

China Portfolio Risk Recap: Q2 2024

July 15, 2024

MPER China Analysts (mper@rhg.com)

This note reviews changes in MPER China risk scores in Q2 2024 and discusses the policy outlook. The highlights are:

- **Foreign investors continued to add exposure to Chinese securities in April and May, but the momentum reversed in June** as the rally in onshore equities fizzled out and a domestic flight to safety dragged bond yields to record lows.
- **Sanctions Exposure Scores** jumped in Q2 as blacklisting activity reached a new high due to concerns about Chinese entities sustaining Russia's war in Ukraine (40% of newly sanctioned entities), contributing to China's military modernization (21%), facilitating human rights violations (13%), and supporting terrorist organizations (13%).
- **Fundamental Risk Scores** saw major updates following the release of information in annual reports and several methodology updates. The biggest moves were driven by disclosures around subsidies, industrial policy funding, state ownership, executive linkages to the PLA and CCP, and sensitive technology development involvement.
- **Controversy Exposure** remained high in Q2—53 of the issuers we track were implicated in major China risk stories. The most prominent Controversy Stories were Subsidies to Strategic Sectors, Tech Self Reliance and Support of Iran.

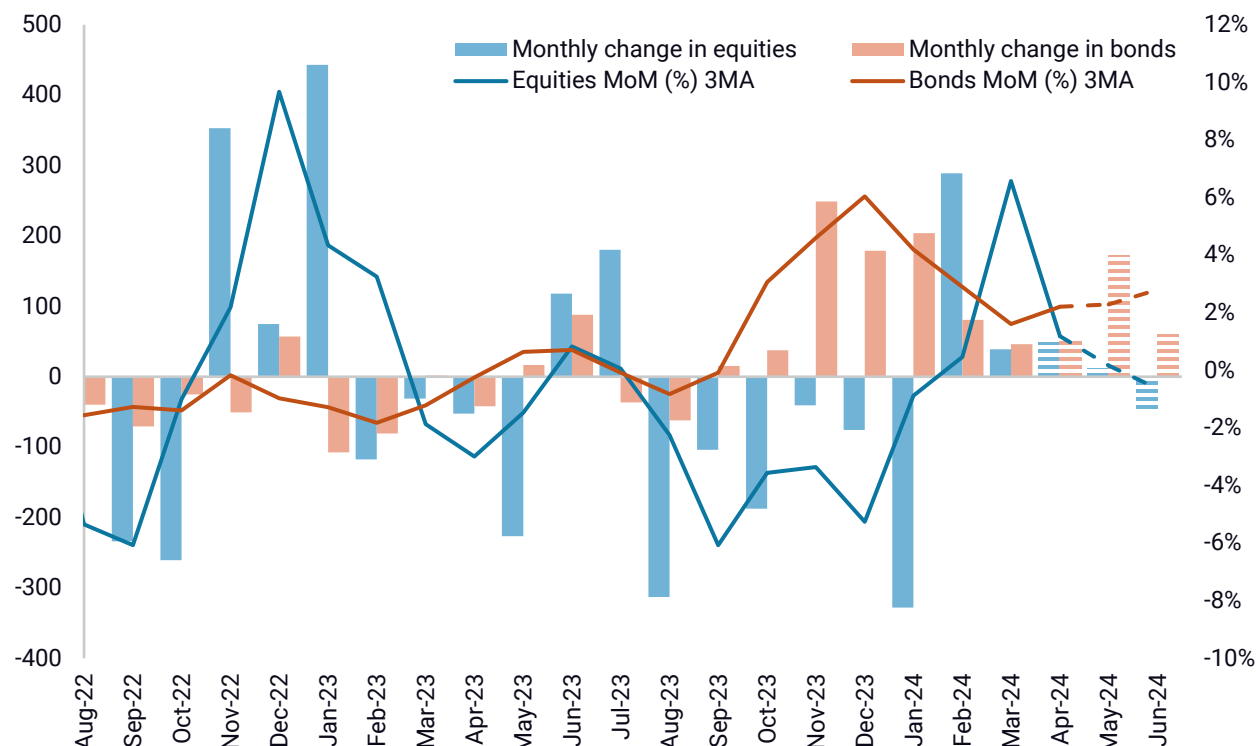
Foreign portfolio investment momentum

Foreign investors continued to increase exposure to Chinese securities in Q2 2024, but momentum slowed toward the end of the quarter (Figure 1). Investors bought **equities** in April and May but reduced their exposure in June as the rally fizzled out and the Shanghai Composite Index dipped back below the psychologically important 3,000 points mark amid concerns about earnings and domestic economic resilience. Foreign demand for **bonds** remained relatively solid throughout Q2 but as Chinese investors sought safer assets, bond yields dropped to two-decade lows. Yields on 20- and 50-year bonds have been trading at historic lows for months and the 10-year government yield slipped to 2.22% at the end of June, the lowest since records began in 2002.

