

# Fundamentally Speaking

Newsletter of the Capricorn Diversified Investment Fund (CDIF)

ARSN: 139 774 646

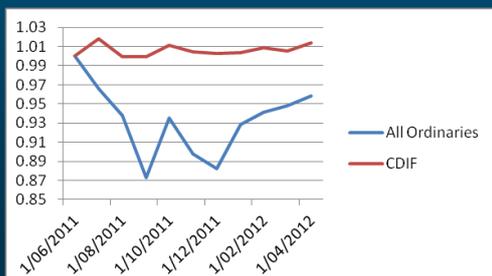
EDITION 2 – June 2012



## COMPARATIVE PERFORMANCE

Capricorn Diversified Investment Fund has recently celebrated twelve months in operation. Since 16 May 2011 the fund has grown as new subscribers contribute and the assets of the fund contribute to earnings. Investors have received their first distribution at an annualized rate of about 4% tax-free. The falling interest rate environment has made such a return attractive, and it is expected to increase significantly as the redevelopment of The Grand Hotel is completed.

The Capricorn Diversified Investment Fund continues to outperform the market. By way



Source: Hubb - ProfitSource

of performance comparison, the closing value of the All Ordinaries index was 4724 on 16th May 2011. As at 29 May 2012, the All Ordinaries stood at 4068, a fall of 13.89%. Comparing the two data points, the fund outperformed the All Ordinaries index by 10.01%. Since our launch date we continue with a conservative investment portfolio comprising investments in Telstra, Max Trust, Wide Bay Building Society Bonds and the redevelopment of The Grand site.

Work on The Grand redevelopment has started and is projected to be finished in January 2013. CIPL is committed to taking about a quarter of the floor area of The Grand and Knight Frank is assisting with further lease arrangements. Once The Grand is complete, tenanted cash flows into the fund are expected to increase significantly, leading to a substantial uplift in distributions. The fund will continue to invest in local development across a range of asset types. The current CDIF assets are shown in the table to the bottom-right.

## WELCOME

Welcome to edition 2 of the Capricorn Diversified Investment Fund's (CDIF) newsletter – Fundamentally Speaking. Fundamentally Speaking will be distributed periodically with other relevant material. In it we look at the characteristics of the fund and highlight the fund manager's future intentions for investment and growth in the fund. Please don't hesitate to contact us if you have any comments or enquiries.

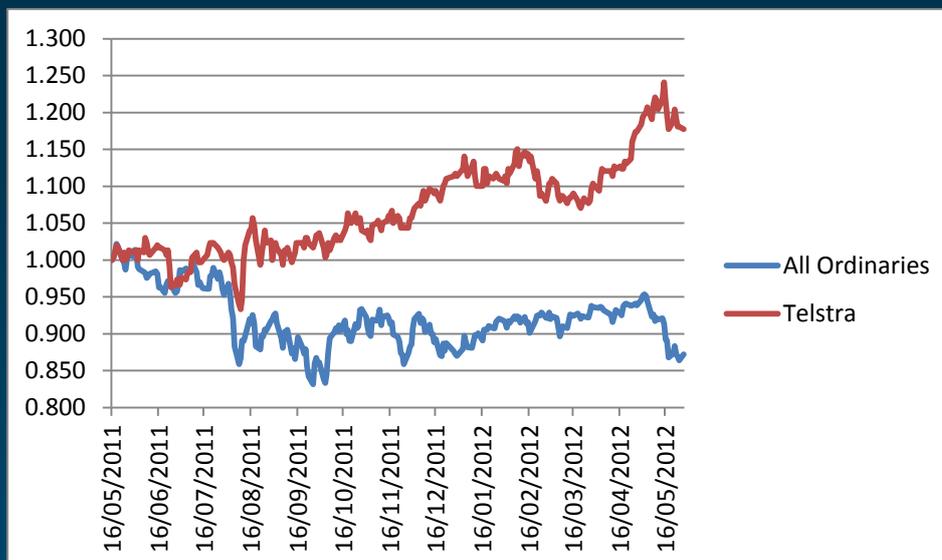
Asset	Amount
Cash	449,800
Listed Investments	\$559,700
Wide Bay Building	\$503,500
Grand Hotel	\$1,890,000
Shares in CIPL	\$390,000

All figures are approximate as at June 2012

## Listed Investments

### Telstra (TLS)

Telstra's share price has benefitted from the twin positives of a falling interest rate environment and the resolution of the NBN agreement with the federal Government.



