Prescient
CHINA

PRESCIENT CHINA QUARTERLY COMMENTARY

2025 Q2

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RECIPROCAL REALITY

The second quarter of 2025 was among the most consequential in recent memory. It opened with President Trump's unexpected announcement of "reciprocal" tariffs on global trade, which rapidly escalated into a focused trade war with China. Tariffs between the U.S. and China surged by 125% on both sides before bilateral talks in Geneva resulted in a partial rollback of 115%. As of this writing, baseline tariffs on Chinese imports into the U.S. remain at 30%, while U.S. goods entering China face a 10% tariff. We will continue to assess the broader implications of Trump's trade strategy in this quarter's analysis.

Equity markets in both China and the U.S. experienced heightened volatility. After sharp drawdowns in April, indices recovered to post positive quarterly returns. The onshore CSI 300 Total Return (TR) Index returned 3.49% in USD. Offshore benchmarks—the MSCI China TR Index and the Hang Seng China Enterprises (HSCE) TR Index—returned 2.01% and 2.45% in USD, respectively. In the U.S., equity markets rallied strongly following the global pause in tariff escalation and the temporary U.S.-China truce. The S&P 500 TR Index delivered a 10.94% return for the quarter, reversing first-quarter losses and bringing year-to-date returns back into positive territory.

Prescient China strategies extended their strong performance. The Prescient China Equity Fund, focused on onshore A-shares, outperformed the CSI 300 TR Index by 1.24% after fees, delivering a 4.73% return in USD for the quarter. Year-to-date, the strategy has returned 5.44% in USD net of fees, outperforming its benchmark by 2.28%. Meanwhile, the Prescient China Balanced Fund, our multi-asset flexible solution, returned 3.88% in USD for the quarter and is up 7.63% year-to-date—exceeding its China CPI+3% benchmark by 8.29% over six months.

With U.S. policy direction increasingly uncertain under the Trump administration, global markets remain in uncharted waters. China continues to offer the best diversification benefits within global portfolios, but the current environment underscores the importance of disciplined risk management and robust portfolio construction.

TRUMP'S "DEALS"

RATIONALITY PREVAILS?

The first half of April 2025 saw some of the most pronounced volatility in recent memory across Chinese markets—mirrored by similarly sharp dislocations in US equity and fixed income markets. Investor sentiment shifted materially when President Trump reversed course on his initial "reciprocal" tariff strategy, announcing a 90-day pause and implementing a blanket 10% interim tariff. Markets responded with a notable relief rally.

The quarter's most constructive development came in early May, when US and Chinese representatives reached a breakthrough in Geneva, agreeing to roll back 115% of the tit-for-tat tariff increases with effect from 14 May. Both sides committed to continued dialogue under a reduced and more manageable 10% tariff framework. This announcement was particularly significant for China-focused asset managers like ourselves. It demonstrated two key points:

1. The Trump administration—despite its confrontational rhetoric and social media posture—may be more pragmatic than commonly perceived. This is a constructive signal for the United States and for global markets.
2. The US no longer holds the same degree of leverage in Trade War 2.0 with China as it did during Trump's first term. Notably, the Geneva meetings took place at the urging of the US trade negotiation team.

The return of rational diplomacy from the world's most powerful office provided a clear sense of relief for markets. For China in particular, the outcome may be viewed as a modest tactical gain, but more importantly, it delivered a significant boost to investor confidence and policy credibility.

PERSISTENT DEADLOCK

The interim 10% tariff rates have meaningfully lowered trade barriers and helped stabilise global markets. However, with the 12 August expiry date approaching, a permanent agreement remains elusive. Although both sides resumed trade negotiations in London on 9–10 June, little progress appears to have been made, despite triumphalist claims on Truth Social of "amazing DEALS". In reality, the talks likely ended in continued deadlock.

Between the Geneva and London discussions, and seemingly frustrated by limited access to rare earth minerals, President Trump introduced a series of additional restrictions targeting China. These included:

- New US Commerce Department guidance suggesting that the use of Huawei's AI chips "anywhere in the world" could violate US export controls;
- A ban on the sale of US jet engine components and related technology to China;
- Restrictions on exports of electronic design automation (EDA) software used in the development of advanced AI chips;
- A plan announced by Secretary of State Marco Rubio to begin "aggressively" revoking visas for Chinese students.

As of early July, most of these measures have been reversed, coinciding with signs that China has resumed approvals for the export of rare earth minerals to the US for civilian use.

With respect to the broader trade negotiations, the only tangible outcome thus far is a basic framework for continued talks. While modest, having a structure in place is preferable to none, and we remain cautiously optimistic that both sides can find a politically viable path toward further tariff reductions.

