



Why invest in Asia now?

Lloyd George Advisory (HK) Limited

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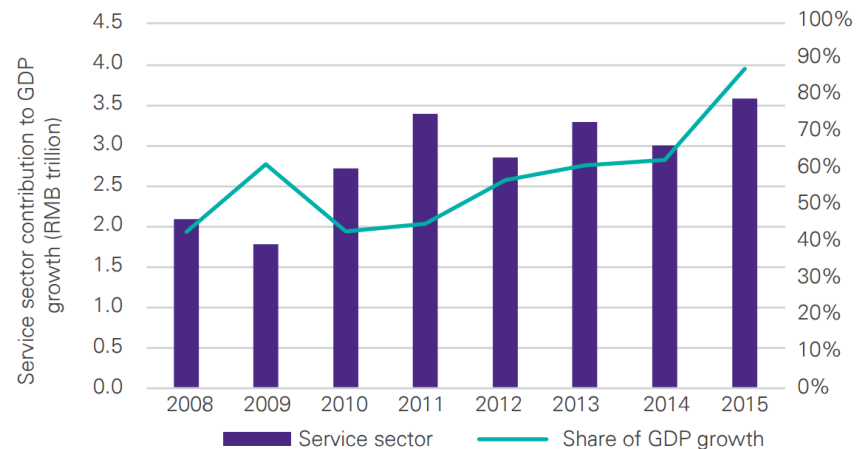
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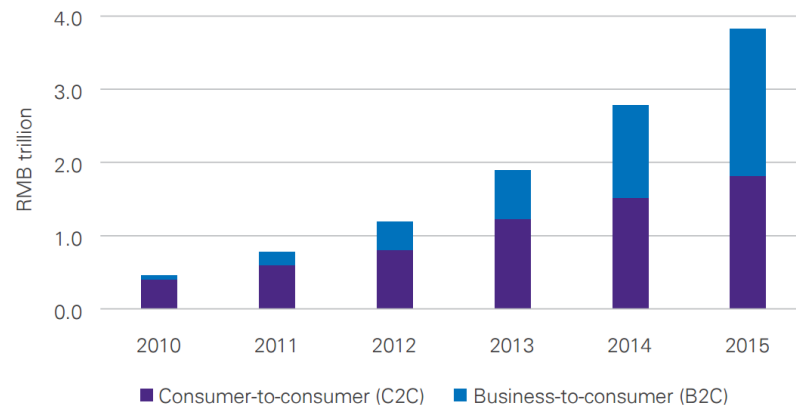
China: key drivers for 2017

- Growth stable at 6.5 to 6.7%
- Simplified tax regime to be implemented from 1Q 2017
- Continued political stability
- 2.3% Inflation expected
- US interest rate increase will benefit Chinese banks
- Currency weakness will be managed and is positive both for exports and for domestic consumer spending, investment
- 'One Belt One Road' is using excess industrial capacity and creating new markets for Chinese products
- As property seems expensive, new capital will flow instead to the equity markets
- As the US becomes protectionist under President Trump, China will be a key beneficiary of neglected markets
- China will create its own equivalent of the now-defunct TPP

