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# ATTRIBUTES OF WATER INFRASTRUCTURE INVESTING



**Kinetics Mutual Funds, Inc.**

**May 2009**

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# Global Water Issues & Investment Opportunities



# Water Investment Opportunity – The World’s Third Largest Industry

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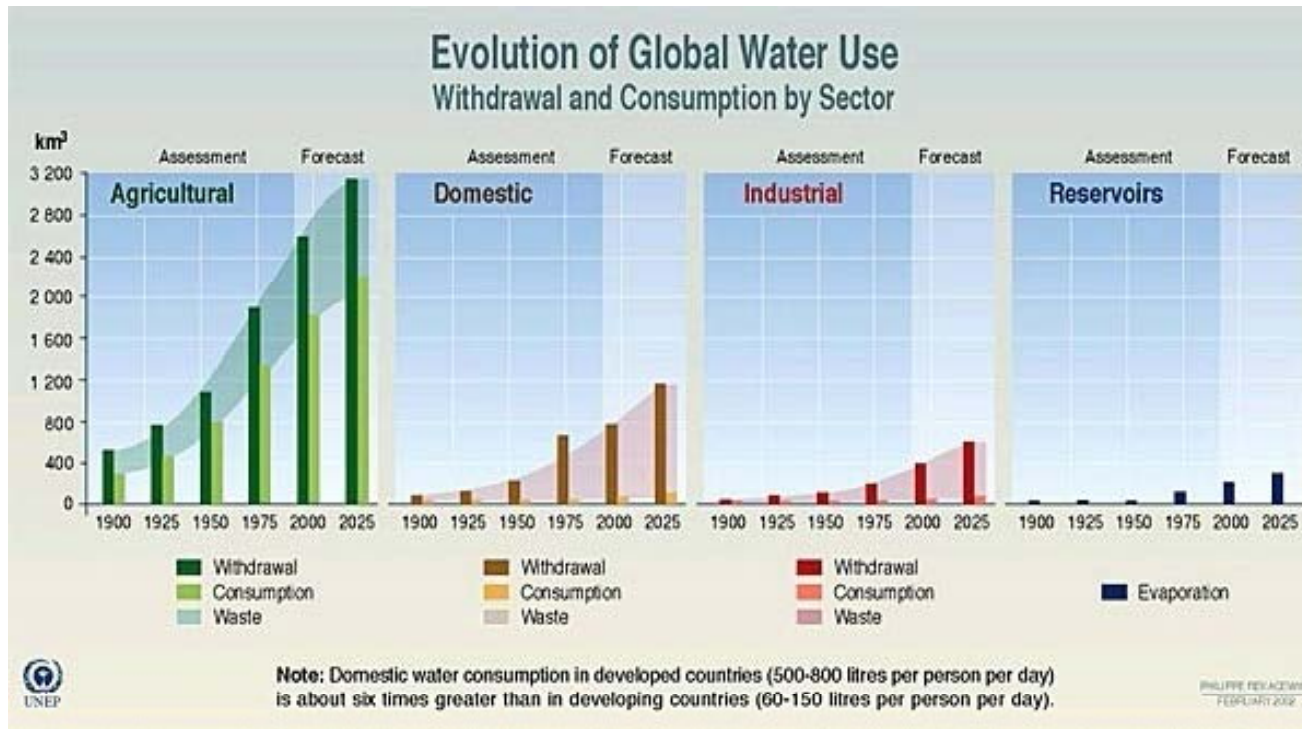
The Global Water Industry provides one of the largest and under-invested areas for investment.

- The Water industry is a \$500+ billion global market exceeded only by oil & electricity
- One of the most critical inputs to global economy; essential for all industries to operate
- The Water industry is comprised of 9 sub sectors:

Water Utilities  
Chemicals  
Waste Water Utilities  
Contract Operations  
Conveyance  
Equipment  
Maintenance Services  
Instruments & Testing  
Engineering & Consulting

# Global Water Use

Agriculture accounts for 75% of total global water consumption (crop irrigation), while Industrial use accounts for 20%.



Source: Igor A. Shiklomanov, State Hydrological Institute (SHI, St. Petersburg) and United Nations Educational, Scientific and Cultural Organisation (UNESCO, Paris), 1999.

# Water Investment Opportunities

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Macro and demographic trends will lead to multi-decade investments in the water space.

In our view:

- Accelerating spending due to population increases, industrialization, regulatory oversight, etc.
- Revenue growth 6-8% in developed countries and 15%+ in emerging countries
- Certain sub-sectors such as desalination, trench less pipe replacement and water technology could exceed industry growth rates
- Non-cyclical spending typically leads to strong, predictable revenue growth regardless of market conditions
- Opportunity for global exposure and diversification
- Low correlation with traditional investments
- Ever increasing global supply/demand imbalances increase the likelihood of sustainable returns
- Macro-risks are often misjudged by the public market, creating trading opportunities while macro-economic factors have various impacts on the water sub sectors

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# Industry Composition & Revenue Characteristics



# Industry Components

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Water is the world's third largest industry, exceeded only by oil and electricity.<sup>1</sup>

