Invesco

The China position:

Gauging institutional investor confidence

Written by:

The Economist INTELLIGENCE UNIT

Foreword

Marty Flanagan,
President and CEO,
Invesco Ltd.

Welcome to *The China position*, a comprehensive survey commissioned by Invesco and conducted by the Economist Intelligence Unit to gauge current and future investment allocations to Chinese investments. The survey includes responses from over 400 market participants across functions in the investment industry—including asset owners such as institutional investors, insurers and endowments; fund professionals such as asset and wealth managers; and investment professionals within commercial banks.

China represents an opportunity like none other Invesco has seen in our 30-year presence in this important market. Since China began opening up through various investment approaches in the 1980s, the country has stayed on a remarkably steady journey of market reforms. Indeed, we would argue that China's sustained economic expansion can, at least in part, be explained by this continued commitment to economic reform, supporting the growth and transformation of the Chinese economy that has lifted living standards for countless millions.

In this, our first broad look at how market participants currently allocate to China and their plans for the future, we see a near universal recognition of the vast scale and promise of China as an investment destination. We find that most organisations already have at least some exposure to Chinese investments, and the majority plan to further allocate to onshore assets, such as Shanghai- and Shenzhen-listed A shares or domestic credit, as well as offshore assets such as Hong Kong-listed H shares and US-dollar denominated debt. There are a broad variety of vehicles available for investors to access these markets—QFII, Stock and Bond Connect, ETFs, and managed funds to name a few. As access proliferates, the market will undoubtedly become more efficient, more liquid, and an increasingly substantial part of global portfolios.

China's expanding economy and markets are changing the investment landscape in unprecedented ways, and challenges remain to bridge global capital with Chinese opportunities. A notable minority of those surveyed have valid reservations around transparency and legal protections, and there remains some economic uncertainty about the domestic economy, especially with US-China trade tensions still unresolved at the time of this writing. Nonetheless, we see a broad market consensus that China is simply too massive an investment opportunity to ignore—and one we believe will only become more compelling in coming years.

About the research

The China position: Gauging institutional investor confidence is an Economist Intelligence Unit report, sponsored by Invesco. It analyses results from a survey of 411 institutional investor and asset owner organisations (approximately 200 in Europe, the Middle East and Africa, 100 in North America, and 100 from Asia-Pacific). Respondent seniority ranged from vice-president to C-suite management at asset and wealth management firms, commercial banks, endowment funds, family offices, government agencies, hedge funds, insurance and reinsurance companies, pension funds, and sovereign wealth funds. Assets under management at surveyed organisations spanned from US$500m to greater than US$10bn. The survey was conducted over August and September 2019. Respondents generally described their organisation's China exposure as above average when compared with industry peers.

Monica Woodley is the author and Jason Wincuinas is the editor. In addition to the survey, this report draws on Economist Intelligence Unit data, desk research and in-depth interviews with subject matter experts who have C-suite experience at asset-owner firms, running multi-billion dollar investment funds.

Our thanks are due to the following individuals for their time and insights:

- **Jimmy Chang**, chief investment strategist, Rockefeller Capital Management
- **Mark Delaney**, deputy chief executive and chief investment officer, AustralianSuper
- **Kevin Wade**, chief investment officer, Superannuation Arrangements of the University of London (SAUL)

Executive summary

- In a survey of institutional investor and asset owner organisations across Asia-Pacific (APAC), Europe, the Middle East and Africa (EMEA), and North America, a majority (nine in ten) claim some level of dedicated exposure to China.
- Investments are growing: about half of respondents with dedicated China exposure report their investments have “risen significantly” in the past 12 months.
- Equities are the most-cited way organisations invest in China. Over 60% of respondents with dedicated China exposure report both equities and fixed income onshore holdings.
- Respondents cited improvements to their own China expertise as the top driver for dedicated investment exposure.
- Nearly four in ten respondents say environmental, social and governance (ESG) factors play a role in all of their investment decisions; fewer than three in ten say ESG is particularly important for China investments.
- Chinese asset classes in our survey could see increased investment from foreign organisations over the next 12 months, with respondents highlighting technology, financial services and “new economy” sectors as most attractive.
- Risk assessments are largely even across asset classes, but on a regional split respondents in APAC are more concerned than counterparts in North America or EMEA.
- Respondents are mixed on the impact of US-China trade tensions, with similar numbers expecting either a positive or negative effect. But a majority of respondents report that their organisations expect to increase exposure over the next 12 months, regardless of outlook.
- About three-quarters of survey respondents say China’s economy will improve over the next 12 months; about two-thirds say the same for global economic conditions.

Growing economy, growing investment

The lure of a country with both a strong export-led manufacturing sector and a consumer base of 1.4bn citizens with rapidly rising incomes is difficult for investors to ignore. Since the global financial crisis, as developed markets in the West have struggled to grow consistently, China's rapid economic expansion has won over many initially sceptical investors (due to the market's less-than-transparent nature). At the same time, gradual market liberalisations have made it easier for foreign investors to take advantage of the country's growth.

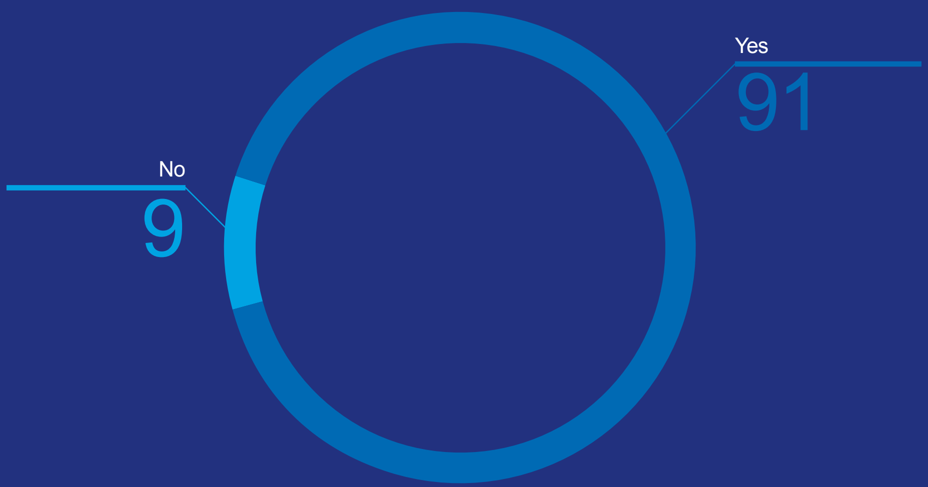
In 2019 (up to August 31st), foreign direct investment (FDI) into China grew by 3.2% year on year, reaching US$89.3bn, with certain sectors experiencing much higher growth levels. FDI into high-tech industries surged by 39.3%, reaching US$24.6bn and accounting for almost a third of foreign investments. Since the beginning of the year, foreign funding helped establish 27,704 new enterprises in the country.[1]

In a survey conducted by The Economist Intelligence Unit, institutional investor and asset owner organisations from around the world show strong interest in China, with nine in ten claiming a dedicated investment exposure. The term "dedicated" refers to China-specific investments that are deliberate and not acquired through broader holdings such as regional or emerging market funds. This category could include equities, fixed income or alternative assets through managed funds, exchange-traded funds (ETFs) or other investment vehicles.

Of those without dedicated exposures, about two-thirds still pursue China exposure through a global, Asia or emerging-market basket. Of those respondents who say that investments of any kind into China or its companies do not figure into their organisation's overall investment decision-making process, nearly half still report having some exposure through multi-country baskets, and just over a quarter through an Asia or emerging-market basket. Even for those not specifically targeting Chinese assets, exposure still seeps into portfolios. It's an indication that China may represent a larger portion of global investments than even some major asset owners or managers might have predicted. At the same time, respondents in the survey believed themselves to be ahead of the competition, with nearly 80% describing their organisation's China exposure, when compared with industry peers, as above average.

FIG 1. ASSERTIVE EXPOSURE

Does your organisation have a dedicated investment exposure to China currently? (%)



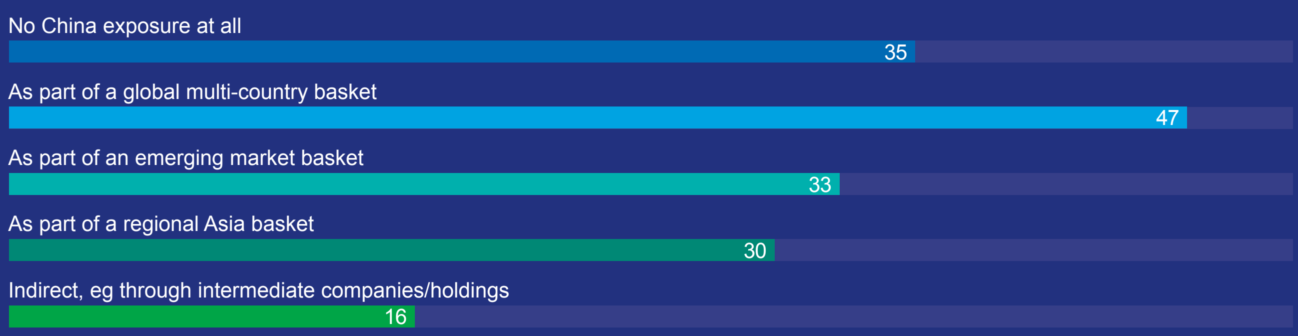
Source: The Economist Intelligence Unit. Sample size: 411

[1] BBC, "China economy: FDI grows steadily in the Jan-Aug period", September 17th 2019 (via EIU viewswire)

With China now the world's largest economy by purchasing power parity (second largest by nominal GDP, behind the US), and making up a growing share of global indices, it's a difficult market for investors to ignore, especially for large institutional and asset owner organisations. As Mark Delaney, deputy chief executive and chief investment officer of AustralianSuper, explains, "large global pension funds will have a set allocation to emerging markets, particularly China, as a hedge against low growth rates in Europe and the US."

