their historical lows (now at 1.6%), and the PBoC has recently cut the PSL rate by 25bps to 1.5% to support "Six Network" investments. In this China Musings, we focus on the diverging US and China rate cycles and their implications to Chinese equities, and we reaffirm our tactical preference for A over H at the index level, upgrade Banks to Overweight, and continue to embrace a diversified, barbell approach to trade for alpha within the Chinese equity universe.

Exhibit 1: US-China yield gaps have widened to record highs

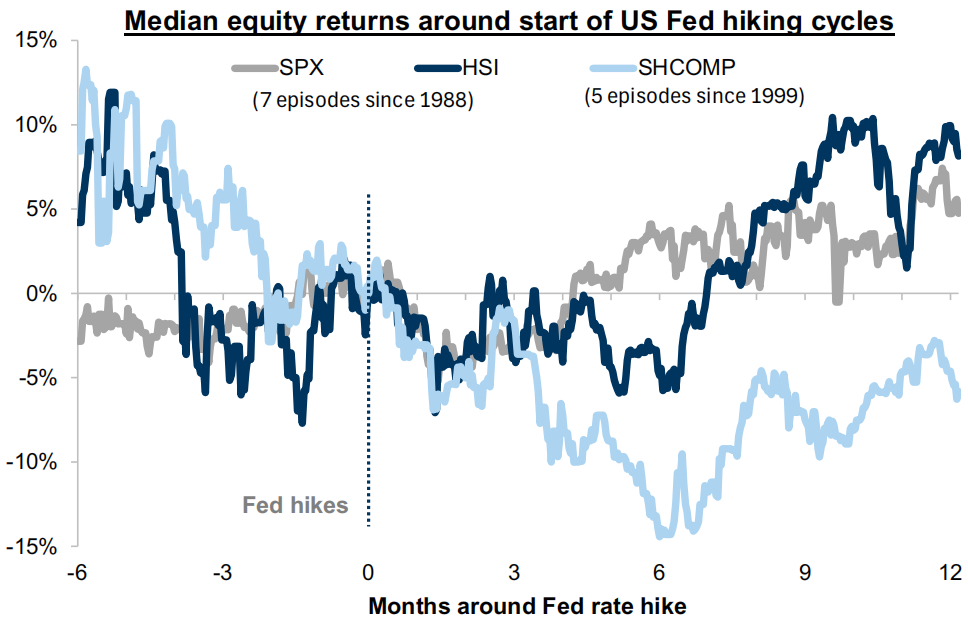


Source: Wind, Goldman Sachs Global Investment Research

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2. US policy rate increases are usually 2 to 3 quarters headwinds to equity returns. Empirically, US equities typically struggled around the start of Fed tightening cycles, but the market was able to digest higher policy rates in most cases after a period of consolidation and resumed the uptrend 4-5 months after the initial hikes. This historical pattern is also largely applicable to the HK/China markets, where offshore and onshore equities (proxied by HSI and SHCOMP) usually fell and range-traded in the first 6 months of a US rate-hike cycle and took around 3 to 4 quarters to return to previous peaks, everything else being equal.

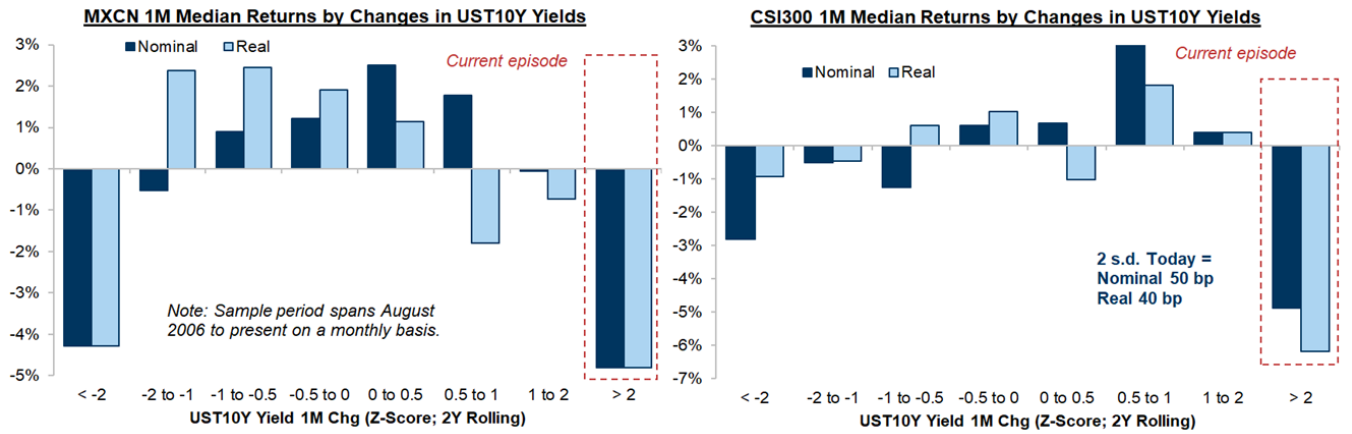
Exhibit 2: US and China equities typically struggled around the start of Fed tightening cycles



