



LIFE SETTLEMENTS FUNDS

SUM ASSURED

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EXCHANGE PLACE

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Chairman's Message

Welcome to 2010. I had intended to talk about some of the positive changes we're introducing in the fund, but we'll save that for the next newsletter. I think it's more important that we use this time to address some economic issues and reaffirm the benefits of the life settlements asset class.



Ian Cotton

Whilst the majority of our investors are based in Australia, we have of course substantial numbers in 19 other countries throughout the world, all at varying stages of the economic cycle. As we enter 2010 the general consensus appears to be one of "guarded optimism".

The world may have avoided a depression; however it's going to take many years to rebuild. In the meantime there will continue to be casualties and growth will be slower than we have come to expect in recent years.

What this means is that non-correlated investments, such as life settlements, will have a crucial role to play in the next few years. Why? Because of the volatility and subdued returns expected in the traditional asset classes of equities and real estate.

Australia has been lucky to date in regards to residential real-estate as we have not seen the same declines as experienced in the USA and Europe. However we presently have some of the most over-priced cities in the world, so we need to maintain high immigration levels to sustain the demand.

Similarly with equities, 2009 saw great leaps made in recovering part of the value that disappeared from 2008 to March 2009.

However most markets have stagnated over the last 4 months or so, with some pessimists considering they rose too quickly and do not accurately reflect the state of the economy. Plus we've already seen that diversifying across various sectors in equities is not really diversification at all.

To underpin this no-one yet knows with any certainty what long-term impact the government stimulus packages will bring. The debts that governments all over the world have incurred have to be repaid, which could result in higher taxes.

Meanwhile the secondary market for life insurance caught a good deal of attention in 2009 from U.S. legislatures, regulators and the news media.

The increased awareness stemmed in part from the considerable growth of the life settlement industry. Life settlement companies have paid policy owners more than US\$10 billion over the past 10 years, which was US\$6 billion to US\$7 billion more than the cash surrender value of their policies, according to an estimate by the Life Insurance Settlement Association.

Thus it is the simplicity of life settlements that makes it a very attractive investment in the current economic climate. It's a win-win situation. As already mentioned above we provide substantial equity to those U.S. policy owners wishing to sell their policy. We do this by utilising your investment monies in a low-risk, compliant and regulated industry. From this we generate attractive and relatively stable returns, not impacted by economic factors.

With the prospect of some businesses struggling across most sectors, it is important for everyone to understand who owes them money when it becomes due and payable. From our perspective I wanted to emphasise the counterparty risk associated with your investment. Consequently you'll see in an article elsewhere in this newsletter a break-up of the 70 highly rated insurance companies that have issued the life insurance policies we all now share in. Suffice to say that the Board are very happy with the comfort level provided by this diversification.

We'll have a lot more information to update you in the near future regarding the new Luxembourg-based fund we are establishing and some of the exciting changes we are introducing. In the meantime we are continuing to focus on delivering positive returns for our investors.

Benefits of Hedging



Stephanie Nolan

We have certainly seen some strong fluctuations in currencies in 2009 and our Ordinary Unit-holders have benefited from the decision to introduce a hedging component. The Fund's Ordinary Unit class is denominated in Australian dollars.

Stephanie Nolan, our Chief Financial Officer, confirmed "With our assets being held in US dollars the fluctuation in the Australian / United States currency rate would have had a marked impact on the worth of the underlying assets had we not introduced hedging at the start of the year".

Indeed this currency rate has fluctuated between A\$0.6247 and A\$0.9405 which represents a movement of a staggering 50.55% over the year. This was the most volatile year for the Australian dollar in the 23 years since it was floated.

"We certainly haven't seen fluctuations to that extent for many years, but we have the comfort of the hedge should it repeat again in the near future" Stephanie added.

The Ordinary Unit's performance for the calendar year (1/1/2009 to 31/12/2009) was 14.57%.



Credit Risk



Stephen Knott

The economic problems of the last 18 months has highlighted the importance of understanding credit risk, or more particularly for our fund the counter-party risk associated with the pool of policies we own. Obviously we rely on getting paid by the insurance companies at the appropriate time for the assets that we own.

