

Breakout Session 2: Navigating geopolitical risks and opportunities in EM equities – a spotlight on China and India

2024 Frontier Advisors Annual Conference

Chair:



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— Opinion

Get ready for a riskier world

The causes and effects of geopolitical risk events are complex and multi-faceted. Events can take many years to develop and are almost impossible to predict.

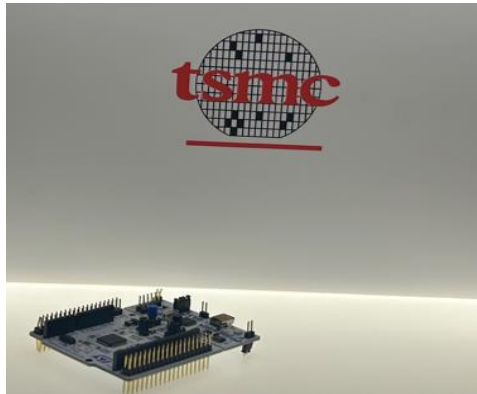
Raphael Arndt

Jun 15, 2024 - 5.00am

Source: AFR



Source: Rayliant Global Advisors



Source: Frontier Advisors, C WorldWide



Source: Financial Times

Australia's China challenge

PM shrugs off concerns over Chinese ownership of lithium plant



Chinese Premier Li Qiang's planned visit to the lithium plant in Perth highlights the emerging global competition over critical minerals.

Jun 12, 2024 | Andrew Tillett

Source: AFR

Agenda

- Our speakers
- Frontier perspectives – setting the scene
- PM perspectives – practical approaches to assessing geopolitical and EM sovereign risk
- Asset owner perspectives:
 - EM allocation considerations for a new world order
 - Active risk budgeting, delegated versus standalone, flexible implementation, EM ex-China

