The Post-Covid Economy Recovery in China (2023)

January 2023

BAIN & COMPANY

China ended the “Zero-Covid” policy since December 2022

Jan-Apr 2020

Covid-19 outbreak
Wuhan Lockdown

Coronavirus was **first recorded** and Wuhan became the **first the city under strict restrictive measures**

Aug 2021

“Zero-Covid” first mentioned

In response to the wide spread of Delta, China adopted **a new strategy, “Zero-Covid”**

Mar-Jun 2022

Shanghai Lockdown

Omicron widespread in Shanghai and the city responded with **mass PCR testing** and strict **lockdown**

Oct 2022

20th National Party Congress

President Xi **reaffirms** China's **adherence** to “Zero-Covid” policy

Nov 2022

“China’s 20 measures”

Called for **scientific and precise** control, e.g. end identification of close contacts of close contacts

Dec 2022

“10-point plan”
Downgrade Covid to Class B

Relax restrictions and finally end Zero-Covid incl. no longer quarantine for infected, Stop designating high-risk area, remove travel restrictions

Source: Lit research; Bain analysis

China also unveiled plans to accelerate economic growth

- **President Xi** hosted **The Central Economic Work Conference** held in Beijing in December 15-16 2022
- The meeting emphasized that **the economic is expected to pick up in 2023**, and we must **strengthen our confidence in accelerating economic growth**. Below are important growth levers and highlights:

Consumption

- Restoring and growing domestic **consumption** must be given **priority**
- **Local governments** e.g. Beijing, Henan launched multiple measures e.g. coupons to **boost domestic demand**

Real-estate

- Adhere to “housing is for living in, not for speculation”
- Ensure **stable development** of the market supported by **tailored monetary policy** e.g. 16-Point Plan

Private enterprise

- **Unwaveringly support** the private economy
- “*I’ve **always supported** private enterprises; I also worked in places where private economy is developed.” (Xi said)*

Foreign company

- Continue to **attract and utilize** foreign investment with some measures taken e.g. **ease pf market access** in trade, logistics, professional services etc.

Tech company

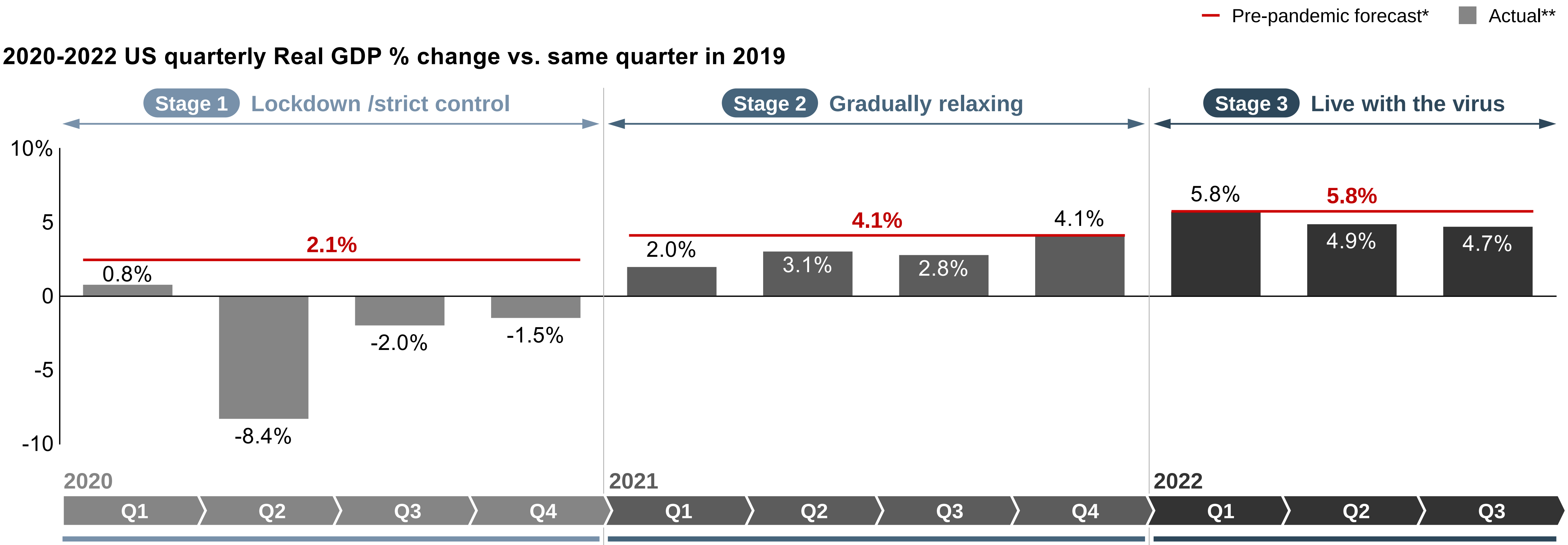
- Accelerate the R&D and promotion of **cutting-edge technologies** e.g. new energy, AI, bio-manufacturing green low-carbon and quantum computing

Platform company

- **Support platform** enterprises in **leading development, job creation and international competition**

Source: Lit research; Bain analysis

US: economy bounced back as the government eased restrictions in 2021Q1



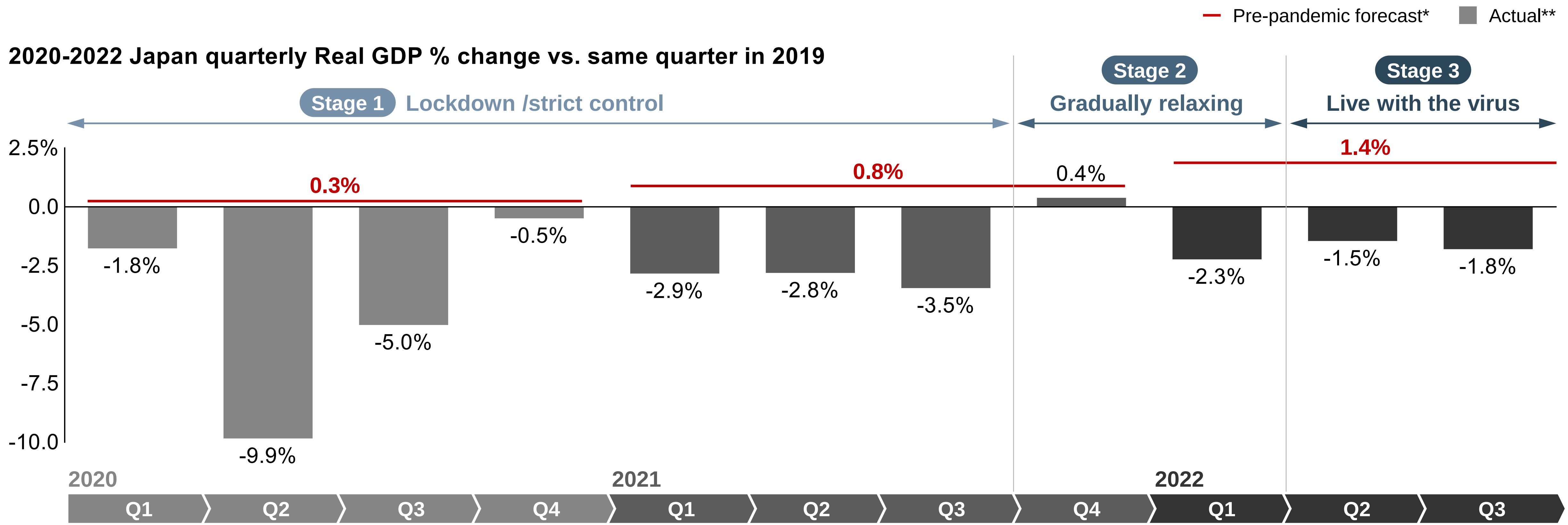
- US citizens were required to follow strict **self-quarantine** and **travel restrictions**

