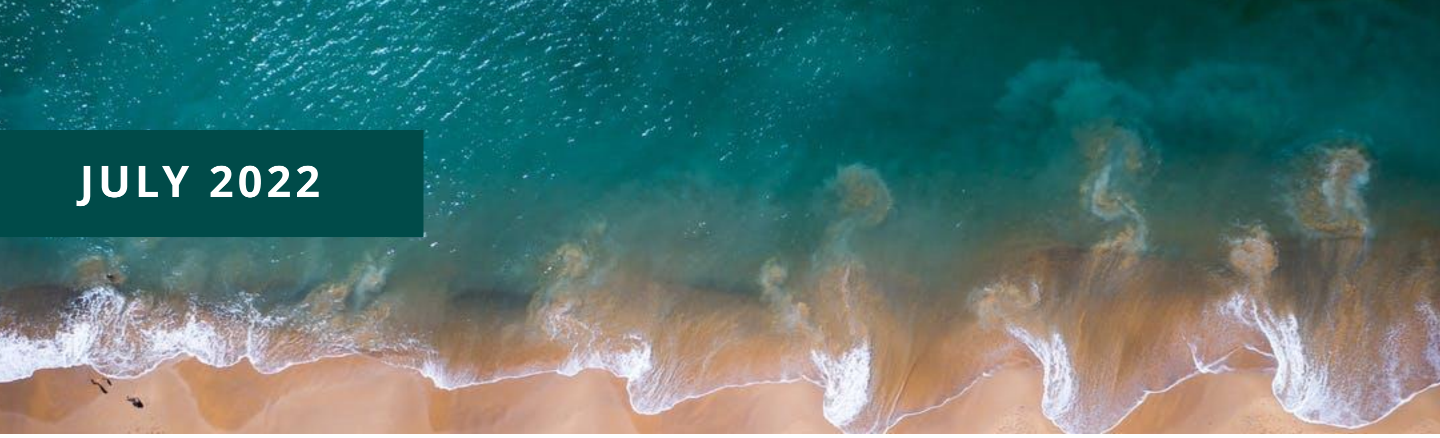


THINK DIFFERENTLY
TO GET DIFFERENTIATED RESULTS

Monthly Investment Update

Executive Summary

A brutal start to 2022 only got worse in June. Markets, across the board, continue to reflect a sea of red. After a strong performance in 2021, the S&P 500, along with the technology sector, ended up one of the region's hardest-hit markets this year. Bonds were no different either. "Safe" bond investments, such as the popular iShares 20+ Year Treasury Bond ETF, experienced double-digit declines. Amid the redness, there were few patches of green, of which Trend-following Alternatives were one segment that delivered positive returns.

Investing when times are tough can be emotionally hard, but they often present the best times to invest as markets offer a chance to invest at a better price. For instance, history has shown that investing in China 'A' equities whenever sentiment is bad has tended to reward investors, and those who had done so in recent declines would have meaningfully outperformed global equities. The same can be inferred for US small-caps going forward as they reach multi-year low valuations amid market weaknesses.

High inflation, rising interest rates, and fears of a recession have convinced many of a more challenging time ahead. While no one knows with certainty when or even if such times will come, what is certain is that economies and markets are self-correcting; and may even lead to slower inflation and lower interest rates down the road. In knowing of their possibility, investors would be better off preparing for them rather than timing these events, as we have done so by positioning in Healthcare and Quality Value.

Many would have adapted their spending habits in order to cope with higher prices (e.g. eating at home instead of at a restaurant). But not all things are as simple as that. One thing harder to control is the cost of mortgages, which banks are quick to adjust when interest rates rise. To ensure that one is ahead of the curve, one should consider investing in areas with a higher return, such as Asia High Yield which is currently yielding over 15% in a time where inflation has lowered fixed income investment returns.

Finexis Asset Management

MARKET REVIEW

The figure below is not a colour vision test. It actually shows the year-to-date performance for ETFs across asset classes.

Source: Bloomberg as at 4 July 2022

A few observations.

<u>It was a sea of red</u>
There were few places to hide. Historically, investors have counted on bonds to diversify when their equity investments are down. With interest rates hitting record lows in recent years, we warned that the classical bond shield would not be as effective.