Source: Goldman Sachs Global Investment Research

3. Higher US (real) bond yields present a bigger test for equity returns. While equities were able to weather through higher policy rates historically, the impact of rapidly rising US bond yields, in both real and nominal terms, has been more challenging for equity performance in the short term. For both offshore and onshore Chinese equities, and the Asian stock market more broadly, we note fairly resilient performance when US bond yields have risen moderately, but usually had a more difficult time when 10Y US nominal/real yields increased more than 2 s.d. within 1 month, equivalent to 0.5%/0.4% of upward rate repricing respectively.

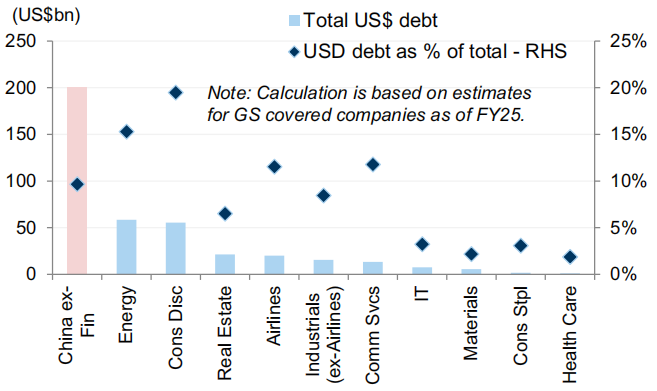
Exhibit 3: Rapid upward repricing of nominal and real US bond yields is usually suppressive to equities



Source: US Department of the Treasury, FactSet, MSCI, Data compiled by Goldman Sachs Global Investment Research

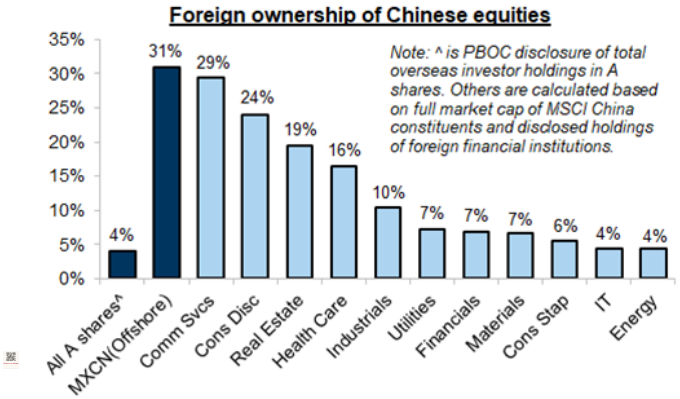
4. Flows trump fundamentals. Higher US rates could weigh on Chinese equity valuations via lower (expected) demand growth, higher financing cost, and increase in cost of equity (COE). From a financial leverage standpoint, the majority of Chinese corporate debt and bank loans are denominated in local currency, with foreign/USD debt representing around 10% of the total debt outstanding in the listed universe (ex-Financials) based on company disclosures. Also, considering that the Rmb has stayed resilient against the USD ytd, the foreign currency debt burden seems manageable for Chinese corporates. And with index valuations having already meaningfully de-rated (see #8 below), in our view, the potential pressures on equities could manifest mainly through the financial/capital flows channel which is likely to disproportionately impact the offshore market given much higher foreign investor participation compared with A shares, assuming that the tightening in US financial conditions doesn't result in a material slowdown in global growth and/or a significant risk-off event for global equities.

Exhibit 4: In aggregate, the foreign currency debt burden seems manageable for listed Chinese companies



Source: Company reports, Goldman Sachs Global Investment Research

Exhibit 5: Impact of tighter financial conditions in the US could impact the offshore market in a more pronounced manner

