

Fairview Emerging Companies Fund

31 Dec 2010

The Fairview Emerging Companies Fund (the Fund), distributed by nabInvest, offers investors a high quality, diversified exposure to Australian small companies, managed by an experienced 3-strong investment team with backgrounds well suited to the small companies market. Zenith believes the Manager's 'core', style neutral, targeted tracking-error approach makes the Fund an appealing alternative to other small cap managers that target higher tracking error and/or favour a particular investment style.

Fairview Equity Partners Pty Ltd (Fairview) was established in August 2008 by Chris Adams, Leigh Cronin, and Michael Glenane as a boutique venture, partnering with nabInvest. Zenith considers Fairview's partnership with nabInvest to be a sound arrangement, as nabInvest's capital contribution and distribution support provides stability for both the Manager and investors, and allows the investment team to focus their efforts on managing the portfolio.

The investment team utilises a collaborative management approach with Adams, Cronin and Glenane co-managing the Fund. Each team member provides equal stock research and decision making input into the process. The team previously had a working relationship at Goldman Sachs JBWere Asset Management (GSJBW) and in Zenith's view, the team's combined experience in small companies is a major strength. In acknowledgement of the team's broad experience across all market sectors, there is no formal allocation of stock and/or sector responsibilities.

The Fund's investment objective is to outperform the S&P/ASX Small Ordinaries Accumulation Index by ~5% p.a. (before management fees) over rolling 5 year periods, within a tracking error range of 5% to 7%. Overall, Zenith believes that Fairview's process appropriately leverages the key strengths of the Portfolio Managers, primarily being their bottom-up stock research skills, extensive company and industry contacts.

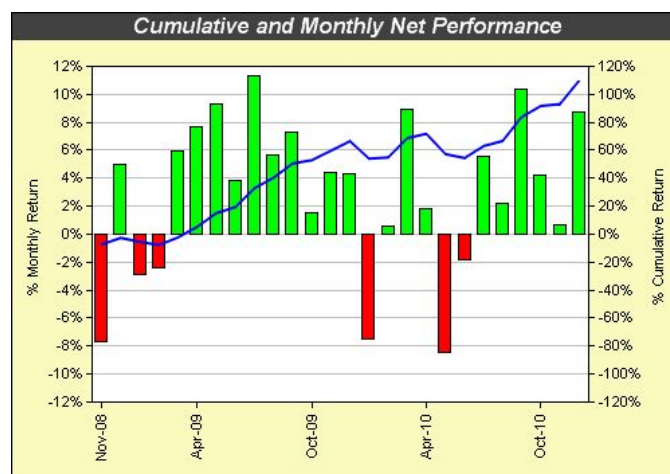
In constructing the portfolio, the Manager aims to add value predominately through stock selection, rather than taking large 'top-down' macroeconomic bets against the benchmark. Stocks selected are those which the team has the highest conviction in, based on 4 key factors (insight, valuation upside, qualitative characteristics and risk). The Fund will generally hold between 25 and 55 stocks in its portfolio (typically around 50 stocks), with portfolio turnover generally within 40-60%p.a.

Fees include a management fee of 1.20%p.a. and a 20.5% performance fee (after fees and expenses) in excess of the S&P/ASX Small Ordinaries Accumulation Index. The performance fee is subject to a high watermark, and is not payable in a period of negative absolute performance. Zenith considers the level of fees overall to be relatively expensive in comparison to its peers.

The Fund is most appropriate for investors seeking to achieve a well blended exposure to Australian Equities small companies. Given the Fund's 'core', style neutral approach bias, the Fund is an attractive option for investors seeking a single fund exposure to Australian small companies.

Zenith rates the Fund RECOMMENDED.

Key Features	Description
APIR Code	ANT0002AU
Asset Class	Australian Shares
Sub-Asset Class	Small Companies
Investment Style	Neutral
Zenith Assigned Benchmark	S&P / ASX Small Ordinaries (Accum)
Tracking error (% p.a.)	5 to 7 (% p.a.)
Recommended Investment Timeframe	5 + years
Portfolio Manager	Chris Adams
Portfolio Manager	Leigh Cronin
Portfolio Manager	Michael Glenane
Investment Team Size	3



Performance Analysis

Performance Statistics		2 Yrs	1 Yr	6 Mths
Performance (% p.a.)	Fund	46.99	26.08	35.92
	Benchmark	33.41	13.04	29.90
	Median	38.48	17.82	27.64

The Fairview Emerging Companies Fund targets ~5% outperformance (before fees) above the S&P/ASX Small Ordinaries Accumulation Index over 5 year rolling periods, within a tracking error range of 5-7%.

