



# Federated Hermes China Equity Fund

Where are the contrarian opportunities in China?

Presented by  
Jonathan Pines  
Co-Portfolio Manager

20 April 2023

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For professional investors only

# Federated Hermes

Leading the way in innovative, responsible investing

## Federated Hermes, Inc

- Established in 1955
- Headquartered in Pittsburgh
- Focus on client outcomes
- Listed on the NYSE (FHI)

## Federated Hermes Limited

- A subsidiary of Federated Hermes, Inc<sup>1</sup>
- Active investment since 1983
- Headquartered in London
- Integration of ESG insights into investment portfolios, coupled with strong corporate engagement



<sup>1</sup> Effective from 1 September 2021. <sup>2</sup> Please note the total AUM figure includes **US\$48.4bn** managed by Federated Hermes Limited, of which US\$8.2bn of assets are managed or under an advisory agreement by Hermes GPE LLP ("Hermes GPE"). US\$89.6m of total group AUM figure represents Federated Hermes Limited mandates under advice.

Source: Federated Hermes as at 31 December 2022.

US\$ **668.9** bn<sup>2</sup>  
Assets under management

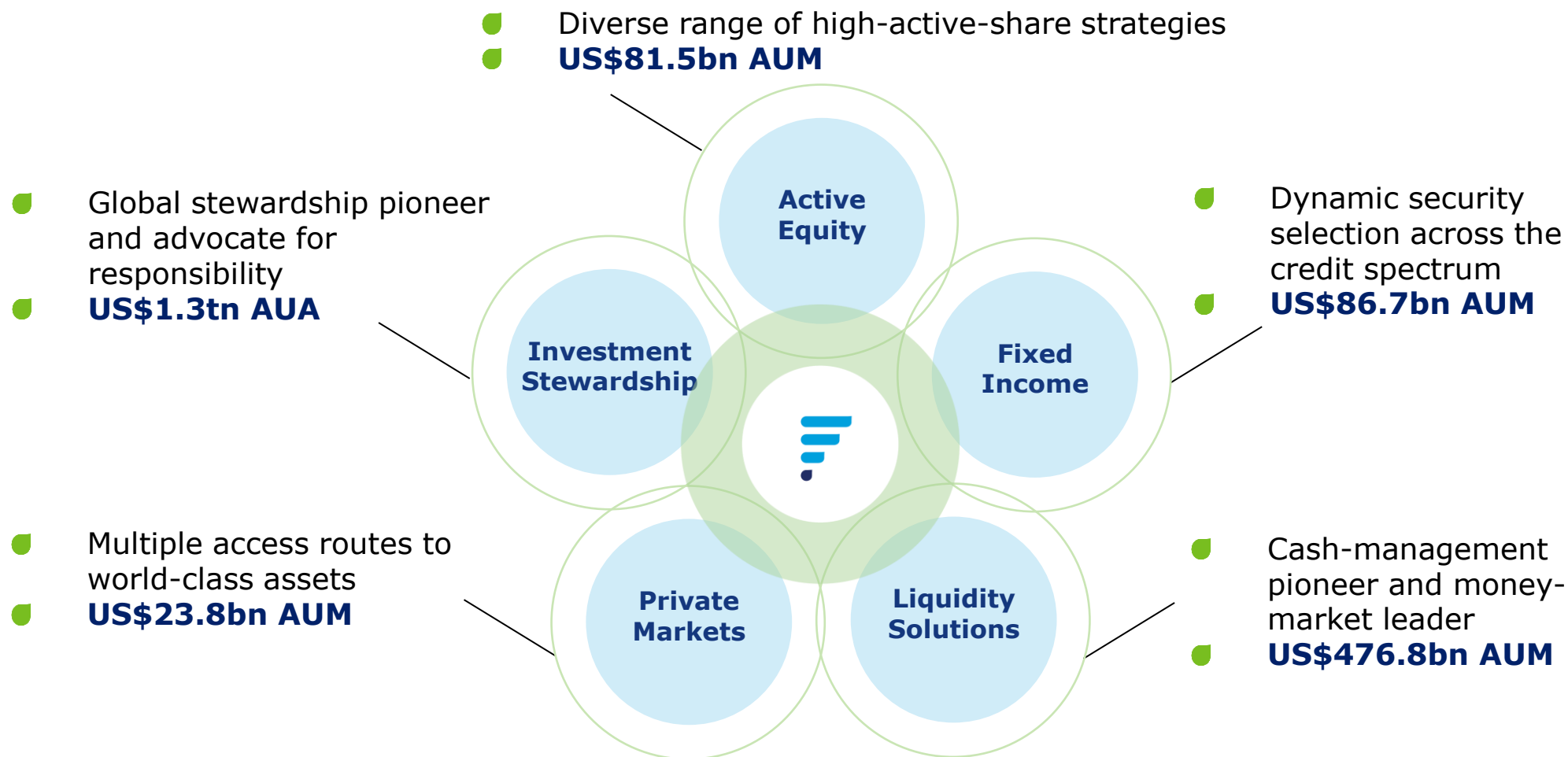
US\$ **1.3** tn  
Assets under stewardship

