MIRAE ASSET
Global Investments

New China: Impact of the Chinese Consumer

Shanghai, China

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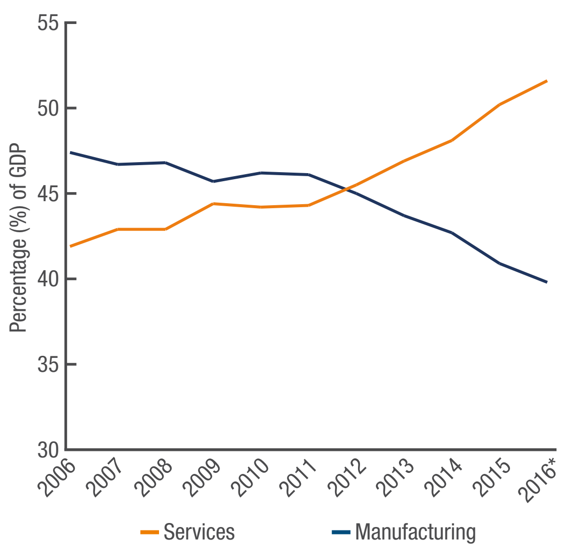
The transition of the Chinese economy from a manufacturing-led growth model to a consumer services-led growth model is widely expected to continue to create secular growth investing opportunities. However, the transition, thus far, has not been easy or straightforward. Even as China's growth is expected to slow down as government reforms are being made to shift the economy towards consumer spending, investors remain focused on China's stock market. Yet, China's stock market, representing less than 15% of household financial assets,[1] has only a small impact on Chinese households and therefore, the Chinese economy. Investors need to keep an eye on the bigger picture.

The Two Chinas

China's economy is moving in two different directions. "Old China", which is dominated by state-owned and heavy industries such as manufacturing and construction, is slowing down. "New China", on the other hand, with its innovative companies and focus on middle class consumption, has experienced resilient and even robust growth, in spite of slower growth in gross domestic product (GDP) and short term stock market volatility.

In 2006, Old China, as represented predominantly by the manufacturing industry, constituted 47.4% of China's GDP. Today, the manufacturing industry has contracted to 39.8% of the country's GDP.[2] Meanwhile, New China, as represented by the service industry, has been rising steadily. In 2016, the service industry accounted for more than half of China's GDP, rising to 51.6%, up from 42.9% a decade ago (see chart 1).

Chart 1: The Service Industry Now Accounts for Most of China's GDP



*Estimate. Source: National Bureau of Statistics, CIA World Factbook.

> New China, with its innovative companies and focus on middle class consumption, has experienced resilient and even robust growth.

[1] The Economist, June 2015.
[2] CIA World Factbook, as of 2016.

The shift from the manufacturing sector to the services sector is an indication of China's progress in transitioning towards greater domestic consumption. As Old China may be stalling, New China is becoming an important engine of economic growth, especially as it pertains to job creation and middle class expansion. New China employs more than 300 million people, the largest share of the country's 775 million workers.[3]

New China vs. Old China*

NEW CHINA	OLD CHINA
Internet/E-Commerce	Heavy Machinery
Clean Energy	Energy (Coal)
Beauty/Personal Care	Textiles and Apparel
Healthcare	Steel/ Metals
Education	Chemical Materials
Travel & Tourism	Railways, Shipping and other Transportation
Financial Services/Insurance	Rubber and Plastics

*A representative sample of industries, not a full list.

New China's Growth Engine — The Consumer

New China is driven by an expanding and wealthier middle class population. Today, more than 46% of Chinese households are considered to be middle class. By 2020, 60% of Chinese households are expected to fall into this middle class category.[4] In absolute terms, the size of the Chinese middle class is even more impressive. The middle class in China will grow to 303 million by 2020, up from 218 million in 2015 (see chart 2). To put that figure into perspective, the Chinese middle class is approximately the size of the entire US population.