Setting the scene

EM index evolution

- Nature of asset class is that opportunities always ‘emerging’, others fading/exiting
- Key drivers are demographics, economic and ‘geopolitical’

MSCI EM index evolution

1988	ADDITIONS																	2023																							
Argentina																		Brazil	Peru																						
Brazil			Columbia															Chile	Philippines																						
Chile			India															China	Poland																						
Greece			Pakistan		China															Colombia	Qatar																				
Jordan			Peru		Israel		Czech Rep															Czech Republic	Saudi Arabia																		
Malaysia	Indonesia		Sri Lanka		Poland		Hungary		Egypt		Qatar		Argentina					Egypt	South Africa																						
Philippines	Turkey		Korea		Venezuela		South Afr.		Taiwan		Russia		Morocco		Greece		UAE		Pakistan		Saudi Arab.		Kuwait		Greece	Taiwan															
Portugal	1989	1992	1994	1995	1996	1997	2001	2006	2008	2009	2010	2013	2014	2017	2019	2020	2021	2022					Hungary	Thailand																	
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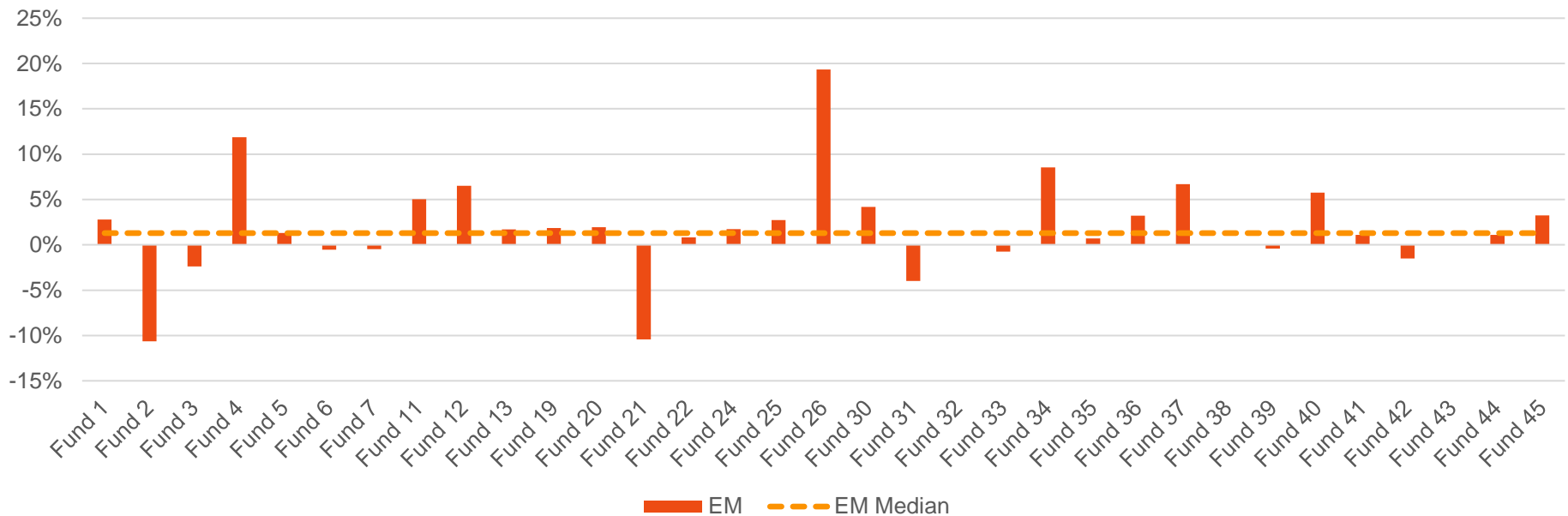
Source: MSCI, Frontier Advisors

