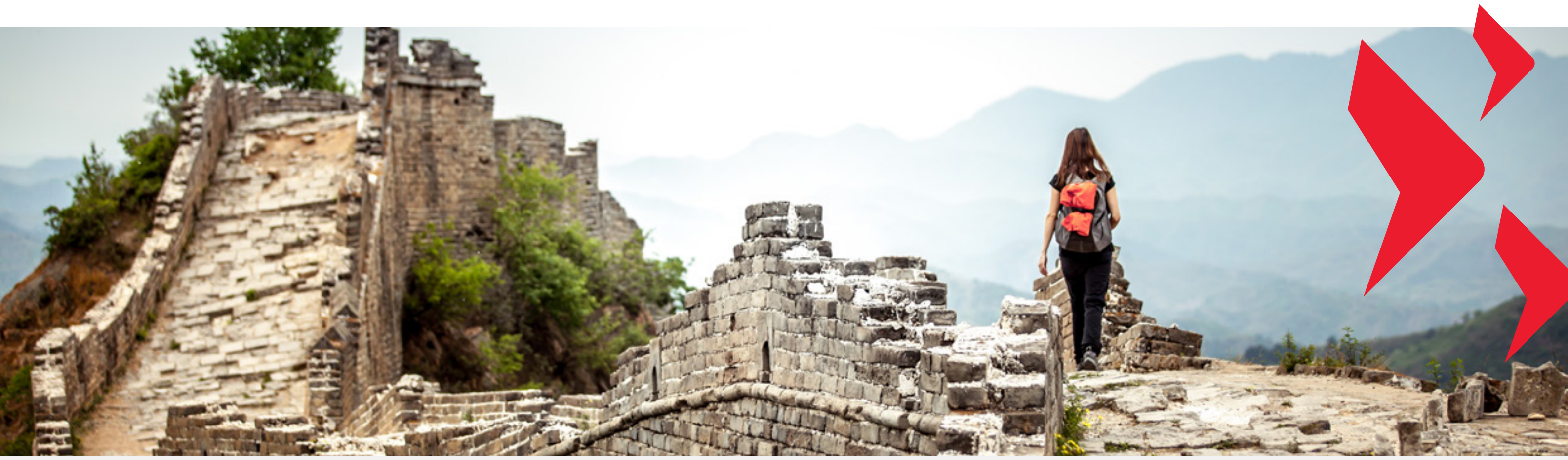

2023 Market Outlook

Tracking China's re-opening

China's zero-COVID policy and the turmoil in its property sector had weighed on the Chinese economy and equity markets in 2022. We believe that we are past the worst in terms of impact for investors and with valuations, earnings expectations and investor positioning at extremely low levels, the potential upside is attractive as China moves towards re-opening its economy in 2023.

The Chinese government faces multiple policy trade-offs in 2023 as it seeks to create a more balanced and sustainable economy in the long term while ensuring social stability in the near term. This balancing act is further complicated by the country's COVID policy, a slowing global economy and rising geopolitical tensions.

> **There is still a case for holding Chinese equities.**

THE CASE FOR CHINA

Despite China's recent macro and geopolitical challenges, we believe that there is still a case for holding Chinese equities in investor portfolios. Over the longer term, economic development remains one of the Chinese Communist Party's top priorities - GDP per capita is targeted to grow by a compounded average growth rate of +5% by 2035 according to the 20th Party Congress report. Higher domestic consumption, more diversified growth drivers and improved resource allocation should result in a more balanced economy.

Despite recent restrictions imposed by the US to limit Chinese companies' access to advanced semiconductor chips, we believe that China's pace of innovation will continue as the government focuses on innovation and supply chain security. It is forecasted that over the next five years, China's foundry capacity will grow at more than twice the rate compared to the rest of the world, as China seeks to localise its semiconductor supply[1].

The Chinese A-share market is a large and diverse equity market which offers investors significant portfolio diversification. China A has a correlation of 0.33 with Developed Markets and 0.49 with Emerging Markets[2]. China's bond market is also one of the largest in the

Source: [1]Gartner. [2]Bloomberg. Weekly returns for the period of November 2012 to November 2022.

world. The low correlation between Chinese and global government bonds of 0.24 since 2013 offers diversification benefits to global investors[3]. With investors significantly underweight both these asset classes, the potential upside from a rise in allocations is compelling.

