

How do you invest sustainably in China?

Jack Nelson



Risk factors

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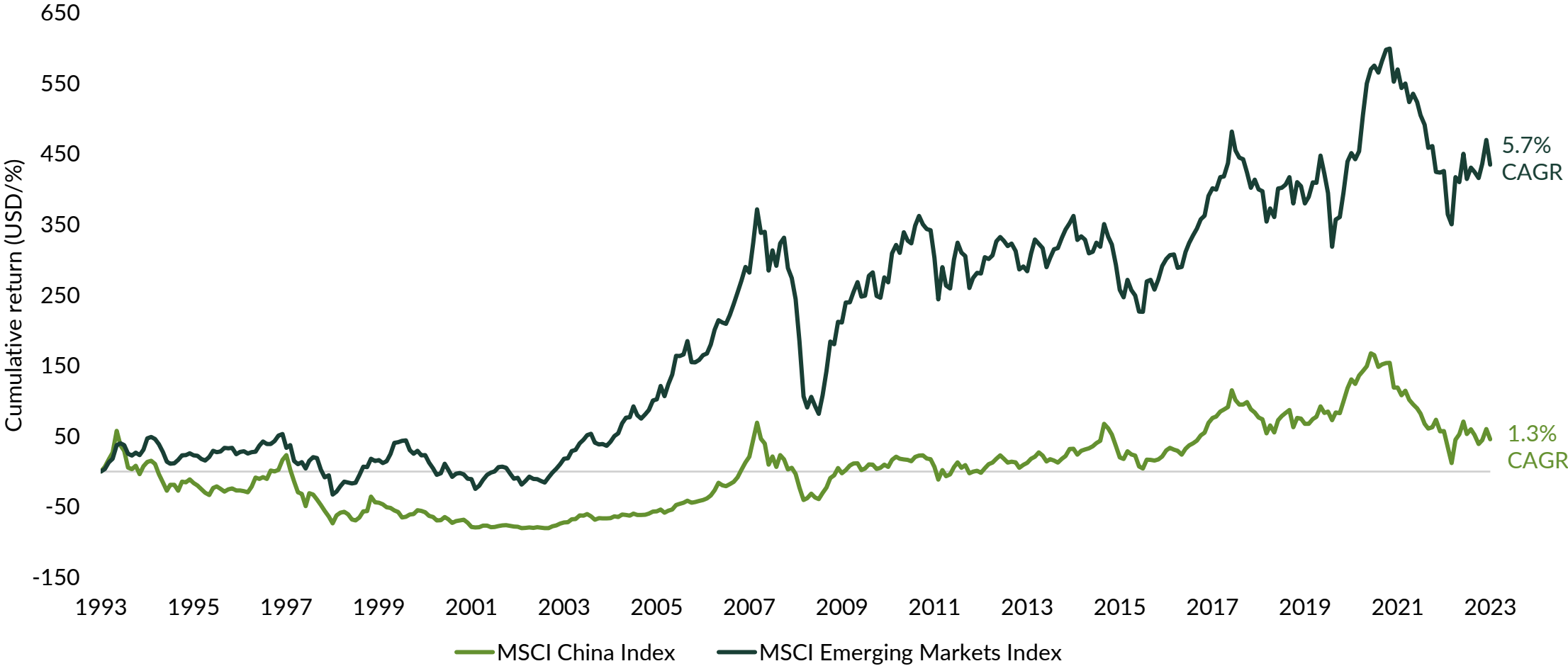
Shanghai 1990



