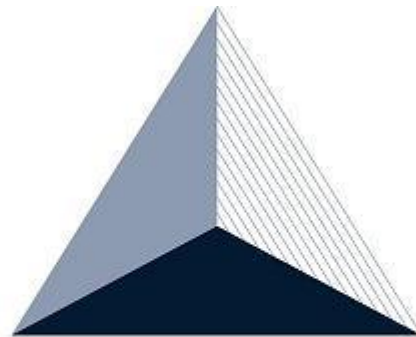




K2 ASSET MANAGEMENT

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K2 ASSET MANAGEMENT

***Global Equities***

***Active Management, Absolute Return***



## **DISCLAIMER**

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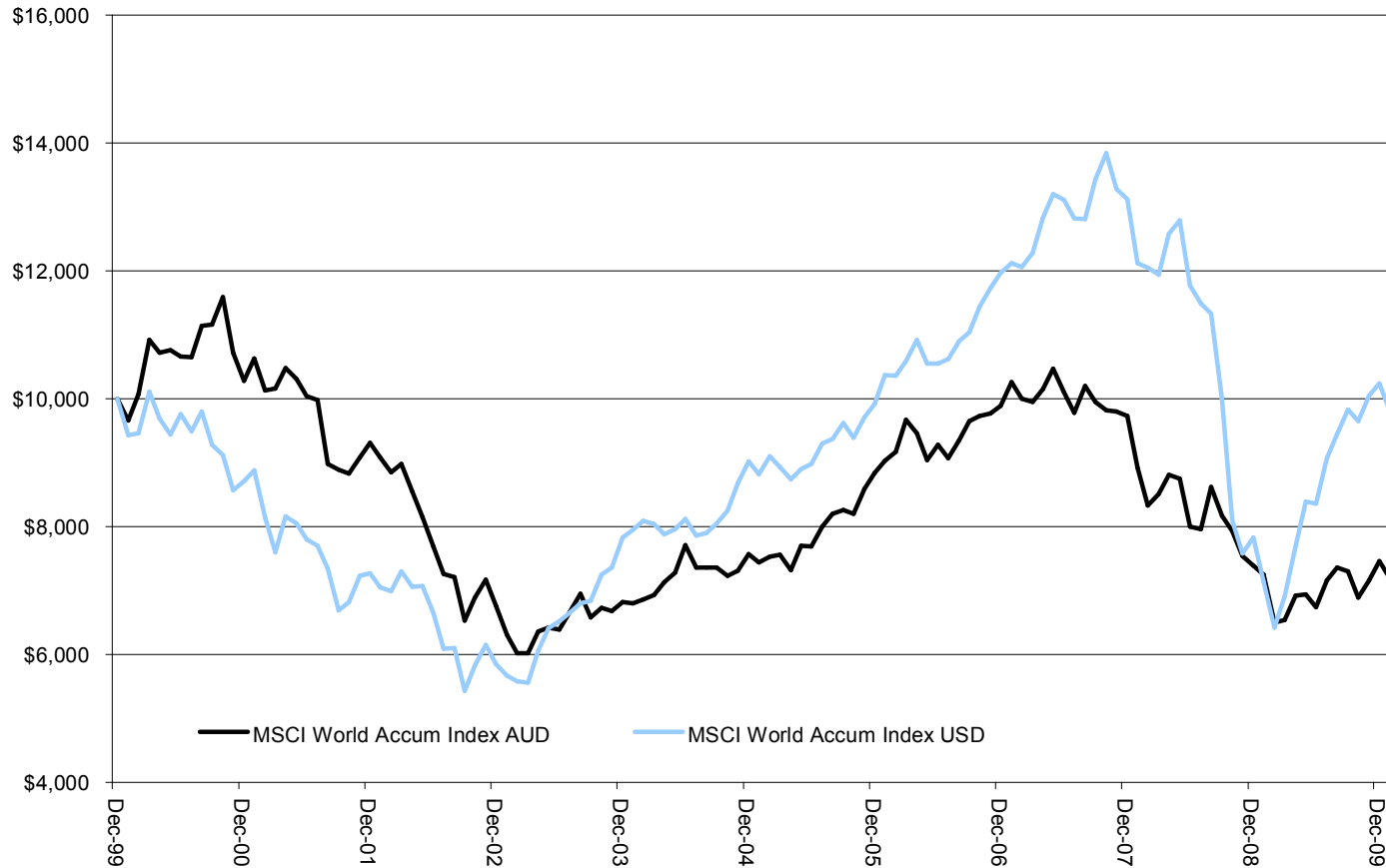
# Active Management



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## The index has not delivered

Growth of \$10,000 Jan 2000 - Jan 2010  
MSCI World Accum Index AUD/USD



# Absolute Return

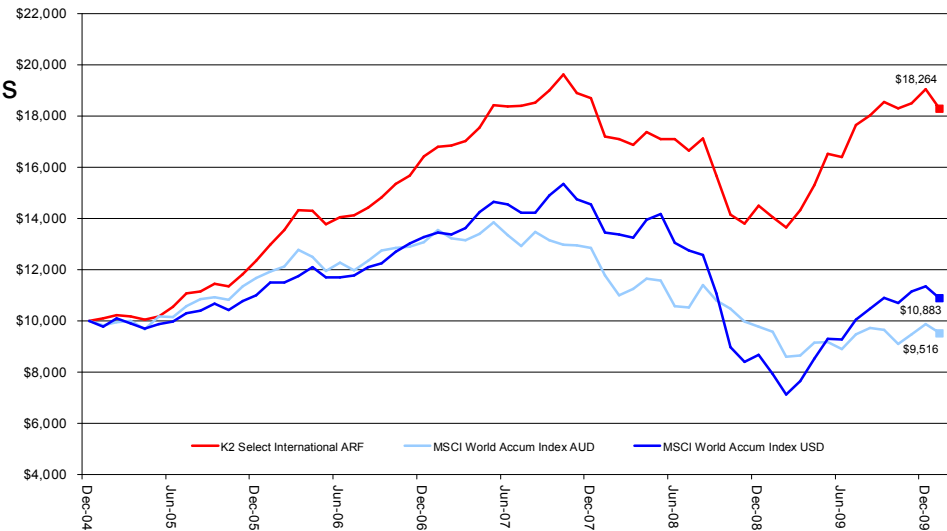


K2 ASSET MANAGEMENT

## Clients focus on the Absolute Return

- Tracking the index has not delivered competitive returns over a long time frame.
- Protecting capital is vital
- Stock picking and asset allocation are the key determinants of outperformance .... Not the market.
- **Clients focus on the Absolute Return**

Growth of \$10,000: Jan 2005 - Jan 2010  
K2 Select International ARF vs MSCI World Accum Index AUD/USD



Source: Morningstar February 2010

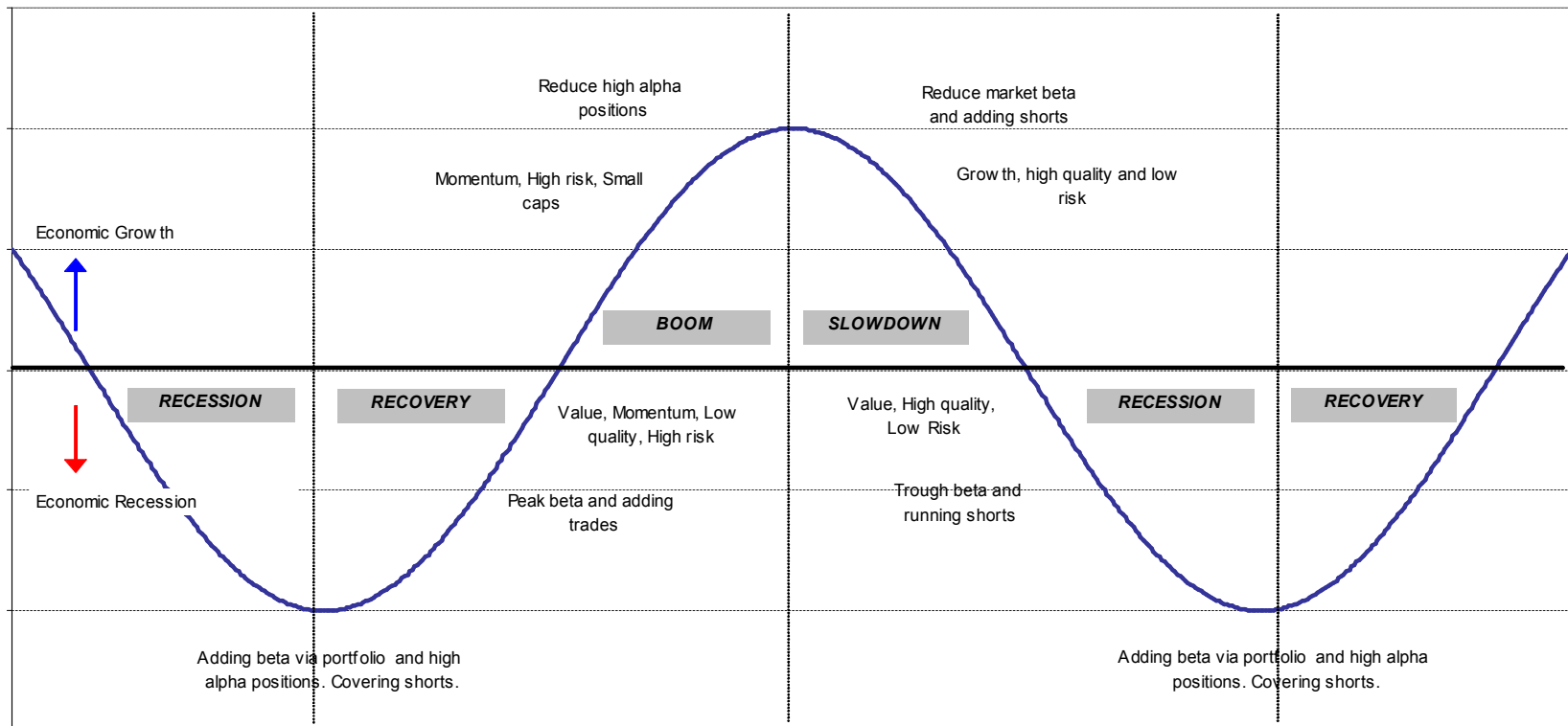
# Active Management



K2 ASSET MANAGEMENT

**K2 Asset Management believes in a flexible investment process to perform consistently because investment cycles are not uniform across global and regional markets at any one point in time.**

K2 portfolio construction & style vs Economic Cycle



# Alternative to Long Only



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## Empowering Managers

LONG ONLY MANAGERS	LONG/SHORT MANAGERS
<b>Inflexible investment mandates</b> Long only funds are expected to be fully invested (>95%) at all times.	<b>Flexible investment mandates</b> Managers benefit from their negative views of stocks and sectors, and can have a much lower net equity exposure
<b>Investment merit</b> Long only managers generally invest in companies that meet particular investment criteria, regardless of whether that stock will decline in the short-medium term.	<b>Investment merit – or not</b> Active managers focus on high conviction ideas, selecting those most likely to add value to the portfolio, whether a positive or negative view.
<b>Index driven</b> Long only managers typically manage funds around an index because that is their performance benchmark.	<b>Absolute return</b> Investment objectives that aim to provide a specific 'absolute return', not to beat an index benchmark.

