

About this Review	
Sector Reviewed	<b>Australian Small Companies</b>
Total Funds Rated	28
Date of this Sector Review	April 2009
About this Fund	
Fund Reviewed	<b>Ausbil Australian Emerging Leaders Fund</b>
Fund Size (\$M)	\$480
Responsible Entity	Ausbil Dexia Ltd
Fund Commenced	May 2002
Retail Fee (p.a.)	N/A
Wholesale Fee (p.a.)	0.85% + Performance Fee of 15% of Fund Returns above the Benchmark Index
Structure Availability	Platforms, Wholesale
About the Fund Manager	
Fund Manager	Ausbil Dexia Ltd
Ownership	70% Dexia Asset Management, 30% Ausbil Dexia staff
Assets Managed in this Sector (\$M)	578
Years Managing this Asset Class	10
Investment Team	
Team Size Dedicated to this Fund	13
Portfolio Manager	Paul Xiradis, John Grace, Adam Dixon
Number of Analysts	11
Departures/Team Ratio (past 2 years)	29%
Investment Process	
Style	'Core' / 'Rotational'
Targeted Value Add Above Index (p.a.)	3.0%
Typical Tracking Error (p.a.)	4.5% - 5.5% (max 6%)
Typical Stock Numbers	30-40
Typical Capitalisation Bias	70% mid cap / 30% small cap
Franking Level (FY08)	70%
Tax Efficiency – Income in Total Distribution (FY08)	99%
Discount Gains as % of Total Capital Gains (FY08)	100%
Maximum of Portfolio in any One Stock	10%
Maximum of Portfolio in any One Sector	No hard limits
Maximum of issued capital of any one stock	10%
Minimum Capitalisation (\$M)	200 <sup>th</sup> stock by market capitalisation
Maximum Size Limit of Fund (\$M)	1,200
Fund Rating History	
April 2009	Highly Recommended
May 2008	Highly Recommended
February 2007	Highly Recommended
February 2006	Highly Recommended

## What this Rating means

➤ The Highly Recommended rating indicates that Lonsec has high conviction that the fund or product can achieve its objectives and, if applicable, outperform peers over an appropriate investment timeframe. The manager or product has strong competitive advantages in people, process and product design and has no areas of material weakness. The investment is a preferred entry point to access this asset class or strategy.

## Using this Fund

- This is General Advice only and should be read in conjunction with the Disclaimer, Disclosure and Warning on the final page.
- Advisers should note that this Fund has a bias towards mid-cap stocks, and as such is not a direct replacement for a 'traditional' small caps fund. In Lonsec's opinion the Fund should be used to complement a large cap (top 50) exposure in clients' portfolios up to 15% of the total portfolio, depending on client risk preferences. Lonsec would caution investors regarding the appropriateness of using both this Fund and the Ausbil Australian Active Equity Fund in the same portfolio, given the mid cap overlap
- The Fund is subject to equity market risk and movements (both positive and negative) in the share prices of the underlying securities in the portfolio. Investors should therefore be aware that the Fund may experience periods of negative returns and that there is a risk of potential capital losses being incurred on their investment.

## Changes since Previous Lonsec Review

- Tony Waters was hired as an equities analyst, joining the team in October 2008. Waters comes from a sell side background. Tony was also offered equity in the business.
- Sarah Lau who has been with Ausbil for 1.5 years is now a fully fledged equities analyst. Previously she held an assistant analyst role.

## Lonsec Opinion of this Fund

### Philosophy (Style)

- Ausbil's investment philosophy of focusing on company earnings and the belief that earnings revisions ultimately drive share prices has been adhered to by the manager since the inception of the Fund in 2002.
- Ausbil has been able to execute this philosophy with a high level of success which is backed-up by the manager's solid performance track record over the long term covering various investment cycles.
- The Ausbil Emerging Leaders Fund is differentiated to peers in the Lonsec Australian equity small cap sector by its bias to 'mid' cap stocks (ASX 51 -100 stocks by market capitalisation), as opposed to 'small' cap stocks (ex ASX 100 stocks by market capitalisation).

