Session 1

SPEAKERS
Nick Samouilhan

Nick Samouilhan
My name is Nick Samouilhan and on a span to introduce the session speaking about change and I guess it's encapsulated by that phrase “for things to stay the same things will need to change”. Now, it's a very well-known quote from a book called The Leopard. And I think that that was one of those books where people know the quote, but very few people have actually read the book, I'm one of those. But for those who haven't read the book, the book is about, it’s set 200 years ago, in Italy and it concerns a particular aristocratic family. And because they're aristocratic, they live in a particular way. They are at the top of society, they live in the biggest house. They have lots of influence and power in society. But there's a problem. Because at that stage, 200 years ago, Europe was undergoing change, there was the Industrial Revolution. And there was the rise of other power people who made money from industry. And those individuals are going to replace everyone, they did replace, the aristocrats at the top of society. The quote itself is about the family, which says, “Well, we've lived this particular way, we've had all this power and this life. And to stay like that, to keep our power, to keep our wealth, we'll change what we do, we need to go into industry.

In some ways, the quote is a call to arms, a recognition that all of us in this room, people in general, have a problem. What we do is we’re very, very good at working out what we need to do to get a particular outcome. And then we keep doing that and we often confuse doing things with the outcome. And my main message today is that for everyone in the room, for Wellington, what we're trying to achieve hasn't changed. We all want the same thing we wanted years ago, we want to grow money for a time, you have a time for, well, for retirement to pass on for capital spending and so on. But the way we get there may have changed may have changed. So that's my main message today.

I'm going to go through what I think is the main argument for the change and then what I think is going to happen for markets. And I say the word think, because we just don't know: this could happen, it could not happen. As a general rule, the more confident an investor is, the less you should believe them.

So, with that, what I'm going to do is start with just a poll. It's a simple poll, just to gauge what your peers are on the question really, is to try and work out how long we've all been investing for. Great, now the reason I asked this is, if you go back to this whole idea about linking what we do with outcome, the way we've worked that out is we haven't read textbooks, we've all kind of experienced investing and learnt our own rules. But the only place we've learned from is ultimately our experience, which you can see behind here, you have lots of individual majority of individuals investing for less than 20 years, or there are some more than 20 years. But the majority of us [are] in that period before that. And the reason that matters, is if I then start talking about the regime, here's a very simple way of looking at that.

Behind me is a really simple two by two at the bottom. This is just thinking about the environment that we invest in. At the bottom, you can see the inflation, think of it as high or low. But don't get too complicated. Is inflation high or low? And on the other side, are we growing or not growing? And I've given them useful labels. So are we going too hot? Are we growing too fast, and is there too much inflation? Or are we just right in the green part, are we growing really fast, but there's no inflation. And then cold where there is not. There’s a sort of four quadrants, if you want four combinations of growth and inflation. Now, do not get confused by the four things you see there. We don't spend our time equally between these two. Because for the vast majority, given that poll, the vast majority of people in the room, this is your experience, you spent almost all of your time on the left-hand side. So all I've done here is looked in the last, I think this is the last 30 years. And all I've done here is said where have we spent our time investing if this is our experience, where we spend our time investing in the answer is almost always in the Goldilocks period. And occasionally we went into the blue part, this is the world that we think we live in. And if we try and work out what to do, we've learned all our rules from spending that time. The argument out there is that maybe that's changed. And then we move back into a different environment. And here's the key thing. This isn't the usual, this is the anomaly. Let's look at this data.

On the left-hand side over there is if you look at the full period, if you go back in time, where actually we spent most of our time in the periods where you're growing too fast, and there's too much inflation, or in stagflation. So we've all lived most of our career on the right-hand side of that chart in a place where we spend most of our time in these periods, like Goldilocks. And going back in time, though, that's not true. We spent more of our time on the other regimes. And the question ready is today, what happens if that changes? What happens if we start to move and we recognise that maybe we've been living in the anomalous period, and we go back to more balance type environment, maybe things change. And here are the reasons why people give, there's lots of reasons people talk about why we could change, but I've just put four here. And if it's helpful on the left-hand side, I'd put two, commodity markets and labour, think of these as the inputs. If you're running an economy, these are the things that you need to pay for to build and run businesses, commodities and labour. Both of those, I think we can make a very strong case, are going to be more expensive going forward. On the commodity market, if we speak to our experts at Wellington, they'll talk about huge underinvestment for a number of years in commodities. They'll also then talk about the fallout of Russia and Ukraine, where the supply is fragmenting and we can't get supply from where we used to. So, the supply of commodities is tighter, but the demand is higher because we're trying to build things like new ways of running the economy that needs commodities. So that's going to be tighter. On the bottom left-hand side it’s also true, if you just think about one of the anomalies today it’s that we have a really strong labour markets all over the world. And if you combine those tight labour markets with what governments have told us they want to do, governments want to rebalance the pie, to let individuals address inequality by increasing wages. And we see that if you look at the data, wages are going up all over the world, it's getting more expensive to hire people, I'm sure that resonates with many of you.

So, on the left-hand side, the input costs are going up, it's very different. If I showed you the charts for those for two of the last 2030 years, they went one way. Commodities got cheaper, labour got cheaper, that may be changing. On the right-hand side is, if you want, the change in policy, what we try and do as a government. And both of those two things talk to a more volatile world. Think about the top right-hand side, it was a very simple thing about China and the US for a long time. They viewed themselves as economic complements, they're trying to integrate themselves more and more in a way that lowers prices and makes things better, they now don't do that anymore. They increasingly see themselves as strategic competitors. So, what that's going to mean is that we're going to start disentangling the supply chains and become more volatile. On the bottom right-hand side, there's been this huge change. And what we expect governments to do is, think of the argument in the US now, which expects the government's take over of student debt. [The] Same is true all over the world, we expect governments to step in and spend money, where we never did in the past. If you put these two things together, and again, I'm not sure how true these are, but a combination of more expensive inputs on the left-hand side, and a bias towards spending too much money on the right-hand side, and you get a return, if you want, to the 1970s. Now, this may not be true. But it's worthwhile thinking through just going back to this idea of change. What if this is true? And we've done some work, and we found three things.

So, if you just think about what you need to think about in your own portfolios, there are three things that I think you need to spend some time on. The first is, what we did is, you can ignore the charts for now, we just looked over time. And we divided the world into periods where the economy was very volatile. On the bottom there, you can see it says most volatile, or when it wasn't very volatile. And then we looked at what happened to interest rates on the left-hand side, and equity valuations on the right-hand side, if you just start with the left. In general, when we go from left to right, when we went from least volatile, to more volatile, interest rates go up. The reverse, of course, has been true for the last three decades. We've gone from a period of very volatile macro economy, to one of not much volatility. So, interest rates came down. They came down a very huge amount, think about the last two, three decades. Now we go. All this data says that if we reverse that process, we should expect interest rates to be higher. Arguably, we started that process. What does that mean? In practice, it means that we need to be very careful buying fixed income because the yields go up and we have to be very active about choosing where we are. It's not a one-way bet anymore. Interest rates are going to be higher, if the world is more volatile. On the right-hand side was surprising for us. We did the same thing for equities, let's look at the equity market. This is global equities here and we said what happens to valuations, if you're in a volatile and non-volatile period, it's on the right-hand side of that chart, and what you can see there is in general, if you go into a volatile period, valuations are lower. It makes complete sense.

If you think about what's happening here, firms, because they live in a more volatile period, their earnings are going up and down, their input costs are going up down, their revenues going up and down. Why would I buy that? I won't spend that much money building up the price. So, if you put these two together, what it means is that as we went from a very volatile period, down to a less volatile period, the last three decades, the period all of us mostly have lived in valuations for equities went up. So, it's a good thing just to buy equities, they just went up and interest rates came down in a one-way direction. If we go back to a more normal environment that changes, interest rates start to go up, valuations come down, it gets tougher.

So that was the first thing we found, and I can talk a bit about what we're trying to do to solve that issue. The second thing we found was this. If this is about valuations, the second one is about the relationships in portfolios. Here's an important one, on the top left-hand side you can see it's about commodities. And do you buy equities in the portfolio or do you invest in commodities? And I'm thinking about things like oil, crude, industrial metals and so on. And if I asked most investors, before they saw this chart, what is the link between these two, they'd say, well, they move together, because when the economy grows, we need more metal, so they will go up. And when the economy grows, equities will also go up, so equities must move the same direction as commodities, bottom left- hand side, that's true. So, you can see that light blue there in the bottom left-hand side, when you're in that period, the same is true for the two on the top left-hand side, so it will appear that we've been in, we spend most of our time in the left-hand quadrants, they move together, you can see that line is upward sloping. When one does well, the other does well. When one does not do well, same thing. Now look at the right-hand side, particularly look at the bottom right-hand side, when you're in a period where there's low growth, but high inflation, commodities and equities move in different directions, the relationship completely changes and they are no longer substitutes, but they are actually diversifying against each other. If you think we're going to move into this environment, commodities will play a different role in portfolios than they have in the past. Now, the question, of course, is why? And I don't know the answer to that. What I think is going on, is that when we're in stagflation periods in the bottom left-hand side, bottom right-hand side, when we're in periods of high inflation, but low growth, I think the reason they move in different reasons is when the oil price goes up, central banks have to hike interest rates, and that brings down the economy. And we saw that last year. Right. So, we saw commodity markets go up and equity markets go down. So, I think, the link there is because the policy, but what this tells us is that the relationship changes. That's the first thing.

The second, probably more important relationship that changes if we spend more time in a different regime, the most important relationship in portfolio, is the link between equities and bonds. Now, when we construct solutions, when you are looking at your own portfolios, the typical way we do that is we have equities to generate returns. And we have bonds to diversify. Because bonds tend to make money, they rally when equities fall, for there's a negative correlation between the two. That's the standard assumption. And if you look at the left-hand side of that chart, that's typically true. So usually you can see in blue there, when equities for bonds do well, it's not perfect, but that has generally been the case. On the left-hand side, that is not true. On the right-hand side, particularly in the bottom right-hand side, when you've got a period of low growth and high inflation, equities and bonds are no longer diversifying their move in the same directions. We saw that last year. We're seeing that this year. So, you now need to rethink about how you protect a portfolio. And there are ways and means of doing that. But they require change and ways of thinking about things.

And then let me just talk about the first thing we found. Again, this is a proposition. If we move into a place where we spend less time in Goldilocks, and more time worrying about inflation, as wartime worried about growth, things start to change. The first thing we found is that interest rates are higher, valuations are lower.

The second thing we found is this: key relationships, equities and bonds, equities and commodities, change completely.

And then the final thing we did is we tried to work out, well, what did we do? We ran some analyses and what we found are these are the asset classes that have historically done well, when you're in these different regimes. When you're growing really fast and inflation is too high and you're in the red zone in the top right-hand side, commodities are the best-performing asset classes. When things are going just right, when you are in green, when there is almost no inflation, and growth is really strong, equities do the best. Credit does the best. You can see what happens there on the top left-hand side. That is the regime most of us have been investing in. That's why if you look at most portfolios, they are primarily focused on equities and fixing many of them just passively. That's been the right thing to do in a world where you spend time, the bottom left-hand side. When you go into recession and there's no inflation, bonds do really well. That's not true if you go into the bottom right-hand side. Now, the reason we did this analysis is if you looked at our portfolios, in fact, if I, if I looked at any of your own portfolios, I suspect what I would see is that you've correctly diversified portfolios globally, you've gone and allocated around the world, even if you think, well, this year, the US did really well, in Japan it did not, at least I was diversified. I was positioned for different outcomes. And some of you may well be doing the same thing with sectors or styles. Very, very, very few portfolios are positioned for regime diversification, positioning for different regimes. And that's why last year, many portfolios struggled.

