fisher funds

FROM THE
# undergrowth

SEPTEMBER 10

Prepare yourself… this newsletter is dedicated to good news. It is Spring, so it's time to put away the woolly jerseys and shrug off the overcoats of negativity that are far too heavy for the current climate. We decided to report just good news this month, and the really good news is that we found so many positive things to write about that we had to trim our text to fit it all in!

## At a glance
As at 31 August 2010

**Unit Prices ($)**

| | |
|---|---|
| NZ Growth Fund | 2.7608 |
| Australian Growth Fund | 2.1704 |
| International Growth Fund | 1.1365 |
| Fledgling Fund | 0.9963 |
| KiwiSaver Growth | 1.0388 |
| Infrastructure Fund | 1.2381 |

**Performance (August 2010)**

| | |
|---|---|
| NZ Growth Fund | -1.2% |
| Australian Growth Fund | 8.9% |
| International Growth Fund | -0.3% |
| Fledgling Fund | -1.2% |
| KiwiSaver Growth | 2.4% |
| Infrastructure Fund | -1.5% |
| NZ50 Gross index | 0.0% |
| S&P/ASX 300 ($NZ) | 0.8% |
| MSCI Global Small Cap Index | -0.9% |

# Our Portfolios

## What has been going on since we last spoke?

It is always risky to write a newsletter just after Wall Street has rallied for a couple of days on good economic news. There is a very real possibility that by the time this newsletter gets to you – in fact before it even makes it to the printer – the market might have fallen back to square one, or even lower. But actually it doesn't matter, because regardless of what happens tomorrow or next week, there has been enough positive news of late to suggest that the long term trend in markets is likely to be upwards.

Last month we said that the chatter about a looming double dip had become quite deafening. We spoke to a lot of investors at our roadshow about the potential of a double dip, and we reiterated our view to them that a double dip was unlikely because on balance, the economic news emerging around the world is improving and is suggestive of a recovery not a deterioration.

Good news from the US during August included the fact that the manufacturing sector has expanded for 13 consecutive months, there has been a robust rebound in agricultural exports, consumer confidence and house prices edged up, and consumer spending rose at the fastest pace for four months.

In Europe, economic confidence is the highest in two years, as unemployment concerns have eased and economic activity appears to be holding up in spite of spending cuts in countries like Greece and Spain.

Manufacturing in China grew at a faster pace than expected, confirming that China's economic growth is stabilizing. India's economy expanded at the fastest pace in two and a half years and South Korean manufacturers' confidence rebounded in August.

The good news came thick and fast in Australia – the Australian economy grew at its fastest pace in three years during the last quarter, exports increased 5.6%, household spending increased, and rising commodity prices have led to a record monthly trade surplus.

> "Nobody can go back and start a new beginning, but anyone can start today and make a new ending."
>
> Maria Robinson

In New Zealand, net migration bounced back, dairy prices have lifted, and ours is one of just a handful of countries that are considered by the IMF to be well-positioned to face another economic shock.

It is the news at company level that really gives us cause for optimism. You will have seen a number of company profit results and comments from annual shareholder meetings reported during the past two months. You may have missed some of them because so much of the news has centred on South Canterbury Finance and global economic

Have you joined KiwiSaver yet?*

# Your Portfolios (cont.)

goings-on. But there have been some interesting comments made by chief executives and chairmen, and a lot of these comments have reinforced our confidence in the companies that we have picked for your portfolios.

Our research files are bulging with notes from our meetings and conversations with our companies in recent months, but here is a small sample:

**Ryman Healthcare** Chairman David Kerr – "Income certainty is steadily increasing… demand is certain to remain very strong. We are ahead of last year and are on track to achieve our medium term target of 15% growth in realized profits for the full year."

**Delegat's** Managing Director Jim Delegat – "We have achieved some notable milestones during the 2010 financial year, including sales volume growth of 76% in North America and the establishment of in-market sales teams in Canada and New Zealand. The Group has robust business plans in place for the 2011 financial year and is confident in its ability to achieve forecast case sales."

**WHK** Managing Director Kevin White – "The final dividend represents a 167% increase on last year's dividend and reflects the Group's extremely strong financial position and the outlook for continued strong cash flow from operations."

