PRUSIK

LONG ONLY ABSOLUTE RETURN INVESTING IN ASIA

Prusik Asian Equity Income Fund

Quarterly Investment Report
31 March 2020

FOR PROFESSIONAL INVESTORS ONLY

1Q20 Performance Commentary

1Q20 was an extremely poor quarter for the fund both from an absolute and relative perspective. The fund fell by 27.8%compared to the MSCI AC Asia Pacific Ex Japan Gross Return (USD) (the Index) which fell 20.7%. The biggest contributors were **Multi Commodity Exchange**, **Singapore Telecoms** and **HM Sampoerna** (although these were very marginal gains). The biggest detractors were **Samsonite**, **CK Hutchison** and **Scentre Group**. Obviously, the losses were experienced largely in March as Covid-19 fears pushed markets lower. The poor performance deserves some explanation and so this report will focus on why the loss occurred, why we made the decisions we did and where we go from here. We would certainly share our investors' frustration and annoyance with this performance which is obviously unacceptable. But all we can do is explain why the loss occurred and what we are doing to maximise the chances that we can generate better returns going forward. Much of the following sounds like we are seeking excuses – we are not. We take positions that are very different to the index and over time, they have tended to work but this time they have not. We could have made different decisions in hindsight and protected capital more effectively.

1Q20 Attribution Analysis

	Avg % Wgt			Total Return (%)			Allocation	Selection	Total Attribution
	PAEIF	Index	+/-	PAEIF	Index	+/-			
South Korea	7.2%	11.3%	-4.1%	-16.3%	-22.8%	6.5%	0.1%	0.4%	0.8%
Thailand	4.1%	2.3%	1.8%	-20.2%	-34.4%	14.2%	-0.2%	0.6%	0.3%
Taiwan	0.0%	11.5%	-11.5%	0.0%	-19.0%	19.0%	0.1%	0.0%	0.2%
Singapore	8.4%	2.9%	5.5%	-14.9%	-28.3%	13.4%	-0.3%	0.6%	0.1%
New Zealand	0.0%	0.7%	-0.7%	0.0%	-16.1%	16.1%	-0.1%	0.0%	0.0%
Australia	4.4%	14.8%	-10.5%	-60.8%	-33.4%	-27.4%	0.5%	-1.6%	-0.1%
India	13.0%	8.3%	4.7%	-26.6%	-30.9%	4.3%	-0.6%	0.7%	-0.1%
Philippines	2.8%	0.9%	1.9%	-28.7%	-31.8%	3.1%	-0.3%	0.0%	-0.3%
Indonesia	6.2%	1.8%	4.4%	-35.4%	-39.4%	4.1%	-0.5%	0.2%	-0.9%
Macau	7.4%	0.3%	7.1%	-33.3%	-31.7%	-1.7%	-1.0%	-0.1%	-1.1%
United States	2.4%	0.0%	2.4%	-60.3%	-44.6%	-15.7%	-0.7%	-0.6%	-1.2%
Hong Kong	31.8%	11.5%	20.2%	-23.0%	-16.2%	-6.9%	0.2%	-2.1%	-1.8%
China	10.9%	31.6%	-20.6%	-24.8%	-9.6%	-15.2%	-1.5%	-1.6%	-3.0%
Total							-4.0%	-3.4%	-6.9%

Source: Prusik/Bloomberg

The main reasons for the underperformance (not all captured in numbers above) were:

- Being underweight China.
- Being underweight the technology sector (particularly with regards to the China Internet sector).
- Being overweight small and mid-cap stocks (which cost approximately 500bps).
- Increased beta from traditionally low risk stocks.
- Overweight "physical" vs "virtual" assets (we own hardly any virtual assets).
- Exposure to travel and tourism sector. Changes in valuation (Median P/E for PAEIF holdings fell 19% compared to MXAPJ P/E which fell 12%).

One issue that we mention above is the increasing beta[1] of certain stocks in the portfolio. **Over the quarter the average beta of stocks in the PAEIF portfolio increased from 0.7x to 1.1x**. As can be seen from the table below, the increase in beta for some of our positions this year (with betas above 1.25x) has been extreme. We also include some other large cap. stocks which we do not own, but which have also seen their betas *fall* over this period.