RARE EARTHS

What are rare earth minerals, and why is the Trump administration so concerned about limited access? Without delving into technical specifics beyond our remit, rare earth minerals are essential inputs in the manufacture of a wide range of advanced technologies—including consumer electronics, semiconductors, electric vehicles (EVs), medical devices, aircraft engines, and military systems such as fighter jets, missile guidance systems, and radar platforms.

In 2024, China was estimated to account for approximately 69% of global rare earth ore production. More critically, it controlled around 90% of the world's rare earth processing capacity. While numerous announcements have been made regarding new investments into non-Chinese processing infrastructure, any substantive shift in the global supply chain will likely take years if not decades to materialise.

Going forward, we expect Chinese authorities to apply heightened scrutiny to US buyers, particularly around declared end-use applications. Automotive manufacturers such as Ford and General Motors are unlikely to face major obstacles in securing the necessary inputs for EV production. However, any firm with perceived or direct ties to the US defence sector may encounter significant challenges in obtaining rare earth exports from China at commercial volumes.

CAUTIOUS OPTIMISM

Following the 115% rollback in "reciprocal" tariffs, the minimum additional tariffs on Chinese imports into the US remain at 30%, a level established under the Trump administration. When factoring in legacy tariffs from the Biden era, which averaged between 20–25%, the effective tariff burden on Chinese goods entering the US now stands at approximately 50–55%.

The Chinese Yuan (CNY) has appreciated by only around 2% against the US dollar year-to-date. Should it follow the path of other Asian currencies this year, further depreciation could amplify cost pressures for American importers. In our view, the sustainability of current tariff levels is increasingly questionable, particularly if there is any serious consideration given to the inflationary consequences for the US domestic economy.

Recent full-year earnings reports from major US retailers leave little doubt: rising input costs will, inevitably, need to be passed on to consumers. The lagged impact of tariffs on inflation and consumption may become more evident as we progress through the second half of the year.

Figure 1

Retailer	FY end	Net Income Margin
Walmart (WMT.US)	Jan 2025	3.0%
Costco (COST.US)	Sep 2024	2.9%
Target (TGT.US)	Feb 2025	3.8%

Sources: Prescient, Bloomberg (as at July 2025)

Figure 1 highlights that Target's net margin of 3.8% is the highest among the major US retailers listed. This underscores the limited capacity for any of America's retail giants to fully absorb the 30% additional tariffs currently in place compared to pre-January 2025 levels. Given the high proportion of Chinese-sourced goods in their supply chains, attempts to cross-subsidise will likely have a material impact on earnings. This does not even take into account the tariffs of up to 40% imposed on certain countries under new tariff letters issued by the Trump administration in early July.

The direct impact on CPI may remain limited in the short term, as the index is structurally weighted towards categories such as shelter, transportation, energy, and services like healthcare and education. However, with the US mid-term elections approaching in 2026, Republicans will have strong political incentives to shield their middle and lower-income voter base from rising prices, particularly for everyday goods.

As a result, we see a low likelihood of tariffs increasing further in the near term. With the "back-to-school" shopping season in August and September, followed by Thanksgiving in November and the Christmas season in December, the political cost of triggering a spike in consumer prices would be significant. It is also worth noting that major retailers typically place large-volume orders at least three months in advance. Accordingly, we expect intensified lobbying efforts in Washington aimed at reducing tariffs as the retail calendar ramps up in the second half of the year.

CHINA'S PERSPECTIVE

DEAL OR COERCION?

If one were to follow only President Trump's Truth Social posts, one might be forgiven for believing he had secured some of the most significant "deals" of the century. According to him, he has been "Mr. NICE GUY" for China, having supposedly saved the country from "a very bad situation" by brokering the Geneva tariff reduction agreement. In reality, however, President Trump appears to be facing a growing credibility challenge in financial markets. After initial bouts of extreme volatility and subsequent buying frenzy in April triggered by his "reciprocal" tariff announcements and abrupt pause, markets now seem increasingly sceptical. The frequency of policy reversals has led to diminishing market sensitivity to Trump's rhetoric, particularly when it relates to trade "deals", which now appear to be heavily discounted by investors.

The trade "deal" announced with the UK in June, for example, offered limited concessions and was arguably more symbolic than substantive. The original 10% "reciprocal" tariff on UK exports to the US remained in place. Tariffs on automobiles were reduced from 25% to 10%, but only for a quota of 100,000 vehicles—barely covering the 102,000 cars the UK exported to the US in 2024, according to the Society of Motor Manufacturers and Traders (SMMT). Tariffs of 25% on UK steel and aluminium exports were left unchanged. In exchange, the UK agreed to eliminate a 19% tariff on US ethanol and a 20% tariff on US beef, while also introducing import quotas. In sum, the US secured tariff relief for its exports, while UK goods continue to face significant barriers, particularly in industrial sectors. A rather one-sided deal by any measure.

