

About this Review	
Sector reviewed	<b>Global Equities – Regional (China)</b>
Total Funds rated	2
Date of this Sector Review	May 2009
About this Fund	
Fund reviewed	<b>Premium China Fund</b>
Fund Size (\$M)	268 (31 January 2009)
Responsible Entity	Macquarie Investment Management
Fund Commenced	November 2005
Retail Fee (p.a.)	N/A
Wholesale Fee (p.a.)	2.00% + Performance Fee of 15% of Fund performance > MSCI China Free
About the Fund Manager	
Fund Manager	Value Partners Group Limited
Ownership	Listed on HK Stock Exchange, 35% Cheah Cheng Hye, 18% Yeh V-Nee, 15% senior staff
Assets managed in this sector (\$billion)	US\$2.9 (February 2009)
Years managing this asset class	15
Investment Team	
Team size dedicated to this Fund	16
Located	Hong Kong
Portfolio Manager	Chau Yee Man
Number of Analysts/Researchers	11
Turnover/Team Ratio (past 2 yrs)	62%
Investment Process	
Style	Value
Targeted Value Add above Index (p.a.)	Not Targeted
Typical Tracking Error (p.a.)	N/A
Typical Stock Numbers	70 – 110
Currency Approach	Active
Stock bet limits	± 10%
Sector/Industry bet limits	Nil
Country bet limits	100% Greater China
Fund Rating History	
May 2009	Recommended
February 2008	Highly Recommended
November 2005	Highly Recommended

## What this Rating Means

➤ The Recommended rating indicates that Lonsec has conviction that the fund or product can achieve its objectives and, if applicable, outperform peers over an appropriate investment timeframe. The manager or product has a number of competitive advantages in people, process and product design. The investment is a recommended entry point to access this asset class or strategy.

## Using this Fund

- This is General Advice only and should be read in conjunction with the Disclaimer, Disclosure and Warning on the final page
- The Fund is a 'long' only global (Asian) equity fund and as such will generally sit within the growth component of a balanced portfolio. As a regional specific fund, Lonsec considers the Fund suitable for high risk profile investors with a 5+ year investment time horizons
- Lonsec recognises that China is an increasingly important growth market within global equities and there is a broad spectrum of investment opportunity for advisers seeking to give clients exposure to the economy (eg. single country funds, regional funds, emerging markets / BRIC funds or resource stocks). Lonsec believes a broader Asia ex-Japan mandate is an attractive initial mechanism for gaining exposure to the China region and, in theory at least, allows investment managers the flexibility to position the portfolio in favour or against China depending on the relative strength of their conviction in Chinese stocks. However, those clients wishing to gain a deeper exposure to the China theme may prefer a single country approach such as this Fund.
- Lonsec notes that Premium China Funds Management (Premium China) incorporates a degree of active currency management (i.e. beyond A\$ hedging) in its management of the Fund. The Fund's currency hedging strategy is automated based on application of an algorithm (see *currency management section of the report*). Lonsec observes that, historically, adding consistent alpha from currency management is notoriously difficult, even for currency specialists using sophisticated tools and techniques. Accordingly, the Fund should only be considered for those investors (i) seeking a product which combines the active management of both global equities and currency exposures and (ii) who demonstrate sufficient tolerance for the potential additional volatility arising from active currency management.

## Changes since Previous Lonsec Review

- In January 2009, the manager moved from an unhedged currency stance to an active currency strategy. This function is outsourced to Macquarie investment Management Limited (the Responsible Entity of the Fund). This has resulted in a rise in underlying fees (2.00% pa versus 1.88% pa previously). Premium China advises that the rise in fees is attributable to the rising cost of implementing the dynamic hedging strategy (12 basis points).

- Choi Nga Chung, senior fund manager, left Value Partners in late 2008. There has also been a considerable reduction in the number of investment analysts over the year.
- Mark Dickens, Head of Risk Management, left Value Partners in December 2008.
- The manager has created two Deputy CIO roles and promoted Renee Hung and Louis So from the investment team to these positions.
- Like many investment firms within emerging market equities, the manager has witnessed large outflows in Funds Under Management (FUM). The manager's current FUM is approximately a 60% drop from its peak in late 2007. Against this backdrop of weaker profitability, the manager reduced overall staff numbers from 100 to 80 in September 2008. The bulk of these retrenchments were in support positions, though the pull back in research analysts confirms some impact on the investment team.
- Value Partners has broadened its investment range beyond equities since Lonsec's last review, with the release of Chinese property and fixed interest funds. Plans to launch an Exchange Traded Fund (ETF) are well advanced and the manager has stated its intent to broaden its investment capability beyond China with further product development in the next few years.

