



Fund Performance Commentary

Period: 1st to 31st of December 2004

The Australian Share Market

The Australian equity market continued to surge in November by 3.03% (S&P/ASX200 Index). The main factors driving the share market were largely unchanged from the previous month, namely strong domestic spending, record low interest rates and unemployment, and the continued strength of the US economy.

The Australian Dollar rose 1.05%, largely as a result of the weakness in the USD caused by investor concerns about the US twin deficits. Most of the commodity prices strengthened in the month and quarter. WTIS crude oil weakened 11.80% in December to US\$42.23/bbl while gold strengthened in the quarter due to the weakness in the USD.

The Australian share market continued to rise in December by 3.03% due to strong domestic spending, fiscal stimulus, record low interest rates and unemployment, and strong demand for Australian goods from a buoyant world economy.

The strong AUD (rising almost 3% in trade weighted terms) contributed to the widening of the trade deficit from \$2.37b in October to \$2.66b in November, the largest monthly deficit since April 2003. Exports were down 0.4% in November, with the 2% fall in rural products the main cause. Non-rural volumes increased, though negated by the rise in the AUD. Import volumes also strengthened, with consumption imports rising 0.9%.

Retail trade is still relatively strong, and rose by 0.1% in November, after a revised fall of 0.1% the previous month. Turnover was higher in food, up 0.5%, and household goods, up 1.3%. Department stores and clothing retailers recorded 1.6% and 0.8% lower turnover respectively in November. Hospitality and recreation volumes were also depressed.

The housing market is experiencing a slow correction, with dwelling approvals falling 0.3%, the smallest fall in seven months, compared to 1.0% fall in October. Private house approvals rose 0.9% compared to a 1.1% fall in October. The major correction has been in the apartment sector which fell 5.4%.

In summary, the Australian real economy is steady, with some signs of weakness in the overheated housing market. Interest rates were steady, and oil prices eased off from recent highs. Employment is still strong, with official unemployment at around 5.3%, a record low since 1978.

Retailing and Consumer Spending suffered a major reversal in December.

The best performing sectors in November were Food, Beverage & Tobacco (+7.9%), Pharmaceuticals & Biotechnology (+7.1%) and Insurance (+7.1%). The worst performing sectors in the month were Automobiles & Components (-32.3%), Consumer Durables & Apparel (-5.4%) and Retailing (-3.3%).

Non-cyclical shares benefited.

Solid performance was seen in Food & Drug Retailing (+7.7%), Capital Goods (+7.3%), Retailing (+7.1%), Media (+6.7%), and Consumer Durables & Apparel (+6.5%).

The world economy continued surging as global oil prices

The world economy continued surging in December. The major share markets all rose in the December quarter. WTIS crude oil

retreated.

The US economy remains strong due to strong employment, consumer demand and corporate investments.

weakened 11.80% in December to US\$42.23/bbl while gold strengthened in the quarter due to the weakness in the USD. The USD fell against most major currencies, associated with US structural constraints and investor concerns about the 'twin deficits'.

The US real economy continues to grow. Employment rose in December by 157,000, giving an annual growth rate of 1.7%. Unemployment was steady at 5.4%. The Federal Reserve raised official interest rates by 0.25% to 2.25%. The October trade deficit numbers came in at a record US\$55.5b, worse than expected, while the budget deficit widened slightly to US\$164.7b in the September quarter.

Other data suggest that the housing market is suffering slight weakness, personal incomes are slowly rising as personal consumption and retail sales ease. Industrial Production is slowly rising as Durable Goods orders also increased slightly by 1.6% in November. What is also salient is the consistent but modest rise in consumer sentiments in various indices. Core CPI is steady at 2.2%.

The UK economy appears to be stalling with disappointing economic data. The trade deficit widened to £5.3b in October from £4.4b in September. Manufacturing output and Industrial Production both fell, while the oil & gas sector shutdown did not take advantage of higher world prices. CPI is steady at around 1.3%.

The Eurozone economies remain soft, with forecast growth now cut from 2.5% to 1.9% for 2005. Inflation expectations also rose from 1.8% to 2.0%. The GDP growth estimates for Europe for 2004 are now expected to be 1.1% for Germany, 2.1% for France and 1.2% for Italy.

