Investment Market Update No. 28

November 2006

Editorial

Clients enjoyed strong returns over the past few months, notwithstanding an expectation of a further interest rate increase in November.

In this issue we cover:

1. Tax reports;
2. Recent activities;
3. Telstra 3;
4. Fee review;
5. Staff update;
6. Investment briefs.

David French
Managing Director and Senior Investment Advisor

Tax reports

Tax reports have now been mailed out. Clients with margin loans will have also received a letter detailing their interest costs. Please contact us if you have not received yours or if you have any queries.

Recent activities

At Capricorn Investment Partners we aim to offer superior client service. Here's some of what we've been doing recently.

We have updated client records with Centrelink and the ATO. This large task saves valuable hours and improves accuracy in ensuring clients are getting the most from their financial affairs.

One client, who because of chronic illness needs a health care card, risked losing her disability pension due to receiving an inheritance. Using superannuation, we avoided the loss of the card. Based on our recommendations, the client will soon be re-entitled to a substantial government pension.

Australian Energy Income Fund (FIELDS), has been one of my poorer investment recommendations. As discussed in an earlier newsletter, we contacted this company directly to ascertain whether the market had in fact got its view of the investment wrong. Based on those discussions, and other information, we formed the view that it was better to ride out the storm. Ultimately Santos Limited bid for FIELDS, but was then trumped by Beach Petroleum which offered a premium of 4 per cent to face value of $100. These events turned a disappointing performance into an exceptional performance, and show the value of doing some research before getting wound up in the hype.

We have been able to reinvest the FIELDS proceeds for many clients in BIS Cleanaway notes. Like FIELDS these are somewhat more risky hybrid/fixed interest assets, however we believe that the business case is sound, and that the risk is adequately compensated for by a yield in excess of 10 per cent.

Graincorp reset preference shares have matured early, and we were able to replace these with a new instrument from Nufarm Limited. Nufarm is a company I am very familiar with. This instrument offers an attractive yield and, we believe, superior credit quality.

We sincerely hope you are happy with our efforts on your behalf and ask that you contact us if you have any concerns.

Telstra 3

Existing shareholders are being offered a preferential entitlement of a minimum 3000 shares if they would like to participate in T3. We have accepted the entitlement for most portfolios.

22 Archer Street PO Box 564 Rockhampton Qld 4700
Telephone 07 **4920 4600** Facsimile 07 4922 9069
Email enquiries@capinvest.com.au Internet www.capinvest.com.au
ABN 26 095 998 771 Australian Financial Services Licence No. 237435

The sale is offered in installments, with $2.00 payable now, and an amount to be determined in a book build (similar to an auction), payable in a year's time. As added incentive, retail shareholders receive a 5 per cent discount on the institutional share price. Provided the final installment is paid in a year's time, holders of T3 also receive a bonus Telstra share for every 25 T3 installment receipts held. The value of these retail concessions is around $0.24 per share, which implies a return on listing of around 10 per cent. The installment receipts are entitled to full dividends, making a gross dividend yield of 20 per cent for 2007/08.

We believe that Telstra's business outlook is improving, and therefore that the installment receipts represent an attractive investment opportunity.

Fee Review

CIPL provides a capital city standard service in a regional city, with an unusually high level of personal client interaction. We deal with a very wide range of client requirements including managing portfolios, dealing with Centrelink and the ATO, and interacting with client's accountants and solicitors. Clients receive all of these services for less than the fees charged by a retail managed fund. Further since inception, the average return across all portfolios has been 12 per cent per annum, generally exceeding benchmark.

In common with most businesses we have experienced significant cost increases. Further, our new staff including a dedicated IT programmer and two graduate assistants, provide direct client benefits as evidenced by our generally timely attention to client queries. We also take training seriously - in addition to normal ongoing training, we have completed update courses in superannuation, and attended research conferences with access to senior company management.

In light of the above, we are undertaking a comprehensive review of fees. We will write to clients individually with any proposed alterations to the current structure.

Staff Update

We have some new staff including Angela Jenner who has just completed a degree in accounting from CQU, and Adrian Cahill who joined us following his completion of a Bachelor of Finance at Bond University. Richard Ng also joined us as self managed superannuation fund administrator. Richard has a degree in accounting and an MBA.

In December Zac Sorensen is completing a course in advanced company valuation at the Amsterdam Institute of Finance and will then take several months of long service leave. With Angela's and Adrian's help, I will take responsibility for Zac's tasks and clients' needs until he returns.

Investment Briefs

Here are some trading ideas for non-portfolio clients:

Transfield Services Limited (TSE)
At the recent AGM the TSE indicated that the general outlook was for sustained growth across all divisions, and that new business totaling $200 million had been secured over the last 15 months. TSE does not appear overly expensive given expectations of earnings per share growth, and shareholder benefits that are likely to accrue from the spin-out of infrastructure assets in early 2007.

Allco Finance Group (AFG)
Allco is expecting EPs growth of 20 per cent for full year 2007, but more importantly the company has emphasized a solid pipeline of initiatives across several divisions. Improved access to debt facilities means that Allco can finance more aircraft, ships and property, and create more public wholesale funds. Allco is expecting $2bn in new funds management for 2007.

Paladin resources Limited (PDN)
Two key milestones have been reached on the road to producing uranium, including commissioning of the Langer Heinrich mine, and the completion of the Kayelkera feasibility study. Full production from LH is expected by September 2007. Uranium prices continue to hold high levels and this will be the first conventional uranium mine to come on stream for several years.

AWB Limited (AWB)
Another low in the wheat harvest, a cut in the base fee component of the pool management fee, removal of the single desk marketing structure, and potential Iraqi related tax liabilities make this stock look like a basket case. Analysts have calculated the impact of this downside at about $1.06 per share. Fully discounting these negatives suggests a valuation of $2.79 compared with the current market price of $2.56. Not one for the faint hearted, but would not be the first time an iconic stock has risen from the ashes.

You are advised to seek advice regarding your particular situation before acting on anything contained herein.

22 Archer Street PO Box 564 Rockhampton Qld 4700
Telephone 07 **4920 4600** Facsimile 07 4922 9069
Email enquiries@capinvest.com.au Internet www.capinvest.com.au
ABN 26 095 998 771 Australian Financial Services Licence No. 237435