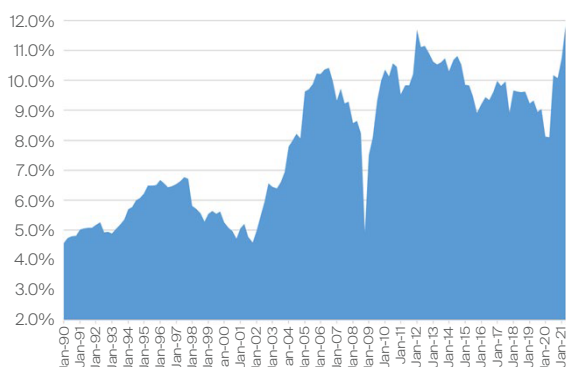


Monthly Manager Views

# FSSA Regional India Strategy

Land, Labour, Capital and Entrepreneurship. These are the well-known “Factors of Production” as defined by classical economists. The Entrepreneur (or Company) is the one that combines these factors to earn a profit. However, in our view, each of these factors has been overly exploited over the past 20-30 years and everything has become secondary to “profit” (to be used interchangeably with “market capitalisation”, albeit the link between the two has grown tenuous in recent years). The chart below, which shows how corporate profits have grown in relation to GDP in the US, captures the trend well – the ratio has more than doubled over 30 years. In other words, the pendulum has perhaps swung too far in favour of capital market participants.

**Corporate Profit/GDP - USA (1990-2021)**



Source: US Bureau of Economic Analysis

The true cost of natural resources is only now being assessed, as investors scrutinise aspects like carbon intensity, water use and greenhouse gas emissions, and insist on sustainable development. Interesting things are afoot with respect to labour as well. In the US, the median hourly wage adjusted for inflation has barely changed from 1979 to 2019, whereas the top 10% of earners witnessed a significant jump<sup>1</sup>. The recent trend of labour union drives and mass strikes, despite record low levels of

## RISK FACTORS

This is a financial promotion for The FSSA India Strategy. This information is for professional clients only in the EEA and elsewhere where lawful. Investing involves certain risks including:

- **The value of investments and any income from them may go down as well as up and are not guaranteed. Investors may get back significantly less than the original amount invested.**
- **Currency risk:** the Fund invests in assets which are denominated in other currencies; changes in exchange rates will affect the value of the Fund and could create losses. Currency control decisions made by governments could affect the value of the Fund's investments and could cause the Fund to defer or suspend redemptions of its shares.
- **Indian subcontinent risk:** although India has seen rapid economic and structural development, investing there may still involve increased risks of political and governmental intervention, potentially limitations on the allocation of the Fund's capital, and legal, regulatory, economic and other risks including greater liquidity risk, restrictions on investment or transfer of assets, failed/delayed settlement and difficulties valuing securities.
- **Single country / specific region risk:** investing in a single country or specific region may be riskier than investing in a number of different countries or regions. Investing in a larger number of countries or regions helps spread risk.
- **Smaller companies risk:** Investments in smaller companies may be riskier and more difficult to buy and sell than investments in larger companies.

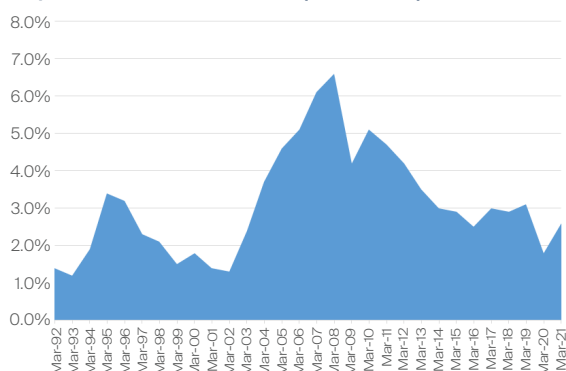
For a full description of the terms of investment and the risks please see the Prospectus and Key Investor Information Document for each Fund.

**If you are in any doubt as to the suitability of our funds for your investment needs, please seek investment advice.**

unemployment in the US, is symptomatic of this problem. And interest rates, as we know, have gone only one way for a very long time. This too, seems to be changing. Finally, tax, though not a factor of production, has also been coming down, with most large multinationals (MNCs) routing profits through tax havens. Again, there has been a backlash against such ‘tax avoidance’ practices. So, all the factors of production are starting to reverse trend, in a way, or at least in the US, the largest economy in the world.