Shanghai 2018



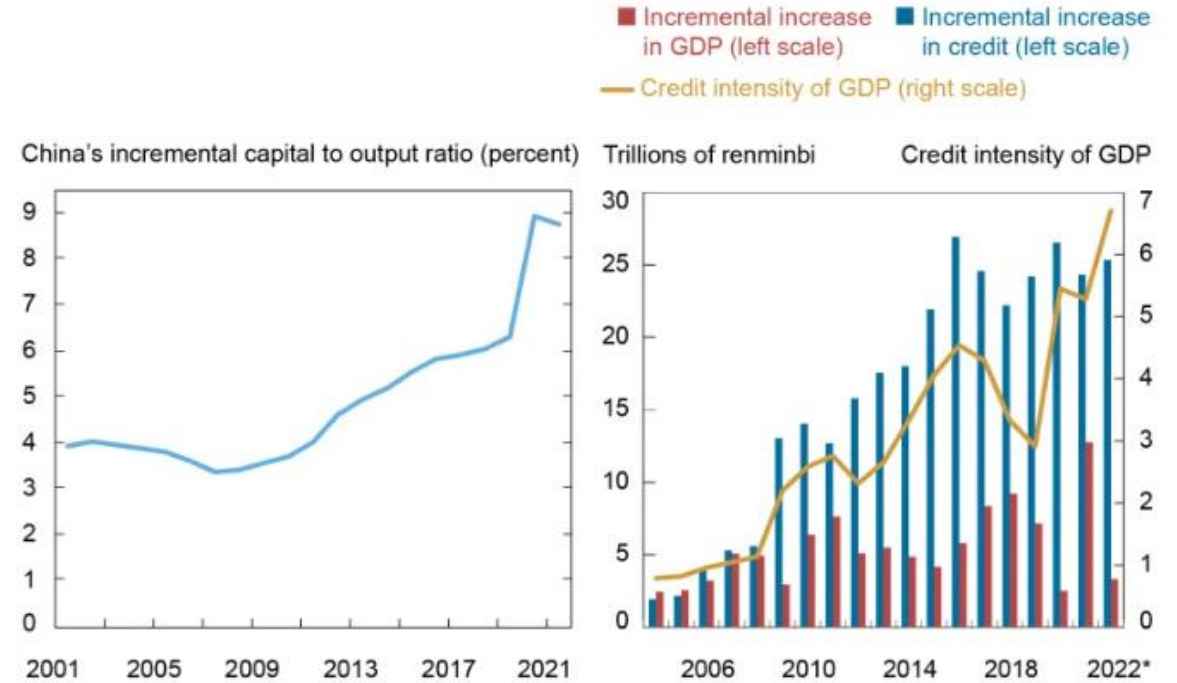
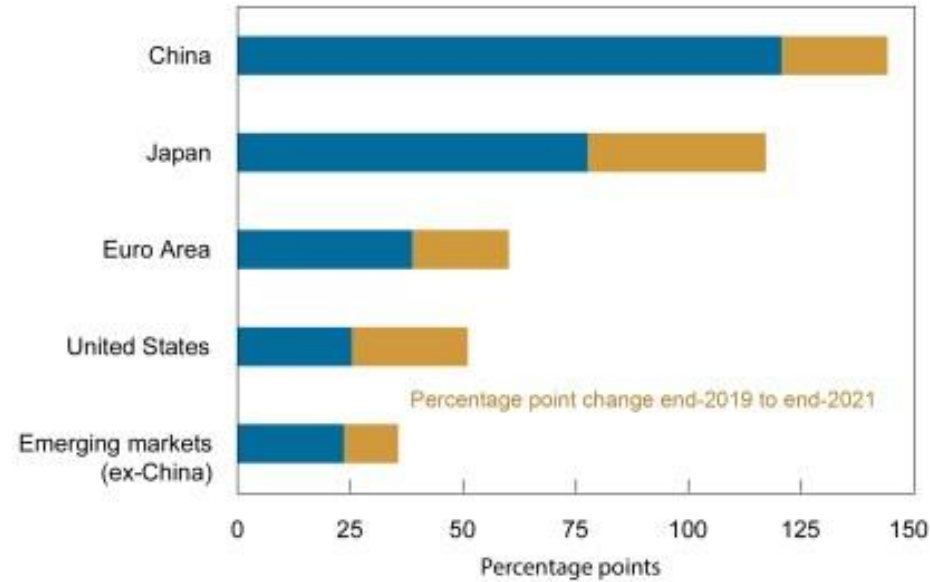
Strong development but weak returns



These figures refer to the past. Past performance is not indicative of future performance. For investors based in countries with currencies other than USD, the return may increase or decrease as a result of currency fluctuations. Source: FactSet as at 31 August 2023.

The end of the road?

