Investment Ideas and Solutions – Leaders Discuss Markets & Strategies

The discussion began with a focus on risk management, with an expert remarking that he has been spreading the word on risk management developments that have been taking place in recent decades and how the Asian market is adopting the latest techniques. He noted that the past two years in Asia had provided a textbook case for risk management, with 2017 beginning as if it would be risky, but risk turned out at historical lows, while 2018 began with an early flourish and then went straight down for the rest of the year.

These were the topics discussed:

- *How deeply have events in the US, such as the government shut-down, the trade wars and geopolitical factors affected companies and markets?*
- *The outlook for US Small and Mid-Cap Equities.*
- *The outlook for global equities.*
- *How will global monetary policy affect the markets this year?*
- *Is gold rising or falling in portfolio formation? Paper gold, or physical?*
- *The search for yield.*
- *New money-market and other funds in Hong Kong.*
- *What is the demand for ETFs and other passive funds in Asia?*
- *Will Asian equities perform in 2019?*
- *Risk management to improve investment performance and downsize the downside.*
- *Are diamonds an asset class, should they be in wealth portfolios?*

PANEL SPEAKERS

- **Sally Ryder**, Managing Director, Ryder Diamonds
- **Thorsten Becker**, Senior Fund Manager, J O Hambro Capital Management
- **Harold Kim**, CEO, Neo Risk Investment Advisors
- **Tobias Bland**, CEO, EIP
- **Steven Cohen**, Chief Investment Officer, CBM Investment Management
- **Joshua Rotbart**, Managing Partner, J. Rotbart & Co.

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THE KEY TAKEAWAYS

Risk management requires systems and actions

The past two years in Asia have provided a textbook case for risk management, with 2017 beginning as if it would be risky, but risk turned out at historical lows, while 2018 began with an early flourish and then went straight down for the rest of the year. Nobody can predict risk changes exactly, but the important element is to asses it systematically and adjust portfolio exposures accordingly. No action is not an option.

Diamonds - be selective

Diamonds are not a commodity as they cannot be standardised into a weight or other category and therefore there can be no price index. Selectively, coloured diamonds have performed remarkably well in the past five years, while white diamonds have seen a glut driven by India's massive investment in cutting and polishing facility in the past 10 years.

Gold - a store of value and a safe haven

Gold should be a core holding in any HNWI family portfolio. It is a long-term store of value, it has performed at least as well as equities since it was delinked from the US dollar in 1976 and it is a non-correlated asset that in physical form can be stored outside the global financial system. It is a hedge against dollar weakness and inflation, and it remains both a scarce asset and is highly liquid in all formats. If economies are up, people buy gold for jewellery, if things are weak, it acts as a hedge.

US economy appears solid

The US economy is strong, the regulatory burdens are diminished - lower corporate taxes at 21% since January 2018 and other regulatory adjustments - and the investment climate is therefore a lot better. The smaller and medium-sized companies, the lifeblood of the economy, are therefore enjoying a considerably more business-friendly environment. Tweets and politics aside, it would appear that the US markets are alive and well under Trump.

Fiscal matters appear conducive

The US fiscal situation is still positive, the monetary situation is still accommodative, even though we have higher rates now they are still low in a historical context and with a supportive regulatory environment, this all appears good for risk assets. However, be wary of inflation lurking and for the Fed to reverse its position again and tighten. Avoid leveraged companies.

"HOW THEN," HE ASKED, RHETORICALLY, "do you recognise that the environment has changed, and then how do you respond, systematically to reduce the risk? And that is exactly what we are trying to do, we are trying to be systematic. There are many different approaches to this, but the key message is that any kind of risk management is better than no risk management. If you do nothing, that's not risk management."

He then elucidated by noting that the market collectively is rather smart and therefore what his firm does is build statistical models that look at past behaviour to try and link that to what is happening today. "I am always the first to admit, we don't catch the first big downdraft, but it is vital to have in place a process to react when changes in risk happen, and if you react appropriately, you will outperform the markets."

He added that having been in the markets for more than 30 years, he never remembers waking up with absolutely no worries. He said there are always events, always surprises and one can never accurately product the future, but one must make sure to react to events and market vacillations.

Cautiously optimistic, for now

"I am not in the business of predicting return," he added, "but, we think equity markets are going to be okay this year, in particular Asian equity markets because current accounts look good,

THORSTEN BECKER
J O Hambro Capital Management

TOBIAS BLAND
EIP

growth is still higher than other regions in the world, and valuations are fair. We are therefore fairly cautiously optimistic about Asian equities, but other equity markets globally are at different parts of the cycle, with the US being ahead, so that is where we think the risk will show up first, when earnings start to decline. However, for now, we think it is okay now that the macro situation has settled at a different level."

The discussion then migrated to diamonds. "Not many people know much about diamonds," this expert commented. "Trust and integrity are therefore vital."

She explained that diamonds are not a commodity, because there is no standardised quantity and therefore as a result there can be no price index. "Even when a diamond is graded with the colour and clarity and cut, polish and symmetry there are still bandings of price," she remarked, "and what influences the price of diamonds in the market is supply and demand. If there are indexes they don't truly tell the actual wholesale or retail value of the diamond."

