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MTC Asset Management
Founders Fund

Commentary (Founders Fund)

March 2019

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 large cap 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 70.7% (8.2% p.a.), outperforming the KLCI but underperforming the DJIA, which returned -21.6% (-3.5% p.a.) and 105.5% (11.3% p.a.) respectively.

Benchmark Comparison

Quarter

As we mentioned in our commentary last quarter, we expected a recovery for MTC of >30% from our December 2018 lows, delivering a 39% return for the quarter. We are now close to recovering our entire yearly loss in performance for 2018. Whilst the DJIA also performed well for the quarter due to the change in market sentiment, we outperformed the DJIA by 27.8%. The main reason for our outperformance was due to our portfolio consisting of 81% of Deep Value stocks in Dec 2018 that have appreciated significantly over their all-time lows (Mar 2018: 81% as well, reflecting our discipline of holding our stocks through market swings). In addition to that, our increased leverage last quarter also magnified our returns in the current quarter.

It should also be noted that we did not change the composition of the portfolio at all this year, except for the trimming of our Malaysian semiconductor supplies manufacturing company that we indicated was an investment mistake in our previous commentary (even this company appreciated in 2019).

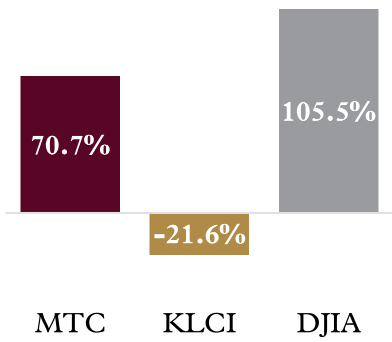
The KLCI on the other hand performed negatively for the quarter at -1.6%, due to the continued lack of confidence among investors and the public in general. This re-affirms our strategy of investing globally and in developed markets.

NAV

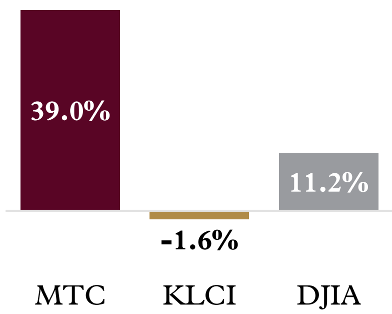
Class S: 170.66

Performance

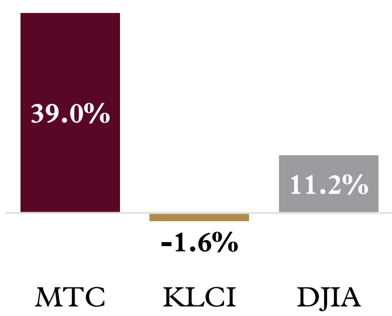
Since Inception (24 Jul 2012)



Year to Date (Mar 2019)



Quarter (Mar 2019)



Portfolio

Buy and Let It Grow

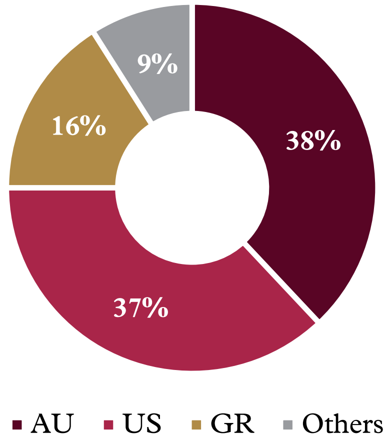
Continuing from our learnings from managing the portfolio over the last 6½ years, more often than not the best strategy to implement once you have already bought great companies if to give them time to grow. As such, we have not altered the composition of the portfolio and have not sold any of our investments, besides the Malaysian investment mentioned above. We continue to be bullish on the prospects of our investments in media, tech hardware and retailing, and still consider these companies to be Deep Value. Despite the stock price increases, these companies still average a dividend yield of >5%. Further, from a business perspective structurally, there are no changes in strategy or industry.

