



Analyst
Liang Shibin
+6565311516
liangsb@phillip.com.sg

It's All About Alpha Generation

Executive Summary

- **Alpha ratio measures the outperformance of funds over their benchmarks.**
- **Over the last 20 quarters, majority of funds tend to outperform against their benchmarks during boom times and underperform during downturn periods.**
- **Alpha ratio is seldom constant as majority of funds do not consistently beat their benchmark.**
- **31 out of a total of 388 funds were able to generate positive Alpha over the last 3 years.**
- **8 funds were identified for recommendation through in-house analysis and selection framework.**

Introduction – What is Alpha?

One of the key objectives of investing in actively-managed funds is the search for outperforming fund managers. Simply put, outperformance of funds can be measured by the ratio known as Alpha. Alpha ratio is the measure of risk-adjusted excess return against a specific benchmark for the fund. A positive Alpha implies that the manager of that fund had delivered a return over and above that which is required to compensate investors. Similarly, a negative Alpha would indicate that the fund had underperformed the benchmark index and investors became worse off investing in the particular fund. Identifying positive alpha funds maximizes investors' chances of achieving persistent outperformance.

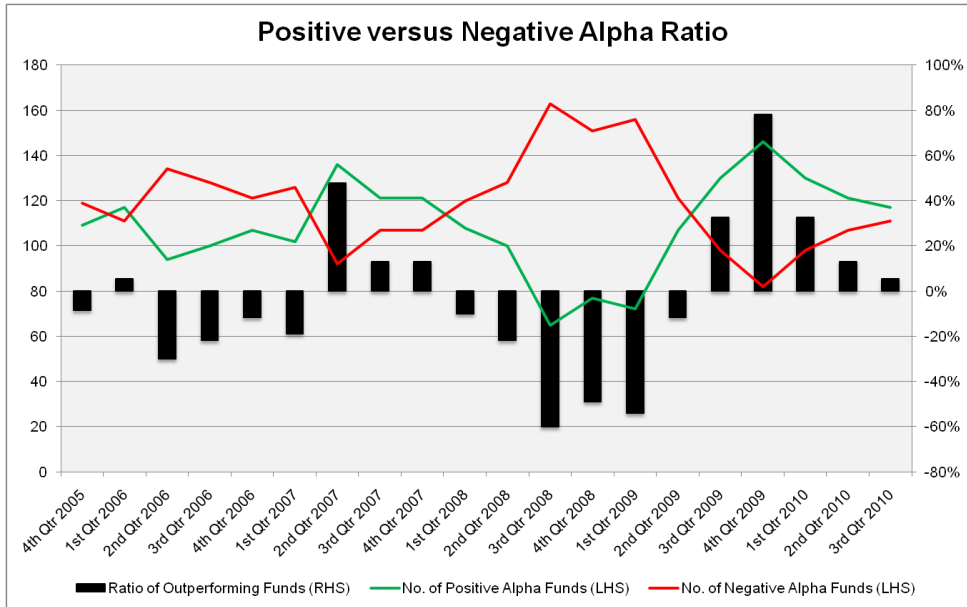
As an onset, fund managers are often deemed as professionals who possess true securities picking skills together with superior knowledge and experience in the investment arena. As such, investors would expect fund managers to deliver a higher return than what a typical benchmark index can achieve. In other words, Alpha may be the single measurement that justify the annual management fees and charges set out on an individual basis by the fund managers.

A recent study is conducted on 228 selected funds (with at least 5 years track record) distributed by Phillip Capital over the last 20 quarters, identifying the percentage of positive alpha funds against negative alpha funds. The results were displayed on Chart 1 on the next page. From Chart 1, the percentage of negative alpha funds against positive alpha funds was significantly higher during the 2008 crisis period. At the same time, we saw a greater percentage of positive alpha funds during the boom times, notably the second quarter of 2007 and fourth quarter of 2009. This proves that there is a strong tendency for fund managers to outperform the broad market during the bull periods and underperform the corresponding benchmarks during downturns.

Based on the findings from this study, one would have also realised that majority of the funds do not consistently beat its benchmark over the last few years and it is going to take an extra effort to identify the outperforming funds. Choosing the right fund can be as important as choosing the right market to be in.



Chart 1: Positive and Negative Alpha (from 3rd Qtr 2005 till 3rd Qtr 2010)



Majority of the funds tend to underperform their benchmarks during crisis period and outperform during the boom times.

