



2047 Moves Closer

Interesting perspective on Hong Kong, as Robert has been there over 37 years, since age 26! It looks like the end, at increasing speed, of a wonderful democratic capitalism.

Investments, with growth, are still possible, but on a careful specialty-idea basis. U.S. / China trade 'disputes are likely the new normal.

Enjoy the read. Comments or questions always welcome.

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Investment Outlook

2047 Moves Closer

When Britain and China agreed on the Handover of Hong Kong in 1997, with the understanding that “One Country Two Systems” would allow Hong Kong to preserve its traditional freedoms, Deng Xiaoping said that by 2047, China and Hong Kong would be indistinguishable, and the merger would be completed (as well as a 50 years extension of all property leases).

Recent events in the “Special Administrative Region” have moved that date closer. Following the violent attacks on the New China News Agency offices, and several mainland China banks, with petrol bombs, rocks and other weapons. China has quietly decided to take a stronger line in enforcing “Patriotic Education” in Hong Kong schools, and press freedoms are being slowly curtailed. For the time being, the British legal system, and the Final Court of Appeal survive – a fundamental assurance of fair play (and no corruption) to the business community. But the subtle pressure is growing on, for instance, the Chief Executive of Cathay Pacific, who was forced to resign after expressing support for some of his employees who joined the protests. Money talks: and the ability of an airline, or a bank, or any foreign company, to operate freely in China, is always subject to politics.

For anyone, like the author, who lived in Hong Kong in the Golden era of 1982-1997, these are sad and depressing developments which do not presage such a happy future. When I arrived in Hong Kong in March 1982, I was astonished by the laissez-faire dynamism and energy of the place – a “barren rock” in the South China Sea with no natural resources, a refugee population of 6 million Cantonese (98%), Filipinos, and expats from Europe, Japan, America, Australia – from almost everywhere.



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There was a flat income tax of 15% for everyone – so if you worked hard, you kept 85% of your salary and bonus – what a contrast to Britain or European welfare states! Even if property seemed pricey (it is now 3 or 4 times more so) everyone was there “temporarily”. It was fairly said that it was the only place in the world when you could have a good business idea in the morning, incorporate by lunch time, and be making a profit by the end of the day!

The legendary British Financial Secretary of the 1960s, Sir John Cowperthwaite, was so convinced of “Laissez Faire” that he would not allow his civil servants to collect economic statistics in case they were tempted to intervene - The Chinese Sage Mencius called it “Wu Wei” or “Do Nothing”. Margaret Thatcher used to repeat the old Chinese adage that the best way to govern a Kingdom was like cooking a small fish (ie. don’t meddle).

Hong Kong in its heyday was a marvelous practical demonstration of Libertarianism applied to daily life and business: minimal government; no welfare; just guaranteed law and order. But sadly in the past 5 months that seems to have broken down. The trust between the people and the local government and the police force, is inseparably fractured, 2047 is rapidly drawing nearer.

Meanwhile in China, where the use of facial recognition has been perfected, they are now adding “emotional recognition” which sounds like science fiction but may enable police and authorities to anticipate crimes or violent acts.

In any case, the “animal spirits” of investors in Hong Kong and China have already revived. Hong Kong share prices have jumped 5% from the bottom. China A shares have outperformed (+32%) the S&P500 (+25%) in 2019.



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China is not going to be held back, though its economy will certainly slow in the next 3/4 years. Its national effort to catch up in technology, AI, renewable energy, batteries, high speed trains, medicine and biotechnology, 5G communications, blockchain financial technology, via its domestic consumer brands as well as domestic oil and gas production – none of these trends will reverse.