## People and Resources

- Lonsec views the depth and experience of the key members of the investment team to be a key competitive advantage of the manager. Importantly, key members of the team have managed money over various investment cycles which Lonsec believes is beneficial in volatile markets. There have not been any departures from the senior ranks within the team, with senior members of the team having been with Ausbil for seven years or more.
- While Lonsec considers the risk of a departure from within the senior ranks of the investment team to be low, 'key person risk' means that the Fund's rating is more susceptible to a downgrade in the event of the departure of the key person.
- As noted in the previous review of this Fund, Ben McGarry left the team in April 2008 after being with Ausbil for approximately one year. Ausbil subsequently hired Tony Waters, which Lonsec believes should cover any gaps resulting from Ben's departure.
- As noted in the last review of this Fund, Ausbil has broadened the equity ownership within the business to incorporate most members of the investment team. Currently all analysts, apart from Sarah Lau (Equities Analyst), have an equity stake within the business. Lonsec believes that providing equity ownership should reduce the level of staff turnover that the manager has experienced in the junior to mid level analyst ranks. Lonsec believes that having 'skin in the game' more closely aligns the interests of the business and investors. Overall, Lonsec believes the manager's alignment of interests to be moderate to high.
- Ausbil Dexia has indicated that the capital raising by the Dexia Group has no impact on the local asset management business. Ausbil Dexia (joint venture between Dexia Asset Management and the Ausbil Australian team) is well capitalised with no gearing. The manager has also indicated that in the worst case scenario, where Dexia's asset management business was sold, the Australian business could continue to operate as a stand alone entity.
- Ausbil runs an internship program with the University of New South Wales which provides students with work experience within the managed fund industry, at the same time providing Ausbil with a potential recruitment source for junior analysts. Lonsec views this positively, as having a mix of youth and experience within the team is important for future succession planning and growth.
- Ausbil has indicated that they have not had to reduce staff at this stage as a result of the market downturn. The manager did indicate that additional hires have been deferred. Lonsec does not believe that there are any notable gaps in the current investment team requiring immediate additional resources.

## Research and Portfolio Construction

- Ausbil's research process has been applied consistently since the inception of the fund. The combination of top-down inputs with bottom-up up stock research has been applied effectively over various investment environments. Lonsec believes that the manager's research and portfolio

construction process provides the flexibility to tilt the portfolio to take advantage of prevailing market environments.

- Lonsec believes that Ausbil's stock ranking model serves to promote a strong level of consistency in valuation across all stocks in the manager's investable universe. The bias towards PE relativities is also considered appropriate given the manager's focus on earnings and earnings revisions.
- Given the importance of 'top-down' analysis to the investment process, Lonsec is particularly pleased that this insight is obtained in-house. The manager conducted approximately 460 direct company visits over the last year which is consistent with its 'bottom-up' research effort. Pleasingly the manager has indicated that it intends to increase the number of company visits and it does not intend to reduce its travel budget.

## Risk Management

- Lonsec believes that Ausbil's risk management processes are in line with industry practices. The manager adequately monitors all of the relevant risk factors within its portfolio covering aspects such as stock and sector risk. The manager currently uses the Goldman Sachs JB Were risk management tool.

## Performance

- The manager has consistently been able to add value over all periods assessed (1, 2, 3 and 5 years) as at 31 January 2009 both against the S&P/ASX Small Ordinaries Index as well as a composite index (70% Midcap 50 and 30% Small Ordinaries Index).

## Fund Size

- Lonsec believes that Ausbil has sufficient fund capacity in order to effectively execute its investment strategy for this fund. As at 31 December 2008, Ausbil's total funds under management (FUM) in the Ausbil Emerging Leaders Fund was \$578 million (trust and mandate strategy). The manager's fund mandate, which is biased towards mid capitalisation stocks, should enable the manager to manage higher FUM relative to traditional small cap managers who invest further down the market capitalisation spectrum and hence face greater liquidity pressures.

## Overall

- Lonsec has rated the Ausbil Australian Emerging Leaders Fund as Highly Recommended. This is primarily based on Lonsec's high regard for the senior members of the manager's investment team and the effective implementation of the manager's investment process which has been applied consistently since the inception of the Fund.
- Lonsec considers a key strength of this Fund to be the depth of experience the manager has within its senior ranks. Senior members within the team have considerable industry experience and have managed money in various market cycles. Lonsec believes that this experience will be critical in a period where market volatility has increased.
- Lonsec believes that the level of staff turnover within the mid to junior experienced members of the team may reduce as a result of the broadening of equity ownership within the team.

