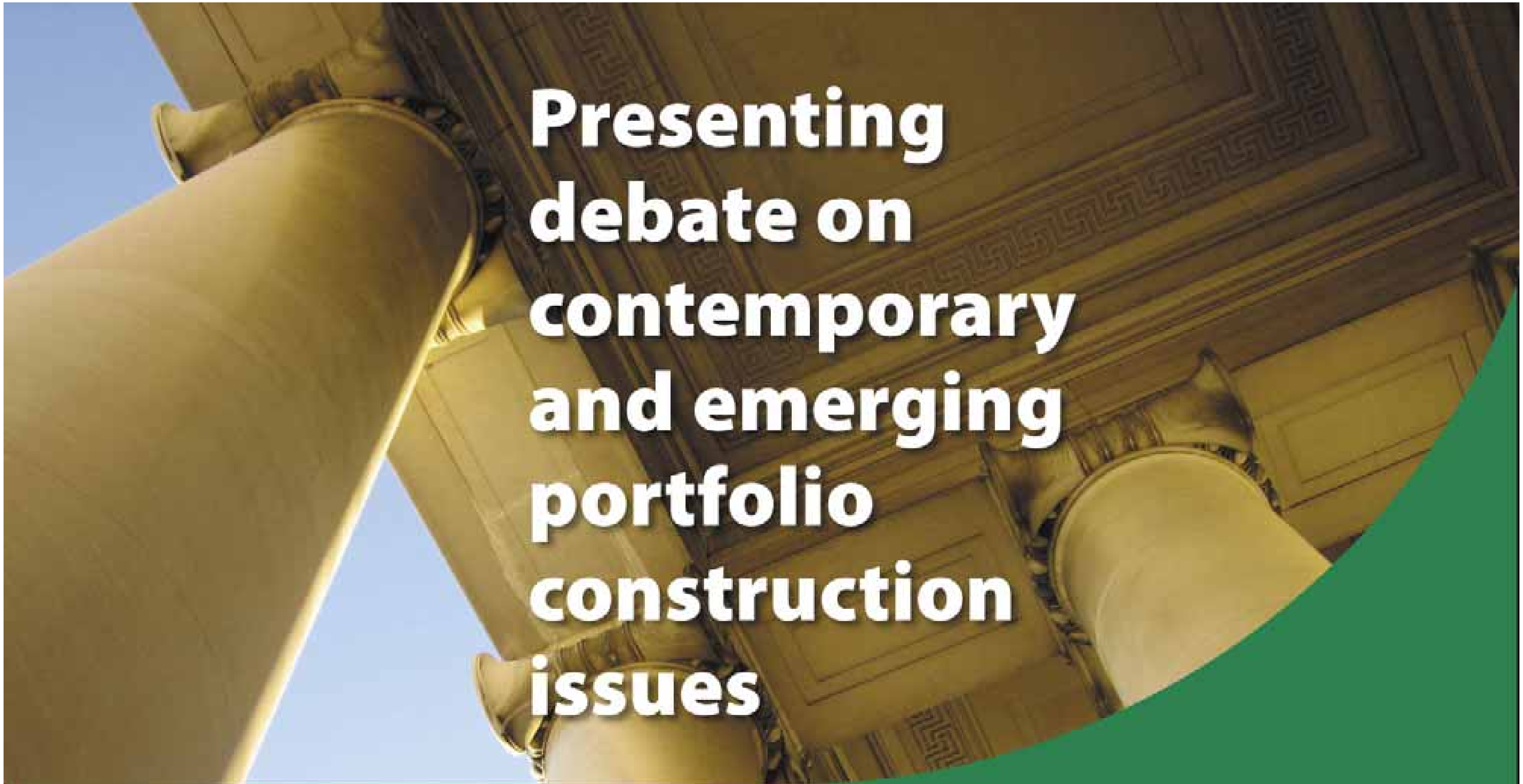


Presenting debate on contemporary and emerging portfolio construction issues

portfolio construction

CONFERENCE

15 & 16 August 2007 | AJC Convention Centre, Randwick, Sydney

SELECT ASSET MANAGEMENT

At the end of the party who will be left standing?

An alternative investment solution for challenging times ahead

Alter
nati
vethin
king.

Agenda

- The current investment landscape
- The potential role of alternative investments
- Some additional considerations

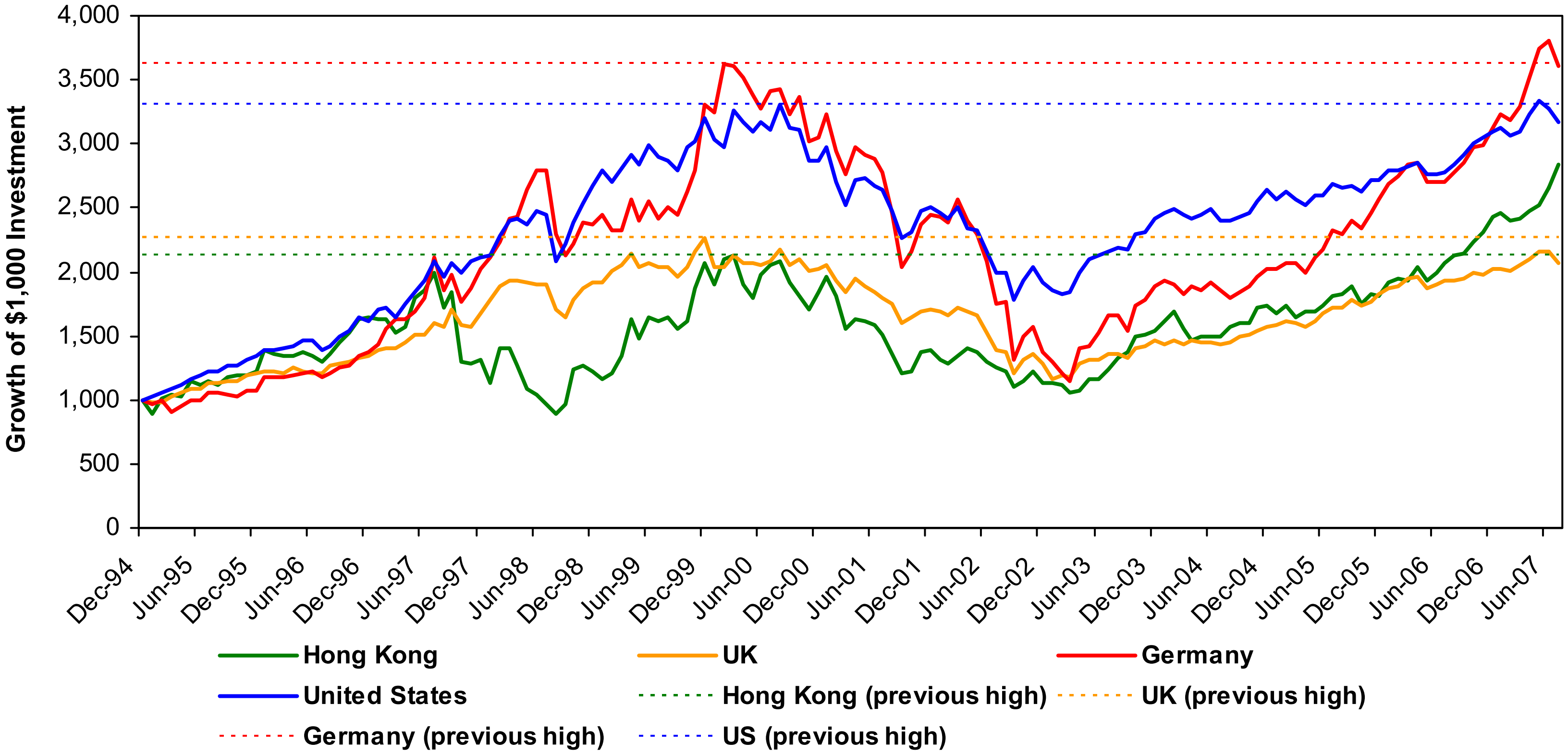
Alter nati vethin king.

How good can it get?

