COOPER INVESTORS ASIAN EQUITIES 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.

JUNE 2020

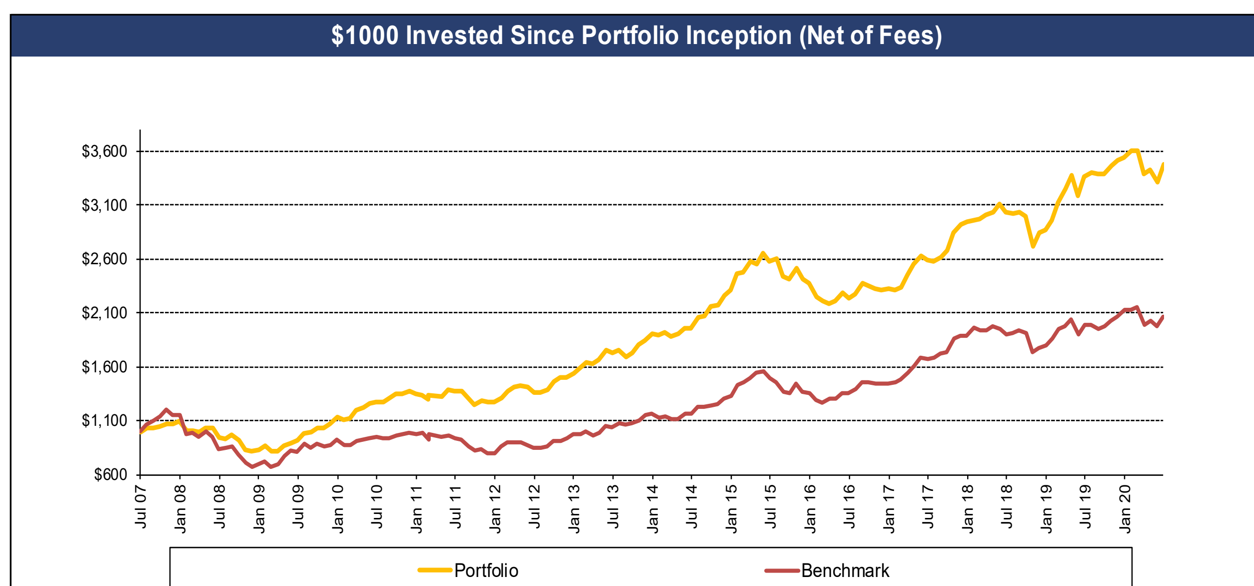
Focus and persistence are my only two keys to success. – *Sun Piaoyang, Founder and Chairman of Hengrui*

Without strategy, execution is aimless. Without execution, strategy is useless. – Morris Chang, Founder of Taiwan Semiconductor Manufacturing Company

No external force can fail a person or a company. A person falls by what is in his / her heart. A company falls by internal management. – *Yu Minhong, Founder and Chairman of New Oriental*

	**PORTFOLIO	#BENCHMARK	VALUE ADDED
ROLLING 3 MONTH	2.38%	3.75%	-1.37%
ROLLING 1 YEAR	3.25%	3.65%	-0.40%
ROLLING 2 YEAR	6.97%	4.21%	2.76%
ROLLING 3 YEAR	10.27%	7.41%	2.86%
ROLLING 5 YEAR	6.15%	6.73%	-0.58%
ROLLING 7 YEAR	10.43%	10.35%	0.08%
ROLLING 10 YEAR	10.56%	8.10%	2.46%
SINCE INCEPTION*	10.05%	5.74%	4.31%
SINCE INCEPTION^	247.13%	106.63%	140.50%

*Annualised
^Cumulative (2 July 2007)
**Historical figures are derived from the historical returns of the existing Cooper Investors Asian Equities Fund Wholesale Class, net of fees and costs that are applicable to Retail Class units.
MSCI AC Asia ex Japan Net Divs in AUD



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Market and Portfolio Performance

After a sharp drop over the March quarter, the Asian market rebounded alongside global indices. The portfolio gained 2.4% over the June quarter, compared to 3.8% of our Benchmark. The relative underperformance was driven by the sharp rise of the Korean and Taiwanese markets in which we had relatively light exposure, as well as stock selection in ASEAN. For the financial year 2020, our portfolio returned 3.3% against the Benchmark of 3.6%. Please note these performance numbers are net of all fees and expenses.

