6 INDUSTRY OVERVIEW

6.1 THE CLOSED-END FUND INDUSTRY

A Brief History

CEFs, or investment trusts as they are commonly known in the UK, have been around a lot longer than unit trusts. The oldest, Foreign & Colonial Investment Trust Plc, made its debut way back in 1868. Its stated objectives were *"to give the investor of moderate means the same advantages as the large capitalist in diminishing the risk of investing in Foreign and Colonial Government Stocks, by spreading the investment over a number of stocks"*.

During the 'Roaring Twenties', CEFs mushroomed in the US. This was a time of immense economic, political and social prosperity. But during the Great Crash of 1929, CEFs were among the worst hit. The fault lies in the extensive use of borrowings by fund managers, pyramiding (funds buying other funds), and shenanigans. Although various legislations were introduced to regulate the industry and protect shareholders, CEFs remained sidelined for decades, eventually becoming overshadowed by open-end funds or unit trusts.

CEFs or investment trusts in the UK managed to escape the Great Crash of 1929 almost unscathed. In the early 1930s, investment trusts in the UK still put most of their money into fixed interest securities. The move into equities only took off at the end of the 1930s. By the mid-1960s, however, investment trusts began to lose favour among small investors due to the rise of the welfare state and the competing attractions of investment alternatives such as pension schemes and life insurance plans. At this stage, big institutions like the insurance companies and pension funds found themselves short of expertise to manage the influx of funds. Investment trusts stepped in to fill this gap. But this proved short-lived as the big institutions started moving their investment management activities in-house by the mid-1970s.

During this time, when CEFs were largely shunned by individual investors and big institutions alike, shares of many CEFs traded at discounts, with market prices significantly lower than their NAV. This triggered off a string of hostile takeover bids, often from big institutions, which identified an opportunity to buy a portfolio of investments on the cheap. For many, this spelt the demise of CEFs. But not quite.

CEFs made a comeback in the mid-1980s, revitalised by innovative variations to the types of funds available. The spectacular performance of emerging market equities in the early 1980s revived investor interest. Closed-end country funds, with its fixed capitalisation, were regarded as a more suitable vehicle for investing in emerging market economies rather than the open-end alternative. The growing popularity of closed-end sector funds in the late 1980s and 1990s further stimulated the CEF industry. The introduction of what the financial press called 'celebrity funds' by a number of well-known fund managers also added some zest to the industry. However a better reflection of the investing public's renewed appreciation of CEFs is the narrowing of discounts or even premiums to NAV.

(Source: Investment Trusts, Anthea Masey, Chapter 3: The History of the Investment Trust, 'Closed-End Fund' Gabelli & Company Inc. and 'Using Funds to Invest in Developing Securities Market', William G. McBride, Lipper Analytical Services Inc)

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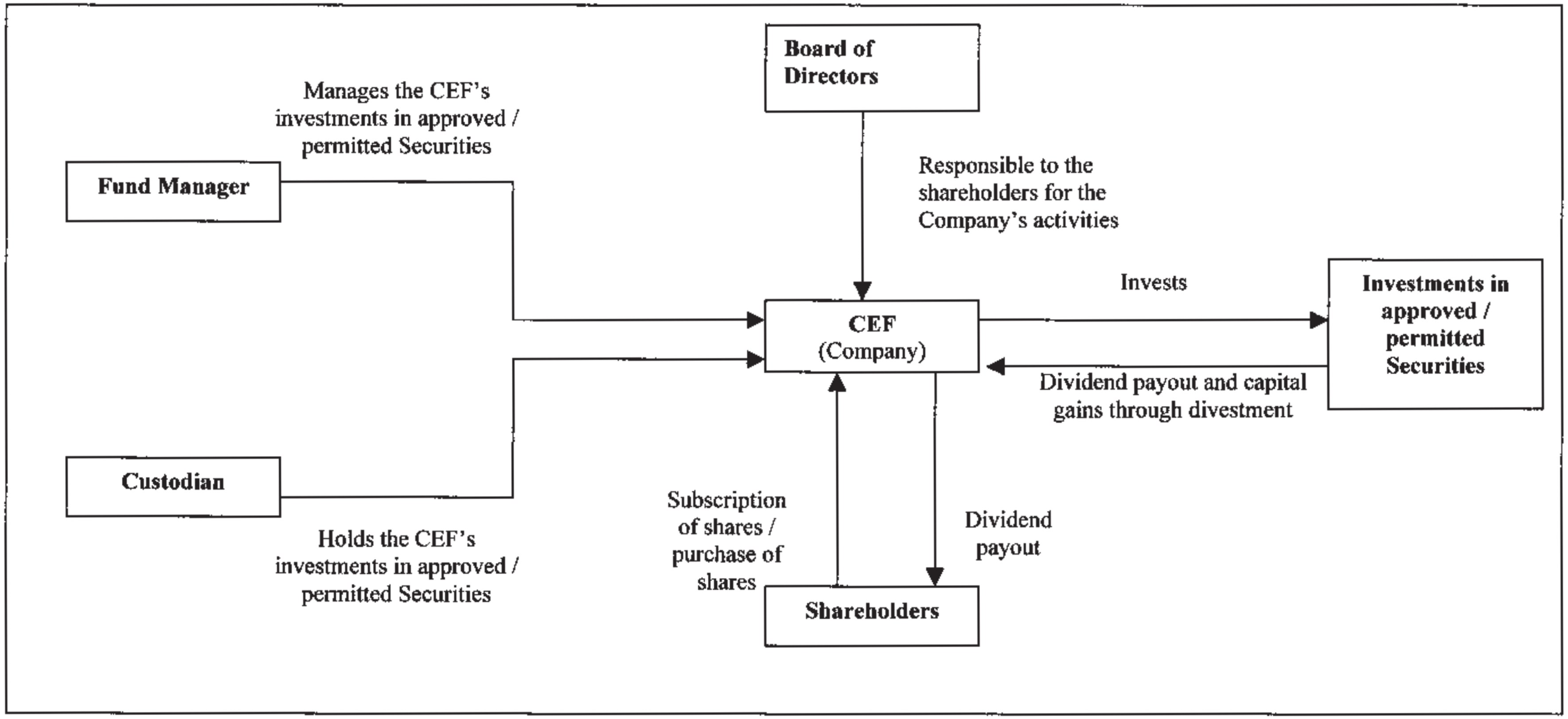
6 INDUSTRY OVERVIEW (Cont'd)

Basic Structure



6.2 TYPES OF CLOSED-END FUNDS

The different types of CEFs include:

(i) *Diversified Equity Funds*

These CEFs focus on common stocks traded on stock exchanges. They usually consist of stocks issued by a broad mix of companies and diversified across many industries, geographic regions and economic sectors. Some of them specialize in a particular asset class or investment style, such as large-cap, small-cap, growth and value. For example, Amanah Millenia Fund Berhad *(formerly known as Amanah Smallcap Fund Berhad)* ("**AMFB**") invests primarily in equities listed on Bursa Securities and other stock exchanges in the region.

(ii) *Sector and Specialty Funds*

Contrary to the diversified equity funds, these CEFs concentrate on stocks of a particular industry, such as banking, technologies, properties and others, or on specialized securities such as preferred stocks or convertible securities. For instance, Petroleum and Resources Corporation, Emerging Markets Telecommunications Fund Inc, Polar Capital Technology Trust Plc, etc.

