PRUSIK

LONG ONLY ABSOLUTE RETURN INVESTING IN ASIA

Prusik Asian Equity Income Fund

Quarterly Investment Report
30 September 2020

FOR PROFESSIONAL INVESTORS ONLY

3Q20 Review and Outlook

Attribution Analysis

	Avg % Wgt		Total Return (%)		Allocation bps	Selection bps	Total Attribution bps
	PAEIF	MXAPJ	PAEIF	MXAPJ			
Australia	2.6%	13.5%	5.5%	2.6%	99	-4	51
Vietnam	2.0%	0.0%	17.8%	0.0%	27	0	27
Thailand	3.6%	1.9%	-2.2%	-13.8%	-36	52	12
Malaysia	1.1%	1.6%	-2.7%	2.7%	4	-6	-4
Philippines	4.2%	0.7%	2.1%	-2.6%	-46	18	-17
South Korea	8.9%	11.1%	10.8%	12.6%	0	-15	-20
Singapore	4.1%	2.2%	-6.3%	-1.0%	-25	-24	-40
Taiwan	0.0%	11.9%	0.0%	17.3%	-80	0	-103
Indonesia	5.5%	1.3%	-17.5%	-6.9%	-47	-76	-143
India	18.8%	7.8%	1.2%	15.2%	52	-250	-174
China	6.8%	36.7%	2.6%	13.7%	-138	-77	-236
Hong Kong	34.8%	9.9%	-3.4%	0.9%	-175	-156	-330

Source: Bloomberg/Prusik

The pattern of underperformance is very similar to that of the past 12 months: Our lack of exposure to Chinese internet stocks and our high exposure to traditional stocks in Hong Kong accounts for the bulk of our underperformance. In addition, our Indian and Indonesian portfolios underperformed although there was no particular reason that we can identify behind that (it was due to de-rating rather than any fundamental change).

2020 vs 2000

Today's market reminds me of the 1999/2000 tech bubble in many different ways:

- Extreme overvaluation within a narrow range of stocks.
- Optimism that the current growth prospects of internet stocks will be sustained, and no future competitor will be able to dislodge current market leaders.
- Pessimism about the growth of most other sectors in the economy.
- Temporarily increased demand for technology products (in 1999, this was due to "Y2K" spending vs today where it is due to WFH/ecommerce).
- Significant monetary support (in 1999 due to fears over Y2K).
- Momentum investing popular as investors give up following fundamentals.
- High quality stocks with no "story" being de-rated (e.g. Unilever and Diageo fell 30% in the 12 months leading up to the Nasdaq peak in March 2000).
- Retail investors very active (particularly in hot sectors).
- The invention of new ways of measuring valuation[1].