Water Stock Universe	Universe of 500+ Publicly-traded Global Companies Market Capitalization of \$1 trillion+
2007 Revenue	\$500+ billion annual revenue worldwide \$100+ billion annual revenue in US
Expected Future Capital Expenditures	\$500 billion estimated in developed markets annually by 2012 \$1-\$1.5 trillion in emerging and developing markets annually by 2012 <sup>2</sup>
Public Market Capacity	Quantity of publicly-traded companies increasing Companies with limited float provide opportunity as they are under followed Median Market Capitalization of \$850+ million

Source:

1. John Maxwell III Parker Global Strategies LLC

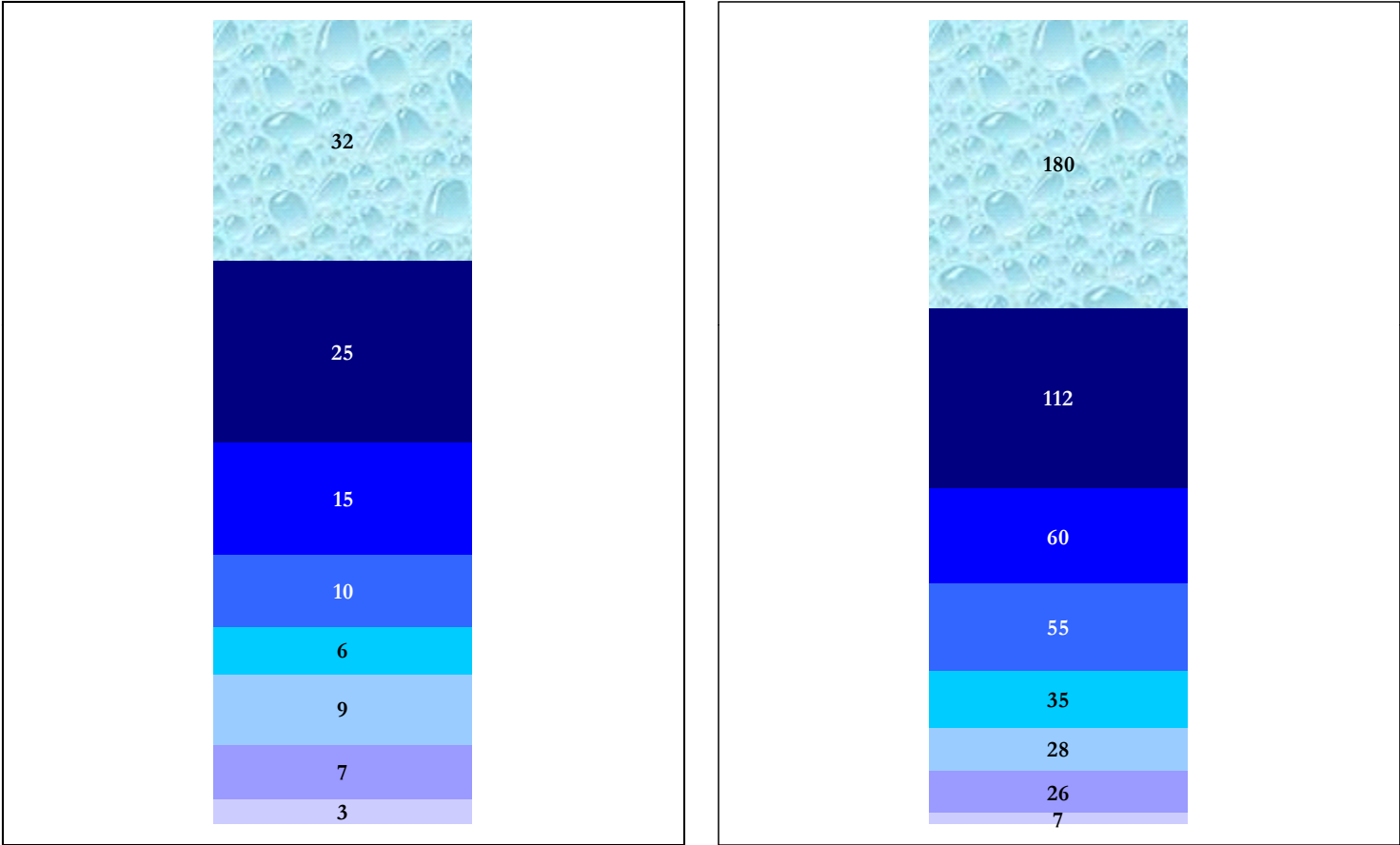
2. Associated Press Business News 5/31/06

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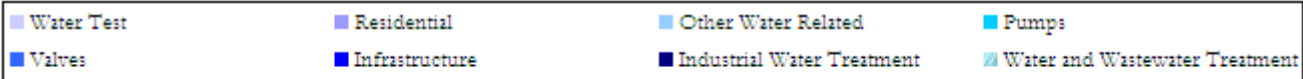
# Investment Opportunity - The United States & Global Water Market

