CI ASIAN TIGER FUND
QUARTERLY COMMENTARY REPORT

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

For current performance information please refer to the Monthly Performance Report.

MARCH 2016

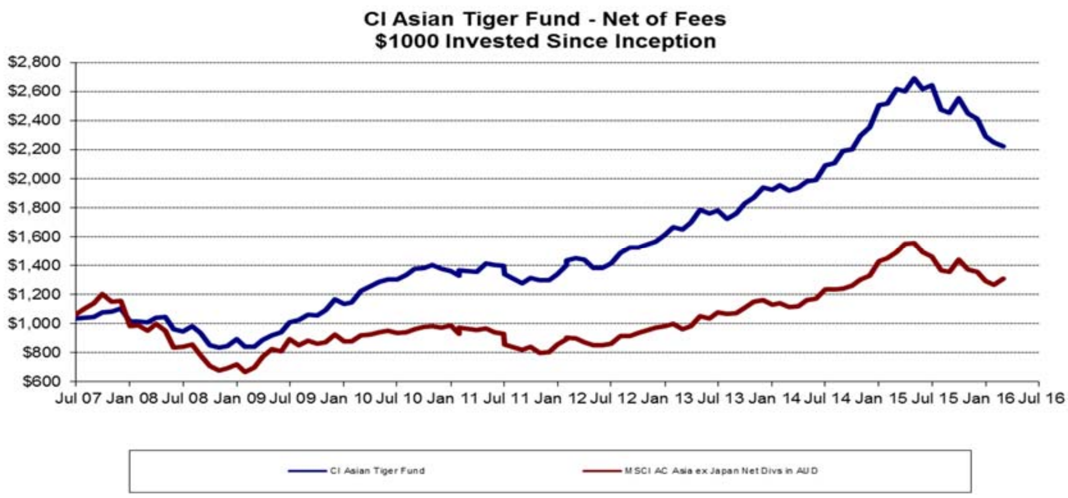
"Seven Social Sins:
Wealth without work
Pleasure without conscience
Knowledge without character
Commerce without morality
Science without humanity
Worship without sacrifice
Politics without principle".
Gandhi

"If you are patient in one moment of anger, you will escape a hundred days of sorrow". Chinese proverb

"Sour, sweet, bitter, pungent – all must be tasted". Chinese proverb

	**PORTFOLIO	#BENCHMARK	VALUE ADDED
ROLLING 3 MONTH	-7.66%	-3.74%	-3.92%
ROLLING 1 YEAR	-13.79%	-12.46%	-1.33%
ROLLING 2 YEAR	9.39%	8.44%	0.95%
ROLLING 3 YEAR	12.07%	10.78%	1.29%
ROLLING 5 YEAR	12.12%	6.07%	6.05%
ROLLING 7 YEAR	17.37%	9.33%	8.04%
SINCE INCEPTION*	11.47%	3.11%	8.36%
SINCE INCEPTION^	158.60%	30.70%	127.90%

*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

Global markets were generally weaker over the March quarter. In Australian dollar terms with net dividends the MSCI AC World index fell 5.2% compared with a fall of 3.7% in the MSCI Asia Ex-Japan index. The falls were accentuated by the strength in the A$. In local currency terms the MSCI World index with net dividends was down 1.5%, while the MSCI AC Asia Ex-Japan index was actually up very slightly (+0.2%). The performance of the ATF over the quarter was disappointing with the portfolio falling 7.66% compared to our benchmark which fell 3.74%. The main reasons for this are more fully articulated in the section below entitled "The Portfolio".

MSCI Data with net dividends	March Qtr 2016 in A$ terms	March Qtr 2016 in local currency terms	12 month end of March 2016 in A$ terms	12 month end of March 2016 in local currency terms
AC World	-5.2%	-1.5%	-5.0%	-4.9%
AC Asia ex JP	-3.7%	0.2%	-12.5%	-10.3%
China	-10.0%	-4.7%	-19.4%	-18.8%
Hong Kong	-5.9%	-0.5%	-7.3%	-6.6%
India	-7.8%	-2.4%	-13.8%	-8.1%
Indonesia	5.2%	7.0%	-13.1%	-11.2%
Korea	-0.6%	2.5%	-6.6%	-3.0%
Malaysia	7.1%	2.9%	-8.6%	-3.1%
Philippines	1.2%	4.7%	-9.9%	-6.6%
Singapore	-0.6%	-0.2%	-12.5%	-13.5%
Taiwan	1.9%	5.5%	-9.1%	-5.9%
Thailand	10.6%	14.3%	-13.3%	-5.6%

Looking back over the latest quarter there was again a wide variation in the performance of Asian stock markets. The best of them in A$ terms were Thailand (+10.6%), Malaysia (+7.1%) and Indonesia (+5.2%), while the worst were China (-10.0%), India (-7.8%) and Hong Kong (-5.9%). That said, it is important to remember that quarterly movements have to be kept in perspective. With this in mind, Thailand, Malaysia and Indonesia were the worst performing Asian markets in A$ terms over calendar 2015 and Hong Kong and India the best.

