Research @ Citi Podcast, Episode 63: China & India Equities — Market Drivers and Risks in 2026

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Transcript:

Erica Poon Werkun (0:00)

Welcome to the Research @ Citi podcast. I'm your host, Erica Poon Werkun, Head of Research for JANA and Asia South at Citi. This is our inaugural launch episode for Asia Pacific, and I'm delighted to be joined today by two of my colleagues: Pierre Lau, our China Equity Strategist, and Surendra Goyal, our Head of India Research covering India Strategy and Indian IT services sector here at Citi. Pierre, Surendra, welcome to the show.

Let me first kick off with Citi Research's view on global EM equities, where we remain constructive in a global context. We see approximately 13% upside for the MSCI EM Index, with a year-end target of 1,540. Our constructive view is based on three key tailwinds that we see aligning for the year ahead.

First, the fundamentals are solid. We expect EM to deliver the strongest earnings growth of any major region in 2026, with consensus forecasting around 17% EPS growth. Second, we anticipate Fed rate cuts. Historically, a Fed easing cycle combined with a global economic soft landing, which is our base case, has been a powerful catalyst for EM equities. And third, the AI theme continues to be a major driver. EM-based AI stocks still offer an attractive valuation-to-growth trade-off compared to the U.S. peers and have been strong upward earnings revisions.

Let me now turn our focus to two of our most dynamic economies in Asia, China and India. And let me first chat with Pierre on China.

Pierre, Hong Kong and China stock markets were the outperformers among global markets in 2025, benefiting from tech and AI, strong export, and increased global liquidity. What is Citi's view on these markets in 2026?

Pierre Lau (2:01)

Hello, Erica. We are constructive to Hong Kong and China's stock market in 2026. We are not too much concerned about the decelerated economic growth in second half last year, because the full-year 5% GDP growth target last year was easily met after outperforming in the first half. And bear in mind, second half of 2024 was high.

We understand that some local governments might have held up some new project development, postponing to 2026. We are more optimistic to PRC development in 2026 compared to that years ago before 2025 because of positive catalysts from China market, domestically from the 15th five-year plan, and externally for more export clarity.

We prefer H to A shares, but the former is more sensitive to U.S. dollar rate cut and would have quality improvement for more top-tier A-share companies to have H-share listing in Hong Kong.

Erica Poon Werkun (2:56)

Well, government policy is probably the most important factor to decide performance of Hong Kong and China markets. And with 2026 being the first year of China's 15th five-year plan, what could be the key growth drivers of the plan that we could expect?

Pierre Lau (3:09)

Very good questions, Erica. The top three goals of the 15th five-year plan, including a) to build a modern system to consolidate economy; b) to accelerate scientific and technological self-reliance; and c) to build a strong domestic market. And among these top three goals, the first and third ones seem to be rather general, whereas the second one is more specific, related to the tech sector.

In our opinion, this highlights tech development being the top priority in the eyes of the PRC government and has become more difficult for China to import advanced technology from overseas based on the experience in the last five years.

Meanwhile, it's well highlighting that the target to expand high-level opening up to the outside world has become more important, ranked No. 5 among goals in the 15th five-year plan from No. 9 in the 14th five-year plan. China is eager to have better trade relations, in particular with emerging countries, to offset the reduction from Sino-U.S. trade.

Erica Poon Werkun (4:18)

Looking at China's 2025 GDP, 52% was from consumption, 15% from investment, and 33% from export. So, taking both domestic policy and external trade relation into account, where shall we find relatively more upside in 2026?

Pierre Lau (4:38)

This is a very popular question. We prefer export and investment to consumer in 2026. For export, PR's export gained global market share in 2025 up 0.4 percentage point year-on-year to 15%, better than expected. Audiovisual equipment and mechanical equipment have consistently helped the largest share and show steady growth. New energy vehicle, lithium battery, and solar panel have seen a rapid surge in their share, becoming new growth drivers for China.

China has competitive edge in export compared to many other nations, with comprehensive value chains in many manufacturing industries. The competitiveness is further enhanced by more automations in China. China's intensity using robots for productions doubled in last two years to 470 units per 10,000 workers, just behind Singapore and Korea.

Confidence on international trades should further be enhanced. We have Sino-U.S. trade deal signed, conducive to boost PRC export growth in 2026. We are upbeat on PRC export in 2026.

Erica Poon Werkun (5:51)

From a fundamental perspective, Hang Seng Index EPS growth in 2025 was the lowest in recent years, tracked by negative contributions from the internet sector. So what will be the outlook for 2026? Shall we expect improvement ahead?

Pierre Lau (6:06)

We do have good news. We are expecting HSI EPS growth to improve to 9.1% year-on-year in 2026, much better than 2.2% year-on-year last year. We attribute accelerations mainly from the internet sector on the expectation of reduced competition of food-delivery businesses amid anti-involution measures.

Erica Poon Werkun (6:29)

Hong Kong and China markets could be volatile, vulnerable to both internal and external factors. So what do you think will be the key risk factors for the China market in 2026?

Pierre Lau (6:40)

Investors do care about risk and return, and we see key risk factors of Chinese economy, including a) PRC property price outlook probably still drag with a lot of unsold inventory; b) China urbanization was 67% in 2024, with two-thirds population living in cities. Upside for urbanization seems not a lot since the base was already high; and c) aging populations and reduced birth rate could retard social demand and consumption.

Beyond this, while we like the fast growth from the new economy sector, they account for less than 25% PRC GDP compositions. The majority of PRC GDP are still from the old economy sector, which we could not expect very high growth.

