Value hunter

Kenanga Investors Bhd chief investment officer Lee Sook Yee's diligence and thorough research process have helped her discover small and mid-cap gems — and outperform her peers in the industry.

BY **KUEK SER KWANG ZHE**

Lee Sook Yee has had an eventful ride since she assumed the role of chief investment officer at Kenanga Investors Bhd in March 2013. In just under three years, she has boosted the firm's reputation as a formidable player in the local asset management industry.

Under her stewardship, Kenanga Investors' retail assets grew more than RM1 billion last year. She also helped the firm launch its first internally managed regional funds.

These achievements did not happen by chance. Lee is known among her peers as a sharp stock picker. She is also a disciplined value investor.

"Kenanga Investors and I have the same value investing philosophy, so we are a good match. When I assumed the role [of chief investment officer], I was already familiar with the processes — this is very important. I am very diligent and disciplined when it comes to conducting research," says Lee.

It was her thorough process that helped her discover some investment gems in the small and mid-cap space. For instance, she was one of the earliest to buy into Inari Amertron Bhd and IFCA MSC Bhd, which eventually led to her equity funds outperforming.

The clearest indication of her success is her management of the Kenanga Growth Fund, her firm's flagship fund, which invests in Malaysian growth stocks. "When I joined about three years ago, the fund had about RM100 million under management. Now, it has RM600 million," says Lee.

"The fund delivered a return of 21% in 2015 versus the FBM KLCI's decline of 4%. In 2014 and 2013, the fund rose 9% and 26% respectively, substantially outperforming the market's return of -6% and 10% respectively over the same period," she adds.

Under Lee's management, the Kenanga Growth Fund has won the award for Best Malaysia Equity Fund (over 3-year period) at The Edge-Lipper Fund Awards for the past three years.

As at Jan 29, the Thomson Reuters Lipper Leaders showed that the fund had generated a return of 117.44% and 380.03% for the five and 10-year period, outperforming the other 148 equity funds in Malaysia. The second best performer was the Eastspring Investments Dana al-Ilham fund, which saw a return of 78.31% and 268.24% for the five and 10-year period respectively.

Lee studied economics at the London School of Economics and Political Science and later obtained a master's degree from the University of Cambridge. After graduation, she worked as a sell-side analyst before eventually transitioning to a buy-side analyst.

Over the next 10 years, she progressed quickly in her career, becoming a portfolio manager with UOB-OSK Asset Management and then vice-president at Credit-Suisse Asset Management in Singapore, where she co-managed funds that focused on emerging Asian markets. She was head of equities at local boutique asset management firm Meridian Asset Management before assuming her current role at Kenanga Investors.

The year 2013 was a defining one for K&N Kenanga Holdings Group as that was the year it acquired ING Fund Bhd and ECM Libra Investment Bank Bhd to become the largest independent investment bank in Malaysia. The acquisition also boosted the company's stockbroking business, making it one of the top three players in the industry, with the largest retail segment in the market.

It was during this period that Kenanga Investors (the asset management division of Kenanga Investment Bank Bhd) was undergoing a rebranding following K&N Kenanga Holdings' acquisition of ECM Libra Financial Group's investment banking and stockbroking businesses and Kenanga Investors' acquisition of ING Funds Bhd. The firm intended to unite all its subsidiaries and products under a single brand name to enhance the market visibility of its products.

One of the initiatives under this process was to appoint a chief investment officer to oversee the investments of all the funds under the group. "The industry is quite small and people tend to know each other. If you have a good track record, people will knock on your door," says Lee. "I decided to join Kenanga because it has a very clear plan and vision. And the offer was a very exciting career proposition for me."

FOCUSING ON SMALL AND MID-CAP STOCKS

One of the things Lee did after joining Kenanga Investors was to rebalance the Kenanga Growth Fund, from a defensive portfolio to a growth one that invested more in small and mid-cap stocks. The underlying value investing philosophy remained the same, but the stock-picking experienced a shift.

That was due to the global economy rebounding five years after the crisis, which saw trading activity picking up tremendously and oil prices trading at a fairly high level. These set the context for the tremendous growth of small and mid-cap stocks.

"2013 was the year when small and mid-cap high beta stocks totally outperformed the defensive ones. We rebalanced the portfolio into more growth-oriented stocks," says Lee.

At the time, the growth of defensive and dividend-yielding stocks stagnated, marking the end of the honeymoon period for fund managers with large-cap, defensive stocks.

"That was the time to look outside the benchmark and identify growth stocks. The benchmark is very restrictive with the 30 stocks in it. You have utilities, telcos and banks, but they were not really growing," says Lee.

