



ELLERSTON ASIA

Ellerston Asian Investments

Investor Update October 2020

Performance

PERFORMANCE TO 30 SEPTEMBER 2020

- EAI was up 2.24% during the month versus the benchmark which was up 1.45%.
- CYTD in 2020 EAI is up 5.07% and has outperformed the benchmark by 3.54%.
- MTD in October EAI has generated positive absolute returns and positive alpha.
- The most recent NTA (October 12th) is \$1.2753.

%	1 Month	3 Months	6 Months	1 Year	2 Years p.a.	Since Inception p.a.**
EAI Net	2.24%	7.64%	11.36%	14.44%	10.25%	7.63%
Benchmark*	1.45%	5.49%	8.61%	8.53%	4.76%	7.51%
Alpha	0.79%	2.20%	2.75%	5.91%	5.49%	0.12%

. * Benchmark is MSCI Asia ex Japan (non-accumulation) Index in AUD. Inception is Sept 2015.

RISING & SUSTAINABLE DIVIDEND

- Ellerston Asian Investments aims is to have a **sustainable dividend policy** based on multiple years of profit reserves.
- As shown below, EAI began paying dividends during Financial Year 2019 and paid higher final and interim dividends in the following financial year.
- In recognition of our **strong performance** and franking credit balance in FY20, EAI has declared and paid a final dividend of **2.5 cents per share fully franked**. This is an increase of **67% on the interim dividend**.
- As of June 30, 2020 EAI had a franking credit balance of 8.5c per share. As at the end of September the Company had franking credits and a current year tax liability combined of 7.5 cents per share.

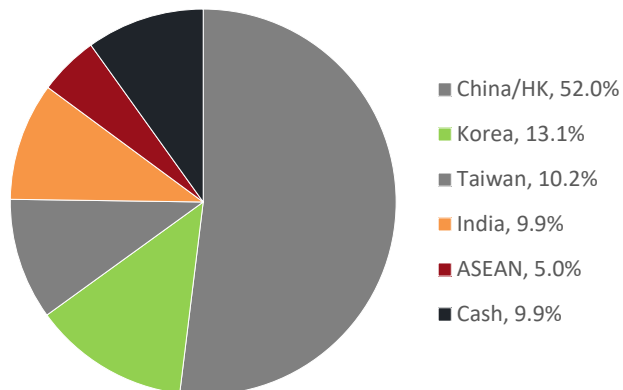
Ex Dividend Date	Pay Date	Amount	Franking
4 Sept 2020	2 Oct 2020	2.5c	100%
5 March 2020	27 March 2020	1.5c	100%
4 Sept 2019	4 Oct 2019	1.5c	100%
20 March 2019	5 April 2019	1.0c	100%
5 Sept 2018	5 Oct 2018	1.0c	100%

Portfolio Positioning

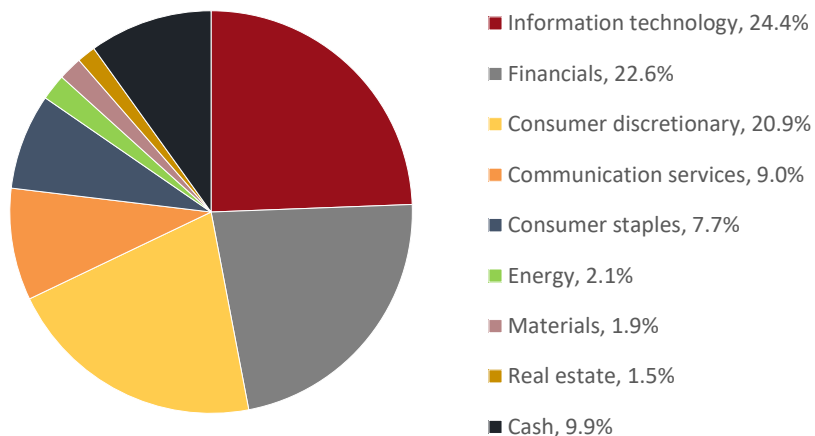
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PORTFOLIO CHARACTERISTICS AS OF 30 SEPTEMBER 2020