As governments started to raise interest rates and reverse years of accommodative policies, bond investors were shell-shocked as they experienced double-digit declines in "safe" bond investments, underperforming even junk bonds. The popular iShares 20+ Year Treasury Bond ETF is down 22% this year, while the Singapore Government Bond UCITS ETF which only holds Singapore government bonds is down 7.6%. For a lot of investors, it is the first time in the past 40 years they got caught off guard by the "risk" which never existed in their minds. Even with all the warnings and reminders, it came as a surprise. **This shows that even when it comes to classical "safe" assets, valuation matters.**

<u>Some areas were very red</u>
The dark red areas represent investments that experienced the largest losses this year. Broadly, the areas are represented by tech and thematic funds. In the long run, these strategies are expected to do well but investors need to recognise that these are particularly volatile segments, and investing on stories alone is not enough.

Similarly, the US S&P was one of the worst hit regionally. What is the common element? No matter how one cuts it, the overvalued markets dropped the most. **This shows that sticking to the discipline on valuation, while it does not pay off immediately, will eventually work.**

<u>Some areas are less red</u>
Asia is not immune from the volatility but is faring much better. China 'A' equity markets are down in the single digits, dropping less than US government bonds.

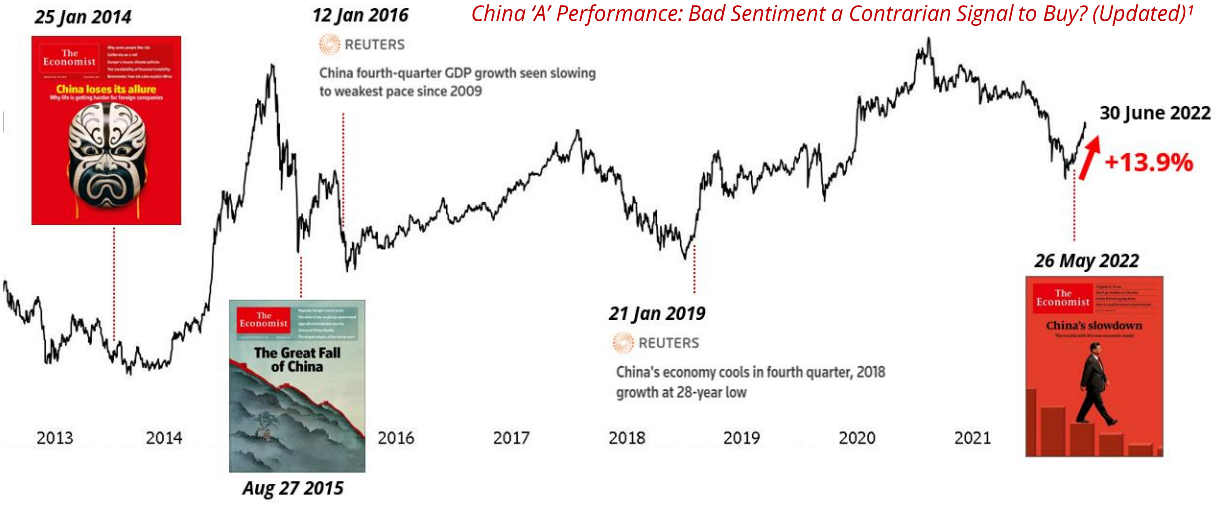
At the start of the year, Chinese market fundamentals were mixed: Regulatory and monetary policy pressures had abated, but economic numbers were lacklustre. Nevertheless, valuations of Chinese equities were pricing in recession scenarios which made it attractive enough for us to have active allocations. **This shows that bad stories and terrifying headlines often create good opportunities for investors who have done their work.**

<u>There are spots of green...</u>
...indicating positive performance. Investors might ask why their portfolios were not allocated to such segments at the start of the year. Let's see what some of these investments are: ProShares UltraPro Short S&P500, Direxion Daily 20+ Year Treasury Bear 3X Shares.

It'll be nice to say "if only I had invested in these funds at the start of the year." At this point, one needs to ask how likely they would have shorted the market at the start of the year. **Hindsight is powerful, only on hindsight.**

The good news is there is another segment that is positive this year and is easier to integrate into a portfolio: trend following. Despite the challenging environment, there have been strong trends across asset classes that trend following has been able to benefit from. As we mentioned before, unlike many other forms of investments including popular alternative strategies such as private equity, trend following is not dependent on markets going up to be profitable. **Even when traditional markets are challenged, true diversification can be achieved with the right alternative strategies.**

POSITIONING FOR RECOVERY



Does a market crystal ball exist? Last month (as an interesting thought experiment), we looked at where the China 'A' equity market was whenever sentiment was bad. The quick conclusion was that such periods of 'bad news' were good contrarian indicators for long-term investors to buy, not sell. As shown in the illustration above, the latest 'buy signal' triggered on 26th May 2022, after going through a meaningful decline. This was interesting for two reasons:

1. The China 'A' market had been a year-to-date underperformer up till then, lagging global equities by more than 9%.

2. Many investors had capitulated. One of the largest China 'A' ETF saw investors selling out more than US$1 billion worth of assets in March and April[2].

