

AUSTRALIAN

# RESEARCH

MANAGED INVESTMENTS ANALYSIS

## Perpetual Protected Investments – Series 3

March 2008

Exposure to a menu of managed funds with  
100% capital protection and a choice of up to 100% financing

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## Australian Managed Investments Structured Products – Structured Equity

**Note:** This report is based on the PDS, dated 17 March 2008, together with other information provided by PIML as at March 2008.

# Perpetual Protected Investments – Series 3

Exposure to a menu of managed funds with 100% capital protection and a choice of up to 100% financing



### Offer Overview

The Perpetual Protected Investments – Series 3 (the *Product* or *PPI*) is being offered by Perpetual Investment Management Limited (*PIML*). The Product provides investors with the ability to select investments from a menu of 20 managed funds (the *Funds*) while providing capital protection at maturity via a constant proportion portfolio insurance (*CPPI*) structure (the Funds together with the capital protection constitute the *Investment Strategies*). Capital protection incorporates profit lock-in, subject to the net asset value (*NAV*) of the Product reaching prescribed levels. The Product is primarily designed as a loan investment, with investors able to borrow up to 100% of their original invested amount, subject to a minimum loan of A\$50K. There is also a Capitalised Investment Loan facility to suit SMSF investors with an indicative 50% LVR. The capital protection applies at maturity (6 years and 10 months). Investors may, however, exit early through a quarterly liquidity facility. The Product is managed through a managed-investment scheme on a separately managed account (*SMA*) platform.

### Offer Detail

Offer Period	26-May-08:27-Jun-08
Investment Date	25-Jul-08
Maturity (years)	31-May-15 (6 years 10 months)
Min. Investment	A\$10,000/A\$25,000/A\$50,000*
Liquidity	Quarterly
Distributions	Reinvested

\*A\$10,000 per Fund (no loan); A\$25,000 per Capitalised Investment Loan; A\$50,000 per 100% Investment Loan.

### Risk/Return Profile



### Fees (paid to advisors), incl. GST, %

Upfront	Up to 3.3
Ongoing*	Up to 0.65

\* Commissions are payable to advisors: 2.2% from the Establishment Fee and 1.1% and 0.65% pa from the Loan Facility. Commissions are paid by PIML

### Investment View

#### Investor Suitability

Investors should note this report assesses the investment merit of the Product, not the underlying managed funds. As noted above, the Product primarily targets investors seeking up to 100% financing and expect the Product to appreciate by more than the total after-tax product and borrowing costs. Aegis regards the Product as best suited to several types of investors; investors who are relatively asset poor, income rich (unable to secure alternative lower-cost finance but able to service interest costs and receive the greatest tax deductibility benefits); investors who do not wish to liquidate existing investments but seek an enlarged exposure to equities; investors who are concerned about market volatility and direction over the foreseeable future and value both capital protection (at maturity) and the insulating effect of CPPI-related rebalancing into cash; and highly risk-averse superannuants and retirees seeking equities returns but limited downside risk. Loan investors should note while their initial investment amount is capital protected, they may incur a loss equal to cumulative interest costs, income-related CGT and tax costs plus any sell spreads on redemption. Investors should also note the CPPI structure is path dependent and is adversely impacted by volatility in the underlying investment. The consensus view generally is that the current market volatility will persist for the foreseeable future and this may result in an investment becoming considerably invested into the cash asset.

#### Recommendation

Aegis has reviewed the Product and issued a **HIGHLY RECOMMENDED** rating.

The investment opinion in this report is current as at the date of publication. Investors and advisors should be aware that over time the circumstances of the issuer and/or product may change, which may affect our investment opinion.

## SWOT Summary

### Strengths

- Well-structured CPPI mechanism that: lowers de-leverage risk through the initial bond floor level and the rebalancing triggers; improves tax effectiveness through the call-option structure; and lowers downside risk through the profit lock-in structure.
- The ability to invest through an SMA platform providing taxation benefits during the term (the ability to utilise capital losses derived from the CPPI rebalancing process) and the option not to incur a CGT event at maturity by continuing to hold Fund Units.
- Fund selection based on third-party due diligence and consideration of CPPI suitability. Risk/return can be tailored, given asset class and investment-style diversification of the investment menu and the ability to select multiple Funds (subject to A\$10K/Fund minimum).

### Weaknesses

- A long protected term during which there is no ability to switch Funds other than to redeem early. The long term also reduces the inherent value of capital protection.
- Liquidity is infrequent (quarterly), reducing the ability to market-time an early exit.

### Opportunities

- The ability for SMSF investors to access 50% (indicative only) financing through the Capitalised Investment Loan facility.
- Underlying Funds: The opportunity to access lower-cost wholesale versions of a diverse range of Funds.
- Potential to outperform the underlying fund in declining markets through the insulating impact of being rebalanced into cash.

### Threats

- Market-timing risks are high. Inclusion of the specialist asset class investments, however, may serve to add diversification to the portfolio. Additionally, the greater the volatility of a Fund, the greater the likelihood of hitting a sell trigger.
- Loan investors are exposed to interest-rate risk, unless they select a term-fixed-interest loan. The opportunity cost is generally high considering the current level of interest rates. Conversely, however, rising interest rates lower de-leverage risk (lower bond floor).