Service sector's contribution to China's GDP growth

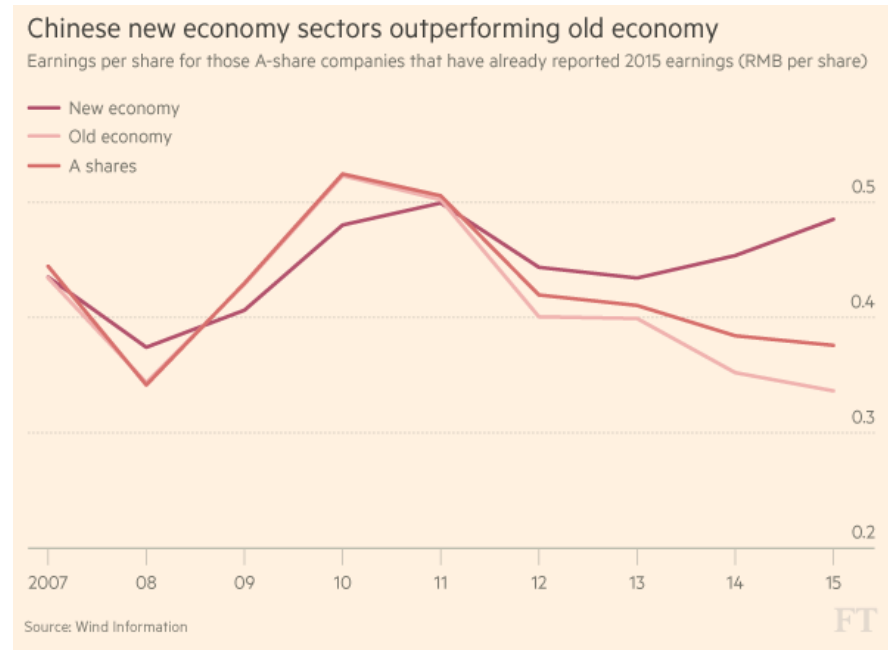


Online shopping in China 2010-2015



New Economy vs. Old Economy

- China's consumer-oriented "new economy" is propelled by service industries, technological upgrading and greener living
- "New economy" companies posted an average EPS of Rmb0.48 last year, up 6.7% from 2014, whereas "old" economy companies declined in average earnings per share to Rmb0.33, down - 5.7% from 2014
- In 2015, consumption growth accounted for 66.4% of China's GDP growth
- We highlight 6 key investment themes:
 - Healthcare
 - Education
 - Lifestyle
 - Internet
 - Environment
 - Travel
 - Technology
- With the opening of the Shenzhen-Hong Kong Stock Connect, we can now access New Economy of China directly, allowing us to have more niche exposure in China through H-shares, ADR's, and A-shares



Travel

Highlights (Outbound Travel):

- China's outbound travellers (excl. HK/Macau) are 120mn, and stand at only 4.1% of the total population, much lower than US (14% excl. trips to Mexico and Canada), Japan (13%) and Korea (25%)
- China's total outbound travellers should grow at 17% CAGR by 2020E, due to 1) increasing number of passport holders; 2) visa relaxations; 3) relatively stable RMB
- 2015-2020 CAGRs of 22%, 22%, and 23% in Chinese outbound travellers to Thailand, Korea, and Japan, respectively, which account for 43% of total outbound travellers
- Chinese tourists spent US\$215bn on outbound travel last year, a rise of 53% on the previous year (near 2x US levels)

Highlights (Domestic Travel):

- Currently China's per capita tourism spend is only USD188, lower than global average of USD333
- China's domestic tourist volumes have seen a 13% CAGR growth over past 10 years
- Scarcity of high-quality natural sites in China, with the number of visitors to China's Huangshan and Emeishan standing at only 0.21% of the total population, compared with 1% for US national parks
- China plans to build 100 airports and double the high-speed railway network coverage, which should contribute to visitor volume growth

Beneficiaries

SHENZHEN
AIRPORT GROUP
深圳机场集团



Shenzhen Airport

Gateway to China

Already an innovation hub, Shenzhen plans to become a global gateway city. Pax traffic from international routes grew 33.9% YoY, with % of international traffic increasing to 5.2% from 4.2% in FY15



Huangshan Tourism

Most famous mountain range in China

Operates cable cars, hotels, and travel services in addition to charging admission fees. Increasing accessibility due to a new high-speed railway, which will cut travel time from Shanghai to Huangshan from 9 to 2 hrs.



TravelSky

Monopoly GDS provider

A utility provider to airlines, ticket agents, and airports with ~90% market share, TravelSky acts as a general proxy play on the growth of the entire travel and tourism industry, both domestic and outbound.

Healthcare

Highlights:

- Healthcare spending is 5% of GDP compared to >10% for developed nations; more room to grow; spending projected to grow from US\$357bn in 2011 to US\$1tn in 2020
- Industry is expected to experience long-term growth due to:
 - **Aging population:** by 2050, nearly 33% of Chinese population will be >50
 - **Accelerating chronic disease prevalence:** for example, 11% of Chinese had diabetes vs. 9% in US. Pre-diabetes present in 40% of population ages 18-29, and 47% amongst 30-39
 - **Increasing government spending:** government committed to spend 6.5-7% of GDP to support a growth of Rmb8tn in the healthcare sector by 2020
 - **Expanding medical insurance coverage scheme:** government aims to have universal coverage across China by 2020
- However, near term challenges on the back of ongoing government efforts to reduce patient costs – these policies should force more consolidation, accelerate R&D approvals and encourage public hospital privatization (Phoenix Healthcare will be a beneficiary)

Examples:



Beijing Tonrentang

>300 years of TCM production

A third of drugs included on the 2015 Essential Drug List are TCMs, which are 100% reimbursable. TCM sales grew at CAGR of 24%. Beijing Tongrentang enjoys the strongest brand recognition.



