

Premium China Fund

30 Jun 2009

The Premium China Fund (the Fund) offers investors a pure, direct exposure to China's nascent equity markets, via a strategy that favours value investment principles. The underlying manager of the Fund, Value Partners, does not manage the Fund with reference to the benchmark, and can invest the Fund across small to large-cap Hong Kong listed shares, China A shares, China B shares, and Taiwan shares. Zenith considers the Manager's relatively large, highly experienced investment team, and disciplined investment process to be the Fund's key competitive advantages.

The investment team consists of 15 investment professionals who are organised into 5 stock research 'clusters'. The Chief Investment Officer is Cheah Cheng Hye who is also one of the founders of the group and in Zenith's opinion is an exceptional investor within the China region. Since Zenith's previous review, a reduction in headcount has been implemented in response to a steep fall in funds under management. In addition, Jacky Choi (Senior Fund Manager) has retired from the firm. Although clearly disappointing, Zenith believes the team remains the largest and most experienced among the numerous China-focussed investment strategies available to Australian investors. Zenith also takes comfort that the multi-cluster approach spreads decision making responsibility, which in practice ensures the process is not overly reliant on the input of any individual team member.

While Value Partners is a Hong Kong based group, the investment team pride themselves on conducting extensive, on the ground research on Chinese companies in China. In Zenith's view, this is both a critical component and strong feature of the Manager's investment process as it ensures the investment team are able to properly assess company management, operations and market conditions prior to making an investment in a company.

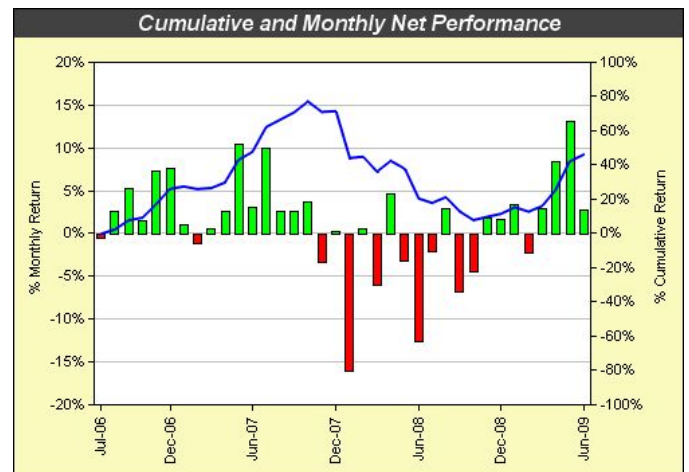
The investment process is built on producing detailed, in-house fundamental research, with a clear focus on identifying undervalued companies generating strong and growing cashflow. The Manager also seeks companies with solid liquidity (trading turnover) so that investments can be readily sold if required. As a result, the portfolio consists of attractively valued, well managed and liquid companies that generate the majority of their revenue and earnings from China. The Manager's investment process pays no attention to the various China stock exchange indices and as a result will provide a materially different return profile to that of the broader China stock market. Given the dominant weightings of a small number of large stocks in the China indices and the fact that the indices have not always reflected the rapid growth of the economy, Zenith strongly favours this investment approach to the region.

In January 2009 an active currency hedging strategy was put in place (the Fund was previously unhedged), and the Fund's base fee was increased by 12 basis points to 2%. The strategy, called Dynamic Currency Hedging (DCH) is implemented by Macquarie Investment Management Limited. DCH uses a systematic model to adjust the Fund's level of hedging (from 0-100%) in response to fluctuations in the Australian Dollar. Although Zenith acknowledges that the strategy has been introduced primarily to reduce the Fund's volatility, we would prefer the Manager offer separate unhedged and DCH versions of the strategy for investors to choose from.

As with the majority of fast developing emerging markets, investors should be aware that the Fund is likely to experience high levels of capital volatility over short term time frames. From this perspective, it is important that investors adopt a long-term (5+ years) investment approach when investing in the Fund.