ALPHA OPPORTUNITIES

Within Chinese equities, we believe that there are alpha opportunities in sectors that are aligned with China's strategic goals as well as in sectors that will benefit from China's structural growth trends.

In the near term however, we see the services, industrials and materials sectors benefitting from China's re-opening and recovery. As most global central banks continue to hike rates into 2023, albeit at a slower pace, we expect Chinese policymakers to keep monetary policy accommodative, which would be supportive for Chinese bonds.

We expect China's growth to bottom out in the first quarter of 2023 as the government fine tunes its COVID policy (reduced mass testing and fewer days of quarantine) and provides more supportive measures for the property sector (lowered restrictions for funds in the escrow accounts and financing support for private developers). Fundamentals may remain depressed in the short term given the lagged impact from policy easing. A full re-opening would probably take place around the first half of 2023 and China's GDP growth is likely to rebound to 4-5% in 2023, up from 3-4% in 2022. That said, a disorderly re-opening and a rise in inflation as the economy rebounds would be key risks for China.

PROPERTY TURNAROUND ONLY IN LATE 2023

In the fourth quarter of 2022, the government had announced several measures to help alleviate the liquidity pressure within the property sector. RMB250bn of financing was set aside to support the private developers while the People's Bank of China and the China Banking and Insurance Regulatory Commission issued a "16-point plan" regarding the delivery of completed units, refinancing and risk management. For the first time, the plan acknowledged the importance of supporting companies and not just projects. The grace period for banks to reduce their exposures to the property sector was also lengthened. That said, execution is still key and a recovery in physical property sales is needed for the sector to normalise.

At the point of writing, primary sales and property investment remain weak and it would take time for homebuyers' confidence to return. As such, we are unlikely to see a turnaround in property fundamentals till late 2023. As the government seeks to reduce systemic risks and

Opportunities within Chinese equities

Market/Sectors	Rationale
China A	
High-end manufacturing, new energy, healthcare, semiconductors	Government's strategic goals of self-sufficiency, technology independence and energy security
MSCI China	
Renewables	China's goal to reach peak carbon emissions in 2030 and carbon neutrality in 2060
Hospitality	Structural increase in Chinese spending on domestic and international travel
Smart infrastructure	Digitalisation and data proliferation

Source: Eastspring Investments, November 2022.

Source: [3]Bloomberg. Weekly returns for the period of January 2013 to October 2022.

bolster market sentiment, the property-related sectors may enjoy a re-rating although the upside would be capped by still-weak fundamentals. Against this backdrop, we continue to favour state-owned developers over private developers.

We see the Local Government Financing Vehicles (LGFVs) continuing to play a key role in supporting the economy as infrastructure will be an important growth driver in the near term. LGFVs are fully owned by the respective local governments and are set up to finance, invest in and operate local public infrastructure and social welfare projects. Although the downturn in the property sector has raised concerns over the financial health of these vehicles, their deep linkages with the local governments and the potential damage to the regional funding environment from any default suggest that there will be government support to help resolve LGFV debt issues. In addition, the local governments' fiscal balances are likely to improve in 2023 as China gradually re-opens.

Investment implications

Themes	Rationale	China A equities	MSCI China equities	China onshore bonds (Sovereigns/LGFVs)
Enhancing portfolio diversification	Low correlations with global asset classes suggest that Chinese equities and bonds can help increase portfolio diversification.	✓		✓
Positioning for China's re-opening/recovery	Bottoming of economy in 1Q23 to lead to more stable earnings and market re-rating. Current underweight positioning in portfolios and cheap valuations suggest attractive upside.	✓	✓	
Benefitting from China's accommodative monetary policy	Still low domestic interest rates, amid a global tightening cycle, will underpin Chinese assets.	✓	✓	✓
Achieving China's strategic goals	Alpha opportunities can be found in sectors that support China's strategic goals of self-sufficiency, technological independence, energy security and its net zero ambition.	✓	✓	

Source: Eastspring Investments, November 2022.

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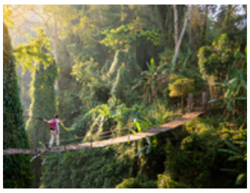
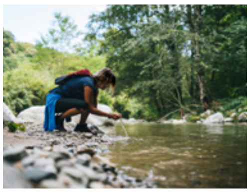
Explore the other themes in our 2023 Market Outlook

Mapping
another new normal



Embracing
a different Asia



Charting
sustainability pathways

Pursuing
resilience amid volatility

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