Vietnam, a country where exports to the US make up roughly 30% of its annual GDP, became the second country to reach a "deal" with the US. In early July, Trump announced an agreement under which Vietnam would eliminate all tariffs and non-tariff barriers on US imports. In return, the US would reduce its tariff on Vietnamese exports from 46% to 20%. However, any goods deemed to be "trans-shipped", likely targeting goods originating from China, would be subject to a punitive 40% tariff. The enforcement of trans-shipment controls will be operationally complex and the definition of such "trans-shipped" goods will be very sensitive politically, potentially escalating the China-US trade tensions further. Regardless, a 20% blanket tariff places Vietnam in a materially worse position than before. This, too, appears to benefit the US disproportionately. For Vietnam, the question remains: is this truly a "deal" or simply the result of economic coercion?

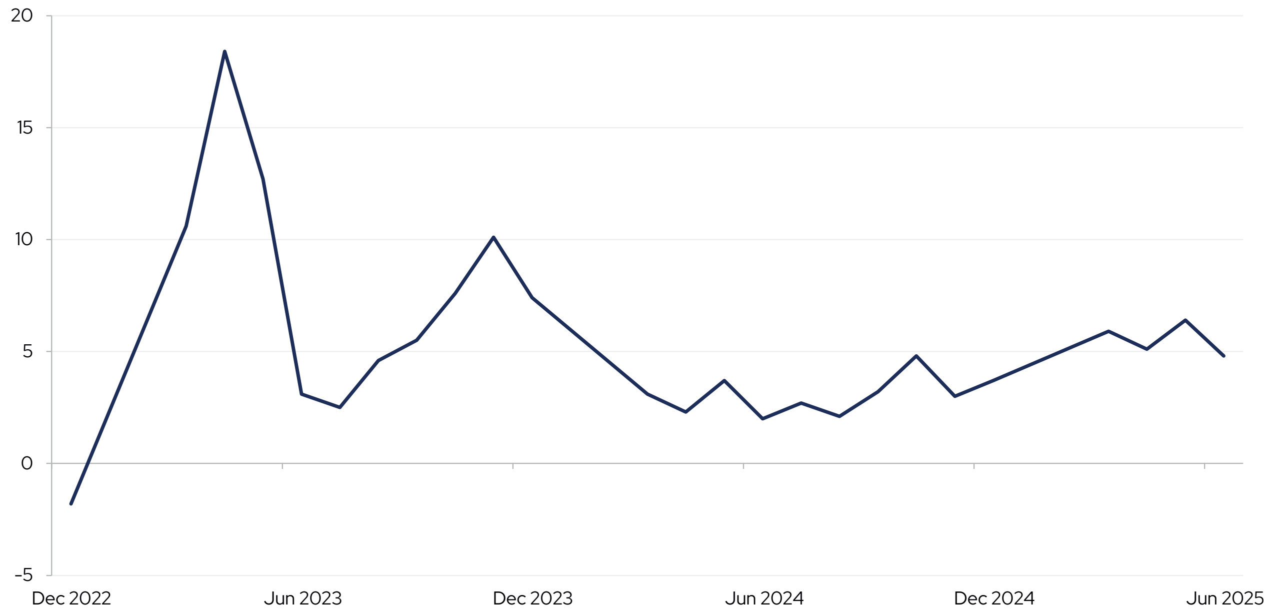
At the time of writing, the global "reciprocal" tariff deadline has been extended to 1 August, as the Trump administration seeks to formalise more bilateral agreements. Whether substantive deals can be struck with economies of meaningful scale under such tight timelines and politically charged conditions remains to be seen. China's deadline is currently set for 12 August, and while the path forward is uncertain, we remain cautiously optimistic that a constructive, **non-coercive agreement** between the two superpowers can eventually be reached.

BEYOND TARIFFS

While Trump's tariff policies have dominated global headlines, Chinese policymakers have remained focused on domestic priorities. A key objective has been to stimulate consumer spending and unlock a portion of the population's record-high savings. To that end, authorities have rolled out targeted consumption vouchers, offering subsidies ranging from 15% to 40% on a broad array of goods and services – from mobile phones and smartwatches to household appliances and dining experiences.

These stimulus efforts appear to be gaining traction, contributing to a gradual recovery in consumer sentiment and retail activity. As illustrated in Figure 2, recent data show an improvement in retail sales growth across China despite a minor slowdown at the end of June.

