

## What You Should Know This Week: CSOP's Weekly China Wrap Up

### China continues to defy expectations in strong growth, but need continued fiscal reform

China could see its economy continue its solid 6.9% growth rate in the second half of the year, according to PBOC governor Zhou Xiaochuan, defying expectations of a slowdown widespread among economists. Speaking at a panel discussion with other global policy makers, Zhou painted a healthy picture of China's economy; imports and exports both showed strong growth, as well as fiscal income. On financial stability, the governor noted that shadow banking activities have slowed in response to government initiatives, while cuts in overcapacity of steel and cement may hit the 10% target set by the government. On a cautious tone however, he also addressed the growing problem of rising corporate and local government debt, stating that the "government must pay more attention to fiscal reform".

#### *What is the concern?*

China's corporate debt has been a growing concern for the global financial community, with global policy makers like Fed Governor Jerome Powell commenting specifically to China that the "risks are significant". The IMF also noted as they raised its growth estimates for China for both 2017 and 2018, that expansionary policies come at the cost increased financial risk on the back of rapid credit expansion. In response to these concerns, Governor Zhou's comments are uncharacteristically bold for the generally reserved central banker, sending a strong message of commitment to the integrity of the financial markets in China. The comments also come just a few days ahead of the National Congress meeting, and it remains to be seen if reforms will pick up on the backdrop of a stronger economy.

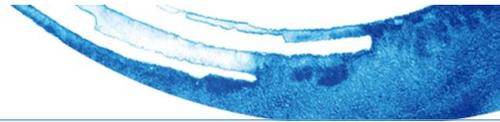
### President Xi Jinping kicks off the 19<sup>th</sup> National Congress

In his 3-hour keynote speech delivered to more than 2300 delegates, China's President Xi reviewed the country's achievements in the past five years and shared his vision for the future. His speech marked the beginning of the all-important seven-day gathering of China's elite to elect the next country leadership. Xi asserted the rise of China's international influence and promised to continue the anti-corruption campaign. Meanwhile he expressed great confidence in the ideology of the Chinese Communist Party (CCP) and the current political model.

#### *China under Xi, past and future*

President Xi's campaign of economic growth, war on corruption, and improving China's image on the international stage had won great support from the ordinary Chinese people, during his first five-year term as the state leader. China's economic growth stayed at a healthy level since he took helm in 2012, and the supply-side reform proved effective in containing systematic financial risk. Corruption in the public sector has been evidently reduced in the past five years, with many high-end restaurants that previously had been frequent by public officials going bankrupt. Meanwhile, the "One Belt and One Road" Summit earlier this year was widely considered as a diplomatic victory for China.

For the future, President Xi set a few crucial milestones to achieve for the ruling party. First, China will focus on eliminating counties with wages below the poverty line, by 2020. With a growing wealth gap alarming to the socialist party, the government committed itself to increasing social security and equality. Second, China will modernize its defense systems and aim to build a world-class army by 2050. President Xi assured the focus on growing its military power had no motives of hegemony; however, he vowed to fight any separatist interests.



## **National Congress continued; China lays out its ambitions, domestically and internationally**

With the National Congress fully under way, the markets were busy interpreting meanings behind President Xi Jinping's 3+ hour speech from the first day. In the speech, the president outlined his plans for the leadership and for the nation in the next five years and beyond, touching upon nearly every socioeconomic topic relevant in today's China. President Xi also used the platform to reiterate the party's stance in power and leadership, emphasizing the central role the Party will play in China's future. Furthermore, he detailed his vision for the "Chinese dream" – in which China is a great modern socialist country by 2050 with a first-class military, and where "Chinese people will enjoy greater happiness and well-being, and the Chinese nation will stand taller and firmer in the world". What he did not mention was a specific growth target – a subtle de-emphasis which some market participants picked up as a potential sign of a shift in the Party's focus in development.