Setting the scene

Investor positioning

- Asset owners have reduced strategic and active allocations to EM, despite relative valuations
- Multiple drivers including China risk

Super fund exposure to EM (versus MSCI ACWI ex-Aus) at 30 June 2023



Source: eVestment, Frontier, Portfolio Holdings Disclosure

Setting the scene

Investor approaches to EM are evolving

- The case for standalone EM country allocations is not new
 - But motivations are broader and rationale perhaps stronger
- Pros & cons – integrated, standalone or carve-out

Carve out example (EM ex China + China)

Carve out (e.g. EM ex-China + China)

Suitable for funds with relatively high appetite for complexity and less fee sensitivity that can allocate specialist resources to manage asset allocation decisions (if deviating from benchmark weight); or investors seeking greater control over their specific country exposures (e.g. China)

Pros

- Better calibration of overall and specific EM exposures carved out. This can lead to improved implementation efficiency (including divestment) and more targeted determination of a portfolio's underlying exposure in idiosyncratic markets like China.
- Investment manager that has specialist knowledge in Chinese markets, rather than an EM manager with a more generalist approach to emerging markets.
- Declining correlations with rest of EM implies diversification benefits can be achieved by separating and re-weighting the likes of China and India.

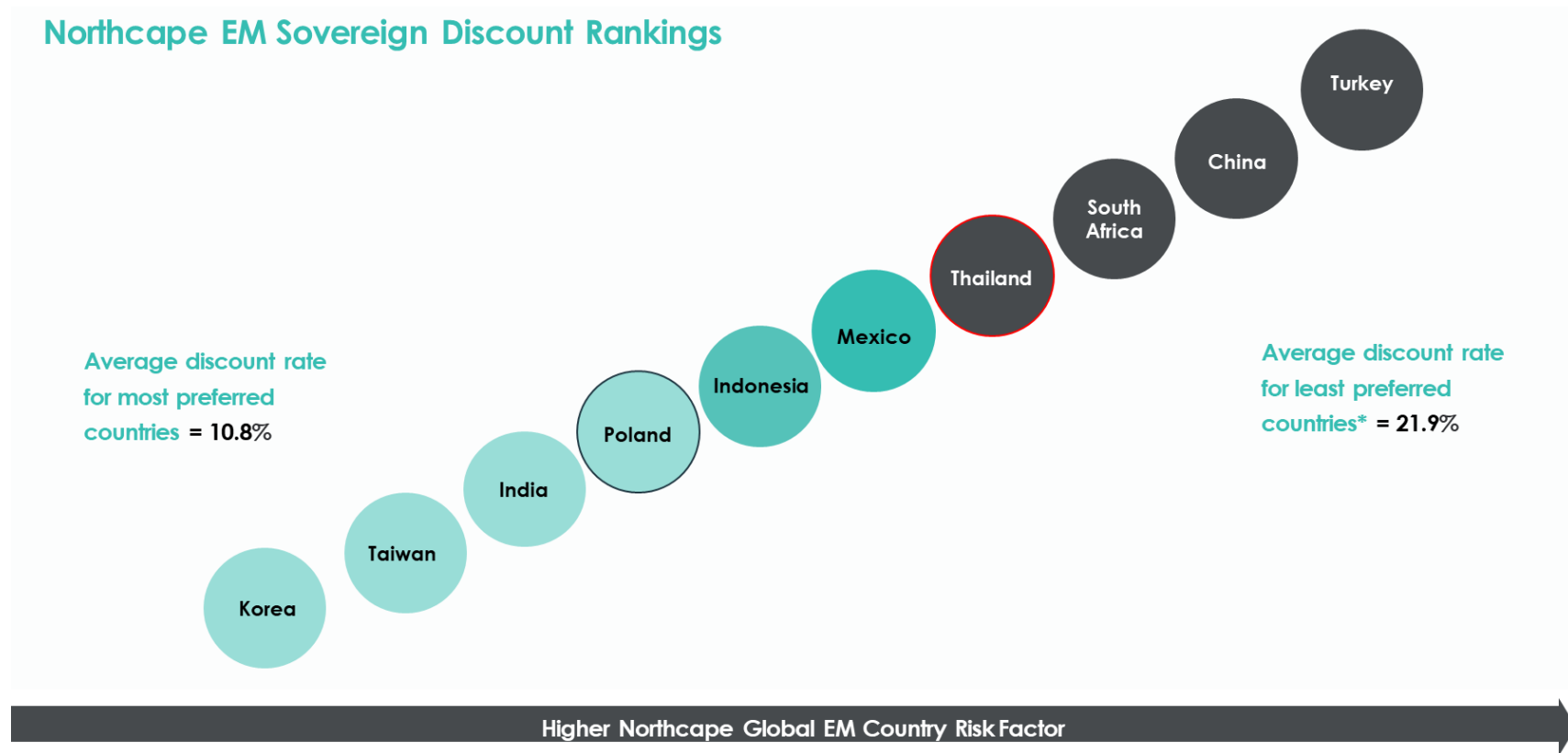
Cons

- Transfers part of asset allocation decisions within EM from PMs to asset owners.
- Adds complexity for investors in portfolio construction, risk management and manager selection.
- Implementation might be challenged if reluctance from preferred managers to carve out China for example from their investment universe. Although this is less of an issue than it was.