Across Asia, impact from Covid-19 is steadily waning. Factories in China are humming, restaurants in Hong Kong are full, and even parts of India are gradually opening. Risks of a second wave, in our opinion, remain manageable. For countries that handled the first wave relatively well, vigilance became part of the grass-root culture. For example, a regional breakout in Beijing in the second half of June was met with resolute community lockdown, city-wide rapid testings, and strict social distancing rules in a city with over 20 million residents. These measures were effective, and newly infected cases dropped to nearly nil after 10 days.

The recovery of business fundamentals, however, is much more uneven. The strong are getting stronger - we observe that the companies with the right leadership, humble yet progressive culture, and ample resources as a result of years of proper financial planning, sailed through Covid-19 largely unscathed. As the economies open up, these companies are gearing up to capture even more market share from their weaker, less-organized peers who are still reeling from the pandemic. We expect this trend to continue far beyond Covid 19-impacted periods.

For the 3 months and financial year ended on June 30th 2020, our China and Hong Kong portfolio holdings contributed 1.2% and 1.4% to outperformance, respectively.

The contribution to outperformance came from a diversified group of businesses that were relatively defensive against Covid-19, such as online entertainment, data centres, grocery stores, and innovative pharmaceutical companies. These industries have been a research focus for the fund for a long time, and we are pleased to see the favourable long term trends accelerated further over the past year.

We are also increasingly excited about portfolio companies that are best-in-class in industries with short term challenges. The news headlines for life insurance, manufacturing and travel / lodging remain negative. Stocks in these industries are also still trading considerably below pre-Covid-19 levels. But the best companies in these industries, often led by tenacious and long term thinking founders, have quietly streamlined their operations, enhanced their digital capabilities, and in some cases made counter-cyclical investments to further strengthen their competitive positions.

Consider China Lodging, the leading hotel chain in China, as an example. Under the leadership of its visionary founder Mr. Ji Qi, China Lodging invested heavily into IT infrastructure and a membership program over the past decade. It enjoys an extensive technology toolkit with over 40 in-house solutions, ranging from a mobile housekeeping app, automated check-in/check-out, to delivery robots for guests. It also has a thrifty, hands-on and entrepreneurial culture. When cities first opened up and hotel demand remained weak, China Lodging hotel staff rolled up their sleeves, went out and passed around business cards at train stations, government office buildings and local businesses. Their hard-work and enterprising spirit paid off – China Lodging gained a lot of new local business clients, first to meet their staff quarantining needs, and later on for normal business travel. As a result of its technological prowess and culture, China Lodging recovered much faster than its peers, ramping up occupancy at over 70% by the end of June, compared to less than 50% for the industry. Going forward, we are not only confident about China Lodging's continued recovery, but also on the accelerated pace of its expansion, both domestically and overseas.

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AIA is another example. A prolonged Hong Kong protest and border closure between mainland China and Hong Kong posted obvious short term challenges. AIA management, however, focuses on growing and planning for the long term. It continues to recruit and high-grade its agency base, widening the quality gap between its full-time, highly educated agency force and its competitors' often part-time and disorganized agencies. Digital initiatives became front and centre. It developed a digital process that can prospect, communicate with, and finally convert new clients. This process was first tested successfully in China, and later introduced to other markets such as Thailand. Despite the volatility of its near term operating trends, the long term value latencies for AIA grew substantially over the past 12 months. These latencies include further expansion into mainland China, cross-learnings between different regions, and generally growing public awareness of the large protection gap in Asia.

For the Chinese companies currently listed in the US, a noteworthy development is the enabling of dual-listing on the Hong Kong Stock Exchange (HKEx). Before 2018, due to certain restrictions by HKEx, listing in the US was the only practical option for Chinese technology companies. HKEx made a series of reforms to enable these companies to dual-list in Hong Kong. Since then, three large internet companies, Alibaba, JD and Netease, have completed their dual listings. We expect more US-listed Chinese companies to follow suit.

