



KUDU FUND

EMERGING EUROPE, MIDDLE EAST, AFRICA

MONTHLY REPORT DECEMBER 07

KUDU

Monthly Report

The Kudu fund rose 0.8% in December, compared to a fall of -1.3% by the Morgan Stanley Pan European Index, and a rise of 2.2% by the Morgan Stanley Europe Middle East and Africa Index. The two indices taken together give a reasonable picture of the markets in which the Kudu fund operates.

The Kudu fund rose by 7.3% in 2007, in extremely volatile and difficult markets. Many important sectors, such as banking, real estate and retail, suffered severe bear markets in 2007, with large benchmark companies with limited debt, such as Woolworths in South Africa, falling 30-40% in value.

January has seen further extreme turmoil in world markets. By late month, most markets, from Hong Kong to Russia, have fallen by more than 10%.

It is clear that something is badly wrong with global markets. US 10 year government bonds, the global benchmark, now yield just over 3%. The Greenspan, or Fed, model, named after the recently retired Chairman of the Federal Reserve, compares this yield to the inverse of the price/earnings ratio of equities, the earnings yield, giving a simple indicator of whether stocks are under or over-valued.

Conventional wisdom would imply that equities need to generate an adequate return above bonds to entice investors: an equity risk premium. However, over the long run, including periods of strong and weak economic growth, equities have historically generated strong earnings growth, whereas bond yields are fixed coupons, with no possibility of growth. In the real world, any theoretical risk premium is balanced by the likelihood of earnings growth.

Extending the model to emerging markets raises the question of a further risk premium for the higher perceived risk of investing in newer markets. Not surprisingly, emerging markets have historically delivered, and will most likely continue to deliver very strong earnings growth. Since 2000, the EMEA region has delivered 300% of the GDP growth of the US and western Europe, in both strong and weak conditions. The superiority of younger more dynamic emerging market economies, effectively neutralises the higher theoretical equity risk premium.

EMEA stocks currently trade on an earnings multiple of 10-12 times, a yield of 8-10%, based on cautious estimates of 2008 earnings, a discount of 60% to the US 10 year bond yield of 3.5%. Historically EMEA stocks have always traded at a discount to the Fed Model, but the current valuation gap is substantial.

Lewis Group, the sixty-five year old furniture company in South Africa, trades on around 5 times earnings declared 08

earnings, an 80% discount to fair value. South African interest rates will likely fall sharply in 2008 giving further confidence to earnings forecasts. Lewis has no debt. Gazprom, the 60 billion dollar Russian gas giant, which controls the central heating and power needs in most of western Europe sells at 9 times 08 earnings yield, a 70% discount to fair value.

Something is obviously seriously troubling global investors to pass on such huge potential gains. Confidence, that crucial ingredient to stock markets, is shot to pieces by the sub-prime and credit crisis of 2007. With US inflation at around 2.2%, and global inflation well above 3%, investors are keen to own an asset – 10 year US bonds, which deliver either negligible inflation adjusted returns, if you live in America, or a guaranteed loss-making proposition if you live abroad. In Qatar, with its double digit inflation, US 10 year bonds offer a substantial annualised loss. Amazingly Gulf states continue to buy US debt (not for much longer perhaps).

The investment conundrum, of shares trading at huge discounts to fair and probable value, is a reflection of investors' collective irrational desire to avoid loss in the very short term, even when clearly offered the rational alternative of making large gains over the long term. The dominating role of thousands of hedge funds collectively trying to offer investors no short term downside risk, but 100% of upside market moves, has clearly exacerbated an already irrational tendency.

John Maynard Keynes was the first major economist to draw attention to the huge role that psychological and behavioural factors play in economics and markets. More recently the school of behavioural finance, with its well known proponent Robert Schiller of Yale, have focused academic study on the dominating role of human psychology in economic decision-making.