Source: Frontier Advisors

PM perspectives - Northcape

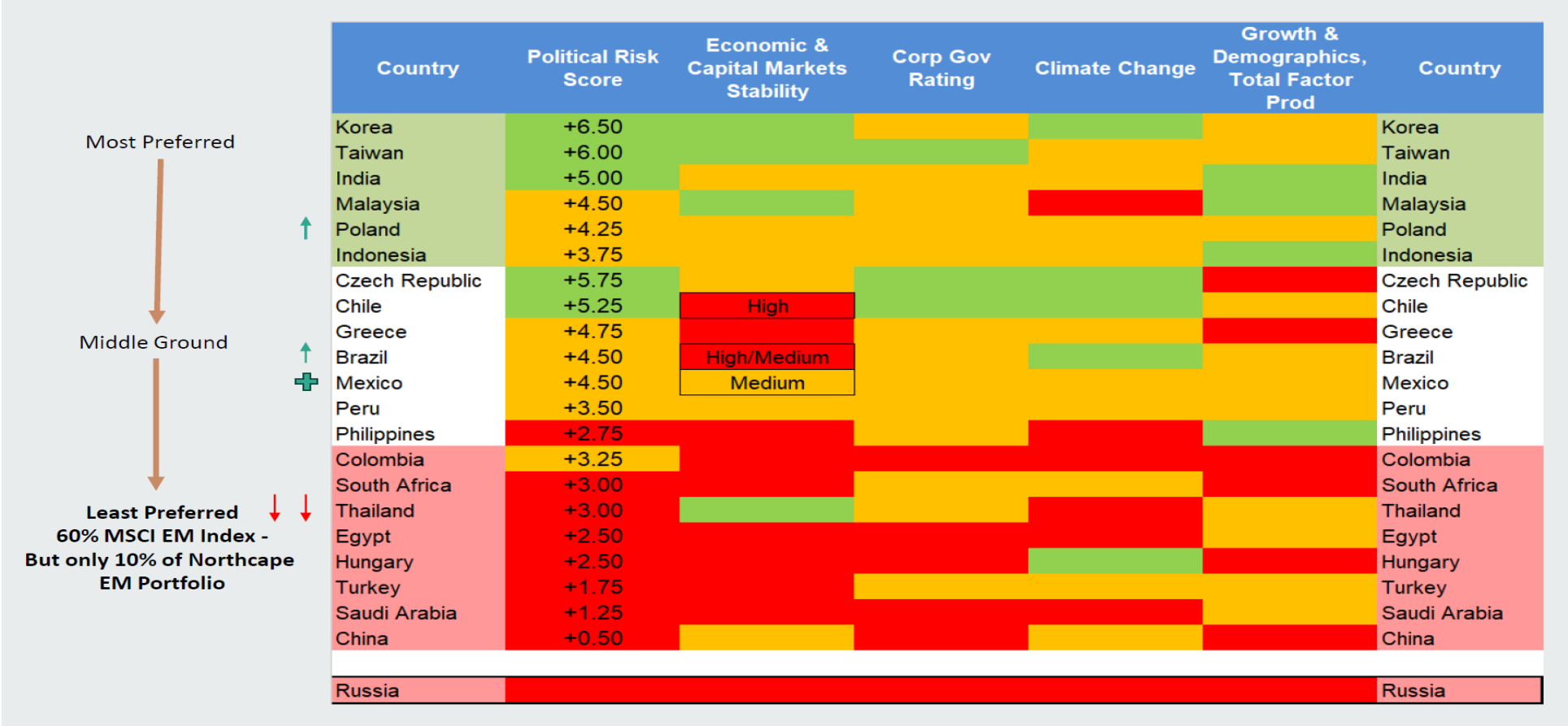
Northcape EM sovereign discount rankings



