invest@mtcasset.com
+60 3 2289 5055

MTC Asset Management
Founders Fund

Commentary (Founders Fund)

March 2020

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 global companies. Performance is reported in USD.

Performance

MTC delivered a since inception net return of 41.2% (4.6% p.a.), outperforming the KLCI but underperforming the DJIA, which returned -39.1% (-6.2% p.a.) and 73.7% (7.4% p.a.) respectively.

Benchmark & Market Insights

Covid-19, MTC and the Market

Knowledge and news about the Covid-19 virus was widespread in early January, but majority of the people and governments thought it was exclusive to the East and only in March did we really experience the speed and magnitude of the spread. As such the response with lockdowns and the movement control orders, ultimately froze the economy and correspondingly the markets declined with the same speed and magnitude. We at MTC also did not predict the sheer impact of Covid-19, but we have continuously emphasized over the last two years on how we felt the markets were overvalued. In our December 2019 Commentary we had a section titled "No Crisis Observable in the Near Term but Overvalued", and in other sections of the commentary we also stated how we were "ending the year with ~25% cash".

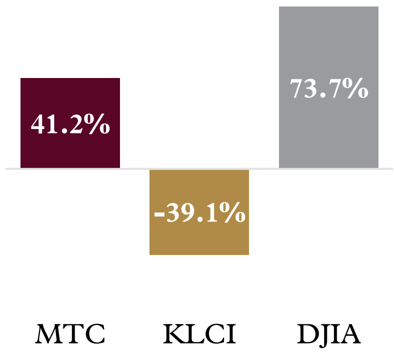
Ever since the end of February, most developed market indices and individual stocks have been declining at a rate of -10% a week to a bottom sometime between 20-23 Mar 2020.

NAV

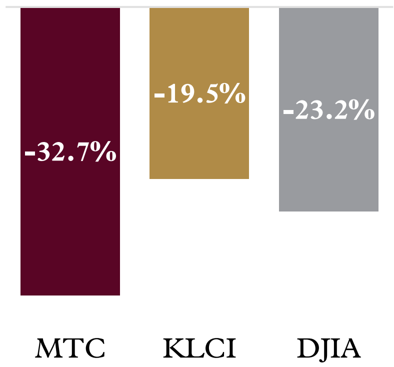
Class S:	141.20

Performance

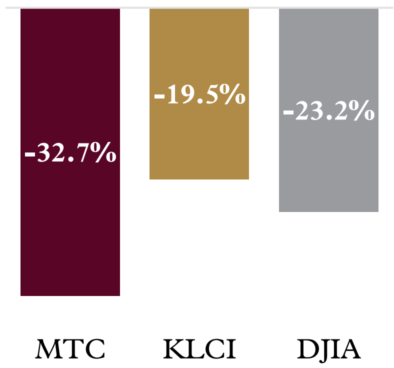
Since Inception (24 Jul 2012)



Year to Date (Mar 2020)



Quarter (Mar 2020)



Benchmark & Market Insights (continued)

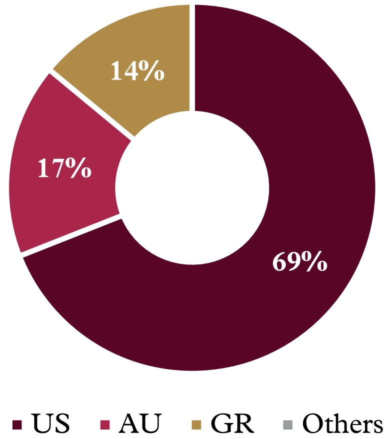
Covid-19, MTC and the Market (continued)

During this period we executed two strategies: (1) utilising our cash (and towards the end of the month with some leverage) to purchase the exact same stocks we have been commenting in our last few commentaries that are deep value or growth at a reasonable price: Media, Tech Hardware, Autos, Retail, etc., and (2) switched from companies that declined less (thereby less cheap) to companies that declined more (extremely cheap). We are very confident that this strategy will result in our next recovery being much larger (possibly even 100% in a span of two years compared to our March 2020 valuation of 141, hence NAV of ~282). This would be a bigger magnitude compared to our last recoveries from our lows in Mar 2016 to a high in Feb 2018, or our lows in Dec 2018 to a high in Jan 2019.

