Quarterly Letter – 2009 Q1

We traveled extensively in Q1, visiting companies in nine countries and attending two regional conferences where we met companies from over one dozen other countries. In our Q4 letter, we provided a lengthy assessment of how our frontier markets are faring during the global recession. Despite meeting nearly 100 companies in Q1, there is little we would change from what we wrote at the beginning of this year. Our view is that the United States and much of the world is experiencing a once in several generations debt deleveraging. By definition, this will be slow and painful. Economic recovery will not occur as rapidly or be as robust as in other post-World War II recessions, in our opinion. Thus, we approached 2009 as a year where patience and discipline would be key. We sought to stick to our investment principles as modified slightly by our Q4 experience:

- be long-term minded, buying simple businesses that we can understand and model;
- favor companies that are direct plays on frontier countries with stable or improving prospects;
- buy or top-up positions at a discount to our estimate of intrinsic value, and (Q4 lesson) use limits well below the current trading price in this environment;
- trim or sell positions if they rally beyond our estimate of intrinsic value, and (Q4 lesson) don't justify exceptions to this rule in this environment; and
- in this environment, be cautious especially of value traps where the stock price declines ahead of the fundamentals, making the stock look very attractive on a trailing valuation basis.

So while what we wrote in Q4 still holds, here are observations from our travels and experience in Q1:

1. The global recession is affecting the frontier countries we are invested in with a delayed impact, with Q1 being the first quarter of full effect (Q4 had a partial effect). Nevertheless, we expect some companies will continue to show no impact in their Q1 results.
2. Many of the economies we invest in are in better fundamental shape than the US and the developed world, but they are also smaller and less robust. Their smaller size at some point could make them vulnerable to an extended, deep global downturn.
3. As-reported median EPS growth for our portfolio companies was 1% in 2008. By comparison, US S&P 500 as-reported EPS fell 78%. We expect our portfolio to have roughly flat profits again this year, although our view certainly may change as events unfold.
4. Current estimates show that all 14 of our portfolio countries should have positive GDP growth in 2009.
5. To date, remittances from overseas foreign workers generally have held up better than expected.
6. Parent companies of three mobile phone operators we have owned increased their ownership in the past five weeks, taking advantage of lower prices. For multinationals, emerging and frontier markets offer continued growth prospects at reasonable prices.
7. Banking systems in many countries we invest in are sound, with loan and profit growth occurring in 2008 and possibly again in 2009. If the regulations in place in

countries like Egypt, Mauritius, and Peru existed in the US, the ongoing banking crisis most likely would never have occurred.

8. Several disparate frontier companies we follow that were affected by the global recession in late 2008 reported volume rebounds in February after they significantly cut pricing. We find these data points interesting, but are unsure of their importance. For example, revenue and margin rebounds will take longer and the volume increase may signal only the end of a spending collapse rather than the beginning of a spending upturn.
9. Healthy disinflation continues throughout our universe. Deflation is not a concern yet[1].

Let us elaborate on some of the above points. The global recession is severe enough that every country is affected, and some frontier countries are among those proportionally the most affected—Estonia, Kazakhstan, Latvia, Lithuania, Romania, and Ukraine, for example. While we have no investments in these places, several of our portfolio countries, such as Nigeria and Vietnam, have their own homegrown crises that the global recession has made worse. In other countries that could <u>not</u> be said to be in crisis—Egypt and the Philippines come to mind—certain segments of the economy began to see pronounced global recessionary effects during Q4. This included not just directly affected sectors such as exporters and tourism, but also producers of consumer discretionary products for the local market. In other words, local consumers, who have not lost their jobs, are not maxed out on credit cards, and are not underwater on their mortgages (indeed these consumers likely have no credit cards or mortgages), voluntarily began reducing consumption of non-staple items after seeing what was happening in the world. It is hard to gauge how long lasting this psychologically driven consumption reduction will last. It is clear that most producers of staple products in these countries (e.g. mobile phone operators, consumer-packaged goods) are <u>not</u> seeing the same physiological impact, as consumption of their products are steady. We continue our long-standing practice of favoring frontier companies that serve frontier markets rather than those that export to global markets.

