Kishore Muktinutalapati
Head - Investment Strategy
Tel: +971 (0)2 696 2358
kishore.muktinutalapati@adcb.com

Prerana Seth
Fixed Income Strategist
Tel: +971 (0)2 696 2878
prerana.seth@adcb.com

Mohammed Al Hemeiri
Senior Analyst
Tel: +971 (0)2 696 2236
mohammed.alhemeiri@adcb.com

Ahmed Al Falahi
Analyst
Tel: +971 (0)2 497 3934
ahmed.a5@adcb.com

Nura Al Suwaidi
Analyst
Tel: +971 (0)2 497 9520
Nura.Alsuwaidi@adcb.com

Visit Investment Strategy Webpage to read our other reports

Bottom line: recent rally in China onshore equities attracted investors' attention; for this rally to continue, policy support is needed; for the real estate sector "no news is good news."

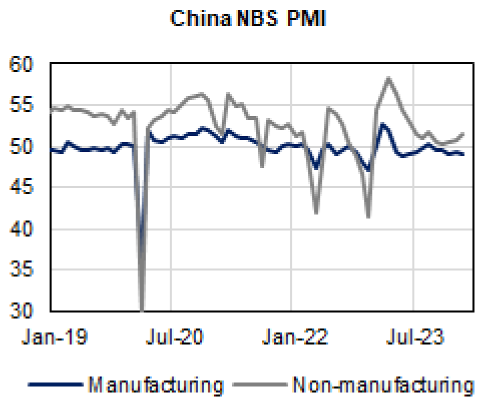
- **We expect China to deliver GDP growth of 5% during 2024 helped by strong consumption and stable property sector which are in turn helped by ongoing policy stimulus.**
- **China is likely to emerge out of its consumer sector deflation in the next few months as more volatile food prices stop being a drag (February data already points to this).**
- **The recent strength in China onshore equities could continue as long as the policy remains supportive. Valuations are cheap, positioning is light, and liquidity is returning.**
- **We prefer three themes: new economy (semiconductors, AI, and robotics), deglobalization (defense, cybersecurity, and food security), and strong consumer (discretionary, and digital).**

- **Macro**
  - ***Growth:*** During 2024, we expect China to deliver GDP growth of close to 5% in line with market expectations. However, one needs to keep in mind that a nominal GDP growth of 5% is still one of the highest across developed markets. China – which is as big as the US – growing at 5% still adds phenomenal output to the global GDP.
  - ***Property sector:*** We think property sector will gradually stop being the headwind for China's macro through the next 12 months. Policy support, which is very targeted, is likely to prevent property sector issues from spilling over into the rest of the economy. To that effect, we believe that no news (from the property sector) is good news (for the economy).
  - ***Consumption:*** We expect China's consumption growth to outpace the headline GDP growth during 2024. Helped by stabilization in the housing market, and social welfare programs by the government, China's consumption sector is likely to pick up. A portion of the total household deposits which were estimated to be USD18.41trn as at end-2023 (and equivalent to more than 30 months of retail sales) could find their way into the real economy through consumer spending.
  - ***Inflation:*** China has been grappling with deflation in both its corporate and consumer sectors. However, we believe that consumer inflation is likely to turn positive in the next couple of months as some of the drag associated with more volatile food prices abates. Perhaps this is beginning to play out already. China CPI for the month of February 2024 rose 0.7% y-o-y versus expectations for a rise of 0.3% y-o-y.
  - ***Fiscal policy:*** While we do not expect a blanket-style stimulus from Chinese authorities over the next 12 months, we do expect them to deliver more targeted measures aimed at reviving sentiment in real estate and consumer sectors. The focus on new age economic sectors like semiconductors, AI, and robotics is likely to pick up pace.
  - ***Monetary policy:*** PBoC has eased substantially over recent months with cuts to Reserve Requirement Ratio (RRR) and Loan Prime Rates (LPR). Especially the recent cut to five-year loan prime rate which was the largest on record was aimed at stabilizing the property sector. However, China regulators also face dilemma in terms of any cuts to its short-term

interest rates is likely to cause weakness in the currency. Therefore, we expect Chinese regulators to continue delivering targeted easing even on the monetary policy front.