The number of businesses and banks that are in financial trouble in the United States means that any deterioration in their financial position will have a flow-on effect to smaller businesses and thus the economy. Consequently diversification is very important as you don't want to be in the position of relying on one company or bank for your payments.

Director Stephen Knott confirmed that "The Board of the Life Settlements Wholesale Fund are pleased that from the outset we sought a wide diversification of issuing insurance companies as part of our policy purchase criteria". Another part of these criteria considers the rating of the company that has issued the policy being considered. "We look for policies that have been issued by an insurer with a suitable A.M. Best rating. AM Best is an organisation that provides ratings of the financial strength of insurance companies after analysing their balance sheet and operating performance" Stephen added.

Our portfolio of 547 policies has been issued by 70 different insurance companies. This diversification ensures that our exposure to any one issuing company or group is limited. Whilst some of these companies have experienced a small downgrade in their rating as a result of the global financial crisis, the majority were not impacted as the US insurance regulations require they hold funds in reserves to meet their known requirements.

The financial strength of these companies as at the end of December 2009 is shown to the right:-

AM Best Rating Category	Percentage Holding
Superior (A++ & A+)	62.00%
Excellent (A & A-)	34.36%
Good (B++ & B+)	3.64%
Fair (B & B-)	0.004%

"Consequently the Board are very comfortable with the risk profile within our portfolio and believe the diversification aspect has only strengthened our position" Stephen stated.

Q&A



Mark Brigden - Executive Manager
Australia and New Zealand

Mark Answers Your Questions.

- **Underlying assets** - does the fund buy and hold the actual policies (like we do) or are they involved in derivatives over non-existing, manufactured portfolio's which bring other risks to consider eg counterparty risk of relying on one institution for payment.
- **Valuation methodology** – Importantly, did the fund revalue their portfolio towards the end of 2008, following the release of the latest industry valuation tables (2008 VBT)? If not, they may have substantially overvalued the market valuation of their underlying assets, thus causing potential problems for your investment down the track.

Q The success of this fund and the asset class has meant more and more life settlement funds are actively seeking investment. So if I'm considering an investment in the asset class, what should I look for?

A There are a number of things to consider, including:-

- **Quality of people** - strong technical skills are required to negotiate through the regulatory, legal and tax minefields, thus it's always better to deal with proven performers.
- **Proven operations** – it is a detailed process to source policies, understand the terms of each policy, undertake the actuarial analysis, settle the transaction and then actively manage that portfolio. Look for Fund Managers that offer this expertise in-house to ensure effective, on-going management.
- **Transparent processes** – ensure they can provide you with an understanding of their pricing methodology and selection criteria. This should include details of the credit quality and good diversification of the issuing companies, spread of health impairments, ages and life expectancies.

Q Can you explain some benefits of life settlements?

A The key point is obviously that the non-correlated aspect can provide real diversification to your investment portfolio. But to summarise the main benefits of an investment with us I'd say:-

1. The underlying assets are unaffected by market and economic conditions.
2. You are not speculating on future value potential, as the face value that we eventually receive is known at the outset, plus you have a superior yield potential.
3. Relatively low risk to investment capital.
4. We utilise a stringent assessment selection process.
5. The comfort of the integrity of safekeeping of the policies.
6. Regular audits by an internationally recognised firm.
6. Experienced partners and transparent operations.
7. Increasing regulation has strengthened the industry.



Valuation Methodology

Traditionally the Life Settlements Wholesale Fund has used a proprietary model to value our policy assets. Then every six months, at the end of June and December, we would have an independent actuary value our portfolio using a probabilistic method, which is the most widely-used valuation methodology in the life settlement market. This often resulted in minor differences at valuation times, which were reported and explained in our public financial statements. The difference would fluctuate depending on individual policy characteristics and what stages in their cycle the policies were at (impacted by new policies coming in).

However in view of the global financial crisis and industry events in 2008, the Board decided that it was in our investors best interests to ensure that the Fund was valued in the most transparent way possible and as closely as possible reflected current market conditions.

