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Commentary (Founders Fund)

December 2023

Written by Devan Linus, Chief Investment Officer

Objective

MTC Founders Fund ("Founders", "MTC" or the "Fund") aims to achieve a net return of 8-12% 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 other developed countries and employs a value driven, bottom-up investment approach. MTC's benchmark is the Straits Times Index ("STI") and the MSCI All Country World Index ("MSCI ACWI"). The STI was chosen as a benchmark as MTC's investors are predominantly from Southeast Asia and benchmark themselves to Singapore. MSCI ACWI is the second benchmark as it was designed to best represent broad global equity-market performance. Performance is reported in USD.

Performance

MTC delivered a since inception net return of 132.2% (7.6% p.a.), outperforming the STI but slightly underperforming the MSCI ACWI, which returned 3.3% (0.3% p.a.) and 139.4% (7.9% p.a.) respectively.

Benchmark Comparison

Founders, STI & MSCI ACWI

STI and MSCI ACWI managed to reverse its Q3 2023 negative performance, where specifically the MSCI ACWI returned double digit for the Q4 quarter at 10.7%. MTC, on the other hand, continued its strong performance, delivering a return of 22.0% for the quarter. Our success this year can be attributed to two key factors: (1) effective stock picking, and (2) the discipline to hold onto our stocks, even in the face of their underperformance last year.

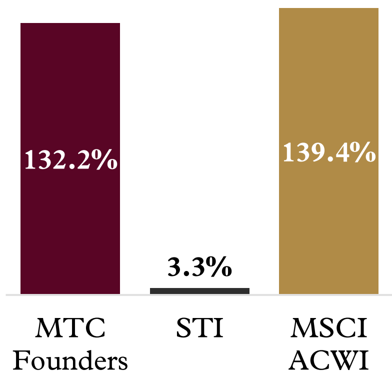
Throughout our years of investing, we consistently emphasize our belief that predicting the future trajectory of general market trends, country-specific indices, and even individual stocks or sectors is highly challenging. This sentiment applies not only to the beginning of this year when many market participants and economists anticipated a challenging period due to interest rate increases and recession concerns, but it also extends to various points in the past. As of December 2023, a review of financial articles and the year-to-date performance of the MSCI ACWI and S&P500, which stands at approximately 20%, reinforces the notion that attempting to predict the market remains a challenging task. As we approach 2024, we reiterate our position that attempting to predict market movements is very unpredictable.

NAV

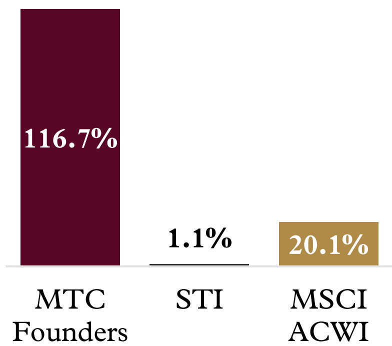
Class S:	232.15

Performance

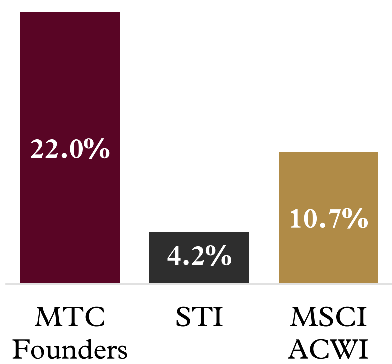
Since Inception (24 Jul 2012)



Year to Date (Dec 2023)



Quarter (Dec 2023)



Benchmark Comparison (contineud)

Founders, STI & MSCI ACWI (continued)

The above doesn't breakdown the specifics. To answer why the global market (MSCI ACWI) recovered by 20% and why our portfolio did even better at 116%, we will explain further. In the short term, the market price of stocks may not always reflect their true value. Take Meta/Facebook, for example; it was undervalued at the end of 2022. The market recovery in 2023 is essentially the realization by investors that many stocks were undervalued, prompting them to buy these stocks at higher prices. Another factor is the emergence of new investment themes, such as Artificial Intelligence (AI). While some AI stocks like Nvidia may be debatable in terms of valuation, many other AI stocks were already considered overvalued in 2022 and became even more speculative in 2023. So, the combination of genuinely undervalued companies appreciating and overvalued stocks going up (overcoming poor sector performance such as Pharma) contributed to the market's 20% return in 2023.