FIG 2. UNDEDICATED DOESN'T MEAN UNEXPOSED

How organisations claiming no dedicated China investment still see exposure (%)



Source: The Economist Intelligence Unit. Sample size: 43

FIG 3. EMEA IN THE MIDDLE

Organisations with no exposure at all by region (%)

Source: The Economist Intelligence Unit. Sample size: 411

Results that test exposure levels in the survey also highlight a trend in the overall numbers: EMEA respondents sit closest to the average, while those in APAC and North America more commonly take up outlier positions. For respondents with no China exposure, the fewest were in APAC, the most were in North America and those in EMEA were in the middle. It's a pattern much repeated.

The hunt for alpha versus the need for transparency

Performance—particularly when viewed against Western markets—has been a main driver of survey respondents' dedicated investment exposure. The growth, profit and expansion potential of China's listed companies is a factor for four out of ten investors, while the strong macroeconomic performance of China and concerns about the longer-term upside potential of markets outside China were selected by about a quarter. This is supported by respondents' investment experience. Over half have seen their Chinese investments rise significantly in the past year, with a third saying their investments have risen somewhat. Only 4% experienced falls. This performance is a vital part of the story to help organisations meet one of their top objectives for dedicated exposure—seeking alpha. Over three-quarters of respondents, regardless of their objective, say they have met their goals.

But not everyone has such a favourable view of the country's prospects. For those without a dedicated exposure, or claiming China plays no role in investment decisions, survey results point to concerns about economic stability for over a third of respondents, with a quarter saying they believe low risk-adjusted returns and currency considerations may impact value or profit.

> **Before we had to translate the positive macro to the more difficult micro. Now the situation is the opposite**
>
> **MARK DELANEY**, AUSTRALIANSUPER

For Mr Delaney, China's overall economic growth had once been a main investment driver, but now individual companies attract his attention. "Before we had to translate the positive macro to the more difficult micro. Now the situation is the opposite, with stronger companies but a more difficult macro situation", he says. "For many years, equities were expensive, and the big ones still are, but valuations have come down. There are also now a lot of first-class businesses…And bonds are more attractive as China has higher interest rates [than many other markets]."

Access is increasing interest

Chinese investments are more attractive to foreign investors now that they are easier to access. In August 2019 China's State Administration of Foreign Exchange announced elimination of quotas for foreign investor asset purchases under the US dollar-denominated Qualified Foreign Institutional Investor (QFII) and the Renminbi Qualified Foreign Institutional Investor schemes, which allow access to China's A-shares market.[2]

Other schemes, such as the Shanghai-Hong Kong Stock Connect (launched in 2014), Shenzhen-Hong Kong Stock Connect (launched in 2016) and the London-Shanghai Stock Connect (2019), also make it easier for foreign investors to invest in Chinese companies. So long as all other relevant laws and regulations are followed, the schemes allow eligible companies listed on the two stock exchanges to issue, list and trade depositary receipts on the counterpart's exchange.[3]

Slightly over a quarter of survey respondents say that a reduction of legal restrictions for investing in Chinese financial markets or institutions would be a driver of dedicated exposure.

Increased coverage and expertise

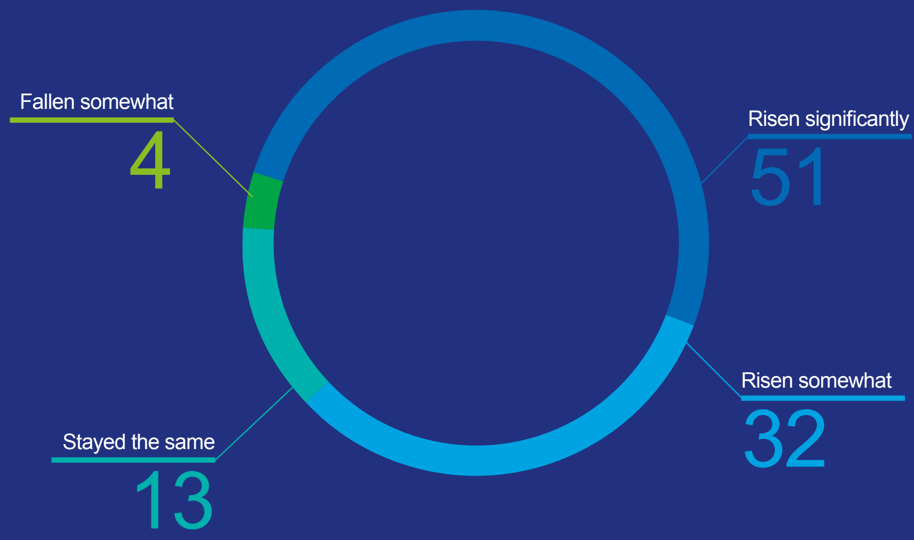
For those whose allocations are based on benchmarks, the increase of Chinese assets in global indices has been an impetus for dedicated investment exposure. Almost a third say that an increase in China's weighting in global indices such as MSCI or FTSE is a factor, while a similar number of survey respondents without a dedicated exposure say an increased weighting would be a catalyst for considering one.

As MSCI, a large index provider, expects to quadruple its mainland Chinese holdings this year,[4] this is likely to spur further investment. That inclusion, says Kevin Wade, who is the chief investment officer of Superannuation Arrangements of the University of London (SAUL), "is a strong reason to invest. That makes it a larger universe with more investors looking there—making it a stronger market."

[2] The Economist Intelligence Unit, China report September 2019
[3] Baker McKenzie, https://www.bakermckenzie.com/en/insight/publications/2019/07/launch-shanghai-london-stock-connect
[4] Washington Post, https://www.washingtonpost.com/opinions/2019/06/13/chinas-infiltration-us-capital-markets-is-national-security-concern/

FIG 4. RISING REGULARLY

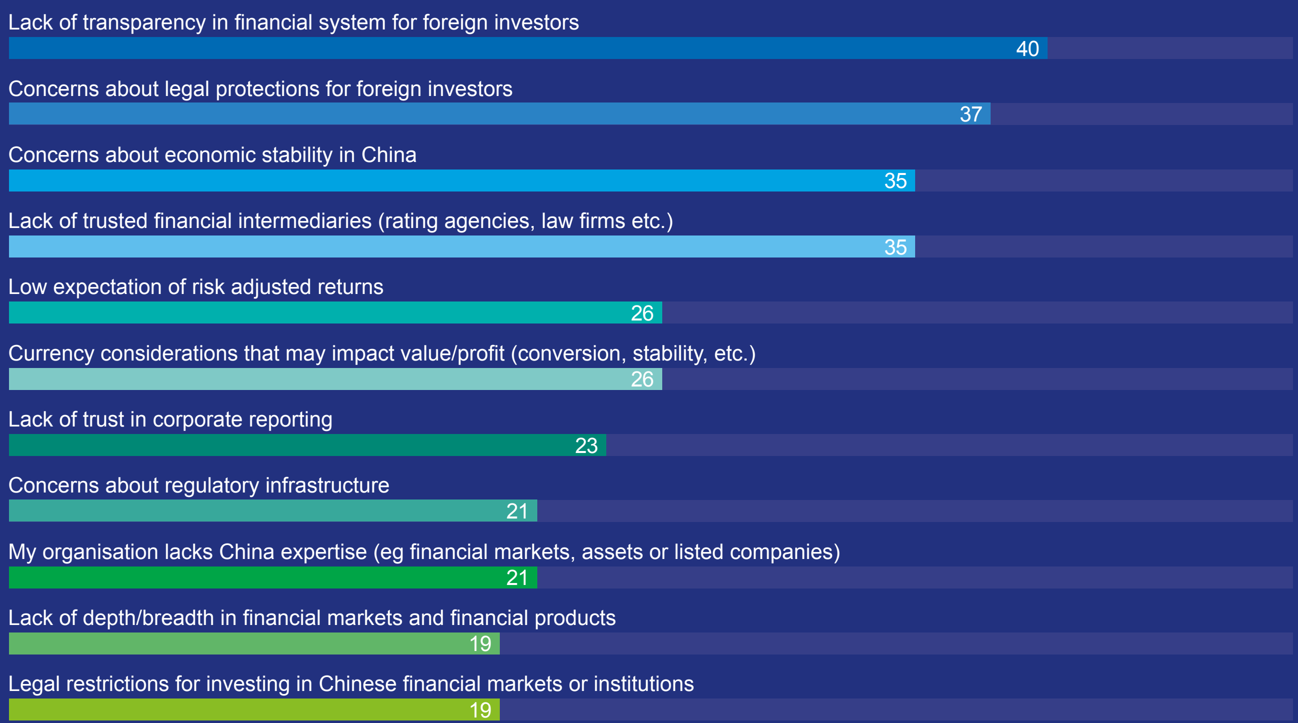
Over the past 12 months, what changes have you observed in relation to your organisation's investments in China? (Respondents with dedicated exposure only) (%)



Source: The Economist Intelligence Unit. Sample size: 280

FIG 5. SIDE-LINING CONCERNS

What do you consider to be the biggest challenges to having a dedicated investment exposure to China? (Firms with no dedicated investment exposure to China only) (%)



Source: The Economist Intelligence Unit. Sample size: 43

It also helps with familiarity, which can lead to increased expertise, which is the top reason respondents gave for growing dedicated investment exposure. And for organisations that claimed no dedicated exposure, over a fifth cite a lack of China expertise as one of the biggest obstacles. That rises to over a quarter for the respondents who say their organisation has no investments of any kind in China and the country's companies do not figure into their overall investment decision-making process.

