FSSA Investment Managers

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Client Update

Beyond the AI rally

November 2025

Asian equities have staged a robust rally in 2025. Yet beneath the headline figure lies a narrow driver of performance. In the year to date, almost two-thirds of the total return of the MSCI AC Asia Pacific ex-Japan index has been driven by technology and AI-related companies.[1] Outside of these sectors, many high-quality businesses – particularly in Southeast Asia, India and China's traditional sectors – have not performed despite solid earnings growth, improving governance and attractive valuations.

This bifurcation reflects a broader global trend. In the US, the economy's resilience has been attributed to a "very significant AI-related, tech-related investment surge."[2] Companies like Nvidia, Broadcom and OpenAI have led the charge with circular deals and strategic alliances that have sent company valuations soaring.

In Asia too, Korean and Taiwanese chipmakers and Chinese technology platforms have seen valuations expand rapidly on the future promise of AI. Taiwan Semiconductor Manufacturing (TSMC), Tencent, Alibaba and Samsung Electronics – all related to the AI theme – are the top four companies in the MSCI AC Asia Pacific ex-Japan index. They now comprise almost a quarter of the index's weight. On a country level, TSMC commands a staggering 56% of MSCI Taiwan, up from 24% in 2015. Samsung Electronics and SK Hynix together represent almost 40% of MSCI Korea, compared to just 23% a decade ago.[3] This underscores the outsized role of a handful of firms in shaping regional returns.

With everything seemingly about AI, we believe it is critical to remain disciplined in our investment approach and focused on quality. Looking back through history, we have been here before – including the dot-com bubble, the global financial crisis (GFC), the China equity market exuberance of 2015 and the rise (and subsequent fall) of the profitless growth companies in 2020. As the saying goes: history doesn't repeat, but it often rhymes. Excess will eventually give way to the reality of earnings and cash flows, and when the tide turns, we believe high-quality businesses will preserve capital best.

Performance review

As benchmark-agnostic investors, we pay little attention to index compositions or returns. We focus instead on generating absolute returns for our clients in the long run. Since inception, the FSSA Asia equity strategy has generated positive returns over all 3-year, 5-year and 10-year rolling periods.[4] Our track record, when viewed through the lens of the market environment, shows that our portfolios tend to perform better in "normal" markets (-15% to +15% 1-year rolling returns) and bear markets (more than 15% decline), than in steeply rising markets (defined as over 15% 1-year rolling returns).

Through our bottom-up research, we own dominant industry leaders that have exposure to AI like TSMC and Tencent, but we remain sceptical about the many unproven AI-related companies in Asia. Last year we added considerably to our position in Tencent, and TSMC remains a core position across the team's portfolios.

TSMC has continued to perform strongly, being the key supplier of advanced semiconductor chips used in the AI capex boom. Revenue and profit compounded at 21% and

[1] FSSA Investment Managers, FactSet, MSCI, as at 30 September 2025.
[2] https://www.ft.com/content/74224d84-8a7a-4d0d-a30d-1716e2d43b7a
[3] FactSet, MSCI, as at 30 September 2025.
[4] Based on FSSA Asia Equity Leaders composite performance vs. MSCI Asia Pacific ex Japan Index since inception from 31 January 2001 to 30 September 2025.

27% CAGR[5] respectively over the past five years. However, when one of the highest quality and largest companies in Asia delivers such strong operating performance (well matched by share price returns), we think it is natural to have some concerns about the current cycle.

On the other hand, Tencent is seeing improvements after a few difficult years navigating the regulatory environment and weak economy. A returning focus on evergreen games and the deployment of AI within its business has driven productivity gains and better advertising outcomes. In recent meetings with the management, we have been impressed by Tencent's AI strategy and its disciplined approach to technology investments.

Although Tencent was not the first mover in large language models (LLM), we believe its strong customer-centric mindset and versatile culture supports its right to win. Tencent's Yuanbao AI assistant, launched in May 2024, is already ranked top 3 in China (by daily active users), with search, translation, writing and summarising tools. It is integrated into the WeChat app, which already enjoys a formidable moat and network effects with over 1.3 billion monthly active users.