(iii) *Single Country Funds*

As suggested by its name, these funds focus on securities of a single country. These funds became popular in the early 1980s due to the impressive performance of emerging market equities. Some of the examples of single country funds include, Malaysia Fund Inc, China Fund Inc, Germany Fund, etc.

(iv) *Regional Funds*

Some CEFs focus on regions rather than individual countries. Examples of regional funds are Asia Pacific Fund Inc, European Assets Plc, Pacific Horizon Plc, etc.

(v) *Global / International Funds*

While regional funds concentrate on a particular region, global funds take a global perspective by investing in global markets. For example, Global Income Fund Inc, World Trust Fund Plc, etc.

(Source: Compilation by CDSB)

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6.3 THE BENEFITS OF CLOSED-END FUNDS

(i) Power of Pooling

CEFs pool money from many investors and assemble a portfolio of stocks, bonds and other securities to meet the CEF's investment objectives. The pooling of assets from multiple shareholders allows a CEF to diversify more broadly than a single investor would be able to. This is aptly expressed in Foreign and Colonial Investment Trust Plc's investment objective, which is *"to give the investor of moderate means the same advantages as the large capitalist in diminishing the risk of investing in Foreign and Colonial Government Stocks by spreading the investment over a number of stocks"(Source: Investment Trusts, Anthea Masey, Chapter 3: The History of the Investment Trust)*. Thus, where an investor with RM10,000 could buy only a small number of a particular stock(s), a CEF with an asset size of say RM100 million, will be able to buy far more.

(ii) Management Expertise

Each CEF has its own investment policy and objective. Fund managers conduct the investment research and make the necessary investment decisions based on this mandate. Many individual investors neither have the time, energy, skills, experience, resource nor desire to follow the stock market and research investments on a full time basis. With CEFs, all the investors need to do is make the initial choice of which CEF to invest in. This decision will be based primarily on two (2) factors: the CEF's investment objective, and who the fund manager is.

(iii) Stable Pool of Funds

In contrast to open-end funds or unit trusts, the pool of assets available for investment remains stable for CEFs. CEF fund managers do not have to worry about having enough liquidity to meet redemption requests or identify enough opportunities to invest inflow of funds, which in the case of open-end funds, are beyond the fund manager's control. As a consequence, CEF fund managers have much greater flexibility to put the assets to work on a long-term strategy as the fund manager's investment decisions are totally separated from the shareholders' decision in relation to their shareholdings in CEFs. It was for this reason that the PRC decided to introduce CEFs in the early 1990s before unit trusts, which was introduced only in 2001 *(Source: www.stock888.net)*.

(iv) Better Investment Opportunities

With a stable pool of assets, CEFs have a much broader range of investment choices and greater flexibility in deciding where and how to invest. For example, CEFs have more leeway to invest in illiquid and small capital securities that may offer potentially higher returns as well as allows CEFs to be more focused when investing.

(v) Lower Expenses

Ceteris paribus, lower expenses may generate better returns for investors. Open-end funds or unit trust funds are marketed with the support of well-established distribution networks, which includes financial planners, banks and insurance companies. With CEFs, there is no need for such marketing and distribution expenses.

Additionally, the CEF's stable pool of assets implies lower portfolio turnover, which translates into lower commission expenses.

(vi) Less Reinvestment Problems

With less buying and selling activities compared to an open-ended fund, there would be less reinvestment decisions for the CEF to make. The more reinvestment decisions to be made, the higher the risks of making the wrong decisions and thus the higher the chances that the performance of a fund would be inferior. As a result, chances of success for CEFs are much higher.

(vii) Additional Return Potential

The market price of CEFs is determined by the interplay between demand and supply. Consequently, the market price of a CEF need not equal its NAV. When demand is greater than supply, CEFs may sell at a premium to its NAV. Likewise, when supply exceeds demand, CEFs may sell at a discount to NAV. This feature gives investors the potential for additional returns. When the CEF discount narrows or its premium widens, the price return of the CEF will be greater than the NAV return. This is illustrated in the examples below.

- **Exploiting the premium**

  The first example is shown by **Figure 1** below. It shows the return to an investor in a situation where the CEF is issued at par during the IPO stage and subsequently moves to a consistent premium. This can happen when the fund manager has a consistently superior track record and investors are confident that the NAV of the CEF will expand. It shows how CEF investors can exploit a premium widening.

  A UTF investor would buy and sell based on NAV. In **Figure 1**, a UTF investor buys at point X or RM1.00 and sells at point Z or RM1.50, giving him a return of RM0.50 (before subtracting loading charges). A CEF investor buys at the same point as the UTF investor, ie point X or RM1.00. Over time, the CEF moves into a premium. The CEF investor sells at the same time as the UTF investor, which corresponds to point Y or RM1.90. This gives the CEF investor a total return of RM0.90 (A+B), which consists of a NAV return of RM0.50 (B) and a premium of RM0.40 (A).

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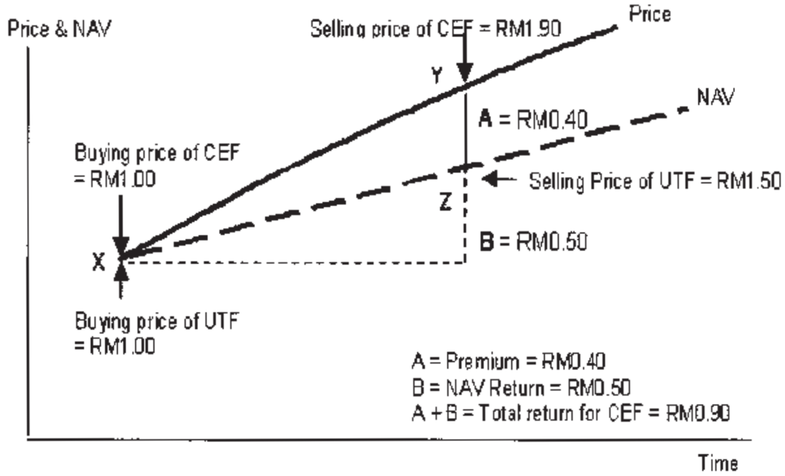
Figure 1: Exploiting the premium



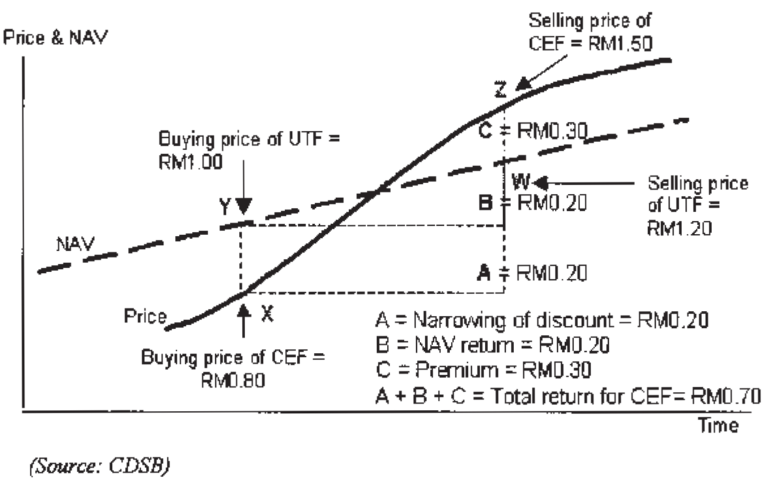
(Source: CDSB)

- **Benefiting from the discount**

Figure 2 shows the second example where a CEF moves from a discount to a premium. Assume that an investor buys a CEF at point X or at RM0.80, when the CEF is trading at a 20% discount to NAV. Over time, the discount evaporates and turns into a premium. The CEF investor decides to sell the CEF at point Z or at a price of RM1.50.

