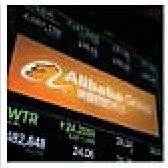

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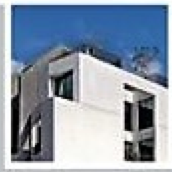

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Is it time to hunt for bargains?

Aggregate Asset Management is embracing the recent stock market volatility and seeking out undervalued companies. What are its fund managers buying? And what are they doing differently? Turn to our Cover Story on Pages 14 and 15.

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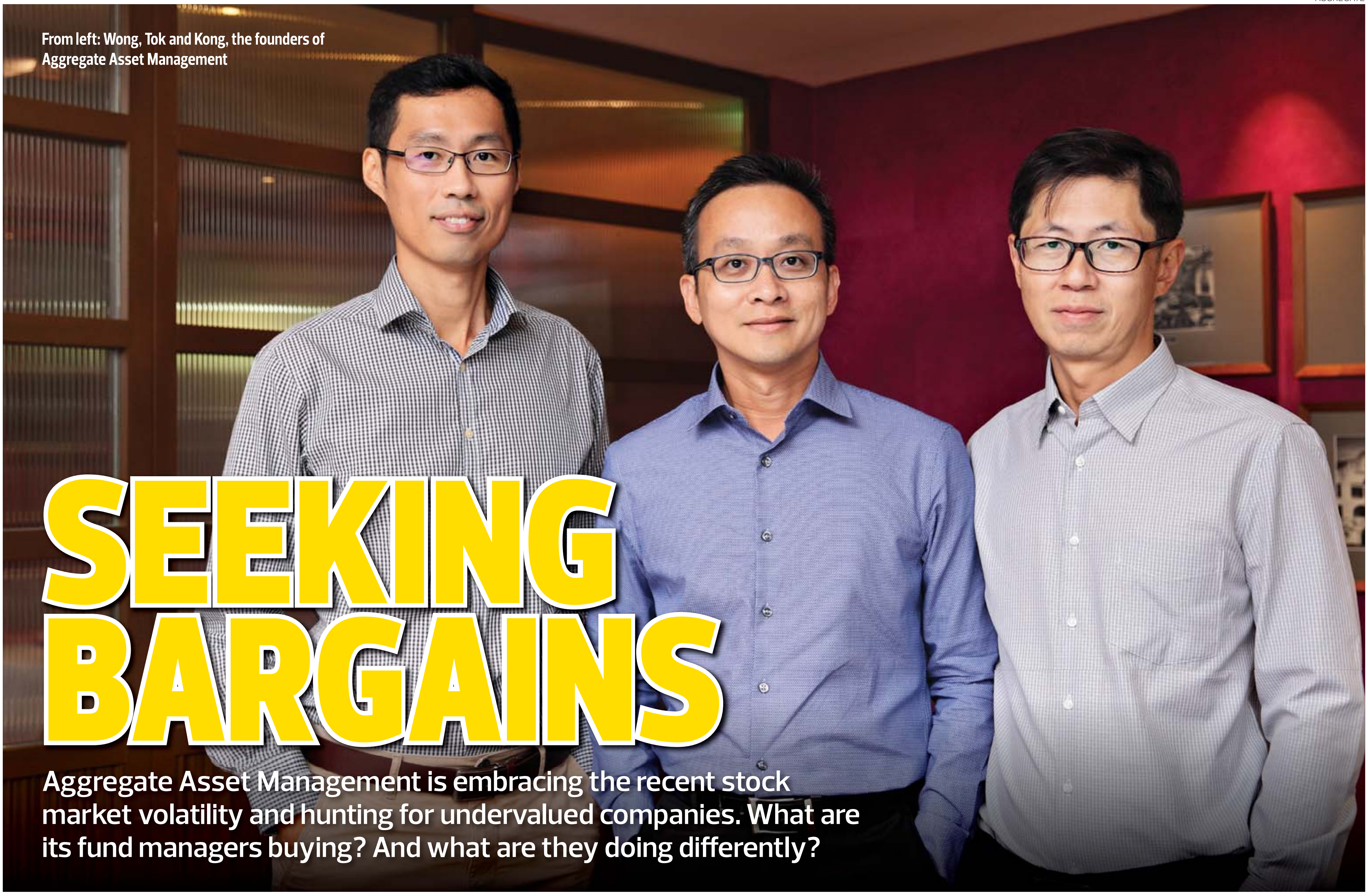

From left: Wong, Tok and Kong, the founders of Aggregate Asset Management

SEEKING BARGAINS

Aggregate Asset Management is embracing the recent stock market volatility and hunting for undervalued companies. What are its fund managers buying? And what are they doing differently?

