REOPENING THE CHINA DISCUSSION

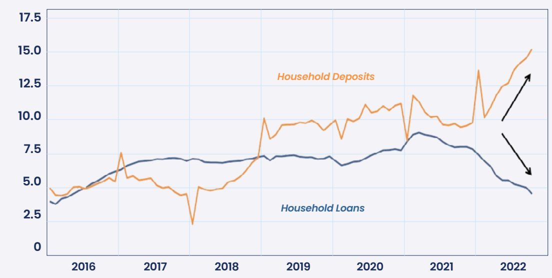
Investing in China has become an even more polarizing topic of late. The omnipresent concerns remain: perceived financial system vulnerabilities, geopolitical risk (Hong Kong, Taiwan, Xinjiang, etc.) and opacity emanating from the tightly-controlled flow of information. In recent years, a host of new issues and challenges have emerged. With President Xi Jinping consolidating power atop the Chinese Communist Party (CCP) following October's congress and exceedingly rare public protests breaking out in response to zero-COVID policies, it is an opportune time to revisit the investment case for Chinese assets.

When analyzing the prospects of any asset class, it is imperative to consider both short-to-medium term factors as well as longer-term ones. Frequently these temporal assessments can point in opposing directions. And while high conviction views make for more compelling stories, in most cases our research does not produce a blanket "good" or "bad" rating, but instead attempts to determine whether the outlook is improving or deteriorating.

For China, our short and longer-term views have been at odds with one another for a few years. For the former, monetary tightening squeezed financial conditions and pushed the property sector to the edge of default. A regulatory overhaul of private internet companies resulted in much more constrained business models and arguably dented entrepreneurial spirits. The trade war with the US caused unnecessary economic losses for both sides. More recently, COVID-zero policies have depressed virtually all facets of economic activity.

These immediate challenges had to be weighed against a more constructive long-term outlook. With a burgeoning middle class, China is transitioning to a more sustainable domestic demand-driven growth model. The country's sheer scale makes it nearly impossible to displace as the nucleus of global supply chains, but importantly, China no longer competes solely on low-cost manufacturing. Significant investment has been directed towards moving up the value chain, and focus is steadily shifting from duplication to innovation. Additionally, as the country's financial sector continues to gradually liberalize and open to foreigners, the mismatch between China's economic heft and under-representation in global indices and investment portfolios should erode over time.

Lockdowns have caused a surge in Chinese household savings
Annual Change in CNY Trillions



Sources: Macrobond, Alpine Macro, PBoC, Forstrong Global Asset Management

So the question now is, have recent events changed our views for better or worse? The short answer... both. While Western news media has sensationalized the recent protests, they are nonetheless emblematic of brewing public exasperation with COVID-zero restrictions. The CCP is likely to forcefully douse dissent, while quietly continuing to decrease the stringency of public health measures. Fears of a Tiananmen Square-type incident are wide of the mark. And although China's reopening will be a prolonged process, there are numerous green shoots emerging. Monetary and fiscal policy have turned accommodative and macroprudential measures to address property sector stress are being deployed. Per the chart below, already high Chinese household savings rates have surged during lockdowns, making a burst of pent-up demand highly likely in 2023.

Looking past cyclical factors, the long-term investment case for Chinese assets has downshifted somewhat. The positives remain, but it may be a bumpier path along the way. There was some optimism that the Biden administration in the US would take a less hawkish approach to China than their predecessors. While brash rhetoric has cooled down, tangible actions have not. The latest restrictions on selling US intellectual property to China are a prime example; lacking the headline fodder of "trade wars" but arguably having a more profound impact. The US ultimately cannot contain China's development, but it can throttle it to an extent. Additionally, the appointment of Xi loyalists to the CCP Politburo leaves little room for dissenting opinions and weakens checks and balances in the Chinese political system. With short and longer-term outlooks moving in opposite directions yet again, Chinese stocks currently offer more of a tactical opportunity than a secular one.

GLOBAL STRATEGY OVERVIEW

CASH

Rising money market yields raise the appeal of cash and equivalents amidst the current volatile market environment. However, on an inflation-adjusted basis, cash yields remain negative, while numerous equity and fixed income asset classes now offer attractive real yields. We have elected to maintain cash near neutral levels this quarter.

BONDS

There are a number of pockets within global bond markets which look increasingly attractive. Spreads on sub-investment grade US corporate bonds and loans have widened materially, despite very low default rates, relatively healthy fundamentals and low refinance risk. We remain overweight US corporate debt in client portfolios.

EQUITIES

Sentiment towards equities remains depressed as investors continue to grapple with tightening financial conditions and an array of geopolitical headwinds. However, valuations and dividend yield remain amongst the best predictors of long-term equity returns, and both have undergone a significant restoration this year. Equity positioning remains overweight and has been modestly increased this quarter.

OPPORTUNITIES

Hong Kong should see an economic boost from the recent easing of COVID lockdown restrictions, but numerous challenges remain. Specifically, imported (and tightening) US monetary policy and less of an onus for US-listed Chinese stocks to move their primary listings to HKEX detract from the investment thesis. Hong Kong stocks have been liquidated in client portfolios this quarter.

FORSTRONG
GLOBAL ASSET MANAGEMENT INC.

STRATEGY DASHBOARD: Q4 - NOVEMBER 2022

FORSTRONG STRATEGIES	INCEPTION DATE	1 MONTH	YTD	1 YEAR	3 YEAR	5 YEAR	10 YEARS	SINCE INCEPTION
GLOBAL SERIES								
Global Income	30/06/08	2.10%	-9.14%	-7.82%	0.08%	1.51%	5.32%	6.76%
Global Balanced	30/06/03	1.75%	-12.42%	-11.21%	2.05%	2.75%	6.62%	6.45%
Global Growth	30/06/03	3.14%	-13.67%	-12.28%	3.97%	4.12%	8.35%	7.58%
Core Income	30/06/08	1.70%	-8.20%	-6.86%	0.85%	1.96%	4.51%	5.77%
Core Balanced	30/06/03	1.73%	-8.86%	-7.82%	3.37%	3.51%	5.98%	6.64%
Core Growth	30/06/03	2.96%	-10.36%	-9.20%	5.15%	4.65%	7.40%	7.57%
GLOBAL EQUITY								
Emerging Markets Equity Focus	31/01/19	-5.38%	-17.88%	-17.56%	-2.17%	-	-	-1.68%
Global Ex-North America Equity Focus	31/12/19	1.74%	-17.57%	-17.26%	-	-	-	-2.16%

* Performance as of October 31th, 2022

Performance statistics for ETF Managed Portfolios are calculated from documented actual investment strategies as set by Forstrong's Investment Committee and applied to its portfolios mandates, and are intended to provide an approximation of composite results for separately managed accounts. Actual performance of individual separate accounts may vary with average gross "composite" performance statistics presented here due to client-specific portfolio differences with respect to size, inflow/outflow history, and inception dates, as well as intra-day market volatilities versus daily closing prices. Performance numbers are net of total ETF expense ratios and custody fees, but before withholding taxes, transaction costs and other investment management and advisor fees. Past investment results provide no indication of future performance. Future returns are dependent on the general investment environment, the nature of the investment mandate and specific portfolio risks. A rate of return for one year or less is not annualized.