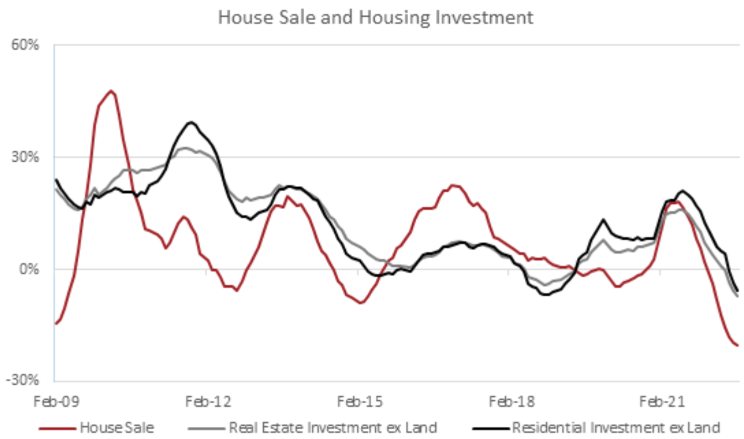
China Bulletin: Market View



China's insistence on sticking to its Dynamic COVID Zero policy, is dampening market participants' hopes that a change of policy may boost growth momentum. The expected change of course may marginally improve personal consumption spending, especially on services, however we would argue the move will do more harm than good to the economy, at least in the short term. This is due to the initial shock and possible further disruption to the manufacturing process. Although it is widely believed that halting the flow of people and goods is dragging growth, we support the idea that the tight housing policy of the last 5 years is finally taking effect in the housing market, and economic pain starting to emerge. House sales have fallen to a two-decade low, and the outlook is even more bleak as property developers line up to default. Since the real estate and construction sectors comprise 15% of GDP, the pain will be either acute, sustained, or both. We share some optimism that the drag from the housing sector may abate from 23Q1, while we remain positive on growth in 2023.

Recent data still exhibits signs of early recovery. Household deposits and corporate long-term loans are both growing strongly. However, growth of household long-term loans continues to slow, echoing the housing market downturn. Fixed asset investment in manufacturing and infrastructure are both growing robustly. The former may still be tested by slowing external demand, while the latter may continue its momentum. Confidence, however, is yet to recover in the service sector, due to interruption from the covid breakout and containment policy. Though the policy is here to stay, it is very likely to be implemented in a more coordinated and efficient way going forward, which could alleviate the uncertainty facing the service sector.

China's equity market has bounced back substantially from the trough after the National Day holiday. Its extremely attractive valuations and the much healthier status of the economy add to an optimistic view on China equities. We would recommend overweighting solidly growing sectors with reasonable valuations, most notably the healthcare sector, and to a lesser extent, new energy supply chain names.

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