

Dalton Nicol Reid

Investment Review – May 2009

Market Wrap

EQUITY MARKETS

- Markets consolidated in May – portfolios underperformed as market rally pushed into lower quality areas of the market and defensives underperformed.

FIXED INTEREST

- Fixed Interest portfolio outperformed the index with the long bonds selling off.

PROPERTY

- Portfolio under-performed after strong recent performance.

AS AT 31 MAY 2009	1 MONTH	3 MONTHS	6 MONTHS	1 YEAR	3 YEARS	5 YEARS
INTERNATIONAL EQUITIES						
Dow Jones Industrial	4.07%	20.35%	-3.72%	-32.74%	-8.70%	-3.56%
MSCI World Index	7.96%	28.40%	8.63%	-36.81%	-9.99%	-1.55%
AUSTRALIAN EQUITIES						
S&P/ASX 200	0.99%	14.16%	2.02%	-32.48%	-8.61%	1.99%
FIXED INTEREST						
UBS Comp Bnd (0+yr)	-0.72%	-0.60%	0.80%	11.83%	6.65%	6.26%
UBS Corp Bd (0+yr)	0.95%	0.70%	2.44%	10.41%	6.01%	5.98%
PROPERTY						
S&P/ASX 200 A-REIT	3.64%	9.39%	-28.87%	-54.77%	-27.34%	-14.93%

Property Trusts - Outlook

- Outlook:
 - De-leveraging continues (\$9bn raised in last 6 months)
 - De-gearing of “majors” mostly complete (see table below)
 - Asset values still falling – will overhang sector for some time to come but covenants safe post raisings
 - Smaller trusts still in difficult situation – may have spikes in price but will struggle to survive

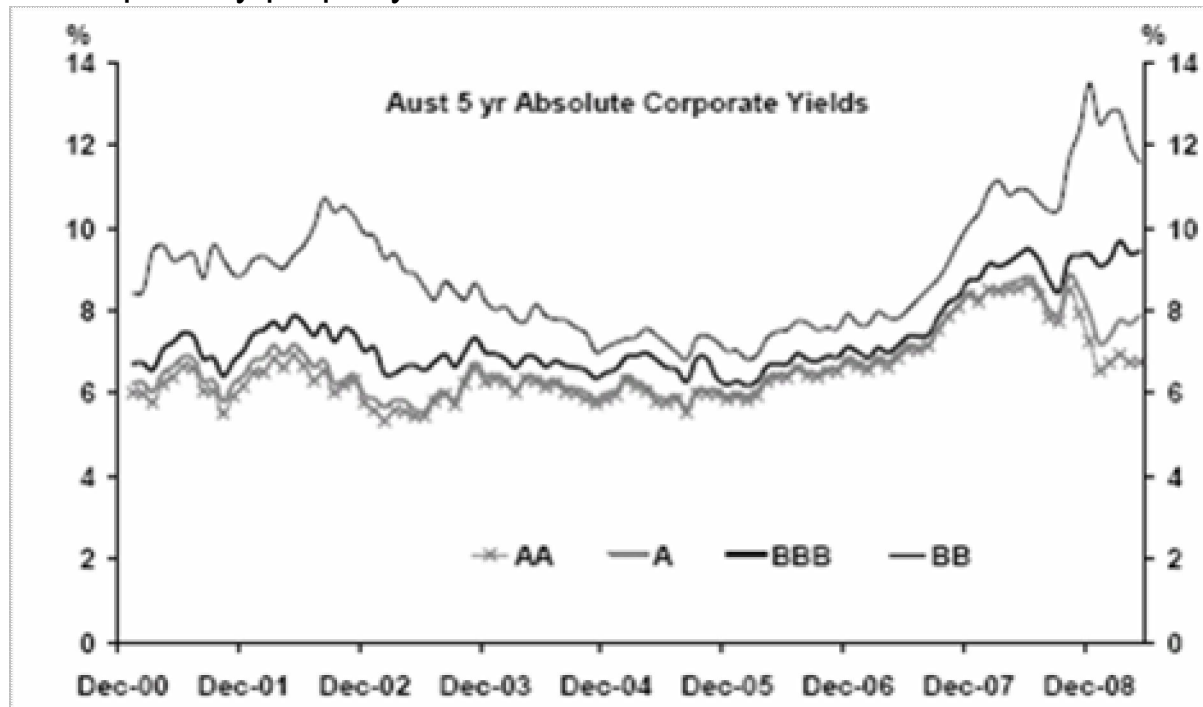
CURRENT PORTFOLIO	GEARING	IMPLIED CAP RATE
WESTFIELD GROUP	34.6%	7.6%
STOCKLAND GROUP	20.5%	7.9%
DEXUS PROPERTY GROUP	28.8%	9.3%
MACQUARIE OFFICE GROUP	36.1%	9.2%
GOODMAN GROUP	34.1%	9.8%
SECTOR GEARING	30.6%	8.1%
MAJORS NOT HELD		
<i>GENERAL PROPERTY TRUST</i>	21.1%	8.2%
<i>MIRVAC GROUP</i>	21.5%	8.7%
<i>CFS RETAILS PROPERTY TRUST</i>	25.8%	8.1%
<i>COMMONWEALTH PROPERTY OFFICE FUND</i>	26.2%	8.9%

