invest@mtcasset.com
+60 3 2289 5055

Commentary (Founders Fund)

September 2018

Written by Devan Linus, Chief Investment Officer

Objective

MTC Founders Fund ("Founders", "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 Kuala Lumpur Composite Index ("KLCI") and the Dow Jones Industrial Average ("DJIA"). The KLCI was chosen as a benchmark as MTC's investors predominantly originate from Malaysia, where the DJIA has historically been the best representation of the global companies. Performance is reported in USD.

Performance

MTC delivered a since inception net return of 75.5% (9.4% p.a.), outperforming the KLCI and underperforming the DJIA, which returned -15.6% (-2.6% p.a.) and 109.7% (12.6% p.a.) respectively.

Benchmark Comparison

We declined significantly for the quarter, at -5.3% in comparison to the DJIA that appreciated 9.0%. This has greatly affected us and hence our underperformance since inception performance against the DJIA.

The core difference in performance between MTC and the DIJA is that the DJIA has been influenced significantly from the appreciation of tech component stocks namely Apple, Cisco and Microsoft and other top gainers such as Merck in healthcare and Visa in financials. In combination these five stocks appreciated 16% for the period, which pulled up the overall DJIA performance.

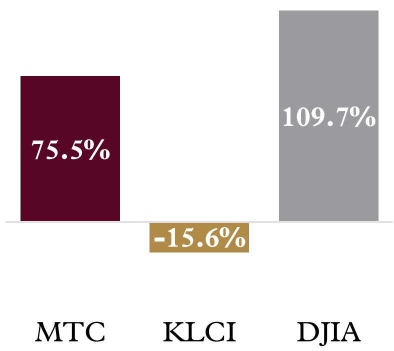
Whilst we have recognised our underperformance, the action we have taken in rebalancing the portfolio is deliberate and important as we feel many tech stocks are overly valued, such as the FAANG (Facebook, Apple, Amazon, Netflix and Google) which on average pays only a dividend yield of just 0.3% and has a high average PE of 75. Furthermore, other companies such as Merck and Visa that has generated a good returns for the year are generally considered low growth companies that we feel have minimal room for further appreciation based on current valuations.

NAV

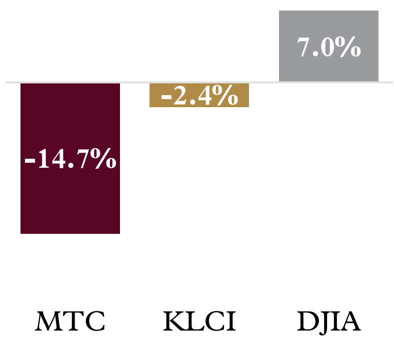
Class S: 175.51

Performance

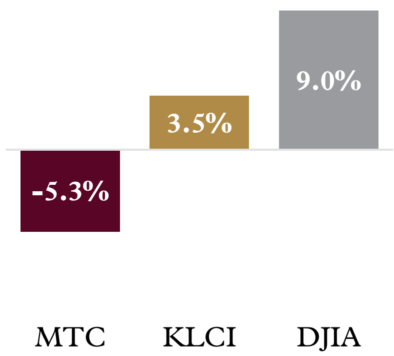
Since Inception (24 Jul 2012)



Year to Date (Sep 2018)



Quarter (Sep 2018)



Copyright © 2012-2018. All Rights Reserved.

Devan Linus, Chief Investment Officer

Benchmark Comparison (continued)

Another reason for the underperformance is that the stock prices within our new portfolio hasn't necessarily appreciated just yet. We have generally shifted the portfolio into stocks in tech hardware, media and retailing sectors that continue to underperform for the quarter.

Buying at the absolute bottom is almost close to impossible, and it is common to experience a further drop of up to -20% before we start seeing the recovery and perhaps a 100-200% appreciation in the next 3-5 years. The difference compared to prior periods for the Fund, is that we have shifted our portfolio significantly all at once from the high growth tech stocks to what we call slow growth but deep value companies (81% of the portfolio). To give comfort, our portfolio is averaging a dividend yield of approximately 6.0% and has a low PE ratio of 10.1.

Lastly, our underperformance is also due to the geographical shift of our portfolio where we now only have a 34% allocation to listed companies in the US; while indexes outside the US have not performed as well as the US. The ASX200, DAX, and STI for example have only performed 0.5%, 0.1% and 0.6% respectively for the quarter. We continue to remain bullish on the US in general, but we do however note the overvaluation in many companies.

