



HISTORY

Exploring Culture and Companies in Changsha, China

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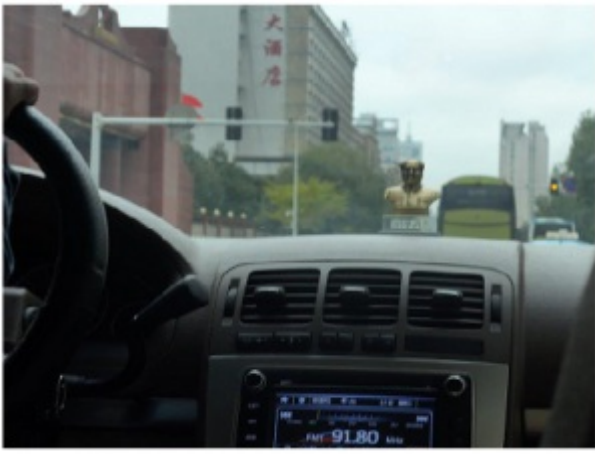
As you'll know if you've been following my recent travels, my team and I have been touring various cities in China. We've been reporting about the economic conditions we have seen, exploring the culture and visiting companies in search of potential investment opportunities. Our next blog stop is Changsha, the capital city of Hunan Province.



High-speed train, Guiyang, China station

My team and I departed for Changsha via high-speed train from the new (and huge) station in Guiyang. We started our journey at 200-plus kilometers per hour, traveling through mountainous countryside and traversing many tunnels and bridges.

We purchased lunch on the train but also received free drinks and snacks, including crunchy green, packaged dried peas with the Chinese characters translating as "American peas." The snack reminded me of my short stint at an advertising agency on Madison Avenue in New York when I was a student. We were researching a sort of dehydrated pea product for a major food firm. The peas did not need refrigeration and could be soaked in water to reproduce fat, juicy peas that looked fresh. The brand name they picked was "Sleeping Beauty" peas, but the survey we did among potential consumers found that respondents got their fairy tales mixed up and associated that with the poison apple of Snow White and the Seven Dwarfs. That—along with the unappetizing look of the shriveled peas before soaking—killed the project. But my Chinese dried "American peas" along this particular journey were quite tasty.



Riding with Chairman Mao

Leaving Guiyang we made several stops on the way to Changsha including Zhijiang, the site of the final major battle with the Japanese during World War II, as well as Shaoshan, the birthplace of Chairman Mao Zedong. Finally, we reached Changsha and the eight-platform Changsha South Railway Station, which opened in 2009. The station is part of the Beijing-Guangzhou-Shenzhen-Hong Kong high-speed railway and it had an enormous garage conveniently on the same level as the arrival floor for regional travelers. Red and green lights above each parking space denoted which spaces were free and which were occupied. As with our train, the parking lot was packed. As we drove off, our driver was chatting with his hands-free cell phone, and I noticed a small Chairman Mao bust on the dashboard. As Changsha was the home of Chairman Mao for many of his formative years, it made sense to honor him, but the driver explained that it was also there to drive away any evil or bad luck.

Observing the heavy traffic on the way to our hotel, it was clear to me that despite the tremendous amount of infrastructure building that has already taken place in China, there is a need for more. Vehicle sales in China have outstripped those in the United States—some 21 million passenger cars were sold in China in 2015 versus 17.5 million light vehicles sold in the United States.¹ Still, vehicle penetration is only seven vehicles per 100 people in China, versus 70 per 100 for the United States—so there is room for even more growth.²

Changsha is surrounded by three major rivers including the Xiang, the Liuyang, and the Laodao. The city has thus been a major distribution center for goods coming from all over China by river ships and barges. The Chinese characters for Changsha mean “long sand,” possibly because in the middle of the Xiang River, a tributary of the Yangtze River, there’s a sandbank.



River view in Changsha, China

The city is not only a strategic river and railway hub but an airline hub as well. The Changsha Huanghua Airport serves as the regional hub for China Southern Airlines and other local and international airlines with flights to many major cities domestically and internationally including Hong Kong, Bangkok, Seoul, Pusan and Osaka. In 2015, the airport saw an all-time high of 19 million passengers.³

In 2013, the “Sky City” skyscraper project broke ground promising to be the world’s tallest building at 838 meters and 220 floors, which would top Dubai’s Burj Khalifa. However, the project was halted by authorities citing lack of government licenses and experts questioning whether such a tall building could be built safely in only the seven months planned. The building is apparently now in the final approval phases, but according to local reports, the foundation is being used as a fish farm by local farmers—so its completion remains uncertain. Meanwhile, a mini [Sky City project of 57 stories](#) was completed in Changsha in less than a month.

