

Future Quality Insights from China

One year on from China's policy pivot, tech is the big winner, but the recovery still looks uneven

By Finn Stewart, Global Equity Portfolio Analyst

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The view on the ground

I travelled to China recently to attend an annual investment conference, one year on from the government's policy pivot which unveiled a raft of measures intended to boost the economy. It was my first visit, and while the conference was busy and investors were cautiously upbeat, a resurgent stock market only tells half the story.



Source: photo of Shanghai by Finn Stewart

A recovery led by markets, not consumers

The post-stimulus rally in equities has been driven by the tech sector's strong performance, with markets also pricing in the potential for further policy support. Beyond that, doubts persist. In the midst of a generational property bust, consumer confidence is low and savings rates are high. There remains a glut of excess capacity in the manufacturing sector and global players have made it clear that this supply should be incrementally soaked up by domestic consumers. In the tier-one and new tier-one cities of Shenzhen, Guangzhou and Hangzhou, activity looks healthy. However, it is these cities which are at the heart of China's technology resurgence. In lower-tier cities, the after-effects of the property downturn are more evident, in the form of empty property developments and weak demand. Policymakers find themselves in a difficult position as they look to encourage spending without over-stimulating financial markets.

Technology the clear bright spot

The artificial intelligence (AI) theme dominated the conference, with discussions focussed on China's push to build out its domestic capabilities in the AI supply chain and the many constraints faced by Chinese players due to export restrictions. As the tariff war with the US continues, Chinese companies have been pushed towards domestic alternatives to reduce reliance on imported technology. Spending is rising sharply, albeit from a smaller base than in the US but is constrained to some extent by the inaccessibility of the highest performance compute. Some local players in the semiconductor sector trade at very high valuations, reflecting both scarcity and enthusiasm, but the direction of travel is unmistakable. Many of the public companies which have boosted their AI investments are already seeing improvements as a result.

Alibaba's cloud revenues, for instance, have accelerated from single-digit growth to close to 30% as cloud migrations accelerate and companies execute more AI workloads. With limited access to high-end chips, Tencent has prioritised internal use cases in its profitable gaming division, where AI is improving efficiency and performance in game design. These are tangible productivity gains with visible returns on investment, which appears more like disciplined capital allocation than bubble behaviour.

The power of franchises

Something that stood out from meeting companies and observing life on the ground was the scale of China's leading digital franchises. Platforms such as Tencent, Alibaba, and ByteDance are deeply embedded in daily life. The time people spend within these ecosystems, for communication, payments, shopping, and entertainment, is extraordinary.

These businesses have built dominance over decades. Their challenge now is not reach, but monetisation. For example, Tencent Music is moving from user growth to premiumisation. The average subscriber spends around one dollar a month, and improving that figure will depend on generating incremental value which customers are willing to pay for. This is where the strength of the franchise is so crucial and why we consider it one of our four pillars of Future Quality.

Trip.com is another case in point. It sits at the centre of China's policy drive to boost consumption and domestic tourism, providing a seamless platform for travel and experiences. As services spending recovers, Trip is well placed to benefit. Both companies are largely insulated from global trade tensions and align with China's focus on domestic demand.

Valuation discipline still essential

Some parts of the market—particularly the semiconductor supply chain—look expensive, trading at multiples that are difficult to justify on fundamentals. The large internet platforms, by contrast, appear reasonably valued if their transition into higher-margin, AI-enabled businesses continues. The perennial question is the discount required to compensate regulatory and geopolitical risk. This is a point that investors have clearly been reappraising of late, on relative basis to global markets.

Beyond the numbers

Investing in China involves understanding how policy interacts with business growth. Expansion often requires government approval, and companies have, at times, been known to smooth profit delivery to stay below the political radar. Yet that also presents a degree of predictability which has been absent in other jurisdictions.

Away from the conference, I was struck by how advanced China's infrastructure and technology are. Trains run on time, payments are entirely digital, and the major cities feel highly developed. The categorisation of China as an emerging market doesn't match the reality in many urban areas. There also seems to be a greater openness to visitors, perhaps reflecting an effort to project confidence and attract more tourism. China's attempts at boosting its soft power are becoming evident.

What it means for the Future Quality process

The trip reinforced our conviction that China remains home to companies with genuine Future Quality characteristics and often at a discount to global peers. The economic recovery may be uneven, but within it are strong, domestically focused businesses capable of compounding value over the long term due to idiosyncratic factors, which are appealing candidates for inclusion in our Future Quality portfolios

About the author

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Finn joined Nikko AM (now Amova AM) in February 2022 as an intern, supporting projects in the Global Equity team. He has since continued his stay as a member of the team in an analyst role.

Finn holds a first-class Master's degree in Theoretical Physics from the University of St Andrews and is a CFA® charterholder.



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