In fact, for some of our companies, we are seeing the emergence of increasingly positive indicators of growth in their business. In particular, the German automakers are experiencing positive reviews, with increased order take-up of their newly introduced pure electric vehicles in addition to their existing combustible engine vehicles. Examples of these new vehicles are the newly introduced BMW 3 Series, Mercedes EQC, and Audi E-Tron. On the other hand, the pure electric and overvalued darling, Tesla, had a 31% decline in deliveries in Q1 2019 to just 63,000 vehicles, which is still only 10% of the deliveries that Mercedes and BMW do on average on a quarterly basis (i.e. 600,000 vehicles), despite having similar market cap figures. For comparison purposes, Tesla, Daimler (Mercedes), and BMW market caps at the end of Dec 2018 was $57, €49 and €46 billion respectively. Currently, for Mar 2019, the respective market caps are $46, €62 and €50 billion, a decline of -19% for Tesla and an appreciation of 27% and 9% for Daimler and BMW respectively.

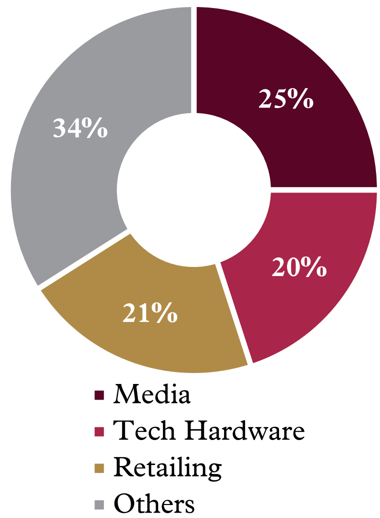
In the media space we continue to see the shift from traditional advertising to online media, with new unique methods of delivering advertisements that have better reach and targeting than before. Examples are short videos ads on your mobile phone's social media or video app accounts that are targeted based on what you normally watch, read, etc. In growing markets like India and Indonesia, the mobile phone today has much higher penetration than traditional television and even newspapers. Also, the innovative media companies are adopting the right use of Artificial Intelligence to remove fake content, tracking user engagement and optimising content delivery, among other things.

For our tech hardware and retailing companies, there are no significant changes in the current quarter worth elaborating about. As mentioned in the header above, sometimes the best thing to do when you invest in a company is just sit back and let it grow.

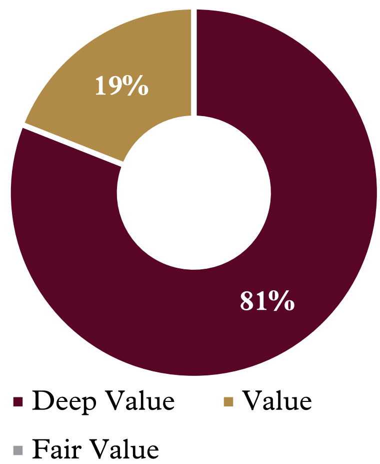
Company Listing Breakdown



Sector Breakdown



Value Breakdown



Market Insights

Tech IPOs

After a strong start to the year for markets globally, it has become an expectation that the rest of the year is to be a year of continued growth for the markets, supporting the upcoming IPOs of the last group of celebrated tech unicorns. Among the notable ones are Uber, Palantir, Pinterest, Slack, WeWork, Airbnb, in addition to the recently listed Lyft. All the companies above are listing without having produced any profit and in the case of a few, their losses are equivalent to the revenue they generate! For example, WeWork, which had revenue of $1.8 billion in 2018, had losses of $2.0 billion. We find this whole euphoria to be a bit of a concern, because when the last two tech behemoths, Google and Facebook listed, they had for the years prior, profits that were growing. Furthermore, they were creating a new innovative form of service or product that never existed in the brick and mortar form before.

If we look at two of the unicorns above, WeWork is a property leasing company and Uber is essentially a taxi booking service. I don't think when people invest in real estate, they charge a rental that is half the price of their cost, so why should the same treatment apply for WeWork, whose only differentiator to other service office companies such as Regus (which has been operating since 1989 and is listed), is that they use the buzzword "coworking space" instead of "service office" or "business centres". Uber on the other hand has a lot of users (which is why investors are head over heels for it), but those users are acquired based on the fact that Uber uses the capital it raised to subsidize the difference between what the customers pay and what the drivers collect. If Uber was to follow standard market economics and charge the passengers a mark-up of what they pay drivers plus overheads, the majority of passengers would just drop Uber and take public transport instead, given the high cost of private car rides. How about Uber Eats? Customers will likely opt to cook themselves or walk down the road to buy a sandwich (important to also note that lifestyle trends are moving towards healthy living, so walking is exercise). As for Uber Parcel Delivery, customers will just revert to DHL or Fedex that provide cheaper services, insurance, and doesn't have a random (untrained) stranger picking up your confidential documents.

