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**AFA** National **Conference** 2009

GOLD COAST October 4-6 • RACV Royal Pines Resort

**Welcome**

**AFA National Conference  
2009**

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# AFA National Conference 2009

GOLD COAST October 4-6 • RACV Royal Pines Resort

## Investment & Technical

Session Stream 7

Paul Cuddy



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**“Cash is king.... But for how long?”**

Paul Cuddy, CEO, Bennelong Australian Equity Partners

**When is the right time to dip your toes back into equities?**

Lessons learnt from the GFC



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# Bennelong Australian Equity Partners

**AFA Conference**  
**October 2009**

**Paul Cuddy** CEO, Bennelong Australian Equity Partners



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## Agenda

- The Bennelong Story
- GFC - What Happened?
- Outlook - What Now?
- Portfolio Strategy

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# Business Introduction

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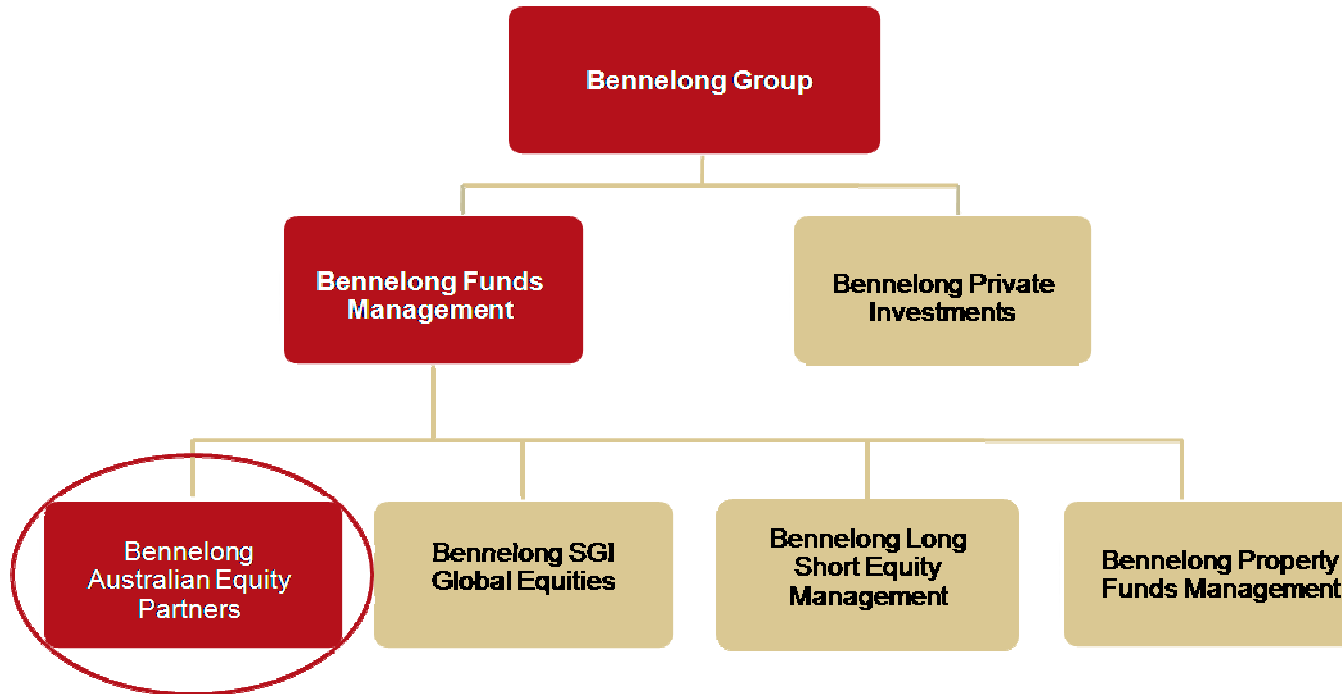
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# The Bennelong Story

- **Bennelong Australian Equity Partners**
  - Boutique Australian equities investment manager
  - Founded by Paul Cuddy & Mark East (July 2008)
  - Investment team (5) has 75yrs+ investment experience
  - Entire investment team are shareholders - client alignment
  - Core 'quality' style agnostic process
  - Fundamental bottom-up manager - incorporates proprietary investment tools
  - FUM >\$400m
- **Bennelong Partnership**
  - Well capitalised private partnership
  - Exclusive support protects IP and ensures undistracted commitment
  - Foundation - genuine philanthropic agenda

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# The Bennelong Story



*"The ultimate beneficiary of the net assets & income of the Bennelong Group is the Bennelong Foundation"*