So to date in the countries in our portfolio, we have seen more second-order (e.g. psychological) effects than first-order effects (e.g. reduced spending due to an income reduction). We believe the first-order effects will come, but gauging their delay and magnitude is largely speculation. If a company we are watching shows no effect in its results through Q1, does that mean it will have no effect, or just that it has not yet occurred? Further, as stock prices are already down significantly, will the impact be any greater than what is already in the stock price? We have grappled with these questions in recent months.

Certainly, the evidence to date points to the global recession affecting our portfolio countries and companies less than you might expect. Although there were some Q4 disappointments, the median 2008 reported EPS change of our portfolio companies is still

[1] Deflation is occurring in Zimbabwe now that its economy has dollarized and hyperinflation has ended. Since its last reported inflation rate in 2008 was 231 million percent (inflation immediately prior to dollarization would have been even much higher than this but authorities stopped calculating the rate in October), no one is complaining that prices have fallen 2%-3% per month in 2009.

positive at +1%[2] for 2008, a sharp contrast with the S&P 500 where the reported EPS change was -78%[3]. We expect a similar level of EPS in 2009, although this expectation could change depending on the global situation. One statistic we've watched at the country level is remittances (overseas foreign workers sending money home to their family members) for signs of weakness as South Asian, Egyptian, and Filipino workers lose their jobs in the US, Europe, and the Middle East. In magnitude, remittances can equal 10% or more of some country's GDP. Data to date are holding up better than expected, with some countries such as Bangladesh still posting double-digit percentage remittance gains over last year[4].

Current estimates show that all 14 countries we invest in should have positive GDP growth in 2009. No doubt, these estimates are on the decline—as they are for developed and emerging countries—and we cannot rule out a slip into negative territory for one or more of our countries. But as a whole, we will see economic growth this year, with average GDP currently up an estimated 5%, or 3% if you exclude Qatar. See table 1 for details.

So with our portfolio countries and their banking systems generally in better shape than the US and the developed world, we worry about a war of attrition. Will the relative strength of our countries ebb away if they face wave after wave of economic bad news should the developed world have a deep and prolonged downturn? Size may matter in this context. On the other hand, the IMF, with the G20 promising to enlarge its resources greatly, exists for this very mission of helping developing countries through global economic shocks. This could mitigate the size issue.

Some are seeing and acting on opportunities in our universe. Owners of several mobile operators we know have increased their holdings recently. On March 13, PLDT, parent of Piltel, the second largest Philippine mobile operator by subscribers, announced it was buying out the minority owners at a yet-to-be announced premium. On April 5, France Telecom announced it would increase its ownership of Mobinil, the largest Egyptian mobile operator by subscribers, from 36% to 51%, paying an 82% premium on the acquired shares[5]. And

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[2] This number may change slightly as a few stragglers have yet to report.

[3] We state the reported EPS change for simplicity and to avoid the all-too-common bias with operating earnings where expenses integral to the running of a business (e.g. inventory and receivable write-offs; layoff expenses; facility closings) are repeatedly excluded from earnings. Our portfolio's operating EPS performance would definitely be stronger than the reported EPS figure. To cite two examples, Kingdom Hotel Investments grew operating income 67%, but its reported EPS dropped 58% as it wrote down investments in several projects it canceled, and as gains from sale in 2007 did not reoccur. Orascom Telecom grew operating income 15%, but EPS dropped 76% as large gains from sale in 2007 did not reoccur. Nevertheless, our median holding slightly grew EPS in 2008 even with these items.

[4] We do worry that a repatriation effect could be boosting remittances, but it is difficult to tell if that is actually occurring. Workers about to return home tend to remit higher amounts as they leave their country of employment, so with more workers than normal returning home due to job losses, the data could remain robust for a while then drop sharply once the workers are home.

