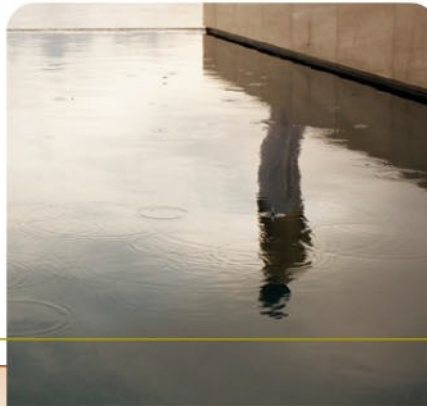


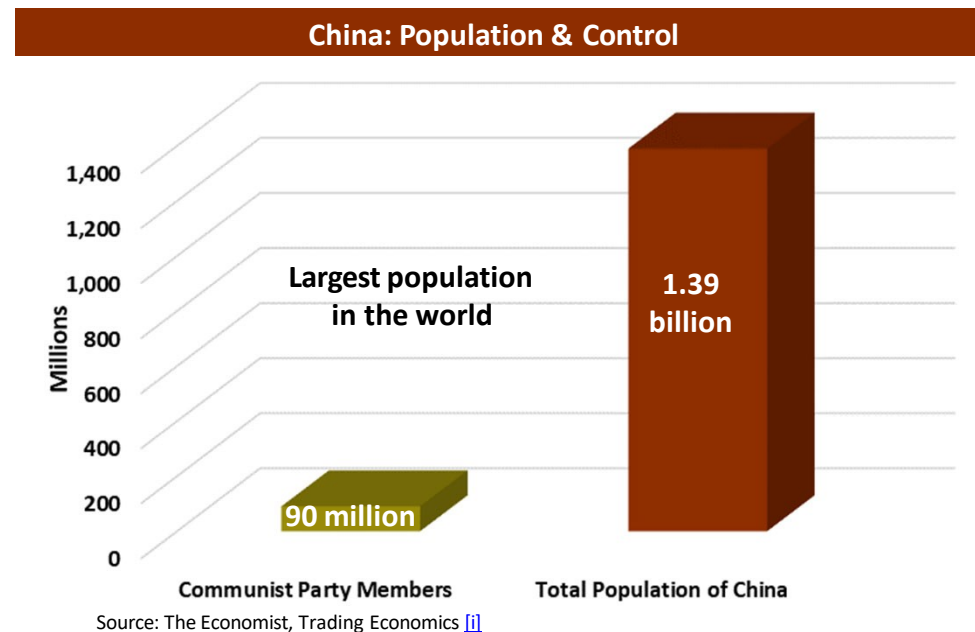
THE CASE FOR CHINA A SHARES 菲利普斯公司



Wealth Strategies | Vested

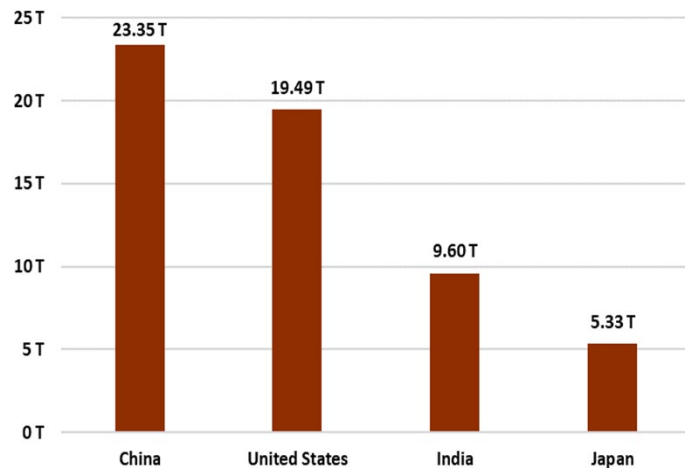
Understanding China

- ❑ The centralization of power and industry has been a characteristic of Chinese society dating back to its dynastic era. Today, this system has evolved to 90 million communists controlling 1.39 billion citizens. President Xi Jinping (a lifetime appointee) has modernized the concentrated system of industrialization with unprecedented economic growth.
- ❑ In order to maintain the economic growth derived from this centralized system, Chinese policy is engineered for stability by providing:
 - ❑ Free healthcare
 - ❑ Targeted poverty alleviation
 - ❑ Governmental regulation of stock markets geared towards protecting the profits of local investors
 - ❑ Highly subsidized industrial policies
 - ❑ Free education



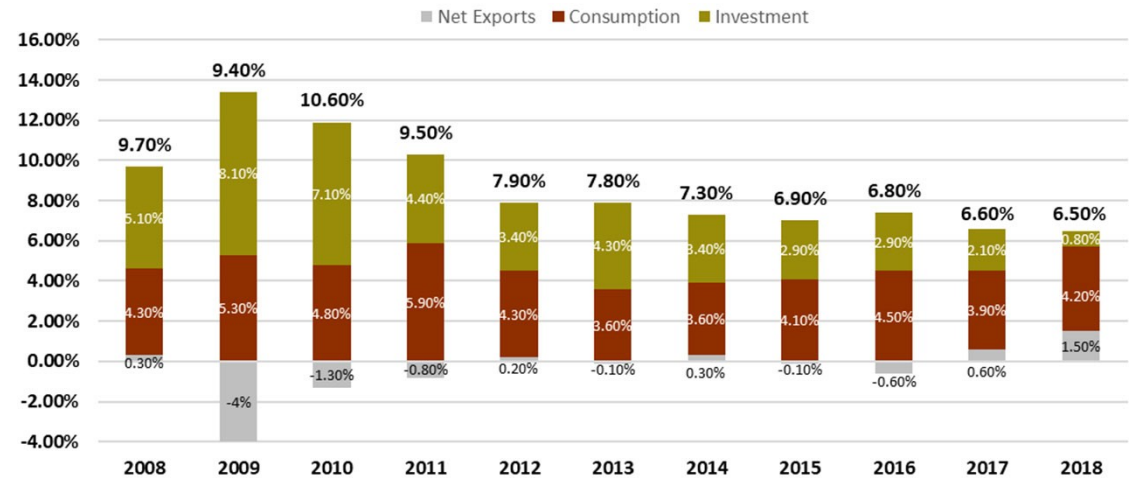
China Is Too Big To Ignore

Country GDP by Purchasing Power Parity (PPP)



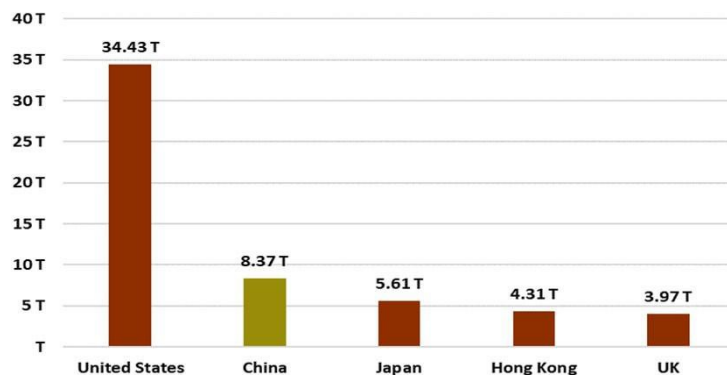
Source: The World Bank, GDP 2017 [\[ii\]](#)

China Real GDP Contribution: Y/Y Percent Change



Source: J.P. Morgan Asset Management, Guide to the Markets [\[iv\]](#)

Global Stock Exchanges by Market Cap (Trillion USD)