Change in credit-to-GDP (2007-2021)

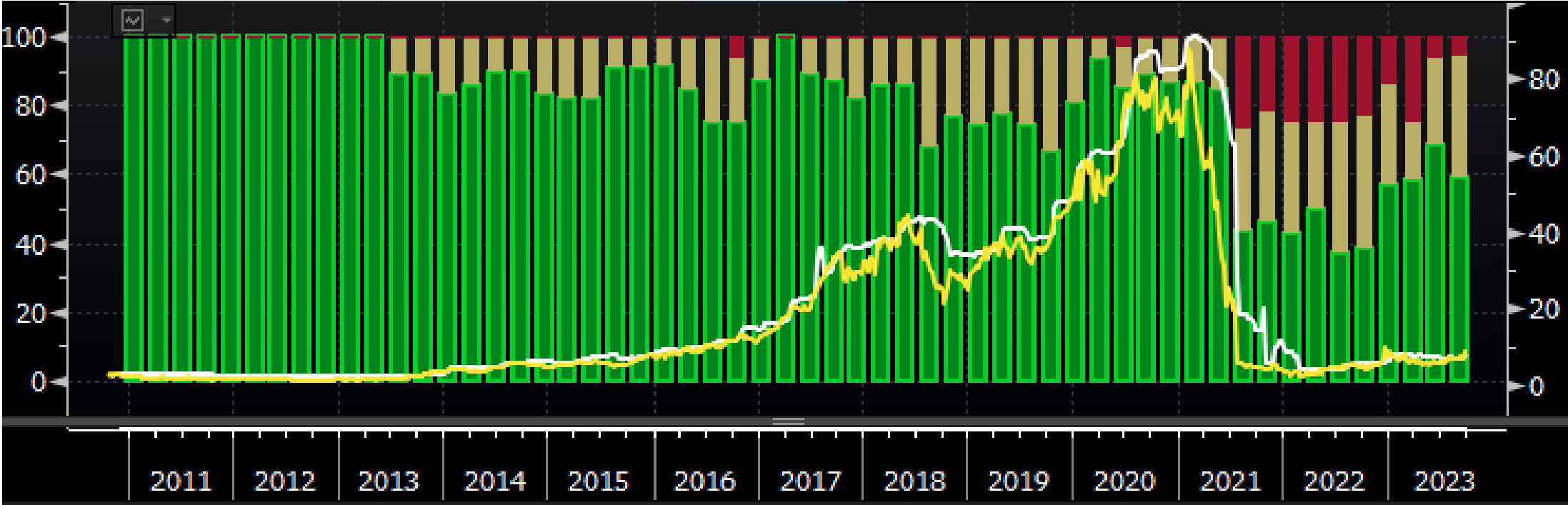


Source for LHS: Bank for International Settlements via CEIC. Source for RHS: Author's calculations, based on data from the National Bureau of Statistics of China and the People's Bank of China via CEIC. Notes: Left panel shows five-year moving average. Incremental capital to output ratio (ICOR) is calculated as the ratio of gross fixed capital formation to GDP divided by real GDP growth. In right panel, data shown for 2022 are through June*. Credit intensity of GDP is the ratio of the incremental increase in credit over the incremental increase in GDP on a three-year moving average. GDP refers to gross domestic product, the monetary value of all the finished goods and services produced within a country's borders in a specific time period.

Roads to nowhere?



Capital serves the state



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The Khodokovsky Risk

Alibaba Founder Hiding Out

Tokyo

The Times, 30 November 2022

**REN ZHIQIANG 18 YEARS IN PRISON
AFTER CALLING XI ZINPING: "A CLOWN"**

The Guardian, 23 September 2020

**HNA Chairman falls to his
death in France**

Reuters, 4 July 2018

**Bao Fan, top Chinese banker, the latest CEO to go
missing**

CNN, 17 February 2023

CEO whisked out in a wheelchair – jailed for 13 years

The Guardian, 19 August 2022

Paucity of reliable financial information

KPMG sued for \$830m over “appalling” Chinese audit
Financial Times, 5 September 2022

Ernst & Young Says It Isn’t Responsible for Luckin Coffee’s Accounting Misconduct
Wall Street Journal, 16 July 2020

Evergrande Says PWC Resigns After 2021 Audit Disagreements
Bloomberg, 16 January 2023

China instructs state firms to phase out big four auditors
The Guardian, 22 February 2023

China’s Hanergy Thin Film unveils huge loss as auditor flags concerns
South China Morning Post, 11 January 2023

Governance issues

Company 1

- **Not a research center.** Evidence indicates that ██████████ will operate a hotel in Engelberg, and misled shareholders by calling it a research center.
- **Other Swiss hotel properties.** ██████████ unlisted parent owns several hotels in Switzerland, creating opportunities for undisclosed related-party transactions.
- ██████████ **construction company.** A construction company partly owned by ██████████ sold a Swiss property to ██████████ parent company, creating opportunities for undisclosed related-party transactions.
- **Hot-headed chairman.** ██████████ statements show he does not understand shareholder concerns regarding public disclosures, or does not care.

