# PRUSIK ASIA FUND PLC
# PRUSIK INVESTMENT MANAGEMENT LLP

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***An Independent, Asian Specialist, Investment Management Team***

**NAV Updates**

| *Series* | *July 10* | *MTD* | *YTD* |
|---|---|---|---|
| Class A | 153.95 | 0.96% | -13.56% |
| Class B | 154.02 | 0.95% | -13.55% |
| Class C GBP | 83.29 | 0.63% | -14.16% |
| Class D SGD | 213.96 | 0.91 % | |

Fund Size $248m

**NAV Updates**

| *Series* | *Aug 10* | *MTD* | *YTD* |
|---|---|---|---|
| Class A | 158.54 | 2.98% | -10.98% |
| Class B | 158.62 | 2.99% | -10.97% |
| Class C GBP | 85.89 | 3.12% | -11.48% |
| Class D SGD | 220.49 | 3.05% | |

Fund Size $235m

**Performance**

| | |
|---|---|
| 2005Q4 | +8.86% |
| 2006 | +33.94% |
| 2007 | +21.88% |
| 2008 | -20.84% |
| 2009 | +26.59% |
| 2010 (YTD) | -10.98% |

The fund rose 0.96% in July and rose by a further 2.98% in August. Asia continues to display very clearly its lack of homogeneity. Year to date performances are hugely varied with over 50% difference between best and worst performing country index. The key to the latter part of the year will be whether this can remain the case, leaving Asia in a very interesting place for investors with a mind to pick and chose, but possibly dull from an overall index perspective. The risk is that another exogenous shock from outside the region increases correlation once again as investors try to reduce risk. Although we believe that another round of distressing news from the West is actually quite possible, we are simultaneously struck by how vibrant and busy many of the domestic economies are across the region. Therefore we cannot help but feel that the right countries and the right companies in Asia still afford, at worst, good refuge for overseas investors and in fact may actually continue to deliver strong returns especially if western governments continue with money creation policies which could flood the better growth areas of the world with liquidity.

Given the excellent growth numbers we are seeing in Asia, a key question is: Why isn't the region performing better? We think the answer lies in a couple of simple observations. Firstly, the external facing areas of the region, manufacturing, exporters and parts of the economy exposed to this, remain at risk. Despite rapid growth in the domestic economies, this remains a very significant part of many economies especially in North Asia. Secondly, the new 'monetary policy' in Asia that we have written about previously is certainly acting as a brake on what would historically by now be a large asset bull market. Governments in China, Hong Kong, and Singapore have taken strong steps to curtail speculation in the property markets and to prevent overzealous lending in general, leaving another large portion of the stock market less appealing - thanks to perceived policy

*Prusik Asia Fund plc (the "Fund") is an open-ended investment company with variable capital incorporated with limited liability in Ireland under the Companies Acts 1963 to 2005 with registration number 407740 and established as an undertaking for collective investment in transferable securities pursuant to the European Communities (Undertakings for Collective Investment in Transferable Securities) Regulations, 2003, as amended).*
*Prusik Investment Management LLP is authorized and regulated by the Financial Services Authority (FSA).*

risk. Finally, China continues to cast a pall over the region which is not just air pollution. Traditionally, sentiment has largely been drawn from what the government is perceived to be able to achieve in China. The view from a distance is that the Chinese government can control everything and will successfully engineer just the right amount of growth at the right time. The view from those close to Chinese politics is that there is currently tremendous disagreement amongst the top politicians and a sense of fear that they do not have the control they want. The extraordinary rumour last week, since clearly proven not to be true, that the head of People's Bank of China had 'fled' to America was indicative. Whilst laughable on one level, it does suggest that the politics must be in some disarray for something like that to be circulated at all.

**Prusik Asia Fund**

The Prusik Asia Fund portfolio continues to remain in "all weather" stocks which we believe can deliver a good total return over the year in any environment. These stocks are chosen for their defensive well-managed businesses, high dividend yield and high ROIC / low valuation combination as well as for their appropriate levels of trading liquidity for the fund. We have slightly increased our exposure to Malaysia, Singapore and India and also taken a first step to re-enter a newly calm Thailand, where foreign ownership and valuations are much lower than those in Indonesia but a strong domestic story is building. We have reduced our Hong Kong and China exposure accordingly. We remain quite cautious on what the world might bring but increasingly confident that the right stocks in Asia can do very well. August was a good testament to our view.