**Aevum** Managing Director Steve Mann – "The result has improved significantly compared with last year, as the company made substantial progress and built business momentum. Cash flow increased strongly by 37% driven by an improvement in sales. The Board believes that Stockland's offer is inadequate, highly opportunistic and significantly undervalues Aevum." *Note, Stockland Corporation announced a conditional takeover bid for Aevum in early August, at $1.50 per share. At the time of writing this newsletter, the Aevum share price is trading at $1.70, suggesting that Aevum shareholders agree with Fisher Funds' view that the takeover offer is too low. It is nevertheless pleasing that the Aevum share price has lifted 56% in five weeks.*

We have loads of reasons to feel optimistic about the outlook for your portfolios – do contact us if you'd like us to share some more with you.

### New Zealand

The NZ share market (NZ50G) was flat for the month, outperforming global equities (MSCI World Index down 3.7%). August is a heavy reporting season, and profit results were mixed but with no major surprises either way. Our net portfolio return of -1.2% for August represented an underperformance against both the NZ50G index and the Mid-Cap gross index (NZSEMCG). While this is hardly good news, and detracts slightly from our otherwise positive newsletter, we are comfortable that this underperformance will be reversed with improving economic conditions. The retailers, **Pumpkin Patch** and **Kathmandu** hurt our performance as did **NZX**. While retail stocks suffer at any sign of economic weakness, they are the first to reflect any lift in economic activity. The market was unimpressed with the **Opus** result with analysts comparing it unfavourably against the 2H2009 result, however we were comfortable with the result and with our discussions with management. The two retirement village operators were the best performers, although the Metlifecare share price moved up prior to reporting a lift in NAV late in the month.

### Australia

August was a very healthy month for the Fisher Funds Australian Growth Fund with performance pleasing from both an absolute and relative perspective. The Fund generated a gross return of 8.9% in New Zealand dollar terms versus the broad market which was up 0.6% and the Small Industrials index (our preferred performance benchmark) which rose 3.1%. Other than still retaining a 50% currency hedge which means we didn't fully benefit from the fall in the value of the New Zealand dollar over the month, pretty much everything else went as well as can be expected. August is full year reporting for most of our Australian listed companies. In what was generally a patchy reporting season the companies in the Fisher Funds Australian Growth Fund performed strongly, growing profits on average by over 30% and beating analyst expectations. We witnessed a number of positive share price reactions to these profit results.

Financial services software firm **Bravura Solutions** advised the market that it had received an approach for a potential takeover at close to a 100% premium to the prevailing share price. The Board of the company rebuffed this offer, which we agree was the right course of action, but it has reminded the market of the value inherent in this business.

### International

Our International fund finished the month slightly lower, but ahead of its benchmark performance. Earnings season has come to a close and the following quote from Carl Bass, the CEO of portfolio company **Autodesk**, is the sort of thing we love to hear from our companies:

"I think there is a pretty sizable disconnect between the people I talk to who are running businesses, and what you read on Wall Street. People are continuing to make investments, and they realize that even in this economic environment, there's plenty of opportunity."

Datacash, a UK listed comparable to **Wirecard**, announced they received a takeover offer from Mastercard for a 50% premium. This follows the announcement back in April that CyberSource, a US listed comparable, would be acquired by Visa. Both companies were acquired at a similar transaction multiple. While Wirecard shares have already rallied nearly 25% since the first announcement, if you apply the same transaction multiple, it infers a further 50% upside for Wirecard shares. We strongly believe that Wirecard is a superior business to both of these companies and is one of the largest holdings in the fund. **Hyflux** announced a 50:50 joint venture with Japanese based Mitsui & Co. This will give them access to more capital to enable them to bid for new projects in China.

### Infrastructure

The Infrastructure Fund was not immune to the weakness in international share markets during the month. However, given its low risk nature it was able to contain the decline to 1.5% compared with the falls of between 3% and 5% in international indices. Top up investments were made in **Zurich Airport**, **Norfolk Southern** and **Fedex**, while the first bond investment in social infrastructure was made, being **Auckland Healthcare**, which is government guaranteed.

The **TNT** result announced during the month was relatively disappointing and the share price fell 12.5% for the month. As a consequence of the poor result this stock is under review.