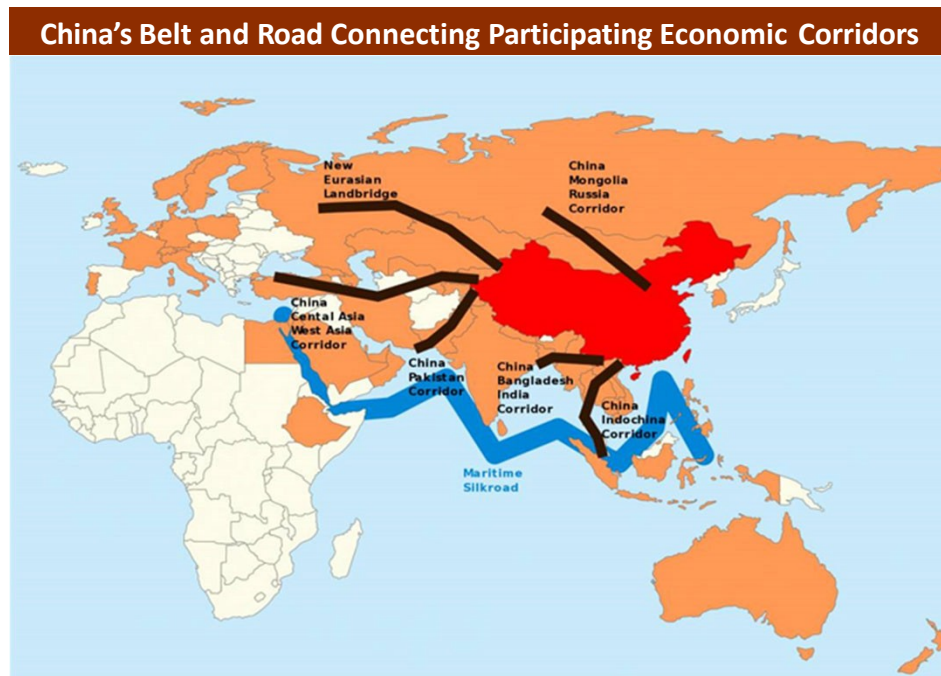


Source: Statista, data as of May 2019 [\[iii\]](#)

- ❑ Largest economy in the world in PPP terms:
 - ❑ Largest manufacturer in the world
 - ❑ Largest online retail market in the world
 - ❑ Largest share of global green house gas emissions (28%)
 - ❑ Largest investor in renewable energy
- ❑ China is transitioning to a consumption driven economy.
- ❑ Second largest equity market in the world.
- ❑ Third largest fixed income market in the world.

China's Belt and Road Initiative

- ❑ Through the multinational aspirations of the Marshall Plan, the United States rebuilt the infrastructure of a world ravaged by the Second World War.
- ❑ The unprecedented investment opportunities for American companies derived from the new multinational economic order allowed them to profit immensely from community development and the revitalization of infrastructure, once thought unsalvageable
- ❑ This open and advantageous foreign policy allowed the United States to export goods cheaply to its many trading partners, branding the nation as the nexus of global trade.
- ❑ But today, the United States has descended into policies of bilateral trade circumventing opportunities for growth through the rapidly developing global markets.



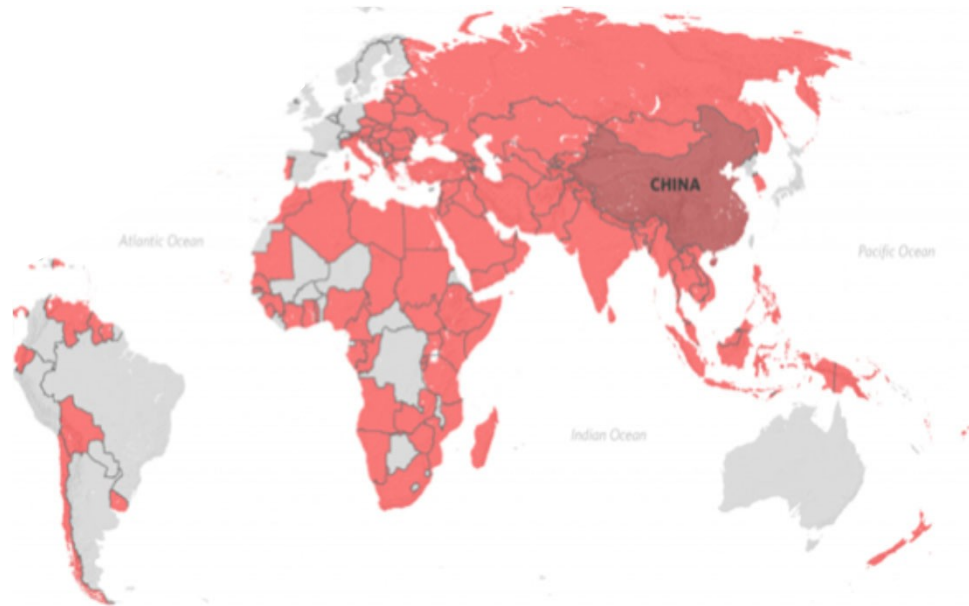
Examples: If you would have invested \$1,000 in the following stocks at the end of WWII, here's what those positions would be worth today:

- ❑ Johnson & Johnson would be worth \$7.5 million + dividends today
- ❑ Exxon Mobil/Standard Oil would be worth \$2.4 million today [\[xiv\]](#)

- ❑ China has ascended to become the driving force behind the newest evolution of multinational trade in the largest change in global order post-WWII.
- ❑ Through its Belt and Road Initiative, China aspires to restore the "ancient Silk Road," while simultaneously industrializing regions of the Middle East, Latin America, Africa, and Asia.
- ❑ The investment opportunities in Chinese industry serve as the modern equivalent to those derived from the United States at the turn of the last economic era.
- ❑ The scale of this initiative would have been unimaginable during the beginning of the last economic era, and the magnitude of profits from it are as equally unimaginable today.

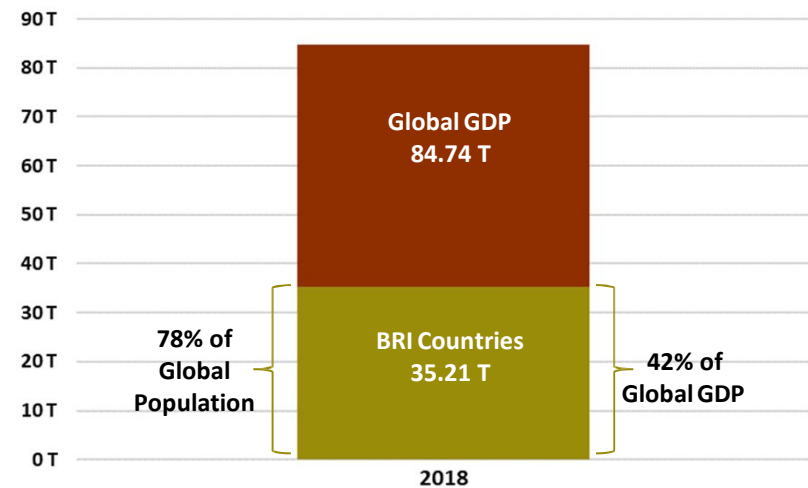
China's Belt and Road Initiative

Participating Countries in China's Belt and Road Initiative



Source: China's Belt and Road Portal, IMF; Copyright Stratfor 2019 [\[v\]](#)

Belt and Road Countries as a % of Global GDP (in USD)



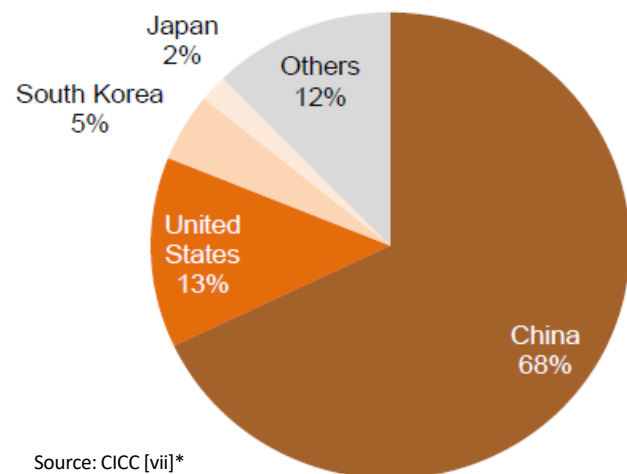
Source: China's Belt and Road Portal, IMF; Copyright Stratfor 2019 [\[vi\]](#)

- ❑ Increased infrastructure spending (over \$1 trillion in infrastructure projects: railways, roads, and pipelines to gain control of cost-effective trade routes to easily export surplus resources to participating countries) funded by low-interest loans to participating countries.
- ❑ The extensive reach of the initiative whose participant nations produce 48% of the world's GDP and contain 78% of the global population.
- ❑ Massive government subsidies of raw materials to meet the demand of local and international community development projects to build factories, power plants, schools, and domestic dwellings.
- ❑ Increased consumption on account of job creation and wage growth due to increased demand.