- Buoyant domestic equity markets
- Strong Australian economic growth – beneficiary of resources boom / China growth
- Frantic merger and acquisition & private equity activity globally – a product of expanding corporate profits
- Many international equity markets hitting all-time highs
- Tame inflationary environment
- High yield markets (until recently) very benign – credit spreads very tight
- Low levels of volatility

Global equity market strength

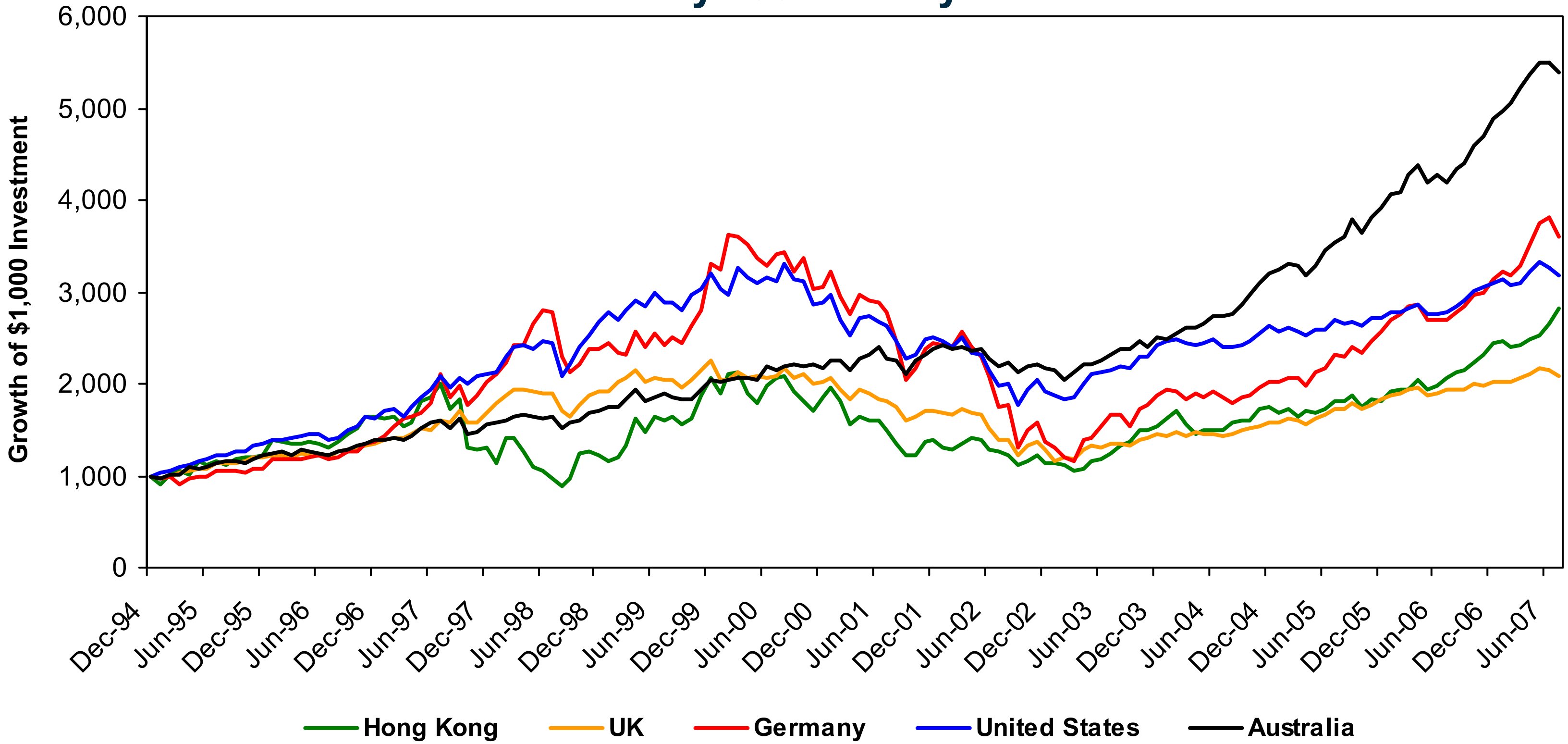
Global equity markets: Performance of $1,000 investment January 1995 to July 2007



Source: Bloomberg. Performance is stated in local currency terms. Hong Kong: Hang Seng Index, UK: FTSE 100 Index, Germany: DAX Index, United States: S&P500 Index. All indices are stated in local currency terms.

But Australia doing even better!

Global and Australian equity markets: Performance of $1,000 investment January 1995 to July 2007



Source: Bloomberg. Performance is stated in local currency terms. Hong Kong: Hang Seng Index, UK: FTSE 100 Index, Germany: DAX Index, United States: S&P500 Index, Australia: S&P/ASX 200 Accumulation Index. All indices are stated in local currency terms.

IMF and BIS - why is the boom happening?

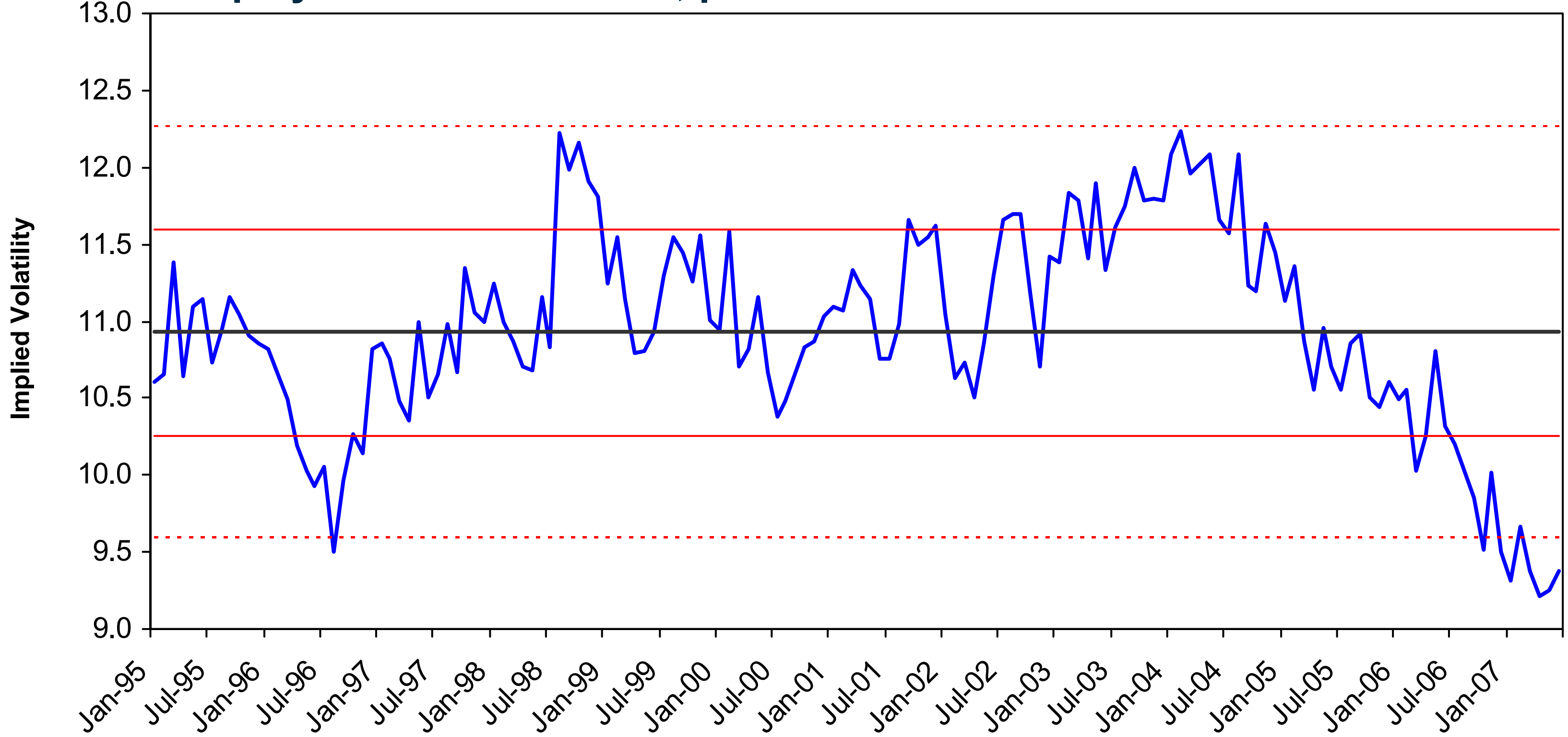
- Plentiful supply of global liquidity, fuelled by low interest rates (primarily in US earlier in the decade)
- Loosening of credit policies by rating agencies and banks
  - Leveraged loans to corporates
  - Credit generally to private sector

International Monetary Fund - Monetary and Capital Markets Department Global Markets Monitoring and Analysis Division, 2006, “Financial Market Update”, pages 6-10
Bank For International Settlements, 24 June 2007, “77th Annual Report – 1 April 2006 to 31 March 2007”

Aggregate market volatility at historic lows

Alternativethinking.