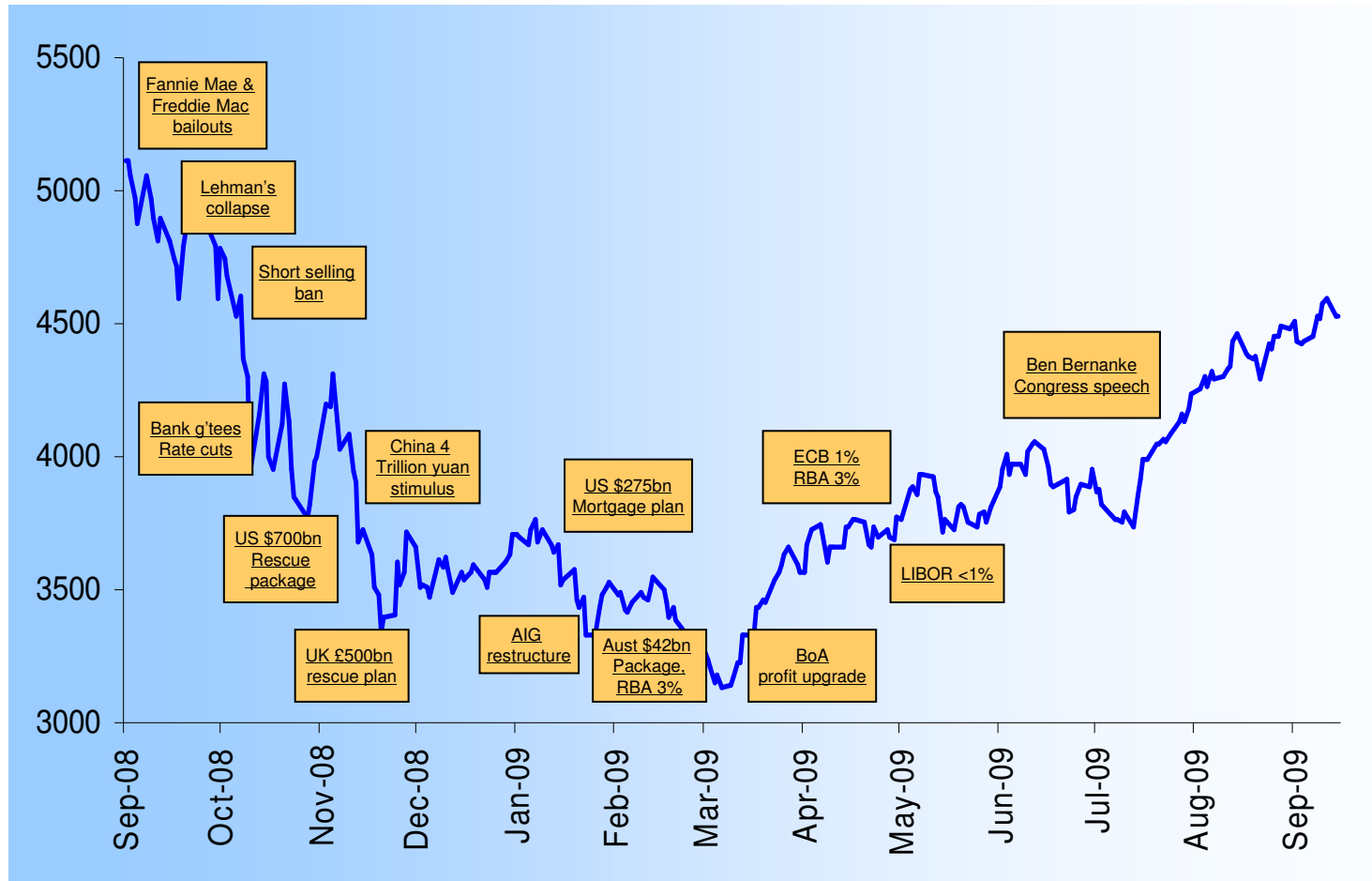
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# GFC – What happened?

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# Year in Review



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# GFC – What happened?

- Pre-GFC conditions
  - Excessive consumer/business leveraging
  - Creative capital structures fuelled liquidity
  - Unsustainable lending practices
  - Leveraged consumers drove retail & housing sectors
  - Historically low bad debt provisions
  
- GFC – The perfect storm?
  - Bad debts emerge
  - Liquidity dried up as credit markets shut down
  - Confidence in the global financial system rocked - record volatility
  - Series of high profile collapses eg. Lehmans, BNB, ABC Learning
  - Consumer/business confidence collapsed
  - Consumer & business moved to conserve cash
  - Financial viability tested - debt covenants?
  - Severe earnings downgrade cycle

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## GFC – Medicine?

- Regulatory initiatives
  - Short selling bans
- Nationalisation of borderline businesses
  - US – Fannie Mae & Freddie Mac, AIG
  - UK – RBS, Lloyds
- Unprecedented fiscal stimulus
  - US \$750bn Polson plan + \$275bn mortgage holders
  - UK £500bn package
  - Australia \$42bn package
- Administrative stimulus
  - Bank g'tees
  - Quantitative easings
  - FOHG
- Interest rate cuts
- Recapitalisations

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# Outlook – What now?

