

February 2010

Performance

The Asia Fund rose 4.2% in February and is now up 0.5% year to date. It is up 38.3% over the nine months since 1st June 2009 versus only 18.3% for the FTSE Asia Large Cap Index. Of course, one swallow does not make a summer, as the saying goes, but it is encouraging to note that our new approach seems to be working.

In truth, consumer sector out-performance is the pattern of the past. The MSCI Asia Consumer Staples Index (FTSE don't offer sector breakdowns) has returned 8.4% per annum since 1st January 1997 (which is when we launched our Fund) versus 4.2% per annum for the MSCI Asia Index over that period.

The poor return of the overall market is a salutary wake-up call to all those who think that high GDP growth translates into strong stock market returns. Much of the growth in emerging markets is driven by low value added, highly cyclical activities, such as manufacturing, construction and commodities. Furthermore, due to a weak regulatory backdrop, what wealth that is created ends up in the pockets of a small number of tycoons.

As consumer businesses are generally low in capital intensity they tend to generate higher returns. And, because reputation affects brand integrity, they tend to adopt better corporate governance and financial controls. This is the winning combination that Warren Buffett spotted some time ago. Obsession with short term tracking errors, Sharpe Ratios and index relative returns means that this simple point is lost on most "factory fund" managers.

Add in emerging market consumer tail winds and we think we are onto a winner. Indeed, Nestle India and Vinamilk, Vietnam's dominant beverage business, have just reported 23% and 75% net profit growth for FY09 respectively, while Chinese confectionery company Hsu Fu Chi announced 30% profit growth for its latest quarter. Recession...er, what recession?

Some might say: "well, we endorse your strategy; but why should we pay your (albeit, reduced) fees when we can access these stocks through an ETF?" Aside from not being able to talk to an ETF (a relief, arguably), the simple truth is that our portfolio is impossible to replicate. Several of our holdings still only trade by appointment - partly because we have locked up the free floats.

Indeed, of the 42 stocks that make up the MSCI Asia Consumer Staples Index, only 19 qualify for our own Arisaig Asia Dominant Consumer Companies Index (54 names) as true consumer businesses. About 20% of the MSCI Index is accounted for by plantation companies and MSCI's free float and market cap limits rule out a number of the best businesses.

FUND DETAILS:	as at 28 February 2010				
	AAF*	ASEAN	AIF	AGCF	AKF
NAV (US\$):	26.68	32.59	43.24	35.61	54.28
SIZE (US\$M):	1,328.7	183.5	502.9	558.9	90.5
UNITS ISSUED (M):	49.8	5.6	11.6	15.7	1.7
LAUNCHED:	31.12.96	1.4.98	11.6.99	1.6.00	6.10.00
AAF% HOLDING:		13.7	37.8	42.1	6.8

* AAF is a holding fund investing in our specialist sub-regional funds.

Pizza Delivery

What's more, an important part of our job is to identify emerging dominant consumer businesses. We were able in February to add to the portfolio one such example, Jubilant Foodworks, which runs India's largest fast food chain under the Domino's Pizza brand. The company listed in Mumbai a few weeks ago with a market cap of only USD200 million.

This is a business we have followed for many years as it is owned by the Bhartia family who also run a specialty chemicals firm that we used to own. We first started talking to them about fast food when they had only thirty outlets. Now they have 300 with 70 new ones planned per annum for the next five years.

Management reckon that the market could easily cope with 2,000 stores. Its main competitor Yum!, despite its huge success in China through KFC (about which we wrote a 100 page report), has still to get the formula right for India. For now, Jubilant's business model is still delivery based and therefore capex per store is undemanding. Working capital is tightly managed, and internal cash flow generation should be sufficient to fund the company's ambitious growth plans.

Meanwhile, consumption of pizza in India is just USD20 cents per capita per annum; negligible when compared to USD15 in Singapore or USD69 in the USA. As incomes rise so do people's aspirations. Indeed, KFC's success in China came only once it started charging premium prices for the experience of "western dining". The sector in India has grown at almost 25% per annum for the past decade. Our Arisaig Crystal Ball "S" curve analysis suggests that it could be 5x its current size in ten years' time.