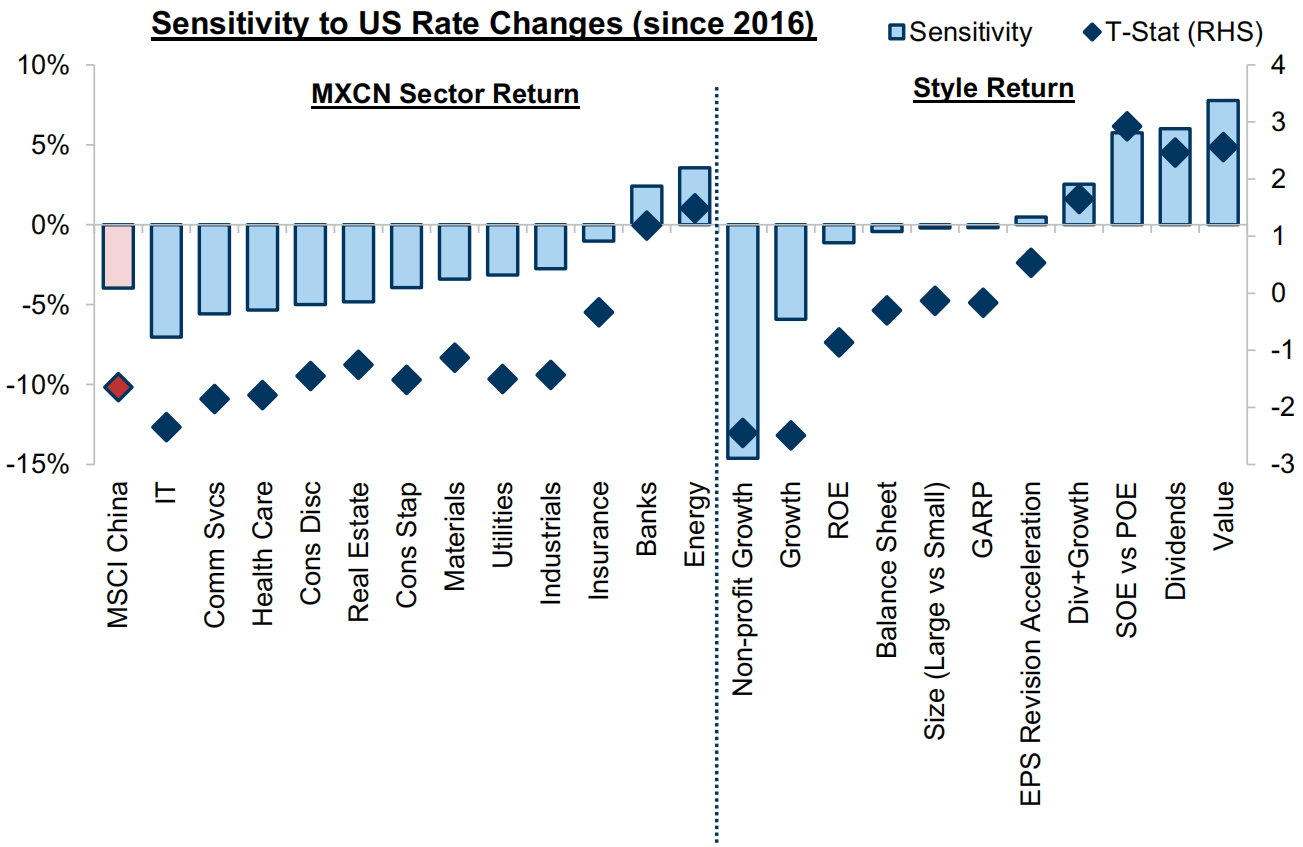


Source: Wind, Bloomberg, Goldman Sachs Global Investment Research

5. Cash return appears a good hedge to rising US rates. Sectorally, Energy, Banks, and to a lesser extent, Insurance usually outperform in a rising US rate cycle. The outperformance of Energy may reflect the impact of oil-induced inflation, which has often been a trigger for monetary policy tightening in past episodes. Chinese Banks also tend to benefit disproportionately in a higher interest rate environment likely due to NIM

expansion, especially during periods when US and China rate cycles were more in sync. Thematically, Value and Dividend-related factors have consistently fared well when US rates increased, showcasing the rise of valuation premiums for companies and/or sectors that are capable of generating stable and predictable cash returns to shareholders when risk-free rates rise. Conversely, non-profit growth stocks, or long-duration equities where a significant part of their current market capitalization is attributable to their future earnings streams usually lag in such an environment.

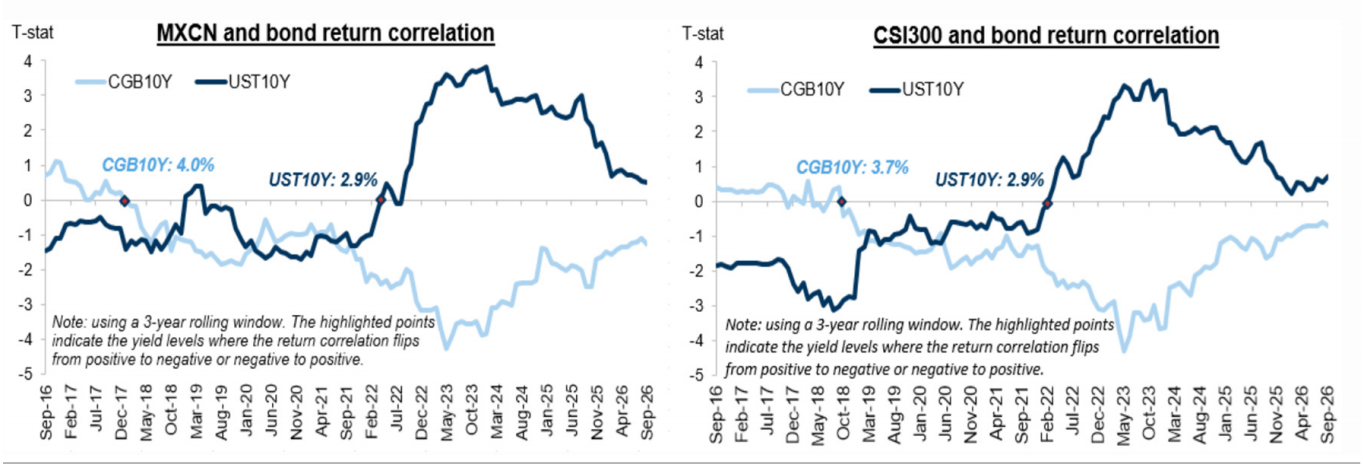
Exhibit 6: Value and cash returns typically outperform when US rates rise



