May 2012 Monthly Comment written 31 May 11 AM CDT

The third annual mid-year euro debt scare really got going in May, making the month similar to May 2010 and August 2011 in terms of poor performance. We estimate we lost 4%-5% this month. The MSCI Frontier Markets (FM) Index dropped 5%, while the S&P 500 fell 6%, and the MSCI EAFE and MSCI Emerging Markets (EM) indices each dropped 11%, all on a total returns basis through May 30 (final monthly values for all indexes we cite are not available as we write this). For the year, we remain up 4%, while the S&P 500 is up 5%. MSCI EM is now flat (it was up 18% after February), as is MSCI FM. MSCI EAFE is down 3%. Lower prices and good earnings caused our weighted average trailing portfolio PE to fall to 5.8, the lowest month-end value we've ever had (we did reach 5.7 intra-month in November 2008). Price/book of 0.9 tied a prior low, while our dividend yield rose to 5.7%. Further, the new stocks we are buying are cheaper than our weighted average. This year we bought seven new positions that we still hold. The current, trailing PEs of these positions are: 5.1, 4.1, 8.6, 3.9, 5.1, 2.6, and 1.7. Lest one conclude that stocks this cheap must be dogs, these seven companies have an average trailing return on ending equity of 27.9%, and we estimate their local currency profit growth will average 16% this year. All seven of these companies are the clear market leader at what they do in their home country. The ability to buy companies like these at valuations this low explains why our cash position dropped from 14% at the end of December to 5% at the end of April and May. We have written extensively about Europe's problems and we remain worried about their effects on the global economy and possibly our near-term performance. But we like our chances in the medium to longer term with the portfolio we have at current valuations.

In May, we traveled to Cambodia, Laos, Myanmar, Tanzania, and Zimbabwe. Zimbabwe continues to be one of the more fascinating countries on the planet. Since dollarization occurred in early 2009, the government has little money to spend and the central bank can't print its own currency, making Keynesians and Monetarists shudder. How have they done in this fiscal and monetary straight jacket? The IMF says RGDP grew 6% in 2009, 8% in 2010, and 9% in 2011. We profiled Zimbabwe in depth in Frontaura Observer #15 back in September 2009. That piece was one of the most popular we have written and it mostly remains fresh today, although we should provide an update on one anecdote. When we visited in June 2009, we noted that there was virtually no automobile traffic. In May 2012, we experienced genuine evening rush hour bumper-to-bumper traffic. Ah, progress! Despite banking system liquidity issues that can cause delay in payments, as there is no lender of last resort, people somehow have the money to buy gas (at much more expensive prices than in 2009 we would add), and unlike in the hyperinflationary days, gas is actually available. Locals told us that the traffic jams that have developed over the past six month are the worst in their lifetimes (although by global standards, traffic is not bad). But the good news does not stop there. Electrical outages are now common, as demand is growing. These are high-class problems compared to the prior hyperinflation and an economy previously shrinking at a double-digit percentage rate. Political risks remain high, of course, and space does not allow us to get into that. We attended the fourth iteration of an investment conference that commenced in 2009. The mood was ebullient in 2009 as hyperinflation ended, but enthusiasm has declined some each year. The stock market peaked in October 2009 and is off 21% from a more recent high in June 2011. But the economy and company earnings continue to grow. It is what contrarians like us look for.

Frontaura Global Frontier Fund

Fund Objective

Bloomberg Tickers: FRGLFRO US Equity, FRGLFRC KY Equity

Investing exclusively in publicly traded companies in frontier markets, provide investors with a net return series that over multiple years exceeds that of the major global developed and emerging equity indices.

Investment Strategy

We seek to exploit pricing inefficiencies in frontier equity markets. Our investment approach uses both top-down country factors and bottom-up company factors. At the country level, we examine sovereign risk and calculate country scores that measure currency vulnerability. At the company level, we model each company's discounted cash flow using our proprietary valuation tool that accounts for expected exchange rate changes and fading rates of return on invested capital and profit growth as time passes. Ultimately, we aim to own solid businesses at attractive prices in stable or improving countries.

