"Chance only favours the prepared mind"- Louis Pasteur.

The economic data coming out of China has shown the consequences of the government's zero-COVID policy, and it seems very unlikely that, after 65 days of isolation, China will be able to reach their stated target of 5.5% growth in GDP this year despite the recent stimulus measures that they have put in place. The lockdowns have had far reaching effects not only for the national firms, residents and workers but also the multi-national firms that do business in the region.

The Fund felt the consequences of the Chinese lockdowns as various holdings cut their 2022 forecasts owing to the reduction in consumer traffic, and a limited ability to ship orders from their distribution facilities. Fortunately, the worst of these lockdowns now seem to be behind us, and case rates have fallen to levels where the administration is prepared to allow certain areas to reopen and business to resume. We expect that the full consequences of the lockdowns will become apparent in the next quarter's results, but with that, a greater visibility on the rest of the year, as well as a positive impact from pent-up demand after weeks of being confined to apartments.

Inflation has also been close to the top of investors' minds in recent months. Here too there have been some positive indications, with data showing a small respite from the rapid increase seen over the past six months. The chart below shows the Federal Reserve's preferred measure of inflation where the April reading marked the second month of slower growth since the peak of 5.29% in February. We expect that this number will continue to fall in the coming months, but the long-term inflation to remain at higher levels than that experienced over the past 10 years.

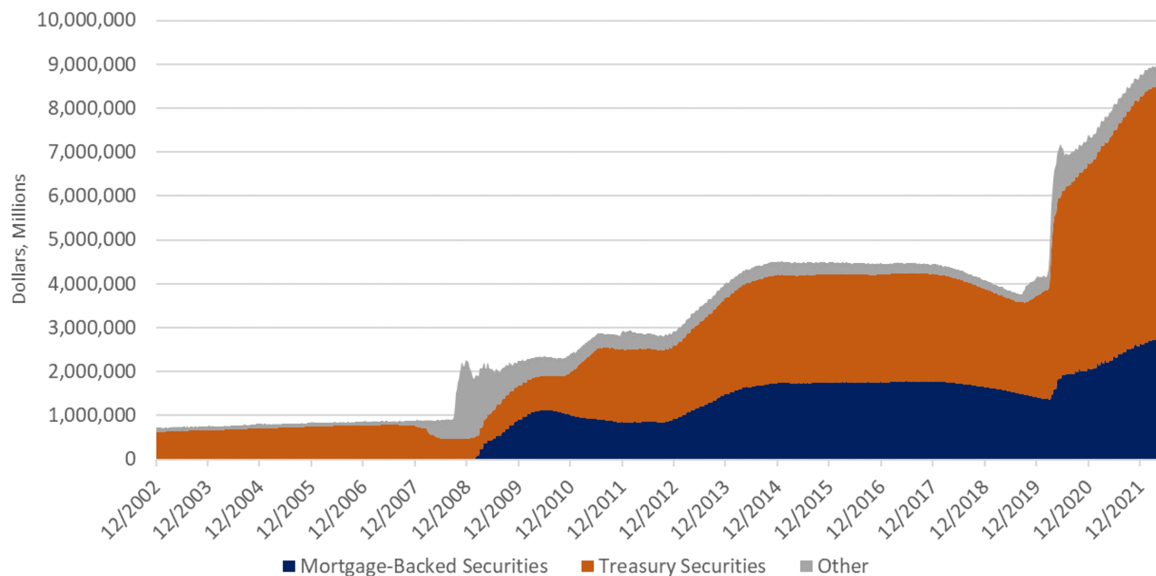
Source: TIM/ Bloomberg

Despite commodity prices (ex-energy) declining, inflation in Europe shows little sign of abating, with Eurozone CPI rising 8.1% in May, owing to German and Spanish inflation increasing by 8.7% and 8.5% respectively. The rise in energy prices resulting from the war in Ukraine and the EU's decision to wean

