Hello and welcome to this programme from Baillie Gifford. The latest in the series where we talk to the fund managers of the group's different investment trust. My name is Gavin Lumsden, I'm from Citywire and today, I'm speaking to Roderick Snell, manager of Pacific Horizon investment Trust. Roddy is a partner at Baillie Gifford, having joined the Edinburgh based company nearly 18 years ago. He's worked on Pacific Horizon for ten years and became the Asia Pacific fund's lead manager in 2021

This is a great time to be hearing from an experienced Asia investor. While lots of attention is paid to China's slower than expected recovery from the pandemic, the region is viewed as being in better than shape than many economies in the west. I'm sure Roddy will give us his thoughts on both those topics. Right, time to meet Roddy. Hello Roddy. Thanks very much for joining us, how are you?

Very good, thank you.

I'll start off with my questions if I may. You're a growth investor. In fact, you describe your strategy as growth squared. Can you remind us what you mean by growth squared and why you still believe in it after what has been a tough 18 months for growth investors?

Certainly. We believe Asia will be one, if not the fastest growing region over the coming decades and we simply want to be invested in its fastest growing companies. So, it's growth times growth or growth squared, as we like to say. We have faith in this because it works. We've been managing dedicated Asian money since 1989. So, for more than three decades. And we've got a very good track record over really, all reasonable timeframes and through numerous market crises, political upheavals, cycles, and investment styles. If I bring it in today, when I look at the portfolio, I'm genuinely excited. Rarely do the characteristics of our holdings look this attractive. For instance, the average growth of the portfolio is substantially higher than the index. Yet, the valuations of the portfolio are about the same as the index, if not a discount.

You very rarely see that. Normally, we would be paying a 20% to 40%-plus premium to the index, but today, there is no value for that extra growth. So overall, really very happy with the portfolio and certainly, no change from us trying to find the fastest growing companies in the fastest growing region or growth squared, as we like to call it.

Specifically, what are the long-term growth trends you've identified in Asia?

I'd probably highlight three key areas for the portfolio at the moment. First, we would have a big exposure to the rise of the Asian consumer. Really driven by increasing wealth and positive demographics. This is arguably one of the most powerful investment themes of the next decade with Asia likely to be adding at least one to 1.5 billion people to the middleclass by 2030. However, unlike the past decade, where most of these additions came from north Asia, like China, this time it's going to be more from the younger countries of India and Southeast Asia. Which is where we are positioned with our three largest overweight countries being India, Vietnam, and Indonesia. Second theme probably worth highlighting would be the energy transition.

Now, some of these we're exposed to directly with companies such as LONGi Green Energy, the world's largest solar panel manufacturer in China. Most of our exposure's actually the supply chain. Be that batteries through companies like Samsung SDI, supplies a number of key western brands including BMW or through more materials, especially copper and a little bit of nickel, which is why we're in such a large position in materials in the portfolio. Then finally, innovation. Which continues at a rapid pace across Asia. We've been adding to a number of areas over the past six months, in particular, semiconductors, where Asia is a world leader. For example, we added significantly to our holding in EO Technics recently. This is a company that supplies equipment for the drilling and cutting of wafers and semiconductors. Crucially, they focus on lasers technology.

So, whereas today's technology is based on ceramic blades and drills, as semiconductors get smaller and more complex, lasers will be needed and EO Technics is arguably the world leader in this field. So, we expect exponential growth from their products over the next five years. So those are probably the three areas I'd highlight at the moment. The Asian consumer, the green transition and innovation across Asia.

Despite the global economic turmoil over the way in Ukraine and inflation, it seems Asian economies and some of the region's stock markets have been quite resilient. Why is this and is it the beginning of some sort of convergence with more developed markets?

That's a great question. Yes, I think it could be and the reason is really quite simple. The macro position of Asia looks very good compared to the west. That's really because the west has behaved, actually, like a classic emerging market and while Asia has been orthodox and restrained. For example, firstly Asia didn't print money and destroy its balance sheets, stimulating during COVID. China's physical monetary stimulus was about 10% of GDP versus Europe at 70% or 80%. Secondly, for a long time, Asia's had sensible real interest rates versus negative in the west. Thirdly, we really don't have any inflation issues across Asia. Supply chains have been okay and there are no labour issues. People are keen and need to go to work. Finally, capital inflows into Asia and, actually, more broadly in emerging markets, have actually been negative for the best part of a decade.