Figure 2: China Retail Sales Value - YoY% Change



Sources: Prescient, Bloomberg (as at 30 June 2025)

Amid ongoing uncertainty, the People's Bank of China (PBoC) took further steps to support economic stability by lowering benchmark lending rates by 10 basis points in May. In parallel, the reserve requirement ratio (RRR) was cut by 50 basis points to enhance liquidity conditions and encourage lending.

On the fiscal front, the central government has thus far held off on deploying additional stimulus, supported by stronger-than-expected economic momentum. GDP expanded by 5.4% year-on-year in Q1 and 5.2% year-on-year in Q2,, surpassing the official growth target of around 5%. The current temporary truce in US-China trade tensions is expected to provide further support to China's growth trajectory over the remainder of the year even as tariff related uncertainties remain.

Should economic and trade conditions deteriorate meaningfully, we believe Chinese policymakers retain ample fiscal headroom to act decisively. Market speculation around potential stimulus measures continues to circulate, including reports cited by Bloomberg of possible cash subsidies for families with children, a policy that could address both declining birth rates and persistently muted household spending. We will provide a detailed assessment of any such policies once formally announced.

MARKETS

Despite heightened volatility earlier in the quarter driven by "reciprocal" tariff headlines, most global equity markets ultimately closed the quarter in positive territory. US equities rallied sharply, reversing earlier losses and bringing year-to-date returns back into the black. China's recovery was delayed by roughly a month, largely due to the timing of the Geneva talks, and as such, the figures shown in Figure 3 below are not strictly like-for-like comparisons.

Figure 3

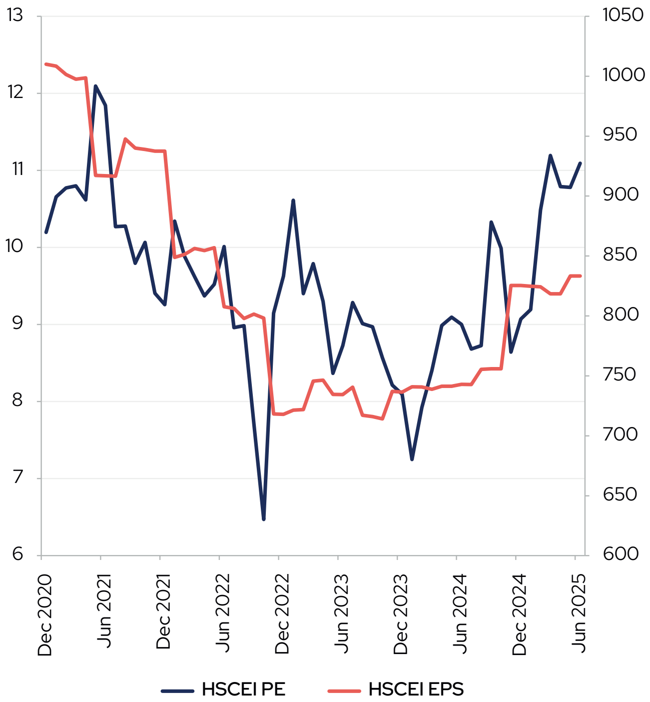
Market	Index	Q2 Return	2025 YTD
S&P 500	S&P 500 Index	10.57%	5.50%
China Offshore	MSCI China Index	0.75%	15.51%
China Onshore	CSI300 Index	2.58%	1.92%

Sources: Prescient, Bloomberg (as at 30 June 2025). Returns in USD.

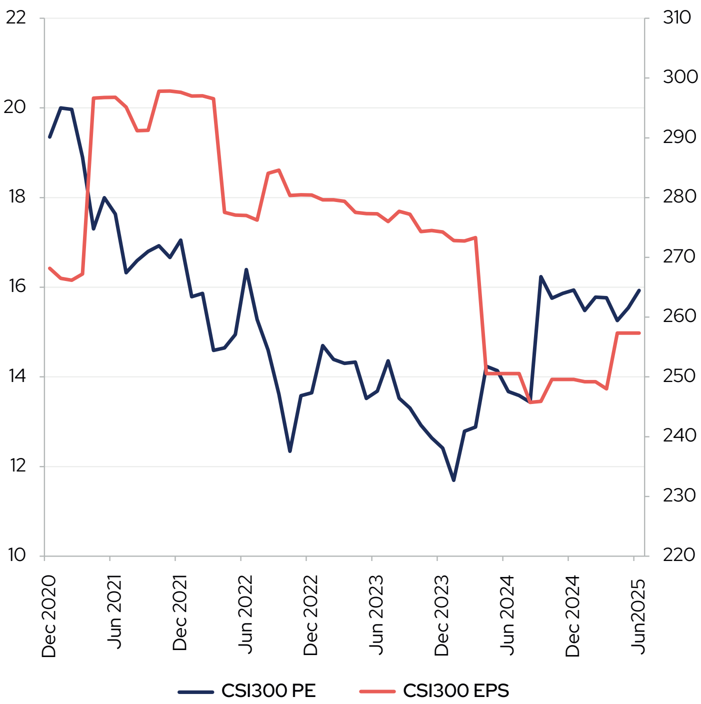
Nonetheless, both Chinese onshore and offshore markets delivered positive quarterly returns. On a year-to-date basis, China offshore equities continue to outperform global peers. Over the past few months, we have communicated that should the rally in China offshore/Hong Kong equities persist, we would consider reallocating towards China onshore A-shares within our multi-asset strategies, where valuations remain relatively more attractive.

