

KHALEEJ EQUITY FUND

Securities & Investment Company BSC
Bahrain domiciled open-ended investment fund
Report Issued: January 2009

Peer Group:

GCC

Fund Manager/Adviser:

Team

Location:

Manama, Bahrain

Launch Date: March 2004

Fund Size (November 2008):

US\$88m

Group Contact No:

+973 1751 5000

Website:

www.sicobahrain.com

S&P ID Number: N/A



INVESTMENT STYLE

	Value	Blend	Growth
Large-Cap			
Mid-Cap			
Small-Cap			

Please see page 2 for required research analyst certification disclosure.

Further information on S&P's fund coverage can be found at www.funds.standardandpoors.com

STANDARD & POOR'S OPINION (DECEMBER 2008)

The Khaleej Equity Fund has established itself as one of the best-performing GCC equities funds. Its success is a testament to the group's disciplined yet decisive approach. The strong performance until last summer resulted from stock selection while, more recently, raising cash to 60% has added most value.

Head of asset management Shakeel Sarwar has been involved with this portfolio since 2004. Over the last 12 months, Sarwar has split the investment side of the team into two units, one dedicated to research and the other to portfolio management. Malik Zahir was appointed to lead the research effort, while Naveed Ahmed rejoined the group and is the day-to-day manager of this fund. These changes address our previous concerns over the depth of the resources and the amount of responsibility falling directly on Sarwar's shoulders. Moreover, it is encouraging to see the team has not lost any members over the last year.

The team's research-intensive approach is nevertheless unchanged. Analysts are in charge of idea generation and their views are directly reflected in the fund. The portfolio managers are nevertheless free to add their own perspective, which can include both top-down and bottom-up considerations. Sarwar has the final say on portfolio construction and retains the right to veto. The portfolio is concentrated yet broadly diversified.

The deliberately measured approach adopted by the top management of the bank is likely to make Securities & Investment Company BSC (SICO) a more stable outfit than several peers during times of significant disruption.

We hold Sarwar in high regard, as his approach has proved rigorous, while still allowing for flair. While Ahmed's role in this fund is growing, we take comfort from the fact that Sarwar is still closely involved with portfolio construction. This justifies the upgrade to S&P AA.

FACT FILE

Group: Securities & Investment Company BSC (SICO) is a Bahrain-domiciled investment bank set up in 1995, with main activities in asset management, corporate finance, brokerage, custody and administration of funds. It is owned by a number of regional institutions and its employees.

Team: Sarwar heads the asset management team of 11, including three managers and five analysts. They are responsible for assets around \$472m.

Fund Manager: Sarwar (13 years' experience) and Ahmed (five years' experience) are those most involved with this fund. Ahmed is the day-to-day manager.

Style: This focused fund is constructed mainly bottom-up but within the context of a top-down overlay. There is no style bias, with the fund holding both growth and value stocks.

Past performance: Over the 12 months to the end of October 2008, the fund returned -20.6% compared to -37.9% of the MSCI GCC index.

FUND MANAGER & TEAM

Anthony Mallis is CEO of SICO. Sarwar heads the asset management unit of 11. Together with Ahmed (five years' experience) and Faisal Jiwani (five), Sarwar focuses on portfolio management. The research team is headed by Malik Zahir (eight years' experience) and includes Waruna Kumarage (seven), Aneel Kanwer (six), Zainab Mian (seven) and Alaa Alaabed (one). Hasan Haider is still part of the team but will move to a relationship management role. Further support is provided by one trader and one administrator.

Each analyst covers a broad sector and a geographic area. Zahir covers around 40-50 companies and Kumarage around 30, leaving the remaining analysts to cover a total of 20-30 companies.

Shakeel Sarwar - head of asset management - MBA (IBA Karachi), joined SICO in December 2004 and is head of asset management. His experience includes five years at Riyadh Bank (Saudi Arabia) and four years with ABN AMRO Securities (in the UK and Pakistan).

Naveed Ahmed - MBA (IBA Karachi), CFA, re-joined SICO in June 2008. He has five years' experience and was first at SICO from 2005 to 2007.

Malik Zahir - CFA, ACMA, has eight years' experience. He joined SICO in 2007 from Amba Research. He heads the research team and covers financials.