So, we haven't had hot money coming into the region for a very long time. You add these up and that's the reason why Asia has been so resilient. To put that resilience into perspective, remember until recently, the US dollar had been on an absolute tear. It's the highest it had been for 40 years and typically at any other time in history, that would have sucked all the money out of Asia and emerging markets and you would have had a crisis in a number of countries. That simply hasn't happened this time and that's a very strong signal, I think, for the position of Asia. If you want to be very bullish, you might say that the US dollar has peaked and that would be a massive tailwind for Asia. I think actually, quite likely over the coming few years.

You've mentioned three of the countries that you're overweight in compared to the regional stock market index, but just over a third of the trust is invested in China and Hong Kong and it's been a tumultuous time to be an investor there. Many people are anxious about the Chinese market. How do you assuage investors nerves when it comes to China?

Well, China certainly has its challenges, but firstly, I think it's always useful to take a step back and put the country in context because many investors have been bearish on China for decades. If we go back over the past 40 years, China has arguably been the greatest growth achievement in history. In 1980s, GDP per capita was less than Afghanistan. [marker 0:10:00] Today, it's the second largest economy on earth. So, let's not forget, this is a country with a great track record of success and it's successful moved up the value chain, became a technological leader and crucially, it's been investing heavily in infrastructure. Be that the largest high speed rail network in the world or the biggest wind power generator. Now, there are industries such as electric vehicles and batteries, where it's clearly, I'd say, the leader in the world.

Now today, there are certainly challenges. The reopening of the economy has been softer than expected within a weaker than expected consumer and property market and quite high youth unemployment. Again, put that in perspective relative to the west, actually, the macro looks pretty decent in China. We're going to have, probably, 4% to 5% GDP growth, which is better than any other large developed economy. Crucially, they've got significant room to stimulate. Let's not forget, China hasn't been printing money and it's had sensible high interest rates and it can start to cut. I think there are clear signs that policy is easing and there will be support for the private sector. You combine that with valuations, really in a distressed state that they are now and certainly, in the short to midterm, I think China starts to look actually very attractive.

You've been taking advantage of those cheap valuations by adding to China over the past year. could you say a bit more about which areas and companies you're finding opportunities to invest in?

I think the key thing we've been looking for, at the moment, for investments, is companies that are policy aligned. So, we took a new holding, for example, in the past year in a company called Synergy, which is a semiconductor manufacturer, specialising in analog chips. Really, they should be a beneficiary of western substitution as currently, about 90% of analog chips in China come from the US. As I'm sure you can imagine, China is desperate to localise that production. Synergy really is the best Chinese company in this space. It was founded in around 2008 by members or former employees of Texas Instruments, which is the world leader in analog devices. So, they know what they're doing. They've got very close relationship with UMC, which is one of the top three foundries in the world.

So, they have a lot of high-tech capacity to produce their chips and they are the largest domestics player, but that still means they only have a 3% or 4% market share. So, a huge growth opportunity and we actually added relatively recently to the company. We've also been adding to a number of internet names where we think they are aligned with the long-term policies of the government. For example, Baidu, the search business in China. The core search business which generates probably, four or $5 billion a year is probably on seven times PE multiple and that gives you the rest of the business for free. It's these other parts of the business where we're really excited. Baidu is arguably, the leader in autonomous driving technology, for example.

That's very much backed by the government and indeed, Baidu are the only player to have a license for high precision mapping in the country. Given that it's a very sensitive area. They're arguably also a leader in AI. Again, a key area for government policy. Finally, I'd just highlight that it's not all tech names we're finding in China. Some of the traditional names are also very interesting. The likes of Ping An, which is the largest private insurer. Again, this is an area that we think the government is keen to support, given the lack of a social security net in the country and you're paying less than one times price to book for a company generating 20%-plus ROEs, with growth picking up. The value of new business this quarter was about 70% year-on-year. so very strong results and very subdued valuations. So, think very good long-term opportunities there. So really, adding to areas where we think there is long-term government support and valuations are very supportive at the moment.