Australian Equities - Outlook

- The following factors are influencing our view on equities:
 - Cash allocations remain high. Superannuation Funds have 25% in cash and cash at bank at the majors is up around 40%. Cash returns are poor, property uncertain so equities looking more appealing.
 - Australia is beginning to stand out. Australian equities have fallen at a similar rate as the US and UK despite significant economic out-performance. An opportunity for international flows.
 - Credit markets are improving.
 - Inter- bank lending is improving with TED spread down to 50 bps (from 450 in Nov).
 - Majors are raising money without guarantee.
 - Corporate bond market improving – RIO, WDC among others tapping the market.
 - Substantial capital raised in Australia has significantly improved balance sheets – see property trusts.

Australian Equities - Outlook

- The following factors are influencing our view on equities:
 - Credit markets are improving cont.
 - Note credit still expensive but improving.
 - But availability of bank credit has further to go in most markets especially property.



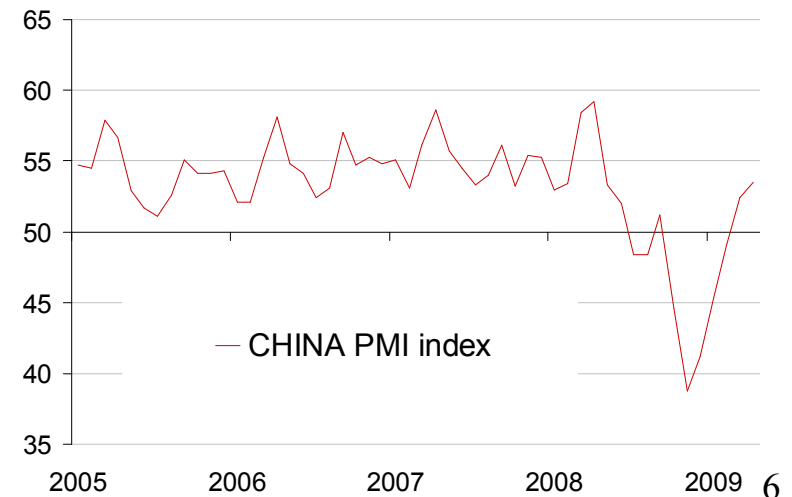
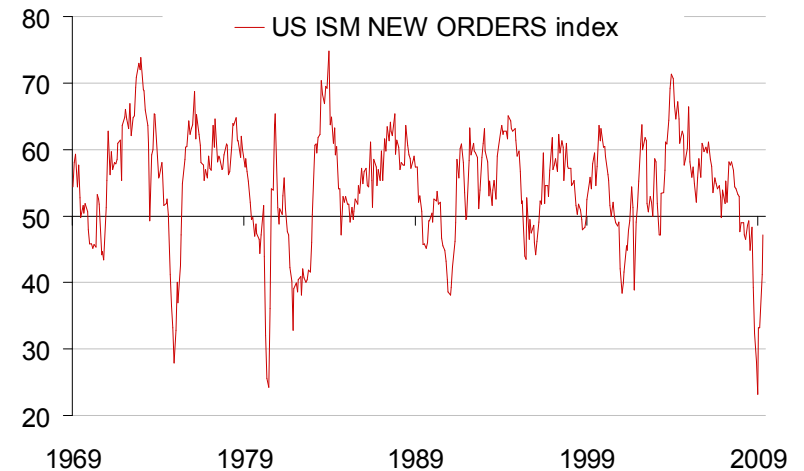
Australian Equities - Outlook

- The following factors are influencing our view on equities:
 - Volatility Index Improving.



