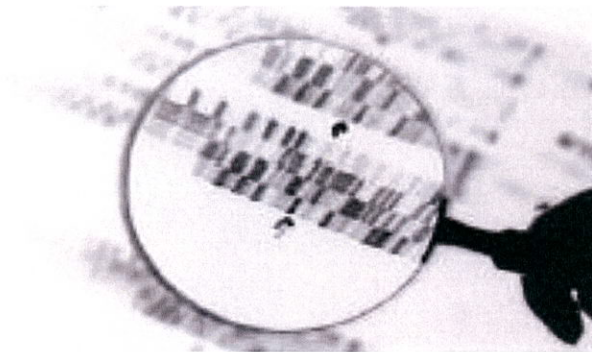


Concentrated Income Equities Strategy

eQRsecurities

Australian Equities Research



September 2010

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Australian Equities Research

Strategy Overview

Objective

- eQR Securities in conjunction with BT Financial Group equities research provides strategic equities investment support in the form of the Concentrated Income Equities Strategy. The objective is to assist in building and managing portfolios that aim to outperform the average yield of the S&P / ASX 200 Index over a rolling 3 year period with the potential for capital growth.

Style

- Our equities investment philosophy is built upon focusing on high quality companies that are attractively priced to their medium to long term earnings and cash flow capacity.
- The primary investment universe is the S&P/ASX 200 with the additional filter criteria being companies must have a minimum market capitalisation and annual turnover of \$A400m). This reduces the initial universe by approximately 10-20 companies.
- We believe a portfolio of 8-12 stocks adequately achieves an effective balance between reducing stock specific risk and delivering portfolio efficiency. This approach also allows the investment team to focus on a smaller number of higher conviction investment positions. It is our belief that the risk-return trade-off can be optimised by knowing fewer companies very well rather than many companies superficially.
- Due to the portfolio's concentrated positions, the strategy focuses on high quality, blue chip stocks.

Philosophy

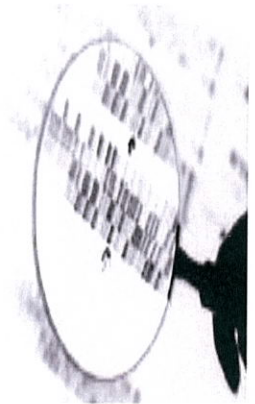
- Centric to the eQR Securities equities research philosophy is the view that establishing and maintaining a structured process to identify securities with strong fundamentals, low probability of 'failing' and a favourable earnings outlook relative to the broader index will allow market inefficiencies to be exploited through an investment cycle, and assist with long term income strategies.
- A robust risk management framework is essential in identifying securities with key fail points, both on a relative and absolute basis. Investment decisions should focus on the need for capital preservation and a sustainable risk adjusted returns through an investment cycle over the medium to longer term.
- A deep understanding of investment markets, prevailing economic conditions and company fundamentals, and applying this to a disciplined stock review process in our view provides the potential for a superior investment outcome over the long term. It also provides the framework in which we can minimise the risk of loss. Deeply embedded into the equities selection process is the focus to look beyond short-term market dynamics and focus on long-term macro thematic and the impact on financial asset market risks and returns on stocks and industries. We typically model our analysis up to ten years into the future.

Strategy Overview

Philosophy Con't

- All investment strategies and investment decisions are governed by an investment committee that provides oversight to ensure decisions are consistent, structured and unbiased and to ensure appropriate investment due diligence framework is maintained at all times. The below diagram summarises the overarching Investment & Governance committee:

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"eQR Securities believes stocks with strong free cash flows, high returns on equity and invested capital and a history of consistent dividends that are attractively priced relative to their long term valuation provide attractive income opportunities."



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The Investment Process: 5 steps

Step 1

- (a) **Define Universe** – S&P/ASX200 with a focus on “blue Chip” companies.
- (b) **Qualitative stock evaluation guidelines**
In selecting stocks for its universe, consideration will be given to a number of factors including, but not necessarily restricted to, the following:
 - i. **(segment and position)** industry prospects and potential for the company to achieve moderate growth rates;
 - ii. **(key differentiating factors)** what is unique about the company and/or its product or services. Robustness of the company’s business model and ability to achieve growth in its earnings and valuation;
 - iii. **(management and Board)** experience, capability and achievements in relevant field;
 - iv. **(track record)** ability to achieve targets, make successful acquisitions;
 - v. **(financial stability)** gearing, interest cover, cash balances, cash flow;
 - vi. **(earnings outlook)** whether the company is able to achieve moderate earnings growth that will enable it to maintain and deliver steadily increasing dividends/distributions;
 - vii. **(likely share price catalysts)** short and long-term;
 - viii. **(valuation);** current price against valuation/price target
 - ix. **(key risks);** and
 - x. **(market sentiment)** sector outlook.