China 'A' performance since 26 May 2022: +13.9%. This positive return is even more impressive in the context of the 6% decline in global equities over the same period.

Unfortunately, we still do not believe there is a crystal ball that can accurately and consistently time markets, but there are a few important takeaways that we can gather. The first one is best summed up by Warren Buffet: 'Be fearful when others are greedy and be greedy when others are fearful'. Such uncertain periods are usually the best times to invest – however, this is emotionally hard to do as shown by investors getting out just in time to miss the rebound.

The other thing to note is that betting on past winners does not make it a winning investment going forward. Investors need to recognize that markets often take turns to perform; such is the ebb and flow of the market cycle. Consequently, investors will do well to have a process that can identify opportunities that are getting on the highway rather than coming off one.

Practically, the current situation is a reflection of improving Fundamental, Valuation, and Technical (FVT) inputs which are supportive of our China 'A' equity position. It also goes to show that good opportunities can still be found amidst today's uncertainty. **Here, we highlight another recovery position which is offering attractive returns for investors who can look past near-term concerns: US small-caps.**

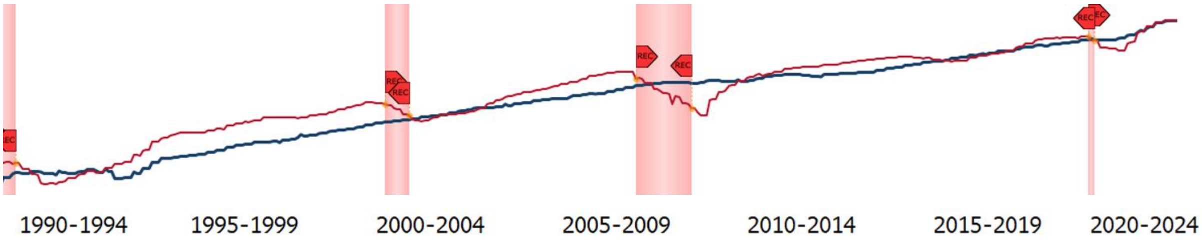
Indeed, the perceived 'higher risk' of small-caps may seem out of place given recessionary concerns today, but current price declines and multi-year low valuations are *already* pricing in a chance of recession. Subsequently, investors stand to benefit if things don't turn out as bad as expected. If they do turn out to be bad, we are comforted by the margin of safety that is present – already, we observed some signs of this playing out in Q2 2022; whereby the small-cap S&P 600 index declined by less than the 'blue-chip' S&P 500 in a risk-off market. At the end of the day, we seek to preserve strong rebound potential in our portfolios while avoiding the risk of permanent capital loss.

Source: ¹ Bloomberg, Reuters, The Economist. CSI 300 from 30/6/2012 to 30/6/2022. ²ASHR ETF.

STABILITY AMID VUCA

*VUCA is used to describe environments with **Volatility, Uncertainty, Complexity** and **Ambiguity***

Earnings Over Time for Healthcare and S&P 500



Last month, we discussed how our Stability positions provide True Diversification so that our portfolios remain 'seaworthy' enough to reach their intended destinations. This time, we discuss in further detail how this is achieved in the context of today's *VUCA* environment.

From our conversations, we note that **investors have a few key concerns today; namely inflation, rising interest rates, and the possibility of an incoming recession**.

Firstly, we caution against extrapolating such concerns too far into the future as economies and markets are ultimately self-correcting. Higher inflation and interest rates eventually lead to lower demand (or a plunge in activity which causes a recession), and subsequently lower inflation and interest rates. '*Big Short*' investor Michael Burry recently made headlines[1] for predicting exactly that – a period of slower inflation and ultimately lower interest rates.

If we do find ourselves in a period of higher inflation or slower growth, our stability positions – Healthcare and Quality Value equities - are well-positioned to withstand more than a few hard knocks and bruises. Take Healthcare for instance. The sector is relatively immune from inflationary pressures since the last thing anyone will do is stop getting medical care due to rising costs or even a recession.

