CI BRUNSWICK FUND
QUARTERLY REPORT

Cooper Investors Pty Limited AFS Licence Number 221794 ABN 26 100 409 890

JUNE 2014

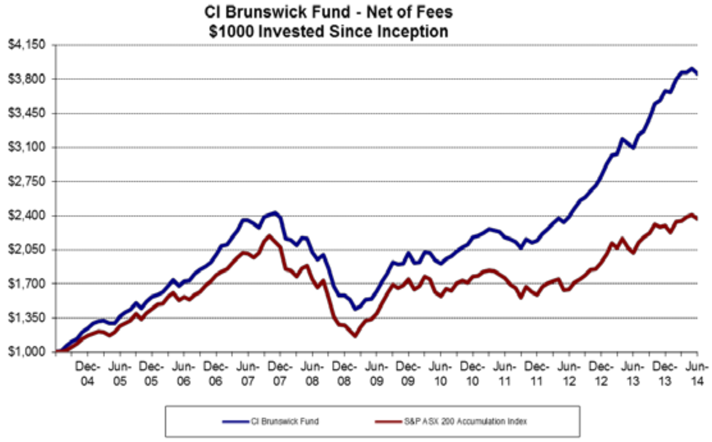
"Success is not final, failure is not fatal: it is the courage to continue that counts". Winston Churchill

"I've failed over and over in my life and that is why I succeed". Michael Jordan

"Your margin is my opportunity". Jeff Bezos

	****PORTFOLIO**	**#BENCHMARK**	**VALUE ADDED**
ROLLING 3 MONTH	0.06%	0.93%	-0.87%
ROLLING 1 YEAR	26.79%	17.43%	9.36%
ROLLING 3 YEAR	23.42%	10.37%	13.05%
ROLLING 5 YEAR	20.98%	11.20%	9.78%
ROLLING 7 YEAR	8.92%	2.34%	6.58%
ROLLING 10 YEAR	18.14%	9.01%	9.13%
SINCE INCEPTION*	18.14%	9.01%	9.13%
SINCE INCEPTION^	429.33%	136.86%	292.47%

* Annualised
^ Cumulative (1 July 2004)
** Before fees and expenses
# S&P ASX 200 Accumulation Index



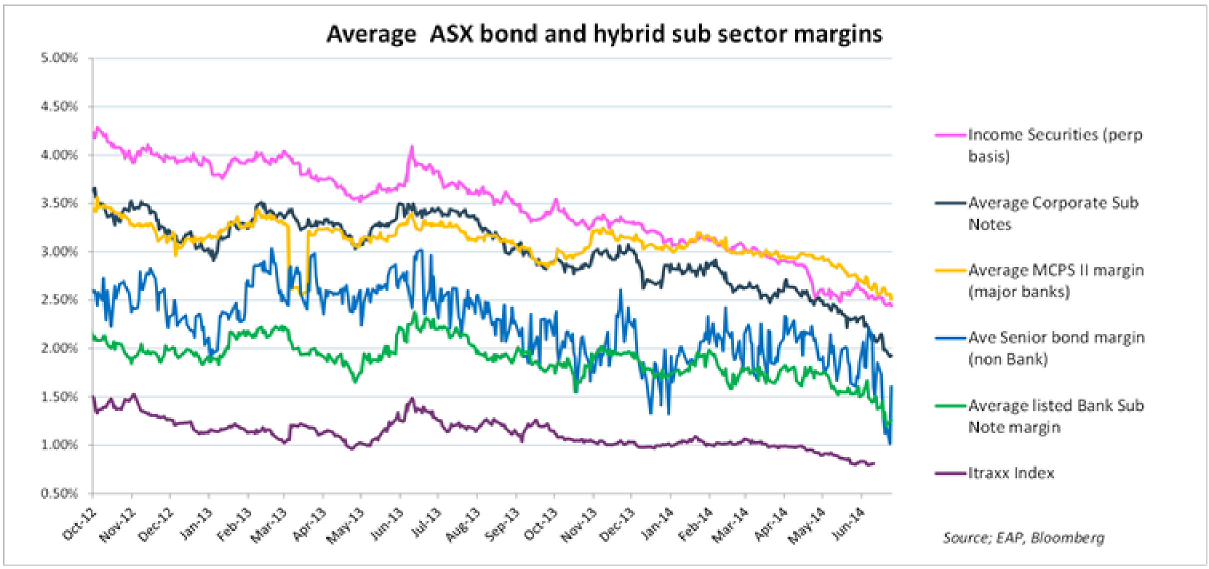
Market and Portfolio Performance

The S&P/ASX200 Accumulation Index rose over the quarter and year to 30 June 2014 by 0.93% and 17.43% respectively. The portfolio returned 0.06% and 26.79%.