- As vaccination accelerating, the government gradually **eased mask request & travel restrictions**
- Economy mainly driven by **personal consumption** and **fixed investment**

- The government declared "**the pandemic is over**"
- Economy growth **slowed down** as **high inflation**

Note: *Forecasted Real GDP is from December 2019 forecast by HIS; ** Actual real GDP is seasonally adjusted value
Source: IHS Market Macroeconomic Data; OECD; Bain analysis

Japan: economy gradually recovered, but have not reached pre-pandemic level yet due to slow growth in consumption



- The government repeatedly declared the **'State of Emergency' for three times**, and implemented strict control measures;
- **Export,** the major growth driver, bounced back to **pre-pandemic level in 2021** from 2020 slump

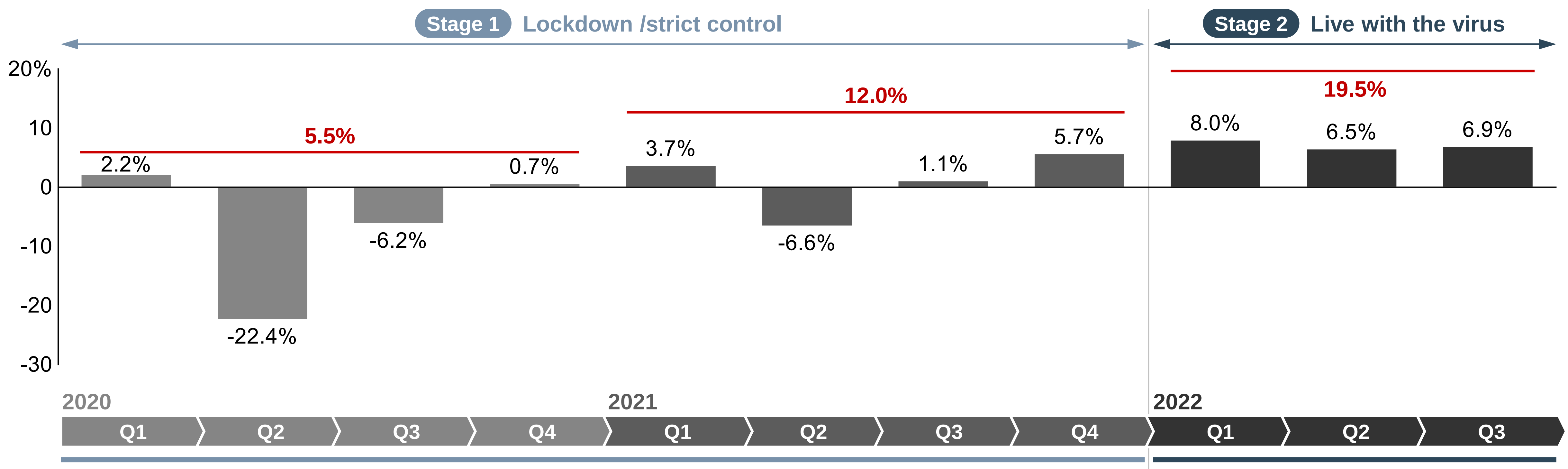
- With high vaccination rate, the government removed 'State of Emergency' , and **started test for relaxing restrictions**

- **Completely lifted** control measures;
- **Consumption and investment** drove growth yet total still **below pre-pandemic**

Note: *Forecasted Real GDP is from December 2019 forecast by IHS, ** Actual real GDP is seasonally adjusted value
Source: IHS Market Macroeconomic Data; OECD; Bain analysis

India: economy bounced back after recovering from Delta wave and the ease of restrictions in Q4 2021

2020-2022 India quarterly Real GDP % change vs. same quarter in 2019



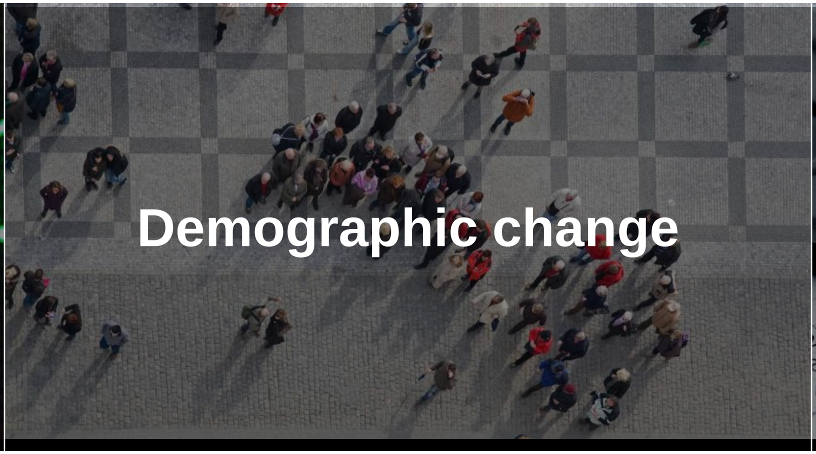
- The government launched several **phases of lockdown** in early stage;
- After relaxing control in late 2020, India got hit by the largest **Delta** wave from Feb 2021, resulting in further **state-wide lockdowns**

- **Completely lifted** lockdowns and restrictions;
- Economy rebounded as **fixed investment** and **consumption** regained momentum

Note: *Forecasted Real GDP is from December 2019 forecast by IHS, ** Actual real GDP is seasonally adjusted value
Source: IHS Market Macroeconomic Data; OECD; Bain analysis

Although there remains certain medium and long-term systemic risks of the Chinese economy...

