

CI BRUNSWICK FUND QUARTERLY REPORT



Cooper Investors Pty Limited AFS Licence Number 221794 ABN 26 100 409 890

DECEMBER 2007

"Nature does not hurry, yet everything is accomplished" Lao Tzu

"The superior man does not waste himself on what is distant, on what is absent. He stands in the here and now, in the real situation" Confucius

PORTFOLIO & MARKET PERFORMANCE

	BRUNSWICK FUND**	UBSA BANK BILL INDEX	UBS COMP BOND INDEX	S&P ASX 200	MSCI HEDGED#	HEDGE FUND INDEX*
3 MONTHS	-0.14%	1.7%	0.3%	-2.7%	-3.1%	0.3%
FYTD	1.73%	3.41%	1.74%	3.00%	-2.16%	-2.33%
2007*	36.6%	6.4%	4.0%	28.7%	22.9%	12.7%
2006*	26.6%	5.7%	3.4%	23.9%	16.3%	7.8%
2005*	36.1%	5.6%	7.8%	26.3%	10.9%	1.1%
SINCE INCEPTION ⁰	28.12%	6.1%	4.8%	23.2%	13.4%	5.5%
SINCE INCEPTION [^]	138.12%	23.0%	17.9%	107.5%	55.1%	20.5%

* Financial year to 30 June

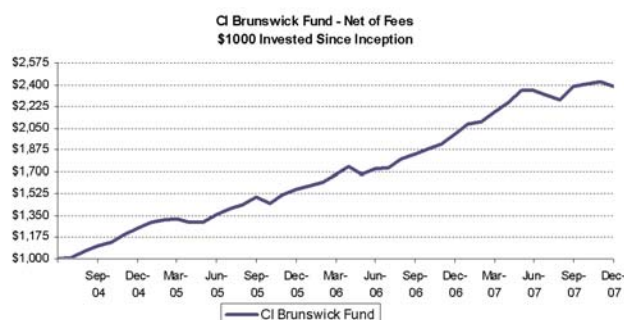
** Net performance - after management and performance fees and expenses

⁰ Annualised

[^] Cumulative since the CI Brunswick Fund was launched on 1st July 2004

^x HFRX - Hedge Fund Research Index (representing returns from hedge funds)

[#] MSCI hedged to AS (representing returns on international equity markets)



Over the December quarter the Australian stock market fell by 2.7% and the global markets fell by 3.1%. This was the second quarter in the last five years that the Australian market fell. Volatility was again high as the markets absorbed the continuing bad news from the sub prime crisis. Bond yields continued to rise in Australia and like the stock market fixed interest returns were poor. Property prices fell as capitalization rates rose and the Australian listed property market had its worst quarter for 10 years falling 13%. Cash and some of the Asian markets were the only investment classes to show positive returns. The Australian dollar also fell by a couple of percent.

The fund returned -0.1% for the quarter and 19.2% for the year to December 2007(after fees and expenses).

By far the best stock in the quarter was Rio which rose by 25% following rises in profit forecasts and the proposed takeover by BHP. Other stocks that performed particularly well included BG (+15%), Standard Chartered (+10%), Oil Search (+12%) and some smaller stocks including Real Estate.com, Australian Agricultural Company and Plan B. For the first time our short positions added significant value of close to 1%.

The cash weighting averaged 10% over the quarter and provided some stability to the portfolio.

On the negative side, Trinity, a Queensland based property company fell by around 20% and Brambles fell by around 20%.

The portfolio has an equity exposure of 85% of which 12.8% is in overseas stocks, the cash weighting is 15% and this is mostly held in bank bills. There is no exposure to fixed interest or any unlisted securities. The short positions are 6.1% of the portfolio and about half of the international currency positions are hedged back to the Australian Dollar.

More detail on the portfolio is set out below.

The objective of the Brunswick Fund is to produce long term returns that are above general equity market returns. The fund should be considered an equity based fund. We do however have a lot of flexibility in how the portfolio is invested.

Our intention is to offer a real value proposition to our unit holders that is quite different to the standard institutional products that are available and to give the fund the best chance of delivering very good returns.

The Brunswick Fund has three differentiating features that we believe enable it to deliver very good returns over the medium term and make a difference for unit holders.

The first is through the portfolio having very broad investment parameters that have no institutional style rules and constraints. The portfolio can invest in international markets, in non equity asset classes and can use shorts and gearing. Thus the portfolio should be invested where we see the opportunities rather than by reference to benchmarks and other institutional style descriptors.