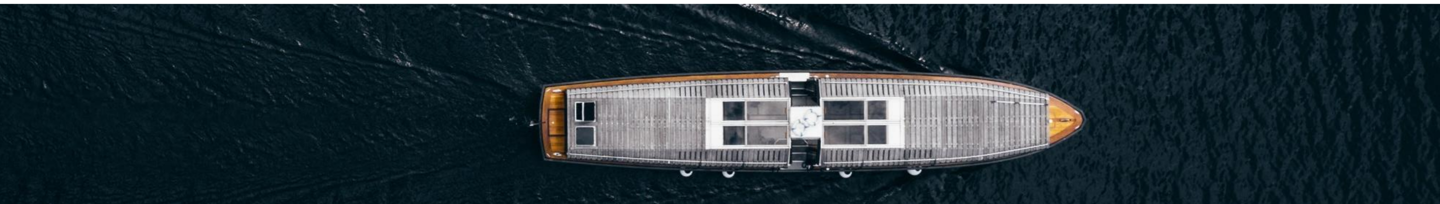
As illustrated in the above chart, this shows up in the stable earnings profile for the Healthcare sector as a whole. Earnings have even managed to hold up relatively well during recessions as indicated by the red shaded areas on the chart. It should not come as a surprise that the Healthcare sector has been one of the top performers during inflationary periods since 1939, according to Blackrock.

As mentioned before, it is also important to have a strong valuation discipline when it comes to long-term investing, as it is one of the best indicators of future returns. It also turns out that in periods of high inflation, investors were less willing to accept higher valuation markets like they used to, and instead reward investments with lower P/E ratios[2]. This bodes well for our Quality Value equity exposures, and our portfolios overall:

	Valuation (P/E Ratio)[3]
Our Equity Portfolio	12.1
Global Equities	13.7
S&P 500	15.8

Again, we remind investors that such uncertain periods are part and parcel of investing, and are good times for astute investors to pick up bargains.

Source: Bloomberg. [1]Bloomberg 'Michael Burry's Bullwhip' Tweet Deserves Serious Attention.
[2]Schroders. [3]Bloomberg, Forward 12 Month Est P/E as of 30/6/2022.



SEARCH FOR YIELD

Inflation has driven governments to raise interest rates, leading to a profound impact on investors.

The direct impact is on their fixed income investments. There is an inverse relationship between interest rates and bond prices i.e. rising rates leads to bond prices dropping. We will not belabour the challenges facing bond investors as we have covered this before. What we will mention is **we have positioned the portfolios for higher rates via segments of fixed income that provide higher coupon while being less sensitive to interest rates.**

When faced with inflation, investors can choose to adjust their habits: Take public transport instead of driving, eat at home instead of at restaurants. But one thing harder to control is their cost of home ownership.

Mortgage rates are rising with interest rates. Home owners would likely have received letters from their banks informing them of higher monthly mortgage payments. The chart shows how mortgage rates have more than doubled in less than a year.

https://www.todayonline.com/singapore/spore-mortgage-rates-roughly-double-6-months-set-rise-further-say-property-analysts-1891916

There are a few ways to mitigate higher mortgage payments.

Favourable loan package
Homeowners have been rushing to lock in favourable terms so that the increase in monthly payments is mitigated.

There is limited benefit from doing so. Banks have been quick to adjust their mortgage rates. As with investing, favourable terms tend to be secured before, not after the fact. Furthermore, many homeowners are locked in on their current loan packages and would have to pay a fee to reprice or refinance.

Higher salary
Another option is to get higher salaries to cope with rising pressures on home affordability. This is easier said than done at a time when companies are reviewing and even downsizing their workforce.

Even where companies are raising wages, they would do so by reducing their margins or charging more for their goods and services, in turn stoking inflationary pressures. Companies and governments are mindful not to get into an unsustainable wage-price spiral.

Investment that funds mortgage payments
The math is simple for a mortgage borrower: keeping money in the bank means one is lending the bank money at a low rate which the bank turns around to lend back to the depositor/home-owner at a higher rate.

One can address this by investing in areas with a higher return than their cost of mortgage. We have mentioned before that starting yield is a good indicator of future performance. For example, Asian high yield markets are yielding over 15% which is meaningfully higher than mortgage rates. This benefit does not come for free, one needs to pay with appropriate risk-tolerance. Green shoots are showing; property prices have risen on the back of policy support from the Central Bank, finance ministry, and local governments.

The search for yield is ever more relevant in an environment of higher interest rates. Compared to the first two options, **investing is a relatively scalable and controllable way for one to cope with higher mortgage payments.**

HOW ARE WE POSITIONED?

