

# Five Oceans World Fund - Wholesale

## Fund report and commentary – 31 March 2008

Performance	3 months (%)	6 months (%)	1 year (%)	Inception <sup>1</sup> (%)
Fund return (gross) <sup>^</sup>	-5.36	-7.28	0.12	2.43
Fund return (net) <sup>#</sup>	-5.66	-8.04	-2.02	0.76
UBSA Bank Bill Index	1.82	3.59	6.99	6.71
MSCI Unhedged \$A	-12.52	-13.97	-14.38	-5.05

<sup>1</sup>Inception date: 3 July 2006

<sup>^</sup>Gross returns assume the reinvestment of distributions and exclude the impact of ongoing management fees. No allowance is made for tax.

<sup>#</sup>Net fund returns are calculated after fees have been deducted, assuming reinvestment of distributions. No allowance is made for tax.

Past performance is not a reliable indicator of future performance.

### Market review

The year has started extremely nervously for equity markets, with global markets down over 9% in aggregate for January alone! For those who were having trouble refocusing after the Christmas break the announcement by Societe Generale, that they had been the victims of a fraud by one of their traders to the tune of €4.9 billion, provided a wake-up jolt. The unwinding of this major position against the backdrop of an already weakened financial sector did little to help overall market sentiment or provide hope for a quick turnaround to the global financial sector's malaise.

The US Federal Reserve was extremely busy through the quarter, announcing three rate cuts that moved the Fed Funds Rate from 4.25% to 2.25%, in a move to stabilize a wounded financial sector and head-off an economy that appeared to be heading into recession. Economic growth in the US slowed to a near standstill in the final quarter of 2007 as fallout from the credit crunch, rising oil prices, the housing slump and rising unemployment took their toll, and expectations are that the US economy is now in recession.

Another indication of the severity of the current situation, during the quarter, was the purchase of a failing Bear Stearns by JP Morgan, with the support of the Fed, who provided backing for Bear Stearns' assets. The Fed also undertook to lend up to \$200 billion of Treasury securities to investment banks in return for illiquid mortgage-backed securities, in a further move to improve liquidity in the banking system. Both these moves took the Fed into new strategic territory and re-enforced the severity of the current situation.

In a reversal from last year, the contagion spread to the emerging markets with China and India both down over 20% for the quarter as global growth shows signs of slowing across the board. The Australia market also was down over 15%, as the realisation of the impact that tighter credit conditions would have for our own financial sector took hold. The US which has been at the forefront of these issues was one of the better relative performers, down just under 10% for the quarter. The Australian dollar finished the quarter down against the Euro and Yen but up slightly against the US dollar.

From a sectoral perspective, energy and precious metals related stocks were the best of a bad bunch and in reality, there was across the board weakness in most sectors.

### Fund performance

Overall, the fund finished down 5.61% for the March quarter, during a quarter when global markets, as measured by the MSCI World Index in \$A, finished down 12.52%. The main contributor to performance during the quarter was the portfolio's index hedges, which provided an offset against the impact of falling markets. These hedges totalled approximately 25% of the portfolios value and covered a number of European and US markets.

From a stock specific perspective Iluca, Western Digital, Singapore Exchange, Bloomsbury, Estee Lauder, and Zimmer all contributed positively to the portfolio while European Minerals, Intel, AXA Philips were the major detractors.

### Fund activity

The market awaits clarifying events to sort through its current dilemma which is set between two opposing views; the short cycle view maintains the current underlying framework for economic growth remains largely intact while the long cycle view dictates that the current market turbulence is signalling fundamental changes to economic structure.

In light of weakening global growth, a perception that rates may be peaking in Australia and continued general risk aversion, we reduced \$A exposure in the portfolio to around 33% by quarter end.

The question we are grappling with currently is that whilst the news has been bad, the market is still skirting a serious correction. The question is has all the bad news been discounted and if not, what additional negative will drive it below current levels? Will it be some acceleration in economic decline, a serious challenge to the survival of a "too big to fail" institution, questions over Chinese growth or the less obvious, slow but incessant loss of liquidity through the de-leveraging of the financial system? Alternatively, from the current weak equity market levels, might a serious bear rally be launched by better than expected outcomes against a backdrop of low expectations?

We continue to grapple with these issues and continue to maintain a cautious stance in the make-up of the portfolio. The portfolio's net exposure to equities sat at 32.5% at quarter end.

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## Consumer

The consumer discretionary sector endured some heavy selling in second half 2007 as concerns regarding the ability of developing economies to maintain their consumption levels arose. Valuations look very attractive at current levels but like all stocks currently, the question mark is over how future earnings will look. We own a range of strong franchises in this sector including Coach Inc, Yum! Brands and Best Buy.

Consumer staples have performed relatively well given their defensive characteristics. We hold two cosmetic companies; US based Estee Lauder and Brazilian based Natura Cosmetics. We sold out of Wal-Mart during the quarter as it had reached our valuation target.

