10 Years of Managing Indian Equities

Rahul Chadha, Co-CIO of Mirae Asset Global Investments (Hong Kong)

1. You have managed Mirae Asset's India strategy for more than 10 years and looked at Indian equities for longer than that. How has India changed in that time?

India has always been a growth story. When I first started my career in 1999, India's information technology (IT) services industry was taking off as a beneficiary of the global outsourcing trend. The government sowed the seeds for growth, which led to a period of strong economic expansion in the subsequent decade. Starting in 2004, however, leaders became singularly focused on seeking economic growth without considering a long term, sustainable foundation for achieving that growth. Following the Global Financial Crisis, earlier excesses became real macroeconomic issues. For example, the infamous twin deficits issue —in the national budget and in foreign trade — led to the long slide in the value of the rupee.

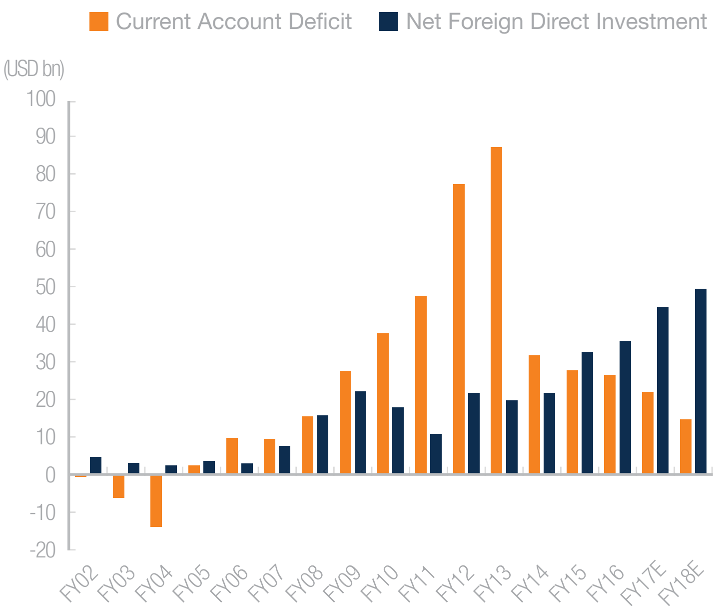
We have seen the government of Prime Minister Modi take bold steps to ensure the sustainability and longevity of India's economic growth, particularly in strengthening the country's institutional framework. The government has made improving the ease of doing business a top priority and encouraged healthy competition between states to attract investment. Government projects are awarded on a more meritocratic basis with greater transparency and meaningfully reduced crony capitalism. For the benefit of the Indian public, the government has made tremendous progress in programs such as unique identification registration, financial inclusion, direct benefit transfer, and online services that have altogether enhanced productivity and transparency.

India is now in a very exciting time where the government has laid the groundwork for long-term sustainable growth. Foreign investors now face lower macro risks than ever before, allowing micro opportunities to shine through.

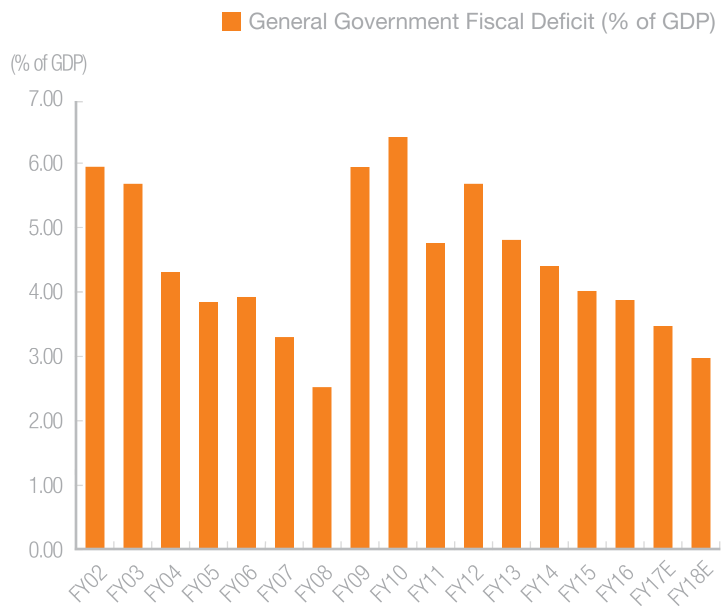
"India is now in a very exciting time where the government has laid the groundwork for long-term sustainable growth."

