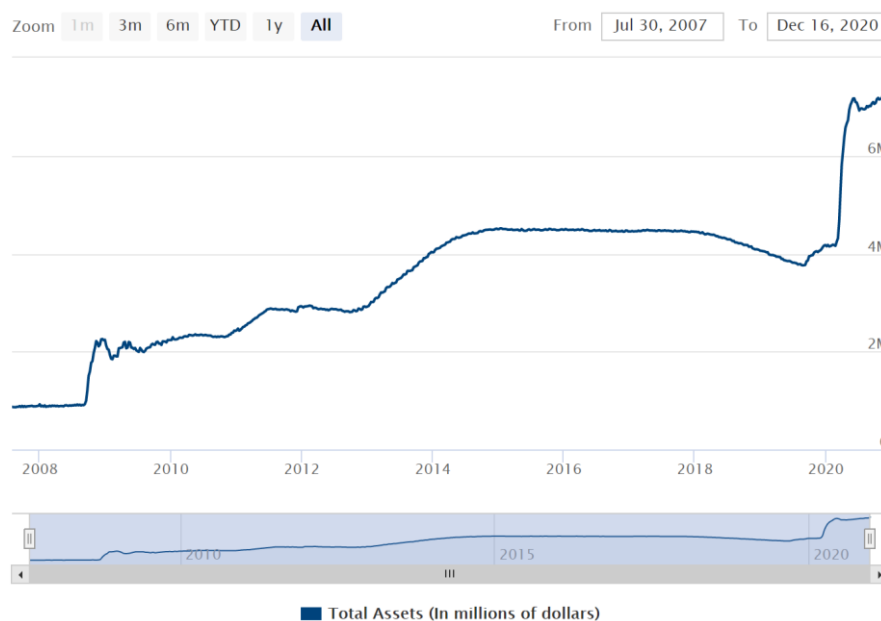


1. Economic and Market Environment

2020 has been one of the most unusual years of my career and with hindsight will probably be remembered as a turning point in our societies, the business world and world economies. The long-forgotten risk of pandemics unfortunately came back to haunt us and affected all aspects of life in 2020, including financial matters. As bad as 2020 turned out to be, it could have been much worse. One positive development this year has been the ability of central banks and world governments to prevent the health crisis becoming a financial and economic crisis. This positive development could have turned out very differently if the Federal Reserve ("FED") and the European Central Bank ("ECB") did not take the appropriate emergency action back in March when credit markets started to freeze, and investors were staring at the abyss. Similarly, world governments put emergency social programs in place to make sure citizens received a minimum income to live.

Unfortunately, this intervention came at a cost and like a house doused in water to extinguish a fire, our economies will require extensive renovation in the coming years. In March, the FED quickly cut its benchmark rates to 0% and embarked on an aggressive expansion of its balance sheet. The ECB took similar measures and European government bond yields are at historic lows. Both central banks have claimed publicly that they do not plan to raise interest rates in the foreseeable future, as long as inflation does not increase substantially. This means that the real return (= after inflation) on cash in bank accounts is likely to stay negative for a while. The European and American governments will also have to work hard to put all the furloughed employees back to work, which will take time and additional funding. We think that in the short and medium term, increasing government debt is unlikely to cause significant problems as depressed yields make borrowing 'free'. Japan has shown that a country can sustain very high government leverage for long periods. For investors, low yields for longer periods should help sustain global equity valuation levels.

FEDERAL RESERVE (FED) BALANCE SHEET



Source: Federal Reserve¹

Another major consequence of this crisis is the increasing pre-eminence of Asia and particularly China. The Chinese government, while starting the pandemic on the wrong foot with local officials trying to hide the problem, eventually took drastic measures and became the first major country to control the disease and restart its economy. Most other Asian economies also performed relatively well, as Taiwan², South Korea and Japan³ escaped relatively unscathed on the health front and their economies performed much better as a result. Six months ago, we wrote about The Economist's 2020 growth forecasts for major economies. Their predictions proved "remarkably" accurate and the real numbers are likely to be very close, with China being the only major economy in the world to deliver growth this year. The US, while facing a deep recession, is doing better than Europe as they enforced lighter lockdowns but are paying a higher price on the health front. All the major economies and especially the eurozone and the USA had to borrow extensively to help with the costs of lockdowns (including broader social programs and increasing healthcare costs) which is likely to have an impact for several years. As a result of a deeper recession and massive borrowing in the Western World, some economists now expect the Chinese economy to overtake the USA within this decade instead of the next one⁴.