The retail, materials and health care sectors were under-performers over the quarter while REITS, utilities and energy out-performed. Portfolio out-performers included nib Holdings, Lifestyle Communities, TFS Corporation and Equity Trustees while under-performers were Ozforex, Pulse Health, Transpacific Industries and Lion Selection Group.

We exited our last hybrid shares being the Transpacific Preference shares. With low cash yields (term deposits at 3.6%) and low inflation, quality income securities trade at record highs and above issued face value. In addition, beneficiaries of low rates have been property, infrastructure and genuine growth stocks.

JUNE 2014



Over the year resources delivered the best and worst stock performance in the ASX 200; Paladin a uranium stock (-66%) and Northern Star a gold stock (+115%). Opportunities have been abundant given 65 stocks in the ASX 200 achieved better than 20% returns. However the rising tide also saw a few sinking boats with 45 stocks in the ASX 200 delivering negative returns.

There appeared to be some weakness in confidence following the first Coalition budget and this was borne out by the rash of earnings downgrades seen through May and June, especially in the retail sector (RCG Group, Reject Shop, Pacific Brands, Super Retail, Kathmandu) and mining exposed companies (Bradken, Tox, Ausdrill).

The spurt of listings continued through the last quarter with another 10 companies coming onto the market, a number of them coming out of private equity hands, making a total of at least 33 for the past twelve months. The amounts raised on listing varied, for example just under $1B (Spotless) down to $90m (Gentrack), and over the year only one listing raised more than $1B. In an environment of low interest rates, a strong equity market, and investors looking for new alternatives, the timing is proving a boon for private equity wishing to exit at a profit. The two largest floats are likely to come over the next six months – Healthscope and Medibank Private – and this will be a stronger test of market appetite.

The portfolio is structured around different categories with the objective of delivering a diversity of attributes that achieve solid outperformance of the ASX 200 over the cycle and particularly in down markets. The category descriptors are:

- **Stalwarts** (35% of the portfolio) – sturdy, strong and generally larger companies with world class privileged market and competitive positions. (Woolworths, Brambles, Recall and Telstra)
- **Bond like equities** (7% of the portfolio) – stocks with secure, low-volatile dividends that can be grown and recapture inflationary effects over time. (AIA and Carindale)
- **Niche growth companies** (30% of the portfolio) – companies growing market share or creating new markets that have clear identifiable value propositions and run by focused, passionate, prudent and experienced management. (Ryman and TPG Telecom)

- **Asset plays** (13% of the portfolio) – stocks with strong or improving balance sheets trading at discounts to net asset value or replacement value. (British Empire, Amalgamated Holdings, Lion Selection and WH Soul Pattinson)
- **Turnarounds** (12% of the portfolio) – sound businesses with good management in place and good balance sheets essential. We especially like government to private turnarounds, spin offs and companies refocusing on core competencies (Fletcher Building and Transpacific Industries)

Currently the portfolio holds around 4% cash. The portfolio has around 11% of assets invested in overseas markets excluding NZ stocks or 26% including NZ stocks. The non NZ stocks are spread across US, UK, Singapore and Hong Kong listed companies.

Portfolio attributes as at June 2014 are summarized below:

P/E	16.7
Beta	0.76
Yield	3.6%
P/Book	2.2x
ROE	13.3%
Tracking error vs. ASX 200	5.39%
Stock Numbers	37

Major sector exposures are:

Sector	**Portfolio Weight**
Financials	30%
Industrials	13%
Consumer Discretionary	6%
Consumer Staples	4%
Telecommunications	9%
Energy	8%
Healthcare	5%
Materials	5%
International Equities*	11%
Cash	4%
Information Technology	3%
Utilities	2%

** Excludes NZ stocks which are considered domestic along with Australian listed securities.*

Market Observations

- We have seen an explosion in corporate activity year to date – as per numbers from *Bloomberg,* there have been over 10,000 global M&A deals done in 2014 for a total value of US$2trn. With significant cash piles on hand and in a world of low growth and zero interest rates, we are not entirely surprised to see boards signing off on these deals.
- The most talked about great crashes didn't happen in fiscal 2014; Chinese economy, global bond prices, Australian housing, the AUD.

