



**Kinetics Water Infrastructure Fund
Conference Call with William Brennan
January 27, 2010**

Disclosures:

Kinetics Asset Management, Inc. (“Kinetics”) is pleased to announce that on January 27, 2010, William Brennan, Portfolio Manager to the Kinetics Water Infrastructure Fund hosted a conference call to financial advisors. The below transcript is intended to provide a summary of Mr. Brennan’s remarks.

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Kinetics Water Infrastructure Fund 1st Quarter 2010 Conference Call

1st Quarter Conference Call
Kinetics Water Infrastructure Fund

Chris Barrett: Hello everyone and thank you for joining us on the first quarter 2010 conference call for the Kinetics Water Infrastructure Fund (the “Fund”). I’m Chris Barrett with the Kinetics Sales and Marketing Group and I’m pleased to introduce Bill Brennan, our Water Infrastructure Portfolio Manager. Bill has managed the Kinetics Water Infrastructure Fund since its inception in June 2007. It gives us great confidence that he and his team are purely focused on the water business and the water business only. Collectively, they have 30 years of experience directly in the water industry. We believe that gives us a distinct advantage in identifying emerging trends, technologies, regulatory shifts and investment opportunities within the water space.

This is an actively managed, global, multi-cap fund focused on water and water resources. Companies within the portfolio typically derive at least 40% of their revenue from water and water-related activities. As an investment theme, water has historically been an attractive non-cyclical opportunity with low correlation to the broader market. Bill takes a tactical approach to managing the Fund, rotating to sub-sectors and regions where spending and growth rates are accelerating.

Before I turn the call over, I want to remind all of our participants that you can access additional information on the Water Infrastructure Fund and all the Kinetics Mutual Funds on our website, <http://www.kineticsfunds.com>. With that, I will now turn the call over to Bill.

Bill Brennan: Thank you Chris, and thank you everyone for joining the call today. As Chris said, and I would like to reiterate, the Fund is a multi-cap value Smid-Cap fund that focuses on problems in the water industry globally as well as projected water issues. It invests in the companies



that provide solution sets and remedial efforts to solve those issues. What I will do during the course of the conference call today is talk about how to position the fund within your portfolio, what the catalysts are for the fund both short term and long term, the general state of the water business, the tactical outlook of the fund, a stimulus update both on the U.S. side and in China, and closing remarks with a Q&A session afterwards.

I would like to begin by discussing the composition of the Fund. Presently, the Fund is categorized by Morningstar as a Smid-Cap fund with a blend rating. We believe it is a value fund. We presently have 55 positions in the Fund, and over the course of the last 3 quarters we have increased our exposure to the China market to 10 total positions. 45% of the portfolio is currently domiciled internationally. Our P/E ratio going forward is right around 12X earnings, our P/B is 1.54, and the median market cap is \$960 million. Now I bring these metrics to your attention because in comparison to other water products, both the passively managed ETFs and the other water mutual funds that may exist, both here and overseas, it's apparent that our Fund really does focus on the value aspect of companies. We're looking to invest in companies at a discount to the intrinsic value of that company and look for the dislocation in both the markets and the investment communities and step in and take positions there.

Now a number of people who are familiar with the Fund and those who are new to it always ask the question: How should it be positioned in a portfolio? You can do this in several different ways. It can be positioned as a natural resource fund. It can also be positioned as a commodity fund. Although it is the most precious commodity in the world, water is not priced as other commodities. It can also be put into an alternative silo for investments. We really look at this, however, as being a Global Smid-Cap Value fund with an emphasis on water and water-related activities that invests in the companies that provide the solutions to the world's water problems, which have been well documented over the last two years. Ultimately, we invest in the solution providers that are taking



care of the world's water problems and we continue to believe that that is the ideal situation, from an investment theme. On a side note: we may be defensive in nature. If the market shows volatility as it has in the past, we will not be afraid to go to 50% cash, if not more, if market conditions deteriorate. We will then wait for the opportunity to step back in at lower valuations once the market has settled. We have held as much as 45% cash in the portfolio in the past, so we have proven that we are not afraid to go to cash in periods of volatility. We are looking to build the portfolio one company at a time and we will establish that position and add to it as the market provides the opportunity. We don't bet the ranch play so you will not see us hold more than 40% of our entire holdings in the top 10. That is greatly different than the other products in the market, some of which have upwards of 55% and even 60% of their portfolio in the top 10 holdings. We are really focused on lower volatility and the risk management of the portfolio.