Over the last three months the A$ appreciated against almost all the Asian currencies in the MSCI Asia Ex-Japan index, with gains ranging from +0.4% v the Singapore dollar to +5.8% against the Indian rupee. The only exception was the Malaysian ringgit where the A$ depreciated 3.9%. The rally in the A$ has been helped by a perception that American interest rates may not rise as fast or as much as generally expected, which has caused US$ weakness. Related to this the Federal Reserve has recently again lowered its GDP forecast in 2016 for the USA from 2.4% to 2.2%. The A$ has also benefited from the strong rally in commodity prices, with the standout being the gold price, which rose 16.4% over the quarter.

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There seems to be growing disillusionment about the capability of global politicians and central bankers to resolve many of the well debated challenges (many of their own making) facing the world. As such, gold and gold shares are being purchased as “insurance” and this is a view we support. Elsewhere there was a rise in the oil price over the last three months, due to perceptions of an agreement between Saudi Arabia and Russia to freeze oil production, while copper and iron ore also rallied.

As previously mentioned Thailand was the best performing Asian stock market over the last quarter. Foreign investors have sold the Thai market over the last few years, but became buyers recently. There is a general belief the government is becoming more proactive in stimulating infrastructure investment and consumption expenditure may have stabilised. While Thailand has a current account surplus, this has been caused by weak consumption, which reduced demand for imports. In addition, exports fell nearly 6% in 2015. The outworking of the current account surplus is that the Thai baht has remained a comparatively resilient currency. The market may have also been helped by views that non performing bank loans may have peaked and the prospect of a general election in 2017, albeit dependent on the passing of an amended draft constitution. The prospect of lower Thai interest rate rates would also have aided sentiment.

The Indonesian market has experienced something of a renaissance over the last three months, rising 5.2% in A$ terms. Lower inflation, declining interest rates and a narrowing current account deficit have all played their part. Bank Indonesia has cut its policy rate three times (cumulative 0.75%) since January 2016. The policy rate currently stands at 6.75% and further reductions are likely. Currency stability has been an important factor in allowing Indonesian interest rates to fall. Another positive has been the potential for a tax amnesty. Indonesia’s current account deficit amounted to 2.1% of GDP compared to 3.1% in the prior year.

At the same time, investors have welcomed President Jokowi Widodo’s new political initiatives. These seem aimed at promoting trade and allowing more foreign investment in the country. For example, some industries had restrictions on 100% foreign ownership and these are now being reviewed. Furthermore, land acquisition has long been an impediment to Indonesian growth. Recent legal decisions have highlighted these may be changing. This is also positive for Indonesian infrastructure development, where the Government, according to CLSA, is apparently focussed on 30 or so priority projects, rather than just a small number of massive high cost projects.

While Indonesia faces ongoing economic challenges, as well as the need to strike a balance between investment liberalisation and populist policies, progress appears to have been made. GDP growth in Indonesia for 2016 is likely to be in the region of 5.0 -5.5%.

The Malaysian market rose 7.1% in A$ terms over the quarter, making it the second best regional market. Overseas investors have stayed away from Malaysian equities in recent times, notwithstanding the market has continued to receive support from domestic investment funds with government linkages. International investors have remained wary of the market due to weak oil prices, political uncertainty (the 1 Malaysian Development Berhad scandal and associated with it, Prime Minister Najib Razak’s leadership position) and weak consumer sentiment. Government revenues from energy have halved to 15% in the last two years, but have been offset by the introduction of a Goods and Services Tax, lower subsidies (e.g. fuel) and higher taxation (e.g. public transport costs). These initiatives have dented consumer demand and curtailed imports.