So the final thing we found is this, which is the idea that if we move into this new regime, we need to think about what we hold. Now I'm going to end with one, the 'take homes', if you want. I'm going to show you something which I probably shouldn't show you. In about two weeks' time, I'm presenting at our internal Investment Committee about the implications of this. And we're trying to work out what do we actually do at Wellington in our multi-asset solutions. And we're going to put forward a number of changes. And if these are signed off, this is what we'll do in our portfolio. So I'll show you what we, again, we haven't yet signed this off. And we're not yet doing this. But I thought I'd show you what we're thinking about doing. And we've grouped them broadly into four different things.

It's about how we change how we think about relationships on the top left-hand side. So what I mean by that is, when we design our portfolios, we're no longer going to assume automatically that bonds will diversify. When you think of something else, what else can be used in our portfolios to protect, maybe it means allocating to other types of protective strategies. There are certain hedge funds, for instance, in alternatives that did really well last year, that are protective when things fall. Maybe we need to allocate more to alternatives in that environment. The other thing to look at, on the top left-hand side there, is commodities. Typically, we viewed commodities in our portfolio as well. Either we have equities, or we own commodities, or maybe a little bit of both. They do the same thing. In portfolios, they both go up at the same time, they both fall at the same time. Maybe that's not true. And maybe commodities play a much more important role in our portfolio than they have for some time, exactly the role they played, by the way, in the 60s and 70s, when we were in that old regime. So the first thing we're going to look at, is do we change some of the assumptions that we build portfolios with. The second one we're going to look at is what we call risk budgeting. All we mean by that is that if the world becomes more volatile, maybe we take the shackles off our managers we invest in at Wellington. We hand over money to our equity managers to run to our fixed income managers to run. But like many of you here, we impose constraints, we say, 'don't go too far away from the benchmark.' Maybe we need to change that. And if we recognise that was more volatile, we need to give them greater freedom, more active ability to change things around. Again, that will be quite a big change. For many of us in the industry. It's been the reverse for the last two, three decades. So we're going to look at that.

The third thing is about the risk in our portfolios is how do we run the risk in our portfolios. And there are two things we're going to look at doing. The first I'm sure, like many of you, when you look at the portfolio, the first thing you look at is tracking error, or something like value at risk. Maybe we need to stop doing that, because those metrics are premised on the last ten or 20 years. And last year, the numbers they gave us, the forecasts, were not very accurate. So maybe what we need to do is change your way of thinking about risk and move away from tracking error and think about scenario testing, instead asking questions like what happens if inflation spikes. What happens to the portfolio? Don't tell me this will be the tracking year if nothing changes, tell me what happens if things change. So that's the risk management. And perhaps the most important thing we're going to be doing is that last one, where, much like many of you, we've had a very…it's been a very busy time with markets. And I feel we're a bit shell shocked. We're all a bit reluctant to make changes. But maybe we need to do that. Maybe we need to look at what we actually own in the portfolio. For instance, if we are worried that equity valuations will fall, maybe we need to get returns from things that don't depend on equity valuations. Things like alternatives may well be playing more of a role in our portfolio, because they don't depend on equities going up. We need to look at that. Maybe we look at more, other, asset classes in the portfolio, things like gold commodities and other things, but we haven't traditionally held in there. And then when it comes to particular equities, and styles and fixed income, I can tell you what we're focused on.

On fixed income, we're going to go to our managers and say, you run this particular portfolio for us. Are you able to make the changes you need to make if you think interest rates are going to spike? Do you have enough freedom in the mandate to move around? Because what we don't want is you coming to us and saying, 'Well, we knew interest rates were going up, but you told us we couldn't change anything'. We want to make that your problem. So what we're going to do is give you the freedom. We're going to make more flexible allocations so that you can make those changes. On the equity side, we may well end up focusing more on companies and there's a panel today about this. Companies focused on change and about quality and so on. We need to think about the how the macro environment translates into how equities perform. And finally, on the alternatives, again, there's a panel today. I think this is a really interesting time for alternatives. I'll give you two things we're going to look at.

The first is if the world starts to become more volatile, currencies start to move around a lot, think about the Yen this year, think about the Dollar. So, strategies that can make money with macro movements and macro hedge funds, they're really well-positioned to do well, in fact, I'm sure many macro managers last year did really well. Maybe it's an environment to allocate to them; it hasn't been for a long time. On the other side, if you think of what's happened, and will interest rates go up, it becomes much more expensive to run a company. If labour costs go up, it becomes much more expensive to run a company. So, the difference between good companies and bad companies will be huge. So, in the alternative world, companies that play long, short, i.e., discriminating between good companies and bad companies, should make more money. Now you need to find the right manager, but their opportunity set is higher. So that's what we're looking at doing in our portfolios. Again, we haven't agreed to any of this, but I thought I'd share it with you today on the idea that we're taking change seriously and we're trying to work out what we actively do in our portfolios to change them to reflect perhaps a risk that things are changing.

And I'll end, I guess, with just the one comment, which goes back to this book, which is that we are all conditioned to think about outcomes. And to confuse those with means, we think we carry on doing the same thing, we get the same outcome. That's usually true but sometimes it's not. And sometimes things change, and we must change with it to get the same outcome. We're not changing any of our outcomes. We're still trying to grow money over time, to generate income, to protect portfolios, but we recognise that perhaps the environment has changed the way we do that needs to change as well.

Now, what I can say is that in true Wellington style, we're going to bookmark today's session. I've opened up by talking about if the change happens, at the end, you'll hear the counter argument. And this is a live debate. So, I don't want to come across as certain about this. But I do want to come across as, as you can tell by us at Wellington, is this is something to think about. And these are the conversations you should have. If this happens, what should you do? And I think that's worth exploring both with you've allocated money to but also amongst yourselves as allocators.

Session 2

SPEAKERS
Niraj Bhagwat
Yash Patodia

MODERATOR
Xiaying Zhang

Xiaying Zhang
Thank you very much, Emily. Good morning, everyone and thank you for having us here today. For the next 45 minutes or so we're really looking forward to providing you with some insights, interesting insights into the investment opportunity that we're seeing here in Asia. I've been reminded by Niraj once again that he really enjoys live Q&A and being challenged. So, we're going to leave plenty of time towards the end of the session for live questions. So please, raise your hand or send your questions to pigeonhole and we'll make sure that we cover them all. We will get right into it then. So, I think, well 2022 reflecting on that year, that kind of crazy year. I think we all had come to face the reality that we have entered in into a new market and economic regime. So that makes 2023 quite interesting, especially for investment opportunities here in Asia, just given the ever-shifting macro geopolitics and even policy backdrops around the world. So, I think to start this panel, would love to hear your guy's insights when it comes to where you're seeing the best opportunities here. In this part of the world, perhaps we can start with Niraj.

Niraj Bhagwat
Thanks Xiayang. Good morning, everyone. I want to take a step back and kind of look at Asia and go back to the last crisis and last global crisis, because in Asia there is a crisis every year. But look, I am in 2008 and that was a big year of, remember BRICS, remember emerging markets and that was the

peak profitability in emerging markets in Asia and since then, through a series of local crises, as well as of course, global crises, the ROIs, or the return on capital enjoyed by the corporate sector is that historical low now. There's been a lot of fluff washed away in Asia. So that's always to me very interesting when somebody's investing, right? You're buying not at the peak of profitability, like I would argue in the US, but you're buying at the low end of the profitability. Meanwhile, most corporates across have become much better on balance sheets and like, say 2007, so that's also a good starting point. And the most important thing is valuations. Because when you buy an asset, that's the most important thing, and valuations are at historical lows, obviously led by China and Korea, but in my 30 years of investing, I've never seen as low valuations. To me that that's an interesting place to look at Asia.

Now, within Asia, I am incredibly bullish on China, I must add, and if you have time, we can engage into it that I'm very bearish equally on China long term, but I'm incredibly bullish on China now. I think we have a window where the interests of Xi Jinping and the Communist Party and all of us are aligned. All of us want the economy to go up. And I think that's where we can be parasites are what they're trying to do and make money. Simple as that. I think China has long-term issues, but I think one must be focused on the opportunities in China. And since last year, we've been buying China in our portfolios, and we are finding incredible opportunities where you buy quality companies domestically; we're trying to stay away from geopolitics in China. So, I think that's my principal area which we're excited about. Obviously, you have to talk about India, which as the second-largest market has a big opportunity. Now, we know India has obviously beneficial geopolitics. And I would say among all the large countries in the world, it is probably the only one staring at a large economic cycle in front of it, which is very rare.

Having said that, the market has done very well. So, I think when, as we already bought them up in India, they're even now, today, at an incredible bottom of opportunities, where you get stocks not having to pay expensive pricing, and you can benefit from the tailwind. And the last but not the least, and often a forgotten part of Asia, are the ASEAN [markets] and Korea. I always call it the three legs of the stool. And what is happening globally is that there are incredible trends in ESG, which is bringing back sectors which were long forgotten and left for dead in the last 10 years and now are very interesting. So, for example, Korean industrials, they've gone through a gut-wrenching time for last 10 years where nobody was interested, people stopped covering these talks, and I think they're going to have, and are already having, an incredible time in Korean industrials. But I will also argue, I was just talking about commodities. I think countries like Malaysia and Indonesia are going to benefit from structural change towards commodities and geopolitics, with stuff like palm oil, and people making more money. You don't have to invest in palm oil, but these countries benefit. So that is where I will stop here.

Yash Patodia
Yes, I'm really excited about innovation. So, Niraj talked a lot about what happened in the past, I'll talk a little bit about what's going to happen in the future. I think innovation is what drives the world forward. And it applies, broad-based, across industries, right? It doesn't matter whether you're a restaurant, you're an auto company, or a bank. If you don't adopt technology, you're just going to be left behind. And I think we're just at a very interesting point when it comes to the innovation cycle. So, I'm going to start with a slide. This talks about why tech in Asia.

I'll summarise this as follows: the first point is saying that there is a demographic dividend to Asia where [there is a] growing middle class, more spending power. The second point is that within [Asia], technology is actually fairly diversified. You have e-commerce, you have artificial intelligence, fintech, etc. And the third point here is that companies have actually come out of COVID much stronger than where they have been in the past. But the point of this slide is that I actually didn't write it. Actually, no human wrote it. This was written by open AI, chat GPT, which some of you may have heard of. This is the question we asked it and this is the response that it gave verbatim. And I wanted to do this just to show you the power of where AI has come from just in the recent past. And how it is doing it, it goes, is by reading basically tons and tons of data. And unlike, say, a search engine, which is just copying something that someone's already written and presenting that to you, this is actually generating the response in real time, what is written here has not been written before. And if you haven't tried this, yet, I encourage you all to go and try it. Because I can see this with high confidence in the next two quarters, or at best, in the next few years. Each and every person, you're going to be using this in some form or the other. So how does this apply to Asia? Well, Asia is the building block that go into building something like chat GPT, which is effectively an AI engine. You need fast processors, you need leading edge everything, materials that go into it, the execution of it, and in order to do that, the components that come together with that, all that lives in Asia. That's the heart of the semiconductor supply chain.

