CI ASIAN TIGER FUND
QUARTERLY REPORT

Cooper Investors Pty Limited AFS Licence Number 221794 ABN 26 100 409 890

JUNE 2015

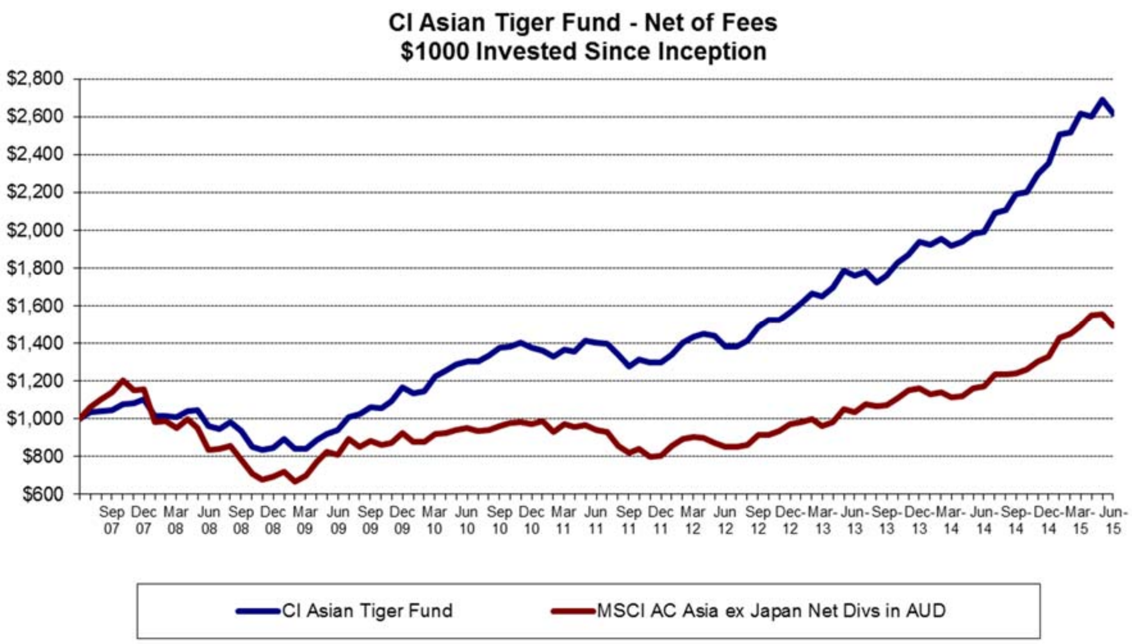
"Peace is not a relationship of nations. It is a condition of mind brought about by serenity of the soul. Lasting peace can only come to peaceful people." Jawaharlal Nehru.

"Water that is too pure has no fish." Ts'ai Ken T'an.

"The true test of one's character is how one handles adversity." W Cheng.

	****PORTFOLIO**	**#BENCHMARK**	**VALUE ADDED**
ROLLING 3 MONTH	0.41%	-0.05%	0.46%
ROLLING 1 YEAR	33.62%	27.52%	6.10%
ROLLING 2 YEAR	23.67%	19.98%	3.69%
ROLLING 3 YEAR	25.69%	20.63%	5.06%
ROLLING 5 YEAR	17.14%	9.49%	7.65%
ROLLING 7 YEAR	17.76%	8.68%	9.08%
SINCE INCEPTION*	14.78%	5.13%	9.65%
SINCE INCEPTION^	201.22%	49.22%	152.00%

*Annualised
^Cumulative (2 July 2007)
**Before fees and expenses
MSCI AC Asia ex Japan Net Divs in AUD



