

Period: 1st to 30th June 2006

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 17.5% as we have taken the opportunity to buy stocks at favourable prices. The actual returns in June for the Retail and Wholesale funds were +2.48% and +2.49% respectively compared to the +1.44% return of the S&P/ASX200. The returns for the June quarter for Retail and Wholesale funds were +3.33% and +3.33% respectively compared to the -1.09% return of the S&P/ASX200.

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 stocks that performed well this month and generated realized capital gains through trading include Bluescope Steel (BSL), Lion Nathan (LNN), Macquarie Bank (MBL), National Australia Bank (NAB), OneSteel (OST), Publishing & Broadcasting (PBL), Toll Holdings (TOL), Westpac Bank (WBC), and Woolworths (WOW).

The stocks that performed well this month and generated unrealized capital gains include The ANZ Bank (ANZ), BHP Billiton (BHP), Bluescope Steel (BSL), Lion Nathan (LNN), Macquarie Bank (MBL), OneSteel (OST), Westfield (WDC), and Woolworths (WOW).

During the month, the shares that detracted from performance either due to low volatility or because they were displaying unrealized losses were Futuris (FCL), Origin Energy (ORG), Orica (ORI), Origin Energy (ORG), Publishing & Broadcasting (PBL), Santos (STO), Tabcorp (TAH), Toll Holdings (TOL), and Woodside (WPL). There were no inclusions or exclusions to the portfolio.

The NavTraDE system resulted in increased weightings in: National Australia Bank (NAB), Westpac Bank (WBC), BHP Billiton (BHP), Fairfax (FXJ), and The ANZ Bank (ANZ).

The NavTraDE system also resulted in decreased weightings in: Origin Energy (ORG), Woolworths (WOW), Futuris (FCL), Bluescope Steel (BSL), Westfield (WDC), Orica (ORI), and Coca-Cola Amatil (CCL).

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

The Australian Share Market

The Australian equity market rose by 1.44% in June (S&P/ASX200 Index), recovering slightly from the 4.9% correction in May.

The Australian stock market rose by 1.44% in June after the May correction.

The Australian economy's growth continued in June with mixed economic data. The RBA left official interests at 5.75% despite a strong rebound in the housing market. Loan approvals rose 4.7% in May (private housing loans rose 1.2%). Building approvals rose 3.3% in May to be 11.7% down from a year ago.

Economic data released were mixed: the housing market recovered; the jobs market is still healthy; but retail sales fell due to high oil prices.

The May unemployment rate fell to a 30-year low of 4.9% from a restated 5.1% in April, mainly driven by a jump in full-time employment and a fall in the number of job-seekers. It is likely that jobs growth in June will slow as indicated by a drop in job ads by 3.3%.

Commodity prices fell during the month, except for crude oil, and should result in a weaker trade balance.

Retail sales fell 0.3% in June due to high oil prices (although still 5.3% higher than last year). The ratio of essential vs discretionary spending is increasing. High oil prices are also impacting car sales, with new vehicle sales down 0.5% in May and down 3.2% for the year.

The June balance of payment will be affected by a general pullback in commodity prices due to concerns about the US economy. All major commodities except crude oil fell in the month.

In summary, the Australian economy remains relatively sound. Some inflationary pressures are becoming apparent, particularly with the flow-on effects of high petrol prices. Consumer confidence weakened. Employment growth is slowing as is productivity gains. However, the housing market is recovering from the mild downturn of previous months.

The best performing sectors were Diversified Financials and Consumer Durables & Apparel.

The best performing sectors in June were Diversified Financials (+6.58%); Consumer Durables & Apparel (+4.75%); Real Estate (+4.51%); and Food & Drug Retailing (+3.80%).

The worst performing sectors were Hotels Restaurants & Leisure (-2.83%); Telecommunication Services (-2.21%); and Transportation (-1.42%).

Global stock markets continued the slide from May with the MSCI index slipping 0.2%. The S&P 500 was steady, the Nasdaq fell 0.3%, the FTSE rose 1.9%, the Nikkei 225 edged up 0.2% while the HangSeng recovered by 2.6%. All other major European stock markets fell. Over the past 12 months the MSCI index has risen 14.9%, even after the May correction.

World markets were down up in June due to concerns of inflation and stalling US economic growth.

All major commodities except crude oil fell: gold fell 4.1% while crude oil rose 3.5%. All the base metals fell, led by zinc 16.6%. This was due to concerns of a slowdown in the US economy flowing to lower imports and hence lower Chinese growth.

The US economy is showing signs of dampening, even as the jobs market is steady. Retail sales figures are soft, inflationary pressures are accumulating and the housing market is losing momentum.

The US stock markets were cautious in the month due to concerns about inflation, a cooling housing market, and a slowing economy. The US real economy had been showing signs of cooling for a few months. The unemployment rate was steady in June at 4.6%, with little or no change for the past two months, compared to 5.0% in June 2005. Average hourly earnings have risen 3.9% in the past year.

The US housing market signals were mixed in May. House sales rising 4.6% after a fall of 2.0% in April, yet down 6% from a year ago. However, existing home sales have fallen for the seven of the past eight months. Median prices fell 4.3% in the month. Housing starts have dropped in three out of the past four months. Overall construction spending, meanwhile, sank 0.4% in May - the biggest monthly decline since September 2004, while inventory is the highest on record.

