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The impact of coronavirus on Chinese equities

Concerns about the economic and financial impact of the coronavirus outbreak have seen some offshore Chinese equities come under pressure.[1] However, Ronald Chan, our chief investment officer for equities, Asia ex-Japan, believes that any market decline would be short-lived or contained. In his view, the outbreak is likely to ease with warmer weather in the spring, and investment sentiment should gradually improve. In the meantime, investors should remain focused on the market's long-term fundamentals.

Worries about the coronavirus have seen global investors become risk-averse, leading to a sell-off in some offshore Chinese equities. However, if we were to use market performance[2] and the experience from the SARS outbreak in 2003 as a point of reference, we believe that a broad-based correction should be relatively short-lived, with a more effective virus containment policy.

In light of heightened public health precaution and the introduction of provincial travel bans, we expect selective market segments such as hospitality, transportation, and gaming activities to face some short-term pressure. Meanwhile, online consumption activities may rise, benefiting other segments.

Uncertainty over the extended Spring Festival holiday period may also cause some disruption to manufacturing production in the first quarter. As such, the Chinese authorities are likely to engage in further policy easing to ensure growth stability.

Nevertheless, if the situation shows signs of containment, then high-quality companies with diversified footprints and strong business models should remain resilient. In our view, these firms could lead the rebound as consumption demand gradually resumes. While a full economic recovery may be delayed, the momentum in the underlying economy—such as the resumption of corporate capital expenditure in the fourth quarter of 2019—should provide a buffer to this unexpected business disruption.

Overall, key secular trends that form the basis of our investment themes are unchanged: online-led consumption upgrade, 5G rollout beneficiaries, and policy-driven opportunities as a result of medical reform, supply-side reforms, and the drive toward sustainability.

As we had mentioned previously, we think that disposable-income growth across China and the convergence of urban and rural incomes will offer unique opportunities for e-commerce platforms and app-based businesses.

We're still of the view that 5G rollout should remain a prominent theme in Greater China equities, especially in China A-shares, because the cell phone replacement cycle in mainland China is expected to shrink from 24 months to its historical average of 15 to 16 months. Therefore, we have a constructive view of battery producers, chips, frequency, and antenna-related industries.

Finally, we believe it makes sense to remain focused on policy-driven opportunities. We're also positive on firms that operate in areas touching on environmental protection, such as natural gas distribution and some waste-to-energy companies—they're likely to do well thanks to expected long-term support from the government.

1 Bloomberg, January 24, 2020 to January 30, 2020: Hong Kong's Hang Seng Index (in Hong Kong dollars) fell by 5.37%, while the MSCI China Index (in U.S. dollars) was down 4.1% during the period. **2 "**Investors look to history for clues on market impact of coronavirus," *Financial Times*, January 28, 2020.

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