How did we make a 116% return? It might seem contradictory since we believe no one can predict the future, but it's not magic—it's a well-supported strategy. Many experts often get it wrong when predicting the overall stock market's direction. Why? Because it's too vast, involving many sectors and countries. We don't follow this top-down approach. Instead, like successful investors Warren Buffett and Charlie Munger, we believe in bottom-up investing. Imagine the market is like a huge puzzle with many pieces (sectors and countries). Trying to predict the entire puzzle is tough. Instead, we focus on individual puzzle pieces, doing thorough research on each. This approach, known as bottom-up investing, relies on being an intelligent investor, hence the name of the book by Ben Graham. Hence, an intelligent investor during a market upturn should be able to outperform the general market, and during a downturn, hopefully perform less poorly than the market. In the event they perform the same or worse, they should, in subsequent years, be able to recover back to outperform the market in the long term.

Unfortunately, we did not fare better than the market during the downturn in 2022; instead, we underperformed. However, what we did achieve was a recovery to outperform the market in 2023, maintaining a continued trajectory of long-term outperformance. Currently, we are 7.2% away from surpassing the MSCI ACWI again. For a more detailed explanation of our outperformance in 2023, please refer to the portfolio section of this commentary.

Portfolio

Outperformance

Our stock outperformance observed in 2023 is a direct result of our strategic move to double down on securities we identified as significantly undervalued during the 2022 downturn. Although we don't strictly adhere to thematic investing, for the sake of clarity for our investors, we can categorize the undervalued securities of 2022 into the following groups: (1) Internet Services, (2) Movie & Entertainment, (3) Semiconductors, (4) China Tech, (5) Others. While we might have used different terms in the past, they essentially refer to the same categories.

YTD Timeline of Performance

In Q1 2023, our performance was remarkable, boasting a 65% return primarily fuelled by the appreciation of two key stocks: Meta and another in the Movie & Entertainment sector. However, Q2 and Q3 saw more modest returns, with 4.1% and 3.7% respectively for the respective quarters.

Portfolio (continued)

YTD Timeline of Performance (continued)

While Meta sustained its upward trajectory, the other stock in Movie & Entertainment experienced a significant decline, approaching share prices reminiscent of 2022. Semiconductors began to appreciate, but this was counteracted by the decline in China Tech. In Q2 and Q3, as we started trimming our exposure to Meta, we concurrently decided to invest in other undervalued securities, particularly in the retail and autos sector. However, the performance of the "Others" category remained relatively subdued during this period. Q4 marked a positive turn for Semiconductors, with our selected securities appreciating over 70% YTD. Meta also continued its impressive performance, recording a 194% YTD appreciation. Our other Internet Services Stocks concluded the year with returns exceeding 50% YTD. On the flip side, selected stocks in Movie & Entertainment, China Tech, and Others remained stagnant, and deeply undervalued.

Geographic, Sector, Value and Leverage Breakdown

The more detailed breakdowns will be provided in the charts section, but the overarching summary reveals that in terms of geography and sector, there hasn't been a substantial change in December 2023 compared to the prior year or quarter. We have remained committed to the same stocks we held in December 2022, with minor additions in other areas as we trimmed our exposure to Meta. If we hadn't trimmed Meta, the chart on Communications might have been much higher than the current 51%. We also reduced some of our Semiconductor stocks, which fall under the Information Technology sector. What did change is our reduction of leverage. Although the reduction in leverage wasn't a result of us actively trimming it down, our dollar leverage remains the same. However, the denominator is much larger due to the more than doubling of the overall stock portfolio. The reason we haven't specifically reduced our leverage, despite the interest rate increases, is that 42% of our portfolio remains in deep value, including Movie & Entertainment, China Tech, and Others. Unlike Meta, which we now consider Fair Value, we still regard Semiconductors as Value, as there is more room for growth. While the share price recovery may have been fuelled by the explosion of AI use cases, the normalization of the supply chain in semiconductors for established purposes, such as the Internet of Things, personal computers, and other automations, is just starting to recover.

Market Insights & Outlook

Opening on Insights

Based on what we mentioned above, the key takeaway is that our market insight remains consistent: predicting the general market's direction in 2024 is uncertain. Bulls may highlight reasons for continued market appreciation, such as momentum from 2023, contained inflation, and China's recovery. On the flip side, bears may point to delayed recession impact, geopolitical tensions such as the wars affecting the market, and a potential correction for high-performing stocks (FAANG/Magnificent 7). Our stance is not to predict the market but to emphasize the importance of saving and investing. Despite uncertainties, a decision on investment must be made, aiming for either a less adverse outcome for bears or above-average returns for bulls.