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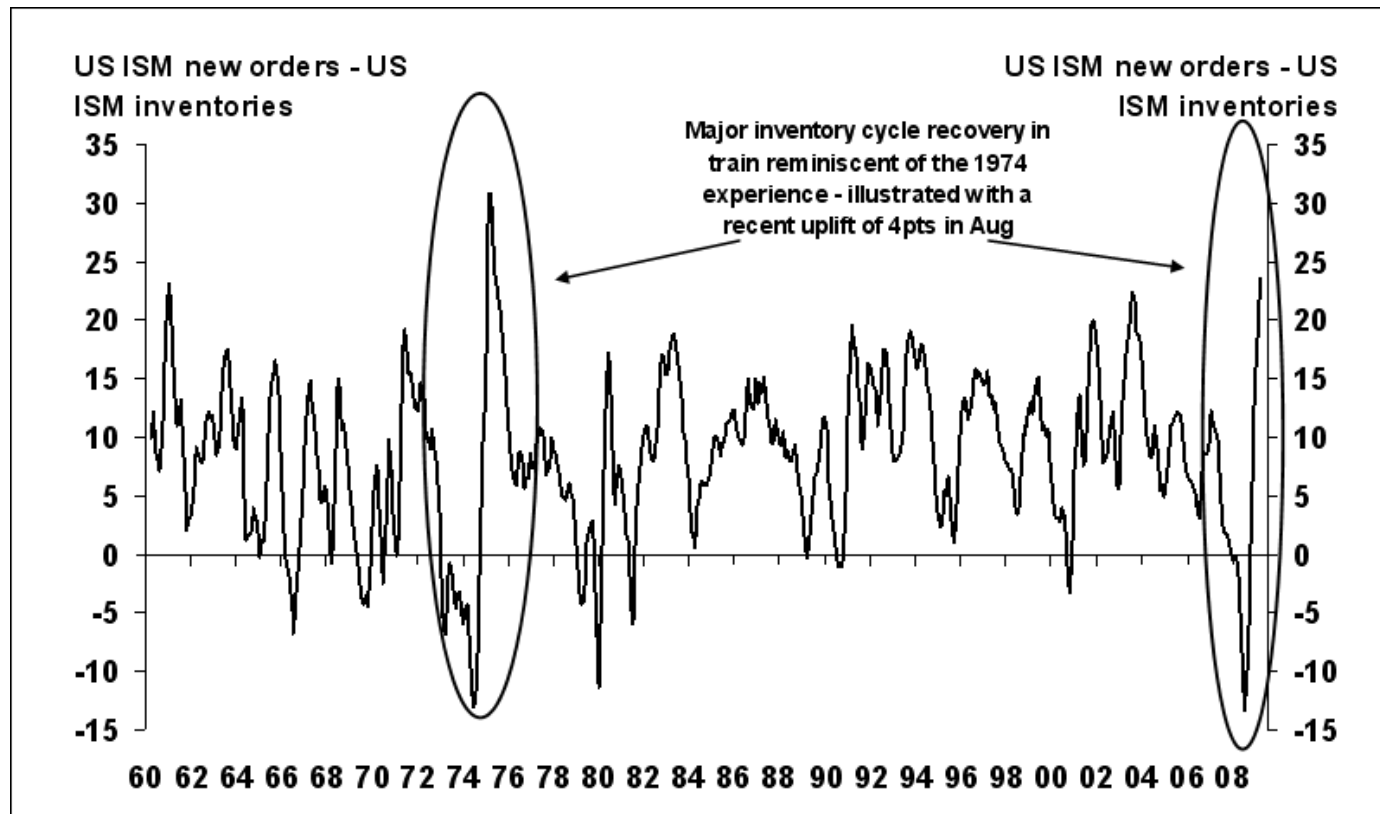
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## Market Outlook

- GFC Recovery?
  - Inventory rebuild is underway
  - OECD leading indicators are improving
  - Credit markets are thawing
  - Consumer confidence rebounding
  - Business confidence at post Dec'07 highs
  - Housing affordability is stronger
  - Interest rate cuts
  - Recapitalisations

