

Analysts: James Gunn; Simone Arblaster

Products Facts

Manager	Prime Value Asset Management	Fund type	Retail	Boutique	Yes
APIR code	PVA0001AU	Specialisation	Growth/GARP	Multimanager	No
Fund status	Open	Peer group	Australian Equities - Large Cap	Inception date	April 10, 1998
Min. investment (A\$)	40000			MER (% pa)	1.44

Standard & Poor's View

S&P rates this fund three stars, reflecting our conviction that the manager will consistently generate risk-adjusted returns in-line with both its relevant investment objectives and its peers.

Prime Value Asset Management Ltd. (Prime Value) is a benchmark-unaware Australian-equities manager that has an absolute-return focus. Stock and sector bets are largely unconstrained and portfolios will typically have a significant exposure to small- and micro-cap stocks. This gives the fund a different risk profile to both its benchmark and large-cap peers, and makes it more suitable as a satellite-type exposure.

Prime Value is deliberately flexible in its decision-making process. There is no prescribed framework for stock analysis; rather, the team conducts analysis that it believes works best for a particular company, sector, or a stage of the market cycle. Top-down and thematic influences are also important considerations within portfolio construction, which is reflected in the size of the fund's active sector tilts.

CIO and co-founder Han Lee was largely running the Prime Value portfolios single-handedly between 1998 and 2004. The expanded team is tight-knit and has continued to deliver impressive excess returns for growth fund investors, particularly over the past year. Notwithstanding this, S&P is of the view that Mr. Lee's macro insights, in particular, need to be supported by a more adequately resourced internal-research effort. The bottom-up 'grunt' work is now largely the responsibility of one analyst, with the experienced Leanne Pan now less actively involved in this aspect of the research effort.

Going forward, S&P would also like to see Prime Value conduct relative performance attribution at the stock level. This would provide a clearer ongoing assessment of the manager's stock picking relative to its investable universe.

Product Features

Prime Value is a benchmark-unaware Australian-equities manager that has an absolute-return focus. The fund aims to achieve positive returns and to outperform the S&P/ASX 300 Accumulation Index over the medium-to-long-term. The target return is 10-15% p.a. over rolling five-year periods. The maximum cash level is set at 30%, but can go higher with board approval. A performance fee of 20.5% is applicable to outperformance of the benchmark, where performance after all fees is positive.

Fund Objectives

Benchmark	S&P/ASX 300 Accumulation Index
Target return (% p.a.)	High than benchmark over the medium to long-term
Target tracking error	Not targeted

Investment Style

Prime Value does not manage its portfolios to a dominant investment style; rather, it adopts a style that reflects the objectives of each strategy. The Prime Value Growth Fund, which targets companies with good growth prospects at an attractive price, is more likely to exhibit a growth bias, whereas the manager's imputation fund is constructed to be more value-oriented. A more distinguishing characteristic of Prime Value's investment approach, relative to S&P's Australian-Equities--Large-Cap peer group, is its bias toward small-caps and micro-caps.

Passive						Active
Value						Growth
Small Cap						Large Cap

Investment Team

Mr. Lee is the managing director and chief investment officer of Prime Value, and is ultimately responsible for the performance of the fund. He has more than 30 years of investment experience, and was a portfolio manager for the Shell staff superannuation fund before co-founding Prime Value in 1998. Mr. Lee was largely managing the Prime Value portfolios single-handedly between 1998 and 2004.

In July 2004, Leanne Pan commenced as portfolio manager for the fund. Ms. Pan has more than 17 years of investment experience, and previously worked with Mr. Lee at Shell between 1990 and 1997, which is a positive for team dynamics. Before commencing with Prime Value, Ms. Pan was a portfolio manager with the Orica superannuation fund.

Mr. Lee and Ms. Pan are supported by Fiona Clark and Andreas Rosenau. Fiona Clark joined Prime Value as an investment analyst in December 2004. As Ms. Clark has recently returned from maternity leave, and is working part-time, her primary focus is attribution analysis and investor relations. Mr. Rosenau joined the team in 2006 as a replacement for quantitative analyst Michael Chien, who departed in May 2006. Mr. Rosenau is highly qualified and brings eight years' business and finance experience to the role, but has only two years of investment management experience. In addition to his responsibilities for the quantitative screening process, Mr. Rosenau is now largely responsible for all bottom-up research, including research-report writing and company modelling. The purpose of this change has been to allow Mr. Lee and Ms. Pan to concentrate on macro themes and portfolio construction, as well as to free them up to conduct more company visits.

S&P is of the view that Mr. Lee's macro insights, in particular, need to be supported by a more adequately resourced internal-research effort. Given the small size of the team and the relative inexperience of Mr. Rosenau, we would prefer to see Ms. Pan remain actively involved in the bottom-up 'grunt' work, or an additional experienced analyst recruited into the team.

