

China Outlook 2026: Navigating the Year of the Fire Horse

Five reasons to be bullish on China (and one key risk to be aware of)

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Improving earnings, an ongoing economic transformation and benign valuations all add up to a positive outlook for the year ahead.

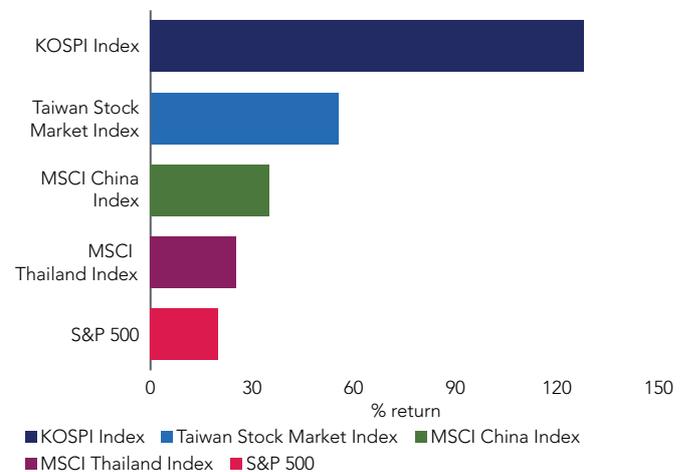
As we celebrate Chinese New Year and welcome the Year of the Fire Horse, it feels like the right moment to step back and think about where China stands, not just as an investment destination, but as a market going through one of the most important transitions in its modern economic history. The past few years have been unpredictable for investors, frustrating at times, and occasionally downright baffling. But 2026 is shaping up differently. There are unmistakable signs of stabilisation, policy clarity is improving, and we're beginning to see pockets of genuine long term opportunity emerging. In other words: this is still a complicated market, but it's no longer a hopeless one.

Let's walk through what feels most important as we head into this new cycle.

1. Where we are seeing opportunity — and why valuations still matter

If you felt uneasy watching Chinese equities in 2025, you weren't alone. Market performance was extraordinarily divergent. Anything connected to AI hardware, semiconductors, or healthcare seemed to levitate almost effortlessly, while many other areas felt stuck in the mud. Financials benefited from aggressive policy easing, mortgage relief and substantial state backed capital support, which helped stabilise balance sheets and drove a strong rebound in sentiment across banks and insurers.

Figure 1: Index returns: leaders and runners up



Source: Bloomberg, total returns in US\$ between 2 January 2025 and 10 February 2026. **Past performance is not a reliable indicator of future performance.**

On the growth side, the winners were clear:

- China's push to build a domestic semiconductor ecosystem is gaining traction.
- AI infrastructure spending is still in its early innings.
- Healthcare continued to move up the value chain, becoming more globally competitive.
- Policy support, capital injections and mortgage relief improved sentiment toward banks.

The challenge, of course, is that markets have already rewarded these trends. Fundamentals are solid, but valuations in these pockets have become undeniably optimistic.

Where we're finding more interesting opportunities is almost the opposite end of the spectrum: the areas the market largely ignored last year. High quality yield names, utilities, cyclicals and select consumer franchises all offer a mix of stability, dividends and earnings that appear close to bottoming. Their valuations simply haven't caught up with their fundamentals.



Valuations: What's cheap and what's not?

