

Dear Investor,

Please find attached our June 2008 Quarterly Investor Report for the Selector Fund.

Over the past quarter, global financial markets have been rocked by a multitude of shocks that have caused havoc amongst financial investors. Volatility in daily share price movements has been nothing short of extraordinarily. It has not been an easy time and as much as one as tried to dodge the “landmines” highlighted in our December 2007 Quarterly Report, fear and panic has spared few.

Over the following pages we have attempted to shed light on how we see the world at present. We have also provided an insight into the collection of businesses that the Fund holds and our reasoning for staying put despite share price gyrations.

Be assured that we take nothing for granted and that the macro events that we speak of may have further to go. That said, while we don't underestimate these global and domestic challenges, the significant value now so clearly and firmly on offer across a multitude of businesses and market sectors has reached a level that is frankly too compelling to ignore.

In short, we think the selling is overdone and while we have previously spoken about the importance of patient investing, it carries even greater weight during these times. For our part, we aim to stay firmly focused on the task at hand.

Finally we would like to thank you for ongoing investment in the Fund and should you wish to discuss any aspect of the report please do not hesitate to contact either Tony Scenna or Corey Vincent .

Regards

Tony Scenna
Corey Vincent
Selector Funds Management

Table of Contents

Fund Performance	Page 3
Macro, where to from here?	Page 5
Equities, a long-term opportunity?	Page 9
Stock selection, looking through to the portfolio	Page 13
Aristocrat Leisure	Page 14
Cabcharge	Page 15
Cochlear	Page 17
Flight Centre	Page 18
Kagara	Page 19
Macquarie Group	Page 20
Primary Healthcare	Page 22
Pharmaxis	Page 23
Telstra	Page 24
Tatts Group	Page 26
Governments – Perfecting the art of stealing	Page 27
Oil notes	Page 30
Uranium	Page 31
Acknowledgements	Page 32
Company Diary	Page 34
Portfolio Statistics	Page 35
Appendix 1 Reported Net profit and Issued Capital	Page 36

FUND PERFORMANCE

Since inception in December 2004 the Fund has delivered a compound annual return of 7.1% to 30 June 2008 (inclusive of \$0.0924 cents in distributions), compared to the All Ordinaries Accumulation Index, which has compounded at 14.1% over the same period.

Statistics page 33 *SFM*

Year of two halves

In this quarterly newsletter we aim to focus on two specific areas of discussion, being the “macro” and “micro” factors at work. The macro issues are bleak at present and we try to pinpoint the “X” factors currently at play in global economies and how this has impacted the Australian equities market.

By “micro” we are referring to the process of selecting company specific stocks. Here we will try to provide added transparency, by highlighting businesses held by the Fund. We share our thoughts as to why we have chosen to invest and stay invested during periods of macro “uncertainty”.

Self-doubt runs high during these periods and adhering to a consistent investment process is made even tougher as stock prices continue their unrelenting decline. It is becoming increasingly apparent that now is the time to look through the fear and loathing, not for a bottom, but with an eye to the value and opportunities on hand. And to achieve this, you need a consistent investment process that has worked in the past, will work in the future and one that you have ultimate confidence in.

Today the Fund is providing a bumpy ride. From this we do not hide. A concentrated portfolio is designed to give out performance. But when an across the board macro driven de-rating occurs, such as we are witnessing today, underperformance can be experienced for a time.

What is important now are the individual stocks that make up the Fund and their ability to shine in the future. The stock specific profiles provided below and the attached appendix aim to demonstrate why we have confidence in these businesses and ultimately the Fund’s ability to deliver.

We finish off our newsletter with separate comments on Governments, Uranium and Oil. We bid a sad farewell to ROC Oil CEO Dr John Doran who passed away suddenly on 27 June 2008. And finally, we note legendary investor Sir John Templeton who also passed away. *SFM*

Big Picture

First up, we'll take aim at the macro issues. Following a number of excellent performance periods stretching over three years, macro events skittled global financial markets during the latter part of calendar year 2007 and moved into over drive during the first half of 2008.

The speed and extent of the price to earnings ratio (PER) de-rating has stunned even the most experienced of investors. We are naturally disappointed that the Fund's unit price has suffered to the extent that it has. A quick glance at Table 1 below shows that the resources boom has so far, hidden or muffled the true extent of the damage inflicted on investors over the past year.

Table 1 Australian Index performance

Index	30 June 2007	1 Nov 2007	30 June 2008	Change Nov 07 peak %	Change Fin Year %
ASX All Ordinaries	6310	6853	5463	-20.3	-13.4
ASX 300 Industrials	9425	9869	6993	-29.1	-25.8
ASX 300 Resources	5337	6550	6511	-0.6	+22.0
ASX 300 Financials	7327	7832	5145	-34.3	-29.8
ASX Small Ordinaries	3978	4176	3178	-23.9	-20.1

Matters were not helped by our natural bias away from the more speculative resources sector where extraordinary gains were generated. The rise and rise of China and other developing nations has continued to fuel enormous demand for commodities and resource stocks in general. Most notably, the stunning surge in the fortunes of group's like Fortescue Metals (market capitalisation \$35 billion) along with coal and coal seam gas operators, typifies investors move away from more traditionally based industrial businesses to resources.

Not surprisingly, such euphoria now has the resources sector forming the largest component of the All Ordinaries Index, surpassing even financials. This is a situation not seen since the mid 1990's. In a rather ominous sign, Southern Cross Equities stockbroker, Charlie Aitkin, proclaimed to The Australian on 25 June 2008,

“Don't stand in the way of the resources train. This is the start of total market domination by resources”.

He may well have called the top of the resources run.

And while the Fund's own investments in resource-based businesses have delivered handsome returns over the initial 3-year holding period, the past six months has seen them languish as investors have sought richer rewards. We share some of the reasons why we remain steadfast in our view of the long-term investment case for these businesses later in the newsletter. **SFM**

Macro, where to from here?

As we wrote in our March 2008 quarterly newsletter, we are in very testing and volatile times. Indiscriminate selling, bordering on panic, has become common as investors try to deal with a plethora of conflicting macro “X” factors.

It has seemed to us that in ducking one bullet, many more have followed in rapid fire. Having come to terms with the first big “X” factor, the US sub-prime credit crunch, other conflicting macro issues are now attracting significant coverage. Today, we are faced with the real and perceived threat of rising global inflation, the rising price of crude oil and the growing concerns of world recession in developed countries. This trifecta has even the most battle hardened veteran investors concerned.

Macro No.1 is inflation. And this is our first point of discussion.

While the US economy may technically avert a recession, our own Reserve Bank Governor Glenn Stevens is walking a fine line with the local economy. Having lifted cash rates to avert an inflation blow off, there are growing concerns that the real economy, with or without the booming commodity sector, is now struggling.

Yet Governor Stevens remains firm that the Reserve Bank’s current course of action is right and that most international governments are now facing similar domestic concerns. This was reflected in a recent speech.

“Around much of the emerging world at the moment, the bigger problem seems to be neither the near or actual recession of the United States, nor the credit crunch about which we hear so much in the discussion of the major countries, but inflation. From Asia to Latin America to Africa, as well as in many of the industrial countries, we are hearing a lot more about inflation now.”

We acknowledge that higher prices have fed into the system and are likely to remain high. As a result, inflation has moved outside the prescriptive band applied by the Reserve Bank. This is to be expected when two major population pools, namely China and India undergo a long duration urbanisation build.

However, we believe the longer-term damage of slowing productivity and falling employment levels present a greater threat. We come to this conclusion by considering how likely the scenario that today’s inflation threat becomes stubbornly entrenched.

We are not solely focused on the consumer price index (CPI). As a measure of rising costs, the jump in CPI points to a worrisome trend, that in large part has been fuelled by a ground shift in many commodity prices for which Australia has a plentiful and geographically advantaged supply. But this represents only half the inflation equation.

For inflation to remain entrenched, the equation also requires strong GDP growth (well above average) and resultant wage increases that spiral upward with prices. Without strong GDP growth, unemployment will rise. We are less convinced that the economic evidence is pointing to strong GDP growth, globally or locally for that matter.

Firstly, we know that the consumer is a lead indicator of economic strength and with retail sales falling off a cliff this quarter, retailers are hurting.

Secondly, take a look at consumer and business sentiment. Both are at record lows here and overseas, underscoring the concerns many have of keeping their jobs at the same time that businesses are looking to cut costs. Prime examples are Citi, Starbucks and locally IAG announcing the shedding of thousands of jobs.

Thirdly, record oil prices are certainly a handbrake on growth. Maybe, this part of the argument is neutralised by the large role oil is already playing in driving prices and the resultant inflationary pressures.

Lastly, it is often worthwhile noting what is happening on the other side of the “ditch”. The economic news from New Zealand is grim at best with a sharp slowdown or even a recession now likely.

And in relation to Australia’s own GDP, having grown at 3% – 4% over the past decade, treasury statistics now forecast non farm domestic product growth of just 2.25%. None of this point to the boom conditions that can lead to a wage and price spiral required for surging inflation. Rather, they all suggest a slowing economic environment that should see GDP slow and employment rates fall as inflation peaks. The natural lag effect will also result in inflationary measures taking longer to subside.

In summary, we believe the economy can self correct without the need for additional rate hikes that are regretted later. We don’t think this fact is lost on Governor Stevens and while interest rates are unlikely to be cut in the near term, we are of the view that official cash rates have now peaked in this country.

Macro No.2 is oil. And this is our second point of discussion.

Many economists are calling oil the biggest “X” factor in global equity markets today. In a recent interview with Fortune Magazine, United States Presidential candidate, Barack Obama, sites energy policy and oil’s role as posing the gravest long-term threat to the US economy.

