



Arafura Pearl Project 2009

INDEPENDENT ASSESSMENT

This report has been prepared for financial advisers only

Scope

Adviser Edge independent assessments are conducted by Barik Pty Ltd trading as Adviser Edge Investment Research (Adviser Edge) which has developed a key industry sector review process that follows a methodology developed specifically for this asset class.

Key Principles

The underlying principles of the assessment process are to:

- identify the long term commercial potential of the project;
- evaluate project management’s capabilities, previous performance in the specific industry and the stability of the organisation;
- evaluate identified markets (domestic and international –existence, stability and growth potential);
- benchmark key performance assumptions and variables against industry and other MIS projects;
- weigh up the relevant risks of the project against projected returns;
- assess project structure and ownership;
- compare and substantiate project fees and expenses;
- determine if the project is structured in such a way as to protect investor’s interests; and
- allow an opinion to be formed regarding the investment quality of the project.

Site Assessment

Adviser Edge conducts a detailed site inspection of the project, meets with all levels of project management and inspects the project’s infrastructure and market accessibility.

The site assessment considers the following areas:

- suitability of the project site for the purpose intended;
- performance of previous project stages located within close proximity to the proposed site;
- management skills, qualifications, capabilities and experience; and
- associated project risks and their management.

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Report Date

8 May 2009.

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Investment Summary

The Arafura Pearl Project 2009 provides investors with the opportunity to become involved in the Australian South Sea pearl industry. Pearls will be produced at Elizabeth Bay, north-west of Nhulunbuy in the Northern Territory, a proven region for cultured South Sea pearl production due to its tropical climate and favourable marine environment.

Established in the Broome region of Western Australia in the late nineteenth century, and later revived in the early 1950s, the cultured pearl industry now reaches across the northern Australian tropics. It is Australia's second most valuable aquaculture export, and was valued at approximately \$314 million in FY2007-08. (Department of Foreign Affairs and Trade)

Arafura Pearls Holdings Ltd (Arafura) is the Responsible Entity (RE) and Project manager for this offer, which represents the fifth Managed Investment Scheme (MIS) offer since FY2004-05. Arafura was established as a partnership in 1998 specifically for the purpose of developing and operating a commercial pearl farm at Elizabeth Bay. Arafura listed on the Australian Securities Exchange in December 2006 (ASX: APB), and is now moving closer to full-size commercial harvests, with approximately 100,000 shells to be harvested in 2009.

Up to 2,350 units (Project Interests) of approximately 100 seeded, hatchery-raised oysters are to be provided by Arafura under this offer. The application fee is \$6,300 (excluding GST) per Project Interest, with investors subsequently liable for deferred management, sales and marketing fees. In addition, investors will be liable for a performance incentive fee should final project returns exceed 16% p.a. on a pre-tax basis, or a fixed Management Fee shortfall if certain sales proceed targets are not met. The investment term is approximately six-and-a-half years.

The independent expert has commented that Arafura's yield estimates appear to be within the collective range for Australian pearl farms employing hatchery shells, qualified experienced technicians and good farm husbandry. Successful pearl production in northern Australia is well established, and has been carried out at the Elizabeth Bay site for more than a decade. While earlier harvests have not met all estimates provided in the Project, the most recent 2008 harvest has confirmed Arafura's ability to produce first harvest pearls to the estimated size.

Environmental factors such as site water quality, storm activity, and pests and diseases have the potential to affect the health of the oysters and the number, size and quality of the pearls produced. Arafura has recently taken measures to insure the mature shell inventory against damage arising from storm activity, environmental pollution, and disease. This policy also

extends to Project shells, and is seen to provide considerable benefit to the offer.

The key markets for Australian South Sea pearls are Hong Kong, Japan, the United States and Switzerland. A large proportion of trade is conducted through Japan in Japanese Yen, and Australian pearl prices consequently vary with exchange rates. Arafura has recently appointed Tim Jones as Manager Sales and Distribution, which will provide Arafura with the flexibility to ensure that the best possible prices are received for the pearls produced.

The potential investment returns from the Project will be affected by a number of performance parameters, with returns expected to be most sensitive to variations in shell sizes and exchange rates. Based on the analysis of the various parameters that contribute to investment returns, Adviser Edge has estimated an indicative pre-tax IRR range of between 2.40% - 23.26%. Using Adviser Edge's investment ratings model, the Arafura Pearl Project 2009 has received a four-star investment rating.

Adviser Edge Rating ★★★★★☆

Project Details

Project Name	Arafura Pearl Project 2009
Product	Australian cultured South Sea Pearls
Responsible Entity	Arafura Pearls Holdings Limited (Arafura)
Operations Manager	Arafura Pearls Holdings Limited (Arafura)

Investment Details

Investment Term	Approximately six-and-a-half years
Unit Size	Project Interest comprised of 405 graded spat and 13 panels
Application Fee (ex-GST)	\$6,300 per Project Interest
Ongoing Fee Structure	Deferred (except insurance)
Minimum Investment	Two Project Interests
Close Date for FY2009	15 June 2009
Investor Finance	12 month interest free Terms Payment
ATO Product Ruling	PR 2009/16

Investor Returns

Potential Investment Returns 2.40% – 23.26% (before tax)

Key Points:

Strengths of the Project

- Arafura is an experienced manager of South Sea pearl farms, managing both investor-owned and company owned shells for over nine years
- The Project has the potential to achieve high returns, provided that yield, quality and price targets are reached
- The quality of the pearls harvested by Arafura and inspected by Adviser Edge has been excellent
- Australian South Sea pearls are a high value commodity, and are in demand for high value jewellery
- Australian production is quota controlled, which assists in ensuring that quality standards are maintained

Weaknesses of the Project

- Pearl farming is inherently risky, being subject to a number of risks including weather and disease. These risks may affect both mortality and quality. However, Arafura has implemented a number of strategies, including insurance, to minimise the impact of these risks
- The Australian pearl farming industry is comprised of a small number of private enterprises, which makes it difficult to obtain independent empirical data on the price, yield and quality assumptions
- The highly specialised nature of pearl farming and use of Arafura's extensive infrastructure means that investors are highly reliant on Arafura to manage the Project for the full term

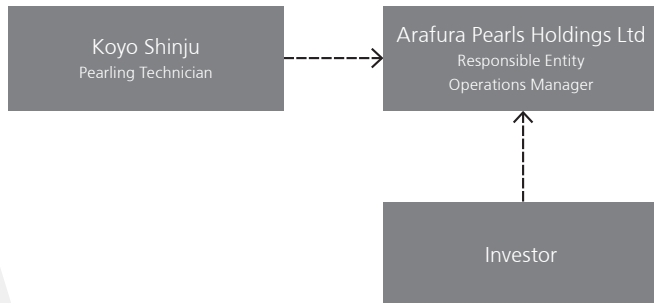
Other Considerations

- The investment is considered illiquid, with no liquid secondary market currently established
- Returns from the Project will be significantly dependent on exchange rates at the time of sale

Investor Suitability

As a general note, investment in agribusiness should represent a balance between the various potential risks and the forecast returns. This project is potentially suitable for investors with a risk tolerant profile and medium-term investment horizon, and as part of a diversified portfolio

Key Counterparties



Arafura Pearls Holdings Limited (Responsible Entity/Operations Manager)

Arafura Pearls Holdings Ltd (Arafura) was established as a partnership in 1998 specifically for the purpose of developing and operating a commercial pearl farming operation north-west of Nhulunbuy on the Gove Peninsula in the Northern Territory. Arafura is listed on the Australian Securities Exchange (ASX Code: APB).

Farming operations are centred on over 500km² of maritime leasehold in Elizabeth Bay, Northern Territory. Elizabeth Bay is located 48km north-west of Nhulunbuy, Northern Territory. A key component of Arafura’s business is an integrated pearl oyster hatchery established in 2001. The company has offices in Darwin for senior operational management, and a corporate head office in Perth, Western Australia.

Arafura has expanded its pearl production capacity in recent years, having increased its initial quota holding of 40,000 shells to 235,000 shells in 2008. Of this quota holding, 140,000 shells are owned by Arafura in its own right.

