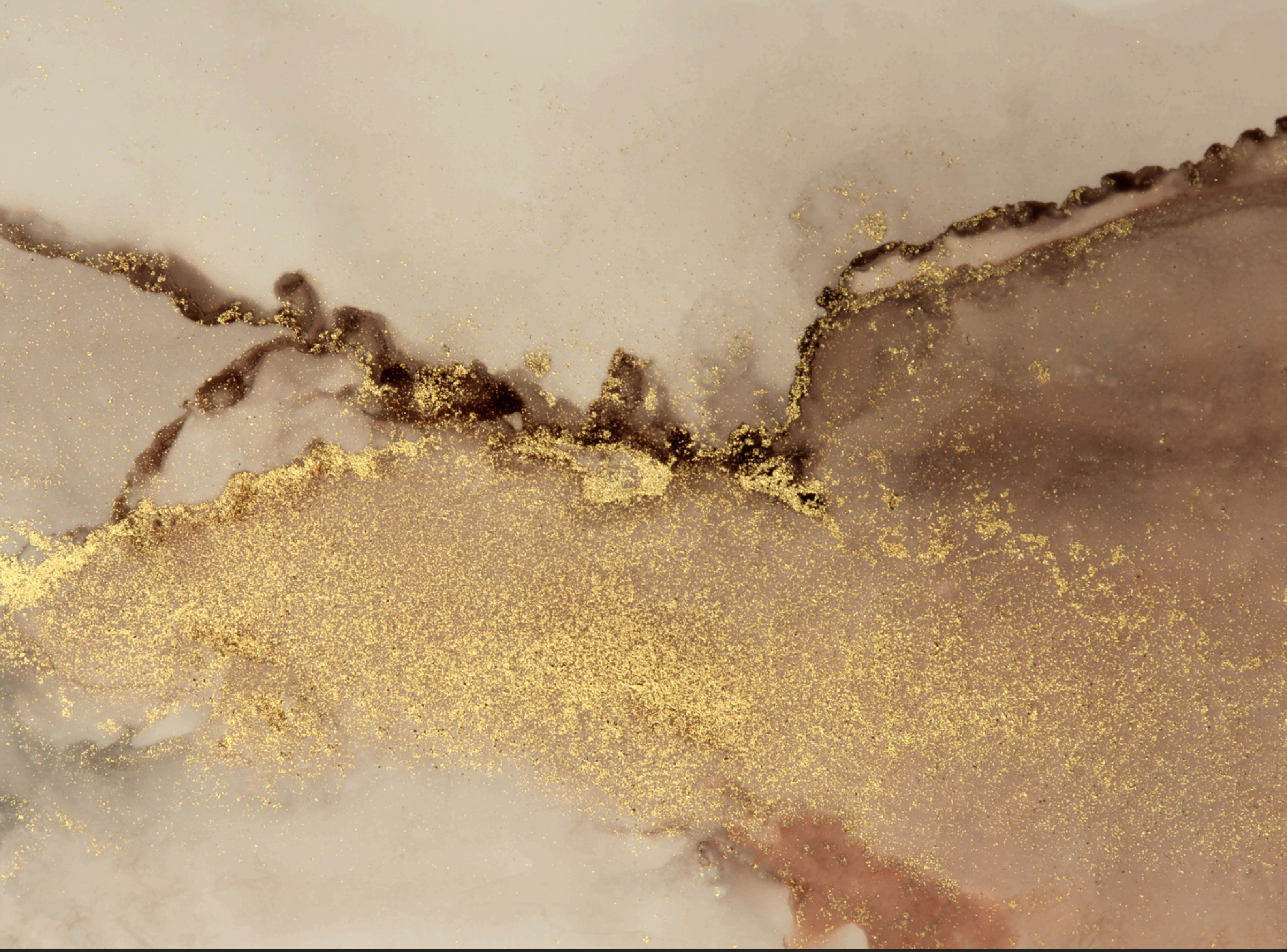


UNIO

Chinese Revival

Unio Global Macro Committee Outlook

March 2025

China's Refocus

Before Donald Trump began his second term as president of the US, the expectation was that he and his administration would focus their early policy moves on China, a strategic issue that unites many of the cabinet, notably Marco Rubio is a China-sceptic.

That the focus of the administration has been on destroying relationships with allies in Canada and Europe has been a surprise, as has the reaction of the German government in reforming the debt brake and the broader urgency of the EU on defence. European markets have also surprised in terms of the re-rating of equities and the de-rating of bonds.

The noise created by the Trump administration vis à vis Europe has obscured developments in China. It is driving progress in AI model building, there has been a rapprochement of sorts between the Communist Party and entrepreneurs like Jack Ma and the government continues to enact periodic stimulus packages.

With emerging market equities still cheap relative to those in the US, this month's Global Macro Council has focused on the case for China.

While it is an enormous economy, China appears to be three to four different macro cycles rolled into one.

First, with echoes of Ireland in the 2000's, China – in the face of deteriorating demographics – is struggling with the deflation of the property market, which as a sector has made up close to 20% of GDP, and the fallout from this has dampened local and regional economies and led to a depression in consumer confidence.

