23rd January, 2015

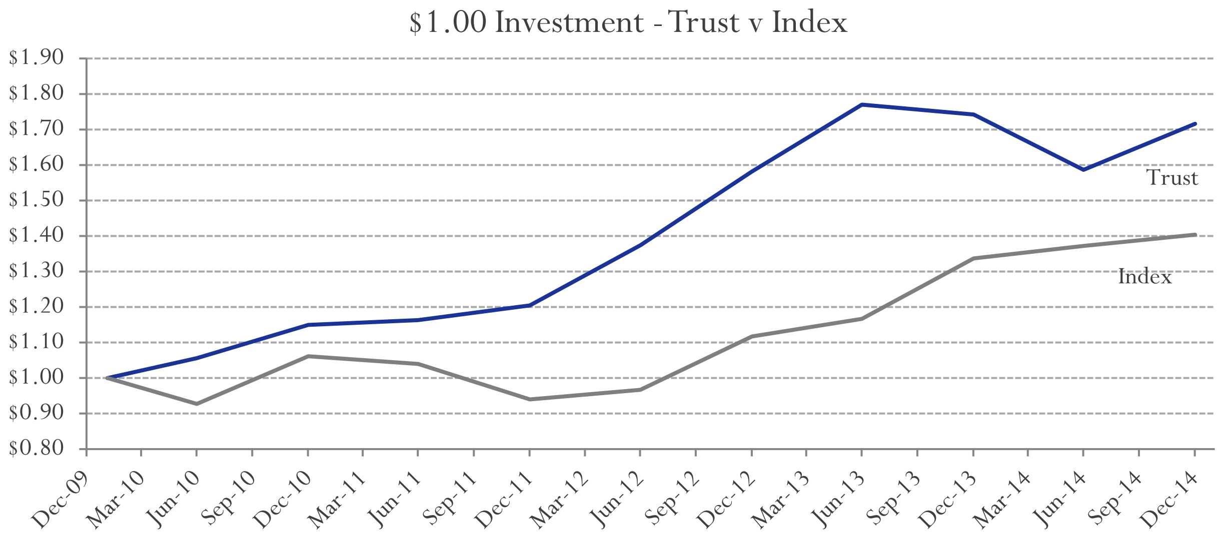
Half Year to 31 December 2014

After some prior soft periods, the Trust has performed well, rising 8.57% for the half year. A summary of this performance is shown in the table below, together with a comparison to the All Ordinaries Accumulation Index (Index) – the broadest measure of performance for the Australian stock market.

	Trust (before Perf. Fee)	Trust (after Perf. Fee)	10 % Benchmark	Index
01-July-2014	$1.5173	$1.5173	$1.5173	45,021.48
31-December-2014	$1.6474	$1.6474	$1.5932	46,046.93
Return	**8.57%**	**8.57%**	**5.00%**	**2.28%**

Please note that while the Trust outperformed the annual 10% Benchmark, because the unit price remains below the High Water Mark (HWM) of $1.7010, no performance fee was either earned or provisioned for. It is also worth remembering that should the unit price rise above the HWM; the subsequent payment of any performance fee is not permitted to reduce the unit price below this HWM level.

The following graph illustrates the historical performance of $1 invested in the Trust versus the Index. The investment in the Trust is after performance fees and includes any distributions which have been made.



The return of the Trust over the half year was driven by the solid performance of the underlying businesses; however the Trust has not been immune to the re-emergence of volatility, having dropped marginally from the levels it was trading at in late August.

Amongst the three earnings streams of:

i. Gain/loss on long term holdings;
ii. Dividend income; and
iii. Gain/loss on event driven investing

Approximately 5.8% of the 8.57% half year return was attributed to a gain on our long term investments. Further to this and due to the significant investments made (during the 2014 financial year) in businesses that are generating strong cash flows, the dividend income for the Trust during this half year was strongly up on the prior year's result. Accordingly, dividend income was responsible for the remaining 2.8% of the Trust's return. Finally, with attractive long term opportunities available, the Trust participated in very few event driven transactions, generating effectively no earnings from this stream. The Trust will always prioritise opportunities to invest capital in attractive long term investments over these short term (typically 3 to 6 months) event transactions. This is because it is far easier to generate healthy returns over long periods of time by investing capital and leaving it with companies that are growing, rather than constantly moving funds from one event to the next – like a bee having to flit from flower to flower to earn its honey. Although, that is not to say these event transactions aren't a valuable tool to use when other investments do not provide the same opportunities.