Improving transparency

While "expertise" is the number one driver among survey respondents for having dedicated investment exposure to China, advancements such as improved corporate reporting, better legal protections, greater regulatory oversight and improvement among financial intermediaries (rating agencies, law firms, etc) are also significant factors for survey respondents to consider increased investment in the country.

For respondents without a dedicated exposure, these same areas are still concerning—four in ten cite a lack of transparency in the financial system for foreign investors. Legal protections for foreign investors and a lack of trusted financial intermediaries are factors that worry more than a third. Over half say that increased legal protections for foreign investors would be a catalyst for a dedicated exposure to China, while over a third also say better corporate reporting would make them consider an allocation. Respondents in EMEA took up a rare outlier position here, choosing improved corporate reporting within China as a top catalyst.

FIG 6. INDICES INSTRUCTING INVESTORS

What were the drivers for the dedicated investment exposure? (%)

Source: The Economist Intelligence Unit.

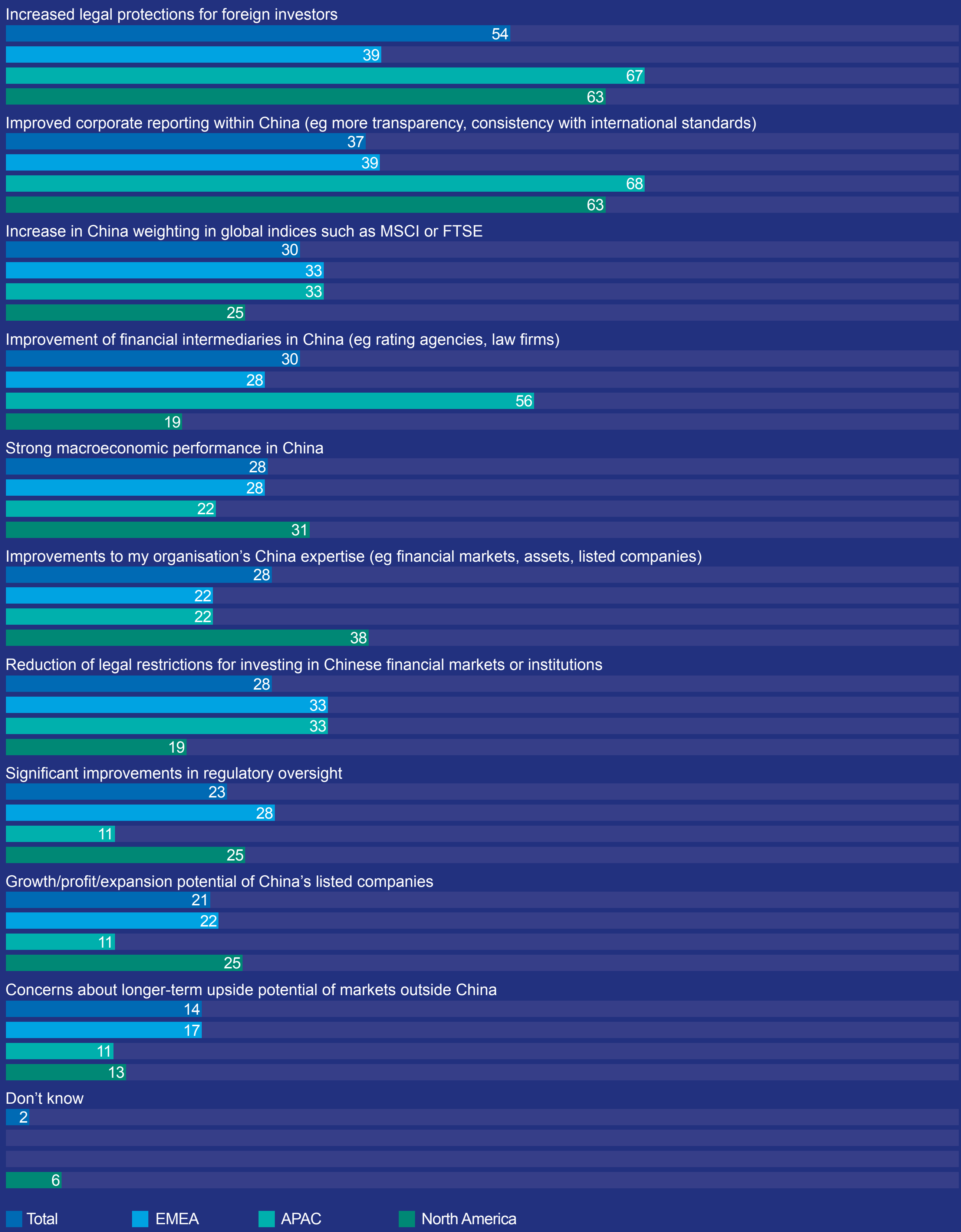
FIG 7. DEVELOPING INSIGHTS

What were the drivers for the dedicated investment exposure?
[Respondents with dedicated exposure only] (%)

Source: The Economist Intelligence Unit. Sample size: 368

FIG 8. WORRY RELIEVERS

What would be a catalyst for considering a dedicated investment exposure to China?
[Respondents with no dedicated exposure to China only, by region] (%)



Source: The Economist Intelligence Unit. Sample size: 43

Invesco perspective

Andrew Lo, Senior Managing Director and Head of Asia Pacific, Invesco Ltd.

Looking at the survey results, I see a fundamental and meaningful shift in sentiment towards China as a large and rapidly growing economy that presents countless opportunities. Until recently, global investors often viewed China more as a source of capital rather than as an investment destination in its own right. Now, organisations see a clear need to carve out a specific allocation to this market. This is a key development in China's market evolution.

We see that market participants appear to remain focused on the long-term opportunity in China despite some macroeconomic softening, market turbulence and geopolitical uncertainty. While the scale of the Chinese market has long been hard to ignore, structural issues such as market access have limited participation from global investors. It's clear that investors are watching these barriers fall and responding positively.

Overall, we think that respondents are optimistic about China over the long run because it's becoming easier to understand and access. Successful investing in any market takes knowledge and experience, so the creation of an institutional base of knowledge among global investors has provided confidence for them to invest in Chinese markets. This is the second-most cited objective for why organisations have a dedicated China exposure. This knowledge acquisition is a strategic asset and is set to accelerate as barriers to entry fall and the market continues to liberalise.

Insights we hear from clients support the survey findings. Many are impressed by China's continued economic growth and reforms over the years, and the reservations they had about entering the market previously are lifting, especially as Chinese equities and bonds are included in global indices.

I'm very optimistic about the future. Despite ongoing trade tensions, the Chinese government is incentivising innovation and opening up their financial markets even further. I am encouraged to see that global investors are looking at China similar to how we see it at Invesco—as a unique and promising long-term opportunity.

The investment process and an ESG nuance

Concerns about transparency in reporting can influence the process used by institutional investor and asset owner organisations when researching and assessing Chinese investments. ESG factors are also increasingly used in the investment process due to growing concerns about the impact of climate change. According to the UN's Principles for Responsible Investments, climate change is still frequently stated as the top concern of its signatories, despite a growing number of topics under the ESG umbrella.[5]

According to Jimmy Chang, chief investment strategist at Rockefeller Capital Management: "We have a consistent ESG engagement process across geographies but getting disclosure in some regions is an issue. In emerging markets, information is not as widely available and it takes more prodding to get what we need. Governance and reporting are very important and we have seen some—but not dramatic—improvement in China."

> **In emerging markets, information is not as widely available and it takes more prodding to get what we need**
>
> **JIMMY CHANG,** ROCKEFELLER CAPITAL MANAGEMENT

Some organisations find they need operations in the country in order to access certain information. "We've had a research office in Beijing since 2013, because if you want to understand the macro picture and know what's happening on the ground, you have to be there," says Mr Delaney. "In terms of stock selection, the process is the same as for other markets, but I really saw a difference in terms of access after I visited companies; relationships still matter."

The survey revealed a preference for using global asset managers to access Chinese investments, but Chinese asset managers, joint venture asset managers and the Hong Kong-based subsidiaries of global asset managers are also used. Respondents in APAC seem to prefer Chinese asset managers and the Hong Kong-based subsidiaries of global asset managers, most likely for their on-the-ground access. North American investors expressed more comfort with global asset managers and ETFs listed in non-China markets.

However, some organisations are confident enough in their expertise to directly own Chinese companies or access Chinese investments on their own as a QFII. Hedge funds, asset managers and insurers are the most likely to have direct ownership of companies or qualify as QFIIs, as well as respondent firms with higher assets under management (US$10bn+).

