Prusik Asia Fund Plc

FSA Authorised
Recognised Schedule 5

Prusik Investment Management LLP

An Independent Asian specialist investment manager

NAV Updates

Series	*31st December '06*	*MTD*	*YTD*
Class A	145.81	+1.97%	33.94%
Class B	145.81	+1.97%	33.94%
Class C GBP	78.64	+1.93%	

Fund Size $200m

NAV Update	**31st December 2006**
Class A USD	
Non distributing	USD145.81
Class B USD	
Distributing*	USD145.81
Class C GBP	
Distributing*	GBP 78.64

The fund rose 1.97% in December. Unfortunately, progress was not helped by events in Thailand, on which more below. China has also become a major driver of the recent upward index move. This is an area where we have been, until recently, too cautious. However, in December we added a number of interesting but not too expensively valued companies.

Asia continues to offer amongst the best investment opportunities in the world, given its strong domestic economies, broad lack of leverage from government to individual level and moderately priced assets like property in comparison with many western countries. However, Asian stock market valuations have been climbing and are now nearer to the global average, so perhaps the easy money has been made shorter term.

With increasingly huge amounts of the global economy owned by leveraged vehicles, sensitivity to and expectations on interest rate changes are now disproportionately important.

We note that earnings are abnormally high. For example, in the US, the after tax profit share of GDP is now 70% above the long term trend, a level only seen once before (in 1929, but we don't want to be emotive!). What is anomalous is that consumers have kept spending in the face of globally soft labour costs (China being an exception where wage growth is robust) and that companies have so far resisted the temptation to add capacity which would bring down returns. Instead they have preferred to invest in either their own paper or other companies. Much of the earnings bubble, if we can call it that, appears to be in global financial sector earnings.

We therefore find ourselves in a situation which may continue until such time as the earnings mean revert or interest rates rise, barring of, course, the unforeseen. After the very strong increases in share prices everywhere in recent weeks, the risks of a correction must be rising.

Therefore, the need for careful stock picking and investing in secure industry change that has drivers which are insulated from the economic cycle becomes more important than ever.

Thailand

The Thai Central Bank's decision to impose draconian capital controls, and its reversal 48 hours later is the equivalent, to us, of a serious breach of corporate governance and for that we give no second chances. This is unfortunate as we have found some attractively valued companies in Thailand beginning to restructure under new foreign ownership. Nonetheless, we have reduced our exposure here, until such time as the country has a new government whose policies towards international investors are more reliable. However, we do feel some sympathy for those countries who have been brave enough to allow their currencies to strengthen only to watch China carefully managing the RMB to keep a competitive upper hand. The episode cost the fund, we estimate, about 75basis points only, thanks to Tony's expert dealing and a swift response.

Infrastructure/ Ultra High Voltage Direct Current Cables

The environment has long been an area of thematic interest to us. Water treatment has been one such area, but the sector has now become crowded with new operators and returns are falling. We fear the same may be about to occur for emissions control companies operating in China. For us rising returns, not top line growth, are the key to a successful investment. Our continued search for companies which offer environmentally better solutions and, ideally, energy saving ones as well, has led us to a new field, which embraces both drivers. Better still, technological barriers to entry are high and growth looks as though it is about to explode.

Way back in the time of Thomas Edison the first commercially transmitted electricity was direct current DC. This was quickly superceded by alternating current AC (albeit against Edisons best advice) which could be better transmitted over long distances at low voltages. DC has been making a comeback. Recently, a technology leap allowing transmission of Ultra High Voltage DC (i.e. over 800Kv when previously 600Kv was the maximum) has resulted in so many advantages that it will likely dominate any new power transmission systems that are being built.

So what are these advantages? Charged at the same voltage, HVDC transmission efficiency is twice that of HVAC over long distances and there is no increased loss of energy as distance increases. Indeed with new insulating materials such as extruded polyethylene, UHVDC can also be cheaper to run at distances as low as 60km.
A UHVDC system is also technically cheaper to maintain, more stable and easier to control. It requires a smaller 'right of way' for power transmitted (it has a smaller electromagnetic field), cables are lighter, so pylons are smaller and it is bi-directional. In short it is the likely future of power transmission grids in most emerging countries but also opens up massive potential for alternative energy sources from which long distance power transmission previously would have been too costly, such as offshore wind farms or solar panels in the desert.

