For professional clients and/or qualified investors only

Q1 2023 Investor Note

Responsible Global Emerging Markets Strategy

Contents:

Key risks

The value of investments and any income derived from them can go down as well as up as a result of market or currency movements and investors may not get back the original amount invested and in a worst case scenario there is a risk of total loss.

This document does not constitute, and should not be construed as, investment advice or a recommendation to buy, sell or otherwise transact in the fund.

Investing in emerging markets is generally considered to involve more risk than developed markets.

Investments may not be suitable for all investors and independent professional advice, including tax advice should be sought, where appropriate.

Screening out sectors or companies may result in less diversification and hence more volatility in investment values.

Impact Investing – Stakeholder primacy

"*It's one thing to feel that you are on the right path but it's another to think that yours is the only path.*" Paulo Coelho

Monopoly is one of the top 3 best-selling board games in the world and originated in the early 20th century when it was designed by Elizabeth Maggie, an outspoken activist for the feminist movement. The game was called the 'The Landlord's Game', showcasing the negative aspects of concentrating land in private monopolies. The interesting aspect of this was that she created a game with two sets of rules:

- a monopolist set, which those of us who have bitterly played the game against family members recognise, that is based on accumulating as much property as possible and crashing opponents by bankrupting them.
- an anti-monopolist set also known as the 'Prosperity' set of rules, which rewarded all the players when wealth was created.

> We like to apply the concept of doing well by doing good.

When the game was acquired by Parker Brothers (today owned by Hasbro) in the early 30's, the concept that was put on sale was only the monopolist set, i.e. the one that can only have a single winner. Most who played the game had only one main goal, to swiftly bring opponents to the brink of bankruptcy. Who knew all along that we could finish the game without the feeling of animosity around the table, especially among family members who were captive players during what were supposed to be festive holidays. The monopolist set was good at illustrating the opposite intention of the game's founder by awakening our animal spirits. It made us forget that everyone could have walked away from the table feeling decent, generous, and collaborative. As the basketball legend Michael Jordan once said, talent wins games, but teamwork and intelligence win championships. Investing in progress does not have to be a binary outcome but can instead be a multifaced circular process for key stakeholders that enables better outcomes.

In line with the above, over the past century we have seen the notion of shareholder primacy take the lead across the globe and become the base argument for governance of the corporate world. During the same period, academia ran ahead with Adam Smith's rational-economic man, whose motivation was to base his acts on solely rational self-interest, all of which centres around selfishness and the concept that there could only be a single winner.

Fortunately for our generation, this century is poised to be shaped with a different mindset, shareholder primacy, whereby a shareholder-centric form of governance focusses on maximising the value of stakeholders along with shareholders of course. We like to apply the concept of doing well by doing good. It starts with doing no harm, and for us this means avoiding companies that have unsustainable business practices. Then it centres around the concept of focusing on companies that are adding value to their stakeholders as a means to generate shareholder returns, what we like to call positive contribution to society and environment. Both qualitatively and quantitively, working side by side with our in-house Responsible Investment team, we ensure our companies fulfil this requirement. We then can share with you how we conclude that our investee companies deserve our client's capital and ultimately how they impact their key stakeholders in a positive fashion and contribute constructively to their societies and environments.

To understand this further, we spend an immense amount of time engaging with our businesses to understand, nudge, and influence them to achieve certain milestones. Our goal is not to push down our values or views'; rather, we focus solely on materiality in our engagements. Materiality can come in many forms or shapes relative to our business. Here we benefit substantially from the expertise of the RI team members who specialise in different verticals, from cyber security to carbon emissions. They provide further understanding around the risks present in different sectors, countries, or specific sub-industries given their worldwide coverage. With the strong research intensity provided by both the investment team and the RI team, we can identify key material risks present for our companies, and we then engage with them with to mitigate these material risks and, where possible, turn adversity into an advantage.

An extension of the stakeholder supremacy remains is what a circular economy is built upon, i.e. providing a way to not only protect the environment but also use natural resources more wisely, develop new sectors, create jobs, and develop new capabilities. Taking a long-term view is embedded in our investment philosophy to ensure we remain committed to creating circular benefits.

We do this largely because sustainable returns require sustainable development. To achieve this, our analysis considers what a company is doing to stay below the ecological ceiling. A few of the areas of focus include:

- enabling a circular economy
- using rain harvesting as a sole means to source water for manufacturing
- focusing on bringing down energy and water usage every year while producing the same or a better product
- ensuring the supply chain is financially supported and remains resilient
- empowering women in rural communities through financial inclusion and education
- providing affordable education to young minds across the different layers of society
- enabling access to medicine at affordable prices for the masses

All the above requires companies to take a long-term view and have a long-term vested interest in the success of a strong social foundation while remaining within the boundaries of an ecological ceiling.

