

Navigating short-term risks of trade disputes and geopolitics

In mid-June, **Tell Media Group**, in cooperation with **Aberdeen Standard Investments**, **Baillie Gifford** and **Robeco**, invited Swedish selectors to discuss Asian equities. Tell Media Group founder **Niklas Tell** moderated the roundtable.

By: **Niklas Tell** Photo: **Christer Salling**



To kick off the roundtable discussion, which was held at Nobis Hotel in central Stockholm in June, Niklas Tell started by asking the fund managers around the table to explain how they view Asian equities at the moment.

EWAN MARKSON-BROWN: "If we look at the long-term, this should be the fastest growing region. It provides a wonderful long-term picture but with short-term noise because of trade tensions and the strong US dollar. Valuations are cheap today but does that mean they will recover in 12 months? I have no idea. Does it mean that they will look good in 5 years? We think so."

HAUKE RIS: "We tend to be bullish on the region - also for the long-term reasons that Ewan pointed out - but currently we focus a lot on earnings growth and earnings revisions, which has been flat for Asia. This year we've seen negative earnings revisions, which is negative for Asia but things are as bleak elsewhere. On a relative basis, the major difference is valuations. In terms of timing, we would need to see the earnings picture improve for us to be more bullish and to say that this is a particularly good time to increase allocations."

YOOJEONG OH: "Despite the macro noise, what puts Asia in a different position to the rest of the world is that while there hasn't been anywhere for new capital to go, companies in the region have been paying down debt and they have been building their balance sheets. They've been preparing themselves for the time when they can start reinvesting again once the political situations calm down. Cash on balance sheets in Asia are much higher compared to

history and also compared to other regions. That's important as it gives companies room to manoeuvre. We very much agree on the long-term growth story that was mentioned earlier but we're also happy for companies to hold on to cash in the current situation."

NIKLAS TELL: I KNOW THAT MOST OF THE SELECTORS AROUND THE TABLE ARE NOT INVOLVED IN ASSET ALLOCATION BUT I WOULD STILL LIKE TO HEAR HOW YOU VIEW ASIA AT THIS POINT IN TIME.

HENRIK ANDERSEN: "We're neutral on emerging markets as a whole but slightly overweight on Asia based on the fact that we think the EPS [earnings per share] revision story has been overdone."

ANDERS LANDSTRÖM: "We're positive on Asia and also on emerging markets in general based on low valuations."

NIKLAS TELL: WHEN I STUDIED AT THE STOCKHOLM SCHOOL OF ECONOMICS A LONG TIME AGO, INVESTING IN EMERGING MARKETS WAS ALL ABOUT EXPLOITING THE INEFFICIENCIES COMPARED TO DEVELOPED MARKETS. WHAT ARE SOME OF THE INEFFICIENCIES YOU SEE TODAY?

EWAN MARKSON-BROWN: "I think you still have some of the standard inefficiencies such as lack of information and local politics and that has not changed. Yes, we do have more data but you still have the underlying noise. The biggest inefficiency we see is the difference between the long-term and the short-term. As a region, Asia is still very

much exposed to financial flows, operational gearing and exports and that means that both markets and valuations are volatile. That has led many investors to be short term, despite the positive longer-term trend in the region. I think the best way to generate alpha in Asia is the ability to sit back and look at the long-term trends and avoid the noise."

HAUKE RIS: "I would like to highlight corporate governance as one of the big inefficiencies in the system. We want to see more of the growth that you see in the region translate into earnings growth. We see improvements but it's a slow process."

YOOJEONG OH: "I think language remains a barrier in Asia. Having a team on the ground is important as it does give you better access. Having meetings without a translator can give you a better understanding as you hear directly how the person you're meeting is expressing himself or herself. We do highlight the fact that we have an ESG team but corporate governance has always been a core part of our investment process. A big difference is that we're now seeing companies asking for ESG meetings themselves. That's an important sign and it highlights the difference international investors have made in the region."

NIKLAS TELL: WE JUST HEARD WHAT THE MANAGERS ARE FOCUSING ON WHEN PICKING STOCKS IN THE REGION. WHAT ARE YOU FOCUSING ON WHEN SELECTING EXTERNAL MANAGERS FOR ASIAN EQUITIES?

