JUNE 2022

THINK DIFFERENTLY

TO GET DIFFERENTIATED RESULTS

Monthly Investment Update

Executive Summary

May was a relative non-event compared to the first four months of 2022. Global equities and bonds were up marginally but remained depressed overall. Some have used the past months of declines as a reason to "cut losses". **Investors who have done so would have incurred permanent capital loss. They would also quash any chance of participating in the recovery** if they do not reinvest. The courage to re-enter the market at the same or even lower price than now is often difficult to find when needed the most. Many of the most successful investors such as Howard Marks and Warren Buffett consider current market declines as good news - great opportunities to acquire good investments at a discounted rate as market declines often pave the way to better future returns.

Amid depressed conditions, investors are tempted to believe that the best days are behind. For some markets, the best days are ahead as they have already priced in bad news. Such is the case for China 'A' and European Value equities where a slew of unfavourable events (such as the resurgence of Covid-19 in China and the Russia-Ukraine invasion) have weakened asset prices. But history has shown they do, eventually, recover to higher levels over time.

Those who chased high returns in popular names (such as Peloton, Zoom, and Netflix), through 2020 and 2021, would have given back most gains or more, as markets finally realized unprofitable or overvalued companies did not deserve such high prices. Investors would do well to know that markets have rewarded those who invest in businesses with profit over the long run, especially at favourable valuations. Therefore, we focus on Fundamental, Valuation, and Technicals (FVT) to ensure that we invest in areas with a good margin-of-safety and avoid those that have poor fundamentals and/or expensive valuations.

It is also common for investors to perceive market timing as a requisite to better returns. But history tells us it is much more predictable and repeatable to obtain above-average returns by acquiring investments with good fundamentals and valuations. Take Asia high yield as an example, history has shown that investors who remain invested during declines were rewarded with better returns. Investors who held during the top 15 periods of outflow averaged 9.03% 12 months after, as compared to locking in losses of -1.60% if they have sold. After all, markets are a device which transfers money from the impatient to the patient.

MARKET REVIEW

May was a relative non-event compared to the first four months of 2022; global equities and bonds were up 0.12% and 0.27% respectively[1]. Instead of focusing on the single month of May, let's see how things are as we near the halfway mark of 2022.

Good news Major markets are down, with global equities and bonds down -12.83% and -11.06% for the year ending May.
Bad news Investors are bailing out

At first glance, one might think we got the sequence above wrong. After all, how can markets being down be good news? And doesn't it make sense to sell now in case things get worse?

First let's look at investors bailing out. After seeing declines in equity and bond markets they were not expecting, investors are cutting losses. We will be blunt here: in doing so, they are

1. Locking in losses
2. Giving up on recovery of the existing investments
3. Missing out on gains from new capital

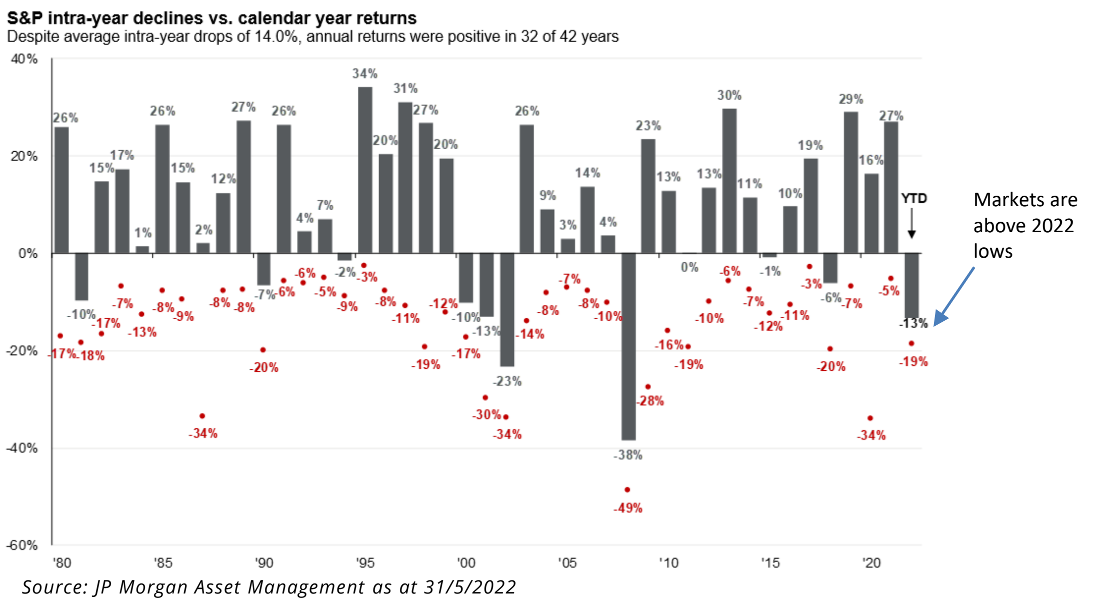
The chart shows that when investors bail out on declines, they are more likely than not to lock in and create permanent capital loss to a portfolio, which to us is bad news. However, such selling patterns happen all the time. They reflect the flushing out of weak hands, with the ensuing volatility creating opportunities.

