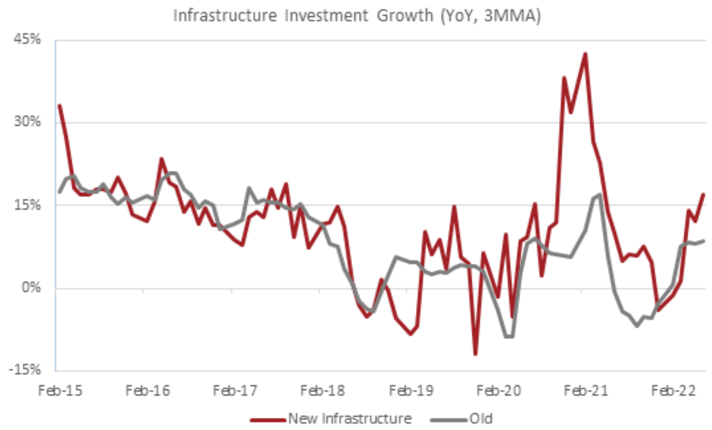
China Bulletin: Market View



The lack of large-scale stimulus from China's politburo meeting at the end of July, and the unexpected disappointing PMI data, has ignited a new round of pessimism in the onshore equity market. Alongside the existing geopolitical risk, bumpy equity market and falling bond yields, it raises more questions about the health of the economy. The housing sector remains a drag on the economy, while the fiscal side is stepping up spending on infrastructure investment, with that momentum expected to continue. Export levels, which are seeing headwinds from possible slowing global demand, and tailwinds from improved competitivity due to robust supply chains and a weaker CNY, may be neither a drag nor a boost to growth. After years of supply-side structural reform, capacity utilisation has stabilised at a healthy level, and manufacturing fixed asset investment is more resilient in the face of a slowdown, adding to the stability of growth momentum.

In the housing sector, under the spotlight since late 2021, sentiment remains negative. The current upheaval in the housing and mortgage markets is inevitable in defusing the thorny bomb that is the swollen real estate sector, and the resulting elevated debt burden. We believe the setback will be temporary, but that many property developers will fall as a result. Once the housing sector has suffered through the pain, we expect China's economy to benefit from a healthier household sector. We suggest keeping a close eye on household debt development, to see if China can achieve a controllable adjustment of the housing sector without further raising household debt.

The again heightened geopolitical risk across the Taiwan Strait has moved the market but has waned quickly. Although the perceived provocation is rare, the diplomatic rhetoric has been harsh. While the scale of military drills has been unprecedented, the status quo across the Taiwan Strait has not changed meaningfully. The tension between China and the US has become a routine part of US elections in recent years, but political standoff is less detrimental to financial markets than trade disputes. On the other hand, in a retrospective way, the geopolitical-event-hit trough of China's equity market is always a good entry point. Combined with the current reasonable valuation levels and with the pessimistic outlook already priced in, we would suggest a more active stance on China's equity market.

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