# What K2 offers : Summary



K2 ASSET MANAGEMENT

## **Mandate**

- Global, Asian, Australian index unaware, long biased equity funds.

## **Strategy**

- To deliver superior risk-adjusted returns through the investment cycle and protect clients' invested capital

## **Objective**

- To achieve a net of fees return 15% p.a over a 3 – 5 year investment cycle.

## **Competitive Advantage**

- Highly regarded and stable team
- Flexible mandate ... long / short / cash
- Limited fund size ... luxury of being nimble
- Flexible style bias, flexible stock selection.
- Active FX hedging



## Simple Vanilla Approach

- Long biased, long/short
- Only invest in equities
- No gearing
- Use cash for protection
- Index, Sector and Region unaware
- Shorting – Event driven and momentum
- Currency – hedged opportunistically to protect gains

# K2 Funds

## Financial Year Returns



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Performance: 31 March 2010	1 year %	3 years % p.a.	5 years % p.a.	7 years % p.a.	10 years % p.a.	Since Inception % p.a.
<b>K2 Select International Fund</b>	<b>34.3</b>	<b>4.2</b>	<b>13.6</b>	-	-	<b>13.3</b>
MSCI World Index A\$	18.3	-7.9	1.0	-	-	1.0
<b>K2 Australian Fund</b>	<b>35.9</b>	<b>6.3</b>	<b>10.9</b>	<b>14.8</b>	<b>14.6</b>	<b>15.2</b>
All Ordinaries Accumulation Index	44.0	-2.4	8.0	12.6	8.8	9.4
<b>K2 Asian Fund</b>	<b>39.3</b>	<b>6.2</b>	<b>11.2</b>	<b>14.2</b>	<b>12.0</b>	<b>13.3</b>
MSCI Asia ex Japan A\$	34.2	0.0	9.5	13.0	4.3	5.5

# Outlook for global equities



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- What we said last time : *April 2009*
- Outlook for global growth : *Where to from here?*
- Risks to the outlook : *Climbing the wall of worry*
- Outlook for international equities : *Where does that leave shares?*
- Current investment themes : *The stocks we are holding*
- Currency : *We run it from an Australian investors perspective*

# What we said in April 2009



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## Summary

- The credit crisis and its resulting effects have produced a truly breathtaking and unprecedented collapse in global growth.
- Consequently 2009 will in general be a complete washout for corporate earnings with the market likely to focus on 2010 as a recovery year
- The unprecedented level of government and monetary stimulus will inevitably gain traction in the months ahead ... and may eventually gain too much traction creating a dash for hard assets.
- Expect volatility to continue, but we feel a market bottom is close if not already here.
- Stock picking and capital protection will remain paramount in a market of lower returns expectations

*Source : Advisors Big Day Out April 2009*

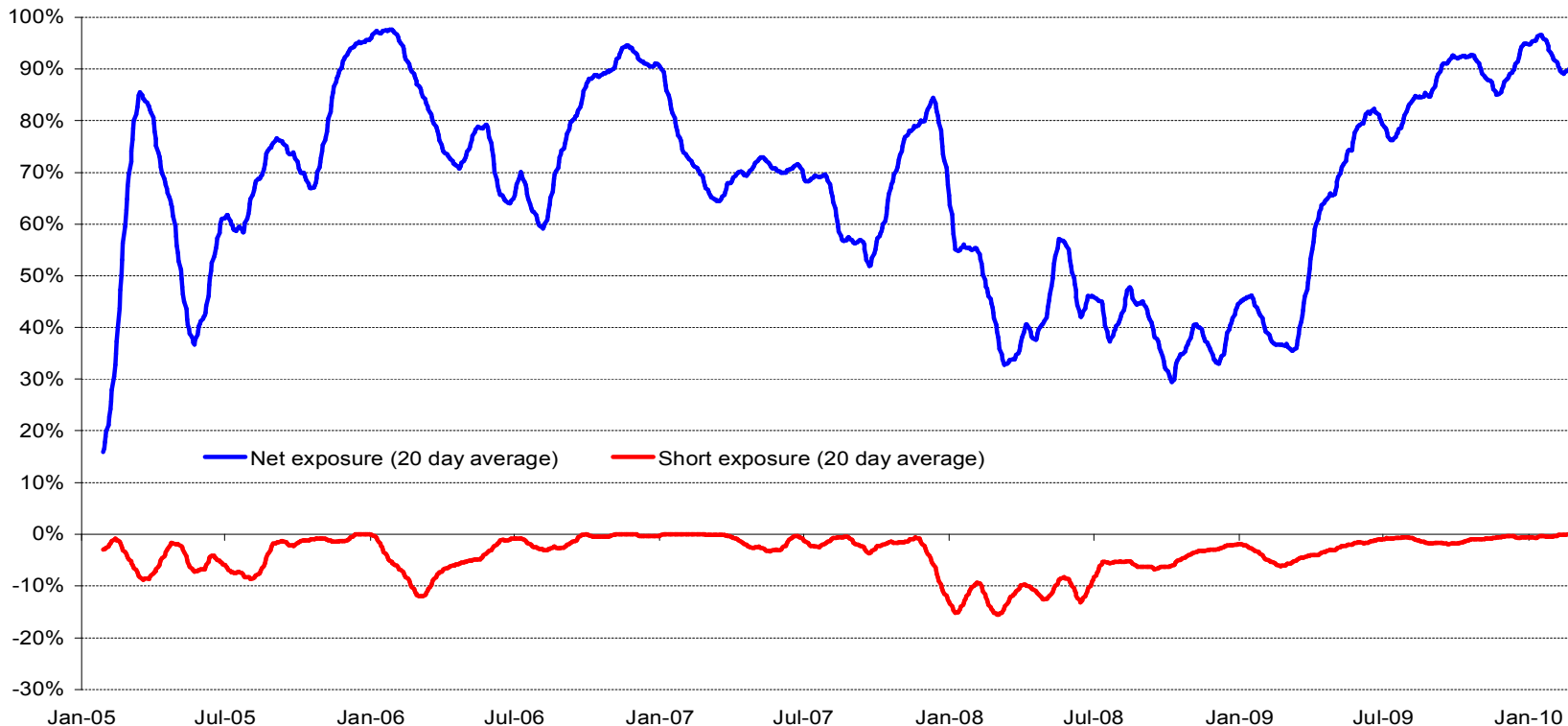
# What we said in April 2009



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## What we did .... Increased exposure ....quickly!

Exposure History - K2 Select International Fund  
January 2005 - February 2010

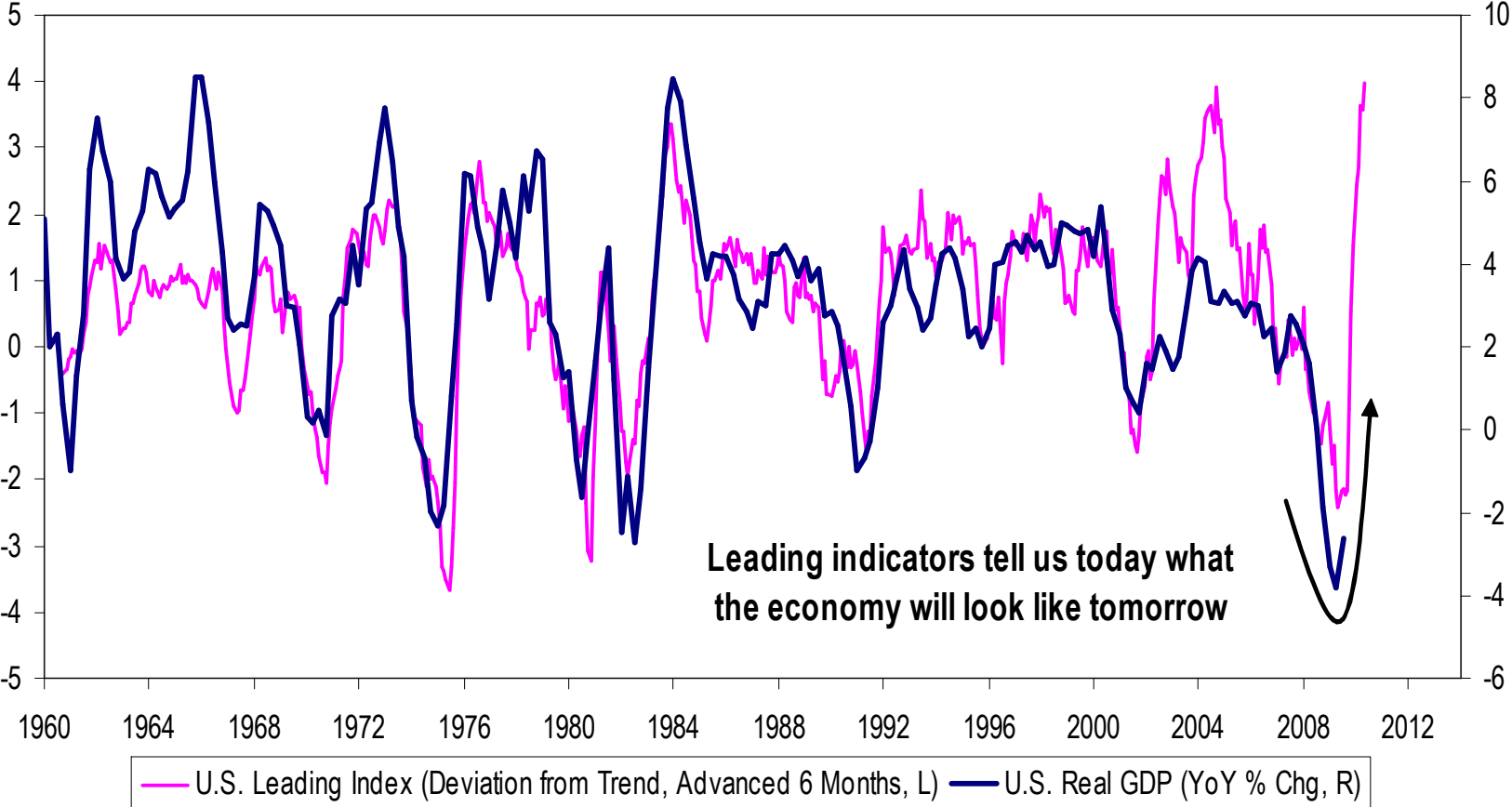


# Outlook for global growth



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## US leading indicators point to a strong recovery in US GDP



