Quarterly Letter – 2011 Q2

We lost 1.1% in Q2, giving back most of our modest Q1 gain, with the year-to-date result now just above break-even at 0.4%. Figures 1 and 2 in the Appendix show our results. We wrote in the Q1 letter that both bulls and bears could find talking points for their respective scenarios in the year-to-date results, and that remains the case three months later. The bullish case is that global markets have absorbed a lot of bad news without dropping and valuations have become cheaper. In our recent June comment we pointed out that:

> *Flat performance and the passage of time can result in a portfolio becoming more cheaply valued, even more so if one invests new cash at valuations below the portfolio average. Frontaura's weighted average trailing reported PE is now 7.8. Our month-end PE was last lower in August 2010, at 7.7, before the global rally commenced after Bernanke's QE2 announcement. The last time the PE was materially lower was in June 2009, at 6.8, only a few months after markets hit their global financial crisis low. Frontaura's price/book is 1.2, a level last seen in August 2009, and last lower in May 2009, at 1.1.*

What goes up must come down

The bear case remains as it was three months ago. Political risk is high; inflation and interest rates are rising in many countries; economic growth is slowing; and the peripheral European debt crisis can't be pushed out forever and represents a global contagion risk. From our frontier markets vantage point, we've written about inflation risk for 18 months and the risk materialized. We now wonder if some countries are showing the first sign of this inflation peaking. That's a low confidence comment as year-over-year rates are likely to continue increasing for several more months. We have noticed some disinflation on a month-over-month basis, however, in countries such as Sri Lanka (where the June price level is below that of February), Uganda, and Vietnam. The data points and the countries are too few to call this a trend, though.

A handful of countries cut interest rates in June or early July, signaling the possible end to their prior inflation-induced tightening cycle. These include Serbia, which began raising rates in August 2010 from a low of 8% to 12.50% in April 2011, before cutting to 12% in June; and Vietnam, which raised rapidly from 7% in November 2010 to 15% in May 2011, before pulling back to 14% on July 4. Further, Ghana made 50 basis point cuts in both May 2011 and July 6, 2011, to reduce their policy rate to 12.5%. They had last cut in July 2010.

Some of these cuts risk being premature, as real rates never became positive in Serbia and Vietnam, and the anticipated year-over-year disinflation later this year is not certain to materialize. The cut in Vietnam surprised us and undermines some recently gained monetary credibility on the inflation-fighting front. We actually hope not to see any further cuts in Vietnam for a while, as doing so could send two possible negative signals. Either 1) the government was actually not all that serious about price stability and can't help itself in reverting back to its prior growth-at-any-cost mentality, or 2) the government is actually quite worried about a hard landing.[1] Global macro price trends support a reduced inflation

[1] We discussed Vietnam in more detail in our June monthly comment.

risk thesis. Commodity prices are off their peaks, with both oil prices and agriculture prices—the two price areas that most affect frontier countries—down some.

The impact of the end of QE2 has been thoroughly debated elsewhere with many differing conclusions, but its end is also supportive of a disinflation thesis for emerging and frontier countries (unless another one or two employment reports as dismal as June's leads the US to QE3). The prospect of better global crop output in 2011 versus a weather-plagued 2010 also supports possible food price relief for frontier counties.

So a positive second half of 2011 frontier markets scenario combines lower valuations with possible lower inflation and lower interest rates. Bears might counter that these attributes (lower valuations, inflation, and rates) could all be a sign of slowing economic growth and a possible double dip. We'll see.

Liquidity and positions

We can't control these factors of course. What we can do and intend to do is to continue discovering, researching, and buying attractively priced companies with high returns on capital. We found many such companies in Q2, but we encountered a dilemma. Many of these companies are small, or illiquid (even for frontier markets, which are less liquid to begin with), or both. In some cases the illiquidity was due to a foreign ownership limit, meaning we could acquire some shares, but not the full position size we desired. Further, we are a larger fund than before, although we will continue to stick to our self-imposed $100-million-size limit (with an upward bias over time due to performance and gradually improving liquidity) that we set at our inception. So, do we: 1) forego these opportunities; 2) violate our process and buy larger companies that don't quite pass our intrinsic value screen; or 3) buy smaller companies, at times initiating basket positions where we group together several companies with similar characteristics to comprise a position? We opted for the third choice. Naturally, this means we have more positions than before; frankly, at 48, we have more than we ever expected.[2] Figure 6 shows our concentration statistics.