STORIES **BY TRINITY CHUA**

Global markets have been hit by an unexpected bout of volatility amid concerns that higher interest rates may slow economic growth. On Feb 5, the Dow Jones Industrial Average fell nearly 1,600 points — its biggest intraday decline in history. The day after, Japan's Nikkei 225 index fell 4.7% and the MSCI AC Asia-Pacific ex-Japan Index (MXAPJ) lost 3.4%, its largest drop in nearly two years.

While some investors are panicking about the decimation of their holdings, the fund managers at boutique firm Aggregate Asset Management may be heaving a sigh of relief. Last year's bull run, which sent major stock markets up by double-digit percentages, made it difficult for active fund managers such as Aggregate to beat the index. Its Aggregate Value Fund returned 12.7% in 2017, falling behind the MXAPJ's 30.2%.

In fact, last year was one of the best years for equity investors in a long time. The Standard & Poor's 500 was up 19.4%, the best it has done since 2013. The Straits Times Index gained 18%, its best performance since 2012, and Hong Kong's Hang Seng Index regained its pre-financial crisis high.

Nevertheless, Aggregate believes Asian equities still look attractive. "Overall, the valuation of our fund by price-to-net-tangible-assets is only 0.6 times," says Kevin Tok, executive director of Aggregate Asset Management. "This goes to show that there are still a lot of undervaluation cases in Asia." The Aggregate Value Fund had a net asset value per share of $174.20 as at end-January. The recent selloff may even have created some buying opportunities.

Asian equities currently trade at valuations similar to the levels of 2009, but not at the euphoric levels of 2007, the fund house says. For instance, the Hong Kong market had a price-to-earnings ratio of 23.2 times and price-to-book ratio of 3.5 times in 2007. At end-2009, valuations moderated to a PE of 17.7 times and a PB of 1.9 times. Currently, the Hang Seng Index trades at a PE of 14 times and a PB of 1.5 times.

Underdogs

Founded in 2012 by Tok, a former financial planner, and veteran fund managers Eric Kong and Wong Seak Eng, Aggregate Asset Management has one fund: the Aggregate Value Fund. It holds more than 600 Asia-Pacific-listed stocks, with assets under management (AUM) of $507 million as at end-January. That makes it a minnow in the fund management industry, where firms are getting larger rather than smaller.

Fund management is becoming an increasingly hostile game as investors' dollars pour into exchange-traded funds and other passive instruments. Inflows for ETFs topped a record US$464 billion ($612 billion) in 2017. Mutual funds saw net inflows of just US$91 billion the same year, according to Credit Suisse.

To compete, a few fund houses have merged their operations in search of scale and cost efficiencies. Aberdeen Asset Management merged with Standard Life to form **Standard Life Aberdeen** while Janus Capital Group and Henderson Group combined to form **Janus Henderson Group**. Firms are also launching creative products such as private debt to court investors.

In addition to these challenges, fund houses face new compliance requirements. This year, the revamped Markets in Financial Instruments Directive (better known as MiFID II) came into force. Among other things, it requires fund managers to disentangle trading and research costs. According to the CFA Institute, asset managers say they will now source less research from banks and brokers. Most of them also say the cost of research is expected to rise across all investment types.

Rising costs make it even more difficult for boutique firms to survive. But Kong thinks Aggregate is in a secure niche that will allow it to thrive. "The backdrop of increasing compliance and regulatory costs is an ongoing one. Small firms like ours have to deliver performance and grow our AUM to keep up with the increasing costs," he says. Aggregate's strength lies in its low cost structure. The company does not buy stock research or visit the companies it invests in. It does all its research work in-house. It claims its expense ratio of less than 0.3% is among the lowest for funds in this region.

"What we do is value investing," says Kong. "We don't see a lot of competition here. I think not many people employ this strategy. It requires a lot of patience and discipline."