As China’s economy size grows larger, economic growth will inevitably enter a stage of **slowed down growth**. OECD predicts that China’s GDP yoy growth rate will be **lower than 2% in 2040**, comparable to those of developed countries



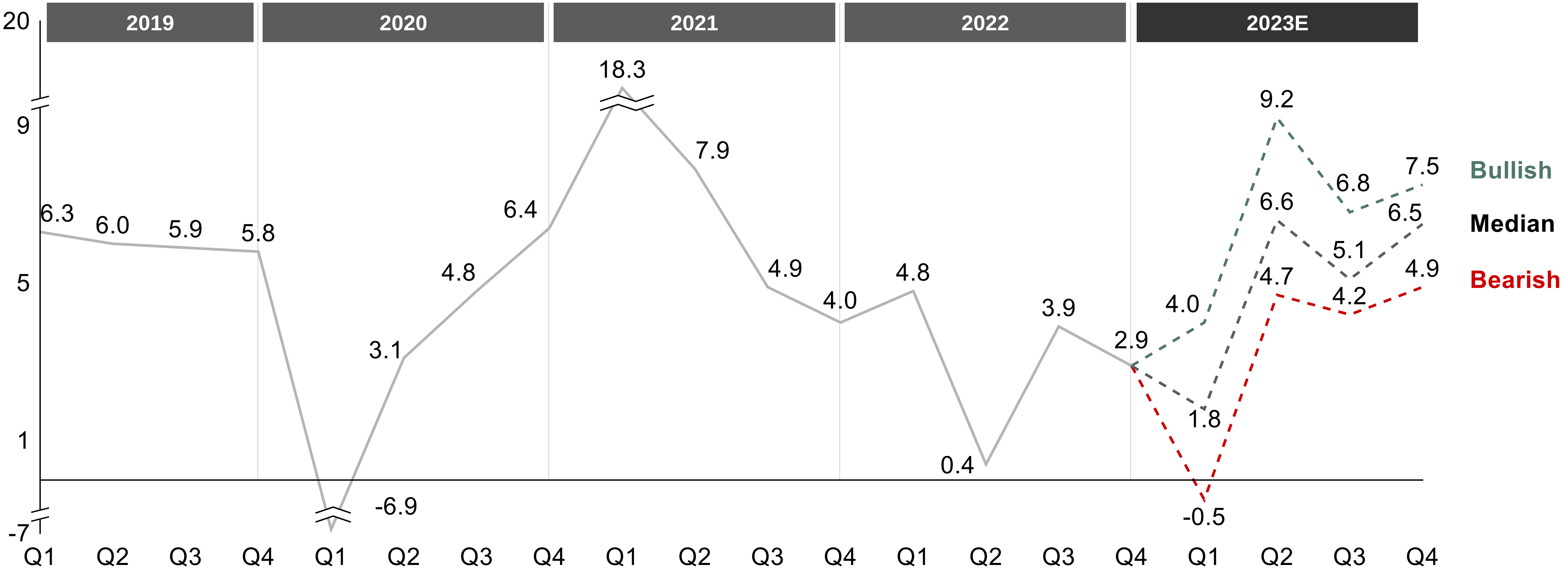
In the past 5 years, **births in China has declined** significantly, while **aging population has continued to increase**. In 2022, births was below 10 million, and the total population experienced **negative growth** for the first time. However, the proportion of the aging population (over 65 years old) has reached **15%**. These will undoubtedly affect China's **labor and consumer markets** in the medium to long term

The past economic development has been fruitful, but at the same time **two foundational problems** remain: one is **the economic growth mode transition**, namely how to achieve sustainable & high-quality development driven by efficiency; the other is the **system reform** issue, rethinking the allocation of market resources

Source: Lit research; Bain analysis

…But in the short-term China's economy is expected to recover

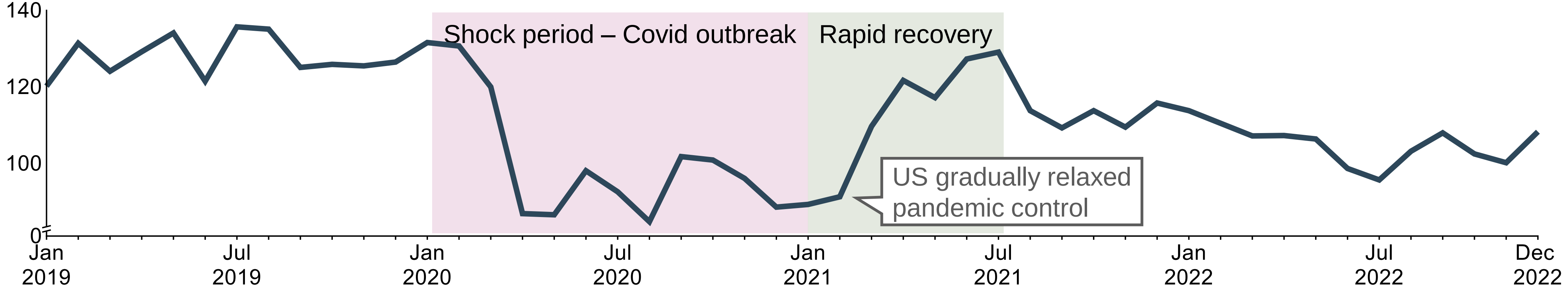
2019-2023E Real GDP growth y-y%



Note: Bullish, median and bearish scenario estimates are based on the synthesis of analyst reports from Morgan Stanley, JPMorgan, UBS, HSBC, CICC, Huatai, Guotai Junan, etc
Source: National Bureau of Statistics of China; Analyst reports; Bain analysis

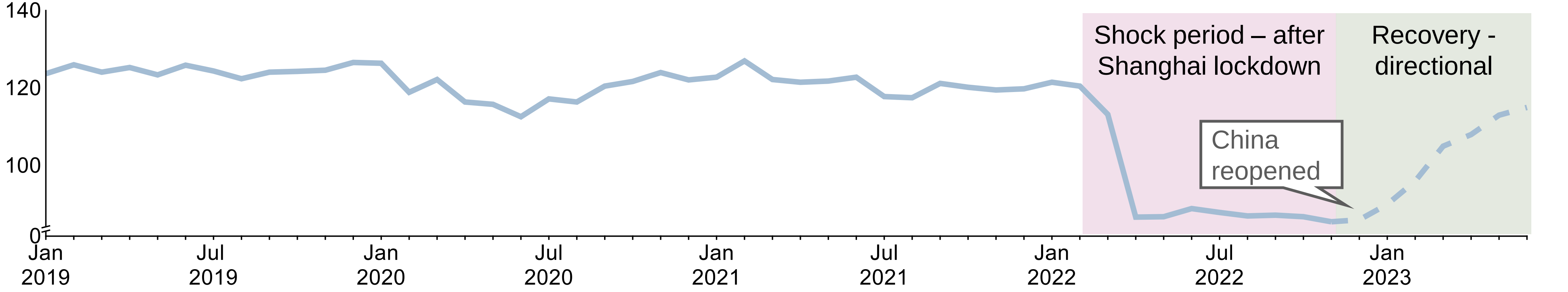
Consumer confidence: China consumer confidence is expected to present a similar trajectory to the US, rebounding from the slump after reopening

