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.

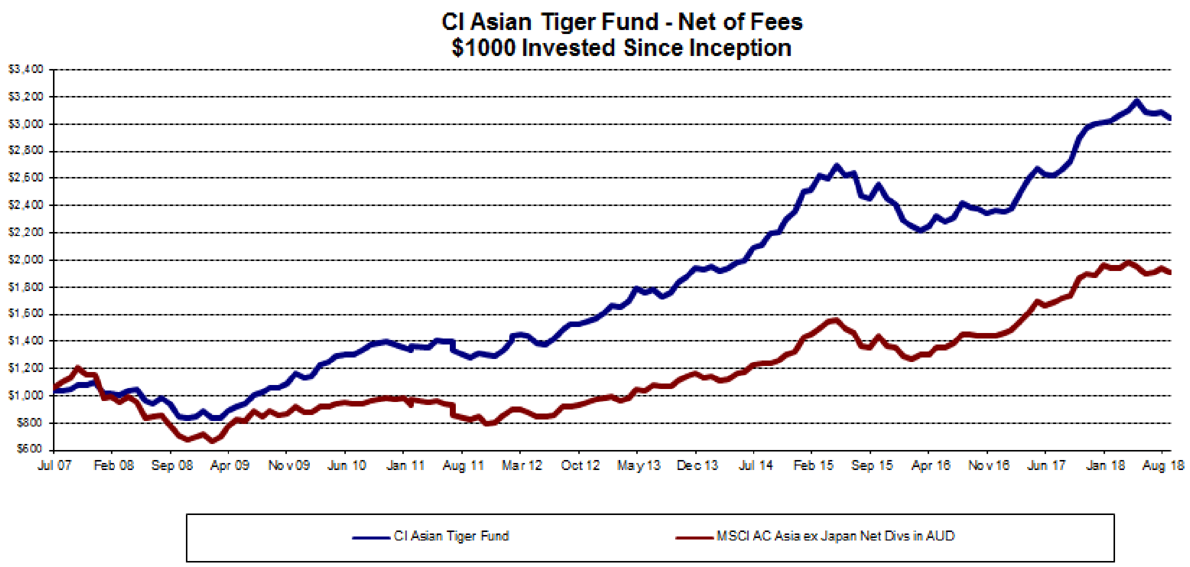
SEPTEMBER 2018

"We simply attempt to be fearful when others are greedy and to be greedy only when others are fearful." Warren Buffet

"In reality, no one knows what the market will do; trying to predict it is a waste of time, and investing based upon that prediction is a speculative undertaking." Seth Klarman

	**PORTFOLIO	#BENCHMARK	VALUE ADDED
ROLLING 3 MONTH	-1.01%	0.51%	-1.52%
ROLLING 1 YEAR	13.07%	10.02%	3.05%
ROLLING 2 YEAR	14.24%	14.74%	-0.50%
ROLLING 3 YEAR	8.74%	12.17%	-3.43%
ROLLING 5 YEAR	13.11%	12.25%	0.86%
ROLLING 7 YEAR	14.76%	12.86%	1.90%
ROLLING 10 YEAR	14.53%	9.37%	5.16%
SINCE INCEPTION*	12.21%	5.93%	6.28%
SINCE INCEPTION^	265.53%	91.22%	174.31%

*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

The Asian markets experienced a volatile quarter as investors oscillated between hope and despair, driving the benchmark up 1.7% in August and then down 1.4% in September. The portfolio fell 1.01% during the September quarter, compared to the 0.51% returns by our benchmark. The short term underperformance was attributed to a few Chinese internet companies giving back some very strong gains over the past two quarters, and elevated regulatory pressure in the Chinese healthcare sector.

