DCG capital

DCG Asia Value Fund

At 30/06/2012
Net NAV/Share
S$112.78 (SGD Class)
US$89.15 (USD Equivalent)

Fund Objective and Strategy

The investment objective of the Fund is to achieve long term capital growth through investments primarily in publicly listed and traded equities and equity-linked securities of companies from Asia ex-Japan countries. The Investment Manager employs a value investing approach in managing the Fund. Using a bottom-up approach, it will seek to identify from within the above mentioned investment universe, attractive long term investment opportunities that the Manager reasonably believes adequately satisfy stringent selection criteria in terms of quality and valuations.

Fund NAV and Performance (net of all fees)

	Fund NAV SGD Class	SGD Class 1M Return	MSCI AxJ Net SGD 1M Return	Fund NAV USD Eq.	USD Eq. 1M Return (%)	MSCI AxJ Net USD 1M Return
Sep-11	S$98.95	-1.1%	-4.1%	US$75.68	-6.1%	-8.7%
Oct-11	S$103.09	4.2%	7.7%	US$83.01	9.7%	12.0%
Nov-11	S$100.58	-2.4%	-6.1%	US$78.45	-5.5%	-8.3%
Dec-11	S$101.68	1.1%	1.7%	US$78.39	-0.1%	0.6%
Jan-12	S$105.88	4.1%	7.4%	US$84.15	7.3%	10.8%
Feb-12	S$111.49	5.3%	5.2%	US$89.15	5.9%	6.0%
Mar-12	S$112.29	0.7%	-2.4%	US$89.28	0.1%	-3.1%
Apr-12	S$111.57	-0.6%	-1.5%	US$90.17	1.0%	0.0%
May-12	S$110.52	-0.9%	-5.9%	US$85.75	-4.9%	-9.6%
Jun-12	S$112.78	2.0%	1.4%	US$89.15	4.0%	3.0%
YTD		10.9%	3.6%		13.7%	6.0%
Since Inception		12.8%	2.1%		10.6%	-0.1%

Country Exposure

HK/ China	29.1%
Singapore	31.1%
Indonesia	12.7%
Malaysia	6.2%
Philippines	3.9%
Norway	0.5%
Sri Lanka	2.9%
Cash	13.6%
	100.0%

Sector Exposure

Consumer Discretionary	13.6%
Consumer Staples	12.3%
Energy	6.0%
Financials	19.2%
Industrials	20.0%
Materials	2.4%
Telco	1.2%
IT	11.7%
Cash	13.6%
	100.0%

Top 5 Holdings

WING TAI HLDGS	GOLDLION HLDGS
ARWANA CITRAMULIA	MALINDO FEEDMILL
EZION HOLDINGS	

Size distribution

	No. of Holdings	% of Holdings
Small Cap (<US$1b)	28	55.7%
Mid Cap (US$1b-$5b)	15	20.5%
Large Cap (>US$5b)	6	10.2%
Total	49	86.4%

Valuation

	Trailing P/E	**Trailing P/B**
DCG Asia Value Fund	9.5x	1.3x
MSCI Asia ex Japan	11.7x	1.5x

Fund Information

Domicile: Caymans Island

Fund inception date: 16/09/2011

Fiscal Year End: 30 June

Subscription Frequency: Once a month at month end with 1 week notice

Redemption Frequency: Once a quarter at quarter end NAV with 1 month notice

Valuation Frequency: Once a month

Fund Manager: DCG Capital Pte Ltd

Fund Administrator: Portcullis Fund Administration (S) Pte Ltd

Minimum Initial Investment: S$250,000

Minimum Subsequent Investment: S$100,000

Management Fee: 1.25% p.a.

Performance Fee: 12.5% of appreciation in NAV subject to high water mark

Early Redemption Fee: (Retained in the Fund)
3% in 1st year; 2% in 2nd year; 1% in 3rd year

Custodian: Deustche Bank AG, Singapore Branch

Legal Counsel: Rajah & Tann LLP

Fund Auditor: Ernst & Young Solutions LLP

Tax Advisor: Ernst & Young Solutions LLP

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Important Notice

Report for the Financial Year ending 30th June 2012

Dear Investors,

The Fund achieved a satisfactory performance over the first reporting period from inception (19 September 2011) to 30th June 2012 with ending Net Asset Value ("NAV") standing at $112.778 a share. This represents a gain of 12.78% over the initial share issue price of $100 and also established the new high water mark (previously $100). The 12.78% return achieved well exceeds the benchmark MSCI Asia ex-Japan's 2.14% gain over the same period.