	Beta (2017-2019)	**Beta (1Q2020)**
Samsonite	1.4x	3.9x
First Pacific	0.2x	2.4x
Qantas	0.8x	2.1x
Scentre Group	0.6x	2.0x
CK Hutchison	0.8x	1.8x
CK Assets	1.0x	1.7x
Swire Pacific	0.8x	1.6x
CK Infrastructure	0.5x	1.5x
Jasmine Infrastructure Fund	0.3x	1.4x
Fortune REIT	0.4x	1.4x
MXAPJ top 10		
Alibaba	*1.5x*	*0.8x*
Tencent	*1.4x*	*0.9x*
TSMC	*1.5x*	*0.9x*
Samsung Electronics	*1.2x*	*0.8x*
AIA	*1.2x*	*1.2x*
CSL	*1.1x*	*0.5x*
China Construction Bank	*1.1x*	*0.6x*
Ping An	*1.1x*	*1.1x*
BHP	*1.1x*	*0.5x*

Source: Prusik/Bloomberg

Some of these are easy to understand. **Samsonite** and **Qantas** are significantly affected by the reduced amount of airline travel and demand for luggage. **Scentre Group** because the lockdown prevents consumers from visiting shopping malls and investors worry about the impact on their tenant's ability to pay rents. But for some stocks we are perplexed**.** **CK Hutchison** has a lower volatility business than the average stock in Hong Kong and is not particularly affected by the Coronavirus. **CK infrastructure** is a utility business which suffers little direct impact. Most surprisingly of all, **Jasmine Infrastructure Fund** has contractually guaranteed, inflation-linked cash flows which it receives from its parent company (and virtually no debt). We do not know why these stocks have seen their beta increase as we do not believe their businesses have become riskier. Could it be that these stocks were owned by investors that viewed them as an alternative to corporate debt and they have been affected by outflows? Is it because some investors have borrowed money to invest in them? Is it just because they are mid and small cap stocks affected by liquidation selling?

On the other hand, it can be seen that most of the big stocks in the index saw their betas fall. This is largely due to the fact that they are either a) technology companies which operate in the "virtual" rather than "physical" world and/or b) they are exposed to China which is perceived to have dealt with the Coronavirus more effectively than most developed markets.

[1] Defined as weekly beta to local index

Strategy Update

Our strategy is relatively simple. We are trying to buy high quality, long duration companies at attractive prices. From 2007, when I first started running this strategy (whilst in Hong Kong), until a couple of years ago it has been, relatively, dominated by quality and less driven by valuations. This was because over this period quality companies were undervalued both in absolute terms and relative to other types of company. However, since 2018, our view was that this had changed, and it was the case that certain high-quality stocks were being valued at levels which provided a very minimal margin of safety. If we translate this into bond equivalent terms, we can give every company in Asia a rating between AAA and D. We focus on the investment grade portion of this universe (BBB and above). When AAA rated companies are yielding 5% and A rated companies are yielding 6% then it is relatively easy to tilt a portfolio towards the AAA rated companies. When AAA rated companies yield 3% and A rated yield 10% then one tends to move the portfolio towards A rated names (all other things being equal). Our view in 2018 and 2019 was that the market was pricing in too high a probability of rates remaining at zero forever and too low a probability of the "world not ending". And so we owned fewer AAA companies (which were trading at equity IRRs of 5-6%) and more A rated companies (trading at equity IRRs of 15%+). However, the arrival of Covid-19 obviously increases the probability of rates remaining lower and the world ending. And so the gap between these two groups have widened further. **Despite this, we believe that our thesis is still correct and A and AA rated companies offer significantly higher expected returns than AAA rated.**

Another issue which we have encountered is that we tend to own companies that, although they are generally low risk, do depend on people being able to leave their homes. Shopping malls, office blocks and even companies like Qantas have relatively stable businesses during the economic cycle. However, if people cannot leave their homes then this is no longer the case. On the other hand, "virtual" companies like Tencent and Alibaba can generate profits even if people are staying at home. Our risk management did not account for such an event. As a result of the lockdown measures put in place in various countries to control Covid-19, the risk of these stocks has increased and this has, in many cases led the beta to increase which increases the risk premium investors demand and therefore lowers the price. In addition, investors worry that the lockdowns might lead to a significant economic downturn which means that, if and when the virus is under control, revenues might not return to the pre-crisis levels for some time. A combination of higher risk premiums, lower expected profits and, in some cases, financial leverage is a toxic combination.

