ARKENOMICS CAPITAL PTE LTD

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UEN No: 202203979D

19th July 2023

Re: Investor Newsletter – July 2023

Dear Investors,

We hope this letter finds you well. I am writing to provide an overview of recent market developments and an update on our portfolio strategy for Arkenomics Provident Fund (the "Fund").

Market Observations for 1st Half 2023

2023 Banking Crisis

Beginning March, we observed liquidity issues, bank failures and the subsequent consolidation of several banks in the United States.

These troubled banks (the "Troubled Banks") were primarily reliant on deposits from cryptocurrency and technology start-up firms. In recent years, these sectors fueled a rapid growth of deposits surpassing the overall economic growth rate of the countries in which these financial institutions operated.

However, when funding for these sectors began to dwindle, exacerbated by the fastest rate hike in the past 40 years, these Troubled Banks witnessed steep withdrawals. To meet redemptions, the Troubled Banks had to sell their held-to-maturity assets, resulting in realized losses. Fearing a run on these banks, depositors quickly began withdrawing cash. These large withdrawals forced U.S. bank regulators to step in and take measures to save the Troubled Banks and prevent a banking contagion.

Outside of the United States, shocks waves to the financial system spread, forcing the collapse of Switzerland's second-largest bank resulting in it being acquired by its larger rival.

U.S. Debt Ceiling

In May, the market's focus turned towards the debt ceiling saga in the United States. In the United States, the debt ceiling is a legislative limit on the amount of national debt that can be incurred by the U.S. Treasury, thus limiting how much money the U.S. federal government may borrow.

This issue, although not new, has historically presented challenges. Since 1960, the U.S. government has raised, extended, or revised the debt limit on 78 occasions, leading to political chaos and uncertainty.

In early June, the U.S. government agreed to suspend the U.S. Debt Ceiling limit till Jan 1, 2025, while implementing caps on several aspects of government spending.

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While these macroeconomic events continue to influence market sentiment, I would like to emphasize that our investment approach at Arkenomics Capital is primarily bottoms-up. We focus on individual stock selection rather than just macroeconomic factors.

Arkenomics Provident Fund's Exposure to Financial Sector

We have carefully evaluated the Fund's current holdings and identified distinct differences between the Fund's bread-and-butter banks versus the banks focused on specific sectors such as technology.

Deposit growth rates of the banks held in the Fund align more closely with the GDP growth rates of the countries where they operate. Furthermore, the clientele base of the banks that the Fund is invested in is diversified, thereby reducing concentration risk in any specific sector(s).

To manage risk and adapt to market conditions, we have reduced the Fund's exposure to U.S. banks from less than 2% to less than 0.5%. The overall realized and unrealized gains or losses from the divestment and current positions respectively are approximately flat. Currently, the Fund does not have any exposure to European banks.

However, we have maintained holdings in the banking sector for several reasons:

1. While we anticipate a normalization of interest rates in the future, we do not expect a return to the low-interest rate environment (since the Global Financial Crisis in 2007 to 2021) anytime soon.

2. The banks in the Fund have performed well in a low-interest-rate environment, and we believe they will thrive assuming interest rates normalize over an extended period.

3. These banks offer an attractive starting dividend yield of over 5% and have the potential for increased dividend income. This provides beneficial cash flow for the Fund's asset redeployment strategies.

Arkenomics Provident Fund's Asset Allocation

At Arkenomics Capital, we:

- Adopt the philosophy that "a bird in the hand is worth two in the bush."

- Consider past and forecasted dividend yields to be qualitatively more important than past and forecasted cash flow yields.

Currently, the US market offers earning yields of approximately 2.5 – 4.0% on stocks of interest, while that of Developed Asian markets offer higher earning yields of 8.0 – 12.5% with dividend yields of between 5.5 – 7.0%.

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Given the relative opportunity costs and market odds, the Fund's geographic allocation is predominantly in Asia. Approximately 80% of the Fund is invested in Asian listed stocks, 12% in U.S. listed stocks, and the remainder in European listed stocks.

It is crucial for the Portfolio to generate cash flow consistently. This allows us to fulfil redemption requests if required and more importantly, reinvest into growth or dividend-yielding stocks regardless of subscription inflows.

The Fund's current portfolio dividend yield stands above 4%. Approximately 25% of the Fund is invested in the growth sector where dividends are typically minimal or non-existent due to reinvestment into business expansion. If we were to adopt a more defensive approach, the Fund's portfolio dividend yield could increase to 6%.

We believe our current allocation to be optimal given the high valuations of U.S. stocks, technology and growth sectors.

Arkenomics Provident Fund Performance

Arkenomics Provident Fund generated a net total return of approx. 9.7%[1] in SGD terms for the 9-month period since inception October'22 to June'23

Total return comprises the following:

1. Capital Appreciation: Approx. 6.8% due to increase in the value of the underlying assets[2].

2. Dividend Returns: Approx. 2.9% due to dividends generated by the underlying assets.

Most funds choose to report their performance in USD. Despite this, we have deliberately denominated our Fund reporting in SGD as we are domiciled in Singapore with most of our current investors being Singaporean and/or regional investors. Furthermore, the SGD is widely recognized as one of the strongest & most stable currencies globally today. Based on the long-term performance of SGD against other major developed market currencies, we believe reporting the Fund's returns in SGD hedges our shareholders' returns from currency erosion.

[1] More specifically, Class A shares generated a net return of 9.73%% and Class B shares generated a net return of 9.61% for the 9-month period October'22 to June'23
[2] Capital Appreciation is net of fund management & performance fees

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Thank you.

Regards,

Peter Lum Shuncai
Portfolio Manager
Arkenomics Provident Fund