Our US-listed portfolio holdings enjoy highly attractive risk-adjusted returns. They generate free cash, usually with a net cash balance sheet, grow at a healthy clip above 15%, and are led by seasoned founders and owner-operators with high integrity. We believe dual listing removes a significant risk and overhang for these companies, and we continue to be optimistic of their long term future.

Our Indian portfolio holdings had a disappointing year, detracting 8bps and 13bps of performance for the 3 months and financial year ended on June 30th 2020, respectively.

The private banks in India had a tough year. Loan growth slowed for the industry, growing only 7% for FY 2020 compared to 12% in FY2019. The slowdown was driven by a sluggish rural economy and weak urban housing market. The implosion of banks with poor lending practices such as Yes Bank further shook investor confidence.

We continue to believe our portfolio holdings of HDFC Bank and Kotak Mahindra Bank are in a far superior position than their industry peers. Both of these banks have built up strong retail franchises over the years, mostly with urban salaried workers. Since their borrowers can work from home and are relatively immune to lockdowns, we have already observed gradual normalisation of loan paybacks. The loan book quality and capital position of both banks remain excellent, thanks to their consistently stringent lending practice. We believe these large private banks are in an excellent position to sustain healthy growth and accelerate share gain.

Similar to the private banks, near term challenges in the IT services industry are paving the way for long term opportunities. The challenge was on the supply side, as these IT companies scrambled to enable their workers to work from home ("WFH"). This was complicated further by the data security sensitivities from some of the big clients in the financial services sectors. These issues have been largely resolved, with 90-95% of the staff now working from home in a productive manner. In the long run, we believe the agile WFH arrangements could provide better access to talent globally, reduce the need for on-site staff in the US and Europe, and deliver cost savings from less travel and physical infrastructure. Tata Consultancy Service, for example, believes that by 2025, only 25% of employees will need to work out of their facilities.

We also observed resilience in demand for IT services. Some of these services such as payroll processing are deeply engrained in the clients' core business operations. Interrupting these services has serious ramifications for the customer experience and operation continuity. As of now, demand

has largely recovered for these business process outsourcing services. Other projects such as IT infrastructure upgrades might be delayed in the short term. But in the long run, WFH and consumers' rapid shift to online services will only make these upgrades more mission critical. Cloud migration and data security further increase the urgency of IT projects. Interestingly, we have observed higher recent interest in IT upgrades from even traditional industries such as utilities and manufacturing.

Our ASEAN portfolio holdings detracted 81bps for the quarter but contributed 27bps of performance for the financial year. Our largest Stalwart holding in ASEAN, the Singapore Exchange, had a volatile quarter which we will discuss later in this letter. Over the long term, we continue to be optimistic about Stalwarts in this region. We also recently furthered our research in the private hospital sector in Thailand and Indonesia, and initiated a few small positions.

Korea and Taiwan detracted 87bps and 13bps of performance for the 3 months and financial year ended on June 30th 2020, respectively. Despite having quite a number of companies from Korea and Taiwan on our watchlist for years, we have not identified many portfolio candidates with adequate risk-adjusted returns. As a result, in a sharply rising market, these regions tend to be a drag on performance. This is natural and by design.

Regions outside of Asia were roughly flat for the quarter but contributed 47bps of outperformance for the financial year. Japan stood out as the region with the most outperformance. We are pleased to see our efforts in investing in global champions with large Asian exposure bearing fruit, and will continue our strategy in these regions.