In a bold move into this new area, China, which has recently announced plans to spend some US$25billion on power systems is planning to spend about half on building 22 UHVDC projects. Previously, international companies such as ABB and Siemens have dominated the power transmission sector in China. However, the government has recently pledged to use local companies of which there are only two who possess the technology to make the key components. One is XJ Electric an A share listed company where notably in 2005 the HVDC division rose from nil to 11% of revenue, and also brought higher margins. We have also been talking to cable manufacturers in Taiwan, Korea and India, where a number of new UHVDC projects are also planned.

Management incentivisation in China

On a recent trip to Northern China, we were told that, 'previously a Chinese businessman's stature was measured by the number of people he managed or employed, now it is measured by the market capitalization of his company!' The Chinese Government's decision officially to allow incentive schemes therefore looks interesting.

From December, any state owned or private company can apply to the CSRC and the State Asset Administrator to issue share options to management, the impact of which could be significant. We think that state owned corporates fall into three camps: corporates where the board is unlikely to introduce an incentive scheme, corporates whose management, we think, would maximize profitability once option packages are introduced, and corporates with quasi incentive packages already in place. We think that those companies in the second camp provide particularly attractive investment opportunities as management, stimulated by an incentive package, starts to manage the business more aggressively.

The Bailian Group is an unfocused portfolio of some of Shanghai's strongest and weakest department stores. Unable to make staff redundant to reduce costs, it has, instead, to open new stores to generate staff positions. Some of its stores are earning a margin in excess of the foreign listed, highly rated PRC department store operators. However, Bailian is earning only a single digit ROE versus the 25% ROEs achieved by the foreign-listed operators. We think that the steps required to boost Bailian's ROE to 30% or more are relatively straightforward but are likely not actionable. Management's disappointment at the lack of any prospect of a profit-oriented incentive scheme was obvious.
A liquor company, whose management was about to strike its options, is an example of a corporate in the second camp. Publicly, management seemed to be overly cautious in its assessment of the prospects for a company which, we thought, was achieving outstanding 60% plus gross margins and possessed significant pricing power.

Finally, a wine company, whose management acquired half the owner's stake two years ago, is an example of a corporate in the third camp. Remuneration packages are based upon management meeting specific return targets, all of which are based upon profitability ratios not top line revenue growth. However, unfortunately, the positive impact of such measures is, often, already discounted in share prices.

40% of the benchmark, against which PRC portfolio managers are judged, consists of BOC, ICBC and China Life. Given the flow into mutual funds, this is forcing funds, alarmingly, to continue buying the key constituents of this benchmark. However, excitingly, there are over 2,000 other Shanghai listed companies, fewer than 5%

of which have any form of incentive scheme. We are therefore switching our A share facility, 5% of the fund, into three companies we feel fall into our second camp.

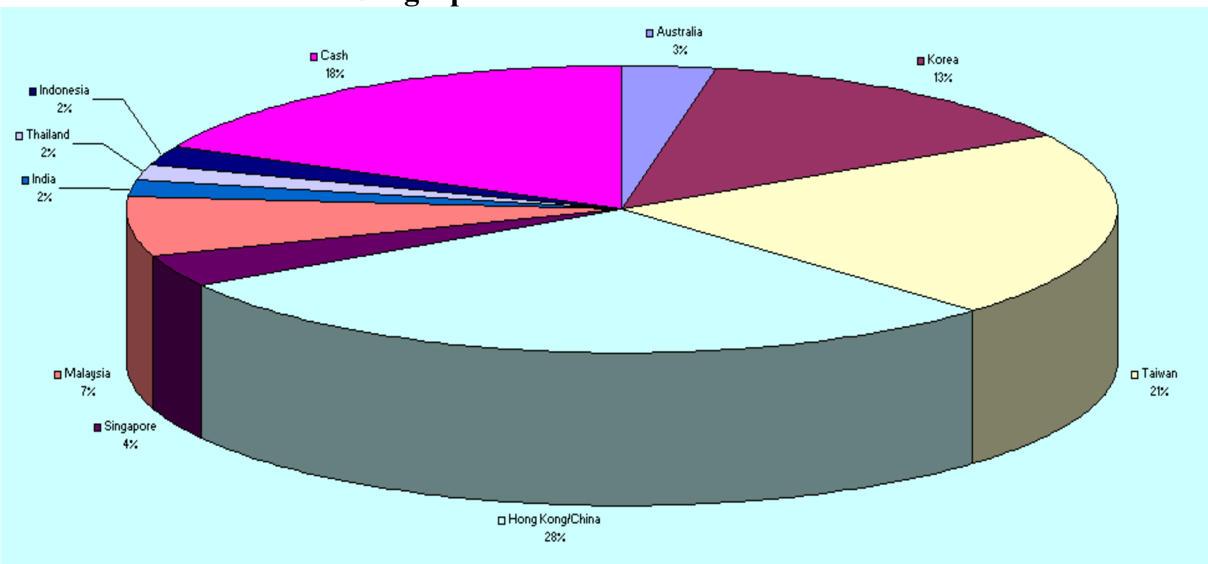
We have now rolled the portfolio PE to 2008 – ex asset plays the price earnings ratio stands at 10x 2008 – which reflects the increased exposure to China. Earnings growth stands at 16% growth with ROE at 17.5%.

