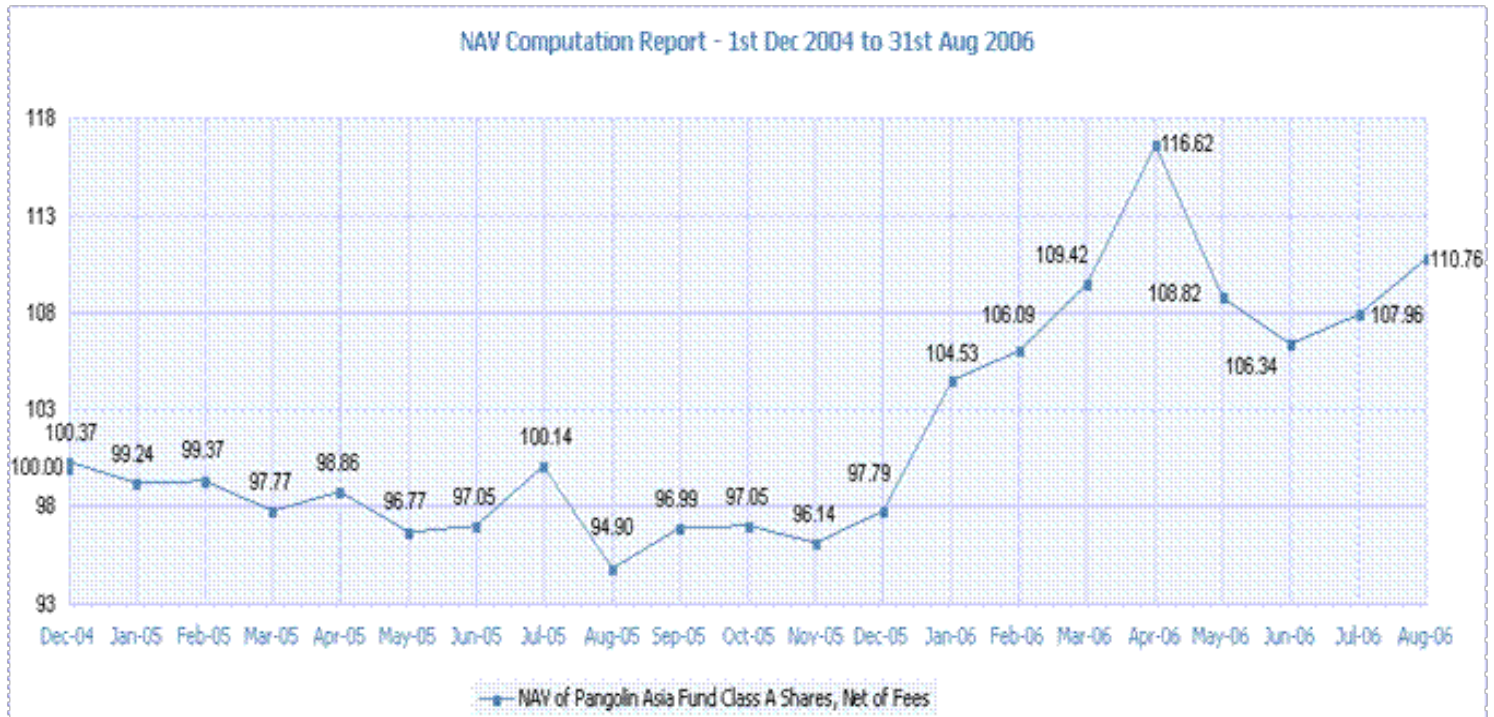




# Pangolin Investment Management

## Pangolin Asia Fund Third Quarter 2006 Report

At 31st of August 2006, the NAV of the Class A shares of Pangolin Asia Fund was US\$110.76 net of all fees and expenses, up from US\$107.96 in July.



At the end of August the fund was approximately 98.5% invested.

## Review

### Thailand

Having just returned from holiday I was struggling to think of anything to write about so I must thank the Thai generals for providing me with some material. The reaction of the financial community to the coup seems to be unanimously bullish, a view I don't share. This acceptance of the military's removal of a democratically elected leader, and the almost total lack of condemnation from world and regional leaders, legitimises the generals' actions and makes it more likely that the armed forces will act similarly again whenever the government is not to their liking.

