

## Monthly Report

### Macro economy:

The HSCEI in February will face further selling pressure due to a number of headwinds. After the Spring Festival holiday period, we believe the government will raise interest rates two to three times in 1H11. With the recent property tightening measures and the expected interest rate rises, housing prices may start falling as early as April 2011. We believe the market has yet priced in any significant decline in housing price.

The better-than-expected U.S. economy coupled with the unrest in Egypt may attract money to flow out of emerging markets and back into the U.S., generating further pressure on the Hong Kong market. However, the silver lining may lie in exports related sectors that will benefit from the better-than-expected U.S. economy.

Our model shows that the HSCEI index could fall by as much as 10.6% in the next three months as the Hong Kong market may be subject to another round of sell off.

We believe the PBoC will raise interest rates two to three times in 1H11.

#### 1) Inflation pressure remains high

Despite a small decline of CPI in December, we expect inflation to remain high through 1H11 as a result of rising domestic food prices and overseas commodity prices. Unusually dry weather over the past 6 months in northern China, where most summer grains are harvested, also adds to the inflation pressure in 2Q11. Our in-house estimate suggests inflation will remain high between 5% and 6% through 1H11.

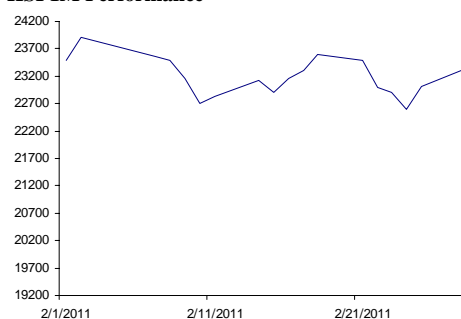
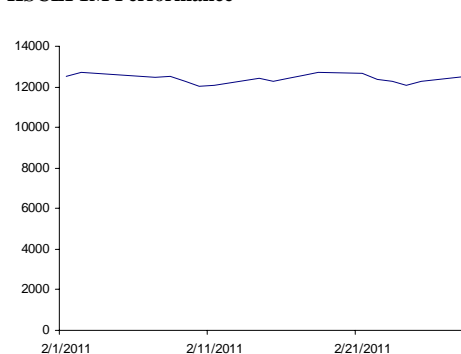
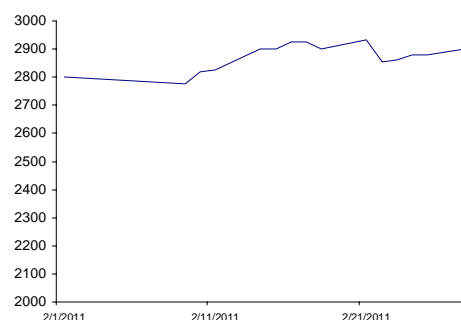
#### 2) Property Tightening Measures

Recent property tightening measures released in January suggests that housing market price correction may happen in April, much earlier than our previous estimate of 2H11. On the 26th of January, following a State Council executive meeting a number of property tightening measures were unveiled.

Hang Seng Index			
Index (%)	5 Days	1 Mth	YTD
HSI	1.76	(0.37)	1.57
HSCEI	2.18	0.68	(0.57)
Red Chip	2.07	(1.95)	(2.38)
Shanghai A	2.22	4.29	3.95
Shenzhen A	2.89	8.55	0.64

Source: bloomberg

Ended at 1/3/2011

**HSI 1M Performance**

**HSCEI 1M Performance**

**SHCOMP 1M Performance**


Amongst the new tightening measures, local residents are now restricted to only two properties and non local residents who already own one property, or can't provide proof of tax payments or social security documents are not allowed to purchase property. This measure, we believe if strictly enforced, will drastically reduce housing investment demand. The severity of this measure exceeds our previous expectation and we believe housing prices will correct earlier than expected.

Affordability will be another factor that will contribute to an earlier-than-expected correction in property prices. Our analysis suggests that affordability ratio (defined as 'monthly mortgage payment / monthly dispensable income') may exceed 60% in 2nd quarter of this year. The only time affordability exceeded this level was prior to the broad-based housing price corrections in mid-2008. If the average sale price were to rise by another 10% from the current level, then affordability would almost be stretched to severe levels seen during late 2007 and early 2008. The recently unveiled property tax in Shanghai and Chongqing will bring further pressure on affordability.

