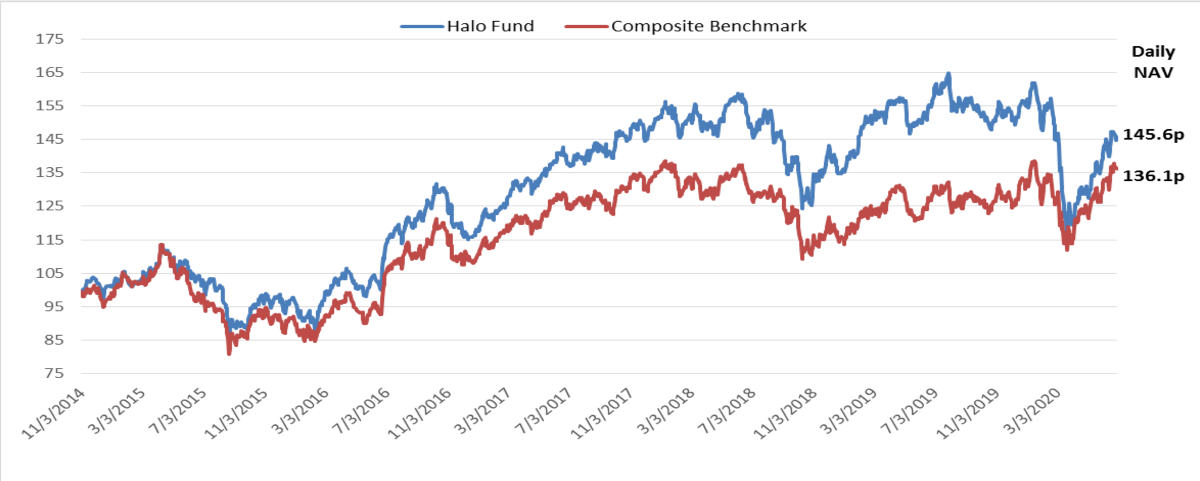
VT HALO Global Asian Consumer Fund

June 2020 Quarterly Letter

The second quarter has surprised the majority of investors with the speed and magnitude of recovery of markets both in Asia and the rest of the world. The Fund has seen the NAV climb from 122.2p to 145.6p representing a 19.1% return. The PMI data across Asia has been stronger than anticipated and in certain countries we are seeing GDP growth for 2020 being revised up amid further evidence of V shaped recoveries in economies that are opening up. As a result, we are fielding incoming questions such as the one below.

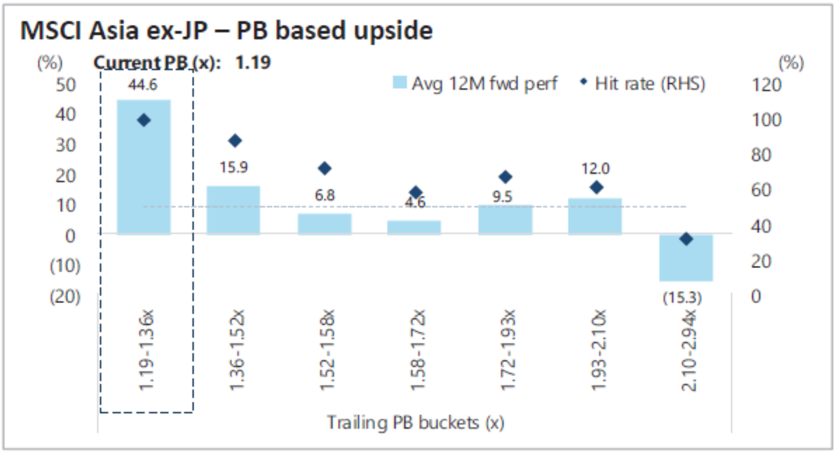


Performance data shown is of the B £ Net Acc. share class. Custom Benchmark, 30% MSCI AC Asia ex Jap Consumer Staples, 30% MSCI AC Asia ex Jap Consumer Discretionary, 10% MSCI Communication Services and 30% MSCI AC Asia ex Japan Index. From 01/12/18 Custom Benchmark reduced Consumer Discretionary to 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.

Are markets overvalued today?

This happens to be one of the most commonly asked questions today following the strong rally in markets over the last quarter. Many investors believe the US market is looking expensive today and the question is, does this apply to Asia as well? If the US sells off, will Asia come off with it? Well in the short-term, markets are correlated and it is likely that markets will decline in Asia if the US falls, but over time we believe it can decouple and there is still value in Asia.