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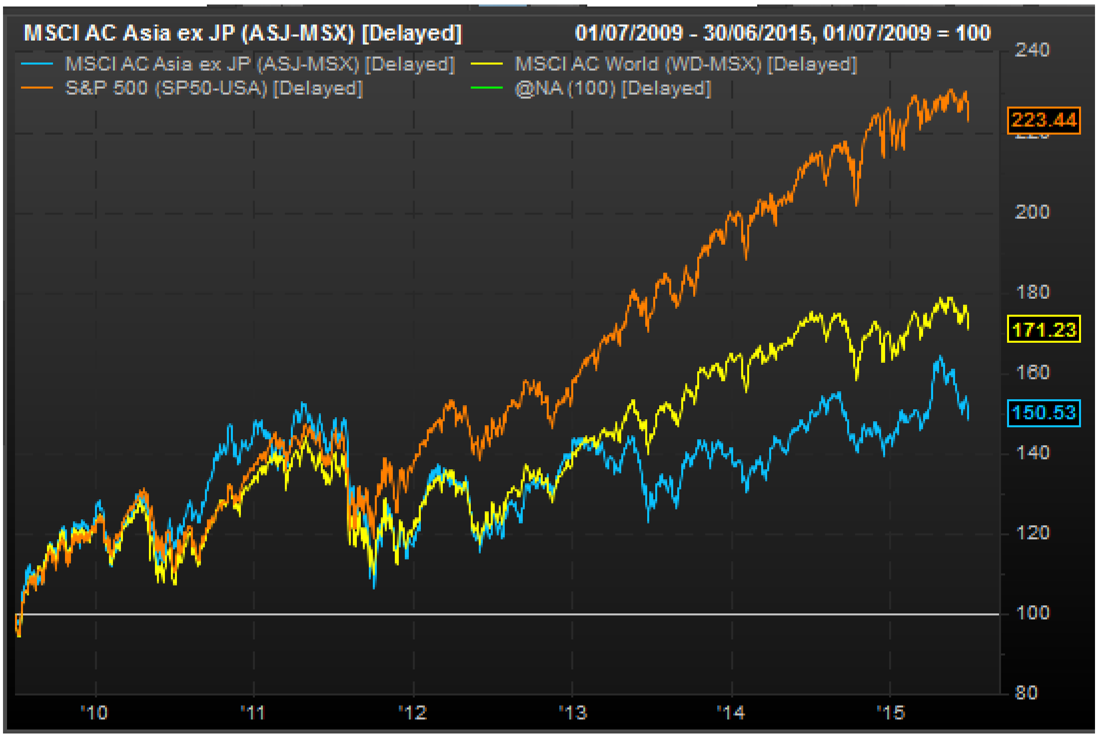
Market and Portfolio Performance

Every year since the Global Financial Crisis (GFC) the Federal Reserve has revised down its official forecast for American GDP (real). It has done so again in 2015, with the official number cut from 2.5% to 1.9%. With growth anaemic in Europe and Japan, it seems hardly surprising that investors are again focussing on Asia. While growth in certain Asian markets has slowed, it remains generally robust by developed market standards. Furthermore, following years of relative underperformance since the GFC (see table below), valuations of many Asian markets compare well with global averages. For example, the Global P/E ratio for 2015 is estimated by JP Morgan at 16.7x, compared with 18.5x in the USA and 13.2x in Asia Pacific ex Japan.



Source: Factset

Over the three months ended June 2015 (impacted by fears of a contagion impact from the ongoing Greek financial crisis) the MSCI AC Asia ex-Japan index was down 0.05% in AUD terms compared with the MSCI AC World Index which fell 0.26% in AUD terms over the same period. The respective figures in AUD terms over the financial year ending June 2015 were gains of 27.52% (Asia) and 23.70% (World). Again there were widely divergent performances from individual Asian markets over the period in question, as highlighted by the table below.

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MSCI Data with Net Dividends	June Quarter 2015 in A$	June Quarter 2015 in local currency	12 months ending June 2015 in A$	12 months ending June 2015 in local currency
AC World	-0.26%	-0.54%	+23.70%	+8.2%
AC Asia Ex Japan	-0.05%	+0.67%	+27.52%	+8.64%
China	+5.40%	+6.03%	+53.02%	+24.65%
Hong Kong	+4.93%	+5.56%	+38.01%	+12.42%
India	-4.20%	-1.92%	+26.80%	+9.33%
Indonesia	-14.60%	-12.39%	+12.38%	+2.92%
Korea	-4.30%	-3.19%	+5.32%	-5.45%
Malaysia	-8.44%	-6.16%	-3.54%	-7.70%
Philippines	-5.53%	-4.13%	+34.33%	+12.99%
Singapore	-0.66%	-1.86%	+18.41%	+3.98%
Taiwan	+0.41%	-0.38%	+26.47%	+6.42%
Thailand	-3.98%	+0.27%	+22.37%	+3.70%

Source: Factset

The performance of Asian stock markets over the last 12 months was demonstrably better than commodity markets. Indeed over the 2014/15 financial year, the gold price fell 11.4%, copper 17.7% and the oil price, despite a rally in the last quarter, 43.6%. Hardly surprisingly, the A$ had a “tough year” against most Asian currencies, which is clearly evident from the above table. We still feel the A$ looks vulnerable to further weakness.

The three best performing Asian markets over the June quarter in A$ terms were China, Hong Kong and Taiwan. All three did very well over the financial year, along with the Philippines and India. In contrast, 7 out of the 10 Asian markets in the benchmark recorded negative returns over the last three months, with the worst being Indonesia and Malaysia. The only Asian market to record a negative return in A$ for the 12 months ending June 2015 was Malaysia, but Korea’s performance in A$ terms was also poor relative to the index.