In our view, it's imperative to (1) abandon attempts at predicting the unpredictable shifts of the general market. Instead, adopt a strategy centred on comprehensive sectoral or country trends. (2) Channel efforts into selecting individual securities that not only align with but outperform the broader trends identified. (3) Embrace a patient, long-term mindset spanning 3 to 5 years, acknowledging the inherent volatility of markets. Even if certain securities experience temporary setbacks, those of high quality tend to recover over time. Lastly, (4) advocate for minimal trading, particularly if time constraints hinder the ability to function as the 'intelligent investor.' This approach mitigates the risk of incurring unnecessary losses and positions investors for enduring success in a dynamic market landscape.

Market Insights & Outlook (continued)

Insight 1: Broad Views of Certain Sectors and Countries

The general insight provided is that artificial intelligence (AI) might be subject to hype similar to previous investment trends like 5G or autonomous driving. The comparison is drawn to the current use of 5G technology, where despite its presence, the practical applications in daily life are somewhat reminiscent of what was possible with 3G and 4G. The cautionary note emphasizes that not every technological development turns into a significant investment success, referencing the case of electric vehicles (EVs). For instance, while Tesla has thrived in the EV market, other companies like Nikola, Rivian, or Lordstown Motors faced challenges and setbacks. This example underscores the importance of discernment in navigating investment trends and selecting companies based on their growth potential and reasonable valuations. Our preference is expressed for investments in "growth at a reasonable price," exemplified by Meta, as opposed to solely chasing high-growth opportunities without considering valuation, as seen with Tesla and Nvidia, even though they have performed tremendously well.

In terms of countries, our view is that the United States stands out with the best probability of continued growth compared to any other nations. While BRIC nations (Brazil, Russia, India, and China) were promoted 15 years ago, the results have not lived up to expectations. Despite some renewed promotion for India and Japan in 2023, we believe their growth potential is less probable than that of the United States. Shifting focus to Southeast Asia, we recognize the dominance of US-listed global players like Sea Group and Alibaba in areas like e-commerce, making it challenging for local players like Grab and Goto, which are largely unprofitable. Regarding the general market in Southeast Asia, including Malaysia's KLCI and Singapore's STI, we are sceptical about their future prospects. Both indices returned close to 0% in the last decade, and we see no compelling argument for a return to double digits. Finance is a zero-sum game, and if one region is expected to outperform, it often comes at the expense of growth in another region. In the interconnected global landscape, our view is that Malaysia and Singapore are unlikely to "steal" growth from other countries, and while Singapore may offer stability akin to Switzerland, real investment gains historically stem from markets like China or the US rather than Switzerland.

Insight 2: Our Securities Groupings

Whilst we have views on many other sectors and companies, we are commenting only on the view of the securities we are investing in:

<u>Internet Services</u> – While our companies in this category are currently assessed as fair value in our opinion, the philosophy of holding onto great companies for the long term remains paramount. Consider the ownership of companies like Coca-Cola, Public Bank, or Microsoft from 30 years ago. Despite significant crashes in 1997 for Public Bank and in 2001 for Microsoft, if one had held onto both stocks since 1990, the compounding rate of return, including dividends, would have exceeded 10% per annum – a remarkable outcome. Unlike the tech startups' promotion of 5x or 10x returns, this example showcases a more than 17x return. We believe the companies we've selected in this category are poised to appreciate over the next decade, and we will diligently monitor their performance.

<u>Semiconductors</u> – We have already commented on this above and previously, although we must be mindful the 70% return would probably not be repeated in 2024. It might just average out to be a high single-digit or low double-digit return stock in the upcoming years.

Market Insights & Outlook (continued)

Insight 2: Our Securities Groupings

Movie & Entertainment – Despite Netflix, most stocks in this industry seem exceptionally undervalued. Careful stock selection is crucial to avoid falling into the value trap. While current industry dynamics, marked by an abundance of streaming services, have led to poor returns in the last two years, it's essential to consider long-term perspectives. Unlike financial analysts or business news that often focus on short-term trends, our belief is that Movie & Entertainment remains a fundamental part of people's lives. Over the past half-decade, it has proven to be a profitable industry and is likely to remain so. Predicting specific players' longevity may be challenging, but it's comparatively easier than forecasting airlines, for instance. Major historical players like Paramount, Sony, and Disney still thrive, in contrast to airlines like Trans World Airlines, Pan American, or even KLM. By selecting the best in the industry, we anticipate potential recovery with even 100% returns over the next 3-5 years as the Movie & Entertainment sector rebounds from its current challenges.