Source : ISI

# Outlook for global growth



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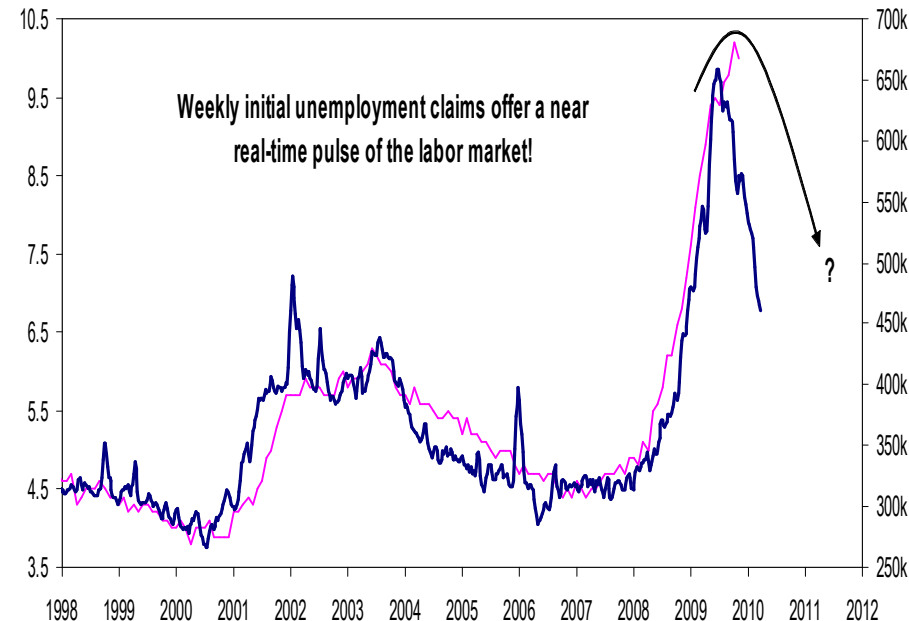
....which will include employment growth hence growth should be sustained

**Leading Indicators Heralding A Strong Cyclical Employment Recovery**



— ISM Employment Index (Avg. of Mfg. & Svcs., Adv 6m, L) — Nonfarm Payroll Growth (YoY % Chg, R)

**Weekly Claims: An Important Leading Indicator Of The Job Market**



— Civilian Unemployment Rate (% L) — Weekly Initial Unemployment Claims (4wk ma, Adv 3m, R)

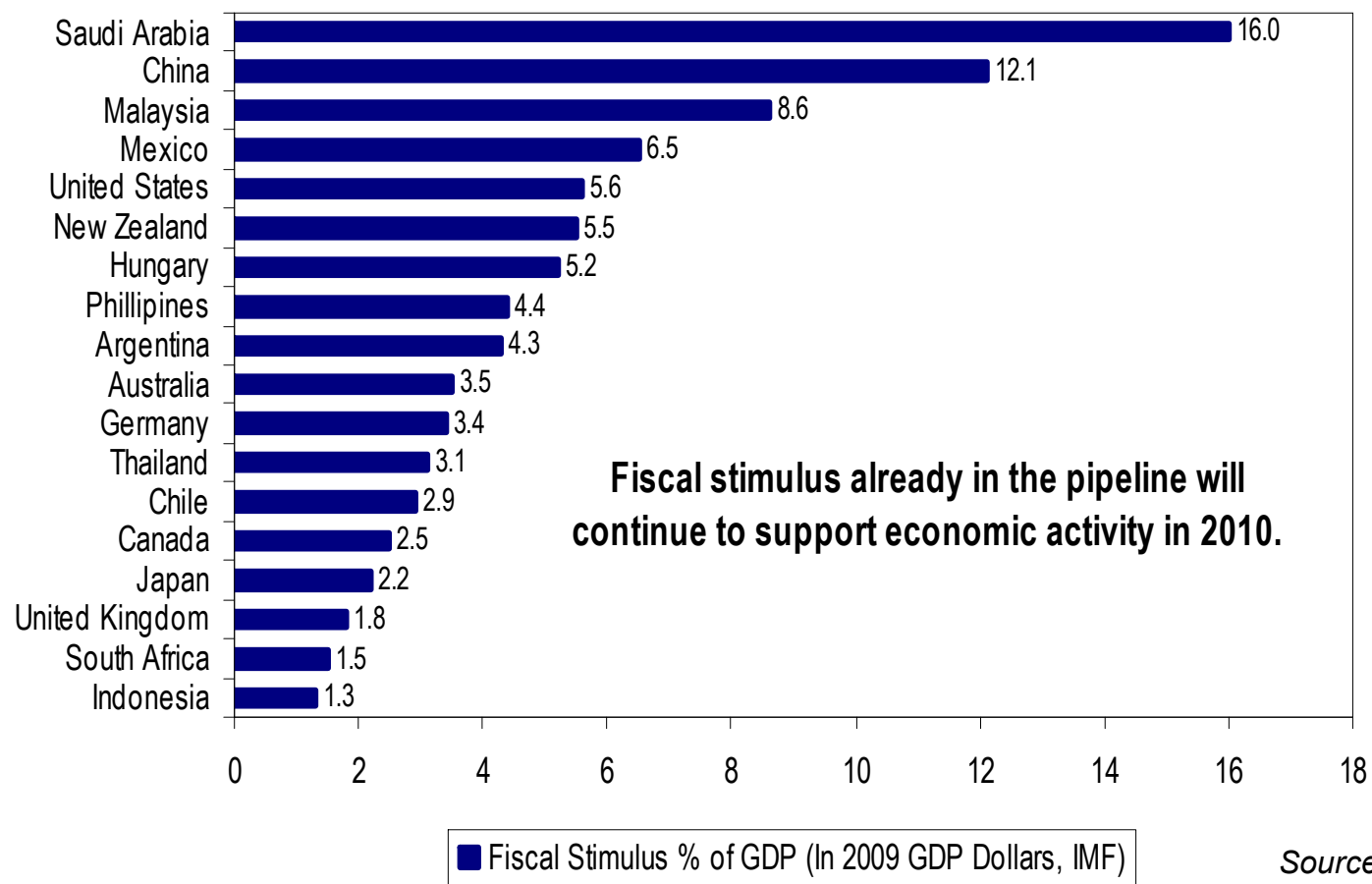
Source : ISI

# Outlook for global growth



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## Fiscal stimulus still playing a role .... with only 1/3<sup>rd</sup> spent



Source ISI

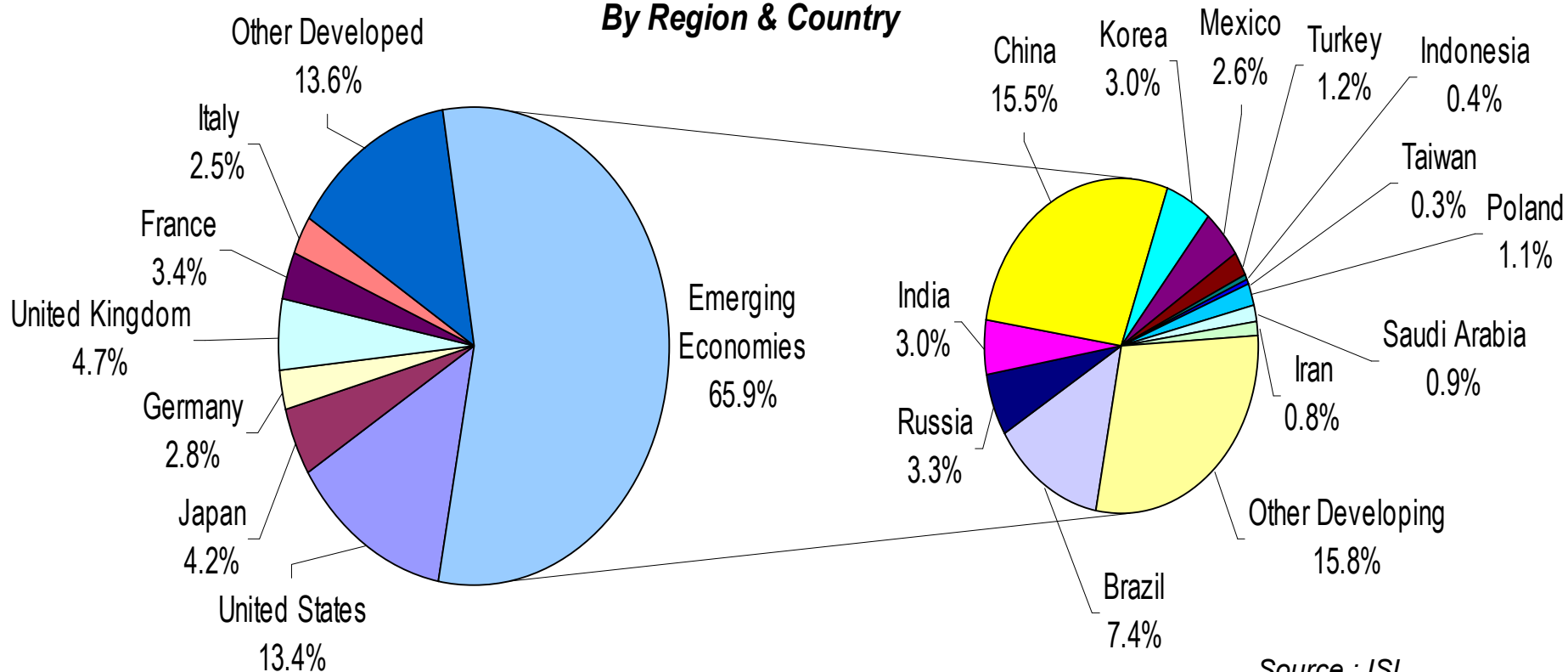
# Outlook for global growth



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**While only 40% of world GDP ...emerging markets make up more than 65% of incremental world GDP growth**

**Contribution To World GDP Growth (IMF)**  
***By Region & Country***



Source : ISI

# Outlook for global growth



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...and if anything China growth is accelerating ... Over heating?