Dividend Stress Test

The current dividend yield of the fund is 6.8%. It is a reasonable question to ask how much this dividend could be cut and we have attempted to stress test the portfolio to answer this question. To do this we have divided the portfolio into 3 main categories.

- Companies that we believe should be extremely resistant to a Coronavirus led downturn (less than 10% cut to dividend).
- Companies that have some economic cyclicality but are not directly impacted by the lockdown (10-33% cut).
- Companies that are directly exposed to the virus and would be significantly affected by an economic downturn. (>33% cut).

Dividend cut in Stress Test	% of NAV	Typical Industries	Examples
Low risk (<10%)	48%	Telecoms, Power Utilities, Tobacco, Consumer Staples	Power Grid, ITC, Hong Kong Broadband Networks, Cheung Kong Infrastructure
Medium risk (10-33%)	37%	Technology, High quality non-bank financials, Hong Kong conglomerates	AIA, Samsung Electronics, Swire Pacific
High risk (>33%)	14%	Macau Casinos, Travel and Tourism, Retail shopping mall REITs	Wynn Macau, Samsonite, Scentre Group

Source: Prusik/Bloomberg

The first group contains Power Utilities (such as **Cikarang Listrindo**, **Power Grid**), Telecoms (such as **JASIF**, **PT Telkom**, **PCCW**), Tobacco (**ITC**, **HM Sampoerna**). These are stocks that are seeing minimal (although not zero) impact from the current environment.

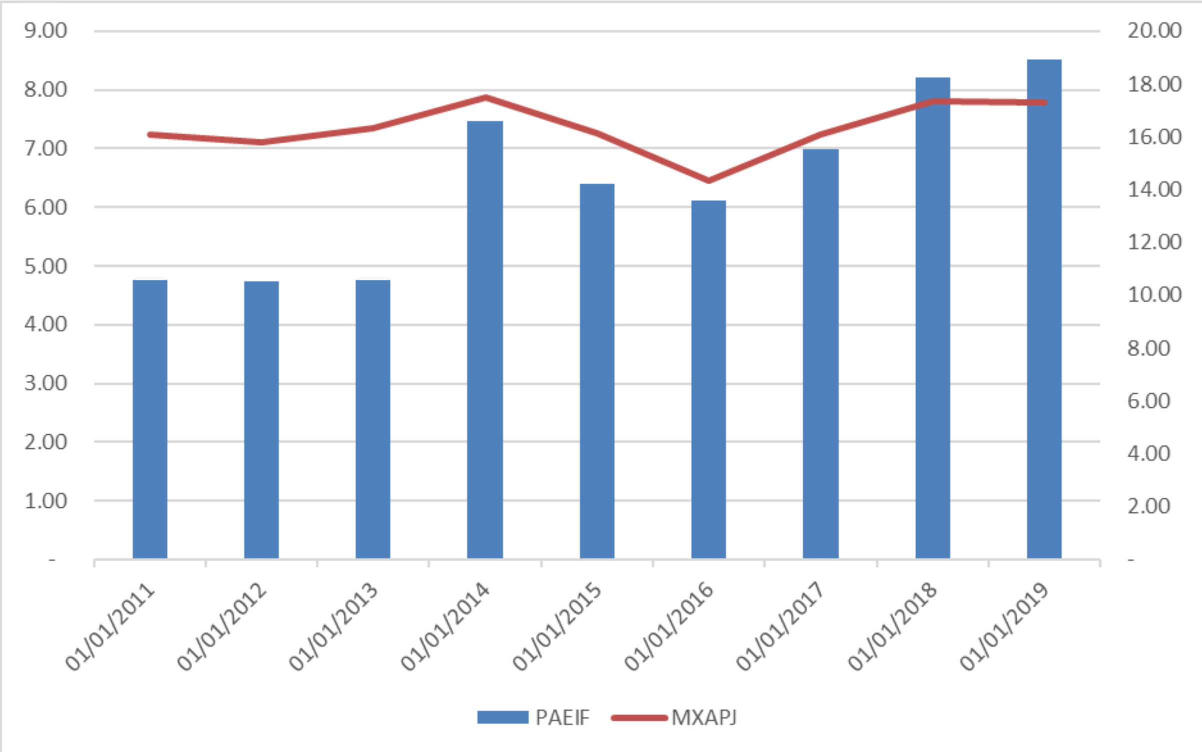
The second group contains stocks such as **Samsung Electronics**, **Infosys**, **Zhejiang Expressway**, **CK Hutchison** and **Swire Pacific**. They have some amount of economic cyclicality and so would be hurt by a global recession but they do not have significant exposure to businesses that are directly affected by the shutdown and, in some cases, own businesses that benefit from it (e.g. **CK Hutchison** owns AS Watsons which is a pharmacy chain).