Oil has been a clear driver of equity markets of late, since it lies at the heart of the inflationary battle. And for now, inflation remains the central bankers' number one priority in all developed countries.

On the surface, the impact is relatively straightforward. If oil continues to track higher, equity markets and the US dollar will remain under pressure. As a result, the world is focused on oil. Many Governments are attempting to stabilise the price of oil with a coordinated response. Iran on the other hand, as a major oil exporter is happy to continue their sabre-rattling military antics.

It looks bleak but there may be some silver linings.

From our vantage point, today's oil price is being driven by a combination of supply and demand issues as well as pure investor speculation. And the way we see it, supply (finite but plentiful today), demand (price sensitive) and speculation (high) each pose a risk to the current oil price.

We remain sceptical of the impact of a coordinated global response on the supply side but note recent industry developments.

Each day Saudi Arabia pumps out a little more than 9.5M barrels of oil equivalent (BOE) or approximately 11% of the world's daily demand of 86M BOE. During June, Saudi Arabia announced a daily top up of 200,000 to 300,000 BOE, representing the first leg of the coordinated supply response. In addition, the Saudi's have indicated that staged capacity increases could see daily production reach 15M BOE by 2025. This is a surprisingly large increase and some question the ability to deliver on the claim. In any case this is not a short term solution.

With US demands consuming approximately 25% of world production or 22M BOE daily, soaring crude prices are derailing the US dollar and the wider economy. As the second leg of a supply side response, the US may release some of its 700M BOE strategic stockpile. The raw numbers however show that this also is not a long-term solution.

Even the Chinese have seen the need to act, surprising the markets with an increase to the cost of fuel at the domestic bowlers. Analysts have been just as quick to dismiss this initiative.

The Economist recently ran an article noting that the Russian supply of oil to global markets had been in a slow decline for the past two years. Not as a result of falling supply but rather through the lack of sufficient infrastructure. Capital expenditure has been neglected for a long period, coinciding with years of low crude prices. They noted that

finally, the wheels appear to be turning. The price surge has seen Russia willing to spend the roubles needed to increase domestic production capacity.

Even collectively, these supply changes may not be the short-term saviour hoped for. But don't underestimate the ability of market speculators to seize on other catalysts for forcing changes crude price futures, particularly during times of significant price speculation.

And what of oil demand?

Today, roughly 30% of market participants on the New York Mercantile Exchange (NYMEX) are identifiable market hedgers with a legitimate business purpose. That fact and a twenty-fold increase in capital flowing towards commodity futures during the past five years - growing at a rate of \$1 billion in contracts per day - point to a remarkable shift in how the price of futures is set, by virtue of who's around to set them.

And the number of paper oil barrels traded daily on NYMEX (and that's just the most regulated Exchange) is over three times the number of physical barrels consumed daily worldwide.

Yet, supply and demand of the physical product, by and large, has remained fairly stable. In 2005, global oil production was 84.6 M barrels per day, and consumption was 83.6 M. Today, those numbers are 86.5 M and 86.4 M respectively. That slight tightening does not seem to justify the tripling in prices.

At some point, if not now, high prices will curtail demand. Consumers will change their behaviour. A natural tipping point will occur. The 1970's oil shock curtailed demand and today's record oil prices will have a similar impact.

Anecdotal evidence suggests this is already happening. And judging by the rash of "plug in battery" announcements released by global vehicle manufacturers, the days of standard combustion engines look all but numbered.

And we are in no doubt that an alternative energy boom is searching for answers to energy substitution. Even Google has embarked on a major project called *RE>C*. This acronym denotes the goal of commercialising a renewable energy that is cheaper than coal.

Logic suggests to us that a top in oil will be put in place at some point down the track, offering some respite to the battered US dollar. Under such a scenario, equity markets would be seen in a more favourable light. Inflationary concerns may actually recede. This would most likely usher in a "bottoming" process in global equity markets. That may also

coincide with a low point in the US housing cycle and US growth. Until then, rising oil prices may well drive global equities and the US dollar lower

And the silver lining mentioned earlier?

1. If oil continues to drive higher it will eventually choke demand and self correct.
2. With a falling US dollar, US exporters are big winners, providing some strength at a time of economic weakness.
3. The continuing decline in equities, means quality companies are selling on price earnings ratios at multi-year lows. Risk is priced into equities and yields are rising. An excellent investing opportunity is emerging. This is discussed below.

And if you too are scratching your head about oil, it is worth remembering that The Economist ran with a cover story in March 1999 “*Drowning in Oil*”.

It predicted that the price of a barrel of oil, having already halved to \$US10,

“Might actually be too optimistic. We may be heading for \$US5”.

In fact, the price of oil hit \$US25 per barrel by December 1999.

Today, with oil trading at record levels of \$US144 per barrel, The Australian newspaper’s lead story under The Wall Street Journal section ran with the headline,

“Oil tipped to hit \$US200 by year-end”.

Some things never change. *SFM*

Equities – a long-term opportunity today?

That’s a quick overview of some macro “X” factors that have prevailed. We can now focus on how these “X” factors have impacted equity markets before delving into the “micro” or our stock selection discussion section.

Equity markets, unlike inflation, do not lag they lead. And typically, they lead well before events unfold. They price in the negatives well before the data is at hand and they lead a recovery well before the worst is actually over.

As we write, the Australian equities market is close to retesting the lows established in March 2008. That was a time of significant financial stress following the US Federal Reserve’s orchestrated takeover of investment bank Bear Stearns. The Fed subsequently

opened its lending window to investment banks in order to avert a major crisis of confidence in the global financial system.

However these and other events have not prevented global share markets experiencing a broad de-rating in price earnings ratios (PER) and an increasing risk premium for equities in general. The key issue is how much risk is now being priced into valuations. What can happen to the “E” for earnings in the equation? The fact that we are re-testing the lows of mid March 2008 would alone suggest significant risk is certainly being priced in.

We would also argue that the “E” has significant economic headwinds already priced in. We have high interest rates, high prices for commodities, consumer sentiment at record lows, retail sales are weak at best and inflation concerns are top of mind.

This is news to no one. Coupled with the fact that equity markets are a leading indicator, we would suggest that each of these “headwinds” are now largely priced into earnings expectations. Individual companies may have their own earnings issues, and they always will, but that is separate to the general de rating underway.

Chart 1 ASX Industrials prospective PE – rolling 12 months forward

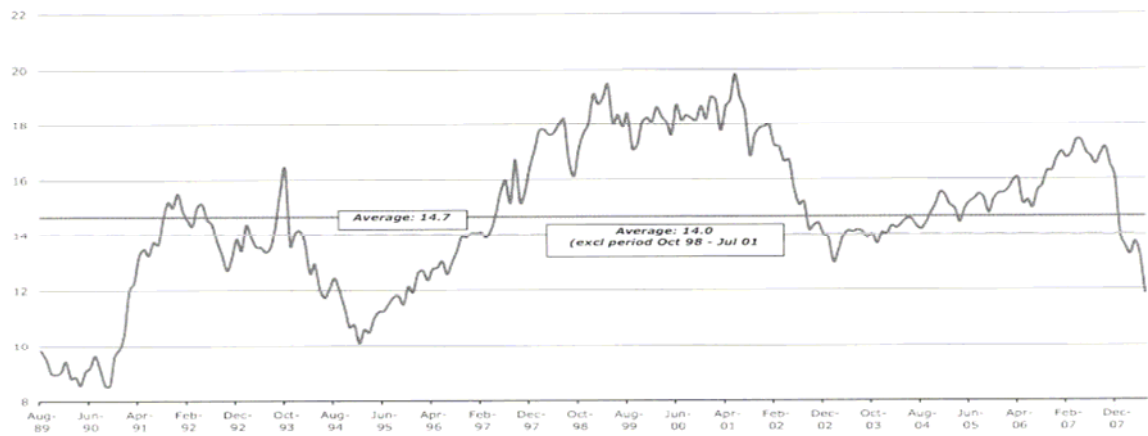
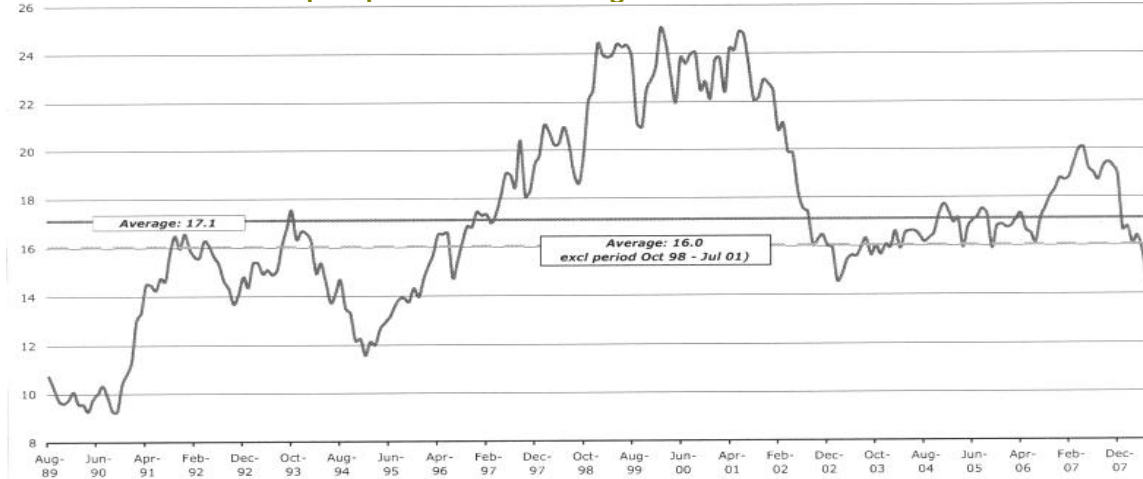


Chart 1 shows the Australian market is now trading on an average PER of 12 times future earnings. This is a 14-year low point against a long-term average - for the ASX 200 industrials going back to 1989 - of 14.7 times earnings. This suggests the market has priced in significant risk.

