

CI BRUNSWICK FUND QUARTERLY REPORT



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

MARCH 2010

“Many a false step is made by standing still.” Anonymous

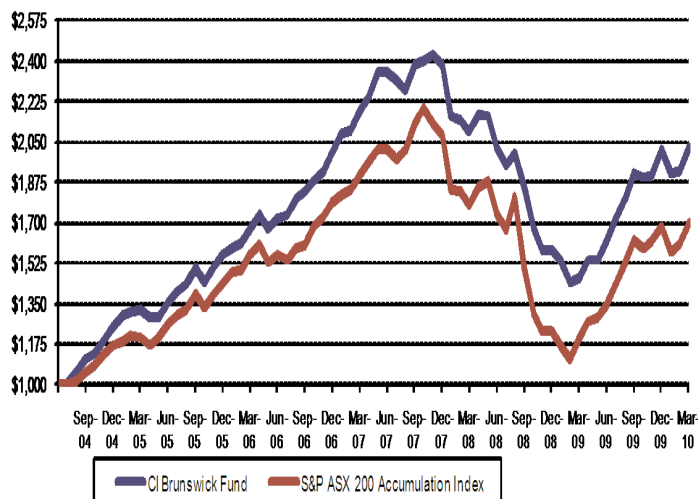
“If you study a problem too long or get too close to a problem you become part of the problem.”

“It does not matter how slowly you go so long as you do not stop.” Confucius

Market and Fund Performance

	**FUND	BENCHMARK	VALUE ADDED
ROLLING 3 MONTHS	0.71%	1.36%	-0.65%
ROLLING 1 YEAR	39.71%	41.70%	-1.99%
ROLLING 2 YEAR	-0.77%	-0.06%	-0.71%
ROLLING 3 YEAR	-1.07%	-2.44%	1.37%
ROLLING 5 YEAR	12.60%	8.07%	4.53%
SINCE INCEPTION*	17.86%	10.48%	7.38%
SINCE INCEPTION^	157.19%	77.42%	79.77%

CI Brunswick Fund - Net of Fees
\$1000 Invested Since Inception



*Annualised

^Cumulative (1 July 2004)

** Before fees and expenses

The Brunswick Fund returned 0.71% over the quarter compared with the index of 1.36%. The main positive contributors to the portfolio's return were BHP, Wotif, Cochlear and Navitas, all of which had good half year profit results and outlook statements.

The under-performing stocks included Healthscope, Austar & QBE. Healthscope announced it was in acquisition discussions with a private aged care group which drew negative response from shareholders who were concerned about value dilution and risks associated with the acquisition. To their credit the Board and Management subsequently withdrew from these discussions. Healthscope management is now focused on delivering higher returns and profits which should flow from the brownfield hospital expansions, the duopoly structure of private hospitals, increased market share in pathology and the profit contribution from the newly established NZ contract.

Austar was impacted by a slower pace of market penetration and some competition from the new free to air digital channels. QBE remains Australia's premier insurance company, but profits have had some headwind due to the currency and low overseas interest rates. QBE have a \$27b investment portfolio backing its insurance business made up of short duration high quality fixed interest assets. The yield on these investments is being depressed due to below normal interest rates in Europe and the US caused by events associated with the GFC. The stock is trading on a price earnings (PE) ratio of 12x and a 6% dividend yield.

The Fund has delivered positive returns over the past 12 months, albeit less than the ASX 200. This is explained by our defensive positions in healthcare, higher cash levels and our mindset being coloured by the GFC which blinded us to the numerous re-rating opportunities in banking, mining, media & discretionary retail stocks. The Fund's historical long term performance remains above market returns.

MARCH 2010

The ASX continues to perform well despite the credit tightening cycle underway in both Australia and China. Our market was up 1.36% for the quarter compared with the World index (AUD) of 1.05%. Over recent years confidence in Australia's equity market has been driven by the 7 Ups ~ commodity volumes/prices; population growth; wages growth; consumer confidence; terms of trade; AUD; and profit growth.

In contrast to the rest of the world, the Chinese stock market returned -3.9% during the March quarter. Sentiment was negatively impacted by China's decision to twice increase the proportion of deposits that the banks must hold as reserves. This rate now stands at 16.5% (large banks) and was increased to "drain liquidity" from the banking system to curb inflation and prevent the economy from "overheating". Credit tightening measures, along with systematic risk concerns associated with the huge banking lending last year and local government debt, have caused some international investors to "shy away" from the Chinese stockmarket recently. Offsetting these factors is that bank provisioning is already high and many market observers believe that China's total debt (central and local government) would only amount to 50-60% and is therefore "manageable", particularly if the country continues to grow as it has done in the past. Moreover China has a high savings ratio and substantial assets.