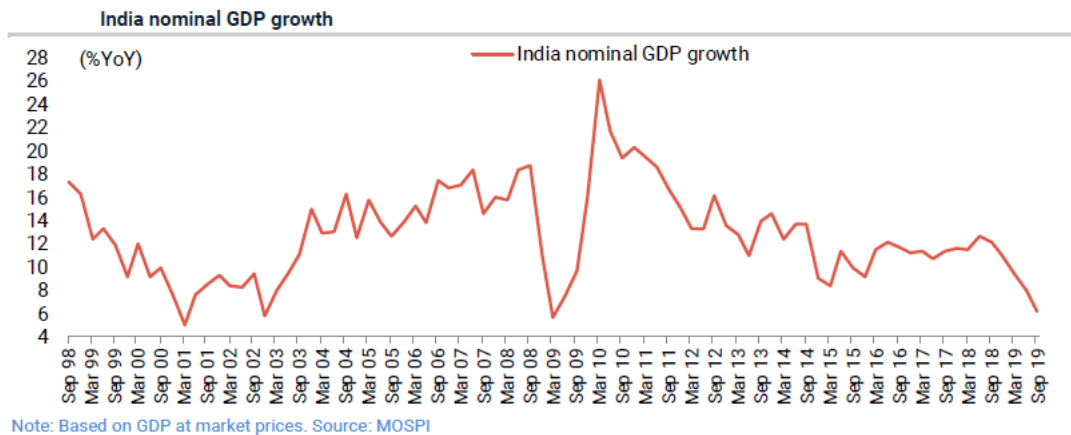
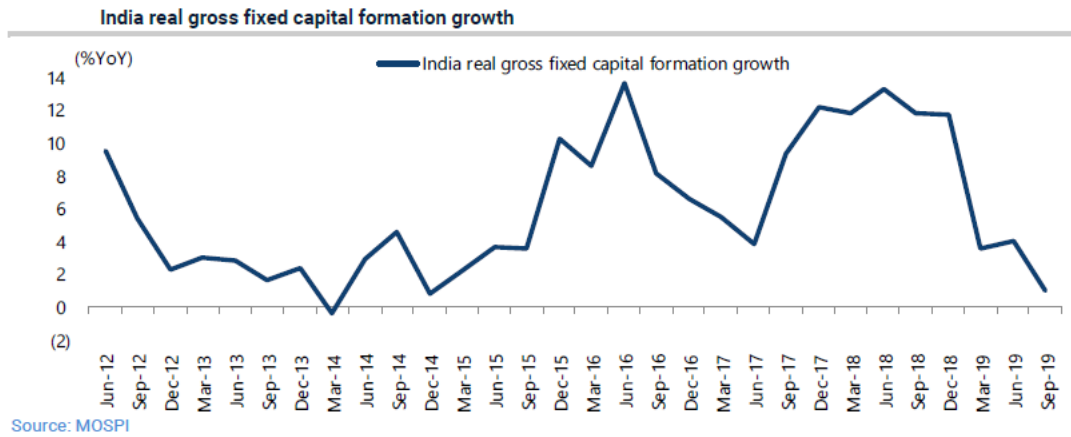
The Hong Kong District Council elections, on November 24, had a 71% turnout and resulted in “pro-democracy” candidates winning 80% of the seats. Although this has little real political consequence, it sends an important message to Beijing. Also, recent demonstrations have been larger in size, and mainly peaceful. There is some hope of calm and dialogue in the next few months, although HK’s economy has suffered from a 43% fall in visitors, especially from Mainland China, and a 24% decline in retails sales.

The Indian economy presents a conundrum, having slowed to 4.5% but, nevertheless, showing the promise of recovery in 2020 as the banking system and property market are cleaned up. Structural reforms, such as GST and demonetization, have slowed down capital formation (insert chart) and economic growth. The business community is having to make a real adjustment to more transparent lending and reporting and more efficient tax collection: all good developments in the longer term. The Modi government has also announced the privatization or listing of 33 public sector companies, including BPCL.

The Bombay stock market has held up well, although India’s Business Today magazine highlights that only 9 stocks, including HDFC, Reliance, ICICI Bank, HDFC Bank (among our largest holdings) have attributed 93% of the market gain of the past 2 months: quality companies, in terms of balance sheets, corporate governance, and earnings growth. Much of the US\$13.2 Bn. invested in India by international investors has come in the form of ETFs, although Indian investors also added US\$8 Bn.



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We expect some “truce” in the US/China trade dispute by December 15 (the due date of the tariffs), which will be a powerful positive signal from US and Asian markets before year-end. Also Boris Johnson’s victory in the UK election will speed up Brexit, and remove uncertainty for international companies. Free trade, rather than protectionism, may be the trend in 2020, further boosting investors’ confidence.

We wish all our customers and readers a very healthy and happy Christmas and all best wishes for the New Year.

Robert Lloyd George
16 December 2019
Hong Kong



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