

# Kinetic Wholesale Emerging Companies Fund

Fund report and commentary – 30 September 2008

Performance						
	Quarter (%)	1 year (%)	3 years (%) p.a.	5 years (%) p.a.	10 years (%) p.a.	Inception (%)
<b>Kinetic Wholesale Emerging Companies Fund</b>	<b>-17.56</b>	-	-	-	-	<b>-19.00</b>
Growth return	-17.55	-	-	-	-	-20.39
Distribution return	-0.01	-	-	-	-	1.39
S&P/ASX Small Ordinaries Accumulation Index	-18.12	-	-	-	-	-17.63

Returns are calculated after fees have been deducted, assuming reinvestment of distributions. No allowance is made for tax. Past performance is not a reliable indicator of future performance.

## Investment objective

The Fund aims to outperform its benchmark, the S&P/ASX Small Ordinaries Accumulation Index, over rolling five-year periods.

## Investment manager

Kinetic Investment Partners Limited

## Investment strategy

Kinetic believes that inefficiencies exist in the small company sector of the market, and these inefficiencies predominately occur at the stock level.

Kinetic uses cash flow analysis to identify companies that they believe have been undervalued / undiscovered by the market. By focusing on cash flow, Kinetic minimises their exposure to accounting manipulations and changes in accounting standards.

Kinetic does not target a specific investment style. Kinetic's investment approach seeks companies undervalued on a cash flow return on investment (CFROI) methodology.

## Distribution frequency

Quarterly

## Suggested minimum investment timeframe

At least five years

Asset allocation		
	Current (%)	Range (%)
Securities	95	90-100
Cash	5	0-10

Top five active positions as at 31 August 2008			
	Fund weight (%)	Index weight (%)	Active weight (%)
Healthscope	4.38	0.88	3.50
Campbell Brothers	3.12	0.00	3.12
Mount Gibson Iron	3.02	0.00	3.02
Windimurra Vanadium	2.99	0.00	2.99
Tassal Group	3.09	0.22	2.87

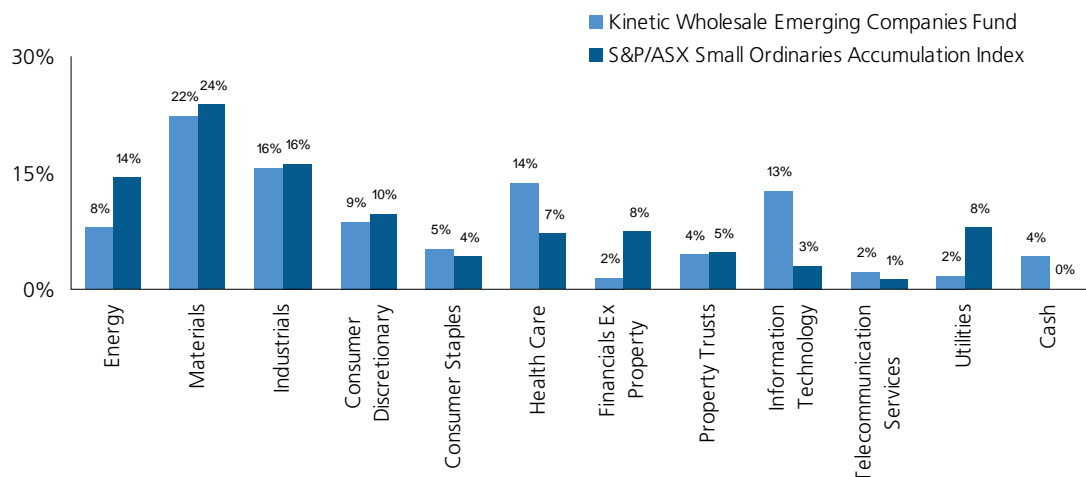
Fund facts	
	Kinetic Wholesale Emerging Companies Fund
Inception date	12/3/2007
Fund size (\$M)	0.00
APIR code	HOW0036AU

Fees	
	Kinetic Wholesale Emerging Companies Fund
Entry fee	Nil
2007/08 ICR	n/a
Management fee	1.15%p.a.
Performance fee	20% of the Fund's gross return over and above the Index plus 1.15 %p.a.
Buy/sell spread	+0.40%/-0.40%

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## Sector exposures as at 31 August 2008



## Commentary

The small cap market underperformed the large cap domestic equities market during the quarter, returning -18.12% (S&P/ASX Small Ordinaries Accumulation Index). Volatility was a key theme, with daily swings of 2% being common. Reporting season was a major event for the quarter. As expected, results highlighted generally tighter conditions over the June half (in contrast to a more buoyant December half period). Forecasts were downgraded in line with company commentary regarding current trading conditions and the expected adverse impact of higher costs going forward. However, the absence of “surprising” negative news (given already low expectations) prompted a relief rally across a range of industrials companies despite the downgrades. In contrast, small resources were weak as some of the bullish momentum pushing up prices continued to recede. Small cap resources ended down 37.56% for the quarter.

The Portfolio outperformed its benchmark during the quarter. Contributing to Portfolio returns were overweight positions in Healthscope (up 17.69%), JB Hi-Fi (up 17.95%) and Campbell Brothers (up 17.92%). Detracting from returns were overweight positions in Sphere Investments (down 62.94%), Windimurra Vanadium (down 48.05%) and Mount Gibson Iron (down 47.45%).

Healthscope’s announced strong earnings results for FY 2008. We continue to support the company based on the defensive nature of its earnings and likely reduction in threshold for abolition of the Medicare levy surcharge. JB Hi-Fi was the subject of speculation over corporate activity during the quarter. The company posted strong earnings results and we view the stock favourably given its strong store rollout program and low cost structure. Sales momentum has continued for the company in the current environment.

Campbell Brothers rose following an announcement that the company is anticipating 60% profit growth this fiscal year.

Growing expectations of a downturn in Chinese growth and market observation of iron ore stockpiling (in Chinese ports) had an impact on the bottom three contributors. We remain confident of iron demand out of China in the medium term. Sphere Investments fell over the quarter primarily due to the decline in the resources sector. Significant progress has been made in the company’s Lebtheinia Iron Ore project in Mauritania. Windimurra Vanadium is soon to be a large scale producer of vanadium which is a key component in the production of high end steel. A decrease in steel production had a negative effect on the stock price. Mount Gibson Iron fell on the back of negative sentiment towards the resources sector.

## Fund outlook

Key risks remain for Australian equity markets: ongoing uncertainty about global financial systems, decreasing commodity prices and a slowing global economy. Australian banks remain well capitalised and the rapid actions taken by government to reduce negative affects on the economy are positive signs. We believe that fundamentally, the Australian economy remains solid and the current volatility will present valuable buying opportunities for the future, with many high-quality stocks trading at multi-year lows and looking extremely attractive on a valuation basis.

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