Country Exposure



Sector Exposure



Top 10 Holdings	Portfolio Weight (%)
Alibaba	13.3%
TSMC	9.3%
Samsung Electronics	9.1%
Tencent	8.0%
Hong Kong Exchanges	5.2%
Ping An Insurance	4.9%
DBS Group	3.0%
Hindustan Unilever	2.7%
China Merchants Bank	2.7%
Reliance Industries	2.1%
Total	60.3%



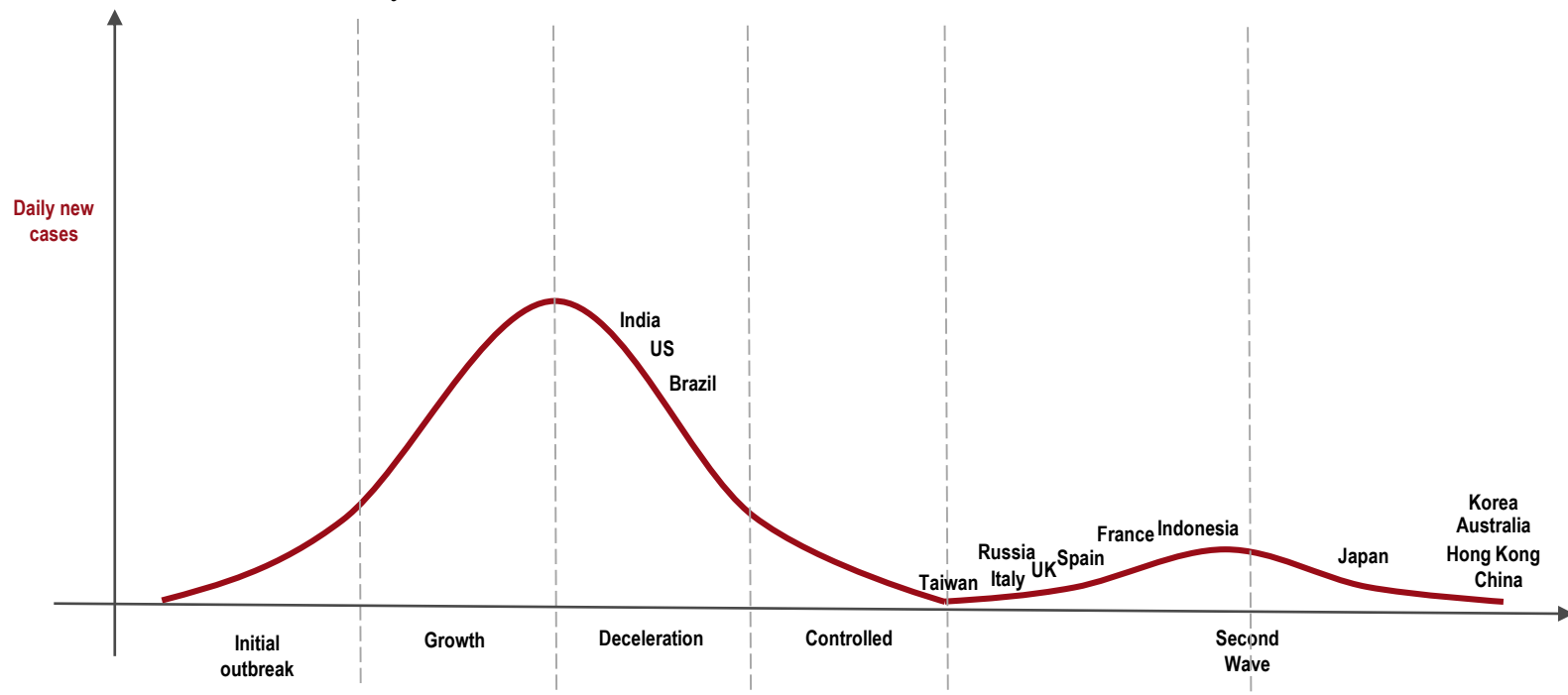
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Market Outlook

COVID-19

REOPENING AND SECOND WAVES

- Most countries in Asia, except India, are in the COVID deceleration phase. Second waves in Asia are currently contained and economies are returning to normal. We are closely watching second waves in Europe.
- Our call that COVID would be FIFO (First In First Out) in nature has informed country allocation, with a preference for North Asia over ASEAN and India.
- This has been the right call in Asia. These markets have outperformed significantly since the global outbreak in late February.