# A bird's eye view

## We share the comments of other kindred souls, investment specialists who share our optimism for the future.

In his July 2010 newsletter Bill Miller, the Chairman and CIO of US investment firm Legg Mason, proclaimed that US stocks today represent the opportunity of a lifetime. He said that "the public's distaste for equities is palpable and understandable, with gentlemen and ladies both preferring bonds". Using Exxon Mobil as an example, Mason said that US large capitalization stocks represent a "once in a lifetime opportunity to buy the best quality companies in the world at bargain prices". He compared the dividend yield and the growth in dividends paid by Exxon with the yields on US treasury stock and noted that the last time stocks were this cheap relative to bonds was in 1951. He then commented that in 1951 he was one year old and didn't have sufficient sentience (awareness) or capital to invest… he does now, and is.

Miller went on to say that "The summer of 2010, when most global markets are down, pessimism about the future is high, and macro concerns predominate, is one of those rare periods where one can reliably adopt a long term strategy that promises (but of course cannot guarantee) returns superior to what just about everybody else is now doing."

Elsewhere in the US, financial services firm Charles Schwab surveyed 1200 money managers in July and found that 59% thought it unlikely that the US economy would head back into recession in the next six months, and 63% expected the US share market would rise in this period.

And James Greenhalgh who writes for The Intelligent Investor blog (www.intelligentinvestor.com.au) sounds like he would fit in well with the Fisher Funds team when he says "As human beings we're very much focused on the here and now, as well as the recent past. But, with the exception of a few difficult periods in history, it has paid to take a five- or ten-year view. I'm sure many investors are holding back waiting for the clouds to lift. But by the time the horizon is clear, stocks will be 30% higher. My experience has been that the value of my portfolio moves sideways for long periods, or drifts down, then all the performance comes in a rush. If you're not already invested, you'll miss the recovery."

# Your questions

## We share our response to a question asked during one of our roadshow presentations

**Q:** What do you think of gold and why don't you have any gold stocks in your Australian fund?

**A:** We don't have a strong view on gold, nor do we spend a great deal of time researching gold and gold stocks. Gold is a commodity and even though it periodically has bursts of popularity leading to strong, uninterrupted price rises, the reverse can happen too, and over time it behaves like any other commodity. We choose not to invest in commodities because a commodity is just that – it has no moat or differentiation. The business of a gold producer is to extract gold and then sell it on a world market at whatever the prevailing price is. One gold producer cannot get a higher price than another, or protect his business from the vagaries of the global gold market. Compare a gold producer with one of our preferred portfolio companies that produces a differentiated, sought after, and essential product or service. Because customers want the products or services of our companies, relatively more than they want competing products or services, our companies have pricing power. It is this pricing power which enables our companies to grow their profits irrespective of the competitive or global environment.

Investing in gold mining companies is not for the faint-hearted because their share prices may not necessarily reflect movements in the underlying gold price. If you invest in the wrong stocks, you can lose money even if the price of physical gold goes up.

Gold is proving popular right now because it is considered a good hedge against inflation. However, we do not believe there is a real threat of inflation, indeed we think that deflation is more likely to be of concern if the economic recovery fails to pick up pace. We think that investors should exercise caution around popular or faddish investments such as gold. Rather than wanting to jump on board because the price is rising, a prudent investor might be better to avoid popular investments for fear of getting in just before the bubble bursts.