Compression in global volatility, January 1995 to June 2007
Displayed with mean level, plus 1 and 2 standard deviations from mean



Source: 36 South Investment Managers Limited - GIVIX Balanced Index. Based at weighted average of components on 1 January 1995. Index comprises aggregate implied volatility across equity, bond/interest rate, commodity and foreign exchange markets.

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Why has volatility been so low?

- Low inflation concerns
  - China and India meeting supply capacity constraints
- Shallower credit cycle
  - Central bank actions
  - Accommodative macroeconomic policy
- Wider spread of risk in the financial system allowing banks to securitize and offload risks
  - Financial innovations
  - Credit derivatives

Source: International Monetary Fund - Monetary and Capital Markets Department Global Markets Monitoring and Analysis Division, 2006, "Financial Market Update", pages 6-10.

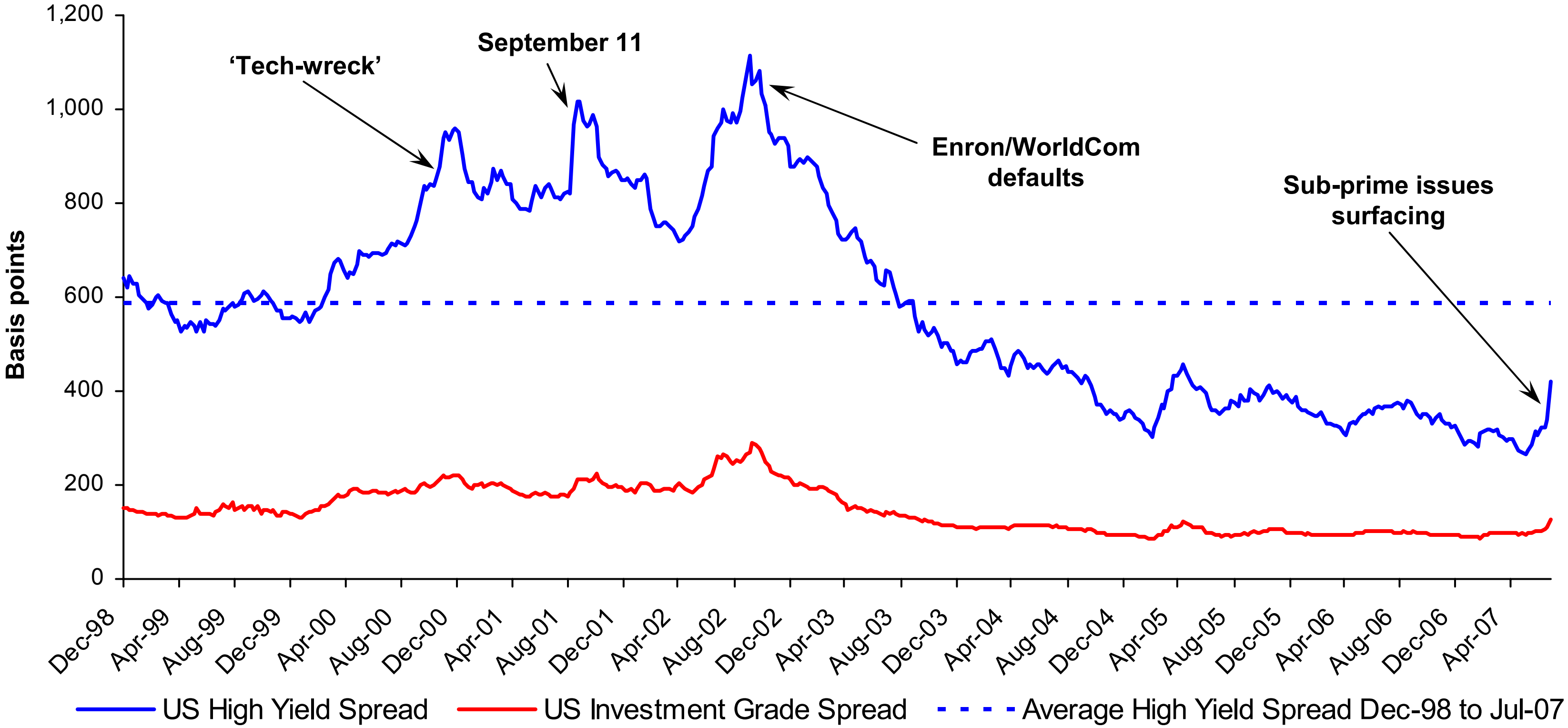
Stark warnings from the BIS

- Credit-related
  - Tight credit spreads
  - Issuance of structured products / CDOs
  - Vulnerability: slowdown in corporate profits
  - Rising LBO activity and increasing company debt
  - Ability of banks to offload credit risk via derivatives
  - Relaxation of credit standards towards households and businesses (+ excessive residential property exposure)
- Systemic
  - Internationalisation of banking / growing interbank activity
  - Unwind of the 'carry trade'

Source: Bank For International Settlements, 24 June 2007, "77th Annual Report – 1 April 2006 to 31 March 2007"

Historically tight credit spreads

High yield and Investment Grade Credit Spreads
December 1998 to July 2007



Source: Credit Suisse - CS High Yield Index Spread to Worst, Bank of America - BOA High Grade Broad Market Corporate Spread to Worst, 31 December 1998 to 26 July 2007

Credit: Comments from an investment bank

- March 2007: The currently tight level of spreads in US high yield markets would not have compensated investors for historical default levels experienced in any 5-year corporate bond market period since the mid-1970's

Source: Bank For International Settlements, 24 June 2007, "77th Annual Report – 1 April 2006 to 31 March 2007", page 115

Danger of complacency – sound familiar?

- Great Depression in the United States in the 1930's
- Financial crisis in South East Asia in the late 1990's
- Failure of LTCM / Russian debt crisis in 1998
- Collapse of global stock markets in 2001
  - None of these events preceded by any noticeable inflation
  - Preceded in all cases by a combination of some common factors:
    - rapid technological innovation
    - rising productivity
    - rapid increases in the prices of equity and real estate and strong fixed investment
    - ongoing technical innovations in the financial sector, including much greater availability of leverage / credit
    - capital inflows (in some cases which suddenly reversed as the crisis worsened)

Source: BIS Working Papers No 205 “Is price stability enough?”, William R White Monetary and Economic Department April 2006, pages 7-8

Danger of complacency – sound familiar?

- “The historical record provides stark evidence that a preceding period of price stability is not sufficient to avoid serious macroeconomic downturns”
- “These facts are as easy to describe as their implications are hard to deny: price stability was not enough to ensure high, sustained growth”

Source: BIS Working Papers No 205 “Is price stability enough?”, William R White Monetary and Economic Department April 2006, pages 7-8

Agenda

- The current investment landscape
- The potential role of alternative investments
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Growing recognition and use of alternatives

Alternativethinking.