### Product Fees (paid by investors)

	Product	Sector Avg.*
<b>Base Fees, % of Portfolio Value</b>		
Upfront <sup>1</sup>	1.1	2.1
Ongoing <sup>2</sup>	1.45	1.9
Exit <sup>3</sup>	0.2	0.2
Average, p.a.	1.9	2.3

\*Based on structured products reviewed by Aegis over the last 12-month period.

<sup>1</sup> Based on a Loan Establishment Fee of 1.1% (incl. GST). Investors may also incur Advisor commissions, as determined by the commercial relationship between investor and advisor.

<sup>2</sup> Capital protection fee of 0.75% p.a. of the protected amount (reducing to 0% if there is no allocation to Fund Units) and an administration fee of 0.7% p.a. of NAV. The amount does not include the MER on the underlying funds.

<sup>3</sup> Assumes a sell spread of 0.2% for underlying Funds.

### Base Fees, % of Expected Income\*

Upfront	3.4	3.1
Ongoing	11.2	15.4
Exit	0.3	0.2
<b>Total</b>	<b>14.8</b>	<b>18.8</b>

\*Assumes an average gross return of 13% p.a.

### Loan Costs

Refer to Section 2 for rates and interest rate structures.

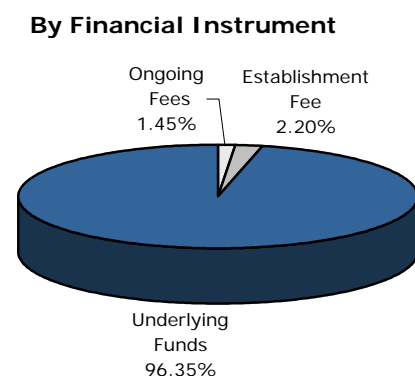
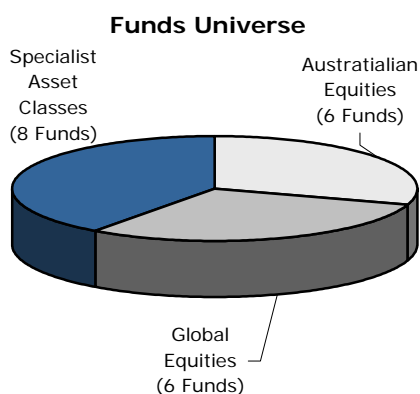
### Indirect Fees

Investors will incur management costs (including cost recoveries) on the underlying Funds, ranging from 0.34% to 1.88% p.a. Some Funds also have performance fees. Refer to Section 5.

### Fee Commentary

Aegis regards the total cost of the Product as competitive and generally lower than comparable products in the market.

## Portfolio Diversification



Source: PIML / Aegis Equities Research

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## 2. Structure

The Product is a managed-investment scheme on an SMA platform. On account of the SMA structure, investors have direct ownership of the assets within their investment. As such, transferring assets to and from the platform may not be a taxable event.

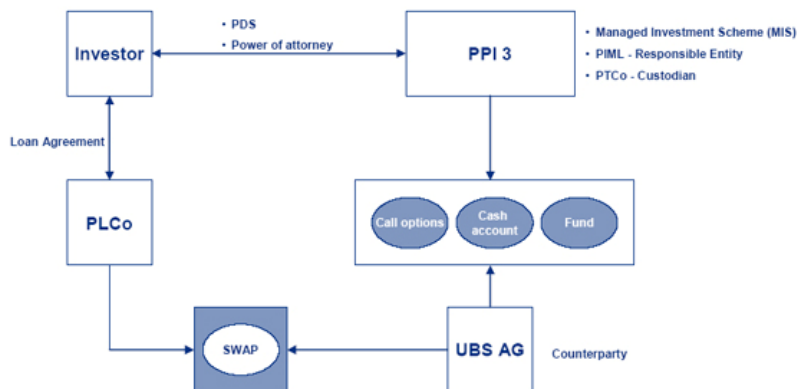
Each investor's portfolio consists of units in the selected Fund (the *Units*), a cash account and call options (the *Call Options*).

The Call Options represent the risk-less asset within the CPPI structure and ensure that, at maturity, investors will receive Units of a value at least equal to their initial investment amount. Using this structure, PIML will enter into a hedging arrangement with UBS AG, London Branch (*UBS*). Under the arrangement, UBS will issue options to PIML to acquire a number of Units at maturity. UBS will also instruct PIML in relation to the CPPI rebalancing process. PIML holds the options on trust for each investor under the SMA structure.

The cash account is a transaction account used to collect distributions and pay fees. It will ordinarily have a nil balance. If there is a residual cash balance after paying annual fees, the balance will be reinvested in additional Units. Conversely, if the cash balance is insufficient to pay fees, PIML will sell an amount of Units to cover the shortfall.

The 100% investment loan is an interest-only, limited-recourse obligation (limited to NAV at maturity if the NAV is less than the initial NAV), with the principal outstanding repayable at the maturity of the loan on 31 May 2015. Interest is externally serviced and investors are unlikely to physically receive distributions.