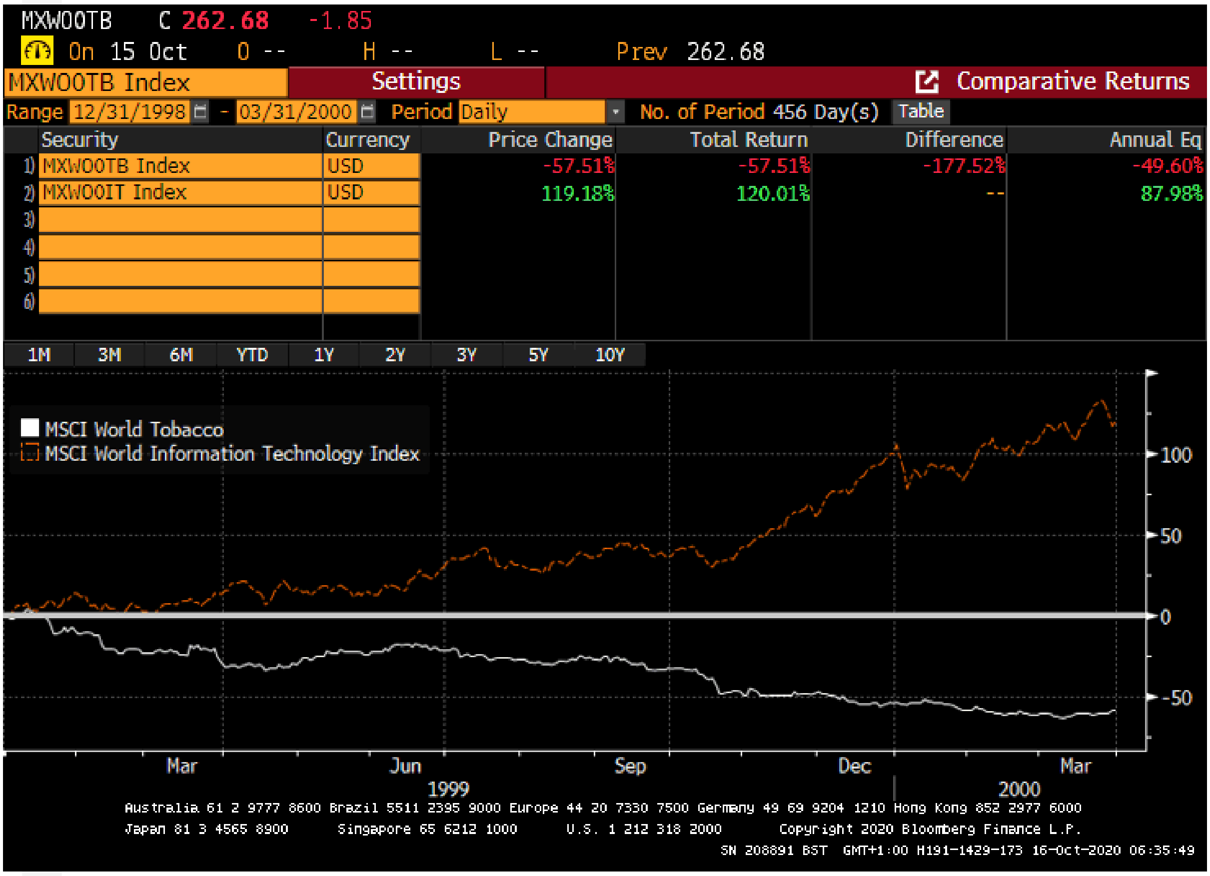
[1] We read a piece of research by one strategist suggesting that certain growth stocks could attract "infinitely high" valuations due to zero interest rates.

- No "catalyst" in sight to end the boom[2].
- Value investing firms closing down after years of poor performance.

There is one sector I think, in particular, which highlights why thinking about the 1999/2000 bubble is relevant to investing today and which also explains why I think investing in unloved sectors in 2020, will likely produce superior returns over the next decade. This is the Tobacco sector.

Tobacco – The Unloved Sector

During March 2000 it was a difficult time to be a value investor. Julian Robertson had just closed his fund claiming that he didn't understand the markets anymore[3]. People had written Warren Buffett off for not buying into the tech bubble. And global tobacco stocks had fallen by 58% since the beginning of 1999 vs a 120% return from the global tech index for 178% of relative underperformance.



Source: Bloomberg

[2] And of course even after the dot.com crash it is no clearer what the catalyst was to burst the bubble.
[3] https://www.nytimes.com/2000/03/31/business/the-end-of-the-game-tiger-management-old-economy-advocate-is-closing.html.

Source: Bloomberg.

Readers can probably guess what happened next. In the subsequent decade, tobacco stocks returned 558% compared to the tech sector which fell 58%.

However, what is interesting to me is **that this performance gap occurred even though the tech bulls were "right"**. I.e. the internet went on to be even bigger and more profitable than even the bulls dared predict and tobacco usage continued to decline in most developed markets as regulation on smoking became tighter and excise taxes increased. In my opinion, there a few key reasons for this:

- **Valuation**. If you pay a high enough price, future growth will not be enough to offset a valuation de-rating. If you pay a low enough price, even modest growth can lead to excellent returns.
- **Competition**. Analysts are good at forecasting demand but often less adept at forecasting supply. High profits lead to higher competition which lead to lower returns. Disruptive companies can gain market share quickly but they can also be disrupted themselves by future competitors. On the other hand, a business like tobacco has no new competitors (who would enter a shrinking business with no ability to advertise?).
- **Capital allocation**. Tobacco companies just returned excess cash to shareholders via dividends and buybacks. Tech companies often wasted their cash flow on expensive acquisitions and unproductive research and development.