Another answer is the fact that we are seeing a rotation out of high beta stocks and beta funds and into steady growers. The water business has consistent growing characteristics and therefore it's ideal if you're taking a look at your portfolio position and want to gravitate towards a lower beta but a steady earnings income. We believe it's a good trade to put a 5% position into the water sector that will provide that steady grower, which institutions, in our opinion, are likely to rotate to.

As for the catalysts for the Fund, we see consistent spending in the water sector, although the stimulus did create some choppiness in the U.S. in 2009. Fortunately, our data over the last several months, which included taking a look at the municipal bond issuance and the water and wastewater CPI, showed both of them moving in the right direction. The upward trajectory was 7% in January and the municipal bond issuance nearly doubled in January from a year ago. These are very good indicators for the water market and for spending because most of the water utilities go to the debt market so we see that as being freed up and we expect that type of situation to increase



during the first half of 2010. Another emphasis within the portfolio is that we have a concentrated position in utilities right now because we feel they are undervalued and the fact that these rotations into these lower-beta, high-yield stocks that there is a prevalence in the market to move towards that yield model. We have positioned the portfolio 2 to 3 quarters ago to take advantage of what we saw as a shift in the mentality and the configuration of companies moving more towards the utility model. Again, we feel that we got there early enough and we will see other institutions go into that sector, especially with the U.S. water utilities providing a nice yield.

I will now speak about the general state of the water business globally since we have been through the economic turmoil and investment paralysis. The business of delivering clean water and protecting water resources is in a relatively comfortable position. This should not come as a surprise; the water industry is driven by a host of compelling non-economic factors such as scarcity, population growth, extensive regulation, and aging infrastructure. These factors have kept the industry purring along even as other industries, such as land development, hit rock bottom. And if you take a look at what is going on in the commercial market and the residential market, we're trying to dislocate and prevent exposure into certain aspects of the real estate market that in the past have had an impact into the water business. The slump in the real estate market has meant a new weakened rate of new water and sewer connections compared with the first half the decade. In addition, the limited financing capacity has surpassed activity in rehabilitating aging US water and wastewater infrastructure. We feel that we really are at the pinnacle and at the convergence of crossing over that line. Consequently, we believe there will be an acceleration through either tariffs or tiered structures in pricing that will continue to surge forward with regards to spending in the water industry not only here in the US, but globally as well. A huge gap still exists between what's needed to be done and what water and sewer rates can support in infrastructure rehabilitation and has been in place since well before the recession. The American Recovery and Reinvestment Act



(ARRA), better known as the economic stimulus package, has provided basically a booster shot to this, but we are still \$600 billion behind in our infrastructure spending on the water side.

Internationally, the investment in water resources and water infrastructure development is down, but not out. We are seeing that trend starting to move upwards again. China and the Middle East nations still offer strong market opportunities, even though the pace has slowed somewhat. Europe is still somewhat of a mixed-bag, with the United Kingdom struggling with regulations and limited rate increases, but Spain, Italy, and the rest of southern Europe remain strong.

The rudder keeping the water industry's stable course throughout these choppy seas is the fact that even during economic slumps, nobody can do without water. We take the position that people will use the same amount of water regardless of what happens to the economy. Even though we see technologies being introduced that limit the water usage, when you take into account that these systems are old and failing, the cost to maintain the day-to-day operations continues to move up.

Right now, on the water-side, there is an immense need to build and upgrade the water infrastructure in both developed and developing economies. The coming growth around delivery and disposal of the commodity really leads us to have a positive view of water related investments across the entire spectrum. Not only from a potable drinking water standard and a wastewater standard, when the wastewater standard is becoming more and more critical, especially in areas like China, but also when we take a look at the industrial sectors. We look at how the change is going to take place with how they deal with their product water, the creation of contaminated water at the point where manufacturing takes place, and how they're going to have to dispose of and treat that water at that site rather than discharging it into surface waters that eventually make their way into municipal drinking waters. The focus is going to be on the production of drinking water for the growing population, water distribution networks, and the collection and treatment of wastewater.