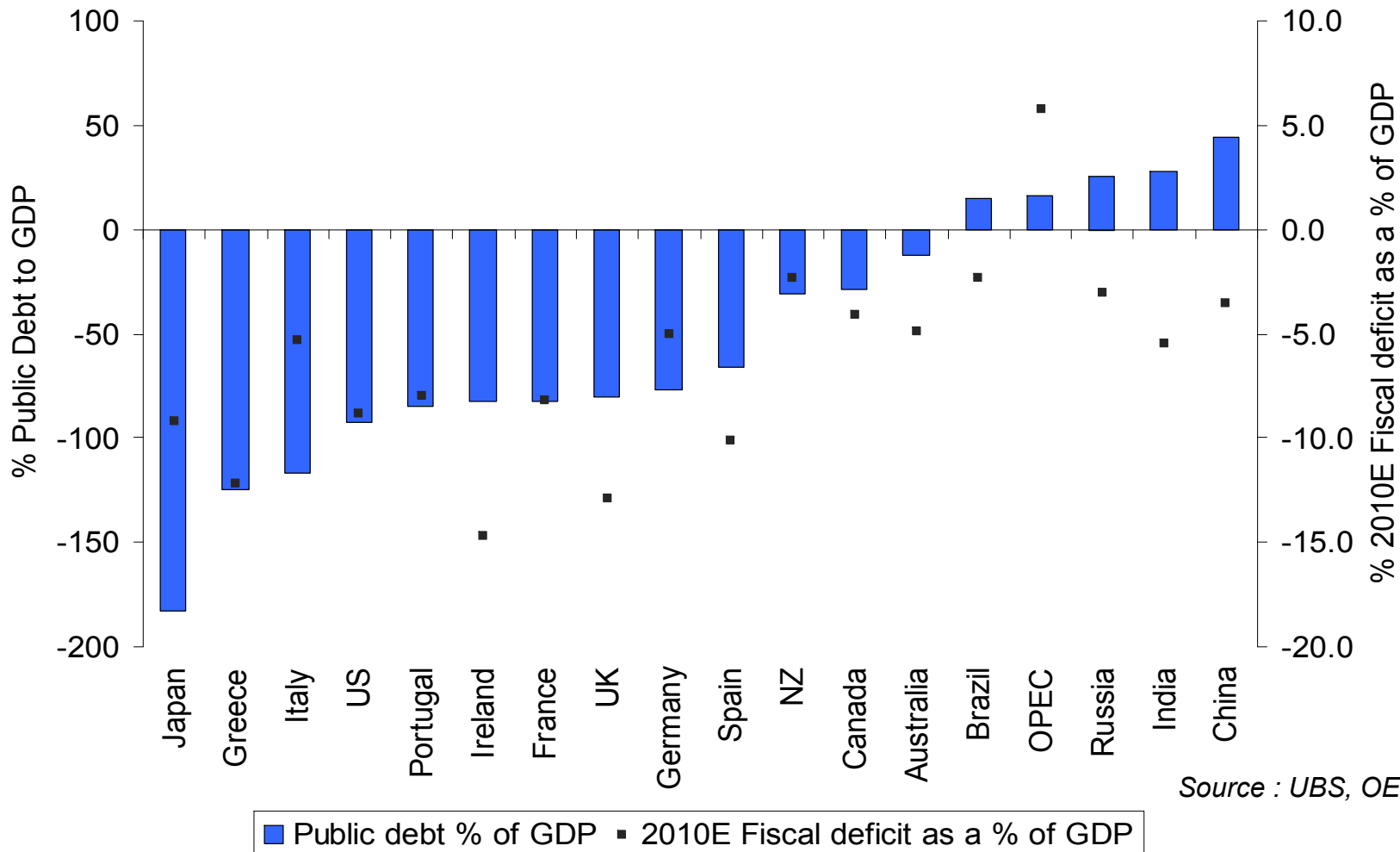


Source : ISI

# Risks to the outlook



## No 1 : Government debt levels = higher taxes, reduced spending



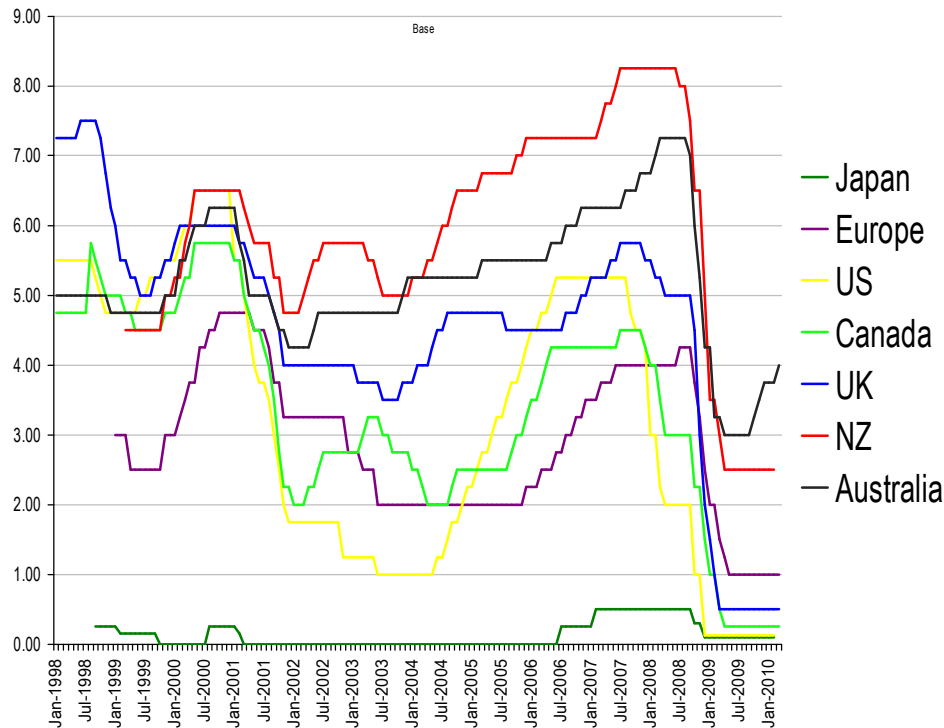
# Risks to the outlook



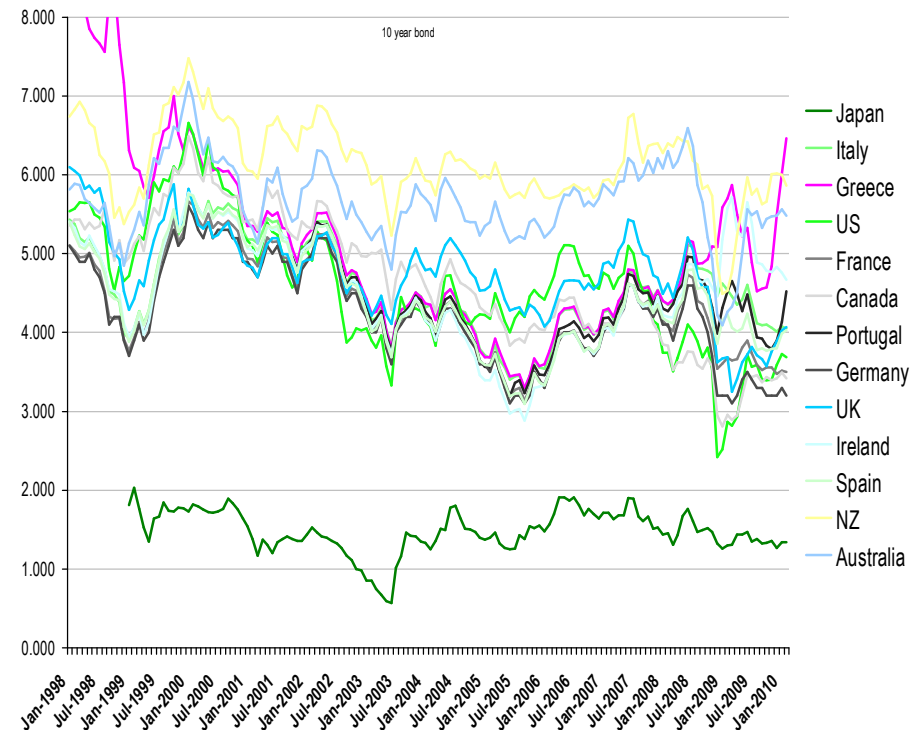
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## No 2 : Interest rates can only go up from here, both headline rates and crowding out

*Intentional rate rises : the base rate*



*Unintentional rate rises : the 10 year bond*



# Risks to the outlook



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**No 3 : Consumer debt levels .... Are consumers stuck in a liquidity trap?**

# Risks to the outlook



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**No 4 :China inflation .... 30% increase in money supply is likely to stoke an inflation problem ... Further tightening?**



Source ISI

# Risks to the outlook



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## No 5 : Donald Rumsfeld's .... Unknown unknowns



