Prescient China Balanced Fund

Quarterly Commentary

END DECEMBER 2020

> “A synchronised global economic recovery created the tempting belief that equities can only go up”

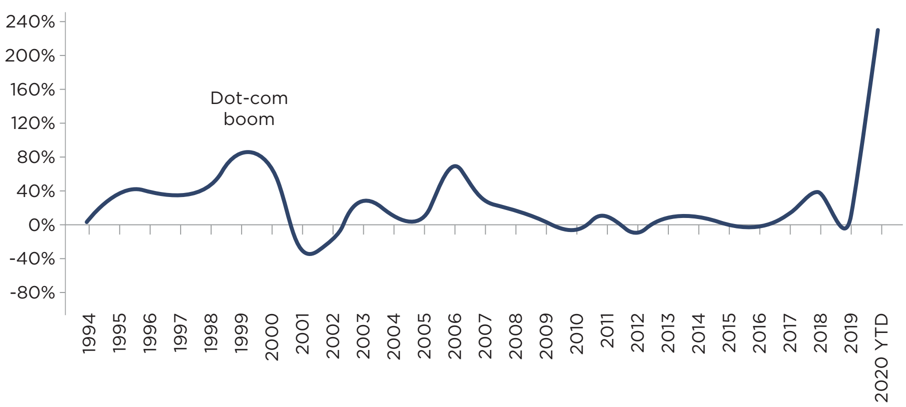
THE BUBBLE PHASE

Despite the tough economic conditions around the globe in 2020, stock markets actually all experienced a phenomenal year. The Chinese stock market as well as the global stock markets continued to rally strongly in Q4 2020, with more and more signs of stock market bubbles forming. The Chinese stock market was up a whopping 38% in US$ for 2020.

A synchronised global economic recovery – as a result of multiple COVID-19 vaccines, improving earnings, zero interest rates as well as aggressive fiscal and monetary stimulus worldwide – created the tempting belief that equities can only go up. “Buying the dip” now appears to be a hugely successful strategy given the environment.

World markets are being driven by a new breed of young tech-savvy retail investors. They’ve driven record growth in stockbroking accounts, adding millions of new investors with no memory of the IT bubble, and ignoring the fundamental principle of investing: PRICE MATTERS. Increasing stock prices also increases wealth, which allows for more leverage and adds to the more irrational buying spirit. From Bitcoin to Tesla, and from CATL to Kweichow Moutai, the resulting gains all look very similar.

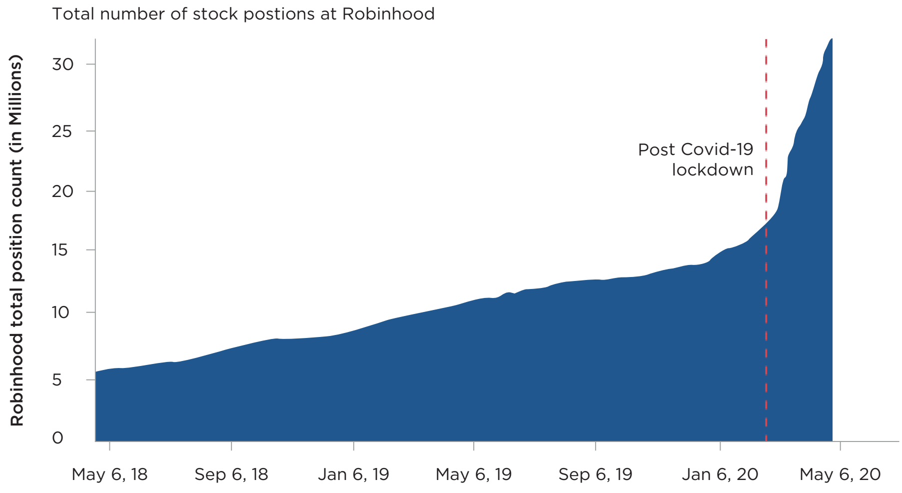
US e-Broker Daily Average Trade (YoY)



Sources: DailyShot.com 14 December 2020

PRESCIENT INVESTMENT MANAGEMENT

Robinhood stock positions spike during coronavirus crisis



Sources: Robinhood, Counterpoint (as at May 2020)

Logic has fallen out of favour, with everyone appearing to believe in the impossible. Valuations are no longer relevant, with market leaders trading at PEs of 50-100 or even more. Even price-to-sales ratios of over 10 have become common, and the phrase "this time is different" is repeated continuously. Retail investors in the US are now showing the exact same behaviour as Chinese retail investors back in 2015. In a world with zero interest rates and a whole new generation of investors who all experienced rapid wealth gains in a few short months, we can't be surprised by the creation of excessive speculative capital.