China Tech – China's trajectory as a nation is far from reaching its peak or resembling Japan in the 90s. Recent events, like the U.S. attempting to restrict Tier 1 chip sales to China, showcase China's resilience and ability to adapt, as seen with Huawei developing its own chips. While we don't advocate investing in Chinese Semiconductors (as we prefer other global players), this serves as an analogy for China's competitiveness in technological advancements. The scope of technological progress extends beyond semiconductors to areas like financial services, agriculture, retailing, and various other tech industries. We believe our chosen company is well-positioned to thrive when China undergoes recovery. If this recovery materializes, it presents another potential scenario for a 100% stock price appreciation in our selected securities.

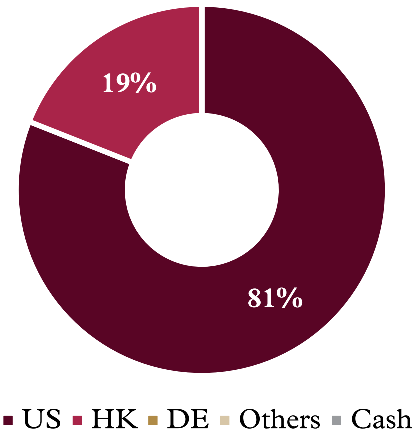
Closing Remarks

While we cannot predict the specific returns for 2024, our outlook for the coming years envisions a solid high single-digit or low double-digit return for our portfolio. While some industry peers may boast about potential 5x or 10x returns, it's crucial to consider the risks associated with such high gains. We've witnessed instances like WeWork facing bankruptcy and Alibaba experiencing a 50% decline from its IPO. In managing MTC's portfolio, our primary focus has been on achieving consistent, absolute long-term returns and avoiding permanent capital losses, even if it means navigating through periods of higher volatility. Unfortunately, correlation in markets can lead to increased volatility, as observed in Q4 2018, Q1 2020, and throughout 2022. Despite these challenging periods, we've consistently recovered to reach new highs. Looking ahead, we hope our investors understand that in a span of 50 years, some investment strategies may undergo temporary underperformance, possibly in succession. While our initial five years were impressive, the recent five years showed flat performance due to heightened volatility. Our aspiration is that the next five years will resemble the positive trajectory of the initial five. In the event of another market downturn, indicated by a 'Value Chart' filled with 'Deep Value' similar to December 2022 at 81%, we want our investors to recognize that the recovery will be explosive. While Meta and our semiconductor investments rebounded swiftly this year, our approach as value investors relies on buying assets at attractive prices and the fortunate timing of their explosive returns. We are optimistic that Movie & Entertainment, China Tech, and Others will follow suit. Regardless of whether these returns materialize in 2024, we believe we can outperform MSCI ACWI on a since inception basis again by the end of the year.

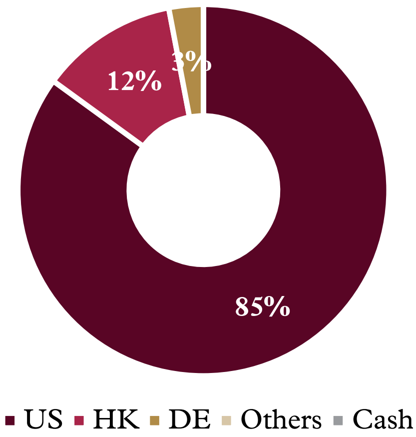
Charts 1: Company Listing and Sector Breakdown

Company Listing Breakdown

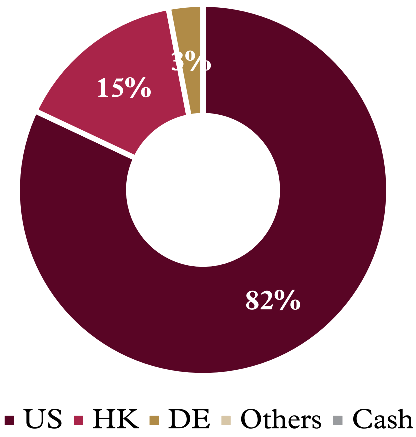
Prior Year (Dec 2022)



Prior Quarter (Sep 2023)