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

The Japanese economy is softening. Real GDP growth has slowed to 0.1% in the third quarter. Import volumes remained steady, while private consumption, business investment and exports have slowed markedly. The fate of the Japanese economy appears increasingly bound to exports to China and the US.

Official Chinese forecasts suggest GDP growth will drop back to 8.5% in 2005 following a 9.1% expansion this year due to a slow-down expected for both investment and exports. 2005 investment increase will be at around 18%, retailing sales is expected to increase by about 9.5%, exports by 15%, and CPI at 3-4%.

Approved Shares for the Navra Funds

The table below presents the list of approved shares that have passed our rigorous share selection process for inclusion in the Navra Funds. They may not be included in the current portfolio depending on a number of factors determined by the Investment Committee's weekly review.

Amcor Limited	AMC	Paper & Packaging
Australia And New Zealand Banking Group Limited	ANZ	Banking / Finance
Australian Gas Light Company	AGL	Infrastructure/Utilities
Australian Share Exchange Limited	ASX	Investment/Financial Services
BHP Billiton Limited	BHP	Diversified Resources
Bluescope Steel Limited	BSL	Building Materials
Boral Limited	BLD	Building Materials
Coca-Cola Amatil Limited	CCL	Food & Household
Fairfax (John) Holdings Limited	FXJ	Media
Foodland Associated Limited	FOA	Food & Staples
Futuris Corporation Limited	FCL	Foods & Household
Harvey Norman Holdings Limited	HVN	Retail

Lend Lease Corporation Limited	LLC	Developer/Contractors
Lion Nathan Limited	LNN	Alcohol / Tobacco
Macquarie Bank Limited	MBL	Banking / Finance
Macquarie Infrastructure Group	MIG	Infrastructure/Utilities
National Australia Bank Limited	NAB	Banking / Finance
National Foods Limited	NFD	Foods & Household
News Corporation Limited	NWSLV	Media
Orica Limited	ORI	Chemicals
Origin Energy Limited	ORG	Infrastructure/Utilities
OneSteel Limited	OST	Building Materials
Paperlinx Limited	PPX	Paper & Packaging
Publishing & Broadcasting Limited	PBL	Media
Qantas Airways Limited	QAN	Transport
Rio Tinto Limited	RIO	Diversified Resources
Santos Limited	STO	Infrastructure/Utilities
Sims Group Limited	SMS	Materials
Tabcorp Holdings Limited	TAH	Consumer Discretionary
Wesfarmers Limited	WES	Diversified Industrials
Westfield Group	WDC	Property
Westpac Banking Corporation	WBC	Banking / Finance
WMC Resources Limited	WMR	Diversified Resources
Woodside Petroleum Limited	WPL	Energy
Woolworths Limited	WOW	Retail

Since inception the number of shares in the portfolio has increased from 20 to 35 shares in order to provide more diversification. Please [click here](#) to view the current portfolio.

Fund Performance

The volatility in the Australian equity market presented us with buying opportunities. The NavTraDE system sells shares as share prices appreciate. Our cash holding at the end of December was 33.6% as we have taken the opportunity to sell shares at favourable prices.

The actual returns in December for the Retail and Wholesale funds were 3.31% and 3.29% respectively as compared to 3.03% return of the S&P/ASX200. The performances for the quarter were 11.44% and 11.21% for the Retail and Wholesale funds compared to 10.52% for the benchmark.

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 realised.

The shares that performed well this month and generated realised capital gains through trading include Foodland (FOA), Publishing & Broadcasting (PBL), Lend Lease (LLC), Macquarie Bank (MBL), ANZ Bank (ANZ), News Corp (NWSLV), Orica (ORI), Qantas (QAN), Australian Share Exchange (ASX), and Futuris (FCL). The shares that performed well this month and generated unrealised capital gains include Australian Share Exchange (ASX), Amcor (AMC), Futuris (FCL), Macquarie Bank (MBL), National Australia Bank (NAB), News Corp (NWSLV), Qantas (QAN), and Westpac Bank (WBC).

