PRUSIK

LONG ONLY ABSOLUTE RETURN INVESTING IN ASIA

Prusik Asian Smaller Companies Fund

Quarterly Investment Report
30 September 2014

FOR PROFESSIONAL INVESTORS ONLY

3Q14 Review and Outlook

Over the quarter the Prusik Asian Smaller Companies Fund was up 1.75% which compares well with the MXAPJ index which was down 3.1%. The major outperformance came in September when the fund rose slightly whilst the index fell 7.2%. This was driven by our holdings in Taiwan, India and Thailand.

This is a long quarterly as we want to set the scene on all our current thematic thinking ahead of the New Year. We have also written about quite a few of our stocks and highlighted some interesting findings from our research colleague Anna's recent trip to China.

The Major Themes for 2015

We want to map out some of the key and over-arching themes facing all investors in 2015 and possibly beyond, not just in Asia but globally too. These themes are all likely to have a huge bearing on how investors behave from here and we believe that some very dramatic changes are needed in perception and behaviour.

As well as addressing those themes which we believe both global and Asian investors need to take note of, we will also drill down into the themes which we think are specific to Asia and are likely to do well in the current environment.

Information

We have argued in previous quarterlies that there is a new and extraordinary change taking place which, in magnitude of importance, is akin to the industrial revolution. Back then investors had to abandon previous notions of where the best stores of wealth lay. At that time most viewed bonds, gold, land and property as the most prudent places to invest but the revolution forced investors to put their money into scary new inventions such as machinery, cars and railways. The rise of the industrial world led to a massive increase in productivity and set a huge wealth transfer in motion. It also set the business and investment scene for decades to come.

This time a new form of productivity increase is here. It is referred to as 'digital' but at its heart lies the new store of value and power, and in turn future wealth, which is information. Information has 'mass' or 'energy' and value. Companies who can and do collect and use information (or data) will outstrip those that do not or cannot. This process has been happening before our eyes at such a pace that it has barely been seen for what it is. **Alibaba**, a world class user of data, is now a listed company with a market capitalisation of US$210 billion which puts it in the top 10 largest listed companies in the world. This has happened so fast it is disregarded as somehow something to distrust. It is almost treated with denial and disbelief.

The rise of information as the crucial differentiating factor between success and failure in many areas causes investors huge headaches for the following reasons:

- The value of information is difficult to calculate clearly and, as **Tesco** recently demonstrated, just having access to information is not enough. **Tesco**, arguably the original poster child for the value of customer information, was just not able to keep up. Successful companies will need to constantly evolve in how they use data.

- The companies who employ data analysis either do not like to share or do not really know themselves the full value of what they are doing. We had one moment of clarity when speaking to an independent consultant to the major US internet names who told us that a targeted advert on **Facebook** had 10x the hit rate of the advertising industry average across all mediums. However, whilst this is a huge number, one cannot simply extrapolate. Investors will have to generalise, observe patterns and look for the anomalies, such as companies or areas showing growth of 20% or more.

- The existing expectation that large companies grow more slowly is turned on its head in the data driven world. Larger companies, by dint of their scale, are in a stronger position to collect more data. The more data a company has the more powerful it is, driving growth further and faster. This is a world in which one should mostly be investing in the market leaders.

- The speed of change is accelerating to almost inhuman levels. This is because much of what is happening is not happening at human speed but at computing speed! For investors that can feel alienating and confusing and become a great excuse to avoid the whole thing. That might work for the next 2-3 years but after that we believe the differentiating factors will be so enormous that fortunes will already have been lost and made and the information giants, and those investing in them, will have won. After all, already 3 of the top 10 largest listed companies in the world (**Apple**, **Google** and **Alibaba**) understand and use information to their advantage.

At this point we would like to stress that we are not advocating investing just in internet companies, rather we are advocating the need to think differently about which sectors have access to information and how companies within those sectors plan to use data to their advantage. Utilities via smart metres, telecoms, logistics companies and railways are all examples of very traditional businesses which can do very well in the information rich world as they can gather a lot of information on how their customers behave.

Deflation

The second point we have to make on over-arching trends comes with the usual warning that we at Prusik are not macro-economic experts. However, we cannot help but notice that with some US$7 trillion pumped into the economy not much has happened beyond raising house prices in central city locations. Salaries have barely risen and goods and services prices continue to fall. The recent moves in key commodity prices are possibly the canaries in the coal mine. It could be that deflation is the biggest macro event that investors have to contend with next.

Taking China as an example, producer prices there have been in deflation for 33 straight months, which is a record. House prices are falling in most major cities and in October CPI stood at a 4 year low of 1.6%, nearly 2% below the People's Bank of China stated target. Money supply which drives nearly 30% of the CPI volatility slid to the lowest growth rate since 1989 of just 3.2% in October. All this points to an almost inevitable abandonment of the measured approach to easing and, at the time of writing, evidence is mounting that more dramatic easing measures are nigh.