The CEF investor's total returns are made up of 3 parts : (i) The narrowing of the discount – Part (A) = RM0.20, (ii) The return on NAV, Part (B) = RM0.20, and (iii) The RM0.30 premium, Part (C). Had the investor invested in a UTF at the same time as he bought the CEF, he would have bought at point Y or at RM1.00. If he sells his UTF at the same time as he sold the CEF, he would have done so at point W or RM1.20. His gross returns from the UTF would only be RM0.20 (before subtracting any loading) or Part B. Obviously, this is much less than the returns of the CEF investor.

Figure 2: Exploiting the discount 1



(Source: CDSB)

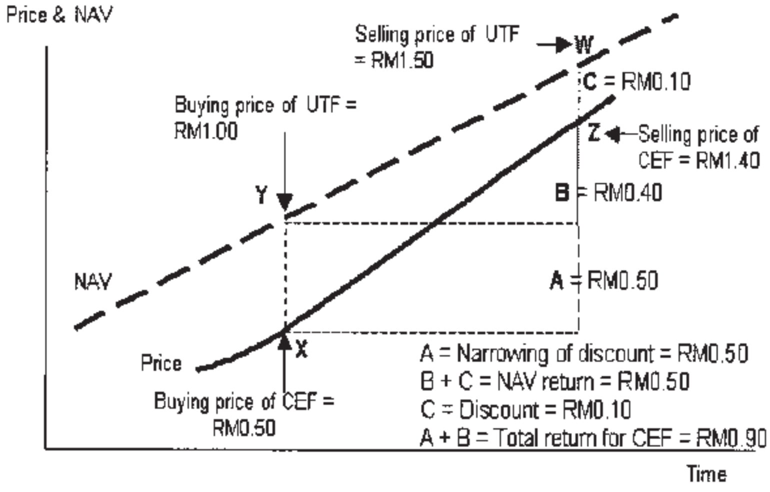
The third simple example is captured by **Figure 3.** It illustrates the return to an investor in a situation where the discount of a CEF narrows but does not move into a premium. Again, assume that an investor buys a CEF at point X or RM0.50, when the CEF is trading at a 50% discount to NAV. Over time, the discount narrows but does not disappear. At point Z or RM1.40, the investor decides to sell the CEF, which is then trading at a smaller discount.

The total return to the CEF investor is Parts B + (A – C). Part B + Part C represent the NAV return of RM0.50 (RM0.40 + RM0.10). Part A represents the initial discount of RM0.50. However, as the CEF is still trading at a RM0.10 discount at point Z, Part C is deducted from Part A (RM0.50-RM0.10). So the total return to the CEF investor is Part A + Part B or RM0.50 + RM0.40 = RM0.90.

Had the investor invested in a UTF instead, buying at point Y and selling at point W, he would have made a gross return of Parts B+C, which is the NAV return of RM0.50 (before subtracting loading). In Malaysia, the front-end or back-end loadings can range from 2% to 7% of NAV. The load is added to the NAV of the shares when calculating the offer and redemption price. Consequently, the net returns to a UTF investor would be Parts B + C less the front-end and/or back-end load.

It is important to note that in a situation where the discount is narrowing, Part C can never be greater than Part A. From this, we can deduce a very important point. Parts A+B will always be greater than Parts B+C. So, when the discount narrows or when the premium widens, the returns from investing in a CEF will always be greater than the returns from investing in a UTF.

Figure 3: Exploiting the discount 2



(Source: CDSB)

6.4 PERFORMANCE OF CLOSED-END FUNDS

Various share market indices are commonly used as benchmarks to assess the performance of CEFs. There are two (2) distinct but related measures to evaluate the performance of a CEF.

(i) An assessment based on the return on NAV; and
(ii) An assessment based on the return on market value.

The former measures the performance of the fund manager while the latter measures the actual investment returns (price performance) of the CEF.

Table 1: Comparison between Investment Trusts / CEFs and unit trusts (based on market value)

Category: Far East ex-Japan - Top 3 Investment Trusts / CEFs and unit trusts as at 7 March 2005

Fund type	Fund name	5-year %
Investment Trust / CEF	Aberdeen New Thai	+171.1
	Scottish Orient Small	+160.2
	Aberdeen Asian Smaller Companies	+113.0
	Average (out of 21 funds)	+34.5
Unit Trust	Lincoln Far East	+72.1
	Baring Korea	+58.0
	First State Asia Pacific A	+54.2
	Average (out of 57 funds)	+2.9

(Source: TrustNet Limited[1])

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[1] *TrustNet Limited is a free daily updated fund information service regulated by the Financial Services Authority of the UK.*

Table 1 shows the top 3 performing UK investment trusts / CEFs and unit trusts within the Far East ex-Japan category, ranked by their 5-year market value return. It clearly shows that investment trusts / CEFs have outperformed their unit trust counterparts. Looking at returns over 5 years, the average cumulative return of investment trusts / CEFs of 34.5% is about 12 times higher than the average 2.9% return of unit trusts.

Table 2: Performance comparison between investment trusts / CEFs and unit trusts (based on NAV)

Category: Far East ex-Japan -Top 3 investment trusts / CEFs and unit trusts as at 7 March 2005

Fund type	Fund name	5-year %
Investment Trust / CEF	Aberdeen New Thai	+142.9
	Scottish Orient Small	+95.2
	Aberdeen Asian Smaller Companies	+68.9
	Average (out of 21 funds)	+13.7
Unit Trust	Lincoln Far East	+72.1
	Baring Korea	+58.0
	First State Asia Pacific A	+54.2
	Average (out of 57 funds)	+2.9

(Source: TrustNet Limited [1])

Table 2 further reaffirms the superior performance of investment trusts / CEFs over their unit trusts peers, this time on the basis of NAV return. It shows the top 3 performing UK CEFs and unit trusts within the Far East Ex-Japan category, ranked by their 5-year NAV return. Again, CEFs performed better than unit trusts.

This is without taking into account the additional returns available to CEF investors due to the existence of discounts and premiums. As shown in **Table 1 and Table 2**, CEFs made a 13.7% NAV return on average, while the average market value return was 34.5%. This implies that CEF investors achieved approximately 20.8 percentage points more return simply from narrowing discounts or widening premiums.

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[1] *TrustNet Limited is a free daily updated fund information service regulated by the Financial Services Authority of the UK.*

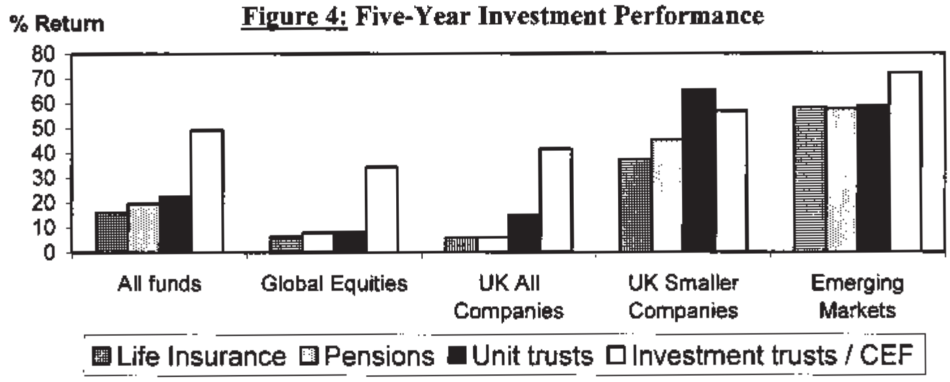
A similar story is told when the performance of CEFs is compared with other asset classes such as life insurance and pensions in the UK, as shown in Table 3 and Figure 4 below.