*Reports that say that something hasn't happened are always interesting to me, because as we know, there are known knowns; there are things we know we know. We also know there are known unknowns; that is to say we know there are some things we do not know. But there are also unknown unknowns -- the ones we don't know we don't know."*

# Outlook for International equities



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**International equities .... Performance has been poor**

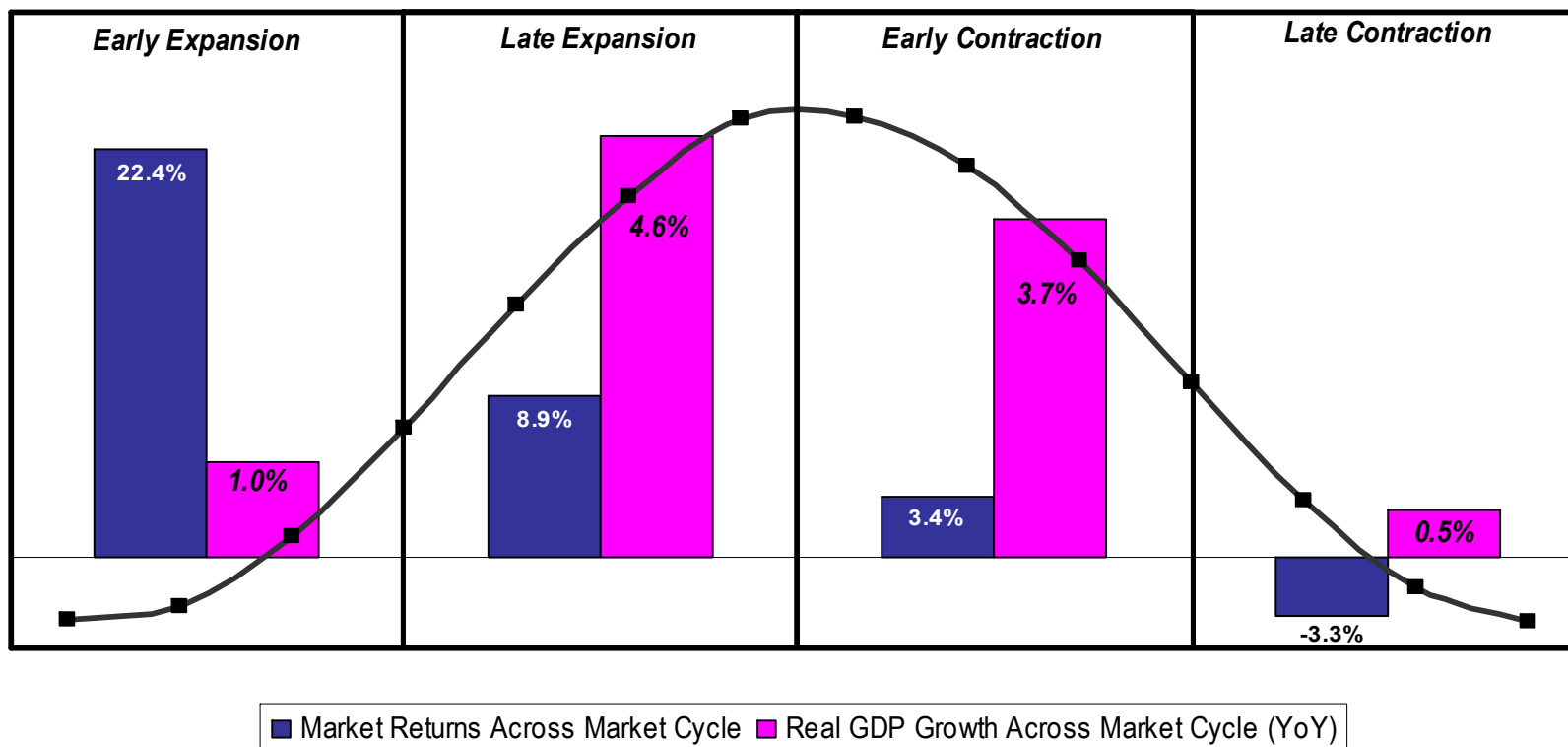
# Outlook for International equities



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**Remember markets are forward looking ... a good year for growth isn't necessarily a good year for equities**

**Outlook For 2010 ... A Year Of Strong GDP, But mild Equity Returns?**

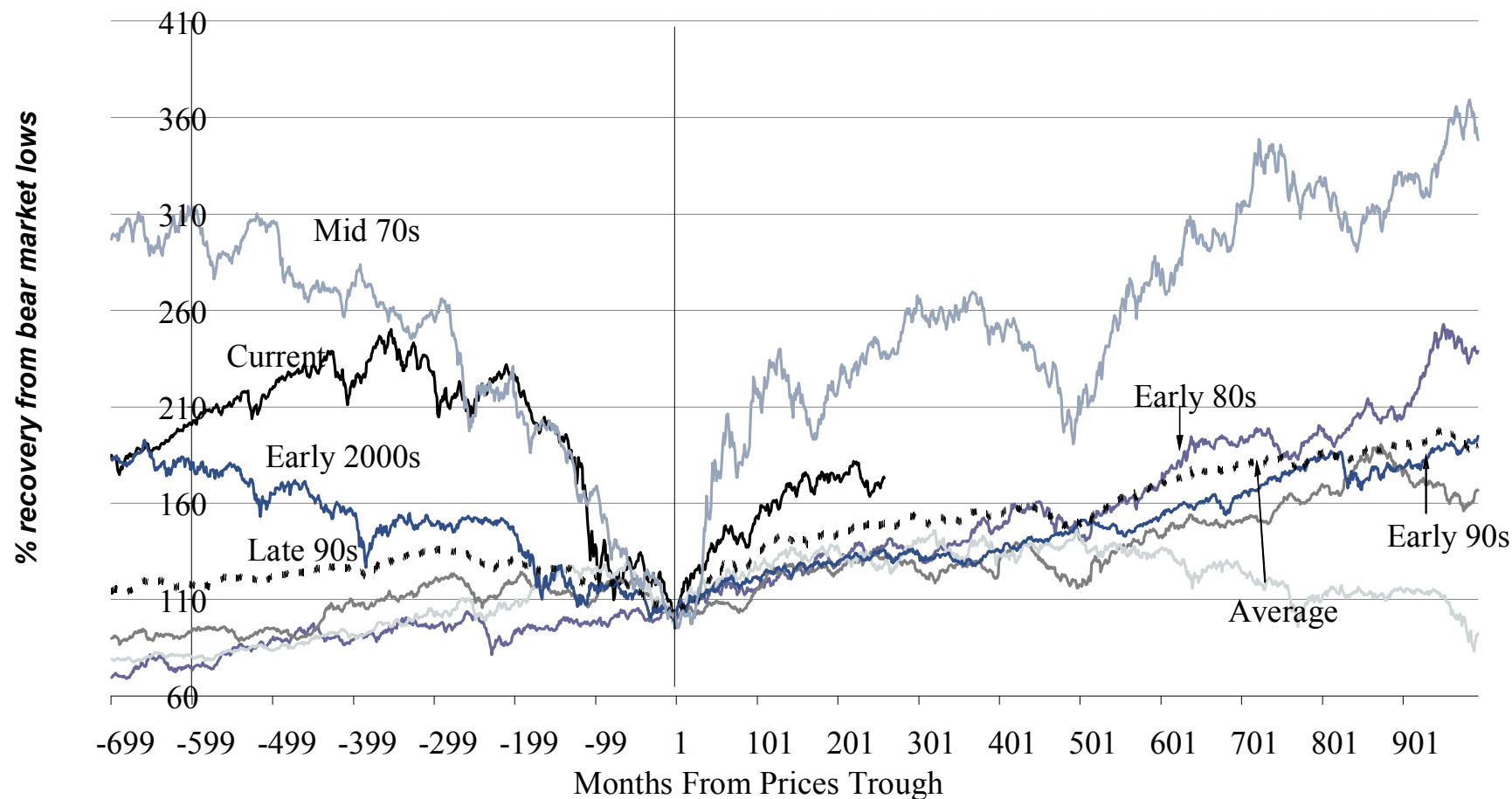


# Outlook for International equities



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## Still plenty to play for in terms of bull market recoveries



Source : Citigroup, Data : FTSE

# Outlook for international equities



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## Market still cheap on trend historical earnings ...

Global price /book on 10 year average earnings



Global price / earnings on 10 year average earnings



Source : Citigroup

# Outlook for international equities



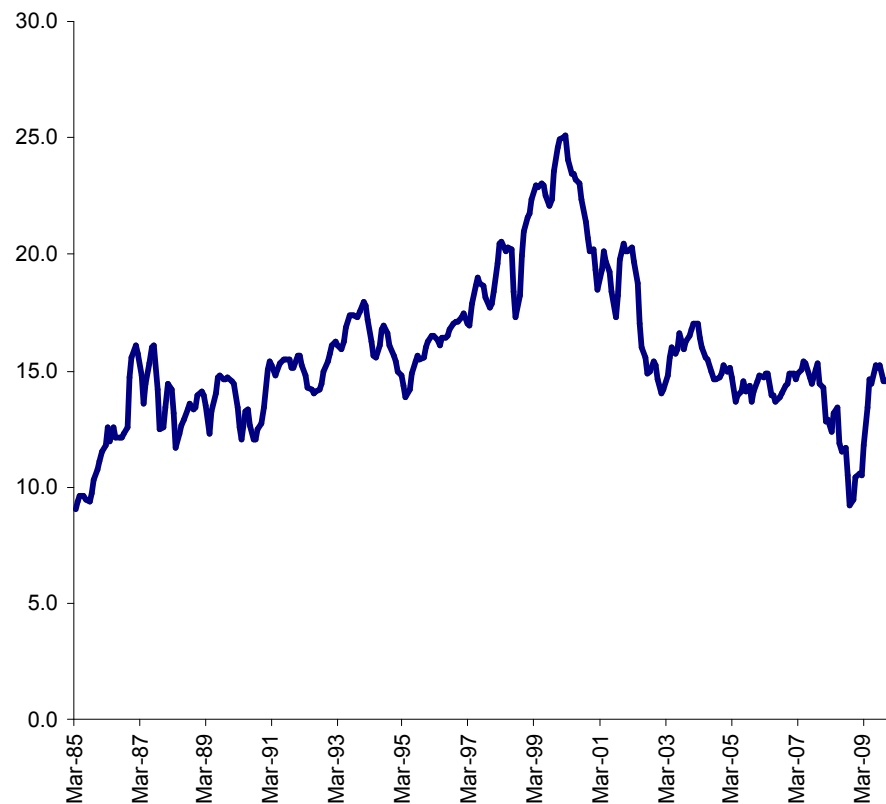
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...fair value on 12 month forward earnings