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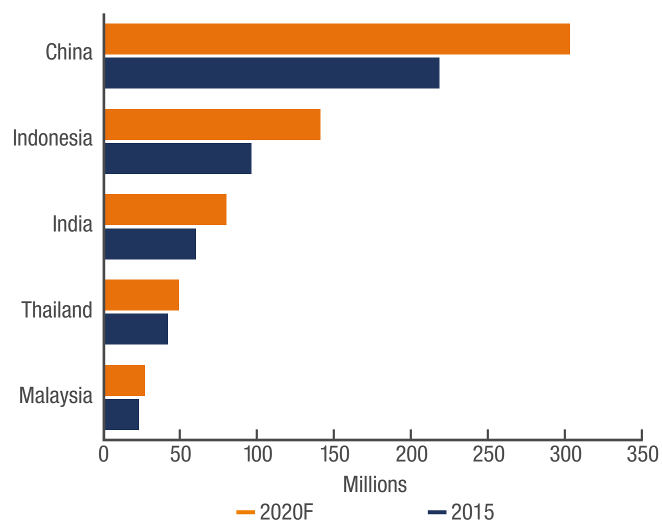
Chart 2: China Has One of the Fastest Growing Middle Class Populations in Asia



Source: BCG, EIU, Mirae Asset. Middle class includes the upper middle class. Middle class in China: Urban households with annual disposable income over $8,000.
Forecasted numbers are projections and not guarantees.

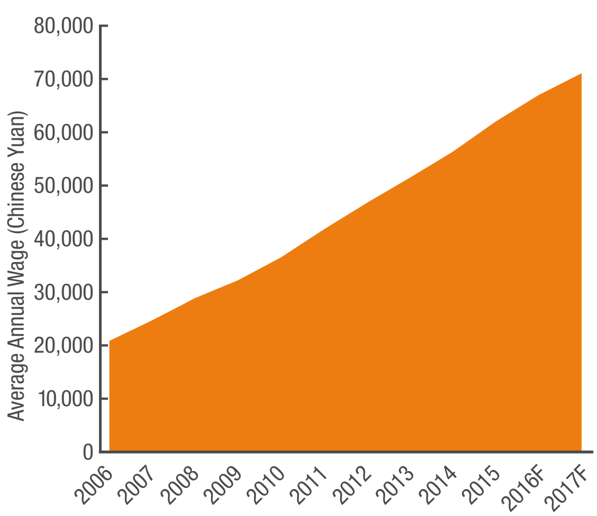
[3] Bloomberg Business, January 2016.
[4] BCG, EIU, November 2016. Middle class includes the upper middle class. Middle class in China: Urban households with annual disposable income over $8,000.

Consumer spending, underpinned by income growth, remains steady and strong even if the Chinese economy is not growing as fast as it once was.

Supporting the growth of the middle class is rising income. Income is one of the most important determinants of middle class consumers' spending decisions. In China, the average annual wage of an urban household grew at a compounded annual growth rate of 13% from 2006 to 2015 (see chart 3). This upward wage trend is expected to continue, albeit at a slower pace, as the economy shifts from low-wage manufacturing industries to better-paying service and high-tech industries.[5] And as wealth increases, consumption is likely to follow.

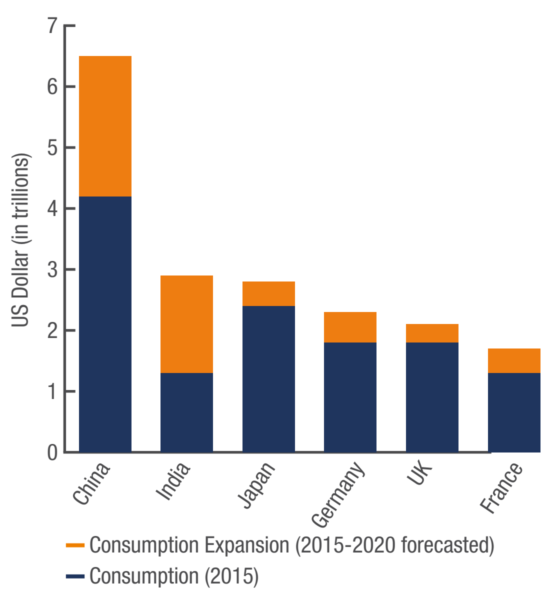
Consumer spending, underpinned by income growth, remains steady and strong even if the Chinese economy is not growing as fast as it once was. According to global research firm Boston Consulting Group (BCG), even if China's economy declines below its official target of 6.5% for the next five years, consumption is still projected to grow 9% annually during the same time period. The Chinese consumer market is anticipated to expand by $2.3 trillion over the next few years to become a $6.5 trillion market by 2020 (see chart 4).