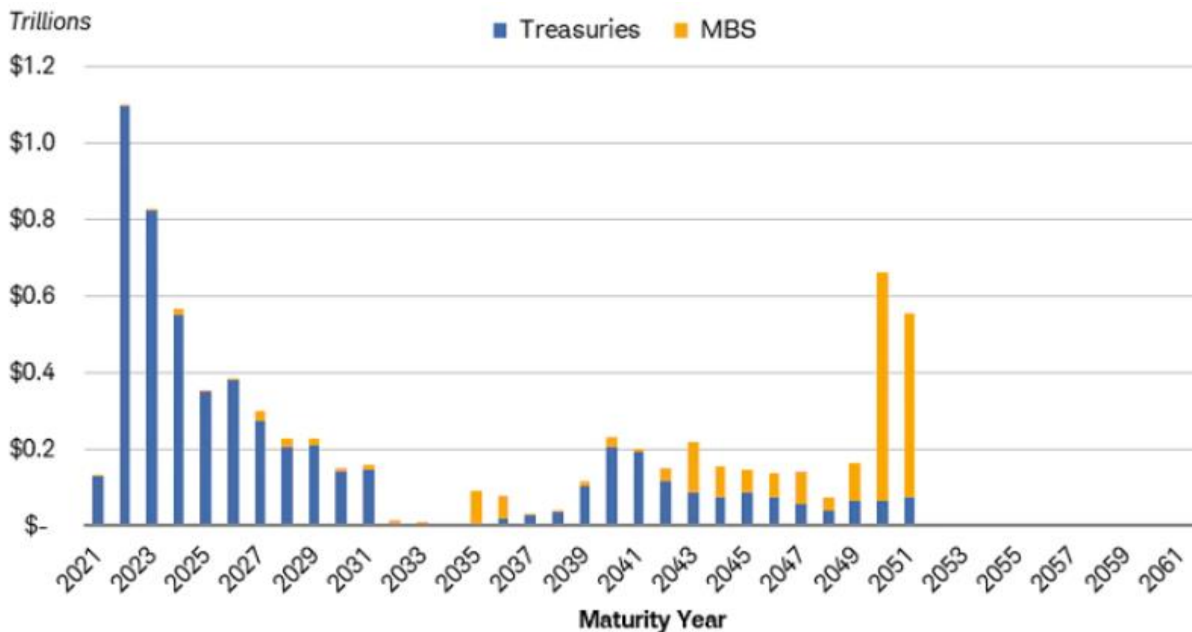
Value of investments can fall as well as rise and you may not get back the amount you have invested

itself off Russian fossil fuels is likely to keep inflation in Europe at higher levels for longer, but here too we expect the headline rate to fall as we progress through the year.

The Federal Reserve has continued with its hawkish rhetoric, calling for multiple 50 basis point rises in the upcoming meetings, however with inflation already starting to roll over, the number of rate hikes expected by the market has fallen, and with it, the 10-year yield. We believe that the Federal Reserve will start quantitative tightening by allowing its stockpile of treasury bills to mature, and not simultaneously renewing them, and that this will have a greater impact on the rate of inflation than the rate rises that the Federal Reserve is placing so much sway by.



Source: TIM/ stlouisfed.org



Source:Federal Reserve Bank of New York

While it is easy to become fixated on all the negative data that gets released almost daily, epitomised by the rock bottom consumer confidence charts, it is worth remembering that most of this data is backward looking and the markets are forward looking, often only trading on the current

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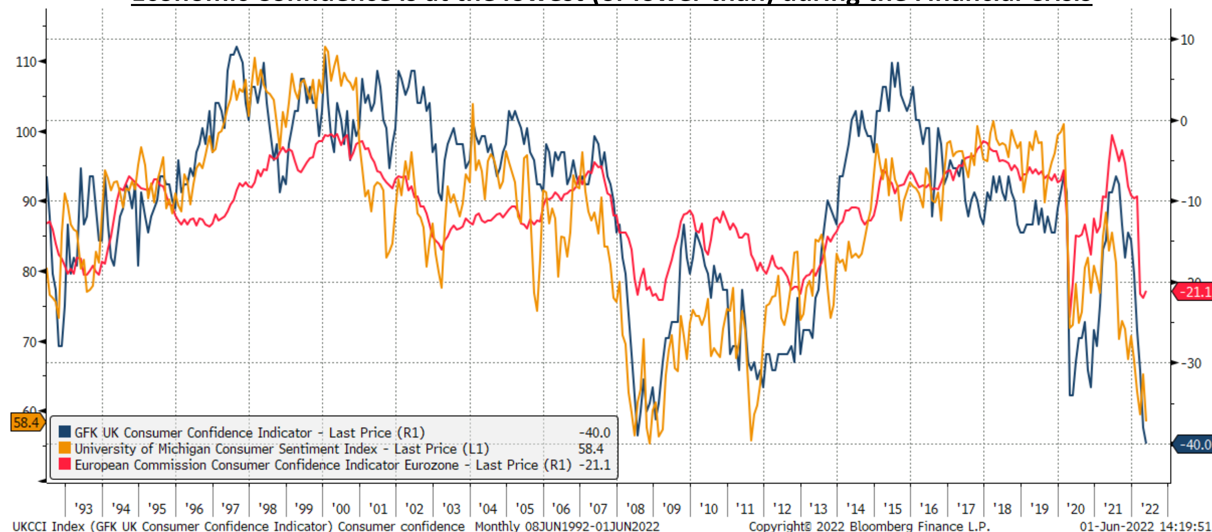
macroeconomic environment temporarily. We believe that focussing on company fundamentals and looking through the current economic malaise and the multiple headwinds will prove to provide investors with the best long-term returns, even if in the short-term, our holdings may feel some pressure.

