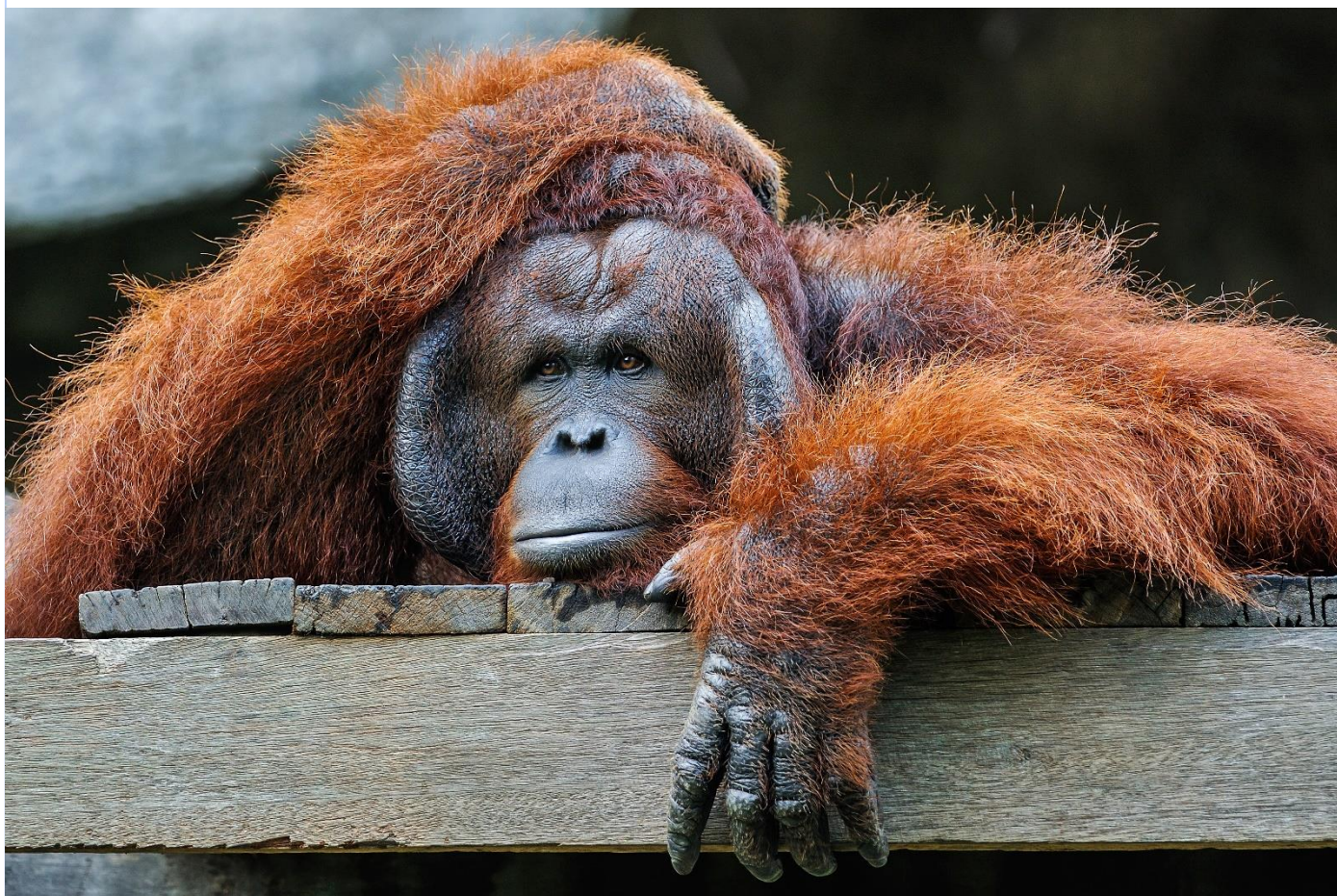




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Apes speak no evil

"What motivates [radical groups] and the millions who support them? The answer, many believe, is stories – about injustice, outrages, ancestors, coreligionists, nonbelievers, stories from the past and present."

