

Korea: Ongoing Opportunities amid Global Recovery

Taewoo Kim, Portfolio Manager

Tae-woo Kim joined Fidelity as a portfolio manager in 2004. He started to manage FF – Korea Fund in October 2007. Prior to joining Fidelity, Taewoo worked as a fund manager at Mirae Asset Management and at Hana Bank. He holds a Bachelor of Business Administration from Yonsei University.

Redemption levels have been on the increase among Korean local retail investors, as the Korean stock market has recently started to lose its upward momentum. Tae-woo Kim, portfolio manager of FF Korea Fund, believes there are ongoing opportunities in the Korean market amid the current global recovery phase. In this Fund Perspective he explains why Korea is still an attractive investment destination for both domestic and foreign investors.

1. Korean retail investors have started to redeem their investments recently as the KOSPI showed some stunted growth. What is your view on the Korean stock market with respect to current flows?

The current redemption levels are due to psychological factors rather than about the Korean stock market dynamics itself.

The global economy and stock market have recovered consistently since early 2009. In particular, the emerging markets have made a strong recovery, with some of them approaching their previous highs seen in late 2007. The KOSPI also recovered to about 85% of its previous high witnessed in late December 2007, which increased the desire among Korean retail investors to take profit. Due to this healthy rebound in recent times investors have become increasingly sceptical about the possibility that the Korean stock market will further increase going forward.

On the other hand, the inflow of foreign investment into Korea increased solidly over the first quarter of 2010. Foreign investors have increased investments in emerging markets including Korea, on the back of climbing prices of raw materials such as crude oil. This trend is still visible now.

As broad economic conditions in the US continue to improve with the currently growing investment and production rates, we may be able to see positive changes on the employment side. This is likely to strengthen the confidence in a solid global economic recovery and improve investors' sentiment, given that the US represents 45% of the global market and accounts for 40% of the global consumption. Accordingly, Korean investors' confidence and interest in domestic stocks is likely to rise on the back of this.

2. If central governments introduce money tightening policies such as interest rate hikes, how will they affect the Korean stock market?

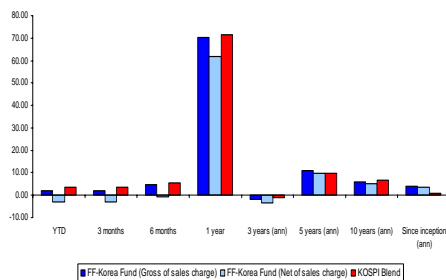
When the global economy showed signs of recovery early this year, it triggered concerns about the possibility that advanced markets such as the US and European nations would raise their interest rates, prompting questions on each country's exit strategies.

However, those concerns were reduced, as the Greek crisis broke out in 1Q10 and consumer prices began to stabilize to an extent. Nevertheless, if the current economic recovery continues for a while, discussions are likely to resume as to whether interest rates should be raised. At this stage, general interest rate hikes are likely to carry both positive and negative impacts. On the one hand, they would signal that the economy has overcome the financial crisis and the private sector is capable of making a recovery on its own. On the other hand, it could lead to a decreased level of liquidity in the market place going forward.

The stock market is not likely to experience a sudden shock because the possibility of policy rate hikes is factored into market expectations. The questions of the Korean economy's resilience to possible rate hikes and how significant these hikes will be are among the key concerns. However, if the Bank of Korea were to miss an opportunity to introduce an interest rate hike, this may lead to other complications going forward.

FUND RETURNS (%)

As at 31. 03. 2010



Source: Fidelity

Benchmark: KOSPI

Figures are in NAV-NAV, in USD terms with dividends reinvested. Past performance is not indicative of future performance. Since inception: 23.10.95.

The benchmark for performance until 31.05.00 was the Korea Stock Market (Price index). Thereafter is the Korea Stock Market Index(Gross)

3. How do you think the recent IPOs of large insurers such as Korea Life Insurance and Samsung Life Insurance will affect the stock market?

IPOs of healthy life insurance stocks will broaden the insurance sector and give investors a wider range of options compared to the non-life insurance stocks available. However, back in 1999 and 2002, we did observe that large-scale rights offerings of existing stocks and high-priced IPOs of new equities had a negative impact on the stock market. Nowadays, corporate analysis and monitoring standards of domestic and foreign investors have improved dramatically compared with the past, not to mention more transparency in corporate governance and accounting. Given this background, I believe that the aforementioned IPOs will be positive for the market.

