

Julius Bär

JULIUS BAER
WEALTH REPORT: ASIA

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Front cover:

The Turret of Palace Museum is a landmark historical building in Beijing, China.

EDITORIAL

Dear Reader,

“It was the best of times, it was the worst of times” – To quote the opening lines of ‘The Tale of Two Cities’ by Charles Dickens is an apt way to describe how most investors see the world today. Overcapacities in traditional industries in China are balanced by the wave of consumer-driven activity and higher value-added services. Slower overall growth in Asia masks the boom that is taking place on a sector level, in particular in areas such as travel, the digital economy and beauty capital. Weighing the pros and cons, are you best served being either cautious or confident?

On balance, we believe the final judgment leans in favour of the ‘best of times’. Most large economies in Asia are addressing their structural challenges and are set to draw in foreign direct investment and portfolio flows as a result. In Japan, aggregated statistics fail to capture the dynamism of consumers as they switch from bricks and mortar distribution to being fully fledged digital citizens. In India, asset quality issues in the banking sector are being recognised while household balance sheets are solid and taking on credit to propel the consumer economy.

Amid this dynamism, this year we have added new items to the Julius Baer Lifestyle Index, enhancing our coverage of beauty-related consumption. While the prices of other luxury goods and services may be modulating, the newfound purchasing power of high net worth individuals in Asia is being evidenced in the strong demand for premium creams and treatments.

We invite you to share these insights offered by the 2016 Julius Baer Wealth Report: Asia and thank you for your longstanding interest.



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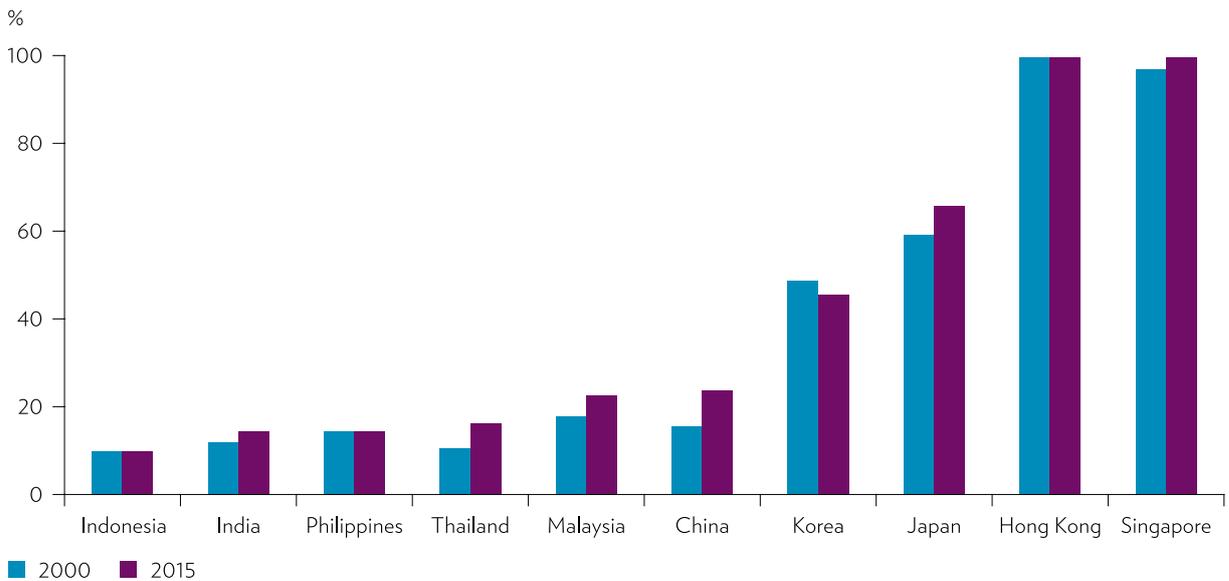


MACRO INTRODUCTION

The 2016 edition of the Julius Baer Wealth Report: Asia marks the sixth consecutive year we have examined trends in wealth creation and lifestyle-related expenditure across the region. Since our first report, Asia has grown by over USD 3 trn in Gross Domestic Product (GDP) and population grew by 157 million. The same number of people has moved into Asia's cities over this period, with 40% of the total population living in metropolises with over one

million residents, according to the World Bank. The knowledge economy has flourished, with close to 14 million patents and trademarks registered, underpinning Asia's continuous movement up the value chain. Likewise travel has boomed: 2015 saw the number of air passengers carried exceed one billion for the first time, representing a 40% increase from when our first report was published in 2011.

Chart 1: Percentage of population living in cities with over one million people

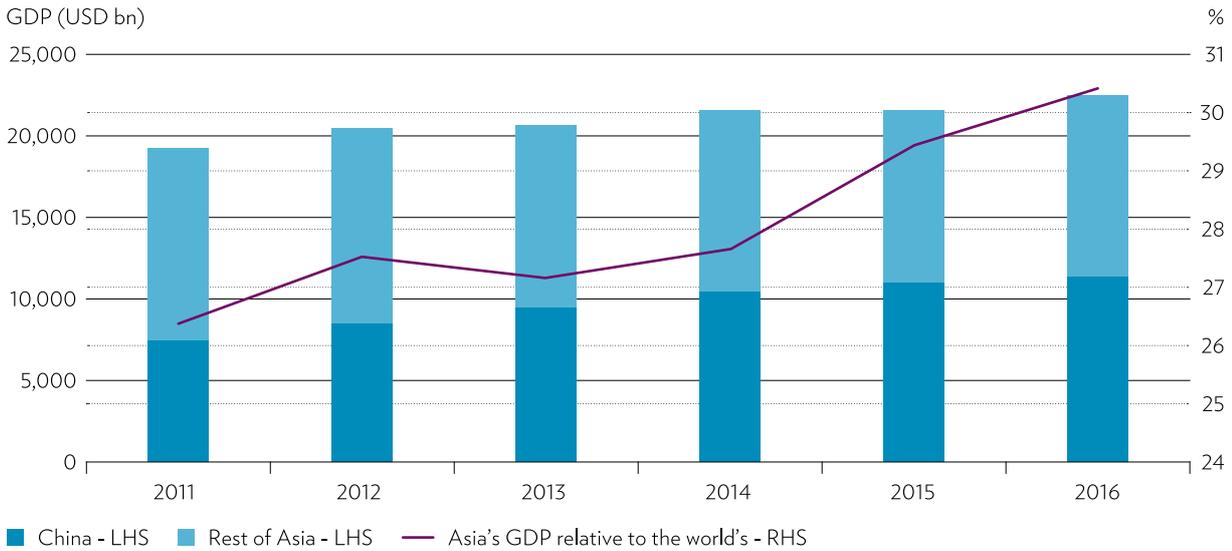


Source: World Bank, Julius Baer

By the same token, international tourist expenditure by Asian travellers has exceeded USD 300 bn, with both China and The Philippines having more than doubled their spending over the past five years. In a broad sense, therefore, the optimism that we expressed regarding Asia's wealth creation prospects in the first report have played out and Julius Baer continues to believe that this region will lead the world in new wealth over the coming decade. Indeed,

most economic fundamentals across Asia today look better than comparables in most parts of the world, in our view and this is unlikely to change over the medium term. Average GDP growth rates, while not as fast as they have previously been, will likely remain relatively high, implying that Asia's share of the global economy will climb beyond the 30% that is set to be reached this year.

Chart 2: Growing slower, but still well ahead of the rest of the world

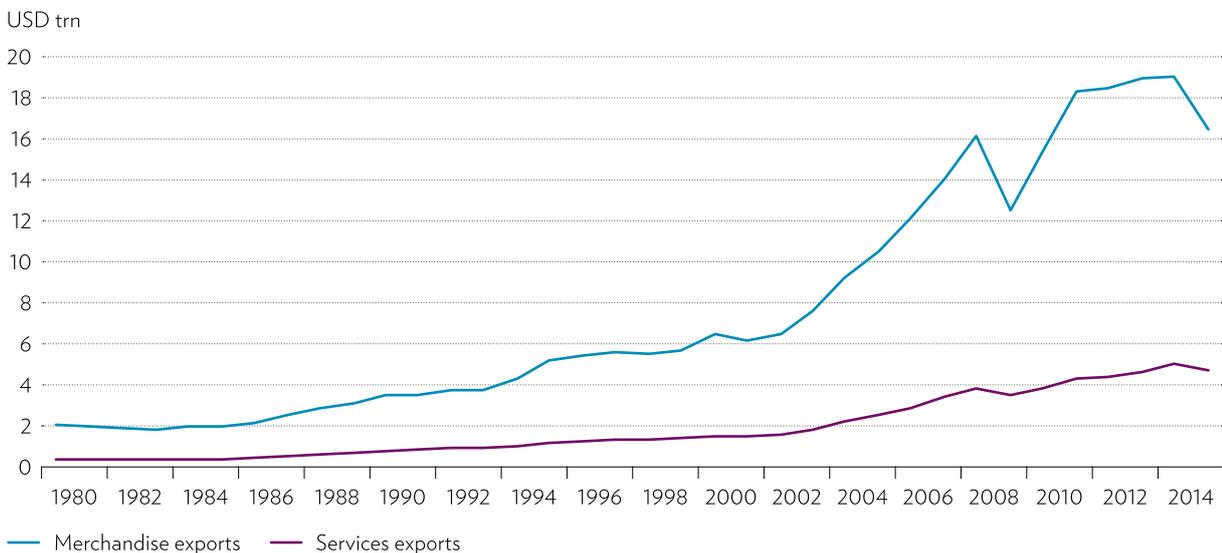


Source: IMF, Julius Baer

While there is ample room to celebrate Asia's economic achievements over the year, the world has simultaneously experienced an array of unexpected and unprecedented developments that should dissuade anyone from resting on their laurels. For example, global trade volumes in 2015 dropped to levels last seen before 2010, according to the World Trade Organisation (WTO). While the economic value added in Asia that stems from services is undoubtedly growing, the wellbeing of the region still remains inextricably tied to the development of manufacturing exports.

Although probably more than 50% of employment in Asia is linked to services, 2015 still saw approximately USD 10 trn worth of merchandise exports, which for a smaller open economy like Singapore, still amounts to double the size of GDP. In other words, the excitement and promise of an accelerating service sector may not fully compensate for the drag in trade volumes, especially when considering that there are spill overs that can impact employment trends, in particular.

Chart 3: Global goods and service exports



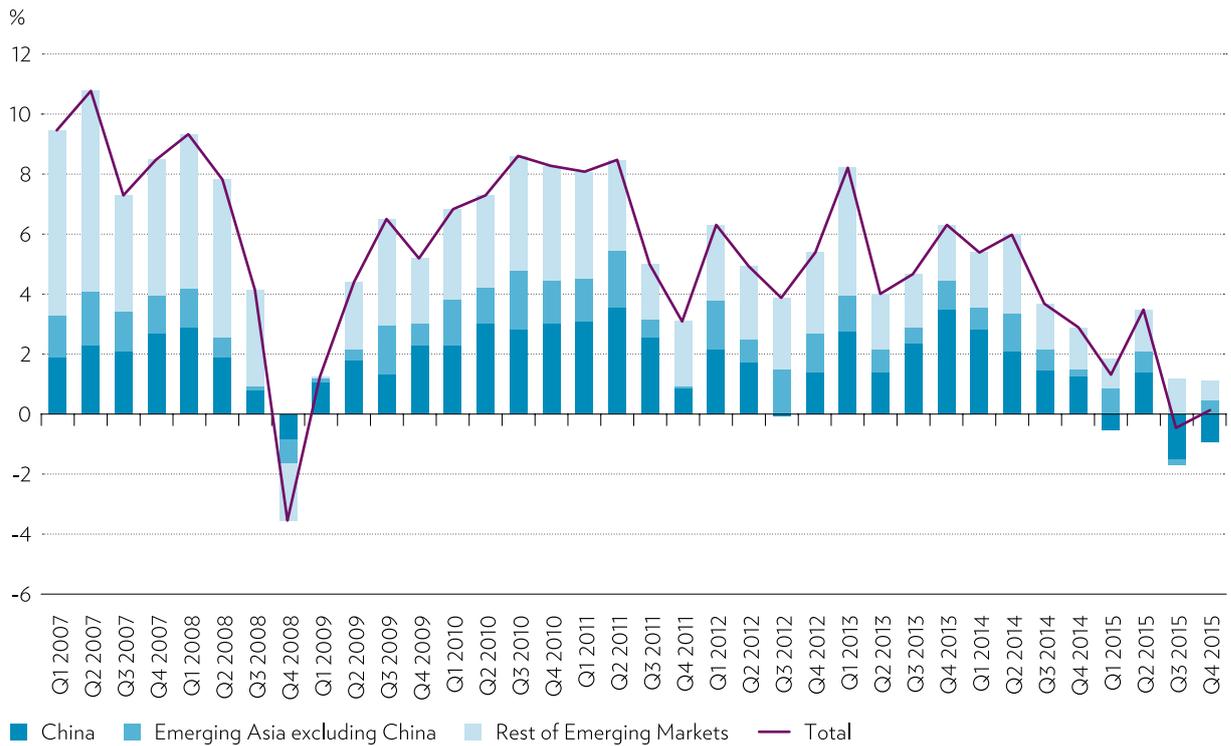
Source: WTO, HSBC, Julius Baer

Further to this, capital inflows to emerging markets have slowed substantially in recent years. The combination of lower capital inflows to emerging markets and the drop in trade can conjure up the notion that we may be witnessing ‘the end of globalisation’ and could be cause for alarm. In part, this would reflect the slowdown in China and the related retooling of its economic model, which now demands less inward investment. Very high investment levels over the past decade have seen the buildup of excess capacities across an array of industries, as evidenced by low utilisation rates. This outcome has led to a chorus of policy makers to advocate that China should speed up the rebalancing of its economy, away from low cost production, supporting services and overall consumption. While there is good cause to believe that this process is

underway, it is equally plausible that substantial restructuring still lies ahead.

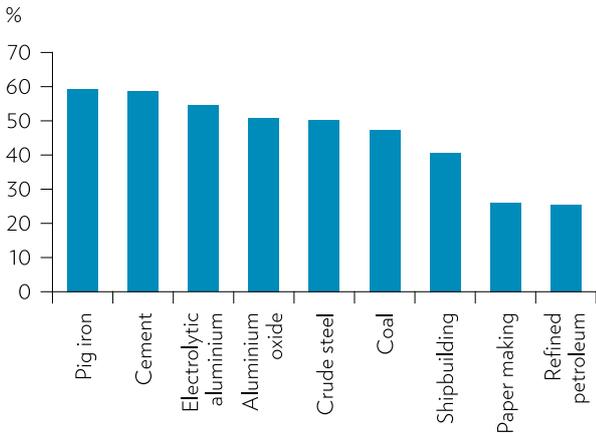
Estimates by HSBC, for example, see room for over two million job losses in the coming years as sectors such as coal, iron & steel and petrochemicals cut back production. It is argued that Japan underwent a similar process in the 1970s, accompanied later on by substantial yen appreciation under the Plaza Accord in 1985. Our view is that China’s rebalancing is clearly a far larger exercise with more at stake; not just for China’s prosperity but with global implications over the very long term. In principle, a medium term outcome whereby the renminbi appreciates against a broad set of currencies would underpin a wealthier society with stronger purchasing power and help drive the re-orientation of economic growth.

Chart 4: Capital inflows as a percentage of GDP



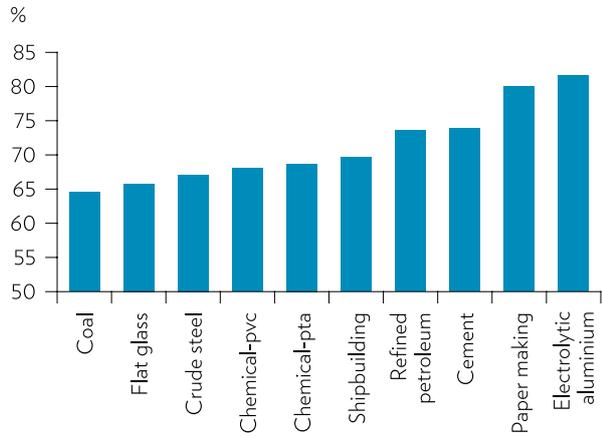
Source: IMF, Julius Baer

Chart 5: China's share of global production by industry (2015)



Source: Nomura Global Economics, Julius Baer

Chart 6: China's capacity utilisation rates by industry (2015)

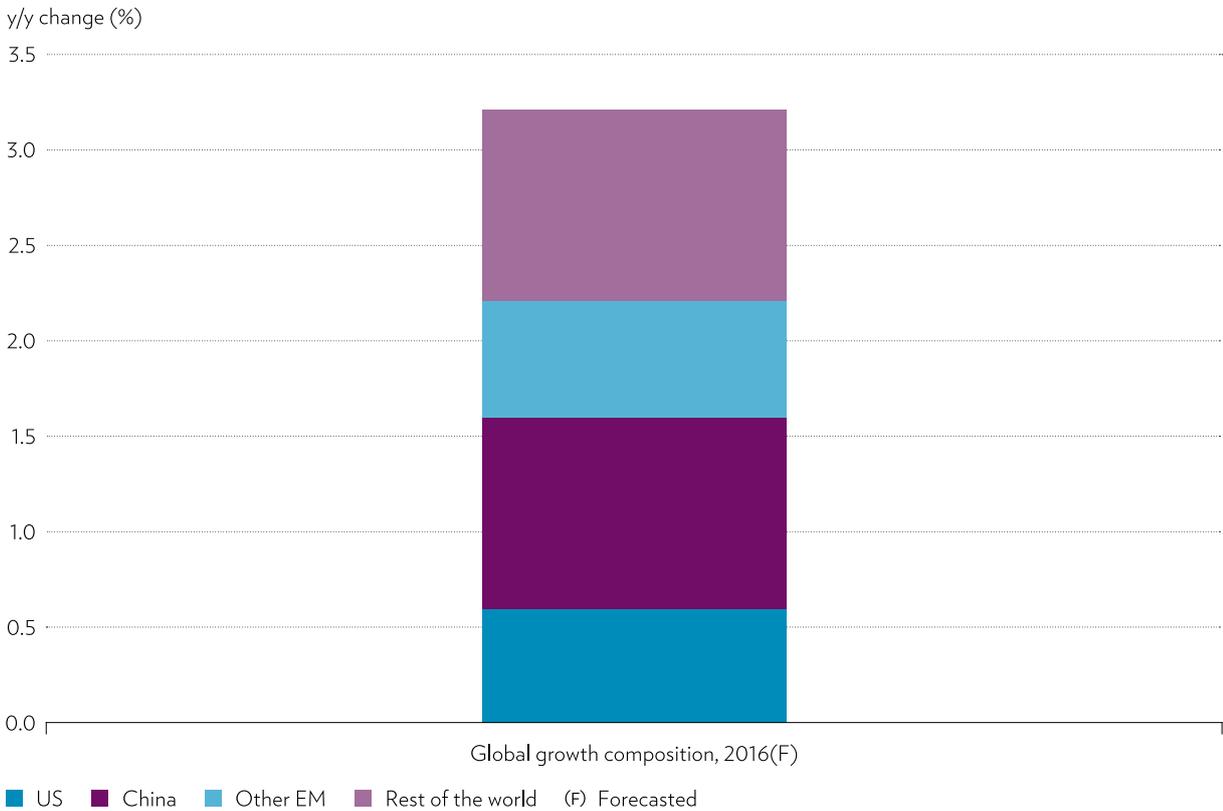


Source: Nomura Global Economics, Julius Baer

In the shorter term, however, we expect to see the next few years mimic the recent trend. In short, global growth will be largely dictated by what happens in the United States (US) and China. Potential GDP growth rates in both have fallen, in part quite naturally due

to demographic shifts, with developments in the rest of the world unable to compensate. This in turn has motivated policy makers to move beyond conventional tools to smoothen the growth cycle.

Chart 7: Global real GDP growth, weighted by nominal GDP



Source: IMF, Deutsche Bank, Julius Baer

The most telling shift that is currently taking place is based on the widespread recognition that the additional easing beyond a certain point, is less likely to yield meaningful benefits. This is arguably the predicament policy makers face in Japan, but less so in Europe. For the US, since the recovery in the labour market began in January 2010, upwards of 14 million jobs have been created, according to the Bureau of

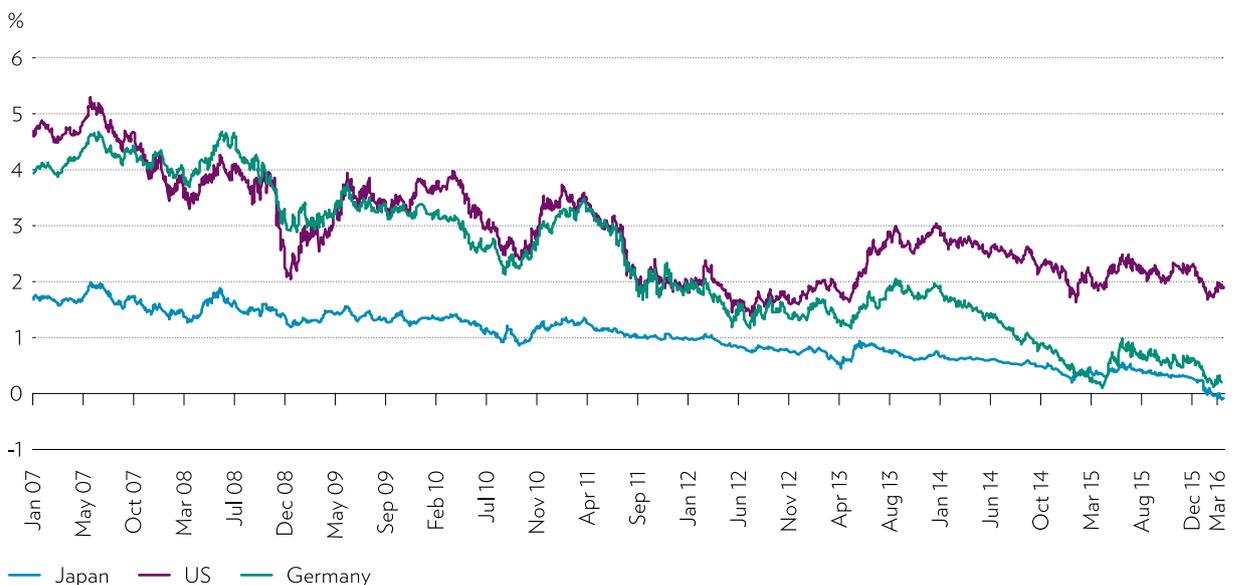
Labor Statistics. At the same time, the expansion of the US Federal Reserve's balance sheet has helped to lift risky asset prices restoring household balance sheets along the way. Arguably US policy can further be declared a success in that US rates have not been pushed below the (in)famous zero lower bound, as is the case for many other developed economies.

Chart 8: US Central bank total assets as a percentage of 2008 GDP



Source: IMF, Bloomberg Finance L.P., Julius Baer

Chart 9: Key interest rates

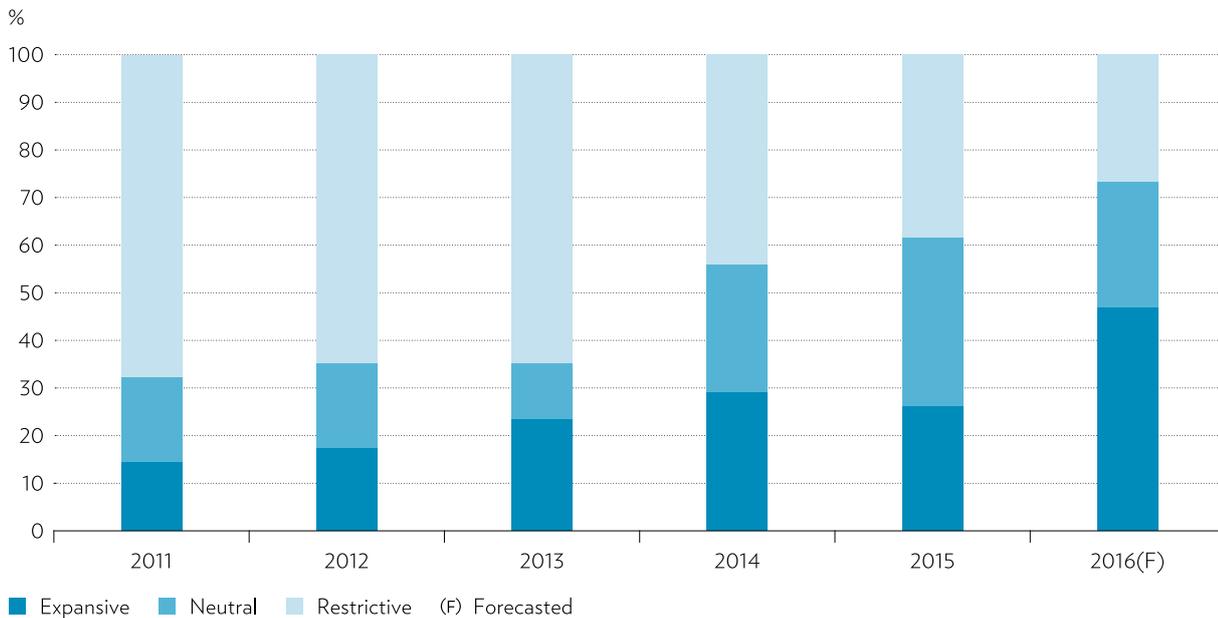


Source: IMF, Julius Baer

Even in economies where asset purchase programmes and/or negative interest rates have become the norm, the singular characteristic of 2016 from a macro perspective can be dubbed the ‘return of fiscal policy’. The combination of fiscal austerity fatigue, widespread concern regarding the efficacy of negative interest rates and a stronger showing for populist-style politics has made increased fiscal spending ‘acceptable’ again. Fiscal responsibility and monetary easing have been

the rallying cry for much of the past five years. The next five Julius Baer Wealth Reports will likely see a different environment where central banks refrain from full normalisation of rates while fiscal policy becomes dominant. In China, we expect to see a tussle between both approaches, designed to cushion the social costs of moving away from commoditised manufacturing exports, which entails slower GDP growth.

Chart 10: Advanced economy fiscal stance

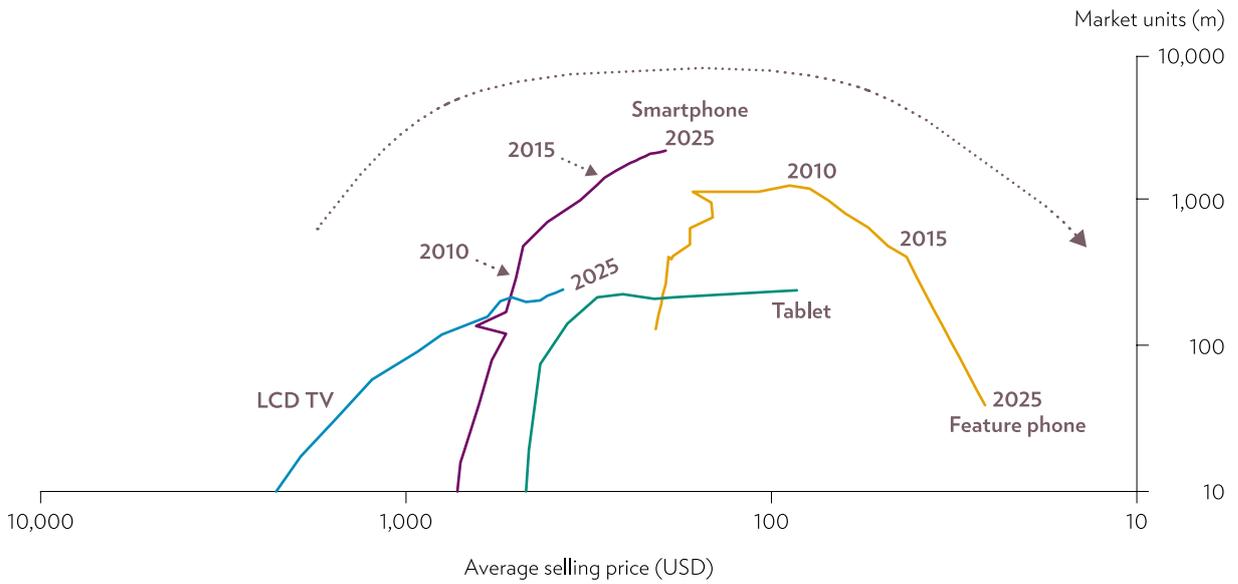


Source: IMF, HSBC, Julius Baer

The key motivating factor that binds most policy makers around the world is the determination (and in many cases, the legal commitment) to stave off deflation. Countries or regions that have deflationary risks, such as the Euro Area, Switzerland and Japan are also matched by the notable lack of inflation in the US. The sizable drop in the US unemployment rate has not been accompanied with a degree of real wage increases so as to push the Federal Reserve to normalise conditions for fear of unwanted price increases. In a later section of this report, we return to the topic of luxury goods and services inflation and find that overall, in Asia, high-end prices fell by 1.68%, in US dollar terms. This marks a stark contrast between conventional inflation series in developed economies, which is often measured in handfuls of basis points.

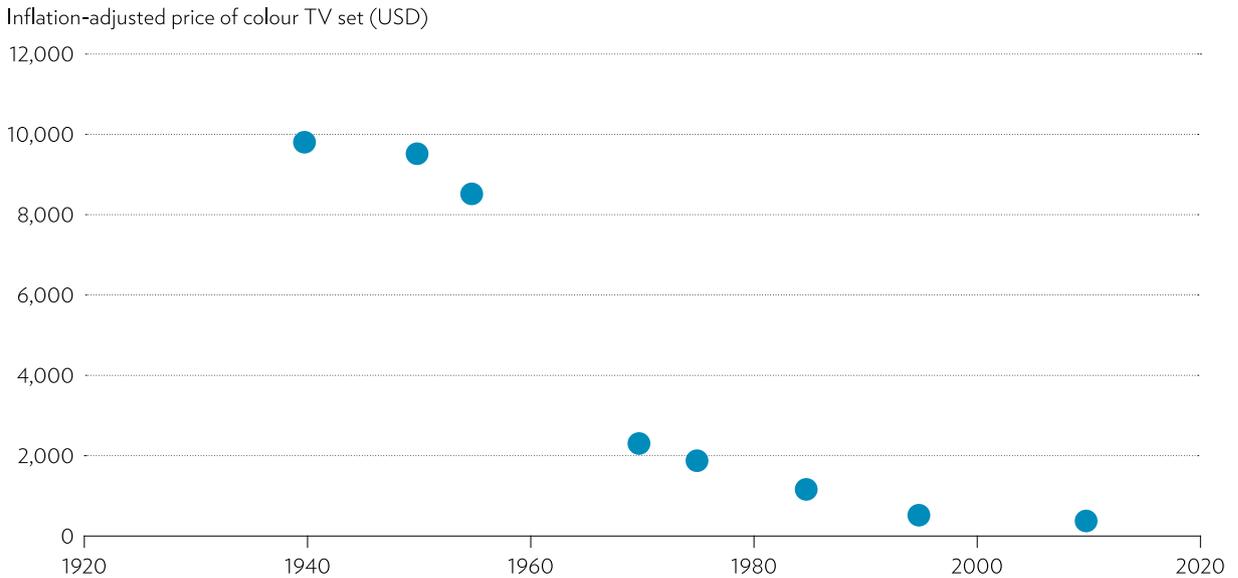
The path ahead will no doubt be very complicated in this arena. For one, the greatly celebrated impacts of ‘disruptive technologies’, which is to say the very rapid adoption of new methods and channels, are equally very deflationary. To illustrate, technology has long been a deflationary force, as evidenced by the price of television sets. These have come down from approximately ten thousand dollars in the 1940’s to a fraction of this price today. Given the pace of this decline, it can hardly be called ‘disruptive’. Fast forward to the present day and the pace of falling prices in consumer electronics and communication devices is indeed, ‘disruptive’.

Chart 11: Technology tends to drive prices lower...



Source: Citi Research, Julius Baer

Chart 12: ...especially over the longer term



Source: Brent Cox (2011), Citi Research, Julius Baer

In the following section of this report, we examine the rise of ‘beauty capital’ whose impacts promise to shake up longstanding norms in the beauty and wellness industries, with interesting questions to be raised about the direction of prices as well. As it happens, the desire to ‘stay young and beautiful’ echoes another deflationary force: global ageing. Japan demonstrates both the opportunity of beauty capital in an ageing society, and likewise the challenge that is presented:

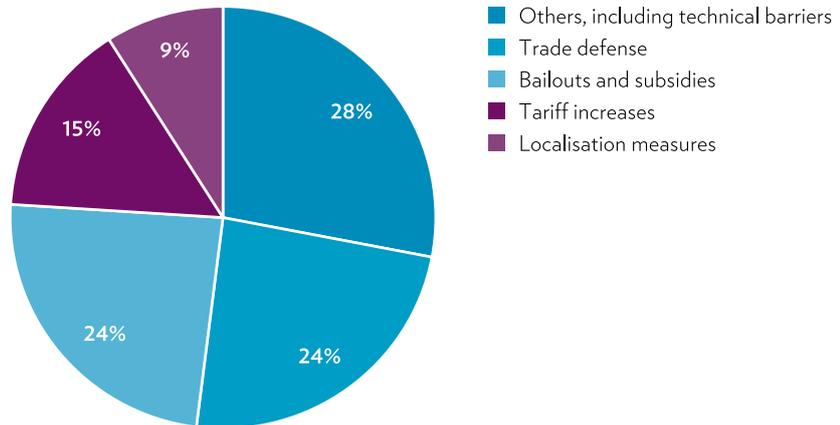
on balance, ageing populations tend to accompany lower inflation.

The second major complication on the macroeconomic front is the risk that protectionism, which has been silently rising. Financial markets dealt a harsh verdict against the outcome of the United Kingdom’s referendum on European Union membership this past summer, arguably in part because of the adverse

impact on trade flows between the two parties. Both fiscal and monetary policy are ill-equipped to counteract artificial hindrances to trade. According to Global Trade Alert, since 2008, over 5,000 trade-

distorting measures have been enacted around the world. In our view, this represents perhaps the most significant threat to wealth creation on a global basis.

Chart 13: Distribution of trade distorting measures since 2008 (%)

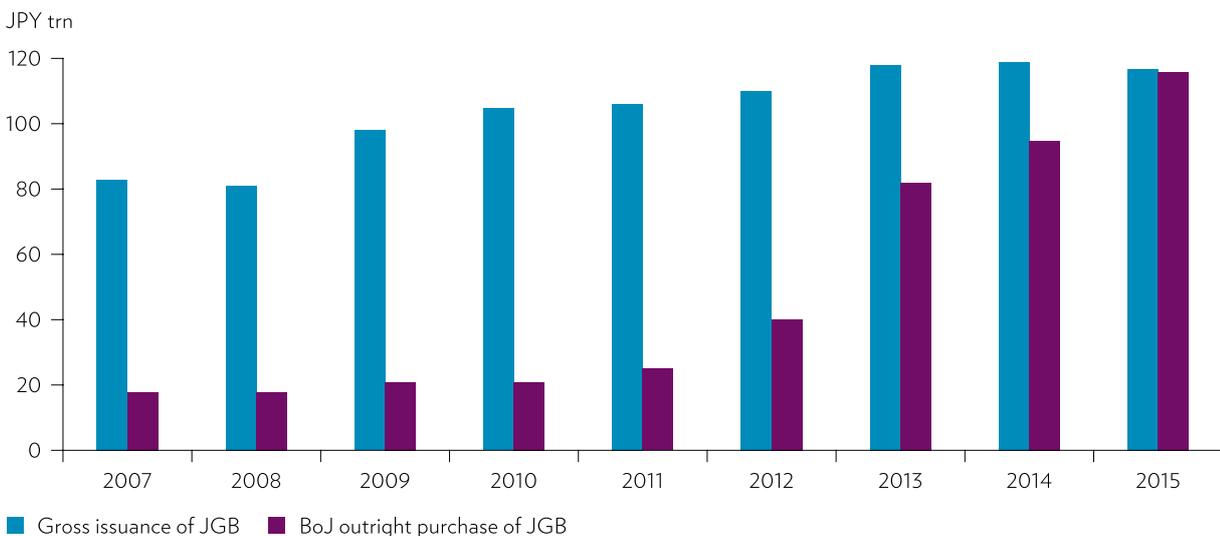


Source: Global Trade Alert, HSBC, Julius Baer

Hopefully, there is time for policy makers to reverse this recent trend and avert a major swing toward protectionism. Undoubtedly, Asia would be hard hit under such circumstances. In the shorter term, however, the region is faced with more prosaic issues, such as the Bank of Japan's policy path given the

move to negative interest rates and the dwindling supply of government bonds available for purchase. In the subsequent section of this report, take a closer look at the factors driving wealth creation, along with the where's and why's.

Chart 14: Gross issuance and Bank of Japan's (BoJ) outright purchase of Japanese government bond



Source: Japan Ministry of Finance, HSBC, Julius Baer

JULIUS BAER LIFESTYLE INDEX

Introducing the 2015/2016 lifestyle index

For the sixth year running, we present our Julius Baer 2016 Lifestyle Index. This index comprises a basket of goods and services that closely reflects the lives of High Net Worth Individuals (HNWI) in Asia. We continue to present our findings across the expanded index of 11 cities but this time, in light of volatile currency movements, we present our data in both local currency and US dollar currency terms to allow for a more thorough analysis of demand and supply trends.

In addition, we included a new skincare item, a high-end skin cream to our index to complement the

facial aesthetic item of botox, extending our number of items measured from 20 to 21. The new item reflects the growing investment by HNWI in Asia on super-premium skincare products.

Overview

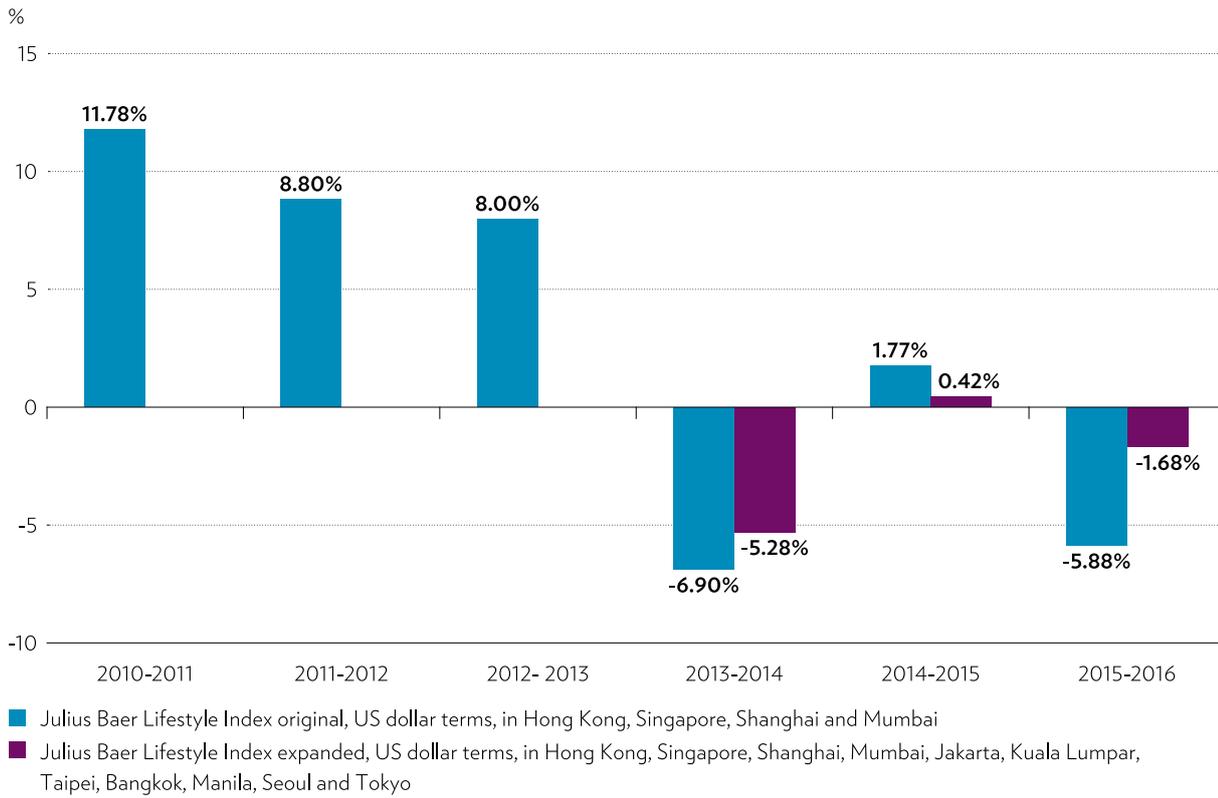
Overall prices for the items in our Lifestyle Index fell by 0.68% in local currency terms and by 1.68% year on year (y/y) in US dollar terms. This lags the average inflation experienced in the various Asian cities of +1.73% y/y during 2015, suggesting low correlation between conventional measures of inflation and that represented by our basket of luxury goods and services.

