

Named portfolio manager(s):

Charles Hovenden (since launch)

Peer group: Fund-of-Hedge-Funds GBP

Location: London

Launch date: October 2001

Fund size (March 2011): US\$78m

Contact group: +353 1 646 1410 or
www.absolutefund.co.uk



Report date May 2011

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

Investment style

Region: Global

Strategy: Multi-strategy

Performance statistics (annualised)

	3 Years	5 Years
Fund	0.4%	2.5%
Index**	7.4%	5.2%
Interest rate ^	2.2%	3.5%
R-Squared vs Index	0.2	0.2
Beta vs Index	0.1	0.1

^ Citi GBP EuroDep 3 Mon GBP
** S&P Global 1200 TR

Risk statistics

	5 Years
Standard deviation	4.2
Downside deviation	3.9
Maximum monthly drawdown (%)	-6.5
Gaining months (%)	68.3
Sharpe ratio	-0.2
Sortino ratio	-0.2

Performance data has been supplied by the fund manager. All statistical data on this report has been run to 28/02/2011 on NAV to NAV basis, with gross income reinvested, in GBP.

Standard & Poor's opinion (May 2011)

Charles Hovenden manages this multi-strategy fund-of-hedge-funds (FOHF) in a conservative manner. He primarily invests in long/short equity (currently 53% of the fund), complemented with fixed income arbitrage, distressed and event-driven strategies. He avoids highly levered or complex strategies (eg, he focuses on pure merger arbitrage within event-driven rather than special situations), and emphasises liquid asset classes (outside distressed). He does not invest in CTA/macro unlike many multi-strategy FOHFs.

Hovenden has run the fund since launch and is solely responsible for investment analysis and decisions, even though his business partner Andrew Wheeler sometimes participates in manager meetings and acts as a "check and balance". His approach has been very consistent, with the implementation evolving at the margin, in particular with respect to strategies that are held for downside protection. Hovenden used to own short-biased credit and equity funds but has disposed of the latter over the past year as he concluded that short-sellers do not add value over a full market cycle. Instead, he believes that it is more effective to focus on low-beta equity managers with superior stockpicking abilities (both on the long and short side). As a hedge against tail risk, he has reinvested with a convertible arbitrage specialist that made over 30% in 2008 but has lost much less than equity short-sellers in the past two years.

The objective has recently been nudged down to Libor plus 3-5% (previously 4-6%) but importantly, the incentive fee structure remains unchanged (15% of gains between 6% and 24% pa, subject to a high-water mark). The fund has fallen short of this target since October 2001, delivering an annualised 3.5% in US dollar terms against 2.5% for the USD 3-month Libor, and 4.4% in sterling compared to 4% for the GBP 3-month Libor. However, unlike many FOHFs, it has generated positive returns over the past three years cumulatively, with below-average standard deviation, and has recently reached a new high water mark.

In light of Hovenden's "safety first" philosophy, the fund typically lags in strong bull markets, such as 2009-10, when performance was held back by a lack of equity beta, while low-beta managers suffered from high stock correlations, particularly in H1 2010. In spite of this, we expect Hovenden to produce returns in line with the objective and are pleased to note the fund had a strong Q1 2011. We have retained the fund's S&P AA rating.

Fund manager & team

London-based Absolute Fund Managers started its fund-of-hedge-funds business in 2001 and currently has £55m (\$89m) assets under management. Charles Hovenden (CIO) is the largest active stakeholder in the business. He is responsible for the group's investment management. Wheeler is the other active shareholder and is head of marketing. He has an investment background but concentrates on marketing and business management, leaving Hovenden free to focus on investment management.

Charles Hovenden - chemistry (Oxford University), worked as a private client portfolio manager and equity analyst at Rothschild for seven years and Bank von Ernst for four years. In 1995 he joined Banque Internationale à Luxembourg as a fund-of-funds manager. He launched Absolute Fund Managers in October 2001.

Andrew Wheeler - business studies (South Bank University), started as a private client fund manager with Fleming Investment management in 1986. From 1995 to 2001 he worked as a multi-fund manager with Dexia Private Bank in Jersey. He was head of marketing at Deutsche Bank Private Banking, London, from 2001 to 2002. From 2003 to May 2007 he was executive director at the family investment office of Unigestion (UK) Ltd. He joined Absolute Fund Managers in June 2007.

