ASTRAL VALUE FUND

Monthly Commentary

JUN 2016

	YTD 2016	Jun 2016	6 Mth	1 Year	MAY-15 Inception To Date	Outperformance Since Inception
Astral (Class B)	-1.4%	-4.1%	-1.4%	-2.8%	-3.2%	
MSCI Asia Pac	-2.3%	-0.2%	-2.3%	-11.9%	-16.0%	12.8%
HSI	-5.1%	-0.1%	-5.1%	-20.8%	-26.1%	22.9%
FSSTI* (USD)	3.5%	4.1%	3.5%	-14.3%	-20.0%	16.8%

*FSSTI was rebased to USD using the month end exchange rate

INVESTMENT OBJECTIVES

Astral Value Fund is a long-biased fund that aims to offer investors exposure to Asian markets equity returns with lesser risks through a disciplined approach to investing in mispriced situations.

FUND INFORMATION

Fund Manager	Astral Asset Management	
Currency	USD	
Jurisdiction	Cayman Islands	
Share Class	A	B
Management Fee	1.5%p.a.	1.2%p.a.
Performance Fee	15%	12%
Early Redemption Fee	3% Year 1 1% Year 2 1% Year 3	3% Year 1 2% Year 2 1% Year 3
High Watermark	Yes	
Dealing Frequency	Monthly	
Redemption Frequency	Monthly	
Fund Admin	APEX Fund Services	
Custodian	DBS Bank	
Fund Auditor	Deloitte	
Legal Advisors	Rodyk (Singapore) Walkers (Cayman)	
Bloomberg	ASTRALV KY Equity	
Website	www.astralasset.com	

Dear Partners and Friends,

June was an event-driven month. The start of the month saw the Fed deciding to put the rate hike on ice and markets cheered with a brief rally. This was followed by Japan, which postponed the sales tax increase in mid-June. The main event, however, was on whether UK will exit the EU. To the surprise of many, Brexit became a reality, and investors scrambled to readjust their asset allocation. For Asian investors though, the impact was assessed to be mainly negligible, and the Hong Kong and Singapore market indices recovered strongly in the last week of the month.

It was a less than desirable month for our portfolio for 3 key reasons. Firstly, June was the month where most of our portfolio companies started to trade ex-dividend. The distribution of dividends and the prevailing uncertainty prompted many to exit their existing positions, weighing negatively on our portfolio. Secondly, several of our HK positions also reacted negatively to company updates on slowing sales. Lastly, as the bulk of our portfolio focused on small to mid-caps, Brexit only made it worse as the resulting month-end recovery mainly benefited the large caps

We remained fully hedged on currency and look forward to putting our cash to good use as the market continue to throw up interesting opportunities.

During this period, we believe that our portfolio has gotten more valuable over time while holding its value, which we will explain in details on what we meant in our newsletter next. We believe the upcoming results season will validate many of our positions.

Do read on for our June newsletter.

Yours Sincerely,
Astral Asset Management

HALF YEARLY COMMENTARY

Dear Partners and Friends,

When we last spoke in December, we spoke of how we managed the first 7 months of operations and how we looked forward to this year after putting the difficult 2015 behind us.

On a macro level, the first six months of 2016 certainly seems a continuation of the difficult conditions in 2H2015. We had a tough January but slowly recovered over the months that followed but then a sharp downdraft in June put us back in a position of where we started.

Overall we finished the first 6 months of the year almost flat. This meant that we ended the first 14 months down 3% whereas indices fell around 15% to 25% during the same period. For our comparative indices to go back to the starting point they have to rally 17% to 33%. As we have avoided significant losses, a small 3% gain would bring us back to the starting point. This scenario bears out Warren Buffet's 2 golden rules in investing:

Rule No.1 is never lose money.

Rule No.2 is never forget rule number one.