"The smaller companies were doing very well, but they were not well-known. They were in a variety of sectors, experiencing high earnings and growth, and growing strongly — these were the gems. I rebalanced the portfolio at the right time."

Lee, who adopts a bottom-up stock-picking approach, attributes the fund's outperformance to the time and effort she and her team put in to look for and conduct research on undervalued companies. She says she made many right calls on small and mid-cap technology stocks in the past three years. And it was the tech names that largely contributed to the returns seen by the Kenanga Growth Fund.

The fund's outperformance has mainly come from stocks in the tech sector, which have benefited from the growing global demand for Apple's iPhone. Two examples are Inari Amertron and Globetronics Technology Bhd.

Nevertheless, Lee is most well-known for her timely calls to buy into IFCA. She was one of the earliest to pick the company in the second half of 2014, but she is most remembered for being one of the first to downgrade and sell the stock in 2015.

IFCA was the market leader in software solutions at the time, providing its solutions and services to 70% of the property companies in Malaysia. When the government announced the implementation of the Goods and Services Tax (GST), the company became a beneficiary of the new tax system. Property companies, including major developers, would have to update their existing software with IFCA to be GST-compliant.

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> *> Lee*

SUHAIMI YUSUF/THE EDGE

In April 2015, IFCA was already the world's top performing software stock. Its share price had appreciated more than 1,400%, from 0.08 sen to RM1.28. Nevertheless, seeing that the share price had skyrocketed and the stock was fully valued, it was only a matter of time before Lee made the contrarian call to downgrade the stock in the first half of 2015 and start selling it.

"I met with the management of IFCA in the middle of 2015. While I still liked the company's long-term plan, I felt the near-term earnings growth might have plateaued somewhat. I took profit on my positions. The share price came down after that, but it was due to other reasons. That said, I still believe IFCA has great potential."

While Lee has made many right calls in the past three years, she has also made some wrong ones. Like many fund managers, the wrong calls were mainly on oil and gas stocks, which outperformed in early 2013 but turned south in the second half of 2014. That was when crude oil prices plunged for a short period of time and caught the market off guard.

"Everyone got caught by the oil and gas exposure, including us to a certain extent. But in the second half of 2014, we were quite quick to cut our holdings in oil and gas," says Lee.

"It was a tough decision because we were overweight oil and gas in 2013 and 2014. We cut it based on the supply and demand scenario. On the demand side, China was slowing down and on the supply side, it was the shale gas revolution that transformed the US from an oil importer to exporter."

In 2014, the Kenanga Growth Fund experienced a lower total return historically of 9.31%, based on information provided by independent investment research company Morningstar Inc. This compares with 14.06%, 26.35% and 20.91% in 2012, 2013 and 2015 respectively. But the fund was still the top performer that year as the other funds also saw lower returns. In the past 10 years, the Kenanga Growth Fund has generated a return of more than 300% and won numerous awards.

Moving forward, Lee will be focusing more on the smaller funds under her watch and actively searching for investment opportunities in the region. "We will look at some of our smaller funds as they are more nimble, have well-defined investment objectives and share the same bottom-up strategy as our flagship funds. The most important thing for us now is to continue establishing a solid track record for these funds. I feel we are now ready to go out and promote them," she says.

"Also, we have been quite Malaysia-centric. We launched our first regional fund — the Asia-Pacific Total Return Fund — in 2013. Its benchmark is against a compound return of 10% per annum. Our total return funds look at the absolute returns of the funds instead of following the old way of relying on benchmarking as a performance indicator," she adds.

"Two years later, we launched our second regional fund — the Asean Tactical Total Return Fund — focusing only on Asean. This fund previously lagged its biggest peers [in Northeast Asia]. So this time around, our Asean fund is in a good position to leverage the expected improvement in the regional market. A reversal in the strength of the US dollar will also benefit the emerging markets, including Asean."

Lee is confident the regional funds will perform in the future, owing to her experience in regional asset management in Singapore and Kenanga's expertise. "The Singapore experience has given me an entirely different perspective. It is very useful for me to actually build up the expertise in our regional funds. We also have expertise in the regional market and have experienced fund managers."

CHALLENGING YEAR AHEAD

Last year, the global stock markets saw a lot of volatility due to the market's anticipation of a Federal Reserve interest rate hike and China's slowing growth. The latter caused commodity prices to tank and sent shockwaves throughout the world's stock markets.

Lee says she expects volatility to remain high this year. "It will be a very challenging year. We have entered a bear market judging by the extent of the fall in major exchanges globally. The Hong Kong, US and Europe indices are down double digits [from last year]. Defensive markets like ours are down 3%. The equity markets started off the year badly."