And then second is on the application side, which is how quickly do these things get adopted and again, I think Asia is actually leading the charge. And that tends to happen, because Asia does not have a lot of legacy infrastructure to deal with. So, take payments, for example. In the US, you're still using a payments stack that is decades old, but if you think about, we're using QR codes for payments here in Singapore, or you think about using UPI in India, you use 10-Pay and Alipay. In China, that experience is not just much better and faster, it's also much cheaper. So, it just opens up the opportunity for the entire economy to prosper. But what is also interesting is that the rate at which technology is being adopted is only accelerating. So, if I were to ask you how long it took Spotify to reach one hundred million users, they took fifty months. Instagram took thirty months. If anyone wanted to guess how long TikTok took, [it was] nine months. chat GPT took two months to reach one hundred million users. That's how rapidly we are all adopting technology. And as I look forward, as I look at the potential of AI, as I look at new platforms that we might come to in the next couple of years, [I see] things such as augmented reality or mixed reality, in which all the large tech companies are investing tens of billions of dollars. And I just think we are in a really interesting space within the technology cycle.

And then finally, I would say on the valuation piece, at least on the semiconductor side, you are, on a historical basis, looking at an industry that is coming out of a cyclical bottom, and [that] on a secular basis has much stronger tail winds. In addition to all the devices that you use today, there's going to be more and more adoption of technology within our lives.

Xiaying Zhang
Thank you so much. Yash, you make me worry about my job, which is not good. But no, I do agree with you. I think innovation will just continue to grow. And Asia is definitely in the forefront of this very secular trends of digitalizing everything. But we didn't really talk about country specifics. So, I just wonder, would it be fair to say that China is on top of your mind when we talk about technologists, given

where they had been before and where they're headed? Are there other little bright spots that you have been able to identify here in Asia?

Yash Patodia
Yes, that's a great question. I think China is definitely front and centre of what we're thinking, similar to what Niraj had said earlier. If you think about the last two years, they were a pretty challenging time for the Chinese tech companies. As I am sure you're all aware, you had regulation come in quite aggressively and in an unpredictable fashion. The companies were dealing with a slow economy, and we had COVID-zero policy, so there was a lot of uncertainty within the market. As you're now coming out of that, things are changing. Regulation is actually getting much better. We were talking to a large Chinese tech company just the other day, and they said that while they had a fairly adversarial relationship with the regulators over the past two years, now the regulator is giving them the message that they're done with the changes that they wanted to see by and large. And the focus is for these companies to help the economy grow again, which I think is just a very positive sign. And then you have the recovery from COVID. As with if you look at all other markets, as you recover from COVID, demand comes back pretty aggressively. And that is a great tailwind for any consumer-oriented company. And I think similarly, a lot of these tech companies in China are going to benefit from that. And then finally, I would say that you've all been seeing headlines in the US right about layoffs. People being let go in the companies in China actually took their medicine last year. There were a lot of layoffs, there was right sizing of costs. So, as you start seeing revenues come back, the operating or cost structure of these companies is just far more optimised in my view.

So, I think China is definitely quite interesting in how it's going. Going forward, the caveat I would put there is that there's still certain pockets that you have to be careful about. In live streaming, for example, I think that is still going to see some pressure going forward. So, I think you have to choose which areas are least vulnerable to regulation.

I think China is just one part of the story. Like when you look outside of China, I mentioned, the semiconductor supply chain. Well, if you look at where leading edge semis are produced, and that's where a lot of value is created, the foundries the leading-edge ones are in Taiwan, where the materials that go into actually forming these really, really tiny chips that are so powerful are. They typically come from Japan, and the semiconductor equipment that goes into them, again, that manufacturing process is coming from Korea, as well as Japan. So the opportunity set is just far wider than just China. And then finally, I would say that India is interesting. The internet sector is actually quite tiny on the public side in places like India. But as you look into the private side, that's where you can get some more differentiated exposure to growth opportunities within some of these countries where the public markets aren't quite receptive yet to these types of companies.

Xiaying Zhang
Perfect, thank you for moving us from China to India, which I think Niraj is very passionate about. First of all, Niraj, congratulations on receiving the Platinum Award for our India focus, equity fund. Great achievement there. And I know you have been investing in Asia for many years. And most recently, I think a lot of investors struggle with the fact that given where we are in India, especially with valuation, and as you mentioned, the tech sector, for example. There have been some questions raised about the

India market, so [we're] curious to hear where you are seeing the opportunities, and perhaps what are the considerations that you're taking into account when investing in Asia?

Niraj Bhagwat
Yes. Well, when you say I've been investing for many years, you just meant that I was old. So, I think valuations in India is often an insightful question. Indian valuations are at a premium to every emerging market. But Indian valuations have always been at a premium to every emerging market in my 30 years I've been investing. And yet, if you look at the returns achieved by the Indian market for the last ten, twenty, thirty years, they've beaten all emerging markets and are sometimes on par with the US, In fact, sometimes beating the US in certain time periods. So, you must ask, why has that been the case? It's not GDP growth has not been the highest GDP growth.

So, if you take for comparison, a country like China, which obviously people compare, rightfully so, large size, typically, when you go to China, and historically has been people looked at China, got seduced by the size of the country, the GDP growth rate, amazing. The infrastructure, physical infrastructure has been amazing, educated workforce. And of course, the ease of doing business things get done very quickly. And everything is doing by the government, and because of that things happen. But also because of that supply to very, very quickly, right. And because supply comes very quickly, returns are much lower across the cycle, just enough supply coming on quickly, all the time. And everything is driven by the government.

Now there's a flip side to everything being driven by the government, as you've seen in the last three years. Right now, compared to India, I just said China has everything because of the government. I would say India has everything despite the government. Anybody's that has been to India, you would know the infrastructure is not there. They would try it, until recently at least, try to do their best to meddle in your business or make it worse and so, if as investors you can find companies which are quality companies and find a way to navigate that environment, you can have sustained outperformance and high returns for much longer than you think. And that is what creates value creation. So, I think people don't sometimes look at numbers, but I think that's behind it.

The second thing, which has been more the case in the last few years is what I would call the Tina factor: "there is no alternative". In the last few years, people got disappointed, rightfully with China. And they looked at a big market, which was attractive and India obviously has a lot of tailwinds going through. And so, India's also had a premium for that, because there's no other large country where you can have a potential for growth as a function in democracy, etc. Now, having said all that, and I said that at the start, I think Indian market has done well. So, for me, it's a great place factor management, I think top down there are sectors like technology, IT services, which are expensive related to the market and I would not be interested there at this price. But there are many stocks, which are bottom up, a lot of bottom-up change is going on. And if you know the landscape, even now I'm finding enough opportunities in a conservative portfolio where you can find change happening and you don't have to pay an arm and leg and you can still navigate the tail end.

Xiaying Zhang

Perfect. Thank you so much Niraj, for sharing those insights. And I think, yes, you mentioned a little bit about private investing. So, let's switch gears and go there. So, as everybody knows, the private equity market has been growing in the last 20 to 30 years, and the access into that particular asset class has become much easier in the last five to six, where whether it's institutional clients, or private wealth and family offices. I'm so sorry, Niraj, it might be a little unfair question to you now. But just given the dynamics of the market today, the gross potential devaluation that is there across the different markets in Asia, if you were investor today, would you be more leaning into private equity or public markets?

Niraj Bhagwat
Well, you do both. So, you'll will be okay with my answer. So, I'm biased, I do any public [markets]. So, take it with a pinch of salt, what I'm going to say. So obviously I'm going to say public, right? So, I think that I talked about valuations. And I really think when I take a step back, and if you believe in regime change, which obviously 90% of us do, then the last regime winners don't work. And the last regime winner was the US equities and US dollar. And then you think about what asset class could take over the leadership and in fact, Asia was the only one which was actually doing well in the last 10 years. But it underperformed the US but outperformed everything else. And I think going forward, it's half of humanity. People don't realise it's half of humanity. And it's got huge size huge valuations with traction and to me, Asia is going to be really attractive on the public side. Now, when you ask me on the private versus public, I would prefer public for the simple reason that, when I look at the last 10 years' winner on a team, which has worked, and I'm talking only generalisation, of course, but private generally when I see a lot of stocks in the US, for example, haven't been marked to market and or business models haven't got the memo, I would say.

Yash Patodia
I guess I do both public and private. So, I'll give you a bit more of a nuanced perspective on the public side, I actually agree with Niraj, I think it's an interesting time. I spoke about the semiconductor supply chain, where we are there, where we are on that front, and as well as the inflections in technology that are going to happen. So if you look at it on a five- to ten-year basis, there's going to be tremendous value that's going to be created. And I think what's interesting to me is differentiated exposure. So you think about a lot of the US names everywhere, whether they want it or not, already own a lot of the "fan" type of names. But Asia tends to be underrepresented. And you're coming off a cyclical bottom secular that looks great, you have some really high quality companies that that just are sort of under the radar. So, I think the public side, in Asia gives you access to a differentiated set of companies, which generally tend to be underrepresented in portfolios.

I think of the private side as being slightly different. Private companies tend to be, we think of them as the future leaders, or the companies of tomorrow, business models that are made [to] emerge tomorrow. And I think that access, as private companies stay private longer, a lot of that value that is created tends to happen within sort of that private world. And I just want to zoom out for a second to just set context on the changes that we've seen, [from] say, 15 years ago, when Apple came out with the iPhone. Everybody said why do I need a phone only to make calls. Why do I care about doing anything else on that? But slowly and steadily, you saw that our lives have changed with that device. And that happens over time, that happens when developers come and start building for it, new business models emerge. Some of you may have taken grabs over. A grab doesn't exist in a non-mobile world, the business model just doesn't exist.

So as you look forward, and you say that okay, there are new things that are happening. There is…I showed you AI. There are potentially new platforms that are going to come in. What are the business models that are going to be created around that those are going to start off in the private world? These companies will scale in the private side, and then they will go public. So, the question for me is, how do you capture that opportunity, which is different from the opportunity that the public side offers you, and I think privates are a great way to access that.

he other dimension where privates can be interesting is in countries where the public markets are not quite ready for businesses that are not printing cash today. Because remember, a lot of these private companies are off to really big markets. So, they have to go through a bit of an investment cycle. So, they might be somewhat unprofitable in the near term, but in the long run, there is a sort of sizable market that they're after.

And the final point I'll make on it is on valuation. And I know that is top of mind for almost anyone who reads the media when it comes to private companies. Unfortunately, some peers of ours have actually done a deal a day, I kid you not. A deal a day. We're lucky if we do one in a month, given the amount of diligence that we do. But the important piece is that, given our public-equity DNA, we're looking at these great private companies through a public market lens. We're looking at them as trying to underwrite when this company goes public, how is Niraj going to evaluate it? How are other public market investors going to evaluate it? And it's on the basis of that that we're actually underwriting returns.

So, for 2022, if I look at last year, there wasn't a lot of activity in the private market, because valuations were still coming down. But as I look forward, what we're seeing on the ground is that people are coming to embrace the reality. They understand that higher interest rates are here, the days of 2020, 2021 are behind us. And you're getting where we’re starting to see material discounts on a lot of the assets that earlier we couldn't justify given the prices, but in which now we would potentially be interested. So, I think the key point to me is that privates give you access to a different set of returns, which I think is hard to capture within the public markets, and I don't see that that regime changing necessarily.

Xiaying Zhang
Niraj, I’ll give you the opportunity to debate Yash.

Niraj Bhagwat
I think we're both on the same thing and you're both kind of saying that: focus on valuations. And I'm just making a simplistic view, in which when you look at the history of markets over the last 80 to 100 years, every time there's been a winner in a decade, it never repeats itself the next decade. So, if, and that's a big if, we enter a new regime, then I'm asking myself as an investor if should we be open to something new, different happening. I'm saying that in my own portfolios, I'm looking at it but I think if you ask me the question [as part of the] big picture, I'm just open to something different happening from the last ten years.