The second is the use of Cooper Investors (VOF) investment approach, this approach has proved very successful in the Australian market and we believe is transferable to other markets and in fact other asset classes.

The third aspect is that Cooper Investors has invested heavily in building up its international equity knowledge and we now have three full time people investing in offshore markets. The Brunswick Fund can consider the ideas and information generated in the international funds and evaluate these against the knowledge we have on the Australian markets.

At a minimum the Brunswick Fund has the opportunity to perform very well. Over the past three and a half years the fund has performed well however we would point out that markets have also been very strong over this period.

Applying Cooper Investor's VoF investment philosophy without reference to indices, benchmarks, institutional style descriptors or portfolio construction rules that apply to institutional equity funds.

We accept volatility as being the cost of participating in investment markets that we expect to deliver long run returns.

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CURRENT CONDITIONS

We believe it will be much more difficult for the Australian stock market to deliver the high returns experienced in the past three years during 2008. This is a more downbeat view than we have expressed previously. The reason is that a number of negative factors have developed over the past year.

We have previously observed that many companies were experiencing serious input cost pressures. This pressure at company level has now moved into consumer prices and we think it is inevitable that the consumer price index will move above the Reserve Banks medium term target range of 2-3% per annum. Many of the volatile items such as food and energy look to be moving into long term uptrend as opposed to cyclical uptrend. Links between the oil price and food prices are increasing and it is a certainty that the pricing of carbon will lead to higher electricity prices. In addition it now seems clear that the long period of China exporting lower prices to developed economies has finished. If these price rises start to move through into compensating higher wages growth then high company margins will be further pressured. With the economy at full employment, with profit margins at record high levels and with changes to the industrial relations law to come the risk of lower profits in some sectors of the economy is real.

The next point is that the sub prime crisis in the US is now having implications in the Australian economy. The most obvious example is the collapse of the Centro business model where the cost and availability of debt deteriorated to the point that the stock price fell 70% in one day. The implications of this event are profound and will roll through seemingly unrelated areas over the next six months. Another major impact is that the cost of borrowing by all companies, including banks, has risen quite sharply. It now seems likely that there will be downgrades to bank sector profits during 2008. The finance and property trust sectors represent 39% of the Australian stock markets capitalization. If these sectors struggle it is impossible for the market as a whole to do well.

The third main point is that the behaviour of listed companies in 2007 has deteriorated. Previously we stated that Australian boards and management were generally running companies well and doing a good job for shareholders. We now feel that the number of companies doing a good job has diminished.

These points are made against an equity market background of historically high return on equity, high profit margins, low share of GDP going to labour and high and rising debt levels.

CORPORATE AUSTRALIA

While most of the issues mentioned above are well understood and have been increasingly discussed, the credit crisis has exposed some company's business models and strategy. Despite this the actions of corporate Australia have not changed despite these obvious negative changes in operating conditions.

For example:

- There was merger and acquisition activity right up to the end of 2007 that appeared marginally value adding at best
- M&A pricing is still being run on last years pricing metrics
- Share buy backs continue across the board
- Capital is not being treated as a scarce resource by companies.
- Executive and Board remuneration is rising unjustifiably sharply

- Companies are still normalizing out most negative aspects in results
- Spin is abounding with only the upsides ever being mentioned in briefings

Some examples of less favourable outcomes are discussed below.

Bendigo Bank had the strongest balance sheet amongst the Australian banking sector. Its loan to deposits ratio was by far the lowest, its culture the most conservative and identifiable and its brand was the strongest. Despite these attractive features Bendigo paid a premium to purchase Adelaide Bank and the combined entities balance sheet now looks similar to all the other banks.

SP Ausnet agreed to purchase the very highly priced infrastructure assets (the infamous Alinta assets) from its parent despite an obvious change in market pricing for such assets. Sp Ausnet continued to pursue this acquisition right up until the point when it becomes clear that the EGM resolution to approve the purchase would be voted down.

Transfield Services Infrastructure fund outbid Babcock and Brown in buying a portfolio of wind farms despite unit holders having an expectation that this fund is different and will add to its portfolio outside the highly competitive energy sector.

Out of the blue NAB buys a small bank in the mid west of the USA.

AGL shocks the market with prices paid for assets early in 2007. Following the profit downgrade and departure of the MD the recent review by KPMG reports that "assumptions were at the upper end of probable outcomes and therefore overly optimistic".

