FLEISHMANHILLARD

The Future of Asset Management

in China 2023

EXECUTIVE SUMMARY

Welcome to the fifth edition of The Future of Asset Management in China white paper.

Despite prolonged restrictions due to the Covid-19 pandemic, mainland China reported 3% GDP growth in 2022. Although its economy may still face challenges due to heightened volatility in the global capital markets, it is generally believed that the most difficult phase is behind us now that the Covid restrictions have come to an end.

Since the reopening of mainland China at the start of the year, clear signs of stabilization have become evident with a solid rebound in economic and social indicators, including strong GDP growth in the first quarter of 2023 – mainland Chinese economy advanced 4.5% year-on-year in the first quarter, up from 2.9% growth in the final quarter of 2022 and topping market estimates of 4%. We have already seen a growing number of asset management firms expanding into mainland China and applying for Fund Management Company (FMC) licenses there or obtaining full control of their mutual fund joint ventures over the past few months.

Despite the positive sentiment, 52% of mainland China respondents cited inflation or stagnation as the number one risk over the next 12 months, with 29% of mainland Chinese investors moving investments into lower risk options, while just a quarter retain the same risk threshold.

Similar to last year, our report shows that asset managers must continue to up their game strengthening both performance (92%) and credibility (89%), the two continue to be important factors when investors choose asset managers. To the question of why mainland Chinese investors select overseas asset managers, it comes down to trust (55%) and their better track record (51%), the two most important reasons this year, compared to better performance (62%) and trust (51%) last year. Noteworthy too from this year's survey is that international firms' ability to offer unique investment strategies that cannot be found with local asset managers (48%) is the third most important reason to select an overseas fund manager.

Looking ahead, asset managers will see the global ESG and sustainability reporting and disclosure standards launched later this year with a view to implementation at the start of 2024. The objective is to harmonize global sustainability and climate disclosure standards, so that they are understandable and enforceable, and bring transparency, accountability and efficiency to the markets.[1] In mainland China, 90% of respondents clearly state that they view a strong ESG product offering as one of the most important qualities for an asset manager.

We hope you find this report insightful and that it helps you to navigate the complexities of asset management industry in mainland China.

Best,

Patrick Yu

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Asia Pacific Lead,
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ASSET MANAGEMENT LANDSCAPE
IN MAINLAND CHINA

MAINLAND CHINA

Market continues to open up with more products, WFOEs and ESG after tough 2022

As Asia's asset management industry haemorrhaged funds through much of last year, it was the mainland China market more than any other that offered a torniquet to stifle the outflows. Yes, it was a horrible year for mainland fund managers, but not as bad as elsewhere.

Mainland China was one of the few markets to achieve net inflows, a reflection of its solidity and resilience that hold it in good stead looking forward. Not only that, the entry of global fund managers as wholly foreign-owned enterprises (WFOEs) to China's domestic mutual fund market shows that Beijing remains committed to opening-up.

Net inflows into mutual fund assets in mainland China plunged amid the country's strict Covid policy, falling exports, a weak property sector and, more broadly, slowing economic growth. Alongside that, trade and geo-political issues undoubtedly raised risk premiums, spooking investors looking to invest in mainland China.

According to Morningstar, assets under management (AUM) of 10,263 China-domiciled mutual funds managed by 154 fund houses fell 6.98% to $2.06 trillion (CNY 14.23 trillion) in September 2022 from $2.29 trillion (CNY 15.83 trillion) a year earlier.[2] Net inflows into the mutual fund market in the first nine months of 2022 were $174.32 billion (CNY 1.21 trillion), down 50.2% from $350.39 billion (CNY 2.11 trillion) in all of 2021.

In January 2023, AUM in mainland China's mutual fund industry stood at $3.95 trillion (CNY 27.3 trillion), up from $3.75 trillion (CNY 25.9 trillion) a year earlier and from $2.00 trillion (CNY 13.8 trillion) in January 2019, just before the pandemic.[3]

China-domiciled funds saw the biggest outflows. Shanghai-Hong Kong-Shenzhen flexible allocation funds stood out as the worst performing type of fund in the first nine months of 2022, with net outflows of $17.25 billion (CNY 119.25 billion).[4] These funds specialize in investing in assets across the three cities.

At the other end of the scale, money market funds performed best with net inflows of $87.75 billion (CNY 606.63 billion), followed by short-term bond funds and pure bond funds with net inflows of respectively $41.21 billion (CNY 284.89 billion) and $17.27 billion (CNY 122.50 billion).[5]

In the year through to the end of November, the economic and market uncertainties saw a reduction in the number of funds launched in China's primary mutual fund market. During the period, there were 741 new fund launches, down from 961 during the same period of 2021. Funds raised dropped sharply by 58.4% to $96.19 billion (CNY 670.2 billion) from $230 billion (CNY 1.61 trillion).

Beijing finally ended its zero-Covid policy in early December last year and mainland China began to reopen, giving an economic lift regionwide. The circumstances of 2022 saw China record its lowest gross domestic product growth in decades. Its GDP growth for the year was 3%. However, it recorded higher than expected GDP growth in the first quarter of 2023 of 4.5% year-on-year. The growth target for the year is 5%. The rebound in mainland China's property sector in early 2023 has also given the market a boost.

While the market looks set for recovery, thanks to structural dynamics that are built-in, such as pent-up wealth accumulation, other factors behind the general market tumult remain. The war in Ukraine, tensions over Taiwan and other geopolitical actions directly affect Chinese companies and, more recently, are having an impact on US and other global companies operating in mainland China.

China issues more FMC licenses, and more overseas firms taking full control of the JVs

Effective April 1, 2020, the Chinese government scrapped foreign ownership caps in the mutual fund sector under a China-US trade deal. Since then, there has been a gradual entry of global mutual funds into the mainland China market. The speed of entry was affected by Covid.

As of the end of March 2023, five financial institutions had secured Chinese regulatory approval to establish WFOE retail fund units to conduct business in the mainland China's mutual fund industry. The China Securities Regulatory Commission (CSRC) granted licenses to enable them to offer onshore investment products and solutions to retail clients and asset management services to institutional clients in mainland China.

In addition, three financial institutions received the regulatory go-ahead to take full control of their Chinese mutual fund ventures. From getting a regulatory nod to getting a business license can take some time.

Several other global asset managers are also preparing for onshore retail mutual fund businesses in mainland China, with more license approvals in the pipeline this year.

WFOE private fund manager QDLP launches

In March 2023, mainland China saw the launch of its first Qualified Domestic Limited Partner (QDLP) fund managed by a WFOE private fund manager (PFM). This is a significant development because it means that foreign fund managers can now choose where to invest globally with the funds raised in mainland China.[6]

The QDLP program was developed to allow fund managers to invest overseas with money raised locally in the mainland. It is a quota-based program, whereby the amount each QDLP is allowed to make in outbound investments is capped by a quota approved by the State Administration for Foreign Exchange (SAFE).

Launched in 2016, the WFOE PFM is a program that was initially designed to allow foreign fund managers to raise funds and invest domestically in mainland China. By linking WFOE PFMs with QDLP, foreign fund managers will be able to optimize the capital structure, as well as human, market and other resources for their business in mainland China and around the world.

Private pensions take off

Arguably the most significant development for the asset management sector in mainland China last year was the launch of mainland China's third pillar in its pension system.

The country is like just about everywhere else in the world in having a pension readiness problem – peoples' pensions are not large enough to cover their retirement. Mainland China's pensions have traditionally been offered through a Pillar I social scheme with the option for Pillar II employer-sponsored supplemental plans.

In November last year, mainland China launched a pilot for Pillar III, a voluntary tax-favoured private pension scheme under the third pillar of the country's pension system – essentially an individual retirement account (IRA). The move is the most important development in years and the biggest change in the pension sector since the launch of the Public Pension Fund (PPF).

Mainland China's aging population and declining birth rate, low social pension benefits, and limited uptake of employer-sponsored plans have created a need for an official voluntary pension scheme that can utilize current individual savings in a regulated, sustainable and tax-efficient manner to help individuals save for retirement.

This new development is expected to help the private pension industry grow from its current $300 billion (CNY 2.07 trillion) value to at least $1.7 trillion (CNY 11.75 trillion) by the year 2025.[7]

The pilot has been launched in 36 cities,[8] including all the tier 1 and tier 2 cities, and will run for a year before being expanded to more parts of the country – no timeline or date has been set for this expansion. The private pension plan is open to all Chinese citizens and resident workers who currently contribute to the basic pension insurance for urban employees or the basic pension insurance for urban and rural residents.

Individuals are limited to one pension account each and are allowed to make voluntary contributions of up to $1,736 (CNY 12,000) per year into their individual pension accounts and enjoy tax relief. They can withdraw their pension benefits when they reach the retirement age or in the event of disability, death, or permanent immigration abroad.

Between 25 November when the pilot started and the end of 2022, the trial drew 19.52 million participants, of whom 6.13 million have made their first contribution to their IRA.[9] That figure rose to 28 million by the end of March 2023, according to Bloomberg.

The new system encourages more than one billion people in mainland China to start their individual pension saving, in turn creating opportunities for various types of service provider. The latter include fund managers and banks, but more will follow with red-hot competition likely. It is time to sit tight for a likely surge in consumer demand.

REITs on the rise

In the midst of the Covid lockdown, in June 2021, nine of mainland China's real estate investment trusts (C-REITs) made their public debut on the Shanghai and Shenzhen bourses, with an aggregate value of $4.52 trillion (CNY 31.2 trillion). They were the first such C-REITs and held infrastructure assets from toll roads and waste treatment plants to logistics and industrial parks.

Since then, through 2022, the C-REIT market has grown dramatically, raising capital totalling more than $10.86 billion (CNY 75 billion), with the listing of 24 infrastructure and rental housing REITs as of December 2022. Asset classes covered by C-REITs expanded last year to include affordable rental housing with three public rental housing REITs that raised a total of $0.55 billion (CNY 3.8 billion).[10] Regulators are looking to further broaden the scope of REITs include consumer-linked infrastructure projects to drive investment. Such projects would include department stores, shopping malls and farmers' markets.

Overall, C-REITs have seen spectacular growth over the last 18 months and, given the vast about of infrastructure and resources in mainland China, the potential for further growth is huge.

In early 2023, mainland chinese officials called on domestic asset managers to more than double initial assets raised for REITs in 2023, while also diversifying their underlying assets to include more technology-themed investments. Mainland China's state planning agency is targeting $28.96 billion (CNY 200 billion) in initial fundraising for a total of 60 REITs by the end of this year, up from the current amount raised of $13.16 billion (CNY 91 billion) since June 2021.