*A positive reading on the black bar (RHS) indicates a greater % of positive alpha funds while a negative reading indicates a greater % of negative alpha funds.

Source: Financial Express, as of 11 Oct 2010

Picking the Outperforming Funds – Consistency over Luck

Given the above illustration, the next step is to identify funds which are able to generate positive Alpha on a consistent basis over a period of time, say three years.

From a total of 388 available funds that Phillip Capital distributes, we ran a test to identify funds which had been generating positive Alpha from the period Jan 2007 to end Dec 2009. The results are as follow (See Table 1 on the next page for details):

1. A total of 31 funds had been generating positive Alpha on a yearly basis since 2007. (Funds with less than 3 years of track record or a single negative Alpha year were eliminated from the study).
2. Interestingly, only 1 bond fund was on the list: DWS Lion Bond Fund. 20 equity funds and 10 balanced funds were on the list as well.
3. During the downturn in 2008, Aberdeen Malaysian Equity Fund and Aberdeen Singapore Equity Fund were the top two positive Alpha funds, declining to a much lesser extent than their respective benchmarks.
4. However during the recovery year in 2009, we saw First State Global Resources and First State Regional India being the top two positive Alpha generating funds, a strong indication that the Alpha ratios for funds are not constant throughout equity cycles.
5. The updated performance of the 31 funds were mixed. Categories such as Equity Global and Balanced Global were in the negative territory on a Year-To-Date basis (-0.23% to -7.00%). Funds which performed strongly include Equity India and Equity Asia Pacific ex Japan funds (+12.0% to +27.0%).
6. With respect to our in-house outlook on the global markets, we identified eight funds which are likely to continue their outperformance in the near future.



PHILLIP SECURITIES PTE LTD

Unit Trust – Wealth Creation Concept

11 Oct 2010

Table 1: Positive Alpha Funds between 2007-2009 with YTD Performance

Name	Category	3-Yr Avg Alpha	Year-To-Date %	Recommended Fund
First State - Regional India	Equity India	13.68	20.55	
First State - Global Resources	Equity Global Resources	12.79	5.91	☺☺☺
Aberdeen Asian Smaller Companies	Equity Small Mid Cap	11.88	25.72	☺☺☺
First State - Regional China	Equity China (Greater)	10.00	8.97	
Aberdeen - Malaysian Equity	Equity Malaysia	8.43	26.94	
Aberdeen - India Opportunities	Equity India	8.03	21.67	
Schroder - Multi Asset Revolution	Bal Global Flexible	7.40	3.72	☺☺☺
Prudential - Global Basics	Equity Global	7.39	3.53	
Phillip - Growth Fund	Bal Global SGD Agg	6.67	1.50	
Aberdeen - Singapore Equity	Equity Singapore	6.31	12.04	☺☺☺
Aberdeen - Global Opportunities	Equity Global	6.22	-4.61	
Fidelity - Global Industrials A	Equity General Industry	6.03	0.79	
Aberdeen American Opportunities	Equity North America	4.70	-5.81	
Henderson - Global Balanced	Bal Global SGD Bal	4.48	-0.90	
Schroder - Greater China	Equity China (Greater)	4.35	0.97	
Lion Global - Singapore Balanced	Bal Singapore SGD Bal	4.30	6.83	☺☺☺
Lion Global - MAP Bal Portfolio	Bal Global SGD Bal	4.06	2.09	
Lion Global - China Growth	Equity China (Greater)	3.80	1.92	
Franklin Asian Flex Cap A	Equity Asia Pac ex Japan	3.62	2.71	
UOB - United Global Capital	Equity Banks and Fin	3.56	-4.86	☺☺☺
First State - Dividend Advantage	Equity Asia Pac ex Japan	3.50	5.59	☺☺☺
UOB - United Global Healthcare	Equity Pharma & Health	3.30	-4.93	
Lion Global - MAP Growth Portfolio	Bal Global SGD Agg	3.26	-0.23	
DWS - Lion Bond A	Bond Global	3.17	3.82	☺☺☺
First State - Global Opportunities	Equity Global	2.88	-7.00	
UOB - Growth Path Portfolio Today	Bal Global Target Maturity	2.86	4.26	
Schroder - SISF Emerging Asia A	Equity Asia Pac ex Japan	2.81	1.09	
Lion Global - Europe Balanced	Bal Europe EUR Bal	2.73	-5.92	
First State - Global Balanced	Bal Global SGD Bal	2.67	-5.31	
DBS - Eight Portfolio E	Equity Global	2.26	-1.00	
DBS - Eight Portfolio B	Bal Global SGD Bal	0.59	4.39	

Source: Financial Express and Unit Trust Research Team, as of 11 Oct 2010

From a total of 31 positive Alpha funds, we further identified 8 funds which are likely to continue their outperformance.