Table 3: 5-Year Investment performance of various fund classes

	Life insurance	Pensions	Unit trusts	**Investment trusts / CEFs**
All funds	16.0%	19.6%	22.5%	**49.2%**
Global equities	6.3%	7.9%	8.3%	**34.4%**
UK All Companies	6.1%	6.0%	14.8%	**41.6%**
UK Smaller Companies	37.5%	45.3%	65.4%	**56.9%**
Emerging Markets	58.1%	57.7%	59.1%	**72.3%**

(Source: 'Closed-ended funds: the weapon of choice for sophisticated investors', International Investment, January 2004, p22)

Figure 4: Five-Year Investment Performance



(Source: Based on 'Closed-ended funds: the weapon of choice for sophisticated investors', International Investment, January 2004, p22)

PAST PERFORMANCE OF THE FUND MANAGER IS NOT AN INDICATION OF FUTURE PERFORMANCE.

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6.5 PLAYERS, COMPETITION AND SUBSTITUTE PRODUCTS/SERVICES

In Malaysia, listed CEFs were introduced in 1997 with the launch of AMFB. AMFB has a life span of ten (10) years and will mature in 2007, after which shareholders will decide whether to continue or wind-up the fund. AMFB was launched when the market was at its peak. AMFB remains the only CEF listed on Bursa Securities to date.

While there is only one CEF listed on Bursa Securities, the presence of CEFs in the major markets of New York, London, Shanghai and Shenzhen are sizable as shown in **Table 4.**

Table 4: CEFs on stock exchanges

Exchange	New York Stock Exchange (as at 31 Jan 2005)	London Stock Exchange (as at 31 Jan 2005)	Shanghai Stock Exchange (as at 31 Jan 2005)	Shenzhen Stock Exchange (as at 31 Jan 2005)	Bursa Securities (as at 31 Jan 2005)
No. of CEFs	658	334	25	30	1
Total listings	2,773	1,299	842	544	974
% of listings	23.7 %	25.7 %	3.0 %	5.5 %	0.1 %

(Source: Based on information extracted from New York Stock Exchange, London Stock Exchange, Bursa Securities, www.p5w.net, Association of Investment Trust Companies, Closed-end Fund Center)

Taking into consideration that there is only one listed CEF on Bursa Securities, the competition within the listed CEF industry in Malaysia is minimal. As such, icapital.biz faces competition from various other such investment funds, which includes amongst others, funds managed by provident and pension funds, unit trusts, asset management companies and insurance companies.

6.6 LAWS AND REGULATIONS

A CEF is governed by the SC Guidelines-CEF and the Listing Requirements. A CEF shall also comply with the Securities Commission Act 1993, SIA, Act, and relevant circulars and directives issued by the SC to CEFs. In addition, a CEF shall comply with all applicable exchange control laws, regulations and notices at all times.

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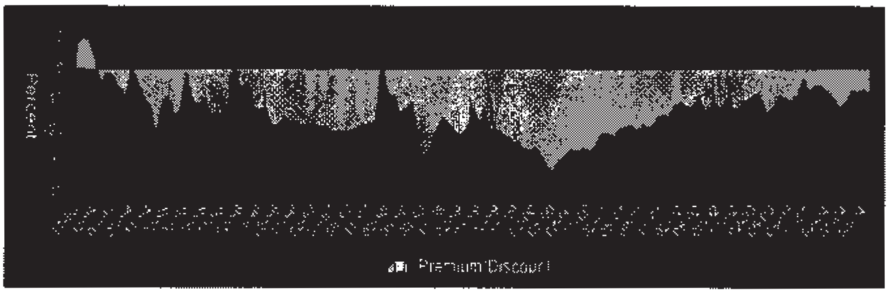
6.7 MANAGING DISCOUNTS

A CEF and/or its shareholders have the power to take action to narrow or eliminate the discount. Some of the options that may be available include share repurchase, open-ending, takeover, liquidation, managed distribution policy and shareholder activism.

(i) Shareholder Activism

CEFs are structured as public limited companies whereby there is no controlling shareholder. In Malaysia, the SC Guidelines - CEF stipulate that no shareholder can hold more than 20% of the total capital of the CEF. Therefore, shareholders have the power to pressure management to do something positive to narrow the discount. Active shareholders may attempt to realise the full value of the CEF by proposing a share repurchase, conversion to an open-end structure[2], takeover or liquidation. This is clearly illustrated in the case of Asia Tigers Fund Inc as explained below.

Figure 5: Asia Tigers Fund, Inc



(Source: www.ETFconnect.com)

Asia Tigers Fund (ATF) is a non-diversified CEF that seeks long-term capital appreciation by investing primarily in Asian equity securities. ATF has been trading on New York Stock Exchange since 19 November 1993. In January 2000, Harvard University bought 2.28 million ATF shares or 11% capital in ATF. At that time, ATF was trading at a 25% discount. By December 2002, Harvard University owned 3 million shares, or almost 23% of ATF's voting stock. Harvard University and other shareholders pressured ATF to convert to an interval fund, which is a CEF that offers to repurchase shares periodically to reduce the discount. By November 2003, the discount narrowed to 7% and Harvard University sold its ATF stake. Between January 2000 to November 2003, ATF's share price and NAV grew 45% and 27% respectively, as shown in **Figure 5**.

(Sources: USA Today, Article entitled 'Squeezing the Discount Out of Closed-End Fund', 26 March 2004, John Waggoner)

(ii) Share Repurchase

CEFs may offer to repurchase shares in order to narrow the discount. Share repurchases give investors the impression that fund managers are trying to reduce the discount, which helps to boost demand. Furthermore, when the CEF buys back shares at a discount to NAV, the NAV per share for the remaining shareholders increases if the shares bought back were cancelled. Share repurchase exercises are subjected to relevant laws and guidelines on share repurchase / share buyback.

[2] Although open ending of a CEF is an option available in foreign markets, there is no precedent of such open ending in Malaysia and is subjected to the SC's approval.

(iii) Open-Ending[2]

CEFs could choose to convert to an open-end structure like that of unit trusts. Once a CEF open-ends, investors can sell their shares in the fund back to the fund manager, who redeems them at NAV. If the CEF does not have enough cash to meet redemptions, the fund manager can sell the assets from the portfolio to raise cash. A CEF's discount narrows considerably after an open-ending announcement is made as can be seen in **Table 5**.

Table 5: Narrowing of discount upon open-ending

CEF	Discount (before announcement)	Discount (after announcement)	Change
Alliance Global Environment	19.18%	4.95%	74.18%
GT Global Developing Markets	14.68%	8.44%	42.52%
New Age Media	19.09%	7.71%	59.64%
Oppenheimer World Bond	9.28%	4.24%	54.29%
Pilgrim America Bank & Thrift	11.65%	6.78%	41.84%
Quest for Value Dual Purpose Fund	5.41%	4.75%	12.34%
Schroder Asian Growth	13.60%	10.20%	25.01%
Worldwide Value Fund	13.59%	5.34%	60.69%

(Source: Closed-End Fund Centre, Wiesenberger Study of Closed-End Fund that Open End, 21 September 1998)

(iv) Takeover

A CEF that trades at a discount or has an attractive portfolio may be a target for a takeover as it represents an opportunity to buy assets on the cheap. Since a CEF has no controlling shareholder, an unfriendly party may attempt a hostile takeover by buying a large block of shares. In Malaysia, the maximum number of shares an investor can hold in a CEF is capped at 20%. While this may make hostile takeover attempts more difficult, however, since no single party can have voting control, it is relatively easier for shareholders to exert influence over the direction and affairs of the CEF. Shareholders may attempt a takeover to replace existing management or change existing investment policy.