Source: FactSet, Goldman Sachs Global Investment Research

6. US and China rates have unequal impact on China equities. China has been an outlier (and outperformer) in the latest global bond market selloff, with China rates extending their downtrend since 2023 and the 10Y CGB now trading near its all-time lows at 1.6%. In the post-Covid era, both A- and H-shares have exhibited positive return correlations with US bond prices (negative with bond yields), implying that US/global liquidity tightening has become an increasingly more dominant (and adverse) factor in Chinese equity pricing, especially when US nominal bond yields surpassed the 3% mark. Conversely, the equity-bond correlations onshore have remained firmly in negative territory, likely reflecting the subdued growth and inflation expectations from mainland investors, and the nature of Chinese equities being a potential effective hedge and a preferred asset allocation choice in a reflationary dynamic.

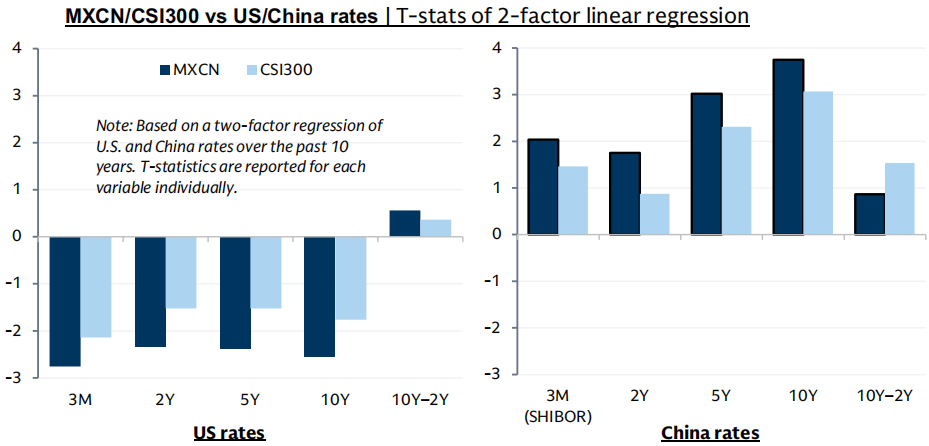
Exhibit 7: Opposite equity-bond correlations between US and China rates



Source: Factset, Wind, Goldman Sachs Global Investment Research

7. Do short- or long-end rates matter more for equities? Theoretically and empirically, 10-year government bond yields in both the US and China appear the most important financial and valuation anchor for Chinese equities. That said, equity return sensitivity vis-a-vis the front-end of the curves has been significant as well, notably US 3M Treasury rates and 3M SHIBOR in China. The shape of the yield curves in both the US and China has demonstrated positive relationships with equities (i.e., positive equity returns on yield-curve steepening and vice versa), although less statistically significant compared with the absolute level of bond yields along the curve.

Exhibit 8: Offshore Chinese equities are negatively correlated with both short- and long-end US rates

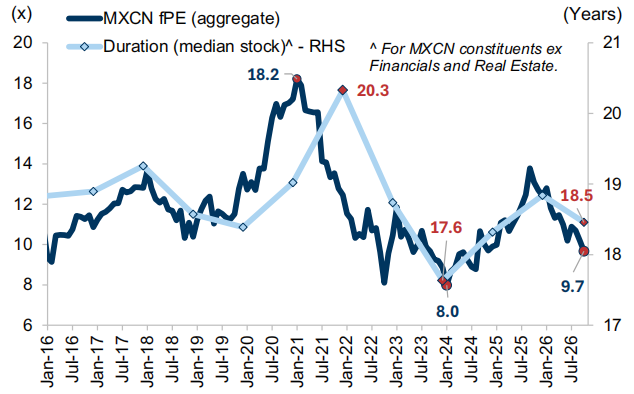


Source: Federal Reserve, PBoC, Wind, FactSet, Bloomberg, Goldman Sachs Global Investment Research

