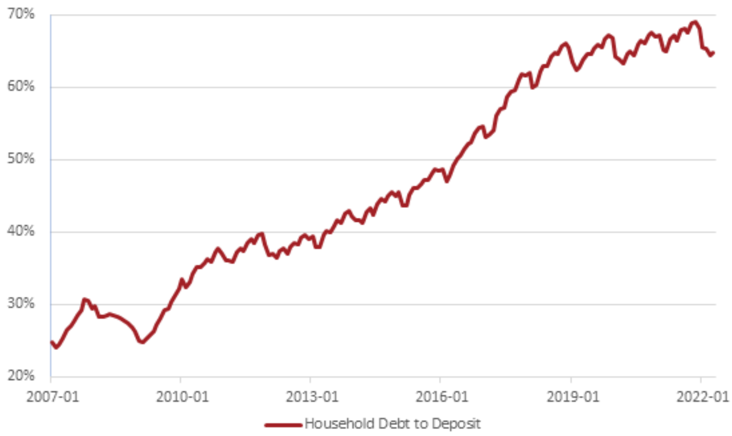
China Bulletin: Market View



The surprising reduction of the 5-year loan prime rate (LPR) by 15 bps, and the extraordinary premier hosted national video conference on stabilizing growth, came in response to the increasing concern about the economic cost of sticking with the current Covid containment policy. Focusing on the tier 1 cities, one could easily conclude that the cost is too huge to bear. Additionally, the disruption to logistics has materially impacted industrial production in the last two months, and consequently is dragging on exports. However, we must remember that less than 10% of the population lives in tier 1 cities, and the disruption to logistics has been escalated to one of the top priorities for the Ministry of Transportation. We are more optimistic about growth in June. We reiterate our view that once the outbreak is under control, the continued disruption and lockdown will be removed soon after, leading to a resumption of the economy's normal trajectory.

The housing market is coming under the spotlight again after the unprecedented 15 bp cut to the 5-year LPR, and the reduced minimum mortgage rate. The 5-year LPR is the benchmark rate for loans longer than 5 years, including long-term corporate loans and mortgages. The move is accommodative but still marginal, and policy makers are drawing a line about loosening the housing market's grip. The recent revoking of loosened policy in some tier 2 cities, and the absence of the Ministry of Housing in the national video conference, shows that high housing prices remain unacceptable to policy makers. This is further evidenced by the pressure of weak employment growth, fragile business confidence and the looming housing market collapse. Although, as long as the household sector remains relatively healthy, an economic downturn may only be temporary and cyclical.

US-China relations are tested again after President Biden's statement about Taiwan, and China will conduct an air patrol shortly. Unity and sovereignty is the foremost concern for China, and the latest speech by US Secretary of State Antony Blinken downplayed the tension. Political headlines may cast more significant influence on financial markets going forward. But if growth momentum picks up, we will remain positive on China's equity market. In the short-term we recommend a low volatility strategy when investing in Chinese equity.

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