- Investors doing very well in recent years and generating easy returns in benign market conditions
- Despite this, growing recognition that this approach may not serve well in times of crisis, or when markets become over-stretched
- A number of sophisticated investors have made sizeable allocations to alternative investments to diversify away from traditional market risks
  - Primarily sophisticated pension, superannuation and endowment funds

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US Endowment Funds

- 2006 survey by National Association of College and University Business Officers of 765 endowment funds
- Dollar-weighted average alternative asset class allocation: 30.9%
- Increases in allocation to private equity, natural resources and hedge funds over preceding 10 years: 533%, 400% & 336% respectively

US endowment fund performance summary, years ending 30 June 2006

Time period	1 year	3 years	5 years	10 years
Number of survey participants	700	656	589	477
Dollar weighted average endowment performance	**15.3%**	**15.6%**	**9.2%**	**11.7%**
S&P 500	8.6%	11.2%	2.5%	8.3%
Lehman Bond Aggregate	-0.8%	2.1%	5.0%	6.2%
Inflation (CPI) - seasonally adjusted	4.3%	3.3%	2.6%	2.6%

Source: 2006 NACUBO Endowment Study. Comparative index returns assume a year-end date of June 30. Rates of return are reported net of management fees and expenses.

Why growing allocations, how easy is it?

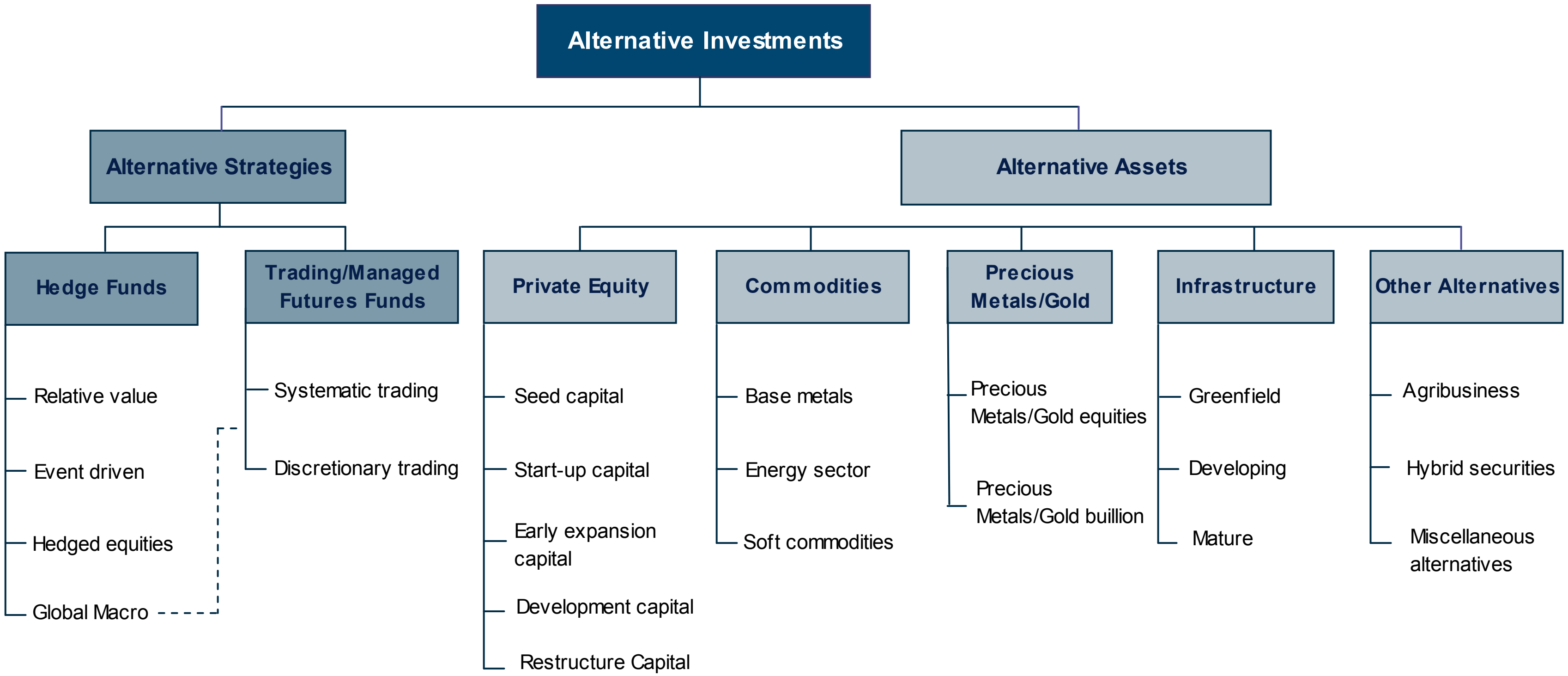
- Diversification into alternatives makes intuitive sense from a portfolio construction perspective

- Analysis of alternative asset classes is far from simple however:
  - Varying liquidity
  - Varying transparency
  - Non-normal distributions
  - Limited publicly available information on many strategies and managers

Alternative Investment Universe: SELECT's View

- It is possible to gain diversification amongst sub-categories of alternative strategies and alternative assets

Alternative Investment Universe



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Performance of alternatives: crisis periods

		Traditional Markets		Alternative Investments				
Crisis	Months	Global Equity Markets	Global Bond Markets	Hedge Funds	Trading Funds	Private Equity	Commodities	Gold Bullion
UK Currency Crisis	Sep-92 to Oct-92	-4.0%	-2.6%	4.1%	-1.4%	3.6%	-2.0%	-0.8%
Mexican Peso Crisis	Oct-94 to Dec-94	-1.2%	0.5%	-1.4%	1.3%	5.6%	2.1%	-3.0%
Asian Stock Market Crisis	Oct-97	-5.4%	2.1%	-1.5%	-1.6%	3.4%	-0.0%	-6.2%
Russian Debt Default / LTCM	Aug-98 to Sep-98	-12.0%	8.1%	-8.1%	9.3%	-3.8%	0.1%	2.1%
Dot-Com Bubble Burst	Apr-00 to May-00	-6.8%	-2.3%	-4.8%	-0.8%	-1.4%	4.7%	-2.5%
September 11	Sep-01	-8.9%	0.7%	-2.8%	1.8%	-2.9%	-7.0%	6.6%
October 2002 Market Correction	Oct-02	-11.1%	1.2%	-1.5%	2.4%	-1.6%	3.6%	3.6%
Equity Bear Market 2000-2003	Apr-00 to Mar-03	-47.7%	24.4%	1.2%	22.9%	-27.0%	14.9%	20.1%

Source: Bloomberg, January 1990 to May 2007, unless otherwise noted. Data is as follows - Global Equity Markets: MSCI World Index (USD), Global Bond Markets: JP Morgan Global Bond Index (USD), Hedge Funds: HFRI Fund Weighted Composite Index (USD), Trading Funds/Managed Futures: Barclay CTA Index (USD), Unlisted Infrastructure: Cambridge Private Equity Index (USD), Commodities: Dow Jones AIG Commodity Index (USD), Gold Bullion (USD). Note that Cambridge Private Equity Index performance is published quarterly - for this analysis quarterly returns have been spread evenly over the relevant months within each quarter.

