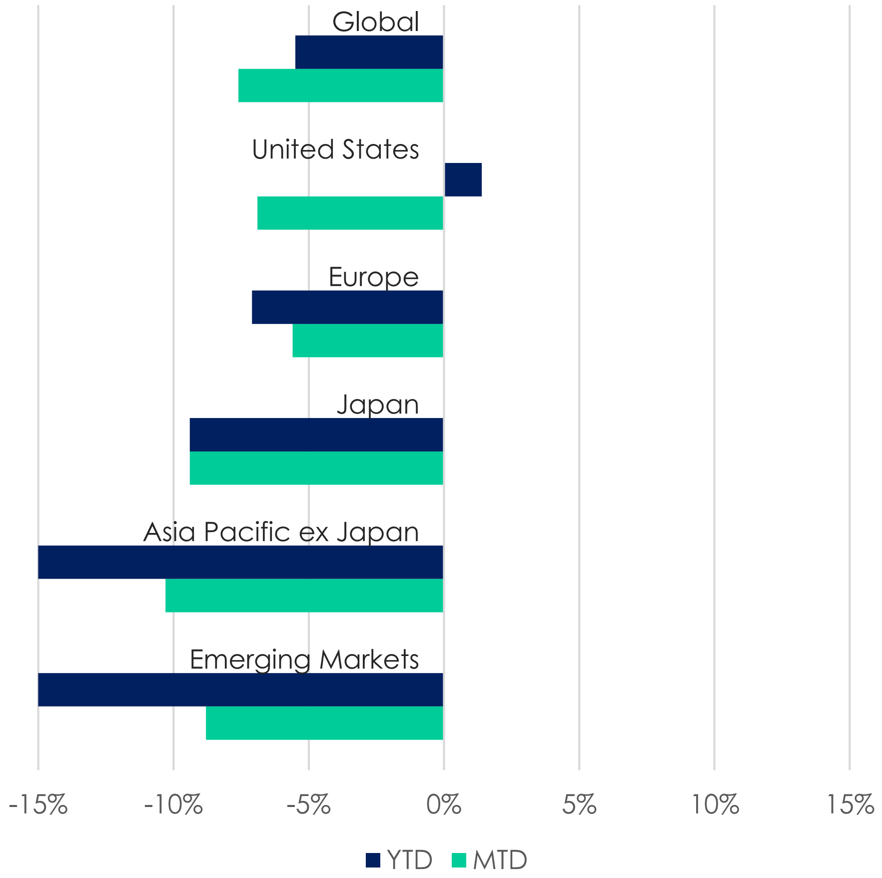
Monthly Investment Update
November 2018

finexis
ASSET MANAGEMENT
汇信资产管理有限公司

Market Review: Equities

Regional Equity Performance



Returns in index currency terms as of 31 Oct 2018. Source: Bloomberg

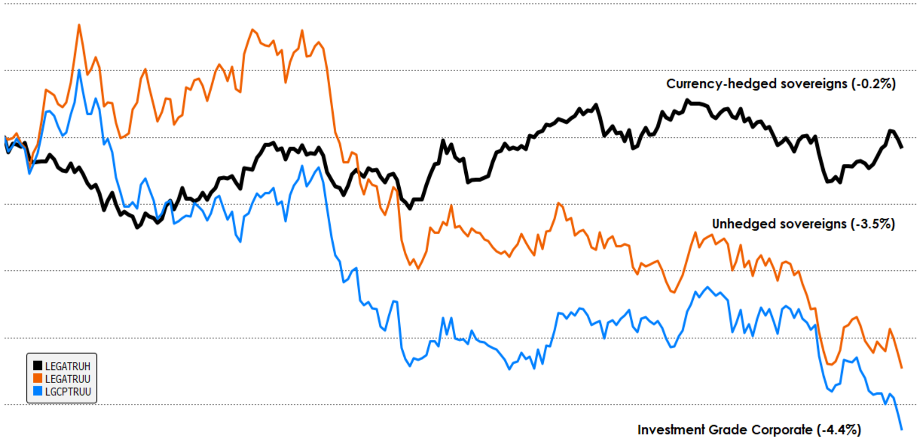
Equities experienced one of the roughest months in recent memory as global markets declined viciously in October. This time, previously resilient US equities fell alongside other risk-assets; resulting in investors feeling the full brunt of the sell-off. The recent volatility can be attributed to a culmination of factors, namely: late-cycle jitters, geopolitical tensions, and withdrawal of liquidity in the market.