For our interviewees, integrating ESG factors into the investment process is now standard across the board, but they feel it is particularly vital for Chinese investments. However, these professionals do take into account the fact that China is still an emerging market.

"We integrate ESG across the board with all of our managers and with China governance is particularly important," according to Mr Wade. "We understand that it will be weaker than in Europe or the US, but our role is still to challenge the decisions of our managers to ensure we're still meeting minimum requirements."

Mr Chang adds: "We are an ESG investor but we prefer to engage constructively with Chinese companies to push for improvements. China is the second-largest economy, so if we can encourage some Chinese companies to improve and become a leader in their sector, that can have a big impact." Mark Delaney echoed a similar point of view.

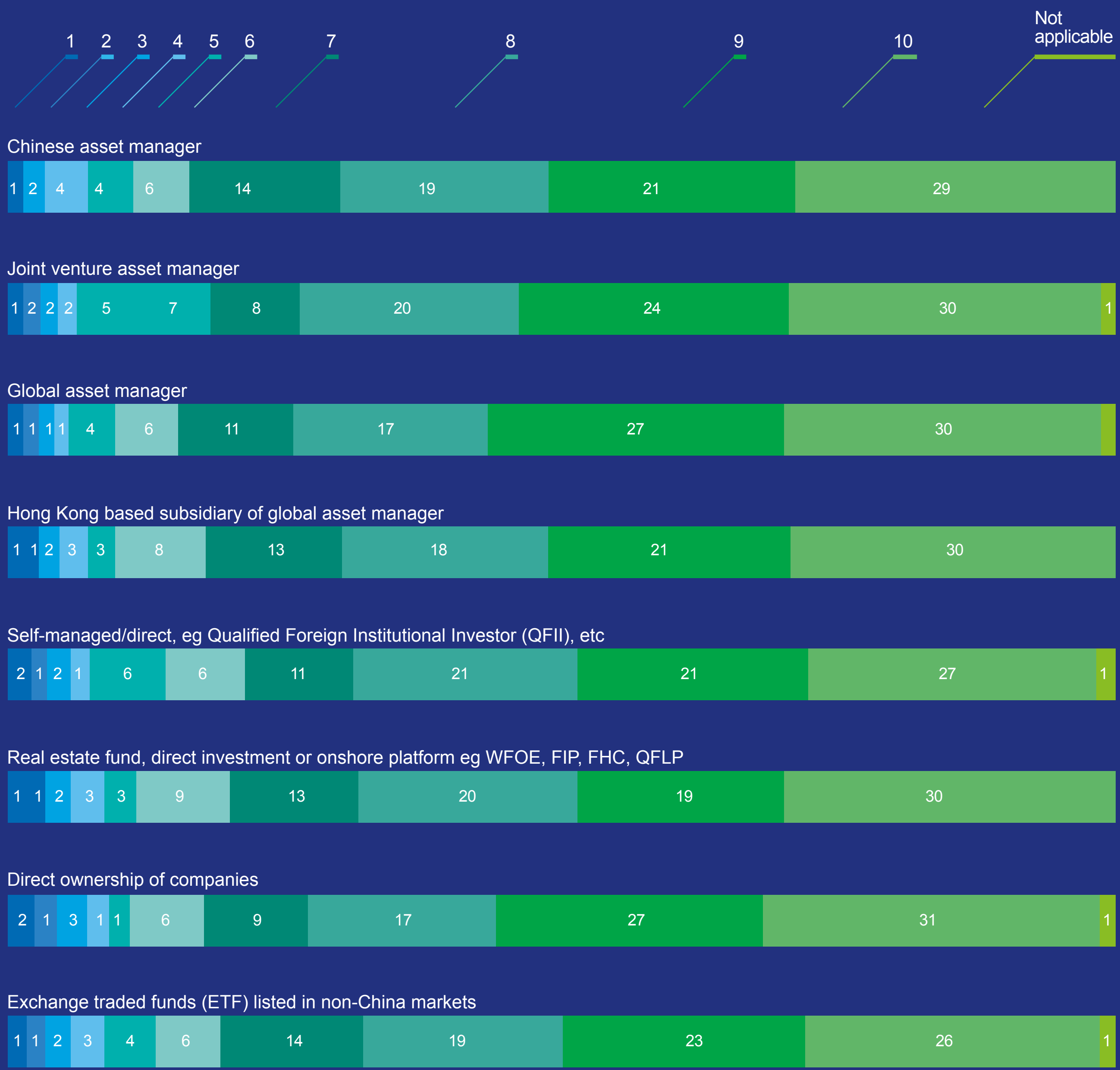
Compared with our expert interviews, survey respondents are less likely to integrate ESG. Fewer than four in ten say ESG is a factor in all of their investment decisions, although that masks strong regional differences—45% of respondents in North America and EMEA and just 14% in APAC. Overall, fewer than three in ten say ESG is particularly important for investments in China and just over a quarter say they sometimes use ESG depending on the type of investment. Meanwhile, almost a third of respondents in APAC use ESG for Chinese investments, and almost half say they sometimes do.

Positively, Mr Delaney sees that Chinese companies are taking on board the importance of raising their game with ESG. "Chinese companies want to be the global best and they know that ESG is a part of that," he says. "Their aspirations are the same as those of developed market companies and that's encouraging."

[5] UN PRI, https://www.unpri.org/pri-blog/climate-change-tops-the-list-of-esg-concerns-for-investors-in-2019/4163.article

FIG 9. HOW DO YOU GET THERE?

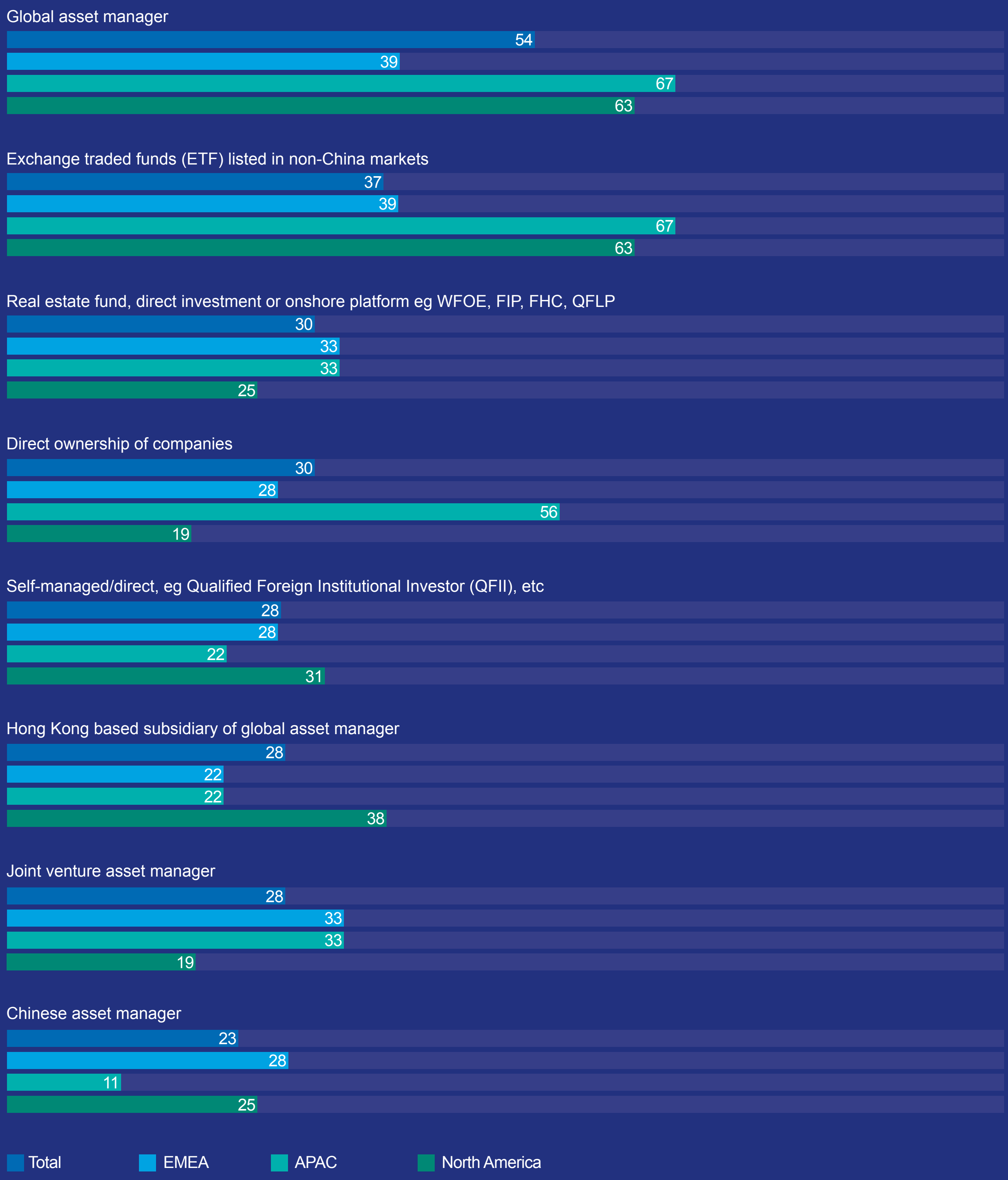
When implementing investments into China, how prominently do the following types of entities figure in your approach? Select one in each row. (Scale of 1-10 with 10 being very prominently and 1 not at all prominently) (%)