Nervous investors cite the impact of a spreading global recession, but older investors will remember that the US economy and stock market absorbed and rebounded from the enormous Savings and Loan crisis of the 1980s and 1990s, an earlier version of sub-prime, and the 1998 rout caused by Long Term Capital and the Asian and Russian crises. If history is any guide, world markets and economies have a good record of weathering apparently catastrophic problems.

The Kudu investment team has an excellent record of navigating difficult and volatile markets, during 9/11, and then again during the sustained bear market in 2002. The fund uses a wide variety of techniques, from short stock positions, short index baskets and futures to protect core long positions in the fund.

Periods of investor panic offer excellent opportunities for gain, and the fund stands

ready to profit from extreme market conditions.

The current market volatility should not cloud or distract attention away from the historic opportunities currently offered by the markets of EMEA. Indeed, whatever the extent to which EMEA is correlated, or de-coupled from western markets, many EMEA equity markets have already sold off sharply in anticipation of slower global growth and lower risk appetite, lowering still further company valuations.

The major countries of the EMEA region, are for the first time in modern history all pursuing market-friendly pro-business economic policies. Following the social misery caused by socialistic and planned economies, politicians, however undemocratic, have realized that their continuance in power is best served by western consensus economic thinking, even if it is tinkered with to suit local conditions.

EMEA countries control 82% of the world's proven oil and gas reserves, and over 95% of available platinum. Super-cities like Cairo with 18 million people, Moscow (18 million) and Istanbul (15 million) are driving economic and social change.

In a world of dwindling Hydrocarbon reserves, Carbon is power, and the wealth and power of energy-rich nations is growing fast. Countries like Kazakhstan and Russia are forcing western oil companies to take smaller returns from new oil and gas fields, and re-negotiating old profit sharing agreements. Russia is a creditor to the world, receiving billions of dollars of net income. Kazakhstan, whose markets were hit hard by the 2007 credit crisis, has no sovereign debt. Unlike western countries, it has no need of government borrowing.

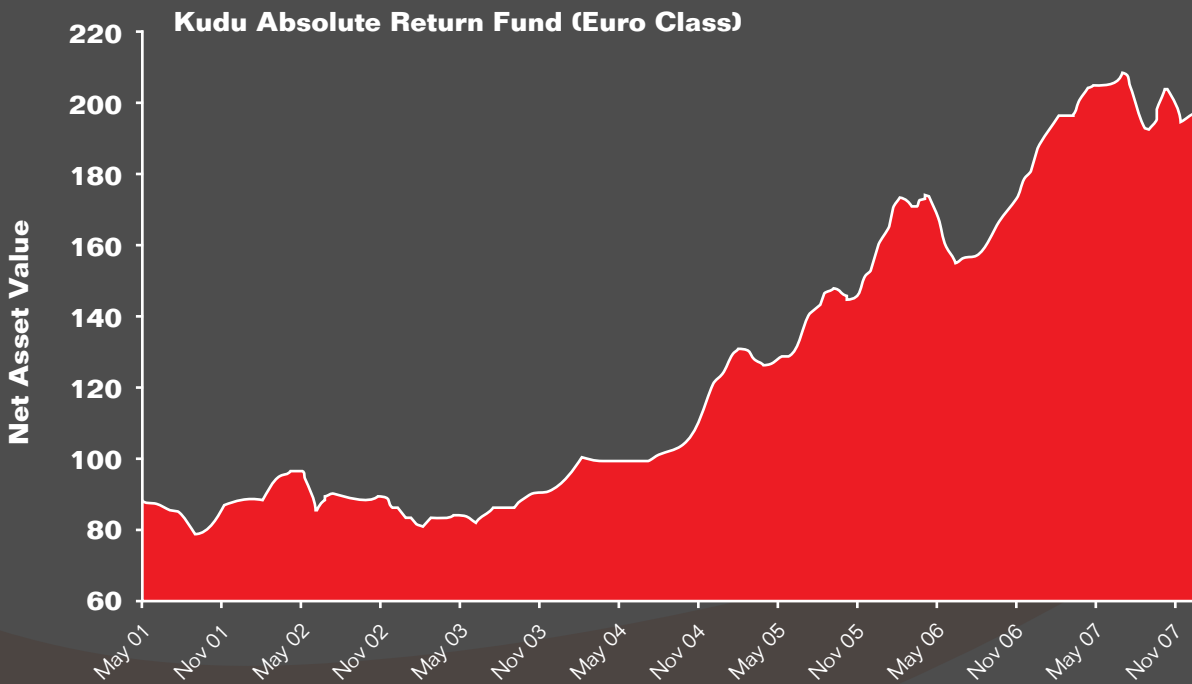
Travellers to Venice often remark upon how such a glorious, sophisticated and wealthy state could sink into total economic decline and oblivion. Venice was at one time the New York or London of the world economy, but changes in trade and a reluctance to change led to a slow decline and fall. It is not hard to imagine more Venices in western Europe as money, power and trade shift to the south and east. The burning rubbish dumps of Naples are a stark symbol of decline, as southern Italy slips into crime-ruled chaos, whilst China, Russia, Ukraine, Qatar, Georgia, Oman and tens of other countries push ahead.