	CHINA	USA	EURO AREA	TREETOP VIEW
GDP % change in 2020 vs. 2019	+1.8%	-3.7%	-7.9%	We think the Chinese economy is on a stronger footing than the rest of the world
Current account as % of GDP for 2020	+1.7%	-2.3%	+2.6%	The USA continues to borrow from the rest of the world potentially resulting in pressure on the US dollar
Government budget deficit for 2020	-5.6%	-14.9%	-9.1%	The eurozone and particularly the US borrowed extensively which will eventually require belt tightening
10-year government bond interest rate	3.1%	0.9%	-0.6%	Rates, except in China are at all times low. As long as inflation remains manageable, central banks will try to keep low rates

Source: The Economist

This unprecedented crisis caused tremendous pain but there are also significant achievements worth celebrating. Chief among them is the ability to develop, test and distribute a vaccine in less than twelve months thanks to the massive

¹ https://www.federalreserve.gov/monetarypolicy/bst_recenttrends.htm

² <https://www.economist.com/asia/2020/12/02/covid-19-has-ravaged-economies-all-over-the-world-but-not-taiwan>

³ <https://www.economist.com/asia/2020/10/13/why-the-pandemic-has-affected-britain-and-japan-so-differently>

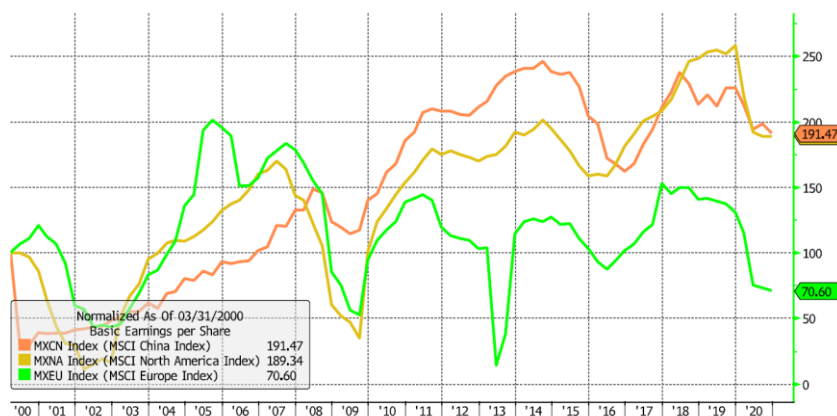
⁴ <https://www.dw.com/en/china-to-overtake-us-as-largest-global-economy-by-2028-report/a-56061395>

progress in genetic science over the last fifteen years. Interestingly, this is where the Western system proved its value with the most effective vaccines created by Western companies thanks to the combined effort of German-Turkish, American and English scientists. The fast development of science in China also played a role with Chinese scientists releasing the genetic code of the virus in January allowing for an unprecedented scientific race. Interestingly, our capitalistic system also had an important role to play. The Pfizer CEO recently explained that the Company board quickly took the decision after emergence of the virus to forgo state aid and allocate USD1bn of the company’s funds to what they believed was the most promising technology⁵. Few politicians and bureaucrats in the world have the capacity to allocate such an enormous amount of capital in such a short amount of time. Even if they did, they probably would not have the ability to choose the right technology. In these difficult times, I think it is important to remember that by investing in the global stock market, we also invest in global progress. The four Companies involved in the development of the vaccine, Moderna, Pfizer, BioNtech and AstraZeneca are all listed and part of various global indexes.

The pandemic also acted as a development accelerator outside healthcare. It proved that remote working and videoconferencing can be used at scale without significant impact on productivity. Again, the tools to make the pandemic more bearable were provided by highly agile American tech companies like Zoom, Microsoft (‘Teams’), Facebook and Amazon, all listed and among the best performers over the last few years. This development is not limited to American tech but is also alive in the rest of the world, particularly in China. E-commerce in China continued its “meteoric rise” led by Alibaba and JD.com and also benefitted more niche business models like VIPShop Holding. Part of the explanation behind the good performance of the global stock markets this year is that crises tend to accelerate societal changes and that the stock markets, especially in recent years, tend to assign more value to companies at the forefront of change like the famous FAANGs⁶.

Given the magnitude of the crisis, earnings per share has been relatively resilient with the exception of Europe. As we can see on the graph below, earnings per share of the MSCI Europe (in green) has been more volatile, has delivered lower growth and delivered worse performance during the pandemic than the American market (in yellow) and the Chinese market (in orange). For European stock investors, we can already speak about two lost decades, as earnings per share is still below 2000’s level. The graph is a good reminder of why at TreeTop we favour a global approach to investing and why it is necessary to look for opportunities beyond our shores.

