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Ultra-high net worth investors focused on China opportunities

For almost two decades, China's government has been pouring massive investments into its inland provinces.

by **Stirling Larkin**

Opportunities have become the rarest of all commodities in 2017. That we're on the cusp of a significant one has Australian ultra-high net worth (UHNW) investors focused. The opportunity is in China's listed markets during the month ahead.

China's CSI 300 index suffered significantly after the seismic retracement (crash) of July 2015. Institutional equity-focused market participants seized on that moment of weakness to both discount China's stockmarket potential and dispel it as a viable emerging markets (EM) alternative – primarily motivated by revenge against China's "state team" investors who prematurely abandoned US markets during the Lehman Brothers and global financial crises.

Accounting for these entrenched biases, Australian UHNW investors alongside their regional peers have taken the time to reassess China's preeminent listed equity bourse – the Composite Shanghai Index 300 or CSI300 – given recent "state team" portended sectorial support, the once-in-five-years National Party Congress, President Trump's first visit to Asia and China this month and recent regional geopolitical rifts.

More than just an isolated index range-bound trading opportunity, any reassessment of China fundamentals and its listed bourses in 2017 affords global investors an opportunity to see how demographics are influencing a maturing China and Chinese investment landscape.

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For almost two decades, China's government has been pouring massive investments into its inland provinces in an attempt to help them catch up with the prosperous coast.

This spending spree has added to the nation's enormous debt load, and many interior provinces, particularly in the northeast and far west, remain far behind.

Increased incomes

Despite this, the performance of parts of southwest China has been striking: major cities have modernised and incomes have risen substantially.

The region's economic prospects have improved enough that people, instead of leaving to seek their fortune elsewhere, are staying closer to home.

Better infrastructure and industrial relocation are now arguably driving a self-sustaining regional growth story.

Most Chinese cities are vastly more prosperous than they were a decade or two ago.

According to official statistics, between 2011-16, prosperous Shanghai, Jiangsu and Zhejiang were no longer seeing their share of the nation's population rise, while Sichuan, Guangxi and Anhui switched from a falling to a rising share.

One specific example can be found in Chengdu, which has benefited from large inflows of investment as technology firms chasing lower labour and land prices shifted manufacturing jobs west.

Foreign tech giants

Half of the world's laptop chips are tested and packaged in Chengdu, and two-thirds of all iPads are made in Foxconn's giant "iPad City" on its outskirts.

Other foreign tech giants – Intel, Quanta, HP, Inventec, Texas Instruments, Dell and Siemens – all have a presence, as do big domestic players like TCL and Lenovo.

Technological innovation is expected to be a much-discussed topic at the party congress.

The new group of leaders will set the growth target for 2018 at the Central Economic Working Conference in December.

China's economic circumstances are considerably different than at past party congresses.

The country's global importance, and its spill-over effects on the rest of the world, continue to increase.

Acknowledging the considerable uncertainty about policy direction in 2018 and beyond, it is prudent to expect an incremental shift in emphasis away from growth towards structural reform.

Mid-term transition

This would allow China's bumpy deceleration to continue in 2018, but at a gradual pace with a "policy put" still in place.

A wholesale abandonment of growth targets is not expected, nor a sharp acceleration in structural reform.

Still, given the stakes, this mid-term transition holds the prospect of being more significant than the last mid-term Congress in 2007.

Of course, UHNW investors know that China growth may inflect after the plenary.

China data has remained strong, with all four PMIs up in the latest readings affirming a healthy 6.7 per cent pace of growth – if that can be believed.

While the monthly economic indicators are likely to improve in the final set of releases before the party congress, it is widely expected that Chinese growth will decelerate modestly into 2018. This reflects a slight deceleration in global growth and therefore Chinese exports, Sino property sector tightening and a combination of tighter financial and perhaps fiscal controls after the party congress.

Given the stakes for the Australian real economy – which has become hooked on Chinese property financing proxies – the Australian dollar and the continuing investment opportunity drought witnessed across global bourses, the near-term future of China's CSI 300 matters.

Stirling Larkin is chief investment officer of Australian Standfirst.

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