Similarly in India, there is decreasing evidence of the structural inflation to which investors have become accustomed. CPI in India just recorded its lowest reading since the basket was created and WPI has fallen to just 2.4%. There are other huge downwards pressures on prices which must not be ignored.

Returning to the subject of the internet, **Google** has just announced a capex plan of US$11 billion, usually the kind of capex spending we would associate with **Intel**. **Google** is investing in servers and it is no surprise that it has announced that it is cutting the prices of its cloud based services to compete with **Amazon**. These vast infrastructures of IT and communications systems are fast becoming moats for the giants like **Google**, **Amazon** and **Facebook** but in turn these companies must attract the volumes to make them worthwhile, both financially and to satisfy their need for data in our new information driven world. Needless to say this kind of behaviour is extremely deflationary and we should expect more competition for 'old economy' businesses in the very near future. For example, **Snapchat**, the mobile based video messaging service, beloved of the under 30s, has just announced it will be facilitating money transfers in the future.

Millennials

The 'Millennial Generation,' or Generation Y, are the 18-30 year olds and they are the largest cohort ever. In fact this age group makes up a staggering 26% of the US population. Coming behind them is the equally enormous Generation Z. Globally there are 1.6 billion people between the ages of 10 and 24; quite staggeringly India accounts for around 20% of this group with 350 million people aged 10 to 24. Demographics and investment have long been closely related and this generational shift – the largest generational shift since the 1960s – will once again cause huge swings in consumer behaviour. Perhaps this is what we are already seeing at **Tesco** and **Coca Cola**, stalwarts of the previous generation in management, product offering and customer base.

Millennials or at least Millennial thinking is already confusing investors. Jack Ma (**Alibaba**) is renowned for putting shareholders well behind his ambitions to help small businesses in China (and for turning up late to important meetings because he was practising Tai Chi!). Mark Zuckerberg has been derided for buying **Whatsapp** at such a huge valuation but maybe his vision for peer to peer advertising will be proven correct over time. In any event, whether these empire builders (for this super breed are a step beyond entrepreneurs) are seeing the future correctly remains to be seen. What we can see already though is that the Millennials' attitude to brands, health, communities, money saving, plus their ability to live with the abstract, will be fundamental to how old businesses adapt successfully to this new generation. Perhaps the biggest difference for investors to bear in mind is that this generation values experience over belongings and conscience over money.

We wish to make three further observations to add to the three explored above:

Speed of Change

We have already alluded to this above but it cannot be underestimated how fast change is taking place. For example, currently around 30% of the world has a smartphone but in 3 years' time this number will be over 50%. By 2018 internet traffic will be 64 times greater than it was in 2005. Mobiles already account for 25% of internet usage globally but in China this number is reaching 40%. Meanwhile advertising on mobile, which considerably lags behind the actual time spent on a mobile and still accounts for only 4% of total advertising spend, is thus expected to rise 10 fold by 2018. Disruptive technologies, smartphones being the latest, thus destroy the old way of doing things and with South East Asia and India just ramping up their telecom networks and selling cheaper smartphones this is still just at inflexion point. This will disrupt advertising, media and retail as well as drive prices down further. Some projections suggest that by 2020 there will be 1 trillion connected objects and 50 billion connected devices worldwide. Even today there are 500 million DVDs worth of data generated daily!

Privacy

It is estimated that 80% of individuals are prepared to trade their information for a personal offering. Further, 84% of Millennials say that social and user-generated content has an influence on what they buy. Governments and companies are already harvesting, using and storing information on all individuals. One US company, **Akamai**, whose technology enables the internet to carry as much traffic as it does (this is fascinating and worth reading about!) sees 75% of ALL internet traffic go through its servers. Although it can only see the IP addresses, the identities of users can easily be supplied by the telecom companies. Meanwhile unlisted Indian company **Inmobi** (valued at US$600 million in 2011 since when revenues have risen nine-fold!) aims to place software in both apps and handsets to track user behaviour and send out very specifically targeted ads. As a result of this data, they are expecting the commerce sector to increase mobile ad spend by ten-fold in the coming year! Our lives are increasingly being scrutinised and hacked into by software and businesses.

Wealth Gap

On 17th October Janet Yellen gave a speech at the Federal Reserve which may prove to be yet another important turning point in this world of change. Her focus was on inequality. She pointed out that “the past several decades have seen the most sustained rise in inequality since the nineteenth century, after more than 40 years of narrowing inequality following the Great Depression.” She also added that the degree of inequality was near the highest levels in the past 100 years and probably higher than much of American history before then.