Correlation and beta to equity markets

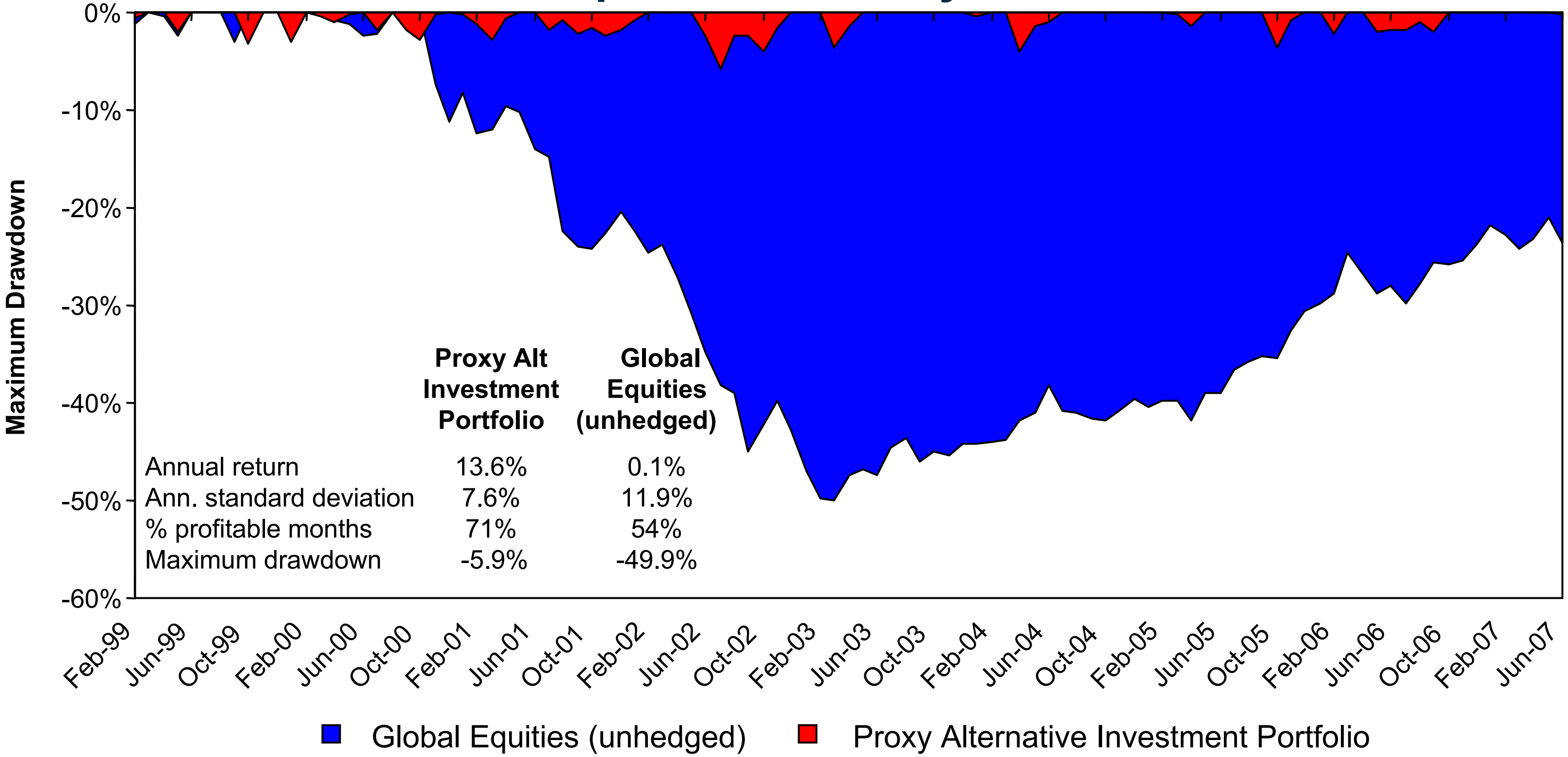
	Alternative Investments				
	Hedge Funds	Trading Funds	Unlisted Private Equity	Commod ities	Gold Bullion
Data period	Jan-90 to May-07	Jan-90 to May-07	Jan-90 to May-07	Feb-91 to May-07	Jan-90 to May-07
Overall correlation to global equity markets	0.68	-0.12	0.42	0.18	0.02
Correlation in positive global equity months	0.56	-0.47	0.34	0.07	-0.05
Beta in positive global equity months	0.81	-0.55	0.61	0.07	-0.04
Correlation in negative global equity months	0.39	-0.12	0.15	0.01	-0.15
Beta in negative global equity months	0.65	-0.10	0.25	0.01	-0.10

Source: Bloomberg, January 1990 to May 2007, unless otherwise noted. Data is as follows - Global Equity Markets: MSCI World Index (USD), Global Bond Markets: JP Morgan Global Bond Index (USD), Hedge Funds: HFRI Fund Weighted Composite Index (USD), Trading Funds/Managed Futures: Barclay CTA Index (USD), Unlisted Infrastructure: Cambridge Private Equity Index (USD), Commodities: Dow Jones AIG Commodity Index (USD), Gold Bullion (USD). Note that Cambridge Private Equity Index performance is published quarterly - for this analysis quarterly returns have been spread evenly over the relevant months within each quarter.

Proxy portfolio: Capital preservation

Alternative thinking.

Drawdown profile: February 1999 to June 2007



	Proxy Alt Investment Portfolio	Global Equities (unhedged)
Annual return	13.6%	0.1%
Ann. standard deviation	7.6%	11.9%
% profitable months	71%	54%
Maximum drawdown	-5.9%	-49.9%

Note: The maximum drawdown is a measure of risk that refers to the peak to trough decline during a specific period of an investment or fund. Source: Select Asset Management Limited, Bloomberg, February 1999 to June 2007. Global Equities (A$ unhedged) is measured by the MSCI World Index. The Portfolio of Alternatives Investments consists of equal weightings of the HFR Fund Weighted Composite Index 100% hedged to A$, Barclays CTA Index 100% hedged to A$, 50/50 blend of Cambridge and Listed Private Equity Index (both 100% hedged to A$), Dow Jones AIG Commodities Index (100% hedged to A$), 50/50 blend of FTSE Gold Mines Index and Gold Bullion (both 100% hedged to A$), and the UBS Australian Listed Infrastructure Index.

Alternativethinking.

Issues with such analysis

- **All indices** - include different types of funds/investments with ranging investment objectives and approaches, plus survivorship bias issues

- **Hedge Funds** - 34% of hedge fund index (measured by asset size) comprises long/short equity funds, many long-biased

- **Hedge funds** - In the months following a market crisis, hedge fund performance is often strong (e.g.1998 LTCM / Russian debt default, HF index +10.3% in following four months and +23.3% in following 12 months) – catalyst for opportunities

Source: Hedge Fund Research Inc., "HFR Industry Report 2nd Quarter 2007"

Issues with such analysis (more)

- **Commodities** - Commodity indices, depending on the provider, tend to have biases to certain markets (e.g. energy allocations - DJ AIG Index: 30% allocation, S&P GSCI: 71% allocation)
- **Gold** - Currency in which gold is stated makes a huge difference in terms of performance
  - Many consider gold by to be a pseudo currency itself
- **Infrastructure** - Difficult to find a broadly representative index (either listed or unlisted) that contains sensible data.

Source: Dow Jones Indices, Goldman Sachs

Lessons from analysis

- Broadly illustrates diversification benefits
- Diversified package of alternative investments offers potential for:
  - Lowly correlated performance
  - Fairly conservative return profile
  - Strong capital preservation characteristics
  - Complementary addition to a more traditional portfolio

Agenda

- The current investment landscape
- The potential role of alternative investments
- **Some additional considerations**

Experience is required

- Specific portfolio 'tilts' to enhance returns and reduce risks
  - Can be taken as a top-down asset allocation view – e.g. avoiding credit / high yield
  - Can occur at the underlying manager level e.g. commodity managers with higher allocations to or specific focus on agricultural futures, private equity managers with less exposure to leveraged buy-outs
- Differences between structure and style of alternative investments
  - Listed alternatives are available, in many cases trading at attractive entry prices – hedge funds, infrastructure and private equity
  - Offshore versus onshore domicile - tax and structuring implications, as well as currency hedging choices
- Market neutrality
  - Important in environment of tight credit spreads and shrinking equity risk premiums
  - Hedge fund investments needn't be long-biased, and can be market neutral or net short as well!

The real lessons from recent fund woes

- Key funds hit arguably not hedge funds but leveraged credit plays
- Most investors better off investing in complex areas via multi-managers/fund of funds
  - Professional oversight
  - More diversified (less damage if wrong)
- View that current situation was unpredictable is incorrect
  - Risk signs were there: historically tight credit spreads & high leverage
- Some hedge funds and fund of hedge funds are in a position to make money from credit woes – unlike traditional managers
- Illiquidity needs to be managed well, especially where leverage involved

Key issues for alternatives diversification

- Invest across a range of alternative strategies and alternative assets
  - Aim for low correlation to mainstream markets and to each other
  - Diversify across theme, strategies and dispersion of investment returns
  - Sources of risk and return should be widely spread - obviously not all linked to traditional market sources
  - Balancing appropriate liquidity can be difficult, but is not impossible
- Accessing some of the best ideas can entail:
  - Significant work to find managers / opportunities
  - A lot of lateral thinking and extensive due diligence
  - Challenges with structure, domicile, tax etc.
- Leverage and illiquidity are typically a bad combination in the wrong structure.