US: \$107 Billion

Global: \$503 Billion



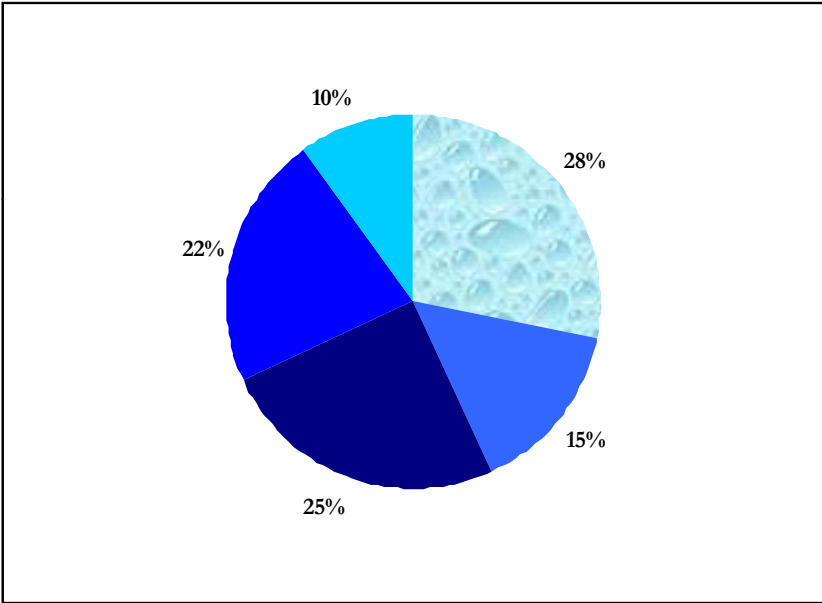
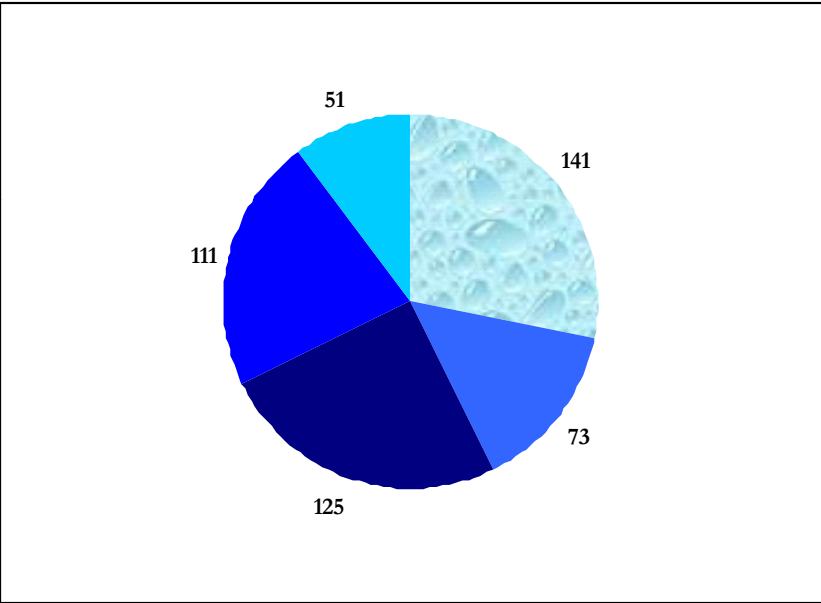
Source: Goldman Sachs



# Investment Opportunity - Global Water Public Equity Market

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## Public Water Companies Worldwide



■ USA ■ China & India ■ Asia / Pacific Rim ■ Europe ■ ROW

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# Water Investing Opportunities