**1,961**  
Employees

**427**  
Investment and  
stewardship staff

# Federated Hermes

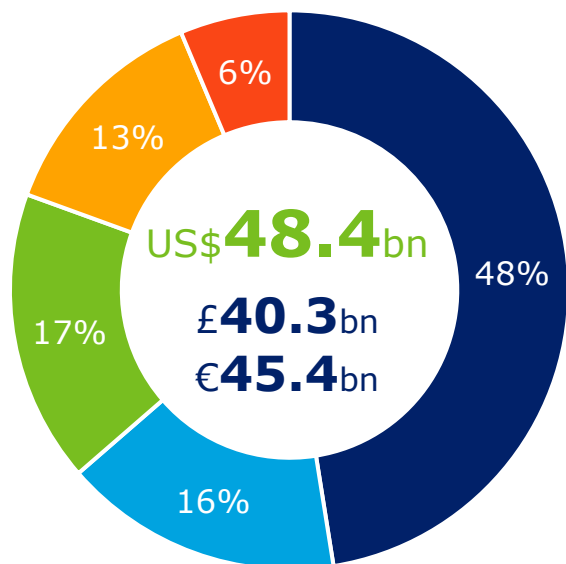
Leading investment and stewardship services



Please note the total AUM figure includes US\$8.2bn of assets managed or under an advisory agreement by Hermes GPE LLP ("Hermes GPE"). US\$89.6m of total group AUM figure represents Federated Hermes Limited mandates under advice. Source: Federated Hermes as at 31 December 2022.

# Federated Hermes Limited

A diversified platform



Total AUM (millions)	USD	GBP	EUR
■ Equity	<b>23,000</b>	19,121	21,551
■ Real Estate	<b>7,820</b>	6,501	7,327
■ HGPE	<b>8,201</b>	6,818	7,684
■ Fixed Income	<b>6,347</b>	5,276	5,947
■ Liquidity	<b>3,073</b>	2,555	2,880

**609** STAFF

Located in:



**278**

Investment and stewardship staff

US\$ **1,340.7**bn

£ **1,144.0**bn / € **1,302.6**bn

Under stewardship

Please note the total AUM figure includes US\$8.2bn / £6.8bn / €7.7bn of assets managed or under an advisory agreement by Hermes GPE LLP ("HGPE"). US\$89.6m / £74.5m / €84.0m of total group AUM figure represents Federated Hermes Limited mandates under advice. Source: Federated Hermes as at 31 December 2022.

# Investment strategies and stewardship services

	1	2	3	4
	LISTED EQUITIES	SPECIALIST FIXED INCOME	PRIVATE MARKETS	THEMATIC
Strategies	<ul style="list-style-type: none"> <li>Global Equities (including Global Equity ESG)</li> <li>Global Emerging Markets</li> <li>Asia ex Japan</li> <li>European Equities</li> <li>SMID</li> <li>Impact Opportunities</li> <li>SDG Engagement Equity</li> <li>Biodiversity</li> </ul>	<ul style="list-style-type: none"> <li>Global High Yield</li> <li>Multi Strategy Credit</li> <li>Absolute Return Credit</li> <li>Direct Lending</li> <li>Real Estate Debt</li> <li>Unconstrained credit</li> <li>EM Debt</li> <li>SDG Engagement High Yield</li> <li>Climate Change High Yield</li> </ul>	<ul style="list-style-type: none"> <li>Real Estate</li> <li>Infrastructure</li> <li>Private Equity</li> </ul>	<ul style="list-style-type: none"> <li>Socially Responsible Investment</li> <li>ESG Driven Investing</li> <li>Impact Investing (e.g., Impact Opportunities)</li> <li>Impact through Engagement (e.g., SDG Engagement High Yield, SDG Engagement Equity)</li> </ul>
AUM <sup>1</sup>	<p><b>US\$23.0bn</b></p> <p>£19.1bn / €21.6bn</p>	<p><b>US\$6.3bn</b></p> <p>£5.3bn / €5.9bn</p>	<p><b>US\$16.0bn</b></p> <p>£13.3bn / €15.0bn</p>	<p><b>US\$4.6bn</b></p> <p>£3.8bn / €4.3bn</p> <p>Thematic AUM is also included under equities, credit and private markets</p>
Approach to ESG Factors	Investment process integrates ESG leveraging quantitative ESG analysis and EOS engagement		Responsible and sustainable investment approach across all private markets capabilities	Tailored, specialist strategies designed to meet specific SRI, ESG and Impact-related objectives
5	Investment insights generated by EOS through its range of active ownership services:			
Stewardship	Stewardship and stakeholder engagement services	Public policy advocacy	Hybrid investment and stewardship mandates	
	<p><b>US\$1,340.7bn</b></p> <p>£1,144.0bn / €1,302.6bn</p>			

**Key:** Investment strategy: Strategies that contribute to Thematic investing

<sup>1</sup> AUM does not include assets under sub advice. Source: Federated Hermes as at 31 December 2022.