Indian retail

This is another emerging consumer sector that we have been staring at for quite a while. Indeed, we first met the pioneering Mr. Biyani of Pantaloon by chance on a plane eight years ago, when he insisted, upon touch-down, on taking us to see his outlet in Bangalore. Since then we have remained firm friends.

PERFORMANCE TO 28 February 2010 (%)										
Performance	10 year	5 year	3 year	2 year	1 year	6 months	1 month	YTD	Since Launch	Annualised Return
Arisaig Asia Fund (%) *	+157.8	+52.8	+3.1	-14.7	+85.7	+21.1	+4.2	+0.5	+297.8	+11.1
Arisaig ASEAN Fund (%)	+122.2	+21.2	-25.8	-28.9	+54.3	+9.3	+1.7	+4.0	+225.9	+10.4
Arisaig India Fund (%)	+59.9	+53.4	-7.8	-32.6	+87.3	+22.5	+2.8	+3.2	+332.4	+14.6
Arisaig Greater China Fund (%)	N/A	+76.7	+35.7	+7.6	+107.9	+26.3	+7.6	-1.1	+256.1	+13.9
Arisaig Korea Fund (%)	N/A	+60.7	+8.4	-4.3	+84.5	+20.6	-2.3	-9.0	+442.8	+19.7

* Reflects the performance of the Arisaig Asian Small Companies Fund from 31.12.96 to 21.1.00 and thereafter the performance of AAF.

This is not to say that we think his formula (throwing the kitchen sink at all sectors from supermarkets to bookstores) will end up a winner. Indeed, limited city-centre space, poor roads to out-of-town locations, inadequate car parking, high rents in India's malls (of which there are still only about 170) make this a very tough backdrop for high volume, low margin models.

What's more, the so called "disorganised sector", the hole-in-the-wall stores known locally as "Kirana", which accept razor thin margins, offer credit and even do home deliveries, are a tough act to take on. We did a trip last month to meet the Tata, Pantaloon, Bhartia, Birla and Shopper Stop groups who are jockeying for position and concluded that is too early to pick a winner. We will devote the next several months to producing an in-depth research report before deciding which way, if any, to leap.

Asian Breweries

Meanwhile, our report on the Asian Brewery Sector is now complete, copies of which should be reaching our investors' desks shortly, along with our end February Holdings Booklet and Henry Root letters (not, incidentally, an ETF offered feature).

In contrast to our Africa Fund, the Asia Fund has historically been "beer lite". Unlike their African peers, Asian breweries have been dogged by poor capital return metrics and low margins. Having looked at the industry in some depth, we believe that this simply reflects market evolution, and that the dynamics of the sector in Asia are set to change radically.

In China, for example, due to a history of non-profit minded provincial state involvement, the industry has been highly fragmented and therefore excessively competitive, resulting in very low prices. A 650 ml bottle of lager, the tippie of choice, costs only USD70 cents in China compared to USD2.60 in, say, Korea or Taiwan. This results in low teen EBITDA margins versus the 30% plus numbers generated by several of our African holdings, invariably cozy duopolies or monopolies, such as the Diageo controlled East African Breweries or Guinness Nigeria.

The history of all major beer markets, bar few, tells the same story. Due to its relatively high capital intensity this is an industry which tends to self-consolidate, invariably resulting in a few large oligopolistic players dominating national markets. This process is already well underway in China. Indeed, 2009 probably represented the inflection point with the dominant players now starting to leverage their scale and increase their prices.

The story in India is unusually different. The sector here is already dominated by only two players - SABMiller and our old friend United Breweries (the latter enjoying over a 50% share). The difficulty in India is that, due to a harsh regulatory environment (high excise duties, intra-state barriers, state controlled distribution, advertising bans, etc), the sector is still very small. Per capita consumption in India is only 1.3 litres per person per annum versus 32.3 in China and 59.5 in Mexico.