[5] As of this writing, the outcome of this change in control is uncertain as Egypt's capital markets regulator ruled that France Telecom must make a mandatory tender offer to all minority shareholders at the same premium price. France Telecom has said it will not do so.

on April 9, France Telecom also announced it was assuming majority control of Sonatel, the West African fixed and mobile operator in Senegal, Mali, Guinea, and Guinea-Bissau. France Telecom will increase its ownership from 42% to 52% by buying part of the government's stake at a 36% premium to the last traded price[6]. We are owners of Piltel and Sonatel; alas, we sold Mobinil during Q1 as it had jumped nearly 75% from its October low and was trading above our estimate of intrinsic value. We still would benefit indirectly if the Mobinil purchase occurs, however, as France Telecom would be buying shares from Orascom Telecom, which we own.

Table 1
Frontaura Global Frontier Fund
Real GDP Change Estimates
April 2009

Country / Region	2009	2010
Developed Areas		
United States	-2.6%	0.2%
Euro Area	-3.2%	0.1%
Japan	-5.8%	-0.2%
Frontaura Portfolio Countries:		
Bangladesh	4.5%	4.0%
Botswana	1.0%	4.7%
Cote d'Ivoire	3.7%	5.1%
Egypt	3.3%	1.4%
Nigeria	2.9%	4.2%
Pakistan	1.0%	2.5%
Philippines	2.9%	4.4%
Qatar	29.0%	17.1%
Senegal	3.0%	5.6%
Sri Lanka	2.5%	3.5%
Tanzania	4.0%	6.0%
Vietnam	4.0%	5.8%
Zambia	3.2%	4.0%
Frontaura Average	5.0%	5.3%
Frontaura Average ex Qatar	3.0%	4.3%

Source: compiled by Frontaura from various sources to include IMF, World Bank, broker research, and Frontaura estimates.

[6] Regulations on the BRVM, the French West African regional stock exchange, do not require France Telecom to make a tender offer to minority shareholders. Nevertheless, this news reversed a slow decline in Sonatel's share price.

Even if the close timing of these three telecom transactions is only coincidence, as some of them may have been in the works for an extended period, we think what they do have in common is target's promise of good growth and low valuation. All had single-digit PEs at the pre-offer trading price.

The Slow March of Progress

It may not seem like it from the headlines in the developed world, but capitalism continues its slow march forward around the globe. The world's newest stock market opened in Syria in March, making it the 135th country by our count to have a stock exchange. This is just the latest of numerous countries currently or formerly hostile to the US that opened bourses over the last two decades. For example, in the past five years, Libya opened an exchange in 2008, and Iraq reopened an exchange in 2004. Iran's exchange dates to 1968, and while North Korea does not have an exchange, it does now have a mobile phone network. In December, the Koryolink network, 75% owned by Orascom Telecom, began operations, initially covering Pyongyang. Technology be it fax, e-mail, the internet, or mobile phones, makes it harder and harder for totalitarian governments to maintain their control over their populations, and despite the limitations on North Korea's network, we can't help but think it will play some role in the eventual liberalization of that country.

Performance

After the turmoil of Q4, Q1 was a placid quarter for us with each month within two percentage points of break-even, and overall performance down 1.67%. A strong US dollar hurt our returns, as we gained about 1.4% for the quarter in local currency. Global indices were much more volatile—plummeting in January and February, before rocketing back in March with one of the sharpest rallies since the 1930s. For the entire quarter, most global indices other than emerging markets were solidly in the red, however, with total returns on the S&P 500, MSCI EAFE, MSCI Emerging Markets, and MSCI Frontier Markets at -11%, -14%, +1%, and -17%, respectively. Our total return from our November 2007 inception to date is now -28%, while total returns of the aforementioned indices are -47%, -54%, -56%, and -61%, respectively.

Our weighted average trailing valuation and return metrics remain excellent with the portfolio PE, price/book, and dividend yield at 6.3, 1.0, and 6.7%, respectively. The weighted average return on ending equity of our portfolio companies is 33.6%. Performance, valuation, and portfolio mix information appear in the Appendix.