Chart 3: Chinese Household Wages Continue to Rise



Source: National Bureau of Statistics, Korn Ferry Hay Group, Mirae Asset. F=forecasted. **Forecasted numbers are projections and not guarantees.**

Chart 4: China is Anticipated to Become a $6.5 Trillion Consumer Market



Source: Economist Intelligence Unit; BCG analysis.
Assumes annual GDP growth of 5.5% for China.
Forecasted numbers are projections and not guarantees.

[5] Boston Consulting Group, "The New China Playbook", January 2016.

Investing for Success In New China

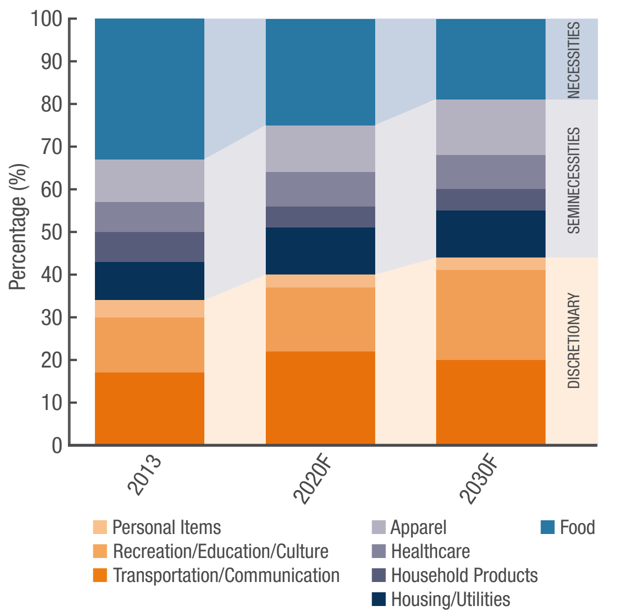
The Chinese consumer is evolving and their spending patterns are fueling a consumption boom in certain sectors and industries. Many of today's consumers in China have moved their purchasing beyond daily necessities such as food and clothing and are allocating more of their spending to discretionary items such as technology, education, recreation and travel (see chart 5).

Consumers in China tend to be younger with spenders under the age of 35 accounting for 65% of consumption growth.[6] In addition to being younger, Chinese consumers are also more tech-savvy and educated with the number of higher-education graduates increasing from 3.8 million to more than 6.8 million in the past decade.[7]

E-commerce

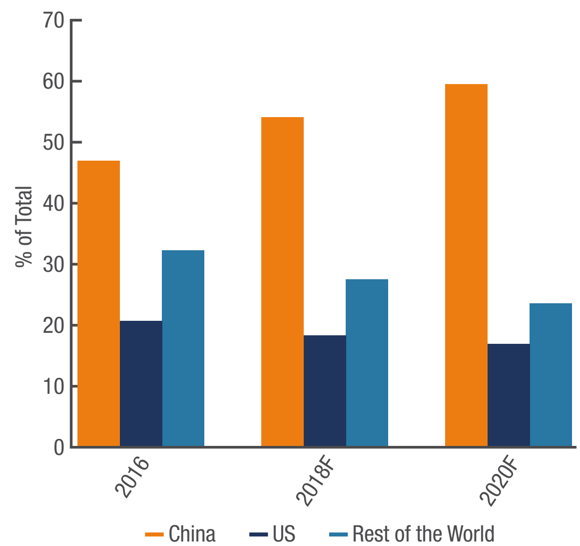
E-commerce is a prime example of an industry that has embraced and benefitted from New China. BCG refers to the growth in e-commerce as one of the most revolutionary changes in the Chinese consumer economy. China is now the world's largest e-commerce market and accounts for 47% of the world's retail e-commerce sales.[8] China should continue to cement its number-one position in the near future as retail e-commerce sales are projected to soar to $2.4 trillion, or 60% of the world market, by 2020 (see chart 6). This is more than twice the sales in the US, UK, Japan, Germany and France combined.