### Investment Structure



- PTCO – Perpetual Trustee Company Pty Ltd
- PIML – Perpetual Investment Management Limited
- PLCo – Perpetual Loan Company Pty Ltd
- UBS AG – UBS AG, London branch (S&P AA)

- PPI 3 - Perpetual Protected Investments – Series 3

Source: Perpetual

### Key Exposure

**Underlying Exposure:** 20 managed Funds (see below), providing exposure to Australian equities, international equities and specialist asset classes.

#### Australian Equities:

- 1 Ausbil Australian Active Equity Fund
- 2 Ausbil Australian Emerging Leaders Fund
- 3 Challenger W'sale Australian Share Fund
- 4 Perpetual's W'sale Australian Fund
- 5 Schroder W'sale Australian Equity Fund
- 6 Vanguard Australian Shares Index Fund

#### Global Equities:

- 1 AXA W'sale Global Equity Value Fund
- 2 DWS Global Equity Thematic Fund
- 3 GVI Global Industrial Share Fund
- 4 Perpetual's W'sale Int'l Share Fund
- 5 T.Rowe Price Global Equity Fund
- 6 Vanguard Int'l Share Index Fund (Hedged)

#### Specialist Asset Classes:

- 1 Aberdeen Asian Opportunities Fund
- 2 Colonial FS W'sale Global Resources Fund
- 3 IOOF/Perennial Global Property Trust
- 4 Macquarie Int'l Infrastructure Securities Trust
- 5 Merrill Lynch Global Allocation Fund Class D
- 6 Perpetual's W'sale Ethical SRI Fund
- 7 Platinum Asia Fund
- 8 Premium China Fund

**Currency Exposure:** Some Funds with exposure to international equities are exposed to currency risk.

### Exit Details

**Exit Facility:** At maturity, investors are required to repay the loan amount in full. Investors may choose from the following: 1) settle the loan from external sources and retain the full amount of Units; 2) settle the loan by selling the Units and retaining the balance of Units (subject to Fund minimums); or 3) rollover their portfolio into a new capital-protected series, if available. If investors exit early, the full amount of the loan principal is repayable in full. Prepaid interest is not refundable.

**Liquidity:** Quarterly, subject to the terms of withdrawal from the Fund.

**Holder Early Redemption:** Early redemption invalidates capital protection.

**Product Leverage**

Used: None

**Capital Protection**

Method: CPPI with profit lock-in. Under the lock-in, the level of protection will increase by 50% of the difference between the portfolio value and the protection floor when the portfolio value reaches 180% of the protection floor. The CPPI structure is relatively unique in that the Cash Asset is based on a Call Option, providing taxation benefits to the investor.

Key Parameters/Metrics: Bond Floor Day 1: 68.0%; Day 1 fall to hit first sell trigger: 20.0%; 6-month fall to hit first sell trigger: 17.7%

Conditions: Must be held to maturity.

Cost: 0.70% p.a. of the protected amount (reducing to 0% in a 'cash lock' event).

Counterparty Risk: With Swap and Call Option, there is a risk UBS (S&P rating: AA) may fail in its obligations.

**Tax**

Disclaimer: Tax consequences depend on individual circumstances. Investors must seek their own taxation advice. The following comments show Aegis' expectation of tax for ordinary Australian taxpayers, but cannot be considered tax advice.

Capital Gains: The sale of Units may give rise to capital gains/losses. The 50% capital gains tax (CGT) discount may apply on Units held for longer than 12 months. Investors should note they may incur capital gains and losses during the investment term as a result of CPPI-related rebalancing. Investment in Call Options does not generate taxable income for an investor during the term of the Product. At maturity, the Investor is delivered Units through the exercise of Call Options. Tax is not paid on any unrealised gains until the Units are sold (at the Investor's discretion, after maturity). Capital losses can be offset against capital gains from sources outside the product.

Distributions: On income account. The reinvestment of distributions may mean investors have to pay any tax on distributions from their own sources. Investors have full entitlement to any attached franking credits.

Interest Deductibility: 100% deductible.

Fee Deductibility: Administration Fee: 100% deductible in the year incurred. Dynamic Management Fee: 100% deductible in the year incurred. The Establishment Fee forms part of the cost base for capital gains tax purposes.

Call Option: The premium paid forms the cost base of Units acquired on the exercise of the Call Option. No tax is payable when the Call Option is exercised.

**Legal Structure**

Wrapper: Managed investment scheme with SMAs.

Custodian: Perpetual Trustee Company Limited

Responsible Entity: Perpetual Investment Management Limited

Offer Document: Perpetual Protected Investment - Series 3 Product Disclosure Statement, dated 17 March 2008.

**Returns**

Capital vs. Income: Mostly/wholly capital. Distributions are likely to be reinvested and will be physically paid only if the Product is fully exposed to the Funds and has a material buffer over the first sell trigger.

Income Frequency: Subject to the distribution policy of the selected Fund.