Whist intensified regulatory pressure is by no means a uniquely Chinese phenomenon today, we have observed an accelerated pace of political reform in China that is worth noting. Comparing to past reforms where policies and execution were often disconnected due to convoluted regulatory bodies with overlapping oversights, this round of reforms is more coordinated with an often newly formed central regulatory entity. As a result, both the depth and pace of execution surpassed those in the past. Some of the recent examples include –

- Pharmaceuticals – a new regulatory body under the name State Medical Insurance Bureau ("SMIB"), was formed in May 2018. It consolidates the functions that used to reside in different state departments, such as healthcare budget control, payment and drug price negotiations. As a result, it wields significant power in the ecosystem and has since forced various pharmaceutical companies to slash prices across a broad range of generic drugs.
- Online Gaming – the government announced that a new regulatory body will be formed for online game approval and oversight, and that "the number of new games approved each year will be reduced" with a strict bias towards 'high quality games'.

These regulations, combined with the market fear that they are harbingers of more to come, caused sector-wide panic and precipitous stock price declines, sometimes as high as 30-40%. We hold a different view, however, and believe the long term operating environment for these industries remains favourable. Chinese healthcare spend is significantly below global standards on both per capita spending and as a % of GDP basis. Out of pocket expense portions are also very high at (30%+) compared to developed markets (<15%). Aging demographics, expanding middle class, combined with the development of commercial health insurance, will propel healthy long term growth. Similarly, online gaming has become a national sport in China, with over 600mm gamers enjoying games as one of the lowest cost entertainment options available. eSport is increasingly recognized as a mainstream competitive sport – it will be an official medal sport for the first time at the 2022 Asian Games in China.

We believe over time the regulatory environment will stabilize with the new rules being more clear and enforceable than the past. This is not necessarily a bad thing, especially for management teams that we invest in. These managers have thrived through numerous economic and political cycles by being flexible and adaptable to the ever changing environment, reserving and preparing for unforeseen situations, and maintaining a conservative balance sheet. The current regulatory headwinds will be no different from the past challenges for them.

During our visits to consumer product companies, we observed a notable slowdown in certain segments of retail in China such as automobiles and air conditioners. We believe the main reasons behind the slowdown are:

- Slowdown in consumer loan issuance as part of a nationwide deleveraging mandate, resulting in growth deceleration or even stagnation in credit-driven discretionary spending (e.g. automobiles)
- A government crackdown on local government financing and off-the-balance sheet financing that led to a sharp slowdown in infrastructure investment and property sales, dampening demand for housing-related spending (e.g. air conditioners and washing machines)

Over the longer term, we believe the consumption upgrade trend remains intact in China. Middle class income continues to grow, and a reduction of personal income tax burden over time will further support higher consumer spending. Consumers are technology-savvy, well-researched and demand superior quality at a reasonable price. Local companies are working hard to upgrade their product offerings and catch up to imported products, providing the consumers with ever more choices. Across a broad array of categories from dairy to cars, products by local manufacturers are increasingly perceived as of equal or even superior quality and at a lower price. Our portfolio holdings such as Anta for sportswear and Vitasoy for soymilk offer some of the best value-for-money for Chinese consumers, and will continue to do well regardless of the broader credit or housing conditions.

After outperforming the other emerging markets since the beginning of the year, the Indian market declined by 9.2% (in AUD) in the month of September, ending the quarter down by 0.2%. As well as concerns around surging fuel prices and falling currency, the recent liquidity crisis around a large conglomerate, Infrastructure Leasing & Financial Services Limited ("IL&FS"), intensified the pressure on the stock market.

A sprawling conglomerate with nearly 170 direct and indirect subsidiaries, IL&FS had expanded by borrowing aggressively in the past few years. Between June and August, five special purpose vehicles under one of its subsidiaries, together with the parent company, failed to service their debt obligations. This set off widespread panic around liquidity for all the Indian non-bank financial companies (NBFCs) and ended with a surprise government seizure of the IL&FS Group.

We believe so far that the spill-over effect to our bank investments in India should be limited, and the long-term trends of financialisation, formalisation, and financial inclusion remain favourable. In the near term, short term headwinds in net interest margins should be partially offset by efficiency gains in operating costs and a reduction in loan provisioning.