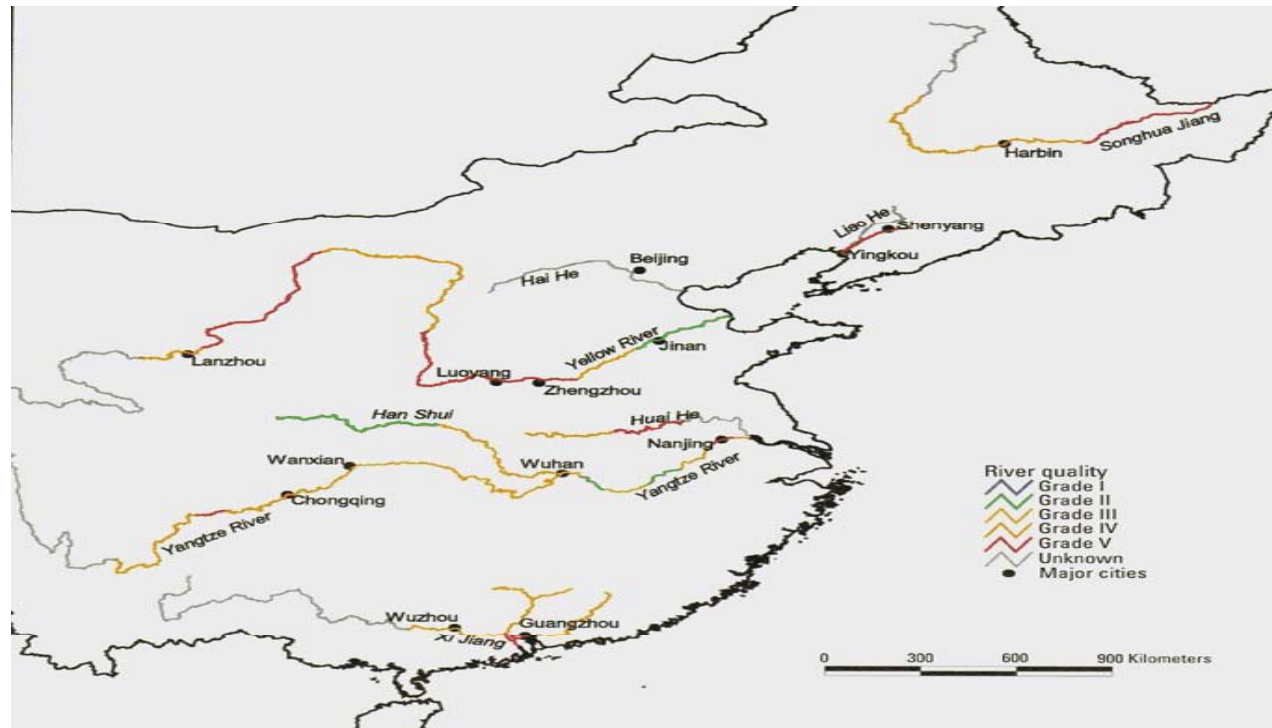




# A Snapshot Of The China Water Landscape

One billion Chinese presently do not have access to clean water...

- Estimates put environmental damage at 8% to 13% of China's national income each year
- China uses 7x to 15x more water per unit of GDP than the West

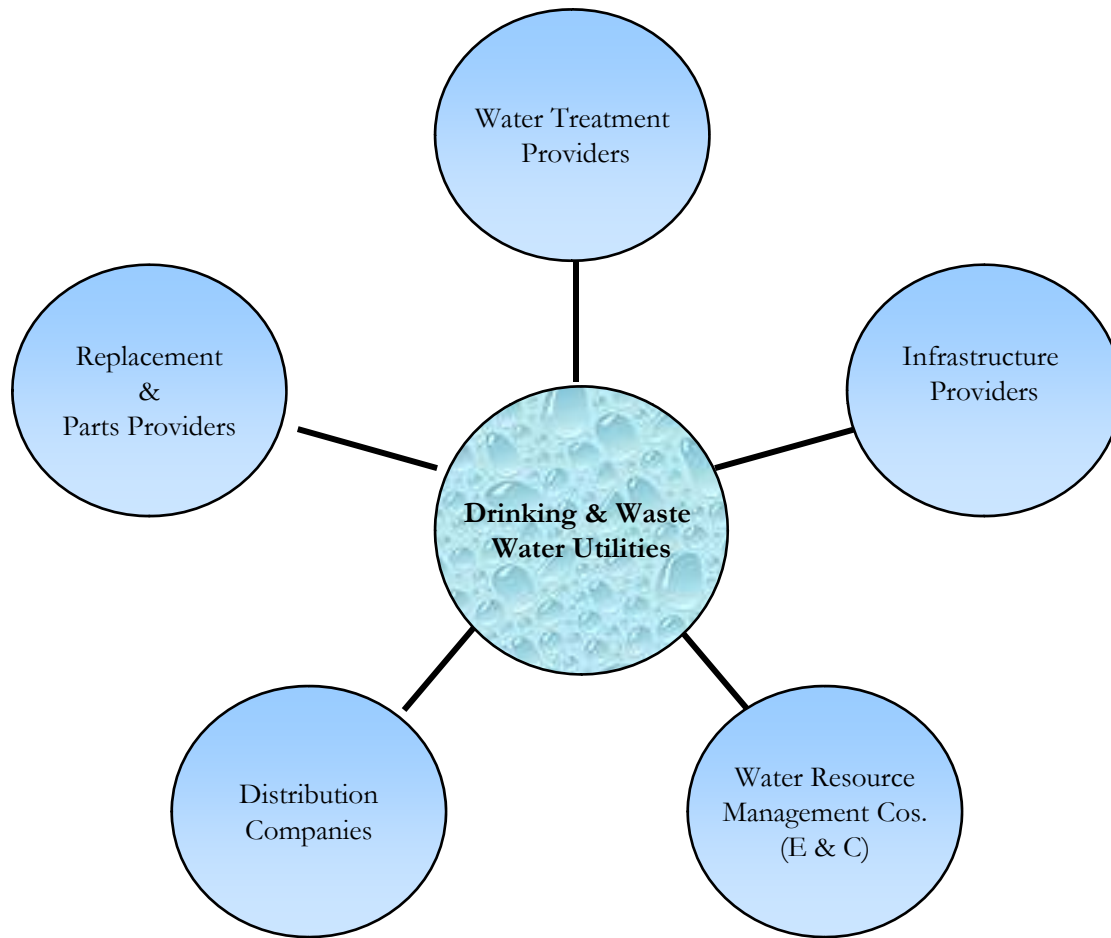


- One ton of water producing only \$2-3 of GDP, compared with the U.S., where one ton nets approximately \$28-\$30 worth of GDP
- China has committed \$125 billion to creating infrastructure over the next 5 years