Source: Hubb - ProfitSource

As well as increasing in value by about 16 per cent, the stock has paid dividends totaling more than \$32,786, a yield of more than 13 per cent calculated on the purchase price. The total return since inception on the investment in Telstra is therefore about 29 per cent. We expect Telstra to continue to perform well as investors seek higher yielding stocks in the falling interest rate environment.

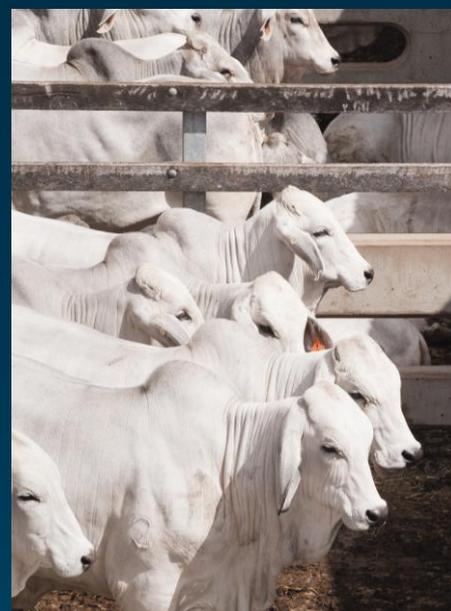
### Max Trust Investments (MXQ)

Max Trust (MXQ) is managed by Threadneedle Asset Management and provides an excellent quarterly breakdown of all assets. It is in wind-up phase with an NTA of 0.377 (trading at \$0.24). Assets held by Max Trust are shown below.

Registered Mortgage Backed Securities	\$51,988,000
Commercial Mortgage Backed Securities	\$24,123,000
Financials and Industries	\$76,791,000
Collateralised Debt Obligations	\$26,750,000
Aircraft	\$33,987,000
Cash	\$11,670,000
<b>Total</b>	<b>\$225,309,000</b>

Recently there has been strong trading in MAX Trust shares, resulting in a return of 17.5 per cent on CDIF's entry price. According to data provided to the ASX, a large investor has been accumulating units in MAX - Alceon GT Pty Ltd, has bought more than 8 million units over a week long period.

The value of Max to unit holders (as opposed to debt holders) is the value of the assets owned by Max, less its debt. Max' net debt levels continue to fall, and stood at around \$80 million at the end of the March quarter. Asset maturities over the next 12 months seem likely to halve that value again. To that end Max' trustees (Trust Company Limited) have commissioned advice regarding the most suitable way to repay the remainder of the debt (which has been vastly reduced over the last two years). It seems that the unit price is responding to an expectation of a positive outcome for unit holders. At around 37 cents per unit, Net Tangible Assets remain well above the traded unit price, suggesting the potential for further gains.



### Distributions report

The units in the fund were issued on 16<sup>th</sup> May 2011, and have now completed the first twelve months in operation. The fund is providing an income return of a little over 4% tax free (after internal fees), which is above many alternate investments. Based on discussions with real estate agents, and indications of interest, The Grand redevelopment is expected to provide a gross yield of about 8.75%. Once on line, this will contribute substantially to the overall income of the fund, and see yields move towards the fund's objective of 8% return plus capital growth.

