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Market Dialogues

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# Alpha Chronicles: A Sharpe Read

## The Art of Equilibrium: Fidelity Defines Savvy Investing

For John Lo, good investing is not just about crunching numbers - it's also about adopting a holistic approach.

Soft skills, like self-awareness, creativity and sang-froid, are just as vital in driving portfolio returns, says Fidelity International's Portfolio Manager and Head of Equities for Singapore.

"People see finance as being all about hard numbers, and there's an over-preoccupation with the science of it," said Singapore-based Lo, who has three decades of investment experience.

"While those elements are important, and there's a basic need to get them right, the softer side of investing is often overlooked."

Fidelity International, founded in 1969 as the international investment arm of the now separate US-based Fidelity Investments, has US$357 billion in assets under management and administration globally. Clients range from pension funds, central banks, sovereign wealth funds, and large corporates to financial institutions, wealth managers and private individuals.

Increasingly, savvy investing is not only about technical and functional knowledge, Lo pointed out. "If it's only the numbers, we can hire engineers and mathematicians to do the investing."

Empathy, critical thinking and curiosity provide a foundation for developing good judgment, said Lo, who founded Fidelity's investment management team in Singapore in 2005, and currently manages US$2.5 billion for institutional clients across three strategies.

"Sometimes, the smartest people make the weirdest decisions because they are driven by internal or external emotions - for example, pride, or they get swayed by others. That's where the need for self-awareness comes in," he added.

This layer of mental and emotional clarity is what gives the fund manager an edge.

"In this day and age, one cannot be a single-trick pony or a single-faceted individual - just crunching data and facts," said Lo, who holds a Bachelor of Economics degree from University of Wales College in the UK, and a Master of Business Administration from Manchester Business School.

"We need to be able to look at a broad spectrum of different things, and relate to them during the investing process. It's a holistic approach."

**Sit and Stare**

Lo also strives to develop the same self-questioning bent in his son and daughter, aged 14 and 12.

"It's important to be able to critique things with the right amount of emotion and intellect, striking a balance between feeling and thinking, and having a critical layer above that, which will adjust for whatever biases you may have," he said.

Allow yourself time and space to recharge, be creative and find inspiration, he advised. "Most Asians are driven to work very hard, and have no time or latitude for serendipity."

Most family routines - his included - tend to fall prey to a more frenetic pace of life, Lo admitted with a smile.

"My wife is a bit of a dragon mum, and she's got the kids moving from one tuition class to another on the weekends. In my view, playtime is equally important - where the kids have space to sit and imagine, or go off and stare at a blank wall."

And his message to colleagues and friends is the same, whether inside or outside the boardroom: Find the space to be yourself, to think, take risks, and be at peace with failure.

This balanced attitude is critical to being a smart investor, Lo added.

"What we do here in Fidelity is a vocation - it's not something you can leave at door at the end of the day. Generating ideas for stock investments is a lifestyle."

That inspiration can come from a myriad of activities - attending a luxury retail conference, dissecting a designer's creative spurts, or taking a mindfulness class.

"Such non-broker events can give you an idea of how to marry the different elements in big business, such as design and creativity," Lo said.

"A mindfulness course can help you develop focus and a sense of balance when dealing with market volatility - do you ignore it when it happens? Or do you trade around it? These are all important principles."

**Bread and Butter**

Fidelity's philosophy embodies an independent as well as comprehensive focus.

Its Asia-Pacific footprint, which comprises 10 offices, 35 portfolio managers and 73 research professionals, has both depth and breadth of resources. Its investment style involves drilling down into individual companies, slicing and dicing the data, as well as identifying trends by connecting the dots, both regionally and globally.

"Our bread and butter is company visits, and our regional presence allows us to independently corroborate what C-level executives are saying in the boardroom with what is actually happening in different parts of the region," Lo said.

Fidelity meets with 17,000 companies annually, and relies 90% of the time on its own proprietary research to make investment decisions.

The process of reaching an investment call is also highly interactive. "The analysts come up with their independent recommendations, and the portfolio managers have the latitude to challenge and debate those recommendations. It is this collaborative process that drives optimal outcomes for our clients," Lo added.

Turning to the Singapore stock market, Lo noted that contrarian value opportunities can still be found in some sectors.

Singapore's traditional segments - property, banking, oil & gas - are facing challenges on the revenue side, and have mostly been ignored by investors overwhelmed by the prevailing negative sentiment.

"Those are the opportunities that we see. Things are not great, but they are not that bad either," Lo added.

**Against the Tide**

Amidst concerns over global growth, the fallout from Britain's vote to exit the European Union, and China's economic outlook, investors should focus on asset values.

"We need to sift through all that noise, and through research, we can examine key criteria, such as the stock's valuations, management's track record through previous crises, the typical cyclicality of its EBIT margins and returns, including ROA[1] and ROI[1]," Lo said.

Understanding the company's performance through various cycles would provide a good indication of its main growth drivers - whether they are the result of competitive pressures, cyclical or structural factors - and what is likely to transpire in the future.

"This approach is definitely data-heavy and laborious, but it's more even-handed, and reflects a balanced perspective, especially at a time when other investors have lost their energy or been scared away," Lo pointed out.