-- Warren Buffet

At the family office we worked in previously, we simply called it "Winning by losing less"

On surface, it may seem that we have not achieved much, but we believe that our portfolio has gotten more valuable over time while holding its value. To illustrate, a year ago at 30 Jun 15, our portfolio was trading at 1.26x PB and EV/EBITDA of 8.96. Fast forward a year later, the price to book of our portfolio was 0.89x and EV/EBITDA of 7.0x. Logically to get a lower PB or EV/EBITDA, the price of our holdings should decline as was what happened to the indices. Our NAV has instead remained relatively constant during this period, as we have sold off some equities which have appreciated and switched to cheaper valuations equities, thereby making our portfolio more valuable.

What we have learnt

It may be more than 100 years since he passed away but when we review our biggest portfolio lessons since inception, Mark Twain's quote keeps coming back to mind.

It ain't what you don't know that gets you into trouble.
It's what you know for sure that just ain't so.

-- Mark Twain

Note: Our fund is only open to "accredited investors" as defined by the Monetary Authority of Singapore

There is a difference between deep conviction and falling in love with a stock. In the starting months of running our fund, we invested into a HK listed private hospital stock which specialized in obstetrics and gynecology. We felt sure that the company had great growth potential and that the future was bright with the relaxation of rules on private hospitals in China. Just imagine buying Raffles Medical or the delisted Thomson Medical at IPO price. We decided to pay a premium over the fair price of the company. Unfortunately, we fell so love with the idea especially after the announcement of the abolishment of the one child policy in China that we made it one of the largest position in our fund by buying more at higher prices.

In May this year, a scandal in the industry caused hospital stocks in China to tumble. We were slow to follow up as we thought the death of a cancer patient was unrelated to babies giving birth. In China though, where reputation was all important, the company's sales fell in May and June and the subsequent downgrades by brokers caused the share price to plunge. Whilst the outlook remains bright, our initial optimism meant that we suffered considerable losses. To be clear, our mistake was in embracing the rosy consensus and neglecting our price discipline thinking that nothing would hinder the rise of the stock. Yet as cautious value investors, we should know better and as it is, it will take some time for the stock to recover. The fundamentals and the business model of this hospital remain rock solid.

Another incident which bears out the lesson of never being too sure was a mentality that the Chinese would never depreciate the Yuan. We initiated several investments in CNH bonds as way to park our excess cash. This was bad call on hindsight as we were tempted by the generous yield but forgot Economics 101. The Chinese were in effect trying to perform impossible economic trinity of allowing free flow of capital, controlling both interest rate and exchange rate in a deflationary environment. Economics has been labelled the dismal science but testing fundamental assumptions in proven economic models should remain a no go for bottoms up stock pickers like us. In the end, we had to lick our wounds and close out all of our positions. Even though the loss was negligible to the fund, we suffered enormous opportunity cost as the excess cash could have gone to better use at the peak of the crisis.

The above two situations reminded us that caution is warranted in investing especially if the valuation is not cheap.

Investment Situation Showcase

What you are about to read should not be taken as investment advice but is a way of explaining our investment process for a certain investment situation of our fund. The investment situation illustrates a typical example of how we invest in a fast growing company situation.

Background and Investment Thesis

Back in 2012, Cogent was one of the many listed logistics players on SGX. We have not heard of the company until we read a news article mentioning that a listed subsidiary of Cogent Holdings won a bid for a six year lease from SLA for the management of the Grandstand, then known as Turf City. What piqued our interest was that we knew that the company was present in the vehicle value chain. The rental for the winning bid was about S$1m and the management indicated that the rental of a part of the complex to second car dealers could almost cover the monthly rental. That gave the company a free option. If the mall was a moderate success, the project would make money.

CEO Benson Tan set about revamping the Turf City. In 2012, this was before massive malls started to pop out in the west of Singapore, making the Grandstand a magnet for Singaporeans residing in the west. Even after new malls sprouted out in the west the last few years, the Grandstand remains the only large open space shopping area in the Bukit Timah area for families with plentiful free parking. We thought the project would do very well and at our time of investment, there were only 1 serious buyer, which conincidentally was the owner. We happily bought in for the fund that we were managing money for at that time.