The Portfolio

Our strategy is to identify stocks with VoF (value latency, operational performance, industry/strategic positioning & focused management). The portfolio can be divided into four broad categories:

1. Stocks with above market dividend yields backed by strong balance sheets and businesses ~ dividends have historically made up over 50% of total returns and we believe this is going to be a key theme over next decade.
2. Growth industries and companies, e.g. education; internet based travel business models; resources and engineering services.
3. Asian geographic exposure ~ Australia's prospects are inextricably linked to the Asian region.
4. Consolidations ~ particularly in OECD countries where economies are mature and face global competition. Firms will need to drive value from consolidation.

The portfolio attributes compared with the broader market are summarized below.

	Portfolio	ASX 200
PE x	14.1	13.2
Beta	0.8	1.0
Yield %	4.7	4.4
Roe %	15.4	14.5
Debt/equity %	40	38
Stock numbers	32	200

Major sector exposures are:

Sector	Portfolio Weight	Stock examples
Energy	7%	Oil Search
Mining stocks	15%	BHP, Coal & Allied, Alumina
Consumer sectors	21%	Glorious Sun, Metcash
Health & Agecare	18%	Healthscope, Cochlear, CSL
Financials	20%	Standard Chartered, Westpac, CBA
Utility & Infrastructure	6%	Trust Power, Australian Infrastructure
Foreign equities	10%	Asian & NZ domiciled stocks
Cash & equivalents	6%	Bank deposits

MARCH 2010

Stock comments:

The Australian coal industry is going through a tremendous growth and rationalisation period with many M&A announcements, the latest being Peabody's bid for Macarthur Coal. The portfolio holds two stocks with exposure to the Queensland and NSW coal industries. Washington Soul Patterson's 60% controlled subsidiary, New Hope Corporation, has steaming coal operations and exploration in Queensland. In addition to their coal and exploration assets New Hope own 18% of Arrow Energy (coal seam gas assets which are currently under takeover by Shell), 100% of Queensland Bulk Handling Coal Terminal in Brisbane as well as coal to liquids technology which is currently under feasibility study. If further tests confirm viability the company will move to process approximately 185,000 tpa of coal into 75 million litres of diesel fuel.

The other company is Coal & Allied which is 75% controlled by Rio Tinto and operates in the Hunter Valley, supplying both domestic and export markets. Both Coal and Allied and New Hope have substantial net cash on balance sheet (Coal & Allied \$400m and New Hope \$1.4b) which will enable them to finance the many growth options both companies have to expand mining and export volumes.

We have an investment in Envestra Limited (ENV) which is Australia's largest natural gas distributor with networks across Victoria, N.S.W., N.T., Queensland and South Australia. ENV has monopoly assets which are regulated by the Australian Energy Regulator. There are good opportunities in this sector because Australia has a regulatory framework that rewards performance and allows companies to exceed return targets. We are also going through a growth period which provides many value growth options. The growth is being driven by population increases, the resource boom and a lot of infrastructure which was built in the 50's, 60's and 70's and needs upgrading. Lastly, we believe that due to the shock of the GFC and the tremendous requirement to incentivize investment in the sector, the AER's regulatory settings will err in favour of investors at least for the next 5 years, i.e. until the capex is completed.

ENV has 2 long term owners - the acquisitive Australian Pipelines (30%) and Cheung Kong Infrastructure with 18.4%. The stock yields 10% (fully backed by operational cashflow) and trades on a small premium to its assessed regulated asset base. Recently, Moody's upgraded their Baa2 rating to stable (previously negative outlook). The upgrade reflects the strengthening of the balance sheet in the last 12 months and a recent successful refinancing leaves the company with average debt duration of 10 years.

Company Trips/Visits ~ CI India Trip March 2010

INDIA – OBSERVATIONS

Our Asian Team undertook a two week trip to India in March 2010. For those interested in a more detailed report please refer to the CI Asian Tiger Fund March 2010 Quarterly Report (see link below).

http://www.cooperinvestors.com/pdf/Reports/AsianTigerFund/citigerfund_report.pdf

Below is a summary of some of the report's relevant highlights:

- India is the seventh largest country in the world and the largest in Asia after China, with an estimated population of just under 1.2bn in 2010. It is also the second most populous country and the largest democracy in the world.
- Around 72% of the country's population still lives in over 600,000 villages throughout India, while the balance of 28% lives in towns and cities. 80% of India's population is Hindu while nearly 140m are Muslim, making it the world's third most populous Muslim country after Indonesia and Pakistan.
- Over forthcoming decades India will enjoy a substantial demographic dividend as the median age of its population is just 25 years. Around 31% of the population is aged 14 years and under, 64% 15-64 and 5% over 65. While India's population growth has slowed in recent years, it is still nearly 1.55% per year, compared with 0.60% in China and a world average of 1.10%.