THE ABSOLUTE FUND

Cayman Islands open-ended limited liability investment company

Fund owner: Absolute Fund Management

Fund manager/adviser: Absolute Fund Managers LLP

Management style

The fund aims to preserve capital in all market conditions and achieve an annualised return of cash plus 3-5%. It focuses principally on long/short equities and arbitrage strategies, excluding CTAs and global macro funds because the manager believes these strategies are difficult to analyse. He generally steers clear of funds that largely invest in derivative structures, in order to avoid undue counterparty risk.

Equity long/short is a significant allocation within the fund, but directionality is limited by only investing in funds that are no more than 30% net long. Hovenden also held short-biased credit and short-biased equity hedge funds until early 2011 but has replaced them with different protection strategies.

The process combines top-down strategy allocation, subject to no more than 25% in any single strategy/region, with quantitative and qualitative fund selection (most added value). Hovenden determines the macroeconomic view with input from hedge fund managers, external articles and sell-side research.

Fund selection starts with a quantitative screening. Attribution analysis is then undertaken to ensure that managers add value from shorting investments as well as from going long. New ideas come from databases, prime brokers, third-party marketers and from the managers of existing holdings.

Hovenden carries out on-site interviews with key team members and the track record is verified with the administrators or prime brokers. Start-ups are avoided and there is a preference for medium-sized hedge funds to ensure access can be gained to the manager rather than the investor relations team.

The portfolio is diversified, with a target of around 40 similarly weighted funds. A maximum of 5% is permitted in any one fund, with initial investments typically sized at about 2%.

There is ongoing monitoring of holdings including visiting at least annually. Fund managers are also telephoned between visits if there is unusual performance or style drift. Sell disciplines include unexplained unusual returns, lack of access to the manager and potentially better ideas.

The fund has a 35-day notice period. Northern Trust provides a credit line to meet redemptions.

Portfolio & performance analysis (March 2011)

Charles Hovenden manages the fund with a conservative, "safety-first" approach. This has resulted in a relatively low drawdown in 2008 (-8.9% in sterling terms), followed by modest gains in 2009 and 2010, compared to other multi-strategy funds-of-hedge-funds.

US and European long/short equities were particularly disappointing last year. The two strategies together accounted for 41% of the fund, contributing 1% to performance before fees in 2010. This was mainly due to Hovenden focusing on low beta/market neutral managers (rather than long-biased funds), who suffered from high stock correlations for much of the year, particularly in H1. However, it remains Hovenden's favoured strategy as he anticipates a continued deleveraging process with plenty of corporate winners and losers.

Strategy allocation has been stable over the past year but Hovenden has added new funds across all sub-strategies, except for distressed, where he considers trimming exposure. He allocated money to a pure merger arbitrage fund in April 2011. Even though M&A spreads are fairly tight, he expects decent returns relative to cash and ideally would like to add another manager in that space. He also invested with a new convertible arbitrage manager (in addition to long-term holding Aristeia) in 2010.

The fund has recently reached a new high-water mark and has posted marginally positive returns over the past three years, compared to -7% for the HFRX Global Hedge Fund index (in US dollar to end-February 2011). It has had a successful Q1 2011 (+2.1%), with positive contribution from all sub-strategies, except for short-biased equity. However, the latter will not feature in the portfolio from May 2011.

Discrete performance (calendar years)

	2007	2008	2009	2010	YTD 28/02/2011
	%	%	%	%	%
Fund	8.0	-8.9	7.5	1.7	1.9
Interest rate ^	5.9	5.8	1.3	0.6	0.1
Index**	8.4	-17.1	17.3	15.5	1.8

^ Citi GBP EuroDep 3 Mon GBP

** S&P Global 1200 TR

Share class screened: KYG0060S1241 (A)

1100110519-FB76B7A95

STANDARD & POOR'S



Portfolio characteristics

(1 March 2011)

No. of holdings	39
Turnover ratio (%)	30
% in top 10	31

Key holdings

	%
Aristeia International *	4.5
Rockhampton *	4.1
Lyon Street	3.0
Feingold O'Keefe *	2.9
Troob *	2.8
Southpaw *	2.8
Coast Value *	2.8
Rockview	2.8
Harvest *	2.7
Brencourt	2.7

* In key holdings a year ago

Allocation breakdown

	%
Cash/net liabilities	1.7
Convertible arbitrage	7.0
Distressed	15.9
Event-driven	6.8
Fixed income arbitrage	12.9
Long/short equity	53.2
Other	2.5

STANDARD & POOR'S

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Symbols and definitions

Long-only fund ratings

AAA The fund demonstrates the highest standards of quality in its sector based on its investment process and management's consistency of performance as compared to funds with similar objectives.