PORTFOLIO CHARACTERISTICS

No. of holdings	32
Turnover ratio (%)	109%
% in top 10	31

TOP 10 HOLDINGS (01/11/08)

	%
Qatar Telecom	4.6
Etihad Etisalat	3.9
Saudi Telecom	3.4
Saudi Cable	3.3
Al Rajhi Bank	3.1
Burgan Bank *	2.7
Emaar Properties *	2.6
Arabian Pipes	2.5
Banque Saudi Fransi	2.4
Gulf Finance House *	2.4

* In top 10 holdings a year ago

ALLOCATION BREAKDOWN (01/11/08)

	Fund %
Bahrain	5.0
Cash	43.0
Kuwait	8.0
Qatar	5.0
Saudi Arabia	25.0
UAE	14.0

KHALEEJ EQUITY FUND

Peer Group: GCC



MANAGEMENT STYLE

The fund is built primarily bottom-up irrespective of the MSCI GCC index and has no predefined style bias. It aims to return over 10% a year over the medium to long term.

Around 600 stocks are screened for size (\$500m minimum) and liquidity (\$0.5m daily trading). This shortlist of 200 names (representing 85-90% of the region's market cap) is reduced to 90-100 stocks that are researched in depth. The final list includes large liquid companies and names added on qualitative grounds by the analysts. The preference is for companies with sound business models, sustainable earnings,

dividends, reasonable or low valuations and a catalyst.

The portfolio holds 35-40 stocks. Position sizes can be 1-3% for less-liquid names with considerable upside (up to a total of 15-20% of the fund), 3-5% for liquid names with at least 20% upside and 5-10% for extremely liquid names (above \$10m a day) with at least 30% upside. Exposure to individual countries is limited to 50%, resulting in a forced underweight to Saudi Arabia. Stop losses (10% absolute monthly fall) prompt a re-evaluation of the investment case.

The fund is priced monthly. Cash can reach 50%. Turnover averages 50%.

PORTFOLIO REVIEW

The fund is in a period of transition and Sarwar believes it will take some time before the restructuring of the portfolio is complete, as he is being deliberately cautious in timing his move back into the market. Furthermore, owing to the exceptional market conditions, the team has applied and obtained the authorisation from the regulator to raise cash up to 100% of the assets.

Portfolio activity over the year has included cutting back the exposure to Saudi Arabia in

Q1 on input from both top-down and bottom-up and reducing the larger banking names in Kuwait in Q2. This move was offset by going back into selected Saudi names, such as Arabian Pipes. Exposure to Oman was also cut to zero on valuation grounds.

Cash was built in October and November and, at review, was around 60% of the total assets.

Turnover has been higher than usual over the last year and is estimated to be above 100%.

PERFORMANCE ANALYSIS (NOVEMBER 2008)

The fund has achieved an enviable track record against both benchmark and comparable peers. Success has resulted primarily from solid bottom-up stock selection. Top-down asset allocation calls have also helped, in particular in 2006 and in the last month.

Over the last 12 months, the fund has once again performed strongly. Up until September 2008, the vast majority of the added value came from stock selection. The underweight in Saudi Arabia hurt in the fourth quarter of 2007 (and explains the fund's underperformance against its MSCI benchmark for

calendar year 2007) but eventually came right in the first quarter of 2008, as the Saudi market corrected. Stock selection in Saudi Arabia and the UAE was strong in the second quarter while the move out of Kuwaiti banks proved early. More recently, asset allocation has been the main driver. At the stock level, Arabtec, Kipco, Sabic (underweight), Zain (zero weighted), Qatar Islamic Bank were the main positive contributors. In contrast, Emaar and Agility have detracted.

DISCRETE PERFORMANCE (CALENDAR YEARS)

	2004	2005	2006	2007	YTD 31/ 10/2008
	%	%	%	%	%
Fund		56.8	-13.9	43.9	-28.4
Index**				42.9	-37.8

** S&P/IFCI GCC

All of the views expressed in this research report accurately reflect our committee's views regarding any and all of the subject securities or issuers. No part of the committee's compensation was, is or will be, directly or indirectly, related to the specific recommendations or views expressed in this research report. © [2008] The McGraw-Hill Companies, Ltd trading as Standard & Poor's ("S&P") 20 Canada Square, Canary Wharf, London, E14 5LH Tel: +44 (0)20-7176 3800. All rights reserved. No part of this publication shall be reproduced, stored in any retrieval system or transmitted in any form electronic or otherwise without the prior written consent of S&P. Any part of the publication by S&P of which this page is a part is made accessible subject to the terms and conditions which are accessible at the url address below ("S&P Terms") - by accessing and viewing this page and/or and pages associated with or attached to it you accept the S&P Terms. Go to <http://www.funds-info.standardandpoors.com> Performance Data Source - © 2008 Morningstar, Inc. All Rights Reserved. The performance information contained herein: (1) is proprietary to Morningstar and/or its content providers; (2) may not be copied or distributed; and (3) is not warranted to be accurate, complete or timely. Neither Morningstar nor its content providers are responsible for any damages or losses arising from any use of this information. Past performance is no guarantee of future results.