Chart 1: Inflation vs index

	Hong Kong	Singapore	China	India	Taiwan	Indonesia	Philippines	Korea	Malaysia	Thailand	Japan	Average
2015 Consumer price inflation	3.00%	-0.50%	1.40%	4.93%	-0.30%	6.40%	1.40%	0.70%	2.10%	-0.90%	0.80%	1.73%
Julius Baer Lifestyle Index Y/Y local currency	-0.47%	-6.76%	-1.14%	-4.62%	3.30%	-1.30%	2.61%	-2.41%	3.34%	0.95%	-0.94%	-0.68%
Julius Baer Lifestyle Index Y/Y USD	-0.56%	-6.61%	-7.08%	-9.25%	-0.26%	-0.58%	-0.62%	-4.52%	-2.93%	-2.21%	16.14%	-1.68%

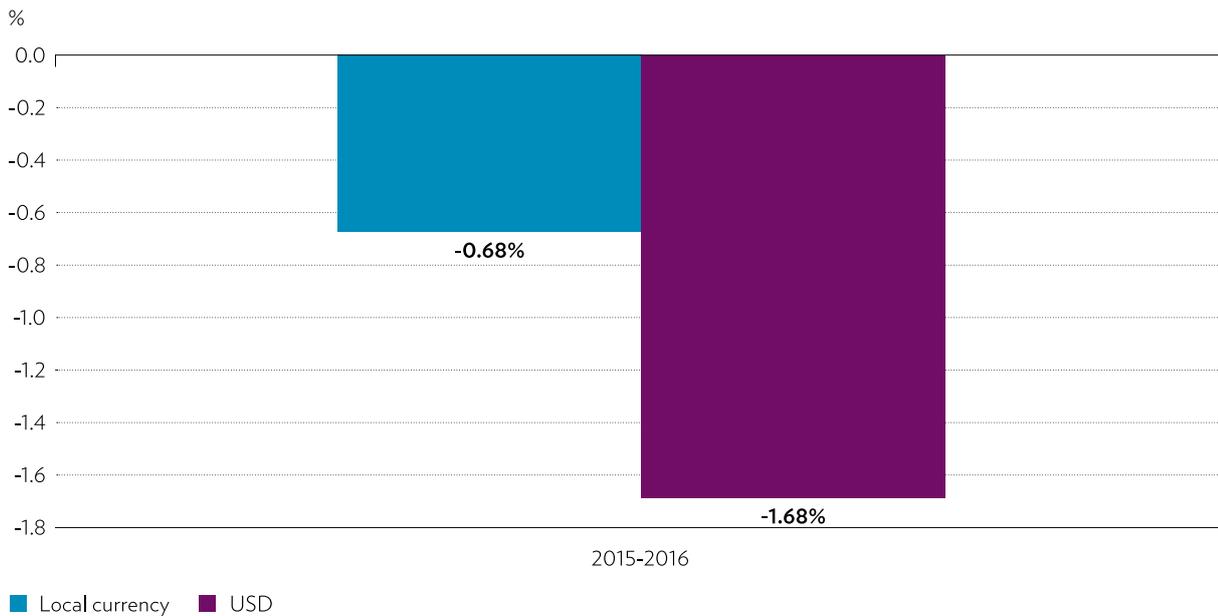
Source: World Bank, CSG Intage, Julius Baer

Chart 2: Julius Baer Lifestyle Index, changes in prices of goods and services y/y, 2010 to 2016, US dollar terms



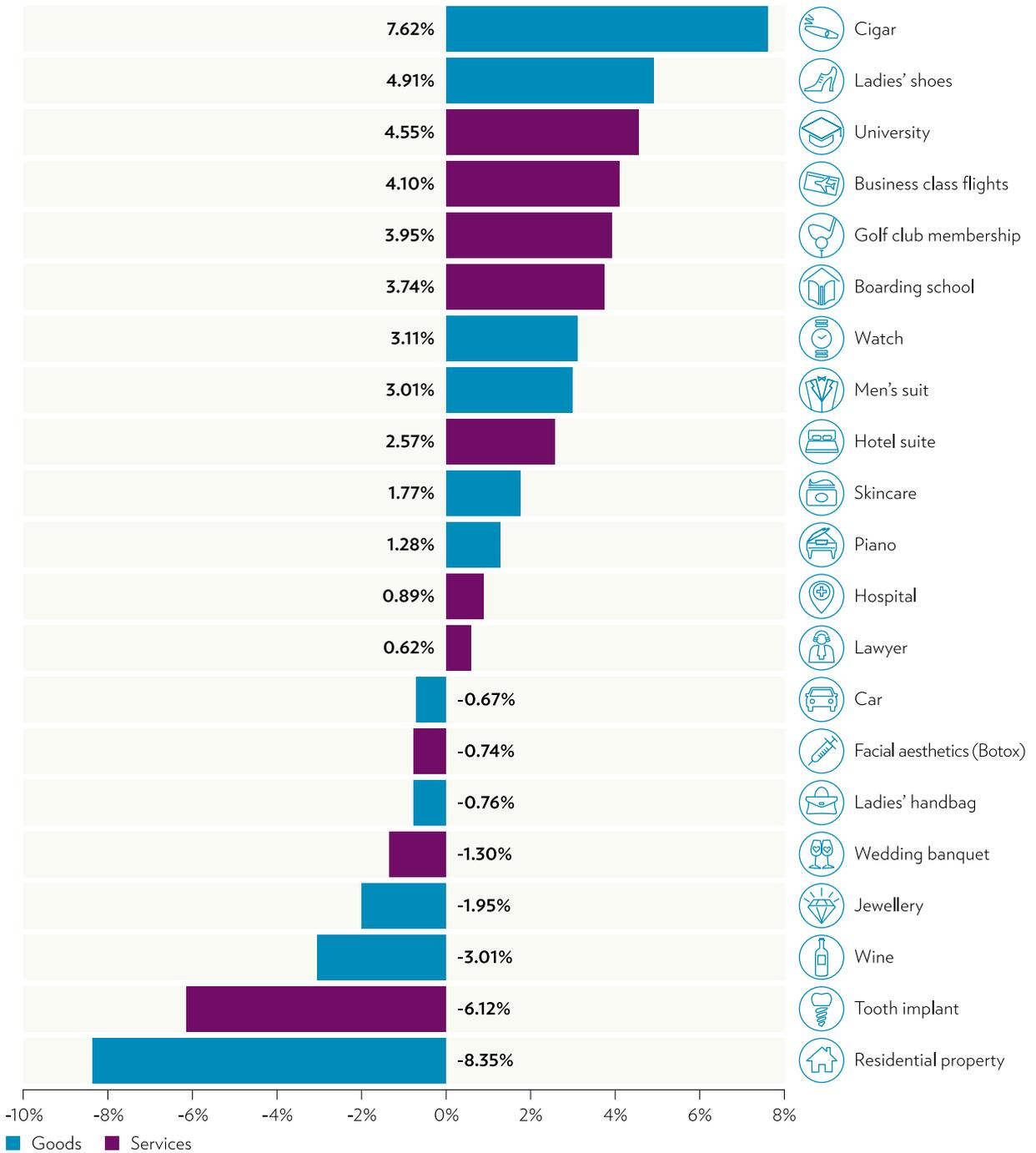
Source: CSG Intage, Julius Baer

Chart 3: Julius Baer Lifestyle Index, changes in prices of goods and services y/y, 2015 to 2016, local currency and US dollar terms



Source: CSG Intage, Julius Baer

Chart 4: Price changes of Julius Baer Lifestyle Index items, y/y US dollar terms

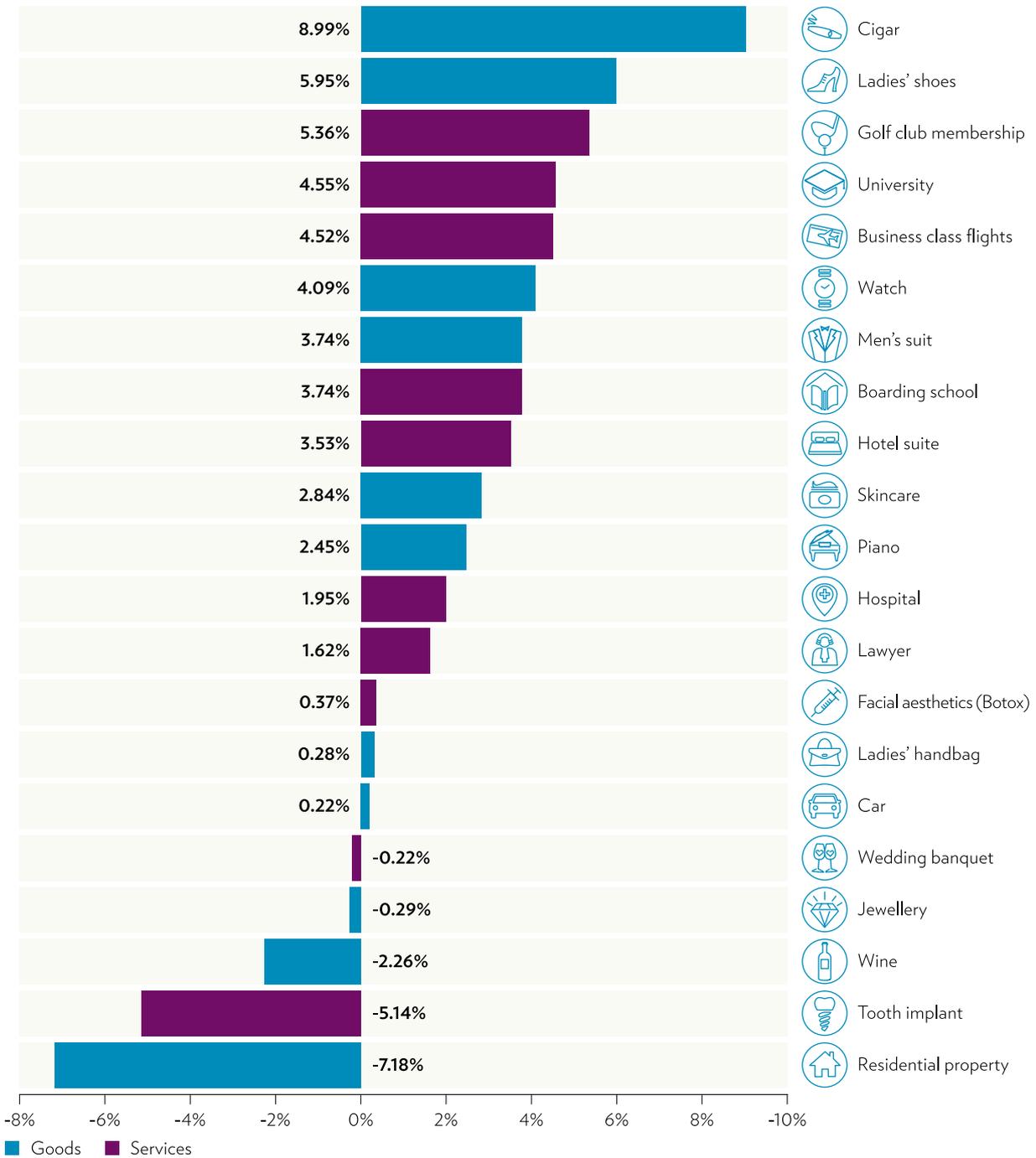


Source: CSG Intage, Julius Baer

In local currency terms, 16 of the 21 items in our index showed positive price momentum y/y, suggesting the overall demand for a number of luxury goods and services remains relatively resilient. The biggest price increases were found in cigars (+8.99%), ladies' shoes (+5.95%) and golf club memberships (+5.36%) while the biggest declines came from residential properties (-7.18%), tooth implants (-5.14%) and wine (-2.26%).

In US dollar terms, we see an overall price decline (-1.68%), the second year since 2013/14 where this has occurred. More specifically, 8 of the 21 items measured suffered price declines on a y/y basis as US dollar strength negated stable or relatively small price increases in local currencies. Of note, the US dollar appreciated against most (8 out of 11) of our measured currencies with the exception of the Japanese yen, Singapore dollar and Indonesian rupiah.

Chart 5: Price changes of Julius Baer Lifestyle Index items, y/y local currency terms



Source: CSG Intage, Julius Baer

US dollar-denominated items such as university fees (+4.55%) and boarding school fees (+3.74%) saw steady price increases, reflecting the ability of prestigious educational institutions to set prices higher regardless of currency movements or economic conditions.

We identify some trends that can help to explain the price movements in our basket of high-end goods and services. The first is the broad-based devaluation of Asian currencies. The second would be government-related measures which typically affect demand dynamics. The third relates to competitive pressures which can also influence prices of luxury goods and services.

Chart 6: Currency effects

	Hong Kong USD/ HKD	Singapore USD/ SGD	Shanghai USD/ CNY	Mumbai USD/ INR	Taipei USD/ TWD	Jakarta USD/ IDR	Manila USD/ PHP	Seoul USD/ KRW	Kuala Lumpur USD/ MYR	Bangkok USD/ THB	Tokyo USD/ JPY	Average
2015 FX rate*	7.75	1.35	6.21	63.71	31.05	13,347.51	45.16	1,129.88	3.77	34.02	123.55	
2016 FX rate*	7.76	1.35	6.64	67.21	32.24	13,242.70	46.74	1,156.74	4.03	35.20	104.29	
Change	-0.10%	0.17%	-6.45%	-5.21%	-3.68%	0.79%	-3.36%	-2.32%	-6.48%	-3.35%	18.47%	-1.05%

* Average FX rate from 1 June – 31 July 2015/2016 respectively

Source: Bloomberg Finance L.P.

As seen in the table above, on average the currencies for the 11 cities we surveyed weakened against the US dollar (-1.05%) between June/July 2015 and June/July 2016. This has a negative impact on our lifestyle index which we report in US dollar terms for standardisation. The worst performing currencies were the Malaysian ringgit (-6.48%), Chinese yuan (-6.45%) and Indian rupee (-5.21%). The major exception was the Japanese yen which gained 18.47% while the Singapore dollar (+0.17%) and Indonesian rupiah (+0.79%) were relatively stable. There is limited impact on Hong Kong dollar (-0.10%) as it is pegged to the US dollar.

A weaker currency not only diminishes the purchasing power of a HNWI in his/her home-currency but also influences his/her decision on where to purchase a particular good. For example, the reversal of yen weakness in 2016 is likely to result in a reduced number of Chinese tourists to Japan where locals are not expected to spend as much at home to counterbalance. On the other hand, the yen's purchasing power has increased, making imported luxury goods more affordable for Japanese tourists abroad.

Government intervention

The personal luxury goods market in China, Hong Kong and Macau remains soft under the number of government measures aimed at reducing ostentatious spending and regulating the grey market in China. This could explain further y/y declines for prices of items such as jewellery, ladies' shoes and wine in Shanghai and Hong Kong.

However, the propensity of the Chinese to spend on luxury items remains high. Research by Bain & Co shows that Chinese consumers continue to make up the largest portion of luxury purchases (31%) globally, followed closely by Americans (24%) and Europeans (18%). Instead of spending in Greater China, Chinese consumers have redirected their purchases to mature markets such as Europe where tax-free shopping is popular as well as Japan and Korea where they seek to leverage on currency fluctuations when it moves in their favour. We see some evidence of this from higher price movements in Seoul and Tokyo for ladies' shoes, ladies' handbags and men's suits where the identical product is available across the various Asian cities.

In the past year, we have also witnessed a reduction of import duties on luxury goods in countries such as China, Indonesia and Thailand. The goal of the duty cuts is to encourage consumers to spend more domestically (rather than abroad) and boost retail-sales growth. This necessarily has a deflationary impact in our index of luxury items where taxes are included in the final calculation.

Another area where we see the impact of regulation and policy changes in the property sector. Here the government has many levers to tweak both supply (land sales) and demand (stamp duties and other taxes and financing restrictions/costs) in order to moderate (from the government's perspective) over-inflated prices or to boost anaemic ones. Government cooling measures have tapered demand for property in Singapore and Jakarta while a more efficient permissions approval process in Mumbai is likely to reduce the price tag for residential projects in the city.

Competitive landscape

A change in supply conditions from a more competitive environment can have an impact on items on our index which are less differentiated and more susceptible to substitution effects (e.g. business class flights and high-end hotel accommodation).

We see a clear example of this in the pricing for business class flights out of Kuala Lumpur, where capacity additions from Middle Eastern Airlines has led to more competition and prices falling by more than 20%, according to industry experts.

The hospitality segment is also susceptible to changes in supply conditions. When new hotels of a similar quality are built in close proximity to existing hotels, there is often a discounting on overall room rates and ancillary rates (function rooms etc). We see some evidence of this for wedding banquet prices in Mumbai (-16.7%) and Seoul (-8.2%) where new high-end hotels opened over the past year. Interestingly, this had an opposite effect in Kuala Lumpur where hoteliers managed to re-price room rates higher as new 5-star hotel supply raised the overall quality of accommodation in the city.



Introducing high-end skin cream to our Lifestyle Index

This year for the first time we include a high-end skincare cream to our Lifestyle Index to complement botox as a facial aesthetic item. As described in our special on beauty capital in the later section of this report, skincare is the second most dynamic and largest growth contributor to the beauty and personal care industry, accounting for nearly one third of global beauty market value growth over 2014–2019(E).

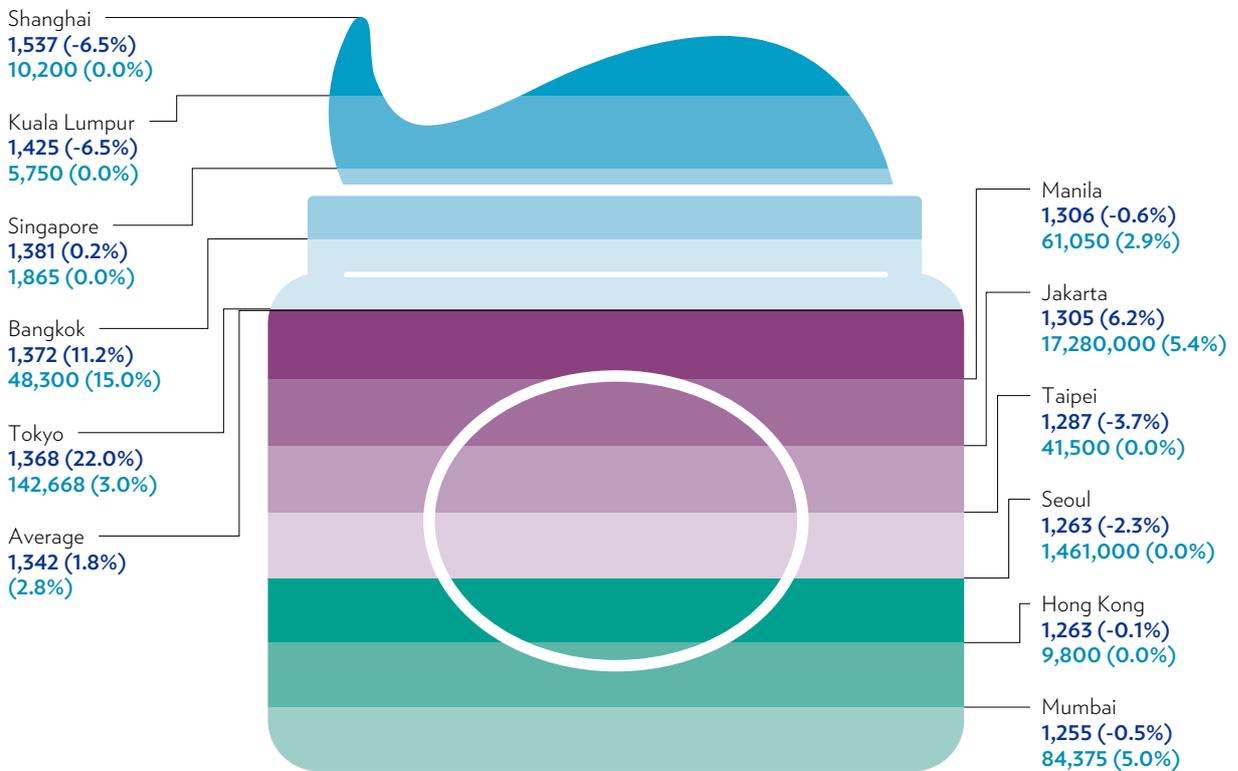
According to Euromonitor, Asia Pacific is predicted to generate USD 6 bn new sales in premium cosmetics over the next five years, due primarily to the strong demand from China. Within the premium cosmetics category, skincare remains the most valuable category in terms of growth potential. Super-premium skincare products have been positioned by cosmetics firms such as Beiersdorf via their super-premium brand

La Prairie to target the ultra-affluent consumers who are not affected by changes in economic conditions.

After extensive research, we have selected La Prairie’s Cellular Cream Platinum Rare (50ml) to represent this category in our index. A 50ml bottle of the cream retails at an average price of USD 1,342 among the cities we surveyed with Shanghai being the most expensive city to purchase the cream (USD 1,537) and Mumbai the cheapest (USD 1,255). This hefty price tag makes it one of the most expensive moisturisers per ounce on the market.

In US dollar terms, we found that the price for our high-end skin cream rose on a y/y basis (+1.8%) outperforming the overall index which fell by an average of 1.68% and reflecting price resilience for the product category. That said, we will need to examine price trends for this item over a longer period of time to make any firm conclusions.

Chart 7: Skincare



■ 2016 cost (USD) / 2016 vs 2015 cost change (%) ■ 2016 cost (Local currency) / 2016 vs 2015 cost change (%)

Source: CSG Intage, Julius Baer

Business class flights

Our index showed an average increase of +4.5% (+4.1% in US dollar terms) in prices for business class flights from specific Asian cities to London/New York. The greatest volatility was seen in flights departing from Kuala Lumpur (-20.6% y/y), Jakarta (+17.0% y/y) and Tokyo (+34.5% y/y).

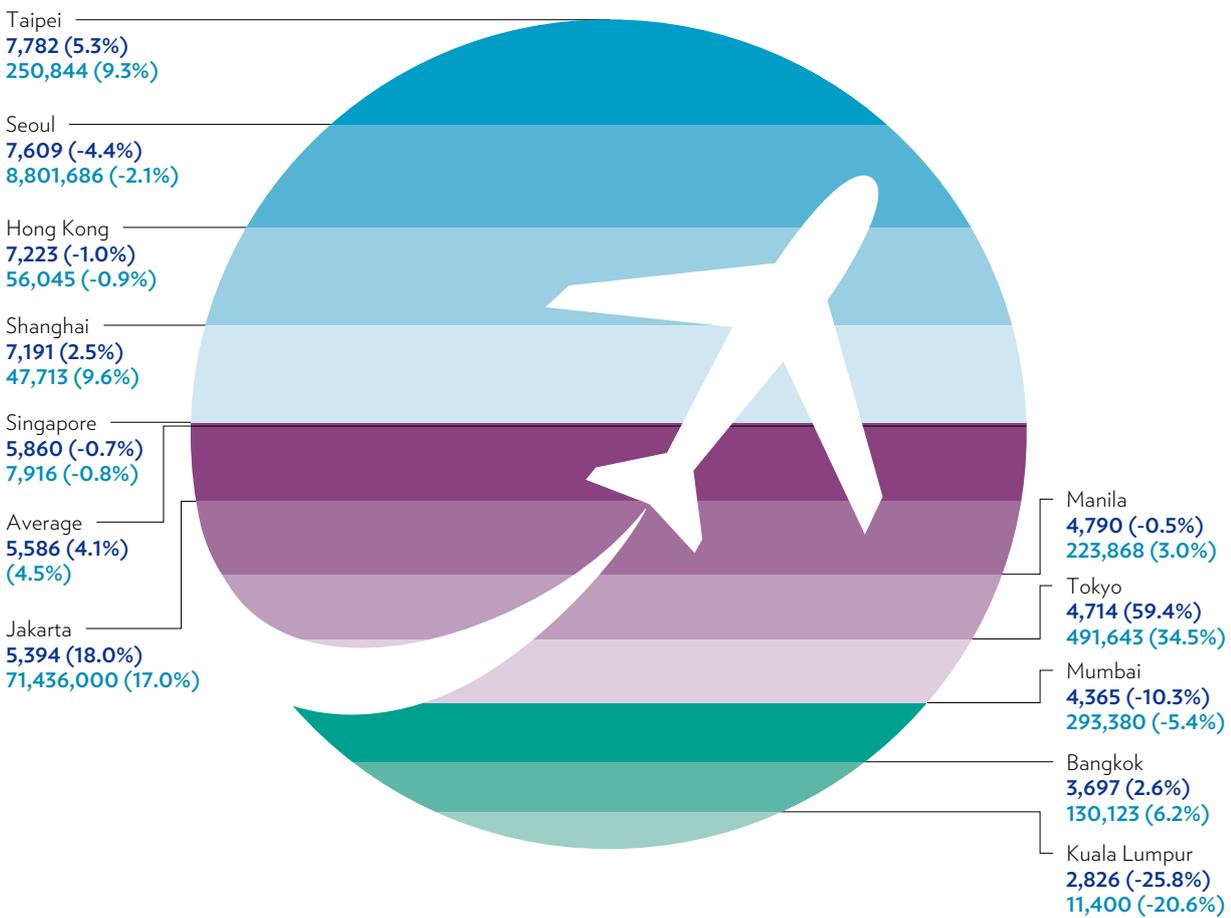
Clearly, the significant strengthening of the Japanese yen was a contributor to higher airfares from Tokyo. However, prices were also reportedly influenced by a reduction in capacity as international carriers like British Airways and United Airlines upgraded from 777s and 747s to smaller but newer 787s, leading to a capacity reduction of 38%–48%. Over the medium term however, we expect pricing dynamics on Japanese outbound flights to be affected by

increased competition from Haneda Airport (versus Narita airport where we currently derive our price data) which has opened a new international terminal to handle both short-haul and long-haul flights.

Business class flights out of Kuala Lumpur were cheaper y/y as the ringgit depreciated and capacity was added by competing airlines. For example, British Airways started adding flights from Kuala Lumpur to London in the past year in a route which has been historically monopolised by Malaysia Airlines.

The cheapest cities for a round-trip full fare business class flight to New York and London are Kuala Lumpur, Bangkok and Mumbai, while the most expensive city for this trip is now Taipei (previously Seoul).

Chart 8: Business class flights



■ 2016 cost (USD) / 2016 vs 2015 cost change (%) ■ 2016 cost (Local currency) / 2016 vs 2015 cost change (%)

Source: CSG Intage, Julius Baer

Residential property

Residential property (defined in our data set as one based in a prime location at around 4,000 sqft in area) which is allocated a higher weighting of 30% in our index due to its importance in asset allocation, experienced one of the largest y/y declines of -7.2% (-8.4% in US dollar terms). Amongst the hardest hit cities were Singapore (-26.4%), Mumbai (-21.9%) and Tokyo (-11.9%).

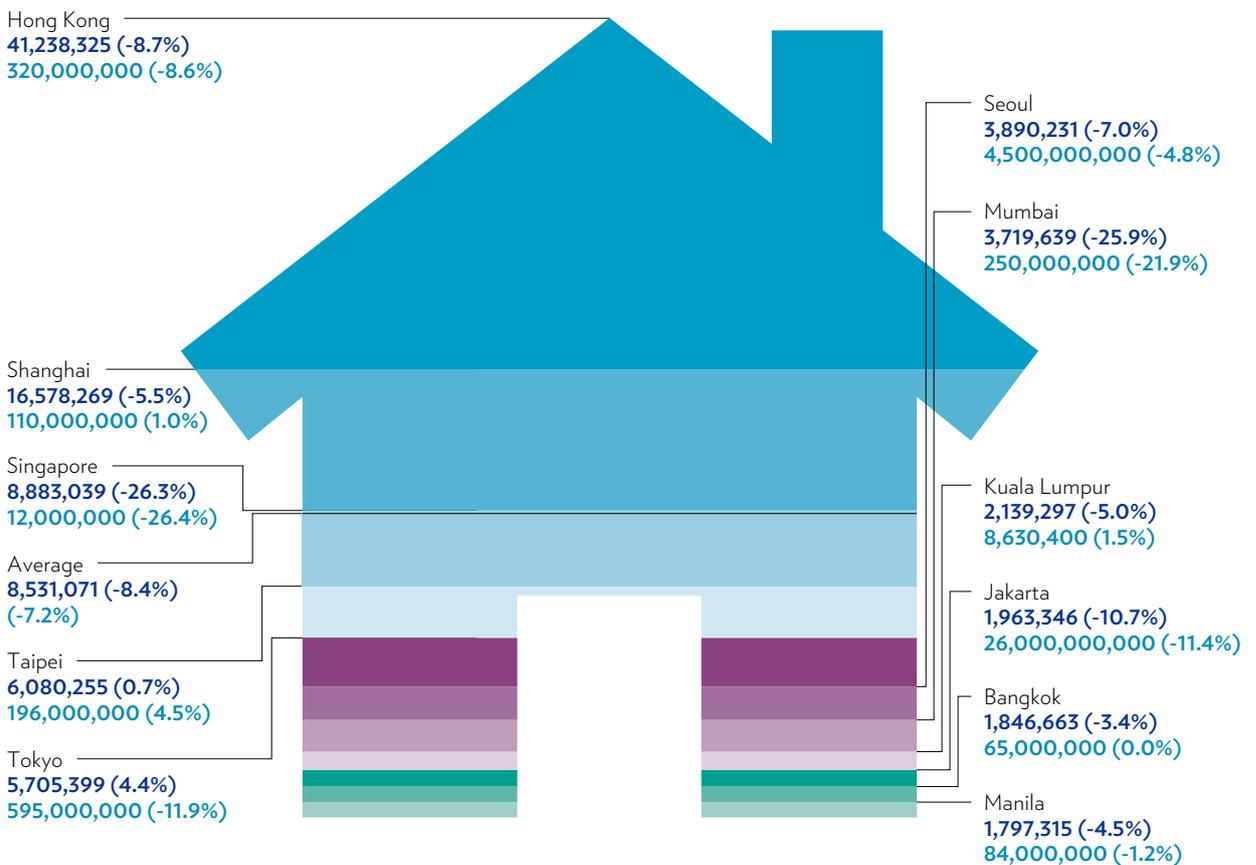
Singapore property prices remained soft as previously imposed stamp duties and property loan restrictions deterred non-resident investors and dampened speculative activity. However, we are starting to see signs of a bottoming of activity particularly in the prime districts where sales volumes have increased sharply in the first half of 2016 due to the various incentives and discounts offered by developers. We believe that over the medium term, Singapore's key destination status for quality health care services coupled with its

enduring status as a liveable and business city, will continue to appeal to foreign homebuyers.

Jakarta property prices continue to moderate in 2016. Although the market saw an increase in launching activity, buying sentiment has remained lukewarm; investors and end-users are holding their plans to buy apartments in view of the current economic slowdown. Tighter mortgage rules since 2013 have hurt sentiment as Bank Indonesia has repeatedly emphasised that it will continue to closely monitor the market and enforce policies to prevent the property market from overheating. There is some expectation however that loan-to-value (LTV) regulations could be eased this year to bolster the current sluggish market.

Overall, we find that property prices remain the loftiest in the financial hubs of Shanghai, Singapore and Hong Kong while they are least expensive in Jakarta, Bangkok and Manila.

Chart 9: Residential property



■ 2016 cost (USD) / 2016 vs 2015 cost change (%) ■ 2016 cost (Local currency) / 2016 vs 2015 cost change (%)

Source: CSG Intage, Julius Baer

Hotel suite

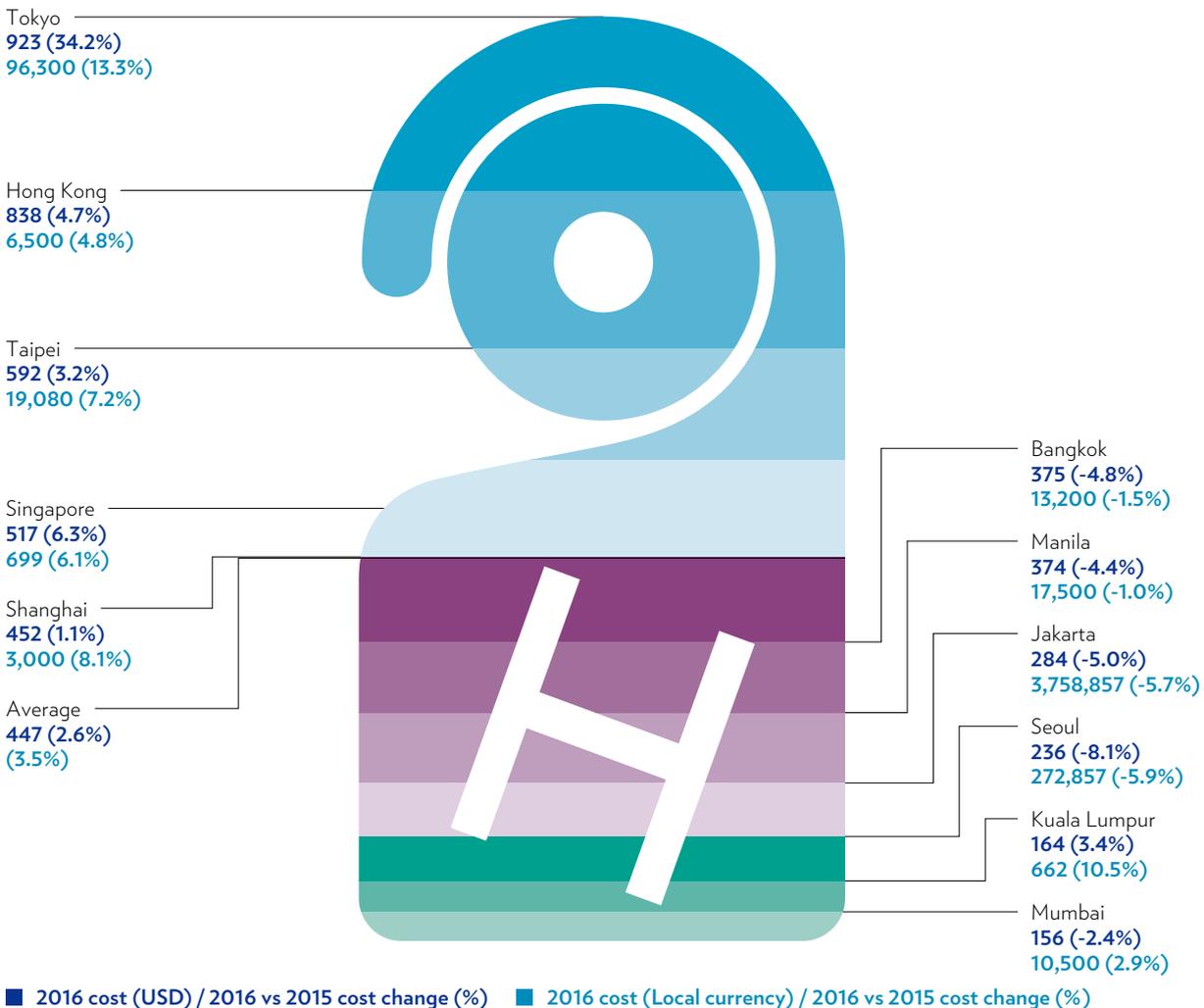
The average cost of an overnight stay at a centrally located 5-star hotel rose by 3.5% (+2.6% in US dollar terms) with the biggest price movements found in Tokyo (+13.3%) and Kuala Lumpur (+10.5%).

Although already the most expensive city for a hotel stay in Asia, room rates in Tokyo inched even higher on the back of record inbound tourist flows and limited new supply. This kept Tokyo in pole position this year as the most expensive hotel suite option

in Asia. By comparison, a stay at a suite of a similar quality is about five times cheaper in Mumbai, which is our least expensive city for the category.

The price jump in Kuala Lumpur may in part be explained by a new supply of high-end hotels (Grand Hyatt, St Regis) which has helped to reprice room rates for the city where rates have typically lagged Asian counterparts. Even so, hotel rates for a 5-star hotel in the city are still the second cheapest in the region besting only Mumbai.

Chart 10: Hotel suite



Source: CSG Intage, Julius Baer

Wedding banquet

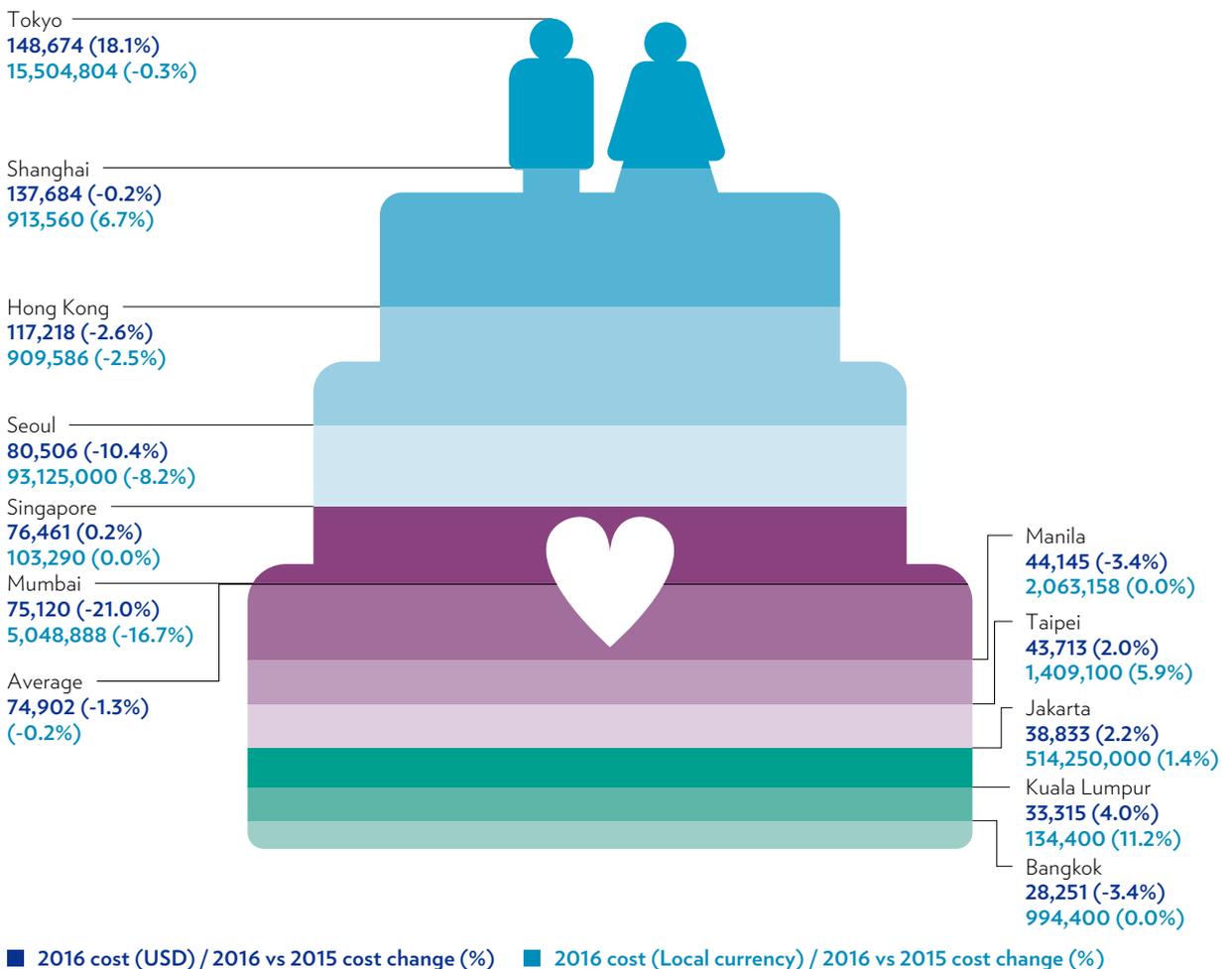
Arguably, no investment is more rewarding than for one's wedding ceremony. Every year, as part of our dataset, we source pricing for a wedding banquet for around 500 guests at a top-end hotel. Banquet pricing typically sees low level of flux in terms of pricing for hotels and tends not to change day to day based on demand. In local currency terms, banquet prices remained stable across the cities we surveyed at -0.2% y/y (-1.3% in US dollar terms).

However, we did see a notable increase in Kuala Lumpur (+11.2%) which is in line with the rising

pricing trend for luxury hotel room rates in Kuala Lumpur from a repricing of the market with new supply. On the other hand, Seoul (-8.2%) and Mumbai (-16.7%) suffered large declines due in part to new hotel/function room supply in those cities (Seoul: New Four Seasons and JW Marriot; Mumbai: New JW Marriot).

The most expensive city in Asia to plan your nuptials continues to be Tokyo (USD 148,674) where it costs more than five times as much as Bangkok (USD 28,251) the cheapest city to do so.

Chart 11: Wedding banquet



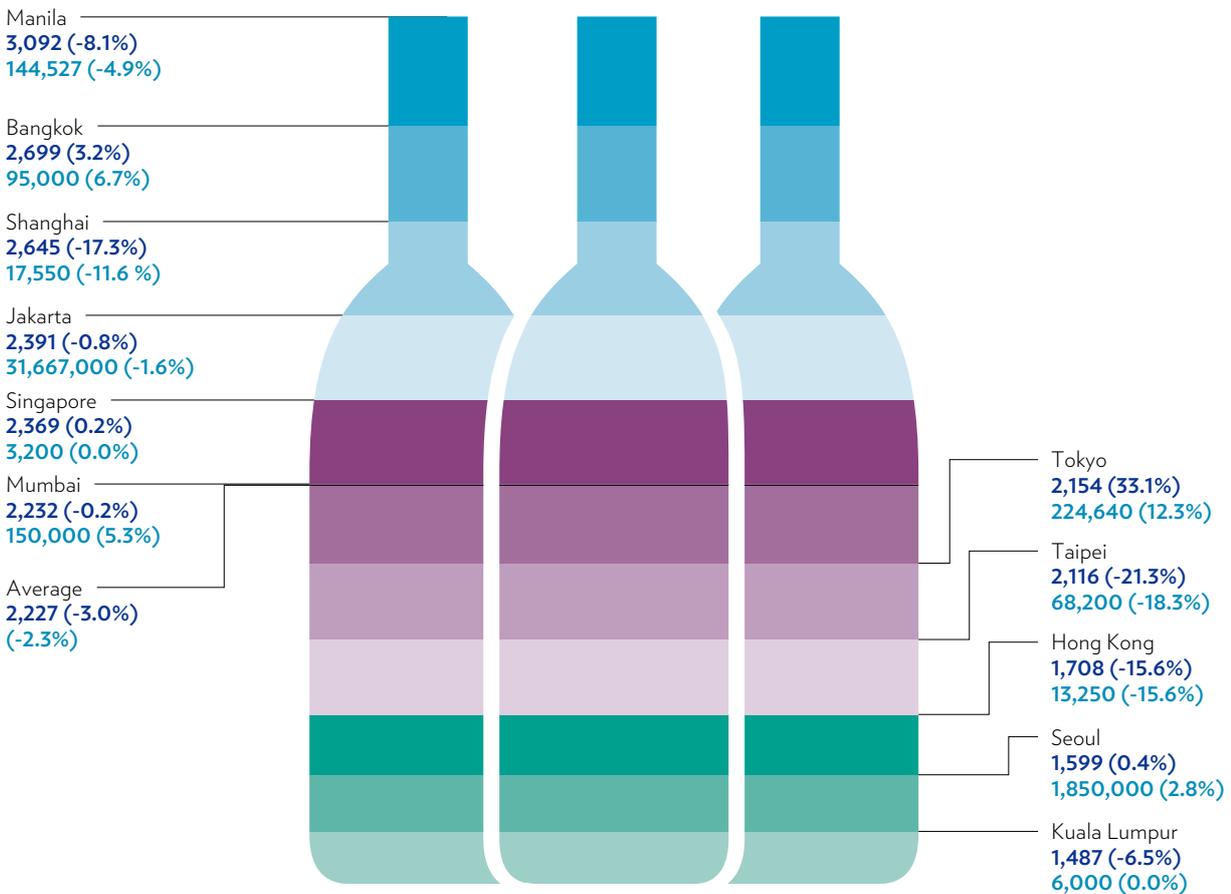
Source: CSG Intage, Julius Baer

Wine

On average in local currency terms, the price for a 750ml of our bottle of Chateau Lafite Rothschild 2000 fell by 2.3% (-3.0% in US dollar terms) this year. We found the largest price declines in Taipei (-18.3%), Hong Kong (-15.6%) and Shanghai (-11.6%) where the impact of austerity measures continue to have a lingering effect. The most expensive city to purchase a bottle of our Hero wine remains Manila where it is almost twice as expensive as the same bottle from Kuala Lumpur (where it is the cheapest).

The price of the wine item in our index has consistently come down in recent years, but this is a normalisation in price, which previously was arguably elevated. A number of reasons contribute to the decline including a shift in buying patterns (Burgundy on the rise), counterfeit industry in China and political changes discouraging lavish gift-giving in China. We should still treat Lafite as the ‘king of first growth’. It is also worth mentioning that apart from the Lafite, there are many other highly-rated expensive Bordeaux wines that have fallen to ‘bargain’ level prices, according to wine experts at Christie’s in Hong Kong.