**Technical analysis**

We apologised last report for bringing 'dark arts' into our review, but do feel it's important to be aware that if a stock market loses technical support then it also loses the confidence of a significant portion of investors. There was a notable development last month with a new signal suggesting caution is warranted in the US. The measures which we follow are in fact intellectually satisfying in that they measure and indicate the levels of coherence within the market itself. For example, how many new 12 months highs and lows are seen on the same day and other factors which aim to 'cross check' sanity levels within the stock market itself. It seems that the stock market is now showing signs of severe internal incoherence and distress and although statistically this can lead to nothing, the percentage probability once this signal is given of a meaningful decline rises to about 30%. Furthermore, as we write, a rare signal has been generated in the volatility measure VIX, suggesting downside for equities.

**M&A**

On a more positive note we are very

pleased to see a break out in M&A activity. Given how strong corporate cash flows are and how underutilised corporate balance sheets are it is a relief to finally see some action and August saw the strongest burst of deal making for that month in over a decade. If this momentum continues then the very early stage recovery in bank lending that emerged only a matter of weeks ago could become a more persistent trend. This would be excellent news for the globe, finally transmitting some of the cash from the sidelines to the real economy and giving the West a much better chance of achieving the 'inflation outcome' so needed to resolve the debt problems. We are particularly pleased to see the main sectors in the M&A spotlight include some of our favourite themes such as gold, food and telecoms. In the telecoms sector worldwide corporate activity is set to total over $285 billion, surpassing the previous record set in 2005 and highlighting the need to increase capacity in mobile broadband as data traffic explodes. This should be very positive for the mobile telecom sector, which remains our largest theme.

**Mobile Telecom**

Mobile companies around the world were notable for their out-performance during August and this theme now seems to be gathering some comments in the press. To see what is happening in the sector it is worth glancing at Japan's NTT DoCoMo which will see data revenue surpass voice revenue next year. Today's data Average Revenue Per User is Y2,450 whilst voice ARPU is Y2,900 but the data revenue will increase as smart phones and tablets, such as the iPad gain popularity. As this changeover takes place all manner of new revenue sources will emerge such as content provision and the ability to charge per quantity of data used. In dollar terms DoCoMo is up 21% year to date.

**Wages**

Rumour has it that top business advisors to the British government are strongly warning of a possible sharp increase in union activity and, as we write, the London Underground is suffering some strike action. Perhaps, before acting, British workers should take a judicious look at their US counterparts who are suffering savage wage cuts in the order of 2 – 7%, especially at local and state government level. There the jobless numbers continue to be quite shocking and a recent visit to California by a Prusik contact revealed that anyone now lucky enough to find new employment in that state, at least, now negotiates first over not the incoming package but indeed what will happen if and when the job is ended.

Meanwhile in Asia, wages continue to rocket skywards. In an unprecedented move in Hong Kong, last month, a minimum wage was set, at HK$ 33 per hour, causing some pain amongst the fast food operators and some hue and cry over the passing on of the world's most *'laissez-faire'* free market economy. Meanwhile although wages in China are well known to be rising sharply after the breakout of labour unrest, it is less well known that wages are also rising in Bangladesh, which has been widely tipped to benefit from any exodus of the lowest end manufacturers in China. Here, following some strikes amongst textile workers there is a call for wages to triple from US$ 25 to US$ 70 per month.

As an aside, it is very unlikely that wages in China will not continue to rise. China's Premier, Wen Jiabao, told a visiting delegation from Japan last Sunday that Japanese companies were exploiting Chinese workers by not paying them decent wages. Even leaving aside the government's desires, plentiful cheap labour in China is coming to an end. The number of youngsters entering the labour force will start declining from this year and is set to fall by 30% in the coming 10 years. Older workers are traditionally less flexible and of those in their 40's only 11% are statistically likely migrate to find work compared to 24% of their 16 – 30 year old counterparts.

**Inventories**

When one starts to look at inventories, this dramatic shift in power over wages will be more restrained.  Even as early as May before the Greek crisis unfolded, there were signs that inventories were starting to increase. Although one would expect that raw material inventories might increase as demand recovers, there are recent signs of build up in the finished goods sector. In the Korea Times recently, LG Displays' CFO was quoted as saying that 'TV set makers have been missing their targets since May due to weaker demand which is prompting them to remain conservative in their panel purchases. Their inventory levels have risen by one or two weeks'. This needs to be watched closely but there is a risk that the next move is another leg down in US import prices. Indeed in June we saw import prices in the US fall by 1.3% which was the sharpest monthly drop since March 2009 and the first since June 2009. The US terms of trade index has jumped accordingly and in tandem we saw the July terms of trade numbers in Asia deteriorate quite dramatically. In July, China's terms of trade fell 19.8%, Japan's fell 8.5%, Korea's fell 6.8% and Taiwan's fell 2.6%. Some of these big moves can be accounted for by wage and currency shifts but the speed with which the surplus production will be consumed will depend on how quickly western balance sheets are repaired. In Europe, at least, the headline numbers suggest this may be happening faster than in previous cycles.

