INDOSUEZ WEALTH MANAGEMENT

# CIO PERSPECTIVES

30 September 2024

## Introducing XiNomics

**Last week, China unveiled its most substantial stimulus measures since 2015. The triptych package, aimed at reviving growth, is essentially a domestic-oriented stimulus that could bring some "light at the end of the tunnel" for China equity investors, even if selectivity remains key. A welcome "first arrow" from policymakers which now calls for a second "fiscal arrow". This time could be different: pessimists look at this move as "too little and too late", but optimists like ourselves see this bold move as a clear willingness to put a floor on equity valuations, stop the deflation process and restore consumer confidence. We remain positive on emerging markets, China will provide an additional and much needed engine to the asset class, with positive repercussions on the rest of Asia. Investors remain largely absent from this market, the rally could have further legs.**

### The most significant stimulus measures since 2015

A slew of stimulus measures (Table 1) were announced by the People's Bank of China (PBoC), China Securities Regulatory Commission (CSRC) and National Financial Regulatory Administration (NFRA) on 24 September 2024, directed at supporting the housing and stock markets.

**Table 1: Key Measures Announced 24 September**

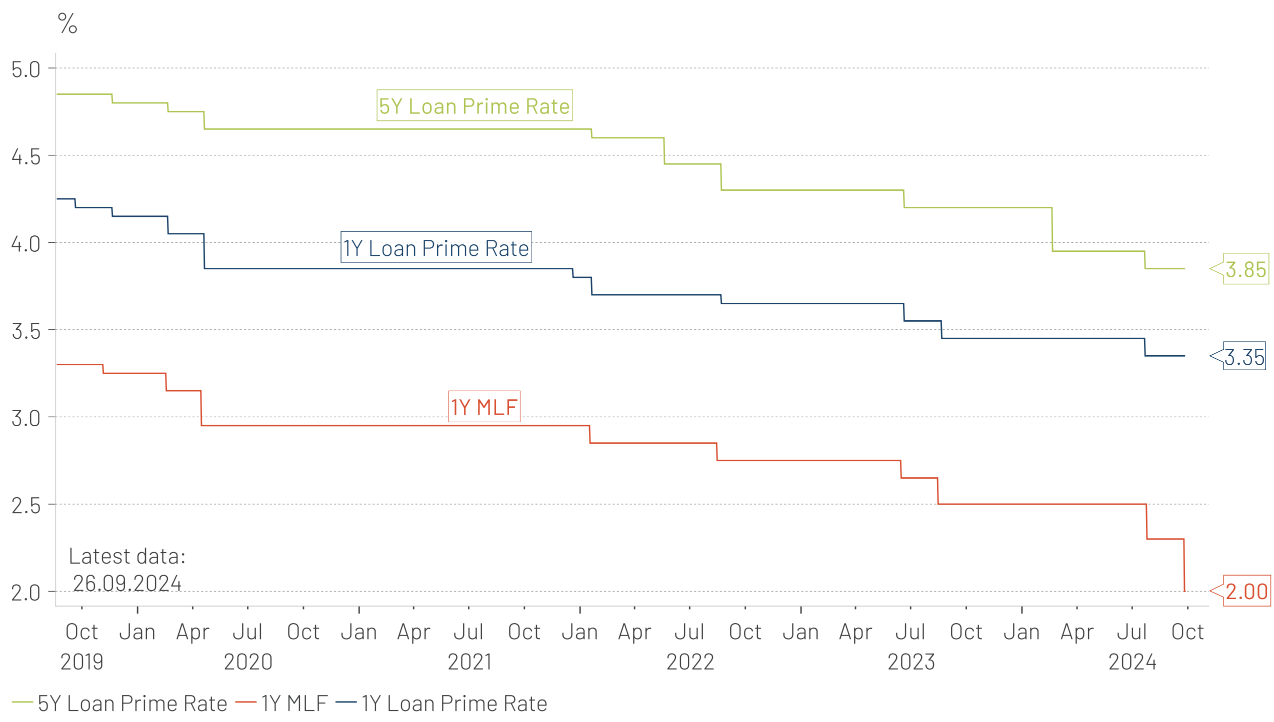
| Monetary Policy | Housing Market | Stock Market |
|---|---|---|
| Broad-based | Targeted | Targeted |