Chart 12: Wine



■ 2016 cost (USD) / 2016 vs 2015 cost change (%) ■ 2016 cost (Local currency) / 2016 vs 2015 cost change (%)

Source: CSG Intage, Julius Baer

Jewellery

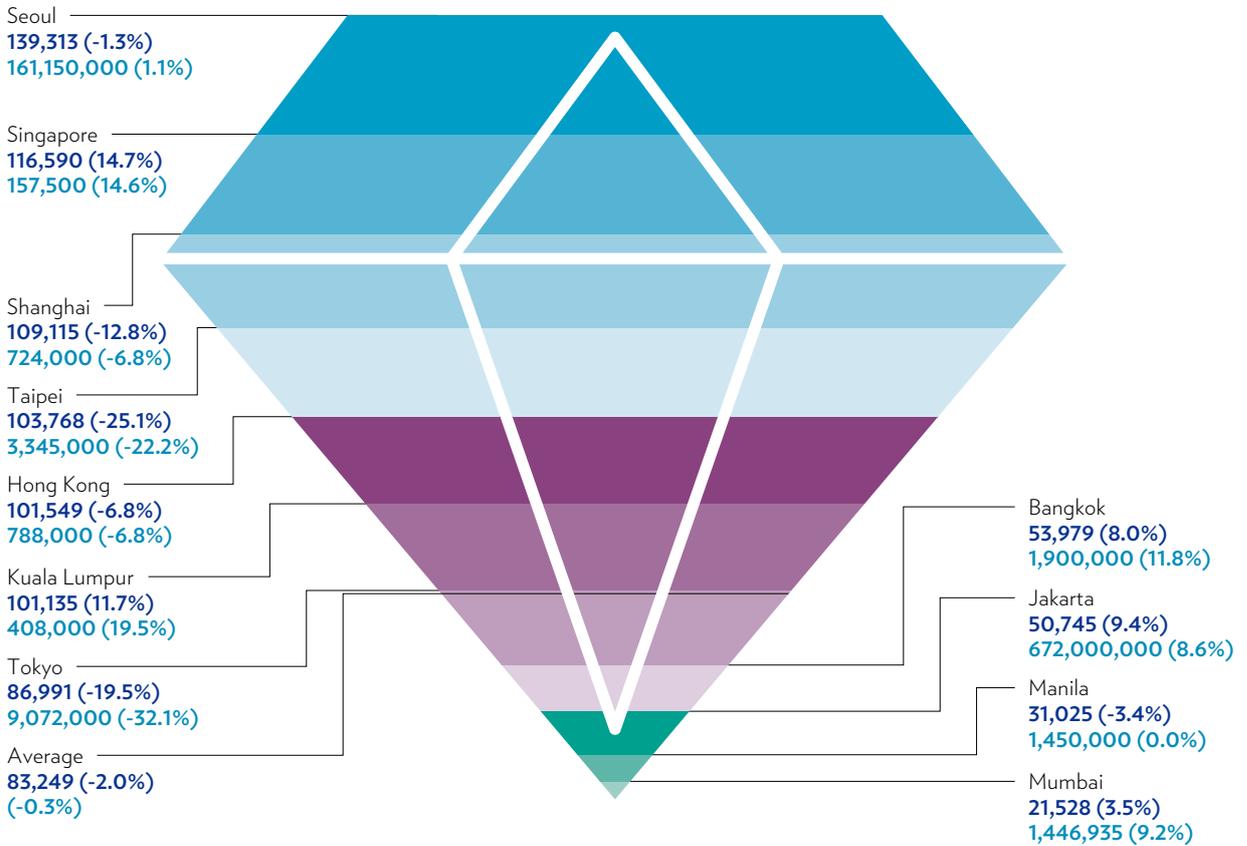
Our index showed a flat price trend for jewellery this year (-0.3% in local currency, -2.0% in US dollar terms). Yet, jewellery is perhaps the hardest item in the index to standardise and build a clear picture of pricing and demand/supply trends. In the index, the only real 'standard' item that we try to look for across the markets is the Tiffany cut single stone. Even then, we might find variations from y/y depending on the colour, clarity and size of the stone that is available.

The main trend in APAC ex Japan for high end jewellery is that consumers are gradually shifting away from 'local' producers towards the branded ones, but the former still makes up about 80% of sales, according to industry experts.

Consumers in Asia tend to focus more on the individual stones and their cost, and worry less about setting, design and craftsmanship of the overall piece. Some brands, like Tiffany, are trying out targeted, mono-themed strategies like trying to raise awareness of single items, such as yellow diamonds. There is a perception now, especially in China, that diamonds are the only stone that can have an investment value, yellow diamonds in particular.

The prevailing view in the industry is that no other store has this cache at the moment. So this is a unique strategy that may be copied in some form by other firms in the future. Overall, it is not expected that local jewellers will match their craftsmanship or design capabilities, well into the medium term.

Chart 13: Jewellery



■ 2016 cost (USD) / 2016 vs 2015 cost change (%) ■ 2016 cost (Local currency) / 2016 vs 2015 cost change (%)

Source: CSG Intage, Julius Baer

Watch

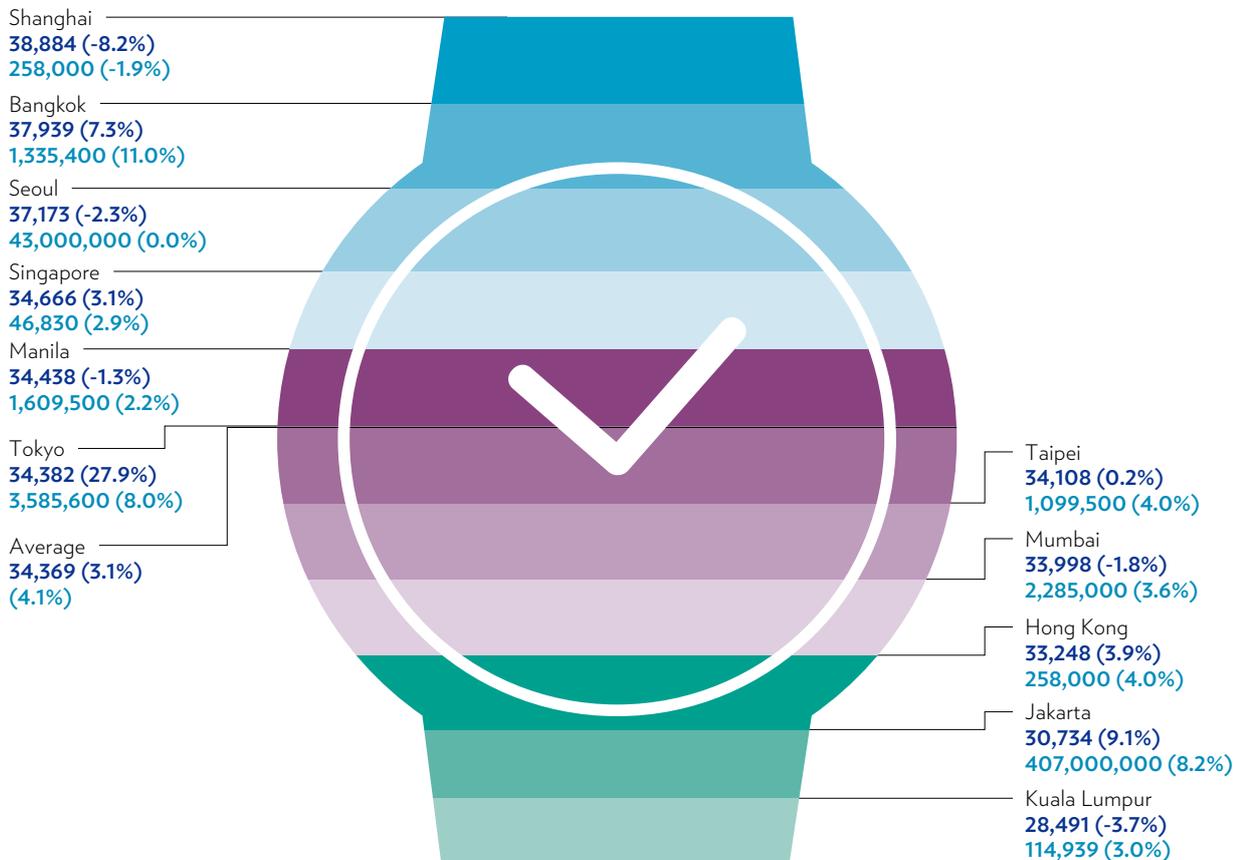
The watch item in our index this year is the Rolex Oyster Perpetual Day-Date 40 in yellow gold which replaces the 41mm Day-Date II. Individually, the changes in the Day-Date 40 are all small, but taken as a whole they represent a significant upgrade to Rolex's flagship model. The new flagship model features a new case, dials and next-generation movement.

We found positive price trends for our watch item across 9 of the 11 cities (except for Shanghai (-1.9%) and Seoul (0.0%)) helped by a model upgrade and

a bullish vintage Rolex market. This is reflective of the fact that the Day-Date is considered to be very fashionable currently especially with younger collectors. On average, our watch item saw prices rising by 4.1% in local currency terms (+3.1% in US dollar terms) making it one of the outperformers in the index.

We find Kuala Lumpur to be the least expensive city to purchase our watch (USD 28,491) while Shanghai remains the most pricey (USD 38,884).

Chart 14: Watch



■ 2016 cost (USD) / 2016 vs 2015 cost change (%) ■ 2016 cost (Local currency) / 2016 vs 2015 cost change (%)

Source: CSG Intage, Julius Baer

Car

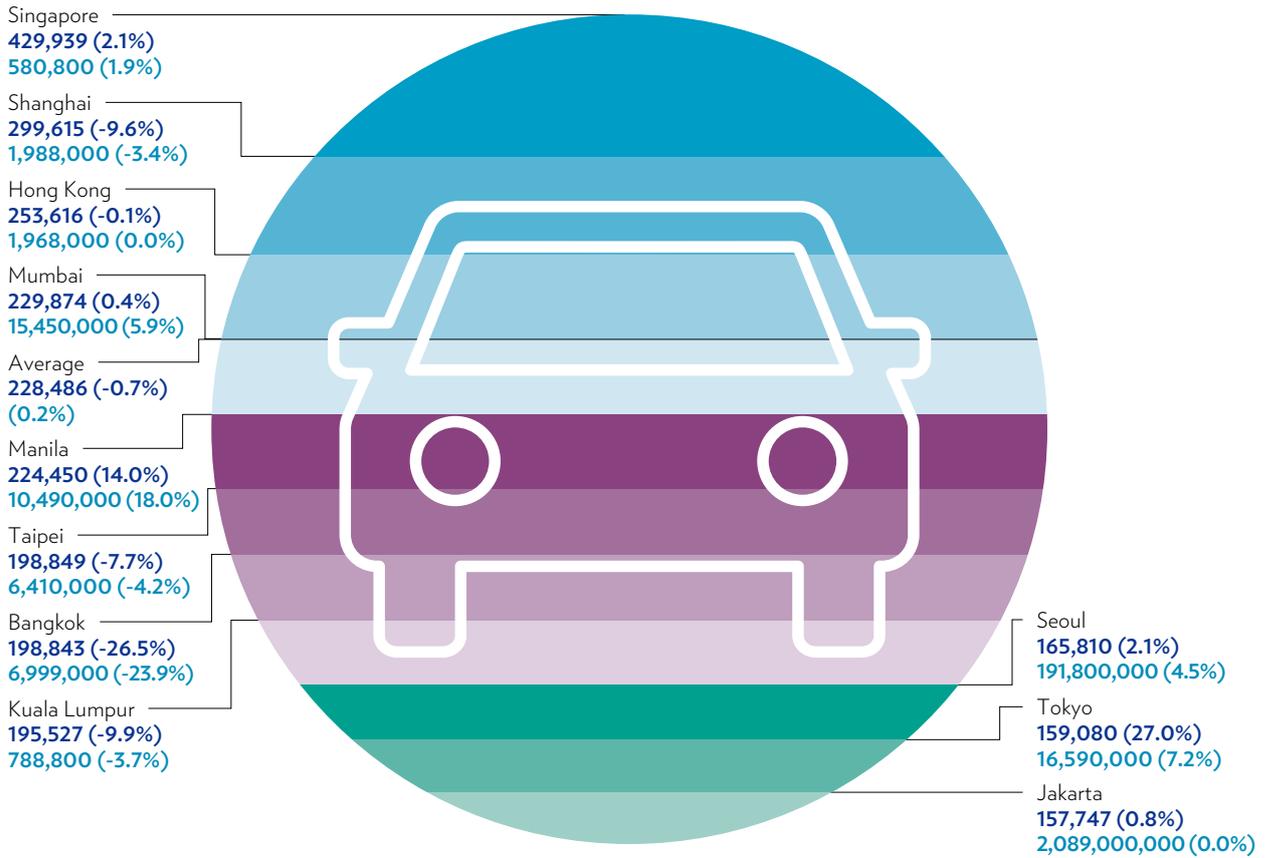
We have replaced the luxury sedan in our index this year with the redesigned BMW 7 Series (previously Mercedes-Benz S-Class) which is also the flagship model of the brand for BMW. The new BMW 7 series features several innovations including the industry’s first Display Key, Gesture Control, Remote Control Parking, a passenger compartment constructed with light-weight carbon fibre and BMW Panorama glass roof Sky Lounge.

On average, our car item saw stable pricing trends over the past year up 0.2% in local currency terms (-0.7% in USD terms). At the extremes, we saw a

large price increase in Manila of 18.0% helped by a model upgrade (BMW 750Li from BMW 740Li, which is still available), while Bangkok saw a price fall of -23.9% as a price adjustment was carried out to stay competitive as Mercedes Benz dropped prices across its model range.

Singapore clinches the title of most expensive city to purchase a brand new BMW 7 Series sedan (approximately USD 430,000) due to import duties and regulatory taxes whereas Shanghai is a distant second at about USD 300,000. Jakarta is the cheapest overall to procure our car item (approximately USD 158,000).

Chart 15: Car



■ 2016 cost (USD) / 2016 vs 2015 cost change (%) ■ 2016 cost (Local currency) / 2016 vs 2015 cost change (%)

All prices for BMW 750Li except:
 2015: BMW 740Li for Bangkok, Jakarta, Kuala Lumpur and Manila
 2016: BMW 740Li for Bangkok, Jakarta and Kuala Lumpur
Source: CSG Intage, Julius Baer

Chart 16: 2016 Julius Baer Lifestyle Index city ranking by items, in USD

Item (USD)	Hong Kong	Singapore	Shanghai	Mumbai	Taipei	Jakarta	Manila	Seoul	Kuala Lumpur	Bangkok	Tokyo
 Business class flights	3	5	4	9	1	6	7	2	11	10	8
 Residential property	1	3	2	7	4	9	11	6	8	10	5
 Wedding banquet	3	5	2	6	8	9	7	4	10	11	1
 Hotel Suite	2	4	5	11	3	8	7	9	10	6	1
 Tooth implant	2	5	3	11	4	9	10	7	8	6	1
 Hospital	3	4	1	6	10	11	9	7	8	2	5
 Golf club membership	2	5	4	8	6	11	1	7	9	10	3
 Lawyer	4	1	8	6	9	7	5	3	2	10	11
 Watch	9	4	1	8	7	10	5	3	11	2	6
 Ladies' handbag	9	6	2	11	7	1	10	5	8	4	3
 Wine	9	5	3	6	8	4	1	10	11	2	7
 Jewellery	5	2	3	11	4	9	10	1	6	8	7
 Men's suit	3	4	2	11	7	5	10	1	8	6	9
 Facial aesthetics (Botox)	2	9	1	10	4	8	11	6	5	3	7
 Piano	6	7	3	5	4	10	2	8	11	1	9
 Car	3	1	2	4	6	11	5	9	8	7	10
 Cigar	3	6	1	11	2	9	5	8	7	4	10
 Ladies' shoes	5	3	2	6	10	4	7	8	11	9	1
 Skincare	10	3	1	11	8	7	6	9	2	4	5
Average	4.10	4.00	2.48	7.62	5.43	7.14	6.24	5.48	7.43	5.57	5.29

Source: CSG Intage, Julius Baer

Chart 17: Change in ranking 2015/2016



(-) Change from 2015 ranking

Source: CSG Intage, Julius Baer

Most expensive city: Shanghai

For the second year since we began to compare the cost of luxury living in Asian cities, Shanghai is ranked as the most expensive city scoring first place for 5 items (hospital stay, watch, botox, cigars and high-end skin cream) and second for another 6 (property, wedding banquet, ladies' handbag, men's suit, car and ladies' shoes). As seasoned shoppers will know, factors such as exchange rates, taxes and duties can cause a luxury item to cost significantly more on the mainland than overseas.

Least expensive city: Mumbai

For the second year since we began to compare the cost of luxury living in Asian cities, Mumbai is ranked

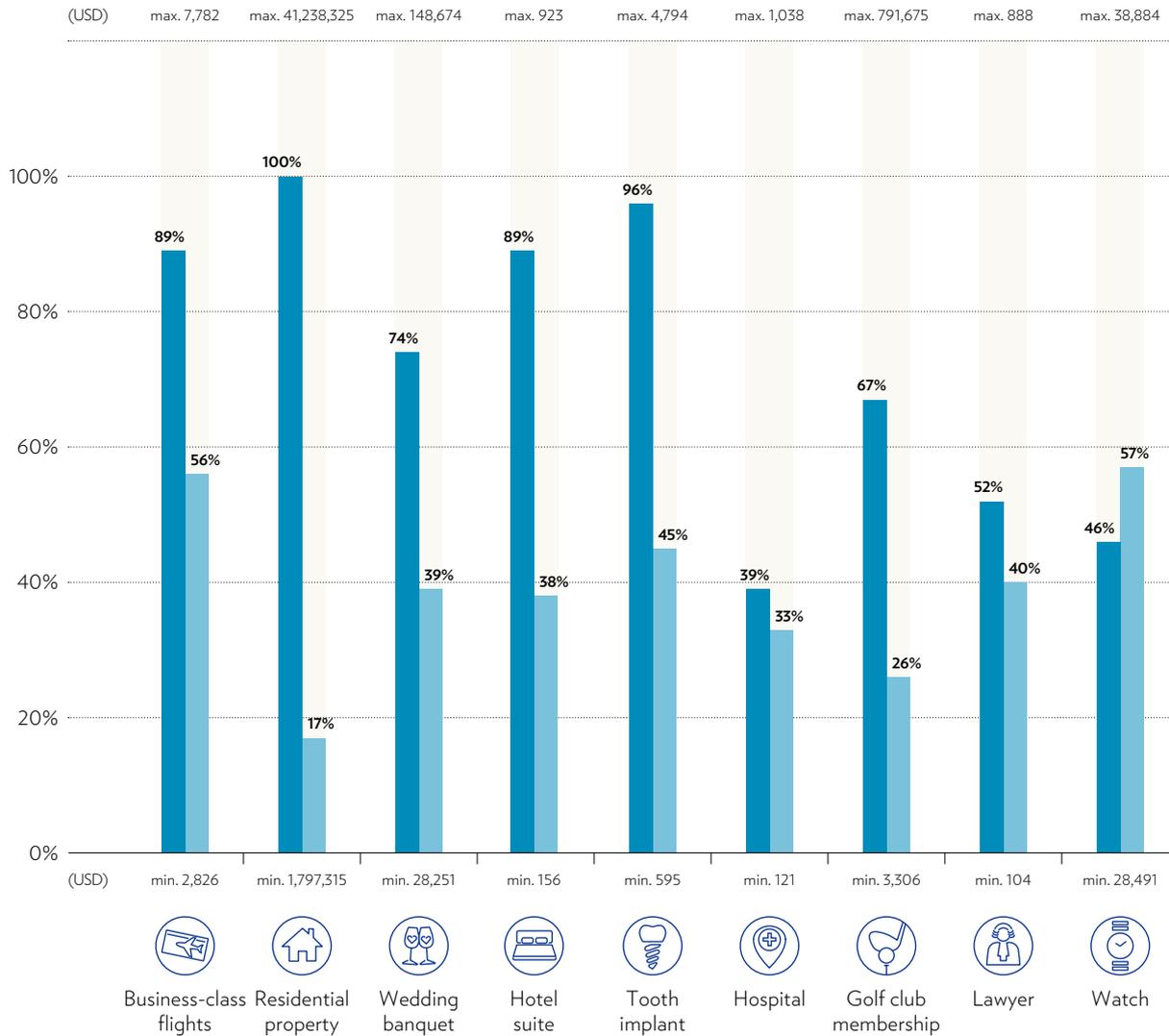
as the least expensive city scoring 11th for 7 items (hotel suite, tooth implant, ladies' handbag, jewellery, men's suit, cigars and skincare) and second cheapest for botox.

Upgrades and downgrades

Singapore has overtaken from Hong Kong as the second most expensive city in Asia as the latter remains out of favour with Chinese tourists. Another notable upgrade is Tokyo (up 3 notches from 7th to 4th spot) due to favourable FX rates displacing Bangkok which is downgraded from 5th to 7th. Kuala Lumpur falls 2 notches from 8th to 10th position on adverse currency movement.



Chart 18: Julius Baer Lifestyle Index – Hong Kong



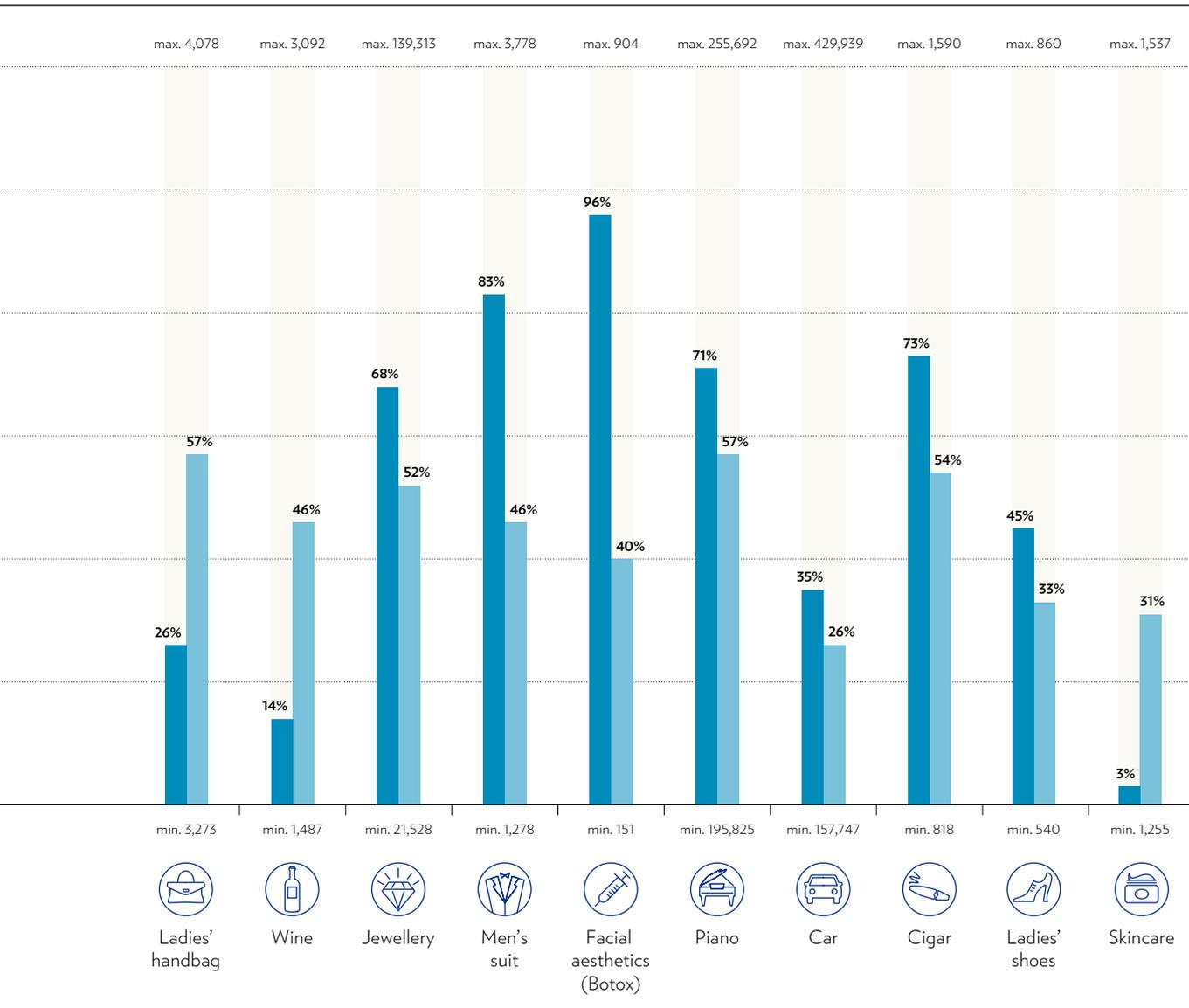
■ Hong Kong ■ Average

Source: CSG Intage, Julius Baer

City comparisons – Hong Kong

Our basket of goods and services fell by 0.56% y/y in Hong Kong as large price increases for golf club memberships (+36.5%), cigars (+12.5%) and pianos (+8.2%) were offset by declines in wine (-15.6%), residential property (-8.7%) and jewellery (-6.8%). This is better than the average price decline of -1.68% across the cities.

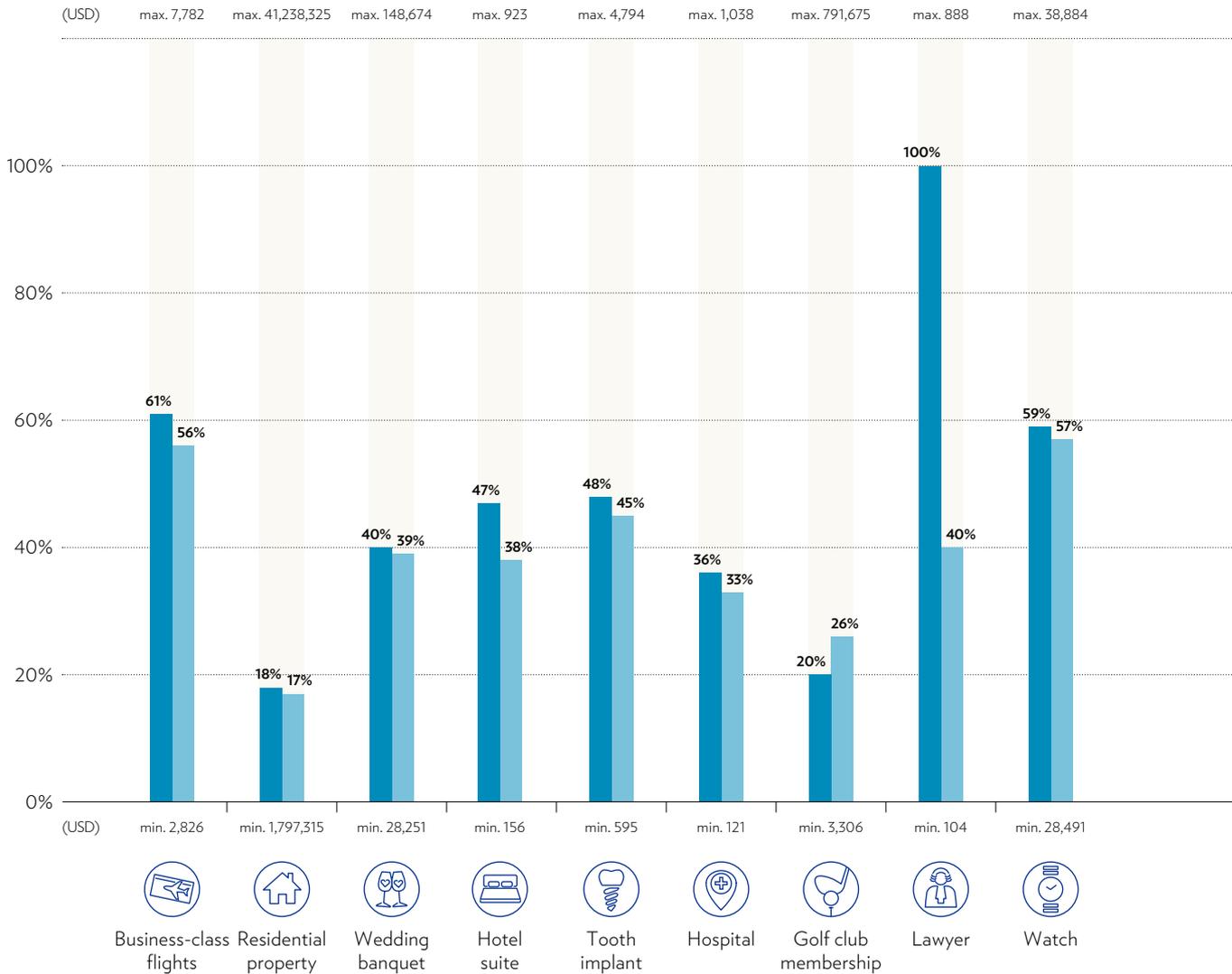
Hong Kong retains its status as the most expensive place in Asia to live in with high-end property still about five times as costly as the average for the region. Yet for certain items value is emerging after prices have fallen in recent years. A bottle of our top-end wine is attractively priced at a third of what it costs on average in the region, our ladies’ handbag retails at a fraction of that in other Asian cities and our newest addition, high-end skin cream, is second cheapest in the region after Mumbai.



We remain sanguine on the Hong Kong economy as we expect the bellwether property sector to remain resilient. Hong Kong real estate is highly sensitive to interest rates, which given Hong Kong’s currency peg, follow those of the United States where rate hikes have been pushed back. There is also optimism in the commercial sector, where the transition from luxury shops to mass market shops is close to completion, and landlords can start from a new base.

Our view on the Hong Kong dollar (which is pegged to the US dollar) is bullish as US economic data is improving despite an already strong currency, justifying more currency strength.

Chart 19: Julius Baer Lifestyle Index – Singapore



■ Singapore ■ Average

Source: CSG Intage, Julius Baer

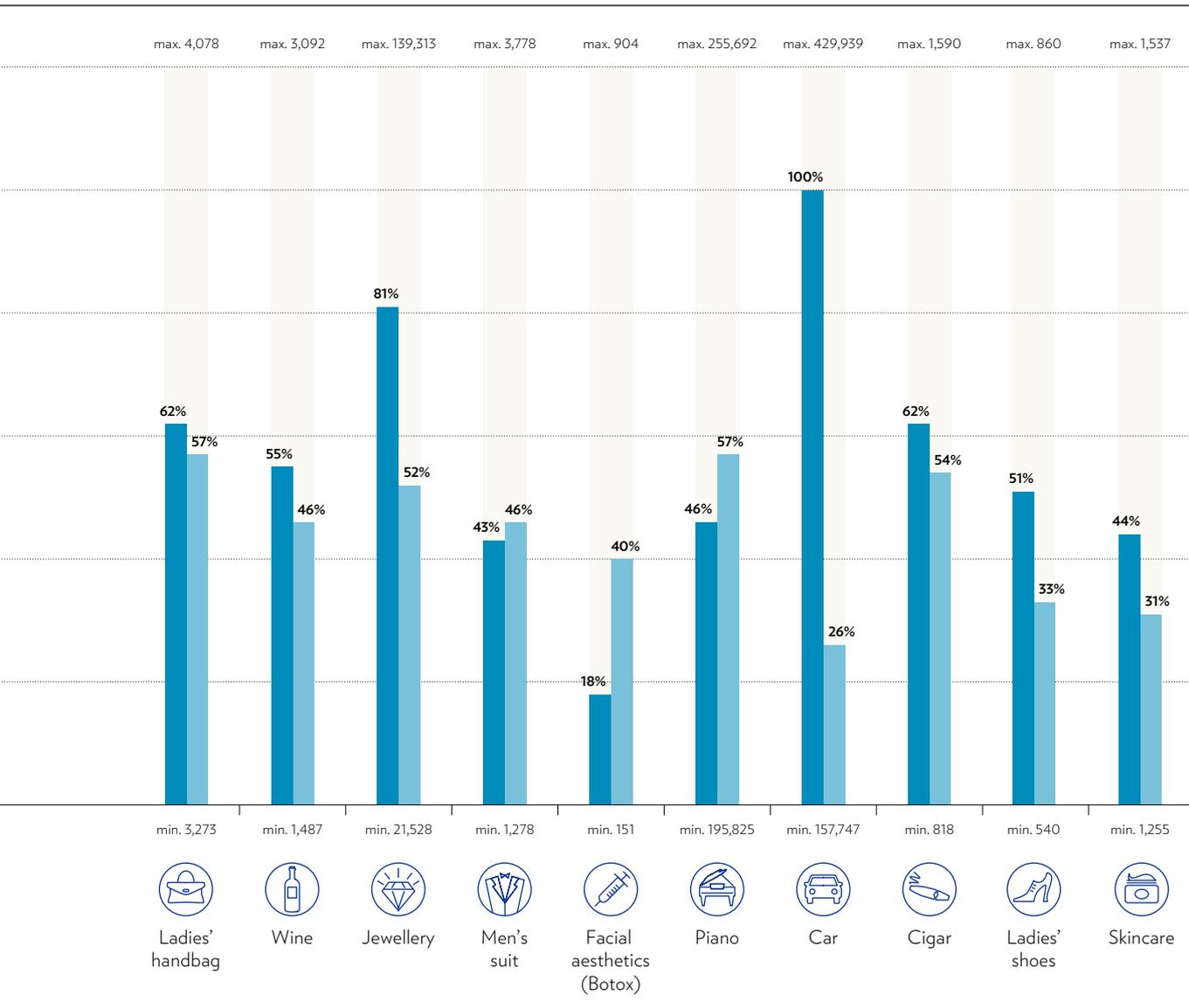
City comparisons – Singapore

Our basket of goods and services fell by 6.6% y/y in Singapore dragged by a significant decline in high-end property prices (-26.3%). Large price increases for items such as jewellery (+14.7%) and cigars (+20.0%) were unable to make up for the difference. The price performance for our luxury index in Singapore was worse than the -1.68% across the cities.

Singapore has gained ground on Hong Kong this year and it is now the 2nd most expensive city in Asia according to our index. Cars, legal fees and jewellery are considerably more expensive in the lion-city but

these can be explained by idiosyncratic factors such as local taxes and controlled supply for cars.

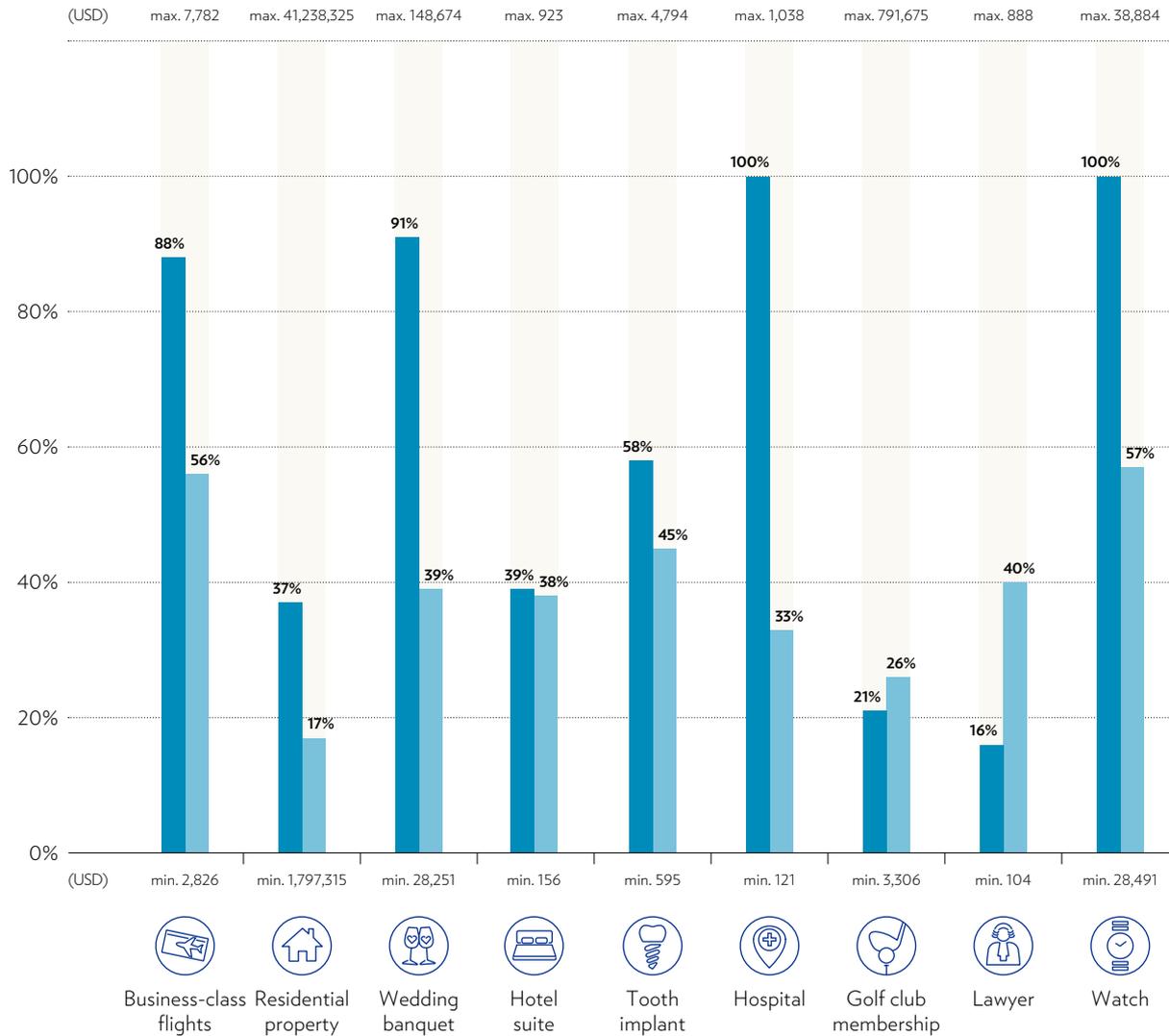
Botox and golf club memberships could be considered as ‘cheap’ relative to the region. Golf club membership prices (-4.2%) in Singapore have fallen after buyers stopped trading in memberships in the wake of government announcements that it was taking back the land from three clubs and that two others would not have their leases renewed. Over the medium term however, we would expect membership prices to rise again as players from clubs due to close buy new memberships to continue playing the sport.



Our view on the Singapore economy is relatively cautious as despite some recovery in the industrial sector, low global external demand will continue to weigh on the highly export-dependent economy, with a slowing China having a particular weight. In addition, the banking sector could be affected by a slowdown in Europe from 'Brexit' as it has a greater direct exposure to the UK than ASEAN counterparts.

We have a neutral view on the Singapore dollar as we expect the currency to trend down in connection with a slowing China and a possible downward re-centering of the MAS's target band due to continued low-inflation.

Chart 20: Julius Baer Lifestyle Index – Shanghai



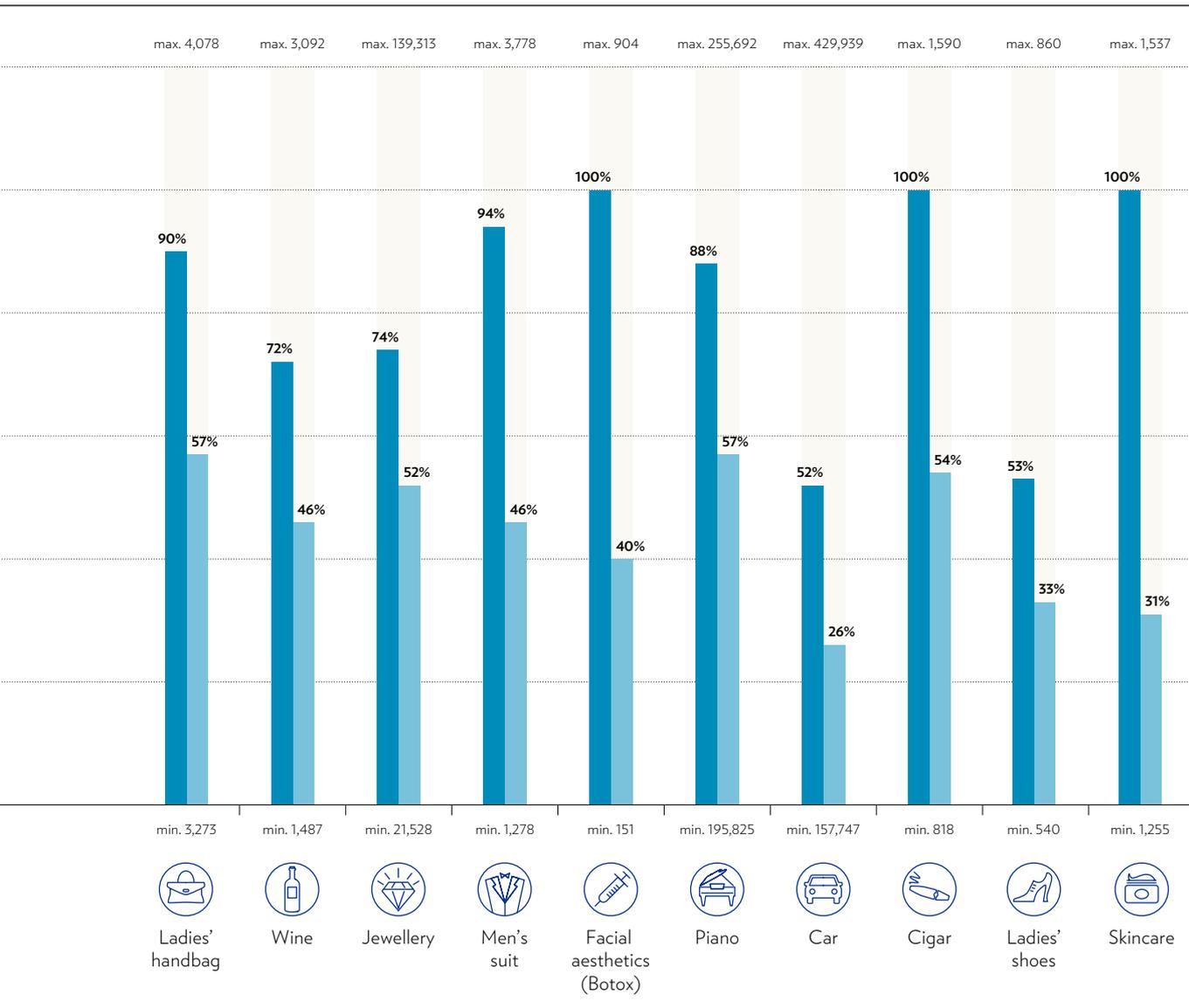
■ Shanghai ■ Average

Source: CSG Intage, Julius Baer

City comparisons – Shanghai

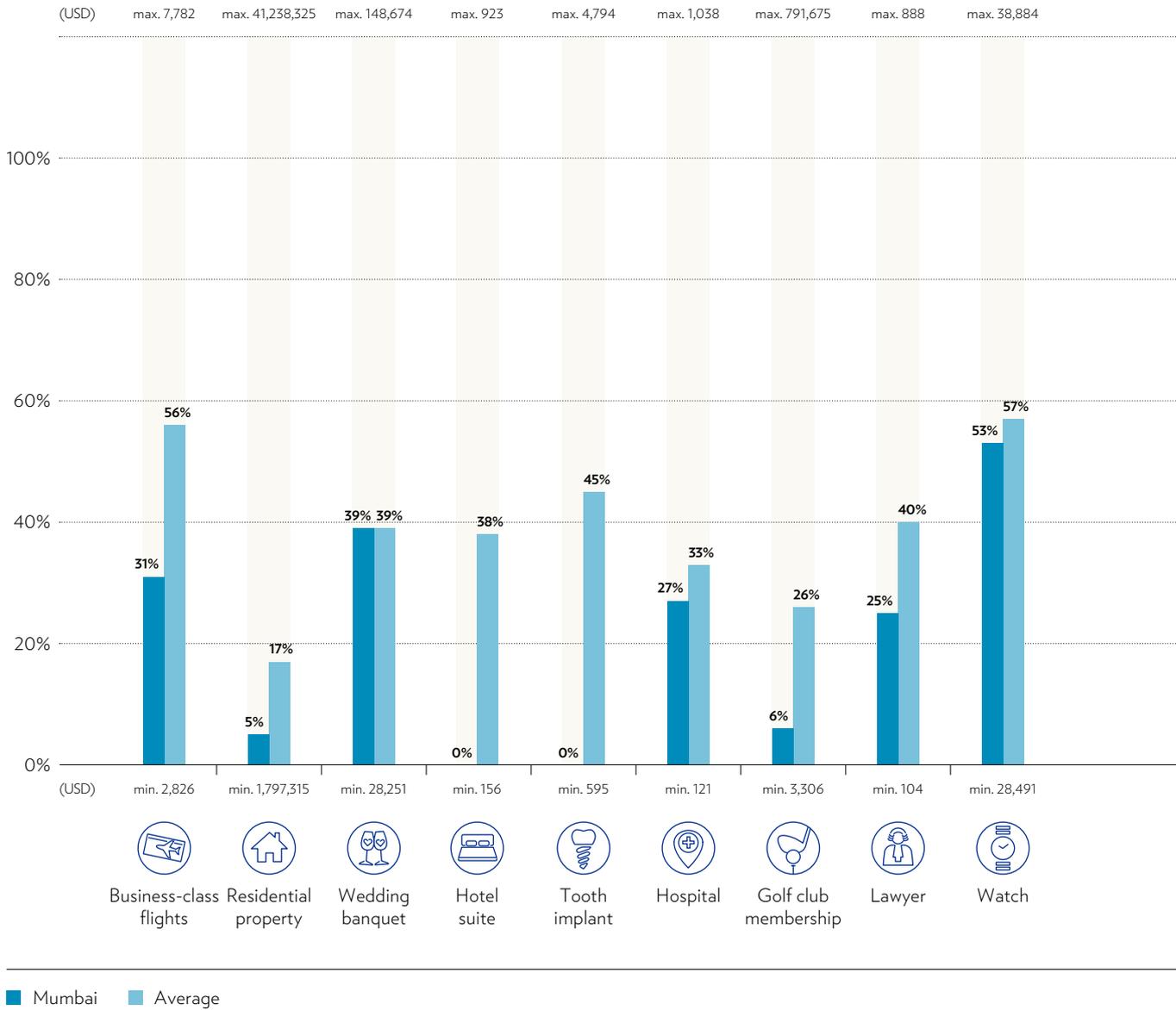
Our basket of goods and services fell by 7.0% y/y in Shanghai affected by a depreciation (-6.5%) of the Chinese yuan against the US dollar. This was more deflationary than the -1.68% we saw across the cities. In addition, most items saw prices falling except for tooth implants (+10%), cigars (+7.5%) and business class flights (+2.5%). The items with outsized declines were botox (-29.8%), ladies’ shoes (-20.0%), wine (-17.3%) and legal fees (-13.9%).