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While exports have also fallen, it is important to state that Malaysia continues to run a current account surplus. GDP growth in 2015 was around 5% and this is likely to fall to around 4% in 2016, as slower domestic consumption is partially offset by continued expenditure on infrastructure (RM1.4tr Economic Transformation Programme), growth in exports and the likelihood of further decline in interest rates. Sensibly the Government is trying to keep its budget deficit target around 3% and the country's debt to GDP ratio below its self-imposed ceiling of 55%.

China was again a much debated subject and the market fell 10% in A$ terms over the last three months. Much of the talk centred on China's currency and fears of devaluation. That said, China's foreign exchange reserves fell less than US$29bn in February to just over US$3.2tr. In recent months a lot of capital seems to have come out of China due to the repayment of US$ debt and unwinding of the RMB carry trade. On the 2 March, Moody's Investors Services highlighted some of the challenges facing China, when it changed its outlook to negative from stable on China's government credit range. At the same time, it affirmed China's Aa3 Credit Rating.

The main reasons Moody's gave for this change, in summarised format, were as follows:

(1) The ongoing and prospective weakening of financial metrics as reflected in rising government debt (32.5% of GDP in 2012, an estimated 40.6% in 2015 and an expected 43% in 2017), and large and rising contingent liabilities (local government, policy banks and state owned enterprises or SOE's), on the government balance sheet;
(2) A continuing fall in reserves (US$3.2billion in January 2016 v a peak of over US$3.9billion in June 2014), which highlight policy, currency and growth risk; and
(3) Uncertainty about the authority's capacity to implement reform. China's institutions are being tested by challenges stemming from the multiple policy objectives of maintaining economic reform and mitigating market volatility.

Nevertheless, it is also important to mention that Moody's reaffirmed China's Aa3 Credit Rating. In this regard the company highlighted that while China's GDP growth is slowing it still remains higher than its global peers. It further nominated a "relatively moderate level of government debt which is financed at low cost, high domestic savings and substantial foreign exchange reserves".

China achieved real GDP growth of 6.9% in 2015 compared to 7.4% in 2014 and expectations for 2016 are for growth of between 6-7%. In contrast CPI inflation in China during 2015 amounted to 1.4% versus 2% in 2014. Further interest rate cuts are likely in China this year.

Allied to China, GDP growth in Hong Kong slowed to 2.4% in 2015 and the Government expects a further reduction to 1.5% (mid-point) in 2016. Consumption growth has been subdued, while retail sales and visitor numbers from China have also been weak. Notwithstanding government initiatives to stimulate demand, investment growth has also been poor; with delays occurring in major projects like the Hong Kong-Zhuhai-Macao Bridge Project and the Hong Kong-Shenzhen-Guangzhou Rail link. In A$ terms, the Hong Kong market fell 5.9% over the last three months, making it the third worst performing market in the region.

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The Indian market performed poorly over the quarter and one factor exacerbating this was the weakness in the rupee which fell 5.8% against the A$. The A$ performance of the Indian market over the period in question was negative 7.8%. In the circumstances in which it found itself, we believe the Indian government produced a responsible budget. This focused on the rural sector, infrastructure and public sector undertaking banks. Nevertheless following a good performance last year foreign institutional investors have been "profit taking", perhaps sensing that the Indian story, like that of China, is "long term" in nature.

From a regional standpoint two other things are worth highlighting. First, the much awaited Trans Pacific Partnership was signed in February. This agreement now needs to be ratified by its 12 members over the next two years. While an important development it excludes many important Asian countries, not least China. Secondly, the announcement in November 2015, of the victory of Aung Sang Suu Kyi's National League for Democracy, in Myanmar is significant. It is a reminder to all, that the democratic process in Asia, so long in the making and with many attendant faults, continues to move in the right direction.

The Portfolio

From a performance standpoint, the portfolio was adversely impacted by its underweight positions in Taiwan and Korea during the quarter. Whilst being overweight in ASEAN benefited, this was partially offset by India's underperformance, which is also an overweight position.

From a stock specific standpoint, the portfolio was negatively impacted by the poor performance during the quarter of Boer Power and Kepco Plant Service (discussed later), a handful of Chinese names (combination of market weakness and RMB depreciation and capital flow related concerns), as well as profit taking in Max Financial services following a successful de-merger.

During the quarter, the portfolio undertook a number of portfolio changes.