Okay, so Thaksin was allegedly a bit corrupt (not unique in Asia) but he was not Saddam Hussain (allegedly a despot). The army has partly justified its action by pointing to the political deadlock that has gripped Thailand since the last election. Thaksin can justifiably argue that this was caused by the opposition's spoiling tactics when they realised they had no hope of overturning his massive majority. General Suharto once described democracy as the oppression of the minority by the majority, but in this case we have the urban and middle class minority imposing their will on the rural majority.

Thailand will now have a non-elected caretaker government while a new constitution is written (perhaps with clauses to prevent the rural majority's choice being elected). Non-elected governments tend to be authoritarian (that would be a disaster) or populist (like Thaksin). Free elections under the new constitution are promised within a year and no doubt the generals mean it, unless of course they follow the course of countless dictators before them and decide that maybe the time to step down needs to be delayed a while....



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Meanwhile the much-revered king has stuck his head above the parapet and endorsed the coup, presumably to the annoyance of at least some of his Thaksin-supporting adoring subjects, who might now question his infallibility.

That's my view anyway.

The fund holds one stock in Thailand, LPN Development, which has been seeing strong demand for its Bangkok apartments.

## Singapore

In Singapore (where they don't do politics) the fund has two holdings accounting for about 25% of the NAV. One of them, Boardroom, is subject to a bid from the major shareholders. They are looking to increase their stake rather than take over the company and are not paying above the market price, but all the same it is always encouraging when the insiders show this kind of faith in their companies.

## Malaysia

Malaysian politics are getting messier as a result of some dissatisfaction over the performance of the Prime Minister, Abdullah Badawi. People are worried as normally taboo racial overtones are creeping into the squabbling. Today rioting by Christians over the execution of three of their not-so-nice co-religionists has broken out in some parts of Indonesia, which will hopefully serve as a reminder to Malaysians to where this kind of talk can lead. It might also alert some Westerners to the fact that it is not only Muslims who get upset over religion.

The next UMNO (the dominant Malay party in the ruling coalition) conference might actually produce a few dissenters, which would make a change from the norm. The chances of policies being debated still remain minute.

At an investors' conference I attended this week, a Malaysian semiconductor assembler admitted that with hindsight that they would not have opened their plant in China and that they are now adding new capacity in Malaysia. They are not the first company to encounter operational difficulties in the PRC, but it is rare to hear this kind of admission in a public forum. This is perhaps surprising as this came only a few days after the departing chief of an American chip manufacturer had been highly critical of the bureaucratic impediments to doing business in Penang.

## Indonesia

Given that the President of Indonesia is a former General (democratically elected) one can assume he would know if anyone was planning a coup or not, so we can relax on that front. The market is anticipating falling inflation and interest rates, and the return of the consumer. The fund's holdings in Indonesia are biased towards consumption and should benefit if this trend continues.

Worryingly the pace of reform is still frustratingly slow and the government has capitulated in the face of union opposition to its labour reforms. Things are moving in the right direction (just) but the country is still in dire need of exactly the kind of foreign investor who will be deterred by any serious outbreaks of civil disorder.

## Other

The recent decline in the oil price will have been welcomed by the managements of most of the fund's holdings. One thing I like about France is that they print English newspapers there, so I was able to spot the following quotation from Rex Tillerson, Exxon's new chairman, in the daily Telegraph on August 27<sup>th</sup>:

*"There is a complete disconnection between the fundamentals of supply and demand on crude oil. If you had a supply and demand connection, the price would be somewhere between \$30 and \$40 a barrel."*

He ought to know. I hope he's right.



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Other than a declining oil price (maybe) there doesn't seem to be much of good news around just now. Maybe I am suffering from post-holiday blues but I'd be a bit more cheerful if one of my brokers didn't keep insisting that world markets are going to crash in October.

How he knows this I don't know. I hope he's wrong.

James Hay

22<sup>nd</sup> September 2006

*More details concerning the fund's investments are always available to shareholders in the fund on request.*

*As always, Investors are encouraged to suggest ideas, comment or interrogate as they see fit.*

Further information can be found at [www.pangolinfund.com](http://www.pangolinfund.com).

*If you would rather not receive this email please let us know at [info@pangolinfund.com](mailto:info@pangolinfund.com)*