FIGURE 1

Monthly change in foreign holdings of onshore CNY equities and bonds*

Monthly change in RMB billion (left) and percent m-o-m change 3MA (right)



Source: Rhodium MPER China based on data from the PBOC. *Estimates for the latest months based on fund flow and other high frequency data.

Sanctions Exposure

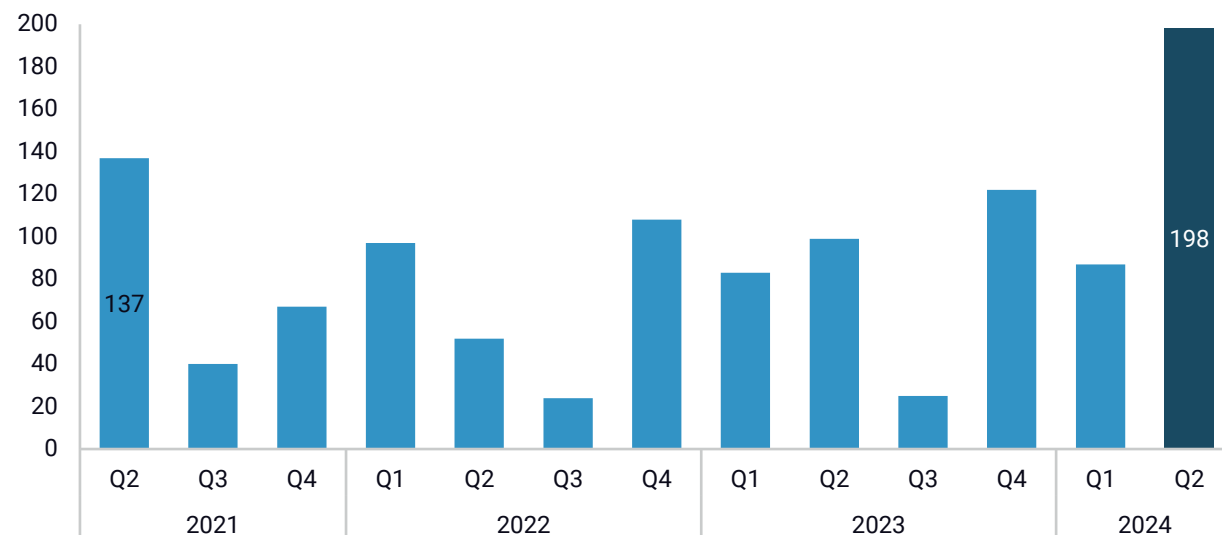
Governments added a record 198 Chinese entities to [major OECD sanction programs and blacklists](#) in Q2 2024, surpassing the previous all-time high of 137 additions in Q2 2021 (Figure 2). This intensification of blacklisting activity was driven by heightened concerns about Chinese entities providing support to Russia's military-industrial complex, accounting for 40% of the newly sanctioned entities. Chinese firms have also been added to sanctions and red-flag lists for supporting China's military modernization, including its quantum and "spy balloon" programs (21%), enabling human rights violations (13%), and supporting terrorist organizations (13%) (Figure 3, right).

These developments added new Sanctions Exposure Scores to 17 Chinese security issuers. The scores of 12 other issuers changed due to equity investments and divestments made in Q2 2024. A selected sample of issuers with updated Sanctions Exposure Scores is shown in Table 1, with the full data available on [the MPER portal](#). The changes increased the cumulative Sanctions Exposure Score of all 8,476 securities in our sample to 5,047 (Figure 4).