- ***Geo-political risks:*** The ongoing competition between the US and China on a range of matters is likely to continue. However, we think – very counterintuitively – a potential trump administration in the US is likely to be relatively less hawkish on China. For more discussion on US-China engagement model and our thoughts please listen to our podcast 4Cs of US-China relationship.
- ***China NPC 2024:*** Recent China's National People's Congress unveiled the country's targets for this year. GDP growth target was set at around 5% like last year but the growth is expected to be achieved against a higher base. The growth is expected to be funded by 3% fiscal budget, RMB1trn of long-dated bonds, and RMB3.9trn of special local government bonds.

China's business activity is set to pick up



Source: National Bureau of Statistics of China, LSEG Workspace, and ADCB Asset Management

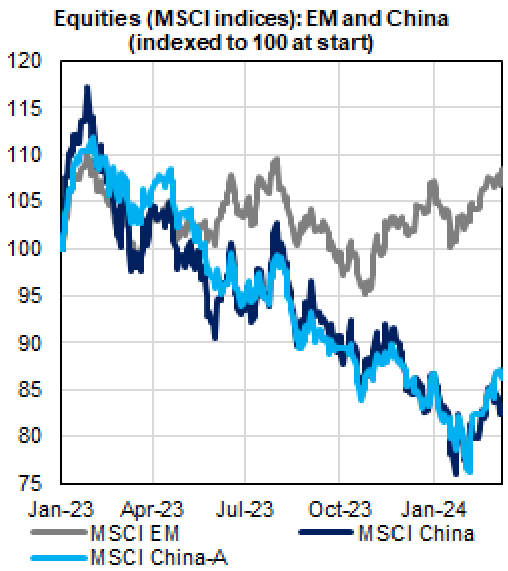
China's consumer is expected to exit deflatio

Source: National Bureau of Statistics of China, Workspace, and ADCB Asset Management

- **Equity markets**
  - ***Recent rally:*** after having fallen for three consecutive years China A shares have started 2024 on a weaker footing. However, since mid-February the onshore China market bounced back strongly attracting some interest. This was after a range of announcements including the appointment of a new chairperson of the CSRC, and introduction of a range of capital market stabilization policies which we discuss below. While both onshore and offshore market indices have moved in lockstep since the start of the year the more recent period has seen a divergence with China A shares outperforming the more mainstream indices.
  - ***Policy support:*** In recent months regulators have attempted to support equity markets directly. From quant trading restrictions to SOEs buying local listed shares to restricting some local mutual funds from selling shares, all measures have been aimed at stabilizing the equity markets. Taking the next step, with an aim to build an investor-oriented capital market, market cap has been included as the KPI for SOEs' Senior management.
  - ***Liquidity:*** Increasing share buybacks and strong flows into ETF bode well for market liquidity. Further the cuts in RRR are likely to inject more liquidity which is long-term in nature. Also, interest rate cuts are likely to help too.

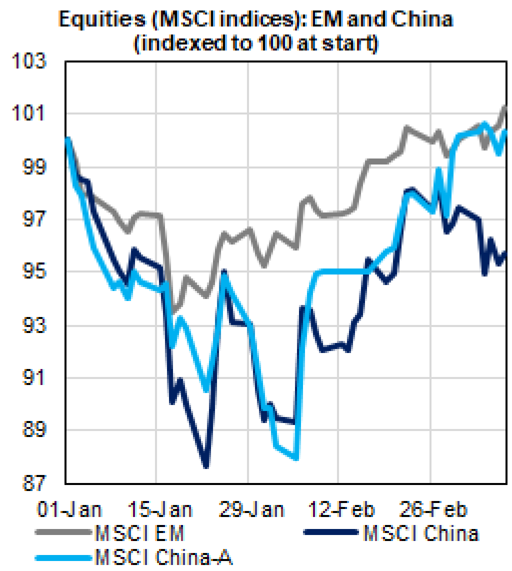
- ***Valuations:*** Valuations for Chinese equities remain cheap. For the context MSI China index trades on c9x the 12-month forward EPS compared to MSCI US index which is trading on c21x 12-month forward EPS.
- ***Positioning:*** Total flows into Chinese equities has been very weak given the significant outflows recorded over the past several months. As per the data from EPFR, average global emerging market equity fund is sizably underweight China.