Hong Kong and China

The Chinese (+5.40%) and Hong Kong (+4.93%) markets remained buoyant over the quarter aided by further policy initiatives to support the market. International investors seem to have been underweight the market, and equity ownership by Chinese households remain comparatively modest. Nevertheless the stock market in China has corrected significantly in the last month and is a timely reminder to investors, that while governments may be able to influence markets they cannot control them. Chinese interest rates were reduced in May, and then again in June, when the Peoples Bank of China cut 1 year deposit rates to 2.00% (from 2.25% in May) and 1 year lending rates to 4.85% (from 5.1% in May). Recent economic statistics have been weak and many people believe the Chinese Government’s official GDP forecast of around 7% for 2015 looks challenging. Nevertheless the Government is clearly focused on “quality over quantity” as it endeavours to move the country from investment to consumption driven growth. We believe there are grounds for optimism, but that it will take longer than is generally expected.

Other positives included the ongoing impact of the Stock Connect programme and further new initiatives such as the decision made by the China Securities Regulatory Commission (CSRC) to allow Chinese

Mutual fund investors with no QDII (Qualified Domestic Institutional Investor) quota to invest in the HK market (via Stock Connect). Interestingly, China A shares still trade at a premium of 29% (10 year average 16%) to their counterparts in HK, albeit this has narrowed in recent times. Going forward a potentially important theme will be whether there is reform to China's major State Owned Enterprises or SOE's. If this occurs and is genuine (as opposed to centralisation of control), it will be very positive for the stock market, which historically has been very dependent on policy driven initiatives for performance. Rumours of SOE consolidation, especially in crucial industries like oil, telecom and transportation abound at the moment. This process would also help in the creation of national champions. Clearly many SOE's and banks in China need recapitalising so the authorities would have been happy with the direction of the market over the last 12 months. That acknowledged, the CSRC has recently tightened regulations relating to margin financing and leveraged equity products as a "bubble market" is in no one's interests.

From an economic standpoint, inflation in China continues to fall and amounted to only 1.2% YOY in May (1.5% YOY in April). Further interest rate declines in China are possible if inflation falls further, but this seems likely to be more challenging from current levels. In contrast, China reduced its RRR to 18.5% (from 19.5%) for the country's major banks in April and further reductions seem probable. Also over the quarter, highlighting ongoing indications of further financial sector liberalisation, China removed the 75% Loan to Deposit ratio requirement for the country's banks.

The long awaited MSCI Market Classification review in respect of China was announced on 15th June 2015. The successful launch of the Stock Connect trading link between HK and Shanghai (November 2014) prompted some market observers to expect China A shares to be included in the MSCI's Emerging Markets index. Nevertheless, despite genuine progress on reform and the further opening up of Chinese equity markets, the MSCI decided to defer a decision for the moment. However, the MSCI continues with its plan for a 5% partial inclusion (May 2017) of A shares into the MSCI Emerging Markets index. To this end it continues to liaise with the CSRC on this matter. Areas of outstanding concern for the MSCI, and major global investors, are the further liberalisation of the quota allocation system, capital mobility restrictions and more clarification on the beneficial ownership of investments. Clearly it is a matter of "when rather than if" China A shares are included in the MSCI Emerging Markets index and the effect will be significant. Currently China accounts for 25.3% of the Emerging Markets index, but this lifts to 30% with a 5% inclusion of A shares and Chinese ADR's, and a very significant 43.6% on potential full inclusion of China A at a "future point in time".

McKinsey Global Institute released a report earlier in the year entitled "Debt and (not much) Deleveraging", which is well worth reading. This report highlighted that World debt (household/corporate/ government/financial) has not fallen post the Global Financial Crisis, but has in fact increased, from US$142tr (269% of GDP) in 2007 to US$199tr (280% of GDP) in 2014. The same report highlighted that over the same period China's debt has risen from US$7.4tr (158% of GDP) to US$28.2tr (282% of GDP). In China, McKinsey found three areas of particular concern: "the concentration of debt in real estate, the rapid growth and complexity in shadow banking and the off balance sheet borrowing by local governments". Furthermore, McKinsey estimated "that nearly half of the debt of Chinese households, corporations and governments is directly or indirectly related to real estate". This is potentially a source of major risk. However the report also highlighted that government debt amounts to only 55% of GDP, which gives the government considerable financial flexibility to handle a crisis. Additional comments were "even if half of property related loans defaulted and lost 80%

of their value we calculate China's government debts would rise to 79% to fund the financial sector bailout". Whether it would lead to a large fall in GDP growth is another question.

