Neutron Asia Absolute Return Fund

Monthly Newsletter (Aug 2019)

NAV & Returns

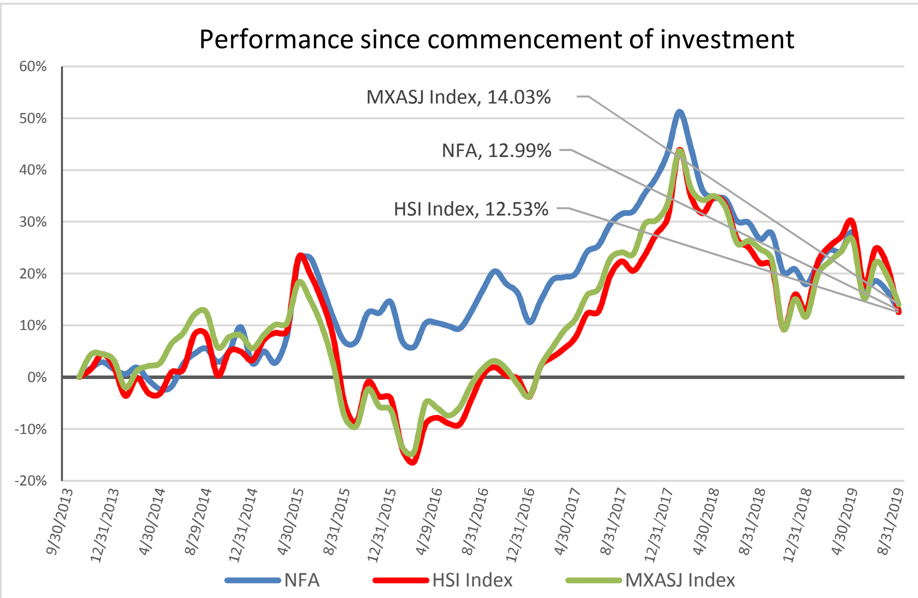
Neutron Fund Limited	NAV/Share (HK$)	MoM	YTD	Since Investment
Neutron Asia Absolute Return Fund (“**NFA**”)	998.8583	↓ -3.08%	↓ -4.19 %	↑ +12.99%

Historical Monthly Returns

MoM	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	YTD
NFA – Net Returns													
2019	+3.41	+2.13	-0.21	+2.82	-8.13	+1.05	-1.72	-3.08					**-4.19**
2018	+5.45	-4.59	-5.68	-1.09	-0.21	-3.13	-0.23	-2.46	+0.90	-5.88	+0.52	-2.45	**-17.78**
2017	+3.86	+3.37	+0.47	+0.56	+3.51	+1.01	+3.23	+1.55	+0.39	+2.62	+2.29	+3.49	**+29.66**
2016	-6.64	-0.96	+4.32	+0.04	-0.53	-0.39	+3.04	+3.73	+2.98	-2.03	-1.55	-4.79	**-3.37**
2015	+2.26	-2.12	+5.02	+13.59	+0.41	-4.31	-5.33	-4.22	+0.12	+5.14	+0.00	+1.83	**+11.49**
2014	-0.88	+1.23	-2.34	-1.79	+0.49	+4.41	+1.98	+0.98	-2.46	+2.00	+4.43	-6.37	**+1.14**
2013										+1.68	+1.24	-1.37	**+1.52**
Hall Park Capital – Gross Returns													
2013	+11.98	+1.76	+2.87	+6.79	+9.71	-7.19	+2.83	-1.79	+2.08				**+31.39**[(1)]
2012	+2.45	+6.61	-4.36	-1.41	-2.89	+1.28	+3.28	+1.30	+0.63	+3.89	+2.11	+4.24	**+16.61**
2011	-3.10	-4.20	+5.57	+0.28	-0.87	-1.56	-1.53	+3.11	+1.29	-3.73	-0.27	-1.10	**-6.11**
2010	-0.72	-0.29	+1.53	+4.44	-2.93	-0.53	+1.81	+3.26	+11.89	+4.23	+0.96	+8.39	**+29.82**
2009	+1.12	+2.88	+3.77	+1.19	+7.92	+1.26	+1.89	-3.40	+0.86	+0.07	+4.22	+6.91	**+28.36**