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

- **Hansoh Pharmaceutical** (Positive progress on new drugs development pipeline)
- **Techtronic** (Positive operating trends; beneficiary of stay-at-home economy)
- **Netease** (Strong online games performance and rich game pipeline)
- **WNS** (Fast recovery of business process outsourcing client demand)
- **GDS** (Strong demand for cloud data centres in China; attracting high quality investors such as Hillhouse)

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

- **Singapore Exchange** (Termination of contract with MSCI)
- **AIA** (Concerns around Hong Kong / China border closure and social unrest in Hong Kong)
- **Momo** (Uninspiring quarterly result. We believe the long term trends remain positive)
- **Ping An** (Concerns around its ability to sell high ticket protection policies when customers are still reluctant to take face-to-face meetings. We believe these concerns are short-lived)

Portfolio Review

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Portfolio by Industry Sectors	
Consumer	27.7%
Financials	21.4%
Information Technology	16.9%
Communication Services	14.0%
Health Care	7.2%
Real Estate	2.9%
Industrials	2.8%
Utilities	0.0%
CASH	7.1%

Portfolio by Country	
China and Hong Kong	60.1%
ASEAN	10.1%
India	8.0%
Korea and Taiwan	10.6%
Japan & Other	4.1%
CASH	7.1%

Portfolio Attributes[1]	
Number of stocks	41
Number of stocks outside of benchmark	9
Beta	0.9
P/E (x)	21.8
P/FCF (x)	25.1
Dividend Yields	1.7
Historical EPS Growth %	17.5
Forecast EPS Growth %	8.5
ROE %	13.7
Tracking Error vs Benchmark	3.7

The portfolio is positioned around five subsets of values as follows:

- **Stalwarts (38%)** - sturdy, strong and generally larger companies with world class privileged market and competitive positions. (Singapore Exchange)
- **Growth (40%)** – growing companies with identifiable value propositions using traditional value metrics and run by focused, prudent and experienced management (Tencent)
- **Cyclicals (5%)** - stocks showing upside leverage to the cycle with experienced and contrarian managers who can allocate capital prudently and with good balance sheets. (Huazhu)
- **Low Risk Turnarounds (9%)** - sound businesses with good management in place and good balance sheets. We especially like spin offs and government to private turnarounds. (Sun Art Retail)
- **Bond-Like Equities (2%)** - businesses with secure, low-volatile dividends that can be grown and recapture inflationary effects over time. (Link Real Estate Investment Trust)

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; or 2) owner operator, where the strong and

[1] Source: UBS PAS

unique culture permeates the organization, and 'thinking like an owner' becomes second nature to the management team. Together these two management types account for nearly 60% of our portfolio.

Portfolio by Management Type	
Founder Led	32.1%
Owner Operator	23.6%
Focussed Management	37.2%
CASH	7.1%

Recent Portfolio Changes

We initiated a position in **momo.com (8454-TW)**, the leading ecommerce platform in Taiwan. In the past, eCommerce penetration in Taiwan stagnated at a relatively low level of 10%, compared to over 20% in other Asian or developed countries. However, two recent developments could significantly accelerate its growth going forward. On the demand side, social distancing over the past few months solidified the consumer behaviour of shopping online. Even after the relaxing of these social distancing rules, consumers still prefer the convenience and variety of eCommerce and have not fully returned to physical stores. Equally important, on the supply side, brands used to reserve the best selling products for offline department stores. Over the past year, however, we observed a wholesale change in the brands' attitude towards online. Momo.com now sources products directly from brands, accessing their best inventory, instead of going through a third party distributor.

We had a number of in-depth discussions with management, including an one-on-one video call with its de facto founder who was appointed by its parent company Fubon Group to set up Momo.com from scratch in 2004. We found its culture down to earth and pragmatic. Management invested aggressively into Momo.com's strengths as an online retailer, including logistics infrastructure, mobile product, customer rewards programs and supplier relationships. But at the same time, the company understood that it would not be able to develop superior technology than the international giants such as Amazon and Alibaba. Instead, it aims to be a fast follower and adopts only the technology that suits its own operations.

We believe Momo.com could sustain ~25% annual revenue growth with potential for meaningful margin expansion over the next few years.