Key issues (continued)

- Differentiate between:
  - Skill based investments
  - Those relying on risk premiums which may not exist tomorrow (e.g. Yen carry trade, positive yield curve)
- 'Blow up' risk
  - It is not just hedge funds that 'blow up', many listed companies do as well
  - However, underlying manager diversification does provide comfort - make sure that one 'blow up' does not cause critical portfolio damage
- Two or more highly volatile investments may actually be complementary and provide strong risk-adjusted returns when combined in a portfolio
- Major challenge for individuals to diversify across a broad spectrum of alternative investments
  - Requires appropriate operational scale and breadth of research

Increasing competition

- As alternative investment industry develops and capital allocations increase some areas currently classified as alternative are clearly likely to become more mainstream (the oxymoron!)
- Potential for opportunities and performance to be eroded
- Fight for capacity in better managers and strategies likely to intensify – some strategies are capacity constrained

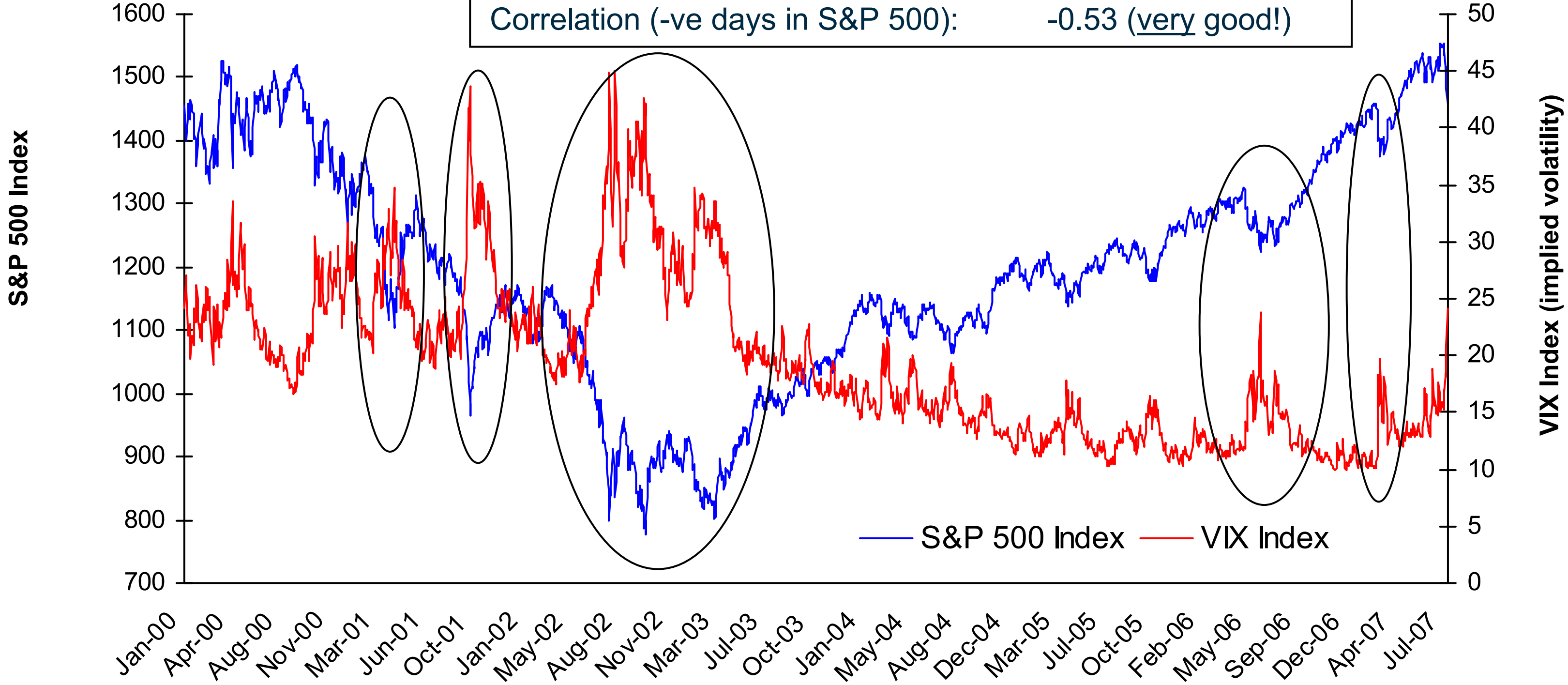
What does this mean for the industry?

- More sophisticated investors likely to invest in increasingly less mainstream opportunities
  - Some truly uncorrelated
  - Added layer of diversification, in some cases performance completely unrelated to traditional markets
  - Smaller weight of capital
- Some novel, innovative and unconventional managers exist - many operating in inefficient markets
  - Potential for strong risk-adjusted performance
  - However, different set of risks and different approach to due diligence

Some examples: Volatility Jan-00 to Jul-07

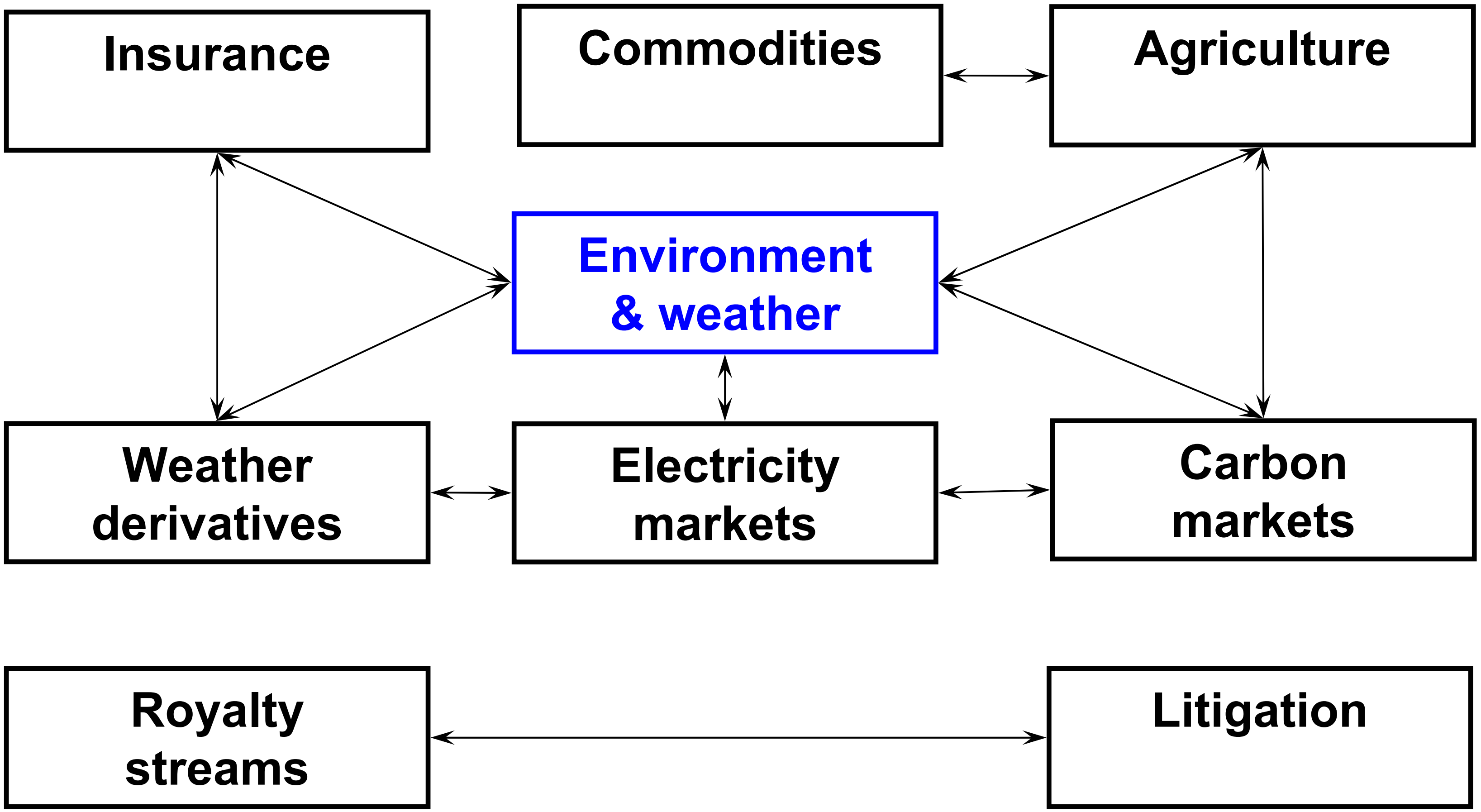
- VIX Index (implied volatility of the S&P500 Index) is negatively correlated to the S&P500 Index itself – when the market crashes, volatility rises

Daily correlation:	-0.11
Correlation (+ve days in S&P 500):	0.45 (good)
Correlation (-ve days in S&P 500):	-0.53 (very good!)