Source: Northcape

PM perspectives - Northcape

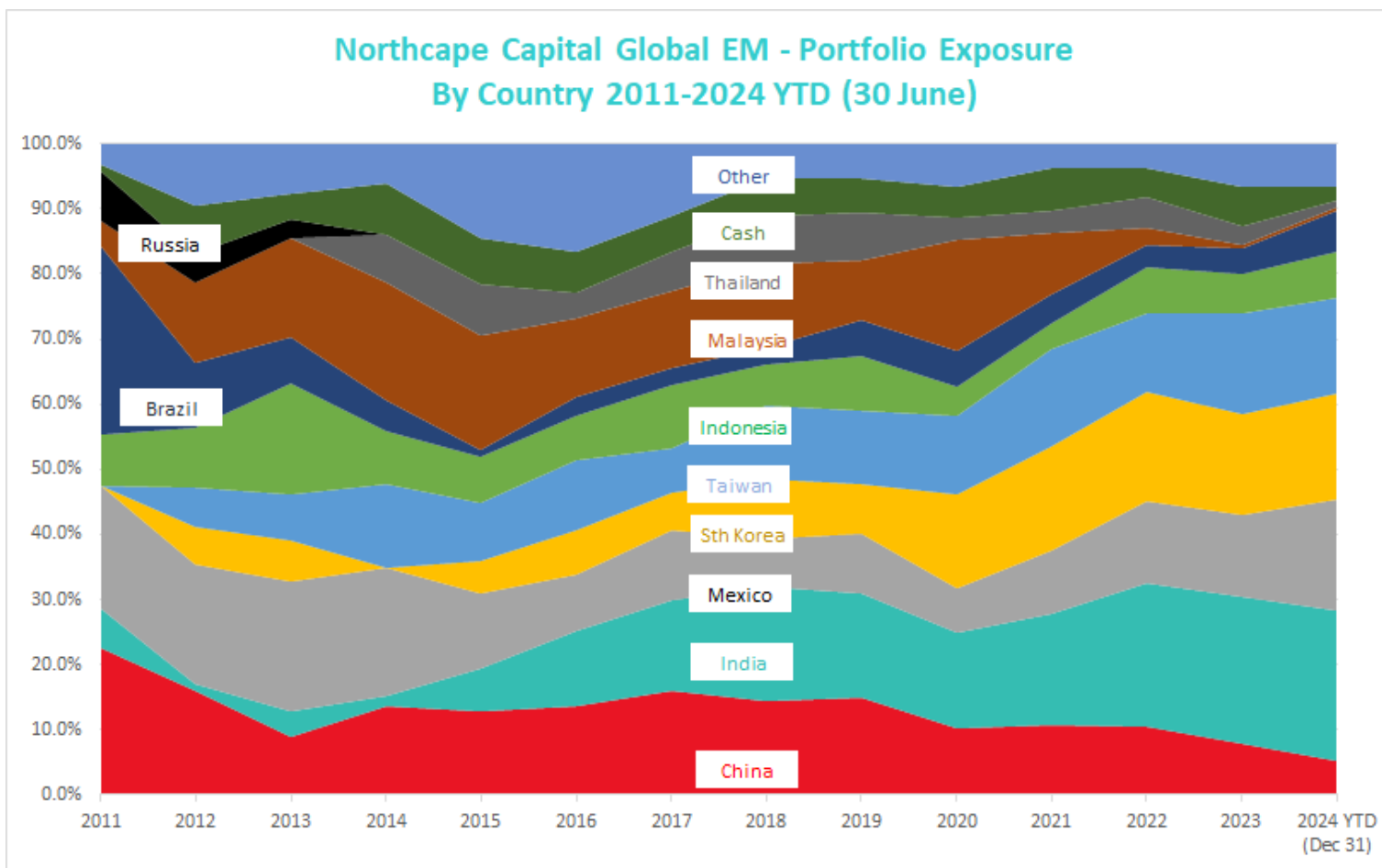
Discount rate inputs



Source: Northcape