Xiaying Zhang
Perfect. Great, thank you. And I think yes, you did mention that obviously, on our private side, we do run global IPs. So, you get to see a lot of the deals that our US colleagues are working on as well. I'm just curious to see whether you can help us compare a little bit when it comes to the privates and the areas that we're playing in? What are some of the main differences or even similarities compared to the North American market versus the Asian markets that you're covering today?

Yash Patodia
So, I think the similarities is an easy one, because I think the trend of private companies staying private continues to be really strong. And I think it's important to step back and think about why is that the case? Why are companies staying private longer and the reason, when we talk to founders, we find is that when they're targeting a really large market and they want to invest and they come into the public markets, there's often a lot of pressure on a quarterly basis to show earnings. And I'll give you an example.

There was a company that we invested in, one of the largest e-commerce players in Korea today. When we met them, they said they want to raise hundreds of millions, actually, billions, in order to develop infrastructure to enable really quick delivery for e-commerce, and their public peers said, we're not going to do anything like this because if I take a billion dollars off my balance sheet to invest, my public shareholders will kill me. Six years later, all these companies are public and it's still the same conversation, one continues to invest in infrastructure and is actually starting to see their margins expand. The others are still saying that "I'm not going to invest because if I do that my public shareholders won't like it". Now, if the company we invested in on the private side had gone public, I just don't know whether they'd be able to raise enough capital to actually make the investments that they needed to and become a sizable player today. So, I think that's the benefit. and that trend, I think continues.

And I think the reason why it's become more relevant in the past couple of decades, as opposed to [those] prior to them, is because a lot of these companies can scale very quickly. Like we saw in that chart, you'll see quick scaling. And, as a result of that, if you stop your journey in the middle of it, you may not be able to capture the market the way you can and make the strategic decisions that you want to in terms of the differences. I think the US market has done the private side for a long time, The capital markets understand it, they're ready for it, they're ready for these companies to go public. Markets in Asia are still evolving on that front. And I think that's one of the challenges that companies have, that even if they do want to go public, they just won't find shareholders on the public side who understand the nature of these businesses to actually subscribe to them. So, I think there's a difference in what the market allows. And that's another forcing factor for companies to actually stay private for longer, because they not only want to capture the market, but they want to start showing profitability in order to then go public in these regions.

Xiaying Zhang
But maybe we just end the session by asking you guys, what is a one key takeaway. 30 seconds. For each one of you, for our audience here,

Yash Patodia
I would say take us at a really interesting spot. So, look for differentiated access, which in my mind is public equities within Asia on the tech side, because they tend to be underrepresented. And most people aren't even aware of them. And then differentiated access to the private side because the value creation that happens when a company is private, tends to be tends to be captured within the private equity space.

Niraj Bhagwat
So I would say three principal things that I think the last three years has taught me as an investor more than ever: that we should be open to possibilities which we never dreamt off. Who would have thought of COVID? Who would have thought of the kind of war that we are seeing in Europe in today's times? And so, I think just be open to the possibilities that something different might happen. And you'll be ready with your portfolio and look at your portfolio differently than perhaps the past as I'm sure that we all had.

The second thing I would say is obviously I'm going to be biased, but I think Asia, when I think globally, is the area that is going to take leadership in terms of the equity asset class, I can't find any other place which is valued as attractively, with good balance sheets and a good growth profile. But within that, I would argue that people focus a lot on China. I think people should focus on what about other businesses across Asia, because that's where I think you make money. And I think that's what Nick hinted as well.

Session 3

SPEAKERS
Dáire Dunne

Thank you. A lot has changed in Singapore since I moved here. When I moved to Singapore, to get to work in the morning, I used to call a taxi from the home phone in the apartment, I'd speak to an operator, they let me know when the taxi roughly would arrive (that bore no relation to when the taxi would actually arrive). You get in the taxi, you get to work and you had to have cash. If you didn't have something close to the exact amount of money, a big argument then ensued. I could go upstairs to the office, I pick up my copy of the Financial Times. And I could sit down and catch up on what had happened the prior day in markets. There are probably some of the younger investors in the room thinking when did this guy actually come to Singapore, in the 70s?

That was only fifteen years ago. So, I moved to Singapore with my family in 2008, 2009. I've been here ever since. And my life has changed in that intervening period. And I know everybody else's likely has as well. The pattern of our daily routines, our behaviours have all evolved and changed over time. Maybe I could ask for a show of hands from anybody in the room that's used an ATM in the last week. One old school anybody that's stood in a taxi queue in the last week. Another I greatly doubt either of you enjoyed those experiences. And I'm sure you were probably thinking of what you could have done better with the time. So, a lot has really changed. And what I'm here to talk a little bit about are some of those really big, interesting changes that are happening around the world, how we can think about the investment implications of those changes, and understand whether or not they represent opportunities.

Wellington has a really long history of thinking about big structural changes around the world. We started a project in 1981 called Future Themes, where we asked everybody at the organisation to take a step back to think about the big structural changes that are happening around the world and to share those ideas. We've run that project every seven years since then, we have a databank of fifteen to one hundred ideas about the future over that timeframe. And it's fascinating to look at all the ideas that were on earth during that period of time. In the most recent project from future themes that we ran 60% of the participants weren't even born when we ran at the very first time in 1981. So, it's a credible history of long-term, thematic thinking.

And what I'm going to talk about over the next fifteen or twenty minutes or so are three big ideas, three big structural changes that we see happening in the world today, and the investment opportunities that come from those structural changes. So as Emily mentioned, I lead Wellington's thematic effort based here in Singapore. We have a team in Singapore, we have a team in London. And we're really excited about the opportunity that this represents. So, we're going to jump straight in. And these are the three big ideas that I want to talk about today.

So, the first is, we're moving from a concentrated growth model, which was the model of prior generations, to something that will deliberately be more inclusive. The concentrated growth model of the past was that GDP-obsessed model that we all got used to. And if you think back to the inception of GDP, and it was first invented by the economist Kuznets in the 1940s. One of the reasons why there was such a push to come up with a broad measure of economic activity in economies was in the aftermath of the Great Depression in the United States, one of the big lessons learned was there wasn't good enough data to make economic decisions. That was one of the reasons why the Great Depression was as harsh as it ended up being. There was no proper data on unemployment, there was no proper data on inflation. So, GDP was this catch-all measure of economic activity. But even Kuznets himself said it was a poor measure of overall economic health within an economy. But like a lot of measures, as soon as we have a measure that we can look at, we obsess about it, we push it to its max, and it creates other unintended consequences over time. Some of the consequences of this growth obsession of the last forty years have been a real concentration of winners.

We see it in industries where you've got monopolies and certain industries that have really grown successfully over time, to the exclusion of other participants. So, we had this winner-take-all corporate model that grew over time. But at the citizen level within economies, it was also the same: inequality measures have grown substantially over time COVID turbocharge that just in the last few years, so we're moving from this world of concentrated growth, where there's a sense of dissatisfaction around the economic experience that many of us are feeling to a desire. For a more inclusive growth model, something that thinks more about the necessary services that we need to have access to, for ourselves and for future generations. Singapore is not an any different. Inequality measures in Singapore have really ballooned in the last few years. If you listen to some of the big tech think tanks here in Singapore, they've identified social inequality as one of the biggest threats to social cohesion over the next fifty years. So, the government is also taking this incredibly seriously here.. So, this inclusive growth dynamic, we think, creates a whole variety of really interesting tailwinds within economies. The tailwinds from some industries will shift to headwinds and new dynamics, new opportunities will occur. I'll touch on some of the themes included in that big change as I go through.

The second big change that's underway is that our economic model didn't really think very much about climate consequences over the past forty or fifty years, producers didn't really have to think about their carbon footprint or water intensity. They're recycling. We, as consumers, when we go to the supermarket go to cold storage, and there's two tubs of strawberries, one from Mexico and one from Australia. Do you really sit there and think well, I wonder, like what the carbon intensity of their journey from their point of source was like, and maybe I should pay more for one? No, but I'm pretty sure in the years ahead we will have to think about that. Controversially, I would say that within our lifetime, everyone in this room will have their own carbon budget that [they] will have to stay within on an annual basis. Corporates are having to think about it. We as consumers are the real difference makers. It'll be our behaviour that really drives change over time. So, we're moving from this world of economic neglect to one which is much more focused on sustainability. I'm probably not telling you anything you don't know on that topic.

But there's a huge capital shift that needs to happen to make this a reality. And it's an ever-present reality here in Singapore as well. 2022 was 20% wetter than the long-term average in Singapore. The last ten years have been the hottest ten years on record in Singapore. Two days ago, Tuesday, I'm, I'm sure many of you remember it. It was insanely wet. I sat looking out the window at rain basically, from the time I woke up to the time I went to bed. It was the wettest day in February ever recorded, and the data goes back to 1869. So, we're seeing the reality of climate change here in Singapore. You know the big threat for us living here is rising sea levels. You know 80% of the sea wall in Singapore is already reinforced, but a lot more change needs to happen. And in the neighbouring countries, they haven't got the resources that Singapore has to deal with this. Jakarta is a few hours in an aeroplane to one of the fastest-sinking cities in the world. There are 10 million people living in that city. There are six hundred urban centres similar to Jakarta, dotted all over the world that are close to coastal flooding potential. So just think of the amount of capital it needs to move. Trillions of dollars over our lifetimes, to try and adapt to that changing reality. So that's an enormous change. The generation before us didn't spend a second thinking about this issue, the generation that will come after us will be the one living with the worst consequences of it. And what we'll see now is much more pressure on our generation to step up to the plate and to finance that transition over time.

The third, big change that we see happening is changes in the nature of globalisation. I'm a massive champion of globalisation. I benefited massively from it. Personally, I am Irish. I was educated all over the world. I worked all over the world. I married a woman who was born in Sri Lanka and grew up in Australia. We met in London, and now we live here. So, I feel like there's no greater champion for globalisation than me. But I can see that it's changing. The globalisation that's benefited most of us most acutely in the last forty years is this enormous disinflationary force that's been unleashed. We've had amazing stimulus all over the world with no inflation in sight. That part of the globalisation story is leaving us behind. And that's a really big change that globalisation as a force for deflation or disinflation, is weakening, and we need to think about that. Otherwise, we will have to live structurally with higher prices for almost everything into the future. There's a geopolitical angle to that for sure.

But I think it really does mean that we need to think differently about how we use innovation, innovation in goods, for sure. And you can see in the manufacturing sector supply chains changing, you can see the use and adoption of robotics and industrial automation. It's happening faster than ever. But where it's really interesting is on the service sector side. All measures of globalisation related to goods show slowdown. Globalisation related to services, however, is really changing.

A total aside, and an interesting anecdote was that I was talking to my sister recently. She’s based in rural Ireland. And she said to me on the phone ‘Something that we've really gotten into watching as a family is ‘Physical 100’. Have you heard of it?’ I said ‘Wow!’

So, the export of those global services continues to gather pace. It's the same for the knowledge economy. So, I could hear Yash talking on the stage a little bit earlier on about chat GPT and its implications globally. Again, that's a really interesting disinflationary force in the service economy. Maybe we can get a show of hands on who's used chat GPT here in the audience. That's a lot of people. I did a meeting about two weeks ago. And I then brought GPT out. I did a meeting with a CIO locally. And before I went out to the meeting, I typed into chat GPT ‘Give me eight conversation topics for a conversation with an investment, a chief investment officer’. I had actually written down stuff in my notebook before I was about to leave. More than half the topics that I was going to raise, it gave back to me within seconds. So it's changing the nature of all our jobs. There was a story in Bloomberg just a week ago, about JP Morgan clamping down on the use of chat GPT day to day in the office. So, we're used to thinking about innovation and automation and its effect on globalisation in the physical goods world. But in the service economy, we're really going to have to get used to that in the years ahead. And that likely will be where the disinflation force evolves.