Taiwan

With some more optimistic about renewed world growth, the Taiwanese market was the 3rd best performing market in Asia over the last 3 months. Nevertheless the current reality is that the economy in Taiwan is suffering from weak exports and this is hurting growth. The Government recently downgraded its GDP growth forecast for 2015 by 0.5% to 3.28%, but some market forecasts are even lower at sub 3%. With inflation negative at the moment the central bank's policy rate was recently left unchanged at 1.875%. The ruling KMT is expected to officially select Ms. Hung Hsiu-Chu as its presidential candidate for the January 2016 general elections very shortly. Ms. Hung, who is likely to be portrayed as being very pro-China by the opposition, appears to have a difficult task in persuading voters that she can do better than President Ma in economic, social welfare and justice matters. Expect election uncertainty in future months.

Singapore

Despite an easing in its exchange rate over the last 12 months, Singapore remains an expensive place. The situation is only being exacerbated by the tougher stance taken by the Government against foreign labour. Perhaps it is not surprising that the People's Action Party Is pursuing populist policies, given that it faces an election next year. With retail sales lacklustre, weaker tourism and a property market under pressure, the outlook for the economy remains constrained.

Indonesia

The market's fall of 14.60% (A$ terms) in the June quarter made the country the worst performing market in the region. Politics and economics continue to weigh on Indonesia. While the PDI-P party lead by Megawati Soekarnoputri (daughter of Indonesia's first Prime Minister Sukarno) won the Indonesian presidency and obtained a decent number of seats in parliament, this only occurred because of the appeal of Joko Widodo amongst the country's electorate. Nevertheless, the relationship between Megawati Sukarnoputri and Joko Widodo remains a challenging one, not least because each regards themselves as the person in charge. Fears of more government intervention following the ordering of state controlled cement companies to lower prices are also concerning.

Turning to economics, Bank Indonesia has cut its GDP forecast for 2015 by 0.4% to 5.2% (real). This reflects weak credit growth and domestic demand along with subdued investment demand. Bank Indonesia's benchmark interest rate remains unchanged at 7.5%, despite the more subdued outlook for the economy. Near term, the Central Bank has little flexibility to cut rates because of the recent increase in inflation (the annual rate in May was 7.1%), a weakening currency and the need to see a continued improvement in the current account deficit (3% of GDP in 2014). Accelerated infrastructure spending is crucial if the Indonesian economy is going to improve its growth trajectory.

Malaysia

Malaysia was another poorly performing market in A$ terms, falling 8.44% during the quarter and 3.54% over the financial year. The performance of the Malaysian market has been adversely impacted by both politics and economics. Dr Mahathir, the former Prime Minister of Malaysia, has subjected the current Prime Minister Najib Razak to verbal attack on a variety of topics, but particularly the 1MDB scandal. From a political perspective, Malaysia's 3 party opposition alliance called the Pakatan Rakyat (comprising of the DAP, PAS and PKR) has spilt over policy differences. One of these related to the call for the introduction of Islamic penal code ("hudud") in Kelantan. This adds political uncertainly to a country with an ethnically diverse population base.

From an economic perspective, annual inflation in Malaysia continued to increase to 2.1% in May (+1.8% in April) due to the introduction of a 6% Goods and Service Tax (GST) in April. Despite this, a weak economy may still lead to a further reduction in interest rates (circa 25bps). Falling consumer sentiment (high debt) and credit growth remain negatives. Furthermore, low oil prices continue to adversely impact the country's economy with even Petronas reducing capex. Reflecting weak crude prices, the Malaysian Ringgit, which has been amongst the worst performing currencies this year, is now trading close to levels last seen during the Asian Financial Crisis.

Philippines

While market returns were negative over the last 3 months, the Philippines still managed to rise 34.33% in A$ over the financial year. Growth in the Philippines in the first quarter of 2015 slowed to 5.2%. However, with Aquino in his last 12 months as President, and a likely uplift in Government spending on investment, growth is expected to rebound later in the year. With an election due to occur in May 2016, politics is destined to become more of a talking point in the Philippines over ensuing months. That said, private consumption growth remains strong. The Central Bank has a targeted inflation rate of between 2%-4% and, in May, the annual inflation rate dropped to 1.6%. However, with the economy remaining sound, it is unclear whether interest rate cuts will materialise. To this end the central bank recently left its policy interest rate unchanged at 4%.