Overall, Zenith considers the Fund as a highly attractive investment vehicle for those wishing to gain exposure to China, and therefore rates the Fund **HIGHLY RECOMMENDED**.

Key Features	Description
APIR Code	MAQ0441AU
Asset Class	International Shares
Sub-Asset Class	Regional
Investment Style	Value
Benchmark	MSCI China Free Index
Recommended Investment Timeframe	5 + years
Chief Investment Officer	Cheng Hye Cheah
Investment Team Size	15



Performance Analysis

Performance Statistics	3 Yrs (% p.a.)	2 Yrs (% p.a.)	1 Yr (% p.a.)
Performance - Fund	13.39	-0.54	21.34
Performance - Benchmark	15.12	-1.55	8.85

The Premium China Fund aims to outperform its benchmark (MSCI China Free Index) over a 3-5 year period. Since the Fund's inception in October 2005, the Fund has slightly underperformed its benchmark, with performance numbers improving over late 2008 - early 2009. Given the Manager's benchmark-unaware investment style, and ability to invest outside the Fund's benchmark, Zenith believes that investors should anticipate performance to differ substantially from the benchmark over shorter timeframes.

Consistency Analysis

Consistency Statistics	3 Yrs	2 Yrs	1 Yr
History of Monthly Excess Return (%)	52.78	58.33	58.33
History of Monthly Excess Return (Rising Mkts %)	33.33	33.33	44.44
History of Monthly Excess Return (Falling Mkts %)	91.67	100.00	100.00

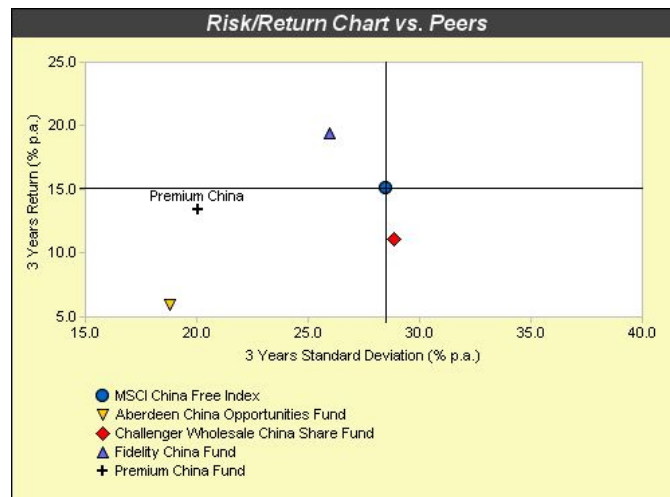
Supporting the view that Value Partners operate a "true to label" value approach is the output from the consistency data analysis which illustrates Value Partner's superior results versus the index in falling markets. Moreover, Zenith takes added comfort in Value Partners' consistency in producing excess returns (particularly in falling markets) in the management of other mandates since the inception of the firm in 1993.

Risk / Return Analysis

Risk / Return Statistics	3 Yrs	2 Yrs	1 Yr
Information Ratio - Fund	-0.11	0.06	0.98
Sharpe Ratio - Fund	0.35	-0.31	0.88
Standard Deviation (% p.a.) - Fund	20.03	22.17	17.98
Tracking Error (% p.a.) - Fund	15.38	17.28	12.78

Standard deviation of performance for this Fund is expected to be high, consistent with the volatility of the Chinese share market. Tracking error is also expected to be high, driven by the benchmark unaware investment process.

The following risk/return chart graphically illustrates the performance of Value Partners relative to some of its competitors.