In recent years, Changsha has become an important creative center for television and entertainment arts, with its many television stations producing some of the most popular programs in China. These programs have also fueled other forms of entertainment, including karaoke bars, dance clubs and theater shows, as well as related businesses like hair salons, fashion stores and snack shops serving hot and spicy nibbles in the evenings.

Our hotel, located in the North Star Delta area, had a huge shopping mall connected to it and was part of a mixed-use development with apartments, shops and a beautiful walkway and cycling path along the riverfront. Apparently the project was done at the behest of the government since it did not appear economically viable—at least in the short term. The four 30-story towers were completed but empty, the shops were empty and our hotel wasn’t fully occupied.



Shopping mall in Changsha, China

We started our company visits in Changsha with a call on a health care-related company. The founder of the company discovered that Chinese hospital treatments for eye problems were limited because of a lack of the required equipment. In cooperation with state-owned hospitals and other partners, he raised enough money to start eye clinics in hospitals using advanced, specialized eye-treatment equipment. The business grew fast and he expanded with more standalone eye-care facilities. A manager told us that the biggest challenge they faced was finding qualified staff, so they offer various incentive programs, including stock options for doctors. Treatments offered include Lasik surgery, cataract removal and correction of eyesight with glasses (optometry).

In our search for potential investments, we called on the financial office of Changsha Municipal People's Government to meet the director and vice director. They welcomed us and explained that the office's function was to help companies in Changsha gain access to the capital market and serve as the bridge between enterprises and investors by encouraging stock exchange listings. Specifically, they collect information about companies that could be eligible to list on the various Chinese stock exchanges and publish a list of such companies, now reaching 200 in number. The officers said that Changsha is relatively undeveloped compared with coastal regions, but has a good opportunity to catch up, because of its strategic location in the center of Southern China and as a hub for the exchange of talent, information and capital. Two high-speed rail lines cross Changsha, and a third one is under construction (connecting Chongqing and Xiamen), which facilitate the communication between the city and more developed regions on the coast. Changsha's residents are hardworking and adventuresome, and there are three prestigious universities in Changsha, namely National University of Defense Technology, Hunan University and Central South University, which facilitates the commercialization of technology. The officers then explained that before the initial public offering (IPO) stage, most companies need private equity investment but there is fierce competition and pre-IPO valuations are volatile.

After our business visits one evening, we went to the theater to see a live show with Hunan singers, dancers and comedians, produced by an entertainment group with origins in the rare-earth business. Tickets for the show were relatively expensive, but the theater was full of Chinese tourists and groups. The show started with Las Vegas-style dancing women in costumes, followed by comedy sketches and musical acts. A female comedian was fantastic and made the audience laugh continuously. She picked one of our analysts named Chris from the audience to get up on stage and reenact scenes from the movie *Titanic*. She continued with a lot of double-meaning puns (double entendre), which I did not totally understand and my fellow spectators couldn't (or were too embarrassed to) translate fully. She had the audience in stitches and embarrassed Chris to no end. Even though I didn't understand all the jokes, I was able to appreciate the comedic spectacle of it.



Catching a show in Changsha, China

In another act, one of the singers was introduced by the master of ceremonies as a person from a very poor background. They showed films of his early life in a poor farming community, and how he was now going into the countryside to help the poor people by giving them money and gifts. The master of ceremonies then asked the audience to purchase his music (on CD) to support his altruistic pursuits. There was one singer who drank bottles of beer "donated" from the audience, a way to get the audience to drink the beer put on the tables in front of us and also encourage us to purchase more. We had seen this sales tactic before in other shows in China.

We also visited a company engaged in a wide variety of publishing and distribution including textbooks and popular books, as well as a newspaper, audio and video products, paper and printing supplies. Interestingly, they told us they don't need approval from the Education Department of China for online education products; they have individual business agreements with schools. However, content is based on printed text books that have already been inspected by the government. I spoke with one company official about the use of British English versus American English, and he said he preferred British English, but his son was actually studying in the state of Missouri in the United States.