- The manager’s investment process, which incorporates both top-down inputs with bottom-up stock research has been well executed and is reflected in the Fund having outperformed the benchmark over most periods.
- Lonsec believes that the Fund continues to have sufficient capacity to manage this Fund effectively.

## People & Resources

### Size and Experience

Ausbil does not have a specialist team dedicated solely to the Emerging Leaders Fund (mid / small cap fund). Rather, the investment team is responsible for researching stocks across the full market capitalisation spectrum, and for managing both Ausbil’s large and mid/ small cap fund. In total, Ausbil’s investment team consists of nine personnel, including seven with direct stock analysis responsibilities. The investment team also benefits from the resources of two dedicated dealing resources and two quantitative analysts. The team (excluding the quant and dealing resources) has an average of approximately 16 years of industry experience which is slightly above the Lonsec peer group average in the small cap Australian equity sector.

The CEO and Head of Equities is Paul Xiradis. Xiradis has approximately 30 years of industry experience including previous senior roles at Legal and General Asset Management and BZW Investment Management. Lonsec considers Xiradis to be a high quality and experienced investment professional. Xiradis maintains a ‘hands on’ approach to portfolio construction, investment strategy, and in driving the overall investment management process.

Xiradis is supported by Deputy Head of Equities John Grace and Portfolio Manager Adam Dixon. These three team members form the Portfolio Construction Committee. Grace and Dixon have 24 years and 14 years industry experience respectively. The Head of Research and Chief Economist is John Honan, who also has a significant 31 years industry experience. Honan is a key input during the ‘top-down’ (macroeconomic) phase of the investment process.

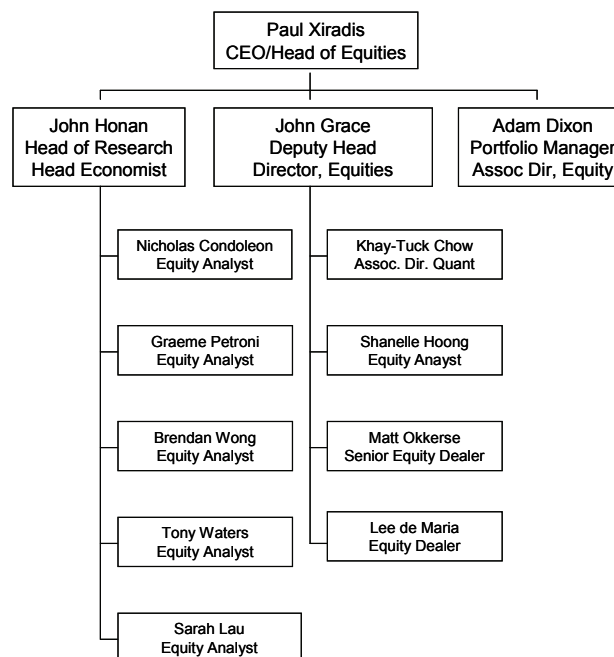
Ausbil has a joint venture agreement with the Dexia Group (Dexia), a large European bank and fund manager with global FUM of approximately \$161 billion. Dexia, provides compliance support to Ausbil, which in turn markets their global equity socially responsible investment SRI offering in Australia. Lonsec is pleased with this structure, noting that it allows Ausbil to manage money as a ‘boutique’, whilst enjoying the support of a large global banking group.

On 30 September 2008 Dexia announced that it will receive a EUR 6.4 billion capital injection from the governments of Belgium, France and Luxembourg and from existing shareholders. The capital raising aims to secure the solvency of the Group. Dexia expects its Tier 1 capital ratio (measure of a bank’s capital adequacy), at the end of September 2008, before the capital increase, to be above 10%. Following the capital injection Dexia, should remain one of the better capitalised banks in Europe.

One part of Dexia’s business that remained under pressure was Financial Security Assurance (FSA), a subsidiary of Dexia that deals in credit reinsurance. Ausbil Dexia indicated

to Lonsec that FSA did not make up a significant portion of Dexia’s overall business. On the 14<sup>th</sup> November 2008, Dexia announced it had entered into a binding agreement to sell FSA Holdings to Assured Guaranty Ltd (a bond insurer listed on the New York Stock Exchange). Subsequent to the announcement Ausbil has confirmed that Dexia has sold the majority of FSA, retaining only a small equity interest in the company. The parent company has also undertaken a review of its operations and has subsequently closed down its lending centres outside its home country.