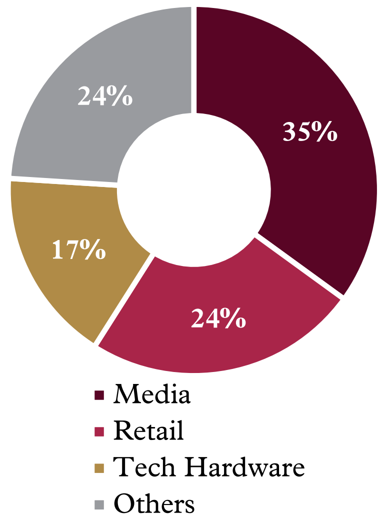
However, if you analyse our YTD performance, it does look quite pale in comparison to our two benchmarks the DJIA and KLCI. The main reason for the underperformance, is honestly in a time of crisis all theories of diversification goes out the door and it is more of the luck of portfolio entering the crisis that determines your return. Hence, if you were diversified entering the last Global Financial Crisis, but your diversification had a strong component of banking stocks, your portfolio would have sunk more than 40% in a year as banking stocks on average declined 80%, and the non-banks also crashed ~20%. The question is which banking stock did you invest in, and if it was JP Morgan or banks in the East of the world you would have recovered quicker.

And in this Covid-19 crisis whoever was in the sector of Travel & Leisure, Retail or Food & Beverages (which for all purposes has always been known to be a reasonable defensive sector) would have been hammered severely. So our 32.7% decline, can be attributed to half being invested heavily in autos and retail, and the other half was our deliberate act of buying at every week of March, which some bears or pessimist would call "catching a falling knife". We would like to emphasize that we would rather catch a falling knife, because if we never took the risk of letting our hands bleed, you would never have accumulated all these knives for cheap to later sell it when the prices are great again. What you don't want, is to have the knife stab your heart, which we are not going to experience because all of our companies are either net cash or have minimal debt and liquidity that can last for years. Entering this crisis, we were not in the Travel & Leisure sector, be it airlines, cruises or hotels, which if highly indebted, the risk of bankruptcy would be very probable (there are significant bargains now in this sector… so the research is extremely important to pick a company that is least likely to go bankrupt).

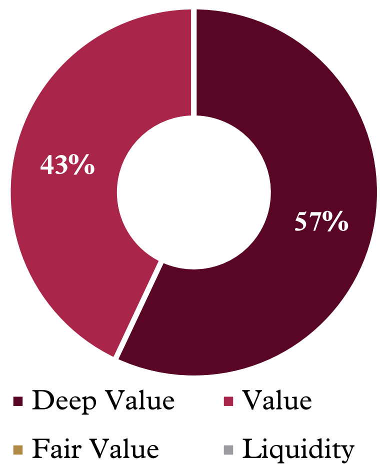
Company Listing Breakdown



Sector Breakdown



Value Breakdown



Benchmark & Market Insights (continued)

Covid-19, MTC and the Market (continued)

The next question then turns to the DJIA, and the reason why the DJIA did not seem to have crashed as much, at only -23.2%. The DJIA consist of 30 blue chips that generally represents the US stock market, where stocks in Travel & Leisure was limited to just 1, being Boeing, and 3 in Retailing where 2 out of the 3 were Walgreens in pharmaceuticals and Walmart in groceries, that today is deemed essential and are still generating revenue by selling to customers. So, in the short term the DJIA did not decline as much. Problems may be worse for other component stocks in the future if the lockdown persists, and the market would then either decline more (but at a much less steep rate) or may just hover at current prices for a while. We do believe and that MTC's portfolio or a well-managed active portfolio - by buying and selling, switching, shorting, etc., will perform better in the recovery (but we must distinguish between 'well-managed active' vs 'passive' portfolios). The act of switching, shorting, buying and selling if done well creates the extra return especially during a crisis when things are cheap as volatility creates opportunity.