## Lonsec Opinion of this Fund

### Philosophy / Style

- Value Partners believes that whilst markets will efficiently reflect stock valuations over the long term, inefficiencies exist over the short term that can be profited from via fundamental analysis. The manager's philosophy is based on the Graham-Dodd value approach, tailored to suit Asian markets (i.e. with a greater focus on corporate governance and on cash flow analysis). The Graham-Dodd approach incorporates the concept of 'margin of safety'.
- The manager adopts a bottom up value investment style, with no intended bias based on market capitalisation, geographical location, or sector. That said, historically Value Partners have displayed a bias towards small and mid caps. The Fund is managed in a 'benchmark unaware' fashion, with a focus on absolute returns. Value Partners are often contrarian in approach, with the senior fund managers encouraged to take 'professional risks' (i.e. to take benchmark risk).
- The Fund is focused on the Greater China region, which encapsulates mainland China, Hong Kong and Taiwan. Unlike some other China focused products offered by competitors, the manager is able to access the domestic China 'A' share market which is generally unavailable to foreign investors without approval from Chinese authorities (via the Qualified Foreign Institutional Investor or QFII program). The China 'A' market has a significantly larger stock universe than the China 'B' market, and the 'H' share and red chip markets (which are typically dominated by larger cap stocks). In Lonsec's view, access to the 'A' market is a significant advantage although Lonsec notes that Chinese authorities have increased the number of foreign firms with QFII status over the last year.

### People and Resources

- Chairman and CIO of Value Partners is Cheng Hye Cheah, who is highly regarded within the Greater China region, and in Lonsec's opinion is a well experienced and high calibre investment professional.
- Cheah remains actively involved in the day-to-day stock research and in Lonsec's opinion is integral in influencing the firm's macro views which will have a bearing on portfolio composition. By way of illustration, energy is one of the major current themes of the portfolio, and in particular renewable energy companies deemed to benefit from government aims of reducing pollution and diversifying energy sources. Cheah has been a strong proponent of the theme and his research led the firm to BYD, a company specialising in electric batteries for automobiles. The company is now one of the fund's top 10 holdings and the stock has appreciated from around HK\$12 to over HK\$25 currently. Cheah's pivotal role in this approach is further entrenched by his control in ratifying or rejecting the buy and sell decisions of the senior fund managers.
- Given this, Lonsec considers **key person risk** in Cheah to be high, as he has been critical in the development of the investment process and team. However, this risk is substantially mitigated by the ownership structure (whereby Cheah owns approximately 35% of Value Partners), as well as Cheah's significant co-investment in the Value Partners' Funds.
- Related to this aspect, Lonsec notes that the manager has recently created two co-CIO positions and promoted two senior fund managers to those roles, being Renee Hung and Louis So who joined Value Partners in the 1990s as graduates. Cheah has stated publicly that eventually one of these candidates is likely to become CIO and he will relinquish his investment responsibilities to focus solely on the Chairman's role. Lonsec believes that succession planning is a critical issue for boutiques or modest sized investment teams. This team development is a positive signal and possibly a response to the Chairman's additional non-investment responsibilities following the firm's public listing in 2007. Nevertheless, Cheah's involvement in the Fund is an aspect of ongoing interest to Lonsec.
- In previous reports Lonsec has noted that "*pleasingly Cheah is 'insulated' from non-investment functions, which allows him to focus almost solely on the investment side*". We have less conviction that this continues to be the case. Furthermore, Lonsec believes his efforts to increase the revenue streams for the firm by launching other capabilities (property, fixed income and ETFs) may be a distraction to his investment responsibilities and the team's unified focus. The manager's ambition to grow the business is understandable and no doubt will appease the interests of external shareholders, but in Lonsec's view this aspect must be managed carefully to avoid damaging the existing core equities capability. Lonsec notes that Cheah continues to be assisted by a business team including CEO Franco Ngan in the application of the strategic business objectives.
- The senior fund manager directly responsible for this Fund is Yee-Man Chau. Chau joined Value Partners in 2005. Prior to Value Partners, Chau was a Senior Investment Manager at Credit Agricole Asset Management and also

spent time at hedge fund manager Sofaer Global Research. Lonsec has met with Chau, most recently in April 2009, and believes that she is a quality and competent investor.