Reforms set for wealth connect and HK-China MRF

Further reforms are in the pipeline for the expansion of the Greater Bay Area Wealth Management Connect (WMC) and the Mutual Recognition of Funds (MRF) schemes after proposals put forward by Hong Kong's Securities and Futures Commission (SFC) were well received by mainland China regulators. The reforms are likely to take place by mid-year.

The mainland China seeks to leverage Hong Kong's position as an international financial center to attract more foreign investors from Europe and the US, using the various connect schemes between Hong Kong and mainland China.

Thus far, both schemes have underwhelmed fund managers who have been unable to take advantage of the WMC and MRF schemes due to the limited scope and strict requirements of the products involved. However, the new reforms seek to address these issues and will likely expand the range of eligible products, relax investment promotion restrictions, and allow more financial institutions to participate.

The Greater Bay Area WMC cross-border investment scheme allows eligible financial products, including locally domiciled mutual funds, to be distributed between Guangdong province, Hong Kong and Macau. It was launched during the Covid pandemic in October 2021.

Currently, regulatory and policy barriers in mainland China prevent Hong Kong banks and fund managers from providing cross-border advisory services. Fund managers also complain that the existing scheme only allows the sale of rather unexciting low and medium-risk products to mainland Chinese investors, who are more attracted to higher risk products with higher returns.

Meanwhile, the Hong Kong-Mainland MRF scheme, which was launched in 2015 to facilitate cross-border fund sales, is set for change. The MRF scheme has been criticized for its restrictions on inflows from mainland investors, and the requirement for fund products to be domiciled in Hong Kong.

The MRF scheme requires that a Hong Kong-domiciled fund seeking approval for sale in mainland China must ensure its fund manager holds a Hong Kong asset management licence and does not delegate the fund's investment functions to overseas managers. The objective was to encourage global fund houses to expand their local teams and operations, and to foster Hong Kong's growth as an investment management hub. But the SFC has acknowledged that this is inefficient, so it will likely be changed.

Another irksome MRF regulation is the one that the size of assets raised for any fund in the mainland cannot surpass 50% of the fund's total assets.

By the end of 2022, a total of 84 funds had been sold northbound and southbound under the MRF scheme, with a total net subscription of $1.82 billion (CNY 12.56 billion). Hong Kong-domiciled funds sold to mainland Chinese investors via the MRF scheme recorded a 19.3% year-on-year drop in cumulative net subscriptions, to $1.67 billion (CNY 11.54 billion) by end-2022 from $2.07 billion (CNY 14.3 billion) at the end of 2021.

ESG compliance lags, while Chinese demand for ESG products booms

Mainland China's performance on ESG-compliant investing during the past year is a mixed bag. On ESG ratings, its companies rank lower not only than overseas nations, but also most emerging markets. A combination of censorship, surveillance, environmental and labor issues undermine its efforts to follow ESG principles. In particular, the semi-conductor sector has been targeted for US national security reasons.

Sustainalytics, the sustainable rating agency owned by Morningstar, in October downgraded three leading Chinese tech companies on its watchlist to the category of "non-compliant with UN principles". [11]

A recent report from World Wide Fund for Nature noted that Chinese asset managers need to invest more attention in setting higher standards. The report showed that during the past year, among Chinese asset managers, there was a decline in the relevance of sustainability in the organization's strategy and investment beliefs, a sharp decline in active ownership and a reduction in disclosures.[12]

On a more positive note, the recently established ESG Committee of the China Association for Public Companies (CAPCO) has said China needs to build an ESG management and evaluation system "with Chinese characteristics and international recognition", which shows a desire to accelerate ESG development in China in such a way that it works within the international framework. The new global ESG reporting and disclosure standards to be launched later this year will also help to improve performance in this area in mainland China.

Against a backdrop of the global rise of the anti-greenwashing movement in ESG investing, mainland Chinese regulators are prioritizing to clamp down on greenwashing. It means that asset managers will become increasingly rigorous in their product naming and marketing materials. As ESG investment grows, so the regulators will look more closely at this issue.

SURVEY FINDINGS

- TRUE Global Intelligence, the in-house research practice of FleishmanHillard, fielded an online survey among 250 investment, finance and banking professionals in mainland China during the period April 4-11, 2023.
- Now in its fifth year, the survey is conducted to explore what mainland China investors think about different investment products and themes. We also asked them about their experiences with overseas asset managers, their access to financial information and advice, and their use of digital platforms.
- Mainland Chinese respondents to the survey have traded or invested in at least one of the followings:

Equities funds	72%
Fixed income funds	70%
ETFs	53%
Alternatives	34%
Balanced funds	54%
PE funds	44%

- Mainland Chinese investors primarily traded/invested in equities funds (72%) and fixed income funds (70%), and are most interested in investing in the same types of funds over the next 12 months (65%, 56% respectively).
- Asset management house performance (92%) and size of asset management house (91%) are the most important attributes when selecting an asset manager.
- Almost three in four (73%) mainland Chinese investors have invested in funds run by overseas managers (+23 pps YoY), because global brands have more trust (55%) and a better track record (51%).
- Post-Covid, 29% of mainland Chinese investors are moving investments into lower risk assets, while a quarter retain the same risk threshold.
- Over half (52%) consider inflation/stagflation to be the biggest financial risk.
- The highest level of interest lies in AI funds (62%) and thematic funds (48%) for future investments.
- The AI sector (53%) and healthcare/biotech (48%) sector are of most interest for investment.
- Nearly two-thirds of mainland Chinese investors are interested in investing in the APAC region (64%), especifically in China A-shares (75%) and Hong Kong (58%).
- Fund house websites (46%) and social media (44%) are used most for information on funds/ investment products.
- On social media, Weibo has gained popularity (79% vs 63% a year earlier).
- More investors are using independent financial advisers (53% vs 40% a year earlier) and insurance agents/brokers (48% vs 29% a year earlier) for fund patronage this year.
- Digital platforms continue to be used (77%), particularly for instant analysis and advice on asset allocations.
- Over half of the investors (56%) have used ChatGPT/ AI tools and found it intuitive (91%) and useful (87%).
- Transparency in customer communication (90%) and strong ESG offering (90%) with clear goals and objectives (90%) continue to be an important part of the offering from overseas asset managers.

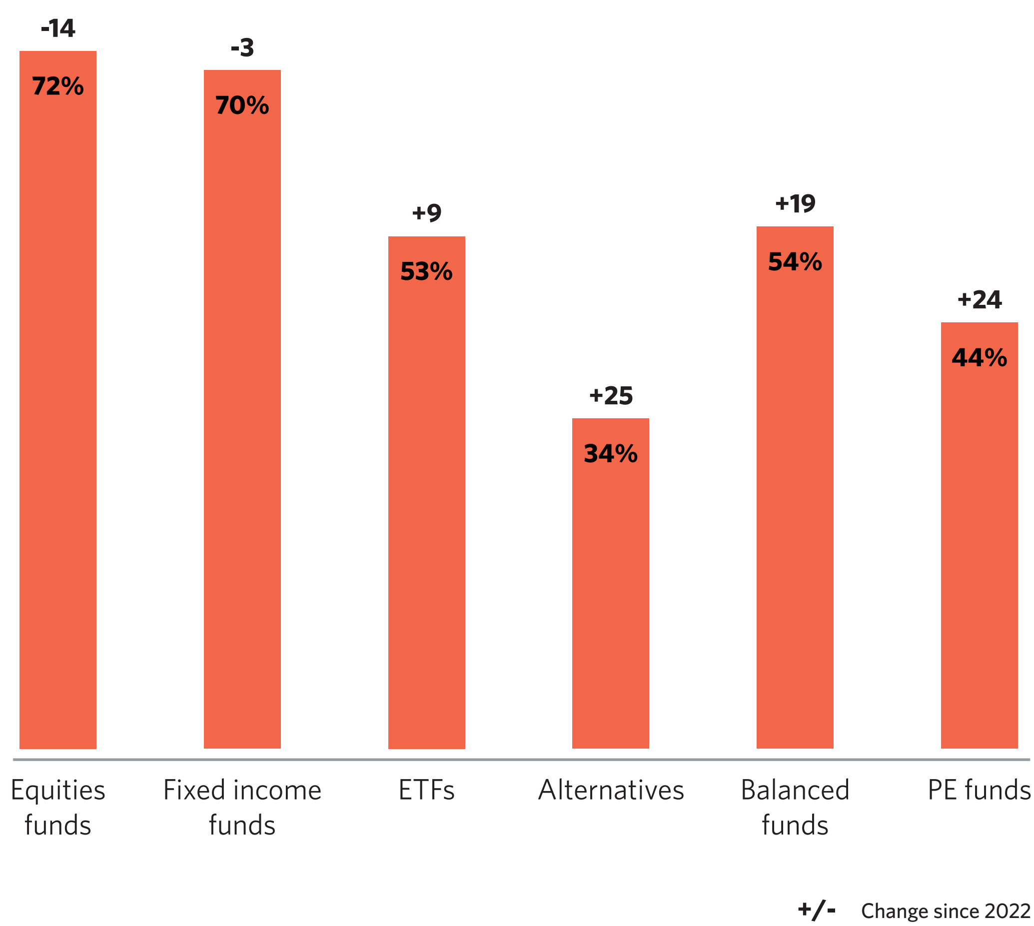
SURVEY RESULTS

Experience and outlook

Although equities funds (72%) and fixed income funds (70%) remain the top two most frequently traded/invested products for mainland China investors in 2022, in line with the trend across Asia, there was a growing interest among mainland Chinese investors for other investment products, especially balanced funds (up 19 pps to 54%), PE funds (up 24 pps to 44%) and alternatives (up 25 pps to 34%).

Noteworthy too is that ETFs saw strong growth in mainland China over the past year. ETFs provide investors with more diversified exposure in the Chinese equities market. More than half (53%) said they have invested in ETFs during the past year, up 9 pps from a year earlier. The momentum of ETFs in mainland China is expected to see sustained growth in 2023 as investors bet on a Chinese market revival.