Company 2

- **Fraud conviction raises governance concerns.** Government records show that companies owned by ██████████ chairman and family members, including his ex-wife, used fake and fraudulent invoices to dodge taxes, and were punished for other financial wrongdoing.
- **Senior executives lack relevant backgrounds.** ██████████ four co-founders are very lucky, talented, or something else because none have CVs that would presage success in running a huge company selling automation components.

What is risk?

Relative

$$\text{VaR}_{1-\alpha}(X) \leq \text{RVaR}_{\alpha,\beta}(X) \leq \text{CVaR}_{1-\alpha}(X) \leq \text{EVaR}_{1-\alpha}(X),$$

where

$$\text{VaR}_{1-\alpha}(X) := \inf_{t \in \mathbb{R}} \{t : \Pr(X \leq t) \geq 1 - \alpha\},$$

$$\text{CVaR}_{1-\alpha}(X) := \frac{1}{\alpha} \int_0^\alpha \text{VaR}_{1-\gamma}(X) d\gamma,$$

$$\text{RVaR}_{\alpha,\beta}(X) := \frac{1}{\beta - \alpha} \int_\alpha^\beta \text{VaR}_{1-\gamma}(X) d\gamma,$$

$$\text{EVaR}_{1-\alpha}(X) := \inf_{z > 0} \{z^{-1} \ln(M_X(z)/\alpha)\},$$

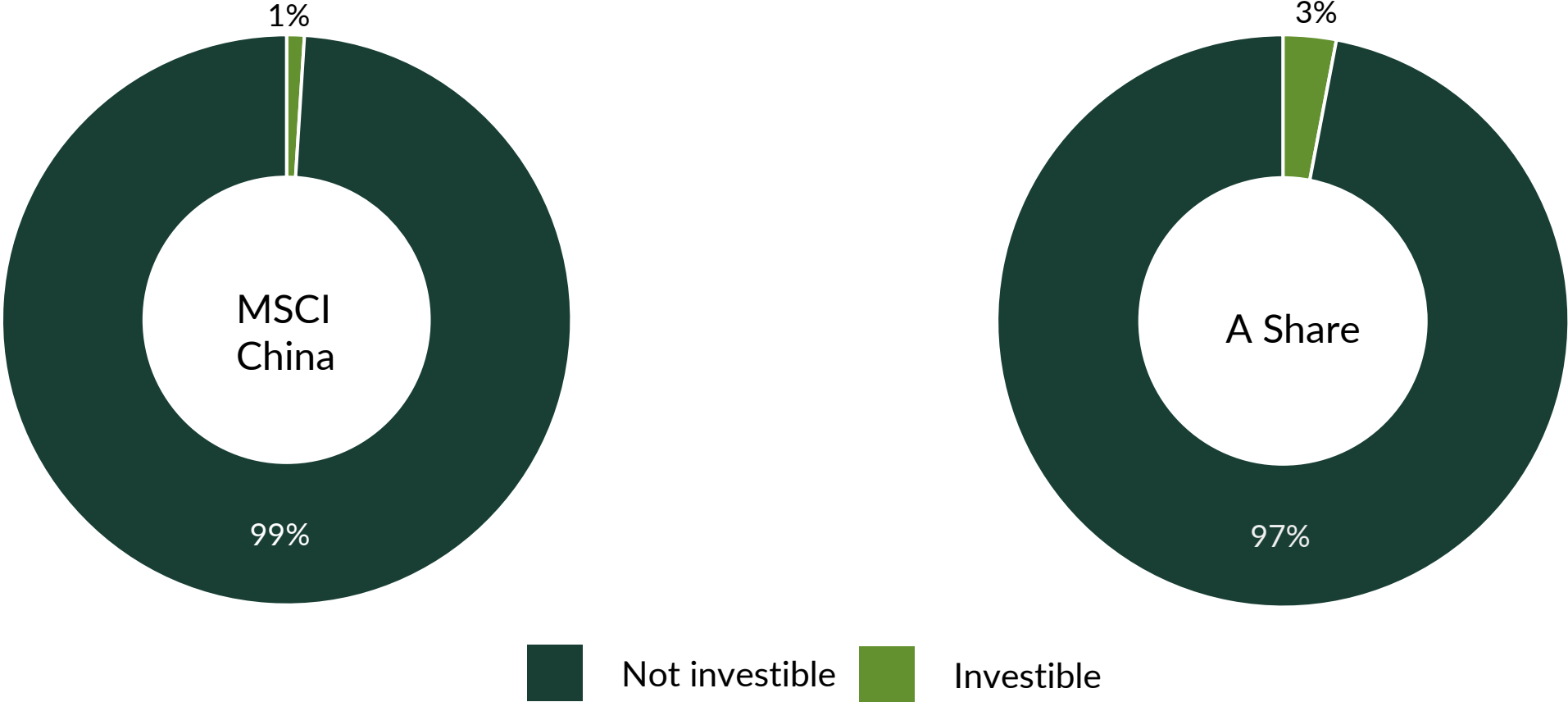
What is risk?