➤ There has been considerable change to the investment team in the past year, largely centred on the analyst ranks. The manager's growth in FUM triggered the hiring of additional analyst resources in 2007. With the subsequent market downturn, the manager has reduced the analyst resource. The manager currently has 4 analysts versus 12 at the time of last review, though within this pool 2 analysts were promoted and retained to the position of assistant fund manager (meaning a net loss of 6 analysts). In addition, one senior fund manager departed with Choi Nga Chung resigning from the firm in November 2008. There are no plans to replace Choi with other team members assuming his stock research and 'cluster' (explained below) responsibilities.

➤ Lonsec believes the manager is adequately resourced for this Fund, but its high level of team turnover over the past two years relative to peers could be a sign of some instability. Lonsec recognises that historically there has been a degree of analyst turnover at Value Partners given its unique culture and investment approach, but this past year is on an unprecedented scale. While Lonsec takes comfort that the majority of the senior team remain engaged with the Fund and acknowledge the solid depth of experience in the senior ranks, team stability is an area of ongoing interest with this strategy.

➤ Overall, Lonsec considers alignment of interests between the investment team and investors to be reasonably high through significant staff ownership of the company, a modest level of co-investment in the fund and the existence of a performance fee.

### Research and Portfolio Construction

➤ Lonsec considers Value Partners investment process to be well developed, though appears less transparent and formally structured than the average manager within the Lonsec Asian equities or emerging markets universe. The manager organises its research along a team wide generalist approach, with research overseen by a 'cluster matrix' that somewhat blurs reporting lines. The fund managers and analysts act as generalists and serve multiple clusters. While Lonsec considers the team structure at Value Partners to be sound, it is highly differentiated, and a greater definition of sector responsibilities amongst the investment team (both portfolio managers and analysts) may serve to enhance the research effort.

➤ Despite this structural observation, Lonsec believes the quality and rigour of the manager's bottom up active company research process remains impressive and stable. The manager adopts an 'audit' type approach, which Lonsec considers sound given the limited transparency and corporate governance issues that are prevalent within the region.

### Risk Management

➤ The manager takes a benchmark unaware approach and accordingly, the risk constraints of the fund are sufficiently broad to allow the portfolio management team flexibility to

position the portfolio in line with the team's views. As a predominately bottom up, stock selection driven manager, not surprisingly, stock selection is the major risk component in the portfolio. In the stock research process, aspects of risk management are more formally engaged such as the requirement to meet company management and consider issues in corporate governance. The manager also introduced *Risk Metrics* to enhance its portfolio risk management monitoring in 2008.

### Performance

➤ The Fund targets long term capital growth aiming to generate net returns exceeding the MSCI China Free Index over a three to five year period (before changes in exchange rates). The Fund is denominated in Australian dollars, while the Index is calculated in Hong Kong dollars. The Fund does not have a Tracking Error target (or constraint), and as such advisers should note that returns may differ significantly from that produced by both the index and 'benchmark aware' Greater China funds. The Fund has delivered a return of -14.7% over the year to 31 March 2009, which is in line with the MSCI China Index (unhedged) which also returned -14.7% over the same period.

➤ Lonsec prefers to measure performance over a longer time frame, at least three years, and this Fund has recently met this milestone. Over the three years to March 2009, the Fund has delivered 2.4% pa, underperforming the MSCI China Index return of 8.6% pa. The performance record must be considered within the context of this manager's investment style. The Fund's relative underperformance has occurred within a period of extraordinary growth within the Chinese market, particularly in the earlier segment of the Fund's availability. In 2007 the MSCI China A Index (reflecting stocks listed on the Shanghai and Shenzhen A markets) returned 158% (in local currency terms). Value Partners' investment style espouses a bias towards 'quality' and 'value' (refer 'Investment Style/Philosophy') and the manager found the market climate unsupportive over 2007. Accordingly, the Fund has held little exposure to 'A' shares since inception due to stretched valuations. The manager has recently started to find more opportunity in this portion of the market.

