Dividend forecasting

10 March 2022

How China's dividend factors in the Russia-Ukraine crisis

Ruiying Zhao, Research Analyst

Key Implications

- Automobile and parts, basic resources, energy, food and beverage, industrial goods and services, and technology will show a mixed picture—poised to benefit from government supports according to the "two sessions," but concurrently also exposed to the risks from the Russia-Ukraine crisis.
- Dividends risk is expected to stay low or medium, mainly attributable to three mitigating factors—policy support, state-owned entity (SOE) governance and infrequent dividend payers.

When geopolitical risks counter the "two sessions"

The National People's Conference (NPC) and the Chinese People's Political Consultative Conference (CPPCC) have set the roadmap for China's future agenda at "two sessions," the annual plenary sessions of the two conferences, last week. Sectors such as oil and gas, electric vehicles, and technology were highlighted under the goals of energy security, decarbonization and digital economy. However, the recent geopolitical tensions cast uncertainty on this blueprint as mainland China, a long-standing trade partner of both Russia and Ukraine, grapples with the implications from this conflict, particularly the economic impact through potential supply chain disruptions. The recent downtrend in stock prices for Chinese equity markets, in line with the volatility seen across global markets, seems to point toward strong headwinds for the roadmap going forward.

We have identified six sectors highlighted at the "two sessions" that are exposed to geopolitical risks—all marked as medium to high market risk based on our assessment in consideration of value chain analysis, stock price change, consensus earnings per share (EPS) change, and local news in the past two weeks. Next, we evaluate the dividends risk passing through market risk based on three mitigating factors: policy support, SOE governance, and infrequent dividend payers. Factor A assumes that policy guidance emphasized at the "two sessions" indicates the government's full year support for the sector, which is likely to provide ample buffer against demand/supply shocks. Factor B emphasizes the role of state-owned enterprises to maintain relatively stable payouts despite external or internal market shocks, based on our observation on historical patterns. Factor C refers to the situation that when some highly risky firms in a sector do not pay dividends, we estimate the overall dividend risk for a sector to be lower.

Contacts

Ruiying Zhao, Research Analyst · dividendsupport@ihsmarkit.com

Flow-down risks analysis of key sectors in mainland China

The pass-through from market risk to dividends is relieved by factor A, B, and C

	Autos and parts	Basic resources	Energy	Food and beverage	Industrial goods and services	Tech
Stock price change*	↓↓	↑	↑↑	↓	↓	↓↓
EPS consensus change*	↑	↑	↑	↑	↓	↓
Market risk						
A: Supported by government stimulus?	Yes	-	Yes	Yes	Yes	-
B: Mostly state-owned-enterprises?	-	Yes	Yes	-	-	-
C: Infrequent/zero dividend payers?	-	-	-	-	-	Yes
Dividends risk						

High Risk Medium Risk Low Risk

Note: *↓ or ↑ means the average absolute change is less than 4%. ↓↓ or ↑↑ means the average absolute change is above 4%.
Data is as of date of Mar 7th compared to that of Feb 21st, three trading days ahead of the invasion.
Source: IHS Markit

© 2022 IHS Markit

Dividend risk analysis by sector

Automobile and parts (low): Global sanctions against Russia may disrupt the chip supply chain further but the overall impact on Mainland China is mild. China has either diversified its chip related imports or strengthened its domestic production (including neon gas, palladium, and platinum) since the US-China trade war. Furthermore, for the year of 2022, the state planner **(Factor A)** has committed to removing curbs on Electric Vehicles gradually and therefore the risk flowing through to dividends is lower, such as **BYD Co (CNE100000296)** and **Amperex Tech (CNE100003662)**.

Basic resources (low): Steel and Iron ore from Russia were less than 1% of total basic resources imports last year.[1] Though the Aluminum imports from Russia were interrupted recently, the market relies largely on the long-term contracts, which are immune from the conflict. In terms of dividends, the risk is lower with the capacity of state-owned enterprises **(Factor B)** such as **Baoshan Iron & Steel (CNE0000015R4)** and **Aluminum Corp. of China (CNE1000000T0)** to maintain a sustainable dividend policy to counteract volatile earnings.

Energy (Low-Medium): To meet growing demand this year, China faces increasing pressure to maintain supply security from surging oil and gas import price reflected in supply costs. Nevertheless, the government may intervene to manage the volatility of price to avoid market disruption. **(Factor A)** At the Fifth Session of the National People's Congress last week, the government further highlighted that energy security is a priority. In terms of dividends, the risk is downgraded to low as major players such as **PetroChina (CNE1000007Q1)** and **China Petroleum & Chem (CNE0000018G1)** would sustain its payouts (including special dividends) even in years with muted earnings. However, we mark dividends at a medium risk for private enterprises such as **Xinjiang Beiken Energy Engineering (CNE100002C54)**, **ENN Ecological**

1. Data source: https://www.lgmi.com/guanshi/yjzx/index.asp

Holdings (CNE000000DG7), and **Guanghui Energy (CNE0000012G4)**, which rely largely on the spot price and not on long-term contracts.

