



A thoughtful, succinct, overview from Robert Lloyd George – consistent with his earlier messages.

The U.S. Federal Reserve continues to convey uncertainty on interest rates, which is not a helpful phenomenon. Also, despite the general agreement that higher rates would signal strength, the market remains fickle, or immature, and panics short term at the suggestion!

We believe that slow growth and low interest rates bode extremely well for equities of companies with growing dividend cash flow.

Comments welcome as always.

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*September 13, 2016*



## LLOYD GEORGE A D V I S O R Y

September 2016

### Investment Outlook

#### Global Trade Continues to Slow

World stock markets react in the short term to central banks pronouncements and policies, especially the Federal Reserve, which is now less likely to raise rates before the November election. The crisis of Brexit appears to have come and gone with extraordinary speed as markets have rebounded from their sharp falls in late June. This may be somewhat like the “phony war” of 1939-1940 before the reality of the economic crisis facing Europe sinks into the minds of investors. In the longer run, however, as Keynes said, “in the short term, the market is a voting machine; in the long term, a weighing machine.” What it weighs is surely the volume of business as well as its profitability. While some on-line businesses, like Amazon and its like, have enormously increased their sales volume in recent years, profitability and margins are still thin.

In the real world of physical trade, however, we are cautious because we continue to see signs of slowdown everywhere we travel. In Singapore this summer, the large container port was half empty, something we have never seen before over the last 25 years. China’s imports have fallen about 12.5% from a year ago. While the price of oil has fallen from \$110 to about \$45 today, the volume of oil being shipped is also beginning to decline slightly. Perhaps the shift to electric cars will be the tipping point in the consumption of gasoline and the imports of crude oil into large developed economies. China’s demand for steel is also falling despite short-term speculative



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recoveries. The ship scrapping business in India has been caught in a squeeze by the fall in value of steel over the past six months.

Our conclusion, seen from Hong Kong, is that the small open trading economies, such as Hong Kong, Singapore, and also South Korea, Japan, and Taiwan (as well as the UK) will suffer in the next two or three years from this squeeze on their exports; and profits will be negatively affected. However, the large “continental” economies, such as the USA, China, and India, will be able to weather the storm in better health if their domestic consumer sectors continue to grow steadily. This is what we have seen in China so far as the state-owned enterprises and heavy industries, like steel, shipping, construction, coal, oil, and many others, have been squeezed and are suffering downturns in profitability because of large oversupply and overcapacity. Nevertheless, the growth in China continues to be impressive in the areas of healthcare, education, travel and tourism, and consumer products. Our Chinese portfolio consists of two education companies, Maple Leaf and TAL Education; a Traditional Chinese Medicine (TCM) healthcare stock; and several plays on tourism, including China Lodging and TravelSky. These areas continue to see earnings growth in the area of 20%.

India, however, is the one major economy where we have conviction that, despite a global slowdown in 2017 and the two years following, will maintain its steady growth due to favourable demographic and population trends (half of the 1.3 billion Indians are under 25); interest rates falling from a high real level of 7% today; a stable Rupee; and infrastructure development starting from a point where China was in 1995. Most importantly, India’s consumer spending will continue to be strong because of rising incomes, better education, a better electricity supply, and more economic opportunities. These trends are also mirrored to some extent in the neighboring economies of Pakistan, Bangladesh, and Sri Lanka. There are, of course, large challenges to overcome - corruption, bureaucracy, illiteracy, and the slow-moving pace of change in a



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democracy; but there is nowhere else in the world where we see the potential for growth being so bright as in the subcontinent.

We shall be launching our Indian Ocean Fund in the 3<sup>rd</sup> quarter of 2016 with this clear vision, always focusing on the need for careful stock selection and risk controls.

Robert Lloyd George  
13<sup>th</sup> September 2016

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