# Macro – Inventory Cycle

## Inventory Cycle 2009 'vs 1974?

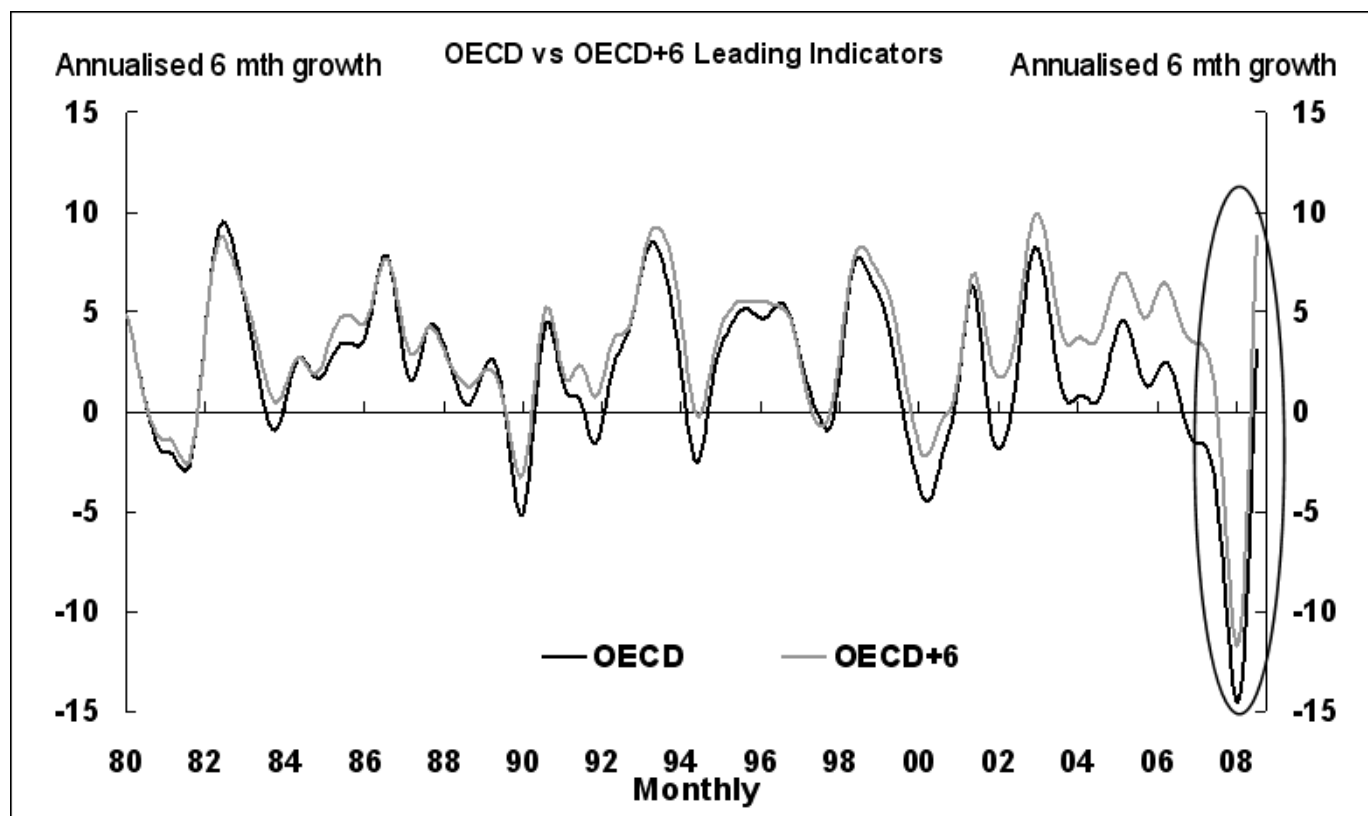


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# Macro – Economic Indicators