Uniquely, the fund does not charge its investors an annual management fee. Instead, Aggregate takes 20% of the fund's annual profits if the fund exceeds its previous net asset value record. The fund is only available to accredited investors and has a minimum subscription of $150,000. It aims to produce absolute annual gains of at least 10%, and has managed to do so every year except one. The fund had a dividend yield of 3.5% as at end-December last year.

Kong and Wong used to run boutique fund house Yeoman Capital, while Tok was a manager at Manulife. "We take a long-term investment horizon. If you can compound your money by 10%, you can double your money every seven years," says Tok. "We believe you can beat the average market indices over the long term by holding a portfolio of undervalued stocks." Aggregate holds its stocks for an average period of between three and five years.

Long-term outperformance

This strategy has allowed the Aggregate Value Fund to beat other funds that invest in Asia-Pacific ex-Japan equities by a wide margin over a three-year period (see Table 1). Its three-year return to end-January this year was 33.7%, while its closest competitor gained 15.7% over the same period. It underperforms its peers over a shorter time period, though.

Kong says the fund's short-term underperformance has a lot to do with the way Aggregate runs its fund. "The top performers in the Aggregate Value Fund portfolio delivered 256% [last year], beating the tech stocks' return of 67%," he says in a year-end report to investors. "The problem lies in the allocation. The top-performing stocks in our fund are only allocated 1.78%."

Individual stocks in Aggregate's portfolio typically represent no more than 2% of the fund's total holdings. This is to minimise risk from a single stock crashing. The trade-off is that it is difficult for the fund to outperform the market over the short term, especially when market returns are driven by outsized gains of stocks with significant weights in an index.

"We have seen many funds losing a lot of investors' money from time to time. Many had to close too. The main reason for their demise is usually because they put large amounts of their portfolio into a single idea and borrowed lots of money to do it," Kong says.

'Don't get emotional'

Aggregate's stock selection process begins with quantitative analysis. The managers screen tens of thousands of stocks, narrowing them down to a pool of about 2,000 stocks through a scoring system. They look at indicators such as income, cash flow and dividend yield. The companies are also scored based on valuation

Table 1

MORNINGSTAR DIRECT

Performances of Asia-Pacific ex-Japan funds available to local investors

NAME	FUND SIZE ($ MIL)	YTD RETURN (%)*	1-YEAR RETURN (%)*	3-YEAR RETURN (%)*	STOCKS HELD
Legg Mason MC Asia Pacific A USD Dis(A)	4	3.0	26.6	10.2	52
Janus Henderson Asian Growth	5	3.5	25.6	7.7	NA
UOB United Asian Growth Opportunities	13	3.5	17.7	6.1	47
LionGlobal Asia Pacific SGD	22	6.4	30.3	9.6	43
Threadneedle (Lux) Dev Asia Gr & Inc AUP	31	6.2	26.5	10.1	49
Allianz Asia Pacific Equity A EUR	39	4.8	29.7	9.1	45
Schroder Asian Total Return SGD	39	2.4	28.2	11.7	NA
Janus Henderson Hrzn Asian Growth A2 USD	40	3.6	25.9	8.6	40
LGlobal Fds Asian High Convict Eq L USD	45	6.4	29.5	12.0	42
Nikko AM Shenton Asia Pacific	90	3.6	28.9	7.8	NA
Fidelity Asia Pacific Opps I-Acc-USD	103	1.9	29.2	15.7	31
Legg Mason QS MV APexJ Eq G&I A USDDisM+	111	5.6	20.4	8.1	111
Threadneedle (Lux) Asia Contr Eq ZU	251	6.1	33.3	14.0	55
Emerise Pacific Rim Equity R/A USD	289	1.8	18.0	6.0	46
Eastspring Inv Asian Low Vol Eq ADM	406	3.5	15.1	NA	123
Investec GSF Asia Pacific Eq A Acc USD	480	5.5	38.6	11.7	59
Aggregate Value Fund	507	3.1	14.4	33.7	610
Fidelity Asia Pacific Div A-Dis-USD	609	3.4	21.4	9.4	98
Fidelity Asian Equity S-Acc-SGD	1,384	4.5	31.1	14.3	NA
JPM Asia Pacific Equity A (acc) USD	1,495	5.5	31.5	12.1	79
Aberdeen SP Pacific Eq SGD	1,612	4.6	22.5	6.8	43
First State Dividend Advantage	2,118	4.0	28.0	9.9	NA
Schroder ISF Asian Ttl Ret C Acc USD	5,773	2.5	28.0	11.6	56