ANDERS LANDSTRÖM: "It's a very familiar discussion but I guess the question is whether Asia is maybe becoming

more semi-efficient. We still, however, see Asia as a potential source of alpha - especially in the mid- and small-cap area. There are also big differences between countries, which could be another source of alpha for external managers even if country allocation is difficult to get right on a consistent basis."

PARTICIPANTS

- **SUSANNE BOLIN GÄRTNER**
Head of fund selection & ESG for external funds, Folksam
- **ANDERS LANDSTRÖM**
Head of manager research, Länsförsäkringar
- **HENRIK ANDERSEN**
Senior fund analyst, Large corporates & financial institutions, SEB
- **ANDREAS SÖDERSTRÖM**
Senior fund analyst, Movestic
- **YOOJEONG OH**
Investment director in the Asian equities team, Aberdeen Standard Investments
- **EWAN MARKSON-BROWN**
Investment manager in the emerging markets equity team, Baillie Gifford
- **HAUKE RIS**
Client portfolio manager Asia-Pacific equities, Robeco



SUSANNE BOLIN GÄRTNER
Folksam

Head of fund selection & ESG for external funds at Folksam. She joined in 2009 from Alecta where she was head of markets. She has previously also worked in different positions at SEB and at Max Matthiessen.



ANDERS LANDSTRÖM
Länsförsäkringar

Head of manager research at Länsförsäkringar since October 2013. He joined Länsförsäkringar as a senior manager research analyst in 2003.

HENRIK ANDERSEN: "The selection process is the same but I think it's important to understand the level of ESG integration as we think that's one way to exploit inefficiencies. We've also been selecting managers that are more geared towards A-shares."

NIKLAS TELL: THE US-CHINA DISPUTE HAS POTENTIALLY GOT AN IMPACT ON OTHER COUNTRIES AS WELL. IS IT EVEN POSSIBLE TO HAVE A VIEW OR HOW DO YOU DEAL WITH THIS RIGHT NOW?

HAUKE RIS: "I think you can have a view on the short-term effects but clearly the reason for why you ask it in that way is because it's very unpredictable because of the people in charge. For us as portfolio managers, the first question is how we're positioned and how we could be affected. You would expect exporters in China to be hurt the most but few of the true exporters are listed companies. That has led us to conclude that it will be more about second order effects, which could be that future layoffs hurts consumption and that we could see social unrest."

EWAN MARKSON-BROWN: "I think we see 2018 as a discontinuity - the year when the integration between China and the US stopped. We don't have a cold war any longer - it's a technology war and we will see a lot of tech investments in both China and in the US."

NIKLAS TELL: WHAT WOULD YOU SAY ARE THE BIGGEST RISKS OR CHALLENGES WHEN SELECTING MANAGERS IN THIS SPECIFIC AREA?

ANDREAS SÖDERSTRÖM: "I think one challenge for us is to evaluate to what degree fund managers are integrating ESG into their investment processes. It's easy to say you do that but it's hard for us to check. Another challenge is to manage time as we get a lot of phone calls from managers that want to come to present, not least managers of China A-shares."

NIKLAS TELL: CAPACITY WAS AN ISSUE IN EMERGING MARKET FUNDS SOME YEARS BACK. IS THIS AN ISSUE YOU LOOK AT WHEN SELECTING EXTERNAL MANAGERS?

HENRIK ANDERSEN: "It's something you need to keep an eye on but it obviously depends on what strategy you're looking at."

SUSANNE BOLIN GÄRTNER: "I think it's less of a problem today. It is, however, something you have to look out for, especially when it comes to small caps."

ANDERS LANDSTRÖM: "I agree that it's mostly a problem in small- and mid-caps. There you often find funds that are either too small or too big. In general, however, we tend to find better managers in Asian equities compared to broader emerging markets funds."

HAUKE RIS: "I also think that you could see the A-shares market opening up as an opportunity when it comes to capacity. It's a very big market with some 4000 stocks out of which at least 500 are very liquid."