Source: The Economist Intelligence Unit. Sample size: 280

FIG 10. COMPETING CONFIDENCES

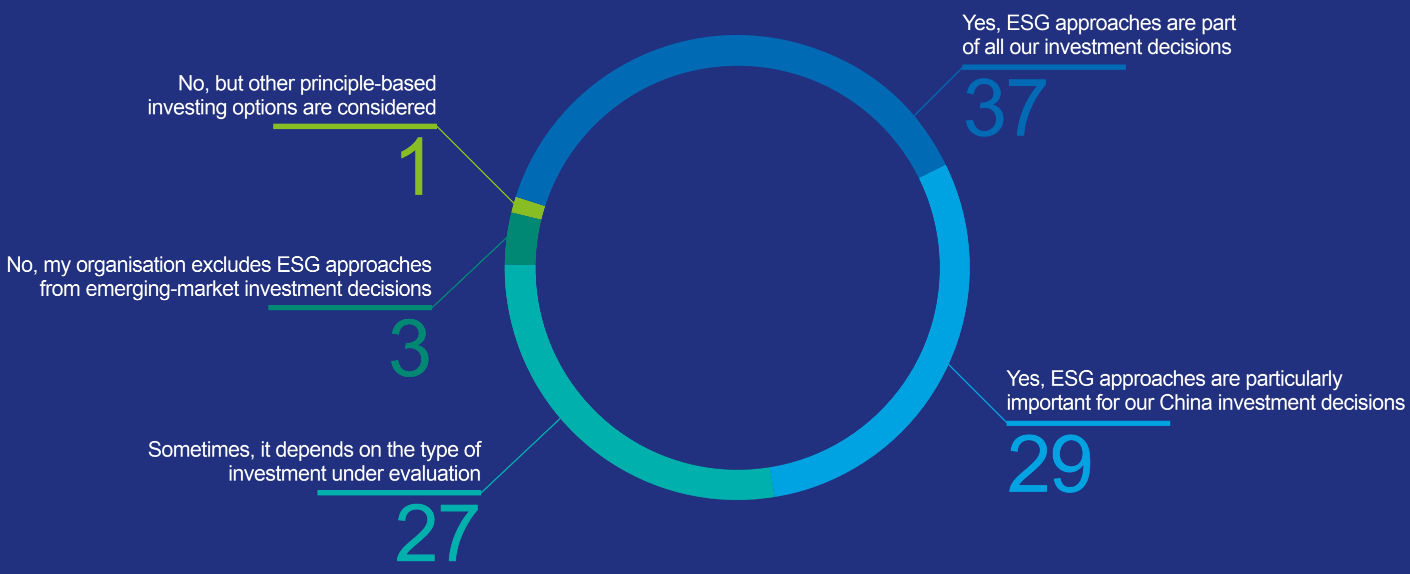
Average investor sentiment on types of entities by region (%)



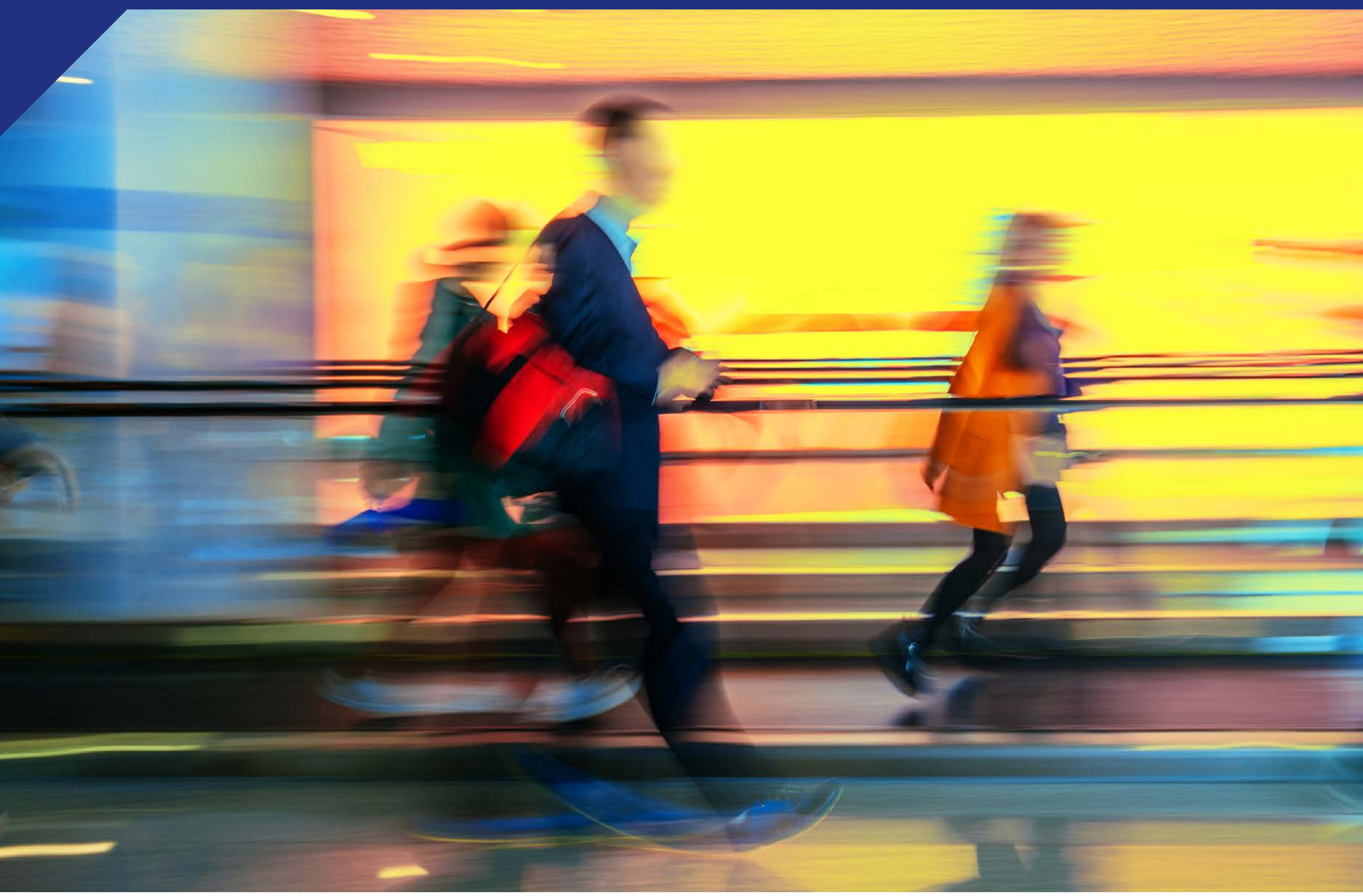
Source: The Economist Intelligence Unit. Sample size: 280

FIG 11. GOING GREEN

Is ESG investing a consideration in your organisation's China exposure? (%)



Source: The Economist Intelligence Unit. Sample size: 411



Top asset classes and investment themes

Equities are the most popular asset class in the survey, with over two-thirds of respondents claiming a direct allocation to China onshore equity market A shares[6] (and as high as 82% in North America). Meanwhile, over half have a direct allocation to China offshore equity market H shares[7] (with APAC reaching 80%). It appears that investing in equities is the most straightforward way organisations seek to benefit from growth related to Chinese companies that are focused on achieving “global best” status.

According to Mr Wade, the A-shares market is mainly Chinese retail investors, so there is currently a wider dispersion of returns than seen in more developed markets. But as more institutional investors enter, it should become a stronger market, making it still more attractive.

While listings within the country are growing, a US listing is still the goal of many large Chinese companies. Over the past two decades, about 200 Chinese firms have gone public in the US—more than from any other foreign country—with a total market value of US$1trn. Most have their main listing in the US, while some have their secondary one in America and a main listing in China.[8]

FIG 12. NORTH AMERICANS MOST BULLISH ON A SHARES

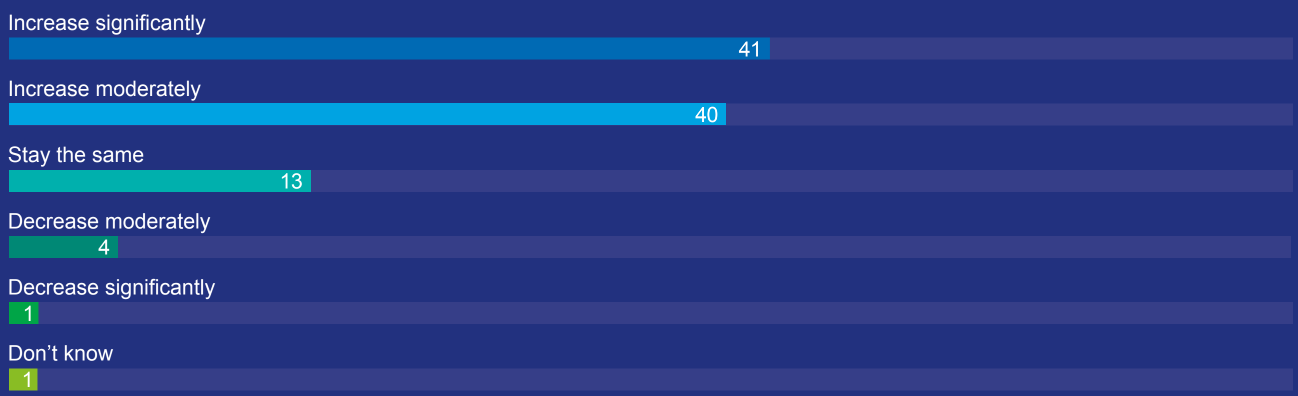
How does your organisation implement its dedicated investment exposure currently? (%)

Respondents with direct allocation to China A-shares onshore equity markets

Source: The Economist Intelligence Unit. Sample size: 255

FIG 13. EVERYBODY UP

Over the next 12 months, to what extent do you expect your organisation’s exposure allocations to China to change? (%)



Source: The Economist Intelligence Unit. Sample size: 280

[6] A-shares are equities of mainland China companies traded on the Shanghai Stock Exchange or the Shenzhen Stock Exchange and quoted in the local currency.
[7] H-shares are equities of mainland China companies traded on Hong Kong Exchange and quoted in Hong Kong dollars.
[8] *The Economist*, “Chinese stocks in America: Far from home”

These US-listed Chinese firms are often an entry point for investors, as they provide access to the growth of China, but with the reporting rigour and transparency of a developed market listing.

