

RARE Series Emerging Markets Fund

31 Aug 2010

The RARE Series Emerging Markets Fund (the Fund) provides investors with exposure to the growth of infrastructure within emerging markets. The Fund is benchmarked to the Citigroup Global Emerging Market Sovereign Bond Investment Grade USD index + 5% and aims to achieve a return of 15% over a full market cycle. The process and philosophy mirror RARE's Infrastructure Value Fund which is managed by the highly regarded RARE investment team. In Zenith's view, the product offers a pure infrastructure exposure into an ever-growing market.

RARE has a well resourced and highly experienced investment team, consisting of ten investment professionals. All members are based in Sydney and the team is led by Richard Elmslie and Nick Langley. Elmslie has over 20 years of global infrastructure experience. Prior to co-founding RARE in 2006, Elmslie held positions as Head of Power and joint Head of Infrastructure at UBS Investment Bank. Consequently, he possesses a strong knowledge of global infrastructure and its various sub-sectors and is well regarded by Zenith. Nick Langley (Investment Director, Senior Portfolio Manager) has 12 years experience, which includes 4 years with AMP Capital's infrastructure funds management team. The newly appointed Charles Hamieh (Investment Analyst and Portfolio Manager) rounds out the team. Elmslie, Langley and Hamieh form a 3 member investment committee that oversees the portfolio construction process. All analysts have specific stock research responsibilities, with responsibilities divided along sub-sector and regional lines. Zenith has met with the majority of RARE's investment team and have been impressed by the depth, experience and structure of the team. The team's high level of experience ensures strong coverage of the investible universe and the collegiate approach promotes a healthy internal debate regarding investment ideas.

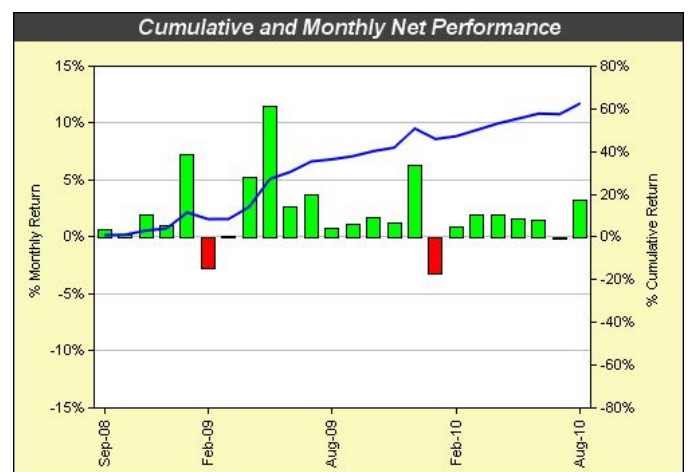
RARE specialises in global listed infrastructure investments. The Manager focuses on specific subsectors of the infrastructure universe specifically, regulated assets and user pays assets such as toll roads. There are three broad components to the RARE investment process: initial screening; fundamental research including financial modelling; and portfolio construction. RARE employs a series of quantitative and qualitative screens (liquidity, gearing, coverage ratios, predictability of cash flows, attractive yield, low volatility of earnings) to reduce its initial investment universe of 350 stocks down to a RARE Emerging Market 150 investment universe. Intensive fundamental research is then employed, culminating in a detailed research report for each company, which includes various sections of qualitative analysis and a discounted cash flow valuation. Portfolio construction is benchmark unaware in nature and portfolio weights are therefore expected to deviate significantly from those of the standard infrastructure sector benchmarks at a stock, sub-sector and regional level. The portfolio will generally contain around 25-60 stocks. In Zenith's view, RARE's portfolio construction process embodies an appropriate blend of fundamental research and Investment Committee discretion. The management of risk within the portfolio is driven by extensive fundamental research at an individual stock level and adherence to portfolio constraints.

RARE applies a 1.33% p.a. management fee with a 10.25% performance fee. The performance fee is based on positive outperformance of the benchmark.

Zenith considers the Fund to be very well structured and managed by a high calibre investment team. We believe there are significant diversification benefits to incorporating an emerging market listed infrastructure fund to an investor's portfolio as it could potentially enhance the risk/return profile of the overall portfolio.