So, let's turn to India where, by contrast, you've reduced your exposure. India now counts for a quarter of the portfolio. Can you talk us through your view on India overall and the companies you've reduced, in particular?

We remain very positive India, I think is the key message. As you say, it's a quarter of the portfolio and, actually, our largest overweight position, just ahead of Vietnam. Now, we have trimmed some stocks and that was really based on valuations. That was done mostly six to 12 months ago and included companies like Indigo Paints or Happiest Minds, the IT outsourcer. These are great companies, but they have done very, very well and were trading on multiples of nearly or more than 100 times PE. We've simply been finding better growth opportunities elsewhere. Particularly in China and, actually, more recently in Vietnam. So just trimming some of those very highly rated stocks in India, where we think the valuations were too high for the growth rates that we were expecting in the next five years.

Overall, really do remain very positive. The country has some great companies. I'd also highlight two interesting developments that we see taking place at the moment in the country. The first would be that cheap smartphones have brought the internet to the masses. That really has catalysed really, for the first time in India, a number of genuinely innovative technology companies. If you go to Bangalore, which is at the centre of this innovation, the city really is just booming. This provides direct opportunities for us to invest in. For example, the trust owns Dailyhunt, that's a private company that effectively it's the shortform video app, the TikTok of India. Also more broadly, this innovation could add significant growth to the country over the coming decades that's really not captured in peoples' GDP forecasts.

Could you say a bit more about some of the companies you are investing in, in India?

The opportunities are broad. Certainly, I think bringing the internet to the masses is a huge opportunity and we've got actually, a pretty big exposure to that through the likes of Delhivery. It's the largest private logistics company in the country and really, a play on ecommerce, where it's got a 50% market share in deliveries. We also own direct internet platforms like PB Fintech, which is the Go Compare of India, if you like. Price comparison site. That's growing revenues at 30%, 40%-plus at the moment. I also think that actually, Reliance Industries is very interesting. This is the company that's best known for its petrochemicals business. Actually, this is the company that brought 4G mobile internet to India and has rapidly become the biggest domestic ecommerce business.

Actually, just recently, the Qatar Wealth Fund are rumoured to be investing in the retail division at $100 billion valuation. So, a huge wealth creation has gone on there in recent years. Finally, I'd say [inaudible 0:17:17] the traditional sectors in India that are exciting. Especially infrastructure. India is finally investing again. So we own companies like Skipper, which is the largest power transmission cable company in the country. We continue to have large exposure to real estate developers like Indiabulls. We actually doubled our position relatively recently. That's an industry that's consolidated down to a handful of players and we think is at the start of a big construction cycle. So, plenty of opportunities in India from technology to traditional construction businesses.

Let's move on to Vietnam and another of your overweights against the MSCI All-Country Asia Index. Vietnam's your second largest overweight, with about 6% of the trust. So, the market was very weak for most of last year, but has done much better since November. I believe you're just back from a trip to the country. So, what were your key impressions and findings?

As a reminder and as I think we've mentioned many times before, the rationale for Vietnam is that we think it's the best structural growth story of any Asian economy over the next decade or two. Really, because it's one of the few Asian countries building up a successful export manufacturing industry, which is what you need to do as an emerging economy in order to emerge. They've done a fantastic job of this, especially with companies looking to diverse away from China predominantly picking Vietnam. Now, that said and as you mentioned, the country had been very weak, particularly last year, down about 30%. Really over concerns over the economy and there are a couple of issues.

Firstly, you had a corruption clampdown in the country because partly on embezzlement during COVID, but more importantly, a clampdown on the property sector, really related to some property land purchases that were deemed unlawful. At the same time as that, you also had a clampdown on bond issuances to the property sector, which removes a source of funding and led to a liquidity squeeze at the property companies, which spilled over into the banking sector. Now, those issues, with the property and the banks led the market. Remember, it's 90% retail so very short-term, led the market, to get very nervous on property and the banks. The good news is that having been to the country, it's pretty clear that these are not systemic issues. They're relatively short-term in the property and the banking space and should be sorted out [marker 0:20:00] in reasonable time.