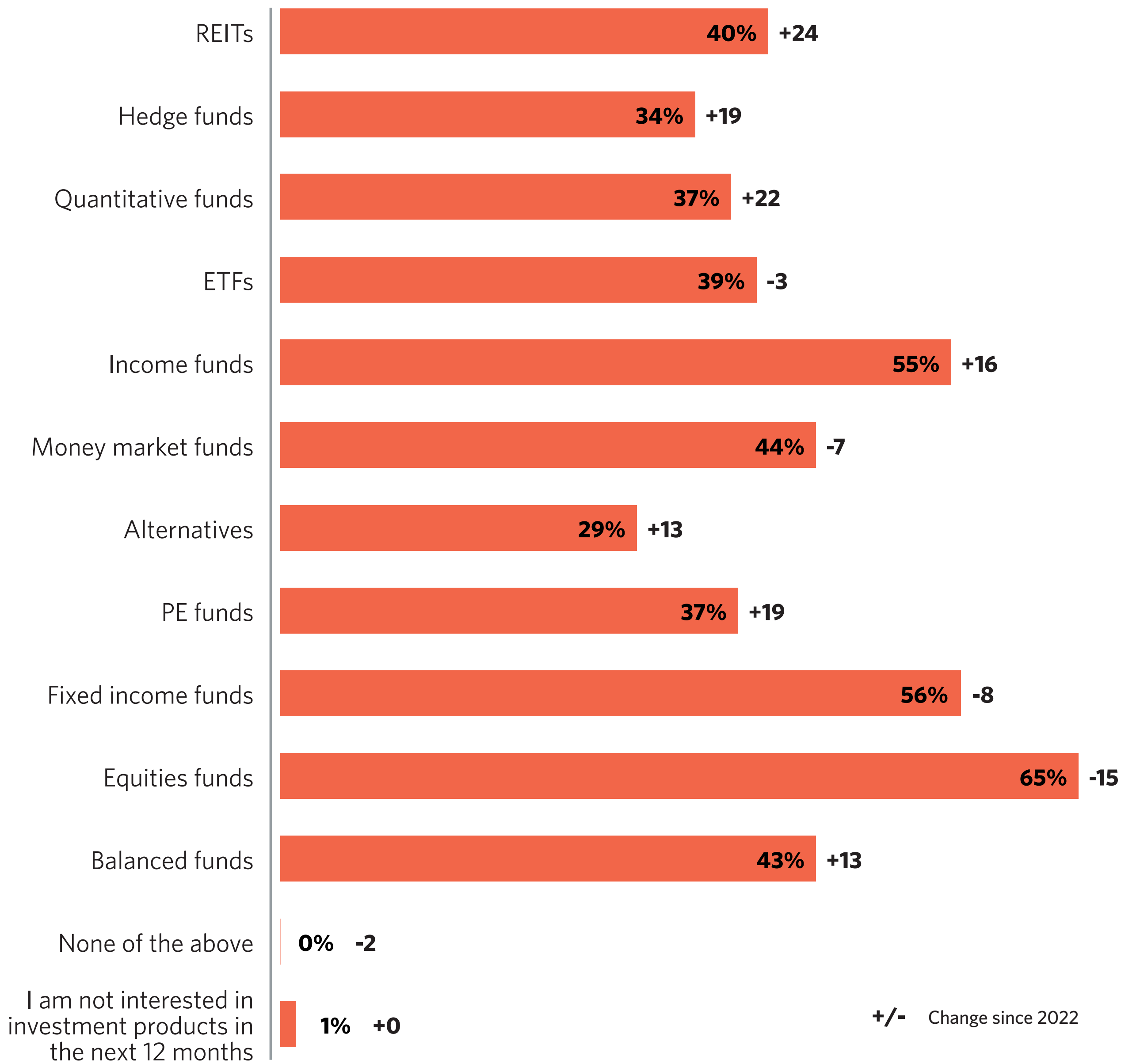
Please select the types of financial products which you have traded or invested in.



Moving to 2023, mainland Chinese investors continue to see equities funds (65%) and fixed income funds (56%) as the major investment products, but more than half of the respondents (55%) expressed interest in income funds in the next 12 months, up 16 pps from a year ago.

The C-REIT market continued to grow very rapidly following its debut in 2021, with mainland Chinese government continuing to expand the asset class by including affordable rental housing in August last year and adding shopping malls to its REIT pilot program in March this year. Investor interest in REITs has increased by 24 pps to 40% this year and it is believed that demand for REITs will continue to grow sharply.

What kind of investment products are you interested in the next 12 months?

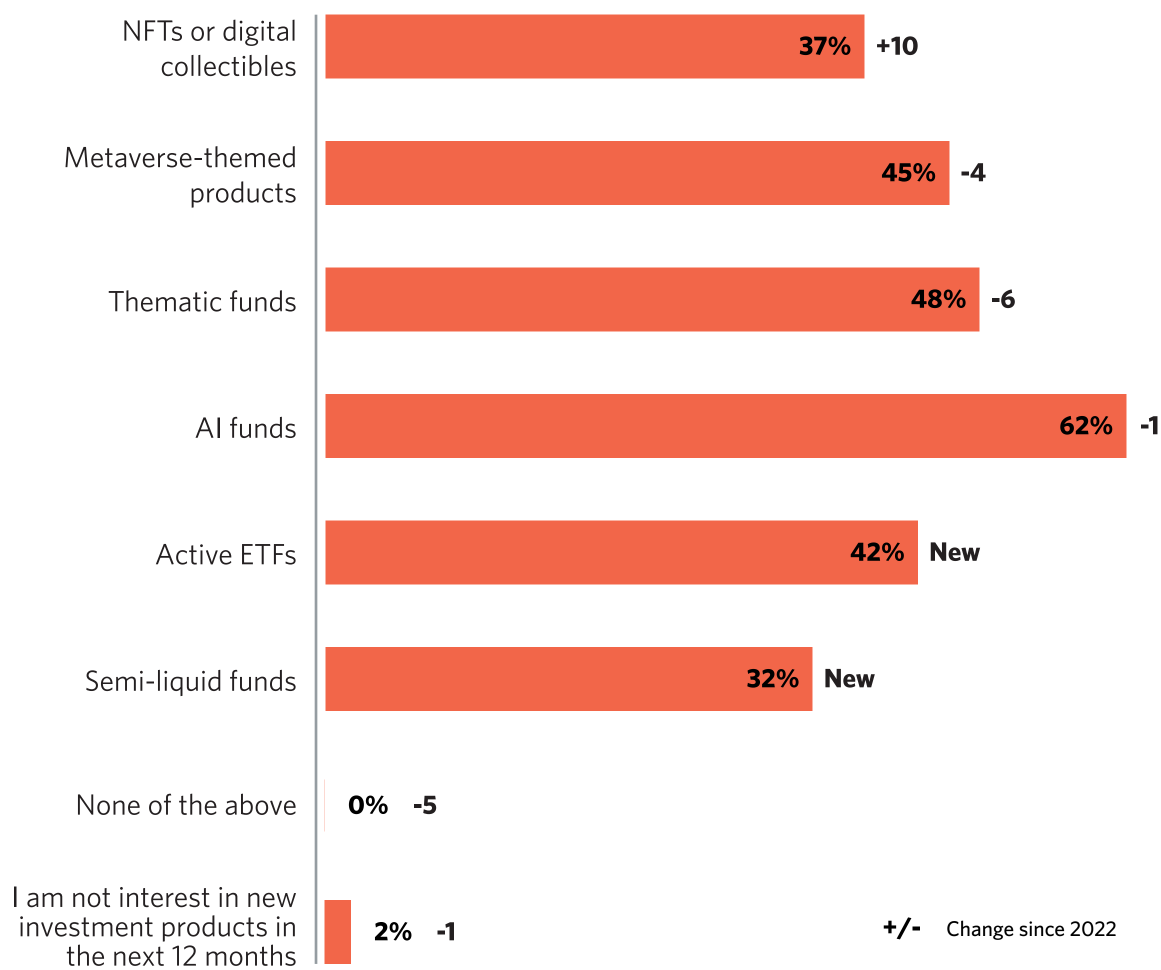


Upcoming investment themes and regions

Amid high adoption of AI in mainland China across different industries, AI funds continue to be of most interest among mainland Chinese investors, with 62% of respondents saying they are likely to invest in then during the next 12 months, followed by thematic funds (48%) and metaverse-themed products (45%). Only 2% of the respondents said they are not interested in such new investment-themed products.

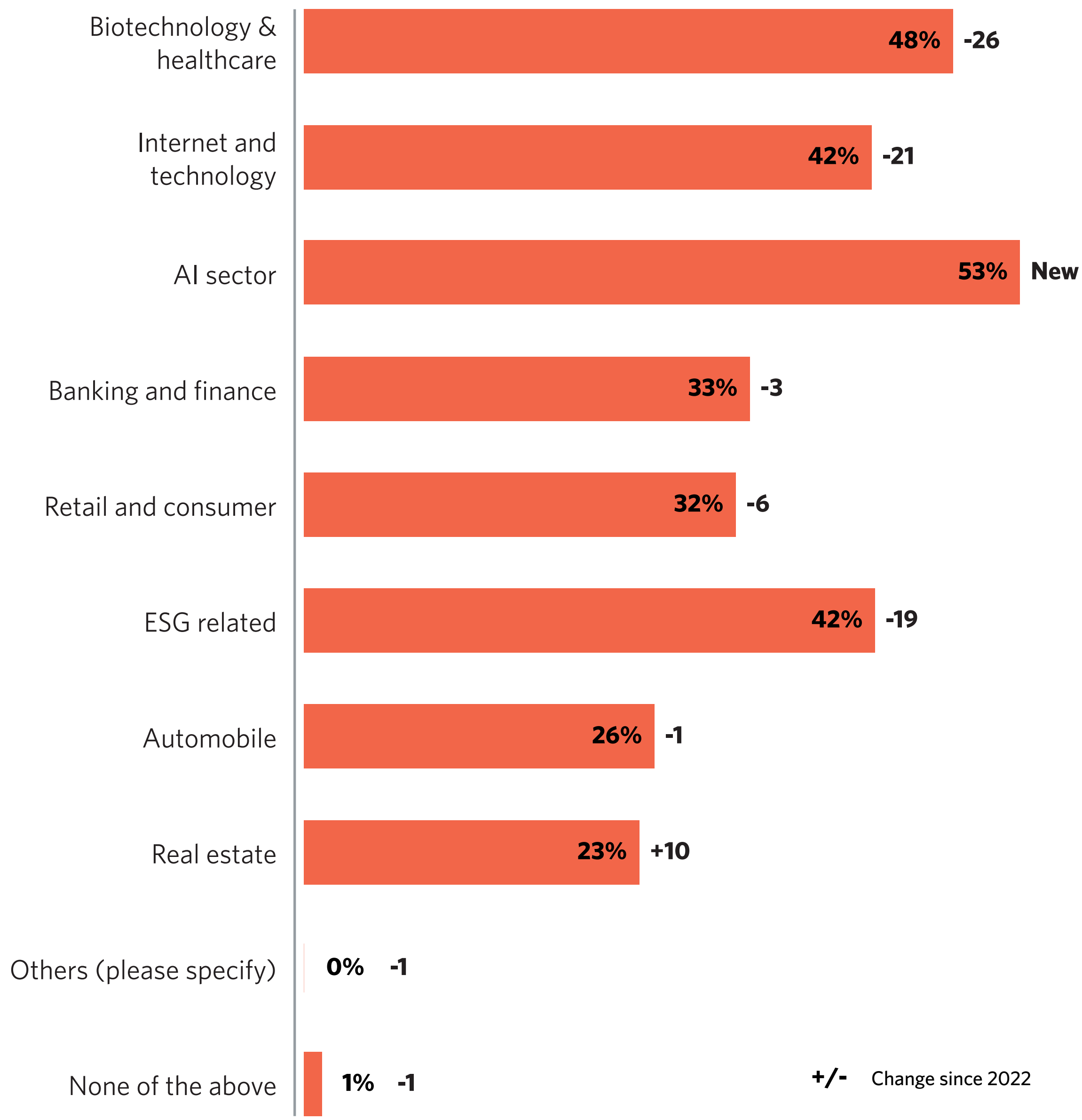
In addition, mainland Chinese investors have a growing interest in digital collectibles, up 10 pps to 37%, the highest among all the markets covered in the survey. Mainland Chinese investors are also interested in active ETFs (42%) and semi-liquid funds (32%) – broadly in line with the trend in Asia.