And in Chart 2, according to Goldman Sachs JBWere (GSJBW), if you remove banks, which have collectively recorded some of the Australian market’s biggest falls, today’s PER is around 14 times compared to a long term average of 16 times as illustrated below.

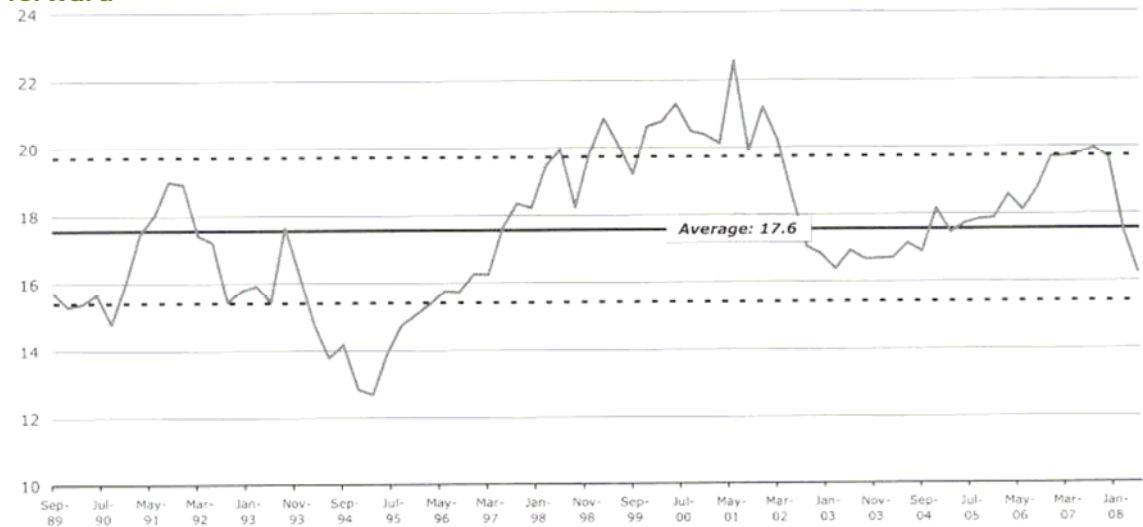
A general sector analysis shows large falls across the board have been recorded since 1 November 2007. Banks, Industrials, Property Trusts and Consumer Discretionary stocks have all fallen between 35% - 50% and more in some specific cases.

Chart 2 ASX Ex Banks prospective PE – rolling 12 months forward



Take the example of seasoned retailer Harvey Norman (HVN). This stock has fallen 60% in six months and now offers an attractive 5% yield. At every annual meeting we have attended, investors complain about Gerry Harvey’s miserly dividend policy. He is no longer an easy target on this basis. Watch for the insiders as a guide to buying this one as Harvey Norman has a history of picking up market share in down turns.

Chart 3 ASX Industrials Inflation adjusted PER – rolling 12 months forward



GSJBW noted that historically, equities trade on lower PER multiples during periods of

high inflation reflecting the increased yield on offer in bonds and fixed interest investments. So they adjusted the PER for inflation, using a forecast CPI of 4.4%. In Chart 3, this led to an adjusted PER of 16.3 times, compared to the long-term average of 17.6 times. In summary, the GSJBW view notes that the market appears undervalued from a historical PER perspective. And that's before yield is considered.

Yields move inversely to the PER. As the price drops, the cash yield rises. This is very apparent today and was highlighted in the Harvey Norman example. At the end of June a quick look through the ASX 300 revealed more than twenty companies on a PER of 10 or less and a cash yield of at least 7%.

Higher yields generally reflect higher risk. And the reality is that many high yielding investments will be chopped down by a declining "E", and their inability to maintain dividends. Some companies, however, like the Tatts Group - discussed a little later, have confirmed dividends will be maintained.

It becomes an attractive proposition when a low PER is combined with a high yield. If you can close your eyes to the capital side (growth) for a period, it's a far more rewarding and less stressful way to undertake long term investing. It's a matter of looking through individual situations to determine what is sustainable.

Our view is that risk and fear are now being priced into equities. This has occurred in an extremely short time frame and we expect continued volatility as is characteristic of high and low points in equity markets.

The Fund has not escaped the impact of this sell off. It is worth noting that the broad based and indiscriminate PER de-rating has reduced the total value of the Fund's portfolio holdings significantly more so than any individual profit downgrade. No businesses in the portfolio have had terminal operational issues.

With the knowledge that equity markets will at some point look through the macro issues, we remain of the view that now is not the time to exit equities on a wholesale basis. In fact, past experience tells us that these periods often provide outstanding investment opportunities. We have no special powers or are under any illusion that we can pick the low point in the market. Rather, we point out that a lot of negative news is now being priced in. At some point investor confidence will return. Our main focus is to sensibly position the portfolio for that time. *SFM*

Stock Selection – looking through to the portfolio

So far, we have discussed some of the bleak and conflicting signals in the macro economic environment and how they have impacted Australian equities in general. Here we take a closer look at a selection of investments held by the Fund.

Selector Funds Management Limited manages a long only, buy and hold, concentrated portfolio of Australian equities. This in itself is rather unique. In the modern age of where the typical fund manager bases investment decisions on replicating a share market index or holding large numbers of diversified businesses in order to ward off under performance is illogical at best and naïve at the extreme.

We think it makes more sense to identify and invest in companies that can deliver profit performance well into the future even when it is judged unfashionable or too risky by others. And it makes compelling sense when a broad market sell off occurs, Judging the success and performance of a business on share price action alone ignore the basic principle that share price will ultimately move in step with profitability.

Yet as is usually the way, it is at these extreme points that real value often emerges. In essence, today is a better investing environment even though performance statistics tell you otherwise. Table 2 lists in alphabetical order, 10 businesses that represent 80% of the Fund’s dollar value. The vertical columns represent 11 of the 21 business qualities, which make up our investment “roadmap”, plus how long Selector has held each business. Below this we outline some of the individual business characteristics and how they relate to the roadmap.

Table 2. 10 portfolio holdings, 11 roadmap qualities

	Individuals we trust	Track Record	Niche or Franchise	Free Cash flow	Re invest	Industry Position	ROE ROCE ROA	Low Debt	Manageable Cap Ex	Held Since
Aristocrat	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	2008
Cabcharge	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	2005
Cochlear	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	2004
Flight Centre	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	2004
Kagara	Yes	Yes	-	Yes	Yes	-	Yes	Yes	-	2004
Macquarie	Yes	Yes	Yes	Yes	Yes	Yes	Yes	-	Yes	2008
Primary HC	Yes	Yes	Yes	Yes	Yes	Yes	-	-	Yes	2008
Pharmaxis	Yes	Yes	Yes	-	Yes	-	-	Yes	Yes	2004
Telstra	Yes	Yes	Yes	Yes	Yes	Yes	Yes	-	-	2004
Tatts Group	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	2004

We include Appendix 1 to highlight how in the short run, share prices will overshoot and undershoot based on investor expectations but over the long run, higher profits do largely translate into higher share prices, particularly when a company’s issued share capital

remains relatively stable. In turn this translates into delivering long-term value for shareholders.

Our investment process is consistent and underscored by a strong belief that the detailed research and analysis we have undertaken on each investment case will translate into real earnings growth over the years.

Holding a random set of businesses may appear confusing and even too concentrated for some. But when we think of investing, we don't start with the notion of how do we construct a portfolio that is as painless to the investor as possible. Of course we would like it to be painless, but the world of business doesn't work like that. Painless also implies taking little or no risk and changing direction so often, in the hope of avoiding the unknown.

No, when we think of investing we aim to keep it really simple. We start and finish with a common belief that it just makes sense to hold a few good businesses, run by managers who are businesslike in their thinking and where the numbers that back up the business are compelling. Over time, the combination of both can translate into powerful investment outcomes.

In each business we seek to buy into, we look for the following investment qualities.

- ✓ Management team that can balance leadership skills with common sense
- ✓ Focus on a core business offering with scalable business qualities
- ✓ Attaining strong market leading position by embracing innovation
- ✓ Ability to grow from within (organic) aided by strategic acquisitions
- ✓ Investing where necessary, avoiding debt where possible
- ✓ Converting expectations into reality, revenues into high quality free cash flow
- ✓ Generating high returns on invested shareholder capital
- ✓ Keeping to an absolute minimum the release of new share capital
- ✓ Returning profits to shareholders via real earnings per share growth and dividends

Aristocrat Leisure (ALL)

While this is a recent addition to our portfolio, it is a company we know well and have researched over ten years.

Aristocrat is one of four globally dominant gaming machine manufacturers. The others include global leader, International Game Technology (IGT), WMS Industries and Bally Technologies.

The group dominates the market in Australia and has built up significant international presence spanning over fifty five years of operations.

At its core, Aristocrat has been an innovator of product and prepared to embrace sensible expansion. It is held in very high regard by gaming operators because of its exceptional array of quality product. Visually (equating to entertainment value) and algorithmically (equating to generating the highest win rate for players and highest return on capital invested for operators), Aristocrat machines have stood the test of time.

But above all, this is a high margin business. One of the current milestones set by management and highlighted on our business roadmap for the group, is for all geographical markets to achieve earnings before interest and tax (EBIT) margins of 40%. Not surprisingly, the business throws up exceptional quantities of free cash flows even after the significant reinvestment of profits into research and development.