"We are not yet investing in Chinese A shares, we are sticking to Chinese companies with listings in Hong Kong and New York," Mr Chang says. "Over the past year, our exposure to China has held steady. We're now raising our exposure but not significantly. We are bottom-up stock pickers and valuations are looking more attractive."

Over half of survey respondents plan to increase their allocations of onshore equities in next 12 months (59% in North America), while just under half plan to increase their exposure to markets offshore (again, slightly higher in North America at 55%). Just one in ten plan to decrease their exposure.

"Our China allocation has stayed about the same over the past year, in listed equities like Alibaba and Tencent," Mr Delaney says. "But we now have a CIBM [China Interbank Bond Market] account so we can invest directly in government bonds, so we are now trying to settle on an entry strategy."

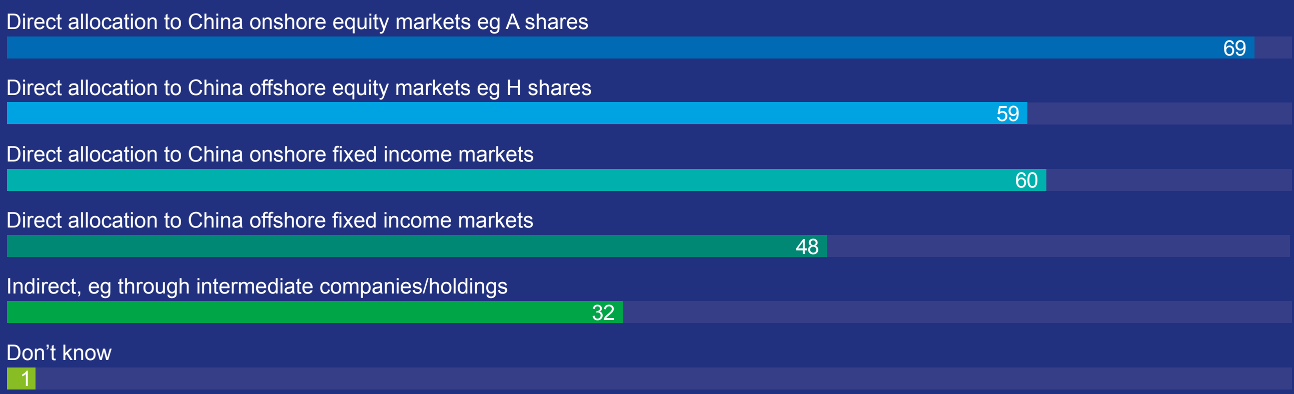
Onshore fixed income markets are popular, with six in ten survey respondents having a direct allocation. Just under half have exposure to offshore fixed income markets (58% for APAC). A similar number plan to increase their allocations to Government/Quasi/SOE debt onshore, corporate and local government debt onshore, while four in ten say they will boost their exposure to offshore corporate debt and offshore government debt.

About half of respondents say they will increase their allocations of alternative assets, real estate, direct ownership of companies, and currency, with North American respondents consistently more bullish across these asset classes.

Respondents' risk and return assessments are largely even across asset classes; but on a regional split, respondents in APAC are more concerned about risk than their counterparts in North America or EMEA.

FIG 14. DIRECT ALLOCATIONS GROWING

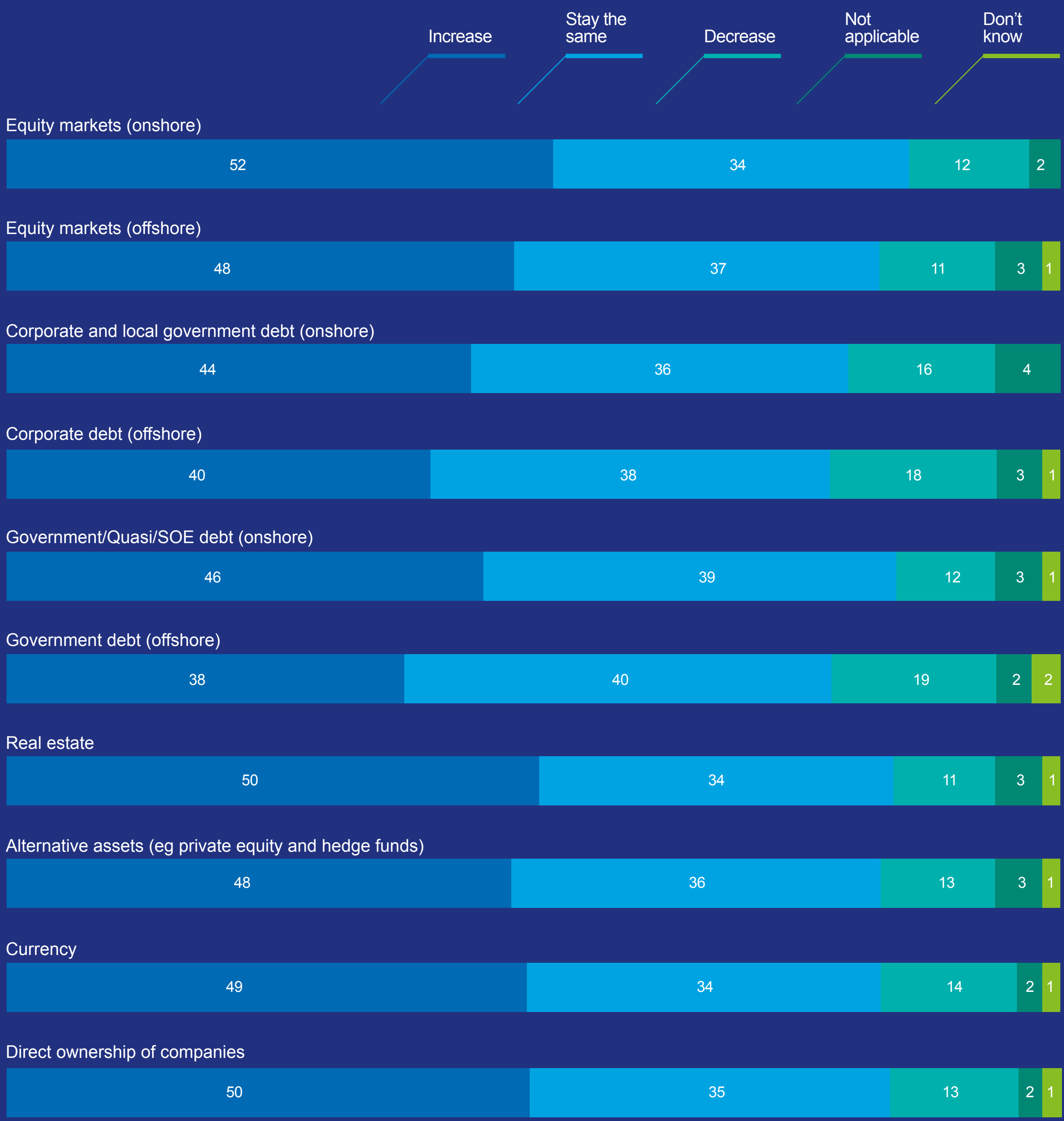
How does your organisation implement its dedicated investment exposure currently? (%)



Source: The Economist Intelligence Unit. Sample size: 368

FIG 15. ASSET OWNERSHIP ACCELERATES

Over the next 12 months, what changes do you expect your organisation to make regarding its allocations in China for the following asset classes? (%)



Source: The Economist Intelligence Unit. Sample size: 411

While real estate is seen as having the least risk, direct ownership of companies is seen as having the most reward potential.

"Beyond our equity exposure, about six years ago we invested in a private equity [PE] fund focused on Chinese energy infrastructure," says Mr Wade. "With the country's environmental concerns, we expected that the government would 'clean up'. The returns haven't been great but it's PE—some of the companies do well but others have struggled."