Mr. Lee is the only equity holder among the investment team, although the other members are each rewarded with a fixed share of any performance fees and management fees.

New					Experienced
Small					Large
Unstable					Stable

Investment Process

The key tenets of Prime Value's investment philosophy are that minimising mistakes produces superior performance; investment is as much an art as science; benchmarks are inefficient and value can be added through top-down decision making, particularly through the application of portfolio tilts. Business valuation underpins all investment decisions.

Prime Value is less process-driven in its decision making than many of its peers. The investment process is best described as flexible, with both bottom-up and top-down considerations impacting on stock selection. Idea generation comes from a variety of sources, including but not limited to quantitative screening, brokers, IPOs/placements, economic data and industry news. The quantitative screening model, includes historical and forecast data for approximately 500 stocks. Data sources include company historicals, IRESS and internal and broker forecasts. The number of companies included in this database, which has been increased since S&P last review, reflects the breadth of the manager's investable universe. In addition to idea generation, application of the screen is the primary means by which the manager narrows its investable universe and prioritises fundamental research.

The team is more reliant on broker research for its large cap coverage (top 100 companies), preferring to focus its internal research effort on small-caps and micro-caps. This is a function of being a small investment team (three dedicated personnel) but also that Prime Value believes there are greater inefficiencies to exploit down the capitalisation spectrum and that these companies tend to be less complex from a fundamental analysis perspective. While broker research, where available, is still used in the manager's coverage of small caps, and a potential source of stock momentum, the manager has stated that its ex-100 coverage is now much more driven by internally-generated research.

There are no prescribed frameworks for stock analysis; rather, the team has the flexibility to conduct analysis that it believes works best for a particular company, sector or even a stage of the market cycle. That being said, the team places particular emphasis on assessing management quality, and typically has access to senior management at least for its small and micro-cap holdings. The research template, which tends to be thesis rather than model-driven, is focussed on identifying the key investment case and risks, largely through SWOT analysis and qualitative (market position, product mix and management) and quantitative (financial ratios) peer comparison. The source of the valuation and resulting return expectation will largely depend on whether the research is internally or externally driven.

As an unconstrained fund manager, Prime Value do not take a relative-to-benchmark approach in determining stock weights, nor is a target tracking error set for either the Growth or Imputation funds. Top-down and thematic influences are also an important consideration within portfolio construction, as reflected in the active sector tilts within both funds. At a high level, each fund will comprise a core, growth and income component. While there is no pre-defined allocation to these portfolio components within either fund, the Growth Fund will have a larger growth overlay and the Imputation Fund will have large income overlay. Stocks with an 'enhanced' level of earnings growth driven by a strong return on equity, positive sectoral dynamics and evidence of a competitive advantage will be included in the growth component. A

limited number of what the manager calls 'blue-sky' opportunities may also be included - these are those companies with high growth potential, but not necessarily a proven earnings track record. The income component will include those stocks offering a high degree of both earnings and dividend income certainty, with a bias towards a higher stream of tax effective dividend income.

In determining individual weights, the key determinants are the risk/reward characteristics of each stock. Stocks with the largest portfolio weighting will be where the team has the highest degree of confidence, where there is the least perceived downside risk and adequate liquidity. Stocks exhibiting these characteristics would normally attract a weighting of at least 2%. In determining whether a stock will be held at +2% or less than 2%, the team makes a positive (green light) or negative (red light) assessment against nine criteria. These criteria are research (positive if internal), whether the stock is included in the quantitative database, financial strength, expected total return, industry themes (does it meet a top-down portfolio theme?), management quality, company meeting (yes or no), liquidity and volatility. Those stocks which score greater than seven green lights will typically constitute major holdings (greater than 2%), whereas stocks scoring less than seven green lights but at least a green light on expected total return will be a minor holding (<2%), with potential for that position to be increased with greater conviction. There is no greater weight applied to any one of these factors or indeed a minimum number of green lights for a minor holding.

The portfolio construction process is overlaid with risk control measures, which are detailed in the Risk Management section of this report. The final portfolio will typically hold between 30-60 stocks, a significant proportion of which has historically been in small (ex-100) and micro cap (ex-300) holdings. Maximum cash levels are set at 30% and may go higher, subject to approval from Prime Value's board of directors. Irrespective of market conditions, S&P believes that investors would expect the manager to be more fully invested than it has been in recent years.