Source: Bloomberg. S&P 500 Index and VIX Index (measuring implied volatility of the S&P 500 Index. Data and statistics are based on daily data from 1 January 2000 to 27 July 2007.

Some examples: Non-correlated opportunities



Summary and conclusion

- Market conditions very benign, but some biggest periods of market stress have also occurred when this is the case

- A portfolio of alternative investments offers the opportunity to diversify away from some traditional market risks
  - Our view: a meaningful (at least 10% to 20%) allocation required
  - Allocations in practice vary: Hermes (largest UK pension fund): 10%, APB (largest European pension fund): 21.5%, calPERS (largest US pension fund): 13.5%, Harvard Endowment Fund: 38%, Yale Endowment Fund: 54.5%

- Challenges exist for individuals in researching and accessing alternatives

- The alternative investment universe continues to develop each year – some of best opportunities are some of the hardest to find and research

- Professionally managed multi-manager funds of alternative investments offer a potential solution

Source: Financial Times, May 7 2006 “Hermes proposes changes for BT fund”, International Fund Investment, December 2006, “Dutch allocations to alternatives will likely increase substantially in ‘07”, calPERS website. SELECT calculations based on $31.5bn in alternative investment management programme versus total assets managed by calPERS of $230.3bn at 31 December 2006 and SeekingAlpha.com, 20 November 2006 “Learning from the Harvard & Yale Endowments”

Alternativethinking.

Select Alternatives Portfolio

Provides a simple solution for investors/advisers seeking exposure to a range of alternative investments in a form that provides:

- Professional management and due diligence across the full spectrum of alternatives
- Access to some of the world's premier alternatives managers and funds
- Disciplined exposure to quality listed alternatives at attractive prices
- A sound fund structure providing acceptable liquidity and regular pricing; and
- Semi-annual distributions

Select Alternatives Portfolio

Description	➢ Provides a total alternatives portfolio solution accessing a diversified range of Australian and international "alternative" investments ➢ Utilises a multi-manager approach across a range of unlisted and listed alternative investments, overseen by SELECT's investment team ➢ Core allocations are currently made to our world-class partners Gottex, Aspect and Baker Steel ➢ Offers access to an innovative portfolio of alternative investments with monthly liquidity
Launched	➢ Launched on 1 April 2004*.
Option	**Select Alternatives Portfolio**
Objectives	➢ Aims to achieve attractive absolute returns that are lowly correlated to share, bond and property market movements over the medium to long term ➢ Target net return of cash plus 4%-5% p.a. with volatility of 7-8% p.a. over 3 to 5 year rolling periods ➢ When combined with a mainstream portfolio aims to preserve and enhance investors' wealth across varied market conditions
Current FUM	**A$47.8m****

* Prior to 1 April 2004 the name of the Select Alternatives Portfolio was the Select Aspect Multi-Strategy Fund (launched 25 June 2003) and the mandate was different.
**As at 30 June 2007. Excluding the 30 June distribution.