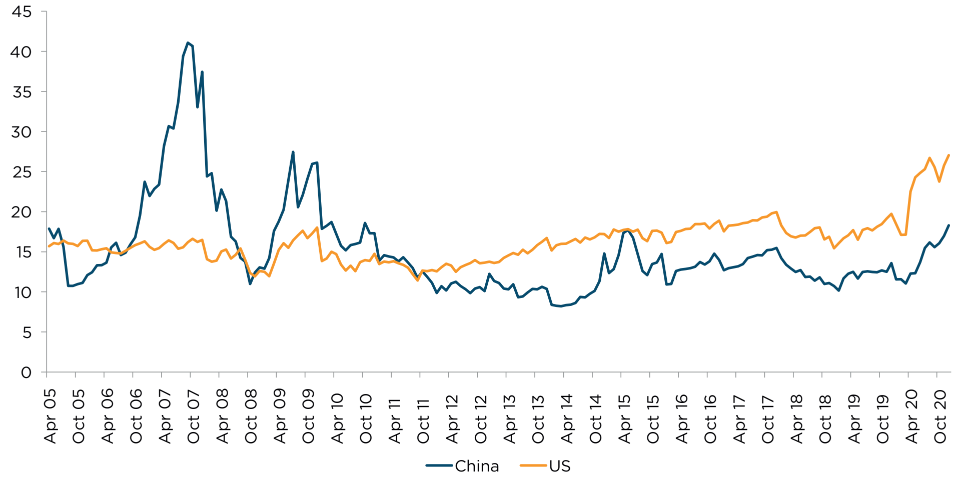
Peak market, at peak valuations, at near peak earnings – this is truly a moment to be fearful. What are our models telling us right now? We'll start cutting equities on our valuation model should the market continue to rally into the new year. Forward PE ratios have risen to 20 and though still reasonable, we believe it's certainly no longer cheap. Unlike the rally of 2015, when the entire market PE ratio was high due to high PE of small-cap stocks, this rally is the opposite. Today's high valuations are driven by market leaders with strong balance sheets and cash flows, trading at PEs of 50 plus, combined with banking stocks with PEs of around six. The result is that opportunities are far fewer than during the 2015 peak.

Prescient China Balanced Fund

Quarterly Commentary

END DECEMBER 2020

1 year forward PE ratios



Sources: Prescient, Bloomberg (as at December 2020)

> Chinese valuations are the highest since we started the Fund in 2013

Chinese valuations are the highest since we started the Fund in 2013 by a material margin. However, it's still at a 50% discount to US valuations. US stocks valuations are at their most expensive levels since the IT bubble.

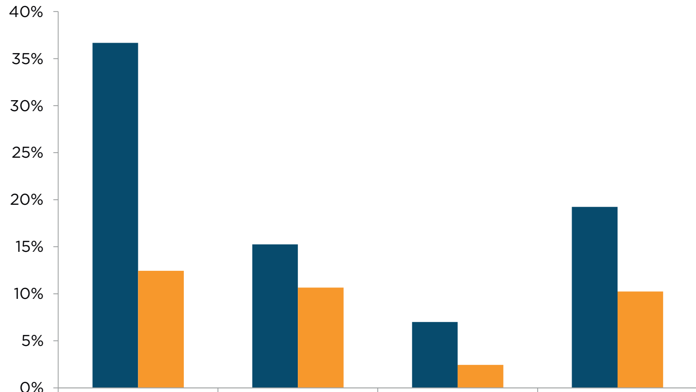
For us, it has become more and more clear that with so much "free" money in the world, the market is going a little crazy. There will be a lot of justifications for the high valuations, but the results will all be the same. As the market gets more extreme, we're going to get more careful. As Warren Buffet said, "Be fearful when others are greedy..."