Zenith rates the fund **RECOMMENDED**.

Key Features	Description
APIR Code	TGP0015AU
Asset Class	International Shares
Sub-Asset Class	Infrastructure
Investment Style	Listed Securities
Benchmark	S&P Global Infrastructure Index Hedged A\$
Investment Director, Senior Portfolio Manager	Richard Elmslie
Investment Director, Senior Portfolio Manager	Nick Langley
Portfolio Manager, Investment Analyst	Charles Hamieh
Investment Team Size	10



Performance Analysis

Performance Statistics	2 Yrs (% p.a.)	1 Yr (% p.a.)	6 Mths (%)
Performance - Fund	27.40	19.25	10.46
Performance - Benchmark	-4.34	11.23	2.51

The Fund is benchmarked to the Citigroup Global Emerging Market Sovereign Bond Investment Grade USD Index +5% (unhedged) and aims to deliver a target return of 15% p.a. over a full investment cycle of (5 years to 8 years). The benchmark is generated internally by RARE and reviewed by the investment administration in order to provide a true return comparison for the Fund.

The Fund's track record is not long enough to provide reliable performance data. However, in the short time since its inception, the Fund has generated stellar returns each year and significantly outperformed the benchmark.

Income/Growth Splits

The income/growth split for the last year is:

2009/10: 7.33% (Income); 9.21% (Growth); 16.54%(TR)

Consistency Analysis

Consistency Statistics	2 Yrs	1 Yr
History of Monthly Excess Return (%)	58.33	58.33
History of Monthly Excess Return (Rising Mkts %)	40.00	50.00
History of Monthly Excess Return (Falling Mkts %)	88.89	75.00

The fund has generated a remarkable level of outperformance since inception in September 2008. It has shown its strongest performance in falling markets, and a moderate level of outperformance in rising markets. Whilst the time frame of less than two years does not allow for meaningful conclusions to be drawn, Zenith feels confident in the Fund's ability to outperform in all market conditions over the prescribed investment timeframe.

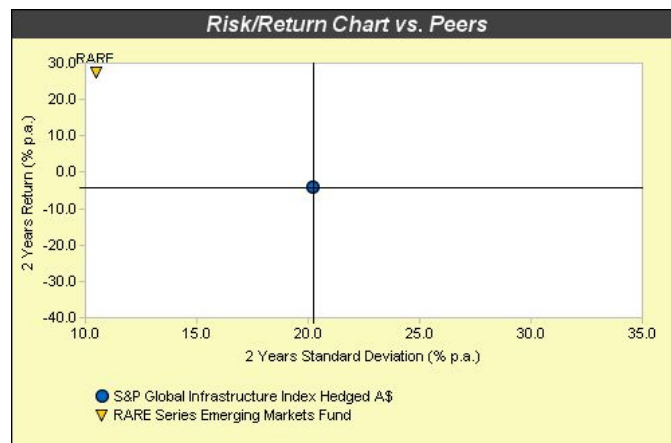
Risk / Return Analysis

Risk / Return Statistics	2 Yrs	1 Yr
Information Ratio - Fund	1.71	0.63
Sharpe Ratio - Fund	2.19	2.08
Standard Deviation (% p.a.) - Fund	10.51	7.23
Tracking Error (% p.a.) - Fund	18.61	12.78

Zenith believes the Fund's two year track record is too short to draw meaningful conclusions.

The risk of the Fund, as measured by standard deviation, is extremely low. As this is a specialised emerging markets fund, it cannot be easily compared to the other infrastructure funds. In absolute terms, this figure represents a comparatively low risk fund. As this is a 'benchmark unaware' fund, returns may diverge from the prescribed benchmark in the future.

The risk/return chart below graphically illustrates the Fund's exceptional performance since inception.