It is most likely no accident that the recent protests in Hong Kong were led by a 17 year old, Joshua Wong. One could also argue that recent issues arising in Catalan, Scotland and the Middle East are also driven by the same imperative. The Generations Y and Z are mostly locked out of the system by a vast financial barrier. As a generation they have a much higher propensity to justice, community, outrage and arguably they have little to lose.

Source: The Guardian

We would also add that with the oil price as low as it is currently, this is becoming one of the more serious rising risks in the coming few years. The ‘breakeven’ price for oil in Saudi is $98 per barrel and in Iran is $131 per barrel, so prolonged weakness in the oil price may mean there is more political disruption from the oil producing countries than we have seen in the recent past.

Summary So Far

Pulling this all together, we can see that there will be some very important secular themes arising out of the changes we are seeing. As thematic investors this is very exciting.

Very broadly, given the trends in deflation, information and in demographics, **it would seem important to focus on companies or themes which are asset light, information rich combined with a clear and effective policy of how to use data, and which appeal to the new Millennial or online customer base. Other good themes would also be areas which benefit from new changes in behaviour or a background of shortages (i.e. companies which can maintain pricing power in a world of increasing competition).** We also think that traditional businesses with wide moats and where one can categorically foresee very little change or challenge from the virtual, automated, robotic or algorithmic worlds will also be interesting, largely because so much of the traditional business we currently know will be challenged in one way or another. Healthcare is possibly one example in Asia where we see shortages for a while to come. Infrastructure is another.

We have written a series of short pieces below on each of the areas we think looks interesting for Asian investors. In the meantime it is very important to realise that in the medium term index investing is going to become harder as the larger, older and less competitive companies struggle against the very strong tide of change.

In a deflationary world of rapidly rising productivity and computer speed driven change, some of the larger index sectors such as property, banking, resources, labour-heavy manufacturing and “baby boomer” brands all need careful reconsideration and caution.

Our BIG Asian Themes

Reform

We began writing about reform in early 2014 and at the time focused on China and the policy changes there, all of which have been chronicled in our previous reports this year. Since the end of June the Shanghai Index has been in a stealth bull market and despite dire warnings of slower growth in Western press has since risen over 20%. This is in stark comparison with the small decline in the MXAPJ Index and a less than 5% move up in the Hang Seng Index over the same period. The rise in the Shanghai Index has been a locally driven rally, fuelled by the reform announcements and, it has to be said, a fair amount of margin lending. Margin outstanding equates to 9% of the Shanghai Index free float compared to just 2% in the US. At the time of writing, in the past week, a one day trading volume record was reached of a US$100 billion in China. To put this in context, the daily trading volume of the rest of the Asian region which we invest in is US$20 billion!

We have also seen dramatic outperformance in India, where the reformist new Modi government is settling in and investors here expect both reform and economic recovery in 2015. It is tempting to say much of this is already priced in but, as we have previously pointed out, local ownership of the stock market as a percentage of GDP is standing at one fifth of its previous high in the 1990s.

Korea is steadily moving ahead with reform as well, albeit with a much more sceptical reception from investors. To some extent we believe this is justified as we are still seeing vestiges of 'old style' corporate governance behaviour, for example in the **Hyundai Group**. The locals, however, have been strong participants in the second tier companies and we think that 2015 may be the year where companies which are improving capital allocation and increasing dividend payout ratios following the new tax policies, could be richly rewarded by investors.

ASEAN

We have written extensively about this theme since 2012 and we still see huge potential as we come into 2015, the year of the ASEAN Economic Community (AEC). Next year renders ASEAN a free trade zone, similar to Europe but without the hindrance of the single currency. With over 600 million consumers in the region it is a great opportunity for business. Meanwhile, the opening and development of countries like Myanmar, Laos and Cambodia, as well as the recovery of Vietnam, bodes well for many regional companies, many of which are operating from Thailand, Malaysia and Singapore. Amongst our favourite ways of investing in this theme are the construction companies, such as **Siam Cement** and **Sino Thai Engineering and Construction**, and regional brands such as the 'Beauty Buffet' cosmetics shop chain owned by **Beauty Community**. Anecdotally, it is impressive how many companies, large and small, are planning to expand their business activities across a significant part, or indeed, the whole region.

Internet

Asian mobile users are deemed to be 5 years ahead of Westerners in terms of what they understand a smartphone can do. This is partly for demographic reasons and partly because many people in Developing Asia have missed out some or all of the stages – such as the PC – that came before the handset. For many people in Asia their phone is their first and only means of accessing the internet. The larger listed internet companies in the region, such as **Baidu** or **Alibaba,** are therefore world class in terms of data analysis and offerings, as well as their size. Korea, meanwhile, is the place to look for future trends in terms of gaming through to money transfer.