## OECD Leading Indicators

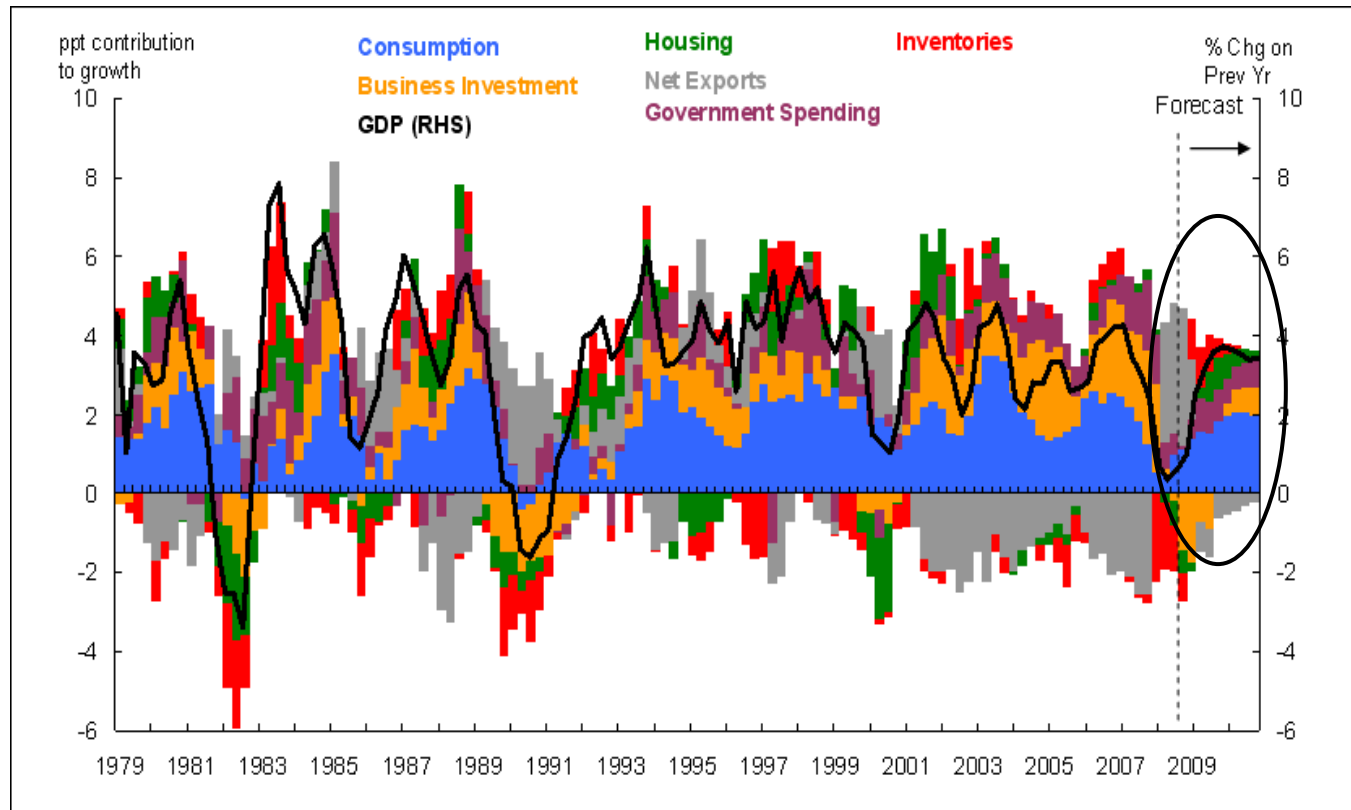


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# Macro – Economic Drivers

## GDP Drivers

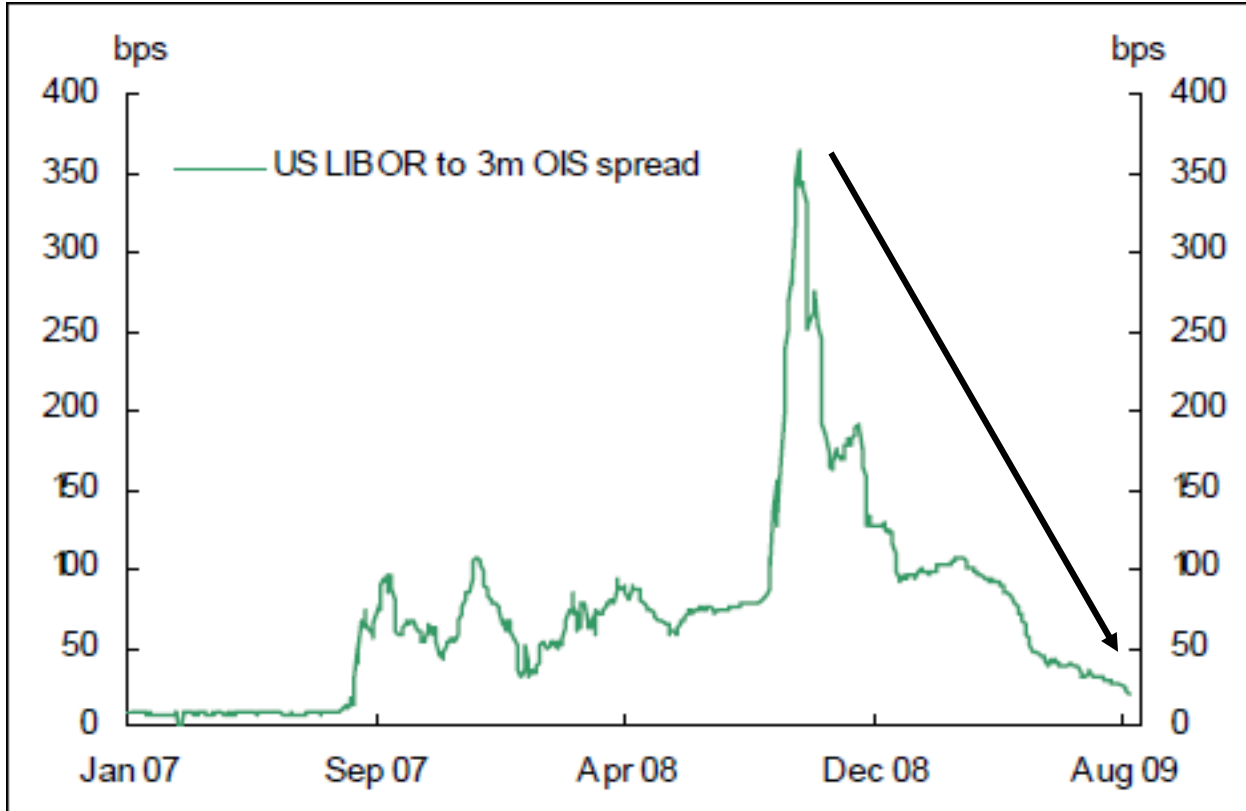


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# Macro – Credit Market

## Credit Premiums

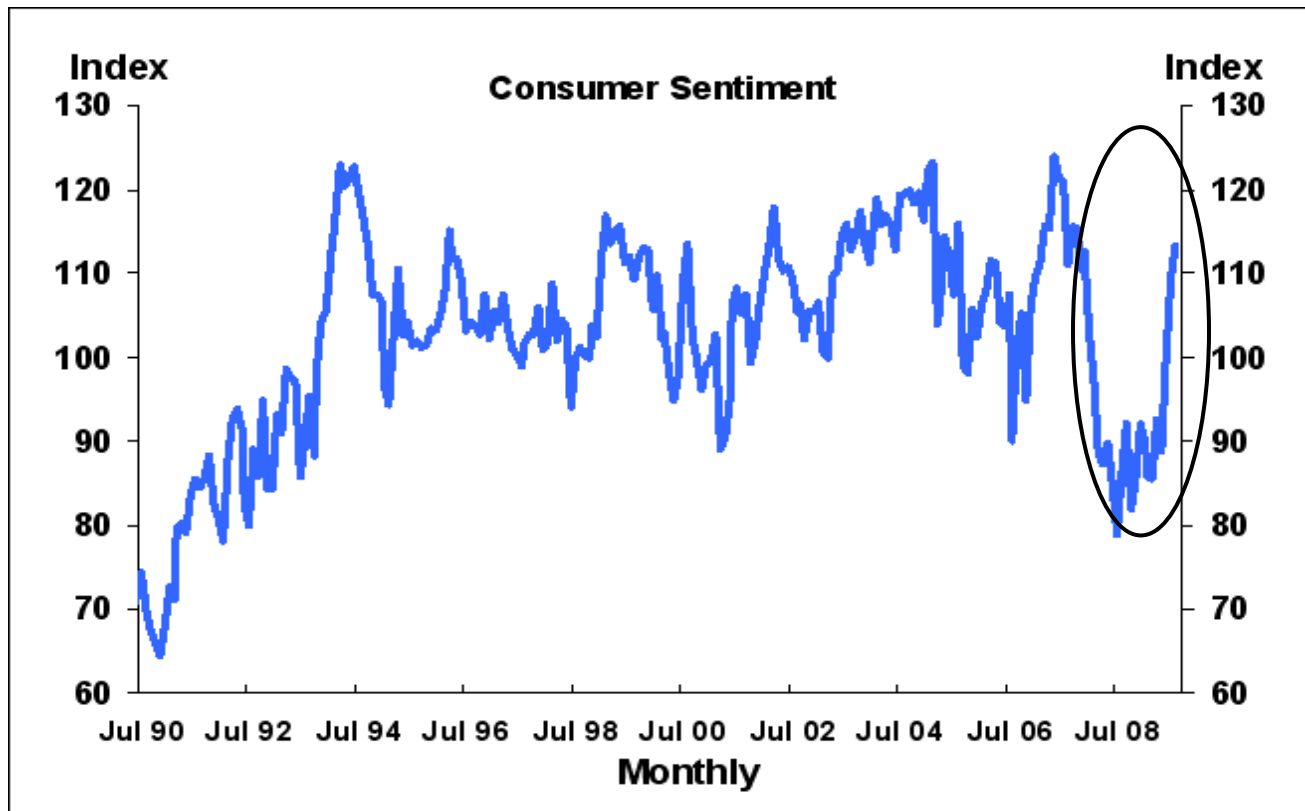


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# Macro – Consumer

## Consumer Confidence

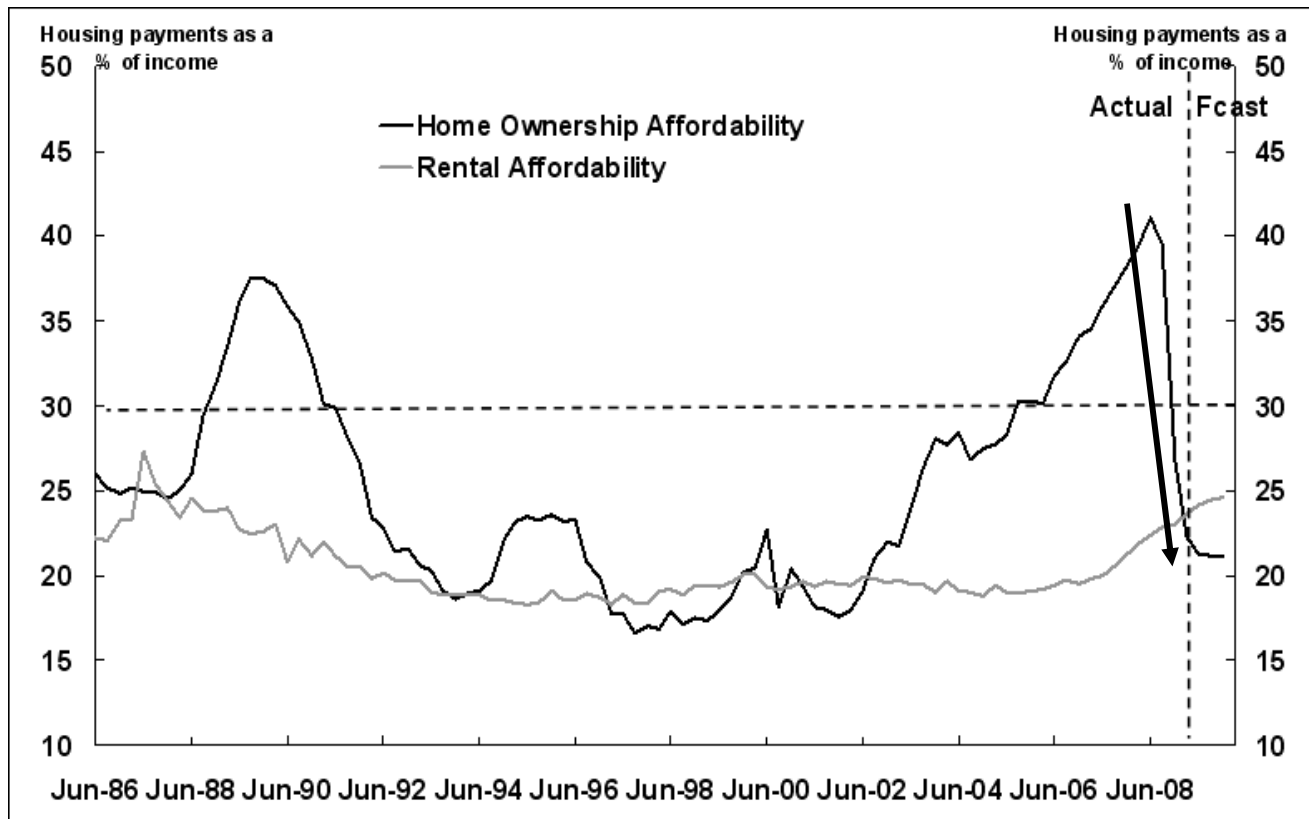


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# Macro – Housing Market

## Housing Affordability

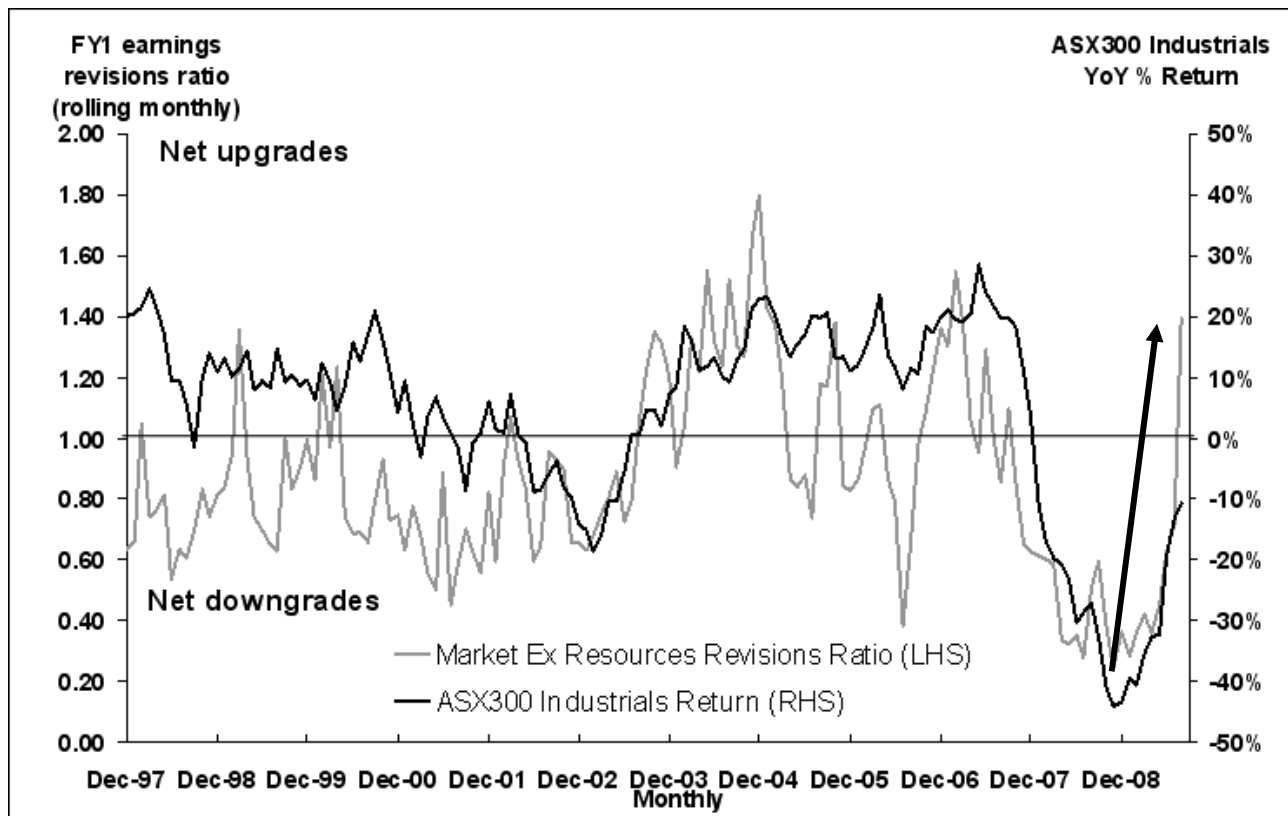


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# Equity Market Sentiment

## Earnings Revisions Ratio 'vs Returns



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# Portfolio Strategy

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## June 2009 Result Themes

Themes	Implications
<b>Operating Leverage</b>	<ul style="list-style-type: none"> <li>- Jun'09 results delivered better than expected cost reduction.</li> <li>- Cash conserve strategies have cut overheads, staff, capex as the world de-stocked.</li> <li>- Highlights operating &amp; margin leverage to improving demand.</li> </ul>
<b>Business Capex</b>	<ul style="list-style-type: none"> <li>- Significant upside in business capex.</li> <li>- LNG projects planning to spend over \$200bn.</li> <li>- Significant infrastructure et al construction projects.</li> </ul>
