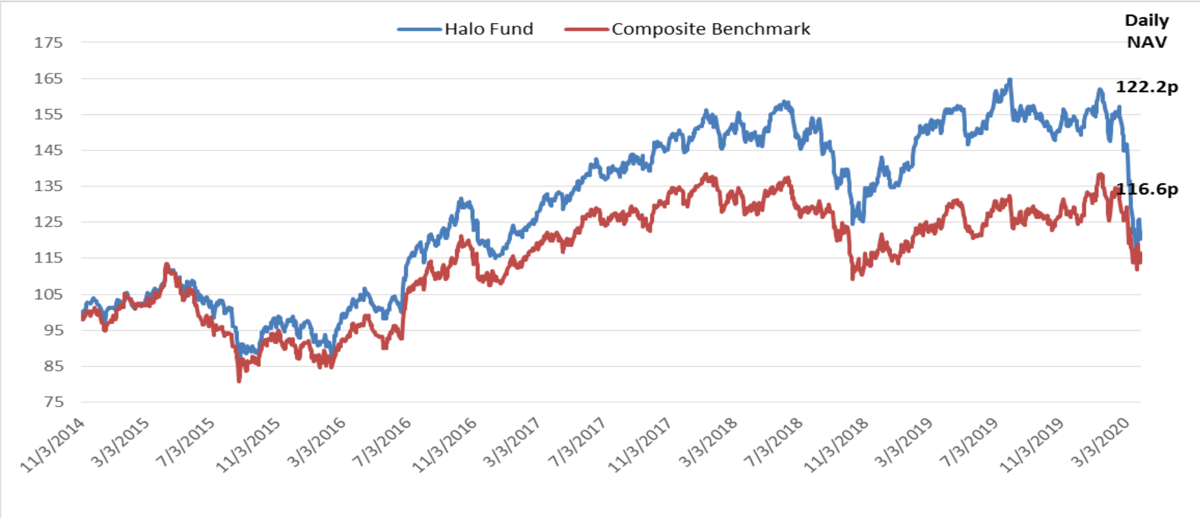
# VT HALO Global Asian Consumer Fund

## March 2020 Quarterly Letter

The first quarter will certainly be a quarter to remember as this Black Swan event of a once in a century pandemic hits the world. With our focus on the consumer in Emerging Asia, we are right in the eye of the storm as our stocks felt a direct impact from the lockdowns and falling consumer confidence.

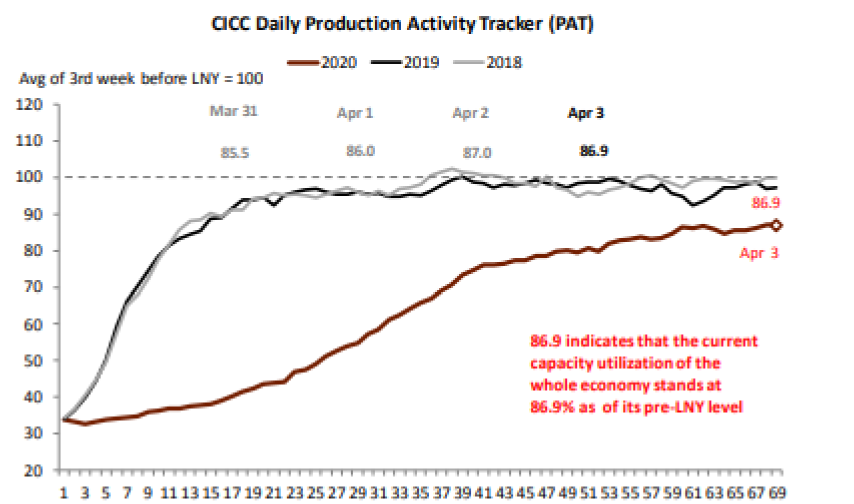



*Performance data shown is of the B £ Net Acc. share class. Custom Benchmark, 30% MSCI AC Asia ex Jap Consumer Staples, 30% MSCI AC Asia ex Jap Consumer Discretionary, 10% MSCI Communication Services and 30% MSCI AC Asia ex Japan Index. From 01/12/18 Custom Benchmark reduced Consumer Discretionary to 30% and added 10% Communication Services, due to reclassification by MSCI. Past performance is not a guarantee of future returns. Data from Valu-Trac Administration Services and Reuters. This is for illustrative purposes only and in accordance with our Prospectus Halo does not benchmark against any index* in accordance with our Information Memorandum and Prospectus.