Then, the Chinese government has, in the past year, tried to bolster the economy, mostly with liquidity injections. Our sense of these policy moves is that they are more designed to help de-leveraging than they are to improve demand in a traditional Keynesian sense.

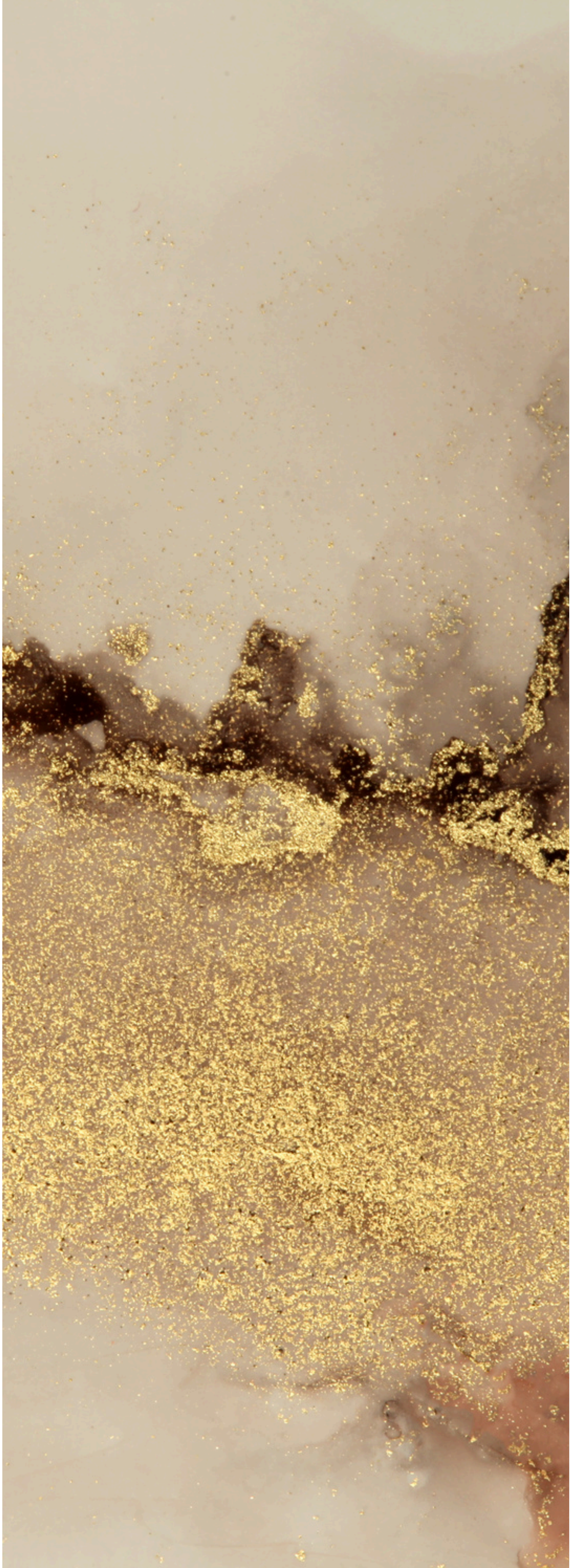
Six Little Dragons

Policymakers seem torn between the risks of re-igniting the property bubble and allowing this to deflate in an orderly manner. In that context, we don't expect a meaningful pick up in growth and inflation (end of deflation). To a large extent, this is already reflected in Chinese bond yields, which are now lower than those in Japan!

Yet, the rally in Chinese equities in the past two months has been catalysed by the publication of AI model results from the DeepSeek AI project, which in turn has focused attention on the efforts of firms like Alibaba in the AI field.

A policy boost came in the form of the 'Six Dragons' meeting on the 17th February in Hangzhou where Xi Jinping met the heads of six technology firms in key sectors – such as AI, ecommerce and robotics.

Politically the meeting is perceived as being significant in the sense that the government ceases to be a headwind to Chinese tech firms, and now acts to support them, and that it has drawn some tech giants like Alibaba in 'from the cold'.



Emphasis on Consumption

In that context policy risk internally has fallen but rises in the sense that the Trump administration's next move may be to further restrict trade with China. Earlier rounds of tariffs on China have led to lower trade between the US and China (China exports close to 13% of goods to the US compared with 22% some eight years ago, according to NinetyOne), and some commentators consider that the growing trade divide between the US and its allies will open up opportunities for China to grow trade with the rest of the world.

In the context of a weaker property market, there are large amounts of capital in banks, and this may at some stage find its way into the equity market if there is an upturn in consumer confidence.

We are struck by the fact that whilst it is an enormous economy, China is only 6% of world equity market cap. There are good reasons for this – geopolitics, lack of transparency and poor governance and so far, a lack of financial market deepening around the equity market.

Perhaps the most compelling factor for equities is valuation and China still trades at a large valuation discount (some 40% to world equities, according to HSBC).

Overall, our view is that Chinese equities are cheap and are enjoying a catalyst from the IT sector. A stronger economy may be needed to further re-rate the market.

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