In June 2007, Arafura entered into a joint venture agreement with Arrow Pearl Co Pty Ltd and associates to manage its pearling operations in Beagle Bay, Western Australia. Beagle Bay has been producing pearls since the early 1980s. The Arrow Pearl farm has a 15,000 shell quota and substantial land and sea infrastructure to manage the company owned cultured pearls.

Board of Directors – Arafura Pearls Holdings Limited

Director	Credentials	Industry	Director
Mark Ceglinski – Non-Executive Chairman	★	★	★
Andrew Hewitt – Chief Executive Officer	★	★	★
Christopher Cleveland – Executive Director	★	★	★
Jeffrey Mews – Non-Executive Director	★	★	★

Key Points:

- Arafura has substantial experience and resources in the Australian pearl industry
- Arafura has taken steps to improve its balance sheet as it moves closer to a full cycle level of production
- Koyo Shinju are considered to be highly experienced pearl technicians. The skill of the individual technicians will have a significant bearing on overall Project performance.

Board of Directors

Adviser Edge believes that the directors of Arafura possess the appropriate experience and credentials to fulfil the company’s role as Responsible Entity.

Corporate governance and compliance

Adviser Edge has reviewed the corporate governance documents supplied by Arafura, including the corporate governance statement, board charter, and corporate code of conduct. Adviser Edge is satisfied that Arafura has adopted appropriate corporate and financial management procedures for a company of its size and nature. However, Adviser Edge would have preferred a separation of roles between the Responsible Entity and the Project manager.

Financial performance

Key financial data* – As at 30 June		
Financial Profitability	2008	2007
Revenue (\$,000)	6,514	8,445
Net profit (\$,000)	10,960	4,543
Profit margin (%)	168.2	53.8
ROCE (%)	27.5	12.3
ROE (%)	23.6	13.5
Market Measures	2008	2007
EPS (basic/cents)	9	4
P/E Ratio	1.0	4.0
NTA per Share (\$ per share)	0.41	0.30
Financial Liquidity/Solvency	2008	2007
Net working Capital (\$,000)	438.6	6,698.7
Current Ratio	1.07	2.18
Quick Ratio	0.41	1.49
Debt to equity ratio	0.28	0.27
Gearing ¹	22%	21%
Interest Cover	40.78	25.79

Source: Arafura Financial Report 2008.

¹ Gearing is calculated as Total Liabilities/Total Assets.

Arafura had a mixed year in FY2008, with a fall in net profit as a result of lower MIS sales, down to \$4.5 million from \$9.8 million in FY2007. However, Arafura uses MIS as a form of financing rather than as a source of recurrent income, with a target of becoming self-sufficient from its pearling operations. As a consequence, its MIS sales result is not considered to be a critical component of the company's long-term financial performance.

Although Arafura's share price has significantly deteriorated over FY2008 as a result of its short-term cash requirements and general equity market conditions, Arafura has moved to stabilise its cash flow position through a \$4.8 million rights issue in 2009. Having secured its immediate cash flow needs to complete the current harvest, Arafura expects to be able to meet its on-going operational and capital expenditure requirements through revenue from annual pearl harvests and MIS raisings in respect of this Project.

The increase in net profit in FY2008 is a result of an increased valuation of the market value of pearls owned by Arafura, which reflects the expected future cash flow following the pearl harvest. In addition to this, Arafura's strategy of using minimal debt to fund expansion activities has kept fixed costs relatively low.

Adviser Edge expects MIS sales in FY2009 will be important for Arafura's short-term cash needs. However, the company will become less reliant on MIS sales in future years, as the cash flow from harvested pearls is expected to substantially increase. Arafura expects to harvest approximately 100,000 shells in September 2009.

Although Arafura continues to be reliant on MIS sales to sustain cash flow, Adviser Edge believes that Arafura will successfully shift its earnings towards pearl production and sales in the medium-term. While there is a risk that the company's MIS sales may not reach expectations, Arafura has a number of avenues to secure short-term funding, which have been successfully accessed in the past.

MIS Capital Raising History – Arafura

Project Name	Financial Year	Capital Raised (\$ million)
Arafura Pearl Farms 2005	2005	0.9
Arafura Pearl Project 2006	2006	4.6
Arafura Pearl Project 2007	2007	9.8
Arafura Pearl Project 2008	2008	4.5
TOTAL		\$19.8

Operational Management

Arafura will be responsible for the propagation of pearl oysters and their management and harvest over the Project term. Arafura has developed the necessary infrastructure and relationships for a modern pearl production and marketing operation. The company operates a regional office in Darwin that serves as an administrative base for senior operations management, while the head office in Perth fulfils Arafura's corporate requirements.

Assets relevant to operations include a fleet of service vessels and a permanent land base at Elizabeth Bay, which also incorporates a pearl hatchery operation. Arafura has recently commissioned a new pearling mothership, *Aracat*. Arafura also has ongoing research and development programs in areas such as the genetic tracking of hatchery broodstock and aspects of the grow-out process. These programs are aimed at improving both the quality and productivity of its operations.

Key Operational Personnel

Key Personnel	Credentials	Industry	MIS
Captain Chris Cleveland – Executive Director and Pearling Advisor	★	★	★
Colin Watts – General Manager Operations	★	★	
Tim Jones – Manager Sales and Distribution	★	★	
Juan Carlos Gutierrez Serrano – Hatchery Manager	★	★	★

Adviser Edge believes that Arafura's operational management personnel are suitably qualified and experienced to meet Project objectives.

Executive Director, Captain Chris Cleveland joined Arafura in 2005 and provides valuable management oversight to Arafura's operations. Chris periodically conducts site visits and reports directly to the board. Chris has extensive pearling industry experience, having formerly held the position of General Manager of Operations for Australia's two largest South Sea pearl producers, Paspaley and MG Kailis. Chris also serves as a member nominee on the NT Pearling Industry Advisory Committee and represents Arafura on industry matters.

Colin Watts was promoted to General Manager of Operations in August 2008, having acted as Project Manager for Arafura Pearls over the past two years. Colin has over 28 years of experience in general management, and is a qualified civil engineer. Colin also has previous experience in the civil earthmoving and the construction and contracting industries.

Tim Jones joined Arafura in October 2008 in the capacity of Manager Sales and Distribution. Prior to joining Arafura, Tim was the Sales and Distribution Manager for MG Kailis, one of the world's largest pearl jewellery brands. Tim also has previous experience in the jewellery business with the sales and marketing arm of DeBeers, one of the largest diamond trading companies in the world. Tim has an honours degree in Archaeology from University College, London.

Juan Carlos Gutierrez Serrano is the Elizabeth Bay hatchery manager. Juan is a qualified marine biologist with a Masters degree in Aquaculture from Deakin University. Juan has had over five years' experience in hatchery operations prior to joining Arafura in 2006, and has capably managed the growth in Arafura's hatchery production, which is required to service its rapidly expanding operations.

Key Counterparties

Key Counterparties		
Company	Role	Location
Koyo Shinju	Pearling Technician	Wagu, Japan

Arafura formally engaged the experienced Japanese firm Koyo Shinju in 2006 to perform the specialised oyster seeding and harvest operations for a 10-year period. Koyo Shinju is an integrated Japanese pearling firm with capabilities ranging from technical consulting to the management of their own pearl farming, grading and marketing operations. Based in Wagu in the Japanese province of Shima, the company employs approximately 50–60 staff and has been involved with Australian South Sea Pearl production for over 40 years.

Koyo Shinju's employees are considered to be highly experienced and suitable pearl technicians for the Project. It is also pleasing to see Arafura's adoption of management strategies that match seeded pearls with individual pearl technicians. This process helps to ensure that mortality rates and the size of implanted nuclei are not compromised in the interests of efficiency.

Independent Expert

Independent Expert		
Focus	Company	Responsible Person
Pearl production	Serena Sanders	Serenidae Pty Ltd

Arafura has engaged Serena Sanders of Serenidae Pty Ltd to provide an assessment of Arafura's production practices and productivity estimates. Serena has over 20 years of involvement in the pearl industry in senior management and external

consulting roles, and holds a Bachelor of Science (Marine Biology/Zoology) degree with honours.

The independent expert is considered suitably qualified to undertake her assigned reporting role under the offer.

