Prusik Asia Fund Plc

FSA Authorised
Recognised Schedule 5

Prusik Investment Management LLP

An Independent Asian specialist investment manager

NAV Updates

Series	*July 09*	*MTD*	*YTD*
Class A	169.8	+6.77%	+20.70%
Class B	169.8	+6.71%	+20.65%
Class C GBP	92.52	+6.65%	+17.47%

Fund Size $415m

Series	*Aug 09*	*MTD*	*YTD*
Class A	161.41	-4.94%	+14.74%
Class B	161.49	-4.89%	+14.74%
Class C GBP	88.19	-4.68%	+11.97%

Fund Size $405m

Performance

2005Q4	+8.86%
2006	+33.94%
2007	+21.88%
2008	- 20.84%
2009(YTD)	+14.74%

The fund rose 6.8% in July and then fell back 4% in August. The portfolio was largely fully invested over this period. We have found it frustratingly hard to make the returns we would have liked to over the summer months. We feel confident that the stocks we hold have good growth and plenty of upside and have been fully invested. However, a combination of a continued rally in regional banks, regional property companies and lower quality beneficiaries of cyclical recovery has left our portfolio behind. Secondly, the fund has been heavily invested in telecoms on the back of the convergence/ mobile internet theme. This has not performed as well as we had hoped, so far, with the general view that any improvement in data revenue will be more than offset by the continued collapse in voice revenue. Thus, a lot of the profits we have made through other legs of the entire “convergence” theme (Chinese internet search and travel booking engines Baidu & C Trip), the visual display manufacturing foodchain (PrimeView, Epistar, Jusung, LG & Samsung) have been offset by the poor performance of the distributors. We are adding companies higher up in the food chain, such as the content suppliers and have reinvested in NC Soft and NHN in Korea and also added more in Taiwan. We have maintained and recently added to our investments in Gold which has suffered from the resurgent Australian dollar, not helping our performance. (see later paragraph on gold). We have no exposure to Chinese A shares, but have seen the Hong Kong counters in the portfolio a little weaker this month as a result of the slowdown in Chinese bank lending.

Since we launched Prusik we have often found one of our themes takes time to bear fruit, but have always had the luxury of plenty of other themes in the portfolio performing well thus allowing us to hold the slower ones and allow them to develop. Given we have more than the normal number dragging at the moment, and in the face of what have been extremely strong markets we have been revisiting our rationale constantly. Our conclusion is not to change tack, but to continue to add to the areas which are progressing. Indeed, as we write below we feel that some of our most recently disappointing themes – gold, mobile operators and Taiwan domestic - are ready to perform well between now and the end of the year.

As investors in the fund ourselves we share your frustrations at our under-performance during a period which has again shown Asia's increasing attractiveness relative to other parts of the world. Perhaps the hardest part of tackling a period of under performance is having the nerve to stick to the knitting and to know that circumstances will come round. We feel more strongly than ever that by the end of the year the easy money driven rally will have once again given way to something altogether more challenging. For possibly years, genuine growth will be sought globally for its rarity. We are sure that Asia, and in particular our vision of Asia, via themes where growth drivers are ultimately insulated from cyclicality will ultimately prove to be the most worthwhile investments.

China Update

There is no such thing as a smooth ride in China and in August investors once again became painfully aware that one is at the mercy of policymakers and the timing of announcements. As we had previously expected, the much needed slowdown in lending growth (RMB 1.7 trillion per month at peak to around RMB 200-300bill this month) finally came through in early August and was followed by a sharp correction in the local indices of over 20% which dragged down many counters in Hong Kong as well. More recently the authorities have also suggested that certain industries, such as steel and cement, face over capacity and they will be taking steps to curb further over expansion. This is ultimately good news for the economy. We had been recently hearing some alarming anecdotes of companies already underwater, with unused capacity, and being ordered to build more and not to worry about the offtake. In steel, for example current domestic production is around 670million tons, but actually demand is only 400-500million tons so, in any event, working through the resultant inventories will take time. Additionally, many local governments were starting to become irresponsible with excess funds some of which have made their way into the stock market or property. In all, therefore, this announcement is prudent and timely.