Investment Personnel

Name	Title	Time with Manager
Richard Elmslie	Investment Director, Senior Portfolio Manager	4 Yr(s)
Nick Langley	Investment Director, Senior Portfolio Manager	4 Yr(s)
Charles Hamieh	Portfolio Manager, Investment Analyst	4 Mth(s)
Rod Chisholm	Head of Research	4 Yr(s)
David Maywald	Senior Investment Analyst	4 Yr(s)
Tim Snelgrove	Analyst / Trader	1 Yr(s)
Ben May	Investment Analyst	5 Mth(s)
Shane Hurst	Investment Analyst	3 Mth(s)
Ann Chau	Investment Analyst	3 Mth(s)
Dan Simmonds	Investment Analyst	2 Mth(s)

Organisation

RARE Infrastructure Limited is a boutique investment management company that specialises exclusively in global listed infrastructure in both developed and emerging markets. The RARE business is 62% owned by staff (the majority by Elmslie and Langley) and 38% by ASX-listed Treasury Group. Treasury provide RARE with back office support. This structure enables the investment team to entirely focus on investment management functions which is ideal in Zenith's opinion. RARE has grown significantly since inception in 2006, with approximately AUD\$2.6 billion in funds under management.

Investment Team

RARE has a very well resourced team of 10 investment professionals, with a net gain of two additional analysts since our last review. All members are based in Sydney and are highly experienced; the investment analysts have an average of at least 9 years experience. This high level of experience

ensures strong coverage of the investible universe and a healthy internal debate regarding investment ideas.

The investment team is led by Richard Elmslie and Nick Langley. Elmslie has 20 years of global infrastructure experience. Prior to co-founding RARE in 2006, his roles included Head of Power and joint Head of Infrastructure at UBS Investment Bank. Langley has over 12 years experience in the infrastructure sector, which includes 4 years with AMP Capital's Infrastructure Funds Management Team. Langley also worked alongside Richard Elmslie at UBS. In Zenith's view, Elmslie and Langley are highly regarded investment directors in comparison to their peers and possess extensive knowledge of global infrastructure.

The other portfolio manager for this fund is Charles Hamieh. Charles Hamieh is a new addition to the team and brings with him 13 years of investment experience. Hamieh has previously worked in global infrastructure securities at AMP Capital, Hastings Fund Management and Challenger where he created and ran a dedicated infrastructure fund. Prior to joining RARE, he was a Director and Head of Asia Pacific Research at AMP Brookfield. He has previously worked with Nick Langley at AMP Capital. Zenith views his high level of experience, in particular his previous portfolio management experience, very favourably.

Since Zenith's last review, there have been three staff departures. Co-emerging markets portfolio manager and senior analyst Sarah Shaw has departed, alongside two analysts, Tim Humphries and Jonathon Reyes. RARE had already implemented a global search for additional analysts, so the departures were replaced in tandem with the new appointments. Importantly, the Fund retains two of its three co-portfolio managers. Zenith believes the personnel changes will cause minimal impact to the Fund and that the new appointments will contribute strongly to the team. The new additions are: Charles Hamieh (co-emerging markets portfolio manager and analyst), Ben May, Shane Hurst, Dan Simmonds and Ann Chau. These analysts have an average of more than 10 years investment experience and come from a diverse array of backgrounds, with prior experience from companies such as Deloitte, UBS Global Asset Management and AMP Capital. The analyst team is led by Rod Chisholm, the Head of Research. Chisholm has over 11 years of infrastructure experience gained in equities research and investment banking at HSBC. Whilst Zenith acknowledges that three departures are not ideal, we have met with all senior members of the RARE investment team and have been highly impressed with their industry and valuations experience. It is apparent that the new team have a more collegiate culture which should improve discussion of investment ideas.

All team members (except for Elmslie and Langley) have stock responsibilities divided into both primary and secondary sectors and regions. Portfolio management is driven by a 3 member Investment Committee that is comprised of Elmslie, Langley and Hamieh with investment ideas based on stock ideas from the team.

RARE also have an Investment Advisory Board which includes external appointments. The board consists of Mark Burgess (Managing Director of Treasury Group Limited) and David Bowers (Managing Director of Absolute Strategy Research) as well as Elmslie and Langley. RARE have announced the appointment of a new board member, Jonathon Mirrlees-Black. Mirrlees-Black has over 20 years of experience in the infrastructure sector, including 12 years as a sell side research

analyst and 8 years as a management consultant to global infrastructure companies and sits on the UK Water Regulator's Advisory Panel. Zenith views Mirrlees-Black's appointment favourably, and believes that his experience and relationships with regulators will add another dimension to the investment process.