China's Investment Landscape

- ❑ China's equity market expansion is influencing global markets:
 - ❑ 4 of the top 10 global banks are from China
 - ❑ 6 of the top 10 companies in the Asia Pacific Ex- Japan are from China
- ❑ China is the world's best place to search for growth stocks.
- ❑ China has 68% of the world's mid-cap, high-growth listed companies in consumer, healthcare, and technology sectors

Growth Stocks by Country Distribution



Top 10 Global Banks

Rank	Company	Country	Assets (USD)
1	ICBC	China	\$4.21 trillion
2	CC Bank Corp.	China	\$3.63 trillion
3	Ag. Bank of China	China	\$3.44 trillion
4	Bank of China	China	\$3.26 trillion
5	JP Morgan Chase	U.s	\$3.10 trillion
6	MUFJ Financial Group	Japan	\$2.89 trillion
7	HSBC Holdings	England	\$2.65 trillion
8	BNP Paribas	France	\$2.65 trillion
9	Bank of America	U.S.	\$2.64 trillion
10	China Development Bank	China	\$2.47 trillion

Source: Bloomberg, L.P. [viii]

Top 10 Companies: Asia Pacific Ex-Japan

Rank	Company	Country	Market Value (USD)
1	Tencent	China	\$265.38 million
2	Alibaba	China	\$225.47 million
3	Taiwan Semi.	Taiwan	\$199.86 million
4	Samsung	S. Korea	\$175.91 million
5	AIA Group	Hong Kong	\$120.64 million
6	CC Bank Corp.	China	\$79.39 million
7	Ping An Insurance	China	\$57.15 million
8	China Mobile	China	\$55.06 million
9	Reliance Industries	India	\$52.91 million
10	Industrial Com. Bank	China	\$48.14 million

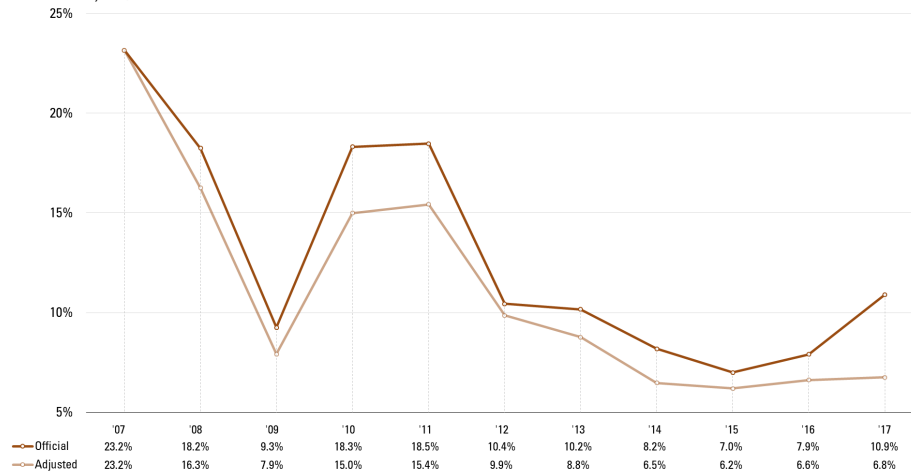
Source: Bloomberg, L.P. [ix]*

Is China Just a House of Cards?

Are China's GDP Numbers Fabricated?

The prior system was driven by provincial accounting and a tendency by local Chinese officials to inflate growth numbers to reflect their economic performance and enhance their chances for promotion. In recent years, the National Bureau of Statistics has started adjusting these numbers down to control for local bias, moving from the provincial reporting model to a more centralized accounting model.

China Nominal GDP Growth
Official vs. Adjusted, 2007 - 2017

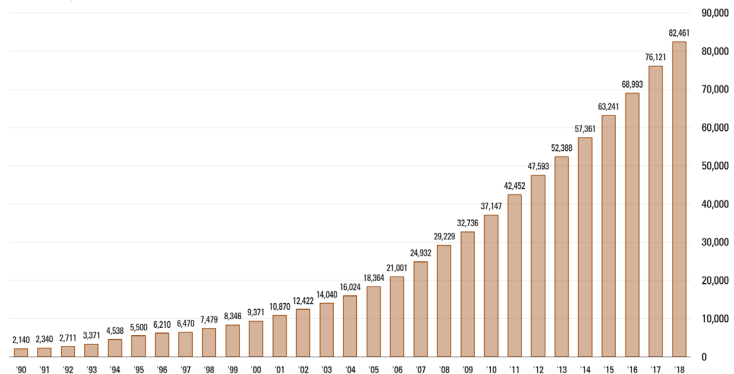


Source: Bloomberg LP, data as of 12/31/2017

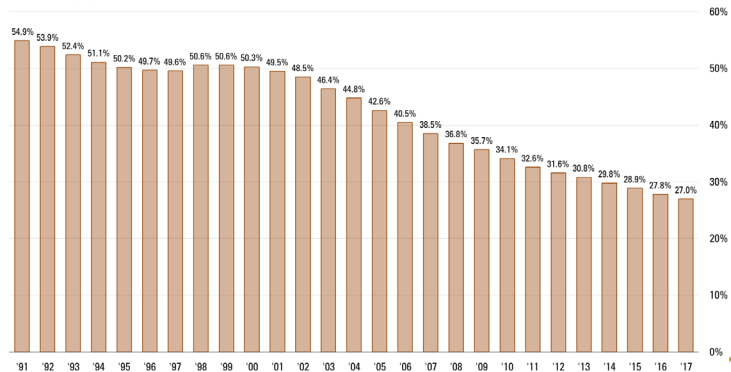
Are the New Numbers Real?

The revised system relies more on actual economic output and hard data that is difficult to fabricate, such as nominal wages and infrastructure spending. Nominal wages in China have been in a steady uptrend for more than a decade, in turn pushing low-end/low wage agriculture and manufacturing jobs to other countries such as Vietnam and India.

China Average Yearly Wages
Total in CNY, 1990 - 2019



China Employment in Manufacturing & Agriculture
% of total employment, 1991 - 2017



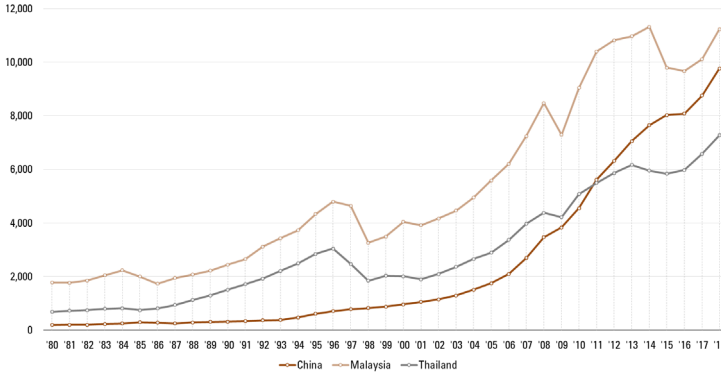
Source: National Bureau of Statistics of China, official data as of 12/31/2018

More Proof China's GDP is Real

Chinese GDP Per Capita Is Not Out of The Ordinary Comparably

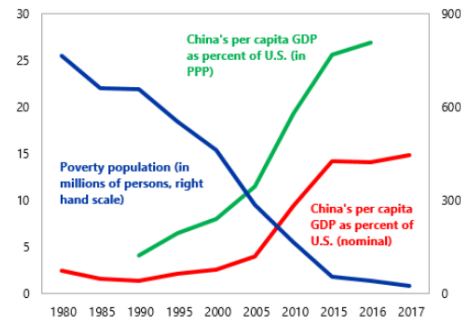
Using International Monetary Fund data and estimates, the Chinese economy is not out of the ordinary when compared to other comparable Asian countries, another indication that the move to centralize economic reporting is inspiring confidence.