Also our charts compare, 31 Dec 2019 to 31 Mar 2020 for the DJIA which is a -23.2% decline, however if you would to examine the peak on 12 Feb 2020 at 29,551, it fell to 18,591 on 23 Mar 2020, which is -37% fall. It might be hard to comprehend the fear by any investment professionals or even regular investors during this period. We were certainly fearful for sure but we decided to be hungry for gains, and at -37% fall this hunger is warranted. Correspondingly, at the end of March the DJIA recovered, and possibly at the day of the release of this letter the DJIA would have entered a new bull run. We created financial history in March 2020, both being one of the steepest declines of the DJIA in one month, and also the fastest recovery. It doesn't mean we won't enter a bear run again but buying in March would be a good move as we are investing when things are of value, and our time horizon is not measured by days, weeks or months but years.

The KLCI, our other benchmark declined less, but that is only because in the last 8 years since July 2012 to December 2019 it lost money (-24.4%), and the same can be said for many other emerging markets. Singapore Straits Times index for the same period only appreciated, 0.8% whereas MTC and DJIA did 109.8% and 126.2% respectively.

Portfolio

Technology & Bricks and Mortar

Our portfolio can be broken down to two major segments being Technology and Bricks-and-Mortar. Year-to-Date our Technology stocks have generally declined much less around ~25%, whereas our stocks in Bricks-and-Mortar decline more than -50%. The reasoning is logical, Technology stocks like Google, Microsoft, Facebook, etc. benefit from the continuous subscription model to their services, and the increase in activity as most people are consuming online media while staying home. As such these companies are still generating revenue (advertising may be less, but it's still there), but more importantly these companies have substantial amounts of cash on their balance sheet, so there is no market panic that these companies would go bankrupt, hence a lessened decline in its share price.

For our Bricks-and-Mortar stocks however, due to the act of the lockdown these companies are generating close to zero revenue especially if they don't have an online presence. This is probably the first time since the world war where you have a lockdown for a sustained duration of potentially months.

How we are playing this (and how we have already been playing this) is to pick the Bricks-and-Mortar player that:

Portfolio (continued)

Technology & Bricks and Mortar (continued)

(1) Has No Debt or Minimal Debt

Our companies in the Bricks-and-Mortar space, either has no debt, or if it does have some debt, has substantial amount of liquidity, be it cash or standing agreements from their lenders to draw down more capital. To understand the second point, a lot of companies in the latter half of the last decade deliberately took debt given that interest rates were close to 0%, despite the fact that they didn't need the cash. If the companies return on equity or capital was significantly more than the interest rates or their cost of capital it made absolute sense to do so, as long as they still took debt with enough buffer even if there was a crisis. Illustratively, to emphasis the point, let's say a company has a market cap of $60 billion (pre-Covid-19), and they took $20 billion worth of debt. Assume that only $10 billion was used and the remaining $10 billion was left in cash for a rainy day. Also assume the same company also locked in agreements that allowed them to draw more debt by a further $10 billion for the next five years. Hence, now Post-Covid-19 if the company took this new debt, they would have increased their total debt to $30 billion, but in reality have $20 billion of cash. Assuming the stock price declined 50% its market cap would have halved to $30 billion, an investor with little research work done would assume that the company was going to go bankrupt given the debt is 100% of its market cap, and correspondingly panic, further sending its stock price even lower and perhaps resulting in the company crashing 70% of its Feb 2020 peak (giving us MTC an opportunity to buy more). Why did we buy more? If the company needs $10 billion a year to sustain its operations that means it can actually last for two years, so it is pretty good bargain if we feel the impact of Covid-19 would be less than two years. So, this is an example of Autos, where a lot of people think the company is highly indebted, but in reality some of the auto companies, and the ones we invested in, have a lot of liquidity. Contrast that with US Airline companies or Boeing, they probably only have cash that can last a few months, and without a government bailout they will go under. If you did your homework, there are probably some airlines that were lucky, in that they did a sale and leaseback of their planes perhaps a year or two ago and just timing wise happened to have cash entering this crisis.