**Investor Leverage**

Available:	100% Investment Loan	Capitalised Investment Loan
Loan to Value Ratio (LVR) :	Up to 100%, with the option of a renewable Annual Interest Loan to borrow and prepay the interest on the 100% Investment Loan each year.	Up to approx. 50% (Final LVR will be set on or about 20 June 2008).
Cost (Interest Options and Rates):	1) Fixed rate for the term of the loan, monthly in arrears for the first 12 months and then prepaid annually in advance from June 2008 (10.30%); 2) fixed annually, prepaid annually in advance from June 2008 (10.40% until June 2009); and 3) variable rate, payable monthly in arrears (10.10%). Aegis notes the interest-rate levels are lower than comparable products in the market.	Fixed rate for the term. Interest rate will be set on 20 June 2008. No principal and interest payments are required during the term of the loan. Limited-recourse loan with interest accrued monthly in arrears and capitalised into the loan balance over the term of the product.
Recourse:	Limited recourse to Product NAV at maturity, subject to no default by investor, UBS or PIML.	

**Management**

Team: The Perpetual Structured Products Group was established in October 2005 as part of Perpetual's Wealth Management division. The Product represents the third series of this particular investment structure. The five key members of the management team are Russel Chesler, James Parker, Arian Neiron, Russell Grigg and Michael Brown. In Aegis' view, they are all well qualified for their respective roles.

**Risks**

Refer to the *Risks* section in the PDS.

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## 3. Investment Process

### Product Philosophy

As noted earlier, while the loan is optional, the Product has been designed specifically for investors seeking geared investment. The capital protection is incorporated into the Product primarily for the purpose of providing security to the lender and, in turn, investment financing to the investor.

The investment menu has undergone a due-diligence review by Mercer. PIML's intention was to utilise Mercer's institutional-grade managed-funds review process.

The CPPI mechanism has been designed with the investor in mind, based on a longer 6 year 10 months protected period, to reduce the likelihood of a de-leverage event. PIML will be offering a slightly different method of capital protection via the CPPI structure. Traditionally, the CPPI structure involves an allocation between the underlying investment and cash. However, acting on behalf of PIML, UBS has replaced the cash exposure with an exposure to Call Options. Call Options have a zero strike price and will automatically be exercised at maturity. Each Call Option will deliver the investor Units in the Fund equal to A\$1.00.

### Investment Menu Criteria

The Product's investment menu (see Figure 2) was selected based on the following criteria:

- **Experience of Investment Manager and Performance History.** Mercer was primarily responsible for assessing the historical performance and experience of the investment manager. Mercer provided an assessment of the people and the process as well as an opinion and rating of each of the managers. Mercer's assessment was cross-checked with ratings from independent research houses, where available. Mercer also undertook an assessment of the overall investment menu to determine whether there was sufficient diversity by asset class and investment style.
- **Suitability of Fund for Capital Protection.** For each eligible Fund, PIML assessed the suitability to the CPPI method of capital protection. In this respect, Funds with higher volatility were rejected. Furthermore, each Fund needed to have sufficient reporting and Unit-pricing practices to enable the CPPI mechanism to operate effectively.
- **Advisor Demand.** PIML favoured Funds with sufficient advisor demand and confidence.

Based on the above criteria, as well as various other considerations such as fund size and liquidity, a shortlist of eligible Funds was created and presented to the PIML Product Investment Committee for final determination.

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Figure 1. Menu of the Underlying Investment Funds

Fund Name	MER (p.a.)	Features/Style and Comments
<b>Australian Equities Funds</b>		
Ausbil Australian Active Equity Fund	0.90%	Style-neutral Fund aiming to provide long-term growth with moderate tax-effective income. The investment process is designed to capture changes in earnings and earnings revision at an early stage to exploit inefficiencies in the stock-price movement.
Ausbil Australian Emerging Leaders Fund	0.85%	A moderately concentrated, very actively managed high-conviction portfolio, with a focus on mid to small stocks. Selection approach is style neutral, with an emphasis on early identification of earnings and earnings revisions.
Challenger W'sale Australian Share Fund	0.90%	Style-neutral Fund. The manager adopts a longer-term investment horizon and utilises fundamental analysis with a combination of valuation and qualitative company assessment, to identify mispriced companies.
Perpetual's Wholesale Australian Fund	0.99%	Moderately concentrated portfolio with significant weighting to the financial and materials sectors. Selection approach emphasises strong fundamentals and appropriate valuations.
Schroder W'sale Australia Equity Fund	0.92%	The Fund targets companies with quality growth business models with a long-term sustainable competitive advantage in their industry. Due to its longer-term selection perspective, the Fund has a buy-and-hold approach.
Vanguard Australian Shares Index Fund	0.34%	The Fund seeks to match the total return of the S&P/ASX 300 Index on a pre-fees basis. The Fund is managed using a passive strategy, and is not expecting any upside above the index return.
<b>Global Equities Funds</b>		
AXA W'sale Global Equity Value Fund	0.97%	A highly diversified portfolio characterised by some contrarian company and/or sector positions. Selection approach favours cheaper stocks with long-term earnings power. A consistent, high-conviction style.
DWS Global Equity Thematic Fund	0.90%	The manager aims to identify early on major secular and cyclical themes across country, regional and sector boundaries. The strategy is relatively benchmark unaware and has significant exposure to emerging markets.
GVI Global Industry Share Fund	1.23%	The Fund invests in a portfolio of global industrial companies that GVI believes are of high quality and offer good value. The manager is taking a conservative and value-based investment approach. The Fund is established in February 2005 and has a limited track record.
Perpetual's W'sale International Share Fund	1.23%	A broadly diversified portfolio, with stock selection based on strong fundamentals and attractive valuations. Perpetual took over from former manager Fidelity in March 2005. Consequently, past performance provides little guide to future performance.
T.Rowe Price Global Equity Fund	1.30%	Portfolio is relatively high risk and high conviction and likely to be high beta and overweight emerging markets over time. The selection approach has a strong growth emphasis and aims to take advantage of fundamental structural changes and growth opportunities, with competition largely avoided. The Fund has a limited track record (less than one year).
Vanguard Int'l Share Index Fund (Hedged)	0.36%	The Fund seeks on a pre-fees basis to match the total return of the MSCI World ex-Australia Index, hedged to the Australian dollar. The Fund is managed using a passive strategy and has outperformed the benchmark significantly since inception, mainly due to currency hedging.