Yet in absolute terms, Shanghai remains the most expensive city in Asia. To put it another way, legal fees and golf club memberships are the only two items which are cheaper in Shanghai than in the region. In many cases, luxury goods and services originating from Shanghai cost two times what they would cost elsewhere in Asia.



In terms of our currency outlook, we are expecting mild depreciation for the Chinese yuan against the US dollar due to cyclical and structural pressures in the Chinese economy. We are overall positive on the Chinese economy. Market worries have calmed after better data in the first half indicated a temporary stabilisation of economic conditions. We expect a controlled slowdown to resume in the second half of 2016.

Chart 21: Julius Baer Lifestyle Index – Mumbai



Source: CSG Intage, Julius Baer

City comparisons – Mumbai

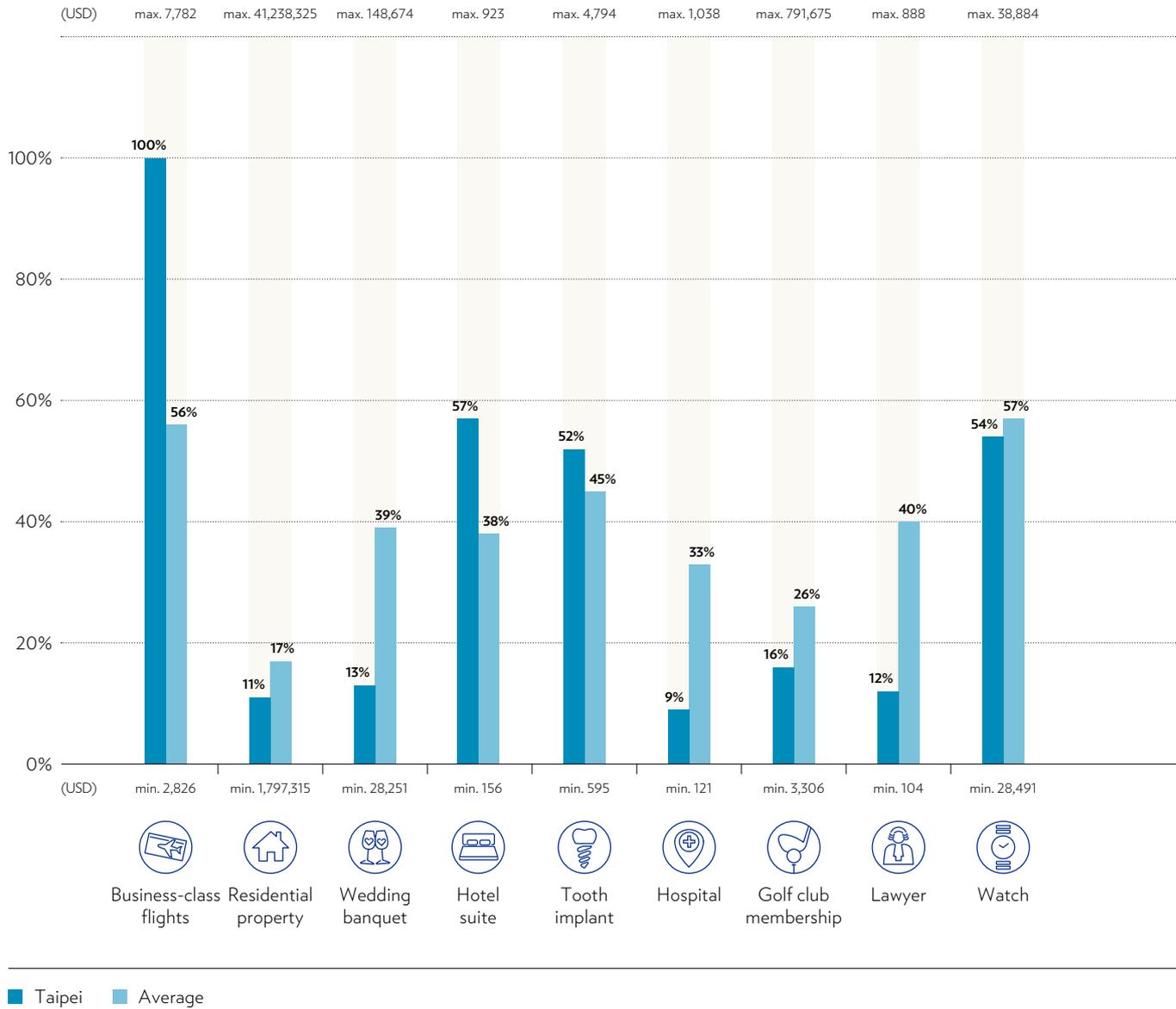
Our basket of goods and services fell by 9.2% y/y in Mumbai affected by a depreciation (-5.2%) of the Indian rupee against the US dollar. Mumbai saw the largest single city price deflation this year as compared to the -1.68% regionally. Several items experienced price falls with the exception of legal fees (+20.3%), golf club memberships (+19.7%) and cigars (+13.3%) which performed well. The items with outsized declines were tooth implants (-39.8%), residential property (-25.9%) and wedding banquets (-21%).

For the second year running, Mumbai qualifies as the least expensive city to purchase our selected high-end goods and services. Mumbai is the cheapest location to acquire 7 of our 21 measured items and in many cases it is the cheapest by a wide margin. We expect moderate growth of luxury and high-end goods and services in India which remains a domestically driven market. Despite a growing number of HNWI's, research has shown that the nation's affluent consumers tend to shy away from ostentatious displays of wealth.



Our outlook for the Indian economy and the currency is moderately bullish – we expect continued outperformance of the rupee against its Asian emerging market peers given its resilience. We expect the rupee to profit from a better macroeconomic backdrop and an improving balance of payments. In addition, we expect a steady flow of reforms to keep more realistic expectations for fundamental change alive.

Chart 22: Julius Baer Lifestyle Index – Taipei

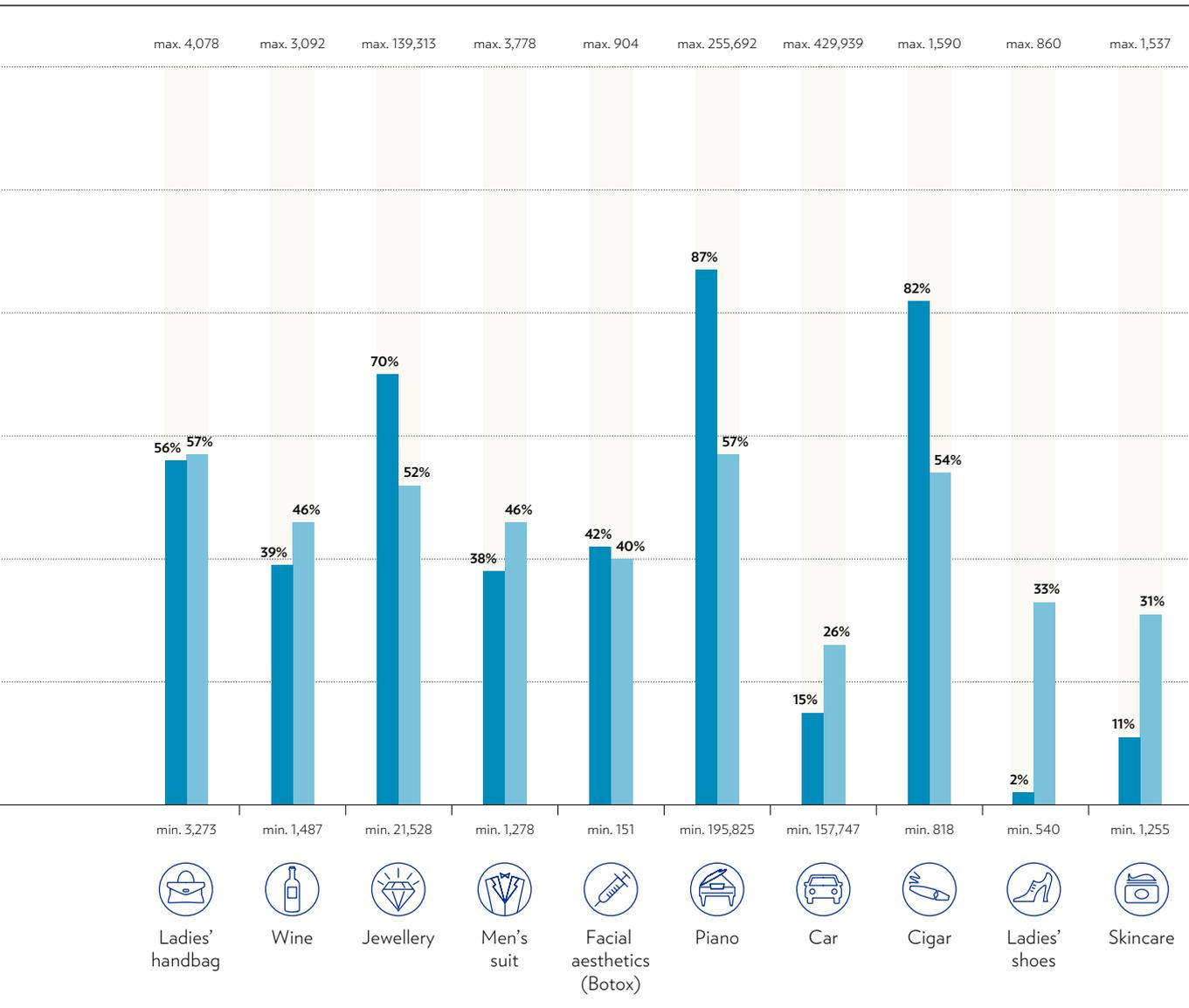


Source: CSG Intage, Julius Baer

City comparisons – Taipei

Our basket of goods and services fell slightly by 0.26% y/y in Taipei in a somewhat mixed picture. Items which showed large price falls include jewellery (-25.1%), wine (-21.3%) and golf club memberships (-9.1%) while ladies’ shoes (+27.8%) and botox (+25.6%) outperformed. Overall, price momentum outperformed the average price movement of -1.68% across the cities.

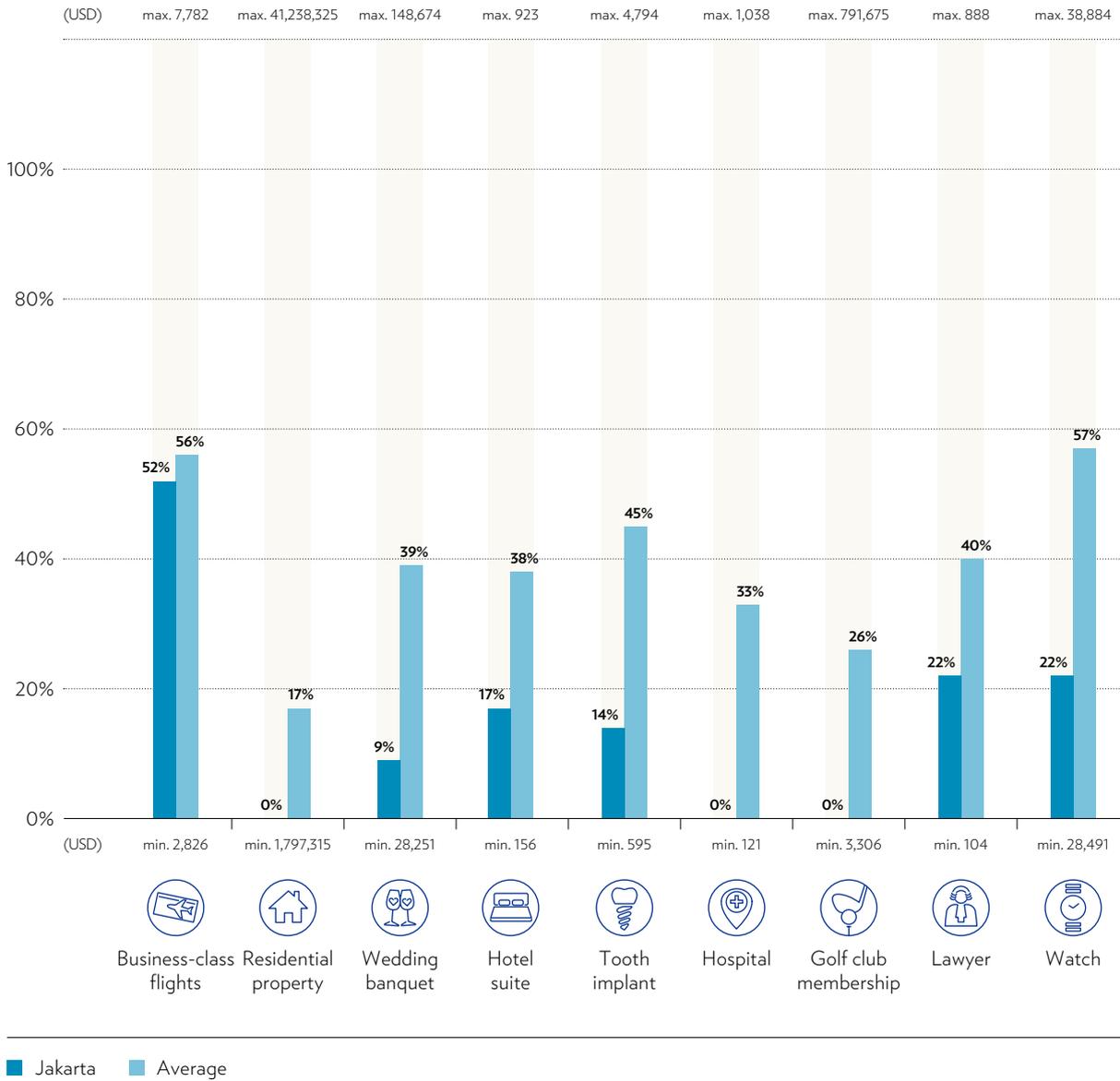
Relative to regional peers, Taipei’s goods and services are not expensive with the city retaining its 6th spot in our index ranking. Historically, tourism marketing has focused largely on local culture, natural sights, street food and cuisine. However, this may change as the government has been taking steps to promote Taiwan as a luxury shopping destination including easing visa restrictions, introducing a more consumer-friendly tax system and opening more upscale department stores in the Taipei 101 area. Given the attractive pricing of the city’s goods and services, we see further upside potential for the city’s ranking.



We have been mildly optimistic on the Taiwanese economy however, we note that this year's growth forecasts have a downward bias as weakness in external demand for the island's products and components is starting to impact recent signs of economic recovery.

Over the medium term, the newly elected government plans to focus on industrial upgrading, income distribution and reducing trade reliance on China. It remains to be seen if these reform measures can be executed given an anaemic macro-environment, limited fiscal firepower and regional competition.

Chart 23: Julius Baer Lifestyle Index – Jakarta

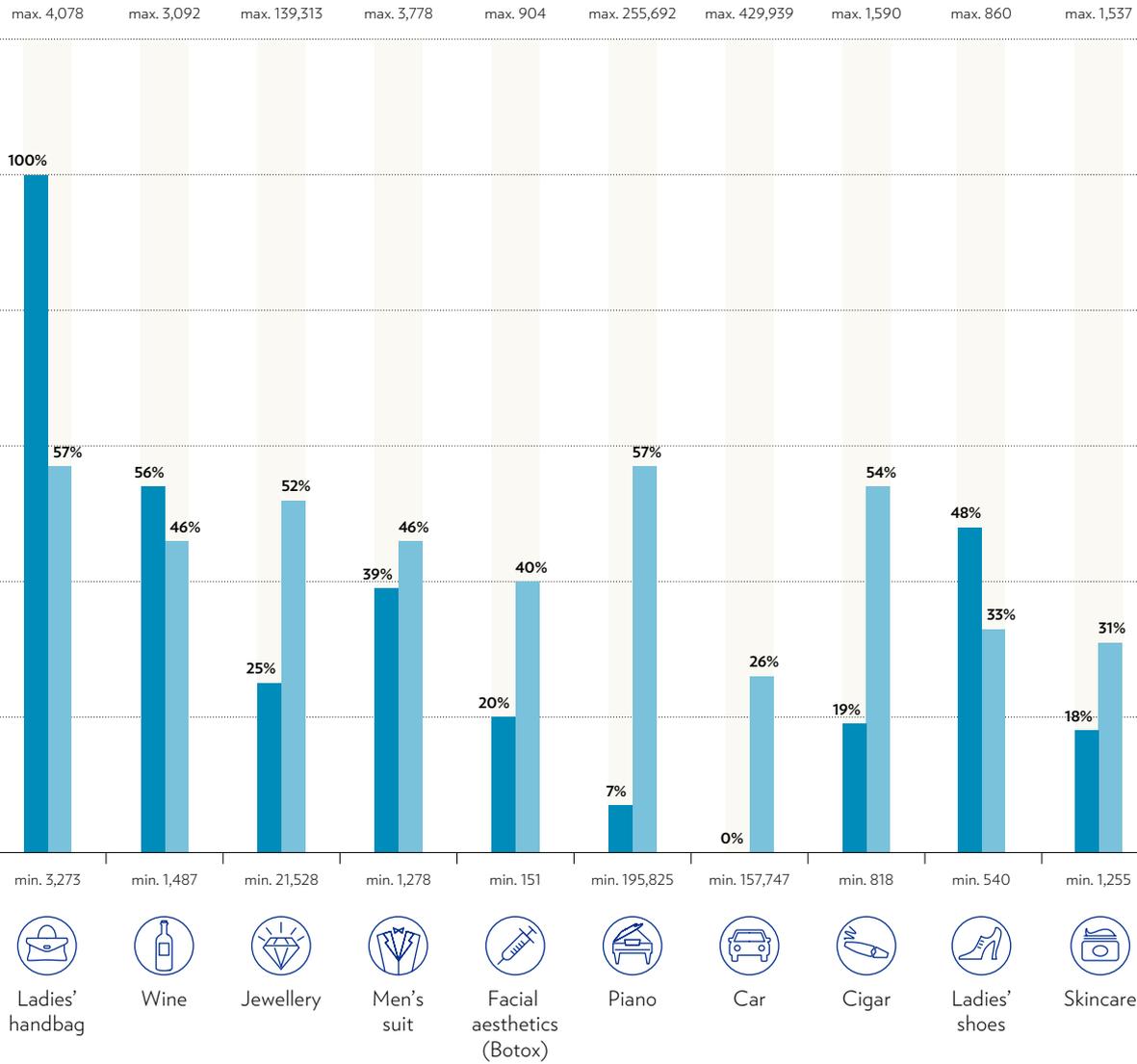


Source: CSG Intage, Julius Baer

City comparisons – Jakarta

Our basket of goods and services fell by 0.58% y/y in Jakarta as healthy price increases in golf club memberships (+26.0%), business class flights (+18.0%) and legal fees (+11.9%) were more than offset by a decline in tooth implants (-14.6%) and residential property (-10.7%) which carries a higher weight. Overall, the fall in prices in Jakarta were mild as compared to the region (-1.68%).

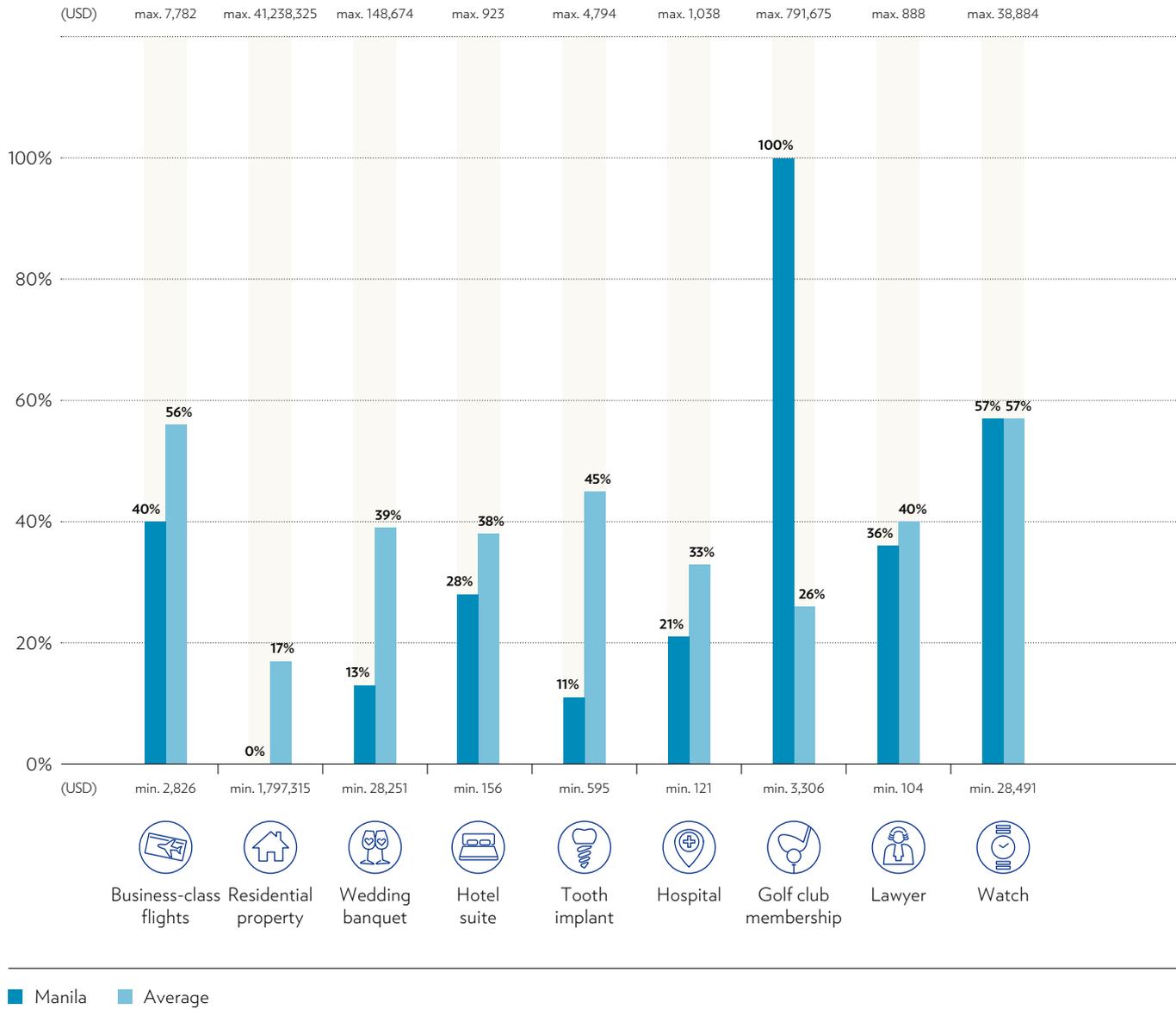
Notwithstanding, Jakarta still ranks third cheapest in our index within the region (up one level from last year). It is cheapest for hospital stays and golf club memberships and second cheapest for cars and watches. The only item where it claims top spot is for ladies’ handbags.



An important development in Indonesia in 2015 was the exemption of luxury tax from certain items which are found in our lifestyle index such as musical instruments and branded goods in order to boost household consumption and reduce overseas spending. So far this has not had a large impact on the price data of affected items in our index, suggesting that retailers had not fully passed through lower taxes on to consumers.

We are neutral on the Indonesian rupiah with a mildly depreciating outlook. While the pass-through of important reforms has lifted investor confidence somewhat, still rather weak fundamentals, such as a considerable current-account deficit, will continue to weigh on the currency.

Chart 24: Julius Baer Lifestyle Index – Manila

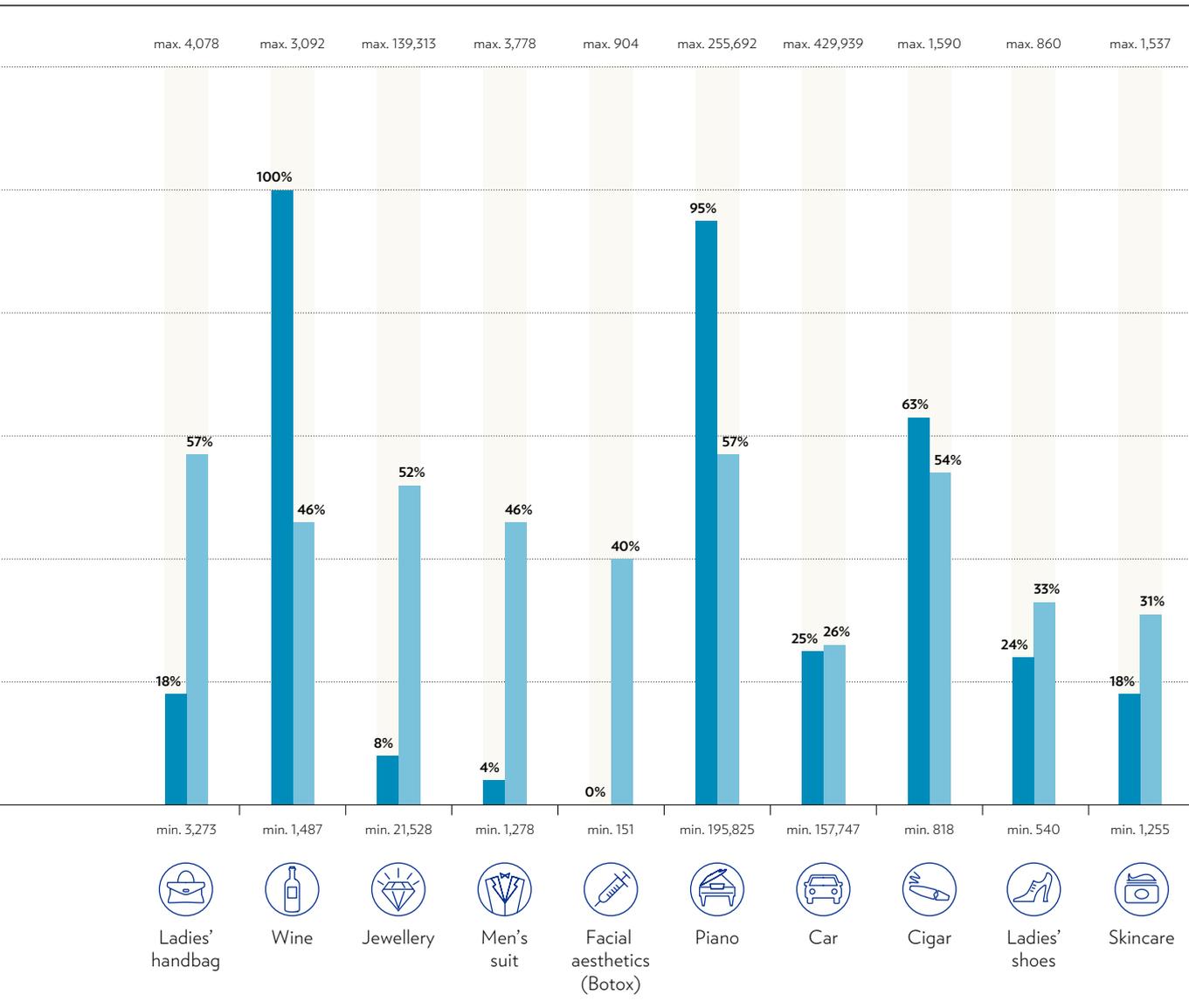


Source: CSG Intage, Julius Baer

City comparisons – Manila

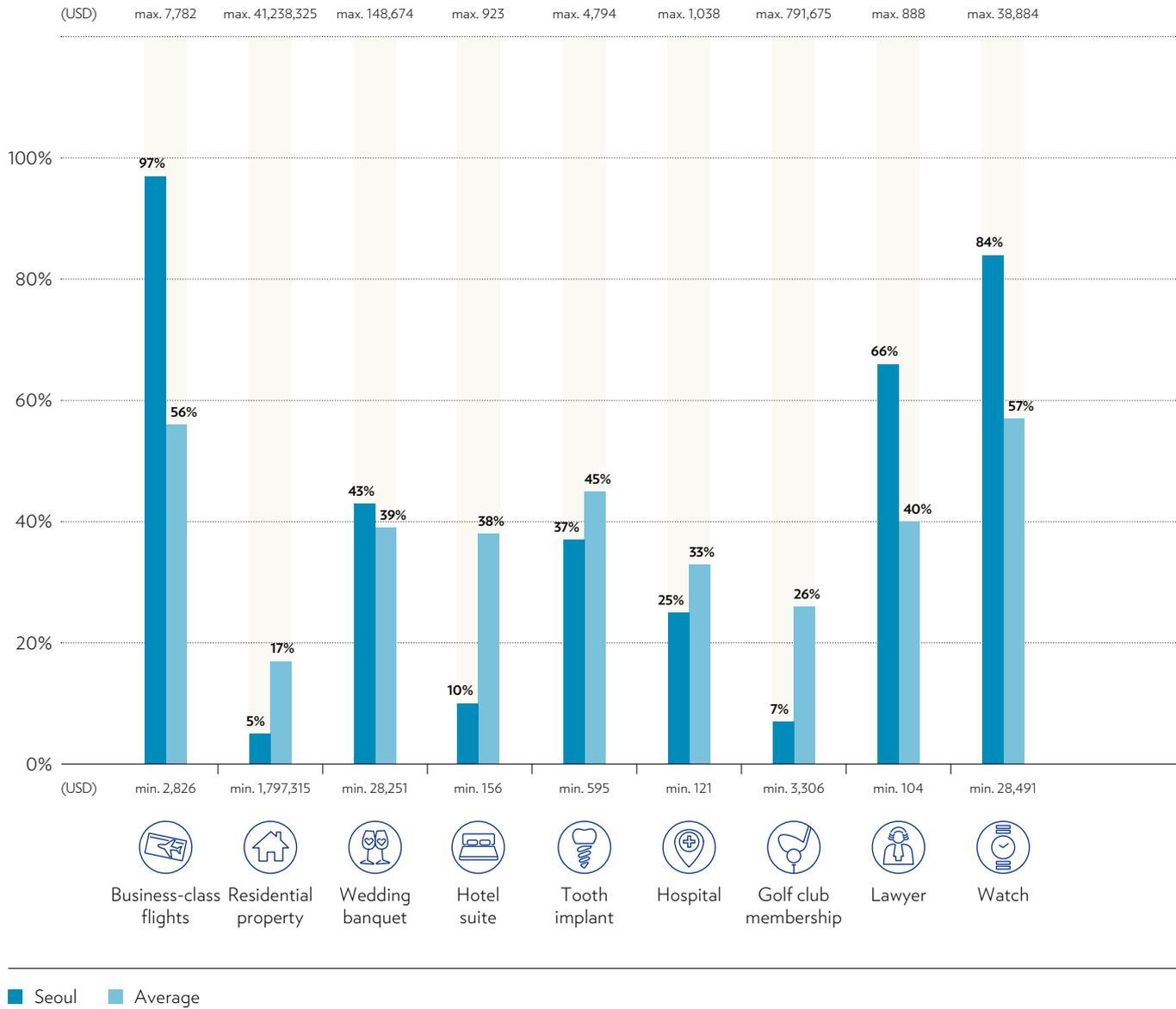
Our basket of goods and services fell by 0.62% y/y in Manila tempered by a weaker peso (-3.3%) and price declines in all but 3 items in the index, namely cars (+14.0%), men’s suits (+10.5%), golf club memberships (+8.3%) and cigars (+1.4%). This was a better performance than the region’s -1.68%.

In relative terms, Manila is the 4th cheapest city to obtain our basket of goods and services (up from 3rd cheapest previously). It remains the least expensive city to purchase a luxury high-end apartment, a segment which has seen growing interest from expatriates who are converting from lessees to unit owners, as well as overseas based Filipinos. As with years past, Manila remains one of the least expensive places to purchase branded ladies’ handbags and Armani suits, or to seek cosmetic medical procedures like botox and tooth implants.



Our view on the Philippines economy is neutral, as much depends on the new government's ability to execute on announced policies. Key drivers are plans to increase deficit spending from 0.9% of GDP in 2015 to 3.0% of GDP, and infrastructure spending from an average of 2.2% in the past five years to around 5.0% in the next six years.

Chart 25: Julius Baer Lifestyle Index – Seoul

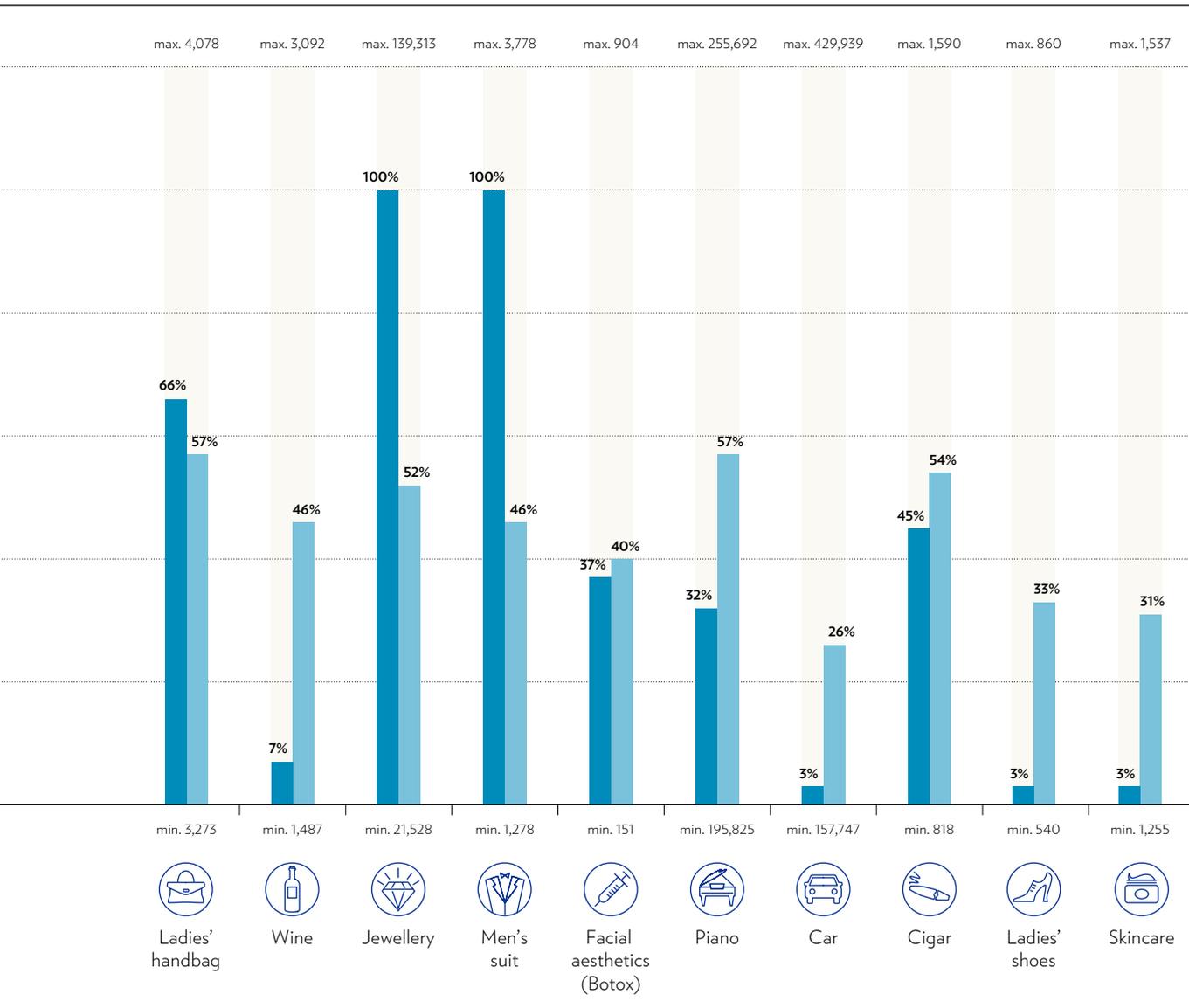


Source: CSG Intage, Julius Baer

City comparisons – Seoul

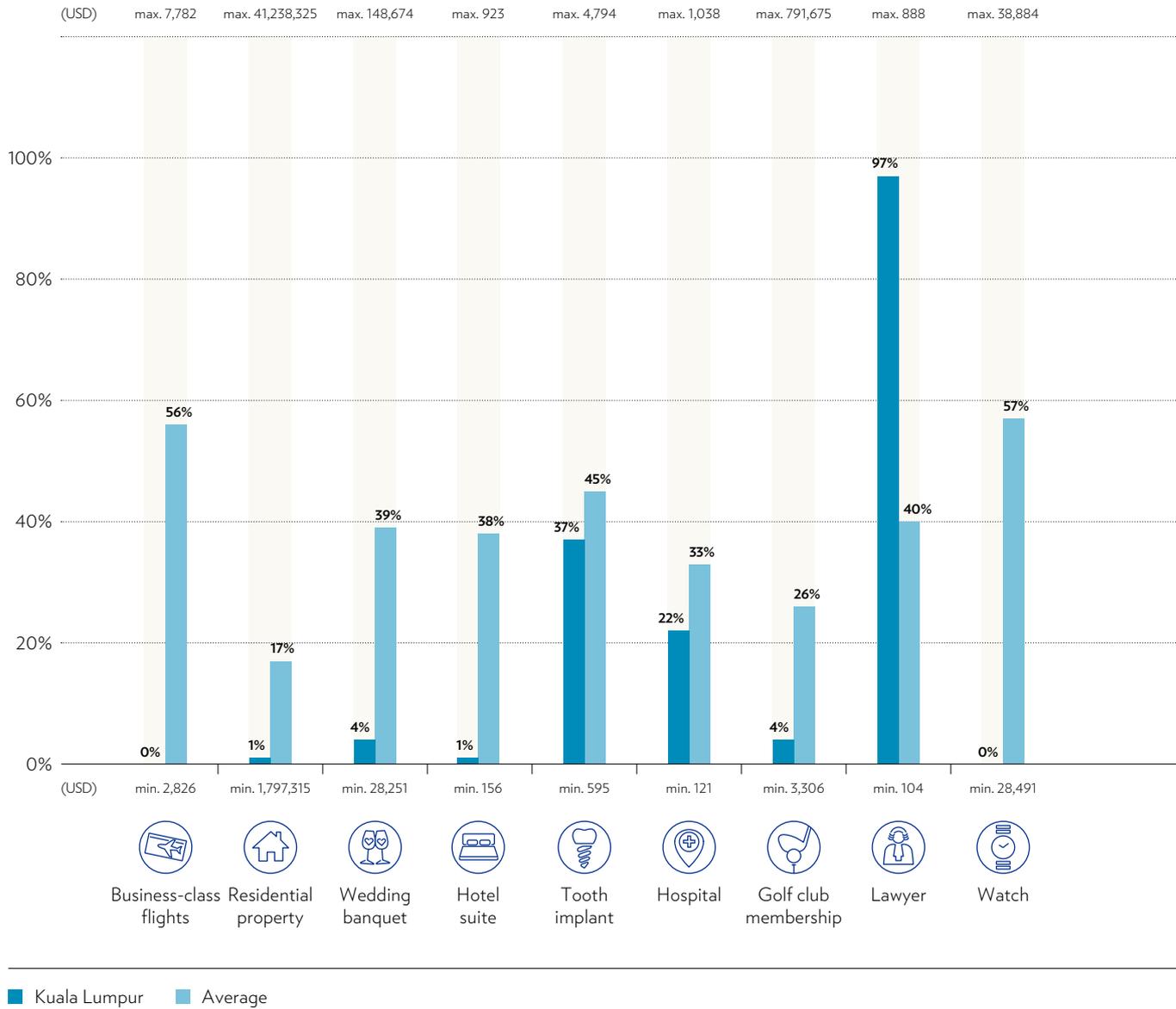
Our basket of goods and services fell by 4.52% y/y in Seoul affected by local currency weakness (-2.3%) and large corrections in the prices of certain items such as tooth implants (-33.7%), botox treatments (-18.6%) and golf club memberships (-12.3%). This was a more severe fall than the average for the region (-1.68%).

Seoul has fallen to the 5th most expensive from 4th a year ago based on our methodology. It is the most expensive to purchase an Armani suit, a diamond ring or simply as a point of disembarkation for long-haul business class flights to New York and London. Yet in certain areas such as cosmetic/elective procedures in plastic surgery and dentistry, prices have declined due to heightened competition.



We are mildly positive on the Korean economy and currency as despite concerns about large household debt, the Bank of Korea is likely to cut interest rates further in the second half of 2016. Fiscal support is underway too and this should stabilise growth. In addition, fundamentals remain strong with the nation's large current-account surplus while valuation is attractive.