As the Trust remains fully invested in much the same long term opportunities as in 2014, it has incurred significantly reduced brokerage costs during the current half year. This saving touches on the significant benefits of inactivity in investing. So material (and somewhat surreptitious) are the effects of frictional costs (such as brokerage and taxes) on long term wealth creation, I thought I should elaborate with an example.

Say we have two avid stock market investors following very different philosophies. Firstly we have Slow-Moving-Syd, and while he likes to keep abreast of the operating results of businesses, he cares far too deeply about the maintenance of his backyard to worry about each daily movement of the market. Accordingly, with each passing year and each rise and fall that his stocks endure, Syd continues to leave his investments precisely as they were before. Then there's Trigger-Happy-Harry, whose favourite thing of a morning is to enjoy his double shot latte while sifting through the daily share tables to find out exactly what his stocks are worth and what he might buy or sell that day.

Let's now assume that they have $100,000 to invest and based on their past performance, both Syd and Harry can expect to achieve average annual returns of 10%, that they both incur brokerage costs of 0.4% each time they buy or sell shares and that they have the same tax rates of 37%. Following their results over ten years will help illustrate who gets busy and who gets wealthy.

At the outset, Syd selects the businesses to which he considers offer favourable opportunities and accordingly invests his $100,000. In doing so, he incurs $400 of brokerage and then promptly returns to mowing the lawn. Ten years pass by and one day he is stopped in the street by an old friend from school who works as a stock broker and this chance encounter reminds Syd that he should see how his shares are going. In keeping with his previously demonstrated abilities of earning an annual 10% return, Syd has found that his shares are now worth $258,337. This gives Syd an average annual return of 9.96% over ten years and a capital gain of $158,337.

Unlike Syd bumping into his broker once in a decade, Harry keeps in close contact with those 'in the know', and on average tends to turn over the entire value of his portfolio once a year. So, at the same time Syd was selecting his businesses to invest in, Harry was finishing the last of his latte and concluding what to trade. At the end of the first year, just like Syd, Harry had also incurred $400 of brokerage and achieved the same 10% return, giving both portfolios a value of $109,560. However, during that first year, Harry had identified new opportunities to seize upon and consequently maneuvered his portfolio to do just that. Realising the fruits of his efforts over the prior year, Harry had to hand over part of his 10% return to the tax office, leaving him now with $105,895 to invest in these new ideas. True to form, in this second year, Harry's investments generated another 10% return, giving his total portfolio a value of $116,018 (unbeknown to Syd, at this same time his portfolio had risen to $120,516). Now at the end of this second year Harry received a call from his adviser with the next big thing. Adjusting his portfolio to take advantage of this opportunity, Harry paid his dues to the tax man and was left with $112,137 to invest. Continuing in this way, at the end of ten years and many cups of coffee, Harry's investment had grown to $177,314, of which gave him an average annual return of 5.89% and a gain of $77,314.

While both Syd and Harry's investment ideas generated annual returns of 10%, because Syd had not incurred consistent frictional costs, he was able to accrue gains of $158,337 which turned out to be over double those of Harry's at $77,314. To calm Harry's anxiety over where his escaped earnings had gone, he can feel good knowing that by shelling out $10,994 over the years, they had made a significant contribution to funding his broker's yacht. Not stopping there, he can also nominate himself for Australian of the Year, as he carried out his civil duties in an exemplary fashion by handing $42,325 to the government. This isn't even taking into consideration how busy he would have kept his accountant journaling all of those transactions. People like Harry keep the world going round…

However, by remaining invested throughout the ten year period, not only were Syd's funds free to continue growing, earning returns of 10% on the full value of each prior year's performance, but his time was likewise free to identify new opportunities to invest his savings in, or to just continue pushing the lawn mower around.

While Syd may very well choose to one day sell his positions and incur a tax liability, until then, the 'deferred tax liability' on his unrealised gains will act like a zero covenant, interest free loan from the government – affording him more capital to earn further returns on in the future.

While compounding is a powerful force in wealth creation, when married with patience, it becomes (as Einstein marveled) the eighth wonder of the world.

As the manager of the Trust, I do not aim to be busy, I aim to be effective, and so with their recent performance continuing, the Trust will remain invested in the current businesses.

Furthermore, the philosophy of earning money *alongside* its investors, rather than *from* its investors is the bedrock to the operating structure and remuneration framework of the Trust, and it means that I get paid for being right, not for being a man of action. This is what affords the patience to wait for our returns.

However it does not mean that new investments will not continue to be researched (this is an activity that can never be finished), as the prospect of future dividend income and further contributions of capital provide the option of investing in any new prospects identified.

Though overall, the unique approach of the Trust is not an end in itself, but rather, something that will underpin our long term performance – which I expect to be above that of the market.

Luke Trickett