EARNINGS PER SHARE (EPS) OF MAJOR WORLD INDEXES



Source: Bloomberg

On the valuation front, the world stock markets are not particularly cheap on near-term earnings multiples with the MSCI All Countries World trading on 19x 2021 earnings according to Bloomberg. However, companies continue to

⁵https://news.yahoo.com/pfizer-ceo-refused-taxpayer-money-175100171.html?guccounter=1&guce_referrer=aHR0cHM6Ly93d3cuZ29vZ2xlMnVbS8&guce_referrer_sig=AQAAALDMCByCR_dV3ZR38mDOEYepSOM4wD716KEEBsx9HRCyS7GASPKIN7bCqdp4Oe4BTEH-yG-AE0ng04t0LhPPdPu694cbkXl3qvD47_UdHTkFEBpFL7-P0oYvdkTT8LXqXjCjzY3hascdLyp1D6oJXwUSOD0tAx7SddwxifTlegw

⁶ FAANG: acronym for Facebook, Amazon, Apple, Netflix and Google

progress, and we can expect earnings growth to continue in the next few years⁷. According to Bloomberg, the same MSCI All Countries World trades on 16x 2022 earnings in-line with its long-term average. Earnings growth is the major reason why we believe at Treetop that the global stock market remains the most interesting financial asset for long-term investors. Unlike bonds, which have a very low fixed yield right now, stocks have a yield which continues to grow with the progress in our societies⁷.

Before concluding, I would like to thank our clients who trusted us during these volatile times, and I am delighted that TreeTop has generally been able to deliver good results for them in 2020⁷. I would also like to thank our employees who have quickly adjusted to a new normal and have been able to continue to deliver excellent services to clients. Five years ago, after a few enjoyable meetings with Andrew Dalrymple, I also decided to start a partnership with Aubrey Capital Management from Edinburgh. This partnership has delivered results well-beyond our expectations and I would like to thank them for their excellent work and wish for many more good years ahead. This alliance with Aubrey Capital Management is also an important chapter in TreeTop's transformation from a Company with a limited product range, mostly run by myself, to a Company with a wider offering of both active and passive global equity funds. We will continue to work on finding the best solutions for our clients and we already expect the launch of a few more products next year. The TreeTop team wish you an exciting 2021 and will continue to be available for any questions you might have.

2. Our convictions

2020 ended up being a decent year for our strategy with a significant portion of our investments going up, despite the unusually difficult economic situation. Some of our best performers were companies at the forefront of changes that made life easier for their customers during the pandemic, like **VIPSHOP HOLDING**, a leader in apparel e-commerce in China or **ZOOPLUS**, a leading European online retailer for pet food and accessories. Other companies delivered outstanding results in spite of the pandemic like **HORIZON THERAPEUTICS**, an American bio-technology company which launched a successful new drug treating a debilitating eye disease, or **MAN WAH HOLDINGS**, a well-known brand selling luxury sofas in China.

All these companies, while active in different sectors and geographies, have the common characteristic to be run by agile entrepreneurs with the ability to quickly adjust to new situations. In most cases, the companies are the leader, or one of the leaders, in their sector and have strong balance sheets that enable them to take market share from smaller, less well-capitalized competitors. Another characteristic of our investment strategy is to look for opportunities in sectors where we think the long-term potential is not recognized by the market. Like the entrepreneurs we invest with, we thrive to be flexible depending on the long-term opportunities. For example, we switched our Asian exposure from Japan in the eighties, to South-Korea in the nineties to India and China since 2005. Similarly, we did invest in fossil fuels in the past, as well as automobiles, but have switched our exposure increasingly to biopharma and internet businesses.

