

PREMIER SPONSOR ARTICLE SERIES

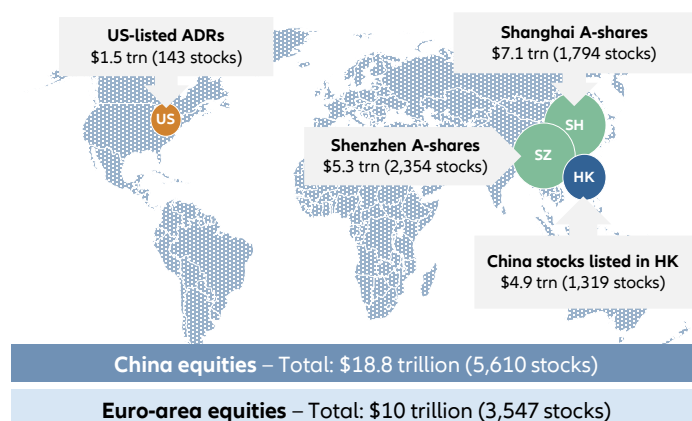
Quick Facts About China Equities

China's equity markets have opened up as the country's economy transforms. From Shenzhen and Hong Kong listings to the Nasdaq-like STAR board, Chinese companies are attracting significant capital from foreign investors. Here are eight things to help you learn about China equities.

1. Relatively large equity opportunity set

China's capital markets have expanded significantly in recent years. The combined market capitalisation of the exchanges in Shanghai, Shenzhen and Hong Kong – plus US-listed American Depositary Receipts (ADRs) – is around USD 19 trillion (see Exhibit 1). This is significantly higher than the USD 10 trillion market cap of euro-area equities. Even within China A-shares, the different listing venues offer varying exposures to sectors and market caps. Investing across China's exchanges can bring different exposures.

Exhibit 1: Stock exchanges for China equities (in USD)



Source: Shenzhen Stock Exchange, Shanghai Stock Exchange, Hong Kong Stock Exchange, Bloomberg, Allianz Global Investors, as of December 31, 2020. The total figures are for comparison only, the stocks included may be listed in more than one exchange. Offshore China stocks are defined based on companies with ultimate parent domiciled in China. Suspended stocks, investment funds and unit trusts are excluded.

2. An economy driven by an increasingly dynamic private sector

Historically China's economy was driven by spending and employment at large State Owned Enterprises (SOEs) but significant reforms drove down their share of GDP from 50% to 30% over the last 15 years. According to a paper from the World Economic Forum on 7 May 2019 the private sector, often expressed by the numbers 60/70/80/90, is contributing 60% of China's GDP, 70% of innovation, 80% of urban employment and 90% of new jobs. China's policies are also encouraging a dynamic, startup culture which it hopes will incubate tech success.

3. The STAR market (Shanghai Stock Exchange Science and Technology Innovation Board) for tech and science startups

Recent developments such as the Nasdaq-like STAR board, which streamlined listing requirements, are facilitating the growing number of tech-driven IPOs. After launching in July 2019 with 25 names, the market had grown to 215 listed companies by January 2021. There are currently around 500 firms at different stages of the IPO registration pipeline. The FTSE already has plans in place to include the STAR market in its equity indices, although MSCI has not yet detailed how it will treat the new market.

4. New infrastructure

One of the important consequences of rising trade tensions between the US and China has been a strengthening of Beijing’s resolve to be self-reliant in innovation-driven and strategically important industries. Irrespective of trade tensions, China is determined to develop a 21st century economy built on “new infrastructure” as part of the “Made in China 2025” policy. Key industries benefiting from this include artificial intelligence, 5G, cybersecurity, alternative energy, electric vehicles, semiconductors and other sectors leading the change.

5. The “youngest” in Asia

China is the youngest market regionally, reflecting the dynamic nature of China’s corporate universe. This means Chinese companies have been part of the region’s benchmark index constituents for the shortest amount of time. Based on the MSCI All Country Asia Pacific ex Japan Index, the average onshore stock in China has been listed for only seven years, whereas the average stock in other markets has been listed for over 20 years.