A stock market bubble can take a while to form. Over time, our clients have asked why we've kept the benchmark for the Prescient China Balanced Fund at inflation plus, rather than a market-based/ more investable benchmark. The reason then, as it is now, is that having a static 65/35 stock/fixed-income type of benchmark inevitably leads to herding to the fixed-benchmark allocations levels. We've always wanted to maintain the flexibility of sitting in bonds or cash should a bubble develop. In current market conditions, we may end up following through on an aggressive switch into bonds and cash.

Fund Performance

In 2020, the Prescient China Balanced Fund, saw a return of 37% for the year in rand terms. Since its inception, the Fund's annualised performance in rands is 19.24%, beating our long-term China CPI + 3 benchmark by 9% per annum. This means our South African investors have earned close to 14% per annum long term real return in rands.[1]

Returns of China Balanced Fund (USD C class) in ZAR - net of fees (1%)



	1 Year	3 Years	5 Years	Since Inception
Prescient China Balanced Fund	36.67%	15.25%	6.99%	19.24%
China CPI + 3	12.44%	10.65%	2.45%	10.24%

Source: Prescient (as at December 2020)

During Q4 2020 the Fund was up 0.5% in South African rands and up 15% in US dollars which brings the returns of the year to around 37% in rands. Over the very long term, even combined with strong alpha generation capabilities, we believe it will be very difficult to continue to deliver returns at this level.

We'd like to urge our clients to lower their real return expectations going forward when buying our funds. Inflation plus 11% to 13% will be very difficult to replicate in future. We've always pointed out that when we started Prescient China funds, valuations were at their cheapest in a decade, and valuations are currently at their most expensive in a decade. We believe a more realistic return target will be around Chinese inflation plus 6% – 8% over the next market cycle.

1 Since inception – maximum rolling 1 year return: 122.4%, minimum rolling 1 year return: -13.5%

PRESCIENT
INVESTMENT MANAGEMENT

“We successfully registered a private fund company in Mainland China”

Business update

At the end of December 2020, we successfully registered a private fund company in Mainland China. As the Chinese financial markets continue to open up, we grabbed the opportunity to establish a Chinese Hedge Fund. We'll soon start to participate in the local Chinese derivative market, allowing us access to more instruments in China, and enabling us to take advantage of more investment opportunities. There are still many regulatory hurdles to cross, but we expect our China Hedge Fund to be launched by the end of Q3 2021. We're very excited about this development: a product that gives investors all the upside in the Chinese markets, with limited to no downside over the cycle. Due to China still being a young market, the strategy will have very strict capacity constraints. We'll be sharing updates with our clients as we get closer to the launch of our hedge fund product.

PRESCIENT
INVESTMENT MANAGEMENT

DISCLAIMER

Prescient Investment Management (Pty) Ltd is an authorised financial services provider (FSP 612). Collective Investment Schemes in Securities (CIS) should be considered as medium to long-term investments. The value may go up as well as down and past performance is not necessarily a guide to future performance. CISs are traded at the ruling price and can engage in scrip lending and borrowing. A schedule of fees, charges and maximum comissions is available on request from the Manager. A CIS may be closed to new investors in order for it to be managed more efficiently in accordance with its mandate. There is no guarantee in respect of capital or returns in a portfolio. Performance has been calculated using net NAV to NAV numbers with income reinvested. The performance for each period shown reflects the return for investors who have been fully invested for that period. Individual investor performance may differ as a result of initial fees, the actual investment date, the date of reinvestments and dividend withholding tax. Full performance calculations are available from the manager on request.

Annualised performance shows longer-term performance rescaled to a one-year period. Annualised performance is the average return per year over the period. Actual annual figures are available to the investor on request. Highest and lowest is returns for any one year over the period since inception have been shown. NAV is the net asset value represents the assets of a Fund less its liabilities.

Prescient Management Company (RF) (Pty) Ltd is registered and approved under the Collective Investment Schemes Control Act (No.45 of 2002). For any additional information such as fund prices, fees, brochures, minimum disclosure documents and application forms, please visit **www.prescient.co.za**

The forecasts are based on reasonable assumptions, are not guaranteed to occur, and are provided for illustrative purposes only.