

# Fund managers rethink strategies

## Oil price crash forces them to adjust their portfolios

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**F**UND managers' strategies on oil and gas related stocks are varied amid a weak crude oil price trend although they say that the impact on their portfolios thus far has not been major.

Some have already made certain changes to their portfolios, switching to stocks from other sectors and taking a hit, some are holding onto their investments.

There is also the mix strategy of waiting for good buys in anticipation of more dips and considering exits from their oil and gas exposure if the crude oil turmoil shows no signs of abating.

Of course, their decisions also vary from market to market.

Notably, the Malaysian market is among the worst stock-market performers in the region year-to-date, down more than 6%.

As a contrast, China markets are up 30% on average.

Lower energy costs is generally favourable to equities but the Malaysian market is an exception due to the much favoured oil and gas sector here, points out Thomas Yong, chief executive officer at fund management firm Fortress Capital.

Lower revenue from the country's oil and gas exports because of the decline in price has raised questions on the Government's ability to fund its fiscal budget and the recent weakness of the ringgit serves to exacerbate concerns of foreign investors, he notes.

Still, most fund managers surveyed say impact has been minimal on their respective portfolios.

### Switching stocks

"Generally, our portfolios have declined about 6.5% in value since oil started to come down drastically in June," says Danny Wong, fund manager at Areca Capital which invests mostly in the Malaysian market.

The impact is rather minimal since we were underweight on the bigger local oil and gas firms for their high valuations since the second quarter, we focused on the mid-small cap service-oriented players, he says.

"As a tactical move, we are switching from one oil and gas stock to another just to keep the beta low."

Wong says Areca has also switched to stocks from other sectors like insurance and utilities since the rapid decline of crude.

He feels that amid the current oversupply of crude globally which is the main reason for the fall in the price, demand for the commodity will not be an issue, moving forward in line with increasing population and wealth especially in high-growth countries like China, Indonesia and India.

Wong also points out that alternative energy is rather costly and capital intensive and therefore, not able to be a major threat over the next few years.

"We're now looking at some over-sold high beta local names."

"We have seen many cycles and this round it is not a crisis, recession nor is it due to geo-political issues."

He believes what's happening is temporary and "the dust will settle".

"As a long term investor, I will take advantage of the market movements as per the famous quote - buy when there is blood



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**Tan:** The fall in oil price has very limited impact on us as our cash levels for both our local and global funds are very high.



**Yong:** What investors really need to brace for is the increased volatility of prices going forward.

running on the streets, but be cautious and do your homework."

### Mulling over an exit

Capital Dynamics founder and managing director Tan Teng Boo, who manages about RM1bil worth in global funds, may exit the one overseas oil and gas investment that his house has while for the other overseas alternate energy stock that it is invested in, he says that although its price has fallen sharply, "we are still recording profits and holding on to it for the longer term."

For its global funds, Capital Dynamics' main exposures are to the London and Hong Kong stock markets.

As for his Malaysian investments, Tan, well-known for his value-investing strategies, says there is no exposure to the oil and gas sector whatsoever.

"We have zero cut-loss here and are cash-rich, we are watching but not buying yet."

Tan has been bearish on markets since the end of last year and warns that there is more downside to come, stemming mainly from the rich valuations in the local market, the New York Stock Exchange and NASDAQ, to name a few.

"Reinforcing our worries is a US monetary policy that is highly opaque and confusing and where the Federal Reserve keeps shifting its monetary goal posts."

"Overall, the fall in oil price has very limited impact on us as our cash levels for both our local and global funds are very high."

### Holding on

For Fortress Capital's Yong, holding on to its oil and gas investments is the strategy for now.

Yong, who co-founded the fund management firm which invests in regional stocks, says it has less than 5% exposure to the sector, largely in Singapore.

"As our current positions are in large and financially resilient oil and gas operators trading at single digit forward earnings, we are

inclined towards holding onto our existing positions, he says.

New positions in the sector will be added only with better crude oil price visibility, Yong says, adding that his portfolios currently comprise mainly of China banks.

"While prices in Singapore have not been spared, the impact is significantly muted because of the much lower valuation levels there and our smaller position."

He says the Malaysian oil and gas industry has for the large part of the year been the most favoured sector domestically due to Petronas' large outsourcing expenditure.

"The equity prices in this sector had performed strongly and as a result our interests had shifted to other sectors."

Like Wong, he opines that although supply conditions of oil and gas have shifted as a result of US and Canada's expanded oil supply from shale gas, other global demand supply conditions and the costs of production have not dramatically changed.

"Assumptions based on these factors easily justify eventual recovery above US\$80 per barrel for Brent."

"What investors really need to brace for is the increased volatility of prices going forward."

Gerald Ambrose, managing director of Aberdeen Asset Management, declines to elaborate on what kind of an impact declining crude has had on the fund management house's investments.

"Our strategy remains the same, buy well-managed stocks at the right price, in fact, some of the oil and gas stocks are at attractive valuations already."

### Buying into niche companies

Meanwhile, in his most recent blog posting, emerging market guru and the executive chairman of Templeton Emerging Markets Group Mark Mobius offers some consolation in the wake of the current crude oil saga, noting that some oil fields in Malaysia have "very low cost" (of production), as well

below US\$50 per barrel.

"Therefore, lower oil prices don't necessarily mean companies in the sector will be unprofitable," he writes in the Dec 3 posting.

The 78-year-old Mobius who spends a good part of his working life travelling to emerging markets to discover economic potential says it is important to stock-pick in Malaysia, where valuations have been higher than in some other Asian markets, while at the same time, performance has generally been somewhat disappointing.

He advocates buying into the utility and consumer sectors to ride on Malaysia's long-term goal of becoming a high-income country but warns of a few bumps that could impact this vision.

"As investors, we have to maintain a long-term view and focus on companies we feel can survive and prosper amid changing conditions, and that fill an interesting niche."

Mobius says Templeton also looks out for companies that have the potential to serve consumers not only in Malaysia but throughout the region, and even globally.

The price of Brent crude, the global benchmark has collapsed to below US\$70 per barrel, the lowest in four years and is about 37% down since the beginning of the year.

The drastic drop, made worse by The Organization of Petroleum Exporting Countries' recent decision to not slash production has had chain effects, including affecting other commodity and currency markets worldwide.

No one knows for sure when prices will stabilise again but some analysts are predicting that they will go down by another 10% to 15% by the end of the year amid weakening global economies.

Some of the oil and gas stocks on Bursa Malaysia that have been beaten down in the past three months include SapuraKencana Petroleum Bhd, Bumi Armada Bhd and Dialog Group Bhd which are trading about 50%, 143% and 31% off their respective 52-week peak prices.

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