2015 – Issue 4

STUART + CARLYON

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The Dragon is alive and well

In the investment markets the topic of China always generates a lot of the conversation and it is hard, even, to recall that not so long ago the world's most populous nation was almost totally disengaged from the world economy.

Recently the IMF voted to include the Chinese yuan (Renminbi) in its basket of reserve currencies along with the yen, pound, euro and US dollar. It's weighting will be the 3rd largest behind the US dollar and Euro and ahead of the yen and pound.

There were several reactions, globally, to the inclusion of Chinese currency in the overall basket, and not all were favourable. Critics worry that China can now directly manipulate the international currency markets and that the latest move is the thin end of a wedge to weaken the international power of the US Dollar.

Ben Bernanke, the former Chairman of the American Federal Reserve, has equated the yuan's acceptance with that of a primary school student earning a gold star for effort. It's a symbol.

Said Bernanke: "China received the equivalent of a gold star this week, when the International Monetary Fund agreed to include the Chinese currency, the renminbi, as part of an IMF-managed asset called the Special Drawing Right, or SDR. Like the awarding of a gold star, inclusion in the SDR is almost entirely symbolic. This confers no meaningful additional powers or privileges on China."

What it is likely to do is reinforce China's stated desire to become more, not less, driven by market forces, and bolster reforms to their financial system.

China inevitably features in the presentations we attend and recently investment managers, Platinum and Magellan shared some insights. Platinum says there is a lot of talk of China's economy slowing down which is true but it is still growing at around 7% per annum. China still has a strong balance sheet with 80% in US treasury bills.

The rise and rise of the middle class underpins considerable discretionary spending. In 2014 China reported:

- 32 million passengers flying per month
- 640 million internet users
- 109 million overseas tourists
- $5 billion in box office revenue (US box office 2014 was $10.4 billion)
- 25 million cars sold (US auto sales same period 16.5 million.)
- 14 billion e-commerce parcels delivered

The booming discretionary spend has started to shape the western business world. Making the most of the Chinese thirst for status brands is Galeries Lafayette in Paris. The stunning fashion department store now has a special entrance for the Chinese tour groups who arrive to take advantage of duty free prices. Brands such as Gucci and Yves St Laurent have profited from this sector of the market. Staff are fluent in Mandarin.

Meanwhile in Hollywood, movie makers are tailoring their creations to fit in with Chinese viewer tastes, the Chinese box office is making the difference between risky domestic results versus more assured global box office returns. The high octane Fast/Furious series does more business in China than in the USA.

Censorship is still a factor and scenes that may have once painted China as the bad guys are now ending up on the cutting room floor. The producers of Skyfall, ditched a scene that portrayed China as weak.

And even Macdonald's in China have modified their offerings to suit the local market. The latest burger consists of steam buns encasing 3 pieces of pork in Sichuan Chinese green pepper sauces, bacon and lettuce.

On a recent trip to Singapore for a nephew's wedding, Susanna saw these ceramic burgers at MAD (the Museum of Art & Design), which showcases contemporary Chinese artists. The Gallery is located on Tanglin Rd at the top end of Orchard Rd, and was a lovely break from the shopping mecca.

So where do our fund managers see opportunity?

Platinum has nearly as much exposure to China as it does in the USA. They see more opportunities in China to buy companies at better value. Also they invest in global companies exposed to the Chinese consumer - for instance they are taking advantage of the surging number of Chinese travellers by investing in Samsonite baggage and Carnival cruises.

Platinum is also investing in the information tech sector and their top holdings - Samsung, Ericsson, Cisco and Intel – will benefit from the continued growth in the use of the mobile and e-commerce industry.

Magellan is taking a different tack. They talked recently about the outlook for China and the prospects of an oversupply of housing, slowing export growth as well as vulnerable fiscal positions of local government which are dealing with the overdue fall-out of corruption. A lot of infrastructure expenditure never resulted in anything concrete.

The lower demand for commodities has depreciated the currencies of commodity exporters such as Brazil, Australia and Russia, and is one main reason why share prices have been slashed for giant companies Rio and BHP.

Magellan say it is very unlikely that we'll see a total collapse of the Chinese economy as Chinese authorities are taking steps to slow credit growth and manage the housing correction and given all China's debt is held domestically.

Magellan remains invested in the cashless sector (Visa, Paypal) and like Platinum investing defensively in old tech companies (IBM, Intel, Microsoft) which supply the new tech sector - the providers of Cloud storage and smart chips. Magellan sees these companies as survivors in a slowing down economy.

What does all this mean for our client portfolios?

China's economy has hit a few bumps of reality lately, even while the currency has been accepted by the IMF as an integral part of the global basket of currencies. Their economy has big issues ahead and for the time-being there will be "relative" austerity.

But it's important to remember that there are always businesses that see these challenges as opportunities and can deliver growth and income. For careful investors China has plenty of upside. The key is to focus on companies that deliver fundamental market needs. Forget the fads and be careful of the start-ups.

With continuing low interest rates, we're investing in funds that look for companies that will provide goods and services that people need or in most cases want! This guideline applies to all our diversified international funds, not just to the Chinese component of our portfolios.

Just off Wall Street

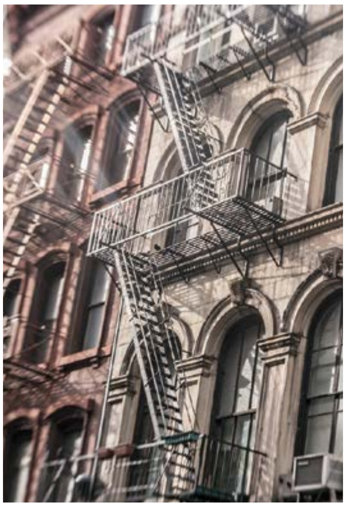
Many of our clients who travel prefer taking the independent route. Package tours? No way! Yet putting an itinerary together, booking accommodation, transport all takes time however. Then there's the mystery of what to do when you reach your destination.

For those who want less hassle and more discovery, there is another option. Bespoke guided groups allow you to get a particularly rich and memorable experience, and fully organised. We have a client who runs New York Curated Ltd. They have put together an eclectic 5 day itinerary of art, architecture, design and food in the New York that only New Yorkers know about.

Forget Times Square. NY Curated Ltd will take you to the hip areas of Manhattan and Brooklyn to visit artist lofts, interesting art galleries, amazing architectural spaces, avant-garde theatre, and foodie restaurants. Everything is taken care of so that you can just enjoy the vibe of the Big Apple. The September 2015 offering was sold out – in 2016 there's one in May and two in September.

So if you are after a unique travel experience beyond the usual tourist haunts, go to *www.newyorkcurated.com* or contact Karin on 021 663019 for detailed itineraries.

Festive greetings to all our wonderful clients and all those that support Stuart+Carlyon! Our last day in the office is 23 December and we have skeleton staff from 11 January till 18 January. We wish you happy and safe holidays.



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