The volatility going forward could be due to the market's reaction to the Chinese government's policy adjustment, as the economy experiences slower growth as it transitions into a consumption-driven one, she adds. "It is not China's economy that really matters, it is the reaction to the policy. You saw the renminbi devaluation [last year] was just a few percentage points and that was already big enough to cause a global selldown in all regional currencies."

However, Lee is not expecting China's economy to have a hard landing as its service sector remains robust and the People's Bank of China (PBoC) still has a lot of room to ease its monetary policy. "The PBoC's reserves have come down to RMB3 trillion, but that is still one of the biggest currency reserves in the world. It can cut interest rates or implement fiscal spending to shore up its economy," she says.

Unlike the doomsayers, Lee does not expect a global recession to happen. Rather, she foresees the global economy growing slowly and unevenly.

"The central banks, especially the BoJ (Bank of Japan), ECB (European Central Bank) and PBoC, still have a lot of policy room to manoeuvre another round of quantitative easing. In fact, the US rate hike process is likely to be delayed in the current environment. We are not painting a global recession scenario."

Against such a backdrop, stock-picking will be one of the keys for alpha performance, says Lee. She is overweight on the "new economy sector" in the Northeast Asia region, which includes China, South Korea and Taiwan. The sectors she prefers are internet, telecoms, healthcare and technology, such as electric vehicles.

"These countries are transitioning to a new economy. As an investor, you should go along with the governments' policy or what they do," she adds.

As for the Asean region, Lee is overweight on the infrastructure sector, including the construction sector in Indonesia and Thailand, which are banking on higher infrastructure spending. Infrastructure concessionaires and construction companies are expected to be the beneficiaries.

"There is always execution risk. It happened to Indonesia last year, but there have been some improvements in terms of the [execution] momentum and [capital] disbursement. I think Indonesia stands on relatively better ground than Thailand [as it still cannot sort out its political problems]," she says.

The Indonesian government launched several infrastructure projects last year, including a Trans-Sumatra toll road, a plan to develop 24 seaports and an ambitious power plant programme. It was also reported that more than US$500 billion would be spent on new infrastructure projects in the next five years.

Major infrastructure projects underway in Thailand include the 300km double-track railway line, the construction of which kick-started this month and is expected to be completed in the next 36 months. There is another 600km of railway projects to come in the next year. The Thai government announced that it planned to spend more than US$100 billion in a seven-year infrastructure programme.

On the home front, Lee is negative on the local economy as she expects the country's gross domestic product growth to decelerate on the back of lower consumption, falling commodity prices and slower external demand.

Investor sentiment is also being capped by the weak currency and subdued corporate earnings growth while the market's valuations remain relatively high compared with its regional peers such as Indonesia, Thailand and the Philippines. This is despite the positive news that the 1Malaysia Development Bhd debt issues have been resolved and there is liquidity support for the market from a large institutional base.

Against such a backdrop, Lee is overweight on sectors that have more resilient earnings. They include construction and infrastructure players as well as exporters. "[We are overweight on] the construction and infrastructure sectors because of the continuous fiscal pump-priming, and exporters for their currency earnings and gradual global growth," she says.

Lee cautions investors who are following the exporters theme to look at the ringgit's weakness, especially moving into the second half. "Exporters, such as those in the technology, furniture and manufacturing sectors, may still be good in the first half, but one has to be nimble and watch for a potential reversal of the ringgit's weakness," she says.

"And of course, if the ringgit strengthens, you will probably have to start looking at the reverse beneficiaries. For example, the automobile sector because their cost is in US dollars or Japanese yen, but their revenue is in ringgit."

Looking forward, Lee expects a rebound in the second half for the local economy. "While I am cautious, I am fairly optimistic of a rebound in the second half because Malaysia was one of the worst performing markets last year in US dollar terms. Its index lost 22% — worse than Indonesia, Thailand, Singapore and the Philippines," she says.

"At the same time, there is potential corporate earnings rebound in the second half. This is simply because of the low base effect. The numbers have been negative for the past two years."

Another reason for her optimism is that oil prices may start bottoming out in the second half of the year, which in turn will see the ringgit strengthen. "Oil prices are so depressed that I don't think they can stay there forever. At some point, a physical market adjustment will take place, such as Opec [Organization of the Petroleum Exporting Countries] cutting production. When these marginal guys cannot survive anymore, that is when your supply comes down and oil prices rebound.

"And when this happen, the ringgit will probably strengthen. So, these are the possible catalysts for the local market in the second half of the year." E