While earnings recovery in the A-share market has been slower, the relative outperformance of onshore equities in Q2 versus their offshore counterparts suggests that the onshore rebound may now be underway. Looking at Figure 4 below, we can see that average earnings in Hong Kong started to recover in August 2024 and increased sharply in November, The onshore A shares earnings recovery only really started in April this year, almost a half year lag compared to Hong Kong.

Figure 4:
HSCEI PE ratio vs EPS



CSI 300 PE ratio vs EPS



Sources: Prescient, Bloomberg (as at 30 June 2025)

China's onshore A-share market continues to exhibit lower correlation with global equities during periods of market stress compared to offshore-listed Chinese companies in Hong Kong. From a valuation standpoint, both onshore and offshore Chinese equities remain attractively priced relative to global peers.

From a global portfolio construction perspective, the potential for a structural decoupling between the Chinese and US economies further reinforces the case for diversification. Our conviction in avoiding concentration, particularly in US equities, remains stronger than ever. As we have consistently stated, the ultimate outcome of the current trade conflict remains uncertain. While we believe China is increasingly operating from a position of strength, prudence dictates maintaining balanced exposure across both the US and Chinese markets.

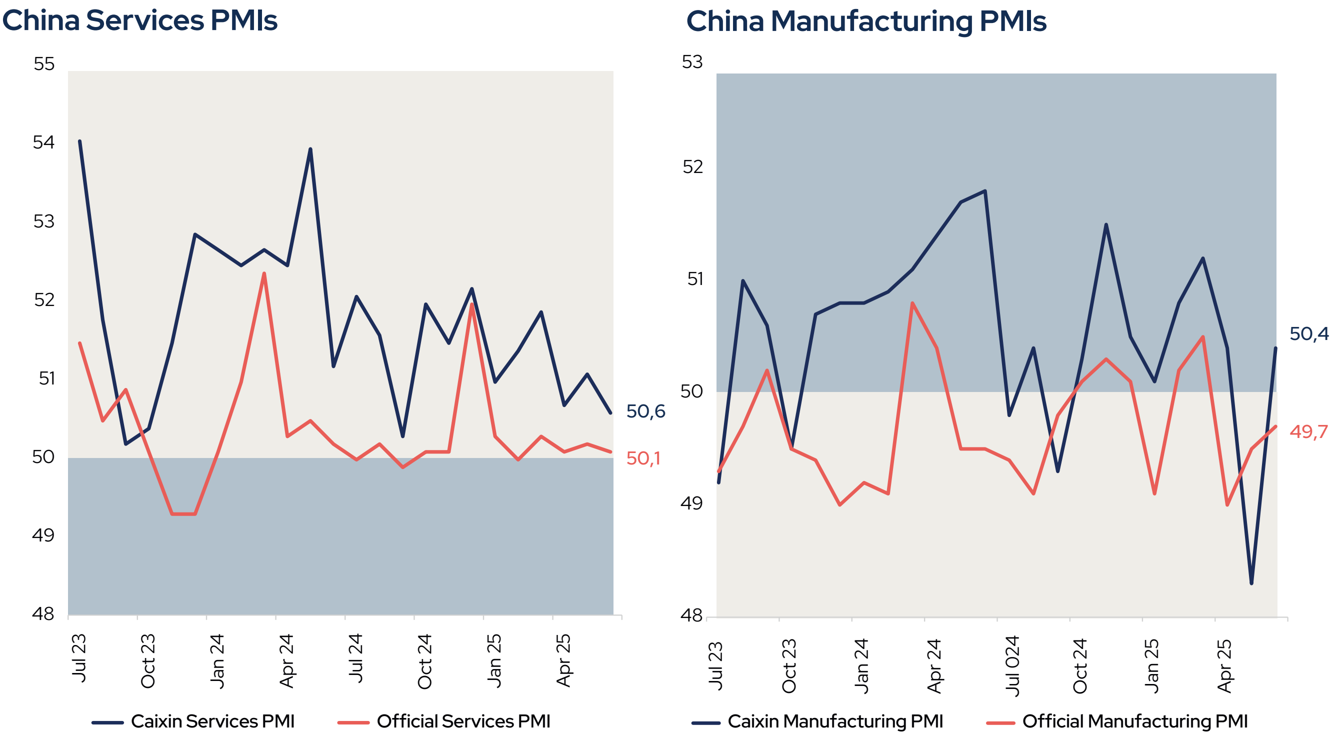
Chinese equities now present a compelling diversification opportunity within global portfolios. Depressed valuations, a supportive domestic policy environment, and relatively lower sensitivity to trade-related disruptions all strengthen the investment case. China-listed equities, whose revenues are primarily derived from the domestic market, are currently trading at valuations that effectively price in zero growth. In our view, simply holding these assets offers the potential for reasonable real returns amidst ongoing global uncertainty, with meaningful upside if sentiment improves.

