

# CI BRUNSWICK FUND QUARTERLY REPORT



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

## SEPTEMBER 2007

*"The increase in China's demand for metals over this period (2000-2020) may be comparable to the total demand of the industrial world today."*  
Charlie Lenegan MD Rio Tinto Australia

*"Short of a few ambiguous incidents, I can think of no circumstances where the expanded rule of law and enhanced property rights failed to increase material prosperity"* Alan Greenspan, *The Age of Turbulence*

*"You can breed a thoroughbred racehorse to the point it dies of a common cold"*

*"There is an assumption that more information is better. We believe that enough information is appropriate...but too much information can be unhelpful in building clarity and confidence..."*

*"Queensland Rail was taking a more commercial approach to investment decision"* QR CIO Dallas Stower

### PORTFOLIO PERFORMANCE

	BRUNSWICK FUND	UBSA BANK BILL INDEX	UBS COMP BOND INDEX	S&P ASX 200	MSCI HEDGED#	HEDGE FUND INDEX*
3 MONTHS	1.33%	1.64%	1.48%	5.89%	0.96%	-1.95%
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 <sup>0</sup>	30.66%	6.0%	5.12%	26.3%	15.6%	5.9%
SINCE INCEPTION <sup>^</sup>	138.46%	20.85%	17.6%	113.3%	60.0%	20.5%

\* Financial year to 30 June

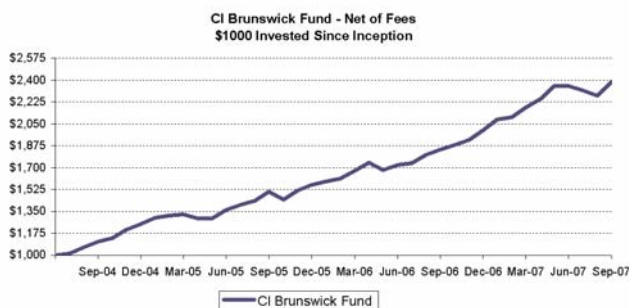
\* Net performance - after management and performance fees and expenses

<sup>0</sup> Annualised

<sup>^</sup> 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)



The September quarter was extremely volatile for all investment markets. At the height of the sell off in equity markets the Australian market was down 11% over the June year end level, however, by the end of the quarter the market was up by around 5.9%. Bond yields were also volatile but yields at the end of September were largely unchanged from June levels. International markets were similarly volatile and while they finished higher over the quarter, the Australian market performed better. The A\$ ended the quarter showing strong gains, especially against the US\$.

The portfolio rose by 1.3% over the quarter and by 29.4% for the year. The portfolio result did not keep pace with the Australian equity market over the quarter.

The portfolio holds a number of smaller cap stocks that did not recover fully from the price declines in August. Examples of these stocks include Trinity, and WHK Group. Additionally a number of stocks that were held with the aim of providing the portfolio with stability in difficult markets did not actually do

their job. For example the Transurban share price fell by 9% over the quarter. On the positive side resource, insurance, healthcare and the grouping of Asian bank stocks performed strongly.

The portfolio currently has around 6% in bank bills, a further 4% in cash, 92% is invested in stocks and around 2% in short positions. Around 10% of the portfolio is held in international stocks. We added Standard Chartered to the portfolio; this rounds out to four the grouping of banks that operate in Asian markets.

Our investment views are primarily based on our interactions with companies, both in Australia and overseas. Some of the important factors that we are including in our thinking on portfolio construction are:

- Most companies are experiencing price rises, some on inputs, some on outputs and some on both.
- The strong A\$ is having an impact on the Australian share market as most of the successful leading companies have increasing overseas operations, offsetting this is the observation that rising currencies are coincident with strong economies.
- The Australian economy and companies are generally doing better than other developed economies and companies.
- The Reserve Bank of Australia is very confident in the fundamentals of the Australian economy
- The amount of debt in the economy has risen significantly over the past few years; this has been offset though by strong asset price rises. The higher levels of debt increase anxiety levels when bad news is announced.
- There is a strong preference by investors for equity over fixed interest; this is exacerbated by the move to invest more of Asia's savings in equity rather than debt.
- Confidence needs to remain high to continue the virtuous cycle of rising leverage, consumption and asset prices. The fact that the markets have overcome the extreme volatility in August suggests a very strong underlying demand for equity investments.
- Quality overseas companies are cheaper on most metrics than quality Australian companies but growth is likely to be stronger in Australia.

Overall we are not changing the portfolio in a significant manner. We feel that over the medium term equity markets will offer enough opportunities to offset shorter term volatility. We do not feel that pricing is attractive enough to use gearing.

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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## VoF OBSERVATIONS ~ INDUSTRY TRENDS & BEHAVIOUR

On a recent trip to Europe we visited over 40 companies, including the operations of eight companies that are in the portfolio. These range from relatively small companies such as Realestate.com to the global insurer QBE, which has a very large European business based in London.

One approach we use is to own a cluster of stocks that are based on a common investment idea or theme.

One investment idea in the portfolio is the Asian banking and finance theme. The basic principle is that as countries develop and per capita incomes rise the use of banking, insurance and investment products rises much faster than the general level of economic activity. Rather than buying a large position in one bank in one country we have bought four banks, each with a 2% weighting. We have previously visited Standard Chartered Bank in Hong Kong and we took the opportunity to visit the head office in London. The meeting added conviction to our basic investment thesis and gave us confidence to add Standard Chartered to the portfolio. The portfolio also owns AXA which operates businesses in eight Asian countries.

We believe that the value of gas and renewable energy sources will continue to rise as the oil market tightens up further and the technology to develop clean coal remains a long way from being applied commercially. The portfolio has owned Oil Search, Trust Power (NZ) and Viridis for quite a while. We visited BG in London and decided the company was a legitimate candidate for the portfolio and, after some further research, added the stock into the portfolio. Excluding BHP there are four stocks in the portfolio that are in this grouping. BHP is the largest weighting in the portfolio.

On a more general note a couple of other interesting general trends we observed are likely to become quite important.

The first is that the power seems to be shifting away from financially based companies back to the operating type companies. At the extreme the comparison might be between a company such as Lend Lease that is steeped in project management, development and construction and an infrastructure trust that is heavily financially structured with the aim of growing funds under management as quickly as possible. Obviously both models can be successful but we feel the operators are becoming more valuable relative to financial based models.

Another notable trend is how much greater importance is being given to the topic of emissions, environmental responsibility, climate change and sustainability has become a major issue at Board tables and in company strategy and planning. At most of our meetings these issues were discussed. Tesco for instance has taken a proactive approach to its environmental responsibility. There is a lot of cynicism that companies are talking more than doing and are ticking the boxes. Our feeling is that the companies are genuine and that at a minimum they see that genuine sustainability is essential to long term survival. Successful companies must respond to changing consumer expectations, just as politicians do.

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