Chart 26: Julius Baer Lifestyle Index – Kuala Lumpur

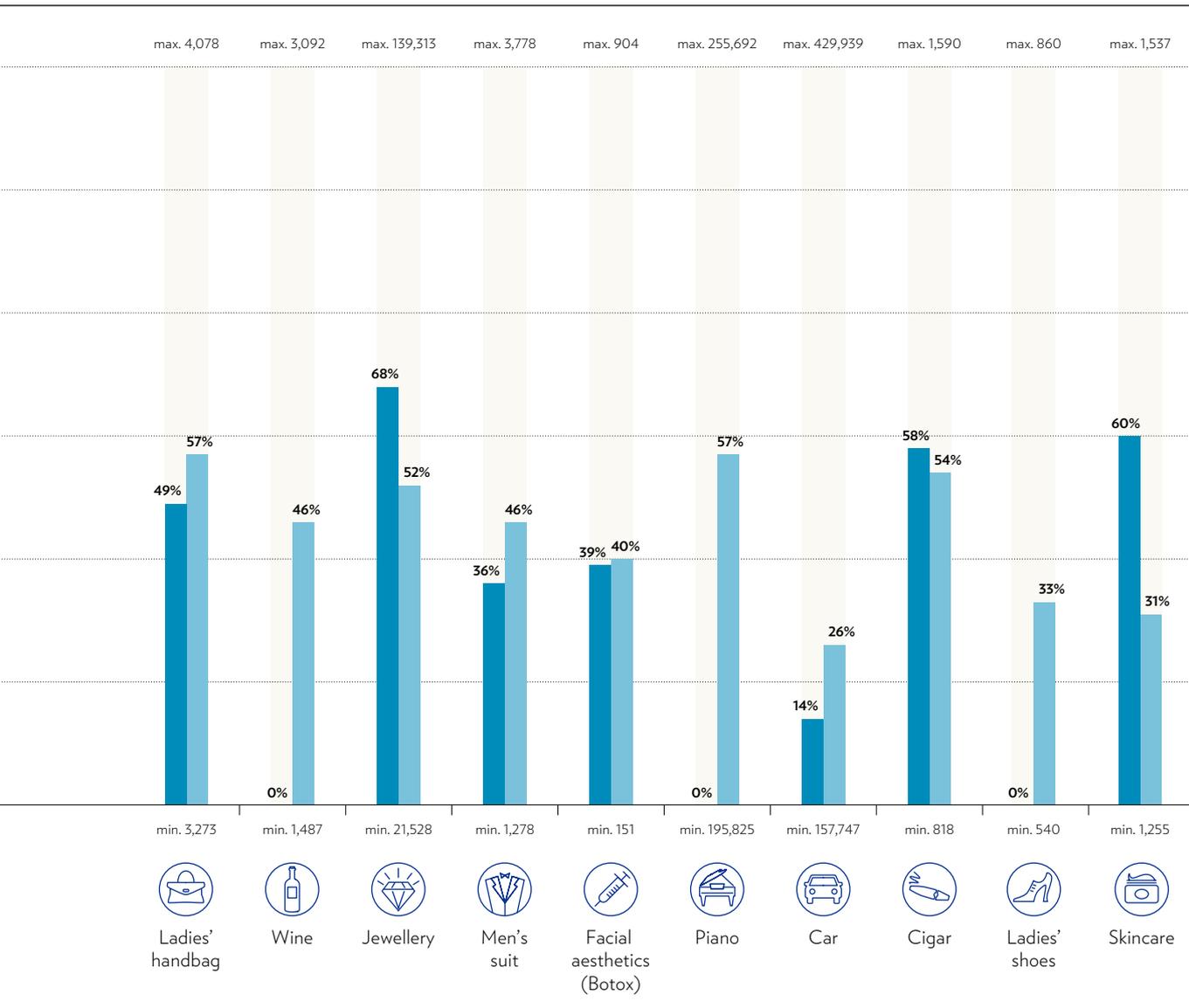


Source: CSG Intage, Julius Baer

City comparisons – Kuala Lumpur

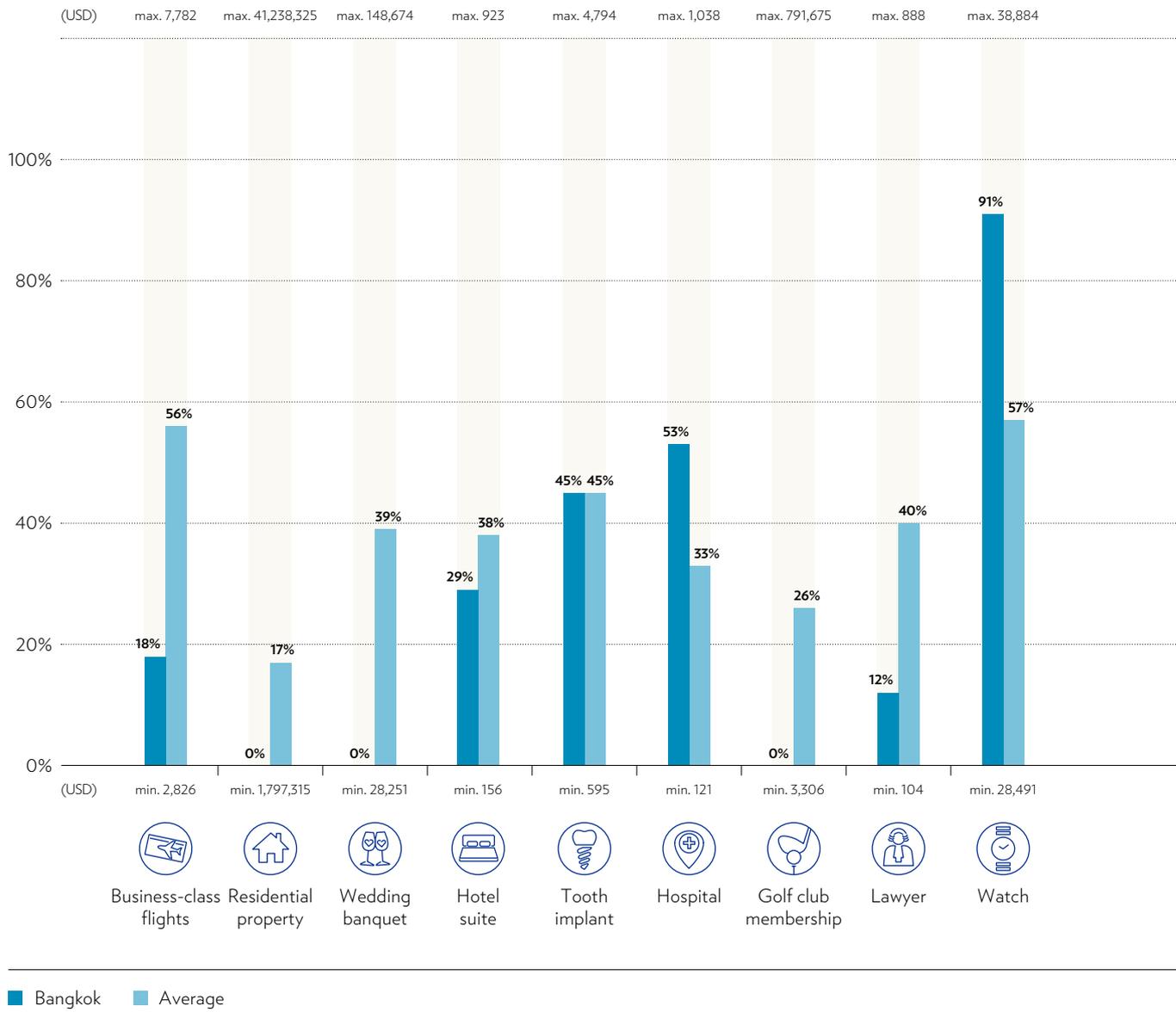
Our basket of goods and services fell by 2.93% y/y in Kuala Lumpur as the Malaysian ringgit depreciated significantly (-6.5%) against the US dollar and items such as business class flights (-25.8%) and legal fees (-28.5%) fell by more than 20% y/y. Overall, price momentum underperformed the average price increase of -1.68% across the cities.

Within the region, Kuala Lumpur ranks as the second least expensive city down two notches from 2014/2015 where it ranked 8th overall. Kuala Lumpur offers the best value for business class flights, luxury watches, wine, pianos and ladies’ shoes where it is the cheapest in Asia to purchase these items.



Our view on the Malaysian economy is favourable despite some risks such as a further decline in oil prices which still account for a large part of public revenues. The economy has diversified from commodities and the introduction of GST in 2015 has helped to broaden the revenue base. We expect a mild depreciation for the ringgit over the course of the next year supported by improving trade surplus and foreign-exchange reserves.

Chart 27: Julius Baer Lifestyle Index – Bangkok

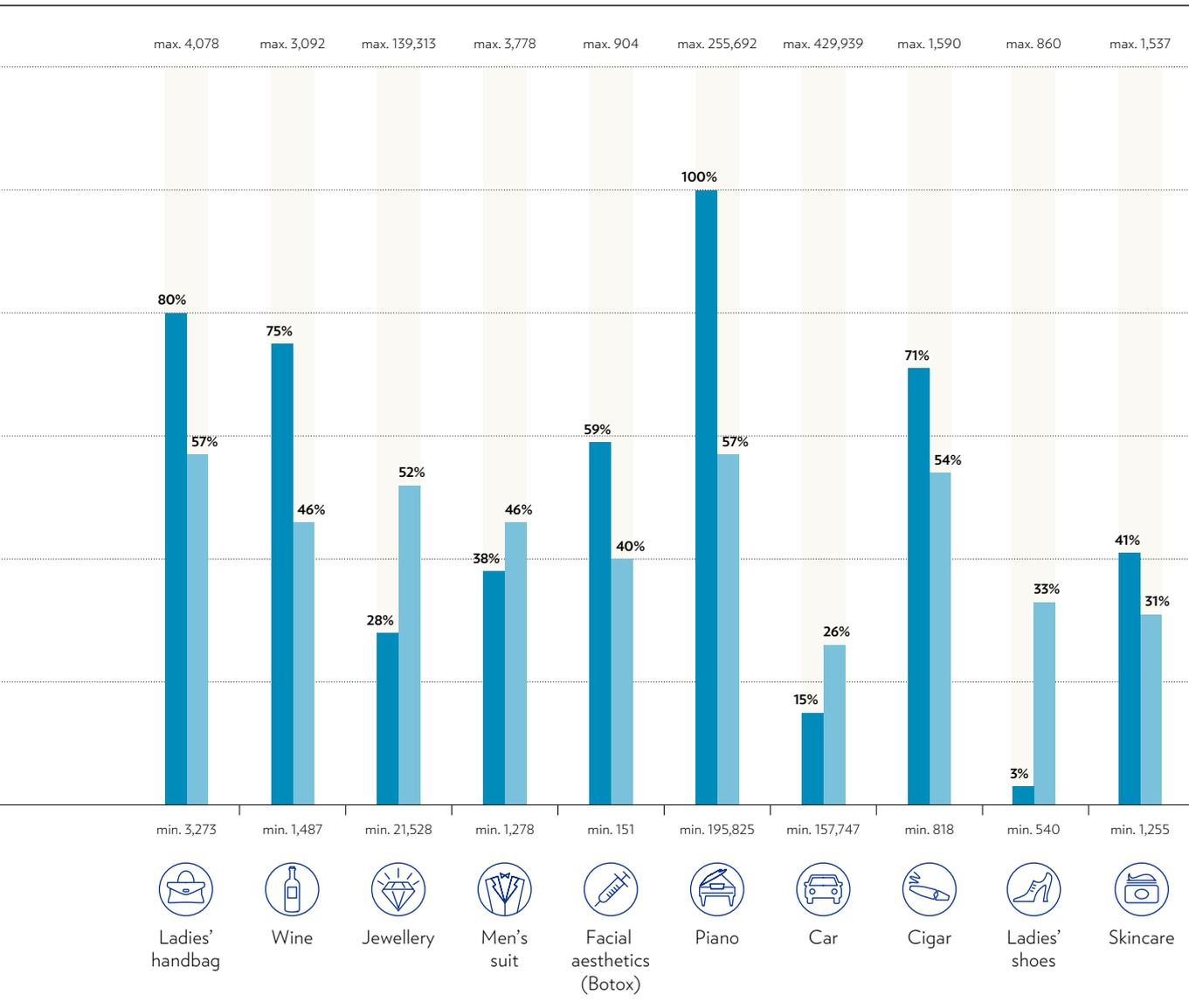


Source: CSG Intage, Julius Baer

City comparisons – Bangkok

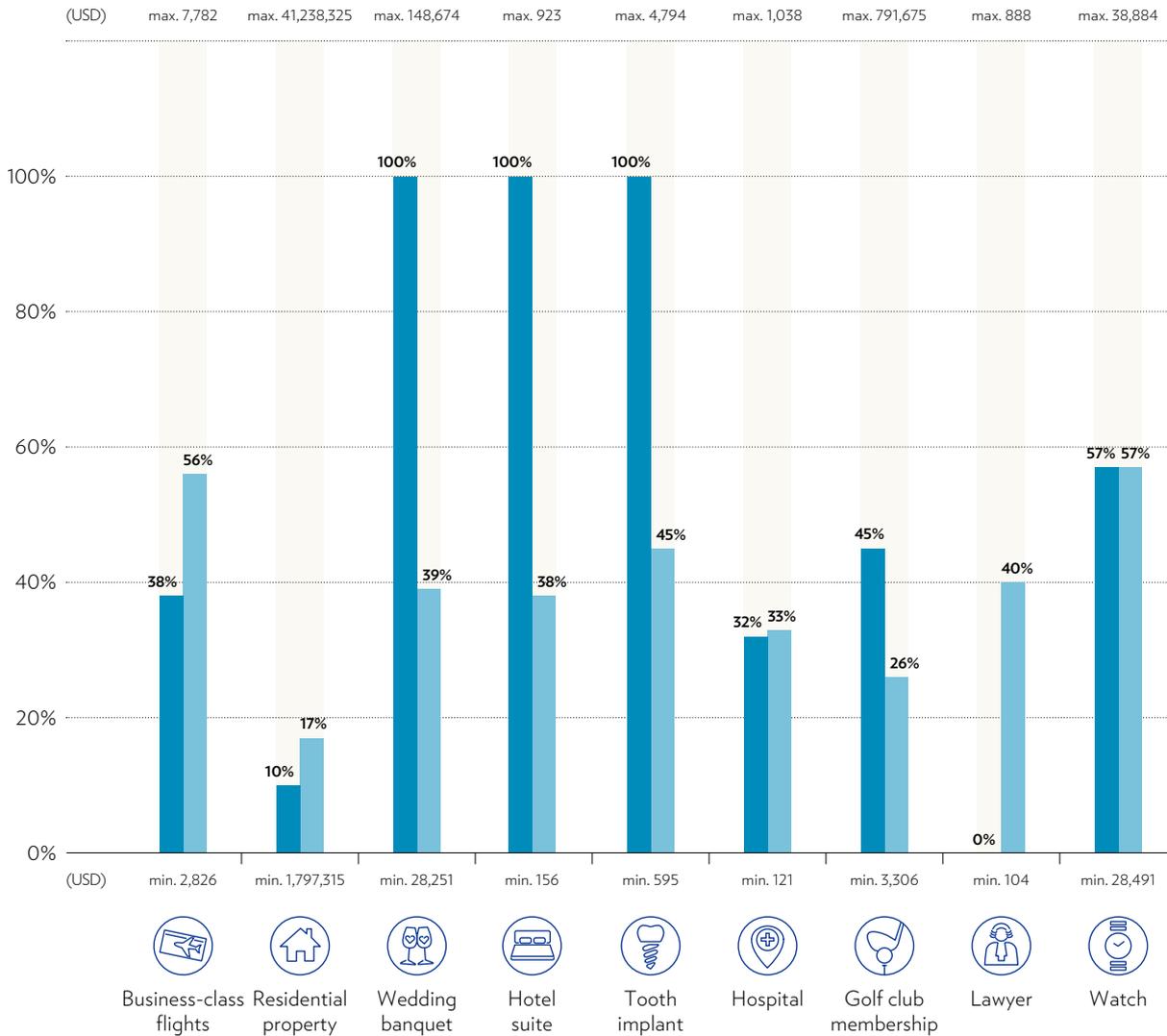
Our basket of goods and services rose by 2.21% y/y in Bangkok as generally positive price performance offset a weaker Thai baht. We saw steady price gains in most items in our basket such as skincare (+11.2%), tooth implants (+9.8%) with the exception of the luxury cars item (-26.5%).

Bangkok currently ranks as the 7th most expensive city in Asia for luxurious living, which is two notches below last year’s position. While big ticket items like property (ranked 11th most expensive), wedding banquets (ranked 11th) and golf club memberships (ranked 11th) are excellent value in Bangkok, it is a price leader for certain discretionary items such as pianos, cars, jewellery and wine largely due to high import taxes on luxury goods.



Following in the footsteps of Indonesia, the Thai customs department is considering reducing import duties on luxury goods to boost spending at home and give a fillip to the tourism industry. If this is implemented, we expect Bangkok's ranking in our index to fall closer to peers such as Manila and Jakarta within ASEAN given comparable living costs.

Chart 28: Julius Baer Lifestyle Index – Tokyo



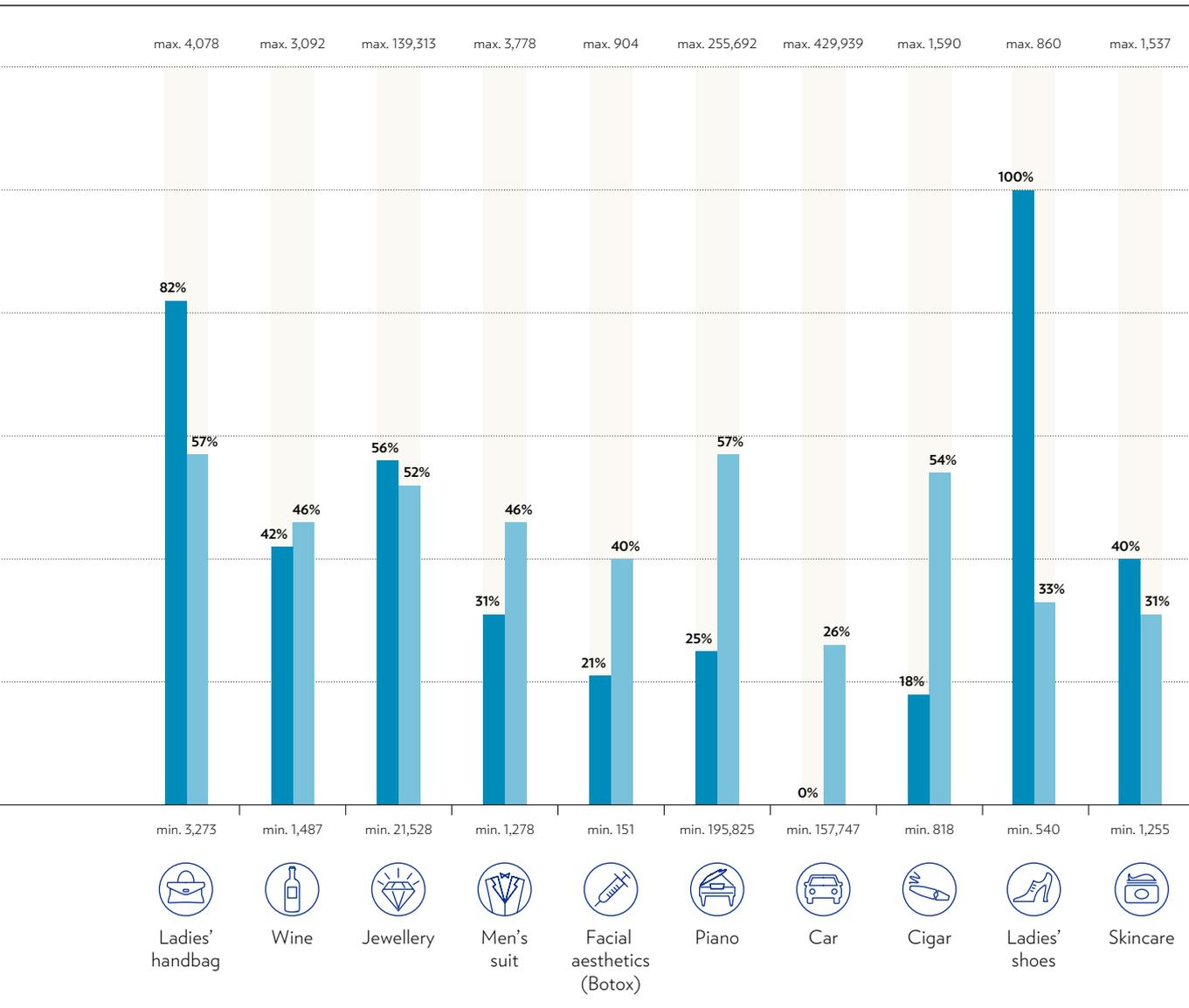
■ Tokyo ■ Average

Source: CSG Intage, Julius Baer

City comparisons – Tokyo

Our basket of goods and services rose by the most in Tokyo (+16.14%) y/y due primarily to the surging yen (+18.4%). However, stripping out the FX component, we still saw high double-digit increases in the price of business class flights, hotel suites, and men’s suits.

As a result, Tokyo rises 3 notches to capture the position of 4th most expensive city in Asia. For individual items, Tokyo is the most expensive city to host a wedding banquet, stay at a top-end hotel, go for a tooth implant and procure ladies’ shoes. On the other hand, it is one of the least expensive for legal fees, cigars and luxury cars.



Given exceptional movements in the currency during our measurement period, the price increases we saw this year may not be sustained. This is supported by our bearish view of the Japanese yen over a 12-month time frame, as we expect the return of deflationary threats to force the Bank of Japan to expand its policy further preventing the yen from strengthening short term, weakening it in the longer term.

On the plus side, however, the upcoming Olympics promises to raise Tokyo's profile quite substantially for travellers into the medium term. Non-resident spending will likely see a considerable boost into the medium term as Tokyo enhances its infrastructure from already high levels, to accommodate more visitors.



ARISING ASIA – BEAUTY CAPITAL

- Urbanisation and an ageing population are driving the worldwide beauty market.
- Asia makes up 36% of the global beauty market and it is expected to grow 4.5% every year until 2019, far faster than the global market.
- China is expected to overtake Japan as the second largest premium beauty market after the US by 2018.
- Premium skincare is one of the fastest growing segments within Asia led by China as consumers become more willing to invest into higher-end products and expanding skincare regimes.

Introduction

Beauty is a modern obsession. The average man or woman in modern society spends 30–40 minutes in a typical day washing, dressing, and grooming himself or herself. A survey by Euromonitor across a number of major markets finds no discernible differences in terms of time spent on beauty routines.

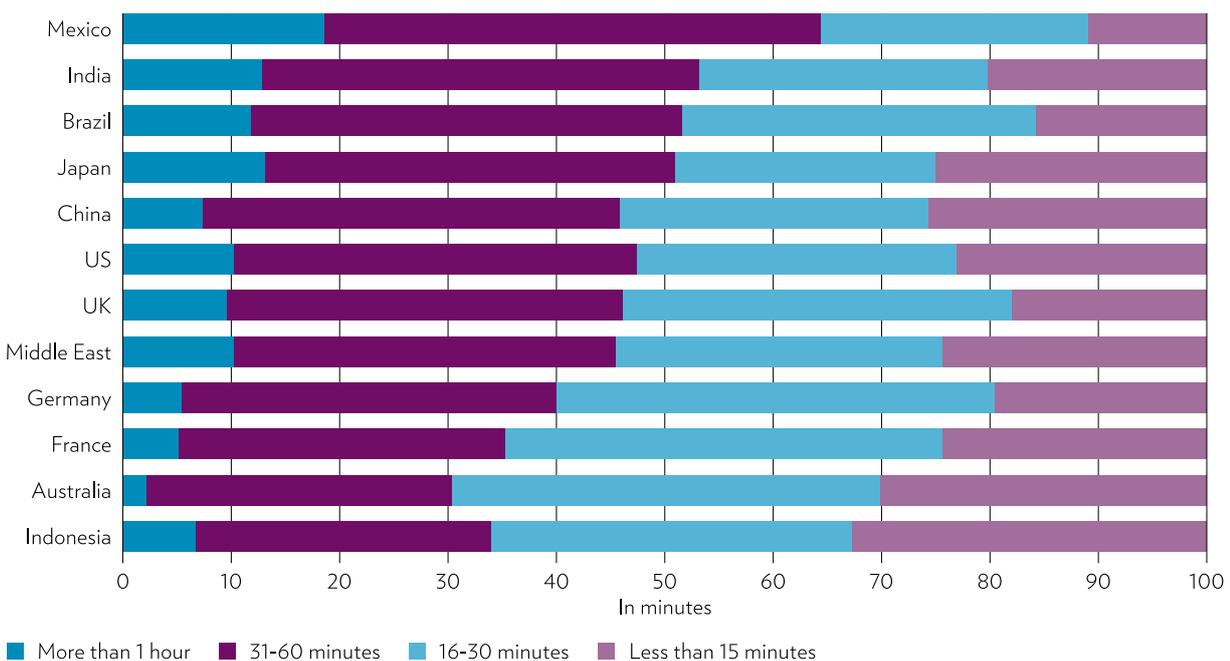
We not only spend time enhancing our appearance; we spend large sums of money on it too. The global beauty market reached a size of USD 229 bn in 2015 and continues to grow at a steady rate. In this edition

of the Wealth Report: Asia we examine the beauty market with a specific focus on the Asian consumer and premium skincare.

Size of the global beauty market

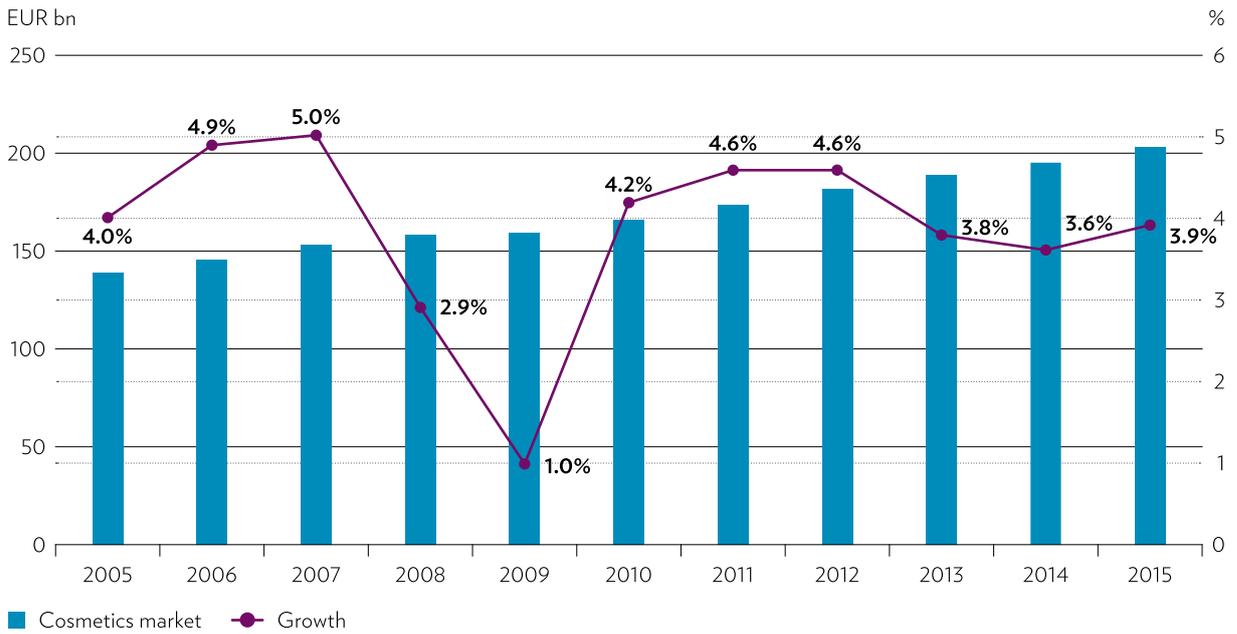
The size of the global beauty market reached EUR 203 bn (USD 229 bn), recording growth of 3.9% in 2015, in line with the average of 3.9% observed in the past decade. The market continues to expand steadily and has proved resilient even during times of tough economic conditions, reporting positive growth even during the Lehman crisis.

Chart 1: Daily grooming time in selected countries (2014)



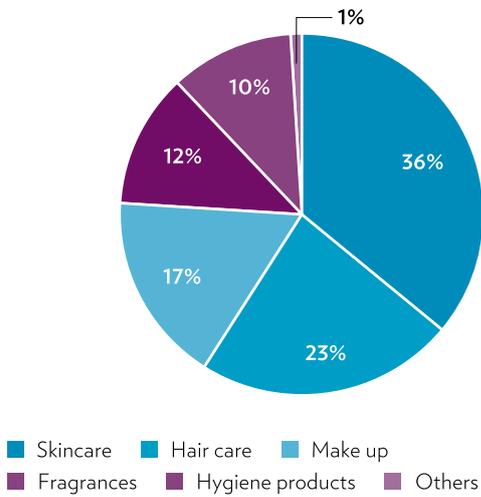
Source: Euromonitor

Chart 2: Global cosmetics industry market growth



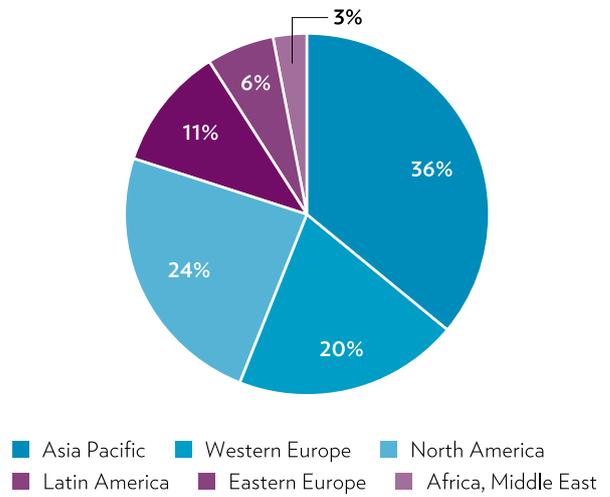
Source: L’Oreal Annual Report 2015

Chart 3: Global cosmetics market segmentation by products (2015)



Source: L’Oreal Annual Report 2015

Chart 4: Global cosmetics market segmentation by geography (2015)



Source: L’Oreal Annual Report 2015

Beauty market at a glance

By product segment, skincare and hair care account for more than half of the beauty market while by geography, Asia continues to dominate demand at 36%. In the next decade, every region in the world is expected to grow with China, US, Brazil, India and Japan expected to be the top five markets.

Skincare accounts for 36% of the beauty market, the largest by far and is expected to remain so. Global sales for skincare are expected to exceed USD 131 bn by 2019 mainly driven by emerging markets in Asia including China which will account for nearly 60% of skincare’s value growth by 2019.

China: Slowly rising to the top

In the global beauty market, China ranks second, having exceeded Japan in US dollar terms in 2013,

following the depreciation of the Japanese yen. US remains the global leader but it is possible that China could overtake the US in the next decade.

Chart 5: Historical growth of selected beauty markets

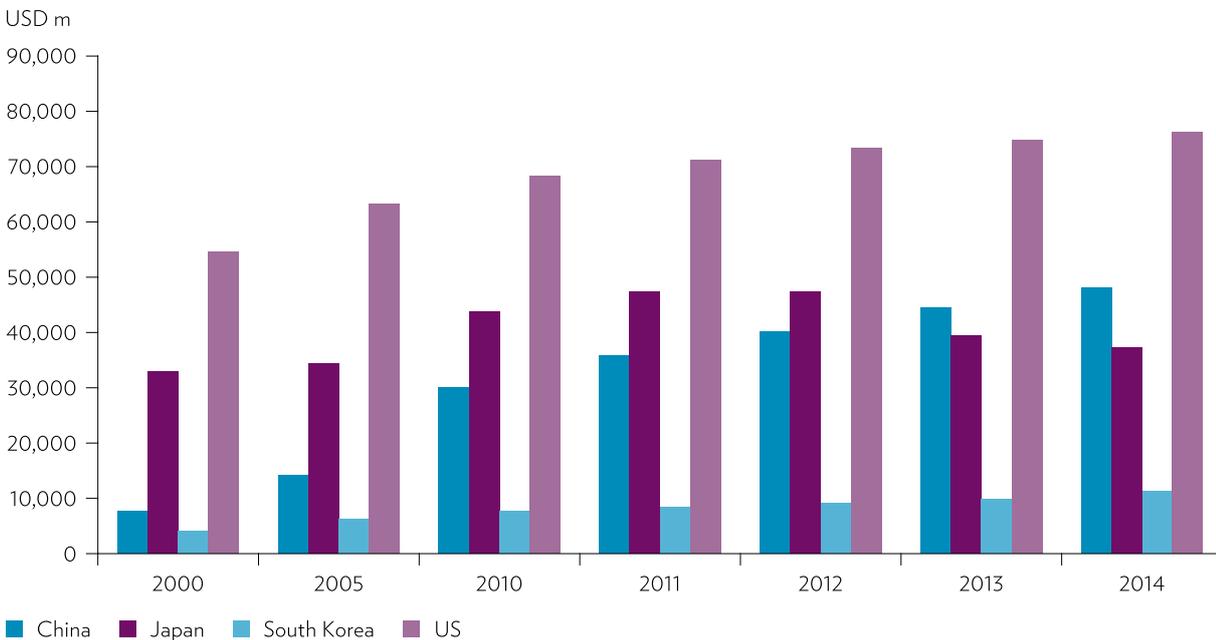
Markets	2000 (USD m)	2005 (USD m)	2010 (USD m)	2011 (USD m)	2012 (USD m)	2013 (USD m)	2014 (USD m)	2000-14 CAGR (%)
China	7,629	13,951	30,134	35,540	39,914	44,229	47,806	14.0
Japan	32,637	34,658	43,806	47,204	47,457	39,259	37,116	0.9
South Korea	4,302	6,164	7,545	8,682	9,228	10,058	11,081	7.0
US	54,459	63,592	68,020	71,056	73,459	74,861	76,276	2.4

Source: CLSA, Euromonitor

China has already assumed the mantle as the leading global consumer of skincare products, having surpassed the US within the past decade and having overtaken Japan in 2013. Within China's beauty

market, half of the total revenue comes from skincare, which has seen a 14.0% compound annual growth rate (CAGR) since 2015, a faster growth rate than the overall beauty industry.

Chart 6: Beauty market by geography



Source: CLSA, Euromonitor

Key demand drivers

Emerging Asian markets: Urbanisation

Urbanisation is a key driver behind beauty product consumption. Higher population density in urban areas facilitates product distribution. Demand for beauty products also tend to rise alongside a rise in disposable income and increased social interaction. Within Asia, India and China have significant potential for greater urbanisation. In the past decade, China grew its urbanisation rate by almost 50%. Yet this is still 35% below the level of developed countries. India's is even lower, but growth in urbanisation is occurring at a slower pace.

Developed markets: Ageing Population

In contrast to emerging markets, an ageing population is a more important driver for the beauty market in the US and Western Europe. By 2017, approximately half of the population in the US will be 50 years or older thereby controlling 70 percent of the country's disposable income. Worldwide, the spending power of this >50-year age group is expected to reach USD 15 trn by 2020¹.

Global beauty market growth by segment

Natural products: Industry players have expanded their portfolios into natural products driven by consumers' and manufacturers' interest to be more environmentally responsible, as well as public scrutiny

over the safety of ingredients. While natural products first debuted in the skincare product segment, they have now expanded to other segments of the beauty industry.

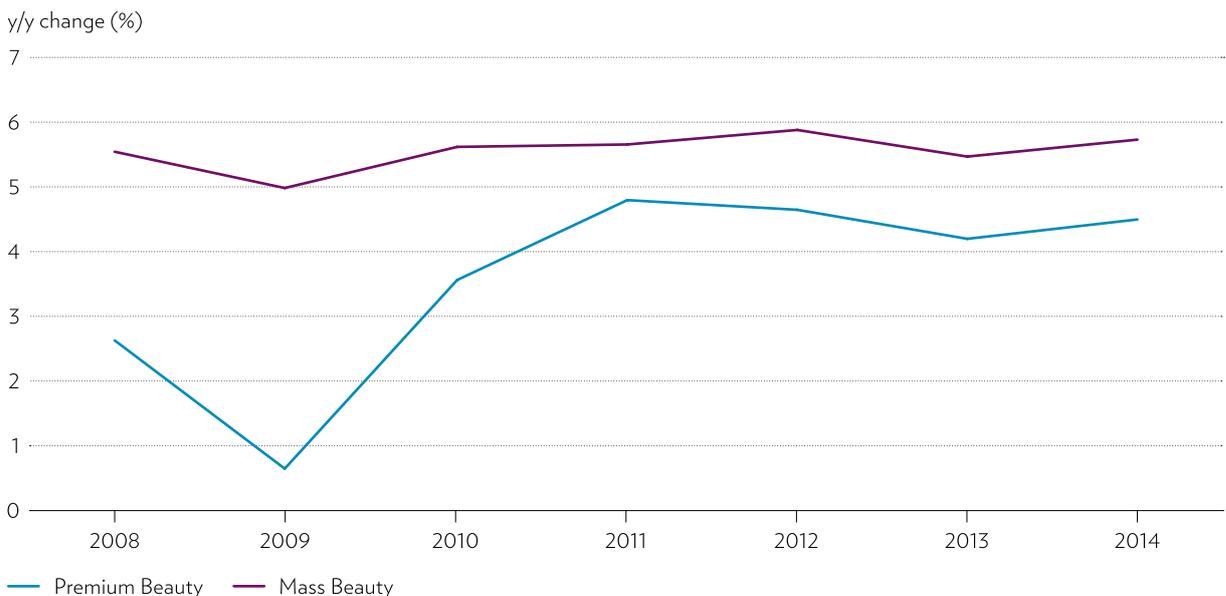
Men's products: There has been an acceleration in demand for men's products in the past few years led by Asia (which accounts for two-thirds of global demand). However, the market for men's skincare is still miniscule compared to the women's skincare market at roughly 3%, implying significant upside potential².

Premiumisation: As consumer concern for personal appearance grows, demand for more sophisticated ingredient formulations and efficacious solutions is increasing. This is particularly noticeable in skincare which is the most valuable category in terms of growth potential in the premium space. Strong demand from Asia, Latin America and North America is expected to add over USD 5 bn in new sales to this segment between 2012 and 2017³.

Focus on the premium beauty market

The growth of the premium beauty market is expected to generate a quarter of the growth for the global beauty industry over the next five years largely driven by China which is expected to overtake Japan as the second largest premium beauty market after the US by 2018.

Chart 7: Premium beauty vs mass beauty growth



Source: Euromonitor

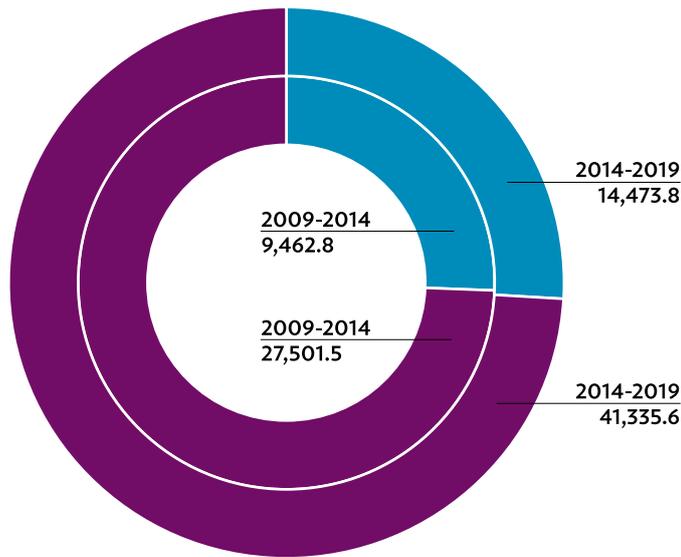
¹ Source: Bank of America Merrill Lynch

² Source: Ernst & Young

³ Source: Euromonitor

Chart 8: Premium vs mass proportion and historic vs forecast (2009–2019)

Values are in millions USD



■ Premium ■ Mass

Source: Euromonitor

Premium beauty is forecasted to grow slightly faster than mass beauty, with a 3% CAGR up to 2019. Companies which focus on premium beauty products still rely on developed markets for the bulk of their growth. However, the emerging markets contribution continues to increase with China, the largest growth contributor, expected to add USD 5.2 bn in retail value by 2019.

Premium skincare

The premium skincare market can be roughly divided into masstige, prestige and ultra-prestige segments which are thus defined by price, retail availability and marketing. Ultra-prestige segments are expensive and exclusive with low accessibility at more than ten times the price point of a mass-market brand. Prestige brands are less exclusive than ultra-prestige brands and can be found at five to ten times the price point of mass-market. Masstige brands, including dermatologist brands and other less exclusive brands, typically retail at two to five times the price point of a mass-market product.

In the US market, the premium skincare market has grown at a CAGR of 5.5% over the past decade as more customers are willing to invest money into skincare and expanding skincare regimes, driving growth in the ultra-prestige and prestige segments.

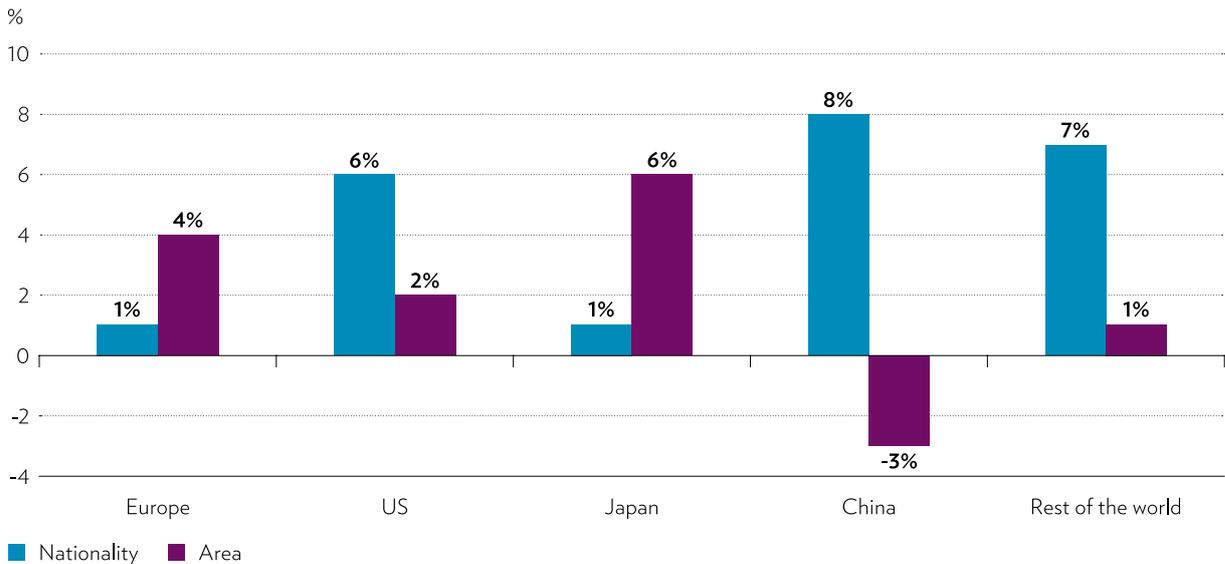
In China, the premium skincare market has grown to comprise a quarter of the total skincare market up from 17% in 2001. This is below the share in other Asian markets such as Hong Kong (72%), Taiwan (59%), South Korea (57%) and Japan (55%)⁴. The high numbers in Asia stand in contrast to the proportion in the West at only 20% in Germany, 30% in the US, 44% in Canada and 48% in France. Looking at other Asian markets there is significant growth potential for the Chinese market.