➤ 2008 was tumultuous for all managers and perhaps not the best climate in which to judge fundamental active strategies, but theoretically should have been more suited to Value Partners' conservative valuation approach. Perhaps investors could have expected greater rewards than have materialised from this Fund over the past year. However, drawing conclusions on this manager's performance against a benchmark is also complicated by the manager's ability to hold stocks outside China but exposed to the China growth story (eg. 6% of the portfolio in Taiwanese stocks, 2% in Singapore stocks, and 2% in US stocks as at March 2009).

➤ Lonsec believes this Fund is likely to lag strong momentum driven markets, however, may provide some defensive protection when markets correct. Historically, the Fund has tended to perform stronger in 'down' months consistent with the manager's value investment style. While a pleasing characteristic, this is tempered by the Chinese market witnessing more 'up' months over the sample period

assessed, and the muted level of outperformance for this Fund given the correction in Chinese stocks.

➤ The manager's recent improved relative performance suggests the current environment for Chinese equities may hold brighter prospects for the manager's investment approach. Lonsec notes that like most emerging markets, the China share market corrected through much of 2008, though has recently bounced higher and is up 50% from its October 2008 lows. Despite this it remains well below the heights of late 2007. Chinese stocks are trading below their long term average p/e, suggesting good opportunity for this manager to source attractive investment ideas.

### Overall

➤ Lonsec has downgraded the Fund to a 'Recommended' rating at this review. While Lonsec believes the Fund to be an attractive access point to the China market, the manager is undergoing a period of change influencing Lonsec's overall depth of conviction in the strategy. This is not only reflected in elevated turnover in the investment team, admittedly at the less senior levels, but also at the corporate level where the manager's launching of other capabilities must be managed carefully to avoid diluting the key strengths of this offer. While the Fund remains appropriate for those seeking an enhanced exposure to China, those seeking a more diversified exposure may wish to consider a broader Asian equities or emerging markets fund.

## People & Resources

Premium China Funds Management is a Sydney based financial services firm established in 2005, to bring specialist Asian focused funds, particularly China, to the Australian market. Responsibility for the management of the Fund has been outsourced to Hong Kong-based manager, Value Partners. Value Partners was founded in February 1993 by Cheah Cheng Hye and V-Nee Yeh. Value Partners currently employs 80 staff, including investment, marketing, finance, internal audit, and compliance staff. Value Partners listed on the Hong Kong Stock Exchange in November 2007 although ownership of the firm remains primarily with the founders Cheah (35%) and Yeh (18%), and senior staff (15%).

The Value Partners investment team consists of 16 personnel (excluding three dealer resources). However, it is important to note that this experience primarily resides amongst the senior members of the team, including the CIO and the five senior fund managers. The average level of industry experience amongst this group is 12 years.

In total, the team consists of a CIO, two Deputy CIOs, two senior fund managers, four fund managers, two associate fund managers, four analysts, and one research associate. Essentially the difference between a senior fund manager and a fund manager is that fund managers have only limited buy/sell discretion.

A distinguishing characteristic about Value Partners is the approach adopted in relation to the hiring of new investment staff. Essentially Value Partners will generally not employ junior personnel who have previously worked at another fund manager. This is based on the premise that they want to mould new team members into the Value Partners investment 'mindset' and not have to assist them in

'unlearning' what they have learnt at another funds management house (Lonsec observes a similar practice at Aberdeen Asset Management). These junior members are trained within Value Partners (there is a strong focus on in-house training) and will either progress to a more senior role or will leave the manager. To date Value Partners have only once externally recruited a senior member to the investment team, being Portfolio Manager, Yee Man Chau.

Macquarie Investment Management is the Responsible Entity for this Fund. Custody has been outsourced to JP Morgan.

### Team Structure

The investment team is led by Cheah, who has 30 years of industry experience (15 years at Value Partners). Prior to co-founding Value Partners, Cheah was the Head of Morgan Grenfell's Hong Kong equities research department, where he also acted as a proprietary trader.

