

## REVIEW OF 1999 AND OUTLOOK FOR 1H2000

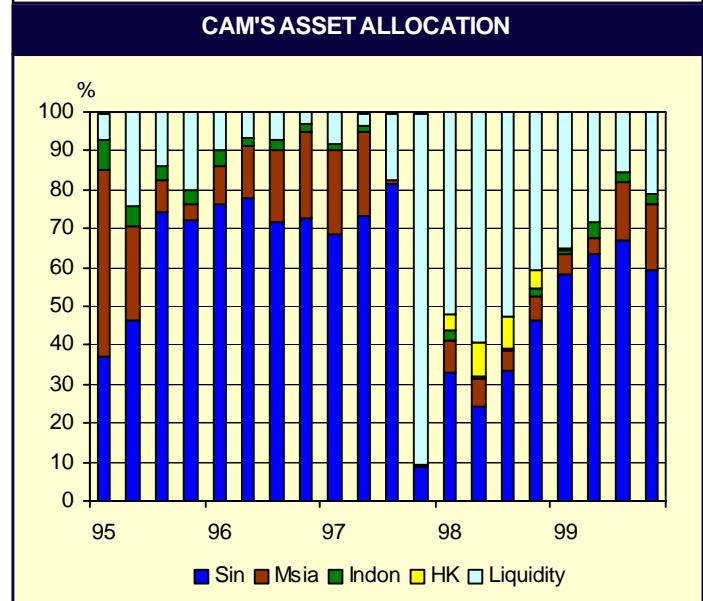
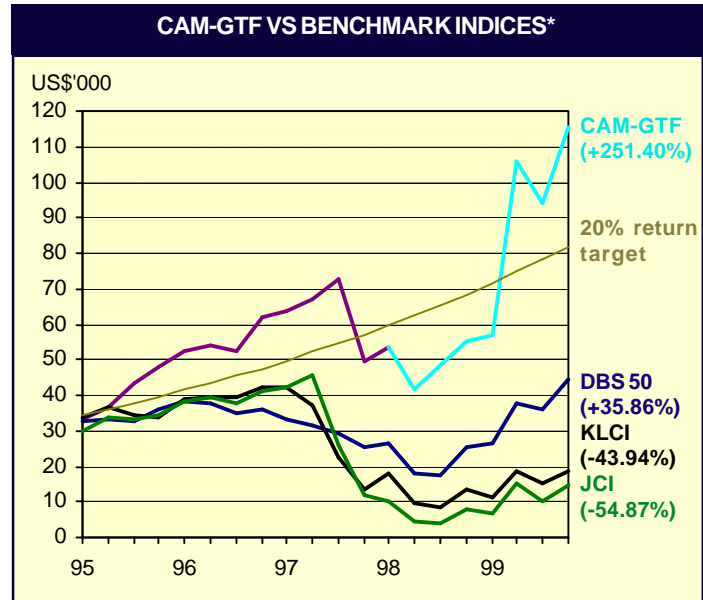
### PERFORMANCE

#### A v-shaped recovery

The Singapore, Malaysia and Indonesia markets bounced back with a sharp recovery in 1999, retracing much of their losses from the 1997-8 contagion (before accounting for currency losses), and crossed Y2K without a glitch.

CAM's flagship fund, CAM-GTF, whose base currency is in US\$, more than doubled, returning a stellar 108.4%, compared with the DBS 50, the KLCI, and the JCI gains of 75.5%, 38.6% and 94.0% respectively (US\$ rebased). The bulk of its gains was achieved in the first half, when the markets were trading at more attractive valuations and hence risks were lower. Nonetheless, the fund continued to improve with a 8.9% gain HoH, outperforming two of its three benchmark indices for the period.

