APS ALL CHINA LONG SHORT (CAYMAN) FUND

FUND DETAILS

Structure	Open-ended	
Domicile	Cayman	
Inception date	1 July 2008	
Base currency	USD	
Fund size	USD74 million	
Number of Holdings	60	
Lead Manager	Wong Kok Hoi	
NAV Prices at 30th Sep 2018	Class A	USD246.54
	Class B	USD89.60

SUBSCRIPTION

	Class A	Class B
Bloomberg	APSCHIN KY	APSCHIB KY
Liquidity	Weekly	Weekly
Min investment	USD100,000	USD100,000
Lock Up Period	Nil	Nil
Management fee	2%	2%
Performance fee	20% with 8% Hurdle Rate p.a	20% with High Water Mark
Subscription deadline	3pm (Singapore time) 4 Business Days prior to the relevant Subscription Day	
Redemption deadline	3pm (Singapore time) 4 Business Days prior to the relevant Redemption Day	
Redemption fee	Up to 3%	
Subscription fee	Up to 5%	
Legal advisers	Walkers (Cayman) Yuan Tai Law Offices (SG) Rajah & Tan LLP (China)	
Auditor	Deloitte & Touche	
Administrator	HSBC Institutional Trust Services (Singapore) Limited	
Prime Broker	UBS AG	

STRATEGY DESCRIPTION

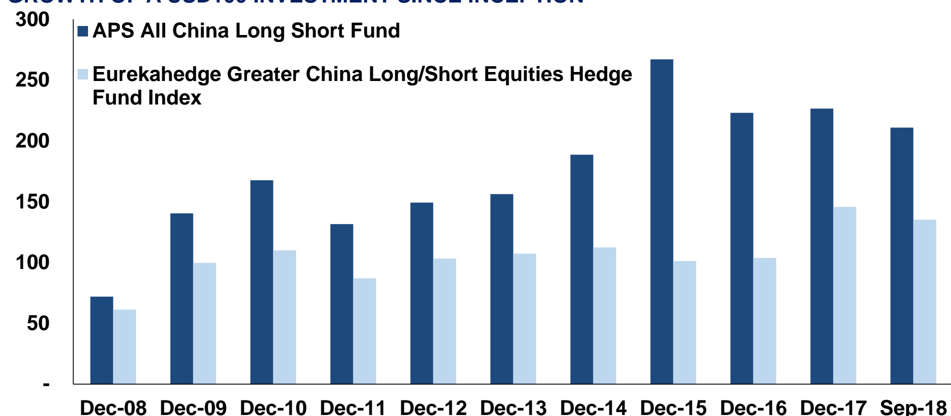
The APS All China Long Short Fund (ACLSF) invests in stocks of companies established or operating in the People's Republic of China that are listed on exchanges in China, Taiwan, Hong Kong and Singapore. The fund seeks to generate alpha from both its long as well as short positions. Our emphasis is on risk-adjusted returns, and avoiding a permanent loss of capital when we make our investment decisions. We invest in companies with strong management teams and durable growth prospects at attractive valuations. The fund sells short stocks of companies with dubious or weak business franchises, and yet are over-valued, especially if they are run by incompetent or dishonest management. We conduct primary research on company fundamentals, which includes members of the management teams, and adopt a strong investigative slant. Site visits and meetings with management form an important part of our research work. We seek to achieve annualized double-digit returns for our investors over a market cycle.

PERFORMANCE AS 30 SEPTEMBER 2018

					Annualized Returns (%)		
	1M	3Q	YTD	1Y	3Y	5Y	Since Incept.
ACLSF Net Returns	4.83	-0.80	-6.89	-4.60	-3.60	6.03	7.56
Eurekahedge Greater China Long/Short Equities Hedge Fund Index*	-2.42	-8.63	-8.91	-3.66	6.61	7.98	7.71
Difference	7.25	7.83	2.02	-0.94	-10.21	-1.95	-0.15

Performance of the Fund is represented by the asset weighted performance of the Class A and Class B share classes. The Fund is not managed against a benchmark, and the Index is only shown as an illustration. All performance quoted represents past performance and is no guarantee of future results. Current performance may be lower or higher than the return figures quoted. The fund returns are net of all fees and charges.
**Based on 3.39% of funds which have reported September 2018 returns as at 5th October 2018.*

GROWTH OF A USD100 INVESTMENT SINCE INCEPTION**



***Current investment team structure implemented in Jul 2008*
Fund returns are cumulative and are net of management and performance fees.

COMMENTARY

The Fund was down 0.80% net-of-fees in the quarter 2018, while the Eurekahedge Greater China Long/Short Equities Hedge Fund Index was down 8.63% during the same period.

China has taken a tougher of late in countering the Trump Administration's assault on Chinese exports, with Vice Premier Liu He cancelling his trip for trade negotiations in September. China's sense is that there would probably be little real progress from any trade talks before the November US mid-term elections. China would be better served by focusing its energy on maintaining a healthy domestic economy.