Performance through May 2012[1]

Period	Frontaura	S&P 500	MSCI EAFE	MSCI Emerging	MSCI Frontier
2007 Q4	2%	- 5%	- 5%	- 7%	4%
2008 Q1	1%	- 9%	- 9%	- 11%	- 2%
2008 Q2	6%	- 3%	- 2%	- 1%	2%
2008 Q3	- 11%	- 8%	- 21%	- 27%	- 23%
2008 Q4	- 25%	- 22%	- 20%	- 28%	- 39%
2009 Q1	- 2%	- 11%	- 14%	1%	- 17%
2009 Q2	28%	16%	25%	35%	35%
2009 Q3	17%	16%	19%	21%	11%
2009 Q4	- 1%	6%	2%	9%	- 10%
2010 Q1	10%	5%	1%	2%	11%
2010 Q2	5%	-11%	- 14%	- 8%	- 10%
2010 Q3	9%	11%	16%	18%	14%
2010 Q4	9%	11%	7%	7%	8%
2011 Q1	2%	6%	3%	2%	- 5%
2011 Q2	- 1%	0%	2%	- 1%	0%
2011 Q3	- 10%	- 14%	- 19%	- 23%	- 12%
2011 Q4	- 6%	12%	3%	4%	- 2%
2012 Q1	6%	13%	11%	14%	6%
2012 Q2	- 2%	- 6%	- 13%	- 12%	- 6%
2008	- 28%	- 37%	- 43%	- 53%	- 54%
2009	46%	26%	32%	79%	12%
2010	37%	15%	8%	19%	24%
2011	-15%	2%	- 12%	- 18%	- 19%
2012	4%	5%	- 3%	0%	0%
ITD CAGR	5.9%	- 1.4%	- 9.1%	- 6.0%	- 12.8%

Holdings Summary

Country	Holding
Vietnam	16%
Nigeria	8%
Qatar	8%
Tanzania	8%
Zimbabwe	6%
Pakistan	6%
Iraq	5%
Estonia	5%
United Arab Emirates	4%
Serbia	4%
Ukraine	4%
Cambodia	3%
Botswana	3%
Senegal	3%
USA (cash only)	3%
Rwanda	2%
Romania	2%
Bulgaria	2%
Laos	1%
Cote d'Ivoire	1%
Oman	1%
Cyprus	1%
Colombia	1%
Ghana	1%
Montenegro	1%
Others	1%

Industry	Holding
Banks	27%
Industrials	16%
Consumer Discretionary	16%
Consumer Staples	15%
Telecommunication Services	6%
Cash	5%
Specialty Finance	3%
Insurance	3%
Energy	3%
Materials	2%
Diversified	2%
Asset Management/Brokerage	1%

Portfolio Statistics

Portfolio Price to Earnings	5.8
Portfolio Price to Book	0.9
Portfolio Dividend Yield	5.7%
Return on Ending Equity	21.7%

Terms / Service Providers

Management Fee	2%	Attorney	Foley & Lardner LLP
Performance Fee	20% with high-water mark	Auditor	RSM McGladrey, Inc.
Subscription	Minimum: $1,000,000; new investors accepted monthly	Fund Administrator	Michael J. Liccar & Co.
Withdrawals	2-year lockup, quarterly with 90-day notice	Global Custodian	Bank of New York Mellon

1 Frontaura returns are actual returns, net of all fees, through 31 May 2012 with a subject-to-change estimate for the most recent month, for an investor joining the fund at inception, making no further contributions, and making no withdrawals. Investors joining on other dates, making additional contributions, or making withdrawals may have different returns. Returns for 2007 Q4 commence 1 November 2007. Index returns are on a total return basis, net of any withholding tax, through 30 May 2012, as final index values for May are not available at time of publication.

2 Market, portfolio, and most recent 12 months of reported fundamental data as of 31 May 2012. Portfolio PE and PB are the harmonic means of all positions, weighted by position size. Portfolio dividend yield and return on ending equity are the means of all positions, weighted by position size. The yield on Frontaura Global Frontier Fund is less than our portfolio dividend yield due to cash held, withholding taxes, management fees, and operating expenses. At present, we retain all income, rather than distribute it.

Disclaimer

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