US China Relations

SCENARIOS AND TAIL RISKS

Scenario	Description	Investment Implications for Equities	Time Frame	Probability
Base Case	The US is in hegemonic decline and China is in ascendancy. Ongoing tension in trade, technology, capital markets and foreign policy is the new normal. Investors need to get used to “competitive coexistence.”	America looks like an Emerging Market but is priced like a superpower (21x PE). China is priced like an Emerging Market (13x PE) but is acting like a superpower. Bet on the second horse (i.e. China).	10 Years +	High
US Bear Case	November election is disputed, wide spread civil unrest ensues, Trump refuses to leave office, constitutional crisis ensues, USD collapses, US economy collapses. Trajectory of hegemonic decline steepens and becomes irreversible.	US centric global portfolios get smashed. Buy gold. Utilize option strategies going into November. Buy domestic demand stocks in EM (beneficiaries of weak USD).	6 months	Medium, getting lower
China Bear Case	China oversteps new geopolitical position and starts conflict with Taiwan. HK situation worsens materially. Taiwan conflict leads to global involvement and middle powers have to pick sides. Xi gets into trouble at home as he abandoned “hide and bide” too soon. No successor in sight.	Buy gold. Utilize option strategies and stay liquid. Avoid equities in China, the US and middle powers who could get caught in between. Avoid supply chain reliant companies. Invest in domestic demand stocks in domestic demand economies like India.	1- 5 years	Very low
US Bull Case	Trump or Biden wins in an undisputed landslide. Markets rally sharply. Fiscal policy continues to support the post-COVID economy. Interest rates stay at zero.	US equities rally sharply and the USD appreciates. China equities perform well but lag relative to the US. The case for exporters increases. Rotation to value.	1- 4 years	Medium
China Bull Case	Tensions abate in Trump’s second term or Biden wins but his administration does not include super hawks like Navarro and Lighthizer so relations are more civil and predictable. Chinese economy booms post COVID due to ultra accommodative policies. China surpasses the US economically, militarily and technologically. Xi goes on to a 3 rd term with total support.	Buy Chinese equities, particularly Chinese tech.	5-10 years +	Medium

US Election

SCENARIOS AND OUTCOMES

Scenario	Scenario 1: Red Wave	Scenario 2: Mixed Outcome	Scenario 3: Blue Wave	Scenario 4: Tail Risk
Outcome	Trump wins. Republicans retain the Senate and take the House.	Trump wins but Democrats control the House and/or Senate. Biden wins but Republicans control the House and/or Senate.	Biden wins. Democrats take the Senate and retain the House.	Election outcome is unclear for an extended period of time and/or outcome is clear but disputed by the loser. Messy transition.
Probability	5%	35%	50% = Base Case	10%
Policies	Small stimulus focused on further tax cuts and manufacturing. Further deregulation. Focus on energy independence. Continued hawkish stance on China, but possibly not as bad as Term 1.	Policy gridlock. Limited legislative/policy change.	Large stimulus focused on infrastructure and green technology. Partial rollback of Trump tax cuts. Greater regulatory focus on US big tech. More rationale and predictable China policies.	Policy vacuum in the short term.
Equities	Positive for US equities, mixed for Asian equities. Outcome for EM flows depends on the reaction of the USD.	Negative for global equities initially as the probability of a large stimulus is reduced. Biden win better for Asia in the near term.	Positive for global equities as its a clean/uncontested victory and expectations of more stimulus increase.	Negative for US and global equities.
Comment	Sharp rotation into cyclicals a possibility. Trump bump 2.0.	Defensives and quality could be relative winners initially. EM and non-US DM could outperform in the short term.	Sharp rotation into cyclicals a possibility, with the exception of oil. Asian/EM equities could relief rally on less antagonistic trade and investment policies. Asia tech could outperform US tech on potential regulatory scrutiny for the latter.	Asia and non-US DM to outperform the US. Losers could be high beta stock that have performed well since March bottom. Significant profit taking as investors want to lock in gains.