Although Chinese power plants and steelmakers are looking for alternatives to Russia coal as some domestic banks are weighing commodity financing for Moscow, the overall risk is under control for a market where 90% of the coal is produced domestically.[2] The dividend risk is expected to be lower as major coal players responded firmly to government guidance **(Factor B)** when exposed to external or internal shocks historically, as shown in the case of **China Shenhua Energy (CNE100000767)** last year; the government-led coal titan boosted production as requested by Beijing during the nationwide power cut to mitigate demand/supply imbalance.

Food and beverage (low): Despite surging prices of imported commodities owing to the Russia-Ukraine crisis, the pressure on upstream costs is moderate because of diversified imported sources[3] and heavy domestic production[4]. Further, the "two sessions" **(Factor A)** set the full-year inflation target at around 3%.[5] Thanks to high domestic production, diversified import source, and government intervention on price control, we do not expect the profitability and dividend payout will be significantly impacted by the Ukraine-Russia crisis in the near term.

Industrials goods and services (low): In Mainland China, where electricity prices are tightly regulated,[6] the pass-through from energy cost pressure to end users is relatively moderate. But consumer usage of electricity is prioritized over that of manufacturers which adds uncertainty to the industrials. However, we label the dividend risk to stay low **(Factor A)** in consideration of the government's resolution to ramp up infrastructure projects for the 14th Five Year Plan (2021–25), which is expected to boost Industrials further this year.

Technology (low–medium): Global sanctions on exporting hi-tech products to Russia are creating a dilemma for Chinese tech companies with exposure to foreign markets. Companies demonstrated divergent responses as TikTok blocked Russia-run networks in EU while Didi cancelled its exit from Russia under public pressure. Chinese giant smartphone maker Xiaomi maintained a "wait and see" attitude toward sales in Russia concerning its business risk.[7] Although the geopolitical risks add more uncertainty to the Chinese technology firms, we do not see significant impact **(Factor C)** on the dividend performance. Among Hang Seng Tech Index, only **Lenovo (HK0992009065)** and **Tencent (KYG875721634)** are ranking in the top dividend contributors of the Index, and their dividends risk are expected to be at medium level. **SMIC (CNE1000041W8)**, **Xiaomi (KYG9830T1067)**, and **Didi (US23292E1082)** are not dividend payers and there is no signal for a regular cash dividend to be initiated from them in the near term, indicating a lower level of dividends risk. **TikTok**, owned by Beijing-based ByteDance, has not been listed yet.

2. "...domestic suppliers—responsible for 90% of China's coal supplies ..." https://www.ft.com/content/ff4f8306-e8b8-41e4-9ce0-702ec86ef182

3. "Soybeans are the only major crop where China relies heavily on imports—84% of domestic consumption in 2021, mostly from US and Brazil." Russia-Ukraine conflict has a limited impact on China's food prices (cnbc.com)

4. "Wheat imported from Russia accounts less than 1% of total imports." https://www.chinanews.com.cn/cj/2022/03-03/9690997.shtml

5. Data source: the state council, the people's republic of China http://www.gov.cn/zhengce/2022-03/06/content_5677461.htm

6. See the IHS Markit Strategic Report: Russia – Ukraine conflict: Global and regional growth and inflation implications

7. "Chinese smartphone shipments to Russia plunge as rouble collapses" https://www.ft.com/content/8f3e0214-94b1-4d73-b34f-31c189437578

Key dividends to follow

Stock name	ISIN	ICB sector	Impacted index
PetroChina	CNE1000003W8	Energy	FTSE China 50, CSI300, Hang Seng Index
China Petroleum & Chem Corp	CNE0000018G1	Energy	FTSE China 50, CSI300, Hang Seng Index
CNOOC	HK0883013259	Energy	Hang Seng Index, Hang Seng China Enterprises
Lenovo Group	HK0992009065	Technology	Hang Seng Tech Index, Hang Seng Index
Tencent Holdings	KYG875721634	Technology	FTSE China 50, Hang Seng Tech Index, Hang Seng Index, Hang Seng China Enterprises

Note: Only stocks from analyst coverage included.
Source: IHS Markit

IHS Markit Customer Care

CustomerCare@ihsmarkit.com

Asia and the Pacific Rim

Japan: +81 3 6262 1887

Asia Pacific: +604 291 3600

Europe, Middle East, and Africa: +44 (0) 1344 328 300

Americas: +1 800 447 2273

IHS Markit®