Positioning for Recovery	Stability Amid VUCA	Search for Yield
China ‘A’ Equities	Healthcare Equities	Asian High-Yield Bonds
Emerging Markets Equities	Quality Value	Emerging Markets Short Duration Bonds
US Small-Cap Equities		
Europe Equities		

The ‘Positioning for Recovery’ positions are expected to do well as the economy and markets gradually work through current shorter-term volatility, while the complementary Stability and Yield positions provide effective diversification to the rest of the portfolios.

ASSET ALLOCATION STRATEGY

-- Underweight | – Slight Underweight | = Neutral | + Slight Overweight | ++ Overweight

Equity: Regions

United States

US Small-caps as relative valuations are attractive and expected to benefit as economies recover. **Healthcare** as earnings are more stable and less dependent on broader economic cycle. **Quality Value** as valuations are attractive and expected to benefit as economies recover. Quality bias to avoid potential 'value traps'.

Europe

Relative valuations are attractive and expected to benefit as economies recover

Japan

Maintaining no exposure as they are less attractive compared to other opportunities

Asia Pacific ex Japan

Maintain **China 'A'** slight overweight as deleveraging cycle has taken its course, with credit conditions expected to improve.

Emerging Markets

Neutral as valuations are attractive relative to developed markets, but where earnings tend to be less resilient

Fixed Income

Global

Focus on currency-hedged government bonds and unconstrained credit to buffer portfolio volatility during periods of stress.

Investment Grade Corporate

Maintaining no exposure as low incremental yield and long duration credit exposure are less attractive than other segments

US High Yield

Maintaining no exposure due to relative poorer valuations.

Asia

Attractive yield across major fixed income markets with room for capital appreciation and better fundamentals.

Emerging Markets Debt

Hard currency short duration focus as a more defensive credit investment amid low rates.

MARKET INDEX RETURNS

Equity Regional	MTD	YTD	10Y	20Y
Global	-8.40	-19.97	9.36	7.83
United States	-8.26	-19.97	12.94	9.07
Europe	-8.00	-14.42	8.50	5.92
Japan	-2.06	-4.80	11.70	5.01
Asia Pacific ex Japan	-5.74	-15.65	5.35	8.59
Emerging Markets	-6.63	-17.57	3.42	8.78

Equity Markets	MTD	YTD	10Y	20Y
Australia	-8.76	-9.31	10.79	9.57
Brazil	-11.50	-5.99	6.13	11.52
China “A”	10.43	-8.30	8.45	7.62
China “H”	4.72	-5.22	1.40	10.09
Hong Kong	3.00	-4.82	4.70	7.33
India	-4.47	-8.26	13.28	16.75
Indonesia	-2.72	7.23	8.10	17.02
Korea	-13.14	-21.52	4.13	7.85
Malaysia	-7.94	-6.09	2.31	7.30
Russia	-5.83	-40.98	10.24	14.49
Singapore	-4.03	1.37	4.35	6.14
Taiwan	-10.52	-17.23	11.36	9.23
Thailand	-5.71	-3.84	6.22	11.15

Equity Sectors	MTD	YTD	10Y	20Y
Gold	-13.80	-13.91	-3.63	1.35
Energy	-16.91	31.64	4.25	7.57
Technology	-9.87	-29.64	17.10	11.53
Healthcare	-3.13	-10.06	12.87	9.36
Financials	-10.90	-18.73	12.44	4.45

Fixed Income	MTD	YTD	10Y	20Y
Global Aggregate	-3.21	-13.91	0.11	3.25
Global Aggregate (H)	-1.52	-9.06	2.23	3.62
High Yield	-7.29	-14.80	3.93	7.41
Asia	-2.17	-10.65	2.98	5.38
Emerging Markets	-4.57	-17.14	2.48	7.03

Note: (H) Currency Hedged

Currencies	MTD	YTD	10Y	20Y
USD/SGD	1.50	3.08	0.95	-1.19
EUR/SGD	-0.86	-4.98	-0.94	-0.92
JPY/SGD	5.48	17.94	5.46	0.64

Commodities	MTD	YTD	10Y	20Y
Gold	-1.64	-1.20	1.24	9.14
Energy	-7.77	40.62	2.21	7.09

*As of **30 June 2022**. Source: Bloomberg. Total return in index local currency terms. 10 and 20 year returns are annualized.*

“Far more money has been lost by investors trying to anticipate corrections, than lost in the corrections themselves.

Peter Lynch

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