High gasoline prices and the recent East Coast floods are dampening the retail market: retail sales rose 0.1% after a revised 0.8% rise in April. Excluding gasoline, retail sales actually fell 0.1% in May. Auto sales were a major factor; excluding auto sales retail sales rose 0.5%. A leading survey shows retail sales, excluding autos, recovering to 0.4% in June.

On June 5, Ben Bernanke, the Fed Chairman, warned of inflationary pressures, leading to a rout on the stock markets. US inflation seems to be at the top end of a price-stability zone. Core inflation rose 0.2% in May but inflation-adjusted spending grew only 0.1% due to the impact of high gasoline prices on disposable incomes. Growth in personal income also slowed, rising 0.4% in May, down from a 0.7% increase in April.

China is still the powerhouse of world economic growth. Fundamentals look sound and bode well for continued GDP growth although demand side concerns are increasing.

The trade deficit rose after two months of declines to be up 2.5% in April and is expected to widen in May due to high energy prices and a slowing economy.

As a lagging indicator the March quarter GDP grew 5.6% p.a., propelled by a surge in consumer spending. The June quarter figures are expected to show a different result.

Chinas economic news are also most positive and the expectation is rising of a GDP growth of 10%+ in 2006. The economy grew by 10.3% in the March quarter, surpassing the official target of 8%. China's surging trade surplus reached a monthly record high of \$14.5 billion in June. Bank lending also surged in the past six months although slipping 22% in May due to government intervention. All economic indicators suggest previous official GDP growth forecast of 9.0% to be pessimistic, although risk factors are increasing.

Share Market Outlook

Australian economic fundamentals remain sound. Inflationary pressures are slowly increasing. Economic growth is likely to remain around 3% due to healthy domestic fundamentals and the continuing strengths in the Chinese economy.

The labour market appears buoyant but may have passed its peak. Consumer confidence has slipped due to high oil prices.

Global stock markets are entering a period of increased volatility as the US economy slows.

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

The world economy is heading for a period of cautiousness on the back of concerns about global inflation and slowing US economy. Chinas economic growth appears unstoppable in the short term. However stock prices are factoring in a longer term fall in demand for raw materials.

The Australian economy is still relatively strong, with relatively low inflation, high unemployment, and a robust housing market, driven by the strong resources sector. However, the risks of a further interest rate rise have increased with the rebounding of the housing market. Continued high oil prices are starting to affect consumer confidence. Nevertheless, business investment remains strong particularly in mining, transport and construction. The recent bulk commodities price negotiations were positive and should lock in high profits for mining companies in the next twelve months.

The US economy is now showing signs of weakness due to rising inflationary pressures despite almost three years of tight monetary policy, softening consumer confidence, high fuel prices, and negative savings in the face of a falling housing market. It is likely that the US economic growth will moderate to about 2% in 2007 from 3%+ in 2006. Unemployment may rise as consumer spending moderates and the excess in housing stocks are reduced. Manufacturing is likely to see further cost pressures if world oil prices continues to remain high. As demand from China and India continues to grow as their economies develop, it is likely that high crude oil prices will begin to offset the benefits of cheap Chinese imports.

The impact of a slowing US economy has not begun to bite in the global real economy, although this has seen increased volatility in world stock markets. Continued growth in developing countries may take the edge of a slowdown in the US economy. Europe's growth is slow but relatively steady. Unemployment is at recent lows though inflationary pressures are increasing. GDP growth should be around 2% in 2006. Japans growth is now at its strongest in years and there are some expectations that the Bank of Japan may lift interest rates to positive. However strong business confidence, consumer confidence in Japan is still weak due to declining wage costs.

The outlook for the Australian equity market is positive in the short term as the resources and consumer sectors continue to support the rest of the economy. However, we may be entering a period of uncertainty and hence more marked stock market volatility. Present weaknesses in the stock market are driven mainly by concerns over global stock over-valuations and fears of global inflation and should present buying opportunities. The housing market is rebounding. The unemployment rate is low and should support domestic consumption. The interest rate outlook is still relatively benign although on a mild tightening bias. Further rate rises are possible due to the expansionary effects of the budget and a resurgent housing sector but should remain historically benign.

It is probable that Chinas growth will continue for the foreseeable future due to its present early position on the growth cycle. China's demand for world commodities and consumer goods is driving growth in other global regions, stimulating turnarounds in Japan and Europe. Concerns about the sustainability of US economic growth and inflationary pressures are beginning to flow through to global stock markets. Although any real economic flow through of weaker US demand will take place in the medium term, we expect to see further stock market volatility.

The risks to the world economy in the short to medium term have increased albeit slightly. The likelihood of a significant downturn in the world economy is low. The outlook continues to be positive in the short to medium term. It is becoming clearer that high oil prices a more probable scenario as the Chinese economy grows beyond expectations and global supply remains constrained.

Resources companies may benefit from rising production and prices. Banks should benefit from continued economic growth.

Ongoing problems are expected in the telco sector and industries affected by high fuel costs.

With export performance now an even greater driver of the Australian economy, export-oriented sectors, in particular Resources and Energy, should see further share price rises. Sectors able to harness general economic activity such as Banks and Infrastructure should also benefit. The wealth effects of buoyant housing and equity markets should support Materials companies, and the resurgent consumer confidence is likely to boost retail companies, particularly through the expansionary effects of the Federal Budget. Weakness in the consumer sector could result from continued high oil prices.

Manufacturing and telecommunication should remain relatively weak. Airlines, transportation companies and tourism related industries could face cost pressures from high oil prices. The rural sector remains unappealing.