We believe Tencent should continue to be a key beneficiary of AI developments with its strong ecosystem and the ability to harness data across its network from its WeChat, Gaming and Payments businesses. We expect the ongoing roll-out of various user-friendly AI capabilities should further cement its usage while creating new avenues of growth.

Improving governance and unlocking shareholder value

Away from the exciting world of AI to the (perceived) dull world of conglomerates, Jardine Matheson, the Hong Kong-based group with roots stretching back to 1832, has been reinventing itself. It has taken some time to reap the rewards of its reforms, but the direction of travel looks positive. We remain significant and constructive shareholders of various Jardine group companies.

As one of the storied *hongs* of the British colonial era, the Jardine group of today has sprawling business interests ranging from real estate to supermarkets, hotels and automotives. Helmed by the Keswick family for more than five generations, the group's crossholdings, double discount on net asset values and overall complexity has long been a bone of contention for minority shareholders.

A holdover from the 1980s, Jardine Strategic (JS) held stakes in the group's underlying businesses, with Jardine Matheson (JM) owning 85% of JS, and JS in turn owning 60% of JM in a convoluted circular structure. Directors sat on the boards of multiple group companies with little care for the semblance of independence. This fortress arrangement meant that the family could maintain control and fend off hostile bids, despite holding just 17% of the stock.

The family had argued that the group structure fostered stability and business continuity – it enabled the management to put aside worries about loss of control, ignore short-term fluctuations in the share price and make longer-term strategic decisions without hindrance. To us, it was a remnant of the past, not fit for purpose and an excuse to hold on to subpar governance standards.

In 2021, with many of the group's businesses facing structural headwinds, executive chairman Ben Keswick finally took steps to privatise JS and cancel the shares, with the double discount consequently removed. While there were grumbles about "fair value", the result was enhanced corporate governance and transparency at the group level.

More governance reforms followed, including a refreshed board with independent directors like Stuart Gulliver (ex-HSBC), Keyu Jin (sits on the board of Richemont Group) and Janine Feng (managing director at Carlyle Group). The leadership of its subsidiaries has been professionalised too, with new external CEOs at DFI, Mandarin Oriental and Hongkong Land bringing external experience and a sharper operational focus. All three have begun to focus on the most attractive parts of their businesses, while exiting non-core ventures to improve returns on invested capital and return cash to shareholders where appropriate. Improving total shareholder return is the new mantra for the group.

These changes are redefining Jardine Matheson. "The era of talented amateurs (Jardine general managers who rotate across businesses and geographies) is over," according to finance director Graham Baker in a recent meeting, "Now is the era of professional management – specialists are needed."

More needs to be done to shift the group back towards a growth pathway, but we expect changes to accelerate in the coming years. Lincoln Pan recently joined as JM's CEO, taking over from John Witt who retired from the company. Pan joins from private equity group PAG and is the first external *taipan* at the group. This is significant and another indication of the changing culture at the group.

In the meantime, Astra International, Jardine's 50.1%-owned Indonesian subsidiary, is a key contributor to the group's earnings and cash flows. It is central to the group's future. Despite concerns over its exposure to coal mining services and automotive disruption, its diversified portfolio offers resilient cash flows and steady

[5] Compound annual growth rate. All company data herein retrieved from company annual reports or other such investor reports. Financial metrics and valuations are from FactSet and Bloomberg. As at 30 September 2025 or otherwise noted.

growth. A strategic review is underway, with expectations of portfolio rationalisation and a renewed focus on core businesses akin to what has happened at other Jardine group companies.

The valuations of both JM and Astra look attractive and we have added to both. The group has spent over US$7bn on buybacks and asset disposals, including the sale of prime Hong Kong office space and a reduction in property development exposure. JM trades at 10x 2025 earnings and 0.6x book value, with a 4% yield. Astra, meanwhile, trades at 7.6x forward earnings and 1x book, despite its strong fundamentals. Both companies are priced below long-term averages, suggesting upside potential as reforms take hold.