The aspects that are driving this right now are significant capital expenditure requirements, which are only going up, and increased recognition of the value of water. We see a number of funds coming to market now that are buying water rights across the world. The quality of water, the sanitation of it, and just as important although people tend to overlook it, the security of the supply and the sanitation all play a role. Again, there is a political aspect to the water business. So, political willingness to price water according to economic principles and charging the users accordingly, we see us moving more and more towards full-cost pricing where we will pay for the energy, the transmission, and the treatment of the water, which means as we told people over the course of the last several years, expect that your water bills, at least in the U.S., will go up anywhere from 2 – 5 times to reflect that, based on your position geographically and the scarcity of the water.

Now let me spend a second on the water utilities. With the low interest rate environment right now investors have a renewed thirst for yield. We feel we got ahead of the curve and with money market returns in single digit basis points and treasury yields low, the case for owning high quality water utilities is definitely en vogue at this point and we feel we are ahead of that curve and have positioned the portfolio quite well to take advantage of that.

Water stocks, when evaluating the three main sectors - water treatment, water industrials and services, and water utilities – varied in their returns in 2009, and utilities lagged in performance. Therefore, based on our value premise, we felt the need to increase our portfolio holdings in those specific utilities during the year to obtain what we believe will be favorable valuations relative to the rest of the water sector. Water utilities may not grow very fast, but we feel they are remarkably consistent, delivering solid but not spectacular returns every year. This enables these stocks to deliver impressive compounded returns over time. While US water utilities returned approximately 5.0% as a group in 2009, valuation sensitivity and appropriate weighting allowed us to establish positions and add to existing positions at multi-year low prices. Investing in water is not as simple



and straightforward as investing in other commodity groups, but this is likely to change in short order. The utilities really are the “anchor” stocks, defined as cheap, high quality companies with solid dividends that have a lower beta relative to the broader market, prospects for continued earnings growth, and the possibility for valuation and multiple expansions based on increased cost for water treatment and delivery.

The recent upward trend is providing a real clear snapshot that a rebound in 2010 in water spending is clearly occurring. With that in mind, we anticipate that pipe manufacturers, which have been in somewhat of a slump, pump companies, meter manufacturers, and integrated water treatment solution providers, such as Veolia (VE) and Suez (GSZ FP), will benefit from stimulus money earmarked for water projects that is finally freeing up in 2010. There is going to be a race in the next several weeks to get that deployed and into the RFPs because there is a time clock against them. So we believe you will see a couple of very strong quarters of earnings in many of these sub-sectors based on the stimulus. Also, the annual maintenance and upgrades that were postponed during the last 15 months, but are now underway, give us somewhat of a sigh of relief to see that certain industrials will move forward and we believe decouple from the other industrials in the broader market. In the context of what investment professionals are calling the “new normal” - diminished growth, deleveraging, and increased government involvement that will reduce profits - we believe that the water group as a whole could experience significant investor interest in 2010 and beyond.

As far as the stimulus is concerned, with regards to the update both in the U.S. and in China and how that is impacting the portfolio right now, we believe this recovery, at least in the water market, is well underway, but it is difficult to separate the purely cyclical forces of improvement from those created by the government’s fiscal and monetary spending. Many have asserted that the recovery is not self-sustaining. We do not agree. In our view, whether the economic growth seen



this far is primarily stimulus-based or not is less important than whether it creates a perception of recovery that, in turn, becomes a self-sustaining reality by boosting confidence. We are seeing an underlying recovery in the water market based on the municipal bond market based on the CPI that gives us comfort going forward with regards to the portfolio. Once we get beyond the stimulus package, I believe that you will see tariffs and tiered water usage similar to what people in California have experienced in certain counties and other areas of the country where there is scarcity. You will see these tiered systems go in effect which will basically be the first step forward in full-cost pricing.

We think China's growth, under their 2-year stimulus program, which is massive compared to their GDP, could be 8.5-10.5% in 2010. The government there is spending in two areas: military complex and water infrastructure because they realize that the latter is critical to China's continued GDP growth. That being said, what we've seen is a new entry of Chinese-based companies into the U.S. market, listing in the U.S. market from a transparency standpoint, even though there are always questions about really how transparent the Chinese market is. We feel that the move by certain Chinese water companies to list here in the U.S. is a great step forward and provides a degree of confidence for us. It also allows us to purchase companies outside China that are directly involved in and have the majority of their business reside within the China footprint.

