



Investment Market Update No. 31 June 2008

Editorial

"Faith can move mountains but you'd better take your spade."

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David French

Managing Director and Senior Investment Advisor

The Business

Do you know that CIPL now has 13 dedicated and enthusiastic staff? That's 1 staff member for every 20 portfolio clients – a very favourable ratio. It means that there is always someone available to deal with your needs, and it means that the Advisors – David, Sue, Justin and Bob, can concentrate on more complex tasks, while other competent people handle general administrative matters. All advisors and several other staff are shareholders of CIPL, a measure designed to encourage a more client focused working environment.

We expect that clients will gain a lot from our more team based approach to client service. It protects the business from loss of knowledge if someone does leave, and it means that there is always someone on hand to assist with your needs. Toward the back of this newsletter, you will find a 'Putting Names to Faces' section for more info on CIPL staff and their roles. You won't need to remember all this, but if we transfer your request onto someone else, be assured that it's because we want you to deal with someone who specialises in that particular matter.

Aside from staffing matters, we are undertaking some significant internal measures that will improve our service. One is the redevelopment of our client administration and reporting system, which we have rebuilt over the last year. We expect to roll this out within the next couple of months. The upgrade will offer superior reporting and more user friendly web access. It will allow CIPL staff to keep you better informed and up to date, particularly regarding changes in your portfolio. The new system will also result in reduced

paper clutter and improved speed in making portfolio changes.


We have been concerned for some time that we have not had an investment offering suitable for clients with smaller balances. Consequently, we recently recruited Andrew Brown and Robyn Donovan, who are developing a Property and Infrastructure Fund. We think this fund will be attractive to investors with smaller balances (although anyone will be free to subscribe).

The fund will invest in various property and infrastructure assets in regional areas, predominately in Central Queensland. We have long believed that the residents of regional towns and cities should be able to participate in the economic growth and expansion of the areas they live in. We plan to provide such an opportunity through the fund.

With Andrew and Robyn running the initiative, you can be confident that this new development will not distract CIPL from continuing to provide an efficient and professional service to our existing clients.

Market Update

Unfortunately our fears about the future of the stockmarket, which we outlined in our December newsletter, have proven to be true. There is no avoiding the fact that the second half of the 2007/08 financial year has not been a pleasant one for investors. It has also meant we have had to work very, very hard to assist clients in this difficult environment.



The Australian Stock Exchange 200 index, an index of the 200 largest shares in the stock market, has fallen approximately 17.5% since the beginning of the year. With the exception of a handful of resource stocks, falls in share prices have occurred across all sectors. This has even included companies and industries that were previously considered safe and reliable, such as banks and infrastructure companies.

The credit crunch, which began with the sub-prime debacle in the United States, has proven to be longer and more extensive than predicted by nearly all economic and market commentators. Companies which carried significant levels of debt were heavily sold off by the market, regardless of whether or not the company was able to meet debt repayments.

While we are of course disappointed with the market's performance, history has shown that during market falls the worst action investors can take is to make panicked or rash investment decisions. Although your portfolio has most likely suffered along with the entire market, it is important to remember a few key points:

- investing is for the long term (an old saying is that the key to wealth is 'about time in the market, not timing the market'); and
- a tried and tested investment strategy delivers better, more reliable returns in the long term, rather than constantly looking out for the 'flavour of the month'

The two paragraphs below are from our December newsletter – we have reproduced them here word-for-word because we still feel the same now as we did back then:

"CIPL's focus is on income generating investments, with a good track record, or with substantial security. In the current environment of increasing interest rates, these investments have not performed well compared to the market as a whole. On the other hand, their cash flow generating ability has remained strong, and generally speaking our portfolios have avoided the recent rash of profit warnings."

"Our policy is that the cash generating ability of the portfolio is more important than day to day movements in the overall value of the portfolio. Cash flows can be used to pay superannuation pensions and to make additional investments, without selling assets. Capital gains are nice but they cannot be used in that way."

Our approach and attitude to investing has not changed. Although we regularly assess the exposure of all portfolios to various risks and externalities, we believe that our strategy, which has produced above-average returns in the past, should not be changed on the basis of one market downturn.

