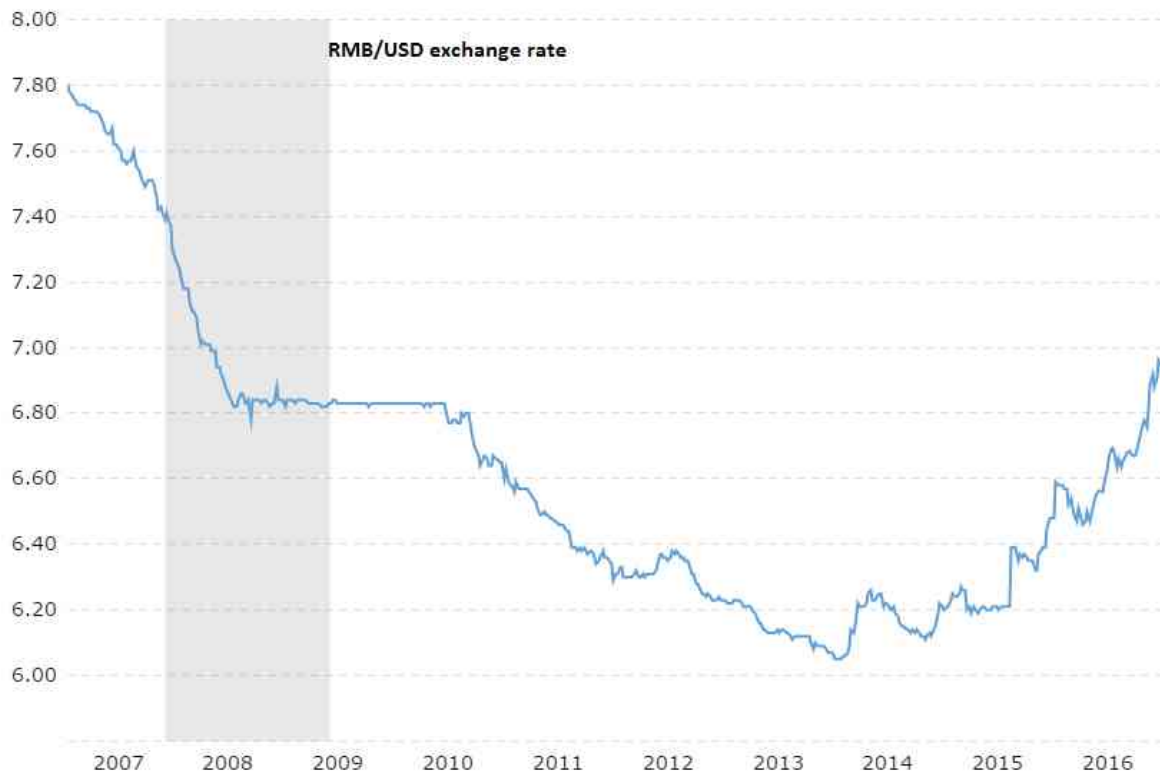


China investment thesis for 2017 and beyond

All eyes on the forex

Chen Lin, January 2017



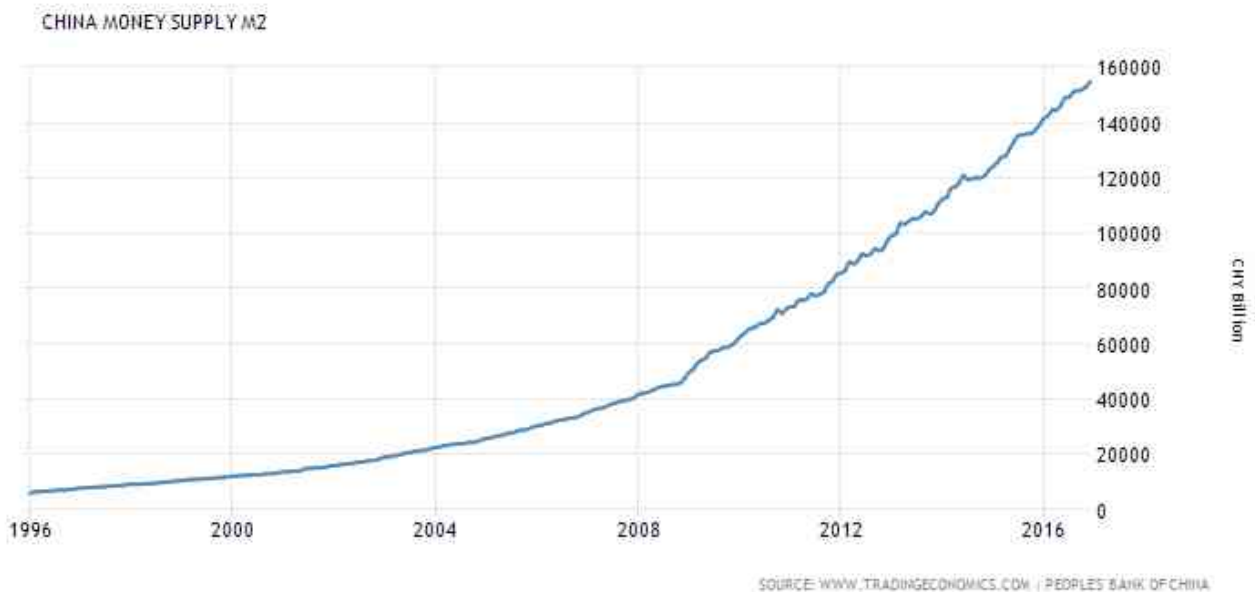
I put the 5 year chart of Chinese forex reserve and RMB exchange rate here. You can see the huge correlation between these two. By the end of 2016, China forex reserve dropped to about 3 trillion USD, the record low since 2011. Multiple factors contributed to the drop. The outflow of RMB is the key. The strength of USD is the other factor because China forex is in different currencies and it loses value when USD is strengthen.