Tonghua Dongbao

Largest insulin player

Chronic diseases like diabetes have seen increasing prevalence. Insulin business is more sustainable and predictable, and for Tonghua is growing at 23% CAGR and 30% profit growth for next three years.



Aier Eye Hospital

Largest private eye hospital chain

Myopia rising quickly in East Asia, and is in general linked to higher incomes, urbanization, and education. In Shanghai, 86% of high school students suffer from myopia. Aier has 60 branches across China.

Education

Highlights:

- 15% of government fiscal spending has been on education since 2010. Surpassing social security 11%, healthcare 7% and military 6%. Over the last 12 years, the annual spending on education has risen from RMB300bn to over RMB2.3tr
- Education takes a significant share of wallet spend. 2-19% of China household income is spent on education (comprised of 2-11% on school tuition, 1-9% on after-class tutoring) compared to Korea (17%), Japan (10%) and US (2%)
- The penetration rate of after-class tutoring from K-12 in China is at roughly 36%. From historical estimates, by 2020E, this number could reach 47%, representing a 5-Year CAGR of 16%
- Currently primary and secondary school education spend represents 2-3% of China's GDP and roughly 60% of total education expenditure in 2014
- Average admission rate of the top 154 universities in China is 9% compared to 28% of the top 50 universities in the US
- Chinese parents desire to send their children overseas with 73% of Chinese students studying at international schools going to the US, UK, Australia and Canada. Total enrolment numbers doubled from 2009-2013, and is expected to grow at a CAGR of 11.8% from 2013 to 2017 to reach 244,600 students by 2017. Over the past three years the international school market revenue has grown at a CAGR of 23%, and is expected to grow 17.9% in the next three years

Beneficiaries



TAL Education

Premium after-school tutoring

TAL grew their student enrolments to 788,320 students representing a 42.5% 6-year CAGR, while also growing revenue and net income at CAGR 41.2% and 33.7%, respectively in the same period



Maple Leaf

Dual BC/Chinese diploma intl. school

Asset light model with local governments to capitalize on recent education push for more PPP projects. 90% of students go to overseas universities, 51% of which go to Global Top 100 universities



51 Talk

Online 1-on-1 English lessons

Leveraging on cheap labour in the Philippines, 51 Talk offers online affordable proprietary English classes at a GPM 63.6%, in a market only 10% penetrated

Internet

Highlights:

- Internet usage has already penetrated over 50% of total China population, ~70% of population aged 15-64, and 74% of mobile phone users. We are entering a different stage of growth for the leading internet players, characterized by:
- **Shift from quantity to quality:** remaining user expansion will come from lower-tier cities, but marginal cost of user acquisition will increase and marginal revenue potential will decrease. Therefore, the internet story in China is shifting from “quantity” (user growth and penetration) to “quality” (user engagement and monetization) of existing users
- **Mobilizing user base:** big players with proven user engagement, particularly on mobile platforms, will be able to leverage their user-base to promote an increasingly broader array of value-added services. BAT (Baidu, Alibaba, Tencent) have a considerable advantage in this regard.
- **Content providers to lead:** high-quality content providers, which leverage on technological advances in online/mobile infrastructure, will also continue to enjoy rapid growth as . These include players in game development as well as online live video streaming
- **Monetization pressure from investors:** whereas the last few years were characterized by a frenzy of subsidized market share grab by the major internet players, with the Chinese consumer as the biggest beneficiary, O2O subsidies have dropped and will continue to do so as consumers pick up their willingness to spend

Examples:

Tencent 腾讯

Tencent
Internet giant

Wechat has an average daily time use of >1hr per user, a penetration of 93%/69% in tier 1/2 cities, capturing 52% of mobile internet time. This allows Tencent to tap into new growth opportunities in a low-cost way.

网易 NETEASE

www.163.com
NetEase

Leading game developer

NetEase is the top game developer in China with ~10%/23% market share in PC/mobile games. It has recently launched a cross-border e-commerce website to further service its user base, which now generates 20% of revenue.



ChinaNetCenter

Wangsu Science

Leading content delivery network provider

Because CDNs optimize Internet traffic, they are a proxy utility to the fast-growing online streaming video and other data-heavy applications. China's Internet traffic should accelerate to 26% YoY, benefiting Wangsu.