Allco buys Rubicon in a related party transaction. Rubicon is the manager of underperforming property trusts whose DNA includes massive use of debt.

Lend Lease and Mirvac confirm they are talking about potential transaction. This is surprising from a Lend Lease perspective as a value proposition is not evident.

Why has behaviour not changed?

A major reason is that many companies have lost their commercial savvy streak. How many companies actually have a capability to evaluate M&A opportunities internally? How many companies have Directors who can take a medium term decision, can reject propositions from management, can reject recommendations from advisers and question ratings agencies?

Management and boards do not respect the quality of existing company assets enough compared to the lure of alternative assets offered to them. For instance Bendigo Bank did not value their existing business and culture sufficiently compared to the Adelaide business they ended up buying.

Many companies are still using overly optimistic assumptions in their budgeting and investment evaluations.

A real but unsavoury reason for some over optimistic corporate behaviour is that some management teams know that their stock prices and prospects are overrated and therefore while their scrip has value they are compelled to keep dealing, moving and muddying the waters so that they are not exposed.

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Finally and most important of all is that many companies undertake strategic M&A as opposed to value M&A. For instance the Bendigo acquisition of Adelaide bank was all about a 20 year strategy rather than the current value proposition. AGL's over priced acquisitions last year were also all about strategic positioning rather than value. We are entering a period when strong companies will be able to buy both strategically and at very low prices from weakened companies.

The time when most company boards do act decisively is in a crisis that is so obvious that inaction places their own reputation at risk.

When we travel overseas we find many companies who have faced extremely harsh operating conditions in the recent past and have adjusted their businesses and attitudes to survive. These survivors often perform very well when their internal rationalisations are completed and their operating conditions improve. It seems to us that there are better opportunities to buy large, well performing companies at cheap or fair prices overseas than in Australia at present.

On a more positive note there are many excellent management teams in Australia. If conditions do remain tougher there will be opportunities for these teams to add significant value. In recent years there have been some fantastic corporate transactions such as a number of QBE purchases, the Incitec Pivot acquisition of Southern Cross Fertiliser and some of the sales of media assets to private equity groups. We would expect the differential in management teams to be more accentuated in the next year.

Additional comments on the portfolio

International stocks

The proportion of the portfolio held in non Australian stocks has risen to around 12.5% of the portfolio. Over the past year the international stocks in the portfolio have performed ahead of the Australian market.

The portfolio owns four Asian bank stocks. In the March quarterly report we wrote a detailed piece on why we felt that Asian banking stocks were a far more attractive investment proposition than owning Australian banking stocks. The four stocks we own have all performed strongly and as a group have done significantly better than the Australian banks. The sub prime crisis has had little impact on the Asian banks because they held little or no sub prime debt securities and have more deposits than loans and therefore are not impacted by widening credit spreads on corporate borrowings.

The other two stocks, BG in the UK and Trust Power in New Zealand are in the energy sector, when combined with Oil Search and BHP they provide the portfolios direct energy exposure.

In the past we felt that Australian stocks offered a more positive investment proposition than international stocks however we now feel that the relative attractiveness of the Australian market has diminished significantly and therefore we are likely to increase the weighting to international stocks. While there are no definitive guidelines a weighting of up to 30% of the portfolio under current conditions is reasonable.

We are confident that with a dedicated team focusing on the international sector and a common investment methodology and set of core beliefs, the BF will be able to successfully evaluate international ideas against the Australian opportunity set.

Cash and fixed interest

The portfolios cash weighting is currently around 14%, most of which is held

in short dated bank bills. There is no holding in longer dated fixed interest.

We have invested most of the cash weighting in Australian bank bills because the bill rate of around 7.25% is at a historically high margin compared to the cash rate of 6.75%. Cash held with the custodian earns less than the cash rate so the pick up in yield for no additional risk is substantial. The bank bill market is very liquid so there is no penalty if we need to sell the bills to fund other investments.

We have not held any longer dated fixed interest investments because we have been concerned about rising inflation and until recently the very low interest spreads on corporate risk. We feel long dated bonds and corporate paper remain unattractive but shorter dated Government bonds are more attractive today.

Shorting:

The BF has had up to 8% of its asset value in short positions but generally has held more modest positions of 2-4% short. The experience to date has been positive but mixed.