Investment Specifications

Target subscription	2,350 Project Interests
Location	Elizabeth Bay, Northern Territory
Unit size	405 graded spat plus 13 panels
Minimum application	Two Project Interests
Project asset ownership	Ownership of panels oysters
Liquidity	Illiquid – no established secondary market
Insurance	Compulsory
Investor finance provider	Not provided

Arafura is giving investors the opportunity to participate in the Australian pearling industry through the offer of 2,350 units (Project Interests) in the Arafura Pearl Project 2009, with provision for oversubscriptions subject to quota restrictions.

The Project pearl farm is located on a marine leasehold covering 500km² at Elizabeth Bay, near Nhulunbuy off the northwest coast of the Northern Territory. This lease was established in 1998 with the Northern Land Council (NLC). The lease expires on 3 September 2018, with a 10-year renewal option.

Investors are required to purchase a minimum of two Project Interests, each initially comprised of 405 selected spat (settled pearl oyster larvae). Arafura has provided a guarantee that it will replace any spat necessary to ensure that 18 months after the project commencement there are at least 177 viable pearl oysters available per Project Interest. This guarantee has been calculated to accommodate the selection and seeding of 159 pearl oysters. After accounting for post-operative oyster mortalities and seed rejections, Arafura intends to make available 100 healthy seeded oysters to meet quota limits.

Project structure and agreements

When investors are accepted into the Project, they will be bound by a number of legal agreements that outline the rights and responsibilities of each party involved in the investment scheme. These agreements are outlined in the Project's Product Disclosure Statement (PDS). It is recommended that each potential investor and their adviser read and understand the Project agreements to ensure that the Project is suitable for the investors needs.

Fee Schedule

The fees outlined in the following tables relate to an investment made on or before 15 June 2009. Fees may vary depending on the date of application.

Key Points:

- All ongoing fees (except insurance) are deferred until harvest
- The Project term is approximately six-and-a-half years
- Arafura has incentive to maximise returns through management and marketing fees linked to proceeds
- The technical and specialised nature of pearl farming, means the Project is significantly reliant on Arafura

Initial cost to the investor

Schedule of initial fees (ex GST)*

Payment Type	Cost per Project Interest
Application Fee	\$6,300

Ongoing cost to the investor

Schedule of ongoing fees (ex GST) (per Project Interest)

Fee	Cost
Deferred Management Fee	30% of gross pearl sales proceeds ¹
Sales and Marketing Fee	10% of gross pearl sales proceeds ¹
Deferred Management Fee Shortfall	Up to a maximum of \$5,900 ²
Bonus	10% of the amount that exceeds the benchmark ³
Insurance	Estimated to be 1.5% of agreed value per annum ⁴

¹ Gross pearl sales proceeds means the proceeds received through the sale of polished and/or further improved pearls.

² This fee is only payable in the event that the sales and marketing fee and the deferred marketing fee do not exceed specified amounts. The actual amount payable will depend on the amount of the shortfall, the number of years remaining on the Project term, and the number of oysters lost if the Management Agreement is terminated or there are significant losses to grower oysters.

³ The benchmark is the amount of harvest proceeds, less all applicable costs and expenses, that must be paid on final harvest to provide an investor with a before-tax internal rate of return of 16%.

⁴ Estimated to be 1.5% of the agreed value of seeded shells.

Ongoing fees are deferred and include a management fee and sales and marketing fee. Fees are calculated as a proportion of gross pearl sales proceeds and deducted prior to any distribution being made to investors.

If the sum of deferred fees is less than the prescribed shortfall amount of \$5,900 (excluding GST) per Project Interest at the conclusion of the Project, investors will be invoiced for the difference.

Bonus

Arafura is entitled to a performance incentive fee equal to 10% of any amount by which each Project Interest exceeds a pre-tax IRR of 16% p.a. at the completion of the Project term.

Shell insurance

Under the terms of the Management Agreement, Arafura is required to use all reasonable endeavours to arrange insurance of Project oysters on behalf of investors. Arafura has indicated that it has obtained quotes to insure mature shells against the risk of damage arising from storm activity, environmental pollution, and disease.

Adviser Edge believes that the use of insurance to protect against insurable production risks should be part of a comprehensive risk management strategy whenever economically feasible. Arafura has recently taken measures to insure its entire shell inventory under the aforementioned policy to mitigate the risks of extreme climatic events and a range of other events. This policy also applies to Project shells and is seen to provide considerable benefit to the offer.

Where insurance cover is maintained, Arafura has agreed to share some of the estimated cost of insurance premiums under the policy. This annual cost will be limited to 1.5% of the agreed value of seeded shells prescribed under the policy, and acts to reduce the financial impact of the cover on investment returns.

Fee Analysis

With any MIS project, the application fee is generally dictated by the actual development cost incurred in establishing and managing the Project, other administration costs such as corporate overheads, marketing and PDS development expenses, and the profit margin taken by the Project manager.

The total application fee for the Project has increased by 1.6% on the previous year. Due to the limited availability of third party information on pearl farming, it is difficult to assess the reasonableness of the fees payable. Arafura has provided a financial model that estimates the costs and expenses associated with managing the Project. This model provides incentives for Arafura to ensure good outcomes for investors, while also taking on substantial risk in relation to the costs of growing out and managing the Project.

Having given due consideration to the information provided to Adviser Edge and the intellectual property made available to investors in the Project, Adviser Edge considers the fees charged to investors to be reasonable.

Risk apportionment

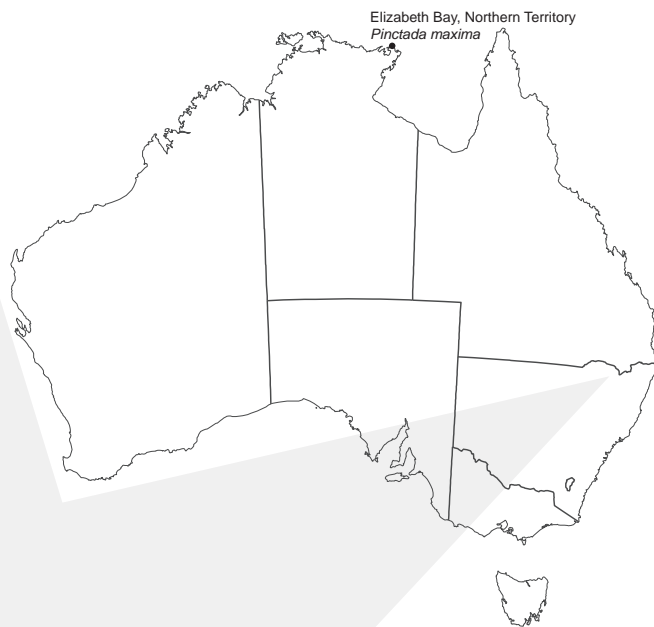
Risk apportionment refers to the level of risk the Project Manager/RE shares with investors as a consequence of the Project fee structure. When ongoing Project fees are deferred and linked to harvest proceeds, the level of risk sharing between investors and the Project manager is more evenly aligned.

The fee structure provides incentives for Arafura to achieve the best outcomes for the Project through the deferred management fee and the sales and marketing fee.

Additional Information**Taxation advice**

The Project has been issued a product ruling PR 2009/16, which provides certainty in relation to the taxation consequences of investing in the Project.

Adviser Edge does not conduct detailed analysis on the implications of the Project's Product Ruling, and it is advised that investors seek appropriate professional advice in relation to the full financial and taxation implications of their investment.



Adviser Edge has not conducted a site inspection to Elizabeth Bay in 2009 due to time and weather constraints. Adviser Edge intends to undertake a site inspection in the near future to review the progress made by Arafura. The information contained in this section was prepared after the site inspection conducted on 7 and 8 September 2007.

Region

The Nhulunbuy region is located in Arnhem Land, which is under the stewardship of its traditional Aboriginal owners. The development of economic activities such as mining and aquaculture in the area is tightly regulated by the Northern Land Council (NLC), which was established in 1973 to represent the interests of the traditional Aboriginal landowners. (NLC 2003) The process of obtaining permission for a commercial enterprise in the region is complicated, requiring approval by the NLC and also consent from the Minister for Aboriginal and Torres Strait Island Affairs for terms exceeding ten years.