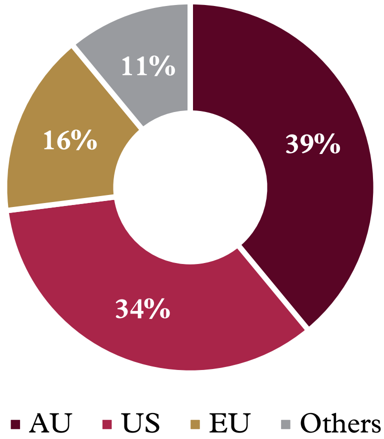
Market Insights

US-China Trade War

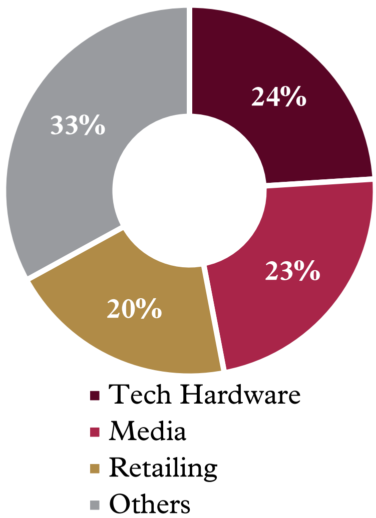
In addition to the above, the macroeconomic headwind of the US-China Trade War has also exacerbated the volatility in the capital markets and more so for listed companies outside the US which have resulted in negative stock prices. We are of the overall view that the impact of the US-China Trade War is to the benefit of the US, as China is a net exporter to the US. Hence, the effect of tariffs or extra protectionist measures would hurt China more (hence why we are not invested in China). Furthermore, while US does rely hugely on China for growth, they also export and manufacture in many other regions in the world, a big growth area being South America, and their long-term trading partners such as Japan and Europe that are not necessarily big fans of China.

As a fund, we must be completely aware and up to date with this issue and have to invest in companies where the impact of the trade war will impact us minimally. As such, we have invested in companies that are not significantly dependant on China's growth and are predominantly deriving their earnings from their home and local markets. Companies in the Tech Hardware, Media and Retailing space in our portfolio are examples of the above. It is unlike construction or commodities that are influenced heavily by macroeconomic factors.

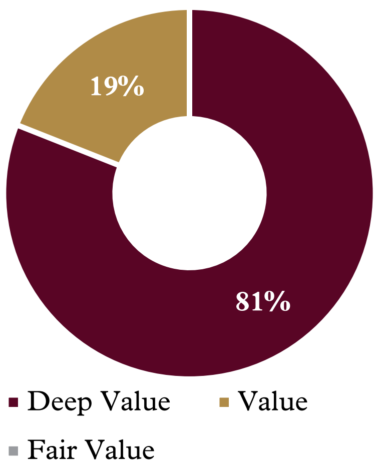
Company Listing Breakdown



Sector Breakdown



Value Breakdown



Copyright © 2012-2018. All Rights Reserved.

Market Insights (continued)

Oil Price Recovery

The potential sanctions on Iran by the US, the prior sanctions on Qatar in 2017, and in addition to the various Middle East geopolitical issues has resulted in a big oil price recovery from its low in 2016. To put this into perspective, Brent has appreciated 122% from Jan 2016 to Sep 2018 from a price of $37.22 to $82.72, and the market pundits are talking about oil potentially surpassing $100 mark. This sudden increase in oil prices, especially when people thought in 2016 was doomsday, helps to solidify the concept of value investing that if you buy at the low and if you are patient enough, you can expect significant returns. The main point here that we want to emphasize is the potential benefit that high oil prices have for oil depending nations such as Malaysia, Middle East, US, etc. For other emerging markets where the countries are net importers, the sudden surge in oil prices have created a quick shock that has resulted in declines in the respective stock markets. Ultimately, the key question that we should be asking is whether oil prices in its current value is the new normal? Why? Because when companies and countries adjust to the new normal, you are likely to see significant pickup in the markets for those countries. Hence, we see a major buying opportunity as emerging markets has been hammered because of this. We would like to reiterate that we exited all of commodities at the tail end of 2016 but should prices dip again, we could go back into it. Alternatively, we could stay away from pure commodity plays but invest only in companies that might benefit indirectly from the trickle-down effect. The key thing here is that this increase in oil prices have created a buying opportunity as a result of an emerging markets decline.

