

LIGHTHOUSE ADVISORS

Keeping Your Capital Safe

Presentation to HKSFA

27 September 2017



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Who We Are



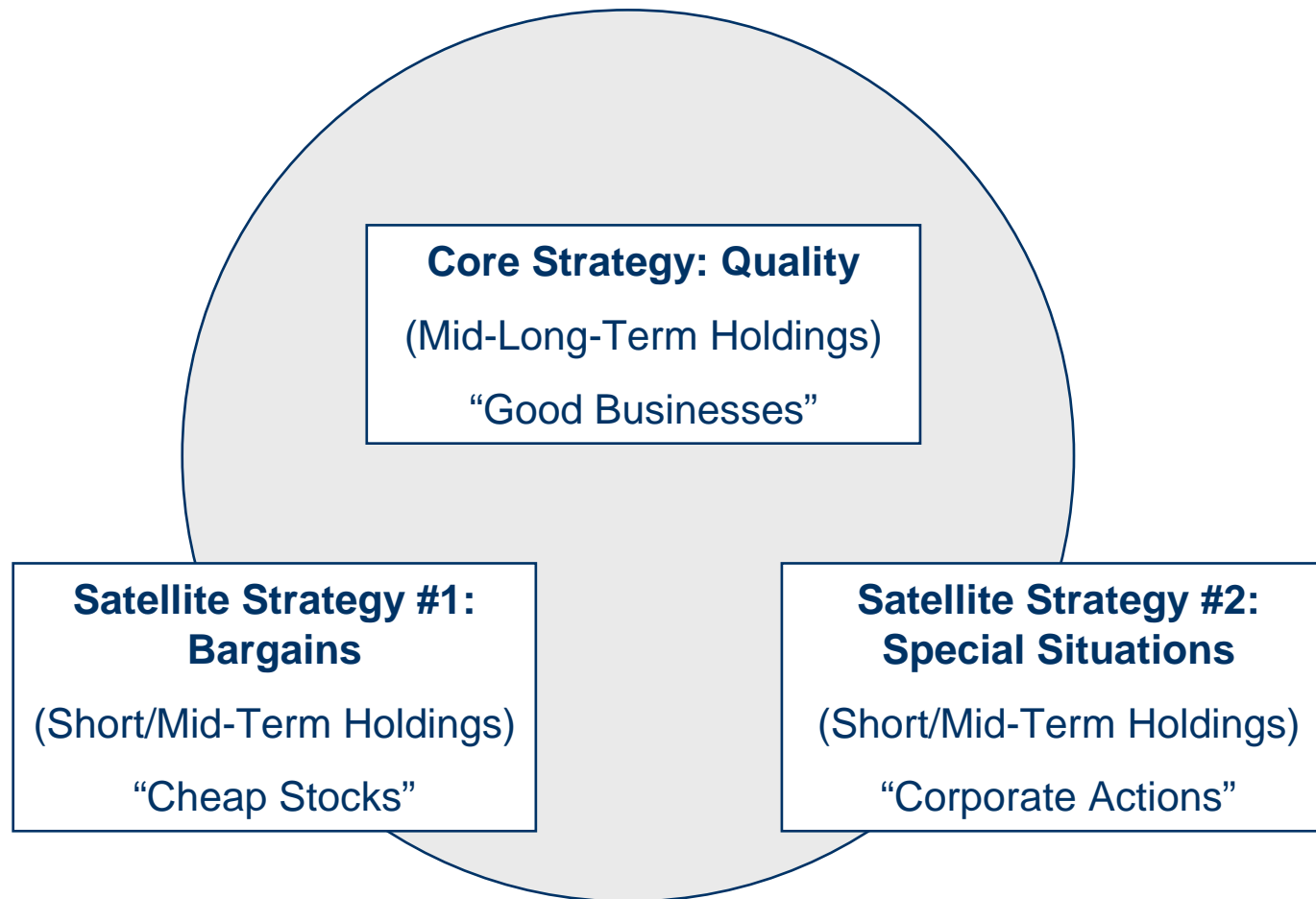
- **The Firm**

- Based in **Singapore**, started in 2008
- **Registered Fund Manager**
 - Regulated by the Monetary Authority of Singapore
- Currently focused on **Asian Equities**
 - Key Markets: **Singapore & Hong Kong**

- **The Team**

- **Benjamin KOH** (Chief Investment Officer / Founder)
 - Previously at **APS Asset Management**
 - 15 years' investment experience (since 2002)
- **OH Chiah Ching** (Investment Analyst)
 - Previously at **First State Investments**
 - 12 years' investment experience (since 2005)

Investment Strategy: Core-Satellite Approach



Portfolio Management



- Concentrated in 15-30 selections
- Position Sizing
 - Initial 2-4%
 - Standard 4-6%
 - High Conviction 6-8%
- Limit 15% per security
- No limit on cash
- Sale Considerations
 - Mistake
 - Fundamentals deteriorate
 - Better opportunities