As it turned out, the Grandstand was a roaring success. Just as we were about to sell out as the market started take notice of the company's prospects, we decided to meet the management just in case we missed out something.

Discussion with the owners however brought up another interesting project. Prior to the Grandstand, Cogent's core operations revolved around warehousing, transportation logistics and container storage. One key part of the business was unloading containers from ports in Singapore to its clients' warehouse and then driving the empty containers to an empty land to store the empty containers and then driving back its empty truck to its warehouse. Cogent had recently designed, patented and intended to build an integrated warehouse in Tuas with the ability to store the empty containers on the roof of its warehouse. The building design had the effect of significantly improving the efficiency as container trucks with empty containers now only need to make 1 trip to its integrated warehouse to store both the empty container and truck. The reduced trip would save much costs for both the company and customers.

We were confident that the new building which was completed in early 2015 would significantly improve the operations of the company and therefore the earnings of the company. The additional warehouse space would also increase Cogent's rental income and reduce its rental costs as the existing premise was rented. Hence, at the start of the new fund, we initiated an investment into the company.

How it turned out

The operations of the company improved as the rental income from the new warehouse and the planned efficiencies from the integrated building started to kick in. A sell-side broker started covering the stock late in 2015. In January this year, there was news that the company could be selling out their company or asset at a much higher price. Whether or not the company is taken private, we believe that there is still potential for more optimisation for the company's business. From the time we invested in May 2015, the stock returned close to 50% as at the end of June 2016.

Our View of the World Now

At present, there is much angst and fear over the current state of the world's economy. UK's unexpected exit from the Euro will certainly increase the uncertainties in the global arena. The flight to safety was apparent as many investors opted to put their money in money market funds, negative yield bonds and gold. One of our peers remarked recently that the current state of affairs is worse than Asian Financial Crisis in 1997 and the Global Financial Crisis in 2008. His reasoning was that policy makers have ran out of tools with interest rate already near zero and quantitative easing already implemented and a great depression was coming soon.

Bearishness has been most visible on China with famous investor George Soros predicting an impending credit bust like what happened to the US in 2007. Other critics point to the example of Japan in the 1980s where they predict the same deflation trap will happen to China. Yet we believe critics and the mainstream often missed out on the most important factor – Demographics.

Japan's rise since the end of World War II was based on its rise in exports and till today exporters still hold sway in the country. Evidence is most evident in that whenever the BOJ depreciates the Yen, the export dominated Nikkei will rise. The reliance on exports was mainly because the ageing Japan's population of 30 million with its isolationistic immigrant policies would never be sufficient to supply the end demand. This meant that the fortunes of the country was forever dependent on exports. However, new hungry countries are always on the horizon to compete to sell to the same end market of United States.

China, with its 1.3 billion population, was one such eager competitor. Continuous movement up the value chain over the years since early 1990s has made the Chinese a fearsome competitor in many areas of exports. Today, the clothes we wear, the mobile phones and computers we use or even the MSG used in our food originates from China.

The export-driven growth have helped China raise the incomes of its people and many have been lifted out of abject poverty. Indeed the sheer size of the population have started making them an end market in itself. In spite of the talk of China's doom, domestic consumption has continued to rise at double digits every month. The transition from an export-led economy to a consumer-led economy is underway. However, time will be needed as the elephant in the room do need some time and space to maneuver.

This is the big picture of continuing to invest in China's growth. No doubt, there will be growing pains. The goods and services in demand by the consumers will also evolve with time and more become sophisticated, but we believe patient investors who invest wisely in this juggernaut of change will be rewarded in due time.

We would like to thank our partners for their continued support, and we welcome potential partners to contact us at enquiries@astralasset.com for more information.

Sincerely,

Astral Asset Management