Q1 earnings

Earnings season in frontier markets differs from the US. Reporting occurs later, often in the second month after quarter end and occasionally not until the third; the numbers are more volatile, as managements tend to focus only on their annual plans and not on how the quarters line up; and the reporting is more limited. For example, some companies report only semi-annually; some may report only partial information such as revenue and pretax

[2] How to count our positions is not as obvious as it might seem. In Iraq, as we've explained in previous writings, our investment thesis is a macro play without much focus on individual companies, so we have always counted all of our positions (presently 11) as only one, an Iraq basket. In Vietnam, we started with individual positions, but now due to the limitations mentioned, we have 14 positions. Nearly half of these individual positions are smaller than most of our individual Iraq stocks. Do we count Vietnam as 14, or as 1, or a number in between, as some of the Vietnam positions are similar companies that we mentally group together? Lacking conviction or cleverness, we opted to keep counting things as we always have. We count every position as one for except those in Iraq, which we only count as one. At some point, we may have to change our Iraq counting if we begin to winnow our basket to fewer companies, paying more attention to company-specific fundamentals and valuation. There are two other nuances. First, if we own a company on multiple exchanges, say in its home country and on a secondary exchange such as London, we only count this as one position, since it is only one company. Second, if we value a position at zero, we do not count it.

profit; and some may report only unconsolidated results at times other than year-end. Further, frontier investors don't tend to react to earnings the same way as US investors. So one must unlearn some developed world methods to analyze interim reports in the frontier world. We've often seen terrible numbers one period followed by blowout results the next, or the reverse. A great nine months can lead to an unbelievably bad Q4, with the year ending right in line with our original expectations when the year began.

Overall, some of our companies' Q1 results disappointed us, although there were a wide range of outcomes, good and bad. To generalize, the issues seem to be more present in our European holdings than elsewhere and, ignoring geography, more present in our banks than in our operating companies. We would characterize some of this as a hangover from the global financial crisis or its resulting austerity. Mind you, we are not talking about toxic assets going bad like in the developed world; rather, just general tough business conditions in a few countries, leading to an uptick in non-performing loans and provisions, or a decline in margins in the face of lackluster revenue. Some companies have lowered or not reinstated their dividend, although nine of our companies still have a double-digit yield.

Figure 4 shows that our three worst performing countries in Q2 were in Europe (Serbia -14%, Cyprus -10%, and Bulgaria -8%). Soft earnings contributed to this, but the poor Q2 performance was as much a reversal after strong Q1 price gains, where we were up 29% in Bulgaria, 17% in Serbia, and 8% in Cyprus. Our European investment thesis was predicated mainly on stocks being too cheap after the 2008-2009 selloff rather than on earnings growth; in fact, we did expect the earnings of some companies to decline after we bought them. Our thesis remains intact, although perhaps with not as much cushion as when we first bought into the region at the end of 2009. Overall, we project our companies to have weighted average unlevered profit growth of 11% in their current fiscal years, although we should note that our models aim to project unlevered profit over a full economic cycle, rather than to peg the exact profit a company will report each year.

Management Company News

We made two Southeast Asian trips during the quarter, to Cambodia, Laos, Myanmar, and Vietnam. See the May and June monthly comments for further discussion. We already are planning three or four trips for Q3 and Q4 that we will talk about at a later time.

We present our usual quarterly figures on performance, investment mix, and attribution in the Appendix that follows.

Regards,

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Appendix

Figure 1
Frontaura Global Frontier Fund LLC
Performance[3]
30 June 2011

Period	Frontaura	S&P 500	MSCI EAFE	MSCI Emerging	MSCI Frontier
2008	- 28%	- 37%	- 43%	- 53%	- 54%
2009	46%	26%	32%	79%	12%
2010	37%	15%	8%	19%	24%
2011 Q1	2%	6%	3%	2%	- 5%
2011 Q2	- 1%	0%	2%	- 1%	0%
2011 YTD	0%	6%	5%	1%	- 6%
Inception to Date	47%	- 8%	- 20%	- 7%	- 38%
ITD CAGR	11.2%	- 2.1%	- 6.0%	- 1.9%	- 12.2%

Figure 2
Frontaura Global Frontier Fund LLC
Monthly Performance
30 June 2011[5]

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	YTD
2007											0.4%	1.6%	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%	-28.1%
2009	-2.0%	-0.4%	0.7%	7.7%	14.4%	4.1%	1.4%	4.7%	10.6%	-1.4%	-0.2%	0.2%	46.0%
2010	-0.9%	4.2%	6.6%	4.5%	-1.2%	1.9%	3.4%	0.7%	4.7%	3.5%	1.5%	3.3%	37.1%
2011	2.8%	-3.7%	2.7%	-0.4%	1.0%	-1.7%							0.4%

[3] Returns commence 1 November 2007. Frontaura returns are net of all fees, 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. Index returns are in US dollars on a total return basis, net of any withholding tax.