What kind of new investment-themed products are you interested in the next 12 months in the post-Covid era?



In terms of industry sectors to invest in, mainland Chinese investors show tremendous interest in the AI sector (53%), followed by biotechnology and healthcare (48%), all of which are consistent with the Asian market trend, once again demonstrating that the new economic sectors are highly sought-after by investors. It is interesting to see that the real estate sector, which had been falling out of favour in Hong Kong, Singapore and South Korea, saw growing interest among investors in mainland China, with 23% of them showing interest, up 10 pps as compared to a year earlier, which can be attributed to the signs of stabilization in the local property market backed by a supportive government policy.

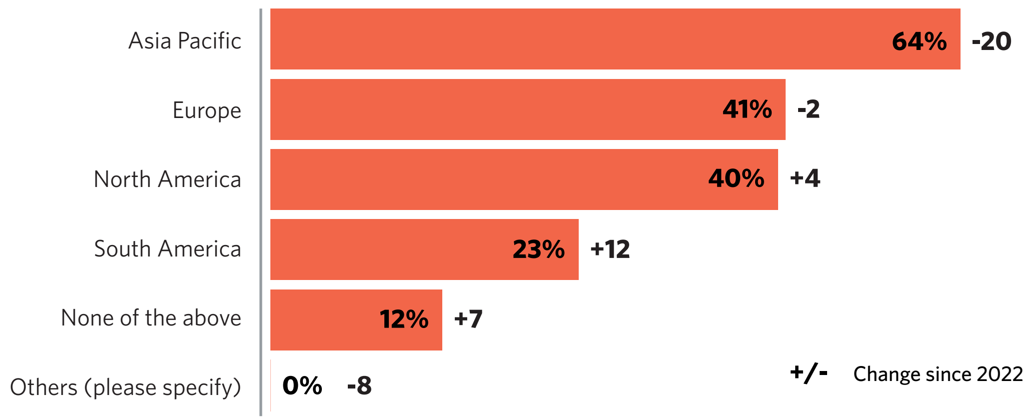
Which sectors are you most interested in investing in the next 12 months in the post-Covid era?



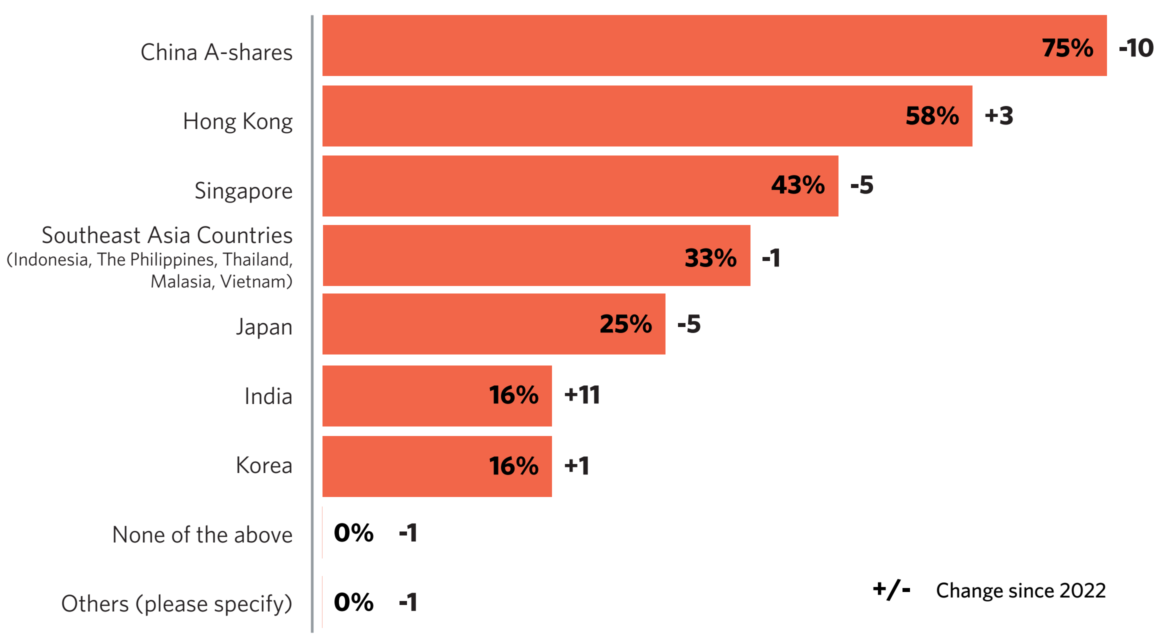
Mainland Chinese investors continue to show strong preference for investing in Asia Pacific (64%), followed by Europe (41%) and North America (40%). For those interested in Asia Pacific, the most important reason is exploring investment opportunities within their own country, which is likely due to the lifting of Covid restrictions, the government's supportive policies and incentives, as well as the gradual recovery of the economy.

Investors in mainland China showed a growing willingness to diversify their investments to South America. From a geopolitical-regulatory perspective, mainland Chinese investors might see South America as a friendly market due to the tightened investment screening of mainland Chinese investment in the US and the EU.

Which region(s) are you most interested in investing in the next 12 months in the post-Covid era?



Which countries / market(s) are you most interested in investing in the next 12 months in the post-Covid era?

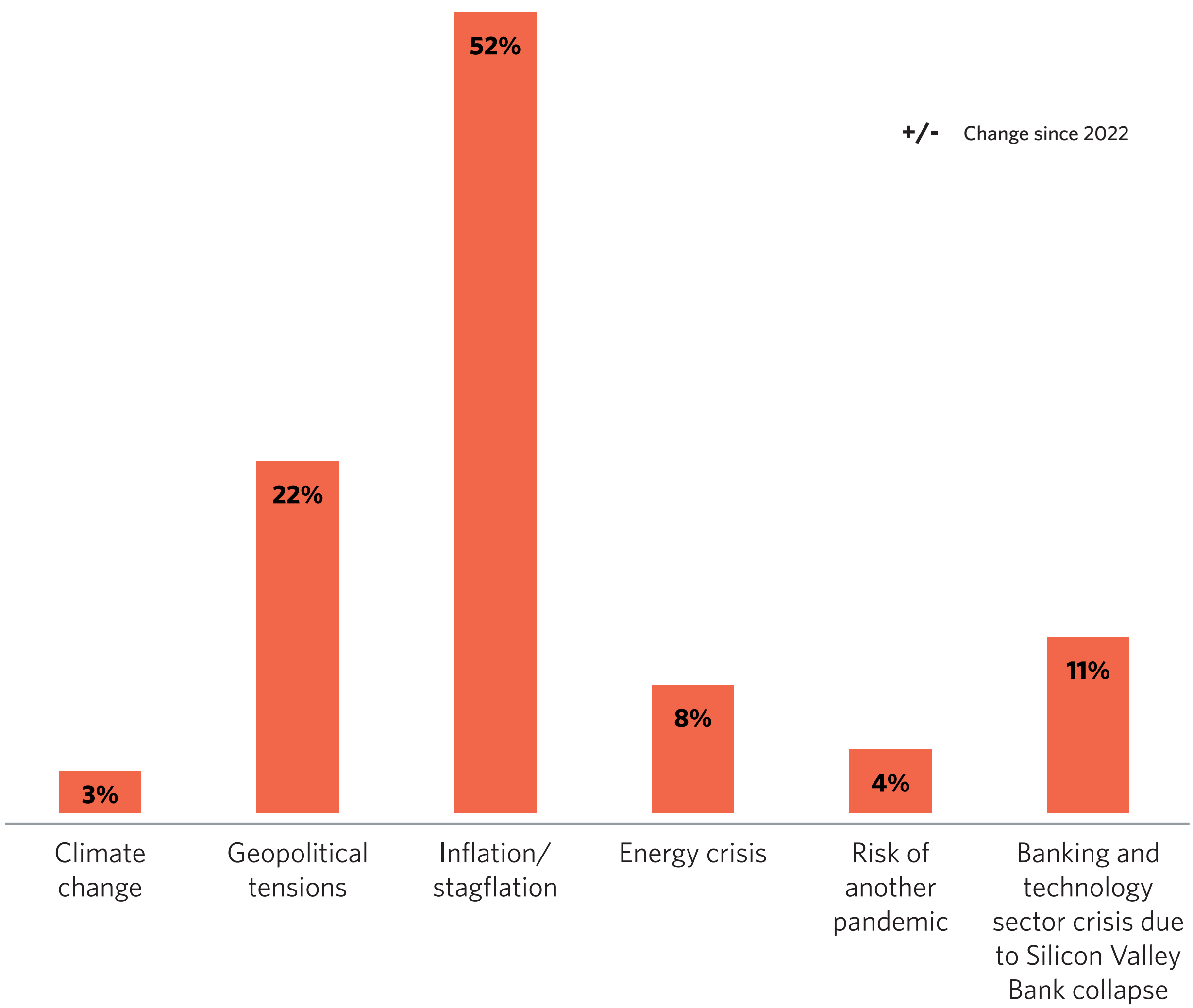


Upcoming risks

As with the other markets in APAC, inflation or stagflation is considered the biggest financial risk among mainland Chinese investors (52%), far higher than concerns over geopolitical tensions (22%).

Although Silicon Valley Bank (SVB) played a vital role in providing financial services to many innovative and high-growth companies in the technology sector, mainland Chinese investors are less concerned about the collapse of SVB (11%) and believe the region will likely face limited contagion risk. Compared with climate change (3%), mainland Chinese investors are more concerned about the energy crisis brought by the Russia-Ukraine war (8%) as well as the risk of another pandemic (4%).