During the month, shares that detracted from performance either due to low volatility or because they were displaying unrealised losses include BoraL (BLD), Bluescope Steel (BSL), Harvey Norman (HVN), Origin Energy (ORG), and Woodside (WPL). In December Futuris (FCL) was added to the portfolio.

The NavTraDE system resulted in increased weightings in: Woodside (WPL), Santos (STO), and Tabcorp (TAH). The NavTraDE system also resulted in decreased weightings in: Foodland (FOA), Publishing & Broadcasting (PBL), and News Corp (NWSLV).

Share Market Outlook

Australian economic fundamentals appear sound and interest rate pressure has reduced due to a softening housing market and consumer spending. Inflation expectations are around the middle of the RBA range as oil prices ease and the rise in the AUD has tempered. The market seems to have priced in a rate cut sometime in February. The strong AUD is having a negative impact on exporters, including miners, and a positive impact on importers, providing the impetus for the recent record balance of trade figures.

Strong global growth continues to drive demand for Australian commodities. The US economic outlook remains positive. Real consumer expenditure remains resilient and combined with strong growth in capital goods orders and housing starts, should see a solid rebound in the GDP to near 4%, notwithstanding a weakness in net exports. The labour market outlook is positive, and with strong corporate profitability and cash flows, the outlook for capital spending is positive.

Economic growth likely to remain near 3.25% due to healthy domestic fundamentals and the continuing strengths in the US and Chinese economies.

The pace of Chinese economic growth is expected to slow, although demand for imports should still support global commodity prices. Official 2005 forecasts suggest a CPI of 4% fiscal revenue will rise by 14% compared to 21% this year. China's GDP growth is likely to be around 8%, slightly down on 8.8% this year. Consumption is expected to increase by 13% supported by higher urban and rural incomes. Chinese imports of Asian goods are buoying the Asian economies and the risk of a hard landing remains, particularly for Japan and South Korea.

Japanese economic prospects are weakening as leading indicators suggest. Bank lending is still negative, suggesting an extended growth period would be unsustainable even if corporate cash flows improve. Real GDP has slowed to a trickle, and official forecast is for GDP growth of only 1.2% in 2005 compared to 2.8% in 2004. Japan's long-term structural constraints remain unabated.

The outlook remains positive for the global economy, though less positive than for the past 2 years. A modest slowdown in the US economy may occur, but with still low (though rising) interest rates, a relatively modest unemployment rate, and continued East Asian governmental appetite for US assets, it appears that a major downturn in the US economy is unlikely in the short to medium term. There is also increasing signs that the Chinese economic growth rate can be maintained, providing a continued stimulus to commodity prices.

However, it is possible the major risk posed by the Asian tsunami has not been fully factored by the market, and may lead to further volatility in the share markets.

The key drivers of global growth remains the US and China, with the addition of unknown variables brought by the Indian Ocean tsunami.

The risks to the world economy in the medium term are unforeseen spikes in the crude oil prices, the US current account deficit (running at 5.1% of GDP), a widening trade deficit, and a sharp rise in interest rates should East Asian appetite for US assets diminish (especially through internal shocks), and a slowdown in the Chinese economy. A further unknown is the medium term effect of the Asian tsunami. A short term boost to productivity is likely as replacement industries benefit from the rebuilding process. However, this may lead to higher credit growth, and depressed economic conditions in the Indian Ocean/East Asian region in the medium term.

We forecast continued strength in resources shares and companies deriving high earnings from overseas markets, particularly in the US and China.

Consumer spending is likely to trend downwards post the Christmas spending season.

Due to these facts, we forecast continued strength in resources shares and companies deriving high earnings from overseas markets, particularly in the US and China. In view of a possible softening in the consumer spending sector, we forecast a slight decrease in the price performance of domestic cyclical shares and retail shares. However, intrinsic factors (e.g. petrol discounting and/or corporate activity) may support the prices of the major retail chains such as Coles Myer and Woolworths.

We also forecast a slightly increasing price performance in the industrial shares leveraged to cyclical sectors and companies with quality earnings and high sustainable growth.

In our opinion a strong domestic economy and continued growth of the global economies, the share market is expected to do well in the coming months. As NavTrade exploits such short-term volatility to add value, we are positive for the fund in the coming months.