However, the same Profit-to-GDP chart for India (below) looks like a mirror image of the one for the US, at least over the past decade.

**Corporate Profit/GDP - India (1992-2021)**



Source: Center For Monitoring Indian Economy (CMIE)

Why? The main reason could be a multitude of exogenous shocks to the economy, such as corporate scandals resulting in bureaucratic and credit freezes, demonetisation, the collapse of non-banking financial companies (NBFCs) and the transition to Goods and Service Tax (GST). However, even if we look at the factors of production, they are somewhat different. For one, India has traditionally been a capital-starved economy. Data from the International Monetary Fund (IMF) shows that real interest rates in India have averaged around 4.9% over the past decade, which is significantly above global averages (most developed markets have deeply negative real interest rates now). Not only are rates high,

availability of credit is relatively scarce given that a huge proportion of the economy still operates in the informal segment. Labour is also a complicated matter in India – whilst it is inarguably cheap, the laws are draconian, which ends up dis-incentivising Indian companies from making large employment commitments. Finally, the Indian government has only recently caught on to the thought that the country’s natural resources were not being valued properly – ergo a massive re-farming of licences for minerals like coal, iron ore and even telecom spectrum over the past decade. Even land has become hard to come by in India recently, with every industrialist we meet lamenting on how long (and how much) it takes to buy clean titles.

India is unique among large economies in the sense that it has yet to see the formalised economy (corporates and capital market participants) benefit in quite the same way as in some others. Our view is that as a result of policy measures taken in the last few years, cyclical factors and global geopolitical constraints, corporate profits in India will be a larger part of the economy in the next decade. That said, we are mindful of the pitfalls that await those companies that exploit some or all factors of production. For one, we try to stay far away from companies that seek to benefit by incurring a massive cost to the environment – polluting industries and mining companies, for example. Similarly, companies that do not value workers and their safety are another no-no (we tend to look at the percentage of contracted staff, injury and fatality track records, etc.). We also believe that companies must earn their social licence to operate, and paying taxes is a big part of that. We take a negative view of companies that design their business model around tax arbitrages or try their best to short-change the exchequer. And finally, we tend to pass on companies that have a poor attitude to debt (those that tend to bet the farm at the top of cycles, don’t recognise duration mismatches, or punt in foreign unhedged debt, for example). We greatly value management teams that recognise the long-term risks involved in all these matters and are willing to learn and even incur short-term costs to make their businesses more sustainable.

<sup>1</sup> Economic Policy Institute: State of Working America Wages 2019 by Elise Gould; published February 20, 2020

\*Company data retrieved from company annual reports or other such investor reports. Financial metrics and valuations are from FactSet and Bloomberg. As at 31 January 2022 or otherwise noted.

### Important Information

This material is for general information purposes only. It does not constitute investment or financial advice and does not take into account any specific investment objectives, financial situation or needs. This is not an offer to provide asset management services, is not a recommendation or an offer or solicitation to buy, hold or sell any security or to execute any agreement for portfolio management or investment advisory services and this material has not been prepared in connection with any such offer. Before making any investment decision you should conduct your own due diligence and consider your individual investment needs, objectives and financial situation and read the relevant offering documents for details including the risk factors disclosure. Any person who acts upon, or changes their investment position in reliance on, the information contained in these materials does so entirely at their own risk.

We have taken reasonable care to ensure that this material is accurate, current, and complete and fit for its intended purpose and audience as at the date of publication but the information contained in the material may be subject to change thereafter without notice. No assurance is given or liability accepted regarding the accuracy, validity or completeness of this material.

To the extent this material contains any expression of opinion or forward-looking statements, such opinions and statements are based on assumptions, matters and sources believed to be true and reliable at the time of publication only. This material reflects the views of the individual writers only. Those views may change, may not prove to be valid and may not reflect the views of everyone at First Sentier Investors.

Past performance is not indicative of future performance. All investment involves risks and the value of investments and the income from them may go down as well as up and you may not get back your original investment. Actual outcomes or results may differ materially from those discussed. Readers must not place undue reliance on forward-looking statements as there is no certainty that conditions current at the time of publication will continue.