8. The diverging US and China rate cycles sync well with our tactical market preference for A (OW) over H (MW). Higher US rates may continue to restrain valuation upside and portfolio flows for H-shares where earnings (revision) momentum stays lackluster. That said, index PE has dropped to the low-end of its recent-year range, and the long-awaited earnings inflection point could materialize in the forthcoming results season, both suggesting rather limited drawdown risks from current levels if GS rate forecasts prevail. Domestically, compressed bond yields continue to imply elevated ERP for A-shares (CSI300) where 2Q26 profit growth reached 20% yoy, the highest since 2021. An attractive growth/valuation profile, continued supportive capital market policy

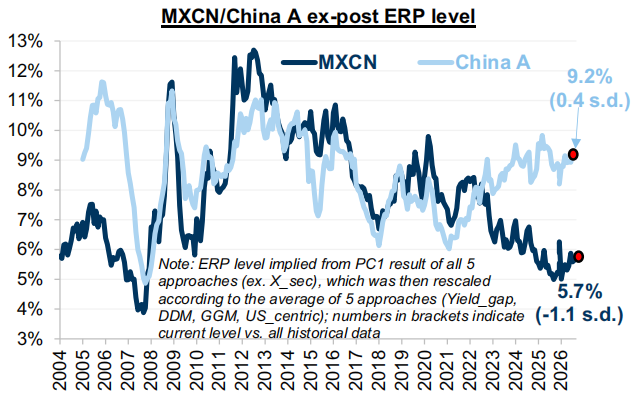
(e.g., liquidity support from the National Team), and easy financial conditions remain the key pillars of our constructive investment case for A-shares.

Exhibit 9: Index PE and equity duration of offshore equities are both at or close to cycle lows



Source: FactSet, Goldman Sachs Global Investment Research

Exhibit 10: ERP for A shares is at the high-end of its recent-year range

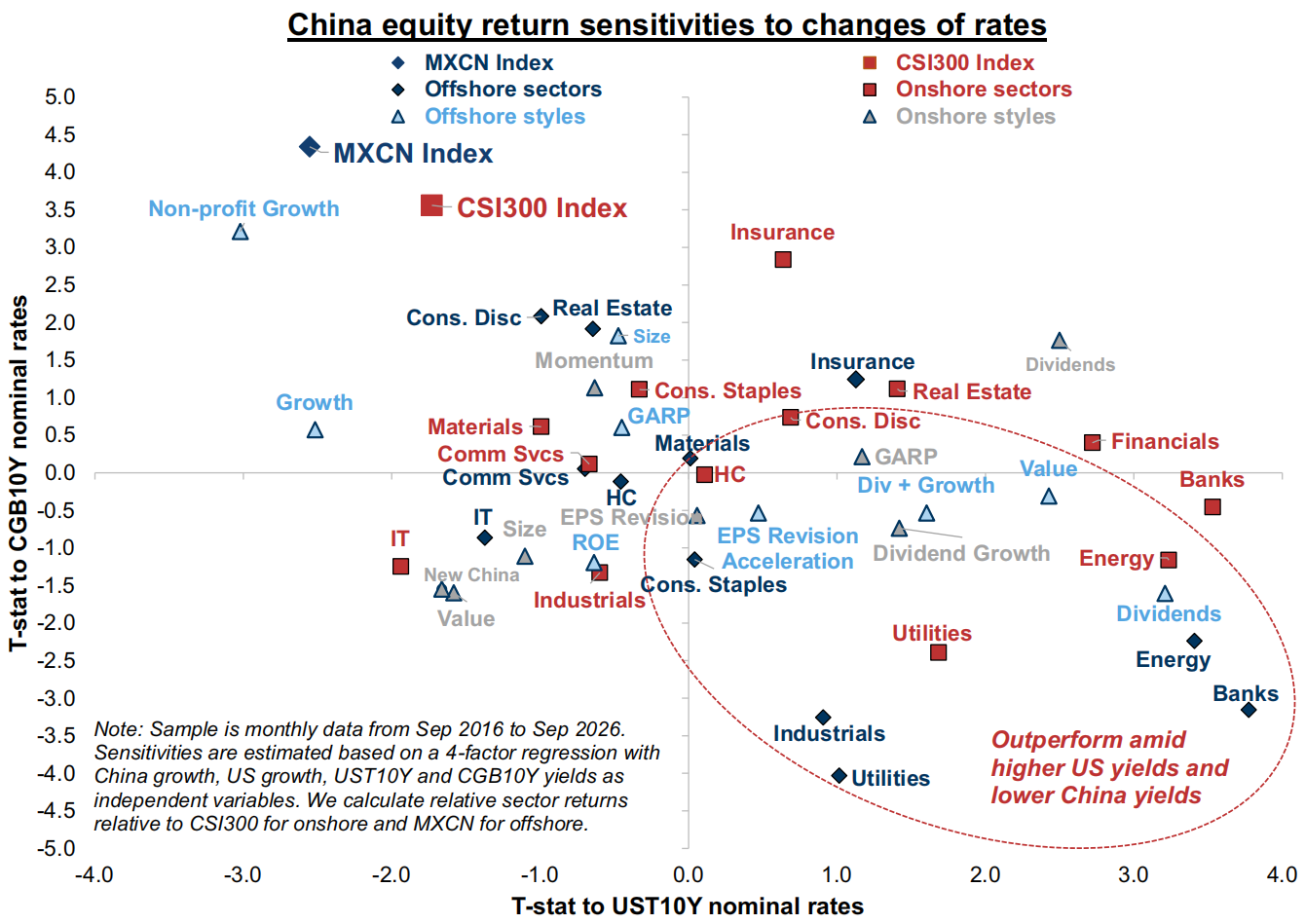


For detailed methodology, please refer to Global Strategy Paper | China ERP: Your risks and expected returns of investing in China, 4 July 2023

