



Fund Performance Commentary

Period: 1st to 30th June 2005

Fund Performance

The volatility in the Australian equity market presented us with buying opportunities. The NavTraDE system buys shares as share prices depreciate. Our cash holding at the end of June was 26.9% as we have taken the opportunity to sell shares at favourable prices. The actual returns in June for the Retail and Wholesale funds were +6.18% and +6.38% respectively compared to +4.17% return of the S&P/ASX200 Price Index. The returns for the past year were +22.93% retail and +22.74% wholesale compared to +21.08% for the S&P/ASX200 Price Index.

The NavTraDE system takes advantage of irrational investor behaviour to buy quality companies as their share prices are falling and to sell them as they are rising. Consequently, the system can realize capital gains from dealing in shares with volatile price movements, irrespective of the net price movement from the beginning to the end of the period. It takes time for shares to move through price cycles and therefore for the potential of the NavTraDE system to be fully realized.

The shares that performed well this month and generated realized capital gains through trading include Australian Gas Light Company (AGL), ANZ Bank (ANZ), Australian Share Exchange (ASX), BlueScope Steel (BSL), Macquarie Bank (MBL), Origin Energy (ORG), Santos (STO), Westpac Bank (WBC), and Woodside Petroleum (WPL).

The shares that performed well this month and generated unrealized capital gains include BHP Billiton (BHP), Coca-Cola Amatil (CCL), Futuris (FCL), Lend Lease (LNN), Orica (ORI), Paperlinx (PPX), Toll Holdings (TOL), and Wesfarmers (WES).

During the month, shares that detracted from performance either due to low volatility or because they were displaying unrealized losses include Publishing & Broadcasting (PBL).

The NavTraDE system resulted in increased weightings in: Paperlinx (PPX) and Coca-Cola Amatil (CCL).

The NavTraDE system also resulted in decreased weightings in: Westpac Bank (WBC), Macquarie Bank (MBL), The Australian Share Exchange (ASX) and ANZ Bank (ANZ).

To view our current portfolio, please [click here](#).

The Australian Share Market

The Australian equity market surged 4.17% in June (S&P/ASX200 Index), bringing the yearly return to a massive +21.08%, reflecting solid economic fundamentals. The Australian economy is now in the longest sustained growth period since Federation and was steady in the month of June.

Retail sales rose by 0.9% in May, more than reversing April's 0.5% decline. The sales increase was mainly due to a rebound in department stores sales (+9.1%) and clothing retailers (+4.5%) caused by heavy winter discounting to clear share. Both personal and business credit grew in May, while housing credit also rose by 1.0%.

The Australian share market rose 4.17% in June. Most major share markets also rose while the US share markets were flat.

The unemployment rate fell 0.1% to a new low of 5.0% in June, the 10th consecutive month of jobs growth. The participation rate also increased 0.1% to 64.7%. Encouragingly, full-time employment grew by 60,200 at the expense of part-time jobs.

The housing market continues to defy gravity: dwelling commencements fell by 2.2% in the March quarter but dwelling approvals rose 4.5% in May due to a 40% spike in Queensland. Commercial building approvals fell 14%.

The current account deficit widened in the March quarter to \$15.6 billion, up \$0.2 billion. The trade deficit was stable at \$1.6 billion in May, with higher export prices for coal and iron ore responsible for the 2% increase in exports value. Imports also rose 2% due mainly to higher fuel costs, solid domestic demand and a strong A\$.

In summary, the Australian real economy continued to grow, with the small rebound in the housing market continuing. GDP grew by 0.7% in the March

quarter though productivity growth continues to decline by 2.4% over the year. CPI was around 2.5% p.a. Interest rates were steady, and consumer confidence surged due to record unemployment, relatively low inflation and the announced tax cuts.

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The best performing sectors in June were Pharmaceuticals & Biotechnology (+14.5%); Energy (+13.6%); and Technology, Hardware & Equipment (+12.5%). Pharmaceuticals & Biotechnology and Technology, Hardware & Equipment were among the poorest performers the previous month.

The worst performing sectors were Media (-1.2%); Food, Beverage & Tobacco (+0.1%); and Software & Services (+0.5%).

The world economy remains strong, largely driven by the US economy.

The performances of the global share markets were mixed: The S&P 500 index was flat (-0.01%) while the Nasdaq fell 0.54%. The FTSE rose 3.01%, the Nikkei 225 rose 3.73% and the HangSeng rose 2.41%.

Business confidence in the US remains firm. Greenspan testified to the Joint Economic Committee that "the US economy seems to be on a reasonably firm footing, and underlying inflation remains contained."

GDP rose 3.8% p.a. in the last quarter. Industrial production rose 0.4% in May (or +2.7% p.a.) after falling 0.3% in April, mainly due to a rise in manufacturing production. Capacity utilization rose from 79.1% to 79.4% in May.

The unemployment rate fell 0.1% to 5.1% in May. Retail sales fell 0.5% following a 1.5% rise in April to be up 6.4% in the year. CPI fell 0.1% in May due to a 2% fall in energy prices. Annual CPI fell from 3.5% to 2.8%.

Housing starts increased 0.2% in May (+9.4% in April) to be up 1.8% for the year. Existing home sales fell 0.7% (+4.5% in April) or up 3.5% for the year. Median house prices rose 12.5% in the year. New home sales rose by 2.1% (-0.1% in April).