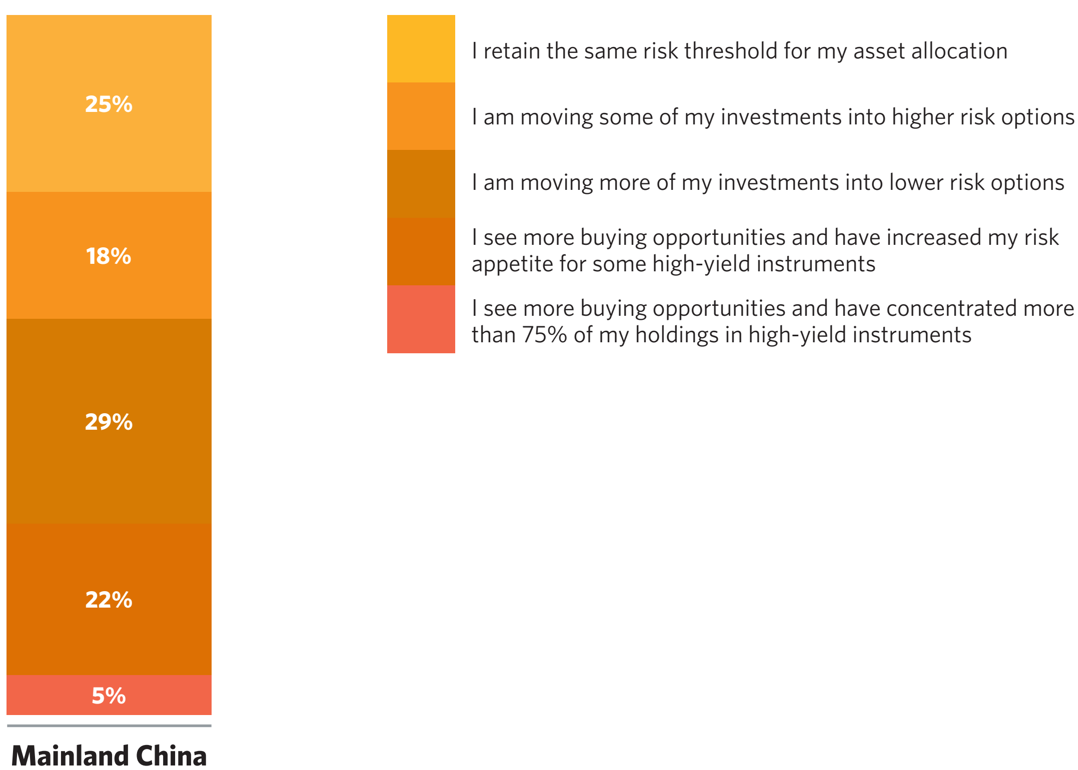
What do you view as the biggest financial risk for your portfolio right now?



Although business activities have gradually resumed in mainland China since the start of 2023, 29% of investors in mainland China said that they would shift their investments into lower risk asset classes, reflecting their desire to build a better, more resilient portfolio that may help them withstand future volatility and the broader vagaries of the market.

Nevertheless, the survey showed that 22% of mainland Chinese investors are risk-takers as they show greater appetite to seek out buying opportunities for high-yield instruments. A quarter of the respondents, however, said that they would maintain the same risk threshold for their asset allocation.

All markets have now re-opened and business activities resumed business post-Covid. How has this affected your investment outlook and risk appetite in terms of your asset allocation?

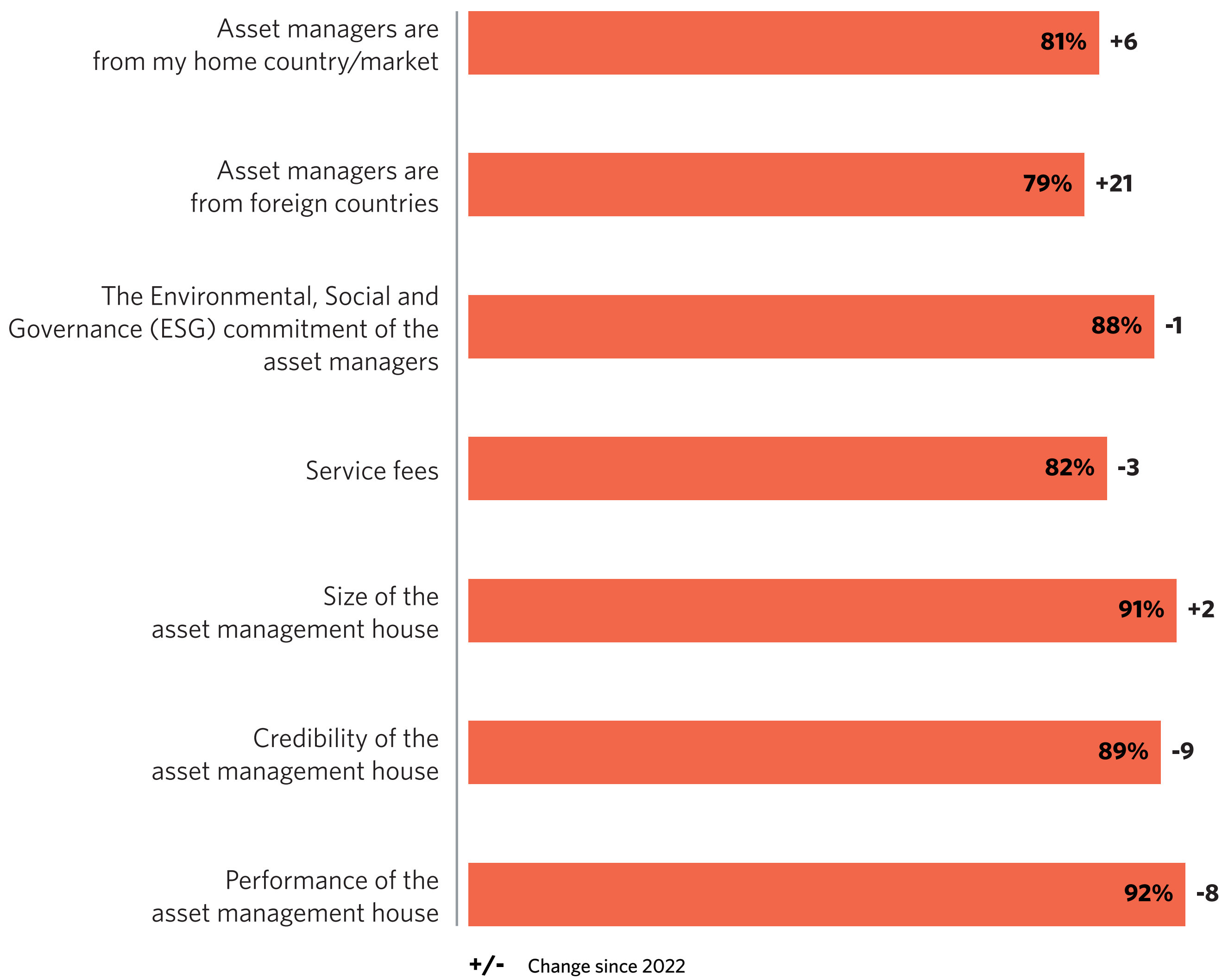


Thoughts on global asset managers

Performance (92%), size of the asset management house (91%) and credibility (89%) are the most important factors for mainland Chinese investors when choosing an asset manager.

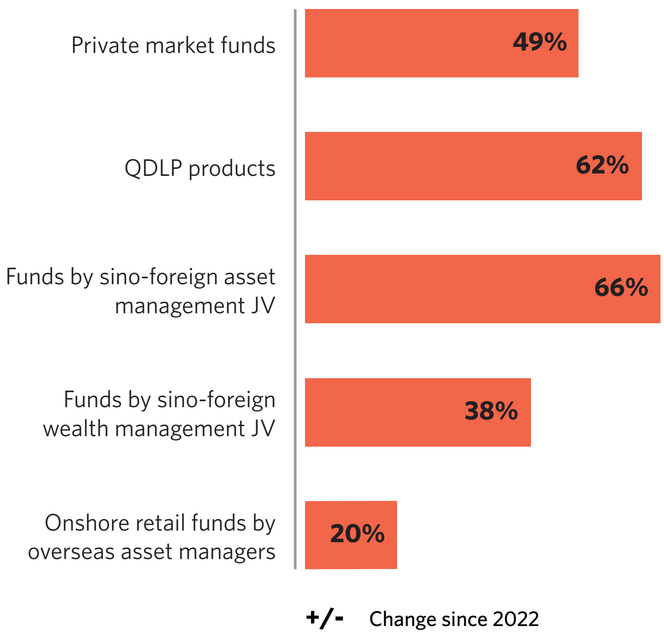
The ESG commitment of asset managers (88%) is also highly valued by mainland Chinese investors, demonstrating that business sustainability and social responsibility are gaining traction among corporates in the country and mainland Chinese investors are likely to choose like-minded asset managers to build long-term success together.

How important are each of the following when choosing an asset manager?



Interestingly, 73% of the mainland Chinese investors said that they have invested in local fund products run buy overseas asset managers, up 23 pps from a year earlier. Most of those who purchased products from overseas asset managers said they have more trust in global brands (55%), while 51% of them noted that these overseas asset managers have better track record. Nearly half (48%) said that overseas asset managers can offer unique investment strategies that they cannot find among purely local market players.

Types of funds invested



73% **(+23 pps)**

of Chinese investors have invested in local fund products run by overseas asset managers