Chart 5: Chinese Households are Allocating More of Their Spending to Discretionary Categories



Source: McKinsey Global Institute.
F=forecasted. **Forecasted numbers are projections and not guarantees.**

Chart 6: China is the World's Largest Retail E-commerce Market



Source: eMarketer, Aug 2016. China excludes Hong Kong. Note: includes products or services ordered using the Internet via any device, regardless of the method of payment of fulfillment; excludes travel and event tickets.
F=forecasted. **Forecasted numbers are projections and not guarantees.**

[6] Boston Consulting Group, "The New China Playbook", January 2016.

[7] National Bureau of Statistics, data through 2015. Regular institutions of higher education include full-time universities, colleges, institutions of higher professional education and institutions of higher vocational education.

[8] eMarketer, August 2016.

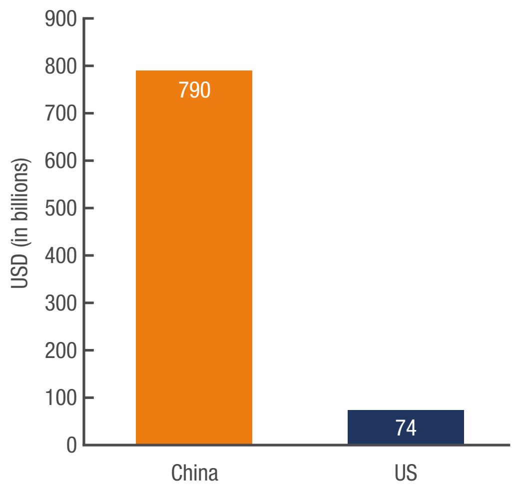
The top Chinese e-commerce companies who dominate in e-commerce have online platforms that are content-rich, with user-friendly websites and mobile applications, and a fast, reliable delivery service.

The e-commerce boom in China is creating historic opportunities to invest in local internet companies. However, e-commerce companies will need to do more than just provide customers a platform to shop if they want to win in New China. In China, a majority of shopping is done not only online but also on a mobile device. In 2016, Chinese consumers made $790 billion in mobile payments, around eleven times more than US consumers (see chart 7).

The top Chinese e-commerce companies who dominate this space have an online platform that is content-rich, with user-friendly websites and mobile applications, and a fast, reliable delivery service. Strategic partnerships can also provide a competitive advantage. One of China's largest e-commerce companies has been able to respond to customers' mobile shopping preferences and boost their mobile orders by partnering with one of the country's most popular instant messaging applications to access and grow their base of active users.

Top companies in this space tend to have first leader advantage in business-to-consumer (B2C) strategy and are at the forefront of innovation in mobile payment solutions. In a market where there is a proliferation of counterfeit goods, the most successful companies have been able to earn and keep the trust of their customers by offering high-quality, authentic products at competitive prices. These leading e-commerce companies are focused on cultivating brand loyalty through customer satisfaction, building large scale fulfillment centers and investing in a comprehensive and dependable logistics network with their merchants and delivery partners. As a result, successful Chinese e-commerce companies in New China have garnered investor confidence by increasing their base of active buyers, growing mobile revenue and improving their monetization rates.

Chart 7: China is a Leader in Mobile Payments



Source: McKinsey Global Institute, "China's Digital Economy: A Leading Global Force." Data as of 2016.

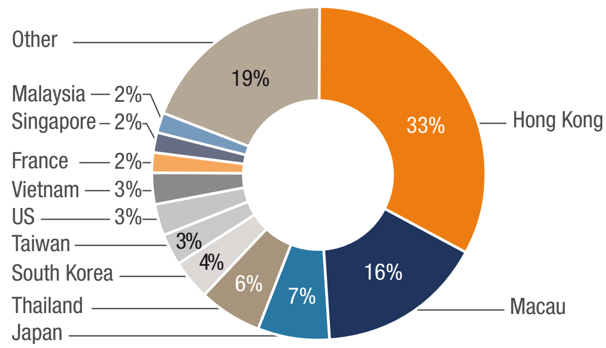
Travel & Tourism

Another dynamic industry in New China is travel and tourism. As the Chinese consumer becomes wealthier, a top aspiration is to experience more leisure travel, boosting demand for a range of service-based businesses.