Country Attribution and Discussion

Our biggest country winners in Q1 were the United Arab Emirates and Pakistan, where our positions were up 125% and 54%, respectively. Holdings in the Philippines, Vietnam, and Sri Lanka all gained between 10% and 20% for us. On the losing side were our positions in Botswana, down 41%, and Nigeria, down 35%. Our stocks in Zambia, Bangladesh, Qatar, and Senegal all dropped between 10% and 20%. As we only own one to three stocks per country, some of these performances are more stock driven, such as Kingdom Hotel Investments in the UAE, than a reflection of country performance.

Pakistan's strength surprised us, yet it serves as an example of how good things can happen when good businesses trade at extremely low valuations. We note with irony that MSCI kicked Pakistan out of its emerging market index on the last trading day in December, prior to the country's Q1 rally, demonstrating that index inclusion or exclusion can be a contra-indicator.[7] In fairness to MSCI, the Karachi All Share Index rose a more muted 12% in Q1 and was only back to its December 24 level by quarter end.

Surprising us on the downside was Qatar. In times where fears of global economic recession dominate investor concerns, one might have thought that the world's fastest growing economy—the IMF estimates Qatar will grow 29% real in 2009—would be more resilient. Instead, the DSM 20 Index dropped 29% in the quarter. Qatar's economic growth is occurring as the country ramps up its liquefied natural gas production, from 31 million tons annually in 2007 to 77 million tons in 2012. The $13 billion Qatargas II project went live in April, contributing 15.6 million tons of this expansion. This project will be capable of supplying 20% of the UK's natural gas needs.

Geithner, Take Notice!

Regulatory authorities in Qatar continue to demonstrate they are willing to bend over backwards to support the banking system, which generally is well capitalized with few problem loans to begin with. Last year, the sovereign wealth fund Qatar Investment Authority announced they would inject an extra 10% of equity capital into banks in two stages as a show of their support. Commercial Bank of Qatar (CBQ), which we own, took this money that they did not really need, and then increased their annual dividend by an amount similar to the first stage of new capital. At quarter end, CBQ traded at a trailing PE of 5.3, with price/book at 0.9, and a dividend yield of 15.1%. EPS grew 61% in 2007 and a further 15% in 2008, while non-performing loans (NPLs) are less than 1% of gross loans and are 99% provisioned for (we do expect NPLs to rise). CBQ's ratio of tangible equity to tangible assets was 16.3% at year-end before the QIA injection, making it extraordinarily well capitalized. By comparison, according to Bloomberg, the Swiss global bank UBS has tangible equity to tangible assets of only 1.0%!

The Q1 Qatari equities selloff created an issue for Qatari banks holding equities in their investment book. We hate this all-too-common practice of banks playing the stock market, as it nearly always ends in tears around the globe[8]. We tolerated it in CBQ's case as the investments represented only 8% of equity. In March, Qatar's central bank rode to the rescue, announcing they would buy all listed equities in banks' investment portfolios at the December 31 price, and by quarter end this process was complete. Problem solved. But it gets even better. Rumors are that the central bank may more greatly restrict listed equity investments for banks going forward, a move we wholeheartedly support. But just in case equities go back up, over the next five years banks have the option to repurchase what they

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[7] MSCI removed Sri Lanka from its emerging markets index in May 2001. The Sri Lankan index rose 7.7-fold over the next 67 months in US dollar terms.

[8] Banks tend to begin investing in the market during a bubble where you "can't lose." When the inevitable drop occurs and the market burns their fingers, the practice subsides…until the next bull market is underway. This pattern repeats in country after country around the globe.

sold (perhaps within the forthcoming tighter restrictions) at the same December 31 price. While we do not favor government intervention, moves by the Qatari authorities have clearly been supportive of their banking system and financial markets, with as yet no observable negative consequences.

