



Disruptive Events and Technologies

Wonderful, enviable perspective. Incorporates macro happenings with stock selection discipline criteria.

Georgian Capital focuses on dividend growing companies in Canada and the United States – but we appreciate Robert Lloyd George’s clear writings on the Far East.

Enjoy! Questions, and referrals to receive future missives, are welcome.

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Investment Outlook

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The speed of change appears to accelerate both in technological disruptions and also in the diplomatic political area, as Donald Trump prepares to meet with Kim Jong-un. It is worth remembering that since the truce in 1953, North and South Korea and the United States have still been in a state of war, and no peace has ever been signed. Hence, the existence of the Demilitarised zone, DMZ (about 1 mile wide) is a more complete barrier than the Berlin Wall ever was.

About 20 years ago, I had a visit in Seoul with the Minister for Reunification, who expressed to me the concerns that the South Koreans had, given that the 20 million population of North Korea was living at such a primitive economic level (and the country was suffering through a severe famine), the capital costs for South Korea to invest in, and upgrade, the infrastructure and living standards of North Korea would be 20 times that undertaken by West Germany for East Germany after 1990 (which cost US\$1 trillion, and took nearly 20 years).

Nevertheless, the implication is that Kim Jong-un wants to modernise his economy just as Deng Xiaoping did for China after 1989, retaining the complete control of the Communist party (and his family) while allowing economic liberalisation and the advent of market forces. The West wrongly assumed that the Communist Party in China would wither away or lose control, under the pressure of the new economic freedoms. But nearly 30 years later, it has not happened and President Xi Jinping is in more complete control than anyone since Mao. Perhaps Kim Jong-un can do it too, but it is a much less sure prospect with a family dynasty (the only parallel is Cuba, where the Castros have finally handed over power to a new president after 60 years).

Investors may be bewildered by the speed of change, and it is necessary to have the “seeing eye” or look two steps ahead to see who may be the winners and losers of this tectonic change



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in the North Asian geopolitical balance. Japan is apprehensive. South Korea's Chaebol may be ready to seize hold of the opportunity of a new market. In the longer run, there is no doubt that China's hegemonic influence over the Korean peninsula will be strengthened, and the US influence diminished. Within 10 years, Taiwan may be absorbed by China.

The threat of US protectionism has already caused repercussions all around Asia, and China has responded by opening up its banking, insurance, fund management, and even automobile sectors. The shares of China's domestic automobile manufacturers have fallen sharply. Given a more open market in consumer (for instance, medical products), American and Western brands will most probably prevail. We have also seen sharp falls in Chinese drug stocks. Asia's business model was to protect its infant industries for as long as possible, and now the Americans are getting tougher. There will be a shakeout in these more vulnerable sectors.

India is the least affected economy because of its lower ratio of Foreign Trade to GDP, and its large domestic consumer market, which is unaffected by US protectionism. We continue to see a rapid growth of corporate earnings in India (nearly 23% in the coming 12 months) and we are confident that Mr. Modi has an assured re-election in May 2019. Nevertheless, our main concern today is the rise in oil prices, which is pushing up India's current account deficit from less than 1% back up to about 2% of GDP (it was 5% a few years ago). The Rupee has fallen by 4% this year, and foreign investors are again becoming skittish. Nevertheless, the flow of domestic savings and capital continues to support the Indian share market; and we do not think that there is a severe risk for the Indian economy, since the sensitivity to energy prices has reduced in recent years.

Although the meeting between North and South Korea on 27th April has received the top international headlines, an equally consequential but less reported meeting was held between Chinese President Xi Jinping and India Prime Minister Narendra Modi in Wuhan. These two countries represent 40% of the world's population and have been linked culturally since before the Han Dynasty (200BC) or the era of Emperor Ashoka (232BC), both in trading networks as well as the travels of pilgrims and exchange of knowledge and religions. The dissemination of Buddhism from India to China had a transformative effect on Confucian and Taoist culture.



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Mr Modi wanted to meet President Xi Jinping in order to alleviate Himalayan Frontier tensions near to Bhutan, where there was almost a military clash last year. In addition, India feels surrounded by Chinese diplomatic engagement in Pakistan, Bangladesh, Sri Lanka, Myanmar and, even more recently, the Maldives. Mr Modi is a man of vision, and wants to keep peace with his neighbours, particularly with the May 2019 election approaching. Although both countries have close diplomatic relationship with the US, their own peaceful relationship is more important in its long term beneficial consequences for Asia, and for investors in the region.

One historic development this week was when Mr Modi announced that all 600,000 Indian villages now have access to electricity. As with the inclusion of many poorer Indian citizens to the modern financial economy (with 300 million new bank accounts being opened in the past 3 years) this development of power has a deep social and economic significance.

In conclusion, we are facing a volatile summer in Asian share markets, owing to the shadow of protectionism looming over the region. We have reviewed all our positions, both in the broad Bamboo Asian portfolio as well as the Indian Ocean region and are satisfied that we own the best companies, with good earnings prospects both in the immediate 12 months and beyond, which are worth holding, despite the short term buffeting of trade winds. In particular, we have taken a positive view of the China A Share market, which has corrected by a considerable degree in the last year, but we view this as an opportunity because of its opening up to foreign investors and because of the underlying momentum of growth and profitability, particularly in the technology and medical sectors in China.



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This month, we have engaged a Singapore based advisor similar to VAL-Q in India which will enhance our coverage of the markets in Singapore, Malaysia, Thailand, Indonesia and the Philippines. In fact, we have had an underweight exposure in these markets in the past 12 months, which has not hurt our performance. The coming Malaysian election has caused a lot of political uncertainty. Thailand, while appearing more stable under military government, is experiencing slow economic growth, despite the steadiness of the Baht. Singapore remains a fairly overpriced market with high real estate values, although these have corrected over the past 5 years. The most interesting market in South East Asia, in our view, is Vietnam which has risen about 40% in the past 12 months and retains the attraction of being a younger, faster growing, economy in a 'catch up phase' of manufacturing expansion.

Robert Lloyd George
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Hong Kong

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