Performance

While most of the fund's impressive longer-term track record is attributable to Mr. Lee and also Yong Quek, the expanded team has continued to deliver impressive excess returns for Growth Fund. The Growth fund outperformed the S&P/ASX 300 Accumulation Index by 3.5% and 7.6% over the 3 and 5 years ending April 30 2008 (before performance fees). Prime Value's conviction in the resources story has proven a very strong contributor to relative returns and the portfolio remained overweight to both the materials (4.3%) and energy sectors (4.4%) at March-end 2008.

Performance has been particular strong over the last year. Over a period in which the index lost 5.9% (1 year to April 30 2008), the fund delivered a positive return of 4.6% (before performance fees). The allocation to cash provided a strong buffer during this period, as did the significant underweighting to financials (-25.9% at March-end 2008).

In light of the key drivers of market performance and portfolio positioning, it's not surprising that stock attribution shows that resource stocks or those substantially leveraged to the sector have been the biggest contributors to performance on an absolute basis. In order to better understand the sources of excess return, S&P would like to see Prime Value conduct relative performance attribution at the stock level. This would provide a clearer ongoing assessment of the manager's stock picking relative to its investable universe.

Given the manager's absolute-return, benchmark-agnostic approach, the strategy will generate a high tracking error (6.5% pa over the last five years). Investors have historically been well compensated for bearing this additional level of benchmark risk (tracking error).

Prime Value's low turnover approach is a positive for after-tax returns.

Performance Measures

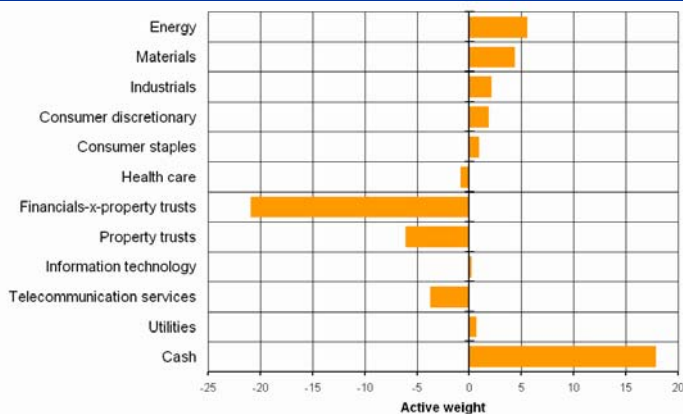
Average portfolio turnover (%)	25
Typical number of stocks in portfolio	30-60

Source: Prime Value Asset Management.

investors, we would like to see this supported by a formal, independent assessment of the manager's capacity.

Analyst(s): James Gunn; Simone Arblaster.
Release authorised by: Mark Hoven.

Sector Exposure Versus Fund Benchmark (at March 31, 2008)



Source: Prime Value Asset Management.

Risk Management

Prime Value structures its portfolios quite differently to both the benchmark (S&P/ASX 300 Accumulation Index) and peers, with stock and sector positions are largely unconstrained. The CIO has complete discretion in this regard, other than individual investments cannot exceed 10% of the portfolios (with the exception of BHP for the Prime Value Growth Fund), the number of stocks in each portfolio must be greater than 20 and cash levels must be kept to less than 30%. As at Mar 31 2008, 17.6% of the Prime Value Growth Fund was in cash and 27.7% was in small caps. The allocation to small caps included a 10.8% holding in micro caps, which typically carry far greater liquidity risk due to their small size and lack of broker coverage. While not a hard constraint, the manager looks to invest in companies with a market capitalisation of at least \$50 million.

S&P would like to see Prime Value employ analytical risk attribution systems on a more ongoing basis, in order to better understand contributions to overall portfolio risk and any unintended factor exposures.

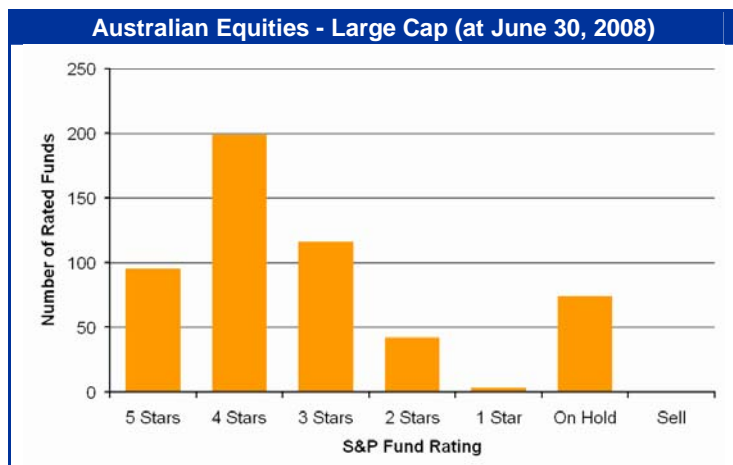
Management Group Profile

Prime Value Asset Management Ltd. (Prime Value) is a boutique investment firm that was set-up in 1998 by Mr. Han Lee (principal), the managing director and chief investment officer, and Y Yong Quek (principal), executive director. The firm has 13 staff, including the four-person investment team (three dedicated) and is solely focussed on Australian equities. There is a strong alignment of interests between investors; the principals of the business and the investment team whose combined investments in the two funds represent approximately 5% of funds under management.