The chart also shows that markets are above 2022 lows, which means more bad news for those who bailed out and will miss out on the subsequent recovery.

Why would we see market declines as good news? Because the flip side to price declines is better future return. Successful investing requires one to go against their natural instincts; to fight instead of take flight. Such counterintuitive behaviour is not unique. Leaning downhill while skiing, steering into a skid instead of slamming on the brakes; these are other examples where counterintuitive actions are critical[2].

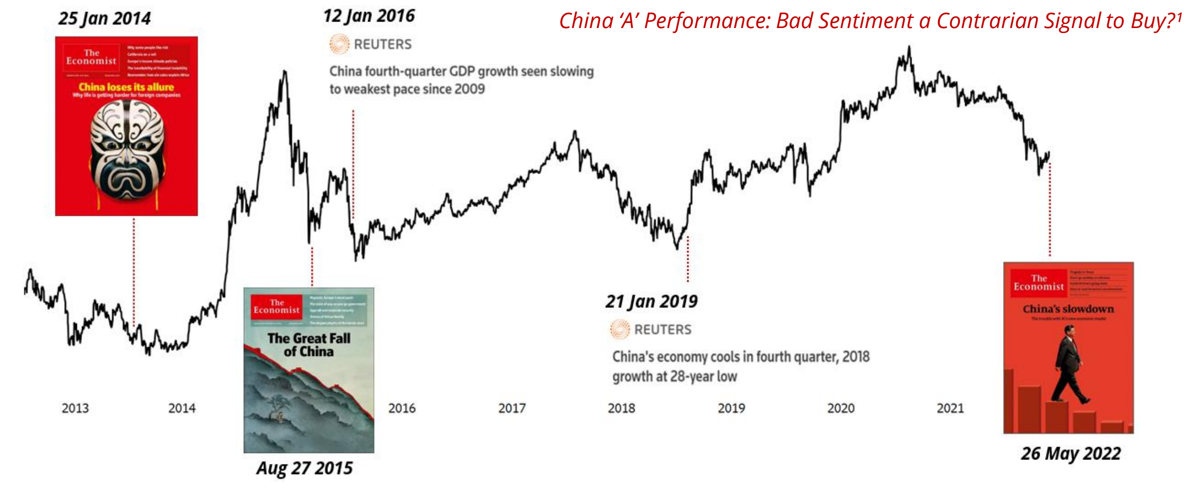
Howard Marks, one of the most successful investors out there, said this week[3] he was happier today than he was 6 months ago before markets tanked. He is not alone, other investors who have gone through multiple market cycles have mentioned that market declines are good rather than bad. If they have succeeded with such mindsets, perhaps it is worth considering if one can think that way too, or work with an investment manager who does.

[1]*Source: Bloomberg. Global equities: MSCI ACWI, Global bonds: Bloomberg Global Aggregate Index.*
[2]https://www.productiveflourishing.com/steer-through-the-skid/
[3]https://youtu.be/4Q_bluCd5V4?t=61



Source: JP Morgan Asset Management as at 31/5/2022

POSITIONING FOR RECOVERY



After months of market declines, some investors are starting to think that the best days are behind for markets. But seemingly endless bad news has tended to come together with down markets and this time is no different. Today's news headline came courtesy of JPMorgan's CEO Jamie Dimon, who warned of an incoming economic 'hurricane'. Even more recently, Tesla's CEO Elon Musk said that he had a 'super bad feeling' about the economy. Should investors worry?

It's always darkest just before the dawn.

