

China equities

The outlook in 100, 200 and 400 words.

China equities have had a strong start to 2019 and **Bin Shi**, Head of China Equities, and his team give their outlook on what to expect in the rest of 2019 and what sectors to look out for.

In 100 words

We identified a turning point for China's equity markets in Q4 2018 because we believed then, as we do now, that 2019 would be a much better year than 2018.

We based our view on growing policy support from China's government and easing China-US trade tensions, and recent market movements have been consistent with what we have been saying.

The market rebound so far this year has been sharp and we certainly do not expect the same magnitude of return to repeat every month. Markets will likely be volatile, but we maintain a positive outlook for China equities in 2019.

In 200 words

That's partly because we are seeing targeted policy support from the Chinese government.

China's authorities cut the amount of cash banks must hold in reserve, increased liquidity, and channeled credit to smaller companies.

Additionally, fiscal policy has turned supportive, with tax cuts for consumers and businesses, as well as increased spending on infrastructure.

Regulations have eased and key sectors, like auto and financial services, have opened to foreign investors.

Restricted access to these sectors is a point of contention between the US and China, so China's moves are, in our view, conducive to easing trade tensions in the coming months.

In 400 words

Looking specifically at the markets, valuations remain inexpensive and we still see potential long-term investment opportunities.



Three attractive themes include:

- **Premiumization:** As incomes and the number of higher-income households rise in China, consumers are trading up for premium brands. An example of this lies in baijiu (white liquor) in China, where we are seeing strong demand for premium segments.
- **R&D and Innovation:** Chinese companies are raising R&D spending and becoming more innovative. In 2017, China overtook Japan as the 2nd largest source of international patent applications¹ and we see innovations across many sectors, particularly healthcare, IT, e-commerce, and insurance.
- **Education:** China's market for education, and particularly for after-school tutoring, is both large and growing. It is also fragmented, and some of the larger firms in the sector have the opportunity to add market share because they are better resourced than smaller players.

These themes, as well as fundamental trends like urbanization, automation, population ageing, and the rise of the services sector are long-term in nature and we believe that by identifying and investing in leading companies within these trends, we can deliver growth for investors over the long term.

¹ Source: OECD, WIPS, Morgan Stanley Research estimates, as of end-December 2017

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