The point of this story is that it isn't about whether the internet will continue to grow in importance over the coming decade or whether sectors that are currently facing difficult operating conditions will continue to see challenges. **Rather it is just that the expectations for one versus the other are at such an extreme**. It highlights that focusing on fundamentals (rather than just narratives) is important. What are the lessons for today? I think the characteristics that led tobacco to such strong performance were the same ones that we look for today in PAEIF.

- Stable, predictable cash flows.

- Low cyclicality of earnings.
- Dominant market position.
- Good capital allocation discipline.
- Trading with significant upside to normalised valuations.

This means that we tend to favour stocks that look similar to tobacco stocks 20 years ago including:

- **Consumers** (including tobacco).
- **Telecoms** (including mobile phone towers).
- **Power Infrastructure** (Avoiding generation and focusing on transmission & distribution).
- **Real Estate** (in selected markets where we believe a significant move to WFH is less likely).
- **Toll Roads**.

Note that there are some areas traditionally favoured by value investors that we don't own as, even though they have significant upside potential in certain macro environments, they don't have the characteristics that we seek. These include:

- **Banks**. Too cyclical, no earnings visibility, reliant on interest rates rising. We have a very small amount of exposure here (3% of NAV) but, in general, we avoid this sector.
- **Energy**. Too cyclical, no earnings visibility, reliant on forecasting oil prices correctly.

Portfolio Activity

The biggest change in the portfolio in the past 12 months has been the increase in the fund's exposure to the consumer sector which has grown from less than 10% to around 25% of the portfolio.

New Positions

- **Dairy Farm**
  - **Dairy Farm** operates a number of grocery, convenience stores (7-11), home furnishings (IKEA) and health and beauty businesses across Asia.
  - Led by new CEO, Ian McLeod (known for turning around Coles in Australia), we believe returns are likely to improve to market levels as the company exits non-core businesses (e.g. Taiwan grocery).
- **Mindspace Business Parks REIT**
  - **Mindspace** owns several business parks in India which cater largely to multi-national companies taking advantage of India's technology workforce[4].
  - Tenants include Accenture, Facebook, Amazon and Bank of America.
  - Low risk as market rents are 23% above contracted levels (with 4-5% annual escalations built into existing contracts). Collection rates are running at 98% for 2Q20.
  - Offering a 7.5% dividend yield with high single-digit growth in distributions and low debt (15% debt to market value).
  - Strong corporate governance (50% independent Directors, manager can be removed with 60% approval of independent shareholders).
- **Kasikorn Bank**
  - 8x P/E, 5% dividend yield and 0.5x Price to book.
  - Well capitalised bank with conservative management.

[4] India produces 2.6m STEM Graduates annually

  - Key catalyst will be re-opening of Thai tourism industry (=11-12% of GDP) as Thailand has virtually no covid cases.
  - Stock implies ROE will remain <5%. However, a return to 8-10% levels is likely once economy recovers.
- **Nagacorp**
  - Monopoly casino provider in Phnom Penh, Cambodia.
  - August data shows company operating at 90-95% of pre-Covid levels.
  - Has continued to pay dividends throughout downturn.
  - Free cash flow yield of 8-9% and offering a 6% dividend yield.
- **Thai Beverage**
  - Virtual monopoly in Thai Spirits business (90% market share).
  - 52% shareholding in Saigon Brewery.
  - Stock has been weak due to lockdown in Thailand but August data showed both spirits and beer business in Thailand experiencing positive year-on-year growth.
  - 14x P/E and 4% dividend yield.

Exited Positions

- **Cromwell European REIT**. Limited upside to target price. Better value in pure Asian real estate.
- **HM Sampoerna**. Reached target price.
- **Indian Energy Exchange**. Reached target price.
- **Infosys**. Reached target price.
- **Link REIT**. Switched into **Sun Hung Kai** Properties for better risk/return characteristics. We are also concerned about their capital allocation following the purchase of a London office asset.
- **Sarana Menara Nusantara**. Reached target price.
- **Travelsky**. Concern that China international travel market will recover more slowly than market is implying.

