Horizon Asia Opportunity

Q4 2021 Commentary

February 2022

In the fourth quarter of 2021, the Horizon Asia Opportunity Institutional Composite (the "Strategy") declined 3.4%, net of fees, compared to the MSCI All Country Asia Index (the "Index"), which declined 2.2%. The Strategy's holdings in system integrator and network service providers in Japan contributed positively. Internet service companies and entertainment content owners in Japan detracted from performance. During 2021, the Strategy gained 1.2%, net of fees, while the Index declined 2.3%.

The final quarter of 2021 was a difficult one for the Asian equity markets. As noted above, the Index declined 2.2%, underperforming the MSCI All Country World Index, which rose 6.7%. For 2021, the Index was down by 2.3%, while the world index gained 18.5%. The main reasons for Asia's underperformance were weak returns in China, Japan and other Asian developed markets such as Singapore and Hong Kong. Resource heavy markets such as Australia and Indonesia fared better. In general, Asian economies are energy consumers rather than energy and natural resources exporters, with exception of Australia, Indonesia and Malaysia. The US dollar's strength was also detrimental to returns in the Asian equity markets.

	Total Return	
	Q4 2021	FY 2021
MSCI Japan	-0.88%	13.79%
MSCI China	-5.93%	-21.22%
MSCI Hong Kong	-3.42%	-3.41%
MSCI Taiwan	7.72%	24.75%
MSCI Phillipines	3.68%	2.53%
MSCI Korea Index	-0.14%	0.20%
MSCI India	0.00%	28.86%
MSCI Indonesia	6.18%	4.26%
MSCI Malaysia	1.30%	-2.90%
MSCI Singapore	-4.04%	7.84%
MSCI Thailand	1.73%	10.25%
MSCI Australia	1.67%	17.99%
MSCI AC Asia Index	-2.20%	-2.28%

Source: Bloomberg. In local currency, except all country index in USD

The Chinese market continued its decline during the fourth quarter by falling 6.1%, as measured by the MSCI China index. The real estate sector was hit especially hard during the second half of 2021. This is a continuation of the fallout from the Three Red Lines policy introduced in August 2021, which pushed many highly leveraged real estate developers such as Evergrande and Fantasia into well publicized financial difficulties. At the same time, political pressure on the Chinese internet/technology companies, especially those listed abroad, such as Alibaba, continued. All of these events increased uncertainty and led some international investors to call the Chinese equity markets non investable.

China is going to hold 20th National Party Congress in November 2022. It is widely expected that Xi Jinping will be elected as president for a third term. In order to make this process go smoothly, we expect the

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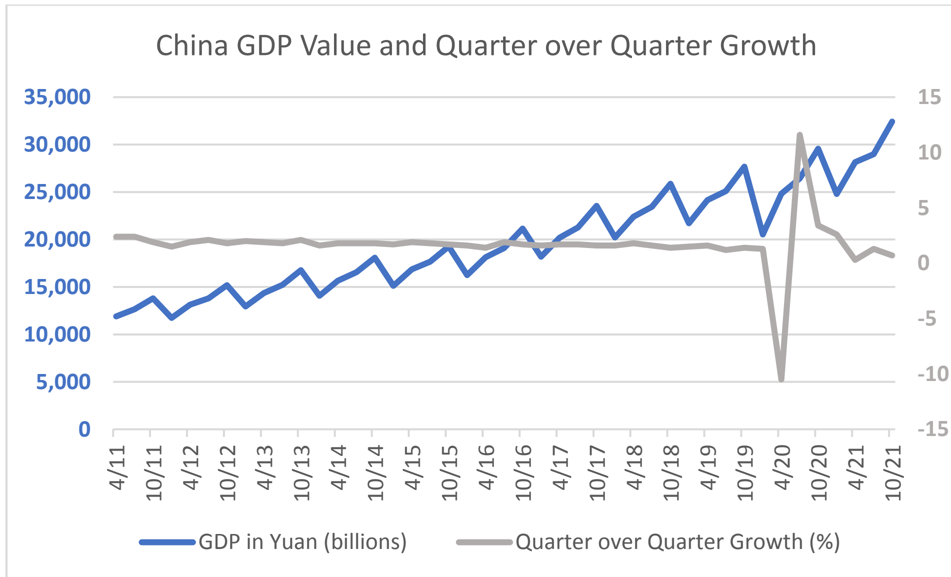
Chinese government to engineer a stable domestic environment both politically and economically. The first order of business in 2021 was to contain the spread of COVID by employing draconian measures such as closing the borders of infected cities such as Xian. This was followed by Beijing where the Winter Olympic were to be held. These strict measures and real estate woes caused a further slowdown of the domestic economy; in the 4th quarter, real GDP growth was 4.0%, and 8.1% for full year 2021.