Cheah sits above the team of fund managers and analysts. That said, while there is great credence paid to the investment authority of the senior members, in practice the team work closely in the investment process to a reasonably flat structure. While certain members of the team may have greater specialisation in specific sectors, there is no formal allocation of sector responsibilities. Rather, team members act as 'generalists', and are arranged loosely in to research clusters.

Each research cluster has an appointed head from the 5 most senior members of the team (including the CIO) and each cluster head has responsibility for directing the work of the underlying fund managers and analysts (as such the analysts are very much 'task orientated' and will serve multiple clusters). Worthy of note is that all members of the investment team undertake stock research. This may include Cheah, who retains a 'hands on' approach including attending a large number of company meetings, though this aspect of his role continues to be balanced with his Chairman responsibilities.

### Turnover

Over the last two years there has been high turnover in the team, though notably it is largely at the analyst level. Much of the growth in the investment team has been in the analyst pool (grew from five analysts in 2006 to be 12 analysts at 2008). During the period January 2007 – January 2009, the manager hired 10 analysts and 10 analysts were retrenched. This growth and scaling back of the investment team has been commensurate with Value Partners' growth in FUM (peaked at US\$7 billion in late 2007 to US\$2.9 billion as at April 2009). The senior team remains largely unaffected, aside from the loss of one senior fund manager in November 2008.

While Lonsec cannot make an assessment of the likelihood of a staff member departing in the future, 'key person risk' means that the rating of the fund manager is more susceptible to downgrade in the event of senior staff departure.

## Remuneration / Alignment of Interests

Variable remuneration paid to members of the investment team is determined at the discretion of Cheah. The variable remuneration pool is calculated as a % of Value Partner's pre-tax profit and the manager has indicated to Lonsec that variable remuneration is an important component of a team member's remuneration. Most members of the investment team co-invest in the Value Partners' funds, and Cheah in particular has a significant co-investment. In addition, the Value Partners company co-invests (> US\$10 million) in the funds. Further enhancing alignment of interests is the ownership structure at Value Partners, as well as performance fee structure in place; the fee applicable on this Fund is 2.00% + 15% of Fund returns in excess of the MSCI China Free Index, with a 'high watermark'.

## Research Approach

### Overview

The Value Partners research process seeks to identify stocks that possess the following three key characteristics, being 'the right business, run by the right people, at the right price'. The research process begins with a screen of the investable universe utilising a series of value based filters. Whilst all stocks are not required to meet certain pre-determined parameters, the manager's general definition of value includes stocks that possess the following characteristics: PE<10, PBR<2, Div>4%, ROE>10%, strong cash flow and strong balance sheet.

Stocks that pass the preliminary screens are then subject to a detailed analysis that incorporates both qualitative and quantitative evaluations. The output of this process generally results in a stock being categorised into one of three 'buckets' being, 'undervalued', 'fair-valued' or 'overvalued'. Value Partners tend to buy stocks regarded as undervalued and sell stocks considered fair-valued. Multiple valuation models are permitted, with method selection driven primarily by the analyst's assessment of the nature of the company. All valuation models are proprietary with external broker research generally not utilised.

### Screening of Stocks

The Fund's investable universe includes all stocks currently listed on the Greater China stock exchanges (being Taiwan, Hong Kong and China), which collectively account for more than 2,000 companies. The initial screening process aims to reduce the investable universe to a more manageable set of opportunities. Stocks are screened using a range of value metrics including, P/E, P/B, ROE, and Dividend Yield. Value Partners utilise Bloomberg data as the basis of the screening process. Lonsec notes that Value Partners do not require stocks to meet certain 'hurdle' rates per-se in order to be considered appropriate for further investigation, but rather utilise the above mentioned filters as the basis of idea generation. To this end, Value Partners are primarily reliant on the insights and experience of the senior portfolio managers to identify a set of possible investment opportunities by regularly screening the universe utilising different forms of scenario analysis.

## Research Focus

Each company identified by these screens is subject to preliminary financial analysis. It is at this point in the process that companies are generally required to meet minimum quantitative requirements concerning capital adequacy, profitability / valuation and forecast yield to warrant further analysis. The minimum requirements set will vary for each company and/or industry sector and are entirely at the discretion of the portfolio manager. Initial company contact is also instigated in order to make a preliminary assessment of management quality. At this stage of the process the manager completes a questionnaire relating to their estimate of the companies' one-to-two year forecasted earnings.