Zenith has been encouraged by the Fund's performance since its inception (as at the 30th November 2010, when the review was conducted). The Fund has managed to outperform the benchmark on a consistent basis over this timeframe, and Zenith has confidence the Manager can meet the Fund's objectives over the long-term.

Zenith has previously observed new small cap managers that have delivered impressive numbers by taking advantage of low FUM, and investing in less liquid, lower market cap stocks. Pleasingly, Zenith notes that in Fairview's case this has not occurred, and that since inception the Fund has been managed according to a consistent investment process that is repeatable at the Managers stated capacity constraints.

Income / Growth Analysis (Financial Year)

- **30th June 2010:** Total Return 29.48%, Income Return 6.08%, Growth Return 23.45%.

Consistency Analysis

Consistency Statistics		2 Yrs	1 Yr
Excess Rtn - All Mkts (% of Mths)	Fund	75.00	83.33
	Median	58.33	58.33
Excess Rtn - Rising Mkts (% of Mths)	Fund	76.47	100.00
	Median	52.94	50.00
Excess Rtn - Falling Mkts (% of Mths)	Fund	71.43	50.00
	Median	71.43	75.00

Since inception, the Fund has outperformed the benchmark on a consistent basis, during both rising and falling markets. The Fund has outperformed 75% of the time overall through all market conditions (as at November 2010).

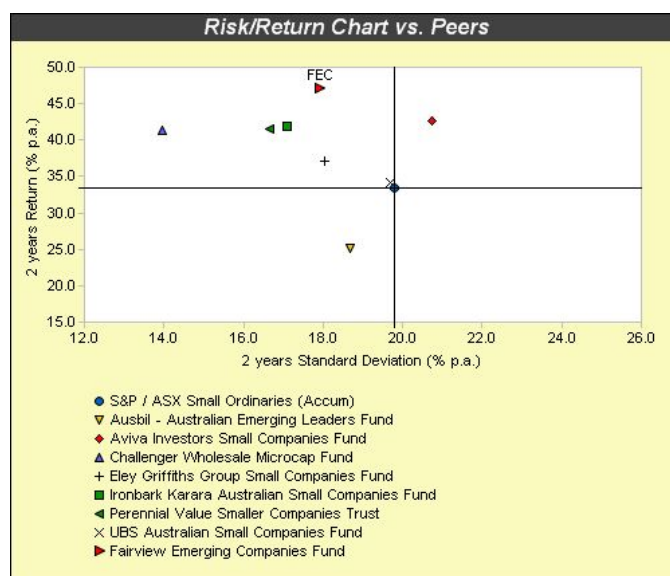
Zenith does however consider the funds return history to be too short to provide any meaningful conclusions.

Zenith believes that Fairview's investment style does not favour an outperformance bias towards either rising or falling markets. Fairview proactively seeks to avoid taking large sector tilts, which are generally kept to within +/- 10% against the index. Furthermore, any bias towards value or growth investment styles is also monitored, and if deemed necessary actively controlled to ensure style bias remains both intentional and within acceptable limits.

Risk / Return Analysis

Risk / Return Statistics		2 Yrs	1 Yr
Information Ratio	Fund	1.87	4.71
	Median	0.85	0.88
Sharpe Ratio	Fund	2.39	1.07
	Median	1.86	0.76
Standard Deviation (% p.a.)	Fund	17.92	20.00
	Median	17.92	17.44
Tracking Error (% p.a.)	Fund	7.27	2.77
	Median	7.67	5.12

Zenith notes that the Fund's performance history is too short to provide any meaningful conclusions. However, we believe that the Fund's performance figures thus far have been strong, whilst managing volatility (as measured by standard deviation) within reasonable levels. Zenith believes the Fund has been managed in a fashion which reflects the risk/return expectations of the strategy and investment process. Tracking error has been slightly higher than the targeted 5-7%, which Zenith attributes to the volatile market conditions during the early stages of the Fund's inception, and over the shorter term history this has significantly dropped.