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[2] Although open ending of a CEF is an option available in foreign markets, there is no precedent of such open ending in Malaysia and is subjected to the SC's approval.

(v) Liquidation

Alternatively, shareholders of a CEF may opt for liquidation, which essentially terminates the CEF. As the CEF approaches the liquidation date, the discount narrows. At the close of business, all assets are liquidated and shareholders are returned an amount equal to the NAV per share.

Table 6: France Growth Fund Inc liquidation

Date	Price (USD)	NAV (USD)	Discount
25 March 2004	7.40	8.45	12.43%
8 April 2004	8.31	8.81	5.68%
14 May 2004	7.93	8.28	4.23%
4 June 2004	8.43	8.61	2.09%

Table 6 shows the series of events from the announcement of liquidation to the actual liquidation of France Growth Fund, Inc (FGF). On 6 April 2004, FGF announced that it would call a special meeting of shareholders to vote on its liquidation. Following the announcement, the discount narrowed to 5.68% as at 8 April 2004, from the 12.43% discount recorded on 25 March 2004. On 27 May 2004, FGF's shareholders voted and approved the liquidation. By 4 June 2004, the discount narrowed to 2.09%. 18 June 2004 marked the last trading day of FGF shares. And on 21 June 2004, FGF reported liquidating distributions at USD8.42 per share, which was the NAV per share at the close of business.

(Source: www.francegrowthfund.com)

(vi) Managed Distribution Policy

Another method used to stimulate interest in CEFs is via a managed distribution policy. CEFs are introducing or increasing the frequency of dividend payments to shareholders in order to avoid shares from trading at a discount. Generally, dividends are in the form of regular fixed payments or payments based on a percentage of NAV. When CEFs are trading at a discount, these dividend payments offer investors an opportunity for higher dividend yields. For example, investors may pay only RM0.80 for shares in a CEF trading at a 20% discount, but collect dividends from a portfolio worth RM1.00, thus allowing them higher dividend yields. Nevertheless, such consistent cash outflows could compromise the performance of CEFs, especially in periods of underperformance. During bad times, CEFs may not be able to cover the distributions from other revenue streams, which could lead to a scenario involving a return of capital.

6.8 DEMAND AND SUPPLY CONDITIONS

The demand for a CEF depends on the ability of its fund manager to continuously perform and deliver results. The performance of a CEF depends on the appreciation in values of the underlying assets. As such, a value investing philosophy and prudent investment selections will assist a CEF to continuously deliver results. In addition, a CEF may attempt to increase the demand for its shares by offering dividends, engaging in tender offers (where the CEF offers to purchase its shares directly from shareholders at NAV), or instituting a share repurchase program (where the CEF buys its shares in the open market).

The supply for a CEF is, on the other hand, dependent on the expectations and behaviour of investors. Given that the investment objective of icapital.biz is long-term capital appreciation, investors who expect return in the shorter term may not be able to enjoy the appreciation. Investors who are easily influenced by market sentiments tend to withdraw from investing during bear markets, thus increasing the supply. Conversely, these same investors will tend to buy aggressively during bull markets, forcing the demand for the CEF to rise.

6.9 PROSPECTS OF THE COMPANY

CEFs (or investment trusts) have come a long way since 1868 when it was first introduced in the UK. In many ways, it is one of the best-kept secrets of the investment world. Buying a CEF is one of the cheapest and simplest ways of accessing the stock market.

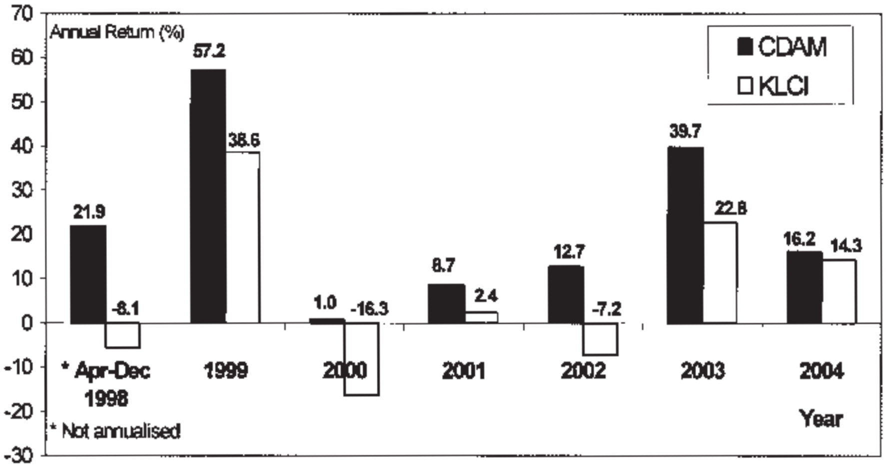
The one important factor that differentiates CEFs is the quality of the fund manager. In order to enjoy superior investment returns, having the right fund manager is imperative.

6.9.1 PERFORMANCE OF FUNDS UNDER CDAM'S MANAGEMENT

Since its inception, the annual returns (net of all expenses) of funds under CDAM's management have consistently outperformed the KLCI and the EMAS Index.

(i) Funds under CDAM's management have beaten the KLCI and the EMAS Index in every single year;
(ii) Funds under CDAM's management have beaten the KLCI and the EMAS Index on a cumulative basis;
(iii) No negative returns have been recorded in any year; and
(iv) In 1998, 2000 and 2002, CDAM registered positive returns despite the negative returns recorded by the bearish general market – see **Figure 6**.

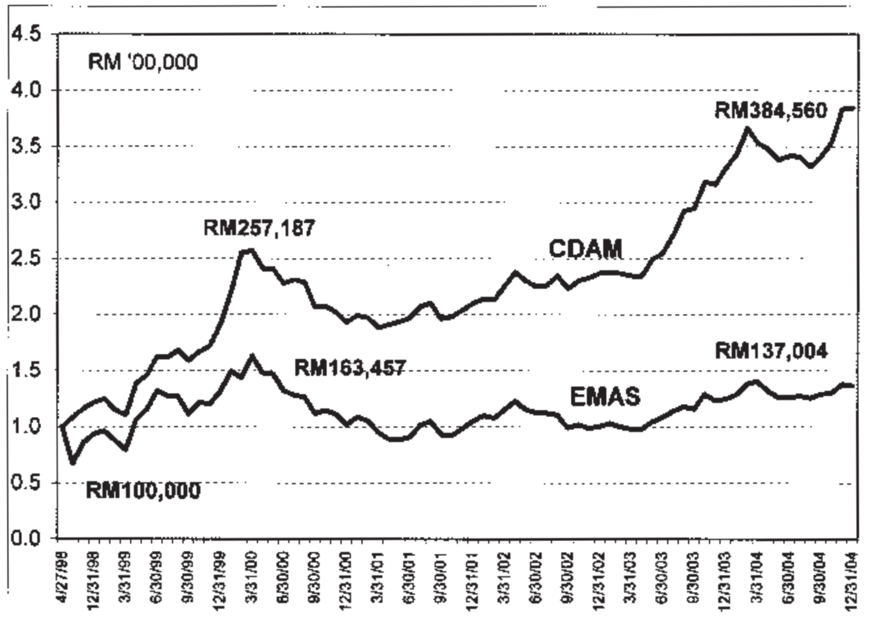
Figure 6: Performance of funds under CDAM's management versus KLCI