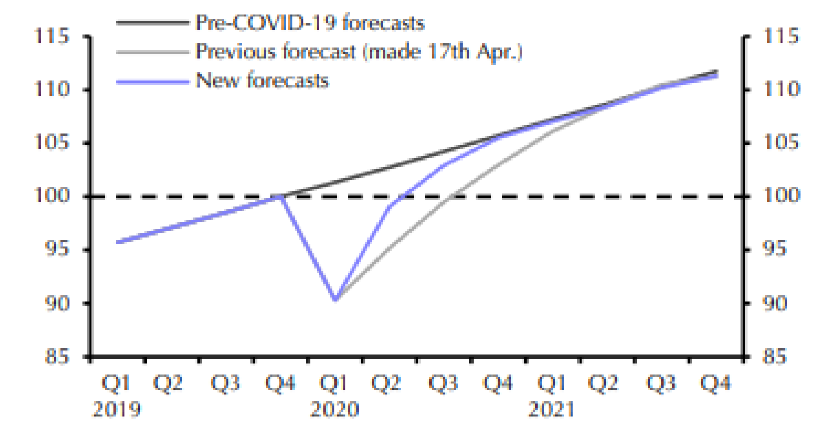
The price to book ratio today for MSCI Asia ex-Japan is 1.5x, which according to history provides a high probability of investors experiencing a positive return over the next 12 months. More precisely, the chart from Jefferies below indicates that with a starting price to book of somewhere between 1.36x and 1.52x the likelihood of achieving a positive return is 85% over the next 12 months, with the average return being 15.9%. We would concur with this based on how we view the world today in Asia.



Why we shall see positive returns over the next 12 months

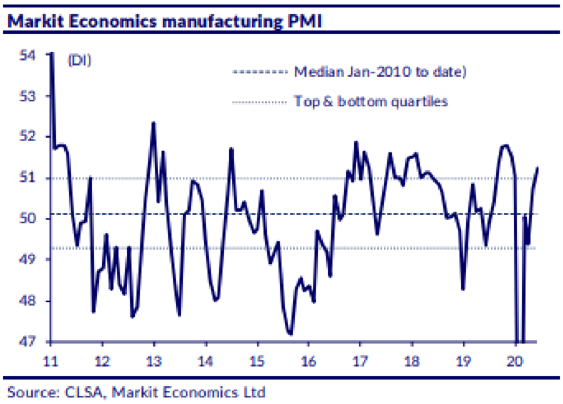
Principally this is down to two factors. Firstly, China and Vietnam, which currently represent some 65% of the Fund, are experiencing a rebound in GDP growth in Q2 post their lockdowns. Their economies are recovering quickly as consumer confidence returns, as there have been no new material outbreaks in either country. We are seeing upgrades to GDP numbers for 2020, with China now expected to grow between 2-3% and Vietnam at 3.5-4.5%, having grown 1.8% in the first half of 2020, including a 3 week lockdown and subsequent recovery. In both countries, exports have held up better than expected as COVID 19 primarily impacts domestic services more than demand for goods. The chart below from Capital Economics shows their revised view on how China's GDP growth will look against the trend line pre COVID 19. What they are forecasting now is China's GDP to be back to its long run trend growth rate by the end of Q2 2021, which has been revised from the end of Q4 2021. This is based on stronger PMI data in Q2, which has indicated a V shaped recovery helped by the support of the fiscal and monetary policies.

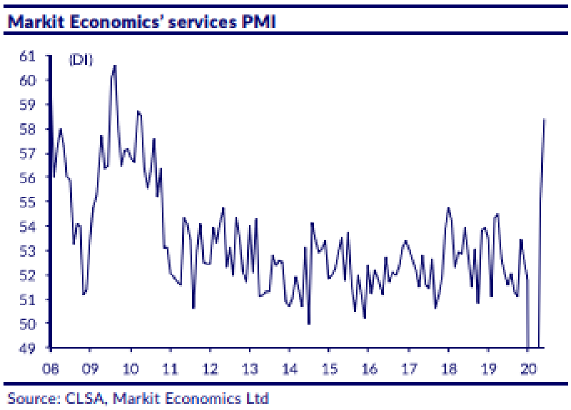
Chart 3: Projected Level of Official GDP (Q4 2019 = 100, constant prices)



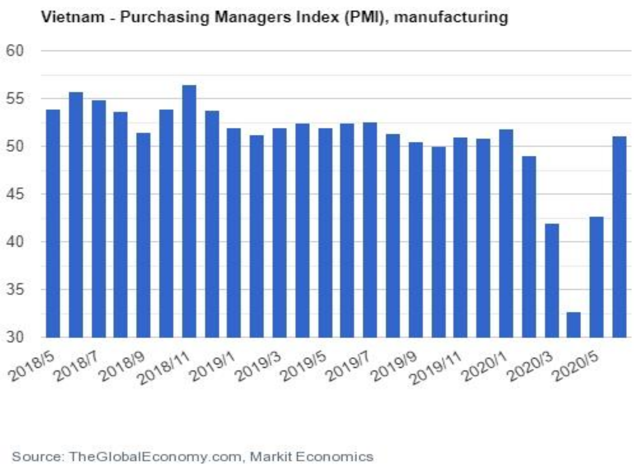
Sources: CEIC, Capital Economics

China has witnessed a V shaped recovery in the PMI data both for manufacturing and more importantly the service sector. The recovery in these readings over the last couple of months has been coming in at stronger than expected levels providing increased confidence that activity and consumption has returned. The service sector has rebounded to levels not seen since the stimulus post the Global Financial Crisis.