In closing, water investing is not a direct investment based on some arbitrary value per gallon of water, because basically how you and I pay for it here in the states is at the tap. It really is a strategic investment in the many sub-sectors that are involved in its extraction, treatment, regulation, metering, conveyance, and resource management on both the domestic and global stages. Many investors are going to look at water in varying capacities, whether it is commodities, natural resources, alternatives, and utilities. But these are just a few of the boxes that water is placed into by the investment community. Although water is continually referred to as the next oil, we



have always looked at this over the past 20 year history of my involvement in the water business as an engineering consultant and now as a portfolio manager that the consistent growth of the water business would provide investors with the exposure to a solid growth commodity that remains a necessity in everyday life.

In summary, we believe that the Fund accomplished its stated goals in 2009, which were to invest with a value approach, thereby minimizing volatility while emphasizing risk management. We will continue to use cash as a hedge when we feel the market valuations are fully or over-priced. We believe the economic underpinnings of today's markets are somewhat stable while valuation multiples have expanded in certain sub-sectors beyond what would be our normal investment comfort level. Therefore, you will see us rotate into sub-sectors that we feel are true value plays and in regions where there is a strong economy and strong currency. We remain confident in our ability to identify good companies at reasonable valuations and looking at 2010, we will remain cautiously optimistic even though there are unresolved issues in the market brought on by the stimulus package. We feel comfortable and are of the opinion that even if the market did remain flat during this year, the active selection of water equities may be in a position to outperform water benchmarks in 2010.

On that note, I would like to hand things back over to Chris Barrett for any questions.

Chris Barrett: While we are waiting for questions in the queue, I would like to remind all participants that you may access our top holdings, fact sheets, prospectuses, and all performance information for this and all of our mutual funds at <http://www.kineticsfunds.com>.

Also, we have an updated retail approved overview presentation for the Water Infrastructure Fund that you can request from our internal marketing group. Please direct any requests to Bob Uly or Tom Gormley at (914) 703-6950 or by email to Marketing@kineticsfunds.com.



Question 1: You mentioned that you would take your cash position up to 50%. In the past two years, you outperformed the market in the down market of 2008 and under-performed last year so you are flat, which is good. How much of that was the nature of the industry and how much was your effective use of the cash positioning?

Bill Brennan: That's a very good question and I would say that both came into play. The spending in the water business became very choppy over the last 15-18 months, and because of that, we decided to pull away from sectors that we normally would have gravitated towards. In particular, we reduced our exposure in the area of the pipe companies based on a downward trend in the real estate market and also based on the fact that pipe companies like Mueller Water (MWA) along with others we had previously owned in the portfolio really had a run in the second quarter of 2009. At that point we made a conscientious decision to look at the valuations and decided that certain industrials and certain sub-sectors in the water business were really trading around 2011 and 2012 valuations and we left. That being said, that did have an impact on the portfolio that caused us to under-perform and we saw some of the companies that we sold during that time period actually appreciate another 20-30% and in some cases even 40%. They have since pulled back down and have even gone below the price at which we bought them. We then reinitiated positions in the portfolio seeing that the trends in the market were now moving in their favor as we got through the 4th quarter of 2009.



Water Infrastructure Fund Top 15 as of December 31, 2009	
URS Corp New	5.82%
Ameron Intl Inc	5.53%
Geberit	4.72%
Lindsay Corp	4.00%
Armttec Infrastructure Trust	3.19%
Veolia Environnement	2.80%
Northwest Pipe Co	2.69%
Guangdong Invest	2.55%
Tetra Tech Inc	2.37%
Itron Inc	2.36%
Esco Technologies Inc	2.35%
Acea SPA	2.34%
Middlesex Water Co	2.31%
Severn Trent	2.29%
Connecticut Water Svc Inc	2.29%

The information contained in this chart is updated at the discretion of Kinetics Asset Management, Inc. and is only representative of the Fund's portfolio on the date specified. Additionally, position size may not be indicative of actual market position due to the use of call and put options.