Companies that qualify through the preliminary process are then subject to detailed analysis. While the format or emphasis of the detailed stock review is at the discretion of the individual portfolio manager, it generally encompasses both qualitative (Porter SWOT type analysis) and quantitative (financial modelling) evaluations. Although a variety of valuation tools are used within the quantitative modelling process, the primary focus is on identifying a company's earnings potential over the next one or two years.

Value Partners adopts an 'audit' type approach to researching stocks with approximately 70% of an analyst's time spent on the ground meeting with company management (with approximately 1000 company meetings per annum) and with relevant industry participants including suppliers, customers, industry experts, competitors and government authorities (where appropriate). There is a strong focus on understanding the business and in some instances new investment opportunities may take up to two months to completely evaluate.

Aside from the initial screening process (which involves the use of Bloomberg data), Value Partners are predominantly reliant on internally generated research when evaluating companies. Whilst Value Partners may utilise external broker research as a cross-check, it is not relied on for investment decision making, and in some instances is used for identifying contrarian investment opportunities.

Once a company is considered as investment grade it is added to the Value Partners' buy list and a price limit is set. Value partners do incorporate peer reviews into the investment process, however, this primarily serves as a sounding board, with the portfolio manager responsible for making the final decision on a stock. That said, it is important to note that Cheah has a veto power over the portfolio manager investment decisions.

### Valuation approach

Value Partners generally utilise one to two year forecasted data when evaluating stocks. Lonsec considers this approach to be appropriate given the inherent difficulties associated with forecasting long-term trends in a market that lacks full-transparency. Analysts can select the valuation method they consider most appropriate given the company type, stage of its life cycle and the industry in which it operate. Valuation metrics such as, PE, EV / EBITDA, ROE, ROA, PBR and dividend yield are utilised. In addition, profitability ratios, activity ratios, solvency ratios and liquidity ratios are also commonly utilised. Although the use of different valuation tools between stocks and sectors can

potentially introduce some inconsistency in valuation, this risk is reduced through the close working relationships between the analysts and portfolio managers. All valuation models/tools used are proprietary with external broker research generally not utilised.

## Portfolio Construction

### Overview

Portfolio construction is an intuitive process where the portfolio manager, Chau, attempts to build a portfolio of Value Partners most preferred stocks (i.e. the stocks that are considered most attractive based on the qualitative and quantitative research undertaken) whilst taking into account liquidity. Important to note is that Chau draws on the pool of research generated by the investment team, and, thus, while she ultimately constructs the portfolio it essentially incorporates a team based approach. The manager will typically 'tier into' positions.

Whilst portfolio construction is a bottom up process, Value Partners' CIO will provide strategic input regarding factors such as cash levels and whether there should be a defensive or aggressive stance in the portfolio. In addition, positions that represent > 7% of a stock's issued capital are required to be approved by the CIO.

The Fund may invest in stocks listed on the Hong Kong, mainland China, or Taiwan exchanges, as well as companies listed on other exchanges that have significant exposure to the Greater China region (i.e. have significant assets or investments in Greater China or generate a large portion of their revenue from the region). Also worthy of note is that the Fund is able to invest in 'Private Chips' (privately owned companies started by mainland Chinese entrepreneurs, the majority of which are incorporated outside of the mainland but conduct the bulk of their operations within the mainland).

Given Value Partners' market presence, it is in some instances able to receive 'block trades' from some companies. This can allow for more efficient execution as well as potentially a lower price. In addition, to reduce downside risk the manager may in some cases arrange a convertible bond with the company they are seeking to invest in. This means Value Partners is able to convert this to equity if the company performs well, but if it does not then Value Partners is able to get back the initial face value of the bond (so long as the company is still in operation).

### Accountability

Whilst there is a team-based approach at the manager, Chau is responsible for the performance of this Fund. That said, the CIO has ultimate 'veto' over the portfolio. Cheah's ownership stake in Value Partners and his co-investment into the Value Partners' funds ensures a strong level of accountability.