References to specific securities (if any) are included for the purpose of illustration only and should not be construed as a recommendation to buy or sell the same. Any securities referenced may or may not form part of the holdings of First Sentier Investors' portfolios at a certain point in time, and the holdings may change over time.

References to comparative benchmarks or indices (if any) are for illustrative and comparison purposes only, may not be available for direct investment, are unmanaged, assume reinvestment of income, and have limitations when used for comparison or other purposes because they may have volatility, credit, or other material characteristics (such as number and types of securities) that are different from the funds managed by First Sentier Investors.

### Selling restrictions

Not all First Sentier Investors products are available in all jurisdictions.

This material is neither directed at nor intended to be accessed by persons resident in, or citizens of any country, or types or categories of individual where to allow such access would be unlawful or where it would require any registration, filing, application for any licence or approval or other steps to be taken by First Sentier Investors in order to comply with local laws or regulatory requirements in such country.

This material is intended for 'professional clients' (as defined by the UK Financial Conduct Authority, or under MiFID II), 'wholesale clients' (as defined under the Corporations Act 2001 (Cth) or Financial Markets Conduct Act 2013 (New Zealand) and 'institutional' investors as may be defined in the jurisdiction in which the material is received, including Hong Kong, Singapore and the United States, and should not be relied upon by or be passed to other persons.

The First Sentier Investors funds referenced in these materials are not registered for sale in the United States and this document is not an offer for sale of funds to US persons (as such term is used in Regulation S promulgated under the 1933 Act). Fund-specific information has been provided to illustrate First Sentier Investors' expertise in the strategy. Differences between fund-specific constraints or fees and those of a similarly managed mandate would affect performance results.

### About First Sentier Investors

References to 'we', 'us' or 'our' are references to First Sentier Investors, a global asset management business which is ultimately owned by Mitsubishi UFJ Financial Group (MUFG). Certain of our investment teams operate under the trading names FSSA Investment Managers, Stewart Investors and Realindex Investments, all of which are part of the First Sentier Investors group.

This material may not be copied or reproduced in whole or in part, and in any form or by any means circulated without the prior written consent of First Sentier Investors.

We communicate and conduct business through different legal entities in different locations. This material is communicated in:<sup>[1]</sup>

- **Australia and New Zealand** by First Sentier Investors (Australia) IM Limited, authorised and regulated in Australia by the Australian Securities and Investments Commission (AFSL 289017; ABN 89 114 194311)
- **European Economic Area** by First Sentier Investors (Ireland) Limited, authorised and regulated in Ireland by the Central Bank of Ireland (CBI reg no. C182306; reg office 70 Sir John Rogerson's Quay, Dublin 2, Ireland; reg company no. 629188)
- **Hong Kong** by First Sentier Investors (Hong Kong) Limited and has not been reviewed by the Securities & Futures Commission in Hong Kong
- **Singapore** by First Sentier Investors (Singapore) (reg company no. 196900420D) and has not been reviewed by the Monetary Authority of Singapore. First Sentier Investors (registration number 53236800B) is a business division of First Sentier Investors (Singapore).
- **Japan** by First Sentier Investors (Japan) Limited, authorised and regulated by the Financial Service Agency (Director of Kanto Local Finance Bureau (Registered Financial Institutions) No.261)
- **United Kingdom** by First Sentier Investors (UK) Funds Limited, authorised and regulated by the Financial Conduct Authority (reg. no. 2294743; reg office Finsbury Circus House, 15 Finsbury Circus, London EC2M 7EB)
- **United States** by First Sentier Investors (US) LLC, authorised and regulated by the Securities Exchange Commission (RIA 801-93167).
- **Other jurisdictions**, where this document may lawfully be issued, by First Sentier Investors International IM Limited, authorised and regulated in the UK by the Financial Conduct Authority (registration number 122512; registered office 23 St. Andrew Square, Edinburgh, EH2 1BB number SC079063).

To the extent permitted by law, MUFG and its subsidiaries are not liable for any loss or damage as a result of reliance on any statement or information contained in this document. Neither MUFG nor any of its subsidiaries guarantee the performance of any investment products referred to in this document or the repayment of capital. Any investments referred to are not deposits or other liabilities of MUFG or its subsidiaries, and are subject to investment risk, including loss of income and capital invested.

© First Sentier Investors Group

<sup>[1]</sup> If the materials will be made available in other locations, seek advice from Regulatory Compliance.