Starting in 2017, China has implemented strict rules in order to curb currency outflow. Citizens are forbidden to exchange USD for the purpose of real estate or foreign investment. Any transactions over 50K RMB(7K USD) has to be declared. China also declared that bitcoin was illegal in early 2017 to combat the “illegal” money exchange.

The key question for gold and silver investors is if Chinese RMB continues to weaken and forex reserve is getting lower and lower, what kind of impact will it have on gold and silver prices?

There are two folds. First, China is one of the largest consumers of gold. If any crisis happens in China, small or big, gold demands will likely to weaken. Some people may sell gold and silver to meet the end's needs just like the Asian crisis in 1997. Second, there is a possibility that the Chinese government may forbid buying gold and silver, force people to turn them in to curb currency outflow, just like the bitcoin. This can also hit gold hard.

On the other hand, gold and silver have been the currency in China for thousands of years. In case of crisis, the demands of gold and silver will ultimately explode. Historically Chinese governments always over-printed money that led to hyper inflation. That's why gold and silver are always the real money and are generally accepted currency in China.



Here is the 10 year M2 money supply chart of China. Every time I looked at the M2 money supply in China in the past years I was frightened. You can compare the M2 in China vs US. At the end of 2016, China M2 stood at 155 trillion RMB. If you convert it into USD at 7:1, it is 22.14 trillion USD. At the same time, US M2 is ONLY 13.25 trillion! Had China not depreciated its currency, it would have been at 2x US. This is not sustainable. Something have to give in the long run.

From investment point of view, I believe the commodity boom triggered by the China buildup is

basically long over. I have been bearish for base metal for many years. I would call for investors' attentions to the next China trade. The rapid growth of China in the past decades leads to many problem, one of the key issues is pollution.



This is a picture of the famous Tiananmen square in the center of Beijing. Pollution is becoming the number one issue for the Chinese people and Chinese government. That's why I started the lithium trade back in 2015 when I saw the lithium price exploding in China.

<http://www.chenpicks.com/archive/lithiumreport2016.pdf> I see the current lithium rally can last as long as the pollution is the number one concern in China. I also interested in platinum and palladium, because they are heavily used in the emission control in cars and trucks. China is tightening the car and truck emission standard rapidly, that will increase the PGM demands for years to come.

Another angle to play the China cycle is, believe it or not, biotech. The poor quality of air and aging population will create huge market for cancer treatment for example. Recently Japanese firm Takeda spent 5 billions to buy US biotech, Ariad, for its cancer treatment pipeline is one example. This Japanese firm is very smart, positioning themselves ahead of the major trend. This is only the tip of the iceberg, many more is going to come. Just wait until Chinese firms start to buy biotechs here. That's why I started to invest in biotech about 5 years ago when I turned bearish to many physical commodities. I believe most investors in the US as well as Canada right now are too hang up about the pharma pricing issues in the US but miss the huge incoming opportunity from China. I envision big Chinese investment like takeovers in the mining sectors we experienced in the past years will happen in

the biotech area in the next few years. Chinese will hunt for good medicine by huge waves in a just few years just like they are buying the condos right now from Vancouver to New York City.

In conclusion, I am very blessed to have big successes from mining to energy to biotech in the past decade. While I believe that the Chinese demand lead commodity boom like base metal etc is all but long over, the next phase of demand is about to start, if not already. That includes clean energy, clean air, that's why I like lithium and PGM, and soft “commodities” like biotechnology. I am positioning myself and my subscribers ahead of the major trend.

In the mean time, I am deeply concerned about the massive money printing in China. Historically it doesn't end well. That could lead to 2000 or 2008 types of crisis. Usually during this type of crisis, gold and silver goes down first but it will create a once in a lifetime buying opportunity. It is very hard to predict if it will happen or when it will happen. But I always keep my eyes on this kind of possibility and always keep my subscribers informed.

Chen Lin is a successful money manager and writer of popular newsletter “What is Chen Buying and What is Chen selling”. You can learn more about Chen's work and his newsletter at www.chenpicks.com.