– Geoff Colvin –



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What We Learned This Quarter

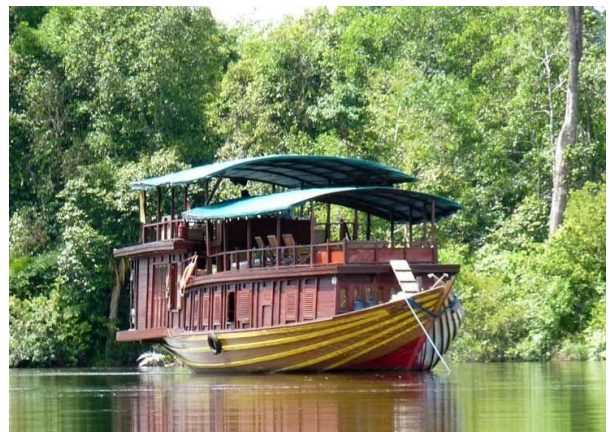
Apes speak no Evil

The tale of humans and apes

One great thing about Indonesia is the opportunity to explore the natural wonders of the country. We recently made such a trip, visiting the captivating Orangutan center at the Tanjung Puting National Park in southern part of Borneo island.



Source: Orangutan Foundation International



Source: Bobobobo.com

Unspoiled beauty in Tanjung Puting orangutan center

The park offers astonishing jungle river tours that bring you up close and personal with Borneo's great ape. Just imagine: during the day you sit on the deck of a private Klotok riverboat, observing the jungle and listening to forest bird chirping sounds while enjoying a drink. At nightfall you moor on the edge of the jungle, listening to its sounds and seeing fireflies while a delicious dinner is being prepared. Later you retire to your bed under a clear display of the stars in the sky. Believe us when we say that this is a place you can fall in love with. Tropical forest at its best.



Source: Heyokha



Source: Bobobobo.com

Magnificent orangutan in Tanjung Puting



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During our trip, it was striking to see the resemblance between orangutans and humans. Orangutans can recognise themselves in mirrors, use sophisticated tools and some can even communicate with humans through sign language! (They also can be sexually attracted to human females, but don't tell that to your spouse) Our similarity is not limited to behaviour: the red-haired ape shares 97 % of human's DNA. Can you imagine?

Inspite of this similarity in DNA, the orangutan is easily 5-10 times stronger than a human. We'd probably win a (sign language) argument with an orangutan, but even our best UFC fighter would not to stand a chance fighting one. The risk of being harmed was made pretty clear to us when visiting Tanjung Puting, as we were constantly warned to avoid upsetting the Orangutans (see picture below).

This is a good reminder about human - or Homo sapiens' - physical limitation and made us wonder how Homo sapiens ever managed to rise and conquer the world. To answer this big question, we have been reading the book *Sapiens, A Brief History of Humankind* by Yuval Noah Harari. According to his theories, the rise of the Homo sapiens took more than strength and intelligence.



This is just mind boggling. Did someone actually try that before?

A warning sign for the “Homo sapiens” in the Orangutan center in Tanjung Puting. A good reminder of our physical limitation.