For the month of June, the net NAV rose 2% out-performing the benchmark's 1.4% rise and erased the losses of April and May of 0.6% and 0.9% respectively.

At every financial year end, there is also a process of crystallization of the performance fees and equalisation credits or debits for each investor. This process is explained in the attached Appendix. The Fund's accounts are currently being audited and the audited financial statements will be sent to investors in due course.

Portfolio Review

The DCG Asia Value Fund has been managed on an absolute return basis using the value investing approach, seeking the best value that we can find in the Asia ex-Japan universe of stocks. Our stock selection and portfolio construction process is driven by a bottom-up, stock-by-stock selection process and the stock weights are determined by our level of conviction as to the degree of undervaluation and attractiveness of each stock.

As of 30th June 2012, the Fund was 86% invested in 49 stocks with 31% in Singapore, 29% in Hong Kong/China, 12% in Indonesia and the balance spread across Malaysia, Philippines and Sri Lanka.

In terms of broad industry sectors, the Consumer sectors accounted for 25% followed by the Industrials sector (20%), the Financials sector (19%) and the IT sector (11%).

Top 5 contributors to return were:

1. Ezion
2. Arwana Citramulia
3. Sincere Watch HK
4. Prince Frog
5. Malindo Feedmill

Top 5 detractors from return were:

1. Chen Hsong
2. Moiselle
3. Lung Kee
4. Springland
5. Samsonite

In investing, not every idea will work out. So what went wrong with these bottom five non-performers?

Chen Hsong is a plastic injection moulding equipment maker based in China. It has been in the machining business for more than 50 years. We purchased the stock when it was trading at 5x PE and there was net cash on its balance sheet. The slowdown in industrial activity in China as well as increases in raw material and labour costs hit the company's top and bottom line significantly, with revenue down 24% year-on-year and profits down 52% year-on-year. Dividend was cut from HK$0.27 in 2011 to HK$0.12 in 2012.

Lung Kee, another industrial company that makes mould bases and related products, also issued a profit warning due to cut backs in orders and cost increases.

We bought into these two companies as valuations were rather attractive with strong balance sheets and net cash positions. However, they were both quite dependent on the Europe and US markets which saw demand for the companies' products weakened significantly. While both material and labour costs increased they were not able to pass on these increases and margins were compressed. Moreover, their operating leverage was high as they had large fixed costs relative to variable costs. We had since exited our positions in these two stocks and redeployed our capital into better ideas elsewhere.

Moiselle is a branded apparel and accessories company operating in the Greater China region. We invested in this company for our yield bucket as the company has a consistent track record of dividend pay-outs over the last 5 years and the stock offered an attractive dividend yield of about 8%. The economic slowdown in China has impacted the company's performance for the year ended March 2012 with total revenue falling by 6%. Operating margins were eroded by 5 percentage points owing to escalating rental expenses and labour costs, resulting in a 33% drop in core earnings. Nevertheless the company declared a total dividend pay-out of HK$0.23/share (HK$0.17 ordinary and HK$0.06 special dividend) for the financial year, which translates to a pay-out ratio of 61% and a dividend yield of 12%. The company's balance sheet remains strong with net cash position of HK$268 million and no debt. It currently trades at 10x PE and 0.8x P/B and we remain comfortable holding on to this investment.

Springland is one of the best regional department store and supermarket operators in the Greater Yangtze River Delta, China, which fits into our aggressive growth bucket. 2011 was a good year for Springland with revenue having increased 20% to Rmb3.6 billion and net profit having risen 56% to Rmb590 million. The company's department stores sales increased 27.8% year-on-year and supermarkets sales grew 24%. However, due to the significant slowdown in consumer spending in China in the first half of 2012, the company experienced low teen same-store-sales growth ("SSSG") rate for department stores and flattish SSSG in the supermarkets segment. Expectations for department store sales were revised down from double to single digit growth. At the current depressed price level, the stock is trading at 12x earnings and we will continue to hold onto our investment as we believe that growth will return to this dynamic economic region before long.