While end-December is typically a window dressing period for most funds (where key investments are pushed up to dress up the end-value of portfolios), by contrast and governed by our sell discipline, we sold some of our positions into the market's strength. Consequently, our cash position rose to 21% of NAV compared with 16% at the end of 3Q99. We will look to re-invest the cash on either market declines or when there are investment opportunities that offer high returns at low risk. As mentioned in our previous newsletters, the cash proportion of the Fund is determined by our ability to find value in the market.



INDICES (US\$)	4Q99	QoQ (%)	HoH (%)	YoY (%)
<b>CAM-GTF*</b>	<b>115,615</b>	<b>23.2</b>	<b>8.9</b>	<b>108.4</b>
DBS 50	494	23.5	18.1	75.5
KLCI	214	20.3	0.1	38.6
JCI	10	47.0	-2.0	94.0
INDICES (LOCAL CURRENCY)	4Q99	QoQ (%)	HoH (%)	YoY (%)
<b>CAM-GTF* (S\$)</b>	<b>192,383</b>	<b>20.7</b>	<b>6.6</b>	<b>109.0</b>
DBS 50 (S\$)	822	21.1	15.7	77.2
KLCI (RM)	812	20.3	0.2	38.6
JCI (Rp)	677	23.5	2.2	70.1

## OUTLOOK FOR THE MARKETS

Y2K worries have dissipated, but our concern remains with rising US interest rates, with the 30-year long bond rising above its historical 5 year average of 6.4%. Commodity prices continue to stay firm, and oil is still above US\$25 per barrel. The growth in monetary base ahead of a dreaded Y2K melt down scenario, of which some spillage has gone to push global markets higher towards the end of the millenium, will be reabsorbed by central banks around the world. While US equity markets have up to now largely ignored rising rates, we believe that eventually, equity markets will revert to its traditional inverse relationship with interest rates i.e. a rise in interest rates will lead to a fall in equity prices.

What does this have to do with Asian equities? From our observation, the Asian equity markets are driven to a large degree by foreign monies. Equities are now yielding significantly less than the long bond, implying a risk discount for what is historically viewed as a higher risk asset class.

High valuations suggest a near term correction. Asia is likely to see a more bumpy road ahead, especially being vulnerable to higher cost of funds, and with domestic consumption still not strong enough to head off any potential slowdown in exports.

On the bright side, as more Asian currencies are freely floating, central banks have more freedom to chart their own economic course. All Asian economies according to consensus forecasts, will enjoy positive GDP growth, albeit at a slower pace than in the rebound phase of 1999. Asian companies continue to rebuild their balance sheets, shedding loss making subsidiaries and improving return on equity although this remains a very slow process. Nonetheless, post the 1997-98 crisis, Asia offers superior earnings growth prospects in comparison with the US, and currencies are expected to strengthen vis-à-vis the US\$. As such we remain optimistic in the longer term. Asia will continue to be a manufacturing force for the world's consumers and in the next few decades it shall grow to become the consuming force as well.

### Singapore



Singapore had a very good run, and significantly exceeded the previous high achieved pre-Asian contagion. The market was buoyed by a confluence

of positive factors: better economic prospects throughout the region, and hence an improved earnings outlook which attracted a wave of liquidity. Singapore was also perceived as the most attractive market in South East Asia for most of the year with Malaysia partially closed and other countries still beleaguered by weak banking systems. In the last quarter, the wave of optimism was powered by Nasdaq and dot.com companies.

More importantly, which of these factors remain relevant in the new year? The economic backdrop is favourable, with strong external growth and a recovery of the domestic sector. However the scope for earnings surprises or upgrades is limited. Liquidity is also switching in favour of Malaysia, particularly with valuations becoming increasingly stretched here. Optimists support their argument for further rises by benchmarking to US valuations, specifically for technology companies but we are averse to doing this, and are wary of the market's vulnerability to external shocks. We would be buyers into any significant correction, but at these levels, see limited opportunities.