*MSCI World P/B FY2010*



*MSCI World P/E FY2010*



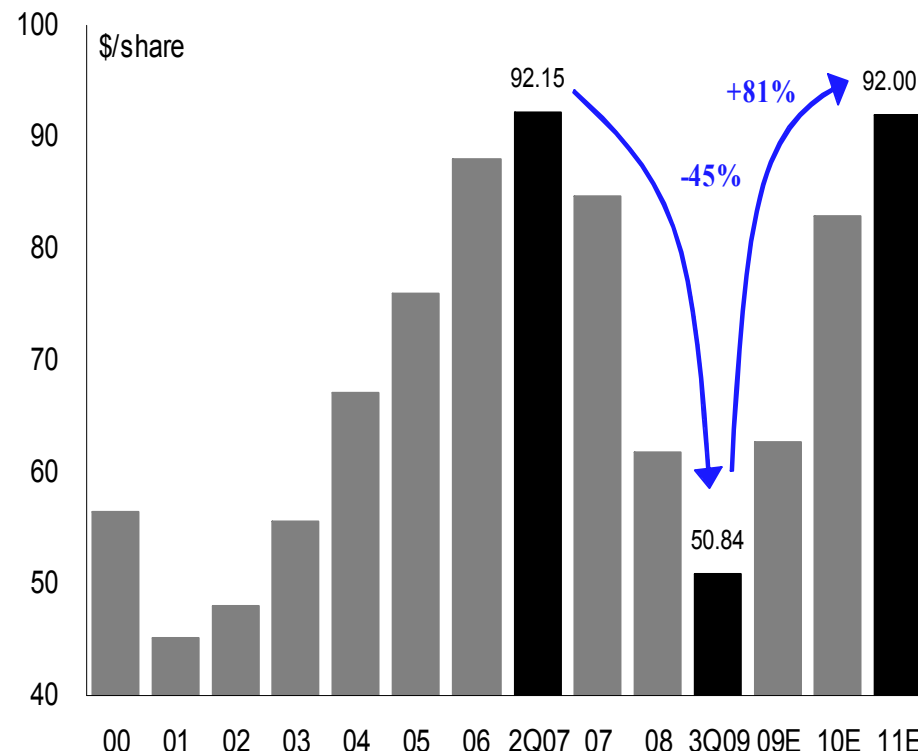
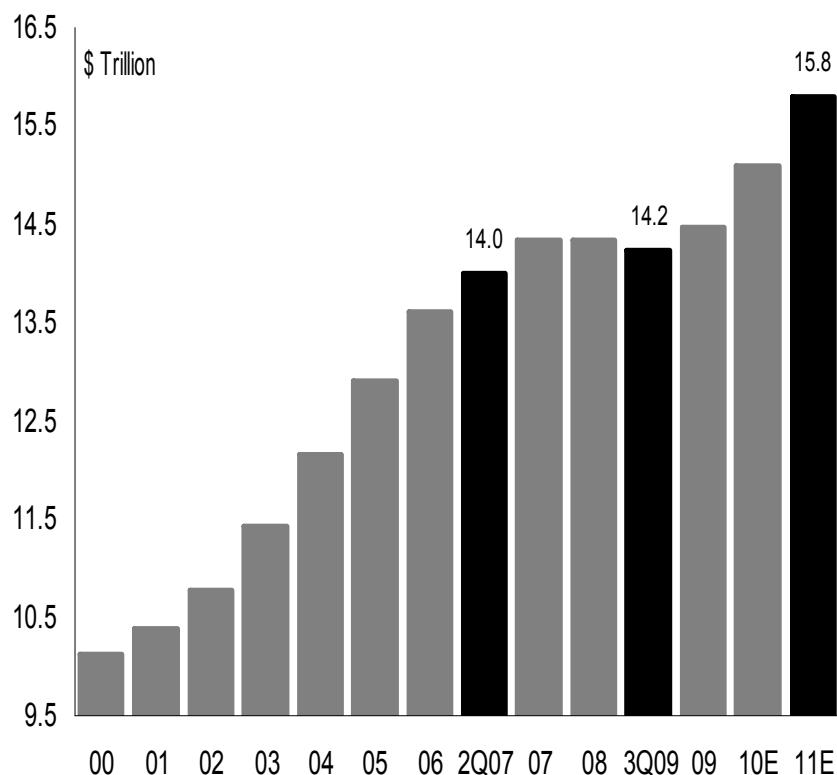
Source : Factset data

# Outlook for international equities



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## GDP data points to undercooked earnings estimates



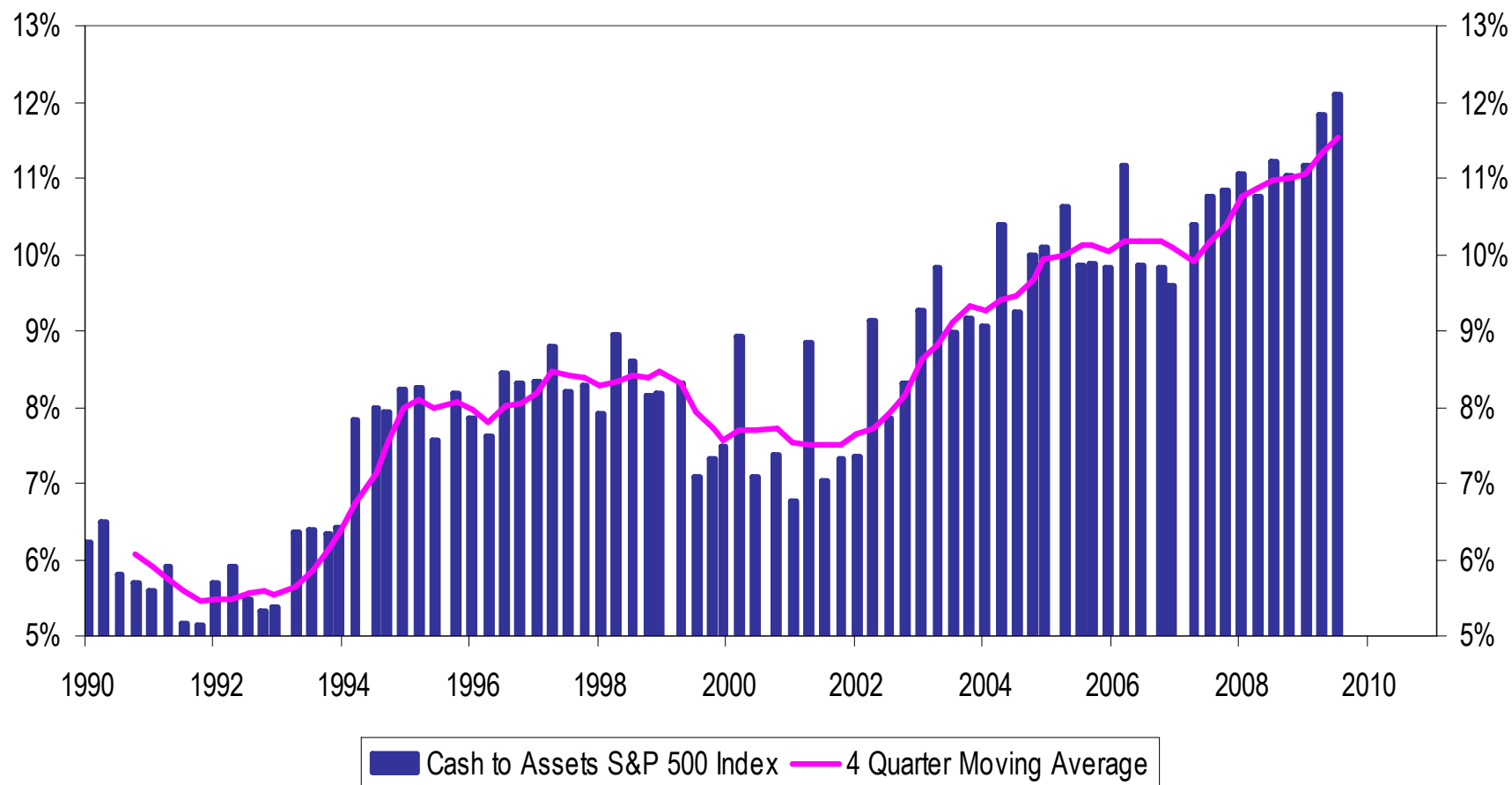
Source : UBS

# Outlook for international equities



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## Record cash levels point to heightened M&A activity