Investment Personnel

Name	Title	Tenure
Chris Adams	Portfolio Manager	2 Yr(s)
Leigh Cronin	Portfolio Manager	2 Yr(s)
Michael Glenane	Portfolio Manager	2 Yr(s)

Organisation:

Fairview Equity Partners Pty Ltd (Fairview) is a boutique funds management firm that has been established solely for the purposes of this Fund. Founded in August 2008, the firm has 3 founding Executive Directors / Portfolio Managers - Chris Adams, Leigh Cronin, and Michael Glenane, who previously had a working relationship at Goldman Sachs JBWere Asset Management (GSJBW).

Reflecting a common approach among boutiques, Fairview has partnered with nabInvest, the direct investment

management business of the NAB Group. nabInvest committed funding to cover set up costs, along with ongoing working capital for approximately 3 years. nabInvest has been issued a 46% stake in Fairview, with the remaining equity split equally between the 3 Executive Directors (i.e. - 18% each).

nabInvest provides Fairview with client services and marketing functions are performed by nabInvest, with other non-investment functions (e.g. IT, legal, back-office) outsourced to third-party providers.

The remuneration for all 3 Portfolio Managers is tied to business profitability as a key determinant of total compensation. Financial penalties also exist should a Portfolio Manager depart within the first several years of operation. Zenith considers this structure to well align the portfolio managers with the unit holders in the fund.

nabInvest has invested seed capital into the Fund, co-investing alongside Adams, Cronin, and Glenane. Zenith strongly endorses the investment by stakeholders in their own product, as it creates a structural alignment of interests with investors. Also pleasing is Fairview's proposed Funds under Management (FUM) capacity of \$500-\$600 million. Zenith views this to be a relatively conservative estimate of where capacity constraints exist for managers in this sector, and therefore consider the likelihood of future FUM levels detracting from performance to be low. The Fund has approximately \$63 million in FUM, as at the 31st December 2010. Zenith has been encouraged by the firm's progression since inception, and is pleased the firm is currently in a profitable position.

In summary, Zenith considers Fairview's partnership with nabInvest to be a sound arrangement, as nabInvest's capital contribution and distribution support provides stability for both the Manager and investors, and allows the investment team to focus their efforts on managing the portfolio. Furthermore, with equity in the business and material investment in the Fund, Zenith views the strong alignment of interests with investors in the Fund to be a significant attraction of the offering.

Investment Team:

Fairview's investment team of 3 highly experienced investment professionals Adams, Cronin & Glenane take a collaborative approach to stock research and decision making, with each member providing equal input into the process. In acknowledgement of the team's broad experience across all market sectors, there is no formal allocation of stock and/or sector responsibilities. Each stock researched is covered by 2 analysts, and all are required to peer review each other's analysis and provide input into portfolio construction.

The 3 all worked closely together for a number of years at Goldman Sachs JBWere Asset Management (GSJBW) and covered both large and small caps. The experience gained within the Australian Small Companies sector provides a deep familiarity with most of the Fund's investment universe, and also provides invaluable corporate and industry contacts.

Adams has over 15 years experience in financial markets, including serving as a Senior Investment Manager within GSJBW for over 10 years with both portfolio management and sector based responsibilities. Most recently, he had Portfolio Management responsibility for GSJBW's Emerging Leaders Fund for approximately 1 year.

Cronin was employed by GSJBW for over 12 years, firstly on the sell side as head of the firm's banking and finance sector research team before serving as a Senior Investment Manager with broad sector responsibilities.

Glenane has over 18 years experience, including a number of years at GSJBW as a Senior Investment Manager. Before joining GSJBW, Glenane built a strong track record as an analyst with McIntosh Securities (now Merrill Lynch) and then CSFB (now Credit Suisse).