Figure 3
Frontaura Global Frontier Fund LLC
Portfolio Mix and Statistics[4]
30 June 2011

Holdings Summary

Country	Holding
Vietnam	14%
USA (cash only)	10%
Pakistan	9%
Qatar	8%
Tanzania	8%
Serbia	8%
Senegal	5%
Nigeria	5%
Botswana	5%
Iraq	5%
Zambia	4%
United Arab Emirates	3%
Zimbabwe	3%
Cyprus	2%
Bulgaria	2%
Ghana	2%
Sri Lanka	2%
Colombia	1%
Cote d'Ivoire	1%
Montenegro	1%
Uganda	1%
Others	1%

Industry	Holding
Banks	31%
Cash	14%
Consumer Staples	12%
Industrials	11%
Consumer Discretionary	7%
Telecommunication Services	6%
Specialty Finance	5%
Materials	4%
Insurance	3%
Diversified	2%
Health Care	2%
Asset Management/Brokerage	1%
Oil Marketing	1%

Portfolio Statistics[2]

Portfolio Price to Earnings	7.8
Portfolio Price to Book	1.2
Portfolio Dividend Yield	4.3%
Return on Ending Equity	21.9%

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[4] Portfolio valuation statistics use the most recent 12 months of reported fundamental data as of 30 June 2011. 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.

We hold most, but not all cash, in the United States. We also include in the US total, any euros we hold in non-frontier, non-emerging countries. These euro amounts often are not material. We include all other cash we hold outside the US in that country's total, regardless of what currency the cash is in. For example, Vietnam is a prefunding market, so we include our cash there in the Vietnam total, even though nearly all of this cash is in US dollars.

Figure 4
Frontaura Global Frontier Fund LLC
5 Best and Worst Performing Countries
2011 Q2

5 Best Countries			5 Worst Countries		
Country	**Frontaura Return**	**MSCI Return[5]**	**Country**	**Frontaura Return**	**MSCI Return**
Cote d'Ivoire	157%	--	Serbia	-14%	5%
Uganda	64%	--	Cyprus	-10%	--
Ghana	27%	23%	Bulgaria	-8%	-15%
Zimbabwe	15%	9%	Tanzania	-8%	--
Sri Lanka	14%	-9%	Pakistan	-8%	2%

Figure 5
Frontaura Global Frontier Fund LLC
Significant Quarterly Country Mix Changes[6]
30 June 2011

Country	Percentage Point Change	Explanation
Vietnam	+7	Ongoing buying of new positions
United Arab Emirates	+3	New position
Pakistan	-2	Sale of appreciated position once it qualified as a long-term capital gain

[5] MSCI country indices stated on a total return basis with dividends net of any withholding tax. We show "--" if MSCI does not have an index for a given country.
[6] We show countries whose weighting has changed by two percentage points or more. Total may not add to 0 due to rounding and exclusion of countries changing by less than two percentage points. Note that we do not show the United States as we only hold cash there. See the Figure 3 footnote for a discussion of how we classify cash by country.

Figure 6
Frontaura Global Frontier Fund LLC
Portfolio Concentration[7]
30 June 2011

			Change from Prior Quarter	
	Companies	Countries	Companies	Countries
Positions	48	22	+7	-1
Top 5	25%	47%	-5	4
Top 10	42%	71%	-4	2
Top 20	64%	89%	-4	4
Top 20 + US (Cash)	75%	99%	-9	--

[7] We do not include the US in our country count and most of the percentage totals as we hold only cash there. Change from Prior Quarter represents the change in the number of positions and the change in percentage points for the top 5, 10, and 20 positions. The Top 20 + US row does include the US cash percentage in the percentage totals. See the Figure 3 footnote for a discussion of how we classify cash by country.