Source: Parker Global, UN, World Bank

# Drinking & Wastewater Utilities As The “Gatekeepers” Of Spending

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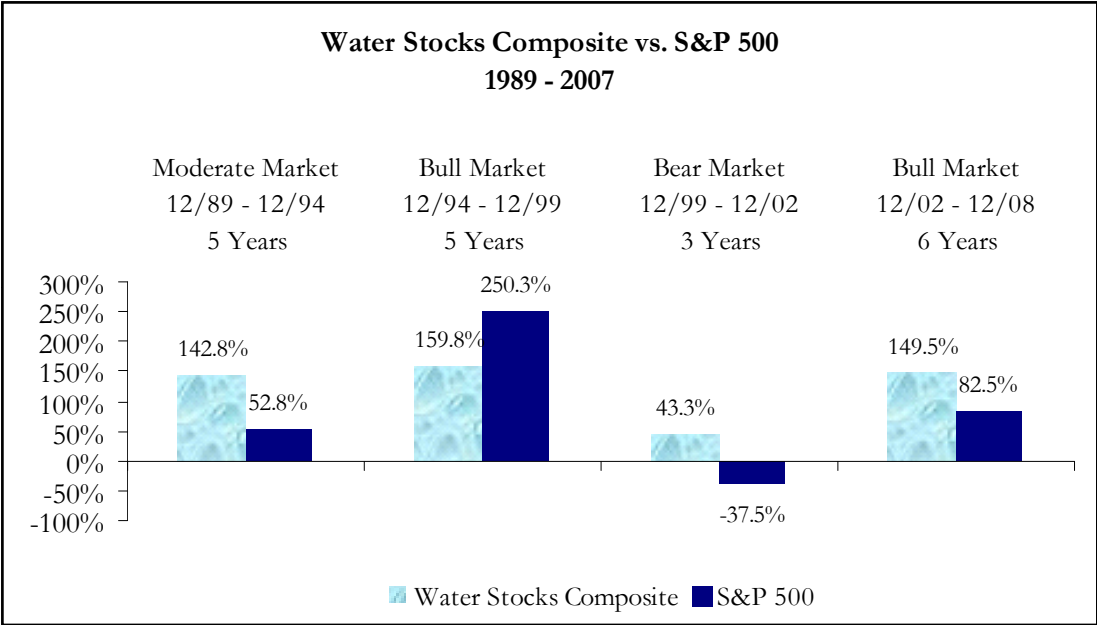


Water Utilities spend on capital expenditures regardless of the business cycle. This spending creates a “tail wind” for companies with exposure to the spending.

In the U.S. alone there are over 50,000 water utilities. The Environmental Protection Agency and Congressional Budget Office released separate reports outlining REQUIRED spending for U.S. water and waste water maintenance which ranged from \$550 billion to \$1 trillion by 2019.

# Water Industry - Historically Strong Returns

Water stocks have demonstrated above-average returns in various market conditions.



\*The Composite of U.S. Water Stocks represents a basket of 6 publicly-traded water utilities and 12 equipment manufacturers that had at least 20 years of business experience in the water industry. The six water utilities represent the six companies with 20 year operating history and does not include any take over or bankrupt entities. The list of securities that comprise this basket are available upon request. A direct investment in the water composite is not possible

