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A Unique Mind On The Markets

RESEARCH NOTE

February 24, 2025

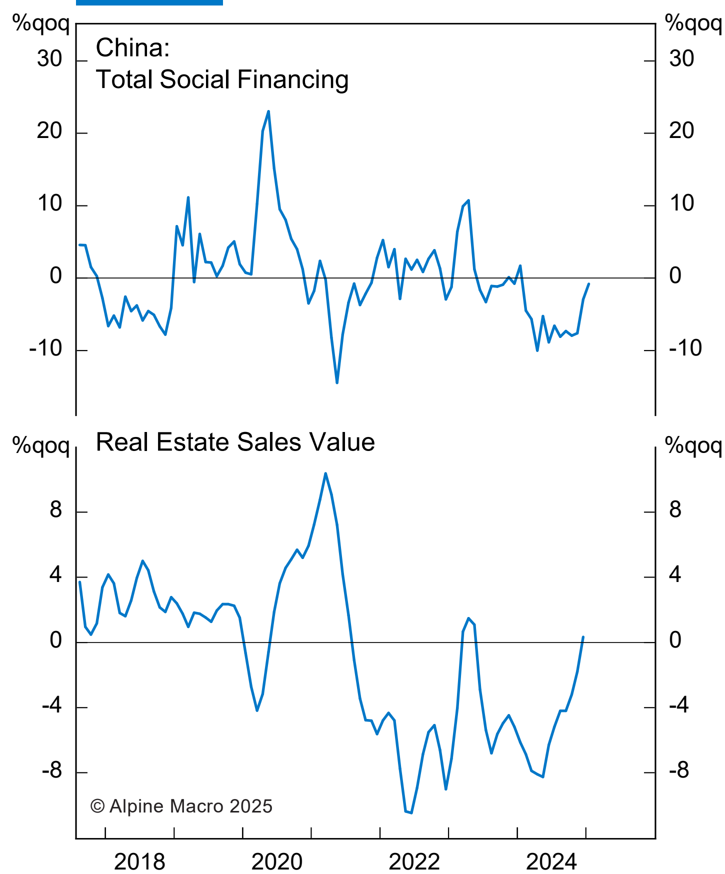
The China Surge: To Buy Or Not To Buy?

While the advance in U.S. equities seems to have stalled, Chinese shares have surged, led by tech stocks. Many clients have asked whether this rally is sustainable and if it's too late to buy. Alpine Macro has turned positive on Chinese stocks and recommended an overweight in Chinese equities since September last year.[1] Our positive view seems to be playing out. Although there have been a few major false rallies in the past, we believe that the current breakout is likely to be more durable:

First, while China's overall economy remains weak and GDP growth is still below potential, there are signs of improvement. The drop in real estate investment is narrowing, and contraction or deceleration in money supply, bank loans, and total social financing is also easing on a Q/Q basis (**Chart 1**). Additionally, Beijing is ramping up fiscal spending with larger doses of stimulus and earlier disbursements. Consumer confidence, which had crashed during the pandemic, is slowly recovering. Overall, the economy appears to have turned a corner.

Second, Xi Jinping's policy has shifted further in favor of private businesses. In a recent closed-door symposium with private entrepreneurs, Xi indicated that the government would take more aggressive steps to deregulate the economy, level the playing field for private firms, and offer more support to entrepreneurs.

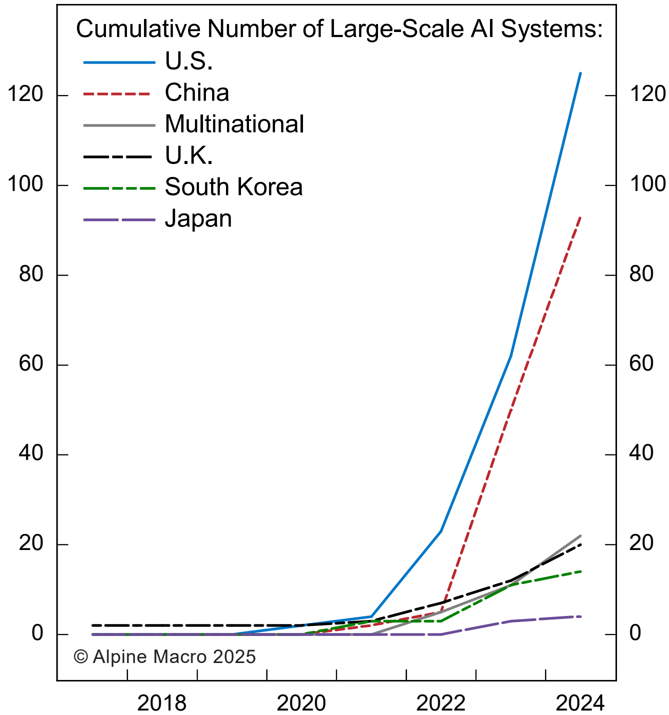
Chart 1 Signs Of Economic Improvement



Notably, Xi's speech made no mention of "common prosperity", state guidance, or rectification. This signals that the crackdown on private businesses five years ago has backfired. Now, Xi is pivoting from a "rectification movement" to a "revitalization campaign" aimed at encouraging private sector growth.