For long-term investors, JM and Astra offer broad exposure to Asia's growth story, backed by improving governance and attractive valuations. Reassuringly, JM is the family's main wealth generator, which ensures alignment, and the Keswick family have a good reputation for stewardship and a multi-generational track record of creating enduring value.

What hurt

Elsewhere in Indonesia, Bank Central Asia (BCA) detracted from performance as it reported weaker loan growth and a mild increase in credit costs. Despite its derating, BCA's underlying fundamentals remain strong. We continue to believe it to be a conservative, well-managed bank with structural advantages and a long runway for growth. It has a long history of operating in a challenging external environment, and we are confident backing the franchise and the people. We think it is reasonably valued for its high rates of compounding book value.

BCA has undergone positive transformations while maintaining its competitive edge in transactions, technology and culture. Over the past five years, the bank has doubled its customer base to over 33 million, expanded its digital footprint and maintained industry-leading profitability – all while adhering to a conservative lending philosophy that prioritises long-term franchise value over short-term growth.

With a CASA[6] ratio of nearly 80%, BCA's deposit cost stands at just 1.4%, compared to 3-5% for peers. This enables it to offer competitive loan rates while sustaining high net interest margins, low credit costs and attractive return on assets. Meanwhile, it has launched "Blu", a digital-only brand targeting younger customers, and it handles 30–40% of Indonesia's digital transactions. These efforts have helped the bank maintain or even improve its relevance in a rapidly evolving financial landscape.

Against the backdrop of Indonesia's macroeconomic challenges – including weak job creation and political uncertainty following the election of Prabowo Subianto as president – BCA continues to gain market share. Our recent meetings with the management were reassuring, and we believe its conservative stance should position it as a safe haven during periods of market stress.

In India, Tata Consultancy Services (TCS) declined on concerns about US immigration changes and weaker client demand/spend due to general macro uncertainty around AI and the ongoing tariff war. Despite being an industry leader, there is some scepticism around TCS, with concerns about the lack of growth in the international business and the disadvantage of being an incumbent during the significant technology shift of AI.

On the first point, TCS has been derated due to its abnormally weak revenue growth, but beyond the headline figure, its slower growth in international markets appears to be because of a few client-specific issues in the insurance and healthcare sectors. The company is clear that growth in developed markets should improve. We believe the recent weakness does not reflect a structural deterioration in its business model, as TCS continues to participate in, and win, many strategic digital transformation deals.

On the second point, the concerns are valid – the entire industry is facing disruption. AI will likely be deflationary in the near term, with 20-30% productivity gains being redeployed elsewhere. In the medium-to-long term, however, enterprises will need "help" in managing complex operating environments and making use of what AI has to offer. According to various industry reports, only 5% of companies appear to be achieving AI value at scale[7] – but at this stage, the end-state is ever-changing and uncertain.

All of this means that the long-term impact of AI on TCS's business (and IT services in general) is unclear. In the meantime, valuations are not cheap and there are other companies offering better risk-reward. We have kept a position but have trimmed in light of the uncertainty.

Techtronic Industries (TTI), the Hong Kong-listed manufacturer behind Milwaukee and Ryobi power tools, also detracted from performance. Despite operational success and consistent growth, its share price has been impacted by slowing consumer demand and scrutiny from short sellers over accounting practices (which the company strongly refuted). More recently it has been derated on concerns about Trump's tariff wars, though it has already evolved its operational footprint in response to the geopolitical tensions. China now accounts for just 30% of production, down from around 80% five years ago. Facilities in Vietnam, Mexico and the US have helped mitigate tariff exposure, while positioning TTI for growth in Europe and Asia.

[6] Current and savings accounts.
[7] MIT NANDA, July 2025: The GenAI Divide, State of AI in Business in 2025; and Boston Consulting Group, September 2025: The Widening AI Value Gap, Build for the Future 2025

We continue to think it is an attractive and well-managed franchise, which has been tested through cycles. After taking on too much debt in the GFC, we take comfort in its much stronger balance sheet, which puts it in a better position than peers and allows it to ride out – or even benefit from – a difficult external environment. We have taken the opportunity to add on weakness.

