

Technology: Reshaping China and creating future leaders

Bin Shi, Head of China Equities, led a presentation and panel Q&A session at GCC 2019 on January 8th that discussed how technology is rapidly changing China's economy and society and why investors may be able to find long-term opportunities as this phenomenon continues.

Host

Bin Shi, Head of China Equities

Panelists

Julius Luo

CFO of TAL Education

Yang Fengxue

Senior Partner at DHgate.com and

Founding Member of Hema

Opening the panel, Bin Shi reflected on 2018 as both a challenging year for China equity investors but also a year in which a series of underlying changes emerged as drivers of the Chinese economy.

Increasingly, these drivers have taken the lead as new forces for growth in China at a time when the influence of some of the traditional drivers, like fixed asset investment and exports, may have peaked.

Bin explained that technology is at the heart of this transition and the growth of technology during the past ten years has been very significant.

Bin highlighted three reasons for this development.

R&D and innovation are spurring growth

Chinese companies have significantly increased their spending on research and development during the past ten years from an estimated USD 49bn in 2007 to USD 265bn in 2017¹.

As a result, Chinese companies have become much more innovative, producing more patents as a share of GDP than Japan, and delivering a paradigm shift in the quality of their products and services.

¹ Source: OECD, WIPS, Morgan Stanley Research estimates, as of Dec 2017

Bin pointed out that one example of this shift is in the smartphone industry, where Chinese companies have delivered highly innovative products that have helped them compete more fiercely with international competitors.

China is ramping up automation

Demographic changes in China mean labor shortages and wage increases, so Chinese companies are responding by automating their manufacturing operations.

Bin pointed out that 'in just five to six years, many companies in China have significantly increased the usage of robots in their workflow.' China now leads the world in robot installations, and has become one of the world's largest markets for robotics systems.

Mobile internet is rapidly changing consumer behavior

Continuing the innovation theme, Bin showed that improving smartphones, growing user bases, and the widening range of online products and services are driving a rapid change in consumer behavior and increasing the share of total retail sales that are made online.

Compared to more developed markets, China is seeing a huge amount of online consumer activity. As Bin pointed out, 'that's because China doesn't have the baggage that developed markets do, which means Chinese companies can develop faster in new areas, like online retail. For example, in the US, offline retail dominates, which reduces the speed through which companies can shift online.'

Singles Day is a great example of how far Chinese companies have come and what their capabilities are.

Bin went on to say that 'Singles Day is a great example of how far Chinese companies have come and what their capabilities are.' Starting in 2009, this event has grown into the world's largest retail festival, beating total combined sales in the US-based Black Friday & Cyber Monday by more than three times.

While sales levels are significant, Bin pointed out that the fact that IT platforms running Singles Day can process more than 220,000 orders per second and deliver orders within two days shows that the supporting infrastructure is truly world class.





Bin went on to explain that while IT firms benefit from these trends, the impact of technology is not just limited to this sector. In fact, technology is having a major influence on other more traditional sectors and that investors can find opportunities as this influence spreads.

Education is one such sector and panelist Julius Luo, CFO of TAL Education, a leading education company in China, explained how his company has developed its business by investing heavily in R&D, developing technology - like a centralized online platform for education content - and using data to refine and improve their services and in-class experience.

One such example is the application of technology in the classroom. Julius explained that 'we use a lot of technology in our classrooms. If you go to some of our learning centers, you'll find two cameras in the front. These cameras record the class, analyse student engagement levels, and provide instant feedback to the teachers, who can then adjust the class and delivery.'

Offline retail is another area where the application of technology is rapidly creating new business models in China - with the recent development of 'New Retail' being one stand-out example.

Yang Fengxue acknowledged the growth of 'New Retail' and explained that investors should

look closely into these new models and look to the underlying technology driving the growth, such as customer and product tracking, because that's where there are interesting investment opportunities.

Looking back to the current state of the market, Yang advised attendees that now is an excellent time to look closely into potential investments in the China tech sector saying, 'at the current time, there are many truly valuable companies whose valuations have suffered because of the market, and that means it's an excellent time to look for investment opportunities.'

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Summary

China is slowing but opportunities remain

Summing up the presentation and Q&A session, Bin reminded the audience that while slower economic growth and trade tensions are dominating the news headlines, there's a lot happening in China related to fundamental structural changes in China.

As China changes, investors can find many exciting opportunities across a range of companies that are benefiting from the three driving trends discussed during the session, particularly in 'new economy' areas like IT, consumer, and healthcare.



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