With about 6% of the population holding passports,[9] most Chinese residents tend to travel domestically. About half of all Chinese tourists are expected to purchase leisure trips to destinations in sub-tropical southern China, particularly Hong Kong and Macau (see chart 8).

Leisure travel is expected to experience healthy growth and become a regular part of life for many Chinese households as affordability, holiday leave, better transportation and the desire to travel increases. The number of domestic trips in China increased from 870 million in 2003 to a staggering 4.4 billion in 2016.[10] This has had a tremendous impact on the Chinese economy.

Chart 8: Hong Kong and Macau are Major Beneficiaries of Chinese Tourism



Source: CLSA, CEIC Euromonitor, July 2017.

[9] Forbes, January 2016.
[10] National Bureau of Statistics, China National Tourism Administration.

Winning in New China

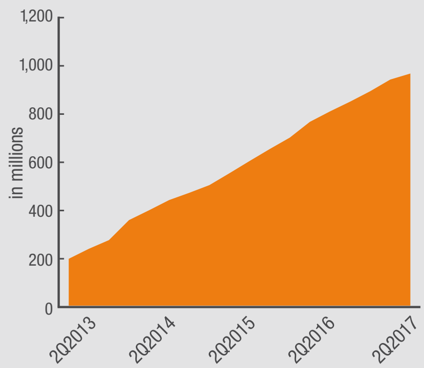
New China is presenting companies with incredible investment opportunities. Here are examples of companies that have benefited from consumer spending in the rising service-based industries.

Mirae Asset Global Investments may or may not hold positions in the companies discussed and this is not a recommendation to buy, hold or sell these companies.

TENCENT

Tencent is China's largest instant messaging and social network service provider. Its mobile platform, WeChat, dominates the mobile phone messaging app market with more than an 80% market share.[1] WeChat's monthly active users have grown almost fivefold since 2013.

Monthly Active Users



[1] eMarketer, 2017.

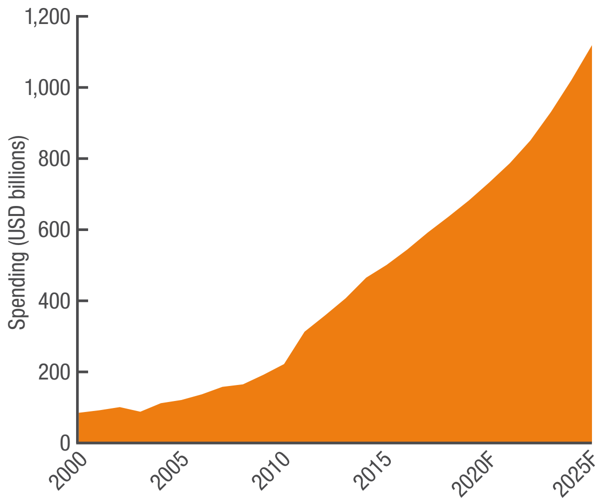
Source: Tencent. Weixin and WeChat combined. WeChat is known as Weixin in China.

In 2016, domestic tourism spending generated 82% of direct travel and tourism GDP and created more than 23 million jobs.[11] Domestic tourism spending is forecasted to continue its upward trajectory and reach $1.1 trillion by 2025, up from $544 billion in 2016 (see chart 9).

The fast-growing leisure travel market in New China affects many business segments, from restaurants to airlines to hotels, and provides numerous opportunities to invest in the travel theme. One route is through online travel agencies. The top online travel service provider in China has been able to maintain its market leader status with its early-mover advantage, largest global hotel network and one-stop distribution platform offering air tickets, packaged tours, car rental and other travel-related services.

Hotel and hospitality is another investable service-based industry benefiting from Chinese tourism. One emerging market company is offering Chinese tourists a unique lifestyle experience in their luxury hotels and restaurants backed by a high standard of service. They have achieved economies of scale through strategic acquisitions of selected properties in China and by forming joint ventures with business partners who have local knowledge and expertise.

