China's early start on the road to recovery

March 2021

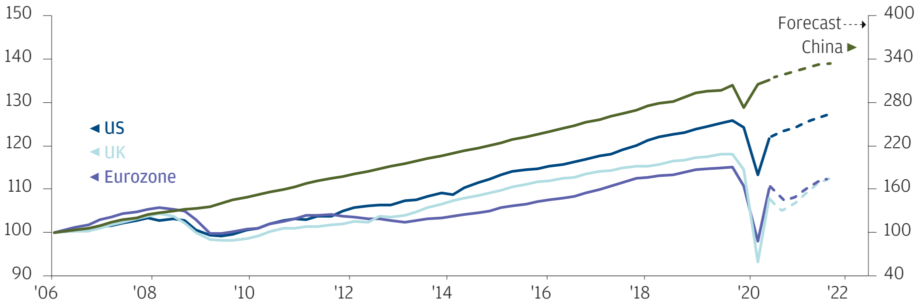
China is among the earliest economies to shake off the effects of the severe economic and social disruption caused by the global public health crisis. As the nation continues along its road to recovery, we believe a consolidating economy and a cautious central bank have made Chinese assets relatively attractive.

Year of the Ox

China - the first country hit by the pandemic – is also among the first to come out the other side. And, compared to its global peers, it has emerged relatively unscathed. Indeed, China was one of the few economies to actually grow in 2020: GDP in the final quarter was up 6.5%[1], with the economy growing 2.3% over 2020 as a whole, versus a global contraction of 3.5%.[2]

Most mobility restrictions have now been lifted, and mobile phone 'health codes' are being used to mitigate the risk of new waves of infection. With recent data releases also showing industrial output in the country expanding in the last three quarters of 2020 – bolstered by the manufacturing sector and steady exports[3] – it certainly looks like a positive start to the Year of the Ox.

EXHIBIT 1: REAL GDP GROWTH
INDEX LEVEL, REBASED TO 100 AT 1Q 2006



Source: BEA, Bloomberg, Eurostat, National Bureau of Statistics of China, ONS, J.P. Morgan Asset Management. Forecasts are from Bloomber contributor composite. Past performance is not a reliable indicator of current and future results. Guide to the Markets - Europe. Data as of 31 December 2020.

[1] Thomas Hale, 'China's economy expands at faster rate than before coronavirus' (Financial Times, 18 January 2021)

[2] International Monetary Fund, 'World Economic Outlook Update' (January 2021)

[3] https://www.reuters.com/article/us-china-economy-activity-idUSKBN29N042

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Bulls in China

The Chinese government has taken a different approach from developed market governments in terms of fiscal stimulus, relying mainly on infrastructure investment instead of cash handouts to help stabilise its economy. Investment, particularly state-led infrastructure projects, has been the major contributor to the recovery since April. The consumption and services sectors are also picking up, strengthening the economic resurgence in the second half of 2020.

The recovery allows the People's Bank of China (PBOC) to carry out a balanced monetary policy, focusing on targeted support to the real economy. Since the PBOC has avoided large-scale liquidity injections and asset purchases, the renminbi has remained strong against the US dollar – hitting a 30-month high in January this year.[4]

With the US dollar forecast to weaken in the medium term, the PBOC should have more flexibility in allowing the renminbi to appreciate. While this may seem to undermine China's export competitiveness, a stronger RMB would also imply cheaper imports of consumer goods, raw materials and manufacturing components.

Moreover, China is looking to attract more international capital into its financial markets, so a modest appreciation could enhance the appeal of Chinese assets.

The real economy

Support to the real economy – particularly SMEs and the technology sector – remains the top priority for the PBOC.

China's cyclical upswing could add to a broad range of structural growth factors that would favour companies in the new economy. If anything, the public health crisis has accelerated technology adoption in finance, education, healthcare and other areas within the services sector. Beijing has committed USD 1.4 trillion of investment to accelerate digital growth infrastructure in its bid to become a global tech leader, reducing reliance on foreign names while strengthening local ones.

Five years forward

Chinese policymakers are focusing on long-term potential, with an emphasis on the quality (rather than quantity) of economic growth. In China's 14th five-year plan, domestic consumption and technological innovation are the focal points.

Domestic leaders in the consumer services and technology sectors – sectors that are key components of China's stock markets – could become the major beneficiaries of these new policies, creating a wealth of growth opportunities for investors.

[4] Hudson Lockett, 'China's currency heads into Biden era on front foot' (Financial Times, 22 January 2021)

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