However, what may be for the good of China's medium term outlook is likely to mean more headwinds for the local stock exchange and related counters. We believe growth this year will remain fairly robust and not produce any nasty surprises, but that it will trend to slightly below potential as we move into next year. We do believe the government will remain supportive and step in with new measures should things slip too much, which is comforting, but it will not iron out the stop/go action in the local stock market which is further exaggerated by the retail nature of investors and their tendency to herding and high drama. In short, although China's liquidity is not tightened it is now less loose, there are plenty of new IPOs , higher share valuations and the risk of earnings disappointments due to the difficulty in passing on cost increases to also contend with. But, the real problem causing indigestion in the stock market is expectations which have perhaps been too high. Perhaps China , having been the early bird in the rally that started last November will now take a back seat while the rest of the world catches up.

There are many who believe that China will keep the rest of the world out of danger by its rapid growth. We are not so sure. While we can see tremendous growth and investment opportunities within China, the risk is in assuming the whole country will continue to operate in a way which, firstly, is predictable and, secondly, is benign to the rest of us when they, too, are struggling for growth and stability and a secure future. We know that the authorities in China place the economic health and stability of the US amongst their very highest priorities, not least because they own so many US$ assets. However, expect this concern to come on their terms. Here are a few things we believe we should be watching out for in the coming year.

Chinas Dwindling Current Account Surplus

The recent pattern has been for exports to be rather lacklustre while imports have grown rapidly fuelled by Fixed Asset Investment and inventory building. The July figures illustrate this well; exports fell 23% yoy (June was -21.4% yoy) whilst imports fell 14.9% yoy (June was -13.2% yoy). If you extrapolate the recent monthly trends into next year then Chinas trade surplus will be nearly zero by the 4Q 09. The July trade surplus was only 1.5% of 2008 GDP vs 6.8% last year. By the end of the year, if the trade surplus hits zero then China will still have a current account surplus of 3% of GDP. However, if this pace of import growth persists then China will be a current account deficit country by mid next year.

Some noted economists are already pointing out that this has quite large implications for the rest of the world, especially if this adjustment takes place so rapidly. Firstly, if China chose to keep stimulating its own economy and didn't allow its currency to weaken then it would soon become a net seller of Treasuries! In this environment it is possible to see very little US stimulus, leading to little demand, leading the circle quickly back to China needing to increase domestic stimulus and so on.

The easy way to not meet this eventuality head on at 90 miles an hour is to slow China's import demand. This will hurt the stock markets, as we have already seen, and possibly international sentiment too at some point, but in the immediate future China is showing very robust growth in many other areas of the economy and can afford to take this path.

Reverse Globalisation

In a recent WSJ the headline ' Appliance maker leaves China for US' leapt off the page. Farouk Systems, a maker of hair irons, is shifting back to Texas to 'help control quality and inventory and, in time , to bring costs down to those in China'. The same article quotes a longer speech on the same subject by Jeff Immelt of GE saying that it is now possible and important to compete from home soil as the 'American renewal will be built on technology' which requires speed and quality and the need to be closer to customers. We agree that the American renewal will be technology led and can only assume that with nearly 10% unemployment in the US, wages are so low that genuine competition with China might be possible. It is too early to say whether this is flag waving or the start of something genuine, but we shall not be too sanguine.

Supercurrency

This has been discussed before, and is reportedly supported by a number of highly regarded economists from the World Bank and beyond; but perhaps we should now start to take seriously the idea that somebody (possibly China) is planning to lead the creation of a supercurrency with which to replace the US$ as the global currency of trade. The idea might be that the new currency will be created from a broad basket including the Chinese RMB the US$ and will also be backed by gold, oil, iron ore and many other resources. We can see from China's perspective, and that of many other trading partners, that this would reduce dependency on the US$, insulate global players from potential US$ inflation and reduce currency fluctuations. The concept of including commodities is not new, but will be controversial not least because they can be subject to price manipulation. Leaving aside the medium term political implications and the immediate dent to the pride of the US, we think any such propositions becoming reality or even just becoming more widely discussed, could, in the first instance, be quite positive for the US$. China, in particular, has nothing to benefit from a very weak US$ as it holds so many US$ assets and it exports to the US too, so extreme care would be taken to include the US$ in a very supportive manner. Indeed it is possible to see this as a possible outcome after a painful period of US$ weakness. Another major implication of both US$ weakness or the creation of a new supercurrency would be a very positive impact on demand for gold (on which more below).