Source: MSCI, FactSet, Wind, Goldman Sachs Global Investment Research

9. Positioning in a bipolar rate environment. Holding macro growth factors in both the US and China constant and stripping out the rate and liquidity factors in our multivariate top-down regression model, we note that the themes of Value, Dividend, and Cash Returns appear best positioned to generate alpha for investors when rates in the US and China move in opposite directions, and/or the US-China yield spreads stay as wide as they currently are. This also leads us to raise Banks to Overweight but neutralize Insurance (to Marketweight) to further dial up the weights of the Dividend and Value factors in our sector allocation framework. On the flip-side, sectors with relatively high gearing ratios and USD debt exposures could come under pressure, notably airline operators, and select automakers, property developers, and AI infrastructure names (Exhibit 13).

Exhibit 11: Banks and Energy tend to trade better when US rates are high and China rates are low



Source: FactSet, Wind, Goldman Sachs Global Investment Research

Exhibit 12: We upgrade Banks to Overweight, funded by a downgrade of Insurance to Marketweight

Allocation	MSCI China industry groups	Weight in MSCI China (%)	26 Perf	26-28E EPS CAGR	27E P/E (X)	27E P/B (X)	27E PEG	Policy sensitivity ^	Growth sensitivity ^^	Valuation z-score^^^	Overseas revenue % ^^^^	MF Positioning (bp)^^^^^
Overweight	Banks	14.8	20%	9%	6.2	0.5	0.7	30%	32%	1.8	8%	-130
	Retailing	13.6	-24%	33%	10.2	1.3	0.4	50%	24%	-0.7	6%	43
	Tech Hardware	7.3	-8%	37%	13.1	2.2	0.5	10%	92%	-0.8	44%	-31
	Materials	5.3	-19%	12%	8.3	1.5	0.7	50%	76%	-1.1	18%	-1
	Capital Goods	3.5	-15%	18%	9.3	1.0	0.6	90%	56%	-0.1	12%	-1
Marketweight	Media	17.6	-31%	11%	11.3	1.8	1.1	50%	8%	-1.5	6%	43
	Health Care	5.9	11%	20%	23.9	2.9	0.9	80%	36%	0.3	28%	11
	Consumer Svcs	4.6	-26%	47%	12.6	1.7	0.4	50%	84%	-0.4	1%	-12
	Insurance	4.5	-20%	6%	4.6	0.7	0.5	20%	80%	-2.1	0%	-28
	Autos	3.6	-29%	42%	11.0	1.5	0.3	5%	68%	-1.4	21%	-8
	Energy	3.7	15%	3%	9.5	0.9	1.9	30%	72%	1.2	21%	-35
	Semis	2.2	1%	65%	37.1	4.6	0.9	50%	96%	1.0	22%	-31
	Utilities	2.0	-1%	8%	10.3	0.9	1.4	80%	16%	0.8	7%	-22
	Div Financials	1.9	-15%	10%	7.2	0.7	0.6	50%	88%	-0.8	9%	-28
Underweight	Food Bev	2.6	-12%	18%	13.6	2.4	1.4	30%	64%	-0.9	3%	3
	Consumer Durables	1.8	-15%	14%	9.9	1.6	0.7	10%	20%	-1.2	41%	-9
	Real Estate	1.6	3%	17%	11.0	0.6	0.8	90%	52%	1.3	0%	-4
	Transportation	1.6	-1%	8%	10.3	1.1	0.9	30%	44%	0.0	49%	9
	Telecom	0.3	-20%	8%	9.3	0.6	1.5	-	28%	-1.9	0%	-3

Note: ^based on overall score of policy scorecard, higher score indicates higher sensitivity to policy easing across 5 dimensions - financial condition, macro, property, and regulation; ^^based on monthly relative return (to MXCN) sensitivity vs. CAI growth (mom change on qoq); ^^^z-score vs. 5-year historical average; ^^^^based on MSCI China companies with available revenue by geography data; ^^^^^based on allocation in top Asia/EM funds as of Sep 30, 2026

Source: FactSet, MSCI, Factiva, EPFR, Goldman Sachs Global Investment Research

Exhibit 13: Sectors with companies with high gearing ratios and relatively high USD debt exposures could come under pressure if US rates stay elevated