Korea

The Korean market was down 4.30% in A$ terms over the last 3 months. Following a 0.25% reduction to 1.75% in March, further interest rate reductions seem likely. Exports fell nearly 11% YOY in May following a poor performance in the prior month. This reflects sub-trend economic growth in the American, European and Chinese markets, together with the strength of the Korean Won against the Japanese Yen. With the MERS virus outbreak set to negatively impact on consumer sentiment and the tourism industry, the Bank of Korea is likely to further reduce interest rates later in the year. The Korean market also suffers from poor corporate governance (Chaebols in particular), a low dividend yield and an index dominated by the Samsung and Hyundai groups (nearly 50% of the MSCI Korea index). The primary potential catalyst for the market continues to be legislation imposing a 10% additional tax on their excess cash reserves which are not used to make investments, pay higher salaries or increase dividends. The low valuation of the Korean market continues to attract foreign buying with local pension funds the main sellers.

India

In India expectations clearly got ahead of fundamentals and the market fell 4.20% in A$ over the last 3 months. The country has not been helped by the recent rebound in oil prices and the economy has not been as robust as perhaps the economic statistics indicate. While Indian GDP this year should amount to 7.5%, the number is calculated using new methodology and is not easily reconcilable with the current subdued performance from corporate India. Furthermore, a delay in the passing of the Land Bill (the Central and State governments can both pass legislation) has disappointed investors, as has the format of the proposed Goods and Services Tax or GST. In regard to the proposed GST, it would seem that at least initially, products like alcohol, tobacco and fuel could be left out and continued to be taxed by the states. Furthermore, the exact rate of GST is yet to be agreed and the subject is generating a lot of debate. Among other things the purpose of introducing a GST was to replace a myriad of other taxes, thereby reducing regulatory burdens and their overall tax impost.

While positive things have occurred in India over the last 12 months, such as greater financial inclusion (Jan Dhan Yojana), the transformation of the economy will take time and require patience. That stated, Indian corporate profits as a percentage of GDP remain low (a little over 4%) with good latent recovery potential. For Modi to be successful in the task of running India, he will need to raise the "skill set in his own party", delegate more, foster a genuine team spirit among his ministers and further engage with other political parties. As Ambit Capital recently pointed out, where Mr Modi has taken a personal interest in initiatives, there have been spectacular successes. Examples include Jan Dhan Yojana (150m bank accounts in 9 months), insurance schemes (100m policies sold in a month), Aadhar (around 850m people now enrolled with unique identification numbers), road building and coal production. However in projects where Mr Modi is less involved, like resolving the financial crisis in the State Electricity Boards, progress was been very slow. It would appear that while Modi is very capable, many of his ministers don't have his expertise or experience.

In June the Reserve Bank of India (RBI) cut its repo rate from 7.5% to 7.25%. The reduction seems to have been motivated by concerns associated with the monsoon season, through to ongoing weak investment demand. Changes in subsidy regime and weak agricultural prices have also negatively impacted India's still significant rural economy. The Government's desire to stamp out corruption, as epitomised by the Black Money Bill, is also having an adverse impact on property prices in many parts of India. Varied economic indicators make deciphering how quickly the Indian economy is recovering fraught with difficulty. While inflation has fallen significantly, to meet its 4% inflation target by 2018, the RBI is going to be very dependent on the Modi Government reforming the Indian economy. India's CPI amounted to 5% YOY in April 2015. Nevertheless, investors continue to be positive about the country's prospects. According to a recent UN report, Foreign Direct Investment (FDI) in India increased 22% to US$34bn in 2014. Manufacturing featured as policy efforts to grow the industry, built around the "Make in India" initiative (launched 2014), gained momentum. According to the UN report, the No 1 recipient of FDI in the world is now China (US$129bn) followed by the US (US$92bn).

Thailand

Thailand's economy continues to be very weak with poor consumer sentiment and credit growth. The market fell 3.98% in A$ terms over the quarter. For growth to resume it is crucial that the National Council for Peace and Order (aka the Military) "kick start" the proposed infrastructure programme, where little progress has been made to date. Having reduced its policy rate in February, the Bank of Thailand cut it again by 0.25% to 1.5% in April 2015. However, with the economy remaining weak, further interest rate cuts are possible, especially if the Thai Baht continues to be comparatively stable. Thailand's annual inflation rate was again negative (-1.3%) in May mirroring political uncertainty, low commodity prices and a weak economy. Foreign investors continue to sell the Thai market, as they have done for the last couple of years.

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The Portfolio

While the geographic and industrial composition of the portfolio did not alter greatly over the June quarter, a number of changes were made to the portfolio's individual holdings.

We have always sought to have sensible geographic diversity as a means of controlling risk. We remain steadfast in our belief that no one can predict the future with any measure of accuracy and will therefore maintain this policy.