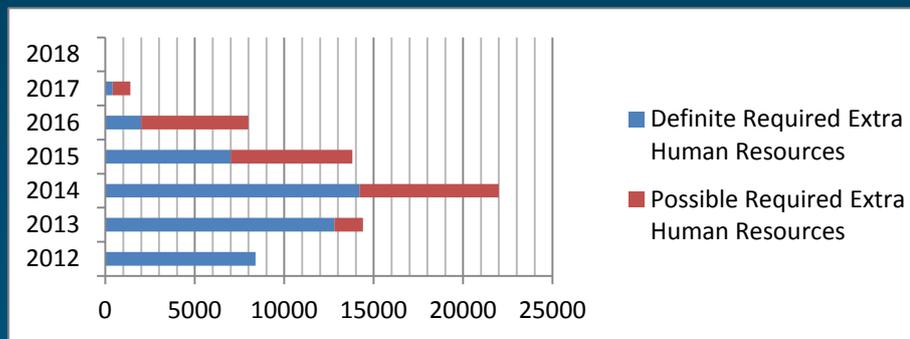
### Valuation Methodology

The valuation of the fund and calculation of Net Asset Value (NAV) is an ongoing process which starts on the 15<sup>th</sup> of each month when the underlying data is provided to Richard Symons, our Chief Financial Officer (CFO). The CFO calculates the unit price which is influenced by Net Asset Value and the number of units on issue. Applications for new units are processed according to the unit price applying to the month in which the application was received. The process is overseen by the CDIF Compliance Committee.

## Outlook for the Central Queensland region

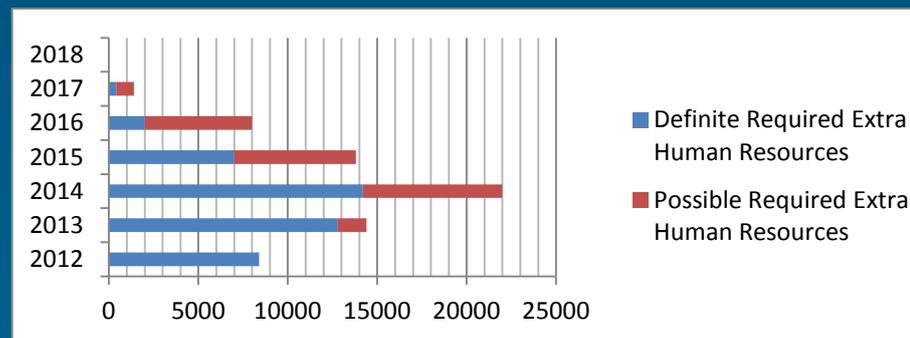
While the focus of the resources boom is on the coal industry, coal seam methane is almost becoming a household word. There has been some bad press around the industry and no doubt there is truth in some of it, but the fact is that the industrial activity centered on Gladstone, Queensland is of mind blowing proportions. The graphs below show the projected employment levels for construction and operational stages, and encompasses both actual and possible projects. What is clear, even at this early stage, is that the massive increase in employment levels is putting enormous pressure on availability of residences and office space. The demand in Gladstone is spilling over into Rockhampton (110km to the North), and as a consequence rental accommodation and commercial office space is becoming tight. There are few new commercial buildings in the town, and those with car parking are sought after. Such an environment is ideal for the redevelopment of The Grand, which we expect to have on-line by early in the new-year. Current lease rates seem to be around \$300 gross, suggesting a gross yield from the redevelopment of about 8.5% when fully tenanted.

## Construction



Source: Tanner Consulting 2012

## Operations



Source: Tanner Consulting 2012



## The Grand Redevelopment

As at the time of writing this The Grand Hotel as we knew it is rubble. However the reconstruction is also well underway. Engineering surveys concluded that restoration of the original façade was not practicable and a new design has now been finalised. The planning report was completed by CQ Consulting Group, and is expected to pass through council with no complications. CDIF has identified a Project Manager – Kevin Murphy – who has also agreed to invest about \$600,000 in the project as well as oversee the completion of the construction over the next seven months or so. Capricorn Investment Partners Ltd has agreed to be an anchor tenant to the development and Knight Frank has been appointed as letting agents. We are hopeful of finding a tenant who will take on the hotel portion of the lease with an eye to supporting the local music scene, as the Cave Bar did for many years.

