

Monday 8th December 2008

PATF temporarily revalued to protect investor equity and future interests

This update contains information about the recent performance of the Protected Asset TEP Fund and the necessary decision taken by the Fund's Directors to value assets on a Net Realisable Value ('NRV') basis to protect investor equity and future interests.

Liquidity in the traded endowment market has diminished since July 2008 as the impact of the slowdown in global money market, bond, property and equity markets has taken effect. Despite the fact that the Fund's performance has remained positive during the worst of this period, redemptions from the Fund have been steadily increasing since February 2008.

The Fund is now faced with the prospect of realising additional assets to meet these increased redemptions. The Board believe that it is in the interest of all investors to:

"Ensure that the valuation of the Fund should reflect the realisation value of these assets so as not to disadvantage shareholders who wish to maintain their holdings in the Fund."

It is intended to continue using this valuation method until the strain posed by high levels of redemptions is alleviated.

The Board, acting on the advice of its Advisors, believe that this action is both necessary and fair to all shareholders.

"It protects the future performance of the Fund, whilst also ensuring that those who leave the Fund receive an equitable value achievable under current market conditions."

The Fund was launched in March 2001 in a positive and dynamic investment climate which is very different to that which we are experiencing today. The past year has witnessed dramatic events and massive upheaval in the global economy, which have naturally had an impact on market values and investment strategies.

The returns on endowment policies are in part dependent on the returns made by the life companies' life funds. In the short-term, returns may be smoothed during good times to build up reserves, which can then be released in difficult times. Life companies have used their 'free assets' and 'inherited estates' to support annual bonuses over the past few years, however, this has not prevented cuts in terminal bonuses. The level of these bonuses play a fundamental role in driving the performance of PATF.

To help you better understand what is happening, please see below a Question and Answer section which we hope will address most of the questions you may have.

Questions and Answers

What are the changes in the Traded Endowment Market that have affected the Fund?

In the majority of cases, maturity and surrender values are lower now than they were 12 months ago. This has been reflected in the Traded Endowment Market where the price of policies has fallen. Typically, traded endowment funds use market makers to buy and sell policies in this market. When the Fund was launched, demand for policies exceeded supply. More recently this situation has reversed and there is now an excess supply of policies being offered for sale in the market, which has the effect of reducing liquidity, as well as depressing prices.

What is the change in Valuation Method to reflect Net Realisable Value?

Since the beginning of 2008 the Fund has experienced significant redemptions and moved into a net outflow of cash in April 2008. With very poor liquidity in the TEP market, the Fund has become a forced seller of policies with surrender the only available option to quickly meet these redemptions. The change in valuation basis for the Fund will lead to a fall in the price of the policies held by the Fund of approximately 35%. Failure to carry out this action would have meant that investors leaving the Fund would have been subsidised by those remaining.

Why did the change in Valuation Method result in a drop in the share price?

The Fund sources policies via market makers who specialise in Traded Endowment Policies (TEPs). Typically this market trades in a range between 10 and 20% above surrender value. For buyers of TEPs who intend to maintain their holding until maturity, the price paid above surrender value still represents a discount to the inherent value in the policy.

PATF was designed to buy TEPs and hold them until maturity when the guarantees built into the policy in the form of reversionary bonuses and terminal bonuses, together with capital appreciation generated by the life offices managing the assets of a policy, would generate a positive return. Historically this strategy has returned between 6 and 12% per annum for investors.

"The Fund has become a forced seller of policies."

It is no longer equitable to continue to value the Fund in line with values in the secondary market as there is insufficient liquidity in this market to accommodate PATF shareholder redemptions and as such the Fund must be valued to take account of the surrender value of these policies.

What happened to bonus declarations in 2008?

Throughout the course of 2008 the majority of life companies announced their bonuses reflecting the year's poor returns on equities, fixed interest and property investments. The pace of announcements has accelerated in recent months with Standard Life making two interim declarations in the last 12 weeks; Norwich Union declaring an interim bonus cut for the first time since the technology bubble burst in 2001; similarly General Accident, Guardian and Legal and General have also made two interim bonus declarations since the start of 2008.

Bonus rates are a factor in the pricing of TEPs, as bonus rates have been falling, so too has the valuation applied to the policies held by the Fund. This has naturally resulted in the NAV of the Fund falling.

What effect has poor liquidity had on redemptions?

An easing in the level of redemptions during the first half of 2008 gave some hope that the Fund would be able to trade normally through to the time when large numbers of policies held in the portfolio would mature over the next three years. However, an increase in the level of redemptions was experienced throughout the summer whereby cash flow modelling confirms that assets in excess of the available liquidity in the TEP market must be realised to allow the Fund to continue. This means the Fund will have to surrender policies in order to increase liquidity to meet further redemption requests.

How is the redemption process managed?

The Scheme Particulars of the Fund allow for the application of a redemption gate in

situations where more than 5% of the net issued shares are being redeemed. The Directors have applied these measures to all share classes of the Fund.

This does not mean that shareholders will only receive 5% of their redemption proceeds. Redemptions are processed in batches grouped by month in the order in which they are received; each batch is cleared in full before redemptions for the next batch are paid out. To date redeeming shareholders have received their proceeds over the course of two to three months.

Typically, redemption proceeds are paid within 10 business days of the NAV being published, however this may increase owing to the need to surrender policies back to the various life offices.

The price at which shares are redeemed will be determined on each monthly valuation day on which shares are being redeemed; so for example, if a redemption is being processed over three months then the NAV applicable on each dealing point may be different.