Mobile Internet – update

We have just seen the first substantial report from the broking community underlining our opinion that mobile operators will benefit from the arrival of 3G. Specifically they are suggesting that China Unicom, one of our holdings, will see dramatic subscriber adds as a result of the new tarrif structure and internet access offerings they have on their new WCDMA 3G network. They believe that Average Revenue Per Subscriber could be as much as RMB 100 for the new 3G rates versus the current average of RMB 41 for 2G GSM subscribers. Unicom have also just announced they have signed with Apple to carry the iPhone from 4Q 09 which will help with publicity for their new 3G system and it is also important to note that Unicom also has the same standard as international operators , making access to handsets and handset choice more attractive for users than at other Chinese operators. Although, globally, handset sales are down 6.1% in 2Q 09 YOY while smart phone sales are up 27% in the same period, it will probably not be really crystal clear to the pessimists until the early part of next year that WDCDMA subscriber numbers are growing strongly. At that point it will be hard to refute that the same beneficial impact should be felt at most 3G mobile operators, many of whom are still trading on single digit PE multiples and have dividend yields over 5%.

Augmented Reality

As Arthur C Clarke wrote ' Any sufficiently advanced technology is indistinguishable from magic'. As we enter the content centric age in technology (the last age was the network centric, prior to that PC centric and, before, system centric) we urge you to remember that whilst much of the world economy maybe foundering, innovation is oblivious to economics. The next technology boom is already with us because the foundations, mobile internet and cloud computing, are in place and we will be continually startled by the speed of life and business changing innovation.
One brand new example is a new update to the Apple operating system which allows the operator to layer information over in-coming images. Layar, as it is called, is already available in the Netherlands where it was developed and it allows the user to download information whilst viewing images through the camera on the phone , much like a pilot might see information on his visor in state-of-the-art fighter aircraft. At yankodesign.com you can see an example where the user can view a town through the cam-

era lens and choose whether to view the tourist information, which will include historical data, cultural information etc or consumer information such as shop opening and special offers. There are also applications for viewing a house and seeing information about whether it is for sale, for how much, which agent, viewing pictures of the interior and so on.
This is just one of many new content driven applications which will drive users to buy smart phones and pay more for their mobile internet services in the explosion of internet usage and data traffic that is yet to come.

Privacy

With ubiquitous mobile phone cameras, Twitter and Facebook, Layar and lets not forget Google, and now the incoming mobile internet it is possible to imagine a future world where there is very little privacy. Not much more than a century ago privacy was rare for different reasons as people lived in small communities and with large families in small houses and were bound to their employers. This is still not uncommon in developing countries but for the west, could it be that in a few decades time we will look back on privacy as the anomaly?

Bill to Mobile

In our search for new themes, we are always interested in new patterns of behaviour. One intriguing example of this has been the increasing use of the mobile phone as a means of making small payments in places as far and wide as Africa and Japan.

In Korea currently around 50% of online purchases of music, film and games items are now paid via mobiles! The company which facilitates this, Danal, which has been operating bill to mobile payments in Korea since 2000, now has over half the market share in handling online payments in Korea, owns international as well as domestic patents on its software and is about to launch in the US (with Verizon but more US mobile companies will be recruited later) in the new year with Taiwan ongoing and China to follow.

Unlike premium SMS which is another bill to mobile process, Danal offers a swift transaction process which not only provides both the content provider and mobile phone operator with much better security regarding the purchaser and a bigger slice of the turnover, but is also very popular with the users. Firstly, bill to mobile gives the purchaser the opportunity to delay payment till his bill arrives at month end but also, crucially, the transaction process is an easy two step entry of a mobile phone number and ID and so is instantly more appealing than the laborious entering of credit card details.

In Korea, Danal is still enjoying growth of about 20% but it has other businesses such as online games which are less easy to forecast returns from and have lower margins. In the US however, Danal has negotiated a 6% share in transaction value (vs 2% in Korea) and stands in the deal alongside Verizon who will take 9% of the share, with the rest going to the content provider. Verizon will put Danal's servers into their server rooms making it very hard for other competitors to enter.