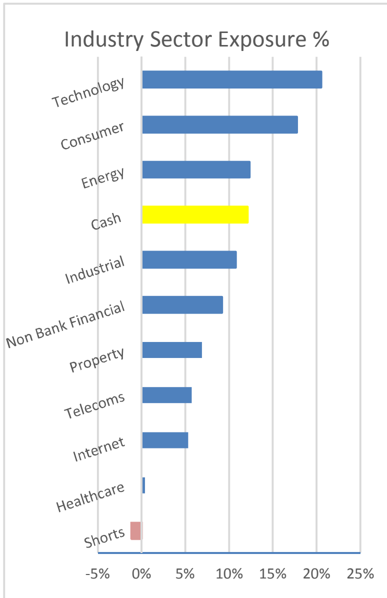
(1) The Hall Park Capital Account is provided for illustrative purposes only, and represents the portfolio manager’s personal account. The account pursued an investment strategy that was substantially similar to NFA with any differences due primarily to portfolio management decisions given the market conditions prevailing during the period. The account was closed after September 2013, with assets transferred to NFA. Additional information can be provided upon request.

Performance



For further info, please visit Bloomberg ticker: BNNEUTA:KY; or website http://neutronasiaabsolute.bricneutron.com/

Industry Sector Holdings



For short position, investments group as shorts.

Fund Information

Investment Objective	The investment objective of Neutron Asia Absolute Return Fund is to focus on but not limited to Asia ex Japan and aims to generate positive returns in all market conditions.		
Investment Style	It is a concentrated portfolio of stock picks employing a fundamental value approach seeking to take advantage of trading opportunities from both the long and the short side.		
Investment Launch Date	2 October 2013	**Domicile**	Cayman Islands
Fund Size	HK$170 million Approx. US$22 million	**Fiscal Year End**	31 December
Administrator & Custodian	DBS Bank Ltd., Hong Kong Branch	**Auditor**	Ernst & Young Limited
Directors	Vincent Leung Patrick Harrigan (Independent) Sean Flynn (Independent)	**Portfolio Manager**	Jonathan Garrick jonathan@bricneutron.com
Management Fee	1.5% p.a.	**Performance Fee**	15% of profits above hurdle
Dealing	Monthly	**Redemption Fee**	1% for early redemption in the first year

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In August, the fund weakened -3.08% net of fees. The NAV is 998.8583 as of August 30th, 2019 to leave the fund down -4.19% year to date.

For the portfolio, the negative impact from the escalating protests in HK coupled with the heightened US-China trade tensions continued to weigh on markets with the Hang Seng Index falling -7.4% in August. The Trump tweet at the start of the month applying a 10% tariff on the remaining $300bn of Chinese imports set the tone. Tensions rose further as the Chinese Renminbi depreciated through the psychological 7.00 threshold and the US labelled China a currency manipulator. Despite the US trying to dial back the tariff threats in the middle of the month, the situation was re-escalated by China a few days later with tit for tat tariff hikes. Once again, this provided a negative impact on the portfolio most heavily felt in the HK/China names. Regarding performance attribution, there was a broad weakness in Hong Kong-listed large caps including internet, technology, non-bank financials and energy. On the positive side, the main contributions were from large-cap tech and our branded consumer companies. On the short side, our index futures provided positive contribution whilst our single stock shorts were mixed.