I'd say that doesn't mean Vietnam's completely out of the woods. There's a broader issue you see out there now from this corruption clampdown, which is really a policy paralysis. The big issue being the infrastructure is not being as proved as fast as it needs to. That is an issue they do need to sort out. If you go to some of the special economic zones, they are having for example, power shortages at the moment. For companies like Samsung Electronics, you simply can't afford to have power outages. So, it's certainly an area that Vietnam needs to address quickly. All of these issues are being resolved and overall, Vietnam's economy is fine. There're inflation issues, they can cut rates and it knows what it needs to do.

So having come back from Vietnam, we've really viewed this as a bit of a buying opportunity and have added [unclear 0:20:53] to our holders in the country. Took a new holding in Mobile World, for example, which is the largest electronics retail in the country. It's also building up the second largest grocery business in Vietnam. So today, I think Vietnam will be about 7% of the trust, having added to a couple of the names and that new holding in Mobile World. Overall, the long-term story of Vietnam remains very much intact.

Very positive on Vietnam. What about Indonesia? You've touched on that already, but at nearly 8% of Pacific Horizons, you have been reducing the exposure. So, could you say a little bit more about what you're finding in Indonesia?

From a top-down perspective I think Indonesia's doing really very well. The macro looks good. They've had no major credit cycle over the past four or five years. Inflation is fine and domestic growth looks good. Historically, Indonesia has always been the biggest beneficiary in ASEAN of rising raw material prices. If you go back to 2002 to 2012, this would have been the best performing economy in the region. Today, I think what's particularly exciting is that Indonesia is flush with materials that are really needed for the green transition. This is the world's largest producer if nickel and green energy could really transform the country. That's helped by the fact that several years ago, the country banned the export or raw materials. So, you actually need to setup processing plants in Indonesia to process those materials before you export them.

That's leading to a lot of investments in the country. The numbers are big. There's been about 25 to $30 billion in FTI in some of these areas. In the likes of [unclear 0:22:43] and LG, some of the world's biggest battery makers. Tesla are rumoured to be looking to invest another $5 billion into the country as well. The scale of the things is just huge. If you go to the TKA Industrial Park, for example, out on one of the islands, this is an industrial park the size of Edinburgh. It's focused purely on making batteries and it's all powered by renewables, hydro and solar. So big opportunities for the country in these areas. Now perhaps counterintuitively, we have been reducing some of our exposure to Indonesia and that's really been focused on reducing out exposure to Nickel. That's because there's probably, in our view, too much supply coming on from Indonesia.

Now that's great for Indonesia, but not so good for the companies involved. The issue really comes down to a technology called HPAL, which is process used to convert non-battery grade nickel to battery grade nickel. Now, HPAL has always been very, very costly, and difficult and people haven't got it to work. It appears that the Chinese have cracked this technology and they've been investing tens of billions of dollars into Indonesia and will be doing the same for several years. So, we don't think there's going to be a huge shortage of battery grade nickel in the next three to four years because of this transformation that's come about from HPAL. So, we've been a little bit more cautious on nickel and hence, we've been reducing that nickel exposure in terms of the companies that we invest in.

More thematically, but linking to the nickel topic, energy transition is top of mind for many investors, particularly around energy security. Can you say a bit more about how you're responding to this in the fund?

Yes, we've probably got 10% to 15% of the portfolio invested in companies involved in the energy transition. Now, most of that would be actually in the supply chain. So, in materials. As I say, that would mostly be copper today. We used to have quite a bit of nickel, but that's been significantly reduced. So, it's mostly copper and the rationale for that, as we've discussed previously, is that we think there's a real tightness in supply for nickel. There won't be significant supply coming on for the next ten years. That's how long it takes from identifying and bringing a mine online. If anything, the timing is getting longer. That's coming up against a demand inflection point that we see for copper. It's the world's best conductor of electricity and the green transition simply can't happen without significant amounts of copper for transmission, electric vehicles, etcetera.