As risk-off sentiment descended upon markets, sectors that had rallied strongly over the year declined the most. In the US, high-growth tech stocks detracted meaningfully from performance – Amazon -20%, Nvidia -24%, Netflix -19% were a few names that declined sharply, though still firmly in the green for the year. Financial companies, a laggard year-to-date, fell by less than the broader market. Year-to-date, the US S&P 500 Index remained in positive territory, gaining a modest 1.4%.

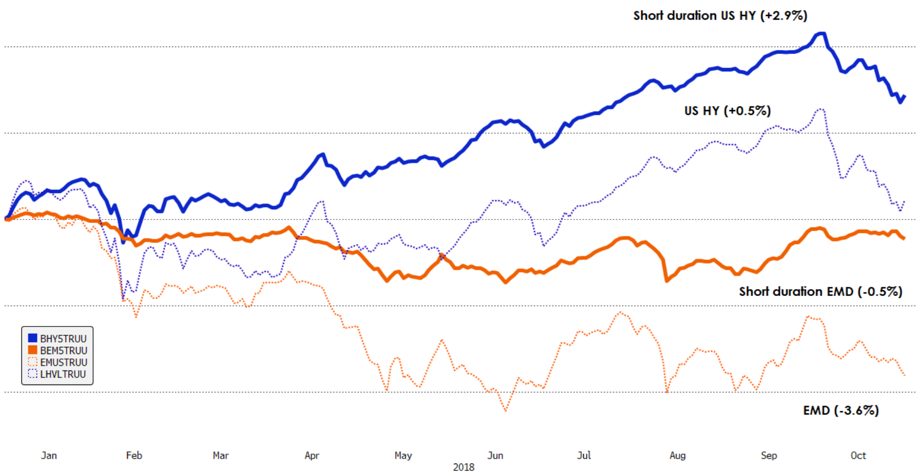
Asia and emerging market equities continued their decline as trade tensions between US-China continued to dominate news headlines, affecting investor sentiment. At the same time, the dollar has continued to appreciate, providing another headwind for foreign companies that borrow in the currency. That said, developing markets ended the month on a more upbeat note, rallying strongly on the back of pledges by the Chinese government to stimulate the economy, as well as on speculation that trade tensions may ease going forward.

Market Review: Fixed Income

Currency-hedged sovereign bonds resilient under stress



Short duration debt outperformed for both US high yield and EMD



Source: Bloomberg

October was a test of resilience for fixed income portfolio. This portfolio has two components: flight to safety and risk-adjusted yield. The flight to safety investments are focused on currency-hedged sovereign bonds which were flat in October while practically all other fixed income segments were down. Currency-hedged sovereign bonds are also flat for the year, which means we are not paying too much for "insurance".

Investment grade corporate bonds were down 1.7% in October and -4.4% year-to-date. Here we are reminded that even though "investment grade corporate" may sound less risky than "junk (high yield)", paying attention to valuation makes a difference in the returns we get.

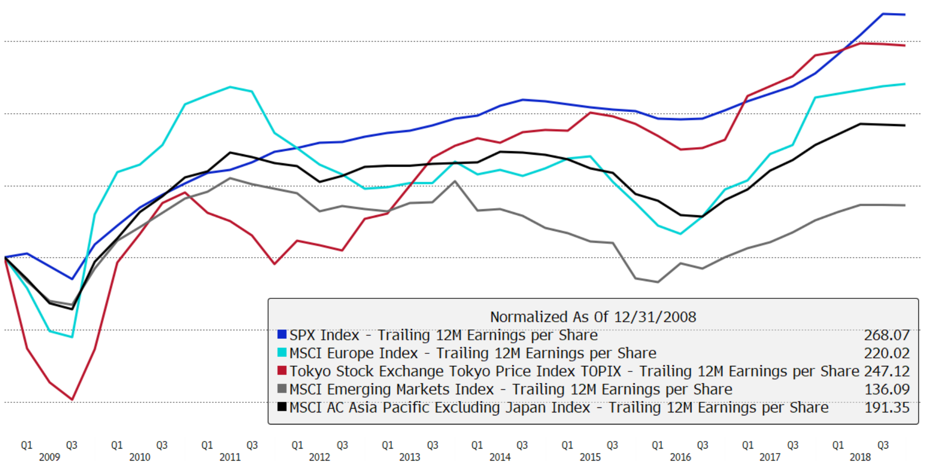
For the yield investments, our bias to short duration has served the portfolios well; contributing on the upside, while being defensive on the downside. Amid months of large gains and losses this year, short duration exposures in high yield and emerging markets have outperformed their broader markets.