Source : ISI

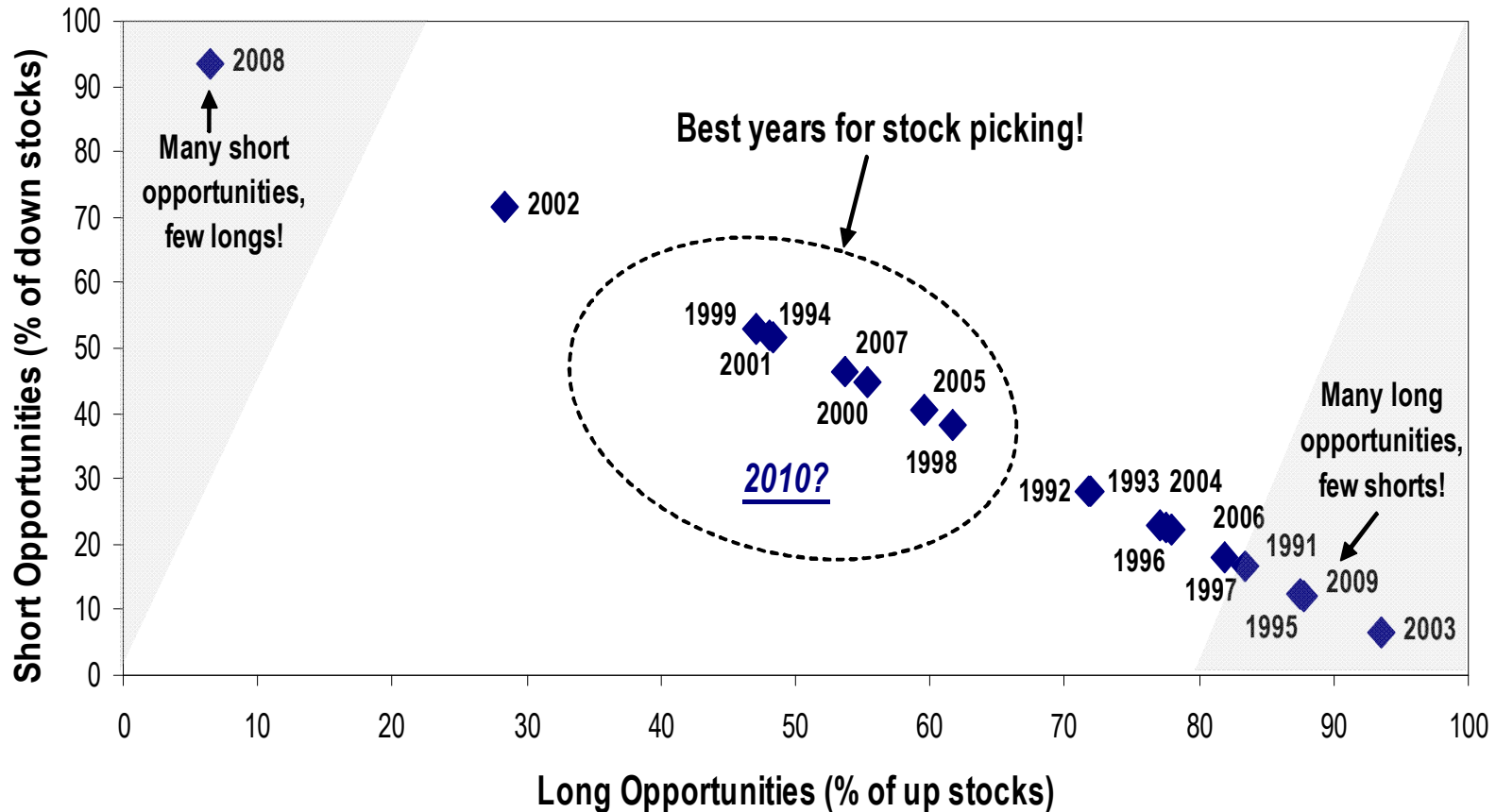
# Current investment themes



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## The major macro event has passed ...time to pick stocks

*It's a stock market! .... Not a market of stocks*



Source ISI, Data : S&P

# Current investment themes



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The world is dominated by mega trends ... and as a global fund we can invest in them.

## **Carbon Economics**

- Low emission power
- Renewable Energy
- Energy Efficiency

## **Band width growth**

- Devices
- Storage
- Content
- Network Infrastructure

## **Reflation**

- Gold
- REITS
- Financials
- Some commodities

## **Baby Boomers**

- Generics v's Big Pharma
- Medicare / Medicaid dependence
- Social Security shortfall
- Extraction of costs out of system

## **Ageing Infrastructure**

- Ageing power grids
- Rail infrastructure
- Roads and Bridges

## **Globalisation**

- Transport Co's
- Freight Co's
- Cross Border transactions
- Port and logistics

# Current investment themes



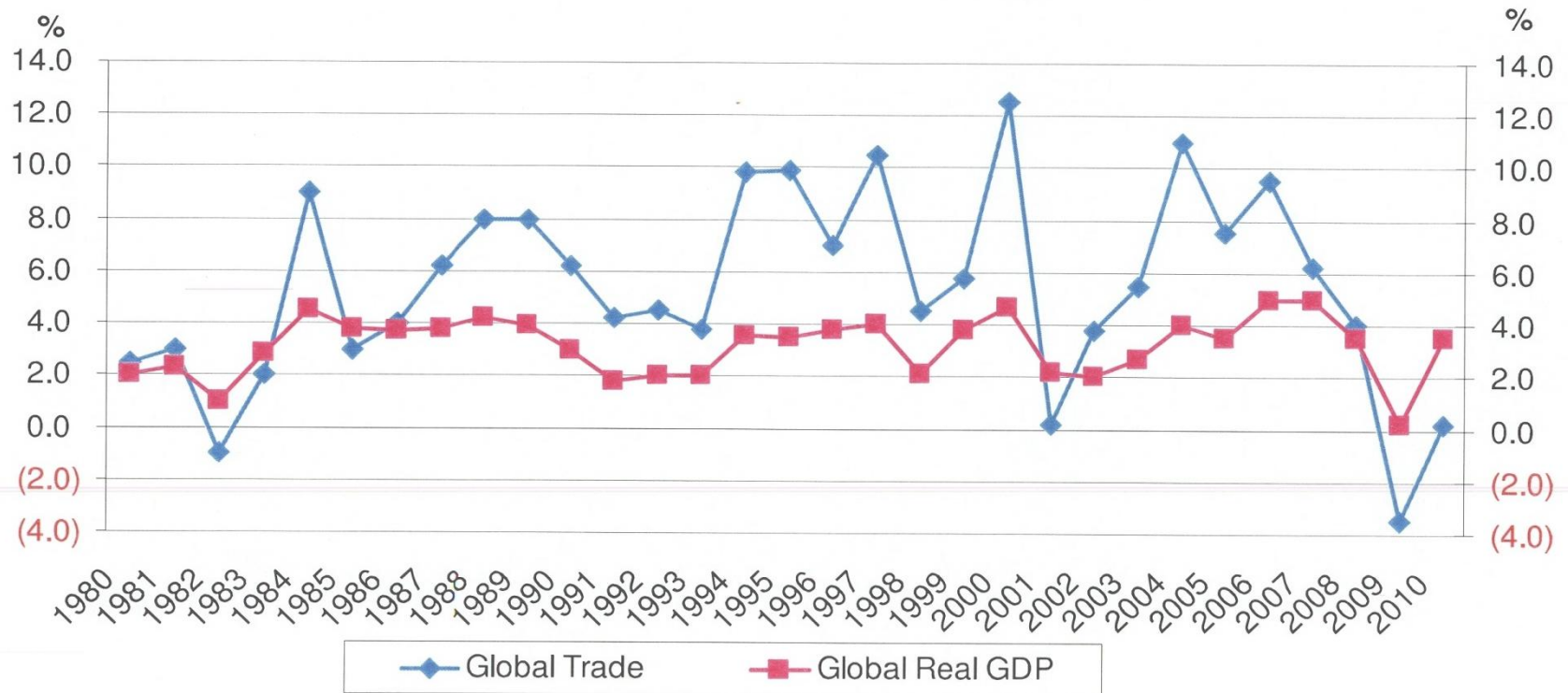
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## Globalisation is making a big comeback ... good for transports

### Global Trade Dynamics vs. Global GDP

Global Trade (Y-o-Y Growth)

Global GDP (Y-o-Y Growth)



# Current investment themes



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## Currencies are only accentuating the trend

### Key Plays

#### •Shippers

- AP Moller
- TUI

#### •Freight

- TNT, Deutsche Post, Fedex, UPS, Toll

#### •Logistics

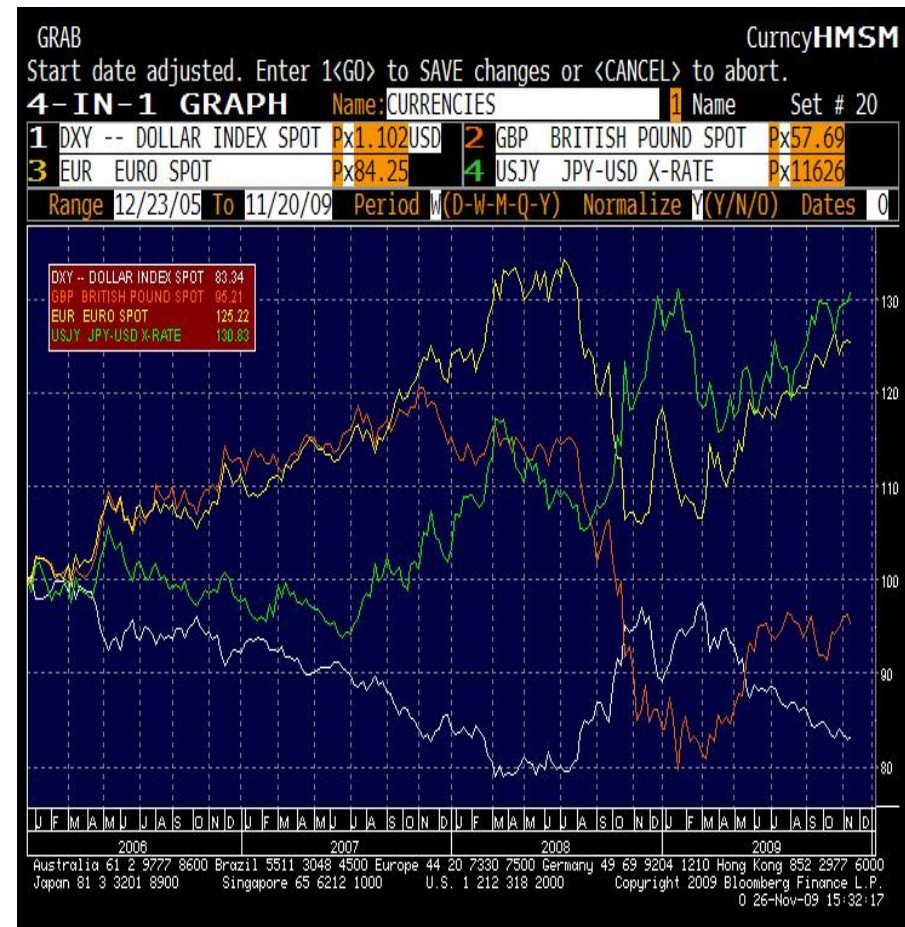
- Kuene and Nagel, Pannilpina, Expeditors