(Source: Data on CDAM –Messrs Hewitt Associates)
(Source: Data on KLCI –Daily Diary issued by Bursa Securities and www.bursamalaysia.com)

From 27 April 1998 to 31 December 2004, funds under CDAM's management earned an annual compound return of 22.32%, compared with only 5.84% and 4.82% for the KLCI and EMAS Index respectively. In other words, an initial investment of RM100,000 invested with CDAM in April 1998 would have grown to RM384,560 by December 2004 as opposed to RM146,173 and RM137,004 for the KLCI and EMAS Index- see **Figure** 7. Even if an investor started to invest with CDAM during the peak period in March 2000 with RM257,187, his investment would still grow to RM384,560 by December 2004 or a positive return of 49.53%. When this is compared to the investment made in EMAS Index during the same period, the initial investment is RM163,457 and will only be worth RM137,004 as at December 2004, generating a negative return of 16.2% *(Source: CDAM)*.

Figure 7: Cumulative returns of funds under CDAM's management versus EMAS Index



(Source: Data on CDAM – Messrs Hewitt Associates)
(Source: Data on EMAS Index –Daily Diary issued by Bursa Securities and www.bursamalaysia.com)

Going Beyond an Impressive Track Record

While CDAM's track record is impressive, it is already history. What matters is future performance. Contrary to what is commonly perceived, the track record is not the most important factor in choosing a fund manager. The really key question is this - how can the fund manager sustain its superior performance and ensure future investment success? How can a client be sure that the past performance is not due to luck? How does CDAM deliver a consistent and sustainable performance to its clients?

The only thing that can ensure future investment success, which is what matters most, is to have a sound, rational investment approach and the discipline to apply them consistently. It is of utmost importance to carefully evaluate the philosophy and the underlying investment approach of the fund manager rather than just focus on past performance.

CDAM's investment philosophy/approach is outlined in Section 5.1.2 of this Prospectus.

PAST PERFORMANCE OF THE FUND MANAGER IS NOT AN INDICATION OF FUTURE PERFORMANCE.

6.9.2 INVESTMENT OUTLOOK

The best time to invest in a CEF is when the market is undervalued or when there is a lack of excessive optimism. Comparing **Figure 8** with **Figure 9** shows that the Bursa Securities is currently trading at the low end of its valuation, despite the Malaysian economy recording healthy economic performance in recent years.

Figure 8: Historical PE Ratios

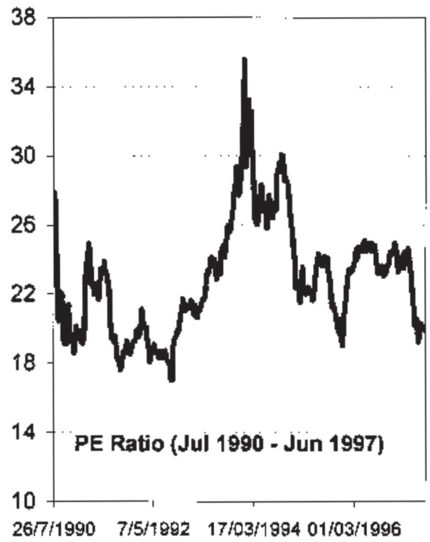
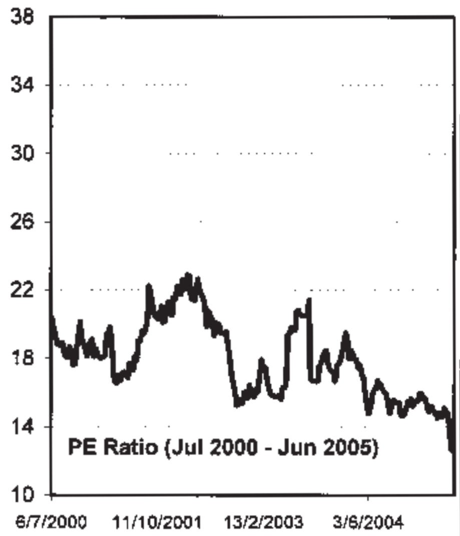


Figure 9: Historical PE Ratios



(Source: Various issues of i Capital throughout the period under review)

Table 7, which measures the market capitalisation to GDP ratio, also indicates that the valuation of Bursa Securities is undemanding. Clearly, such a scenario makes for a positive environment to launch icapital.biz.

Table 7: Nominal GDP and total market capitalisation

Year	Market capitalisation (RM billion)	Nominal GDP (RM billion)	Market capitalisation/ GDP
1990	131.66	119.08	1.11
1991	161.39	135.12	1.19
1992	245.82	150.68	1.63
1993	619.64	172.19	3.60
1994	508.85	195.46	2.60
1995	565.63	222.47	2.54
1996	806.77	253.73	3.18
1997	375.80	281.80	1.33
1998	374.52	283.24	1.32
1999	552.69	300.76	1.84
2000	444.35	343.22	1.29
2001	464.98	334.40	1.39
2002	481.62	361.62	1.33
2003	640.28	394.20	1.62
2004	722.04	447.55	1.61

(Source: Various reports issued by Bank Negara Malaysia)

6.9.3 REVIEW AND OUTLOOK OF THE MALAYSIAN ECONOMY

The launch of icapital.biz is further complemented by Malaysia's favourable economic outlook. Despite being hit severely by the financial crisis in 1997/98, Malaysia's economy managed to recover quickly in 1999. As shown in **Table 8**, Malaysia's economic performance has been strong compared with the regional countries.

Table 8 : Real GDP Growth in East Asian Countries

(%)	1998	1999	2000	2001	2002	2003	2004	2005*
Malaysia	-7.4	6.1	8.9	0.3	4.4	5.4	7.1	5.7
Singapore	-0.8	6.8	9.6	-2.0	3.2	1.4	8.4	2.5
Hong Kong	-5.0	3.4	10.2	0.5	1.9	3.1	8.1	6.0
S. Korea	-6.9	9.5	8.5	3.8	7.0	3.1	4.6	2.7
Taiwan	4.3	5.3	5.8	-2.2	3.9	3.3	5.7	2.5
Indonesia	-13.1	0.8	4.9	3.4	4.3	4.5	5.1	6.4
Thailand	-10.5	4.4	4.8	2.2	5.3	6.9	6.1	3.3
Philippines	0.4	3.4	4.4	1.8	3.3	4.6	6.1	4.6

** 1st Quarter 2005*

(Source: Department of Statistics, Malaysia, Bank Negara Malaysia, Singapore's Department of Statistics, Hong Kong's Census & Statistics Department, Korea National Statistics Office, Taiwan's National Statistics Office, National Economic and Social Development Board of Thailand, Central Bank of the Philippines, and Statistics Indonesia)

Malaysia's economy also rebounded swiftly after the technology bubble burst in 2000 – see **Figure 10**. In 2004, Malaysia's economy grew by 7.1%. *i* Capital, the newsletter by CDSB, expects another healthy economic growth for the Malaysian economy in 2005.