So, we think that, actually, the demand for copper from the green transition could equal or actually, surpass the demand we saw in the last [unclear 0:25:44] cycle, when China was industrialising in the 2000s and as I say, we simply don't see the supply coming on for the next decade to meet that. So quite big exposures to copper across the portfolio. The other areas we've got big positions in terms of the supply chain would be batteries. Particularly in South Korea, the likes of Samsung SDI which I mentioned earlier, supplying the likes of BMW. Then we also have some direct plays like LONGi Green Energy, which is the largest solar panel maker in the world, in China. Looking for new ideas continuously. We haven't actually owned many of the electric vehicle manufacturers themselves. Particularly in China.

We've struggled to identify who will be the winners in that space and have preferred, as I say, to go for the supply chains of copper or batteries. We are possibly starting to see the winners emerging in the China space. The likes of BYD cementing strong competitive positions. So, looking very hard at the EV manufacturers now in China and might be looking to add to those in due course.

Last question from me before we go onto the Q&A from the audience. Pacific Horizon, you're largely investing in quoted companies listed on stock exchanges, but just over 5% is invested in unquoted private companies. I think you've mentioned one of those already, the Dailyhunt in India. Can you update us on the private company exposure of the trust and are you finding any new opportunities off-market?

So, with a number of our private companies such as Delhivery and Zomato having listed over the past 12 to 24 months, our private company exposure is currently down to about 6%. That will be made up of three companies, which would be ByteDance, the maker of TikTok in China. About 2% of the portfolio. Dailyhunt in India, as mentioned, about 3% and Micro Connect in China, which is again, 1%. In terms of opportunities, to be fair, there haven't been that many lately. The pipeline is certainly much weaker than it was 12 to 18 months ago. However, we did make our first new private investment in some time in Micro Connect. Actually, about two weeks ago. This is a really interesting business. It's actually an exchange business for financing small and medium size Chinese companies who typically don't have access to formal credit.

It was actually founded by the former long-time CEO of Hong Kong Exchanged, Giles Lee. So, someone who knows all about exchanges in the region. It's also really flush with cash and unusually, it's already profitable. It's a really interesting model, it takes advantage of the almost entirely digital payments in China, to effectively enforce daily revenue contracts. i.e., they make a loan, they then take a daily slice of the revenue from the borrower directly from their account. So, it's a really neat model. Means they're relatively low risk as cash comes back to you daily from the top of the P&L, direct from the lenders*(sic)* account. That in turn, means that they can charge lower fees, but still generate very high returns. Then these loans can be packaged up and they will eventually be sold on the Micro Connect Exchange. So, it's quite an early-stage business. As I say, it's unusual in that it's already profitable. We think it's backed by some very impressive people and we took just over a 1% position for the trust relatively recently.

So, let's turn to the questions from the audience and I I'll start with "What has surprised you the most during the last year? Either positive or negative within the portfolio and why?"

I guess I was probably surprised the most has actually just been how operationally good the [marker 0:30:00] vast majority of companies in the portfolio have been. Generally speaking, I would say the majority of our holdings have exceeded our expectations in terms of growth. Especially in markets like Vietnam, Indonesia and increasingly, India. That's coupled with the disappointment that that hasn't necessarily been rewarded by the market as much as I would have expected. Especially given the positive macro position that I think we find Asia in today. A couple of reasons for that. I think the market still in incredibly bearish or cautious on China and, also, until recently, you still had a very strong US dollar that is a significant headwind for the region. Now as I say, I think a number of those headwinds are staring to dissipate and in the long-term that better macro positioning of Asia will be richly rewarded.

I certainly think China, given its current valuations is really not being rewarded for any of the growth that it's got and I think certainly for the short to mid-term is well positioned. So that would really be the biggest surprise, positively, has been the performance of the companies. The negative surprise has perhaps been that that hasn't been rewarded yet, in the multiples that people are prepared to Pay.

Good point. That leads onto a number of questions around performance. So medium-term, longer-term performance of Pacific Horizon beating the index, beating the benchmark quite well, very well over the longer-term. "Your enthusiasm has remained unchanged, so why should an investor have confidence that this time you might be right?"