<b>Consumer Resilience</b>	<ul style="list-style-type: none"> <li>- Consumer confidence supported by low interest rates, fuel prices, fiscal stimulus.</li> <li>- Consumer spending portion of GDP only +0.8% qoq versus +1.1% for non-farm, implies economy is strong ex-stimulus.</li> </ul>
<b>Broadening Economic Recovery</b>	<ul style="list-style-type: none"> <li>- Early cycle beneficiaries (consumer) have already reported strong comparable growth.</li> <li>- Signs of a pick-up in other sectors eg. housing, construction, financials, media...</li> </ul>
<b>Rising Interest Rates</b>	<ul style="list-style-type: none"> <li>- Australia is emerging from the GFC in relatively strong shape.</li> <li>- The RBA will be monitoring credit conditions, spending, unemployment and CPI.</li> <li>- Banks have raised capital ratios and are reporting better than expected bad debts.</li> </ul>
<b>China Story</b>	<ul style="list-style-type: none"> <li>- GDP growth recovered from 6% to 8% in June. IP +11% in June. FAI +34% " .</li> <li>- Positive for industrial metal demand.</li> <li>- Potential risk that credit binge is funding speculative investment in shares, commodities, and property. Policy response?</li> </ul>

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## Opportunities - LNG Sector

- Strong demand for LNG – 48 Trains
  - \$US295bn capex
- 17 undergoing FEED activities
  - \$120bn capex
- Limited resource capacity
  - to build 4-6 simultaneously