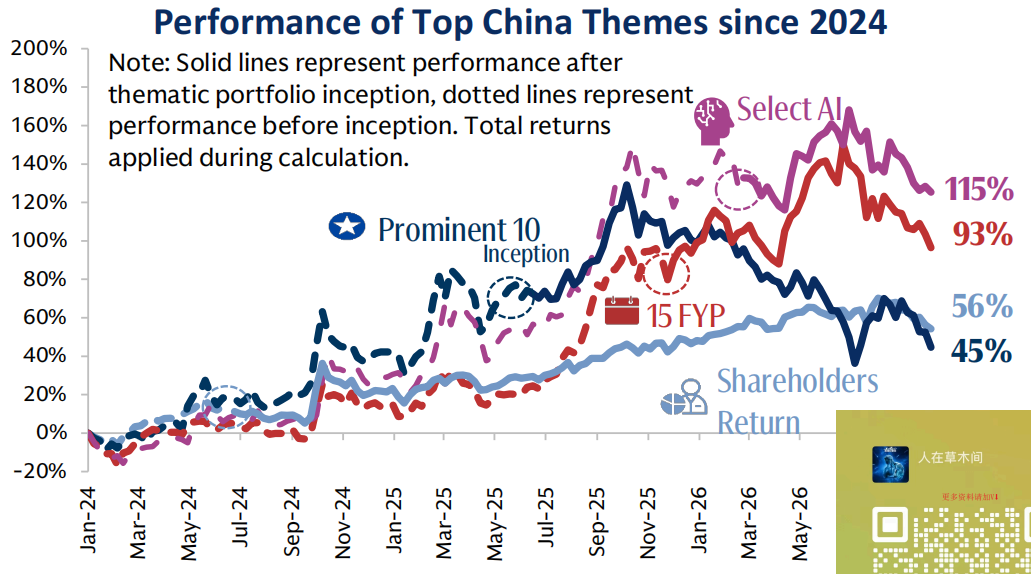
BBG Ticker	Company Name	GICS Sub-industry	Quoted Price		≥$1bn Listed Market Cap (US$bn)	≥$5mn 6M ADVT (US$mn)	≥1.0x Total Debt / Equity	≥10% USD Debt / Total Debt	2027E P/E (x)	2027E P/B (x)
Companies with high leverage and high USD debt exposure										
601111 CG	Air China	Airlines	CNY	5.64	9.8	76	3.9x	10%	39	1.9
600029 CG	China Southern	Airlines	CNY	4.72	9.5	67	8.6x	13%	26	2.2
600115 CG	China Eastern	Airlines	CNY	3.16	8.1	109	5.8x	11%	20	1.6
NIO UN	NIO	Automobiles	USD	3.39	8.0	152	7.1x	30%	47	8.6
000002 CS	China Vanke	Real Estate	CNY	3.50	5.1	112	3.2x	12%	-	0.6
656 HK	Fosun International	Conglomerates	HKD	4.90	5.1	5	2.3x	10%	9	0.3
960 HK	Longfor Group	Real Estate	HKD	5.05	4.6	19	1.0x	10%	18	0.2
GDS UQ	GDS Holdings	Internet Infrastructure	USD	22.47	4.4	72	1.5x	26%	-	1.0
VNET UW	VNET Group	Internet Infrastructure	USD	3.88	1.1	50	7.5x	21%	422	1.0
Median					**5.1**	**72**	**3.9x**	**12%**	**26**	**1.0**

Note: Ranked by market cap. Debt / Equity ratios reflect latest reported financials. USD debt exposure sourced from FY2025 filings. Valuations reflect FactSet estimates; pricing as of Oct 19, 2026.

Source: FactSet, IBES, Company data, Goldman Sachs Global Investment Research

10. Holding onto the barbell (approach). Our barbell strategy comprises a few of what we view as alpha-generating components in a difficult beta environment: a) on the Growth/offensive side, we still see the theme of AI as one of the strongest structural growth stories in Chinese equities, especially for AI hardware and certain healthcare firms that are well-placed to gain global market share and/or domestic AI companies that are favorably exposed to government policy support, notably the 15th Five-Year Plan. Our refreshed China Select AI Portfolio is a well-diversified list of 50 names across the 5 key layers of the Chinese AI value chain; b) the middle part of the barbell contains select H-share Internet names where valuation has significantly de-rated but profit growth could soon recover on GS forecasts ; and, c) shareholder/cash return proxies that have continued to generate superior Sharpe ratios and provide attractive cash incomes to the portfolio in both A- and H-shares (see Exhibit 15).

