The China Rambler

An Occasional Letter On Topics Of Interest To China Investors

Issue #4. *"Seek Truth From Facts"* **Feb. 1st, 2025**

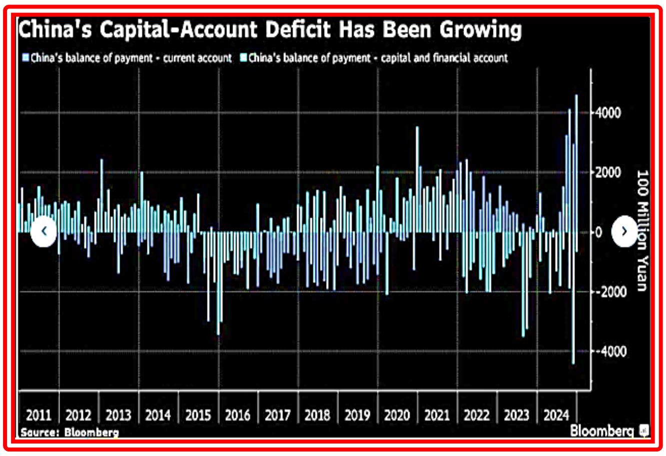
In this edition: What I learned about capital outflows queuing at the bank. Why Johnson Electric (00179) is a pass and what a good Dividend Policy looks like.

The Plural Of Anecdote May Not Be 'Data'; But That's Not To Say The Odd One Doesn't Have Value..

True story. Last month I was in the early morning queue at the Bank of China's Hong Kong head office waiting, at 0830, for the counters to open at 0900. I was there to complete the closing of some bank accounts and, having a bit of time, got talking to the young-ish (30s?) couple behind me. Let's call them Bob and Phyllis.

Bob: 'Is this the queue to open a bank account?' Bob's accent told me he wasn't from HK.
Me: 'I think so, are you living in Hong Kong?'
Phyllis: 'No, we live in Shanghai. We've come to Hong Kong to open a bank account.'
Me: 'Why do you want a Hong Kong account if you're living in Shanghai?'
Bob: 'We want to buy U.S. stocks; we're opening an account with Futu and need one.'
Me: 'Why do you want to buy U.S. stocks?'
Phyllis: 'We think that market is very stable and seems to have a reliable rising trend.'
Bob: 'Yes, and we're sure tech names listed there have a promising future.'

I'll come back to Bob and Phyllis in a moment. First, a digression into China's Capital Account flows for 2024, which were a record, out.



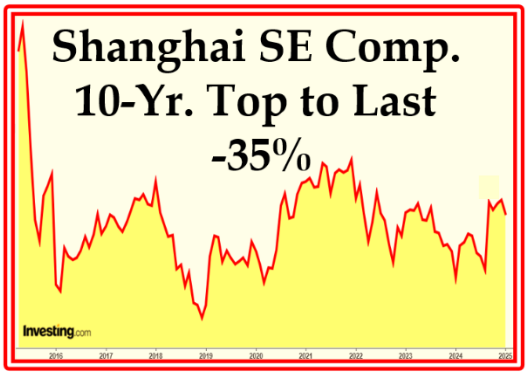
The chart is from a Bloomberg article of January 18th and a little hard to read but the message is clear. Dosh-out of China last year exceeded dosh-in by a wide margin. In the article Bloomberg reckon Bob, Phyllis and their friends shifted around U$182bn via local banks. In addition, foreigners weren't as keen to put money in as they have been creating a negative double-whammy.

Back to Bob and Phyllis.

Me: 'Did you ever consider buying local stocks in China?'
Phyllis: 'Did we ever! But we've lost so much there we're not interested anymore.'
Me: 'So, what tech names excite you in the U.S.?'
Bob: 'All of them really; but we'll start with some Apple, Nvidia and Microsoft perhaps?'

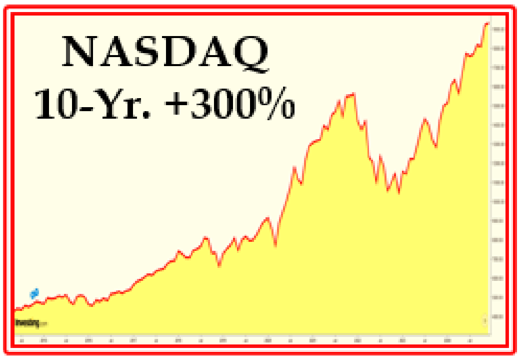
I wasn't asked for an opinion at this point, so didn't offer one. I judged the couple to be professionals of some sort and young enough to be able to recover the tuition I sense they're about to pay with their flutter into a now very mature bull market. This interaction made me think though about some related issues, as follows:

#1. Bob and Phyllis are being rational. Domestic markets have been unrewarding, forever.