Also located at Nhulunbuy is Rio Tinto's multi-billion dollar bauxite operation. As the primary source of employment and income in the region, the operation has a positive effect on the local economy and maintains a high level of infrastructure in the region. Rio Tinto and its predecessor Alcan's both have a strong environmental record at the site, including ISO 14001 accreditation. This suggests that the risk that Rio Tinto may pose to Arafura's operations is low. That said, the operation does generate a high volume of shipping activity that poses a potential risk of marine contamination from the ballast water of ships, which originates from all over the world.

Climate

At approximately 12° latitude, the Nhulunbuy region experiences tropical weather patterns. Climate data from the Australian

Key Points:

- Adviser Edge's last site inspection of Arafura's operations was carried out in September 2007
- Koyo Shinju conduct the seeding and harvesting operations
- The location of the Project is ideally suited to pearl farming, although cyclones remain a risk to the Project
- Arafura has made significant investment into infrastructure and equipment at its operations

Bureau of Meteorology's (BOM) nearest observation point to Nhulunbuy (Gove) was assessed to evaluate regional climatic conditions. From December to April the region encounters heavy rainfall with monthly averages exceeding 195mm. Average temperature data for the region reflects relatively stable maximum and minimum temperatures, with annual averages of 30.7°C and 23.2°C respectively. (BOM 2007) This climate is recognised as being well suited to the production of cultured pearls.

Nhulunbuy's location also makes it susceptible to tropical cyclones, which can occur in northern Australia from November through to April. Since records began in 1948, 12 cyclones have been reported in the Nhulunbuy region. These have occurred every four to seven years, with the exception of a 15-year hiatus between December 1981 and March 2003.

While the area surrounding Nhulunbuy has remained relatively free from tropical cyclone activity over recent decades, Tropical Cyclone Ingrid in March 2005 and Tropical Cyclone Monica in April 2006 caused widespread damage across northern Australia. Cyclone Monica largely avoided Elizabeth Bay, however cyclone Ingrid seriously affected Arafura's operations, resulting in significant asset damage and loss of stock.

In addition to employing various management practices and systems to mitigate the risk of storm activity, Arafura has obtained quotes to insure mature shell against the risk of significant damage caused by storm activity and environmental damage, excluding that arising from disease contamination.

Site selection

Arafura's Elizabeth Bay operation is situated on the north-east tip of the Northern Territory, approximately 48km north of Nhulunbuy. The Elizabeth Bay site was identified for pearl production in the mid 1990s by pre-eminent marine biologist and *Pinctada maxima* expert, Dr Robert Rose. In the late 1990s, Arafura conducted ecological and environmental surveys

on the site, which indicated that tidal flow, water exchange and plankton levels were suitable for South Sea pearl production.

Following the positive findings of these surveys, the company successfully negotiated a lease agreement with the Arnhem Land Aboriginal Land Trust and the NLC in 1998, extending rights to over 500km² in and around Elizabeth Bay for the sole purpose of pearl production. The lease term is 20 years expiring on 3 September 2018, with a 10-year renewal option.

While Arafura has assumed control of a secondary site in Beagle Bay, WA, all Project shell associated with the offer will be produced out of Arafura's Elizabeth Bay operations. That said, the Beagle Bay operations may provide an alternative source of mature virgin shell should the grow-out process at Elizabeth Bay fail to produce sufficient quantities of quality shell for seeding, subject to quarantine restrictions.

Species

Pinctada maxima, commonly known as the silver lip oyster, will be used as the host pearl oyster variety. This species, which produces the South Sea Pearl, occurs naturally in Western Australia and the Northern Territory, and has been farmed in these regions for over four decades.

Hatchery-bred *Pinctada maxima* shells will be used for the Project, sourced from Arafura's own hatchery operations located at Elizabeth Bay. Arafura's hatchery has produced commercial spat since 2001 and forecasts production of 900,000 selected spat in the 2007-08 season. Arafura has indicated that its hatchery is one of the most advanced in Australia and has the capacity to produce spat numbers well in excess of its requirements. At the time of the visit hatchery management was preparing the facility for the first spawning of the new season.

Cultured pearl production

The oyster shell production process from hatchery rearing to seeding usually takes between 18 to 24 months. Hatchery rearing involves the culture of larvae and newly settled small juveniles (spat) inside a controlled environment. (Rose 2003) Following an on-shore nursery phase lasting two to three weeks, spat are placed in an ocean nursery for a period of 10 to 12 weeks before undergoing selection and grading according to potential viability.

Juvenile oysters must experience a grow-out phase, which occurs in the ocean and can last up to 15 months. During this period, the oysters are placed in 30-pocket netted panels and attached to long lines suspended by buoys that are anchored to the sea floor. Each line is approximately 100m long and holds 100 panels, spaced at 1m between panels and submerged approximately 2m below the ocean surface.

The pearl cultivation process begins with the seeding of the virgin shell. Technicians from the Japanese company Koyo Shinju will perform the delicate seeding operation on Project oysters. The technician makes a small incision in the gonad of the oyster in which they graft a nucleus and a piece of mantle tissue from another oyster. Post operation, the shells are placed in panels and rested in sites on the ocean floor for a period of around two weeks, with divers turning the panels every two days. Following the resting period, each panel (typically holding six seeded shells) is placed back into long lines.

Seeded shells are cleaned every three to six weeks, and where appropriate a representative sample may be x-rayed to determine whether the nucleus has been retained. The first pearl harvest takes place 18 to 24 months after seeding. Shells that are determined to be in adequate health following the first harvest are reseeded with a larger nucleus and the process continues.

The independent expert has indicated that the management techniques and procedures used on the existing farm are well developed and based on methods used on other well run Australian and South East Asian pearl farms.

During the visit Adviser Edge also took the opportunity to view the condition of oysters at various stages of development. Oysters in eight-pocket panels associated with the 2005 wholesale offer appeared to be in good condition and of an encouraging size, with approximately 10 months of development remaining prior to seeding in 2008. A sample of younger oysters in 15-pocket panels associated with the 2006 project offer also appeared to be in good condition, showing good mantle extension and marine weed and pest control. Some experimentation had been conducted by placing oysters immediately into eight-pocket panels following the grow out process, with the aim of reducing handling and the disruption to shells during such transfer operations. Arafura has indicated that this approach has shown good results thus far.

A sample of juvenile oysters in 30-pocket panels associated with the 2007 Project offer had commenced the grow-out process following a successful spawning season in 2006-07. These oysters appeared to be showing greater variability as would be expected prior to culling. However, shell cleaning did not appear to have been as vigilant in this instance. Proficient shell cleaning is essential in promoting oyster feeding and health at such a vulnerable stage, and the independent expert has noted that rotations were slightly behind schedule due to a delay in deploying new cleaning boats.

Project infrastructure

Land-based infrastructure at the Elizabeth Bay base appeared well resourced. This included the hatchery and laboratory, office and workshop facilities, staff quarters, mess hall and recreation

hall. An on-site power generator provides electricity, and the base is connected by a satellite communications system. An additional \$200,000 worth of development, including more accommodation and a new septic system, will be under construction during the coming year.

Arafura has a well-maintained fleet of boats at its disposal, including a 32-metre mothership, several cleaning boats, dive boats, and work boats. Capital investment in supporting infrastructure has increased in line with general maintenance requirements and expansion plans. On the preceding visit in February 2007, Adviser Edge visited the Darwin shipyard where a contractor was in the process of building three new cleaning boats for the company at a cost of approximately \$150,000 each. These craft have been specially designed in consultation with Arafura, and are expected to deliver superior performance and reliability to existing boats. Sea trials for the first new cleaning boat were underway at the time of the visit and a larger mother ship, *Aracat*, has recently been commissioned with Arafura taking delivery in early 2009. The larger mothership reduces downtime, as staff can remain on boat during pearling operations.

Operational capabilities

Strong ties to the Thursday Island community provide a ready source of capable workers, and the size of the Australian pearling industry should also provide access to a well-trained and compatible workforce. Arafura also has a strong relationship with local Aboriginal elders, which is an important consideration in avoiding unnecessary disruptions and in maintaining the company's lease agreement.

Arafura is currently undertaking four separate research and development programs (R&D), which it has funded in conjunction with rebates available through the Australian government agency AusIndustry. These programs are focused on varying stages of the production cycle, with subjects including grow-out practices, genetic tracking of brood stock and post-operative care. The company has also entered into an R&D joint venture seeking to gain a detailed understanding of how the oyster genetically controls bio-fabrication. It is hoped that this information can be used to identify pearl oysters that are a source of high quality donor mantle tissue, which can then be applied in Arafura's hatchery program.