Well firstly I think generally speaking, long-term performance has been very good and indeed, it's been good for many, many years. If you go back, we've been managing the trust for two or three decades so, I think this is a tried and trusted philosophy or process that we haven't changed. Now, over short periods of time, certainly we can be out of step with the market. I think that's all part of being a long-term investor. You want to have a portfolio that is very different and active and that is certainly what you get with Pacific Horizon. We have big positions in the likes or Vietnam that is completely out of index, for example and if you compare us to many other managers, our largest overweight being materials, would look very different. We think that's right over long periods of time, but for 12 to 18 months we can certainly be out of step with the market.

I think it comes back to our overall philosophy for Asia, which is this is a growth market and the best way to gear into that is investing in the fastest growing companies. As I say, growth squared and that's what we've done for many, many years and what we plan to continue doing. As I say, I think Asia looks better positioned really, than it ever has done in the past ten or 20 years. It really is the western markets that are behaving like the emerging markets. Asia is looking much better from a macro perspective and if you're prepared to wait in the medium to long-term, I think that will be richly rewarded, particularly given where valuations are today.

Yes, the valuations would suggest that maybe a rebound might occur. A few questions on China. One viewer asks, "With China growth slowing, are you too overweight in China compared to the rest of Asia?"

In terms of overweight underweights, we wouldn't be overweight China at the moment although we'd be sort of overweight, I suppose, the Chinese consumer and growth. I think this comes back to firstly, investing in individual companies. We're not trying to invest in China for some large macro call, we're investing in it because it's genuinely got some of those innovative companies across Asia currently trading at very cheap valuations. As I say, take Baidu that I mentioned earlier. I think you're getting all the interesting parts of the business for free at the moment and these are in key areas like autonomous driving and AI. Even businesses like Alibaba, you're probably only paying five or six-times PE multiples for the core ecommerce business that generated $30 billion of earnings last year.

So, I think there's some great businesses trading at distressed valuations and there's a lot of this in the price. As I say, I don't think there's going to be some systemic major issue in China. They actually have a pretty strong economy and a lot of room to manoeuvre and if and when they choose to do so, you could see a very significant rerating of a number of those companies over the next 12 to 24 months. I actually think, strangely China, we very long-term investors, our time horizon typically five or ten years. I think China, in some ways, it's actually easier to be positive in the short to mid-term, i.e., over the next three years. The biggest issue for China really comes down to geopolitics, where it seems clear the US is going to continue turning the screw on the country, particularly in key areas of technology such as semiconductors, etcetera.

That's probably the biggest risk for China. I can only see that gradually escalating over the next five, six, seven years. That's probably the biggest cloud for the investment case for China, rather than the outlook for the economy and the individual companies in the long-term.

"What about the political situation in China?" he asks. Well, I think you've covered that. Then he goes on to say, "They are a threat to the democratic west." which is alluding to what you've just been talking about. Is there anymore you can say about that geopolitical overhang?

I think it's complicated, but certainly, it is the biggest long-term challenge. Actually, I don't think it's really what China does or China being a threat to the democratic west. I think actually, if you look at what China's done over the past two or three years, it 's actually been incredibly passive. It really hasn't done anything particularly aggressive outwardly to the US or to any of her allies. I think the bigger issue is really what the US does irrespective of how China behaves. Ultimately, all the indications I see is, they'll keep tightening the screws. We've actually commissioned a lot of work speaking to the DAJ, the Ministry of Defence, with the intelligence services and the financial regulators in the US and the direction is clear. It is to make life more difficult for China, especially in key areas such as semiconductors, AI, quantum computing, military, etcetera. They want to inhibit them here.

Now, the big question for us is okay, they're going to make life more difficult for China, but are they actually going to make China simply uninvestable for say, US or western investors? There, I think that's unlikely. All our work suggests there are so many competing forces. Congress and the Senate make like to do so, but the administration less so. Big business is dead against that. It's also a hugely complicated task how you go about enacting such [unclear 0:38:24]. The trajectory is clear and negative, but it stops short of any real drastic action. I don't actually think there's much China can do about this. Politically, it works in he US across the political divide to be a China bear. So, I think the policies will continue to tighten around China. Which at the same time, for investors actually gives a lot of individual opportunities.