# China Equity Fund Overview

## Characteristics

Fund AUM	US\$ 31.3m
Fund inception	20 July 2022
Co-Portfolio Managers	Sandy Pei & Jonathan Pines
Style	Contrarian
Benchmark	MSCI China All Shares Index
Typical number of stocks	30-60 (51)
Base Currency	USD

## Risk Statistics

Ex-ante tracking error	6.54
Ex-ante beta	0.96
Active money	84.07

Concentrated portfolio, 'bottom-up' analysis, contrarian style

We seek attractive price-to-value propositions, prioritising asymmetry of future potential returns over both absolute 'upside' of the investment and quality of the company

**The value of investments and income from them may go down as well as up, and you may not get back the original amount invested. Past performance is not a reliable indicator of future results. Any investments overseas may be affected by currency exchange rates. Investments in emerging markets tend to be more volatile than those in mature markets and the value of an investment can move sharply down or up. The fund has environmental and/or social characteristics and so may perform differently to other strategies, as its exposures reflect its sustainability criteria.**

Source: Federated Hermes and Barra as at 31 March 2023.

# The China valuation discount

The Hang Seng trades at a multi-decade low relative to the world since 1998



Source: Bloomberg as at 31 March 2023.

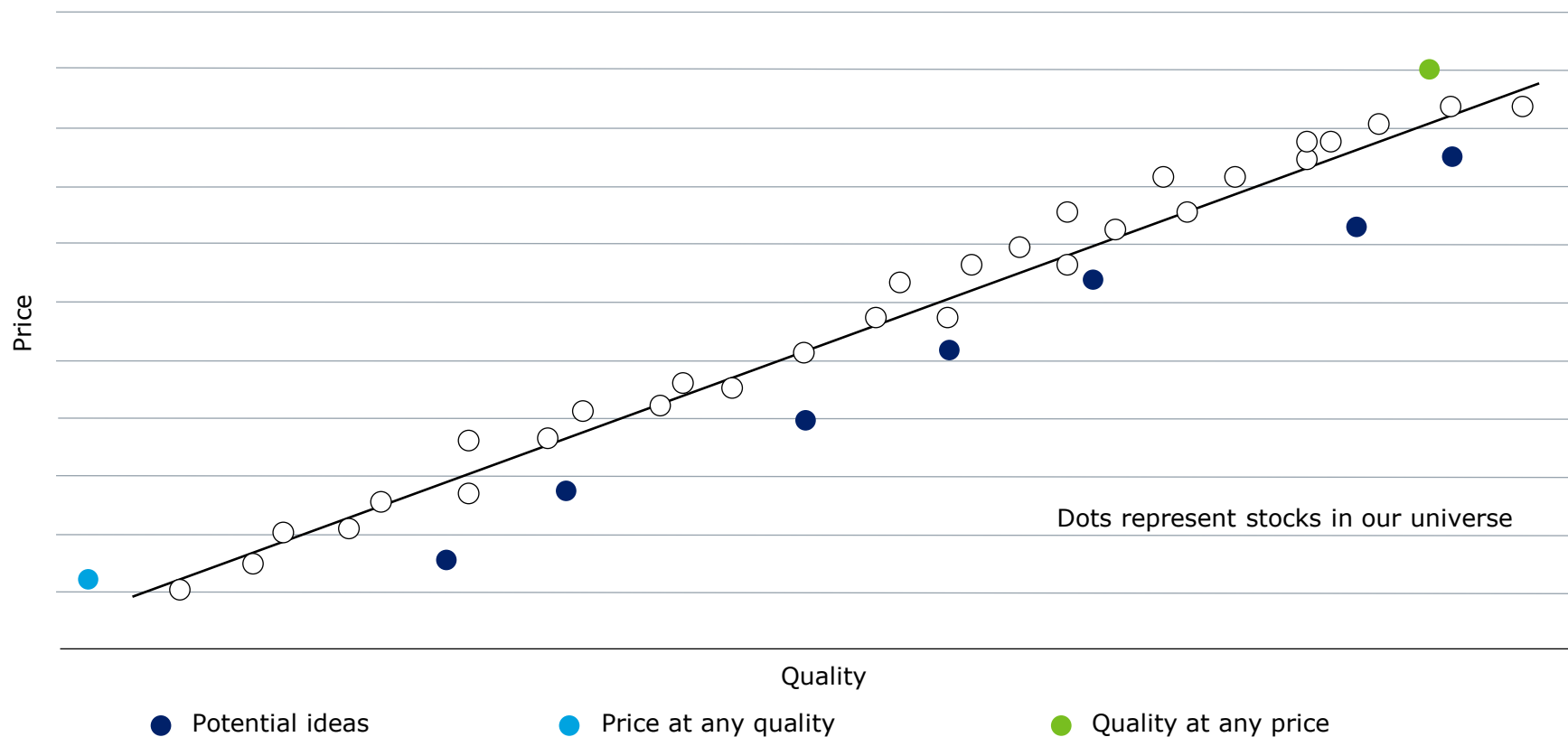
**Past performance is not a reliable indicator of future results.**