FIGURE 2

Chinese entities added to major sanctions and red-flag lists

Number of newly sanctioned or red-flagged Chinese entities by quarter

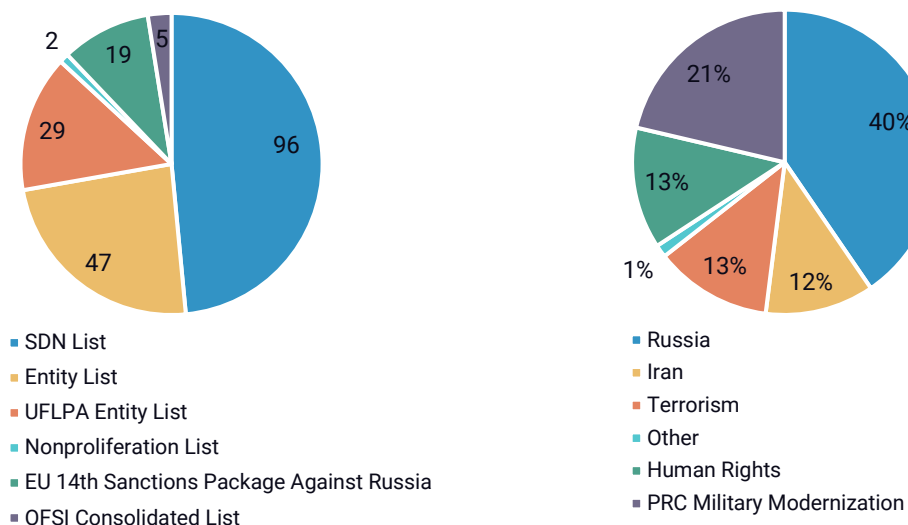


Source: Rhodium Group MPER China. *MPER China tracks more than 50 sanctions and red-flag programs by major market economy governments and international organizations, see the full list [here](#).

FIGURE 3

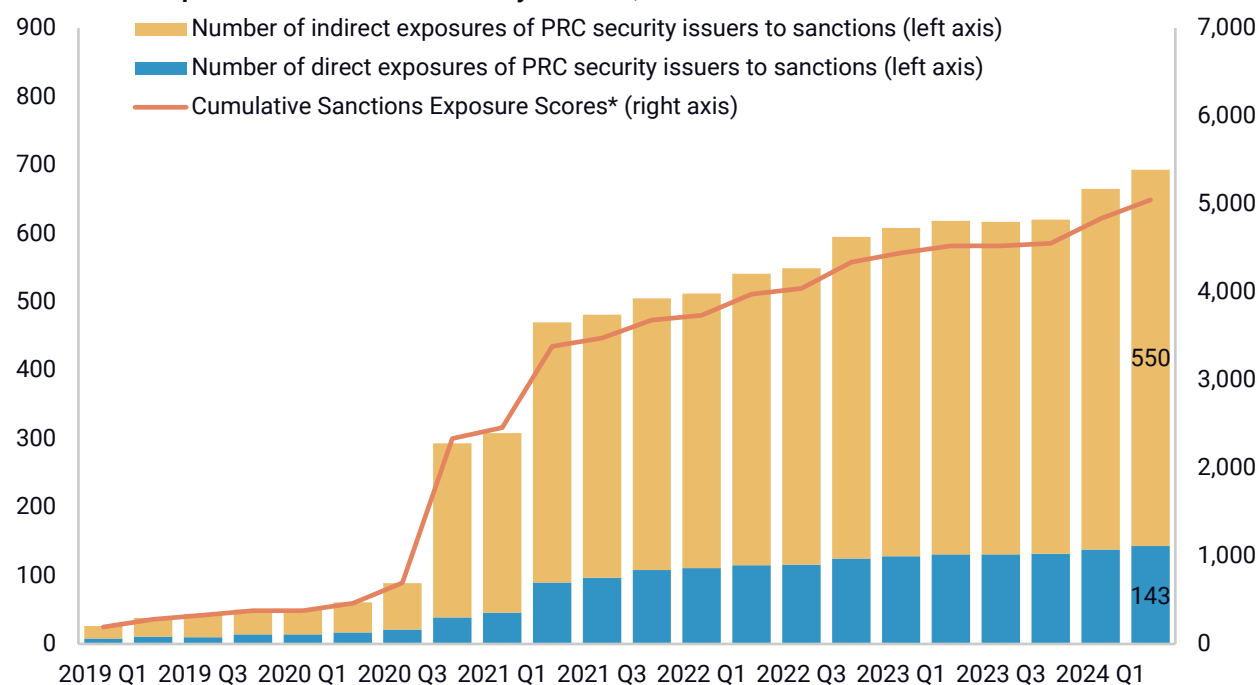
Breakdown of newly added entities to major sanctions list, Q2 2024

Breakdown by sanctions lists (left), themes* (right)



Source: Rhodium Group MPER China. *Breakdown by theme based on Rhodium research.