Source: Heyokha

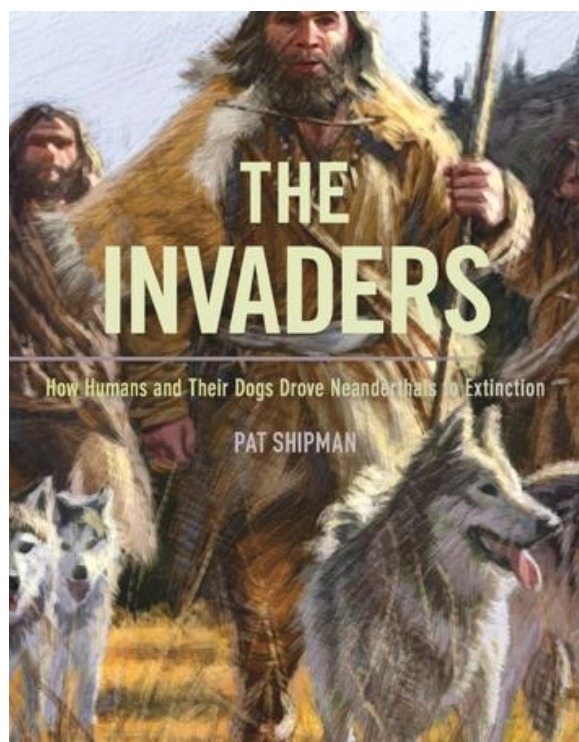


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Skeletons in the Closet

The Homo sapiens did not only compete for dominance with other animals. From about two million years ago until around 10,000 years ago, several human species were roaming around this planet, at the same time.

One of those species were the Neanderthals. Unlike the prevailing image we have of them as being brutish and stupid “cave people”, they actually had a bigger brain size than we do. In addition, the Neanderthals were more muscular than Sapiens, better adapted to cold climates, able to use tools and fire, good at hunting, and apparently took care of their sick and infirm.

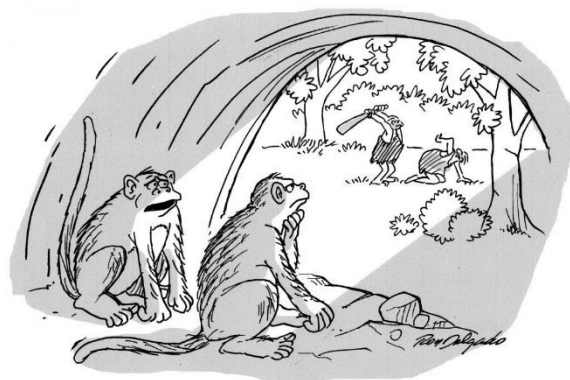


The rise of Homo sapiens and.... their dogs

While there are different theories about the extinction of the Neanderthals, one of them tells the tale of Homo sapiens driving the Neanderthals from the face of this planet.

Competition for resources might have flared up into violence and potentially resulted in the first and most significant ethnic-cleansing campaign in history. Looking at our ongoing intolerant behaviour, it is indeed difficult to imagine that

Sapiens were more accommodative towards other human species such as the Neanderthals.



" Now you've seen them - - - Do you want to keep evolving ? "

The question is, why couldn't the strong, brainy, cold-proof Neanderthals survive our onslaught? Harari's answer: Homo sapiens conquered the world thanks above all to its unique language and ability to imagine.

Sharing and believing in fiction: The rise of the Homo sapiens

The era characterised by the appearance of new ways of thinking and language - between 70k and 30k years ago – is referred to as the Cognitive Revolution. The new linguistic skills acquired at that time enabled the Homo sapiens to expand into larger bands and develop tighter and more sophisticated types of cooperation.

The truly unique feature of our language is the ability to talk about things and concepts that we have never seen, touched or smelled. Legends, myths and belief appeared for the first time during this era. In other words, our language enabled us to share and believe in FICTION.

A monkey could never be convinced to give us a banana by promising him limitless bananas in life after death. Homo sapiens can, although you might have to come up with something better than bananas.

Harari argues that communicating fiction was such a game changer as it has enabled us to imagine things as a collective group. To illustrate the impact of this, Harari mentions a basketball game as an example. We can play the basketball game with complete strangers because they have all learned an



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identical set of ideas about basketball. These ideas are entirely imaginary, but if everyone shares them, we can play the game.

Unlike apes or Neanderthals, Homo sapiens post cognitive revolution can cooperate in extremely flexible ways with countless numbers of strangers.

Mutual aid between and among members of a species may be the most potent force in evolution. And that's why Homo sapiens rule the world. We were just able to get a larger group to stand behind a cause, whether good or bad. The rest is history.

Big government eroding the trust in free market

Student: "If I study conscientiously, how many years will it take me to learn Zen?"

