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CAPITAL MANAGEMENT

November 2019 – China through the US Looking Glass III

Several of my colleagues have been visiting China over the last twelve months. Given our exclusive focus on the GEM consumer and our significant weighting in China we have been keen to determine the impact of US/Sino trade friction on the spending patterns of the man/woman in the street.

Our visits have basically shown that despite all the tariffs that have been imposed there has been little impact on consumption generally and even less on the companies in which we have an interest. Although still a sizeable part of the economy, export industries are no longer the engine of economic growth that they once were. It is the domestic economy which is now paramount.

But it is not just us that get this impression of buoyant consumption. Back in February I wrote that a number of US and multinational consumer-facing companies seem to be saying the same thing. Given that the tensions between Presidents Xi and Trump had only just started to escalate in August last year, several of you remained unconvinced. The view was that the imposition of tariffs would (or could) eventually curtail spending. This view had something to be said for it. So we waited.

Successive quarterly results from these same US and multinational companies have not shown the Chinese consumer battening down the hatches. If anything the reverse. The latest numbers for Q3 are no exception: consumer demand remains very healthy with luxury brands in particular appearing buoyant (BMW, Daimler, Estée Lauder, L'Oréal).

Although it comes as no surprise that sales in Hong Kong have weakened significantly, this has been more than offset by strength in Mainland demand. Several of the Q3 results (Nike, Las Vegas Sands and Kimberly-Clark) contained mention of further investment in China in order to meet this potential.

Trends that we highlighted in previous notes continue unabated:

i. clever ecommerce strategies continue to be key for success in China. Yum China (YUMC) reported that its 230 million digital members are the driver behind its growth. Strategic partnerships with Tmall and WeChat have helped Nike to grow its online business by 70%. Adidas has been busy these last two years building a digital hub in China. Starbucks just celebrated its 1 year partnership with Alibaba;

ii. premiumisation (it's still a dreadful word) whether it be fancier diapers/nappies (Kimberly-Clark), bouncier trainers (Nike) or more luxuriant cosmetics (P&G and Unilever) is also still paying dividends

Last week you may have seen Andrew Dalrymple's note written following a week he spent in China. The impact of tariffs was hardly mentioned during all the meetings he had with the consumer companies that interest us. John Ewart had a similar experience back in May.

As far as the Chinese consumer is concerned it seems to be a case of "Trade war?" "What trade war?"

Mark Martyrossian, Chief Executive Officer

Mark has been involved with Asian equities in a number of capacities since 1987. Initially in equity sales at Hoare Govett he then established and managed a trading book at Crosby Securities in Hong Kong before initiating a corporate finance business focused primarily on China. After the sale of Crosby Securities, he joined Warburgs with his China team.

On his return to London Mark founded a FCA registered fund management business which in 2003 started managing a number of Asian equity funds. He managed that business until 2016 when he sold his interest. Having known Andrew Dalrymple for 20 years and worked with him in Hong Kong, Mark joined Aubrey in 2017 as CEO.

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