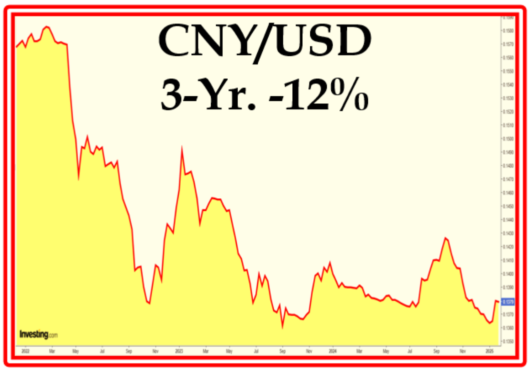
The broader concern is if right-thinking professionals, let alone the Moms and Pops who turn up for daily disappointment, aren't taking an interest, who will? We know the international crowd abandoned all hope some time ago.

#2. There are two ways of looking at Shanghai professionals clamouring to get into U.S. tech.



Boosters will argue it shows valuations can expand more as the pool of investors appears, almost, limitless. The more worldly might note it reminds of the need for caution when stock tips start to come from shoeshine boys.

#3. A small amount of Rmb weakness can be tolerated by China Inc. and may be welcome.



But what's Hong Kong's purpose if it's not helping capital *into* China? Are authorities happy it's now helping capital out undermining the currency in the process? Might they one day just say, 'Enough!' and clip Hong Kong's wings in this regard?

I hope it works out for my queue-buddies; they seemed nice people: but they represent a real problem. How long can China continue offering poor homes for savings like low yielding deposits, opaque wealth management products, unreliable real estate or value destroying stocks? If it can't do better capital will continue to vote with its feet; a situation that won't be tolerated forever. Something, eventually, will have to give.

Stockwatch: Johnson Electric #00179

Summary of a recent closer look

Basically: (All historic) Market cap.: U$1.2bn, P/E: 5.3x, Yield: 5.9%, P/B: 0.5. Avg. daily T/O (3m) 950k shares. **Business: everything that goes 'whirr' in your car i.e. micromotors.**

Old timers will know this name well. The company has been a staple of the small-cap circuit for just about ever. I hadn't checked in for a few years so thought a review overdue.

It's a great company; there's no denying it. They've operated successfully for decades in a cutthroat industry and prospered; and they've negotiated recent years deftly.

They knock out over four million products a day with practically zero defects. They supply over 1,600 customers and manage operations in 22 countries. Not an easy trick to pull off.

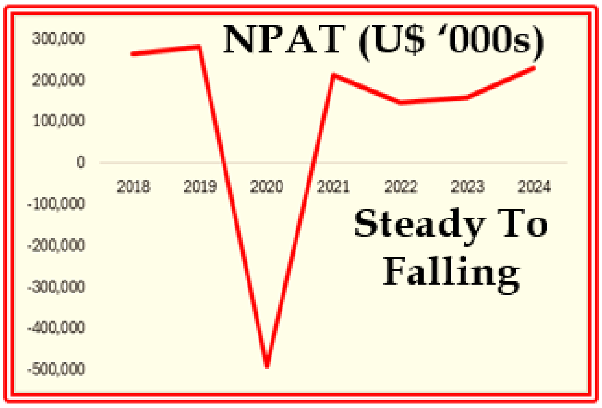
The problem is I can't see how they do a lot better than they're doing. In fact, the latest Q3 update (March Y/E) guided to a full year fall in sales for FY'25.

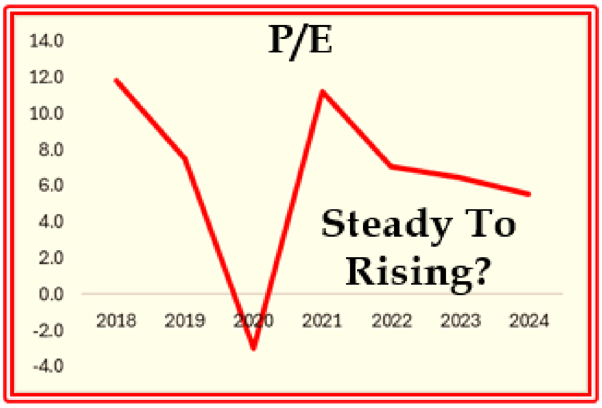
ROE has fallen from pre COVID levels and given the macro environment for their customers it seems unlikely it can be recovered soon. They're also price-takers in a difficult space.

Not to like: A CB issued in 2014 is an obvious red-flag. A thumping goodwill loss in 2020 wasn't clearly explained. The industry big-dog, Nidec 6594.T, is a brutish competitor.