RARE was established in 2006 and is 62% owned by staff (majority by Elmslie and Langley) and 38% by ASX-listed Treasury Group. The remuneration structure includes a highly competitive base salary with a bonus structure that is linked to the profitability of the business. RARE have now implemented an attractive employee equity plan which further aligns the interest of the team to the overall success of the business. In Zenith's view, RARE's remuneration policy, ownership structure and employee equity scheme should assist with staff retention.

Most non-investment functions are managed by Treasury Group, a highly rated organisation that has successfully implemented the outsourcing of non-investment functions approach with several other boutiques. This structure enables the investment team to focus purely on investment management. The launch of the RARE Series Emerging Markets Fund in September 2008 provides Zenith with a limited track record to assess performance; however the fund has performed extremely well since inception. Zenith is comfortable in RARE's appointment of Hamieh as the Portfolio Manager of the Fund, based on his previous portfolio management experience. Hamieh is well supported by the remaining members of the Investment Committee (Elmslie and Langley) who provide a significant level of experience which is also reflected in the track record of the RARE Infrastructure Value Fund.

Investment Process

RARE specialises in global listed infrastructure investments. The manager focuses on regulated assets such as utilities, and user pays assets like toll roads. They generally limit exposure to the higher risk/return sub-category of competitive assets such as telecommunications and the lower risk/return sub-category of community & social assets.

RARE believes that significant and attractive investment opportunities exist in the listed infrastructure sector and the manager employs a benchmark unaware approach when constructing its portfolio.

Security Selection

There are two broad components to the RARE security selection process:

1. Initial Screening

The starting investible universe includes only those stocks from the global universe of listed securities that meet RARE's definition of regulated assets and user pays assets, as well as a number of hand-picked stocks that display infrastructure characteristics but may be classified in different sectors. At least 50% of the company's EBITDA must be derived from emerging markets. This leaves a remaining universe of approximately 350 stocks.

From here, RARE screens out the majority of stocks with a market capitalisation of less than USD \$100 million and on a number of basic financial parameters including gearing (i.e. Net Debt/Enterprise Value, and EBIT/Interest), cash flow and

valuation measures (Enterprise Value to EBITDA and Price/Earnings Multiples). Small/micro cap stocks below the USD \$100 million threshold may be considered if RARE is comfortable with the liquidity of the stock. The resultant investible universe consists of around 150 stocks.

The remaining 150 stocks are ranked based on the above mentioned financial parameters and the investment team chooses those stocks from each industry subsector that it considers will provide the most attractive opportunities for further qualitative & quantitative analysis. The 'focus list', consisting of 75-100 securities will proceed to the full fundamental research stage.

RARE's initial screening stage ensures that, whilst a broad range of stocks are given preliminary consideration, the final focus list is sufficiently small for the team to conduct intensive analysis on each stock. The financial parameters considered by the team at this stage appear sound and should help the team identify attractive potential investment opportunities.

2. Fundamental Research

The fundamental research process begins with sourcing extensive information on each company and on the market. Primary information sources include: information releases from the company; economic and industry statistics and market data; regulatory or other statutory body reports; and information obtained from company visits. Secondary information sources include: external databases (e.g. Bloomberg); credit analysis and reports; broker analysis; and broker/industry sponsored conferences. Company visits are a critical part of the RARE process, with the investment team undertaking a minimum of 10 international trips per annum of 2 to 3 weeks duration to visit companies (generally 2-3 team members travel per quarter). The travel budget is large, commensurate with the high level of travel. In addition, frequent company contact via telephone calls, conference calls, email and webcast are used as supplements.

RARE uses this information to build an in-depth understanding of the markets, sectors and/or regions in which a company operates. A standard research report is prepared for each company, which includes analysis of various quantitative and qualitative attributes. Specific components of the report include: divisional analysis, meeting notes, peer analysis, SWOT analysis, industry information and valuation.