Final Note

We are very aware that the performance of the fund has been extremely poor over the past 12 months and are thankful for the support and patience of our investors. We do not take this support for granted and are very keen to return to generating the returns that you expect (and we believe we can deliver). Although we can't necessarily do anything other than continue to do the best job we can, we believe that **the current opportunity set today is as good as I have ever seen it and we believe the outlook for future returns (in both absolute and relative terms) is extremely bright**.

The base case for our fund is that dividend growth for our portfolio continues to grow at 5-10%. This would lead to a "mid to low teens" total return, assuming valuation remains unchanged. If valuations revert to the mean then this would lead to upside of approximately 60% in absolute terms or 90% relative to the MXAPJ[5].

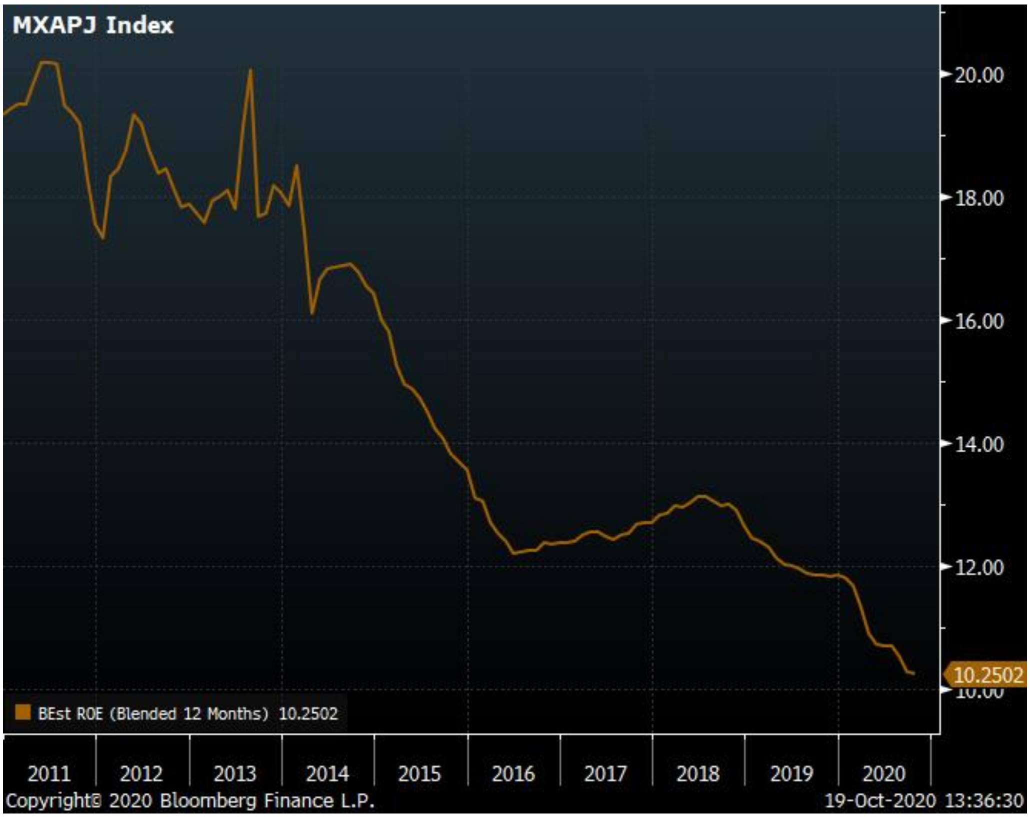
Ultimately, my belief is that there is a reasonably high chance (>50%) that the world does revert to the mean and Covid-19 is less of an issue in 2022 than it is today and well managed businesses, with good balance sheets, will survive and prosper and that the world will not become 100% digital. And just like the tobacco sector in 1999, it is not that the concerns which investors have over traditional businesses are unwarranted, it is just that the current valuations already discount that pessimistic view and as long as these companies continue to pay and grow dividends, over time, the market

[5] Using an equal weight of P/E, P/B and Dividend yield. 10-year average data.

will reflect that in higher valuations. There is also the prospect that earnings growth might be above these levels driven by the ROE cycle in Asia.