Impact of exogenous factors (currency and regulation)

Despite a slowdown in the macro-environment, global luxury demand for beauty products is still growing, sustained by tourist consumption, which has been heavily influenced by currency fluctuations and regulations. Consumption and nationality are mutually exclusive in the luxury market. China continues to be the top consumer country (a third of the total market), but Chinese customers tend to consume outside their home country. Europe and Japan benefited from this trend in 2015, with Japan growing the fastest followed by Europe.

⁴ Source: Mirae Asset Financial Group

Chart 9: Luxury goods demand growth by nationality and area (2015)



Source: Business Monitor International

What is driving growth for the Asian beauty market?

The growing consciousness towards maintaining one’s personal appearance and a considerable increase in disposable incomes are the two major drivers of growth for the beauty market in the Asia Pacific region.

How is the Asian beauty market different?

One area where Asian consumers tend to spend or invest more than those on other continents is on skincare because of the increased cultural importance of having well-maintained skin. For example, skincare accounts for roughly 70% of the Chinese beauty market whereas it is only 35% in North America, 32% in Brazil, or 37% in Russia⁵.

Asians also tend to spend more on products that have higher price points (premium or prestige products) with added functions (e.g. whitening, anti-ageing, anti-pollution). An Asian woman, on average, will use eight different skincare products each day, including special products like whitening creams.

In addition, local cosmetic players in Asia are generally very strong compared to those in other emerging markets. This is because many Asian countries have

solid competitiveness in manufacturing, and local companies usually have better distribution networks.

‘Asianification’ of the beauty market

There is a growing number of Asia-inspired products and innovation present already in international markets and the Asianification trend is expected to grow stronger and deliver more product concepts from the region.

The Korean wave

Within Asia, South Korea is one of the most innovative beauty markets with local companies that pioneered BB and alphabet creams within the skincare category. Korean brands have also been expanding internationally. In 2015, Korean exports to China grew more than 300% y/y in value terms (Japanese exports increased 34%)⁶. Korean cosmetics companies have gained popularity in China due to the surge in Chinese tourism as well as aggressive product marketing by Korean companies. One company which has been particularly successful is Amorepacific which has popular brands such as Innisfree and Sulwhasoo. The latter combines Asian medicinal herbs with advanced modern science as its selling point in Western markets.

⁵ Source: Mirae Asset Financial Group

⁶ Source: China Customs

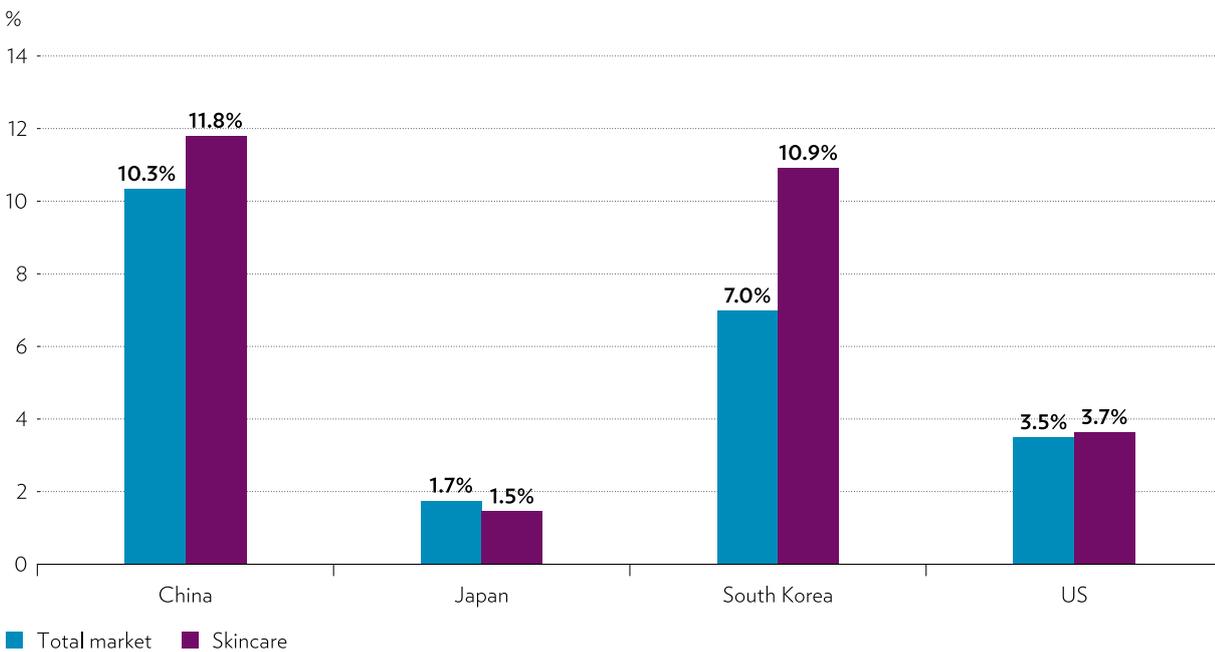
Focus on the Chinese beauty market

The Chinese beauty market is the second-largest in the world with a size of USD 47 bn in 2014 or a CAGR of 14% since 2000. Beauty products remain highly discretionary items where there is still a low annual cosmetics consumption per capita of USD 35, one-eighth that of Japan. As incomes rise, consumers

become more willing to spend money on beauty either by purchasing more product types or more expensive products. According to Euromonitor, the Chinese beauty market is expected to grow at a CAGR of 10.3% from 2015 to 2019 and reach CNY 491 bn (USD 77 bn) in 2019.

China is one of the fastest growing beauty markets

Chart 10: Projected growth of total beauty and skincare market for 2015–2019 (CAGR) (2015–2019)



Source: Euromonitor

Chinese consumers today shop globally

Chinese consumers are one of the biggest drivers of luxury spending worldwide. They spend the most globally (31%) on luxury goods, followed by the Americans (24%) and the Europeans (18%)⁷. 80% of luxury shopping by the Chinese is done abroad with only about 20% in Mainland China. Travel destinations for Chinese luxury shoppers tend to respond to currency fluctuations as they take advantage of favourable price gaps overseas for example in Japan, Korea or Europe.

E-commerce

As a growing number of customers shop on the internet, and e-commerce platforms (like Taobao and JD.com) have matured, e-commerce has delivered the highest growth in the past three years, with a CAGR of 37%⁸. As seen in chart 11, internet retailing as a sales channel for beauty products has grown from 1% to 16% in the five years since 2009. This is partly due to the structural decline faced by general merchandisers and department stores and this trend is likely to continue.

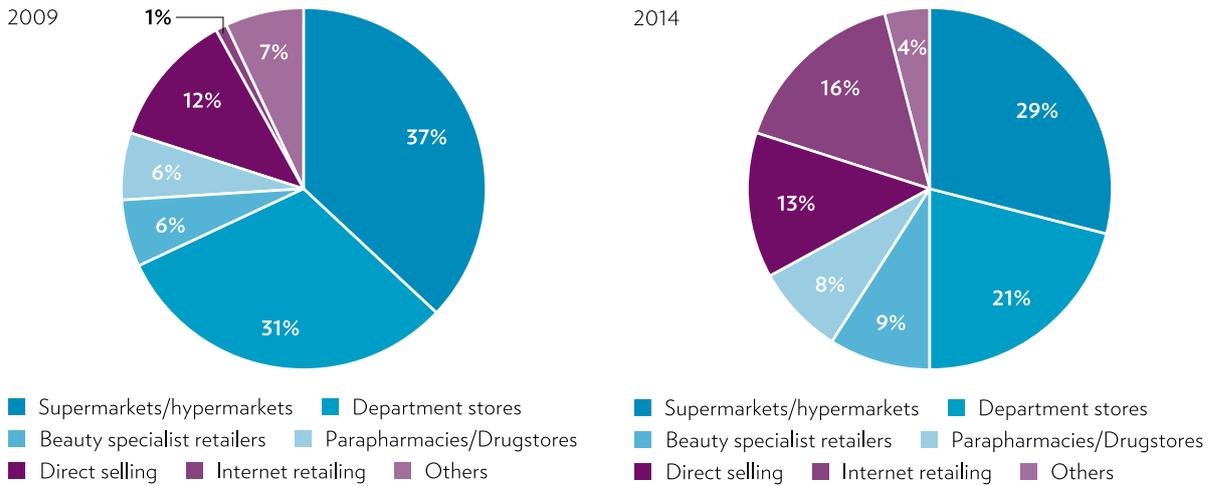
Growth areas in China

The most important growth areas in China today are e-commerce, speciality stores and Asian brands.

⁷ Source: Bain & Co.

⁸ Source: iResearch

Chart 11: China beauty product retail sales by sales channel



Source: Euromonitor, UBS

Specialty stores

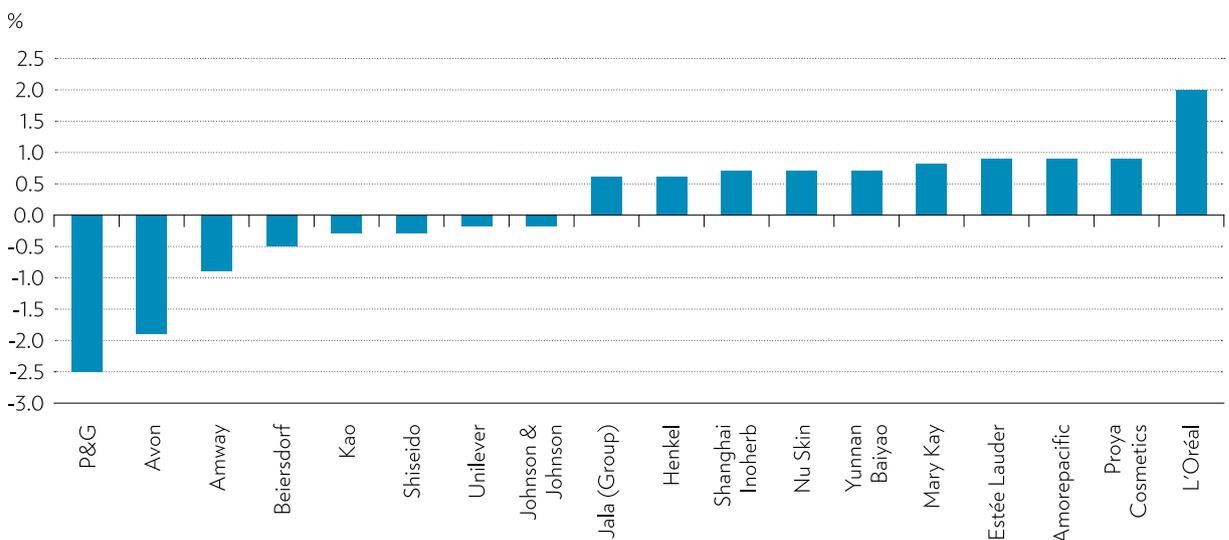
Within the brick-and-mortar space, specialty stores have been doing well, helping to meet demand in lower-tier cities where other channels have been insufficient. In several tier 2 and 3 cities, specialty stores account for more than half of the market. In a number of tier 4 and 5 cities, specialty stores are the only avenue where customers can buy beauty products. Overall, specialty stores have recorded a CAGR of 10% in skincare sales over the past 10 years.

The rise of Asian brands

International brands had a first mover advantage

when they arrived in China in the 1980s and 1990s when the personal care market was still nascent. Multinational companies were able to gain leading positions with their branding strategies, channel development experience and deep pockets. However, in recent years Asian brands have begun to fight back and have grown their market share steadily from 39% in 2010 to 46% in 2014⁹. As can be seen in the chart below, brands such as Amorepacific, PROYA Cosmetics and Yunnan Baiyao have gained significant market share in the past five years at the expense of the larger players like Unilever and Procter & Gamble (P&G).

Chart 12: Share of growth in selected beauty companies in China (2009–2014)



Source: Euromonitor

⁹ Source: Euromonitor

Focus on the millennial consumers

Millennials, defined as people born in the 1980s and 1990s, are an important demographic that consumer-products companies, including those in the beauty industry, are trying to figure out. Globally, there are about 2 billion millennials with 86% of them living in emerging markets¹⁰.

A bear argument for the long-term growth in luxury is that millennial consumers care more about experiences than spending on luxury when compared to the older generation. In addition, it appears that millennial consumers are also less brand loyal. Having a strong online presence is important to gaining interest with millennials. This is especially the case in China where millennial consumers are more likely to purchase via Daigou (shopping agent).

Research has shown that millennials are demanding and price-sensitive consumers who seek value deals. A number of surveys have shown that top brands with the highest exposure to female millennials share underlying factors such as price and brand quality.

The Chinese millennial

Millennials account for 28% of the Chinese population¹¹. They tend to purchase more via Daigou than the older demographic due to the perceived benefits of a broader selection, more exclusive products and better customer service. Like their counterparts elsewhere, Chinese millennials tend to be less brand loyal, and more focused on price due in part to a more pessimistic personal financial outlook.

Social media and the millennial consumer

Social media has dramatically changed the traditional relationship between brand and consumers. For example, beauty brands control only 3% of the 15 billion views and they appear only in 2.5% of the searches per keyword on YouTube. On the other hand, the top 25 beauty bloggers have 2,600% more comments than beauty brand's channels¹². This is a challenge for global beauty companies who will increasingly need to use social media as a way to anticipate and monetise market trends.

Conclusion

The outlook for the Asian beauty market is bright with the Chinese premium skincare market being one of the fastest growing segments. The Asian beauty market is fast evolving with Asian brands gaining market share from international brands and even exporting Asian beauty concepts to the West. The millennial consumer continues to pose a challenge for global beauty industry players given their different value set and propensity to buy and obtain product information through newer, less 'orthodox' channels.

Finally, in conjunction with our research on this topic, we have added an ultra-prestige skincare item to our Lifestyle Index to complement botox as a facial aesthetic item. We expect demand for this category to grow over the long-term as an important luxury consumer product for the HNWI in Asia. Our findings can be found in the Lifestyle Section of this report.

¹⁰ Source: Bank of America Merrill Lynch

¹¹ Source: US Census International Data Base, Nielsen

¹² Source: Ernst & Young

SINGAPORE MACRO

Singapore has regained much of the ground it lost since the crisis of 2008. Singapore's annual average nominal GDP growth rate in the new millennium (2000–08) was 6.4%. Since 2008, the growth rate has fallen somewhat to 5.8%. The story is similar with respect to real GDP growth rates. If anything, the gap is smaller at 5.5% and 5.1% respectively.

In the 2011 Singapore General Elections, the ruling People's Action Party returned to office but with a reduced mandate. In 2015, however, the Party won again and with a much larger vote share than it did in 2011. The policies that were put in place since 2011, however, have stayed. The annual average growth rates of the economy in the last four years up to 2015 at 3.8% and 3.4% in nominal and real terms respectively are reasonable growth rates for an advanced economy with a rapidly ageing population and with tight controls on influx of foreign labour. Singapore is managing its transition to that of mature and ageing economy well.

Prudent management

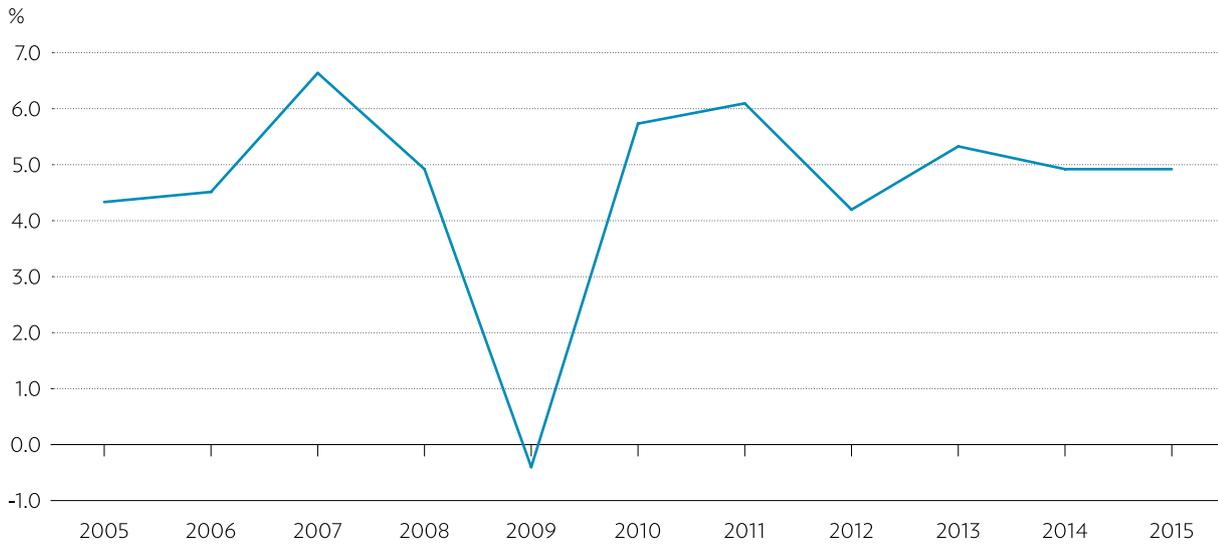
Singapore has restricted inflows on immigrants since 2010–11. At the same time, mindful of the consequences of a property bubble going bust, the government and the Monetary Authority of Singapore (MAS) have tightened loan norms and

raised stamp duties on home purchases. Both buyers and sellers now have to pay stamp duty. In fact, these norms were gradually introduced from 2009 onwards. Property speculation has waned considerably along with real demand as immigrants were the biggest contributors to real demand. Excess supply of housing too has played part in the property slump that has endured for quite some time. Home prices have dropped 9% from the peak in 2013 and transaction volumes have halved. Yet the decline has been orderly. Relatively high down payment from the buyers (at least 20%) has shielded bank balance sheets from the deterioration in asset values.

Labour market concerns

Wage growth in Singapore has been resilient (see chart 1). Total wage growth has averaged 5.2% per annum since the crisis similar to that of 5.1% in the years preceding the crisis. These figures are nominal and include employers' contribution to the Central Provident Fund. Wages at the bottom fifth percentile too have grown more strongly than before. For the six years ending 2014, the annual average wage growth has been 4.7% compared to a meagre 0.9% in the eight years up to 2008. Real wages are rising even faster. The consumer price index has been contracting steadily for a long time. Up to June 2016, the contraction in CPI (y/y change) had lasted 20 months.

Chart 1: Total nominal wage growth



Source: Ministry of Manpower, Singapore

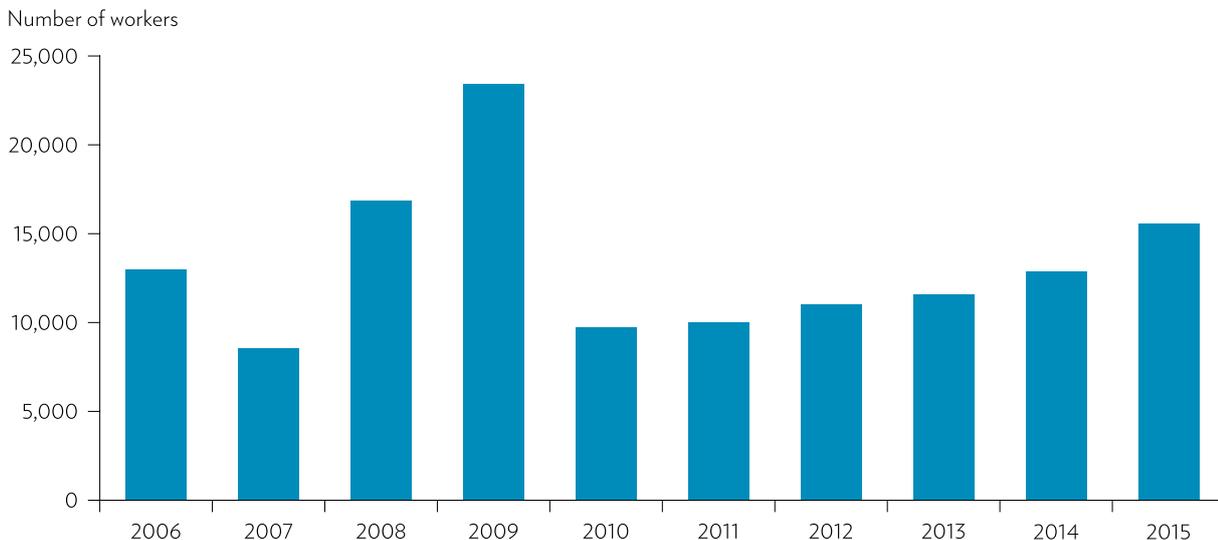
Yet there are some areas of labour anxiety as mentioned in the biannual Macro-Economic Review prepared by MAS:

“Residents who have been laid off are finding it increasingly difficult to re-enter the workforce within six months, with the re-entry rate falling steadily since March 2015 to 51% as of December 2015. This was particularly the case for PMETs¹. While about half the job openings in Q4 2015 were PMET-related, only 48% of resident PMETs made redundant re-entered

the workforce within six months, much lower than clerical, sales & service workers (63%) and production & transport operators, cleaners & labourers (53%).”

Redundancies have been rising steadily since 2010. Redundancies include retrenchment and early release of contract workers. They spiked in 2008 and in 2009 and came down sharply in 2010. However, since then they have been rising steadily, reaching a 15,580 in 2015 (see chart 2).

Chart 2: Redundancy



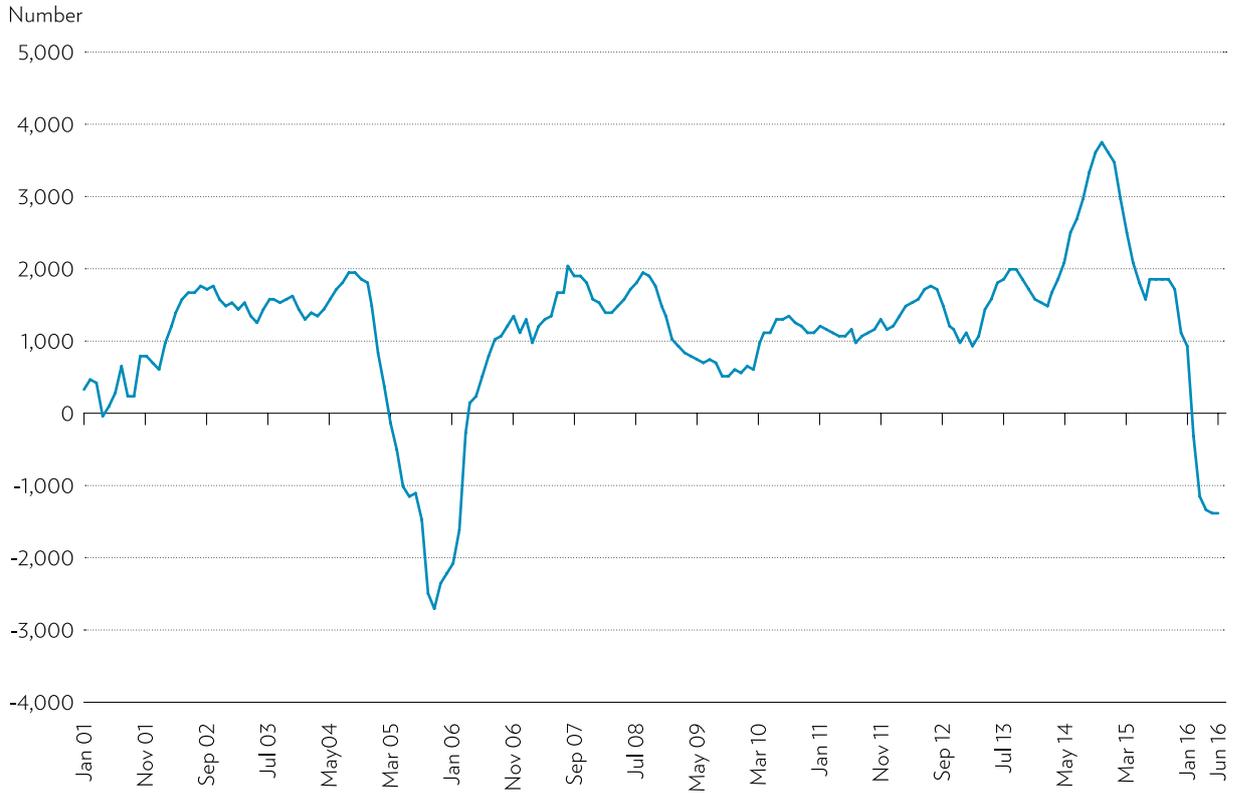
Source: Ministry of Manpower, Singapore

¹ PMET stands for Professionals, Managers, Executives and Technicians.

Low levels of economic dynamism are evident too. Formation of new businesses has yet to recover. It has been down in the last five months up to June 2016 (see chart 3). Clearly, cost of doing business in

Singapore is a big factor. This statistic accords with anecdotal reports of businesses relocating out of Singapore for cost reasons.

Chart 3: Net new business formation (6-month moving average)

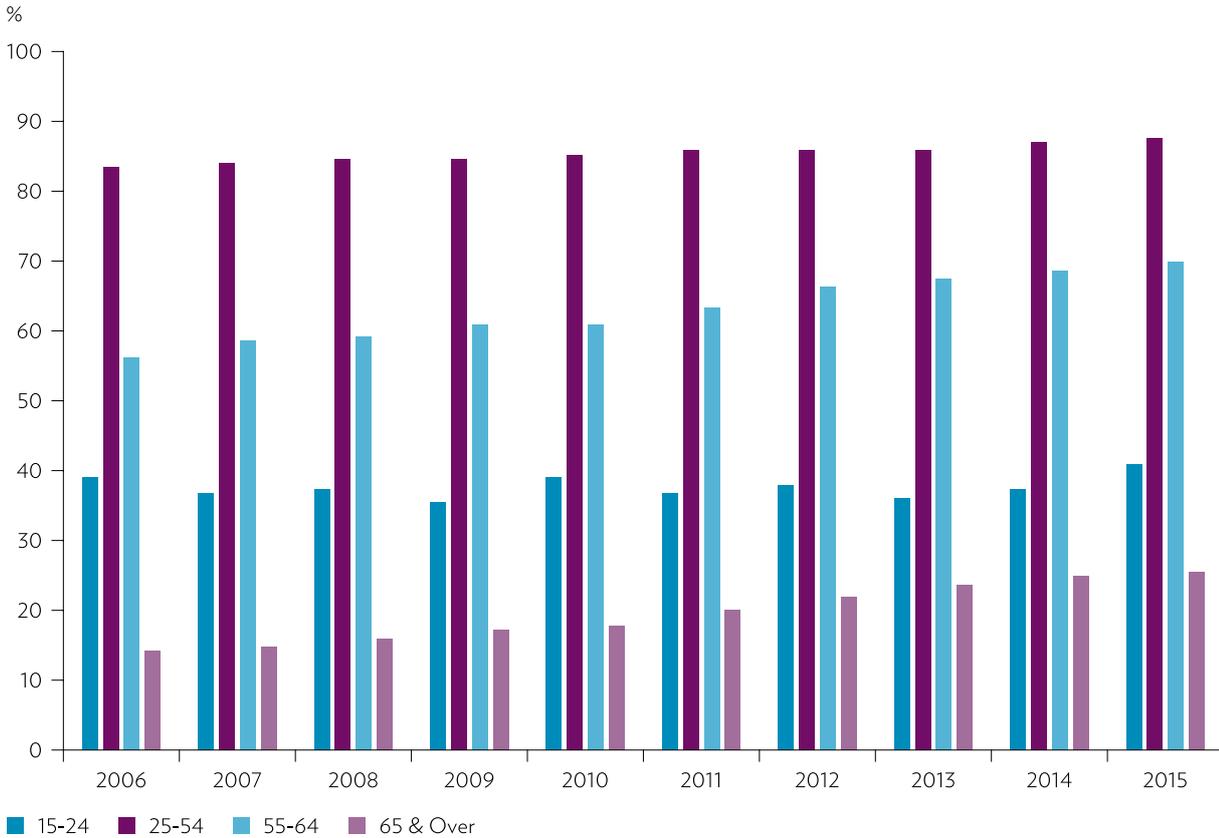


Source: Department of Statistics, Government of Singapore

Much of this is intentional. The Singapore government is encouraging uncompetitive businesses to close down as it is keen to raise Singapore’s capital and labour productivity. This will not be a painless transition. A tight immigration policy has drawn senior citizens to the labour force. Participation rate for people above 55 in the labour force has risen (see chart 4). For those in the age group 55–64, participation rate has gone up from 56.3% in 2005 to 69.5% in 2015. For those above 65 years, the

participation rate is up from 14.3% in 2005 to 25.8% in 2015. This is not necessarily a bad thing. They keep themselves economically independent and mentally healthy too as they are gainfully employed in some activity. Yet there is a skills mismatch for an economy that aspires to become productivity and knowledge based rather than rely on factor accumulation as before. This is a worldwide phenomenon with no straightforward answers.

Chart 4: Labour force participation rate by age group



Source: Department of Statistics, Government of Singapore

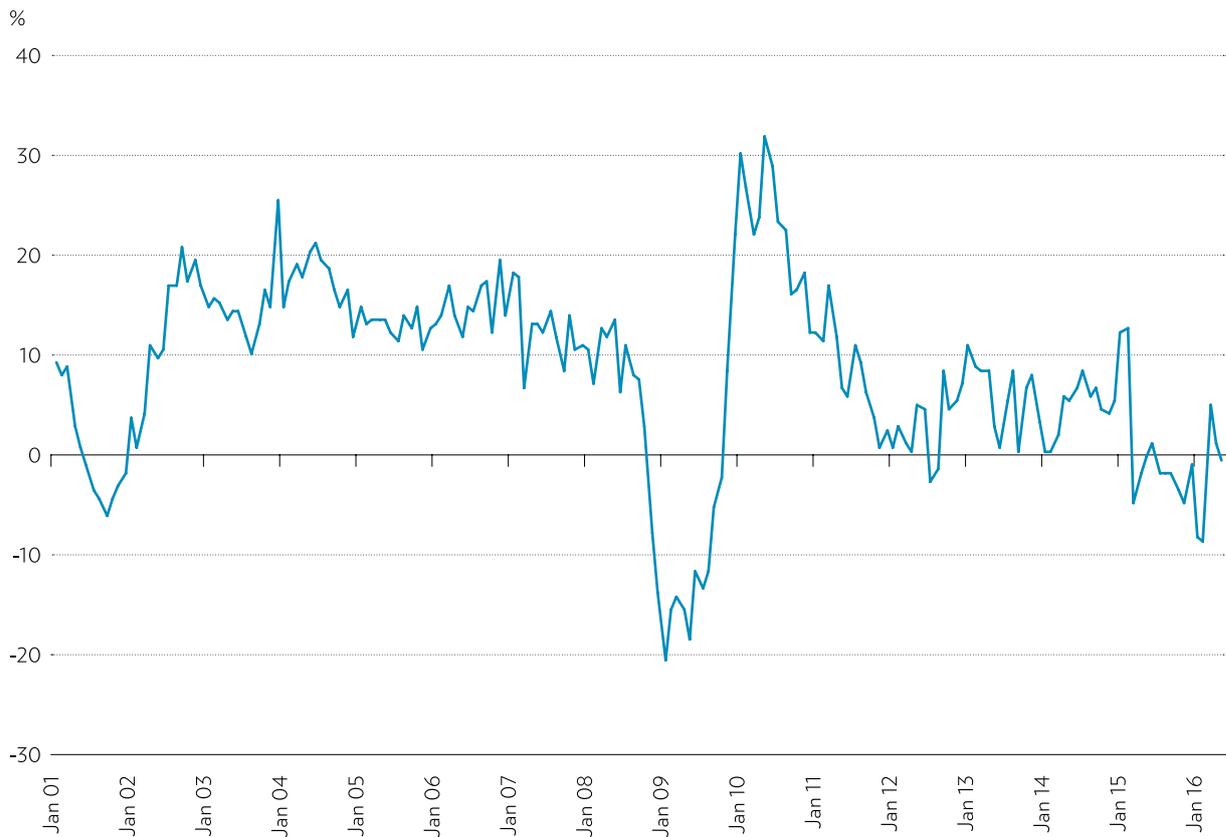
Global headwinds

While Singapore’s costs and tight labour market are important factors, the main challenge has come from a stagnant global economy given its export-oriented economy. The International Monetary Fund (IMF) has been downgrading its global growth forecasts year after year (see chart 5). Forecasts for 2016 have been lowered by the IMF. Monetary stimulus that has been applied by central banks around the world has not yet returned the world economy to sustained growth.

The stimulus has sustained asset prices more successfully, though.

Consequently, export growth from emerging Asia in volume terms has been declining. Data available up to February 2016 show that export growth from emerging Asia turned negative in March of last year and has persisted since then, except for a break in June 2015 (see chart 5).

Chart 5: Emerging Asia export growth (seasonally adjusted. Fixed base 2005=100)



Source: CPB Netherlands Bureau for Economic Policy Analysis

Singapore dollar as a store of value

As a small, open economy, Singapore remains vulnerable to a downturn in the world economy as policymakers elsewhere in advanced economies appear determined to repeat the boom–bust cycles. That is a non–diversifiable risk for Singapore. However, the important point is that Singapore is managing its domestic risks quite ably.

Under the circumstances, Singapore has opted to manage the difficult transition through restructuring and deflation in the prices of goods, services and

assets rather than through asset price reflation. That is commendable. Indeed, Singapore’s gently deflating property market has kept it shielded thus far from any systemic risks.

A counterfactual scenario would have been to persist with stimulus with painful and debilitating consequences down the road. Therefore, Singapore’s strategy of managing the transition through income support for lower income families while the rest of the economy restructures appears sound. That marks out the Singapore dollar as a long–term store of value.



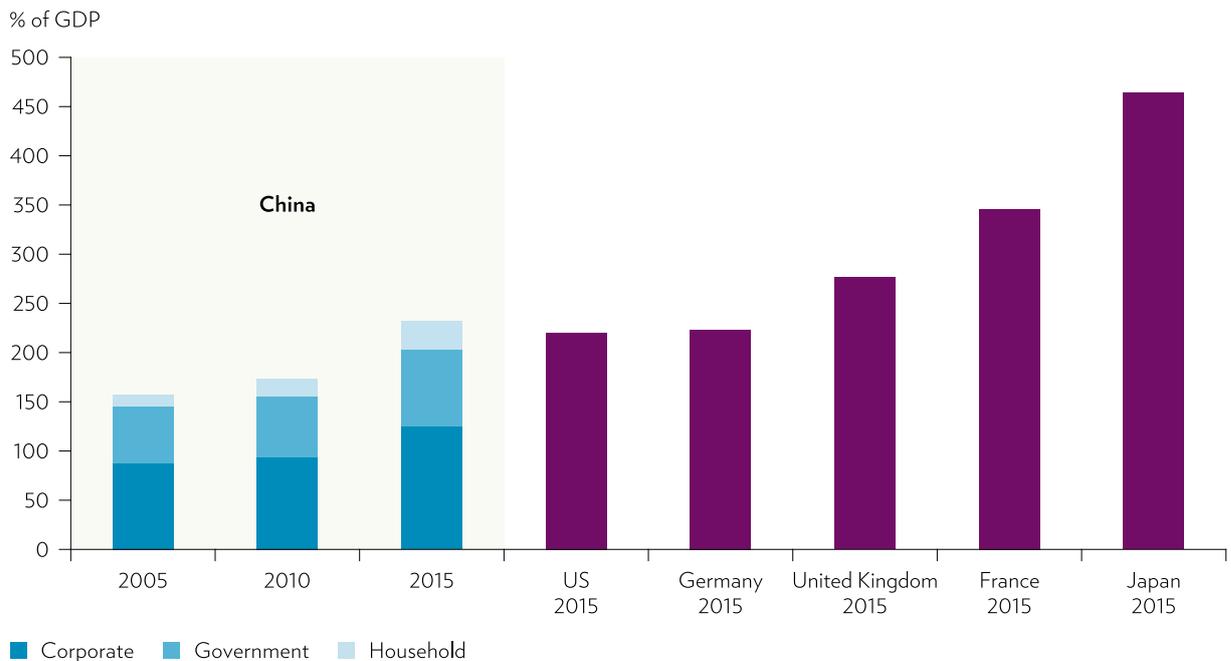
CHINA MACRO

For the first decade of the 21st century, China’s GDP growth rate averaged above 10% per year. Since the peak in 2010, growth has averaged around 7% and is widely assumed to trend lower. The debate over the causes and implications of this structural decline in growth has dominated much of the China-related narrative in recent years, in our view; to the point the nature of China’s ongoing transformation is lost in the noise that this debate generates. In short, it is well known that China is slowing down, but there is more to this story than a secular peak in growth rates.

First, in terms of risks, the deceleration in growth has been accompanied by a broad increase in leverage. Government-linked and corporate debt, in particular, has grown substantially, moving the needle by a significant portion of GDP. All told, over the past

decade, China has accumulated roughly USD 2 trn of debt, based on numbers from the IMF and Bank of America Merrill Lynch. On the surface, this increase has caused alarm in some corners, notwithstanding the fact that over the same period, China has gone from being a two trillion dollar economy to one that is five times the size now. Furthermore, debt service ratios – these measure China’s ability to access foreign currency to make good on debt payments not denominated in renminbi – are very robust. Hence the increase in the debt, especially when measured against mature economies that are smaller in size, needs to be put into perspective. Any rapid increase in leverage has to be monitored closely for signs of distress in debt service, but we would argue that China is far away from posing a systemic risk in this regard.

Chart 1: China’s gross debt as a percentage of GDP

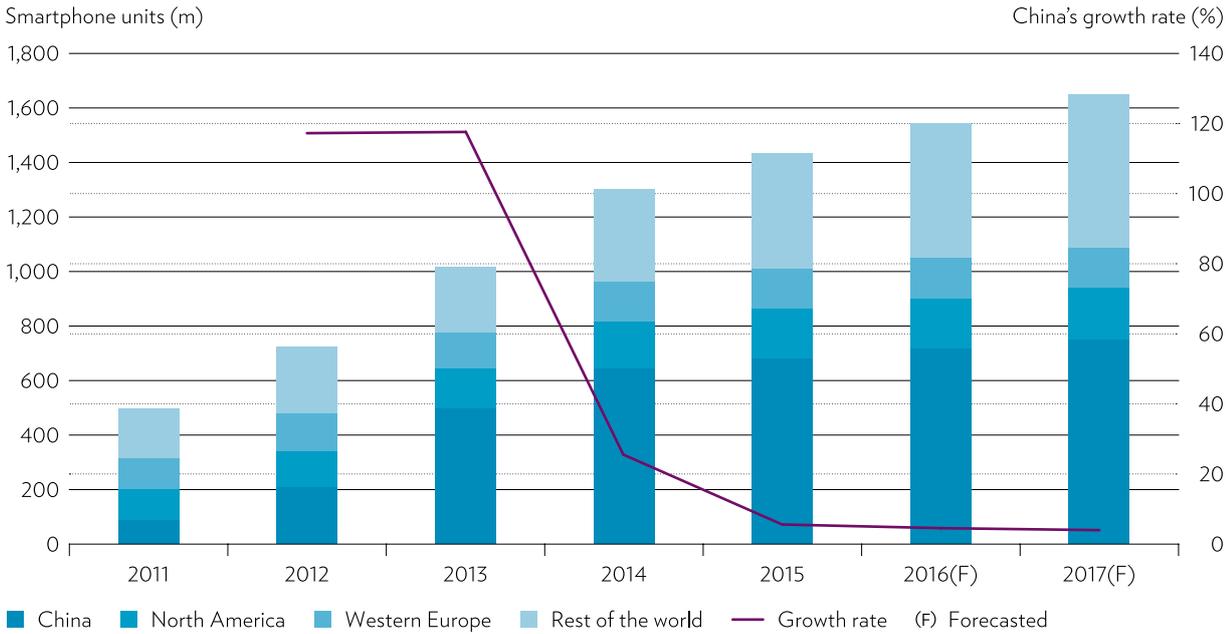


Source: Bank of America Merrill Lynch, Julius Baer

More poignantly, the critical question is to what extent the economy is shifting towards higher value-added services and in turn, a consumer-driven model. Taking this a step further, there is a notion that economies can 'leap frog' stages in their development, something that is arguably taking place in China now. For example, China lags other countries in terms of

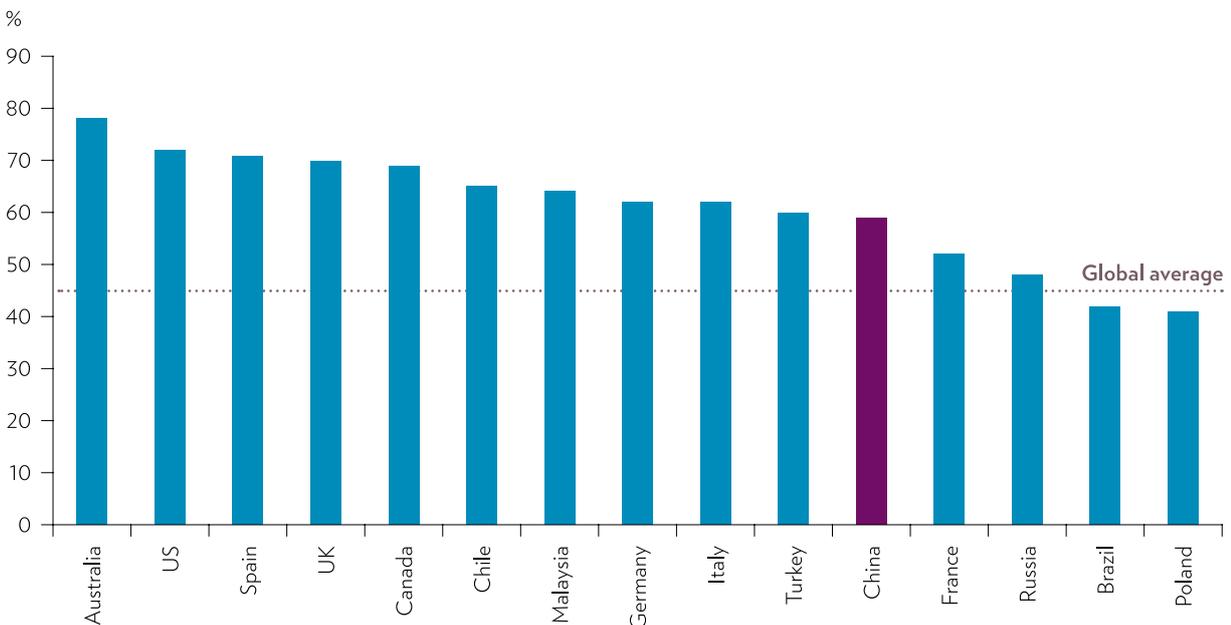
overall smartphone usage, yet at the same time, roughly half the world's smartphones are sold to Chinese consumers. What this fact magnifies is the untold potential of China's digital economy, a topic we explore more closely in the entrepreneur profile that follows this section.

