



What are the investible themes in China?

January 2021

KEY TAKEAWAYS:

- China is leading the world and its peers in Asia on the road to economic recovery, and relatively attractive opportunities have emerged as growth resumes.
- Key potential growth opportunities are emerging in China's technology (tech), healthcare and consumer industries. Taking an active, longer-term focus and bottom-up stock picking approach could help identify quality Chinese corporates, and capture opportunities in China's equity markets.
- The global economic recovery is continuing and North Asia has emerged as a key focus for some investors seeking growth. China, with economic growth projected at 2% in 2020 and 7.9% in 2021¹, takes the spotlight with relatively attractive long-term investment themes in its equity markets.
- Growing domestic demand, import substitution and technological advances are likely the key considerations for investors seeking to optimise China's potential in their growth portfolio. We share our views on some investible themes for 2021 in China's equity markets.

3 investible themes in China's market

The global public health crisis has accelerated some structural trends in China, including domestic technological development, healthcare innovation and consumption upgrade. Such long-term trends are likely to take hold as recovery broadens in domestic demand. Additionally, the Chinese government is also continuing to promote coordinated pro-growth policies while deepening reform measures that support these trends.

1 Tech in everyday life

Tech has gone beyond smart phones and eCommerce in China. Artificial intelligence and cloud computing are becoming a part of everyday life. Amid geopolitical uncertainty and facing a decoupling risk with the US, China's tech industry is embracing an inward economic pivot, and looking to make breakthroughs in core technologies to reduce its reliance on imported software and hardware.



Software application:

The trend towards digitalisation has accelerated the commercial- and home-use of software. Cybersecurity, for example, currently accounts for a relatively small portion of Chinese corporate spending, but could gradually take up a larger share in the overall tech spend.

~RMB

110 billion
in 2024

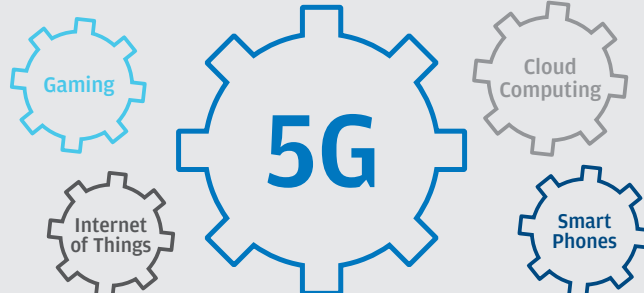
China's cybersecurity market size is expected to increase by more than four times from about RMB20 billion in 2014²

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Semiconductor manufacturing:

China is building a domestic tech industry, particularly in semiconductors where previously, it had primarily been an importer. In addition, the deployment of 5G has also driven market demand for semiconductors.



Clean energy application:

China is moving towards greater consumption of cleaner energy, and has become a leader in the use and manufacture of electric vehicles and solar energy equipment. Electric vehicle sales are expected to grow further on the back of supportive government policies, and increasing demand for environmental-friendly vehicles.

19%

Annual new energy vehicle sales in China is estimated to reach 5.9 million units in 2025 with a penetration of 19%, up from 1% in 2015²

2 Longer-term healthcare demand

One of the structural changes arising from the crisis is increased demand for healthcare services and products, including healthcare infrastructure, preventive treatment and vaccine development. China's healthcare industry covers a considerable number of sectors, and spending on such services could continue to grow. We believe three macro trends are relatively attractive:



Research & development (R&D) outsourcing:

Contract research and contract manufacturing organisations could benefit from rising demand for R&D outsourcing globally.

Up >3x

China's biologics outsourcing services market size is expected to reach RMB9.2 billion in 2021 from RMB2.1 billion in 2016³



Medical equipment manufacturing:

Another trend accelerated by the global health crisis is increased spending on quality medical services and products, especially by the growing middle class in China. Against this backdrop, this could benefit hospitals and medical equipment suppliers.

7.9%

China's estimated healthcare expenditure as % of GDP in 2026, versus 6.2% a decade ago³



Pharmaceutical R&D:

Innovative pharmaceuticals and diagnostics-related corporates could also benefit from China's long-term investment in R&D. The return of Chinese talent from overseas is helping to fuel innovation in pharmaceutical R&D, alongside the creation of more pharma companies. This could boost scientific R&D in the domestic market.

46%

Year-on-year growth in China's healthcare R&D expenditure in 2018, versus 7% in the US³

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3 Better living standards and 'premiumisation'

As household income increases and the standard of living improves in China, its middle class is increasingly focused on lifestyle upgrades in both daily necessities and entertainment. Alongside supportive domestic policies, consumption is expected to become a key driver of economic growth.



'Premiumisation':

Wealth accumulation and the resulting lifestyle upgrades and greater demand for quality products and services have created a constructive backdrop for industry leaders in consumer staples such as dairy products, snacks and condiments. China's consumption 'premiumisation' is gradually driving growth.

Up >1x

Condiments market size in China is estimated to increase to about RMB300 billion in 2023 from RMB128 billion in 2013⁴



Online entertainment:

Chinese consumers across generations are increasingly shifting to online entertainment services, aided by higher adoption of broadband services. Wireless, or accessing the internet through mobile devices, is also gaining traction. We believe demand for 'live' streaming and online entertainment platforms could grow rapidly.

US\$

14.7 billion

in revenue by 2023

China's over-the-top video market is expected to maintain a compound annual growth rate (CAGR) of 20% in the five years from 2018, increasing revenue from US\$5.8 billion⁵



Offline consumption:

Changing mobility patterns globally have driven increased interest in travel within China. Cross-provincial tourism is regaining momentum, and this could bolster offline consumption, benefitting the tourism-related industries. This emerging trend, alongside Hainan Island's plan to turn into a free trade port by more than tripling its duty-free allowance, is driving overall consumption demand.

RMB

100,000

Quota for offshore duty free shopping is more than tripled from RMB30,000 per person/per year⁶

Capturing robust opportunities in Chinese equities with a professional team

China has entered a new economic cycle with opportunities evolving from several long-term structural growth trends. China's onshore equity markets offer a wider set of opportunities including more innovative ideas as compared with the offshore market. Nonetheless, this would also mean a prudent approach is needed to capture quality opportunities.

Leveraging our on-the-ground research which focuses on company fundamentals, our investment professionals integrate bottom-up stock selection with structural themes, seeking to capture opportunities with long-term growth potential.

Local expertise



1,600+

Company meeting annually⁷

In-depth coverage



590+

Greater China stocks, of which over 270 are A-Shares⁷

Dedicated Investment Team



20+

Investment professionals dedicated for Greater China Team⁷

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¹"China Economic Update - December 2020", The World Bank, 23.12.2020. ²Bernstein analysis, China Association of Automobile Manufacturers, Morgan Stanley, company data. J.P. Morgan Asset Management. Data as of end-May 2019. ³PWC, Frost & Sullivan, company data. J.P. Morgan Asset Management. Data as of end-May 2019. ⁴The World Bank, HSBC, company data. J.P. Morgan Asset Management. Data as of end-May 2019. ⁵"China Entertainment & Media Outlook 2019-2023", PWC, May 2019. ⁶"Hainan to raise duty-free shopping quota to 100,000 yuan", Xinhua, 30.06.2020. ⁷J.P. Morgan Asset Management as of 30.11.2020.



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