Environment

Highlights:

- The past few decades of growth in China were fuelled by an energy and resource heavy growth model
- In 2013, China accounted for 15% of global output and consumed between 45% and 65% of global copper, coal, aluminium, and cement. China emits more CO2 than the US and EU combined
- 60% of China's groundwater is unfit for consumption
- **50% of China's mass social incidents are pollution-related and increasing social pressure is forcing policymakers to act**
- Environmental protection law implemented in Jan. 2015, corporates face uncapped fines for environmental violations
- 13th 5-year plan has clear environmental targets like increasing non-fossil fuel energy to 15% and reducing emissions per unit of GDP by 40-45% by 2020. To reach these targets, environmental services investments will likely double to 2.5% of GDP
- Government is moving from investor to supervisor/promoter of PPPs and TPTs - investment multiplier effect
- Clean energy, autos, and water treatment will be the biggest beneficiaries

Examples:



Zhengzhou Yutong Bus

Largest new energy bus manufacturer

26% market share and strong R&D capability. Benefiting from EV subsidy policies. Sound financial management, 93% dividend pay out ratio. Increasing gov. scrutiny in industry increase barriers to entry.



China Yangtze Power

Pure play on hydroelectric power

Competitive landing tariffs put it in a better position than other hydroelectric producers and utilities. Future asset injections from SOE parent. Pledged DPO of 70% and low gearing compared to large hydro and coal IPP peers.



Beijing Originwater Tech

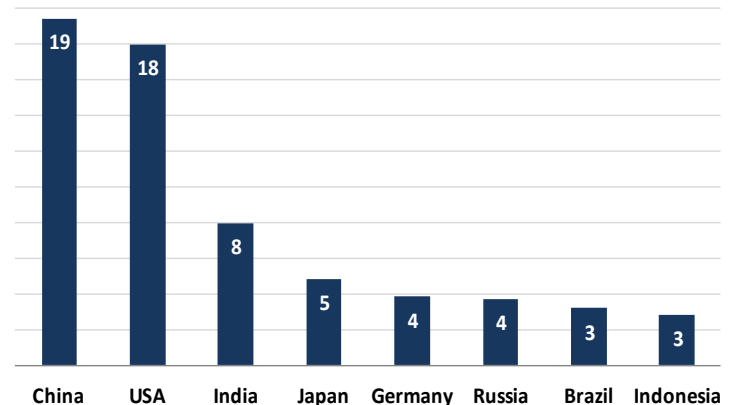
Wastewater treatment technology

Leader in membrane bioreactor (MRB) technology, which improves wastewater discharge and decreases land requirement by 50-70%. Critical for new urban WWT facilities and upgrades.

India outlook – Large growing emerging economy

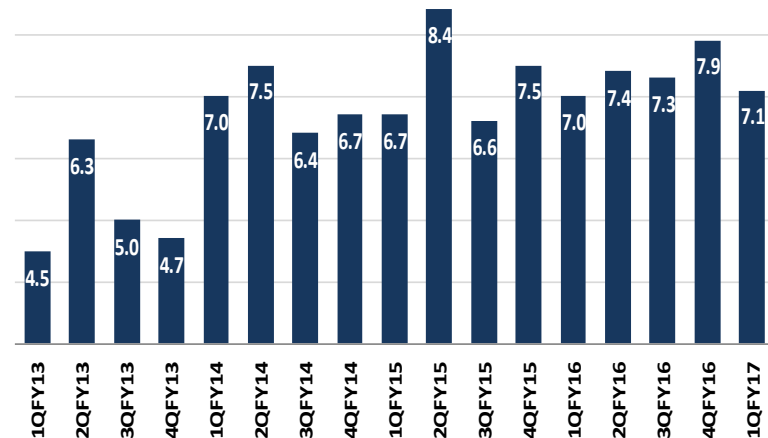
- Largest democracy in the world with a population of 1.31 bn accounting for 17.7% of the world population
- Third largest economy in the world in terms of GDP (PPP)
- One of the fastest growing economies with a GDP growth of 7%+
- Services sector dominating India GDP (~62%) unlike in other emerging markets
- Share of agriculture in GDP declining
- GDP growth can sustain
 - Young demography
 - Make in India – investment in infrastructure
 - On going reforms
 - Favourable macro

GDP (PPP; Int.\$ trn)



Source: IMF

Real GDP Growth Rate (% YoY)