We are definitely not oil experts and we are certainly not predicting prices for the next months or year, but we do understand from our high-level analysis of historical trends in industries that it takes years for boom and bust cycles to form. The recent bust in 2016 should show evident that a future bust isn't in the short term horizon as we are only two years in from the last bust.

Portfolio

High Dividend Yields

In the six years of running the fund and the last decade managing a value investing family office, we have benefited tremendously by investing in value growth companies specifically in the technology sector. At every other decade, a new theme in terms of high growth industries will form, and we feel we are at the tail-end of the tech boom. Therefore, in the interim as we look out for these new growth industries, we are being defensive in our investment strategy by shifting to high dividend yielding stocks in stable, well run and innovative businesses. Capital preservation for the long term has always been our goal and objective. Whilst there are short term volatilities in this defensive strategy, our comfort is in the dividends we are going to receive over the next few years. In addition to that, we have selected and invested in companies that have shown a history of good management and innovation in driving strong capital growth.

For example, one of the automobile company that we have invested in, owns a majority subsidiary that operates in the ride hailing space and is a significant rival to Uber in the geography that it is operating in. Secondly, over the last two decades they have shown the ability to ride out the crises of the Tech Bubble in 1999, the Global Financial Crisis in 2008 and the European Sovereign Debt Crisis in 2010 just to name a few. Thirdly, their innovation has continued in the emergence of leading electric cars which sales should surpass Tesla very soon, and its testing of autonomous vehicles. Lastly, it pays a high dividend yield above 5%.

Copyright © 2012-2018. All Rights Reserved.

Portfolio (continued)

High Dividend Yields (continued)

Another example would be in one of the retailing company that we have invested in. They have already introduced an ecommerce website with a variety of features from book and collect, deliver to home, price matching, etc. where they have managed to provide a unique alternative to Amazon in the geography that they are operating in. Secondly, similar to the automobile company above, they have shown the ability to ride out the financial/economic crises of the last two decades. Thirdly, they own a portfolio of real estate in developed nations that have shown consistent real estate prices and GDP growth. The real estate portfolio is also a good hedge during an economic down cycle in that when retail profits drop, they can substitute the profits through rental income. Fourthly, they have continued to innovate by expanding to other emerging markets and re-fitting their retail stores to serve a new wave of customers. Lastly, it pays a high dividend yield above 5%.

The Changing of the Media Landscape

With the resurgence of tech companies in the last decade, the media space too has changed significantly, where you see traditional media companies being supplanted by new tech conglomerates that are benefiting from the increase penetration of the internet and mobile usage. This has enabled companies such as Netflix to sit at the same level playing field as companies like Disney, Fox Studios, and Time Warner. Netflix do not just distribute and charge for content but instead are now producing content that have generated close to the same number of awards in the Emmy's as their rivals. When it comes to advertising on the other hand, newspapers and broadcast TV are now being supplanted by online rivals such as Google which owns YouTube or Facebook which owns Instagram. They have shown the ability to generate better advertising rates through the unique targeting strategy using big data to better understand consumer preferences much better than traditional newspaper and broadcast TV.

We now have a 23% allocation to Media and we are embracing the new companies that understand how to adapt their businesses to the ever changing media landscape. Our investment is not only in the tech conglomerates, but also in the traditional media that can adapt and innovate. Good examples of traditional media are NBA and WWE. Both two have created their own app, distribution platform and have managed to maximise the value of their content by charging on all angles by increasing variety, expanding global reach while still fending off competition from the tech conglomerates. You still can't watch a full live match of the NBA or WWE on YouTube or Netflix, and their user base on their relevant platforms has been growing steadily over the last few years. Although NBA isn't a listed company, WWE is and their share price performance that has appreciated >400% in the last three years from a price of $17.61 in Jan 2016 to $96.73 in Sep 2018.

We believe in owning a combination of traditional media and online media companies to manage risk as one has to be careful of crazy overblown valuations which a lot of online media companies tend to have. Prior to 2000, the darling media stock was AOL and Yahoo (that had high valuations and low profits), and today they are almost non-existent whereas the likes of Disney, Fox Studios and WWE still exist and are thriving. We continue to research, compare and evaluate this growth sector that should provide a good balance to our high dividend yield plays. A final supporting argument to this sector is China. Regardless of the trade wars and macroeconomic headwinds, China has a growing middle class where media and content is going to be a big part of their lives and spending.