Samsonite's shares plunged 16% on 15 June 2012 after Choice Magazine, a monthly publication of the Hong Kong Consumer Council, reported that the side handles of its CubeLite and Tokyo Chic suitcases contained excessive levels of Polycyclic Aromatic Hydrocarbons ("PAH"s), a chemical substance that could cause cancer with over-exposure. In response to the media report, Samsonite issued independent test reports done in Europe showing significantly lower levels of PAHs but nevertheless recalled the two models for replacement of the side handles to reassure consumer confidence. However, given already-weak consumption figures in China and fierce competition from another industry player in India, the stock price of Samsonite remains depressed at around HK$12 reflecting expectations of slower sales growth and lower profit margins in FY2012. There is also concern that CVC Partners and RBS, who currently own 23% and 13% of Samsonite respectively, may further reduce their holdings in the company after the lock-up period expired in December 2011. We see this as a temporary setback and we do not think that there is a permanent impairment of its global brand franchise. We expect Samsonite will continue to grow its Asian business rapidly and ride on the growth of the regional travel markets as budget carriers as well as growing discretionary spending power entice more people to travel. The stock is now trading on 13x forward earnings compared to 24x for a competitor, Tumi.

Portfolio Construction

We built the portfolio, which now comprises 49 stock positions, around six "buckets": **Special Situations, Aggressive Growth, Asset, Steady Growth/Dividend Yield, Cyclicals** and **Moat/Franchise**. We look for multiple sources of return in this challenging, volatile environment where economic growth is subdued and policy risks abound. In order to control investment risk, we also sought to diversify across countries as well as industries and have limited our single stock exposure to no more than 5% of the portfolio so far, although our mandate allows us to hold up to 10% weight in a single stock.

During the past nine months we have invested in a number of **Special Situations**. These are situations where there is an announced corporate event such as a takeover offer or restructuring that gives a high probability of near term capital appreciation and limited downside risk. Stocks in this bucket include **Little Sheep** and **International Mining Machinery**, which we had talked about in earlier letters.

Another **Special Situation** that we recently invested in is **Eng Teknologi**, a Malaysian listed hard-disk drive component supplier with operations in Malaysia, Thailand, Philippines and China. In July 2011, the major shareholder had made a cash offer of MYR2.50 per share to buy out the minority shareholders. Due to the severe flooding in Thailand, some of the company's factories in Thailand were badly damaged, resulting in the financing for the takeover being withdrawn. Subsequently in March 2012, the offer price was revised to MYR2.00 per share with the share price then trading at around MYR1.80. As it was trading at a 10% discount to the offer price we took a position expecting the offer to be successful. The minority shareholders have since approved the deal at an EGM held recently and the stock had appreciated to MYR1.97. The deal is now awaiting final regulatory approval which we expect will be given.

Within the **Asset** bucket, we made reasonable returns from our investments in **Hong Kong Land, Wing Tai Properties** and **Wheelock Properties**. Despite the share price appreciation over our initial investments, these stocks continue to trade at hefty discounts from their respective net asset values (NAVs). While there is no certainty that the discounts will narrow (and indeed one way to narrow the discounts would be through a decline in asset values), we like the risk-reward ratio and in the meantime expect to continue receiving good dividends from these investments.

The large discount in the case of **Wing Tai** prompted the Chairman, who is also the single largest shareholder, to make a voluntary conditional partial cash offer to purchase an additional 15% stake at a price of $1.39 per share. We purchased the stock in December 2011 after the stock price had fallen to below $1.00 after the Singapore government announced the buyer's additional stamp duty. The stock was then trading at a hefty discount from its NAV of $2.57 per share and revalued net asset value (RNAV) of $3.30.

With the announcement of the voluntary cash offer, the stock had rebounded to $1.30 and we had the option of either selling down our position or submitting our holdings for acceptance of the partial cash offer. In the end we sold half our position and tendered the remaining half of which about 20% was accepted at the cash offer price. We are happy to hold the remaining position as it offers a dividend yield of about 4**%**, backed by a RNAV of $3.30.

Wing Tai is sitting on an attractive portfolio of residential apartments, commercial properties, as well as stakes in two listed entities – Wing Tai Properties (HK) and Wing Tai (Malaysia). It also owns and operates a number of retail businesses including G2000, Top Shop and Dorothy Perkins.

Within our **Steady Growth/Dividend Yield** bucket are companies which are growing at a more measured pace of between 5% - 10% a year. These companies, being more mature, tend to generate excess free cash flows and have a consistent record of paying dividends to shareholders. **Citic Telecom, SIA Engineering, SATS, Amtek, Venture** and **Jiangsu Expressway** are some of the companies under this bucket that we have invested in. All in all, during the 9 month plus period, total dividend income received accounted for about a fifth of the total return of the Fund which is a rather significant contributor to the Fund's total return.

