# A better tomorrow

*Hedge fund managers this year were spared the dramatic market movements of 2011, but nevertheless faced challenges. Managers from a cross-section of strategies relate their experiences and provide their outlook for 2013.*

*As told to Yvonne Chan*

**CHINA RE-RATING: KYU HO, WUZHU ASIA PARTNERS**
**Pan-Asia long/short equity**

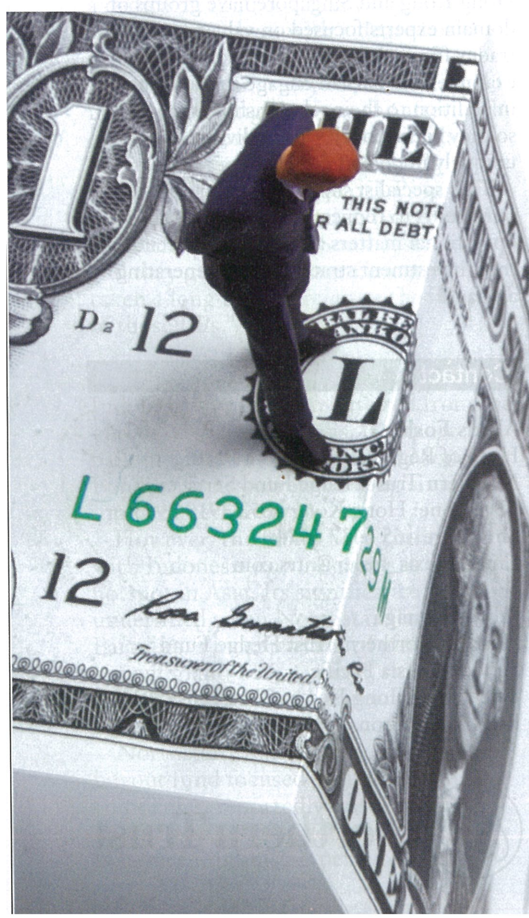
By and large, we did not find any major market surprises this year with fundamentals, which were in line with our expectations. However, we were surprised by how well the market received the news of the European Central Bank's bond-buying scheme and US Federal Reserve's launch of quantitative easing, or QE3, in September. We saw a re-rating on the market without necessarily seeing a follow-through on earnings.

The best market opportunities for our long positions this year were in some Southeast Asian countries, where domestic consumption is the main driver of their economies. For our shorts, we found interesting opportunities in structurally weak companies in countries such as Japan, Korea and Taiwan.

The challenge this year was avoiding value traps: assets that look very cheap but in fact might not be recovering any time soon, so the stocks stay cheap. However, we did identify companies that are very cheap because of cyclical reasons and were a bit more comfortable with, as we believed that the cycle would pick up.

Next year will be interesting. The market consensus is that the Chinese economy has stabilised, with some early signs of recovery, and the market has re-rated to reflect this. We do not anticipate strong earnings growth based on our on-the-ground research. However, the market does not look expensive if you believe in the earnings. There is definitely room to re-rate, especially for H-shares, though the extent would greatly depend on the market's confidence in earnings as well as the growth trajectory.

Whether the US economy can exhibit more robust signs of an economic upturn and the eurozone can work through its sovereign debt issues will remain the key question marks going into 2013.



*Will the US fall off the fiscal cliff?*

**POLICY FEARS MODERATING: GOVERT HEIJBOER, TRUE PARTNER**
**Global volatility arbitrage**

The theme for us this past year was about finding opportunities in volatility spreads between indices around the world. We were long volatility exposure in Asia, and short in other parts of the world. That's worked quite well for us.

We were generally neutral on volatility because we tend to do much better when markets are panicky, as the opportunities tend to be much larger. Frankly, that did not happen this year. We had downturns, but not in an extreme, panicky way.

There was, it seemed, a persistent fear in the market that something would happen. The US was facing a fiscal cliff and debt ceiling, and the Europe Union had problems with Greece. I found it surprising that there seemed to be much fear in the US market, despite the fact that it did go up quite a bit this year.

As we trade global arbitrage opportunities, it becomes interesting for us when market behavior is somewhat different in Europe and the US than in Asia. We can capitalise on it by engaging in volatility spreads. On average, people in Asia are a bit less fearful on what's going in the other parts of the world, perhaps a bit more optimistic.

Next year, it's possible that there will still be quite a bit of fear in the markets, which will subside slightly if nothing materialises.