GDP per Capita (current US\$)
China, Malaysia, & Thailand 1980 - 2018



Source: International Monetary Fund, World Economic Outlook (April 2019)

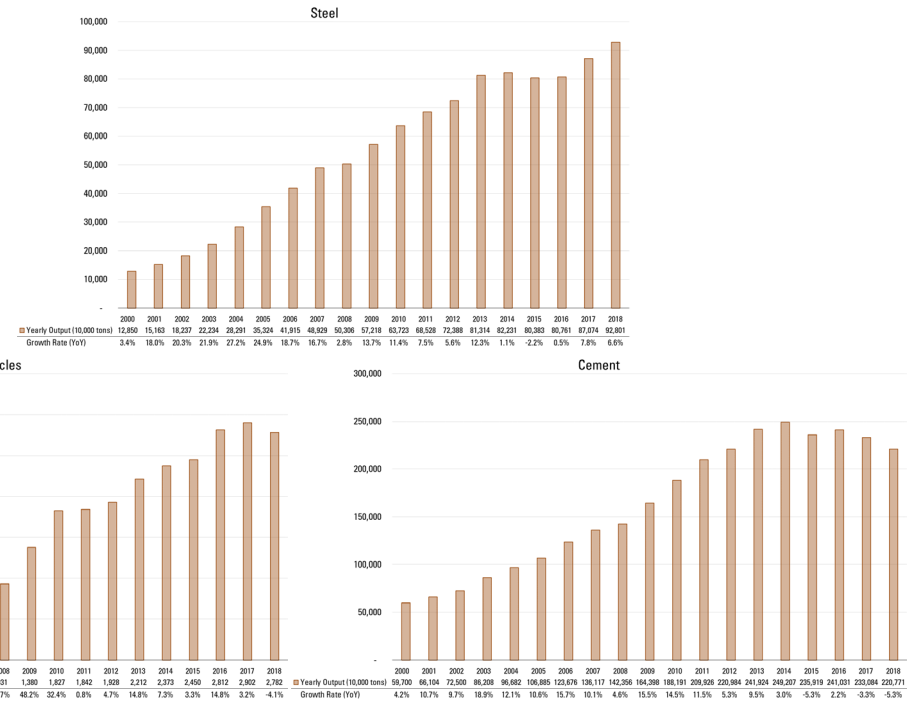
Growing from strength-to-strength Rapid growth means rising living standards.



Sources: CEIC, National Bureau of Statistics of China statistical yearbook.

Industrial Production

Chinese industrial production in core materials/products such as steel, cement, and cars/trucks remain strong; lending additional confidence to overall GDP growth numbers.



Source: National Bureau of Statistics of China, official data as of 12/31/2018

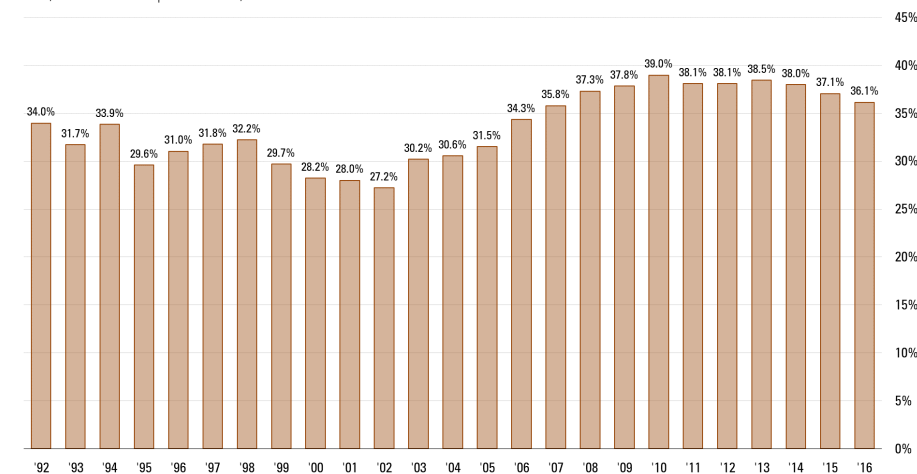
Unlocking the Chinese Savings Phenomena

Unlocking the Chinese Savings Phenomena

The savings rate in China is one of the highest in the world, trending higher throughout the 90s before peaking in 2010. The rate of savings has begun to moderate in recent years as household consumption and spending has accelerated. “Unlocking” the Chinese savings phenomena is one of, if not the most, important metric to watch for future economic expansion.

China Savings Rate

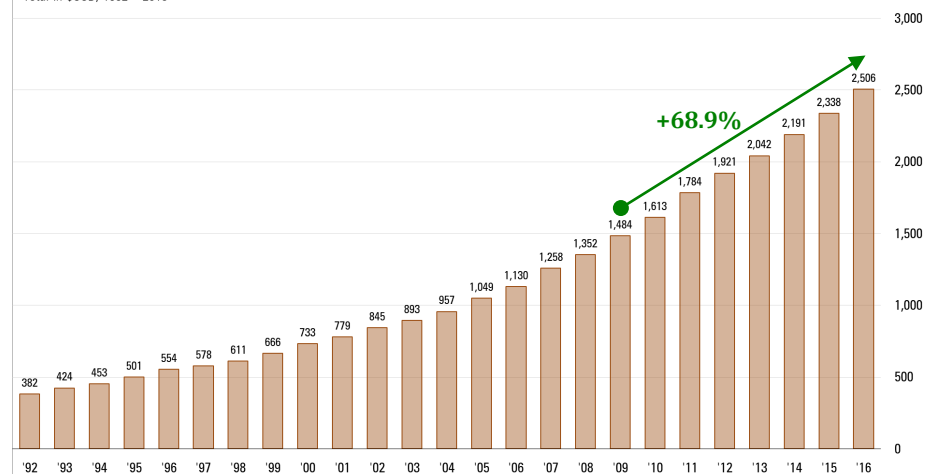
Total, % of household disposable income, 1992 – 2018



Source: National Bureau of Statistics of China, official data as of 12/31/2018

China Household Consumption per Capita

Total in \$USD, 1992 – 2016



Source: National Bureau of Statistics of China, official data as of 12/31/2018

Addressing Retirement & Healthcare as Impediments to Growth & Consumption

Addressing Two of the Biggest Hold-Backs to Increased Consumption

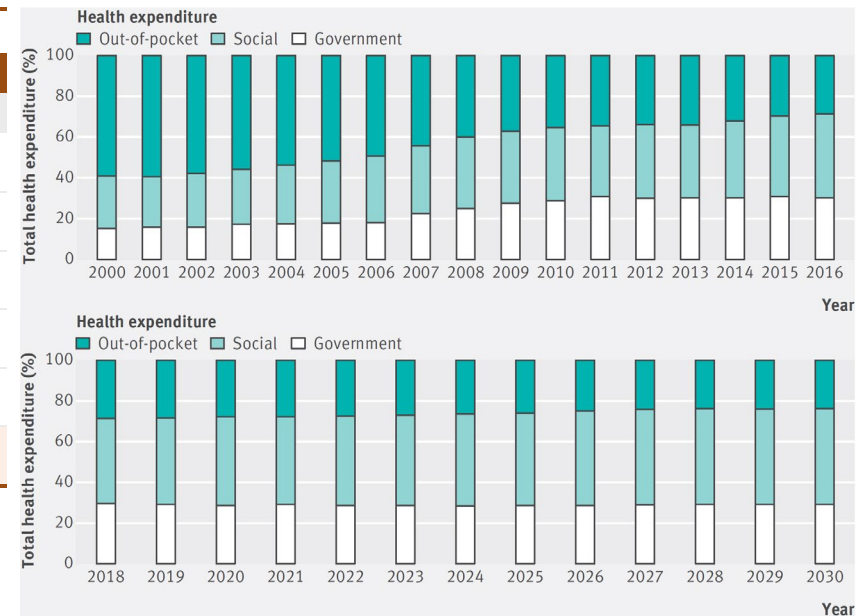
China has recently rolled out a more stable, Western-style pension policy for citizens, similar to our own Social Security system, which has dramatically stabilized and innovated health care for its citizens. To China's credit, the Chinese government has recognized these two issues as vitally important to future growth as China's youngest generations have given all indications they like to spend and consume.