Chart 2: Number of smartphones by region



Source: Citi Research, Julius Baer

Chart 3: Percentage of adult population with a smartphone (2015)

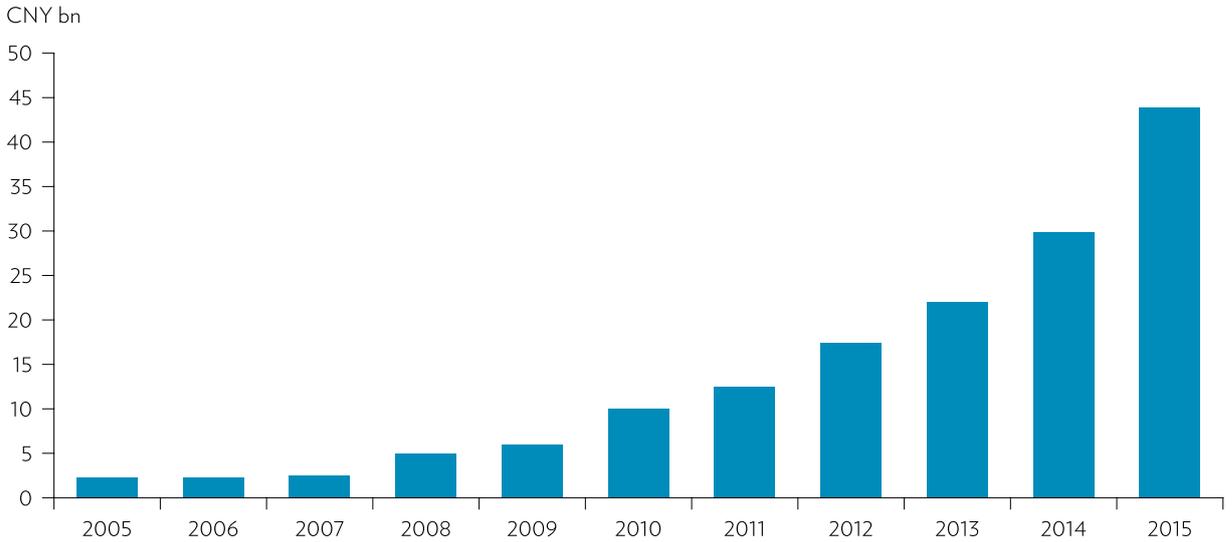


Source: Citi Research, Pew Research, Julius Baer

Beyond hardware, China is equally undergoing rapid growth in software: perhaps one of the clearest examples of this is the boom in movie box office sales. The well over CNY 40 bn per year in movie theater

revenue speaks of the opportunities in mobile content distribution, as smartphone penetration rises in tandem with the demand for content.

Chart 4: China's box office revenue

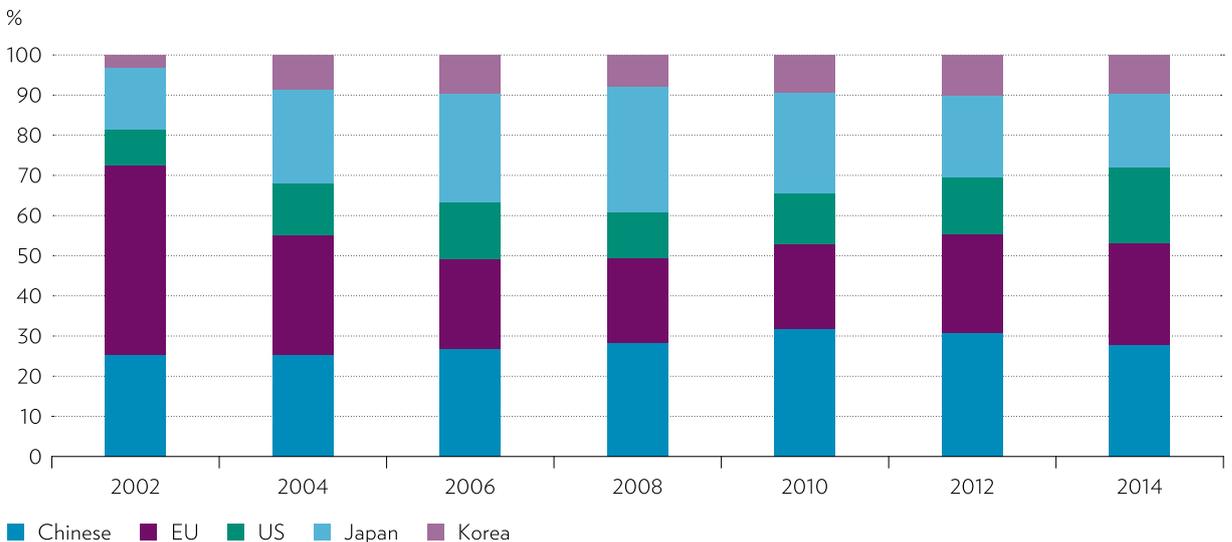


Source: CLSA, China State Administration for Radio, Film and Television, Julius Baer

More prosaically perhaps, the market for passenger vehicles displays another important facet of China's development: intense competition where early leads do not guarantee a permanent dominant position. A decade ago, European car makers were in pole position relative to other car makers in China. Since

then, market shares have shifted, with Korean and US manufacturers jostling for customers alongside Japanese and Chinese firms. This outcome underscores an important distinction that we argue is vital to keep per capita income growth rising: market-derived competition and innovation.

Chart 5: Market share of passenger vehicles by origin

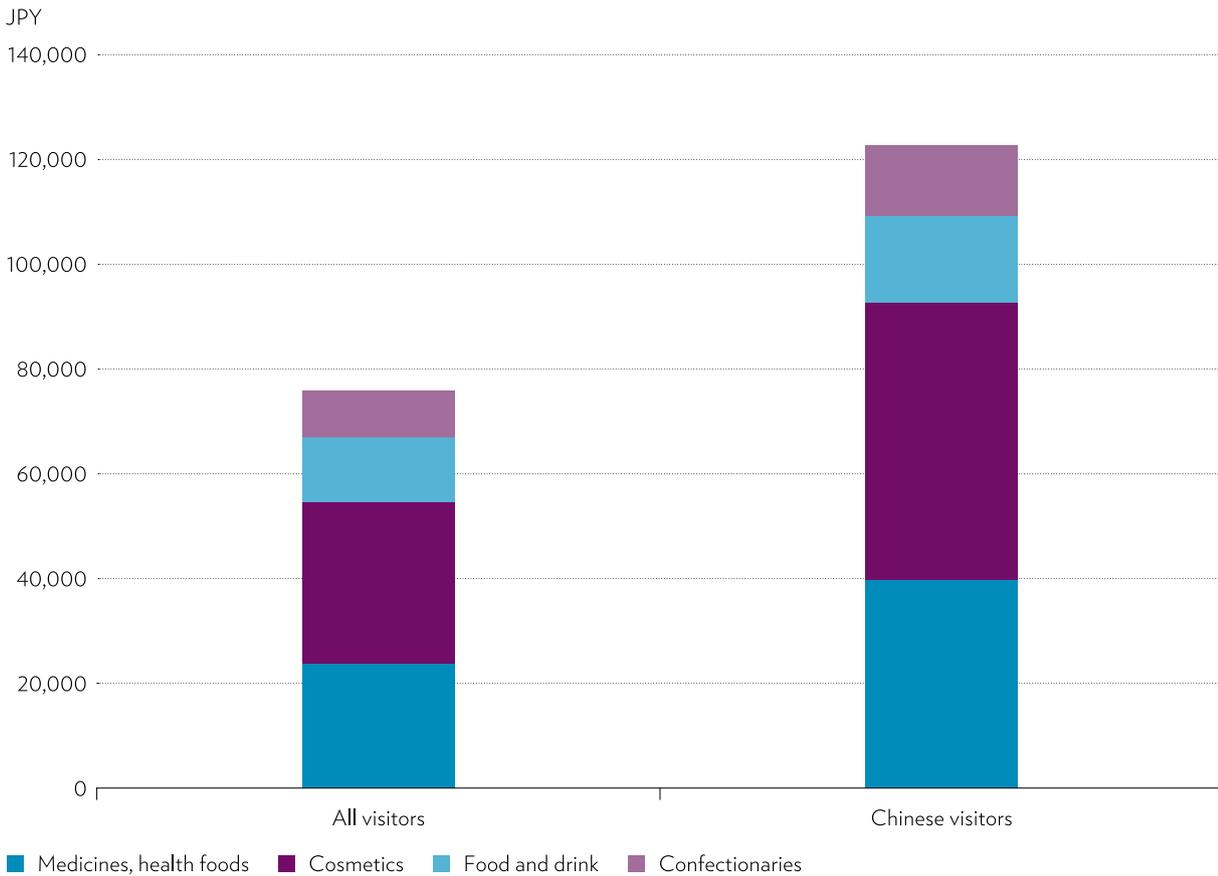


Source: UBS Investment Bank, Julius Baer

Lastly, sticking with the ‘beauty capital’ theme of this year’s report, this is certainly one area that China’s influence is being widely felt. As tourism volumes grow globally, visitors from China are notable for their high spending, especially in the cosmetics and related goods. For an economy such as Japan, being able to

attract some of this demand has been an important trend in recent years. Indeed, the average outlay by a visitor to Japan from China is 60% higher than the average, with roughly USD 500 being spent on cosmetics alone.

Chart 6: Amount spent by item, per shopper (between October and December 2015)



Source: Japan Tourism Agency, JP Morgan, Julius Baer

What this demonstrates to us is that aggregate measures of wealth, in particular nominal GDP size, have less relevance today now that China’s economy has reached its current size. Far greater importance

should be placed on sector-level developments to see where consumers are headed next, be it as tourists with increased spending power or as avid fans of digital content in a fiercely competitive environment.

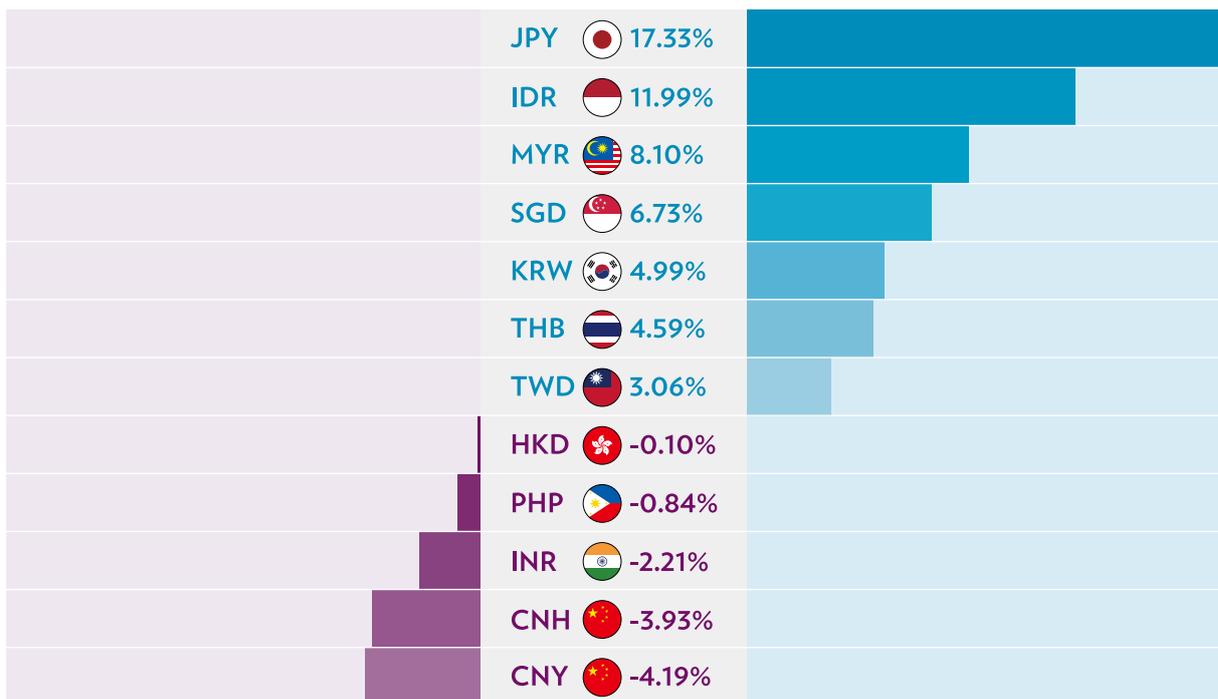
INDONESIA MACRO

Indonesia: Staying out of the limelight

Indonesia was considered one of the ‘Fragile Five’ economies along with India in 2013 when the Federal Reserve thought aloud about ending its bond purchases (Quantitative Easing). The US dollar could buy 3% more Indonesian rupiah by the end of 2014 and 10% more by the end of 2015. However, something interesting happened along the way.

The Indonesian rupiah had weakened to an average exchange rate of USD/IDR 14,402.3 in September 2015. By the end of the year, it had strengthened to USD/IDR 13,840.0. Indeed, since October 2015, the Indonesian rupiah had been the top performer among Asian currencies vs. US dollar, except for the Japanese yen (see chart 1).

Chart 1: Asian currencies in recent months (% change vs. US dollar) (between October 2015 and July 2016)



Source: Bloomberg Finance L.P.

Indonesian President Joko Widodo (October 2014), assumed office a few months after Narendra Modi (May 2014) took office in India. Initially, he struggled to get the better of his opposition in his own party and outside. The international press dubbed the country’s attempt to secure Indonesian ownership of resource assets as ‘resource nationalism’. This turnaround has been largely because the Indonesian

government had received breathing space to govern. Further, the falling price of crude oil helped prevent the fiscal deficit from getting out of control. Of course, the government took action like India did by cutting fuel subsidies and raising fuel prices towards the end of 2014. Indonesia’s fiscal deficit is a modest 3.9%, in part thanks to these efforts.

Another reason for the outperformance of the Indonesian currency has been the relatively better health of the Indonesian banking system and its inflation performance. Just to provide a comparative perspective, Indonesia's banks have a capital adequacy ratio of 21%, while non-performing loans were 2.5% (gross) and 1.2% (net).

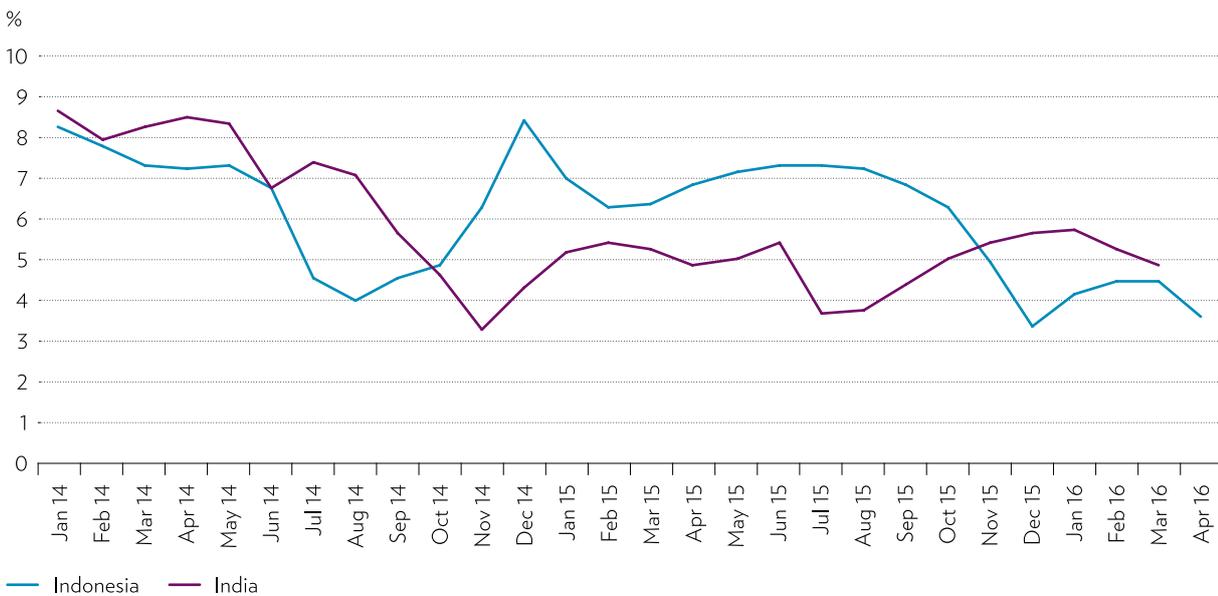
Indonesia's current account deficit/GDP ratio is estimated at 2.1% for 2015. Indonesia's economy is not clearly firing on all cylinders. Two-wheeler and automobile sales are trending down. GDP growth which was expected to be around 5.0% for 2016 is now estimated only at 4.8%. While the forecast is for the growth rate to recover to 5.4% next year (Asian Development Bank estimates), it is quite possible that global headwinds peg the growth rate back to 5.0%, if the numbers for the first quarter are any indication. GDP growth contracted q/q for an annual growth rate of 4.9%, whereas consensus expectations expected 5.1%. This is not a big miss but a minor disappointment, nonetheless. Overall, economic growth rate for 2016 is still expected to be around 5.0%.

Inflation in Indonesia looked likely to get out of hand in 2015 as it did between 2013 and 2014 (one reason why it was part of the 'Fragile Five' club) but it quickly

subsided thanks to the falling price of crude oil, slower economic growth and more moderate growth in M2 Money supply. Relative to India, inflation has been benign so far this year. Earlier rate hikes in 2013 and 2015 placed the central bank in a position to ease policy in 2016, from a position of strength. Despite a narrower interest rate differential, the rupiah has remained resilient in the face of global shocks, such as the surprise Brexit vote. In February, Bank Indonesia lowered the reserve requirement on banks from 7.5% to 6.5%. It took effect from mid-March. The rupiah did not weaken then. Nor has the financial market turmoil caused by the British vote to exit the European Union weakened the rupiah. The currency has remained resilient. Clearly, Bank Indonesia has passed the test of credibility with financial markets.

In April 2016, Indonesia also changed its monetary policy framework by replacing the one-year rate as a policy instrument with a one-week repo rate. The one-year policy rate was at 6.75% when this change was announced. The one-week repo rate was 5.5%. It was not a rate cut but it was a stealth ease, nonetheless. By referencing the one-week rate, the psychology on interest rates will change as the focus will be on a much lower number. The one-week (reverse) repo rate was further lowered to 5.25% in June.

Chart 2: Indonesian inflation trails Indian inflation rate

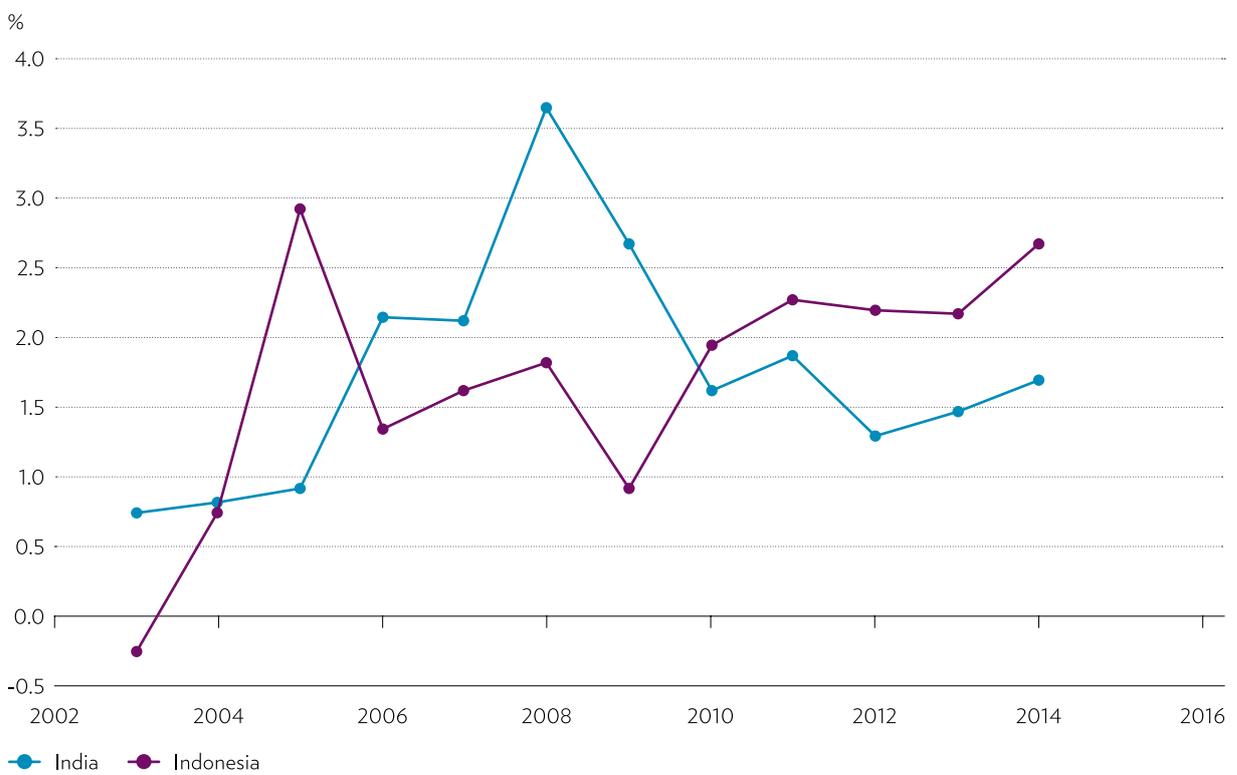


Source: Ministry of Statistics and Programme Implementation, India and Bank Indonesia

In a move to liberalise investment into the economy, Indonesia removed many items from the Negative Investment List in February of this year. This opens the door to foreign participation in a broad range of sectors and alleviates the risks of protectionism as discussed earlier in this year's report. Interestingly, Indonesia has expressed an interest to join the Trans-Pacific Partnership; this in itself would likely boost trade but could also potentially expose the rupiah to upward pressures. Foreign ownership can be a double-edged sword. The currency can quickly become overvalued as inflows surge.

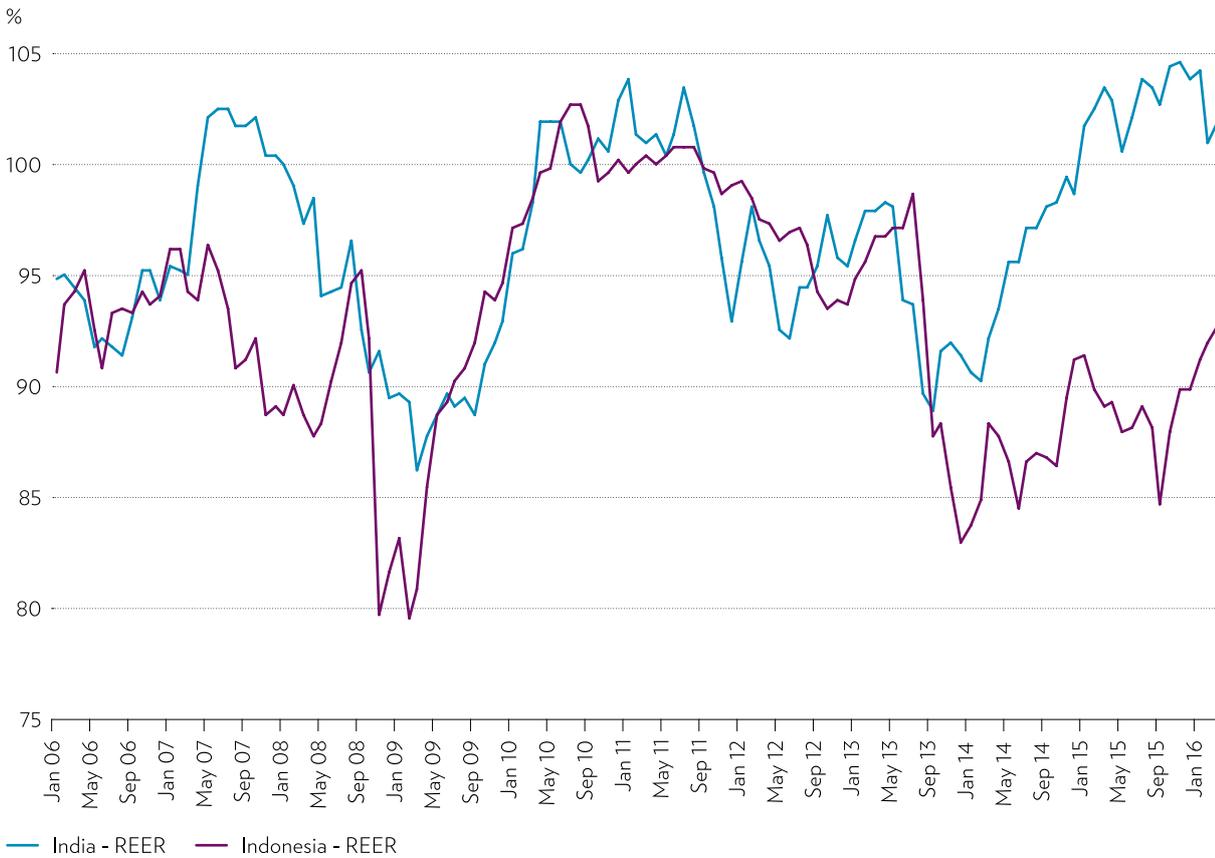
Indeed, Indonesia experienced the negative effects of huge and rapid entry of foreign capital from 2010 to 2012 which subsequently exited in 2013. However, this time it is not about portfolio flows but about direct investment inflows. The country is still proceeding only gradually on liberalising foreign ownership rules. In dollar terms, India has received more foreign direct investment (FDI) than Indonesia. However, as a share of GDP, Indonesia has received more FDI than India since 2010 (see chart 3). In real terms, the rupiah effective exchange rate is more competitive than that of the Indian rupee (see chart 4).

Chart 3: FDI inflows



Source: UNCTAD

Chart 4: Real Effective Exchange Rates (REER): rupiah is better off (2010=100)



Source: Bank for International Settlements

Barring a significant deterioration in external conditions, the outlook for Indonesia is moderately positive. The positives as mentioned include moderating inflation, stronger rupiah, pick-up in business sentiment and credit growth as well as higher spending on infrastructure investment by the

government. In addition, a number of economic reform packages, including the Tax Amnesty programme which recently came into force, have been implemented. These should help to support the currency and attract greater investment interest from both portfolio and FDI investors.

INDIA MACRO

India: Capitalising on macroeconomic stability

The medium term outlook for India is predicated on addressing a number of key structural challenges. Chief among these is to raise the level of investment, providing a supply side boost that will see India harness its enormous potential to the fullest extent. At the same time, examining inefficiencies in the power sector and taxation, in particular, would serve to lessen the burden of doing business and bolster fiscal institutions.

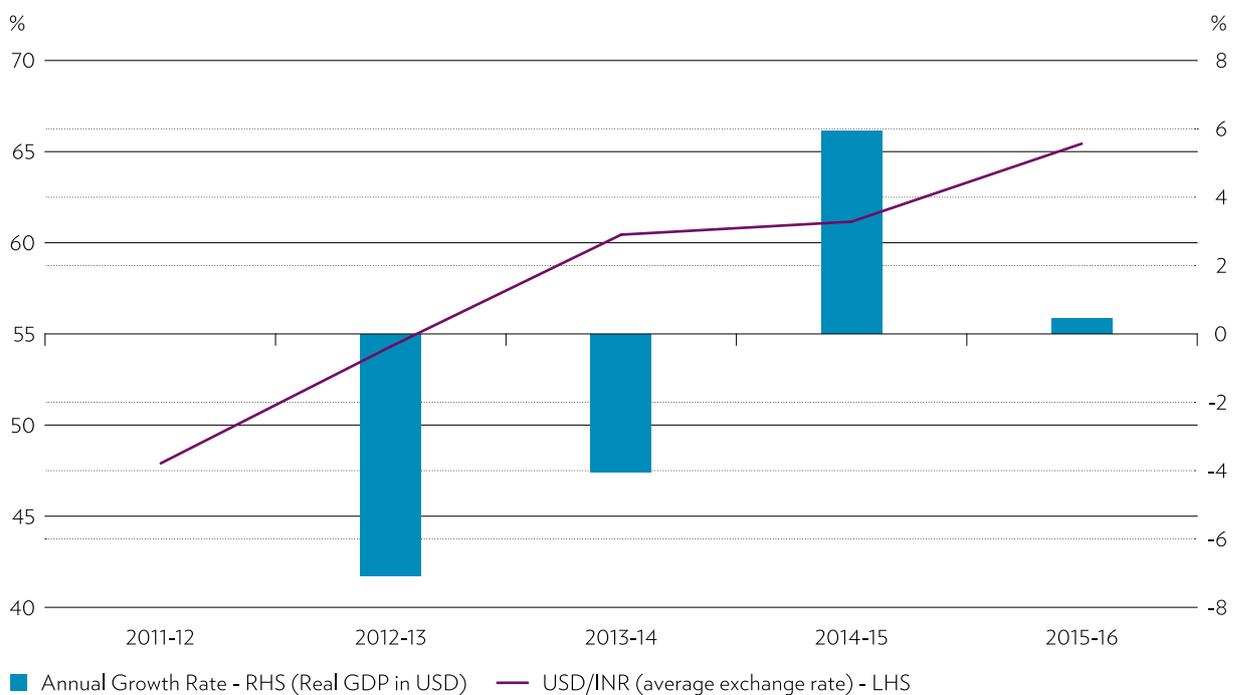
While not underestimating the work that lies ahead, important milestones are being reached, such as progress on sales taxes. Such efforts promise to lessen the drag on growth, which in

recent years, has arguably underwhelmed many observers.

Not firing on all cylinders

In dollar terms, India's GDP growth rates in the last few years has been rather modest. In the financial years 2012-13 and in 2013-14, India's real GDP in US dollar terms contracted 7% and 4% respectively (see chart 1). In 2014-15, thanks to the stability in the IND/USD exchange rate, India's real GDP growth in dollar terms was nearly 6.0%. Again, in 2015-16, GDP growth rate in US dollar terms is almost flat at 0.5%. The rupee price of the US dollar has gone up by nearly 40% from 2011-12 to 2015-16 (based on monthly average of USD/INR exchange rate).

Chart 1: India's real annual GDP growth rate in USD and USD/INR exchange rate



Source: Ministry of Statistics and Programme Implementation, Government of India, Julius Baer

In local currency terms, IMF forecasts Indian GDP growth at 7.5% for 2016–17 and 2017–18. The Reserve Bank of India (RBI) forecasts growth in ‘Gross Value Added’ (GVA) of 7.6% and 7.9% for these two years. If subsidies are added and indirect taxes are subtracted from GDP, one gets GVA. Since these two are considered government payments and receipts respectively, the emphasis is on GVA rather than on GDP. Indian GDP in nominal terms crossed the USD 2 trn mark in 2014–15. India’s financial year runs from April to March. As per IMF forecasts, among the major economies, India’s growth rate is expected to be the highest. For India, the scope for catch-up exists as its GDP crossed the USD 2 trn threshold only recently and in per capita terms, its GDP is lower than countries like China, Indonesia, Thailand and Malaysia.

The government has begun addressing many long-standing problems. At the same time, new challenges have cropped up. We will analyse India’s macro-economy in the light of the policy achievements in the two years that this government has been in office and policy challenges that lie ahead.

Public investment driving growth

Power sector reforms

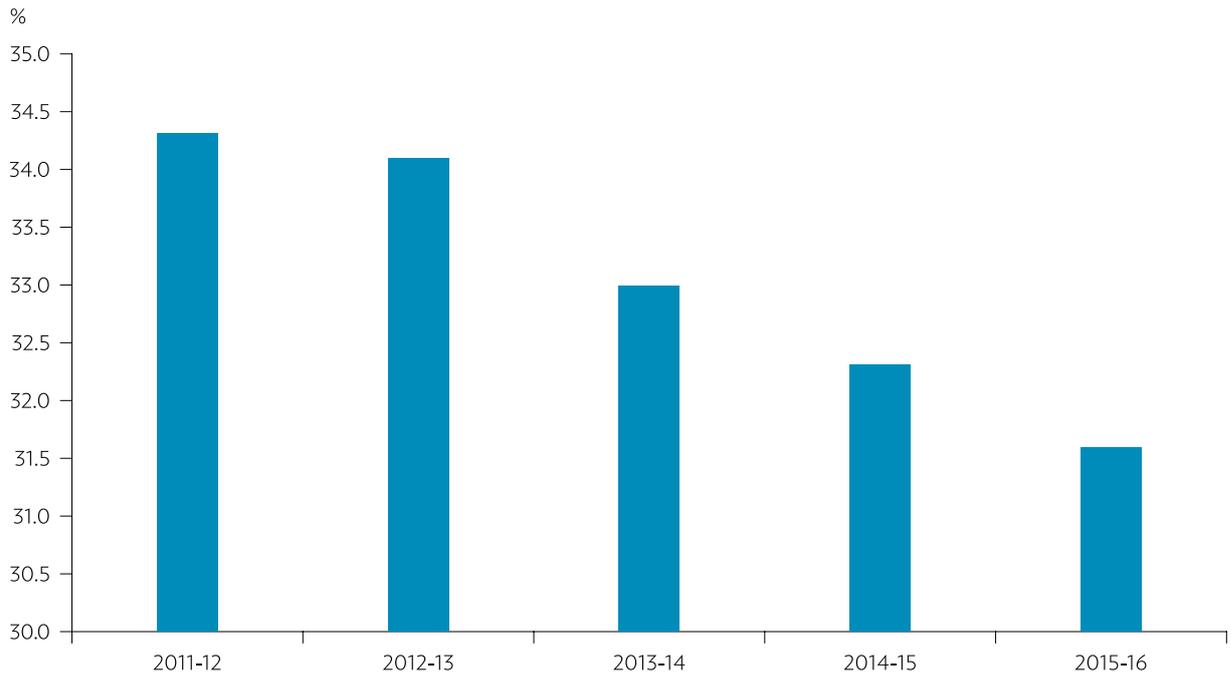
Electricity, roads and water are the key concerns of an average Indian. This government is working on providing all Indians electricity 24/7 through multiple fronts. They are providing lighting to villages, they are replacing halogen lamps with LED lighting and thus saving hugely on power consumption and they have come up with an incentive (carrot-and-stick) scheme ‘UDAY’ (which means the dawn in Hindi) to make the state-run electrical utilities transfer their losses to the State government budgets.

Government-owned and managed utilities have incurred losses because they have chosen to distribute power free to farmers. Meanwhile, they have arguably undercharged households and overcharged industries for electricity consumption, which has caused the latter back out of the distribution and generate captive power. Nor are they able to buy power produced by independent power producers. India had enabled power generation in the private sector. However, distribution remains in the hands of the state-run utilities that are hobbled by losses. The new government’s scheme UDAY is meant to address many problems that are intertwined.

Utilities’ balance sheets will improve under the scheme. Banks’ loans lent to utilities that are not performing will be replaced by state-guaranteed bonds. Power producers will benefit as utilities will buy power from them again. States will have to provide for electricity subsidy explicitly, going forward, if they wish to sell electricity below economic rates. Lastly, if States continued to avoid taking responsibility for their subsidies, then their borrowing limits might be reduced.

Making up for private investment slack

India’s growth is driven by public investment in roads, railways, ports and energy whereas private investment spending is not picking up. Gross fixed capital formation (GFCF) is estimated to have grown at 3.6% in nominal terms in 2015–16 and 5.3% in real terms, indicating that there is deflation in the prices of equipment. As share of GDP, GFCF has declined steadily from 34.3% in 2011–12 to 31.6% in 2015–16.

Chart 2: Ratio of gross fixed capital formation to GDP at constant 2011–12 prices

Source: Ministry of Statistics and Programme Implementation, Government of India, Julius Baer

The government has continued to build roads at a fast pace. Road construction picked up pace in 2014–15. 36,000 kms of new rural roads were added in 2014–15, about 11,000 kms more than in the previous year. 8,000 kms of highways were added in 2014–15 compared to only 3,500 kms in the year before. Out of the target of 10,000 kms for 2015–16, about 76% was achieved in the financial year 2015–16.

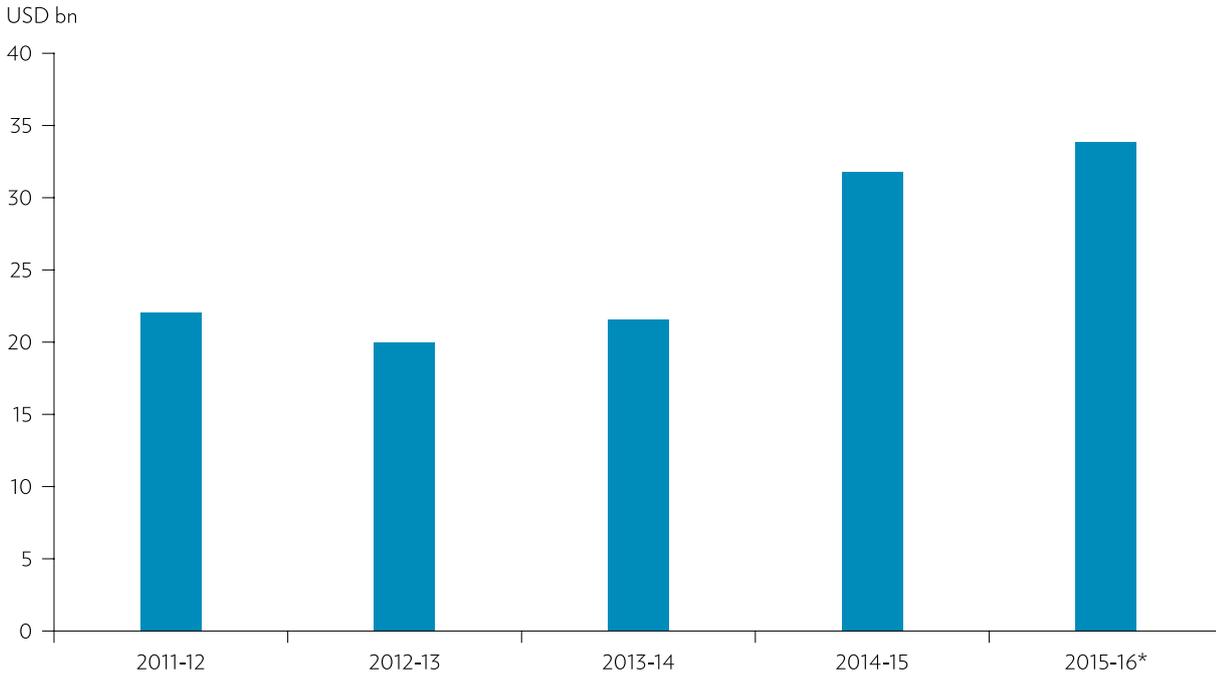
It is a matter of debate, however in India's case, the urgent need for infrastructure and other investment should be the focus of policy making, avoiding outcomes that purely generate asset inflation.

The government has also announced a comprehensive Hydrocarbon Exploration and Licensing Policy (HELP) which has helped remove policy uncertainties. License fees will be based on revenues and not on profits. Oil companies can apply to take up exploration fields not already covered by exploration. Following this, the fields will be put up for auction by the government, in which the bidder offering the highest share in revenue to the

government will get it. In other words, they do not have to wait for the government to offer the fields for exploration. They can initiate action at their end. It might draw in foreign investor interest especially if the persisting uncertainty over tax claims based on a retrospective tax law is removed. This government has not yet repealed the law brought in by the previous government that renders firms liable to taxes on income or capital gains that would have been exempt from tax under laws prevailing then. It has pledged not to make fresh retrospective tax claims but the pending legal disputes are still winding their way through international arbitration and that indeed is an overhang on rising investment interest.

Yet, India has been successful in recent years – especially since the Modi government came to office – in picking up FDI. Net FDI – as per Balance of Payment statistics of the Reserve Bank of India (RBI) – was USD 33.7 bn in the first nine months of 2015–16, higher than USD 31.6 bn received in the whole of 2014–15 (see chart 3).

Chart 3: Net FDI inflows into India



* Data for 2015–16 are only for nine months from April 2015 to December 2015.

Source: Reserve Bank of India

Monetary policy and investment revival

India’s monetary policy has become increasingly accommodative in the last two years. When Raghuram Rajan took over as the RBI Governor, the policy rate was 7.5%. It was raised to 8.0% in the first few months of his term. From January 2014, it has been declining and now stands at 6.5%¹. In real terms, the policy rate has increased. The trailing 12-month inflation rate in January 2014 was 9.7%. The policy rate then was 8.0%. Hence, the real rate was -1.7%. Now, the policy rate is 6.5% and the inflation rate as of May 2016 is 5.8%. The current real policy interest rate is +0.7%. It has swung 2.4% in the last two years. Has it held back investment?

The answer is not straightforward. Firstly, the real rate of interest has ensured exchange rate stability. Secondly, the growth rate of the economy has improved gradually in the last two years from 6.6% to 7.6%. Yet, the rupee has depreciated steadily, against the US dollar. In other words, RBI had not allowed financial conditions to become too tight with interest rates and currency, both being stronger. M3 growth rate is somewhat low at 10.7%. In a balance sheet constrained environment, low interest rates stoke speculative investment in real estate and stock markets rather than in real assets that generate employment. It is a matter of debate, however in India’s case, the urgent need for infrastructure and other investment should be the focus of policy making, avoiding outcomes that purely generate asset inflation.

¹ Source: Bloomberg Finance L.P.

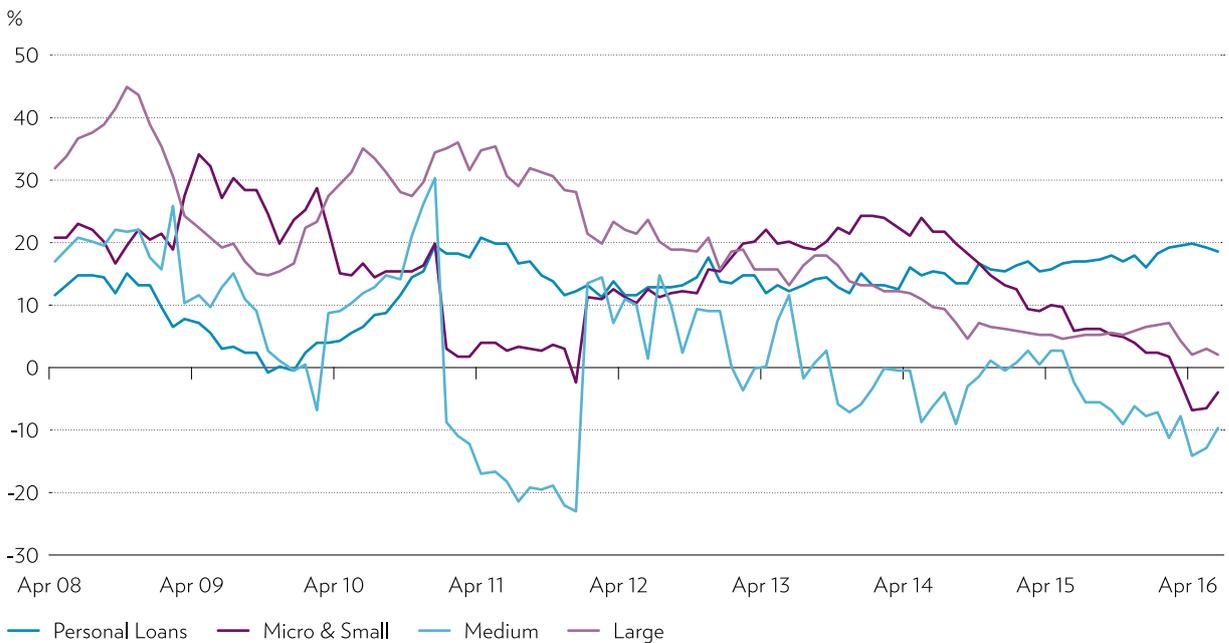
India has a balance sheet challenge. Both its banks and its large corporate borrowers have strained balance sheets. According to the June 2016 report on financial stability published by RBI, the percentage of stressed assets of the Indian banking system was 11.5%. The figure for government-owned banks was higher at 14.5%.