6. Steady foreign inflows

The Shanghai and Shenzhen Stock Connect schemes that launched a little over five years ago allow investors outside of mainland China to buy A-shares in Shanghai or Shenzhen via the Hong Kong exchange (known as a “northbound” trade). Since the Shanghai Stock Connect opened in November 2014, Chinese equities have enjoyed 62 months of “northbound” inflows with only 13 months of outflows. Notably, the ongoing inflows have occurred despite macro headwinds including political volatility caused by rising trade tensions between the US and China.

7. Lower correlation with global equities

China A-shares have a correlation of 0.21 with global equities over the last 10 years as of 31 December 2020. That means China A-shares move in the same direction as global equities only 21% of the time. Or looked at another way, almost 80% of the time they move in a different direction. In comparison, US and global equities have a correlation of 0.94. Holding China A-shares in a global equity portfolio may therefore add diversification benefits.

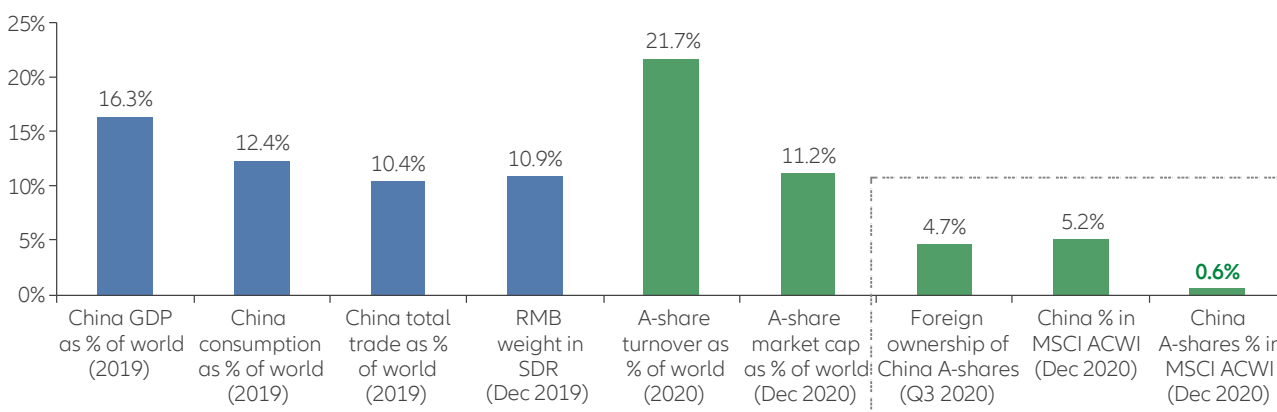
8. A mismatch between China’s scale and its index weight

China’s increasing weight in key benchmarks such as the MSCI All Country World Index (ACWI) is accelerating the institutionalisation of its market. However, when comparing with China’s economic influence and market scale (accounting for 16% of global economic output among other factors), China may still be under-represented in benchmark indices (see Exhibit 2). Further, investors replicating an index’s China allocation are underweight some of the fastest growing Chinese companies, specifically the young, dynamic tech and “new infrastructure” firms discussed earlier.

Is your portfolio properly accessing the China’s equity opportunity set?

Our research suggests that index tracking may not always be the appropriate approach to China investing. For a more balanced approach to China or a portfolio to better reflect the full China opportunity set, investors may want to consider allocating more to China A-shares than benchmarks do or carving out an even larger standalone All-China equity allocation.

Exhibit 2: Key statistics on China and China equities



Source: Wind, Allianz Global Investors. Data as of January 2021

Important Information

Data is sourced from Allianz Global Investors, as of 17 March 2021, unless otherwise stated.

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Source: Allianz Global Investors, data as at 31 December 2020

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