*What were the key messages of his speech?*

President Xi Jinping is making out to be one of the most influential Chinese leaders in history, in the league of Mao Zedong and Deng Xiaoping. The congress meeting is yet another show of his power, driving home the message of an emerging and burgeoning China – under the stronghold of the Communist Party. His message regarding domestic policies is clear: there will be zero tolerance for corruption; property market will be controlled, as "houses are for living in, not for speculation"; systematic risk will be dealt with via reducing debt, further reforms, and strengthening state-owned enterprises. Meanwhile, he also promised the continuance of opening of markets, of the financial and services sectors, and lowering the barrier for foreign businesses. This thought was echoed by China Banking Regulatory Commission Chairman Guo Shuqing, the country's top banking regulator, in his address to the congress on the second day. Chairman Guo recognized the falling market share of foreign banks as a detriment to competition, and promised to give overseas banks "more room" in market participation.

Externally, the president sounded his intentions for China to take on a more driving role in many global issues such as the environment, international security, and globalization. While China has the second largest economy in the world, the country has yet to hold proportional influence in international affairs – but President Xi looks to bring China closer to the center of the discussions. While there were no surprising outcomes to come out of the assembly thus far, it remains to be seen by both domestic and international community how President Xi drives the messages into action.

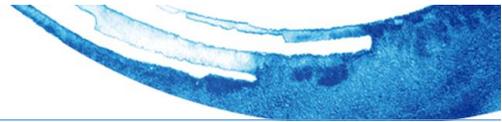
## **China's Yelp/Groupon/FoodPanda mash-up receives USD 30 billion valuation**

Meituan Dianping, a Chinese service focused e-commerce platform, became the world's fourth most valuable start-up at a valuation of USD 30 billion, trailing behind the ride-sharing behemoth Uber, Chinese counterpart Didi, and Chinese electronics company Xiaomi. The company offers a plethora of web-based services, ranging from food delivery to restaurant reviews to movie ticket bookings to discounted group purchases (similar to Groupon). In the latest round of funding led by Tencent, USD 4 billion was raised from a variety of investors, of which the newest being US travel giant, Priceline Group. As a result of Priceline's investment, Meituan Dianping will enter a strategic partnership with Agoda.com, a hotel and travel booking site under Priceline, to further develop the travel booking aspect of the services.

*What is Meituan Dianping, and how did it become so valuable?*

While mostly unknown outside of China, Meituan Dianping is one of the hottest new technology companies domestically. Similar to how the acronym BAT was created to refer to three tech giants Baidu, Alibaba and Tencent, a new acronym has emerged to refer to Meituan Dianping and two popular tech startups; TMD, referring to Jinri Toutiao, Meituan Dianping, Didi Chuxing. These companies are the beneficiaries of the rapid rise in smartphone use in China, with first mover advantage giving them near monopolies in their respective jurisdictions. Competition is in the horizon however, including Alibaba-

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backed Ele.me. Meituan Dianping faces particularly high competition risk, given its vast scope of business. In addition, with three of the top four most highly valued start-ups in the world being Chinese, there are some concerns arising over China's venture bubble, with lofty valuations for an opaque and illiquid asset.

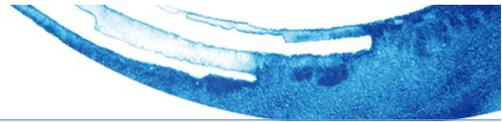
### **Hong Kong Stock Exchange lobbies for a decrease of stamp duty on stock trading**

Hong Kong Stock Exchange (HKEx) is reportedly lobbying the new local government to reduce or even waive the stamp duty on stock trading. Currently, the 10 bps stamp duty is charged on both purchase and sale of stocks, deterring high-frequency traders and market makers from participating in the local market. The newly elected leader made promoting the financial service sector a part of her policy platform, a stance that made the trading tax reduction potentially more likely.

*What are the implications of a policy change?*

The total market capitalization of Hong Kong listed stocks ranks number four after those of the US, China, and Japan, according to Bloomberg. However the daily turnover is only a fraction of that of China, let alone the US. The high trading tax is often blamed for the poor liquidity. For comparison, US exchanges don't impose any such levies, while exchanges in China charge a 10 bps stamp duty only on the sale of stocks. Other developed economies, such as Japan, Australia and Singapore, also do not have such taxes on equity trades.