Investment Personnel

Name	Title	Time with Manager
Cheng Hye Cheah	Chief Investment Officer	16 Yr(s)
Renee Hung	Deputy Chief Investment Officer	11 Yr(s)
Louis So	Deputy Chief Investment Officer	10 Yr(s)
Yee-man Chau	Senior Fund Manager	4 Yr(s)
Fawaz Habel	Senior Fund Manager	4 Mth(s)
Norman Ho	Senior Fund Manager	14 Yr(s)

Organisation:

The Premium China Fund is managed by Sensible Asset Management (SAM) and its sub-investment manager, Value Partners. SAM is a wholly owned subsidiary of Value Partners and was formed in December 2004 with a key purpose of accessing offshore markets and relationships. In essence SAM performs the marketing function and Value Partners is responsible for the management of the underlying portfolio.

Value Partners was established in 1993 by founding partners Cheah Cheng Hye and V-Nee Yeh as a specialist value investment manager focused on the Asia Pacific, with an emphasis on the Greater China region. The company started out with US\$3 million in assets under management and has grown rapidly with approximately US\$4 billion under management as at 30 June 2009.

In November 2007, Value Partners carried out an initial public offering (IPO) through the Stock Exchange of Hong Kong, becoming Hong Kong's first listed asset management firm. The listing primarily occurred because 2 US private equity shareholders of the group were required to realise their investment (having owned a total of approximately 30% of the firm). Importantly, post the listing, key Value Partners investment professionals have retained similar levels of equity ownership in the business. Approximately 51% of the equity in Value Partners is owned by staff with founder Cheah Cheng Hye holding approximately 35% and the 5 senior fund managers having between 2% and 3% equity ownership each. The remainder of staff equity (i.e. less than 5%) is held by

senior non-investment staff including the Chief Executive Officer, the Chief Operation Officer and the Chief Compliance Officer. Zenith believes that staff equity participation is important as it helps to retain and incentivise key staff.

Other shareholders of Value Partners include business co-founder; V-Nee Yeh (approximately 16%) who is no longer actively involved in the funds management business, as well as a large insurance firm (Ping An Insurance, approximately 9%) and 2 private equity firms (Holding Capital and Passport Capital, approximately 5% each). Given that such a large proportion of the business is owned by these groups and Value Partners staff, the free float on the company stock is only approximately 10%.

Although revenues, particularly from performance fees, have fallen significantly, Value Partners has remained profitable, and appears stable with no debt on balance sheet. Zenith notes that the firm, which currently manages 36 funds, intends to further expand its product offering to include, for example passively managed products (i.e. ETFs). In addition, an Asian Bond Fund is also in development, which was originally intended to be launched in December 2008 but has been put on hold indefinitely. The firm has since hired a manager with a background in fixed income, and is looking to further build its capability in this asset class.

Zenith is cautious about the prospect of future product launches, which may detract from the investment team's focus on this Fund. New developments will therefore be monitored closely, to ensure that the Manager has taken steps to maintain the quality and level of resources for its existing strategies, prior to the seeding of any new Fund.

Investment Team:

Value Partners' investment team currently comprises 15 investment professionals, including the Chief Investment Officer (CIO); 2 Deputy CIOs; and 3 Senior Fund Managers. The team is organised into 5 "clusters" with each cluster headed by a senior team member (i.e. CIO, Deputy CIO, or Senior PM), and comprising a further 2 or 3 analysts. The objective of each cluster is to identify approximately 40-50 executable investment opportunities each year. The CIO provides general direction to all clusters and may direct clusters to explore specific research issues if required. Each of the cluster heads has both stock research and portfolio management responsibilities, which in Zenith's view helps to facilitate close collaboration between senior team members and the overall team.

As a result of Value Partners' team structure the Manager tends to adopt more of a generalist approach with no formal sector or geographic responsibilities. The approach has tended to result in senior fund managers and analysts evolving with particular areas of specialisation. This is an unusual team structure that Zenith has not observed previously. While it has worked well for Value Partners to date, we believe that a potential issue could be adequate communication between the clusters. Pleasingly, to combat this issue the CIO steers the overall strategy and ensures collaboration among the clusters. In addition the cluster heads meet weekly to ensure smooth operation of the research process and that there is no overlapping research.

