

Monthly Investment Report

Antares Lodestar Absolute Return Trust Australian Shares

Market Review

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- Early January gains were erased by month end as selling pressure resulted in the ASX 200 Accumulation Index recording its largest monthly fall since November 2008 to close down 6.2%.
- Australia underperformed the US S&P 500 which declined by 3.7%. The Euro Stoxx was down by 6.3% and the MSCI Asia ex Japan Index fell by 6.4%. Most markets gave back their December gains. The VIX index of implied volatility broke 18 for the first time since May 2008 then rebounded to 24.6 by month end as equities endured selling pressure.
- Policy risk seemed to be at the core of market concerns, such as the tightening of monetary policy in China and the possibility that the Obama administration will introduce tougher banking regulations. The prospect of China moderating its monetary stimulus impacted commodity prices and resulted in the local Resources sector falling by 9.4% in January. Although Obama's proposal had a negative effect on sentiment the local banks did not underperform (Banks Index -4.3%). Global markets are also concerned about Greece's fiscal crisis which resulted in its long bond yield rising by 108bp during January, a 365bp spread over the German benchmark.
- Despite the consternation over Chinese economic policy, spot iron ore prices were supported by tight physical markets. By contrast base metals were dragged lower, with zinc (-17.2%) registering the largest decline.
- The Energy sector (-9.8%) extended its relative downtrend for the eighth month. Spot WTI retreated by 8.2% over the month despite an extremely cold Northern Hemisphere winter and US refinery operating rates at two decade lows. The potential withdrawal of Chinese stimulus had a more pronounced effect on crude prices.
- Although the RBA did not meet in January, expectations of an imminent interest rate rise of 25bp were underpinned by strong employment, retail, and building approvals data. As we go to print, the RBA surprised the market by leaving rates unchanged in February. The currency immediately fell by ~ 1c to \$US 0.88.
- US data was mixed. Jobs, home sales and retail data disappointed the market while the ISM survey continued to highlight a manufacturing recovery. GDP rose by a 5.7% annualised rate (exp +4.8%) with most of the increase attributed to a slower drawdown in business inventories. The FOMC maintained its stance that interest rates would remain at "exceptionally" low levels for an extended period. The US dollar and US bond markets were firmer during January as risk appetite dissipated.

Portfolio Activity

- During January the Fund decreased its net exposure from 78% to 50% by month end. This move was consistent with the risks Lodestar saw developing in global markets that were highlighted in last month's Outlook. Essentially, the announcements from China in relation to tighter monetary policy settings unsettled markets. This was

further exacerbated by the Obama administration's stance on the degree and structure of leverage within the banking industry and in Europe, Greece's sovereign financial position became overly precarious.

- The main change to the portfolio was reducing the global cyclical component of the portfolio from 34% to 19%. A derivative strategy using S&P/ASX200 Index Puts was also implemented in order to protect capital. This resulted in minimising the gross exposure fall relative to the net exposure.

Fund Performance

Period ending 31.01.10	1m %	3m %	1yr %	2yr % p.a.	Since Inception % p.a.
Total Return	-3.64	-0.79	23.19	-2.16	0.35
Benchmark *	0.36	0.93	3.47	5.43	5.87
ASX200 Accum. ^	-6.18	-0.93	35.16	-5.78	-3.90

Performance returns are calculated net of management and performance fees and are 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 lost 3.6% (post fees) in January which was disappointing. The defensive action taken during January did soften the fall and the quarterly and six monthly performance remains pleasing against all asset classes.
- The Fund's volatility has continued to decline throughout 2009 and into 2010. It remains closer to Australian Government Bonds than it does to the Australian Sharemarket.

Positive Influences

Company	January Return %	Fund Position %
Ramsay Health Care	5.2	1.9
SMS Management	6.0	0.9
Flight Centre	7.6	0.8

- Ramsay Healthcare (RHC):** The market responded favourably to RHC's announcement that they had made their first (continental) European acquisition - a 57% stake in the French private hospital operator, Proclif. This is an important incremental step in the company's stated growth strategy. Late in the month RHC also upgraded FY10 earnings growth guidance to ~11%.
- SMS Technology (SMX):** Strong sales and staff utilisation through H110 have resulted in SMX re-hiring with the aim of exceeding FY08 levels in FY10. The company is well positioned for organic and acquisitive growth given its balance sheet strength and market position.
- Flight Centre (FLT):** The company upgraded its pre tax profit guidance for FY10 by ~ 25% which represents an

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increase of around 70% from their FY09 result. In response, shares in the company rallied 8% by month end.

Negative Influences

Company	January Return %	Fund Position %
BHP Billiton	-9.0	5.5
Newcrest Mining	-11.4	2.6
Wesfarmers	-12.8	2.2

- BHP Billiton (BHP):** The Dec '09 production report was mixed. The positive highlight being iron ore which improved by 10.5% vs. pcp and reflected the ramping up of project RGP4. This was offset somewhat by weaker than expected performances from the petroleum and coal divisions. Management was more upbeat than in the previous quarterly update but still cautious about the short term outlook. BHP share price weakness was mainly attributed to underlying commodity price weakness.
- Newcrest Mining (NCM):** The 2Q10 production and sales report was solid as cost performance was impressive and copper guidance was marginally increased. However, weakness in gold and copper during January weighed on NCM's performance. The company confirmed its FY10 guidance and remains our preferred gold exposure.
- Wesfarmers (WES):** WES weakness was mainly attributed to the flow on effect of commentary by Woolworths (WOW) during its quarterly sales report in which it highlighted competitive pressure in food retailing, mainly from Aldi. While Coles was not specifically cited as a competitive threat, the market is concerned about long term EBIT margin compression in the food retail business. WES has recently benefited from analyst upgrades to coal price assumptions and Coles supermarkets gaining traction.