MARCH 2010

- According to the World Bank, it is estimated that today around 42% (504m) of India's population lives below the international poverty line of US\$1.25 a day, compared with 60% in 1980.
- Today, India's GDP per head amounts to US\$1,240 compared with China's of US\$4,170. Interestingly, Brazil and Russia, the two other BRIC countries, have GDP per head of US\$8,480 and US\$10,030, highlighting that India remains a very poor country.
- India v China ~ From the standpoint of investing, India is most frequently compared with China. That said, this is easier "said than done" as each market is uniquely different, with both having "strengths and weaknesses". For example, we would prefer India to China for its democracy, rule of law (however slow), public information, free market economy (v a command economy), property rights, private companies, forward looking institutions (RBI, SEBI, etc), domestic consumption model (25% net savings as a percentage of disposable income) and lastly, but very significantly, its demographic profile. In contrast, China is preferred over India in such areas as government efficiency, methodical planning, infrastructure and urban development and in its support for "national champions" in the corporate sector. While some may debate the point, India's strengths appear a little more qualitative than quantitative and China's the reverse. In the last 20 years China has "outperformed" India on most generally accepted economic indicators – GDP growth, inflation, external and government balances, etc. Conversely, India has outperformed on a political factors.
- Going forward both countries seem likely to be competitors in some areas, e.g. water in the Himalayas and energy in the Middle East, as well as having different political agendas. That said, they could also be complimentary to each other in areas like computers with India strong in software and China strong in hardware. In reality, it is in India's and China's interests to see continued peaceful economic development and we feel positions are warranted in both countries, in any portfolio investing in the region, as the future is always difficult, if not impossible to predict.
- India and Australia ~ Australian companies who have Indian operations include Leighton, Macquarie, Resmed, GHD, Cochlear and Woolworths. India is Australia's 8th largest (two way) trading partner with 3.9% share. India ranks behind China (14.7%), Japan (13.4%), the US (9.4%), UK (5.3%), Republic of Korea (5%), Singapore (4.7%) and New Zealand (3.9%). However, in exports, India represents Australia's fourth largest market with 6.6% share, after Japan (19.3%), China (15.6%) and the Republic of Korea (7.4%). India has been one of the fastest growing export markets for Australia over the last 5 years, and consequently has overtaken the US and UK as Australia's major export markets. Australia's main exports to India are coal, non-monetary gold, education (#2 most popular destination for Indian students), copper and fertilisers. In comparison, India only represents 1% of Australia's imports. However, the share of Indian imports into Australia has also been rising. Australia's main imports from India are in equipment, gems, medicines and textiles. As well, the largest Indian software firms (including TCS, Infosys) are represented in Australia and have a small but growing presence. From an investment standpoint, Australia is a net exporter of capital to India. In 2006, the total value of investments in India was 2.3b (mainly through portfolio investment, with direct investment being very low). In comparison, India had invested 600m in Australia at the end of 2006. That said, a number of resource and IT related projects has seen this rise in recent years. While most of the focus to date has been on Australia's relationship with China (and rightly so), greater linkages with India are likely to emerge over the coming years.

Market Observations & Outlook

The Australian economy is being profoundly influenced by the current mining and energy boom.

The RBA recently published an excellent paper summarizing Australia's 5 major mining booms over the past 160 years. The 5 booms were: the 1850 gold rush, the late 19th century mineral boom; mining booms in the 1960's/early 70's and the late 1970's; and the present energy & minerals boom. The RBA makes the following observations of these periods:

- The booms did not last longer than 15 years. However, it remains to be seen whether, due to the absolute size of

MARCH 2010

India and China, the current boom goes beyond the historical duration.

- The booms ended because of resource depletion or slower economic activity resulting from domestic or international developments.
- The booms all served to improve and strengthen Australia's economy through increased investment in the mining sector and associated infrastructure. Furthermore population growth increased in the early phases of the booms.
- Notwithstanding the growth in the economy, not all sectors were beneficiaries as some industries went into decline due to difficulty in competing for labour against the expanding and higher paying sectors.
- The differences with the current boom: 1) mining investment as a share of GDP has been much higher compared with previous booms, as has been the rise in the terms of trade due to the strength in both prices and volumes. 2) This is the first boom we have had under a floating exchange rate which may dissipate higher inflation rates which typically have accompanied such booms. 3) The RBA seems well (better) informed in terms of the monetary policy settings required to meet the challenges associated with mining booms. This partially explains their proactive stance on raising interest rates.