** As at end-January 2018*

Table 2

AGGREGATE ASSET MANAGEMENT

A snapshot of the Aggregate Value Fund (as at end-December 2017)

VALUATION	
Dividend yield	3.53%
Price-to-net tangible asset	0.6 times
Price-to-earnings	13.1 times
Return on equity	5.3%
5-year return on equity	6.1%
WEIGHTAGE	
Number of stocks	610
Top 5 holdings	4.7%
Top 10 holdings	8.4%
TOP 5 STOCKS	
Road King Infrastructure	1.26%
Hung Hing Printing Group	0.96%
Oriental Watch Holdings	0.88%
Ming Fai International Holdings	0.84%
Chuang's Consortium International	0.79%
COUNTRY WEIGHTAGE	
Hong Kong	34.79%
Korea	20.54%
Malaysia	11.23%
Japan	7.41%
Singapore	6.82%
Taiwan	6.57%
China-H	6.26%
Thailand	2.81%
Australia, Indonesia, Vietnam	1.23%
Cash	2.34%

metrics such as PE and PB ratios. Tok says the firm looks at more than five years of historical financial performance.

Stocks that make it through this first screening are then analysed in greater detail. Aggregate typically favours companies with net-cash or low-debt positions, as this would indicate a better survival rate when interest rates go up. Now, after five years in operation, Tok says the team is adding more rules to find better bargains.

"When you spread out to so many stocks, individual allocations would be low, which means we can avoid emotional and behavioural mistakes," he says. "We try not to fall in love with each stock, especially to the extent where you keep investing in a stock. Traditionally, when people run a very concentrated portfolio, they put a lot of emotions into a particular stock. If it turns out [badly], it will be a disaster."

Aggregate recently hired three analysts to grow its investment team. Tok hopes this will help the fund uncover other rule-based investing strategies. "We are turning this into a science," he says.

To test its rules, Aggregate will divide a stock market into 10 baskets, based on the specific factors involved. Then, it back-tests these rules to determine the consistency of performance for each basket of stocks over 10 to 15 years.

"We are looking at things such as standard deviation of cash flow over time. If the cash flow is stable [over time], will the stock perform better?" Tok explains. "Another is dividend. If a company that pays stable dividends over many years does a dividend cut for one year, how will it perform a few years later?" The three founders are not above putting their own money into the stock markets to test out new investing rules, Tok says.

But how much does a rule-based fund differ from the numerous smart-beta ETFs that are becoming popular with investors? "What differentiates us from passive smart-beta funds is that we add a layer of qualitative checking and study the financial data of the companies we are investing in," says Wong. "There is info that is hard to filter such as stock buybacks, rights issues and dilution in shares."

Clearance stocks

Aggregates focuses on small- to mid-cap stocks with market capitalisations of between $40 million and $500 million. As at end-December last year, the fund was heavily weighted in Hong Kong and Korean stocks, at 35% and 21%, respectively (see Table 2). About 21% of the fund was in consumer discretionary companies.

Its top five holdings include **Road King Infrastructure**, a toll road and property firm; and printing firm **Hung Hing Printing Group**. Others are **Oriental Watch Holdings**, hotel service provider **Ming Fai International Holdings** and property developer **Chuang's Consortium International**. Most of these stocks had gone through a period of depressed share prices but are fundamentally sound. For instance, Road King's shares collapsed after the 2008 global financial crisis. While they regained some ground, partly thanks to government actions to stimulate the economy, they did not breach their previous highs until last year. Aggregate bought into Road King when it had a market cap of HK$5 billion and a net tangible book value of HK$12 billion. It also had a dividend yield of 7.6%. Today, Road King has a market cap of nearly HK$11 billion ($1.85 billion).

Now, Wong is bullish about the automotive industry in Malaysia. "In Malaysia, we recently allocated more to automotive-related stocks. A lot of people rely on private transport. Every year, the country is adding 600,000 new cars on the road. They also have local plants to export to overseas," he says. The Malaysian economy has been relatively weak, which has affected the share prices of local automotive companies. But Wong expects some recovery this year.