Zen master: "Seven years"

Student: "If I double my effort and do nothing but study, how long will it take me?"

Zen master: "Fourteen years"

We made a point that any large scale human cooperation is rooted in beliefs that exist only in people's collective imagination. However, these shared beliefs can be fragile as faith in them might be lost. And because of this, a shift in paradigms can have a major impact on the status quo.



When Homo sapiens lost faith in money, Weimar Republic

Source: Internet

A. Value of paper money is an ultimate example of belief and trust

An example of a man-made belief or faith based on trust is the monetary system. Money is not coins or banknotes. It is anything that people are willing to use in order to represent the value of other things for the purpose of exchanging goods and services, and to store wealth conveniently.

In prisons, for instance, cigarettes have often served as money. Even non-smoking prisoners are happy to accept cigarettes as payment. Money was a purely a product of mental revolution.



In prisons, cigarettes is money.

Source: www.theguardian.com

Money is about trust and allows complete strangers to trade. The thing is that this trust is very universal and we believe in money partly because the governments believe in them and demands them in taxes. The crucial role of this trust explains why our financial systems are so tightly related to our political, social, and ideological systems.

People may speak different languages, obey different rulers and belong to the different religions but all believed in money (gold, silver, or US\$). The mere fact that the European believes in US\$ would cause Chinese to believe in US\$ too.

Two people who could not agree on ideological or religious beliefs could nevertheless agree on monetary belief, because whereas ideology or religion asks us to believe in something, money asks us to believe that other people believe in something. Even the biggest enemies lusted after the other side's money.



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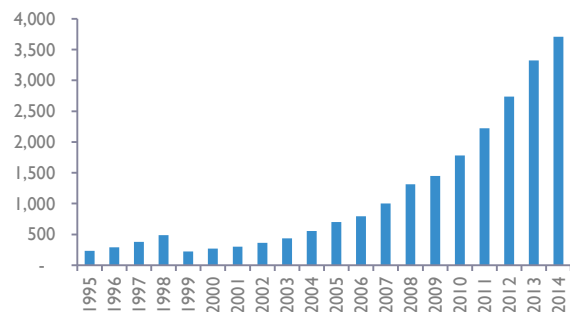
Whilst money is more open minded, it has a dark side: it is not based on sacred values and humanity. Instead, it is backed by the cold and impersonal law of supply and demand.

As people accepted the law of supply and demand, the boom and bust cycles started to become a part of life i.e. Economics 101. A bubble creates oversupply and not enough demand. Bubbles have to implode because by definition a bubble involves a non-sustainable pattern of price changes or cash flows. Bubbles burst and people would start over and worked out the over supply situation.

Iceland is a good example of a country that dealt with the underlying problems post GFC, not just the symptoms. They started over and now Iceland's economy has become one of the top performers in Europe.

Another good example are some Asian countries after the Asian Crisis. Fortune destroyed and new bigger fortune is created by those who rightly deserve in the process after.

Indonesia Loan outstanding in Rp, trn



Source: Bank Indonesia

B. Trust in free market mechanism in question

One fundamental belief that will be increasingly in question, in our view, is the belief that governments are willing to let capitalism and markets do their work (letting the boom and bust cycles run its course).

Instead of studying the supply and demand of goods and services, investors these days find themselves focusing on central bank policy and the supply of money. It is becoming apparent that watching the Fed (and BOJ, PBOC, ECB, the list goes on and on) has become the most essential part of the investment process.

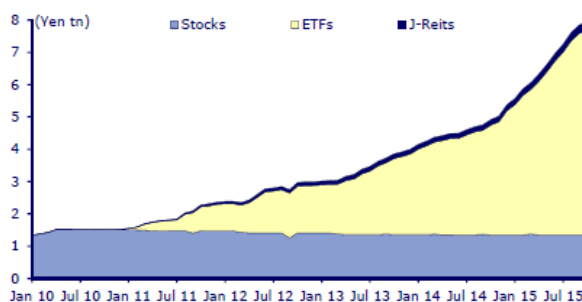
Operation Twist????!!