On the cash side, those of you who have been in the Fund know that at the end of February and at the end of March in 2009, the portfolio dramatically changed. We were holding somewhere between 35% to 40% cash in the portfolio in 2008. As of the end of February and by March 9, 2009 we had gone back to being roughly 95%-99% invested in the marketplace, feeling that at that point in time the market had become oversold. Our quantitative analysis and technical analysis indicated that it was safe for us to go into certain sub-sectors, especially those like the utilities. The reason I keep bringing that up is because when we look at the market overall and we see how earnings are being achieved through cost-cutting, when we take a look at the year-over-year comps and in a number of these industrial companies like Flowserve (FLS), which we don't own, that forward looking number as far as where these companies are going to come out as sales, operating margins, and EPS, we continually see negative numbers coming up across the board. Now, a lot of the cost-cutting has already been done in 2009 and in the industrials, where these companies can continue to



cut further if there is not an upward in sales remains to be seen by us. We look very cautiously at the sub-sectors we feel have an upward trend and are moving into positive sales year-over-year. In summary, I would say it was both cash and also the position in the portfolio that got us through the volatility and led us to under-perform in 2009. Again, when you look at our metrics in this portfolio we are very different from other water funds and we don't deviate from what our investment mandate is.

Question 1 (Con't): Right now, are you a little more US oriented than you were at times last year?

Bill Brennan: Right now, the Fund's assets are invested approximately 45% to 47% overseas. We have been trying to keep it half-and-half, especially when we see the water spending in the U.S. that we believe will pick up in 2010. You will see us, moving forward, fluctuate from 40% to 60% on both sides of it. Again, those of you familiar with the product know that we have a self-imposed mandate that we don't want to have any more than typically 20% to 25% exposure of the portfolio into what is considered emerging markets. I would say as a benchmark going forward that you will see us in that range, whether it is 40% U.S. and 60% overseas if we feel this acceleration in China or the Middle East or other areas with regards to water infrastructure building can be beneficial to the portfolio. If we see the United States and Congress really get serious with regards to tariffs on the products that actually cause contamination of the water, then we may shift and have the flexibility to move into the names that we feel will benefit from those activities and that type of spending.



Question 2: Do you see any particular sub-sector in the portfolio that you feel, at this point, has superior return characteristics?

Bill Brennan: Yes we do. We feel that a number of the overseas utilities right now continue to be under-priced and mispriced by the marketplace. As we go through and take a look at certain names like United Technologies (UTX), Severn Trent (SVT LN), and Northumbrian Water Group (NWG LN), even with the UK utilities, we believe there is a fundamental disconnect between how the market views this OFWAT situation and really what the underlying opportunity is in a public water portfolio. The UK, right now, is of interest to us because the pricing pressures have really put the green light on with some private equity firms taking a look and saying: What's the underlying value going forward over the next 20 years of these entities? As I've said, this pricing of water is going to become more and more prevalent and as that becomes full-cost pricing, and people look at this as a commodity price on a per-acre foot if you exchanged the water right, I would say that your water utilities, not only overseas but here in the U.S., are going to have a significant interest by the investment community. So I think that to a large degree, the standard metrics of how utilities have been valued will at some point in time be at a disconnect, and people will look at what the underlying ownership of the water is on a per-liter / per-gallon basis. That to me is very exciting as we're moving into this mentality and we see more water rights firms and funds being established and causing the price of water to move, especially when you take a look at other applications that are coming in, as far as water usage. The old standards, as far as heavy industry, were steel and semiconductors. Now you've got solar and solar thermal plants, which consume enormous amounts of water. These utilities are very well positioned for the next 3-5 years and that brings up another point: when we buy a company in the portfolio, we make sure we do exactly that. We intend to own



the company and treat it as such. We are not traders. We will tactically trade out at target prices. But right now, I think the utilities have a long way to go from where they presently are.

Question 3: First, can you comment on the valuation of the water names that you're holding that are in China?