Utilising the inputs of age, gender, and smoking and an appropriate mortality table, the Probabilistic Pricing Model uses the insured's life expectancy to determine a mortality curve for the insured. This model then calculates two economic curves:

- Cash inflow is the policy death benefit spread over the entire mortality curve in proportion to the insured's probability of not surviving each future year. It is possible for the mortality curve to extend past the policy maturity date and thus cause some probable death benefits to be theoretically lost. This does not occur in the Deterministic Pricing model.
- Cash outflow is the cost of the policy to maturity over the mortality curve in proportion to the insured's probability to surviving each future year.

These two economic curves are combined to create a "probable cash flow". This is then discounted to a net present value at the investor's expected rate of return to determine an economic value of the life insurance policy. The Probabilistic Pricing Model's portfolio theory also takes into account that a large portfolio will tend to approximate the blended mortality curves of all insured.

The Probabilistic Model takes into account the fact that some individuals will die prior to, and some after, the life expectancy dates of the insured. This is a better reflection of reality.

Since June 30, 2009 the Fund has used an independent actuary to value the Fund monthly using a Probabilistic Pricing Methodology and will continue this process going forward. The new Life Settlements International Fund will also adopt this method.

News from New Zealand

Investors Current Needs

Over the last few months Lyn has undertaken an extensive road trip and connected with existing and new advisers to get their feedback on what their investors are currently looking for in an investment. Three key areas kept coming up:

- Surety of capital
- Access to their money
- Strong returns

The last 2 years has seen some of the most turbulent times many investors have experienced during their investing periods. For most investors the market volatility is scary and the "game" of chasing returns has consequences for the risk reward pay off without the consideration for an investment time horizon. Losing capital or watching an investment take a dip is never comfortable for an investor, no matter under what circumstances it occurs. Asset allocation and diversification within a portfolio can be used as tools to realign the investor's requirements for capital stability, access and return.

Life Settlements show similar characteristics when we consider capital stability, access and return. By owning the beneficial right to the sum assured of a life policy the capital value of the asset is known, it is just the specific time that is unsure. The asset value is reflected over time in the unit price which grows by the aggregation of the increased value each month of each policy plus any maturities which may be collected.

As an open ended unitized fund, an investor can sell down a portion of their holding at any time, so they are able to generate funds when they require. Alternatively, where the Fund has net income to distribute, distributions will be paid to investors at least annually and unit holders can choose to receive or reinvest these distributions.

The strength of the investment is backed by the research into the financial strength of the US insurance companies issuing the life policies, and the highly regulated market maintained by legislation. Each policy is analysed before it is purchased and included in the Fund so the Funds' criteria for a continual strong return for investors is maintained.

For more information, or to arrange a presentation please contact Lyn Buckley - mobile: 0274 501 518.



Lyn Buckley



"The prospect of a life insurance company failing to pay a death benefit is less likely than the United States of America defaulting on a Treasury note payment. This association of zero Beta-risk with positive extra-risk-free return is at the basis of the revolution brought to capital asset pricing by life settlement portfolios. The premiere item for optimum portfolio selection has now become the life settlement product."

Tom Climo, former Professor of Accounting and Finance and a former Chief Economic Adviser to a major stock life insurance company.

"The credit quality of bonds, stocks and similar investments is influenced by economic factors, political factors and natural phenomena. The credit quality of a portfolio of life settlements is not influenced by these factors, but rather by the accuracy of mortality assumptions (assuming of course that the underlying credit quality of the insurance carrier is A or better). Therefore, a portfolio of life settlements serves to diversify the risk of the traditional portfolio."

Evolution of the Life Settlement Industry: A Provider's Reflection on Trends and Developments. Craig L. Seitel, 2008.

"Life expectancy is not a 'best guess' or likely date of death, but the sum of mathematical probabilities of survival to each possible age."

"As more policies are introduced to the portfolio, it becomes more stable."

Stuart Silverman and Daniel Theodore, principals and consulting actuaries with Milliman New York.

"The life settlement market has the growth, stability, regulatory oversight and acceptance both domestically and internationally to thrive. The market is increasingly well-regulated, transparent and positioned to provide value to investor and consumer alike."

"It is a safe prediction that by the end of 2012 the key elements of portfolio diversification for sophisticated investors will be equities, bonds, commodities, real estate and longevity".

Wharton Financial Centre – Life Settlements: Signposts to a Principal Asset Class. Sam Rosenfeld.