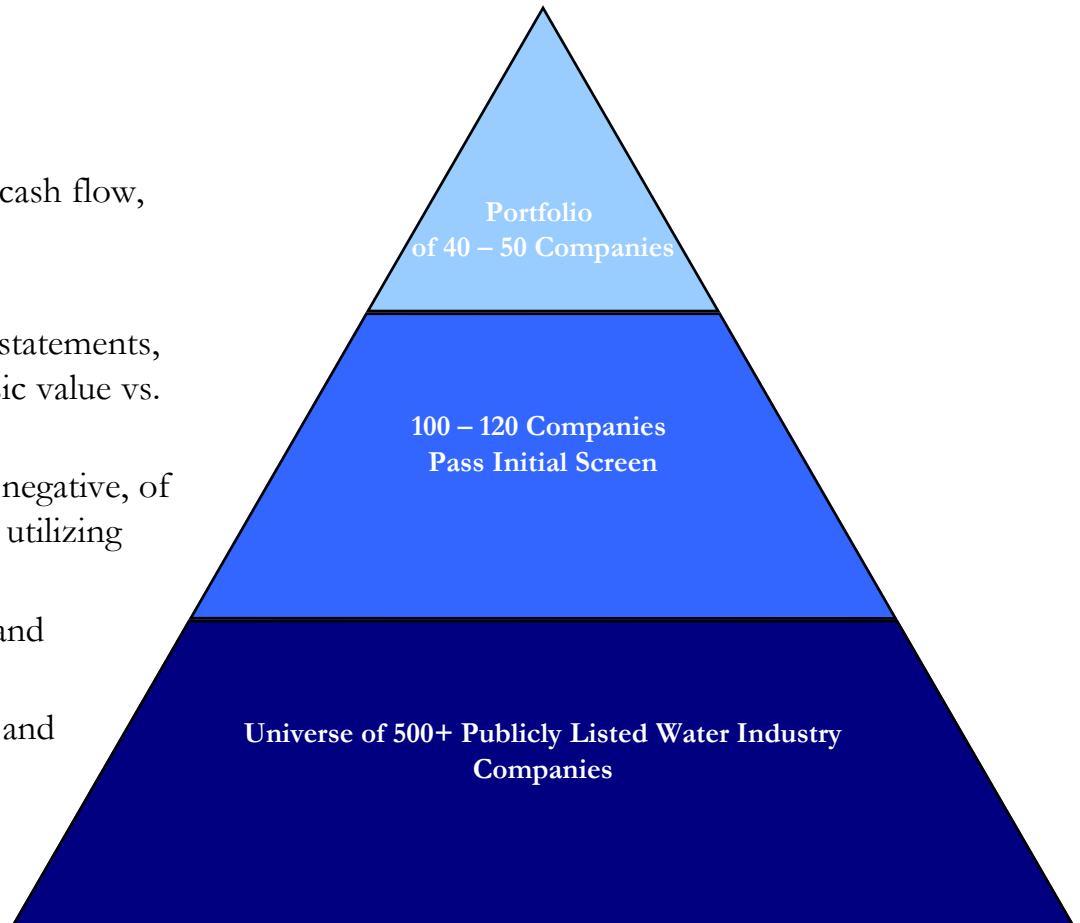
NOTE: The information on indexes is for illustrative purposes only and is not intended to imply the performance of any investment. The index and composite assume the reinvestment of dividends and interest. The S&P 500 is a widely-recognized index representative of the broad markets. A direct investment in an index is not possible.

Past performance does not represent future results

# Investment Methodology



- Define water universe
- Screen for under/overvalued issues
- Rank stocks based on fundamentals (EPS, cash flow, ROE, etc.)
- Rank companies in a relative value format
- Perform additional analysis using financial statements, databases and research to determine intrinsic value vs. market value
- Identify potential issues, both positive and negative, of each company considered for the portfolio utilizing research and modeling
- Converse with industry contacts, analysts, and company officers
- Determine the purchase price of a security and allocation to portfolio
- Monitor positions on a daily basis

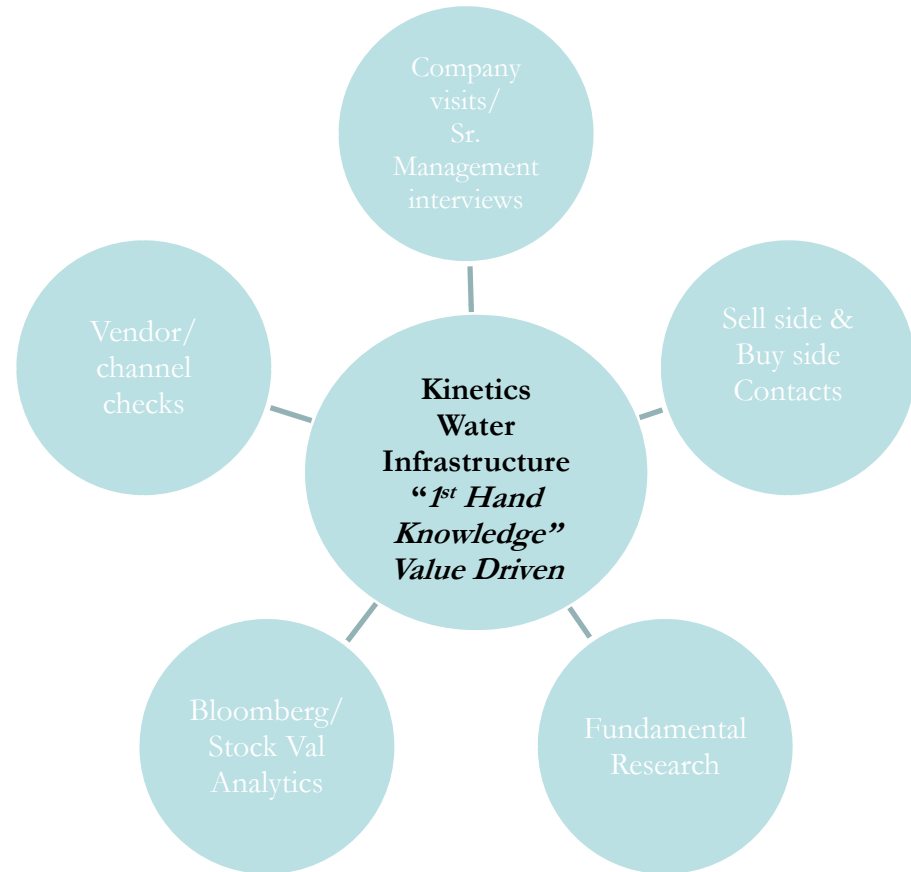


# Our Core Idea Generation

An thorough understanding of the water space both globally and locally combined with a wide network of contacts stemming from past water related experience