| 7-day reverse repo cut by 20 bps to 1.5% | minimum down-payment ratio for second homes will be lowered to 15% from 25%, now in line with first-home downpayment rules | provide at least CNY 500 billion of liquidity support for stocks, including a swap facility allowing securities firms, funds and insurance companies to tap liquidity from PBoC to buy stocks where they can pledge assets |
| 5Y Loan Prime Rate cut by 25 bps | PBoC's CNY 300 billion re-lending programme announced in May will be ramped up to provide 100% of the principal of bank loans extended to regional state-owned enterprises to buy unsold homes, up from 60% | a separate specialised refinancing facility for listed companies and major shareholders to buy back shares, raise holdings |
| Required Reserve Ratio cut by 50 bps, releasing CNY 1 trillion in long-term liquidity (PboC highlighted that there could be a further cut of 25 bps to 50 bps by end 2024) | PBoC will guide banks to reduce interest rates on existing mortgages to the vicinity of interest rates for newly issued loans. PBoC Governor Pan said the cut in outstanding mortgage rates is expected to reduce household interest expenses by CNY 150 billion | CSRC will be releasing six measures to support M&A soon |
| Boost Core Tier-One capital to six major commercial banks which will likely increase their capacity to expand credit | increase its support to 100% of the affordable-housing loans under the CNY 300 billion programme announced in May, up from 60% originally | |
| Cut rates on CNY 300 billion worth of 1 year medium-term lending facility (MLF) loans to some Financial Institutions to 2%, from 2.3% | | |