Currently the entire team is based out of Hong Kong which facilitates strong information flow, although, given the intensive company visitation program it is not uncommon for half the

team to be out of the office at any one point in time. The investment team meets formally on a weekly basis and will hold more regular "ad hoc" meetings when the need arises.

Value Partners' CIO, Cheah Cheng Hye, initially commenced his financial career in journalism with the Asian Wall Street Journal and Far East Economic Review, before joining Morgan Grenfell and founding its equities research department (1989 - 1993). A deeply passionate stock picker, he remains dedicated to company visits and undertaking bottom-up research. In Zenith's view, Hye remains a critical component of the Value Partners investment team and while the key person risk surrounding him has diminished as the overall team has grown in stature and experience, we believe he continues to be the key investment professional in the group.

Value Partners places a strong emphasis in ensuring its team follows a consistent investment approach. To this end, the firm has a preference for employing university graduates or analysts with limited "buy side" experience, as Value Partners can more easily mould its employees to the internal "way of thinking". For example, the Firm's 2 Deputy CIO's have made their way through the ranks having joined Value Partners upon completion of academic study (Renee Hung - joined in 1998, Loius So - joined in 1999). The remaining 3 senior fund managers have either funds management or broking experience (Norman Ho - Dao Heng Securities; Yee-man Chau - Credit Agricole Asset Management; Fawaz Habel - R3 Capital Partners). Within the senior ranks of the team an average of over 10 years average industry experience exists, with an average tenure at the manager of approximately 9 years.

Habel is the most recent senior addition to the team, having joined in April 2009 to help build the Firm's fixed income capability. For this reason, although his hire is a positive for the Manager, Zenith considers his day-to-day contribution to this Fund to be limited.

Since its establishment Value Partners has experienced limited turnover at the senior level, however recently a reduction in headcount was implemented in response to a steep fall in funds under management. In addition, since Zenith's previous review of the Fund, Jacky Choi (Senior Fund Manager) has retired from the firm.

Taking the above changes into consideration, in Zenith's view the team remains the largest and most experienced among the numerous China-focussed investment strategies available to Australian investors. The firm continues to successfully develop its team members, as reflected by the several internal promotions that have occurred. Zenith also takes comfort that the multi-cluster approach spreads decision making responsibility, which in practice ensures the process is not overly reliant on the input of any individual team member.

In addition to the investment team, Value Partners has built a large infrastructure of support in the areas of compliance, audit, sales and marketing, business development, portfolio administration, office management and investor relations. In Zenith's opinion, the Manager has successfully transitioned from being a small boutique to a specialist fund manager with strong capabilities across all disciplines. Importantly this growth has allowed investment personnel to remain focused on the investment process. A strong internally driven culture exists within Value Partners with the value orientated approach deeply embedded in the psyche of all members of the investment team, who act more like stakeholders in each investee business rather than shareholders in the company.

We believe this is a healthy approach and "mind set" to adopt when committing investors money to an investment.

The staff bonus structure at Value Partners is based on team performance rather than individual performance with all members of staff participating in the pool to varying degrees (based on level of seniority). Bonuses are paid in cash and are derived from a bonus pool of 25% of the company's pre tax profits.

In summary, we rate the Value Partners investment team highly in terms of level of experience, expertise and the team based approach.

Investment Process

As the Manager's name indicates, Value Partners uses a "value" investment style which is described by the manager as an adaptation of "Graham & Dodd" investing techniques to Asian stock markets. Benjamin Graham and David Dodd are frequently referred to as the "founders of value investing" following the publishing of their book, *Security Analysis*, in 1934. The subsequent publication, *The Intelligent Investor*, was once described by Warren Buffet as the "best investment book ever written".

As a value investor, Value Partners seeks out over-looked, under-valued companies with strong and growing cashflows and sound management. Value Partners' investment philosophy is described as disciplined, contrarian and absolute return focused. The manager believes that Asian Pacific stock markets are dominated by momentum with stocks traded in an inefficient and emotional way. This leads to excellent investment opportunities for disciplined, patient value investors.