### Risk limits

There are a number of risk limits in place in relation to the Fund, these include; a maximum individual stock weight of 10% of total portfolio value (120% of index weight if the stock represents > 10% of the MSCI China Free Index). That said, individual stock weights are generally not expected to represent > 2%-3% of portfolio value (with 5% considered a

significant holding). The maximum holding of any individual company's issued capital is 10% (however this is a per fund limit rather than an aggregate limit across all funds). The maximum allocation to cash is 20% of total fund value. Borrowing or stock lending is not permitted and foreign exchange can only be utilised to execute the settlement of securities (counter parties must have an S&P rating of at least A1 or a Moody's rating of at least P-1). The maximum exposure to China A class shares is 35% of portfolio value, however, the manager has stated that initially this allocation is unlikely to exceed 5%.

### Risk management

Beyond the risk management entailed in the manager's bottom up stock selection approach, Chau is responsible for monitoring any significant tilts in the portfolio. The manager undertakes monthly liquidity testing, which does not involve minimum liquidity levels but rather is taken into account by Chau when considering the cash level necessary within the portfolio.

Macquarie Investment Management monitors compliance with mandate guidelines, which serves as a secondary check to the Value Partners internal compliance function.

## Currency Management

### Currency as an asset class & hedging

Value Partners do not manage currency as a separate asset class and do not engage in cross currency hedging.

Prior to January 2009, the Premium China Fund was managed on a fully unhedged basis. As such, investors were exposed to the impact of currency fluctuations. Subsequent to January 2009, the Fund manager incorporated a degree of active currency hedging into the Fund. According to Premium China, the change was made to reduce the level of volatility of the fund's currency movements.

The Fund's Dynamic Currency Hedging Strategy operated by Macquarie Investment Management Limited allows Macquarie to hedge a varying proportion of the Fund's international exposure (0% to 100%) back to Australian dollars. The hedging strategy is highly automated based on application of an algorithm. As the Australian currency appreciates, the hedge will increase to offset the gains and conversely, as the dollar weakens the hedge can be reduced. The Fund's currency exposure was 59% hedged at 31 March 2009.

**Quantitative Performance Analysis**  
**Annualised after-fee % Returns as at 31 March 2009**

	1 Year		2Years		3 Years		5 Years	
	Fund	Peer Group	Fund	Peer Group	Fund	Peer Group	Fund	Peer Group
Performance (% pa)	-14.7	-	-4.2	-	2.4	-	-	-
Standard Deviation (% pa)	17.7	-	21.2	-	18.8	-	-	-
Excess Returns (% pa)	10.0	-	7.2	-	7.3	-	-	-
Outperformance Ratio (%)	66.7	-	58.3	-	58.3	-	-	-
Worst Drawdown (%)	-24.4	-	-39.2	-	-39.2	-	-	-
Sharpe Ratio	-1.2	-	-0.5	-	-0.2	-	-	-
Information Ratio	1.1	-	0.9	-	1.0	-	-	-
Tracking Error (% pa)	9.3	-	8.4	-	7.7	-	-	-

Fund: Premium China Fund

Benchmark: MSCI AC Far East Free ex Japan Gr Div A\$

*Note:* The Fund manager takes a benchmark unaware approach to portfolio construction, however, does charge a performance fee based on the Fund's performance against the *MSCI China Free index*. The table above references a broader Asian equities benchmark to enable a regional comparison. The performance commentary provided in the opinion section of this report references the MSCI China Free Index.

## Glossary

<b>Absolute Return</b>	'Top line' actual return, after fees
<b>Excess Return</b>	Return in excess of the benchmark return (Alpha)
<b>Standard Deviation</b>	Volatility of monthly Absolute Returns
<b>Tracking Error</b>	Volatility of monthly Excess Returns against the benchmark (the Standard Deviation of monthly Excess Returns)
<b>Sharpe Ratio</b>	Absolute reward for absolute risk taken (outperformance of the risk free return (Bank Bills) / Standard Deviation)
<b>Information Ratio</b>	Relative reward for relative risk taken (Excess Returns / Tracking Error)
<b>Worst Drawdown</b>	The worst cumulative loss ('peak to trough') experienced over the period assessed

## Analyst Disclosure & Certification

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**Date Prepared: May 2009**  
**Senior Analyst: Steve Sweeney**  
**Release Authorised by: Paul Pavlidis**

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