MIXED ECONOMIC DATA

Business confidence in China has remained stable, with services PMIs consistently above the 50 mark, indicating continued expansion despite the series of tariff shocks during the quarter. Manufacturing PMIs—more directly impacted by trade developments—initially saw a sharp decline following the tariff announcements but rebounded strongly in response to the temporary truce between China and the US.

Encouragingly, the Caixin PMIs, which place greater weight on private sector activity, also reflect a resilient tone and improved confidence under current market conditions. Refer to Figure 5 below for further detail.

Figure 5:

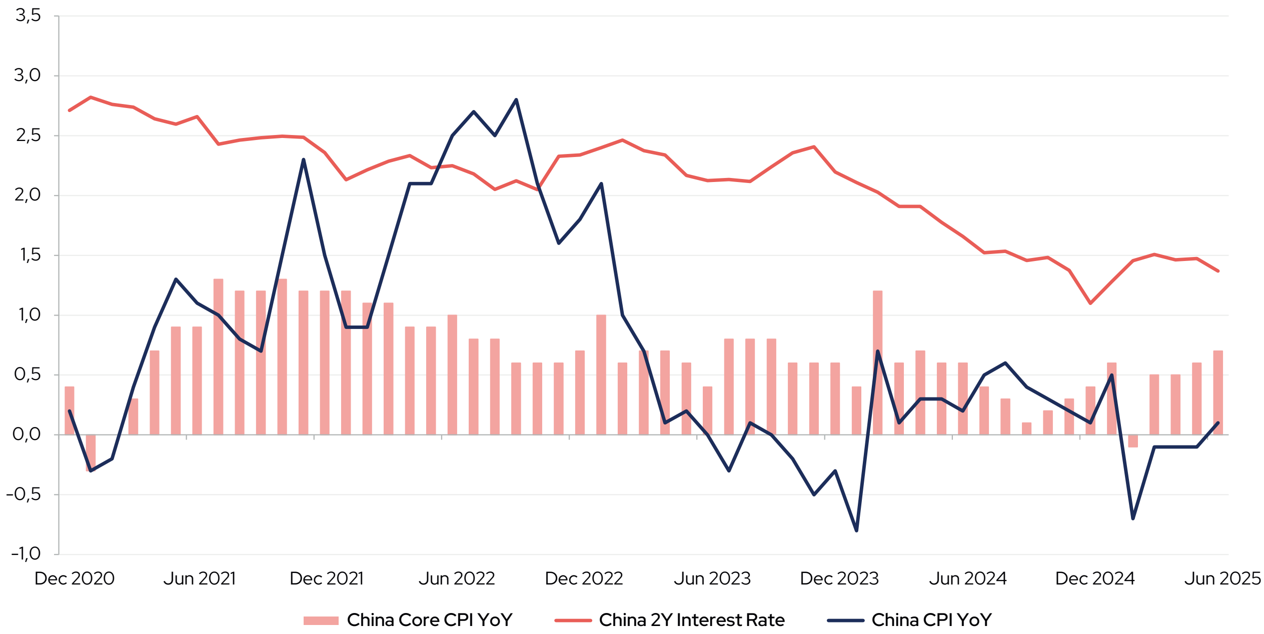


Sources: Prescient, Bloomberg (as at 30 June 2025)

Persistently low inflation and ongoing producer price (PPI) deflation remain key concerns for the Chinese economy. Headline consumer price inflation turned positive in June for the first time in five months, but only marginally so, at +0.1% year-on-year. Meanwhile, producer prices saw a further acceleration in declines, falling -3.6% year-on-year.