From an investment perspective the internet sector is especially challenging for its fast pace of change. However, the larger companies dominate probably more than in any other sector and because of this and their sophisticated use of data, they still grow faster than traditional peers. As an example, the recent annual 11/11 online shopping day in China saw **Alibaba's** ecommerce sales up 58% year on year and a whopping 43% of transactions were conducted from a mobile. This was the scene in the parcel sorting office last year so imagine what it looked like this year!

Source: Thomson Reuters

We suspect that the story we have watched unfold in China will be repeated across India and ASEAN in the coming 3 years. The frustration for investors is that, as yet, there are very few listed companies here in this sector. However, just because they are not clearly visible to stock market investors does not mean that they will not unleash an equally disruptive influence on certain bricks and mortar businesses.

Data Analysis and Software

Persistent Systems is a mid cap Indian IT company with a bit of a twist. Typically Indian IT companies carry out large scale projects for companies based in the US and Europe, often banks, to help them reduce costs and improve efficiency. Rather than try and replicate these more traditional services and go head to head with the incumbents, the management of **Persistent Systems** decided many years ago to focus on what we now understand to be the faster growing 'new' areas of technology, namely data analytics, social networking, mobile and cloud computing.

Our analyst travelled to India earlier in the year and all conversations with the traditional IT outsourcing companies led to the same end, that **Persistent Systems** was the one company in the industry they truly admired in terms of the nature of the work the company is doing in this space and how early management had decided to invest in these new areas. Speaking to the larger cap Indian IT companies also led our analyst to understand that owing to the ticket size of projects in these 'new' areas of data analytics, social networking, mobile and cloud computing being much smaller, it was more likely that the leaders in this field at this point in time would be small and mid-sized companies rather than the likes of **Infosys**. As a further indicator of its quality, **Persistent** counts the likes of **IBM** and **Salesforce.com** amongst its customer base. While we think the company looks attractive in its own right, we also think it is a potential take out target given that a time may come when the large cap Indian IT companies want a quick fix to get ahead in these data analytics, social networking, mobile and cloud computing related projects. Following a strong performance of the shares recently the stock is now trading on a March 2016e P/E of 17.7x with 8% of its market cap in cash. In recent years, pre-stripping out the cash, it has consistently generated over 20% ROCE.

Telecoms

Traditionally, telecoms have been perceived as deflationary; however, we believe the arrival of smartphones, data and apps is starting to call this received wisdom into question. While 'prices' of some mobile services might 'fall,' for example users may receive more free minutes, we believe the tangible value subscribers accrue by owning a smartphone and in turn their appetite to pay for and their price elasticity in relation to that value has fundamentally changed. Further, with regard to the potential for the build out of wifi services to act as a deflationary force for telecom companies, conversations with the companies themselves reveal that they are very keen to see this happen as it allows them to relieve some of the burden on their existing networks, especially at peak times. The Korean telecom companies already offer a clear example of how an improved ability to charge for data can lead to rising ARPUs and revenues. Excitingly, we are possibly starting to see the beginning of this process in Hong Kong too.

We also want to highlight that telecoms companies are in a unique position in terms of the size of their subscriber bases, payment infrastructure and their ability to simultaneously observe customer behaviour and provide data related services. Put like this, they almost sound like internet companies!

In general this is a harder sector to invest in via smaller companies although software/data analysis focused companies such as **Persistent Systems** and equipment suppliers are two areas to benefit. Handsets also are a clear beneficiary of this theme.

Handsets

This is a theme which remains interesting in the shorter term due to the potential for very high growth rates of lower cost smartphones in developing countries over the next 2-3 years. While on the one hand the low end smartphone market is horribly competitive, the positive upshot of this is that falling prices of the low end Chinese handsets (a **Xiaomi** handset is around $150 or less and it looks like an iPhone) will also help drive very strong growth in developing countries. Global share for China smartphone brands in terms of volumes is already high at an estimated 36% in 1H14 but this is expected to rise to 45% in 2015. After China, India and South East Asia are likely to be the next big focus. **Samsung** currently has the largest share in these markets but is struggling to maintain market share against the local brands. Indeed, **Xiaomi's** suppliers have been guided that they will sell 80 million phones in 2016, up from 40 million estimated in 2014. Looking further out, competition in the Android camp may intensify and we could see some consolidation of smaller players by the Chinese brand leaders, **Xiaomi**, **Lenovo / Moto** and **Huawei**. Nonetheless, the coming two years in terms of growth are likely to remain impressive.

We were interested to hear from our analyst upon her return from China that smartphones are so essential to day to day life there that everyone now carries around with them what she believed to be Chinese manufactured cordless chargers or battery packs. This has become such a common phenomenon in China that there are posters and frequent announcements at airports about not putting these chargers in luggage which goes in the airplane hold. Apparently, these portable, cordless chargers have a tendency to short circuit and catch fire, making them the last thing that should be packed into unsupervised luggage! We were also amused to learn about some very China specific functions available on Chinese smartphones. For example, **Lenovo** has a function in its camera / picture tool whereby people can adjust the whiteness of their face in their photos!

