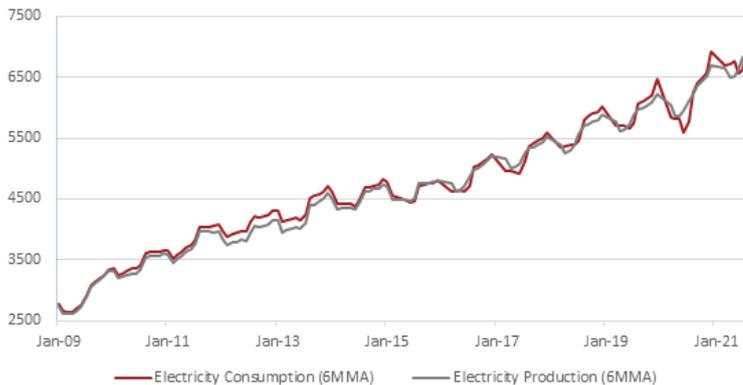


China Bulletin: Market View

Electricity production vs consumption



The unexpected default of an onshore property developer on its offshore debt coupled with the turmoil during the national day holiday, jolted the China offshore bond market. This came just after concerns about China's real estate sector had marginally eased. The continuous tightening of housing policy starts to bite, especially those expanding too fast on too bold borrowing. Though it is still possible that policy makers will ease the grip on the housing market slightly to avoid the contagion and collapse of the entire sector. We will keep a close eye on any such movements.

It seems the shortage of energy is becoming a global phenomenon and in China it appears as a tight balance of power. Since the large-scale update of the electrical grid and construction of power plants in the early 2000s, blackouts have been very scarce in recent decades, yet they are emerging again due to strong demand and sluggish supply.

Traditionally southern China is equipped to produce hydropower however 2021 saw droughts in the region creating a shortage of supply. To make things worse, thermal power supply is hit by skyrocketing coal prices, stemming from the effective supply-side-reform aiming to reduce the excess capacity in coal mining. The shortage in China and across the globe may make this winter terribly cold, but we will keep watching to see if it could lead to a period of persistent inflation.

The equity market shows another picture, reversing the previous trend that energy names prevail. On the contrary, it is large caps and the healthcare sector that outperform the market, just like the old normal before the Chinese New Year. To us it means an overall bull market is not in sight and investors must seek structural opportunities. Before we can safely say the shortage is merely temporary, we suggest certain weight should be placed on energy names, both old and new. In addition, financials, dragged by the upheaval in the real estate sector, are below their fair value in our view, thus worth watching as well.

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