Outlook

- As mentioned last month, the Chinese Government's proclamation of a tightening monetary stance has unsettled global cyclical stocks. In 2009 China was the predominant consumer of basic materials. The policy move on a stand alone basis is simply an appropriate response to strong growth. It endeavours to protect the Chinese economy from policy error or the speculative bubbles that have developed in China over the past year.
- The reason this announcement has had such a profound impact is that it coincides with the growing concern that the U.S economy is not recovering quickly enough. However, there are definitely signs that a US recovery is underway; fourth quarter GDP grew at an annualised rate of 4.7%. However this was mainly driven by the cessation of the destocking phase of the inventory cycle. The level of consumer activity in this data is of concern. The activity surveys point to the recovery being manufacturing centric with the non-manufacturing survey lagging. This is supported by the fact that the low \$US dollar is now

helping the competitiveness of the U.S economy. It has not however been of long enough duration to improve the poor employment environment in the economy.

- The US initial (unemployment) claims data are concerning given the trend is still increasing. In addition, the employment statistics appear to be stabilising without conclusively improving. The latest data show the unemployment rate in the U.S falling from 10% to 9.7% and the broader measure U6 falling from 17.3% to 16.5%, however both these numbers contain some statistical concerns and the market may need next month's data to determine if there has been a turning point. Meanwhile, the Congressional Budget Office has forecast that the unemployment rate will average 10% in CY10, and GDP growth will average 2.1% and 2.4% in CY10 and CY11 respectively. These forecasts do not imply a robust recovery, particularly as they are tracking against low bases in 2008 and 2009.
- U.S reporting season is well advanced with only 25% of S&P500 companies still to report. At this stage the profits (ex financials) are up 13.3% vs this time last year (Q4 2008) and 73% of companies have produced positive surprises vs market consensus. This is particularly encouraging as the all important revenue line generally improved. Previously Lodestar has highlighted that a significant portion of US corporate results earlier in the cycle had been driven largely by cost cutting. Lodestar also pointed out that profit estimates were achieved through margin expansion. This is only good to a certain point, as sustainable earnings growth projections need the backdrop of an improving economy. Hence, the share market started focusing on revenue growth as well. Stocks that met the market's profit expectations but missed at the revenue line have frequently met with investor selling in the current and previous reporting seasons.
- Some market commentators are comparing the US economy with that of Japan ten years ago, based on the economy being export lead with weak consumers and good corporate profit experiences. This is interesting as these parallels are definitely valid. What is discouraging is that the Japanese sharemarket still lost ground over the decade. The recovery in the key US economy cannot drive the sharemarket significantly higher until improving statistics start to feed into employment growth. The US consumption expenditure is around 70% of GDP thus statistics such as the University of Michigan Consumer Sentiment indicator, initial claims and official employment data will be increasingly important in ensuing months.
- The Greek economic situation is now in sharp global focus. Greece only produces about 2% of Eurozone's GDP. The reason Greece is receiving so much attention is that: 1) there is a fear of contagion into more important economies such as Spain, 2) if the rest of Europe is forced to bail out Greece it will force Greece and others to instil significantly greater fiscal discipline on their respective economies, and 3) the market is developing significant concerns regarding global growth projections, particularly as the key single driver (China) has started implementing financial disciplines (tighter lending policy).
- The contagion affect has already begun with the PIGS (Portugal, Italy, Greece and Spain) Credit Default Swap* spreads in Jan/Feb blowing out to exceed the crisis levels

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last seen in October 2008. As mentioned in last month's report this has ramifications for the pricing of sovereign bond holdings by major institutions globally. The fiscal discipline imposed on the above countries is certainly not pro growth for Eurozone, especially if a bail out for Greece et al is required. The likely imposition of wage freezes in Greece has been met with strike action. Thus there is early evidence of economic dislocation.

- In a very short period of time the market has become quite concerned about the fragility of the global economy, i.e. the economic recovery is proving more anaemic than markets would have expected by now. Against this backdrop sharemarket consolidation and / or sector rotation may occur.
- In Australia there was a significant event in early February. The Reserve Bank of Australia decided not to increase rates for a record fourth consecutive time. This is a positive development for the Australian sharemarket as it indicates that the RBA monetary policy will not be too aggressive. This is an administration that was particularly hawkish with policy leading into the Global Financial Crisis. The RBA continued to raise official interest rates twice when consumer sentiment had already fallen significantly.
- Reporting season has commenced in Australia. The results and the company guidance will be of heightened significance this year. Even at this early stage of the year the market has received several profit warnings and upgrades from disparate corporate sectors. The Australian and global economies have had a volatile time over the past two years with most regions having some

sort of recovery in the past six months. The divergent locations, industries and levels of management expertise should result in a reporting season that will be more varied than normal. Stock picking will be of prime importance this year. Valuations are moderate and earnings expectations are set at a very high level for financial year 2011.

** A Credit Default Swap is a contract between two parties. It is similar to buying insurance against a "credit event" on a bond, where for various reasons the bond payments are not made. The "event" can be failure to pay, reference credit undergoing restructuring, bankruptcy or a credit rating downgrade. Thus, in the case of Greece and other European countries at the moment, the perceived risk of default or other such credit events has increased significantly. As these Swaps can be traded the price moves reflecting the probability of a credit event. These Swaps can be used for hedging or speculation depending on whether the buyer actually holds the underlying security or not.*

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