# China – Developments in six key risks

<b>Risk</b>	<b>When risk peaked?</b>	<b>Developments since peak</b>
<b>Delisting of ADRs</b>	Early 2022	Risk has substantially lessened following US-China technical co-operation
<b>VIE structures</b>	Constant “background” risk	Continuing
<b>Common Prosperity</b>	Q2 2022	Risk fallen as China adopts acts that are more business and growth friendly
<b>Tensions with US</b>	Ongoing	Long term trajectory uncertain and actions might be tactical but China softening approach (Foreign minister appointment, sharp reduction in “wolf warrior” diplomacy, less aggressive foreign policy)
<b>Zero-covid policy</b>	Q4 2022	Risk eliminated as policy abandoned
<b>Property contagion</b>	Possibly 2022	Huge, ongoing, policy response and capital raises



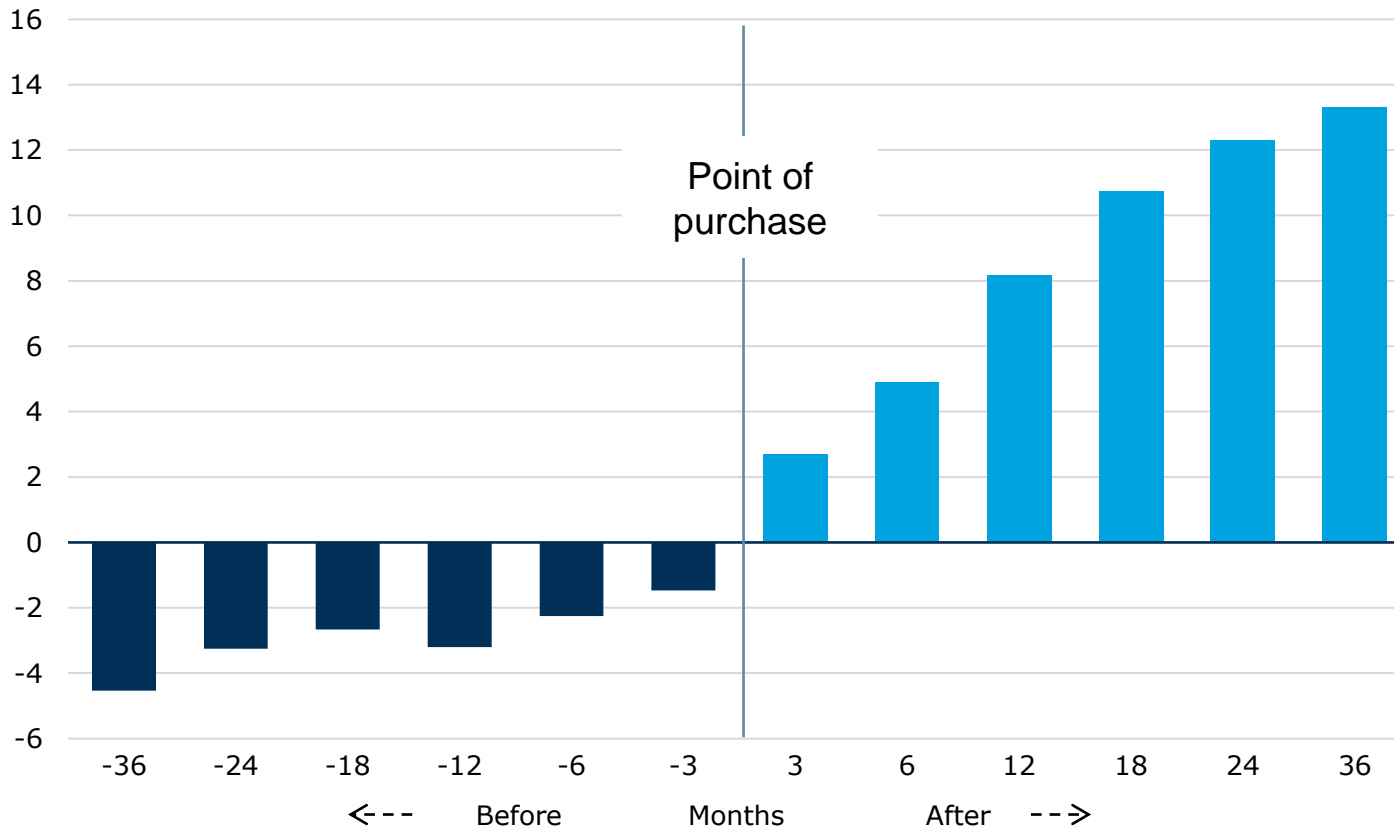
# Investment Philosophy



# Contrarian style

## Contrarian investment style drives long-term returns

### Buys relative return (%)



"... the overweights have added very strong and fairly persistent alpha

Unusually, the underweights have also contributed positively

There is clear evidence of skill in stock picking."

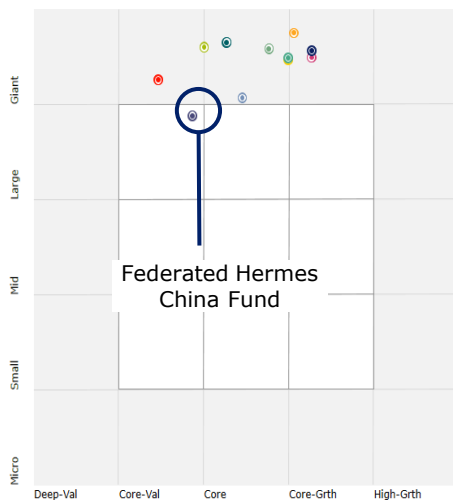
Analytics

Source: Analytics as at 28 February 2023.