So, these three big areas of change are three things that we get very excited about. Why not have a more equitable world that’s more sustainable, where we harness the power of innovation better in our day to day lives. So, these are big structural change, changes that we see happening around the world. But they generate really interesting investment opportunities that I want to touch on. The investment opportunities here are under each of the three big categories of inclusion, sustainability and innovation.

At Wellington, we manage a modular platform of themes that are global, and emerging markets that cover all these ideas that are on the page. Just some ideas. So, within inclusion, you can think of things like healthcare inclusion. There almost isn't a government in the world not trying to spend more on health care. That's particularly the case in the emerging markets. Healthcare spending as a proportion of GDP in emerging markets is less than half of what it is in the developed world, but it's growing twice as quick. 85% of the world's population lives in an emerging market, 90% of the world's population growth between now and 2050 will happen in emerging markets. So, this healthcare inclusion idea is something that we can get really excited about. Financial inclusion is another one of these inclusion ideas that we think is really fascinating. If you read much about the UN Sustainable Development Goals, they make it very clear that almost all of the seventeen Sustainable Development Goals are built upon the foundation of financial inclusion. Without access to capital, it's very difficult to make long-term decisions. You can't save, you can't invest, there's no stability. So that financial inclusion idea is a really fascinating one all around the world. But particularly in the part of the world that we live in here.

On the sustainability side, there's an enormous range of different ideas, from climate mitigation to climate resilience. The resilience idea really copes with this concept that no matter what we do, from now on, no matter how hard we try, there's a certain amount of global warming baked in. It's irreversible at this stage. And that means rising sea levels. That means more volatile weather patterns. It means hotter temperatures, and means longer monsoons, I won't ask for a show of hands, but who's sick of the rain at this point? We just have to get used to that. So, this climate resilience theme just focuses on the enablers. That will help us cope with that in the years ahead. The future of food is another fascinating idea within the sustainability category. The food system is one of the largest greenhouse gas emitters globally. The waste within food is incredible. Almost 40% of all the food that we produce ends up as waste product, it's not consumed. So, thinking about how we make food more efficiently, how we store it better, how we recycle it more effectively, are all really big issues that need to be addressed over time. They're all politically sensitive. And the food lobby and the farming lobby and countries around the world continues to be incredibly powerful. So, change has been slow but the desire for change continues to accelerate. Singapore is a country that imports 90% of its food. I can play around with the margins to maybe get that number a bit lower. But food self-sufficiency is not within sight in Singapore. So, understanding how you have a more resilient supply chain of food over time is incredibly important. And the crisis in Ukraine and Russia has been a real wake up call. In that regard, food security has become national security in countries all around the world. In the innovation area this is really fascinating.

There are so many really interesting things happening in this space, the automation and robotics one is one that I think has a real relevance for people here locally. Singapore has the second-highest adoption rate for robotics in the world after Korea. It's funny, we see it in our day to day lives, we're used to thinking about robots and big factory settings in the industrial structures. But actually, if you go to a museum now, there are ones in Singapore where you can get a robot to take you around and give you a guided tour, you can go for a walk in the Botanic Gardens and see robots cutting the grass at night when most of us are sleeping. You can go to Changi or into the MRT and see robots either cleaning or offering people guidance or direction. You can go to libraries and the book replacement on the shelves, five thousand books a day, being put back by robots. So, in each layer of our lives, our interaction is changing with technology in a way that it might be jarring to us, it's very natural for our children. Elsewhere in the innovation category, I want to touch a little bit on enterprise intelligence as a theme. COVID was a massive accelerant for the use of enterprise software solutions. I'm sure everybody here at this point is sick of using Zoom or WebEx or Teams.

Ten years ago, we wouldn't have dreamt of using that technology the way we have it today. But as we've adopted those norms, we've also adopted the norms of file sharing, cybersecurity, data management, cloud systems and all the infrastructure that has to come behind that to support it. So that evolution is real. And Singapore is a very knowledge-based economy; for sure, I think we're probably more adaptable to that. We've seen it probably earlier, and the systems here and the digital infrastructure in Singapore is world class. But in many parts of the world, they're still way behind. So, this opportunity, again, we find really, really fascinating. I'm going to touch on one theme in a tiny bit more detail, which is education, because it's one that I have a real passion for, and one that I'm really fascinated by. So, I'll obviously have you know I've got three children. They're all at varying levels at school and actually,

I sit on the board of UWC here in Singapore. So, I have real passion and interest in schooling and how it's evolving and an interest in the use of technology and the interaction between the virtual and the physical and how it's relevant for schools over time. This is such an enormous opportunity and it's changing so quickly. Governments are weighing in with really strong policy support. You can see that at the top of the page humanitarian organisations all over the world recognise this as the bedrock on which economic progress can really be made.

There are three big changes happening in the education space that I really want to touch on. So, the first is the demographic change. So, we all know this population, the world is increasing, but it's actually increasing at an accelerating rate right now. Over the next twenty years, the population of the world will increase by 12%, which is a staggering number. Over the last twenty years, we've seen a huge increase in the number of children leaving secondary school. Over that twenty-year period, the increase has been 30%. Many of those have come from the emerging world. The frequency with which those children go on to tertiary education to university or vocational training or others is less than half of what we see in the developed world, but it's increasing. The demand for education continues to rise, populations are growing. And there's a huge role to play for private capital to make that happen. You know, we all know, the scare stories in China of what happened to the after school tuition space in the last few years. But we shouldn't ignore the fact that the private providers of secondary and tertiary education have actually increased their footprint in China over that timeframe with government support, because the government knows that on their own, they can't meet the demand requirements that are there right now. So that first big change is that population dynamic that we're seeing is happening all over the world.

The second is, the delivery is changing. COVID radically changed how education has been delivered all over the world. That's not a temporary change. I can see it in conversations about the future of education, there's a really deep need and willingness to understand and entertain the idea of the 'Virtual Campus'. How you can use infrastructure more effectively, how you can get children on different learning schedules, how can we customise more easily experiences in the virtual world? How you can bring in skills and expertise from all over the world to benefit your cohort of students, and how you can take what you're doing in your well-funded school environment and make it accessible to others that don't have access to that and other parts of the world? That digital transition is real and permanent. And that will be a lasting legacy of COVID. For the children that have grown up with that, for them, that's not a big deal. It's a natural part of what they've experienced at school in the last number of years.

The third really big change that's happening in education is that the things that we need to learn have changed and the nature of our work has changed. I mentioned chat GPT and I mentioned automation and robotics. The jobs of the future are different. And what we need to learn, of course, is changing and evolving. The World Economic Forum estimates that one billion people need to reskill between now and 2030 to stay in the labour market. So, it's not just about schools and universities. It's about training and providing those learning opportunities for us to stay relevant in our jobs over time. So, what I want to finish on before we open it up for questions, and I hope there's a few questions and are what I really encourage you to think about as it relates to thematic investing.

So, the first thing I asked you to think about is how underrepresented any of these big structural changes or themes are in your portfolios today, because that's the big opportunity. We have seventeen global themes on our platform. They're all less than 3% of the MSCI ACWI Index today. I don't know how big they'll be in the future, but my guess is many of them will be a lot bigger than that over time.

The education theme that we have is ten basis points of the ACWI Index today. What would that number be in a decade's time? So, look for things that are underrepresented in your core equity exposure that you're excited about, that you think have structural tailwinds behind them. The second point I make is to think about thematics as a bridge, to think about it as maybe insulating yourself against the core of the future. Healthcare in emerging markets. A decade ago, when we were building our exposures, was one hundred and forty basis points (bps) of the index in that ten-year period, it's gone from one hundred and forty bps in the index to about 4%. That's a big change that has been positive, but it's still 4%. That's tiny relative to where it could be over time. In the developed markets. It's like three or four times that level. So, think about thematics as a bridge to the core of the future.

And then the third point I would make is that thematic risk is different to security-level risks in portfolios, which have to be really thoughtful and deliberate about that. Over time, thematics has developed a bit of a reputation as being a bit volatile. But with the right kind of risk management systems and the right kind of portfolio construction techniques you can insulate yourself against that. We spent a lot of time thinking about the management of risk from a thematic perspective. And we'd love to be a thought partner for anybody that's interested in allocating more exposure in the thematic space.

There's amazing, exciting things happening in the world today. And most investors don't have sufficient exposure to these big areas of structural change, and thematics can provide a way to do that in your portfolio.

Session 4

SPEAKERS
Ross Dilkes
Irene Tse

MODERATOR
Jonathan Ross

Jonathan Tan
Good morning to everybody. And it's a privilege to be sharing the stage for two very distinguishing speeches today. Just really looking back, 2022, as Emily mentioned, was really volatile year. It was the first time we've seen fixed income in such big draw downs, equities together, negative and double-digit

returns, and the efficient backdrop rate hikes, supply chain disruptions, geopolitics, Russia, Ukraine, all these things are really things that we're super-familiar with. And really, we're trying to see going forward, what kind of opportunities are there. If you just look at the title, we have here today when volatility brings opportunity.

This sums up what we think is going to happen for 2023. We think that really, the volatility will bring us a lot of opportunity across this process, but particularly so in fixed income. Let's dig into debt in three key angles. The first is going to be on the global cycle. The second, the central banks, and third, the potential for regime change. Now, just starting with the global cycle, a couple of slides should bring us true. And if you just look at any metric out there, this has showed the rough picture that growth is dipping down. And the consensus is that we will be seeing some of a shallow recession on the horizon. Then again, there are options to growth. You think Japan comes to mind, China comes to mind. And this chart is a chart put together by Oxford, they look at the measures in terms of stringencies of COVID restrictions. And you can see China both on a relative basis as well as the absolute basis, still at the top. So, upside risks to global growth are indeed around. Now, maybe we just start off in terms of the global cycle here. And I wanted to mention first in China now, I mean, given that you're really the go-to expert in a lot of China things, I just wanted to let you share with the audience here today how you think about China. How do you think of the upside risks to growth in 2023?

Irene Tse
Yes, I think with the opening behind us now, let me lay out five cases, upside cases that show why China is not currently in the price.

First, in terms of property, China is not Japan. If you look at most of the property developers, they have either gone bust or they are being assaulted by SAE. SAE does not have a balance sheet problem. So, what China was able to do in the last 18 months is exactly opposite of what Japan tried to do in the fifteen years after 1989. So they managed to claim a property sector.

Two, the government has recently started relaxing the purchase of second home. For example, Wuhan, an upper-tier city, was the first experiment to relax restrictions all the way. Those of Dongguan and Fushan followed afterwards. Now, to give you some context, all these restrictions were put in place in 2016. So, the fact that they are now relaxing second home restrictions, is basically [a sign that], in my view, the leadership now is pivoting again, away from the three rent line.