In Zenith's opinion, the group's focus and specialisation in Asia and particularly Chinese stock investment is a strong advantage of the group.

Security Selection

Background - China Equity Market:

Prior to describing Value Partners stock selection and portfolio construction approach, it is worth providing a brief explanation of the make up and structure of the Chinese equity markets.

There are currently 4 stock exchanges in the Greater China region including Hong Kong, Shanghai, Shenzhen and Taiwan which can offer foreign investors exposure to the fast growing Mainland Chinese economy. For decades, the Hong Kong Stock Exchange has been the main sharemarket for foreign investors to gain investment exposure to China. However, as Shanghai and Shenzhen gradually open up to foreigners, and a growing number of private entrepreneurs from Mainland China list their companies on the Shanghai and Shenzhen stock exchanges, the investment markets and opportunities are expanding rapidly.

Depending on their place of incorporation and listing, mainland Chinese companies can be classified as "A", "B", "H", and "G" shares, and "Red Chips".

"A" shares represent the largest class of Chinese shares and are traded on the Shanghai or Shenzhen Stock Exchanges, in local currency (the "Renminbi") and are available only to China residents and Qualified Foreign Institutional Investors (QFII). Approximately 1/3rd of A shares listed on the Mainland exchanges are tradable, with the remaining 2/3rd state-owned

and non-tradable. The Fund will invest into A shares through the QFII scheme, and restricts its allocation to A shares to a maximum 35% (generally much lower than this limit) given the illiquid, immature nature of this market. Value Partners currently gain access to "A" shares through broker quotas and intend to apply for a QFII licence of its own, once the minimum US\$5 billion FUM hurdle can be met.

"B" share companies are incorporated in Mainland China and their shares are traded on either the Shanghai (quoted in US dollars) or Shenzhen (quoted in Hong Kong dollars) Stock Exchanges. This share class can be traded by non-residents of the PRC (People's Republic of China) and by residents with appropriate foreign currency dealing accounts. B shares represent the smallest class of Chinese shares.

"H" share companies are incorporated in Mainland China but listed on the Hong Kong Stock Exchange. "H" shares are quoted in Hong Kong dollars and have no resident restrictions. Approximately 50 stocks are dual listed on the "A" and "H" share markets.

"Red chips" are companies incorporated outside of Mainland China (e.g. Bermuda, Cayman Islands, and Hong Kong) with direct or substantial indirect ownership by a PRC state entity. They are traded on the Hong Kong Stock Exchange, are quoted in Hong Kong dollars, and like the "H" shares have no resident ownership restrictions.

"G" shares are corporations that have recently gone public following the Chinese government's decision to allow the 2/3rds of non tradable corporations to float in an attempt to attain higher liquidity, increase corporate governance and improve productivity. However, "G" shares are essentially the same as "A" shares with both being traded on the Shanghai or Shenzhen Stock Exchanges in Renminbi and are available only to China residents and Qualified Foreign Institutional Investors (QFII).

The Fund will invest in Mainland Chinese companies as well as non-Mainland Chinese companies so long as they have significant assets, investment, production activities, trading or other business interests in the Greater China region, or derive a significant part of their revenue from the Greater China region.

Security Selection:

Investment Universe

The Premium China Fund is focused on investing only in Greater China and as such its investable universe comprises approximately 3,600 stocks including Hong Kong listed shares, China A shares, China B shares, and Taiwan shares. The Fund is an "all caps" mandate and as such is likely to have exposure to large, mid-cap and small companies within the portfolio. While the Manager may invest in stocks with a market capitalisation of above US\$200m, Zenith believes that in reality the Fund will rarely invest down to this level given that Value Partners do not want to be the largest shareholder in positions held. This will tend to result in the Fund having a medium to large cap bias. The Manager readily acknowledges that the market capitalisation of the stocks they invest in has increased as a function of their growth in funds under management and liquidity requirements.