New economy

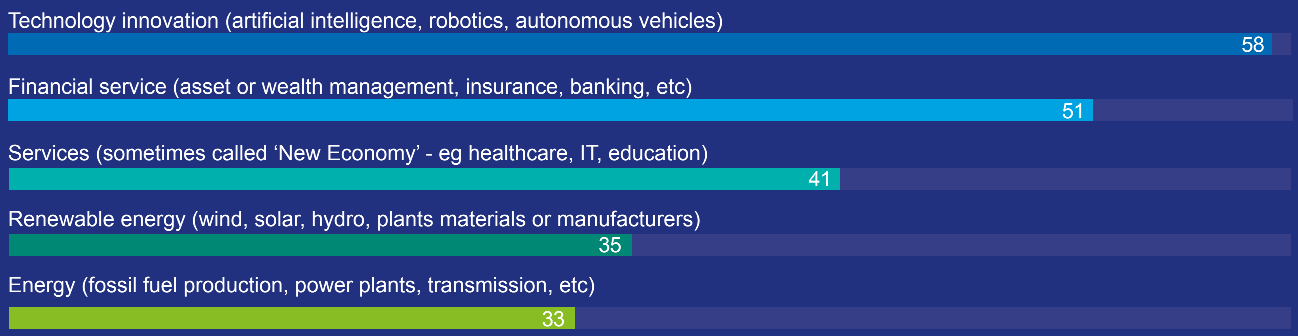
With big names such as Alibaba and Tencent, it is unsurprising that technology is seen as the top investment theme for the next 12 months, selected by almost six in ten respondents. Other themes that tap into China's rising consumer power, such as financial services, "new economy"[9] companies and consumption, are also popular. And energy, both traditional and renewable, to power the country's growth is another favourite.

Mr Chang is more positive about "new economy" equities. "We are seeing some companies in the new economy space with strong free cash flow, rising dividends and attractive valuations," he says. "Dividends are also rising at some state-owned companies as the government has cut taxes and provided other stimulus and so now is demanding that be paid back in the form of dividends."

Mr Delaney also sees the country's strengthening consumer base as a driver of investment. "The domestic market is growing by 9% per annum and standards of living are rising. So the new economy sector is really growing," he says. "China is in transition from an export-led to a domestic consumption economy and trade tensions have put that on fast forward."

FIG 16. AN ATTRACTIVE NEW ECONOMY

Over the next 12 months, which of the following themes or trends do you believe are most likely to attract investment from your organisation into China? (%)



Source: The Economist Intelligence Unit; respondents with dedicated exposure (368)

[9] Industries with a strong digital component, ranging from retail to services to insurance, which develop products and business via new models, operations or technologies, qualify as "new economy".

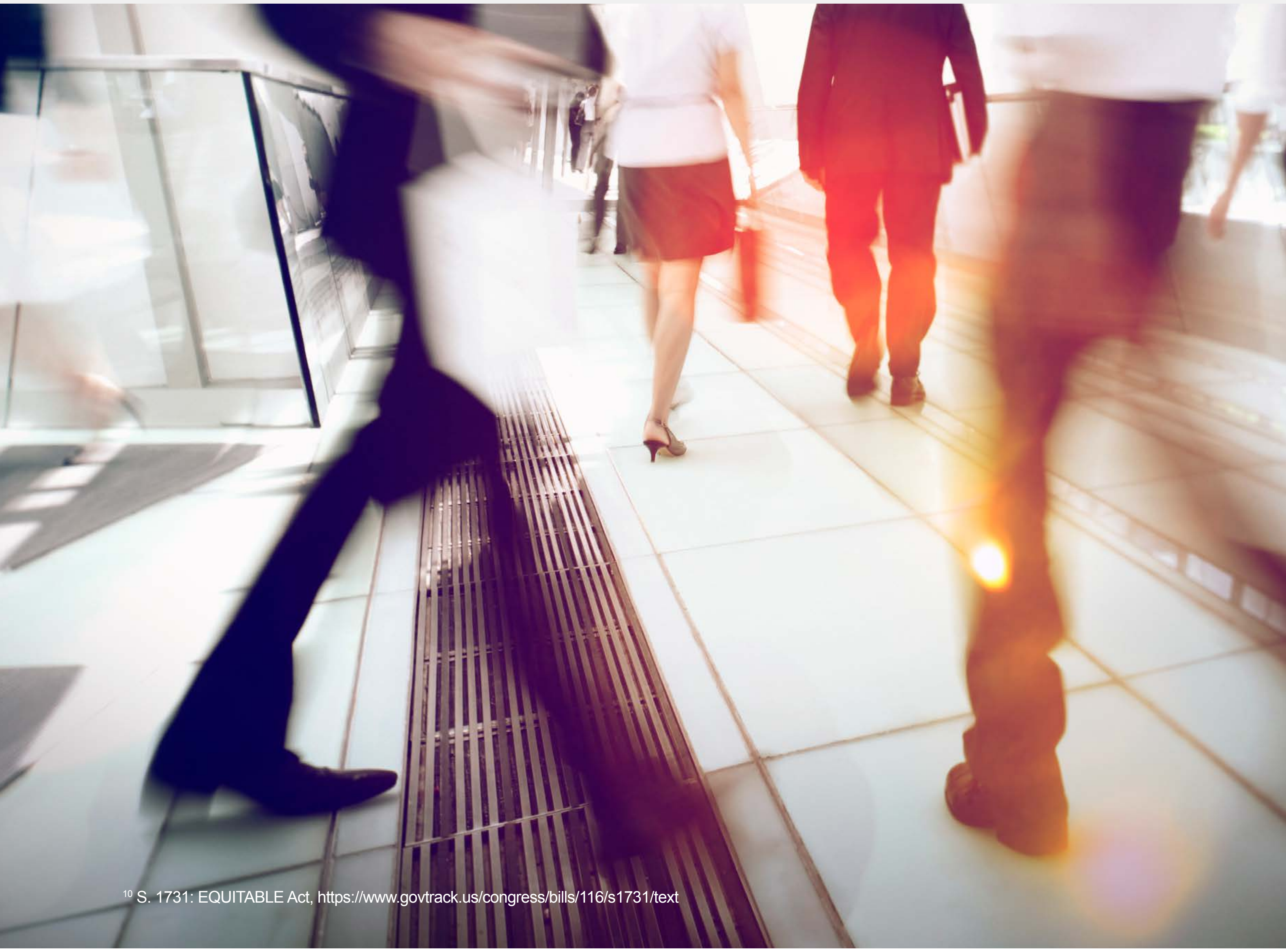
Trade tensions, protectionism and the future

While Mr Delaney sees a posible positive effect from ongoing trade tensions between the US and China, the survey paints a more mixed picture. While 44% of respondents say it will have a negative impact on their investment decisions, 42% say it will have a positive impact. North American respondents are more optimistic, while those in APAC are the most negative.

However, even some of those with a negative view plan to increase their investments, perhaps betting the dispute cannot last forever and seeing this as a buying opportunity. Over two-thirds will increase their exposure (a third significantly), while just one in ten plan to reduce it.

"Our expectations for 2020 is that the trade tensions will de-escalate and the government will continue to pump stimulus into the economy," Mr Chang says. "Over the course of September, we have seen conciliatory gestures…I don't think there will be a comprehensive deal but a partial deal to address the trade imbalance, intellectual property concerns and access to the market, and markets have reacted favourably to that de-escalation."

However, Mr Delaney questions whether the trade tensions will result in restrictions on investments. "We don't think there will be restraints on investments



[10] S. 1731: EQUITABLE Act, https://www.govtrack.us/congress/bills/116/s1731/text

but there may be on where Chinese technology is used, which would influence our ability to invest."

In June 2019 a US senator, Marco Rubio, introduced the Equitable Act—which stands for: Ensuring Quality Information and Transparency for Abroad-Based Listings on our Exchanges. The aim is to give the Public Company Accounting Oversight Board (PCAOB) more power to examine Chinese auditors' work on financial statements of US-listed Chinese companies. It means Chinese companies would face removal from US exchanges if PCAOB inspections were blocked.[10] (Established by the Sarbanes–Oxley Act of 2002, the PCAOB is a body that "oversees the audits of public companies and SEC-registered brokers and dealers in order to protect investors and further the public interest in the preparation of informative, accurate, and independent audit reports.")[11]

According to Mr Chang: "There is still a strong pipeline of Chinese companies planning to list in the US, but as Congress focuses on improving the disclosure from Chinese companies, will that discourage some from listing there? Politics could make a difference, but tier-one companies are still going to want that New York listing."

The Economist Intelligence Unit does not expect an agreement over trade until after the US presidential election in 2020, forecasting bilateral tensions to persist and worsen in other areas. The uncertainty generated by the US-China trade tensions and diminished corporate prospects in China's slowing economy underpin our forecast for FDI inflows to fall to US$193.7bn in 2019.[12]

FIG 17. OPTIMISM OVERCOMES TENSIONS

Expectations of the US-China trade tensions to have on investment by region (%)

Source: The Economist Intelligence Unit. Sample size: 411

[10] S. 1731: EQUITABLE Act, https://www.govtrack.us/congress/bills/116/s1731/text
[11] PCAOB https://pcaobus.org/About/History/Pages/mission-vision-values.aspx
[12] The Economist Intelligence Unit, China report September 2019

Conclusion: A bright future?

