[Asset owner conversations]

Participants:
James Davis – OPTrust
Harsha Patel – RailPen
Tony Broccardo – Barclays Pension

Paul Colwell - WTW
Paul Deane-Williams - TAI
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Agenda

- Building a strategic case of why China is set to become an increasingly important part of global portfolios over years to come
- A cross asset class perspective on where opportunities lie
- What are the typical challenges of accessing China's capital market and what are the mitigation strategies?

Summary of talking points

- Liang started the conversation by giving an overview of TAI's Asset classes of tomorrow: China research which covers the investment potential of these capital markets for institutional investors. That research was three years ago and now WTW is recommending building up allocations to China in the region of 20% of the growth portfolio by 2030. Follow the rationale on pages 1-7 of the presentation deck or read this published article.
- Paul Colwell continued with an argument supporting a standalone equity allocation to China, including the benefit of diversification and potential excess return for those with the ability to take advantage of an inefficient market.
- The equity market used to be dominated by state owned enterprises (SOEs) and with no easy access in the past. However, the market has evolved significantly with SOEs no longer dominating, better transparency and massively improved access.
- Allocating to China should be seen as a journey that balances the pace of market developments with the need to build diversity in a global portfolio.
- The world order is shifting so should our investment portfolio which is currently still very anchored on the past.
- Monetary and fiscal policies in China have been very stable, relative to record-breaking stimulus seen in the Western economies.
- China is evolving rapidly on environmental aspects, but the S (social) factor among ESG is where investors may face some difficulties due to its complex nature.
- It is important to recognise risks such as operational, legal, reputational, and financial risks can indeed arise from human rights issues and it is a global challenge, not unique to China. Investors need to conduct their due diligence properly and seek to understand the risk exposure in this regard. That being said, investors are reminded not to take the Western media view of China as fact, particularly the myth that investing in China = supporting the Party. There is also the myth that one can divest from China, in fact it is really not possible given *Made in China* is found in most parts of most economies globally.
- There is a sense that blanket bans from investing, while perhaps providing 'good' optics are generally blunt and ineffective. It also denies 1.4bn people's access to capital, which works against investors' initial motivations of addressing the issues on "S". Investing in companies

that deliver good societal impact and collective engagement on a case-by-case basis are more effective in influencing the direction of travel.

- Reputational risk should be treated separately from ESG risks.
- What are the opportunities beyond equities? Accessibility to fixed income is no longer a restriction and there are opportunities in sovereign bonds. For the corporate credit market, there are concerns about liquidity, sub-standard credit analysis and unreliable ratings (95% are rated AA and above). Real assets have issues including property rights, governance and SOEs owning a majority of the infrastructure market.

About the Thinking Ahead Institute

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