Perhaps QE4 will be name liked Operation Turn???



In fact, since 2010 every small market selloff (not even real deterioration of the real economy) are followed by immediate central banks responses. By quickly riding to the rescue, the Fed is effectively front-running investors. This phenomenon is not only happening in the US, but also Europe and Japan.

Bank of Japan holdings of Japanese equities



Note: In book value terms. Data up 20 October 2015

Source: CLSA, CEIC data, Bank of Japan

Case and point, the BOJ is now the second biggest investor in the Tokyo stock market after the Government Pension Investment Fund.

With these expansionary policies, governments are getting bigger and bigger, creating one bubble after another.



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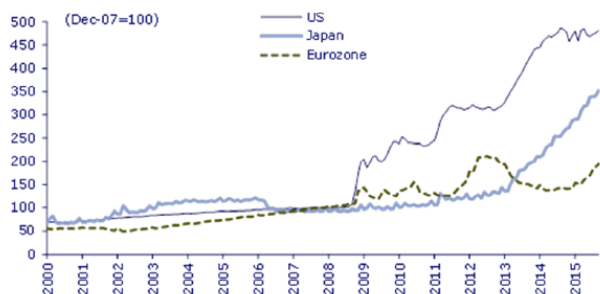
The big government monster captured by contemporary Indonesian artist, Eko Nugroho

Source: Heyokha

C. Why governments are getting out of control?

Globally, 14 trillion USD equivalent have been printed since the end of the GFC. Not only the global economy did not deleverage from the 2008 crash but instead doubled down on more debt.

US, Japan and Eurozone monetary base (rebased to Dec-07=100)

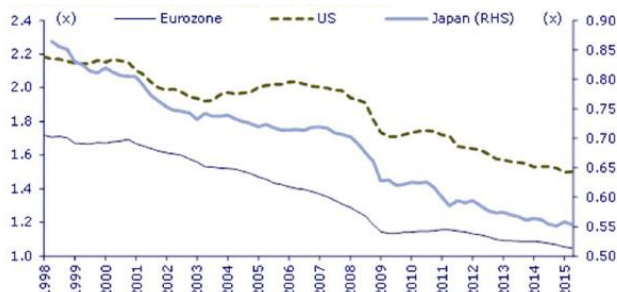


Expansionary monetary policies are accelerating

Source: CLSA, Federal Reserve, Bank of Japan, ECB

It becomes ever more evident that Western central banks find themselves in a trap of their own making as their balance sheets have expanded as a consequence of asset purchases.

US, Japan and Eurozone money velocity (Nominal GDP/M2)

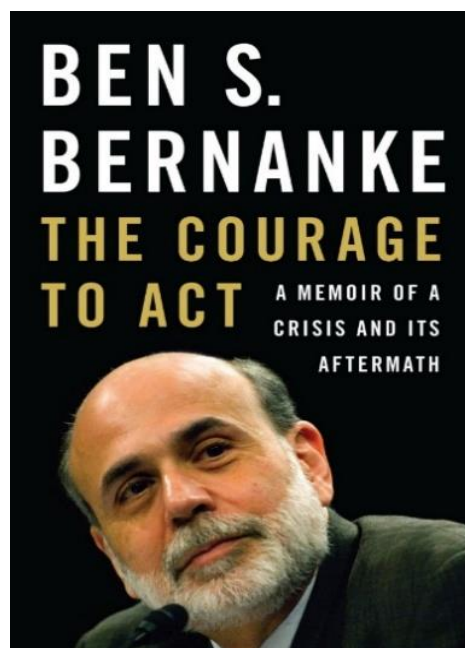


Despite all the money printed out of thin air, Money velocity is decelerating

Source: CLSA, CEIC Data

D. Why trapped?

CLSA strategist Chris Wood notes that Bernanke's writings make clear that he still does not understand that his quantitative easing policies have had the precise opposite effect of what was intended, namely that they are deflationary not inflationary.



