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IN PERSON

Fine China

BY MATT BROWN | BANKER & TRADESMAN STAFF WRITER

Tim Moore came home from China impressed with that country's ongoing growth and huge appetite for western-style consumerism. As a portfolio manager for Cabot Money Management, Moore was there scouting companies that would make suitable investments for Cabot's clients, mainly pension funds and high-net-worth individuals. But it's not all designer handbags and Buicks over there. Like the United States at the beginning of the last century, the price of progress is paid by the environment and a curious "shadow banking" market that has sprung up to meet demand. Here, Moore talks about China's promise, its command economy and "ghost cities."



Tim Moore

Title: Portfolio Manager, Cabot Money Management Inc.; Salem

Age: 32

Experience: One year at Cabot, nine years in international equity research.

5 FIVE THINGS MOORE LEARNED ABOUT CHINA:

- 1 China's economy has an engine to grow four times as fast as the United States or Europe for the next five years.
- 2 There's no shortage of consumer retail shopping in China – it clearly is still in the early innings, with ample room to grow.
- 3 I don't think the real estate or banking systems are headed for a hard landing like other investors say – maybe a soft landing in real estate and even softer in banking when credit tightening stops in early 2012.
- 4 Their high speed bullet train is more impressive and practical than any Amtrak line we have in the U.S.
- 5 Traffic congestion and smog in Beijing is as bad as people say.

Q: You recently took a trip to China. What were you doing there?

A: We try to go to regions of the world that we think are interesting investment opportunities. I got the chance to meet with the chief executive officers or the chief investment officers of 14 different companies and ask them questions for about 45 minutes about how business is going; how are trends? How do they invest? What's the outlook?

Q: What kinds of things did you hear from these folks?

A: We went in trying to confirm our thesis that the most interesting trend that we're seeing in China now is the rise of the domestic consumer going out there and doing retail purchases. There's a large middle class rising up that has a lot more purchasing power, and that was very interesting. We went to some of these stores and malls and some of these high-end luxury malls, and some of the customers are spending close to six weeks' salary compared to the average per capita income in China. They go in there and spend \$1,300, \$1,400 on a shopping trip and the average person in China only makes an average of \$1,000 per month.

Another thing that we saw was the urbanization play. China 10 years ago, 12 years ago had almost 70 percent of its population as farmers. Now, it's 52 percent. So, a lot of the people are moving in from the rural areas to the cities.

Q: Why would any of this be important for banks, investors or financial institutions here in the Boston area?

A: It's important because this year, and probably going forward the next three or four years, China is the fastest growing country in the world. They're growing their GDP at 9 percent a year. In the U.S., we'll be lucky if we can do 2 percent next year. Europe? 0 percent, 1 percent next year. So, it really is the growth engine of the world. China, just as an example, has no debt. Savings rates over there are very high, 20-30 percent.

It's a command economy, unlike a democracy, or a natural



free market and there is this element of 'shadow banking,' which is a big concern for a lot of people, and what that is is non-banks giving out loans. It's not so much loan sharks, but about 20 percent of the loans in China are from this shadow banking industry, and the China regulators are starting to crack down on it. They know it could be a risk later on, but at the same time, it's been beneficial to help some of the smaller companies and mom-and-pops get loans.

Q: Are the shadow banks you mentioned the first place a Chinese business goes for a loan, or are they a lender of last resort?

A: Usually, an entrepreneur, the first thing they'll do is go to a regular bank. They might have some cash, but they don't have any operational history, so maybe half the time they get rejected, so they go to these shadow bank lenders, who are charging 10 percent to 50 percent a year. You're not getting the 5 percent lending rate you'd get at a big bank. But they want to start their business or they want to do a real estate development project, and they get the loans. There's still some rigorous standards to get approved, but it is still a big part of lending over there. It mostly goes toward business investment, auto purchasing, urban development and business start-ups. They are starting to look into regulating that a little better,

and right now the other 80 percent of loans are still growing pretty well.

Q: Can you differentiate China's banking sector from ours or from the West's? Are they trying to westernize, or is that not what they're looking at?

A: They are westernizing, there's no doubt. For example, Shanghai right now versus 10 years ago is completely different. It's a very modern city. It looked like a mini version of New York with skyscrapers and lit-up buildings and amazing architectural designs. A lot of that has been through the banking system. The banking system over there still has very good lending requirements. They're not as leveraged and they're not as risky as the banks in Europe by any means. One of the biggest banks in Europe is BNP Paribas, and that company is lending out 22 times what they have in their capital core equity. None of the banks in China are doing that and they have rigorous standards. There are pockets of weakness. You'll hear about a town or a small province that has defaulted.

Q: You mentioned urbanization. Are people there talking about suburbanization? Something we saw in the last 50 years, where people who moved to cities for jobs thought, 'you know, what I'd really like is a house just outside the city?'

A: It's happening, but it's not natural like it was in the U.S. It's planned by the government. The government goes and works with development companies. They're building skyscrapers in downtown Shanghai or downtown Beijing, but the same day they're doing that, they're building stuff 10 miles outside the city that's half the price point or a third the price point and they're getting people to move in from the rural areas to both of those at the same speed. And they're building them six months or a year before anyone moves there. Occasionally, they get called ghost cities. I took trains and taxis by 20 or 30 buildings that had 100-200 units each that were completely empty and they probably won't be filled for 6-12 months. But they build them so far in advance that they can move a whole town into one building. It really is a very different planned economy. And the rents I saw in Shanghai were comparable to Boston. To live in a nice building, a two-bedroom would've been \$3,000.