The numbers in the US are very exciting. This year it is conservatively estimated that some US$10billion (up from US$6.6bill in 2008) of transactions will take place online in the US in the segment Danal is targeting. The experience in Taiwan and Korea was that 15% of transactions switched to bill to mobile in year 1 which bodes very well for Danal. Additionally the company is convinced that the availability of bill to mobile actually increases transaction numbers as well, given it is so easy and attractive to users. Certainly in Korea online transactions went from W200bill to W1.4 trillion in 2 years after bill to mobile was launched. It is tempting to dismiss that as being part of the early growth in internet. However, it is important not to forget we are entering another gigantic spell of growth in internet usage via mobile/3G and the use of smart phones, the psychology of bill to mobile therefore is likely to feel very natural to users. As a result Danal is looking likely to at least double its revenue growth in the coming year and profits may rise more given margins on the US business are so attractive. Currently the company trades on 14x 2010 earnings, and we like the fact that at this time it is only followed by two small local brokers.

Finally, we must point out that the deal Danal has secured with Verizon hands 9% of all bill to mobile revenue to the mobile operator! Most of this will presumably go straight to the bottom line. Taking an unrealistic back of the envelope approach to make a point, whilst $900million may not be huge in revenue terms for any mobile company and it will eventually be shared amongst them, nonetheless $900million in additional profits to Verizon would have increased net income by 12% last year!

Taiwan Domestic – update

With no fanfare Taiwan is quietly one of the better performing stocks markets in Asia this year. We ask you to show us where else in the world have you seen property prices double this year? And yet in a somewhat unedifying suburb of Taipei residential prices have indeed risen from $2000/sq foot to $4000/sq foot! However, if you ask a local whether they are thinking of buying property they will probably say yes but not yet, but they will when it falls by another 10% in value!

Taiwan is interesting for many different reasons.

Firstly, they are a master class in how to live with deflation. This is a country which enjoys global leadership in the manufacture of a myriad of technologies all of which are subject to Moores Law. They can live off the smell of an oily rag and make profits. This means companies are in fact extremely leanly managed. For example, cement in Taiwan is produced at a GP per tonne 30% higher than in China as there has been no demand for cement in Taiwan. However, it means their whole mentality is geared to expecting more of the same which is why reversing consumption habits of the past decade will take time.

Secondly, as a result of the point above and partly also due to living for decades in constant political fear of China, the Taiwanese live spectacularly below their means. As we have written about extensively before, huge savings are kept offshore, both private and corporate, which could change the landscape of Taiwan in a generation if brought home and spent. Meanwhile, the average car in Taiwan is between 13 and 14 years old! In Taiwan everyone eats a lunchbox, the usual cost of which is $50 (US$ 1.51!) but a $60 lunchbox is considered to be 'gold dusted' to cost so much!

Thirdly, as a result of such modest consumption many of the key sectors are hugely consolidated. For example, only two department stores comprise 80% of all department store sales, the top three hypermarkets have 75% combined market share, whilst 80% of cement demand is satisfied by the two main players. As a result, when the consumer finally gets moving, the stock market will be a truly extraordi-

nary place.
Fourthly, Taiwan money supply M2 as a percentage of GDP stands at a whopping 2.25x compared with 1.2x in Hong Kong and 1.5x in Singapore. Fixed asset investment has remained below 20% of GDP since 1995 and banks are offering 1% teaser rates for mortgages. Meanwhile the tax rate is still 40% but this could fall, whilst the government for the first time in a decade is beginning some major infrastructure projects.

We note that the Chinese signing of the MOU with Taiwan is still to come later this autumn. It is widely anticipated but should nonetheless keep the tone positive. Further to that we expect a steady trickle of related news flow as China shops for assets in Taiwan.

Finally, all of the above adds up to a very positive outlook for Taiwan on a multi year basis. Taiwan proved in the 1989 boom that it can march to the sound of its own tune and anyone living there will tell you how little attention is often paid to world events. We are a long way from even starting to repeat that heady period of the 80's but we do think that Taiwan has a strong chance to become a remarkable outperformer in a world with fewer uncorrelated opportunities.