Now, are these two businesses great and innovative, and therefore worth something? The answer is Yes, but not the expected $100 billion valuation for Uber or the expected $45 billion valuation for WeWork. In contrast, profit making Japan East Railway has a market cap of around $35 billion despite being one of the largest railway companies in the world with 6 billion passengers a year, compared to Uber that has a very moderate 100 million monthly active users. Hyatt, with an $8 billion market cap, has more than 700 hotel locations worldwide compared to just 560 WeWork office locations. Tell me something doesn't seem right!

All in all, our view is that these unicorns (and fortunately for its founders), will likely be able to list with the valuations expected above, as the market seems to be enamoured more with the story than the fundamentals, and most importantly the long-term viability of these business models. If we wind back the clock to 1999, remember that many internet companies were heralded to be the new kings of the universe, only to crash by >75% from their peak, and most ultimately to bankruptcy. The most notable being pets.com and etoys.com; these were the darling companies of the '90s that were supposed to sell their products globally and online, which ultimately went bust and lost many investors money, subsequently causing a Nasdaq stock market decline that lasted three years up to 2003. The difference between 1999 and 2019 is that pets.com at its peak had a valuation of $300 million; Uber for its listing is asking for $100 billion! You can imagine the impact if it is proven that unicorns really do not exist.

As a final point, Lyft on its first day of listing on 29 Mar 2019, closed at a share price of $78.29. As at 15 April 2019, its share price is $56.11, a -28% return in less than a month. I think you get the picture of why we are no longer heavily invested in technology stocks.

Outlook

Despite our negative outlook on the unicorns, we believe that our stocks will be shielded if there is any crash in the markets as they are operating in completely different industries. For our tech hardware companies, their revenue and earnings are not expected to be affected as much even if the unicorns were to crash. The difference between certain tech hardware companies of today versus before is that their customers are not only other tech companies but many traditional brick and mortar players, such as home appliances, automobiles, retailers, and logistics, that provide good customer and revenue diversification should the tech unicorns order less.

Having said that, and despite us buying our Deep Value companies and letting them grow, we are adopting a strategy of prudence and are already beginning to trim some of our stocks to de-leverage the portfolio. This might benefit the investors that came in early last year less, as there will be less magnification for appreciation in the short term but will protect our portfolio if a downturn is to occur. We do not think the downturn will happen this year, as the market players and the people in control will do their best to maintain market prices at their current levels in order to list these unicorns, but once the notable unicorns are listed, the risk of a downturn or crash would be much greater.

When that crash does happen and it pushes other great companies into cheap valuation territory, we intend to swoop in and buy some gems, adding a few growth companies to our current high dividend yielding and steady companies, as we have liquidity ready to take advantage of such an environment.

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.

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MTC Asset Management
Meranti Fund

Commentary (Meranti Fund)

March 2019

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 23.2% (7.9% p.a.), outperforming the KLCI but underperforming the DJIA, which returned -1.6% (-0.6% p.a.) and 43.5% (14.1% p.a.) respectively.

Benchmark Comparison

Meranti and Founders

In MYR terms and for the quarter, Meranti performed positively at 40%, similar to Founders where the currency impact was minimal for the year. Meranti continues to have a 32% allocation to Malaysia, with a 1st quarter performance of our Malaysian investments that appreciated similarly to our global investments.

