
The Governance of China Investment Corporation on Its Way to Becoming a Sophisticated Institutional Investor

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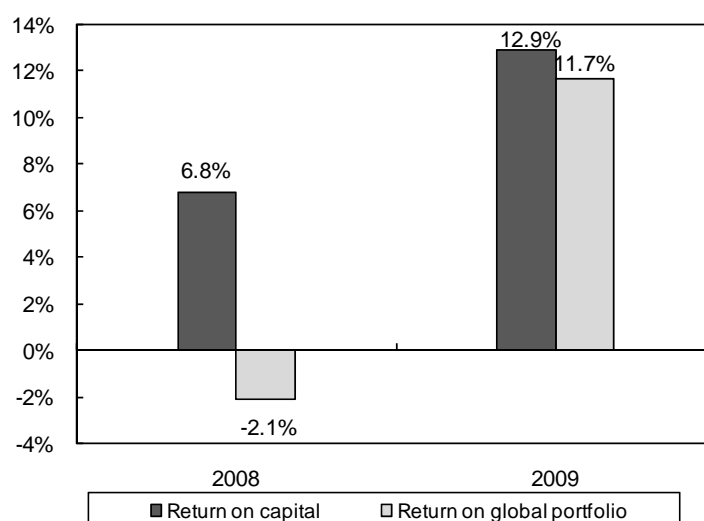
I. CIC's investment performance in 2009

1. Year-on-year performance improves in 2009

On 29 July 2010 China Investment Corporation (CIC) published its annual report for 2009. Established on 29 September 2007 independently of the People's Bank of China and with the aim of diversifying China's foreign exchange reserves and obtaining a long-term return, CIC is a sovereign wealth fund with \$200 billion to invest both at home and abroad.

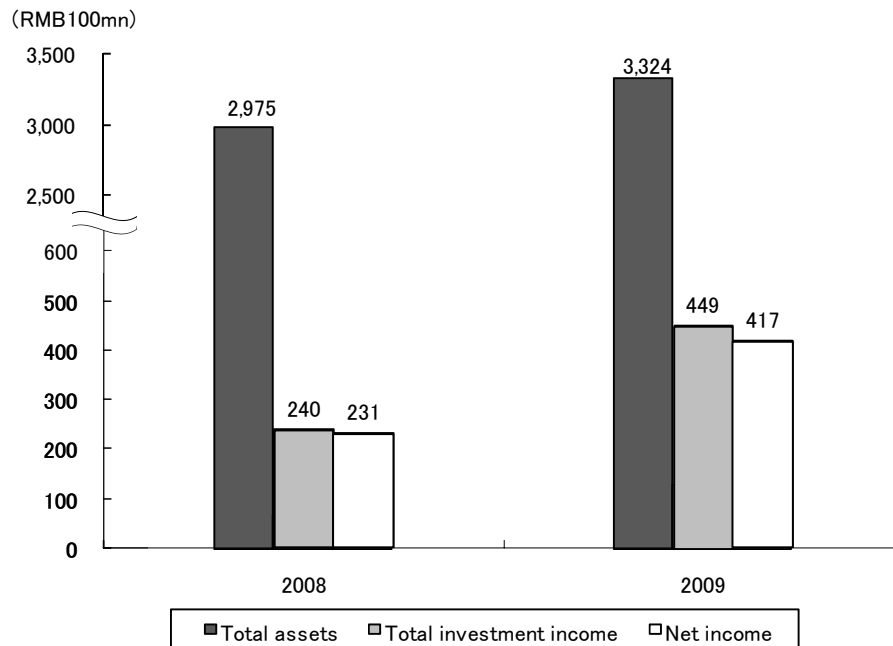
In 2009 it achieved a return of 11.7% on its overseas investments (compared with – 2.1% in 2008) and an overall return on equity of 12.9% on its overseas and domestic investments (the latter consisting of investments in domestic financial institutions) combined (compared with 6.8% in 2008) (Figure 1). Its investment performance was therefore better in 2009 than in 2008.

Figure 1: CIC's investment performance



Source: Nomura Institute of Capital Markets Research, based on CIC's annual report for 2009

Figure 2: CIC's key financial indicators



Source: Nomura Institute of Capital Markets Research, based on CIC's annual report for 2009

As a result, CIC's total assets increased from \$297.5 billion in 2008 to \$332.4 billion in 2009, while its return on investment increased from \$24.0 billion to \$44.9 billion, and its net income from \$23.1 billion to \$41.7 billion (Figure 2).