If you can find areas where China needs to be self-sufficient, it is and will continue to double down in those areas. So, companies like Synergy, that I mentioned earlier, where China needs to be able to get its own indigenous semiconductors, they should probably do very well over the next five to ten years. Overall, that is the biggest headwind that China faces and I don't see that disappearing.

Some questions on India now, if we could turn your attention back to there. There's a question about Hong Kong. This is quite an interesting one, I think before we get onto India. "What is your view on Hong Kong stocks and in particular, on the reducing liquidity pattern experienced there?"

So, we've got relatively little exposure to Hong Kong. It's really Tektronix, which is actually a tool manufacturer, really exposed more to the US than Asia and a couple of other smallish holdings, but it's [marker 0:40:00] an area where we find limited investment opportunities. That's really got very little to do with the big macro calls in Hong Kong. It's simply that we have a very strong growth hurdle for any companies that we invest in. We want to be able to at least double our money over a five-year time horizon from companies being able to grow. So, we really want earnings of a minimum of 15% to 20% per annum and we simply don't find many of those in Hong Kong today. Particularly relative to other areas like Vietnam or Indonesia. So, our underweight position to Hong Kong really is stock specific if you like.

The broader positioning of Hong Kong, I think it's certainly had a challenging period, but ultimately, it's very clear that China needs Hong Kong to be a functioning entity. Remember, China has a closed capital account and there is no way I see them wanting to end that over the next ten or 15 years. Therefore, they need Hong Kong to access the international markets. So, it certainly still holds an important strategic position. So, I think the overall financial space and economics of Hong Kong will be reasonable, but it's struggling to find decent stock ideas there. In terms of liquidity, I think you're seeing issues with the types of company in Hong Kong not being that attractive and, also, the number of international investors having issues with China and therefore, being less willing to invest, so liquidity is coming down.

I'll turn to India now. "Do you find better opportunities in large-caps like banks or smaller, more innovative companies?" and I'll run that alongside "What is your view on India banks?" So large-caps, banks, and smaller companies please.

In terms of the market-cap for India, we're really invested across the spectrum. You know, we've got holdings in some of the largest companies in India like Reliance, which is a couple of hundred billion dollars, right down to very small companies like Skipper which would be less than $100 million when we first took our holding. So generally speaking, we find opportunities across the spectrum. I suppose over the past 12, 18 months, probably slightly more opportunities in the small and mid-cap space. Generally speaking, agnostic to the market-cap, it's where we find the opportunities and that's across the spectrum if you will. In terms of the banking sector itself, I think it's got probably one of the most attractive private banking sectors across the emerging markets.

Effectively, you have an industry which is 70% or so, controlled by state-owned banks, the majority of which are terrible. I would say they are culturally bankrupt and very poor at lending. That has meant that the private sector banks have been able to take a 1% or 2% share every year from the public sector banks, which means that they can grow significantly more than the industry in a market that is fundamentally underbanked with low loans to GDP. So, you've got very strong growth with a massive competitive advantage against most of the industry, which I think makes the private banks very attractive and, actually, not particularly expensive at the moment. The likes of HTFC Bank, arguably the highest quality bank in India and you're not paying much more than two times price to book for. So overall, I think the financial space, the private sector banks in India are very attractive. I would be very cautious about investing in any of the state-owned banks in the country.

We focused in China's tensions with the US, "What happens if there's a war between China and India?"

Well, I suppose, always difficult to judge the hypothetical. Depends on the scale of the war or what caused it, who was at fault? Clearly, any significant military action between the two countries would be very serious. You're talking about two nuclear powers in a part of the world where that would have serious ramifications. So not knowing what would be the cause of that war, ultimately, I should think it would be very bad for markets and you would probably see geopolitical tensions rise to very, very high levels. So no, it would be a very serious event which I should think would be hugely damaging for stocks across the region. That's the best that I could say.

Fair enough. Last question relating to Japan, which you don't invest in, obviously. "What effect do you think Japan's changing approach to the yield on Japanese government bonds will have on the region?" Perhaps you could explain some of the context to that question as well.

