

New China Perspectives



Welcome to the weekly issue of Morgan Creek's *New China Perspectives*. It is comprised of research from Morgan Creek's China-based investment team together with curated articles of interest. In addition to timely political and economic news covering greater China, Morgan Creek's China team seeks to provide in-depth perspectives on investing in the technology, consumer and healthcare sectors in the region. Our research leverages the "on the ground"

insights of our team together with Morgan Creek's decades-long experience in covering the region. Our team are focused, thematic investors primarily covering the technology, consumer, and healthcare sectors and investing in private companies and early-stage managers with deep local expertise. To learn more about our team and investment offerings, please email chinateam@morgancreekc.com.

Best Regards,

Handwritten signature of Mark W. Yusko

Mark W. Yusko
CEO & CIO

NOTES FROM THE BUND¹

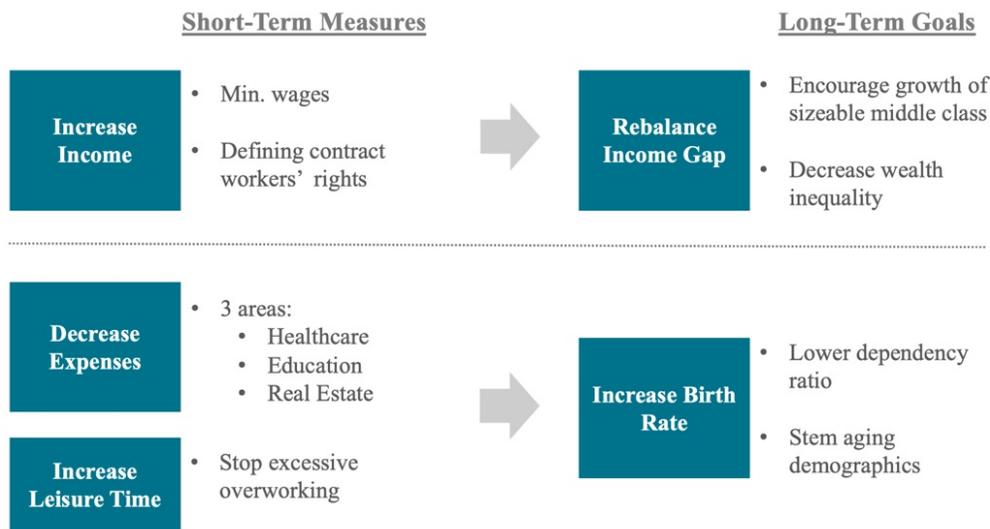
In our last newsletter, we continued a five-week discussion on the recent regulatory changes made by China, and the implications for both China's economy and the broader world economy by discussing the catalyst for these regulatory changes. We will continue the discussion this week with a focus on the specific plan laid out by the Chinese government.

China is focusing its efforts on three important areas in its quest towards self-reliance:

- Raising domestic demand (*i.e.*, consumption)
- Supporting domestic supply (*i.e.*, production)
- Implementing rules governing its new economy for sustainable growth

The objective behind the first two areas is domestic substitution of consumption (away from exports) and supply chains (away from relying on foreign equipment/channels). The aim behind the third is to ensure that both demand and supply develop in a sustainable manner over the long run.

Figure 1: Driving domestic demand



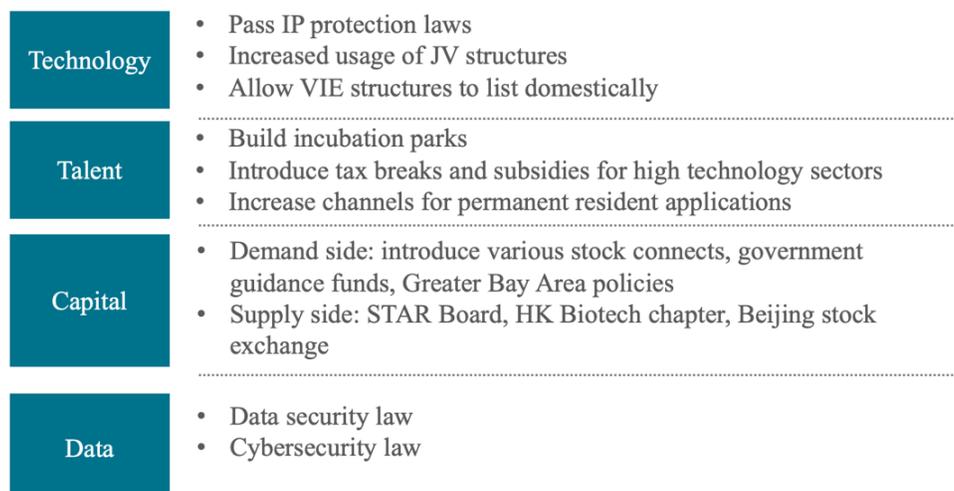
There are three ways to increase domestic consumption for the average Chinese individual: (i) increasing their income, (ii) decreasing their essential expenses and (iii) increasing their leisure time. The government has attempted to achieve these goals via policies including:

- Protecting workers' rights to ensure they are not left behind in an increasingly digitalized economy
- Reducing healthcare, education and property costs which on average contribute up to 43% of a Chinese individual's expense
- Regulating excessive overworking

Successful application of these policies over the long run is expected to support a sizeable middle class and potentially help reverse China's aging demographics².