We do our homework to see where our companies can have the biggest impact considering their business model through our rigorous research process and targeted engagement. Most importantly, we incorporate a nuanced view that GDP per capita is not the only metric to consider when analysing what makes an emerging nation successful or not. The same can be said for when we analyse a company—it is not down to financial success only, but a good investment case relies on how our investments contribute positively to its key stakeholders and whether that is sustainable long-term. The role of alternative metrics to assess the societal and environmental impact of companies, alongside the financials ones, is what we excel in to ensure that we are right stewards of our clients' capital, acting in the best interest of the long-term wellbeing of the citizens of the emerging world to generate sustainable returns for our clients.

> "We do our homework to see where our companies can have the biggest impact."

Investment Case Study – FPT Vietnam

FPT has three main business lines: Technology (software, outsourcing, IT Services), Education (related to IT), and Telecoms (broadband internet provider) in Vietnam.

History – FPT (Financing and Promoting Technology) was founded in 1988 by Russian-trained Vietnamese engineers taking advantage of Vietnam's opening to a market economy. FPT grew to be the largest import/trader of Information and Communication Technology equipment in Vietnam. During the Asian Financial Crisis (1997), the company was close to bankruptcy due to its foreign currency exposure and sensitivity to economic cycles. Having learned their lesson, the company embarked on a strategy to offset the short USD position by exporting IT outsourcing from Vietnam. To build and obtain these skills required FPT to set up its own university and training centres. While importing and selling IT equipment (both B2C and B2B) in Vietnam, FPT vertically integrated by setting up a joint venture (JV) with the government to launch a fix broadband operator.

FPT is ideally positioned to harness the secular growth of the global IT outsourcing market, increase in Vietnamese IT software/service market, the Vietnamese private education market, and the steady growth of broadband and IT infrastructure penetration in Vietnam.

IT outsourcing, domestic self-develop software and private education in Vietnam, are the fastest growing, most profitable, value-creating, cash generative, and most competitively advantaged business units at FPT. The least value creating business units have been divested over time.

> "FPT is ideally positioned to harness the secular growth of the global IT outsourcing market."

Both **Customers** and **Communities** benefit from the operations. As an illustration, FPT provides global IT services and software enabling companies to improve productivity, digital experience, and move onto the cloud amongst other services. This benefits both the client and their customer communities. In Vietnam they work with both the government and private sector including SMEs. From an Education perspective, FPT builds and operates universities and training centres, which benefit society by building a highly skilled technology workforce. Last year, FPT's Education surpassed the milestone of having 108,100 full-time equivalent students registered throughout the system, becoming a mega-scale educational organisation. They have also entered the lower end of the private education market to provide affordable, higher-quality education. Their telecom arm provides infrastructure to enable better connectivity for all of society.

Employees and Culture: Employee retention is key for the IT services business. FPT's overall employee turnover was 17% in 2022, among the lowest in the sector. This is down from 28% in 2019, showcasing the benefits of addressing the needs of the workforce through compensation and benefit redesign. FPT has historically strived to keep equal and fair opportunities for all employees, despite the tech sector historically having a high percentage of male employees. In 2022, the number of female employees accounted for 38.1% of the total, and the number of female managers and leaders grew by 19.6% over the same period, accounting for 34.6% of the total managerial positions. The company has a fair and transparent income policy, which means employee income is solely based on performance, position, and contributions.

The **Environmental** impact of FPT's activities is small and thus immaterial to the investment case. FPT's focus is on the environmental footprint of its real estate portfolio (education campuses, schools, and IT consulting campuses). The construction of all its buildings incorporates the latest technologies and design knowledge to lower the resource intensity and negative emissions from both the construction at inception and usage during the building's lifetime. As an example, the 5.9-hectare FPT Complex, the largest such IT service centre in central Vietnam, has been recognised for Excellence in Design for Greater Efficiencies by Vietnam's Construction Ministry and the World Bank for achieving a 20% savings in energy, water, and use of materials. The campuses are also designed to foster higher productivity, collaboration and employee satisfaction. FPT's sustainability principles also apply to tier 1 suppliers and ESG factors are considered in all procurement decisions.