Twin Deficits: Lower Current Account & Fiscal Deficits with Higher Foreign Direct Investments

Source: CLSA, RBI, CMIE, Mirae Asset Global Investments (2017)



Source: CLSA, RBI, Ministry of Finance, RBI, Mirae Asset Global Investments (2017)



2. You have beaten the benchmark nine out of the last 10 years. You are in the top decile of onshore and offshore managers across key performance metrics.[1] How did you do it? What are the factors for success?

As I mentioned earlier, India truly is the land of opportunity where growth can be found literally everywhere. At the same time, we must not forget that it is still very much an emerging country where investors are exposed to more risks than they would be in many other markets.

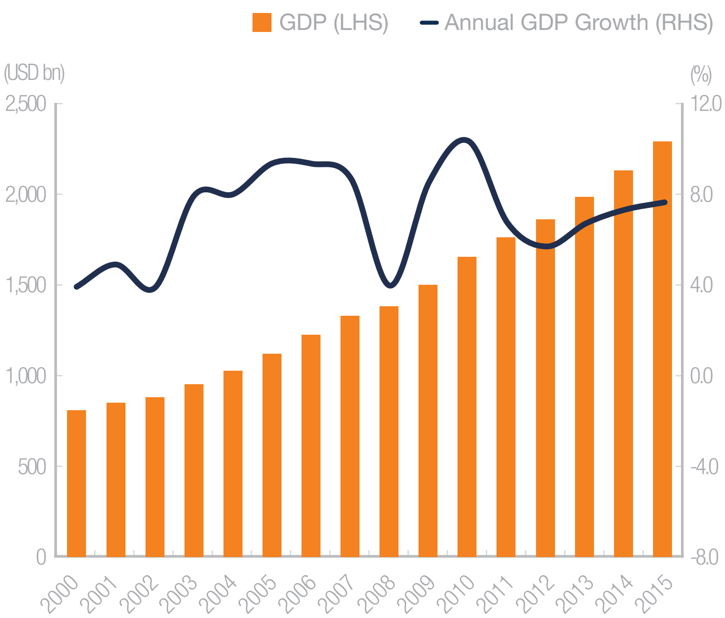
India was in a strong bull market with many "pie in the sky" stories when I first started managing the Indian equity strategy in 2006. Then, in 2007-2008, it was in a period of hubris with Indian corporates believing that foreign investors had limited options as attractive as India. Infrastructure companies were valued for growth optionality of new projects baking an almost perfect execution. Outbound acquisitions of Corus by Tata Steel, Jaguar Land Rover by Tata Motors, or Novelis by Hindalco were examples of the zeal of Indian corporates to build global footprints.[2]

[1] Morningstar Direct, Indian Equities, including both off-shore and on-shore peers (387 total investments ranked), Mirae Asset Global Investments (December 2016). Return metrics include annualized returns, Sharpe ratio, information ratio, upside capture ratio, and downside capture ratio.

[2] Various media reports and Company Disclosures, Mirae Asset Global Investments (2017)

India: Land of Growth

Source: World Bank Development Indicators, Mirae Asset Global Investments (2017)



Over subsequent years, it was a much more sobering experience where reality and execution were revealed to be much tougher than perception and management talks. This was exacerbated by a global downturn, domestic environmental concerns, and excess raw material unavailability pushing back large-scale power and commodity projects. The high cost of capital, overly ambitious expansion plans, and execution delays resulted in wiping out some companies' equity.

This is why I am convinced that quality is key. There are segments of the Indian market we avoid. For the rest, I try to look for sector-leading companies with scalable business models, directed by strong and clean management. The focus is on quality, to make sure we don't have the kinds of holdings that could undermine the portfolio.

What I look for in businesses is predictability, but this certainty has to come at a reasonable price. Buying good companies at any price is a fallacy. If you can find predictability on a consistent basis, and have a bit of luck, you have the recipe for long-term consistent success.

> *“Buying good companies at any price is a fallacy.”*

It is also important to be close to the consumer, observing their wants and needs, and their consumption patterns. I want to find companies that understand their consumers and have clear strategies in place to monetize them. For example, Godrej Consumer Products' success has been a result of its ability to fulfil consumers' desire for hair color products by providing L'Oreal-like products at the India price point. Similarly, Maruti Suzuki was able to do the same in the passenger car market. Not only have these companies been successful in introducing consumers to their respective product categories, but they have also been at the forefront of innovation to remain relevant to consumers as they moved up the value chain.