### Malaysia



The Malaysian stockmarket, despite the implementation of capital controls in September 1998, put in a creditable performance in 1999. However, most of the gains occurred in the first half of the year; the second half returned only 0.14% on the back of election jitters. Fortunately, the ruling party, Barisan Nasional (BN), retained its two-thirds majority. However, closer analysis reveals that all is not well with the ground swell. The pro-business sector, including the majority of the Chinese, voted for status quo, but a fairly large number of Malays swung towards the pro-Muslim faction, Parti Islam Se-Malaysia (PAS). These voters were clearly expressing their dissatisfaction with the incumbent party and its practice of cronyism.

Amidst Malaysia's much acclaimed self-styled recovery from the Asian crisis, the key question to be asked is "has Malaysia reformed along with the rest of Asia?" or phrased another way, "what has changed?" Capital controls did lend stability to exporters and they prospered. But more importantly, interest rates were driven down to their lowest level in years. Predictably, domestic monies with little alternative ploughed whole-heartedly into the stockmarket, reigniting the paper reflation cycle once again. This insular approach contrasts with the

restructuring efforts seen in Korea and Singapore, both of which have won foreign investor support. Taking a medium to long term view, if Malaysia remains cloistered, its industries will fast lose their competitive edge and they will not be in a position to compete globally.

away at these old corporate dinosaurs. It has reached a point where such reform will require much capital, and we are likely to see several large state sales through a privatisation programme in the coming year. Early indications are that around US\$20bn will be raised through listings in Hong Kong alone.

## Indonesia



The Indonesian stockmarket proved to be one for the stout-hearted, epitomising the phrase “high risk, high returns” with the Jakarta Composite Index roller-coasting to a final gain of 94% in US dollar terms. It was an eventful year for the country, culminating in the election of its new president in October 1999, with Abdurrahman Wahid taking the post. His election is best summed as the combined result of negotiated favours and compromises, evident in the composition of his cabinet. This is hardly meant as a criticism; for a culture as deeply rooted and complex as Indonesia, change takes time. Unfortunately, time may not be on Wahid’s side. The 59-year-old Mr. Wahid has suffered at least two strokes in recent years and is nearly blind. This change in Government may in future, be viewed as the turning point and a new beginning for Indonesia. For now, the road ahead is still a rocky path and a high premium must be accorded for the risks involved compared with less trying opportunities available elsewhere in the region.

## China



WTO entry looks all the more likely with the blessing from the US, and the implications of WTO entry to China is enormous. China’s risk premium will be reduced as the regulatory and legal framework is clarified. In short, it will play by international rules. The immediate impact of opening its doors to trade will be the harsh discovery of more imports, and that could put pressure on the Yuan, particularly if current account surpluses turn to deficit. Industrial production in China could fall as less efficient producers lose out to imports. Policymakers face the dilemma of balancing the need for reform against possible mass social unrest. The policymakers know what needs to be done, but are held back by the harsh reality of unemployment, and the lack of a social security system as well as private sector employment opportunities. Nonetheless, State Owned Enterprise (SOE) reforms are still on the cards, and the government will chip

## Hong Kong



Hong Kong will be a major beneficiary should China join the WTO. In many ways, it will complement China’s needs through the service sector. Amongst others, China has underdeveloped banking, insurance, fund management, telecommunications, and retail sectors, whereas HK derives 85% of its GDP from such service driven sectors. That is not to say Hong Kong will not try to reinvent itself. The recent attention paid to internet related businesses and the large market capitalisation accorded to such start ups are sure signs that investors want to move away from the traditional staple of property companies and banks. We are, however, cautious given current valuations in the internet industry.

## Taiwan



The Taiwan Straits last saw significant Chinese military exercise with the firing of live missiles four years ago, just ahead of Taiwan’s general elections in 1996. That was when the Taiwan Weighted Index touched a low of just above 4500. Whether China will go through the same motions again this March, when Taiwan has its general elections, remains to be seen. This time, the index stands at above 9500, and we still have the lingering issue of an uncertain “State to state” relationship with China. Politics aside, Taiwan continues to have a thriving electronics industry, despite the earthquake in September, and unless the pro independence party wins a majority, investors should look to opportunities in that sector.