NIKLAS TELL: HOW DO YOU VIEW THE INCLUSION OF A-SHARES INTO INDICES? DO YOU NEED TO REDEFINE YOUR ASIA EXPOSURE? SHOULD IT BE ASIA EX CHINA?

SUSANNE BOLIN GÄRTNER: "I think that will be coming as China is becoming too dominant in the Asia funds but I would not single out A-shares. I think you need to look at Asia versus China and then both A-shares and H-shares."



YOOJEONG OH: "The A-shares market has been great for us and we've had people on the ground looking at A-shares since 2007 - all fluent in mandarin of course. When we launched our A-shares fund, it was very much run in the same way as we run other strategies in the region and in the beginning it was some 60 per cent mid-caps. Over time, the fund has become more large-caps but that's thanks to the growth of our holdings and the development of the market."

HENRIK ANDERSEN: "What would you say are the main differences between following an A-shares company from an H-share company as an analyst?"

YOOJEONG OH: "Companies in the A-shares market are typically more domestically focused and that's what we want to capture in the A-shares market as well - the growth of the domestic consumer. Companies in the H-shares market are typically more internationally focused."

HENRIK ANDERSEN: "What does it mean for you as an analyst when you prepare meetings with these companies? Are there any differences?"

YOOJEONG OH: "I would say in general, the broad questions are the same. That said, we would typically spend more time on governance questions when it comes to A-shares companies, simply because we don't know them as well. Some of our holdings in India, for example, are companies that we've held for 20 years and over that time we've built a track-record and we know them very well. For newer companies, we need to understand better how they think and make money within their operating environment. That means that even if we don't know the company itself,

we will typically know a competitor, customer or a supplier and can get a feel for a company that way."

HAUKE RIS: "Many times it can also be a language issue with H-shares companies typically reporting in English whereas many A-shares companies only releasing their reports in Mandarin."

NIKLAS TELL: WITH THE INCLUSION OF MORE A-SHARES COMPANIES IN INDICES, HAS THAT LEAD YOU TO REVIEW THE MANAGERS YOU'RE CURRENTLY USING FOR ASIAN EQUITIES TO MAKE SURE THEY HAVE THE CAPABILITY?

ANDERS LANDSTRÖM: "It's absolutely something you must be aware of. Some are very good and have done it for a long time with local representation and staff that speak the language etc. Others are behind the curve in terms of resources but still invest in A-shares, which is more of a question mark. Another thing to be aware of is that most international managers that go into A-shares have a quality focus. With everyone focusing on the same companies, you risk getting exposure to the same companies regardless of which manager you select."

NIKLAS TELL: HOW WOULD YOU COMPARE INDIA AND CHINA AND WOULD YOU PREFER ONE OVER THE OTHER?

EWAN MARKSON-BROWN: "We like both countries but they will give you very different portfolios. If you only compare the quality of corporate governance and management, India is far better where you have a legal system that is British and a government that tends to stay out of things."



HENRIK ANDERSEN
SEB Large Corporates & Financial Institutions
Senior fund analyst, manager research at SEB. He joined SEB in 2016 from Nordea in Copenhagen where he was a senior analyst. He has previously also worked as a senior fund analyst at Danske Bank in Copenhagen.



ANDREAS SÖDERSTRÖM
Movestic
Senior fund analyst at Movestic. Prior to joining Movestic in August 2017, he was a manager research analyst at Länsförsäkringar. He has previously also worked as a fund analyst at JRS Asset Management and at Carnegie Private Banking.

That means that we can focus more on the companies themselves. In China, you don't have control of the government and you don't really know what they're doing but the market in China is far bigger and will give you more technology exposure and innovative companies."

YOOJEONG OH: "One big difference is how capital has been allowed to be allocated. If you think of China, you've not had free capital allocation and they've allowed companies such as Tencent and Alibaba to be built domestically to be champions. If you think of India, it has always been more open and it has allowed capital to be allocated to where it's needed. India doesn't have their own domestic tech champions in the same way as China but we do see a lot of entrepreneurial activities happening also in technology. It's a deep market that has proven to be a fertile hunting ground for us."