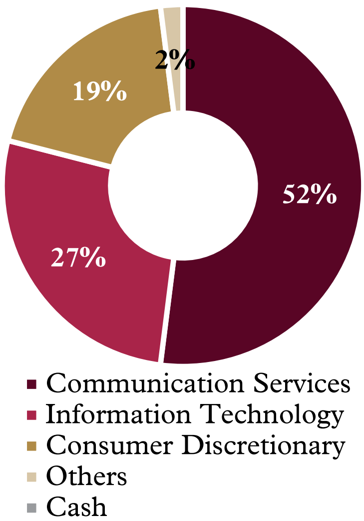
Current Quarter (Dec 2023)



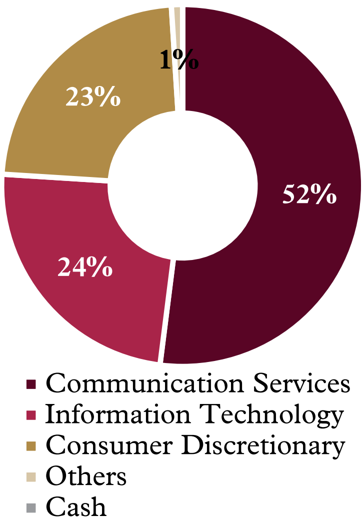
For Q4 2023, US allocation reduced to 82%, as we trimmed semiconductor stocks and made a slight increase to our selected securities in China.

Sector Breakdown (GICS)

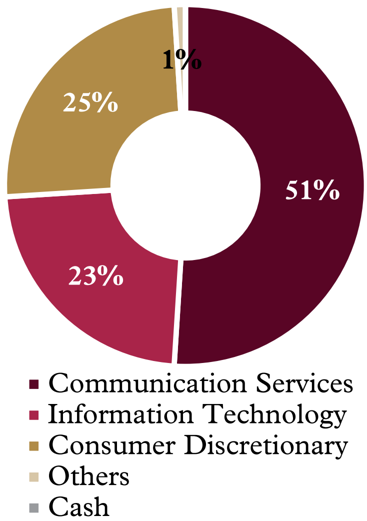
Prior Year (Dec 2022)



Prior Quarter (Sep 2023)



Current Quarter (Dec 2023)

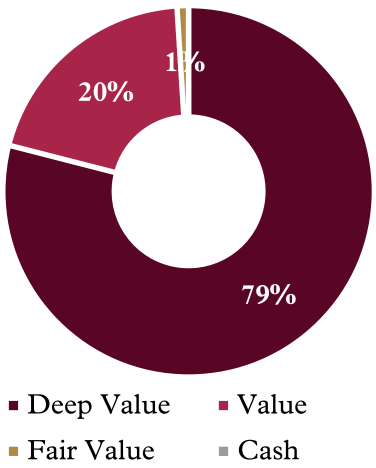


Compared to the prior quarter and year, there was not much change in the sector breakdown, as we trimmed securities in sectors that appreciated and increased allocation to securities sectors that did not move.

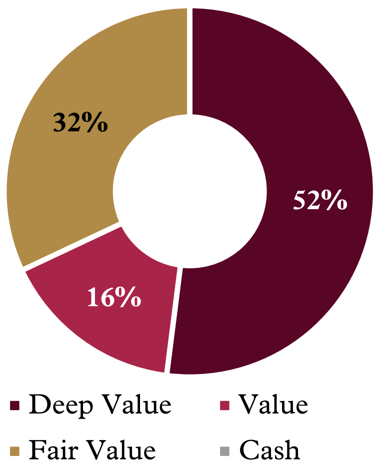
Charts 2: Value and Leverage Breakdown

Value Breakdown

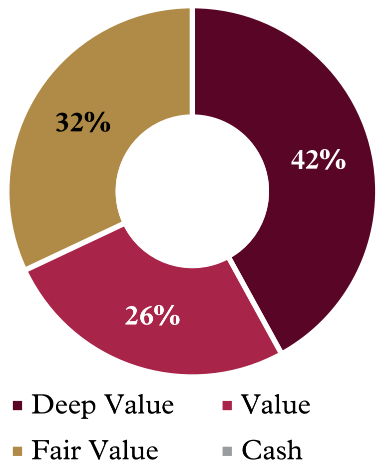
Prior Year (Dec 2022)



Prior Quarter (Sep 2023)



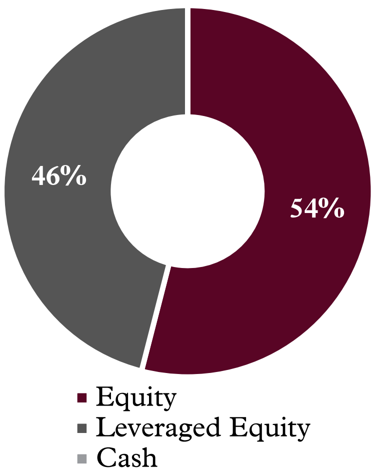
Current Quarter (Dec 2023)



