MOI GLOBAL

Update on Our Holdings in Korea

This article has been excerpted from a letter by MOI Global instructors Chan Lee and Albert Yong, managing partners of Petra Capital Management, based in Seoul.

We increased our position in **Yuhan**, one of the largest pharmaceutical companies in Korea with a long history of operations, when the stock price plummeted during 2018. Yuhan sells a variety of subscription and over-the-counter drugs as well as active pharmaceutical ingredients (APIs). The company's main drugs include both licensed-in global blockbusters and in-house manufactured generics. Its API business has been growing steadily through its partnerships with global pharmaceutical companies such as Gilead Sciences. Lately, the company has been actively pursuing an "open innovation" strategy in its research and development of new original drugs. Despite the seemingly slow progress, the company has amassed outstanding research and development capability, and we think its pipeline of diverse drug candidates has potential in the global market. However, the stock was trading cheap for a long time because of the market's lack of understanding of such prospect.

The stock price finally rose during the third quarter when the company announced its first major license-out deal, a lung cancer drug candidate to Janssen Biotech for US$1.25 billion. This announcement was made public in early November while the broader Korean market was going through a rout. In addition, many investors do not seem to realize that the company is also a major manufacturer of home and personal care products through its joint venture with Kimberly- Clark (whose value is not fully reflected in the current stock price). Thus, we think the company is still substantially discounted with a high margin of safety.

We also increased our position in **CS Wind**, a leading wind tower manufacturer. The company manufactures wind towers in six different overseas production facilities and delivers them to global wind turbine manufacturers including Siemens, Vestas and GE Energy. As wind power technology continues to grow in scale and becomes increasingly cost competitive against fossil fuels, the wind power industry is likely to expand further even without governmental subsidies. The company has a proven track record of satisfying stringent quality requirements and technical specifications of global turbine makers. That is why the company continues to win orders from major upcoming wind farm projects. With a recent acquisition of a U.K. outfit, the company also made its foray into the offshore wind power market, which is expected to grow faster than the onshore wind power market. For this reason, we think the company is significantly undervalued given its favorable industry outlook and the competitive market position.

Despite the broader market decline last year, we had a few winners. In particular, the stock price of **SM Entertainment** [replay session], Korea's largest entertainment agency/music studio, rose substantially as the company generated strong cash flow from its diversified portfolio of K-pop artists. As Korean Wave (*Hallyu*) continues to gain popularity worldwide through new media platforms such as YouTube and other streaming services, the company's topline and profit are likely to grow even further. We like the fact that the company has a very well-structured in-house production system, which will allow it to keep churning out hit music along with new K-pop stars. Some of its K-pop artists are recruited from other countries such as China, Japan, Thailand and the U.S., which increases their international appeal. Even with the last year's price rise, we believe the stock has further room to ascend.

Nevertheless, the stock prices of most of our portfolio companies declined along with the general market in 2018. The stock price of **Com2uS** [replay session], a major developer and publisher of mobiles games, began to slide during the second half of last year because of uncertainties surrounding the delay in launching of the new *Skylanders* mobile game. However, we remain confident that, as one of the most competitive mobile game developers in the world, the company will continue to grow by providing updates and spinoffs of its flagship game, *Summoners War*, and successfully launching a number of new games. The company is also likely to improve its capital allocation by using its excess cash for buying back shares and acquiring other smaller game developers which will strengthen the company's game pipeline. That is why we think the stock has substantial upside potential.

The stock price of **Hankook Tire** [replay session] declined significantly last year because of the delay of its new production facility in the U.S. as well as the sluggish industry outlook. We believe that the current setback is rather temporary in nature. The company's new factory will eventually ramp up its production, allowing the company to gain its market share in the U.S. Based on our in-depth research, we continue to believe that Hankook Tire is still the most efficient tire manufacturer in the world, and it is likely that the company will recover its high profit margin in the near future. Given the competitiveness of its products and growth outlook, we think the current stock price is exceptionally cheap.

The stock price of **Jahwa Electronics**, a manufacturer of a key camera module component for smartphones, dropped substantially last year along with other smartphone manufacturers in Korea amid slower growth in smartphone sales. Also, the company's lower production yield in some parts caused weak earnings during last year. However, given the company's competitive edge in core technology, we believe that the company is likely to overcome the current setback and resume generating strong cash flow. Despite the recent slowdown, the stock is substantially undervalued at the current price.

By the end of 2018, we sold all of our positions in **Korea Re**, **Mando**, and **POSCO**. Although we believe that these companies are still somewhat undervalued, we exited the positions because we found more compelling value investing opportunities. With the sale proceeds, we initiated a few new small positions. We believe that these companies have resilient business models and competitive advantages in each of their respective fields. More importantly, these companies are significantly discounted compared to their intrinsic value. We will discuss the specifics later once we complete building meaningful positions.