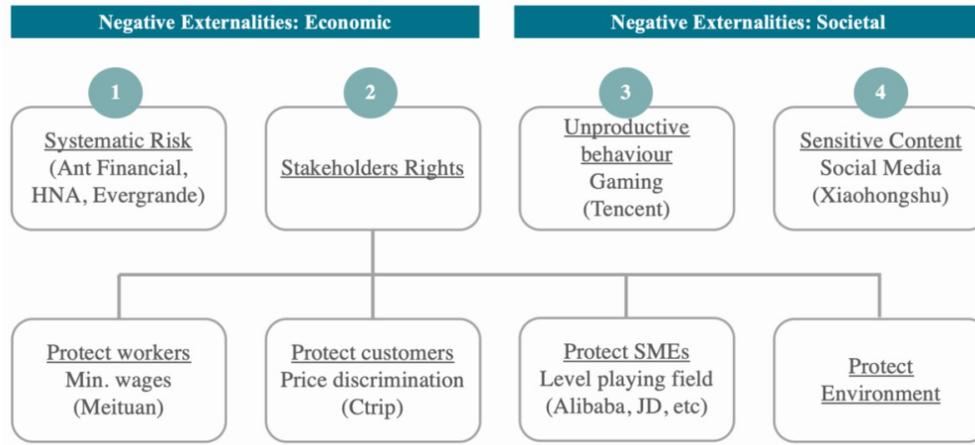
China plans to develop and maintain a domestic ecosystem conducive to local innovation and ease bottlenecks in its domestic supply chains resulting from the current US-China tensions. As can be seen in the chart below, many of these policies are supportive of innovation's "golden geese": the private enterprises and foreign investors (see a more detailed discussion of this in "Part 4") operating in China.

Figure 2: Promoting domestic supply production channels



It is critical for China to update its regulatory framework for its new economic model, keeping in mind a system that is designed for sustained, long term development. Crucial points for such a model include adopting a multi-faceted perspective considering the impact of externalities, which we discuss as the blind spots of capitalism in the next section.

Figure 3: Ensure sustainable, high quality economic growth



Negative externalities on the economic front typically manifest in two forms:

- Development of “moral hazard” business models like Ant Financial³, or the creation of significantly overleveraged companies like Evergrande which could become too big to fail, threatening a financial contagion
- Inattention to important stakeholder rights not considered in profit calculations but which are important to a company’s (and to society’s) long term stability and growth. China addresses this by explicitly drafting regulations which reduce systematic risk and balance stakeholder rights

China also considers other negative externalities, or undesirable outcomes, on the social front including:

- Protecting minors against “unproductive” behavior, for example by defining time limits on playing mobile games
- Regulating “sensitive” content which is deemed to be potentially destabilizing to society

Companies can become sources of social instability either through their normal pursuit of profits or by negligence. As an example, recent revelations at Facebook show how it created programs that target young children and neglected to monitor hate speech/content. Together with other social media platforms, Facebook was utilized as a tool during the Washington DC riots after the US presidential elections as well. These are all issues that regulators worldwide face, but China’s approach has been to preempt potential social issues by adopting upfront a “parental” stance⁴.

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CHINA NEWS SPOTLIGHT

China's stock markets see foreign capital inflows hit record high: Despite the existence of multiple unfavorable factors such as the coronavirus, a downturn in the

consumer market, as well as the crackdown on the Internet industry and the property sector, foreign capital flows into China's equity markets reached a record high in 2021. [Read more.](#)

China to 'timely replenish' liquidity shortfalls with cash injections before Lunar New Year holiday: China's central bank is set to replenish liquidity shortfalls before the Lunar New Year holiday, the China Securities Journal reported, even as markets were split on whether more monetary easing was imminent in the world's second-largest economy. [Read more.](#)

China-US space race heats up as Chinese firm plans over 40 launches this year: China's main space contractor plans more than 40 launches this year, consolidating the country's presence on a front that is becoming a source of rivalry with the United States. [Read more.](#)

Geely to launch new ride-hailing platform, amid Didi's plight: Geely, China's longstanding automotive manufacturer, will launch a new ride-hailing platform headquartered in Chongqing, according to Jiemian News. [Read more.](#)

Cloud Village, music streaming service of NetEase, lists on the Hong Kong Stock Exchange: Cloud Village, the music streaming service of Chinese gaming giant NetEase, has listed on the Hong Kong Stock Exchange on Thursday. [Read more.](#)

Chinese ride-hailing giant Didi to delist from the US and prepare to go public in Hong Kong: Didi, the Chinese ride-hailing behemoth, said on Friday that it will begin delisting from the New York Stock Exchange and plans to list in Hong Kong. [Read more.](#)

Big Pharma must sacrifice upfront profits to get on China's coveted list of medicines eligible for insurance reimbursements: On November 16, Du Jia, a 32-year-old mother in the Guangdong provincial city of Maoming, posted a video of her son, nicknamed Little Mili, on China's Little Red Book social media platform. [Read more.](#)

Hong Kong ophthalmic drugs pioneer sets its sights on cracking China's US\$20.2 billion eye disease treatment market: Zhaoke Ophthalmology, a Hong Kong-listed company focusing on the development and sale of ophthalmic drugs, is aiming to take a leading role in mainland China's eye disease market as the country's innovation ecosystem matures. [Read more.](#)

Chinese Terracotta Warriors city Xian in lockdown as Covid-19 outbreak grows: The northwestern Chinese city of Xian launched lockdown measures on Thursday as it accounted for 63 of the country's 71 new local symptomatic Covid-19 cases, detected in citywide testing. [Read more.](#)

¹ The Bund is a historic waterfront area in central Shanghai, where Morgan Creek's office is located. From the 1860s to the 1930s, it was the rich and powerful center of the foreign establishment in Shanghai, operating as a legally protected treaty port. The picture above is part of the historical waterfront.

² China's authorities conducted a [poll](#) following the introduction of its three child policy which revealed that high living and child rearing expenses discourage its citizens from having more children.

³ Albeit there was likely also [political considerations](#) in halting Ant's IPO as well.

⁴ There are, no doubt, also political considerations around control behind China's posture on social media.

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