1 Alpine Macro *EM & China Strategy Special Alert* "China's 'Whatever It Takes' Moment?", (September 24, 2024).

Chart 2 The AI Race

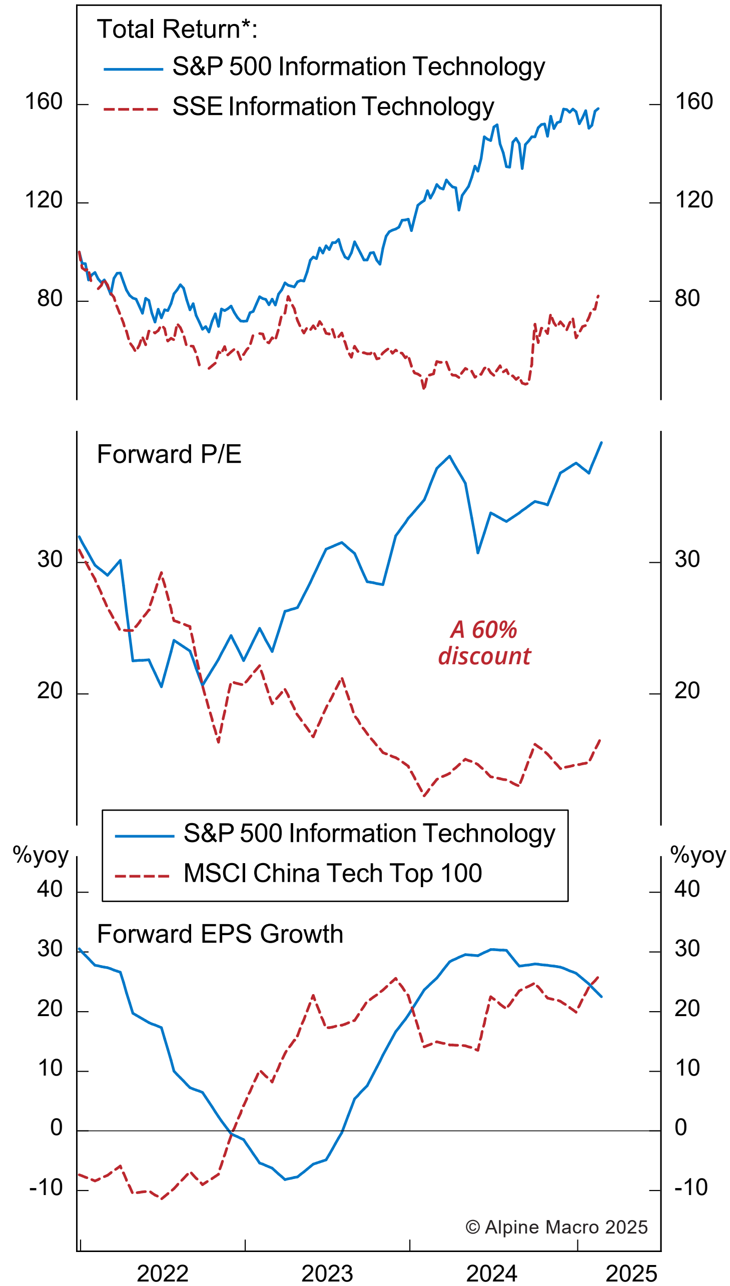


Note: The source defines AI models as "large-scale" when their training compute is confirmed to exceed 10^23 FLOP; source: Epoch, OurWorldinData

Third, the geopolitical climate is also evolving. The Trump administration appears to have more grievances with liberal Western governments than with Russia or China. Trump, who generally dislikes war, seems to believe that the U.S., along with major powers like Russia and China, can solve many of the world's problems.

Importantly, Trump's foreign and trade policies are driven more by commercial interests than by ideology, marking a clear departure from the Biden administration. The Trump administration has shown relatively little hostility towards Beijing, often criticizing its Western allies instead. We've long argued that Trump offers Beijing its best chance for improved relations with Washington, and this seems to be playing out.

Chart 3 The Case For Buying Chinese Tech Stocks



*In USD terms; rebased to Jan 2022=100

Fourth, the DeepSeek shock has shaken investors awake, drawing their attention to the rapid developments in China's tech sector. Chart 2 shows the intensifying AI race and neck-and-neck competition between U.S. and Chinese tech companies.

Importantly, Chinese tech stocks have massively underperformed their U.S. counterparts for an extended period (**Chart 3**), making their valuations notably compelling at this juncture. This is particularly so when earnings growth for Chinese tech companies has actually begun to exceed that for the U.S. tech index.

Bottom line: We believe the surge in Chinese shares will likely continue, fueled by improvements in China's economy, government policies, geopolitics, tech growth and valuation. However, Chinese equities are highly volatile. Investors looking to ride the rally should be prepared for sharp drawdowns and dramatic price swings. That said, the potential returns could be substantial within a 6-12 month horizon.

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