**Past performance is not a reliable indicator of future results.**

# Federated Hermes China Equity Fund

## Style map vs peers<sup>1</sup>



- Low overlap with peers and high active share
- Seek attractive price-to-value propositions, not the cheapest stocks

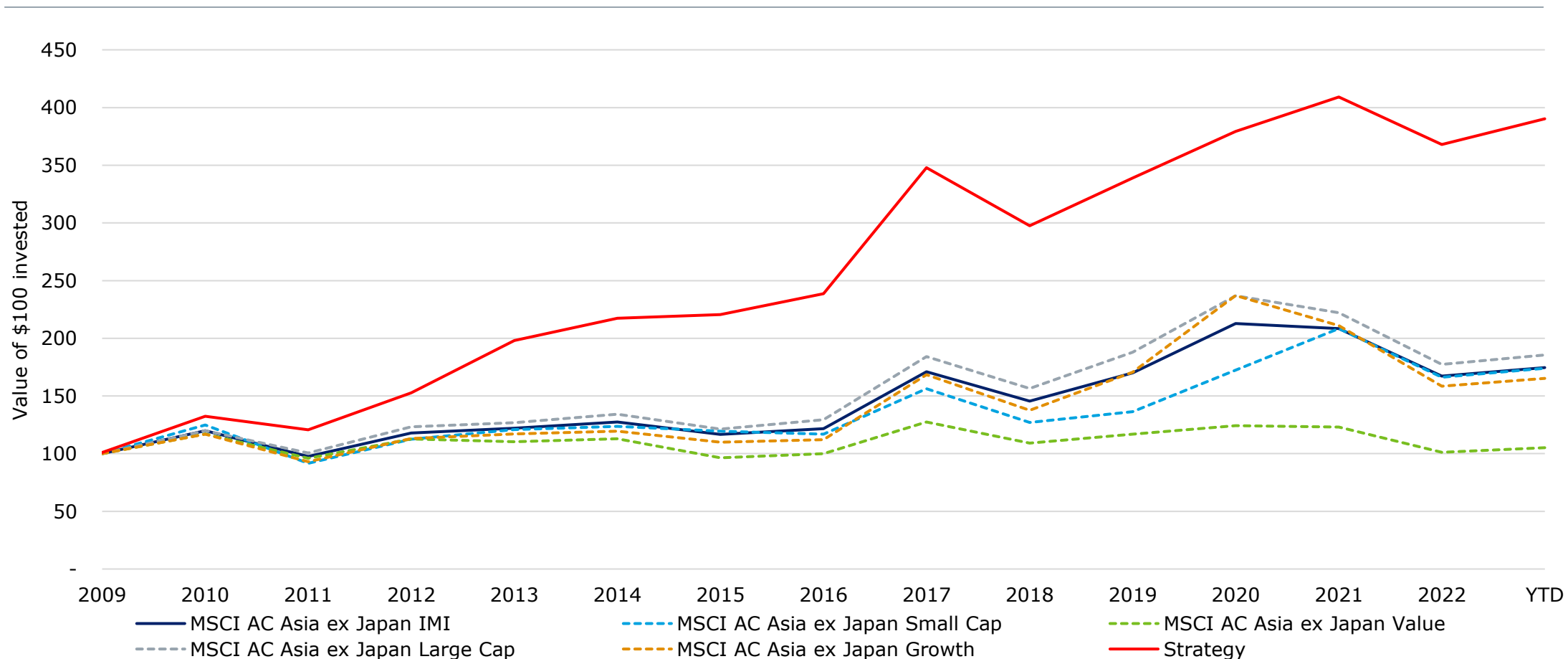
	Portfolio Date	P/E Ratio (TTM)	P/B Ratio (TTM)	Dividend Yield	Average Market Cap (mil) <sup>2</sup>	# of Stock Holdings	ROE % (TTM)	ROA % (TTM)
<b>Federated Hermes China Eq X USD Acc</b>	<b>28/02/2023</b>	<b>13.23</b>	<b>1.11</b>	3.30	<b>15,911</b>	<b>59</b>	<b>9.10</b>	<b>4.24</b>
JPM China A (dist) USD	28/02/2023	21.57	2.88	1.38	43,639	77	13.99	7.03
UBS (Lux) EF China Oppo(USD) P USD acc	28/02/2023	11.87	1.41	2.63	44,330	62	14.50	7.43
Fidelity China Consumer Y-Acc-USD	28/02/2023	27.31	3.03	1.37	66,710	64	11.27	6.23
Fidelity China Focus A-Dis-USD	28/02/2023	9.03	1.01	4.76	29,733	83	11.48	4.85
FSSA China Growth II USD Acc	28/02/2023	14.16	2.14	3.03	20,605	56	18.05	8.69
UBS (Lux) ES All China (USD) P acc	28/02/2023	13.27	1.71	2.51	47,751	58	15.48	8.24
Mediolanum BB Chns Rd Opp LA	31/12/2022	18.84	2.45	1.75	37,994	122	13.22	6.61
Schroder ISF China Opps C Acc USD	31/03/2023	20.67	2.23	1.39	41,217	76	11.46	5.31
Allianz All China Equity WT USD	28/02/2023	17.86	2.36	1.66	40,916	80	14.14	6.86
Barings Hong Kong China A USD Inc	28/02/2023	15.99	2.10	1.98	51,543	62	10.95	4.56