All 3 team members achieved a strong personal track record at GSJBW, which is backed by detailed attribution analysis showing their stock picking track record and contribution to fund performance. In tracking and rewarding performance at Fairview, a policy has been established whereby bonuses are based on the achievement of information ratio targets on an annual basis. As the information ratio is a risk adjusted metric, Zenith believes this discourages each analyst from taking excessive risks in the pursuit of outperformance. Also noteworthy is that performance related bonuses are shared equally amongst the team, which is a strong expression of the team-based approach.

In addition to research responsibilities, all 3 team members share dealing and business management responsibilities, which represent a small portion of their daily duties. Zenith believes the current resourcing is appropriate for its size, however, should FUM grow significantly the benefit of an additional analyst would become more prevalent.

In Zenith's view, Fairview is well resourced with 3 senior investment professionals, who are all highly experienced and have strong track records in small companies' investment.

Investment Process

The Fund's investment objective is to outperform the S&P/ASX Small Ordinaries Accumulation Index by ~5% p.a. (before management fees) over rolling 5 year periods, within a tracking error range of 5% to 7%. Fairview aims to achieve its objective by applying a 'core', style neutral (a blend of growth and value) approach and focussing on superior stock selection as its primary source of outperformance, rather than taking large sector and factor tilts away from the benchmark. Portfolio biases are therefore monitored closely to ensure they do not become excessive and breach the Fund's stringent risk controls. The Manager cites its focus on intensive company research, and following a disciplined and consistent investment process, as key underpinnings of the strategy.

Overall, Zenith believes that Fairview's process appropriately leverages off the key strengths of the Portfolio Managers, primarily being their bottom-up stock research skills and extensive company and industry contacts.

Security Selection

Initial Screening:

Starting with an initial investment universe of over 1,000 companies, Fairview applies screens to automatically eliminate loss makers, concept stocks such as early stage biotechs / junior mining exploration companies and listed investment companies.

Detailed and thorough filters are then applied, which assess stocks based on factors including cash flow and balance sheet strength, and quality of management. Fairview has designed

its filters to reduce the universe to approximately 200 companies for ongoing active research.

Investment Analysis:

Fairview's investment analysis methodology places critical importance on company visitations and forming a subjective view on the quality of the management team in place. To this end, Fairview is committed to meeting with company management of both existing and potential stocks for inclusion in the portfolio on at least a quarterly basis.

Zenith believes having 3 senior investment professionals in the Small Companies sector provides a key competitive advantage in this regard. Fairview typically has 2 PM's in attendance at management meetings. This provides the team with two points of view to consider, and allows cross-checking of information and assumptions that are derived from these meetings.

In addition to company specific analysis, Fairview use Porter style analysis to review industries on an ongoing basis. More specifically, this industry analysis involves evaluating growth prospects, competitive dynamics, and potential long-term returns for companies operating in the industry. This is intended to enable the team to identify sectors/industries that are undergoing favourable structural change, or are advantageously positioned in the business cycle.

Fairview's modelling and valuation estimates draw upon several valuation techniques and metrics, including Discounted Cash Flow (DCF), Price/Earnings ratio multiples, and sum of the parts, with a range of supportive metrics preferred in building an investment case. The team considers the extent of earnings growth and sustainable returns on capital as the ultimate determinants of a company's value. In addition, an appropriate balance sheet structure, which reduces the likelihood of financial distress, is also a key requirement for investment.

Investment Conviction and Peer Review:

Having performed the above independent analysis, Fairview then seeks to build conviction around the investment case by reference to 4 key factors:

Strength of thesis and insight

- Assess points of difference in Fairview's valuation with that of the prevailing market consensus.
- Determine whether the potential stock mispricing is sufficient to warrant investment.

Qualitative

- Further due diligence is conducted on the quality of the company, its management and industry dynamics

Valuation upside and confidence

- Rather than set specific price targets, Fairview establishes a fair value range for a stock, based on various valuation techniques and metrics.
- Fairview typically takes a 1 to 3 year view on forecasting earnings growth, and will also seek to identify potential catalysts for a positive re-rating of a stock.
- Low levels of confidence in the reliability of data and assumptions used for a company's valuation are likely to rule out any potential investment.