Erica Poon Werkun (7:31)

Thanks for answering my questions on China, Pierre. Let me now turn to Surendra on India. So Surendra, let's talk about India earnings. How has the trend been in the last few years and what are we expecting in fiscal 2026?

Surendra Goyal (7:44)

Hi Erica. Let me start by highlighting that the 20-year CAGR of earnings for a large-cap Indian index is around 12% CAGR. And our global strategists have highlighted in the past how Indian corporates have a good track record of converting nominal GDP to earnings.

Over the past few years, we had strong four years post-COVID FY20 to FY24, where the earnings growth was almost 18% to 20% CAGR, and then we had a couple of slow years, mid- to high-single-digit growth. This was also a period where we did see downgrades vs. expectations. In the recent past, we have seen some stability in earnings revisions and are expecting some recovery in FY27, where earnings growth, we expect that it recovers to mid-teen levels.

Erica Poon Werkun (8:33)

What do the major macroeconomic indicators suggest about the Indian economy? Is there a divergence between macro and earnings? And what is giving comfort on the improvement in the growth trajectory?

Surendra Goyal (8:45)

Sure Erica, that's a very common question that we get from investors. The major macroeconomic indicators in India have been quite robust. And the question of divergence just keeps coming up. Headline real GDP in both FY26 and FY27 is expected to be strong at 7% plus. And yet earnings trends have been slow. We think there have been a number of things at play.

Firstly, real GDP trends have been robust, but nominal GDP growth of high single-digit is lower than historical trends. And that does have an impact on earnings growth. Secondly, consumption has been a bit on the slower side in the past couple of years, and competitive intensity is also high across multiple sectors.

Over the past year, we see a number of growth-supportive actions by the government and central bank, the most notable ones being personal income tax change, which leaves more money in the hands of people, as well as the reduction in GST rates. We are seeing decent pickup in some categories of consumption now. Rural trends have continued to be supportive. We have also seen a decent pickup in credit growth from lows of around 9% year over year. Now it's closer to 14%. So overall, we feel that things are moving in the right direction.

Erica Poon Werkun (10:02)

On foreign flows, we saw selling in India last year, and that has continued into this year. What are the concerns that you hear in your investor conversations?

Surendra Goyal (10:34)

Yeah, the common concerns we hear, there are broadly three things at play. First is the earnings downgrade point, which I already alluded to. Earnings have been a bit slower, and they have fallen short of expectations in the last year and a half, couple of years. Given that India market valuations have always been on the higher side in the EM context, these downgrades did impact.

Secondly, the U.S. trade deal. Earlier on, there was an expectation that India would be relatively better than its EM peer group on the trade deal. However, that has not played out so far. And India ended up with effective tariffs, which at this point are higher than most of its peer group.

And then the last point is obviously last year was the year of the AI trade, and we saw that across EM as well. And India is less correlated to the AI theme compared to some other markets, and that has also resulted in some outflows in our view.

Erica Poon Werkun (11:08)

Right. Well, conversely, domestic flows continue to be very robust and a key driver of markets. So, what has been driving that and how have recent trends been?

Surendra Goyal (11:19)

So recent trends on domestic flows have continued to be robust, although there is some monthly volatility in flows, as you would expect. And this is not a recent phenomenon. It's been going on for some time now, where we have seen equitization of household savings, driving a lot of domestic flows into the market.

Last year, we saw domestic institutional investors deploying around $90 billion into the market, and that compares to the $18 billion of foreign-money outflows. The primary markets in India have been quite buoyant as well. And around one third of the domestic institutional inflow has actually gone into the primary segment of the market last year.

Erica Poon Werkun (12:01)

Surendra, in your 2026 outlook report, you highlighted that you expect the year to start from a better risk-reward standpoint. And so, what is driving that?

Surendra Goyal (12:11)

So we feel that the setup going into 2026 is better and some of the challenges are getting addressed. Firstly, from a setup perspective, India is an underweight for EM investors now. And last year, it did underperform the EM index quite substantially. And just to give you some context on this, if you look at the past 20 years, there have been very few points where India has been an underweight for EM investors. So expectations are muted going into this year, and relative valuations have also somewhat moderated.

Second, I already mentioned that we are expecting an improvement in earnings outlook and decent growth. Third is a favorable U.S. deal in coming weeks or months could really help market performance. And finally, the last 12 months have been all about the AI trade. Any broad basing there could help India. So overall, we do feel that the risk-reward looks quite reasonable for India this year.

Erica Poon Werkun (13:07)

Great. Well, let's wrap up this podcast with the last question for Surendra. What are the key risks to India market performance for calendar 26?

Surendra Goyal (13:18)

So the key risks are firstly the earnings recovery bit, which I spoke about. The expectations are that we will see a recovery after two slow years. And if that disappoints, that is obviously a significant risk.

Secondly, the U.S. trade deal has been taking time. So while the impact on any large-cap index earnings is likely limited, this does impact the investor sentiment and multiple in our view.

And third is if the AI trade continues very strongly this year as well — and as I mentioned, India is less correlated to that trade — then that could also imply a relative kind of a risk for the Indian market in this year.

Erica Poon Werkun (14:00)

Great. Thanks, Surendra and Pierre, for joining me. This episode of Research @ Citi was recorded on Tuesday, Jan. 20, 2026. I'm your host, Erica Poom Werkun. Thank you for listening.

Disclaimer (14:34)