For those who may not know, CIPL uses the best research from a panel of 5 stockbrokers, and other research subscriptions. You are in fact dealing with a very sophisticated business with excellent resources that brings a capital city approach to a country town (apologies to those city clients who like us anyway!).

It is also worth noting that CIPL has increased staffing levels over the last 6 months, something that should give clients confidence that we are prepared to service them well whatever the conditions.

We see the market as oversold at present. Some basic economic indicators are being overlooked, including the fact that appropriate use of debt often adds significant value to companies, and that resources are commodities which over the long term get cheaper, not dearer. This downturn is cyclical. It will pass and the task at hand is to manage through it sensibly.

Ownership of Assets

Some clients have asked if CIPL is like OPES Prime.

To recap, OPES Prime was a stockbroker and margin loan lender which business model revolved around using clients' assets as collateral for business debts.

Without realising it, OPES Prime's clients signed over ownership of their shares to OPES Prime. When OPES Prime ran into financial difficulties and was unable to repay its debts, the banks came looking for the collateral behind those debts. The net result was that OPES Prime's clients ended up losing the majority of their investments.


Let me highlight an important fact about being a client at Capricorn Investment Partners – at all times YOU are the beneficial owner of your assets that we manage on your behalf. CIPL's business model protects you in three ways:

First, your assets do not form part of our company structure (you can have a copy of CIPL's balance sheet if you wish). Second, our contract with you explicitly precludes using your assets as security for loans (except when clients have a margin loan as part of their own arrangements). Third, clients' assets are all held individually – they are never pooled together.

For what it's worth, our business is heavily regulated and externally audited and none of us here are keen for a stint in the "big house".

In a nutshell, CIPL is nothing like OPES Prime, Tricom or any of the others. The security of your investments is not reliant on or affected by the future of CIPL.

Although we have no intention of going anywhere, least of all of going out of business, we hope that this



information makes you feel more confident about the nature of your relationship with us.

Self-Managed Superannuation

Although many of you may already have a self-managed superannuation fund, we thought it was timely to remind clients of our expertise in this area.

With over 7 years experience of dealing with self-managed superannuation funds, we have the right skills and knowledge to help you set up and manage your self-managed superannuation fund.

As we have been telling clients for many years, a self-managed superannuation fund is one of the most tax-efficient and flexible vehicles within which to hold assets. For reasonably sized portfolios SMSF's are generally cheaper to run, are more flexible, and achieve better overall results.

Working in conjunction with the financial planners, we have a dedicated accountant who oversees all of the SMSF work, and works with your personal and superannuation fund accountants to ensure that we get the best result for you. CIPL devotes a lot of resources to getting this right, and all our work is externally audited by specialists.

If you have a self managed superannuation fund, you can be confident that it is being managed to the highest standards (our auditors won't allow anything less!). If you are thinking of setting a SMSF up, or know someone who might be interested, we can help you assess whether or not it is the right strategy for you.

Putting Names to Faces

In light of the recent staff changes at CIPL and our continued growth in staff numbers, we thought it might be a good time to tell clients a bit more about each person's role. And show you what they look like!

The Advisory Team



L-R Justin Baiocchi, David French, Sue Dunne and Bob Stewart.

The members of CIPL's Advisory Team develop your financial plans and ensure that all your financial planning needs are met and carried out. You can talk to any of them about your affairs.

David has overall responsibility for the portfolios, management of staff and recommendations on complex client matters.

Justin Baiocchi and Sue Dunne meet with clients, develop your Statements of Advice and provide ongoing strategic management of clients' affairs.

Bob Stewart has over 40 years experience in financial markets, and is responsible for running the Advisor Trading Centre (ATC). Bob's main role is to advise on and execute trades for clients who do not require ongoing financial planning advice.

The Compliance/Development Team



L-R Mike Greinke, Ben Scott, Robyn Donovan

Mike Greinke is Compliance Manager and ensures that we meet our statutory and legal obligations. Mike is a CPA with extensive experience in the Australian Taxation Office. He works with clients' accountants to make sure everything is up to date and accurate, and advises on client accounting/compliance matters.

Ben Scott is our IT Manager and is responsible for maintaining and developing the Portfolio Administration System (PAS). Ben also manages our proprietary software and our computer network. He helps clients with log-in and computer issues, and is responsible for improving the system.