The ATF introduced a new stock, in the form of a Chinese brand owner and retailer. We feel the industry still has considerable "runway" for growth, reflecting trading up, replacement demand and "feel good" trends. Overseas precedents suggest the market could consolidate over time, which would benefit this company as the industry leader. The company, which has a high degree of insider ownership and close to 20 years of operating history, is prudent in the manner in which it is expanding, being asset light, with efficient use of technology and judicious M&A. The company is in a net cash position and should achieve above market growth. Finally the entity generates healthy returns, and trades at a "sensible" valuation.

On the other hand, the ATF exited three positions. The first was an industrial company supplying the healthcare industry. Whilst the company provides exposure to themes which we are favourably disposed to, we have not been able to gain sufficient clarity around future growth drivers, which coupled with "high" valuations and disappointing results to date, resulted in our selling decision. The second stock which was sold was Standard Chartered, where we think operating trends are likely to remain challenging for a prolonged period of time. This has been a poor investment for the portfolio, it has been held for a long period of time and in hindsight should have been sold much earlier.

Finally, the portfolio exited its holding in Boer Power, reflecting serious governance concerns following the company's recent announcement to restate historical financial accounts.

In addition to the above, the portfolio made a number of modest changes during the quarter. One such change was the decision to "top up" our holding in Kepco Plant Service following share price weakness. We think the fourth quarter result reflected a number of "one-off" factors and the future outlook both domestically and internationally remains positive, reflecting a combination of capacity additions to the power industry, rising requirement for maintenance and retrofit services as well as new contract wins. The ATF has also been using the weakness in China to selectively add to our existing positions.

From a geographical perspective, the portfolio remains overweight India and ASEAN, whilst maintaining a large absolute weighting in China / Hong Kong, as well as being heavily weighted towards the Asian consumer, through both direct and indirect (e.g. auto components) exposures. The reasons for this strategy have been articulated in previous Quarterlies.

Market Weights (%)	Portfolio	Benchmark	Differences
Hong Kong/China	42.1	40.5	1.6
Indonesia	5.5	3.4	2.1
India	15.4	9.3	6.1
South Korea	4.6	17.9	-13.3
Malaysia	4.4	4.1	0.3
Philippines	6.7	1.7	5.0
Singapore	6.7	5.4	1.3
Thailand	2.7	2.7	0.0
Taiwan	5.5	15.0	-9.5

International Visits – Observations and Comment: India

We recently had an interesting trip to India touring the length and breadth of the country. During our visit, there was much debate about the recently released Indian budget, on which we will comment later. Following something of a honeymoon period, Prime Minister Modi has recently suffered electoral defeats in some state assembly elections (Delhi and Bihar). This, coupled with rural distress, caused by two disappointing monsoon seasons and some signs of civil unrest, has cast a bit of a shadow over the market. Prime Minister Modi also has spent a lot of time in promoting India abroad, but going forward seems more likely to be focused on internal issues such as getting important legislation (Bankruptcy law and the GST bill) passed. Furthermore, we were recently reminded, by Ambit Capital, who we visited in Delhi, that while India has made rapid economic progress in recent years, this has not been the case on social indicators. According to an Ambit report, the problem is particularly severe in Northern India (Rajasthan to Bihar) which accounts for 45% of India's population and where healthcare, education and jobs are lacking. Relative to other Emerging Markets India does not rank well from a Human Development Index perspective.

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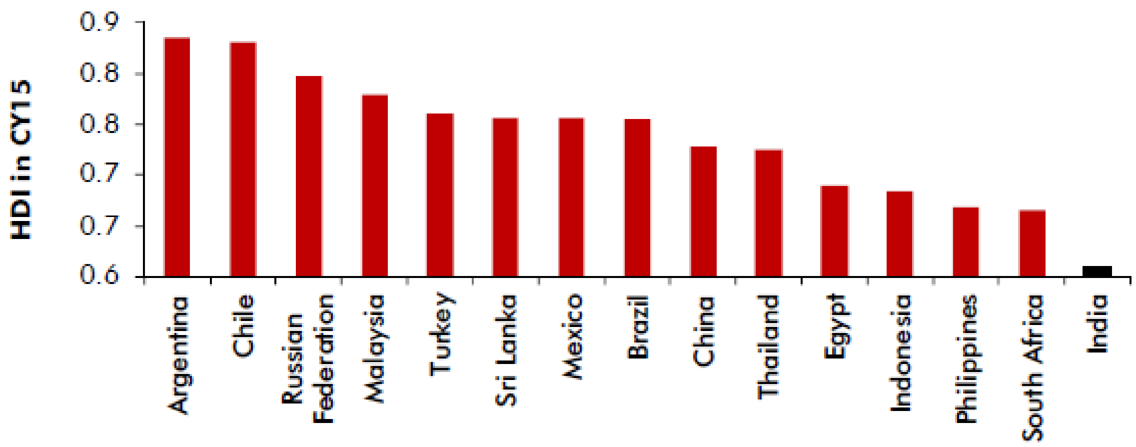
As demonstrated in the chart below, Emerging Market peers like Russia, Turkey and Mexico have significantly superior Human Development Index (HDI) scores as compared to that of India (April 2016).