China's Social Security System

Category	Contribution*		Description
	Employer Rates	Employee Rates	
Pension	Around 10%-22%	Around 8%	An individual can receive a pension based on the amount in their individual fund after retirement
Medical	Around 5%-12%	Around 2%	In the event of illness/non-occupational injury, an employee can have part of the treatment cost covered by medical insurance
Unemployment	Around 2%	Around 1%	In the event of redundancy, the employee may claim unemployment for a maximum of 24 months
Maternity	Around 0.5%-1%	—	During maternity leave, the employee receives reimbursement from this insurance fund
Work-related injury	Around 0.5%-2%	—	The work-related injury fund covers the cost of treatment should an occupational injury/illness occur
Housing fund	Around 5%-12%	Around 5%-12%	Designed to ensure that workers save to purchase housing

*The contribution amount in each category is calculated by utilizing the employee's payment base figure and multiplying it by the different percentages required by each local government entity.

Source: "China's Social Security System", China Briefing (9/25/2017)



Source: "Medical Research in China", British Medical Journal (2/14/2018)

What Are China A-Shares?

China A-Shares represent China's domestic onshore stock market, one that has been largely off-limits to non-domestic Chinese citizens until recently. The A-share market opens more opportunities for global investors to take part in China's dynamic economy that is taking shape as the country shifts away from exports and manufacturing and more toward innovation, consumer consumptions, and services.

A-shares are a much larger, more diverse, and liquid universe of companies than the offshore H-share market, that is more easily accessed by foreign retail and institutional investors.

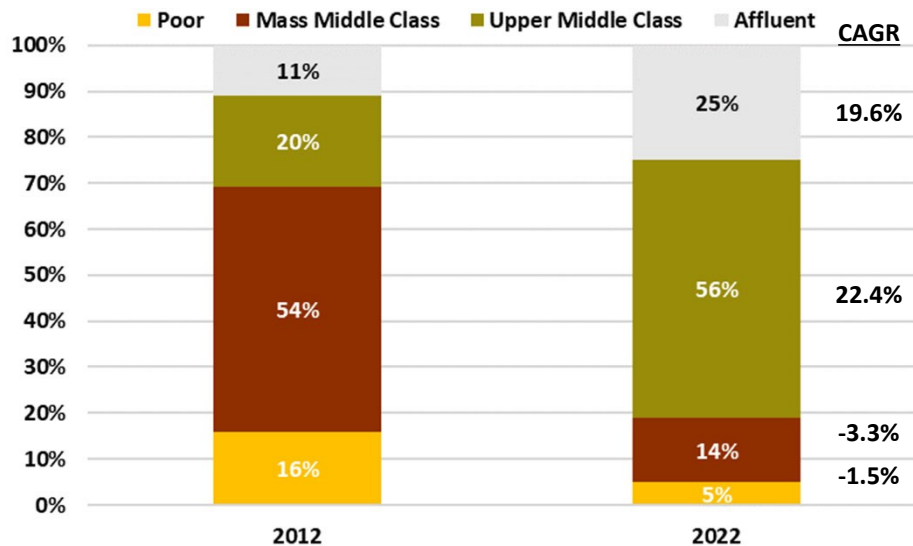
With a market cap of almost \$8.37 trillion USD, the 3,400 listed A-share companies now represent the second-largest stock market in the world, behind only the U.S. market.

Currently, 80% of A-share trading is done by China retail investors.

Why China A-Shares

- The magnitude of China's middle class growth is transforming the nation and its composition of private consumption; the rise of the upper middle class leads to higher income, which translates to a higher propensity to consume more.

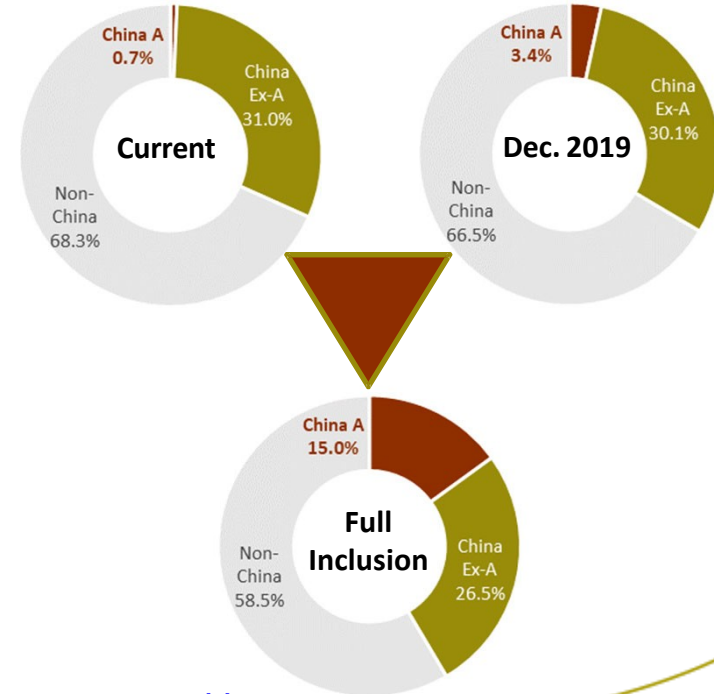
Urban Private Consumption by Income Segment: % of Tot. China Pop.



Source: McKinsey & Company [x]

- Increased A-share inclusion into the MSCI indices will drive positive fund inflows into the A-share market; total incremental fund inflows between June 2019 – December 2019 are projected to be \$80 billion USD.

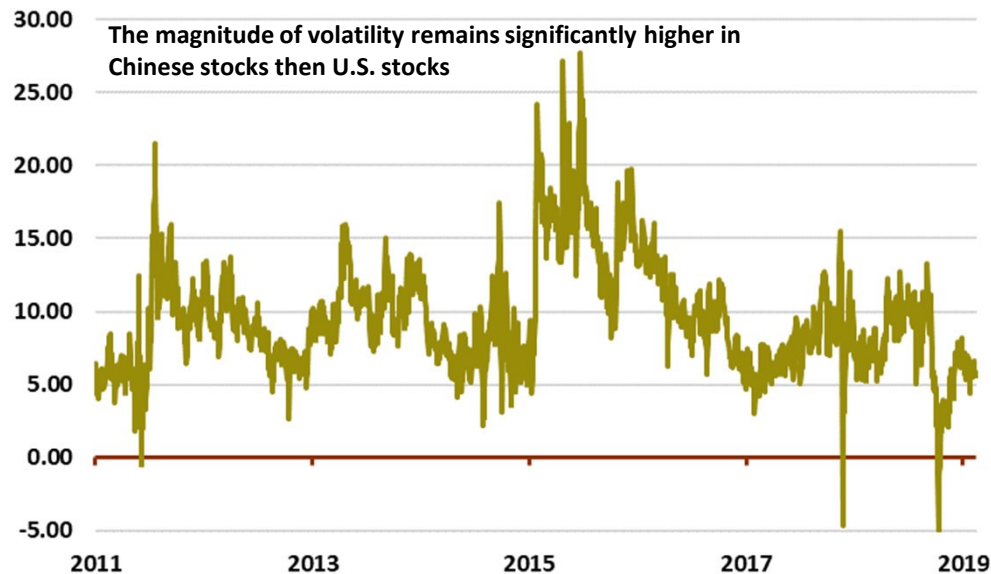
Benchmark Inclusion Into The MSCI EM Index



Source: MSCI, CICC [xi]

A-Share Market Nuances

Stock Market Volatility Spread: China vs. U.S.