The third group are companies that are significantly affected by the virus. There are only two companies in this group which are **Samsonite** and **Scentre Group** (although we have since sold both stocks). The question here is to decide whether the share price already discounts too negative a scenario. For example, **Scentre Group** is discounting a permanent 40% fall in asset valuations which is extremely pessimistic. However, there are circumstances where that would be possible.

The overall stress test leads to a dividend cut of 15-20% (which would be 20-25% from the start of the year as some estimates have already been cut). This would reduce the prospective dividend yield to around 5.5% which is still significantly higher than the historic average for the portfolio (4.1%) and much higher than our internal valuation (approx. 3.5%). By comparison, the market yields just 3.7%.

Dividend Growth since inception[2]

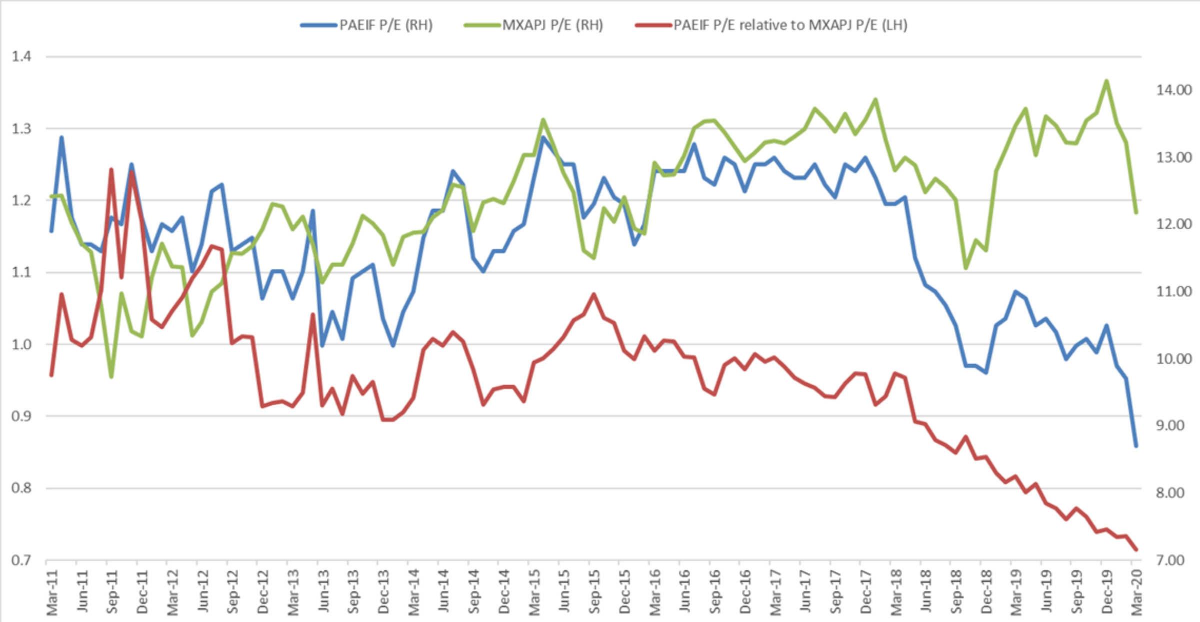
Since the fund was launched, dividends have grown at 7.5% a year compared to just 0.9% for the MXAPJ (see chart below). Ultimately, we believe that this is the test of the strategy – whether we can sustain and grow dividends over time. Share prices can fluctuate as sentiment shifts but dividends (and cash flows) are the real measure of investment returns.