It is important to recognize news headlines for what they are – events that have usually already happened. Since markets are forward-looking, any bad news is quickly priced in, at which point future returns are expected to be better provided the investment is of good fundamentals and valuations.

The illustration above shows the performance of China 'A' equities, where we currently have a slight overweight. An interesting thought experiment is to look at where the market was when sentiment was poor – represented by *The Economist* covers, and *Reuters* news headlines. A quick glance shows that these 'bad news' are good contrarian indicators for long-term investors to buy, rather than sell. The latest *The Economist* cover is titled 'China's Slowdown'. At the same time, our time-tested FVT indicators are turning more favourable, with the Chinese economy also starting to re-open from harsh Covid-lockdowns. As long-term investors, would you buy or sell?

Another example relates to investments in European Value equities, which seemed to be in the eye of the hurricane earlier this year as the Russia-Ukraine invasion happened. Today, it is one of the best performing major markets this year as 'FVT' drivers prevailed noise in the market: **better valuations provided a margin-of-safety amidst the broader market sell-off.**

For those who are more numerically inclined: a recent study by Goldman Sachs showed that the best days often come after markets' worst moments – the median return following the start of bear markets is +24% in the following 12-months. This is more than double compared to investing in 'normal' periods. The conclusion was that 'the risk of missing out on the recovery still exceeds the risk of further pullback'. No one knows for sure if markets will be higher or lower tomorrow, next week, next month, or even next year. **What we do know with high certainty is that markets will eventually be higher and investors who can sit through or even take advantage of such temporary market declines will be rewarded over the market cycle.**

Those still concerned about Jamie Dimon's earlier ominous forecast may instead be reassured by one of his employees. Marko Kolanovic, a top-ranked strategist and co-head of Global Research, remains positive that 'there will be no recession given support from US consumers, global post-COVID reopening, and China stimulus and recovery".

[1] Source: Bloomberg, Reuters, The Economist. CSI 300 Index from 2/6/2005 to 2/6/2022.

STABILITY AMID VUCA

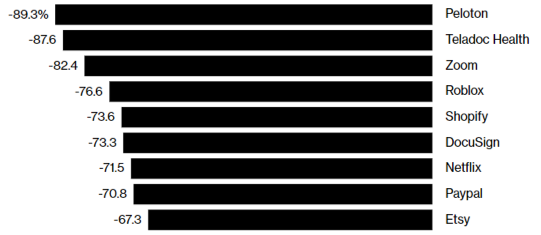
VUCA is used to describe environments with ***Volatility, Uncertainty, Complexity*** *and* ***Ambiguity***

Think of two ships that encountered the rough seas of 2022. The first has a gaping hole and the crew is frantically working to bail water, but they ultimately fail and abandon ship. The second ship has taken some damage but is otherwise seaworthy. The crew is able to continue navigating through rough conditions to arrive at their destination.

While investors are in the red this year, there are two types just like the ships above.

One type is distracted (even distraught) nursing large losses that they did not expect. In the past two years, investors were drawn to investments that were shooting out the lights with triple-digit gains. They have just as quickly given back most of these gains and in some cases much more:

Percent Drop From Record High[1]



