

# Monthly Investment Report

## Antares Lodestar Absolute Return Trust Australian Shares

### Market Review

#### John Morgan, Chief Investment Officer Lodestar Capital Partners

- The ASX 200 Accumulation Index returned 3.6% in June after having rallied in each of the preceding three months, however the Australian market posted a 24.2% loss for FY09. Only three years since 1950 have recorded worse annual returns.
- Over the last 12 months international markets also fell sharply with the S+P 500 declining by 28.2%, the FTSE 100 down by 24.5%, the Nikkei 225 down by 26.1% and Euro Stoxx 50 was down by 28.8%.
- Defensives such as consumer staples (-7%) and healthcare (-3%) outperformed in the financial year but lagged the March to June rally. Despite the dislocation in global financial markets the banking sector delivered a creditable performance of -7.2% for FY09. This was primarily due to a government guarantee on wholesale funding and the belief that Australia would be less vulnerable to sharp economic weakness and asset price delation than other developed economies. Resource stocks underperformed (-32%) during the year but this was confined to the first half of the financial year, as resources later recovered in response to firmer commodity prices, assisted by strong Chinese economic stimulus.
- During June the best performing sectors in the Australian market were telcos (+8.6%), healthcare (+8.1%) and financials (+6.5%). The underperformers were utilities (-3.8%), materials (-0.1%) and energy (+0.4%).
- Within the best performing large market capitalisation stocks were Goodman Group (+48%), Fortescue Metals Group (+44.7%), David Jones (+26%), Macquarie Group (+23.5%) and JB Hi Fi (+23.3%). The worst performers were Nufarm (-25.1%), Aquarius Platinum (-19.1%), Transfield Services (-11.6%) and Toll Holdings (11.2%).
- FY09 was a "game of two halves" for bonds, as yields based in January as investors turned to safe havens in the face of extreme economic uncertainty. By the latter half of the financial year in reaction to the need for public borrowing to defray the economic and financial crisis and as the pace of contraction eased, yields rose sharply. Australian 10 year bonds yielded 3.85% at their January low and ended June at 5.52%, down 93bps for the year. Over the same period US bond yields lost 44 bps to close at 3.54% after reaching a low in 2.05% in December 2008.
- The Australian dollar peaked at US\$0.98 in July 2008 but fell sharply by the end of August to near US\$0.60. This was mainly in response to a rallying USD and sharp declines in commodity prices. The A\$ subsequently recovered a lot of ground to finish June at US\$0.806 as the scenario reversed – commodities rebounded and the USD was sold off.
- Crude oil (WTI) peaked in July 2008 at US \$145.30 and fell sharply to reach a low in December of US\$31.41 before ending the year at US\$69.90. A confluence of factors such as the prospect of global economic stability, a strong bounce in Chinese activity and OPEC supply discipline offered support.
- Gold was relatively flat (+0.7%) during the year despite interest rate volatility and high risk aversion. Gold closed at US\$926.00 on June 30.
- Economic data in June were strong with Consumer Sentiment rising by 12.7% (now up 18% pcp), the second largest rise on record. New motor vehicle sales also rose. Q1 Australian GDP rose by 0.4% q/q, which was strongly ahead of market expectations, though the annual pace of 0.4% y/y was the weakest since Q4 1991. The quarterly result was boosted by strong net exports which contributed 2.2% to GDP in Q1 but offset by the fall in domestic demand which was the weakest for 8 years. The RBA elected to leave rates unchanged against the backdrop of these data.

### Portfolio Activity

- The Fund increased its net exposure to the market during June as we took advantage of the market retracement of ~7%. Our buying rationale is based on improved Australian and Chinese economic outlooks versus previous expectations. During the current pullback we will selectively take advantage of stock prices that have retreated to attractive valuations.
- The net exposure rose from 21% to 75%. We mainly purchased domestic cyclical stocks that are likely to benefit from the better than expected performance of the Australian economy. Financials were also added to the portfolio as the unemployment cycle, although deteriorating, is not as weak as the sharemarket was anticipating. As there may not be further deterioration in bad debts, consensus earnings estimates may not be subject to downgrades so the current levels of provisioning by banks may prove to be adequate.
- Essentially, the gross exposure rose with the net exposure increase but the number of shorts declined over the month.

### Fund Performance

Period ending 30.06.09	1m %	3m %	1yr %	2yr %	Since Inception % p.a.
Total Return	1.11	2.58	-18.61	-10.46	-6.49
Benchmark *	0.26	0.78	5.58	6.47	6.49
ASX200 Accum. ^	4.01	11.29	-20.14	-16.84	-11.33

Performance returns are calculated net of management fees and pre tax. Past performance is not a reliable indicator of future performance, the value of your investment can go up and down. \* 90 day Bank Bill rate resets quarterly (Benchmark) and is used for the purposes of calculating the performance fee. ^ S&P/ASX 200 Australian Shares Accumulation Index is provided for comparison purposes due to the Australian Share investment focus of this Fund. It is not the Fund's benchmark. Inception date 1 March 2007.

- The Fund returned 1.1% in June. The Fund's approach to buying stocks as they were correcting made it difficult to add value in the short term but it will augur well if these stocks rally in line with an improving economy. Some of

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the Fund's recent purchases have retraced further with little or no deterioration in the fundamentals, while selected defensive holdings underperformed as many have been used to fund recent capital raisings.