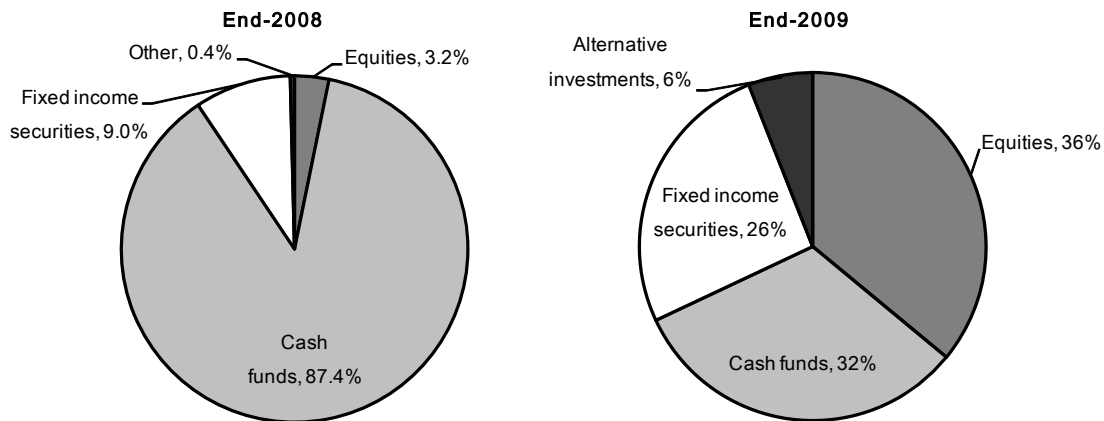
2. Portfolio has been diversified

In achieving this performance, CIC timed its investments carefully. In 2008, it eschewed new investments and cashed in its existing ones as the global economy was dragged down by the financial crisis. In 2009, however, it began to step up its investments in May after the global financial system had shown signs of stabilizing in the first quarter and after efforts to shore up domestic financial institutions and stimulate the economy had begun to bear fruit.

As a result, CIC made \$58.0 billion of new overseas investments in 2009 as a whole¹. Its approach to new overseas investments has had two distinct features. One has been to diversify its portfolio by investing in publicly traded equities and bonds around the world. The other has been to invest directly in leading companies in the fields of infrastructure and clean/renewable energy.

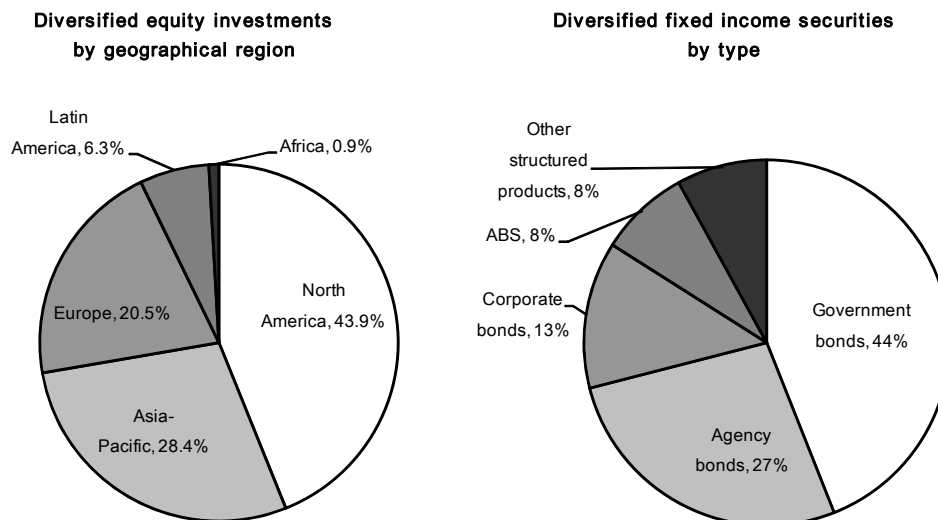
¹ For more information on CIC's investments in 2009, see Sekine, Eiichi, "China's Foreign Exchange Reserves and China Investment Corporation's Steps towards Diversifying How It Manages Them," Nomura Journal of Capital Markets, Winter 2009, Vol.1, No.4 and Sekine, Eiichi, "Shigen/Enerugii o Chuushin ni Kasoku suru Chuugoku CIC no Kaigaitoushi" [CIC's Growing Investments Overseas, Especially in Resource and Energy Companies], Kikan Chuugoku Shihon Shijou Kenkyuu, Winter 2010 (Japanese only).