Shareholders have benefitted from FPT's track record of execution, capital allocation discipline, governance, risk management, and culture leading to the topline growing 7x and operating profit growing 5x over the past decade.[1]

[1] Source: Data referenced from FPT Annual Report 2022

Travel log – Indonesia

During February, we visited Indonesia for the first time since the pandemic spending five days meeting with executives, stuck in traffic jams, visiting wet markets and modern retail malls, gathering insights and generating further conviction around our companies' competitive moats.

Indonesia's potential is huge. The building blocks are in place to becoming an ASEAN superpower. The country is blessed with an array of natural resources, both hard and soft. Indonesia is the world's largest exporter of palm oil and thermal coal and as a local commentator quickly pointed out… 'you can grow anything on Java.'

Many of the consumers, management teams and colleagues we talked to were generally very confident in the direction Indonesia was heading, the only real concern being the election in 2024. Throughout his 2nd term, President Joko Widodo (Jokowi) has been able to plan and more importantly, execute, implementing reforms and policies which have been supportive of growth including:

- Infrastructure spending – 1,700km in toll roads – 9x longer than the roads constructed under the previous leadership era, 30 reservoirs, 18 ports and 21 airports all constructed in the first 8 years of the Jokowi leadership[2]. More importantly, the majority of this spend has come outside of Java – including the headline $39bn build of the new capital city, Nusantara.
- Downstream development of the commodity industry, whereby the country processes its raw materials into products of higher value.
- The government has eight priority sectors from fisheries to oil and natural gas, covering twenty-one commodities in total.
- Upcoming Labour and Land law reforms targeting the lower income segment to help provide an even playing field.

> "The building blocks are in place to becoming an ASEAN superpower."

As per The World Bank, poverty as a percentage of population has fallen from 23% in 1999 to 9.5% in 2022 yet inequality remains an issue that Indonesia is trying to address. Geographic difficulties (7,500 islands), education inequality and concentrated economic growth on Java are headwinds that the country must overcome. We believe some of our investments in the country are playing a key role, particularly in empowering the female population who are often disenfranchised through access to finance, as well as education.

[2] https://www.pwc.com/id/en/media-centre/infrastructure-news/september-2022/jokowi-builds-1700-km-toll-roads-2-1-times-the-length-of-the-previous-era.html

More recently, Indonesia has flexed its geopolitical muscle. Jokowi's recent visits to both Moscow and Kiev were seen as an attempt for peace keeping talks and demonstrative of Indonesia's neutral status. Indonesia also hosted the G20 in Bali, further illustrating Indonesia's growing presence in the region. All are hoping that the policy momentum continues. The real fear that many locals highlighted was that Indonesia returns to a period of 'auto-pilot' – a period of substantial planning but little execution as has been witnessed in the past.

During our visit, we spent a day with **Bank Rakyat (BRI)** which we invested in, in Q4 2022. Bank Rakyat is unlike any bank globally and to fully understand the business model, being on the ground is important. We spent time with a regional loan officer in a branch and a BRILink agent in a local wet market as well as the management team.

Bank Rakyat operates a hybrid banking model specialising in micro-loans, savings, and insurance products in Indonesia (targeting 165mn people and 62mn businesses). The long-term growth opportunity for BRI is attractive, 51% of the population are unbanked[3]. The 51% lack the financial tools (savings, payment services, access to credit, risk management tools) which present a hurdle to generating wealth and driving economic prosperity. Bank credit in Indonesia only covers 17% of population. BRI are striving to bridge that gap. BRI's ambitions are aligned with the government who are aspiring to achieve 90% financial inclusion by 2024.

An hour with a loan officer at a Bank Rakyat office was a stark contrast to visits to banks in the UK. The loan officer was fully digital. No desk, no computer, no paper. Armed with an iPad, the officer completes all Know Your Client information, documentation, sales pipelines, on the road and face-to-face with customers. Approval days for many products have been reduced from 20 days to just one. The level of efficiency seems years ahead of developed world banks.

BRILink Agents- we spent some time with a BRILink agent in a Jakarta wet market. The agent is a key touchpoint between the bank and the local merchants, facilitating cash deposits, cash withdrawals, support on bill payments as well approving small loans.

In many instances, the agent also runs a Warung (small shop). Not only is the agent supporting increased financial inclusiveness for the merchants but also supports their income from the store takings. The agent had a relationship with all Warung owners in the wet market, forming a significant barrier for competition to try and displace. Further, BRI have 650k BriLink agents around the country covering 80% of total Indonesian villages, facilitating people in remote areas to utilise banking services and promote financial inclusion. The decentralised structure improves the economics of micro lending and builds strong customer relationships.

It is only when you are on the road, seeing business in action, that you can fully grasp the idiosyncrasies of such business models.