Source: China Daily

Chinese smartphone cordless charger / battery pack

We prefer the component makers to specific handset brands and the Chinese casing supplier, **Tongda Group Holdings Ltd**, sits in an interesting position. The current trend is for metal casing but with a 4G handset this causes interference problems with the huge numbers of antenna inside the phone. It is also extremely expensive and time consuming to mill the internal structure of the metal casing which requires detailed shapes to hold the components in place. **Tongda** has a unique materials solution which welds a metal back to a plastic surround, thus both solving the interference problem and reducing the internal moulding process to a much quicker and cheaper solution. **Tongda** is guiding for volume growth in the coming year of around 25% and for margins to rise, but we think this could be a modest estimate.

We have also recently invested in **Erajaya Swasembada Tbk PT**, the mobile phone retailer based in Indonesia. The company currently makes 30% of its sales through its own stores and 70% of its sales via its distributors but is hoping to make the split 50:50 in the coming years. **Erajaya** is the market leader by a wide margin and has continued to take share in the last 18 months with the company now having 28% share of the market. It is clearly the preferred partner of its customers given that it was selected as the only company in Indonesia to set up an 'Android Nation' store for **Google** and is also a designated **Apple** re-seller via its 'i-Box' stores. The shares have been very weak recently as overstocking from **Samsung Electronics** led to sales and profits taking a short term tumble. However, given the still very low penetration rate of smartphones in Indonesia, combined with the company's strong competitive position, we are willing to overlook these short term weaknesses and recently purchased the shares. The stock is trading on just 13.1x 2014e P/E compared to Taiwanese mobile phone retailer, **Senao International Co Ltd**, which is trading on a 2014e P/E of 15.3x.

Leisure / Tourism / Culture / Entertainment and Experience

Companies in this theme have done very well in the past two years but we see no reason for this to slow down in 2015. Chinese tourist arrivals to Korea in the summer months topped 50% year on year increases and their spending on live entertainment, Korean branded clothes and cosmetics, duty free goods and hotels has followed suit.

We continue to like this theme, firstly because there are still relatively few ways of gaining investment exposure to companies offering leisure 'experience' as opposed to the traditional retail sector and secondly, because these companies are very varied in nature. For example, investing in companies which benefit from people's desire to travel, to see live entertainment, to go to the cinema or visit a water park evidently spans many different sectors. We also believe that the desire to consume 'experience' rather than 'things' is a 'Millennial' behaviour which will continue to boom as ASEAN and India, both having very young populations, continue to see their middle classes swell in number.

Thanks to the recent addition of about 2,000 new cinema screens in China, Hollywood can now make US$100 million from a box office hit in China in just a few days. Unsurprisingly, Hollywood's blockbuster line-up for 2015, one of its biggest ever, has a specific eye to the Asian market. It will be increasingly common to find, as with the latest Transformers movie, Asian actors in lead roles in Hollywood as well as regional locations.

Major Cineplex is Thai listed cinema chain which is conforming to the increasingly familiar pattern of expanding into ASEAN, in this case Cambodia, where it is successfully opening a number of new cinemas in conjunction with a top end mall operator there, **Eon Mall**. **Major's** local business is growing well with the success of more local content movies and next year promises to be interesting for most cinema operators. **Major** also has an enticing dividend yield of 4.5%.

Infrastructure

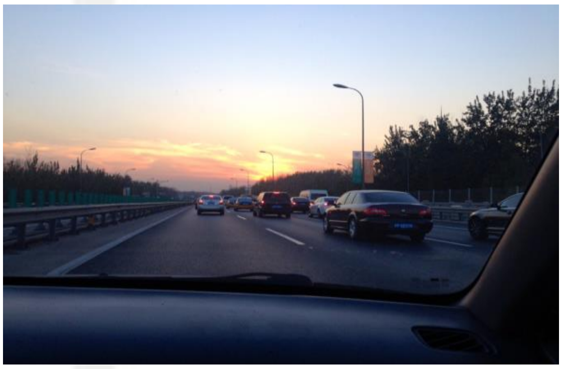
As China has famously spent so much on infrastructure in recent years it is tempting to think that the infrastructure boom in Asia is over; however, far from it. Even in China the trends in urbanisation are triggering new and massive projects, whilst in ASEAN the process has barely begun in places like Myanmar. For China the biggest trend shaping the country is 10 to 15 million people moving from the countryside into cities every year!