Figure 3: Breakdown of CIC's global portfolio



Source: Nomura Institute of Capital Markets Research, based on CIC's annual report for 2009

Figure 4: Breakdown of CIC's global portfolio (diversified investments)



Source: Nomura Institute of Capital Markets Research, based on CIC's annual report for 2009

As a result, CIC's global portfolio underwent a major change between 2008 and 2009. For example, its cash position declined from 87.4% to 32%, while equities increased from 3.2% to 36% and bonds from 9% to 26% (Figure 3). At the same time, its global equity portfolio (excluding direct investments) was 43.9% invested in North America, 28.4% invested in the Asia-Pacific region, 20.5% invested in Europe, 6.3% invested in Latin America, and 0.9% invested in Africa (Figure 4) while its global fixed income portfolio was 44% invested in government bonds, 27% invested in agency bonds, 13% invested in corporate bonds, 8% invested in asset-backed securities, and 8% invested in other structured products (Figure 4). Its main direct investments are listed in Figure 5.

Figure 5: CIC's main direct investments (2009)

Company	Contract month	Amount of investment (\$mn)	Type of investment	Sector	Approximate initial ownership %
Teck Resources (Canada)	July	1,500	Class B subordinate voting shares	Mining and mineral development	17.2%
JSC KazMuna Exploration Production (Kazakhstan)	July	940	Global depositary receipts	Oil and gas	10.6%
Nobel Oil Group (Russia)	September	270	Equity acquisition	Oil and gas	45.0%
PT Bumi Resources (Indonesia)	September	1,900	Private debt	Thermal coal production	-
Noble Group (Singapore)	September	858	Common stock	Resources	14.9% of outstanding shares on an undiluted basis
SouthGobi Resources (Canada)	November	500	30-year secured convertible debenture	Coal mining and exploration	-
AES Corporation (US)	November	1,581	Common stock	Power generation	15.0%
GCL-Poly Energy Holdings (Hong Kong)	November	717	Common stock	Renewable energy	20.1% on a fully-diluted basis

Source: Nomura Institute of Capital Markets Research, based on CIC's annual report for 2009

3. Changes to CIC's governance and personnel systems contribute to performance

CIC's annual report for 2009 points out that CIC's better performance in 2009 was the result not only of its more aggressive investment stance but also of changes to its governance and personnel systems.

We therefore now take a closer look at what the report says about CIC's investment management process, risk management, personnel system, and human resource development, especially the changes that were made in 2009. Some of this information was previously available on CIC's website.

II. CIC's investment management process

1. Investment management prerequisites

1) CIC's organizational structure

(1) Legal status

CIC was established on 29 September 2007 as a wholly state-owned company incorporated in accordance with China's Company Law². It was initially capitalized with \$200 billion in reserves purchased from the People's Bank of China in exchange for RMB1,550 billion in government bonds issued by the Ministry of Finance, which is therefore a key stakeholder. Of the \$200 billion in registered capital, slightly over

² For further details of the arguments for and against the establishment of CIC, see Sekine, Eiichi, "China Seeks to Actively Invest Foreign Exchange Reserves," Nomura Capital Market Review, Winter 2007, Vol.10, No.4.

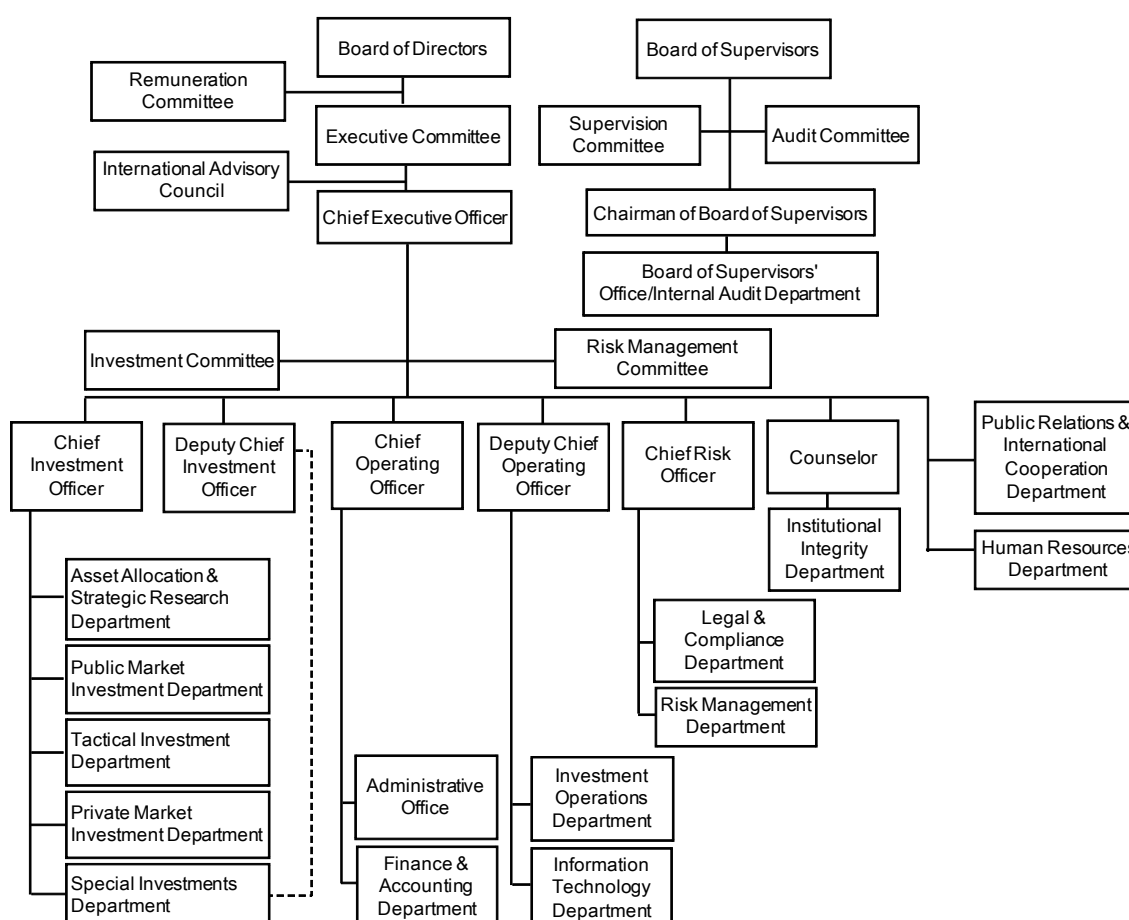
50% was allocated to global investment. The balance is invested in domestic financial institutions by CIC's subsidiary, Central Huijin Investment Ltd. (Central Huijin).