Risk assessment

- Earnings risk - Quantitative measures such as earnings momentum and volatility are considered in conjunction with the team's qualitative assessment to assess the short-term earnings outlook. Fairview will generally avoid stocks with potential downside to consensus earnings forecasts as this normally results in underperformance.
- Financial risk - Gearing levels and future refinancing requirements are examined to obtain comfort that a company will continue to be adequately financed to pursue its objectives.
- Liquidity - Measures of stock liquidity are reviewed to ensure the Fund will be able to enter and exit a position.

Zenith views Fairview's stock research process to be built on solid investment principles. Although Fairview's final research note is brief (typically 1-2 pages), Zenith believes it adequately documents the investment rationale behind each stock in the portfolio, and provides sufficient information for ongoing review and debate. Moreover, whilst the process and valuation methodology is not as structured as some of the Manager's peers, the experience and expertise of the investment team overall, gives Zenith a high level of confidence that this flexibility will assist the team in making timely and considered investment decisions.

Portfolio Construction

Fairview's approach to portfolio construction, like its stock research process, is collaborative and not structured on formulaic guidelines in setting portfolio weights. In constructing the portfolio, the Manager aims to add value predominately through stock selection, rather than taking large 'top-down' sector bets against the benchmark. Sector and factor exposures are carefully managed to ensure the Fund remains true-to-label as a 'core' style neutral exposure to Australian Small Companies. Sector weights are typically kept within +/- 10% of the benchmark (soft constraint).

Stocks selected for investment are those which the team has the highest conviction in (i.e. - attractive upside versus level of risk). Intuitively, higher conviction will generally result in a higher weight. Conviction levels are primarily determined during the analysis and discussion conducted throughout the preceding stock selection process (i.e. - 4 key factors). It is expected that the majority of stocks in the portfolio will have the approval of all 3 portfolio managers. In the event there is a dissenter, the position is limited to a maximum 0.50% of the Fund. Although positions without unanimous support rarely occur in the Fund, Zenith views the 0.50% limit as a sensible constraint.

As a 'bottom-up' stock picker, Fairview's sell discipline centres on ensuring the original investment thesis for a stock remains intact. This requires regular review and debate by the team, particularly as a stock approaches its price objective and the potential for further material upside decreases. Stocks may also be trimmed to return the stock back to its original target weight, and/or to comply with the Fund's risk constraints (i.e. - max. 5% active weight).

Position sizes will generally fluctuate between 0.5% - 3.5%, with a maximum weight of 5%. The portfolio overall is intended to hold between 25 and 55 stocks, and will typically hold around 50 stocks. The Fund has a formal maximum cash limit of 10%, however Fairview endeavour to remain close to fully invested, (i.e. - cash exposure below 2%) a practice which Zenith endorses. Large cash inflows are usually equitised

using SPI futures until the cash can be prudently invested in physical stocks.

Turnover levels are expected to fluctuate between 40% - 60% p.a., although the Manager is prepared to exceed these levels depending on the prevailing market conditions. The Fund cannot hold any stocks within the S&P/ASX 50 Index, however up to 20% of the Fund can be held in mid cap stocks (i.e. top 51-100). This prevents the Manager from being forced to immediately sell stocks that enter the S&P/ASX 100 Index, and also potentially allows greater sector diversification (e.g. - gain higher quality exposure to the resources sector). Zenith is comfortable with these constraints, which allow the Manager a degree of flexibility, but also ensure the Fund remains predominately invested in the small caps market segment.

Risk Management

Portfolio Constraints	Description
Security Numbers	25 to 55
Weight - Security Rel. Index (%)	+/- 5%
Weight - GICS Rel. Index (%)	+/- 10% (soft constraint)
Weight - S&P/ASX 50-100 (%)	max: 20% generally ~10%
Weight - S&P/ASX 50 (%)	max: 0%
Tracking error (% p.a.)	5% p.a. to 7% p.a.
Cash (%)	Max 10%; generally ~2%

Fairview's risk management approach is primarily a function of avoiding stocks with high downside risk, and through careful management of sector/style tilts at the portfolio level, which are subject to a soft constraint of +/- 10% of the benchmark weight. Thorough due diligence is conducted during the stock research process, so that the potential downside to an investment thesis can be properly understood and accounted for. In Zenith's opinion, Fairview's requirement that all stock research must be subject to regular peer review, ensures the team's investment assumptions and conviction levels are constantly being challenged for validity.

