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Malayan Traders Capital
Founders Fund

Commentary

June 2015

Written by Devan Linus Rajadurai, Chief Investment Officer

Objective

Malayan Traders Capital Founders Fund ("Malayan Traders", "MTC" or the "Fund") aims to achieve a net return of 10-15% p.a. over a 3-5 year period by investing in a portfolio of global listed equities. MTC invests predominantly in blue chip companies listed in the US and Emerging Asia and employs a value driven, bottom-up investment approach. MTC's benchmark is the Singapore Straits Times Index ("STI") and the MSCI All Country World Index ("MSCI ACWI"). The STI was chosen as a benchmark as MTC's investors predominantly originate from Southeast Asia, where the STI is the most commonly followed index. Performance is reported in USD.

Performance

At the end of May, MTC delivered a year-to-date ("YTD") return of 12.3%, driven by a combination of shrewd stockpicking; a thorough understanding of the global economy and the corresponding overvaluation of certain markets; and knowing when to get out. However, for the month of June, MTC's portfolio retreated -5%, mainly due to the contagion effect of China's stock market bubble bursting and the potential default of Greece. Nonetheless, despite the negative performance this month, the majority of our portfolio companies (we have exited some of our long term winners) are the cheapest they have ever been. To understand our investment philosophy and its implementation, we discuss three regions: China, South East Asia and US.

Market Insights

Overhype of China

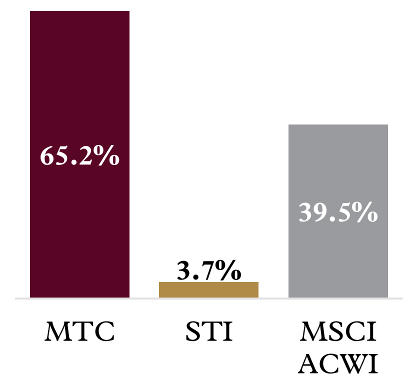
On May 28th, the second last trading day of the month, the Shanghai Composite closed 6.5% down, after a yearlong streak of bubble-type gains. This was one of the main drivers that caused our performance decline, despite the fact that we had already exited all our positions in China and Hong Kong (the contagion effect of the decline in one market affecting other markets). We commented on the formation of this bubble in our April commentary where we noted that up until July 2014, the Shanghai Composite was tepid and hovering around the 2,000 mark. From then until the end of June, just before the bubble popped, the Composite was at the 5,000 mark – a staggering 150% return.

NAV

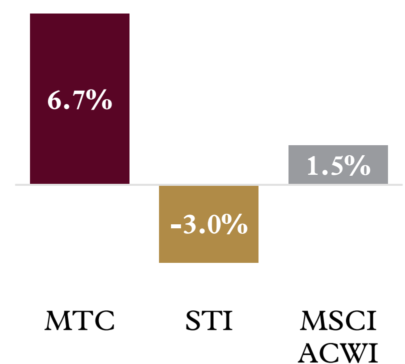
Class A:	165.21

Performance

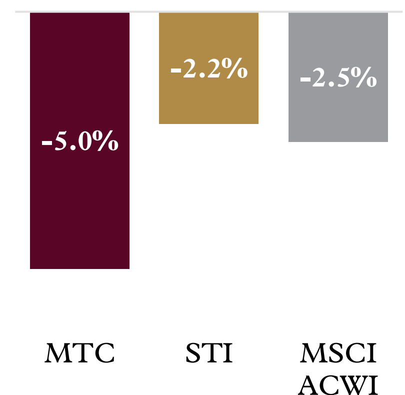
Since Inception (24 Jul 2012)



Year to Date (2015)



Month (Jun 2015)



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Market Insights (continued)