Central Huijin was established in December 2003 to inject public funds (in the form of foreign exchange reserves) into China's state-owned commercial banks. The People's Bank of China is therefore another key stakeholder. The global investment activities of CIC and the domestic investment activities of Central Huijin are operationally completely separate, with strict firewalls between them.

(2) Thinking behind CIC's organizational structure

Under China's Company Law, CIC is required to have a board of directors and a board of supervisors (Figure 6). Based on objectives and broad policy set by its shareholder, China's State Council, the Board of Directors decides CIC's development strategy, management policies, and investment objectives. Responsible for monitoring the ethical behavior of directors and executives as well as the effectiveness of supervisory procedures within the company, the Board of Supervisors reports directly

Figure 6: CIC organizational chart



Source: Nomura Institute of Capital Markets Research, based on CIC's annual report for 2009

to the shareholder. It also has its own secretariat.

Directors are appointed by the State Council. The chairman of the Board of Supervisors is appointed by the State Council from among the board's members. There are 11 directors, five of whom come from the State Development and Reform Commission, the Ministry of Finance, the Ministry of Commerce, the People's Bank of China, and the State Administration of Foreign Exchange (SAFE). The current chairman (chief executive officer) comes from the Ministry of Finance, the vice chairman (president and chief investment officer) comes from the China Securities Regulatory Commission (CSRC), and the executive vice president (chief operating officer) also comes from the Ministry of Finance.

Figure 7: Members of CIC's Executive Committee

Committee members			
Title	Name	Date of birth	Education & career
Chairman & Chief Executive Officer	Lou Jiwei	1950	MA in economics, professor. PhD supervisor, Director General of the Macroeconomic Control Department of the State Commission for Restructuring the Economic Systems, Deputy Governor of Guizhou Province, Executive Deputy Minister of Finance, Deputy Secretary General (ministerial level) of the State Council.
Vice Chairman, President & Chief Investment Officer	Gao Xiqing	1953	LLD, professor, PhD supervisor. General Counsel and the Director General of the Public Offering Supervision Department, Deputy Chairman and Chief Executive Officer of the Bank of China International (Holdings) Limited, Deputy Chairman at the China Securities Regulatory Commission, Deputy Chairman of the National Council for the Social Security Fund.
Chairman of Board of Supervisors	Jin Liquan	1949	Graduate student of economics. Executive Deputy Director of China to the World Bank Group, Director General of the World Bank Department at the Ministry of Finance, Deputy Minister of Finance, member of the Monetary Policy Committee of the People's Bank of China, Vice President (Operations 1) of the Asian Development Bank (ADB).
Executive Director, Executive Vice President & Chief Operating Officer	Zhang Hongli	1950	PhD in economics. Deputy Director General of the Department of Education, Science and Culture, Director General of the Budget Department, Deputy Minister of Finance.
Executive Vice President	Peng Chun	1962	PhD in economics. Branch president of the Bank of Communications in Urumqi, Nanning and Guangzhou, Assistant to the President, Executive Vice President, and Executive Director of the Bank of Communications, currently Director and President of Central Huijin.
Executive Vice President & Deputy Chief Operating Officer	Fan Yifei	1964	PhD in economics. General Manager of the Finance and Accounting Department, General Manager of the Planning and Finance Department, Assistant to the President, and Executive Vice President of China Construction Bank.
Executive Vice President & Deputy Chief Investment Officer	Xie Ping	1955	PhD in economics, professor, PhD supervisor. Deputy Director General of the Policy Research Office, Director General of the Non-Banking Supervision Department, President of the Hunan branch, Director General of the Research Bureau, and Director General of the Financial Stability Department of the People's Bank of China, Chairman of Shenyin & Wanguo Securities Co. Ltd., President of Central Huijin.
Executive Vice President & Chief Risk Officer	Wang Jianxi	1951	PhD in accounting, PhD supervisor. Chief Accountant and Director General of the International Department at the China Securities Regulatory Commission (CSRC), Chief Financial Officer and Executive Vice President of the Bank of China International, President of the Bank of China International (UK), Assistant Chairman of CSRC, Deputy Chairman of Central Huijin, Chairman of China International Capital Corporation.
Counselor & Member of the Executive Committee	Liang Xiang	1955	BEng. Deputy Director of Planning Institution of Chemical Industry, Deputy Director of Planning Department at the Ministry of Chemical Industry, General Manager of the Second Credit Department, the Buyer Credit Department, the Export Credit Department, Assistant President, and Secretary of the Discipline Inspecting Commission in the Export-Import Bank of China.