Country	**%**	**Overweight / Underweight**	**%**
Hong Kong / China	39.7%	Underweight	-2.7%
Indonesia	3.1%	Overweight	0.2%
India	17.8%	Overweight	9.5%
South Korea	6.6%	Underweight	-10.8%
Malaysia	4.2%	Overweight	0.3%
Philippines	6.0%	Overweight	4.5%
Singapore	6.3%	Overweight	0.7%
Thailand	2.3%	Underweight	-0.3%
Taiwan	5.5%	Underweight	-9.9%
Cash	8.5%		

The performance of Asian markets over the last 12 months has reduced the number of absolutely attractive stocks from a valuation perspective. As such, we continue to hold 8.5% of the portfolio's capital in cash, awaiting what we hope will be better entry points. Trading activities remain controlled with portfolio turnover running at an annual rate of around 17%.

By industry, the portfolio's three largest exposures are 26% in industrials (overweight), 25% in financials (underweight), and 14.9% in consumer discretionary (overweight). Aside from telecommunications services, to which the portfolio has no exposure (under review), we are least represented in the healthcare sector (2.8% weighting), utilities (3.8% weighting) and the information technology (7.1% weighting) industries. That acknowledged, while our weighting in the healthcare sector is modest, we are overweight relative to the benchmark. Valuations in the sector are the main impediment to us having greater exposure. In regard to information technology and following our trip to India, we have recently increased the portfolio's exposure to this industry.

Two information technology (IT) / business process outsourcing (BPO) companies were added to the portfolio in the last three months and we believe that both have good growth prospects. India has a global competitive advantage in both these industries and is increasingly moving up the value chain. Furthermore with slow growth in the West, many companies are looking to cut costs by utilising the skills and expertise of Indian IT and BPO companies. These industries have scale barriers in the form of product capabilities, large customer contracts and good reputations / track records. While varying, both companies have good levels of reoccurring revenue and loyal customer bases.

The other new Indian name we added during the quarter is involved in the Indian pharmaceutical industry. India has grown its presence in the generic pharmaceutical industry over many years. Today the Indian pharmaceutical market is the third largest in the world from a volume perspective and the

13th biggest in terms of value. The industry has high barriers to entry due to large capital expenditure requirements associated with new drug development, as well as substantial regulatory requirements. Nevertheless, with its long history in the industry (skills, vertically integrated, moving up value chain etc.) and large size (scale benefits, synergies etc.), Indian companies are well placed globally. Furthermore with their inherent cost advantages, generic pharmaceutical products are only destined to become more popular in future years. The portfolio's holding is a family company with a focus on organic growth through research and development (R&D) rather than M&A. It has a leading presence in the US generics market, good exposure to a number of emerging markets, an improving domestic business and its R&D pipeline looks promising (complex generics and differentiated formulations).

The only other new investment, initiated in the June quarter, was in a Chinese dairy company. While a Chinese SOE owns just over 16% of this company, its stake is nearly matched by the combined stakes of two highly respected international dairy companies, who also have board representation. As per capita consumption of dairy products in China remains low at 20kg / year, against a world average of 55kg / year, growth prospects for the company remain excellent. As the number two player in the industry, the company is in a good position to participate in further consolidation. Furthermore, it is a leader in UHT milk (standard and premium) and yoghurt, ensuring it is in a good position to grow its share of the premium segment of the dairy cabinet. Going forward, we expect the company to average earnings growth of at least 10-15% per year. This stake was funded by a partial reduction, due to valuation considerations, in a FMCG company and a packaging company in Hong Kong.

Over the last 3 months we have fully exited two investments from the portfolio. Some time ago we invested in a Korean convenience store retailer, as we liked the longer term dynamics of the industry. Over the last 3 months this same company announced a significant corporate acquisition. Not only was this investment outside its core business activity, but it also used up all of its substantial cash resources. We did not like this move and having informed the company of our attitude, exited our investment, albeit at a good profit. We also downsized another Korean position reflecting higher regulatory/legal risks associated with its business in China. The other entity which we sold outright was a Taiwanese/Chinese beauty chain retailer, which we felt was failing to deliver on expectations, thus undermining our confidence in management. We exited close to our breakeven price, feeling we could do better elsewhere.

International Visits – Observations and Comments: Southeast Asia

During May the Asian team visited the Philippines, Thailand, Malaysia, Singapore and Indonesia on a trip that lasted a little over two weeks. In addition to the aforementioned countries, we also visited Vietnam. While not part of the benchmark, we see Vietnam as an important part of ASEAN and wanted to familiarise ourselves with recent developments in the country. As usual the purpose of our visit to Southeast Asia was to visit existing portfolio holdings and to follow up on a number of new ideas. Herewith are a number of observations and comments which we found interesting.