Over the past two years we have held a number of short positions that were based on the stocks high valuation as opposed to the stocks fundamental quality. These positions have not added value and have led us to conclude that at the moment overvaluation alone is not enough of a reason to go short.

Earlier this year we had a couple of short positions in stocks we felt were fundamentally unattractive but not badly run. In one instance shortly after closing out the position a private equity bid for the company and the share price rose sharply. The conclusion from that experience was that in a market environment where there is a high tolerance for risk tolerance shorting can be very dangerous. In this regard the environment is changing though.

We have had one very successful short position recently where the basis of the position was the riskiness of the company's business model and disclosures rather than the valuation itself.

The conclusion from these experiences is that the ability to short stocks has a legitimate place in the BF toolkit but as is always the case there is no single formula that works over time.

We have included below comments from one of our global fund portfolio managers on obesity and diabetes. While the Brunswick Fund does not own any overseas pharmaceutical stocks at present it is an area of interest.

Allan says is a section dedicated to the research we have conducted in the previous three months.

"Allan says... Bigger snacks mean bigger slacks!"

"Never eat more than you can lift" –Miss Piggy

Once again we cannot doubt Miss Piggy's wisdom as the harsh realities of our lifestyle catch up with our waistlines. Classified as a disease which is defined as any deviation from the normal structure of any body part, obesity diminishes both quality of life and life expectancy. It is also a common risk factor for a number of diseases from diabetes to heart disease and some types of cancer. This Allan says will focus on the impact that rising obesity levels are having on the prevalence of diabetes, in particular type 2 diabetes. Type 2 diabetes comprises 90% of the diabetes population and is described as a 'lifestyle disease' compared to type 1 diabetes, or juvenile diabetes which is commonly thought to be a genetic disease.

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According to the International Diabetes Federation obesity and type 2 diabetes are causally linked. Weight gain leads to insulin resistance through several mechanisms. Insulin resistance places a greater demand on the pancreatic capacity to produce insulin, which also declines with age, leading to the development of clinical diabetes. Physical inactivity, both a cause and consequence of weight gain, also contributes to insulin resistance.

The increase in obesity is a global problem, with the spread of western lifestyles impacting all regions, particularly Asia-Pacific. It is expected that 70% of new diabetes patients will come from developing countries as increasing income and urbanization leads to rising obesity levels. China has recently overtaken the US as the fastest growing diabetic population.

Globally more than 1.1 billion people are overweight where overweight is defined as having a body mass index between 25 and 30 for an adult, while 400 million people are obese which means having a body mass index greater than 30. That is approx 20% of the global population is overweight and more than 6% are clinically obese. Currently the number of diabetics is at 250 million people which means that 60% of obese people end up contracting diabetes. More than 1/3 of the US population is clinically obese!

There are several reasons for the fast progression of obesity and diabetes, however, increased calorie intake and/or lowered energy expenditure are the key aspects. Fat consumption per capita in the US has increased by 25% in the last 50 years to 145 grams fat consumed per capita per day. This compares to the FDA recommendation that daily fat intake for a typical adult should not exceed 65 grams. Compounding the situation is a less active lifestyle driven by an electronics age. Consequently the number of diabetics has grown from 110 million in 1994 to almost 250 million in 2007, a growth rate of 6.4% p.a.

Novo Nordisk, a specialist pharmaceutical company based in Denmark is a world leader in diabetes care. It has a 53% share of the global insulin market and has the broadest diabetes product portfolio. Novo is highly focused on diabetes care with 75% of revenue coming from diabetes care products. The remaining 25% of revenue is generated by Novo's specialized biopharmaceuticals division where they have leading positions in coagulation disorders, growth hormone disorders and hormone therapy for women.

There is a time lag of 5-7 years from when a patient is diagnosed with diabetes to becoming a Novo patient. When a type 2 diabetic patient is diagnosed, the normal procedure is a tablet treatment that helps insulin production or sensitivity. This type of treatment goes on for several years, but with unchanged habits in terms of diet and exercise, the body will slowly be unable to produce insulin by itself and insulin injections are needed instead. Current Novo patients are mostly those who had diabetes diagnosed in 2000 and earlier. Novo expect to see an increasing number of insulin patients over the next 5 to 10 years as the patients diagnosed with diabetes post 2000 will move from the tablet to Novo's leading insulin injections.

Novo is uniquely positioned to benefit from attractive industry fundamentals supported by its strong market position. We expect Novo to deliver consistent earnings growth above the industry average.

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