(2) Has An Aspirational Brand Value

It would be a surface level or very general comment to say that every Bricks-and-Mortar store has brand value because it is visible, such as the store, the signboard, the marketing etc. However, there are companies that have a stronger brand that is ingrained in our minds, and others that are less ingrained. So let's give another example, during this lockdown as you think what food to order if you're sick of cooking every day, the first thing that might come to mind is "McDonalds" or "KFC" because it has strong Brand Value, and unlikely "Manhattan Fish Markets" would come to your mind as the brand value is less. Now what is "Aspirational Brand Value", that is a brand that when things recover it is a product or service that people aspire to obtain to keep themselves motivated to be great again. Something to aspire to, maybe it's that travel tour to climb Mount Everest before the next pandemic comes again, or buying that Rolex that you actually wanted to buy this year, or maybe even during the current lockdown to save money by cooking at home just to buy that iPhone that you previously kept on saying was too expensive. This is why luxury goods at times have been called defensive sectors, but that theory doesn't just apply to luxury goods, it could be for mass market goods or services that have "Aspirational Brand Value". Call it anything you want whether its high-end or aspirational brand retail therapy that society always look to, revenue will be less but not zero, and when things recover revenue will be the same if not growing more.

Portfolio (continued)

Technology & Bricks and Mortar (continued)

(3) Large Companies and Too Big to Fail

We have always stuck to large cap companies in our investment philosophy, so that during times of crisis we get the additional protection from government, bank, credit holder and shareholder bailouts. Any of the four parties mentioned above dot not want to see their company go bankrupt, as they will be booking in a loss, or the contagion effect may be worse, such as loss of jobs, trickle down effects to other sectors, social upheaval, etc. Let's assume a credit holder (another illustrative example), had loans amounting to $50 million to five small companies ($10 million a company), and one large company that it loaned $50 million to. Assuming each company regardless small or large needed $5 million to survive and the credit holder only had $10 million cash available right now to give out, who do you save? If they saved two small companies, in the end they will only have the $20 million repaid and also have sacrificed $80 million of the other loans, assuming the rest went under. On the other hand if it saved just that one large company (giving it $5 million first, and saving the other $5 million if they were to ask again a few months from now) it would have the ability to have $50 million repaid at the expense of the five other companies going under, sacrificing only $50 million. Although this is a simplistic assumption as there are many other variables, the overall conclusion is a company that is too big to fail will always get saved first. We observed this in the global financial crisis, where the US government created a bailout plan to save the banks, and we saw this again in March where the US government created a bailout plan to save US companies with a large portion for the Airlines, Boeing and other Travel & Leisure companies. However, bailouts don't just come from the government, they also come from the other three parties mentioned before. Therefore, the analysis that needs to be conducted, is an understanding on which company is likely to get a bailout. Points (1) and (2) above are one of the factors, being a large cap is another, but there are many more other factors that are used in evaluating which company is deemed too big to fail. The analysis becomes more difficult, in that the four parties above, especially the government do not want to create a 'moral hazard' by encouraging genuinely terribly managed companies to be bailed out. That's why in the last global financial crisis they allowed Bear Stearns and Lehmann Brothers to fail. It's an extensive amount of work too dig into the details, but this is why hedge funds and a well-managed active portfolio can outperform coming out of a crisis when the analysis is done thoroughly.

We must not underestimate the extend of research required during this period, as a company that goes bankrupt in one's portfolio can be quite devastating, but at the same time being too conservative and having only mediocre companies that will only appreciate marginally 5% p.a. over the next decade would be deemed quite terrible as well as it would take a decade to recover the current losses during the crisis.

Our companies in Bricks-and-Mortar meets the three criteria above among many others, and our companies in the technology sector were already those that have the lowest valuations within the sector.