Politics

Politics is a "work in progress" and each market has its own unique political challenges.

- Malaysia – According to one senior Malaysian analyst it is a case of "when, not if" Najib Razak (current Prime Minister) is replaced.

- Philippines – There is strong confidence (complacency?) in the corporate sector that a new president will continue with the reforms undertaken by the Aquino administration. However, as one banking executive puts it, "businesses take a wait and see" approach to investment, until the outcome of the election is known.
- Thailand – The military government is credited with keeping the nation "peaceful" and "calm", and potential elections in late 2016 will usher in "Thai style" democracy where the military retains significant power.
- Indonesia – President Jokowi's new administration is seen to be still "learning the ropes" and "lacks political experience", creating significant hurdles to implementing Jokowi's reforms.

Regional integration

"Regional integration" was a buzzword from our meetings, and rightly so, in our view. It presents significant opportunities for ASEAN companies (and also potential threats). Below is a summary of several developments.

- ASEAN Economic Community (AEC) – The CEO of the Philippine Stock Exchange, Hans Sicat, was particularly excited about opportunities created by the AEC for Filipino corporates and the flow-on impact for the exchange. In Thailand, bank and cement companies are likely to capitalise on opportunities from the AEC, given the country's central location in ASEAN and its relatively developed corporate sector. We also believe several milk companies in Southeast Asia may be beneficiaries, as they increasingly source raw materials and sell products regionally.
- Trans Pacific Partnership (TPP) - The likely passing of the TPP, a free trade agreement between 12 developed and developing nations, through the US congress by the end of 2015 should disproportionately benefit Vietnam (the poorest country in the group) given the nature of its exports (low value-add) and key markets (Europe and the US). The TPP will strengthen the nation's goal to become the "world's factory".
- New Silk Road - China's influence in the region, already significant, is expected to become more pronounced with its 'One-Belt-One-Road' strategy, which covers land and water trade routes. This is potentially a long-term threat to some, as Chinese competitors gain better access to inter-Asia and intra-Asia trade routes. Speaking of ASEAN-China relations, recent tensions were not evident in our meeting with the Airport of Thailand. Indeed a senior executive proudly proclaimed that Chinese tourists "are very welcome in Thailand", citing that 25% of tourists passing through Suvarnabhumi airport are now come from that country.

Infrastructure

Two words sum up the wish-list from corporates - 'infrastructure investment'. This will reduce the costs of doing business; improve export competitiveness, through supply chain enhancements and by lowering working capital requirements. Lafarge Republic's CFO summed it up well when he said of the Philippines: "[It] is fundamentally under-housed and lacking in infrastructure, it has the right demographics and low unemployment". We too are positive on the infrastructure investment theme and it has favourable multiplier effects for businesses and consumers.

Some pertinent points:

- Government and PPP projects are all the rage across the region. The Thai Government plans to spend US$60bn from 2015-2022 on new infrastructure including roads, mass transit networks and rail projects. In Indonesia, the Government has set a target of tripling its annual spending on infrastructure from US$31bn to US$90bn. The Philippines has similarly ambitious plans. However, disbursements in these markets have so far been disappointing.
- Commercial and retail property expansion is being driven by rising modern retail penetration (per capita retail space in Philippines/Indonesia is 60-75% lower than Korea and Japan), regional city developments (drivers: 80% of Filipino foreign workers have families in provincial areas; BPO offices are moving out of Manila due to higher property prices). Robinsons Land, a Filipino property company, has locked in 10-15% annual increases in office and retail space openings in the next three years.
- Cement consumption in Indonesia and Philippines is 70% below Malaysia on a per capita basis. Positively, the cement industry has high barriers to entry and suffers from regional shortages, although we recognise that Indonesia faces a 25% increase in capacity in 2016/2017.

Financials

In Singapore, Malaysia and Thailand, high levels of consumer debt and weak corporate demand are constraining credit growth. Indonesia and the Philippines are bucking this trend and are still managing to grow credit relatively strongly. Most banks cited infrastructure investment as a driver of credit growth, but this has yet to eventuate. Margins have come down across most markets with the exception of Singapore, where banks are starting to see margins stabilise in anticipation of higher US rates. Asset quality remains benign. We do not see systemic risks emerging, although some banks have identified increased commodities impairments (Indonesia and Malaysia most impacted). Credit costs have been very low in recent years and are expected to increase modestly in future years.