Source: UNDP, Ambit Capital research

Turning to the budget. As is the case with most Indian budgets, it pleased some sections of society, but not all. Nevertheless, the Indian Finance Minister, Arun Jaitley, outlined a very large investment to aid farmers and to alleviate poverty. In addition, further significant amounts of capital were committed to develop infrastructure. Commendably, the Government, with the help of lower oil prices, maintained its budget deficit target of 3.5% in 2016/17 v the estimated 3.9% this year (Y/E March). This demonstrated fiscal discipline to investors and that it remains focussed on macro-economic stability. That said, there was a price paid for this in the form of muted support for other sections of the Indian economy. Indeed, with massive non-performing assets (NPA's) in public sector banks (circa 70% of system loans), weak private sector investment and declining exports, many thought the Government should have done more to support the struggling manufacturing sector.

Nevertheless there is only so much "money in the bank" and this time it was the corporate sector that would be disappointed. With the world economy subdued, the Indian Government has refocussed on domestic demand and consumption led growth. All things considered, perhaps a sensible near term view. The key now for the Modi led government, is the implementation of the budget and this can be very challenging, in a country where "red tape" and bureaucracy remain entrenched.

Despite the challenges, we feel it would be wrong to underestimate Modi. Ideologically he does not appear right wing or left wing. He simply wants to create wealth to enhance the standard of living for all Indians. To this end, he apparently aspires for "double digit" GDP growth in future years. In an attempt to better understand the man, we asked a highly successful Gujarat businessman who has created a billion dollar corporation, what statements best describe the current Indian Prime Minister.

The nominated words were:

1. Has charisma
2. Hard working
3. Dictatorial
4. Does not delegate easily
5. Conscious of India's image
6. Survivor (will do what it takes)
7. Learns quickly
8. Does not trust easily
9. Wants results
10 Aware of need to deliver

By focussing attention on the rural sector, infrastructure and to some extent on the recapitalisation of India's state run banks, the latest budget is focussing on the country's most pressing issues. While the agricultural sector only accounted for 17.4% (2015/16) of India's GDP, over 50% of people are still dependent on it. Two years of rural distress have decimated the countryside in India and the budget allocated Rs445bn to the Ministry of Agriculture and Farming Welfare, compared to Rs229bn in 2015/16. A further Rs887bn has been allocated in 2015/16 for Rural Development (Rs797bn previously). A significant part of this (Rs385bn) will be spent on job creation (the MGNREGS scheme). Another focus area is rural electrification with the aim of 100% coverage of rural India by 2018.

In regard to agricultural land in India, only 46% of cultivable land is under irrigation, making the remainder of it subject to the vagaries of the monsoon. As such, the Government has set aside considerable funds for irrigation and the sinking of wells. From a social perspective, the government's goal of universal electrification across rural India would significantly improve farmer welfare and quality of life. These and other rural initiatives are aimed at encouraging agricultural investment and improving farm profitability. If achieved, the Government's aim of doubling rural income by 2022 may not be just a "pipe dream". The Unique Identification Number scheme in India, called Aadaar, is crucial to the renaissance of rural India. This allied to personal bank accounts (the Fintech revolution) will enable direct transfers of subsidy and social welfare payments to intended recipients, reducing corruption and boosting consumption.

Another major thrust of the BJP's budget was infrastructure spending, where it intends to commit Rs2.2tr in 2016/17 compared to Rs970bn in the previous year. A significant part of this will be spent on road construction, assuming land acquisition and public private partnership issues can be resolved. Port and nuclear power development and some other areas are also in the spotlight. Productivity should also be enhanced and this in turn should increase private sector investment.