Exhibit 14: Our preferred themes and the corresponding portfolios' performance within the Chinese equity universe



Source: FactSet, Goldman Sachs Global Investment Research

Exhibit 15: Our GS China Shareholder Returns Portfolio includes a list of 30 companies which have been actively returning cash to shareholders

GS China Shareholder Returns Portfolio			>30 or >5 or >5						>10bn	>50mn				
Ticker	Name	GICS Industry Group	Payout Ratio (5yr avg, %)	27E Div Yield (%)	25 Buyback Yield (%)	SOE	Quoted Price	Quoted Currency	Listed Mkt Cap (US$bn)	6M ADVT (US$mn)	27E PE (x)	27E PEG (x)	26-28E EPS CAGR (%)	27E PB (x)
Stable Cash Cows														
939 HK	CCB	Banks	30	5.2	-	√	9.9	HKD	302	262	6	0.6	9	0.5
600519 CG	Kweichow Moutai	Food Bev	62	4.2	0.3	√	1325.0	CNY	248	774	18	3.1	6	5.8
601138 CG	Foxconn	Tech HW	54	3.6	0.0		47.7	CNY	142	1634	12	0.4	32	3.5
600036 CG	CMB	Banks	34	5.1	-	√	43.1	CNY	133	484	7	1.3	5	0.8
000333 CS	Midea	Cons Dur	56	5.5	1.9		86.5	CNY	89	391	13	1.6	8	2.6
3988 HK	Bank of China	Banks	31	4.9	-	√	6.1	HKD	65	141	7	0.7	9	0.5
2318 HK	Ping An	Insurance	43	7.4	0.3		50.1	HKD	47	244	5	0.5	9	0.6
000858 CS	Wuliangye	Food Bev	92	7.1	-	√	72.8	CNY	42	358	16	2.0	11	2.4
9618 HK	JD.com	Retailing	44	3.8	7.4		106.1	HKD	33	142	6	0.3	29	0.9
000651 CS	Gree	Cons Dur	55	7.5	-	√	39.9	CNY	33	252	8	3.6	3	1.3
300760 CS	Mindray	HC Equip	60	3.0	0.1		167.6	CNY	30	215	21	1.8	13	4.5
1109 HK	CR Land	Real Estate	34	4.5	-	√	31.1	HKD	28	111	8	0.8	10	0.6
2020 HK	ANTA	Cons Dur	44	4.0	0.9		78.0	HKD	28	72	11	0.9	13	2.1
600887 CG	Yili	Food Bev	76	5.6	0.1		27.8	CNY	26	229	13	1.8	18	2.9
600690 CG	Haier Smart Home	Cons Dur	43	6.1	0.5		20.8	CNY	19	135	9	0.9	9	1.4
000568 CS	Luzhou Laojiao	Food Bev	64	5.6	0.0	√	72.6	CNY	16	149	13	1.6	9	2.1
YUMC UN	YUM China	Cons Svcs	32	2.9	6.6		45.0	USD	15	71	13	1.3	13	2.8
			+>5pp in 25 vs. past 5Y avg						>5bn	>30mn				
Ticker	Name	GICS Industry Group	Payout Ratio (5yr avg, %)	25 Payout Ratio (%)	Buyback lending?	SOE	Quoted Price	Quoted Currency	Listed Mkt Cap (US$bn)	6M ADVT (US$mn)	27E PE (x)	27E PEG (x)	26-28E EPS CAGR (%)	27E PB (x)
Shareholder Return Improvers														
300750 CS	CATL	Cap Goods	19	50			267.0	CNY	170	1860	10	0.6	21	2.6
603288 CG	Foshan Haitian	Food Bev	61	113			34.2	CNY	28	97	23	2.9	9	4.6
603986 CG	GigaDevice Semi	Semis	19	32	√		282.4	CNY	28	3363	12	-0.8	0	3.9
002352 CS	S.F.	Transport	31	40			31.8	CNY	22	102	12	1.1	13	1.4
000338 CS	Weichai Power	Cap Goods	48	58	√	√	21.4	CNY	21	441	9	0.5	26	1.7
002714 CS	Muyuan Foods	Food Bev	24	48	√		41.2	CNY	20	298	8	-1.5	-	2.4
002050 CS	Sanhua	Cap Goods	35	41	√		32.7	CNY	18	649	26	1.6	19	3.6
002493 CS	Rongsheng Petrochem	Materials	77	113	√		11.7	CNY	16	106	13	0.8	15	2.1
600436 CG	Pientzehuang	Pharma	51	83	√	√	125.9	CNY	11	93	32	2.3	12	4.2
2057 HK	ZTO Express	Transport	27	43			158.3	HKD	11	38	9	0.6	13	1.3
002311 CS	Haid Group	Food Bev	32	50			43.5	CNY	11	68	14	0.7	28	2.4
002304 CS	Yanghe Brewery	Food Bev	79	100		√	38.0	CNY	9	40	23	1.5	16	1.2
600570 CG	Hundsun Tech	Software	19	31	√		20.2	CNY	6	93	24	1.3	18	3.2
Median							-	-	**28**	**149**	**12**	**1.1**	**12**	**2.1**
Aggregate									**1672**	**12914**				

Notes: Prices as of Oct 19, 2026; Valuation and EPS growth items are I/B/E/S consensus.

Source: FactSet, I/B/E/S, Goldman Sachs Global Investment Research