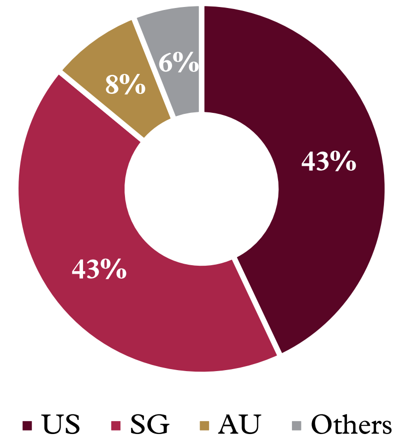
Overhype of China (continued)

Despite this single day retreat, the overhyping of China persisted, with many intelligent economists claiming that this was merely a temporary correction. News such as Great Britain joining the Asian Infrastructure Investment Bank and China overtaking the US as the world's superpower continued to fuel China's growth story. While aspirations are great and encouraging, one must also face reality, and the reality is that a large billion dollar company like Gome Appliances cannot fly from HKD1.00 to HKD2.00 in a week, no matter how large the population in China is; that China's property prices in the major cities are overpriced – the Chinese government themselves are indirectly admitting this by imposing cooling measures; and that China's GDP growth is no longer 10% p.a., but (a still respectable) 7%. There was a period when it was evident that China was undervalued i.e. in 2014, which resulted in us investing in Chinese financials; but at times the market can get ahead of itself and become excessive. Having said that, we continue to believe in the strength of the Chinese economy. However, we feel that it is not being valued correctly at this point. We don't want a situation where we are investing in Alibaba because of the hype, only to lose 50% in the subsequent months after its IPO (like Facebook did); rather we want to buy a great company like Alibaba when it is actually trading at reasonable levels (like how we bought Facebook in Dec '12). Throughout July, we are seeing the Chinese market fall tremendously, and when it falls enough we will swoop in again and buy the good and great companies of China on the cheap.

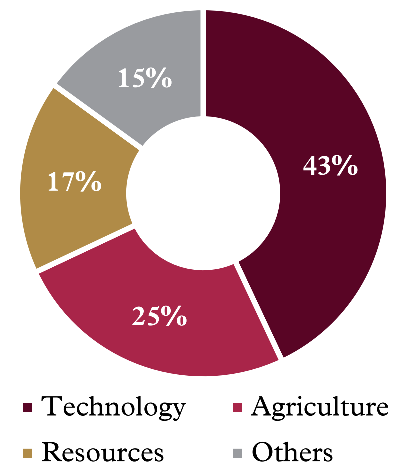
Value of South East Asia

For the first half of the year, South East Asia ("SEA") as a region has not been doing very well, with the STI, KLCI, and the Jakarta Composite Index returning -1.4%, -3.1%, and -6.1% YTD respectively. Further, the Malaysian Ringgit and the Indonesian Rupiah have both retreated by about 15% against the US Dollar since July 2014. Add the price crashes in oil, coal, copper, and palm oil to the equation and it is pretty self-explanatory as to why these economies are significantly hurt. To make matters worse, you have the political disappointment of Indonesian President Widodo coupled with the slew of public scandals and broken campaign promises, and the ongoing investigations of 1MDB that has caused major upheavals in Malaysia. For SEA, the index is not necessarily a true reflection of the region's performance as companies in the index are usually supported by the respective country's governments. What you don't see is huge stock price crashes of companies not represented in the index.

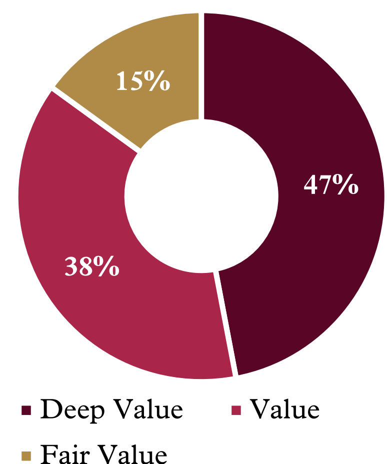
Company Listing Breakdown



Sector Breakdown



Value Breakdown



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Market Insights (continued)

Value of South East Asia (continued)

As such, in SEA, you can find very cheap companies that have solid businesses with good management teams that global institutions have overlooked (partly because of the big behemoth, China), and a tremendous opportunity to generate outsized returns.