AA The fund demonstrates very high standards of quality in its sector based on its investment process and management's consistency of performance as compared to funds with similar objectives.

A The fund demonstrates high standards of quality in its sector based on its investment process and management's consistency of performance as compared to funds with similar objectives.

Fund-of-hedge-funds ratings

Absolute return fund ratings

Specialist fund ratings

AAA The fund demonstrates the highest standards of quality based on its investment process, risk awareness and consistency of performance relative to its own objectives.

AA The fund demonstrates very high standards of quality based on its investment process, risk awareness and consistency of performance relative to its own objectives.

A The fund demonstrates high standards of quality based on its investment process, risk awareness and consistency of performance relative to its own objectives.

Ucits III flexible beta fund ratings

AAA The fund demonstrates the highest standards of quality based on its investment process, risk awareness and consistency relative to its own objectives and relative to comparable flexible beta funds.

AA The fund demonstrates very high standards of quality based on its investment process, risk awareness and consistency relative to its own objectives and relative to comparable flexible beta funds.

A The fund demonstrates high standards of quality based on its investment process, risk awareness and consistency relative to its own objectives and relative to comparable flexible beta funds.

All fund ratings

Not Rated (NR) Funds designated as Not Rated currently do not meet the requisite performance standards and/or the minimum qualitative criteria to achieve a fund rating.

Under Review (UR) Ratings are placed Under Review when significant management changes occur at the fund manager or fund management team level and Standard & Poor's Fund Services has not had the opportunity yet to evaluate their impact on the qualitative appraisal.

(New) Signifies where a major event has occurred for which there is no fund-specific track record available. This includes: funds recently launched, the implementation of a new investment process or mandate and may include structural changes within a fund team.

Tenure Review (TR) The fund manager/team involved in the management of the fund does not currently have the minimum 12 months' relevant investment management experience required to be eligible to be considered for a rating.

Long-term fund management rating LTFMR The fund has been rated in the A/AA/AAA fund rating band for five consecutive years or more, and continues to hold a rating.

Bond fund volatility ratings

The bond fund volatility rating is our current opinion of a fund's sensitivity to changing market conditions. Volatility ratings evaluate the fund's sensitivity to interest rate movement, credit risk, investment diversification or concentration, liquidity, leverage and other factors. For V1-V4 categories, risk is considered relative to a portfolio composed of government securities and denominated in the base currency of the fund.

V1 Bond funds that possess low sensitivity to changing market conditions. These funds possess an aggregate level of risk that is less than or equal to that of a portfolio comprising government securities maturing within one to three years, and denominated in the base currency of the fund. These funds possess an aggregate level of risk that is less than or equal to that of a portfolio comprising the highest quality fixed income instruments with an average maturity of 12 months or less. Within this category, certain funds are designated with a plus sign (+), indicating extremely low sensitivity to changing market conditions.

V2 Bond funds that possess low to moderate sensitivity to changing market conditions. These funds possess an aggregate level of risk that is less than or equal to that of a portfolio comprising government securities maturing within three to seven years, and denominated in the base currency of the fund.

V3 Bond funds that possess moderate sensitivity to changing market conditions. These funds possess an aggregate level of risk that is less than or equal to that of a portfolio comprising government securities maturing within seven to 10 years, and denominated in the base currency of the fund.

V4 Bond funds that possess moderate to high sensitivity to changing market conditions. These funds possess an aggregate level of risk that is less than or equal to that of a portfolio comprising government securities maturing beyond 10 years and denominated in the base currency of the fund.

V5 Bond funds that possess high sensitivity to changing market conditions. These funds may be exposed to a variety of significant risks including high concentration risks, high leverage, and investments in complex structured and/or less liquid securities.

V6 Bond funds that possess the highest sensitivity to changing market conditions. These funds include those with highly speculative investment strategies with multiple forms of significant risks, with little or no diversification benefits.

Absolute return fund N ratings

The N rating is Standard & Poor's indication of a fund's potential capital stability in normal markets. It is a qualitative rating but is based on annualised weekly downside deviation. N1 is the most stable and N9 the least.