Fundamentals remained strong for most of the ASEAN markets. However, the Indonesian Rupiah and Philippines Peso continued to be weak given these countries' growing current account deficits. The currency pressure, combined with rising inflation, pushed a number of central banks to raise rates. The portfolio's holdings in the ASEAN region are predominantly in Singapore and Thailand, with only one holding each in Malaysia and Indonesia. We believe the impact of general central bank tightening in ASEAN countries to our portfolio will be limited.

The biggest contributors to performance in terms of total shareholder return in AUD included:

- Taiwan Semiconductor Manufacturing Company (positive outlook on the ramp up of its new 7 nanometer node)
- Central Pattana (solid performance in existing mall operations with new malls opening in 2H'18)

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- Ping An (strong growth in number of customers and core insurance business; promising progress in fintech)

The biggest detractors to performance in terms of total shareholder return in AUD included:

- Tencent (uncertainty around gaming regulations)
- 51Jobs (missed investor expectations due to elevated sales and marketing spend)
- Shanghai Fosun Pharmaceutical (regulatory concerns on its generic drugs portfolio and capital raising)

The Portfolio - Strategy, Structure, Process and Recent Changes

Strategy

- The ATF strategy targets enduring capital growth and tends to out-perform in down-markets
- The strategy is to find a portfolio of stocks in Asia with the best risk-adjusted value latencies across 6 subsets of value
- The strategy emphasizes long term thinking in research, investment horizon and partnership with management
- The strategy allocates capital based on bottom up stock selections and industry analysis

Structure

- Concentrated, long-only, long-term equities portfolio with 30-50 stocks
- Portfolio companies with risk adjusted value latencies across 6 subsets of value
- Long term investments in 'proprietary managers' who think and act like business owners
  - Passionate, humble and focused
  - Aligned incentives
  - Knowledgeable and 'learning machines'
  - Value-based capital allocation with conservative balance sheets

The current portfolio is positioned around 5 subsets of value as follows:

- **Stalwarts** (45%) - sturdy, strong and generally larger companies with world class privileged market and competitive positions. (HDFC Bank)
- **Growth companies** (30%) – growing companies with identifiable value propositions using traditional value metrics and run by focused, prudent and experienced management. (Vitasoy)
- **Cyclicals (8%)** - stocks showing upside leverage to the cycle with experienced and contrarian managers who can allocate capital prudently and with good balance sheets. (Leeno)
- **Asset Plays** (6%) - stocks with strong or improving balance sheets trading at discounts to net asset value or replacement value. (Jardine Strategic)
- **Low Risk Turnarounds (2%)** - sound businesses with good management in place and good balance sheets. We especially like spin offs and government to private turnarounds. (China Mengniu)

Currently the portfolio holds 8% cash.

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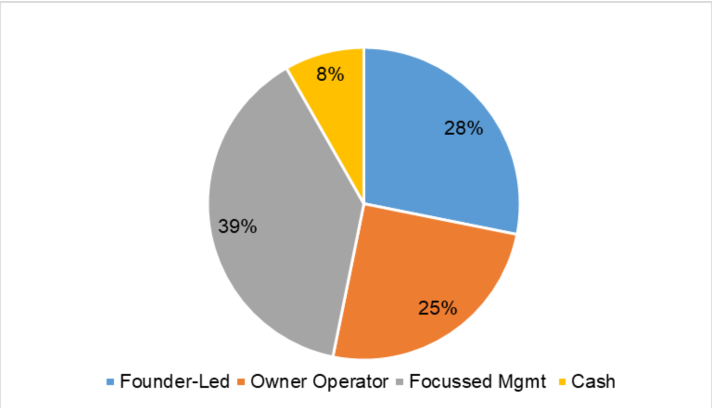
Portfolio attributes as at Sep 2018 are summarized below:

	Portfolio*
Number of stocks	36
Beta	0.91
P/E (x)	17.1
Yield (%)	1.8
P/B (x)	3.1
Historical EPSg (%)	15.3
Forecast EPSg (%)	13.0
Return on Equity (%)	18.4
Dividend Cover (x)	3.3
Net Debt/Equity (%)	-10
Tracking Erros vs MSCI Asia ex Japan	3.59

Portfolio Breakdown by Management Type



We believe the management types that produce the most attractive investment opportunities in Asia are:

1) Founder-led, where the original founder aligns his/her interest with investors and remains committed to leading the business to bigger successes; and

2) owner operator, where the strong and unique culture permeates the organization, and 'thinking like an owner' becomes second nature to the management team.

Portfolio Risk Review

The portfolio's volatility remains below our benchmark. The portfolio has also outperformed ~80% of the time during down-markets. We believe this is an outworking of the CI VoF and Subsets of Value investment process.

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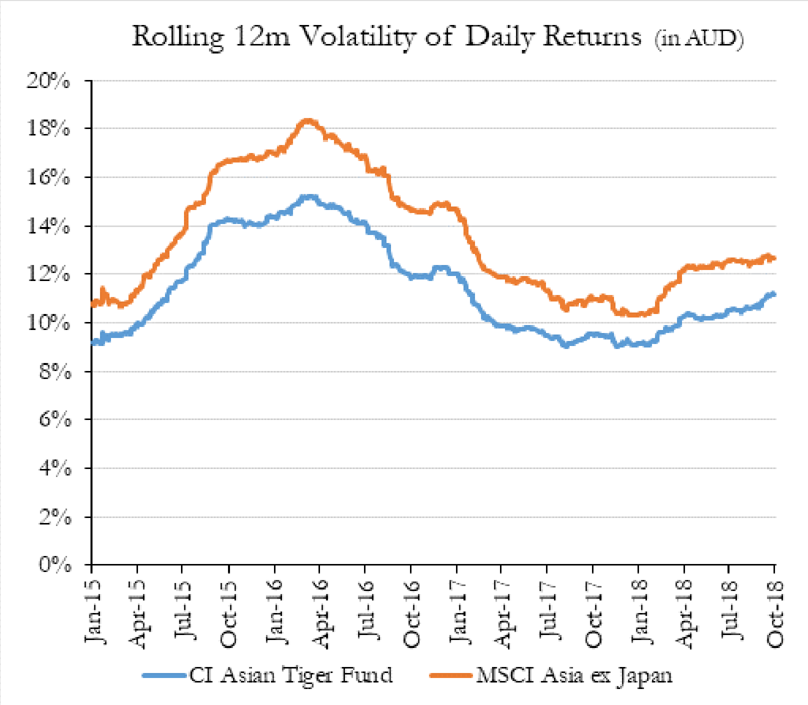