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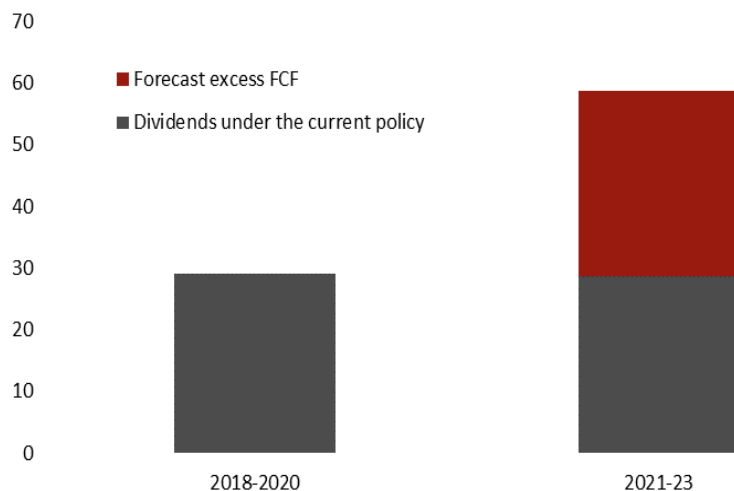
Stock Discussion

Samsung Electronics

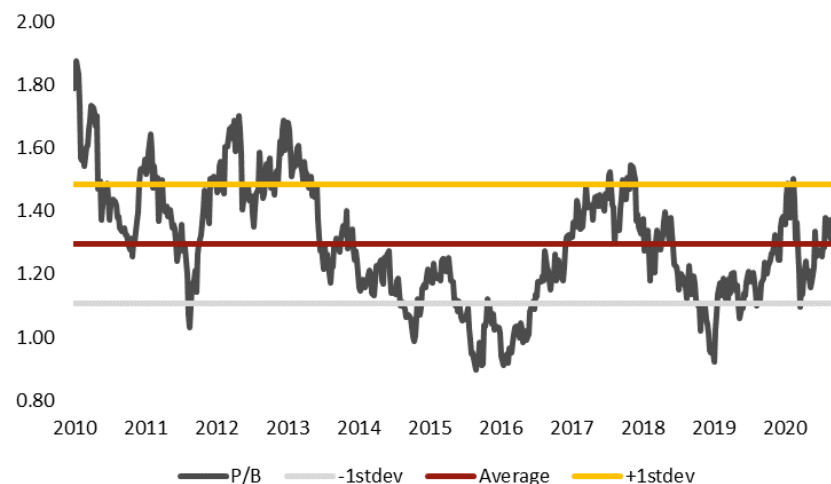
BENEFICIARY OF US/CHINA TENSIONS AND 5G

- Samsung is global #1 in smartphones, memory chips and display panels. Global top 5 in foundry and network equipment.
- The company has a fortress balance sheet, is net cash and is becoming increasingly shareholder friendly.
- Potential net beneficiary of US sanctions against Huawei and SMIC. Huawei issues unlikely to go away under a Biden administration.
- Has both short term (memory cycle upturn, capital management) and long term catalysts (5G).
- Valuation is cheap trading on 1.35x P/B and 12x P/E vs ROE of ~13% and 3yr EPS CAGR of ~20%. Could be a beneficiary of rotation to cyclicals.
- We have held the stock in EAI since inception and is up ~70% over this period.

Samsung Electronics capital management upside (KRWtn)



