



Health Care's Rich, Diverse Landscape

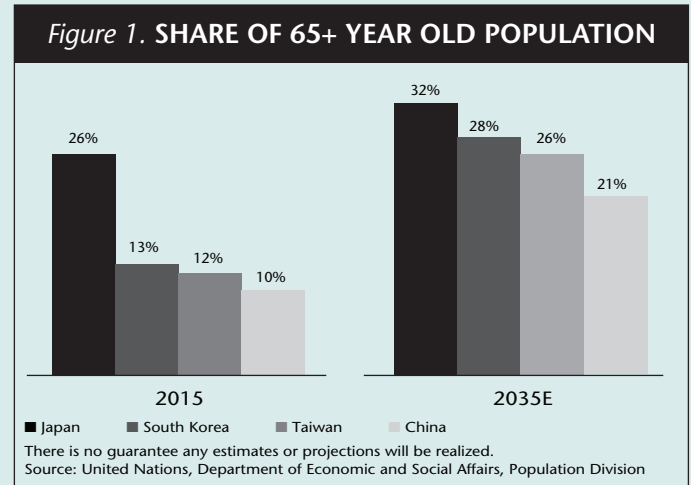
Asia boasts a large and heterogeneous health care sector, reflecting the diversity of the region itself. Demographics, rising income and innovation each contribute to the sector's growth, creating compelling long-term investment opportunities. As bottom-up investors, we believe stock selection is key, as the success of individual companies can have a number of complex drivers, from regulatory frameworks, to pricing power and competitive moats. Within this dynamic sector, competition can be fierce, particularly among companies that provide lower value products and services. Investing with a long-term view, we find individual companies most interesting when viewed through the lens of innovation. We define innovative companies as those competing on intellectual property, quality and service. Many innovative health care companies are thriving and making new investments in research and development. As in the past, Asia's consumers will continue to play an important role in the growth of health care-related industries, with patients seeking better quality care and services as incomes rise. Here is a high-level look at some of the themes our investment team is following across the region.

Spotlight: Japan

Fast-tracking regenerative therapies and neurological research

More than a quarter of Japan's population is age 65 or older (see Figure 1), making age-related health care research a national priority. To accelerate investments and innovation, Japanese regulators allow treatments for some age-related conditions to come to market very quickly when they show early promise in small-scale trials. As a result, companies can begin to earn money from treatments, even as treatments are still being tested on a larger scale. This regulatory framework is spurring investments in regenerative therapies for conditions such as macular degeneration, as well as launching a race to treat neurological conditions that currently have limited and often unsatisfactory treatment options, including Alzheimer's and Parkinson's diseases.

While Japan's demographics are particularly challenging, they are by no means unique. Many other North Asian countries



face a similar future. South Korea, Taiwan and China will each have roughly a quarter of their populations over the age of 65 in the next 20 years. At present, Japan has gained a significant head start on tackling research into age-related conditions by allowing companies to go to market concurrently while conducting clinical trials. Japan's leadership role has global implications. If a company in Japan can engineer a major breakthrough in treatments for Alzheimer's or Parkinson's diseases, for example, we believe there will be a huge market for such treatments worldwide.

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Spotlight: China

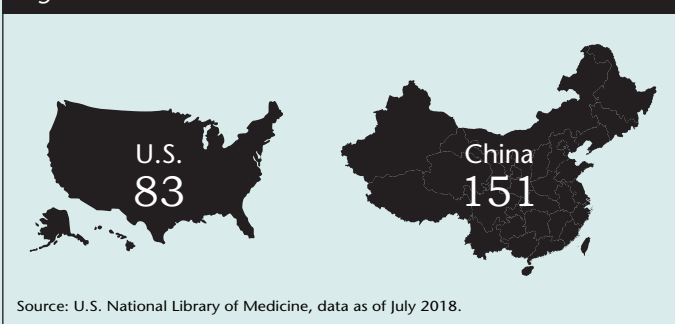
China's oncology research ecosystem flourishes, enjoying an influx of talent and capital

Over 3.8 million new cases of cancer were diagnosed in China in 2016, according to the China National Cancer Center. Cancer remains a leading cause of death in China, where four people die of cancer every minute. While Western populations tend to have higher incidents of breast and prostate cancers, Chinese patients experience higher rates of stomach and liver cancers. As government health care systems grapple with a high volume of new cancer cases, drug manufacturers in China are conducting clinical trials to test the effectiveness of these new treatments. At present, the number of clinical trials for CAR-T treatments conducted in China—which help patient's T cells attack cancer cells—is nearly double that of the U.S. (see Figure 2).



“Many doctors and researchers who return to China seek the influence and prestige of running their own labs and having more agency within a highly dynamic region and sector.”

Figure 2. CLINICAL TRIALS FOR CAR-T TREATMENTS



On the regulatory front, China has taken significant strides toward promoting innovation. China’s health care regulator, the National Medical Product Administration (NMPA), is becoming increasingly aligned to U.S. FDA standards. One step in this process was becoming a member of ICH, the International Council for Harmonisation of Technical Requirements for Pharmaceuticals for Human Use. This global organization helps members share data through more uniform data standards. Other reforms that China is implementing include efforts to expand the number of prescription drugs available through the government health care system while also lowering the price of generics.

Notably, China has a robust ecosystem that includes health care talent driving innovation in the sector, as well as venture capital funding the sector. Many scientists who trained and worked in the United States for decades are now returning to China as researchers and business entrepreneurs. The allure of working in China is not necessarily a desire to make more money. Rather, many doctors and researchers who return to China seek the influence and prestige of running their own labs and having more agency within a highly dynamic region and sector. They recognize that their most fulfilling and exciting work opportunities may be in China.