Copyright © 2012-2018. All Rights Reserved.

Outlook

Despite our bullishness of the portfolio as described above, we do have to re-emphasize that the market and macroeconomic headwinds that we are currently facing will provide some instability. Hence, in the short term, we are expecting continued volatility to our portfolio and we don't expect a good return for 2018, reiterating our comment from the last commentary. We do acknowledge that a crisis is forming but again we reiterate, we don't see this taking place anytime soon given the strong US economy and the recovery of oil prices. We compare 2018 to that of 2006, where the market rose, only to fall in 2008 and ultimately bottoming up in 2009. What we have done is shifted our portfolio away from high value growth stocks to that of deep value and high dividend yields to protect our portfolio if the crisis comes sooner than expected.

Disclaimer

The views expressed in this report are those of Devan Linus Rajadurai, MTC's Co-Founder, CEO & 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.

Copyright © 2012-2018. All Rights Reserved.

invest@mtcasset.com
+60 3 2289 5055

MTC Asset Management
Meranti Fund

Commentary (Meranti Fund)

September 2018

Written by Devan Linus, Chief Investment Officer

Objective

This commentary should be read in conjunction with the MTC Founders Fund Commentary. MTC Meranti Fund (“Meranti”, “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 with an approximate 30% exposure to Malaysian listed entities. Its overseas exposure is close to an exact replica of our sister fund, MTC Founders Fund (“Founders”). Besides its continuous Malaysian exposure, Meranti’s investment approach is the same as the Founders Fund. Performance is reported in MYR.

Performance

MTC delivered a since inception net return of 30.3% (12.5% p.a.), outperforming the KLCI and underperforming the DJIA, which returned 7.3% (3.2% p.a.) and 48.5% (19.2% p.a.) respectively.

Benchmark Comparison

Meranti and Founders

In MYR terms, Meranti performed better than Founders. However, in USD terms we performed similarly with our YTD and Quarter performance declining at -12.2% and -1.9% respectively. Our YTD and Quarter decline was primarily due to the Global portion of the portfolio. The 33% Malaysian stocks allocation did not impact the portfolio for the year or quarter as the gains and declines of our Malaysian stocks netted each other out.

KLCI

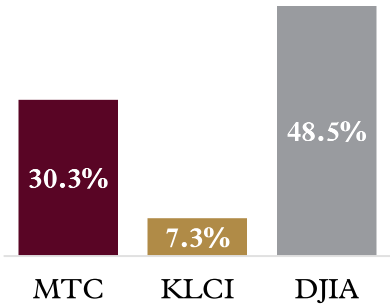
The KLCI performed 0% for 2018 up to September, but during these periods it was extremely volatile post May when Tun Mahathir won the election to be Malaysia’s new Prime Minister. On Jan 1, the KLCI appreciated 3.9% to May 1, then declining -9.0% to July 1, only to recover 6.0% to Sep 30. Our Malaysian stocks have unfortunately not recovered in line with the post-election rally, and the reasons for that is we owned a company in the tech hardware space prior to the elections and started buying into a media company that crashed due to the elections. We would also like to point out that since our inception, the KLCI has barely moved with a performance of only 7.3%. We are still pessimistic about the overall market due to the crowding out by fund managers and sovereign wealth funds investing in stocks that are low growth but highly valued.

NAV

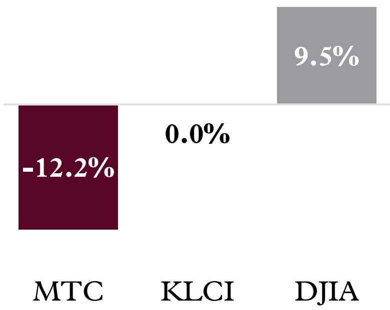
Class S: 130.32

Performance

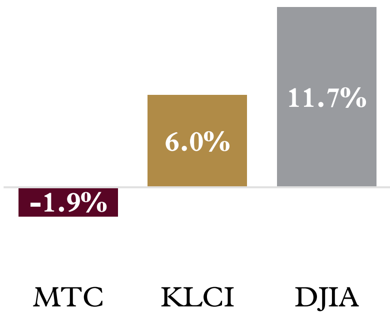
Since Inception (28 Jul 2016)



Year to Date (Sep 2018)



Quarter (Sep 2018)



Copyright © 2012-2018. All Rights Reserved.

