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GLOBAL MACRO VIEWS

China pulse check

U.S. exceptionalism is being stress-tested, the prospect of trade wars is growing, and Germany's fiscal stimulus is game changing. Amid these developing situations, it's worth checking in on a country resurfacing on investor radars, China.

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The U.S. economy is slowing under the weight of prolonged tariff uncertainty, while prospects for Europe brighten amid a fiscal thrust. Despite the escalation of U.S. tariffs, China is showing signs of stabilizing, attracting investor interest alongside a robust year-to-date equity rally.

There remain reasons for caution, with U.S. tariffs coming faster and higher than anticipated, warranting a selective investment approach.

Tariff red lines temper green growth shoots

The Chinese economy has been showing tentative bright spots, supported by fiscal and monetary easing that began in late 2024. Solid Lunar New Year spending, signs of bottoming in property and equity markets and a lift to exports from front-loading ahead of tariff threats have provided further tailwinds.

Even so, the structural backdrop remains challenged due to industrial overcapacity, low confidence and worsening demographics. Sharply rising trade tensions further threaten the main engine of growth, industrial exports.

Stimulus to partly prop up growth

Market expectations were ostensibly running high heading into this year's National Party Congress (NPC), yet China policymakers largely met them by announcing a highly ambitious "around 5%" 2025 growth target.

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Importantly, the announcement accompanied a slew of fiscal stimulus measures:

- A larger government deficit (4% vs 3% in 2024)
- An additional RMB300 billion boost of special treasury bond issuance (which now stands at RMB1.3 trillion, largely for retail and commercial equipment trade-in programs)
- A new, but previously announced, RMB500 billion state recapitalization
- A local government special bond quota of RMB4.4 trillion.
- Over the medium term, there is also an argument to be made that China has continued to diversify its export markets effectively.

Together, these should provide a 1.5-2 percentage point fiscal impulse to China's economy, in our view.

Will this be enough to support growth?

On the margin, yes. The trade-in program should provide some temporary respite for overcapacity sectors. However, for all the mention of consumption in this year's NPC, there was an absence of a meaningful boost to social spending, which in turn, would alleviate the structural headwinds for consumption.

Structural factors will likely continue to be a persistent drag, in our view, as the economy shifts to a lower rate of potential growth.

Will it be enough to fully offset U.S. tariffs?

Unlikely. A downward revision to our 2025 growth forecast, from 4.25% to 4%, captures the risks around the swiftness and steepness of the U.S. tariff announcements. While the U.S. administration has applied 20% tariffs on Chinese goods based on fentanyl flow, greater tariff announcements are expected after 2 April. There is scope for negotiations, though tariffs and ongoing uncertainty will likely drag sentiment.

Is there room for China's growth to improve?

Yes. Policymakers are keeping some powder dry to respond to any sharp deterioration in the external macro environment. Tentative signs of property market stabilization are helping, while the rise of DeepSeek and its positive artificial intelligence implications may further bolster confidence. Over the medium term, there is also an argument to be made that China has continued to diversify its export markets effectively. Should the transatlantic rift become more structural and permanent, greater economic cooperation may result in more integration with a Europe that is focused on rearmament, rebuilding infrastructure and the energy transition.

Over the medium term, there is also an argument to be made that China has continued to diversify its export markets effectively.

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Selectivity across assets

Despite the tariff headwinds ahead, further upside in Chinese equities is possible thanks to stimulus measures and wide-ranging trade deal prospects. China could also prosper in an environment in which tariffs on certain sectors are unlikely to be raised, and Chinese companies are able to make long-term investment decisions in the context of a more enduring framework.

By contrast, after an aggressive fixed income rally in late 2024, we have seen some correction in China's government bonds. This has been largely tied to a sharp rally in Chinese equities, aided by Deepseek; higher bond supply just as the central bank dampened expectations of a near term rate cut; and heavy local positioning. Yields are likely more reflective of fair value at current levels, in our view, reflecting near-term fiscal stimulus and ongoing trade tension uncertainty and lingering structural issues.

The world has arguably become more resilient to faltering Chinese demand than a decade ago. Yet for all policymakers' focus on reducing China's vulnerabilities by improving their manufacturing prowess, they are perhaps even more beholden to global demand, warranting a selective investment approach.

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Endnotes

Sources

All market and economic data from Bloomberg, FactSet and Morningstar.

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