Major government reform programs are under way in telecommunications, healthcare and financial services, including stock exchange and market regulation. In healthcare, for example, pathology funding has been cut by \$200mpa (approximately 10%) and issues such as deregulation of collection centre licences will spur further competition and so help to keep a lid on prices. PBS reductions are being helped by the growth in generic pharmaceuticals and government mandated price reductions. The Government wishes to change the funding methodology for public hospitals shifts funding from a 60/40 State/Federal funding share to 40/60. The creation of Local Hospital Networks for the delivery of health management runs the very real risk of only adding another layer on what is already a bloated bureaucracy. It is interesting to note the actions by Medibank Private in acquiring firstly Australian Health Management and more latterly the Australian arm of US healthcare service provider Mckesson. These deals, together with the recently announced diabetes spend, would indicate increasing government emphasis on out of hospital care to prevent and manage disease. A lot more will need to be done across the entire healthcare spectrum (including primary physicians, aged care and mental health) to avoid the cost implications of the demographic shift coming over the next twenty years.

Global stock markets have staged a major recovery from the lows of March 2009. However there are a number of general points worth considering in trying to assess the likelihood of further substantial gains:

1. In the long term, stock markets will reflect corporate profit growth, in turn largely a function of the world's economic health. Currently economic growth in the Western world is anemic. Most of the visits we have made to industrial companies resulted in the view that, although activity levels are no longer falling, there is no sign of any real upturn. The bounce in stock markets, from an oversold level, has restored price earnings ratios to long term averages of 14-15X. To rise further, in the absence of PE expansion, will need sustainable earnings growth.
2. The theme of deleveraging has, in our view, a way to run yet. In digging the private financial sector out of a hole, and in pump priming to avoid recession, governments have taken on massive amounts of debt and gone into budget deficits. When added to long term pension and health liabilities, it is apparent either spending cuts, or higher taxes, or most likely both, will be required over time to fix public balance sheets. This will clearly hinder economic growth.
3. The consumer has over the last fifteen years had the benefit of falling interest rates, rising asset prices, and generally falling tax rates – a perfect concoction to drive increased spending, particularly when allied to increased leverage. These factors are now behind us, and are in most cases reversing.
4. While things are always a little different in different eras, we do note the example of Japan. There have been four rallies of substance in the Japanese market since its peak in 1989. There rallies have ranged in size from 44% to 131%. The fact remains though, that this market is today at less than half its level of twenty years ago. And the primary reason for its continued decline has been the lack of economic growth in Japan, with declining nominal GDP growth causing the end of each rally. The lesson for the Western world, and the USA in particular, may be

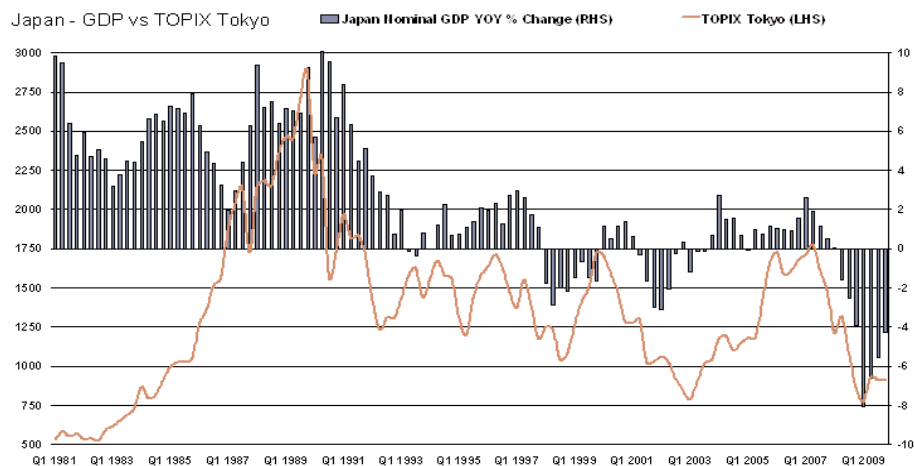
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MARCH 2010

that if monetary policy (which cannot be loosened more than is currently the case) does not gain traction, the deleveraging phenomenon will drive an extended period of subpar growth and thus lower than average share market returns.



Source: GSJBW Research Estimates

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