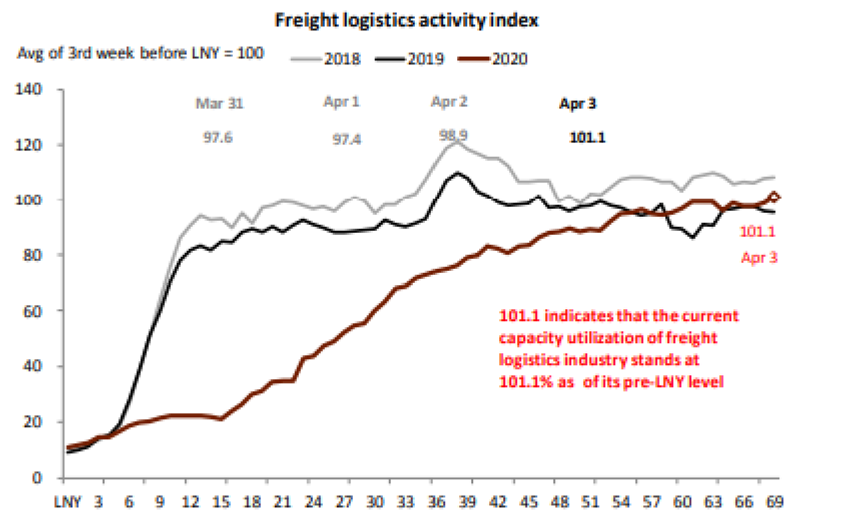
Naturally we are all in the dark as to how exactly this is going to pan out, with the timing of the ending of lockdowns and social distancing in the US, Europe and Asia remaining uncertain. When will there be accurate serology testing we can do at home and a vaccine to allow us to return to some sort of normality? So rather than speculate as to how we can play the markets in the near term, watching the daily numbers on COVID-19 cases and when they will peak, we have been focussing on valuations today and the returns in the future.

**China's experience**

Following the removal of the lockdown in China, we are seeing the economy returning to some sort of normality, although the data is mixed. According to CICC we can see below that production activity has reached 87% of prior year levels, and with regards to logistics, it is now just above its pre-Chinese New Year (CNY) levels. This may be on the back of playing catch up post the lockdown. Both these data points illustrate certain activities are normalising. But to counter this, we are not yet seeing capacity utilisation back to prior year levels, and one can expect certain industries geared towards exports to see deteriorating demand as the rest of the world temporarily shuts down.




*Source: G7, Ministry of Transport, Subway web in selected cities, CICC Research*




*Source: Ministry of Transport, G7, CICC Research*

We are hearing that visits to shopping malls are running at around 50% of levels before the virus, but increasing on a week by week basis. On the other hand Restaurants are only back to 30-40% occupancy, flights are only running at 20% of pre CNY levels and cinemas remain closed. Naturally spending habits will change, with ecommerce being on obvious beneficiary of the shift in shopping behaviour. A drive towards a more healthy lifestyle is also supporting the growth in the healthcare and sportswear sectors. The desire to have perhaps material items and instead spend more on fewer experiences, which was a trend prior to lockdown, is likely to remain a focus for consumers, although large group gatherings may be slow to return.

China though will not return to 2019 levels that quickly, especially as there have been a number of jobs lost and the manufacturing export sector will see tough conditions in the near term. Hence government stimulus is coming with additional RRR cuts for the banks to encourage lending to the

SME sector. We also expect further infrastructure bond issuance both at the national and provincial level to accelerate fixed asset investment as private sector investment is likely to remain weak, given a large output gap. The government is also keen to encourage further consumption and we have seen action with regards to cutting VAT on certain items, subsidies on white goods and autos, together with some local governments providing coupons for certain consumption items. All in all we are seeing estimates for GDP growth in Q1 to be down anywhere between 5-9% on last year and GDP growth for 2020 to come in somewhere between 2-3%. This assumes no further acceleration in infection rates and the need for additional social distancing.