For more detailed explanation on our thesis of specific sectors and companies, have a re-read of all our commentaries from 2018 to 2019. Being true value investors (having sacrificed momentum returns the last two years), if we already deemed the companies to be undervalued with a continued strong growth thesis, it only makes sense to buy more and use up our cash if it is 50% cheaper. We look at the business and its price today, in comparison to what we think the price would be three-five years from now. If it goes down further by more, or if we reach our risk limit, just be comfortable we already bought it close to the bottom. For a more detailed explanation on the concept of value investing and the view of the markets during Covid-19, we encourage our investors and readers to read the memos of Howard Marks available on the Oaktree Capital website. Our thinking and views of the market are close to 100% of his and his firm, and rather than trying to write our views of the market he probably and maybe definitely can articulate the situation better than we can.

Outlook

As much as we enjoy giving an Outlook every quarter (investors and readers expect it), we have always put a caveat that forecast, predictions and outlooks when it comes the macro economy is generally a very hard thing to do and many times the professionals tend to get it wrong, including ourselves. What is more important is the understanding of the micro and the specific companies or investments, then acting accordingly by managing the portfolio. But as much as we target a 10-15% return, we don't know in the short term (1-12 months) whether we are going to get -30%, 5%, 10% or 60%. What we can comment is that you should look at things in terms of probability and degree of certainty and understand the philosophy of a particular investor or economist to why he or she chose to have a particular outlook. A pessimist would always have a negative outlook and an optimist would always have a positive outlook, regardless of the facts. We at MTC are definitely an optimist; (1) because of history, human civilisation has always advanced, only the dinosaurs declined, and if we did miss out on the absolute bottom and if after 5 years from today only made 10% instead of 20%, it's still growth and it's still better than fixed deposit or the Malaysia and Singapore index. On the other hand, if we were a pessimist and didn't make any moves during this period, we will perhaps lock in a 5% return going forward, which means on an arithmetic basis it will take 6 years to recover our losses as opposed to the previous optimistic scenario of only 3 years or on the worst case basis of 10% and 1.5 years on the expected case basis of 20%. (2) Strategic moves do make a difference, some could have be temporary pessimistic of the market and in this instance, would have shorted the market to make short term returns during these times (some hedge funds practice this), but because we are optimistic, we would buy more or switch, and sacrifice short terms returns for greater long term returns than we initially were likely to receive. So that's why we hope our investors and readers understand our philosophy and the philosophy of value investing to be more optimistic during these times, as the saying goes "when other people are fearful it is time to be greedy". We were greedy in March, we may be greedy again.

Now as for our actual outlook, we have mentioned to investors and readers that one should look more about the probability of a writer's outlook as opposed to just taking it as gospel. As investment professionals, many times when we do provide outlooks, we blurt out our views but fail to mention the probability of it actually happening. The reality however, if even if we were to put a number down, who is to tell really whether the outlook really has a 50%, 60%, or 90% chance of occurring. All we can say or do is try and give strong arguments to why we are optimistic, but more importantly how we are executing our strategy given our views? In MTC's case, we explained it in the sections above. Having said this, we will still try to give an outlook, and I guess the main question now is have we bottomed out??

There are strong arguments as to why 23 March 2020 could have been the bottom. A bear market is described as 20% drop of its peak, and the market created new history by reaching that number in a month, and not just 20% but 37%! If I am not mistaken the last time a comparable speedy decline of more than >20% was the Black Monday, 19 Oct 1987 or the start of the Great Depression, October 1929. During both times the world did not have interest rates at close to 0%, so nobody is really suffering a margin call overnight. Secondly, from the time of the mass spread of the virus to the announcement of the stimulus was at a record pace. The US really only started to get wind of the extend of Covid-19 in Feb but provided a quick effective bi-partisan stimulus by the third week of March. In the last Global Financial Crisis, Bear Stearns collapsed in late 2007 which was the start of the financial crisis and the bailout at the time known as the "TARP" only came out in Oct 2008, after Lehman collapsed in Sep 2008. So, there is a very high chance the speedy bailout and monetary easing (interest rates close to 0%), would help manage the situation. Some companies may go bust, but March 23 valuations were already factoring that in with many companies trading below net tangible book. Another point is perhaps the market hasn't reached the bottom, but maybe certain companies may have. As for our companies, we have doubled down as prices have gone way below what we would call bankruptcy prices.