Maintaining an environment free of pollution is key to maximising the productivity of a pearl farm, as polluted water can detrimentally affect oyster health as well as pearl size and quality. Arafura has implemented an Environmental Management Plan, which identifies potential environmental impacts associated with its pearl farming operations and outlines management practices and procedures designed to

minimise their effects. Given the sensitive nature of the project site, this represents a critical risk management strategy.

Operations systems are continually being revised to satisfy regulatory requirements and provide for greater traceability throughout the production process with the aim of advancing understanding of the site and genetic stock. Prior to the appointment of Pearling Adviser Chris Cleveland, no water nutrient level monitoring and recording procedures were in place. Chris Cleveland has suggested such a program, in addition to monitoring of ocean temperature, salinity and pH in order to better understand the operating environment.

Pearl oysters are also susceptible to a range of diseases, with the health of the shell continually monitored throughout the cleaning cycle. In addition to this, the Aquatic Pest Management Unit (APMU) operated by the Northern Territory Fisheries department continually monitors marine pests. Arafura and the APMU had not identified any uncontrolled marine pests in the Nhulunbuy area at the time of writing.

Harvesting

Japanese pearl oyster technicians Koyo Shinju have been engaged to undertake the Project's harvesting operations. These will be carried out between June and August each year. Arafura's general manager, in consultation with Koyo Shinju, will determine the most appropriate time to commence the pearl harvest. Koyo Shinju is well qualified to undertake this role within the project, and Arafura strengthened this important counterparty relationship in 2006 via the negotiation of a 10-year agreement for Koyo Shinju to provide technical services to Arafura.

At the time of the visit, Arafura was completing its seventh harvest and oyster seeding operations with the aid of external technicians Koyo Shinju. Pearls were being harvested from various locations within the lease and provided the first opportunity for Arafura to assess product quality from oysters farmed at newly explored reaches such as Cotton Island, as well as the first product that was seeded by Koyo Shinju. This time is the busiest period during the year. It places significant demands on permanent staff and requires a large influx of seasonal labour.

Pearls were being harvested on the mother ship and the oysters re-seeded depending on the quality of the harvested pearl. Care was taken to ensure pearls were segregated according to the location where they were grown and the age of the donor oyster prior to being transported to the Elizabeth Bay base where a sorting and preliminary grading room had been constructed. Upon inspection in the grading room the pearls were naturally variable in size, shape, colour and lustre but were generally considered to be of a good standard relative to previous years.

Market Overview

Product type	Australian South Sea pearls
Primary use	Jewellery
Key target market	Domestic and export
Major competitors	Paspaley Pearls and other South Sea pearl producers

Marketing strategy

The Project pearls are expected to undergo polishing and sorting to improve marketability. After loose pearl valuation, a portion of the Project pearls are expected to be set aside for value adding opportunities, such as matching and stranding of pearls, which can carry a premium to loose single pearl lots.

Arafura has recently appointed Tim Jones as Manager of Sales and Distribution to manage the sales and marketing of the pearls produced as part of the Project. Tim has substantial experience in the sales and marketing of loose pearls, pearl jewellery and uncut diamonds, having previously worked for the MG Kailis Group and DeBeers.

Arafura's sales and marketing strategy has become more flexible with the appointment of Tim Jones. Arafura now intends to market the pearls using a combination of internal marketing and the use of external sales. The pearls are expected to be marketed locally and overseas in the major South Sea pearl markets of Japan, Hong Kong, Europe and the United States.

Arafura expects that value adding and a flexible sales and distribution strategy will result in higher prices for investors in the Project when compared to relying on a single independent third party agent. Arafura has advised that it will be compensated for the value adding and sales and marketing activities undertaken on behalf of investors by the sales and marketing fee under the Project agreements.

Adviser Edge considers the marketing strategy adopted by Arafura to be sound. By establishing internal marketing capabilities, Arafura is well placed to maximise grower returns.

Market overview

Japan is the largest importer of both natural and cultured pearls, importing just over 32% of total world imports in 2006, valued at an estimated US\$380 million. Other major importers include Hong Kong (26%), the United States (26%) and Australia (11%). The largest destinations for Australian produced pearls, in order of export value, are Hong Kong, Japan and the United States.

Hong Kong is the world's largest exporter of pearls responsible for over 34% of world exports in 2006, valued at an estimated US\$405 million. Hong Kong is followed by Japan (23%), Australia

Key Points:

- Arafura has established internal sales and marketing capabilities
- Australia is recognised as the highest quality producer of South Sea pearls
- The major destinations for Australian South Sea pearls are Hong Kong, Japan and the United States

(21%) and China (12%). (UN Comtrade 2008) Hong Kong is predominantly a re-exporter of value-added pearls, whereas Japan, Australia and China are both producers and exporters. The largest exporter of unimproved cultured pearls is French Polynesia, exporting over \$110 million of product in 2006.

The Australian pearl industry exports are valued at approximately \$314 million. (Department of Foreign Affairs and Trade, 2008) This accounts for approximately 93% if all non-edible fisheries products. (ABARE 2008) Japan, the United States, Hong Kong, France and Switzerland rank as Australia's major markets, with the majority of trade conducted in Japanese Yen. Consequently, Australian pearl receipts vary with the value of the Australian Dollar/Japanese Yen exchange rate.

South Sea pearl production is also common throughout South East Asia, with large industries now established in Indonesia and the Philippines. While neither of these countries possesses the same reputation for quality that the Australian industry has fostered over many decades, they have had a significant impact on world supply. In recent years the market for Australian South Sea pearls has experienced a downturn, due largely to mounting global inventories arising from the export of hatchery and farming technologies to developing countries. A steady appreciation in the Australian Dollar in recent years, as well as the broader global financial crisis, has also affected the Australian South Sea pearl market.

Market outlook

The value of Australian pearl exports fell by 22% in 2007, compared to an 11% decrease in the volume of trade. (DFAT 2008) Adviser Edge has conducted an analysis of approximate price data for improved cultured pearls, generated from DFAT data compiled between 1997 and 2007. This analysis demonstrated a marked decrease in the market value of pearl exports since 2002. This period coincides with a strong increase in traded volumes and the value of the Australian dollar. There also appears to have been a transition from exporting predominantly unimproved pearls to worked pearls over the period.

The significant price decline experienced for the entire pearl category early this decade (i.e. including freshwater, South Sea and Tahitian pearls), was in response to a rapid increase in global

pearl production. Prices now appear to have stabilised somewhat as the market responds to lower production forecasts and more restrained production growth in Indonesia. Chinese production of freshwater pearls, a low quality pearl, stabilised during 2007 and accounted for almost 20% of global pearl trade in 2007. The growth in Chinese pearl production has caused a flood in supply of low quality pearls, although this has contributed to renewed popularity in pearls as a jewellery accessory.

The supply of Australian South Sea pearls is restricted by production quota licences issued by the Western Australia and Northern Territory governments. In addition to this, the RE and the Paspaley Group now control approximately 80% of Australia's total quota, either directly or indirectly. This structure gives some stability to the supply side of the market, as production can be controlled to a large extent (Jewellery Net Asia 2007).

The United States market represents an important future demand growth driver for Australian South Sea pearls, due to the relatively large size of the market. Some encouraging demand trends have emerged, with pearls estimated to have increased their share in the overall United States jewellery market from 3% to 6% in the three years to 2006, in response to lower market prices. (Jewellery Net Asia 2007) Emerging markets also hold significant potential for Australian South Sea pearl producers as consumer affluence expands in developing nations such as China and India in response to strong economic growth.

The global financial crisis that started in late 2007 represents a risk to consumer demand in many key markets for Australian South Sea pearls. While it is too early to judge the potential severity of the current downturn, many economic commentators are predicting below average growth in economies such as the United States, the European Union and Japan over the near to medium-term. Balancing the expected weakness in demand is a depreciation in the Australian dollar against the Yen and the US dollar, although it should be noted that the currencies of other key South Sea pearl export countries, the Indonesian rupiah and the Philippine peso, have also depreciated against the Yen and the US dollar.