**Food**

One of our longest standing investment themes has re-emerged this summer with a vengeance. Soft commodity prices have surged once again thanks to a drought in Russia and parts of Africa and Asia, floods in New England, south eastern USA and not least Pakistan, and the arrival of La Nina which threatens crops in the second half of the year. Scientists are pointing out that extreme weather events are happening more often and with higher intensity than ever before. Moreover, 2010 has so far been the hottest on record and an incredible 17 countries have reported new record peak temperatures. In a paper just published in *Nature*, by Chinese scientists, it is argued that average temperatures in China have risen by 1.2°C since 1960 and will increase by another 1 to 5°C by 2100. They also write that food yields could fall as a result of climate change by as much as 13% by 2050. Indeed wheat yields in China already fell 4.5% between 1979 and 2000 thanks to rising temperatures. Furthermore as emerging countries add more meat to their diet, food demand could increase as much as by 50% in the coming 20 years. In order to meet this demand at current crop yields some 2.5bn additional hectares of agricultural land will be needed but only 750mn may be available, spread over 95 countries.

With such statistics it is hardly surprising that interest in buying agribusinesses is rising and it is possible that BHP Billiton's recent bid for Potash will trigger renewed vigour in this sector. In Asia we are constantly short of good quality ways of investing in food, with plantations usually top of the list. Here share prices remain surprisingly muted despite expectations of at least a 10% appreciation in palm oil prices as the weather closes in during the latter part of the year.

**Domestic Singapore**

Singapore is booming. A record 950,000 visitors arrived in June, up 27% yoy and in the first half a total of 5.5mn new arrivals hit a new record 9% higher than the previous peak. The second half, which is traditionally seasonally stronger, promises to be even better with Formula 1 and Youth Olympic events further fuelling demand.  Prusik's recent visit confirms this. Anecdotally there is a shortage of taxis, with a half hour wait not uncommon, whilst restaurants are full, hotel room rates are up over 20% year to date and even getting one is a struggle, with average occupancy rising to over 88%. One major new draw in Singapore are the new attractions, Universal Studios, currently 'at capacity' according to management, an aquarium, but the jewel in the crown is the two new casinos. Asian gamblers behave very differently to those in Las Vegas. They take their gambling very seriously and many believe they can beat the house. Consequently they use very few of the enticements that social gamblers like, such as free drinks, leaving casino margins nicely intact.

**Genting Singapore**

In our June monthly, we wrote about Genting Singapore and how we expected them to be a major beneficiary of the tourist arrivals into the region. In fact Genting's Q2 results thumped all expectations, including ours which were well above market estimates. These results beat forecasts on all levels from sales growth to profit margins and cash flow generation. On a per day basis, we estimate that the Resorts World Sentosa casino generated gross gaming revenue of about S$10mn during 2Q versus S$7-8mn in Q1 which compares well to its only competition Marina Bay Sands, which made turnover of S$4-5mn.  Extrapolating this data, it appears that Singapore's gaming market could be worth a whopping S$5.5bn with RWS having a market share of 70%.  Our expectation is that RWS is the key beneficiary of the new tourism and gambling boom and we expect the competitive environment to remain benign due to the stretched balance sheet at the parent level of competitor Marina Bay Sands.

We also believe the additional attractions at RWS, including Universal Studios, mean that RWS will be the resort of choice for all categories of visitors to Singapore.  Universal is expected to be fully functional by the end of the year which will start contributing to top line growth and enhance margins further going into 2011.

The additional positive is that they have managed to successfully sell their UK operations to their parents at attractive valuations for Genting Singapore shareholders.  This provides a decent buffer on the balance sheet to explore other growth opportunities in Asia or return capital to shareholders. Valuations still look attractive relative to our growth estimates and the company generates a ROE of 18% against a cost of equity of 6.5%.

The portfolio has a 12% weighting in Singapore with every holding directly exposed to this domestic growth story, through commercial and retail property REITs, advertising revenue and newspaper sales, mobile telephony, hospitality and tourism.

**AviChina**

There are more private helicopters in the city of Sao Paulo than in the whole of China. Currently there are around 30,000 civilian helicopters worldwide, but China has less than 200. Indeed the number of civilian helicopters per one million persons stands at 42 in the US, 56 in Canada, 15 in the UK and 6.3 in Japan, but a mere 0.13 in China.