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Figure 1. Menu of the Underlying Investment Funds (continued)

**Specialist Asset Classes**

Aberdeen Asian Opportunities Fund	1.18%	An active manager that believes superior long-term returns are achieved by identifying good-quality stocks at reasonable valuations and holding for the long term. Style-neutral Fund with a focus on fundamental analysis and balance-sheet strength.
Colonial First State Wholesale Global Resources Fund	1.16%	A selection with emphasis on companies with robust fundamentals and well positioned to perform through the resources cycle. Currency risk is not hedged.
IOOF/Perennial Global Property Trust	1.05%	Portfolio of 40-50 securities diversified by market, country and sector. Selection approach emphasises securities that hold quality property assets generating strong recurring cash flows. Currency exposure is generally hedged. The Fund has a short track record.
Macquarie International Infrastructure Securities Fund	1.00%	Portfolio of 20-50 listed infrastructure securities, mainly in the regulated and user-demand infrastructure segments. The aim is to generate a return characterised by a strong, defensive yield element plus potential for material capital gains. Currency is hedged.
Merrill Lynch Global Allocation Fund Class D	0.20%	The Fund aims to maximise total returns while managing risk and is generally diversified across markets, industries and issuers. In selecting equity investments, a value-style approach is taken in selecting equity investments. The Fund may also buy fixed-income securities.
Perpetual's Wholesale Ethical SRI Fund	1.18%	Invests in quality Australian shares of socially responsible companies. The manager has an opportunistic approach, with strategy biased toward value style, which can swing to having a growth exposure in periods where growth companies offer compelling value.
Platinum Asia Fund	1.54%	The manager focuses on absolute return, aiming to add value using all sources of returns from stock, industry, country and currency. Stock selection is guided by thematic drivers supported by intensive bottom-up analysis. Short-selling is also utilised to enhance return.
Premium China Fund	1.88%	Managed by Value Partners Limited, the Fund aims to provide long-term capital growth exceeding the MSCI China Free Index (HKD). The Fund seeks to identify undervalued securities that will benefit from the upside correction. Currency risk is largely un-hedged.

Source: Aegis Equities Research/PIML

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## 4. Performance Analytics

### Managed Funds' Historical Performance

Figure 2 presents the historical performance of the Funds included on the investment menu. A risk analysis has been performed for a five-year period or since inception for Funds commenced after 31 January 2003. All performance is post-tax and net of ongoing fees.

Most Funds in the menu recorded a single-digit or negative one-year return ending 31 January 2008. This can largely be explained by the sharp drop in share prices across equities markets and the listed property sector in January 2008. For the same one-year period, only three of the twenty Funds achieved double-digit returns, namely Colonial FS W'sale Global Resources Fund, Platinum Asia Fund, and Premium China Fund. All three Funds have very specific underlying investment and benefited from the significant growth in their targeted sectors and regions.

Performance across the funds of a particular asset class have varied significantly. This reinforces the point that investors should give careful consideration to the selection of the underlying fund.