There is the looming fiscal cliff in the US, but I think that will very likely be a 'kick the can down the road' event because probably at some point, a compromise will be found. Further down the year, however, there will likely be a debt-ceiling crisis again in the US.

The probability of dramatic events is somewhat low but there could be events that shock the markets. Europe seems somewhat under control, but if something emerges from the shadows, the situation could very quickly change. For example, there's not a lot of talk about the UK. The economy is not doing so well, but you don't hear much about it because the attention is on the euro.

In Asia, market sentiment might be even more positive next year, if China takes extra measures to stimulate the economy. Nowadays, compared to a few years, ago, market movements are more politically driven in the sense that there's much more direct impact from decisions by politicians. Therefore, it's much less predictable.

**CRACKS IN LUXURY PLAYS: EDDIE TAM, CENTRAL ASSET INVESTMENTS**
**Multi-strategy**

Europe is hanging in there, although there's a range. Germany is stellar, up 26%; the rest isn't bad overall.

Hot money started flowing back into Asia, particularly to Hong Kong and China, from the end of the Q3 and it's been driving up the markets. This is more or less how we saw it last year, but in between there were a lot of headline macro worries. Navigating through it was more difficult than predicting it.

China's property sector did very well. We were very bullish on Chinese property bonds and correctly predicted that they would not fail, at least not the large listed ones. Real-estate transactions have rebounded very healthily this year and prices are stable.

What surprised us was the sustainability of some luxury retail plays. Burberry and Mulberry started to crack; these are European-listed but are sometimes regarded as surrogate Asian plays. Other luxury brands have been very resilient. For example, Prada, which is listed in Hong Kong, has been going from strength to strength. I've found the stock to be quite expensive, but shorting it would not work.

In first half of next year, there won't be any change in Europe, but in 2H2013, the ball will be back into the political court. It will depend on how Germany works it out.

As the Americans are terribly conservative, they view the fiscal cliff as being imminent, when in actuality it's not. I predict that second term of [President Barack] Obama will start to address that issue. Once he does that, it's possible the economy will slow even further because it will involve less government spending, but the market may reward it with a higher price-to-earnings ratio. It's short-term pain, but could be better for the long term.

**A NEW BULL RUN: WONG YU LIANG, LUMIERE CAPITAL**
**Asian deep value**

This year has been a good year to buy stocks at cheap prices, with 2012 marking the continuation of a bear market that began in 2011. We managed to find several bargains, especially in the Hong Kong market, with many stocks having fallen more than 60% from their peak prices in 2011.

In 2012, markets were seemingly trading with a very short-term outlook, with few participants looking deep into the fundamentals of each company. Stocks of companies have moved up and down in tandem with sector or country sentiment, without paying heed to the individual merits of each business.

As bottom-up stock pickers, this gave us plentiful opportunities to acquire cheaply priced stocks of companies with strong, growing businesses that happened to be operating in countries and sectors that were out of favour.

We predict 2013 will be a good year for stocks, because valuations are low and the earnings of many businesses – especially in Greater China – were hard-hit in 2H2011 and 1H2012. Expectations have also become more realistic compared to the heady days in early 2011, and we are likely to see an earnings recovery starting from end-2012 onwards.

We have found more bargains than we have money to invest in. The availability of plentiful cheap stocks today reminds us of the conditions in late 2002-early 2003, when stock prices declined substantially over a long bear market after the internet bubble burst. Earnings started recovering from a low base, eventually spawning a multi-year bull market.

**A CREDIT MELT-UP: ROBERT APPLEBY, ADM CAPITAL**
**Distressed debt**

This year we have experienced a credit melt-up. Right across the credit curve, you have had record demand met by record issuance. Nothing will stop the lesser credits jumping in on the game; some have tried, a few have failed.

The hunt for yield globally is on. In the zero-rate interest world, it's not just New York and London calling to buy Asian credit. Places like Seoul, Tokyo and Beijing are also looking for yield. Asian credit holds a premium to credit elsewhere and investors are harvesting that premium.

We've always been extremely careful about where we play on the credit curve. We may choose not to play at all. For a long time we felt that the choice has to be made carefully and we are reducing our exposure to public credit as we speak.

Looking ahead, we have long held the view that investors will be rewarded for the extra work needed in private credit markets. Companies that need cash, and don't have the luxury of tapping into the public debt markets, will have to get it elsewhere. This is where private credit can play a role. ■


*Luxury brands are sometimes seen as surrogate Asian plays*