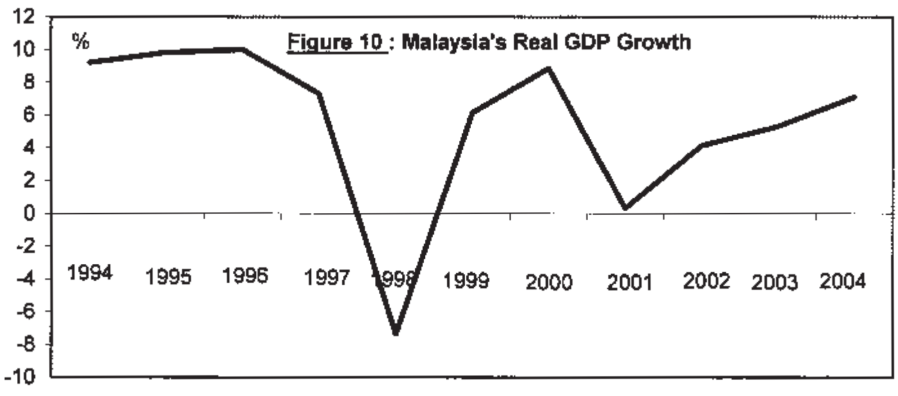
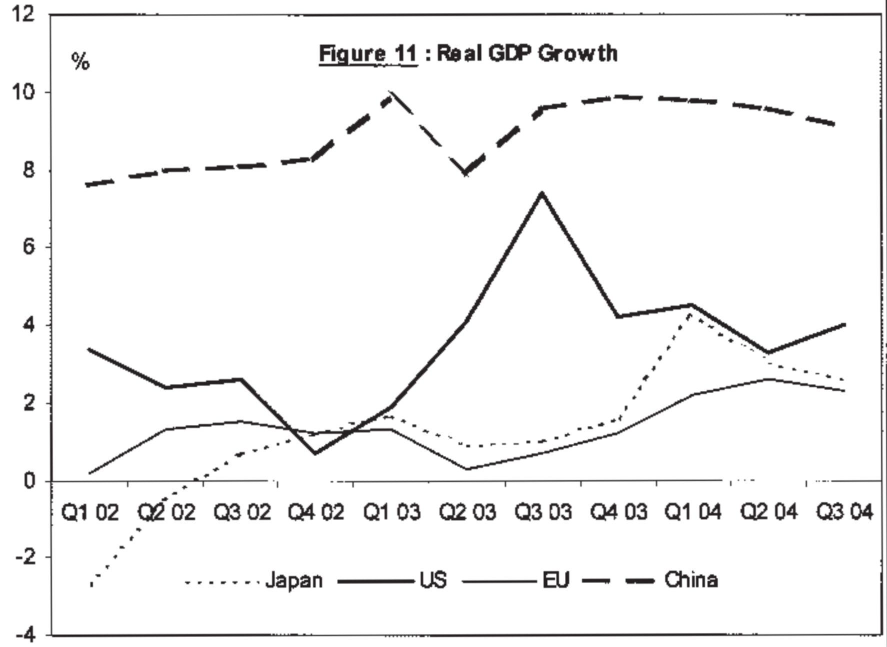


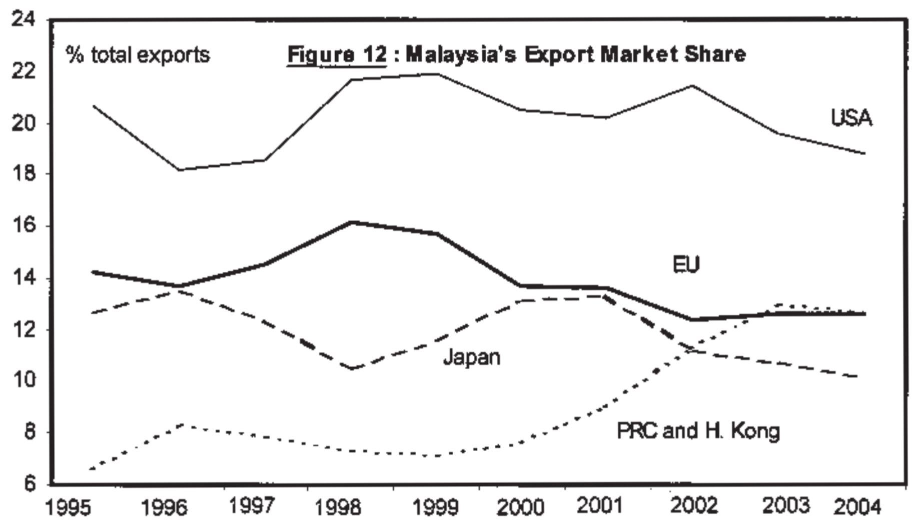
Figure 10 : Malaysia's Real GDP Growth

(Source: Department of Statistics)



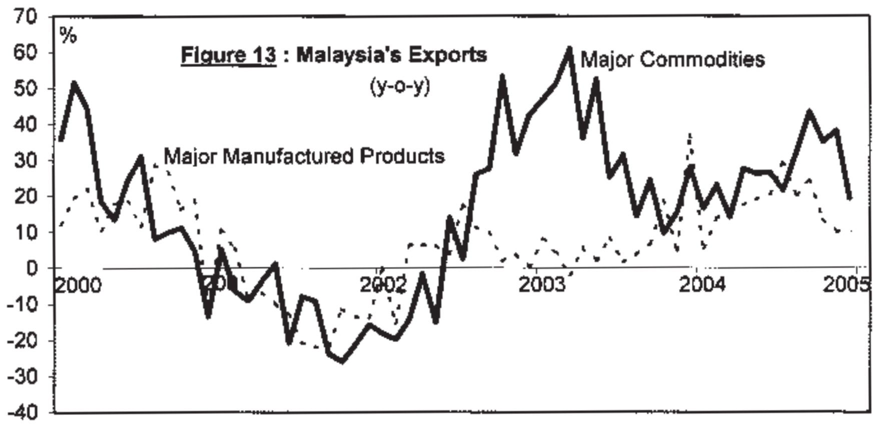
(Source : Japan's Cabinet Office, US Bureau of Economic Analysis, Eurostat and PRC's National Bureau of Statistics)

Economic growth in the last few years has been sustained by strong external demand as well as stable domestic demand. The synchronised world economic recovery has benefited an export-dependent economy like Malaysia. **Figure 11** shows economic growth of the major economies in the last few years. **Figure 12** shows Malaysia's exports to her major export markets. Malaysia's exports to the PRC has demonstrated an uptrend since 1999, in line with the rapid growth of the PRC's economy.



