Kai Kong Chay
Senior Portfolio Manager
Greater China Equities

On 15 April, the People's Bank of China (PBOC), China's central bank, announced a reduction in its reserve requirement ratio (RRR). Subsequently, the government also published 23 measures to support individual and small businesses and stepped up its efforts to keep supply and industrial chains stable. In this investment note, Kai Kong Chay, Senior Portfolio Manager, Greater China Equities, presents an updated view of the China and Hong Kong markets. He believes that the latest measures reiterate China's stance on economic stability and sees opportunities in China and Hong Kong equities that could benefit from these supportive policy actions.

China rolls out measures to support economic growth

China's central bank flexes its monetary-policy tools

China announced several measures to release long-term liquidity into the financial system to bolster the economy. These include:[1]

- On 15 April, the PBoC reduced the RRR for most banks by 25 basis points and by 50 basis points for smaller lenders, effective 25 April.
- The one-year policy interest rate remains unchanged, disappointing most economists who predicted a cut.[2] (See Chart 1)
- According to the PBoC, the RRR change will unleash about RMB530 billion (US$83 billion) of long-term liquidity into the economy. The PBoC last reduced the ratio in December 2021.

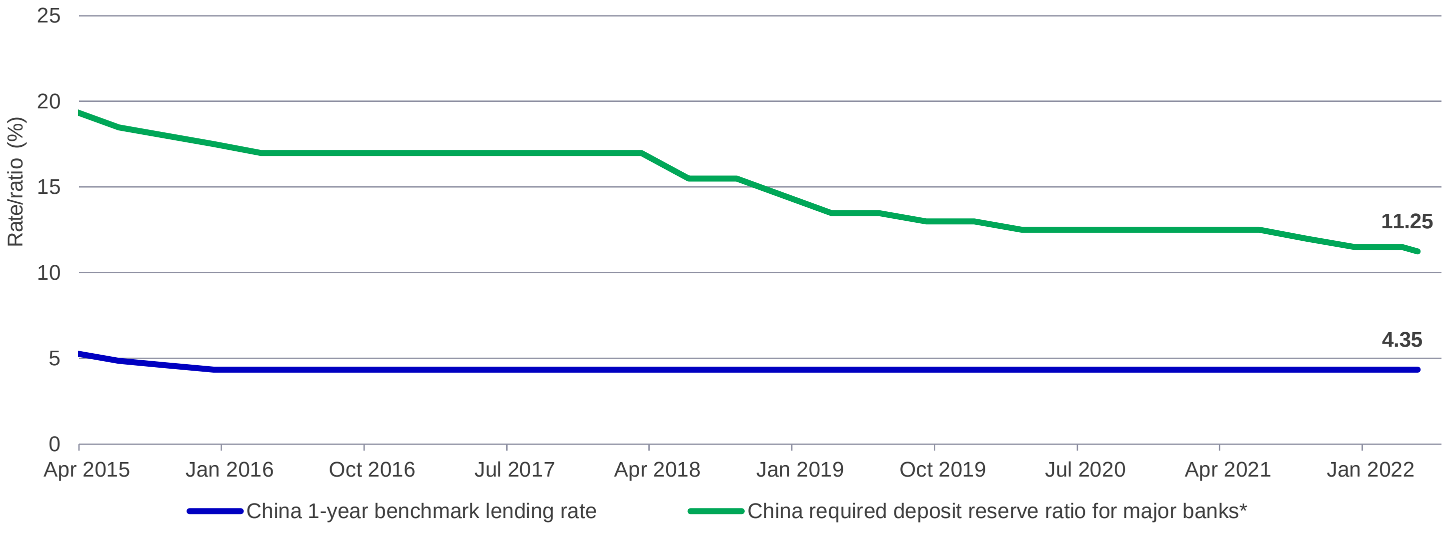
Measures to support economic growth

In addition, China's corporates or small and medium enterprises (SMEs) may benefit after the central bank announced 23 additional measures to support the economy. Some key highlights include: [3]

- Banks are being urged to expand lending to people with "flexible employment", such as taxi drivers, online shop-owners, and truck drivers, and provide longer-term and cheaper loans to small businesses.
- The PBOC vowed to extend or establish relending programs that provide funds for banks to lend to sectors that were hit by the pandemic. Such relending programs are expected to represent approximately RMB1 trillion (US$157 billion) in additional bank loans.
- Local authorities are being called on to set appropriate minimum down payment requirements, and mortgage rates based on each city's conditions and banks are encouraged to support the reasonable financing needs of property developers and construction companies.