Asia ex-Japan index valuations

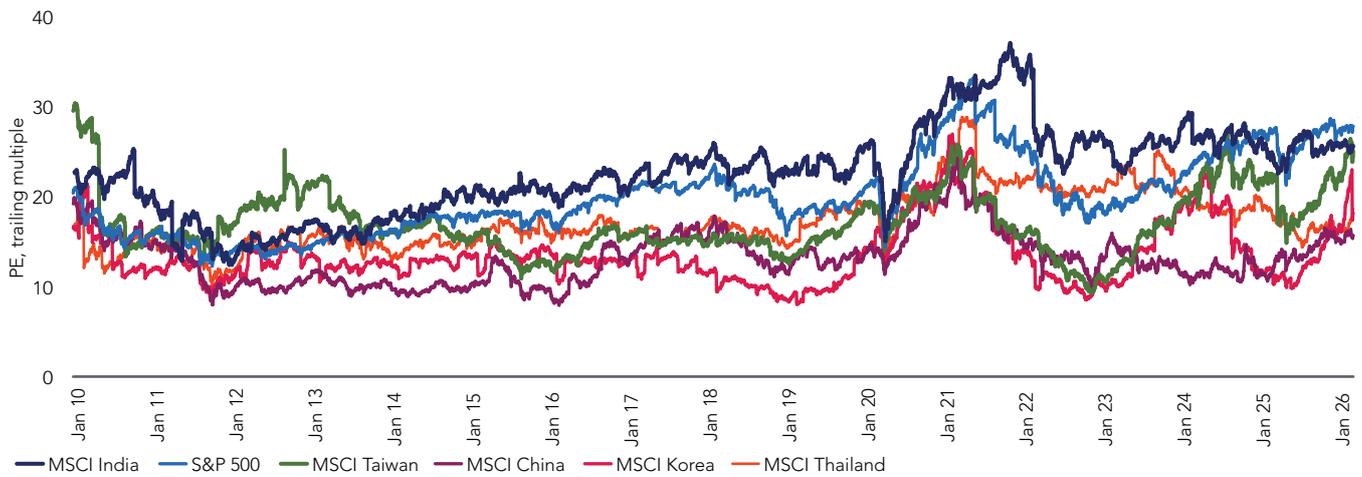
Here's the honest, simple picture:

- **Relative to its own history**, China is not expensive. MSCI China trades on a forward P/E of around 12.6X — only slightly above its long term average, even after a meaningful 2025 rally.
- **Relative to Asia**, China remains one of the cheaper large markets. Korea and Taiwan — last year's AI/semiconductor favourites — saw significant re ratings, though Korea still sits below its historical average.

- **Relative to developed markets**, China is outright cheap. Global portfolios remain heavily underweight, creating an asymmetry: it wouldn't take much for sentiment or flows to turn meaningfully.

You can feel this in client conversations. No one is euphoric about China, but the despair of 2023 and early 2024 has faded. Investors have stopped calling China "uninvestable". Expectations are low. Valuations are fair. And that combination is often the starting point for the best investment stories.

Figure 2: Headroom for China and South Korea?

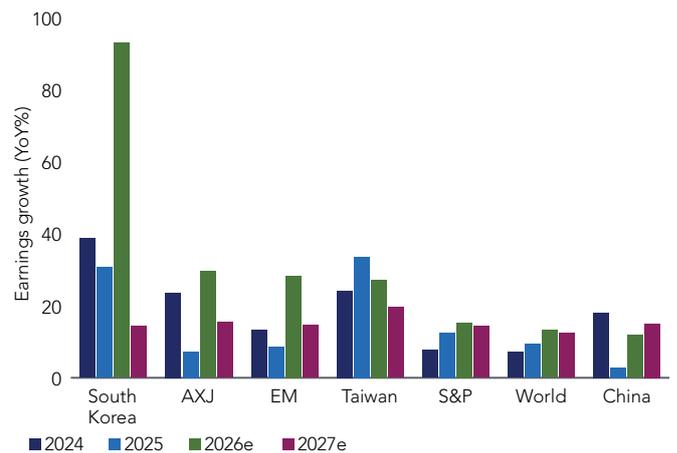


Source: Bloomberg as of 31 December 2025. **Past performance is not a reliable indicator of future performance.**

2. Earnings: A quietly improving story

One of the most encouraging shifts heading into 2026 is the stabilisation and in some cases, recovery of earnings. For the broader market, consensus now points to a mid teens earnings rebound, led by consumer facing sectors where competition has rationalised, margins have recovered and market structure looks healthier. Importantly, this recovery doesn't rely on heroic GDP assumptions. It reflects companies resetting, cutting wasteful price wars, and operating in a more realistic environment.

Figure 3: Asia and EM forecast to drive earnings growth in 2026



Source: Bloomberg, in US\$, as of January 2026. Based on calendar year earnings growth. Forecasts cannot be guaranteed. **Past performance is not a reliable indicator of future performance.**



How does this compare with the rest of Asia?