Gold

Since its low in March 2001 at $250, gold has nearly tripled in value. It has, since late 2001, been part of our portfolios, both professional and personal, and has been a very defensive store of wealth over the recent turbulent times. We believe the bull market in gold is far from over. Indeed at the time of writing, gold stands less than 10% away from the highs of this bull market which came in early 2008, since when it has formed a beautiful reverse head and shoulders chart pattern which has technical analysts drooling over the gains to come.

But what of the fundamentals? In the first instance many argue that the future of gold depends on an inflationary outcome to the current economic crisis. Without delving in to the guts of that argument here, although we have sympathy to that view, we prefer to note that other factors are adding up fast to suggest gold prices will go higher from here – perhaps even giving us a sneak preview as to the outcome of the inflation/deflation debate?

Our arguments are very simply about supply and demand combined with the very real likelihood that somebody somewhere (we think China, probably) will initiate a new currency backed to a greater or lesser degree with gold.
Firstly, on supply, global central bank net sales of gold fell 83% yoy in the first half of 2009, with purchases actually rising more recently turning central bankers into net buyers! Indeed in 1H09 purchases were already nearly double the same period in 08. It is suggested that by the end of 2009 central bank gold sales will fall to the lowest level since 1994 or 71% below the average of the last decade. What is more there is no indication that sales will recover again next year. This leaves the IMF as the last remaining major seller of gold, with another round of selling due to commence next year, but aside from this, the 488 tons per year of sales we have become used to looks set to dry up.

Secondly, South Africa's gold production has fallen for 20 years, falling 75% from its peak to the lowest level since 1922 due to a combination of chronic energy shortages, terrible labour problems and declining ore grades. China is now the worlds largest producer of gold. However, China's supply of gold seems likely to dwindle in the coming decade. Some data suggests that Chinas reserves of economically viable gold will last only 4 years whilst the total reserve base would only last 14 years at the current extraction rates.

Thirdly, and perhaps more profoundly, it is possible we have seen ‘peak gold’ production for the world. According to the United States Geological Survey over two thirds of all gold ever extracted has been mined in the past 50 years and it would seem that we have now mined over 60% of all the gold available. Indeed recently, despite exploration spending increasing by 6 fold since 2001, the actual increase of gold resources from new discoveries has fallen sharply. Although new resources have been opened by the large miners, the depletion at smaller mines has meant that overall resources have depleted at double the rate of new openings. Furthermore, this has been taking place against a backdrop of rising gold prices where more expensively extracted gold deposits are becoming viable once more. The raw statistics from the major gold producing countries are quite shocking. US production peaked in 1998 and has since fallen 37%, Australia peaked in 1997 and has fallen 30% since, in Canada the peak was 1991 and since production has dropped 43% while Indonesia and Peru have both seen more recent peaks followed by declines. These countries comprise nearly half of all global output.

Finally, it would seem that we have also sold ahead our ability to ramp up production as prices increase. The old mining adage of ‘worst grade first, best grade last’ was ignored in the bear market decades of low priced gold and the desperate need to stay in business, so any hope of being able to ramp up new supply to meet rising prices is likely to be in vain.

On demand, China is also the worlds largest consumer of gold. Last year, despite the crisis, per capita consumption of gold rose 8% yoy although, as with many consumption statistics, Chinas average consumption of gold remains 85% below the world average.

Jewellery demand is still the largest source of global gold demand, accounting for 57% last year. Although it has fallen 35% since the peak in 1997, gold prices have continued to rise fuelled by investment demand. Coin minting rose 40% last year to a 20 year high whilst bar hoarding rose 62%. ETFs and online trading have also widened the availability of gold to investors. In total therefore, gold demand rose 7% last year and was up 35% YOY in 1Q09. Supply has been met in part by recycling and destocking from jewellery makers, but this has fallen away nearly 40% in the past quarter.