Engagement Update

We engage with companies to encourage them to develop business-relevant and impactful sustainability strategies, and to clearly assign oversight responsibilities for their implementation to management and the board. The purpose of our engagement is both to mitigate risk and benefit from opportunities over the mid-to-long-term. We record every interaction and milestones we achieve and are happy to share these details with our clients upon request.

During the quarter we conducted 15 engagements with 9 of our investments and achieved 4 milestones. Many of these engagements were in Asia, specifically focused on Corporate Governance and Climate Change. Environmental Standards is the area where we have achieved the most milestone success during the quarter. From a Sustainable Development Goal language, we have predominantly engaged and achieved success on SDG 12 (ensuring sustainable consumption and production patterns).

Notable engagements during the quarter included our Chinese investments, **Hualan Biologics** and **Tencent**, and **Biocon** in India.

We engaged with **Tencent** on three different occasions, on various subjects ranging from human rights, data privacy, diversity, equality and inclusion, which also includes dialogue with a senior board member. In our engagements, we outlined our expectations based on previous dialogue and included an outstanding question on its government data request policy for its Chinese platform. We encouraged conducting human rights due diligence to identify, prevent, and mitigate actual and potential human rights risks in its operations and supply chain, as well to identify any risks posed by its products. We also recommended disclosure on government data requests, and where not possible due to the legal and regulatory environment, to publicly state this is not possible. We also recommended disclosing intersectional diversity data after the publication of its detailed workplace representation and attrition data for the first time. We also provided best practice examples for each of our recommendations and will follow up in the next quarter on progress. We continue to monitor the situation and will follow up with the company over the coming quarters.

With **Hualan Biologics** we engaged on its reporting and

> "Environmental Standards is the area where we achieved the most milestone success during the quarter."

[3] source: https://theasianbanker.com/finance-indonesia-2022/

governance structure with the aim of understanding its ESG progress and how it plans to improve relevant disclosure. We suggested the company focus on improving its ESG rating as the priority. We mentioned that it has separated the combined CEO and Chair roles since its AGM last year, and it can communicate with rating agencies about this change and any other discrepancies found in their reports. We also recommended that the company issue a standalone ESG report, and it should start from areas that are flagged up in the materiality assessment. For example, SASB recommends pharmaceutical companies focus on product safety and quality, access to health care and human capital management as priorities. We also encouraged the company to include its meaningful social activities in a formal report. The company has donated 180,000 flu vaccines to many developing countries such as Cambodia, Albania, Moldova and Mongolia, since 2015. Lastly, we also encouraged the company to disclose the results of its environmental management, such as scope 1 and 2 emissions and toxic material management.

With **Biocon**, we sent a letter to the board regarding its EGM proposals (predominantly remuneration and board regulatory related) and in response we had a very inspiring discussion on the company's ESG reporting. We advised them to disclose time-bound targets and Scope 3 emissions, as doing so is considered best practice and an increasing number of peers are already doing this. We also spoke about the company's high employee turnover rate, which Biocon stated was linked to India's year of the 'Great Resignation'. They are confident that they will retain more staff in the coming year. The company also explained that their near-miss incident rate doubled because there is more awareness of workplace health and safety and therefore staff report more incidents. We considered the company very receptive to our feedback and will follow up with them once we review the newly published ESG report.

Voting

One of the core pillars of our investment process and philosophy is active ownership, i.e., engagement and voting. On the latter, we believe that we have a duty as shareholders to use our votes to send a clear message to the boards of the companies that we own, about improvements they can make in their corporate governance practices. We, therefore, exercise our right to vote across all our holdings.

Starting with the high-level numbers, during the quarter we voted at shareholder meetings for 8 of our companies. Out of the 61 resolutions, we voted on, we voted 'For' management for 90% of these and 'Against' management for 5%. We abstained in 3.3% of the votes, and the final 1.7% was on Management Say on Pay.

We will highlight two of the case studies this quarter where we voted against management. We voted against the Chairman of Wal-Mart de Mexico as the company does not have a three-committee board structure (audit, remuneration and nomination), in line with regional best practice. While the company have an audit and corporate practices committee, there is no evidence of a nominations committee or a remuneration committee. Our custom policy is to vote against the Board Chair, where a three-committee structure is not in place, in markets where this is common.