The following section provides a discussion of the key project parameters that directly affect the performance of the investment.

Pearl Yield and Quality

Project Year	Arafura %
First harvest mortality rate [^] (% of seeded shells)	24%
Second harvest mortality rate [^] (% of seeded shells)	12%
Saleable shells (% of harvest)	80%
First harvest average size (momme/piece)	0.72
Second harvest average size (momme/piece)	1.20

Source: Arafura, 2009.

[^] Survival rate refers to the number of pearls harvested from confirmed seeded shells.

Yield

The lower mortality rate, increased proportion of harvestable shell, higher average pearl weight, and higher proportion of marketable pearls assumed in the second harvest is due to the larger oyster size and proven compatibility of the oysters to cultured pearl production.

The quality of farm management will have a strong bearing on yield outcomes over the Project term, influenced by factors such as the average size of shell seeded following the grow-out stage, size of the nuclei inserted into the shells, the timeliness of shell cleaning operations, and the proficiency of seeding and harvesting operations. These factors will have a bearing on mortality rates, the size of pearls and nacre growth. Theft is also a risk for such a highly valued product, although the isolation of the farm and regular governmental surveillance of the region for illegal boats should help to mitigate the risk.

Arafura has provided Adviser Edge with empirical production data from its past three harvests to support future yield estimates. The 2008 harvest confirms Arafura's harvest size assumption of 0.72 momme/piece, although it should be noted that the 2006 and 2007 harvests produced smaller pearls. This confirms that the improvement in shell husbandry and site understanding has resulted in significant improvement to pearl quality.

The experience that Arafura has gained since establishing the Elizabeth Bay farm in 1998 is expected to provide a strong foundation for future operations. Continued improvement in production practices, assisted by the agreement forged with highly experienced pearling technicians Koyo Shinju, various research and development initiatives, and the further accumulation of site-specific knowledge, has the potential to provide some upside to historical performance levels. Arafura has indicated that it believes these assumptions are conservative given its knowledge of the industry.

Key Points:

- Given variability of exchange rates and quality, it is difficult to accurately estimate the pearl prices that may be received
- Arafura is intending to value-add to the pearls to provide investors with prices that exceed the prevailing farmgate prices
- Yield and quality will be largely be determined by the size of the shells grown and the skill of the seeding technicians

The independent expert has noted that she believes that the production assumptions appear to be within a feasible range for Australian pearl farms operating hatchery shells and using qualified, experienced technicians and good farm husbandry practices. Critical to the success of the Project will be the skill and expertise of the technicians used to seed the shells, as this will have a bearing on the amount of seed rejection (vomit) and size of nuclei implanted in the shells.

In addition to management related factors, environmental factors such as site water quality (including temperature, nutrient content, tidal activity, and pest and disease loads, amongst others) and storm activity have the potential to affect the health of oysters and the size and quality of pearls produced.

The category five Cyclone Monica in April 2006 did not result in any damage to the pearl farm or the land-based infrastructure, although Cyclone Ingrid in March 2005 did result in the loss of 30% of stock and significant damage to vessels and buildings. However, these events are considered to be exceptional, as there had not been a tropical cyclone greater than category two in the preceding 40 years.

Arafura has attempted to minimise the potential impact of weather related events through the provision of shell insurance, where economically feasible, from the time leading up to the first seeding of project shell, as well as the maintenance of a formal Cyclone Contingency Plan. This plan includes the selection of sheltered sites within the lease and the implementation of a system that enables oyster panels to be lowered to a greater depth in the event of extreme weather conditions. All buildings and land-based infrastructure have been constructed to cyclone proof standards in accordance with local building codes.

The isolated nature of the site, combined with Arafura's Environmental Management Plan, is intended to mitigate the potential for water pollution to threaten project viability. The extensive lease area controlled by Arafura allows for production to be spread into isolated management blocks, which will assist

in controlling the spread of disease and pollutants. This will also provide benefits in the selection of sheltered locations for long-lines.

Arafura maintains an active Disease Management Plan to mitigate the risks of disease, and the condition of the shells are actively monitored during cleaning rotations as well as by the Aquatic Pest Management Unit (APMU), run by the Northern Territory Fisheries department. At the time of writing, Arafura indicated that neither the APMU nor Arafura has identified any unmanageable marine pests in the Nhulunbuy area.

Quality

A typical Australian South Sea pearl harvest will produce a range of pearls of various qualities. Pearl quality is a function of its lustre, complexion, size, shape and colour. The South Sea pearl is typically larger than most other varieties, averaging approximately 13mm in diameter. (WA Department of Fisheries 2006) While there is no direct link between oyster age and pearl quality, larger pearls are generally produced by larger, more mature oysters. Shells selected for repeated operations generally produce better quality pearls, as they have been intentionally selected according to their health and the quality of their previous production.

Australian South Sea pearls are distinct from the Tahitian Black pearl, and are most commonly coloured white, silver, yellow or gold. Spherical shapes are most valuable, although less uniform shapes known as drop, button, oval, and baroque can also attract high prices. The size (diameter and weight) and lustre of a pearl often have the greatest influence on its value, with lustre determined by the uniformity of the nacre layering around the nucleus.

The suitability of the project site, the quality of work received from the seeding and harvesting technicians, and the standard of farm management practices are likely to significantly affect the quality of pearls produced from the Project. Australian South Sea pearls are internationally regarded as being of the highest quality, and Arafura expects the quality of pearls produced by this Project will at least meet industry standards.

The independent expert has commented that analysis of Arafura's previous harvests is consistent with the variability expected from technicians, husbandry methods and site locations. Inspection of the 2008 harvest by Adviser Edge supports this claim.

Past performance

The 2009 Project will be the fifth MIS project issued by Arafura pearls. As a consequence, Arafura does not have any harvest data pertaining to an MIS project, with the 2005 Project expecting its first harvest in calendar year 2009. However, Arafura has provided Adviser Edge with harvest results from

smaller trial harvests, and an investor report for investors in the 2006 and 2007 Projects.

The 2006 and 2007 harvest data has demonstrated the potential for pearl farming in Elizabeth Bay. Average pearl sizes were smaller than the estimates for the 2009 Project, although these resulted from seeding smaller shells, which could only accommodate smaller nuclei. However, the quality of the pearls harvested was good, with annual improvement in shape and colour.

Improved results should be expected for investors in the 2006 and 2007 Projects. The grower report has indicated that the average shell size to be seeded for the 2006 Project has increased by around 10%, to between 110mm and 120mm when compared to the 2005 Project. This will enable the seeding of a nucleus of 2.4bu, compared to an average nucleus size of 2.2bu in the 2005 project. Assuming average nacre growth over the two year growing period, the average sized pearl should increase from between 10mm and 11mm to between 11 and 12mm.

Pearl Price

Project Parameter	Arafura Estimate
Pearl price (JPY/momme)	18,000
Exchange Rate (AUD/JPY)	75

* Source: Arafura, 2009.

Pearl prices achieved by Australian producers depend on a number of variables, most notably average pearl size and quality, global South Sea pearl production, economic growth and consumption trends in key markets, and the AUD/JPY exchange rate. In recent years Australian South Sea pearl prices have suffered from mounting global supplies of internationally produced South Sea pearls and a steadily appreciating Australian dollar. However, due to the larger pearl shells that are native to Australia, the environmental factors and the domestic quota system, the quality of Australian South Sea pearls are considered superior to pearls produced in South East Asia.

In addition to prevailing market fundamentals, prices expressed in Japanese Yen per momme naturally vary according to the size, shape and colour of the pearl. Arafura has provided an average price estimate of ¥18,000 /momme in Project year zero (FY2009), increasing at an estimated rate of 3.0% per annum. Adviser Edge has reviewed Arafura's quality, size and price assumptions, which appear to be broadly in line with the expected price range for the first harvest. An analysis of potential prices for the second harvest, however, suggests that prices estimated by Arafura may be conservative, due to the expected increase in size at the second harvest.

Adviser Edge views Arafura's average pearl price estimate of ¥18,000/momme as appropriate given current market estimates and commentary provided by industry figures. Given the relationship between foreign exchange rates and inflation rates in different countries, Adviser Edge has included a 2.9% increase in line with the BIS Shrapnel long-term forecast.