<sup>1</sup> Source: Morningstar, latest available data as of 31 March 2023. Coloured dots represent styles of peers as determined by Morningstar. Peer group selected based on top 10 AuM funds in the China Equity Morningstar category. <sup>2</sup> Average market cap is calculated as the geometric mean.

**Past performance and past performance is not a reliable indicator of future results.**

# Outperformance despite an out of favour style

## Asia ex-Japan Strategy



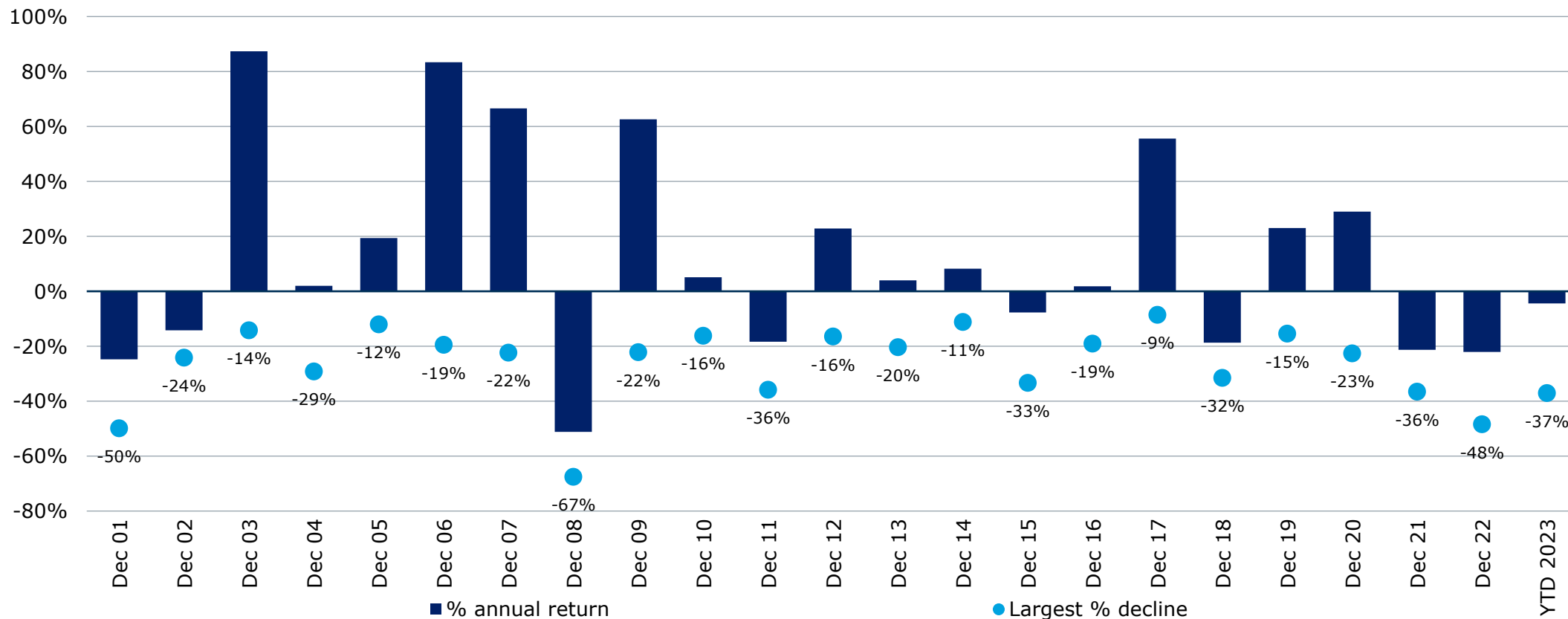
Performance of the strategy is shown in US dollars, net of 75bps management fees and costs, since inception on 01 January 2010. Relevant MSCI indexes used for value, small cap, growth and large cap factors are the MSCI AC Asia Ex Japan Value Index, MSCI AC Asia ex Japan Small Cap Index, MSCI AC Asia Ex Japan Growth Index and the MSCI AC Asia ex Japan Large Cap Index. Relative figures calculated arithmetically. Source. Federated Hermes, Northern Trust, Bloomberg, as at 31 March 2023.