Lastly, and certainly more importantly, I cannot take full credit for the performance – this is a team effort. My most productive work is often done in the coffee shop across the street from our office where I regularly have informal sessions with my research team. I have a team of analysts in Hong Kong with a regional scope as well as a team in Mumbai dedicated to Indian equities that provide invaluable inputs into the strategy. I attribute a big part of our success to our privileged position of having boots on-the-ground without losing the regional perspective.

3. How do you manage risk in your portfolio?

Risk management starts and ends with the quality of businesses we invest in. I like to think of this strategy as a “sleep-well” strategy, where the companies we own should not give us, or our investors, sleepless nights. Of course, we have an independent risk team that helps us monitor portfolio risk in terms of tracking error, sector deviation, etc., but this is secondary. The first line of defense against portfolio tail risk has to come from the underlying quality of the companies we own.

> *“I like to think of this strategy as a “sleep-well” strategy, where the companies we own should not give us, or our investors, sleepless nights.”*

However, as mentioned earlier, we do not seek quality at any price. One important type of risk to manage in a high growth market such as India is the risk of de-rating. Execution is always challenging in India, so it pays to have a margin of safety in terms of valuations. The quality of the company is a prerequisite; valuation comfort determines its weight in the portfolio.

Portfolio management is a relay race where different parts of the portfolio are exposed to different economic drivers. In addition, having companies at different stages of their respective investment theses can also contribute to greater consistency of return over time.

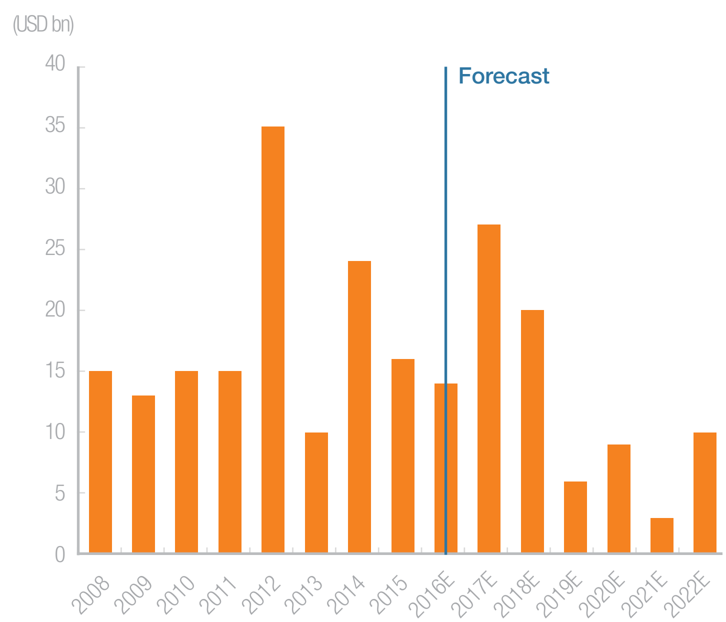
4. What kind of business models do you find appealing and what has been your biggest triumph?

Again, we try to look for businesses with predictability in earnings. The best of these businesses very often come in “large white spaces” in the economy, or structural growth areas that are still being underserved. However, this is only 20 percent of the job. The balance of time needs to be spent on company management and how it innovates to cater to its end consumers.

Indian pharmaceutical companies such as Lupin have been a success story for us. The story here is about companies expanding their reach through scalable economic moats. They have been able to apply their technical know-how from the domestic market and turn that into an attractive proposition for the US generics market, allowing them to grow from nothing to almost USD 1 bn (nearly 50% of total sales) in a period of 8-10 years.[3]

US Patent Expiries: Large Profitable Opportunity

Source: Credit Suisse, IMS Health, Mirae Asset Global Investments (2017)



[3] Mirae Asset Global Investments (2017)

Another good example has been Motherson Sumi Systems, an auto parts manufacturer. When dealing with Indian companies, you are always cautious regarding "big mouthed" management who overpromise as most of them fail to scale up. This is a company that is growing well, with return on equity (ROE) north of 30 percent, and it has not raised external financing in the past 15 years. Putting all the numbers aside, it is a company run by excellent management. With a keen focus on delighting their customers, they have been able to grow from their humble beginnings of supplying to domestic car companies, to becoming an important supplier for global players like Daimler and BMW. We bought the stock in 2010 and sold it in 2016 after the share price increased nearly six-fold.