Return on Equity

The chart below shows the forecast ROE for the MXAPJ over the life of PAEIF. ROE in Asia has been in a downcycle for the last decade with returns falling from 20% in 2011 to around 10% today. This is why earnings growth has been so poor over this period, despite annual nominal GDP growth in the high single-digits. Even though PAEIF has been less affected, the ROE on our current portfolio is approximately 12% which is below the 10-year average of 15%.



What is interesting is that over a longer time period, earnings growth in Asia has actually been higher than the US. However, it was significantly higher for the first decade of this century and much lower for the second decade. It is reasonable to assume that, over the long term, earnings growth will be approximately in line with nominal GDP growth and therefore a return to a 5-10% growth is likely in the next decade. One could also make the case that, following a period of ROE decline and minimal earnings growth, the period from 2020-2030 might well see double-digit earnings (and dividend) growth.

	MXAPJ	**S&P500**
EPS growth 2000-2019	+8.2%	+5.2%
EPS growth 2000-2010	+16.0%	+4.8%
EPS growth 2010-2019	+0.1%	+6.7%
DPS growth 2000-2019	+5.8%	+6.5%
DPS growth 2000-2010	+9.8%	+3.4%
DPS growth 2010-2019	+2.8%	+11.0%

PORTFOLIO PERFORMANCE

Performance Summary (%)
Period ending 30.09.2020

Class 1*	B-USD	Benchmark**
1 Month	-4.92	-2.27
3 Months	-1.47	9.57
Year to Date	-18.85	2.97
2019	11.26	19.48
2018	-9.52	-13.68
2017	32.79	37.32
2016	10.36	7.06
Since Launch⁺	129.09	57.33
Annualised Since Inception	8.87	4.76

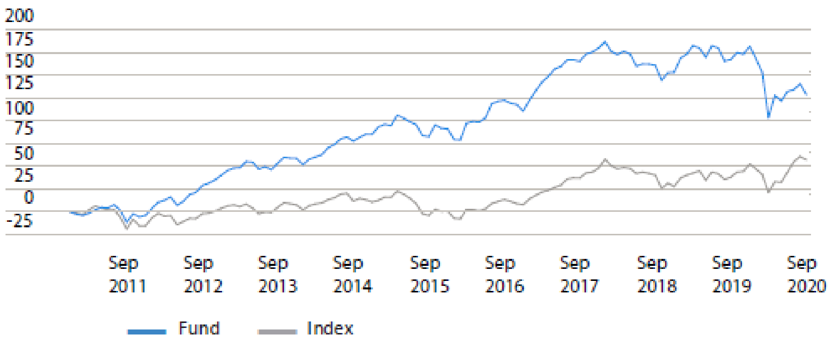
Source: Morningstar

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

**MSCI AC Asia Pacific Ex Japan Gross Return Index (USD)

⁺ Launch date: B 31.12.2010

Fund Performance – Class B (USD) (%)



Source: Morningstar. Total return net income reinvested.