Gross pearl sales proceeds received by investors will be dependent upon the prevailing AUD/JPY exchange rate, as the majority of global trade in South Sea pearls is conducted in Japanese Yen.

Estimating future exchange rates is notoriously difficult, as they are affected by a number of factors that are difficult to predict, including local and domestic inflation rates, interest rates and global economic activity. As a consequence, when assessing the potential returns from the Project, Adviser Edge has used a wide range of assumptions. This has had a large impact on overall returns.

Over the course of the decade, the Australian dollar has experienced a steady appreciation in value, particularly relative to the US dollar and Japanese Yen. The key drivers of this trend have been the appreciation in global commodity prices that comprise over half of Australia's export trade, and an interest rate differential with many foreign economies that encourages foreign investment into comparatively higher yielding Australian assets. The Japanese 'carry trade' has had a particular impact on foreign exchange rates in recent history.

In 2008, BIS Shrapnel released a forecast for the long-term AUD/JPY exchange rate of 95.7. However, it should be noted that this forecast was issued during a period when the exchange rate was between 90 and 104, and before the full extent of the global financial crisis had unfolded. Since that time, the Australian dollar has significantly depreciated, to between 56 and 64 in February 2009. As a consequence of declining interest rates and a reversal of the Japanese 'carry trade' there is potential for the AUD/JPY exchange rate to remain low, especially if global economic recovery takes longer than anticipated and commodity prices remain subdued. While not necessarily a determinant of future exchange rates, the five-year forward exchange rate has reduced substantially from approximately 75 to 53 as at March 2009.

Exchange rates are notoriously volatile, and economic forecasting is an inexact science due to the matrix of global economic scenarios that may prevail over the forecast period. Arafura's estimated average JPY/AUD exchange rate of 75.0 appears to be within historical averages and is a premium on current exchange rates.

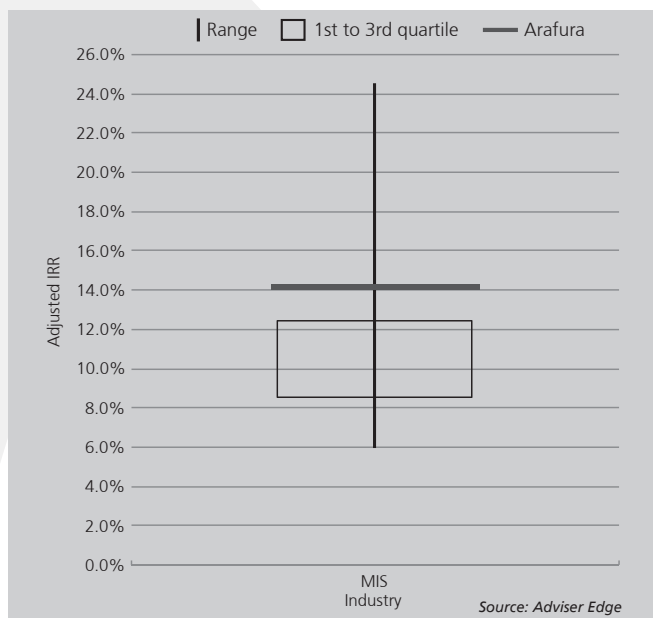
The following section provides an analysis of the potential investment returns for the Project. Please note that this analysis is based on estimated performance assumptions, which may change over the Project term. Investors should be aware of the way in which these assumptions may influence their returns, and should seek additional professional advice to determine whether or not this investment is suitable for their own risk and return objectives.

Adviser Edge Potential IRR Range*		
	Pre-Tax	Post-Tax**
Arafura Pearl Project 2009	2.40%–23.26%	2.40%–23.26%

* The range is provided as a guide only and investors should seek additional professional advice regarding the impact of changes in key variables on Project returns given their individual financial circumstances. The analysis does not consider investor finance arrangements.

** The analysis assumes a 46.5% marginal tax rate for the Project, that investors are registered for GST, and that all GST is rebated in the year paid.

Using a standardised adjustment model, Adviser Edge has calculated an indicative pre-tax adjusted IRR of 14.20% for the Arafura Pearl Project 2009. The following chart benchmarks these adjusted return estimates against all MIS projects researched by Adviser Edge in FY2008.



When compared to all non-forestry MIS projects researched by Adviser Edge in FY2008, the adjusted IRR estimate lies above the third quartile.

Investment Analysis Performance Assumptions

The estimated project returns provided by Adviser Edge have been calculated using various performance assumptions. The

key assumptions adopted by Adviser Edge are presented in the following table. These assumptions have been determined from information provided in the PDS, directly by Arafura, from the independent expert’s report, and independent research performed by Adviser Edge. The following table also includes the performance assumptions adopted by Arafura, as discussed in the Performance Parameters section of this report.

Performance Assumptions	Arafura	Adviser Edge
First harvest (Shells/Project Interest)	77	77
Second harvest (Shells/Project Interest)	44	44
Momme per shell (First Harvest)	0.72	0.70
Momme per shell (Second Harvest)	1.20	1.10
Saleable proportion	80%	80%
Price Estimate (First Harvest) (¥)	18,000	17,800
Price Estimate (Second Harvest) (¥)	18,000	21,800
Average AUD/JPY Exchange Rate	75	75
Price inflation	3.00%	2.90%

Pearl yield

Adviser Edge has adopted Arafura’s estimates in relation to mortality and nucleus rejection, which translates to the estimated number of shells successfully harvested per interest, as demonstrated in the previous table. One of the main risks in achieving the projected number of harvested shells is the number of shells that die or are rejected in the first 18 months of growth. However, Arafura’s replacement guarantee, which ensures a minimum of 176 shells per Project interest after 18 months from Project commencement, increases Adviser Edge’s confidence in this regard. Furthermore, Arafura has advised that the quota system used in the Northern Territory allows for rejection of nuclei, and Arafura intends to seed enough shells to meet the quota limit for each investor of 100 seeded shells per Project Interest.

It is difficult for Adviser Edge to verify Arafura’s assumptions in relation to mortality and rejection due to the lack of publicly available independent information. However, given the replacement guarantee and a quota system which allows for expected nuclei rejection, Adviser Edge is confident that Arafura’s estimated harvest targets are reasonable. The independent expert has stated that the assumptions used are within the collective range for Australian pearl farms producing hatchery shells and using qualified and experienced technicians and good farm husbandry practices.

Pearl quality

An important variable in determining overall returns is average pearl quality and size achieved. Adviser Edge has been able to inspect a sample of pearls from Arafura's 2008 harvest, which appeared to be of excellent quality. A number of examples of different sizes and shapes, including perfect rounds, teardrops and baroque shapes were observed. Arafura has provided Adviser Edge with an estimate for the expected proportion of each pearl grade, which has assisted in determining average pearl prices.

Pearl sizes are determined by nacre growth achieved over the growing period and the size of the nuclei used to seed the shell, which in turn is dependent on shell size at seeding and the expertise of the operating technician. Arafura has estimated average pearl size to be 0.72 momme per piece for the first harvest. The 2008 harvest has demonstrated Arafura's ability to meet its harvest target, with average pearl size reported to be 0.71 momme.

Arafura has significantly increased its expectations for pearl size for the second harvest from 0.85 momme to 1.20 momme. A larger pearl size can be expected for the second harvest as shell sizes are typically larger at seeding, which allows for larger nuclei to be inserted. Provided that Arafura are able to insert the larger sized nuclei for the second harvest and average pearl diameter exceeds 15mm, Adviser Edge is comfortable with the increased pearl sizes.

Arafura has demonstrated its ability to grow and harvest pearls to achieve quality and size objectives for first harvest shells. Although Arafura should be able to grow pearls to the size projected for the second harvest, Adviser Edge has used slightly more conservative assumptions in its analysis.

Pearl price

Predicting average pearl prices is inherently difficult, due to volatility in markets and the AUD/JPY exchange rate. Arafura has provided Adviser Edge with its assumptions regarding farmgate prices for polished pearls of different sizes and grades.¹ In assessing returns, Adviser Edge has reviewed pricing and grading assumptions, historical average prices and exchange rates, and the potential variations in sizes and grades that may be achieved.

In reviewing returns, Adviser Edge's slightly lower price assumptions for pearl prices at the first harvest has been offset by slightly higher price assumptions for the second harvest. Adviser Edge expects that second harvest pearls will be larger and more valuable than first harvest pearls. Arafura has indicated that it may value-add to the pearls through pairing and stranding, which has the potential to increase prices.