Short duration high yield has been a standout this year, with gains of 2.9%. We reduced high yield exposures on valuation concerns in early October, locking in some profit. Even though we would not have predicted the market sell-off which ensued, the valuation discipline served us well.

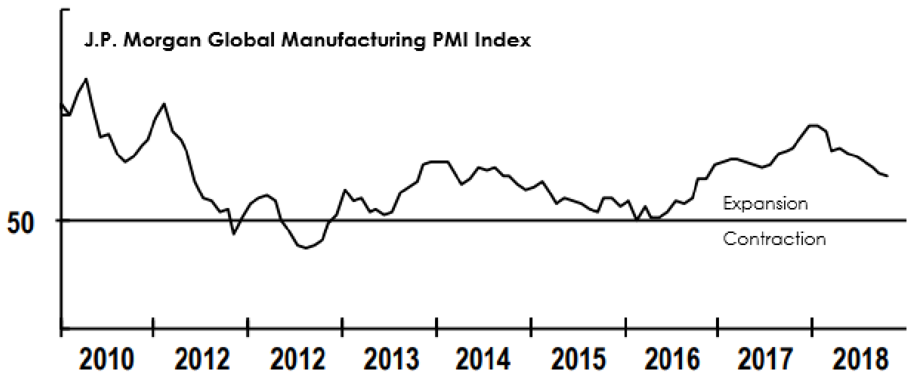
The sell-off also spilled over to emerging market bonds, with hard and local currency bonds dropping by similar amounts. Our specific exposure to short duration EMD have been a relative standout, being flat throughout October and the year.

Key Themes: Riding on late-stage growth

Earnings have held up so far…



…but economic indicators are hinting at further slowdown in growth



Source: Bloomberg, J.P. Morgan and IHS Markit

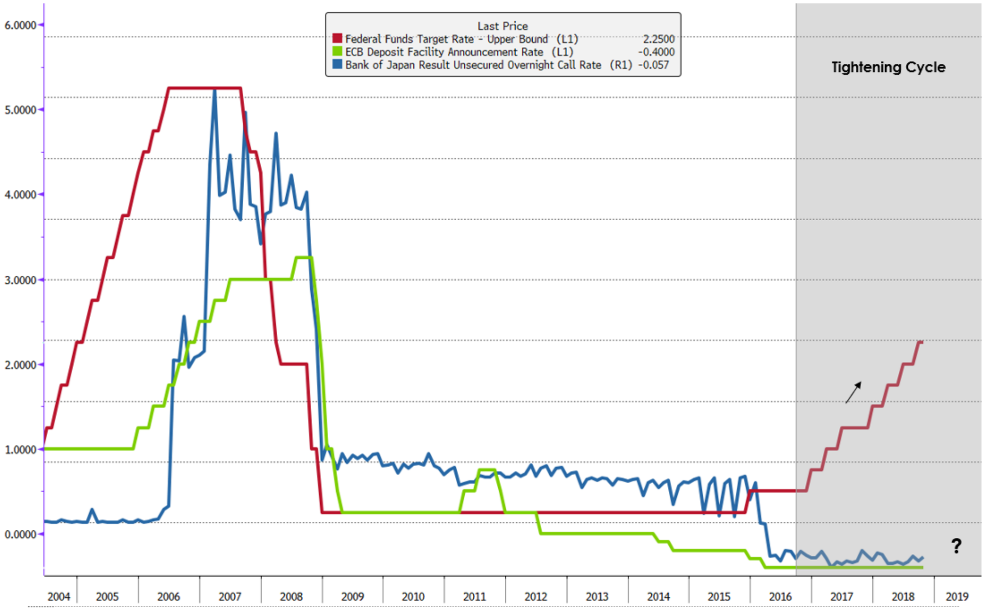
Towards the end of 2017, a popular narrative was that the world has entered a synchronised growth environment that would propel risk assets much higher going forward. While it has not been the smooth ride that most investors were expecting, there are areas in the market which are exhibiting late-stage growth characteristics that may present us with interesting opportunities.