Fraudy Krueger: A Nightmare on Wall Street



- **Meet the Kruegers: Freddy vs. Fraudy**
- **Fraud-ian Slips**
- **Fraud Simulator**

Meet The Kruegers: Freddy vs. Fraudy

Freddy Krueger

- Harms you in your (sleeping) dream
 - kills you physically
- Victims usually children
- Always known as Freddy
- Cannot be defeated
 - Returns after each death
- **NOT REAL**

Fraudy Krueger

- Harms you in your (retirement) dream
 - kills you financially
- Victims usually adults
- Goes by many names
- Cannot be defeated
 - Takes new form each time
- **REAL**

Fraud-ian Slips



- Working Capital Indicators
 - Unusual levels of AR, Inventory, AP
 - Irrational Management of Cash, Debt, Interest Cost
- Worked Examples
 - “Smoking Guns” but Not 100% Proof of Fraud
 - High AR
 - High Inventory
 - Negative Carry

High AR 1: Ace Achieve Infocom (ACE SP)

- IT systems integrator and solutions provider
- During FY13-FY17:
 - AR: 911-1,118 days (2.5-3.5 years)
 - AR > Shareholder Equity
 - Unbilled Receivables 69-85% of total AR
 - Revenue recognized as % of completion
 - No Invoice, No Payment, Effective AR Days: ∞
 - Impossible for auditor to confirm with customers

High AR 2: Triyards (ETL SP)

- Shipyard
- During FY13-FY16:
 - AR: 200-250 days (7-8 months)
 - AR = 75-109% of Shareholder Equity
 - Unbilled Receivables > 50% of total AR
 - Revenue recognized as % of completion
 - No Invoice, No Payment, Effective AR Days: ∞
 - Impossible for auditor to confirm with customers

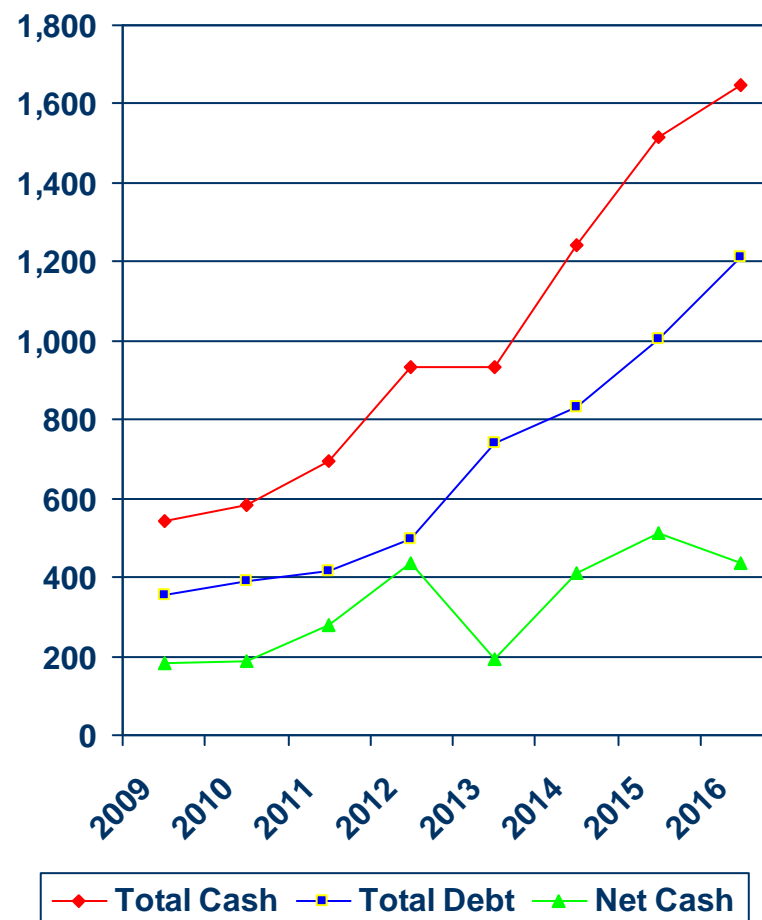
High Inventory: Portico (589 HK)



- Luxury Apparel
- During FY08-FY16:
 - Inventory: 450-500 Days
 - Hugo Boss & Ralph Lauren average 150-200 days
 - Burberry & Hermés average 200-250 days
 - Apparel fashion does not last beyond 1 season (6 mths)
 - Impossible for auditors to check all the stock