Economic Confidence is at the lowest (or lower than) during the Financial Crisis



We do, however, take heart in the fact that many quality companies with high percentage of recurring revenues, solid balance sheets and pricing power that helps to offset the inflationary pressures, have re-rated significantly this year, and some are trading below their 2020 pandemic lows, or even pricing in a recession. We do not see a recession as our base case scenario, although we do stress test our holdings for such an outcome.

Government stimulus has defied, the former CEO of Intel, Andy Grove's adage that "Bad companies are destroyed by crisis, good companies survive them, and great companies are improved by them". We do not, however, expect governments to be as lenient in any forthcoming period of slower growth and thus those who survived the past two years on life support may yet face their judgement day; thus we remain focussed on the quality end of the spectrum. Given that Intel's market capitalisation increased by 0ver 4,500% under Andy Grove's tenure as CEO, his words are worth paying attention to.

The Fund had a difficult month owing to the headwinds facing global markets and fell to the lowest level this year, before recovering towards the end of the month, but still ending up 4.28% lower. As a result, the VT Tyndall Global Select Fund B Acc (GBP) returns for 2022 thus far are -13.02%.

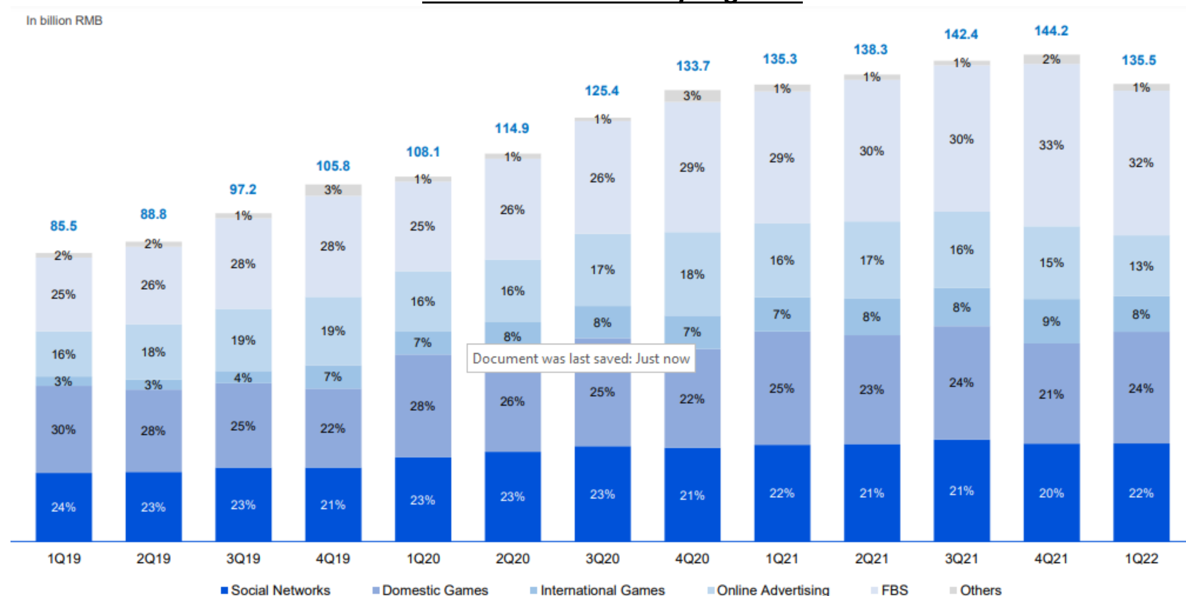
Fund Activity and News

After almost a year of the Chinese politburo attempting to curb the influence of the major Chinese technology companies, clamping down on almost every sphere of e-commerce, from fintech to gaming, came the announcement from Vice-Premier Lui He that the government supported the development of the sector. Combined with President Xi Jinping's comments that the government would step up policy support, including that for the platform economy, led to an increase in optimism towards the embattled Chinese technology sector. Tencent, however, admitted that it would take time for Beijing to act on these promises and that the industry may struggle to grow in the short-term.