The second case study is Naver, where we voted against a Board Director Election. This nominee was flagged for review as we consider him to be over-boarded. He serves as the Chairman of Naver while also serving as the executive Chairman of Alticast Corp. He also serves as Chairman/CEO at Humax Holdings and executive Chairman of Humax Co where he is the founder; we would consider this situation one company given the structure. We generally expect executives to hold only one outside directorship given the time it takes to fulfil the executive role. Further, we view Chair positions as more time intensive than non-Chair positions given the role of the Chair on the board. The nominee also serves as Chair of the compensation committee and is a member of the nominating and ESG committees at Naver. While he has attended all the board meetings at Naver, this nominee has three chair positions, two of which are executive positions. Given the significant roles he must take on for each of the boards, we consider him to be significantly over-boarded.

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Risks and Opportunities around our Banks

The financial headlines this year have been dominated by the events that unfolded for the likes of Silicon Valley Bank, Credit Suisse, and First Republic Bank. Consequently, we have had many enquiries about whether our banks are exposed to similar risks. While risks are everywhere, in particular for banks which have inherent leveraged exposure to the underlying economies, we do not believe the risks causing the downfall of such large financial organisations are applicable to our banks.

Banking in general is mature and undifferentiated in the developed world and with the various government-backed deposit insurance schemes, most of the depositors are ultimately protected by the financial regulators. In a very competitive environment with low interest rates, it becomes difficult to make favourable returns and this can lead to banks being open to seek other means to generate returns. For SVB, this was due to their assets and liabilities not matching with a poor risk framework. For Credit Suisse, it was an ongoing

problem, resulting in trust being eroded over many years. Banking is fundamentally an industry of trust. Trust of hard-earned savings being given to an institution and trust that that capital will remain intact over years to come. It is hard to build and easy to destroy.

Our main banking exposure is across India and Indonesia. The funding base for our investments is predominantly deposits (Current and Savings accounts) with very little concentration (unlike SVB), which can impact the withdrawal of funds in a run scenario. We have seen year after year, even in difficult periods (Covid, GFC, AFC) these banks have continued to grow their deposit base, and the main reason for this stickiness and trust is the companies' reputation in being conservative in their approach to risk. And being conservative in how they handle deposits leads to lower costs of capital. Deposits are dispersed efficiently as loans to businesses ranging from large corporates to SME's or quality retail clients. Lending responsibility means loan losses are lower vs the industry average, leading to the banks becoming stronger with each cycle, while peers run into issues that set them back even further.

> “We generally expect executives to hold only one outside directorship given the time it takes to fulfil the executive role.”

Other aspects that are worth mentioning are the fact that our banks are focused only on core products in domestic markets. Management teams/stewards of these businesses recognise their circle of competence of being good local banks while at the same time, local banking environments remains attractive simply because of credit penetration, access to finance, and product depth remains low (mortgages, credit cards). All of these are basic banking products and can be very profitable if done right in an environment of long-term demand.

It is also worth mentioning that the banks we have selected remains well capitalised versus western peers both in terms of liquidity and capital adequacy. A strong buffer is never bad, but the key is to maintain the trust, as a bank run is very hard to come out of. Based on our analysis and many years of investing and closely following our companies (we have held **HDFC Bank** for over 13 years), we remain confident that our banks remain resilient with strong social licenses to operate in their respective societies and governed by strong management teams that stick to their knitting.

Portfolio actions and considerations

During the quarter we sold out of our position in Colgate India due to slowing growth relative to its current valuation. We increased our position in **Max Healthcare**, **WEG**, and **Jeronimo Martins** with the residual from the sale.

The quarter was dominated by the ongoing China and US tensions and more notably with the ongoing challenges resulting from the collapse of two mid-sized US lenders in March, impacting the global financial stability. While we do have exposure to various banks in our universe, these are limited to strong domestic franchises, such as **HDFC Bank** (India) and **Bank Central Asia** (Indonesia). As mentioned above, these banks are well capitalised, catering to businesses and individuals on the lending side and acting as safe places for the hard-earned savings of local citizens. The cultures of these two organisations are similar, and conservatism is the key shared value that ensures they remain resilient and can take the long-term view in ensuring they lend to the 'right' type of clients. There is no denying that banks are leveraged investments and if management is incentivised the wrong way, it can cost equity holders substantially. That is why we avoid most banks in our universe, as they do not adhere to our high standards. When done right, the value creation and benefits coming from being exposed to a thriving underlying economy is unmatched. To understand this, we spend a lot of time analysing history (particularly in times of difficulty), the culture, and key decision makers' motivations (financially and non-financially) along with underlying financials to make them eligible for us to invest in.

We started the year on a positive note despite a choppy market environment and continue to remain encouraged by the incoming annual and early year results from our investments, despite the varying degree of difficulties faced in our markets.

Thank you for your trust and support.

CT Responsible Global Emerging Markets Team

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