## Korea



Korea is amongst our top picks within the region. GDP growth is likely to top 7% this year and next, the highest in the region. Korean corporates took the bitter medicine and restructured during and after the Asian crisis. Some failed and went bankrupt, leaving the fitter

survivors. Unemployment which went close to 8% at the height of the crisis, is now below 5%, and heading towards the 15 year average of below 3%. Industrial production continues its sharp increase, and average factory operation rate is back to pre crisis levels. All this is occurring with the Won much cheaper against the Dollar and the Yen than pre crisis. As a result the surplus enjoyed through exports continues to swell. The Daewoo crisis is not all behind us, after 8th February 2000, certain categories of investors can redeem Daewoo instruments at 5% discount, compared with 20% currently. This is part of the government's plan to avoid a major slump in bond prices. It remains to be seen how well the system will cope with the coming redemption.

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## Thailand



As we move into the reporting season for Thai Banks, it will be clear to any analyst that much needs to be done. There is still a lot of red ink and the banks are still dealing with non performing loans. Coupled with the lack of credit worthy borrowers, this makes monetary expansion unlikely. The economy is unlikely to see private sector demand play a significant role until 2001, in the meantime it is still the public purse keeping the economy afloat.

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## Philippines



The government has been following a Keynesian model of fiscal expansion in the hope of stimulating the rest of the economy. This has caused a rising budget deficit, which is running very close to 4% of GDP in 1999. The private sector appears slow to respond. The government's ability to fund the deficit will eventually be put to the test, and taxes might be raised or reformed. This remains uncertain, but the way the deficit is funded will have a dramatic impact on interest rates.

## STRATEGY FOR 2000

Our investment discipline pays heed to the rise in US interest rates. We have consequently reduced our positions which has had the effect of improving the overall P/Es of the portfolio, while maintaining our weightings in companies with good growth rates and low P/Es. This methodology has proven fruitful in 1999, even taking into consideration that the fund was on average, only 70% invested. The present cash position provides us with the ability to capitalise on good opportunities that arise, be it in the form of a market correction, new discoveries or IPOs. We are mindful of not being too conservative by constantly reminding ourselves that money only grows when it is put to work. The expansion in geographical coverage for the fund puts us in good stead to discover new investment opportunities for greater returns.

## CORPORATE DEVELOPMENT

Our readers will be familiar with our proposal for a joint venture with Mr CY Lee, as part of our plan to broaden our geographical coverage. This joint venture will now not proceed, as finer details could not be reached to the satisfaction of all parties. Mr Lee will leave CAM HK at the end of January 2000, and we wish him the very best in his endeavours.

We remain committed to expanding our geographical mandate, as we believe the rest of Asia offers many investment opportunities and attractive growth prospects. However we are also mindful of the risks and will continue our strict discipline of stringent company research before embarking on any investment. We are not unfamiliar with investing beyond our immediate shores. Indeed, more than 30% of our portfolio are in companies with dominant operations in HongKong/China. We intend to expand at a measure pace, keeping to our philosophy of hunting for growth but at the right price.

### ***\* Calculating the Flagship Fund's Performance***

*Readers of our past newsletters would have seen references to CAM's flagship fund which chartered a respectable 3 year track record (31/12/94 – 31/12/97), returning a cumulative 50.63% in US\$ terms and 71.67% in S\$ terms, despite a corporate tax burden of 26% per annum on realised gains. The flagship account was subsequently restructured into the CAM-Growth Triangle Fund (CAM-GTF) at the beginning of 1998. CAM-GTF now represents our single largest account, with a tax structure comparable to other offshore funds, and thus better suited as a flagship fund to establish our track record. The charts and table on page 1 represent the previous flagship fund's 3 year performance plus CAM-GTF's performance since 01/01/98 with numbers rebased to CAM-GTF's NAV per share.*

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