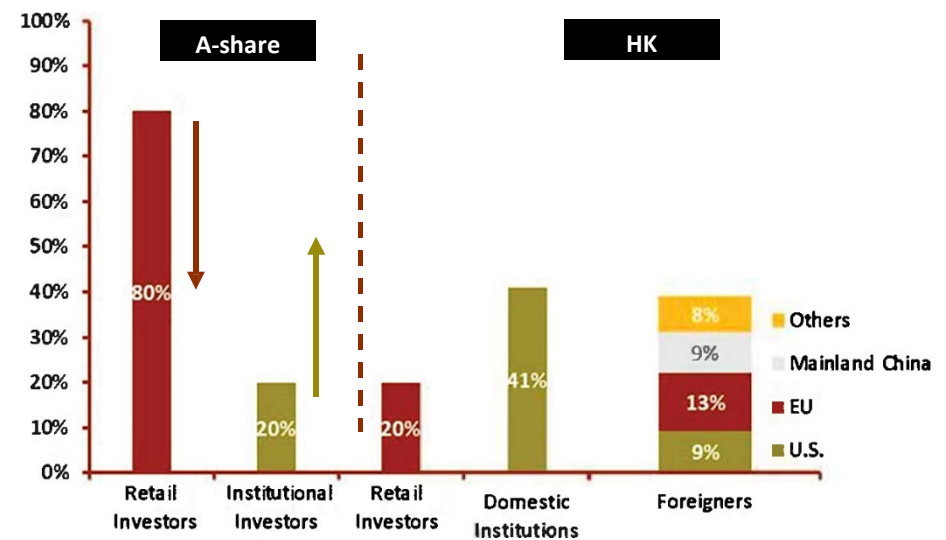
- ❑ The A-Share market is currently dominated by retail investors, and therefore leads to higher equity turnover:
- ❑ Due to the tendency of retail investors buying or selling stocks based on emotion, rather than fundamental valuations, the market is highly liquid and prone to volatility.
- ❑ China's universal capital gains tax of 20% means there is no delineation between short- and long-term capital gains.

- ❑ Currently, valuation is less important as the institutional investor (approximately 20% of investor base) bases decisions on relative valuation (P/E, P/B, PEG, Dividend Yield, etc.).
- ❑ Shareholders have no voting rights in the A-share market.
- ❑ Contrary to how the performance of U.S. based mutual fund managers are evaluated (quarterly and annually), China mutual fund managers are evaluated on a weekly basis due to the short-term trading mentality and higher equity turnover dynamics associated with the China-A share market; **this further supports the need to take an active role in the China-A share market versus a passive allocation.**

A-Share Market Nuances

- ❑ In order to protect domestic investors, the government administers trading halts “for the protection of investors” and to promote “the maintenance of an orderly market.”
 - ❑ Trading halts are typically implemented if a security’s price moves plus or minus 10% in a single trading day.
- ❑ If the government deems that a company is not running “sufficient operations,” (lack of profitability over a 2-yr. period) the company is forced to liquidate assets in order to make up the revenue needed to compensate losses.
 - ❑ A company running insufficient operations faces tighter regulation of stock price movement in the governments attempt to limit losses to retail investors.
- ❑ The necessity for A-Share companies to perform at benchmarks set by the government often result in the manipulation of goodwill on company balance sheets.
 - ❑ Management does not necessarily follow GAAP or IFRS accounting standards for the treatment of goodwill.
 - ❑ Management tends to test and revalue goodwill when its convenient to over, or understate, the value of total assets on its balance sheet.
- ❑ The Chinese Technology Innovation Board:
 - ❑ Created to allow the successful launch of tech IPOs
 - ❑ Circumvents the typical market protocol that only profitable companies are allowed IPO’s in the Chinese A-Share market
 - ❑ Is paramount for successful capital-raising leading to profitability of not yet profitable companies

A-share and HK Stock Exchange Trading Value Market Share



Source: Citi Group [\[xiii\]](#)

CICC's Global Network

CICC is a full-service investment bank with an extensive network covering 28 provinces and municipalities across China, and offices in six international financial hubs, including Hong Kong, New York, Singapore, London, San Francisco, and Frankfurt.

Mainland China

Hong Kong

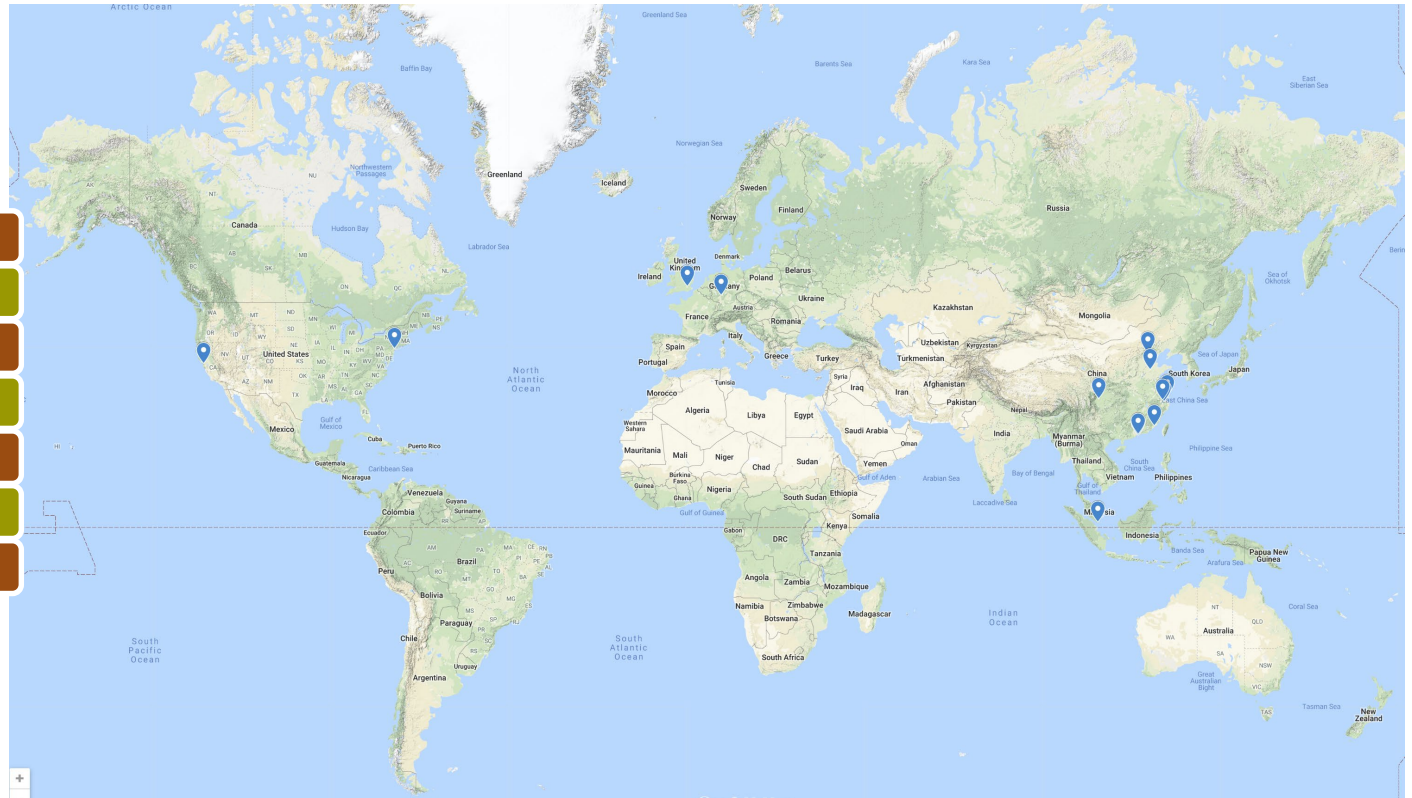
New York

Singapore

London

San Francisco

Frankfurt



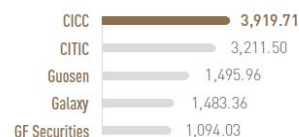
Source: CICC Equity Research Portal, as of 8/27/2019

Award Winning Capital Markets Team

Leveraging its distinct international DNA and vast team of industry experts, CICC has solidified its place as the premier China-focused investment bank.