Nevertheless, coming off such a low base, India is one of the fastest growing markets in the world, with sales having compounded at 18% per annum over the past five years. There is still massive potential for future growth, fuelled by pent-up demand and rising disposable incomes. Profitability, still very low, should improve on the back of economies of scale and product mix enhancement. The icing on the cake would be favourable regulatory reform (we won't hold our breath).

Chinese steroids

Unsurprisingly China reported yet another year of 8% plus GDP growth (the only real surprise being that the announcement came after the year end, unlike in previous years). The country's stimulus package, in total about USD600 billion or 14% of GDP, larger than any other, could only have led to this outcome.

The Communist Party has easy access to the accelerator pedal controlling, as it does, most of the banking sector and, in the form of state-owned enterprises, one third of possible borrowers. Given that exports were down 25% in 2009, and both electricity demand and rail road usage were negative year-on-year, it is clear that the stimulus has been directed at fixed asset accumulation.

With excess cement capacity equivalent to the total capacity of USA and Japan; idle steel plants with the combined capacity of Japan and Korea's; and 30 billion square foot of real estate under construction (that's five square foot per person), the hangover looks like being monumental.

Should the global recovery falter, that USD2.3 trillion of foreign exchange reserves will come in handy. Not that any of this troubles us unduly. Our stocks may be de-rated, but they won't be de-railed. As the evidence of our back testing shows, our men tend to stand tall in the heat of battle.

ARISAIG PARTNERS, 7A Lorong Telok Singapore 049019
Tel (65) 6532 3378 / Fax (65) 6532 6618 28 February 2010
Website: www.arisaig-partners.com

	ASSET ALLOCATION (%)						SECTOR ALLOCATION (%)				
	AAF	ASEAN	AIF	AGCF	AKF		AAF	ASEAN	AIF	AGCF	AKF
Hong Kong	4.8			11.4		Food & Beverage	47.3	39.5	47.5	53.8	19.9
China	37.2			88.5		Consumer Products	26.2	35.6	42.8		75.6
Korea	6.5				95.5	Retail	4.4	19.3		4.1	
India	32.4		85.9			Services	3.7		9.9		
Sri Lanka	4.0		10.6			Supermarkets	17.6			42.0	
Pakistan	1.4		3.7			Other	0.6	4.2			
Singapore	1.6	11.6				No. of Core Holdings	26	5	10	8	3
Malaysia	2.0	15.1				Top Ten Holdings (%)	61.9	98.6	97.7	99.9	95.5
Thailand	0.6	4.2				Top Twenty Holdings(%)	87.7	98.6	100.2	99.9	95.5
Philippines	2.2	16.0				Ave Mkt Cap (US \$m)	2762	3065	2009	3291	3036
Indonesia	4.9	35.6				VALUATION (Dec'10/Mar'11)					
Vietnam	2.2	16.1				PER Weighted (x)	21.3	16.8	22.5	22.3	16.0
Cash	0.2	1.4	-0.2	0.1	4.5	PER Harmonic (x)	19.1	15.0	21.3	20.1	13.4
Total	100.0	100.0	100.0	100.0	100.0	Yield (%)	2.3	2.6	2.1	2.6	1.4
						P/BV (x)	7.5	7.5	12.0	4.2	3.9
						ROCE (%)	46.9	50.7	73.5	26.4	24.1
						EPS Growth (%)	18.0	18.3	16.4	19.0	20.8

The Arisaig family of Funds are daily valued, open-ended, BVI or Mauritius domiciled, Investment Companies, and, with the exception of the Korea fund, are listed on the Irish Stock Exchange. The Funds' NAVs are shown in the Financial Times and on Bloomberg. This Diary is intended to be for the information of holders of one or more of Arisaig's Funds. It is not intended to constitute investment advice and should not be relied upon as such. Investors should be aware that, as the Funds are invested in the securities of smaller companies, share prices can be more volatile and trading liquidity much lower than those of larger companies.