The one encouraging data point on the inflation front is core CPI, which posted its third consecutive month of acceleration, rising by 0.7% year-on-year in June 2025. That said, we maintain our view that China is still far from entering a Japan-style deflationary spiral. As shown in Figure 6 below, the domestic CNY market continues to reflect a healthy real interest rate environment.

Figure 6: China Inflation vs Interest Rates



Sources: Prescient, Bloomberg (as at 30 June 2025)

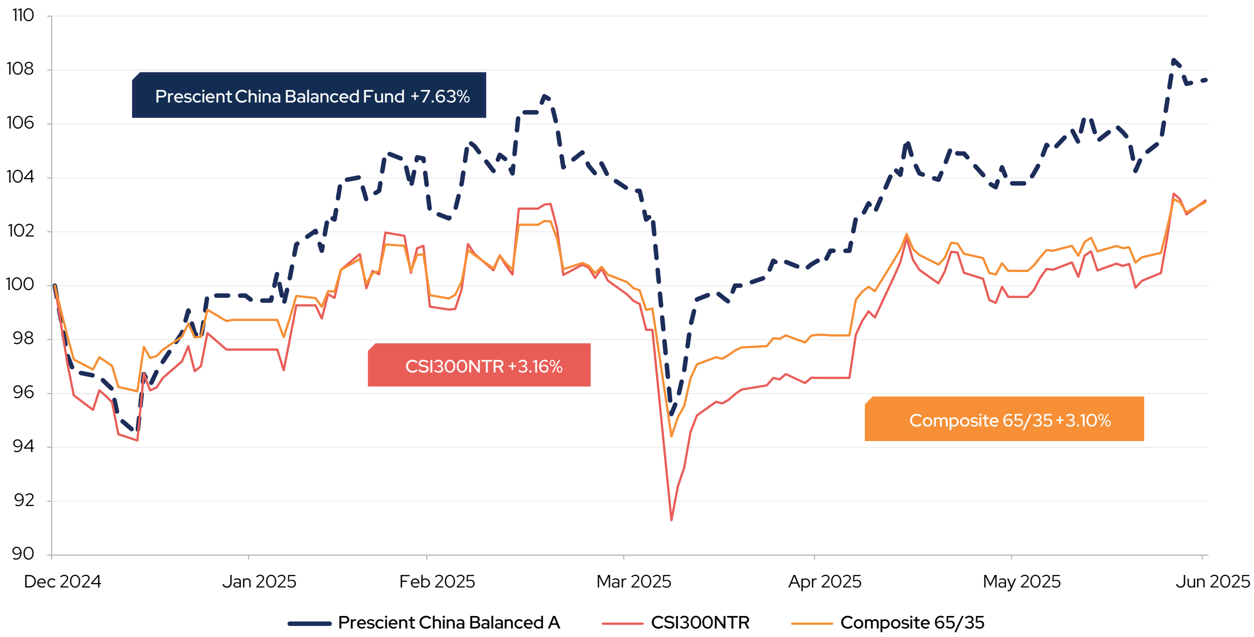
PRESCIENT POSITIONING & PERFORMANCE

PRESCIENT CHINA BALANCED FUND

Our flagship all-in-one flexible China solution—the Prescient China Balanced Fund—continued its strong performance into the second quarter of 2025. The fund delivered a net return of 3.88% in USD for the quarter, outperforming its China CPI+3% benchmark by 3.73%. Year-to-date, the fund has returned 7.63% after fees in USD, even surpassing pure equity benchmarks such as the CSI 300 Total Return Index by 4.47% over the six-month period (see Figures 7 and 8 below).

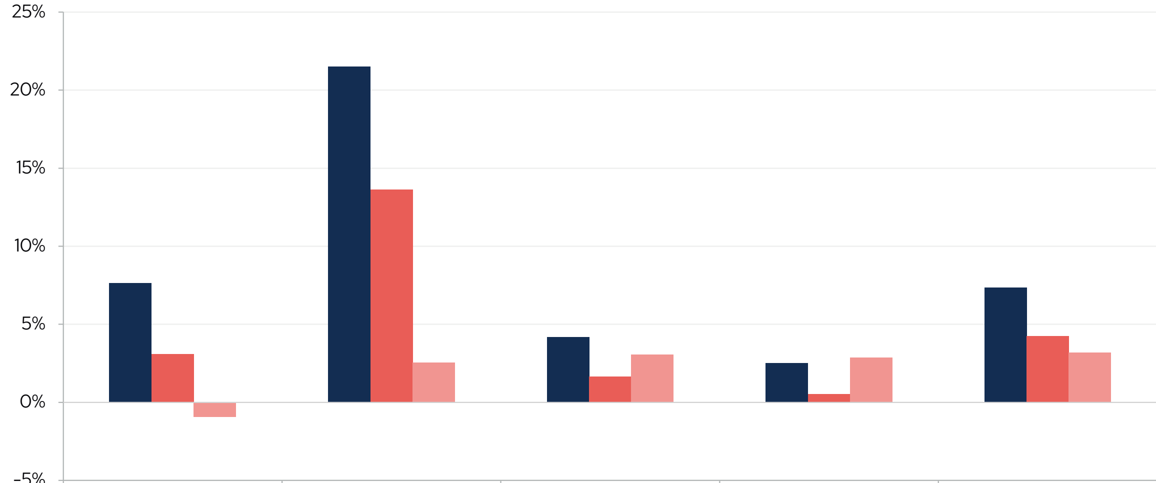
We maintain a dynamic approach to asset allocation and portfolio protection, aiming to capture upside while tightly managing downside risk and overall volatility. This disciplined framework remains especially important as we expect market conditions for the remainder of 2025 to remain volatile, driven by continued geopolitical uncertainty.