Aristocrat shares have fallen from a high of \$17.68 to \$6.00 in a little over a year. Management are once again forecasting no earnings growth this year, making it the fourth flat year in a row. This has led to a raft of broker downgrades and as a contrarian we see significant risk already priced into the stock today.

Some Aristocrat characteristics that align with our roadmap include;

- ✓ Strong brand position
- ✓ Strong global position / regulatory approval in 90 countries, 200 jurisdictions
- ✓ High barriers to entry with few competitors
- ✓ Consistent operating history / track record
- ✓ Growing annuity type revenue streams
- ✓ Little debt / producing excellent free cash flow
- ✓ Management buying back stock / focused on delivering real earnings per share growth
- ✓ Takeover appeal
- ✓ Trading on historically low PE 12 / Yield 7.7%

Cabcharge (CAB)

Cabcharge is in a near monopoly position, operating payment systems linked to taxi fares. It is a position it has held since its establishment in 1976 under the watchful eye of founder and CEO Reg Kermode. Today more than 96% of the national fleet of 18,000 taxis are licensees of the Cabcharge payment service

Each time you pay for a taxi using a plastic card, a 10% surcharge is levied before GST. Cabcharge collects this fee and prudently rebates a portion (2.5%) to the independent taxi networks. The rebate funds the taxi networks business operations and keeps them onside.

Presently, Cabcharge not only owns the major payment service adopted in taxis but a fair chunk of the taxi network operators themselves, with an estimated 58% of the Sydney market and more than 35% in Victoria.

Even those that operate independently of Cabcharge have an historical connection with the group, remaining as major shareholders, with obvious vested interests in the company's financial well being.

We see continued growth being generated from the cash to card conversion of fare payments. Currently cash still makes up the lions' share of preferred payment with a 70% take. Plastic cards make up the remaining 30%, with the Cabcharge branded card representing 12% and the traditional bank cards the balance. We believe the ongoing rise in taxi fares will see this shift to card payment method continue.

Cabcharge continues to invest in the services provided to both taxi operators and networks as illustrated by the recent rollout of general packet radio service system commonly known as GPRS. Apart from making it easier to book jobs, by taking innovation leadership and offering the best available product, the company has been able to maintain clear market leadership.

This is a highly profitable business, generating operating margins in excess of 40% as well as providing an important and essential service within the community.

In contrast, Cabcharge's 2005 joint venture purchase of Westbus from administrators and its subsequent move into regional bus ownership was driven by a fundamental shift in the NSW State Government's funding model for this essential transport service.

In essence, Cabcharge receives a margin based on kilometres travelled and services provided rather than the actual fare box collected. Under this arrangement the State Government is responsible for costs including salaries, fuel and importantly bus upkeep and replacement, while efficiencies driven by Cabcharge management improves the joint venture partnerships' overall operating margin. Importantly, patronage demand drives new services, which in turn drives growth.

This is a lower margin business but with significant earnings protection and few competing players.

The Government currently subsidises buses to the tune of \$1 for each \$1 of fares collected. In contrast, train subsidies are running at \$5 for each dollar of fares collected. Public transport and associated infrastructure is a key imperative for the State Government and this metric is a key reason to ensure the bus system remains functional.

We believe more buses will be required to service more routes. Cabcharge has recently committed to building buses for government contracts at a pre-determined margin.

Some Cabcharge characteristics that align with our roadmap include;

- ✓ Dominant market leading “taxi” network position
- ✓ Strong brand awareness
- ✓ High barriers to entry
- ✓ Consistent operating history / track record
- ✓ High recurring revenue streams
- ✓ Growing the business through the cycle (Bus)
- ✓ Government funding working capital requirements
- ✓ Low capital requirement / high returns on capital funds employed
- ✓ Management team led by founder
- ✓ Shareholder base includes rival taxi network operators
- ✓ Takeover appeal
- ✓ Thematic appeal of getting cars off roads
- ✓ Low debt
- ✓ Highly attractive valuations / PE 14 / Yield 4.5%

Cochlear (COH)

A Cochlear implant surgically implanted into a hearing impaired infant’s inner ear can lead to normal speech and vocabulary by school age.

Cochlear is one of only a handful of companies approved in all developed markets to deliver this technology solution. It is also the global leader with an estimated market share of 70% because it sells a superior product with superior implant reliability. Reliability is absolutely crucial, because the internal component of a cochlear is implanted for life and cannot be easily removed.

Since its origins in 1982, Cochlear has led the hearing impaired field, with over 90,000 patients now carrying a cochlear implant device. The business enjoys wonderful financial metrics, including operating margins nearing 30%, a strong organic growth profile and a near bullet proof balance sheet. The annual incidence of profound hearing loss far outstrips implanted supply, leading to a large unmet clinical need and the basis of a highly sustainable growth profile.

More recently, the company has benefited from the growing body of clinical evidence proving conclusively that children and adults benefit from having two ears implanted rather than the traditional one. Commonly referred to as bilateral implantation, the trend is growing with over 15% of unit sales now bilateral.

While the hardware of a cochlear sits inside the body, the smarts that drive product functionality sit on the outside of the head. As new technologies and upgrades are introduced, the group's focus on making all implants backwards compatible (allows for previous implant recipients to receive software upgrades) remains a key distinguishing feature among its competitors.

Cochlear's commitment to research and development innovation and reinvestment in the re-engineering and scaling up of its supply chain side is all geared towards the business growing rapidly into the future.

Some Cochlear characteristics that align with our roadmap include;

- ✓ Global leader with 70% market share of cochlear implants
- ✓ High barriers to entry with few competitors
- ✓ Consistent operating history / track record
- ✓ Technological leader committed to ongoing innovation
- ✓ Operating in over 90 countries built on organic growth
- ✓ Global demand for implants remains significantly ahead of supply
- ✓ Management team investing into business to sustain a quantum jump in growth
- ✓ Takeover appeal high
- ✓ History of delivering strong high double digit net profit growth / strong cash generation
- ✓ No net debt
- ✓ Supplemented by historically low PE 19 / Yield 3.6%

Flight Centre (FLT)

We have followed the fortunes of this travel agent provider from its inception as a publicly listed company way back in 1995.

The current management team is still in place and from that initial period, the company's fortunes have blossomed with net profit expected to hit \$150M this year, compared to its first year prospectus target of \$12.0M. During this period, the group has had to contend with any number of external shocks including the events surrounding 9/11 and the international outbreak of Severe Acute Respiratory Syndrome (SARS).

Internally, mistakes made and attempts to privatise the group have largely been dealt with. Operationally Flight Centre is a scalable business, which carries no inventory, requires little in the way of working capital and enjoys excellent operating margins of circa 14% with a return on shareholders funds exceeding 20%.

The group has expanded internationally in over nine countries, gaining critical mass in a largely organic manner. Their footprint now extends both physically in over 1500 shopfronts, through the continual rollout of their flagship brand Flight Centre and the virtual world of internet sites that include; www.quickbeds.com.au and www.flightcentrehotels.com.au

Importantly, the management team have avoided the use of debt and continue to sit on a pile of company cash exceeding \$200M.

Despite its return to form and the release of umpteen profit upgrades since June 2007, investors have continued to shun the group. Having hit a record share price of \$32.48 on 4 January 2008, the shares have halved, making them undervalued in our opinion.

Some Flight Centre characteristics that align with our roadmap include;

- ✓ Founding management team in place / significant shareholders
- ✓ Consistent operating history / track record
- ✓ Driving global growth built upon a scalable offering
- ✓ Dominant domestic leading position / growing international presence
- ✓ Strong brand position enjoying economies of scale
- ✓ High cash generation / low working capital requirements
- ✓ Takeover appeal high
- ✓ No debt / significant cash holding
- ✓ Low forecast PE 9 / Yield 6%

Kagara (KZL)

We were initially attracted to the very high grade and low cost operations of Kagara when the zinc price was on its knees. If a project stacks up economically at low commodity prices then it can only benefit from higher prices.

Led by its founder and CEO Kim Robinson, Kagara has come of age. Back in 2002, an investment in Kagara was viewed as unfashionable and high risk. Today, its common sense business approach, based on an organic project development pipeline has seen the group enjoy strong cash flow, reduced debt levels, annual payment of dividends and the development of significant copper production.

Furthermore it is developing significant gold and nickel reserves and closing in on one of the world's largest undeveloped zinc deposits. Acquired for little capital outlay, at cycle lows, these projects each have the potential to be company transforming, yet carry little to no valuation on the balance sheet and are importantly all located in Australia.

In the case of the Admiral Bay zinc deposit located in Broome, West Australia, we are comforted in the knowledge that a world-class zinc resource is being proven up, once again, during times of price weakness. It provides the best stress test to the economics of the business case.

The Lounge Lizard nickel tenement purchased for \$25 million by Kagara in 2006 has come up trumps, with a 61,000 tonne resource deposit recently announced, carrying with it a base case market value of \$400 million. Management has flagged its intentions to sell this asset in the foreseeable future in order to focus its attention on its growing zinc, copper and gold operations. In comparison, Kagara's current market capitalisation of \$760M remains extremely light on, particularly when one considers the value tucked inside the group.

Our view is that patience will be handsomely rewarded, as the various assets on hand are developed and brought into production. During the half, Kagara's share price fell from highs of \$6.00 to \$3.50 in January 2008 driven by a weaker production profile due to unseasonably high rainfall, temporarily closing the local transport route. Like MD Kim Robinson who owns 16% of the group, we saw this as a buying opportunity.