On a nationwide basis, surging new start areas in 2010 implies that the supply for this year may grow by more than 30% excluding affordable housing. With the new property restrictions, we believe demand will be greatly reduced which will then have a flow on effect to developers. The tight liquidity environment currently faced by real estate developers and the need to pay back bank loans will force price cuts in order to promote sales, further driving down housing prices. Under these conditions, we expect transaction volumes to freeze in 1Q11 and we expect property developers to start cutting prices after 3 months.

#### Recommended Stocks

	Current Price	2011 estimated P/E	2011 estimated dividend yield
CNOCC (00883.HK)	\$18.00	11.09X	3.29%
Dalian Port (02880.HK)	\$3.15	12.42X	2.94%

**Stock picks:**
**CNOOC (00883 HK)**

*Investment Rating & Valuation:* 'Buy' rating with a 6-month TP of HK\$24.70, implying a 16.7x 11E P/E. We forecast that EPS in 2010/11/12 will be RMB1.23/1.48/1.65, which is 5%, 9%, 16% higher than market consensus, respectively.

*Key Assumptions:* 1) YoY production growth are 40%, 15% 10% in 2010/11/12; 2) Realized oil price are 74/90/100 US\$/bbl in 2010/11/12.

*How we differ from consensus:* High oil export dependency and the need for national energy security will drive China's long-term demand for crude oil. We believe offshore China will be the country's strategic focus for oil exploration and production in the next decade. Meanwhile, deepwater projects are becoming more and more economically attractive. Supported by the government and base on much smaller reserve size (2.66 B BOE) compared to PetroChina (22.2 B BOE), we believe new deepwater oil & gas fields discoveries could make the company's reserve increase dramatically in the next years.

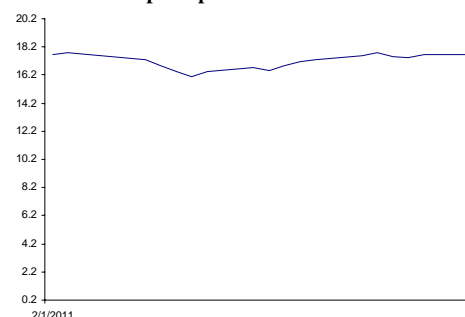
*Catalysts for share price performance:* 1) The announcement of 2010 earnings results in March 2011. 2) New deepwater discoveries.

*Risks:* 1) Falling crude oil prices. We believe that a 1% average realized oil price change would impact EPS by 1.5%. 2) Lower-than-expected production growth rate.

CNOOC (0883.HK)	
2011 estimated P/E	11.09X
2011 estimated P/B	2.74X
2011 estimated dividend yield	3.29%

Source: Bloomberg

CNOOC stock price performance



## Dalian Port (2880 HK)

**Investment Rating & Valuation:** We downgrade the company from 'Buy' to 'Outperform'. We are still quite optimistic about the company's long term growth.

**Key Assumptions:** Dalian Port's cargo throughput will grow amidst a recovery in the world economy and China's foreign trade.

**How we differ from consensus:** Container business contributed ~30% of EBIT for Dalian port, after the consolidation of iron ore terminals from parent company, and the market ignored this. Our macro economist has revised up 2011E export growth to 19.5% and Dalian Port will benefit. On the other hand, we will also see solid oil business growth in 2011. We will see robust growth of oil throughput especially in 2H11. Dalian Port will also raise the rental rate in 2011.

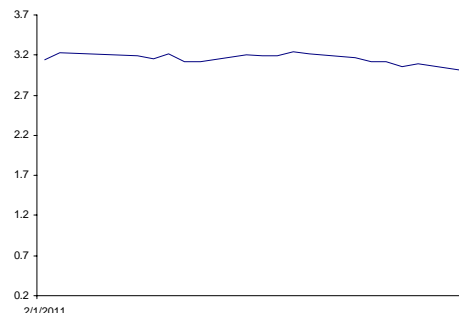
**Catalysts for share price performance:** 1) Recovery in the world economy and China's foreign trade, will boost cargo throughput

**Risks:** 1) China foreign trade recovery to be slower than expectation.

Dalian Port (02880.HK)	
2011 estimated P/E	12.42X
2011 estimated P/B	0.84X
2011 estimated dividend yield	2.94%

Source: Bloomberg

### Dalian Port stock price performance



#### Disclosure of Interests :

Ms. Ellie Chan, Mr. Jeffrey Mok, the Analysts, and their associates do not have any financial interests in the listed corporation(s) mentioned in this report.

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