Online gaming under the spotlight again

China update

In November, Chinese equities experienced positive gains, albeit lagging behind global markets which saw robust rallies amid declining inflation and optimism for a soft US economic landing. Initial enthusiasm from the mid-November meeting between Presidents Biden and Xi waned as little real progress was made despite positive behind-the-scenes developments.

- **The MSCI China and MSCI China A Onshore indices recorded increases of 2.5% and 1.2%, respectively.**
- **Communication Services and Information Technology sectors emerged as leaders in market performance.**
- **Tencent showcased robust growth, up over 13% on better-than-expected earnings data.**

Chinese equities: The month of November in review

China's ongoing economic recovery showed signs of weakness in November. The manufacturing PMI declined to 49.4, suggesting a small contraction and continuing its moderation from October, while the non-manufacturing PMI reached its lowest reading for the year. The Property sector remained a challenge for the economy, with house prices weakening further. Nevertheless, policy easing efforts continued, leading to increased transactions in Tier 1 cities after minimum down-payments and mortgage rates were reduced. Additionally, the Chinese central bank injected a record amount of liquidity into the banking system in mid-December.

Investors are eagerly awaiting clarity on Beijing's growth objectives for 2024 and seeking more concrete signals regarding the government's plans to stabilise the economy in the coming year. While the annual Central Economic Work Conference highlighted the importance of high-quality growth and reiterated the commitment to supportive fiscal policy, it fell short of providing any specific growth targets.

Just when we thought we could bid farewell to the challenges of 2023, an announcement of new online gaming guidelines right before the Christmas weekend plunged shares of Tencent, NetEase, and other gaming/tech stocks into a steep decline, undermining one of the few fast-growing industries in the Chinese economy. The impacts of this development are twofold. Firstly, from a fundamental perspective, the implementation of restrictions on in-game spending and rewards is expected to significantly reduce daily active users and in-app revenue for most online games.

Secondly, this move served as a reminder of the government's previous regulatory crackdown on the tech sector during 2020-2021.

Policy easing efforts in the Property sector led to increased transactions in tier 1 cities.

In mid-December, the Chinese central bank injected record liquidity into banks.

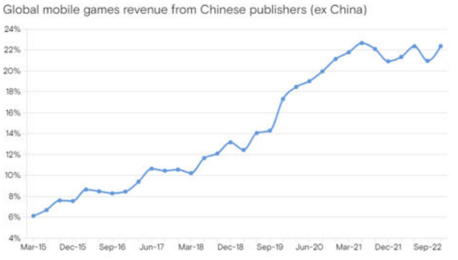
Investors seek clarity on Beijing's 2024 growth goals and plans for stabilisation.

International markets account for over 30% of Chinese companies' total online games revenue.

Given the current economic conditions, the timing of increased regulation is particularly unfavourable. However, in response to market turmoil and industry concerns, the Chinese regulator swiftly adjusted its stance by approving new game titles and expressing a willingness to consider feedback on its plans. As a result, shares of tech stocks managed to regain some of the lost ground in the following trading days.

China's Global Dominance in Online Gaming

China's online games industry is the largest in the world, boasting a user base of approximately 650 million and generating $45 billion in sales in 2022. To fuel growth and diversify business risks, Chinese game developers and publishers have increased overseas expansion. They employ strategies such as development and publishing-only, co-development with international companies, and mergers and acquisitions. They have also looked to create more games that cater to a global audience. These efforts have increased the market share of Chinese companies in global mobile gaming from under 10% in 2017 to 22% in 2022, and international markets now account for over 30% of Chinese companies' total online games revenue, according to research from Goldman Sachs.



Source: SensorTower, Goldman Sachs Research.

The RisCura team would like to extend our warmest wishes for a prosperous and Happy New Year to you and your loved ones!

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