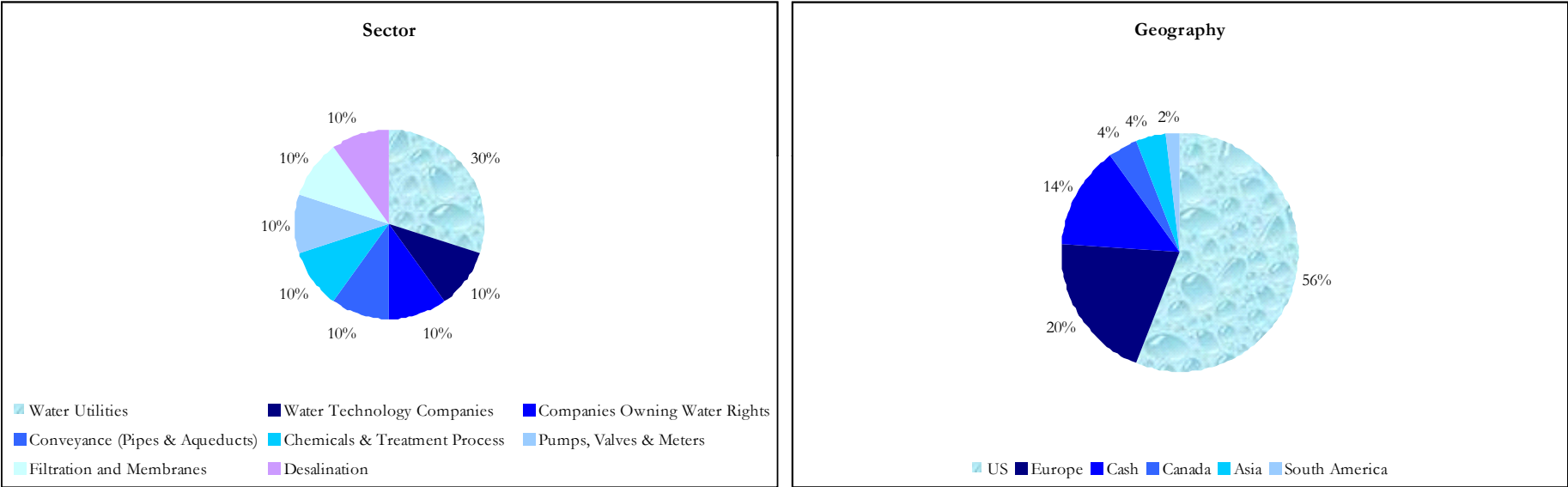
Our knowledge of the water industry is deeper than traditional managers. Mr. Brennan has had substantial experience analyzing many aspects of the water industry.

We believe that such experience coupled with sound technical and fundamental research will produce above-average results for investors looking to capitalize on a growing global water market.



**Look for the long term - buy a “business” not a stock**

# Water As a Tool - Diversified Portfolio Within the Water Industry



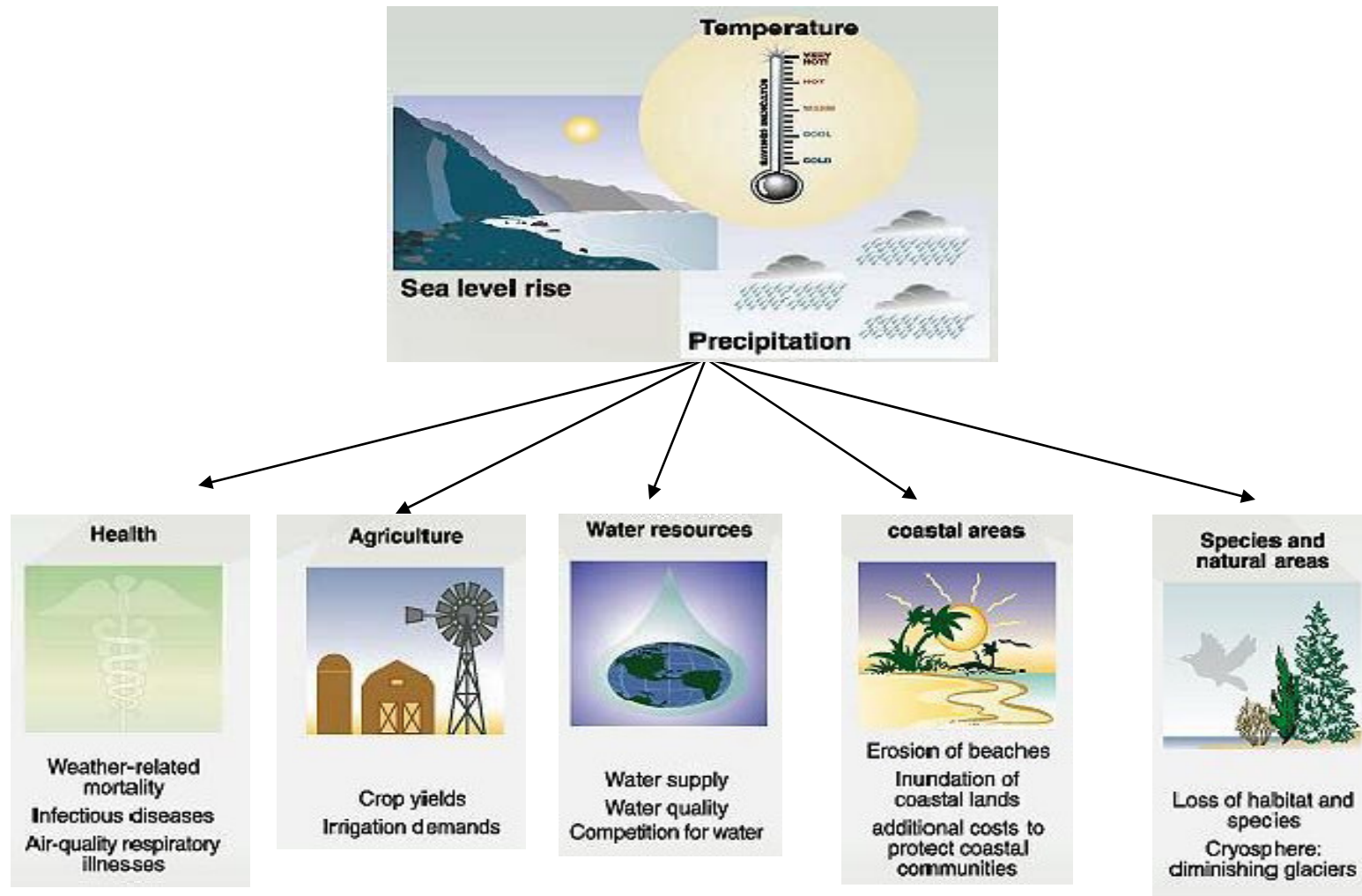
*Model portfolio shown is a typical representative portfolio and is subject to change without notice*