Two issues front-of-mind were capital and funding. ASEAN banks are focused on building stronger capital levels. Fortunately, most are strongly capitalised so there is little need to raise fresh equity, though dividends are unlikely to increase significantly in the near-term. The exception is Malaysia where we are seeing big banks raise or announce intentions to raise capital. The development of digital banking to protect deposits from competitors and disruptive technologies was a big theme. As one Asian bank CEO put it, banks risk “going the way of the dinosaurs” from disruptive technology platforms. We also met with LPI Capital and another life insurance company in Southeast Asia. Both of these companies have been impacted by slowing economic growth and low interest rates but, in our view, these are cyclical challenges rather than structural changes to the insurance industry.

Consumer

The so-called “inflection point” of US$3,000 GDP per capita leads to a dramatic increase in the consumption of financial services and discretionary consumer goods. This was a common theme in meetings in the Philippines (GDP per capita: US$2,800) and Indonesia (GDP per capita: US$3,500). To illustrate, 47% of Filipino households do not own a car (fifth lowest globally) and 46% of Indonesian households have no car (sixth lowest globally). In contrast, Malaysia had the third highest level of car ownership globally (93%) *(Nielsen Global Survey of Automotive Demand, 2014)*.

We believe that there is a tremendous opportunity in the mobile and data segment, as the region bypasses fixed voice lines prevalent in older, developed markets. The statistics are impressive:

- Southeast Asia has 1% e-commerce penetration vs. 11% in China/US.
- Naver, a Korean WhatsApp-like company, has grown to 300m users in ASEAN in just three years.
- Thailand has 140% mobile penetration.

We are actively reviewing opportunities in telecoms, cable TV operators, towers, satellites and data centres.

<u>Commodities</u>

Unsurprisingly, commodities related companies are notably negative in sentiment and operating trends. The clear message we received, particularly from coal companies, was that the market will be "lower for longer". In Indonesia, demand for excavators, which is heavily linked to the coal industry, is 54% below levels in 2011 (year of peak demand). Given the largely fixed cost nature of these businesses, gross profit margins on new equipment sales is close to zero. Coal companies are responding to challenging conditions by using smaller machines. Average (all-in) production costs in Indonesia for coal have fallen to US $40-45/tonne (vs. selling price of US$57/tonne). United Tractors flagged that it will cut production volumes by 50% if the coal price remains below US$65/tonne.

Market Outlook

With quantitative easing now concluded in the US, investors are focused on when and by how much interest rates will be raised by the Federal Reserve. This appears likely to be contingent on conclusive evidence, which to date has been rather elusive, that the American economic revival is gaining momentum. We remain more sceptical than many about the likelihood of this occurrence. As such, we think "cheap capital" (although it seems to be helping financial markets more than the real world) will be around for longer than is generally expected. Indeed deflation continues to be more of an issue than inflation in most parts of the world and this, at least in the near term, seems unlikely to change. While we hope for a happy ending to "quantitative easing", looking at the calibre of many of the world's politicians and central bankers, and the circumstances under which they function, we fear we will be disappointed. Asia would not be immune from such developments and has challenges of its own. Nevertheless we still feel the region is much better placed from a longer term perspective. Political reform continues in many countries, economic growth remains largely healthy by global standards and most but not all countries are well placed from a demographic standpoint. Lastly, while many Asian markets are "two tiered" absolute valuations appear reasonable and have relative appeal compared with global averages.

Asia currently makes up around 68% of the MSCI World Emerging index and many of the others in this index (Russia/Brazil/South Africa) are resource orientated. This gives them some similarity to Australia, without the political stability and tax advantages. We feel these same commodity orientated markets face elevated risks associated with "being caught in the Middle Income trap".

Lastly, many global investors have elected to gain Asian exposure through multi-national companies listed on markets in America, Europe and Japan. While there is nothing wrong with this strategy, many Asian countries were colonised militarily 100 years ago by American, European and Japanese countries. As such, we very much doubt they will allow themselves to be colonised economically over the next 100 years by Western corporates. Until home grown champions have been created in Asia and they have acquired financial clout, together with brands and distribution in developed countries, we doubt the "playing field will ever be even". We feel this gives direct Asian investment inherent advantages.

Portfolio Characteristics

	Portfolio	Benchmark	Variance
Number of Stocks	50	611	561
Beta	0.82	1.0	-0.18
P/E (X)	15.7	12.2	3.5
Yield (%)	2.2	2.8	-0.6
P/B (X)	2.7	1.6	1.1
Historical EPSg(%)	13.4	9.9	3.5
Forecast EPSg(%)	11.6	9.7	1.9
Return on equity (%)	17.4	13.2	4.2
Dividend Cover (x)	2.8	2.9	-0.1
Net Debt/Equity (%)	-1	27	-28