Choose your stones carefully

She reported that over the past year diamond prices have been fairly steady, although over the past five years they had depreciated at least 30%. "There has been a flood of diamonds into the market, beginning for example in 2009 when there was a large investment for the Indian diamond manufacturers, supported by the Indian government, including huge diamond polishing factories, but the result was a glut."

She explained that she was referring there only to white diamonds, but that certain classes of diamonds had in fact appreciated some 40% year over year in the last five years, particularly blue diamonds. "In general, I believe market conditions will improve and we will see increasing prices in general in the coming years."

Gold – multi-faceted merits

The panel turned their attention to gold, with an expert advising on the merits of gold as an investment. Price levels are currently reasonable for entry currently and we know that over time gold outperforms most other assets and is therefore a core holding in many HNWI family

SALLY RYDER
Ryder Diamonds

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portfolios. He also noted that gold within an investment portfolio has a direct relationship to reducing the volatility of the portfolio, as a non-correlated asset.

"People buy gold as a hedge, it is very liquid market and it is scarce," he added. "When the economy is good, people buy gold in the form of jewellery and when the economy is bad people buy it as an investment as a hedge to protect themselves against inflation. These are the major incentives to buy gold."

As to the price, he said he is wary of forecasts, but that looking back in history, since gold was separated from the US dollar [in 1976] it has performed roughly in line with equities at around

10% per annum and has done much better than commodities, bonds or cash over the medium to long term. "Having said that, in the current environment globally, we anticipate gold staying around the current USD1350 level, but on the medium to long term we are still very bullish."

Another expert added that gold is outside the global financial system, further enhancing its value as a safe-haven asset.

The discussion moved to product opportunities, with an expert highlighting a Chinese convertible bond fund. "There is a pipeline of around USD300 billion similar paper coming in the next two years," he reported, "and it coincides with the opening up of the China's capital market, which is where we see an opportunity to achieve alpha."

As an aside, the same panellist remarked that opaque fees such as trailer fees or retrocessions persist in Hong Kong. "You can see a much greater appreciation of assets in Australia, for instance, since they changed that rule over there, and personal wealth has increased much quicker because there are lower fees for the banks. I am surprised the Hong Kong regulators do not simply ban these fees."

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STEVEN COHEN
CBM Investment Management

HAROLD KIM
Neo Risk Investment Advisors

US economy and markets: good for now

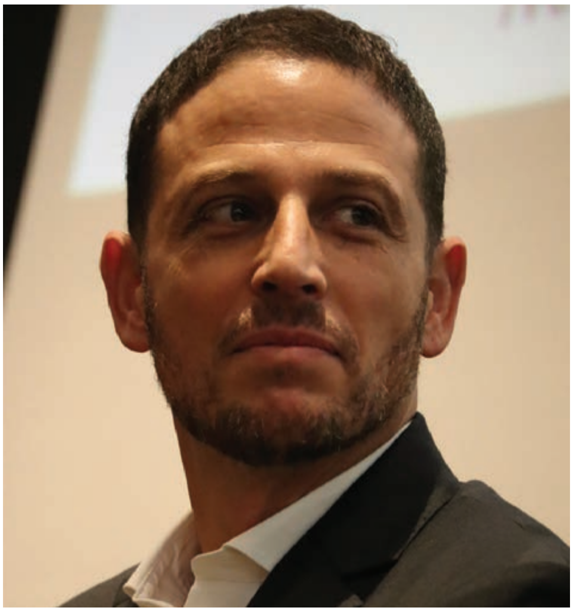
An expert assessed the current state of the US economy, maintaining that investors should ignore the tweets and recognise that the economy is strong, the regulatory burdens are diminished, and the investment climate is therefore a lot better. "Specifically, when I talk to smaller and medium-sized companies, they say it is just a much more business-friendly environment."

He added that the government shutdown had not noticeably impacted the underlying business climate, which remains quite positive.

The same expert highlighted the appeals of the smaller and medium-sized companies, noting that 80% or more of the revenues of most of these companies are domestically sourced. Tax reform has also helped them, as well as the regulatory burdens being lifted. "The multinational companies generally have all kinds of optimisation structures and loopholes that allow them to pay much lower effective tax rate, but for these smaller companies the actual rate coming down to 21% [from January 2018] is a huge benefit."

Turning to politics, he remarked that Trump's presidency had not resulted in the chaos detractors had said would materialise. "The US is a very mature democracy," he noted, "with many checks and balances and voters, the US markets can live with whatever election results emerge."

Another expert added: "The US fiscal situation is still positive, the monetary situation is still accommodative, even though we have higher rates now they are still low in a historical context. The regulatory environment is very supportive of equities. This should be a good environment for risk assets. However, we are facing potential increases of inflation which means the current monetary policy is probably just a pause and further tightening will eventually resume, probably this year. Domestic US equities like many of the smaller companies in the US are better positioned, but avoid leveraged companies, which could be troubled if the rate cycle resumes."



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