Reasons to purchase from overseas asset managers

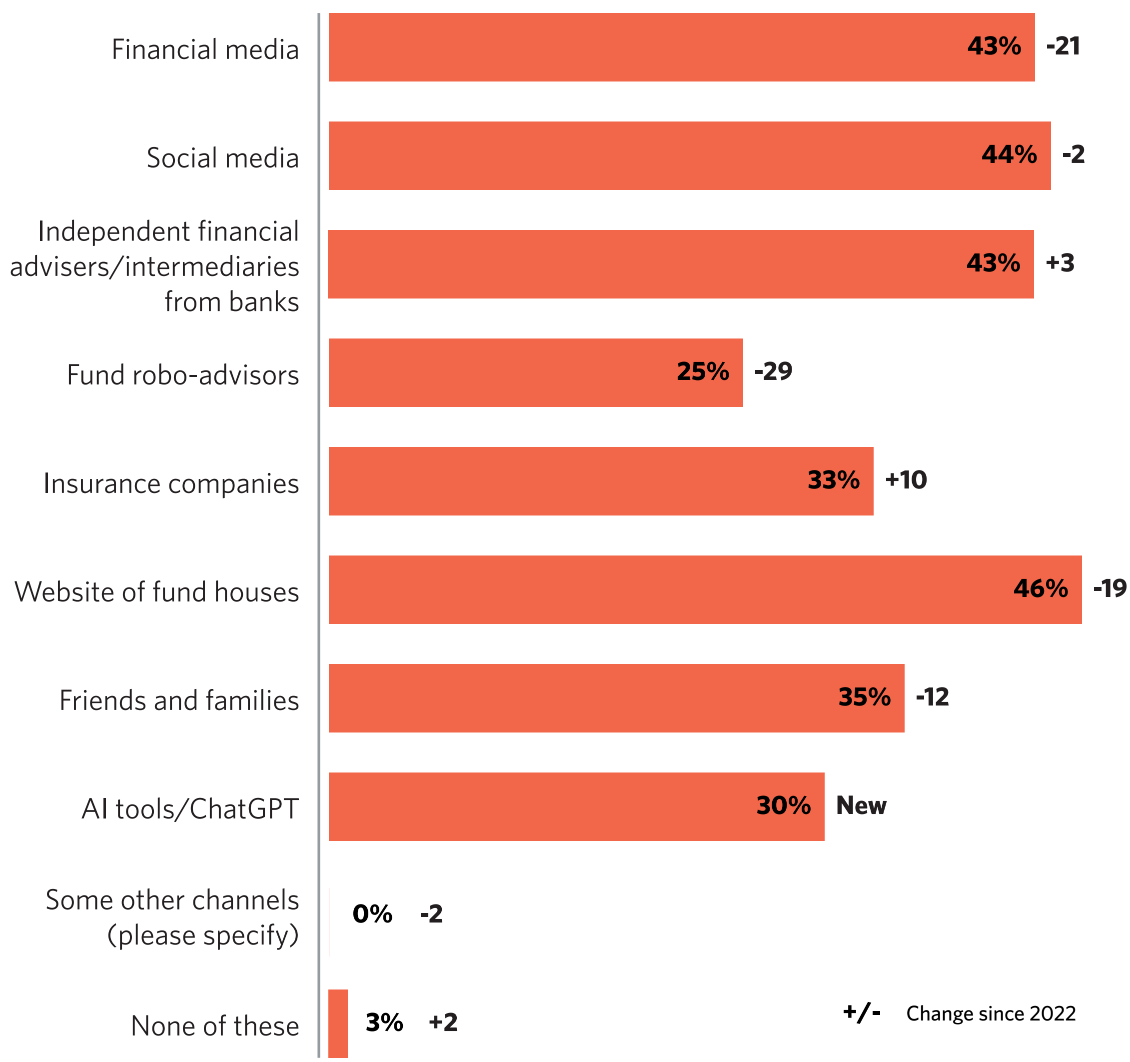
Information sources

Unlike other markets, mainland Chinese investors prefer to obtain product information directly from the fund houses' websites (46%), followed by social media platforms (44%). Compared to investors in other markets in Asia, who prefer receiving product information from financial media (Asia, 53%), only 43% of mainland Chinese investors prefer to get investment information from financial media.

While investors in Hong Kong, Singapore and South Korea rely less on independent financial advisers for product information, mainland Chinese are among the investors who still prefer to receive investment insights and guidance directly from financial advisers (43%, up 3 pps from last year).

It is also interesting to see that mainland Chinese investors show the highest level of acceptance to the usage of ChatGPT or equivalent AI tools as ways to access fund or investment product information as compared to their peers in Asia.

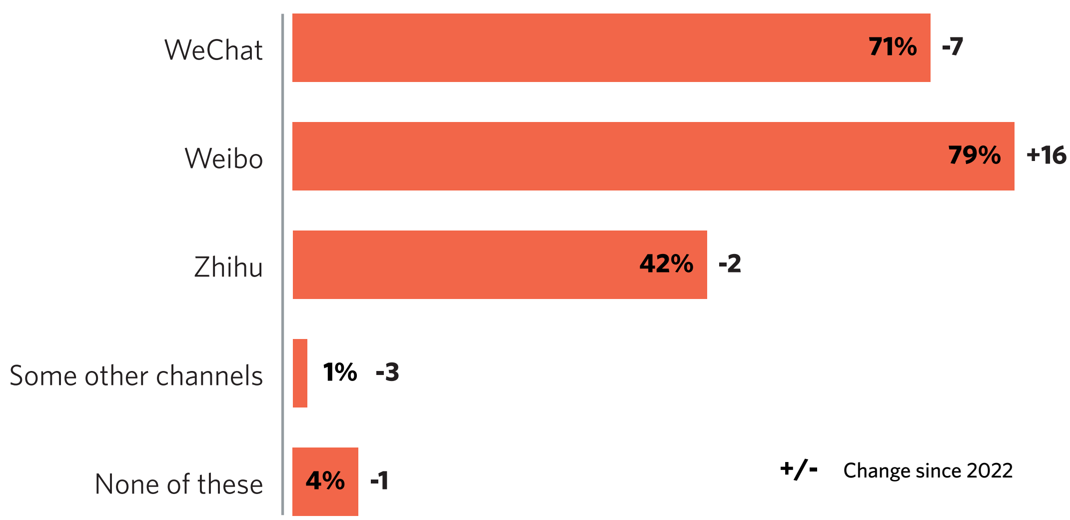
Through which of the following channels do you receive information on funds and investment products?



WeChat has always been described as China's "app for everything" with over 1 billion daily users exchanging news and information, as well as utilising messaging and other functions. It is surprisingly to learn in this year's survey that more mainland Chinese investors said that they use Weibo (79%) more frequently than WeChat (71%) to access fund information. Weibo usage grew 16 pps while that of WeChat dropped 7 pps.

As social media platforms play an important role in the daily lives of mainland Chinese citizens, global asset managers should continue to drive their communications through mainland social media platforms to build deeper engagement with their audiences.

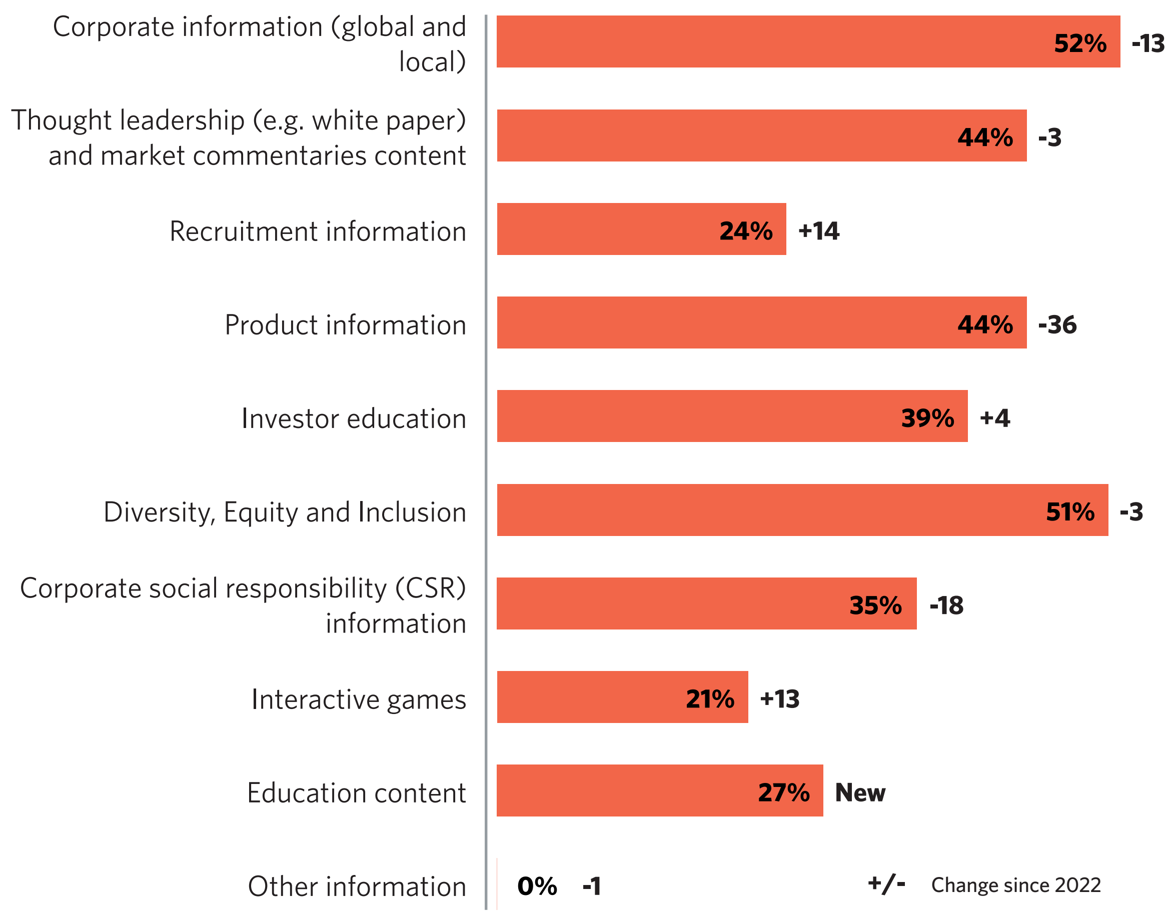
Through which social media platform(s) do you access fund information?



In mainland China, most investors are looking for corporate information (52%) in the social media channels of asset managers. Diversity, equity and inclusion (DE&I) is also increasingly important in mainland China with 51% of respondents saying that they search DE&I information frequently from social platforms (versus 37% in Asia).

Product information (44%), thought leadership (44%) and investor education information (39%) are equally important among mainland Chinese investors. Asset managers who are able to develop thought leadership or investment educational content can build a stronger brand affinity among the mainland Chinese investors.

What type of information do you typically look for from the social media channels of asset managers?

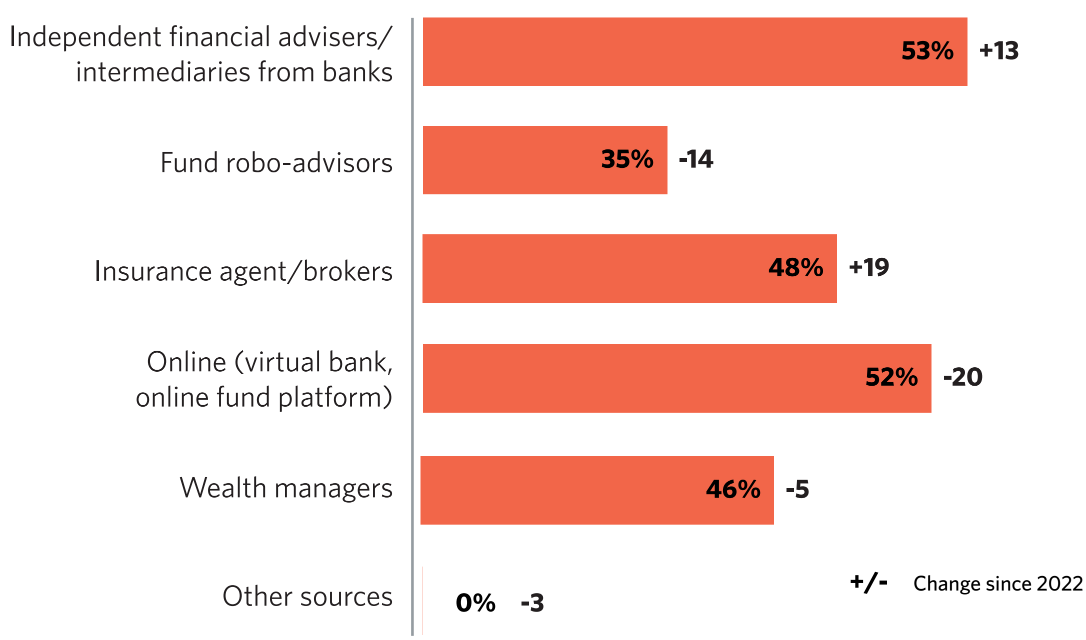


Fund patronage

In mainland China, more than half of investors (53%) prefer independent financial advisers/banks for fund patronage, up 13 pps from last year, making it the most important source for making fund-related investment decisions. Financial advisers/banks are followed by virtual banks or online fund platforms (52%, down 20 pps). Mainland Chinese investors who prefer insurance agents/brokers grew by 19 pps to 48%.