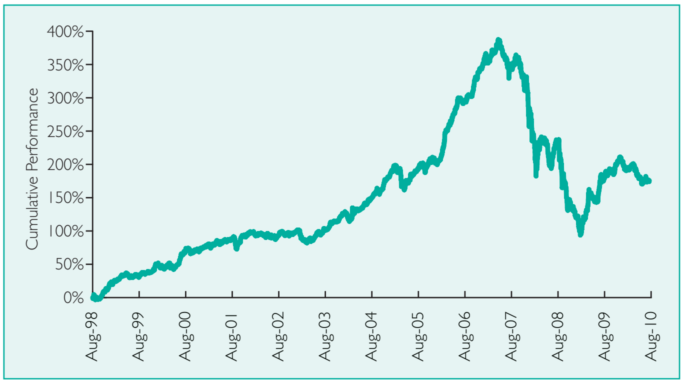
# Fund facts

## Fund Performance

| Fund Net Returns | 1 Year | 2 Years | 3 Years | 5 Years | Since Fund Inception |
|---|---|---|---|---|---|
| NZ Growth Fund | -1.3% | -8.6% | -15.1% | -1.3% | 8.8% |
| Australian Growth Fund | 19.4% | 9.8% | -5.3% | 6.5% | 7.4% |
| International Growth Fund | 4.8% | 6.2% | na | na | 4.6% |
| Infrastructure Fund | 7.7% | na | na | na | 15.5% |
| KiwiSaver Growth Fund | 8.4% | 6.90% | na | na | 1.3% |
| *NB… annualised returns, after tax and fees.* | | | | | |
| **Fund Pre-tax Returns** | | | | | |
| NZ Growth Fund | -0.2% | -7.6% | -14.3% | 1.2% | 11.4% |
| Australian Growth Fund | 19.4% | 10.1% | -5.1% | na | 9.1% |
| International Growth Fund | 3.5% | 6.2% | na | na | 4.6% |
| Infrastructure Fund | 7.7% | na | na | na | 15.5% |
| KiwiSaver Growth Fund | 8.4% | 6.9% | na | na | 1.3% |
| *NB… annualised returns before tax and after fees. They differ from actual returns experienced during these periods.* | | | | | |
| **Market Indices** | | | | | |
| NZ50G | -2.0% | -4.9% | -9.7% | -2.0% | |
| 90day bank bill | 2.8% | 4.0% | 5.6% | 6.5% | |
| S&P/ASX300 (Calculated in $NZ) | 5.3% | -1.3% | -4.4% | 7.6% | |
| MSCI Global Small Cap Index (in $NZ) | 5.7% | -3.5% | -8.0% | -0.3% | |

| August's Biggest Movers | |
|---|---|
| **New Zealand** | |
| Kathmandu | -24% |
| Opus International | -13% |
| Metlifecare | 7% |
| Pumpkin Patch | -5% |
| **Australia** | |
| Aevum | 54% |
| Bravura | 33% |
| Centrebet | 26% |
| DWS | 19% |
| **International** | |
| Bawang | -22% |
| Hanger Orthopedic | -21% |
| Hsu Fu Chi | 17% |
| O2 Micro | -16% |

## New Zealand Growth Fund




**Fund Inception** August 1998

**Portfolio Holdings** – Abano Healthcare, Delegats, Fisher & Paykel Healthcare, Freightways, Infratil, Kathmandu, Mainfreight, Metlifecare, Michael Hill, NZX, Opus International, Pumpkin Patch, Ryman Healthcare, Tower Limited, Wakefield Health.

## Australian Growth Fund


**Fund Inception** June 2005

**Portfolio Holdings** – Aevum, Arrow Energy, Austbrokers, Bravura, Centrebet, Credit Corp, DWS Solutions, McMillan Shakespeare, Nick Scali, Oakton, Pharmaxis, Reckon, Toxfree, Treasury Group, Vision Group, WHK Group.

## International Growth Fund


**Fund Inception** October 2007

**Portfolio Holdings** – Actelion, Advent Software, Autodesk, Bawang International, Biotest, Brembo, China Automation, City Telecom, Conceptus, Equinix, F5 Networks, Gameloft, Hanger Orthopedic, Hansens Natural, Hsu Fu Chi International, Hyflux Limited, Icon PLC, Interactive Intelligence, Jumbo, Midas, Nokian Renkaat, O2 Micro, Okano Valve Manufacturing, Ports Design, Prestige International, Qiagen, Raffles Education, Sarin Technologies, Shinko Plantech, Stratec Biomed, Telvent, Wasion Holdings, Wellstream, Wirecard, Zhuzhou CSR Times Electric.

## Infrastructure Fund


**Fund Inception** December 2008

**Portfolio Holdings** – Flughafen Wien AG, Fraport AG, Norfolk Southern Corp, TNT N.V., Flughafen Zuerich AG, Asciano Group, Union Pacific, Auckland Airport Bonds, Contact Bonds, Genesis Bonds, Meridian Energy Bonds, NZ Post Bonds, Vector Bonds, Wellington International Airport.

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