Outlook (continued)

Therefore, based on the above our Outlook now again would be more optimistic in that our fund NAV would probably hover around the current valuation. If we are wrong, we might suffer a further short-term decline in returns for the quarter, but if our investors and readers believe in our philosophy, the probability of it recovering at a larger magnitude than before will be extremely high. We believe we are better positioned to get to a NAV of 300 in the next few years by the moves we made in March then if we had done nothing and just held the same 25% cash. Of course if we never deployed the cash but deployed everything at 23 Mar 2020 we would had done better, but then again who knew Covid-19 was going to happen at this extent and who knew the exact bottom was 23 Mar 2020 if not a date in the later part of the year. All we know is to make moves and reposition our portfolio to have better asymmetric payoff on the upside. Perhaps, we may experience a further 20% short-term decline if we are not at the bottom but an extra 50% in overall returns after three years compared to our initial expectation in Dec 2019, if we can wait. We can most certainly wait; we do hope our investors can as well.

Disclaimer

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+60 3 2289 5055

MTC Asset Management
Meranti Fund

Commentary (Meranti Fund)

March 2020

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

Meranti delivered a since inception net return of -13.2% (-3.7% p.a.), underperforming Founders but outperforming the KLCI, which returned 8.4% (2.2% p.a.) and -19.24% (-5.5% p.a.) respectively.

Benchmark Comparison

Meranti and Founders

In MYR terms, Meranti performed negatively at -39.6% (-42.8% in USD) YTD, worse than Founders which returned -28.9% (-32.7% in USD). The reason for the underperformance is that in trying to get close to the 30% target exposure to Malaysia we were fully invested in terms of our Malaysian allocation adding the retail sector to our portfolio prior to this Covid-19 situation unfolding. Unfortunately, in Malaysia the market dynamic is such where the risk-reward trade-offs are out of whack, where a stock that otherwise would be deemed conservative with an expected return of just 6-10% p.a., during times of crisis or lack of sentiment can still crash >50%. Malaysia continues to be a speculative market, and the added effect of the government coup, where parliament members shifted parties overnight thereby changing the Prime Minister and government, exacerbated the decline of our Malaysian stocks.

KLCI

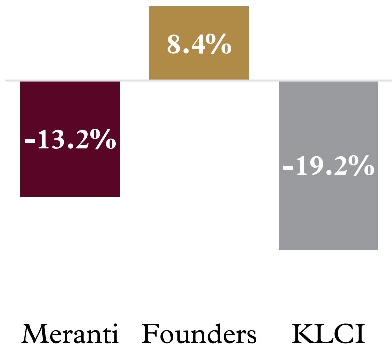
As mentioned in the Founders commentary, sometimes an index/benchmark comparison may not be a true representation of underperformance/overperformance during the short term or times of crisis. KLCI declined less as the components of KLCI were mainly financials and other industries that did not decline as much. Air Asia and REITs for example which are affected are not part of the KLCI calculation. We also need to remember that KLCI has not performed since inception 2016, and economic

NAV

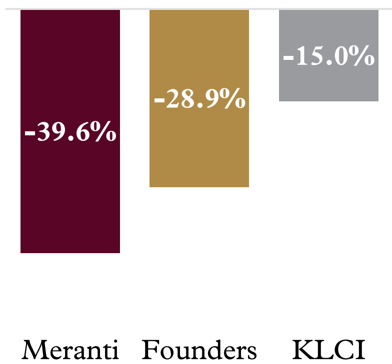
Class S:	86.83

Performance

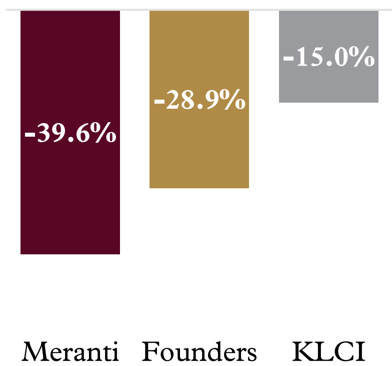
Since Inception (28 Jul 2016)



Year to Date (Mar 2020)



Quarter (Mar 2020)



prospects continue to remain dim. As such our Malaysian stocks have fallen more than our global counterparts, leaving us with only 19% of the portfolio invested in Malaysia (at times of short-term declines we are able to ignore the soft mandate of 30%).