This is partly due to the very rigid control of low flying airspace in China but in March 2009, Guangdong Province set about opening low-altitude airspace for the Chinese air force and in July this year they opened it for civil flights. We believe this pioneers the way forward for all regional low-altitude airspace to be completely liberalized by the government in near future.

AviChina will be one of the biggest beneficiaries due to its incomparable position in the helicopter and general-purpose aircraft sector.

AviChina (along with its parent AVIC) is the leading manufacturer of aviation products in China. Almost all domestic aviation product makers are affiliated with either AVIC or AviChina. Having restructured assets last year, AviChina has embarked on the building of a comprehensive aviation enterprise. It disposed of its underperforming automobile business and replaced it with aviation assets possessing much greater synergy with the existing businesses, better growth potential and higher margins. The launch of AVIC's large aircraft project in 2008 represented a beginning of the take-off (sorry) for the domestic commercial aviation industry in China. We believe that the coming 5-10 years will see a golden age in terms of growth in the aviation market in China as tourism and international travel rises towards western levels. No doubt the Chinese government wants to fast track the domestic manufacture of commercial aircraft and keep the benefits of this important trend at home. As the listed flagship of the country's aviation industry, AviChina is almost uniquely positioned to enjoy the resulting benefits and should be valued accordingly.

It is for all of these reasons that a earnings CAGR of 23% over the next 3 years, or even higher if we take into consideration the potential asset injections from the parent company, is anticipated, making this company seem very attractive.

**Lanco**

Lanco has been and continues to be one of our larger holdings in the fund for the simple reason that it provides the best visibility on the growth opportunity in the Indian power sector at the cheapest valuations. We believe that the current share price is still not factoring in upside from the new under-development project pipeline (4,700 MW of coal-based and gas projects) and that this will change. The company has delivered on execution, increasing their generating capacity fourfold from 500MW at end FY09 to 2,100MW now. We expect this to double again to 4,000 MW over the next 12 months and they have a robust pipeline amounting to 10,000MW by 2015. We believe that merchant power rates will remain strong in the near-to-medium term and, along with capacity increases, will continue to result in strong operating results for the company. With every milestone passed, we expect more attention will be drawn on to Lanco's execution capabilities and cheap valuations.

**Going to the gym**

Readers will know how keen we are on the healthcare industry, domestic consumption themes, especially those involving lifestyle, and any beneficiaries of the rapid growth of urban populations across the region. During Prusik's recent trip to India, we met with Talwalker who are the leading company in the health and wellness sector, offering a complete suite of fitness solutions to its customers. These include the actual gym experience, nutrition counselling, spa therapy, aerobic classes, yoga and so on. The Indian health and wellness services industry is currently worth about US$2.3bn and is expected to grow 30-35% per annum for the next 5 years. Gym penetration levels are much lower than even the Asia Pacific average with total gym memberships in India at 0.23mn members vs. 2.6mn even in China!

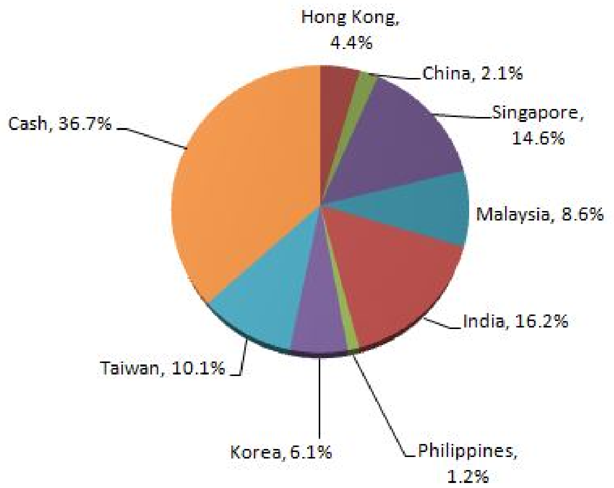
Talwalkers is not only dominant in India but is the 2nd biggest gym chain in Asia (after a multinational brand) and they have a market share of above 10% in India's organised sector. They are currently in 41 cities with 79 gyms. Talwalkers are targeting to end the year with 100 gyms and will look to add 30-35 gyms per annum for next 2 years with a target of 200-225 gyms in 100 cities by 2014. We estimate the company can grow revenues this year by 75% and next year by 50% with profits driven by rising margins thanks to an increase in sales of additional services, such as food, personal training and spa treatments, which are higher margin relative to the basic gym membership. The company already enjoys a decent ROE of 20% but the better margins and higher asset turns will drive this up by another 10% in the coming year. On our estimates the stock is trading on a PE of 18x March 2012 which we feel is significantly undervalued relative to its strong growth prospects and unique position as the dominant listed company in India in this sector.