US Consumer Confidence Index*, 2019-2022



China Consumer Confidence Index, 2019-2023E**

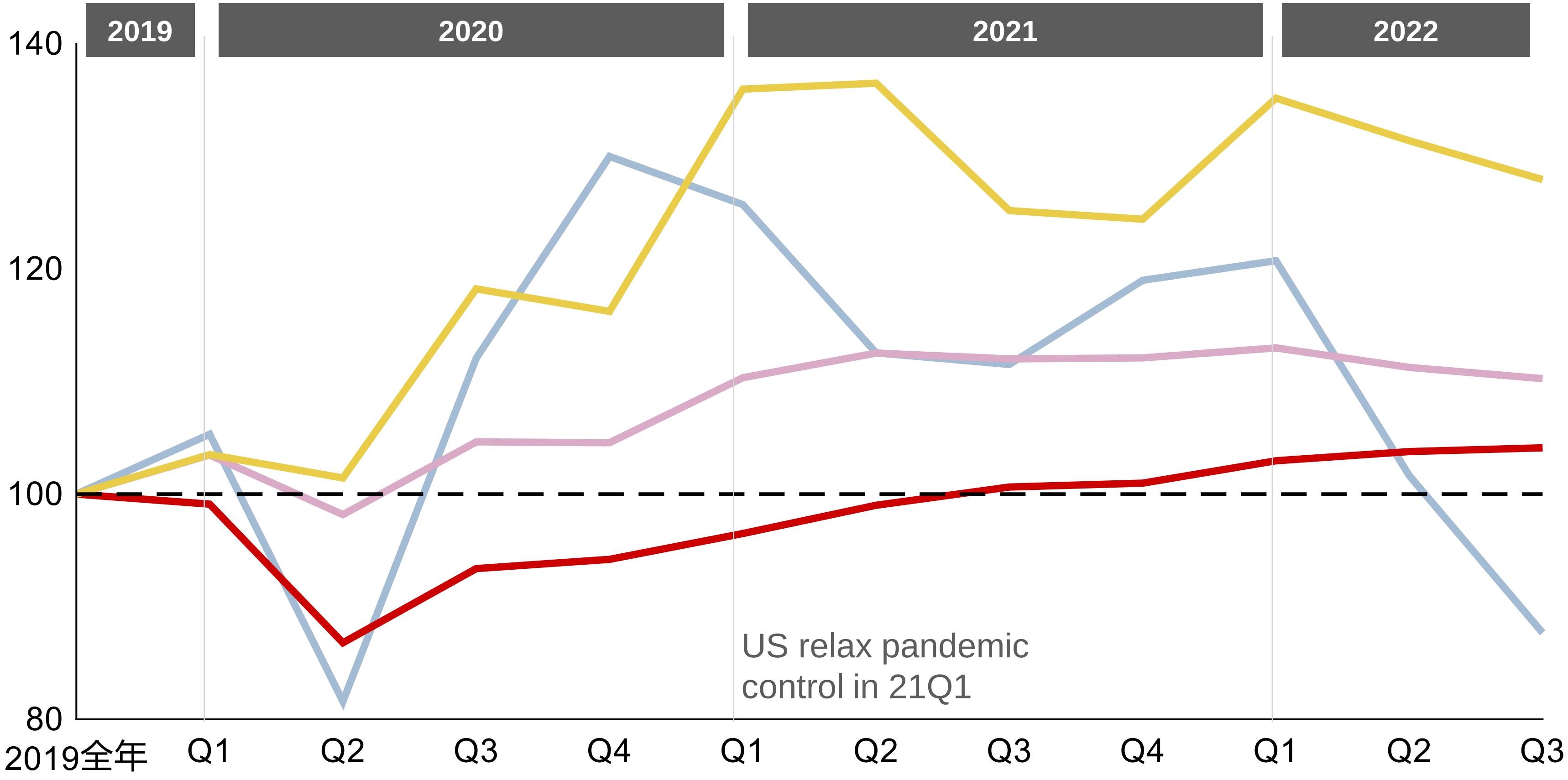
Jan



Note: *The index is issued by the Conference Board and is based on the Consumer Confidence Survey.; ** The China Economic Prosperity Monitoring Center of National Bureau of Statistics is responsible for conducting survey and generating the index
Source: Wind; National Bureau of Statistics of China; Bain analysis

The US: Different consumption sectors showed different recovery trajectories after the first Covid hit in 2020 Q1

2019-2022 US consumer goods, services and properties market change (vs. 2019 same quarter indexed as 100)



- FMCG, durables and services all took personal consumption expensub-categories in GDP as representative indicators; Among them, durables include automobiles, furnishing and durable household equipment, recreational goods and vehicles and others; FMCG using non-durables as proxy, includes food and beverages purchased for off-premises consumption, clothing and footwear, gasoline and other energy goods and others; Services include housing and utilities, health care, transportation, recreation, food services and accommodation, financial services and insurance and others; Properties is represented by existing home sales (about 90% of sales in the U.S. real estate market).
- Source: Wind; U.S. Bureau of Economic Analysis; Bain analysis

Highlights

Durables*

- Rapid growth after Covid driven by **growing in-home** demand; yet **slowed down** after relaxing control

FMCG*

- Less affected vs. services as supported by **essential goods demand** e.g. food and beverages

Services*

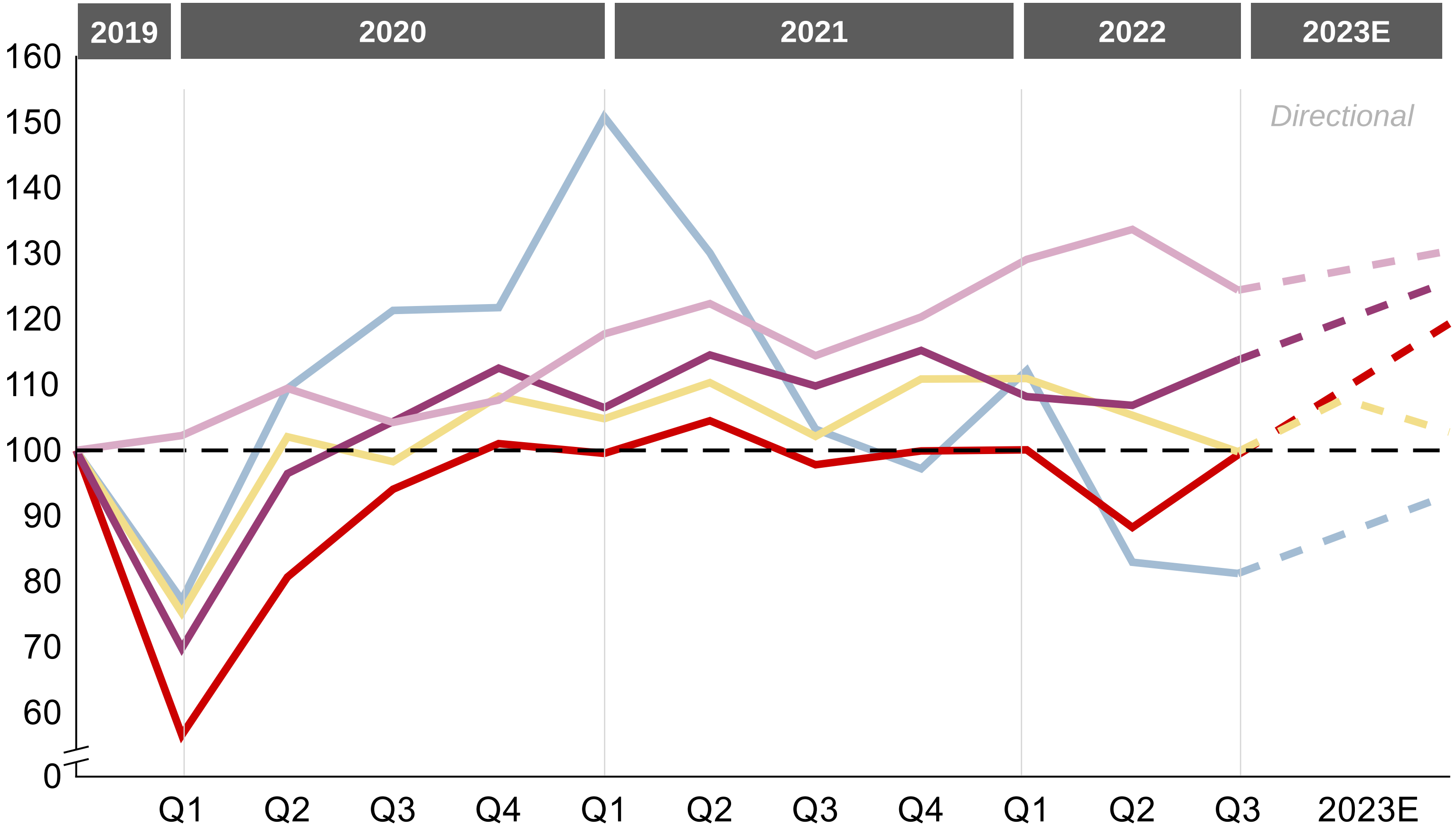
- **Significant drop** after Covid; gradually **recover to pre-pandemic level** after relaxing control