Source: Nomura Institute of Capital Markets Research, based on CIC

Under the Board of Directors is an Executive Committee (with currently nine members, Figure 7), which is responsible for carrying out the Board of Directors' decisions as well as for CIC's day-to-day operations, with authority to make required operating decisions. Under the Executive Committee is an Investment Committee and a Risk Management Committee. The names and careers of all the members of the Board of Directors, the Board of Supervisors, and the Executive Committee are posted on CIC's website. Central Huijin has a separate board of directors, a separate board of supervisors, and a separate management and organization structure.

2) CIC's investment principles and strategy

(1) Investment principles

According to CIC's annual report for 2009, its investment principles are as follows.

First, CIC invests on a commercial basis. Its underlying investment objective is long-term, sustainable and risk-adjusted returns for its shareholder.

Second, CIC is a financial investor. As such, it does not seek to control any company.

Third, CIC is a responsible investor which abides by local laws and regulations in the countries in which it invests, and exercises its corporate social responsibility consciously.

(2) Investment strategy

CIC defines its investment strategy as follows.

First, CIC's investments are research-driven and allocation-driven.

Second, CIC has based its investment approach and benchmark portfolio structure on its mandate and unique circumstances, the risk tolerance of its shareholder, its assessment of market conditions and policies established by its board of directors. In addition, CIC also has learned from the experience of other sovereign wealth funds, university endowment funds and pension funds, and consults with investment professionals globally.

Third, CIC's benchmark portfolio consists of cash funds, equities, fixed income securities and alternative investments. CIC's investments are not limited to any sector, geography or asset class.

CIC's articles of incorporation state that it may (1) invest in foreign currency financial products such as domestic foreign currency bonds, (2) invest in financial products such as overseas bonds, equities, investment trusts and financial derivatives, (3) invest in domestic and overseas equities, (4) employ overseas fund managers, (5) provide loans through entrusted financial institutions, (6) act as a custodian of foreign exchange reserves, (7) establish equity investment funds and fund management

companies, and (8) engage in any other business approved by the relevant government departments.

2. Role of the various departments involved in the investment decision-making process

1) Role of the Asset Allocation and Strategic Research Department

The Asset Allocation and Strategic Research Department (Figure 6) develops a strategic asset allocation (SAA) plan, which has to be approved by the Board Of Directors after being reviewed and approved by the Executive Committee. It also develops a tactical asset allocation (TAA) plan, which it presents every quarter for review by the Executive Committee.

The SAA seeks to strike a balance between absolute return and relative return objectives, taking into consideration diversification requirements, risk profiles, benchmarked returns and deviations, as well as market opportunities. The TAA allocates risk, return expectation and liquidity across asset types.

The TAA includes professional portfolio management techniques such as portfolio optimization and rebalancing mechanisms, as well as currency overlay strategies³. It is research-driven, quantitatively constructed and professionally executed.

The department also serves as the secretariat of the Investment Committee (see below). In addition, the department conducts research on various issues such as strategy and policy, markets and industries, and product research, as well as portfolio analysis, including performance measurement, risk/return attribution, and stress testing.

2) Role of Investment Committee

The Investment Committee is responsible for CIC's investments (Figure 6). The committee sets investment strategies and policies within guidelines approved by the Board of Directors and the Executive Committee, and reviews and approves every investment proposal and external manager's mandate. It has 12 members with CIC's chairman/CEO as chairman (Figure 8).