To like: Continuous operation since 1959. Good communication (apart from 2020) and quarterly updates. Succession assured with Mr. Austin Jesse Wang in the wings.

Would I buy them? No. This is a good example of the great-company/poor-stock conundrum. The yield has risen recently but with profits about to dip it's likely the dividend will be trimmed. The P/E is fair, so multiple expansion probably can't happen. Moreover, with earnings dipping the 'true' P/E is going to be higher than the historic level indicated. In conclusion, without an upward earnings shock or earnings-driven multiple expansion and absent a reliable, pumping dividend I don't see how a minority shareholder could get rewarded here.





How's My Investing?

Performance summary, review of recent trading and other thoughts

January Performance:	**-0.9%**
Performance Since Inception (Nov. '24):	**+0.6%**
Cash Percentage of Portfolio:	**30%**

I'm all set up now so changes to the portfolio will be infrequent and in most months there'll be nothing to report. Which is as it should be. A major enemy of performance is turnover. Another enemy of performance is the absence of or poor dividends [N. B. 32% of the S+Ps total return since 1926 was the result of dividends] and as we head into results season this has been on my mind.

The Weasel's Promise

"Any future determination to pay dividends will be made at the discretion of our board of directors and may be based on a number of factors, including without limitation our future operations and expected earnings, capital requirements and surplus, general financial condition, contractual restrictions and other considerations required under applicable laws and regulations and other factors that the board of directors may deem relevant." 2024 Annual Report.

Not long-ago Listing Rules in Hong Kong changed requiring companies to state their Dividend Policy. A great idea, right?

Good companies, plus or minus, have complied. But a large number, how best to describe them? 'Weasels' will do, have not. Instead, they've opted for boilerplates like you see on the left.

This, BTW, is a lift from one of the largest listed companies in Hong Kong. A profitable, e-commerce enterprise with substantial net cash. However, it seems they're uninterested in telling investors how they'll distribute either future earnings or surplus reserves. This is: a) an insult to minorities, b) disrespectful to the Exchange, c) an obvious indicator of integrity-deficit at the helm and d) makes future-value-analysis impossible. It should surprise nobody to learn this company's stock has been significantly de-rated in the last three years.

This is a mandatory due diligence check and where I find this kind of so-called-policy boilerplate I'll usually move on and look for better prospects; one can do so much better.

Compare the Weasel's Promise with the following update from (one of my holdings) China Shenhua (01088), last month: **"China Shenhua Energy.. has proposed the "Shareholder Return Plan for 2025-2027", pursuant to which,.. profit distribution in the form of cash dividends per annum shall be no less than 65% of the net profit.. of the Company realised in the corresponding year during 2025-2027 and the Company may also implement [An] interim profit distribution.. after taking into.. consideration.. its operational performance and capital needs."** Co. announcement Jan. 21st. ***Now THAT'S's a dividend policy!***

Datawatch

Key Releases In The Last Month

Mostly 😐 Two 😟 One 😊

Markets, in the medium term, are more about rates of change than absolute levels. This is worth noting as several indicators showed signs of improvement last month.

Trade 😐: Dec. Exports +10.7% (Nov. +6.7%), Imports +1% (Nov. -3.9%). Exports, pre-tariff stocking continued. Imports, encouraging.

Prices 😟: Dec. CPI +0.1% (Nov. +0.2%), PPI -2.3% (Nov. -2.5%). The PPI has declined 27-months straight. Deflation is a manifest reality now.

Credit 😐: Dec. M2 +7.3% (Nov. +7.1%), Total Social Financing +8.0% (Nov. +7.8%). A small uptrend at long last.

Consumption 😐: Dec. Retail Sales +3.7% (Nov. +3.0%). A tiny but pleasant surprise.

Industrial Activity 😊: Dec. Industrial Production +6.2% (Nov. +5.4%). Industrial Profits +11% (Nov. -7.3%). Both strong beats.

New Home Prices 😐: Dec. -5.3% (Nov. -5.7%). The month-on-month series was unchanged, the first time that's happened in 18-months.

Business Confidence 😟: Dec. Purchasing Managers Indices. Mfg. 49.1 (Dec. 50.1), Services 50.2 (Dec. 52.2). Both gauges surprisingly weak.

That wraps it up for January. What's here isn't advice or recommendation, it's what I've been up to, how I'm looking at the world and a small piece of the market puzzle which, combined with yours, I hope may be of some use.

"He who receives an idea from me, receives instruction himself without lessening mine; as he who lights his taper at mine, receives light without darkening me". Thomas Jefferson.

Good Luck with ***your*** investing. Feedback please! to me at nial@nialgooding.com