Indian corporations, on their part, have a high debt – equity ratio. Business expansion funded by debt has backfired as global and Indian growth stuttered. Excess capacities in China have arguably seen downward price pressure on steel worldwide. However, with the government and RBI prodding the banks to clean up their balance sheets, the situation is likely to improve. International media has begun to

acknowledge the early signs of problem resolution². Of course, if growth accelerates, asset sale of corporations will become easier and even non-performing bank assets could become regular.

In the budget for 2016–17, the government had earmarked INR 250 bn for bank recapitalisation (around USD 3.6 bn). The first instalment of that recapitalisation should take place fairly soon. However, until the balance sheets of both lenders and borrowers improve, credit growth would remain sluggish. Bank loans to micro, small and medium enterprises are contracting. Credit to large enterprises is growing but the growth rate has slowed sharply from around 7.0% y/y in January to just over 3.0% in May (see chart 4).

Chart 4: Non-food bank credit growth



Source: Reserve Bank of India

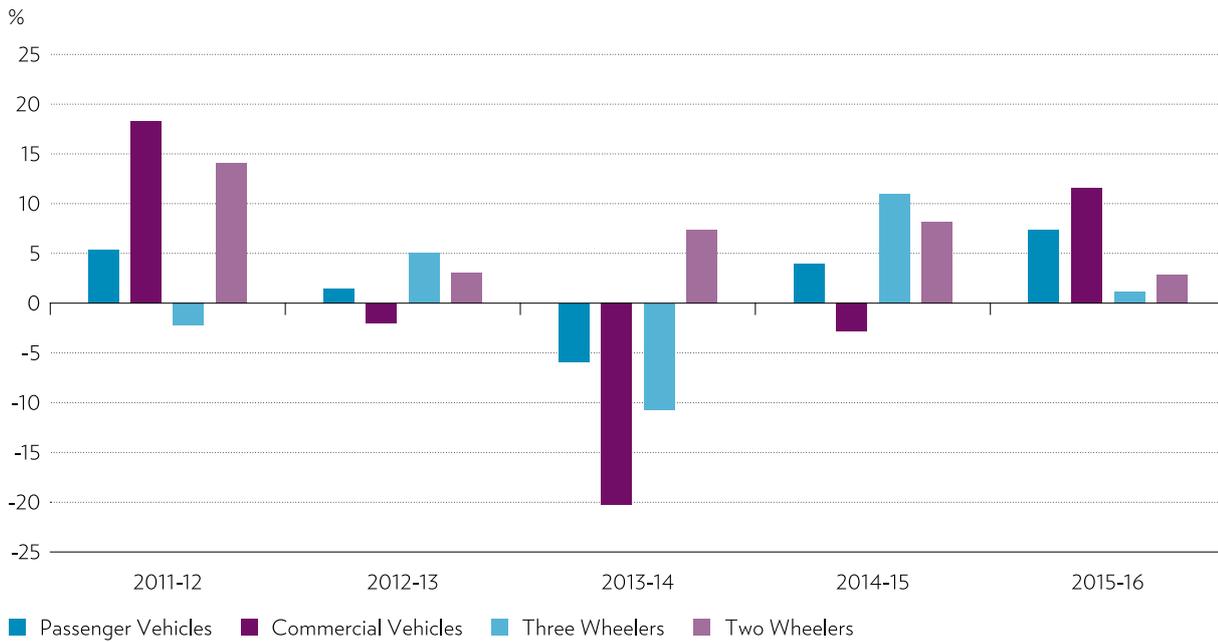
Concluding remarks

For the most part, after two years of a hesitant recovery from the bottom of 2013–14, the conditions for an accelerated economic growth in India are in place. There is a serious attempt to make electricity and road connectivity a reality for all Indians.

Consumer spending is holding up. Household balance sheets are strong. It is evident in the improvement in automobile sales (see chart 5) and in the number of registered GSM mobile phone users (see chart 6). Personal credit growth is strong at 19% y/y, as seen in the chart above on bank credit growth.

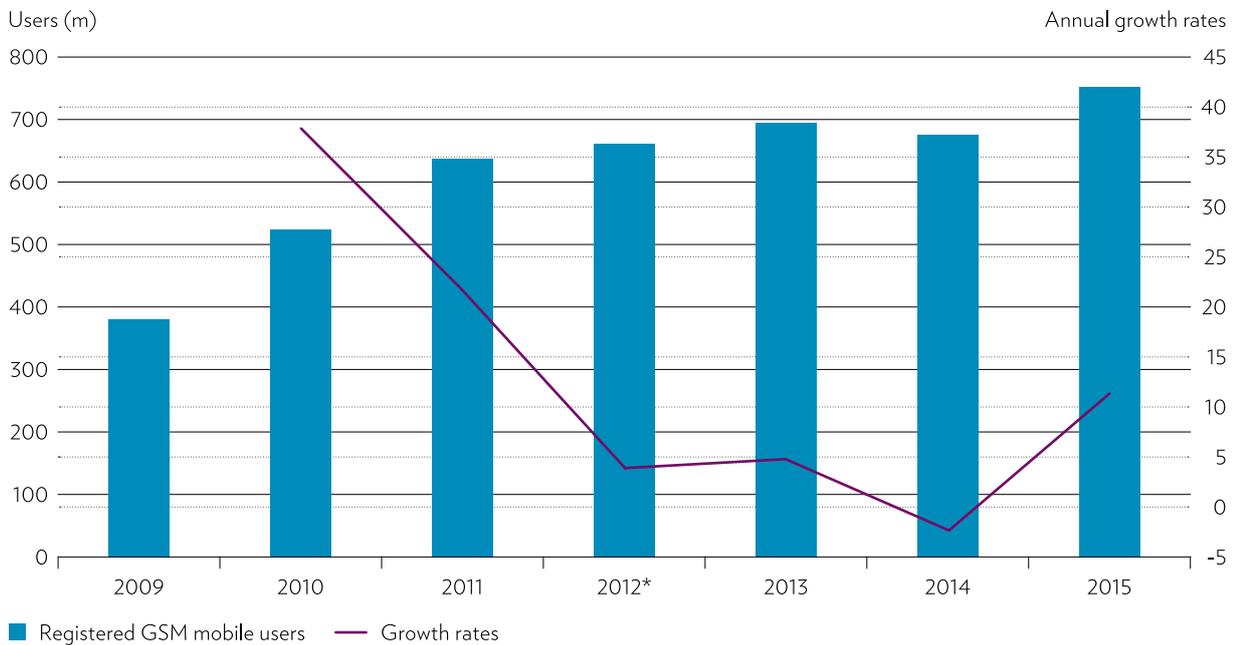
² 'India's banks face up to corporate debt problems', Financial Times, 20 April 2016

Chart 5: Domestic vehicle sales trends



Source: Society of Indian Automobile Manufacturers and media reports (only for 2015–16 figures)

Chart 6: Registered GSM mobile users



* Data only up to November as December data was erroneous.

Source: Cellular Operators Association of India

One of the main risks that India faces is water. India has had two back-to-back deficient monsoon seasons in 2014–15 and in 2015–16. Production of foodgrains has stagnated whereas oil seeds production has declined (see chart 7). In the calendar year 2016,

summer set in early in April and water storage in reservoirs declined. There was drought in ten States and the affected people exceed 300 million. However, offsetting these concerns, the Meteorology Department predicted an ‘above-normal’ monsoon.

Chart 7: Agricultural production



Source: Office of the Economic Advisor, Department of Industrial Policy and Promotion, Government of India.

Much of the anticipated acceleration in economic growth depends on this forecast being realised. Six weeks into the monsoon season that started in June, the monsoon has gathered strength and large parts of India have received normal to excess rainfall. If the trend persists for the second half of the monsoon, it should augur well for rural demand and business confidence. It would matter as much to confidence as to economic growth and, indeed, it might play a very big role in the re-election prospect of this government as it enters the crucial second half of its tenure in the course of the current financial year 2016-17.

An above-average monsoon and continued sluggish global demand for crude oil that will hold oil prices down should set the stage. Further acceleration would depend on free flow of bank credit to industries, consequent investment and employment generation and the creation of a single national market through the implementation of a national Goods and Services Tax. Then, India will have to ensure that there is no recurrence of the familiar overheating of the economy

marked by rising and high inflation, currency overvaluation and current account deficit.

There is greater uncertainty than before on the outlook for the global economy in the coming years. That would strain bank balance sheets and hurt capital market sentiment globally. India would suffer spillover effects. Export growth would be adversely affected but it is already hurting anyway. The incremental impact will be marginal. On the positive side, a global slowdown and market correction or crash would cause oil price to decline. That is important for India. Hence, on balance, India may not be much worse off from global developments.

India's record with short-term growth spurts leaves ample room for caution. They are usually followed by macroeconomic imbalances and a steep fall in the rupee. The government has to do all it can, to avoid a recurrence of that. Subject to that important caveat, it is fair to say that India is looking ahead to 2016-17 with cautious optimism – more optimism and less caution.

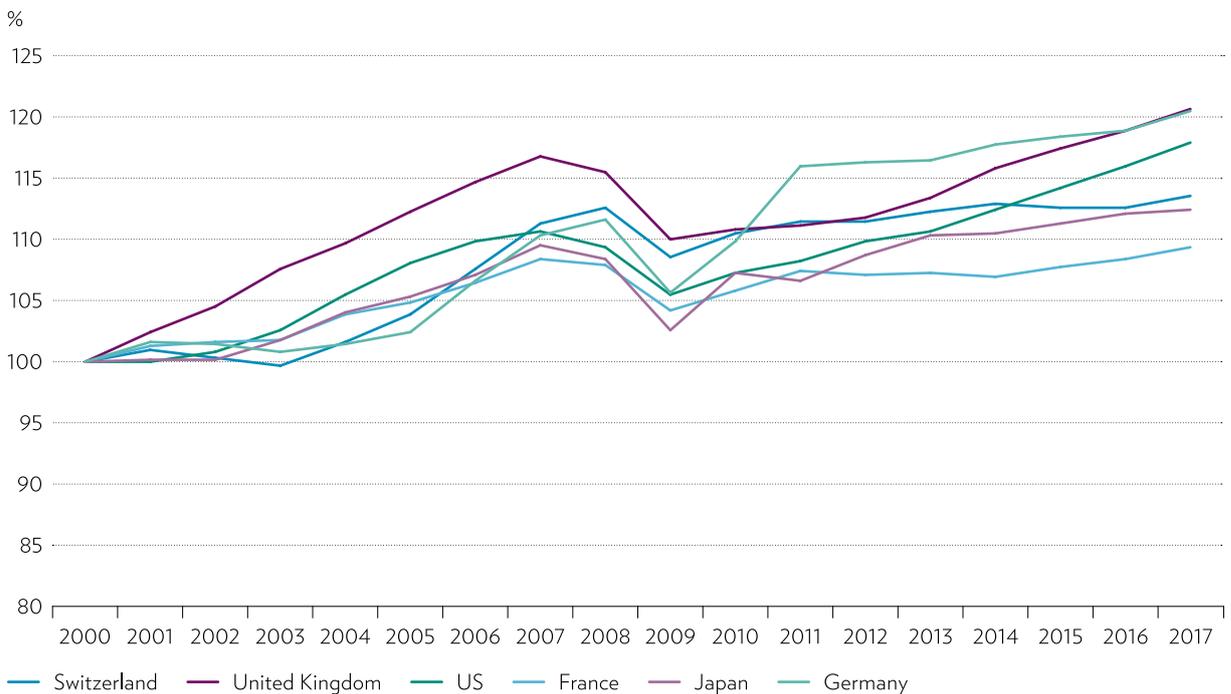


JAPAN MACRO

Over the past five years, Japan’s population has declined by over one million. At the same time, however, per capita income has risen by approximately USD 2,000. These two facts illustrate how Japan’s economy continues to push policy makers, academics and analysts in coming to terms of what ‘needs to be done’ to ‘fix’ a myriad of unique challenges. An ageing population arguably contributes to a natural deflationary drag as lack of meaningful immigration and a shrinking labour force tends to pull down prices. However deflation preserves the purchasing power

of cash, which represents over 40% of the asset allocation of households. High levels of government debt are in stark contrast to low household borrowings and ample savings in the corporate sector. Put differently, despite the often discussed malaise that Japan’s economy seems to be laboring under, the reality is that there are robust counter arguments against this at almost every turn. The most straight forward of all is perhaps that income per head growth in Japan has kept pace with Switzerland over the past 15 years, and exceeded that of France.

Chart 1: Per capita GDP (in local currency) indexed to 2,000

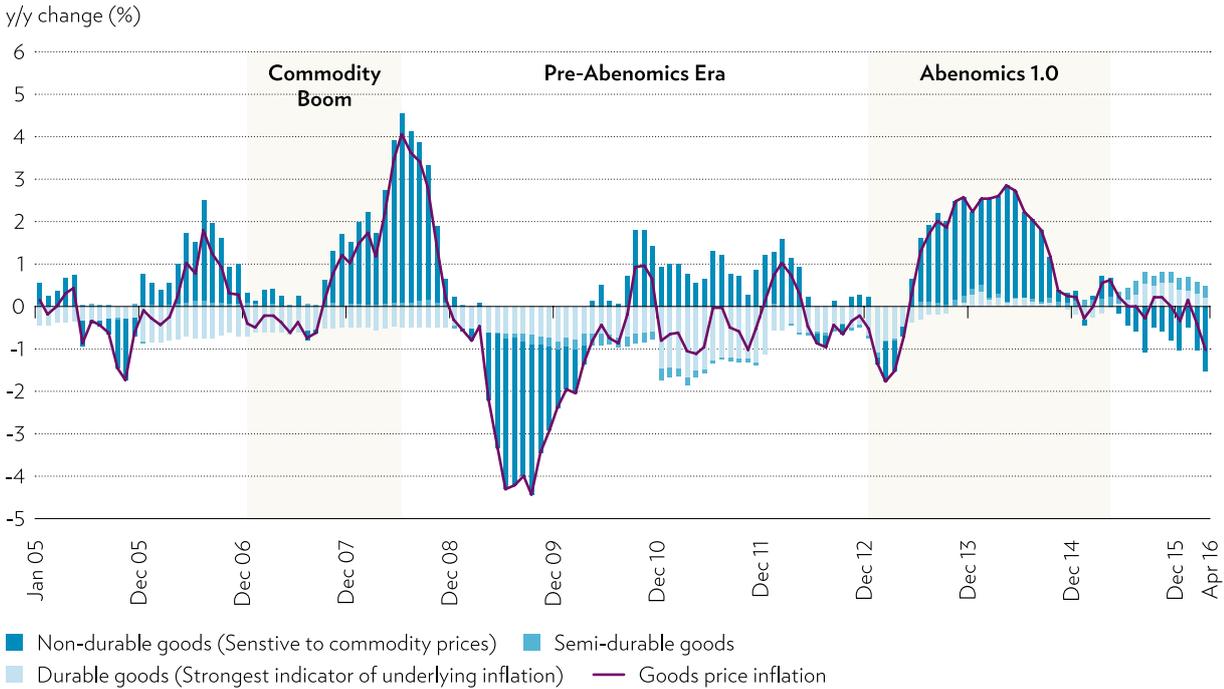


Source: IMF, Julius Baer

Nevertheless, the Abe government launched a series of fiscal, monetary and structural measures in late 2012 to great acclaim, dedicated to overcoming deflation and boosting national income. One core tenant of these policies was the central role to be played by a competitive devaluation of the yen.

Detractors of these efforts, collectively labeled as ‘Abenomics’, point to the limited success in lifting durable goods inflation, as well as the perceived caution on the part of both households and the corporate sector to boost spending.

Chart 2: Contribution to Japan’s goods inflation



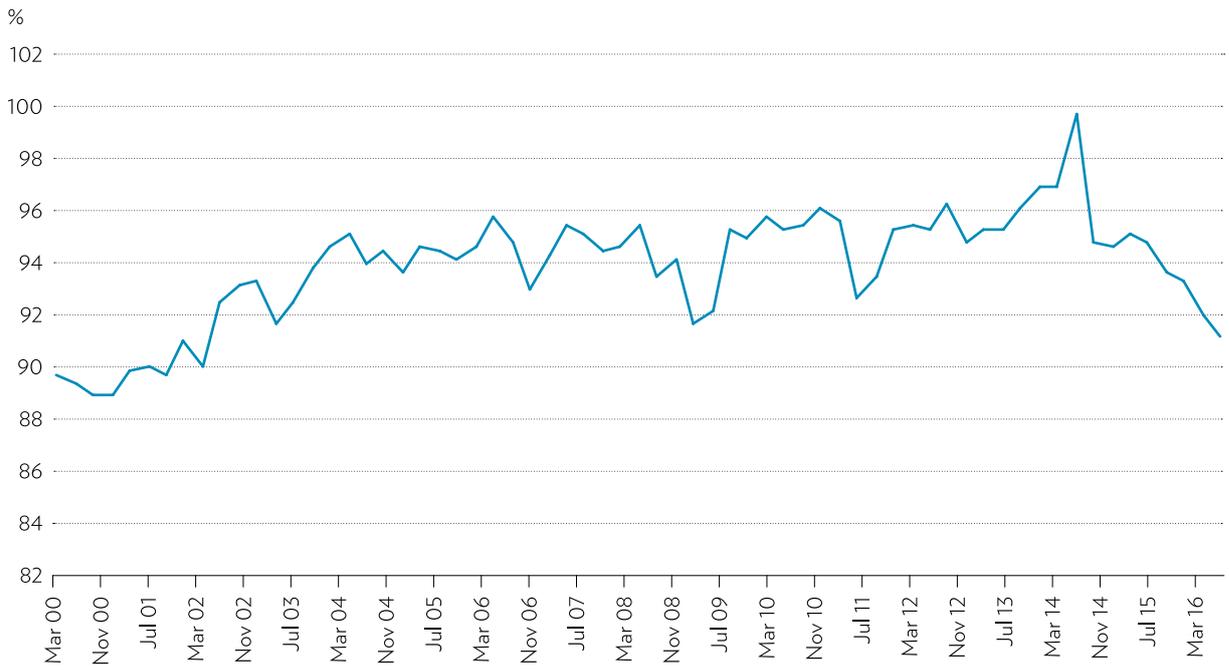
Source: HSBC, Julius Baer

To be fair, during the course of the Abenomics programme, the government lifted consumption taxes in a bid to shore up its long term fiscal outlook. With net government debt at over 130% of GDP, few would argue that measures are not needed to restore Japan’s fiscal path to a more solid footing. However, in the wake of the April 2014 tax hike, consumption appears to have moved sideways. To add insult to injury, in the wake of heightened international political risk over the course of 2016, the yen assumed its traditional function of being a safe haven asset, undermining the BoJ’s concerted efforts to support a depreciation bias in the currency.

That said, the Japanese economy has undergone rapid change, both in connection with Abenomics and arguably separate to it. For example, while aggregate consumption statistics imply that very little has

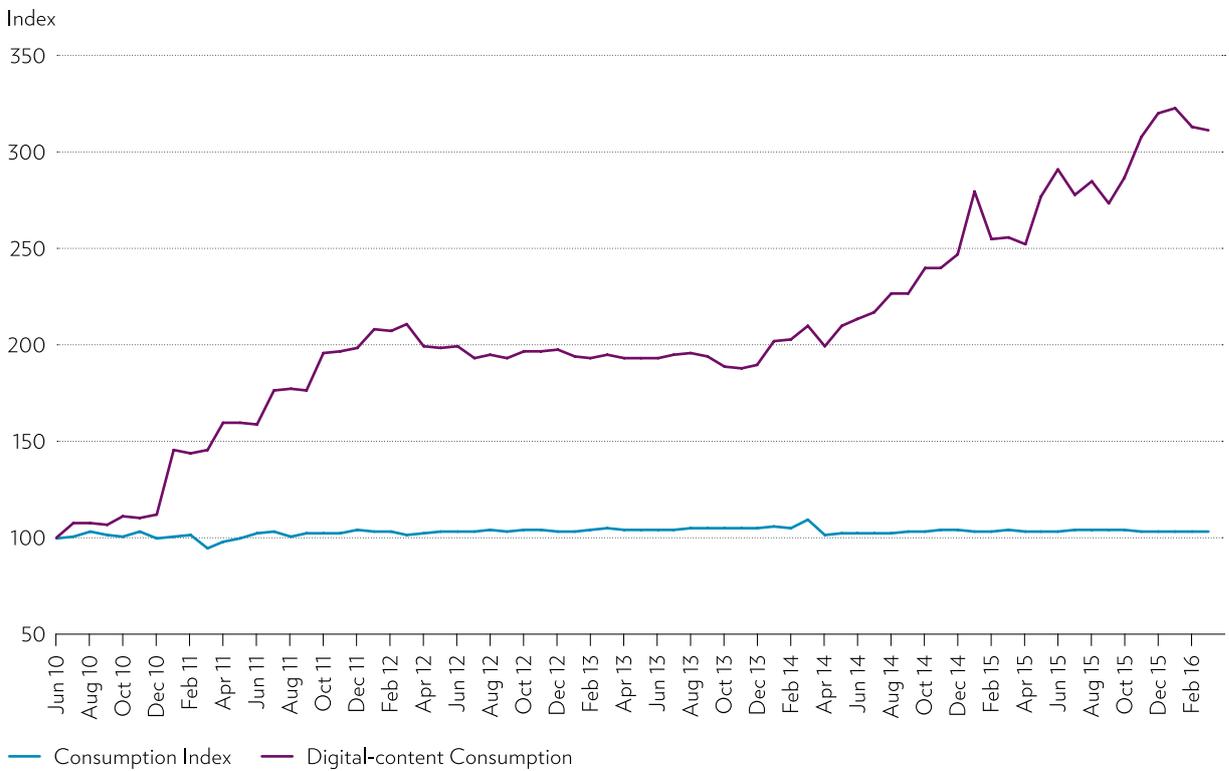
changed in recent years, the way that consumers are engaging with the economy has changed significantly. In this regard, internet-driven sales have grown at a rapid pace, suggesting what we see in overall consumption numbers is a blend of a cautious consumer sentiment and a radical shift to online retailing. This speaks of a much broader global phenomenon which faces off the legacy of bricks and mortar points of sale versus a world that is largely mobile and where consumers rely on their smartphones and tablets to do a lot of what they did in the past. This does not change the outcome that the propensity to consume has not moved higher in a material way; households and the corporate sector do not appear confident enough yet to shift their stockpile of savings into spending or investing, but it is equally wrong to argue that consumption in itself is not dynamic.

Chart 3: Japan's propensity to consume: consumption as a percentage of compensation



Source: Japan Cabinet Office, JP Morgan, Julius Baer

Chart 4: Japan's consumption indices



Source: Bloomberg Finance L.P., Julius Baer

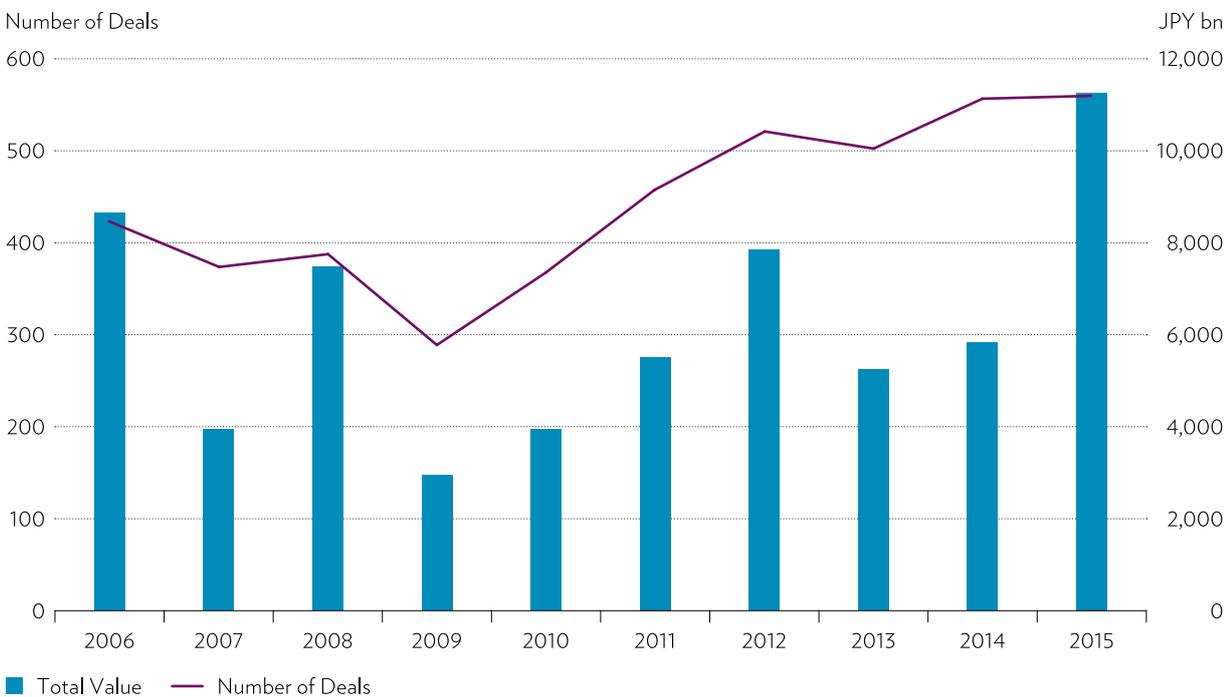
The great debate in Japan over the coming quarters will centre on how to achieve a second wind for Abenomics. Having accomplished an important milestone in its fiscal consolidation and reaped benefits of earlier yen depreciation, the question is invariably down to ‘what next?’

Our view is that policy makers will closely examine the merits of what is termed ‘overt money financing of government deficits’, a.k.a ‘helicopter money’, but ultimately elect not to go down this path. At first glance, it can be argued that both negative interest rates and asset purchase programmes by the BoJ have had a material impact on raising inflation expectations. While this may be the case, it does not automatically follow that helicopter money is the next natural step for the Bank of Japan to take. This is for two reasons: one, the Japanese public is well aware of the extremely high cost of similar undertaking that occurred in the 1930s, equivalent to the oft mentioned German aversion to unconventional monetary policies owing to memories of hyperinflation

in its own past. Second, it may not be technically possible for the Bank of Japan to execute helicopter money without incurring costs for the Finance Ministry, thereby negating the benefits of this strategy in the first place.

In any event, a move to helicopter money would likely be preceded by a period of further negative interest rates and asset buying that could last years. What we image is more likely is that Japan is likely to be forced to persevere through a complicated 2016–17 period, where external factor such as uncertainty over China’s policy mix, the risk of global protectionism and the rise of populism conspire to keep the yen strong. In the shorter term, yen strength will likely see an acceleration of outbound merger and mergers acquisitions (M&A), which has been somewhat neglected in recent years. This means that corporate Japan may end up using the ‘opportunity’ of a stalled Abenomics to gain access to growth markets and customers overseas.

Chart 5: Overseas M&A deals and value



Source: UBS Investment Bank, Julius Baer

We examine the topic of overseas investment opportunities for Japanese companies in the following

section, highlighting an entrepreneur in the dynamic field of Internet security.

NEXT GENERATION ENTREPRENEURS

INTRODUCTION

Mr. Amit Lohia
Group Managing Director, Indorama Corporation

Mr. Amit Lohia is a third generation entrepreneur and Group Managing Director of Indorama Corporation since 2004. Indorama was founded in 1975 by Mr. Lohia's father S.P., and has grown today to become a global manufacturer of a variety of industrial products with over 28,000 employees globally. The company has grown and expanded across the years successfully into several overseas markets in North America, Africa & Europe with a number of greenfield and acquisition projects spearheaded by Mr. Lohia himself.

In this exclusive interview, we get insights from Mr. Lohia about leadership and entrepreneurship in Asia, the influence of his Indian heritage and his views on the challenges and opportunities ahead.



In lieu of what is happening in the world today, how optimistic or worried are you about the current economic environment?

I think there are two aspects to consider: the real economy – which is what our organisation is concerned with as a manufacturer – is still doing fine. In our case, we make products which are used ultimately in day-to-day fast moving consumer goods such as diapers, car-related products, healthcare, wellness and beauty products like cosmetics, and also food fertilisers. The consumption and demand for these still hold strong so our core business is holding up well and I'm fairly optimistic that it will continue to be so in the near future.

I think the financial markets are probably showing more nervousness than I see in our core business. In terms of a macro scenario, we are now in a new paradigm of lower and slower global growth. While we knew this was inevitable and had to come, yet when it came, it still hit us hard and everyone is now getting accustomed to this era of slower growth.

How do you view the monetary and fiscal policies that have been introduced over the past few years? Has the business environment become more certain or do you think it has become riskier?

What affects us directly in our business and our investments are interest rates. I think the low interest rates of the past several years have done their job in most parts, but going forward, I don't think we can bank on it too much more. It has served its purpose and we need to move on and not depend on it too much to save the economy.

At the same time, I don't foresee rates nor inflation to go up too much. Everyone understands and recognises that rapid rising interest rates will do more harm than good – not just for corporations and individuals, but even for governments with high level of debts. It is in nobody's interest to raise rates. Inflation should also remain fairly under control.

How do you view the Asian economy right now and in the foreseeable future?

Asia continues to be important as an economic region for the world and it is also a key part of our business portfolio. While we focus more on organic growth in this region specifically for our business in Southeast Asia, a lot of our assets in China were possible due to the acquisitions we made. When we do M&A acquisitions in the Americas or in Europe, we often acquire their operations and assets in Asia, particularly in China where we have seen strong growth in the country.

Is innovation a key area of focus in your business?

Innovation is actually something we think about a lot internally, and we try to imbue it as part of our corporate culture. I am of the view that innovation should not be compartmentalised as a function in a company and it is key to have all employees think and exercise innovation in their respective functions.

Innovation is not the sole responsibility of the R&D team and it is, in fact, a journey that should be followed collectively by all in the company. It takes time and has to be implemented both at a top-down and bottoms-up approach.

In our company, all business managers demonstrate innovation by spearheading special projects and we have seen that such participation has helped foster the spirit of innovation within our organisation. For example, one which I personally lead is an information-sharing platform likened to a social media sharing platform which we hope will make sharing and learning of information and best practices – a fun, interactive and informative experience.

How do you keep your entrepreneurial spirit sharp when it comes to managing your business?

I believe in the importance of being hands-on yet not micro-managing. It may be a balancing act but it can be done. We practise this in our company where senior managers are hands-on in their respective area but yet empower junior managers sufficiently without being stifling.

We also have to reward entrepreneurial spirit and behaviour and that is also something we try to do. We encourage employees to take on projects and assume the role of a project leader. As the project leader, they are given the autonomy of running the project akin to running their own business; having a proper business case, project plan and managing risks and budgets.

As a successful Global Indian, what do you see as the strengths and weaknesses of the Indian economy?

India is very entrepreneurial as a nation, aided particularly by its large population and rising middle class. Prime Minister Modi's 'Make in India' initiative seems to be pushing the right buttons and sending a strong positive signal and all these can only bode well for the country to cement its position as a leading economy of the world. In terms of challenges, the high interest rates observed will impact growth for the country. I am also of the opinion that prudent financial discipline can be better in many Indian organisations.

Would you say your Indian heritage has influenced your views and practices both personally and professionally?

I come from a traditional Indian family and our business remains primarily family-owned, so in this aspect, our corporate culture is still very much family-oriented. It is a seemingly simple concept but yet very powerful notion. We believe in taking care of each other and this applies not only to our family relationships but it also extends to our company where every employee in our organisation is part of the family.

My father built the company and led it to its success and preserving our family legacy is very important to us and ensuring the preservation of our business for the next generation is part of our DNA. We promote values such as hard work, dedication, commitment, and loyalty in our family as well as in our company culture.

What is your management philosophy? How are you like as a leader?

While I can be very empirical and I love data, I am on the other hand very easy going and believe in the power of delegation. I am more risk averse than my father but I believe we have been well-balanced in our investment decisions.

When I joined Indorama (as my first job), I learned as much as I could from my father in managing the business and now that I have taken over the day-to-day running of the operations, one common trait we still share is our people-oriented approach which is still very much evident in our company culture to date.

INTRODUCTION

Mr. Wu Xinhong
Co-founder and Chief Executive Officer, Meitu, Inc.

Mr. Wu Xinhong is co-founder and CEO of Meitu, Inc. which was established in 2008. After three years of idea conceptualisation, Meitu launched its first mobile app on 14 February 2011. Since then, riding on the exponential growth of smartphone users in China, Meitu's suite of apps, which include MeituPic and BeautyPlus, have been activated on more than 1.1 billion unique smartphones.

Mr. Wu believes Meitu's growth opportunities are still abundant in the global scene. Currently, more than 80% of Meitu's users come from the Greater China region. Developing countries such as Indonesia and India are at the top of his list to expand Meitu's presence as market saturation and intense competition in developed nations limit growth opportunities.

We sit down for an exclusive interview with Mr. Wu to discuss the opportunities and challenges for aspiring entrepreneurs in China.



What are the biggest challenges (obstacles) you've encountered while building Meitu? How have you tackled them?

The first major challenge we have encountered was between 2008 and 2010, when Meitu planned to launch the mobile version of MeituPic (called Meitu Xiuxiu in China). iPhone 1 was released in 2007. We realised that smartphones were becoming a mega-trend. However, we could not find engineers specialised in iOS and Android development, as Meitu is located in Xiamen, a city with a relatively small talent pool. Therefore, the mobile version of MeituPic has remained an idea for over two years. MeituPic's first mobile version was officially launched on 14 February 2011, the Valentines' Day. From idea conceptualisation in 2009 to the official launch in 2011, it took us three years. Luckily, the smartphone has remained a niche market product until 2011.

In 2011, smartphone users grew exponentially. Meitu grabbed and leveraged on this opportunity. Nevertheless, we believe that it could have turned out to be even better if the product had been launched earlier, since optimal user experience could only be achieved through constant product optimisation and upgrade.

The second challenge we face is the current one, that is, migrating the Meitu suite of apps into platform and materialise the commercialisation of our product chain.

Over the next five years, what do you expect to be the key opportunities and challenges facing your business?

In the next five years, a big opportunity not to be missed by Meitu is the rising of the post-00s generation, such as those born from 2000 to 2009. We have leveraged on the opportunity when the post-90s users became the mainstream. Likewise, we have to leverage on the rising of the post-00s generation. Another opportunity not to be missed is the exponential growth of online videos and the boom of user generated content (UGC). Previously, Youku Inc., (formerly known as Youku.com) and iQIYI.com operated more or less like online TV stations in China, streaming professionally produced videos they had procured. UGC is gaining traction in China, e.g. Papi Jiang ('papi 酱'), the most viewed video blogs produced by a talented Chinese video blogger Jiang Yilei, is a typical example of UGC. Previously people doubted whether this type of content would be popular among online viewers, whereas nowadays the younger generation enjoys watching videos produced by their peers. The growth of smartphone users between 2008 and 2015 brought about the explosive growth of visual content. We see 2015 as a turning point when online video started to gain traction. We see substantial growth potential for online videos, including UGC and live stream, both of which use video as media. Meipai, the video editing app launched by Meitu in 2014, also uses video as media.

What products have Meitu launched globally? Has Meitu initiated internationalisation procedures?

We have successfully launched some products globally. BeautyPlus, the global version of BeautyCam (called 美颜相机 in Chinese), is used by over 100 million users globally. India is one of Meitu's biggest overseas markets. Meitu's applications are popular among Japanese users too. Step by step, we will launch the global version of all major products. We have set up offices in seven countries and regions outside China, namely Brazil, Hong Kong, Singapore, India, Indonesia, Japan and the US. The overseas representative offices focus on products localisation and business development.

What makes Meitu stand out from its peers?

We pay great attention to young users and value their need and preference. As students, they think and behave differently from the rest of us who have joined the workforce. Back in 2007, I developed a Martian Translator, many of its users were post 90s who were considered the 'non-mainstream' then. In 2008, we launched MeituPic, targeting young users who were born after the 1990s. Today, we see the boom in demand from the post-00 users who are to turn into the mainstream. Therefore, we value their need and preference.

What is the key message from your experience that you want to share with aspiring entrepreneurs?

I would think of two terms which are of crucial importance to me: one is 'unpredictable' and the other is 'anatta'. In an ever-evolving marketplace with ever-changing user demographics, we need to be open-minded and flexible to embrace all the changes. Entrepreneurs need to embrace the changes with a positive mind-set, since changes might be good or bad. When you are running a business, you tend to be self-centred and make decisions by yourself. However, as the company grows, personal influence and energy is not enough to ensure effective communication with each and every person, therefore, there's a need for decentralisation in order to ensure effective communication within the company. 'Anatta', or selfless, can make you see things from others' perspective, for example, that of the users, colleagues or partners. These two points are really important.

The future development of Meitu cannot solely rely on my own efforts. I need to step back, and transform Meitu into a platform and consequently it would enter into an elevated platform which requires more support. I hope that products can be made efficiently, with each colleague doing their own job. The products are handled by their own project teams. Given my experience, I am able to provide more support to this platform, helping each person to unleash their potential.

As a successful Chinese technopreneur, what do you see as the opportunities and challenges in the current market environment in China? Do you feel the current market environment in China is supportive for young entrepreneurs like you?

A huge opportunity has arisen in China at the moment—the state is encouraging entrepreneurship and innovation. This is an extremely good thing. It has been more than 15 years since I started my own business. We saw unprecedented level of support for innovation from the government. You will find that the entire chain is increasingly improved and becoming more mature, which is a fantastic historical opportunity. China's Internet industry is booming, which renders a great help to entrepreneurs. In the past, it was pretty difficult for a product to reach out to 1 billion users within a day. However, now with WeChat, good things can go viral instantly. It might be a fun game, or a good film. Good things can become a hit and make headline instantly, which means that in a very mature market, as long as you can come out with a good product, you then have the leverage to quickly reach out to more users in a well-established platform. It's not like before when products lacked distribution channels.

What challenges are there in the current market?

At present, some oligarchies have already formed in China. If one has not joined their system, it is very hard to quickly get the needed resources. In China, we have magnates like BAT (Baidu, Alibaba and Tencent). Their presence is seen in almost every arena. This could turn out to be quite a challenge for start-ups.

INTRODUCTION

Mr. Toshio Dogu
Founder and Chief Executive Officer, Digital Arts Inc.

As a founder and chief executive of IT company Digital Arts, Toshio Dogu is on the forefront of meeting Japan's evolving digital security needs. Established in 1995, it now targets providing Internet security solutions for smartphones, building upon its established business of IT security for corporations. Spearheading an international expansion, Digital Arts is taking its 'Made in Japan' technology to new markets and adapting its product range as security needs increase rapidly on the back of new portable services.

Social responsibility is a hallmark of Digital Arts, as many of its products help to filter content and make devices safer for all to use.

In the next pages, Dogu-san explains to us how his approach to being an entrepreneur has changed over time and what his vision for the future is.



What do you do to keep the entrepreneurial focus sharp in a your company?

As an entrepreneur, I take the similar perspective that parents have towards their children. Consequently, it is vital for me to protect my child (company), see it grow and succeed in society overall. This is arguably different from a manager who is not an owner at the same time. While important, I do not concern myself solely with sustaining high profile margins or creating a well-known brand. Rather, my higher goal is to work towards keeping the child (company) in good condition for the longer term.

What are currently your highest priorities?

In many ways, companies can be seen as people. In this context, I feel that most people are running at only 60% of their true capacity, irrespective of their education and abilities. So it is up to the organisation to create an environment where people can reach their true potential and go beyond. Naturally here we also speak of staff evaluation and compensation models. I have found that some firms offer high returns for staff taking higher risks, which is very clear cut from a management perspective; it follows a 'give and take' principal. However, what is lost is the importance of performance as a team. It is essential to maintain a good balance to achieve strong results as a group, and therefore, my focus is on building an organisation and environment where people feel inspired to deliver 130%.

How do you approach the topic of innovating your business?

We approach innovation differently from large companies, where very often the goal is to achieve sales target. Rather, we raise the question, "what can we change?" or "what can we solve?" and build our marketing and innovation activities around the search for those answers. This is also in contrast to the manufacturing sector, where innovation is planted like a seed and technology adapts over time. In our case, the technology we use has been around for some time, but we can apply it in new ways, creating an entirely new concept. Indeed this can be patented and is a 'sweet spot' that we target.

Are you more or less optimistic today than one year ago, regarding the global economy?

As we only recently started our overseas operations, the global economy per se has not been a material factor as of yet. That said, we are very optimistic about the growth prospects of our overall business, as IT is the foundation of the global economy going forward and cybersecurity will certainly play a crucial role. What we observe is that security demand has not kept pace with the development of IT in general. In part, this is because too often people believe that security related incidents "surely cannot happen to me". Organisations have not experienced significant damage in order to take cybersecurity seriously, and I feel that many are not aware that various risks increase as IT usage grow at a rapid pace. By extension, the importance of IT security will not be left behind as risks need to be addressed.

Which markets do you regard as growth markets in Asia/globally for your business?

We are present in both North America and Asia, but we believe our largest growth market right now is Europe. From a cultural perspective, the IT security needs of European consumers are a good match for our business strategy. We are currently setting up our operations in London which will be launched by Summer 2016. For the IT industry in general, however, we see ample opportunities that stretch across Asia, Africa and into South America as well.

Over the next five years, what do you expect to be the key opportunities and challenges facing your business?

Our firm has a 50% market share in the Japanese market. Currently, no Japanese IT company has succeeded on a global scale. As a Japanese IT company, our ambition is to grow beyond our domestic success and meet the challenges and opportunities in the international markets, notably our North American counterparts. In short, our goal is to bring de facto solutions to the global market.

What is the key message from your experience that you want to share with aspiring entrepreneurs?

I believe it is important to remember that when individuals are starting out, be it as entrepreneurs or otherwise, there is a great deal to learn from others. Education is a measure of success for students, however it does not guarantee your success in your career. A certain measure of patience is therefore needed to absorb useful lessons from colleagues and those that have led the way before us. Beyond this, I find that very often entrepreneurs are active in industries that they first started off in as employees, so when you chose your first job, think to yourself “can I devote my life and career to this industry?” Paying close attention to what you experience early on in your working life has great value.



CONCLUSIONS

Despite the fact that it has been almost a decade since the Global Financial Crisis, the consensus among investors that a recovery has come full circle has yet to be formed with confidence. This is evidenced by the seemingly contradictory signs regarding the state of the global economy, Asia included. Asia's growth rates and overall economic fundamentals remain better positioned than the rest of the world, albeit there are clear signs of secularly lower growth. In such an environment, how should investors view the prospects for wealth creation in Asia?

Reflecting upon this year's Julius Baer Wealth Report: Asia, our main takeaway is that sector-level evidence confirms Asia's deserved reputation of dynamism and change. Adoption rates of new technologies that enable consumption and higher value added services are not homogenous across the region, implying that several key economies have ample room to catch up, spurring wealth creation well into the medium term. Mature economies like Hong Kong, Singapore and Japan promise to grow slower, but can take advantage of their sizable accumulation in financial and human capital. As Asia integrates further over the coming years, our key concern is the rise of barriers to trade and protectionism, which threaten value chains across the world and is a risk that needs to be closely monitored.



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