While the government has actively promoted its "Made in India" scheme, the 2016 Budget was not the focus of attention, from an urban and corporate sector perspective. That stated, public sector banks did receive some limited assistance. This comprised Rs250bn, albeit this was part of the Rs700bn, allocated in the previous Budget. This help was badly needed, as without Government support, most of the public sector banks would be bankrupt. Indeed many observers believe no sustainable economic recovery will materialise in India, until this situation is rectified. We sympathise with this view. Clearly stressed loans are impeding public sector banks' ability to lend and thereby fund growth. The positives are the Reserve Bank of India (RBI) has strengthened asset quality reviews and the Government is prepared to consider, albeit with guidelines, industry consolidation.

We also view the establishment of the Bank Board Bureau, headed by the respected Vinrod Rai (ex-Controller and Auditor General of India) in a favourable light, as this will encourage efficiency in the sector and improve corporate governance. The recent announcement from the Bank of Baroda, writing off a significant amount of bad loans and implementing further provisions, highlights that things are slowly changing for the better.

Overall, we did not regard the Indian Budget as negative. The Government had to provide assistance to the agricultural sector and this it did. Perhaps more could have been done to help the corporate sector and in particular, promote manufacturing. In short, the Budget could have been more positive, but like every country, India has to "live within its means". Remember, even the widely applauded budget deficit of 3.5% for 2016/17 assumes divestment and telecom receipts of around Rs1.6tr this year, compared to only Rs0.8tr in the prior year. It is also important to remember that if State government debt is added to government debt, India's budget deficit would be over 6% of GDP according to CLSA. In addition, the firm estimates the 3.5% government deficit forecast for 2016/17 is understated by 0.9%, due to off balance sheet funding of infrastructure in things like roads and railways.

Lastly, implementation of a budget in India is challenging at the moment because of India's three speed economy. This was also highlighted by Ambit Capital who has classified the Indian economy into three distinct segments, comprising:

1. Low speed economy (share of GDP 40%) – agriculture, construction, public administration and banks.
2. Mid speed economy (share of GDP 30%) – commercial transport, manufacturing and residential real estate.
3. High speed economy (share of GDP 30%) – personal transport, hotels, commercial property and business services.

The Reserve Bank of India (RBI) has tried to assist the Indian economy by lowering interest rates, as inflation has declined. CPI inflation in India amounted to 5.2% YOY in February compared to 5.7% in the prior month. The RBI's targeted rate for CPI inflation is 5% by March 2017. The RBI has reduced its repo rate by 1.5% since January 2015 and further cuts are likely. The repo rate in India is now 6.50% having been cut by 0.5% recently. Nevertheless, many Indian public sector banks are not keen to lend for the reasons mentioned previously. In contrast, large sections of the private sector, especially in the slow/mid speed part of the economy, are reluctant to borrow. As such, the long expected investment cycle has failed to materialise and this is damaging economic growth. Furthermore, following the changes in the method by which India's GDP is calculated, official growth numbers seem overstated.

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On our tour around India, one thing that struck us was how quickly technology is being embraced and how it is changing people's lives. The disruption this could have on a wide variety of industries will be very real as will the potential to "do things the India way". A good example of the latter is the success of Patanjali Ayurved (PA), the company founded by Acharya Balkrishna and Baba Rambev in 2006. This company produces a wide variety of Ayurved products in the food and FMCG categories. Recently a lot of press attention has focused on the success of its toothpaste brand Dant Kanti. Indeed it is estimated that PA now has 2.5% of the Indian toothpaste market and is winning market share from both Colgate-Palmolive and Hindustan Lever. Whether or not this success continues remains to be seen.

In regard to technology India's Information Technology and Software Services Export revenue is expected to grow 12% in 2015/16 to US$108bn and a further 10-12% to around US$120bn in 2016/17 according to the National Association of Software and Services Companies or Nasscom. That said, growth has moderated due to slower technology spending by the industry's global clients. Nasscom Chairman Mohan Reddy recently commented "that India increased its market share in global outsourcing from 55% to 56%".

Currently India has some 912m active wireless subscriptions (SIM cards) and around 325m internet users and the numbers continue to expand. Indeed we were reminded by an Indian friend that the country has more mobile phones than toilets. The top websites in India, in order of importance are Google, Facebook, YouTube and Amazon India (source Kotak). The dominance of foreign companies in India is markedly different to China where the reverse is true. Nevertheless there are some important differences between to the two markets. In India the internet is English based rather than Hindi, whereas in China it's all in local language. Laws, regulations and government in India result in an "equal playing field", but this is not the case in China, with its protectionist policies. Internet technicians in India are close to Silicon Valley and therefore favour American software and hardware. Lastly, Indian internet companies are very dependent on overseas capital.