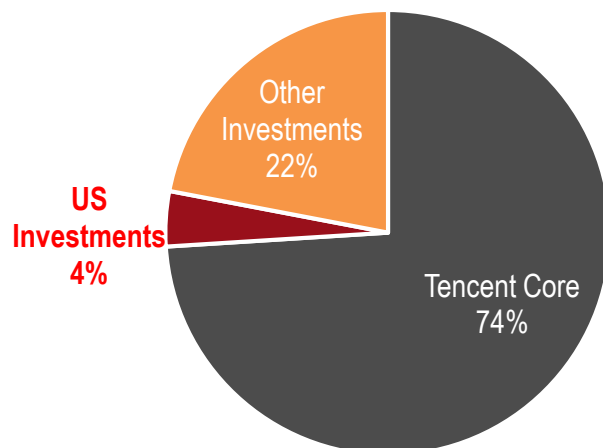
Samsung Electronics price/book



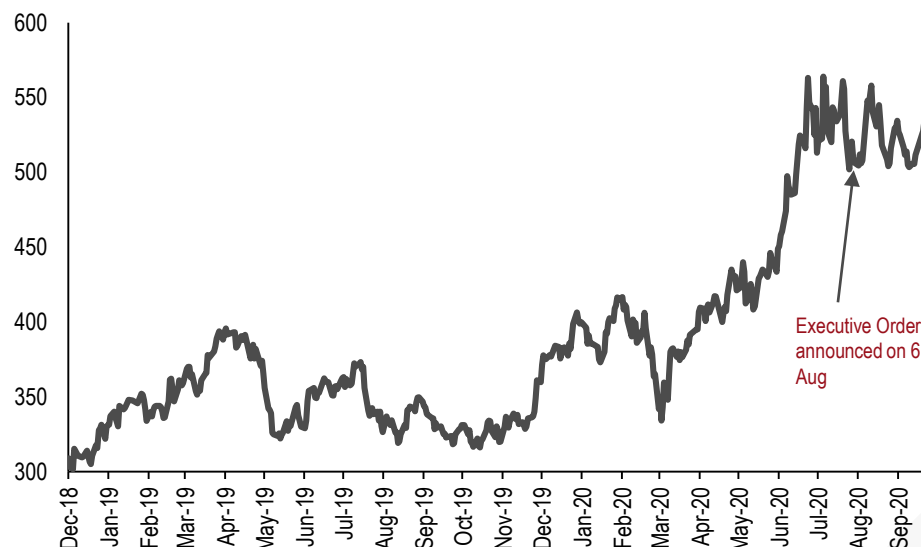
REDUCED RISK FROM EXECUTIVE ORDERS GIVEN LEGAL ISSUES AND US ELECTION OUTLOOK

- President Trump's Executive Order (Aug 6) to ban WeChat was blocked by US Magistrate Judge Laurel Beeler as she questioned the necessity of such ban in protecting national security. Ban may also violate First Amendment and the right to free speech of Chinese Americans and Chinese speakers in America.
- Our discussion with management suggest that the EO is focused on US jurisdiction and on WeChat only, not Tencent's other businesses.
- Risk is also mitigated as Trump gave blessing to the Tiktok-Oracle deal which sees Tiktok retaining control, limiting worst case scenario for Tencent's US gaming assets (mostly minority investments by Tencent).
- A Biden win would likely reduce the near term risk of governing by anti-China EO. We've increased our Tencent position back to ~8%.

Our Tencent SOTP



Share price well supportive at HK\$500



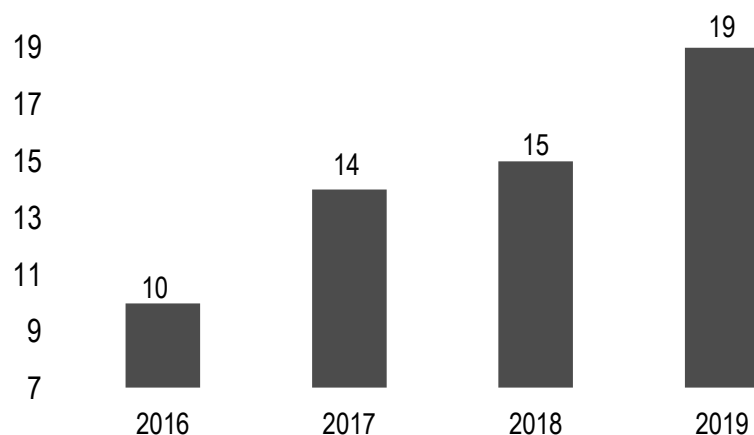
Source: Ellerston Asia, Bloomberg

*Key US investments include Tesla, Activision Blizzard, Snapchat, Universal Music, Warner Music, Spotify, Epic Games, etc.