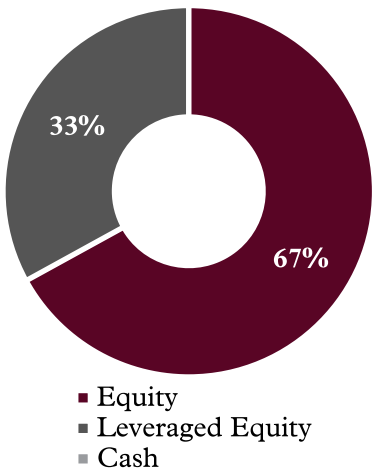
For Q4 2023, we re-rated the remaining semiconductor stocks from deep value to value, which now constitutes 26% of the portfolio.

Portfolio Leverage Breakdown

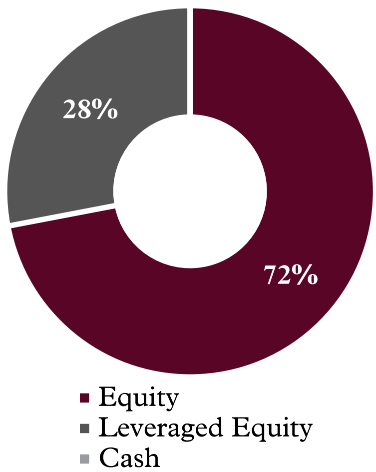
Prior Year (Dec 2022)



Prior Quarter (Sep 2023)



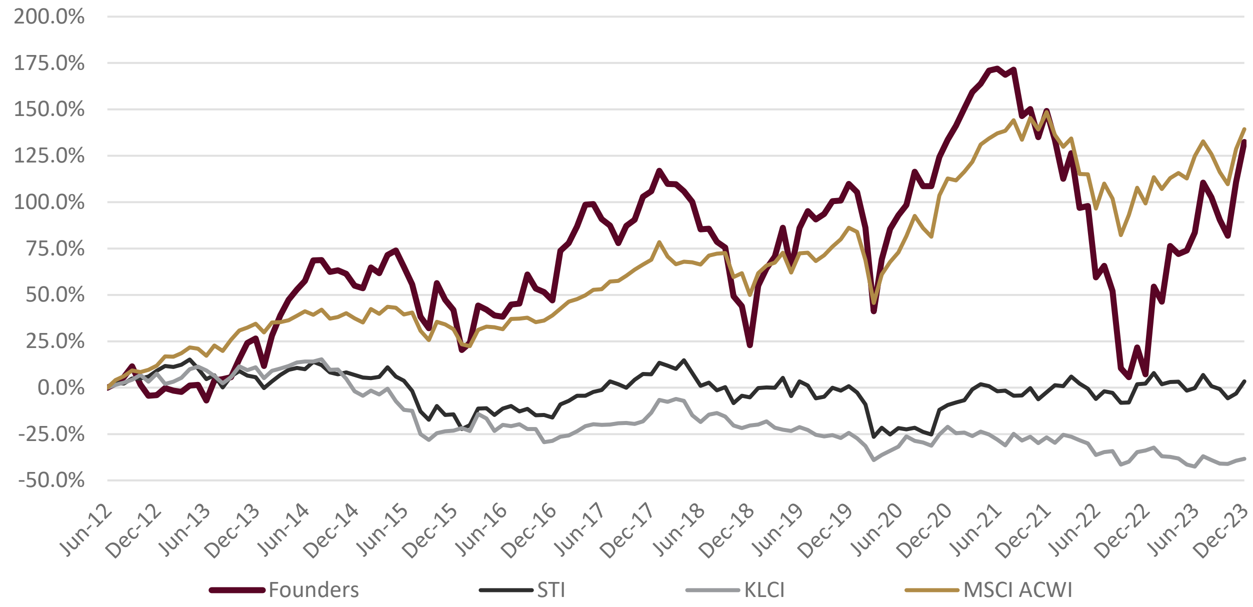
Current Quarter (Dec 2023)



For Q4 2023, leverage declined to 28% as a result of the overall equity portion appreciating significantly for the quarter.

Charts 3: Performance

Since Inception (Jul 2012 – Dec 2023), net of fees, USD



Disclaimer

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