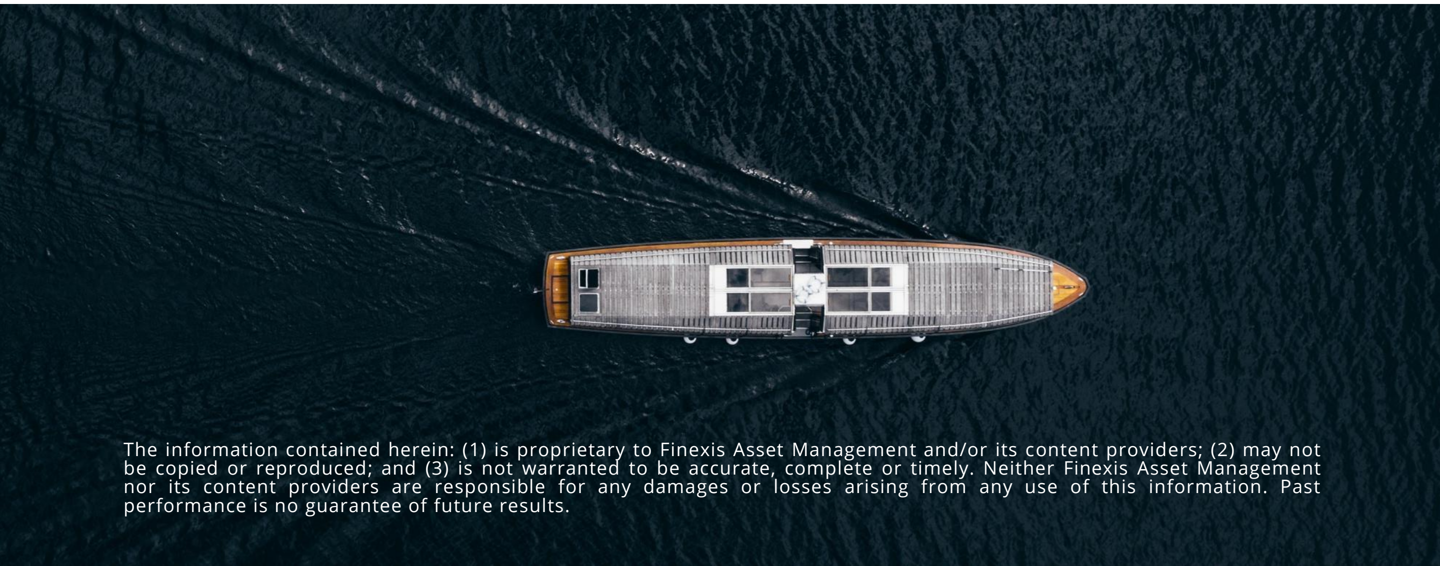
To make things worse, the dollar losses are likely to be larger because more capital was added as prices went higher. This is not us fearmongering; fund flow data reflects investor behaviour that repeats time and again. **What is clear is that a lot of money is late to the party, without paying attention to fundamentals or valuations.**

The steepest declines were concentrated in unprofitable or excessively overvalued companies, as shown in the earlier sample of stocks with large drawdowns. In hindsight, it is now clear to all that such steep declines should not be so surprising. **Throughout the history of capitalism and markets, long-term investors have been rewarded by investing in businesses with profit**, especially when they are offered at attractive valuations. Our 'FVT' process is borne out of this fact.

During volatile periods such as the one we find ourselves in today, how do we stay level headed so that we can 1. stay invested and 2. take the offensive and capture opportunities as they present themselves? Our Stability positions provide True Diversification so that our portfolios remain "seaworthy" and investors are assured that they can reach their destinations.

The benefit of True Diversification is that investors are more able to ride through the emotional roller-coaster that ensues when markets go through inevitable boom-bust cycles. As a reminder, Healthcare and Quality Value equities have a more resilient and stable earnings profile that is expected to hold up better if the economy slows even further (we cannot predict, we can only prepare!). They complement our other positions with meaningful recovery potential. The flip side is that our portfolios may at times seem 'boring' compared to more 'exciting' ones, but they are portfolios built to last.

[1]Source: Bloomberg, May 4th https://www.bloomberg.com/news/articles/2022-05-04/peloton-to-zoom-at-risk-even-after-218-billion-rout-tech-watch?sref=EnJawTd3



SEARCH FOR YIELD

What is the basic objective of investing?
Buy low, sell high.

However, we see more evidence of the opposite: buy high, sell low. When markets are rallying strongly, investors feel like buying. When markets are dropping, investors feel like selling. This psyche, if not managed well, actually lends itself to buying high, and selling low.

The long term return for Asian high yield investors is 5.8%*, arguably a decent return for buy & hold bond investors. Let's take a look at the results of investors' selling activity for Asian high yield funds. The table shows the performance for investors who sold their investments during the largest outflows, and for those who held on to their investments.

An investor who capitulated and sold along with everyone else would have lost -1.60% in the 12 months leading to their disposal. An investor who remained invested during the top 15 periods of outflows would have averaged 9.03% 12 months after. **Both groups have meaningfully different outcomes compared to the buy & hold investor.**

The performance gap is even wider during the periods of strongest selling pressure, as shown from the top 5 outflows. In March this year, the outflows were USD 891,702,135. We cannot predict what the return will be 12 months on, but history can be very telling.

We draw a few lessons from the data.

- Capitulation will happen again and again
- Don't capitulate; the worst time to sell is when the urge is the strongest.
- Buying when others capitulate makes one better off than the average investor

This is why we prefer evidence-based investing rather than feel-based investing.

To do so, one has to manage their natural compulsions, so that they do not react to market moves in ways that backfire on their wealth goals.