## Financials

Financials experienced their worst quarter since 2002 on the back of further write-downs, stretched balance sheets and illiquidity in credit markets. Our strategy regarding stocks has been to largely avoid financials, and find a collection of attractive franchises across a range of sectors at reasonable prices that are reasonably positioned to avoid structural downdrafts.

We own two financial companies in AXA and Anglo Irish Bank, but maintain an offsetting basket hedge on the US financial services sector against these positions.

## Energy and Commodities

Materials were the best performing sector last year and has continued to hold this position through the first quarter of 2008. This performance has been supported by a number of factors; including strong commodity prices, exposure to the developing world (China and India), and their higher growth rates, and Merger and Acquisition activity.

On the commodity front, we are focused on Aluminium. Aluminium is intriguing as its pricing dynamics are more complex than other metals, making it not a simple commodity play. Aluminium is, unlike other traded metals, an intermediate product, processed from raw alumina. A significant part of its value is derived from the highly energy intensive smelting process. A number of Chinese smelters are not economic at high energy prices and we believe that part of that capacity will be withdrawn in the near future supporting aluminium prices. We continue to build positioning in Alumina Ltd, a pure play global alumina company, and we believe, a low cost and growth enabled competitor.

We initiated a position in Australian mineral sands miner Iluka Resources during the quarter. The company announced a rights issue as part of its recent earnings result. We continue to believe in the profitability and growth of its titanium and zircon operations and have participated in this capital raising. The additional capital will guarantee its growth underpinning the commercialisation of the world class Murray and Eucla Basin deposits.

Basic Energy Services reported a strengthening in its underlying environment within oil/gas rig servicing. This environment has been driven by strong energy prices coupled with a cold US winter. Basic Energy remains a core holding for the fund. We exited Western Digital during February after the stock reached our target price.

Western Digital had executed a flawless strategy over 2007 as it expanded into high margin high growth areas such as branded memory products, notebook and server based disk drives.

## Technology and Telecoms

We continue to hold Nokia whose business turnaround continues to exceed expectations although we did lighten the position in order to take some profits given its solid performance in the past 18 months. The company remains confident in its ability to gain further market share over 2008 and is very well positioned in the world's fastest growing markets. Nokia's franchise in developed markets had been in decline for the past three years due to a weak product portfolio but this was offset by increased demand from developing markets for low cost phones. Nokia is clearly benefiting from a revitalised product range, combined with having built an extraordinary distribution and logistics system through China and India. It manufactures within those markets, with state of the art logistics and a cost structure below local competitors, while retaining brand equity.

Telecoms generally had a poor quarter notwithstanding their perceived defensive capabilities. We own positions in Vodafone, Telecom Austria and French companies, Iliad and Neuf Cegetel. Neuf Cegetel is a French wireline telecom services provider and a mobile virtual network operator offering a range of services to consumers, enterprises and wholesale customers. Our position has benefited from a bid from Vivendi's SFR mobile phone division, which currently owns 40.5 percent of Neuf Cegetel, to buy the rest of the company at €36.50.

In summary, we continue to look for opportunities to increase our exposure to the markets in a prudent manner based on our fundamental research but remain highly cautious given the continued malaise affecting global markets.

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## Top five long positions

	Region	Sector	Weight (%)
Iluka Resources	Australia	Materials	3.42
Iamgold Corporation	Canada	Materials	3.22
AXA SA	France	Financials	3.09
Emerson Electric Company	United States	Industrials	2.93
European Minerals Corporation	Canada	Materials	2.88

## Sector exposures

	Net weight* (%)
Retailing	2.99
Banks	0.73
Insurance	3.09
Technology Hardware & Equipment	3.79
Automobile Components	3.45
Telecommunication Services	2.71
Commercial Services & Supplies	-0.19
Consumer Durables & Apparel	0.57
Household & Personal Products	2.09
Consumer Services	1.02
Energy	5.25
Materials	11.94
Capital Goods	5.99
Software & Services	3.24
Food & Staples Retailing	-0.27
Health Care & Equipment	4.81
Pharmaceuticals, Biotechnology & Life Science	3.26
Media	1.28
Semiconductors & Semiconductor Equipment	3.03
Real Estate	-2.30
Transportation	0.42
Unit Trusts	0.46
Sector / Market Hedges	-22.31
Cash and Forwards	64.95

## Regional exposures

	Net weight* (%)
Asia ex Japan	0.00
Europe	11.98
Japan	0.59
North America	8.81
Canada	6.10
Australia	5.32
UK	3.93
Emerging Countries	-1.68
Cash & Forwards	64.95
Total	100.00

## Portfolio structure

	Weight (%)
Long positions	68.24
Short positions	-33.19
Net equity exposure <sup>#</sup>	35.05
Gross equity exposure <sup>^</sup>	101.43

\*May not add to 100% due to rounding.

<sup>#</sup>Net equity exposure is the net equity exposure of the portfolio after short equity positions are deducted from long equity positions.

<sup>^</sup>Gross weight is the percentage of the gross equity exposure of the portfolio. Gross equity exposure is the total of the long and short equity positions in the portfolio.

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