Some Kagara characteristics that align with our roadmap include;

- ✓ Transformed from “start up” position to growing earnings profile
- ✓ Founding management team proven performers / significant shareholders
- ✓ Focused on driving low risk, organic growth
- ✓ High grade / low cost operator
- ✓ Contrarian approach in identifying and developing resource projects
- ✓ Asset rich / Future growth underpinned by number of projects coming to fruition
- ✓ Current market valuation ignoring significant embedded value residing within group
- ✓ Takeover appeal
- ✓ Low debt
- ✓ Dividend paying

Macquarie Group (MQG)

Macquarie Group is an increasingly diversified global investment bank that has growing streams of annuity income. Although its origins can be traced back to 1970, Macquarie

Bank opened its doors in 1985, following Federal Treasurer approval to operate a trading bank. From its inception, the group has sought to grow from within, seeking to exploit market and business opportunities in all types of conditions. It is a model that has worked well to date and from which others have tried to emulate.

And as the latest full year numbers indicate, Macquarie is pushing forward its business model globally, combining experienced long term staff and resources with local partners operating established businesses. This generates significant intellectual leverage in the markets in which it operates. Historically, rising staff numbers are a leading indicator of future growth for the group and over the past ten years, full time staff numbers have risen from 3,119 to 13,107. Offshore operations now account for 40% of total employee numbers while international income rose 14% to \$4.3 billion during 2008, representing more than 57% of total operating income.

Macquarie's capital position is well above prudential requirements, having raised significant new equity prior to the events of the global credit crisis. Historically, it now finds itself with excess capital and a Tier 1 ratio above 15%. Such a strong capital position places Macquarie in a unique position amongst global investment banks and allows the group to benefit and take advantage of opportunities that will flow from the current market fall out. Historically, Macquarie has a culture of investing and growing through the cycle. While others have shed staff during difficult periods, the group has remained steadfast in adapting to the economic conditions and opportunities at hand.

Macquarie's layered and integrated risk management procedures, while not fool proof, are amongst industry best worldwide. They encourage entrepreneurial attitudes referred internally as "freedom within boundaries", a legacy of the former CEO Allan Moss.

The credit crisis has provided an opportunity to invest in this market leader at very attractive valuation metrics. Short term, many revenue streams will be impacted by the credit crisis but on a forward price earnings ratio of 8 times we believe risk is priced in. And while we acknowledge that we have moved early in taking a position, we think we will be handsomely rewarded in time.

Some Macquarie characteristics that align with our roadmap include;

- ✓ Strong brand position
- ✓ Consistent operating history / track record
- ✓ Growing international presence
- ✓ Management team culture built on driving organic growth / significant shareholders
- ✓ Strong balance sheet position / Unique global position
- ✓ Experienced management team committed to investing through economic cycle

- ✓ History of exploiting cycle weakness
- ✓ Historically attractive forward PER 8
- ✓ Yield 6%

Primary Healthcare (PRY)

When Founder and CEO Dr Edmund Bateman considered swapping his medical hat for a business role some 25 years ago, the choice of which business to pursue was given considerable thought. The ideal business needed to be based on a proven model, was scaleable, enjoyed competitive advantages, operated in a favourable industry environment and their remained the opportunity to tackle a large market. In short, Dr Bateman stayed in his profession of medicine and undertook the role of commercialising medical practices, under the one roof, now commonly referred to as medical centres.

The Primary medical centre business model was established in 1985 with just one centre based in Brookvale, Sydney, followed by a listing onto the stock exchange in 1998. Having got the model right over the ensuing years, Primary's reach has extended to over 40 medical centres, treating over four million patients per annum. Based on providing affordable medical treatment in a cost effective manner, Primary's financial metrics are equally impressive with operating margins hitting 50% and maturing centres continuing to generate solid patient growth demand.

While the opportunity to acquire Primary shares at a fair price has been a difficult exercise for investors over this period, last years move by management to acquire its much larger rival, Symbion, was considered an opportunity too good to pass up. Perhaps so, but the credit crisis and the huge debt bill that the group has now picked up courtesy of its \$3.3 billion take over, has certainly weighed on investors.

The subsequent fall in share price, along with a heavily discounted rights issue, provided new investors with the opportunity to jump on board.

While we don't underestimate the significant task in merging the two groups, the Primary management team are proven performers and conservative operators at heart. If one were to look out a few years, we are likely to see a group with net profits hitting \$200 million, trading on a current PER of 10. And with Dr Bateman controlling 50 million shares the desire to succeed is high.

Some Primary characteristics that align with our roadmap include;

- ✓ Founding management team in place / proven performers / significant shareholders
- ✓ Consistent operating history / track record

- ✓ Dominant market position in private medical centres
- ✓ Ageing population demographics underpins long term positive trend in demand
- ✓ Company transforming strategic acquisition of Symbion assets opens up opportunity to drive significant long term earnings growth
- ✓ Business built on high operating margins / low working capital requirements
- ✓ Management committed to high dividend payout

Pharmaxis (PXS)

Pharmaxis is unique in Australian biotechnology terms because the company's business model is centred on retaining 100% ownership of the intellectual property developed rather than partnering or licensing out to third parties. In short, the Pharmaxis model is to own, drive and retain as much of the revenue streams its products generate.

The group's Aridol product is the world's first asthma diagnostic challenge test, with sales in Australia and Europe and final regulatory approval currently underway in the US. The group's second product Bronchitol, has completed pivotal Phase III trials in Bronchiectasis, achieving excellent results. Pharmaxis's third drug is centred on the treatment of Cystic Fibrosis and is also nearing completion, with Phase III trial results expected during the second quarter of 2009.

Aridol and Bronchitol are similarly based, but are titrated into the lungs differently to achieve two separate outcomes. Both formulations are composed of a naturally occurring sugar molecule called mannitol, which has been adopted in food products (considerable safety profile) and brain surgery (to reduce swelling) for many years. A key attraction of the product treatment is the way in which it works.

Bronchitol is a physical solution based on the simple properties of osmosis (movement of water from high concentration to low). Inhaled as a dry powder into the lungs, Bronchitol draws water to the airway surface of the damaged lungs, enabling the lungs cilia to beat and remove mucus, as is the case in healthy lungs. In patient categories with Bronchiectasis and Cystic Fibrosis, the inability to remove mucus from the lungs has a high mortality rate.

Bronchiectasis is a Chronic Obstructive Pulmonary Disease (COPD). COPD is the world's fourth largest killer and is often caused by smoking with no treatment available. Bronchitol is the first product to have successfully completed phase III trials for this disease and as a result, a filing for approval with the Australian Therapeutic Goods Administrator (TGA) is expected during the current quarter. European and US authorities have agreed to approve Bronchitol for Bronchiectasis, subject to a successful second phase III trial that is earmarked to start later this year.

Bronchiectasis and Cystic Fibrosis patients will use Bronchitol twice daily for the rest of their lives. The product is expected to sell for approximately \$6,000 per annum. Gross margins for Aridol and Bronchitol are high at around 80%, while input costs are largely restricted to the use of water and the active ingredient, mannitol. Intellectual property ownership offers a significant barrier to entry as does the company's large patent filings.

Pharmaxis remains extremely well funded, carries no debt and an excellent management and board, who have in the past, successfully developed and taken products to market. In our view, this company has overcome the all important product and regulatory risk but remaining risk lies in both the manufacturing and marketing of the key products.

Some Pharmaxis characteristics that align with our roadmap include;

- ✓ Founding management team in place / proven performers
- ✓ Growing pharmaceutical revenue streams
- ✓ Late stage product development pipeline
- ✓ Seeking 2009 market approval for Bronchitol product for treatment of Cystic Fibrosis
- ✓ High barriers to entry
- ✓ Long term defendable patent protection
- ✓ Significant unmet market needs / Significant market potential
- ✓ High margin business model
- ✓ Takeover appeal high
- ✓ Strong balance sheet position / no debt / \$110M in cash
- ✓ Management long term vision built on internal development / retaining 100% ownership of product pipeline
- ✓ Highly attractive business valuation

Telstra (TLS)

Put simply, Telstra is a business in transition - from old to new.

As the country's incumbent telecommunications carrier it is without peer, offering a full suite of services extending from its traditional monopoly based copper network to the newer offerings of mobile, broadband and pay television.

Telstra provides considerable defensive qualities as well as offering the growth. In our opinion, Sol Trujillo's arrival as CEO in 2005 and his "stakes in the ground" presentation to shareholders on 15 November 2005, was a significant inflection point for the group.

The current five year plan is both radical and necessary, a point not lost on media commentators and investors alike, who have pointed to the significant regulatory risks and massive capital expenditure required.

Others clearly see the need for change and the obvious competitive advantages that it promises. We firmly sit in the latter camp and there are grounds for optimism, despite the ongoing ructions calling for its break-up.

Most notably, management has embraced change and introduced innovation, while cutting costs. The headline numbers suggest little progress has yet been made, with net profit stagnant and margins under pressure.

However a closer look reveals a more promising outlook. Despite the transformation impact, the group continues to generate an operating profit after depreciation of \$6.2 billion on total revenues of \$24.5 billion. Margins have contracted but still stand at an impressive 25%, while at a time of maximum investment, returns on capital invested still remain attractive at 14%.

Operationally, the group has stolen a march on its competitors, grabbing the lion market share in all segments of the telecommunication sector, including 44% in total mobiles, 48% in the all important 3G mobile segment, 48% of internet broadband connections and an estimated 65% of the wireless broadband market. Pay TV operator Foxtel (owned 50% by Telstra) continues to gain traction, with subscriber numbers now exceeding 1.3 million, while the reliance on the traditional copper network income streams, including local call revenues are in slow decline.

