THE CHINESE DECELERATING GROWTH

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BLOOMBERG, SHOWING CHINA GDP IN CONSTANT PRICES, YEAR-OVER-YEAR.

WE TRULY LIVE in interesting times. Since our last article on Artificial Intelligence, quite a few things have happened. One US presidential candidate (Donald Trump) came within an earlobe of being shot dead on the campaign trail, another one (Joe Biden) decided to withdraw his candidacy following unconvincing performances. The outcome of the US election in more uncertain than ever. In Europe, France finds itself rudderless following snap parliamentary elections called by its president, with three blocks, none with a clear majority to govern. On the 31st of July, the decision of the central bank of Japan to increase its interest rate to 0.25% caused margin calls for around US$30 billion worth of equities unwound in a matter of days, wreaking havoc on most markets.

Meanwhile, one company we mentioned last time, Crowdstrike, turned out to be responsible for one of the biggest technological snafus of this century, following a botched update to its security software. Basically, every business running on Windows in the world was affected, with planes stranded and blue screens everywhere. One week later, it seems the situation is back under control, but it shows how closely interconnected everything has become and how fragile things we take for granted are.

Had you suggested such a plot to a Hollywood producer, he would have rejected it offhand as way too unrealistic. Which just goes to show that reality is, indeed, stranger than fiction. This is important, because these events are quite unpredictable and, while they do have an impact on investments, one should not try to invest based on them. Good companies will keep on being good companies, whatever happens around them.

Interestingly, we think the most important thing is happening elsewhere, in China, and is not being discussed enough. We have spoken numerous times already about the fact that China is facing the difficult situation of trying to rebalance its economy from production to consumption (a classic catch 22 for almost every emerging nation) and the impact its slowdown is having on the rest of the world is very noticeable. From the luxury sector to the German economy to raw material prices, the fact that Chinese growth is decelerating rapidly is having an impact.

To us, this is one of the most important themes, one that will stay with us for decades to come. The blueprint here is what happened in Japan after the equity and real estate bubbles burst in 1990. More than 30 years later, equity prices have just come back to 1989 levels, while real estate prices are still significantly lower. While there was no equity bubble in China, we believe its real estate bubble was the biggest of modern times (even bigger than Japan's, and that is saying something) and will take decades to unwind. Since real estate is the main part of Chinese's savings, the impact will be very important and negative. Also, keep in mind that China's demography is already in decline, something that was not the case in 1990's Japan.

To us, this is the story to follow, although it is not making headlines, and not necessarily the US elections. We will continue to invest accordingly.