### Team Structure



Xiradis, Grace, and Dixon are the co-portfolio managers of the Fund although Xiradis, as Head of Equities, has final decision making authority and is ultimately accountable for the performance of the Fund. A committee based decision making structure is used in determining the final portfolio with the focus being on determining the stock weightings rather than the actual stocks to be included in the portfolio. Grace and Dixon also have some stock analysis responsibility in addition to their portfolio management roles. Supporting the portfolio managers are six equity analysts who are each allocated sector responsibilities. ‘Top-down’ inputs are sourced from Chief Economist, Honan and are an important part of the investment process.

This is to ensure that accountability is maintained and that decisions can be made swiftly. Lonsec notes that Honan has assumed the Head of Research role (previously held by John Grace) following a restructure of roles, and all equity analysts now report to him.

Lonsec believes that ‘key person risk’ lies primarily with Xiradis, given that he has been instrumental in the development of both the investment process and the investment team. This risk is partly mitigated by the equity ownership structure in place at Ausbil for senior members of the investment team.

Whilst client service and IT functions are conducted in-house, Fund administration and other back office functions are outsourced to National Custodian Services.

## Turnover

Historically, Ausbil has enjoyed a very stable organisational structure, however over the last 12 to 18 months staff turnover has been moderate to high.

As noted in the previous review of this Fund, Ben McGarry departed the team in April 2008. McGarry was with Ausbil for approximately one year and left the organisation to join a private hedge fund manager.

Subsequent to his departure, Ausbil hired Tony Waters in October 2008. Waters has eight years worth of analytical experience largely as a sell side analyst, however most recently he worked at Investors Mutual for a short period of time, where he held the position of Equity Analyst.

Despite the staff turnover the manager has been able to replace departed analysts and importantly none of the key decision makers have left the team.

## Remuneration / Alignment of Interests

Ausbil operates a team performance incentive program. A maximum of 80% of portfolio manager and analyst variable remuneration is linked to fund outperformance of the benchmark. For portfolio managers, an additional 10% of variable remuneration is linked to business profitability and 10% is based on subjective factors. For analysts, an additional 10% of variable remuneration is linked to stock calls (irrespective of inclusion in the final portfolio) and 10% is based on subjective factors. In addition, senior investment personnel including Xiradis, Grace, Dixon and Honan all have equity stakes in the business.

Ausbil has broadened the equity base within the business with all analysts apart from Sarah Lau having equity.

Ausbil is entitled to a performance fee of 15% of gross returns above the benchmark index (index being a composite consisting of 70% S&P/ASX Midcap 50 Accumulation Index and 30% S&P/ASX Small Ordinaries Accumulation Index), which further assists in the alignment of interests.

## Investment Style

### Style

Ausbil is an active Australian equities fund manager utilising a fundamental 'bottom-up' research approach combined with a 'top-down' overlay. The investment style adopted by the manager is 'core'/'rotational' and the Fund will generally be invested in mid and small cap stocks (bias to mid caps). At different points in time the portfolio may display a 'value' or 'growth' tilt, however over a full market cycle the portfolio is not expected to exhibit any notable style bias.

### Investment Philosophies and Beliefs

Ausbil believes that company earnings and earnings revisions drive stock prices and that investors focus too heavily on present conditions and do not adequately consider the impact of longer-term factors (e.g. changes in the earnings profile of a stock or sector). The manager therefore believes that the key to outperformance is the early identification of earnings revisions and being able to pre-empt stock price movements. By adopting a 'core' approach, Ausbil believes that the Fund should be able to outperform

throughout the full market cycle by exploiting these short-term inefficiencies.