Beijing Urban Design is a design company specialising in subways with a 22% market share in China. In China there are currently some 2,000 km of subways but the government targets are for 8,000 km by 2020. Furthermore 6,000 km of subways are planned by local authorities in smaller cities but are not yet approved. Each kilometre of subway costs Rmb 500 million with 5% of this cost going to the design company. Most of **Beijing Urban Design's** competitors are running at full capacity so expectations are that the company can see 25% per annum sales growth for the coming 5 years.

Environment

One of the themes our analyst was investigating on her trip was what is happening to the environment in China, plus which are the companies which might benefit from the Chinese government's realisation that it must now address the costs of 30 years of rapid economic development. We were interested to hear about the extremes she witnessed. Firstly, arriving in Beijing just at the tail end of APEC, during which the capital city was on 'pollution lockdown' with government organisations, business and schools closed and restrictions on car usage, Anna saw something she had never seen in Beijing: a clear and quite beautiful sunset.

However, several days later when business was back to normal the Beijing smog returned with its usual ferocity. Her experience of some of China's perhaps worst air pollution was yet to come though. After Beijing she travelled to Shijiazhuang, the provincial capital of Hebei province. Together Beijing, Hebei and Tianjian have over the years been transformed into something of an industrial powerhouse of North China but Hebei in particular has become a focus for manufacturing, plants and power generation, mostly as a result of companies being moved out of Beijing to try and improve the air quality there. The impact of this is tangible to say the least. Anna developed a running nose, nasty cough and even nastier eye infection after just one day in Shijiazhuang and has returned with some apocalyptic style photos of hazy orange suns and hard to see buildings, despite their proximity.



Sunset in Beijing post APEC.

Afternoon haze in Shijiazhuang, Hebei.

Smog in Shijiazhuang, Hebei.
Source: Prusik Investment Management

Smog in Shijiazhuang, Hebei.

While environmental damage has for many years been largely tolerated at a government level in China, we believe there are clear signs of change afoot. The Chinese broadsheet media now features articles discussing the environment on a near daily basis, be it the promotion of a government official's new book 'The Smog is Coming,' reference to the government's plans for 'air corridors' in Beijing and the promotion of high tech environmental technology companies from Xi'an.

At a higher level, China and the US recently announced a climate deal in which China agreed to stop increasing greenhouse gas emissions by 2030. This was broadly received as positive on the basis that China has finally set an official target for this to happen, while India and Russia are yet to come out with similar announcements. Equally, we would note that this still means 15 more years more of rising emissions from China and no clear indication from the Chinese government as to what speed emissions will be reduced by once this peak is reached. Overall though, the environmental issues China faces are finally being openly discussed rather than ignored or shied away from, and the government is putting pro-environment policies in place at the highest political level, creating a clear signal that something needs to be done and it intends to take action.

To this end we have invested in **Dynagreen**. **Dynagreen** is a waste-to-energy company and the only company of its kind listed in China. **Dynagreen** is paid to receive municipal waste which it then burns, generating electricity in the process, which it then sells to the grid. Globally, its nearest peer would be **Covanta** in the US, although there are some important differences between the two. Some of the key differences between **Dynagreen** and **Covanta** are that the former receives minimum guarantees for waste volumes to be delivered and electricity to be bought and prices for each. There are also no limits on how much electricity **Dynagreen** can sell to the grid. This makes the visibility on cash flows and returns much clearer for the company and contracts are set so that **Dynagreen** makes a decent, if not excessive 12-14% IRR. The Beijing government is a key shareholder of the company and this makes us confident that **Dynagreen** will be able to consistently win bids for new projects in the future. Indeed, it has won 3 new projects in just the last few months. We participated in the IPO in the summer and the shares performed well within the first several months, although at the time of writing they have been a bit weaker, possibly as the 6 month lock up period approaches.

We have also invested in **Sound Global**, a company which largely builds and provides equipment for waste water treatment. However, **Sound** is increasingly shifting towards building and operating waste water plants. Although this company does not have an SOE backing, we were impressed with the calibre of management both on paper and when we met them in person. Further, the company has a reputation for having a strong technology focus. Trading on just 14.9x 2014e P/E, it is on a significant discount to its Chinese water treatment and environmental peers.

Wealth Management

Wealth management in Asia has been growing hugely over the past decade but from a tiny base. For example, in Indonesia there are now 5 domestic institutions each managing over US$5 billion, compared to 8 years ago when the largest domestic unit trust was just US$300 million.

However, the industry is still hugely underpenetrated and on top of this is it possible that we will see governments begin to formalise the savings and pensions environment, which would lead to further local involvement in stock markets and other savings products.

At the time of writing we are taking part in an IPO of a Singapore listed online funds platform called **iFAST**. This is the ‘Hargreaves Lansdowne’ of South East Asia and we see the opportunity as potentially very large.