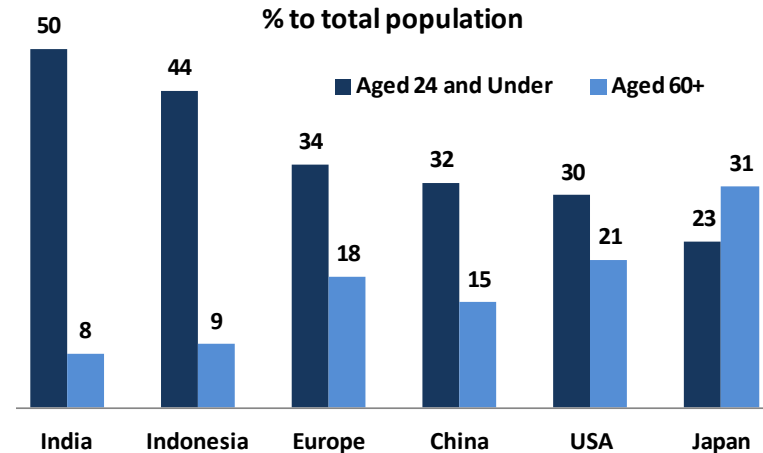


Source: MOSPI, Govt. of India

India Demography – Structural Advantage

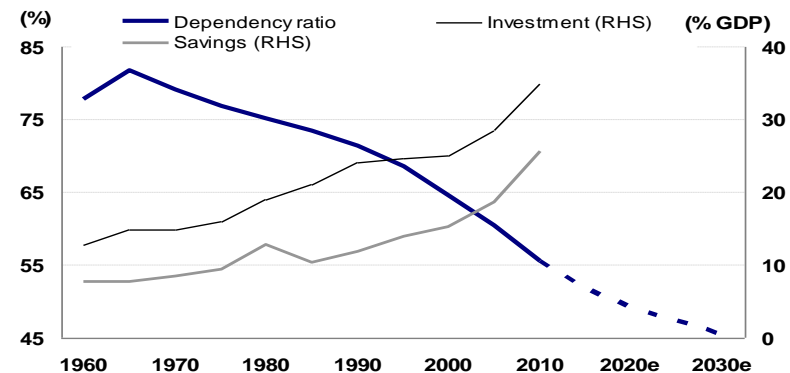
- Young Country - 50% of the population is below the age of 24 years
- Middle class is ballooning with rising consumption power
 - Rising per capita income – US\$195 in 1980 to US\$1,580 in 2014
 - Rising literacy rate – 43% in 1980 to 74% in 2010
 - Declining poverty – 46% in 1980 to 16% in 2010
- India has the potential to become a market for global companies
- A manufacturing hub for automobiles, pharmaceuticals and IT
- Declining dependency ratio should result in higher saving rate (currently 29.3%) and higher investment
- India will add 200mn people to the global workforce over the next 2 decades while China, Europe and Japan will see a decline

India – Favourable Demographics



Source: Euromonitor, CLSA

India – Dependency Ratio



Source: UN, CEIC

Reforms: Structural Changes

- The government announced several structural reforms, the benefits to accrue over a period of time
 - Power sector – UDAY Scheme to tackle debt problem of discoms
 - Coal sector – transparent allocation; domestic production to move up
 - Infrastructure – improvement in road & rail construction
 - Smart cities, housing for all, port development projects etc.
 - Increase in FDI limits in various sectors
- Strong FDI inflow; one of the highest among all countries reflects momentum in investment
- Direct Benefit Transfer (DBT) – subsidy to go down; benefits to poor
- Two major structural changes recently
 - **Demonetization**
 - **Goods and Service Tax (GST)**