All investments and mandates must be reviewed, deliberated on and approved by the Investment Review Committee chaired by the chief investment officer before being submitted to the Investment Committee for approval. The committee meets weekly or more frequently when needed.

³ This involves managing the currency element of a foreign currency asset separately from the underlying asset.

Figure 8: Investment Committee

Chairman	Chairman & Chief Executive Officer
Deputy Chairman	President & Chief Investment Officer
Members	Vice President & Chief Operating Officer, Vice President & Deputy Chief Operating Officer, Vice President & Deputy Investment Officer, Vice President & Chief Risk Officer
	Heads of Asset Allocation & Strategic Research Department and Risk Management Department
	Heads of Public Market Investment Department, Tactical Investment Department, Private Market Investment Department, and Special Investments Department

Source: Nomura Institute of Capital Markets Research, based on CIC's annual report for 2009

3) Function and role of investment departments

Based on decisions made by the Investment Committee, investments and mandates are managed by four investment departments. Each formulates investment proposals based on sound research within the context of the overall portfolio and risk management framework, and builds and manages its portfolios.

Each also recruits external fund managers. Other departments (namely, the Asset Allocation and Strategic Research Department, the Risk Management Department, and the Legal and Compliance Department) are also involved in recruiting and evaluating external fund managers. The functions and roles of the investment departments are as follows.

(1) Public Market Investment Department

This department implements traditional beta strategies. It is responsible for investing in public market equities, fixed-income products, commodities, and currencies as well as cash management. Investment activities are carried out by five teams: Developed Market Equities, Emerging Market Equities, Interest Rate and Cash Management, Credit Investment, and Commodities and FX Hedging. The department makes extensive use of external managers, which invest the majority of the portfolio.

(2) Tactical Investment Department

This department manages proprietary portfolios and outsourced liquid absolute-return portfolios. The department manages three global proprietary portfolios internally (a hedged global equity portfolio, a long only value style portfolio and a

multi-asset portfolio) and two liquid absolute-return investment portfolios (directional and non-directional⁴) utilizing external hedge fund managers.

(3) Private Market Investment Department

This engages in private equity investment through external managers, co-investment vehicles, partnerships and separate accounts. The department is also responsible for real estate and infrastructure investments. It is comprised of four investment teams. The Private Equity Team invests in PE funds directly and through co-investment vehicles. The Real Estate Team invests in publicly traded REITS and direct property investments. The Infrastructure Team and the Credit Opportunities Team invest through external managers.

(4) Special Investments Department

This department makes and manages, on an in-house basis, direct large-scale investments with concentrated positions over longer time horizons.

3. Investment department reforms of 2009

According to its annual report for 2009, CIC continued to strengthen its investment management infrastructure and platform in that year. A Senior Operations Infrastructure Development Steering Committee, chaired by the chief executive officer and comprised of the chief operating officer and major department heads, was formed to oversee projects to strengthen the investment management platform. This company-wide initiative produced several key results in 2009:

First, streamlining and strengthening the investment approval process by standardizing procedures across all investing units and creating an enhanced review process by a new Investment Review Committee chaired by the chief investment officer.

Second, creating an investment operations department to strengthen coordination among different units along the investment process, enhance investment back-office capabilities, improve efficiency, strengthen internal control and better address pre-close and post-close compliance controls and data management issues.

Third, developing CIC's proprietary trading infrastructure and better integrating the proprietary trading, investment operation and accounting, risk analytics and general

⁴ A "directional" approach is a top-down approach that analyzes economic and financial fundamentals and seeks to take advantage of price anomalies arising from political and economic changes at national and regional levels.

Figure 9: Risk Management Committee

Chairman	Chairman & Chief Executive Officer
Deputy Chairman	Vice President & Chief Risk Officer
Members	Vice President & Chief Operating Officer
	Heads of Risk Management Department, Legal & Compliance Department, Asset Allocation & Strategic Research Department
	Heads of Public Relations and International Cooperation Department, Finance & Accounting Department, Internal Audit Department, Administrative Office

Source: Nomura Institute of Capital Markets Research, based on CIC's annual reports for 2009

ledger systems to create a more rigorous straight-through processing (STP)⁵ environment.

On 7 November 2010 CIC announced that it had established a wholly-owned subsidiary in Hong Kong (CIC International (Hong Kong) Co., Limited) and appointed Professor Lawrence J. Lau, a former vice chancellor of the Chinese University of Hong Kong and a former member of CIC's International Advisory Council, to be its first chairman.