**Past performance is not a reliable indicator of future results.**

# MSCI China – annual returns vs annual drawdowns

Investors pay a high price for being “shaken out”

## Annual performance of the MSCI China Index<sup>1</sup>



<sup>1</sup> MSCI China index used to show longer return history.

Source: Bloomberg as at 31 March 2023.

**Past performance is not a reliable indicator of future results.**

# Outperformance in down periods

## Asia ex-Japan Strategy

**Increases likelihood that investors will not be “shaken out” at disadvantageous time**

	Absolute (USD%)	
	Benchmark	Strategy
2010	20	30
<b>2011</b>	<b>-19</b>	<b>-10</b>
2012	21	26
2013	4	29
2014	4	9
<b>2015</b>	<b>-8</b>	<b>1</b>
2016	4	7
2017	41	45
<b>2018</b>	<b>-15</b>	<b>-15</b>
2019	17	13
2020	25	11
<b>2021</b>	<b>-2</b>	<b>7</b>
<b>2022</b>	<b>-20</b>	<b>-11</b>
YTD	4	6

Source: Federated Hermes as at 31 March 2023. Performance of the Asia ex Japan Strategy is shown in USD and net of 75 bps management fees and costs. The information shown is supplemental to the GIPS® compliant composite report provided in the Appendix. Benchmark shown is the MSCI All Country Asia ex Japan IMI. **Past performance is not a reliable indicator of future results.**

# Top 15 holdings

Holdings	Actual weight (%)	Benchmark weight (%)
Tencent	7.08	8.44
Alibaba	5.81	5.23
Baidu	4.48	1.15
JD.com	3.89	1.31
Foxconn Industrial	3.61	0.21
CK Hutchison	3.14	0.00
Swatch Group <sup>1</sup>	3.06	0.00
SF Holding	3.01	0.33
Universal Scientific	2.82	0.00
Tingyi	2.81	0.09
China Oilfield Services	2.58	0.05
Cathay Pacific	2.19	0.00
Weibo	2.09	0.04
Shangri-La Asia	2.07	0.00
Trip.com	2.03	0.57
<b>Total</b>	<b>50.67</b>	

<sup>1</sup> Eligible for purchase as most value, revenue, earnings, net income or net assets derived from Asia.  
Source: Federated Hermes Limited and Bloomberg as at 31 March 2023.

# Summary

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Our portfolio is **concentrated** and stocks are selected through **bottom-up** analysis based on fundamental research

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We have a **contrarian** style and **absolute return** mindset, prioritising the **asymmetry** of future potential returns over both the absolute upside of the investment and quality of the company

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We have a well resourced **effective ESG strategy**, appropriate to our region

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Our team is experienced, diverse and **stable** team, with a **strong track record**, with lead and co-managers founding the strategy in January 2010

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We have a **long-term** investment horizon and tolerate short-term volatility



# Appendix



# China's special character makes separate allocation right for some investors

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- Large market in its own right
  - ~7,500 stocks, with the China A stock market being most liquid after the US
  - High and expected rising weighting in EM and Asia ex Japan benchmarks
  - Three separate venues for trading, each with different capital controls, quality and growth characteristics, legal frameworks, propensity for fraud, and 'over-the-cycle valuations'
- Capital controls, high retail participation and more explicit government support have resulted in A share market being structurally more expensive, a dynamic that is expected to continue
- China highly sentiment and momentum driven (with A share market being retail dominated), with increasing volatility and inefficiency
- Correlation of A share market with the rest of Asia ex Japan, and other global stock exchanges is lower
- Weight of A shares in the benchmark is approximately 50% vs 5% in the Asia ex Japan index<sup>1</sup>
- Tensions with the US increase risks of asset class

<sup>1</sup> Source: Bloomberg.