The Economist Intelligence Unit forecasts real GDP in China to grow by 6.2% per year on average in 2019-20—just about the minimum level required for the government to achieve its goal of doubling real GDP between 2010 and 2020—but slowing to an annual average of 5.5% in 2021-23.[13] Global GDP should also drop to 2.4% in 2019, from 2.9% in 2018, and slowly rebound to 2.5% in 2020 and 2.9% for 2021-23.[14]

> **There is such long-term alpha potential over developed markets**
>
> **KEVIN WADE,** SAUL

"As China tries to engineer a soft landing—after years of increasing leverage to support growth—it is also trying to deleverage," says Mr Chang. "So we do expect to see GDP decelerate over the next five to ten years as there is a realignment."

Even slower growth rates in China are still favourable compared with developed markets, according to Mr Wade. "There is such long-term alpha potential over developed markets that despite the short-term noise [due to trade tensions] our managers are very comfortable long-term," he says. "If we do see a fall back in markets, we would see that as an opportunity to invest. It wouldn't put us off investing because of the long-term benefits."

FIG 18. REALISTIC OR OVERLY OPTIMISTIC?

Respondent expectations by region for global and China's economic growth (%)

Source: The Economist Intelligence Unit. Sample size: 411

[13] Ibid
[14] Ibid

Still, most survey respondents remain positive about China and the global economy. About three-quarters believe China's economy will improve over the next 12 months (83% in North America) and about two-thirds believe global economic conditions over the next 12 months will be better. That optimism translates into increases in investment exposure—four in ten plan to increase significantly and the same number plan to increase moderately. Only 4% say they will reduce exposure.

Such bullishness may be overly optimistic, according to our respondents who say investments of any kind into China do not figure into their organisation's overall decision-making process. They are over 20 percentage points less likely to say that China's economy will be better in a year, and 35 percentage points less likely to say the same about the global economy.

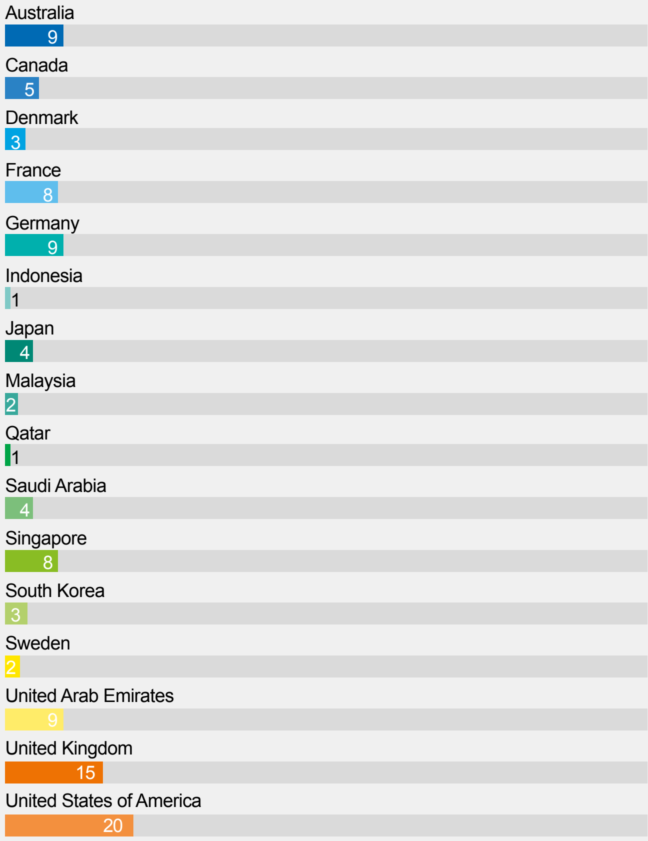
These divergent views highlight the difference that experience makes when it comes to investing in China. Information is a key element driving further investment in China; as both institutional investors and asset owner organisations improve internal information gathering and analysis, they appear more positive on potential. And with China's both growing and opening economy, the increased benchmark allocations from index providers and improving ESG credentials for its companies, even hesitant investors say they are more likely to increase than decrease investments in China, making it a market that investors can't ignore.

Key takeaways

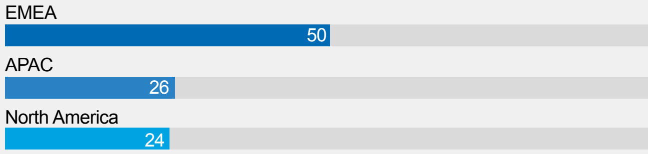
1. Economic forecasts among survey respondents are largely optimistic.
2. Institutional investors and asset owner organisations have a positive outlook on China, particularly for new economy and technology sectors
3. Information is a key element driving China exposure; improving internal information gathering and analysis correlates with investment appetite
4. Risk assessments across asset classes is mostly even; APAC respondents show more caution than those in North America or EMEA
5. Equities are still the most common investment vehicle for China exposure but other asset classes have a growing attraction as information flow improves

Appendix Survey demographics - all respondents (411)

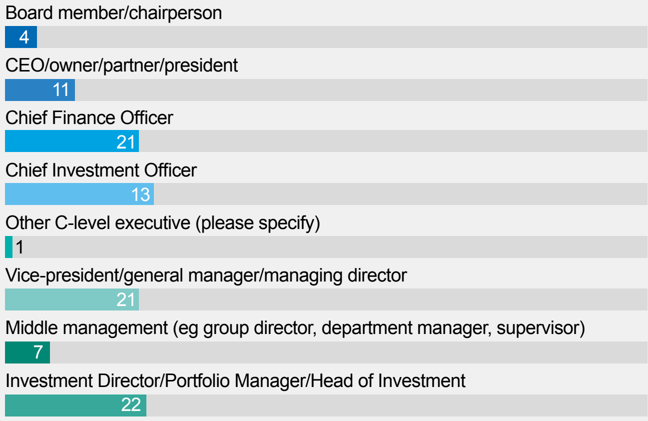
D1. In what country are you located? Select one. (%)



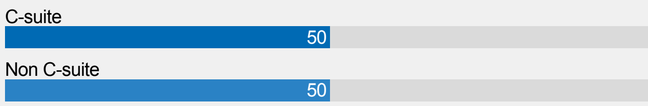
D1a. In what country are you located? Select one. [By region] (%)



D2. Which of the following best describes your job title? Select one. (%)



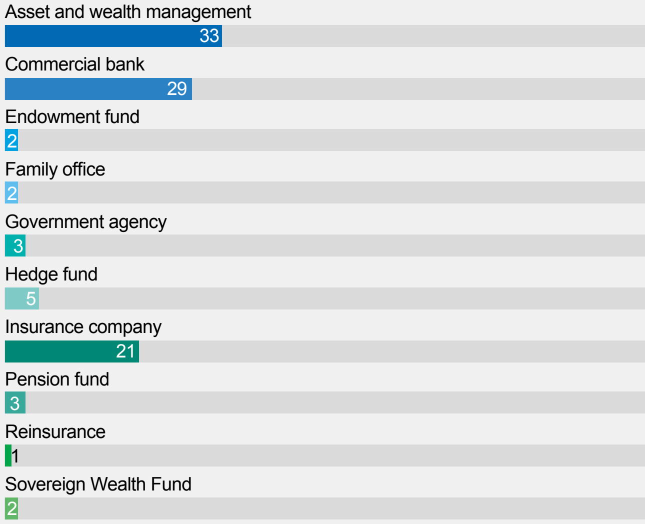
D2a. Which of the following best describes your job title? Select one. [By seniority] (%)



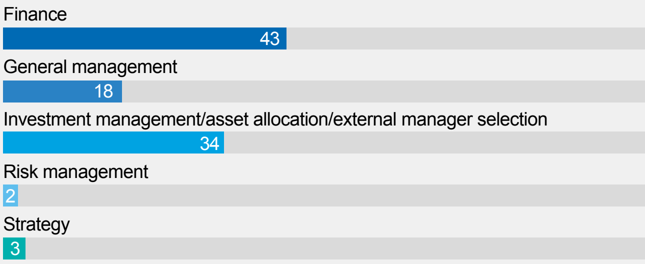
Source: The Economist Intelligence Unit

D3. Which is closest to your firm's assets under management (AUM) in US dollars? Select one. (%)

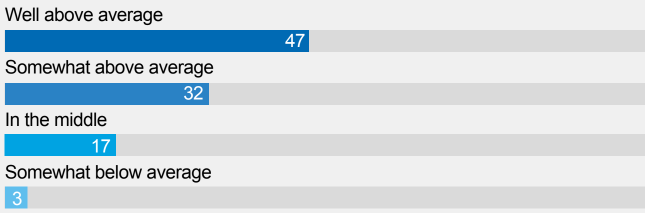
D4. Which of the following most closely describes the organisation you currently work for? Select one. (%)



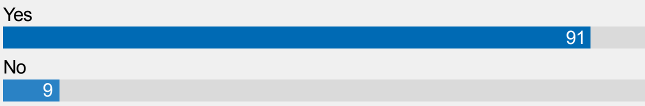
D5. What is your main functional role? Select one. (%)



D6. Broadly, which do you believe best describes your organisation's China exposure as compared to industry peers currently? Select one. (%)



D7. Does your organisation have a branch office or other operations within Mainland China? Select one. (%)



Source: The Economist Intelligence Unit

Investment Risks:
The value of investments and any income will fluctuate (this may partly be the result of exchange rate fluctuations) and investors may not get back the full amount invested.

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