At the end of August, the combined investments of the Prusik Asia Fund, were trading on a weighted average CY11E PER of 16.9x with 20% EPS growth forecast for 2010 generating an ROE of 23% for that year.

Amit is currently in Singapore and India whilst Heather is travelling to Hong Kong next week to attend the CLSA investment forum.

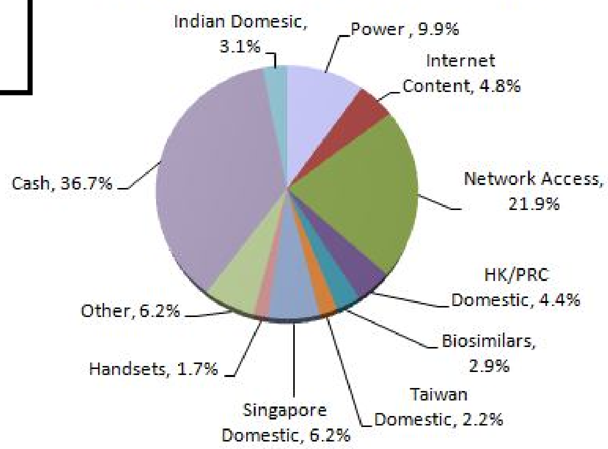
# PRUSIK ASIA FUND
# TOP LINE FIGURES — AUGUST 2010

**Prusik Asia Fund by Country**




| | |
|---|---|
| Number of holdings | 26 |
| Percentage of Fund invested | 63.3% |

**Prusik Asia Fund by Theme**




| | Top 5 Holdings | % |
|---|---|---|
| 1 | HONGKONG ELECTRIC HOLDINGS | 4.4% |
| 2 | LANCO INFRATECH LTD | 3.7% |
| 3 | CAPITACOMMERCIAL TRUST | 3.5% |
| 4 | BHARTI AIRTEL LTD | 3.3% |
| 5 | BHARAT HEAVY ELECTRICALS | 3.2% |

**PAF Monthly Performance**

| Year | Jan | Feb | Mar | Apr | May | Jun | Jul | Aug | Sep | Oct | Nov | Dec | YTD |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| 2005 | | | | | | | | | | -1.9 | 5.64 | 5.08 | 8.86 |
| 2006 | 7.71 | 0.09 | 1.84 | 10.1 | -1.95 | -0.45 | -1.72 | 0.02 | 1.23 | 3.9 | 7.64 | 1.97 | 33.94 |
| 2007 | -0.01 | 1.28 | 3.05 | 4.08 | 3.58 | 4.79 | 3.77 | -3.75 | 5.67 | 2.61 | -6.33 | 1.93 | 21.88 |
| 2008 | -6.78 | 6.91 | -8.06 | 1.81 | 0.67 | -7.69 | 0.21 | -5.34 | -5.33 | -7.37 | 0.02 | 9.75 | -20.84 |
| 2009 | -6.9 | -2.9 | 11.2 | 4.46 | 10.7 | -2.69 | 6.77 | -4.94 | 6.42 | -2.45 | 4.08 | 2.12 | 26.59 |
| 2010 | -9.67 | -2.62 | 3.66 | 1.67 | -7.15 | -0.54 | 0.96 | 2.98 | | | | | -10.98 |

**Key Parties to Fund**

| | |
|---|---|
| Investment Manager | Prusik Investment Management LLP |
| Administrator | Citi Hedge Fund Services (Dublin) |
| Custodian | Brown Brothers Harriman (Dublin) |
| Auditor | Ernst & Young |
| Legal Advisors | Dillon Eustace (Dublin)<br>Simmons & Simmons (London) |

**Key Terms**

| | |
|---|---|
| Denomination | USD |
| Dealing Day | Weekly (Friday) |
| Minimum Subscription | USD100,000 |
| Min Subsequent Subscription | USD10,000 |
| Subscription Notice Period | 2 business days |
| Redemption Notice Period | 2 business days |
| Dividends | |
| Class A | $ Non distributing |
| Class B | $ Distributing |
| Class C | £ Hedged Distributing |
| Class D | SGD Hedged Distributing |

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**Manager Fees**

| | |
|---|---|
| Management Fee | 1.5% p.a. paid monthly in arrears. |
| Performance Fee | 10% of NAV appreciation. With a 6% hurdle. |

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