[1] Bloomberg, 19 April 2022.
[2] Reuters, 18 April 2022.
[3] Bloomberg, 19 April 2022.

Chart 1: China's reserve requirement ratio and lending interest rate (as of 19 April 2022)



Source: Bloomberg, 19 April 2022. *Note: The reserve requirement ratio (RRR) will be reduced to 11.25% is effective from 25 April 2022.

- Policy banks are being asked to step up their financing to major investment projects, while commercial banks are expected to be more
- proactive in lending to infrastructure projects and purchase local government bonds to support advanced construction.

- A transfer of RMB600 billion of profit was made to the central government in mid-April, which will be mainly used for tax rebates and transfer payments to local governments. This profit transfer has increased the base money supply and equals a 25 basis-point cut in the reserve requirement ratio, the PBoC said.

Separately, the China Banking and Insurance Regulatory Commission vowed to increase financial resources for logistics, transportation, and courier industries and use the relending funds to lower financing costs. It will provide funding support to smaller businesses suffering from temporary difficulties due to COVID-19.

The implications of China's newly announced measures

While some market participants expected a bold reduction in interest rates, we believe China has adequate policy tools other than a rate cut to support growth if needed.

Despite a near-term dampening of investor sentiment, we believe the recent measures prove that China is determined to support the local economy:

- China continues to coordinate between epidemic control and economic development. On Monday, 18 April, Chinese Vice Premier Liu underlined efforts to stabilise supply and industrial chains. Shanghai's city authorities have asked 666 local and foreign companies, mainly in the automobile, semiconductor, and energy industries, to resume production amid the city's lockdown.

- We expect more targeted fiscal stimulus to come in the third or fourth quarter of 2022, which will likely underpin further economic growth.

- Despite the fact that more than 60 non-Tier 1 cities have already rolled out relaxation measures, additional housing-related policies may be unveiled. Many cities have introduced more favourable mortgage costs or down payment requirements, while more Tier 2 cities such as Quzhou, Dalian, Suzhou, and Nanjing have relaxed home purchase and/or resale restrictions.[4]

[4] Reuters, 18 February 2022.

- China is pushing ahead with its mRNA vaccine development, which should help fight the spread of Omicron or other COVID-19 variants down the road. For example, the country's health authorities have recently approved the trials of two mRNA vaccines.[5]

Structural growth opportunities in China and Hong Kong equities

While we remain selective, we see opportunities in the sectors and key themes of China and Hong Kong equities that should benefit from China's structural growth story. These opportunities include:

- Exposure to both domestic Hong Kong equities with attractive dividends while also tapping into growth areas.
- Potential beneficiaries in the consumption sector. For example, companies with the ability to pass on cost inflation.
- The materials sector could potentially benefit from a boost in infrastructure investment.
- In general, we continue to favour sectors that should benefit from China's 14th Five-Year Plan (FYP). Preferred themes that the FYP could support include consumption upgrades, research & development (R&D), innovation, renewable energy, and energy transition, as well as new infrastructure. (See China and Hong Kong equity markets tested by a "perfect storm")

China stands ready for further policy measures

Overall, we believe China is ready to act and likely to step up policy easing should a sharper economic slowdown occur. In addition, China has the levers for fiscal support, such as further spending on investments and infrastructure, as well as tax refunds and cuts. While near-term market sentiment has been mixed, we view the latest measures as signs that China is on track to maintain its economic course.

[5] South China Morning Post, 4 April 2022.

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