Third, one key positive remains the debate of how big access saving is: net household deposits rose from about 15 trillion in 2022, to now about 50 trillion in 2023. In GDP terms, that is basically about 22% of GDP in 2021, to now almost about 40% of GDP, a big number. I don't think all of its scope is spent but I would say probably enough for revenge spending. One view that I feel very strongly about and is often debated among investors is if the incoming economic team is going to be more pro-growth, pro-market, and pro-investment than the outgoing one. I also think they will execute much better than the outgoing economic team. So, the big question to ask among investors is is there a policy here that can set the Chinese economy on fire. I see two things, which I think we have to watch very, very closely. Leadership meetings are coming in March and April. What is the consumer stimulus, which was very hotly debated going into the December economic conference? One, hey did not have a consensus because I think the income inequality for inclusions was a big debate about how policies should be set. But I think this will come up again, in the upcoming conference. Two, I think eventually it will really need to get the economy on a sustainable trajectory. I think it requires a one-off inventory adjustment on the housing policy. What would it look like? I think it's going to look like this, the Peoples' Bank of China will revive the PSL facility to lend to support public housing initiated. If we see that, I think we'll get a one-off inventory adjustment. And that will be a very, very powerful stimulus in the current environment. I think we will see those two things coming out of the Leadership Conference in the next 40 days. I think that this will create a great opportunity to continue the uptrend in Chinese equity. I think you can confidently buy on any weakness in equity. And I think the regionals will benefit a great deal as well, particularly Japan and Australia.

Jonathan Tan
Thanks Irene. Thanks for laying all that out and giving us some signposts to really look at. And Ross, maybe I'll turn it to you in terms of building on debt. If you can think about the regional cycle and global cycle, I'd really be interested to hear your views on that.

Ross Dilkes
Yeah, I mean, I think that's, that's obviously the bull case for China. And we've been grappling with some headwinds over the last sort of three to six months around the global economy. But in truth, there's been some resilience there anyway. And China is now a big swing factor. So, as we move into Q2, Q3 even later on in the year, the range of outcomes here is pretty wide. I think even though it's why the skew is more to the upside than the downside, clearly, the China reopening was a big surprise. Not just in terms of the announcement, but I think it's gone even faster and better than the policymakers believed it would. So, this cycle might be more resilient than we thought, as recently as three or six months ago. In truth, Asia actually was impressively resilient if you think about going back to 2021. And if you said to anyone who invested in the Fed would hike 500 basis points from zero to a policy rate where we are today. The dollar would be as strong as it has been, you've seen a 15 to 20% adjustment in DXY. I think people would have said that the region would be really struggling, emerging markets more broadly.

But certainly in Asia, we haven't seen that, central banks have been actually very, very focused on growth, rather than the concerns around global forces. I think that's very different to previous cycles. And that's really important. I think it's a sign of maturity, I think it's a sign of confidence in the underlying growth of the economy. And then what I think what that means for the future, I think that we are likely to really benefit and outperform clearly being dragged by China's pace of reopening. But there's resilience there that gives me confidence around fixed income markets more broadly, local market returns last year, hedged were just below zero, which is incredibly resilient. Even adjusting for the dollar impact less than 10% returns, fixed income in the region and credit; essentially, the whole total return was actually just driven by treasuries, the excess returns were almost flat. I think this is a real sign of maturity, and probably underappreciated, because people focus a lot on the headlines they read around China property, the other concerns they might have around defaults across the system. I think I think there's a lot that we should be recognising and feeling positive about. And that obviously gives me confidence about where we go next, even if we have central banks remaining hawkish as they are right now.

Jonathan Tan
Thanks for that. And I know this question is on the cycle. But maybe just as a preview, China, policy top of mind for everybody? Is it a buy? Or is it more nuanced?

Commented [GGA(1]: There is a garbled word prior to "policy" that is essential to understand this sentence.

Ross Dilkes
Tough one early on. [The] Short answer is no, I think the policy prevent is pretty clear. So, we don't need to debate that I think our brains laid out the bull case that could help to clear some of these structural problems that still exist. But even if you look at the recent data, the shift between SLV contract sales, which has gone up materially, private numbers are still contracting. This is this is a big challenge for the names that still exist or have survived so far. There's a big divergence between higher-tier and lower-tier cities. So, unlike previous cycles, where you had a broad shift, and you could probably capture that through a fairly diversified allocation to China property and watching that really perform, this time round I think it's very, very selective. There are still some refinancing challenges. Even the future path, I think, is still uncertain. What sort of outlook do those companies have in terms of forward profitability? Financing cost that they need to potentially stomach? So, I think the answer is no, but I also think there's opportunity there. So, I think we're leaning into selective ideas, selective names, but I wouldn't think it's going to be the same cycle, as we've seen in the past.

Jonathan Tan
Thanks for that. And if we move on a bit into the next topic, you alluded to this a little about central banks and the impact on markets, we all know how significant central banks can be for the global cycle. And just going forward, if we just look at the way that the markets are pricing in higher for longer is definitely something that's priced in the market. We've seen recent data surprises that has led both the rate cut expectations a bit further out, as well as the lines on the dots on this page a bit higher than they would be as shown here. At the same time, if we look at how QE and QT has happened over the past several years, we've certainly been seeing that significant impact that central banks have had in terms of volatility and ability to suppress. Now, Irene, we've been hearing a lot of this in terms of the internal investor debates, and you've had strong views on this topic. We do want to hear more in terms of how you're thinking about QE and QT.

Irene Tse
Yeah, we have, I think that to speak to the Wellington platform, we have very opinionated equity investors and we also have very opinionated fixed income investors and we and also macro investors. So, the most heated debate in the firm right now, one of them is why is the equity market holding up despite weight has gone up almost 250 bps from the middle of last year. My view is that the reason we're holding up because we're now currently in global QE. We're no longer in global QT. Let me explain.

Coming into Q1 this year, when the BOJ widened the ban on December 19, which was supposed to be a monetary policy tightening, in hindsight, it was actually the beginning of global easing. The reason is, by managing the yield curve exit instead, the amount of JGB they had to buy was so large it was basically two of the faculty, so we went from global QT to global QE actually at its fastest pace since the middle of 2021. So let me give you some numbers. The BOJ has intervened in the JGB market to the tune that by the end of December, they almost own all the JGB. First three, they in 2023, between purchasing JGB and the landing operation, they basically intervene in market to the tune of about 10 trillion in YEN terms. Now to give you some context, in the whole year of 2021, they only bought about 15 trillion JGB. In three days, they did 10 trillion in order to defend them with a band. So, in January alone, they spent about 6% of GDP to defend YCC. So, with global QE back on again, I think that's why the equity market is holding up.

So, let's not look at the past. Let's look in the future. What is it going to look like in terms of global liquidity going forward? When am I supposed to be more conservative on equity again, or am I supposed to go for it? Here are the three factors I think we have to watch carefully. The first one obviously has discussed how BOJ exit YCC and negative interest rates. Two is the treasury January account of the US, it's going to be a very big swing factor in also global liquidity and what is going to drive that is going to be driven by estate and the tax we see going into a debt ceiling. And how and when the debt ceiling is going to be resolved earlier later, that will have a big impact in terms of what the Treasury general account would do. So will the Peoples' Bank of China's balance sheet. PBOC has been injecting a lot of liquidity, but they have not done any long-term funding. For example, in December and January alone, they actually contracted the PSL by about 30 billion. So, what they are going to there? They will go pull out another 2016, where they directly injected 6 trillion into the banking system, which would be the key.

So, I think going forward the interaction of this three things, BOJ, debt ceiling, and also the PBOC balance sheet will be the key to decide on liquidity going forward. My best assessment is we'll go back to global QT, again, sometime between April to mid-June depending on how these three factors interact with each other. Again, these three factors are extremely difficult forecasts. They can swing both ways very quickly. But I think that's a sweet state we have to watch very carefully.

Jonathan Tan
Thanks, Irene. Ross, your space is largely the USD denominated Asia credit market and obviously global central bank has had a big impact here as well. Just really wanted to hear your thoughts also on how central banks affect your space and how you're thinking about the world.

Ross Dilkes
Yeah, I think that the QE QT debate is really important. And I think adding on to what Irene just said, there's another phenomenon where when QE was being used positively, central banks wanted to make it a very proactive policy tool. But I think the counter to that is when they're talking about QT, they want it to happen in the background and no one talks about it. And that disconnect is really challenging. I think what's really interesting about this recent cycle of rates going higher, which is probably a little underappreciated is that maybe the power of QT was substantially more than we thought. And what I mean by that is why haven't these rate hikes actually started to impact the economy as much as we thought they would?

And I think partly, the answer is we had a very long period of time with rates very low. Corporates use that extensively to turn out debt at very low levels. So, the incremental shift higher is only going to happen over time, you're not seeing the stress emerge in the system as a result, that's one powerful factor. But I think also look who's now owning a lot of debt, the central banks have accumulated so much of that borrowing that they're now actually stomaching the losses. So, in the previous cycles, when rates were going higher, it was actually going to come directly through to an end consumer, whether it was through a financial holding an impact on their mortgage rates…something going on within the economy.

Now, I think there's been a kind of suppression of that volatility. And I think about that, from the perspective of you asked about the Fed and the impact on corporates. Well, there is uncertainty, clearly where rates will go from here. I think the Fed probably would like ideally, to pause and see what the impact will be. But naturally, they will stay hawkish for now, in the in the face of the inflation numbers we see. But from the corporate side, I actually think that the story is actually less bad. Not only have they used that advantage that I just talked about previously, but I think they're in a position now where they have confidence in the outlook, in a way that they wouldn't have had previously. And they have the ability to access markets locally, historically, where they had to just take whatever those higher funding costs would be in dollars. We haven't seen that narrative, we've seen people actually pivot to local markets, we've seen stability in those local markets. So, it actually takes the pressure off the US dollar space in a way that we haven't seen previously. So, I actually think the Fed is clearly going to stay relatively hawkish here. We have to live with those high rates for a foreseeable period of time. But actually, the impacts not as negative as you would think, within the corporate universal, or certainly Asia credit.

Jonathan Tan
And, obviously, you're also an expert in local markets. And this any comments on the local central banks, is there any different backdrop you're seeing in the region?

Ross Dilkes
Well, I think one of the biggest differences is just composition of inflation. If you think about inflation as a global phenomenon, particularly through a developed market lens, it's very much about services. Dáire mentioned it just previously, Asia was very much a good inflation number and services as a smaller component, not obviously true for every country across the region. But certainly across the emerging part. That number is already actually coming down. And to some extent, is easier for governments to control that number as well, whether it's through subsidies or other measures, so I think they've been fairly confident that the numbers weren't going to be as bad as we see elsewhere.

Local markets have actually been, as I mentioned, previously, pretty impressively resilient. And certainly, the currency move is less than we would have thought. I think they've generally focused on growth and not worried so much about inflation. So that that to me is, again, a sign of resilience, but also opportunity, as we move to a period where I think we worry less about inflation and think about the forward, I think you're going to start to see central banks almost have the confidence to think about moving ahead of the Fed, which again, is a very new phenomenon versus previous cycles.

Jonathan Tan
Thanks, Ross. And again, coming back to the global central banks. We've seen two major markets here, Europe, Japan, both previously having a lot of negative rates looking outside. Now, interest rate

differentials have shifted so much, and just Irene just wanted to get your thoughts on Europe. How's the ECB and central bank actions there going to impact us?

Irene Tse
I started my career on email convergence. It’s a topic that usually when I start talking about Europe, people fall asleep. But I do think something fundamental is really changing in Europe. And it's really important, and I will spend two seconds on it, I promise won't be long. Structural inflation euro is really, really changing, it’s a lot higher. Our view is, I think there is a risk that European inflation will outpace US inflation.

I know that it's a very non-consensus view, and there are four reasons behind it. One, in the past, Europe had a lot of disinflations primarily because of the periphery. And there's really an end to the relative of this inflation in the periphery area, the core inflation periphery, is actually higher than the whole of Europe currently.