# Strong, Stable Team

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- Strong long term track record for Federated Hermes Asia ex Japan Equity Strategy
  - +5.7% p.a. outperformance in 13 years since inception<sup>1</sup>
  - Federated Hermes Asia ex-Japan Strategy ranked 2/75<sup>2</sup> and Asia ex-Japan fund<sup>3</sup> ranked 3/126<sup>4</sup>, despite headwinds
  - Outperformed all MSCI Asia ex Japan benchmark sub-styles (value, growth, quality, small cap)
  - China overweight for majority of years
- Co-managers of China Equity Strategy were founder managers of Federated Hermes Asia ex Japan Strategy, low analyst turnover
- Co-manager and most of team Chinese
- Understand China-specific elevated risk
  - ADR risks, VIE risks
  - Fraud risks
  - Sectors most likely to be sanctioned by US
  - Sectors most likely to be impacted by more aggressive 'common prosperity' policies

<sup>1</sup> Strategy inception date 1 January 2010. Performance of the Asia ex Japan Strategy is shown in US dollars, net of 75 bps management fees and costs. Relative figures calculated arithmetically. <sup>2</sup> Source: eVestment as at 31 December 2022. <sup>3</sup> Fund inception date 1 November 2012. <sup>4</sup> Source: Morningstar peer rankings as at 28 February 2023. Source: Federated Hermes, Northern Trust, Bloomberg, as at 31 March 2023. Relevant MSCI indexes used for value, low size, growth and quality factors are the MSCI AC Asia Ex Japan Value Index, MSCI AC Asia ex Japan Small Cap Index, MSCI AC Asia Ex Japan Growth Price Index and the MSCI AC Asia ex Japan Quality Index. Returns are indicated for our Asia ex Japan Strategy and there is no guarantee that similar future results will be achieved for any strategy including a China Strategy. The information shown is supplemental to the GIPS® compliant composite report provided in the Appendix.

**Past performance is not a reliable indicator of future results. In particular, the performance of the Federated Hermes Asia ex Japan Equity Strategy is not a reliable indicator of the future performance of the Federated Hermes China Equity Fund.**

# Investment team



**Jonathan Pines, CFA**  
Portfolio Manager  
24 years' industry experience



**Sandy Pei, CFA**  
Co-Portfolio Manager  
13 years' industry experience



**Maggie Sun**  
Investment Analyst  
9 years' industry experience



**Dean Brown, CFA**  
Investment Analyst  
7 years' industry experience



**Jia Xu**  
Investment Analyst  
7 years' industry experience



**James Cook**  
Investment Director  
25 years' industry experience



**Hugh Shepherd**  
Investment Specialist  
13 years' industry experience



**Jonathan Day**  
Portfolio Assistant  
18 years' industry experience

Supplemented by wider team

## Research, Analytics, Trading and Client Support

Global Emerging Markets  
Investment Team

Economics team

Investment Office

Trading

EOS

Quant Research

Risk analysis & Performance  
Measurement

Client Relations

# German Team

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**The value of investments and income from them may go down as well as up, and you may not get back the original amount invested. Any investments overseas may be affected by currency exchange rates. Past performance is not a reliable indicator of future results and targets are not guaranteed.**

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## Federated Hermes

Federated Hermes is a global leader in active, responsible investing.

Guided by our conviction that responsible investing is the best way to create long-term wealth, we provide specialised capabilities across equity, fixed income and private markets, multi-asset and liquidity management strategies, and world-leading stewardship.

Our goals are to help people invest and retire better, to help clients achieve better risk-adjusted returns, and to contribute to positive outcomes that benefit the wider world.

All activities previously carried out by Hermes Investment Management are now undertaken by Federated Hermes Limited (or one of its subsidiaries). We still offer the same distinct investment propositions and pioneering responsible investment and stewardship services for which we are renowned – in addition to important strategies from the entire group.

### Our investment and stewardship capabilities:

- Active equities: global and regional
- Fixed income: across regions, sectors and the yield curve
- Liquidity: solutions driven by four decades of experience
- Private markets: real estate, infrastructure, private equity and debt
- Stewardship: corporate engagement, proxy voting, policy advocacy

For more information, visit [www.hermes-investment.com](http://www.hermes-investment.com) or connect with us on social media:  