Taking a positive view of no further lockdowns being required in China for the rest of the year, and the recent company guidance from our Chinese holdings, which consist of 55% of the portfolio, we can expect to see, on average, over 10% earnings growth from our Chinese companies in 2020. This would be driven by the likes of Alibaba, JD.com, Tencent, in addition to our education, healthcare and utilities names.

**Vietnam can still achieve GDP growth of 3-4% in 2020**

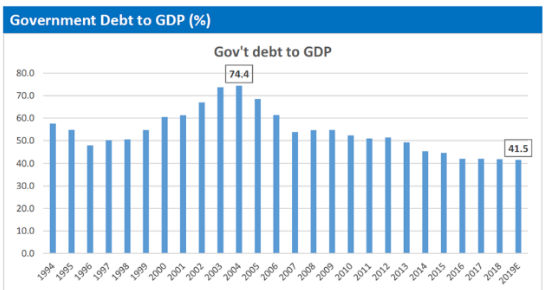
Another country that has remained on top of the virus with the number of cases being a little over 200 as I write, is Vietnam, although the stock market has been one of the worst performing in Asia. Naturally there will be some scepticism over the number of cases, but the government's actions provide credibility that they are not falsifying the figures. The government shut its border to China in early February and quarantined the border towns where a number of cases had occurred. It then effectively closed it borders to Europeans in mid-March and anyone returning to Vietnam who had been living overseas has to spend 14 days in quarantine. This was not done at home but in camps set up by the army, with over 75,000 people remaining in quarantine at the peak. They were also very quick to quarantine people who had been in contact or living close to other cases and in some instances had quarantined over 200 people relating to one case. They have tested over 40,000 people and have as mentioned above just over 200 cases with a majority of these "imported" from abroad, with no recorded deaths. On 1st April they invoked a partial lockdown in the major cities as they were taking no chances, with the aim of keeping the total cases below 1,000. Also from April 9th all visitors arriving in Ho Chi Minh at its airports, trains, bus stations and by private vehicles, will be required to get a test for COVID-19. Similar police check points have also been set up in the other major cities.

This has naturally impacted the economy and they have announced a fiscal stimulus package equivalent to 3% of GDP as well as interest cuts and special lending to directly impacted industries such as tourism. At its low the stock market was down over 30% this year, having already de-rated in 2019. The market reaction in our view is primarily due to the market being dominated by retail investors who account for 85% of the market turnover and trade using margin accounts. With a falling market the margins are called in, further exacerbating the falls. Looking at our Vietnamese holdings, Vincom retail, the shopping mall operator, fell 44% in Q1 and PNJ the jewellery retailer declined 45%. Techcom Bank, whose primary lending is mortgages and maintains the highest capital ratio at 16%, has the lowest leverage of the Vietamese banks at 6x and a ROE of 17.7%, is off 36% and now trades on a price to book of 0.7x. We believe the fundamentals of Vietnam are better than the stock market is indicating and we have recently added to Vincom Retail. We do not believe the near-term shutdown and lost rental income for a month, together with some tenant subsidies warrants a 45% fall in the share price. They are likely to delay the opening of some new malls due in Q3 and Q4 by a few months but we believe the underlying positive trend of an emerging middle class who wish to shop in a modern retail environment has not materially altered. Malls offer the best hygiene, and penetration rates relative to the size of the population remain very low. Malls are a weekend destination for air-conditioned leisure activities as there is little alternative in the major towns and cities, and this trend has not changed overnight due to the pandemic.

Vietnam's GDP growth rate for Q1 is estimated to be 3.8% with retail sales of goods maintaining a positive growth rate of 7.7% and it was the accommodation, catering and tourism sectors that have slumped. Although GDP growth this year will not be in the 6-7% range that we had been expecting in January, we still maintain GDP growth will remain positive and current estimates from economists are in the 4-5% range, based on the pandemic being contained and business activity to gradually normalise in Q3.