Conclusion

Often, professional fund managers are Alpha-seeking in nature and the fact is they should be, given the remuneration they received through annual fees and charges. However, through this study, we observed that less than ten percent of the funds in the sample size were able to generate positive Alpha consistently over the last three years. To achieve this consistency, it will certainly take more than luck. No doubt, Alpha study may not be the single and only test to identify future outperforming funds, it should nevertheless be one of the important criteria to consider when making investment decisions in funds. To further emphasize once again, identifying positive alpha funds maximizes investors' chances of achieving persistent outperformance.



GENERAL DISCLAIMER

This publication shall not be reproduced in whole or in part, distributed or published by you for any purpose. Phillip Securities Pte Ltd shall not be liable for any direct or consequential loss arising from any use of material contained in this publication.

This publication is solely for general information and should not be construed as an offer or solicitation for the subscription, purchase or sale of the securities, and specifically funds, mentioned herein. It does not have any regard to your specific investment objectives, financial situation and any of your particular needs. Accordingly, no warranty whatsoever is given and no liability whatsoever is accepted for any loss arising whether directly or indirectly as a result of any person or group of persons acting on such information and advice. Unit Trusts distributed by Phillip Securities Pte Ltd are not obligations of, deposits in, or guaranteed by, Phillip Securities Pte Ltd or any of its affiliates. No action should be taken without first viewing the details in a fund's prospectus. A copy of the prospectus can be obtained from Phillip Securities Pte Ltd or online at www.eunittrust.com.sg. Past performance is not necessarily indicative of future returns. Investments in unit trusts are subject to investment risks, including the possible loss of the principal amount invested. Investors should note that the value of the units and income from the fund may rise as well as decline. Investors should also note that there are limitations whenever performance is stated or comparison is made to another unit trust or index for any specific period as no funds or indices are directly comparable.

This publication should not be relied upon as authoritative without further being subject to the recipient's own independent verification and exercise of judgment. The fact that this publication has been made available constitutes neither a recommendation to enter into a particular transaction nor a representation that any investment product described in this material is suitable or appropriate for the recipient. Recipients should be aware that the investment products described in this publication may involve significant risks and may not be suitable for all investors, and that any decision to enter into transactions involving such products should not be made unless all such risks are understood and an independent determination has been made that such transactions would be appropriate. Any discussion of the risks contained herein with respect to any product should not be considered to be a disclosure of all risks or a complete discussion of such risks.

Whilst we have taken all reasonable care to ensure that the information contained in this publication is accurate, we do not guarantee the accuracy or completeness of this publication. Any advice contained in this publication is made only on a general basis and is subject to change without notice. We have not given any consideration to and have not made any investigation of the investment objectives, financial situation or particular needs of any specific person or group of persons as we are not in possession of any such information. You may wish to seek advice from a financial adviser before making a commitment to purchase the investment products mentioned. In the event you choose not to seek advice from a financial adviser, you should consider whether the investment product is suitable for you. Any unit trusts mentioned in this publication is not intended for U.S. citizens.

DISCLOSURE OF INTEREST

Statement pursuant to section 36 of the Financial Advisers Act - Phillip Securities Pte Ltd, its directors and employees may have interest in the securities recommended herein from time to time, and its associates and connected persons may also have positions from time to time. Opinions and views expressed in this report are subject to change without notice.

PhillipCapital is a group of companies who together offer a full range of quality and innovative financial services to retail, corporate and institutional customers. Member companies in Singapore include Phillip Securities Pte Ltd, Phillip Securities Research Pte Ltd, Phillip Financial Pte Ltd, Phillip Futures Pte Ltd, Phillip Trading Pte Ltd, Phillip Capital Management (S) Ltd, CyberQuote Pte Ltd, International Factors (Singapore) Ltd and ECICS Ltd.

Information on any and all independent PhillipCapital members and the respective financial services they offer can be obtained through the following website – www.phillip.com.sg. Members can otherwise be identified by their authorised use of PhillipCapital brand name along with their own name in their documentation and literature.