China equities underperformed EM since 2023



Source: MSCI, LSEG Workspace, and ADCB Asset Management

…but China onshore equities performed s YTD



Source: MSCI, LSEG Workspace, and ADCB Asset Man

- Overall, with stable to improving macro, policy support, cheaper valuations, and light positioning, Chinese equity markets can continue to deliver positive returns over the remainder of the year.
  - We prefer China onshore markets to offshore markets at this stage. Admittedly the offshore markets continue to trade on much cheaper valuations. This would make the offshore markets more attractive at a later point, but for now we focus on onshore markets.
  - We look at the Chinese equity market through thematic lens.
    - Given the regulatory support, and significant potential, we believe the new economy sectors are likely to benefit. Here, we would focus on domestic semiconductors, artificial intelligence, robotics, and digital consumer segments.
    - Given the ongoing standoff between China and US we expect security issues to resurface. In which case, defense, food security, and cybersecurity sectors are likely to do well.
    - Also given that Chinese consumer is likely to outpace the overall economy, we would play the resilient consumption via China hotels restaurants and leisure, and digital consumption as a theme.

Disclaimer

ADCB Asset Management Limited ("AAML"), is a member of ADCB Group, licensed by Financial Services Regulatory Authority in Abu Dhabi Global Markets under financial services permission number 170036.

This publication is intended for general information purposes only. It should not be construed as an offer, recommendation or solicitation to purchase or dispose of any securities or to enter in any transaction or adopt any hedging, trading or investment strategy. Neither this publication nor anything contained herein shall form the basis of any contract or commitment whatsoever. Distribution of this publication does not oblige ADCB Group to enter into any transaction.

The content of this publication should not be considered as legal, regulatory, credit, tax or accounting advice. Anyone proposing to rely on or use the information contained in the publication should independently verify and check the accuracy, completeness, reliability and suitability of the information and should obtain independent and specific advice from appropriate professionals or experts regarding information contained in this publication. Investment products are not available to US persons.

Information and opinions contained herein is are based on various sources, including but not limited to public information, annual reports and statistical data that AAML considers accurate and reliable. However, AAML makes no representation or warranty as to the accuracy or completeness of any statement made in or in connection with this publication and accepts no responsibility whatsoever for any loss or damage caused by any act or omission taken as a result of the information contained in this publication. This publication is intended for customers who are either retail or professional investors.

Charts, graphs and related data or information provided in this publication are intended to serve for illustrative purposes only. The information contained in this publication is prepared as of a particular date and time and will not reflect subsequent changes in the market or changes in any other factors relevant to their determination. All statements as to future matters are not guaranteed to be accurate. AAML expressly disclaims any obligation to update or revise any forward looking statement to reflect new information, events or circumstances after the date of this publication or to reflect the occurrence of unanticipated events.

ADCB Group does and may at any time solicit or provide commercial banking, investment banking, credit, advisory or other services to the companies covered in its publications. As a result, recipients of this publication should be aware that any or all of foregoing services may at time give rise to a conflict of interest that could affect the objectivity of this publication. Opinions expressed herein may differ from opinions expressed by other businesses or affiliates of ADCB Group.

Past performance does not guarantee future results. Investment products are not bank deposits and are not guaranteed by ADCB Group. They are subject to investment risk, including possible of loss of principal amount invested. This publication may not be reproduced or circulated without ADCB Group written authority. The manner of circulation and distribution may be restricted by law or regulation in certain jurisdictions. Persons who come into possession of this document are required to inform themselves of, and to observe such restrictions. Any unauthorized use, duplication, or disclosure of this document is prohibited by law and may result in prosecution.