KLCI

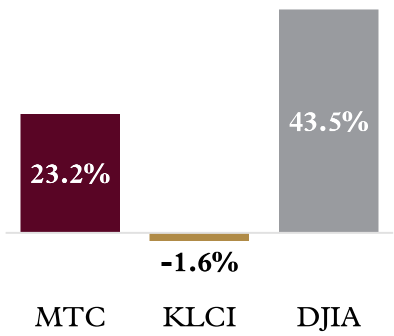
On the other hand, despite the rise in the DJIA at 9.8% in MYR terms, KLCI performed at -2.8% because of the continued negative sentiment among investors and the general public. We commend the current government for attempting to clean up corruption, increase governance, and clawback money for the country as those strategies have generally succeeded for advancing Developing Countries. However, we do recognise that things will take a while, which is probably why the KLCI is not performing. I would give the KLCI time because its current price levels are at five-year lows, and only upside should be expected going forward. Although we disagree with some of the initiatives the incumbent government is proposing, such as reviving old industries such as car manufacturing or airline parts manufacturing that Malaysia has no comparative advantage in, we are optimistic that with the right policies, new entrepreneurs can emerge and grow the economy. Having said that, it is still very tricky to pick sound long term value investments from the crop that is listed on the Bursa.

NAV

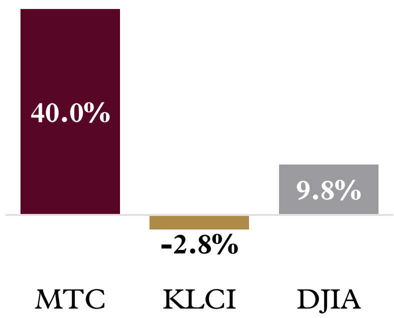
Class S:	123.20

Performance

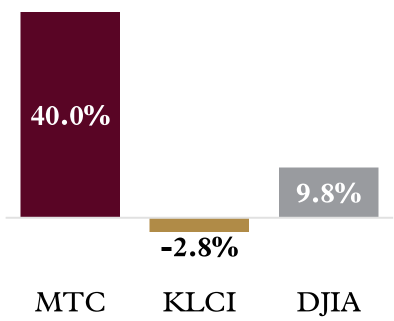
Since Inception (28 Jul 2016)



Year to Date (Mar 2019)



Quarter (Mar 2019)



Portfolio

There has been no selling or buying of shares compared to our last quarter, December 2018, except for the trimming of the company in the tech hardware space that we mentioned in our Founders commentary.

Compared to our previous quarter's sector breakdown, our investment in the media sector has appreciated less relative to our other holdings, hence the lower percentage of 50% compared to 68% in December. This has occurred despite us trimming down the tech hardware space and with no changes in the construction sector. Our Malaysia companies continue to consist of companies in the Deep Value space, however we may consider trimming our Value companies that approach Fair Value. We believe as the Malaysia market remains negative, further opportunities in other large caps will arise, be it in the glove, banking and/or agriculture sectors that we have invested in before.

Outlook

Our outlook is similar to Founders, where we expect the global portion to slowly appreciate but be at the risk of a decline after the tech unicorns list. We are also being patient with our Deep Value Malaysian companies that are already starting their turnaround plans with the support of the new government. In fact, we could be considered more bullish on the downside protection of the Malaysian stock market, in the sense that if the global markets correct, the Malaysian market is so low that it should not go down much further.

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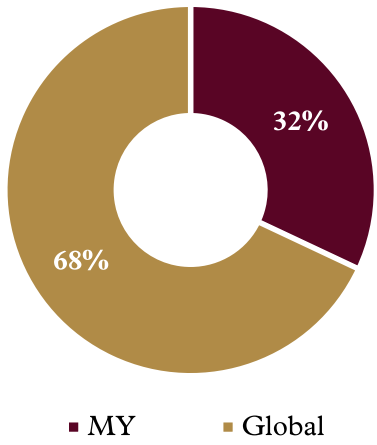
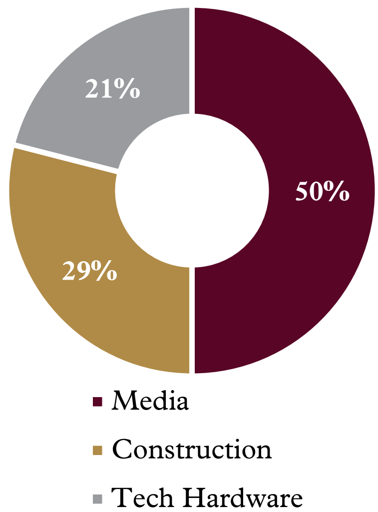
Listing Breakdown



MY Sector Breakdown



MY Value Breakdown