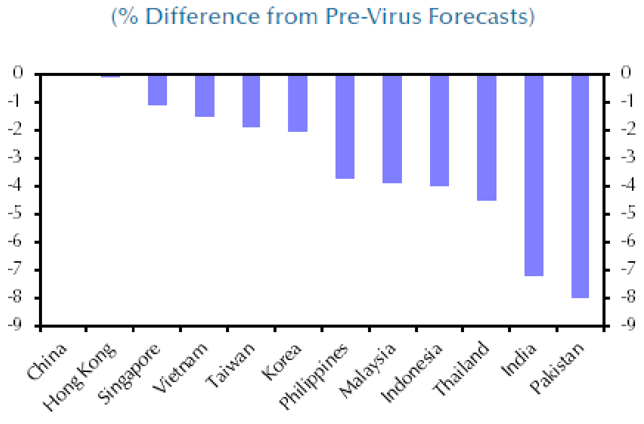


Vietnam has also seen a strong recovery in the PMI, with the level now at 51.1 and we could see this rise further over the next few months as the Government's fiscal stimulus kicks in along with the opening up of air bridges with other Asian countries who have controlled the outbreak of the virus.



Capital Economics have estimated the impact of COVID 19 on GDP for 2022 for the other economies in Asia as illustrated below. We can see for Vietnam the overall impact of COVID 19 on GDP in 2022 to be just over 1% less than it would have been if the pandemic had not occurred. Vietnam was expected to grow between 6-7% p.a. for 2020 to 2022 and so this is little more than a rounding error in my view.

Difference in estimated GDP in 2022 from pre-virus forecasts



Source: Capital Economics

Other countries fare less well, for example the Philippines and India, which are the next largest country weightings at 8% each in our Fund, will see a bigger impact from COVID 19. This is partly down to the lack of large monetary and fiscal stimuli from both countries and also the inability to quickly control the virus to allow life to return to some sort of normalcy.

This impact on growth is largely a 2020 story with a strong rebound likely next year as the harder and deeper the recession this year, the greater the rebound will be in the following year. As illustrated below from CLSA, the rebound next year for Emerging Asia is bigger than the decline, which will result in their GDP for 2021 being larger than 2019. Thailand remains the exception, due to the severity of the recession this year and its reliance on international tourism, therefore taking longer for GDP to recover to 2019 levels. If this holds true and admittedly this is a big IF, as we do not know how the pandemic will behave, then we should expect spending by consumers to rebound strongly, given these economies are driven by consumption. The forecasted 2021 GDP column in the table below signals an impressive rebound due for next year in Asia EM vs ROW. We also think it is fair to assume that out of the 200 vaccines in trials today, some of them will work and become widely available next year, so helping economies and markets recover.

CLSA real GDP growth forecasts

(% YoY)	2017	2018	2019	2020E	2021F
US	2.4	2.9	2.3	(5.0)	3.0
Europe	2.6	1.9	1.2	(7.5)	3.8
Japan	2.2	0.3	0.7	(5.0)	2.0
Australia	2.5	2.8	1.8	(1.4)	3.1
China	6.9	6.7	6.1	2.7	8.4
Hong Kong	3.8	2.8	(1.2)	(6.5)	6.1
India[1]	7.0	6.1	4.2	(6.5)	9.0
Indonesia	5.1	5.2	5.0	(2.2)	5.9
Korea	3.2	2.9	2.0	(0.4)	3.0
Malaysia	5.8	4.8	4.3	(4.4)	5.8
Philippines	6.9	6.3	6.0	(4.8)	8.8
Singapore	4.3	3.4	0.7	(4.1)	6.1
Taiwan	3.3	2.7	2.7	(0.7)	3.1
Thailand	4.1	4.2	2.4	(7.2)	6.5