### Our take on the latest stimulus package

This synchronised, positive monetary surprise (Chart 1) is aimed at creating a virtuous cycle to arrest the further decline in sentiment among consumers and investors towards asset prices, as **the magnitude and timing of monetary policy easing surpassed our expectations**.

Given the global disinflationary environment and dovish monetary policies, with the Federal Reserve (Fed) being the latest to join in, there is now greater room for PBoC to manoeuvre with even more dovishness, supporting domestic growth without a severe impact on its currency.

### Chart 1: China Key Policy Rates




Source: PBoC, Macrobond, Indosuez Wealth Management.

### However...

While policies can be set, the eventual transmission to the economy matters. Market sentiment was clearly lifted by the stronger-than-expected measures (as can be seen in the stock market), but scepticism remained on any lasting impact to China's growth or the property market.

Case in point: PBoC 's re-lending programme has faced a slow take-up due to the poor potential returns and weak buying sentiment while developers continue to face funding risks.

While households are expected to reduce mortgage payments by CNY 150 billion (0.1% of GDP) due to the planned cut in interest rates for existing mortgages, the transmission to consumption will face leakage, as propensity to spend is likely low due to weak consumer confidence (Chart 2).

### Going ahead

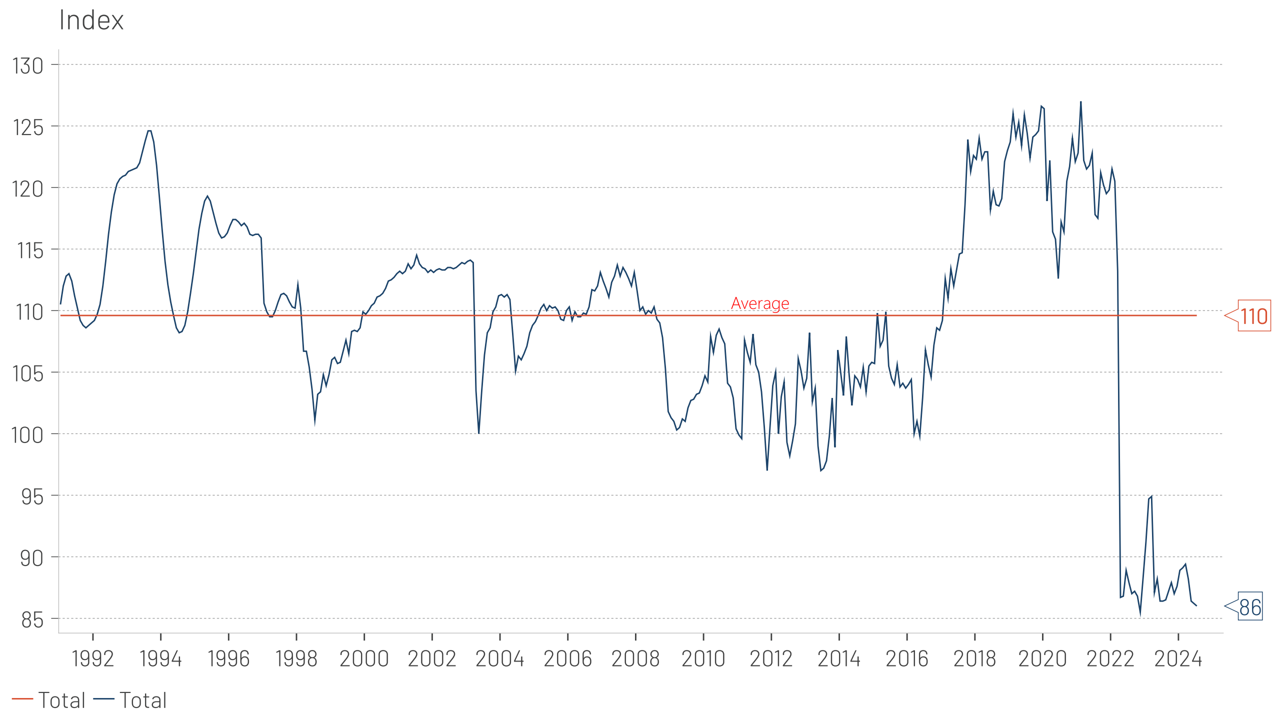
Despite questions on the eventual transmission to sentiments, consumption, or even GDP growth, one thing is for sure - China's recent measures are steps in the right direction.

The concerted effort to announce the various policies show a political will for policy communication, a welcomed (and much needed) pillar of stability for consumer/investor/corporate sentiments as they adjust their expectations.

Beyond the short-term boost to confidence, the market is likely to wait and see whether China actually adds a fiscal leg to the monetary leg of the stimulus (aimed at stimulating consumption via direct budget measures).

The good news? China's policymakers signalled that there will be further policy steps to support growth, fuelling market expectations.

**Chart 2: Chinese Consumer confidence**




Source: CEMAC, Macrobond, Indosuez Wealth Management.

### Light at the end of the tunnel for China equity investors?

The announcement by Chinese authorities of a surprise, substantial, wide-reaching stimulus package has had a **dramatic impact on Chinese equity markets**, so far (at the time of writing): both the Hang Seng China Enterprises index (HSCEI) and Shanghai Shenzhen CSI 300 Index have been up 14% and 16% (in USD), respectively, from 23 September to 27 September 2024 (source: Bloomberg).

**From a low base and deep under-owning by global investors**, the substantial Chinese stimulus package certainly boosted equity investor sentiment as a first leg in a potential, substantial, broad, rally.