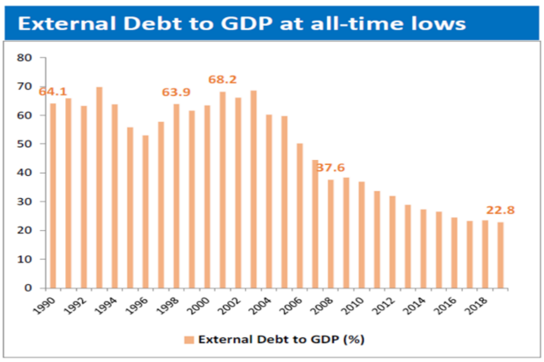
**Philippines: will it maintain positive GDP growth for 2020?**

The other country in ASEAN where we have significant exposure is the Philippines and this has been the worst performing market in Asia for 2020, with foreigners selling consistently in January, February and March. We believe a lot of this is due to a reflex to sell Emerging Markets when there is economic trouble and dash for US Dollars. In the case of the Philippine Peso it has surprised us having held up very well this year and it is unchanged against the US Dollar. This may be due to two factors. Firstly, their current account deficit is improving as domestic consumption falls due to COVID-19, and secondly they are a big beneficiary of falling oil prices, which provides another boost to the current account together with lower inflation boosting the spending power of the consumer. The government has cut interest rates in the Philippines, but rates are still relatively high at 3.25% and they have room to cut them further if need be. Borrowing both by the government and the consumer is low and they have greater room to raise debt levels if necessary with government debt at 41.5% of GDP, which is less than half the percentage found in the US or European countries. Also, post the Asian Financial Crisis and the Global Financial Crisis in the last two decades, they have made a conscious effort to reduce external debt, as you can see in the graph below. Both these factors would have helped steady the Peso.




***Government ready to borrow aggressively, foreign and local to fund fiscal expansionary support***

Source: Philippine Statistics Authority, Bureau of Treasury, Regis Partners estimates



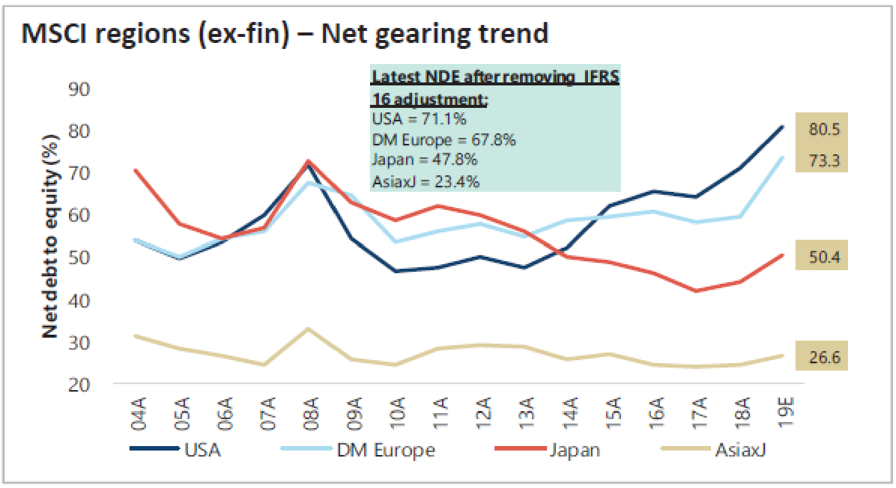

The market fell 31.3% in Q1 and we again see some real value in Philippines stocks, both in ones we hold and others we have been following closely. As the Bloomberg chart below illustrates, the price to book for the PSEi is currently at 1.3x, with the average over the last 10 years being 2.4x. We believe that ultimately the pandemic will disappear, and yes it may take another 12 months, but certain stock markets such as the Philippines are pricing in far too much pessimism.


Our exposure in the Philippines is principally focused on consumer discretionary stocks, with the casino operator Bloomberry, Robinsons Land whose principal business is shopping malls and All Home, a DIY and home furnishings retailer. All 3 shares have fallen over 40% and none of them have any balance sheet issues. On a 12 month view we can see considerable upside from current levels are looking to add at an appropriate time.