FIGURE 4

Sanctions Exposure of Chinese security issuers, Q1 2019 – Q2 2024

Source: Rhodium Group MPER China. *Sum of all combined Sanctions Exposure Scores for 8,476 PRC securities. For detailed methodology, see mper.rhg.com.

TABLE 1

Changes in Sanctions Exposure Scores, selected issuers, Q2 2024

Issuer	Sanctions	Exposure	Change Type	Old score	Updated score**
Wuhan Tianyu Information Industry Ltd	SDN List	Direct	New Addition	0	10
Beijing BDStar Navigation Co Ltd	Entity List	Direct	New Addition	0	9
Beijing LeiKe Defense Technology Co Ltd	Entity List	Direct	New Addition	0	9
Geovis Technology Co Ltd	Entity List	Direct	New Addition	8	9
Raytron Technology Co Ltd	SDN List	Indirect	New Addition	0	9
Wuhan Guide Infrared Co Ltd	SDN List	Indirect	New Addition	0	9
Henan Shenhua Coal & Power Ltd	UFLPA Entity List	Indirect	New Addition	0	8
Inspur Digital Enterprise Technology Ltd	CMIC List	Indirect	Ownership Change	0	8

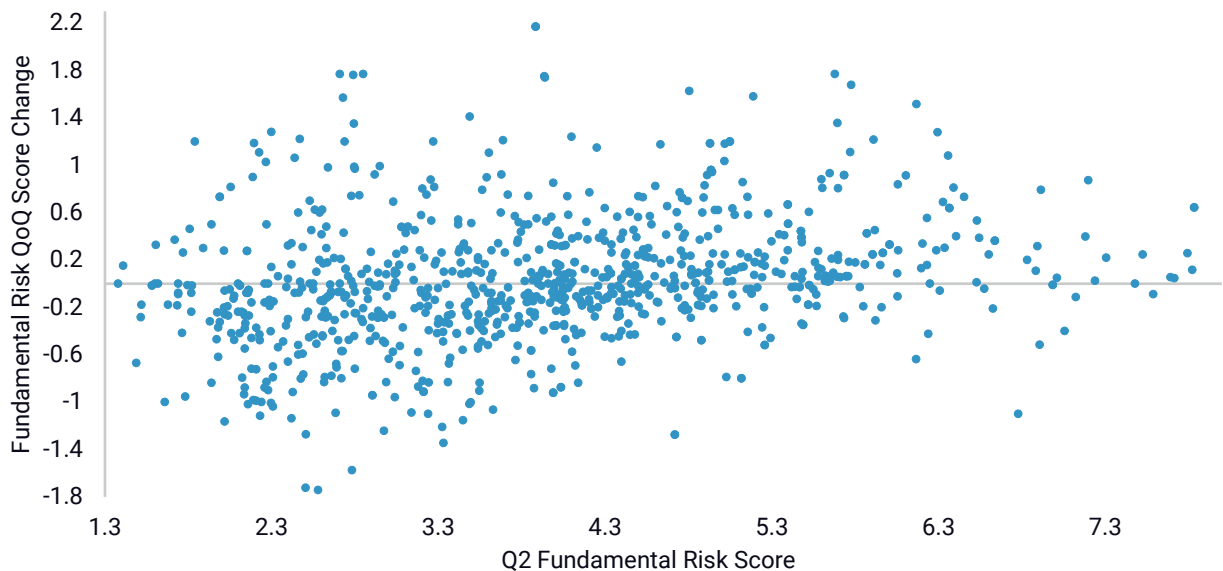
Venustech Group Inc	1260H List	Indirect	Ownership Change	0	8
Shanghai Electric Power Co Ltd	1260H List	Indirect	Ownership Change	5	0

Source: Rhodium Group MPER China. *The complete list of 8,476 PRC securities can be found [here](#). **An issuer’s Sanctions Exposure Score is determined by two primary factors: the severity of the respective sanctions or red-flag list and the proximity of the issuer to the sanctioned or red-flagged legal entity.

Fundamental Risk

A flurry of corporate disclosures and the incorporation of additional data pipelines have led to plenty of movement in our Fundamental Risk Scores, with 396 score increases and 420 decreases. Most of these changes were marginal, but 41 issuers saw a score increase of more than 1 point, and 21 issuers saw a score decrease of more than 1 point (Figure 5).