Source: Prusik/Bloomberg (Left axis corresponds to PAEIF, right axis corresponds to MXAPJ)

The chart below shows how far the portfolio has de-rated both in absolute terms and relative to the market. We believe that the current P/E is pricing in a 30-40% fall in earnings *relative to the index*. In other words, it is pricing a 30-40% fall in earnings for our portfolio in an environment where index earnings were unchanged. This appears, to us, to be excessively pessimistic.

[2] Source: Bloomberg. Dividends for USD B class since 2010. Note 2014 included special dividend from CK Hutch.



Source: Prusik/Bloomberg

Changes to the Portfolio

We bought several new positions during the quarter:

- **PT Telkom**
  - Dominant telecom operator in Indonesia (60% market share)
  - Fast growing fixed broadband business (penetration only 9%)
  - Net cash balance sheet
  - 5.5% dividend yield
- **HM Sampoerna**
  - Indonesian tobacco company 92% owned by Philip Morris
  - Net cash balance sheet
  - 10% dividend yield
- **Fortune REIT**
  - Hong Kong suburban mall REIT
  - Most tenants are non-cyclical (F&B, supermarkets – discretionary spending only 10% of total)
  - Trading at 50% discount to book value
  - 25% debt to assets ratio, 6% dividend yield
- **ICTSI**
  - Global Ports operator based in Philippines with bias towards emerging and frontier markets
  - Focused on consumption goods rather than bulk commodity trading
  - 80% of assets have regulated pricing- typically inflation linked and in USD
  - Medium term growth rate of 5-6% + inflation
  - 4% dividend yield
- **Singapore Telecom**
  - Operator of telecoms businesses across Asia with large operations in Singapore, Australia, India and Indonesia
  - 7.5% dividend yield in a company which is effectively an arm of the Singapore government

- **Indian Energy Exchange**
    - Leading energy exchange with 97% market share
    - Electricity trading in India at nascent stage (4-5% penetration compared to >50% in Europe) with government keen to increase this share
    - Energy exchanges allow more efficient use of power generation – critical in a market such as India
    - Net cash balance sheet, 3.5% dividend yield
- **Infosys**
    - Leading Indian IT Services Company
    - Net cash balance sheet
    - Dividend yield of 5%
    - Medium term growth rate of 8-10%
- **Macquarie**
    - Leading Australian Financial Services Company
    - 6.5% dividend yield
    - Significant infrastructure fund management business well placed to grow in era of low rates and demand for long term, real investment returns

We sold three positions:

- **HSBC** and **OCBC**
    - Both sold as we could achieve better risk/return profiles in other stocks
    - Post Covid environment of lower interest rates and higher credit risk reduces potential upside
- **Singapore Exchange**
    - Reached our price target as current business environment led to significantly increased trading activity. We are less convinced than the market that this is a permanent uplift in earnings potential.

Removing the Front-End Charge

As you will know, we took the decision to remove the "temporary" front-end charge on the Class 2 and U Shares and therefore "re-open" the fund to existing investors for the first time since 2013. This was as a result of our traffic light system finally giving us enough green lights to do so. I believe that, because of the current risk aversion, the valuations available in the market today are as good as I have seen since late 2008. Of course, I do not know what will happen to dividends in 2020 but my focus is on what happens in 2021, 2022 and beyond. I believe that revenues and dividends for your portfolio will be higher in the future than they are today. However, the market is pricing in the opposite. I have added to my investment in the fund on 1 April and it remains, as always, by far my single biggest investment.