Mao Zedong

After our company visit, we stopped in to see the Changsha Municipal Museum, which pays homage to the founding father of the People's Republic of China, Mao Zedong. In the early 1900s Mao Zedong was a student at the teachers' training school in Changsha and later became a teacher and principal of that school. A large building housing an art gallery was closed for renovation, but we were able to visit the humble house where Mao and his wife lived. A small building served as the office of the Hunan Communist Party Central Committee. The site includes a giant seven-meter-high aluminum-magnesium statue of Chairman Mao addressing the masses. After the museum visit, we had a tasty bowl of noodles across the street in a little neighborhood shop down an alley. I noticed a poster on the wall and asked one of my Chinese colleagues what it was. They explained it was an ad for a type of mutual fund that promised high returns. It was somewhat ironic to see an ad promoting capital markets so close to the statute of this iconic Communist leader. My how things have changed!

The next day we visited a company involved in manufacturing lenses for cellphone cameras. They said processing the glass was their specialty and that job was very labor-, technology- and capital-intensive with a relatively high entry barrier. We asked if they were concerned about a deceleration in the growth of smartphone and tablet sales affecting their business. A manager we spoke to was confident there would be new growth drivers such as wearable devices. The company has 80,000 employees and now it is actively pushing forward the automation of manufacturing.

After the trip to the lens company, we visited a large housing project. It was one of the high-end developments located on a stunning site on the Xiang River surrounded by mountains on the other three sides, perfectly meeting the Chinese "feng shui" geomancy requirements for bringing a home good luck. Previously, an old machine tool factory occupied the land, and the architect cleverly integrated part of the old factory into the overall design. The main factory building is now a clubhouse and office for the development with a coffee shop, relaxing area and meeting area. The architect added a unique curved wood stairway to the second floor, an attention-getting detail. This high-end project—like many other such projects we've seen in China—met three required criteria: It is located in the city center; it has non-replicable natural resources; and the city where it's located is rich in historical culture. When discussing maintenance expenses, executives said that they were planning to bring robots in to sweep floors and guard properties in order to address labor shortages and rising wage bills. The chairman of the company also told us that eight robot chefs were already working in the restaurants that serve residents of its developments.

Leaving the city, we went to a special technology park to meet executives of an environmental-protection company. The firm provides a full range of environmental solutions covering air pollution control, waste water treatment, solid waste treatment, energy saving and soil remediation. I began to realize that the Chinese government and people are serious about improving the environment and cleaning the air. Air pollution control is a large business segment for the firm, not surprising given the high level of air pollution in Chinese cities. Management indicated to us that although the percentage of coal in total energy consumption mix may decline, it will likely continue to be the primary source of energy in China for the foreseeable future.

Soil quality is also becoming of bigger concern in China; soil remediation (including farmland and industrial land) is expected to see rapid growth in the next couple of years. Major pollutants in the soil include heavy metal and organic materials. China's Soil Pollution Prevention and Treatment Law was set forth in the 18th Communist Party of China (PNC) National Congress, and was drafted and submitted to the State Council for approval in May 2015. It seems likely to come into effect in 2016. Executives of the company we visited said that Hunan is the most polluted province in China in terms of soil contamination because of the thriving nonferrous metal-related businesses. Private companies will likely form joint ventures with government to invest in the projects, and we've seen Chinese companies acquire foreign companies with expertise in this area. The company we visited boasted of a number of American and Chinese scientists among its ranks—many with doctoral degrees. The experience foreigners have removing poisons, petrochemicals and other pollutants from soil will be very valuable in China since the contamination of ground water there is becoming a critical issue.

Between our company visits, we also toured a number of large shopping malls in the city. The tenants in the malls and on the streets of Changsha included all the recognizable international brand names, but the foreign brands are now being overwhelmed by the increasing number of local brands that have increased their market share, benefiting from foreign expertise combined with local knowledge to market their products. In so many aspects, we've seen how globalization and technological advancements have benefited emerging markets—and this trip was no exception. We truly enjoyed our visit to Changsha and all the diverse companies and tourist pursuits it offers.

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1. Sources: China Association of Automobile Production, *Wall Street Journal*, January 2016.

2. Sources: Bloomberg, World Bank, data as of 2011.

3. Source: Changsha Municipal Government website, "International Travelers Upsurge with Booming Open Economy," December 2015.