As of the end of 2020, our key investments are in Asia, particularly China and India, in convertible bonds in American bio-technology companies and in growth sectors in Europe and the US. In China, we have large investments in **FUFENG** and **DALI FOODS** - both active in the food industry, in **VIPSHOP HOLDING** and **MAN WAH HOLDINGS**, and in software/IT with **CHINASOFT**. We generally tend to keep investments for long periods but sometimes we must act much faster like in the case of **ZHONGSHENG GROUP** or **SHANDONG WEIGAO** where we took most of our profit in less than twelve months, as the underlying investments rerated very quickly. Our strategy in India hasn't performed as well this year, as the country suffered from its deepest economic contraction since independence, and our exposure was mostly related to the domestic economy. We have not made significant changes to our exposure though, as while the pandemic exposed some of the shortcomings of the country, it also showed some of the tremendous progress

⁷ No guarantee of result or performance

achieved by the Indian democracy over the last two decades. One of the key achievements was the ability of the government to send financial aid directly to its citizens thanks to a new biometric identification program. The program helped to avoid a complete economic collapse and the country was even hailed by Bill Gates as one to closely watch for progress⁸. In India, we continue to have significant exposure to housing finance through **INDIABULLS HOUSING FINANCE**, and agri-tech through **UPL LIMITED**. **INDIABULLS HOUSING FINANCE** had to face a terrible financial crisis, but we have hope for next year as the management has done an excellent job navigating a treacherous environment and the situation has now stabilized with fewer competitors. **UPL LIMITED** did better but didn't deliver outstanding stock returns as investors became wary of leverage. As the macro-economic situation stabilizes, we think these Indian companies, run by excellent management teams, are likely to deliver good stock performance given their low valuation levels and good growth prospects.

While we have a much higher exposure to Asia than the global index, we still have large investments in Europe and in the United States. In these regions, we tend to avoid the behemoths like Apple, Facebook or Microsoft but instead go hunting for the underdogs, hoping to find companies that become the leaders of tomorrow. Our key investments are in the consolidation of the equipment rental industry, through **ASHTEAD** and **UNITED RENTALS**, flexible office rental through **IWG** (also known as **REGUS**), fintech through **NORWEGIAN FINANS** and retail modernization with **ZEBRA TECHNOLOGY**. In recent months, we also found several new opportunities in the convertible bonds of American biotechnology companies, like **HORIZON THERAPEUTICS**, **COHERUS BIOSCIENCES** and **HALOZYME THERAPEUTICS**.

In traditional industries like equipment rental, flexible office and finance, we look for Companies addressing a huge market, offering a better product/solution to their clients, eventually resulting in highly profitable business models. In equipment rental, **ASHTEAD** and **UNITED RENTALS** are replacing straight ownership of large equipment with rental, which allows their clients (e.g. infrastructure builders) to have the right piece of equipment at the right place at the right time. Both companies benefit from significant network effects given their national coverage in the US resulting in higher margins than smaller competitors. As a result, **UNITED RENTALS** and **ASHTEAD** have been able to consolidate their industries and should continue to do so in the foreseeable future. **IWG** offers short to medium term office rental to companies all over the world. Like its counterparts in equipment rental, it benefits from a huge network and, like WeWork, is one of the few that can offer a global solution to large businesses. These three businesses delivered very bad stock returns in the first few months of the year and then rerated tremendously as investors started to appreciate the solidity of their business models. A company like **IWG** could eventually benefit from the crisis as management teams from large companies start to appreciate the possibility to spread their workforce geographically and not have everyone in an expensive headquarters in a city centre. While the world has changed, most people will not work from home forever and infrastructure will hopefully still be built requiring large equipment rental.

A success-story this year has been our various investments in the healthcare sector, like **HORIZON THERAPEUTICS** and **SHANDONG WEIGAO**. Their success has little to do with the coronavirus but more with the fact that they have been able to find treatments to various human ailments. As the world population is ageing and we are looking to live in better health for longer, the need for more advanced treatments has exploded in the Western world but also in China and even in India. Reasonable valuations and the existence of interesting convertible bonds has made the risk reward in this sector more palatable to us than in some other growth sectors like software. We have had some churn in this part of the portfolio given the rapid re-rating of some investments. Existing large positions are in **PACIRA BIOSCIENCES**, which has commercialized a new delivery method for anaesthetics, **HALOZYME THERAPEUTICS**, which has also patented a new drug delivery system and is significantly expanding the number of treatments licensed, **COHERUS BIOSCIENCE**, which has a pipeline of biological drugs and finally **JAZZ PHARMACEUTICALS**, which has successfully commercialized a treatment for sleep disorders and has an interesting drugs pipeline in cancer which could provide significant upside.

In conclusion, our strategy has a higher exposure to smaller companies than large indexes, is more concentrated and is more focused on Asia. This has worked well this year and we think it continues to provide an interesting complement to global index tracking and our other active investment strategies.

⁸ <https://www.ndtv.com/india-news/bill-gates-calls-indias-digital-finance-approach-a-global-model-2335995>

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