Interesting Quotes from Other Publications

"The life settlement market works because of arbitrage opportunities between the surrender value and the market investment value of a life insurance policy."

What are Life Settlements – History and Evolution? Insurance Studies Institute 2008.

"Many investors with a banking background will assume that money talks and that sellers will not distinguish one offer from another on the basis of anything other than price, but in a market with very limited standardisation, nothing could be further from the truth. Life settlements will undoubtedly migrate towards a standardised platform over time, but needing to placate regulators in 50 different states is a significant time barrier to that process. Soliciting and choosing good quality policies therefore depends on having the right relationships and on maintaining those relationships."

Life Settlements and Longevity Structures: Pricing and Risk Management. Aspinall, Chaplin and Venn 2009.

"We estimate that in 2008 approximately US\$12 billion worth of life insurance face values were settled. This was essentially unchanged from our estimated US\$12 billion in 2007. By year end 2008 approximately US\$31 billion of US life settlements were in force."

Investors and their capital will return to life settlements as they regain confidence in the market and concerns about their financial stability abate."

Conning Research & Consulting – Life Settlements; A Buyers' Market for Now, 2009



Free Market and Innovation

A life insurance policy is one of the most valuable assets many Americans will ever own. Traditionally, there was only one potential purchaser for a life insurance policy: the issuing insurance company. Under that circumstance, most policy owners found that the only possible "offer" was the policy's cash surrender value set by the insurance company.

Traditionally, policy owners received little, if any, economic value from policies they no longer wanted, needed or could afford. In fact, even today, many policies simply lapse. The value of lapsed policies is enormous. An estimated 90% of all policies issued lapse before paying a claim.

The secondary market for life insurance gives policies liquidity similar to other assets. This liquidity adds to the value of all life insurance for consumers.

Now, market forces ensure that a large percentage of life policies held by seniors are worth significantly more than their cash surrender value. Policy owners can receive, on average, 3 to 4 times the amount of the policy's cash surrender value.

In the last 4 years, life settlements have provided over 8 billion dollars in additional value to seniors in America. Today, the industry is highly regulated, creates additional tax revenue to the US treasury, and employs a sophisticated workforce of thousands of people.

(Extract from www.thevoiceoftheindustry.com)

How to invest in the Fund

Direct investors can buy units in the **Life Settlements Wholesale Fund** by completing an application form which is available in the Product Disclosure Statement (PDS).

The PDS can be downloaded from our website: www.lifeselementsfund.com and/or contact the Fund on 1300 88 13 73 or +61 7 5557 4700 to receive a printed copy of the PDS.

Units in the Fund are also available via the following investment platforms' investor-directed portfolio services (wrap account or master trust) with the minimum investment or additional investment determined by that service:

Australia

- Macquarie Investment Manager
- BT Wrap
- Symmetry (Avanteos)
- Access121 (Avanteos)
- Netwealth
- Wealthsure

New Zealand

- Discovery
- Aegis
- BNZ Custodial Services
- ABN AMRO
- One Answer

Worldwide

- Royal London 360°

Superannuation platform

- Macquarie Super & Pension Manager

Bloomberg

LIFSETW AU - Ordinary Units

LIFSETA AU - AP Units

LIFSETE AU - EA Units

LIFSETS AU - SA Units

Morningstar

LFS0001AU

IDENTIFICATION CODES

APIR CODE	ISIN	PRODUCT NAME
LFS0001AU	AU60LFS00013	Life Settlements Wholesale Fund
LFS0004AU	AU60LFS00047	Life Settlements Wholesale Fund - SA Units (South America)
LFS0003AU	AU60LFS00039	Life Settlements Wholesale Fund - EA Units (Europe-Africa)
LFS0002AU	AU60LFS00021	Life Settlements Wholesale Fund - AP Units (Asia-Pacific)

Life Settlements Funds Limited

Postal address: PO Box 5799, Gold Coast Mail Centre, Qld 9726

Phone: 1300 88 13 73 Facsimile: 1300 88 73 93 (within Australia) International phone: +61 7 5557 4700 International facsimile: +61 7 5591 4375

Email: admin@lifeselementsfund.com Website: www.lifeselementsfund.com

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