EWAN MARKSON-BROWN: "If you look at the last five years, we've had a very concentrated portfolio in China and a far more diverse portfolio in India. That's just a result of the fact that there has been fewer opportunities in China. There's a tendency to build monopolies or oligopolies in China and if you can figure out which company will be the next one that's great. This doesn't happen in India. There are far more 'winners' in India but if you can find them there are bigger 'winners' in China."

HAUKE RIS: "If you're sensitive to valuations, which we are as value investors, there's a tendency to look more at China and Korea compared with India."

SUSANNE BOLIN GÄRTNER: "With the trade war that's going on, I think India is one of the winners. Would you agree?"

YOOJEONG OH: "Yes, they have been relatively insulated. However, as an open economy it's not fully insulated and we've seen tariffs on India as well. It's something that we're following. It's not risk free, which is why we focus on continuous due diligence."

NIKLAS TELL: LOOKING AHEAD, WHAT ARE SOME OF THE BIGGEST RISKS FOR ASIAN EQUITIES?

EWAN MARKSON-BROWN: "I think the biggest risk is that we come to 2030 and Asia hasn't continued to grow and it's not the centre of the world economy. Can the US slow China down? Yes, but it's almost irrelevant compared to what the Chinese government can do themselves. Can they reform and improve productivity? We think that's an absolute yes in India and it should be a yes in China. If local governments allow things to happen, we will see some countries in 10 to 15 years being middle class and approaching developed markets but we will also have countries in the region that will still be emerging markets."

HAUKE RIS: "That's in the very long term. If you take a shorter-term view, it will have to be the trade dispute and geopolitics."

YOOJEONG OH: "Another risk is domestic regulation. We tend to stay away from companies that are active in a regulated environment. It adds an unnecessary risk to the portfolio as we've seen how regulation can be changed with very short notice. It's a known unknown. Longer term, I would agree with Ewan. We back companies that should benefit from the long-term trends in the region and if that doesn't happen, it will of course be bad for the companies we hold."

EWAN MARKSON-BROWN: "We have negative interest rates in most of Europe now and I think it's likely that the interest rate in the US is going towards zero over the next five years. The big question is what that will mean for our region."

NIKLAS TELL: WE HAVE TALKED ABOUT SMALL CAPS AND LARGE CAPS. WHAT ABOUT VALUE VERSUS GROWTH IN ASIA?

ANDERS LANDSTRÖM: "I think that is less relevant in Asia but it's something that we look at and you must be aware of it. I think quality is a more dominant factor in Asia and this can also be linked to ESG and sustainability."

NIKLAS TELL: DO YOU PREFER ONE STYLE OVER THE OTHER?

ANDERS LANDSTRÖM: "Not really. It's a growth-oriented market with some 80 per cent of managers being growth-oriented."

HAUKE RIS: "We're value investors and I think growth versus value is an important factor to consider. It comes down to investment beliefs. Generally, people turn to Asia for growth, which makes sense, but it doesn't have to be accessed via a growth manager. Value is a powerful anomaly that works globally and it also works in Asia. To us, it makes sense, also in a growth environment, to have a high valuation discipline and look for stocks that are discounting very low expectations. When the fundamentals are right and cash flows are good, it can make for an interesting strategy. That said, if you look at the last decade we've had a long streak in favour of growth and the question is what to do going forward. At the end of the day, I guess it comes down to investment beliefs and your take on mean reversion."

EWAN MARKSON-BROWN: "I think you have these long cycles of growth for different types of companies and recently we've actually moved some of the portfolio out of tech and into financials. Right now, it may look like value

but we actually think of these companies as latent growth companies."

NIKLAS TELL: A LOT OF FLOWS TODAY GO THROUGH ETFs AND OTHER PASSIVE VEHICLES. DOES THAT DISTORT HOW WE LOOK AT VALUE VERSUS GROWTH AS THE MARKET WILL KEEP ON PUSHING GROWTH COMPANIES?