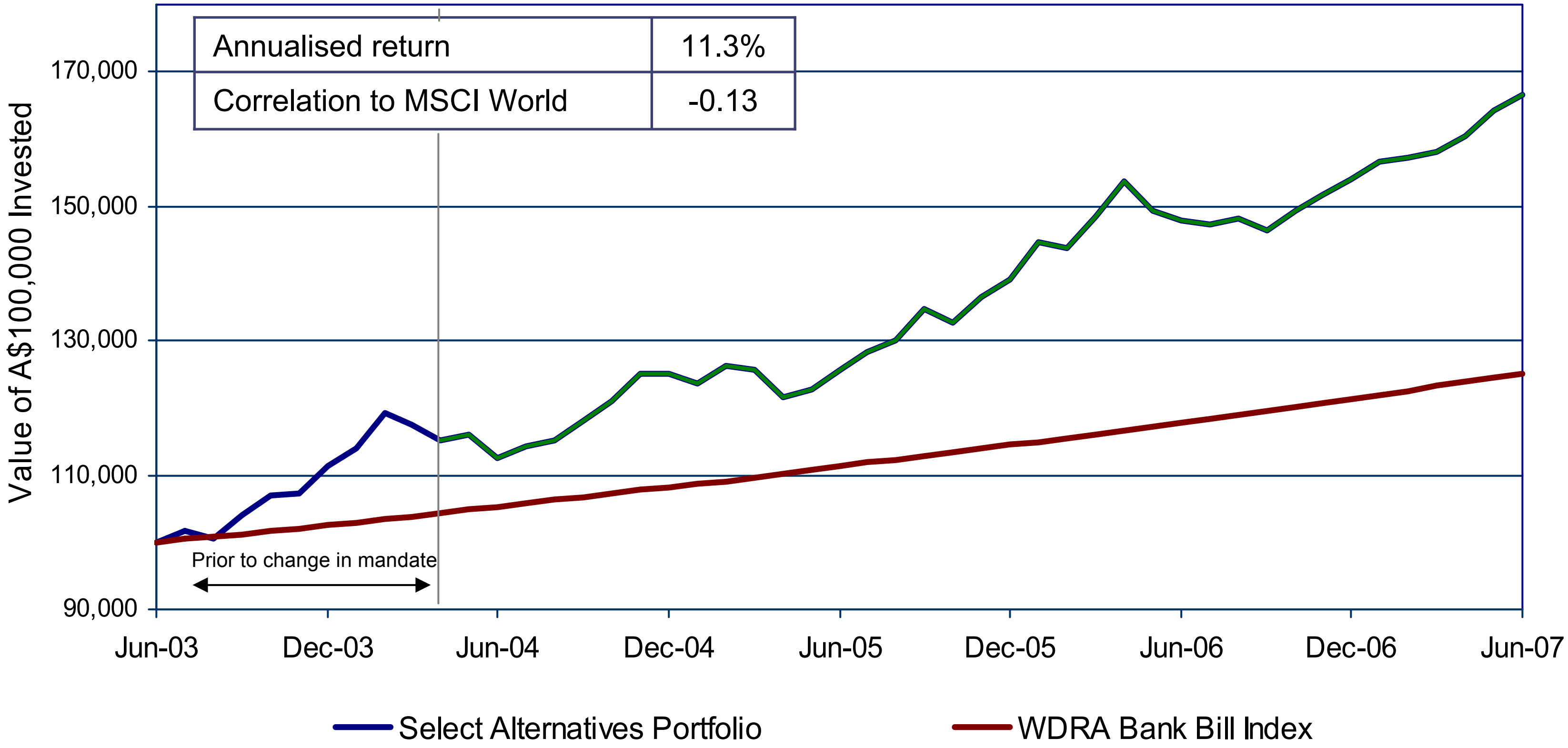
SELECT ASSET MANAGEMENT

Performance: Alternatives Portfolio

01 Jun 03 – 30 Jun 07*

Performance Net of all Fees

Annualised return	11.3%
Correlation to MSCI World	-0.13



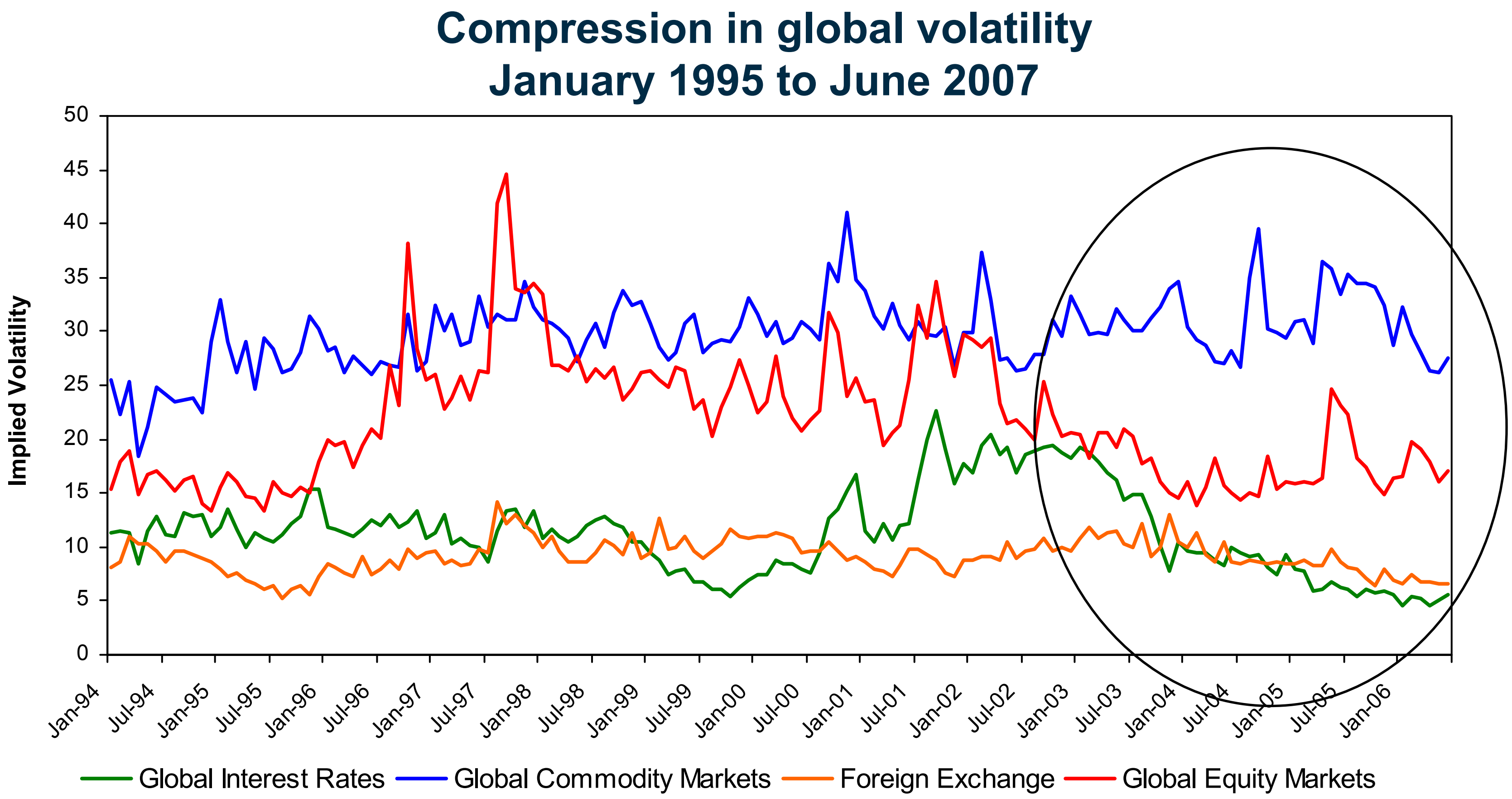
* Prior to 1 April 2004 the name of the Select Alternatives Portfolio was the Select Aspect Multi-Strategy Fund (launched 25 June 2003) and the mandate was different. Past performance is no guarantee of future returns.

Appendix

Appendix

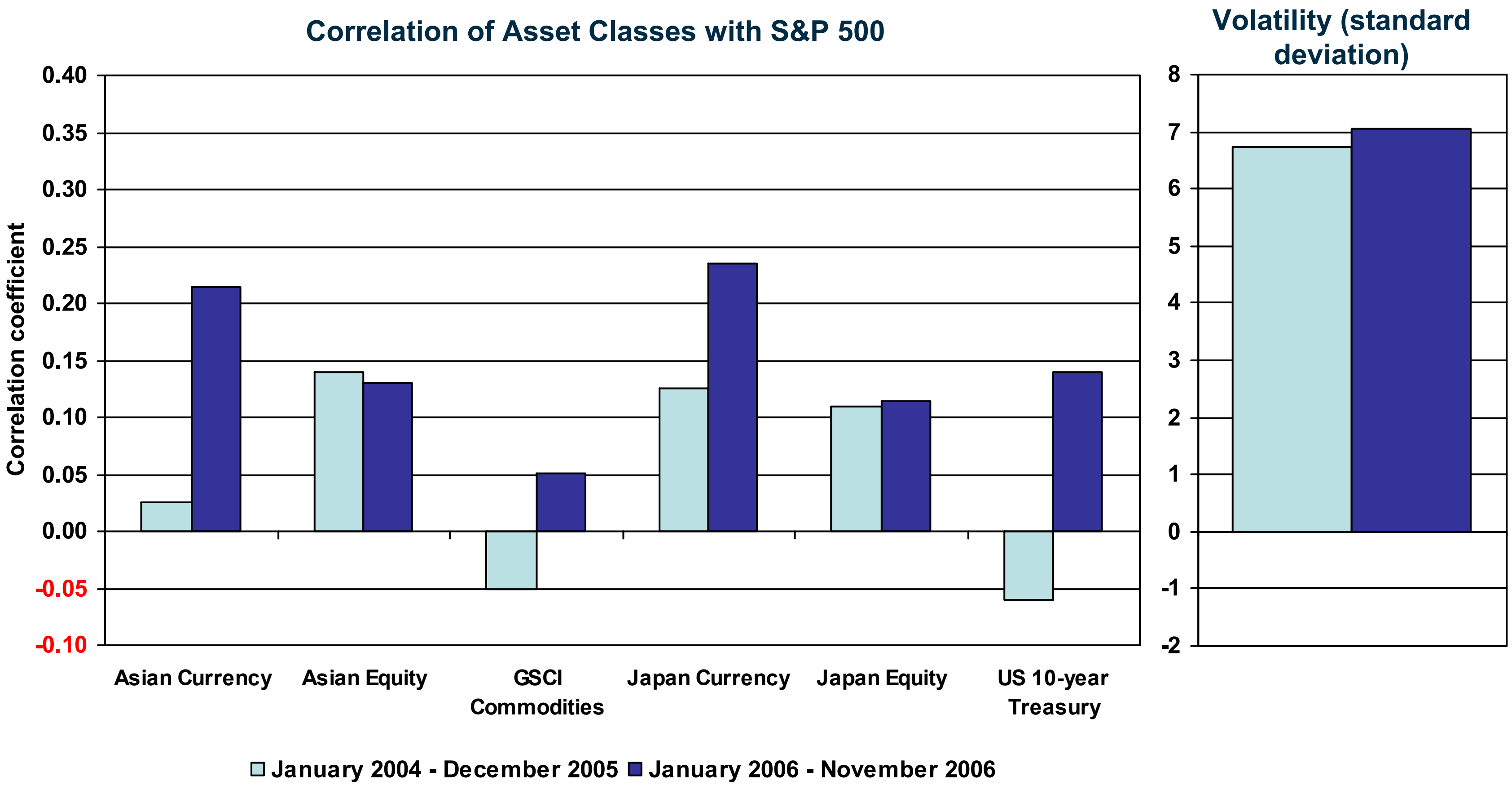
Volatility at historic lows, with exception of commodities: Underlying

Alternativethinking.



Source: 36 South Investment Managers GIVIX Indices comprise implied volatility across equity, bond/interest rate, commodity and foreign exchange markets.

Increasing traditional asset correlation



Source: IMF. Note: Calculations based on daily returns. Market volatility in calculated on an average of the annualised standard deviation of returns for each of the listed asset classes and the S&P 500. Correlations are displayed in the left hand chart, volatility is displayed in the right hand chart.

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