We initiated a position in **Dr. Lal Pathlabs**, India's largest diagnostic lab chain with over 200 labs and 3,000 patient service centres. We had an impressive first meeting with its management team during our visit to India in September 2019. Since then, we have hosted multiple one-on-one video conference calls with its CEO and CFO. Industry dynamics are highly favourable, with both an expanding addressable market and high potential for market consolidation. Barriers to entry are low, and even small independent labs earn an attractive, double digit return on capital. As a result, the industry remains fragmented. Despite being the industry leader, Dr. Lal only has a 3.5% market share. Going forward, however, the competitive advantage of Dr. Lal is becoming more apparent. Its hub-and-spoke model, where blood samples are collected by local centers and shipped to be tested in central labs, is much more capital efficient than the independent operators who have both collection and testing on site. Dr. Lal is then able to invest in high standards of site hygiene, a strong digital infrastructure, a thriving home collection business, and better regulatory compliance. As demands from both consumers and regulators on these aspects are rising, Dr. Lal is well positioned to gain significant market share.

During the quarter, we also initiated positions in **a private hospital in Thailand**. As the premier private hospital group in Thailand, it enjoys favorable long terms trends in both domestic and international segments. On the domestic side, Thailand has a fast ageing population, with rising demand for high quality private hospital care. Increasing penetration of private health insurance improves affordability over time. For the international medical tourists, Thailand offers a highly attractive value proposition - state of the art facilities, highly skilled doctors, five-star hotel level nursing service, no waiting time, and costing 50-60% less than western countries. As a result, over 1 million patients travel to Thailand each year for routine and complex medical procedures. Their travels have been temporarily interrupted by border lockdowns. Having spoken to a number of medical tourism facilitators, we have high confidence that medical tourism is a long term secular trend that will not be structurally altered by COVID-19. In fact, Thailand's success in controlling the spread of the virus relative to other Asian nations would only enhance its reputation as a safe place for those medical procedures.

Stock News

Singapore Exchange announced the termination of its long term partnership with MSCI Indices. We have extensive discussions with its CEO, CFO and IR since the announcement. Our understanding is that during the routine contract renewal discussions that occur every five years, MSCI raised the contract price to a point that is no longer commercially sustainable for Singapore Exchange. We believe Singapore Exchange have alternative options to replace the most popular MSCI products. For example, it announced in July 2020 the launch of FTSE Taiwan which could recover a good portion of the potential volume lost for MSCI Taiwan, one of the most heavily traded MSCI indices. Moreover, Singapore Exchange's true competitive advantage lies in its multi-asset strategy. It offers a comprehensive suite of products that range from equities, fixed income, currency and commodities. For example, if a client wants to cross equities futures contracts with commodities, Singapore Exchange is the only option. We also rate its management highly, and have been impressed with the way they handled a difficult situation. They were transparent with shareholders and swift in finding alternatives.

AIA Chinese Banking and Insurance Regulator (CBIRC) approved AIA to convert its Shanghai branch into a wholly owned subsidiary. AIA became the first foreign life insurer to incorporate in Mainland China. Although this is not an automatic license to do business nationally immediately - AIA still needs to apply for separate regulatory approvals to establish new branches - it does pave the way for faster expansion. AIA China currently only operates in two provinces (Guangdong and Jiangsu) and five cities (Beijing, Shanghai, Shenzhen, Tianjin and Shijiazhuang, Hebei) that represent ~1/3 of China's GDP. We believe its China business could grow to address a much bigger part of the country, and expand multi-fold in the process.

Sun Art announced that a senior executive of Alibaba, Kevin Lin, will be appointed the CEO of RT Mart (the more profitable and bigger part of the two retail brands under Sun Art), and will eventually become the CEO of Sun Art in 2021. The current CEO, Peter Huang, is likely to retire. We met Kevin during his second year leading the Linshoutong ("LST") system in Alibaba, and were very impressed with his deep expertise and palpable passion. He worked at P&G for over 20 years before joining Alibaba Group in 2016. Under his leadership, LST has constructed its own ecosystem, offering supply chain support to mom-and-pop stores and became the largest business-to-business retail platform, covering over one

million stores across the country. With his extensive background in retail and technology, we are confident that Kevin will be a solid CEO for Sun Art's next chapter.