The Chinese adoption of zero-COVID targeting has hurt both multi-national and local companies alike as factories, shops and offices closed in both Beijing and Shanghai as well as in the technology centre of Shenzhen. While the severity of the lockdown should have had little impact on gaming revenues of

Tencent, the inability for companies to complete deliveries was always likely to impact the company's advertising and e-commerce revenues in the past few months.

<u>Tencent's Revenue by Segment</u>



Source: Company Results

In the recent quarter WeChat's payments business declined from the pre-recent lockdown growth rate of greater than 30% to a low teens percentage, however with the governments push for the e-CNY payment solution to regain a greater degree of control over national payments, we doubt that WeChat payments will be able to return to the previous growth rates. There also remains the threat, as seen with AliPay, that the fintech business may have to be spun off into a separate holding structure with would disrupt the business and cause a significant decline in the synergies that the company enjoys from the combined business.

The expected growth in domestic gaming failed to appear in the last quarter as the continuing and increasing restrictions on minor playing hours and other protection measures impacted the number of paying accounts. In the longer-term we expect domestic gaming to return to growth despite growing competition in the sector from companies such as NetEase. Of greater concern is the rapid deceleration in the growth of international gaming (from 24% growth in the previous quarter to only 4% in the latest quarter), which the company highlighted as one of its three key pillars for growth last year (video accounts and cloud being the other two). International gaming was not impacted by COVD-restrictions, and the company believes that the pipeline of large-budget games will enable this segment return to growth, however the recent trend highlights the difficulties to grow outside of China, where the company is the default distributor of titles.

With growth slowing in two of the company's stated growth areas and the company yet to properly monetise video accounts, we fear that Tencent will grow at a rate well below that which it has experienced in the past. When this, is, combined with growing competition in the gaming sphere, and the ever-present spectre of government regulation we feel that capital appreciation may be limited going forward.

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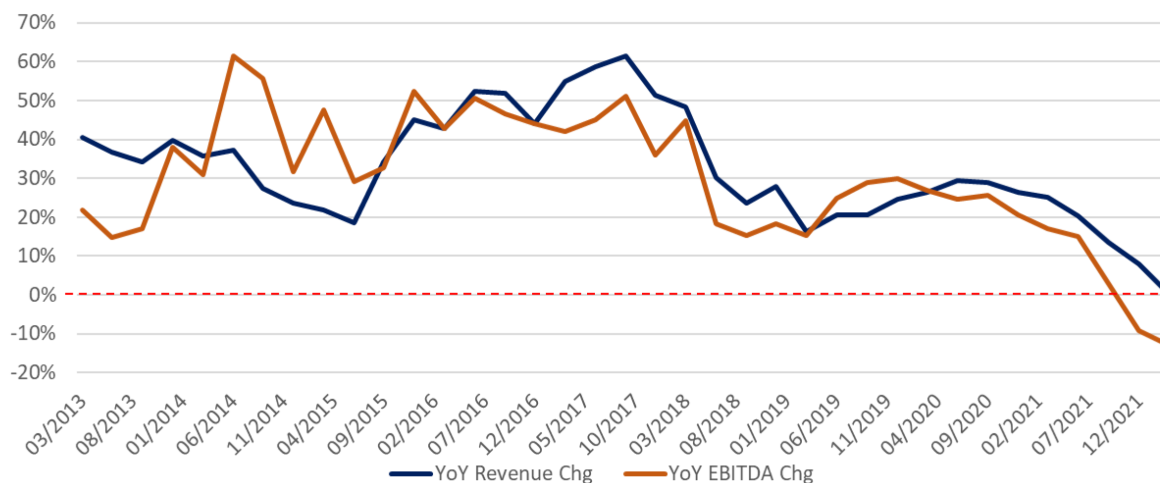
Tencent's growing problems



Source: TIM/ Company data

The Fund has had an interest in Tencent since 2008, firstly though Naspers, which held a 30% stake in the company, before switching to the pure play option in 2017. During this period the stock has appreciated by 3440%, however the company's market capitalisation is currently 50% below its peak in 2021. We halved the position in 2021 owing to valuation concerns while growth was appearing to slow, and the threat of governmental interference following Alibaba founder's comments and the backlash that ensued, and thus only a small positioned remained before we exited it completely this month.

Richard Scrope, Fund Manager, VT Global Select Fund, 31st May 2022
Data source (unless otherwise stated): Bloomberg.

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