Adding to China's leading chain hotel brand

In China, after three years of weak performance, the market is showing signs of recovery. The rebound is from a low base, but we think it is encouraging. Industry consolidation is underway; regulators are adopting a more supportive stance; and domestic confidence in Chinese technology is rising. AI-related companies, semiconductors and technology hardware have been the main beneficiaries, but we are optimistic that performance will broaden out from here.

With Mr Market narrowly focused on all things AI, we have continued to build a position in H World (formerly Huazhu) at attractive valuations. The company has emerged as a dominant force in China's hotel industry – as the second largest hotel chain in China, it has developed a strong brand portfolio and deep operational expertise. H World is widely regarded as an industry innovator, with a strong focus on digital infrastructure and IT systems. These investments have helped it become a cost leader in the sector, while its membership programme has emerged as a key driver of organic traffic and customer retention.

After meeting with several company representatives, we met with founder and chairman Ji Qi in 2024. A serial entrepreneur with a background in technology, he remains central to the company's culture and strategy. Mr Ji built H World on a philosophy of continuous innovation and customer-centric design. He removed what he considered unnecessary features from his hotels – ballrooms, pools, large lobbies – in favour of what he believed guests valued: a good location, a clean and comfortable bed and quality services.

Having experienced many crises at previous start-ups, Mr Ji believes that success comes from being innovative and adapting to trends. He visits hotels and franchisees regularly to stay close to the market and gather feedback. Recognising that the competition has evolved from other hotel groups to Airbnb and aggregators like Booking.com, H World has focused on building a strong network of hotels and developing its membership programme as a more reliable source of traffic. It now has nearly 290 million members generating over 70% of bookings, with the majority coming through direct channels.

In 2024, adjusted EBITDA[8] reached US$935m, with margins supported by its fee-based revenue model – franchisees pay a fee to operate hotels under H World's brands, while the company appoints managers to ensure high service standards and operational consistency. Operating cash flow conversion remains strong, and capex has trended downwards as the company shifts further towards asset-light expansion. However, the share price has been volatile, reflecting investor concerns about declining RevPAR[9] in China in light of the weak macro backdrop.

But we believe a better metric to consider is RevPAR alpha – or the premium commanded by H World's hotels over others in similar locations. This pricing premium, combined with a lower reliance on online travel agencies and high operational efficiency, means H World franchisees can remain profitable in 2025 even as a large swathe of the hotel industry is loss-making. Meanwhile, the superior return profile enjoyed by H World hotels attracts new franchisees, as evidenced by the fact that 50% of 'new' hotels are existing hotel owners joining the H World network. This allows H World to maintain above-industry volume growth – independent of overall market conditions – and consistently gain market share as more independent hotels are converted.

We believe H World has a long runway of growth as it taps into China's rising domestic travel demand, urbanisation and upgraded consumer preferences. While short-term volatility may persist, we believe its long-term fundamentals remain intact. H World's significantly larger economies of scale should drive outsized profit in the long run as a hotel traffic aggregator.

Outlook

We are optimistic on the outlook for Asian equities. With a rising share of global GDP growth, Asia should continue to benefit from the shift towards higher value services-led growth, digital transformation and the ongoing financialisation across the region. Valuations also look attractive in comparison to developed markets like the US, while low ownership of Asian equities in global portfolios provides a good backdrop for absolute returns.

Across the FSSA Asian equity portfolios, our core holdings have continued to deliver good underlying business performance and shareholder returns. Current portfolio valuations remain attractive – as they have been over the last couple of years. Looking forward, we expect earnings to compound at low double-digit rates with circa 20% average returns on equity, while free cash flow yield is at a historic high and companies are returning more cash to shareholders.

[8] Earnings before interest, tax, depreciation and amortisation.
[9] Revenue per available room.

While we can't second guess when the AI theme might run its course, our holdings are characterised by strong competitive advantages, and they have historically managed to preserve margins and profitability through the cycles. We are confident that their strong fundamentals will translate into attractive shareholder returns in the long run, as the market broadens, over time, from its narrow focus on AI.

Source: All company data herein retrieved from company annual reports or other such investor reports. Financial metrics and valuations are from FactSet and Bloomberg. As at 30 September 2025 or otherwise noted.

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