Figure 2. Managed Funds' Historical Performance to 31 January 2008

Fund	Fund Inception	Annual Returns			Risk>Returns	
		1 Yr (%)	3 Yr (%)	5 Yr (%)	Std. Dev. (% p.a.)	Sharpe Ratio*
<b>Australian Equities</b>						
Ausbil Australian Active Equity Fund	Jul-97	2.77	17.84	22.56	12.96	1.31
Ausbil Australian Emerging Leaders Fund	May-02	4.74	17.44	27.28	14.64	1.48
Challenger W'sale Australian Share Fund	Oct-94	-2.13	13.35	18.66	11.87	1.10
Perpetual's W'sale Australian Fund	Feb-97	1.66	14.58	19.53	10.84	1.29
Schroder W'sale Australian Equity Fund	Jul-02	-0.65	15.97	18.59	16.56	0.78
Vanguard Australian Shares Index Fund	Jun-97	1.28	15.58	18.39	11.21	1.14
<b>Global Equities</b>						
AXA W'sale Global Equity Value Fund	Nov-01	-17.37	7.64	9.61	11.71	0.34
DWS Global Equity Thematic Fund	Oct-96	-15.82	11.51	9.55	11.56	0.34
GVI Global Industrial Share Fund	Feb-05	-2.94	n/a	n/a	9.42	0.63
Perpetual's W'sale Int'l Share Fund	Apr-97	-16.37	2.52	5.76	9.75	0.02
T.Rowe Price Global Equity Fund	Sep-06	-7.87	n/a	n/a	15.44	-0.37
Vanguard Int'l Share Index Fund (Hedged)	Jul-00	-4.63	10.91	15.61	12.07	0.83
<b>Specialist Asset Classes</b>						
Aberdeen Asian Opportunities Fund	Oct-03	0.04	17.30	n/a	14.56	0.74
Colonial FS W'sale Global Resources Fund	May-97	30.23	32.27	28.83	14.00	1.66
IOOF/Perennial Global Property Trust	Apr-06	-20.06	n/a	n/a	16.69	-0.35
Macquarie Int'l Infrastructure Securities Trust	Sep-05	6.06	n/a	n/a	9.79	0.87
Merrill Lynch Global Allocation Fund Class D	Jun-05	9.52	n/a	n/a	12.16	0.58
Perpetual's W'sale Ethical SRI Fund	May-02	-1.99	16.16	19.93	13.17	1.09
Platinum Asia Fund	Mar-03	14.65	25.41	n/a	15.47	1.46
Premium China Fund	Oct-05	13.09	n/a	n/a	20.28	1.17

\*Risk-free Benchmark used: average RBA Cash Rate over respective periods.

Source: Aegis Equities Research/van Eyk/PIML/Bloomberg

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The majority of the Funds included in the menu are well established, with a reasonable Fund size and track record. Some have been in existence for more than 10 years and have performed consistently throughout an economic cycle. Volatility (measured by standard deviation) for most Funds remained within 15% p.a.

Investors should note the period since June 2003 has been characterised by generally favourable investment conditions, with equity markets generally increasing and interest rates increasing moderately. However, since the second half of 2007, equities markets across regions (Australian and international) have experienced a higher level of volatility and increased bearish sentiment triggered by the US sub-prime crisis and concerns over financial-sector losses and their flow-on effects on global economies.

This may pose a major threat to the Product, as CPPI structure is inherently “path-dependent” and performance of the underlying investment in the initial stage is crucial to the overall return. Investors also should note historically some of the Funds in the Specialist Asset Classes have established a higher level of volatility, although they may serve to add diversification to the overall portfolio, considering the seven-year term of the Product, and caution should be exercised when allocating a large portion into Funds with high volatility.

### Protected Equity Series I Performance Update

Figure 3 presents the historical performance of all funds issued in the Protected Equity Series 1 (*Series 1*). Series 1 was issued on 19 July 2007. The table presents the performance since the inception of Series 1 of the underlying fund, the Product, the minimum exposure to the underlying fund and the current exposure to the underlying fund.

The table does not include performance data for Series 2 (inception date 21 December 2007). The focus on Series 1 is because there have been two significant market downturns since the inception date, the first of which was shortly after the issue date. In contrast, there has only been one for Series 2. The market environment for Series 1 has been particularly adverse for CPPI-related performance. Figure 3 is provided to highlight the performance risks in such a market environment.

Figure 3. Protected Equity Series 1 Performance (19 July 2007 to 15-Feb 2008)

Fund	Fund Return	PPI Series 1 Return	Participation Rate (29 Feb 2008)	
			Minimum	Current
UBS Australian Share Fund	-11.00%	-9.41%	69.76%	100%
Perpetual's W'sale Australian Share Fund	-11.56%	-14.40%	64.05%	100%
Merrill Lynch Global Allocation Fund – Class D	1.00%	0.43%	100%	100%
T. Rowe Price Global Equity Fund	-8.75%	-9.36%	100%	100%
Colonial FS W'sale Global Resources Fund	5.00%	4.45%	77.86%	100%
Macquarie Int'l Infrastructure Securities Trust	-7.90%	-7.29%	79.54%	100%
Perpetual's W'sale International Share Fund	-14.98%	-14.80%	79%	79%
IOOF/Wholesale Growth Share Fund	-11.60%	-10%	100%	100%
Ausbil Australian Active Equity Fund	-9.48%	-8.10%	58%	100%
PM Capital Absolute Performance Fund	-25.60%	-22.50%	29%	31%
AXA Wholesale Global Equity Fund	-22.90%	-21.40%	39%	41%
Ausbil Australian Emerging Leaders Fund	-10.85%	-16.80%	60%	76%
IOOF/Perennial Wholesale Global Property Trust	-18.30%	-15%	60%	74%

Source: PIML

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In the majority of cases where the underlying fund has generated negative returns, the Product has outperformed the underlying fund. This is a function of the Product being partly exposed to cash through the CPPI rebalancing structure and highlights how the structure can insulate the Product from downward movements in the underlying fund.

Conversely, where the underlying fund has generated positive performance or there has not been a de-leverage event in the Product, the Product has underperformed the underlying. This is due to the impact of fees on the Product.