Figure 7: Prescient China Balanced Fund 2025 YTD - USD Net (Illustrative Performance)



Sources: Prescient, Bloomberg (as at 30 June 2025)

Figure 8: Prescient China Balanced Fund - USD A Class Net



	6M	1Y	5Y	10Y	Since inception 31 Mar 2013
Fund	7,63%	21,51%	4,16%	2,51%	7,35%
Composite 65/35	3,10%	13,63%	1,64%	0,52%	4,25%
CPI+3	-0,94%	2,52%	3,04%	2,86%	3,18%

Sources: Prescient, Bloomberg (as at 30 June 2025). Composite: 65% CSI300 and 35% CSI1Bond

Returns longer than one year have been annualised.

	Fund	Benchmark
Highest rolling 1 year	116.81	17.08
Lowest rolling 1 year	-26.97	-7.82

That said, our current positioning within the fund continues to reflect a bullish view on Chinese equities. We are maintaining a net equity exposure of over 80%, with our options overlay designed to efficiently capture up to 100% of the equity market upside in the event of a rally.

On the downside, we remain disciplined in budgeting and deploying protection strategies to mitigate risk. With markets likely to exhibit binary outcomes over the remainder of 2025, we believe it is critical to maintain a balanced approach – positioned to participate meaningfully in upside scenarios, while safeguarding against potential drawdowns.

OTHER STRATEGIES

The Prescient China Equity Fund, our onshore A-share focused pure China equity strategy, outperformed the CSI 300 Total Return Index by 1.24% after fees, delivering a 4.73% USD return for the quarter. Year-to-date, the strategy has returned 5.44% USD net of fees, outperforming its benchmark by 2.28%. Notably, alpha generation so far in 2025 has been driven by a somewhat unconventional combination of Value, Growth, and Momentum factors, all contributing meaningfully to outperformance.

PREPAREDNESS TRUMPS PERFECT TIMING

2025 has, so far, been a strong year for Chinese equities, with offshore Chinese shares leading global equity returns. Onshore A-shares appear to be gaining momentum following the stellar performance of their offshore counterparts in Hong Kong, supported by both improved earnings and improving price action. At current valuation levels, Chinese equities collectively remain among the most attractive across major global markets.

This year bears some resemblance to 2021–2022, when the Chinese property bubble began to deflate meaningfully. For our Prescient China strategies, we had already significantly reduced and exited our exposure to high-risk property names as early as 2018–2019. However, the market continued to rally irrationally through to 2021, with property-related assets becoming an alpha drag for nearly two years. While we were ultimately vindicated, the experience prompted us to further refine our investment process to reduce the lag between conviction and market recognition.

In 2025, we are seeing a similar sense of validation as markets begin to show more sustainable signs of China's post-COVID recovery. This time, we turned bullish on Chinese equities around 12 to 18 months ahead of the broader market – an improvement on our previous property cycle timing. We recognise that consistently timing markets with precision is extremely difficult, so when faced with the choice, we would rather be two years early than a day late.

We remain confident that the current equity rally in China is still in its early stages. Market levels remain well below the February 2021 highs, and with the prospect of rising earnings, expanding valuation multiples, and CNY appreciation, we believe the medium-term upside for investors is considerable. Our investment team continues to conduct rigorous research and stress-testing to ensure we are prepared for potential downside risks, while staying fully positioned to capture any unexpected upside, particularly through the remainder of 2025.

We will be speaking at the Institute of Retirement Funds Africa and Morningstar conferences in Cape Town and Johannesburg over the coming two months. We look forward to connecting with many of our clients in person and sincerely thank you for your continued support.