RBC China Equity Fund

Commentary as at December 31, 2023

China's stock market was among Asia's worst-performing in 2023 as plunging property prices made it clear that the country's reliance on residential real estate was over and that this engine of economic growth would be difficult to replace. The economy was also hurt by falling foreign investment as companies in the West questioned whether China was still a safe place to invest.

The Real Estate sector, which until recently accounted for 30 percent of China's economic growth, was characterized by the August bankruptcy filing of Evergrande, once the country's second-largest builder. The company, saddled with at least US$300 billion of debt, stoked concern that a liquidation would introduce massive amounts of inventory to the housing market. Meanwhile, U.S. companies increasingly shifted manufacturing from China, the world's second-largest economy, to Mexico, Vietnam, and other emerging markets.

Sector allocation had a negative impact on the Fund's relative returns due to underweight positions in the Energy and overweight positions in Real Estate. This impact of this positioning was offset by the positive impact of an underweight allocation to the Consumer Staples sector. Returns were aided by strong security selection in the Information Technology and Health Care sectors, offset by weaker security selection in Financials.

Holdings that contributed the most to the Fund's performance were CSPC Innovation Pharmaceutical, with its pipeline of experimental treatments for cancer and asthma. Shenyang Xingqi Pharmaceutical, which focuses on eye medications, also performed well, having attained approval for eye drops that delay the progression of shortsightedness in children.

Stocks that limited returns include China Merchants Bank, as investors were concerned about exposure to property and rising non-performing loans. Contemporary Amperex Technology, the world's largest lithium battery maker, also held back performance as falling prices reduced profit margins.

The product manager expects China's economic growth to slow to 4.8% in 2024 from 5.2% in 2023, even with further policy easing. Weakening economic data suggests that policymakers will extend efforts to keep growth from falling further. Expectations for the Chinese economy remain low, and a stabilization in growth above the 4.5% level could renew interest in Chinese stocks, which trade at valuations that are attractive based on history. Other steps that the Chinese government can take to further support jobs and the economy include, paying for the completion of stalled housing projects and boosting spending on infrastructure.