Source: Amazon

Chris wood argues that it would be courageous to do the precise opposite of what Bernanke did.



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A case for gold

There is no means of avoiding the final collapse of a boom brought about by credit expansion. The alternative is only whether the crisis should come sooner as the result of voluntary abandonment of further credit expansion, or later as a final and total catastrophe of the currency system involved.

– Ludwig von Mises, Human Action (1949) –

We at Heyokha are not saying we are doomed and advice to buy farms and stock it with spam, guns and gold.

However, we do believe there is no infinite number of free lunches and that central banks printing money will not be without consequences. At some point, the believe and faith in Central Bankers will be lost.

Gold is an insurance in a situation like today where central banks are applying increasingly reckless monetary policies to address a perceived deflationary problem to prevent a bust.

As such, we feel that the risk reward of gold and gold mining companies are increasingly attractive. While we admit it is impossible to pick the bottom in the near term, the figure on the right indicates that in case of a hyperinflation like in 1923, it didn't make a big difference whether you bought at DM 170 per or DM 30,381 per ounce. Your return would have been enormous either way.

Lesson from history: German Marks needed to buy one ounce of gold

Jan 1919.....	170
Sept 1919.....	499
Jan 1920.....	1,340
Sept 1920.....	1,201
Jan 1921.....	1,349
Sept 1921.....	2,175
Jan 1922.....	3,976
Sept 1922.....	30,381
Jan 1923.....	372,477
Sept 1923.....	269,439,000
Oct 2, 1923.....	6,631,749,000
Oct 9, 1923.....	24,868,950,000
Oct 16, 1923.....	84,969,072,000
Oct 23, 1923.....	1,160,552,882,000
Oct 30, 1923.....	1,347,070,000,000
Nov 5, 1923.....	8,700,000,000,000
Nov 30, 1923.....	87,000,000,000,000

Source: Internet



Collateral damage

“Cities and countries that became rich and powerful inevitably grew arrogant, overconfident and complacent, and they tend to overspend. Having enjoyed incredible success, they adopted a “nothing can go wrong” attitude and inevitably commit gross errors of optimism.”

- Marc Faber

One unintended consequence of the currency wars and bailout policies that begun in late 2008 (with the Fed first launching of quanto easing) is that the “too big to fail” firms that should have seen their demise are staying afloat instead.

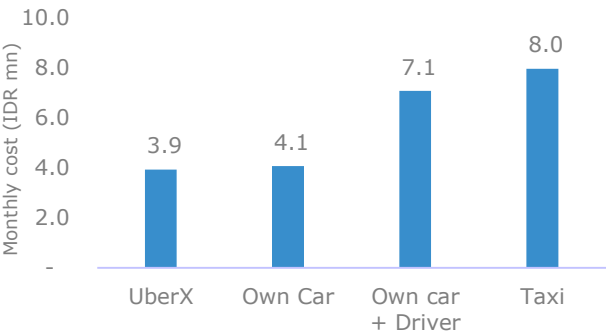
Adding salt to the wound, the increasingly excessive regulatory environment (and protectionist policies) has made life very difficult for the younger and innovative but smaller challengers.

Excessive regulatory environment favours the established players. The big established players can better cope with new regulations as they are able to hire armies of lawyers and lobbyists.

This is a disturbing fact because new entrants have contributed to a disproportionate share of disruptive and innovative business ideas that have benefitted consumers.

One fine example is Uber. The graph on the right clearly indicates that consumers are financially better off using Uber and its popularity is testament to this. Yet, this poster child the sharing economy has been facing regulatory hurdles in many places, including in Jakarta.

Transportation cost for owned car, taxi, and Uber



Note: monthly cost estimates are based on 80 km distance traveled per month

Source: Sucorinvest

It is not only the private sector that is negatively impacted. A low interest rate environment also means that the governments globally have little incentive to reduce their expenditures, which translates into extravagance and inefficiency and crowding out effects.



