

MSCI A-shares inclusion

23 June 2017

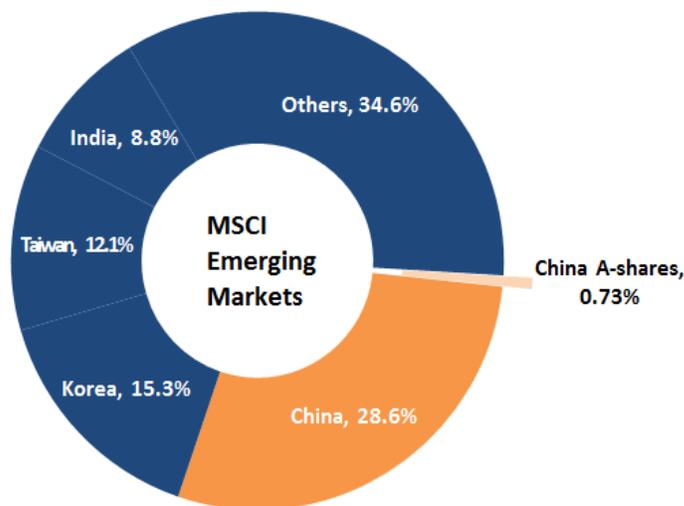


MSCI announced on 20 June its decision to include China A-shares into the MSCI EM and MSCI ACWI indices. Following 3 prior unsuccessful proposals, this ‘yes’ decision marks an important milestone in the integration of A-shares with global equity markets. While the initial inclusion factor is low at 5%, we believe this is positive for overall sentiment.

The inclusion proposal

MSCI will include large cap A-shares which also have an H-share listing, accessible through Stock Connect and have minimum trading suspension history. This increases the number of inclusion names from the initially proposed 169 to 222, meaning that the weight of A-shares in the MSCI EM is 0.73% pro forma versus 0.50%.

A two-step implementation process will be used to account for the existing daily trading limits on Stock Connect. The first step is expected to be implemented in May 2018 followed by second phase in August 2018.



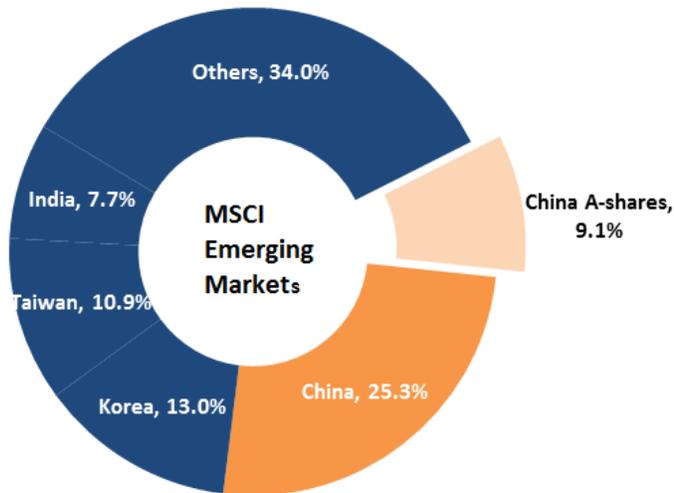
Source: MSCI. Data as of 20 June 2017.

Impact on markets

Currently there is \$1.6 trillion of AUM which tracks the MSCI. To that effect, the flow impact should be approximately \$17 billion, which is not particularly significant for a market that trades \$50-80 billion per day. But more importantly this is a boost to China's internationalization agenda, particularly since it will also encourage fixed income index providers to follow suit.

The inclusion will also mean that global investors will begin to pay more attention to Chinese equities, particularly since MSCI has indicated it is looking into increasing the inclusion factor. We saw this gradual inclusion happen for Korea and Taiwan in the 1990s. South Korea took 6 years to win full inclusion from an initial 20% in 1992 and similarly for Taiwan, the full inclusion process took 9 years from initial inclusion in 1996.

Estimated weight in MSCI EM if full inclusion



Source: MSCI. Data as of 03 March 2017.
Assuming 100% inclusion in 10 years time.

Longer term, greater foreign investor participation should bring about improvement in the A-share's market composition, corporate governance and reporting standards.

A-shares in our portfolios

We have been seeking out the best opportunities in China A-shares since the Stock Connect program was launched in November 2014. Currently our China equity portfolios we have approximately 10-30% exposure in A-shares and approximately 3-10% exposure in our Asia regional portfolios.

Our investment strategy in China remains focused on bottom-up opportunities in the new economy that will benefit from the rise of the Chinese consumers. Some examples of A-shares in our portfolios include consumer discretionary names in household appliances, high-end liquor as well as leading pharmaceuticals.

Our investment teams in Hong Kong and Shanghai will continue to conduct in-depth, on-the-ground research to identify the most attractive opportunities in the Mainland.

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