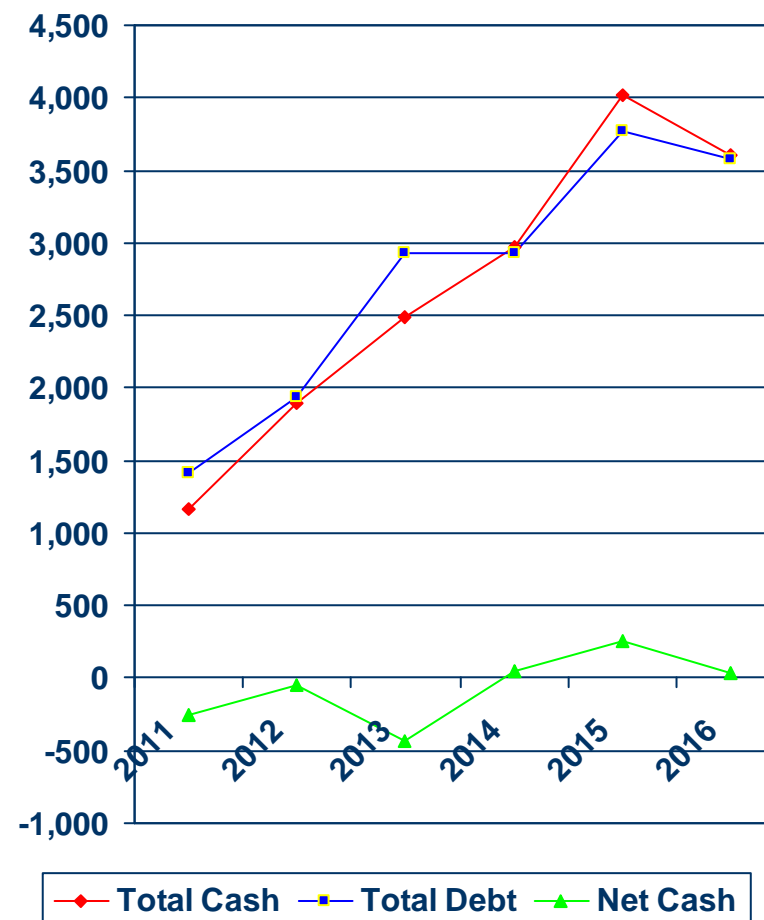
Negative Carry 1: Ecogreen Int'l (2341 HK)

- Flavours and Fragrances
- 2009-2016:
 - Increasing Trend in:
 - Cash
 - Debt
 - Net Cash
 - Negative Carry
 - Debt Cost 5-6%
 - Cash Interest 0.5-2%
 - Balance Sheet
 - Snapshot only
 - Does not reflect daily (average) debt situation



Negative Carry 2: Jiangnan (1366 HK)

- Wires and Cables
- 2011-2016:
 - Increasing Trend in:
 - Cash
 - Debt
 - Net Cash
 - Negative Carry
 - Debt Cost 6-11%
 - Cash Interest 1-2%
 - Balance Sheet
 - Snapshot only
 - Does not reflect daily (average) debt situation



Fraud Simulator

- “Turing Test”
 - Computing
 - Machine output indistinguishable from human output
 - Finance
 - Ponzi dividends funded by share sales and borrowings are indistinguishable from dividends paid from operating cash flow
- Turing Test PASS
 - Cash flows can be created even if the business does not exist
 - Fraud cannot be ruled out
- Turing Test FAIL
 - Cash flows cannot be created unless the business is real and the accounts are “true and fair”
 - Fraud very unlikely

Turing Test 1: Pax Global (327 HK)

- Between 2009-2016:
 - Cash Paid Out: HKD 134m
 - Insiders own 33%, Cash to OPMI: HKD 90m
 - No New Debt, IPO Proceeds HKD 701m
- Financing Cash Flows >> OPMI Payouts
- Turing Test **PASS**
 - Business may be real; BUT
 - Accounts may not be “True and Fair”

Turing Test 2: Minth (425 HK)

- Between 2005-2016:
 - Cash Paid Out: RMB 3.6bn
 - Insiders owned 58% (now 40%), Cash to OPMI: RMB 2.1bn
 - New Debt RMB 1.3bn, New Shares RMB 3.5bn
- Financing Cash Flows >> OPMI Payouts
- Turing Test **PASS**
 - Business may be real; BUT
 - Accounts may not be “True and Fair”

Turing Test 3: Sa Sa (178 HK)

- Between FY08-FY17:
 - Cash Paid Out: HKD 5bn
 - Insiders own 65%, Cash to OPMI: HKD 1.7bn
 - No New Debt, No Shares Issued
- Financing Cash Flows << OPMI Payouts
- Turing Test **FAIL**
 - Business is real; AND
 - Accounts are probably “True and Fair”

Parting Words: Basic Principles

- **Liabilities**

- Usually correct
- May be understated due to 3rd party guarantees, contingent liabilities etc.
- Normally not overstated
- Can usually use “as is”

- **Assets**

- May be overstated in terms of value
- Usually need to be adjusted downwards for actual market value, receivable impairments etc.

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THANK YOU