## Research Approach

### Overview

Investment Style	Core/Rotational
No. of stocks in universe	157
No. of stocks fully modeled	86
No. of stocks partially modeled	Balance modelled by proprietary database
Key Screens	Liquidity and market capitalization, proprietary database
Top-Down	15% Top down Macro economic, sector factors
Bottom-Up	85% bottom up stock specific
Qualitative Analysis	Structured
Research Inputs	Site visits – companies, suppliers & competitors
Use of broker research	Secondary input into decision making. Draw data to establish market consensus view

## Valuation Approach

Primary	Relative Price to Earnings Ratios (Total expected relative return, consensus earnings revisions, two year EPS growth)
Secondary	Discounted Cash Flow Model (DCF)

## Portfolio Construction

Portfolio construction is undertaken by the Portfolio Construction Committee which consists of three senior members of the equities team (Xiradis, Grace, and Dixon). Each member produces their own model portfolio, aiming to overweight stocks that are in the preferred sectors, have 'positive' ratings from the analyst and rank well in the FERRET model (proprietary stock ranking model). Consideration is also given to liquidity, Tracking Error, the relative attractiveness of the 'positive' rated stocks and an overall intuitive assessment. As individual stocks are thoroughly debated during the research process there is usually high continuity of stock candidates across the three model portfolios. As such, when the Portfolio Construction Committee collectively determines the final portfolio, the focus is on determining stock weightings as opposed to selecting the actual stocks. The final portfolio is relatively concentrated and typically includes 30 to 40 stocks.

Since Lonsec's last review there have been no major changes to the manager's portfolio construction process.

Positions in stocks that enter the ASX 50 must generally be exited within a one month timeframe, however some discretion is permitted.

## Risk Monitoring

On a monthly basis, a Goldman Sachs JB Were portfolio analysis tool is utilised to monitor risk within the portfolio. Output from the tool includes the Fund's Tracking Error, primary stocks contributing to risk and major stock and sector positions. In addition, the manager has adopted disciplined sell triggers, which act as an additional risk management mechanism.

Ausbil has an external compliance committee that meets on a quarterly basis and is also subject to both an annual internal (Dexia) and external (PricewaterhouseCoopers) audit.

## Funds under Management

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Ausbil currently manages approximately \$480m (\$578m, trust and mandate) in the Emerging Leaders Fund, which makes Ausbil one of the larger managers in terms of FUM in this sector. The Fund's bias to 'mid' cap stocks means that liquidity and size issues are less of a concern compared to traditional 'small cap' managers.

Lonsec notes that Ausbil has pre-determined a FUM level (\$1.2 billion for this strategy) upon which the Fund will be closed. At current FUM, the manager is at approximately 70% (this figure may change with market movements and stock liquidity) capacity and Lonsec would be disappointed to see inflow in excess of limits stated. In total, Ausbil currently manages approximately \$6.4 billion in Australian equities.

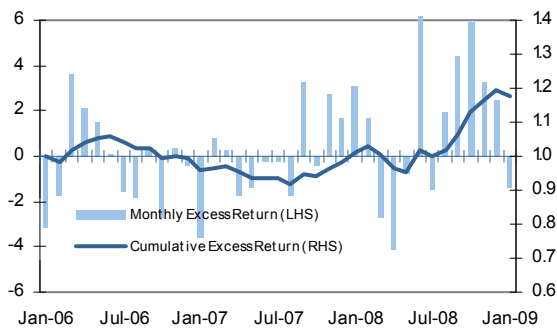
**Quantitative Performance Analysis**  
**Annualised after-fee % returns as at 31 January 2009**

	1 Year		2 Years		3 Years		5 Years	
	Fund	Peer Group	Fund	Peer Group	Fund	Peer Group	Fund	Peer Group
Performance (% pa)	-37.4	-44.3	-19.0	-25.6	-6.0	-8.5	9.1	3.5
Standard Deviation (% pa)	26.0	27.7	23.0	25.1	20.7	22.9	18.0	19.7
Excess Return (% pa)	10.5	3.6	9.4	2.7	6.2	3.7	7.9	2.3
Outperformance Ratio (%)	58.3	53.2	54.2	55.0	52.8	56.3	56.7	55.0
Worst Drawdown (%)	-40.7	-46.2	-45.5	-54.5	-45.5	-54.5	-45.5	-55.0
Time to Recovery (mths)	na	0.0	na	0.0	na	0.0	na	0.0
Sharpe Ratio	-1.7	-1.9	-1.1	-1.3	-0.6	-0.7	0.2	-0.1
Information Ratio	0.9	0.3	1.0	0.4	0.7	0.5	1.0	0.4
Tracking Error (% pa)	11.8	11.8	9.4	9.3	8.9	8.5	7.8	7.5