Stability of the United States of America

If you reside in Asia, chances are that everyone you speak to tends to be "pro-China and no-US". We on the other hand, have been pro-US since 2008 despite it being the instigator of the global financial crisis. We are still pro-US today. The proof is in the pudding, with GDP growth averaging over 2% for the past 5 years, unemployment declining from 10% to 5%, and the continued emergence of business, innovation and a corresponding stock market appreciation. In the last 5 years, the US created the shale oil and gas boom, innovated electrical vehicles for the masses, and spearheaded the creation of smartphones and tablets for the world, among others. As a result of being pro-US, our portfolio has appreciated close to 70% since our inception and the family office that we previously managed since 2007 has more than tripled (3X) mainly because of the US. We have always maintained that we will invest about half of the portfolio in US-listed companies that are not just focused on the US economy, but also deriving revenues from overseas and importantly, benefitting from the growth in Asia. A lot of economists talk about the imminent increase of interest rates and how it will affect the stock market, but the reality is that there are still great and growing US-listed businesses that are not overpriced and are able to weather the storm when things turn sour.

Portfolio Companies

Personal Computer Manufacturer

In the last few years, there has been a lot of talk about the death of the personal computer, with smartphones being their replacement. As such, a lot of chipmakers, hard disk manufacturers, and PC manufacturers' stock prices have languished since 2010. It takes a deep understanding of the industry and the company to make a sound investment in this space. We scoured the tech hardware sector for companies that exhibited positive balance sheets, consistent cash flow generation and sound management and strategy to find hidden gems worth investing in. What we found after hours and hours of research was a PC manufacturer that had previously bought another company's hardware division, integrated it into their own, achieved economies of scale, and perfected supply chain penetration into emerging South America and Asia to deliver growth. The overall disinterest in the industry had made its stock cheap, and undervalued the company's ability to capture market share from the other players. More importantly, management demonstrated their ability to innovate and adapt to the threat of the smartphone. The company now not only assembles PCs, but is also a huge manufacturer of mobile phones and servers, and as a result has generated a return of more than 40% over a 2 year period. We have sold this company, but the said company's stock is retreating again which could present an opportunity. It is never wrong to sell something that is overvalued and buy it back when it becomes undervalued. Also, the PC is not dead!

Outlook

The retreat in our Fund's NAV is not necessarily a negative, but rather a great opportunity for investors to get in on the cheap. Most of the companies we currently own are either at or approaching deep value levels. We are about to clear some of the companies that we have held for many years to take advantage of the opportunities in South East Asia and/or China once the dust from the market selloff settles. The rout of China and Greece has created a great opportunity, and to reiterate what we said in our Dec '14 commentary: "*If you're a passenger in a ship entering a storm, you would be better off having a capable captain handling the ship, rather than commissioning a good-looking but inexperienced sailor or trying to steer the ship*

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Outlook (continued)

yourself." Since Dec '14, we have delivered 6.6% for our investors, and in the next 3-4 years we expect our portfolio to go up by at least 100% (2X) given the opportunities present today.

Disclaimer

The views expressed in this report are those of Devan Linus Rajadurai, MTC's Founder & Chief Investment Officer. MTC's investment strategy is implemented by the Fund's Investment Manager, MTC Asset Management, with the support of its sister entity, MTC Asset Management (M) Sdn. Bhd. licensed by Securities Commission Malaysia (CMSL: eCMSL/A0333/2015), which provides research and operational support to MTC Asset Management. The Fund is a regulated mutual fund under the Mutual Funds Law of the Cayman Islands and is registered with the Cayman Islands Monetary Authority. This report is up-to-date as of 1 August 2016.

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