5. Could you discuss some of your failures and most important lessons from the past decade?

I have certainly made my fair share of mistakes in the past 10 years. One of such missteps was in relation to a waste water treatment company. As we had experienced the level of pollution first-hand in India and witnessed this theme do very well in China, we saw a lot of potential in this sector. What we did not account for was that the order flows, which came from local governments, were delayed more often than not. Again, going back to what we've discussed earlier, execution is always more challenging. The key lesson was that having a margin of safety is crucial, especially when investing in a company whose customer is the government. That said we remain patient and recent activism by Supreme Court on mandating effluent treatment for industrial units should be a significant positive.

On the other hand, I have also made mistakes in terms of missing out on strong rallies. Motherson Sumi Systems, which was discussed earlier as one of our better investments, is also an example where we sold early as we became uncomfortable with the company's ability to meet investors' high expectations. After having returned nearly six-fold in six years, the market was pricing the stock at a price to earnings ratio of 25 on two-year forward earnings and a high sales base of USD 8 billion.[4] While we still saw it as a great company, it had limited valuation support. We exited the stock in 2016, meaning that we were not able to capture the final 30 percent upside.

As we reflect on this missed opportunity in hindsight, we would likely make the same decision now if faced with a similar situation. Discipline pays. We would be happy to miss out on the final stages of a rally if it means being able to avoid large swings in the portfolio and achieve greater consistency in returns. Hopefully we would then be able to redeploy capital into more attractive investment opportunities.

"Discipline pays. We would be happy to miss out on the final stages of a rally if it means being able to avoid large swings in the portfolio and achieve greater consistency in returns."

6. How do you foresee India developing in the next 10 years?

India's next 10 years will be all about productivity improvement. One vital area of improvement is in infrastructure. To offer a personal example: I used to spend close to three hours a day commuting on trains when I was in Mumbai over 10 years ago, which took a lot of my energy. When I arrived in Singapore and Hong Kong my commute time was cut to 30 minutes. This is a simple personal example, but one can imagine the positive impact that reverberates throughout the economy when this happens across the country. In addition, infrastructure is not

[4] Company Disclosures, Mirae Asset Global Investments (2017)

only limited to physical infrastructure such as roads and rail, but also through technology-enabled efficiency gains such as unique identification and e-governance.

I am also hopeful that the government will remain on its path to becoming a cleaner government with less crony capitalism. We have already seen the turning point under the Modi government. India's tremendous potential has always been there, and the people are hungry to prosper and do better in life. What the government has done, and hopefully will continue to do, is create the enabling conditions for India to realize its potential.

With that said, technology is not only being used by Modi's government as a key enabler in government-business and government-citizen interaction, but it also serves as the political leadership's biggest challenge. The test of credibility for the government will be its ability to create 10 million to 12 million jobs annually in this automation-driven world so that India's young population becomes a dividend rather than a mass of disruptive, restless energy.

Many Indians living overseas joke that we Indians do well when we leave India. Highly likely this changes in the next 5-10 years.

Global Offices

Mirae Asset Global Investments
12F, Tower 1, 33, Jong-ro, Jongno-gu,
Seoul, 03159, Republic of Korea
Tel.+82-2-3774-8200

Mirae Asset Global Investments (HK)
Level 15, Three Pacific Place, 1 Queen's
Road East, Hong Kong, HK
Tel.+852-2295-1500

Mirae Asset Global Investments (UK)
4-6 Royal Exchange Buildings,
London, EC3V 3NL, United Kingdom
Tel. +44-20-7715-9900

Mirae Asset Global Investments (USA)
1350 Avenue of the Americas,
33rd Floor, New York, NY, 10019, USA
Tel. +1-212-205-8300

Mirae Asset Global Investments (Taiwan)
6F, NO. 42, Sec.2 Zhongshan N. Rd.,
Taipei City 10445, Taiwan (R.O.C)
Tel. +886-2-7725-7555