Stock Filtering

Value Partners source their stock investment "ideas" from a variety of sources including their initial valuation filter and brokers. As the Manager's focus is on identifying stocks that are under-researched, unknown and undervalued, the vast majority of stock investment ideas are generated internally.

To assist in the identification of stocks meeting these criteria, the Manager utilises a value "screen" which focuses on the key financial measures the Manager deems important. These criteria include:

- Price / Earnings ratio of < 10;
- Price to Book ratio of < 2;
- Dividend Yield of > 4.0%;
- Return on Equity of > 10%;
- Strong cashflows; and
- Strong balance sheet.

The screening process is used as a tool rather than a "black box" which must be strictly followed. The screen is undertaken on the Bloomberg universe of stocks and narrows the universe down to approximately 300 stocks that will be considered to be prospects for portfolio inclusion. The Value Partners approach will often result in it researching "out of favour" stocks, given by nature it tends to be a contrarian style investor.

Valuation

Once a company is identified through the screening process as a potential investment, the investment analyst or senior fund manager will conduct preliminary financial analysis which if deemed attractive will result in initial contact with company management. If the company still appears to be potentially attractive, the analyst / senior fund manager responsible will then conduct detailed financial analysis on the company. The Manager does not rely purely on reported annual financial statements as the accounting profits can sometimes fail to match actual cashflows. In Zenith's view, the greater depth of analysis on the financial performance of the companies is critical in the Chinese market where transparency and compliance is not always of high standard.

While Value Partners focus on the above "value" ratios as the key valuation measures, the Manager will use multiple valuation techniques and adjust depending upon its appropriateness to the stock. The key consideration however, remains free cash flow with working capital requirements, inventory and account receivable / payable all coming under close scrutiny.

Qualitative Research

An essential component of Value Partners company assessment process is meeting with and assessment of company management. This includes an in-depth assessment of their track record, experience and strategy for the business. Value Partners pride themselves on their intensive company visitation program with all members of the investment team travelling extensively within China to meet with companies, their suppliers, customers and competitors. The overall team conducts over 2,000 company visits a year, in addition to meetings conducted by phone. As a disciplined value investor it is a requirement that company management be visited prior to any investment being made. As much as possible, most visits are attended by 2 investment professionals so that there is a cross section of views.

The culmination of the stock research process is the categorisation of stocks into 3 categories as follows:

- Category 1 (undervalued);
- Category 2 (fair valued); and
- Category 3 (overvalued).

Portfolio Construction

The portfolio construction approach is closely linked to the security selection process with the portfolio strongly reflecting the preferred stocks as identified by the investment team. That is, subject to the manager's liquidity requirements, the stocks with the highest weightings in the portfolio will be those deemed as the most attractive from a valuation perspective. The objective of the Fund is to deliver strong absolute returns to investors and as a result, the Manager pays no attention to stock index weights when constructing the portfolio. From this perspective, there are no formal sector or geographical constraints which is consistent with a pure bottom-up stock selection process. The portfolio will range in size from 80 to 120 stocks with the majority of stock weightings being 1% - 2% of the portfolio. The Fund will attempt to hold less than 5% of the issued capital in any single stock, thus not forcing it to report to the market its "substantial" position which could result in it losing any information advantage over the market.

The Manager focuses strongly on stock liquidity (constraints detailed below) which can impact on the weighting of stocks within the portfolio. Portfolio turnover can range widely but is expected to be approximately 100% p.a. although it is often largely driven by the dynamic environment of the Chinese equity markets.

As CIO, Cheah Cheng Hye is ultimately responsible for the Fund; however, day-to-day management of the portfolio rests with senior fund manager, Yee-man Chau and the investment team. The process of building the portfolio is intuitively driven with all funds "tapping" into the same underlying research effort to ensure consistency of approach. The senior fund manager's have ultimate decision making power in the portfolio construction process, including the ability to override recommendations from analysts however this seldom occurs given the team based approach to stock selection.