Market Share

As at March 2008, Prime Value had \$337 million in FUM, approximately 60% of which was in the growth strategy. In order to maintain the opportunistic nature of its style, Prime Value has stated that it will cap its total FUM at \$1 billion. While this is a positive for

S&P Fund Rating Reference Information



Reference Material

Sector Reports
www.standardandpoors.com.au/funds
Reader's Roadmap
www.standardandpoors.com.au/funds
Glossary
www.standardandpoors.com.au/funds
Guide to S&P Qualitative Fund Ratings
www.standardandpoors.com.au/funds
Fund Rating Team Biographies
www.standardandpoors.com.au/funds

Fund Rating Peer Groups by Sector

Australian Equities	International Equities	International Fixed Interest	Alternative Assets
Large Cap Diversified	Diversified Equities	Diversified Fixed Interest	Commodities
Large Cap Income	Emerging Markets	Diversified Fixed Interest Income	Multi-Sector
Large Cap Indexed	Emerging Markets Asia ex Japan	Fixed Interest	Private Equity Listed
Large Cap Industrials	Emerging Markets China	Fixed Interest High Yield	Private Equity Unlisted
Long Short	Emerging Markets India	Fixed Interest Income	Infrastructure Listed
Small Cap	Large Cap Diversified	Mortgages	Infrastructure Unlisted
Specialist	Large Cap Income	Mortgages High Yield	Alternative Strategies
Australian Fixed Interest	Large Cap Indexed	Mortgages High Yield Hybrid	Single Strategy Funds Multimanager
Cash	Large Cap Industrials	Mortgages Conventional	Single Strategy Funds Single Manager
Cash Enhanced	Long Short	Mortgages Hybrid	Multi-Strategy Funds Multimanager
Fixed Interest	Long Short Specialist	International Property	Multi-Strategy Funds Single Manager
Fixed Interest Income	Long Short Regional	Direct Commercial	Multi-sector
Mortgages	Regional Japan	Direct Development	Capital Guaranteed
Mortgages High Yield	Regional UK/Europe	Direct Diversified Direct	20
Mortgages Conventional	Regional US	Direct Industrial	40
Mortgages High Yield Hybrid	Regional Asia	Direct Residential	60
Mortgages Hybrid	Small Cap	Direct Retail	80
Australian Property	Specialist Healthcare	Direct Rural	100
Direct Commercial	Specialist Information Technology	Direct Specialised	Equity
Direct Development	Specialist Resources	Diversified Property	Other
Direct Diversified Direct		Listed	
Direct Industrial			
Direct Residential			
Direct Retail			
Direct Rural			
Direct Specialised			
Diversified Fixed Interest Listed			








Fund Rating Philosophy

A star rating is a forward-looking qualitative assessment of a manager's ability to consistently generate risk-adjusted fund returns (net of fees) in excess of both its relevant investment objectives and its peers.


Fund Rating Process

In assigning a star rating to a fund, Standard & Poor's evaluates: the size, skill, and stability of the manager's investment team; the clarity, implementation, and risk management of the investment process; the fund's objectives, fee structure, and portfolio characteristics; and the manager's business management.

Fund Rating Definitions

	Standard & Poor's has very high conviction that the manager will consistently generate risk-adjusted fund returns in excess of its relevant investment objectives and relative to its peers.
	Standard & Poor's has high conviction that the manager will consistently generate risk-adjusted fund returns in excess of its relevant investment objectives and relative to its peers.
	Standard & Poor's has conviction that the manager will generate risk-adjusted fund returns in-line with its relevant investment objectives and relative to its peers.
	Standard & Poor's has conviction that the manager will not generate risk-adjusted fund returns in in-line with its relevant investment objectives and relative to its peers.
	Standard & Poor's has high conviction that the manager will not generate risk-adjusted fund returns in-line with its relevant investment objectives and relative to its peers.
	Issues that may affect the fund's management have emerged; and the fund rating is temporarily suspended, pending clarification.
	Significant issues exist that potentially will adversely affect the fund's performance. Investors should consider obtaining advice on switching or redeeming funds.

Fund Rating Subscript

 The investment process, fund manager, or the fund has a relatively short history, or the analytical team has changed significantly, but a relevant and demonstrable track record is shown on similar funds.

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