RHB Asset Management

RHB ASIAN INCOME FUND UPDATE – 25 MARCH 2020

Schroder Asian Income Fund (“Target Fund”) Portfolio Update

Source: Schroders, 20 March 2020

Target Fund Performance (as of 20 March 2020)

	Month-to-Date	Year-to-Date
Target Fund (SGD)	-14.0%	-15.6%

Source: Schroders, 20 March 2020

RHB Asian Income Fund (“Fund”) Performance (as of 20 March 2020)

	Month-to-Date	Year-to-Date
Fund (RM)	-13.6%	-15.6%

Source: Lipper IM, 20 March 2020

Target Fund Performance Contribution

Equities were the main detractor from performance (-16%), as concerns over the outbreak weighed on markets and sentiment. While typically stocks with growth exposure would suffer more in normal market sell-off, some of these names have actually outperformed this time especially those in China and for the internet sector. Investors are expecting the impact on corporates in China would be limited as China was the first country hit by the virus, and is also the first which emerge from the trough. For the internet / e-commerce sectors, with more people staying home there is a significant increase in the time spent on the internet, be it for entertainment like gaming and videos or shopping, which could translate into relative stronger, or more defensive, earnings expectation in the current environment.

On the contrary, the traditionally defensive sectors, such as banks and utilities, have suffered in recent market volatility. Banks are suffering from the zero interest rate policies and falling yields around the world, which put pressure on their share prices. For REITs, the brick and mortar nature of their assets mean that investors are expecting rentals to suffer, with the retail sector bearing the brunt given people are not going out to malls. While offices and industrials should theoretically be more resilient given the long-term nature of their rental contracts, they were not spare and also suffered from the broad-based sell-off in the sector. These have had a bigger impact on our performance than in all other sell-offs in the past since inception of this fund (with the exception of the Bernanke shock in 2013) *(Source: Schroders, 20 March 2020)*.

For fixed income, while investment grade remained resilient, high yield suffered with heavy mark to market widening of spreads. In particular, some of the Chinese property developers went down significantly, and the recent profit warning by one of the key developers did not help. The portfolio holdings also experienced volatility as a result, despite our already defensive positioning going into the March sell-off. The current liquidity situation also means that pricing of some of the issues in the index are stale, and might not reflect the exact current pricing that these assets carry. Therefore, we just have to be careful when we look at the performance of the Fund vs the overall broad market performance using index returns.

On a positive note, our hedges contributed +1.0% and helped to offset some losses, highlighting the value-add from our active risk management strategy. Target Fund performance is slightly better given the positive currency effect that our long USD exposure, and the stronger performance of USD assets in SGD terms given the depreciation of the Singapore dollar.

Target Fund Portfolio Positioning

In terms of asset allocation, we have implemented equity hedges since February end through selling -2% index futures on Hong Kong and Singapore. Previously our view was the defensive nature of the equity portfolio and its sensitivity to duration would allow us to keep our position, but given the movement in bond yields and the evolvement in our view, we have decided that we need to reduce the equity exposure in the portfolio. Elsewhere for credit, we added CDS hedges across Indonesia, Brazil and Columbia (-3%). We also trimmed our exposure to EM exposure (through EMAI). Together with the currency hedges on AUD, TWD and SGD that we have implemented, the overall risk level of the fund has been further reduced as overall cash level increased to almost 10%. All in all, looking ahead, we will be cautious and place a strong emphasis on risk management, while continue to look for signals to take advantage of market valuation opportunities to capture returns over the long term.

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Asset Allocation Change Summary

Target Fund (SAI)	28 February 2020	20 March 2020
Equity	57%	49%
Fixed Income	34%	35%
Global	7%	6%
Cash	3%	10%

Source: Schroders, 20 March 2020

Currency Management

Target Fund (SAI)	28 February 2020	20 March 2020
HKD & USD	26.9%	35.9%
SGD	50.4%	46.0%
AUD	9.2%	4.1%
TWD	1.3%	1.6%
Others	12.1%	12.4

Source: Schroders, 20 March 2020

Top 10 Holdings

Our top holdings are REITs / defensive names which offer attractive yields (average yield >5%) and resilience especially during volatile markets.