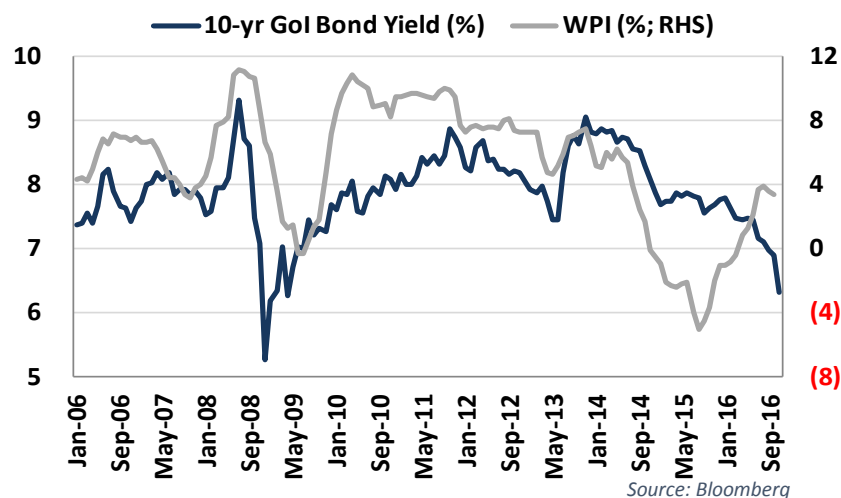
Demonetization

- Demonetization
 - On Nov. 8 government rendered INR 500 & INR 1000 denominations as non-legal tender w.e.f. December 30, 2016
 - INR 500 & INR 1000 form ~86% of currency in circulation (value ~\$ 209 bn)
 - New notes of denomination of INR 2000 & INR 500 introduced to exchange with old one
 - Old notes to be deposited into banking system and new notes to be issued with daily & weekly caps per person initially; old notes to be accepted at select outlets till notified date
- Near-term impact
 - Consumption halt for a few days and slowly started moving up
 - Severe drop in trade across the board
 - 'Wait & watch' mood prevailing across businesses & normalcy to return in about 2-3 months
 - GDP to take hit in H2 FY2017 due to low trade activity and slow down in consumption
 - Sharp hit on counterfeit currency
 - No visibility on earnings growth for corporate for at least next two quarters
 - Banks flush with money; announced lending & deposit rate cuts while government bond yield too has corrected sharply
- Medium & Long term impact
 - Lower inflation & significant improvement in gross fiscal deficit
 - Possibility for higher proportion of GDP coming into accounted / banked channel; consequently taxation reforms can be undertaken; higher and widen tax collection
 - Cut-down on unaccounted money in cash form; move towards lower cash usage
 - Smoother transition for Goods & Service Tax, which will convert India to a single market

Impact of Demonetization & GST

- Government stands to gain a windfall in form on undeclared currency & higher tax revenues from previously undeclared wealth
- Gross fiscal deficit has room to correct more than expectation
- Government bond yields already have shown sharp correction – official rate cut on card
- With an expanded tax base - room for government lower tax rates & improve subdued consumption demand
- Infrastructure allocation and government capex will be boosted
- Thereby paving way for private capex to revive later

Interest Rate & Inflation



Higher Budgetary Allocation

| INR Crs | FY2015 | FY2017e | CAGR |
|-------------------|--------|---------|------|
| Roads | 25,110 | 44,000 | 32% |
| Shipping | 450 | 1,000 | 49% |
| Urban development | 7,720 | 14,000 | 35% |
| Railways | 30,100 | 45,000 | 22% |
| Power | 5,700 | 12,200 | 46% |
| Rural development | 61,800 | 78,300 | 13% |

Source: Union Budget 2016

India sectoral impact and outlook

| Sector | Impact | Outlook |
|----------------------|---|--|
| Banks & financials | High liquidity; lower credit growth; treasury gains | In long term low inflation should be positive for banking, financial services and insurance; with more financial inclusion target market for lenders increases |
| Autos | Significant impact on demand in near-term | The expectation of consumption led growth after few quarters, auto sector is expected to benefit in medium to long term |
| Consumer | Demand impact in near term more for discretionary items | Consumer sector stands to benefit in terms of better logistics planning; uniform taxation & higher purchasing power to customer |
| Real estate & allied | Significant hit in demand in the near term | Real estate demand would depend on pricing decision by developers |
| Telecom | Increased data & voice usage initially | Telecos should not be directly impacted; however there may be some impact on pre-paid recharges of low ticket size |

India sectoral impact and outlook

| Sector | Impact | Outlook |
|------------------------|--|---|
| Cement | Due to linkage with construction sector, cement should see demand hit in near term | Slightly tepid outlook on the construction segment; however, pickup in infra capex by government can be positive for cement |
| Pharma | No direct impact as it's a necessity & significant export revenues | For pharma companies, US FDA actions and Trump administration's policies will have a higher bearing |
| Information Technology | No direct impact as it is largely export driven | Trump administration's view & actions will hold key |
| Retail | Direct impact due to consumer holding back spending | Higher share of digital & plastic mode of payment and improved purchasing power bode well in longer term |