Since Zenith's previous review of the Fund, the Manager elected in January 2009 to put in place an active currency hedging strategy (the Fund was previously unhedged), and increase the Fund's base fee by 12 basis points to 2%. The strategy, called Dynamic Currency Hedging (DCH) is implemented by Macquarie Investment Management Limited. DCH uses a systematic model to adjust the Fund's level of hedging in response to fluctuations in the Australian Dollar. For example, if the Australian Dollar increases in value, the model will signal an increased level of hedging. The strategy is implemented using forward currency contracts and can fluctuate between 0-100%. The Fund may also combine DCH with a static hedge to keep hedging costs to a minimum.

DCH is most likely to add value in a low volatility, trending market (e.g. a gradually rising Australian Dollar). However, such market conditions are not guaranteed to eventuate, and a highly volatile exchange rate will increase the cost of implementing the strategy. Furthermore, it also runs against the Manager's previous contention that the Fund should be unhedged so as to benefit from a potential upward revaluation in China's currency.

Although we acknowledge that the strategy has been introduced primarily to reduce the Fund's volatility, we would argue that investors already recognise and accept that the

Fund's returns are expected to be volatile. Therefore, Zenith would prefer the Manager offer separate unhedged and DCH versions of the strategy for investors to choose from.

In summary, the portfolio construction approach is a collegiate approach which leverages strongly from the stock research process. In Zenith's opinion, portfolio construction is consistent with the Manager's value approach with small weightings in a relatively high number of undervalued stocks representing an ideal exposure to the China market.

Risk Management

Portfolio Constraints	Description
Security Numbers	80 to 120
Weight - GICS Rel. Index (%)	No restrictions
Weight - Holding Rel. Issued capital (%)	max: 10% typically max. 5%
A Class shares	Max 35%, typically no more than 10%
Market capitalisation (\$)	Typical min: US\$200 million although can invest below
Currency	Actively hedged using Macquaire DCH
Liquidity Test	Able to exit 25% of holding in 1 day, 30% in 3 days, 40% in 4 days
Portfolio Turnover (% p.a.)	Approximately 100%
Cash (%)	Max 20% governed by IMA

While Value Partners formal risk management constraints are not extensive, this is compensated for at a stock research level where thorough research is considered the key risk management measure.

The Fund is bound by a maximum constraint of 10% of the issued capital of any single stock but in practice will seldom hold more than 5% in of a single company's market capitalisation.

Stock liquidity is a key concern of the manager and has been formalised within the portfolio construction and risk management approach via a liquidity test. The liquidity test was introduced to the investment process after Value Partners commissioned a report from PriceWaterhouseCoopers (PWC) in mid 2003. The result is a liquidity test where the Manager must now be able to exit 25% of its portfolio in 1 day, 30% in 3 days and 40% in 4 days, based on average daily volume. Zenith believes this is an important risk management measure as it helps to ensure that the portfolio remains invested in liquid stocks that are able to be sold if required. However, although Zenith considers the current liquidity monitoring procedure to be sound, as the firm's FUM increases, we would expect more advanced liquidity monitoring tools to be incorporated into the process. This would ensure precise and timely analysis can be conducted on both liquidity and capacity risks.

The only other constraints are a requirement that investment in A class shares must be restricted to below 35% of the portfolio, which in practice, is not restrictive given that the manager typically holds less than 10% of the portfolio in A class shares. The Manager is also able to hold up to 20% of the portfolio in cash for times when they are unable to identify undervalued investment opportunities that meet their intensive research criteria. In a dynamic, fast expanding market like the Chinese market, we believe it's unlikely that the manager will not be able to find attractive investment opportunities and therefore expect that the Fund will be relatively fully invested over time.