Step 1

- Define Universe & Initial Qualitative evaluation

Step 2

- Risk Management Framework: filter out high risk exposure

Step 3

- Valuation, fundamentals and Yield assessment

Step 4

- Sector Weightings

Step 5

- Portfolio construction

The Investment Process

Step 2

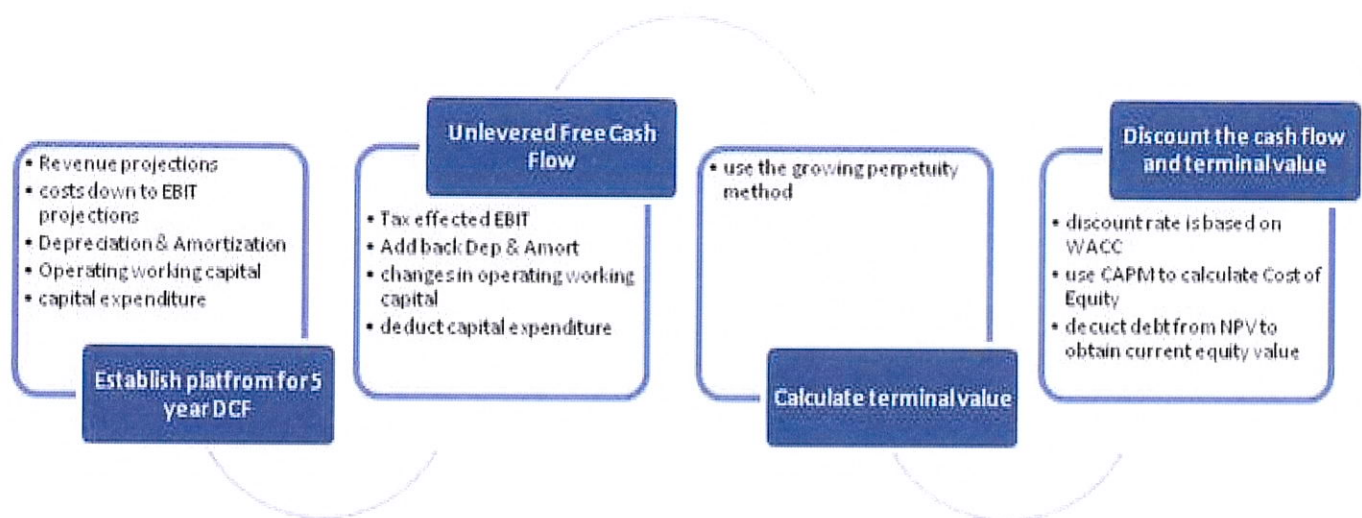
- Apply the Risk Management Framework (**RMF**) to the S&P/ASX 200 universe. The RMF identifies and ranks stocks both on a relative and absolute basis according to key fundamental risk metrics. It is a dynamic risk management framework which can be adjusted in accordance with market fundamentals and stress - tested on a monthly basis. The RMF also gives consideration to Environmental, Social & Governance (ESG) factors.

Step 3

- Valuation, Fundamentals and Yield assessment.
- Apply the eQR Securities Quantitative Lens and DCF filter to ascertain attractively valued, high yielding securities (adjusted for risk using the eQR Securities Risk management Framework as highlighted in step 2). eQR Securities believes stocks with strong free cash flows, high returns on equity and invested capital, a robust earnings outlook, competitive market position and a history of consistent dividends that are attractively priced relative to their long term valuation provide attractive income opportunities.
- An understanding of the operational environment the company operates in via utilisation of a Porter style industry analysis is also conducted.. This involves:

- i. An analysis of the attractiveness of the industry and the resilience of profit margins in the face of competition.
- ii. Defining the long-term growth rates across volume and price for the industry. This helps provide clarity around how sustainable current earnings' growth rates are and how realistic future growth estimates may be.
- iii. Individual companies are reviewed for the strength of their industry positioning. Analysis of the company's management, products/services, strategy and capital position.
- iv. Identification of stock specific risk factors that may impact the delivery of future earnings. These risks centre around capital structure, regulatory risks, geographic risks, currency risk etc. Consensus earnings estimates are generally utilised in discounted cashflow (DCF) modelling (earnings may be adjusted or normalised for the annualised year four number to ensure that we believe this estimate clearly reflects the mid point in the company's earnings cycle).
- v. The flow chart over-page summarises the DCF valuation approach:

The Investment Process



Step 4

- Establish Target Sector Weights using the BT Financial Group Capital Markets Model.

Step 5

- Centric to the portfolio construction process is the application of Modern Portfolio Theory (MPT)². MPT is based on the theory that effective and measured portfolio diversification can lower the risk of the entire portfolio without compromising returns. The key concept in MPT is *Beta* or variance.

- MPT constructs portfolios by mixing securities with differing Betas to produce a portfolio with minimal Beta for the group of stocks as a whole, while allowing returns to potentially accumulate. MPT is applied via a process called Mean Variance

- Optimisation using a powerful mathematical modelling engine. This is a constrained process that incorporates sector exposure, market cap, stock specific limits and floors and thematic issues such as currency and balance sheet risks.

Portfolio Structure

Corporate Actions

- eQR Securities provides guidance on corporate actions in line with the interests of the investors who may hold those securities. The guidance provided does not factor in the specific tax positions or general circumstances of individual investors. (Investors should seek individual tax advice in relation to any corporation).

Tax Considerations

- All portfolio investment decisions are aligned with the broader portfolio strategy and objective. Whilst eQR Securities does not factor in the specific tax positions or general circumstances of individual investors, it may consider general tax implications in its decision making process so as to minimise potential tax implications where possible.
- Whilst the general strategy focuses on highly franked dividends, companies with outstanding income characteristics will also be considered during the investment process

Portfolio Construction Constraints:

Risk Measure	Constraint
Tracking Error – ex ante	3% to 5%
Minimum Market Capitalisation	\$400m
Minimum Annual Turnover	\$400m
Sector Target	+/- 18%
Maximum Overweight – ASX Top 20	Index weight + 7%
Maximum Overweight – ASX 20-60	Index weight + 5%
Maximum Overweight – ASX 60-140	Index weight + 5%
Max single stock weight	25%
Min Single Stock weight (at inception)	2%
Target annual portfolio turnover (p.a.)	<40%

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Dated: 2010

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- EQR, including contact details and services offered by it
- How EQR and its staff are remunerated
- How EQR deals with your complaints

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- (b) deal in each of the financial products referred to above (by arranging for another person to apply for, acquire, vary or dispose of those financial products).

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