Australian Equities - Outlook

- The following factors are influencing our view on equities:
 - Economic fundamentals are improving albeit risks remain.
 - Chinese M2 up 18% in March. Very strong stimulus.
 - China PMI bounces.
 - US ISM New orders bounce

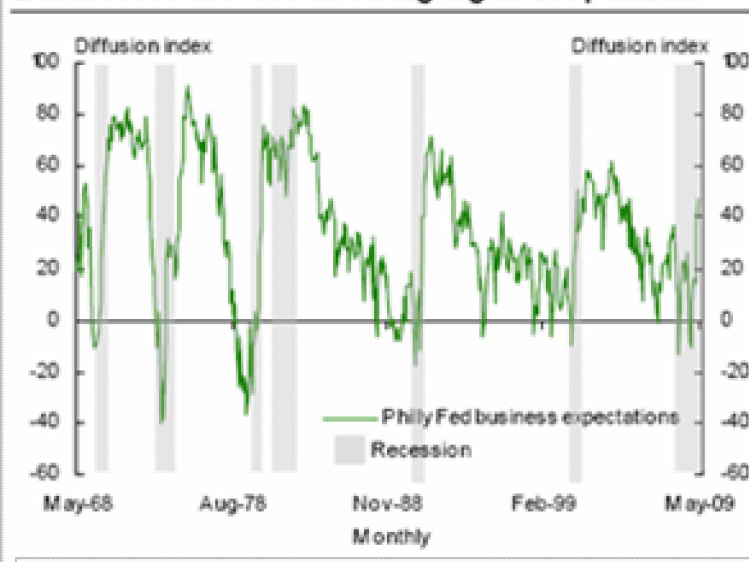


Australian Equities - Outlook

- US business confidence improving
- Australian housing finance approvals bounce.
- They can bounce even with rising unemployment.