PORTFOLIO PERFORMANCE

Performance Summary (%)
Period ending 31.03.2020

Class 1*	**B-USD**	**Benchmark****
1 Month	-19.60	-14.01
3 Months	-27.83	-20.69
2019	11.26	19.48
2018	-9.52	-13.68
2017	32.79	37.32
2016	10.36	7.06
Since Launch+	103.72	21.18
Annualised Since Inception	8.00	2.10

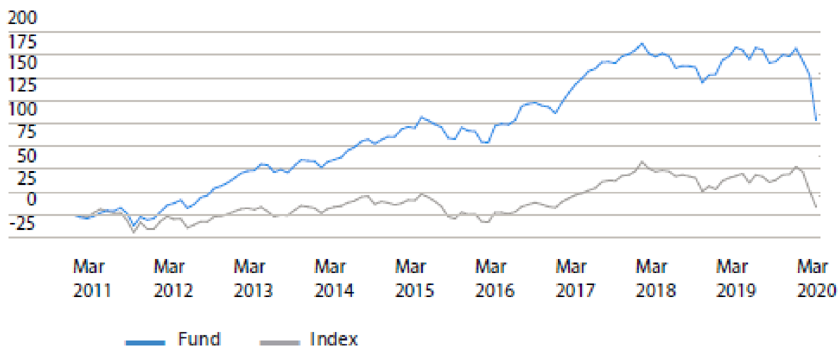
Source: Morningstar

* Class 1 shares were closed to further investment on 30th November 2012

**MSCI Asia Pacific ex Japan

+ Launch date: B 31.12.2010

Fund Performance – Class B (USD) (%)



Source: Morningstar. Total return net income reinvested.

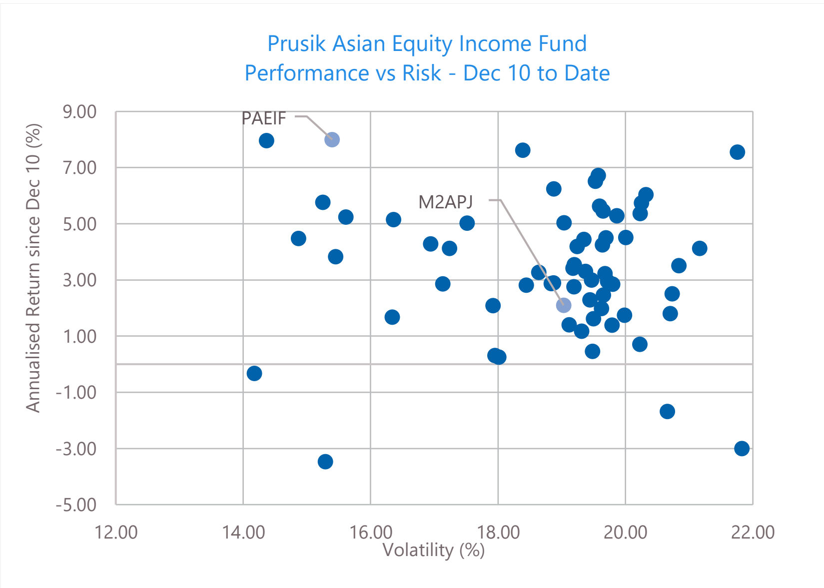
Monthly Performance Summary (%)

	Jan	Feb	Mar	Apr	May	June	July	Aug	Sept	Oct	Nov	Dec	Total
2020	-4.88	-5.63	-19.60										
2019	6.09	1.66	3.47	-0.99	-3.59	4.65	-0.84	-5.11	0.62	2.79	-0.62	3.19	11.26
2018	2.51	-3.76	-1.26	1.34	-1.18	-4.76	0.96	-0.13	-0.52	-6.38	3.49	0.21	-9.52
2017	5.49	4.77	3.98	2.69	3.25	1.11	2.71	0.06	-0.54	2.91	0.85	1.61	32.79
2016	-6.04	-0.37	10.28	0.95	-0.38	2.46	7.56	1.20	0.54	-1.43	-0.68	-3.16	10.36
2015	4.35	1.41	-0.70	6.01	-1.69	-1.97	-1.63	-6.01	-0.70	7.04	-1.91	-0.33	3.17
2014	-4.34	4.03	1.50	1.58	4.63	2.14	3.50	1.24	-2.54	2.31	2.00	-0.05	16.79
2013	3.93	1.78	0.35	4.57	-0.53	-4.95	1.87	-2.24	5.07	4.15	-0.56	-0.25	13.45
2012	8.12	6.54	1.92	3.20	-7.67	3.84	6.72	1.92	6.36	1.97	2.76	3.63	45.77
2011	-2.68	-1.46	2.55	3.90	2.58	-0.60	3.56	-6.06	-12.80	10.62	-3.52	1.79	-3.96

