A MOMENT IN MARKETS – THE CHINA TRADE

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The Chinese economy grew[1] by 4.9% year on year in the third quarter. This follows the 6.8%[2] contraction in the first quarter – the sharpest since records started in 1992 – and 3.2%[3] year on year growth in the second quarter. Has Chinese data been encouraging all-round? How are asset markets reacting and what options do investors have for making a China trade?

Small data, big impact

Unemployment in China[4], which rose to 6.2% in February, is down to 5.4% in September – only marginally higher than 5.2% in December 2019. Industrial production increased 6.9% year on year in September – the highest increase since December 2019. This data point has vindicated the strong recovery in Purchasing Managers Indices[5] (PMIs) – which are important, but only show month on month change in activity. Retail sales[6] – an important barometer of consumer wellbeing – have also bounced back and risen by 3.3% year on year in September after being negative between January and July this year.

The improvement in economic data is in line with an exceedingly low number of new infections in the country – compared to many other countries which are now anguishing over a second wave of the pandemic.

Markets are moving

Market optimism for third quarter data started developing since the start of October. Data has not disappointed and markets are reacting positively (see table below). Investors have a few different options when it comes to positioning themselves for the economic recovery in China.

Asset Class	Month to date	Year to date
S&P China 500 Index	+5.8%	+24.1%
MSCI Emerging Markets Index	+4.0%	+3.0%
Bloomberg Industrial Metals Subindex	3.4%	+4.9%

Source: WisdomTree, Bloomberg. Data as of 19 October 2020. Month to date refers to October returns and Year to date refers to 2020 returns to 19 October. USD total returns shown.

Historical performance is not an indication of future performance and any investments may go down in value.

1. Chinese equities: Around half of the exposure of the S&P China 500 Index is in on-shore listed A-shares – linked closely to the domestic economy – with the remaining being in shares listed across off-shore exchanges. The index, therefore, provides a holistic assessment of Chinese equities and its gains point to the positive impact of improving economic data.

2. Emerging market equities: The fate of the MSCI Emerging Markets Index is inextricably linked to Chinese stocks given China's weight of almost 42% in the index. Consumer discretionary, with a weight of over 20%, is the largest sector in the index with China's Alibaba being the largest stock. The improving financial well-being of the Chinese consumer bodes well for broader emerging markets as well.

3. Industrial metals: With key trading partners – the United States and Europe – still battling rising infections, China is looking to focus on inducing growth in the domestic economy with increased spending on manufacturing and infrastructure. China's imports of copper ores and concentrates in September were significantly above not just 2019 levels, but the prior 5-year range. China's increased spending is helping fuel the rally in copper and the broad industrial metals complex.

Source

[1] [2] [3] [4] [5] [6] Trading Economics as of 19 October 2020

[7] MSCI as of 19 October 2020

[8] Bank of America as of 19 October 2020

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