

# Ellerston Asian Investments Limited (ASX:EAI)

Performance Report | May 2020

## PERFORMANCE SUMMARY

Performance	1 Month	3 Months	6 Months	1 Year	3 Year	Since Inception (p.a.)
Net <sup>^</sup>	-1.28%	-7.46%	-2.34%	7.93%	5.66%	5.75%
Benchmark*	-2.77%	-8.49%	-5.24%	2.02%	2.93%	5.97%
Alpha	1.49%	1.03%	2.90%	5.91%	2.73%	-0.22%

Source: Ellerston Capital

<sup>^</sup> The net return figure is calculated before all tax provisions, after fees & expenses, includes the effects of the share buyback, and excluding the effects of option exercise dilution. Past performance is not a reliable indication of future performance

\*MSCI Asia ex Japan (non-accumulation) (AUD)

## PORTFOLIO COMMENTARY

May saw a continuation of the global market rally that started on March 23, 2020. Since then, both the S&P 500 and the MSCI World Index are up over 30% and the NASDAQ is near its all-time high. Ellerston Asian Investments (EAI) was down 1.3% during May but outperformed the benchmark by 1.5% (net). This outperformance was despite high cash levels and sector rotation out of growth (our strategy) into value. In the last 1 year, EAI has outperformed the benchmark by 5.9% (net). The strong appreciation of Australian Dollar during the month was a headwind for absolute returns. The monthly pre-tax NTA as of May 31, 2020 was \$1.1231, and the most recent daily pre-tax NTA (as of June 12) was \$1.1430

## MARKET OUTLOOK

Similar to the commentary last month, our view is that equities have rallied too far too fast and that markets have become disconnected from the underlying economies both in developed markets (DM) and Emerging Markets (EM). Obviously, there are two ways this disconnect can be rectified: markets can correct and play "catch down" with economic fundamentals, or the market trade sideways while fundamentals "catch up". We think the former is more likely.

**Deterioration of US-China Relations** One major risk that the market continues to brush aside is the ongoing deterioration of US-Sino relations. While Phase I of the trade deal is still nominally in place, it will be difficult to meet the milestones set out in this agreement and there is little scope for moving ahead with Phase II. The situation in Hong Kong has definitely deteriorated with Beijing's intention to move ahead with the National Security Law. Hong Kong protests on this matter have not reached the level of participation seen last year in response to the Extradition Bill, possibly because of COVID-19 and social distancing norms and possibly because the political and personal risk to protesters has increased given the nature of the proposed law.

Finally, the most pressing area of US-Sino tensions for market participants is Chinese stocks that are listed as American Depositary Receipts (ADRs). Some of China's largest companies (Alibaba, Baidu, Pingduoduo) have ADR listings. In late May the US Senate passed the Holding Foreign Companies Accountable Act, which prohibits a company from being listed in the US if it has failed to comply with the Public Company Accounting Oversight Board's (PCAOB) audits for three years in a row. This bill is now in the House and is generally seen as a mechanism for the SEC and the Trump Administration to target Chinese ADRs.

ADR listed Chinese companies are acutely aware of this risk and as a result, there has been a surge of ADRs seeking a secondary listing in Hong Kong. Alibaba did so in 2019, and NetEase and JD have followed already. Baidu and others are expected to pursue a similar path. The main beneficiary of this trend is Hong Kong Exchange, a stock that has been in the portfolio since inception in 2015 and is now one of our largest overweights.

One final point on US-China tensions is the extent to which US-China relations may be used as a campaign tool in the US Presidential election. During May, both sides put out ads berating the other over China policies and/or ties with the country. If polls shows that talking tough on China is a vote winner, we can certainly expect increased anti-China rhetoric going into November.

Given the concerns outlined above, we remain underweight Hong Kong as a market and our China portfolio is primarily domestic demand stocks. From a portfolio management point of view, we have transitioned some of our Alibaba holding from the ADR to the Hong Kong listing and expect to transition NetEase and JD overtime as well.

### Key Facts

<b>Listing Date</b>	4 September 2015
<b>NTA (before tax)*</b>	\$1.1231
<b>NTA (after realised tax)<sup>^</sup></b>	\$1.1231
<b>NTA (after tax)**</b>	\$1.1093
<b>Share Price at 31/05/20</b>	0.875
<b>EAI Market Capitalisation</b>	\$115.9 Million
<b>Average Management Fee</b>	0.84%
<b>Performance Fee</b>	15%

\* NTA (before tax) – Includes taxes that have been paid.

<sup>^</sup> NTA (after realised tax) - Includes a provision for tax on realised gains from the Company's Investment Portfolio.

\*\* NTA (after tax) - Includes any tax on unrealised gains and deferred tax.

**Rotation to Value** Another thematic that was prevalent in May was factor rotation from growth to value. As our investors know, Ellerston Asia is a growth fund and we only invest in stocks that meet our growth criteria. This strategy doesn't change to suit different market conditions as we strongly believe that growth, particularly structural growth, is a more sustainable long term strategy for generating both absolute and relative returns.

As mentioned above, the rotation to value did not damage performance in May as we outperformed the benchmark by 1.5% (net). We do note however that many of the high profile, go-to growth stocks in our portfolio were looking stretched both in terms of valuation and technicals. Meituan (up 41% CYTD), JD (up 44% CYTD) and Naver (up 25% CYTD) are in this category and we have trimmed positions and taken profits in these stocks.