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3Q Market Review

Global markets suffered a big setback in the quarter on the prospect of a rate rise in September. High-yield markets plummeted and credit spreads widened. Stocks fell 10 per cent in the US and almost 20 per cent in most emerging markets. Indonesia suffered one of the worst quarterly corrections since the GFC with the JCI down over 21% (USD terms) in the period.

As discussed in our previous newsletter, we remain cautious in post commodity bull market Indonesia. The table below shows the interest of Japanese business in Indonesia. Interestingly their bullishness peaked at the very top of the JCI (USD terms) in 2013. We see this as a contrarian indicator. We will watch 2015 ranking very closely.

JBIC survey: Promising countries for Japanese companies' overseas expansion

Rank	2006	2010	2013	2014
1	China	China	Indonesia	India
2	India	India	India	Indonesia
3	Vietnam	Vietnam	Thailand	China
4	Thailand	Thailand	China	Thailand
5	USA	Brazil	Vietnam	Vietnam
6	Russia	Indonesia	Brazil	Mexico
7	Brazil	Russia	Mexico	Brazil
8	Korea	USA	Myanmar	USA
9	Indonesia	Korea	Russia	Russia
10	Taiwan	Malaysia	USA	Myanmar

Classic contrarian indicator?

Interesting to see 2015 ranking

Source: JBIC

A big sell down presents an opportunity for us to size up our core holdings positioning. This is especially interesting against the backdrop of series of encouraging Indonesian government reform efforts recently.

One of the companies that we like is Indonesia's leading corn and rice seed producer (as discussed in our IQ15 report). In line with our expectation, the company just reported a strong 3Q, with 9M profit up 110% YoY. We expect strong earnings momentum to continue driven by the country's much needed agriculture reforms. Stock is trading on 12x 2016 PE with 25-30% CAGR in the next few years.

The reality is that, in line with the major trend in other countries, most young people don't want to be a farmer these days. A recent survey by the Indonesian Institute of Sciences (LIPI) has found that more young people prefer to live in the cities. As such, the country could face a dwindling number of farmers that in the long run could threaten its food security.

The survey's preliminary findings discovered that a staggering 90% respondents in three of Central Java's rice producing areas, whose ages ranged from 15 to 29, objected to becoming farmers.

Moreover, the six-month research by the institute also revealed that ALMOST ALL of the 150 parents interviewed for the survey, who had teenagers and worked as farmers, did not want their children to become farmers. Both the young and their parents thought working and living in the cities offered better chances to move up the social ladder.

To deal with this challenge, the government needs to raise farm productivity and better seed is one of the obvious solutions. This is a powerful long term backdrop for the seed company that we invested in.

Another big boost to productivity is the building of dams and the improvement of irrigation where we see government is already making impressive progress. In some regions that have good irrigation networks such as Kediri, they can plant 2-3 times a year while others can only plant once. Imagine the demand for seeds if all regions can plant multiple times a year.



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Another Indonesia-related company that we are adding is in the energy space. Market sell off together with wide spread horror stories about the demise of fossil fuel created some very compelling opportunities in that sector.

The company is an integrated energy company primarily engaged in the production and sale of power, natural gas and LNG. The company currently produces 315MW from its combine cycle power plant (in Indonesia) with a further 650MW (400MW online in 1Q2016) being developed in the Philippines. The company is trading on 4x EV/EBITDA just based on their power business alone, basically giving a zero valuation to their proven gas reserves and LNG business.

In fact, biggest upside is from their development of the first mid-scale modular LNG facility in Sulawesi, Indonesia. After years and years of delays, we recently see major milestones being achieved. We expect first LNG (500mtpa out of total 2m TPA online) to be delivered in late 2016.

Heyokha LNG site visit in Sulawesi



Source: Heyokha

As an insurance, we added positions in gold miners. From the darling to the most hated, major producing gold miners on average are trading at 60% discount to where it was back in 2006 (as far back it goes) when gold was barely above \$600.

Chart GDX J vs. Gold Spot. What does the chart tell us?