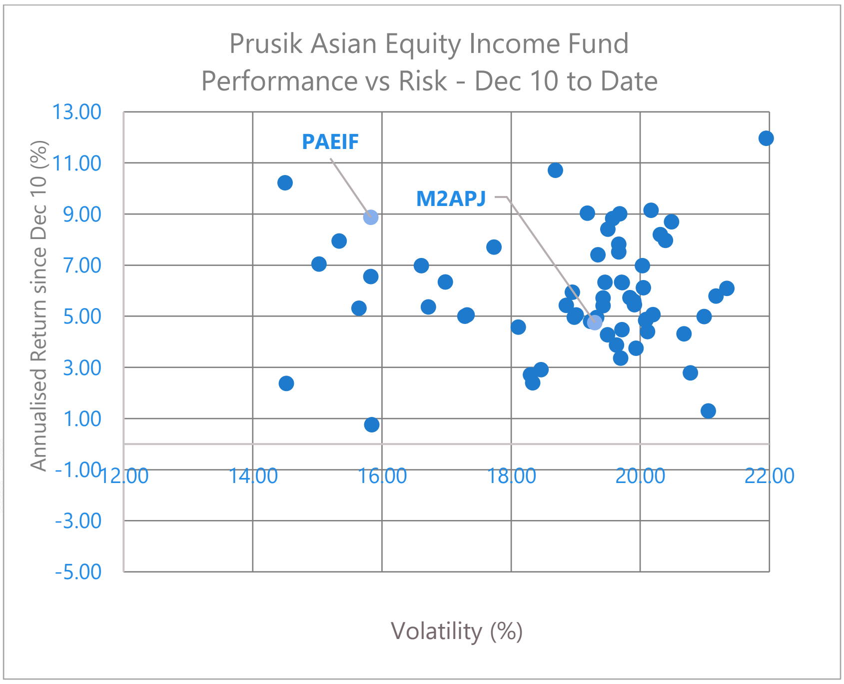
Monthly Performance Summary (%)

	Jan	Feb	Mar	Apr	May	June	July	Aug	Sept	Oct	Nov	Dec	Total
2020	-4.88	-5.63	-19.60	11.98	-2.62	4.67	0.84	2.76	-4.92				
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	0.81
Alpha (%)	5.22
Sharpe Ratio	0.80
Volatility (%)	15.83

Source: Morningstar
Since inception: B 31.12.2010



Source: Morningstar

THEMATIC & GEOGRAPHICAL BREAKDOWN

Top 5 Holdings (%)

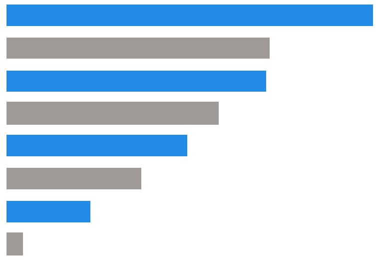
Power Grid Corporation Of India Ltd	6.3
Samsung Electronics-Pref	5.5
ITC Ltd	5.2
AIA Group Ltd	4.7
CK Asset Holdings Ltd	4.7
Total Number of Holdings	43

Portfolio Financial Ratios*

Predicted Price/Earnings Ratio	9.2x
Predicted Dividend Yield (%)	6.2

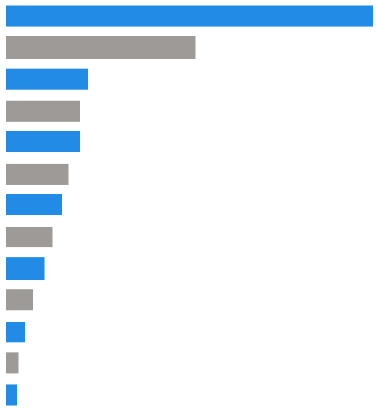
Thematic Breakdown (%)

Consumer	24.3
Communications Infrastructure	17.4
Real Estate	17.2
Power Utilities	14.0
Transport Infrastructure	11.9
Financials	8.8
Technology	5.5
Cash	1.0



Geographical Breakdown (%)

Hong Kong	35.0
India	18.1
Korea	7.8
China	6.9
Singapore	6.9
Macau	5.8
Indonesia	5.2
Philippines	4.3
Thailand	3.5
Vietnam	2.5
Australia	1.8
Malaysia	1.2
Cash	1.0



All data as at 30.09.2020. Source Prusik Investment Management LLP, unless otherwise stated

FUND PARTICULARS

Fund Facts

Fund Size (USD)	627.2m
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 paid quarterly.

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	235.66
B USD	Unhedged	Distributing	B4QVD94	IE00B4QVD949	153.81
C GBP	Hedged	Distributing	B4Q6DB1	IE00B4Q6DB12	142.13
D SGD	Hedged	Distributing	B4NFJT1	IE00B4NFJT16	143.58

*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	137.41
Y GBP	Hedged	Distributing	B4TRL17	IE00B4TRL175	127.54
Z SGD	Hedged	Distributing	B6WDYZ1	IE00B6WDYZ18	133.21

*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	134.89

*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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