HAUKE RIS: "It's a fair point. You do have some big companies in China that are classified as growth and they are also beneficiaries of passive flows. We tend to look through this, even if it is taking a long time. We have to be pragmatic and there's nothing wrong with growth in itself. It's more about being mindful of what we pay for that growth. In this environment, I think it's been a factor for pushing growth higher."

EWAN MARKSON-BROWN: "I think we've benefitted from owning growth companies in that sense. There's always a risk of that reversing. If you invest for the longer term, I don't think it matters but over the shorter term you do get these ups and downs due to flows."

ANDERS LANDSTRÖM: "I agree that it should even out over time but it's a new factor that's becoming more important to be aware of."

YOOJEONG OH: "ETF flows doesn't change how we select stocks, even if it has impacted us over the years. We stick to our quality-focused process regardless of what the current trend in the market is."

SUSANNE BOLIN GÄRTNER: "I also think it's important to know if managers dare to stay out of big names as that will





YOOJEONG OH

Aberdeen Standard Investments
Investment director on the Asian equities team at Aberdeen Standard Investments. She joined Aberdeen Asset Management in 2005 and was initially a member of the UK and European equities team in London before moving to Singapore.



EWAN MARKSON-BROWN

Baillie Gifford
Investment manager in the emerging markets equity team at Baillie Gifford and co-portfolio manager for the Asia ex Japan strategy. He previously worked at Merrill Lynch and Newton as an Asia Pacific portfolio manager.



HAUKE RIS

Robeco
Head of client portfolio management for Robeco fundamental equity and client portfolio manager for Asia-Pacific equities since October 2012. Prior to joining Robeco, he was a portfolio manager at Kempen & Co in Amsterdam, running discretionary private client portfolios.

have a big short-term impact. A manager will look very different to the market as these stocks go up and down.”

YOOJEONG OH: “Sometimes the companies that we don’t own can be the biggest risk bets against the benchmark, such as Alibaba in China and Reliance in India. Even if we don’t own them right now, we do follow them and if our arguments for not owning them changes we will of course look at the investment case again.”

EWAN MARKSON-BROWN: “We almost tend to do the opposite. We focus on a small sub-set of the market and expect our winners to be in what we own. What we don’t own, we don’t look at.”

NIKLAS TELL: WHEN YOU HAVE DONE YOUR RESEARCH AND ARE MEETING WITH MANAGERS, WHAT ARE SOME OF YOUR KEY QUESTIONS?

HENRIK ANDERSEN: “Understanding the decision-making processes and team dynamics are key areas to us. We have recently integrated behavioural aspects into our research to get a more complete picture. This also includes looking for mitigating factors, as well as recognising our own potential behavioural biases as fund analysts.”

SUSANNE BOLIN GÄRTNER: “I think one important question is to understand how managers buy and sell holdings. Who makes the decision? Is it one person or is it a team effort?”

ANDERS LANDSTRÖM: “In general, I like to understand if what we have identified as strengths and weaknesses are something the manager also sees. Basically trying to match what we see in the quant research with the qualitative gathering of information.”

EWAN MARKSON-BROWN: “One question that I don’t get asked that I think is interesting would be: Are you happy? Do you enjoy your job? Those firms where people enjoy coming to work and enjoy what they do tend to do well. If there are disruptions, people tend to focus on that rather than on finding great companies.”

NIKLAS TELL: THAT’S INTERESTING BECAUSE THAT COMES DOWN TO THE COMPANY CULTURE, WHICH IS HUGE BUT I GUESS ALSO VERY DIFFICULT TO UNDERSTAND BASED ON ONE OR TWO MEETINGS.

ANDERS LANDSTRÖM: “It’s tricky and I think the best way is to meet with different people in the organisation. That way you can get some sort of understanding of how a company works.”

ANDREAS SÖDERSTRÖM: “One way to know if a manager is happy at the job or not and to get some sense on the culture is to look at the staff turnover. If the staff is happy, they tend to stay.”

EWAN MARKSON-BROWN: “We spend a lot of time on culture when we research companies, especially if we’re talking about tech companies that rely on people to come up with innovations. In the long term, it makes a huge difference. It should be similar when fund selectors look at asset managers.” ●