One of his stock picks is **Tan Chong Motor Holdings**, which has a market capitalisation of RM1.1 billion ($371 billion). The company distributes Nissan cars and is involved in vehicle financing as well as property development. "It went through very rough patches [as Nissan car sales slowed in Malaysia], with its share price falling from a high of RM6.62 at end-2013 to the current RM1.77 level. Now, sales are slowly picking up. But the share price has not. The recovery might be because of the product cycle. Nissan hasn't come up with new models for a while," Wong says.

Nissan is launching its electric vehicle Leaf in Malaysia this year. Tan Chong's share price is only 42% of its net tangible asset value, Wong notes. "At the current enterprise value of RM2.5 billion and a dividend yield of 1.1%, Tan Chong Motor Holdings is a potential buy and wait-for-recovery opportunity." In Singapore, Wong says tech bets are not "really value for us anymore". Aggregate invested in **Memtech International** and **Frencken Group**; both stocks have rocketed in recent years. Wong likes pallet maker **LHT Holdings** and electronic components trader **Willas-Array Electronics (Holdings)**, which is also listed in Hong Kong.

Shares of LHT have been dragged down, owing to a drop in raw timber supply. But Wong likes it for its increasing free cash flow and stable balance sheet. Its cash is twice the amount of its liabilities. It is also trading at a PE of 13.5 times and a PB of 0.8 times. It has a dividend yield of 7.5%. "Even in 2008, when there was a crisis, LHT still generated positive earnings, which shows the strength of the company," says Wong. "We believe in buying stocks cheap and that value in itself is a sufficient catalyst."

As for Willas-Array, it is trading below its book value and at a discount to earnings. But revenue has been growing 5.1% annually. "Since 2010, the company has also been paying a steady stream of dividends, with the exception of 2016. The company's dividend yield is 5.3%. The stock is trading at just five times its earnings, which is definitely attractive," says Wong. E

Aggregate's new chairman expects to court new clients for the firm

ALBERT CHUA/THE EDGE SINGAPORE

Mahbubani: The standards that [Aggregate has] set are very high. The way they invest is [never] influenced by who [they] know.

Last September, Aggregate Asset Management appointed Kishore Mahbubani as its non-executive chairman and non-executive director. The boutique asset management firm sees the appointment as one way to court bigger clients to its deep-value fund.

Mahbubani, formerly dean of the Lee Kuan Yew School of Public Policy at the National University of Singapore, also serves on the boards of commodities supplier **Wilmar International** as well as **Zurich Insurance Group** and **Zurich Insurance Co**. He was twice appointed as Singapore's ambassador to the United Nations.

As Mahbubani tells it, Aggregate's fund managers Kevin Tok, Wong Seak Eng and Eric Kong asked him to sign on as chairman about 10 months ago. After some thought, he accepted the offer. "The critical thing is the integrity of the firm [because] the most valuable thing I have is my reputation," says Mahbubani, who is also an investor in Aggregate's Aggregate Value Fund. "If there is any suggestion of a lack of integrity, obviously I wouldn't have joined. The standards that [Aggregate has] set are very high. The way they invest is [never] influenced by who [they] know. They are very impartial and objective in their assessments."

Mahbubani has been introducing friends and associates, who are mainly ultra-high-net-worth individuals, to Aggregate. "To my surprise, every one of the big investors I brought here had never heard of Aggregate," he says. "Aggregate provides a valuable blue-chip option."

Today, Aggregate has more than 500 investors on board. They are mostly high-net-worth individuals with annual incomes of between $3 million and $5 million. The fund recently crossed $500 million in assets under management.

Aggregate is now looking to distribute the fund through banks. "As we now have a five-year track record, we feel the institutions can take us a little bit more seriously. In the past, when we spoke to banks, they would not even entertain [us]," Tok says.

Tok points out that having a bank-based distribution network will help the fund grow and add value to its existing clients. "One of the issues for our clients is the monies they have invested with us are not recognised as bankable assets," he says. "We will be talking to a few banks. We are starting due diligence work with a local bank."

The bulk of Aggregate's fund is in Asian equities, a region that has experienced its fair share of geopolitical tensions in recent years. But Mahbubani is optimistic that Asia will continue to boom. "I'm very optimistic about Asia. The Asian growth story is not one straight line. There will be bumps on the road," he says. "But I'm confident that there will no major war in the region. I've taken bets with the world's best-known journalists that there will be no war between China and Japan. I collected the money the next year. When it comes to geopolitical assessments, I tend to win my bets."