### Positive Influences

Company	June Return %	Fund Position %
Resmed	12.3	2.7
JB Hi Fi	23.3	1.4
Downer	19.2	1.0

- ResMed benefited from the stabilisation of the Australian dollar during June and its favourable fundamentals offered support.
- JB Hi Fi upgraded guidance during the month based on stronger consumer demand, solid margins and good cost containment.
- Downer announced a number of contract wins, including a \$NZ 1 billion telecommunications deal with Telecom NZ and the Melbourne Trams contract that runs for at least 8 years. The company also reaffirmed guidance for the upcoming reporting season.

### Negative Influences

Company	June Return %	Fund Position %
Nufarm	-25.0	1.1
Sino Gold	-20.5	1.6
AGL Energy	-3.8	1.4

- Nufarm issued a profit warning on the back of a late planting season and the associated pricing pressure on its glyphosate products.
- Sino Gold held an operational site visit which was well received however the stock fell in line with global gold stocks.
- AGL energy fell slightly in reaction to a broker report speculating the company would write down the value of acquisitions made over the past three years.

### Stock Specific Highlights

- Highlights of the month included announcements by BHP and Rio of a 50/50 JV involving both companies' WA iron ore assets. Rio also severed the financing and asset sale deal with Chinalco that they established earlier in the year and subsequently announced a USD15.2bn rights issue. The deal was well received with both companies rising by ~8.5% on the day of the announcement.
- CSR proposed a de-merger of its sugar and renewable energy business into a separate listed entity and its shares rallied by 6% on the day it was announced.

- David Jones upgraded guidance for FY09 net profit after tax of ~10%, up from ~0.5% previously, in response to better May and June sales due to the economic stimulus package and good cost control. DJS shares rose 10% that day after already posting solid gains during the month. JB Hi Fi also had a strong month after upgrading its FY09 net profit by ~6%, also due to strong sales, solid margins and good cost control. Both retailers have resilient business models and strong management teams.
- NAB announced that it is buying the Aviva Australia wealth management business, including the life insurance operations and investment platform, Navigator, which was well received by the market.

### Outlook

- For the six months to March global economic data showed a deep decline in activity. Since then many indicators have turned around or have at least indicated that the pace of economic contraction has slowed from those earlier levels. The degree of this abatement of poor numbers has varied from region to region.
- China has experienced a strong turnaround with the economy responding well to the boost to money supply and the range of fiscal responses to their slowdown post the Beijing Olympics, as evidenced by the recently released PMI series, where both measures stayed above the expansionary threshold of 50.
- Most of the OECD has produced poor numbers relative to their respective histories, e.g. the U.S. recorded three consecutive quarterly falls in GDP for the first time in 34 years. The last number showed a fall of 5.5% annualised. Other statistics such as housing starts are still poor but off the lows produced earlier in the calendar year.
- Australia's experience has been somewhere in the middle of the above examples. The March quarter GDP rose unexpectedly by 0.4% to (technically) avoid a recession. The unemployment rate has not deteriorated as quickly or as badly as many commentators had predicted. The fiscal and monetary policy responses have boosted consumer sentiment and retail sales. Business lending and capex expectations have been sluggish and remain a weak spot on the generally improved economic landscape. Significantly, the Australian economy is in much better shape than pundits were predicting six to nine months ago which is clearly a positive for the equity market.
- Against the backdrop of a weakening but still quite resilient economy the forthcoming reporting season should be interesting. At many recent industry conferences executives have advised investors of any material changes in their respective operations. There has been very little deterioration announced since May; conversely numerous corporates have provided positive updates. The anecdotal commentaries sit comfortably with the generally supportive economic data, but managements' have also managed to keep expectations at an appropriate level for the June half earnings results.
- It is worth giving an overview of the more significant sectoral outlooks as we approach the August reporting season. Firstly, the global cyclicals have been among the

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best performing stocks since the market bottomed in March, largely in response to the upturn in Chinese economic activity and the leverage to their importation of raw materials such as copper and iron ore. Seasonal factors and the Chinese response to lower commodity prices have both changed, with evidence that stockpiling levels have now abated. The brief outperformance of cyclicals implied that many fund managers decided that the seasonal and stockpiling trends would continue in the foreseeable future but the discontinuation of those trends was also accompanied a stalling in the cyclical rally. This is likely to continue until other developing economies resume economic strength and join the Chinese on the positive economic trajectory.

- Secondly, the banks have proven resilient versus their global peers. In the 6 -9 months there has been significant general and specific provisioning for bad and doubtful debts and it is likely there will be ongoing realisation of bad debts as the economy continues to contract. The significant point is that most banks' management teams have indicated that the duration and severity of loan losses this cycle is unlikely to be as bad as the 1990/1992 bad debt cycle, which suggests that there may be diminishing need for further increases in general provisioning. Under this scenario the banks are likely to have a strong rebound in profitability and ultimately may start returning capital to shareholders. We believe the market has not yet priced this outcome into bank valuations.
- Lastly, a bright spot so far this calendar year has been the strength of the consumer, mainly in response to accommodative fiscal and monetary settings. History leads us to conclude that a continuation of this trend suggests that the unemployment rate is likely to surprise on the low side. Consumer discretionary stocks, such as retailers, have also enjoyed the benefit of purchasing inventory with a stronger currency.
- The Fund has increased its equity market exposure to be near its largest exposure over the last three years. The focus is on stocks and industries with a high level of earnings visibility, such as defensive industrials like healthcare and companies with steady, annuity style earnings. The Fund has added consumer discretionary stocks and the banks owing to the relative strength of the Australian economy. As the global cyclical stocks have already run strongly the Fund believes a pull back in prices is warranted before adding exposure, or at least until the quality of June half earnings can be assessed.

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