While we don't underestimate the challenges ahead, we clearly see a way forward for a business that has the products, services and commitment to innovate. Sitting on a PE of 14.5 and yield of 6.7%, we would argue that the best is yet to come.

Some Telstra characteristics that align with our roadmap include;

- ✓ Dominant local telecommunications provider
- ✓ Strong suite of complimentary product / service offerings
- ✓ Management team / change agents / refocusing and rebasing business cost structure
- ✓ Maintains high barriers to entry
- ✓ Growing demand for new generational product offerings offsetting traditional services
- ✓ High margin business
- ✓ High quality recurring earnings
- ✓ Strong balance sheet
- ✓ Real earnings per share growth

- ✓ High sustainable yield 6.7%

Tatts Group (TTS)

As we note in a later article titled “perfecting the art of stealing”, we were blindsided by the Victorian Government’s recent decision not to allow Tatts, as one of the two incumbent gaming operators, to bid for a new licence post 2012.

While there was risk that this could happen, more galling was the decision of the Government not to pay compensation, despite the clearly stated claims for one. However, our recent meeting with CEO Dick McIlwain certainly put many of our concerns to rest.

While the pokies outcome was not desirable, it has cleared up any uncertainties overhanging the business. The Tatts business beyond 2012, will not include a Victorian gaming leg but it will certainly allow management the opportunity to maximise profits from this division without the added burden of funding a new licence.

Along with its wagering, lotteries and gaming monitoring services - which operate under long duration licences or in perpetuity as is the case with wagering - Tatts continues to pack a solid punch with revenues this year expected to hit \$3.1 billion and operating profits after depreciation of \$430 million.

Operating margins at 14% are somewhat masked by the high turnover nature of the lotteries business. More importantly, Tatts is a high cash generating business with considerable operating leverage.

While the current environment has created investor uncertainty, there are few more capable CEO’s around than McIlwain. Along with a low debt balance sheet and a high yielding investment, forecast at 8.7%, we would argue that these concerns have been well and truly over done.

Some Tatts Group characteristics that align with our roadmap include;

- ✓ Highly regarded CEO / proven shareholder friendly management team
- ✓ Industry dynamics in a state of flux / throwing up generational business opportunity
- ✓ Consistent operating history / track record
- ✓ High quality earnings base
- ✓ Low levels of working capital / strong return on funds employed
- ✓ Low debt levels / attractive PER 12 / Yield 8.7%

Next Quarter

In our next quarterly we aim to update investors on the balance of the Fund's investments including holdings in Australian Wealth Management, Iress Market Technology, NIB Holdings, QBE Insurance, Reece, Roc Oil, Resmed and Seek. *SFM*

Comment on Governments – “Perfecting the art of stealing”

When the Mauritanian Government notified Woodside Petroleum in February 2006 that it was seeking supplementary changes to the production sharing contracts surrounding its Chinguetti oil acreage, investors back home were thinking only one thing - Sovereign Risk.

As is often the way, when you play on foreign soil, success often brings with it a new set of problems. In this case, Woodside and its partners, resolved to settle the dispute by agreeing to pay the Mauritanian Government a “Chinguetti project bonus” of \$100 million dollars. All was forgiven and a revised contract was signed.

In other parts of the world, sovereign risk comes in many other shades of grey. There is the dark grey, almost black scenario where Governments simply confiscate assets. Take for instance Venezuela's nationalisation of the Orinoco oil field in May 2007. Not content with how the cake was being divvied up, foreigners including Exxon, Chevron, Total, BP and Norway's Statoil had assets worth \$US12 billion frozen. President Hugo Chavez simply re-wrote the rules.

All but Exxon and Chevron agreed. Instead they chose a different route to fight, seeking compensation claims via the international courts. And judging by his recent comments on the matter, it's hard to see Chavez losing this one.

"If you freeze us, if you really manage to freeze us, if you damage us, then we will hurt you. Do you know how? We are not going to send oil to the United States."

As things stand, Venezuela is the U.S.'s fourth largest oil supplier behind Canada, Saudi Arabia and Mexico, accounting for 12% of U.S crude oil imports.

And then there are the lighter shades of grey, where the real threat of losing one's assets leads to a new set of rules, applied to future ventures. For gold producer Kingsgate Consolidated, whose operations are based in Thailand, it was simply a case of the Thai authorities wanting a more “equitable” stake when it came to reviewing new exploration applications. Compared to Venezuela this amounted to nothing more than skinned knees.

While it's easy to single out the rogue states, it may come as a surprise to some back home that one of the biggest commercial risks facing businesses today, alongside competition, inflation and even interest rates, is the invisible hand of governments.

In recent months, our respective State Governments have handed down Budgets extending out over the next four years to 2012. In every instance the urgent need for new infrastructure and essential services, such as health and transport were top of mind. And not surprisingly, having failed to provide sufficient maintenance capital expenditure over the past decade, large quantities of investment are now required.

Table 3: State Government budget deficits

Budget Handed Down	Net Debt 2008	Net Debt 2012
South Australia	\$82 M	\$2 B
Queensland	\$22 B gross	\$46 B gross
NSW	\$22 B	\$42 B
Victoria	\$4 B	\$23 B
WA	\$3 B	\$11 B

As the Table 3 above highlights, this comes at a huge price and it's called debt. While the level of debt represents only one data point on a State Governments balance sheet, it goes some way to explaining some recent disturbing developments affecting business.

As we will explain below, in each instance rules were changed, consultation was non-existent and businesses left to pick up the tab. In a rogue state, the cries of sovereign risk would be heard far and wide. Unfortunately for businesses and investors alike, not only do Governments not get it, they seem to be exploiting it.

Victorian Premier, John Brumby's recent decision to dismantle the existing gaming machine ("pokies") structure after the expiry of current licences in 2012 is a noteworthy example.

His decision to allow operators to directly bid and own gaming machines has effectively ended the role of duopoly operators Tabcorp and the Tatts Group. And while the share price thrashing that followed that decision on 10 April 2008 may have caught many on the back foot, what really shocked investors was the Government's view "that neither Tattersall's nor Tabcorp are entitled to compensation".

In both instances, a licence compensation figure of \$598M had been aired in the public arena under the continuous disclosure regime and included in Tabcorp's original prospectus in 1994. It was generally accepted in the public domain, that both operators could claim compensation under a set formula, if another party received a gaming licence.

Straight shooting Tatts CEO Dick McIlwain believes this *“cute little argument to avoid compensation is disgusting”*.

No one argues that licence renewals carry risk. But by seemingly misleading public markets and thousands of shareholders, Brumby has put everyone on notice. According to McIlwain, doing business in Victoria carries enormous political risk. And we would find it difficult to argue the toss.

It is clear that Tabcorp will appeal and Tatts will follow. What is not clear is how the new pokies structure will work and whether the Government, in snubbing the incumbents, have a game plan that will actually work. Our bet is that Brumby has pulled the wrong rein (excuse the pun) and that the Government may have a serious funding gap in relation to both the gaming machine and upcoming wagering licence renewal process. And don't expect either Tabcorp or Tatts to ride to the Government's rescue.

Over in Western Australia, it must have felt like déjà vu for LNG operator Woodside Petroleum. This time it was the Rudd Labour Government handing down a decision that blindsided them.

In this year's budget, the Federal Government has seen fit to remove an oil excise exemption that applied to condensate (light liquid crude oil) produced from hydrocarbon gas reserves from the North West Shelf and onshore Australia.

By removing this “tax loophole”, the Government has awarded itself a tax grab of \$564 million next year and some \$2.5 billion over the next four years.

As Woodside CEO Don Voelte noted in a press release,

“the decision to introduce a condensate excise was made without any consultation with the company”.

Sour grapes perhaps but Voelte also adds,

“This is not a loophole which is being closed, or a free ride which has come to an end. This is a negotiated fiscal arrangement, which formed the basis of Australia's largest resource development. We have lived up to our commitments under this arrangement.”

Suffice to say that Woodside is considering its position.

Not to be outdone, the Queensland Premier has also latched onto the resources boom. Having failed miserably to provide necessary infrastructure for years, it now has its hand out.

Coal royalties in Queensland are set to rise from 7% to 10% on production worth more than \$100 per tonne. And in a fortuitous set of circumstances for the Government, the explosive growth in coal demand has resulted in all coal types selling well north of that figure. In fact, on its own numbers, the Government expects royalties to triple from \$1.0 billion to \$3.2 billion over the next twelve months, making it one of the biggest contributors to State Government coffers.

So next time your thoughts turn to sovereign risk, consider the predicament of many local businesses, who now find themselves sharing their spoils with a new found silent partner – Governments. *SFM*

Other Oil notes of interest: Russia & Saudi Arabi

It's amazing the conspiracy theories going around on oil.

The 11 June 2008 Forbes Magazine article "*The Energy Underworld*" we read RosUkrEnergo, a trading company set up by Gazprom, Russia's biggest oil and gas company, serves primarily to skim off profits from the gas trade.

"We are talking about the gas supply of Ukraine,"

says Tom Mayne, a researcher for Global Witness, a London-based non-governmental organisation that tracks corruption.

"Eighty percent of Russian gas that goes to Europe goes through Ukraine, so it's vital that we know who is controlling the gas, else we could find ourselves at the whim of potentially undesirable elements."

"International organised criminals control significant positions in the global energy and strategic materials markets,"

noted Attorney General Michael Mukasey in April when announcing a new Justice Department strategy to combat organised crime.

"They are expanding their holdings in these sectors, which corrupts the normal functioning of these markets and may have a destabilizing effect on U.S. geopolitical interests." SFM

On 18 June 2008, Glen Mumford writing for The Australian Financial Review titled an article "*Overlooked: Key positive in oil surge*". The article was based on research by Morgan Stanley on "*the monumental transfer of wealth to oil exporters*".