Generally, corporate earnings have held up well amidst the market volatility, which may present an opportunity as prices (and valuation) trend downwards. On the other hand, we are vigilant that economic and business activity may be impacted by a prolonged trade slowdown, or by a general decline in business confidence. The latest J.P. Morgan Global Manufacturing PMI, which is an indicator of global manufacturing activity, continued to slow in October (growing at a slower pace) – a number above 50 indicates expansion, while a number below reflects a contraction in activity.

There is increasing evidence to suggest that Prime Minister Shinzo Abe's efforts to stimulate Japan's economy may be more sustainable. Earnings are robust, with profit margins hovering at their all-time-high. There is a further boost from corporate reforms as evident from increased dividend pay-outs. The ongoing earnings season has been more of a mixed bag so far. While companies like Fanuc Corp provided weaker guidance on their future earnings outlook, Sony Corp., and Softbank reported strong earnings that beat the consensus estimates.

Key Themes: Central bank tightening

Japan and Europe to follow US to hike interest rates?



Source: Bloomberg

Central banks continue to act on their mandate to manage the undesirable aspects of growth, such as inflation and irresponsible investments fuelled by cheap money. The Fed continues its rate hike cycle, while the ECB and BoJ are biding their time to commence their own hikes as they seek signs of overheating in their respective economies.

Short duration: "Interest rates rise, bond prices go down"; this is one of the fundamental tenets in markets. Short duration bonds have less sensitivity to rate hikes than long duration bonds. To continue to earn coupon while mitigating interest rate risk, we reduce portfolio duration by focusing on short duration exposures in high yield and emerging market bonds.

Financials: The good thing about investing is there are always two sides to the coin. While rising rates present a challenge to bond investments (which have been mitigated through short duration), financial equities respond favourably to rising rates. Indeed, the past month saw US banks reporting robust revenue growth driven by higher interest rates; supporting our thesis. One risk that we are paying close attention to is any meaningful slowdown in economic activity that would affect loan demand.

Why do we still hold on to sovereign bonds when rising interest rates are supposedly bad for them? Just as everyone has insurance to cater to rainy days, or pay for airbags in their cars, sovereign bonds play an important role in buffering portfolio volatility during periods of stress. Like any consumer, we want our choice of "insurance" to be effective while limiting opportunity cost. We maintain our focus on currency-hedged global sovereign bonds as a more efficient exposure to manage portfolio volatility.

Key Themes: Search for yield

Years of low rates post the 2008 crisis have resulted in cyclically lower rates of return for many assets. In such environments of low deposit rates and desire to beat inflation, investors are on the constant lookout for opportunities that offer an incremental return over cash. Sometimes, these efforts don't work out well; there are instances of investors losing their entire investment (and even their lives) after betting on opportunities promising high returns without understanding the risks. We take a more measured approach to the search for yield, while managing associated risks. As markets continue to be volatile, we seek yield investments backed by fundamentals to avoid permanent capital loss.

US High Yield: Volatile markets also present opportunities to sell out of overvalued markets and switch into those with better valuation. US high yield did decline as we reduced exposures arising from stretched valuations. Investors in high yield still get meaningful upside from coupons, though rich valuations mean that price appreciation tends to be limited.

EM bonds: The long-term fundamentals for emerging markets are well-known, particularly as many of our investors are able to live and breathe the opportunity (and volatility). We assess the benefit and risk across the various ways to participate in the EM opportunity; from hard currency investment grade to local currency high yield bonds. In the current environment, short duration hard currency EMD continues to provide comparable yield while being more insulated from currency and interest rate risk.