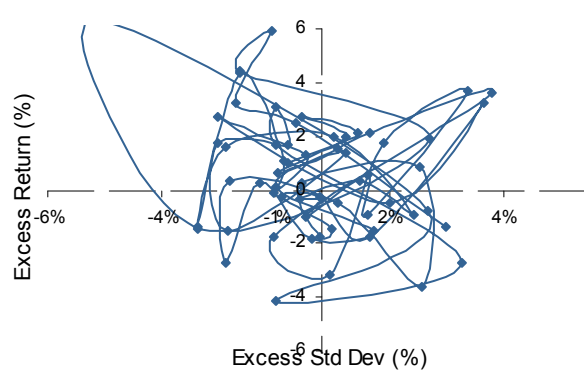
Fund: Ausbil Emerging Leaders Fund, Peer Group: Average among Lonsec Rated Australian Equity (Small Cap) Manager Universe Benchmark: S&P/ASX Small Ordinaries Accumulation Index

*\*Ausbil's internal benchmark for the Fund is a composite index consisting of 70% S&P/ASX Midcap 50 Accumulation Index and 30% S&P/ASX Small Ordinaries Accumulation Index*

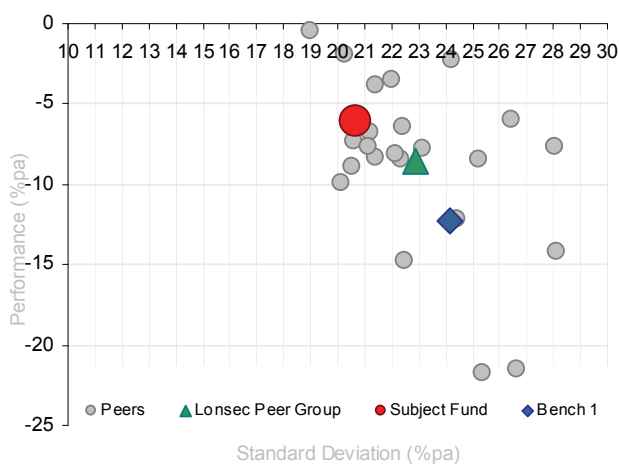
**Cumulative Performance over three years**



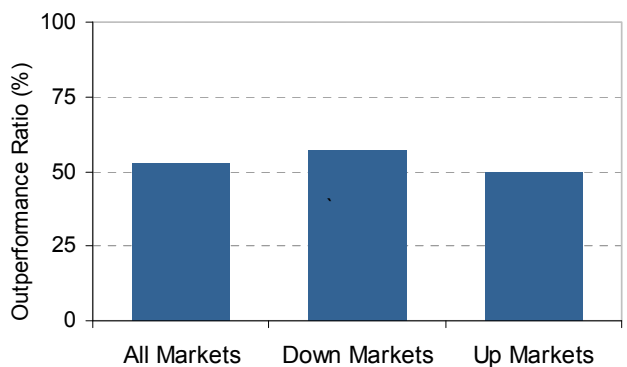
**Snail Trail over five years**



**Risk-Return Chart over three years**



**Outperformance Consistency over three years**



## Glossary

<b>Absolute Return</b>	'Top line' actual return, after fees
<b>Excess Return</b>	Return in excess of the benchmark return
<b>Standard Deviation</b>	Volatility of monthly Absolute Returns
<b>Tracking Error</b>	Volatility of monthly Excess Returns against the benchmark (the Standard Deviation of monthly Excess Returns)
<b>Sharpe Ratio</b>	Absolute reward for absolute risk taken (outperformance of the risk free return (Bank Bills) / Standard Deviation)
<b>Information Ratio</b>	Relative reward for relative risk taken (Excess Returns / Tracking Error)
<b>Worst Drawdown</b>	The worst cumulative loss ('peak to trough') experienced over the period assessed
<b>Time to Recovery</b>	The number of months taken to recover the Worst Drawdown

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**Date Prepared: April 2009**  
**Analyst: Lukasz de Pourbaix**  
**Release Authorised by: Paul Pavlidis**

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