China Bulletin: Market View

In the last fortnight we can see several Chinese cities loosening their grip on the housing market, especially on the demand side, but the bleak housing market may need more in order to recover. Measures announced so far, including lowering the payment ratio and mortgage spread over the benchmark rate, may not be enough to reverse the overly pessimistic outlook. The current loosening is taking place in some top tier cities as well as lower tier cities. The market is still expecting some top-down changes of policy tone as policy makers try to strike a delicate balance between suppressing the overpricing of houses and restoring confidence in the housing market. It is an incredibly difficult task, and the window to watch should lie between now and mid-2022. The housing market remains the Chinese economy's most significant swing factor in 2022.

Though an official fiscal deficit is yet to be announced, various anecdotal evidence points to a less active fiscal policy, and it raises the risk of overreaction in later months.

The perceived fiscal support is certainly weaker than the market expects, and probably weaker than the rhetoric of the Central Economic Work Conference as well. Policy differences between ministries are common, yet the divergence from the conference is unusual due to the fact that the conference is a higher policy coordinating body. One explanation that seems reasonable to us is that fiscal policy makers believe growth is running within their target band. The NPC session scheduled to commence on March 5th will be important. If growth continues to slide as the market is pricing, fiscal policy may have to steer to a more active stance to reverse the outlook. Again, H1 2022 is the key window, making March critically important in the sense of announcing a growth target and policy combination, as well as publishing economic data for the first two months of this year.

Due to the sudden rise of geopolitical tension, we foresee a jolt in the Chinese equity market that will send volatility higher. An additional driver of increased volatility is the split between the statement and the action of policy, as well as the necessity to restore confidence in the housing market on the one hand, and the policy target to suppress its price surge on the other hand. Reinforcing volatility further is the stretched valuation of sectors deemed promising by institutional investors, with increasingly converging preference. We would suggest a low volatility portfolio and prefer a value style over growth, represented by the Shanghai Shenzhen 300 Index and CSI 500 Index respectively.

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