Bill Brennan: There are certain names that we feel the underlying intrinsic value has not been recognized as of yet and we'll see the earnings growth based on what the sales projections are and the specific areas of the water market that they are moving into. As far as CK Infrastructure, I can go through certain names with you right now. Guangdong Investment Limited (270 HK) and Xinjiang Tianye (840 HK), where we have seen an increase as far as the volume in Xinjiang over the last several weeks. People are taking a look at these undervalued Chinese plays for the long term. We still think there is a lot of value there in China, but we're adding some U.S. listed companies like Trittech Evaluations, which is squarely in that water and wastewater component side of the business and we still continue to see good valuations in the China market and in the whole Pacific rim market because we own Maezawa Kyuso (6485 JP), Sinopipe (SPIP SP), and Sinomem (SINO SP). Those are still good value names to own over the long term.

Question 3 (Con't): How much do you worry about government risk in terms of water rights overseas?

Bill Brennan: Well, overseas is different. A quick snapshot, as far as that is concerned, where we really see the water rights being traded right now is in the Western U.S. and Australia. The provinces in China will eventually trade water if the systems are connected. I don't see this



massive push to lock down water rights at the surface, but there are continued moves with the EU as far as the water sharing arrangements between the countries, as far as surface water is concerned. They are still trying to hammer that out. That thing has been an ongoing process for the last 4-5 years and it still isn't in its final disposition. China, because of the structure of the government, the provinces, even though they would like to lock down their water and keep it within their boundaries, similar to what we like to do in the states, they operate their management program as far as water usage on a basin basis. Where I think we have made the mistake here in the United States is that we do it on a state boundary basis and don't look at the basin as a shared resource among the states. That is why you have these constant battles that have now flared up into the Supreme Court between Georgia and Tennessee, North Carolina and South Carolina, Nevada, Colorado, and California with regards to who is going to be able to use what out of the Colorado River. Nevada is actually funding a lot of water projects in California that would make them less dependent on a resource that Nevada would like to take for themselves. You see a lot of tactical movement here in the United States. Over in Australia, because of the situation where the population exists where water doesn't, if there are water rights in those high-density areas, they are a very good asset to hold. I think over the long-term here in the U.S., water rights have to be looked at on a state-by-state basis. That is what people see when they look at the water business overseas in comparison to the U.S. There is no political mandate governing water in the United States. The Water Reclamation Act and the use of the term "Navigable Waters" has created some stir among the states because now it is the federal government's move to see if we can somehow gain a foothold as far as controlling the physical asset. You'll have a number of states backlash at that because of interstate commerce and imminent domain that I think we will shoot that down. Over the long haul, you're dealing with 50 governments in the United States as far as their water disposition is concerned, and each one has their own unique problems. Where I am physically located here in



Pennsylvania, we're dealing with this fracking situation and that is really the big hold up here as far as the product water and if they can't dispose of this and create some kind of great water mechanism to be used as an alternative source after it has been pumped through the frack, then the fracking won't take place. We're seeing companies like Heckmann (HEK), starting to make acquisitions in Louisiana and Texas specifically focused on fracking. Therefore, we realize the companies are moving towards these different industries and this leads me back to what I said earlier in the conference call about the way that we are looking at the industry right now. There are certain sectors that are going to be pinpointed by the EPA at the state levels as far as the product water creation and they have to do something. Oil / gas and pharmaceuticals are the two that come to mind right now that not only does the EPA have a bull's-eye on but also the state governments as well. So that is going to have an impact as far as this whole water rights and water disposition process plays out over the next couple of years.

One last point to make if you have any follow-ups, we have taken our initial step into the publicly traded water rights. There are a limited number of companies here in the US that play in that marketplace and right now we felt that Cadiz (CDZI) is very well positioned, especially in lieu of what's been going on in that southern California region with the increase in the solar thermal plants and their need for water in order to operate. We think that Cadiz has a pretty ideal situation especially with proposed legislation not to develop the Indian reservations in that part of California, which would prohibit the use of solar in that area. Cadiz, as far as a contiguous landmass with underlying water rights, could actually morph into a multi-utility with solar and water providing a nice and interesting situation for investors.

Question 3 (Con't):

Lastly, how do you think that municipalities are going to raise water

rates?