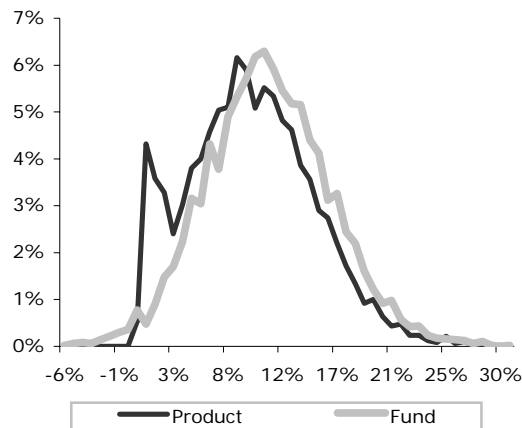
## Expected/Simulated Returns

### Model Parameters

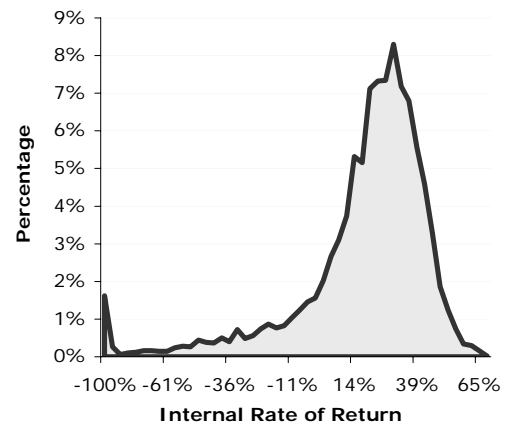
The Monte Carlo analysis below assesses the likelihood of various outcomes in the Product in the context of three market-return scenarios: poor, defined as an average return of 6.5% p.a.; average, defined as an average return of 11.5% p.a.; and good, defined as an average return of 16.5% p.a. A market volatility of 12% is used in all three scenarios, as this level of volatility is broadly consistent with historical averages. Investors should note, however, that volatility levels have increased significantly over the last 9-month period and this heightened level of volatility may persist indefinitely. Volatility is adverse to the performance of CPPI structures.

The data contained in the following analysis have been provided by PIML in relation to the Series 2 structure. Aegis was not privy to the underlying financial model of the Product and, therefore, has not been able to verify the validity of the data independently.

Figure 4. Product Returns – Average Market    Figure 5. Loan Returns – Average Market



Source: PIML



Source: PIML

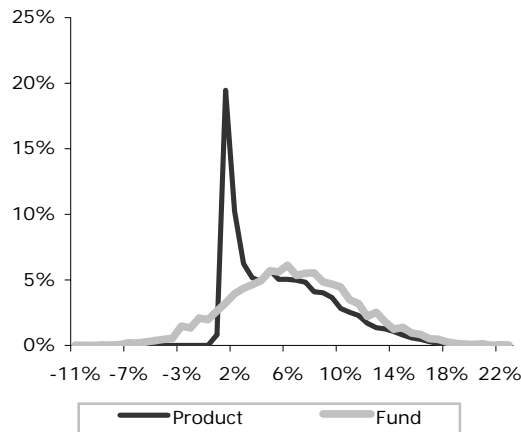
In an average market environment, the mean return for the Product was 9.5% p.a. compared with 11.0% p.a. of the market/Fund. The Product generally underperforms the market/Fund, with the relative benefit of capital protection diminished. In addition, at the lower end of the returns spectrum, the greater distribution of returns in the Product again partly reflects the impact of sell triggers and the consequent compression of returns.

Figure 5 illustrates the distribution of returns for loan investors in such a market environment. The mean return was 17% p.a. It is a clear illustration of increasing returns in an effectively geared investment. In such a market, the mean return of the underlying investment exceeds the after-tax interest costs of the loan.

In a poor market environment (see Figures 6 and 7), the mean return for the Product is 5.2% p.a. compared with 6.2% p.a. of the market/Fund. In this environment, while capital protection safeguards the Product from negative returns, the distribution of returns is weighted to the lower end of the returns spectrum, partly because the sell triggers, by switching the investment into cash-type returns, compress returns relative to the market. While the mean return of the Product is below that of the market, Aegis believes a lower return scenario would generate the opposite outcome, as the Product increasingly benefits from the capital-protection feature.

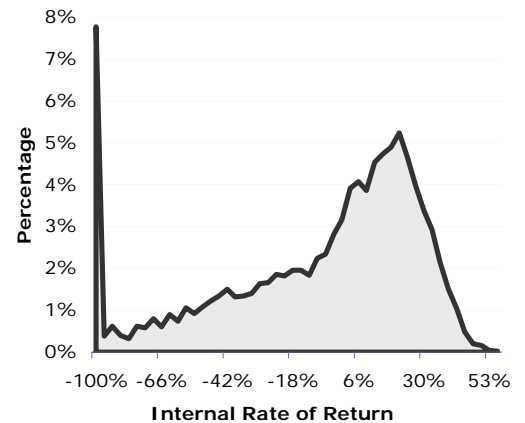
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Figure 6. Product Returns – Poor Market