- China remains all important to the fortunes of the Australian market. The Chinese premier Li Keqiang recently stated that "we will not take short term and forceful stimulus measures in response to economic fluctuation". We think that the central government wants a modest but stable growth rate in order to buy time for their reform initiatives. This does not imply a stall in fixed asset investment or a reduction in government spending on key infrastructure projects. Between January and May this year, the local government of 15 provinces announced infrastructure projects totalling 18trillion RMB (3 trillion AUD). This round of "micro stimulus" will place greater emphasis on sustainable growth and risk management. We expect to see more "reform compatible investments" in industries such as transport, logistic, energy, water treatment, health care and environmental protection. In June the State Council stressed the importance of "completing target growth rate for the year" and is working closely with local governments on rolling out resource reallocation policies, one being the much anticipated SOE reform. It is clear that growth from China in the next few years will still be investment driven and managed by government, albeit market forces will have a greater influence on how decisions are made. We believe a major hurdle faced by the Chinese economy in transition to a consumption driven model is the dispersion of income and growth rate between regions of the east and west, urban and rural which needs to be addressed. Transitions are never easy and we acknowledge that the dividend from such reform policies could take years to surface.

Stock News

Recall (REC) has continued to demonstrate renewed focus and energy post its demerger from Brambles. The company announced its largest acquisition since demerger being the $47m acquisition of CitiStorage in New York, adding 3% to group profits and continuing the consolidation of the fragmented US document storage industry. Later in the quarter Recall announced a facility optimization program whereby the company will over the next twelve months consolidate its facilities in the USA, improving utilization by 3% and lifting margins.

Brambles (BXB) acquired Transpac International during the quarter. Having withdrawn from negotiations to acquire Goodpack, a Singaporean container company, the company has now enhanced its containers capabilities in Europe and North America with this acquisition. Although not a large purchase (max Euro42m), Transpac will fit nicely into Brambles' existing operations.

In stark contrast to a number of other LNG and resource projects, the Oil Search/Exxon LNG project in PNG started up ahead of schedule during the quarter and led to production upgrades for **Oil Search (OSH)** for the 2014 year. The first cargoes from the project have now been shipped.

We participated in the **Equity Trustees (EQT)** capital raising that accompanied their purchase of the ANZ Trustees business in April.

Equity Trustees is a niche financial services business that categorises itself as providing Private Wealth Services and Corporate Fiduciary and Financial Services. In plainer English this means they offer a multitude of services relating to estates, trusts, asset management, aged care and responsible entity services for fund managers.

Equity Trustees was established in 1888 by an Act of Victorian Parliament and has a rich history. An attractive trait is that the company has a conservative, risk conscious culture that has withstood a multitude of investment and regulatory cycles.

The ANZ Trustees business offers many of the same services as Equity Trustees and as such increases scale in a consolidating industry. In particular it has a very large "will bank". ANZ Trustees is even older than Equity Trustees having been established in 1878.

