China's Volatile February Sets Market Up For Big Gains

China's market's received a one-two punch of bad news that sent traders ducking for cover and providing opportunity for our readers.

A Black Swan Or Grey Rhino Event Will Happen? Duh.

Chinese financial markets got off to a rough start in February as the country's top financial planner warned a Black Swan of Gray Rhino event would happen this year. The news sent markets into a tailspin that was deepened as the global equity correction took place.

The warnings from Fan Hengshan, China's vice secretary general of the National Development and Reform Commission, are meaningless. A Black Swan event is something you can't and don't see coming, it could happen at any time, or not, and by definition impossible to predict. A Gray Rhino is an event that you do see coming but do nothing about. If it's going to be ignored what's the point of warning about it?

What this is for money managers and investors is a sentiment driven event that will lead to future gains. While traders were ducking for cover China's economy continued to expand, and despite the small trade disputes US President Donald Trump and Chinese President Xi Jinping have been having.

Another factor contributing to the depth of China's market correction, a correction that saw losses on the Shang Hai exchange near 12%, was the onset of Chinese Lunar New Year. Lunar New Year is a national holiday that shuts down industry, business and expansion for more than a week. One sign that the holiday was anticipated is a surge in trade that occurs every year at about the same time.

January trade figures show exports up by 11.1% YoY and imports up 36.9% YoY as businesses stockpiled materials and goods ahead of the shut-down. Regardless the cause, the figures show robust demand at home and internationally that is expected to sustain growth within the economy. That being said growth is expected to be subdued relative to recent years as authorities crack down on pollution and sustainability.

The next major hurdle for China is the People's Congress scheduled for March. Topics of interest are the possibility of merging top regulators into a single uber-regulator for the financial system, and the possibility now President Xi Jinping may rule indefinitely. The first would entail a merger of the banking and insurance regulators in an effort to further stabilize markets and stamp-out shadow banking. The second could be one of those Gray Rhino events mentioned before. The Chinese Communist Party has recently proposed to remove presidential term limits, a move that would pave the way for President Jinping to remain in power at the end of his second term.

Fund managers at ValuePartners' Asia-Pacific Fund are bullish on Asia Ex-Japan, and China specifically. They see the region's strong start to 2018 driven by robust capital flows, positive macro-data and expansionary earnings outlook.

From their January fund statement;

Although the market retreated in the first trading days of February due to higher inflation expectations . . .we remain constructive on Asia ex-Japan equities in 2018 as corporate earnings generally rise when inflation starts to pick up . . . we expect the ongoing strength in the global economy to drive *another year of synchronized earnings per share (EPS) growth, which is at 12.9% in the region.*

We believe the solid earnings outlook, together with the fair valuation (the 12-month forward price to earnings of the MSCI Asia ex Japan Index was at 13.7 times, versus 19.2 times during the 2007 peak), should turn any potential market pull-back into buy-on-dip opportunity.

The Asia-Pacific Fund is a closed end fund trading on the New York Stock Exchange under the ticker