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# For China, tariff risks loom against tech reprieve

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**The impressive surge in the MXCN, on the back of a lull in tariff tensions and the surprise DeepSeek reveal, seems to have come to a pause, at least. The tech sector positives though look set to continue, as the multi-year regulatory crackdown appears to have ended. The tariff situation will likely hinge on the second round in April, but we expect this to be manageable. For now, we remain Neutral on the MXCN with the internet sector outperforming.**

President Trump's reiteration of tariffs on Canada and Mexico has revived concerns over trade disruptions. The announcement of new restrictions on Chinese investment in US assets and the reiterating of tariffs on Canada and Mexico have triggered a revival of broad tariffs and a slowing of trade activity. This has seen the VIX rise from around 15.6 on Friday to a high of almost 21.5, with the S&P 500 falling almost 1% and the MSCI China (MXCN) falling over 3%. Should investors assume that the 26.5%, six-week surge in the MXCN is at risk of reversing?

While the MXCN's surge and its outperformance over the S&P have been impressive, a sharp reversal is not inevitable, as there are near-term catalysts that could keep the MXCN supported. These include improving core internet sector fundamentals, continued policy support, and reasonable valuations. Indeed, against this backdrop, and the thaw in sentiment, we see further upside potential in the MXCN through the year. But we remain Neutral ahead of the following events that are likely to have a significant impact the MXCN's prospects.

**Regulatory crackdown on internet sector likely over.** Although the revelations about DeepSeek helped spark the ongoing rebound in MXCN, we believe the tech sector's outperformance will be sustained by the apparent end of the multi-year regulatory crackdown. What might have a broader and more immediate impact is the relatively warm tone that

emerged from this month's second private sector symposium. This potentially removes the biggest drag on the sector's overall growth prospects and planned investment, as well as market sentiment on the sector.

While we expect this will help China's internet sector continue to outperform, we await more concrete signals from the next earnings session before taking further portfolio action. For now, we see China's internet sector as Attractive, likely to offer around 15% upside from current levels to our December target. We recommend focusing China exposure on select internet names, but rallies beyond our targets should be used to trim and diversify exposure.

**Tariff risks still loom large.** The fairly contained nature of the first round of tariff exchanges between the US and China seems to have avoided the escalation that some had feared. We estimate the impact will likely be manageable at around a 0.3-0.4 ppt reduction to China's GDP growth. Crucially, China's response seemed designed to avoid escalation with diplomatic negotiations still ongoing.

While the "America First Investment Policy" placing restrictions on Chinese investments into US assets has spooked markets, the next key step will be a potential a second tariff rate hike by the US, most likely after the US Trade Representative's (USTR) investigation report due in early April. The second round of tariffs could be more targeted, with higher tariffs on capital and intermediate goods versus consumer goods. Overall, we expect another 20 ppt of tariff rate hikes over 2025-2026, which will probably cut China's GDP growth by 0.7-1.0 ppt. This should be manageable, especially if blunted by accommodative policy.

The reaction in the Asia IG space to tariff turbulence has been fairly muted. Most Asia IG issuers in general do not have meaningful revenue exposure to the US, so these trade restrictions are likely to have more bark than bite for the segment. We do not see these tariffs fundamentally altering the credit profiles for IG issuers. In our base case, tariffs might actually support our preference for Asia IG given the segment's relatively stronger ability to withstand the tariff turbulence.

**NPC likely to reaffirm policy support for the economy.** The NPC will start on 5 March and last for about one week. We think that policymakers may continue to aim for "around 5%" GDP growth with the budget deficit lifted to 4% (from 3%). We expect GDP growth to slow down to around the middle of the 4-5% range in 2025 from 5% in 2024.

Accordingly, we expect a mild stimulus package, rather than a bazooka. We expect both fiscal and monetary policy to be made marginally more supportive, at least while the halo effect from benign tariff impact and improved sentiment from DeepSeek is still in place.

Fiscal policy is a key focus, and could be incrementally boosted throughout the year in response to any worsening in the tariff situation. On monetary policy, an easing bias is likely to be maintained, and we expect cuts of 50-100bps in the RRR and 20-40bps in the policy rate in 2025. On the CNY, the PBoC has signaled its determination to keep it relatively stable, ahead of potentially more significant tariffs.

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