Tapping into China's accelerating investment management expertise

Contrary to what some people might think, there is continued appetite among many global asset owners for Chinese securities – despite market noise and dynamic policymaking over recent months.

A common approach for the type of longer-term, patient capital synonymous with European pension funds, is to pinpoint key sectors as they strive to capitalise on continuing reforms and liberalisation measures to grow their China exposure as market access widens.

Focusing on short-term fluctuations in, for instance, asset prices and GDP growth misses the fact that China will continue to drive global growth for many years to come. Some funds with this conviction are even going a step further, planning standalone investment strategies and allocations.

Rapidly growing and maturing Chinese investment management industry

The continued development of China's asset management landscape is facilitating these trends. Although a relatively young industry, with the first domestic fund houses set up only just over 20 years ago, in 1998, recent research by Investment & Pensions Europe shows assets under management (AUM) had already increased to RMB124.39trn (€15.51trn) by 2020, second only to the US.

"The expansion of the industry has not only been in terms of AUM, but also in the levels of sophistication, maturity of investment philosophy and approaches to risk management," said Sau Kwan. President of E Fund Management (E Fund), China's largest and also an IPE Global top 100 fund manager. As of September 30th 2021, it has over RMB 2.6 trillion (USD 400 billion) in AUM.

Indeed, the path of E Fund's business reflects this. "We began in 2001 by offering long-only active equity mutual funds. Since then, we have gradually expanded our capacity and now offer a full range of passive equity, fixed income, multi-asset, quantitative and alternative strategies." explained Sau.

This has also come in parallel with the development of greater in-house expertise, through a commitment to grooming the next generation of Chinese portfolio managers.

Alongside an ever-wider product suite and talent development is the adaptability to the unique characteristics of the domestic market. "We are long-term, in-depth research-driven investors, which is essential to obtain sustainable returns in a market with noises and fast developments," added Sau.

In turn, Chinese asset managers like E Fund are broadening their horizons by opening offices in key international financial centres as they become more significant players in the global ecosystem.

Accelerating need for China exposure

As a result, the maturing Chinese local fund managers are well-placed to help global investors fulfil their objectives for more exposure to China as it continues to rise in prominence in global indices.

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For example, the 2021 results of OMFIF's latest survey of global public investors highlighted that as the lower-for-longer interest rate environment continues to drive funds away from traditional regions and haven assets, newer markets are set to benefit – China in particular.

More specifically, in equities, with an inclusion factor now of 20% in MSCI's indices, China A shares, H shares and ADRs represent over 40% of the MSCI Emerging Markets Index. At the same time, April 2019 marked the inclusion of onshore China bonds from the sovereign and some other government entities in the Bloomberg Barclays Global Aggregate (BGA) Index.

This aligns with the view of investment consultants such as Mercer: within equities, institutions should have a meaningful strategic allocation to China's onshore market that could represent 5% to 10% of an overall equity portfolio.

Yet taking such a step inevitably requires on-the-ground insights from local investment management partners that can provide the context behind economic growth and policy direction in relation to market reforms and liberalisation.

Digitalisation as a distinctive characteristic

A recent KPMG report, entitled "New Reality of Asset Management: China", highlights several defining characteristics of China's asset management evolution. What sets the local Chinese investment managers apart from their global peers is its reliance on digitalisation. Chinese market participants are less constrained than their Western counterparts in terms of legacy infrastructure and investment strategies.

This breeds a more innovative and tech-led approach to processes and products. The need for such forward-thinking business and operating models has become even more acute over the past 18 months.

"Chinese asset managers have become power houses for technology advancements."

Yong Guan, Chief Information Officer of E Fund Management

Further, with automation and artificial intelligence (AI) core to enhancing the investor experience, there is a growing need for asset managers to offer scalable processes and tools.

As China develops rapidly, asset managers must meet the need for greater research efficiency and depth by applying new technologies to search, sort and extract key information from vast amounts of data. They must also have access to more datasets and adapt to new sources of data.

"In today's challenging environment, asset managers must be resilient, agile and flexible," said Yong Guan, Chief Information Officer at E Fund, "Chinese asset managers have become power houses for technology advancements." As of September 30th 2021, for example, E Fund has filed 10 patents and 71 proprietary software copyright applications.

Steering investors down a responsible investment path

Inevitably, European pension funds – as with most global institutions – increasingly want environmental, social and governance (ESG) factors embedded in the investment approach when allocating to China.

Fortunately for these investors, this tallies with the direction in which the domestic industry is moving. A report released in February 2021 by the Asset Management Association of China (AMAC), for example, emphasised the ever-sharper focus of the domestic industry on green investment strategies.

While there are varying degrees of engagement, commitment is there. This is clear from the flurry of Chinese fund management companies becoming signatories to the UNPRI in recent years, including E Fund, one of the first signatories in mainland China.

This has, in turn, spurred a growing number of these asset managers to gradually build in-house ESG capabilities and launch sustainable investment products.

E Fund, among the early Chinese signatories to the UNPRI, had also shown the way forward in this area by forging a partnership with Dutch-based APG in 2016 – with the dual goals of return and impact. As reported by IPE in this year's May issue, for the five-year partnership, "engagement is where APG brought know-how to the venture. E Fund brought 'boots on the ground' research and access to corporates. "

FOOTNOTES

1 Source: AMAC, banking wealth management registration and custody centre, Insurance Asset Management Association of China (IAMAC), China Trustee Association, ATC Research