Properties*

- Rapid growth by **favoring fiscal & monetary policy**; **demand declined** as rising interest rate afterwards

China: Different consumption sectors are expected to experience similar recovery trajectories after reopening in 2023

2019-2023E China consumer goods, services and real estate sales change (vs. 2019 same quarter indexed as 100)



Highlights

Services*

- Demand was suppressed in pandemic; **recover quickly** with **social** activities

FMCG* - Essentials

- **Overall moderate growth** yet **stockpiling goods** (household cleaning, ready-to-eat, etc.) are expected to see **growth slow-down**

FMCG* - Non- Essentials

- **Higher growth** esp. in apparel, footwear cosmetics driven by **out-of-home** demand

Real Estate*

- **Recover** gradually by favoring **industry and monetary policy** support

Durables*

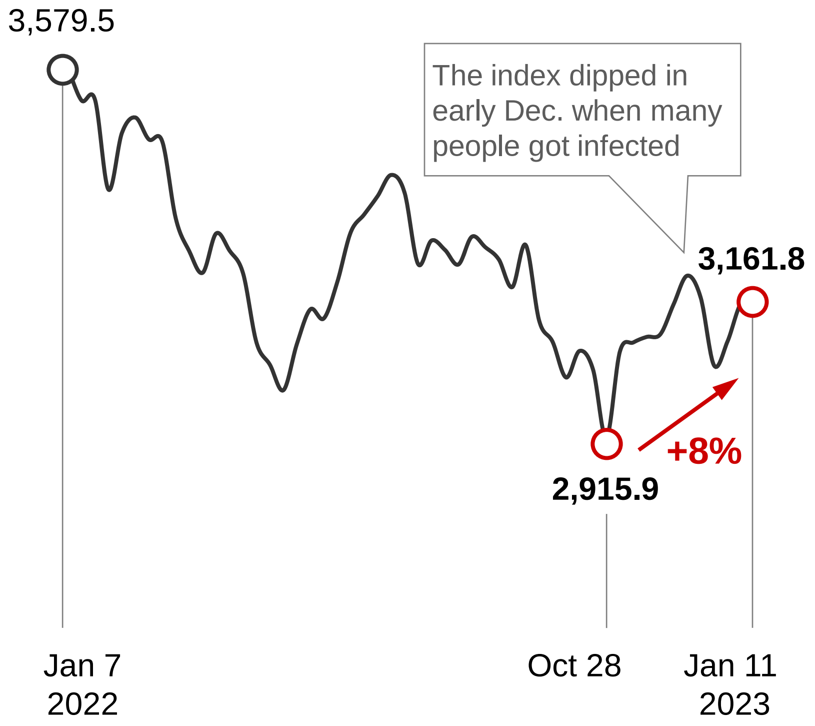
- These categories wi**ll follow property (real estate) recovery**

Note: *FMCG, durables and services Durables all took sub-categories of total retail sales of consumer goods as representative indicators; Among them, durables include home furnishing, home appliances, 3C and others; FMCG – essentials include food, beverage and personal care and others; FMCG – non-essentials include alcohol, beauty, apparel, jewelry and others; Services using catering service as proxy; Real estate using residential housing sales as proxy
Source: National Bureau of Statistics of China; Analyst reports; Bain analysis

Financial investor – public market: stock indices rebounded from November

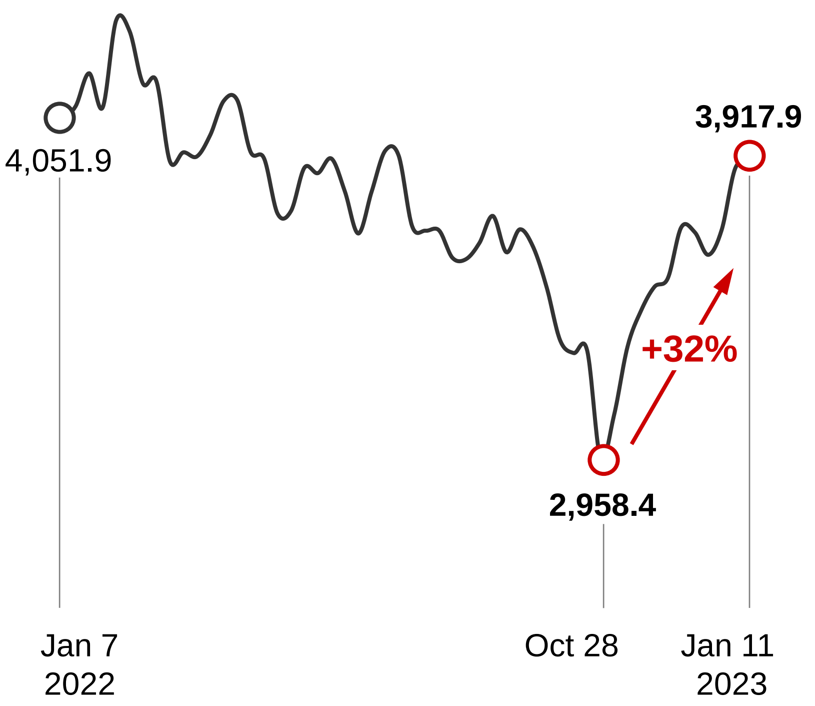
Shanghai Composite Index
(China mainland market)