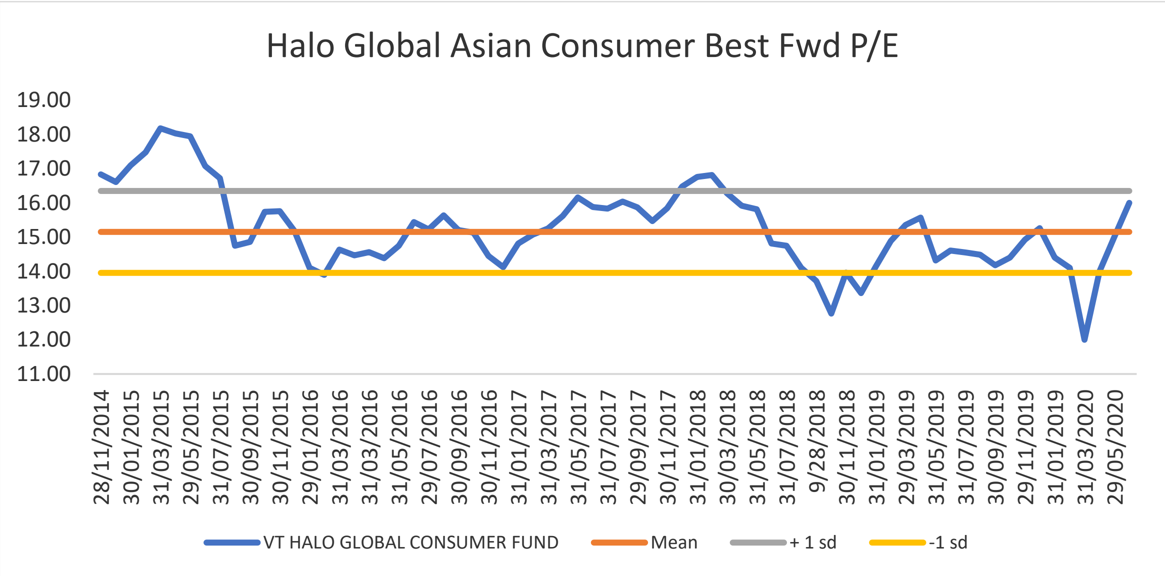
[1] Fiscal year starting April of captioned calendar year.
Source: CLSA, CEIC

So what do we think about the valuations today and the future returns for the Fund over the next 12 to 18 months?

Today we have 55% of the Fund in Chinese stocks and 38% of that is in internet stocks, with a further 20% of our Chinese weighting in Education and Sportswear. These areas are in structural growth sectors expected to deliver 20% earnings growth this year and even faster growth next year as the comparatives are easier given the impact to their businesses from February to May. The other holdings in China (except Sands China), should still see positive growth this year, albeit at a slower rate, but again demonstrate a strong recovery next year. Our holdings in Vietnam are 10% of the Fund and also driven by discretionary spending. The impact of the lockdown will see negative earnings growth in the region of 10-15% for Vincom Retail and PNJ, but assuming GDP rebounds next year with growth likely to be 8%, both will experience over 30% earnings growth next year. If their P/E multiples return to 2019 levels as we exit 2021, this points to at least 30% upside over the next 18 months if we are correct. Vietnam represents very good value today as it has better economic growth, but the stock market has not rebounded in the same way as other markets in North Asia such as Korea, Taiwan or China.

Turning to the Philippines and India where we have experienced a disproportionate impact to our holdings, the discretionary services industries such as shopping mall operators, restaurants, casinos, DIY and retail banking have been badly affected. So although profits will be down significantly, or in some cases perhaps making losses, we are of a view that by the end of 2021 or possibly early 2022, their operations will be back to 2019 run rates. So it is fair to expect another 18 months for the shares of these quality companies to achieve 2019 levels again, but we view this as positive as these shares today are all down between 30-40%, which means if they do achieve 2019 levels again, we shall see a rebound of close to 50% from current prices. We believe the long-term prospects of these companies remain intact.

The Fund today has a forward PE for 2020 of 15.7x and, assuming no large second wave we see over 20% earnings growth next year, leaving the forward PE at the end of 2021 on 13.1x This compares with our long run average forward PE multiple for the Fund, which has been in the range of 14-16x, as shown in the graph below. Implying the expected total return for the Fund would be in the range of 9-23%, which ties back to historical events that if you are starting from a price to book below 1.5x for the MSCI Asia Ex Japan Index your average return has been 15.9%.



Conclusion

Having reviewed our holdings, we expect over 90% of our portfolio to deliver earnings in 2021 above 2019 levels and the other 10% to achieve this in 2022, assuming there are no further national lockdowns and a vaccine becomes available in 2021. This provides us with confidence to expect the unit price of the Fund to return to highs over the next 12 months. So yes it has been a volatile ride but ultimately it will be in the order of 18 months to two years to reach historic highs of January 2020, which, in the scheme of events we are experiencing around the world, does not seem too much of an opportunity cost for investors.