It suggested that Saudi Arabian oil receipts were running at \$US1 billion per day and at \$US135 a barrel, the value of proven oil reserves in the Gulf Co-operation Council was \$US65 trillion compared to a global capitalisation of equity indices of \$US50 trillion.

These countries are finding it impossible to consume these receipts. Mumford suggested much of OPEC's current account surplus of \$US500 billion in 2008 will find its way into Sovereign Wealth Funds (SWF's). Receipts will in the first instance go into sovereign bonds. Morgan Stanley argues this is partly the reason why long-term interest rates have been driven to generational lows. They expect that once these Funds see signs of an improving global economic recovery, equities will be the next major beneficiary.

Morgan Stanley suggests that the prospect of several hundred billion dollars of SWF inflows competing with institutional and mutual fund demand may lead to a stronger for longer surge in global equities. *SFM*

Uranium - A New Beginning

During the latter half of the 1990's, we had the opportunity to attend a presentation by Paladin Energy CEO John Borshoff on the merits of uranium and the changing nature of the industry. Back then, Borshoff struggled to get an audience and even the mere mention of the words uranium and mining in the same sentence, was enough to kill off any decent conversation on the subject.

Fast forward some ten years and the situation is in complete contrast. Borshoff's Paladin now finds itself in front of a growing audience, with a market capitalisation approaching \$4 billion.

We recently caught up with Borshoff to get his take on things and came away believing that uranium mining will be at the forefront of discussion during the coming decade. While our Government may see little political merit in opening up the nuclear debate, foreign countries appear to be embracing this option with open arms.

BHP Billiton's Graeme Hunt, President Uranium and Olympic Dam Development, recently commented that "The world is well on its way to consuming as much energy in the next 25 years as it has consumed throughout modern history". Today, there are some 441 reactors, operating in 30 countries, producing 17% of global electricity demand. There are another 33 reactors under construction and a further 316 planned and proposed reactors to be built out to 2030. France, the world leader, generates 78% of its electricity through nuclear, along with Belgium at 54%, and Sweden at 48%. The US and UK sit at roughly 17% and are increasingly leaning towards reactivating nuclear power plans.

Safety ranks as a key emotive concern but the evidence would suggest otherwise. More pressing for governments is the realisation that change is necessary to tackle climate issues and uranium as an energy source is one of the very few energy alternatives that can produce non-greenhouse gas-emitting power to satisfy base load electricity needs.

As for Paladin, the timing couldn't have been better. Having kicked started production during 2007 at its wholly owned Langer Heinrich, Namibian project, the group is on track to lift uranium production from an initial run rate of 2.6m/lb to a 2012 planned target of 9.3m/lb. At that level of production, Paladin would be contributing some 9% of global supply and aiming to earn a gross margin of \$50 per pound or about \$450 million in operating profits.

All in all, the stars seem to be aligning for both the uranium industry and Paladin but a \$4 billion market capitalisation is a big ask at present. From our vantage point we would suggest that an open mind be kept on the world's growing need for alternative energy and the role that uranium may ultimately play. *SFM*

Acknowledgement

During June, it was with much sadness that we learned of the passing of ROC Oil Founder and CEO Dr John Doran. The sudden loss of an individual is always a shock but especially so when they carry the enormous respect of employees and shareholders alike.

We would be the first to acknowledge that Doran was unique, in fact one of a kind. Our first company meeting with both Doran and CFO Bruce Clement took place at ROC's Sydney based office on 17 November 2005. We had attended the group's annual meeting earlier that same year, where it became very apparent to us that this was no ordinary shareholder get together. What struck us almost immediately was Doran's preparedness to talk candidly of the business and the enormous respect he held for all shareholders, irrespective of shareholding size or stature.

His presentations were insightful, entertaining and always relevant. He avoided popular views, built a business on a "sensibly contrary" approach and never waived from his commitment to tell things as they were – the good and the bad. He always gave us his time, responding openly and honestly. But above all he could be trusted, a commodity rarer than oil itself.

He leaves the company in very good hands but the void left will be very sorely missed by all. *SFM*

And finally

Sir John Templeton, the legendary mutual fund manager who was a pioneer of international investing and later committed much of his fortune to scientific and religious causes, has died. He was aged 95.

Martin Flanagan, chief executive of mutual fund company Invesco, was the chief operating officer at Templeton, Galbraith & Hansberger in 1980's. He believes Templeton was *“one of a kind”*.

After graduating in 1934, Templeton set off on a world tour that exposed him to many countries and cultures before he returned to the US and a job on Wall Street.

When World War II began in 1939, Sir John put that global experience into practise. He borrowed money to buy 104 companies selling at \$US1 a share or less, including 34 companies in bankruptcy. Only four turned out to be worthless.

Mr Flanagan recalled that Sir John exhibited a similar conviction during the 1987 stock market crash. It was Sir John's practise to leave the office just before noon to exercise, take lunch and study. When he returned an anxious Mr Flanagan told Sir John that the market was falling apart. Sir John took it all in his stride.

“The bad news”

Mr Flanagan remembers him saying,

“is we're in a bear market. The good news is it's almost over. Let's find stocks to buy”.

Added Mr Flanagan:

“today you could see that was an obvious thing to do. At the time it was not obvious at all. To have that kind of conviction and leadership is absolutely unique”.

Some things never change. **SFM**

COMPANIES VISITED DURING THE 4th QUARTER 2007-2008

	QBE	QBE Insurance Group AGM	04/04/08
	KZL	Kagara management presentation	08/04/08
	AUW	Australian Wealth Management conference briefing	09/04/08
	NUF	Nufarm conference briefing	09/04/08
	BBP	Babcock & Brown Power conference briefing	09/04/08
	CAB	Cabcharge conference briefing	09/04/08
	PXS	Pharmaxis conference call	16/04/08
	CAN	Coal & Allied AGM	18/04/08
	WES	Wesfarmers investors open day	22/04/08
	TLS	Telstra communication day conference briefing	29/04/08
	SGT	Optus communications day conference briefing	29/04/08
	N/A	Foxtel communications day conference briefing	29/04/08
	SEK	Seek communications day conference briefing	29/04/08
May			
	ALL	Aristocrat Leisure management meeting	01/05/08
	WPL	Woodside Petroleum AGM	01/05/08
	PRY	Primary Healthcare management meeting	01/05/08
	RMD	Resmed conference call	02/05/08
	MIG	Macquarie Infrastructure Group conference briefing	07/05/08
	BHP	BHP Billiton Olympic Dam presentation	07/05/08
	PAN	Panaust conference briefing	07/05/08
	FXJ	Fairfax conference briefing	07/05/08
	ALL	Aristocrat Leisure conference briefing	07/05/08
	PRY	Primary Healthcare conference briefing	07/05/08
	AAX	Ausenco conference briefing	07/05/08
	ROC	ROC Oil AGM	08/05/08
	RMD	Resmed conference briefing	08/05/08
	IRE	Iress conference briefing	08/05/08
	FMG	Fortescue Metals conference briefing	08/05/08
	WBC	Westpac Banking conference briefing	08/05/08
	TLS	Telstra conference briefing	09/05/08
	COH	Cochlear conference briefing	09/05/08
	NXS	Nexus Energy conference briefing	09/05/08
	ROC	ROC Oil conference briefing	09/05/08
	QGC	Queensland Gas conference briefing	09/05/08
	SHG	Sunshine Gas conference briefing	09/05/08
	PXS	Pharmaxis site visit	15/05/08
	NHF	NIB Holdings management meeting	19/05/08
	MQG	Macquarie Group results briefing	20/05/08
	KYC	Keycorp site visit	23/05/08
	TTS	Tatts Group management site visit	27/05/08
	CAB	Cabcharge site visit	29/05/08
	N/A	Coin management briefing	29/05/08
	BNB	Babcock & Brown AGM	30/05/08
June			
	NCM	Newcrest Mining conference briefing	03/06/08
	SBM	St Barbara conference briefing	03/06/08
	OGC	Oceanagold conference briefing	03/06/08
	SGX	Sino Gold Mining conference briefing	03/06/08
	PRY	Primary Healthcare site visit	04/06/08
	SRX	Sirtex site visit	04/06/08
	BNB	Babcock & Brown site visit	09/06/08
	ROC	ROC Oil site visit	16/06/08
	PDN	Paladin Energy management meeting	19/06/08
	AUW	Australian Wealth Management management meeting	20/06/08
	HVN	Harvey Norman Holdings management site visit	26/06/08

FUND REPORT as at 30 June 2008

Issued by Selector Funds Management Limited ABN 85 102 756 347, AFSL 225 316. The investment information in this Fund report is historical and refers to the period to 30 June 2008. **Past performance is not an indicator of future performance** for this fund.

PERFORMANCE SUMMARY

	3 months (%)	6 months (%)	1 Year (%)	Compound Annual Return		
				2 Year (%)	3 Year (%)	Inception ¹ (%)
Total	-15.95	-39.57	-35.94	-11.75	0.91	7.13
Distribution	1.46	1.05	1.12	1.12	1.59	1.84
Growth	-17.41	-40.62	-37.06	-12.87	-0.68	5.29
S&P/ ASX All Ordinaries Accumulation Index	-0.63	-15.22	-12.12	7.00	12.45	14.18

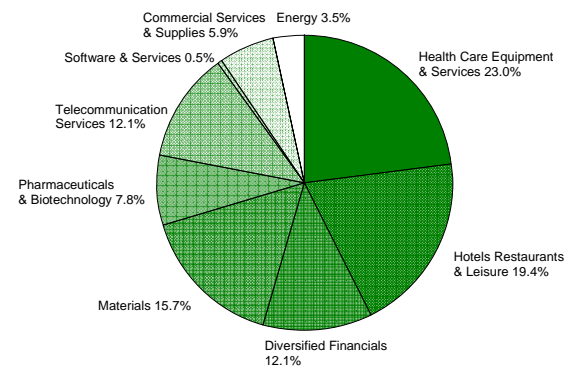
Returns are calculated using exit prices, and are calculated after all fees have been deducted with distributions included and no allowance made for tax. The 'distribution' component represents the amount paid by way of distribution, including net realised capital gains.