Mirae Asset Global Investments (India)
Unit No. 606, 6th Floor, Windsor Building
Off. C.S.T Road, Vidyanagari Marg.
Kalina, Sanatacruz (East), Mumbai
400 098, India
Tel. +91-22-6780-0300

Mirae Asset Global Investments (Brazil)
Rua Olimpíadas, 194/200,
12 Andar, CJ 121, Vila Olímpia
São Paulo, CEP 04551-000, Brazil
Tel: +55-11-2608-8500

Disclaimer

This document has been prepared for presentation, illustration and discussion purpose only and is not legally binding. Whilst complied from sources Mirae Asset Global Investments believes to be accurate, no representation, warranty, assurance or implication to the accuracy, completeness or adequacy from defect of any kind is made. The division, group, subsidiary or affiliate of Mirae Asset Global Investments which produced this document shall not be liable to the recipient or controlling shareholders of the recipient resulting from its use. The views and information discussed or referred in this report are as of the date of publication, are subject to change and may not reflect the current views of the writer(s). The views expressed represent an assessment of market conditions at a specific point in time, are to be treated as opinions only and should not be relied upon as investment advice regarding a particular investment or markets in general. In addition, the opinions expressed are those of the writer(s) and may differ from those of other Mirae Asset Global Investments' investment professionals.

The provision of this document shall not be deemed as constituting any offer, acceptance, or promise of any further contract or amendment to any contract which may exist between the parties. It should not be distributed to any other party except with the written consent of Mirae Asset Global Investments. Nothing herein contained shall be construed as granting the recipient whether directly or indirectly or by implication, any license or right, under any copy right or intellectual property rights to use the information herein. This document may include reference data from third-party sources and Mirae Asset Global Investments has not conducted any audit, validation, or verification of such data. Mirae Asset Global Investments accepts no liability for any loss or damage of any kind resulting out of the unauthorized use of this document. Investment involves risk. Past performance figures are not indicative of future performance. Forward-looking statements are not guarantees of performance. The information presented is not intended to provide specific investment advice. Please carefully read through the offering documents and seek independent professional advice before you make any investment decision. Products, services, and information may not be available in your jurisdiction and may be offered by affiliates, subsidiaries, and/or distributors of Mirae Asset Global Investments as stipulated by local laws and regulations. Please consult with your professional adviser for further information on the availability of products and services within your jurisdiction.

Australia: Mirae Asset Global Investments (HK) Limited is exempt from the requirement to hold an Australian financial services license in respect of the financial services it provides in Australia. Mirae Asset Global Investments (HK) Limited is authorised and regulated by the Securities and Futures Commission of Hong Kong under Hong Kong laws, which differ from Australian laws. For Wholesale Clients only.

Hong Kong: Before making any investment decision to invest in the Fund, investors should read the Fund's Prospectus and the Information for Hong Kong Investors of the Fund for details and the risk factors. Investors should ensure they fully understand the risks associated with the Fund and should also consider their own investment objective and risk tolerance level. Investors are also advised to seek independent professional advice before making any investment. This document is issued by Mirae Asset Global Investments and has not been reviewed by the Hong Kong Securities and Futures Commission.

United Kingdom: This document does not explain all the risks involved in investing in the Fund and therefore you should ensure that you read the Prospectus and the Key Investor Information Documents ("KIID") which contain further information including the applicable risk warnings. The taxation position affecting UK investors is outlined in the Prospectus. The Prospectus and KIID for the Fund are available free of charge from http://investments.miraeasset.eu, or from Mirae Asset Global Investments (UK) Ltd., 4th Floor, 4-6 Royal Exchange Buildings, London EC3V 3NL, United Kingdom, telephone +44 (0)20 7715 9900.

This document has been approved for issue in the United Kingdom by Mirae Asset Global Investments (UK) Ltd, a company incorporated in England & Wales with registered number 06044802, and having its registered office at 4th Floor, 4-6 Royal Exchange Buildings, London EC3V 3NL, United Kingdom. Mirae Asset Global Investments (UK) Ltd. is authorised and regulated by the Financial Conduct Authority with firm reference number 467535.

United States: An investor should consider the Fund's investment objectives, risks, charges and expenses carefully before investing. This and other important information about the investment company can be found in the Fund's prospectus. To obtain a prospectus, contact your financial advisor or call (888) 335-3417. Please read the prospectus carefully before investing.

India: Mutual Fund investments are subject to market risks, read all scheme related documents carefully.