FIGURE 5
Quarterly Fundamental Risk Score* change, Q2 2024
N=894



Source: Rhodium Group MPER China. *Sanctions Exposure Score excluded.

Table 2 shows an illustrative sample of what caused these more significant changes in Q2. Major score upgrades were related to issuers receiving substantial government subsidies and industrial policy funding, new evidence on executive ties to the military, or moves into the development of dual use technologies. Major downgrades were driven by divesting from state ownership and dropping out of procurement relationships with People’s Liberation Army-affiliated companies.

TABLE 2

Notable changes in quarterly Fundamental Risk Scores, selected issuers, Q2 2024

Issuer	Q2 2024	Q1 2024	QoQ change	Change driver
XPeng Inc	3.89	1.72	2.17	Recipient of Government Grant Transfers
Kingsoft Cloud Holdings Ltd	2.85	1.08	1.77	Trade Barriers
Shandong Weigao Group Medical Polymer Co Ltd	3.94	2.19	1.75	Member of Strategic Industry
China XD Electric Co Ltd	5.78	4.1	1.68	Development of Emerging Dual Use Technology
Universal Scientific Industrial Shanghai Co Ltd	4.81	3.18	1.63	Executive Military Ties
H World Group Ltd	2.73	1.16	1.57	Beneficiary of Discriminatory Public Procurement Practices
Canmax Technologies Co Ltd	2.58	4.33	-1.75	Development of Tools of Oppression
Micro-Tech Nanjing Co Ltd	3.33	4.68	-1.35	Percentage of State Ownership
CITIC Securities Co Ltd	4.72	6	-1.28	Military Procurement Participation
Tianqi Lithium Corp	3.32	4.54	-1.22	Implication in International Litigations

Source: Rhodium Group MPER China. Selected issuers only. Access the full list through [the data portal](#). *QoQ change is based on the difference between Q1 2024 and Q2 2024 scores. **Sanction Exposure score excluded.

Controversy Exposure

As of Q2 2024, we have further streamlined our Controversy Exposure data to flag the direct exposure of Chinese security issuers we cover to the most prominent China Controversies. We define the most important China-related Controversies and then track the mentioning of issuers in connection with these Controversies in a subset of authoritative news sources. We flag issuers implicated in major risk events and provide a Controversy Exposure Score, which measures the severity of legal and reputational risk (e.g., the potential addition to a sanctions list is more severe than the risk of trade barriers) and the issuer's proximity to the specific risk (e.g., whether the issuer itself or its shareholders/subsidiaries are involved).

In Q2 2024, we counted 86 mentions of security issuers in connection with major China Controversies in the sources we track, implicating a total of 53 individual security issuers. The Controversy Stories with the most mentions include Subsidies to Strategic Sectors, Tech Self-Reliance, Support of Iran, and Emerging and Critical Technology (Figure 6).

FIGURE 6
Controversy Stories with most mentions
Q2 2024



Source: Rhodium Group MPER China.

Table 3 provides an overview of the most important Controversy Stories and examples for implicated issuers. At the issuer level, US lawmakers’ request for the Treasury Department to investigate certain Chinese companies for their involvement in **Support of Iran** has placed several issuers operating in the defense sector at the highest risk level due to potential future sanctions. Chinese EV battery makers CATL and Gotion are also at severe risk as US lawmakers expressed concerns over their links to **Xinjiang Forced Labor**, posing reputational and potential legal risks if they are listed on the UFLPA Entity List. Several issuers in the automobile industry face high risk due to the EU’s provisional tariffs targeting EV makers that benefitted from **Subsidies to Strategic Sectors**. Additionally, continued US scrutiny of Chinese biotech companies regarding **Data Security and Sovereignty** and **Party Influence in Corporations** has resulted in high-risk levels for WuXi AppTec, GenScript, and Legend Biotech . Detailed information on all the security issuers implicated in major Chinese Controversies can be found on the MPER portal.