Trip and Meeting Notes

We caught up with the CFO of **Li-Ning**, our Chinese sportswear holding. While the start of the year was challenging for all sportswear companies in China due to COVID-19, operating trends are improving as consumers return to their normal lives. Li-Ning was fortunate to have proactively cleared inventory at the end of last year, leaving a clean inventory balance going into the COVID-19 shutdown. Li-Ning's brand has enjoyed a major resurgence, which has allowed the company to consistently hike prices in the past few years and it did so again entering into 2020, which will also help offset the impact of higher levels of discounting in the sector. We are also excited about Li-Ning's new co-CEO, Mr. Takeshi Kosaka, a former executive at Uniqlo, who brings with him experience across supply chain and merchandising which can help streamline Li-Ning's operations.

We spoke to the Chief Strategy Officer of **Tencent**. Tencent reported a very strong first quarter result as consumers stayed at home and consumed more digital entertainment. While consumers are returning to work and school, their passion for high quality online games has not diminished. Tencent has an exciting pipeline of new game title launches in the coming year, which should also help drive growth. Tencent's advertising business outperformed the overall market, driven by meaningful improvements in advertising technology. We are also excited about Tencent's investments into its "mini-program" offering in WeChat which could be a meaningful software business over the long run, and an additional source of value latency.

We had a great video call with the CFO and IR of **Hansoh**. Hansoh remains highly focused on R&D and academic research. It is one of the very few innovative pharmaceutical companies in Asia with a proven track record of creating, producing and selling highly complex and costly biological drugs. Its new drugs pipeline is impressive, with 1-2 potential blockbuster drugs coming into production each year over the next 5 years. We also expect the incremental policies to be supportive of domestic innovation leaders. After all, the success of companies like Hansoh in producing cost-efficient domestic drugs and replacing the expensive import drugs is key to managing the budget burden for the Chinese healthcare system in the years to come.

We also spoke to **Ping An**. The longer term, especially around the technology side of things continue to sound very good, especially now that the new Head of Insurance is applying best practices from Autohome, a subsidiary of Ping An where he serves as the CEO, to Ping An. In particular, the data solutions that Autohome developed and supplied to dealers significantly increased their conversion rate from inquiries to auto purchases. Now the same type of data solutions and intelligence have been developed for Ping An agents as well. We believe Ping An's biggest long term competitive advantage remains the unparalleled access to consumer data. It operates a sprawling empire in consumer finance and medical services that span from Good Doctor online consultation to Ping An retail bank. We believe going forward Ping An could potentially create many ways to cross sell, converting the vast online customers to highly profitable insurance / asset management clients.

We had an impressive call with the CFO of **Apollo Hospitals**, India's largest hospital network. Apollo Hospitals was founded in 1983 and is currently led by the founder's daughter. Over the last 4 decades, Apollo has patiently built out a network of 70 hospitals. Apollo offers one of the best patient experiences in India, embracing the latest equipment and technology, attracting high quality doctors, and most important of all, having the best nursing staff in the country. Nursing staff in a hospital is particularly

important given the amount of time they interact with patients. The company calls this "Tender Loving Care", a phrase it has trademarked! Building a new hospital in India is not easy, with several legs of approvals and interface required at various levels of government. Accordingly, replicating a network such as that of Apollo's is likely to be extremely time and capital consuming for any new entrant. Apart from a profitable hospital operation, Apollo also runs the largest organised pharmacy business in India, with ~3,500 standalone pharmacies. Apollo enjoys significant bargaining power over distributors and passes on the gross margin savings to customers. We have added Apollo Hospitals to our watchlist.

During the quarter we had in-depth conversations with various C-level executives at **ICICI Prudential (IPRU),** including its MD / CEO, Deputy MD, CFO, and Chief Risk Officer. These conversations pointed to a consistently conservative risk management culture. One key tenet for this risk culture is always remembering that they are investing on behalf of small retail investors who count on them for retirement. In addition, these meetings also deepened our understanding and appreciation of the deep and exclusive partnership between its parent company, ICICI Bank, and IPRU. IPRU's products are deeply integrated in all aspects of ICICI Bank's online and offline distribution strategies. Compared to an open platform approach where the bank pushes products by multiple insurers, this approach is much more effective at cross-selling the highly profitable protection products to the bank's customers.

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