Two, one thing we learned through COVID, which was also very opaque market academic debate is fiscal policy is inflationary fiscal in Europe, is expansionary. And here's the math. The government came out with 5% of GDP of fiscal in response to an energy shock at the worst of 6.5%. European gas prices have gone down about 90%. So that energy shock is one from six and a half to one and a half. Guess what the fiscal has come down some but they still at about 4.5%, almost 3 times the size of the energy shock.

Three, monetary policy is still very supportive. Adjust to what they did, they still have a negative rate. And to me, ECBs have too many mandates, right, they have to fight inflation and lately, they decided that they have to make climate response changes as well. To meet that increase, multiplied by managing all the different mandates that increase the possibility that inflation would get out of hand.

Lastly, there's something really changing in the labour market in Europe. And that, to me, watching the evolvement of EMEA to now is my biggest surprise, 12 out of the 19 countries are going to be increasing the minimum wage this year, after 25% increase in Germany in October, there's a list of companies that we track wage deals that has gone up from 4% in 2022, and from our tracking is going to be about 10% this year. So that to me is also a very important component, and the participation wage in European labour market essentially has really increased, and through COVID their labour market has gotten much more dynamic compared to every major G7 country. So, to me, I think this is the story that the way that they have been impacting in Europe is going to be less than we think. And the structural inflation story is going to go up from here in Europe.

Jonathan Tan
Thanks, sorry, I've seen the timer, it seems a bit low on time. So maybe I'll just quickly go through some of these and this chart really talks about the macro environment, I understand that Nick has shown something quite similar in his session. So, I will be quick here. Essentially speaking, this is showing quadrants of where we are in various quarters in terms of real-life GDP, the left quadrants and this disinflation, the right quadrants are periods of inflation. The top quadrants are periods of positive

growth, the bottom quadrants are periods of negative growth. Ultimately speaking, I think very similar to what Nick mentioned, we spent a lot of time in this top left quadrant disinflation and growth of so called the Goldilocks type of period, where inflation environment, as our speakers have really talked about has allowed central banks to dampen volatility and help us go through a very strong growth cycle. If we look in the 30 years before, just now was about 1985, to today, here's 1964 to 1995, and identify if you see a much more messier chart, the cycle really oscillated across various quadrants very frequently. So really, one thing is, are we really at the cusp of a shift and of a regime? Maybe we just go quick one for this one first.

Irene Tse
So one thing that we learn by studying this chart is in those in the 70s regime, while we oscillate in all these four quadrants, we stay in each quadrant in a very short period of time, six months on average. So that's how you that you need to be nimble. You have to forecast ahead which quadrant you go into. But that's really easy to say why, how to do in hindsight, you can always say, Wow, we were in that quadrant. I think if we were back into the regime that will oscillate between quadrant in short period of time, I think 60/40 that the single allocation makes could be very problematic.

Jonathan Tan
And Ross, just a quick one, in terms of your view, impact on market climate implications.

Ross Dilkes
Well, I'm biased, right? So as a fixed income guy, I just wanted to go top left and stay there. And then I can tell everyone that you can buy bonds with your eyes closed. I'm sympathetic that there are definitely some things changing within the global economy that we need to factor into our thinking and quite possibly we don't go back to where we were. I guess the counter argument is that there are some structural forces that are still very powerful,

There is a lot of debt in the system. We clearly haven't solved that problem, we've actually added to it. There are other structural factors that are very powerful: demographics being a very obvious one. So, against those two sorts of competing factors. I'm going to keep an open mind. I think there's certainly a period of time in the in the sort of short to medium term, that we need to be very mindful about that portfolio flexibility. And possibly we're engaged with the structural forces down the road. I guess the only other point that I spend a lot of time thinking about is, and I think Dáire mentioned it just before is asset allocation has always been thought of as a sort of DM and an EM problem, or solving for those solutions, potentially maybe what we're talking about here is as we go into a different environment for cycles we need to think differently about where are those cycles impacting asset classes. It's not just going to be fixed income, bad equity, good. Maybe it's very much more now that you've got an Asia block, which is kind of anchored by the RMB. And you end up with a European block, across Sterling, Swiss, a Euro, and then potentially a Dollar block. Now, I don't think we get to that tomorrow. But I think that these are these are decisions or thoughts that we have to have about how do we allocate for clients. What are the right ways to think about the asset classes? I think the old model is not going to be fit for purpose, even if we haven't solved the debate about structural shifts in regime. So I think that's something that I think a lot about, and I actually think that's probably more important than trying to decide at this point: where are we going to be for the next 30 years?

Jonathan Tan
Gotcha. Thanks. And I will leave as much time as I can for Q&A, there are still a couple of slides. So, I'll just breeze through them really quickly. And starting yields are really attractive as they are right now [at] 5%, [the] highest they've been since 2009. I think we all know that. And [I] just wanted to point out that in terms of thinking about physical allocations, we think of physical doing for roles in portfolios, income, return, liquidity, diversification, when Treasury is yielding 6% - 8%, that could do everything in one bucket. Right now, we need to think a bit about how each and every allocation within fixed income can do the various roles, especially as Irene mentioned about diversification. How do we fill that role?

I understand [that] you have the slides with you as well. When we think of it in three core columns and buckets here, the first one is to reemphasize fixed income, understand that a lot of clients have come into this period underweight the asset class. In the middle column, we want to think about how to complement the portfolio with flexible strategies, liquidity type of strategies, alternatives, really important to build in the additional diversification, uncorrelated returns monetize that volatility. And the last one on the right side is a start, dipping and changing into higher yielding credit.

If you think about the attractive spreads right now, largely we're seeing, the medians are wider. If we see volatility, as we expect, then if spreads do widen out a bit more, if you do your due diligence, or start dipping or trenching into the asset class. Over time, that can actually lock in us for a really good period of time. 10% on high yield 8%, on Asia credit for the next five to six years, really attractive total returns. That's all we really had, in terms of the prepared remarks and the panel discussion.

Session 5

SPEAKERS
Philip Brooks

As we've touched on during the course of the conversations today, we as a firm we don't have a chief investment officer. There are different teams with different views. As I'll highlight as we go through these slides, some of them will talk to some of the consistent through lines that we see across the platform, areas where there's more agreement than disagreement. Some of the slides will highlight other areas where there's more active debate and new differing views across the firm.

So, starting off with China and emerging markets, the story of last year was about the dramatic underperformance of China, your various things coming to affect there. For many investors based in the US, I think there was a misconception that actually, the focus of US policy on deglobalisation and containment of China was somehow responsible for that. We don't think that that was actually the case at all. We think this was a domestically engineered, policy-driven slowdown in the economy, reflected in share market performance. But nevertheless, China lagged dramatically. The story of the last few months is the opposite. China, as we were discussing in a couple of the sessions earlier, has changed the direction of policy in the last two to three months, the Chinese equity market has rebounded very, very rapidly, the market is up depending on the part of the market, you're looking at 30 to 40%. Over the last few months, it has more than made up as at today, that underperformance that was generated in the earlier parts of last year, it's been a very strong rally. Niraj touched on this briefly in one of the earlier sessions. But we think that there is a lot of opportunity for this current rally to continue. Over the next nine to 12 months, it would not surprise us, if in US dollar terms, Chinese equities rose by another 30 to 50% from here. There is a huge opportunity, at least in the short term, in China.

Question marks about the long term. Now, why would there be question marks about the long term? Well, there's a few reasons for that and things can always change. But what this chart shows is over the last 30 years, the cumulative total return of a few different markets and regions. That line along the bottom, that dark orange line there, that's China, $100 invested in China 30 years ago, is today worth about $126. Now that compares to the US, that's the top line on this chart, where that $100 invested would be worth just over $1,650. So, China has not created value for equity investors over a really long-term horizon. Again, that could change. In the short term, we have significant optimism about opportunities in China. But what we would say is investing passively in China, buying the Chinese beta in the hope that that's going to generate a good return. That's proven historically to be a really bad strategy. And we think it continues to be a really bad strategy today.

That's not to say that there aren't stock level opportunities in China, there are. We think they're really interesting, but you definitely don't want to pass the exposure there. Another interesting thing that we're talking about in the firm is the shift in valuations that we've seen over the last year or so. And indeed, over the last decade or so, what this chart highlights is the cyclically adjusted PE. So kind of a long-term smooth PE measure of various markets and regions around the world. The top section of the page is the most expensive markets, the bottom section of the page, the least expensive markets, very top-most expensive market in the world today, the US market, very bottom least expensive market in the world today, China. Now we've seen over all and the lighter blue section is the valuations 12 months ago, the dark blues today, we've seen a big valuation reset down and global equities in the last 12 months. That's great, equities were clearly too expensive, particularly in certain segments. So, the fact that equities are less expensive today is a more compelling buying opportunity relative to a year ago. But what the spread of valuations also highlights is that within global equity space, valuations very materially and in particular, the US is far more expensive still today, even after the 20% decline last year, than any other market in the world. When we look at this page in here, we're thinking about five years' or 10 years' time from now, what does that mean? Well, it means that we're seeing more opportunities in non-US markets than we are seeing in the US as out today on a long horizon. And in particular, we're seeing more opportunities in Asia and the emerging markets around the world. That, on a 10-year view is where many of our investors are most bullish today. Now, those valuations that we just saw on the previous page, that cyclically adjusted PE, one of the reasons that's such an interesting way of thinking about market valuations, is over time, it's had a very, very strong relationship with the forward return of equity markets. So, as Niraj was mentioning earlier, the price you pay for an asset today is incredibly important in determining what return you will generate from that asset over the coming years. You pay too much, your return is low. What this chart shows is because the US market is the most expensive market in the world, looking back at prior periods where the valuations were the same as today, or similar levels, what the return was over the next 10 years. The answer is 5% per year. Now 5% is a lot better than zero. So, I guess it's not that bad.

But if you think back over the last 100 years of equity market performance, on average, markets generated about 10%, 8% to 10% per year. 5 is a lot lower than that long term average, Europe and Japan and middle, somewhat less expensive returns, if history is a guide, maybe five, maybe 6 or 7%. And then yellow right at the top of emerging markets. Here, we're looking at a potential expected return of 12% to 13% per year, over the next decade, more than double the expected return using this framework of the US market. Now, we've been talking a lot about regime change in the presentations today. This is one area where there is a greater view of consistency, internally, more people are aligned to this idea that one area of regime change very likely over the next decade is the US not being the best-performing stock market anymore. It will probably be non-US markets, but specifically, very likely emerging markets. And within that, very likely Asia.

Now, why in particular Asia? This links some of the comments that Yash was making and Dara was making earlier about the importance of innovation. Asia today spends more on innovation than any other region. So it is the purple line that ends the chart on the right. And so at the highest level, the one that it just crosses over the yellow line, that's the US market. So Asia and here that line is not all of Asia, that is just China, Korea and Taiwan. So the largest markets in emerging Asia, combined spend more than the US innovation drives returns over the longer term, there's a strong relationship there. I'm not talking about this year or the next year with the next three years. But over the next five, over the next 10, over the next 15, this is going to drive strong returns in Asia. Another thing that we think is interesting is the performance dynamics in Europe. So what this chart shows is the relative return of Europe versus the US over the last 50ish years. What you can see is that this runs in really long-term trends for the last 15 years, basically until about January, the European market consistently had been underperforming the US. At the very far right hand side of this chart, that little uptick that you're seeing, essentially that is year-to-date 2023 relative performance with Europe beating the US. It might be a false dawn, cards on the table. We don't know for sure. But we do think that there are reasons to believe that we may have now seen a turning point in the relative performance of Europe.