As indicated by its name, the **Cyclicals** bucket consists of businesses which are more cyclical in nature. Often the best time to purchase such companies is during a sector downturn when prospects look bleak but the stocks have fallen to such an extent that appear to be pricing in a worst case scenario. Examples of cyclical stocks we have invested in include **STX OSV, Man Wah, Chen Hsong, Lung Kee** and **Rotary Engineering**.

The bulk of the Fund's return in this reporting period was however generated by the **Aggressive Growth** bucket. These are companies that we judge to be capable of achieving at least 15% earnings growth a year for 5 years or more. Among the major contributors were **Ezion, Arwana Citramulia, Prince Frog** and **Malindo Feedmill**.

The last category is the **Moat / Franchise** bucket, which comprise of companies that have business models with strong and durable competitive advantages such that a large barrier to competition is established. These moats could stem from industry regulations, strong brand franchises, well-established distribution networks, a very competitive cost structure or even oligopolies. Moat / Franchise companies tend to have good pricing power and are able to maintain higher profit margins and earn high returns on shareholder capital. Examples include **AKR, Nippon Indosari, UOB, AIA** and **John Keels**.

Investment Outlook and Strategy

As we have said before, our investment strategy is not based on making predictions or forecasts of macro-economic developments. Not only is it difficult to make such predictions, there is also no guarantee that markets will move in the way we expect even if our prediction proves to be right. This is also because it is impossible to know how much of the known negatives or positives have already been priced in the market in the first place.

It does not mean however, that we can blithely ignore the macro issues as they ultimately have a bearing on economic and business prospects in this part of the world. For a large part of the global economy namely in the US, Europe and Japan, prospects for growth are not promising as these three large economies need to reign in their finances and bring down debt levels. This process of deleveraging can take many years and is taking place against a backdrop of already very high rates of unemployment in the US and Europe.

Although it has been four years since the global financial crisis erupted (with the collapse of Lehman Brothers in September 2008), debt levels remain far too high. With interest rates already zero bound, the policy makers have few options to keep economic growth from contracting and unemployment from rising.

The Euro debt crisis, now already into its third year, is far from resolved and could worsen with Spain now in the spotlight and Italy could be next in the firing line.

In the US, there is an approaching fiscal cliff when, come this year-end, much of the Bush-era tax cuts will expire and automatic spending cuts will kick in. This has raised fears of another US economic recession in 2013.

Meanwhile the Japanese economy, the third largest after China, remains anaemic saddled also by huge national debt and a rapidly ageing and shrinking population.

There is now also concern over the health of the Chinese economy with the most recent data pointing to a marked slowdown of economic activity as the export sector gets hit by the recession in Europe, China's largest export market.

In contrast to the Western economies, the Asian economies (excluding Japan) are generally in better shape with healthy government finances, better capitalized banks, favorable demographics (particularly in South East Asia and India) and low unit labor costs. In its latest report, the Asian Development Bank has forecast growth of about 6% for the region for 2012/13. Despite this, Asian stock markets valuation are trading at valuation levels no higher than most developed markets as can be seen in the following table.

	P/E (X)		**P/B (X)**	**Dividend Yield (%)**
	Trailing 12M	**2012E**	**Trailing 12M**	**Trailing 12M**
MSCI Asia ex Japan	11.5	10.9	1.5	2.9
MSCI USA	14.0	13.0	2.2	2.1
MSCI Europe	14.4	10.2	1.4	4.1
MSCI Japan	20.8	13.1	0.9	2.6
MSCI World	14.3	11.8	1.7	2.8

Source: Goldman Sachs, FactSet, I/B/E/S, MSCI, Bloomberg

Such valuation levels against a backdrop of record low interest rates show that investors are very risk averse. It would appear that both stock and bond markets have already priced in a slow growth scenario with very little earnings growth baked in. Nevertheless, in light of the many macro-economic uncertainties, we will continue our strategy of investing defensively and looking for multiple sources of returns. Investing defensively means staying within our circle of competence, investing only in things we understand, and investing with companies that have little debt on their balance sheets and by insisting on an adequate margin of safety. Even as we keep an eye on all of the above-mentioned macro issues, our chief focus will be on selecting good companies with compelling business fundamentals and valuations to invest in.

At the same time, we will also invest in growth companies and continue to look for new and exciting ideas that can generate significant capital appreciation for the Fund over the coming years.

Daniel Chan

Melvin Tan

Alexis Tran

This document is not intended to constitute investment advice and should not be relied upon as such. Reference to specific securities is not intended to be and should not be interpreted as recommendation to purchase or sell such securities. Past performance is not an indication of future performance.