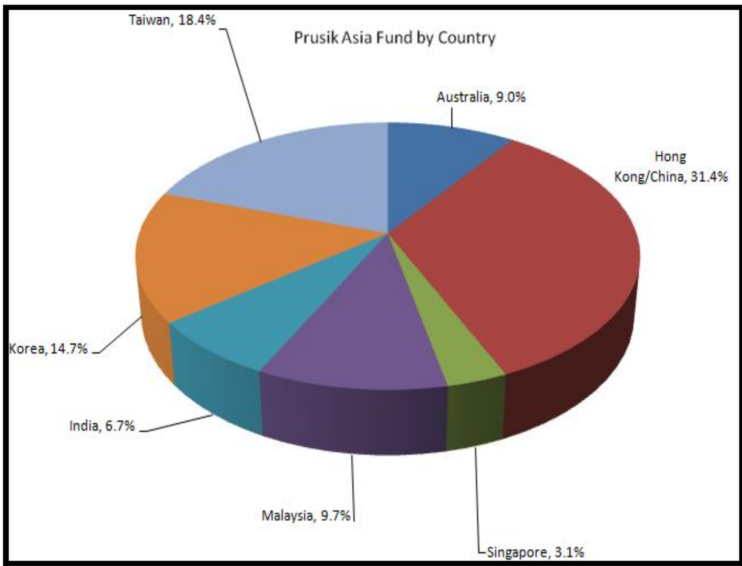
In summary, gold supply will struggle to match ongoing demand. Should demand increase, and certainly the evidence suggests this will be the case from the average investor to the possible backing of a new currency, the price could move sharply higher from here.

We have recently added to our holdings in gold. The Australian miners look particularly cheap versus international counterparts with Lihir and Newcrest trading at a market cap to resource ounce ratio of below 200 versus international miners between 350 and 550! Not surprisingly we have seen the beginnings of M&A which means these cheap levels will not last long, especially if gold breaks out to new highs, as we expect, before long.

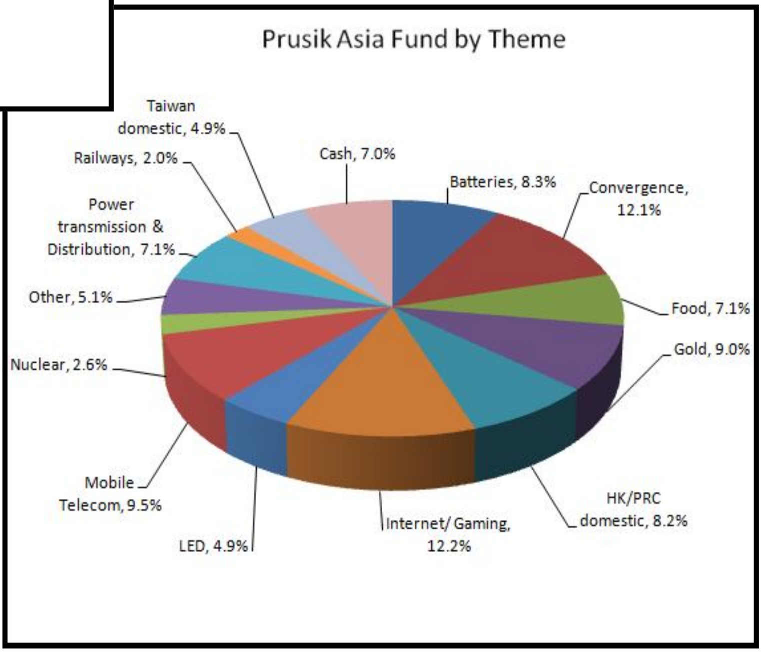
The portfolio trades 21x 2009 forecast earnings and 16.5x 2010 forecast earnings with earnings growth of 27% in 2010, generating an ROE of 20% for that year. This includes gold, pushing up the multiple.

Heather departs Hong Kong, Korea, Malaysia and Singapore in 10 days time. Ed to Shanghai, Hong Kong and Singapore. Amit is currently holed up in Hyderabad.

Prusik Asia Fund
Top Line Figures — July/August 2009



Number of holdings	**39**
Percentage of Fund invested	**93%**



Top 5 Holdings	%
ZTE	3.7%
LG Electronics	3.4%
Lihir	3.4%
Taiwan Fertiliser	3.4%
BHEL	3.3%

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					14.74

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) 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	None
Class B	Annual
Class C	Annual

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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.