III. Risk management

1. Risk Management Committee

CIC also attaches great importance to risk management. It therefore has a Risk Management Committee (Figure 6) with the same status as its Investment Committee. It has 10 members with CIC's chairman/CEO as chairman (Figure 9).

The committee is responsible for devising and implementing CIC's risk management strategy in accordance with the investment policies and risk limits set by the Board Of Directors and the Executive Committee. Its main responsibilities are setting company-wide risk strategy, defining risk management policies, determining exposure thresholds, reviewing and finalizing reports concerning risk management, and establishing risk control evaluation criteria. The committee also has overall responsibility for overseeing and controlling CIC's strategic, financial and operational risks.

⁵ Straight-through processing allows all the data needed to settle a trade (ranging from confirmation to matching, clearing and settlement) to be processed automatically as a seamless stream of electronic data by transmitting it in a standardized format between interoperable systems without the need for manual intervention, thereby increasing efficiency and reducing operational risk and cost.

The committee meets once a quarter or more frequently if needed. The investment departments may attend the committee's meetings if necessary.

2. Role and function of Risk Management Department

1) Function and role of each department with regard to risk management

CIC has developed a comprehensive risk control system to manage market, credit, sector, country, and currency exposure. Risk indicators are also developed and monitored for each external investment manager. CIC utilizes an internationally accepted risk management system as its risk analytic and reporting backbone. Positions are monitored using this system, and comprehensive risk management reports are produced weekly, monthly and quarterly for management review.

Organizationally, the Risk Management Department and the Legal and Compliance Department report to the chief risk officer. Investment risk, including credit, market, liquidity and operating risk, is managed by the Risk Management Department. The department reviews and comments on every investment and external manager mandate proposal. In addition, it participates in the calculation of risk-adjusted performance, assists in the evaluation of internal and external investment managers, and monitors risk performance.

Within the Legal and Compliance Department, the legal team focuses on the development and review of contracts and the management of legal risk. The department's compliance team is charged with the responsibility of ensuring that CIC complies with investment and related laws and regulations of the markets in which it invests as well as its own rules. Reputation risk, country risk, policy risk and other non-commercial risks are addressed by the Public Relations and International Cooperation Department.

2) Cooperation with the Asset Allocation and Strategic Research Department

The Risk Management Department works closely with the Asset Allocation and Strategic Research Department in implementing CIC's risk management system.

"Risk Budgets" for each asset class are developed by the Asset Allocation and Strategic Research Department. The Risk Management Department then sets appropriate risk limits based on these risk budgets. It meets monthly with each investment department to discuss investment strategy, risk developments and other investment risk management issues. Informal discussion and consultation are conducted on a more frequent basis as needed.

3. Improvements to risk control processes in 2009

CIC's annual report for 2009 describes the following improvements that CIC made to its risk control processes in that year.

Figure 10: CIC staff backgrounds

As at end-2009

	Total	Advanced degrees	Overseas work experience	Overseas education	Overseas citizenship
Number	246	199	115	132	31
%	100%	81%	47%	54%	13%

(Compare: end-May 2009)

	Total	Advanced degrees	Overseas work experience	Overseas education	Overseas citizenship
Number	194	184	73	85	18
%	100%	95%	38%	44%	9%

Source: Nomura Institute of Capital Markets Research, based on CIC's annual reports for 2008 and 2009

First, it established an Operating Risk Group within its Risk Management Department.

Second, it implemented a new internal control function throughout the organization. Every departmental unit has identified an internal control representative responsible for identifying and monitoring operating risks within its department. The process is managed by the Internal Control Team, which is part of the Operating Risk Group within the Risk Management Department.

Third, it increased the focus on managing operating and credit risk with clearing banks and custodians.

IV. Personnel system and human resource development

1. Commitment to recruit staff with international experience

CIC requires its international recruits to be talented individuals with (1) plenty of experience of the main international financial markets and (2) an understanding of the Chinese perspective, culture and language. CIC has no restrictions on nationality. For those it recruits internationally, CIC requires a minimum of six years of relevant international experience. All candidates must apply through its on-line application system, which includes subject matter testing in Chinese. All applicants completing that process successfully are interviewed personally, and candidates above the senior staff level meet individually with each member of the senior management team.

During 2009 CIC's staff grew from 148 at the start of the year to 194 at 31 May and 246 at December 31 (Figure 10). Over the year it recruited about 100 new staff. Quite apart from the increase in the number of its staff between May and December

2009, CIC recruited more staff who had either worked or studied abroad or were non-Chinese nationals. About half of its employees have overseas work or education experience or both. 94% of the 83 staff in its investment departments have an advanced degree (masters or above); 78% have received at least part of their education overseas; and 77% have overseas investment experience.