4. The number of stocks held in your portfolio has declined recently from 50 to 37. What are the reasons behind this change, and how will it impact the volatility and risk profile of the Fund?

I held 52 stocks in the portfolio at the end of January, but have reduced this number to 37, as at the end of March. As a result, the tracking error and portfolio concentration have increased slightly. Most of those stocks that have been excluded from the portfolio were either listed in the KOSDAQ market or ones in which I had less conviction. In other words, I have sold those stocks that accounted for only a small portion of the portfolio or whose weights were much smaller relative to the benchmark index. By reducing the number of stocks held in the portfolio, I intend to better manage the risk of individual stocks and construct the portfolio with high-conviction stocks.

5. Could you give some examples of your high conviction names in the portfolio and their respective investment themes?

As at the end of March, LG Chemical and Kia Motors are two stocks whose weights are the highest relative to the benchmark index. After several years of a restructuring process, Kia Motors is fast establishing itself as a leading domestic and overseas automobile house through an effective positioning of its brand identity and releasing successful models. Its investments in production facilities and new car models since 2005 began to bear fruit in 2009, which have led to significant sales growth – a trend that is expected to continue for the time being. Its longer term challenges with debt are likely to be resolved gradually, considering the positive cash flows expected to continue in the future. This is likely to help decrease the carmaker's investment risks. Since 2H09, Kia Motors has released new car models continuously and has achieved significant sales growth in its major markets such as Korea, China, and the US. Kia Motors is predicted to post solid operating results in the coming seasons and I have extended my position in this company in accordance.

Additionally, LG Chemical is continuing to enjoy favorable market conditions thanks to the recovery of the global ethylene market, particularly in China. At the same time, its polarized film sales are increasing consistently thanks to the growth in LCD panel demand. LG Chemical is investing its stable earnings in new businesses such as rechargeable batteries and LCD glass substrates. This diversification effort is expected to have positive implications as the company already has LG Electronics and LG Display as its captive customers.

6. From a longer point of view, what are the reasons to invest in Korea?

Korea boasts many globally leading corporations in a wide spectrum of industries such as semiconductors, televisions, home appliances, automobiles, mobile phones, shipbuilding, steel, chemicals and the Internet. In addition, many of these companies have shown superior market liquidity and accessibility relative to regional peers. Korea's corporate earnings are predicted to increase over 35% year-on-year this year, but the stock market is trading at only about 10 times its corporate earnings forecast for 2010, which means that its valuations are still very attractive relative to other Asian countries or the global market.

TOP TEN HOLDINGS (%)

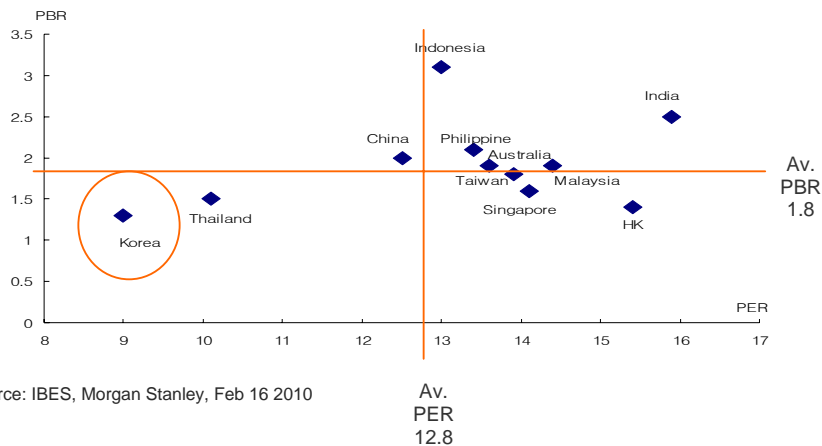
As at 31. 3. 2010	Fund	Benchmark
SAMSUNG ELECTRONICS	10.3	13.7
POSCO	6.1	5.2
HYNIX SEMICONDUCTOR	5.8	1.8
LG CHEMICAL	5.5	1.8
HYUNDAI MOTOR	5	2.9
KIA MOTORS	4.7	1.1
SHINHAN FINANCIAL GROUP	4.3	2.4
SAMSUNG ELECTRO-MECHANICS	4.2	1
KOREA ELECTRIC POWER	3.6	2.7
KOREA AIRLINES	3.4	0.5

Source: Fidelity

Benchmark: KOSPI

References to securities are for illustrative purposes only and does not construe as a recommendation to transact in them.

12M P/E and 2010E P/B of Asian Pacific countries.



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