Local Brands

Local brands have long been a firm favourite of ours as a hunting ground for new investment ideas. Part of the motivation for this is that we believe sometimes multinational companies’ understanding of the local market is inferior to local companies and it is the latter which are best placed to cater to local needs. Another attraction of investing in local brands is that strong and successful brands tend to have deep competitive moats. In the Prusik Asia Smaller Companies Fund there are two local branded companies which we would like to draw to your attention.

The first is **Beauty Community PCL**, a Thai retailer focused on mid range cosmetic and beauty products. As of September this year the company had 264 stores in Thailand based in Bangkok and upcountry. It also has 10 stores in Cambodia, Vietnam, Laos and Myanmar. While the majority of sales come from third party local brands, it also has its own in-house brand of products, ‘Made in Nature’ and ‘Girly Girl,’ which **Beauty** sells in its own stores and via third party distributors and convenience stores. **Beauty** has been seeing very strong sales growth recently with same store sales growth reaching a massive 20% year on year and overall sales growth of 48% year on year in the most recent quarter. Over the next 5 years management are targeting 20-25% sales growth for the company overall. We came across the company following conversations with **Karmax**, another beauty products retailer in Thailand which has been far less successful owing to what we believe is poor management of the company (indeed, when we met with **Karmax** management in 2013 the Chairman spent the majority of the meeting telling us which Thai stocks to be investing in!). We decided to invest in **Beauty** at a time when there was very limited sell side coverage and the company was poorly understood. However, its recent strong sales and earnings growth has attracted investor attention and the shares have re-rated from a low 20s headline multiple when we added it to the Prusik Asian Smaller Companies Fund to a rather eye watering 2014e P/E of 35.6x. **Beauty** has zero debt and cash equivalent to 7% of the market capitalisation.

The second company which we would like to highlight is **Ceat Ltd** in India, a local brand of tyres for two wheelers, three wheelers, agricultural vehicles and commercial vehicles. Our work on the two wheelers in India, **Hero Motor** and **Bajaj Auto**, which are held in the Prusik Asia Fund, led us to believe that the consensus view of future two wheeler, three wheeler and commercial vehicle demand was too low and with the political and economic outlook for India improving, following the election of Mr Modi, then demand in these segments could see a healthy revival. When **Ceat Ltd** popped up on one of our quantitative screens we ensured we met with management during our trip to India in the summer of this year. Here we learned how management were refocusing their efforts on expanding the company's two and three wheeler sales as these products yield higher margins. We also learned that **Ceat Ltd** had been gaining a lot of share recently owing to an aggressive marketing campaign which stressed **Ceat Ltd's** tyres' 'high grip performance,' one of the three key tyre characteristics management had identified as being important to customers. We bought shares in the company when the stock was trading on just a mid-single digit headline P/E multiple. Although we have trimmed our position in the stock following a strong re-rating, we are still enthused about the company's capacity expansion plans which should help drive further rapid growth for **Ceat Ltd** for many years to come.

Finally, we are delighted to announce that Jack Barham has recently joined Prusik and will be training to work alongside Mark in Sales and Marketing. Jack is 19 and impressed us by his strong arguments as to why he did not want to go to university. Although Jack will be on the Sales and Marketing team at Prusik his obvious 'Millennial' credentials have already inspired the investment team to several useful discussions!

PORTFOLIO PERFORMANCE

Performance Summary (%)
Period ending 30.09.2014

	USD	GBP	SGD
1 Month	0.32	0.48	0.41
3 Months	1.75	1.99	1.81
Year to Date	3.30	3.54	3.30
Since Launch+	70.83	73.65	25.33
2013	7.51	7.29	7.64
2012	30.80	31.05	30.69
2011	-19.28	-19.86	-20.04
Annualised 5 years	7.95	7.93	-
Annualised 3 years	10.87	10.98	10.80
Annualised Since Inception	8.39	8.66	4.91

Source: Bloomberg
+ Launch date: A:08.02.08, C: 25.03.08, D: 15.01.10

Fund Performance - Class A USD (%)

Source: Bloomberg. Total return net of fees.

Monthly Performance Summary (%)