As mentioned earlier, Robyn Donovan is working on the Property and Infrastructure Fund and is also responsible for developing new business. Her brief includes finding out what clients want, and addressing client concerns as they relate to our operations.

The Implementation Team



L-R Kathy Donaghey, Kathy Connolly, Bronwyn Large and Paul Donovan

Kathy Donaghey is our Senior Secretary and fulfils the reception role. You'll meet Kathy on the front desk or on the phone. Kathy directs your call to an appropriate person.

Kathy Connolly, Implementation Officer, is responsible for ensuring that administrative work associated with clients' financial affairs is correctly executed. Kathy works closely with the financial planners to correctly implement financial plans, and liaises with Centrelink, banks, superannuation funds and other external parties. You'll be lucky to not hear from Kathy from time to time.

Bronwyn Large is responsible for ensuring that all client transactions are properly recorded in the portfolio system. Bronwyn can help you with missed payments, data records, and following up on banking arrangements.

Paul's role is to ensure proper execution of client orders, and that CIPL's internal records are consistent with external data sources such as CHESSE. Paul works with stockbrokers and managed funds and collates research for use by CIPL.

Sandra French took the above photos, and is CIPL's book-keeper. She monitors CIPL's cash flows, organises invoicing and works with Mike to ensure that our financial resources meet ASIC requirements.

Investment Briefs

Here are some trading ideas for non-portfolio clients:

ANZ Banking Group Limited (ANZ)

ANZ's strategy over the past 5 years has focused on building up the Australian and New Zealand operations, with particular attention to personal banking operations, embracing the consumer sector. There has been

controlled expansion into Asian markets including China and Indonesia. A 5 year target is for Asian operations to contribute 20 per cent of group earnings, and for overall earnings to double in 5 years. The company reported a 13 ½ per cent fall in NPAT for the 6 months ended 31 March 2008. It followed up on 7 April 2008 with an announcement that debt provisions for the first half would exceed market expectations. These factors coupled with turmoil in global markets, and a generally gloomy economic outlook, have depressed the price of the stock to around \$19.00, with a yield of 7 per cent fully franked. ABN Amro believes that ANZ is cheap at these levels.

MacMahon Holdings Limited (MAH)

MacMahon has announced a \$100 million expansion and extension of contract mining work at Saraji Mine. This represents a near doubling of the annual revenue of the contract to around \$75 million, and takes the 2009 order book to above \$1.1 billion. In an announcement on 24 June, the company supported 2008 profit guidance of \$47 million, and indicated a 20-30 per cent profit growth target for 2009. UBS expects that 2009 will see both civil and mining divisions performing strongly. At \$1.70, the stock yields 2.35 per cent and is fully franked.

Mt. Gibson Iron Limited (MGX)

Rio Tinto and Baosteel have announced a settlement for contact iron ore prices for 2009. The fines benchmark price will increase by 79 per cent to 144.6 cents/mtu, and the lump price will increase by 96 ½ per cent to 201.69 cents/mtu. Mt. Gibson is arguably the biggest winner from the new price settlement, due to its higher lump/fines ratio compared to Pilbara producers. The impact of this has been to increase MGX's profit forecast - full year 2008, by 10 per cent and full year 2009 by 12 per cent. The valuation of the share comes to \$3.07, and the 12 month target price to \$3.50. At a market price of \$3.25, the stock carries an outperform recommendation from Macquarie.

Queensland Gas Company Limited (QGC)

The company announced that it expects to achieve reserves upgrades to be confirmed by the certifiers by 30 June 2008. The release of the expected reserves numbers ahead of actual certification is to allow disclosure in a bidders statement for its offer for Roma Petroleum Limited (RPM) previously reported. Basically QGC has exceeded a previous reserves target by 1/3, taking a key step towards approval of the Curtis LNG projection which it is a partner with British Gas (BG). QGC said it would boost reserves from 1317 PJ, to 2370 PJ, well above a previous target of 1800PJ. The share valuation is \$7.30, with a target price of \$6.19. Wilson HTM views it as a buy at the current price of \$5.15.

You are advised to seek advice regarding your particular situation before acting on anything contained herein.