- Growing contracted liquefaction capacity
  - currently 36Mtpa
- Current global capacity 172-193Mtpa
- Chinese demand growing exponentially
  - Cleaner burning credentials
  - 3% of 2005 energy mix (target 10% by 2020)
  - LNG imports 3.5Mt 2008 (60Mt by 2020)
- Risks?
  - Project delays
  - Excess supply (eg. Qatar)
  - Unconventional gas (CSG, shale)



Source: Chevron Australia

## Themes – Portfolio Strategy

Macro-Economic Themes	Portfolio Strategy	BAEP Portfolio
<b>Australian Economic Recovery</b>	Economic recovery becoming more broad based. Diversify exposure from early cycle beneficiaries (consumer) into media, transport, infrastructure etc.	JBH, LLC, AIO
<b>Operating Leverage</b>	Favour stocks with earnings leveraged to improving demand and/or cost reductions.	ANN, FLT
<b>Business Capex</b>	Corporates moving from cash conservation to growth strategies. Growing list of mining, LNG, infrastructure et al capital projects.	CPB, MRM
<b>Rising Interest Rates</b>	Improving credit markets, bad debts, demand and spending will force the RBA to manage monetary policy aggressively to head off inflation.	NAB, ANZ
<b>Global IP</b>	IP appears to have bottomed and global GDP growth is improving led by China and signs of re-stocking in Europe, US...	BHP, OZL

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# Summary

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## Key Points

- GFC Lessons
  - *'If it seems too good to be true...'*