Despite all the macro headwinds, the consumer both in the US and China remains resilient. This month, one of our premium brand-consumer holdings reported outstanding financial results lifting profits far above of the strong revenue growth. On the call the management said the most compelling opportunities were in China with travel retail and local online channels the main engines for growth. China will be 50% of the industry growth over the next 5 to 10 years and their repeat purchase rate is running at 50 to 60%. Regarding the outlook, the CEO said 'We expect another year of strong net sales growth, margin improvement and a double-digit increase in earnings per share.' In addition, our large-cap tech holding continued to gain on incremental positive data and contract wins. One key theme the fund has been focusing on is corporate restructurings and the crystallisation of value as illustrated in last month's newsletter. This month, ahead of the results announcement, rumours re-circulated around PetroChina (857 HK, Mkt cap U$155bn) and the upcoming pipeline reform. More official and comprehensive details are scheduled by October, but the shape of the deal is emerging. The new company, the China Pipeline Company (CPC) has already been set up with a 7 member board of which PetroChina has 3 positions. PetroChina's share in CPC will be around 40%, which is lower than their share of combined pipeline assets at around 55%. For investors, PetroChina is widely unloved and has long been on national service so expectations have been consistantly low. Many assumed deal would be at the floor price of transferring assets of 1.0 times price/book and this, amongst other factors, has been depressing the share price. However, the most recent industry chatter has stated that the transaction would be done according to 'market-based principles' and the suggested valuation range could be 1.2 to 1.3 x book value. This is notably higher than consensus expectations. If the assets are sold above 1.0x book value, PetroChina shareholders would recognize a gain during the initial transaction and an additional gain if the later dated IPO of the CPC comes at a higher multiple. This should yield a bumper dividend for shareholders assuming the management stick to the 45% dividend payout ratio. In August, PetroChina was trading on less than 0.5x price/book with a third of the book value attributed to its pipeline assets. If the pipeline assets are revalued at 1.2x price/book, the remainder of the company is trading on less than 0.2x price/book. PetroChina has its problems, not least huge gas losses that spiked +140% qoq to Rmb7.9bn (U$1.1bn) in 2Q. That said, the valuation discount seems extreme given the assets, cash flow and reserves. We met the management at a presentation after results and have subsequently added to our position.

For HK/China, we are undoubtedly in a perfect storm of powerful macro headwinds, domestic social unrest and a punishing trade war. In August, China's economic data largely came in weaker than expected. Industrial production fell -0.1% mom, FAI slowed to +5.1% and manufacturing PMI fell to 49.5. More worryingly, retail sales fell -0.8% mom following a +1.9% gain in the previous month with autos leading the weakness. There are also unofficial estimates that the tick up in unemployment is accelerating. Importantly for investors, the government has stepped up their response. There was an interest rate liberalization policy that effectively lowered rates and a further 20 new measures to support consumption. We are encouraged by the increased policy action and expect an acceleration in the months ahead. As we enter the half year corporate reporting season, investor expectations and positioning are low with the likelihood for further earnings cuts. September is traditionally the busiest revision month, yet investors may start to focus more on outlook and valuation with a view on 2020 and relief from the current downward pressure. For longer term investors more and more signals are being triggered. Institutional weightings in emerging markets are the lowest since 2001 and within EM, Asia ex-Japan is the biggest underweight. Valuations on a price to book basis are also trading towards the bottom of the 10-year range. The momentum is still moving lower on several metrics due to the social unrest and uncertainty. That said, as with the example above, the increased uncertainty has created opportunities and extreme price dislocations for those with a longer-term horizon. Our value screening – although old-fashioned – is increasingly filled with larger caps as opposed to the small-mid cap names. Looking at the data, we expect more stock buybacks, corporate actions and even privatisations in the months ahead. Consequently, we remain focused on a fundamental value approach identifying solid companies exhibiting structural growth or a clear value with catalyst.

BRIC NEUTRON 尚金資本

Investment Manager: BRIC Neutron Asset Management Limited
Tel: (852) 2810 5338 **Fax:** (852) 2810 5700
Address: Suite 3601, 36th Floor, Tower 2, Lippo Centre, 89 Queensway, Hong Kong