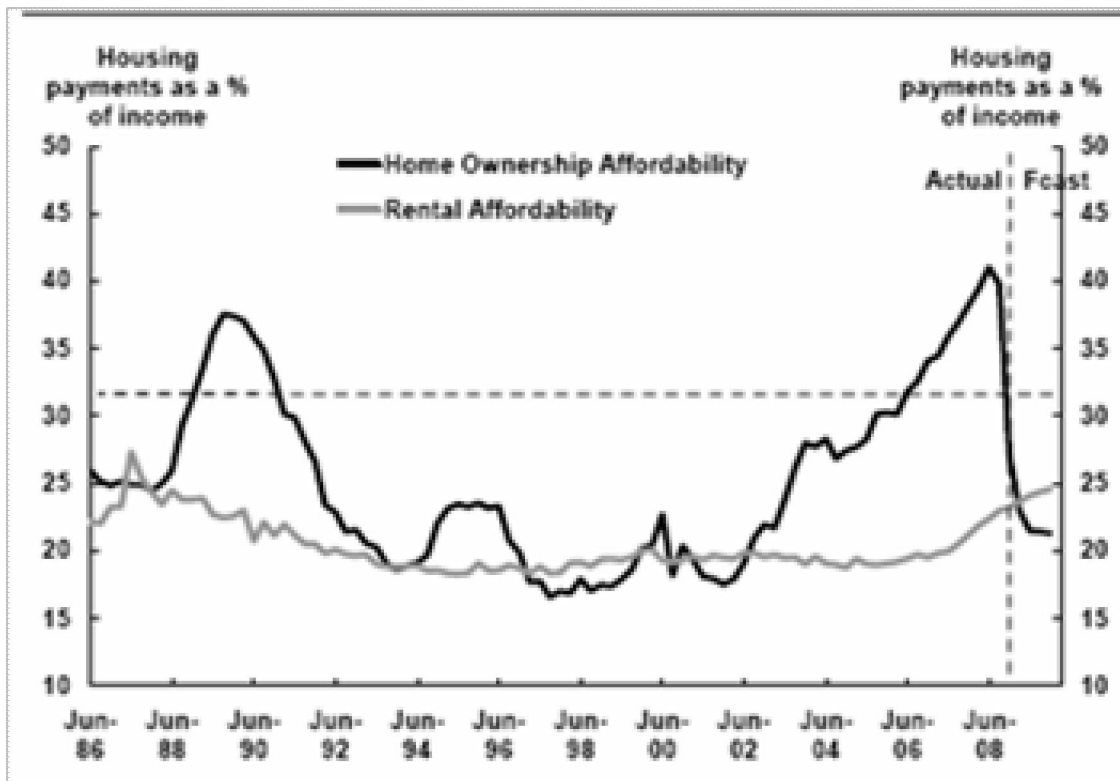


Businesses are also showing signs of optimism



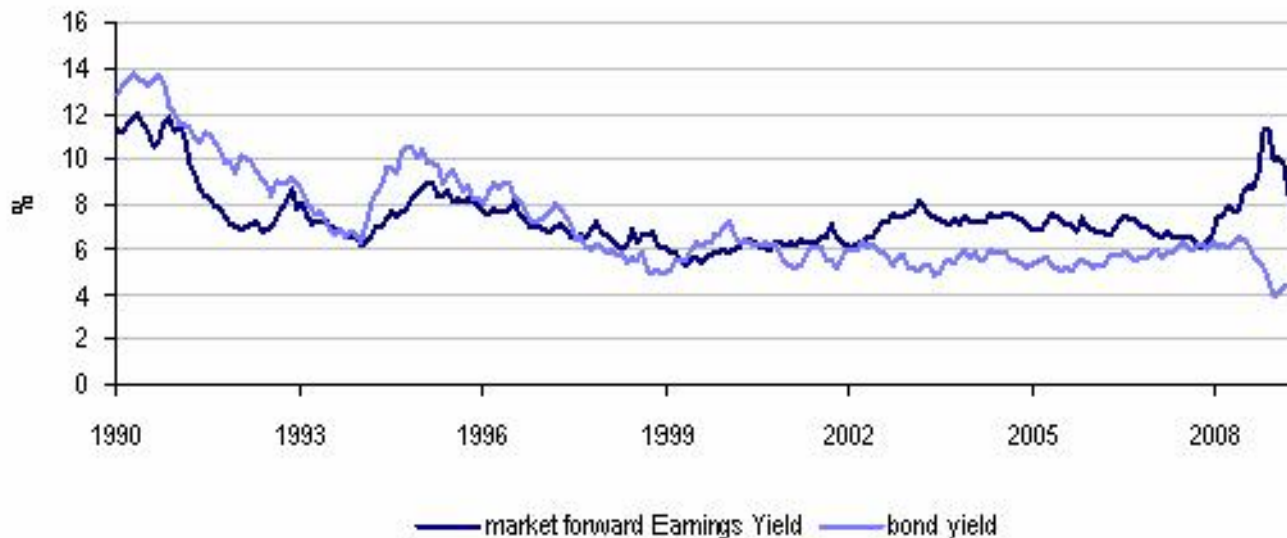
Australian Equities - Outlook

- Key difference for Australia has been performance of housing prices:
 - RBA knows house prices contributed to US issues.
 - Mortgage rates dropped more significantly in Australia than offshore.
 - Rents have increased due to tighter supply.



Australian Equities - Outlook

- Valuations
 - Equities appear good value relative to cash and fixed interest.
 - Cyclical have run hard in short term. Market is looking through the earnings valley for these stocks. PE not a reliable guide at this point and need to focus on ability to meet or beat earnings. We could see a short term pullback in some cyclicals given the strong recent run.
 - We do not expect a pullback to be sharp given the above dynamics.



Portfolio Themes

- Maintain exposure to companies with strong balance sheets
- We are participating in capital raisings where the capital has a positive use such as an acquisition
- Trends emerging – stay at home, trade down, gamble/ drink, infrastructure spending
- A balance between cyclical and defensive is warranted given general economic uncertainties
- Use the bounce to improve the quality of the portfolio
- Chinese GDP forecasts upgraded
- Reduced exposure to major banks

Overall, the portfolios remain conservatively positioned, in strong companies with good balance sheets

Portfolio Moves

- **Incrementus**
 - Sold CAB
 - Bought COH, TAL
- **Virtus**
 - Sold CAB, SHL
 - Bought JBH, COH
- **ProV**
 - Sold CAB, DJS, FXJ
 - Bought WOW, COH

SOURCES

ABN AMRO

Austock

Citigroup

GSJBWere

Macquarie Equities

Morningstar

UBS

Van Eyk

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