During this period it will no longer be possible to request a redemption for a specific monetary value. Instead, all redemptions must be requested as a number of shares in accordance with the Scheme Particulars. This will prevent delays to processing redemption requests whereby a change to the NAV may result in a shareholder having insufficient shares to realise the cash amount requested, preventing that redemption request from being processed.

It is intended to continue using this method until the strain posed by high levels of redemptions is alleviated.

Can redemption requests be cancelled?

In light of these developments the Board have agreed that:

"Investors who no longer wish to redeem from the Fund at these lower values can cancel their redemption request."

This offer is however time limited and will remain in place until the 23rd December 2008.

What is the long-term outlook for the Fund?

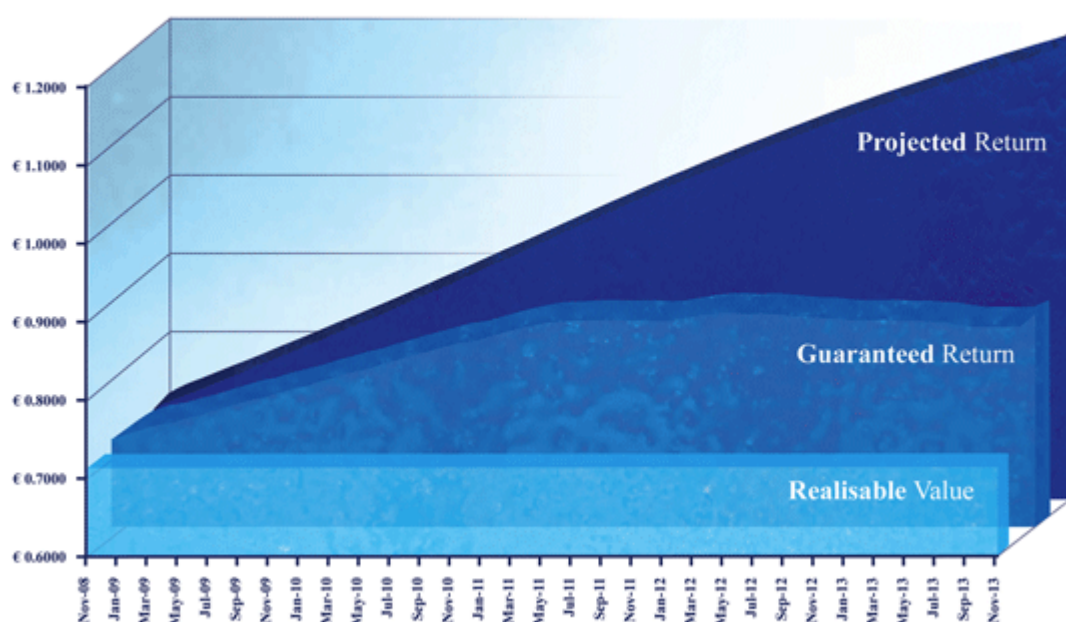
PATF holds policies which do not mature until 2020, given that the Fund buys policies and holds them to maturity; this should serve to witness the faith which the Directors have in the longevity of the Fund.

"There is no intention to close the Fund."

The Fund continues to have exposure in the region of 90% of its holdings, to the top-rated life offices with the strongest financial backing, expressed through strong balance sheets and endorsed by independent ratings agencies.

Once these changes are made, we can see that annual growth, as illustrated in the graph below, should be in the range of 4 and 12% per annum.

PATF Forecast Share Price Returns



It should be noted that the guarantees highlighted above are only available once a policy held by the Fund matures; this is typical within all products which offer investors some form of protection.

Policies held by the Fund are valued based on the market value in the secondary market. Typically these values are below the Target Maturity Value or basic sum assured established when a policy is taken out. Life offices have an excellent track record of paying out the sum assured on maturity and in a number of cases actually exceeding this amount; calculations illustrate that a continuation of this should deliver an extra 2% per annum above the projected return to investors in the Fund.

Will the 'orphan assets' or 'inherited estates' held by life offices still be disbursed?

In short, the answer is "yes". Disbursements from the 'orphan assets' or 'inherited estates' held by life offices will provide further relief for investors in the Fund. It is known that Standard Life are applying estate assets to maturities to off-set possible shortfalls and bring maturities in-line with the Target Maturity Value which is encouraging. At the time of writing, Prudential are undecided as to how best to make disbursements from estate assets. Aviva have however announced that special bonuses will be paid to Commercial Union and General Accident policyholders; this process began in December 2008 and will continue until January 2010. Additional announcements are expected from Aviva in Spring 2009 which are expected to be in the range of £400 and £1,000 per qualifying policy.

"PATF currently holds approx £50m of policies which will directly benefit from inherited estates."

Overall, whilst we acknowledge that the coming months will continue to be testing, the long-term fundamentals for the Fund remain intact and this temporary revaluation should not affect investors who wish to maintain their holdings. We believe this represents an excellent buying opportunity for new investors, a fact we will be highlighting to the professional advisor community over the coming weeks.

If you are in any doubt about what action you should take, you are recommended to seek your own personal financial advice immediately from your stockbroker, bank manager, solicitor, accountant or independent financial adviser.



[Download the Questions and Answers pdf](#)



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The value of investments, and the income from them, can go down as well as up and investors may not recover the amount of their original investment. Past performance is not necessarily a guide to future performance. Full details of the Protected Asset TEP Fund plc, which is an Experienced Investor Fund, can be found in its Scheme Particulars which are available upon request.

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