¹ Arafura will polish the pearls on behalf of investors.

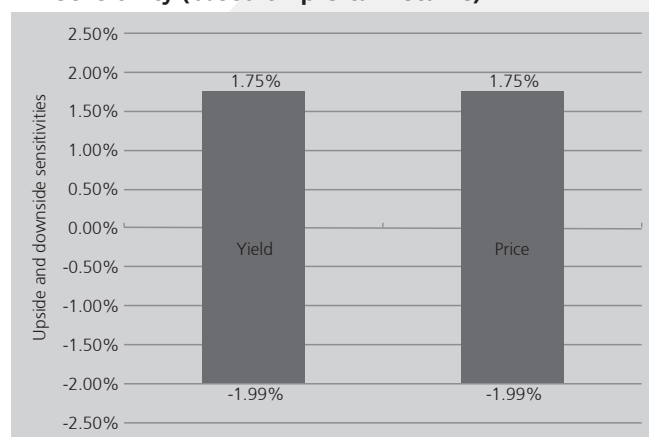
Although, the Australian inflation rate is not expected to be a determinant of actual pearl prices in the future, Adviser Edge has included an inflation rate for Australian dollar-denominated pearl prices. This is because future exchange rate estimates factor assumptions that include domestic and foreign inflation rate projections.

Adviser Edge has adopted slightly different prices than those estimated by Arafura, although these assumptions do not result in a materially different result in overall returns. However, investors should note that the actual prices achieved by the Project will be heavily dependent on overall quality of the harvest and the exchange rate at the time of sale. These factors can significantly affect overall returns, both positively and negatively. To mitigate price and exchange rate risk, Adviser Edge expects that Arafura will be flexible in determining the appropriate time to sell the pearls grown as part of the Project.

Sensitivities

The table below illustrates the sensitivity of investment returns (IRR) given an isolated change in key modelling factors. For the purpose of this analysis, Adviser Edge has considered the sensitivity of returns to isolated changes in yield and price. Yield and price sensitivity reflects a movement of 10% around the Adviser Edge performance assumption.

IRR Sensitivity (based on pre-tax returns)



The analysis illustrates that upside potential IRR is slightly lower than downside potential, due to the impact of the Bonus Fee. In addition to analysing returns based on fixed changes to key parameters, Adviser Edge has also assessed the impact of changes in certain key variables, being the price of pearls (Yen), exchange rate movements, post seeding mortality and variations in quality. The wide range of returns estimated for the Project reflects the potential impact of variations to these variables on overall returns.

Investors should note that an investment in the Project is subject to a high degree of volatility. In particular, the quantity and quality of the pearls harvested and the exchange rate at the time of sale will have a significant effect on overall returns. These variables have the potential to both significantly increase and decrease returns.

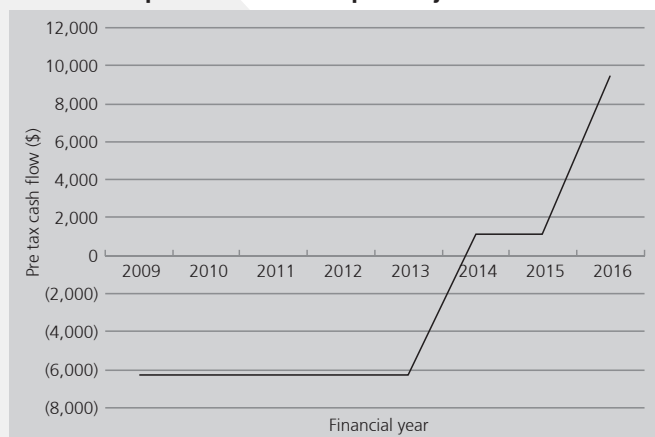
Adviser Edge recommends that investors consult with qualified specialists who understand how changes to an investor's tax status may affect investment returns

Pre-Tax Cash Flow per Project Interest

The Arafura Pearl Project 2009 aims to generate investor returns through the cultivation, establishment and sale of South Sea pearls. The Project has a term of approximately six-and-a-half years. Returns are expected to be generated from the sale of pearls from the first harvest, which is expected in the first half of Project year five (FY2014), and the sale of the pearls from the second harvest, which is expected in the first half of Project year seven (FY2016).

An indicative pre-tax cumulative cash flow for Project is presented below. These cash flows have been calculated using the performance assumptions adopted by Adviser Edge.

Cumulative pre-tax cash flow per Project Interest



Post-Tax Potential

The post-tax returns earned by an investor will depend on the investor's marginal tax rate when harvest returns are received. The post-tax IRR range provided by Adviser Edge assumes that the investor maintains the same marginal tax rate of 46.5% throughout the investment term. It is possible however, that an investor's tax status will change over the life of the Project. A change in tax status may result from a change in circumstance for the investor, or a change in tax policy administered by the Australian government. It is important that investors are aware of how these may affect the post-tax performance of the Project.

Investors in the Arafura Pearl Project 2009 will be subject to risks associated with medium-term aquaculture investments. All potential investors should carefully consider the risks outlined in the Project PDS, and the specific risks outlined in the Adviser Edge research report.

Management risks

MIS management encompasses not only the operational capabilities of the project counterparties, but also the corporate abilities of Arafura to monitor operation performance, ensure that the shells are not overstocked, and to meet the regulatory and statutory responsibilities required of it as Project RE. For all MIS projects there is a risk that if the financial position or performance of management deteriorates, asset condition, project outcomes and/or regulatory outcomes may be temporarily or permanently compromised.

Structure and fee risks

Ongoing management fees are deferred and taken as a percentage of sale proceeds. The fee structure means that investors have some protection from unexpected increases to management costs over the Project term.

The prescribed deferred fee shortfall amount is structured to provide Arafura with some protection against this risk. That said, Arafura's ability to control production costs and maintain adequate operating cash flow will be a critical determinant of the quality of operational management supplied to the Project, and Project outcomes.

Site and aquacultural risks

Investors should be aware of the risks associated with the site and management of the Project. Key areas of risk identified by Adviser Edge are:

Climate and weather

There is the risk that weather conditions can adversely affect the performance of the Project through destruction of Project assets and/or impact to water quality. In particular, there is a risk that cyclone activity may cause significant asset damage and loss of stock. Arafura has adopted various management activities and insurance to cover mature shell to mitigate these risks.

Disease

Biosecurity is important in aquacultural production systems, including pearl farming. For example, disease outbreaks in Akoya shells in Japan has dramatically curtailed the country's production, especially in larger, higher valued pearls. Australia's strict quarantine laws and quota system have been implemented to mitigate this risk.

Technician expertise

The Project is substantially dependent on the skills and expertise of seeding technicians to meet seeding rejection rates and pearl

sizes. Arafura use qualified and experienced technicians from Koyo Shinju to undertake all seeding operations.

Infrastructure

Infrastructure risks include the factors associated with boats, longlines and other infrastructure. Over time, Arafura has developed substantial infrastructure required to manage the pearl farms, which should ensure that Project outcomes are met.

Performance risks

Yield and quality

Activities that deal with pearl farming are exposed to similar risks as those inherent in other aquacultural production systems. These risk can affect shell mortality, average shell size and nacre growth. Investors should be aware that even conservative yield estimates are prone to failing due to adverse growing conditions. However, these threats can be mitigated by good quality management to prevent overstocking, appropriate shell cleaning regimes, and the appropriate selection of broodstock.

Information risk

There is a risk that the productivity assumptions used are too optimistic or that the productivity potential of a selected property may be overestimated.

Price

Investor returns will be directly affected by pearl prices at the time of sale. While prices are generally dictated by the dynamics of supply and demand, changes in certain macro-economic factors can also have an impact. Such factors include exchange rates, interest rates, and inflation. Investors need to be aware that these factors can negatively affect investor returns.

Marketing risks

As with any MIS project, there is a risk that the market for the Project resources will encounter a significant downturn at the time of harvest. This may be due to factors such as competition, regulation and/or market preferences. The effect of reduced demand may affect prices, which could potentially reduce investors' returns. However, it should be noted that as a non-perishable item, pearl sales can be delayed until economic conditions improve.

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