  - Quality experienced investing delivers through cycles
  
- Outlook
  - Stage I → *'Restoring confidence & stimulating the rebuild'*
  - Stage II → *'Evidence of underlying demand recovery?'*
  
- Strategy
  - Pre-March 2009 → Bias to well capitalised defensive earners
  - Current → Increase exposure to quality cyclical earners

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**Thank You**



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# Team Roles

Name & Position	Responsibilities	Investment Experience
<b>Paul Cuddy</b> CEO, Co -Head of Equities 	Co-Head 'Portfolio Team' Lead – investment process & co-pilot Sectors: Resources, Energy	19 years
<b>Mark East</b> CIO, Co -Head of Equities 	Co-Head 'Portfolio Team' Lead – stock selection & portfolio construction Sectors: Banks, Non-Bank Financials	19 years
<b>Keith Hwang</b> Director, Quantitative 	Quantitative Research & Analysis Infrastructure & Database Management Quantitative Portfolio Management	11 years
<b>Michael Chun</b> Equities Analyst 	Sectors: Media, Gaming, Steel, Transport, Infrastructure, Utilities, Chemicals, Agriculture, Paper & Packaging, Miscellaneous (WES, ANN)	17 years
<b>Michael Malseed</b> Equities Analyst 	Sectors: Telecoms, Retail, Food & Beverage, Mining Services, Contractors (LEI,DOW, TSE, UGL), Agriculture (NUF), Building Materials, Healthcare, Info. Technology (WTF, SEK, IRE), Other (MRM, CAB)	8 years

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