1. Inception date - 1 November 2004

MONTHLY DETAIL (past 12 months)

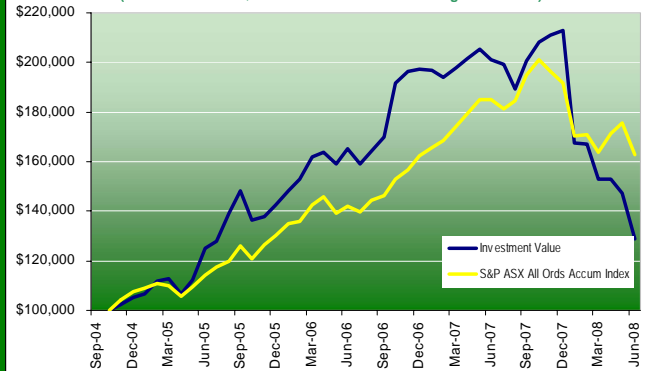
Month ending	Exit Price (\$)	Distribution per Unit (\$)	Month Gain (%) Fund	Compound Inception Gain (%) Fund	Index Level	Month Gain (%) Index	Compound Inception Gain (%) Index
30 Jun 08	1.2078	0.0215	-12.70	7.13	34,336	-7.32	14.18
31 May 08	1.4081	-	-3.53	11.45	37,046	2.45	17.00
30 Apr 08	1.4596	-	-0.19	12.89	36,159	4.64	16.62
31 Mar 08	1.4624	-	-8.28	13.26	34,554	-4.11	15.51
29 Feb 08	1.5944	-	-0.39	16.63	36,036	0.26	17.40
31 Jan 08	1.6006	-	-21.31	17.21	35,942	-11.25	17.77
31 Dec 07	2.0340	-	0.93	26.96	40,498	-2.36	22.83
30 Nov 07	2.0153	-	1.28	27.42	41,478	-2.35	24.49
31 Oct 07	1.9898	-	3.86	27.72	42,478	3.07	26.23
30 Sep 07	1.9158	-	5.92	26.97	41,211	5.78	25.78
31 Aug 07	1.8087	-	-4.88	25.29	38,961	1.70	24.14
31 Jul 07	1.9015	-	-0.91	28.48	38,310	-1.94	24.20

Sector Breakdown



Investment Growth

(based on an initial \$100K investment and all earnings reinvested)



To receive an Information Memorandum

Phone: 61 2 9241 5830, email corey@selectorfund.com.au or visit the website: www.selectorfund.com.au

Applications for units can only be made on the application form in the Information Memorandum (IM) dated 15 October 2004 and Supplementary Information Memorandum (SIM) dated 1 January 2006. Potential investors should consider the IM and SIM before deciding whether to invest in the Fund.

This document provides general information only and is not financial product advice. It does not take into account your individual objectives, financial situation or needs. Information used in this publication, is believed to be accurate. However, subject to any contrary provision in any applicable law, neither Selector Funds Management Limited nor any of its related parties, their employees or directors, provides any warranty of accuracy or reliability in relation to such information or accepts any liability to any person who relies on it.

NPAT / Issued Capital History

Date	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	% Change
Aristocrat															
NPAT \$'M				41.1	58.8	64.9	86	80.2	-106	142.1	244.3	240	247.9	247	501.0%
Issued Capital (m)				417.3	419.6	422.6	451.2	456.3	470.2	476.9	470.5	467.7	464.3	462.6	10.9%
Share Price \$				0.93	2.80	5.54	6.91	5.31	1.31	4.75	11.60	12.88	14.37	6.42	590.3%
Australian Wealth Capital															
NPAT \$'M											14.0	20.1	57.4	72.0	414.3%
Issued Capital (m)											74.30	560.50	564.88	616.50	729.7%
Share Price \$											1.14	2.44	2.66	1.30	14.0%
Cabcharge															
NPAT \$'M						10.9	12.5	16.1	20.2	23.1	27.8	38	51.8	65	496.3%
Issued Capital (m)						107.7	109.4	145.3	112.8	113.5	113.5	112.2	119	120.4	11.8%
Share Price \$						2.12	3.68	2.72	2.95	3.44	4.50	6.36	12.41	8.20	286.8%
Cochlear															
NPAT \$'M	7.1	10.8	10.8	13.3	16.3	20.2	31.2	40.1	58.2	36.8	60.8	86.4	107.6	115	1519.7%
Issued Capital (m)	50	50	50	50	50.5	51.1	52	52.5	53.1	54.2	54.1	54.6	54.8	55	10.0%
Share Price \$	2.50	3.35	4.30	6.27	12.00	28.76	39.00	34.05	32.30	22.72	39.00	54.63	61.00	43.65	1646.0%
Flight Centre															
NPAT \$'M	9	11.9	14.9	18.3	27.9	40.3	42.8	62	70	81.9	76.9	79.9	106.9	148	1544.4%
Issued Capital (m)	78.6	78.6	78.8	78.8	80.9	82	85.5	88.1	93.3	93.6	93.9	94.3	98.8	98.8	25.7%
Share Price \$	0.95	1.92	3.59	2.85	7.18	18.70	27.63	26.90	21.74	18.87	13.83	9.81	19.20	16.67	1654.7%
Kagara															
NPAT \$'M					-0.163	-0.196	-1.054	-1.958	-2.5	3.4	10.5	35.5	89.8	89	2517.6%
Issued Capital (m)					41.9	48.8	70.6	134.5	146.8	163	165.9	187.3	215.2	216.4	416.5%
Share Price \$					0.25	0.28	0.28	0.44	0.56	0.92	1.20	4.15	6.38	4.60	1740.0%
* NPAT growth based on 2004-08 period															
Macquarie Group															
NPAT \$'M	76.1	93	117	141	165	210	242	250	333	494	812	916	1463	1803	2269.3%
Issued Capital (m)	128	139	151	158	161	171	175	198	204	216	224	232	254	275	114.8%
Share Price \$	4.80	5.78	8.50	14.35	19.10	26.40	27.63	33.26	24.70	35.80	48.03	64.68	82.75	52.82	1000.4%

Primary Healthcare													
NPAT \$'M			4.1	5.4	6.3	6.3	12.6	18	37.6	47.5	56.9	53	1192.7%
Issued Capital (m)			64.9	82.5	83.1	98.6	101.2	103.2	118.9	123.2	125.4	142.2	119.1%
Share Price \$			1.81	4.16	3.29	2.90	4.11	6.58	8.60	9.18	5.20	5.20	187.3%
<i>* NPAT growth pre Symbion acquisition</i>													
Reece													
NPAT \$'M	11.9	17.2	27.4	38.8	28.2	42.5	46.7	61.5	75.7	86.8	103.5	115	866.4%
Issued Capital (m)	99.9	99.9	99.9	99.9	99.9	99.9	99.9	99.9	99.9	99.9	99.9	99.9	0.0%
Share Price	1.77	2.04	3.20	3.54	4.00	7.50	7.00	8.25	12.90	15.35	28.05	21.00	1086.4%
Resmed													
NPAT \$US 'M			16.1	22.2	29.9	37.6	45.7	57.3	73.8	108.6	125.8	135	738.5%
Issued Capital (m)			31.1	32.3	33.5	34.1	34.4	35.1	72.5	77.9	79.9	78.8	153.4%
Share Price \$A			1.65	2.33	5.19	2.57	2.99	3.66	4.29	6.20	4.83	3.63	120.0%
Seek													
NPAT \$'M									19.2	34.1	55.5	76.4	297.9%
Issued Capital (m)									281	281	288	288	2.5%
Share Price \$									2.38	5.35	7.38	5.00	110.1%
Telstra													
NPAT \$'B		3.00	3.486	3.7	4.1	3.66	3.4	4.1	4.4	3.2	3.3	3.3	10.0%
Issued Capital (b)		12.88	12.88	12.88	12.88	12.88	12.88	12.63	12.44	12.42	12.42	12.42	-3.6%
Share Price \$		3.30	8.66	6.78	5.38	4.66	4.40	5.03	5.06	3.68	4.59	4.24	28.5%
Tatts Group													
NPAT \$'M									105.6	128.5	248.4	265	150.9%
Issued Capital (m)									706.6	706.6	1258.7	1265.3	79.1%
Share Price \$									2.90	2.79	4.66	2.35	-19.0%

Comment

The following table illustrates, simplistically the relationship that can exist between a company's reported net profit, the number of shares it has on issue and its traded share price.

We compare each company's net profit starting point - being the first year with profits shown, with its ending net profit estimate for 2008.

The percentage profit growth over the period is shown in the last column which can be compared to the company's growth in shares on issue and share price performance

Those companies that have delivered substantial net profit growth, with little earnings dilution have also enjoyed share price performance largely in line with profit growth. Cochlear, Aristocrat, Flight Centre and Reece are a few examples

Those that have largely performed on the top line but not as well on the share price front, perhaps reflect investor concerns that may be over done. These could include Cabcharge, Tatts Group, Seek, Resmed, Primary Healthcare and Macquarie Group

Finally, one can note the significant swings in share prices over the years, but if the right businesses, run by the right managers are identified and held over the long run, share price performance should follow.