31 July 2021

# China Tech Crackdown

**Key Highlights**

- During the week upto 28 July 2021 there was a **blood bath in Chinese markets especially the Tech stocks**.
- This was on back of **crackdown by Chinese government on the Technology companies**, especially the **food delivery apps and education technology companies.**
- Speculations that **U.S. may restrict investment in China** and Hong Kong added to the bearish sentiment.

China's onslaught of regulatory crackdowns on tech companies rattled global markets specially the emerging markets across the globe during the week upto 28 July 2021 the **Shanghai Composite and Hang Seng fell 5% to 7% during the period.** This impacted the currency and bond markets also with the yuan falling as much as 0.6% and 10 year government notes rising by 7 bps to 2.94% during the said period.

**What led to market correction?**

**Embargo on Tech companies:** On Monday 26 July 2021, the Ministry of Industry and Information Technology held a meeting that officially kicked off the action plan to collect information on corporate misdeeds, list specific problem areas and hold offenders legally responsible. The six-month crackdown will focus on four areas: adherence to the anti-monopoly law, protecting users, safeguarding data and obtaining official authorization to operate. Under this new regulation country's internet giants to get their act in order and fix anticompetitive practices and data security issues.

**Crackdown on Education Technology Companies:** In another announcement, Chinese government banned online education firms from teaching courses that are taught in school, from raising foreign capital, and said that they should be registered as non-profit firms. The move led to listed Chinese ed-techs losing billions in market cap- as much as 90%, while privately held hot startups became a sour proposition overnight.

**Clampdown on food delivery apps:** The next day, the government said food delivery apps would have to pay their workers above minimum wage, provide insurance and relax delivery times in rush hours. This led to food delivery apps' shares falling, and increased pressure on them to treat workers better. The so-called gig workers do not get the benefits that a full employee does, and these lack of benefits are the cost advantage for these companies- virtually their DNA. Their entire business model can come under pressure if worker costs rise.

**But why is China attacking its own companies?**

**Demographic Advantage:** Rising social and education costs are **driving down birth rates** in China and leading to an **aging population**. China wants to reverse this, and is trying to make living less expensive - by banning the education apps that advertise heavily, rely on capitalistic models and take up a large portion of parents' and kids' time and money. For the same reason, the government has also clamped down on a booming real estate sector whose growth was led by borrowing.

**Focusing on a different kind of technology:** At the end of 2020 Ant Financial' s IPO was called off and Didi was taken off the app store days after its $4.4 billion public listing for a cybersecurity review. However at the same time

China has steadfastly been protecting its mobile-network and handset-maker Huawei, amid US tensions and its semiconductor industry and artificial intelligence efforts are still going strong.

It seems to be **clamping down on the consumer technology** side of things, because its policy may dictate a **refocus towards industry focused technology**, and not mere consumer apps.

## Will this Impact India?

Though it is too soon to definitively tell; however, **global investors** - stock market investors, venture capitalists and private equity funds **could divert funds to Indian company specially the start-ups** because India is currently a more open and predictable market and at the same time India is slated for more growth.

## Funds Exposure to China

The ongoing volatility in Chinese stock markets has taken a toll on Indian mutual funds (MFs) that invest in China and its related regions. Their net asset values (NAVs) have fallen sharply.

**List of our selected funds which have significant exposure to China**

| Fund Name | Category | Absolute (%) | | | | | China Exposure (%) |
|---|---|---|---|---|---|---|---|
| | | 1 Week | 1 Month | 2 Months | 3 Months | 6 Months | |
| Kotak Global Emerging Market | International – Emerging Markets | -3.72 | -7.87 | -4.76 | -7.13 | -4.36 | 33.43 |
| Edelweiss Emer Mkt Opp | International – Emerging Markets | -4.48 | -9.24 | -6.75 | -10.02 | -8.07 | 30.19 |
| Mirae Asset NYSE FANG+ ETF FOF | International - U.S. | -0.65 | -1.34 | 9.50 | -- | -- | 16.45 |
| Invesco India Invc Glb Cmr FOF | International - Others | 1.10 | -6.45 | -1.84 | -6.88 | 1.72 | 6.90 |
| PGIM India Global Eq Opp. | International - Global | 2.19 | 1.01 | 11.40 | 2.81 | 6.21 | 6.41 |
| Aditya BSL Intl Equity A | International - Global | 1.92 | 0.32 | 3.08 | 1.27 | 12.88 | 5.89 |
| Axis Global Innovation FoF | International - Others | 2.15 | 1.55 | 4.60 | -- | -- | 4.28 |
| Motilal Oswal Nasdaq 100 FOF | International - U.S. | 2.37 | 4.51 | 11.99 | 6.89 | 17.95 | 2.34 |
| Axis Global Equity Alpha FOF | International - Global | 2.10 | 0.28 | 4.32 | 4.07 | 18.75 | 1.81 |
| BNP Paribas Aqua FOF | International - Others | 2.54 | 4.44 | 6.63 | -- | -- | 1.52 |

*Source: Morningstar Direct Data as on 28 Jul 2021*

**List of other funds which have significant exposure to China**

| Fund Name | Category | Absolute (%) | | | | | China Exposure (%) |
|---|---|---|---|---|---|---|---|
| | | 1 Week | 1 Month | 2 Months | 3 Months | 6 Months | |
| Nippon India ETF Hang Seng BeES | International – Country Specific | -6.93 | -12.48 | -9.74 | -11.47 | -8.09 | 63.62 |
| Edelweiss Greater China Eq Off-sh | International – Country Specific | -8.10 | -11.88 | -7.49 | -10.78 | -10.80 | 63.31 |
| Axis Greater China Equity FoF | International – Country Specific | -5.44 | -8.28 | -5.64 | -7.32 | -- | 57.81 |

*Source: Morningstar Direct Data as on 28 Jul 2021*

## Our View

We believe that investors should keep international funds especially the **Global and U.S. centric funds as a core part of their equity portfolio**.

Among the developed markets **US Market Funds** are more attractive due to a very low co-relation with the developing markets, including India, making these funds suitable for diversification.

**Global funds** provide more diversification as different markets behave differently. And hence these funds have more scope for better risk-adjusted returns.

Though, **Emerging markets** funds provide access to fastest growing economies in world, which have potential for high growth, their exposure to countries like China poses a risk on the category.

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