On the flip side, there are stocks that meet our growth criteria but have relatively low PE multiples and have significantly lagged the market since the March low. Examples include Baidu (14x 2021 PE) and Ping An (8x 2021 PE). We have initiated/increased positions in these stocks which provides some insurance against a prolonged rotation to value without compromising our dedication to our high growth strategy.

## PERFORMANCE

In May, China was the largest country contributor to alpha while Korea was the largest detractor. Consumer Discretionary and Financials were the largest sector contributors to alpha while Consumer Staples and Materials were the largest detractors. Meituan and JD were the largest single stock contributors to alpha while Anhui Conch was the largest detractor.

As always, if you have any questions regarding any aspect of EAI or the portfolio, please feel free to contact us at [info@ellerstoncapital.com](mailto:info@ellerstoncapital.com). We are hosting an update conference call on June 18 at 10am AEST for Ellerston Asia investors for which you can register [here](#).

Kind regards,

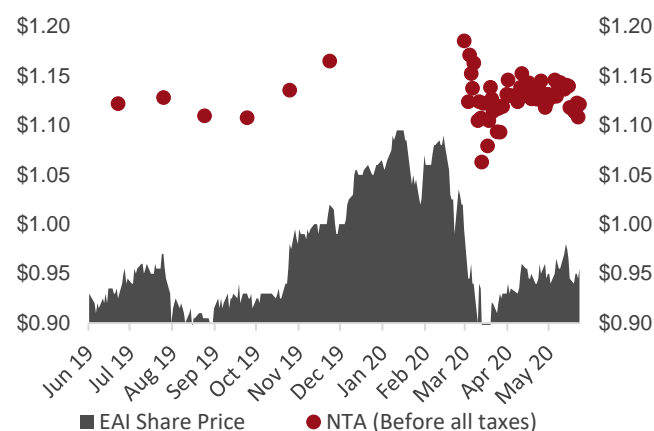
Mary Manning

## PORTFOLIO CHARACTERISTICS

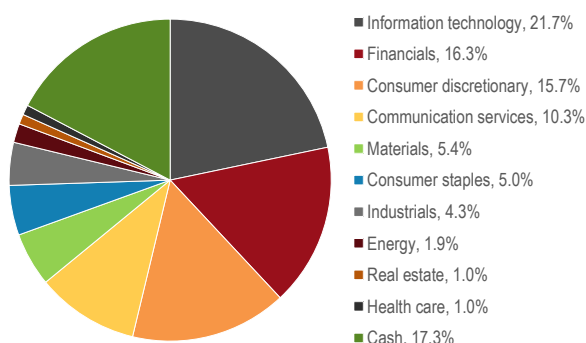
### HOLDINGS

Top 10 holdings	%
Alibaba Group Holding Ltd.	10.0%
Samsung Electronics	8.1%
Tencent Holdings Ltd	7.3%
TSMC	6.9%
Hong Kong Exchanges & Clearing Ltd	5.1%
Ping An Insurance	3.8%
Anhui Conch Cement Company Limited	3.4%
Larsen & Toubro Ltd.	3.2%
China Merchants Bank Co. Ltd.	3.1%
Hindustan Unilever Limited	3.1%

### EAI SHARE PRICE VS NTA

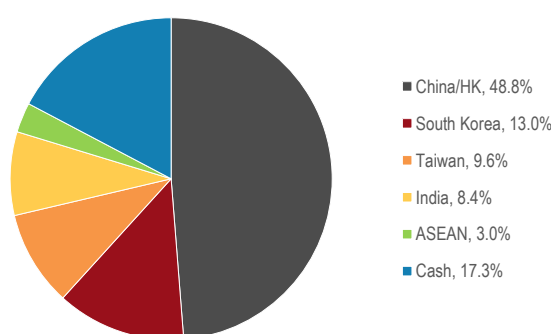


### SECTOR ALLOCATION



Source: Ellerston Capital

### GEOGRAPHIC ALLOCATION



All holding enquiries should be directed to our share registrar, **Link Market Services** on 1300 551 627 or [EAI@linkmarketservices.com.au](mailto:EAI@linkmarketservices.com.au)

Should investors have any questions or queries regarding the company, please contact our **Investor Relations team** on 02 9021 7701 or [info@ellerstoncapital.com](mailto:info@ellerstoncapital.com) or visit us at <https://ellerstoncapital.com/>

#### DISCLAIMER

This report has been prepared for Ellerston Asian Investments Limited by the investment manager Ellerston Capital Limited ABN 34 110 397 674 AFSL No. 283 000. Any information has been prepared for the purpose of providing general information only, without taking account of any particular investor's objectives, financial situation or needs. It is not an offer or invitation for subscription or purchase, or a recommendation of any financial product and is not intended to be relied upon by investors in making an investment decision. Past performance is not a reliable indicator of future performance. To the extent any general financial product advice is provided in this document, it is provided by Ellerston Capital Limited ABN 34 110 397 674 AFSL No. 283 000. An investor, before acting on anything that he or she construes as advice, should consider the appropriateness of such construction and advice having regard to their objectives, financial situation or needs.

#### SYDNEY OFFICE

Level 11, 179 Elizabeth Street,  
Sydney NSW 2000

#### MELBOURNE OFFICE

Level 4, 75-77 Flinders Lane,  
Melbourne VIC, 3000