The Kudu fund is well placed to profit from these rapidly changing currents of history, and to find opportunities for profit in new and exciting markets.

■ **George Case**
 ■ **Jon Bond**
 ■ **Malcolm Levy**

NAV per redeemable share: Class A: £96.60 \$96.51 Class B: €197.46 £207.92 \$207.14

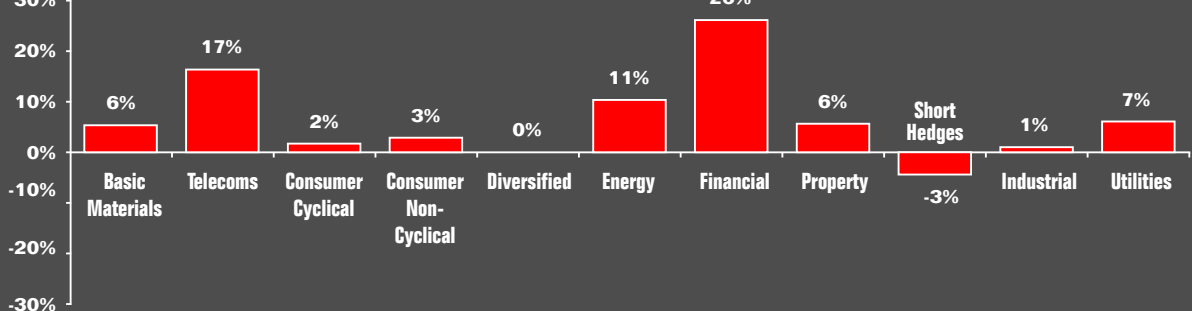
Performance	December	YTD	Rolling 12 months	Since Launch
Class A:	0.83%	-3.49%	N/A	-3.49%
Class B:	0.82%	7.30%	7.30%	124%



Geographic Allocation Exposure as % of Fund NAV

Region	Long	Short	Net	Beta Adjusted Net	Performance Attribution
Europe	5.7	0.0	5.7	3.2	0.24
Greece	2.4	-2.1	0.3	0.2	-0.64
Israel	0.0	0.0	0.0	0.0	0.00
Russia	40.9	-5.3	35.6	19.9	1.31
Turkey	3.7	0.0	3.7	2.1	-0.15
Africa	7.9	0.0	7.9	4.4	-0.64
Middle East	18.7	0.0	18.7	10.5	1.83
Other	13.3	-9.4	3.9	2.1	-1.13
Total	92.6	-16.8	75.8	42.4	0.82