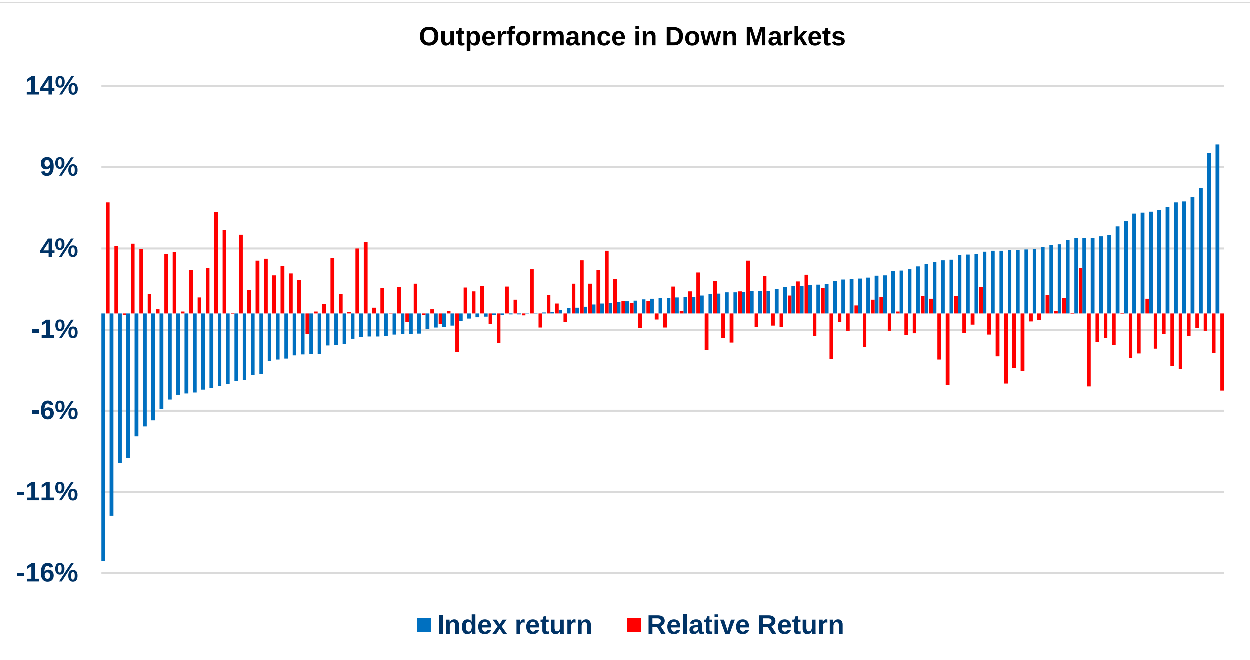

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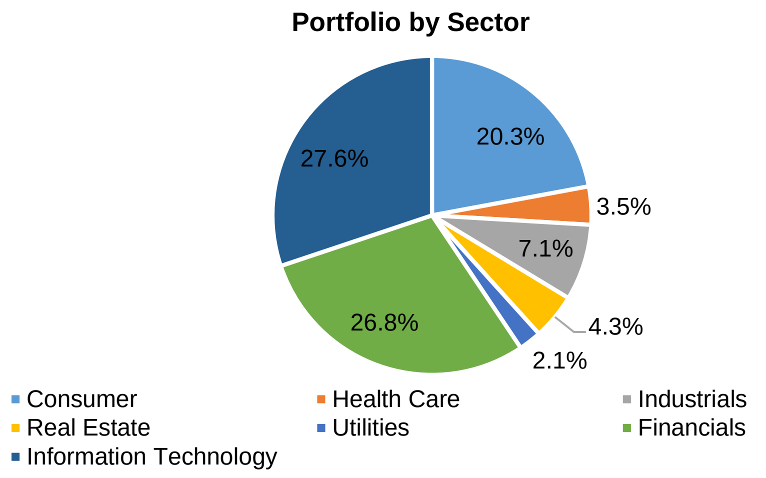
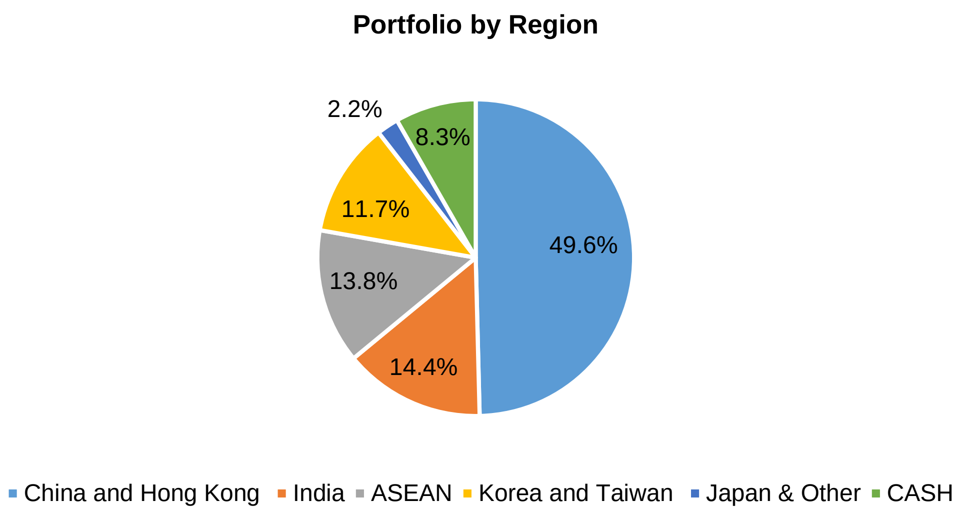
From a sector and country perspective, the ATF current exposure is as follows:





Process

- A small, focused team travels to the Asia region, visiting high-quality management teams repeatedly. On average, we conduct 500+ company meetings and calls per year
- Actively liaise with other CI funds and leverage CI's global networks
- 150+ watchlist stocks provide a pool for new idea generation
- Risk controlled for balance of subsets of value and conviction
- Active positions and benchmark unaware
- Leverage CI's well-resourced research platform and back office

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Recent Portfolio Changes

We have been following a group of companies that are based outside of Asia but capturing the hearts and wallets of Asian consumers for a few years. Over time, we added a number of these companies to our Level 1 research watchlist based on the following criterion -

- A significant portion of sales, profit or assets from the Asian region.
- Thoughtful strategy and a long execution track record in the Asia markets.
- World class corporate governance.
- Existing knowledge base within CI. We prefer companies that our global equities or Australian equities teams have visited repeatedly in the recent years. This also helps us observe and assess the ex-Asia part of their businesses.

During the September quarter we bought **Unicharm**, a leading Japanese-listed diaper and feminine care company. About half of the company's sales are derived from Asia (excluding Japan), with the most exciting growth originating from China and India. The company is well-positioned to take advantage of the prevailing demographic trends in Asia and profitability should improve as the company's businesses outside Japan scale up.

In general we believe having a number of high quality global stocks with Asian exposure is not only consistent with our investment philosophy and process, but also adds a valuable element of diversification to the portfolio over time.

We initiated a position in **Techtronic Industries** this quarter as another example of joint research and travel with our global equities team who have been following the company for years. Techtronic is a family-controlled holding company listed in Hong Kong and the owner of a portfolio of dominant power tools brands (such as Milwaukee, Ryobi and AEG). Techtronic management exudes the characteristics that we are looking for here at CI – passionate about and laser-focused on their core products, highly innovative ("we want to be the Silicon Valley for power tools"), and an accept-no-excuse attitude. We found the following quote from the Company's CEO on its August 2018 earnings call representative of this attitude -

"The issue is not what impact tariffs will have on TTI, the issue is which competitor is best able and best positioned to be nimble and flexible and respond to whatever tariffs come about… And I can tell you right now that we are not making an excuse in advance in telling you that tariffs are going to affect our gross margin, our EBIT margins, they will not."

Stock News

In September **Anta** announced the acquisition of Amer Sports, a Finnish sportwear and sports equipment maker and owner of a portfolio of globally renowned brands such as Salomon, Wilson, Arc'Teryx, Peak Performance, and Atomic. Amer Sports' sales have slowed in the recent years, partly due to lack of success in emerging markets such as China. Anta management's plan is simple – to re-create the Fila success in China with Amer's brands.

Anta's track record with Fila in China has been outstanding – 8 years after the acquisition of Fila's China business, the then little known brand grew sales by 40x whist operating margins expanded from negative to 20%+. Throughout the Fila turnaround process, Anta acquired valuable organizational expertise in supply chain management, international talent acquisition, branding and design. We were impressed by the thoughtful construct (e.g. Anta could end up owning a higher % of the China business with less financial burden) and thorough preparation (e.g. financing secured, minimum shareholder approval risk, etc.) of the deal, reflecting the strong execution ability of Anta's management.