Or absolute



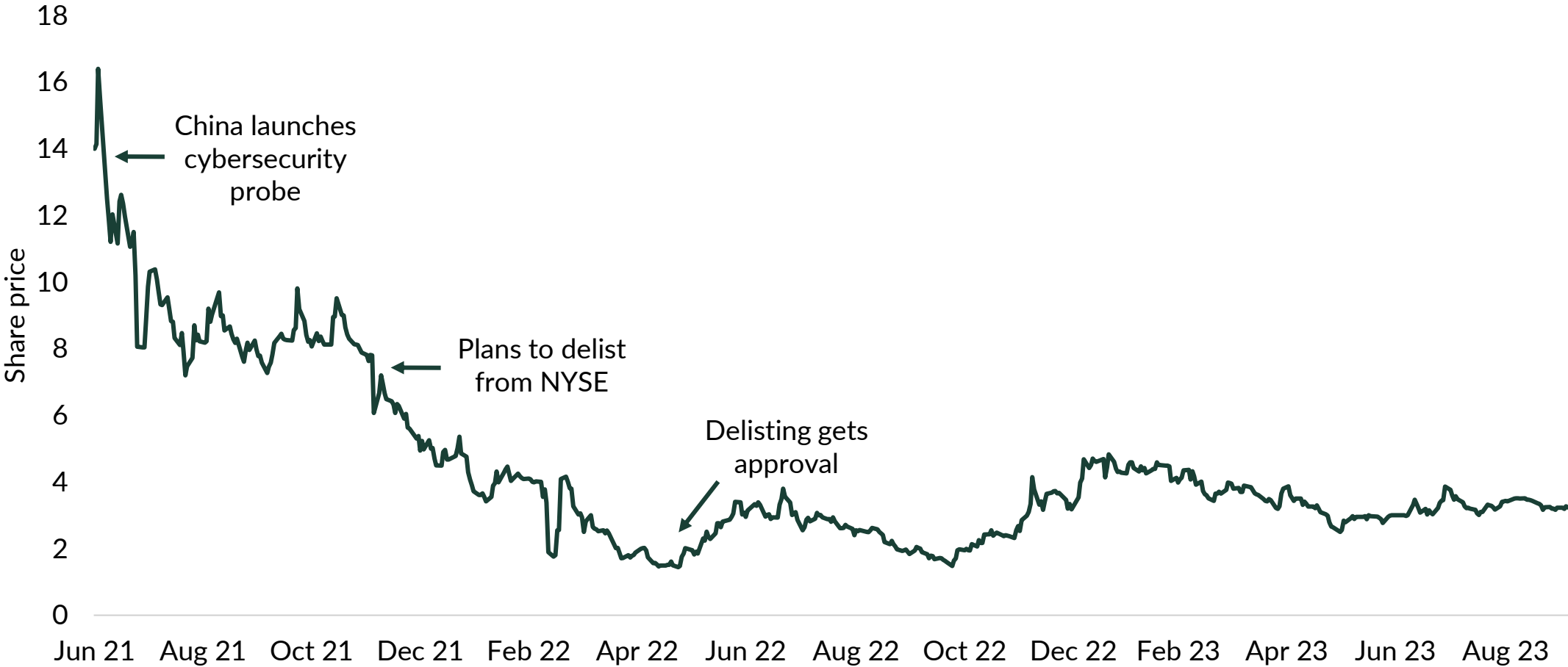
Indices are not the opportunity

Number of companies we see as investible - largest 100 companies of each index



Source: Stewart Investors.