Net Sector Allocation



TOP 5 LONG POSITIONS

	%
MOBILE TELESYSTEMS	5.55%
GAZPROM	4.34%
ALDAR PROPERTIES	3.53%
COMMERCIAL BANK OF QATAR	3.31%
POLYUS GOLD	3.15%

TOP 5 CONTRIBUTORS MTD

	ATTRIBUTION %
ALDAR PROPERTIES	0.83%
MOBILE TELESYSTEMS	0.65%
NOVATEK	0.44%
ISLAMIC ARAB INSURANCE	0.42%
GAZPROM	0.42%

TOP 5 CONTRIBUTORS YTD

	ATTRIBUTION %
ALDAR PROPERTIES	2.44%
AFRICA ISRAEL	2.43%
EVRAZ	2.42%
MOBILE TELESYSTEMS	2.39%
MECHEL	1.69%

FUND INFORMATION

CLASS A

ISIN

€ BMG532541270

£ BMG532541197

\$ BMG532541015

SEDOL

£ B1W7LS0

\$ B1W7LR9

BLOOMBERG

£ CLACTAS BH

\$ CLACTAD BH

US DELAWARE FEEDER

\$ US5011831071

INVESTMENT FOCUS:

OPAP – GREECE

Opap is the lottery and sport betting monopoly in Greece, with the exclusive right and concession to operate such games until 2020. The defensive, cash-generative nature of the business model is coupled with strong growth in customers and the uptake of betting and lottery games. On our estimates, the free-cash flow yield is 9% in 2008, 10% in 2009, and rising. The apparent threat of deregulation has substantially reduced following the exclusion of gambling activities from the EU Directive on Services in the Internal Market. Further, the government ownership of 34% of OPAP, and their previous defence of OPAP's position, give further comfort regarding the monopoly. Upside to our estimates arise from the continual and proven success of new games, as well as the margin improvement arising from internalising the management of these games. This enhanced operational leverage has not been demonstrated to the market. Gambling has proved to be a very resilient industry in times of economic uncertainty.

	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sept	Oct	Nov	Dec	YTD
2001						-1.0	-1.3	-3.0	-5.4	2.0	7.4	2.4	0.6
2002	0.6	-0.5	5.3	2.9	0.0	-10.5	4.8	-0.5	-1.5	0.0	1.4	-4.0	-3.5
2003	-2.9	-2.3	2.6	-0.3	1.5	-3.0	3.9	1.7	0.3	3.1	1.2	1.1	6.9
2004	3.9	4.7	-0.1	0.1	-0.1	0.1	-0.2	1.4	1.4	3.5	5.1	8.6	31.8
2005	4.6	4.1	-2.9	-1.0	1.5	1.8	7.1	2.6	3.2	-2.4	1.3	6.3	29.1
2006	6.0	5.0	-1.4	1.5	-5.3	-5.5	0.8	0.8	3.3	4.5	2.6	5.0	17.7
2007	4.6	2.0	0.2	3.7	0.5	0.3	1.5	-6.6	-0.5	5.4	-4.2	0.8	7.3

Total Return in €
Numbers net of fees (€class)

Domicile: Bermuda and Delaware, USA
 Listing: Irish Stock Exchange
 Assets: \$195mln
 Start Date: Jul-01
 Liquidity: Quarterly
 Lock up: 1 year soft lock up (3% redemption fee)
 Minimum: Class A £/€/ \$100,000
 Performance: 20% with HWM
 Management Fee: 2%
 Administrator: Citi hedge fund services
 Nicola O'Neil +353 1436 7292

Auditors: Ernst and Young
 Management Company: Kudu Emerging Markets Limited
 Subscriptions: Up to last business day of every month

Kudu Emerging Markets Limited is the London based investment advisor to The Kudu Fund, an emerging market absolute return fund. The primary objective of the fund is to achieve long term capital growth by investing in poorly understood markets with high levels of miss-pricing.

The Kudu Fund takes a fundamental approach to investing and looks to capitalise on valuation discrepancies and developing themes across the regions of Africa, the Middle East, southern and eastern Europe as well as western companies with emerging market exposure.

The Kudu Fund is invested in equities, both long and short, and generally invests with a time horizon of 3-18 months.

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