2022-2023 Jan



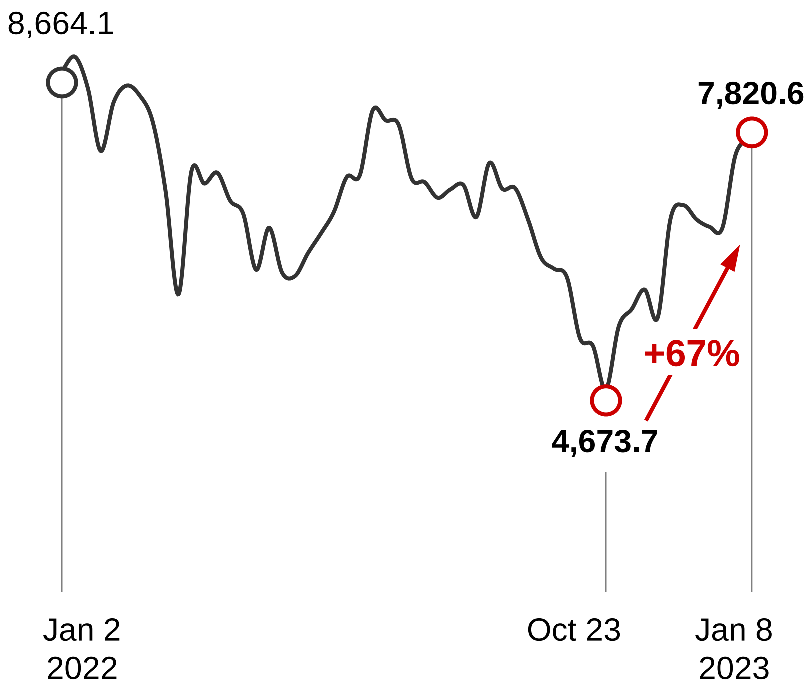
HSCCI
(Hong Kong market)

2022-2023 Jan



Nasdaq Golden Dragon China Index
(US market)

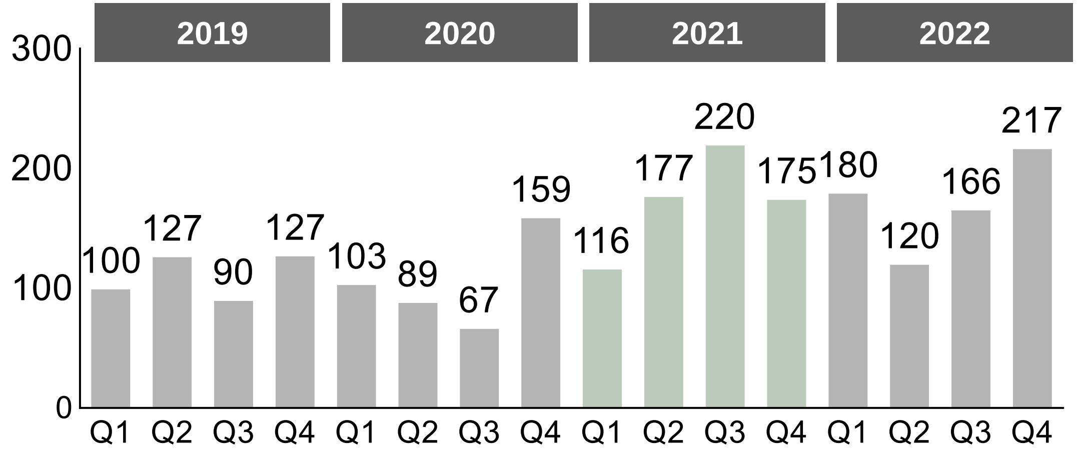
2022-2023 Jan



Note: Shanghai Composite Index is the most important index reflecting status of China mainland stock market; HSCCI refers to Hang Seng China-Affiliated Corporations Index, providing benchmark of "Red Chips", which are Mainland-controlled companies incorporated outside mainland China and listed in Hong Kong; The NASDAQ Golden Dragon China Index is comprised of companies whose common stock is publicly traded in the United States and the majority of whose business is conducted within the People's Republic of China.
Source: Wind; Investing; Bain analysis

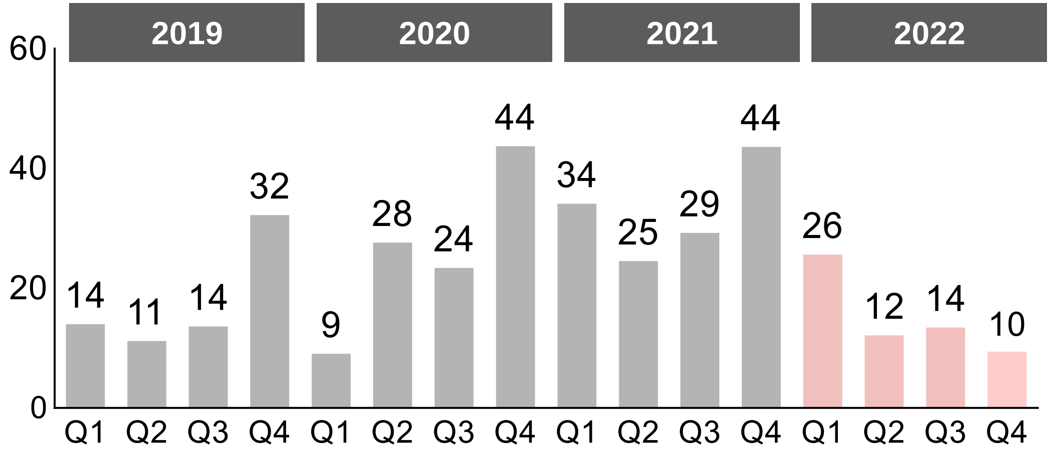
Financial investor – private market: deal value & volume of Chinese PEVC market are expected to rebound gradually after sharp drop in 2022

US PE Deal Value ($B)



yoy growth rate (%)	-5.9%	+64.6%	-0.8%

China PEVC Deal Value* ($B)



yoy growth rate (%)	+46%	+27%	-54%

- US PE market **rebounded after ease of restrictions** in 21Q1 by both **consumption recovery** and **low interest rate**
- However, the market slowed down in 2022 driven by **rising interest rate**, **recession** concern and **regulation on tech** companies

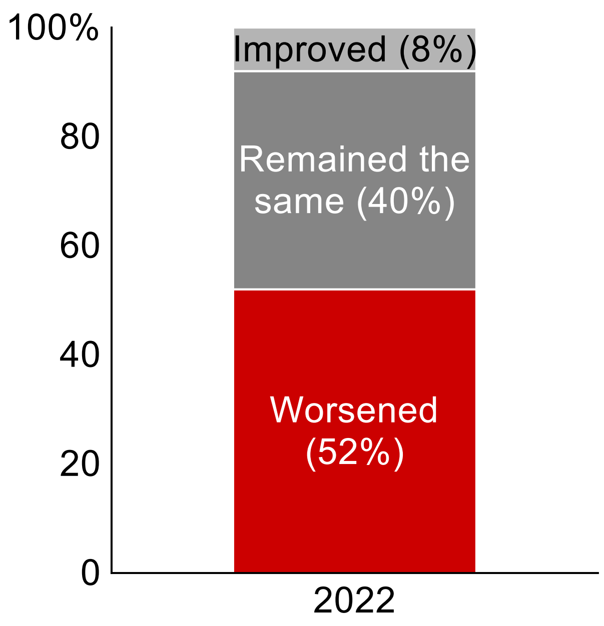
- China PE market **suffered in 2022** by both **concerns on Zero-Covid** and strong **ongoing regulations on platform economy**
- The market is expected to **rebound gradually** driven mainly by the **expected recovery of consumption**, government's **support of private enterprises**, **ease of restrictions for internet platforms**, and **stimulation policies for various sectors**, including "hard technology"
- **Long-term uncertainty** still exits on recovery magnitude

