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Riding The Dragon With JPMorgans China Region Fund

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Investing is hard, that goes without saying. Finding a great place to put your money while getting a good return is complicated in the safest of times. And that's talking about here in the US. When you take into account foreign rules and regulations things can get really complicated, especially for the retail investor. This does

not make investing in foreign companies something to avoid, quite the contrary. Investing in foreign business is a great way to gain exposure to profitable opportunities and diversify your account, it just needs to be done with care.

Take for instance China. China is the worlds 2nd largest economy, third if you count the EU as one economic arena, and is expected to grow at a rate above 6% for at least the next 2 years. It is the source of a healthy portion of the worlds trade goods, is one of the largest consumers of energy and,

despite slowing, still has one of the fastest growing economies on the planet. And it is one of the hardest places to invest, primarily due to tight restrictions put in place by the communist government of the People Republic of China.

If you doubt the difficulty of investing in China all I have to do is point out the large number of types of stocks representing business in or by citizens the country. There are China A shares, and B shares, and H shares, Red chips and P chips traded on exchanges in Hong Kong, Shanghai, Shenzen and Taiwan. Some



◀ shares are only priced in yuan and allowed to be owned by Chinese citizens, others represent companies doing in business in China, others companies doing business outside China. Some are companies owned by the communist government and still others represent a private business sector, private but tightly controlled by the government.

Just to touch base, A shares are those companies who operate in China, whose shares are listed in yuan and which are typically only available to citizens of China. These shares are only available to outside investment through a very few approved brokers. Everything else is a combination of yuan and dollar based issues including companies

operating inside and outside of China but incorporated outside the country for investment purposes.

Stock Funds Are The Best Approach To China

This is where indexing and funds based on those indexes comes into play. Indexing is well respected method of tracking the performance of a market or a sector of a market, funds based on indexes great ways to capture that performance. JPMorgan's closed end equity fund, the China Region Fund (JFC), is aimed at just that. Tracking and capturing the full spectrum of the Chinese market, both mainland A shares and those listed in other markets. The China Region Fund is different from

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most other types of Chinese based index funds, it is aimed at capturing the entire Chinese market, not just one sector. According to the website the funds objective is:

“Long term capital appreciation through investment primarily in equity securities of companies with substantial assets in, or revenues derived from the People's Republic of China, Hong Kong, Taiwan and Macau collectively, the China Region.”

The fund is benchmarked against two well known China indices, the MSCI Golden Dragon Index (80%) and the CSI 300 Index (20%). The Golden Dragon Index is a blend of 280 mid to large cap stocks including yuan and dollar based issues, red chips, p chips and those companies who shares are listed in Hong Kong and Taiwan. The CSI 300 is a listing of the top 300 A share companies listed on the Shanghai and Shenzhen stock exchanges as compiled by the China Securities Index Co, and is market cap weighted index. The JP Morgan China Region Funds targets the top stocks between the two, currently 197, creating the leading index based fund covering all forms of Chinese public companies.

Outlook Positive, Stimulus In The Air

Financials are currently 43.3% of total portfolio, followed by 18.3% in the information technology space. Industrials and consumer

◀ discretionary are each 8.3% with a smattering of holdings in health care, utilities, consumer staples, energy and materials. According to the funds managers this mix is well positioned to take advantage of the economic-slow-down/fiscal response cycle currently underway in China, a cycle not unlike the FOMC inspired rally the US market has seen over the past 8 years.

In the most recent portfolio review managers took note of several measures taken by the People's Bank Of China to support growth, as well as the growing chance new stimulus measure will emerge. Steps already taken include revised rules allowing easier access to investments in Hong Kong, cutting the reserve ratios for banks and stimulus measures aimed directly at Chinese companies operating at home and abroad.

Since the last portfolio update was released further developments, including a fresh round of weakening data, has renewed speculation stimulus measures will be increased. The data, including weak inflation and manufacturing figures, has already led the People's Bank Of China to lower its growth forecast for 2015, still 7%, the second time in 6 months and a sign the bank may be poised to move again. Analysts at JPMorgan had this to say in respect to the data "We expect China to continue easing policy as the domestic economy falters... markets had previously factored in the latter (economic weakness) but not the

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former (policy response)... Given the policy sensitive nature of the market, we expect that this impetus means that the rally will continue..."

Another positive is the expected inclusion of mainland Chinese "A" shares in the MSCI global benchmark indices, shares not currently included and why the JPMorgan China Region Fund is partially based on the CSI 300. This move is expected to be completed in 2016 and could add as much as \$1.7 trillion of liquidity to Chinese markets as fund managers around the world buy in to keep their portfolios balanced. As of yet there are some issues to be resolved but, according to information posted on their website, MSCI is moving forward with the plan and intends to form important partnerships with Chinese regulators in order to help the process along. "Recognizing the significant progress to date and ongoing reform efforts, China A-shares will remain on the 2016

review list for potential inclusion into Emerging Markets,"

The China Region Fund Is Undervalued

Looking at the fund from a value perspective it is undervalued. Net asset value is listed as \$23.75 on the funds website, a near 20% premium to recent lows near \$20. Looking at the fund in terms of market cap it is also trading at a discount, about 18% when compared to portfolio value, not really a surprise given the rapid rise in Chinese stock values over the past year. The rapid rise, 100% over the first half of 2015, coupled with ongoing fears of economic slowdown, have allowed the Chinese market to get well ahead of itself and is providing an entry for US value investors.

Over the past 10 years, taking into account the 2008 global meltdown, asset value is looking pretty steady. The fund has shown a year over year increase in NAV for the past five years, the past year more than 50%, and based on outlook will continue to do so into the coming year. China itself is expected to grow at a rate of at least 7% in 2015 with that edging down only slightly in 2016. With this in mind it is only reasonable to expect values of Chinese assets to grow. The bottom line is that China is a large, growing economy with ample investment opportunities and the JPMorgan China Region Fund is an attractive way for US investors to gain exposure.

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