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

China's economic mastermind Liu He steps out onto center-stage at Davos

President Xi Jinping did not attend Davos this year. In his place, he sent China's economic authority to the annual gathering of global business and political elite. Liu, a strong contender to take the helm of the country's economy for the next five years, told an audience that China would open its domestic market wider and that this year's reform measures could exceed international expectations. Liu, who delivered his half-hour speech in Mandarin, said China's economy was improving and the country was on course to become wealthier. He also called for joint efforts to address global issues ranging from climate change to fighting terrorism. Liu, 66, also warned against a trade war and isolationism during a time of growing, complex technological change. Most importantly for U.S. investors, Liu reaffirmed the government's commitment to ease investment restrictions on foreign companies in manufacturing and services, step up enforcement of intellectual property protection, and "welcome joint efforts from the global community".

What does Liu's speech signal about President Xi's supply-side economic restructuring?

Liu, 66, led the Chinese delegation at the World Economic Forum and was given the same status as the most important leaders. He was the only policymaker who does not hold the position of head of state to speak in one of ten sessions hosted by executive chairman Klaus Schwab. Other speakers to take the chair beside Schwab included US President Donald Trump, German Chancellor Angela Merkel, UK Prime Minister Theresa May, French President Emmanuel Macron, and Indian Prime Minister Narendra Modi. This symbolized the importance of China's economy on the global stage. His remarks come after China recorded 6.9% growth in gross domestic product last year – faster than the official target of around 6.5%. Beijing has also stabilized the CNY exchange rate with capital curbs, ending a sharp currency depreciation seen in the second half of 2015 and in 2016 after missteps in adjusting the rate. In China's annual closed-door economic conference in December 2017, the top leadership singled out three main tasks for the next three years: controlling financial risk, reducing poverty and curbing pollution.

Chinese provinces lower growth targets after Xi Jinping says don't just chase higher figures

President Xi Jinping stressed that local governments should be aiming for sustainable economic growth rather than just chasing high figures. This led Chinese provinces in a race to lower their GDP targets for the year. Among 19 provinces and municipalities that released growth targets for 2018, 12 of them have since lowered their goals. The moves come after the Binhai New Area, the city's economic zone touted as China's future version of Manhattan, admitted this month that it had inflated its GDP figure by a third in 2016. President Xi said during his address to the Communist Party congress in October that the government wanted to pursue quality growth, which would include factors such as tackling pollution and alleviating poverty, rather than an emphasis on the pace of expansion.

Why is this significant for institutional investors?

This move signals the top-down commitment of the CCP to implement President Xi's vision delivered during the 19th Party Congress in December 2017. Investors should consider President Xi's message on monetary policy with the same framework used to view anti-corruption at the provincial level: the vision will be implemented. For years, China as sought to strike a balance between supporting growth and curbing debt, and with last year's annual growth targets reached, there is growing focus toward deleveraging. While this signaled concerns for growth slowdown, performance in 2018 has proved to alleviate those worries. It is generally expected that money-market rates will stay bound to a range.

China's National Internet Finance Association cautions against overseas ICOs and OTC trading

A self-regulatory organization in the field of internet finance in China warned citizens against participating in overseas initial coin offerings (ICOs) and cryptocurrency trading. In a public statement published on January 26, 2018, the National Internet Finance Association (NIFA) writes that, after China issued a ban on ICOs last September and ordered closure of cryptocurrency exchanges, it has seen investors moving their funds to overseas platforms. NIFA states: "Recently, as worldwide governments are tightening regulations on cryptocurrencies, some overseas ICO and trading platforms may also face the risk of being forcefully closed due to compliance issue. Therefore, domestic investors are advised to be cautious of the risk." NIFA was first initiated in 2015 by the People's Bank of China and approved by the State Council. In addition, NIFA highlighted that existing over-the-counter (OTC) trading activities in China are not complying with current regulation. Some domestic social networks have served as a marketplace to facilitate peer-to-peer trading and some non-banking payment tools are also offering services to support the finance, the association states.

What does this mean for cryptocurrency exchanges?

Following the closure of domestic cryptocurrency exchanges, Chinese investors have largely moved to OTC platforms that operate over messaging applications such as WeChat and Telegram. Payment methods such as WeChat Pay, AliPay and bank transfers are still available for OTC traders to push through transactions. Citing details from central bank's ban on ICOs, NIFA made it clear that these activities still fall within the scope of cryptocurrency trading: "Investors should be aware that these trading services all have potential risks on the policy front, and be advised to stay away from these illegal financing activities," NIFA writes.

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 combines 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 combines 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) are 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. G7: An international forum for the governments and central bank governors from 7 major economies
12. UAE: United Arab Emirates
13. SSE: Shanghai Stock Exchange
14. LSE: London Stock Exchange
15. AIIB: Asian Infrastructure Investment Bank
16. WTO: World Trade Organization

Currencies:

1. RMB: Renminbi, the national currency of China

2. USD: US Dollar, the national currency of the United States
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