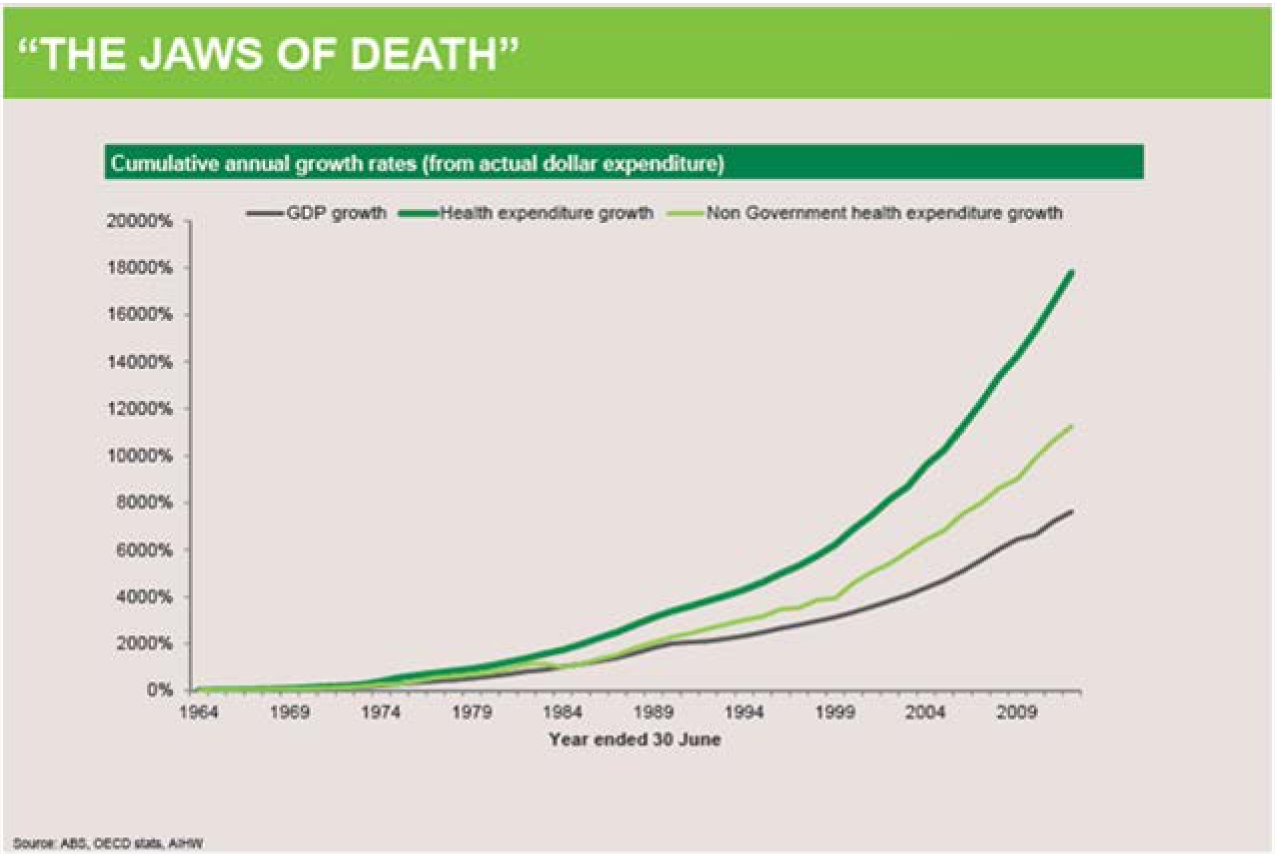
From a numbers perspective the transaction is very attractive with expected scale benefits, synergy benefits and a reasonable price. In the longer term the businesses look to have good prospects with an ageing population requiring trusted advice in an ever more complicated regulatory regime. We feel that the current management team are experienced and have an energy that should enable the company to participate in a growing market opportunity.

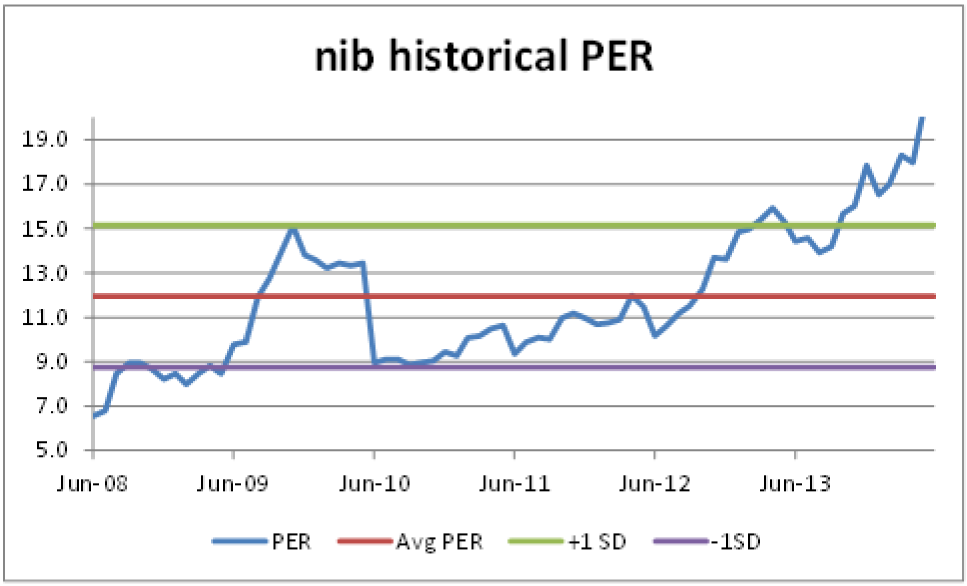
Aurizon (AZJ) and Baosteel joined forces to launch a $1.4B takeover bid for Aquila Resources, the owner of an undeveloped 40mt iron ore resource in WA. After a little noise thrown into the ring by Mineral Resources Ltd, it now appears that the Baosteel bid will be successful. If so, then Aurizon will end up having paid circa $210m for 15% of the acquired entity, effectively a fee to access work done on Aquila's WA iron project to date, and to secure an exclusivity period to develop an integrated multi user rail and port plan for the project. It is Baosteel's current intention to develop the mine and to use Aurizon's newly built rail and port infrastructure. The rail and port project is estimated to cost $5-6B. Aurizon has stated that it does not intend to be a long term holder of its stake in Aquila. We remain suspicious of Baosteel's real motives in acquiring Aquila. We believe the low quality of its iron ore resource is such that at today's iron ore prices the project returns are likely to be sub-optimal and we wonder if Baosteel has ulterior motives in this regard. We remain attracted to the ongoing operational improvements in Aurizon and step up in free cash flow from 2015 onwards – however the announcement makes us suspicious that shareholders may not see the real benefits from these effects.