Regional Attribution

Regionally, sub-Saharan Africa was a laggard in Q1. We made money in Southeast Asia (up 17%), Middle East/North Africa (MENA, up 8%), and South Asia (up 5%), but we lost 21% in sub-Saharan Africa. This region has completely fallen out of favor with investors, and it appears to us to be driven primarily, although not entirely, by the exodus of global investors. These investors exited other more liquid regions earlier, such that while their selling may have subsided elsewhere, it is still ongoing in sub-Saharan Africa. For the moment, local investors, who can be very momentum oriented, are standing aside, waiting for the foreigners to finish. While foreigners are a minority of the ownership, the combination of simultaneous sellers and a dearth of buyers is pushing down prices. At quarter-end, our regional split is 29% MENA, 24% sub-Saharan Africa, 17% South Asia, 13% Southeast Asia, and 16% US (cash only).

Portfolio Changes

Our increase in cash from 8% to 18% during the quarter was not the result of a deliberate decision to raise cash. Rather, it was the outcome of two individual decisions to exit positions, year-end dividend payments, some investor inflows, and deliberative patience with regard to buying (see bullets at the beginning of this letter). Valuation movements did cause us to top up three existing holdings and also to trim three positions. In five of these six cases, we saw a favorable price move between the transaction date and quarter end (topped up positions rose in price; trimmed positions fell in price), and in the other case, the price was flat. One sell decision was due to our increasing discomfort with a company's lack of transparency (incomplete and inconsistent information flow), combined with its valuation above our portfolio norm and its potential vulnerability to economic slowdown. The other sell decision was entirely price driven, as the stock rallied beyond our estimate of intrinsic value. While our positions have declined to 23 stocks in 14 countries, this remains within our target range of 20-25 holdings in 10 or more countries. Nevertheless, we reiterate what we wrote in an earlier letter that we might increase our holdings beyond 25 during this downturn. We have a number of stocks we have watched for some time, and given the increased economic uncertainty, when we do initiate new positions, we may have a greater number of relatively small positions that we ramp up over time.

Stability? Normalcy? Data Mining?

We're not fans of excluding things to make a point (because the exclusions tend to be strongly biased toward eliminating bad data points and keeping all of the good data points to present a more favorable picture than really occurred), and we are also wary of focusing too much on a handful of data points. Having stated that, let us now violate both of those principles to see if we can gain any insight from recent performance. It is clear that the cataclysmic event of this global financial crisis to date was the collapse of Lehman Brothers in September 2008. Nearly every asset class in the world other than US treasuries declined precipitously during the three months of September, October, and November. Any asset class, such as frontier markets, that billed itself as lowly correlated to equities, lost credibility during this period.

This correlation spike has begun receding however. Our inception to date correlation to the S&P 500 rose from 0.44 in August to 0.84 in October. But it has now declined slightly to 0.70 through March. Similarly, our correlation to EAFE rose from 0.62 in August to 0.89 in October, but is now down to 0.67. Our correlation with MSCI Emerging Markets (EM) was 0.65 in August, peaked at 0.86 in October, and is now 0.75. These are only a few data points of course, and this story could fall apart in coming months. In fact, we would expect another spike in correlation if another Lehman-sized shoe were to drop[9]. We think recent experience shows that low correlation strategies most likely will not provide the low correlation feature when you want it the most in times of severe turmoil. But for what it's worth (and this may not be worth much to some people we realize), it might still be possible that low correlation is a benefit to be had most of the time, in times other than those of extreme turmoil. It remains for our fund to prove this, of course, over a longer period, and we can't say with certainty that it will. But it might. We note that correlations between the main geographic global indices have <u>not</u> shown a similar decline since October. The S&P 500's correlation to EAFE since our inception was 0.92 in October. It is now 0.94 through March. S&P 500 correlation to MSCI EM was 0.80 in October; it is now 0.79. EAFE's correlation to MSCI EM has dropped, from 0.97 to 0.92 over this period, but remains very high.

In the four months since November, global equity markets have remained volatile, but we have been stable with monthly returns ranging between -2% and +2% each month. In fact, other than the post-Lehman September-November period, we've never lost more than 2% per month since our inception (which we grant is only 17 months now). We would always point out that events like Lehman do happen throughout history and undoubtedly will happen again, and when they do, we may suffer considerably[10]. But during other times, and by this we do not mean only good times, for our entire existence has been in a tough global bear market, our original promise that we can deliver a return stream superior and different from the major equity asset classes looks intact. Our inception to date return outside of the three Lehman months is +6%, while the S&P 500 is -24% even with these three months excluded. Our correlation to the S&P 500 ex these three months is 0.15.