2. Staff evaluation

CIC has developed a comprehensive evaluation system to both reward performance and to aid in defining training and development requirements for each employee.

Staff are evaluated on a 360-degree basis, with input by peers and subordinates as well as supervisors. Evaluation is not only annual but also upon completion of major tasks and projects. Bonuses, annual pay increases and promotions are tied to the outcome of the performance evaluation.

3. Staff training

CIC places great emphasis on the development of its people and has invested in an extensive training program. The goal of the program is to develop not only the deep skills required for an individual's assignment, but also a broad understanding of CIC's business across markets and products and a "sense of the market" in all its people. Each employee has an annual training plan which is based on a formal skill assessment as well as input from the performance evaluation system.

Each employee is required to undergo 80 hours of formal training each year. Training is conducted at three levels: company-wide by the Human Resources Department, at the departmental level, and at the individual level.

In addition, to build an overall understanding of CIC, staff meetings are held at which senior executives discuss topics such as the role and operations of specific departments, the Santiago Principles⁶, technical issues such as risk management, regulatory developments and compliance, economic developments, company performance and the like.

Extensive use is made of local universities and professional organizations. While most training takes place in China, some overseas programs are arranged for employees as appropriate.

⁶ These are a voluntary code of behavior adopted by sovereign wealth funds in October 2008.

4. Changes to personnel system in 2009

In 2009 CIC made two changes to its personnel system.

First, it implemented a new program to increase hiring of younger professionals from top Chinese and global business and professional schools. Recruits enter a two-year rotation program to allow them to better understand the entire organization, build a broad set of skills and determine where their interests lie so that they can make appropriate career choices.

Second, CIC adopted a new compensation system for all staff comprised of three elements: a basic compensation element, a floating or variable compensation element, which is based on evaluation of behavior and adherence to CIC's core values, and a bonus, which is based on results and achievements. A major objective of this system is to provide appropriate and long-term incentives and strong motivation among all its staff and promote teamwork and harmony across the organization by explicitly recognizing the importance of CIC's values.

On 27 July 2010 CIC conducted a global recruitment campaign for positions in all its departments. Altogether 64 vacancies were advertised. This move was no doubt related to CIC's objective, alluded to in the annual report, of, over time, increasing its level of internally managed portfolios to enhance investment flexibility and reduce investment costs.

V. Conclusion

As we have seen, since its establishment in September 2007, CIC has put in place, and then modified, its investment procedures and risk management system. This process has been one of seeing how an institutional investor such as itself could incorporate a system of checks and balances (Plan – Do – See) in its internal systems. Although CIC is generally seen as a sovereign wealth fund responsible to the State Council and with senior officials from government departments as members of its board of directors and board of supervisors, these efforts to establish a system of governance on a par with that of a private-sector institutional investor should be judged on their own merits.

It is now three years since CIC was established, and it is well on its way to becoming a sophisticated institutional investor. However, we expect it to continue these efforts. The more sophisticated CIC becomes as an institutional investor, the more likely its involvement is to be seen as a kind of investment benchmark. Similarly, employment experience with CIC, be it in one of its investment departments or in a middle or back office function, may become a benchmark for an investment professional's worth. If that happens, CIC's operational model could become a benchmark for other emerging economy sovereign wealth funds. Japan also needs to consider whether its capital markets might benefit if its operational model for its public funds became a benchmark for other emerging economies.

Similarly, as CIC becomes an increasingly important global player, increasing attention has come to be paid to how it exercises its proxy. CIC sees itself as a financial investor, investing solely on a commercial basis⁷. Companies in which it invests may soon have to pay more attention to fostering good investor relations with it. Nor is CIC the only Chinese institution classified as a sovereign wealth fund to invest overseas: others are the National Social Security Fund (with assets totaling RMB776.6 billion as of end-2009) and qualified domestic institutional investors (QDIIs) (with assets under management of \$66.9 billion as of end-September 2010). Japanese companies will probably also need to think about deploying some of their know-how and experience of fostering relations with other institutional investors in their dealings with such mainland Chinese institutional investors.

Furthermore, it has been reported in the Chinese media that CIC has appointed a domestic fund manager as an external fund manager for the first time to manage an MSCI-based fund using H shares and other China concepts stocks via its Hong Kong office⁸. This appointment has been seen by asset managers in both China and overseas as a new opportunity.

CIC's approach to corporate governance and staff development is likely to remain a subject of interest.

⁷ On 31 August 2010 the US Federal Reserve announced that it had approved an application by CIC to acquire up to 10% of Morgan Stanley's voting common stock following CIC's agreement not to exercise or attempt to exercise a controlling influence over Morgan Stanley's management or policies.

⁸ Economic Observer, 19 August 2010 and Oriental Morning Post, 20 August 2010.