I think it's difficult to have a strong view on that. In particular, it's not clear how strongly and for how long Japan will push its new monetary policy for. So, I think I would probably take a wait and see approach to how that develops before giving a firm answer. It's an area I'd probably keep an eye on, but wouldn't have any firm conclusions at this stage.

Any other comments around the use of borrowing by Pacific Horizon?

The trust is currently ungeared at the moment. Took the gearing off probably 18, 20 months ago. So currently ungeared. In the long-term our strong view is that Asia is a growth region and that we probably want to be geared into that. So, it probably makes sense to have some borrowing in the trust. I suppose it's just a matter of timing and yields where they are, you're probably paying for US debt at the moment 5% plus a spread. So, it's probably 6% or 7% to borrow for the trust. It's not quite as attractive as it was a couple of years ago. So, no gearing at the moment, but long-term my view is that you probably want to have some gearing, given the growth one is hoping for from Asia.

Give us a quick summary of conclusion to leave us with before we go.

The conclusion is that we remain very positive on the Asian region, particularly compared to developed markets. I don't think Asia has looked any better. It has behaved far more orthodox than western markets. I think that will be rewarded over the next few years and given the growth we're expecting from areas such as the rising consumer, technology and innovation and the green transition, there are lots of exciting opportunities. Rarely would we be paying such a discount for the growth that we're seeing across the region. So overall, very optimistic and if Asia is going to perform, it will be within the next five years. So are a bit better and I'm very positive on the trust and the region as it stands today.

Thanks very much for summing up and thanks very much for being with us today. That's all we've got time for, but thanks again to Roddy and to you for your time and all your questions. I hope today's session's been useful for you, it's certainly been an eye-opener to me on the valuation opportunity in Asia at the moment.

Annual Past Performance to 31 June Each Year (Net %)

	2019	*2020*	*2021*	*2022*	*2023*
Pacific Horizon Investment Trust	*-8.9*	*46.0*	*77.5*	*-27.9*	*-11.4*
MSCI All Country Asia Ex Japan Index	*3.6*	*5.0*	*25.3*	*-14.4*	*-5.2*

Source: Morningstar, MSCI. Share price, total return in sterling.

Past performance is not a guide to future returns.

The specific risks associated with the trust include:

- *The Trust invests in overseas securities. Changes in the rates of exchange may also cause the value of your investment (and any income it may pay) to go down or up.*
- *The Trust invests in emerging markets where difficulties in dealing, settlement and custody could arise, resulting in a negative impact on the value of your investment.*
- *The Trust invests in China, often through contractual structures that are complex and could be open to challenge, where potential issues with market volatility, political and economic instability including the risk of market shutdown, trading, liquidity, settlement, corporate governance, regulation, legislation and taxation could arise, resulting in a negative impact on the value of your investment.*
- *The Trust's risk could be increased by its investment in private companies. These assets may be more difficult to sell, so changes in their prices may be greater.*
- *The Trust can borrow money to make further investments (sometimes known as "gearing" or "leverage"). The risk is that when this money is repaid by the Trust, the value of the investments may not be enough to cover the borrowing and interest costs, and the Trust will make a loss. If the Trust's investments fall in value, any invested borrowings will increase the amount of this loss.*
- *The Trust can buy back its own shares. The risks from borrowing, referred to above, are increased when a trust buys back its own shares.*
- *Market values for securities which have become difficult to trade may not be readily available and there can be no assurance that any value assigned to such securities will accurately reflect the price the Trust might receive upon their sale.*
- *The Trust can make use of derivatives which may impact on its performance.*
- *Share prices may either be below (at a discount) or above (at a premium) the net asset value (NAV). The Company may issue new shares when the price is at a premium which may reduce the share price. Shares bought at a premium may have a greater risk of loss than those bought at a discount.*
- *The aim of the Trust is to achieve capital growth. You should not expect a significant, or steady, annual income from the Trust.*

Further details of the risks associated with investing in the Trust, including a Key Information Document and how charges are applied, can be found in the Trust specific pages at www.bailliegifford.com, or by calling Baillie Gifford on 0800 917 2112.