Capitulation tends to coincide with market bottoms. We have also said that it is hard if not impossible to consistently pick bottoms. The good news is that once an investor has addressed the urge to capitulate, they will find multiple opportunities to be better off than the rest.

Why? Because the math is clear. Markets reward buy & hold investors with a long term compound return. An investor who buys at any point below that long term trajectory will be better off than the buy & hold investor. **One does not need to market time to be better off.**

Of course when markets decline below that long term trajectory, one cannot resist the urge to pick the bottom. The reasons are obvious because investors want to

1. Avoid further losses
2. Get maximum return

Howard Marks is not just one of the most successful investors, he has been doing that in high yield markets. Even the guru admits that picking bottoms is beyond him, and prefers to capture a few good opportunities along the way down. The rest of us should stop dreaming of picking the bottom, and invest when markets are declining, and below their long term trajectory.

There is an important caveat: they **need to have staying power.** The path to recovery will be affected by policy response to inflation, and how the world transitions to covid as an endemic disease. After all, markets are a device which transfers money from the impatient to the patient.

Asian high yield bond funds	Top 15 largest outflows	Top 5 largest outflows
Ave. Net outflows USD	-262,981,833	-502,303,389
Ave. 12-month realized return if sold	-1.60%	-6.38%
Ave. 12-month forward return when held	9.03%	12.02%

*Source: *Bloomberg, ICE BofA Asian Dollar High Yield Corporate Constrained Index from 31/12/1996 to 31/5/2022. Morningstar asset flows for Asia High yield bond funds from May 2012 to May 2022.*

HOW ARE WE POSITIONED?

Positioning for Recovery[1]	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		

[1]*The first theme is now '**Positioning for Recovery**' to better reflect the nature of the underlying positions. As a reminder, these positions are expected to do well as the economy and markets gradually work through current shorter-term volatility. The complementary Stability and Yield positions continue to 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	0.18	-12.64	10.86	7.96
United States	0.18	-12.76	14.38	9.14
Europe	-0.61	-6.98	9.96	5.88
Japan	0.69	-2.80	12.71	4.66
Asia Pacific ex Japan	0.19	-10.52	6.38	8.64
Emerging Markets	0.46	-11.72	4.53	8.72

Equity Markets	MTD	YTD	10Y	20Y
Australia	-2.45	-0.60	11.89	9.84
Brazil	3.22	6.23	7.41	11.40
China “A”	2.08	-16.95	6.76	7.86
China “H”	2.12	-9.50	1.07	9.93
Hong Kong	2.15	-7.60	4.95	6.83
India	-2.17	-3.96	14.67	17.25
Indonesia	-0.67	10.22	8.83	16.91
Korea	-0.34	-9.65	5.67	8.24
Malaysia	-1.73	2.00	3.31	7.63
Russia	-3.43	-37.32	11.58	14.31
Singapore	-2.80	5.63	5.17	5.94
Taiwan	1.31	-7.50	12.60	9.32
Thailand	0.05	1.98	7.13	11.21

Equity Sectors	MTD	YTD	10Y	20Y
Gold	-9.34	-0.12	-1.96	2.11
Energy	15.77	58.43	6.79	8.56
Technology	-1.49	-21.93	18.67	11.41
Healthcare	0.55	-7.15	13.92	9.16
Financials	2.73	-8.78	14.30	4.80

Fixed Income	MTD	YTD	10Y	20Y
Global Aggregate	0.27	-11.06	0.48	3.59
Global Aggregate (H)	-0.14	-7.66	2.37	3.75
High Yield	0.49	-8.09	4.99	7.15
Asia	-0.22	-8.66	3.39	5.52
Emerging Markets	-0.02	-13.17	3.24	6.98

Note: (H) Currency Hedged

Currencies	MTD	YTD	10Y	20Y
USD/SGD	-0.98	1.55	0.61	-1.32
EUR/SGD	0.81	-4.16	-0.80	-0.63
JPY/SGD	-0.79	11.81	5.09	0.18

Commodities	MTD	YTD	10Y	20Y
Gold	-3.14	0.45	1.65	9.02
Energy	9.53	52.47	2.86	7.85

*As of **31 May 2022**. Source: Bloomberg. Total return in index local currency terms. 10 and 20 year returns are annualized.*

“The stock market is a device which transfers money from the impatient to the patient.”

Warren Buffett

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