Asian High Yield: As mentioned last month, being disciplined paid off as other investors who embraced Asian and local currency bonds without paying attention to valuations have had to nurse losses this year. In 2017, Asian high yield went as low as 4.5%, not a good payoff for taking high yield risk. After correcting this year, and at current yield of 8.7%, Asian high yield markets are compensating investors sufficiently. Nevertheless, we continue to monitor for risks such as default and refinancing problems.

Markets have not been kind to holders of IG corporate bonds which have limited upside potential, and lack the safe-haven attributes of government bonds. While the recent declines have made IG corporates less expensive, their long duration nature make the risk-reward less compelling in light of rising rates. Hence, we continue to fund our overweight allocation from the investment grade corporate segment.

Key Themes: How are we positioned?

Late-stage growth	Central bank tightening	Search for yield
US Large-Growth equities	Financial equities	High-yield short duration bonds
Europe Large-Growth equities	Short duration fixed income	Emerging market short duration bonds
Japan equities		
China 'A' equities		

Asset Allocation Strategy

Equity Regional	--	-	=	+	++	Allocation strategy
United States		■				Large cap growth to capture late stage economic growth, and where large caps are more resilient to rising financing and wage costs. Financials to benefit from rising rates and increasing interest income.
Europe		■				Slight underweight as valuations are on the higher end, and as economic activity continues to moderate.
Japan				■		Slight overweight as economy is supported by structural growth arising from corporate reforms, and equities at attractive valuations.
Asia Pacific ex Japan				■		Maintaining exposure to China 'A' as valuations are attractive and supported by earnings growth.
Emerging Markets			■			Earnings are expected to slow, and valuations are de-rating from high levels.

Fixed Income	--	-	=	+	++	Allocation strategy
Sovereign			■			Focus on hedged global government bonds to buffer portfolio volatility during periods of stress.
Investment Grade	■					Maintaining no exposure as incremental yield does not sufficiently compensate for rich valuation.
High Yield			■			Valuations have become less attractive even as fundamentals continue to be supportive. Maintain short duration to mitigate rate hike impact.
Asia				■		Valuations have improved significantly after being relatively overvalued from 2017, with relatively attractive yields. Maintain short duration to mitigate rate hike impact.
Emerging Market Debt				■		Valuations continue to be attractive amid improving sentiment. Maintain short duration to mitigate rate hike impact.

Notes: - - Underweight - Slight Underweight = Neutral + Slight Overweight + + Overweight

Current Previous

Market Index Returns

Equity Regional	MTD	YTD
Global	-7.6%	-5.5%
United States	-6.9%	1.4%
Europe	-5.6%	-7.1%
Japan	-9.4%	-9.4%
Asia Pacific ex Japan	-10.3%	-17.2%
Emerging Markets	-8.8%	-17.5%

Fixed Income	MTD	YTD
Global Aggregate	-1.1%	-3.5%
High Yield	-1.8%	0.5%
Asia	-1.0%	-2.3%
Emerging Market Debt	-1.4%	-3.6%

Currencies	MTD	YTD
USD/SGD	1.4%	3.7%
EUR/SGD	-1.2%	-2.3%
JPY/SGD	2.1%	3.4%

Commodity	MTD	YTD
Gold	1.9%	-6.8%
Oil (WTI Crude)	-10.8%	8.1%

Equity Countries	MTD	YTD
Australia	-6.1%	-3.9%
Brazil	10.2%	14.4%
China "A"	-8.3%	-21.8%
China "H"	-8.0%	-13.4%
Hong Kong	-10.1%	-16.5%
India	-4.9%	1.1%
Indonesia	-2.4%	-8.2%
Korea	-13.4%	-17.7%
Malaysia	-4.7%	-4.9%
Russia	-5.0%	11.5%
Singapore	-7.3%	-11.3%
Taiwan	-10.9%	-7.9%
Thailand	-5.0%	-4.8%

Equity Sectors	MTD	YTD
Gold	1.9%	-18.4%
Energy	-11.3%	-6.8%
Technology	-8.7%	7.3%
Healthcare	-6.6%	4.4%
Financials	-4.9%	-6.1%

Returns in index currency terms as of 31 October 2018. Source: Bloomberg

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