We attended the **nib holdings (NHF)** investor day. Some key takeaways:

- nib remains a clear #3 in the Australian private health insurance market behind Medibank Private and BUPA. Competition is increasing as Funds and retail brokers step up advertising spend to compete for customers (new to category and switchers). The industry spends around $100m p.a. on advertising (excluding online), however, this has reduced in the last 12 months. Management thinks the spend reduction is only temporary and is due to Medibank Private looking to improve their IPO numbers and BUPA trying to meet profit targets.
- The NZ acquisition is making good progress with some early signs of improving operating trends – a key part of the company's strategy is building the direct-to-consumer channel and growing the market. Private health insurance coverage in NZ is around 30% of the population, compared to 50% in Australia.
- Growth in the international workers and students businesses remains solid and in the future should be supplemented by the 'nib Options' business which had a soft launch in March and will go live in August / September.
- The nib Options business relates to medical tourism i.e. travelling to Thailand for cosmetic surgery.
- Medical spending will continue to grow at a much faster rate than GDP. Management think that spending growth is sustainable but not the Government's relative share (see chart below). The private sector and private funding will have to play a larger role.
- Medical claims inflation will continue to be a key industry thematic, driven mainly by utilisation rather than rising unit costs. For nib, 1% of their hospital customers account for more than 50% of hospital benefits paid (pre risk equalisation).

- Lapse rates are 10%+ p.a. and are continuing to rise as customer churn increases with falling affordability. nib has a higher lapse rate than the industry due to a younger policyholder demographic who are more prone to churning policies.
- Management expect to grow net new policyholders (volumes) in the Australian private health insurance business by 4.5% p.a. (or 1.5x the industry growth rate of 3% p.a.). Adding to this price growth of 4%-6% p.a. and the top line can continue to grow at 8%-10% p.a.
- Post the recent changes to the regulatory capital regime, nib will be required to hold significantly less capital to support premium growth (i.e. decreasing capital strain). As a result, management now expect to have around $50m-$60m of surplus capital above internal targets by the end of FY14. As such, at the full year result management expects to announce a $40m-$50m capital return via either a special dividend or an on-market share buyback.
- For FY15 earnings management believe the 7.99% April-14 price rise combined with the ability to adjust product benefit designs will allow them to achieve their targeted net margin of 5.0%-5.5% for the Australian private health insurance business.





Source: Factset

Overseas Trips

We visited the UK and US (New York and Los Angeles) during late May and early June. One of the primary aims of the trip was to meet firms involved in the property market in the UK to establish whether the NAB's very large commercial real estate problem loans should now be consigned to the past or whether shareholders should contemplate further issues from this book of property loans.

We visited a number of firms involved in the UK property market including agents, accounting firms and investors. It was clear from our meetings that the commercial real estate market has improved significantly over the past six months.