A-share IPOs (1999 - 2017)

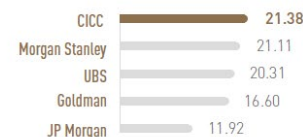
RMB100 Million



Note: underwriting amount refers to the sum of apportioned size of each deal
Source: Wind Info, as of Dec 31, 2017

Overseas IPOs by Chinese Companies (1997 - 2017)

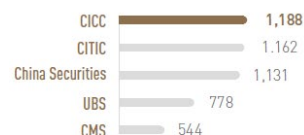
USD Billion



Note: underwriting amount refers to the sum of apportioned size of each deal
Source: Dealogic, as of Dec 31, 2017

No.1 Underwriter of Central SOE-issued Corporate Bonds by Size Underwritten

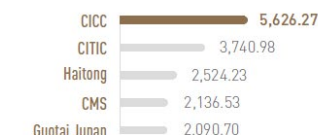
RMB100 Million



Source: Wind, from 2009 to 2017. Privately placed corporate bonds are not included

No.1 Chinese underwriter in investment-grade offshore USD bonds issued by Chinese issuers since 2015

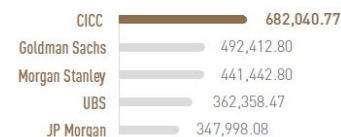
USD Million



Source: Bloomberg, 2015 - 2017; ranking of Chinese brokers by underwriting volume

No.1 in China M&A League Table Since 1997

USD Million



Source: Dealogic, as of Dec 31, 2017

Source: CICC Equity Research Portal, as of 8/27/2019

Frontrunner in M&As with High Client Diversity

Global No.1 in China M&As for 5 consecutive years

Maintaining No.1 position in domestic M&As and ranking No.1 in A-share M&A and reorganization deals in 2017

- China Resources – transfer of ~15% Vanke shares to Shenzhen Metro at RMB31.2 billion
- NARI Technology – acquisition of smart grid assets under State Grid via RMB26.5 billion share offering
- Zoomlion – sale of 80% stake in environmental industry subsidiary at RMB11.6 billion

Continuing in-depth overseas business development, with remarkable cross-border M&A performance

- GLP – USD16.1 billion privatization in SGX
- CEFC China – acquisition of Rosneft shares at USD8.0 billion
- Yancoal Australia – acquisition of Coal & Allied Industries from Rio Tinto at USD3.1 billion and JV establishment with Glencore at USD1.2 billion

Keeping leadership in Hong Kong market and creating value through industrial consolidation

- CNBM – HKD34.4 billion merger of Sinoma via share swap
- Taobao China – HKD22.4 billion investment into Sun Art Retail
- Alibaba – HKD19.9 billion privatization of Intime Retail

OUR AWARDS



CICC Equity Research

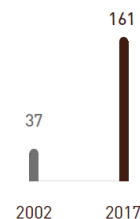
CICC's extensive coverage universe, rigorous methodology, independence, impartiality, and thoroughly professional approach have contributed to its reputation as a world-class equity research institution, earning top rankings in domestic and international analyst polls

AREAS OF COMPREHENSIVE EXPERTISE

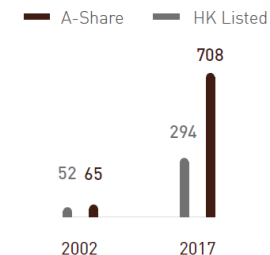
- Global macroeconomics
- Global investment strategies
- Global commodities
- Finance (banking, insurance, securities)
- Technology, media, the internet
- Real estate
- Energy (oil, gas, coal)
- Industrial materials (steel, construction materials, chemicals, nonferrous metals, paper and packaging)
- Heavy industry (construction and engineering, machinery, defense)
- Consumer discretionary (retail, home appliances, electronics, textiles, apparel, light industry, tourism, hotels)
- Consumer staples (food, beverages, agriculture)
- Health care
- Automobiles and auto parts
- Transportation (infrastructure, transportation systems)
- Utilities (IPP, environmental services, alternative energy, electrical equipment)