## Wide Bay Building Society (WBS)

The Wide Bay Building Society bonds continue to contribute an attractive income yield to the fund. They were recently upgraded by one notch by Standard and Poors, and have consistently traded above face value.



## Capricorn Investment Partners Limited (CIPL)

Capricorn Investment Partners Limited is your fund manager. The Capricorn Diversified Investment Fund is being managed locally by specialists in the investment field across portfolio segments. The strength of local specialists is that CIPL understand the regional economy the local investment market and high return opportunities to benefit members. This is the commitment local investors have in our region, and this is the investment culture we are establishing through the Capricorn Diversified Investment Fund.

The fund is focusing on local investment because it can identify high growth assets with a strong investment base.

Capricorn Investment Partners Limited are also recognised as high performing Personal Funds Managers.

Offices in Rockhampton, Sydney and Tamworth service clients throughout the east coast and beyond and over the past year the average portfolio has outperformed the All-Ordinaries index by around 14 per cent. The company has also been successful in winning several bigger ticket jobs including participation in a pre-feasibility study for a commuter rail service between Rockhampton, Gladstone and Bundaberg, an Economic Impact Assessment for the Fitzroy Terminal Project (a coal loader to be located at the mouth of the Fitzroy River) and a feasibility study into the export of woodchip products.

## CDIF makes its first distribution

Earlier in the year Directors of the responsible entity recommended making the first distribution from CDIF. The distribution of 1 cent per unit is tax free and is expected to be made each quarter until the redevelopment of The Grand is complete. The tax free rate of return approximates the expected assessable income for tax purposes within the fund. Because the fund is carrying tax losses from its set-up phase, the actual profit is better retained in the trust until the profit exceeds the accumulated tax losses. By keeping the profits in the trust, an equal value can be distributed as a capital return and pay no tax. Because the value of the profit withheld offsets the value of the distribution, there is no change in Net Asset Value.

Once The Grand is complete, income into the trust is expected to increase markedly and distributions will increase commensurately.

## Who's working on the Grand?

### David French – Capricorn Investment Partners

David French is the Managing Director of Capricorn Investment Partners and a Responsible Manager for CDIF. He has qualifications in Economics and Financial management and is well known and highly regarded in the local community, responsible for growing Capricorn Investment Partners as well as advising many private clients on well management.

### Andrew Brown – CQ Consulting Group

Andrew is a qualified engineer with experience in a wide range of resource industries. He is a Responsible Manager of the CDIF and brings considerable commercial experience in addition to an understanding of the commercial property and investment scene locally.

### Brian Wood – Wood + Day Architects (Sydney)

Wood + Day are specialists providing architectural and project management services for high quality medium sized developments. They will liaise with civil, structural, mechanical and electrical engineers, providing building services to the project.

### Other Ancillary Services

Any significant project also employs a range of local trades and services in the construction and commercial progress of the project. Graham Scott & Associates, Capricorn Surveyors, CQ Consulting, town planning and approvals and JAL Demolition have all contributed to the project to date. As the project progresses, other local businesses will also be involved.

## Other Matters

The establishment of CDIF has opened a number of doors to investment opportunities which are generally not available to the public. CDIF continues to identify and research suitable opportunities as they arise, and is currently investigating an investment into a retirement village at Hervey Bay. Other opportunities being considered include a retirement village in Rockhampton and an investment in a shopping centre in North Rockhampton.

With returns driven by activity in the mining and coal seam gas industries, each opportunity is carefully investigated by the fund under due diligence. While this process plays out, significant funds remain invested in cash. Given this, there seems no reason to change our expectation of a long term income return of 8 per cent plus capital growth on top.



## Capricorn Diversified Investment Fund

ARSN: 139 774 646

Suite 1, Level 2 – 34 East Street  
Suncorp Building

P 07 4920 4600  
F 07 4922 9069

AFSL 237435