<u>Samuel Terry Absolute Return Fund</u> – September 2008 monthly report

The Fund's performance, compared to that of Australian All Ordinaries Accumulation Index and the MSCI World Equities Index, follows:

To 30 September 2008	STAR	All Ords	MSCI ($A)
1 month	-0.71%	-10.62%	-4.63%
3 months	-1.29%	-11.89%	2.52%
1 year	-17.88%	-26.59%	-17.13%
2 years (%p.a.)	-10.25%	-0.98%	-8.18%
Since inception on 1 November 2003 (%p.a.)	4.76%	13.15%	4.26%

After five long years, we finally have the environment for which this Fund was designed. Newspaper headlines of markets and banks collapsing provide wonderful opportunities to buy bargains. As the world went on sale, we went shopping, adding to several of our positions, including **Hunter Hall**, an Australian fund manager (6.3% of the Fund), which fell 18% to a new low, both in PE terms and relative to its funds under management.

I am delighted to report we added a new name, **Macquarie Group**, Australia's leading investment bank to the portfolio. Soon after Lehman's collapse, Macquarie shares fell to less than net tangible asset value for the first time since they listed in 1996. At the price we paid, Macquarie was trading on a P/E ratio of 4-6, and a dividend yield of 13%.

Macquarie has a very strong franchise in Australia, reflected in its average return on equity of over 20% since listing. One reason for this high return on equity is Macquarie's $200bn of satellite funds, which pay high fees to Macquarie, but in which investors' capital is locked up for long periods. Many people have criticised this structure as unfair to the investors in the satellites, but it is a fabulous structure for shareholders in Macquarie Group.

Macquarie's leverage ratio is much less than its US peers, and it has almost no CDO's or the rest of the alphabet soup that have caused so much grief in America and Europe.

Macquarie has an Australian banking license, meaning that its depositors enjoy an explicit guarantee from the Australian government, one of the few rich countries to have no net government debt. This minimises, but does not eliminate the risk that Macquarie could suffer the kind of run that killed Bear Stearns. For this reason, I only invested 3% of the Fund into Macquarie, but by month-end our Macquarie weighting had grown to 4.2%.

Our other major news this month was that **RuralAus**, an Australian timber plantation company (20.6% of the Fund) sold part of its land, meaning that more than half its market capitalisation is backed by net cash and mortgages (the old fashioned kind). This transaction is an important first step towards closing the gap between the share price ($0.17) and the net asset value per share ($0.35). We bought some more shares during the month but they are difficult to buy.

On a sad note, we sold out of **Prince Hill Wines**, a small Australian winemaker that had been 1.4% of the Fund, realising a 71% loss. This has been a tough lesson that picking managements of small “turnaround” companies is outside my circle of competence.

Finally, there has been much talk about the global credit crisis. As someone who has the majority of his family wealth in the Fund, I derive great comfort from knowing that about 50% of the Fund is in companies which have more cash than debt, and about 30% of the Fund is in companies which could repay their debt from operating cash flows within three years. If we have a re-run of the Great Depression (something I doubt), we are positioned far better than most.

Net asset value per unit was $A 0.9057 at the end of September. 1.9% of the Fund was in $A cash. The Fund owned securities issued by 21 companies.

Fred Woollard
16 October 2008