RISK ANALYSIS

Risk Metrics	**Fund (%)**
Beta	0.83
Alpha (%)	6.10
Sharpe Ratio	0.74
Volatility (%)	15.40

Source: Morningstar
Since inception: B 31.12.2010



Source: Morningstar

THEMATIC & GEOGRAPHICAL BREAKDOWN

Top 5 Holdings (%)

Samsung Electronics Co Ltd - Pref	7.6
CK Hutchison Holdings Ltd	7.2
Power Grid Corporation of India	6.7
CK Asset Holdings Ltd	6.1
ITC Ltd	5.2
Total Number of Holdings	37

Portfolio Financial Ratios*

Predicted Price/Earnings Ratio	8.8x
Predicted Dividend Yield (%)	6.8

Thematic Breakdown (%)

Consumer	18.6
Real Estate	18.4
Communications Infrastructure	16.8
Technology	14.9
Power Utilities	14.8
Transport Infrastructure	8.7
Financials	4.6
Cheung Kong / Hutchison	3.1
Cash	0.1

Geographical Breakdown (%)

Hong Kong	34.5
India	16.6
China	11.1
Korea	7.6
Indonesia	7.5
Macau	7.3
Thailand	4.5
Australia	3.8
Philippines	3.6
Singapore	3.3
Cash	0.1

All data as at 31.03.2020. Source Prusik Investment Management LLP, unless otherwise stated

FUND PARTICULARS

Fund Facts

Fund Size (USD)	566.4m
Launch Date	31st December 2010
Fund Structure	UCITS III
Domicile	Dublin
Currencies	USD (base), GBP, SGD

Management Fees

Annual Management Fee
1% p.a paid monthly in arrears

Performance Fee
Class 1: None
Class 2 and Class U: 10% of the net out-performance of the MSCI AC Asia Pacific Ex Japan
Gross Return Index (USD), with a high-water mark.

Temporary Front End Charge: As of 01 April 2020 we are removing the front end charge to the fund.

Dealing

Dealing Line	+353 1 603 6490
Administrator	Brown Brothers Harriman (Dublin)
Dealing Frequency	Daily
Valuation Point	11am UK time
Dealing Cut - off	5pm UK time
Min. Initial Subscription	USD 10,000
Min. Subsequent Subscription	USD 5,000

Share Class Details

Class 1*			SEDOL	ISIN	Month end NAV
A USD	Unhedged	Non Distributing	B4MK5Q6	IE00B4MK5Q67	209.57
B USD	Unhedged	Distributing	B4QVD94	IE00B4QVD949	140.76
C GBP	Hedged	Distributing	B4Q6DB1	IE00B4Q6DB12	131.01
D SGD	Hedged	Distributing	B4NFJT1	IE00B4NFJT16	132.04

*Class 1 shares were closed to further investment on 30th November 2012.

Class 2*			SEDOL	ISIN	Month end NAV
X USD	Unhedged	Distributing	B4PYCL9	IE00B4PYCL99	125.74
Y GBP	Hedged	Distributing	B4TRL17	IE00B4TRL175	117.55
Z SGD	Hedged	Distributing	B6WDYZ1	IE00B6WDYZ18	122.50

*Class 2 shares are open to current investors only and were closed to new investors as of 30th November 2012. Performance fee based on individual investor's holding

Class U*			SEDOL	ISIN	Month end NAV
U GBP	Unhedged	Distributing	BBP6LK6	IE00BBP6LK66	128.22

*Class U shares are open to current investors only. Performance fee based on fund performance as a whole

Dividend Dates

Dividends paid twice annually (January and July)

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