ACHIEVEMENTS

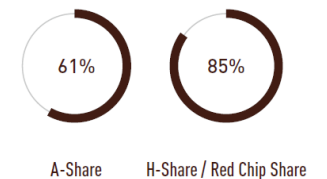
Rapidly Growing China Research Team



Listed Companies Covered by Research Team







Total Coverage of Listed Companies by Market Capitalization



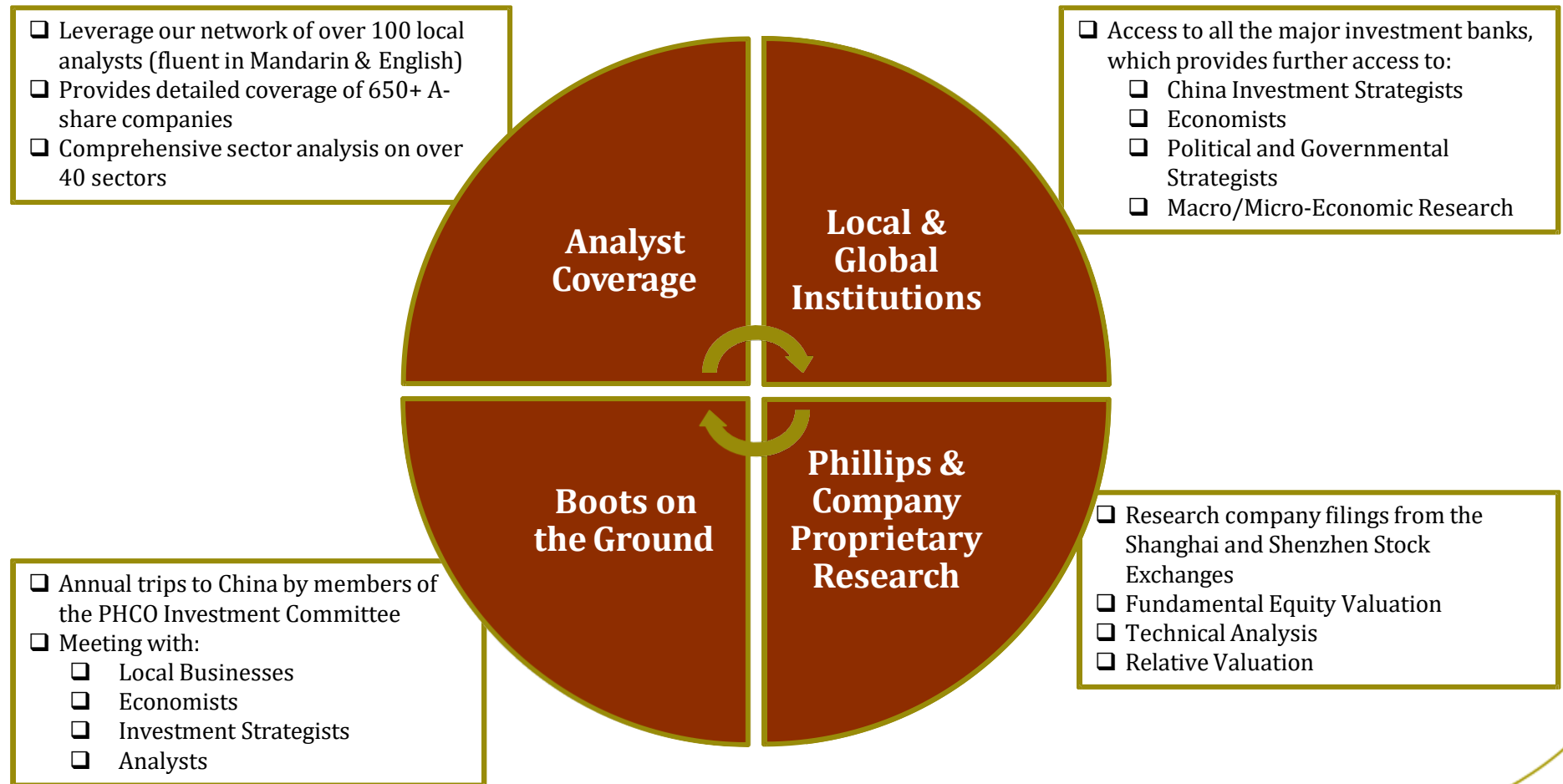
Note: As of Jun 30, 2018

Source: CICC Equity Research Portal, as of 8/27/2019

Investment Themes

Technology, Media & Telecom	Key Investment Themes	Phillips & Co. Target Area
	<ul style="list-style-type: none"> Local innovation upgrade cycle Growing access to smartphones, computers, and internet Expansion of technology into consumer and enterprise markets 	<ul style="list-style-type: none"> Vertical internet marketplaces & technology enabled services Processing and automation Big data and cloud computing IT outsourcing
Consumer Goods & Services	Key Investment Themes	Phillips & Co. Target Area
	<ul style="list-style-type: none"> Marginal propensity to consume more as disposable income grows E-commerce outgrowing traditional consumer facing models Convenience upgrade: D.I.Y. to D.I.F.M. 	<ul style="list-style-type: none"> Consumer products appealing to upgraded consumer demands Mobile-enabled online-to-offline models Logistics services for enhancing online-to-offline service models
Healthcare	Key Investment Themes	Phillips & Co. Target Area
	<ul style="list-style-type: none"> Growth of aging population Strong private spending and emerging prevalence of insurance driven growth Growing awareness and efficacy of traditional practices through adoption of new technologies 	<ul style="list-style-type: none"> Healthcare delivery and diagnostic platforms Consumer healthcare opportunities with strong brand differentiation Healthcare lifestyle upgrade in rural and large disease areas
Industrials/Defense	Key Investment Themes	Phillips & Co. Target Area
	<ul style="list-style-type: none"> Manufacturing upgrade cycle related to Belt & Road Transforming supply dynamics from low-end to high-end steel Expansion of roads, bridges, railways, and pipelines to western China 	<ul style="list-style-type: none"> Financial firms investing in Belt & Road projects Basic materials/metals used for upgrading steel from low-end to premium-quality Heavy machinery and logistics for enhancing the speed and quality of infrastructure projects

Research Process



A-Share Investment Mechanics

- ❑ Phillips & Company, through Pershing, BNY Mellon, and Citi Bank, has direct access to the Shanghai-Hong Kong Stock Connect, which allows foreign investors to purchase direct A-share companies on both the Shanghai and Shenzhen Stock Exchanges.
- ❑ BNY Mellon also has one of the largest FOREX trading desks on Wall Street which allows you to purchase local Chinese currency direct in your account at Phillips & Company.

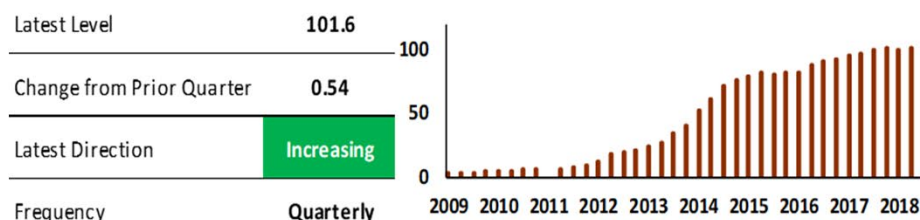
Trading Process



Key Indicators To Watch

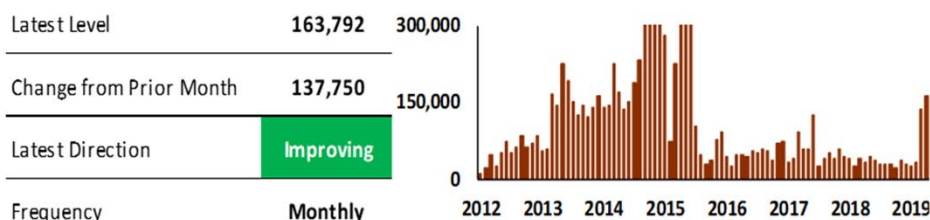
QFII Flows

As of 3/31/2019



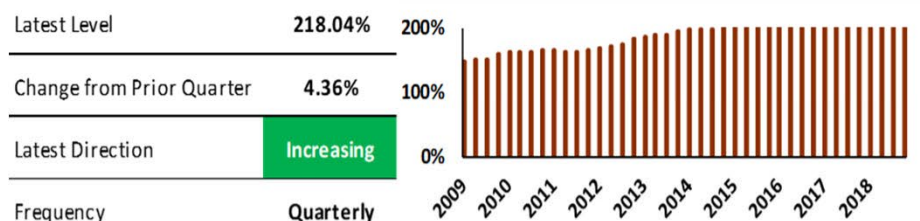
Brokerage Accounts

As of 4/30/2019



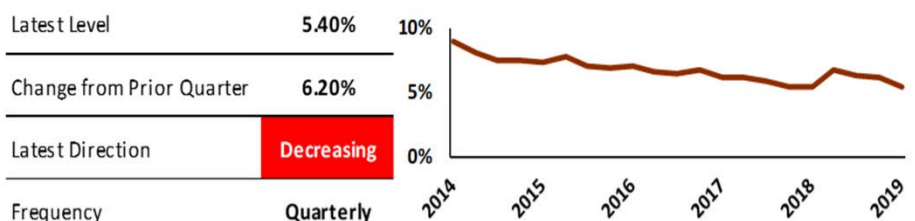
Total Social Finance as % of GDP

As of 3/31/2019



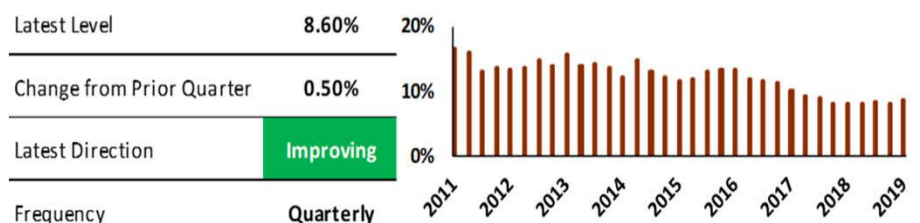
China Consumption Per Capita

As of 3/31/2019



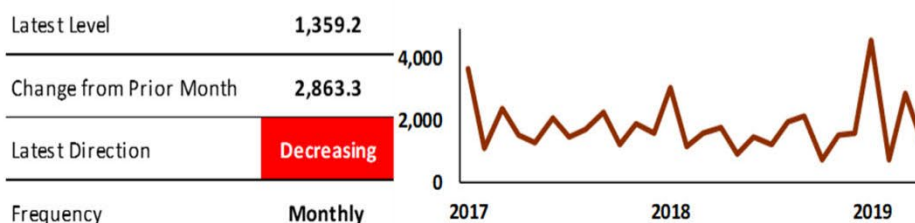
M2 Money Supply % Change YoY

As of 3/31/2019



China All-System Financing Aggregate

As of 4/30/2019



THANK YOU!

Resources

- I. <https://tradingeconomics.com/china/population>
- II. <https://data.worldbank.org/indicator/NY.GDP.MKTP.PP.KD?end=2018&locations=CN-US-IN-IP&start=2018&view=bar>
- III. <https://www.statista.com/statistics/270126/largest-stock-exchange-operators-by-market-capitalization-of-listed-companies/>
- IV. <https://am.jpmorgan.com/gi/getdoc/1383599288808>
- V. <https://worldview.stratfor.com/article/china-changes-gears-belt-and-road-initiative>
- VI. <https://worldview.stratfor.com/article/china-changes-gears-belt-and-road-initiative>
- VII. Source: CICC*
- VIII. <https://www.bloomberg.com/news/articles/2018-08-12/china-s-giant-banks-top-this-ranking-a-cause-for-concern>
- IX. Source: Bloomberg, L.P.*
- X. <https://www.mckinsey.com/industries/retail/our-insights/mapping-chinas-middle-class>
- XI. <https://www.msci.com/china>
- XII. <https://fred.stlouisfed.org/series/VXFXICLS>
- XIII. <https://www.citibank.com/mss/docs/China-Roadshow-deck.pdf>
- XIV. <https://www.lovemoney.com/gallerylist/52663/stocks-your-parents-should-have-bought-in-the-year-you-were-born>

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