Source: PIML

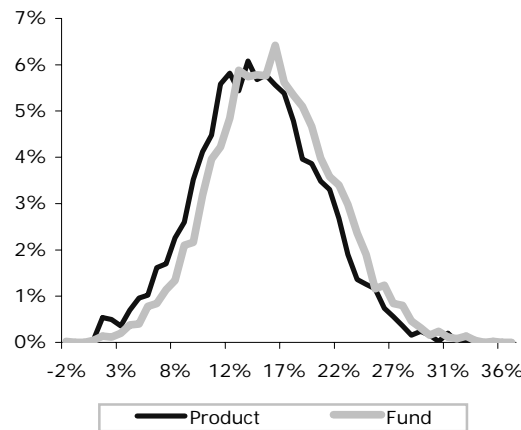
Figure 7. Loan Returns – Poor Market



Source: PIML

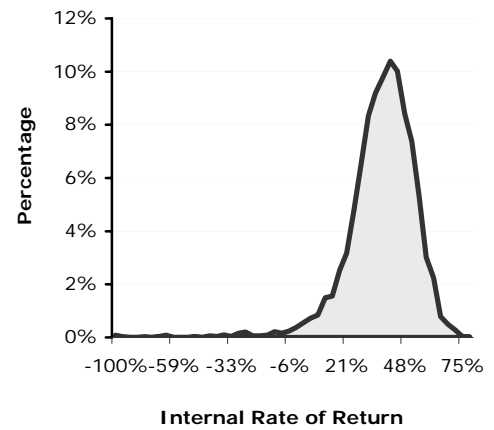
Figure 7 illustrates the distribution of returns in such an environment for loan investors. The mean return is -12% p.a. The chart illustrates that while the Product is protected, losses equal to the cumulative interest costs and income and CGT-related tax costs can be incurred.

Figure 8. Product Returns – Strong Market



Source: PIML

Figure 9. Loan Returns – Strong Market



Source: PIML

In a good market scenario, the Product predictably underperforms the market on account of its fees and there is very little, if any, benefit associated with the capital-protection mechanism.

### Model Assumptions

The Monte Carlo analysis above was based on the following: Loan interest rate 9.20%; Interest type fixed for the term prepaid annually; income yield 4%; Percentage of yield franked 90%; Bond floor discount rate p.a. 6.80%; Investor marginal tax rate 46.50%; Term 7 years; Assumption where no IRR could be calculated -100%.

#### Item:

Income – Income yield from underlying Funds:  
Investment loan interest:  
Interest loan interest (pre-paid options only):  
Loan establishment fee:  
Dynamic management service fee (0.65%):  
Administration fee (0.75% of portfolio value):  
CGT on sale of Units:  
Exercise of Call Options:  
Offsetting of capital gains and losses:

#### Tax Treatment:

Taxable  
100% of prepaid interest is deductible upfront.  
100% of interest incurred is deductible.  
100% deductible over first five years.  
100% deductible as incurred.  
100% deductible as incurred.  
Assumes FIFO, 50% CGT disc., if applicable  
Not a CGT event  
Loss offsetting choices have not been optimised.

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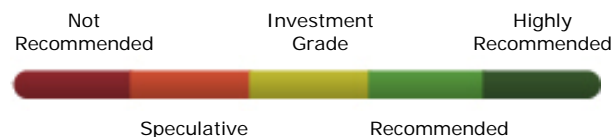
## Appendix – Ratings Process

Aegis has developed a framework for rating investment product offerings in Australia. Our review process gives consideration to a broad number of qualitative and quantitative factors.

Essentially, the evaluation process includes the following key factors: product management and underlying portfolio construction; investment management, product structure, risk management, experience and performance; fees, risks and likely outcomes.

### The Ratings

Our rating is based on the following scale:



**Highly Recommended:** indicates that Aegis believes this is a superior grade product that has exceeded the requirements of our review process across a number of key evaluation parameters and scored exceptionally in a number of categories. It has an attractive risk/return trade-off; however, we caution that the risk/return trade-off will not be suitable for all investors.

**Recommended:** indicates that Aegis believes this is an above average grade product that has exceeded the minimum requirements of our review process across a number of key evaluation parameters. It has an above average risk/return trade-off; however, we caution that the risk/return trade-off will not be suitable for all investors.

**Investment Grade:** indicates that Aegis believes this is a suitable product that has met the aggregate requirements of our review process across a number of key evaluation parameters. The product may provide unique diversification opportunities, but may not stand apart from its peers. It has an acceptable risk/return trade-off; however, we caution that the risk/return trade-off will not be suitable for all investors. In the previous five category rating system, this category was termed 'Approved'.

**Speculative:** indicates that Aegis believes this is a product that has a number of positive attributes; however, there are a number of risks that make investing in this product a speculative proposal. While Aegis does not rule out investing in this product, investors should be very aware of, and be comfortable with, the specific risks. The product may provide unique diversification opportunities; however, concerns over one or more features means that it may not be suitable for most investors.

**Not Recommended:** indicates that Aegis believes that despite the product's merits and attributes, it has failed to meet the minimum aggregate requirements of our review process across a number of key evaluation parameters. However, this does not mean that the product is without merit.

This report has been commissioned, and, as such, Aegis has received a fee for its publication. However, under no circumstances has Aegis been influenced, either directly or indirectly, in making statements and/or recommendations contained in this report.

**The offer of the securities is made in the Perpetual Protected Investments Series 2 Product Disclosure Statement (PDS), and anyone wishing to acquire the securities should complete the application form in the PDS.**

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