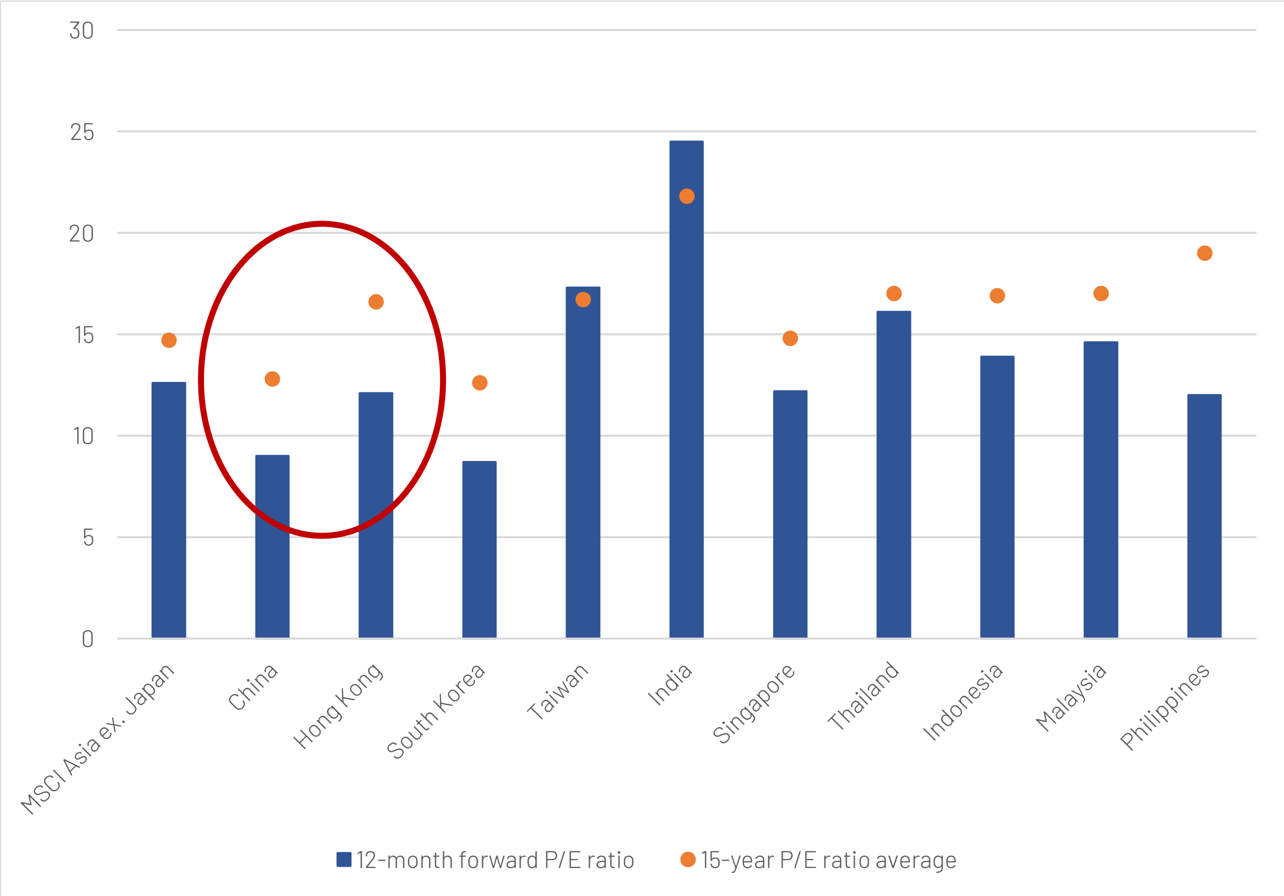
However, we believe that global investors might remain somewhat cautious, at first, in order to assess whether further policy announcements come online, particularly on the fiscal front and the transmission of stimulus measures to actual consumption. The obvious question remains the potential difference between real economy growth and corporate profits versus actual equity market performance.

China's latest substantial policy stimulus announcement is essentially a domestic economy-oriented package that could bring **some "light at the end of the tunnel" for Chinese equity investors**. Main support factors are (very) low valuations (forward P/E multiple for MSCI China remains undemanding at 9.5x after the current rally, at the time of writing) and a potential switch in global investment flows back to China, in addition to substantial, specific, liquidity programs aimed at local equity markets (stimulus package).

Another potential catalyst for Chinese equity markets is the *National Stabilisation Fund*: the PBoC confirmed that this is under consideration. This could boost local equity markets down the line.

As for China equity market positioning, at this time, we prefer large cap, liquid and high beta stocks as well as selective yield plays, mainly in the internet and financial sectors. In addition, we favour subsidised sectors such as Automobile and Home appliances. In any case, stock selectivity will remain key in China, more so than ever.

**Chart 3: Deep valuations discounts for China/Hong Kong equity markets - Asia 12-month forward Price/Earnings ratios vs. long-term average**




Source: FactSet, Macrobond, Indosuez Wealth Management.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