China 2022: A Year of Opportunity

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China is accelerating efforts to achieve Common Prosperity and implementing other policy initiatives aimed at sustainable growth. What will this reshuffling of policy priorities mean for investors in 2022 across China's equity and bond markets? We asked Vivian Lin Thurston, CFA, a portfolio manager on our Emerging Markets Growth, China A-Shares Growth, China Growth, and Emerging Markets ex China Growth strategies, and Clifford Chi-wai Lau, CFA, a portfolio manager on our emerging markets debt team.

Watch the video or read the recap below.

A Year of Opportunity

Vivian: We expect year 2022 to be a rebalancing year of the Chinese economy. We expect the Chinese government to balance between growth and sustainability, more so going forward, as a result of its new initiatives in Common Prosperity and Carbon Neutrality.

Economics

Clifford: Economic performance has been on track, but there are many conflicting forces behind the scenes, as political agenda gains influence relative to technocratic economic policies.

Vivian: Against this backdrop, we are likely to see a shift of the mix of Chinese economic growth going forward. Previous growth drivers, such as the internet economy, could contribute less. Other growth drivers, including high-end manufacturing and green energy, could accelerate.

Bonds

Clifford: We expect balanced, two-way flows to drive the Chinese government bond market in 2022. Foreign inflows should continue to be strong, as China is one of the few major economies running positive real interest rates. But Chinese bonds could become less attractive, as interest rates rise globally amid pent-up inflationary pressures.

Given these countervailing factors, local inflation could dictate the direction of the Chinese bond market this year. But I'm cautiously optimistic on Chinese government bonds, and I think that current valuations are still attractive, both from an outright and relative perspectives.

Equities

Vivian: Some equity market segments have faced regulatory and policy headwinds. But this has stabilized in recent times.

We continue to see structural growth opportunities in consumer and healthcare, especially those industries with lower policy risks, including liquor, travel, Chinese traditional medicine, and specialty medical services.

We also like technology. Digital technology used to be dominant, and is still important, but hardware-driven technology advancement will be a bigger story going forward. This includes high-end manufacturing, automation, semiconductors, EV batteries, and the like.

Currency

Clifford: The renminbi is an important risk factor to watch for currency-adjusted bond returns. It is strong now, but could start to be challenged, as there is an increasing need to loosen Chinese macro polices, and export growth may start to slow.

Inflation

Vivian: We are also watching inflation. China's consumer inflation has been quite moderate in recent times. This was driven by lower and weaker-than-expected consumer spending and demand in 2021 as a result of COVID lockdowns.

If the COVID situation stabilizes in 2022, and the Chinese government moderates its zero-tolerance policy against COVID, we could see more opening up in 2022, and further upward pressure on China's consumer prices going forward.

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