Conclusion

While we are open minded, at the moment we are skeptical of the green shoots theory that global recovery is just around the corner. Whether we are right or wrong on timing, though, we think a recovery when it does come is likely to be weak and tentative[11]. We are

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[9] We worry about the exposure of Western European banks to non-local currency loans in Eastern Europe for example.

[10] From September through November, we lost 32%, slightly worse than the S&P 500, down 30%, and slightly better than EAFE, down 35%. MSCI EM did considerably worse, losing 45%.

[11] For example, one scenario where we would be wrong on timing but correct on the quality of the recovery would be if the unprecedented level of government stimulus did lead to a near-term recovery. Since the degree of

not afraid to buy stocks in this environment, but we are very careful as to what we buy, when we buy it, and what we pay for it. The timing question is not one of trying to time the market, for one can never get that right exactly, but rather one of fundamentals—are we reasonably certain of the company's prospects and outlook over the long run in a time of uncertainty. We are stewards of your money and we want to protect your capital as best we can, while positioning the portfolio for capital appreciation in good companies available at low prices.

Uncertainty and timing is also a question with which our investor and potential investors are struggling. As we have written before, in this environment we welcome any new investors who want to dollar cost average into their initial commitment over a period of months or quarters on a schedule that makes sense for them. Current investors may also schedule follow-on investments with individual monthly contributions being of any reasonable size. We know this flexibility has made a difference to several investors and thus we want to reiterate that it remains available for any contribution series that commences in 2009. We thank you for your continued interest in Frontaura.

Regards,

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stimulus is not sustainable, however, the recovery may falter once the government inevitably withdraws the stimulus.

Statistical Appendix

Table 2
Frontaura Global Frontier Fund LLC
Quarterly and Monthly Performance
31 March 2009

Month	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%
2008	- 28%	- 37%	- 43%	- 53%	- 54%
2009 YTD	- 2%	- 11%	- 14%	1%	- 17%
ITD	- 28%	- 47%	- 54%	- 56%	- 61%

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	YTD	ITD
2007											0.4%	1.6%	2.0%	2.0%
2008	0.7%	0.6%	-0.1%	3.4%	3.9%	-1.0%	-0.8%	-2.2%	-7.9%	-17.5%	-10.7%	1.4%	-28.0%	-26.7%
2009	-2.0%	-0.4%	0.7%										-1.7%	-27.9%

* Returns for 2007 Q4 commence 1 November 2007.
Frontaura returns are actual returns, net of all fees, for an investor joining the fund at inception and making no further contributions. Investors joining on other dates or making additional contributions may have different returns. Index returns are in US dollars on a total return basis, net of any withholding tax.

Table 3
Frontaura Global Frontier Fund LLC
Portfolio Metrics
31 March 2009

Holdings Summary

Industry	Holding
Banking	18%
Cash	18%
Telecommunication Services	14%
Consumer Discretionary	13%
Consumer Staples	13%
Diversified	7%
Oil Marketing	7%
Industrials	4%
Asset Management/Brokerage	3%
Insurance	3%

Country	Holding
USA (cash only)	16%
Qatar	14%
United Arab Emirates	11%
Sri Lanka	9%
Vietnam	7%
Zambia	6%
Philippines	5%
Cote d'Ivoire	5%
Bangladesh	5%
Senegal	5%
Botswana	4%
Egypt	3%
Pakistan	3%
Tanzania	2%
Nigeria	2%

Portfolio Statistics

Portfolio Price to Earnings	6.3
Portfolio Price to Book	1.0
Portfolio Dividend Yield	6.7%
Weighted Average ROEE	33.6%

Market, portfolio, and most recent 12 months of reported fundamental data as of 31 March 2009.
Portfolio PE and PB are the harmonic means of all positions, weighted by position size.
Portfolio dividend yield and return on ending equity (ROEE) are the means of all positions, weighted by position size.