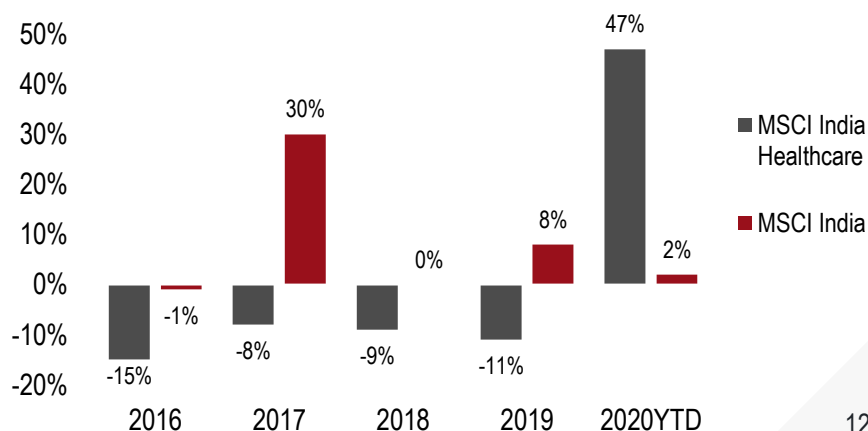
INDIAN PHARMA TO BENEFIT FROM A CHANGE IN ADMINISTRATION

- Indian Pharma companies supply about 40% of the volume of finished dosage pharma products in the US. In the past 2 years, while the world has been focused on the US-China trade war, the US has been running a stealth trade war with India targeting the Pharma sector.
- Since the Trump administration was elected, the number of FDA warning letters issued to Indian Pharma companies has nearly doubled. This impacted about 18% of the total pipeline for drug makers in India. As a result, the Indian Pharma index underperformed the broader Indian markets between 2016-19.
- The COVID-19 outbreak has seen the Indian Pharma index outperform. We believe a Biden win will likely see a change in FDA's stance towards Indian Pharma which should see a further rerating of the sector, and hence we have reinitiated a position in Sun Pharma.
- Sun Pharma is India's largest pharma company and is currently trading below its 5-year PE average of 27x with a 3-year earnings CAGR of 15%.

FDA Warning Letters to Indian Pharma Companies



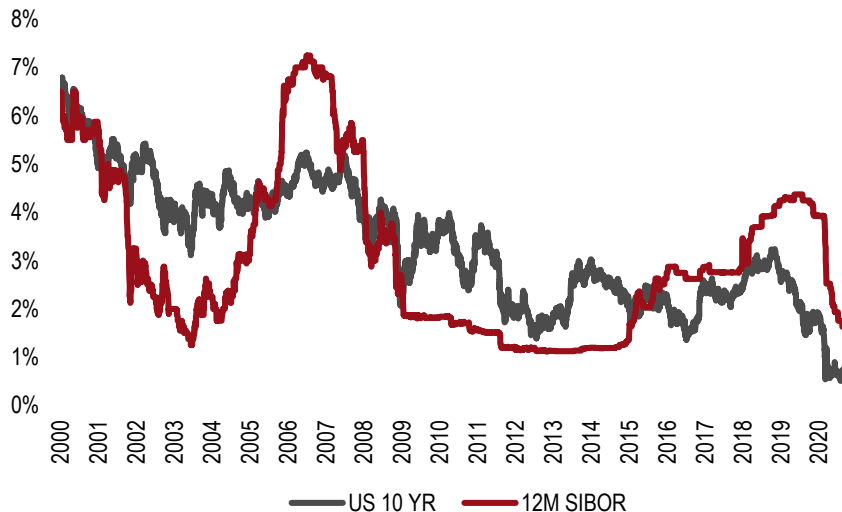
Performance – Indian Pharma vs Broader Indian Markets



SINGAPORE BANKS ARE BENEFICIARIES OF HIGHER RATES IN THE US

- The Singapore banks, DBS, OCBC and UOB, have very low loan to deposit ratios. As such, when rates rise, assets reprice faster than liabilities and margin expand.
- Singapore monetary policy is synchronized with US monetary policy. SIBOR has tracked the US 10 year very closely over the last 10 years.
- A Biden win (and/or Blue Wave) will likely be positive for rates as additional fiscal stimulus may ultimately prove inflationary.
- DBS is our top pick in the Singapore banks and one of the only stocks EAI owns in all of ASEAN.
- The bank is currently trading at <1x P/B and 11x PE with a 3 year growth CAGR of 12%.

US 10 Year vs SIBOR



DBS P/B Ratio – More than 1 s.d. below average





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Q&A

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Thank you

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