The risk management process is further aided by the application quantitative metrics focusing on earnings revision trends (to assess the risk of further downward revisions) and liquidity measures (to assess the ability of the Fund to enter and exit a position). In using quantitative analysis to manage risk, the Manager is mindful of BARRA risk factors and sector exposures. However, the team is aware of the limitations of such analysis, and prefers to conduct a more subjective assessment of risk. Although the risk management systems in place are currently sufficient, should FUM levels rise materially in future, Zenith would expect more sophisticated tools for monitoring stock liquidity, etc to be implemented.

Tracking error is targeted at 5% - 7%. Fairview is generally conservative in setting active sector weights, which are expected to be around +/- 5%, comfortably within the soft +/- 10% limit. The Fund's risk management strategy may also involve broadening out the portfolio, with the number of stocks in the Fund expected to be around the upper end of the 25-55 range, where market conditions are volatile and the team has an uncertain outlook. Overall, Zenith believes the experience of all 3 PM' contributes to a deep understanding of risk, and views the Fund's performance throughout recent market volatility as a positive test of the Manager's prudent risk management approach.

Risks of the Fund

As is the case with all Australian equities based products, the biggest risk to this Fund is a sustained downturn in Australian small cap equities, which is likely lead to negative performance. Investors can minimise this risk on their portfolio overall by adopting a long-term investment horizon of 5+ years, and implementing periodic and disciplined rebalancing of a portfolio as per long-term strategic allocation targets.

Another major risk for fund managers is excessive FUM. Excessive FUM can cause serious problems particularly in the small companies segment given the relative illiquidity of numerous stocks in the sector and therefore can hinder a manager's ability to react to market movements in a timely manner. Pleasingly, Fairview is well aware of this potential threat and has set the Fund's capacity around \$500-\$600 million, which is a conservative target in comparison to many of the Manager's peers. Furthermore, Zenith notes that consideration of stock specific liquidity is built into Fairview's investment process.

As with any start-up manager, business and operational risks are elevated while the Firm seeks to establish a profitable level of FUM. The firm is currently profitable, largely due to the Funds ability to attain performance fees. Zenith believes the financial backing and distribution support from nabInvest provides a key foundation for organisational stability in the medium to long term.

As with most boutique fund managers, key person risk is high, and any departure would trigger a review of Zenith's rating on the Fund. However, offsetting this risk to a large degree is Fairview's ownership structure, co-investment by the team in the Fund, and remuneration agreements that compel each of the PM's to remain with Fairview for the long-term, with financial penalties imposed should a Portfolio Manager depart within the first several years of operation.

Applications of the Fund

2 years Excess Correlation Table	
Fund Name	Excess Correlation
Aviva Investors Small Companies Fund	0.65
Challenger Wholesale Microcap Fund	0.56
Ironbark Karara Australian Small Companies Fund	0.59
Perennial Value Smaller Companies Trust	0.68

For investors seeking to achieve a well blended exposure to Australian Equities, Zenith suggests the Fund is best used in combination with a large-cap Australian Equities Fund. The Fund has a slight bias toward mid-caps (up to 20% weight), but is not permitted to invest in stocks within the S&P/ASX 50 Index. This implies that the potential for overlap with a large-cap Australian Equities Fund is slightly higher versus other small cap funds which are restricted from investing in mid caps.

As with all small-companies funds, Zenith believes the Fund is most appropriate for those investors seeking a growth based investment and who are prepared to invest for at least 5 years to maximise their potential for optimal results. Fairview's 'core', neutral style approach and objective of limiting tracking error to a range of 5% - 7%, makes the Fund an attractive option for investors seeking a single fund exposure to Australian small companies.

Fees

Fairview has set the base management fee for the Fund at 1.20%. The Manager also charges a 20.5% performance fee (after fees and expenses) in excess of the S&P/ASX Small Ordinaries Accumulation Index. The performance fee is subject to the Fund outperforming its previous high watermark, and is not payable in a period of negative absolute performance. There is also a buy/sell spread of 0.30% charged on the unit price on entry and exit. Zenith considers the level of fees overall to be moderately expensive in comparison with peers.

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