Source: Current Price Gross Domestic Product in China, Chinese Yuans, Quarterly, Seasonally Adjusted; Organization for Economic Co-Operation and Development via Federal Reserve Bank of St. Louis. GDP Constant Price QoQ Growth; National Bureau of Statistics of China via Bloomberg

To counter the economic slowdown, The People Bank of China (PBOC) lowered the one-year loan prime rate to 3.8%, down from 3.85% in December 2021. This was followed by another 10 basis point cut to 3.7% in January 2022. In addition, PBOC lowered its 5 year prime loan rate by 5 basis points, the first such cut since April 2020. However, this does not mean that China wants to go back to a hyper-growth economy fueled by easy monetary policy.

Rather, we tend to look at all of these macro and micro policy changes as part of Chinese president Xi's long term plan to move the country back to a Chinese Communist Party-led (CCP) socialist dictatorship with more stable growth and "common prosperity" for the masses, closer to What Chairman Mao was envisioning initially before the personal cult of Mao made the outcome very different from this ideal. This is a clear departure from the reformist policy that Deng Xiaoping and Zhu Rongji were contemplating, with term limits for the highest office and economic reform driven by inviting foreign capital and technological advances from the West. Therefore, we expect that pressure on hyper real estate developments based on easy credit will continue and the dominance of Chinese internet/technology companies will erode.

We believe Xi will also focus more on building a domestic supply chain without a heavy reliance on the West, and will continue to accumulate natural resources overseas to secure a stable supply to China.

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These major changes in China's longer term direction indicate that the inflationary pressures created by the Covid pandemic will not be eased so quickly.

We expect the Chinese economy to overcome some short-term, self-induced headwinds, and eventually establish a better balanced model of growth. The most important macroeconomic factor on China's side to achieve this goal is its very high savings. Gross National savings peaked at around 50% in 2010 but was still at 44% in 2019.

Due to their underperformance in 2021, the Asian equity markets are still trading at relatively attractive levels compared to the rest of the world. The dividends yields for the MSCI Assa Index is currently at a 2.5% level, which is higher than the yield on local 10 year government bonds or the US 10 year government bond. This characteristic is very defensive in nature and bodes well for Asian equity markets' relative return prospects. The only significant risk is a further US dollar rally, which would depress Asian asset returns in US dollar terms. We have been avoiding investing in the Chinese equity markets and sidestepping the potential negative impact on our Asia Strategy portfolio. At the same time, we believe it is important to be open-minded and keep our eyes on developments there to see if there are attractive investment opportunities in the future.

Global Valuation Comparison

	P/E FY22e	P/E FY23e	P/B FY22e	EV/EBITDA FY22e	ROE FY22e	Div Yield FY22e (%)	10yr Bond Yield Current
Japan	13.7	12.6	1.2	8.3	9.2	2.3	0.2
China	12.5	10.8	1.6	12.4	11.1	2.2	2.8
Asia ex-Japan	14.0	12.4	1.8	10.5	11.5	2.5	NA
US	19.7	17.9	4.4	13.5	22.6	1.5	2.0
Europe	14.5	13.4	1.8	9.3	10.2	3.0	0.6

Japanese universe is TSE 1. Chinese universe is MSCI China Index. US universe is S&P 500. European universe is STOXX Europe 600. Asia ex Japan universe is MSCI AC Asia ex-Japan Index. As of 2/17/2022.
Source: Bloomberg

IMPORTANT RISK DISCLOSURES

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The MSCI All Countries Asia Index® captures large and mid-cap companies represented across 3 Developed Markets countries and 8 Emerging Markets countries in Asia. With 930 constituents, the index covers approximately 85% of the free float-adjusted market capitalization in each country.

The MSCI China A Index measures large and mid-cap representation across China securities listed on the Shanghai and Shenzhen exchanges. The index covers only those securities that are accessible through "Stock Connect".

The S&P 500® is widely regarded as the best single gauge of large-cap U.S. equities and serves as the foundation for a wide range of investment products. The index includes 500 leading companies and captures approximately 80% coverage of available market capitalization.

The STOXX Europe 600 Index is derived from the STOXX Europe Total Market Index (TMI) and is a subset of the STOXX Global 1800 Index. With a fixed number of 600 components, the STOXX Europe 600 Index represents large, mid and small capitalization companies across 17 countries of the European region: Austria, Belgium, Denmark, Finland, France, Germany, Ireland, Italy, Luxembourg, the Netherlands, Norway, Poland, Portugal, Spain, Sweden, Switzerland and the United Kingdom.

TOPIX is a free-float adjusted market capitalization-weighted index that is calculated based on all the domestic common stocks listed on the TSE First Section. TOPIX shows the measure of current market capitalization assuming that market capitalization as of the base date (January 4, 1968) is 100 points. This is a measure of the overall trend in the stock market and is used as a benchmark for investment in Japanese stocks.

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