Socially unacceptable business models



These figures refer to the past. Past performance is not indicative of future performance. Source: Bloomberg as at 5 October 2023.

Alignment



Sustainable development challenges



Companies not countries

Quality Chinese companies and their global peers

Industry	Company	Market cap (USDbn)
Third party verification	Centre Testing International	4
	SGS	15
Software for building industry	Glodon	5
	Autodesk	43
Industrial automation and electrification	Shenzhen Inovance Tech	25
	Siemens	116
Pharmacy chains	Yifeng Pharmacy Chain	5
	CVS	90
Analog semiconductors	Silergy Corp	4
	Texas Instruments	144

Companies held in our portfolios.

Source for market capitalisation: S&P Capital IQ as at 28 September 2023.

Glodon



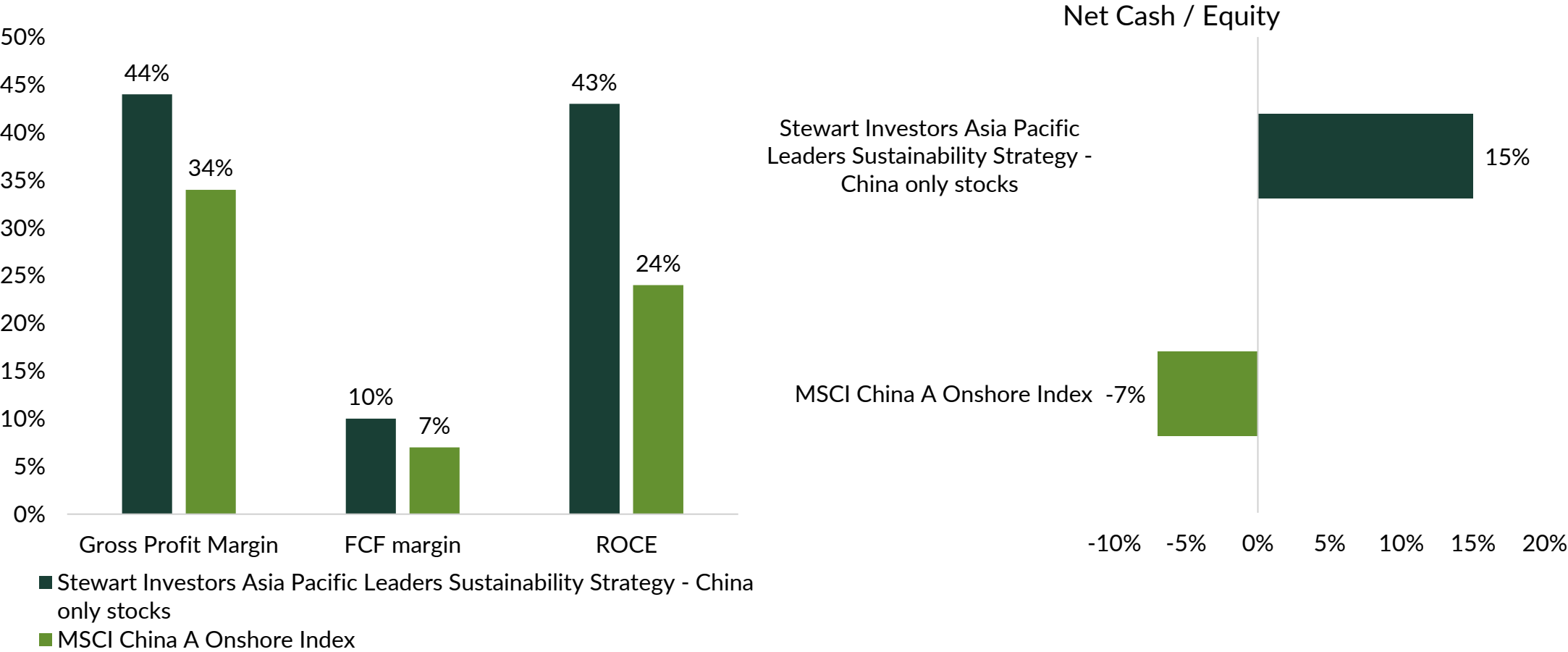
Shenzhen Inovance



Yifeng Pharmacy Chain