#### •Retail

- EBAY (Pay Pal), Visa , Mastercard

#### •Port Handling Logistics

- Cargotec, Boskalis, Hamberg Ports, Asciano, COSCO Pacific, Vopak



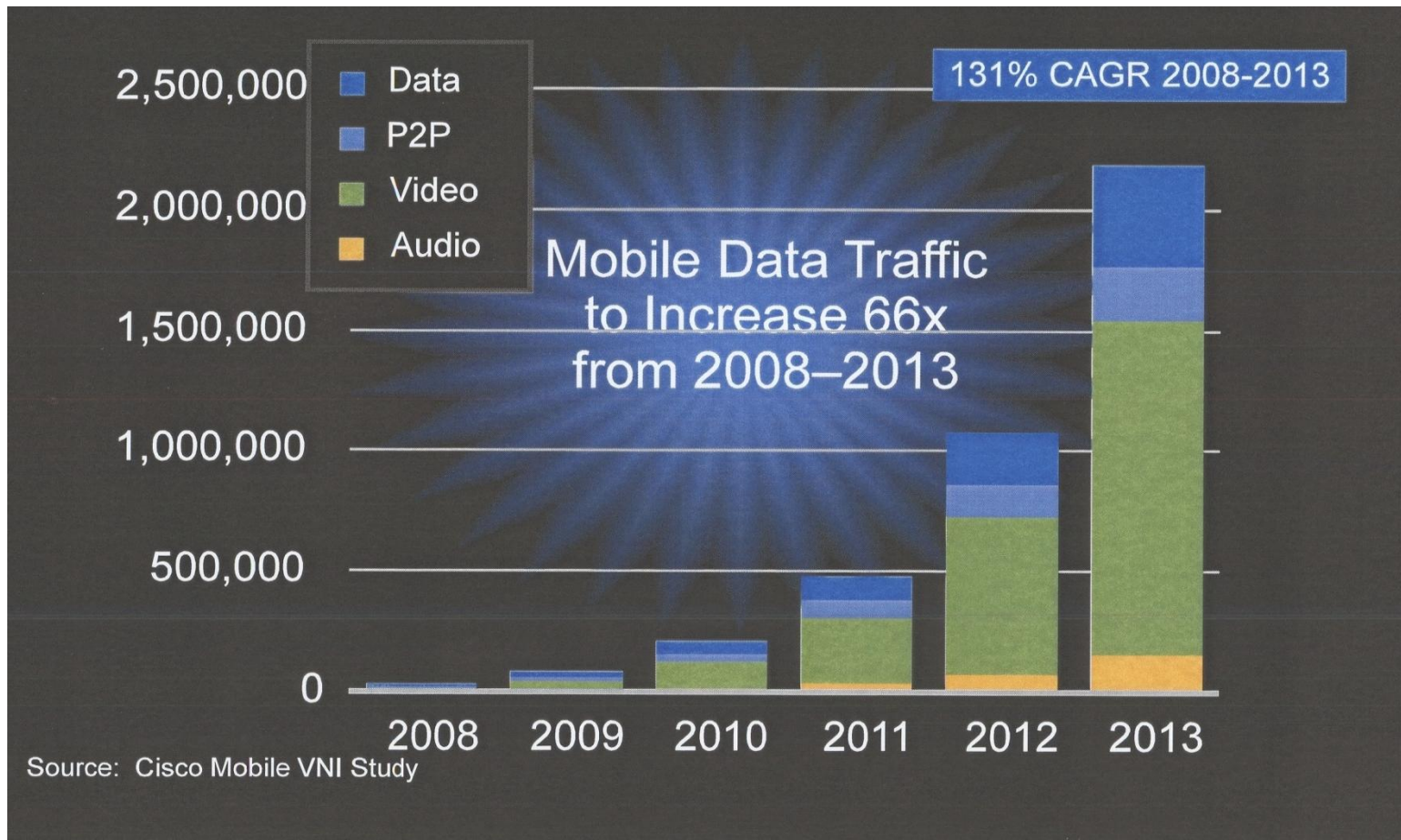
Source : Bloomberg

# Current investment themes



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## Band width .... Exponential growth as the internet goes mobile



Source : Cisco

# Current investment themes



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## Band width .... Exponential growth on the internet and mobile

### Devices

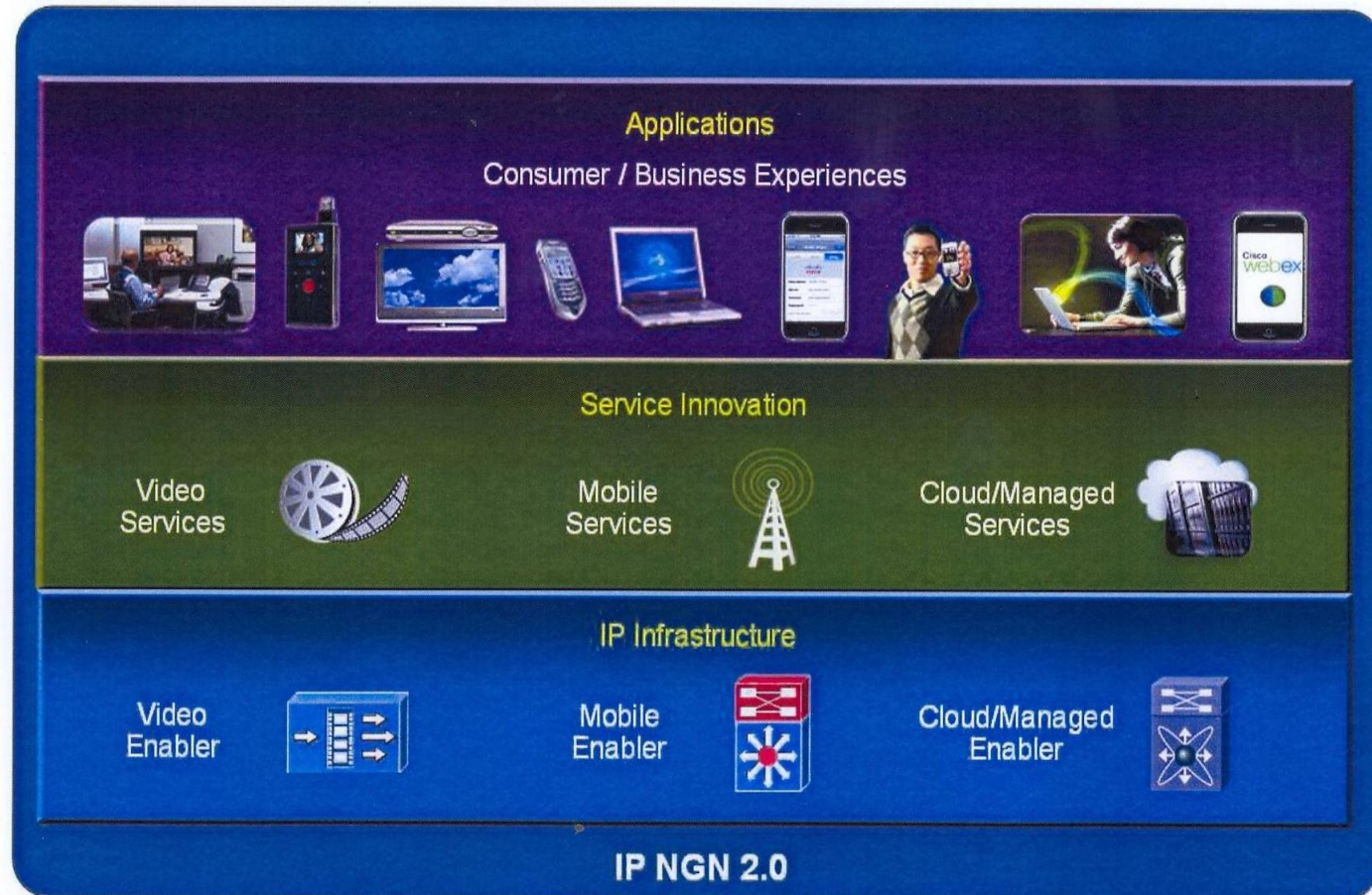
- Apple, RIMM, Qualcomm, HP

### Content / storage

- Google, American Tower, Digital Multimedia, Telecity, Equinix, Pay TV providers, SES Global

### Network Infrastructure

- Cisco, EMC, Juniper Networks, Finisar, Security Co's



Source : Cisco



## We run the currency from an Australian investors perspective

- Positives
- Higher US growth adds to commodity demand
- Sovereign debt concerns attracts focus to Australia's low Government debt position (impact is fading)
- Any appreciation of the Chinese currency will have a positive impact for the AUD
- Australia continues to be seen as a defensive exposure to Asia's growth
- Attractive interest rate differentials with high nominal interest rates (4.0%)
- Spot commodity prices remain high
- Domestic residential property market is overheating which will keep pressure on interest rates.

AUD Hedging % - K2 Select International Fund  
January 2005 - February 2010



- Negatives
- Recovering US economic activity will:
  - a/. raise demand for USD
  - b/. increase expectations of higher short term interest rates
  - c/. Lower the budget deficit as tax revenues recover
- Chinese monetary tightening may translate into a sharp fall in the rate of bank loan growth & lower GDP growth
- RBA may slow monetary tightening if economic recovery slows with less government stimulus
- Carry Trade unwinding
- China's commodity demand has moderated in the last couple of months
- Commodity inventories are building

# What we are saying in 2010



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## Summary

- An economic recovery is now in motion in most major economies
- Consequently 2010 and 2011 are likely to be recovery years for both economic growth and global earnings.
- Markets have priced in some of this recovery, but are not expensive on most measures and in our view have not factored in enough of an earnings recovery.
- Clearly the crisis has created many legacy issues which we need to watch carefully, but on balance we feel equity markets can 'climb the wall of worry' through 2010 and deliver competitive returns versus other asset classes
- Legacy issues point to out performance from emerging markets over western markets over the long term ... short term the market may be underestimating the rebound in the US
- The major macro event has passed, barring any unforeseen events, returns expectations from here will be muted on the up and the downside .... stock picking will become the major determinant of outperformance going forward.