The manager's funds under management has grown significantly in recent years to approximately US\$4 billion as at 30 June 2009. The Manager intends to review their strategy in relation to funds under management capacity when they reach US\$10 billion. As with most managers, funds under management capacity is largely a function of the size of the overall investible universe which equates to approximately US\$6 trillion (including Hong Kong listed shares, China A shares, China B shares, and Taiwan stock exchanges). As such, Zenith does not consider Value Partners to be capacity constrained at this time, although we do note that the Manager may no longer be able to invest meaningful positions in companies in the small cap segment of the market.

Risks of the Fund

In Zenith's opinion the major risks of the Fund are summarised below:

Regional risk - the Fund invests in the Greater China region and will not have the diversity of a globally diversified portfolio. Furthermore, while potential returns can be higher from emerging markets, this has been historically associated with greater unpredictability and volatility.

Manager / key person risk - the driving force behind Value Partners remains one of its co-founders and current CIO, Cheah Cheng Hye. While he has a further 5 senior investment professionals within the investment team, in Zenith's opinion he remains a critical component. While as a "boutique" Value Partners is more dependent upon a single or fewer number of key investment professional than perhaps its institutional peers, Zenith would argue the risk of losing an individual is less given all are "locked in" via significant equity stakes;

Currency risk - the Fund uses a Dynamic Currency Hedging strategy that allows the Fund's level of hedging to fluctuate between 0-100%. As a result there is a risk that due to unexpected changes in currency markets DCH may detract from rather than enhance the Fund's performance.

Investment style risk - the nature of value investing is that in rising market conditions when stock valuations move to extremes, the style tends to underperform.

Capacity risk - the ability for Value Partners to continue to deliver strong performance in the face of growing funds under management (US\$4 billion as at 30 June 2009) and an increasing number of products (1 initially to 36 currently). Having high levels of funds under management (FUM) presents additional challengers to any fund manager, as high FUM has the potential to hamper a fund manager's ability to trade efficiently particularly in smaller capitalisation stocks.

Applications of the Fund

The Fund provides a high quality investment for those investors seeking to gain exposure to the exciting and potentially high returning Chinese stockmarket. Given that the China stock market indices have not always reflected the rapid growth of the Chinese economy, we believe the Value Partners' absolute return, value investing approach provides an optimal exposure to the China market.

As with most developing markets, spectacular returns can be associated with very high levels of volatility. It is for this reason that we recommend only those investors adopting a long term investment horizon (5+ years) consider an investment in the Fund. In addition, given its specialist, regional nature, we believe an allocation of no more than 10% of an investor's international equities exposure is prudent.

The Fund should be viewed as a capital growth based investment; however the relatively high level of portfolio turnover is likely to result in large components of the Fund's return being delivered via income in the form of realised capital gains. From this perspective, the Fund may suit low marginal tax rate payers such as self managed superannuation funds, where realised gains will not have such an impact on after tax returns.

Fees

Management Fee:

The Manager is remunerated through a base fee and an incentive fee. The base fee is 2% per annum, accrued daily and paid monthly in arrears. The fee has been increased from 1.88%, to incorporate a 0.12% charge for Dynamic Currency Management.

Not included in the base fee is an expense recovery estimate fee of 0.3%.

Performance Fee:

The incentive fee is calculated daily and payable quarterly in arrears and is equal to 15% of the performance in excess of the return of the MSCI China Free Index. The MSCI China Free Index represents non-local investors' opportunities to invest in China's mainland stock markets. While the MSCI China Free Index is dominated by a small number of large stocks and therefore tends not to be representative of the broader China stockmarket, we believe its use as the performance benchmark for the Fund is reasonable.

A buy / sell spread of +/- 0.25% exists in the Fund to cover transaction costs which is an additional charge investors need to be mindful of.

Given the Fund's long-only mandate, Zenith considers the fee structure in place to be very high. Over time, Zenith believes the current fee structure will become more difficult to justify as other Funds Management firms rapidly build their investment capabilities in the Greater China region, which may lead to increasingly competitive alternatives being offered to Australian investors.

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