Detailed financial models are produced and maintained for each company, with the forecast cash flows from these models used to construct discounted cash flow (DCF) valuations. RARE spends considerable effort in determining an appropriate discount rate for each company for use in their DCF models. This is an area where RARE believes it can use its insight to add considerable rigour to the valuation process. It considers both stock specific risks (e.g. quality of management and corporate governance, structural complexity, acquisition strategy, refinancing upside) and risks relative to the company's peer group (maintenance capex, earnings volatility, monopoly characteristics, and political and regulatory risks). These factors are weighted to arrive at the cost of debt and equity which are combined to produce the discount rate. The output of the DCF model is an Internal Rate of Return (IRR) and target entry/exit prices for each company on the focus list, which is used to construct the portfolio.

Following its analysis, RARE may discuss its findings with company management and other industry participants

including competitors and regulators, which can generate new ideas or clarify existing assumptions.

RARE's approach to fundamental research appears comprehensive and very well structured. The high level of experience across the investment team ensures that a significant number of companies can be analysed at an in-depth level.

Portfolio Construction

Portfolio construction is undertaken by a 3 member Investment Committee, which includes Richard Elmslie, Nick Langley and Charles Hamieh. The first consideration is the IRR of each stock on the focus list, where a ranking system is used to set maximum stock limits relative to expected IRRs. Limits are as follows:

- Rank 1: 17%+ IRR = maximum 6% weight
- Rank 2: 15-17% IRR = maximum 5% weight
- Rank 3: 13-15% IRR = maximum 4% weight and
- Rank 4: 11-13% IRR = maximum 3% weight.

The portfolio will consist almost entirely of Rank 1 and 2 stocks but stock weights are permitted to drift via market movement up to an additional 1/3rd of the maximum weights.

The Investment Committee uses this matrix as a guide and determines weightings within these bands. RARE estimates that weightings within the portfolio are 80% based on the stocks IRR and 20% based on Investment Committee's qualitative overlay. The additional factors considered include the overall portfolio allocation across infrastructure sub-sectors and regions, as well as macro-economic inputs. These macro inputs are guided by quarterly broker panels where a panel of 5 brokers are asked for their 3-5 year outlooks which are subsequently fed into the models and used in portfolio decisions. RARE has enhanced its investment process by establishing an Investment Advisory Board (IAB) consisting of Elmslie, Langley, Mark Burgess, David Bowers and new appointee, Jonathon Mirrlees-Black. The RARE IAB was established to analyse macro economic data and assist in forming a viewpoint on the macro economic outlook. This provides many of the underlying macro assumptions and scenarios which feed into the models and the portfolio construction process. The Manager believes approximately 20% of its value-add is derived from top down influences with the remaining 80% coming from bottom-up stock selection.

The portfolio construction process is benchmark unaware and portfolio weights are therefore expected to deviate significantly from those of the standard infrastructure sector benchmarks at a stock, sub-sector and regional level. The portfolio will generally contain around 25-60 stocks, each typically with a minimum 1% weight. Portfolio turnover is expected to average 50% p.a. over the long term.

RARE has a strong focus on liquidity, aiming to ensure that its buy/sell decisions can be executed in a timely manner. The Investment Committee uses the target entry/exit prices determined by the analyst during the valuation to trade the portfolio. Each week an IRR stock ranking list is printed. Changes in the IRR ranking will prompt a stock valuation review. Furthermore, fundamental changes to the business model that will impact on RARE's view on the stock's prospects or a significant market price decline will be examined. When a stock price declines, RARE will reassess the fundamentals of the company to determine if the stock should be sold or the holding increased.

In summary, the portfolio construction process is an intuitive extension of RARE's bottom-up security selection process. In Zenith's view, RARE has achieved an appropriate blend of fundamental research by the analyst team and portfolio manager skill.

Risk Management

Portfolio Constraints	Description
Sector Parameters - Essential Service (%)	20% to 80%
Sector Parameters - Transport (%)	20% to 80%
Sector Parameters - Communications (%)	0% to 20%
Sector Parameters - Community & Social (%)	0% to 20%
Sector Parameters - Cash (%)	0% to 20%
Regional Parameters - Developing (%)	80% to 100%
Regional Parameters - Cash (%)	0% to 20%
Asset Maturity Parameters - Greenfield (%)	0% to 20%
Asset Maturity Parameters - Developing (%)	0% to 30%
Asset Maturity Parameters - Mature (%)	60% to 100%
Security Holdings	25 to 60

Risk management at an individual security and overall portfolio level is an integral part of the RARE process, however, risk relative to benchmark (tracking error risk) is not considered. Zenith is comfortable with RARE's benchmark unaware approach and we believe that RARE has a firm grasp of the stock specific risks and the overall exposures within the portfolio.