Devan Linus, Chief Investment Officer

Portfolio

Our Malaysian companies in our portfolio are all in the deep value category; trading below net tangible book, and have historically been generating good profits and cash flows; and have paid good dividends. Unfortunately, the global economic headwinds have temporarily impacted our Malaysian Tech Hardware company, such that there is a temporary negative profit. It is important to take note that with the right business strategy and cost cutting initiatives, the company can turn back to a profit very soon, given the global demand for semiconductor and its supporting OEM parts. From that perspective, we don't necessarily see any better alternatives than our investable company, but if we do see other good blue chips companies dropping in value we may switch to those companies with a better outlook.

With our Media investment on the other hand, we are quite bullish. Similarly, to what we described in our commentary on Founders, there is a huge opportunity in the media sector. Malaysian media companies are unique in that we are a multi-national country with many dialects. For example, Netflix, they can't penetrate as well in the local scene as they are predominantly still an English content video provider. The same goes for news and radio, which naturally must be produced locally. Furthermore, there are many other hidden assets in media companies such as property, and non-core businesses that have value that can be instantaneously monetised. We are using this opportunity in the change of government to scoop up media companies in Malaysia at bargain prices. While there may be some political risks in that the major political parties own most of our media companies, a change of shareholding ownership and ultimately a change in management of the companies will result in huge long-term growth and potential. It will be ridiculous to assume that all newspapers or TV channels will shut down tomorrow.

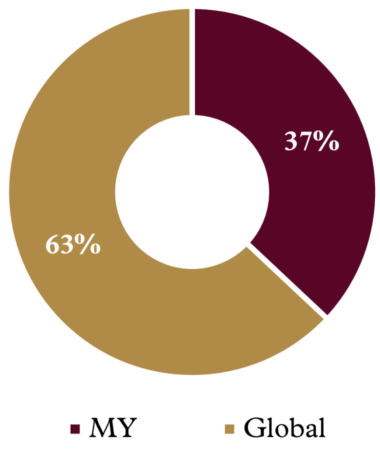
Outlook

Like Founders we don't expect Meranti to produce a good 2018 return. However, because of the Malaysian catalyst, there is a possibility for a quicker recovery if the market starts appreciating our stocks sooner.

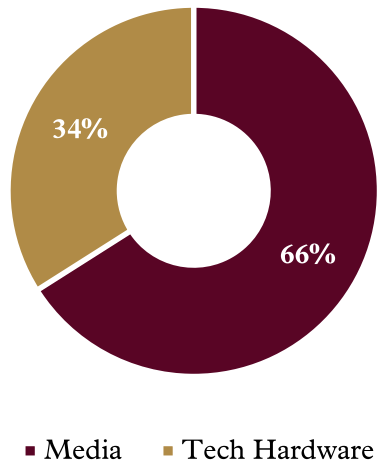
Disclaimer

The views expressed in this report are those of Devan Linus Rajadurai, MTC's Co-Founder, CEO & Chief Investment Officer. MTC's investment strategy is implemented by the Fund's Investment Manager, MTC Asset Management (M) Sdn. Bhd. licensed by Securities Commission Malaysia (CMSL: eCMSL/A0333/2015). The Fund is a regulated wholesale fund under the Capital Markets and Services Act 2007 (CMSA) of Malaysia.

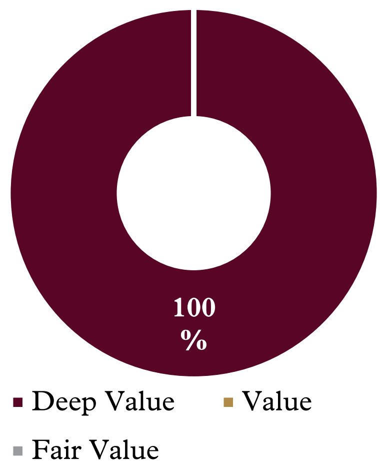
Listing Breakdown



MY Sector Breakdown



MY Value Breakdown



Copyright © 2012-2018. All Rights Reserved. mtcasset.com