Top Holdings in Target Fund	Weight	Country	Industry
HK Electric Investments	2.7%	Hong Kong	Utilities
Mapletree Commercial REIT	2.1%	Singapore	Financial
Ascendas REIT	1.9%	Singapore	Financial
Ausnet Services Ltd	1.9%	Australia	Utilities
Power Grid Corporation Of India Ltd	1.7%	Hong Kong	Utilities
Fortune REIT	1.6%	Hong Kong	Financial
Power Assets Holdings Ltd	1.5%	Hong Kong	Utilities
Mapletree Industrial REIT	1.5%	Singapore	Financial
Capitaland Commercial Trust	1.4%	Singapore	Financial
HKT Trust and HKT	1.3%	Hong Kong	Communications

Source: Schroders, 20 March 2020

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Outlook

While our original assessment was that the impact from the Coronavirus would be transitory, the quick deterioration of the situation in Europe and the US means that the impact is likely to be larger than our original expectation. Given the lockdown of borders and cities around the world, the severity of the economic impact is very high, and our economist team has updated their forecasts with an expectation of -3.1% impact on GDP growth this year, bringing the world into a technical recession. The other developments over the last 2 weeks were the unprecedented move by central banks globally in a coordinated manner to provide supportive measures and liquidity via interest rate cuts and quantitative easing. At the time of writing, the US Fed has just announced that they are committed to unlimited QE, and are setting up facilities to purchase corporate credit directly in both primary and secondary markets. In addition, governments have also announced various fiscal stimulus packages to help the economy brace for this heavy impact. However, the markets have failed to react and regain confidence despite all these measures. This is remarkable and it highlights how much pessimism is priced into the market. This also means that in the near-term, markets are likely to remain highly volatile during the bottoming process, and our approach is to tread carefully and focus on risk management.

Over the more medium-term, there are two issues that we will need to monitor closely:

1. The virus situation – we are looking for a decrease in the rate of newly confirmed cases in Europe and the US. This means that we could then start to see the peak of the epidemic, and then investors could then finally have a better grip on how big and severe the economic impact is. This is perhaps the most important thing that we will need watch closely.
2. Unemployment rate and credit defaults – this is more for downside risk management. Investors are still talking about a V-shape recovery given pent-up demands, but whether the recovery is V-shaped and L-shaped would depend on how the situation evolves from here. If the lockdown is short-lived, the plunge in economic activities is temporary then long-term employment should stay intact, and corporate defaults could also likely be averted given all the stimulus. However, the longer this drags on, the bigger the impact on the economy and when it goes to the tipping point, we could see a large scale rise in unemployment with corporate defaults. This would be a point of no return and we are likely to see much bigger losses before recovery.

We still believe the probability of the 2nd scenario is relatively small currently, but we cannot rule out completely the possibility. This also explains our cautious stance currently. Although short-term uncertainty remains high, we also would like to always remind ourselves that in the midst of all these volatilities and negative headlines, it is very easy for us to lose sight on the more medium-term trend. We should all recognize that we are now back into a zero interest rate environment with the system awashed with liquidity from central banks from all over the world. Very naturally, once things start to stabilize, investors will restart their search for income, and the assets in the portfolio with a current yield of about 5% is likely to be attractive for investors again.

For equities, we expect earnings forecasts to be adjusted downwards in some areas. Industries that are most vulnerable to the COVID-19 shock are manufacturing, gaming, tourism and consumption/travel-related industries (retail, airlines etc.) as they have borne the brunt of the demand shock as travel-related activity has dramatically reduced. At the same time, the sharp pull-back in markets in recent days is starting to throw up more interesting value opportunities. While still early days, we believe that the extraordinary fiscal measures could potentially translate into investments which ultimately could lead to stronger demand for commodities, while some technology or consumption related companies also now offer some interesting yield even after adjusting for earnings and dividend cuts.

Similarly, for credit, widening spreads have presented concerns and opportunities for investors. For us, since we entered into the sell-off with a relatively defensive portfolio, we have preserved some dry powder for us to deploy and pick up some attractive opportunities in the high yield space. As mentioned, near term given the uncertainty of the situation, we are not moving yet back into the asset class, but we are actively looking for opportunities now and would look to gradually add back to some of the more solid names which got punished unproportionally. For example, some of the mega cap names with strong government support in China in the materials and property sector now offer high double digit yield, which to us is getting close to a level where the valuation is justified for the risks of these papers.

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A Product Highlights Sheet ("PHS") highlighting the key features and risks of the RHB Asian Income Fund ("Fund") is available and investors have the right to request for a PHS. Investors are advised to obtain, read and understand the PHS and the contents of the Prospectus dated 6 October 2017 and its supplementary(ies) (if any) ("the Prospectus") before investing. The Prospectus has been registered with the Securities Commission Malaysia who takes no responsibility for its contents. Amongst others, investors should consider the fees and charges involved. Investors should also note that the price of units and distributions payable, if any, may go down as well as up. Where a distribution is declared, investors are advised that following the issue of additional units/distribution, the NAV per unit will be reduced from cum-distribution NAV to ex-distribution NAV. Any issue of units to which the Prospectus relates will only be made on receipt of a form of application referred to in the Prospectus. For more details, please call 1-800-88-3175 for a copy of the PHS and the Prospectus or collect one from any of our branches or authorised distributors.

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