Portfolio

However, despite the losses, we did take opportunity in Meranti to switch out substantially from financials into the Travel & Leisure sector. Similar to the criteria's in Founders, (1) No Debt or Minimal Debt, (2) Has an Aspirational Brand Value, and (3) Large Companies and Too Big to Fail, we have applied this to our investments in Travel & Leisure. Catching the falling knife as prices declined, also added to our losses for the quarter. However, if our thesis proves correct the expected return from our Travel & Leisure could be >250% in the next two years from its current price as of 31 Mar 2020. These are asymmetric risk-return trade-offs you want to make, if it does go bankrupt which is highly unlikely we would lose perhaps 50% of this sectors value (the companies do have assets they can sell in liquidation), but the upside is 250%. As for our allocation to Retail we were unfortunately caught with the lockdown, and all we have to do is be patient. They have a strong brand, and are trading at Price-Earnings valuation <10, at times it has reached ~6 depending on the day. We must not forget specific stocks in Malaysia are more volatile than the rest of the world, so the downside may be unwarranted. Lastly, we have gotten out of Media in Malaysia believing that the new sector combination provides a better risk return payoff going forward.

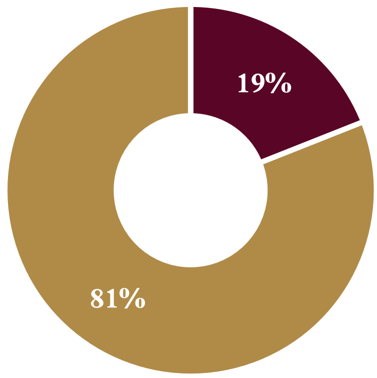
Outlook

Just because Meranti crashed more than Founders, doesn't necessarily mean it will appreciate more, but rather the Malaysian allocation would either result in luck of outperformance or the reason for underperformance. As we mentioned in our last commentary, our global outlook for Malaysia is negative, and as such with a base NAV at 31 Dec 2019, we expected Founders to produce ~8-12% p.a. returns, and Meranti's Malaysian allocation only ~6-10%. In conclusion, we expected Meranti to perform not as well compared to Founders. However, this outlook was when Meranti was at a NAV of 143 and now our NAV is substantially lower at 86, so you are expected make way more from this point if you re-invest during the upcoming months around this discounted NAV. Who knows when the bottom is, all we know now is that our portfolio companies are extremely cheap, and so is our NAV.

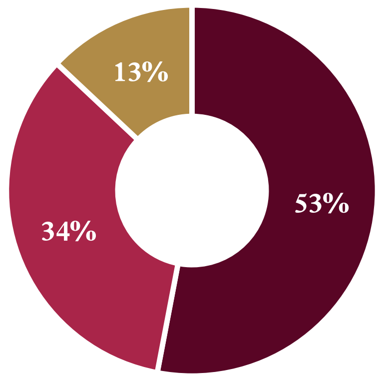
Disclaimer

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.

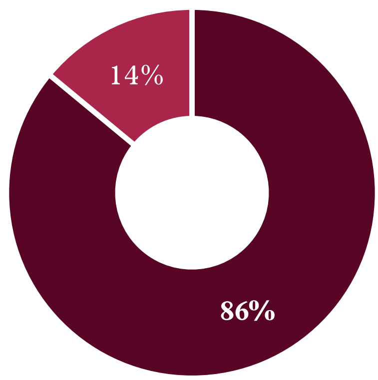
Listing Breakdown



MY Sector Breakdown



MY Value Breakdown



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