To that end, China's Finance Minister Liu Kun in late September indicated that proposed 2018 cuts in government taxes and charges would total CNY1.3 trillion, higher than the target of CNY1.1 tn set out in early 2018. As an incentive, tax cuts for R&D-intensive enterprises were also boosted. There is also speculation among investors that the Value Added Tax may be cut to 13% from the current 16%.

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TOP FIVE HOLDINGS (%)

LONG	
Kweichow Moutai^	10.8
Venustech Group^	9.9
Beijing Orient National	6.4
Gree Electric Appliances	6.3
Shenzhen International	6.1

SHORT	
China Con. Discretionary^	-11.0
Hong Kong Con. Discretionary	-9.4
China Con. Staples	-7.3
Hong Kong Con. Discretionary	-6.9
Hong Kong Con. Discretionary	-4.9

COUNTRY WEIGHTS (%)

China A	73.2
China Others	-29.4
Hong Kong	-20.8
Taiwan	0.7

SECTOR WEIGHTS (%)

Info. Technology	24.3
Consumer Staples	11.2
Industrials	9.9
Health Care	4.7
Financials	3.5
Materials	2.6
Comm. Services	-0.3
Energy	-1.7
Con. Discretionary	-10.3
Futures	-20.2

MARKET CAP (%)

> USD 5 Bn	-5.7
USD 2 – USD 5 Bn	31.5
USD 1 – USD 2 Bn	16.2
< USD 1 Bn	2.0

EXPOSURE SNAPSHOT (%)

Gross	156.6
Net	23.7
Long	90.1
Short	-66.4

^ Due to price movement
Sources: APS, Bloomberg and Wilshire

While the actual extent of tax cuts is unclear at the moment, the trend for government policy is clearly tilted towards promoting innovation and domestic consumption. These have become the main drivers of Chinese economic growth.

Domestic consumption showed some signs of a moderate recovery in August, with retail sales growing 9% YoY, which was 20 basis points higher than in July. Fixed asset investment decelerated, growing 5.3% YoY YTD end-August, 20 basis points lower than the first seven months. The slowdown was mainly due to muted infrastructure spending, which declined -4.3% YoY in August, indicating the central banks' policy of de-leveraging is taking effect.

During the month, global index provider FTSE Russell moved to incorporate China A shares into its indices. The inclusion will start from June 2019, with an initial weighting of 5.57% in its FTSE Russell Emerging Market Index. The weight will increase in two further steps, slated for September 2019 and March 2020. MSCI in late September launched a consultation on a further weight increase of China A shares, following the successful implementation of the 5% initial inclusion between May and August 2018. The proposal, if implemented, could boost China A shares' weight in the MSCI Emerging Markets Index from 0.71% to 2.8% by August 2019 and to 3.4% by May 2020. The three core proposals are: increase the inclusion factor of the 235 China A Large Cap shares from 5% to 20%, bring 168 China A mid-cap shares into the index at a 20% inclusion factor, and admit the ChiNext board in Shenzhen to the list of eligible stock exchange segments.

Our short position in a **Chinese e-commerce company** with ADRs was one of the top contributors in 3Q18. The company's 1Q and 2Q18 results were below street estimates as its margins remained depressed and it struggled to generate profits. Analysts are now expecting continued margin pressure due to the company's investments and the sustained industry-wide pricing pressure from incumbents like Alibaba and new players like Pinduoduo. In early September, the company's CEO was briefly held in custody on suspicion of criminal sexual misconduct in the US. No charges have been filed yet, and US authorities have not announced the outcome of investigations. The stock price has come under considerable pressure since the story broke. We are closely monitoring developments on this front, which has brought into focus some of the corporate governance issues that we have highlighted in the past.

Our short position in the premium-focused **Macau gaming operator** was a top contributor 3Q2018, as the share prices dropped while industry GGR continued to miss expectations. This trend started in May amidst market's concern over the slowing GGR arising from the stock market crash, a slowing property market, and the deteriorating business environment in some sectors. Investors are beginning to worry about the public tender for the casino concession, which is a huge risk. The company has absolutely no equity, as the dividend payout ratio had been about 100% in recent years

Our short position in a **Chinese F&B Company** contributed strongly to the portfolio, mainly driven by the significant share price correction in August. This was led by an overall correction in the sector due to market fears of an economic slowdown in China and continued weak fundamentals at the company.

We think the sector correction was somewhat healthy, as valuations were pricing in unrealistic growth expectations. Fundamentally, we believe the market has realised the company's price-hike- led margin improvements are not sustainable. We note the company continues to lose market share to key competitors like Uni-President China in premium noodles and beverages, specifically Ready-To-Drink (RTD) Tea. This reinforces our view that the company is not yet participating in the longer term premiumisation trend. We hold on to our investment thesis that the company is currently exposed to the mature mass segment as well as declining segments of the noodle markets. It is unable to grow and defend its RTD tea franchise in the face of stiff competition from its peers.