Bill Brennan: Here's the thing, this is something you're going to have to look at on a zip code-by-zip code basis. There are certain municipalities that will be able to access the market and raise the money. Historically, water companies have always had one of the lowest borrowing rates in the marketplace and that will continue because of governments' involvement in this. They realize that everything comes to a standstill if you pull water out of it. When I talk to other commodity managers and ask them to remove water from their commodities for a week and see what happens, all hell breaks loose. From a mining standpoint and a timber standpoint, you can go across the board and they all say the same thing. In this municipal market right now, you're going to see states develop programs for areas that from a financial standpoint just don't have the tax base in order to get it done and to make the necessary upgrades just to keep those systems operating. You're seeing it in certain southern states right now where the states are getting involved in conjunction with the PUC. They are packaging up certain municipal water operations, putting it into a nice package, and the public water companies, because of their capitalization and the fact that they've done this time after time, are going to have a first-mover advantage as these municipal water systems are unable to get bonds launched. The publicly traded water utilities will be there to pick them up. We're already starting to see that in the southeast right now and I think that is going to do nothing but accelerate. We only have 12-15% private ownership of water utilities in the United States. When you go to Europe, it's 45% and moving upward. I expect in the next 5 years, because of the economic situation, that you will see more and more assets transferred over into the public's hand and when you only have basically 10 or 11 publicly traded utilities, they've got a first-mover advantage. From my standpoint and the way I look at the portfolio, I believe we are well positioned to take advantage of that projected event.



Question 4: What regulatory changes do you see both on the domestic and international levels, and what names or subgroups in the portfolio stand to benefit from these regulations?

Bill Brennan: In the U.S., the regulatory component of this has basically been dead on arrival for the last 7 years. What we see right now is a renewed focus on the water industry by Lisa Jackson, the present EPA administrator, and also Carroll Browner, the energy czar. We really feel that the focus of the EPA is at the industrial level. They realized that if they go to the municipal side and say they have to upgrade their water treatment system because a pharmaceutical plant upstream is contaminating their intake of surface water from a river, the government is going to look to the polluter to solve the problem at the point of contact. That's going to be a fundamental shift moving forward that the onus won't be on us. I really think that the EPA is going to focus on the industrial polluters. They already have with oil and gas and I think the next move will be into pharmaceutical. Companies like Tetra Tech (TTEK) and URS Corporation (URS) are very well positioned because the engineering companies provide a solution set. They are the first ones that are called and from that, you create this value chain where Tetra Tech and URS will go to the varying product suppliers and the varying technology companies and implement a protocol. Right now in the water business, we don't see any silver bullet as far as a new technology that is a game changer and that is going to revolutionize the way the business works. What the water business has failed to do is take the existing technologies that are out there, use them in a unified fashion, and package them up in a SKID(?) format or whatever the case may be, as far as a real value solution set that involves not 1 technology or 2, but 5 or 6 that solve multiple problems. We think that the EPA and the federal government here in the U.S. are going to move towards that and we're already starting to see NSG grants as far as investments into water technology move that way. That is refreshing for me because



coming from the engineering side of this business and building these things for 5 years, to see that type of fundamental shift is something we are very encouraged by.

Overseas, with regards to China's regulations, they took our EPA rules and regulations and basically overlaid them. They called it SIPA. From an enforcement standpoint, China still relies on a large part for the large primes; the Suez's, the Veolia's, the ITT's, the large engineering and system integrators to come in and basically set the framework and also take on that regulatory hat. Now the reason why a Veolia and a Suez, which we own in the portfolio, are willing to do that is because when they take a look at China's spending, not only in the course of the next 5 years but take it and extrapolate it out 10, 15, 20 years, they realize that if there is a slip-up or if they fail to walk the regulatory framework and cross their T's and dot their I's, then they will be prohibited from bidding on future larger contracts going forward. So over there, we have a high degree of confidence how those companies are performing regulatory wise and within the framework that has been established. Also of interest is that a lot of these Chinese companies have ex-PRC officials and people who worked in the government now in senior management positions. As these sub-primes are put into the larger water projects, we will see a number of these companies that will get carve-outs and they will act as the eyes and ears, from a regulatory standpoint, for the Chinese government. We see the regulatory side of this as being still involved but not choking it to the point of an economic backlash. We feel a lot more comfortable with an active EPA over one that is inactive, which would allow industries to continue to contaminate water without doing anything to remedy it at the point of contamination.