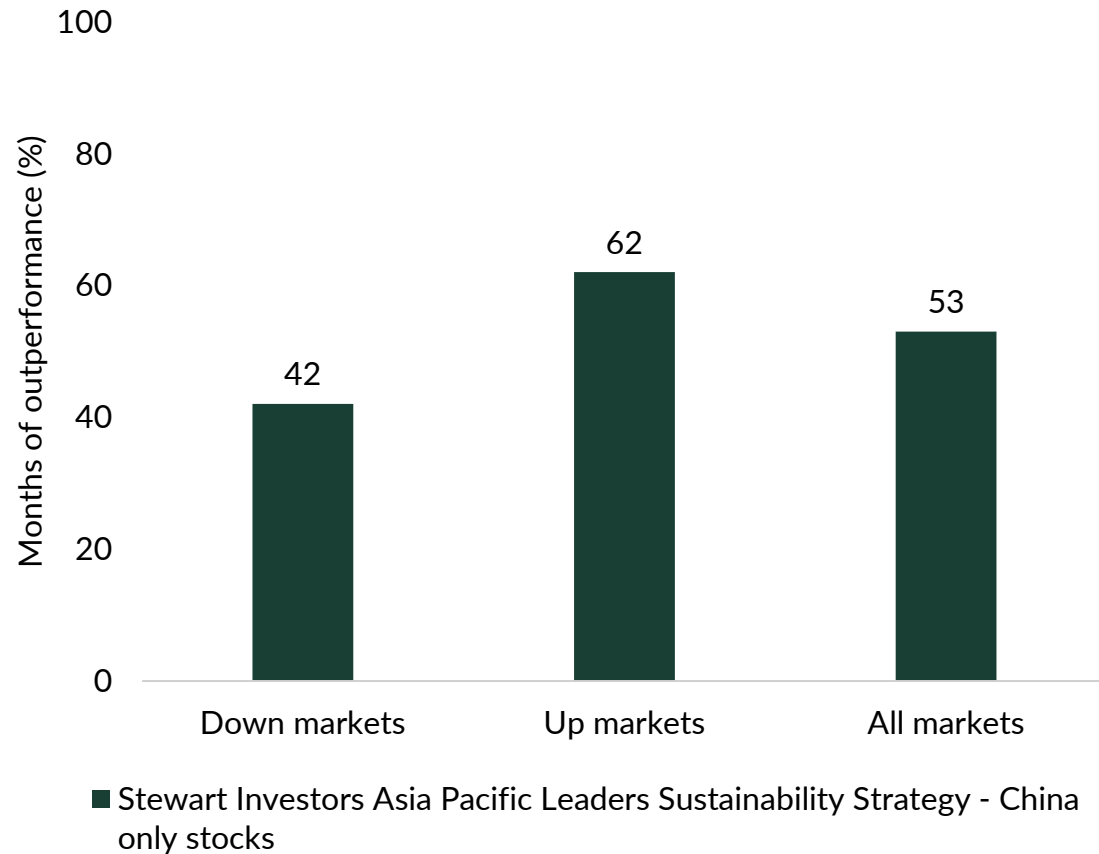
Outcomes of our philosophy



These figures refer to the past. Past performance is not indicative of future performance. For investors based in countries with currencies other than GBP, the return may increase or decrease as a result of currency fluctuations. Source: FactSet. Data shown is the weighted average of all investments as at 30 September 2023 for the Chinese stocks in a representative Stewart Investors Asia Pacific Leaders Sustainability account and MSCI China A Onshore Index. Consolidated figures used for all company data. Figures are subject to rounding and exclude financials. It is not a recommendation or solicitation to purchase or invest in any fund. Differences between the representative account-specific constraints, currency or fees and those of a similarly managed fund or mandate would affect results.