Chart 9: The Upward Trajectory of Domestic Tourism Spending in China is Expected to Continue



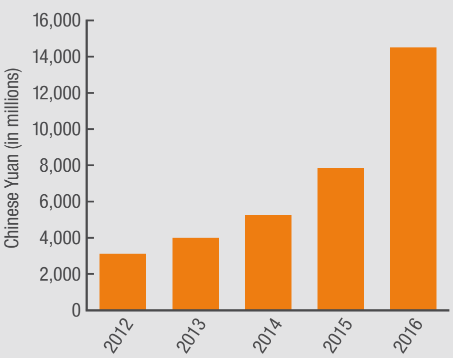
Source: World Travel & Tourism Council. Forecast values start after 2016. F=forecasted. **Forecasted numbers are projections and not guarantees.**

[11] World Travel & Tourism Council, Economic Impact 2017 China.

CTRIP

Ctrip is China's leading online travel company with more than a 60% market share.* Ctrip has extensive product offerings and a large network of global partners. The company's gross profit grew at a compounded annual growth rate of 47% between 2012 and 2016.

Gross Profit

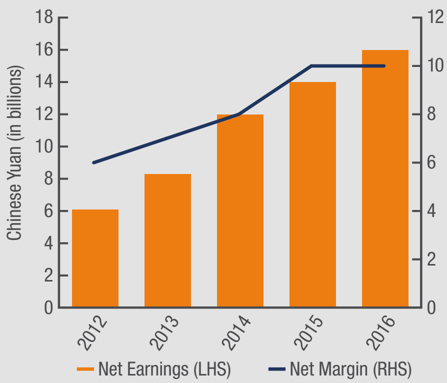


Source: Ctrip.
*CSLA, July 2017.

MIDEA GROUP

Midea Group is a Chinese company that manufactures and distributes household electrical appliances worldwide. More than half of the company's global sales are from China. Midea's net earnings have more than doubled from CNY 6 billion in 2012 to CNY 16 billion in 2016.

Earnings & Margins Growth



LHS=Left hand side. RHS=Right hand side
Source: Midea Group.

Investing in New China

As China continues to rebalance its economy from manufacturing to services and consumption, from Old China to New China, service-based industries will increasingly drive and potentially become the primary source of economic growth. Although the path may be bumpy at times, Mirae Asset believes this transition will continue to evolve into new investment opportunities.

Mirae Asset's proprietary research indicates that New China represents a multi-decade investment theme. Moreover, we believe that the best way to access opportunities in New China is through active management strategies rooted in fundamental, bottom-up research. Our high-conviction investment approach can help investors tap into the long-term growth opportunities of New China.

At Mirae Asset, we believe growing Chinese consumption continues to present investment opportunities even though investors must now be more selective. Economic growth is no longer what it had once been — the rising tide lifting all industries. To an active manager, this change means only that the need for identifying the best companies has become even greater, since not all services companies in New China will succeed. Through active management, however, we believe that an investor can identify the companies best positioned — whether through brand strength, management acumen or technical innovation — to win in New China.

We believe that the best way to access opportunities in New China is through active management strategies rooted in fundamental, bottom-up research.

To learn more about Mirae Asset's range of actively managed emerging market funds, please visit us at miraeasset.com

Please note: There can be no guarantee that any strategy (risk management or otherwise) will be successful. All investing involves risk, including potential loss of principal.

About Mirae Asset Global Investments

Mirae Asset Global Investments manages investment strategies for clients across the globe. With over $105 billion in total assets under management (as of June 2017), and over 600 employees, including 154 dedicated investment professionals, Mirae Asset offers a breadth of emerging markets expertise. Mirae Asset's offices are located in Australia, Brazil, Canada, China, Colombia, Hong Kong, India, Korea, Taiwan, the U.K., the United States and Vietnam.

We focus on actively managed emerging market-focused portfolios through a bottom-up investment process rooted in on-the-ground research. Mirae Asset Global Investments is recognized as one of the world's largest emerging market equity investment managers* and has one of the largest teams of investment professionals dedicated to emerging markets. Our worldwide team of portfolio managers, analysts and strategists maintains proximity to the investment opportunities that we research, allowing a deep understanding of companies and the cultures in which they operate.

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*Source: *Investments & Pensions Europe,* November 2016.

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