While not "hard limits", the guidelines displayed in the table above are placed around individual stock exposures, infrastructure sub-sector exposures, asset maturity exposures and regional exposure. All guidelines are of an absolute nature, not relative to an index. RARE measures exposure to regions and sub-sectors based on the location and sector of the assets the company owns, rather than the stock listing location or GICS classification. Zenith believes this "look through" analysis undertaken by RARE helps provide a more realistic and accurate measure of the risk exposures in the portfolio.

Zenith has a high degree of comfort in RARE's approach to risk management which we consider to be extremely thorough and embedded into all stages of the investment process.

Risks of the Fund

The risks of a fund investing in listed infrastructure, such as the RARE Series Emerging Markets Fund, are comparable to those of global equities funds. The underlying investments of the Fund are companies listed on global stock exchanges and therefore there is exposure to equity market fluctuations. Earnings streams from listed infrastructure companies are potentially more predictable than the broader equities market

as a whole, which has historically resulted in lower performance volatility across the infrastructure sector.

Infrastructure stocks have been negatively impacted by the illiquidity within the global credit market, given the significant amounts of leverage used to fund large infrastructure projects. The markets did not consider the fact that established infrastructure companies generate strong and largely predictable cash flows, and as a result, are easily able to service debt.

While Zenith believes there are inherent defensive characteristics in the listed infrastructure sector, including a modest correlation with the broader equities market and high predictability of earnings, it is still an asset class at the "growth end" of the efficient frontier and should be treated as such when used in an investor's portfolio. Zenith recommends that investors adopt a medium to long-term (5+ years) investment time frame when investing in the Fund.

With RARE's total funds under management (FUM) approximating A\$2.6 billion (as at 30 June 2010), Zenith does not currently consider FUM a hindrance to performance of this Fund.

With regard to key person risk, Zenith considers Elmslie and Langley to be the people responsible for the Investment Committee and if either were to depart it would be considered a material loss for RARE. However, Zenith considers this risk to be mitigated as Elmslie and Langley maintain a significant equity stake in the business. In addition, we acknowledge that the high level of experience across the team significantly reduces the reliance on individual team members. Zenith looks favourably on the recent introduction of an employee equity scheme which will align employee remuneration to the success of the Fund.

Applications of the Fund

Zenith believes there are significant diversification benefits to be gained by adding an Emerging Market listed infrastructure fund to an investor's portfolio as it could have the potential to improve the risk/return profile.

Zenith maintains a long-term view of asset allocation, with global infrastructure being no exception, with an allocation of up to 15% of a portfolio's global equity exposure. The asset class has an ability to generate a 3-4% yield coupled with a growth expectation of 5-6% p.a. in normal market conditions.

Fees

RARE applies a 1.33% p.a. management fee, and a 10.25% performance fee. The performance fee is based on positive outperformance of the benchmark. These fees are slightly higher than the Fund's peers in global developed infrastructure, reflecting the specialised skill set required to manage emerging market investments.

Author: Angela Burmeister
Investment Analyst

Email: angela.burmeister@zenithpartners.com.au

Ph: (03)9642 3320

Fax: (03)9642 3319

DISCLAIMER: This report is prepared exclusively for clients of Zenith Investment Partners (Zenith). The report contains recommendations and advice of a general nature and does not have regard to the particular circumstances or needs of any specific person who may

read it. Each client should assess either personally or with the assistance of a licensed financial adviser whether the Zenith recommendation or advice is appropriate to their situation before making an investment decision. The information contained in the report is believed to be reliable, but its completeness and accuracy is not guaranteed. Opinions expressed may change without notice. Zenith accepts no liability, whether direct or indirect arising from the use of information contained in this report. No part of this document is to be construed as a solicitation to buy or sell any investment. The performance of the investment in this report is not a representation as to future performance or likely return. The material contained in this report is subject to copyright and may not be reproduced without the consent of the copyright owner. Zenith usually receives a fee for assessing the fund manager and product(s) described in this document against accepted criteria considered comprehensive and objective.