Heather visits Malaysia and Singapore later in January.

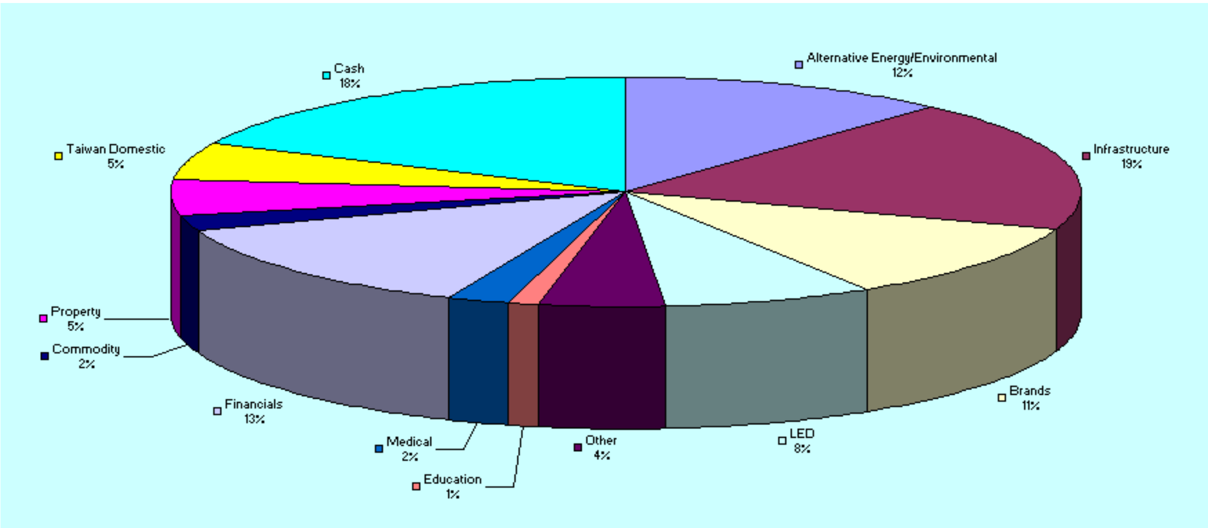
Top 5 Holdings	%
EVERLIGHT ELECTRONICS CO LTD	3.5%
WING LUNG BANK	3.5%
CHINA CONSTRUCTION BANK-H	3.4%
CHINA MOBILE LTD	3.3%
PETROCHINA CO LTD-H	3.3%

Number of holdings	51
Percentage of Fund invested	82%

Geographical Distribution



Distribution by Theme



Year	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
2005										-1.9	5.64	5.08
2006	7.71	0.09	1.84	10.14	-1.95	-0.45	-1.72	0.02	1.23	3.9	7.64	1.97

Key Parties to Fund

Investment Manager	Prusik Investment Management LLP
Administrator	Bisys 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

Manager Fees

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

Prusik Investment Management LLP
63A South Audley Street, London, W1K 2QS.
Tel: (+44) 20 7493 0929 Email tony.morris@prusikim.co.uk
Web : www.prusikim.co.uk Fax : (+44) 20 7493 1770