TABLE 3
Major Controversy Stories and implicated issuers
Q2 2024; selected issuers only

Controversy Story	Description	Issuer (Ticker)	Risk Level
Support of Iran	The Select Committee on CCP has requested the Treasury Department investigate whether the activities of certain Chinese companies and their subsidiaries in relation to Iran have breached US sanctions or merited new sanctions.	AVIChina Industry & Technology (02357.HK)	Severe
		COSCO Shipping Energy Transportation (600026.SH)	Severe
		CRRC Corporation (601766.SH; 01766.HK)	Severe
Xinjiang Forced Labor	US lawmakers called for CATL and Gotion to be added to the UFLPA Entity List due to their connection with forced labor.	CATL (300750.SZ)	Severe
		Gotion High-Tech (002074.SZ)	Severe

Subsidies to Strategic Sectors	The EU announced provisional additional tariffs of up to 38 percent on imports of electric vehicles from China. Individual duties would be applied to BYD, Geely, and SAIC.	BYD (002594.SZ; 01211.HK)	High
		Geely Automobile (00175.HK)	High
		SAIC Motor (600104.SH)	High
Data Security and Sovereignty	US intelligence officials told senators working on a BIOSECURE bill that WuXi AppTec had transferred US intellectual property to Beijing without consent.	Wuxi AppTec (603259.SH; 02359.HK)	High
Party Influence in Corporations	The Select Committee on CCP requested information from the FBI and the Office of the Director of National Intelligence regarding GenScript and its subsidiaries' ties to the CCP.	Genscript Biotech Corporation (01548.HK)	High
		Legend Biotech Corp (LEGN.O)	High

Source: Rhodium Group MPER China.

Policy outlook

Concerns about negative economic spillovers from China's subsidies and industrial policy have intensified and seem likely to remain a sticking point. The EU has imposed provisional tariffs on Chinese EVs. Other nations, including both [developed](#) and [emerging](#) markets, are considering similar trade measures on exports from China across a wide range of sectors including clean tech, metals and mining, and consumer goods.

The House Select Committee on the CCP has been pushing for more China-related legislation and proposals. Notably, the recently proposed [PAID Act](#) requests the Commerce Department to identify and report on Chinese entities infringing on US IP. Following an announcement to renew the Committee, House Speaker Mike Johnson also said the House would consider several Select Committee-championed efforts this fall, including [outbound investment restrictions](#), the [BIOSECURE Act](#), and [de minimis](#) reform.

At their June meetings, G7 leaders [threatened](#) more sanctions on Chinese entities, including financial institutions. Smaller Chinese banks doing business with Russia [may](#) be targeted first. We could also see additional Chinese entities added to the UFLPA Entity List, as DHS seeks to scrutinize [more](#) business sectors and lawmakers push to include Chinese EV battery manufacturers like CATL and Gotion. New additions of Chinese biotech companies to the 1260H List are also possible, as [stipulated](#) by the NDAA for FY 2024.

In June, the Treasury Department [issued](#) its long-awaited proposed regulations to implement the outbound investment EO announced last year. Largely within expectations, the proposed regulations do not cover US investments in publicly traded securities. However, an [outbound investment bill](#) covering such transactions, while excluded from the House version of the NDAA for FY 2025, could still be included in the Senate version or brought to a vote in other legislative packages. Additionally, some lawmakers are pushing to expand the scope of outbound investment regulations to include passive portfolio investment. This could lead to new Chinese entity additions to the NS-CMIC List, prohibiting US persons from trading in publicly traded securities in these entities.

ABOUT RHODIUM GROUP

Rhodium Group is an independent research provider with deep expertise in policy and economic analysis. We help decision-makers in both the public and private sectors navigate global challenges through objective, original, and data-driven research and insights. Our key areas of expertise are China's economy and policy dynamics, and global climate change and energy systems. More information is available at www.rhg.com.

DISCLOSURES

This material was produced by Rhodium Group LLC solely for the recipient. No part of the content may be copied, photocopied or duplicated in any form by any means without the prior written consent of Rhodium Group. Redistribution, forwarding, translation, or republication of this material in any form by you to anyone else is prohibited. Rhodium Group LLC is not an investment advisor. Any information contained herein is not intended to be relied on as investment advice and this information is not purported to be tailored advice to the individual needs, objectives or financial situation of a recipient of this information. This report is intended for informational purposes only and does not constitute a recommendation, or an offer, to buy or sell any securities or related financial instruments. The information contained herein accurately reflects the opinion of Rhodium Group at the time the report was released. The opinions of Rhodium Group are subject to change at any time without notice and without obligation of notification. Rhodium Group does not receive any compensation from companies that may be mentioned in this report. No warranty is made as to the accuracy of the information contained herein.

© 2024 Rhodium Group LLC, 5 Columbus Circle, New York, NY 10019. All rights reserved.

New York | California | Washington, DC | Paris

Website: www.rhg.com