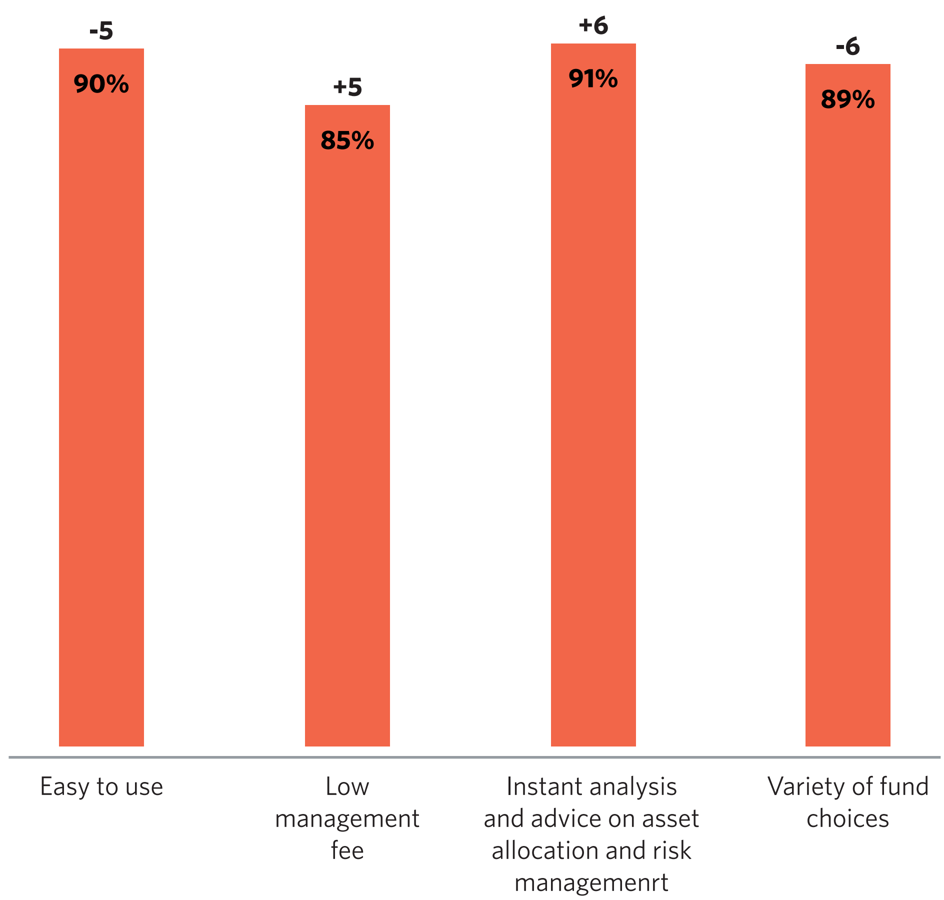
Mainland Chinese investors, however, are shifting away from fund robo-advisors (2023: 35% vs 2022: 49%) despite the growing popularity in Asia (Hong Kong and Singapore up 11 pps and 14 pps respectively).

Please select the sources you use for fund patronage.



More than three quarters (77%) of mainland Chinese investors said they have used digital platforms to purchase mutual funds, and used it for instant analysis and advice on asset allocation and risk management (91%). They also find digital platforms easy to use (90%) with a wide variety of fund choices (89%).

Describe your experience when you use digital platforms to purchase funds.

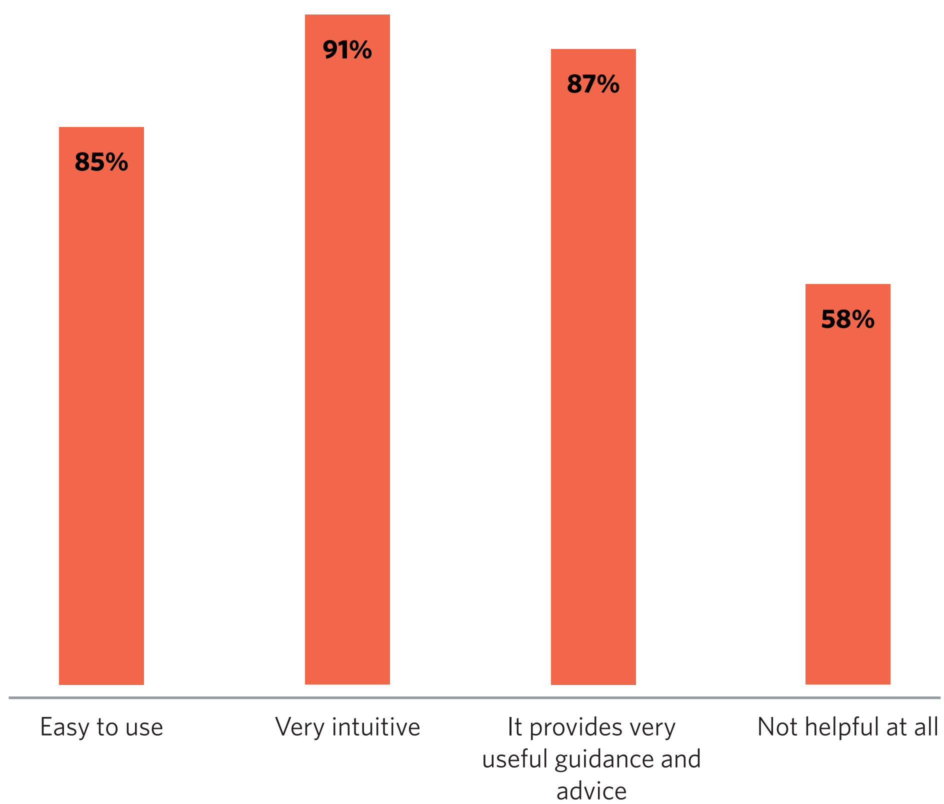


77% **(- 2 pps)** of investors have used digital platforms to purchase mutual funds

+/- Change since 2022

More than half of the mainland Chinese investors (56%) have used ChatGPT or other similar AI tools for making investment decisions, with 91% finding the AI tools very intuitive. Despite the entirely new experience, 58% of the respondents found that these tools are not helpful at all for investment decision-making, so it remains to be seen if ChatGPT or AI tools will replace human-led advisory in making investment decisions.

Describe your experience when you use ChatGPT or other AI tools in selecting fund managers or help you make investment decisions

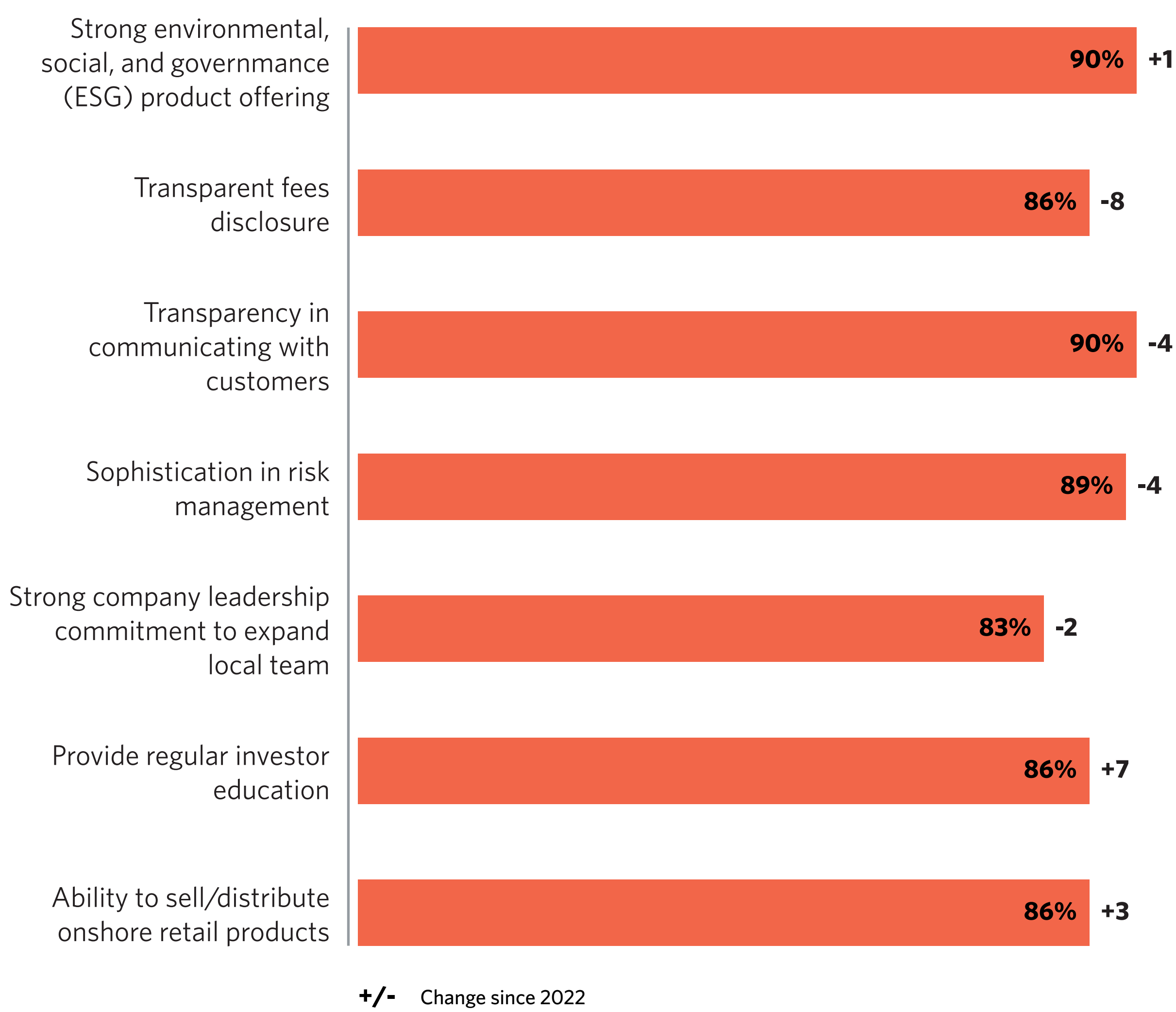


56% of investors have used ChatGPT or other AI tools to select fund managers or help make investment decisions