Valuations are really attractive, we're seeing some structural growth drivers starting to build their unemployment rates continue to improve. So, there are reasons to be optimistic. But if this is a turning point, and again, we think it could be, not that it necessarily has to be, what this dataset shows is that Europe could well be the better the better-performing of these two markets, better than the US, not just for this year. But for the next five years, the next 10 years. These tend to run in long-term performance trends. So again, non-US equities [are] more attractive than US equities today. Europe, in particular, [is] one of the interesting regions there.

The next topic is on globalisation. The globalisation, there have been some some counter arguments to this in the session earlier today that Nick kicked off. And here, it's an area where there is some debate. So clearly we're entering a world, and we're not entering we've been in a world since the Trump administration, of much higher geopolitical risks. And at the very least, a lot of talk about geopolitics and trade disruption, supply chain reshoring deglobalisation. But the interesting thing is, at least as yet, that talk doesn't seem to be reflected in actual data. So, the chart on the left here, this is global exports as a percentage, essentially, of global industrial output. What that shows is actually globalisation peaked in 2006. Now, it's not showing a drop off, we're not seeing at least as yet any slowdown in globalisation. But nor are we seeing an increase in globalisation. We've been at peak globalisation in the history of the global economy for, 15, 16, or 17 years now, but no change yet chart. On the right-hand side world trade volumes. Yet there was a dip down during the COVID pandemic for reasons we're all familiar with. But what we've also seen is a very rapid recovery in global trade back to that pre-COVID trendline. So no data yet, in terms of that slowdown in globalisation.

The other thing that I think is interesting is and I guess intuitively, at least, we all know this, is that China makes a lot of stuff that people want to buy. So the fact that US policy is sort of China containment, trying to slow down the rise of a strategic competitor, I get that for political reasons. But it doesn't impact what people actually do unless policy changes in a way that makes it impossible. But what this chart shows is, at the dark red line at the top, China's exports as a percentage of their trading partners GDP. How much is everyone else spending to trade with China? Well, guess what? It's an upward slope. People are buying more and more stuff from China, not less and less stuff from China. And so again, this whole debate about deglobalisation…. Well, yes, maybe certainly geopolitical risk is higher. But does it actually mean less trade? Well, no, not clear cut. The other thing that I think is really interesting about this, and personally, my take-away is that it probably also indicates that the thrust of US policy is very deeply flawed. And this China containment policy is China's not even a trade-dependent economy. Why spend so much time focused on an area where it's close to a rounding error?

In terms of China's overall GDP, China is the 15th. We're in the 50th percentile of least trade-dependent countries globally. If we really do see deglobalisation, where we need to worry is the countries on the right-hand side of this chart. Sadly, Singapore is one of those countries, small, open trade-dependent economies are going to get hit really hard by deglobalisation. If this is a trend, again, it's an active debate, I'm personally not sure it is happening. But there's a lot of discussion within the firm. What we do know is happening, although it's happening slowly, and from a really low base, is the diversification of supply chains. So what we're talking about here is this “China Plus One” policy that many companies are starting to introduce.

Basically, rather than solely relying on China to produce whatever it is they produce for that company, having another source in addition to China. Now, where is productive capacity going to when it's diversifying away from China? Well, the answer is, it's going to markets like Vietnam, and India and Malaysia and Thailand. It's not going to the US. There's a lot of discussion about reshoring of production from China and other emerging markets back into the developed world. We are not seeing any significant level of that actually happening. And the reason is because it would be crazily expensive to do that.

One data point: making an iPhone today, let us model. An iPhone in China costs about 1000 US dollars to manufacture. If that was to be made in the US it would be double that. iPhones are already insanely expensive. And can you afford to pay twice as much as you pay today? No, you probably can't. The result of that is Apple doesn't make iPhones in the US. Where do they make them? Well, they make them in China and today they make them in India. What this data shows is where reshoring is happening, it's leaving a higher-cost of production country, China, and going to lower-cost of production countries. In all the countries where reshoring is happening, the wages are half to as low as a fifth below wages in China. Ultimately, this is deflationary, not inflationary. And the inflation debate is one that we're actively having at the firm. How long is inflation going to stay above the trend of the last decade at least? We don't know a single answer to that. But there's a lot of debate and discussion.

Other drivers of inflation? In the recent period, 2021, the recovery from COVID starts, supply chain pressures drove inflation higher, supply chains have already dramatically improved in the last 12 to 18 months, supply chain pressures today are lower than they were before COVID. There is no current supply issue in the global economy that's fully fixed. That driver of inflation was transitory. Energy prices were the primary driver of inflation last year. Energy prices have fallen as at today 36% from their peak last year. Energy prices today are at about the same level as they were over the last decade, over the last decade where inflation was 1.5% per year. Energy today is not a structural driver of inflation. This could change. If we saw war in Europe widen from just the Ukraine focus, this would change. But as of today, energy is no longer a structural driver of inflation, or fossil fuel energy, I should say.

Another driver of concern about higher inflation is the recovery of the Chinese economy. And here, the idea is basically that demand is going to come back on stream, growth is going to accelerate, there's going to be more infrastructure spending, that's going to drive commodity prices higher. Well, guess what, that's a story from 15 or 20 years ago, that's not a story for today, China has better infrastructure than nearly everywhere else in the world, including developed markets. There simply isn't the level of commodity demand from China today, that's likely to drive inflation structurally higher. And again, guess what? During the last decade, where inflation averaged 1.5%, China grew at 8% per year, on average. Today, it's growing at generously 5% in the official numbers, [although] we think it's a lot lower. As it rebounds, it's going to rebound up to maybe six, but not eight. And even at eight, we didn't see a period of structurally high inflation in the global economy. So again, this is a debate internally about what might drive inflation persistency.

The result of all of this is the period of inflation, and it's the highest level of inflation that we've seen in the last 20 years in most countries around the world. That period of inflation is rapidly coming to a close. By the end of this year, this is market data, but our macro team at Wellington agrees with this as well, we think inflation will be below 3%. Now, all of that debate that certainly we had at Wellington, but [which] the market has had for the last two years or so is about is inflation structurally higher and what does transitory mean?

Well, it turns out that less than two years is what "transitory" means if this data is correct. Again, things can change in views will change as the data and fundamental forces change. But for now, we see inflation falling very, very rapidly, again, ending this year below three. What I would highlight, and I think this is a really important nuance, is inflation for the last decade was one and a half. We now think it's falling, at least for the next year or two, to more like two and a half. Doesn't sound super high. But two and a half is 60%, higher than the average level of inflation that we had for the prior decade. So it actually is a meaningful shift, even if it's not above the central bank target range of two to three. What I would also say is, we have seen this movie before: the discussion around inflation persistence, and the risk of higher inflation for longer is a valid discussion at the very least, again, the the data doesn't seem to be pointing that way. But when we look back at the last global pandemic, this is the Spanish flu in 1918, we saw a really similar pattern. We saw inflation spike as the as the pandemic ended, and then inflation collapse really, really rapidly. It wasn't persistent then, in my view, [and] in the view of a number of investors at Wellington, and it might not be persistent now, either. And then a non-consensus view. And this is a 10-year,15-year, 20-year view, this is not now this year [or the] next few years. But what this looks at is the relationship between ageing populations' demographics broadly and the inflation rate. Now, the chart on the right-hand side, that long-term decline in population growth rates, that arrow, that where we are. We're mid-trend in slowing global population growth rates. The chart on the left shows the relationship between population growth rate dynamics and inflation. What this data suggests is [that] on a long horizon, the inflation risk that we face today is deflation, not persistently high inflation. But again, here, it's really important to understand the time horizon that we're talking about. This is a 10-to-20-year time horizon, not the few years that Nick was talking about in the first session today.

This will surprise the people in the room who know me well, talking about fixed income, certainly talking about it positively. It's probably a first for me. So nevertheless, bonds are actually super interesting today. Ross and the previous session, they were touching on this, but I completely agree. One of the changes in trend that we're seeing has to do with the level of interest rates in the global economy. We've been through a period over the last decade or so that was essentially an unprecedented experiment in global economics. We had the lowest level of interest rates that we have seen in 3000 years of data on interest rates, with the QE policies that we had. That's now come to an end, although Iran did show some interesting charts in the last session about what's happening with the BOJ and yield-curve control. We can talk more about that if that's helpful. But broadly speaking, in most regular economies, rates are high, and they're not going back down to 0%.

In our view, this is a different regime to the last decade. The result of that is that bonds are really attractive again, yields are very, very interesting today, particularly in credit markets. Now, I'll also mention here, think back to that expected return for US equities, 5% per year. You can buy a range of different credit instruments with yields of between five and 7%. And on average bonds have about a third of the risk of equities. So, on a risk-adjusted basis, these are actually really, really interesting investments today. And in particular, Asia credit is the gem in that asset class. A 7% expected yield with a 4% duration. That trade-off is better than any other place in investment grade credit, in USD terms, in any region around the world. So super bullish [on] Asia credit.

And as Emily introduced, and you heard from our PM in the last session, we've built a capability in that space in the last few years at Wellington. It's a great area. I'm running out of time rapidly. So, I'll be quick on this one. But the energy transition is a fascinating thing. And it has long-term implications for investments but also inflation. So EVs electric vehicles are rapidly gaining market share. That market share has doubled globally in the last two years. Renewable power generation is rapidly gaining market share. It's doubled in the last decade. Hand in hand with that. reliance on fossil fuels is also dramatically lower. I thought this was interesting. The UK today uses 63% less fossil fuels than it did 10 years ago. That's a massive change. What is growing to replace fossil fuels? Well, in particular, it's solar. That's the yellow section of this page. Solar capacity is leading the charge. Excellent pump, by the way. The interesting thing about solar power and renewables in general, is they're technology-driven sectors. What that means is as the technology improves, and this is that innovation argument that Daire was talking about, the costs get lower. So the cost of solar power generation has fallen dramatically over time. And indeed, today, in nearly every country around the world apart from places where it's always cloudy, it is cheaper to generate power through solar energy than it is through fossil fuels. Renewables are the future. And it's not just solar that's getting cheaper. It's essentially every new renewable technology because they're all driven by this innovation trend. This is just one year of data between 2019 and 2020.

But grid-scale solar, the cost of generating that power fell by 16% in that one-year period. Now ultimately what that means is power generation over time will get cheaper and cheaper as we transition away from fossil fuels. That's deflationary rather than inflationary, but again on a long-term horizon. Another interesting thing, when you use more renewables to generate power, you need more batteries to store that power. So, battery demand growing rapidly [on the] chart on the left. [On the] chart on the right, [there is] massive opportunity in Asia. All 10 of the 10-largest battery makers and their more than 90% of market share are based in Asia. It's one of the reasons to be bullish on Asia. Niraj mentioned the other reason, which is historically, Asia has been an importer of fossil fuels. Going forward, we will be an exporter of energy and energy technology to the rest of the world. And related to that, and while China won't be a driver of higher commodity prices, the new energy transition is very likely to be. We see really interesting long-term opportunities in industrial metals. So that kind of rounds out my time.

For your very interesting chat, very interesting presentation. We have unfortunately come up on time. So, you've covered quite a lot, so maybe just one quick takeaway audience.

So, I mean, there's a few that I would love to mention. But Asia, Asia is the main one. So, I’ve mentioned that we think there's a leadership transition underway from US outperformance to other market outperformance. Asia is leading the charge there. So bullish [on] Asia would be the one.