The current account deficit posted yet another record in the March quarter, rising from US\$188.4 billion to US\$195.1 billion. Import prices fell 1.2% in May (+1.2% in April) while producer prices fell 0.6% (+0.6% in April).

The Eurozone economy was relatively flat, with GDP for the March quarter rising 0.5%. CPI fell 0.2% to 1.91% p.a. Inflation fell 0.1% to 1.9% p.a. Unemployment remains high with Germany at 11.7% and France at 10.2%.

China is still the engine of world economic growth. Fundamentals look sound and bode well for continued GDP growth and demand for Western goods and Australian mineral imports.

The World Bank projects China's GDP growth of 8.3% and inflation of 3.5% in 2005. Fixed assets investment growth fell 17.2% p.a. in the March quarter. CPI remained at 1.8% p.a. in May, the lowest in 19 months. Retail sales rose 12.8% year-on-year in May compared with a growth rate of 17.8% for the same month last year and 12.2% for April this year. Urban retail sales rose 13.9% year-on-year, while rural retail sales were up 10.5%.

Industrial production grew at the fastest pace in three months in May, suggesting government investment curbs aren't working. Output rose 16.6% from a year earlier to a record 570 billion yuan (\$69 billion) after increasing 16% in April. However, earnings growth at companies listed on China's yuan-denominated A-share market fell to less than 10% in the first quarter, from 44% a year earlier.

Share Market Outlook

Economic growth is likely to remain around 3.0% due to healthy domestic fundamentals and the continuing strengths in the US and Chinese economies.

Economic fundamentals remain

The world economy is clearly slowing after growing by 5.1% in 2004, the fastest rate since 1976. However, the greatest risk to continued growth rests with the US economy, not only from its domestic consumption but also via demand for Chinese goods. The US growth rate is slowing with the GDP growth rate down to 3.8% in the March quarter from 4.4% in 2004.

The single biggest threat to the US economy is the burgeoning current account deficit, now at 6.3% of GDP and rising. Domestic demand growth has slowed, oil prices is rising again, and inflation is increasing. Consumer growth is driven more by income growth rather than by tax cuts and home

healthy for Australia. The May budget is very stimulatory and is positive for the share market through higher economic activity, reversing some of the negatives of recent months.

Inflationary pressures have moderated, but may increase due to the promised tax cuts and thus the likelihood of further interest rate rises in the latter half of the year remains strong.

Consumer demand remains high and the labour market appears healthy. The risk of a freefall in the housing market is low, and consumer sentiments, though trending down, appears firm.

The key drivers of global growth remain the US and China.

Most shares should benefit from the stimulatory effect of the 2005/06 budget, particularly the banks and retail sectors. Energy shares should benefit from high fuel prices.

equity drawdowns in the past year. The trade deficit is widening while productivity growth falls. However, the business outlook remains positive in the short term. Business confidence is strong with corporate net cash flow at near record levels. Employment remains at record lows. House prices, while moderating, remain high. Long-term interest rates have actually declined while the Federal Reserve raised short-term rates eight times in the past year.

In Australia, the tax cuts announced in the May 10th Federal Budget appears to be buoying a slowing economy. Inflation risk has been moderating as the economy cools. Retail sales are rising again and consumer confidence remains strong. The unemployment rate is at record lows, and the owner-occupied housing market appears remarkably resilient.

Export growth for minerals is still possible as resources companies expand operations as planned and bottle-necks are progressively eased. However, it is likely that the best growth period for resources companies is over as Chinese demand for raw materials moderate. The rural sector appears to be heading for a patchy drought in the Eastern states, dampening the prospects for some affected rural-based companies.

The drivers of the A\$ remains the US\$, Australian monetary policy and commodity prices. It is likely that the A\$ will fall slightly as the US continues to raise interest rates and demand for commodity falls in line with a slowing and rebalancing Chinese economy. This should aid exporters at the expense of importers. Revenues and profits for materials companies should continue to benefit from the substantial April price increases.

The likelihood of a significant downturn in the world economy is low. The outlook continues to be positive in the short to medium term. The global economy grew by about 5% in 2004, and is expected to grow by 3-4% this year. China's GDP growth is still expected to be around 8% and a soft landing is becoming more of a reality as the economy shifts from industrial investment to residential and consumer spending.

The risks to the world economy in the short to medium term are unforeseen spikes in the crude oil prices, the US current account deficit, a widening US trade deficit, and a sharp rise in interest rates should Asian appetite for US assets diminish, and a marked slowdown in the Chinese economy. Higher inflation in the US and China is likely to lead to modestly higher interest rates.

Most shares should reap the benefits of the budget stimulus. The banking sector should continue to benefit from high economic activity and productivity gains. It is likely that some negatives overhanging retail shares, particularly in the consumer discretionary sector, have abated. Energy companies should continue to benefit from high crude oil prices, utilities may benefit from investor speculation on interest rates, and transportation companies may benefit from continued high economic activity.

Negatives are expected from wine shares and companies associated with the rural sector. Steel companies may face pressure from Chinese exports due to slowing Chinese demand and recent capacity additions. Industrial shares are not particularly compelling as a sector.