

Kinetic Wholesale Smaller Companies Fund (CNA)

Fund report and commentary – 30 September 2007

Performance						
	Quarter (%)	1 year (%)	3 years (%) p.a.	5 years (%) p.a.	10 years (%) p.a.	Inception (%) p.a.
Kinetic Wholesale Smaller Companies Fund	4.44	50.94	34.07	31.44	17.66	17.08
Growth return	4.48	26.78	16.46	13.47	0.58	1.34
Distribution return	-0.04	24.16	17.61	17.97	17.08	15.75
S&P/ASX Small Ordinaries Accumulation Index	-0.54	36.71	27.55	25.73	11.35	11.85

Formerly known as the Kinetic Small Companies Wholesale Fund. Closed to new applications including initial and additional investments. 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 provide capital growth over the medium to long term through an actively managed and diversified portfolio of Australian small company shares, and provide returns above the benchmark, the S&P/ASX Small Ordinaries Accumulation Index, over rolling three-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 predominantly occur at the stock level.

Kinetic uses cash flow analysis to identify companies that they believe have been undervalued or undiscovered by the market.

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

Yearly

Suggested minimum investment timeframe

At least five years

Asset allocation

	Current (%)	Range (%)
Securities	98	90-100
Cash	2	0-10

Top five active positions as at 31 August 2007

	Fund weight (%)	Index weight (%)	Active weight (%)
Incitec Pivot	5.04	0.00	5.04
ConnectEast Group	5.93	1.58	4.35
JB Hi-Fi	5.00	0.92	4.08
Transfield Services	4.48	1.36	3.12
Tassal Group	2.99	0.00	2.99

Contributors (quarter) as at 30 September 2007

		Active weight (%) [*]	Value add (%) [^]
Top contributors	Mount Gibson Iron	2.29	1.34
	JB Hi-Fi	3.92	1.17
	Anzon Australia	2.21	1.10
Bottom contributors	Silex Systems	1.76	-0.84
	Marathon Resources	0.54	-0.39
	Precious Metals Australia	1.56	-0.39

^{*}Active weights are daily averages over the period | [^]Relative to benchmark and based on pre fee returns

Fund facts

	Kinetic Wholesale Smaller Companies Fund
Inception date	31/10/1994
Fund size (\$M)	48.9
APIR code	HBC0006AU

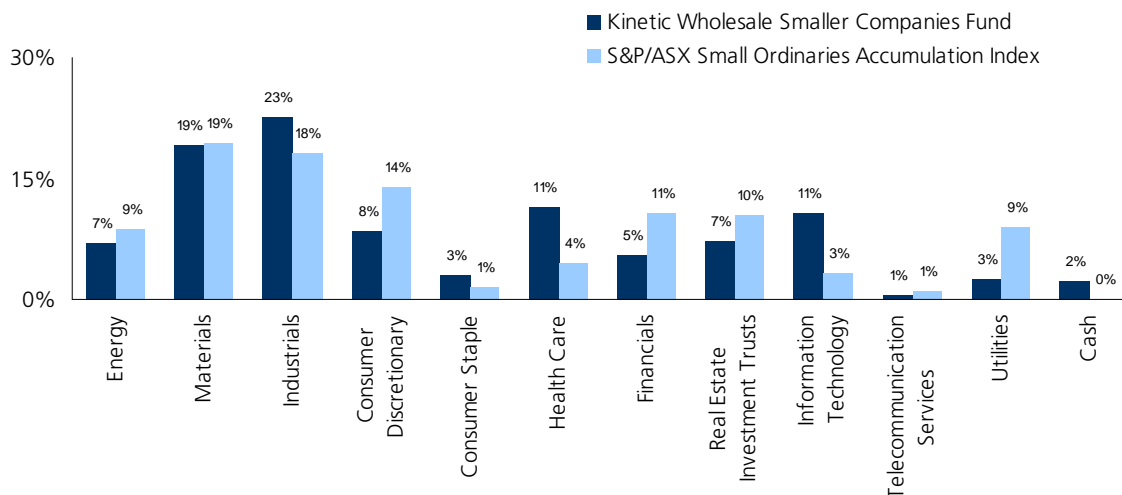
Fees

	Kinetic Smaller Wholesale Companies Fund
Entry fee	Closed
2005/06 MER	0.87%
Management fee	0.768%p.a.
Performance fee	Nil
Buy/sell spread	+0.40%/-0.40%

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Sector exposures as at 31 August 2007



Commentary

The small cap market finished the quarter marginally lower down 0.54% (as measured by the S&P/ASX Small Ordinaries Accumulation Index). A global credit crisis sparked by the US sub-prime meltdown coupled with concerns of a global growth slow down lead to large falls on global equity markets in August. However, Australia's market bounced back in late August as the US Federal Reserve cut interest rates and it appeared there would be little impact on the domestic economy from the fall out. Small Resources led the rally ending 7.84% higher for the quarter.

The portfolio outperformed the benchmark for the quarter. Contributing to returns were overweight positions in Mount Gibson Iron (up 77.61%), JB Hi-Fi Ltd (up 33.73%) and Anzon Australia (up 73.07%). Detracting from performance were overweight positions in Silex Systems Ltd (down 38.05%), Marathon Resources (down 52.00%) and Precious Metals (down 22.41%).

The strengthening price of iron ore during the quarter benefited Mount Gibson Iron as the market began to recognise it as a quality mid cap producer. The stock also benefited from speculation that the next round of contract negotiations between major iron ore producers (RIO, BHP Billiton and CVRD) and iron ore purchasing countries (China) could yield a 50% increase in iron ore prices. JB Hi-Fi ended the quarter higher as the market reacted positively to a better than expected 2007 annual profit result. Upbeat earnings guidance for 2008 also provided further support to the stock. Anzon rallied hard as the market re-rated the stock following the sale of 20% of its BMG project to ITOCHU Corporation. The company is also benefiting from the rising global price of oil and speculation of a potential takeover.

Uranium technology company Silex Systems was caught up in the market downturn during the first half of the quarter and was unable to recover in the absence of any major news flow. The falling price of uranium, off recent highs, coupled with a production downgrade in its recent resources update hurt Marathon Resources over the quarter. Precious Metals finished lower as uncertainty arose regarding the delay in debt finance for its Windimurra mine project.

Fund outlook

Our outlook is relatively cautious as the small cap market broadly appears expensive based on current market levels. This view is based on our belief the recent dislocation in global credit markets and the housing downturn in the US pose a continued threat to returns going forward. We are wary of businesses that display interest rate sensitivity and those highly leveraged to exports due to recent strength in the \$AUD. Despite this we are positive on the energy sector given strengthening gas and oil prices and consumer staples.

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