Note: *China PEVC deal value is based deals with deal size >=$10M; Excludes deals in the financing stage of Franchise funding, Seed/R&D, Concept Deals and Distressed; Excludes deals in infrastructure and real estate, large domestic transfers between SWF, govt. deals and abandoned deals
Source: Pitchbook; AVCJ; Lit research; Bain analysis

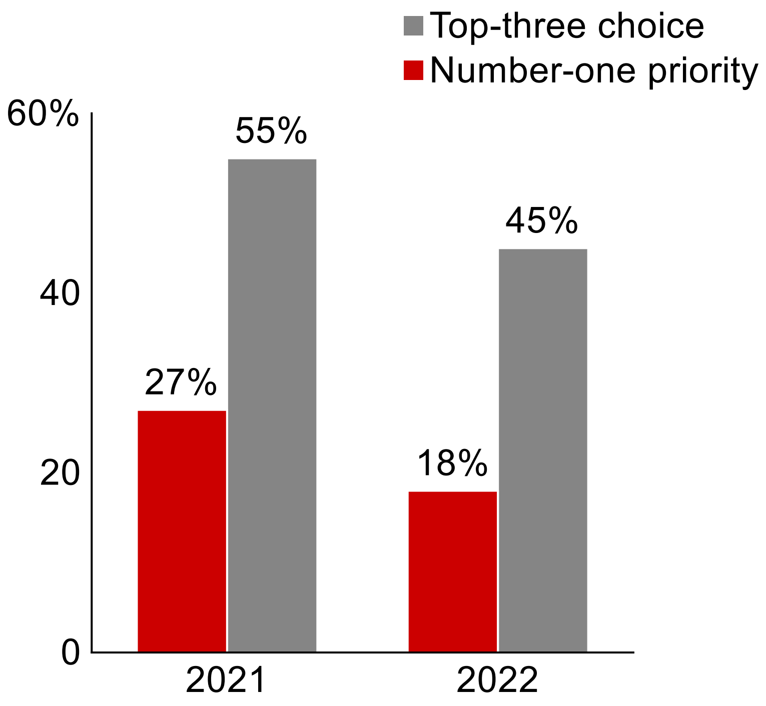
Corporate investor - US: US companies are more likely to be more conservative given the geopolitical complications

The American Chamber of Commerce in Shanghai released a Business Report based on surveys results of **US businesses in China**, reflecting their **opinions and experience** in this market. Key findings of 2022 as below:

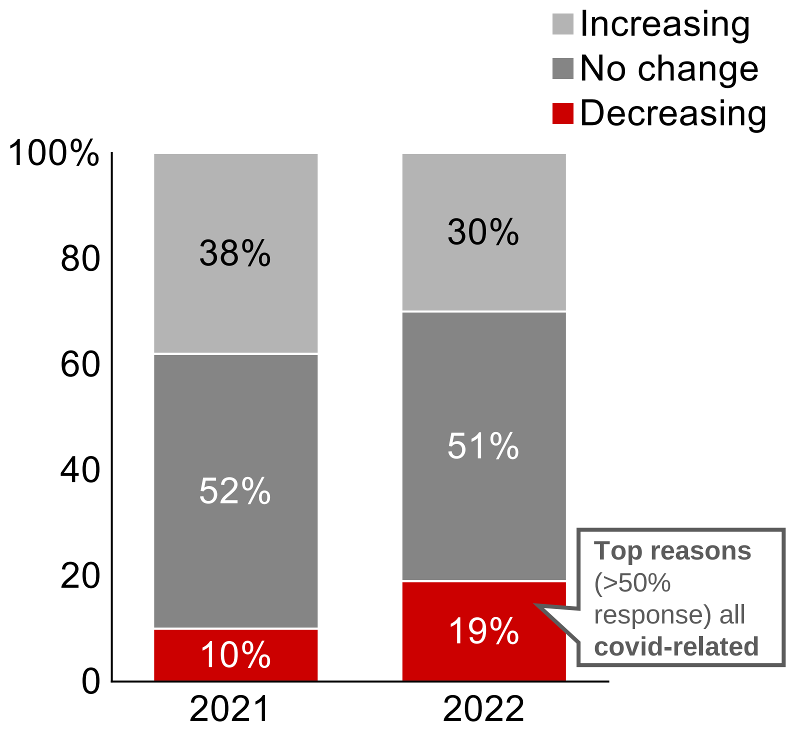
Question: *In the past year, has your global headquarters'* ***confidence*** *changed in China's economic management?*



Question: *How does your global headquarters* ***rank China*** *in your company's global investment plans?*



Question: *How is your company's* ***investment in China changing*** *in 2022 compared to 2021?*