Revenue growth of **Dabur** India has accelerated, propelling strong performance over the quarter. The domestic business, under its new head, is embarking on several initiatives including more aggression on core brands with emphasis on consumer healthcare brands, regionalisation with a locally-driven product strategy, innovation agenda with focus on growing the company's existing small but strong brands, expansion of direct retail reach, cost optimisation including a review of supply chain management, and new management appointments.

After tripling its stock price since early 2017, **51Job**'s share price fell by nearly 40% from its recent peak after reporting worse than expected profit due to rising marketing and product development expenses. Whilst the headline valuation on 51Jobs had been high (33x free cash flow at peak price), we believed there were compelling value latencies in its operating trends and focussed management. With the online recruitment penetration at <25% and 51Jobs being one of the largest online players with ~30% market share, there is a long runway for growth. Its founders remain at the helm and intensely focused on adding value to their recruitment customers. Furthermore, we believe the additional spending will accelerate new product adoption by 51Job's customers and be beneficial for its long term success.

Trip Notes

We joined the global equities team in Tokyo visiting cosmetic, food and beverage, and specialty retail companies. This was followed by a short trip to Seoul, visiting companies in the same industries. Post trip, we enhanced our conviction in Unicharm and are completing research works on another potential investment in Korea.

We also undertook an extensive 2 week trip in China in September across Hong Kong, Hangzhou, Beijing and Shanghai.

We attended the **Alibaba** Investor Day in Hangzhou. We were impressed by the depth of its management bench - out of the 13 presenting senior managers, most of them are high quality leaders that could have led a multi-billion dollar standalone company themselves. The long term operating trends for Alibaba remain very positive. The company is expanding its software and data services from online merchants to offline retail businesses, significantly growing its risk-adjusted addressable market size (offline retail is still 4x the size of online). The Alibaba retail software is now powering over 1 million out of the 6 million mom-and-pop corner stores in China as well a number of large chain retailers selling groceries, electronics, furniture or fashion. Its' cloud and Ant Financial businesses also represent strong value latencies.

We visited a number of healthcare companies in Shanghai and Hong Kong to better understand trends on government spending and reimbursement, as 70% of healthcare related spending in China is covered by the government. The overall policy objective is to control the total healthcare budget by directing spending away from low-efficacy /over-used drugs. Ongoing price cuts are likely to continue but the level of price cuts will differ widely in different categories. For example, domestic generics and imported drugs have seen significant price cuts, whilst biologics and innovative new drugs are much less impacted. The best companies we met during the trip are actively investing in innovation and globalisation which we believe is healthier and more sustainable over the long run.

We were impressed by **TSMC**'s respectful attitude towards industry peers, its "customer first" approach as well as its continuous focus on cost. We think industry trends remain favourable with new opportunities with 5G and AI. TSMC is well-positioned to capture a greater share of the market thanks to an improving competitive position aided by its pure-play foundry business model.

We had a one on one meeting with **Vitasoy**'s CEO and CFO in September and believe the future outlook remains favourable as Vitasoy expands its product selection and geographic coverage in China. We attribute the company's success to stable ownership and management, a clear product focus centering around soymilk and tea, as well as a long-term and judicious approach to investing in people and infrastructure.

Team News

After successful stewardship of the Asian Tiger Fund since its inception in 2007, Mr. Robert Palmer has retired from Cooper Investors, effective on Sep 30th, 2018. We thank Rob for his enormous contribution to the firm for over a decade.

Qiao Ma has assumed portfolio manager responsibilities since June 30th, 2018. Prior to joining CI in July 2017, Qiao spent seven years investing in Asia and the US. Most recently she was the Head of Asia for Jericho Capital, a multi-billion dollar global investment fund based in New York. Qiao has also previously worked at Coatue Management, a New York based investment fund specializing in global technology and consumer sectors and a spinoff of Tiger Management. Prior to her investing career, Qiao worked in the Financial Institutions Group in the Investment Banking Division of Lehman Brothers. Qiao holds a Bachelor of Commerce degree from University of Virginia and an MBA from Harvard Business School.

It is business as usual at the ATF.