Appealing traits and ESG

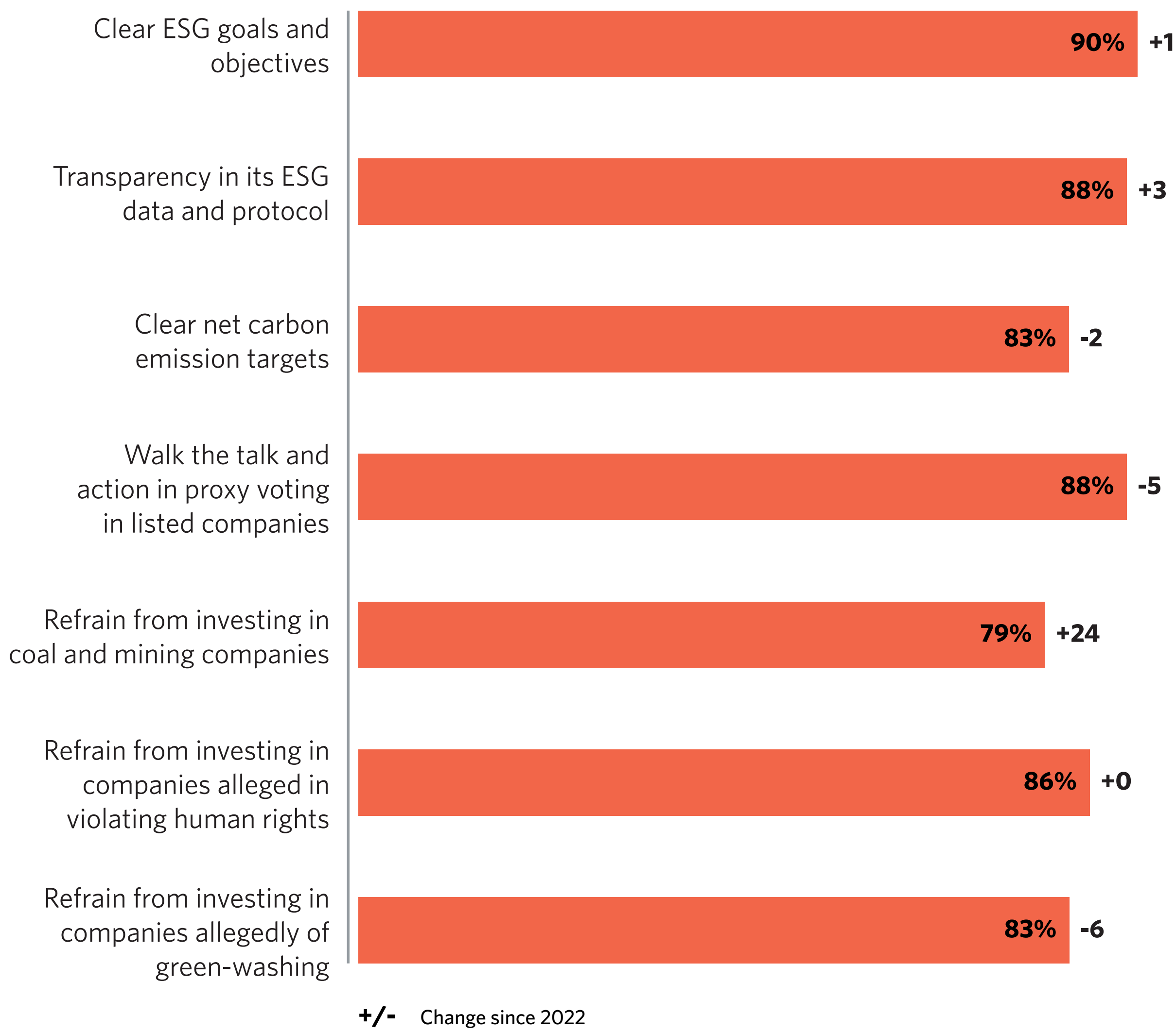
In mainland China, high transparency when communicating with customers (90%) along with strong ESG product offerings (90%) are the most important capabilities investors expect from overseas asset managers. This can be attributed to the central government's growing emphasis on green and sustainability efforts to achieve its net zero carbon target at 2060.

Please indicate how important it is for overseas asset management houses operating in your market to have each of the following.



Clear ESG goals and objectives (90%) represent the most important ESG commitment investors seek from global asset managers. In addition, a demonstrable ability to "walk the talk" and take action in proxy voting in listed companies (88%) and transparency in ESG data and protocols (88%) are the other two factors highly appreciated by the investors in mainland China.

How important are the following Environmental, Social and Governance (ESG) commitments from asset managers?



KEY INSIGHTS FOR ASSET MANAGERS

Looking ahead, there will be a number of challenges and opportunities that mainland China's asset management industry is likely to face in the coming years.

Challenges

Geopolitical risks – The ongoing geopolitical tensions around the world, including the US-China trade tensions, have caused considerable disruption for asset managers operating in mainland China, creating market volatility and prompting managers to exit certain portfolios for downside protection. The coming 12-18 months leading to the 2024 US presidential election will put further pressure on US-headquartered asset managers.

Tightening regulations in the industry – Regulators around the world are progressively ramping up their transparency and reporting demands. The analytics and reporting information required is complex and detailed. Reports must be accurate and often delivered to tight deadlines. Strong governance frameworks providing daily monitoring of regulatory and fund risk profile limits are also essential to maintain the fund's integrity. There have already been cases where asset managers are penalized because of employees using messaging apps for client communications.

All these could potentially increase operating costs, and limit both investment and distribution opportunities. The upcoming global ESG disclosure standard will also set the global ESG reporting standard baseline for local regulators to adopt or follow. Asset managers will need to monitor how the regulatory standards evolve globally, regionally and locally. Asset managers also need to demonstrate authentic actions with tangible results as 88% of respondents said that "walk the talk and action in proxy voting in listed companies" is the most important ESG commitment they want from asset managers.

The Data Security and Personal Information Protection Laws (PIPL) in mainland China - These two regulations will also require global asset managers to comply with regulations both locally and in their home country. Firms need to evaluate their information technology infrastructure to ensure that it complies with the jurisdiction in the PRC. They also need to ensure that they have sought legal advice before exporting any data initially gathered or stored onshore in mainland China. The PIPL also have new requirements that regulate companies' marketing activities using prospective customers' information. Asset managers aiming to market their products and services to prospective mainland Chinese investors need to seek legal advice on the regulatory requirements.

Technological disruption – The asset management industry is being disrupted by technology. Established managers may face challenges from robo-advisors, virtual banks or digital wealth management firms aiming to lure away investors. In addition, the growing adoption of AI and blockchain technologies will also accelerate the technology disruption of traditional managers. Asset managers will need to adapt to these changes if they are to remain competitive and relevant.

Meeting investor service expectations – Investors' transparency demands are growing too. Investors want detailed yet intelligible insights on the levels and sources of an asset manager's performance, along with sophisticated risk metrics on a wide range of factors. Advanced risk and performance analytics are becoming ever more central in investor/consultant due diligence and ongoing investor retention. Producing comprehensive, customizable reports with granular detail that's incorporated into a manager's investment returns and the reasons behind them, gives investors the transparency and comfort they seek. In our latest report, 90% of respondents indicated that transparency in communications with customers is the most important trait or quality they look for in asset managers.

Opportunities

Growing liberalization of the asset management industry – 2023 will see more asset managers receiving FMC licenses and taking full control of their mutual fund joint ventures. The competition with global and local asset managers will be intensified, triggering the global players to innovate their products and distribution strategies to appeal to the investors in mainland China.

Demographic shifts – Mainland China is experiencing significant demographic changes, such as an aging population and growth in digital-savvy young investors looking for more customized investment solutions. The private pensions market is also unleashing huge opportunities for overseas asset managers to bring in their global expertise to mainland China to serve this growing demographic. Asset managers need to look at these growth opportunities to launch new products and strategies to meet their needs.

The growing interest in ChatGPT and AI tools for investment information also present opportunities for asset managers to further adopt technology to innovate and make advances to meet customers' needs on information, portfolio construction and asset allocation.

Investing good and doing good – Responsbile investing is increasingly important to institutions and younger generations. In mainland China, 62% and 48% of respondents indicated that they intend to invest in AI and thematic products respectively in the next 12 months, presenting tremendous opportunities for asset managers expanding into this category. Mainland China last year overtook the US as the world's second largest climate funds market, reflecting the favourable domestic conditions for ESG responsible investing. Mainland China is now the largest market for ESG responsible investing in Asia and continues to rapidly develop its ESG ecosystem.

Growth in appetite for private markets and innovative products – Amid the high market volatility, there is growing interest from investors in private equities and alternatives, which are less correlated with the markets. REITs, active ETFs and semi-liquid products are also starting to draw substantial interest from mainland Chinese investors that asset managers cannot miss. It's time for asset managers to diversify their investment strategies and innovative products targeted at private markets.

Growing high-net-worth investors (HNWIs) and family offices – Mainland Chinese HNWIs and family offices continue to seek more investment solutions and advice to yield asset growth and preservation. Many mainland Chinese family offices have started to diversify their risk and assets around the world in the wake of the recent crisis in the US and European banking sectors.

Concluding thoughts

Mainland China continues to be a growing market for asset managers despite the ongoing geopolitical risks and US-China tensions. In addition to credibility and performance that continue to be key for investors when they choose an asset manager – a key observation of our reports over the past five years – firms need to prepare with thorough risk analysis and preparation to weather any potential storm in the market.

In addition, asset managers also need to fully embrace technological innovation, demonstrate their commitment to the region and enhance transparency in communications with their customers. Product diversification into AI, thematic and responsible investing, and private markets, as well as innovating bespoke solutions for an aging population, HNWIs and family offices, will also be essential for asset managers to flourish.

Underpinning all of these will be the need for each asset manager to have a distinct narrative on its global strengths and ESG commitment to tap into such a burgeoning market.

Are you ready?

FleishmanHillard is committed to advising all asset managers, financial institutions and other professional bodies in supporting their market entry, thought leadership and public affairs campaigns in mainland China.

> **“FleishmanHillard is your go-to-advisory firm in managing your communications and reputation in mainland China.”**

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