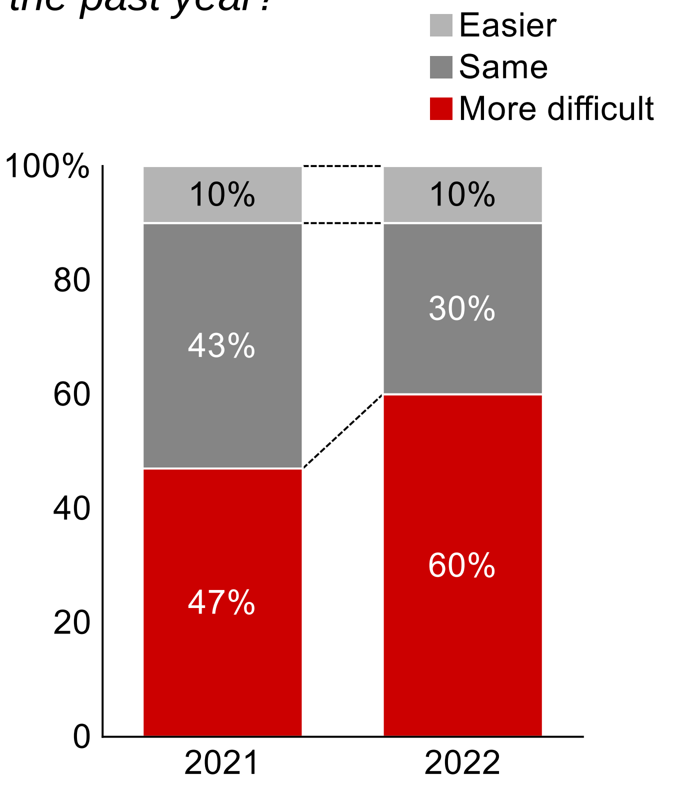


Source: 2022 China Business Report released by the American Chamber of Commerce

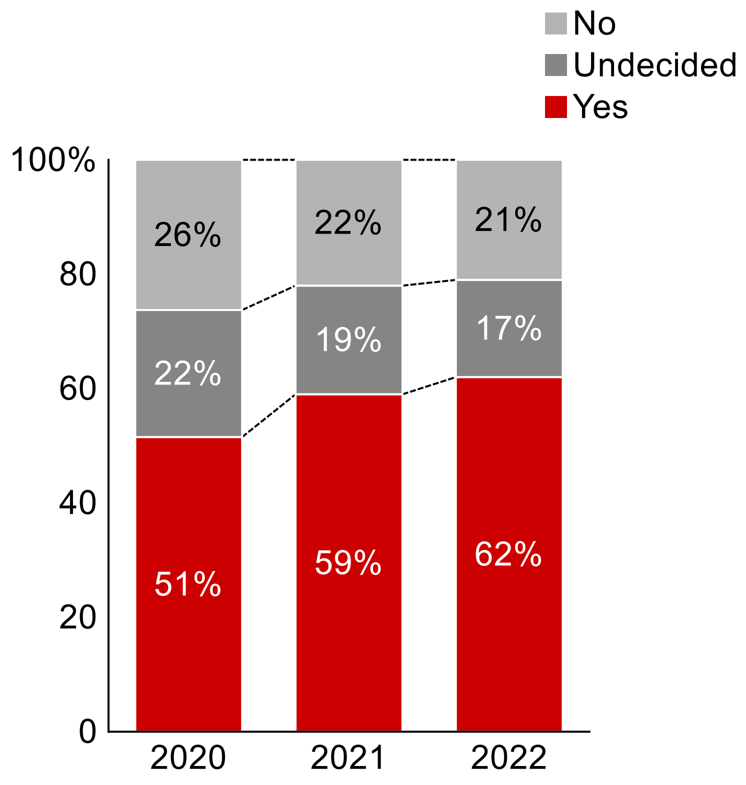
Corporate investor - EU: EU companies maintained willingness to invest in China, despite the challenged operations in 2022

The EU Chamber of Commerce in China released a Business Confidence Survey each year based on surveys results of **EU businesses in China**, reflecting their **opinions and experience** in this market. Key findings of 2022 as below:

Question: *How has your industry's* ***business environment*** *changed over the past year?*



Question: *Is your company considering expanding* ***China operations*** *in 2022?*



"The change of the policy gives us more certainty in operations and supply chain, and will bring much more ***predictability in our operations globally****."*

Frank Hammes, Rolls-Royce China Director

"The sudden end of China's zero-COVID-19 policy is a game changer. German companies will quickly adjust their business operations to the new conditions and will be ***more optimistic thereafter for the year ahead****."*

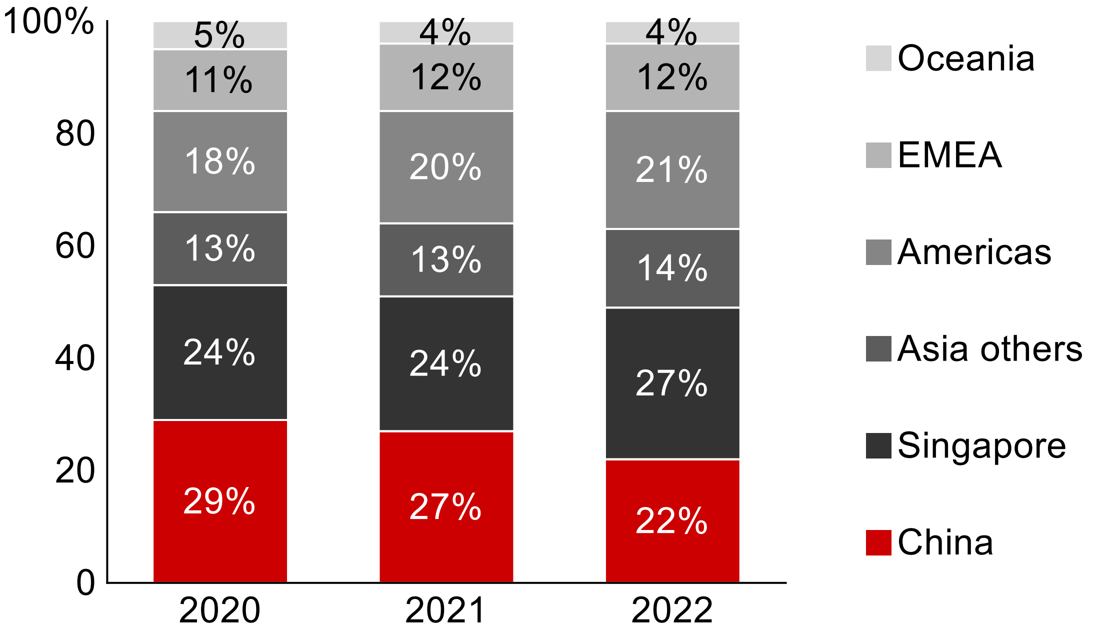
Clas Neumann, Chairperson of German Chamber of Commerce East China

Source: 2022 China Business Confidence Survey released by the EU Chamber of Commerce in China

Corporate investor – Singapore & Middle East: Sovereign wealth funds in these areas are more optimistic with significant portfolio allocation to China market

Singapore leading investor treats China as its top priority in global portfolio

Temasek* AUM by region (as of Mar 2022)



Total AUM** **~500B USD**

Middle East investors view China as an important future growth driver

*"On a geographic basis, we continue to see **China** and India as **key drivers of global growth** in the years to come."*

Hamed bin Zayed al-Nahyan,
Managing Director of ADIA (Abu Dhabi Investment Authority)

*"As some asset owners turn cautious on Chinese assets, **Middle Eastern** funds continue to **increase allocations to the country**, e.g. ADIA likely to deepen its reach."*

*"ADIA's holding of Chinese shares **increased from $300M in 2015 to $1.4B in 2021**."*

Diego Lopez, Managing Director of Global SWF
(platform tracking all global sovereign wealth funds)

* Temasek is a global investment company headquartered in Singapore, ranked top 20 (in terms of AUM size) sovereign wealth fund globally; AUM refers to asset under management
Source: Company official website; Lit research

Three recommendations for companies to accelerate the recovery of China business

China's **market environment and consumer behavior** has changed quite dramatically over the past three years. MNCs should re-examine the Chinese market and competitive landscape, enhance and change their understanding of the Chinese market

China is still **the best consumer story** and **the best global learning ground,** companies need to regain confidence in the Chinese market

With the **renewed market knowledge** and **proper scenario planning**, MNCs could consider seizing the development opportunities in the dynamic situation, **re-committing their investments** to China, creating a second growth engine, and achieving long-term sustainable development

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