PM perspectives - Northcape

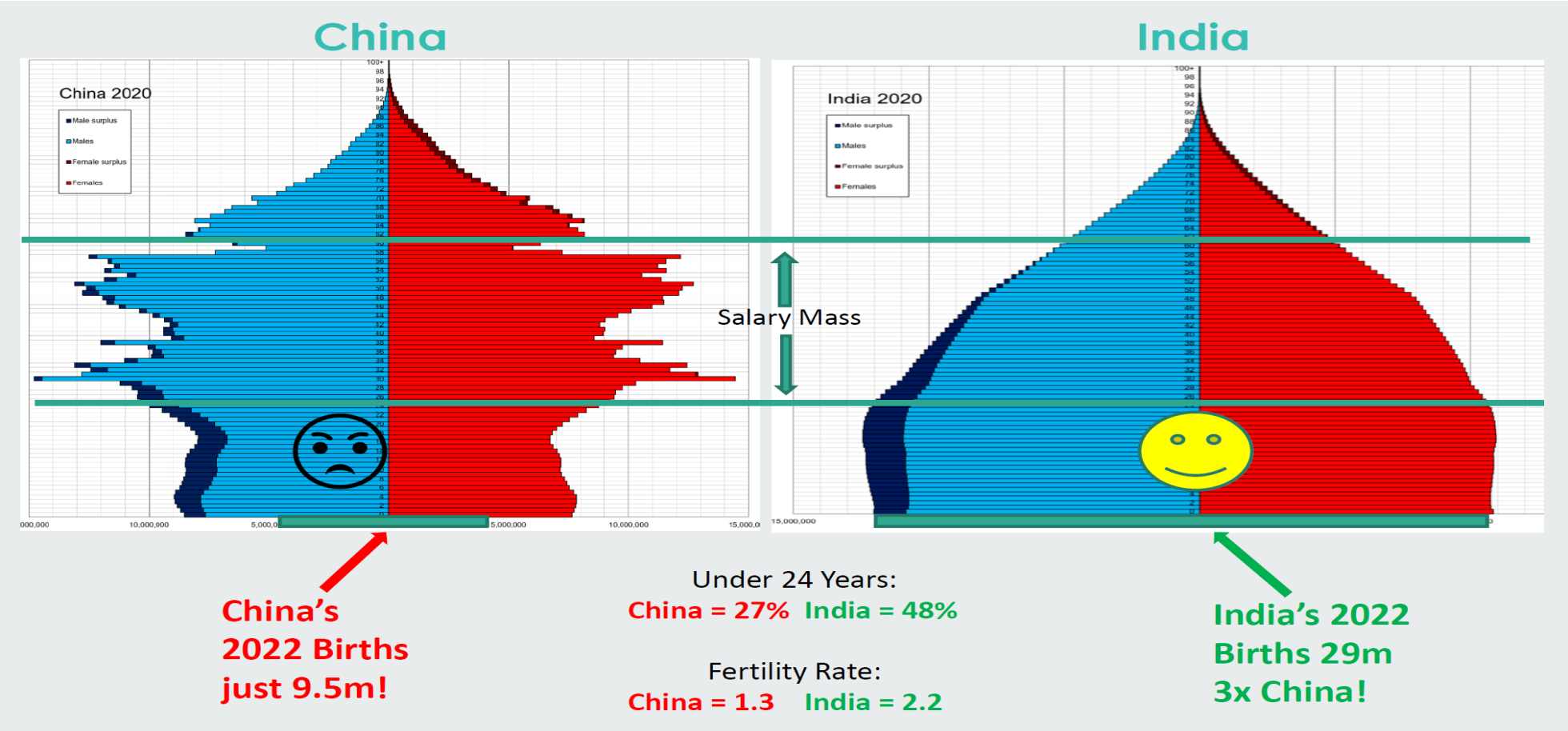
Country weightings in portfolio reflect dynamic sovereign risk assessment