"This allows us to go against the tide, and that's where we can generate returns for our clients."

In fact, the focus on value[1] has never been more pertinent than over the last nine months, Lo noted.

"What is of reasonable value has become super expensive of late, as any stock that is doing vaguely OK has been priced for perfection, so I have been spending less time on those sectors."

Instead, a significant polarisation has taken place between stocks with strong fundamentals and all the rest, which have been perceived as "rubbish".

"That's where the opportunities lie - on the value side. And if investors take a longer term view, there are definitely gems to be found amidst the rubble," Lo noted.

"If the world is really in that much trouble as everyone suggests it might be, nothing will be spared. For the stocks that are priced for perfection, there's potential for more disappointment, as compared to stocks where there are few or no expectations at all."

But apart from the carpe-diem approach of seizing the right opportunities, the importance of staying your hand at strategic moments cannot be overlooked, especially when a stock's fundamentals warrant it, Lo added.

"When volatility in markets is driven by big macro moves or themes, it's important to be completely focused and disciplined. You need to will yourself not to act, and certainly not overreact, based on the excessive noise."

### [1]Definitions of the Day

**Value Investing**
It refers to the strategy of selecting stocks that trade below their intrinsic values or long-term fundamentals, ie. those undervalued by the market. Examples include stocks with lower-than-average price-to-book or price-to-earnings ratios and/or high dividend yields. Value investors have the opportunity to profit by buying when share prices are deflated.

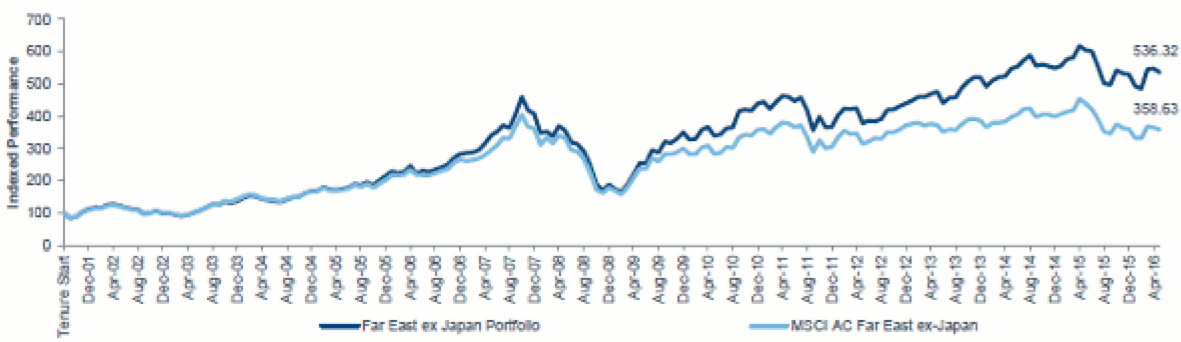
**Return on Assets**
ROA is a financial ratio that illustrates how well management is employing the company's total assets to make a profit or generate revenue. It is commonly defined as net income divided by total assets.

**Return on Investment**
ROI refers to rate of return, and is used to measure profitability for a given amount of time. To calculate ROI, the benefit (or return) of an investment is divided by the cost of the investment, and the result is expressed as a percentage or a ratio. A high ROI means the investment gains compare favourably to its investment cost.

## Far East ex Japan strategy

### Performance

**Performance since inception**
**Annualised excess returns vs. index: +3.0%**




| | 3 months | 6 months | 1 year | 3 year cumulative | 3 year annualized | 5 year cumulative | 5 year annualized | Since Tenure cumulative | Since Tenure annualized |
|---|---|---|---|---|---|---|---|---|---|
| FExJ Portfolio | 10.5% | 0.6% | -11.3% | 12.6% | 4.0% | 16.7% | 3.1% | 436.3% | 12.1% |
| Index | 8.0% | -1.3% | -18.4% | -3.8% | -1.3% | -4.9% | -1.0% | 258.6% | 9.0% |
| Excess returns | 2.4% | 1.9% | 7.1% | 16.3% | 5.3% | 21.5% | 4.1% | 177.7% | 3.0% |

**Outperformance over all standard time periods**

Source: Fidelity International. Data as at 31 May 2016. Comparative Index: MSCI AC Far East ex-Japan. Performance figures are gross of fees in USD terms.
John Lo's management of rep account 1 – from 1 September 2001 to 31 March 2015, thereafter rep account 2.
The returns for rep account 1 are for an investment trust, equity exposure only, with cash stripped out and equity rebased to 100%.

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Photo: Company file

Alpha Chronicles is a regular column on SGX's My Gateway website that aims to profile best-in-class fund managers in the asset management industry. The excess return of a fund relative to that of its benchmark is its alpha, while the Sharpe ratio - developed by Nobel Laureate William Sharpe - measures the fund's risk-adjusted returns.

For previous editions of Alpha Chronicles: A Sharpe Read, please click **here**.

For more information, or if you would like your asset managers to be featured on SGX Market Dialogues, please send suggestions to **jennifer.tan@sgx.com**.

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