The company recently shared their beverage strategy of focusing on their loss-making bottled water franchise, which we feel is structurally challenged. This is a poor allocation of the company's resources given its much lower returns on invested capital. This is not the first time the company has tried to turn this business around, and we therefore remain less sanguine on its success. We will continue to track the company's strategy closely to look for signs of change, but for now, our investment view on the company remains.

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Midea Group was a detractor for the quarter, despite its 1H 2018 results meeting market expectations with net income that was up 19.7% and topline growing 14.6%. However, recent sell through data indicates slowing sales for Midea's key products like air conditioners, which decelerated to 17.5% YTD end-July from 20% at the end of the first half. Other segments such as small appliances also saw significant slow-down.

Venustech Group's share underperformed the CSI 300 Index by about 9 percentage points in 3Q 2018 after the company clarified that its FY earnings growth guidance was only around 8%, instead of an expected 30% increase mentioned in an earlier announcement that included one-off elements. This revised figure was below market expectations. Its 1H earnings report also showed that after stripping out the accounting gain from the change in accounting methodology for equity investments, its recurring net loss was CNY68 mn, deteriorating from CNY24 mn a year ago. While orders from some other sectors grew an aggregate 35% YoY, new orders from the military did not improve in 1H. However, revenue from high entry barrier urban security operations surged to CNY50 mn, and could contribute CNY200 mn to the 2018 topline. We expect this service offering to make a meaningful contribution to the company's topline growth in coming years, as well as improve the company's overall cash flow profile.

Beijing Orient National detracted from performance during the quarter, dragged lower largely by weak 2Q earnings. Its 1H results showed topline growth of 5.78%, and bottom line growth of only 2.48%, which was at the low end of company guidance. This was mainly the result of delay in revenue recognition and the initial startup cost of about CNY50 mn for its industrial internet business. Many investors have high growth expectations for this segment as well as the government sector, but both showed sluggish growth during 1H due to a delay in revenue recognition. The growth rates for both segments are expected to recover during the second half.

BJ Oriental can look forward to a boost in winning orders due to its inclusion in the cross-industry national platform that has strong backing from the central government. With some help from Huawei, the company is already booking new orders in Beijing, Shanghai and Zhongshan. We are staying invested as we expect BJ Oriental to meet its earnings growth guidance of around 30%, which makes the 23x 2018E P/E valuation reasonable, on top of its entrenched position in the rapidly growing market of big data application software.

RECENT NEW POSITIONS

We have initiated a short position in an **online auto finance and marketing service provider** in China. We believe that the company's business model is weak and its management has very limited competence in growing the business. China's auto industry is facing a slowdown in demand this year, and at the same time the cost of funding is increasing for this company. Additionally, we also expect a higher delinquency rate this year, which will further reduce its earnings. Our research suggests that the current valuation still does not fully incorporate the headwinds that the company is facing.

We established a position in **Shanghai Fosun Pharmaceutical**, a healthcare conglomerate that mainly manufactures pharmaceuticals, but also invests in for-profit private hospitals. It also holds a 27.83% stake in China's largest pharma distributor Sinopharm. We expect new business drivers like Biosimilars and CART-T will accelerate growth over the next 3 to 5 years.

Over the next 3 years, its pharma manufacturing business is expected to deliver 15% CAGR, while Fosun's pharmaceutical distribution affiliate Sinopharm is expected to grow at 8% CAGR. Its new business in Biosimilars will likely see its first drug approved during FY2018, and it also holds a 71.38% stake in Henlius which is expected to be listed in Hong Kong in the coming months. Fosun also has a stake in Gland Pharma, which it will use as its platform to break into the lucrative US market. On top of all this, Fosun has a CAR-T therapy joint venture with Kite Pharma, and an early stage pipeline in small-molecular targeted drugs.

RECENT EXITS

We exited **Shenzhen Sunway Communication** as the company might not be able to sustain its earnings growth of over 50% during the next 2 years due to fierce competition in the areas such as wireless charging, shielding, and filters. The valuation was stretched at of 33x 2018E P/E, which was a 25% premium to the sector average.

China's tariff hike on petroleum imports from the US prompted us to exit our position in **Zhejiang Satellite** on heightened earnings risk, despite 2Q earnings recovering from 1Q weakness as production resumed. The company's margins might suffer as it uses imported ethane as feedstock for its ethylene business.

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The representative of the Fund in Switzerland is ARM Swiss Representatives SA, Route de Cité-Ouest 2, 1196 Gland, Switzerland. The paying agent of the Fund in Switzerland is Banque Cantonale de Genève, 17, quai de l'Ile, 1204 Geneva, Switzerland. The Memorandum, the Fund's Memorandum and Articles of Association and the Fund's annual and semi-annual financial statements can be obtained free of charge from the representative in Switzerland. The place of performance and jurisdiction of the Fund in Switzerland is the registered office of the representative in Switzerland with regards to the Shares distributed in and from Switzerland.

Unless otherwise stated, all information is as of 30th September 2018 and sourced internally from APS

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