# Weekly Market **Commentary**

**January 21, 2020**

## China Outlook | 2020

Gregory J. Hahn, CFA
ghahn@winthropcm.com
317.663.7510

Adam Coons, CFA
acoons@winthropcm.com
317.663.7502

Lance Bertsch, CFA, FRM
lbertsch@winthropcm.com
317.660.7257

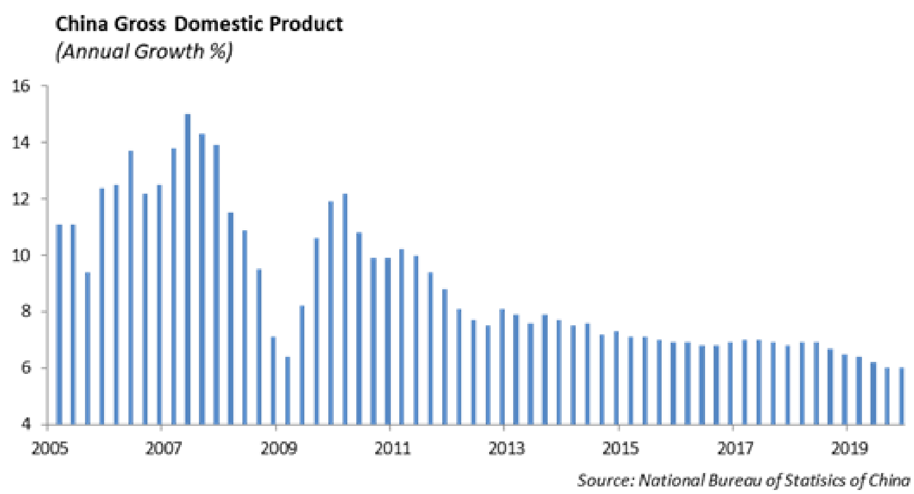
Freddy Lavric
flavric@winthropcm.com
317.663.7505

Charles Kovarik
ckovarik@winthropcm.com
317.663.7503

www.winthropcm.com

With the first phase of a U.S. – China trade deal completed, we believe the economic growth prospects for China will remain challenging as global growth remains subdued and China digests its growing debt burden. However, structural shifts in China's economy will allow for accelerated growth prospects once these challenges are addressed. Ultimately, China is the engine for global economic growth and addressing phase two trade issues will be important to getting the engine firing again.

China confirmed last week that its economy, the second largest in the world, grew at its slowest rate of growth in the past 29 years. China's GDP growth slowed to a pace of 6.1% year-over-year according to the release from the National Bureau of Statistics as trade pressures and business confidence declined. The pace of growth, which was lower than the 6.8% pace in 2018, still fell within the government's established range of 6.0% to 6.5% for 2019.




We expect this slow growth economy will translate to positive but lower returns for the china stocks. Given the reduced amount of stimulus in the system last year, we expect the Heng Sang Index (HIS) to return 6% - 9% for the year. The HIS is heavily weighted to the financial sector, and we expect regulatory changes in banking to weigh on over all returns for China stocks.In addition, China's economy and financial system is suppressed under the weight of huge debt burden which further impacts growth and business activity.

### China's Debt Problem

Like the U.S. which has federal and municipal debt, China utilizes both federal and local debt to finance its government programs and infrastructure spending. We estimate that gross federal debt has increased modestly to roughly $6.0 trillion, while China's local debt has ballooned an additional $6 trillion. While the general government debt amounts to 50% of GDP, when combined with local debt the ratio surges to over 100% total debt as a percent of GDP. Tax revenue and the returns on its infrastructure projects that were built with borrowed money aren't enough to pay down this debt. China has over $500 billion of debt coming due over the next two years that requires refinancing of government, bank loans and local debt. If China is ever perceived to have trouble accessing the public markets for its debt, it will increase borrowing costs.

## China Exposure in WCM's Asset Allocation

We currently utilize the SPDR S&P China ETF (GXC) in our Tactical Allocation and Core Sector Series Models. GXC has a .59% expense ratio and a 1.53% distribution yield. The top 10 holdings represent over 48% of the fund which has 731 total holdings. Alibaba and Tencent Holdings are the two largest holdings representing 13.8% and 11.6% respectively. The fund is invested in equities in Hong Kong and China representing 76.7% and 22.1% respectively.