Source: Northcape

PM perspectives - Northcape

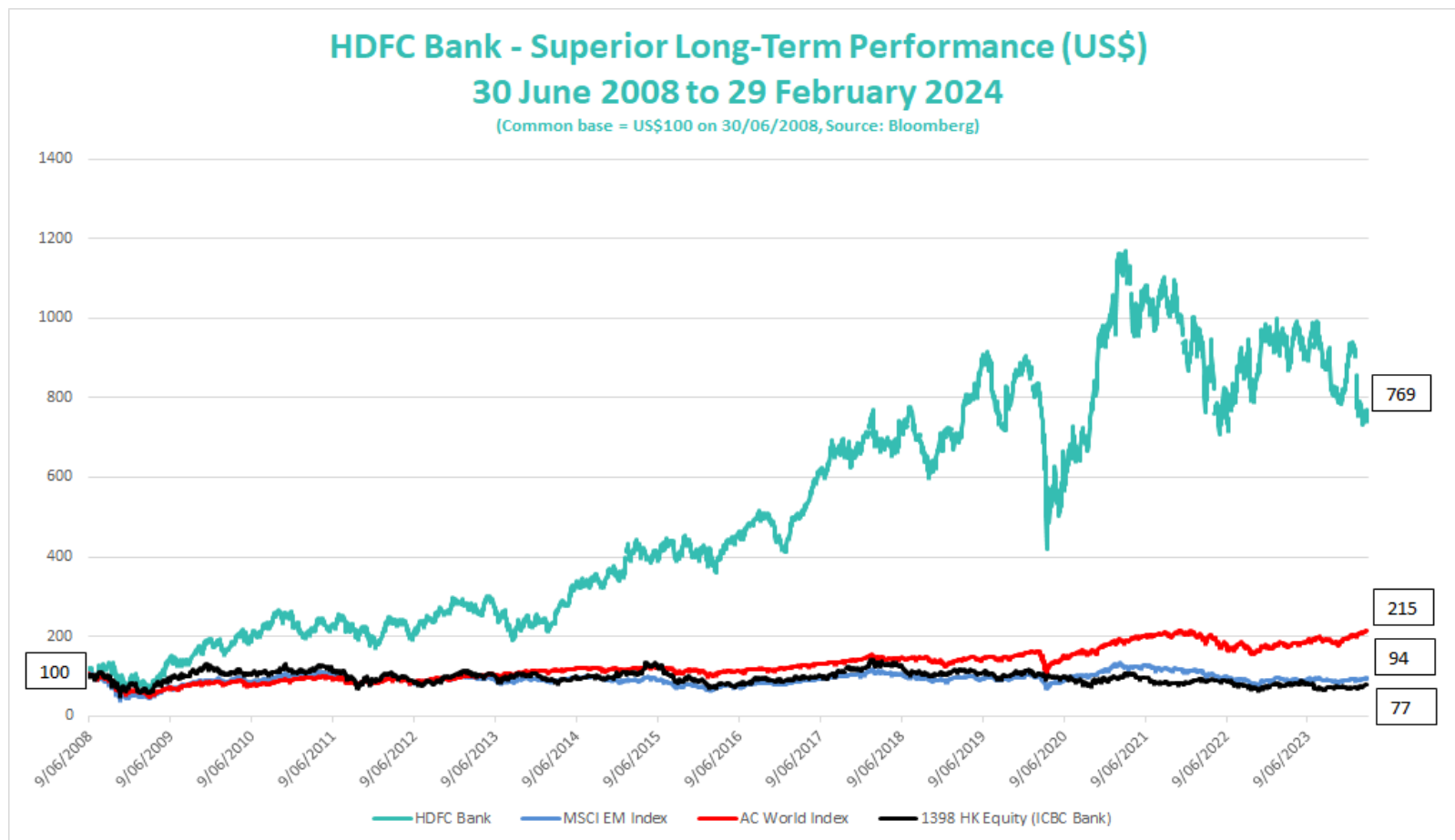
Demographics - China versus India



Source: Northcape

PM perspectives - Northcape

HDFC Bank – India’s leading private bank (US\$ performance)



Source: Northcape

Key takeaways

- Monitor dedicated and look-through EM country exposures and risk contributions to ensure they are commensurate with expectations/intentional – particularly major markets like China and India.
- Engage with Frontier on strategies and managers which may be value-adding and complementary to your existing EM exposure.
- Consider if you have adequate exposure to EM equities. It has been a lost decade for EM in beta terms. However, we maintain forward-looking conviction in the return-enhancing potential and diversification benefits of maintaining an active, dedicated exposure to EM equities.

Thank you for joining us.

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