- **South Korea and Taiwan** still look strong, but expectations are normalising after a white hot year fuelled by AI capex and semiconductor demand.
- **India** is poised for better numbers this year, but valuations are so stretched that the earnings to valuation trade off is simply less compelling.

This is one of the rare moments where China sits in the sweet spot: **solid earnings recovery + reasonable valuations**, while several peers offer either growth without value, or value without growth.

3. The Policy backdrop: Property, consumers, and the long view

If you follow China, you know the policy narrative can move markets as much as earnings. The encouraging news is that 2026 looks more predictable than recent years.

Property: Slowly becoming less of a problem

No one expects a property “recovery”: that ship has sailed. But we are seeing the contours of a *managed, orderly adjustment*. Mortgage rates are down. Some inventory is being purchased by local governments (albeit in modest amounts). The sector is shrinking as a share of GDP, and that’s healthy. The key risk now isn’t collapse; it’s the lingering drag on sentiment and household spending. And even that drag is better understood than before.

The Consumer: helped, but not transformed

Beijing continues trying to support consumption through subsidies and incentives. But the simple truth is that households won’t replace cars or appliances annually just because they’re subsidised. These measures help, but their impact fades quickly. Early evidence is already visible in softer auto and smartphone shipments. Consumer confidence remains the missing ingredient but not an impossible one to recover, especially if income growth and job stability improve.

4. The 15th Five Year Plan: Where China wants to go

Perhaps the most important long term signal for investors comes from the next Five Year Plan. The priorities are becoming clear:

- **Technological self reliance** (AI, semiconductors, digital infrastructure)
- **Green energy and advanced manufacturing** (a move away from low end exports)
- **Stronger domestic consumption** (better social safety nets, more disposable income)
- **A deeper, more efficient “unified national market”**
- **Breaking dependence on traditional property led growth**

There is a noticeable shift from chasing growth at all costs to prioritising *quality, resilience, and productivity*. That’s not the China of a decade ago and it’s not meant to be.

One area worth highlighting is exports. China is quietly expanding its presence in non traditional markets, including ASEAN, Africa, Latin America, and the Middle East. At the same time, tensions with Western economies have eased off from their most acute levels. It’s not a return to the old world, but it is a less adversarial environment.

5. The Risks: What keeps us awake at night?

Of course, no China outlook is complete without addressing risk honestly.

Property – Less dangerous than before, but still a drag. Something to monitor, not something to fear.

Geopolitics – A background risk but one that feels cyclically quieter than in prior years.

Regulatory confidence (The Big One) – This remains the single most important swing factor for market sentiment. Investors can live with slower growth, changing export patterns, and even geopolitical noise. What they struggle with is unpredictable policy. Surprise regulatory actions, whether in tech, solar, online travel or taxation, can undo months of rebuilding confidence. The positive news is that policymakers seem more aware of this now. But it remains the variable we watch most closely.

Final thoughts: Why the Fire Horse year feels different

There’s something fitting about moving into the Year of the Fire Horse. It’s a symbol of strength, transformation, and forward momentum and China’s market feels like it’s slowly moving back toward those qualities. No one is pretending the old hyper growth model is returning; it isn’t. But that doesn’t make China un-investable, far from it. The economy is evolving into something more balanced, more sustainable, and more innovation led. Earnings are improving, valuations remain supportive, policy direction is clearer, and sentiment, while still cautious, is no longer anchored in despair. For patient investors, that combination can be genuinely powerful.

What makes this moment even more compelling is the nature of China’s market itself. It remains broad, inefficient, and heavily sentiment driven, characteristics that often frustrate benchmark oriented investors but create fertile ground for stock pickers. While many global indices hover near all time highs, China still trades well below its 2021 peak, offering a differentiated and meaningful opportunity set. As the first three years of our China Strategy have shown, a contrarian, bottom up approach that targets mispriced companies across the quality spectrum can thrive in this environment.

With the outlook improving and dispersion likely to remain high, we believe this remains an exceptionally favourable landscape for active investors to uncover value and capture long term growth.

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