Outcomes of our philosophy

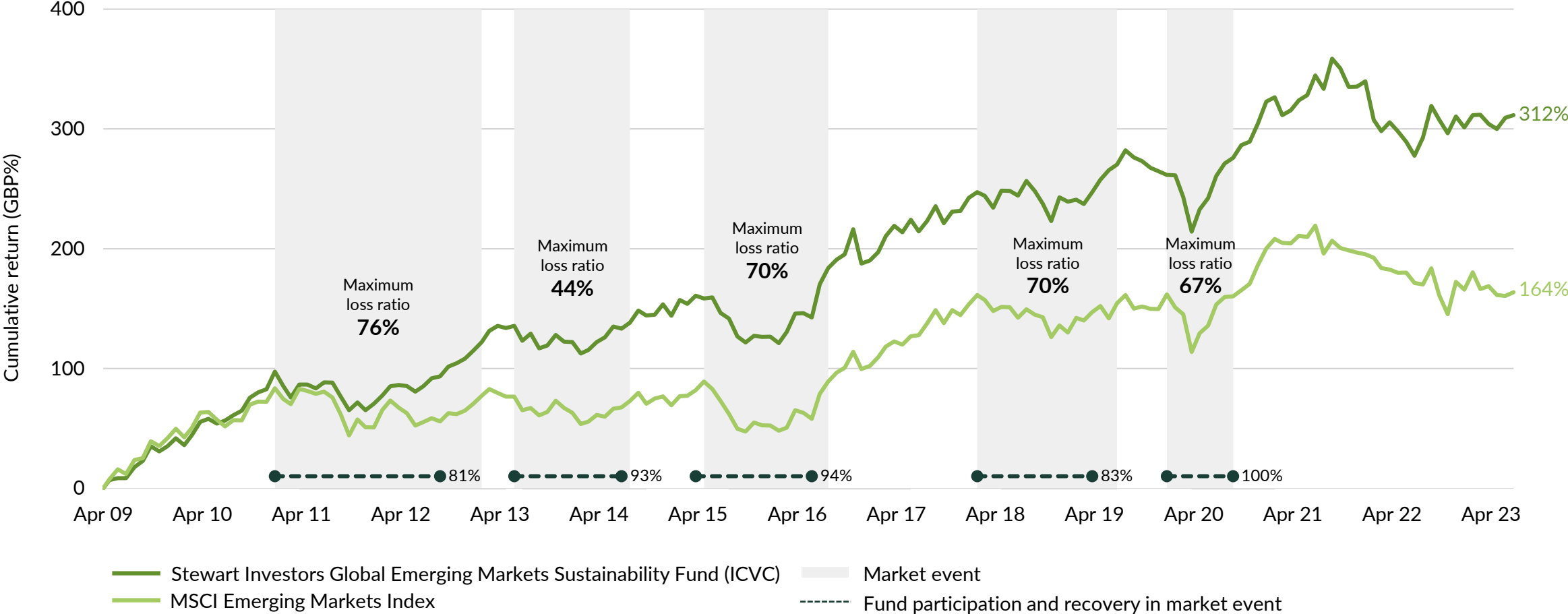
Outperformance in particular markets



These figures refer to the past. Past performance is not indicative of future performance. For investors based in countries with currencies other than GBP, the return may increase or decrease as a result of currency fluctuations. Source: Stewart Investors as at 30 September 2023, covering the period 31 December 2019 to 30 September 2023. Performance is calculated on a gross of fees basis. The data shows the performance of Chinese stocks held in a representative Stewart Investors Asia Pacific Leaders Sustainability account. Source for MSCI China A Onshore Index: FactSet, income reinvested gross of tax. It is not a recommendation or solicitation to purchase or invest in any fund. Differences between the representative account-specific constraints, currency or fees and those of a similarly managed fund or mandate would affect results.

Outcomes of our philosophy

Long-term performance profile



These figures refer to the past. Past performance is not indicative of future performance. For investors based in countries with currencies other than GBP, the return may increase or decrease as a result of currency fluctuations. Source for Fund: Lipper IM/Stewart Investors. Performance data is calculated on a net basis by deducting fees incurred at fund level (e.g. the management fee and other fund expenses), save that it does not take account of initial charges or switching fees (if any). Income reinvested is included on a net of tax basis. Source for index: FactSet, income reinvested net of tax. Performance calculated since launch of the GBP B accumulation share class on 8 April 2009 to 30 June 2023. Market event periods determined by Stewart Investors. Fund participation shows the time exposure of the Fund performance to the market event. The maximum loss ratio is the ratio of the Fund's maximum loss compared to the index's maximum loss during the same market event. For full Fund performance tables please refer to the performance slide.

Is it possible to invest sustainably in China?

Our focus on risk in absolute terms

- > Allows us to say no
- > Emphasises quality and sustainability positioning
- > Requires independent thinking
- > Offers downside protection and long-term growth



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