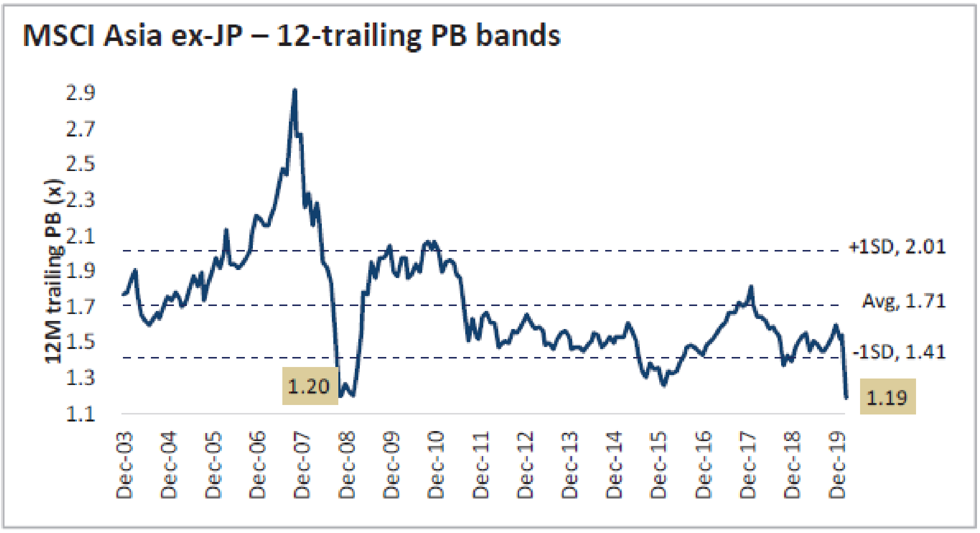
GDP growth expectations have fallen from 6% and are now closer to zero and it depends on the size of the fiscal stimulus the government is prepared to embark on for the rest of the year to see if they can maintain positive GDP growth. The government has room to spend, but remains cautious in raising debt levels, and has even mentioned if they spend more now there might be tax increases later to help pay for it.

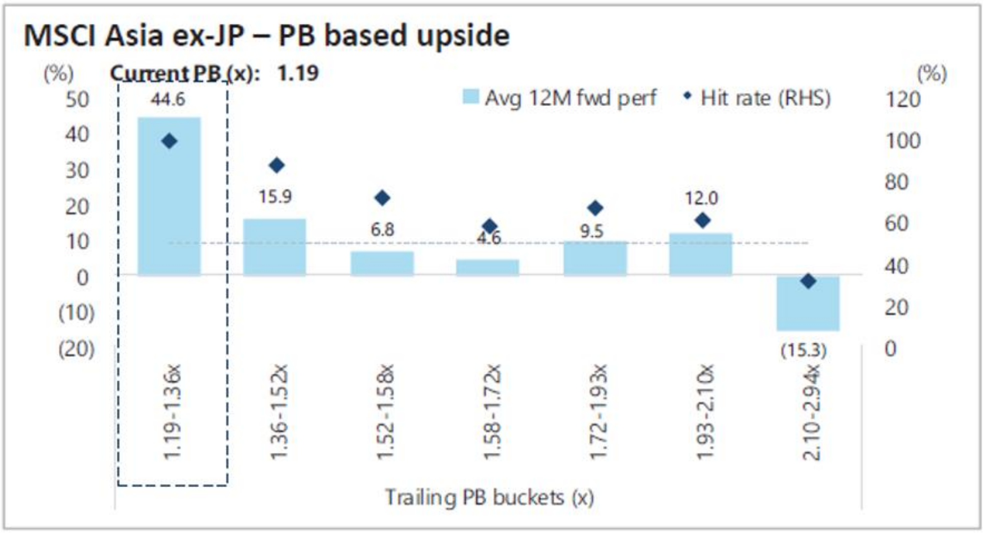
**Conclusion**

Our view can be neatly summed up with the charts below which I have taken from a Jefferies presentation. Asian corporates have better balance sheets than the rest of the world and the valuations today are also starting from a lower position, which should bode well for dividends and solvency.



After the sell off we have witnessed in Q1 the valuations based on price to book, are at similar levels to the Global Finance Crisis.




Based on historical experience, when valuations reach these levels, one can expect the average return to be 44% with a probability of 100% over the next 12 months. Needless to say history may not be a good guide to the future as this time it might be different, but it certainly provides a good indication we are close to a floor with regards to equity market valuations, and positive returns are to be expected if you have a longer time horizon of over a year.