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THE recent fluctuations of the ringgit against major currencies have become a focal point of concern among local investors. As a highly open economy actively engaged in international trade, Malaysia's economy is intricately tied to global markets, exposing investors to the vagaries of currency movements.

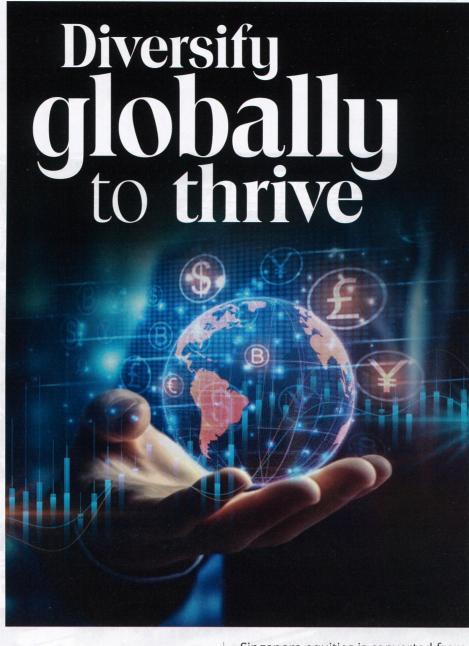
From a household perspective, Malaysians are also feeling the pinch in the form of imported inflation due to the country's heavy reliance on imported goods and services. Against this backdrop, it becomes imperative for investors to prioritise currency diversification and invest across a broad basket of different geographical markets to optimise returns.

In this article, we'll delve deeper into the importance of managing currency exposure in a portfolio as well as the strategic considerations when investing abroad.

Same market, different results

Currency volatility can play a significant role that influences overall performance returns. Given the heightened movements in currency markets, it is crucial for investors to adeptly manage currency exposure.

There is a substantial disparity in total returns for the benchmark KLCI when viewed from both the ringgit and US dollar perspectives. For example, a foreign investor participating in the local market might experience diminished returns when converting the investment back from



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ringgit to US dollar, where the local currency has been depreciating against the greenback.

Conversely, when a local investor invests abroad and the respective foreign currency appreciates, the investor stands to gain higher returns from the investment. For example, a ringgit-based investor would realise higher returns when the value of the investment in

Singapore equities is converted from Singapore dollar back to ringgit.

It's crucial to acknowledge that the examples mentioned above only reflect periods of the ringgit's weakness between 2018 and 2023. Asserting that the ringgit will always weaken against foreign currencies like the US dollar and the Singapore dollar would not be reflective of the country's true fundamentals.

The key takeaway is that it is good risk management to diversify currency exposure for long-term investments. To manage currency risk, investors can opt to hedge their portfolios to minimise the risk of adverse currency swings and its impact on performance returns.

By hedging one's portfolio, an investor chooses to solely focus on investment gains/(losses) directly from the underlying asset as opposed to any currency movements. Thus, an investor can protect investment returns from adverse currency fluctuations and instead focus the bulk of his investment entirely on the performance of the underlying asset class.

There are different considerations that an investor should think about when deciding to hedge. Chief among them is the investor's own objective and risk appetite.

A more aggressive investor may be able to tolerate a larger amount of volatility in his portfolio and may opt for an unhedged currency class. On the other hand, a more conservative investor who requires a steady income stream may choose to invest

in a hedged currency class to shield returns from unfavourable forex translation.

Principles of investing abroad

While investing in domestic equities presents a home advantage due to familiarity with local market dynamics, there are advantages of investing abroad that extend beyond just currency considerations.

These include tapping into a much wider investment universe to access Quality Compounders. In our definition, these are companies with strong business moats, sound financial management and possess a long runway for growth.

Given the inherent differences between local and foreign markets, investing abroad requires a more thoughtful approach and deeper consideration. Economic cycles, regulatory environments and political systems can vary greatly across regions and countries, which can demand substantial resources and time.

But beyond technical analysis, there is also a need to understand different cultural nuances and local customs that have a bearing on impact on consumption behaviour and demographic trends.

A patient and strategic approach becomes essential, allowing investors to navigate short-term fluctuations and tune out market noise to clearly articulate their long-term convictions. The ability to stay grounded and avoid complacency is equally critical by considering different perspectives as well as challenging their own beliefs

In the current investment landscape, there are growing concerns that certain blue-chip investments in foreign markets like the US are overvalued. However, it is vital to discern the presence of Quality Compounders within the wider investment universe that maintain reasonable valuations.

When venturing into foreign markets, a crucial question for investors to ask is whether the company's valuation, when weighed alongside factors such as its business moat, management execution and growth potential, is reasonable.

For example, does the company's fundamentals justify its valuations to yield a compounded annual return of at least 8%-10% over the next 3 years? Similarly, is there long-term visibility on growth and risk?

Answering these questions thoughtfully is integral to formulating a successful strategy when investing abroad. Technological strides have made it more accessible for everyone to invest globally. Real-time market information, data analytics and digital platforms are empowering investors to make more timely and informed decisions.

By adhering to some of the key fundamental principles discussed here, investors can unlock the full potential of a globally diversified portfolio, paving the way for long-term financial success.