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Spotlight: India

Pivoting toward higher value products

India’s pharmaceutical manufacturing sector has traditionally been focused on producing generic drugs and simple oral solids that are easy to manufacture, such as aspirin. This history has earned India the nickname of the world’s drugstore (See Figure

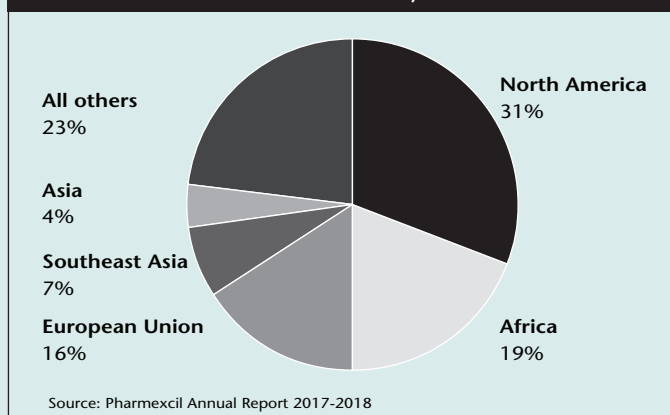
3). Following two decades of leadership in generics, however, many Indian pharmaceutical companies now seek to pivot toward higher value products. As generic drugs experience price deflation every year, companies in the industry will need to evolve in order to survive.

We see early signs of consolidation among pharmaceutical companies in India, a trend that we expect to continue. It won’t be an easy transition toward higher value products, but some of the better-managed Indian companies may have an advantage in that they currently have significant scale and manufacturing assets on the ground that could potentially be converted to new uses. Examples of more complex products include respiratory inhalers that deliver medicine from a mechanical device; injectables that deliver medicine through a single use syringe; and biologics, which represent more complex proteins that interact in the body in a more natural way.

While the move toward a more innovative health care sector in India is still in its early days, some companies are actively seeding more money into research and development efforts. More companies, both public and private, are researching new chemical entities, as well as new biologic entities. We also see the rise of outsourced clinical trials using contract research organizations (CROs), analogous to outsourcing IT services. Global companies find the economics of moving some of their medical research and development efforts offshore to India compelling. We expect that some of the more successful CROs may be able to grow rapidly in the coming years.

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Figure 3. GLOBAL DISTRIBUTION OF INDIA’S PHARMACEUTICAL EXPORTS, BY REGION



“In Asia, improvements in health care can have a large impact on communities, particularly around lower-cost solutions that make health care more accessible.”

Spotlight: Health care through an ESG lens

Improving quality of life

Health care is often a natural area of focus for environmental, social and governance (ESG) investment strategies, falling neatly into the category of promoting social good. In Asia, improvements in health care can have a large impact on communities, particularly around lower-cost solutions that make health care more accessible. At the same time, the health care sector is a prime example of how ESG themes are already part of many mainstream investment frameworks. Many equity growth strategies in Asia consider health care as part of the mix for purely financial reasons. From an ESG vantage point, we believe focusing on innovative health care companies that deliver world-class health care solutions at affordable prices while improving quality of life can help identify even more compelling long-term opportunities.

In Asia, we see examples of health care progress across the spectrum of income levels. Consider the example of Bangladesh, a low-income country with a young population and large workforce. A handful of companies in Bangladesh are already very successful at manufacturing generic drugs. Labor costs in Bangladesh are lower than in India, the current leader in generics, making Bangladesh an emerging hub for the next generation of generics manufacturers. These Bangladeshi companies serve their own large domestic market, while also exporting affordable generic drugs to many other low-income countries, improving quality of life for millions.

Turning to the wealthy island nation of Singapore, some Singaporean hospitals are expanding operations and facilities to China, meeting demand among middle-class Chinese consumers for improved and comparatively affordable local health care options. These hospitals use a multidisciplinary team of physicians to provide patients integrated, peer-reviewed and audited medical services, with an emphasis on superior health outcomes. Chinese medical patients who once flew to Singapore for care are now finding more options available in mainland China. China's local governments are encouraging partnerships with Asian regional hospital operators who can bring much-needed high-quality care and service models closer to home for their citizens.

Asian economies are developing health care models that suit the specific needs of their citizens and demographics. Just as many parts of Asia have been able to leapfrog the West in terms of mobile phone adoption and microfinance offerings, we expect to see opportunities for leapfrogging in the health care arena as well. In the context of a globally diversified portfolio, health care can play a meaningful role for investors seeking to tap the long-term growth potential of Asia.

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Risks and Opportunities of Investing in Asia's Health Care Sector

Risks

- ✿ Bringing new medical treatments to market can take years, and health care companies often face a longer time horizon for monetizing intellectual property
- ✿ The sector is highly governed by regulatory frameworks and changes in regulations can negatively impact companies
- ✿ As markets become more globalized, lower value health care products have less pricing power and face steeper competition
- ✿ Stock prices for companies not yet earning profits can be highly volatile
- ✿ It's important to invest with a long-term time horizon, typically five years or longer, as Asia equities can be volatile over the short term

Opportunities

- ✿ Demographics provide health care companies with attractive long-term growth potential
- ✿ Innovative medical treatments developed in Asia can be marketed worldwide
- ✿ Japan and China have regulatory frameworks that are encouraging high levels of investment and innovation
- ✿ Countries can learn best health care practices from neighbors, allowing for faster growth and development
- ✿ An active approach to security selection is essential to managing risks and adding the potential for alpha



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