CIMB preferred

28 July 2021

Regional Equities

China Market Update – Heightening Regulatory Risk

What happened?

- The crackdown by China regulators in property, big tech, and most recently, the food delivery, and education sectors has caused some "panic selling" in the overall Chinese equity market. This has created uncertainties as the market worries if the government could expand to other industries such as healthcare or others.

New government measures

- Central government announced new rules to regulate the after-school tutoring (AST) industry.
- China revised rules to support third-child policy.
- Mortgage rates for first-house purchases in Shanghai will climb to 5% from the current 4.65%, while rate for the second-house purchases will increase to 5.7% from 5.25%.
- Central government issued guidance of real estate monitoring, which argues to continue to regulate market orders including developers, housing transactions, rentals and property management.
- China issued regulation to tighten oversight of the online food delivery sector.

Why does regulator clampdown?

- To rein in private enterprises that it blames for exacerbating inequality, increasing financial risk and challenging the government's authority.
- The focus on "common prosperity" that may mean more regulatory changes in areas with important social welfare implications.
- Our read is the intention is probably to allocate more resources and capital towards the more productive high-tech manufacturing and technology sector.

China to concentrate on tech-dependency

- During the recent China National People's Congress (NPC) ended on 11 Mar, China reiterated its commitment to reduce dependence on US key technology. The government will further direct resources to focus on semiconductors, artificial intelligence, quantum computing, neuroscience, and biotech. Public and private sector spending on research and development of new products is projected to rise to $580 billion a year by 2025 -- more than what U.S. spent in 2018. While China would still need to rely on foreign technology, aggressive moves such as tax exemption and incentives could help to encourage future growth in the China semiconductor or IT-related industries.

CIMB Asset Class Outlook

- Though regulatory risk remains elevated in the near term, we remain Overweight on Regional Equity over the long term as Chinese economy continues to recover from the pandemic crisis, continued investment into key technology sectors to reduce dependency on the US, commitment to achieve carbon neutrality by 2060, hence, a high priority in green sectors such as renewable energy, electric vehicles and environmentally friendly industrial equipment, and also the recent sell-off has brought down its overall equity market valuation to a more attractive level.

Recommended strategy

- Investors are advised to have a diversified investment portfolio allocation with a combination of Equity, Bond, and Alternative.
- For investors with zero or low exposure to Regional equity, average cost in to gain exposure at a more attractive entry point.
- For investors with high exposure to single country/sectorial focus equity funds, may consider to diversify into balanced or fixed income funds to reduce volatility.

Source: CIMB Consumer Products, Wealth & Preferred, Bloomberg, Principal Asset Management – July 2021

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