A couple of years ago there was a large increase in demand for prime London trophy properties from mainly foreign capital, including sovereign wealth funds and mega wealthy individuals. Shortly thereafter contrarian funds became interested in London property and began to look for investment properties. These investors clearly initially stabilised prices in London and then pushed prices higher. Until mid 2013 there were very few buyers for properties outside London and very few buyers for non prime properties. However towards the end of 2013 the market outside Central London started to turn sharply as the demand pushed out from London into regional areas and also pushed out from prime properties into secondary properties.

One successful property investor described the change in the market over the past 18 months as follows. "We were able to buy a secondary shopping center on a yield of 8%, there were virtually no other buyers for this property at the time. The property was purchased at a price 40% below its peak valuation. Financiers (and there were only 2 or 3 possible lenders) limited the gearing on the property to a 68% loan to valuation ratio (58% senior debt and 10% mezzanine debt) at an average interest rate of Libor plus 4.46%. The current market valuation of the property is based on a 7% yield and we have recently refinanced the property on an 80% loan to valuation ratio at an interest rate of Libor plus 2.9% (and there were 15 potential lenders)."

They are now looking to sell at a yield of 6.5% which will include some rental income growth. Taking into account the drop in yield, the drop in interest costs and the increase in leverage the return on their equity will be very high.

This success is being played out across many parts of the UK and is attracting further investors, albeit they will have missed the major move in the market.

The rise in property prices is not just a book entry, during 2013 there was a record transaction amount of £20b, of this amount foreign buyers accounted for 71% of the volume.

The **National Bank of Australia (NAB**) property book is spread across all markets outside London and is certainly not prime in nature, however it is clear that there are buyers of properties in virtually all UK markets and that there are buyers of property loan books from banks. We therefore feel quite confident that the write downs of the NAB commercial real estate loan book have finished and the negativity around this issue should be consigned to the rear vision mirror by investors. A very good outcome would be write backs by NAB of some of its provisions on the UK property book, however we are not factoring this possibility into earnings estimates yet.

The turn in the UK markets is not confined to property, the equity market has now turned its attention to the potential upside from investing in previously distressed and unsaleable bank equity. There has been one or two successful sales of bank equity in the UK, as well as the listing of TSB, and the large number of capital raisings on the UK equity market suggest buyers may emerge for the entire NAB UK banking business.

We feel that investors should be contemplating the long awaited exit by NAB from the UK, and if this happens in the next year or two there would likely be a rerating of NAB.

It was another solid reporting season for the banks with all players reporting higher earnings and dividends, driven by moderate revenue growth and declining loan impairment charges.

Revenue growth in the mid-to-high single digits was primarily due to improving credit growth offset somewhat by falling net interest margins. Whilst falling wholesale funding costs and lower competition for deposits are a positive for net interest margins, the aggressive competition on front book lending and customer preference for lower spread fixed rate mortgages has seen net interest margins continue to decline. The banks demonstrated good cost control with modest improvement in cost ratios.

Asset quality trends continue to improve with low interest rates and rising asset prices driving reduced rates of new impairments as well as write-back gains on previously provisioned exposures. This culminated in another period of significant declines in bad and doubtful debt expenses, highlighted by lower net write-offs and lower collective provision coverage.

We think that in the current environment these positive asset quality trends are likely to continue. Banks will need to keep building capital to meet the new APRA Domestic Systematically Important Bank (D-SIB) capital buffer and the requirement to remove double-gearing from within their wealth management subsidiaries. We think these new capital requirements are very manageable given the banks generate a lot of organic capital and their dividend reinvestment programs are another ready source of capital.

JUNE 2014

The recent May 2014 APRA banking statistics and RBA credit aggregates showed that credit growth in May 2014 was 4.7% on an annualised basis. Housing lending grew at 6.2%, driven again by investor lending growth of 8.5% and more subdued owner-occupier growth of 5.2%. Business lending growth remains low at 2.8%, but improved slightly from April. Credit growth seems to be making a slow and steady recovery, consistent with our company and industry feedback.

Over the last 6 months NAB has seen the largest increase in housing lending market share followed by ANZ, with CBA and WBC both losing ground. NAB lost the most market share in business lending over the last 6 months, which underpins the revenue pressure they are seeing in their core business banking franchise, with the other major banks gaining share over this period led by WBC and ANZ. While deposit market share continues to be dominated by CBA and WBC, NAB has gained the most market share over the last 6 months in an effort to improve their funding composition and be ready to meet APRA's LCR requirements.