The HKEx could potentially suggest to either align the stamp duty to the Chinese markets, effectively halving the current stamp duty burden, or to remove it completely. The policy change, if approved, is expected to improve the liquidity of the Hong Kong stock market, and ultimately benefit HKEx, a monopoly of its kind in the city. HKEx's stock price rallied almost 5% during Monday's trading session. The reaction could be overly optimistic however, given a tax policy change could be difficult to implement. Firstly, the stamp duty is a steady source of revenue for the government. Secondly, any such proposal would take some time for the government to examine, approve, and implement, especially given the political environment in Hong Kong.



## Index definition:

1. The FTSE China A50 Index is the benchmark for investors to access the China domestic market through A Shares – securities of companies incorporated in mainland China and traded by Chinese and institutional investors under the Qualified Foreign Institutional Investor and Renminbi Qualified Foreign Institutional Investor (QFII & RQFII) regulation. Note that one cannot invest directly in an index
2. The CHINEXT index is China's Nasdaq-like barometer of high-tech stocks. Note that one cannot invest directly in an index
3. The MSCI China Index captures large and mid-cap representation across China H shares, B shares, Red chips, P chips and foreign listings (e.g. ADRs). With 150 constituents, the index covers about 85% of this China equity universe. Note that one cannot invest directly in an index
4. Bloomberg's Global Aggregate + China Index combine the Global Aggregate Index with the treasury and policy bank component of the China Aggregate Index. The EM (Emerging Market) Local Currency Government + China Index combine the EM Local Currency Government Index and treasury component of the China Aggregate Index. Note that one cannot invest directly in an index
5. Citibank's World Government Bond Index (WGBI) measures the performance of fixed-rate, local currency, investment grade sovereign bonds. The JPMorgan Emerging Market Bond Index (EMBI) is a set of three bond indices that track bonds in emerging markets. Note that one cannot invest directly in an index
6. The Hang Seng China Enterprises Index is a free-float capitalization-weighted index comprised of H-Shares listed on the Hong Kong Stock Exchange and included in the Hang Seng Mainland Composite Index. Note that one cannot invest directly in an index

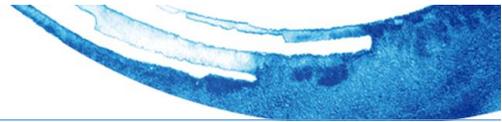
## Institutions:

1. PBOC: People's Bank of China
2. SOE: State-owned enterprise
3. IMF: International Monetary Fund
4. CBRC: China Banking Regulatory Commission
5. CIRC: China Insurance Regulatory Commission
6. CSRC: China Securities Regulatory Commission
7. SAFE: State Administration for Foreign Exchange
8. ICBC: Industrial and Commercial Bank of China
9. EU: European Union
10. G20: An international forum for the governments and central bank governors from 20 major economies
11. UAE: United Arab Emirates
12. SSE: Shanghai Stock Exchange
13. LSE: London Stock Exchange
14. AIIB: Asian Infrastructure Investment Bank
15. WTO: World Trade Organization

## Currencies:

1. RMB: Renminbi, the national currency of China
2. USD: US Dollar, the national currency of the United States

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3. GBP: Pound Sterling/Great British Pound, the national currency of the United Kingdom
4. JPY: Japanese Yen, the national currency of Japan
5. EUR: Euro, the official currency of the Eurozone
6. HKD: Hong Kong Dollar, the national currency of Hong Kong
7. USDCNH: Abbreviation for the US offshore Dollar/RMB currency pair

**Others:**

1. IPO: Initial public offering
2. SPO: Secondary Public Offering
3. MoM: month over month
4. YoY: Year over year
5. GDP: Gross Domestic Product
6. EM: Emerging Market
7. Bps: Basis points
8. FX: Foreign Exchange
8. OTC: Over-the-counter
9. GDP: Gross domestic product
10. ETF: Exchange-traded fund
11. FATCA: Foreign Account Tax Compliance Act
12. TPP: Trans-Pacific Partnership
13. SDR: Special Drawing Right, an international reserve asset
14. OBOR: One Belt, One Road
15. RCEP: Regional Comprehensive Economic Partnership