Given the prior comments search, social networking and messaging opportunities may be limited in India, as they are dominated by foreign companies. Furthermore the main Apps in India are currently found in mobile software, online gaming and online content and to date Indian corporate presence is comparatively limited. Nevertheless the potential for Indian internet companies in this area seems much greater. According to Kotak Entertainment, gaming and music downloads amounted to 37% of total App downloads compared to 25% for shopping. The top five e tailers in India are currently Amazon, Flipkart, Snap deal, Paytm and EBay (source Kotak). Amazon is rumoured to be losing significant amounts of capital in India, but the market remains a priority. Indeed it is apparently determined to be the top e commerce player in India, having failed in this regard in China.

India, a global market leader in the export of generic drugs, is also doing well in this area. Indeed Indian generic pharmaceutical exports amounted to US$14.78bn in FY 2015 and are expected to increase to US$16.04bn in FY 2016. That acknowledged, some Indian generic pharmaceutical companies are under increasing scrutiny from regulatory bodies like the US FDA. Issues that have been raised include making false statements, failing to report drugs that did not meet specifications and plants not complying with standards. We think the industry understands the importance of these issues and is taking all steps to comply and lift standards.

Another area of importance for the country is in the area of remittances. These are payments made by Indians working abroad to their families in India. Indian overseas remittances amounted to US$38billion in 2015, which was only a modest fall from the US$39billion recorded in 2014. Remittances have been disappointing recently because of low oil prices, which are negatively impacting Middle-Eastern economies. Nevertheless India's current account deficit has benefited materially from lower oil prices. While lower remittances are a slight negative, foreign direct investment into the country remains strong.

In order for a sustainable recovery to occur in India, it is crucial that the financial sector remains sound. Given the importance we attach to this, we have set out some specific comments on the outlook for the industry.

The growth opportunities for the Indian banking sector are significant given the early stage development of the economy (GDP per capita of US$1,800) and low banking penetration (less than half the population actively use the banking system and total bank credit to GDP is only 60%). Loan growth across the sector has averaged 13% over the last three years (slightly higher than nominal GDP) and this growth is expected to continue, or perhaps even accelerate, as India's economy grows. On a regional basis, the Indian banking sector compares favourably with other developing markets in terms of structure, regulatory landscape, profitability and growth opportunities. Broadly speaking, the private sector's prospects are comparable to those in Indonesia and the Philippines (similar penetration, structure, profitability and growth prospects) and relatively more attractive than China and Vietnam (greater market share for private players, better capitalised, less state interference). While the financial sector makes up only 15% of the index, the investable universe in the Indian financial sector is relatively more diverse than other developing Asian markets.

State-owned (PSU) banks retain a dominant position in terms of branch network and deposit base, and still account for over 70% of industry loans. However, these banks are financially constrained by asset quality issues (some estimates suggest up to 10% of loans may be impaired) and weak capital bases (estimates on recapitalisation requirements range from US$30bn to US$40bn over the next three years). For the most part, private sector banks are better positioned to benefit from India's ongoing economic growth. They are financially much stronger and have the resources to invest in the network and systems, and in doing so they are likely to continue to take more market share from PSU banks.

Like other banking sectors regionally, the ability to protect and mobilise low cost deposits is paramount to sustain asset growth, margins and returns. To do this, banks are vying to become the customers' 'primary' bank, but how they achieve this may differ to paths taken in more developed markets. So, perhaps the two most uncertain as well as exciting recent developments in the Indian banking sector, are the impact of mobile/digital banking and the 23 new bank licenses issued in 2014 and 2015, including two universal banking licences (IDFC and Bandham).

Both of these factors could have a profound impact on encouraging greater financial inclusion and to mobilise savings, and over time, to change the competitive landscape.

Another unique characteristic of the Indian financial sector is the prevalence of non-bank finance companies (NBFCs), which account for almost 10% of financial system assets. The prominence of NBFCs in India primarily stems from the large unbanked population as well as the low levels of retail banking penetration, where currently less than 20% of bank loans, are to retail customers. This is consistent with other developing banking markets where the formal banking sector exists (at least in its early stages) mainly to service corporates/state-owned enterprises.