(Source: Based on data issued by the Department of Statistics)

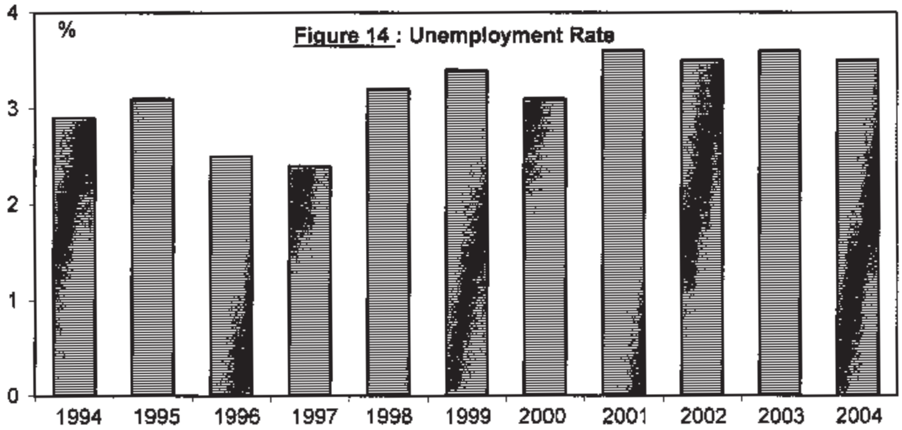
Besides the synchronised global recovery, Malaysia has also benefited from the rise in commodity prices, as she is also rich in natural resources. Although exports of electrical and electronic products are important to Malaysia's overall export performance, exports of commodities have remained significant. As shown in **Figure 13**, buoyant exports of palm oil, natural gas, crude oil, etc have contributed to sustaining Malaysia's exports and thus economic growth. With the PRC, India, and other East Asian countries expected to continue growing strongly, demand for palm oil, natural gas, crude oil, rubber, timber, and other commodities is expected to remain strong.



(Source: Based on data issued by the Department of Statistics)

As of 21 July 2005 the RM is no longer pegged to the US Dollar. Although the peg has been removed, Bank Negara Malaysia is expected to monitor the RM's exchange rate closely to ensure that the RM trades closely to its fair value. The huge international reserves would enable Bank Negara Malaysia to comfortably manage the RM's exchange rate in the interest of Malaysia's exports.

On the other hand, growth in domestic demand was underpinned by strong private consumption as well as continued supportive fiscal policy and accommodative monetary policy. Although the Malaysian government has been trying to consolidate her fiscal position, the cut back in public sector expenditure has been mild. Private consumption has been able to grow strongly due to a stable labour market condition (see **Figure 14**), low interest rate and high commodity prices.



(Source: Based on various issues of Economic Report)

The landslide win in the 2004 election proved a simple but highly important point about Malaysia. It is certainly not a nation of extremists. Despite big swings in voting trends amidst a multi-ethnic, multi-religious society, Malaysia has been able to maintain political stability for nearly all of its independent years. The massive mandate given by the electorate to the current ruling coalition provides an opportune time for the new administration to address the structural problems Malaysia faces by speedily implementing reform programmes. These reforms are expected to further enhance the fundamentals strength of the Malaysian economy.

Malaysia's economic outlook remains favourable. Externally, although world economic growth is expected to moderate in 2005, the slowdown is expected to be relatively mild. According to the International Monetary Fund, the world economy is projected to expand by 4.3% in 2005, slightly slower than the 5.0% expected for 2004. On the domestic front, Malaysia's economic fundamentals stay strong. Despite having a low unemployment rate, inflationary pressure stays benign. In addition, the current account of the balance of payments has been recording huge surpluses for many years and this favourable performance is expected to continue given the positive world economic outlook. Malaysia's international reserves have been on a steady climb for some time and are currently at a comfortable level. At the end of 2004, Malaysia's international reserves stood at RM253.5 billion or USD66.7 billion. This was sufficient to finance 8.2 months of retained imports and was 6.1 times the short-term external debt. Although the federal government's financial position has been in a deficit for 7 continuous years, about 80% of the deficit is financed by domestic savings. Foreign debt remains low. The external debt service ratio as at the end of September 2004 was a low 4.6%. In addition, the government has taken measures to reduce the fiscal deficit. For 2005, *i* Capital has forecasted that Malaysia's economy would grow in the range of 5.0%-6.0%.

6.9.4 REVIEW AND OUTLOOK OF THE REGIONAL ECONOMIES

South East Asia's economies were hit hard during the Asian financial crisis. Real GDP of ASEAN contracted 7.1% in 1998. However, after undergoing positive changes, both politically and economically, optimism is returning to the region again. This is reflected from the huge run up in the region's stock markets. **Figure 15** shows the growth rate of ASEAN from 1996 to 2003. The region as a whole holds much promise for investors in light of its huge population and rising level of per capita income – see **Table 9.**

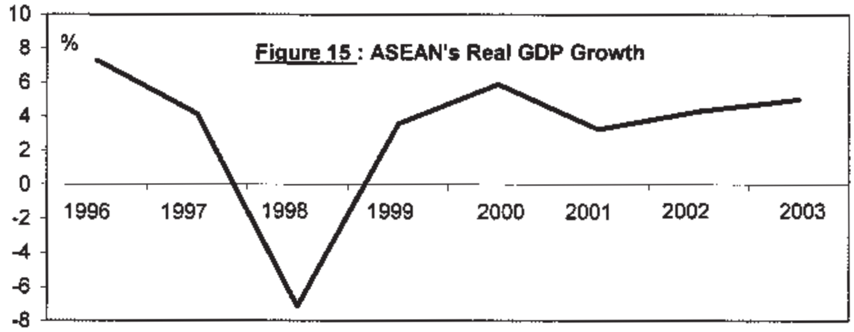


Figure 15 : ASEAN's Real GDP Growth

Source : ASEAN Secretariate

Table 9: Population and Gross National Income per capita

	Indonesia	Malaysia	Philippines	Singapore	Thailand	Vietnam
2003 population (million)	214.5	24.8	81.5	4.3	62.0	81.3
2003 Gross national income per capita (USD)	810	3,780	1,080	21,230	2,190	480

(Source : www.worldbank.org)

With the region's huge potential as well as positive political and economic changes, *i* Capital is confident that foreign direct investment flow into ASEAN could return to or even surpass the levels before the Asian financial crisis – see **Table 10.**

Table 10 : Foreign direct investment (USD million)

	1992-97 annual average	1998	1999	2000	2001	2002	2003
Malaysia	5,816	2,714	3,895	3,788	554	3,203	2,474
Singapore	8,295	7,690	16,067	17,217	15,038	5,730	11,409
Thailand	2,269	7,491	6,091	3,350	3,813	1,068	1,802
Indonesia	3,518	-241	-1,866	-4,550	-2,977	145	-597
Philippines	1,343	2,212	1,725	1,345	982	1,792	319

(Source : United Nations Conference on Trade and Development)

i Capital believes that the rapid emergence of the PRC and India further boosts the attractiveness of the region. Almost 40% of the world's population live in these two countries. Given their huge population and rising income levels, the potentials of the PRC and India are immeasurable – see **Table 11.**

Table 11: Economic Indicators for India and the PRC

	PRC			India		
	GDP growth (%)	Gross national income per capita (USD)	Population (million)	GDP growth (%)	Gross national income per capita (USD)	Population (million)
1999	7.1	780	1,253.7	7.1	440	999.0
2000	8.0	840	1,262.6	3.9	450	1,015.9
2001	7.5	900	1,271.8	5.2	460	1,032.5
2002	8.0	960	1,280.4	4.6	470	1,048.6
2003	9.1	1,100	1,288.4	8.0	530	1,064.4

(Source : www.worldbank.org)

In summary, the prospects for icapital.biz looks bright. At its core, icapital.biz is supported by a top performing fund manager. CDAM's consistent success is attributed to its sound intellectual framework for making investment decisions. This investment framework provides CDAM with an unsurpassed edge in identifying investment opportunities and delivering results for icapital.biz. On top of having the right fund manager, the prospect of icapital.biz is further enhanced by a positive investment environment. Bursa Securities is at the low end of its valuation and Malaysia's economic outlook remains favourable. All in all, these factors put forth a compelling case for investing in icapital.biz.

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