Question 5: With regards to private and public ownership, could you substitute the words “corporate” and “government” and go over those statistics?



Bill Brennan: There has been a roadblock or an impediment here where the publicly trade water utilities like to have and have enjoyed a first-mover position. We feel that some of these larger infrastructure funds will probably either team up with them in the future or, as I've said with the UK, the likelihood that you'll see private equity step in there and purchase some of those regulatory utilities and take them private is moving north of 50-50. In certain parts of the world, however, you will still see government involvement. This will vary based on the involvement with regard to rate cases and the rate increases. You will never see a privatization to the point where someone steps in, buys a municipal operation, and just goes hog wild and is allowed to increase rates by 50%. You are always going to have a regulatory power to some degree when pricing is involved. From a growth perspective to some people, if you are involved in technologies or the semi industry, this thing is not going to go from \$0 to \$400 million on a dime based on water, but we believe you are going to have that steady growth. We think that the U.S. government and the state governments, based on the present state from an economic standpoint, will encourage and you will see more involvement of private corporations into municipal and wastewater operations, especially on the wastewater side. This is an area that for some reason continues to be an ignored piece of the water business. People are so focused on drinking water, but what they don't realize is that the wastewater is responsible for a large percentage of the contamination that does exist within our drinking water and continues to exist because our regulations are so old that the asset disposition has changed considerably over the last 25 years. We have a number of things in the water today that we didn't have 25 years ago because of the pharmaceutical industry and vitamins and things of that nature and the fact that we pass these things out. It goes through wastewater, goes to surface water, and goes right back into the municipal water. We think that on the wastewater side, you will see an increase as far as privatization is concerned.



We get asked all the time about when China is going to step in, kick everyone out, and say this is our water business. We don't think that is going to happen, at least not in our lifetime. I'm not going to sit here and say that it's 100% that an event like that couldn't take place because when you look at water and you take it on a country by country basis, using the Middle East as an example, when you see where their military assets are deployed, as far as protection of infrastructure, there is more military infrastructure around the desalinization plants than there is around the refineries. It gives you an idea, from their standpoint, as to where they place their value and if the water was removed by an attack or whatever the case may be, you've got a health outbreak, you've got anarchy, you've got all these things that can arise.

Here in the states, we're going to take a look at this on a state-by-state basis and look at the unique characteristics that underline both at the political level and also at the composition of the water and that will determine the government's involvement going forward and the need for them if they don't feel that they have the proper infrastructure to bring privatization and bring corporate dollars in to move forward and jointly control the asset.

Question 5 (Con't): I have heard conflicting reports about silver being used as a decontaminant, while also being a contaminant itself. Can you elaborate on the role of silver in the decontamination process?

Bill Brennan: Silver-based purification units have been used in Europe for years. Algae and bacteria can't grow on silver. If you take it back historically, you'll understand why the British navy used silver goblets and silver pitchers because the water stayed clean. My opinion of silver is from an industrial metal standpoint and the fact that the increase in usage when you take a look at the number of wastewater treatments plants that going to be necessary, you are going to have an



increased demand for silver globally. On the nano-side, and I've spent some time in the nano-technology world where I was on the board of a nano-tech company and heard every argument that there is with regards to the increase in incidence of cancer and the fact that these particles break away over a longer term. When we look at empirical and scientific data, if we see something that is presented to us in the water sector that is a couple of days of test data for a certain technology, we throw that out. We need to see something longer term to determine if these particles break away. The good thing about this, however, is that these things are being brought to light at the very initial stages of it and if there is enough public outcry and enough public interest in it, if in fact that is the case, you won't see those type of technologies implemented into everyday situations. We have enough problems as it is, just with the current disposition of our water and so from that standpoint to add anything more into it our water will make it worse than it actually is currently. We think from an investment standpoint, silver has got a component and is going to be a part going forward. Perhaps not in the nano configuration, but as far as the silver component with regards to waste water, absolutely.

Chris Barrett: With that, we would like to thank everyone for joining us today. We appreciate your continued interest and support. Please do not hesitate to contact our marketing department, at (914) 703-6950 or at our website, www.kineticsfunds.com, with any follow-up questions or requests for materials.

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