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# Case Studies



# Global Warming-What Does Climate Change Impact?



Source: GRID Arendal

## Case 1: The Investment Case for Water Utilities

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In our view, U.S. water utilities (as well as most global water utilities) are regulated monopolies benefiting from rate base increases which are typically controlled by Utility commissions.

### **Barriers to Entry**

Water is costly to transport over long distances, making competition almost obsolete; other utilities have greater competition; Capital intensity (PP&E / Operating Revs) is twice that of electric utilities.

### **Basis of Returns**

Infrastructure requirements are catalysts for capital expenditures; Increasing capital expenditures leads to increasing revenues.

### **Increasing Privatization**

Less than 20% of the 55,000 water systems in the U.S. are investor-owned; Water systems are easier to monetize via privatization than other municipal assets.

# Case 2: Clean Tech-Water

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## Market

- Several projects and sites under development mainly in UK and East coast U.S.
- No proven technologies on the market (no single wave or tidal stream energy converter has been producing electricity continuously for a year!); many years of development and testing for all concepts
- Wave & tidal stream will take another 5-10 years of product development
- Tidal barrage proven but limited & large scale

## Opportunities

- In our opinion, despite an abundance of opportunities, Marine technology is unlikely to be invested in because:
  - Most wave and tidal stream companies are still developing the technology
  - Large capital investments required
  - Support not sufficient to carry through to cost competitiveness
  - Many issues to be solved, access to grid, durability, etc.
  - Tidal barrage only suitable for project finance

	Expansion Capital	Development/ Generation	PE/MBO
Wave	LOW	LOW	NO
Tidal	NO	LOW	NO

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# Key Management Backgrounds



**William Brennan**

*Portfolio Manager, Kinetics Asset Management, Inc.*

William Brennan serves as Portfolio Manager of the Kinetics Water Infrastructure Fund and is responsible for helping create the firm's water investment management presence.

Mr. Brennan is the Co-Founder and President of Brennan Investment Partners, LLC, a registered investment advisor focused solely on water and water-related investing. In 2006, Mr. Brennan Co-Founded Aqua Terra Asset Management, Inc., a subsidiary of Boenning & Scatergood, where he was responsible for overseeing Aqua Terra's investments, serving as President, Managing Director and Director of Equities, until September 2008. From April 2005 through October 2008, Mr. Brennan was a Co-Portfolio Manager for the Praetor Global Water Equities Fund, based in Luxembourg. During such time, Mr. Brennan was responsible for the portfolio selection of the Claymore Global and Domestic Water UITs, the first water investment products launched in the U.S. From 2000 through 2006, Mr. Brennan served as Portfolio Advisor/Analyst to Summit Water Partners, a San Diego-based water-related hedge fund. Mr. Brennan was also a Director with Law Environment/Law International, an international engineering and design company based in Atlanta, from 1989 through 1992.

Mr. Brennan is a graduate of Lehigh University with a B.S. in Mechanical Engineering/Biology, where he was a distinguished graduate of the Air Force ROTC program and a starter on both the Varsity Football & Baseball teams. He also received an M.S. in Biomedical Engineering from Colorado State University and an MBA from Villanova University, where he is currently an adjunct professor in the graduate M.B.A. program, a position he has held since 2001.

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