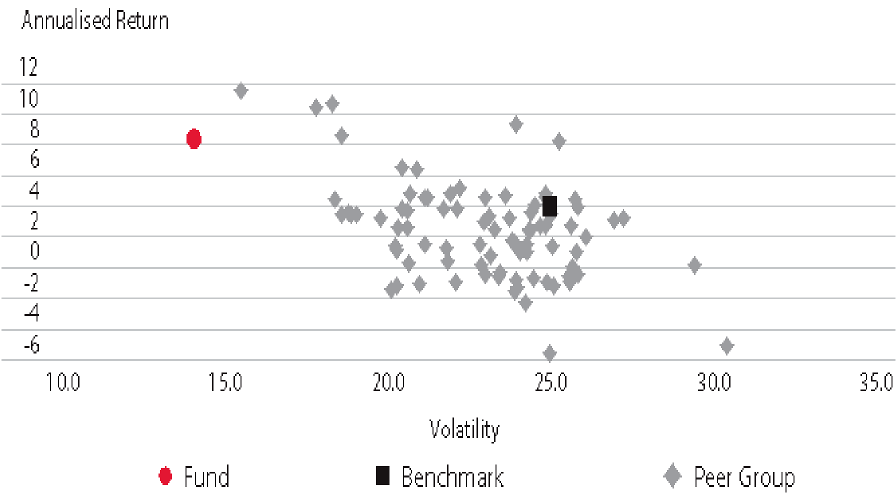
	Jan	Feb	Mar	Apr	May	June	July	Aug	Sept	Oct	Nov	Dec	Total
2014	0.21	3.58	-2.62	-2.50	0.56	2.45	-1.39	2.86	0.32				
2013	7.27	3.73	1.32	1.82	3.58	-9.40	0.10	-4.52	3.54	2.84	-1.44	-0.51	7.51
2012	5.05	7.75	-1.04	4.29	-5.53	3.11	2.27	-0.65	5.40	1.27	4.12	1.81	30.80
2011	-2.15	0.43	2.35	3.75	-0.57	-1.22	3.60	-11.67	-8.27	0.37	-5.50	-1.07	-19.28

RISK ANALYSIS

Risk Metrics	Fund
Beta	0.54
Alpha (%)	6.2
Sharpe Ratio	0.60
Volatility (%)	14.0
% of the portfolio –which could be sold in 2 business days	58.2

Source: Bloomberg
Since Inception: A:08.02.08

Risk Adjusted Performance - Class A USD (%)



Source: Bloomberg. Annualised return and 1 year volatility versus the peer group (open ended offshore Asia Pacific ex Japan Equity Fund Index), 8.02.08 to 30.09.14

THEMATIC & GEOGRAPHICAL BREAKDOWN

Top 5 Holdings (%)

Silverlake Axis Ltd	4.7
CEAT Limited	3.8
Wasion Group	3.4
Premium Leisure	3.0
eMemory Technology Inc.	2.9
Total Number of Holdings	55

Portfolio Financial Ratios*

Predicted Price/Earnings Ratio	13.6x
Predicted Return on Equity (%)	20.1
Predicted Earnings Growth (%)	25.5

*Fiscal year periods

Thematic Breakdown (%)

Leisure / Tourism	17.9
LED / Cloud computing / Software	16.6
Brands / Beauty	11.6
Automation / Internet of things	9.7
Vietnam	8.6
Financialisation	6.3
Local Brands	6.3
Cash	5.8
Telecoms / Infrastructure / Logistics	4.9
Environment	3.6
Healthcare	3.3
Energy services	2.9
Internet	2.7

Geographical Breakdown (%)

Hong Kong / China	22.5
India	12.5
Korea	11.4
Singapore	9.8
Vietnam	8.6
Taiwan	8.3
Philippines	7.1
Malaysia	6.1
Cash	5.8
Thailand	4.6
Australia	2.7
Sri Lanka	0.6

All data as at 30.09.14. Source: Prusik Investment Management LLP, unless otherwise stated.

FUND PARTICULARS

Fund Facts

Fund Size (USD)	193.2m
Launch Date	8 February 2008
Fund Structure	UCITS III
Domicile	Dublin
Currencies	USD (base), GBP, SGD

Management Fees

Annual Management Fee
1.5% p.a Paid monthly in arrears

Performance Fee
All classes except Class U: Provided the fund achieves an overall increase of 6% a yearly performance fee of 10% of the total returns will be applied.
Class U: Provided the fund achieves an overall increase of 1.5% per quarter, a performance fee of 10% of the total return will be applied.

Dealing

Dealing Line	+353 1 603 6490
Administrator	Brown Brothers Harriman (Dublin)
Dealing Frequency	Weekly, Friday
Min. Initial Subscription	USD 10,000
Subscription Notice	2 business days
Redemption Notice	2 business days

Share Class Details

Codes			SEDOL	ISIN	Month end NAV
Class 1					
A USD	Unhedged	Non Distributing	B2PKN21	IE00B2PKN210	170.83
B USD	Unhedged	Distributing	B2PKN32	IE00B2PKN327	170.99
C GBP	Hedged	Distributing	B2PKN43	IE00B2PKN434	89.17
D SGD	Hedged	Distributing	B3M3HJ5	IE00B3M3HJ55	234.95
Performance fee based on individual investor's holding					
U GBP	Unhedged	Distributing	BBQ37T7	IE00BBQ37T77	96.73

Performance fee based on fund performance as a whole
All share classes are closed to new investors as of 30th September 2013.

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