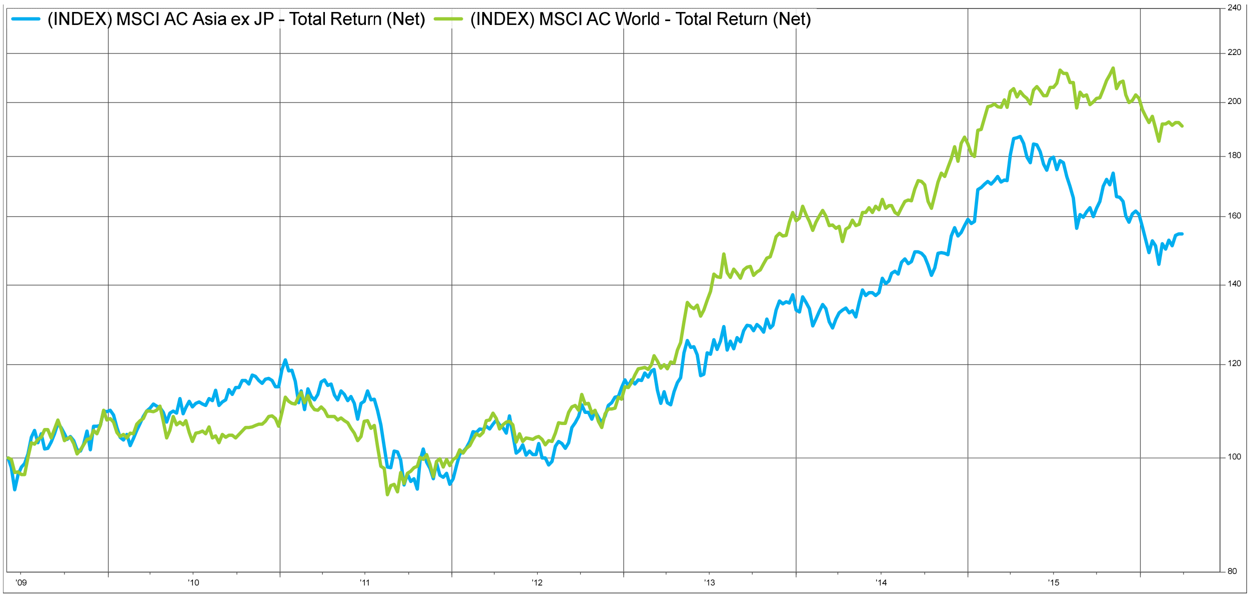
Interestingly, the cultural affinity for Indians to hold physical assets such as gold, has seen loans secured against gold become a key product for many NBFCs. Surely, a product that is uniquely Indian. According to CLSA gold accounted for 12.4% (US$843bn) of Indian household assets in March 2015, while equity, pension and insurance funds collectively accounted for just 11.8% (US$788bn).

Market Outlook

Notwithstanding the modest uptick in American interest rates, the Western world continues to experiment with unorthodox monetary policy, whether led by Yellen, Draghi, or Kuroda. On evidence to date, we continue to lack conviction that the outcome will be successful.

Negative interest rates in many countries around the world, are a “real step into the unknown”. Even respected financial institutions like the Bank of International Settlements (BIS) have come out warning of the dangers. In a paper written last year entitled “Ultra Low or Negative Interest Rates: What they mean for financial stability and growth”, by H Hannoun, the dangers are well articulated. The report is well worth reading, in summary, the dangers are disincentive (to reduce debt), distraction (fixated on monetary policy), distortion (in asset prices), disruption (in the business models of financial institutions), and disillusion (in the ability of central bankers). We feel the latter point could also be extended to most politicians around the world.

As shown in the chart below, the MSCI (AC) Asia Pacific Ex-Japan Index has dramatically underperformed the MSCI World Index since the GFC. Notwithstanding our generally cautious view on the global environment, this strengthens the relative valuation argument for Asia, at a time when absolute valuations remain reasonable. We continue to have faith in the Asian region, but acknowledge it would not be immune should the global economic situation deteriorate further.



Source: FactSet

For current performance information please refer to the Monthly Performance Report.

MARCH 2016

Portfolio Characteristics

	Portfolio	Benchmark	Variance
Number of Stocks	47	624	577
Beta	0.84	1.0	-0.16
P/E (X)	14.03	12.39	1.64
Yield (%)	2.81	2.89	-0.09
P/B (X)	1.99	1.32	0.66
Historical EPSg(%)	11.84	8.63	3.21
Forecast EPSg(%)	8.00	3.15	4.85
Return on equity (%)	14.25	10.70	3.55
Dividend Cover (x)	2.58	2.80	-0.22
Net Debt/Equity (%)	-5.31	24.01	-29.32

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